

# INSURANCE ASSET MANAGER

## INSURANCE FROM THE INVESTMENT ANGLE

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## CONNING PRESIDENT WOODY BRADFORD SCANS THE GLOBE FOR OPPORTUNITIES

*When Conning & Co., a perennial leader in the field of insurance asset management, celebrates its 100th anniversary in 2012, the firm will still be actively expanding its scope of activities under owner Aquiline Capital Partners LLC, which purchased the Hartford, CT-based manager in 2009. So says Woody E. Bradford, who joined Conning in early 2010, and as president and COO is guiding the firm's growth strategy.*

*Conning already has the acquisition of DFA Capital Management, a global risk and capital management specialist, under its belt, and recently lined up an Asia-based joint venture with Cathay Financial Holdings. Conning acquired a taste for international exposure when it was owned by Swiss Re from 2001 to 2009, but the pace under Aquiline has definitely quickened.*

*As the insurance asset management business becomes more global, Bradford comments, "Conning is excited about growth opportunities here in the US and overseas." A veteran of Putnam Investments, Bradford was an operating partner with Advent International, a global private equity firm, before Aquiline offered him the opportunity to join Conning. In this interview, IAM editor Alex McCallum asked Bradford a wide range of questions about Conning's post-crisis positioning and issues affecting the investment side of the insurance industry.*

***IAM: As one of the long-standing leaders in insurance asset management, what does Conning see as the most important trends that have developed from the financial crisis for investment firms active in this sector?***

***Bradford:*** One of the major changes we see is the accelerated evolution toward holistic management of risk. There is now an expanding understanding of risk that is forcing investment managers to generate superior risk adjusted returns on capital, not just returns. Capital management strategies are explicitly quantifying risks and playing a more critical role in driving decision-making.

We are also seeing increased imperatives from regulators and rating agencies. We believe that regulation in the aftermath of the financial crisis may affect more property-casualty insurers than the crisis itself.

***IAM: You must feel, then, that your acquisition of DFA Capital assets has been timely. You purchased DFA last November, yes?***

***Bradford:*** Yes, that's right. Coming out of 2008, we decided that we needed to have more advanced technology and more advanced tools. And so we searched the marketplace for leaders that could help strengthen our technology platform. When we first met with DFA Capital, we found that their technology and approach were exactly what insurance companies needed, and we went and bought the company. For Conning, it's a great fit because DFA brought advanced technology, tools and models that reflected real world risks. So, combining their technology and our talent was perfect for us, and a great fit for them too.

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***IAM: How extensive geographically did DFA operate when you first encountered them?***

**Bradford:** DFA Capital had offices here in the US and in Europe, and that's one of the things that attracted us. In many ways, they felt like a global company through their presence and positioning so, for us, it was certainly an extra benefit to partner with a firm that had a strong European presence and client base.

It's been a timely acquisition. Risk is an important topic of discussion amongst our clients. And for us now to have DFA's highly-regarded tool kits to analyze an insurer's risks, and to model and re-model portfolios, is a real competitive advantage for us.

***IAM: And presumably, this is of particular significance during this challenging period of low yields?***

**Bradford:** Correct. The DFA approach certainly helps insurance companies think through, in a sophisticated way, what risks they want to take to increase their yields. This is somewhat different from a simplistic approach like, "Yields are low. It's time to buy high yield bonds or emerging market debt." Our approach is a little different, which is to say, "Let's look at what all your options are across your entire portfolio and find a way to increase the yield and return on capital for your entire book of business." So it's not just a simplistic slice and dice, or buying the next "hot fad". For us at Conning, being almost a hundred years old and fairly conservative, we prefer a more integrated and holistic approach.

***IAM: Looking at the entire insurance industry post-crisis, domestically and globally, do you expect an increase or decrease in consolidation and M&A activity in certain areas, and what kind of impact will the trends that you identify have on insurance asset managers here and abroad.***

**Bradford:** In the US market, there is consolidation among insurers with specialist expertise, and expansion of specialty insurance. Large and mid-size insurers have been acquiring specialty insurers to support expansion strategies and to leverage traditionally larger underwriting margins associated with specialty markets.

The conditions currently driving M&A activity for property-casualty insurers and reinsurers are unused underwriting capacity, compressed margins, and the development of more complex and restrictive capital management oversight.

The developing regulatory climate in Europe with Solvency II will lead to more restrictive capital adequacy requirements and substantially more complex and costly compliance reporting. Larger insurers generally will be affected less adversely by the costs as a percentage of revenue. Achieving scale becomes an even more important incentive for M&A in this environment, especially among the smallest of insurers for both US and international insurers, Lloyd's syndicates offer both expansion and specialty expertise opportunities, such as seen lately with Ryan Specialty /Jubilee and Hanover/Chaucer.

***IAM: Until recently, it was rare to find the very large insurers looking for investment management externally, but times have changed. What are the main reasons for this, and what are the potential advantages and challenges?***

**Bradford:** There are a number of factors that continue to shape the industry. Increasing competitive intensity and heightened risk awareness post-financial crisis have led to an environment where insurers are seeking innovative solutions to improve their risk adjusted returns, and returns on capital. Leveraging the deep, holistic expertise of a third-party asset manager enables insurers to focus on their core business of insurance. It allows in many cases for an enhancement of knowledge and expertise on the investment side, and of course, lower costs and access to a scaled investment platform can be attractive motivations.

***IAM: With insurance outsourcing expanding internationally as well as domestically, how rapidly are you becoming active in markets other than Europe, where you have been operating for a number of years? And which markets look most promising, and will you consider expanding through acquisitions and partnerships as well as organically?***

**Bradford:** We are very much focused on enhancing our global presence. In Europe, we have an investment and sales team located in Dublin and London as well as a financial modeling and analytics business in Cologne, Germany, acquired late last year.

With our latest initiative, in June, we took a big step in the Asia-Pacific region by teaming up 50-50 with Cathay Financial Holding Co., Ltd. of Taiwan to launch an asset management company that will have its headquarters in Hong Kong. We expect that our joint venture will have a leadership team in place by

the end of this year and we will be targeting markets in Taiwan, China, South Korea, Japan and Vietnam, as well as Hong Kong.

As you can tell, we see tremendous opportunities in Europe and in Asia for growth.

**IAM: Yes, I can see that.**

**Bradford:** As the business is becoming more global, it's critical for us to be as global as our clients, and we are achieving that.

We also recognize that the markets in these world regions can be quite different from one another. For example, take Asia, where yields are generally lower than we have in the US, or look at liability durations for Asian life companies that don't have a local equivalent to the 30-year bond. An insurance company looking for a good yield and longer duration exposure has to look outside its domestic market. And that's where we come in.

**IAM: Back to Europe again, do you think the impact of the EU's impending Solvency II regulations will offer more, or fewer, opportunities for building investment relationships with European insurance companies? What are the main factors involved, and do they include a certain amount of anxiety over the sovereign risk situation in Europe?**

**Bradford:** Solvency II will offer significantly more opportunities for building investment relationships with European insurance companies in a number of areas.

There is a distinct difference between the fundamental framework of Solvency I and II. Under Solvency I, required capital was simply a proportion of statutory liabilities without regard for business or market risks; however, Solvency II is a risk-based approach where required capital will be based on the actual risks on the balance sheet. This distinction and its impact for insurers will create an increased need for risk and capital management solutions to facilitate insurers' understanding of and full compliance with Solvency II.

The sovereign concerns have been widely covered in the press and present a host of additional investment risks separate from the regulatory changes, which insurers should be evaluating very carefully.

**IAM: When you look back at the investment performance of insurance companies during and after the financial crisis, do you have any observations that might help insurers and their advisors the next time round – in terms of positioning, strategy, staffing, regulations and so forth?**

**Bradford:** In a nutshell, we believe that a quality, well-structured diversified portfolio, expertly synchronized to your liabilities that require no forced liquidations, is the best plan for insurers. Take risks where you can get paid for them and improve risk-adjusted returns on capital. Don't panic: Establish a prudent investment plan built to weather the storms -- and stick to it.

**IAM: A final question. Conning is one of the few pure insurance asset management companies, if I'm not mistaken. Do you think this gives you an advantage over your competitors?**

**Bradford:** I think it's a real edge. Here are three reasons why:

First, since insurance is our one and only focus, we understand insurance challenges. We are able to customize solutions that meet insurers' needs. In fact, our chief investment officer is an actuary!

Second, we have deep expertise in risk and capital management. We are very knowledgeable about the risks that insurance companies face, and our solutions and portfolios are developed much more effectively with this in-depth know-how.

Third, our investment philosophy is to protect on the downside and to participate on the upside. We have done that consistently and our clients have benefited from the strong results we have delivered.

There is no question in my mind that this is due to our insurance focus which has helped us become the largest, independently-owned insurance asset management company in the world.

**IAM. Thank you.**