



# Capital Markets Special Report

The **NAIC's Capital Markets Bureau** monitors developments in the capital markets globally and analyzes their potential impact on the investment portfolios of US insurance companies. A list of archived Capital Markets Bureau Special Reports is available via the [index](#)

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## U.S. Insurance Industry Unaffiliated Investment Management Update, Year-End 2016

The decision by an insurer to use an unaffiliated investment manager can be driven by many factors. Insurers may seek an outside investment manager to help optimize their asset-liability matching goals, manage investment risk, enhance investment returns, reduce costs, or to assist in navigating an ever-changing and challenging investment market environment within their own unique individual investment, business and regulatory constraints.

An insurer may hire an unaffiliated investment manager to gain access to resources that it offers, which the insurer may not have in-house. Another insurer may seek an unaffiliated investment manager to tap its specialized knowledge or particular investment strategies or to help manage a small portion (or considerable portion) of its general account assets. Some large global investment firms offer broader access to investment and risk management solutions, while smaller firms or individuals may offer narrower or specific investment offerings. As an insurer considers outsourcing investment management, it may work with just one investment firm, or it may choose to hire multiple firms.

And as insurer investments are subject to regulatory, rating, duration, cash flow, statutory accounting and risk tolerance limitations (among others), insurers must be cautious upon selecting unaffiliated investment manager(s). That is, managing an insurer portfolio requires an understanding of the insurer's business and goals. While return is important in the continued low interest rate environment, insurers should be wary of firms that promise high returns with little to no risk. Investment managers that are hired to manage an insurer's assets must apply appropriate investment strategies, be suitable to manage the respective assets (i.e., according to insurance laws) and be comfortable with managing under the aforementioned constraints. As such, insurers tend to outsource to managers based on reputation and peer recommendations.

This report is an update to the NAIC Capital Markets Bureau Special Report published in May 2015 titled "U.S. Insurance Industry Third-Party Investment Management," which had discussed the increase in U.S. insurers outsourcing to unaffiliated investment managers. In this report, we provide an update on the industry's use of unaffiliated investment management firms and market trends.

### Investment Management Outsourcing by U.S. Insurers in 2016

Of the 4,466 U.S. insurance companies that filed annual statements in 2016, about 40% (1,801) indicated that they had a single unaffiliated investment firm manage more than 10% of their total reported assets at year-end 2016. In addition, approximately 30% (or 1,361 insurers) reported that they had unaffiliated investment managers managing more than 50% of their aggregate assets. About 29%

of insurers (1,308) reported having one firm manage more than 10% of their assets, while also having more than 50% of their total assets outsourced to an unaffiliated investment manager.

Property/casualty (P/C) companies represented the largest insurer type that outsourced investment management in 2016. P/C companies, as shown in Table 1, represented 67% of all insurers that outsourced more than 10% of their assets to one firm and also outsourced more than 50% of their total assets at year-end 2016. And the P/C companies that outsourced more than 10% of their assets to one firm and more than 50% of their total assets accounted for 33% of all P/C companies that reported financial statements at year-end 2016. Note that P/C insurers comprised nearly 60% of all U.S. insurers filing at year-end 2016.

**Table 1: Number of Insurers Outsourcing to Unaffiliated Investment Managers, Year-End 2016**

	Property/ Casualty	Health	Life	Fraternal	Title	Total
<b>Total Number of Insurers</b>	<b>2,630</b>	<b>967</b>	<b>738</b>	<b>77</b>	<b>54</b>	<b>4,466</b>
<b>&gt; 10% of Assets Outsourced to One Firm</b>	<b>1,168</b>	<b>364</b>	<b>225</b>	<b>29</b>	<b>15</b>	<b>1,801</b>
<i>Pct. Of Total Outsourced</i>	<i>65%</i>	<i>20%</i>	<i>12%</i>	<i>2%</i>	<i>1%</i>	<i>100%</i>
<i>Pct. Of Total Number by Industry Type</i>	<i>44%</i>	<i>38%</i>	<i>30%</i>	<i>38%</i>	<i>28%</i>	
<b>&gt; 50% of Total Assets Outsourced</b>	<b>916</b>	<b>217</b>	<b>190</b>	<b>27</b>	<b>11</b>	<b>1,361</b>
<i>Pct. Of Total Outsourced</i>	<i>67%</i>	<i>16%</i>	<i>14%</i>	<i>2%</i>	<i>1%</i>	<i>100%</i>
<i>Pct. Of Total Number by Industry Type</i>	<i>35%</i>	<i>22%</i>	<i>26%</i>	<i>35%</i>	<i>20%</i>	
<b>&gt; 10% of Assets Outsourced to One Firm and &gt; 50% of Total Assets Outsourced</b>	<b>877</b>	<b>211</b>	<b>182</b>	<b>27</b>	<b>11</b>	<b>1,308</b>
<i>Pct. Of Total Outsourced</i>	<i>67%</i>	<i>16%</i>	<i>14%</i>	<i>2%</i>	<i>1%</i>	<i>100%</i>
<i>Pct. Of Total Number by Industry Type</i>	<i>33%</i>	<i>22%</i>	<i>25%</i>	<i>35%</i>	<i>20%</i>	

### Size of Insurers Outsourcing Investment Management, Year-End 2016

As shown in Table 2, small insurers (those with less than \$250 million in assets under management) accounted for 71% of the insurers that had more than 10% of their assets managed by one investment manager. Additionally, small companies accounted for the highest percentage of insurers that outsourced more than half of their assets to unaffiliated investment managers, at 73% of total insurers.

For smaller insurers, an unaffiliated investment management arrangement may represent a more cost-effective way to invest some or all of their assets. An insurer, for example, with limited resources (financial, staff or otherwise) may gain access to greater resources—such as investment expertise and capabilities—at a lower cost by working with an unaffiliated manager. A company with a small asset base may not be able to cost-effectively replicate the skills or deep experience of an unaffiliated investment manager, particularly for specialty asset classes such as high-yield, real estate or private equity.

**Table 2: U.S. Insurers Outsourcing to Unaffiliated Investment Managers by Assets Under Management, Year-End 2016**

2016 Asset Size	Companies Outsourcing > 10% of Assets to One Firm		Companies Outsourcing > 50% of Total Assets	
< 250mm	1,285	71%	993	73%
Between \$250mm and \$500mm	204	11%	155	11%
Between \$500mm and \$1B	128	7%	82	6%
Between \$1B and \$2.5B	113	6%	75	6%
Between \$2.5B and \$5B	33	2%	25	2%
Greater than \$10B	20	1%	17	1%
Between \$5B and \$10B	18	1%	14	1%
<b>Total</b>	<b>1,801</b>	<b>100%</b>	<b>1,361</b>	<b>100%</b>

### Named Investment Managers by U.S. Insurers

The 10 unaffiliated investment management firms most often reported by U.S. insurers at year-end 2016 are shown in Table 3. BlackRock topped the list for the year, with 228 different insurers (about 5%) citing them as at least one of their hired unaffiliated investment managers. The second and third largest were Conning and New England Asset Management (NEAM), respectively. Note that some insurers may outsource to more than one asset management firm at a time, which is reflected in the data shown in Table 3. In comparison, the firm most cited by U.S. insurers as an unaffiliated investment manager at year-end 2013 (as indicated in the aforementioned published NAIC Capital Markets Special Report in 2015) was New England Asset Management, with BlackRock and Conning included in the top four.

**Table 3: Investment Managers Most Often Listed by U.S. Insurers, Year-End 2016**

Most Listed Investment Firms:		Number of Insurance Companies
1	BlackRock	228
2	Conning	204
3	New England Asset Management, Inc. (Gen Re Capital)	170
4	Deutsche Investment Management Americas, Inc.	137
5	Wellington Management Co. LLP	110
6	Asset Allocation and Management Company LLC (AAM)	104
7	Wells Capital Management, Inc.	88
8	Goldman Sachs Asset Management LP	84
9	Prime Advisors, Inc.	74
10	Pacific Investment Management Co. LLC (PIMCO)	68

### NAIC Regulatory Guidance and Additional Reporting Requirements for Year-End 2016

According to NAIC guidance (as included in the *Financial Condition Examiners Handbook*), in performing risk-focused examinations, examiners conducting financial condition exams related to investment advisors are directed to identify and take steps to address any significant risks associated with an insurer's use of unaffiliated investment advisers. These steps may include determining whether investment advisers are suitable for their role (i.e., registered and in good standing with the U.S. Securities and Exchange Commission (SEC) and/or state securities regulators); ensuring that investment advisory agreements contain appropriate provisions; confirming that the adviser is acting in accordance

with the agreement; and determining if management/board oversight of the investment adviser is sufficient for the relationship in place.

In examining the provisions of the investment advisory/management agreements, examiners consider whether there are appropriate provisions to adequately address selection of investments, authority for transactions, conflicts of interest, fiduciary responsibility, calculations of fees and review of performance.

For year-end 2016, U.S. insurers were required, for the first time, to furnish additional information about their unaffiliated investment managers as identified in the NAIC Annual Statement Instructions. These additional requirements provide state insurance regulators with important tools that help them focus on potential risks.

One such piece of information that insurers are required to provide is a Legal Entity Identifier (LEI) for any investment advisors, brokers/dealers or individuals acting on behalf of broker/dealers that had access to their investment accounts, handled securities or had the authority to make investments on the insurer's behalf. The LEI requirement is a consequence of the financial crisis and is a unique identifier of a legally distinct entity that engages in financial market activities.

In addition, insurers are required to report their investment manager's Central Registration Depository (CRD) number (whether they are unaffiliated or affiliated investment managers), which is issued by the Financial Industry Regulatory Authority (FINRA) to brokers, dealers or individuals that are licensed and contracted to manage an insurer's assets, on behalf of the insurer.

Insurers are also required to specify if their investment advisor is registered, and if registered, to supply the government agency that it is registered with (SEC or state securities regulators) and to complete information regarding the registration of its current Investment Management Agreement (IMA) showing whether an IMA for an investment manager was filed with its state of domicile, with a state other than its state of domicile, or if it was not filed with any state.

In addition, effective year-end 2016, insurers were to disclose how much of their assets were managed by unaffiliated investment firms and whether: 1) any single firm, unaffiliated with the reporting entity, managed more than 10% of their total assets; and/or 2) more than 50% of their assets were managed by an unaffiliated firm.

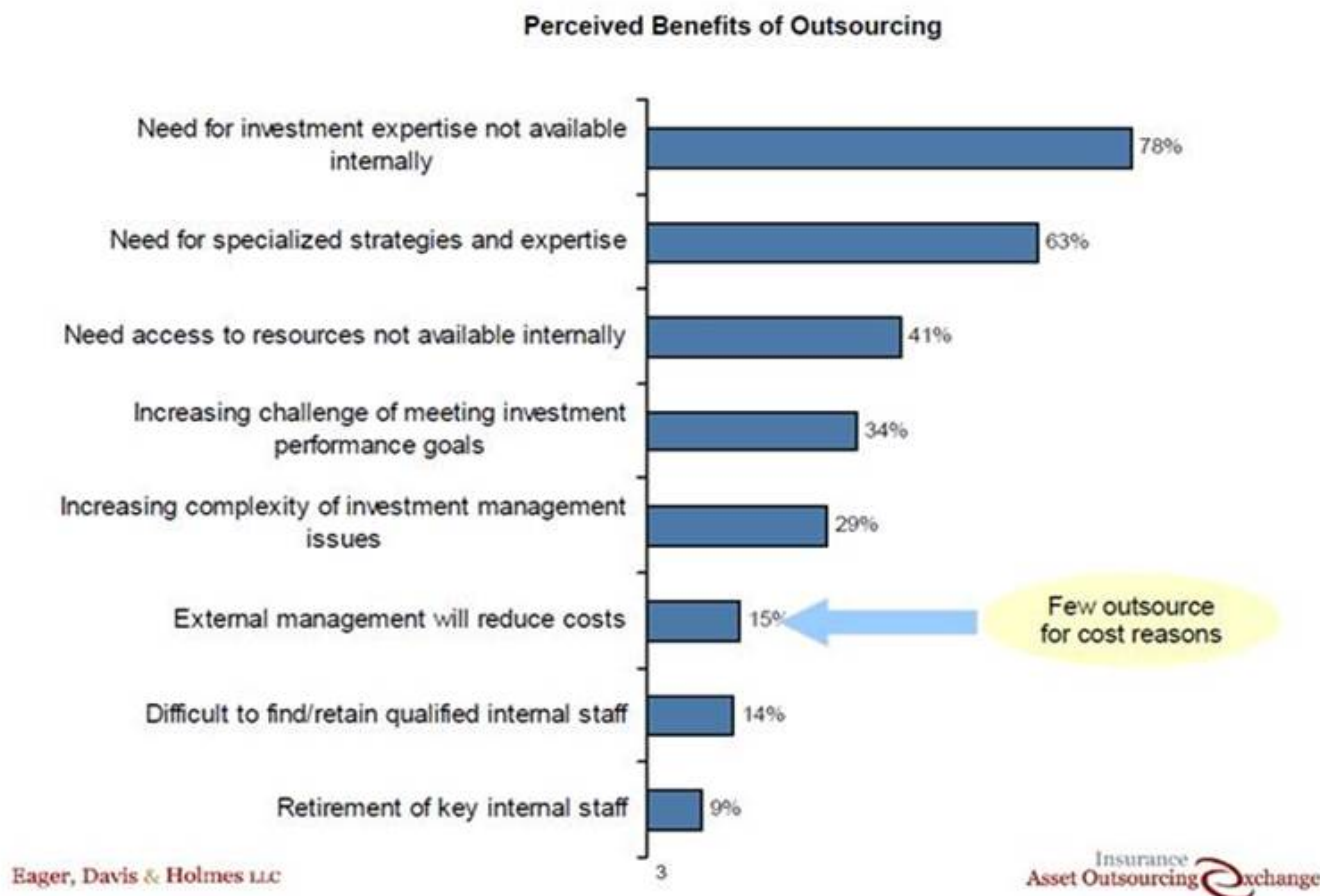
### **Trends in Outsourcing by U.S. Insurers**

In a 2017 study commissioned by State Street Corp. (a financial services provider), which included more than 100 respondents from the insurance sector, 32% of those surveyed said that they expected to outsource investment management, or increase outsourcing, in the coming year. The majority of the surveyed insurers (60%) also indicated that they may consolidate their investment management needs by placing larger mandates with fewer providers, allowing them to gain more control of investment management decisions and to have negotiating power with the unaffiliated managers.

In addition, data from Asset Outsourcing Exchange (a promoter of third-party insurance asset management information) shows that 78% of insurers surveyed cited the need for investment expertise not available internally as a reason for outsourcing the investment management function. (See Chart 1.) This was followed by 63% responding that they outsource due to the need for specialized strategies and expertise. Very few, that is, only 15% surveyed, outsource to reduce costs. In terms of sectors (that is, in cases where an insurer does not outsource its entire investment portfolio), the most popular mandate was for specialized fixed-income, such as emerging market debt and high-yield, in 2016.

### **Chart 1:**

## Why Insurance Companies Outsource Investment Management



A survey from Patpatia & Associates, a consultant that tracks insurance outsourcing, indicated that the total amount of investments outsourced by the U.S. insurance industry was approximately \$1.3 trillion in 2014, which represented an 18.2% increase from 2013 and a 30% increase from 2011. We expect that the total amount of investments outsourced by the U.S. insurance industry at year-end 2016 (and into 2017) has increased further, based in part, on this trend, and also because the total amount of assets under management by U.S. insurers has continued to increase year over year. Asset Outsourcing Exchange estimates that in 2016, about \$1.92 trillion in insurer investments (that is, for North American insurers, which includes the U.S. as well as Canada) were outsourced to unaffiliated investment managers. In addition, the NAIC reported data showed that the number of U.S. insurers outsourcing to unaffiliated investment managers has been increasing, as a total of 1,197 U.S. insurers disclosed use of a unaffiliated asset manager at year-end 2013, compared to about 1,800 at year-end 2016.

### Conclusion

In 2016, more than 40% of U.S. insurers that filed their annual statements with the NAIC acknowledged outsourcing more than 10% of their assets to a single unaffiliated investment manager, while more than 30% reported outsourcing more than 50% of their aggregate assets to unaffiliated managers. As of year-end 2016, the majority of U.S. insurers that outsourced to unaffiliated investment firms were small P/C companies with assets under management totaling less than \$500 million. The investment firms that were more often listed by insurers represented some of the larger global investment management firms (in terms of total assets under management), such as BlackRock and PIMCO.

Key drivers for U.S. insurers outsourcing investment management include gaining access to additional investment resources and expertise and specialized strategies that they otherwise would not have

available in-house. In a survey conducted by Asset Outsourcing Exchange, specialized fixed-income mandates—such as emerging market debt, high yield and other focused strategies—remained the most popular outsourced investment solutions for insurers in 2016.

The NAIC Capital Markets Bureau will continue to monitor trends in unaffiliated investment management of U.S. insurer assets and report as deemed appropriate.

February 9, 2018 Major Insurer Share Prices		Close	Change %			Prior		
			Week	QTD	YTD	Week	Quarter	Year
Life	Aflac	\$84.77	(4.7)	(3.4)	(3.4)	\$88.95	\$87.78	\$87.78
	Ameriprise	153.88	(8.1)	(9.2)	(9.2)	167.50	169.47	169.47
	Genworth	2.76	(8.9)	(11.3)	(11.3)	3.03	3.11	3.11
	Lincoln	75.38	(9.2)	(1.9)	(1.9)	83.04	76.87	76.87
	MetLife	44.61	(6.2)	(11.8)	(11.8)	47.56	50.56	50.56
	Principal	61.39	(7.5)	(13.0)	(13.0)	66.35	70.56	70.56
	Prudential	106.04	(9.6)	(7.8)	(7.8)	117.33	114.98	114.98
	UNUM	49.21	(6.6)	(10.3)	(10.3)	52.71	54.89	54.89
PC	Axis Capital	49.81	(0.7)	(0.9)	(0.9)	50.17	50.26	50.26
	Allstate	90.89	(7.2)	(13.2)	(13.2)	97.94	104.71	104.71
	Arch Capital	86.88	(4.5)	(4.3)	(4.3)	90.95	90.77	90.77
	Cincinnati	72.14	(5.6)	(3.8)	(3.8)	76.38	74.97	74.97
	Chubb	144.52	(5.7)	(1.1)	(1.1)	153.25	146.13	146.13
	Everest Re	239.77	4.4	8.4	8.4	229.61	221.26	221.26
	Progressive	52.22	(1.9)	(7.3)	(7.3)	53.24	56.32	56.32
	Travelers	137.08	(7.3)	1.1	1.1	147.95	135.64	135.64
	WR Berkley	68.02	(7.2)	(5.1)	(5.1)	73.31	71.65	71.65
	XL	41.86	9.4	19.1	19.1	38.25	35.16	35.16
Other	AON	\$137.91	(4.0)	2.9	2.9	\$143.59	\$134.00	\$134.00
	AIG	60.22	(4.5)	1.1	1.1	63.04	59.58	59.58
	Assurant	88.01	(4.3)	(12.7)	(12.7)	91.95	100.84	100.84
	Fidelity National	37.28	(1.7)	(5.0)	(5.0)	37.92	39.24	39.24
	Hartford	53.98	(6.9)	(4.1)	(4.1)	58.01	56.28	56.28
	Marsh	80.43	(5.0)	(1.2)	(1.2)	84.69	81.39	81.39
Health	Aetna	\$176.39	(4.7)	(2.2)	(2.2)	\$185.00	\$180.39	\$180.39
	Cigna	193.77	(5.2)	(4.6)	(4.6)	204.46	203.09	203.09
	Humana	265.32	(4.0)	7.0	7.0	276.50	248.07	248.07
	United	220.96	(4.7)	0.2	0.2	231.88	220.46	220.46
Monoline	Assured	\$34.57	(1.8)	2.1	2.1	\$35.19	\$33.87	\$33.87
	MBIA	7.25	0.1	(1.0)	(1.0)	7.24	7.32	7.32
	MGIC	14.01	(6.2)	(0.7)	(0.7)	14.94	14.11	14.11
	Radian	20.71	(7.7)	0.5	0.5	22.44	20.61	20.61
	XL Capital	41.86	9.4	19.1	19.1	38.25	35.16	35.16

February 9, 2018							
Major Market Variables		Change %			Prior		
		Close	Week	QTD	YTD	Week	Quarter
Dow Jones Ind	24,190.90	(5.2)	(2.1)	(2.1)	25,520.96	24,719.22	24,719.22
S&P 500	2,619.55	(5.2)	(2.0)	(2.0)	2,762.13	2,673.61	2,673.61
S&P Financial	458.95	(5.8)	(1.1)	(1.1)	487.21	463.94	463.94
S&P Insurance	386.87	(5.6)	(3.8)	(3.8)	409.97	402.08	402.08
US Dollar \$		Change %			Prior		
		/ Euro	\$1.22	(1.7)	2.1	2.1	\$1.25
/ Crude Oil bbl	59.23	(9.3)	(1.5)	(1.5)	65.28	60.11	60.11
/ Gold oz	1,313.10	(1.1)	0.6	0.6	1,328.10	1,305.20	1,305.20
Treasury Ylds %		Change bp			%	%	%
1 Year	1.89	0.02	0.14	0.14	1.87	1.75	1.75
10 Year	2.85	0.01	0.45	0.45	2.84	2.41	2.41
30 Year	3.16	0.07	0.42	0.42	3.09	2.74	2.74
Corp Credit Spreads -bp		Change %			Prior		
		CDX.IG	60.33	20.0	23.1	23.1	50.28

February 9, 2018										
Major Insurer Bond Yields					Weekly Change					YTD
					Price			Spread over UST		Spread
Company		Coupon	Maturity	Current	Change	Yield	B.P.	Change	Change	
Life	Ameriprise	AMP	3.700%	10/15/2024	\$102.49	\$0.40	3.28%	55	(5)	(10)
	Lincoln National	LNC	3.350%	3/9/2025	\$98.37	(\$0.18)	3.61%	84	6	0
	MassMutual	MASSMU	3.600%	4/9/2024	\$102.40	\$0.45	3.17%	48	(4)	(8)
	MetLife	MET	4.050%	3/1/2045	\$97.03	(\$0.55)	4.24%	110	(3)	7
	New York Life	NYL	2.350%	7/14/2026	\$92.32	\$0.11	3.41%	59	(1)	1
	Pacific Life	PACLIF	5.125%	1/30/2043	\$107.06	(\$0.83)	4.64%	152	(0)	(4)
	Principal	PFG	6.050%	10/15/2036	\$123.17	(\$0.94)	4.24%	123	3	(0)
	Prudential	PRU	4.600%	5/15/2044	\$105.94	(\$1.43)	4.22%	111	2	4
	Allstate	ALL	4.500%	6/15/2043	\$107.12	(\$1.24)	4.05%	93	0	(6)
	Berkshire Hathaway	BRK	4.300%	5/15/2043	\$106.19	(\$0.66)	3.91%	81	(2)	(9)
	Travelers	TRV	4.600%	8/1/2043	\$109.43	(\$1.07)	4.01%	89	(1)	(8)
	XL Group	XL	6.250%	5/15/2027	\$116.11	\$0.39	4.14%	127	(6)	(14)
Other	AON	AON	4.250%	12/12/2042	\$96.33	(\$1.03)	4.50%	138	1	(1)
	AIG	AIG	6.820%	11/15/2037	\$127.69	(\$0.36)	4.66%	160	(1)	2
	Hartford	HIG	4.300%	4/15/2043	\$101.16	(\$0.42)	4.22%	112	(4)	(3)
	Nationwide	NATMUT	5.300%	11/18/2044	\$111.86	(\$0.52)	4.53%	137	(8)	(7)
Health	Aetna	AET	6.750%	12/15/2037	\$130.48	(\$2.31)	4.43%	139	9	(1)
	CIGNA	CI	6.150%	11/15/2036	\$120.94	(\$1.59)	4.49%	145	6	8
	United Healthcare	UNH	4.750%	7/15/2045	\$111.66	(\$1.89)	4.04%	91	4	(6)

Questions and comments are always welcome. Please contact the Capital Markets Bureau at [CapitalMarkets@naic.org](mailto:CapitalMarkets@naic.org).

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