A Leading Global Investment Management Firm

Strategic Asset Allocation Approach

June 2021

CONNING®

FOR PROPERTY/CASUALTY INSURERS

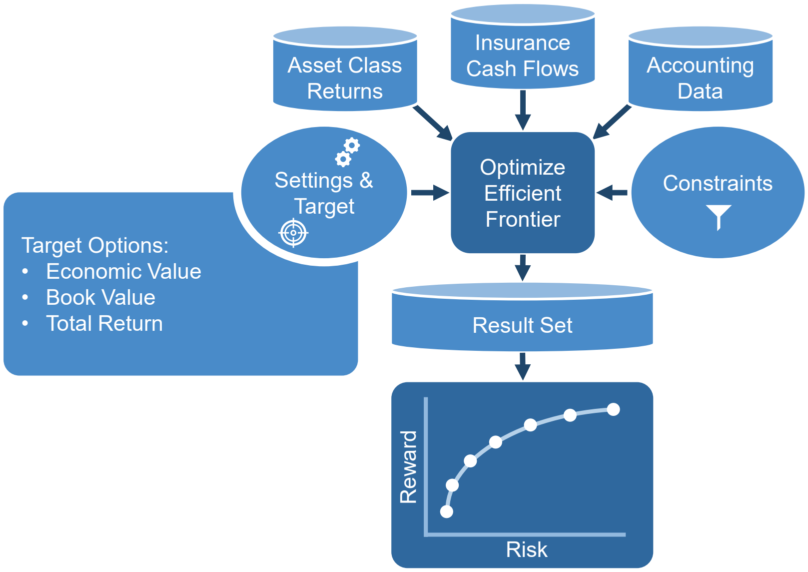
Empowering Financial Decision-Making for Executives

Property and Casualty (P&C) insurers as capital constrained entities must constantly measure, assess, and plan allocations for the various risks they take. These risks include their balance sheet leverage, underwriting performance, reinsurance program, reserving practices and investment strategy. All of this is further complicated by meeting the varied needs of regulators, rating agencies, policyholders or other stakeholders and the expected return of the organization. For all these reasons a P&C insurer's investment strategy cannot be optimized in isolation.

Each P&C insurer pursues different strategies based on the risks written, the company's unique profit goals and most importantly the firm's risk tolerance. A successful strategy requires a holistic approach in analyzing and setting an appropriate investment strategy that complements the company's overall business. Failing to analyze the investment choices along with all these considerations can result in suboptimal enterprise outcomes.

Conning's philosophy for managing the investment portfolio of P&C insurers relies on a Strategic Asset Allocation (SAA) approach (Figure 1.). While some might approach this exercise through the lens of optimizing the investment returns only, Conning views the role of the portfolio within the entire operation of an insurance company, i.e., a holistic company framework. Once we capture the totality of the operations, Conning then looks to think about portfolio optimization.

Figure 1 Model of Conning's Holistic SAA Approach



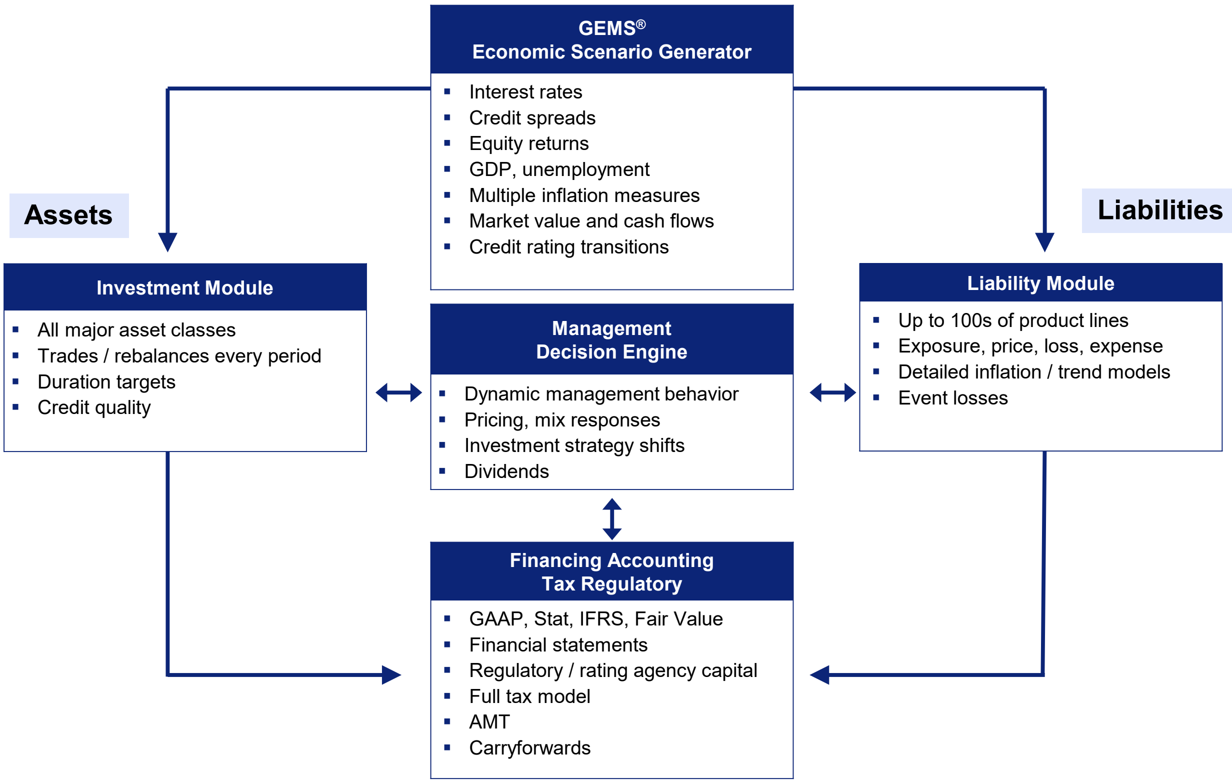
Prepared by Conning, Inc.

Many asset managers think investment strategy decisions should be centered solely around optimizing returns. However, this fails to incorporate future claims payouts and the risk of payment expectations. An example is the incorporation of uncertainty around the cost of future claims resulting from unexpected inflation. Another missed perspective is the incorporation of an appropriate timeframe. We believe, similarly to how a company plans for its business, a reasonable time frame to keep in mind is typically three to five years.

Conning also differentiates itself by optimizing the value of the company through an efficient frontier framework with **Economic Value** as a driving metric. **Economic Value** is the market value of a company's assets minus the discounted value of future liability payouts plus value from future business operations.

At the commencement of the process, Conning utilizes its award-winning[1] economic scenario generator, GEMS® Economic Scenario Generator software (Figure 2). The software produces real-world economic and capital market scenarios involving inflation, interest rates and equity returns all to be used in the calculations of a company's financial model. This provides stochastic scenarios for a range of paths across a multi-year time frame to optimize company value, not just investment returns.

Figure 2 Conning's GEMS® Optimization Process



Prepared by Conning, Inc.

This holistic view allows us to incorporate P&C assets and liabilities into a single optimization. As such, we can capture impacts on the business, impacts on the investment portfolio and the interdependencies and interplay between the two. By examining both sides of the balance sheet using the same set of stochastic scenarios, no risk is overlooked and no opportunity is missed. This provides a framework for assessing the company's value across a range of accounting, tax, and regulatory regimes to ensure stakeholders' key considerations are not missed.

When helping clients evaluate investment strategies, Conning takes great care in understanding their objectives and risk tolerance as well as their constraints and time horizons, which enables them to think through, focus on, and communicate how the strategic decisions support profitability and financial strength. For instance, ensuring that liability payments and inflation risks affecting reserves are incorporated provides stakeholders a more in-depth understanding of the impact on the entire organization and not just projected investment returns. Having communicated extensively with the client's management and having completed thousands of different economic simulations using GEMS® software, we can dive deeper into different forms of analysis.

Examples of Analysis Employed During Conning's SAA Process:

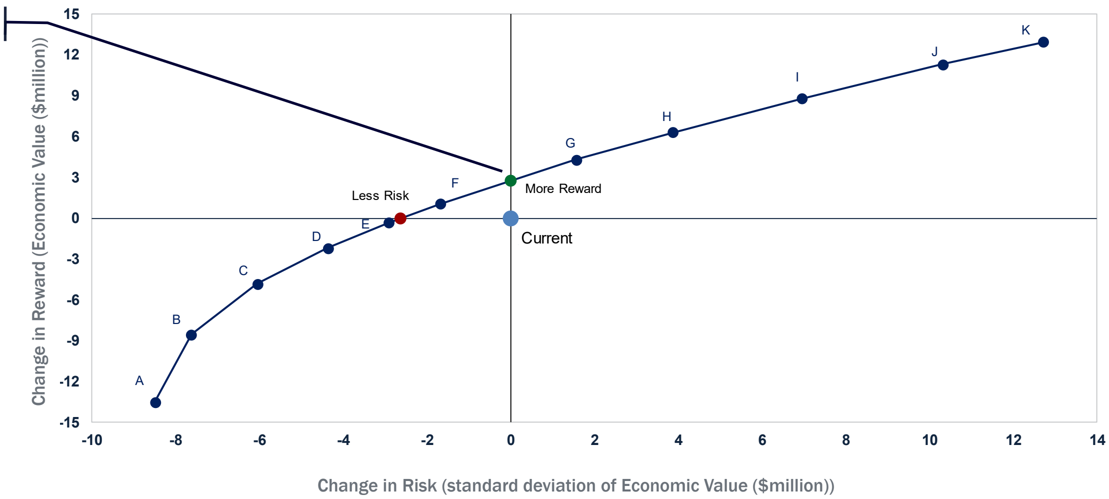
Optimizing Investment Strategies: The efficient frontier (Figure 3) shows how a company's risk and reward can change from portfolio A (lower risk and return) to portfolio K (higher risk and return) by shifting the allocations to a wide selection of investment vehicles with different risk factors such as credit quality, liquidity and duration.

The company's current investment strategy is plotted with the efficient frontier to show opportunities for more optimal enterprise outcomes that may result from varying alternative portfolio strategies.

We can also demonstrate the value of increased limits to certain types of investments, such as increasing equity and alternative allocations or adding new asset classes, to help generate additional value by improving returns for each level of risk or increasing diversification.

Figure 3 Investment Optimization: Efficient Frontier

Average Rating Duration	A+ 5.5
Cash & Treasuries	5%
Municipals	26%
Corporates A&above	4%
Corporates BBB	4%
Structured	18%
CLOs	5%
CMLs	1%
Private Placements	5%
High Yield	5%
Convertibles	4%
EMD	5%
Bank Loans	0%
Equities	18%
Hedge Funds	0%
Private Equity	2%
Real Estate	0%



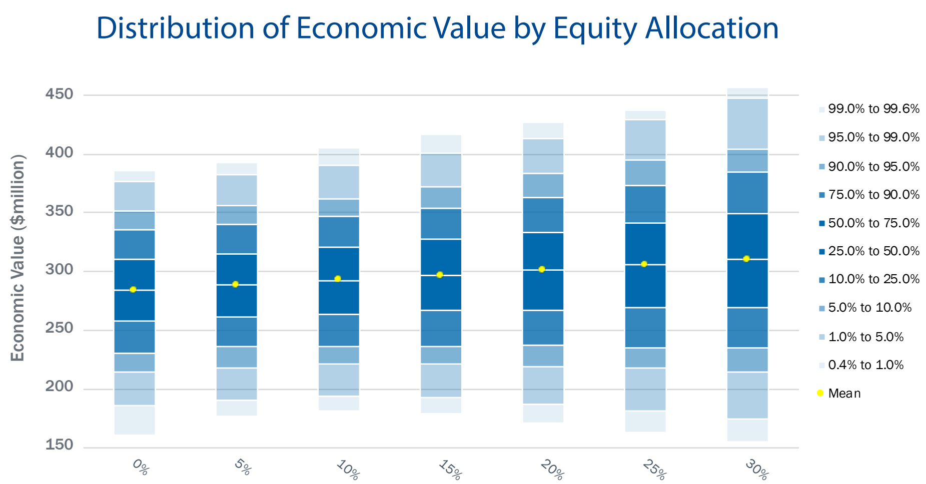
Prepared by Conning, Inc. Source: Conning Allocation Optimizer™ using investment returns and liability cash flows from GEMS® Economic Scenario Generator. Example provided for illustrative purposes only.

*Economic value is equivalent to a company's surplus or equity but calculated on an economic basis rather than an accounting basis. This means all assets are market to market value, liabilities are stated on a present value basis, and it includes the net cash flows generated by future operations.

Evaluating Alternative Investment Strategies: To identify the most efficient risk/reward strategy, Conning can display the impact of significant investment decisions (such as fixed income duration or a particular asset class allocation), to determine how it affects key financial metrics such as investment income, surplus volatility, and economic value. Ignoring those measures could lead to less optimal choices.

For example, the distribution of economic value by equity strategy shows that a company can reach maximum diversification benefit from a 10% allocation, while downside risk increases beyond a 15% allocation (Figure 4).

Figure 4 Evaluating Alternative Investment Strategies

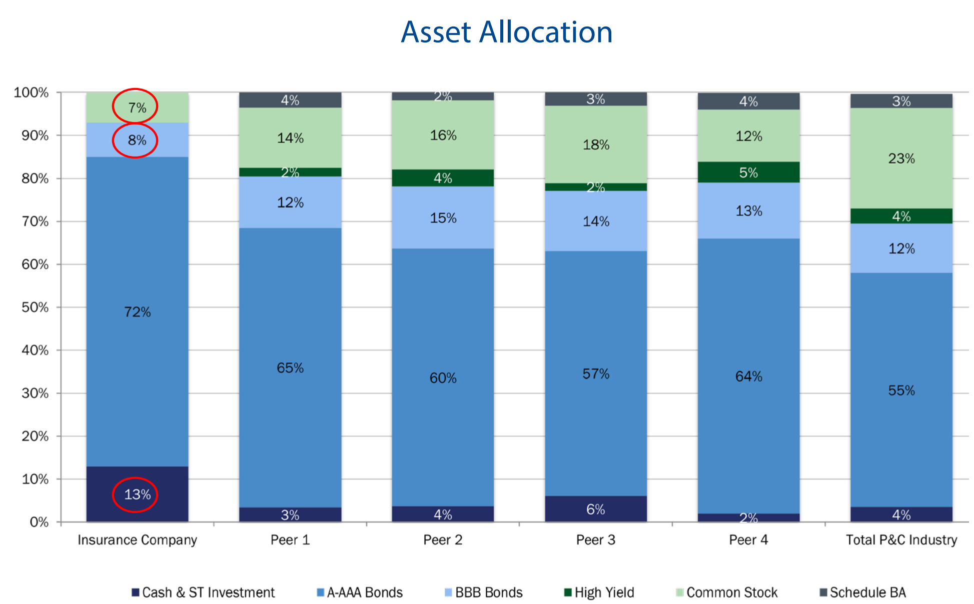


Prepared by Conning, Inc. Source: Conning Allocation Optimizer™ using investment returns and liability cash flows from GEMS® Economic Scenario Generator. Example provided for illustrative purposes only.

Peer Analysis: Conning assembles peer analysis reports for its clients which include information on the investment portfolio, underwriting & operational aspects of their business. With this tool a client can see how their competitors' portfolios are structured to help them evaluate their current positioning relative to industry or peer norms.

Peer analysis provides a company's management useful insight into trends and opportunities to assist in determining how much risk they are comfortable taking on the investment side of the balance sheet. Peer analysis can also inform where a company might be an outlier relative to their peers and industry. This can prepare management for possible questions from regulators and rating agencies who are often using similar tools.

Figure 5 Peer Analysis: Asset Allocation

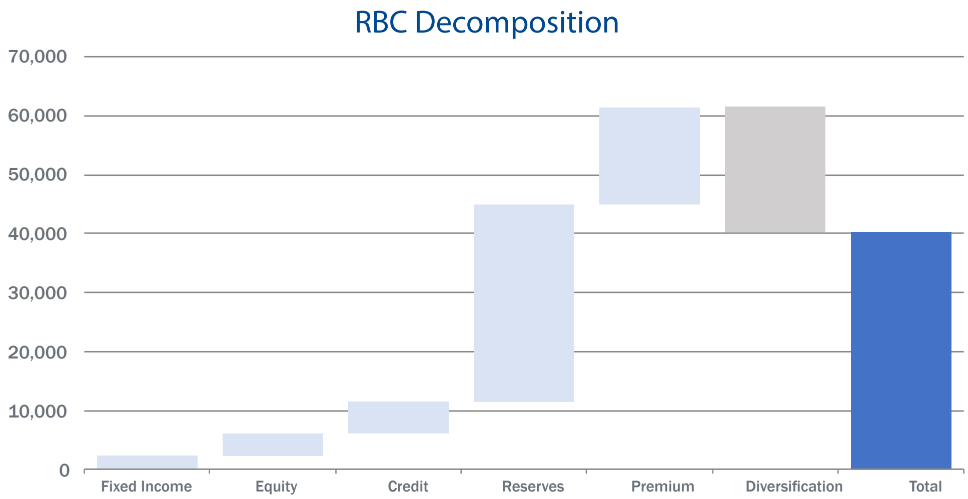


Prepared by Conning, Inc. Example provided for illustrative purposes only.

Figure 5 demonstrates how an insurance company profile might be more conservative relative to its peers, which translates to a less optimal portfolio and more forgone investment opportunities.

Risk-Based Capital Analysis: Conning measures the relative contribution of the different risk elements and how a proposed investment strategy impacts company's capital including RBC, BCAR or other relevant rating agency or regulatory frameworks. Figure 6 demonstrates the contribution of major risks factors and the magnitude of diversification among those risks.

Figure 6 Risk-Based Capital (RBC) Analysis

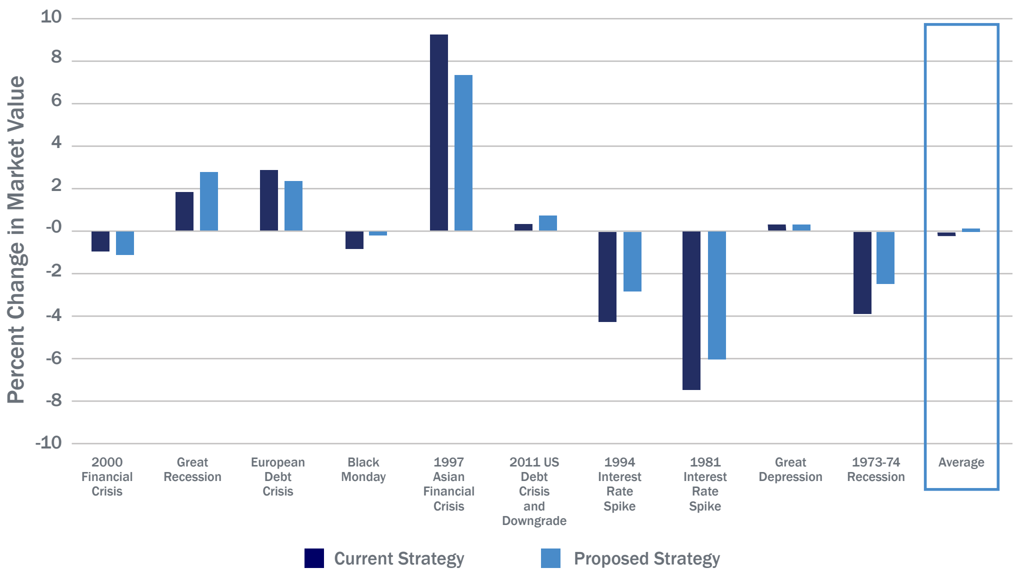


Prepared by Conning, Inc. using sample data. Example provided for illustrative purposes only.

Risk Management: A valuable step in validating an investment decision is understanding downside risk. This entails a back testing analysis or performing "what if" deterministic scenarios to see how a proposed investment is expected to affect company's financials in extreme circumstances.

For example, Figure 7 demonstrates how a proposed strategy could have performed historically during major financial or economic events compared to the existing portfolio.

Figure 7 Historical Stress Test

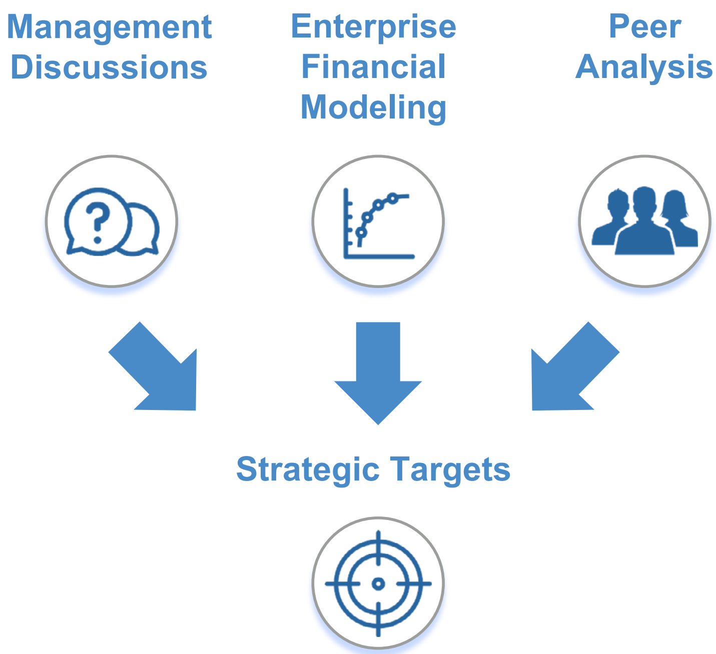


Prepared by Conning, Inc. Source: Conning Allocation Optimizer™ using investment returns and liability cash flows from GEMS® Economic Scenario Generator. Example provided for illustrative purposes only.

Strategic Targets

Through the various types of analysis involved in the SAA process, Conning works to empower insurers to not only find an optimal investment strategy that fits their unique needs and risk tolerance, but also to communicate why a particular strategy is the most optimal for their company (Figure 8).

Figure 8 Strategic Targets

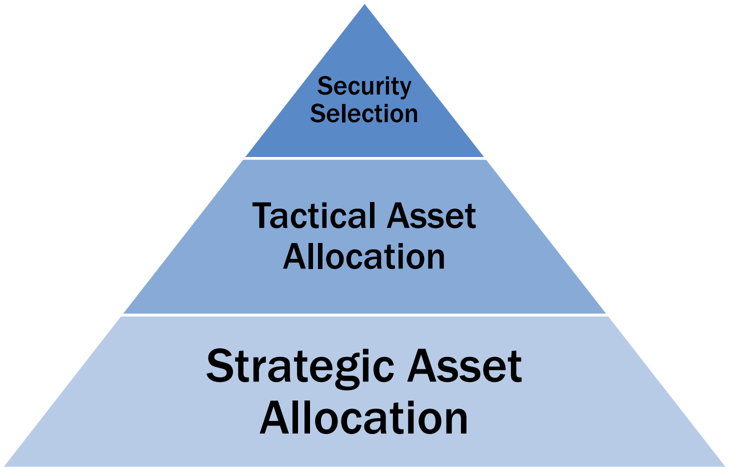


Prepared by Conning, Inc.

The optimal result is an investment strategy customized to fit a P&C insurer's risk profile that improves return and reduces risk both economically and in statutory terms. With an optimal investment strategy in hand, the next step in the process is a revision to the investment policy, guidelines, and performance benchmark(s) to reflect the new strategy.

Conning's institutional solutions and portfolio management teams work with clients to implement the SAA output, which sets a long-term framework for the enterprise to meet its stated goals and risk preferences. The SAA process essentially structures the portfolio risk factors or beta to achieve long term success. The portfolio manager can stay focused on executing through sector calls and security selections to deliver the insurance company's alpha or excess returns targets.

Figure 9 Customized Portfolio Approach



Strategic Asset Allocation is an important extension of an insurer's risk & capital management. Conning's SAA approach is customized for each client and supports the company's unique insurance operations and risk profile. When partnering with P&C insurers, Conning strives to become an important extension of a client's financial, risk, and capital management process. We collaborate to find new opportunities to ensure the company's unique needs are satisfied while enhancing company value and mitigating unnecessary risks.

About Conning

Conning (www.conning.com) is a leading investment management firm with a long history of serving the insurance industry. Conning supports institutional investors, including insurers and pension plans, with investment solutions, risk modeling software, and industry research. Founded in 1912, Conning has investment centers in Asia, Europe and North America.

Disclosures:

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Footnote:

[1] For more information and disclosures regarding our industry recognition, please visit our website – https://www.conning.com/about-us/industry-recognition

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