NAIC National Association of Insurance Commissioners & The CENTER for INSURANCE POLICY and RESEARCH Capital Markets Special Report

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Growth in U.S. Insurance Industry's Cash and Invested Assets Slows in 2018

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Executive Summary

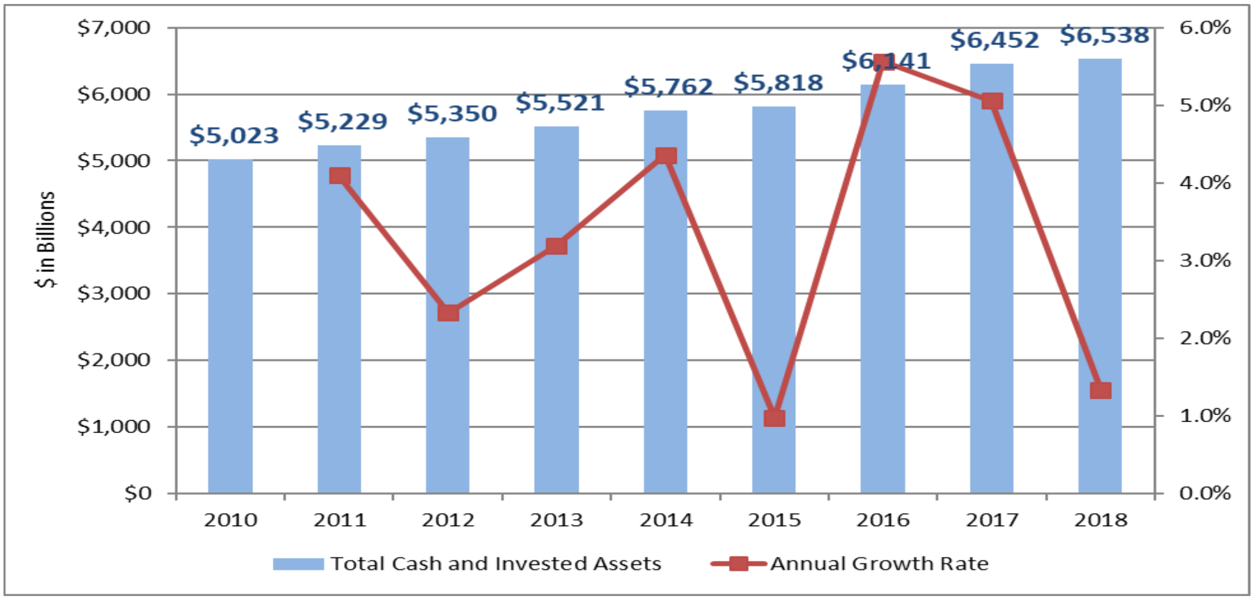
- Growth in the U.S. insurance industry's cash and invested assets slowed to an increase of 1.3% as of year-end 2018 versus a 5.1% increase at year-end 2017.
- Asset distribution and assets by insurer type remained relatively unchanged year-over-year, with bonds remaining as the largest component of U.S. insurer investments and life companies holding the largest share of invested assets.
- U.S. insurers continued to invest in higher risk, less liquid assets (such as mortgages and Schedule BA assets) in 2018, with interest rates remaining relatively low.
- Exposure to mortgages and Schedule BA assets in 2018 grew at a faster pace than the industry's overall growth in total cash and invested assets.
- The credit quality of the industry's bond holdings improved slightly at year-end 2018, with 5.1% of exposure carrying NAIC 3 designations and below, compared to 5.5% at year-end 2017.

This NAIC Capital Markets Bureau's annual special report examines the U.S. insurance industry's cash and invested assets, as reported by approximately 4,500 insurance companies for the year ended Dec. 31, 2018. We review noteworthy changes in the industry's distribution of assets over time, as well as trends in asset distribution by insurer type and size. A detailed analysis of the industry's bond exposure is also provided, drilling down by bond type and credit quality.

U.S. insurers' reported cash and invested assets, including affiliated and unaffiliated investments, have steadily increased since at least 2010. Chart 1 shows the industry's total cash and invested assets on a book/adjusted carrying value (BACV) basis from 2010 through 2018, along with annual year-over-year (YOY) growth rates. The industry has experienced a compound annual growth rate (CAGR) of 3.4% in cash and invested assets from 2010 through 2018, with year-end 2018 cash and invested assets over

$6.5 trillion. Asset growth slowed in 2018 to 1.3%, following growth rates greater than 5% in 2016 and 2017.

Chart 1: Total U.S. Insurance Industry Cash and Invested Assets, 2010–2018



Note: Includes affiliated and unaffiliated investments.

Bond Investments Are the Asset of Choice

The U.S. insurance industry's asset allocations are relatively stable and have not changed significantly for many years. Bonds remained the largest component of U.S. insurer assets at year-end 2018, representing 65.7% of total cash and invested assets. Common stock investments were the second largest holding for the industry at 12% of total cash and invested assets, followed by mortgages at 8.5% and Schedule BA assets (other long-term investments) at 5.6%. (See Table 1.) These rankings have been unchanged since at least 2010.

Table 1: Total U.S. Insurance Industry Cash and Invested Assets by Asset Class and Insurer Type, Year-End 2018 (BACV$ in millions)

Asset Class	Life	P/C	Health	Fraternal	Title	Total	% of Total
Bonds	2,999,456	1,054,242	128,601	108,412	5,150	4,295,861	65.7%
Common Stock	158,004	582,735	36,781	4,506	2,214	784,240	12.0%
Mortgages	521,544	20,799	145	12,429	54	554,970	8.5%
Schedule BA (Other Long-Term Assets)	189,859	156,355	13,377	5,667	171	365,429	5.6%
Cash & Short-Term Investments	104,975	103,741	40,615	2,499	1,426	253,257	3.9%
Contract Loans	129,333	3	0	2,905	-	132,241	2.0%
Derivatives	56,423	424	6	29	-	56,883	0.9%
Real Estate	20,482	13,768	5,728	282	229	40,489	0.6%
Preferred Stock	12,310	5,567	598	687	383	19,546	0.3%
Securities Lending (Reinvested Collateral)	12,576	4,996	998	593	-	19,164	0.3%
Other Receivables	9,014	6,665	470	96	10	16,256	0.2%
Total	**4,213,978**	**1,949,294**	**227,319**	**138,105**	**9,638**	**6,538,335**	**100%**
% of Total	64.5%	29.8%	3.5%	2.1%	0.1%	100%	

The industry's total cash and invested assets by insurer type have also remained consistent over the last several years. Life companies held the largest share, or 64.5%, of the industry's total cash and invested assets in 2018, while property/casualty (P/C) companies continued to account for almost 30% of total cash and invested assets.

No significant changes in the mix of cash and invested assets as of year-end 2018 were noted when compared to year-end 2017. However, the allocation to common stock decreased to 12% of cash and invested assets at year-end 2018 from 12.5% as of year-end 2017. (See Table 2.) The decline is likely due in part to the weak performance of the equity markets in December 2018; the Standard & Poor's 500 Index (S&P 500) declined 6.2% in 2018. The industry's allocation to mortgages increased on a YOY basis to account for 8.5% of cash and invested assets as of year-end 2018, compared to 7.9% as of year-end 2017. U.S. insurers' BACV exposure to mortgages has been rising since at least 2010.

Table 2: Total U.S. Insurance Industry Cash and Invested Assets by Asset Class and Insurer Type, Year-End 2017 (BACV$ in millions)

Asset Class	Life	P/C	Health	Fraternal	Title	Total	% of Total
Bonds	2,982,586	1,003,354	116,948	106,703	4,858	4,214,449	65.3%
Common Stock	166,027	598,478	37,510	4,486	2,460	808,962	12.5%
Mortgages	477,051	18,119	134	11,583	81	506,968	7.9%
Schedule BA (Other Long-Term Assets)	177,694	159,418	11,312	4,783	210	353,416	5.5%
Cash & Short-Term Investments	105,008	117,258	46,189	2,925	1,196	272,575	4.2%
Contract Loans	129,027	3	-	2,884	-	131,915	2.0%
Derivatives	58,661	233	1	48	-	58,942	0.9%
Real Estate	23,550	12,849	5,544	286	227	42,457	0.7%
Preferred Stock	10,514	5,522	454	612	402	17,504	0.3%
Securities Lending (Reinvested Collateral)	16,870	4,476	724	571	-	22,640	0.4%
Other Receivables	11,652	9,785	652	67	5	22,161	0.3%
Total	**4,158,640**	**1,929,496**	**219,468**	**134,946**	**9,440**	**6,451,989**	**100%**
% of Total	**64.5%**	**29.9%**	**3.4%**	**2.1%**	**0.1%**	**100%**	

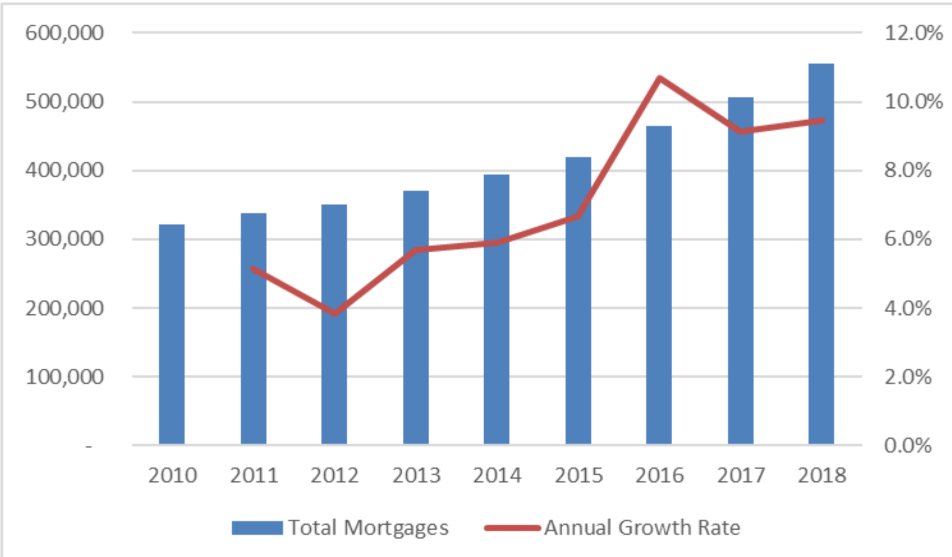
For year-end 2018, bonds accounted for the largest asset class for all insurer types. Bonds represented 71% and 79% of cash and invested assets for life and fraternal companies, and they represented 54%, 57% and 53% of cash and invested assets for P/C, health and title companies, respectively. Mortgages were the second largest asset class for life and fraternal companies (12% and 9%, respectively), while common stock was the second largest for P/C and title companies (30% and 23%, respectively), and cash and short-term investments were the second largest for health companies (18%). The top two asset allocations for each insurer type have not changed in recent years.

Push into Higher Risk, Less Liquid Assets Continue

Given the prolonged low interest rate environment, U.S. insurers have been investing more of their dollars in higher yielding assets, such as mortgages, private equity, hedge funds and privately placed bonds. Although these asset classes generally offer higher yields than public corporate bonds, they are typically less liquid, have less transparency and are subject to greater price volatility.

The U.S. insurance industry's exposure to mortgages increased to $555 billion at year-end 2018 from $322 billion at year-end 2010, for a CAGR of 7.1%. (See Chart 2.) The rate of growth of mortgage exposure for the eight-year period is approximately double that of the industry's cash and invested assets. For the last three years, the annual growth in mortgage exposure has been at or near double-digits—9.5%, 9.1% and 10.7% in 2018, 2017 and 2016, respectively.

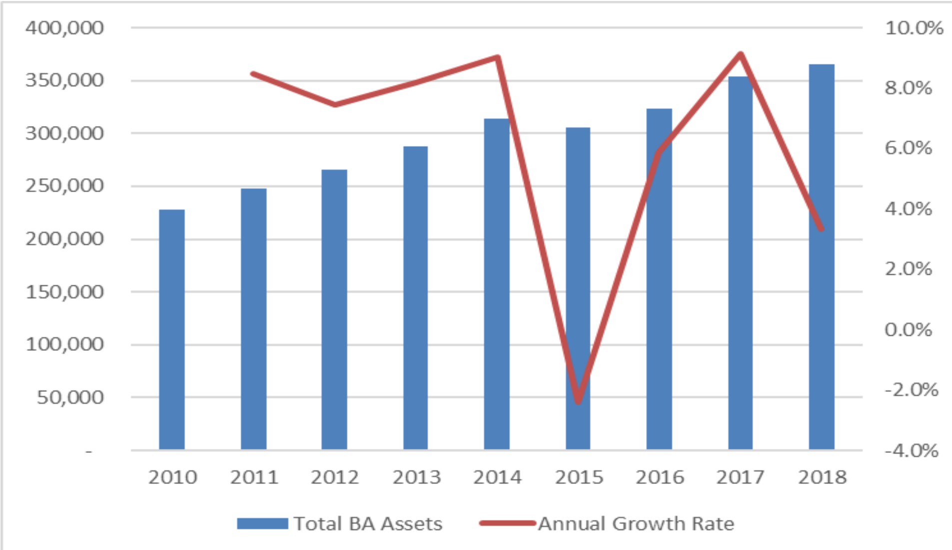
Chart 2: U.S. Insurance Industry Mortgage Exposure, 2010–2018



Life companies accounted for the majority of the industry's mortgage exposure, or 94% of the total. For life companies, $521.5 billion mortgage exposure at year-end 2018 represented 12.4% of their total cash and invested assets, an increase from 11.5% at year-end 2017. P/C companies' mortgage exposure represented only 3.6% of the industry's exposure, but it has been growing at a relatively fast pace—14.8%. 15.8% and 31.4% in 2018, 2017 and 2016, respectively—albeit from a low base.

We also noted a steady increase in BACV over time for Schedule BA assets. Schedule BA exposure increased to $365.2 billion at year-end 2018 from $228 billion at year-end 2010, for a CAGR of 6.1%. (See Chart 3.) The industry's exposure to Schedule BA assets grew faster than the 3.4% CAGR of total cash and invested assets over the eight-year period, although growth slowed in 2018 to 3.3%.

Chart 3: U.S. Insurance Industry Schedule BA Asset Exposure, 2010–2018



Life and P/C companies held 95% of the industry's Schedule BA exposure, with $189.8 billion and $156.3 billion, respectively, at year-end 2018. In 2018, Schedule BA exposure at P/C companies decreased 2%, after increasing 7.6% and 9.4% in 2017 and 2016, respectively. Title companies' exposure also declined by 18.6% in 2018, while life, health and fraternal companies' exposure increased 6.8%, 16.9% and 18.5%, respectively. As a percent of cash and invested assets, however, P/C companies held the largest share of Schedule BA assets at 8%, followed by health and life companies at 5.8% and 4.5%, respectively.

Unaffiliated Schedule BA exposure totaled $160.7 billion at year-end 2018, or 44% of total Schedule BA assets. The industry's exposure to unaffiliated Schedule BA assets increased 8% in 2018, a higher growth rate than the 3.3% increase in total Schedule BA assets. Unaffiliated Schedule BA exposure increased 7.9% and 4.5% in 2017 and 2016, respectively—or lower than the annual growth rates in exposure to total Schedule BA assets.

Further Insights into the Insurance Industry's Cash and Invested Assets

Consistent with previous years, the largest U.S. insurers (those with assets under management greater than $10 billion) held the majority, or 73%, of the industry's total cash and invested assets at year-end 2018. (See Table 3.) Exposure for this group totaled $4.8 trillion, an increase of 1.3% compared to year-end 2017—and the same as the increase in total cash and invested assets for the industry.

Table 3: U.S. Insurance Industry Cash and Invested Assets by Insurer Size, Year-End 2018 (BACV$ in millions)

Asset Class	Greater Than $10B	Between $5B and $10B	Between $2.5B and $5B	Between $1B and $2.5B	Between $500mm and $1B	Between $250mm and $500mm	Less Than $250mm
Bonds	3,066,658	328,908	272,979	281,471	130,766	97,844	117,234
Common Stock	551,173	64,935	52,706	56,440	24,657	19,524	14,806
Mortgages	510,910	20,518	11,597	7,905	2,060	1,224	756
BA & Other	301,148	24,830	14,538	14,323	6,349	2,459	1,753
Cash & Short-Term Investments	128,342	16,419	22,283	21,257	18,266	15,051	31,640
Contract Loans	116,374	7,055	3,423	3,661	604	709	415
Derivatives	54,029	1,953	432	445	23	0	1
Real Estate	26,700	2,857	2,520	4,434	1,603	1,147	1,225
Preferred Stock	11,417	2,123	2,145	1,900	893	507	560
Securities Lending (Reinvested Collateral)	14,534	1,970	1,005	1,095	250	154	155
Other Receivables	11,584	602	2,505	729	412	47	375
Total	**4,792,870**	**472,169**	**386,133**	**393,661**	**185,881**	**138,667**	**168,921**
% of Total	73.3%	7.2%	5.9%	6.0%	2.8%	2.1%	2.6%

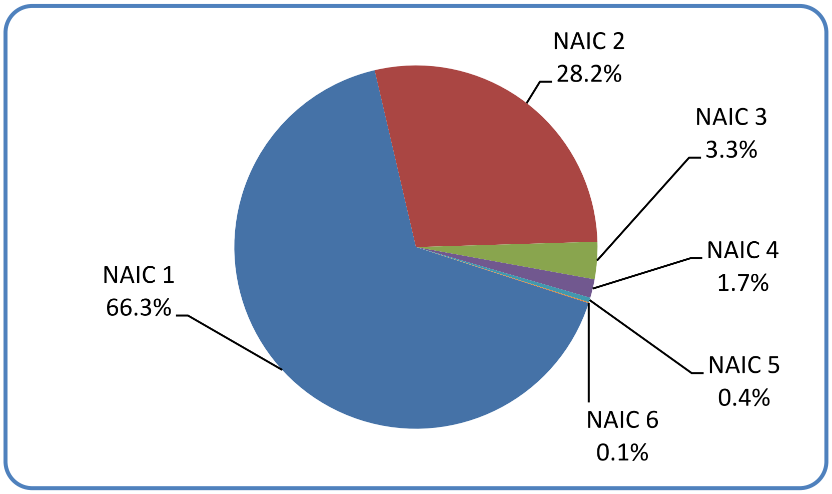
The U.S. insurance industry reported $4.3 trillion in bonds at year-end 2018, an increase of 1.9% compared to year-end 2017. Bond exposure increased at a faster pace than the 1.3% YOY growth in total cash and invested assets. The ranking of bond types at year-end 2018 remained consistent with prior years. Corporate bonds and municipals bonds were the two largest bond types, representing 54.6% and 12.1%, respectively, of the industry's total bond exposure. (See Table 4.) Asset-backed securities (ABS) and other structured securities, agency-backed residential mortgage-backed securities (RMBS) and U.S. government bonds followed and accounted for 8.5%, 6.8% and 6.7% of total bond exposure, respectively. Note that as of 2018, U.S. insurers were required to report bank loans as a separate line item in Schedule D Part 1. This includes bank loans that are acquired through an assignment, participation or syndication, as well as bank loans that are issued directly by a reporting entity. As of year-end 2018, the U.S. insurance industry's exposure to bank loans totaled $53.7 billion, of which $50.1 billion were acquired bank loans.

Table 4: Bond Breakdown by Insurer Type, Year-End 2018 (BACV$ in millions)

Bond Type	Life	P/C	Health	Fraternal	Title	Total	% of Total
Corporate Bonds	1,843,607	373,750	49,295	74,674	2,431	2,343,757	54.6%
Municipal Bonds	195,605	291,975	23,176	8,500	1,108	520,364	12.1%
ABS and Other Structured Securities	279,815	69,743	10,390	4,089	27	364,065	8.5%
Agency-Backed RMBS	174,887	88,760	16,985	9,245	703	290,580	6.8%
U.S. Government	150,279	115,355	17,695	2,066	311	285,707	6.7%
Private-Label CMBS	130,608	38,565	4,593	3,845	23	177,634	4.1%
Private-Label RMBS	75,040	19,119	1,177	1,133	0	96,469	2.2%
Agency-Backed CMBS	47,423	21,339	1,182	3,035	67	73,046	1.7%
Foreign Government	43,496	18,574	726	1,066	249	64,111	1.5%
Bank Loans	39,597	11,685	1,658	504	207	53,651	1.2%
Hybrid Securities	15,512	3,185	307	227	22	19,253	0.4%
ETF-SVO Identified Funds	3,574	2,021	1,114	27	1	6,737	0.2%
Bond Mutual Funds-SVO Identified Funds	11	159	303	0	-	474	0.0%
Total	**2,999,455**	**1,054,231**	**128,601**	**108,412**	**5,149**	**4,295,848**	**100%**
% of Total	69.8%	24.5%	3.0%	2.5%	0.1%	100%	

The credit quality of the industry's bond holdings improved marginally for the second year in a row. Investment grade bonds, or those with reported NAIC 1 or NAIC 2 designations, accounted for 94.9% of total bonds compared to 94.5% and 94.1%, at year-end 2017 and 2016, respectively. Below-investment grade bonds, or those with reported NAIC 3 designations and below, represented 5.1% of bond exposure. (See Chart 4.) While the exposure to below-investment grade bonds as a percent of total bond exposure decreased at life, P/C and title companies, it increased marginally at health and fraternal companies to 5.5% and 5.1%, respectively. Title companies, in particular, reduced their below-investment grade exposure from 9.1% of total bond exposure at year-end 2017 to 6% as of year-end 2018.

Chart 4: Reported Credit Quality of U.S. Insurance Industry's Bond Portfolio at Year-End 2018



The Capital Markets Bureau will continue to monitor trends in the U.S. insurance industry's various invested asset types and report as deemed appropriate.

Questions and comments are always welcome. Please contact the Capital Markets Bureau at CapitalMarkets@naic.org.

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