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BlackRock

Navigating through uncertainty

A new playbook for insurers



12th

Annual Global Insurance Report

378

Senior executives surveyed

27

Markets

US\$29T

Assets under management

Navigating this report

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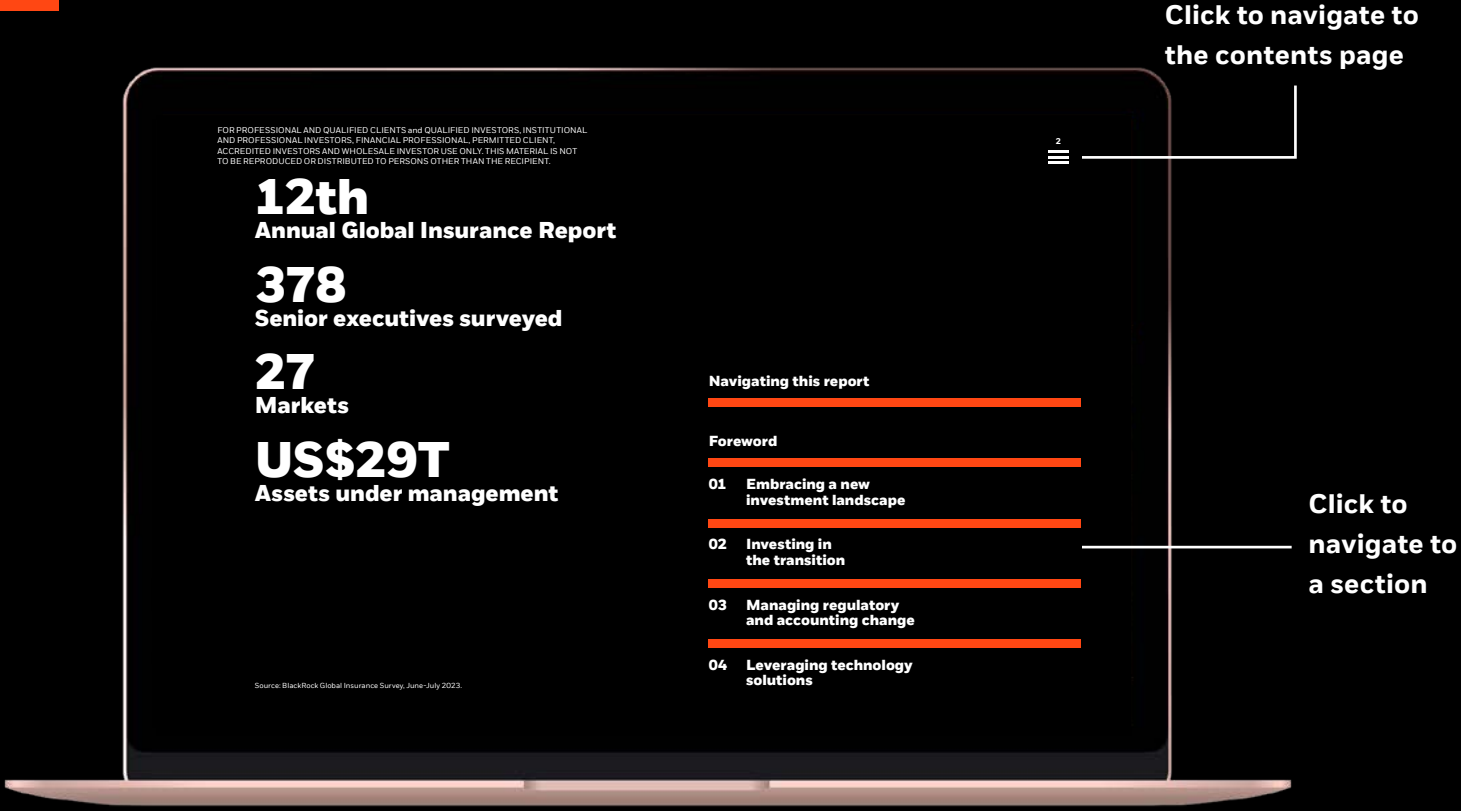
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Foreword



Mark Erickson

Global Head of
BlackRock's Financial
Institutions Group

This year's Global Insurance Report comes in the second post-Covid year, amid five structural mega forces affecting the macro outlook and examined more in depth in BlackRock Investment Institute's 2023 Midyear Outlook: the aging population; the transition to a low-carbon economy; global fragmentation; the changing roles of banks and non-bank financial institutions; and artificial intelligence and digital disruption. These factors, coupled with upcoming changes to insurance regulatory and accounting regimes, create new challenges and opportunities for Chief Investment Officers and other investors.

Our survey of 378 insurers representing \$29 trillion in assets reflects four key themes in terms of what our clients are doing to navigate the new environment.

1 Embracing a new investment landscape

Recession risk, which was the second-highest investment concern of 2022 at 50%, rose to become the top concern of 2023 at 59%. For the second year in a row, the top economic surprise was inflation dynamics at 71%, followed by market volatility at 56%. In terms of emerging risks, the banking sector at 56% was the greatest

area of concern. In light of this, 60% of respondents have reviewed their strategic asset allocation (SAA), with a bias to flexibility. Within overall fixed income portfolios, the most-cited planned increase to allocations was to government and agency bonds at 51%. Private markets allocations remain limited, with 69% of respondents noting only a 1-6% current allocation, though 89% of respondents expect to opportunistically increase this exposure over the next two years.

2 Investing in the transition

In 2021, 95% of insurers told us climate risk would impact their portfolio construction; in 2022, 85% said they were likely to commit to specific climate objectives in their investment portfolios; and this year, following significant policy support in major economies, respondents are focusing on implementing these objectives into actual investment opportunities. Some 62% of respondents are focused on clean energy infrastructure, 46% on green real estate, and 42% on core infrastructure. However, challenges to implementation exist, and 54% cited market volatility as the biggest hurdle.

3 Managing regulatory and accounting changes

Regulatory change is happening globally. The implementation of risk-based capital (RBC) standards in Asia, Solvency II reforms in Europe, the evolution of Solvency UK, and the National Association of Insurance Commissioners (NAIC)

review of structured securities in the U.S. are influencing investment decision-making. Given these changes, 65% of respondents stated that they will need to reallocate assets and 49% are reviewing risk frameworks and reporting requirements. Accounting changes, notably IFRS 9 on financial investments and IFRS 17 on insurance contracts, are also being implemented. More than 40% of respondents noted that these changes will drive a review of risk frameworks and reporting requirements, a review of SAA, and a need to reallocate assets.

4 Leveraging technology solutions

The use of technology is central to insurers' priorities and intersects with the other themes identified in our report. In terms of prioritizing tech and infrastructure investments, the two top priorities cited were risk management and increased operational efficiency. In terms of how technology is intersecting with SAA, more than 40% sought workflow automation and better integration of data, regulatory capital, and liabilities.

Thank you to everyone who participated in the survey and shared their insights. We hope that this report proves thought provoking and insightful. We look forward to partnering with you on navigating these new mega forces affecting this uncertain macro backdrop and continuing our discussion with you on these key themes.



01 | Embracing a new investment landscape



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In a period of continued geopolitical and macroeconomic uncertainty, our focus will remain on executing a disciplined approach to risk-taking and ALM (asset and liability management) whilst identifying and harvesting investment opportunities for both general account and unit linked portfolios.”

Stephan van Vliet
Group CIO, Zurich Insurance Group

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01 Embracing a new investment landscape

01 Embracing a new investment landscape

Inflation and recession risks persist while new investment opportunities emerge

This year's survey provides further evidence that we are in a new regime of greater macroeconomic and market volatility, shaped by tight monetary policy. Inflation remains front of mind for insurers, with 71% selecting inflation dynamics as the biggest economic surprise for the second year in a row.

In the face of persistently high inflation, central banks have aggressively hiked interest rates in most major economies. This has many respondents worried about the months ahead. Indeed, 59% believe recession risk to be the most serious macro consideration in the next 12-24 months.

After recent failures in the U.S. banking sector, 56% of respondents see the banking sector as the area in which further cracks are most likely to appear. This rises to 77% for North American respondents. In APAC, 55% of respondents cite residential real estate.

The risk of defaults in alternatives funds is also a prominent concern for respondents in EMEA (49%) and APAC (58%). Responses to the survey suggest that while this will not stop the trend of increasing allocations to private markets, insurers may be more selective in their approach.

“Our privates program is expanding, and we have slowed the pace of deployment as managers adjust to the changing liquidity conditions. Quality is always a priority, where proven track record, clear style and strategy, and a long-serving, stable team drive our selection criteria.”

Mark Konyn, Group CIO, AIA

01 Embracing a new investment landscape

Insurers reviewed their strategic asset allocation (SAA)

Insurers have adjusted their SAAs in light of this challenging macroeconomic environment. This year's survey shows that 60% ended up doing so, driven by the need for greater flexibility (44%) and the desire to invest in new asset classes (42%).

Cautiously optimistic

Despite perceived recession risks and liquidity concerns, this year's survey shows no major asset class shifts. In public markets, respondents do not expect material reallocations to public fixed income, despite the significantly higher yields available. In private markets, meanwhile, insurers are showing a bias towards quality. Although broad allocations to private credit and private equity will remain steady and continue to grow, albeit at a slower pace than recent years, allocations to high-grade alternative credit are expected to see the largest increase, with 39% planning to increase allocations, more than in any other broad asset class.

“The aggressive tightening of monetary policy globally has created an environment of heightened volatility and uncertainty. One of the key focus areas of our investment approach is assessing downside protection, which we believe limits the potential for poor investment outcomes resulting from difficult macro conditions. As a result, we believe our portfolio is positioned to capitalize on opportunities arising from market dislocations.”

Cole Charnas, Partner, 26North

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01 Embracing a new investment landscape

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Public fixed income

Allocations to public fixed income continue to be a core part of insurers' SAAs, with 92% planning to maintain or increase their allocations. Within this, 51% plan to increase their allocation to government and agency bonds, which offer higher yields and relatively efficient capital-adjusted returns. In a continuing trend from previous years, 42% plan to increase allocations to green, social, and sustainable bonds.

“With higher book yields available, we have put more emphasis on high-quality interest-bearing investments to fund the guarantees to our customers on a solid and less volatile basis. In doing so, we ensure a certain level of portfolio diversification.”

Alexander Mayer, CFO, W&W Group

01 Embracing a new investment landscape

Private markets

As in our last two surveys, insurers plan to increase allocations to private markets, with 89% of this year's respondents planning to do so over the next two years. While in previous years insurers were looking to allocate across a broad range of assets, the 2023 results show higher conviction from respondents: 60% of insurers are planning to increase allocations to direct lending, and 57% to multi-alternatives. By contrast, they expect to decrease allocations to both real estate debt and equity, as well as to traditional private equity.

“Our invested capital to private markets is still below our strategic target, so we keep allocating new commitments, although at a reduced pace compared with previous years. The dislocations in certain markets offer opportunities for investors like us that can invest through the cycle.”

Francesco Martorana, Group CIO, Assicurazioni Generali

01 Embracing a new investment landscape

For insurers, increasing their allocation to private markets is not without challenges. Rising defaults in alternatives funds was chosen by 45% as the area they believe further financial cracks are most likely to occur. Against this backdrop, insurers are being more selective in their approach as they expand their private markets program.

“We feel middle-market loans being underwritten in the current high-interest rate environment offer a compelling return profile, and that infrastructure has attractive attributes in terms of inflation protection, duration, impact as well as risk return characteristics. We are optimistic that the US Inflation Reduction Act will provide good investment opportunities in the US. We are exploring investment solutions and structures to benefit from those developments.”

Stephan van Vliet, Group CIO, Zurich Insurance Group

“The results of this year’s survey support our belief that direct lending represents a strong investment proposition for insurers. Sixty percent of insurers who responded to the survey agree. Furthermore, attractive pricing and built-in downside protection support increased allocations, even in a recessionary environment.”

James Keenan, CIO and Global Head of Private Debt, BlackRock

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Finding opportunities in a changing investment landscape

James Keenan

CIO and Global Head of Private Debt

Peter Gailliot

Global CIO, Financial Institutions Group

Public Markets

Against a backdrop of tightening monetary policy, economic uncertainty, and market volatility, global growth has remained surprisingly resilient in 2023. While 2022 represented the worst annual performance for global fixed income markets in several decades, the increase in yield across regions created the first opportunity since the Global Financial Crisis (GFC) to mitigate income volatility for years to come. As central banks pulled back from the unprecedented levels of stimulus enacted during the pandemic, financial repression went into reverse. The assets that most directly bore the brunt of this shift in policy were those specifically targeted by central bankers post the GFC, i.e., sovereign bonds. While the mark-to-market drawdown in these assets was extreme, it also provided a rare opportunity for capital-aware investors to put money to work in high-quality, liquid assets at yields that were primarily reserved for high yield and private markets over the prior 15

years. Today, investors can enhance the durability of cash flows and quality of their portfolios without sacrificing income, leaving 35% of survey respondents expecting to increase their allocation to public fixed income over the next 12-24 months, compared with 8% expecting to reduce their allocation.

We agree with survey respondents that the most serious macro consideration remains recession risk. The full effects of monetary policy tightening have yet to be realized, and there's a high likelihood that higher rates, along with elevated levels of inflation and tighter lending standards by the global banking community, will lead to a more pronounced economic slowdown. Despite this negative growth outlook, insurers should look to take advantage of today's elevated yield levels across high-quality spread assets, given the potential reemergence of traditional correlations between growth and the price of government bonds.

Rates

Despite the inversion of the yield curve across many sovereign markets, we are most constructive

on the intermediate part of the rates curve. While investors can maximize yield in the shortest tenors on the curve, there is considerable value in 3-to-10-year tenors where insurers can lock in income for a longer period of time and avoid the potential reinvestment risk during a global easing cycle. Although peak policy-rate forecasts grab much of the headlines, we have been focused instead on the length of time central banks are willing to hold these higher policy levels, and we expect that to remain our focus going into 2024.

Credit

We view credit today less as a source of excess return and more as a source to generate income. Within investment-grade corporates, we are most constructive on Euro and GBP markets, though we expect excess returns to be limited to carry as the stronger starting point for credit fundamentals is likely to be offset by macro headwinds and current valuations. In the U.S., the tightening of global financial conditions will continue to exert pressure on corporate earnings. Multi-decade highs in interest rates are putting pressure on highly levered businesses, which, combined with slowing nominal growth, is likely to

01 BlackRock perspective

drive more defaults and restructurings. Given these dynamics, we favor up-in-quality allocations throughout global credit markets, favoring A-rated debt over BBB-rated debt, investment grade over high yield, and a tilt to higher-quality issuers across emerging markets.

Securitized

As central banks and governments flooded the market with liquidity after the GFC and Covid, we often referred to securitized assets as a whole, given that those massive tailwinds supported assets up and down the capital stack. That is no longer the case today. Spreads across securitized assets moved materially wider in March 2023, following broader concern about regional bank failures and stress in the commercial real estate market. While spreads have since tightened, there is still broad dispersion across the market. Assets that reflect the most value today include broadly syndicated collateralized loan obligations (CLOs), and the non-qualified portion of residential mortgage-backed securities (RMBS). We also find value across traditional and non-traditional segments of the asset-backed securities market, though we remain wary of the subprime consumer

exposure. As regional banks historically issued close to 25% of outstanding commercial real estate loans, the commercial real estate market saw the largest negative impact from March 2023. This added pressure on the pre-existing areas of concern (retail, office dynamics post-Covid) leaves us more cautious on the space. This concern is reflected in our survey as well, as real estate remains one of the largest areas of anticipated net reductions from respondents in the next 12-24 months.

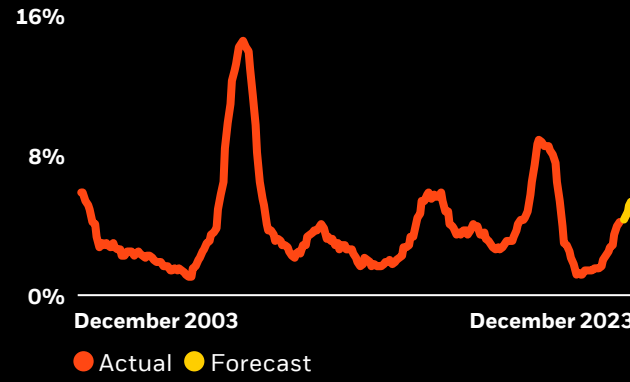
Private Markets

Our base case for the 2023 macro backdrop in the U.S. and Europe remains characterized by a mix of 1) below trend economic growth; 2) persistently elevated services inflation; and 3) a more restrictive monetary policy framework, relative to the past few decades. As a result, corporate borrowers are likely to have to contend with a higher cost of capital for some time. Investors are watching the outlook for defaults and credit losses, with more than a third of respondents considering rising global corporate defaults as the first key macro consideration for their portfolio. For year-end 2023 in the public markets

(leveraged loan and high-yield bond issuers combined), we forecast a trailing 12-month, issuer-weighted U.S. default rate of 5-6%, and 4-4.5% in Europe. These levels would be modestly lower than the pandemic peaks and are well below the highs of the GFC, owing in part to the significant amount of proactive refinancing and liquidity raising in 2020-2021.¹

We continue to expect a year end USD default rate of 5-6%

Trailing 12-month, issuer-weighted default forecasts for the Moody's universe of USD leveraged loan and HY bond issuers (combined).



Source: BlackRock, Moody's. Captures actual data through July 31, 2023, and BlackRock forecasts through year end 2023.

Assumptions, opinions and estimates are provided for illustrative purposes only. They should not be relied upon as recommendations to buy or sell securities. Forecasts of financial market trends that are based on current market conditions constitute our judgment and are subject to change without notice. 1. BlackRock, Moody's.

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Losses in U.S. direct lending remained largely consistent with public high-yield debt and leveraged loan markets in 2022² and could follow the public markets higher this year. However, we see potential for private credit to be less impacted, in part because of the structural seniority of private loans and the covenant protections they come with.

Along with manager selection, diversification remains a cornerstone of portfolio construction, and its relevance and importance have risen exponentially as markets have shifted.

Three-quarters of respondents plan to maintain or increase their allocation to private debt in the next 12- 24 months, an acknowledgment that the addressable market and pricing power are expected to improve following regional bank disruptions. The combination of built-in resilience to losses and attractive pricing upside, as compared with public market debt, captures the benefits of both wider spreads and base-rate increases, and continues to draw investors to the asset class.

Alongside the strong tailwinds in corporate private debt, private infrastructure debt continues to

experience tremendous growth with advances in technology, supportive government policy, an increased rate environment, and energy transition thematics driving strong demand for financing for projects globally. The essential nature of infrastructure assets, many of which are backed by visible and contracted income streams, makes them generally low risk debt investments which are resilient to broad market volatility.

Private real estate debt directly benefits from the current market environment and targets investments with stable current income supported by assets with resilient cash flow and positive demand generators. As traditional lenders retrench, private real estate debt lenders can dictate wider private market spreads at lower loan-to-value ratios. Combined with increased base rates, this drives a compelling risk-adjusted return profile across the capital stack.

Furthermore, the liquidity of private debt fund structures is typically well matched to the duration of the investments (a notable point, given the recent focus on asset-liability mismatches in the bank channel). The structural tailwinds in private debt supply have been met with rising demand, as

borrowers are increasingly drawn to private debt over traditional sources of financing such as banks and the public markets. Borrowers appreciate the certainty of execution offered by private debt (which, unlike the public market, is not reliant upon broader syndication of deals to a wide range of investors), as well as its suitability in a broad range of transactions.

These positive market forces are likely to support a continued increase in private debt deal flow, as well as an increase in the pricing premium versus the public high-yield and leveraged-loan markets. When combined with the stronger downside mitigation we are seeing from increased protections such as maintenance covenants, tighter EBITDA definitions, and limits on debt incurrence, we believe the risk/reward trade-off in private debt is particularly strong right now. Going forward, we believe these factors will help support better underwriting outcomes in private debt and address the challenges of diversification and reliable income generation for insurers.



02 | Investing in the transition

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Our entire program is focused on sustainable outcomes. The prospects of stranded assets and valuation shifts are thematic drivers. Non-sustainable strategies will become riskier over time as investors recalibrate the impact of energy transition and climate change. For long-term investors, the risk/reward assessment remains rooted in sustainable outcomes.”

Mark Kony
Group CIO, AIA



02 Investing in the transition

Sustainability and the low-carbon transition are front and center for insurers

This year’s survey shows that insurers are focused on the investment opportunities linked to the transition to a low-carbon economy. These opportunities are being enhanced by ‘green’ industrial policies, with the U.S., the EU, and China all having recently introduced measures to support the low-carbon transition, including subsidies for emerging technologies.

Investing in the transition

For 62% of respondents to our insurance survey, clean-energy infrastructure is seen as the largest investment opportunity arising from the transition, rising to almost three-quarters in North America. This comes against the backdrop of recent policy developments, such as the Inflation Reduction Act in the U.S. and the Green Deal Industrial Plan in the EU, which have increased the volume and returns of investment to reduce carbon emissions and advance sustainability technology.

Insurers thus utilize transition-focused private markets to meet climate objectives, as well as to drive returns. However, public markets are still seen as a source of opportunity: 37% of respondents see green bonds as an investment opportunity arising from the transition to net zero.

“ESG-themed bonds are a straightforward investment that we are accumulating to meet our sustainability goals. We invest in both public and private ESG-themed bonds, and at times partner with global institutions to issue private ESG-themed bonds that specifically match our sustainability goals.”

Masao Aratani, Director, Deputy President, Representative Executive Officer, the Investment Division, Meiji Yasuda Life Insurance Company

02 Investing in the transition

The challenges of implementing transition strategies in a volatile world

Despite the more supportive policy environment in many major economies, insurers still face challenges in implementing sustainability strategies. For 54% of our respondents, market volatility is one of the biggest hurdles in doing so.

Insurers expect this challenge to persist. Two other key challenges cited by insurers were the uncertainty of generating persistent returns through sustainable investments (43%) and the difficulty of integrating sustainability into their SAA framework (40%). These challenges were felt particularly keenly in North America.

“Insurance companies are critical to provide capital for energy transition, and we have already allocated significant amounts both to equity and debt. It is a secular trend and involves both developed and emerging markets. Discipline is anyhow necessary to assess return and risk: initiatives need to be financially sustainable and not too exposed to regulatory and technological changes.”

Francesco Martorana, Group CIO, Assicurazioni Generali

02 BlackRock perspective

The transition to a low-carbon economy

Jessica Tan

Head of Sustainable and Transition Solutions

David Giordano

Global Head of Climate Infrastructure

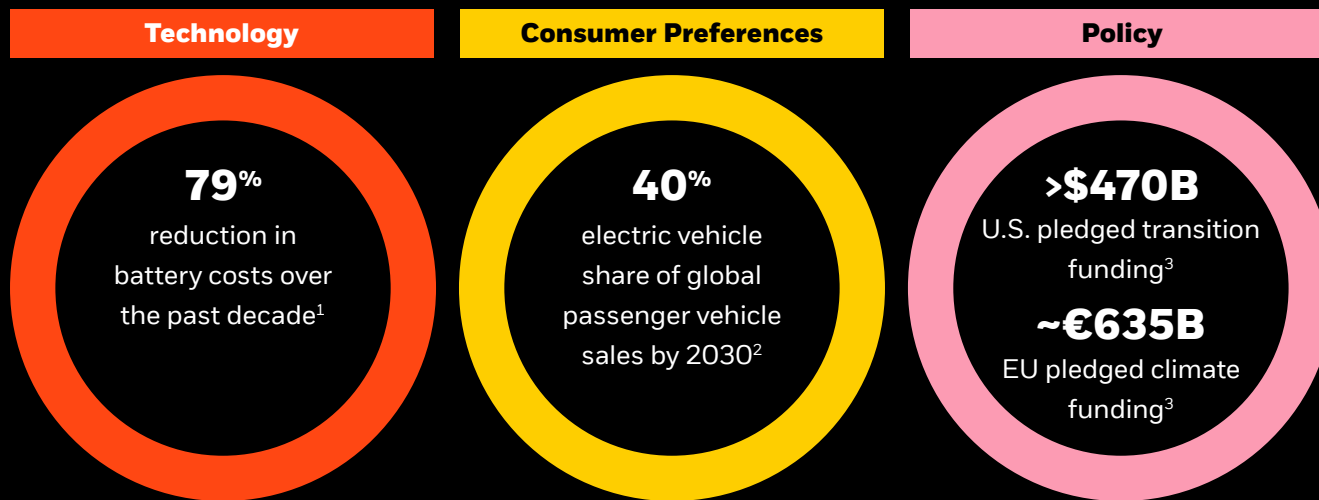
The transition to a low-carbon economy is top of mind for many of BlackRock’s clients and for insurers around the world. In our recent market survey of 200 institutional investors,⁴ 56% said that they plan to increase transition allocations in the next one to three years.⁵ The effects of this transition will create complexity, risk, and opportunity for companies and investors in decades to come—and are already playing out in markets today.

Technological innovation, consumer and investor preferences, and government policies are driving this economic transformation and shift to a low-carbon economy. Physical climate change continues to create financial risk, which is affecting asset prices and insurer liabilities. In 2022, insurers covered \$120 billion for natural catastrophes.⁶

These drivers tend to reinforce one another. As technologies develop and become more advanced, they often become cheaper. This leads to more demand as lower-carbon alternatives become more affordable. Governments, in some cases spurred by increasing physical risk, create incentives for low-carbon technologies, which

lower costs even further. The U.S. Inflation Reduction Act, for example, contains a range of policy measures to spur the transition, including tax incentives, rebates, grants, and loans. These are likely to trigger greater investment in, and demand for, low-carbon energy infrastructure and technology.

Three forces are driving an economic transformation



Creating investment opportunities with different implications for regions and sectors

1. BloombergNEF, Top 10 Energy Storage Trends in 2023. 2. BloombergNEF, Electric Vehicle Outlook 2022. This figure reflects the report’s Economic Transition Scenario. 3. BII, Rocky Mountain Institute, and European Commission, December 2022. 4. BlackRock iResearchServices global survey, sample size n=200, May-June 2023. 5. Global Perspectives on investing in the low-carbon transition, BlackRock September 2023. 6. January 2023 Munich RE.

02 BlackRock perspective

Ultimately, these drivers will help transform the way we make and use energy, move goods and people, and build and reshape the environment.⁷

These trends are reshaping production and consumption—and spurring significant capital investment. The past few years have already seen an increase in capital investments in the energy system and the transition. The International Energy Agency recently estimated that such investment—covering everything from power plants to oil and gas facilities to cooling systems and cars—has increased to around \$2.8 trillion in 2023, up from \$2.2 trillion in the past decade.⁸

The BlackRock Investment Institute Transition Scenario (BIITS) research suggests that continued investment is needed in both low-carbon and high-carbon portions of the energy system to help match supply and demand as the transition unfolds at different speeds across regions and sectors.

The BIITS estimates that investment in the energy system is likely to increase from \$3.5 trillion a year this decade to \$4.5 trillion by the 2040s, equating to an increase of more than \$1 trillion per year in

capex. It expects low-carbon investment to make up to 80% of the total by that time, showing that capital investment in higher-carbon sectors is still relevant now and in the future.⁹ Some higher-carbon investments could face transition risk, but we think this can be managed by prudent planning, including diversification.

We expect adoption of low-carbon energy sources to reach tipping points across regions and sectors when their relative costs fall below those of incumbent sources and when barriers to adoption are low. Sectors such as power and automotives within key regions—mainly in developed markets—are in the “fast lane,” where we expect tipping points in the near term to lead to large-scale decarbonization by mid-century. Carbon-intensive sectors, notably heavy industry and transport, and several sectors in emerging markets are in “slower lanes” because of a higher cost of capital, rapid energy-demand growth, and a larger share of “hard to abate” sectors.

The transition to a low-carbon economy will require replacing today’s operating expenses with new capital, which in turn requires significant upfront financing. We believe that these capital

flows can represent investment opportunities across asset classes, where these shifts have not yet been priced in by markets.

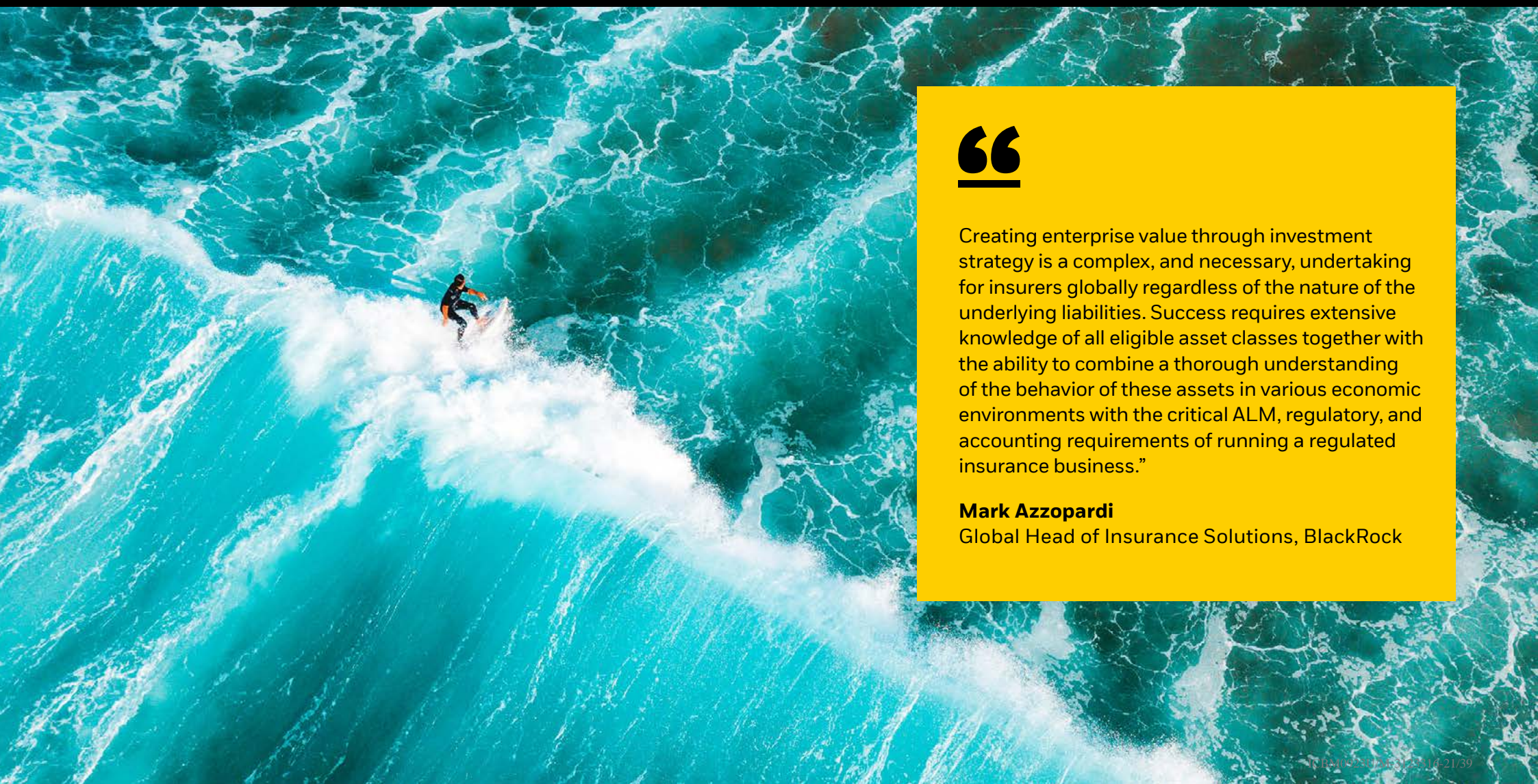
For cost and price discovery to happen, we believe the financial capital needs to be connected to transition opportunities. As noted in the 2023 Global Insurance Report, insurers expect to see low-carbon-transition investment opportunities in clean-energy infrastructure (62%), green real estate (46%), and core infrastructure (42%), among others.

This transition will be a complex process as new profit pools emerge, and existing ones shift between sectors, players, and regions. In our view, the successful investors of the next decade will be those who can navigate that complexity to capture investment opportunities while simultaneously mitigating constantly evolving risks. According to our recent market survey,¹⁰ institutional investors rank strength of sustainable and transition investment research, proprietary deal access, and performance of sustainable and transition solutions as the most important factors in selecting a manager for transition allocation.

7. (1) January 2023 BloombergNEF, Top 10 Energy Storage Trends in 2023 / (2) BloombergNEF, Electric Vehicle Outlook 2022. This figure reflects the report’s Economic Transition Scenario. / (3) December 2022 BII, Rocky Mountain Institute and European Commission. 8. June 2023 IEA Publication. 9. July 2023 BlackRock Investment Institute Transition Scenario (BIITS). 10. [BlackRock iResearchServices global survey](#), sample size n=200, May-June 2023.



03 | Managing regulatory and accounting changes



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Creating enterprise value through investment strategy is a complex, and necessary, undertaking for insurers globally regardless of the nature of the underlying liabilities. Success requires extensive knowledge of all eligible asset classes together with the ability to combine a thorough understanding of the behavior of these assets in various economic environments with the critical ALM, regulatory, and accounting requirements of running a regulated insurance business.”

Mark Azzopardi

Global Head of Insurance Solutions, BlackRock

03 Managing regulatory and accounting changes

Regulatory and accounting change is taking place in many global insurance markets. Many Asian countries are transitioning to a risk-based capital (RBC) framework. The U.S. is reviewing the regulatory treatment of structured products. In EMEA, Solvency UK and Solvency EU are under review. Meanwhile, new accounting standards, specifically IFRS 9 for assets and IFRS 17 for liabilities, will have significant impact in certain regions.

This year's survey shows that these factors are likely to result in changes to risk appetite and asset allocations.

APAC

“In 2025, the new International Capital Standards regulatory framework will start in Japan, changing the capital standard to an economic-value basis. We have worked for several years to shift our asset allocation in various ways to prepare for the transition. For example, we reduced our equity exposure after we looked closely at the surplus on an economic-value basis and evaluated it against risk.”

Masao Aratani, Director, Deputy President, Representative Executive Officer, the Investment Division, Meiji Yasuda Life Insurance Company

03 Managing regulatory and accounting changes

“Changes to regulatory capital requirements are a material development in APAC markets, requiring an evolution in approach across all asset classes to ensure insurers can continue to deliver good stakeholder outcomes. We expect the increased focus on ALM to result in changes to SAAs and underlying portfolio-management approaches.”

Henry Ashworth, Head of Insurance Solutions for APAC, BlackRock

Among APAC respondents, 69% said they would need to reallocate assets because of changing regulations. This figure rises to 80% for respondents based in countries where an RBC regime has not yet been implemented. Meanwhile, half expect the emergence of standardized and enhanced reporting requirements, as currently seen in EMEA and North America.

Although IFRS or the equivalent will be implemented in most markets, APAC insurers expect less change in response to the new accounting standards, with only 44% expecting to reallocate assets as a result.

EMEA

Regulation in EMEA is undergoing meaningful reform. Further, Solvency UK reforms are intended to be fully implemented by the end of 2024, and EU Solvency II reforms are likely to be implemented over 2025 and 2026. In the context of these reforms, 65% of EMEA insurers are looking to reallocate assets and 57% to review their risk appetites or reporting metrics. Amid the implementation of the new IFRS standards from the start of the year, almost half of European insurers stated that they will review their investment risk appetites or reporting metrics as a result.

“The proposed reforms of EU Solvency II regulations could increase capital requirements of EU insurers by around €90 billion, with investment implications including the changing efficiency of public and private fixed income asset classes, the potential need for better duration matching, and the increased attractiveness of equities. Combined with the higher-interest-rate environment, these changes will require insurers to reassess the efficiency of their investment portfolios.”

Viktor Knava, Head of Insurance Solutions for EMEA, BlackRock

03 Managing regulatory and accounting changes

North America

Even though the proposed regulatory changes in the U.S. are more targeted than in EMEA or APAC, insurers are still reporting that these will drive change in their portfolios. The National Association of Insurance Commissioners (NAIC) is expected to modify the capital requirements for CLOs and certain types of private securitizations. Among U.S. respondents, 95% stated that they are either currently invested in or plan to invest in a strategy employing a structured insurance solution. And despite the NAIC review, 50% plan to increase their CLO allocations in the next few years. Overall, the prospect of regulatory change will play at least some part in the reallocation of assets for 62% of insurers. It will have a role in the review of investment risk appetites and SAAs for 62% and 55%, respectively.

“The sheer volume of regulatory proposals is a departure from recent years and is driven by the NAIC’s objective to identify and eliminate regulatory arbitrage. In particular, the NAIC is seeking transparency on complex assets and clear reflection of the associated risks. Meanwhile, the proposed S&P capital framework evolution is expected to drive nuanced changes to allocations without materially impacting the total level of required capital.”

Ann Bryant, Head of Insurance Solutions for North America, BlackRock

In Bermuda, the Bermuda Monetary Authority has issued a consultation paper proposing a series of amendments aimed at enhancing the regulatory regime and bringing it closer to Solvency II in nature. If implemented, the proposals will impact both the ability and the attractiveness of holding higher-risk assets in Bermuda.

03 **BlackRock perspective**

Adapting to a new regulatory and accounting environment

Mark Azzopardi

Global Head of Insurance Solutions

In this year's edition of the Global Insurance Report, 38% of this year's respondents have ranked regulatory developments as one of the three most serious considerations for their firm's investment strategy over the next 12 to 24 months, and 65% indicated that they would need to reallocate assets in response to regulatory and accounting changes. It's easy to see why. Over the past year and a half, the extent and impact of regulatory and accounting developments have increased dramatically.

The U.S. has historically operated as a rules-based regulatory regime, but several initiatives are currently underway as the National Association of Insurance Commissioners (NAIC) and state regulators move towards a more principles-based framework. A common theme underlying these initiatives is the NAIC's goal of increasing investment transparency and capital adequacy within the insurance industry. This includes efforts to eliminate capital arbitrage for securitized and structured products and to reduce reliance on credit ratings from "nationally recognized statistical rating organizations" (NRSROs). The NAIC is also updating its designation categories for RBC to cover CLOs, has made a proposal, has made a proposal to require rated-note feeder funds to be filed with them for capital designations and has adopted a new, and higher, residual-tranche RBC factor, to take effect in 2024 year-end reporting.

In the near term, these changes introduce additional uncertainty and regulatory risk to be considered in an insurer's asset-allocation process, particularly regarding lower-quality CLO allocations and certain structured private investments. In the long term, when the NAIC's approach becomes clearer, there will be potential for greater transparency, certainty, and alignment of the regulatory treatment of investments with the underlying asset risk.

Meanwhile, the Bermuda Monetary Authority's latest consultation papers have proposed enhancements that require more rigorous asset and liability management, governance, validation, stress testing, and reporting for insurers. This should result in strengthened capital and reserving requirements and could impact Bermuda's relative attractiveness as a reinsurance jurisdiction for asset-intensive business.

03 BlackRock perspective

In EMEA, Solvency II is under review in both the EU and the UK. While the EU review covers a broad range of investment topics, the UK review focuses primarily on the Matching Adjustment—a component of the regulations that primarily impacts annuity writers. In both reviews, the risk margin, which is regulatory capital held against unhedgeable risk, is expected to fall and result in a release of capital. A likely consequence of the UK reform is that a broader range of potentially riskier fixed income assets will be both eligible and efficient for backing annuity liabilities.

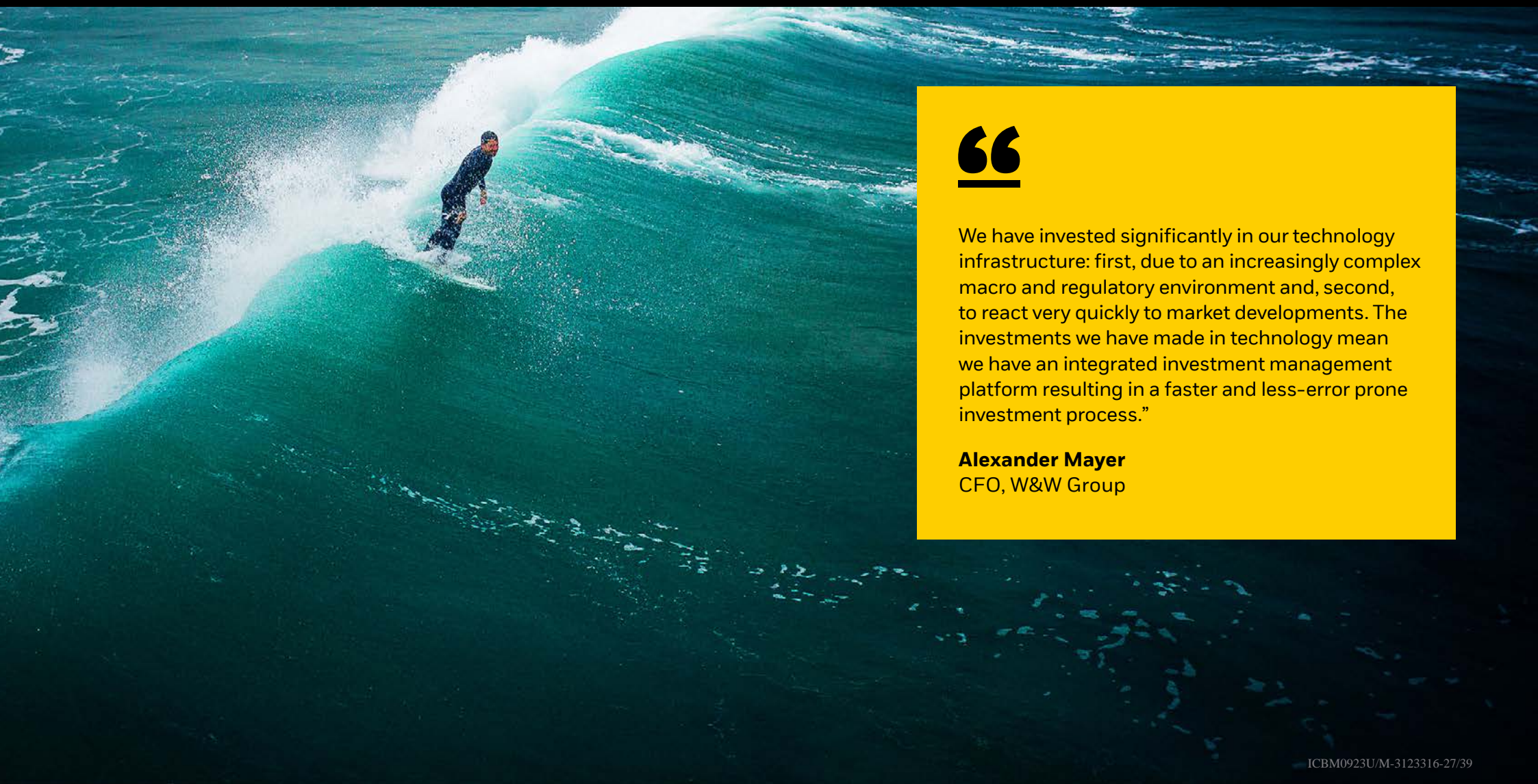
Similarly, insurers across APAC are adapting to the introduction of new principles-based capital frameworks including Hong Kong RBC, Singapore RBC 2 and Insurance Capital Standard (ICS) in Japan, Taiwan, and Korea. These frameworks share many similarities with Solvency II and will introduce risk-based, market-consistent regulation with look-through to the underlying assets. Their introduction is likely to encourage both superior capital adequacy (potentially via de-risking in the first instance) and diversification while also discouraging capital arbitrage by promoting substance over form.

Beyond navigating regulatory change, insurers must also consider developments in rating-agency and accounting frameworks. Recently, S&P Ratings released its updated S&P Insurer Risk-Based Capital Adequacy Methodology. On the accounting front, IFRS 9 and 17 both took effect on January 1 this year and entail significant changes to how listed insurers outside the U.S. present their financial statements. As with the U.S. GAAP Long Duration Targeted Improvements (LDTI) framework, which was also implemented at the start of the year, these have already resulted in insurers reviewing their management of income statement volatility.

These regulatory, accounting, and rating-agency developments all need to be managed proactively, and this explains why, ultimately, 65% of respondents report that they will change their asset mix. Our experience with clients over the past year supports this conclusion. Our client teams and insurance advisory function have seen increasing, and increasingly sophisticated, proactive engagement from clients who are keen to tap into our experience in building and delivering effective insurance investment strategies in all regulatory, accounting, and macroeconomic environments.



04 | Leveraging technology solutions



“

We have invested significantly in our technology infrastructure: first, due to an increasingly complex macro and regulatory environment and, second, to react very quickly to market developments. The investments we have made in technology mean we have an integrated investment management platform resulting in a faster and less-error prone investment process.”

Alexander Mayer
CFO, W&W Group

04 Leveraging technology solutions

Technology’s role in managing risk

Against an increasingly volatile and complex macroeconomic and regulatory backdrop, insurers recognize the importance of investing in technology infrastructure to manage risk, with 47% choosing this as an area they will prioritize. Risk management becomes more relevant with the changing patterns in asset allocation, particularly for insurers growing their exposure to private markets.

For 45% of our respondents, compliance with regulatory needs is a priority for future technology investment. Meanwhile, 43% identified the implementation of regulatory capital integration as the area in which technology can add the most value to the SAA process.

Overall, insurers have a clear focus on using technology to manage the increasing complexity that regulatory change brings.

“ALM is a focus for our firm. We are a large, acquisitive corporation that has significant complexity and infrastructure. We are investing in technology to have more real-time reporting of our exposures so we can make quicker investment decisions and optimize our investment processes on the short end of the curve to take advantage of the rate environment.”

Courtney Mattson, Vice President of Global Enterprise Treasury,
United Health Group

04 Leveraging technology solutions

APAC adapts to RBC regimes

Two-thirds of insurers will need to reallocate assets because of the implementation of RBC regimes. In response, half of APAC respondents stated that they would be prioritizing risk management.

The challenge for insurers is to make significant SAA changes while simultaneously adapting to new regulatory requirements. Technology appears to offer insurers a means of navigating that shift, with the integration of both liabilities and regulatory capital among the top three areas insurers believe technology can add the most value to the evolution of SAAs, both in APAC and globally.

Improving efficiency and cutting costs

Beyond technology's value in managing risk and regulatory change, 47% of respondents cited operational efficiency as a priority for their tech investments. Respondents also highlighted two key technological advances: workflow automation and data integration across the entire insurance platform.

04 BlackRock perspective

The Decision is in the Data

Griff Norquist

U.S. Head of Financial Institutions for the Aladdin Business

Change is everywhere, and it's clear that even the pace of change has gained momentum. Whether it's markets, climate, regulation, or geopolitics, it's easy to surmise there's now more complexity than ever before.

For insurers around the world, change has always been expressed through data: the liabilities therein, risks and opportunities (both inherent or supposed), as well as insights. Data, after all, acts as the raw material for competitive innovation, risk management, and decision-making power.

That decision-making power is, however, dependent on the confidence you have in the data itself—the strength of your Investment Book of Record (IBOR), how it aligns with your Accounting Book of Record (ABOR), and the overarching ability to report.

And while AI has garnered the lion's share of recent headlines, many are ill-positioned to take advantage of it (and other emerging technologies) without a tech ecosystem that's efficient, scalable, and able to evolve.

There are still opportunities for growth and differentiation, but to make decisions with confidence, insurers need to have an ecosystem that they can trust. And that trustworthiness comes from accurate, actionable, and timely data.

This need for timely and actionable data becomes ever more important against the backdrop of current market conditions. Heightened volatility and the risk of recession—this year's most cited macroeconomic consideration—mean everyone across the organization has a risk point of view.

It's a necessary view, made even more pressing when combined with the need to see public and private markets assets together with a healthy underpinning of accounting capabilities, along with the increasing complexity of portfolios at large. In fact, 89% of those surveyed said they plan to increase allocations to private markets. In order to successfully implement this, insurers need a common data language, from public markets to private markets and from the front office through to operational processes—embedded in a trusted tech ecosystem—that liberates decision-making from the weight of outdated legacy systems, enables a more productive investment organization, and ultimately, unifies the investment management process.

It's there that opportunities exist for insurers: to streamline their investment operations, better manage change, acutely and overall, and deliver better investment outcomes.

The decision itself is in the data.

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