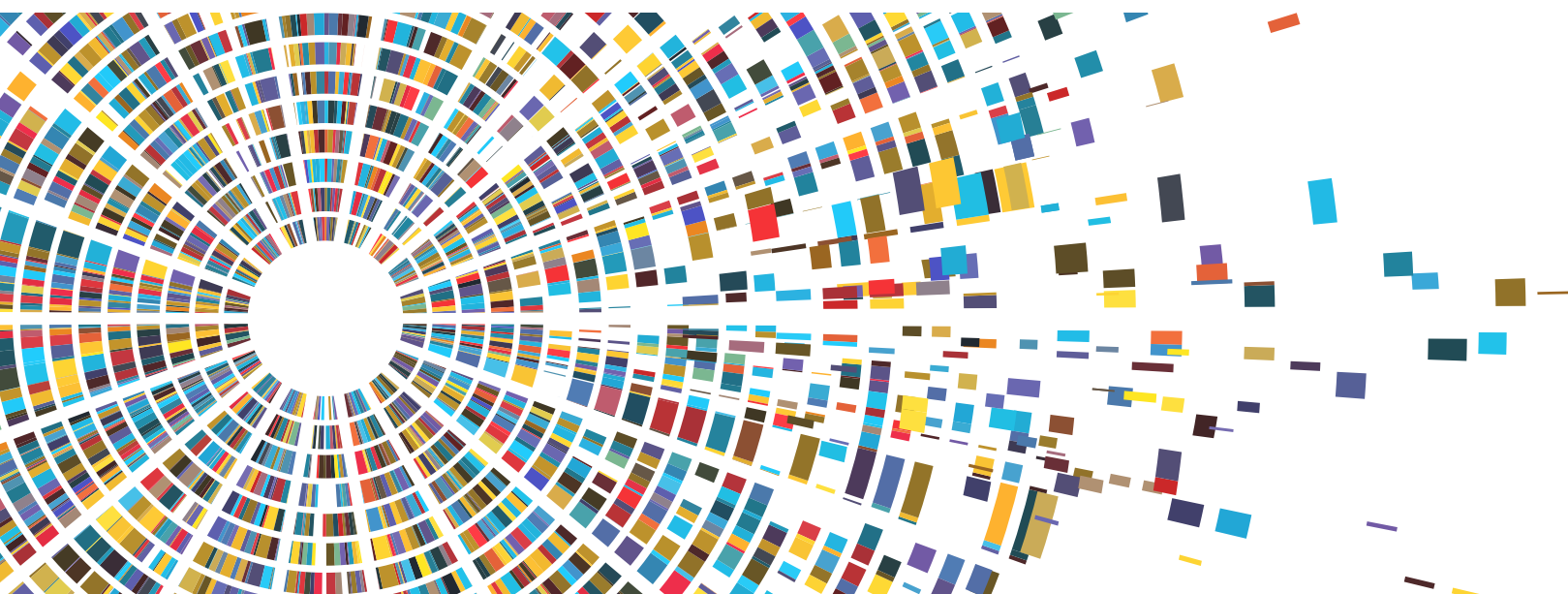




**Asset  
Management**



# GSAM INSURANCE SURVEY 2019

**Cautiously Opportunistic**

April 2019

# INTRODUCTION

Slowing global growth and the reintroduction of market volatility set the backdrop for this year's GSAM Insurance Asset Management Survey, which reveals heightened credit cycle concerns, significant shifts in perceived risks and capped expectations for returns and the investment opportunity set.

US recession is predicted to be a near-term event but not a 2019 event. This year's title, *Cautiously Opportunistic*, underscores insurers' approach to selectively taking risk in light of this view. Flat yield expectations are seen as an opportunity to increase duration in portfolios. While insurers intend to reduce overall equity risk, asset allocation preferences indicate a shift into private equity and away from public equities, which are exposed to more volatility. Modest risk-taking in credit is also planned as spreads are expected to remain range bound this year.

The eighth annual survey released by GSAM Insurance Asset Management incorporates the views of 307 Chief Investment Officers (CIOs) and Chief Financial Officers (CFOs) representing over \$13 trillion in global balance sheet assets, which accounts for around half of the global insurance industry.

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# EXECUTIVE SUMMARY

## KEY TAKEAWAYS

**1 |** Insurers believe we are in the later stages of the credit cycle but do not feel a US recession is imminent.

**2 |** Concerns around rising interest rates that dominated past surveys have vanished as insurance investors are most concerned with credit quality deterioration in their portfolios.

**3 |** With low global yields, insurers continue to express interest in allocating to higher returning, less liquid asset classes like private equity, infrastructure debt and middle market loans.

## FACTS AT A GLANCE

62% expect the 10-year US Treasury yield to remain in the 2.5–3.0% range by year-end, a break from previous results that had an upward bias to rising rates.

27% are concerned about inflation in the next three years in their domestic market, a significant reversal from last year's 74%. Deflation concern is little changed.

62% include Environmental, Social and Governance (ESG) as one of several investment considerations, although the uptake is meaningfully higher in Europe and Asia Pacific.

56% invest in ETFs. Fixed income ETFs are most often used to manage short-term tactical exposures or achieve operational efficiency.

46% invest in insurtech, with Asia Pacific as an outsized contributor at 68%. Improving operational efficiency is the most common draw.

## OVERVIEW

### Respondents from CIOs and CFOs

#### Market Environment

In 2018, sharp bouts of volatility in financial markets in February and the fourth quarter bookended a year that produced generally positive economic data, particularly from the US. The uncertainty created by protectionist policies and nationalist movements across developed economies, including the ongoing US-China trade conflict and Brexit negotiations, exacerbated market movements and weighed on investor confidence.

Central bank policy adjustments in early 2019 have had significant implications for investors with the US Federal Reserve ("Fed") pivoting from steady quarterly rate hikes in 2018 to "on hold" and the European Central Bank (ECB) lowering growth and inflation forecasts while extending stimulus. Investors sharpened their focus on the health of China's economy and its contribution to global growth with the People's Bank of China (PBOC) enacting stimulus of its own. Together, these stabilizing actions supported a notable rally in equity and fixed income markets at the start of this year.

#### Insurance Operating and Regulatory Environment

Low interest rates throughout Asia Pacific and Europe remain a critical challenge for insurers. Following recent central bank policy shifts, global yields have edged lower.

Life insurers continue to adapt to the "lower for longer" yield environment that has challenged guaranteed rate and long-term products. Many have exited non-core businesses or consolidated in an attempt to gain scale.

Strong capital positions and ample liquidity enabled property and casualty (P&C) writers and non-life reinsurers to withstand 2018 catastrophe losses that were driven by another active Atlantic hurricane season and the most destructive California wildfire season on record. After three consecutive years of high catastrophe activity, policy rates are poised to, but have yet to, meaningfully reprice.

M&A continues to be a focal point in the insurance industry as more capital enters from reinsurance vehicles, private equity and alternative asset managers. Large underwriters are also investigating tie-ups and bolt-on acquisitions to expand and diversify. Large and small insurers are increasingly exploring the world of insurtech to improve operational efficiency and gain competitive advantages.

Changes to Risk-Based Capital (RBC) calibration and the accounting treatment of long duration contracts and financial instruments are top of mind industry developments.

## Summary of Survey Respondents

GSAM Insurance Asset Management continued its partnership with KRC Research, an independent research provider, to conduct its eighth annual global insurance investment survey. The survey provides valuable insights from CIOs and CFOs regarding the macroeconomic outlook, return expectations, asset allocation decisions, portfolio construction and industry themes.

We received responses from 251 CIOs and senior investment professionals, 35 CFOs and senior finance managers and 21 individuals who serve as

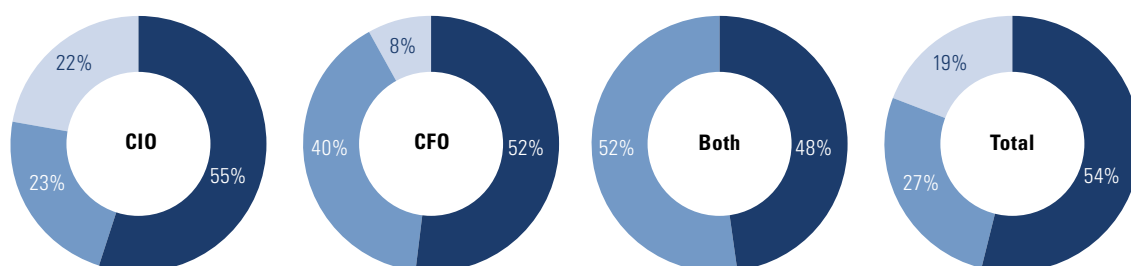
both the CIO and CFO. This year, our survey included insurance companies that invest over \$13 trillion in balance sheet assets, which represents around half of the balance sheet assets for the global insurance sector. The participating companies represent a broad cross section of the industry in terms of size, line of business and geography. The table below summarizes the profile of this year's respondents.

## Participants of the 2019 Insurance Survey

Type	CIO	CFO	Both	Total
<b>P&amp;C / Non-Life</b>	83	18	8	109
<b>Life</b>	109	10	8	127
<b>Multi-Line</b>	30	1	1	32
<b>Health</b>	17	4	3	24
<b>Reinsurance</b>	10	1	0	11
<b>Captive</b>	2	1	1	4
<b>Total</b>	<b>251</b>	<b>35</b>	<b>21</b>	<b>307</b>

Participants (Regional, %)

- Americas
- EMEA
- Asia Pacific

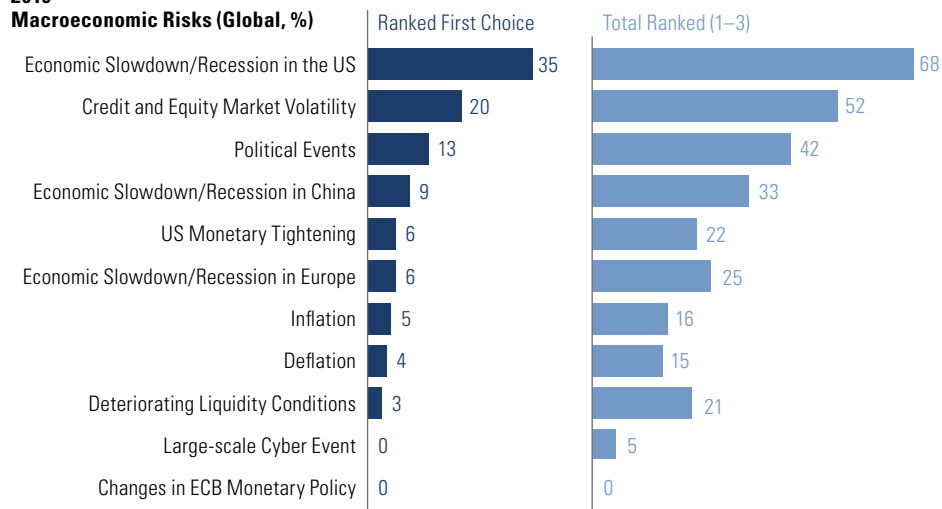


## GLOBAL MACROECONOMIC CLIMATE

Economic slowdown in the US and market volatility are insurance investors' top concerns for 2019.

**Which of the following issues poses the greatest macroeconomic risk to your investment portfolio? Please select and rank your top three.**

### 2019

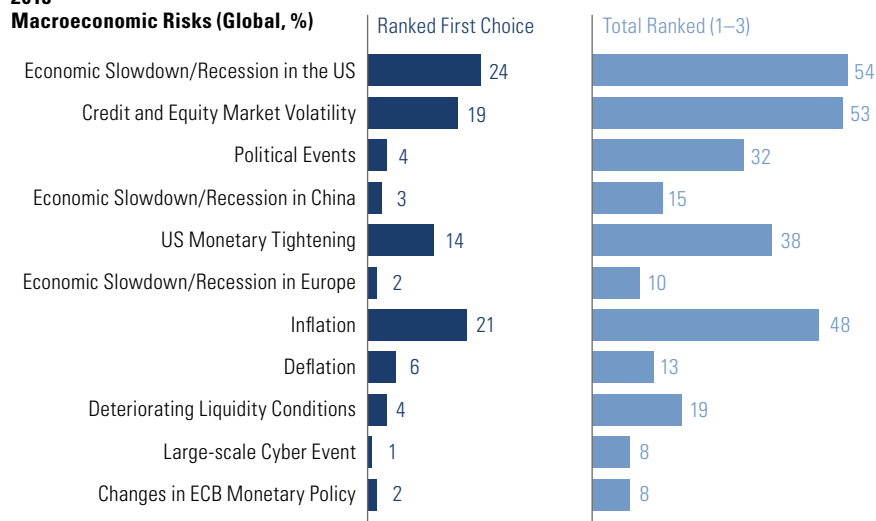


Risks of inflation and US monetary tightening fell materially while concerns around China's economy rose.

Regionally, those surveyed in the Americas and Asia Pacific ranked a US slowdown as the greatest 2019 concern.

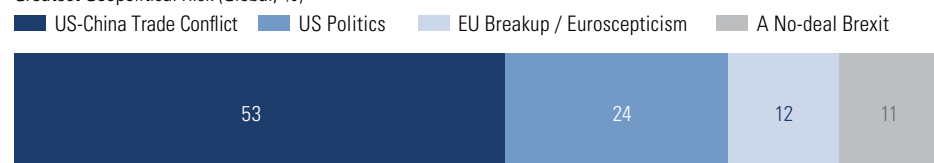
In Europe, the top macroeconomic concern this year was political events, followed by economic slowdown in Europe and the US.

### 2018



**Which of the following poses the greatest geopolitical risk to your investment portfolio over the next 12 months?**

Greatest Geopolitical Risk (Global, %)

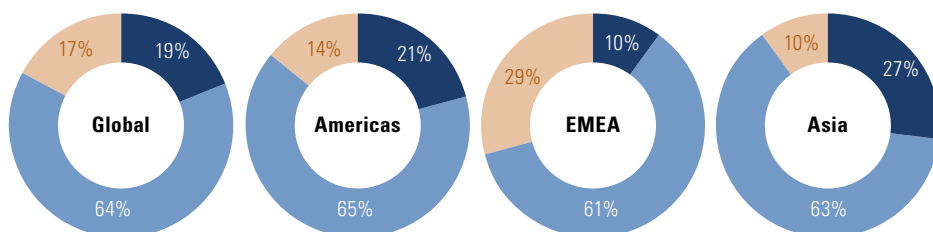


Year-over-year, 10% more respondents ranked political events as a top three macro risk. Regional consensus formed around the US-China trade conflict as the greatest risk to investment portfolios over the next 12 months.

## How significant is the impact of potential future Federal Reserve interest rate hikes on your investment portfolio over the next 12 months?

Level of Significance on Investment Portfolio (Regional, %)

Very Significant Moderately Significant Not Significant

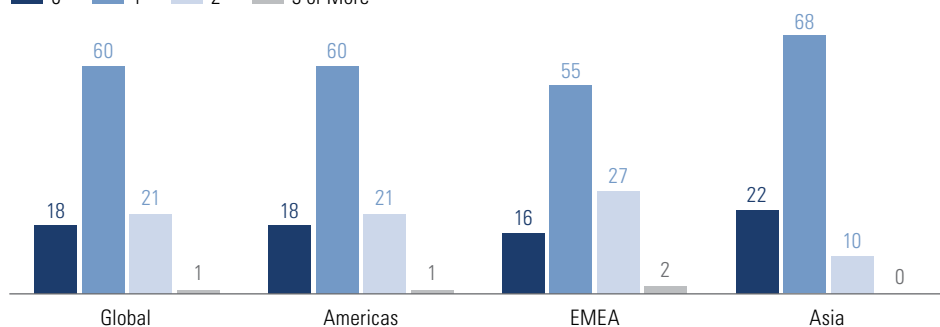


Concerns around monetary tightening have faded.

## How many hikes do you expect from the Federal Reserve in 2019?

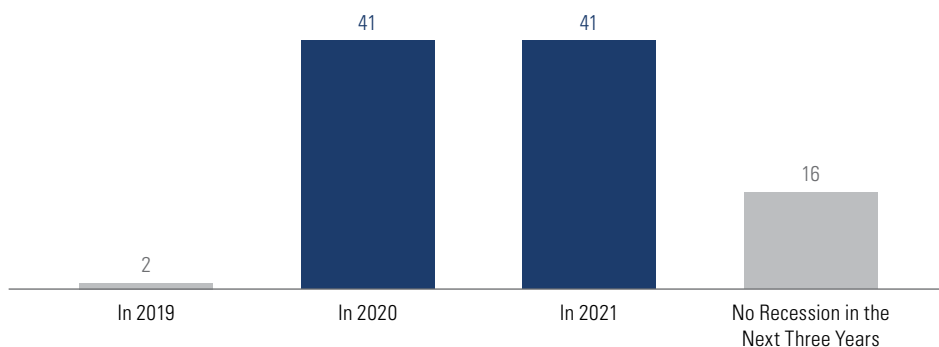
Expected Number of Rate Hikes (Regional, %)

0 1 2 3 or More



## Do you think the US economy will enter a recession in the next three years?

Expectation for US Recession (Global, %)

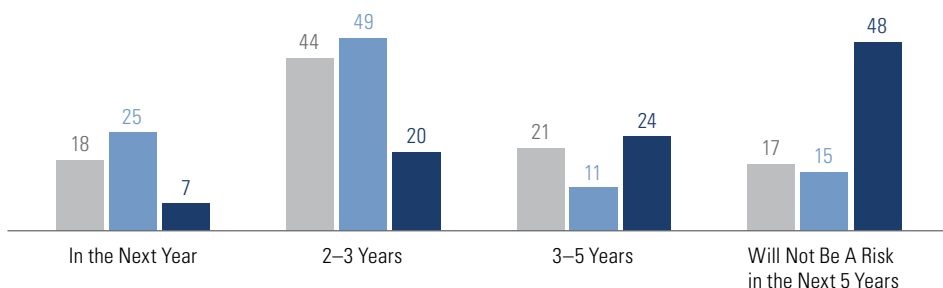


Respondents are divided on a US recession occurring in 2020 or 2021. The disagreement surrounding recession timing is consistent across regions.

## When do you expect inflation to be a concern in your domestic market?

Inflation Expectation (Global, %)

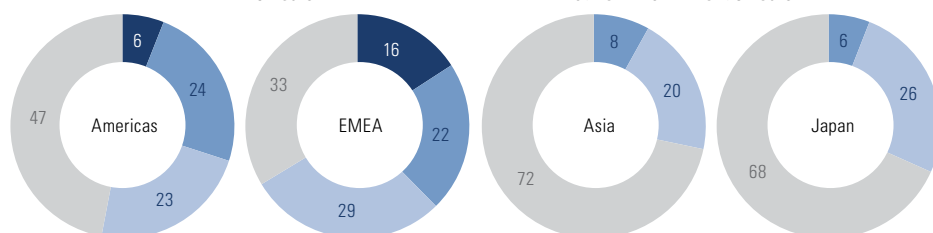
■ 2017 ■ 2018 ■ 2019



Last year, inflation risk was a concern within three years for three-quarters of respondents. This year's results show a significant reversal with only 27% of insurers concerned about inflation in the next three years.

Immediacy of Inflation (Regional, %)

■ In the Next Year ■ 2-3 Years ■ 3-5 Years ■ Will Not Be A Risk in Next 5 Years

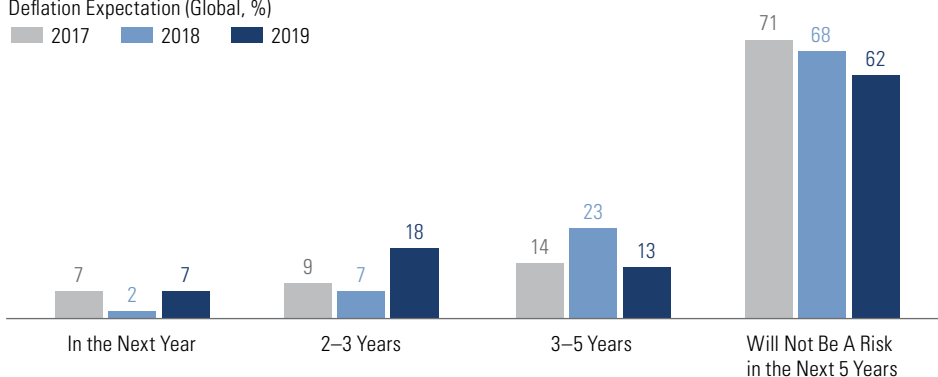


The year-over-year drop in inflation risk is supported by recent economic data showing lower inflation prints in the US and Europe.

## When do you expect deflation to be a concern in your domestic market?

Deflation Expectation (Global, %)

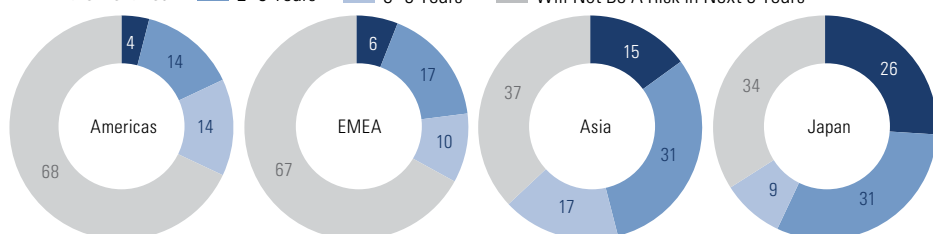
■ 2017 ■ 2018 ■ 2019



While inflation concerns have receded, deflation concerns have not materially risen.

Immediacy of Deflation (Regional, %)

■ In the Next Year ■ 2-3 Years ■ 3-5 Years ■ Will Not Be A Risk in Next 5 Years





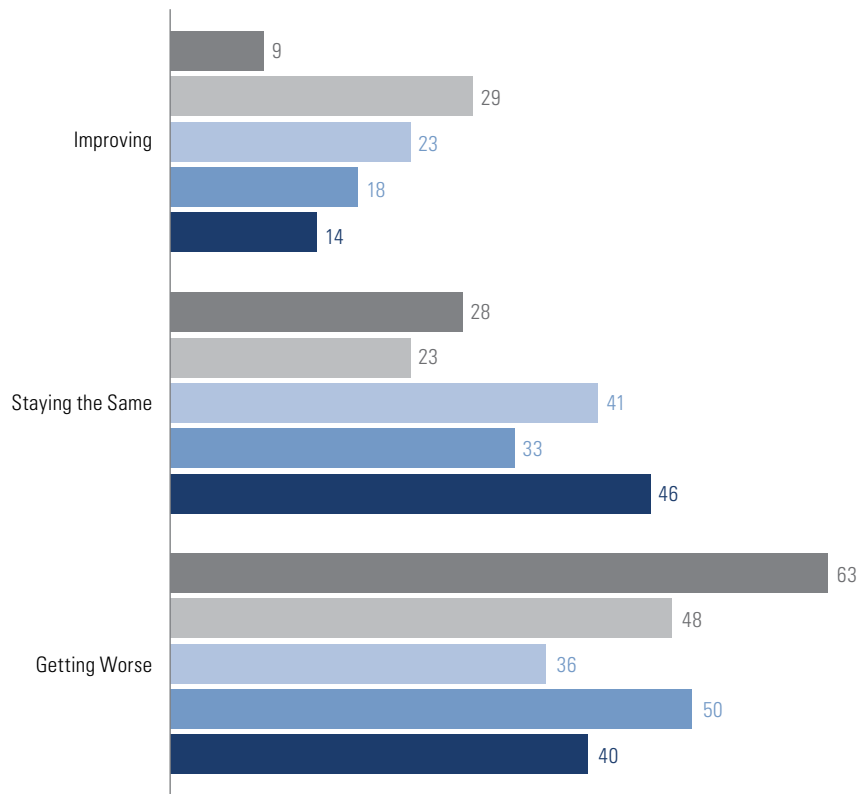
## INVESTMENT OPPORTUNITIES

Insurers are divided on whether the investment opportunity set is stagnant or deteriorating but largely agree that it is not improving.

**Overall, do you feel that investment opportunities are improving, getting worse or staying the same?**

Investment Opportunity Landscape (Global, %)

■ 2015 ■ 2016 ■ 2017 ■ 2018 ■ 2019



This year's results indicate that respondents are the least optimistic they've been since 2015. While they may believe upside is limited, pessimism of 40% is below the five-year average of 47%.

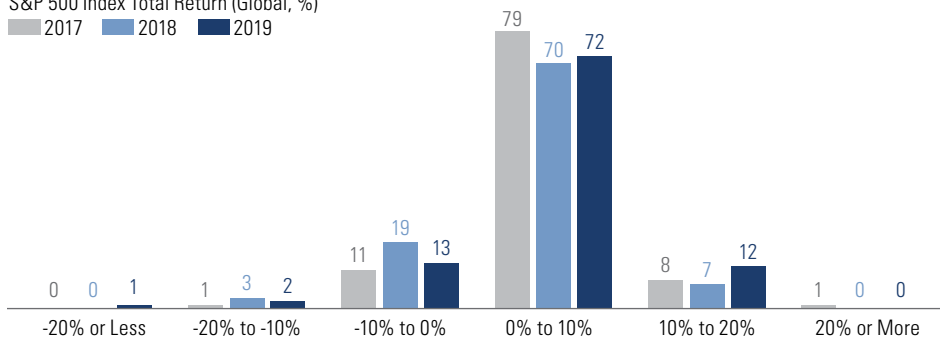
Staying the same is the status quo.

## MARKET OUTLOOK

Lower yields, modest equity returns and late stage credit cycle views form insurers' 2019 market outlook.

### What do you expect the 2019 total return will be for the S&P 500 Index?

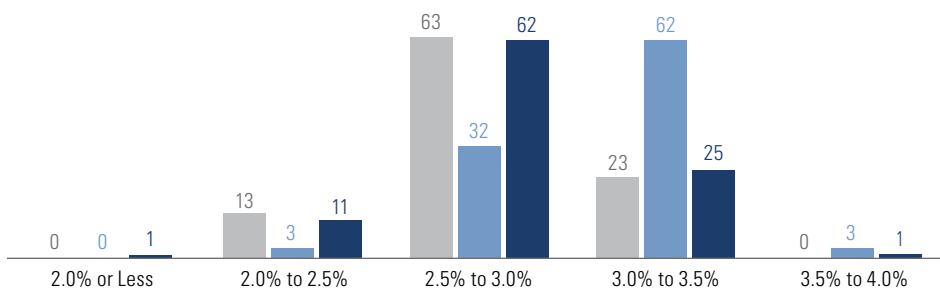
S&P 500 Index Total Return (Global, %)  
 ■ 2017 ■ 2018 ■ 2019



For the third consecutive year, insurers expect modest positive returns for the S&P 500 Index.

### Where do you expect the 10-year US Treasury yield will be at year-end 2019?

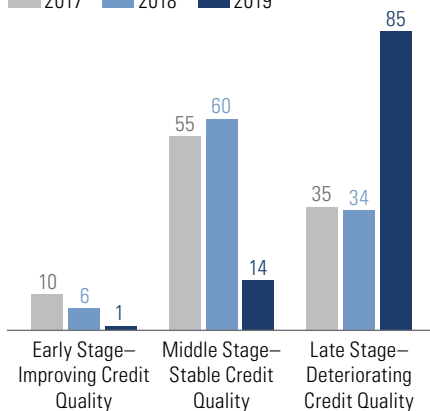
10-Year Treasury Yield (Global, %)  
 ■ 2017 ■ 2018 ■ 2019



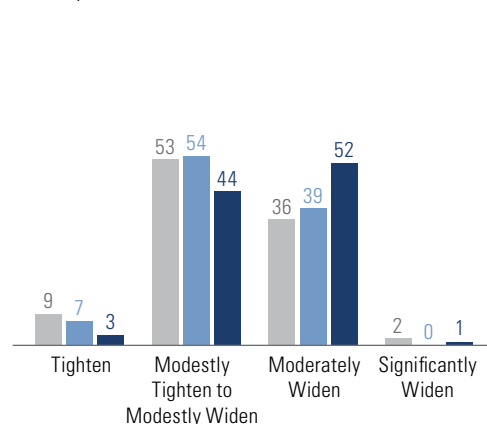
With the potential that we may have seen peak yields during this cycle, the majority of insurers believe the 10-year US Treasury will yield between 2.5% and 3.0% at year-end 2019, demonstrating a retracing to 2017 predictions.

### Where do you think we are in the credit cycle? What do you think will happen to credit spreads in 2019?

Credit Cycle Stage (Global, %)  
 ■ 2017 ■ 2018 ■ 2019



Credit Spreads (Global, %)



In a marked change from the past two years, 85% of insurance investors now believe we are in the late stage of the credit cycle. Spread expectations have shifted towards moderately widen.

## Do you believe liquidity conditions are deteriorating?

Deterioration of Liquidity Conditions (Global, %)

■ Yes ■ No

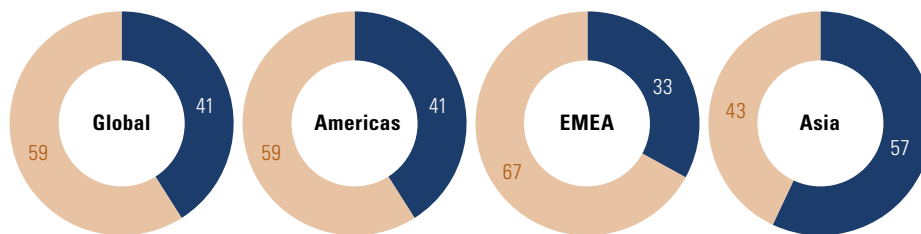


54% of respondents believe that liquidity conditions are deteriorating.

## If yes, do you think deteriorating liquidity conditions will have a significant impact on your investment portfolio?

Impact on Portfolio (Regional, %)

■ Will Have Impact ■ Will Not Have Impact



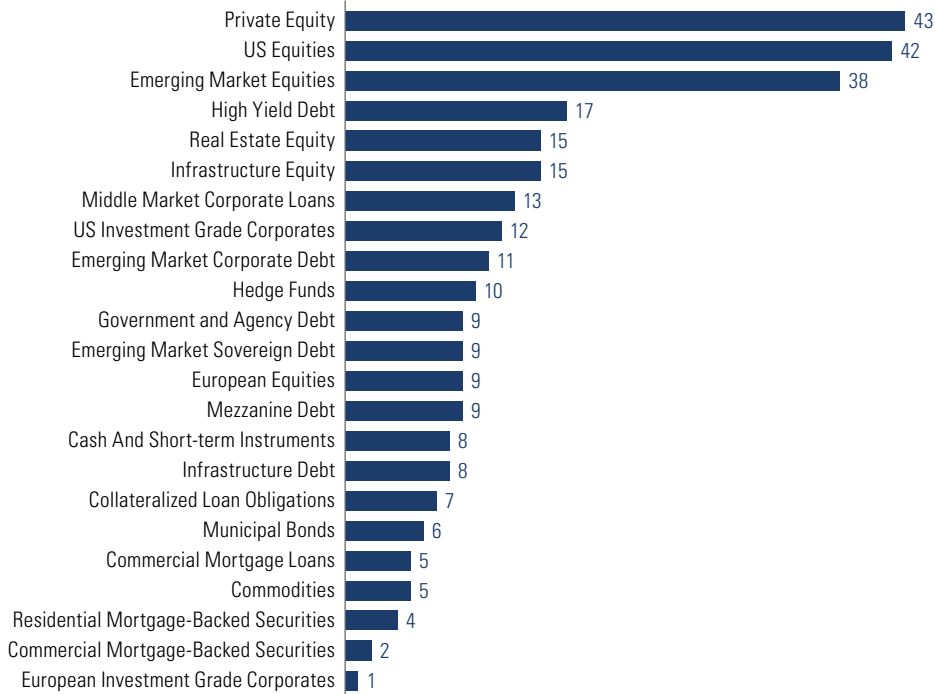
Of those who believe liquidity conditions are deteriorating, most believe the impact on their portfolio will be limited. Asia Pacific is a regional outlier.

## RETURN EXPECTATIONS

Insurance investors continue to expect equities and private assets to broadly outperform public credit.

**Please rank the three asset classes that you expect to deliver highest/lowest total returns in the next 12 months.**

### Highest Ranked Asset Classes (Global, %)



Similar to last year and by a wide margin, insurers expect equities to be the top performing asset class. Private equity, US equities and emerging market equities maintained top rankings.

### Lowest Ranked Asset Classes (Global, %)

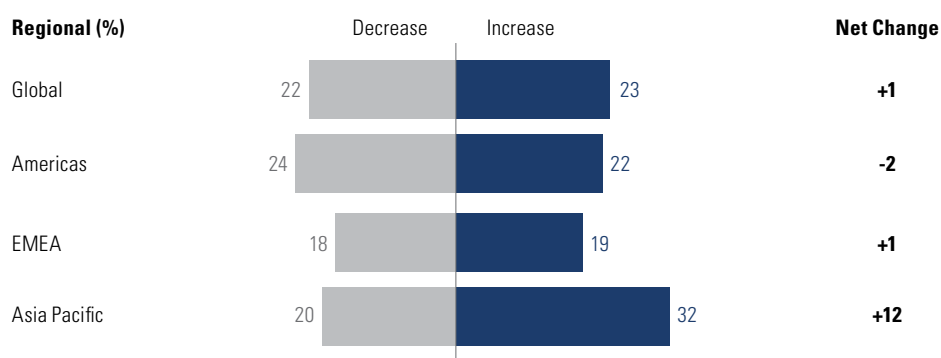


High yield debt represents the greatest disagreement among respondents with 24% expecting the asset class to be one of the lowest returning and 17% predicting it as one of the highest returning.

## PORTFOLIO CONSTRUCTION

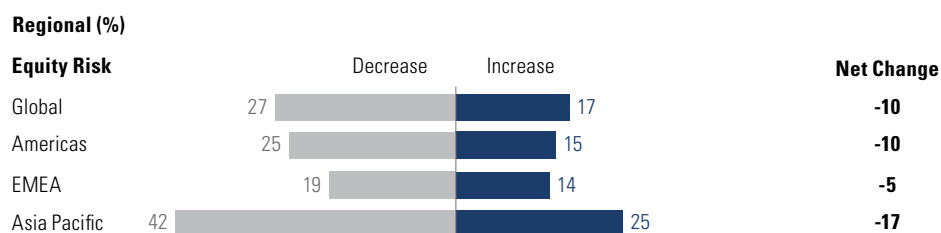
Plans for risk-taking in 2019 vary widely across regions, while credit quality deterioration is perceived as the top portfolio risk.

### Are you planning to increase, decrease or maintain the overall risk in your investment portfolio in the next 12 months?



From a global perspective, risk appetite was little changed year-over-year and remains well below the survey's historical average of +15%. While appetite may appear risk neutral from a global lens, a regional disparity exists with Asia Pacific insurers planning to increase overall risk substantially more than their American and European counterparts.

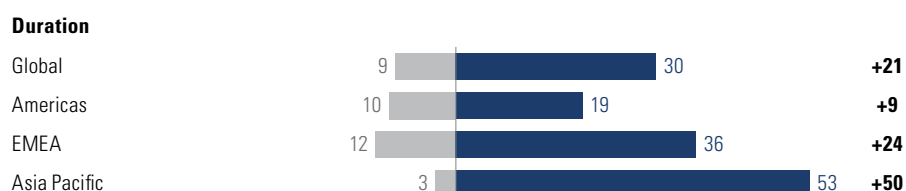
### Are you planning to increase, decrease or maintain the equity risk, credit risk, liquidity and duration in your investment portfolio in the next 12 months?



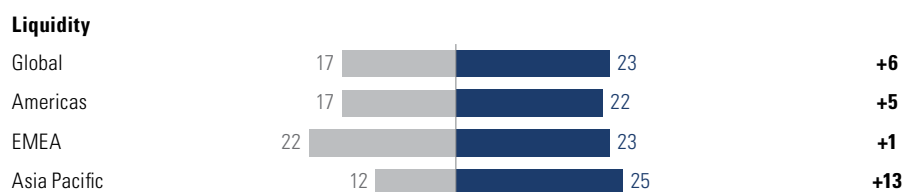
Insurers continue to de-risk from an equity perspective.



Regional differences in credit risk plans are indicative of the limited returns in government securities.



With dovish central bank stance putting rate hikes on the backburner for 2019, insurance companies globally plan to increase duration in their portfolios.

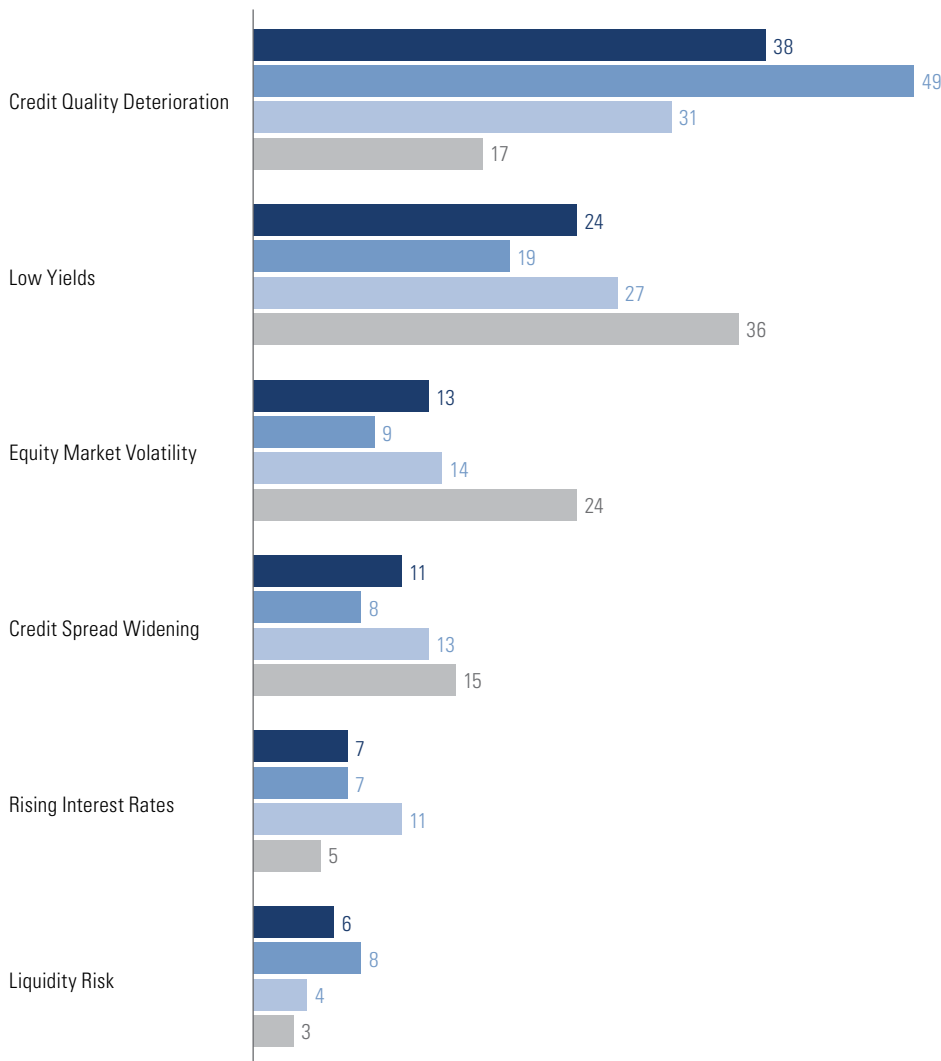


Experiences with increased volatility in 2018, particularly in the fourth quarter, likely contributed to insurers' plans to increase portfolio liquidity this year.

### Please select the investment risk that you are most concerned about.

Concerning Investment Risks (Regional, %)

Global Americas EMEA Asia



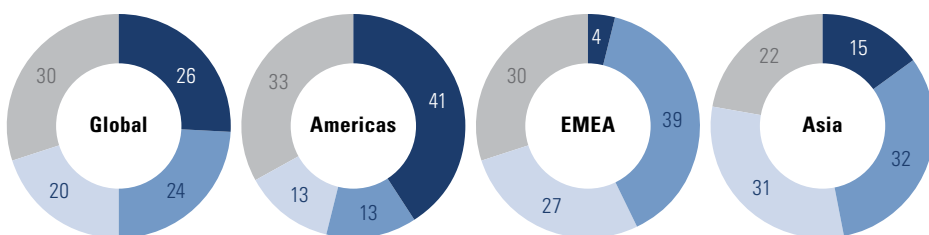
In a pronounced reversal from last year when rising interest rates were cited as the greatest risk to insurers' investment portfolios at 30%, concern around rising rates was among the least prevalent in 2019.

Taking its place, survey respondents expressed concern over credit quality deterioration. This risk is particularly notable in the Americas.

### What developing regulatory/accounting requirements do you expect to have the most significant impact on your investment strategy?

Regulatory/Accounting Requirements (Regional, %)

RBC Recalibration IFRS 17/US GAAP Long Duration Contracts  
IFRS 9/US GAAP Financial Instruments Not Applicable

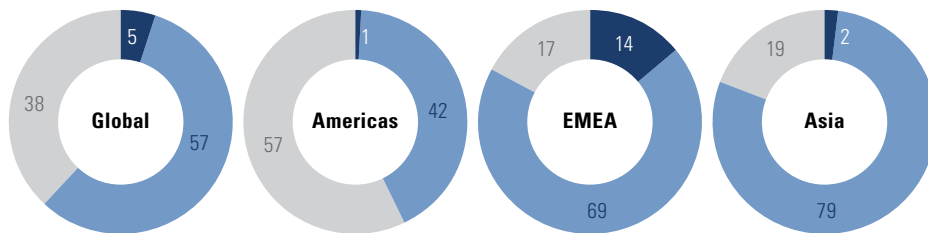


The dispersion of these results is representative of the unique challenges faced by insurers operating in different markets amid evolving regulatory and accounting regimes.

## To what extent is Environmental, Social and Governance (ESG) and/or impact investing an investment consideration?

ESG and/or Impact Investing Considerations (Regional, %)

■ A Primary Consideration ■ One of Several Considerations ■ Not a Consideration

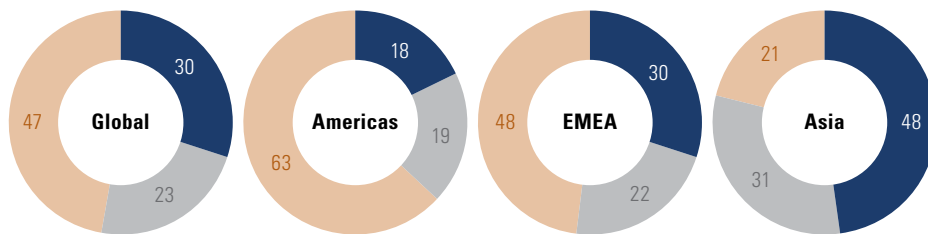


Consistent with previous years, ESG is more often an investment consideration in Europe and Asia Pacific than in the Americas.

## Do you apply the following ESG considerations in your investment portfolio?

Dedicated ESG Investments (Regional, %)

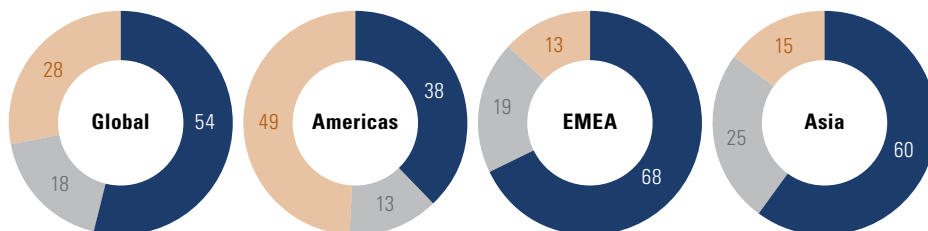
■ Yes ■ No, but Intend to ■ No



Of those insurers who consider ESG in the investment process, dedicated investment sleeves are most utilized in Asia Pacific, while negative screening and avoidance tools have been adopted across regions, led by Europe.

Negative Screening and Avoidance Tools (Regional, %)

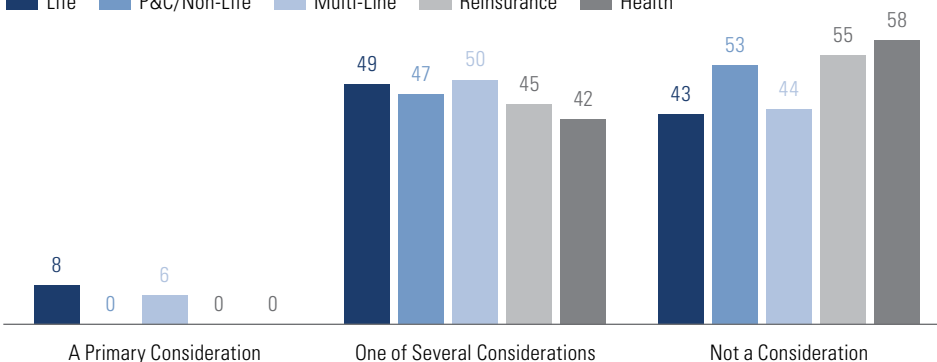
■ Yes ■ No, but Intend to ■ No



## To what extent is climate risk a consideration in your investment process?

Climate Risk Considerations (Type, %)

■ Life ■ P&C/Non-Life ■ Multi-Line ■ Reinsurance ■ Health

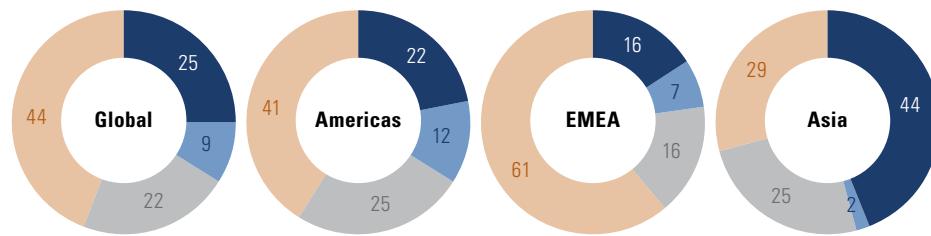


Few global respondents deem climate risk a primary consideration. P&C, Reinsurance and Health companies, perhaps most exposed to climate risk in underwriting, least consider it in the investment process.

## Do you use ETFs?

Type of ETFs (Regional, %)

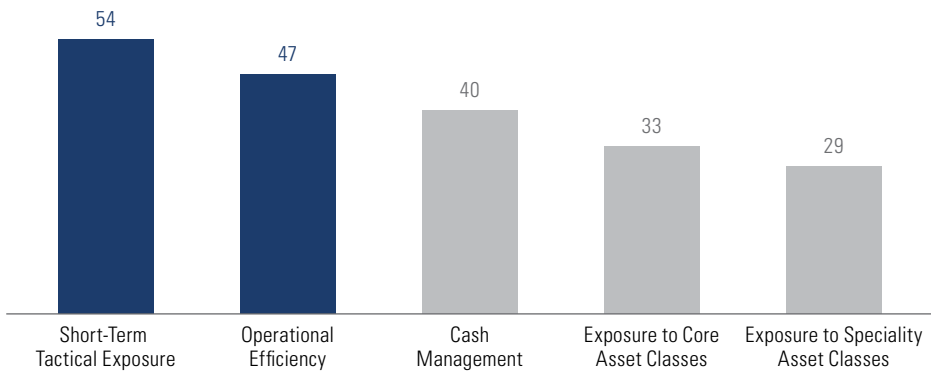
Equity Fixed Income Both Do Not Use ETFs



Most insurers use ETFs as a portion of their equity and/or fixed income allocations. This is particularly true in Asia Pacific, where 71% of respondents reported ETF use.

## What role do fixed income ETFs play in your investment process?

Role of Fixed Income ETFs (Global, %)



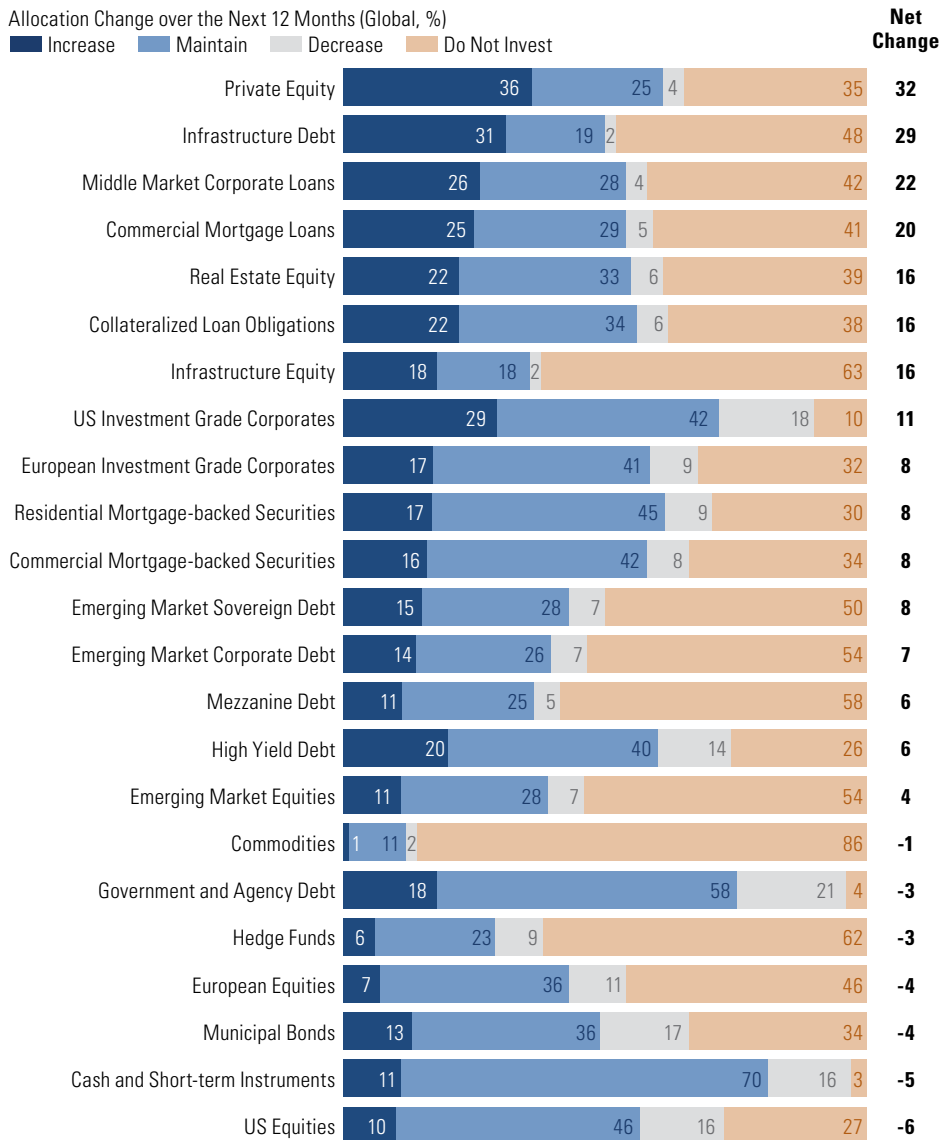
For those insurers who invest in fixed income ETFs, they most commonly use the allocations for short-term tactical exposure and/or operational efficiency.



## ALLOCATION PREFERENCES

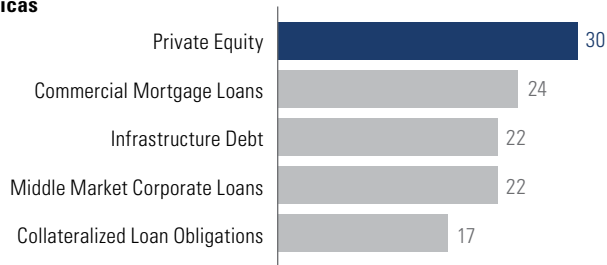
Insurers continue to express interest in allocating to higher returning, less liquid asset classes like private equity, infrastructure debt and middle market loans.

### Are you planning to increase, decrease or maintain your allocation to the following asset classes in the next 12 months?

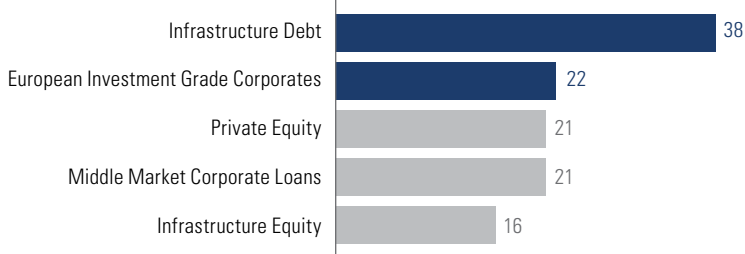


For the fourth consecutive year, insurers plan to increase their allocation to US investment grade corporates. They also plan to add to high yield debt after seeking to reduce allocations in 2018. Respondents intend to decrease holdings of US equities and municipal bonds. European equities have also fallen out of favor, and hedge fund investments continue to be deprioritized by insurance investors.

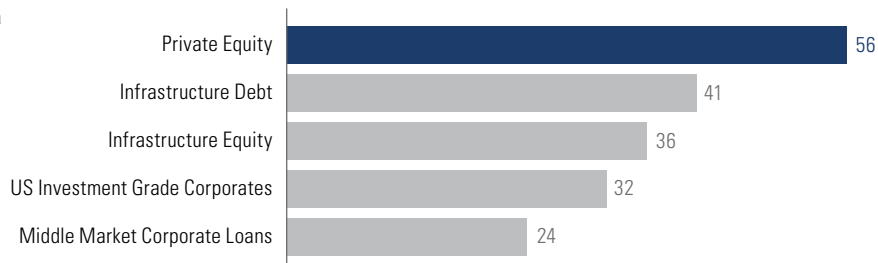
## Allocation Change over the Next 12 Months (Regional, %)

**Americas**

There remains a strong interest in equities and broadly defined private credit on a global level. In the Americas, private equity remained the top allocation change, perhaps a reflection of the available market opportunity.

**EMEA**

European insurers identified domestic investment grade corporates and infrastructure equity as new top five priorities in 2019, effectively replacing commercial mortgage loans and European equities from the 2018 survey.

**Asia**

Asia Pacific insurers' plans to allocate to private equity increased from 46% in 2018 to 56% in 2019.

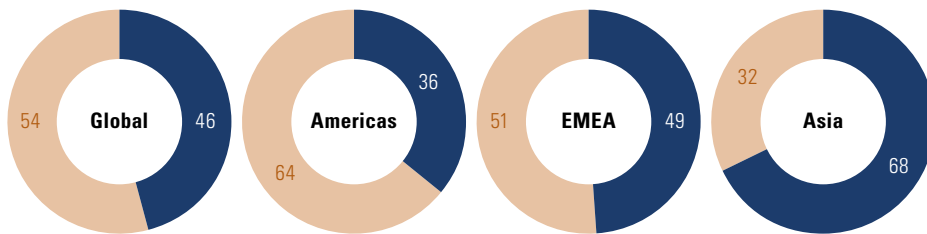
## INDUSTRY THEMES

Insurers are exploring emerging technologies that have implications for the investment portfolio and company operations.

### Do you invest in insurtech?

Investment in Insurtech (Regional, %)

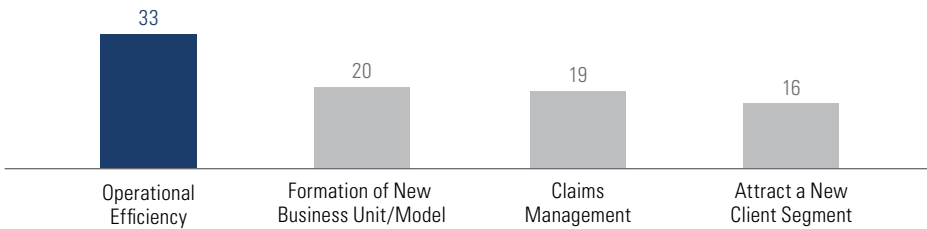
Invest in Insurtech Do Not Invest in Insurtech



For a new look into industry disruption, the 2019 survey inquired about insurtech. Around half of survey respondents invest in insurtech, with Asia Pacific as an outsized contributor.

### If yes, which of the following factors do you most strongly consider when evaluating investments in insurtech?

Insurtech Investment Considerations (Global, %)

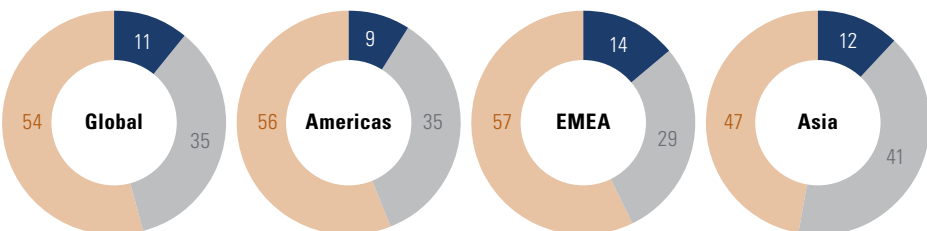


For those insurers who pursue insurtech investments, operational efficiency is the most common motivation among several cited.

### Do big data/artificial intelligence-driven (AI) investment strategies have a role in your investment portfolio?

Investment in Big Data/Artificial Intelligence-Driven Strategies (Regional, %)

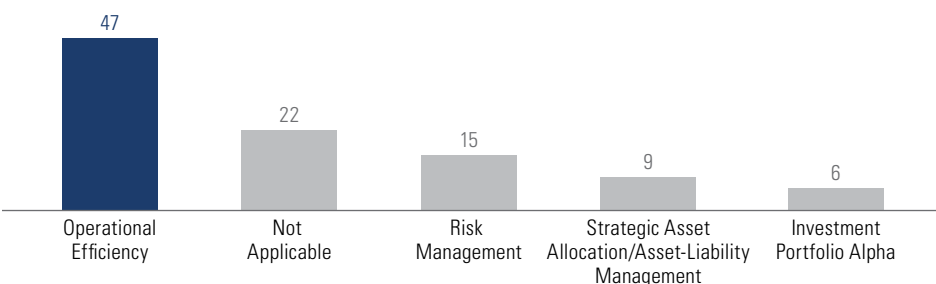
Yes No, but considering implementing No, they do not have a role



Roughly half of insurers feel that big data and AI investment strategies have a potential role in the portfolio.

### What aspect of big data/AI has the greatest potential to improve your company?

Role of Big Data/Artificial Intelligence (Global, %)



Similar to the motivation behind the pursuit of insurtech investments, participants indicated that big data and AI have the greatest potential to improve operational efficiency.

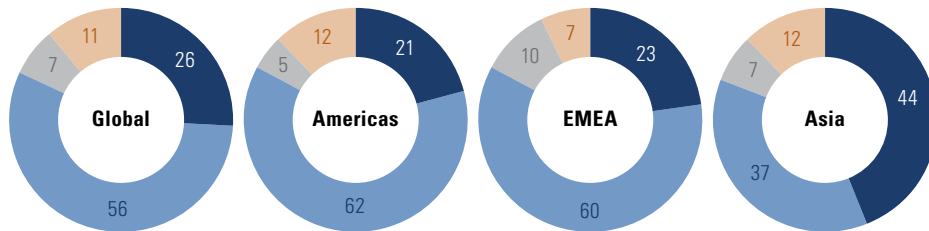
## OUTSOURCING

Respondents plan to outsource around the same amount in 2019. Asia Pacific insurers plan the largest increase in outsourcing.

### Do you anticipate outsourcing more, the same amount or less of your investment portfolio in the next 12 months?

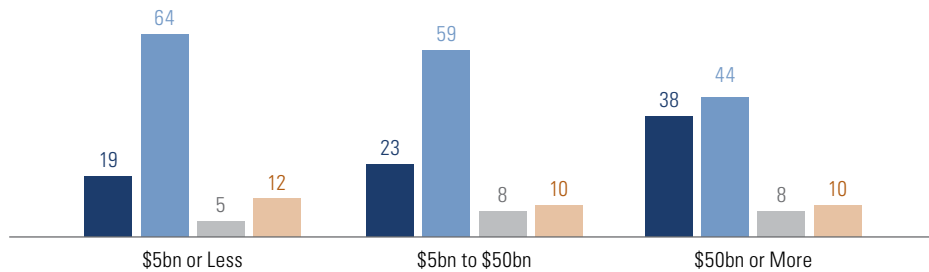
Expected Change in Outsourcing (Regional, %)

More Same Amount Less Do Not Outsource



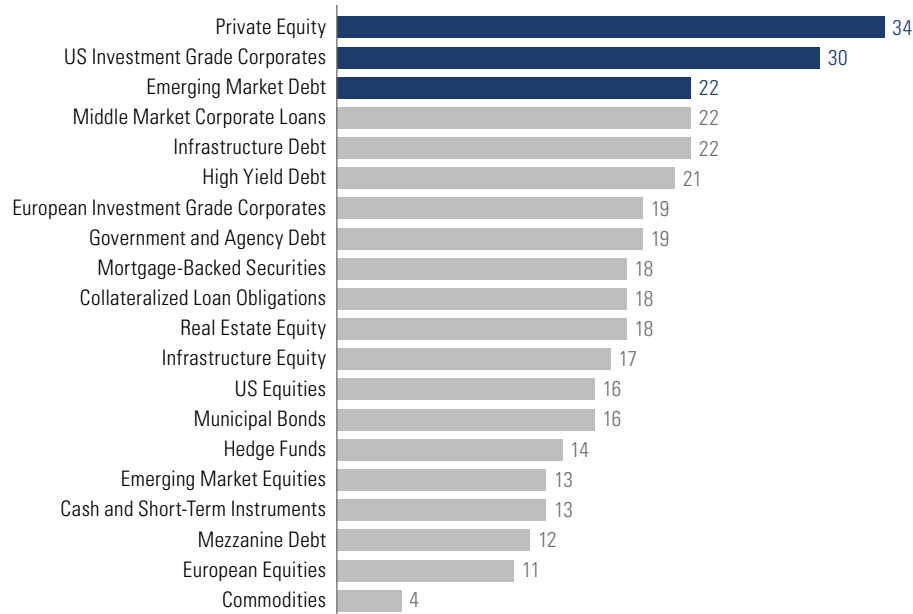
Expected Change in Outsourcing (Size, %)

More Same Amount Less Do Not Outsource



### Which of the following asset classes are you considering outsourcing to a third-party asset manager in the next 12 months?

Asset Classes Expected to Be Outsourced (Global, %)



Insurers are most often considering third-party managers for the management of private equity, US investment grade corporates and opportunistic credit. In Asia Pacific, two-thirds of respondents anticipate outsourcing management of private equity, up 22% year-over-year.

## DISCLOSURES

Views expressed discussed are those of survey respondents, compiled by GSAM as of February 26, 2019.

2019 survey results as of February 26, 2019. 2018 survey results as of February 28, 2018. 2017 survey results as of February 22, 2017. 2016 survey information as of February 24, 2016. 2015 survey results as of February 25, 2015. 2014 survey results as of March 6, 2014. 2013 survey results as of March 5, 2013. 2012 survey results as of May 24, 2012.

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