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Establishing and Managing Insurer Investment Strategies

The changing regulatory landscape and current market environment are creating challenges for the establishment and management of insurers' investment strategies, including: understanding the impact of investment strategy on regulatory capital requirements, identifying new investment strategies to enhance yield, accessing alternative or illiquid assets, and designing a framework for more integrated modeling of assets and liabilities. Moody's Analytics scenario modeling solutions are designed to support flexible asset and liability projection, and the need to align insurers' investment strategies with capital management objectives.

Aligning investment strategy with capital management objectives

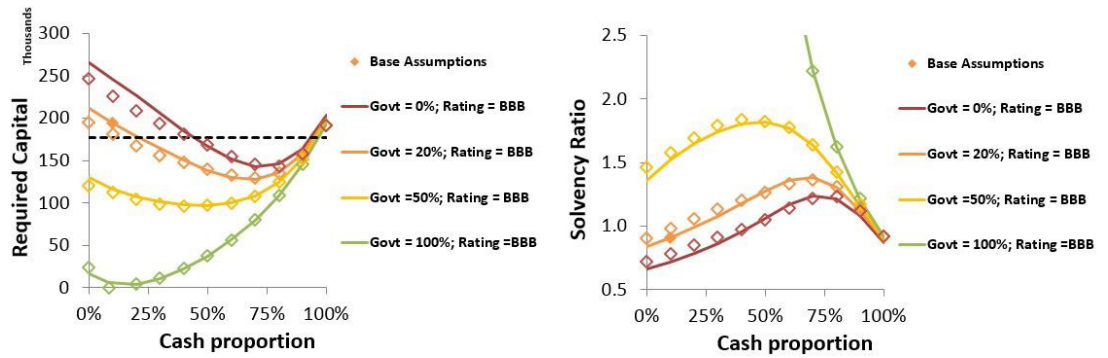
In appraising different investment strategies, insurers must consider the joint objectives of managing capital requirements and risk tolerance, while also maximizing asset returns or earnings generated by their business. Investment objectives are being stated in terms of capital and balance sheet outcomes:

- » Increase asset returns, while maintaining or reducing capital requirements, for example Solvency II SCR.
- » Increase projected earnings, while maintaining or reducing the volatility of projected SCR over the business planning cycle.
- » Reduce SCR and/or reduce projected SCR volatility over the business planning cycle, while maintaining or increasing asset returns.

Traditional return-based portfolio risk models are not capable of addressing these complex path-dependent asset liability modeling (ALM) problems. Establishing the right strategy, and communicating the benefits or risks in that strategy to different business stakeholders, requires a forward-looking scenario-based risk model that simulates the behavior of assets and liabilities over the required time horizon.

Moody's Analytics scenario modeling solutions simulate realistic asset distributions over a range of time horizons, asset classes, and economies, incorporating our extensive economic and capital market research.

FIGURE 1: PROJECTED CAPITAL REQUIREMENTS AND SOLVENCY RATIOS UNDER DIFFERENT ASSET ALLOCATIONS



Asset allocation challenges for insurers

Due to their complexity, the valuation and projection of insurance liabilities typically requires a scenario-based approach, using sophisticated stochastic models of economic risks, combined with a detailed ALM model of the insurance business. Strategic asset allocations must reflect current market prices, and economic state, along with an economically coherent representation of how markets might evolve in the future. Enterprise actuarial valuation systems built for financial reporting and pricing are too cumbersome to support ongoing investment planning and strategic asset allocation activities.

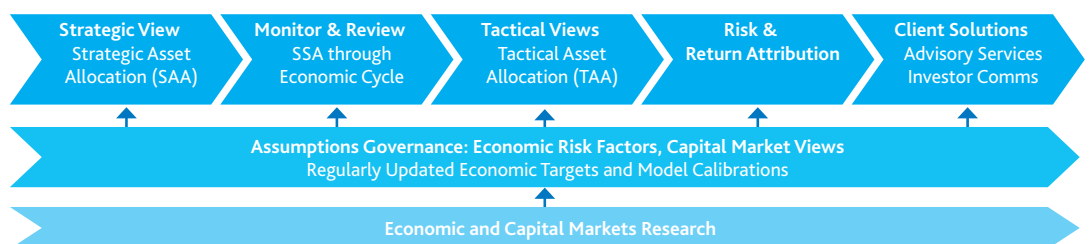
Moody's Analytics bring these requirements together in a robust framework for asset allocation and insurance ALM which addresses:

- » Award-winning scenario modeling solutions, suitable for projecting assets and liabilities over a range of business planning horizons.
- » Efficient methods for calculating and projecting insurance liabilities and capital.
- » Calibration methods and tools to align modeling framework to economic views and capital market assumptions.
- » Research and technical insight on methods for capital management and portfolio optimization.
- » Governance framework for developing and managing assumptions and views.

Economic Modeling - Assumptions Governance

The economic and capital market assumptions are a core element of the asset and liability modeling challenge. Insurers must understand and validate all the assumptions that influence the choice of their asset and liability risk management strategy. These assumptions must be applied consistently across different business functions, markets, and products lines.

FIGURE 2: MOODY'S ANALYTICS FRAMEWORK FOR ASSET ALLOCATION AND INSURANCE ALM



Our "own views" calibration tools enable clients to align risk factor and asset scenario projections with their house views for important economic and capital market variables. However, we recognise that a client's own views might cover only a subset of all the variables and risk factors impacting their assets and liabilities. Moody's Analytics fully justified and documented "best views" assumptions provide a robust and objective baseline which can be aligned to the client's own views.

Our scenario modeling framework ensures that clients can maintain consistent assumptions, aligned with current market prices, and extend them to cover all economies, risk factors, asset classes, and time horizons relevant to their assets, liabilities, and planning horizon.

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