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Impact of macroeconomic environment on insurance industry

Rajeev Sharan

28 November 2023

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Agenda

- Macroeconomic outlook
- Impact of macroeconomic environment on insurance industry performance
- Role of alternative scenarios in risk management



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Macroeconomic outlook

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The global macro environment

Societal environment



Growing middle class, urbanization, widening talent gaps, and increasing life expectancy

- Growing middle class in developing markets
- Mass migration & urbanization
- Workforce transition through automation & talent gaps
- Increasing life expectancy

Macroeconomic environment



High inflation and low growth environment

- Low real growth rates
- High interest rate
- Geopolitical tensions
- Increasing protectionism

Business environment



Increasing competition, decreasing company lifetime and tech companies as new winners

- Cross-industry disruption & increasing competition
- Strengthening of tech superstar companies, e.g., via ecosystems
- Decreasing average company lifetime

Geopolitical environment



Rising geopolitical tensions

- Russia-Ukraine war
- Middle East crisis
- East-West geopolitical tensions
- Supply chain disruption

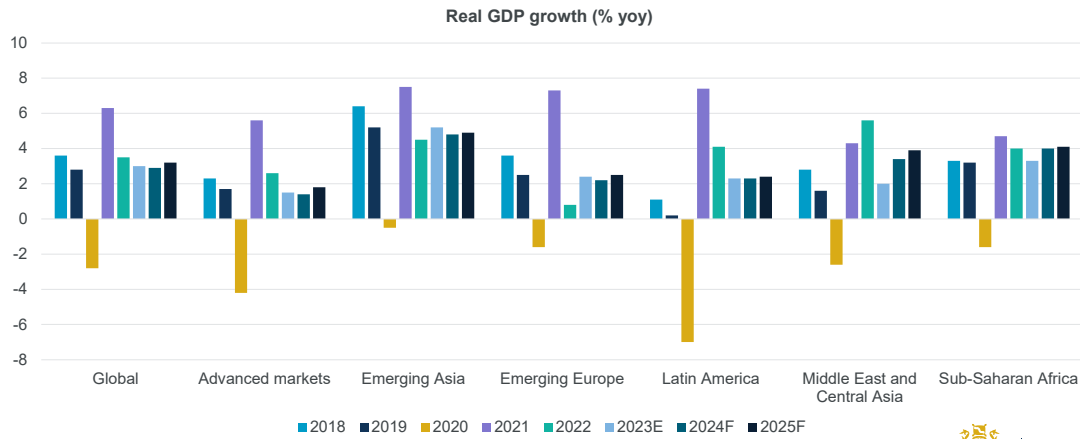


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Economic activity is still below the pre-pandemic levels



Source: IMF



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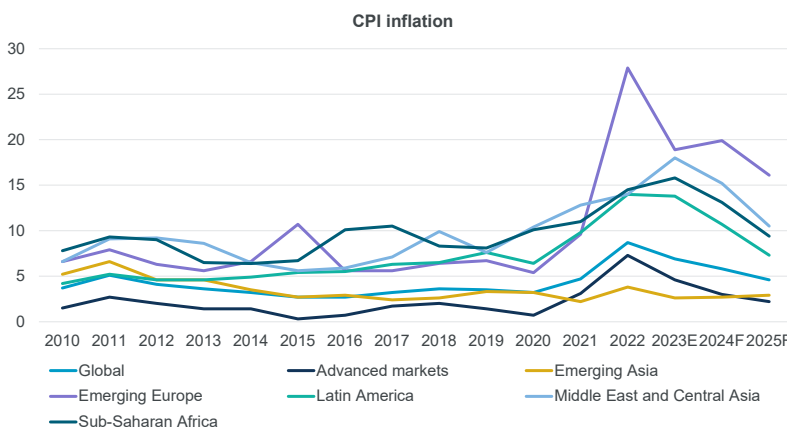
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Inflation remains above the historical average and central bank's target in many countries



Source: IMF, Bloomberg

Key metrics

Country	Latest Inflation	5 Year Average	Inflation Target
US	4.2%	3.0%	2.0%
EZ	5.3%	3.5%	2.0%
UK	6.8%	4.2%	2.0%
NG	24.1%	15.8%	9.0%
ZA	4.7%	4.9%	6.0%
KE	6.7%	6.3%	5.0%
GH	43.1%	18.2%	8.0%
HK	1.8%	1.8%	No Target
KR	3.4%	2.3%	2.0%
CN	-0.3%	1.9%	3.0%
SG	4.1%	2.5%	No Target
IN	7.4%	5.4%	4.0%
TW	1.9%	1.4%	No Target
MY	2.0%	1.5%	No Target
ID	3.3%	2.9%	3.5%
PH	5.3%	4.2%	3.0%
TH	0.9%	1.8%	2.5%



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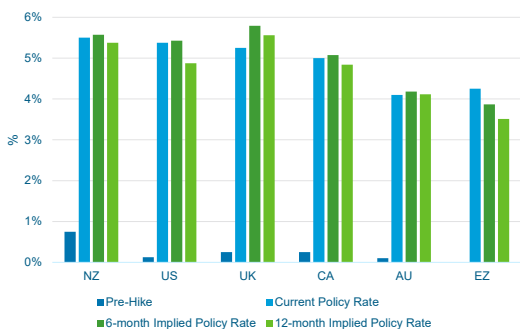
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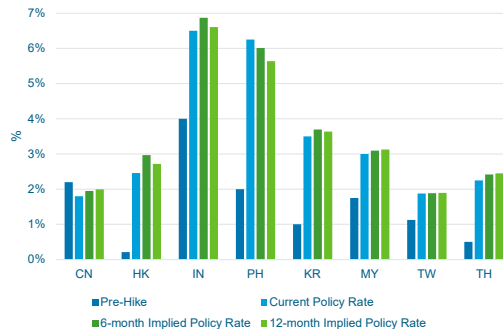
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Interest rates have peaked

Policy rate (%) in Developed markets



Policy rate (%) in Asia



Source: Bloomberg. Pre-hike period refers to rates of respective countries as of end 2021. Current policy rate refer to rates as of 5th Sept 2023. 6-month implied policy rate refer to the implied rates 6 months hence from the date effective 5th Sept 2023 sourced from Bloomberg. 12-month implied policy rate refer to the implied rates 12 months hence from the date effective 5th Sept 2023 sourced from Bloomberg. Country Codes: New Zealand (NZ), United States (US), United Kingdom (UK), Canada (CA), Australia (AU), Euro Zone (EZ), China (CN), Hong Kong (HK), India (IN), Philippines (PH), South Korea (KR), Malaysia (MY), Taiwan (TW), Thailand (TH).



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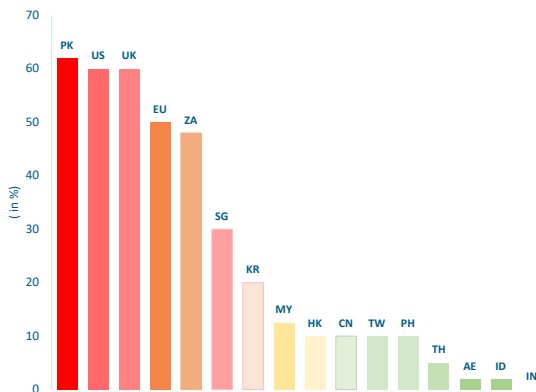
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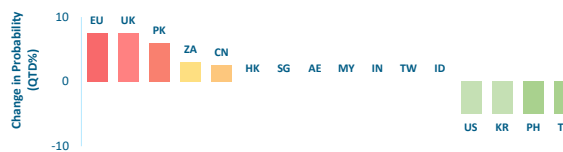
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Probability of recession

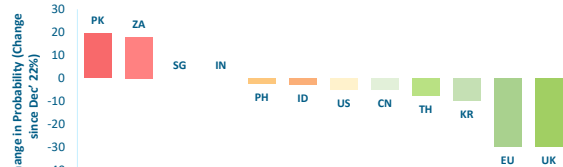
Probability of Recession



Change in Probability of Recession since 2Q 2023



Change in probability of recession since Dec 2022



Notes: LHS: Recession Probability (Y-axis) displays the median forecasted probability of recession (%) in next one year, sourced from Bloomberg as of 30th August 2023. RHS Top: Change in probability of recession (%) since last update, RHS Bottom: Year to date change in probability of recession. Country codes : United States (US), Euro Area (EU), United Kingdom (UK) African Economies: Nigeria (NG), South Africa (ZA), Kenya (KE), Ghana (GH), Hong Kong (HK), Korea (KR), China (CN), Singapore (SG), India (IN), Taiwan (TW), United Arab Emirates (AE), Malaysia (MY), Indonesia (ID), Philippines (PH), Thailand (TH)



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Impact of macroeconomic environment on insurance industry performance

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Poll #1

In general, high inflation and high interest rate environment negatively impact life insurer's profitability?

- 1) True
- 2) False



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The macroeconomic environment creates challenges as well as opportunities

Macroeconomic dynamics

- Slowdown in economic growth
- High inflation
- High interest rates
- Rising unemployment
- Geopolitical tensions

Impact on insurance industry

- Insurance demand
- Claims inflation
- Investment returns
- Balance sheet impact
- Rates



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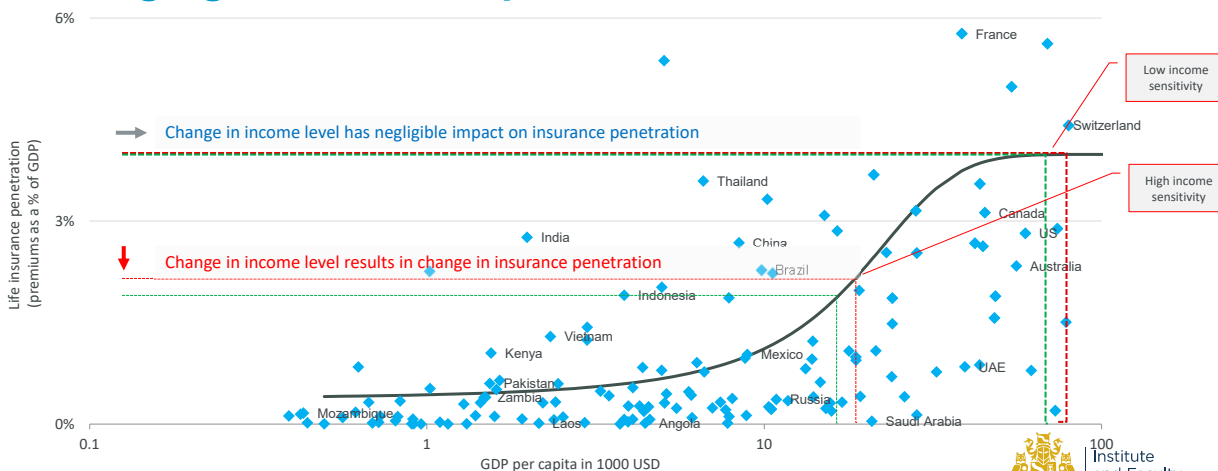
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Insurance demand is more sensitive to income levels in emerging markets compared to advanced markets



Note: The insurance S-curve chart is for illustration purpose only. It may not accurately represent the life insurance penetration and income level in the markets included in this chart.



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High inflation negatively impacts non-life insurance profitability

Line of business	Impact	Comments
Property	Negative	Increase in price of materials as well as higher wages
Motor, physical damage	Negative	Increase in prices of spare parts due to supply chain imbalances, and wage growth
Motor, bodily injury	Negative	Wage growth and medical cost inflation
Liability	Negative	Wage growth, medical, and social inflation
Health	Negative	Medical cost inflation
Mortality	Neutral	Benefits are defined at the time of underwriting



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High interest rates are positive for life insurance industry

Line of business (Life)	Indicator	Impact	Comments
Protection products	Demand	Neutral to positive	Increase in demand of life insurance products with guarantees
	Mortality claims	Neutral	Both premiums and benefits are defined at the time of inception
Life savings, guarantees	Demand	Negative/Positive	Higher lapse rate (in-force); Increased demand for products with guarantees
	Profitability	Positive	Higher investment return; Lower reserves for guarantees
Life savings, unit linked	Demand	Negative	Higher lapse rate as demand shifts toward products with guarantees
	Profitability	Neutral	Investment risk is borne by the policyholders
Annuity	Demand	Positive	Increased attractiveness of annuity products
	Profitability	Positive	Higher investment return; Lower reserves for guarantees



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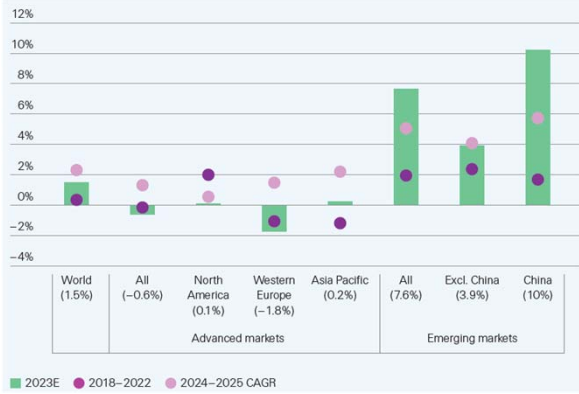
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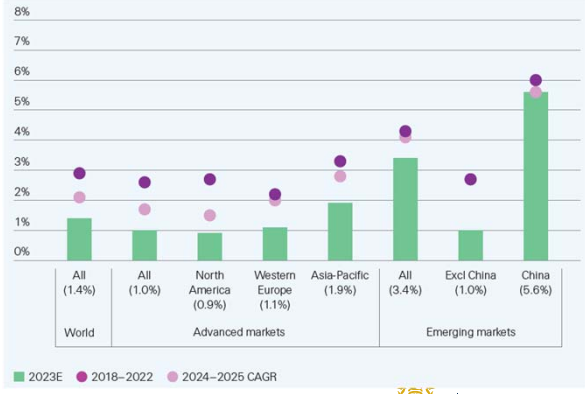
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Both life and non-life premiums expected to recover in 2024-2025

Life premiums real growth by regions (2023 in brackets)



Non-life premiums real growth by regions (2023 in brackets)



Source: Swiss Re Institute, sigma 6/2023



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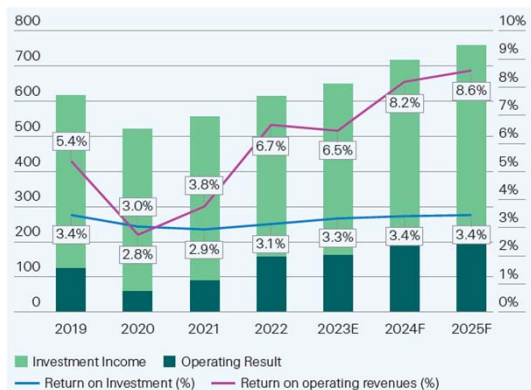
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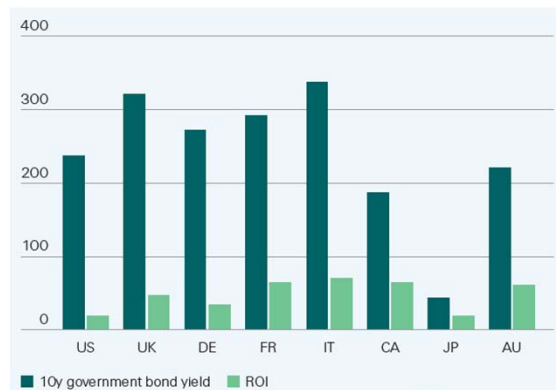
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Life insurance profitability to improve as investment portfolio rolls to higher yielding assets

Life insurance operating and investment profitability



Estimated investment yield changes over 2022-23 (bps)



Source: Swiss Re Institute, sigma 6/2023



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Role of alternative scenarios in risk management

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Poll #2

What's the main purpose of scenario analysis in financial services industry?

- 1) Identify new business opportunities
- 2) Assess the strength and resilience of the financial services company in an adverse environment
- 3) Avoid potential losses and maximize gains
- 4) All the above



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Scenario analysis helps assess strength and resilience of financial institutions in an adverse environment

The importance of stress testing

Role of scenario design in stress testing



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Approached to scenario design

Historical scenario analysis

Hypothetical scenario analysis

Stochastic scenario analysis



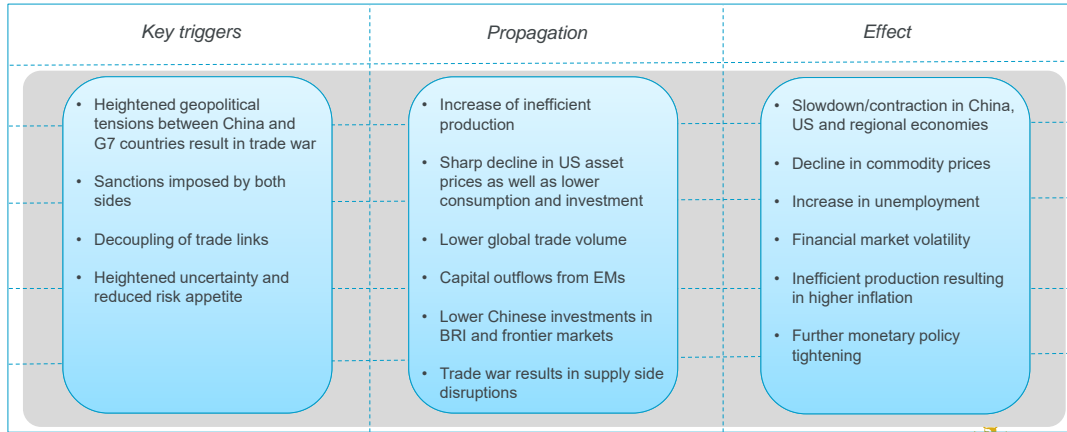
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An example: Geopolitical tension between East and West



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