



TALENT • HEALTH • RETIREMENT • INVESTMENTS

Investment Strategy Under Solvency II

10 May 2016

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Mercer Insurance Investment Team (MIIT)

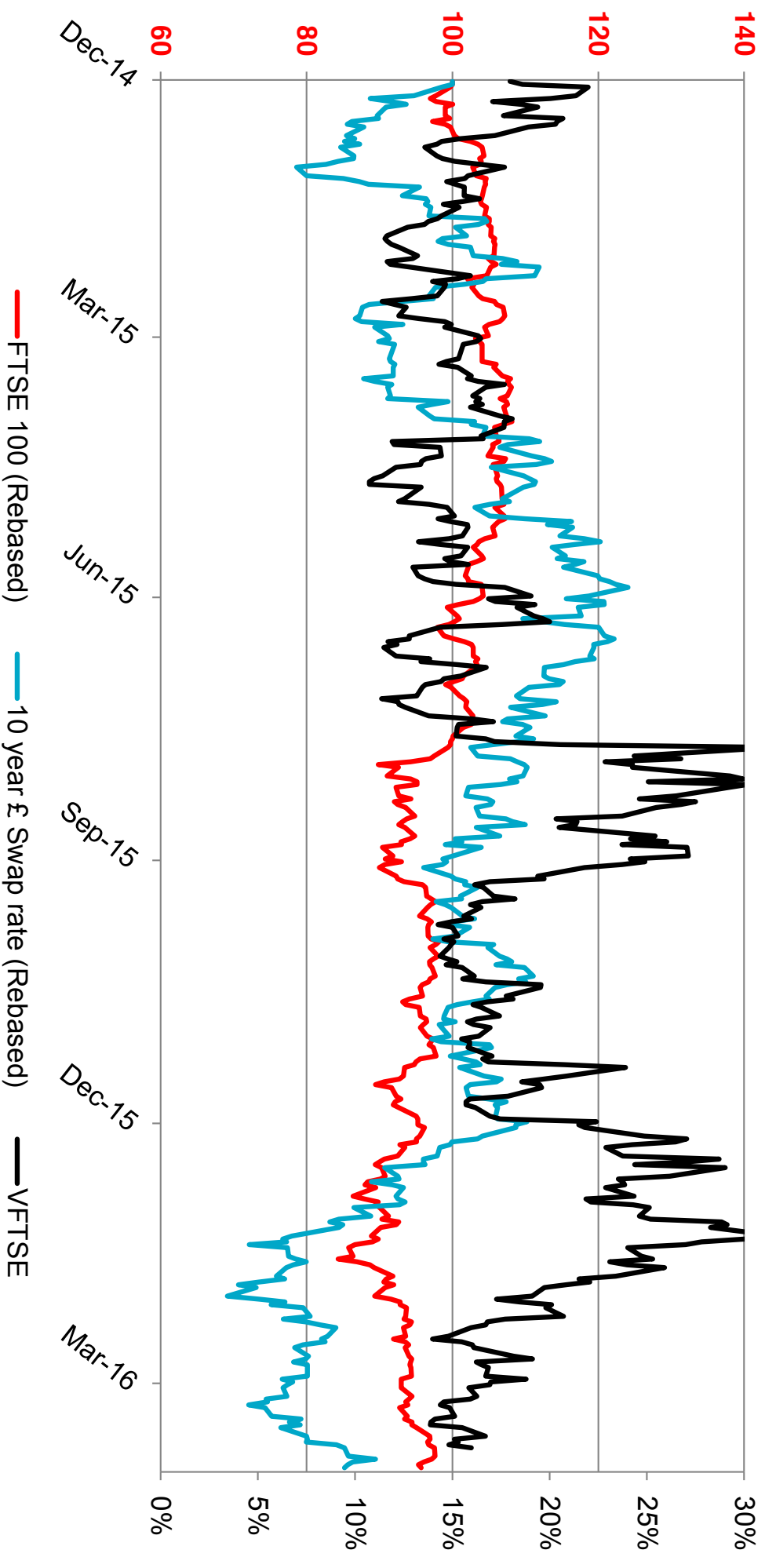
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A. INVESTMENT MARKET UPDATE

- B. Investment strategy under Solvency II
- C. Investment governance under Solvency II
- D. Key actions for insurance NEDs

FINANCIAL MARKET



An Interesting 18 months in the financial market, calming down recently, with long term yield prospect still gloomy.

4 CURRENT HOT TOPICS IMPACTING INSURERS

Solvency II

- ❑ Reconciliation between capital basis and risk appetite
- ❑ Optimisation of investment portfolio
- ❑ Reporting challenges under Pillar 3
- ❑ Compliance, esp. prudent person principle



A. Investment market update

B. INVESTMENT STRATEGY UNDER SOLVENCY II

C. Investment governance under Solvency II

D. Key actions for insurance NEDs

ADOPTING A RISK-OPTIMISED APPROACH

LIABILITY ACCOUNT

SURPLUS

SCR & BUFFER

TECHNICAL PROVISIONS

Design structure to meet wider business objectives

Aligning with the overall (market) risk appetite

Matching the liability profile to reduce capital requirements and risk

Reflect different risk profiles by varying the allocation of the growth assets

ASSET MAPPING

6 ILLIQUID GROWTH

5 SEMI-LIQUID GROWTH

4 LIQUID GROWTH

3 WIDER FIXED INCOME

2 INV. GRADE CORPORATE BONDS

1 CASH & GOVERNMENT

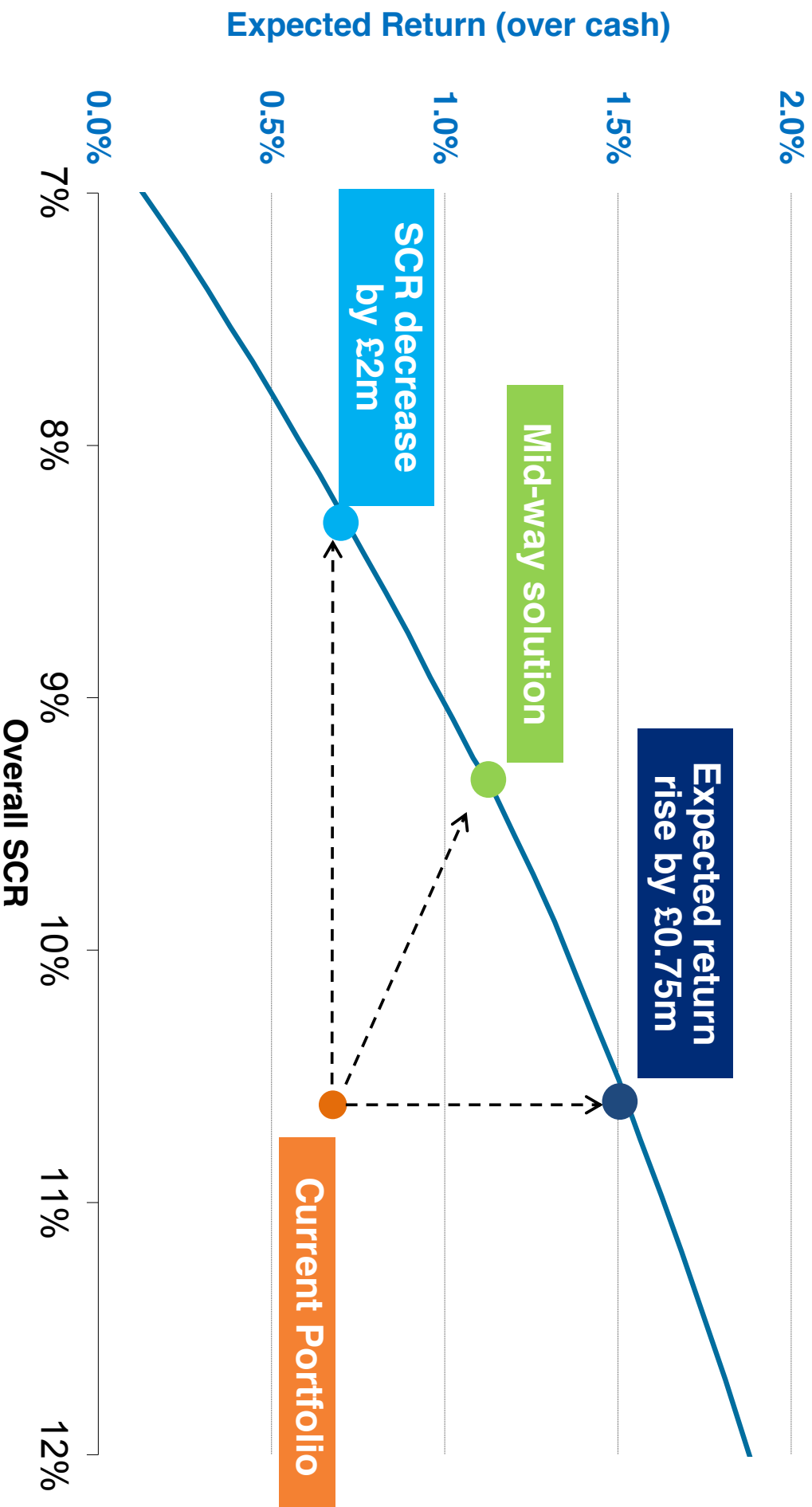
GROWTH ASSETS

HYBRID ASSETS

MATCHING ASSETS

OPTIMISE INVESTMENTS UNDER SOLVENCY II

Illustrative Investment optimisation (per £100m of assets)



CAPTURE FULL POWER OF DIVERSIFICATION

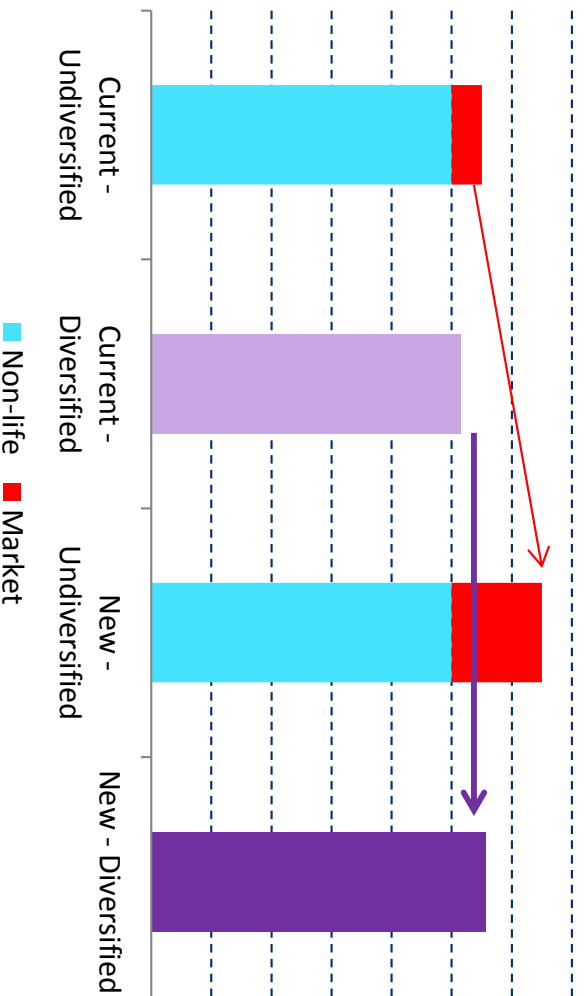
2 examples exploiting diversification effect

1. MARKET VS UNDERWRITING RISKS

- U/w risk SCR can be many times market risk SCR
- A moderate rise in market risk can have little impact on overall SCR due to diversification
- **For a low proportion of market risk...**

...less than half of any increase in the market SCR feeds through to overall SCR

Solvency Capital Requirement

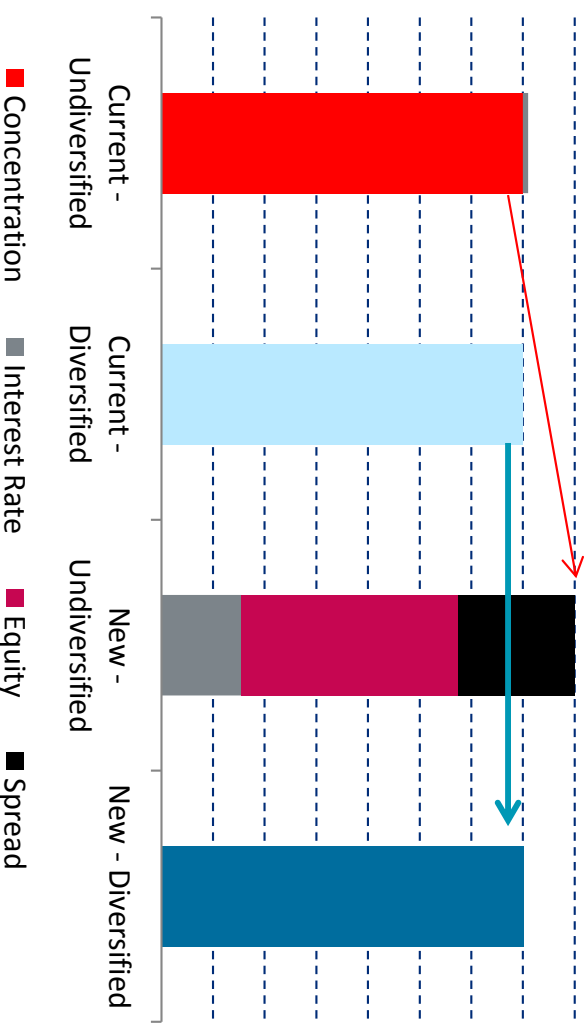


2. CASH CONCENTRATION RISKS

- Cash can attract a surprisingly high SCR charge ...
- ...due to concentration / counterparty risks if limited bank counterparties are used
- **Reducing this materially better capital efficiency....**

...in example below, expected returns are improved by over 2% for same SCR (14%)

Solvency Capital Requirement



- A. Investment market update
- B. Investment strategy under Solvency II

C. INVESTMENT GOVERNANCE UNDER SOLVENCY II

- D. Key actions for insurance NEDs

PRUDENT PERSON PRINCIPLE

A key compliance consideration

Level I Directive - Article 132

... With respect to the whole portfolio of assets, **insurance and reinsurance undertakings shall only invest in assets and instruments whose risks the undertaking concerned can properly identify, measure, monitor, manage, control and report**, and appropriately take into account in the assessment of its overall solvency needs ...

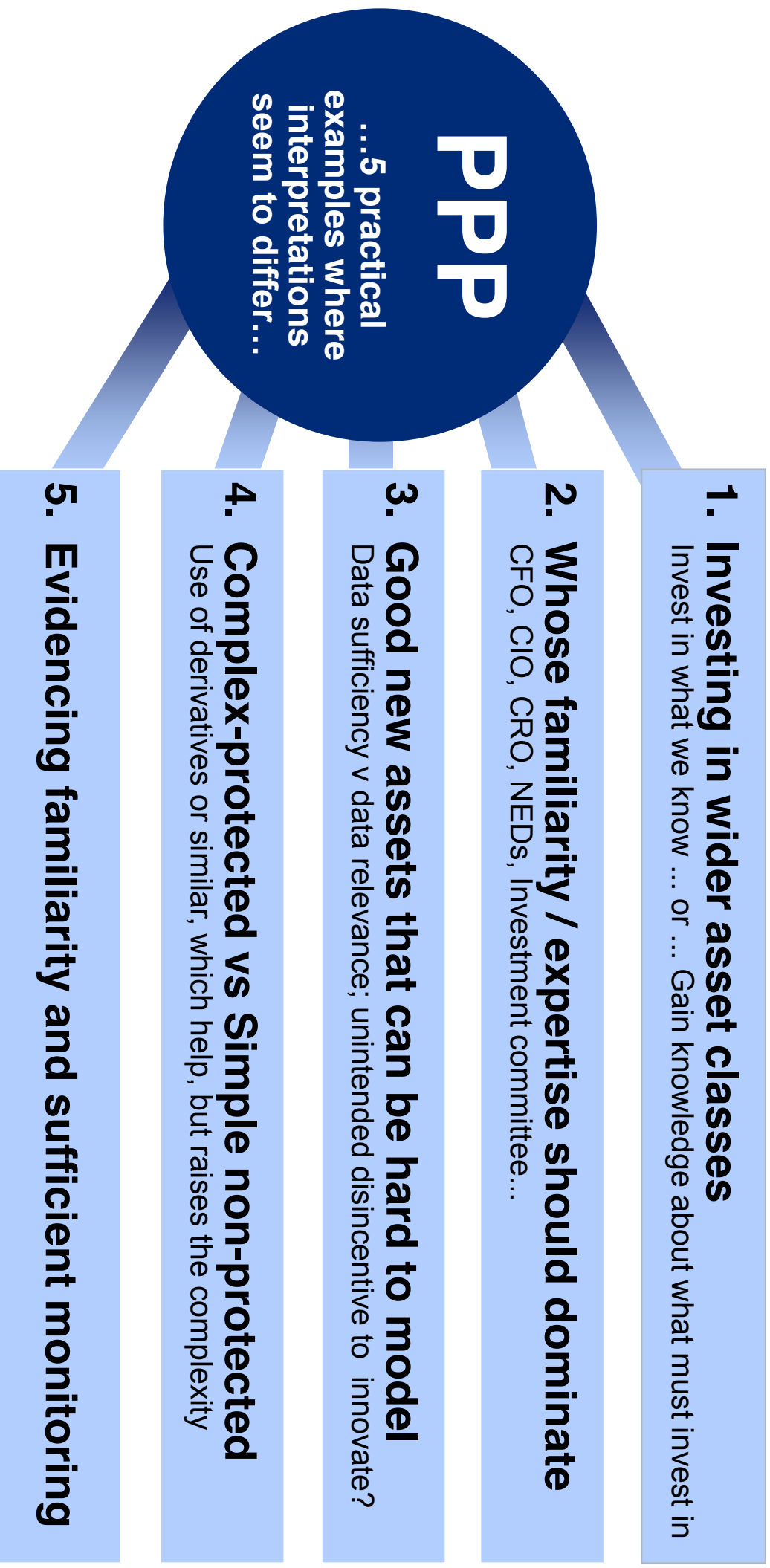
All assets ... shall be invested in such a manner as to **ensure the security, quality, liquidity and profitability of the portfolio as a whole**. In addition the localisation of those assets shall be such as to ensure their availability.

Assets held to cover the technical provisions shall also be **invested in a manner appropriate to the nature and duration of the insurance and reinsurance liabilities**. Those assets shall be **invested in the best interest of all policy holders and beneficiaries taking into account any disclosed policy objective** ...

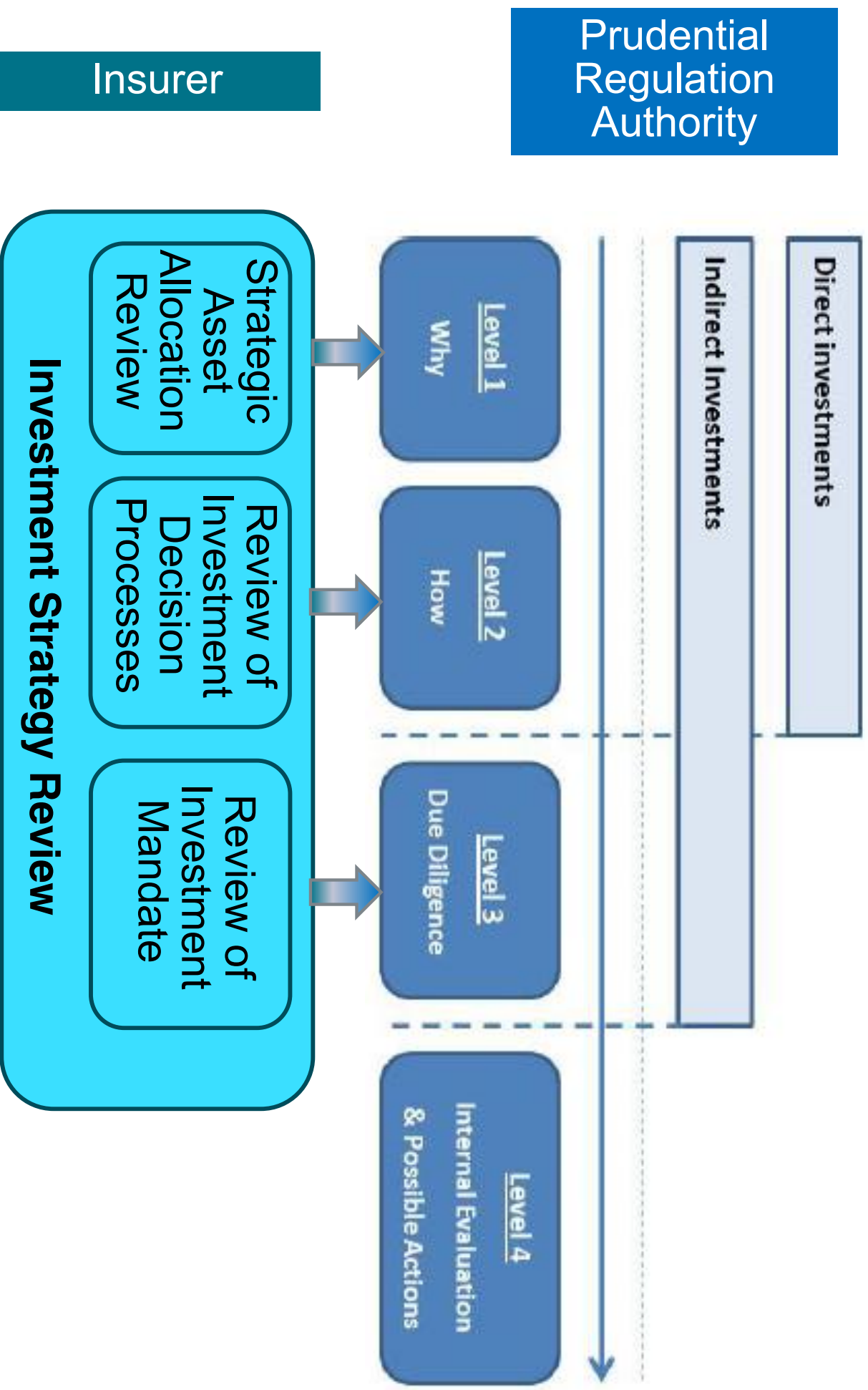


PRACTICAL ISSUES IN INTERPRETING PPP

based on our collective experiences



THE PRA'S INVESTMENT ASSESSMENT MODEL



CRITICAL ROLE OF NEDS



- Invest in line with liabilities
- ... best interest of all policy holders and meet policy objectives
- Ensure the portfolio's security, quality, liquidity and profitability
- Properly identify, measure, monitor, manage, control and report investment risks

1 Retain historic policy / asset universe

2 Expand asset universe & buy governance

A Delegate

B Hire / rely on NEDs

C External support

- A. Investment market update
- B. Investment strategy under Solvency II
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D. KEY ACTIONS FOR INSURANCE NEEDS

KEY ACTIONS FOR INSURANCE NEDS

NEDs have a big role to play during the current solvency regime change. Some important challenges / questions NEDs could raise internally are:

Investment strategy

1. Optimised against Solvency II capital charges?
2. Can return be improved by exploring new asset classes?
3. Are investment managers delivering satisfactory performances?

Decision process

4. Is the process sound and robust?
5. Is there sufficient independent challenge and validation?

APPENDIX

- **GLOSSARY**
- **CONTACT DETAILS**
- **MERCER'S INSURANCE CAPABILITIES**

GLOSSARY

Abbreviation	Description
NED	Non-Executive Directors
S II	Solvency II - European risk-based regulatory framework to be implemented 1/1/16
PPP	Public Private Partnership
AIFMID	The Alternative Investment Fund Managers Directive - a European financial directive
IFRS	International Financial Reporting Standards - internationally accepted accounting 'language' (not accepted by USA)
GAAP	Generally Accepted Accounting Principles (USA) - the standard framework of guidelines for financial accounting
EMIR	European Market Infrastructure Regulation
MiFid II	Markets in Financial Instruments Directive II - technical standards
SCR	Solvency Capital Requirement
ORSA	Own Risk and Solvency Assessment
ALM	Asset Liability Management / Modelling / Matching
M&A	Mergers & Acquisitions

CONTACT DETAILS



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Ravi has over 25 years of financial industry experience spanning several consulting firms and industry roles; insurance and investment disciplines. He specializes in developing governance models for investment decision-making within insurers; driving the ERM discussions across the C-suites; and ensuring that the net of expenses investment outcomes are maximised for insurers. Ravi received an Honours degree in Mathematics and Statistics from the University of Bristol and is a qualified Actuary.



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David joined Mercer's Financial Strategy Group during 2014, bringing his 25 years' experience of proactive institutional business development and client relationship management to the growing insurance consulting team. David holds a BA (Economics & International studies), an MBA (International Finance) as well as an MIM (Master of International Management).



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Niall is a Principal in Mercer's Insurance Investment Team in London. Niall advises insurers on asset liability management, Solvency II, asset allocation and capital & risk optimisation.

Niall is a Fellow of the Institute and Faculty of Actuaries in the UK and qualified in 2004.



PIERS BERTLIN

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Piers is a Principal in Mercer's Insurance Investment Team. Based in London. He advises clients on a broad set of issues including investment strategy, manager selection, asset transfers and performance / manager monitoring.

Piers has over 30 years of experience in the investment business, and has experience both of asset management and investment consulting. He joined Mercer in 2001 following a 17-year career in fund management as an international fund manager.



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Rui is a Senior Associate in Mercer's Insurance Investment Team. He advises insurance clients on asset liability management (ALM), market risk hedging and Solvency II.

He has over 8 years of industry experience and is a Fellow of the Institute and Faculty of Actuaries.

The Insurance Industry

At the heart of MMC

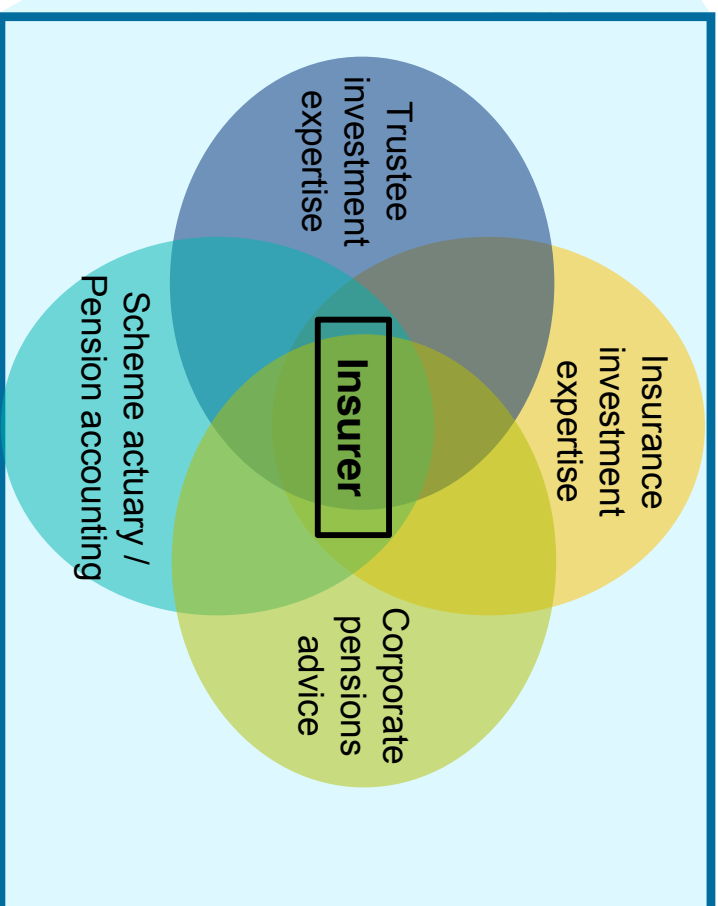


GUY CARPENTER
Risk / Reinsurance Broker
 Capital markets and Actuarial
 ECM and Fiduciary accounts

OLIVER WYMAN
Management Consulting
 Organisational Design, Market
 Entry, Actuarial, M&A

MERCER
Solvency II Consulting
 Investment Strategy & Risk,
 Governance, Research,
 Delegated solutions

MARSH
Insurance Broker
 Risk advisor
 Analytics and Captive insurers



**Globally dedicated to partnering with
 insurance and investment leaders**

**Complementarity, Commonality,
 Collaboration**

Mercer's Global Investment Business

Overview



24

COUNTRIES

1,300

STAFF

60

CITIES



40+

YEARS EXPERIENCE

SOLUTIONS

- Fiduciary management
- Single asset class
- Alternative assets
- Diversified portfolios
- Liability solutions



TOOLS & RESEARCH

- Global manager database
- Performance analytics
- Wealth-management tools
- Investment research



ADVICE

- Investment strategy
- Asset allocation
- Portfolio construction
- Manager selection
- Responsible investment
- Transitions, custody, FX
- Operational risk assessment



820+

Discretionary Clients
\$135+bn under implementation

\$4trn

Subscriber Assets

2,600+

Consulting
Clients
\$9.5trn under advice

As at March 2016

MERCER

How we help our insurance partners

Snapshot of Mercer's insurer services

ENTERPRISE- WIDE VALUE CONSIDERATION

INSURANCE FUND ASSETS RISK MANAGEMENT

RISK ADJUSTED RETURN

IMPLEMENTATION

PENSION SCHEME ASSETS

Target Operating Model	Regulatory review	Strategic Asset Allocation	Mandate design	SCR review
Enterprise Risk Mgmt	ESG validation/calibration	Liability Matching	Manager selection	Std Formula stress
ALM / M&A	Market risk framework	Multi-manager mandate	Operational risk	Select Data aggregator
Governance	Liquidity risk framework	Portfolio construction	Custodian review	ORSA pension risk
Risk dashboard design	Dynamic Risk mgmt	Portfolio Health check	Review of Internal team	S2 reporting approach
Board engagement	Tail risk / stress analysis	Dynamic asset allocation	Fee review / benchmarking	Allow for mgmt actions

SELECTED ADDED-VALUE OUTCOMES

Outperformance of benchmark by +1.1% p.a. over 3 years and +0.9% p.a. over 5 years	Investment strategy validated by external rating agencies and regulator	Improved risk-adjusted return by more than 10% (c.30bps p.a.)	Saved c.10 bps on fees on implementation of a buy and maintain mandate	Reduced SCR from pension assets by more than 50%
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FLEXIBLE & COLLABORATIVE DELIVERY MECHANISMS

Advice & Secondment

Software & Tools

Delegated management

Mercer's Insurance Investment Team



20+
INVESTMENT
PROFESSIONALS



15
COUNTRY
OPERATIONS

25
OFFICES

50+
SUPPORTING
PROFESSIONALS



COMPLIANCE
& GOVERNANCE



RISK
MANAGEMENT



IMPLEMENTATION



INVESTMENT
STRATEGY



CLIENT
RELATIONSHIP
MANAGEMENT



LOOK THROUGH
TIMELY
EFFICIENT
REPORTING
SOLVENCY II FRIENDLY

20
YEAR OPERATING
HISTORY

>\$5bn
CAPITAL DEPLOYED

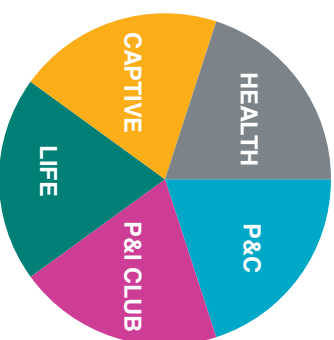


50+
CLIENTS

>6,000
PRIVATE MARKET FUND
OFFERINGS SCREENED

DATA
> 1,300
ACTIVE FUNDS

**125 MANAGER
RESEARCH STAFF**



Mercer has advised diverse insurance clients for more than a decade

A testimony of our strong track record and consistently high service level that we bring to each client assignment every day.

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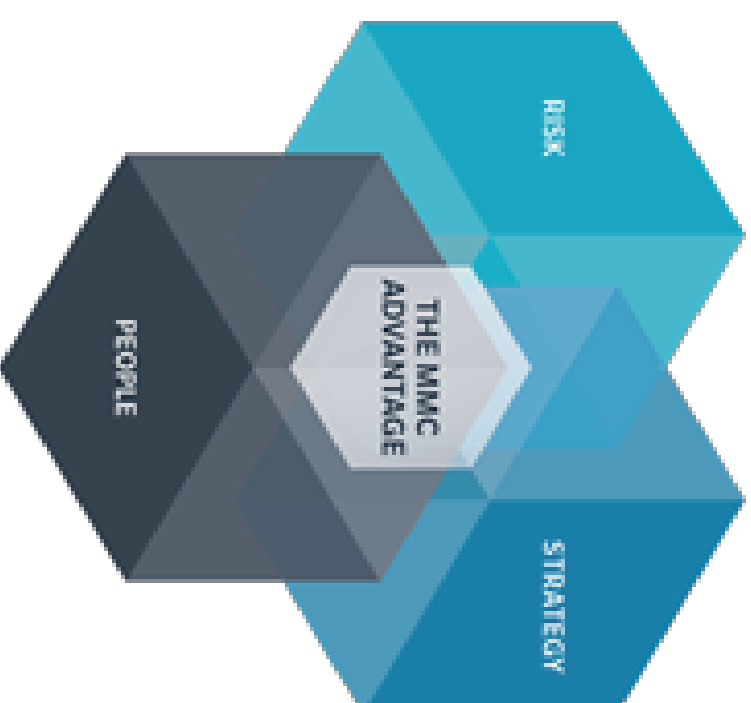
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