

Private Credit Further Developments - Terms of Reference

Background

There have been two successful working parties exploring the development of the private credit market covered under the Life Insurance and Finance & Investment Boards:

- <https://www.actuaries.org.uk/practice-areas/finance-and-investment/disbanded-research-working-parties/private-credit-investment-insurers-meeting-regulatory-requirements-working-party>
- <https://www.actuaries.org.uk/practice-areas/life/disbanded-research-working-parties/asset-liability-management-alm-non-traditional-assets>

The key outputs of these working parties were:

- Observations of industry practice, designed to provoke ideas for best practice amongst insurers
- An “encyclopaedia” of private credit, considering a number of different asset classes and their application to insurers and pension schemes.

Investment in private credit continues to increase across the insurance market and within pension schemes. As such, this working party is expected to pick up where these working parties left off and fill in some of the gaps.

Purpose

The purpose of the working party is to:

- Review current literature, particularly focusing on the analysis already performed by the previous working parties, to ensure that the gaps suggested in this ToR are appropriate and to ensure that current research into the gaps is taken into account.
- Analyse gaps in current research and agree areas of research to be taken forwards.
- Respond to consultation papers from regulators and from government bodies. Whilst we expect to liaise most closely with UK and European bodies, it may be helpful to consult or consider guidance from other regulators (e.g. BMA).
- Provoke thought leadership and innovation within the industry through presentations and forums to gain wider input.

Approach

A working party is proposed to be formed under the sponsorship of the Finance & Investment Committee (FIRC) to take this work forwards. This working party will be cross practice with the Life Insurance Research Committee (LRC) and the Pensions Research Committee (PRC).

Once the gaps and scope have been agreed within the working party, this should be discussed and reviewed by FIRC.

Composition of working party

We recommend a working party of ten members of the actuarial profession working within life insurance, pensions and investment to perform this research.

Specific goals and areas to be investigated

- A summary of existing research material.
- The areas which are currently expected to require further research are:
 - **Broadening the asset classes previously researched into sub investment grade assets.** Most of the existing research considers only investment grade or equivalent debt. But there is a larger body of investments under consideration from global insurers including leveraged loans, SME loans, CLOs etc and these warrant further consideration.
 - **Managing assets through downgrade, default or restructure.** The working parties so far have focused on opportunities and risks but not what happens when things go wrong. We would like the working party to research how insurers or pension schemes should leverage banks, asset managers and other third parties as well as their own expertise to manage through a downturn.
 - **Consider the appropriateness of a private credit strategy in investing sustainably.** We expect the working party to test the hypothesis that an investment strategy including a higher allocation to private credit will result in a more sustainable investment strategy than otherwise. We do not expect this to be the primary focus given there is lots of other research in this area but feel it should be considered specifically for private credit.
 - PRA is expected to publish a consultation paper on **modelling private credit under stress** in insurance companies. It is likely that this will provoke some thought and potential research for this working party.
- The working party is also expected to liaise with regulators and lobbying bodies (e.g. ABI) where possible.

Research methods

The working party will perform a literature review to avoid reinventing prior thought.

The research will then consider a small amount of modelling (e.g. simple studies on liquidity strains) to consider the question of allocation. The other considerations are likely to be largely qualitative and utilising the industry knowledge of the volunteers.

Output

The ultimate aim will be to develop a sessional paper presenting the results of the work. We would expect the working party to wish to present at IFOA conferences towards the end of its research period.

Recommendations

The working party is not expected to make any explicit recommendations.

Potential timetable

Agreement of gaps and areas for WP research - Autumn / Winter 2019 - 2020

Collation of analysis and feedback - Spring 2020

Presentation of sessional paper - Summer / Autumn 2020

Funding

No expectation of external funding.