

6th Seminar on Current Issues in General Insurance (CIGI)

Hotel Sea Princess, Mumbai
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Asset Management & ALM in Current Market Scenario

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Asset Management & ALM

in Current Market Scenario



Disclaimer

All the points covered in this presentation are our personal views and they must not be construed as methodology employed by our current and/or previous organization(s) in any shape or form.

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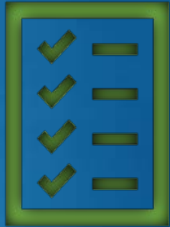
Contents:

Concept of Asset Liability Management

Asset Management

Macroeconomic Trends

Interest Rate and Equity Outlook



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Concept of ALM in Non Life Insurance

- Statutory Requirement (As per circular dated 3rd January 2012)
- Projection of asset proceeds as well as liability outgo
- Stress testing mandate: Assess and manage risks based on different scenarios
- Helps in evaluating an optimal investment strategy

Liabilities in Non Life Insurance

- Technical provisions form a major part of the liabilities.
- There's uncertainty in timing and quantum of the cashflows due to various factors :
 - Reporting and settlement delays
 - Inflation sensitivity
 - Exposure to large claims, catastrophes and accumulation risk

Liabilities in Non Life Insurance

- There's uncertainty in timing and quantum of the cashflows due to various factors :
 - Exposure to other emerging risks (legislative, cyber etc.)
 - Reinsurance delay and default

Risk Measurement & Management

Asset Liability Management

Interest Rate Risk

Duration Matching

Liquidity Risk

Higher Amount of Liquid Assets

Credit Risk

Higher Rated Reinsurers

Currency Risk

Currency Matching

Practical Considerations for ALM in Non Life

Judgement is required in the ways one may consider:

- Allocation of assets across Lines of Business.
- Advance Deposit Premium for Motor Business
- Treatment of Policyholder and/or Shareholder Funds
- Other Liabilities/ Net current assets
- Dealing with default in assets and potential recoveries

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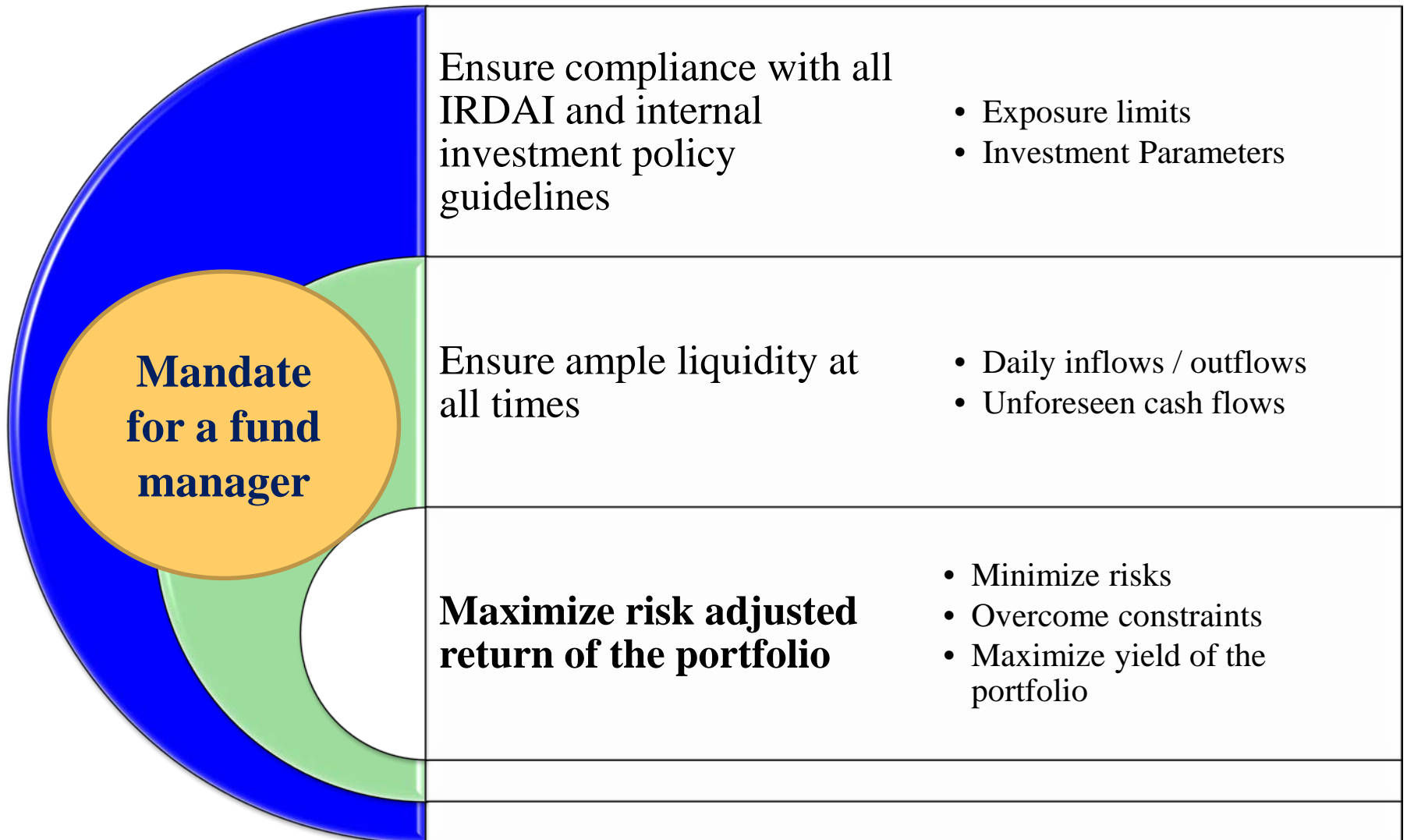
Asset Management

Macroeconomic Trends

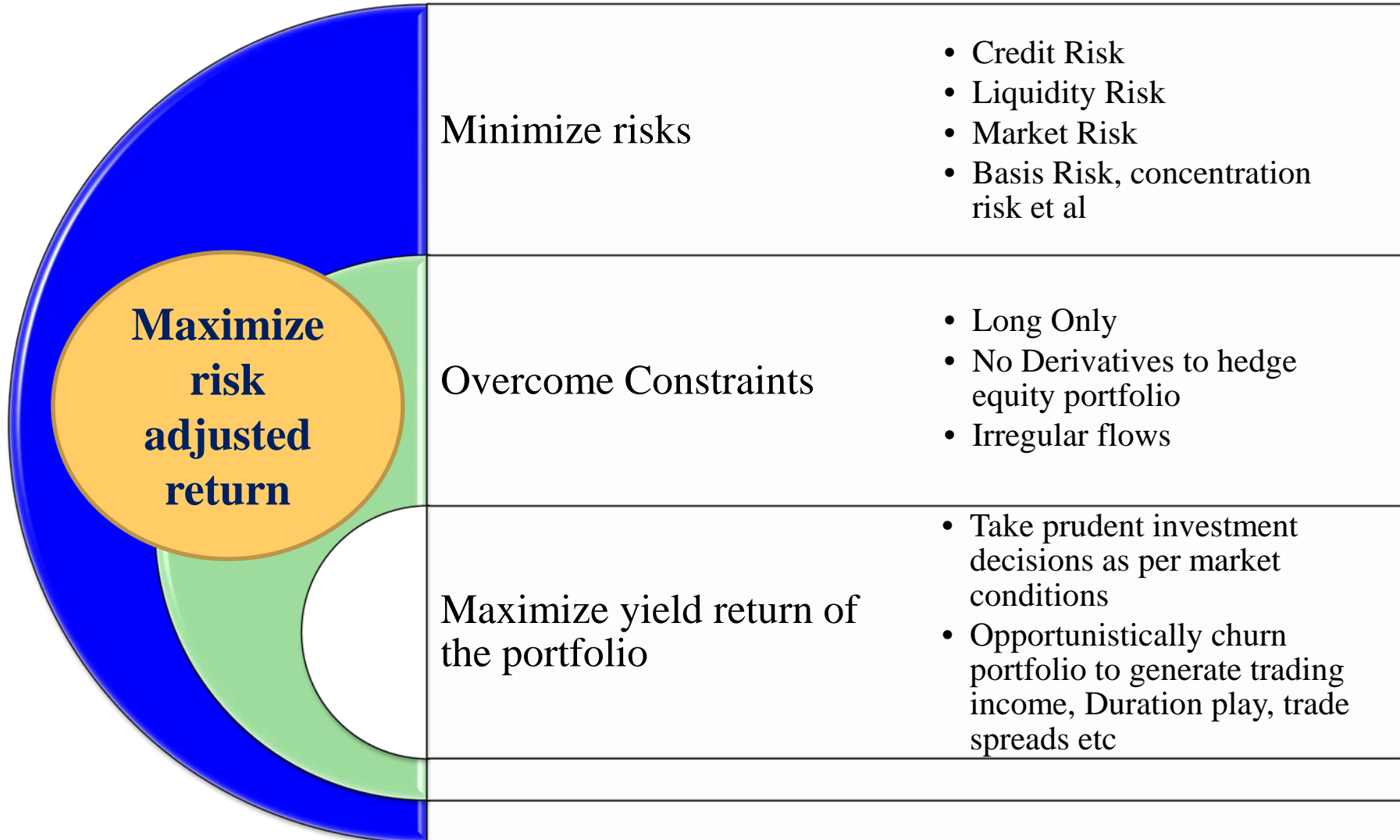
Interest Rate and Equity Outlook



Asset Management



Asset Management



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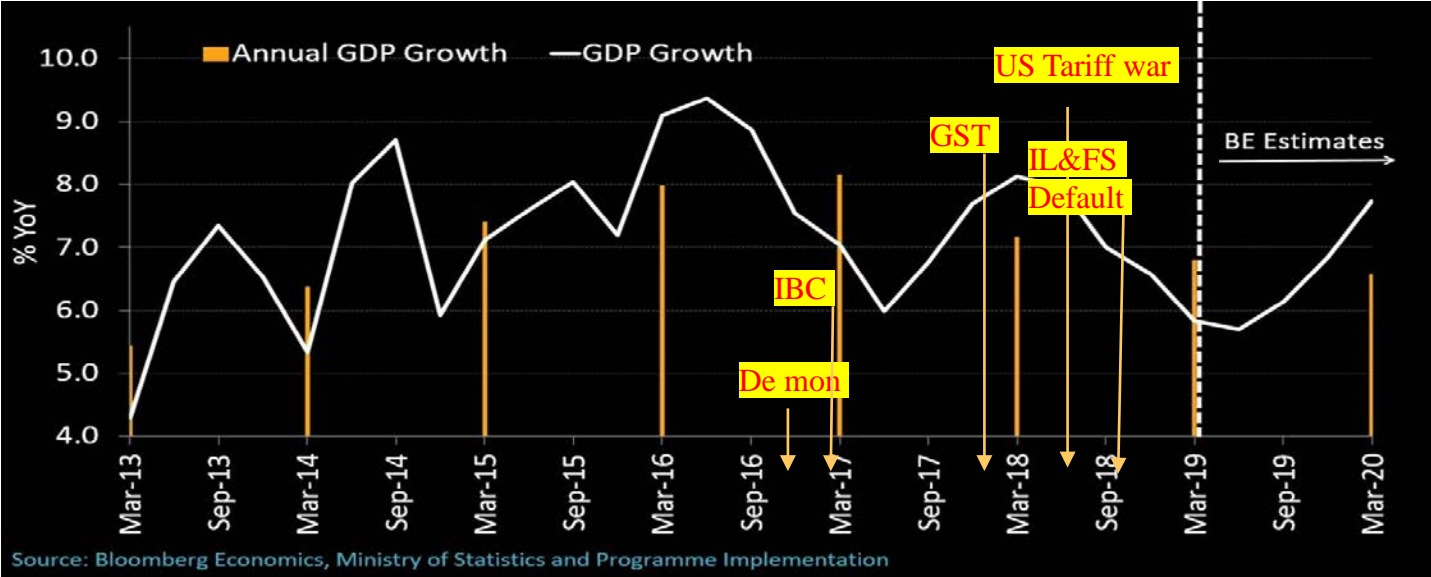
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Macros – Domestic: Cross winds & Head winds



Source: Bloomberg Economics, Ministry of Statistics and Programme Implementation

Cutting GDP growth forecast. Earnings downgrade across multiple sectors. However, revival expected in 2HFY20. Business confidence to get boost from slew of measures announced by the FM.

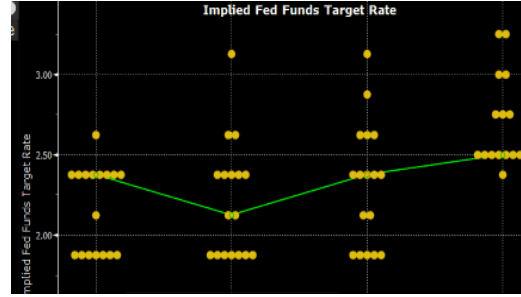
INDICATOR	4Q18	1Q19	2Q19	3Q19	4Q19	1Q20	2Q20	2018	2019	2020
GDP, YoY %	6.6	5.8	5.7	6.1	6.8	7.7	7.8	7.2	6.9	6.6
GVA, YoY %	6.3	5.7	5.6	6.0	6.7	7.6	7.7	6.9	6.8	6.5
Headline CPI, YoY%	2.6	2.5	3.1	3.3	3.7	3.6	3.5	3.6	3.4	3.4
USD/INR	71.8	70.5	69.4	69.2	68.3	67.1	67.1	64.5	69.9	68.4
Central Bank Rate	6.50	6.25	5.75	5.50	5.50	5.25	5.25	6.00	6.25	5.25

Macros – Global: US – Goldilocks; China – slowdown; Europe - Doom & Gloom; Japan - stable

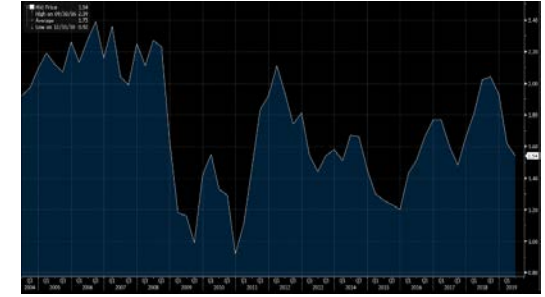
US



U6 Unemployment Rate



FOMC Dot Plot Projection



Core PCE Index

Source: Bloomberg

China

Growth slowed to 6.2% in Q2, its weakest pace in 27 years

Europe & Japan

Germany likely to head into recession, Q2 GDP -0.01%. Bund Yields – ve.
Boris Johnson may go for no deal Brexit
Japan Q2 GDP growth at 0.4%. 3rd straight quarter of GDP expansion.

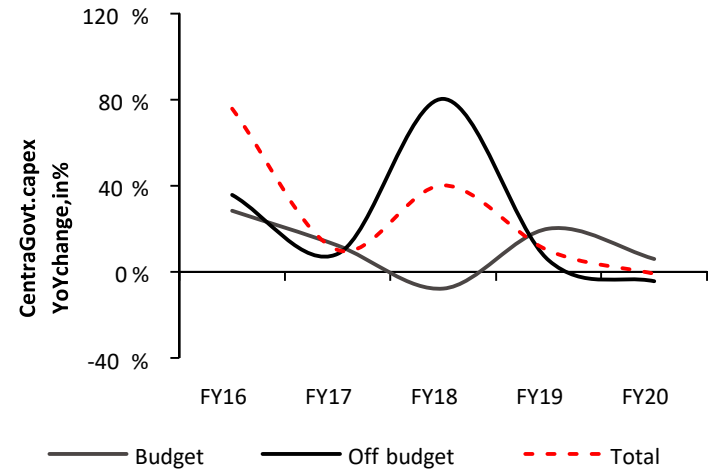
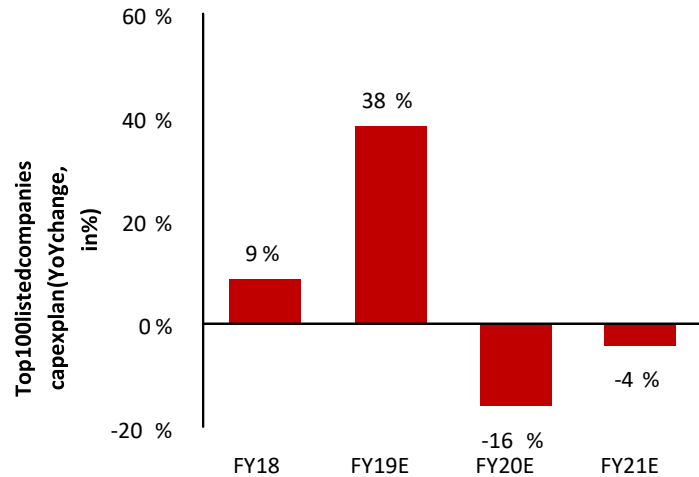
Rising odds of recession

Trade war: Estimate that China GDP will be hit by 1%; global impact of \$585 bn to world GDP. The tweet is mightier than the tariff. Uncertainty shock dwarfs the direct impact of tariffs.

Whipsawing markets

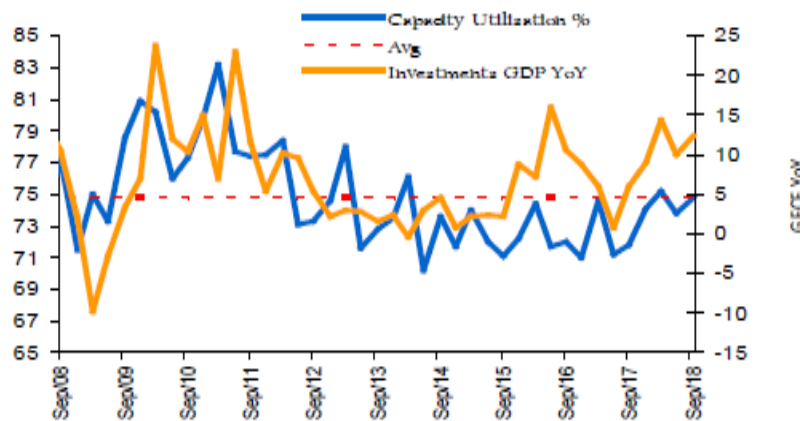


Macros – Domestic: Cross winds & Head winds



Source: Bloomberg, Ambit Capital research

Economy Capacity Utilization & GFCF

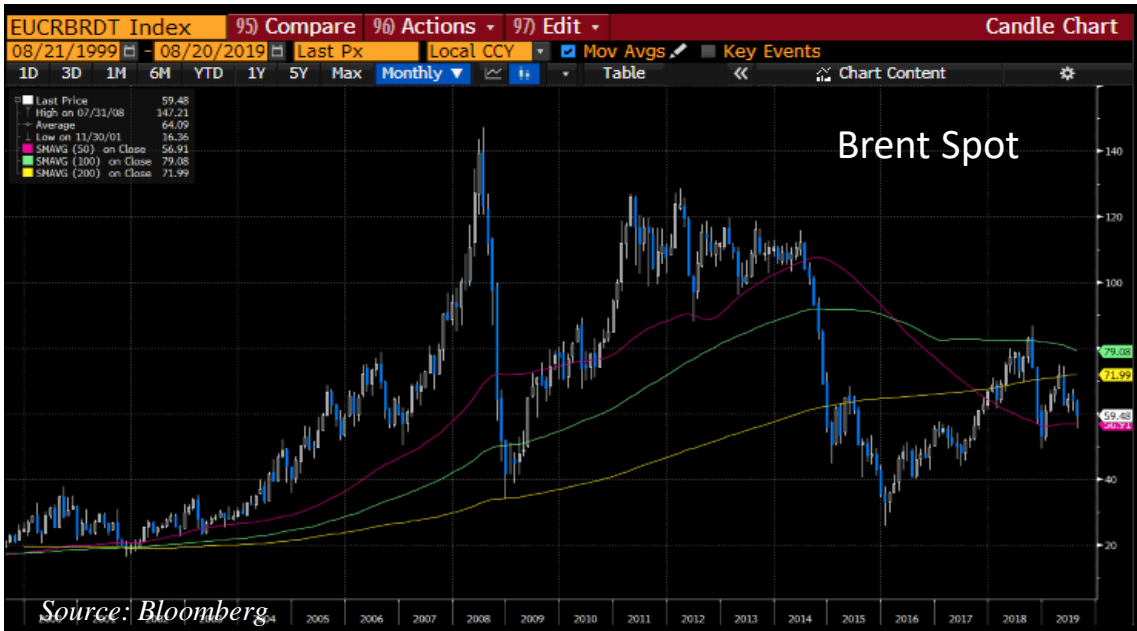


Source: RBI, Bloomberg

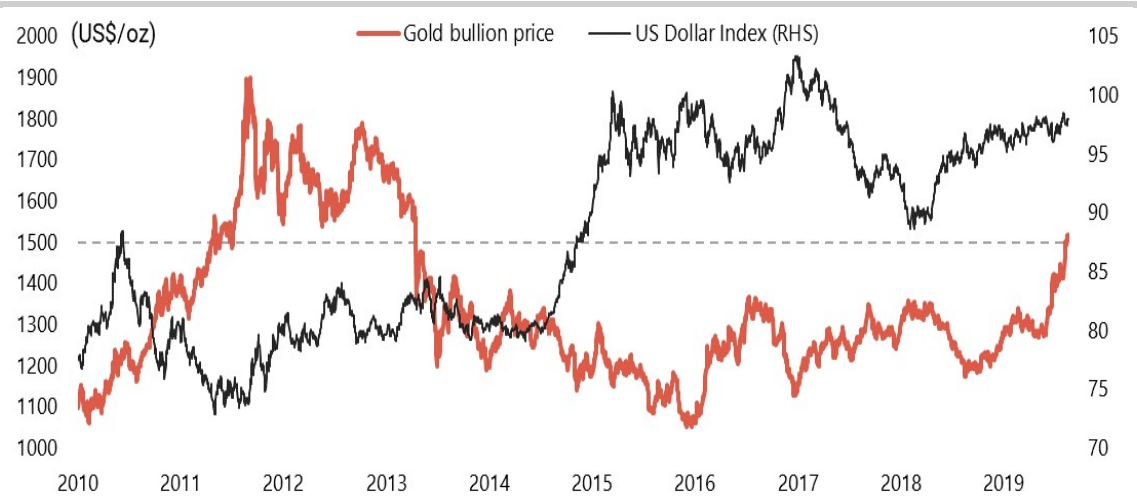
Growth in capex was expected but has not taken off so far. However, Policy stimulus, monsoon turnaround and stable oil may still help India grow faster than others.

Monsoon turnaround - From a deficit of 33% in June to surplus of 34% in August. Forecast that El Nino may remain in neutral zone augurs well for remaining SW monsoon and also NE monsoon thereafter.

Oil & Gold



Global oil prices are expected to remain benign. Demand is weak and US supply growth is strong. Geopolitics risks to stay, may result in heightened volatility.



Source: Bloomberg

Gold Rush: Risk off positioning with trade war uncertainty and multitude of recessionary signs. Gold ETF holding has surged to 6 year high and Silver ETF holdings is at all time high. Gold has given YTD return of 20%.

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Interest Rate Outlook

Latest yield curve inversion sends ominous warning

Spread between 2-year and 10-year Treasury bonds (percentage points)

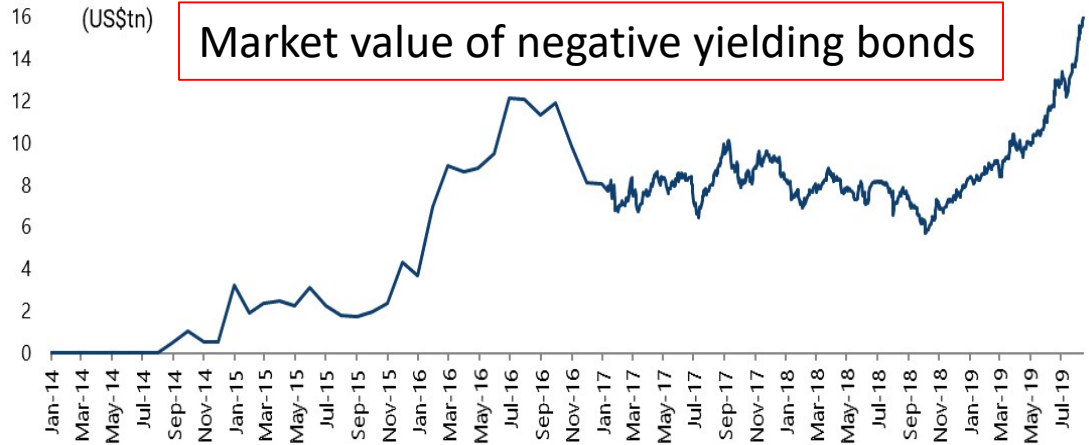


Source: US Treasury

FINANCIAL TIMES

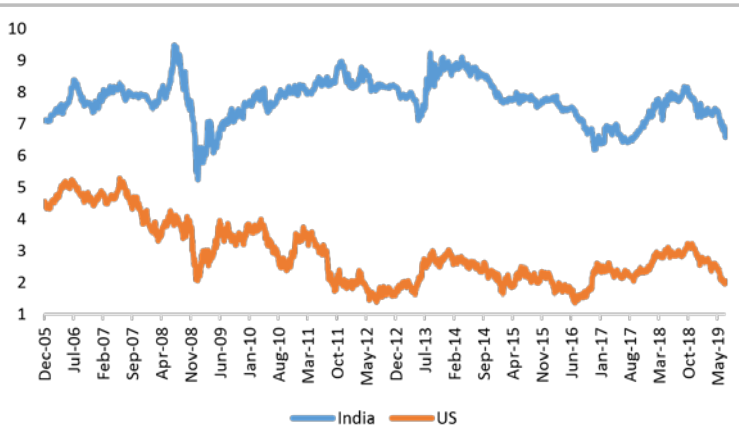
(US\$tn)

Market value of negative yielding bonds



Source: Bloomberg

10 Yr G-sec Yield India vis-a-vis US (%)



Source: SBI Research

First rate cut by Fed since 2008. Probability to cut again by 25 bps is 72%. But markets waiting for commentary at Jackson Hole Symposium to take clues whether 'mid-cycle adjustment' stance has changed. Treasury yields sink to 3 year lows on 'No-limit' Trade War fear.

RBI MPC's unprecedented decision on Aug 7 to cut the repo rate by 35 basis points to 5.40%. CPI remains well under target of 4%. Focus is now growth. Transmission of rate cut is being monitored ever more closely. Accommodative stance and dovish commentary indicates more cuts on cards.

Equity Outlook



Source: Bloomberg

Exhibit 1: Market valuations look reasonable in the historical context
1-y rolling forward PE of Nifty-50 Index, March fiscal year-ends, 2004-20 (X)



Source: BSE, RBI, Kotak Institutional Equities estimates

Credit Crunch has taken it's toll. NBFCs, autos, real estate, infra and many banks have been severely impacted. Telecom and Power have already been grappling with host of issues. IT & Cement have outperformed. Expect BFSI, FMCG, FMEG & Capital goods to lead recovery.

When will the risk appetite return?

Making India a \$ 5 trillion Economy.

Who will be the leaders, wealth creators and disruptors?



Happy Hunting