Insurance Asset Management

Summer 2021

VIG
The chief investment officer for VIG's Hungarian operations checks in

Canopius Group
The group's portfolio strategy and risk manager pens his thoughts

China Pacific Insurance Group
The firm's chief investment officer offers his latest investment thinking

Alarm bells?

The PRA voices its concerns about UK life insurers' risk management of illiquid assets in MA portfolios

HEDGE FUNDS
The latest trends in this investment space for insurers

SUSTAINABLE INVESTMENT SUMMIT
An overview of the one-day conference for institutional investment delegates

GLOBAL EQUITIES
Market commentary on developments in this area

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Editorial Comment

> The UK economy is expected to expand by 7.25% this year. Surely it's onwards and upwards from here?

I have no idea how we are into June already! It seems that despite being under varying levels of lockdown restrictions so far in 2021, it has been one of the quickest six months on record, certainly in my eyes anyway.

As the UK population starts to be on the move again, predictions for UK economic growth look rather healthy. The Bank of England recently said the economy will enjoy its fastest growth in more than 70 years as COVID-19 restrictions are lifted. Indeed, the UK economy is expected to expand by 7.25% this year. Surely it's onwards and upwards from here? Well, it certainly is here at *Insurance Asset Management*. The brand, now in its fifth year is thriving and the content in this June edition supports that. The cover feature for this month looks at the PRA's recent warning over UK life insurers' risk management of illiquid assets as the latter increasingly looks for portfolio diversification and illiquidity spread pickup. We look at whether life insurers have this expertise to manage these assets appropriately and if not what can and should be done.

On top of this, we explore the hedge fund space and the outlook going forward in this area. How are insurers using these alternative investments in their investment portfolios and what are the benefits on offer?

In this issue we provide a detailed overview of the *Sustainable Investment Summit*, which provided insurance companies as well as pension funds, charities and corporates, with the opportunity to learn about the key issues within this investment area. This year's virtual event saw delegates gather online to discuss the latest trends and topics from across the sustainable investment market, as leading professionals and policymakers, such as the International Institute for Environment and Development (IIED), the Climate Disclosure Standards Board, WindEurope and ShareAction, shared their thoughts through a series of expert presentations.

As always, we have a whole host of leading chief investment officers (CIO), portfolio managers and heads of investment offering their views on the current global insurance landscape. For this issue, I am delighted to say we have interviews with the CIO of China Pacific Insurance (Group) Co., Canopius Group's portfolio strategy and risk manager, and the CIO of Vienna Insurance Group Hungary. Enjoy!

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6th floor, 3 London Wall Buildings
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ISSN ISSN 2516-8096

Publisher Member


08


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22


27


12


06
MODERATE
LOW
RISK
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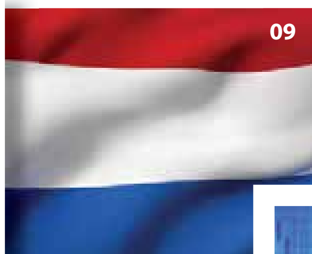
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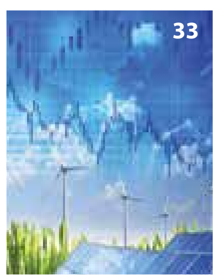
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Summer 2021

News focus

Insurers' exposures to macro risks remain at high level, EIOPA says

An increase in credit risks expected over next 12 months

Written by **Adam Cadle**

Insurers' exposures to macro risks remain at a high level while all other risk categories remain at a medium level, according to EIOPA's Risk Dashboard based on the fourth quarter of 2020 Solvency II data.

EIOPA's Dashboard also tracks credit risk, market risk, liquidity and funding risks, profitability and solvency, interlinkages and imbalances, insurance (underwriting) risks, and market perceptions. The Authority said it expects an increase in credit risks over the next 12 months, reflecting concerns over corporate indebtedness.

> Solvency positions for life business showed an improvement, while non-life business slightly deteriorated

With regards to macro risk, Gross Domestic Product growth and inflation forecasts registered new upward revision. The long-term yields have increased across currencies in the first quarter of 2021. Financial markets remain broadly stable, amid an increase in bond volatility and concern over commercial real estate investments.

Solvency positions for life business showed an improvement, while non-life business slightly deteriorated.

Insurers' profitability, measured by the return on assets and the return on excess of assets over liabilities improved due to positive market performance. Despite this improvement the insurers' profitability remained lower compared to pre-COVID levels.

Insurance risks remain at a medium level in spite of the deterioration of some indicators. The catastrophe loss ratio significantly increased and year-on-year premium growth for non-life continued deteriorating. On the other hand, year-on-year premium growth for life reported a slight recovery after the deterioration in the previous quarters.

> The stress test will evaluate both the impact on the capital and the liquidity position of the undertakings in scope

Market perceptions remain at a medium level with an increasing trend. The insurance sector, both life and non-life, underperformed the stock market in the first quarter of 2021.

The data is based on financial stability and prudential reporting collected from 81 insurance groups and 2463 solo insurance undertakings.

Last month also saw the launch of EIOPA's 2021 insurance stress test for the European insurance market. The 2021 stress test focuses on a prolonged COVID-19 scenario - in a "lower for longer" interest rate environment. The scenario, developed in cooperation with the European Systemic Risk board (ESRB), will assess the impact of economic consequences of the COVID-19 pandemic, which affect confidence worldwide and prolong the economic contraction. EIOPA said "the stress test will evaluate both the impact on the capital and the liquidity position of the undertakings in scope".

The objectives of the 2021 stress test are:

- To assess the resilience of participants to adverse scenarios from a capital and liquidity perspective to provide supervisors with information on whether the insurers are able to withstand severe but plausible shocks;
- To consider possible recommendations to the industry and to allow supervisors to engage with insurers on potential remedial actions;
- To complement the microprudential assessment with the estimation of potential spill-over from the insurance sector triggered by widespread reactions to the prescribed shocks.

EIOPA is now carrying out a Q&A process to provide further clarifications to participants. The stress test results are planned to be published in December 2021.

News in brief

- Italian insurance group Unipol Gruppo has selected the Moody's Analytics Climate Pathway Scenario Service to facilitate its efforts to embed climate risk into its Own Risk and Solvency Assessment (ORSA). Moody's Analytics will provide Unipol Gruppo with climate-aligned scenarios for a range of temperature pathways to help the group assess transition risk exposure.

- ABI director general Huw Evans is to stand down from his current role at the end of the year. Evans will be joining KPMG as a partner in its insurance and long-term savings practice from January 2022.

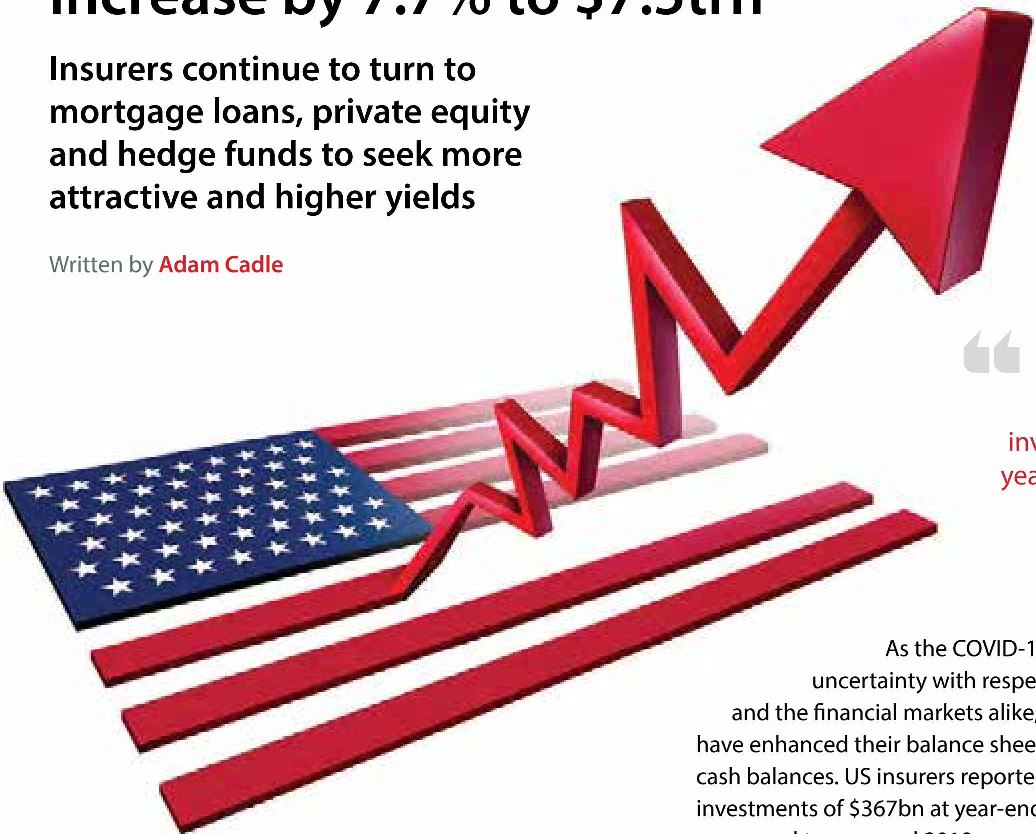
- Zurich's Swiss Solvency Test (SST) ratio rose by 19 percentage points over Q1 2021 to 201%, driven by favourable market conditions and the successful placement of US$1.75bn of subordinated debt. The acquisition of the MetLife P&C business and the early redemption of a hybrid debt instrument partially offset the increase. The latest figure remains well in excess of the group's 160% target level.

- Beazley has recorded an investment return of $27m for Q1 2021 compared to a loss of $55m in the same period last year. The insurer said: "This was a difficult period for fixed income assets, as rising yields generated losses on these exposures. We reduced the duration of our portfolio in the first quarter, which has helped to protect asset values. Equities have performed well and we were able to benefit by adding to our exposures during the period."

US insurance industry's cash and invested assets increase by 7.7% to $7.5trn

Insurers continue to turn to mortgage loans, private equity and hedge funds to seek more attractive and higher yields

Written by **Adam Cadle**



"US insurers reported cash and short-term investments of $367bn at year-end 2020, an increase of 27% compared to year-end 2019

The US insurance industry reported $7.5trn in total cash and invested assets at year-end 2020, an increase of 7.7% compared to year-end 2019.

According to latest figures published by the National Association of Insurance Commissioners (NAIC), the composition of the industry's assets was unchanged from prior years, with bonds and common stocks the largest and second largest asset classes, respectively. Mortgages formed 8.3% of total cash and invested assets.

Life companies hold the largest share, or 65.3%, of the industry's total cash and invested assets in 2020, while P&C companies account for 30.5%.

The share of bonds in the US insurance industry's portfolio at year-end 2020 declined to 62.6% from 63.8% at year-end 2019 as the low interest environment persists and insurers continue to be challenged with finding attractive yields in the fixed income market. Cash and short-term investments increased to 4.9% of total cash and invested assets as of year-end 2020 from 4.1% as of year-end 2019.

As the COVID-19 pandemic created uncertainty with respect to business prospects and the financial markets alike, insurance companies have enhanced their balance sheet liquidity with larger cash balances. US insurers reported cash and short-term investments of $367bn at year-end 2020, an increase of 27% compared to year-end 2019.

US insurance companies continue to seek more attractive and higher yields in relatively illiquid investments, such as mortgage loans, private equity and hedge funds in the prolonged low interest rate environment. While the share of Schedule BA assets in the industry's portfolio increased to 6.1% at year-end 2020 from 5.8% at year-end 2019, the share of mortgages declined to 8.3% from 8.6%. However, US insurers' exposure as measured in terms of BACV to these two asset classes continues to increase, with mortgage exposure increasing 4% YOY to $626bn and Schedule BA exposure increasing over 13% YOY to $456bn.

Growth in Schedule BA assets, including affiliated and unaffiliated, held by US insurance companies accelerated to more than 13% at year-end 2020. Last year marked the second year in a row that Schedule BA assets grew more than 10% on a YOY basis. The annual growth in Schedule BA exposure has generally exceeded the annual growth of total cash and invested assets since 2011; the only exception during the time period analysed was in 2015.

PRA issues warning to life insurance companies over illiquid assets

Regulator says firms can 'expect to be challenged' when investing in asset classes new to them

Written by **Adam Cadle**

The risk management among UK life insurers of illiquid assets is of "particular concern" to the PRA, with latest figures showing MA portfolios have increased since the start of 2018 by 30%, to around £335bn.

At the 18th Conference on Bulk Annuities, PRA executive director for insurance Charlotte Gerken said: "The range of assets that firms hold in their MA portfolios suggests to us that Solvency II (SII) is not in itself a barrier to firms investing in a wide range of asset classes. We see everything from covered bonds to infrastructure; and social housing to restructured Equity Release Mortgages (ERMs) backing annuity liabilities. And whilst the majority of exposures are what might be deemed traditional annuity assets, such as gilts and corporate bonds, less liquid exposures as a proportion of the MA portfolios are large and increasing.

"Insurers may be sole or significant investors in specialised lending and will require a commensurate level of expertise to assess, maintain and potentially work-out such assets."

Gerken added that firms can "expect to be challenged" when investing in asset classes that are new to them.

> Solvency II is not in itself a barrier to firms investing in a wide range of asset classes

Dutch insurers 'resilient' to pandemic - Fitch

Solvency II ratios remain above 160%

Written by **Adam Cadle**

Dutch insurers' overall financial profiles were resilient to the coronavirus pandemic, Fitch Ratings has said.

Insurers' Solvency II (SII) ratios remained above 160%, which corresponds to a Fitch credit factor score of 'aa-' or higher for regulatory solvency. Some insurers' SII ratios declined, mainly due to net capital outflows and the inclusion of banking subsidiaries in solvency capital requirements. Fitch said it expects the sector's capitalisation to remain broadly stable in 2021.

Fitch added: "The high quality of Dutch insurers' fixed-income portfolios reduces the likelihood of material losses from credit migrations or increases in bond default rates potentially caused by the pandemic.

"We expect cautious repositioning to higher-yielding assets to continue, but this is unlikely to materially affect our view of insurers' investment and asset risk metrics."

Institutional investors should take total portfolio approach to China – WTW

Active management also key in reaping diversification/return benefits of Chinese assets

Written by **Adam Cadle**

Using a total portfolio approach and active management of Chinese assets will allow institutional investors gain the long-term diversification and expected return benefits from adding these assets without a negative impact on their overall sustainability profile, new research has shown.

Willis Towers Watson (WTW) research said that although Chinese capital markets provide diversification benefits and attractive alpha opportunities for global investors, substantial challenges on the sustainable investment front have made investors cautious at the same time.

The total portfolio approach considers each risk factor in aggregate across the whole portfolio rather than just within each asset class. This framework allows investors to reduce exposure to assets that have negative sustainability characteristics elsewhere in the portfolio and increase allocation to Chinese assets that have better ESG momentum and better overall risk and return potential. Alternatively, increasing exposure to assets that have positive sustainability characteristics, for example investments in climate solutions, can be used to balance the overall sustainability profile.

> Active management can significantly reduce risk exposures related to poor ESG practices that sometimes can be encountered in China

WTW said skilled "active management can significantly reduce risk exposures related to poor ESG practices that sometimes can be encountered in China". When selecting investment managers, there needs to be a strong emphasis on their ESG integration and stewardship practices.

"Sustainable investing is not just about properly integrating ESG-related information for risk management purposes," WTW investments research team director and China project lead Liang Yin stated.

"It is also about recognising that long-term ESG-related themes, such as climate change, can create return opportunities. China has in recent years emerged as a world leader in funding and developing technologies to combat climate change and its net zero pledge will greatly influence economic and climate policies in the decades to come."

Green bonds top sustainable FI-list for institutional investors – NN IP

Investors 'can enhance impact they make without sacrificing returns'

Written by **Adam Cadle**

Green bonds are the most popular choice of sustainable fixed-income options for institutional investors, according to NN Investment Partners (NN IP).

A poll of over 230 institutional investors globally in March by NN IP found that 45% of investors think that they make the greatest positive impact. This was followed by sustainability-linked bonds (37%), social bonds (11%) and transition bonds (7%).

However, NN IP's survey found that the greatest barrier to green bond investing is the perception of inferior investment returns, according to 44% of respondents, followed by fear of greenwashing (38%) and insufficient market capacity (19%).

In addition, more than three in five respondents (63%) said they would use green bonds as an 'impact bucket' separate from their traditional bond allocation, whereas 20% would use them to replace corporate bonds and 17% to replace government bonds.

Commenting, NN IP lead portfolio manager green bonds Bram Bos said: "It is no surprise that green bonds are clearly the most popular sustainable fixed income instruments because they constitute the most mature and liquid market. They are probably the most effective way for fixed-income investors to enhance the impact they make without sacrificing returns.

> They constitute the most mature and liquid market

"At times, yields might be a little bit lower but over the last seven years, on average a euro-denominated green bond portfolio has generated 40 basis points more than a regular bond portfolio, and for corporate bonds, the difference is 60 basis points."

Although there are several passive alternatives available in the market, NN IP believes there are two key reasons that investors should favour active investing in green bonds."

Länsförsäkringar's recently reported its investments in green, social and thematic (sustainability-oriented) bonds on behalf of customers increased by approximately SEK 7.5bn in 2020.

Investments at the turn of the year amounted to more than SEK 17bn, which corresponds to more than 13% of assets under management in institutional life and insurance portfolios.

Of the approximately SEK 17bn in sustainability-oriented bonds, Länsförsäkringar Liv's investments accounted for approximately SEK 14.5bn, which corresponds to 14% of the life portfolios' capital.

AXA has also announced the successful placement of €1bn of subordinated green bonds due 2041.

The bonds will be issued under AXA Group's newly established Sustainability Bond Framework. The initial fixed coupon has been set at 1.375% per annum until the end of the 6-month call window period (October 2031), when it will become a floating coupon based on 3-month EURIBOR plus a margin including a 100 basis points step up.

ABI joins UN's Principles for Sustainable Insurance Initiative

UK industry can 'amplify' PSI's agenda-setting work

Written by **Adam Cadle**

The Association of British Insurers (ABI) has joined UN Environment Programme's Principles for Sustainable Insurance Initiative (PSI).

The PSI - a global sustainability framework and the largest collaborative initiative between the UN and the insurance industry - aims to strengthen the insurance industry's contribution as risk managers, insurers and investors to building resilient, inclusive and sustainable communities and economies on a healthy planet. The UK insurance industry is the largest in Europe and the fourth largest in the world, and the ABI represents over 200 member companies.

"Modern-day insurance roots can be traced to the UK insurance industry. This year, the UK is hosting COP26, which means that the UK insurance industry - through its risk management, insurance and investment activities - has a historic opportunity to lead by example in speeding up and scaling up the transition to a just and resilient net zero emissions economy," said Butch Bacani, who leads the PSI at the UN Environment Programme.

"This is why the ABI joining the PSI is an important and timely development. 'Insurance is coming home' so the UK insurance industry must go to Glasgow championing and demonstrating urgent and ambitious climate action."

> The ABI joining the PSI is an important and timely development

Last month, the PSI announced that it is establishing a pioneering Net-Zero Insurance Alliance (NZIA), which intends to join the COP26 Race to Zero campaign and the Glasgow Financial Alliance for Net Zero (GFANZ). GFANZ will work to mobilise the trillions of dollars necessary to build a global zero-emissions economy and deliver the goals of the Paris Agreement on Climate Change. Earlier this year, the PSI launched the final report on its ground-breaking project to pilot the recommendations of the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD). The report unveiled state-of-the-art approaches - particularly the use of climate change scenarios - to better assess climate-related physical, transition and litigation risks in the insurance business.

"The ABI is pleased to promote the adoption and implementation of the Principles for Sustainable Insurance throughout our membership. As the world heads towards COP26 in Glasgow, the ABI is focused on efforts to work with members and key stakeholders in accelerating the transition to a net zero economy while helping communities build resilience to a changing climate," said Huw Evans, director general of the ABI. "The ABI is committed to collaboration to address climate change and has been a longstanding supporter of the ClimateWise initiative. By working together with the PSI, we can ensure that the UK industry can join with our international partners to amplify the PSI's agenda-setting work on sustainability, from implementing the TCFD recommendations to supporting the development of the Net-Zero Insurance Alliance it is establishing. There is strength in numbers."

The ABI joins other insurance associations from across the globe that have become PSI supporting institutions, including insurance associations in Australia, Brazil, Canada, China, Colombia, Eastern and Southern Africa, Finland, France, Guernsey, Ireland, Italy, Luxembourg, Mexico, Morocco, New Zealand, Norway, South Africa, the Caribbean, the Netherlands,

> They will shape and promote the debate about sustainable capital investments

Insurers 'predestined partners' for green transformation of economy - GDV

More green bond issuance needed

Written by **Adam Cadle**

Insurers are "predestined partners" for the green transformation of the economy and sustainable infrastructure, GDV general manager Jörg Asmussen has said.

"They will shape and promote the debate about sustainable capital investments – and the industry itself will also become more sustainable step by step."

Asmussen argued, however, that in order for insurers to make their investments more sustainable, they need a much broader range on the market.

"So far, only 4% of the annual new bond issues have been issued as green bonds," he stated.

"Furthermore, more investment opportunities for green infrastructure projects are needed so that progress can be made quickly in reducing CO2. Sustainable investments need transparency: For sustainable and climate-neutral action, companies need extensive, reliable, but also easy-to-use information. For this purpose, an ambitious classification system is being created with the taxonomy in the European Union. In order for investors to be able to work with this information, it must be made available in a clearly and standardised manner in a freely accessible database."

Asmussen also argued that regulatory requirements and supervisory practice should take diversity among insurers into account.

Investor pressure adds momentum for reinsurers to integrate ESG factors

'High' or 'significant' pressure experienced

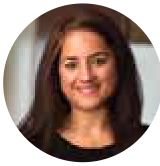
Written by **Adam Cadle**

Against a background of increased legislative and regulatory scrutiny of companies' sustainability practices, investor pressure is emerging as another important driver of environmental, social and governance (ESG) action, particularly for reinsurers, new research from AM Best has suggested.

In a recent AM Best survey of Europe and Asia Pacific-based (re)insurance companies, all the listed reinsurers that participated – including five of the 10 largest reinsurance carriers by non-life gross written premium – reported investors were the most (or second most) important source of pressure to consider ESG risks and opportunities.

Three of the top five said investors were exerting "high pressure" or "significant pressure" on them to consider ESG risks and opportunities. The other two cited "moderate pressure".

People on the move



KATE EL-HILLOW

Global Chief Investment Officer, Russell Investments

El-Hillow, who held several senior investment leadership roles at Goldman Sachs Asset Management, brings vast expertise in portfolio management, trading, outsourced CIO and multi-asset investment solutions. She will oversee all aspects of Russell Investment's division, including portfolio management, implementation and research. El-Hillow has also worked at J.P. Morgan Chase & Co.

KEVIN KERRIDGE

Chief Executive Officer, Hiscox USA

Hiscox has announced that Kevin Kerridge has succeeded Steve Langan as CEO of Hiscox USA. Having joined Hiscox in 1996, Kerridge created the insurer's first direct online business in the UK; initially for home insurance and then for commercial clients. In 2009, Kerridge relocated from London to New York to oversee the launch and development of Hiscox's US digital small business operation.

LINDSEY RIX

Chief Executive Officer, UK, Canada Life

Canada Life has appointed Lindsey Rix as UK CEO following the departure of Doug Brown late last year. Rix will continue to deliver the strategy set by the UK board to deliver a major transformation programme with the ambition to become a major competitor in the retirement market combining the core strengths of its wealth, insurance and asset management businesses.

PAUL GRIFFITHS

Global Head of Institutional Business, HSBC Asset Management

With over 30 years' experience in the industry, Griffiths will be responsible for the commercial development of the firm's institutional business and leading its institutional sales and client management teams. He takes over from Brian Heyworth who left the firm last year. Griffiths joins from First Sentier Investments and has also worked at Aberdeen Asset Management.

OLIVIER DE LAROUZIÈRE

Chief Investment Officer, Global Fixed Income, BNP Paribas Asset Management

De Larouzière will be responsible for managing BNPP AM's global fixed income platform, with a strong focus on investment performance and commercial success. He will retain his existing role as head of BNPP AM's global multi strategy product (GMS) team and will additionally join the business, investment and investment management committees.

JONATHAN AIACH

Investor Relations Director, Generali Global Infrastructure

Generali Global Infrastructure (GGI) has appointed Jonathan Aiach as investor relations director. Aiach's arrival is part of the company's accelerated growth, and in particular the expansion of its investment solutions and its European institutional investor base. GGI manages over €3 billion of assets under management in a number of strategic themes.

Soapbox

Building for the future

Written by **Adam Cadle**

I recently wrote about insurers being the 'predestined partners' for the green transformation of global economies. Indeed, the same can be said for the relationship between insurers and infrastructure.

The UK and the US, for example, look set for an infrastructure boom this year and going forward. US President Joe Biden wants to build a post-pandemic US recovery stating that unless the US makes significant improvements in infrastructure, it risks falling behind China which could, in his words, "eat our lunch". Roads, bridges, ports and water supply systems in the US were mainly built in the 1950s and 1960s, so they are outdated and in need of replacement. In the UK, the government has further promised to boost investment in infrastructure and there is an expectation that civil engineering projects disrupted by lockdown will recover in 2021. The role of the insurer is crucial in this progress and it makes no sense for institutional investors to ignore this asset class. It should be considered as core.

Infrastructure can generally be classified as three key areas: transportation, energy & utilities and social infrastructure. With this the main features associated with this asset class are durable cash flows, inflation hedge, portfolio diversification, long duration for certain sectors, ESG sensitive and illiquidity premiums. These features are more relevant than ever, given insurers' constant search for yield in a market offering low yield and an abundance of risk. The leading purpose of infrastructure investments is to improve economic activity and increase productivity as well as improving social welfare. Insurance companies are active in all of those aspects. Indeed for the US, infrastructure is a natural extension of current investment processes as large US insurers already allocate to revenue-backed municipal bonds.

Capital relief around infrastructure now incorporated under Solvency II regulation has also aided the process of insurers investing in this asset class, and this should now make it top-of-mind for investors.

> The leading purpose of infrastructure investments is to improve economic activity and increase productivity as well as improving social welfare

The ability to access infrastructure in equity or debt format should also be of particular interest to insurers. In a recent article published on its website, Aberdeen Standard Investments, "in debt format, the long-dated nature of loans creates interest from life insurers, with maturities typically in the range of eight to 15 years".

"There's also great interest in infrastructure in equity format. Internal rates of return can be in the region of 8-10%, with an income yield of 4.5% assuming core and core+ European infrastructure assets. This compares attractively to public market equity with our long-term expected returns focus in the region of 6-7% for European equities."

I believe an infrastructure boom is just around the corner. Historically, governments and investors have been terrible at making projects happen but this time it could be different. Private sector investment can and must be allowed to be a major driver of the UK's and US's infrastructure boom, particularly at a time when public purses have been stretched by unprecedented COVID-19 support measures.

CBI chief UK policy director Matthew Fell recently said: "To support its ambitious infrastructure agenda and provide better connectivity, at good value for taxpayers, the government must reinvigorate the UK infrastructure market tackling concerns about regulation and a lack of clarity about investment opportunities.

"The government must commit to an approach that gives confidence to investors and capitalises on the attributes of businesses and public sector establishing itself once again as a world class destination for investment." I couldn't agree more.

A view from China

Adam Cadle speaks to chief investment officer Benjamin Deng about the workings behind China Pacific Insurance Group

WRITTEN BY **ADAM CADLE**

Q Could you provide an overview of China Pacific Insurance Group and your day-to-day role?

In 1991, China Pacific Insurance (Group) Co., Ltd. was founded in Shanghai. CPIC is a leading integrated insurance group in China, providing, through our subsidiaries and along the insurance value chain, a broad range of risk protection solutions, wealth management and asset management services.

With full insurance licenses, CPIC keeps the focus on the insurance business, and has developed expertise in life and health insurance, property and casualty insurance, and investment management, continually achieving balanced growth among all segments.

By the end of 2020, CPIC had a total AUM of CNY2.4 trillion. CPIC ranked No. 193 on Fortune Global 500 in 2020, and No.5 on Brand Finance Insurance 100 in 2021.

Over the past 30 years, CPIC has expanded its competitive strength and became one of China's largest insurance groups with a solid capital position, leading value proposition, and robust risk management, and the first insurer simultaneously listed in Shanghai, Hong Kong and London. The successful issuance of GDR has enabled the company to integrate into the global market. Through the issuance, CPIC would further achieve a diversified and balanced shareholding structure.

My role as the group chief investment officer involves setting group investment policies, the strategic asset allocation (SAA), monitoring market conditions and giving directions on tactical allocation, and advising the chairman and CEO on strategic investments, etc.

Q How has the firm adapted to COVID-19 in terms of its investment thinking and direction? What is your overall investment portfolio structure?

CPIC is a long-term investor following the philosophy of "Value Investing, Long-term Investing, Stable Investing".

> **Over the past 30 years, CPIC has expanded its competitive strength and become one of China's largest insurance groups**

Our investment is directed by our SAA that is liability-driven and aims to bring stability in asset allocation through the macroeconomic cycle. Around the SAA, we have disciplined tactical asset allocation (TAA) based on our assessment on the econo-political condition. On top of the SAA and TAA, we make securities selection based on fundamental research in order to deliver alpha. Our investment performance is measured on a multi-year basis balanced by current year income requirements. In the past years, CPIC has delivered a stable investment return that well exceeded the liability requirement, and our shareholders have realised stable and healthy ROE. In 2020, amid the historical COVID-19 pandemic, we yet again delivered a total investment yield of 5.9%.

With the unprecedented global monetary and fiscal easing and as we anticipate that yields are to fall, we have been focusing on a barbell strategy that strengthens that allocation to long-duration fixed income asset and equity investments, while maintaining very stringent focus on credit risk management. As per our *2020 Annual Report*, CPIC has 78.3% of assets allocated in fixed income, 18.8% in equity, and the remaining part consists of investment properties (0.5%) and cash, cash equivalents and others (2.4%).

Q What was your biggest achievement in your role during 2020?

We did a few great things in 2020. Two things stand out as my biggest 2020 achievements. First, I participated as one of the leading executives in CPIC's highly successful IPO on the London Stock Exchange; and secondly, we delivered a remarkable total investment return despite the severe global pandemic.

Q What do you see as being the biggest challenges for Chinese insurers in 2021?

2021 will bring good macro economic data with China on a very strong economic trajectory and many countries ready to reopen the economies. Insurance companies in China are facing a few challenges including increasing credit default risk as some sectors of the economy are not yet out of the woods and some traditional companies are facing higher pressure amid political and ESG dynamics.

Q Could you explain your focus on ESG?

CPIC has been very proactive on ESG. Each year, in our annual social responsibility report, we tell our achievements on ESG. Our investments philosophy of "Value Investing, Long-term Investing, Stable Investing" is built with company governance as the core, while environmental protection has been a national policy

Total assets of China's insurance companies amounted to RMB 24.3trn at the end of Q1 2021, up by 4.1% from the beginning of the year, latest figures have shown.

- According to the China Banking and Insurance Regulatory Commission (CBIRC), compared with the beginning of the year, assets of P&C insurers registered RMB 2.5trn, up by 5.9%. Assets of life insurance companies reached RMB 20.7trn, up by 3.8%.
- Furthermore, assets of reinsurance companies recorded RMB 541.4bn, up by 9.2%, and assets of insurance asset management companies were RMB 78.4bn, up by 3.1%.
- As of the end of Q1 2021, insurance companies had recorded primary insurance premium income of RMB 1.8trn, up by 7.8% year on year.
- At the end of Q4 2020, the average comprehensive solvency ratio of the insurance companies with data collected was 246.3%, and the average core solvency ratio was 234.3%.

in the past years so being compliant in this respect becomes an essential requirement. CPIC is one of the largest insurance investors in renewable energy, modern agriculture, river cleaning projects, foresting projects, etc. CPIC has taken the highest responsibility in promoting environmental awareness. By the end of 2020, CPIC had provided environmental liability insurance for more than 4,360 enterprises with a total coverage of more than CNY7.9 billion. The company also provides insurance for new energy, with coverage of circa CNY940 billion in 2020. On the investment side, by the end of 2020, CPIC has made circa CNY55 billion direct investments in new energy and environmental protection, which include a 165-acre forest in Qinghai province at the common origin of the three major rivers of china. On social responsibility, CPIC is the winner of the highest national award in poverty alleviation – the 2019 National Poverty Alleviation Award for Organisational Innovation. CPIC was the first company in the world to develop a poverty-prevention insurance product, providing coverage for those who would return to poverty due to unexpected reasons such as illness, education expenses and natural catastrophe. The poverty-prevention insurance has covered more than 100 million people and has paid out CNY620 million on claims. CPIC also provides agricultural poverty alleviation programs, such as climate-index insurance for Qinghai province, cotton and corn insurance for Xinjiang, and poverty alleviation income insurance for Tibet.

Q What are your main aims over the coming years for China Pacific Insurance Group and yourself as group chief investment officer?

To keep delivering stable investment returns that meet liability requirements and ROE requirements. Also we will further enhance our alternative investment capabilities both domestically and overseas.

Q Away from the day-to-day role what do you do to relax?

I have a wide range of hobbies including calligraphy, Tai Chi, poetry, music, and partying with friends.

China is set to become the largest global insurance market, attracting foreign insurers to invest in the country, GlobalData has said.

China's gross written premium (GWP) which stood at US$195.65bn in 2020, is forecasted to reach US$259.97bn in 2024.

In December 2019, the Chinese Banking and Insurance Regulator lifted a 51% cap on foreign insurers ownership in Chinese operating insurers.

Jazmin Chong, insurance analyst at GlobalData, commented: "While the abolished rule levels the regulatory playing field for foreign entries, it is important to recognise that lifting of capped ownership is aimed at benefiting Chinese firms rather than foreign ones.

"China's strategy of opening its market to foreign players is part of the country's wider economic efforts to bridge the gap between international competing firms and China. China is also expecting that foreign insurers will push domestic insurers to learn from global best practices, fostering better corporate governance, risk pricing, and investment management."

CHINA'S RENMINBI DEBT: *a new line of defence?*

Why Chinese onshore bonds are becoming an indispensable asset class for international investors

WRITTEN BY **CARY YEUNG, HEAD OF GREATER CHINA DEBT**

Just over a year after the Covid-19 outbreak began causing economic turmoil around the world, it appears investors may have discovered a new defensive asset: Chinese renminbi debt. The USD16 trillion bond market has come through the crisis exhibiting the sort of stability normally associated with benchmark US Treasuries. Not only did it hold up better than developed market government bonds during a tumultuous first quarter of 2020, it has also since traded within much narrower ranges. Its potential as a risk mitigation tool has also been thrown into sharp relief.

Over the past several months, renminbi bonds have not moved in lockstep with the world's other major bond markets. Neither have they tracked emerging market assets. All of which suggests they could turn out to be a good hedge against the riskier assets investors hold in their portfolios. One explanation for this new-found resilience is that reforms in China have allowed renminbi-denominated bonds to feature more prominently in mainstream global bond benchmarks. Index inclusions are landmark developments, both for China and for investors worldwide. For authorities in Beijing, they are a stamp of approval for their efforts to liberalise the country's capital market and integrate more fully into the international financial system. For investors, it opens up a new world – one where the renminbi becomes a genuinely global investment currency.

Foreign ownership of Chinese bonds was already rising in anticipation of the index changes. Non-Chinese investors built up their holdings of RMB debt to RMB3.2 trillion by December 2020, up nearly 50 per cent from the same month a year before.[1] Of the USD9.5 trillion of assets under management from corporate and public pension funds globally, 0.26 per cent was held in Chinese bonds as of the third quarter of 2020, up from 0.04 per cent in 2015.[2] Further boosting the market's international standing, China has delivered a series of reforms to make it easier for foreigners to access the market. Among the most important, the "Bond Connect" programme, launched in 2017, allows non-Chinese investors to trade in Hong Kong without an onshore account. Already, 75 out of the world's top 100 asset managers have joined the programme while trading volume doubled last year to RMB4.8 trillion.[3] All of which means the inflows seen since the pandemic are likely to be part of a much larger reallocation.

Opportunities beyond pandemic

Policymakers are also keen to attract foreign funds to hasten the development of the asset management industry across the country. This is a priority for Beijing as the country's rapidly aging population demands a sustainable pension system. China's asset management industry – fund houses, insurers and securities and trust companies – is expected to triple in the 10 years to 2028 to RMB47.3 trillion as Beijing removed all foreign ownership restrictions in April 2020.[4] This should help diversify the domestic and foreign institutional investor base for Chinese securities, which is currently dominated by commercial banks. Foreign investors make up just under 3 per cent of total holdings today, which we expect to rise to 3.3 per cent this year.

Calm amid turmoil

The opening up of the market comes at a time when the fundamentals of Chinese local currency bonds look particularly strong. Yields offered by onshore RMB bonds are attractive to international investors as a record USD16 trillion of global bonds yield below zero. The five-year Chinese government bond yield stands at 2.9 per cent, compared with 0.9 per cent for US Treasuries, -0.1 per cent for Japanese Government Bonds and -0.7 per cent for German Bunds with the same maturity – differentials that have never seen before.[5]

Yield is not the only selling point. They also offer a means of diversification. Chinese bonds's returns do not correlate especially strongly with those of any major global asset class – bond or equity. The correlation of returns from renminbi bonds with those of US and European government debt and equities, for example, is less than 0.2.[6] What is more, Chinese bonds have exhibited remarkable resilience during historically volatile periods, such as the 2008 global financial crisis and the European debt crisis.

The Covid pandemic was no exception. Renminbi bonds were among the few asset classes to deliver positive returns during the sharp sell-off of the first quarter of 2020, performing more in line with other G10 government bonds.[7] Of greater significance was that their maximum drawdown for 2020 - their peak-to-trough decline - was just 2.2 per cent, a fraction of the losses endured by global bonds (around 9 per cent) and US dollar investment grade credit (over 15 per cent).[8]

Chinese local currency bonds have also proved to be historically resilient to rising US yields. In the most recent global bond market sell-off, they have performed better than any other fixed income asset classes. This further reinforces their standing as a defensive asset.

RMB - an international currency

As the world's second largest economy matures, Beijing is committed to opening up its financial market and promoting the greater use of the Chinese currency abroad. The RMB is already the world's fifth largest reserve currency but it accounts for just under 2 per cent of the total central bank reserves. If that share were to double, it would amount to an additional RMB1.5 trillion of RMB bond investments, the IMF says.[9] According to Pictet Asset Management's economists, it won't be long before the RMB's share of international reserves is greater than that of the British pound. All of this is likely to lead to a greater appreciation of the RMB, which should contribute strongly to the total return of investors' bond portfolios.

Going green

Another favourable development is China's recent announcement that it plans to be carbon neutral by 2060. The ambitious goal is likely to require as much as USD16 trillion of investments, where we believe green bonds will be an important channel. The PBOC has already promised to improve the country's green finance standards to support the 2060 goal and make it easier for foreign investors to enter the green finance market. As of June 2020, China's outstanding green bonds totalled RMB1.2 trillion, the second largest in the world. This figure should grow in the coming years, helping expand the universe and increase the depth of the Chinese onshore bond market in the long term.

With its population ageing rapidly and its investment needs rising as a consequence, China has every incentive to remove restrictions on the flow of capital across its borders and drawing in foreign funds. And nowhere other than the RMB onshore bond market can investors see China's economic transformation more clearly in the coming years. As the year of the Ox promises to bring growth for Chinese RMB-denominated bonds, the asset class should become an even more integral part of global fixed income investors' portfolios.

In association with

PICTET 1805 Asset Management

1 Wind, Standard Chartered Research as of 31.12.2020
2 eVestment/Reuters
3 Bond Connect as of 31.12.2020
4 Roland Berger, on mutual fund assets under management basis
5 Yield in local currency as of 07.04.2021. Source: Bloomberg
6 All indices are total return and in USD unless indicated. Based on monthly data from 31.10. 2008 – 31.12. 2020. Source: Chinabond, JP Morgan, HSBC, Bloomberg
7 Source: Chinabond, JP Morgan. All indices are total return and in USD. Based on the following periods: Great Financial Crisis (Aug-Oct-2008); EU sovereign debt crisis (Aug-Nov 2011); Covid-19 (21.02.2020-15.04.2020)
8 Bloomberg Barclays China Composite index, USD unhedged basis, global agg and USD IG Source: Bloomberg Barclays
9 IMF: The Future of China's Bond Market, March 2019

Alarm bells?

Adam Cadle explores the PRA's concerns about UK life insurers' risk management of illiquid assets in MA portfolios

WRITTEN BY **ADAM CADLE**

It goes without saying that supervisory risk analysis of any financial sector is absolutely crucial if optimal functionality is to be maintained going forward. The UK insurance space is no different, with the Prudential Regulation Authority (PRA) responsible for the prudential regulation and supervision of banks, building societies, credit unions, insurers and major investment firms. Indeed, when aspects of a financial system don't quite tally up with a regulator's thinking and supervisory statements, alarm bells can naturally start ringing.

The supervision of life insurers and annuity writers since the inception of Solvency II has firmly been on the PRA's radar, and recently the regulator has raised concerns about the risk management of less liquid assets in Matching Adjustment (MA) portfolios within the bulk annuities market. At the 18th Conference on Bulk Annuities, PRA executive director for insurance Charlotte Gerken said "the growth of annuity lines through bulk purchase transfers from defined benefit pension schemes, and the specialisation in annuity lines, attracts significant regulatory focus".

"With much longevity risk currently being reinsured, firms will not have failed to notice that our engagement on asset risk has increased markedly as investment returns on assets backing the annuities are the key driver of pricing in the bulk annuity market," she added. "MA portfolios have increased since the start of 2018 by 30%, to around £335bn. The range of assets that firms hold in their MA portfolios suggests to us that Solvency II is not in itself a barrier to firms investing in a wide range of asset classes. We see everything from covered bonds to infrastructure; and social housing to restructured Equity Release Mortgages (ERMs) backing annuity liabilities. And whilst the majority of exposures are what might be deemed traditional annuity assets, such as gilts and corporate bonds, less liquid exposures as a proportion of the MA portfolios are large and increasing. The risk management of less liquid assets is of particular concern to us. Insurers may be sole or significant investors in specialised lending and will require a commensurate level of expertise to assess, maintain and potentially work-out such assets."

Attractions and concerns

So, with the PRA warning that firms can expect to be "challenged" when investing in asset classes that are new to them, what is the attraction of these less liquid asset classes and how much of a concern is the risk management factor given MA portfolios have risen by 30% to around £335bn?

Hymans Robertson head of insurance investment & ALM Daniel Becker says "such assets may offer diversification, better security, opportunities to tailor to firms' requirements, as well as potentially higher returns".

"They may also deliver societal benefits, e.g. in meeting climate goals. One important thing to remember here is that liquidity is a continuum, not a binary state. There is so much demand for certain so-called illiquid assets, that we really need to think of a better name for them," he adds.

Nevertheless, Becker states that "it is completely understandable that the management of asset-related risks remains a key concern of the PRA".

"After all, spread or credit risk, along with property and other market risks, makes up a significant proportion of UK annuity writers' SCRs. At Hymans Robertson, we see demand for £40bn of bulk annuities a year through to 2030, so portfolios will continue to grow, albeit tempered by the run-off of existing business and increased use of asset reinsurance."

> " It is completely understandable that the management of asset-related risks remains a key concern of the PRA

Another spokesperson who is head of illiquids for a FTSE 100 UK insurer states "the assets would have been financed in any event, so at least in MA portfolios those investments are under heightened risk, ALM and regulatory scrutiny".

Mitigation

In order to mitigate the regulator's concerns, bfinance, director – insurance client consulting, Neil Holmes, argues that new asset classes do mean that "we find a constant need to educate insurers in what they are, what size the market is and how they perform, to ensure firms comply with Prudent Person Principles".

"I see far more requirement/onus on managers to help with this aspect too. That goes for ratings as well. The more 'specialised' asset class you go into, the less likely you are to have ratings from the ECAIs, instead either relying on internal ratings or forgoing ratings as such. We have conducted recent manager searches requiring some form of external

> Managers and consultants need to work together to help mitigate the regulator's concerns

ratings on all individual assets (there are some solutions), but the provision can be limited. The majority of bulk annuity firms run good, sophisticated internal models which the PRA seems happy with, but it takes time for both insurers to understand new asset classes and amend models. So I agree with the PRA and their concern on potential capabilities within risk management. However, this 'problem' is not going away, so managers and consultants need to work together to help mitigate the regulator's concerns."

The FTSE 100 UK insurer head of illiquids says external managers and the abdication of ownership to external advisers can't be relied upon solely. "That resource hire should be in portfolio management/origination, risk oversight and rating assessments," he argues.

It must be noted however that there is no one-size-fits-all solution for the expertise needed to manage these less liquid assets. For Becker, different approaches will work for different firms, and it's not always about specialist expertise, much can be achieved by "refining governance, systems and processes".

"For example, that could include strengthening the new deal approval process or improving systems for the exchange of data between asset manager and insurer. But it's worth remembering that insurers are in the business of taking risk and are well accustomed to dealing with complex exposures – this is not unchartered territory.

"The PRA has raised concerns around the level of matching adjustment benefit that firms take, both in the base balance sheet and in the calculation of the SCR. Some elements of this are beyond individual firms' control – for example, the insensitivity of the fundamental spread in the Solvency II regulations. Some relate to internal ratings and valuation, which is a complex area. One area that is challenging for firms is dealing with asset classes that are not typically publicly-rated. For example, commercial real estate loans. It's not always obvious how firms should benchmark themselves. In some cases, insurers may have more experience of performing ratings than the rating agencies. Of course, the SCR is calibrated to a 1-in-200-year VaR, which means that there is always going to be an element of judgement involved in calibrating models, as we are talking about events that are well in the tail of the distribution of possible outcomes. This is true of more liquid assets just as it is for less liquid."

As with any piece of prudential analysis questions arise. Supervisory expectations in this area have been published such as the Supervisory Statement 1/20 "Solvency II: Prudent Person Principle" and Supervisory Statement 8/18: "Solvency II: Internal models – modelling of the matching adjustment". Is the regulator being too harsh in issuing these concerns and challenges?

"The regulator clearly has a job to do," Becker says. "One welcome aspect of Gerken's speech is the idea of introducing more flexibility around the MA approvals process, alongside other potential areas of reform under HMT's Solvency II review. One thing I think is important is that the regulations should continue to emphasise that internal models should be owned by individual firms. We should expect and encourage divergence rather than reversion to the mean."

Holmes feels there is an "expectation post Brexit for some sensible, advantageous tweak to regulations to assist UK PLC, although the PRA does not seem to currently share that same view".

"Whilst I know that the Regulator's primary concern is to protect the policyholder, it also remains a key figure in UK PLC and needs to consider practicalities at times and allow the BA providers to run efficiently a service that unlocks a segment of the Market (DB/DC) that in my opinion continues to head down an unenviable path. EIOPA showed shortly after the launch of SII in 2016, that it can reflect economic and societal needs in adjusting the capital weightings on Infrastructure, so the PRA needs to be hugely mindful of evolving circumstances in our post-COVID, ongoing very low interest rate, world and allow professional, BA providers to use their knowledge and judgements to run a key service."

Outlook

It doesn't sound as if these supervisory challenges by the PRA will change anytime soon however.

"Close supervision of the MA contributes to securing an adequate degree of protection for policyholders and we will continue to develop our analysis both to improve our supervision and to inform policy development," Gerken argues.

"The Call for Evidence has drawn a wide range of views on the nature of the MA and we are committed to working with the industry and HMT's objectives for the review. Annuity writers may rightly feel that they receive significant supervisory challenge from the PRA. This will not change, given the nature and importance of the annuity product, the significant judgements and assumptions that underpin the MA benefit available to firms, and the impact of annuity providers on our policyholder protection objective."

On the issue of climate change, Gerken said the regulator does want to see firms investing in ways to help manage the risks arising from climate change, however when assessing capital requirements of 'green' assets and 'productive finance', "we must as a prudential regulator consider the risks in individual assets. A departure from such an approach reduces the resilience of firms and potentially the wider financial system".

"We are also open to removing unnecessary barriers. A significant constraint currently is the binary nature of MA approvals, and in the course of supervisory engagement firms have raised the risk of the loss of the MA where breaches have not been rectified within two months.

As part of considering the responses to HMT's Call for Evidence on Solvency II reform, we will review the MA approvals process. And, whether changes there need to be balanced by stronger post-approval supervision to ensure the MA framework continues to work as intended."

Concerns obviously remain in the insurance space over the risk management of illiquid assets in MA portfolios. The regulator and the industry will have to continue working closely together to mitigate any worries.

> "We must as a prudential regulator consider the risks in individual assets. A departure from such an approach reduces the resilience of firms and potentially the wider financial system

Chatting with Canopius

Conor Sweeney, portfolio strategy and risk manager at Canopius, talks to *Insurance Asset Management* about the firm's investment strategies and the excitement of life's simple pleasures returning

WRITTEN BY **ADAM CADLE**

Q Could you provide an overview of Canopius Group and your day-to-day role?

Canopius is a global speciality (re) insurer. We operate one of the largest Lloyd's of London syndicates, and have growing operations in Australia, Singapore, and across the United States.

Being part of the internal investment team, and reporting to the chief investment officer, my role is ultimately to help the group maximise value through its investment strategy. Practically, on a day-to-day basis, that means developing the analytical tools necessary to evaluate prospective investment opportunities in terms of expected return and risk, and optimise the portfolio in the context of our wider balance sheet exposures and corporate objectives.

Q How has the firm adapted to COVID-19 in terms of its investment thinking and direction within the portfolios you manage?

Our primary objective of maximising expected return subject to various risk limits and constraints hasn't changed. But of course, the knock-on impacts resulting from the pandemic are still being felt, evaluated, and priced into financial markets.

The expansive monetary and fiscal policy response to the pandemic enabled liquidity to return to global markets, prices to rebound and subsequently stabilise. At the same time, abundant market liquidity has also resulted in historically low yields on the assets non-life insurers like Canopius have traditionally bought to back their claims liabilities, such as government bonds and other publicly-traded investment grade credit securities.

While such core assets will continue to form the majority of our portfolio going forwards, we expect to deploy more capital to private market (debt) opportunities. While such assets tend to be relatively high-yielding, associated due diligence and implementation is generally more resource-intensive. The illiquid nature of such holdings also has risk implications, which needs careful thought and analysis.

Q What was your biggest achievement in your role during 2020?

The COVID-19 shock induced significant volatility and price dislocations across financial markets, peaking towards the end of March. While uncertainty was undoubtedly elevated at the time, past crises experience showed us that being a willing and able provider of liquidity to financial markets in such circumstances tended to be well rewarded.

Not long before COVID hit, we presented a strategy to our investment committee of how we would respond in the event of a financial market liquidity crisis, and subsequently put in place the necessary operational and governance structures to enable us to execute such a strategy. Doing so in advance enabled us to be dynamic and add risk exposure during March. This planning ultimately helped us capture returns as prices

Photo by: Christian Mueller / Shutterstock.com

recovered through the remainder of the year.

Q What do you see as being the biggest challenges for Canopius and in general UK insurers in 2021?

From the investment side of things, much of the recent market narrative has focused on the risk of higher inflation in the future.

In the US there has been significant amount of fiscal support in response to the pandemic, with an expectation of more to come. Our balance sheet liabilities and nature of our business mean that a significant portion of our portfolio is invested in US dollar fixed income securities. If we experienced higher bond yields in response to higher inflation expectations, that would cause mark-to-market losses on these holdings – I suspect many of our peers would be impacted similarly.

While this impact would be mitigated by the relatively short duration of our portfolio, it would be very interesting to observe the impact of higher interest rates on the broader financial markets, particularly if increases were to occur over a short period of time. In that environment, risk assets could come under pressure, particularly if the monetary policy response is more constrained in the context of its inflation targeting objective, as in the case of the US Federal Reserve.

Our balance sheet liabilities and nature of our business mean that a significant portion of our portfolio is invested in US dollar fixed income securities

Q Could you explain your focus on ESG?

Specific to the investment side, we have established and implemented a *Group Responsible Investment Policy*, which was developed with reference to the UN Principles for Responsible Investment and the *UK Stewardship Code* guidance.

Our investment operating model involves the outsourcing of security selection to external investment managers, and one of the aims of this policy is to ensure our chosen partners are aligned to our ESG principles. Specific to climate change, that is something that has the potential to impact both sides of our balance sheet, and we are working with colleagues throughout our organisation to improve our understanding of this evolving risk.

Q What are your main aims over the coming years for yourself as portfolio strategy and risk manager?

The low yield environment will continue to pose a challenge to insurers. To deliver value as an investment function, that will mean continuing to work hard to source diversified avenues to deliver incremental return, while always ensuring we have understood the associated risk on new investments as far as possible.

At the same time, financial markets are dynamic and prone to dislocation from time to time – ensuring we have the analytical capacity to monitor and understand developments in real time, such that we may capitalise on opportunities when presented in future is something I very much look forward to further developing.

Q Away from the day-to-day role what do you do to relax?

Being in lockdown over the past few months, the options have been more limited of course. I have been doing a lot more cooking than I used to, and I now probably over-rate my abilities in this area! In any case I am very much looking forward to getting back to normality like everybody else, and will try not to take for granted the ability to meet up with friends in a bar, play football, and all the rest of life's simple pleasures.

Invesco was recently named as an alternatives partner for Canopius Group.

Through this partnership, Invesco will provide Canopius with a customised solution of multi alternatives strategies, via Invesco's alternatives platform, which provides access to alternatives, focusing on private debt strategies across the UK, Europe, and US.

Invesco will work alongside Canopius assisting with customised asset allocation, implementation, monitoring and risk oversight.

Canopius chief investment officer Gareth Russell said: "In challenging low-yield market environments such as these, we are always seeking innovative solutions to improve returns in an efficient manner. As a global (re)insurance company, prudent risk management is paramount in all our investment decisions. We understand that investing in less traditional fund structures requires close partnership with experienced investment management professionals.

"We're delighted with the creation and launch of our portfolio with Invesco and look forward to continuing to seek out returns together."

A hedge too far?

Michael Griffiths looks into how insurers are currently feeling about the hedge fund market

WRITTEN BY **MICHAEL GRIFFITHS**

When a coordinated army of amateur investors pumped up the price of video game retailer GameStop earlier this year, a $13 billion hedge fund was left with both huge losses as well as a glaring spotlight. Melvin Capital had bet against GameStop by short-selling its shares. However, this type of investment vehicle became a hot topic when members of the Reddit thread 'wallstreetbets' piled into GameStop with the aim of pushing up the share price to inflict losses on short-sellers, including Melvin Capital. The move, a short-squeeze, saw GameStop's shares surge tenfold in just a matter of weeks.

The episode ignited debate about the strategies and ethics behind inflated stock prices, and the roles of the hedge funds and investors involved. With this battle fresh in mind, and a reminder of the great losses some funds may stand to lose, how is the insurance sector viewing the hedge fund market itself as an asset class in 2021?

Current views

Research into alternative investments in the insurance sector from 2015, published by The Hedge Fund Journal, once stated that what makes hedge funds particularly attractive is their ability to "harness a diverse array of investment and trading strategies" that may be combined to address almost any risk-return spectrum. It means that experienced portfolio strategists may assemble multiple investments into customised, liability-driven portfolios in a way that other alternatives cannot.

According to the latest hedge fund industry update provided by alternative asset data provider, Preqin, neither the ongoing disruption caused by the coronavirus pandemic, or any trading events that have sparked media frenzies, have managed to derail the hedge fund market.

The performance of hedge funds has followed a strong 2020 by continuing its positive trajectory into the first quarter of this year. The Preqin All-Strategies Hedge Fund Benchmark was up 7.81% in Q1 2021, compared with 5.77% for the S&P 500 PR Index, which experienced a volatile quarter.

Preqin's numbers reveal that overall, despite structural changes in the market, hedge funds have revealed their worth to investors by experiencing their best first quarter since 2006. The data shows that equity strategies dominated as credit fell out of favour in Q1, with 42% of new launches equity managers, a figure up 13 percentage points on Q4 2020. Only 7% of new launches in Q1 were credit hedge funds.

Elsewhere, the figures also show that macro strategies launches declined in the first quarter, accounting for just 5% of new funds, a figure down from 13% in Q4 2020. The alternative asset data specialist revealed that Asia-Pacific markets are further along their path to recovery and are capturing investors' attention, with APAC having experienced a 9% increase in fund launches compared with Q4 2020. Furthermore, Preqin states that 84% of investors are intending to invest less than $50m of fresh capital into hedge funds over the next 12 months.

Whilst no new CTA funds came to market in Q1, 28% of investors are planning to target CTAs over the next 12 months, as Sam Monfared, research insights at Preqin, comments: "While hedge funds have continued their strong positive momentum in Q1, the industry has experienced a challenging quarter.

> "Optimism has certainly returned to the industry with recent positive capital inflows being a strong indication of such

"The influx of retail money into equities, along with the fear of inflation and higher rates, rattled the markets. The additional volatility created opportunities for hedge fund managers, and many benefited from the sharp moves in the market."

Looking ahead, Preqin expects that inflation is likely to remain a hot topic among investors in Q2, as more stimulus money flows into global markets. Economists are closely tracking producer price indices (PPIs) and consumer price indices (CPIs) globally, as any increase in interest rates could potentially impact valuations if earnings do not catch up with the interest rate moves.

Preqin anticipates that this could lead to significant rotations in portfolios and create volatility in the markets – which would largely be welcomed by hedge fund managers.

"Despite all these challenges, optimism has certainly returned to the industry with recent positive capital inflows being a strong indication of such," Monfared adds. "In short, 2021 is shaping up to be a great year for hedge funds."

Comparisons

While hedge funds appear to still be performing well after negotiating the impacts of the pandemic, as well as any potential widespread fallout from that hugely reported GameStop frenzy, how do they compare to their alternatives counterparts?

McKinsey's Private Markets Annual Review, published in April, indicated that private equity has followed a similar pattern to hedge funds, brushing off external factors and continuing to perform well, to the extent it is outpacing other private markets asset classes, and most measures of comparable public market performance. McKinsey suggested that investors appear to have a "stronger risk appetite" than they did a decade ago.

And this has been demonstrated in reports of renewed appetite for

> 64% of asset owners are expecting that ESG integration will be positively associated with hedge fund outperformance

private equity exposure, as well as a general increase in risk appetite among insurers. One case from Q1 is German company Talanx, which has benefitted from private equity gains of €88m in reinsurance and industrial lines. Another example is Finnish insurer Varma, which has just recorded the best quarterly investment result in the company's history, affected in particular by the strong performance of both listed and private equities, as well as hedge funds.

Head of Allianz Insurance Asset Management at Allianz Global Investors, Edouard Jozan, states that insurers in general are always searching for such alternative solutions, with real world impact and tangible underlying assets.

Jozan tells *Insurance Asset Management*: "AllianzGI's experience working with insurers is that they predominantly search for alternative solutions with tangible underlying assets like infrastructure, renewables or private companies, contributing to the financing of the real economy."

According to the National Association of Insurance Commissioners (NAIC), US insurance companies are continuing to seek more attractive and higher yields in relatively illiquid investments, such as private equity and hedge funds, in the currently prolonged low interest rate environment.

The largest asset classes reported on Schedule BA include hedge funds and private equity, as well as real estate, and despite suggesting that Schedule BA assets do not represent a significant, or core, investment for US insurers, the NAIC still states that these assets have shown "significant growth" in recent years. Figures show that the share of Schedule BA assets in the insurance industry's portfolio increased from 5.8% at the end 2019, to 6.1% at the end of 2020.

"These solutions support an innovative diversification of their long-term asset allocations, while being selective in the asset classes and regions they invest in, to generate additional returns and social and environmental impacts in line with their client objectives," Jozan adds.

For hedge funds and other alternatives to grow their share of the market, Jozan highlights a key challenge among clients investing within the alternative sector, which is ensuring that environmental, social and governance (ESG) issues are being correctly addressed.

A study published in April conducted by bfinance found that the hedge fund industry is "lagging its peers" when it comes to integrating ESG investment factors. Out of 256 investors surveyed, only 7% – and 13% of large investors with more than $25bn in AUM – reported that their hedge fund and liquid alternatives managers currently offer "high integration" of ESG principles in their investment processes. The figures were revealed to be lower in comparison to other asset classes.

This study also found that over the next 20 years, 64% of asset owners are expecting that ESG integration will be positively associated with hedge fund outperformance. This compares to 88% in equities, 85% in private equity and real assets (real estate, infrastructure) and 80% in bonds.

ESG and ARP

bfinance stated that when hedge fund firms, as an industry, decide to embrace ESG integration and move to meet investor demand, it is expecting the transition to "happen swiftly", and that the COVID crisis will not stall that progress, but rather highlight the need for managers to "think anew about future risks and opportunities

in a changed world". So, could ESG integration be a factor that hinders future investment into hedge funds from the insurance space?

bfinance director, client consulting – insurance, Neil Holmes, tells Insurance Asset Management: "Hedge funds have not been a natural go-to for insurers due to their regulatory capital-consumptive nature, and perceived lack of look-through.

"However, a number of clients have approached hedge funds and liquid alternatives as a good diversifier and non-correlated asset away from traditional asset classes."

bfinance has also carried out Alternative Risk Premia (ARP) searches for insurers over recent years which were deemed more 'insurance-friendly', but Holmes reveals that 2020 was one of the worst years on record for performance in this particular asset class.

"Equity value had already been selling off for a long time before COVID and was in its longest and deepest drawdown prior to COVID exacerbating this further," he adds. "This then lack of confidence showed itself in bfinance's Asset Owners' Survey results in July 2020 noting 48% of hedge fund investors and 64% of ARP investors being dissatisfied with the asset classes strategies' performance. Survey respondents were across a number of institutional investor types, a significant proportion being insurers."

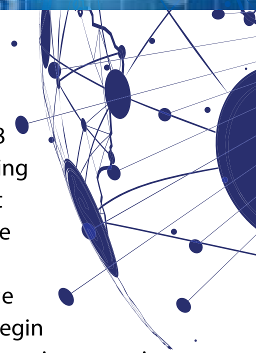
However, bfinance still believes that ARP can still be useful as a diversifier using non-traditional techniques and allow an insurer access to different return streams, uncorrelated to core assets and improve risk-adjusted returns.

"Hedge funds themselves saw a wide dispersion of manager returns, both within and between strategies as a result of the COVID disruption," says Holmes. "The sheer speed of market dislocation in March meant all but the fastest trading-oriented strategies were effectively passengers through the turbulence.

"A number of high-profile names produced unexpected losses and failed to demonstrate the expected diversification behaviour. Eventually, hedge funds did relatively well overall as an asset class in 2020 with the bulk of good performance in Q4."

> "A number of clients have approached hedge funds and liquid alternatives as a good diversifier and non-correlated asset away from traditional asset classes

The message from the insurance industry appears to be that the hedge fund asset class has somewhat shown resilience in the face of several external factors over the past 18 months, to now be sitting in a strong place, albeit relatively. The challenge of ESG integration notwithstanding, hedge funds may yet slowly begin to occupy a small but growing space in the minds of insurance companies.



"In Q4 2020, we have seen a pick-up in investor appetite for hedge funds, and in 2021 both hedge funds and ARP have had very strong starts, Q1 2021 being one of the best quarters on record for hedge funds," Holmes adds.

"Hedge fund and ARP strategies remain a challenge for less well regulatory-capitalised insurers, and whilst such capital charges will remain high, demand is likely to stay subdued. However, there is such a huge range of potential idiosyncratic options, that insurers can view this as a valid option to explore."

> Global green bond issuance could rise by more than 50% to somewhere between $500bn and $550bn in 2021

Market commentary

Green bonds

Written by **Michael Griffiths**

Global green bond issuance could rise by more than 50% to somewhere between $500bn and $550bn in 2021, following a robust first quarter of strong demand, sustained low yields and supportive government policies.

This includes the Joe Biden administration's clean-energy focus, as well as China's updated green bond principles that are driving growth. According to a new report published by *Bloomberg Intelligence (BI)*, net zero emissions targets could accelerate green bond issuance from the two countries this year.

The first quarter saw green bond supply total around $152bn, with governments contributing about $49bn, and financials close to $46bn. BI stated that if this growth trend extends, the tally may exceed $500bn this year by rising over 50% compared to 2020. This total for Q1 was the highest for 10 years, with every corporate sector except communications and consumer staples showing quarter-on-quarter growth.

Even March alone saw more than $74bn in green bond deals, with governmental entities dominating issuance including Italy, France, China Development Bank, German state bank KfW and the European Investment Bank.

BI ESG analyst, Simone Andrews, suggested that US dollar green bond issuance could accelerate under the Biden administration in 2021, as the US President's $2.25trn infrastructure plan may speed up American green capital spending.

"Biden is set to rejoin the Paris Climate Agreement targeting net zero emissions by 2050, which would mean heavy investments in infrastructure, transit, the power sector and green buildings, requiring green bond financing," Andrews said.

"Euro-denominated green debt represented about half of green bond sales in Q1, followed by US dollar sales of 21%. The US green bond supply totalled about $21bn at Q1's end, about a 100% increase from a year earlier."

Around $32bn, or 45% of China's green debt, is to mature this year, leaving it with ample room for net new issuance of Yuan-denominated bonds in line with the nation's pledge to be carbon neutral by 2060, BI also stated.

However, Andrews warned that unless new issuance picks up, it could create an undersupply of emerging market green debt.

"The supply of Chinese green bonds plunged to $13.8bn in in 2020, or a 49% decline compared to the prior year, as borrowers focused on working capital needs given the pandemic" Andrews added.

A lack of standardised criteria by those who verify green-labelled bonds may lead to heightened concerns of "greenwashing", BI has also warned, which could weaken investor confidence.

While 89% of green corporate and sovereign debt issued in Q1 was verified by an external provider, there are growing concerns that despite the "green" marketing, not all proceeds will go towards environmental projects, and that the issuers themselves aren't actually reducing their environmental footprints over time.

According to Refinitiv Lipper data, global equity funds attracted $12.9bn worth of inflows

Market commentary

Global Equity Funds

Written by **Michael Griffiths**

Global equity funds attracted massive inflows of investment in the week ending Wednesday 5 May, boosted by strong corporate earnings and rising hopes of a faster global economic recovery.

Cyclical sectors led the inflows as more industries reopened after pandemic lockdowns and consumers started to splurge on discretionary items, although investors continued to sell funds that invest in Indian equities due to soaring coronavirus cases and deaths in the country. According to Refinitiv Lipper data, global equity funds attracted $12.9bn worth of inflows, the highest amount in three weeks.

However, Kingswood Group then reported that inflation fears were a catalyst for a retreat in global equities. They were down around 3% by Wednesday 12 May but subsequently recovered some of their losses, to end the week down 1.5% and 2.3% in local currency and sterling terms respectively.

According to Kingswood, worries on this front had already been on the increase, and were given a "shot in the arm" by an unexpectedly large jump in the US Core consumer prices rising by 0.9% in April, their largest increase since 1981. This pushed up the annual gain from 1.6% to 3.0%, while headline inflation hit 4.2%.

Kingswood chief investment officer, Rupert Thompson, said that a pause or correction had been looking "overdue", so the recent weakness was not that unexpected.

"The decline as yet is barely noteworthy," Thompson stated. "It won't even count towards hitting the average tally each year of three pullbacks of 5% or more.

"A spike in inflation in April and May had been anticipated, both on the back of economies opening up again and base effects now the comparison is with the low point last spring. However, the April rise was considerably larger than expected. The trillion dollar question now is whether the spike is just temporary or a sign of things to come."

Kingswood indicated that along with most other mainstream forecasters, it would not be changing its medium-term view on the back of just one data point.

"We still expect US inflation to settle back down to around 2-2.5% next year as these temporary supply-demand imbalances ease and growth subsides from its current high rate," Thompson said. "This would still represent a rise in inflation of over 0.5% from the levels seen in recent years."

Meanwhile, the Refinitiv Lipper data showed that global bond funds obtained inflows worth $17.16bn in the week ending 5 May, which was the biggest in three weeks. On the other hand, investors sold $21.6bn in global money market funds, pointing to a rise in risk appetites. The bond market's reaction to the inflation news was restrained, with 10-year government bond yields increasing only 0.05-0.10% in the US and the UK. Kingswood reported that 10-year Treasury yields remain some 0.15% below their highs in March.

In focus: Laszlo Kovacs

Insurance Asset Management checks in with Vienna Insurance Group Hungary chief investment officer Laszlo Kovacs

WRITTEN BY **ADAM CADLE**

VIENNA INSURANCE GROUP (VIG) has recorded a profit before taxes of €346m for 2020, at the upper end of the announced profit range of €300-350m.

In its latest financial results, VIG said it expects profit before taxes for 2021 to be in the range of €450-500m.

Premium volumes increased to €10.43bn and this is expected to remain stable in 2021. Total investments (including cash and cash equivalents) amounted to €36.6bn as of 31 December 2020, representing a 2% year-on-year increase.

The group had a preliminary regulatory solvency ratio of 235% at the end of 2020. Total exposure to green bonds in 2020 was €238m.

VIG has also announced it has successfully placed sustainability senior notes with an aggregate principal amount of €500m with institutional investors in Austria and abroad.

The focus is on expanding investments in socially and ecologically sustainable projects and is in line with the group's long-term capital planning.

The senior notes have a tenor of 15 years and bear interest at a fixed rate of 1.00% per annum. The issue price was set at 99.282% of the nominal amount. Admission of the sustainability notes to the official trading on the Vienna Stock Exchange has been applied for.

Q Could you provide an overview of VIG and your day-to-day role?

I am chief investment officer for the Hungarian operations of Vienna Insurance Group, leading the investment team of 11 persons. We manage insurance assets including unit linked life insurance, which makes the majority of the assets. We are one of the largest providers of unit linked life insurance in Hungary that leads the way in the CEE region in this regard. Beside my role in asset management I am also responsible for the participation management which includes day-to-day management of the affiliated companies.

Q How has the firm adapted to COVID-19 in terms of its investment thinking and direction within the portfolios you manage?

COVID-19 brought a non expected aspect into the asset management world: leaning towards true long term investing by our clients. The length of lockdowns and the fear from loss of

VIENNA INSURANCE GROUP (VIG) has issued an update to its coal policy, following a report exposing its insurance of coal power plants in the Czech Republic and other EU countries.

VIG stated: "If no credible exit plan can be presented, the insurance contract must be terminated as soon as possible. This also applies to the reinsurance business, where we can directly influence the conditions as a leading reinsurer."

For its direct investments, VIG said there will be no new direct investments into companies with more than 30% share of sales from thermal coal mining and/or which produce yearly more than 20 million tonnes of thermal coal and/or which generate more than 30% of their total power generation from thermal coal and/or which generate yearly more than 10 GW energy out of thermal coal.

Inappropriate existing investments will be reduced significantly by more than 50% until end of 2025 respectively will be eliminated completely until end of 2035 at the latest. VIG said it will implement an investment strategy to consciously increase the share of green investments (e.g. renewable energies, green bonds, environmental friendly construction methods, renovation of existing buildings of non-profit societies).

We started reshaping our client portfolios two years ago towards ESG and by the end of 2020, 20-25% of most of the funds consisted of ESG assets

security showed more risk taking by lengthening their investment duration and buying more equities beside higher premium payments.

Q What was your biggest achievement in your role during 2020?

In 2020 I got a reorganisation role in one of the affiliated companies operating in patient service organising which then succeeded to reach excellent operational levels in a few months. Beside that I helped develop a new unit linked life insurance product with an automated model portfolio investment feature that helped us to return as one of the leading life insurers on the market.

Q What do you see as being the biggest challenges for VIG and in general European insurers in 2021?

The biggest challenge I think will be to manage the ketchup dose effect, as daily life slowly turns back to normal and clients start spending instead of saving while the monthly mortgage payments also start ticking again, all drying out the insurance savings market.

Q Could you explain your focus on ESG?

We started reshaping our client portfolios two years ago towards ESG and by the end of 2020, 20-25% of most of the funds consisted of ESG assets. These portfolios received a true boost from this step as the popularity of these emerging asset classes were up. At the beginning of this year we also introduced a 100% ESG fund that quickly gathered huge attention

Photo by: wPavel Kapysh / Shutterstock.com

Photo by: Robson90 / Shutterstock.com

based on our continuous campaign throughout 2020.

Q What are your main aims over the coming years for yourself as chief investment officer?
Keeping up with the market competition in unit linked life insurance and by that also helping to grow the assets for other CEE VIG insurance entities as well.

Q Away from the day-to-day role what do you do to relax?
I am a true soccer fan and try to follow all games and news available about my favourite teams. I also like baking and cooking which is much appreciated by my three daughters during the week, not only at the weekends.

> **I am a true soccer fan and try to follow all games and news available about my favourite teams**

VIENNA INSURANCE GROUP has joined the United Nations Global Compact – the world's largest corporate responsibility and sustainability initiative.

In doing so, VIG has made a commitment to uphold the universal Ten Principles of the UN Global Compact, which relate to the environment, labour, human rights and anti-corruption – areas in which the group is already implementing numerous measures.

The group is thus one of the more than 13,000 companies worldwide that have joined this initiative to date.

VIG is also committed to the UN Sustainable Development Goals (SDGs) and work to achieve them within its sphere of influence. As a participant in the UN Global Compact, the group will also submit an annual Communication on Progress (COP) outlining the action taken during the year to implement the Ten Principles and the SDGs.

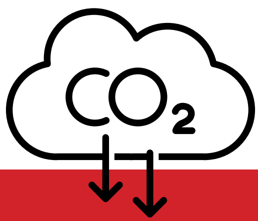
The SDGs have been integrated into the VIG's sustainability reporting since 2019.

"We see the greatest potential for VIG to participate in achieving the United Nations' 17 SDGs in the following four goals: Good Health and Well-being, Climate Action, Sustainable Cities and Communities, and Gender Equality," VIG CEO Elisabeth Stadler explained.

"In future it will be even more important for us to tailor our investment strategy to meet social and ecological criteria and to offer products with environmental value-added. We feel that we have a duty to protect what will matter even more in tomorrow's world: sustainable renewable energy, liveable environments that support resource conservation, and social cohesion. The current pandemic has underlined just how important the latter has become," Stadler added.

A better future

Insurance Asset Management looks at the key sustainable/impact investment developments over recent months



1 Talanx Group (Talanx) is aiming to reduce CO2 intensity in its liquid investment portfolio by 30% by 2025, it has announced. In its sixth sustainability report, Talanx said investments in infrastructure and renewable energies are to be expanded to a volume of €5bn. It has already invested around €3.7bn in infrastructure, a good half of which is in wind power plants. Talanx creates transparency in its investments through membership in the "Principles for Responsible Investment (PRI)" investor initiative. It has also set itself a far-reaching goal for insurance technology and intends to phase out business models based on coal, oil and tar sands by 2038.

2 Arch Capital has confirmed it has not and will not issue any insurance policies covering the Adani Carmichael coal mine. The coalmine is expected to produce eight to ten million tonnes of thermal coal annually. Campaign groups, including the Stop Adani Movement, have been calling on insurers and reinsurers to distance themselves from the project. Arch Capital has approximately $15.8bn in capital and provides insurance, reinsurance and mortgage insurance on a worldwide basis through its wholly owned subsidiaries.

3 New York Life has announced a $1bn impact investment initiative with the aim to address the racial wealth gap by investing in underserved and undercapitalised communities over the next three years with a focus on supporting small businesses, affordable housing, and community development. The company said it will partner with diverse asset managers, federally chartered community development financial institutions and other mission-driven organisations to amplify their efforts on the ground. "The societal events of the past year have stirred an urgency to address America's racial disparities, which the COVID-19 pandemic has only made more glaring. Now, more than ever, is the right time to make impact investments that drive change," New York Life chief investment officer Tony Malloy said.

4 Travelers has announced its commitment to become carbon neutral across its owned operations by 2030. The pledge is a key component of Travelers' ongoing and broader sustainability strategy. The company said it has made significant progress in reducing its carbon footprint, cutting Scope 1 and 2 emissions by more than 40% between 2011 and 2020. Over the next decade, Travelers will achieve carbon neutrality by reducing or offsetting an additional 50,000 metric tons of carbon dioxide – the equivalent of eliminating the impact of about 125 million vehicle miles.

6 MassMutual will transition both its portfolio and operations to net zero, advancing a decarbonised economy. The company's climate change actions will benefit its policyowners, employees, communities and the economy as a whole, while helping ensure its future strength. MassMutual believes that a sustainable future requires immediate and collaborative action to create a path forward.

These commitments, which require abating greenhouse gases added to the atmosphere and balancing emissions output, include:

- Net Zero operations by 2030: Achieving net zero greenhouse gas (GHG) emissions in MassMutual's operations by 2030 by reducing emissions, purchasing renewable energy, and removing the remaining footprint through credible offsets; and,
- Net Zero investment portfolio by 2050:Transitioning to net zero GHG emissions in MassMutual's investment portfolio1 by 2050 through responsible investment and stakeholder collaboration, making MassMutual the first US-based mutual insurance company to make this pledge.

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7 Länsförsäkringar's investments in green, social and thematic (sustainability-oriented) bonds on behalf of customers increased by approximately SEK 7.5bn in 2020. Investments at the turn of the year amounted to more than SEK 17bn, which corresponds to more than 13% of assets under management in institutional life and insurance portfolios. Of the approximately SEK 17bn in sustainability-oriented bonds, Länsförsäkringar Liv's investments accounted for approximately SEK 14.5bn, which corresponds to 14% of the life portfolios' capital. The build-up in 2020 was possible thanks to a focus on direct investment in the primary market and a close dialogue with the issuers of bonds (issuers), which was of particular importance during the introduction of the COVID-19 pandemic. Together with industry colleagues, capital was mobilised and investments were made in socially oriented bonds with the aim of mitigating the health and economic effects of the pandemic, both locally and globally.

5 Russell Investments has pledged to manage carbon-neutral portfolios by 2050. The firm is adding roles to its responsible investing team and establishing a global taskforce to develop a net-zero emissions transition plan. This taskforce will set interim targets in collaboration with clients globally and build upon established practices such as the firm's comprehensive manager research process, which already features ESG scores for managers. The taskforce will also focus on the firm's robust active ownership programme with environmental stewardship and climate risk reporting as key engagement pillars. In addition, taskforce members will collaborate with other firms aligned with the Net Zero Asset Managers Initiative to help develop best practice industry frameworks.

8 Willis Towers Watson Investments is targeting net zero greenhouse gas emissions by 2050 at the latest, with at least a 50% reduction by 2030, in its fully discretionary delegated investment portfolios. Its global chief investment officer Craig Baker said: "Climate change, and a just transition to net zero greenhouse gas emissions, is a systemic and urgent global challenge. We believe that working to achieve net zero by 2050 in our discretionary portfolios is completely consistent with the financial goals we have been given by our clients as climate change has the potential to impact returns across multiple asset classes. We have already embedded this in our investment process and ultimately in the portfolios we are managing and stewarding. Being strategically ahead of a net zero transition will, in our opinion, significantly improve risk-adjusted returns for our clients. This will come from two sources – 'better beta' due to more effective stewardship and 'alpha' as the mispricing of climate issues is resolved."

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9 Varma has invested €200m in the sustainable ETF by the global asset management firm BlackRock. Through its investment, Varma's intention is to support companies in lowering their carbon emissions and to reduce the carbon footprint of its own investments. The BlackRock U.S. Carbon Transition Readiness ETF invests in large- and mid-capitalisation US companies that may be better positioned to benefit from the transition to a low-carbon economy. The ETF's benchmark is the Russell 1000 index, which represents the 1,000 top companies ranked by market value in the US. Along with lowering carbon emissions, the ETF focuses on sustainability criteria related to the environment, social issues and good governance.

10 BlackRock Real Assets has successfully achieved a US$4.8bn final close of Global Renewable Power Fund III ("GRP III" or the "Fund") with commitments from over 100 institutional investors, including leading public and private pension funds, insurance companies, endowments, foundations and family offices from over 18 countries globally. GRP III invests in global climate infrastructure assets, primarily in renewable power generation, across Americas, Europe and Asia. GRP III seeks to deliver attractive risk-adjusted returns with positive and measurable environmental and social impact by investing across the spectrum of renewable power and supporting infrastructure globally, including energy storage and distribution and electrified transport.

> Being strategically ahead of a net zero transition will, in our opinion, significantly improve risk-adjusted returns for our clients

11 Iberdrola and MAPFRE are collaborating closely in the energy area having signed a strategic alliance to make joint investments in renewable energies in Spain. The utility and the insurance company have set up a co-investment vehicle to achieve their goals, using 230 MW of green projects, both wind and photovoltaic, from the energy utility's portfolio. The agreement foresees adding more operating assets, as well as new renewable energy development projects of the energy company's portfolio, reaching 1,000 MW.

12 Folksam Group has published new climate targets for 2025 for its investment portfolios, where the climate footprint from equities, corporate bonds and real estate will be reduced by 29%. The emissions target will primarily be achieved by influencing the companies in which the Folksam Group has invested in reducing its emissions. In addition, the Folksam Group adopts new goals to promote the availability of green investments. By 2025, the goal is for at least 50% of the 86 largest emissions in the Folksam Group's investment portfolios to have adopted scientifically based climate targets.

> We will promote business style innovations such as remote work and telecommuting, and reduce the use of gasoline and electricity by reducing business travel and office space

13 Tokio Marine Holdings has announced its new initiatives for achieving carbon neutrality for its business activities by 2050 by reducing CO2 emission toward 2030 and by increasing the share of renewable sources in its power consumption. Specifically, it will reduce CO2 emitted from the group's business activities by 60% by FY2030. The share of renewable sources in its power consumption at key business facilities will increase to 100% by FY2030.

14 The Bank of England (BoE) has unveiled plans to make its corporate bond purchase scheme (CBPS) more 'green' as the UK government aims to achieve net zero carbon emissions by 2050.

In a speech given in London, BoE markets executive director Andrew Hauser said the bank is to set targets for the overall emissions of its holdings, as well as investing in green corporate bonds when they are available. It is aimed to be an incentive for investors to do the same.

Although the BoE will not immediately sell-off bonds issued by businesses that have high carbon emissions, such firms will have a mandatory requirement to disclose emissions and must set out a roadmap to reduce them, or risk no longer being eligible for bond purchases.

Photo by: IgorGolovniov / Shutterstock.com

15 MS&AD Insurance Group has set a goal of net zero CO2 emissions by FY 2050 to resolve the global risk of climate change. In order to achieve the goal, it also set 2030 interim targets for CO2 emission reduction and renewable energy use. A reduction of 50% is targeted for CO2 emissions for FY 2030, and for renewable energy use, a usage ratio of 60% is being targeted for the same period.

"We will promote business style innovations such as remote work and telecommuting, and reduce the use of gasoline and electricity by reducing business travel and office space," the insurance company stated.

"We will also reduce energy consumption and promote the use of renewable energy by installing state-of-the-art energy-saving equipment in our office buildings, installing solar power generation equipment, replacing company-owned vehicles with fuel-efficient vehicles, and purchasing renewable energy certificates. In addition, we will reduce paper consumption by promoting paperless operations through the Web, such as insurance policy applications, insurance claim procedures, and various announcements."

Sustainable Investment Summit

Our latest virtual conference provided a sustainability update for delegates within the institutional investment space

WRITTEN BY **MICHAEL GRIFFITHS**

Sustainable investing is rapidly becoming a mainstream activity as investors realise the gains from forward facing policies, and the threat of declining performance from more "traditional" safe havens. However, with choice opening up so has the responsibility to select the right forms of sustainable investment, and the issues of risk management and governance are continuing to present challenges.

On 17 March 2021, the Sustainable Investment Summit provided insurance companies as well as pension funds, charities and corporates, with the opportunity to learn about the key issues of this investment space. This year's virtual event saw delegates gather online to discuss the latest trends and topics from across the sustainable investment market, as leading professionals and policymakers shared their thoughts through a series of expert presentations.

Kicking off proceedings, director of shaping sustainable markets at the International Institute for Environment and Development (IIED), Laura Kelly, delivered a keynote speech that explored the "triple crisis" of COVID-19, climate change and biodiversity loss. Kelly discussed the opportunities for public and private investment to support a greener and more inclusive pandemic

recovery.

"There is still a debate if businesses are really serious in actions to improve sustainability and address climate, or if this is simply greenwash, so commitments aren't simply enough," she said.

"One of the ways the IIED is trying to look at the broader picture is market governance mechanisms – rules that shape markets. We've divided these into four categories which are economic incentives, regulatory frameworks, cooperative principles and the newer area emerging around benchmarks to hold companies to account.

"Most investment is still within the US and Europe, but when you look at the sectors that are of interest for renewable energy, basic services, these are the kinds of things that are really important in developing countries too.

"One of the key things is around addressing the risk issues within some of the emerging markets, and encouraging people who want to demonstrate impact in social and environmental terms with their investments into these markets."

Energy

Delegates also heard from Pictet Asset management client portfolio manager, Jennifer Boscardin-Ching, whose talk centred on investing in the energy transition. Boscardin-Ching said that governments worldwide are planning huge programmes to tackle the climate emergency through the transition from fossil fuels to zero-carbon alternatives, which will spur investments into the clean energy industry.

She commented: "A crucial driver is technological innovation which has drastically reduced the cost of environmental and clean technologies, such as renewables or batteries for electric vehicles.

"This has been happening for the last few years. It is due to this technological innovation, and increasing economies of scale, that these technologies and solutions have finally come to parity with more traditional fossil fuel-based technologies, allowing them to compete purely based on economics alone, and not having to rely on government subsidies.

"Take renewables for example, such as solar and wind. While these forms of generation were reliant on subsidies before, today they are in fact in many parts of the world the cheapest way of producing electricity."

On the day, delegates also heard from WindEurope CEO, Giles Dickson, whose session gave an overview of the current wind energy projects across Europe. Dickson told attendees that wind now makes 16% of all the electricity we consume, and he believes that wind energy is going to dominate our energy mix in the future.

"The European Commission say they see wind being one half of all the electricity we consume by 2050," Dickson said. "In nearly all of the EU's scenarios, the total volume of electricity consumption also rises sharply compared to what it is today. That's because we're going to be electrifying so much of our energy mix.

"Today in Europe, electricity is less than one quarter of all the energy we consume, but that's really going to change over the next 30 years. We're going to electrify lots of our transport, heating and industrial processes, and wind energy is going to play a key role in that."

Another session that put forward strongly positive climate targets for the future came from World Gold Council director, John Mulligan, who summarised the climate impact of gold. Mulligan believes the asset has big potential in its mitigation of climate risks.

"We have now quantified gold's carbon footprint," he said. "We have mapped out a high-level pathway to net zero for the industry in alignment with Paris climate targets. We have examined lots of specific actions that will likely contribute to decarbonisation at a scale, and over time periods, that are aligned with climate targets.

"We've also conducted analysis looking at how climate related risks might impact gold's performance as an asset – its risk return profile viewed through a climate lens.

"Gold's carbon footprint is caused almost entirely from the gold mining process, and within that process, the vast majority of emissions are associated with the use of electricity. As decarbonisation of electricity is increasingly accessible, this concentrates the opportunity for gold to move towards carbon neutrality."

The Reporting Landscape

Several speakers for the Summit talked of big future targets across the sustainable investment space, and how masses of data are going to help investors manage their green transitions. A key theme to emerge on the day was the role of reporting, as the space rapidly adapts to meet the need for a global set of standards.

Managing director on the Climate Disclosure Standards Board, Mardi McBrien, provided insight into the current state of play in sustainability reporting, as she highlighted the challenges of meeting the data gap in climate-related reporting.

"When we look at current reporting practice, we still have a long way to go," she commented. "There are commitments with no demonstrable action coming from them, and we're still seeing huge gaps between the narrative and annual reports.

"The capacity for capital markets to affect change really cannot be overstated. As a globe, the allocation of our resources for at least the last century has laid in the hands of the free market, overseeing a period of unprecedented growth. But the cost of this growth has not been accurately calculated, and the allocation of our resources can no longer ignore the finite resources of the planet. This is a daunting challenge, but also represents a huge opportunity."

In another session, CMS senior associate, Thibault Jeakings, and CMS partner, Jae Fassam, looked at how asset screening can play its part.

"Screening can be one of the key tools for pension scheme trustees and pursuing sustainable investment," said Jeakings. "This is especially true given they are likely to have limited involvement in selecting specific investments for their portfolios. Screening can give them a relatively easy route to setting general rules for their investments and imposing sustainability standards, without requiring them to spend disproportionate amounts of their limited time considering the issue.

> **When we look at current reporting practice, we still have a long way to go. There are commitments with no demonstrable action coming from them, and we're still seeing huge gaps between the narrative and annual reports**

"However, it also holds dangers for trustees due to the fiduciary duties to which they are subject, and to risks of complaints from members and employers should they breach those duties."

Fassam added: "It's important to the think about the difference between financial and non-financial factors in this context. For example, when a trustee wants to screen out fossil fuels, and they can make a financial argument based on physical risk in terms of climate to those assets, then that decision is clearly a financial factor. Where it gets trickier is when we think about non-financial factors, and whether they can be used as part of the process in asset screening.

"If there's a good reason to think that members will share the trustee's view on the appropriateness of a non-financial factor, and if taking that non-financial factor into account doesn't pose any risk of significant financial detriment, then there may be a path there for the trustees using that non-financial factor in their investment decision making process."

Future

This theme of differentiating between financial and non-financial factors tied in with several other sessions on the day that explored the growth of ESG integration across the sustainable investment space. Director and lead product strategist for commercialising BlackRock Sustainable Investing's IP in EMEA, Sam Tripuraneni, discussed recent changes in behaviour towards embedding ESG into portfolios.

"We believe that climate risk and sustainability risk are investment risk," Tripuraneni told the delegates. "The best opportunity for long-term performance for our clients, particularly those with a multi-decade investment time horizon, is through sustainability integrated portfolio management. While we entered 2020 focused on environmental issues, we've also seen a broadening of focus across E, S and G issues.

"Our investment convictions were activated across our investment platform by expanding our sustainable price set, by embedding ESG integration into all of our strategies – not just those with a sustainable objective – and by bringing more specific focus, and greater transparency to our investment stewardship programme."

In another session, ShareAction chief executive, Catherine Howarth, also spoke about how stewardship of public and private companies can further drive ESG performance in the future.

Howarth said: "The active stewardship of companies allows investors to add value for clients, not only to risk adjusted returns of a portfolio but to the impact adjusted returns also.

"I think the new UK Stewardship Code is not only an illustration of the UK being world class in the area of responsible investment practice, but will help to accelerate the change under way where good responsible investors have strong skills of stewardship. They are using those not just to achieve improvement in the risk adjusted financial returns, but also in the impact adjusted returns for clients and fund members.

"In the next few years, we'll move beyond seeing ESG as about the management of financially material risk, and very much about achieving positive social and environmental impact, many of which ultimately address systemic risk."

As the Summit increasingly turned to what lies in store for the future of the sustainable investment space, senior responsible investment specialist at HSBC Global Asset Management, Sandra Carlisle, delivered a session about how sustainable investment can look beyond public markets and to emerging opportunities in blended finance and natural capital.

"We know that climate risk is going to disproportionately affect emerging economies, or the global south, but we also know that this is where a great source of future return lies," Carlisle commented.

"We're working with a number of multilateral government institutions on building a framework for sustainable infrastructure. The intention is to develop sustainable infrastructure into a very deep and liquid asset class, and enable the scale up of private investment.

"We know that funding gap runs into tens of trillions of dollars. We also know that this is an asset class in the alternative space where there is significant investor appetite, so this is something to keep an eye on for the future."

Carlisle also captured several of the day's key themes, as she spoke of understanding the energy transition and more methods to analyse the future of the sustainable investment space.

"Another future proofing element of sustainable investment is the need to understand how the energy transition, and how carbon and associated climate issues are going to affect investor's portfolios," she added.

"What we have done is partner with a leading academic institution and produced two reports looking at a range of scenarios, and we've looked at the impact of those pathways to a low carbon economy for a global equity and a global credit portfolio.

"We don't have a crystal ball – I wish we did – but we know that broadly there are two ways. One is through technology, the other is through policy and regulation. Those can play out in different ways, and what we've done with this analysis is give investors the opportunity to play out those scenarios in ways that best align with their own views of how we are going to arrive at a net zero 2050 solution that addresses both asset liability expectations, and risk return expectations."

Current ponderings on industry themes

On the Net-Zero Asset Owner Alliance adding 5 new members with $1trn AUM

We welcome the significant commitment this cohort of new asset owner members are making and the example they are setting. We hope they will encourage other investors to act urgently to align their investment portfolios with a 1.5°C scenario and to play their role in meeting the Paris Agreement.

ALLIANCE CHAIR AND MEMBER OF THE BOARD OF ALLIANZ GUENTHER THALLINGER

On insurers' ESG performance on underwriting being consistently poorer than on investment activity

This finding is surprising. One might expect that the types of systemic risks explored in this survey would be an essential part of the analysis that feeds into development and pricing of underwriting products. This does not appear to be the case – instead, insurers' approach to investment is more advanced. One reason for this might be that insurers have been able to learn from other asset owners and asset managers how to incorporate ESG issues into investment decisions and have benefitted from the general mainstreaming of sustainable finance, while the underwriting side requires a much more insurance-centric approach.

SHAREACTION

On the dollar-denominated Asian credit market

Today, the size of the dollar-demoninated Asian credit market is more than US$1.2trn, and further growth in this market is expected. There are now more than four times as many issuers in the market today compared to 2006, whilst the weighting of the top 20 issuers has shrunk from 63.8% to 40.0%, resulting in a far more diversified market, dominated by corporate issuers.

DWS RESEARCH PAPER

On ways to accelerate authorisation for new insurers

ANNA SWEENEY
PRA's executive director for insurance

We have shown through recent decisions that where an application meets our requirements we are capable of taking a decision quickly, with on average the total time taken to reach a decision now standing at seven months. There are also some specific barriers to entry for small start-up insurers in particular. There is potentially more we can do to provide a mobilisation framework to allow these new entrants to build their businesses under a more proportionate set of regulatory requirements, and this is something we are considering as part of the review of Solvency II – allowing greater space for small scale start-up insurers to innovate and bring new products to the market whilst ensuring that policyholders remain properly protected.

On Gallagher paying $3.57bn for Aon-WTW divestments

This agreement demonstrates strong momentum on the path to close our proposed combination with Willis Towers Watson. We've used this time to align our future leadership team around a one-firm culture that will create new opportunities for colleagues, accelerate innovation on behalf of clients and deliver shareholders the long-term value creation they have come to expect from our team.

GREG CASE
Aon's CEO

On ETF holdings in US insurer general accounts surge 18.4% in 2020 to $36.9bn

RAGHU RAMACHANDRAN
S&P Dow Jones Indices head of insurance asset channel chairman of the board of directors

The continued growth in ETF usage by insurance companies comes from both new companies starting to use ETFs, and companies which already use ETFs buying more ETFs. Even though insurers invest mostly in fixed income securities, they had historically invested in equity ETFs. However, in 2020, these companies increased fixed income ETF usage by 52%. I think it is also interesting that in 2020, insurers traded four times the amount of fixed-income ETFs they held at the beginning of the year. So they are using the liquidity of the ETF market to their advantage.

COENRAAD VROLIJK
Allianz Africa regional CEO

On Allianz completing the acquisition of a majority stake in Jubilee General Insurance, Kenya

Alone and together with the recent acquisitions in leading African markets of Nigeria and Morocco, this transaction is a reflection of Allianz's long-term commitment to Africa and fits with our ambition to gain leadership positions in key markets in the continent.

On Standard Life Aberdeen rebranding as Abrdn

It is a highly-differentiated brand that will create unity across the business, replacing five different brand names that have each been operating independently. Our new name reflects the clarity of focus that the leadership team are bringing to the business as we seek to deliver sustainable growth.

STEPHEN BIRD
Chief Executive

INSURE OUR FUTURE LETTER TO EC

On investments in fossil fuel assets

Investments in fossil fuel assets should not be eligible for the Matching Adjustment under SII. In the face of a potentially unmanageable climate crisis, insurance companies need to expand and accelerate their actions to support the transition from fossil fuels to renewable energy. And more must be done at the regulatory level to ensure that the (re)insurance sector is resilient to climate change and that it plays its role in a just transition. Regulation of the (re) insurance sector appears to have often relied heavily on input from the sector. We hope that going forward the voice of civil society organisations will be better heard in this important space.