

# LOW-INTEREST RATE TASK FORCE

Readiness & Advocacy Committee – Kick-off

March 11, 2020

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# AGENDA

<b>01</b>	<b>INTRODUCTIONS &amp; OVERVIEW OF TASK FORCE</b>	5 min
<b>02</b>	<b>WHAT WE'VE HEARD: INITIAL INDUSTRY PERSPECTIVES</b>	10 min
<b>03</b>	<b>WHAT NOW?</b>	
	• <b>READINESS PLAYBOOK &amp; NEAR-TERM RESPONSE</b>	20 min
	• <b>REGULATORY ADVOCACY PRIORITIES</b>	20 min
<b>04</b>	<b>NEXT STEPS</b>	5 min

# INTRODUCTIONS

## READINESS & ADVOCACY COMMITTEE MEMBERS

Keith Werschke	Pacific Life
Linda Durman	Sammons
Dan Jackson	Athene
Michael Slipowitz	Guardian Life
Stephen Turer	Lincoln
Meagan Phillips	Securian
Bill White	USAA
Ken McCullum	Principal
Holly Snyder	Nationwide
Todd Henderson	Western & Southern
Andrew Michie	Oneamerica
Tim Corbett	Mass Mutual
Ellen Cooper	Lincoln
Raj Krishnan	F&G Life
Paul Gerard	Ohio National

Liz Brill	NY Life
Tom Leonardi	AIG
Jim Mikus	Ameritas
Cliff Lange	Boston Mutual
Joe Engelhard	Met Life
Joel Steinberg	New York Life
Jason Klawonn	Northwestern Mutual
Connie Tang	Prudential

## FACILITATORS

Dave Levenson	LIMRA
Marianne Purushotham	
Kristin Ricci	Oliver Wyman
Scott Campion	
Paul Graham	ACLI

# PROJECT OVERVIEW

The Low-Interest Rate Task Force was brought together to determine:



How ready is the industry?



What can be done now to prepare?



What actions can be taken if/when it does happen?



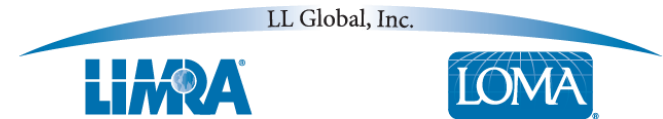
What advocacy efforts can be pursued?

## Facilitators:



**OLIVER WYMAN**

*Strategic support*



*Industry group support*

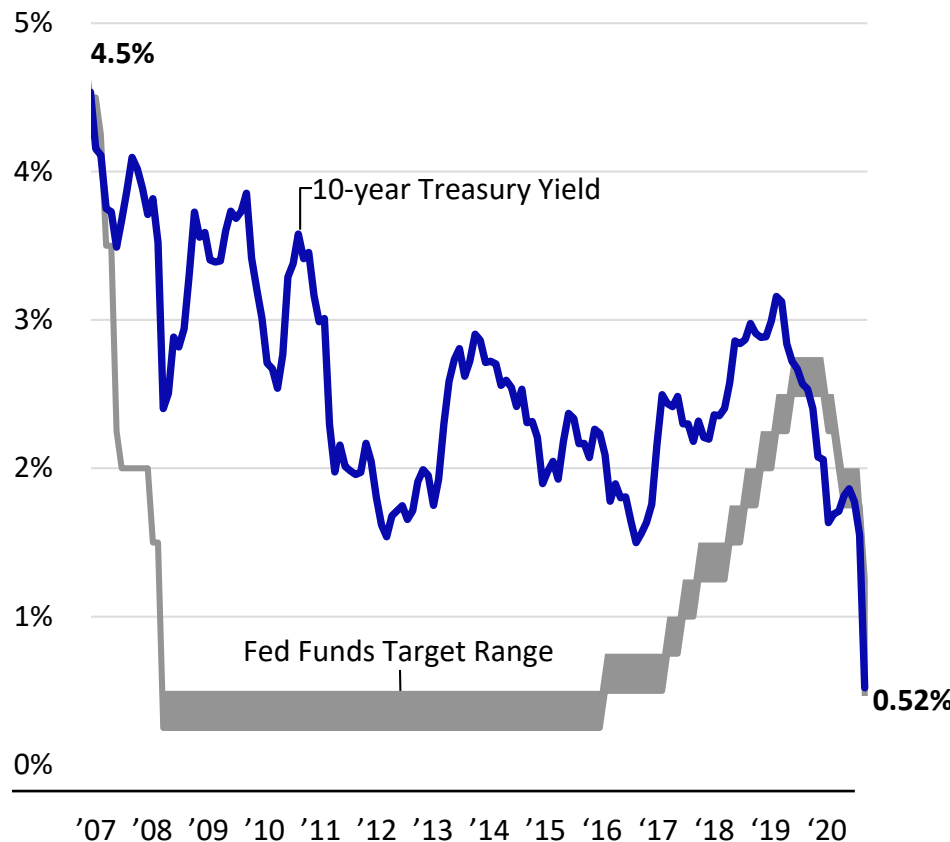


*Advocacy support*

**~30** life insurers represented in total

# EVOLVING MARKET CONDITIONS ACCELERATE THE IMPORTANCE OF ASSESSING READINESS & RESPONDING TO THE EMERGING MARKET ENVIRONMENT

Interest rates in the US have fallen by over 350bps since the financial crisis...



Sources: FRED, S&P. Latest rates as of 3/8/20

...and have been falling rapidly in recent weeks in the face of a potential economic downturn

3/3/20

Yield on 10-Year Treasury Dips Below 1% for First Time in Sign of Anxiety

3/5/20

Federal Reserve Cuts Rates by Half Percentage Point to Combat Virus Fear  
Central bank lowers federal-funds rate range to 1% to 1.25% in its first between-meeting move since the financial crisis

3/6/20

Corporate Debt Engulfed by Market Turbulence

Is the life insurance industry prepared for a Japanese or European type rate environment?



**Japan**  
#2 global life insurance market



**Germany**  
#8 global life insurance market

- Rates have been below 2% since 1998 and below 1% since 2011
- As-of Mar. 11, 10-year bond yield of **-0.06%**
- Rates have been below 2% since 2011
- As-of Mar. 11, 10-year bond **-0.75%**

# OBJECTIVES FOR READINESS & REGULATORY COMMITTEE

## Short-term

- Facilitate industry-wide dialogue on an evolving situation – actions and impacts
- Coordinate industry-level information gathering (surveys, interviews, etc.)
- Identify priorities and approach for industry-level engagement with stakeholders – regulators, rating agencies, investors, customers, distribution, etc.

## Long-term

- Develop a “playbook” to support industry’s response and strategic planning going forward
- Coordinate ongoing communication with regulators and other stakeholders, as needed

# WHAT WE'VE HEARD: INITIAL INDUSTRY PERSPECTIVES

## SHORT-TERM VIEWS

- Most (74%), but not all, insurers have modeled scenarios at least as severe as current rates
- **Top concerns** are:
  - Profitability of in-force (30%)
  - Profitability of new business (26%)
  - Ability to maintain sales (17%)
- Nearly all insurers have:
  - **Re-priced products/updated rates** outside normal cycles (83%)
  - **Convened internal response teams** (78%)
- Half of respondents are considering **slowing new sales or pulling products**
- Across the industry, **~50% of management time is being spent in response to the current rate environment**
- Nearly all insurers are operating under the assumption that **rates could stay at these levels**

### Pressure on profitability & solvency

- Margin compression
- Investor proposition
- Industry-wide solvency
- Uncertainty on regulatory relief
- Competitive reactions / risk-taking

### Ability to deliver a compelling consumer value proposition

- Uncertain consumer responses
- Diminished insurance differentiators
- Lack of affordable solutions
- Relevance to distribution
- Viability of current business model

### Other

- Preparation of regulators, guaranty associations, and other stakeholders
- Impact to corporate bond markets

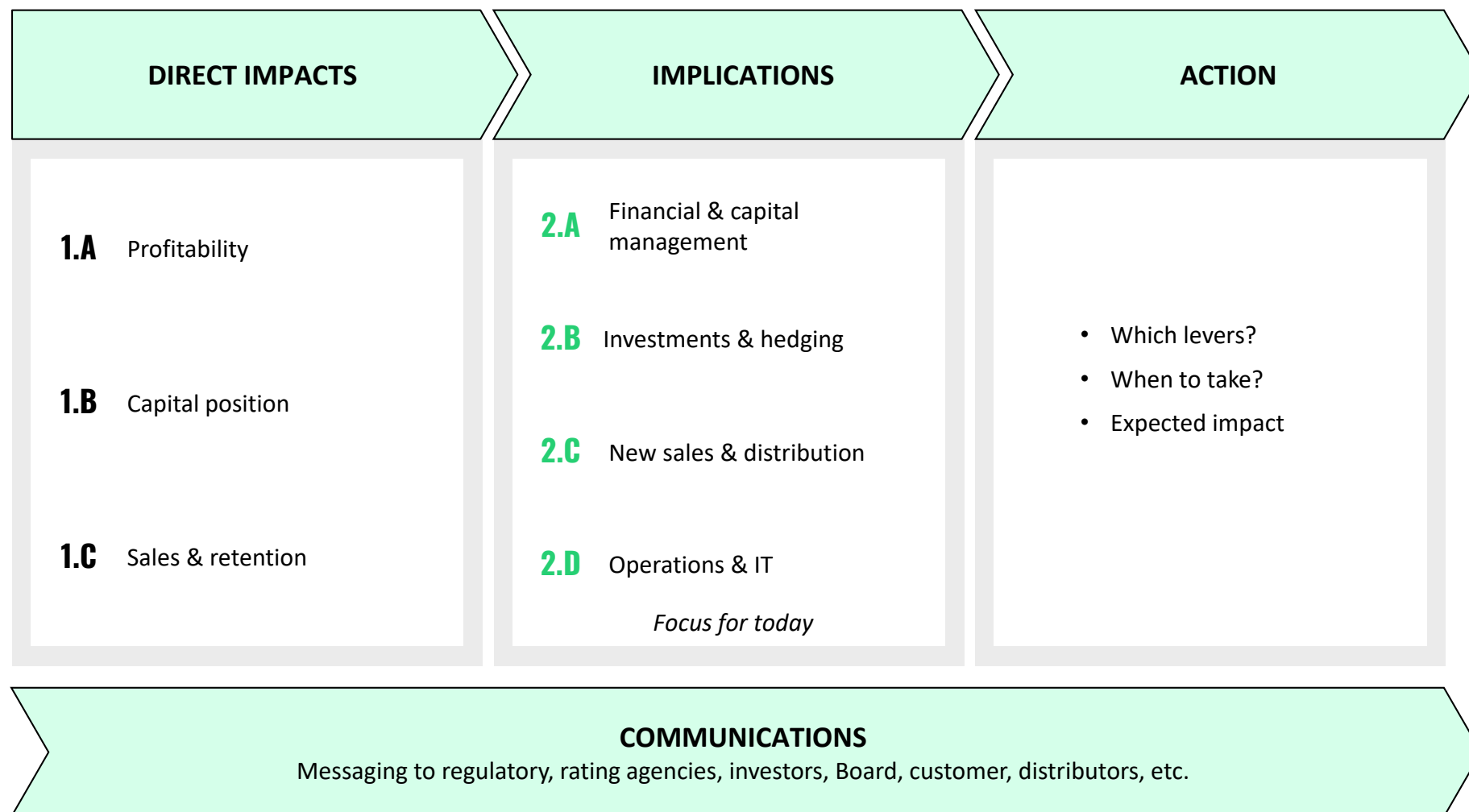
## LONGER-TERM CONCERNS

Sources: LLG Pulse Survey (n=20) (short-term); Interviews with task-force members (n=12) (long-term)

Notes: See appendix for further detail



# WHAT NOW? READINESS PLAYBOOK & NEAR-TERM RESPONSE



# WHAT NOW? RESPONSE TO CURRENT RATE ENVIRONMENT

## Financial & capital management

	Sub-category	Considerations	Potential actions
2.A Financial & capital management	Financials	<ul style="list-style-type: none"> <li>Evaluate impacts to financials:               <ul style="list-style-type: none"> <li>GAAP/Stat/IFRS</li> <li>Multiple scenarios</li> </ul> </li> </ul>	
	Capital (RBC, rating agency, internal capital)	<ul style="list-style-type: none"> <li>Evaluate capital position:               <ul style="list-style-type: none"> <li>Point-in-time position</li> <li>Project year-end (revised sales forecast, multiple scenarios)</li> </ul> </li> <li>Re-evaluate planned capital actions (share buybacks, etc.)</li> <li>Availability of potential capital levers</li> </ul>	<ul style="list-style-type: none"> <li>Seek regulatory relief</li> <li>Changes to dividend policy</li> <li>Portfolio actions/sales</li> <li>Execute contingency actions</li> </ul>
	In-force management	<ul style="list-style-type: none"> <li>Identify at-risk in-force blocks               <ul style="list-style-type: none"> <li>Credit or cap floors</li> <li>Other embedded guarantees</li> </ul> </li> <li>Review credit / cap rate strategy</li> <li>Explore levers (restrict flows, offer exchanges / buy-outs)</li> </ul>	<ul style="list-style-type: none"> <li>Update crediting / cap rates</li> <li>Seek regulatory relief/action</li> </ul>
	Modeling	<ul style="list-style-type: none"> <li>Review rate assumptions and implicit assumptions in models:               <ul style="list-style-type: none"> <li>Scenario generator / negative rates</li> <li>Mean-reversion</li> <li>Equity / rate correlations</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>Update models, as needed</li> </ul>

# WHAT NOW? RESPONSE TO CURRENT RATE ENVIRONMENT

## Investments & hedging

	Sub-category	Considerations	Potential actions
2.B Investments & hedging	Asset management	<ul style="list-style-type: none"> <li>• Monitor availability of assets &amp; performance of credit markets</li> <li>• Monitor ability of external manager to meet asset management mandates</li> <li>• Review SAA and investment guidelines</li> </ul>	<ul style="list-style-type: none"> <li>• Based on monitoring</li> </ul>
	Hedging & ALM	<ul style="list-style-type: none"> <li>• Consider changes to ALM strategy</li> <li>• Monitor performance of hedge strategy in recent market environment</li> <li>• Review hedge targets &amp; objectives</li> </ul>	<ul style="list-style-type: none"> <li>• Execute on changes in strategy, if applicable</li> </ul>

# WHAT NOW? RESPONSE TO CURRENT RATE ENVIRONMENT

## New sales & distribution

	Sub-category	Considerations	Potential actions
2.C New sales & distribution	Profitability of new business	<ul style="list-style-type: none"> <li>Assess new business profitability</li> <li>Changes to pricing guidelines:               <ul style="list-style-type: none"> <li>Economic assumptions</li> <li>Hurdle rates</li> </ul> </li> <li>Identify ability to re-price products and timeframe required for changes               <ul style="list-style-type: none"> <li>Implicit floors in product design</li> <li>Bracket features</li> <li>Tax/regulatory requirements</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>Re-price products</li> <li>Slow / stop sales of products</li> <li>Modify product designs</li> </ul>
	Product development	<ul style="list-style-type: none"> <li>Supportability of products in low rate environment (e.g., reliance on NII vs. mortality margin, fee revenue)</li> </ul>	<ul style="list-style-type: none"> <li>Introduce new products</li> </ul>
	Distribution	<ul style="list-style-type: none"> <li>Revise new sales expectations</li> <li>Evaluated expected impact to agency compensation / commission volumes</li> <li>Assess ability to maintain agent force:               <ul style="list-style-type: none"> <li>Captive: Retention &amp; recruitment</li> <li>Independent: Relevance</li> </ul> </li> <li>Consider viability for traditional compensation models if material shifts in sales volumes/products</li> </ul>	<ul style="list-style-type: none"> <li>Provide near-term support for agent force</li> <li>Adjust channel focus</li> </ul>

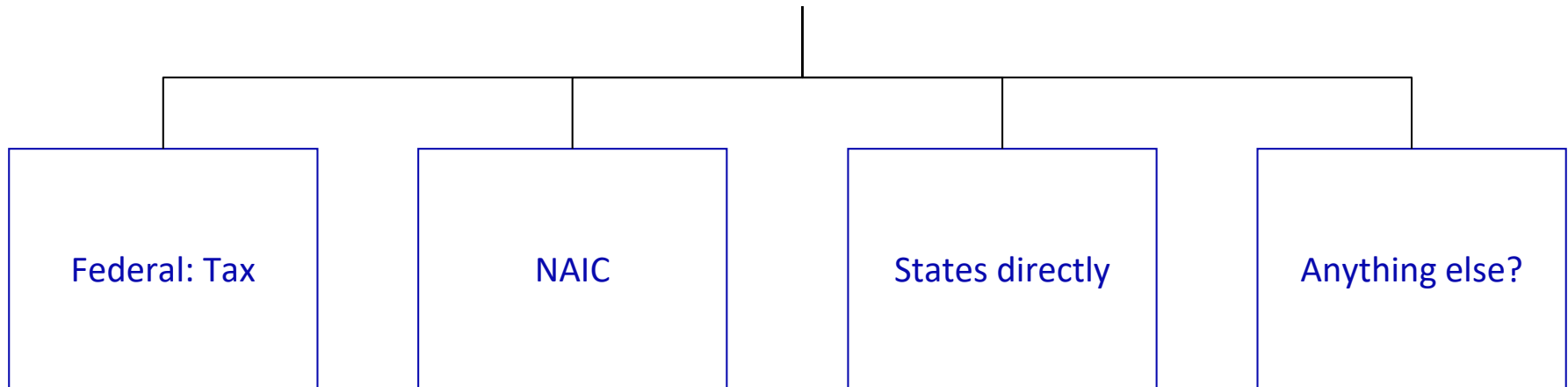
# WHAT NOW? RESPONSE TO CURRENT RATE ENVIRONMENT

## Operations & IT

	Sub-category	Considerations	Potential actions
<b>2.D</b> <b>Operations / IT</b>  <i>Note: intended to capture low rate impacts, not full implications or coronavirus</i>	<b>Systems</b>	<ul style="list-style-type: none"> <li>• Systems ability to take negative rates               <ul style="list-style-type: none"> <li>– Valuation engines</li> <li>– Hedging platforms</li> <li>– Admin systems</li> <li>– Etc.</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• Identify &amp; update systems</li> <li>• Determine availability of work-arounds if long lead time</li> </ul>
	<b>Expense mgmt.</b>	<ul style="list-style-type: none"> <li>• Supportable expense base in a prolonged low-rate environment (with lower sales and reduced NII)</li> </ul>	<ul style="list-style-type: none"> <li>• Identify &amp; pull operational levers to reduce expense base (scale headcount, automate, etc.)</li> </ul>

# WHAT NOW? REGULATORY ADVOCACY PRIORITIES

## POTENTIAL LOW INTEREST RATE REGULATORY RESPONSES



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**Our next working group discussion will focus on regulatory priorities identified today**

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# OPEN QUESTIONS & NEXT STEPS

## Open questions

- Objectives for this group: what does the deliverable look like?
- Industry-wide readiness survey – topics for focus?
- Consideration of COVID-19 situation
- Any other business?

## Next steps

- Welcome any off-line feedback/reactions from today's conversation
- Weekly working group meetings (Thursday at 3pm ET)

# **APPENDIX**

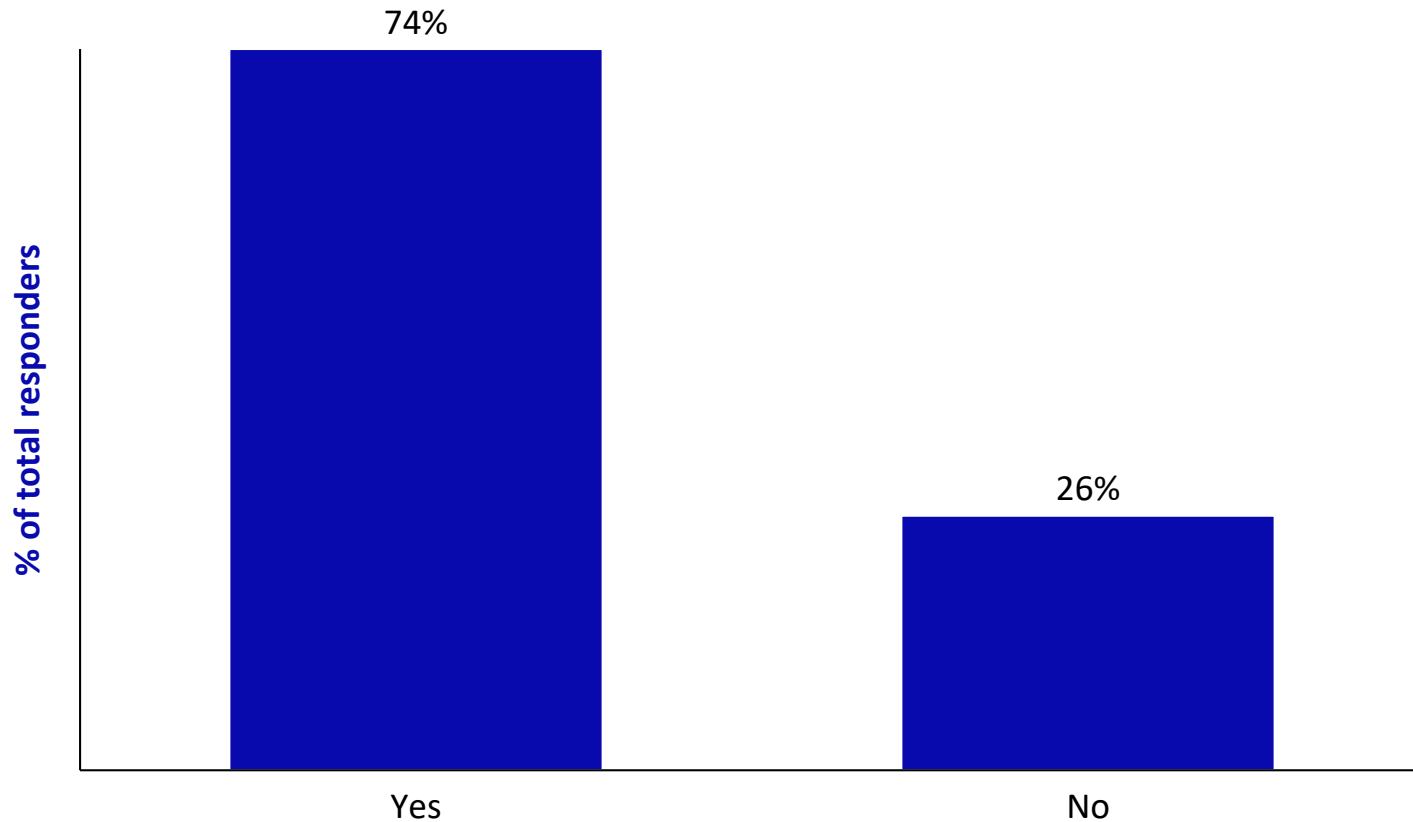
**RESULTS FROM LLG PULSE SURVEY (AS-OF MAR. 11)**



# READINESS FLASH SURVEY RESULTS

Based on 23 responses received as of 3/11/20

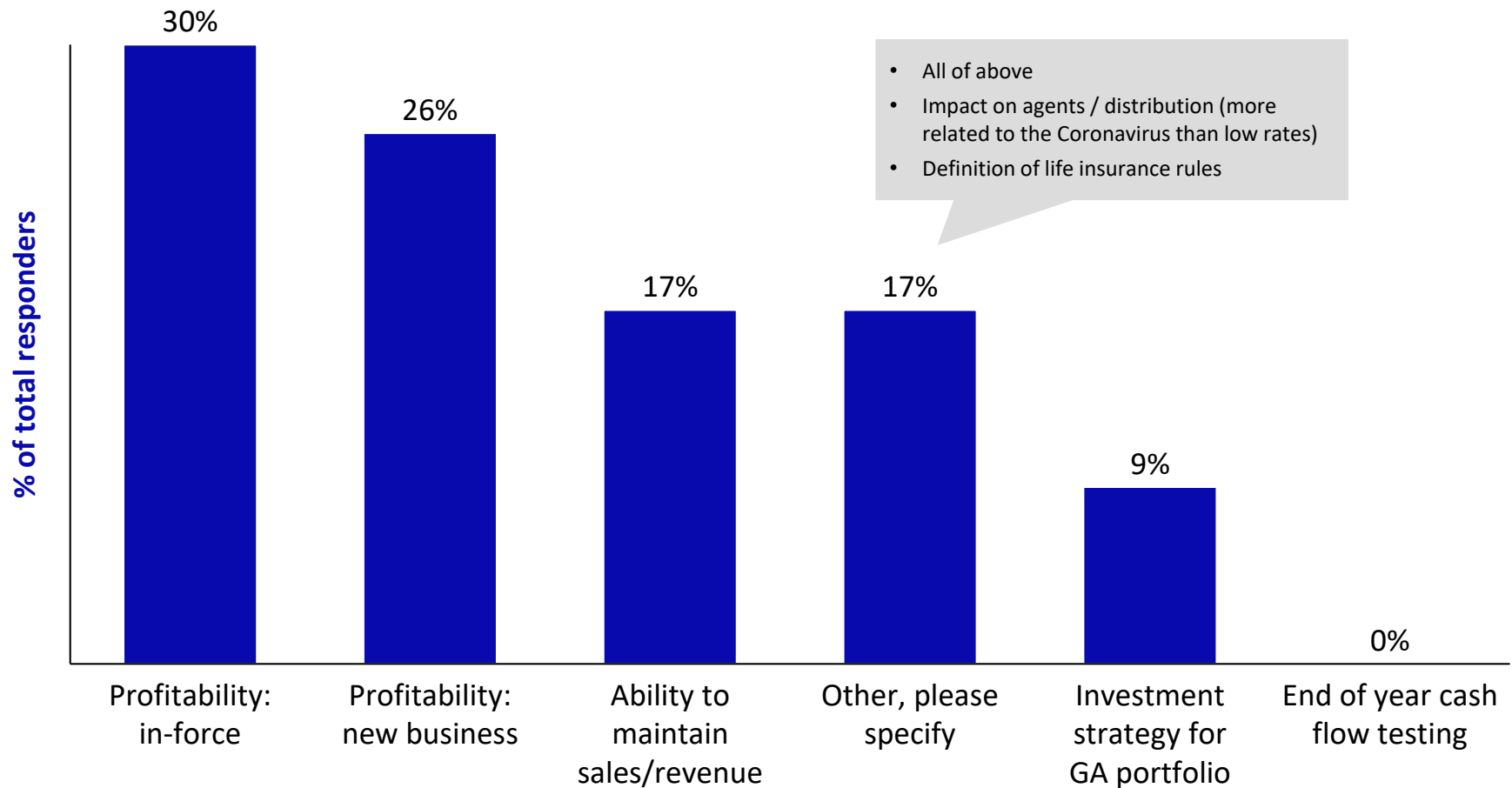
**Q1 - For internal purposes, have you explicitly modeled rate scenarios in which the 10-year Treasury falls to current levels? (~0.6% as-of March 9th)**



# READINESS FLASH SURVEY RESULTS

Based on 23 responses received as of 3/11/20

Q2 - What is your biggest concern right now in regards to the current rate environment? (single choice)



# READINESS FLASH SURVEY RESULTS

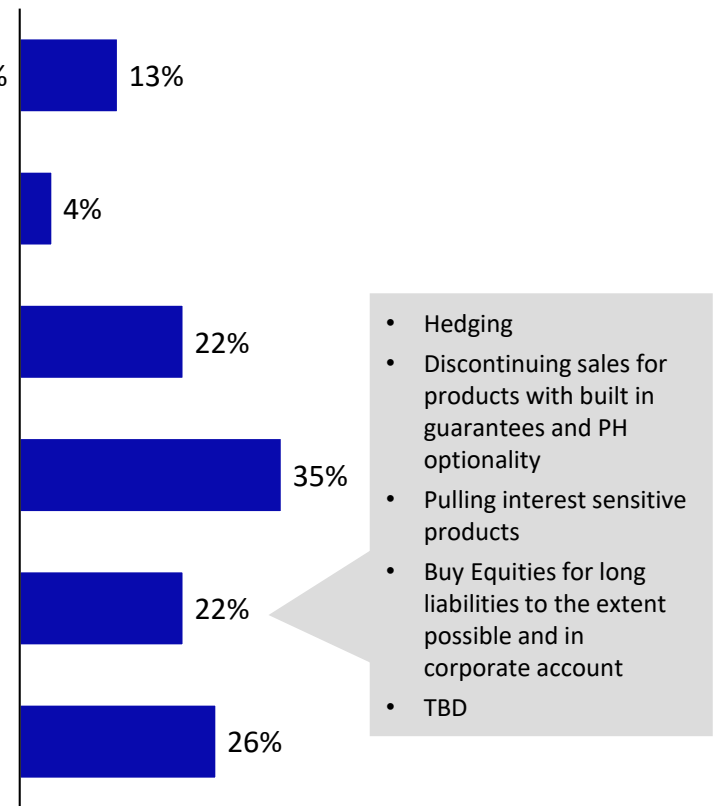
Based on 23 responses received as of 3/11/20

Q3 - What actions, if any, **have been taken to date** to mitigate the effects of the current rate environment? (Check all that apply)



% of responders who chose selected answer

Q4 - What other actions, if any, **are being considered** to mitigate the effects of the current rate environment? (Check all that apply)

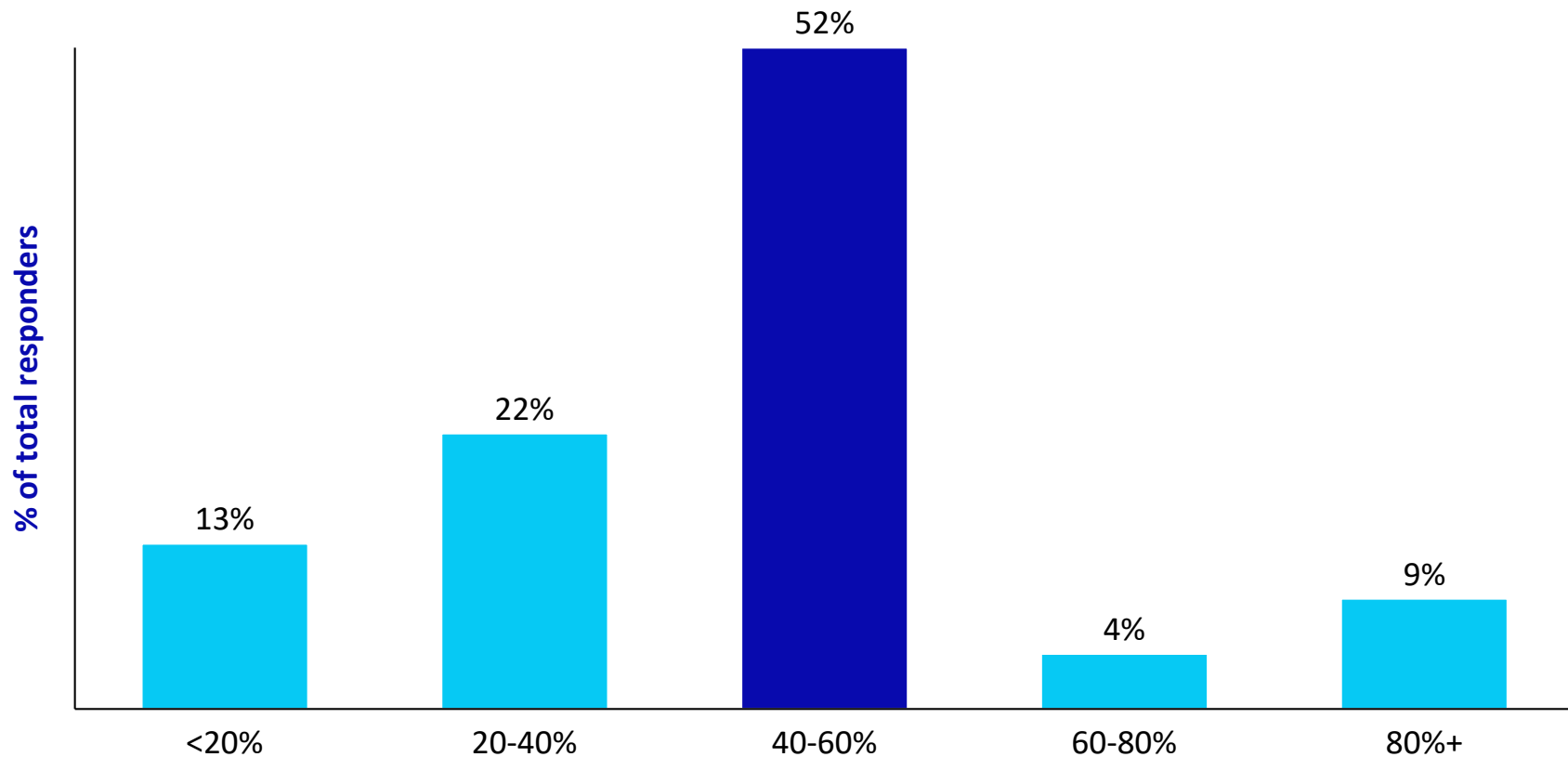


% of responders who chose selected answer

# READINESS FLASH SURVEY RESULTS

Based on 23 responses received as of 3/11/20

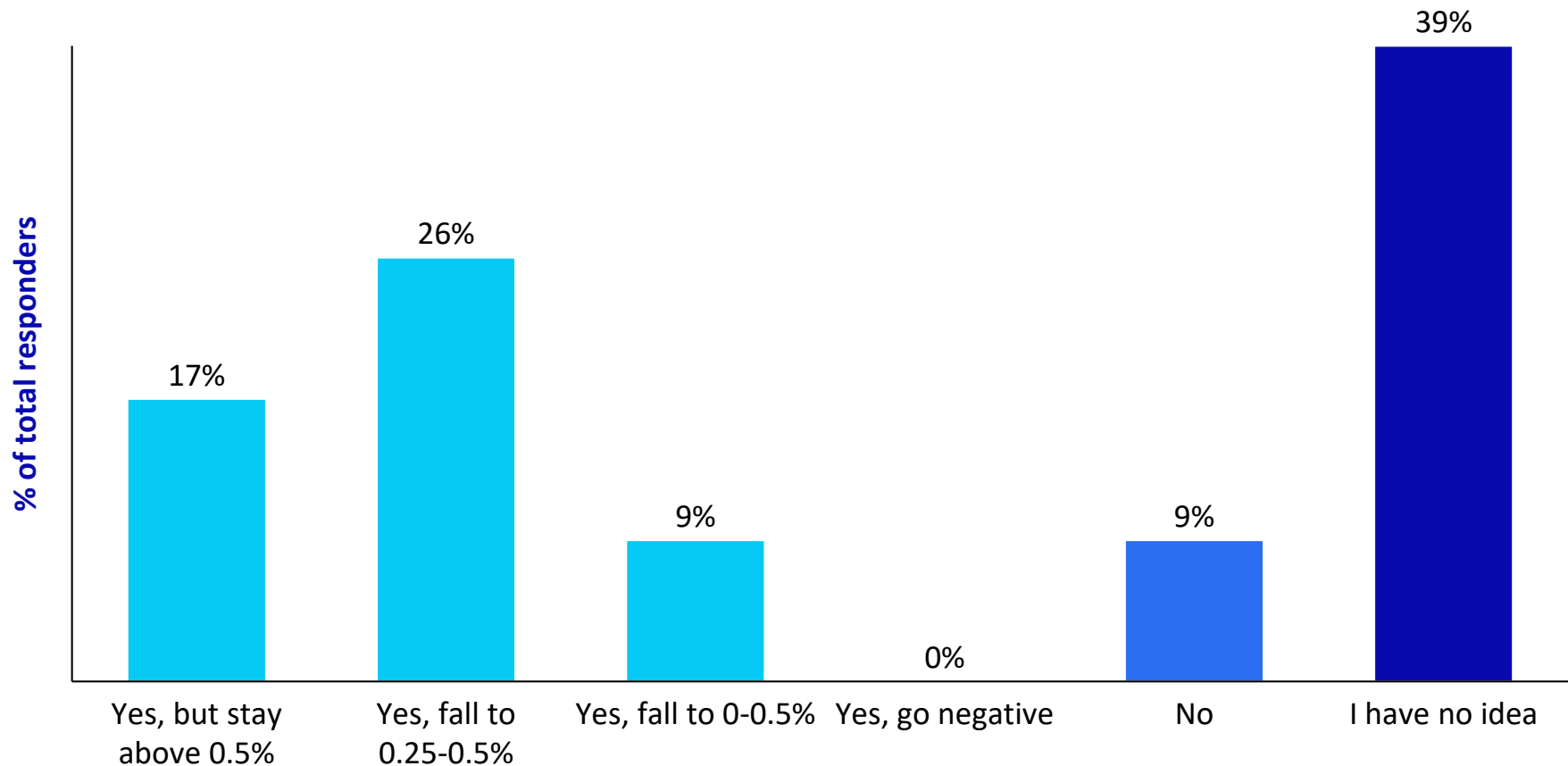
**Q5 - What share of senior management time is being spent evaluating and responding to the current rate environment? (single choice)**



# READINESS FLASH SURVEY RESULTS

Based on 23 responses received as of 3/11/20

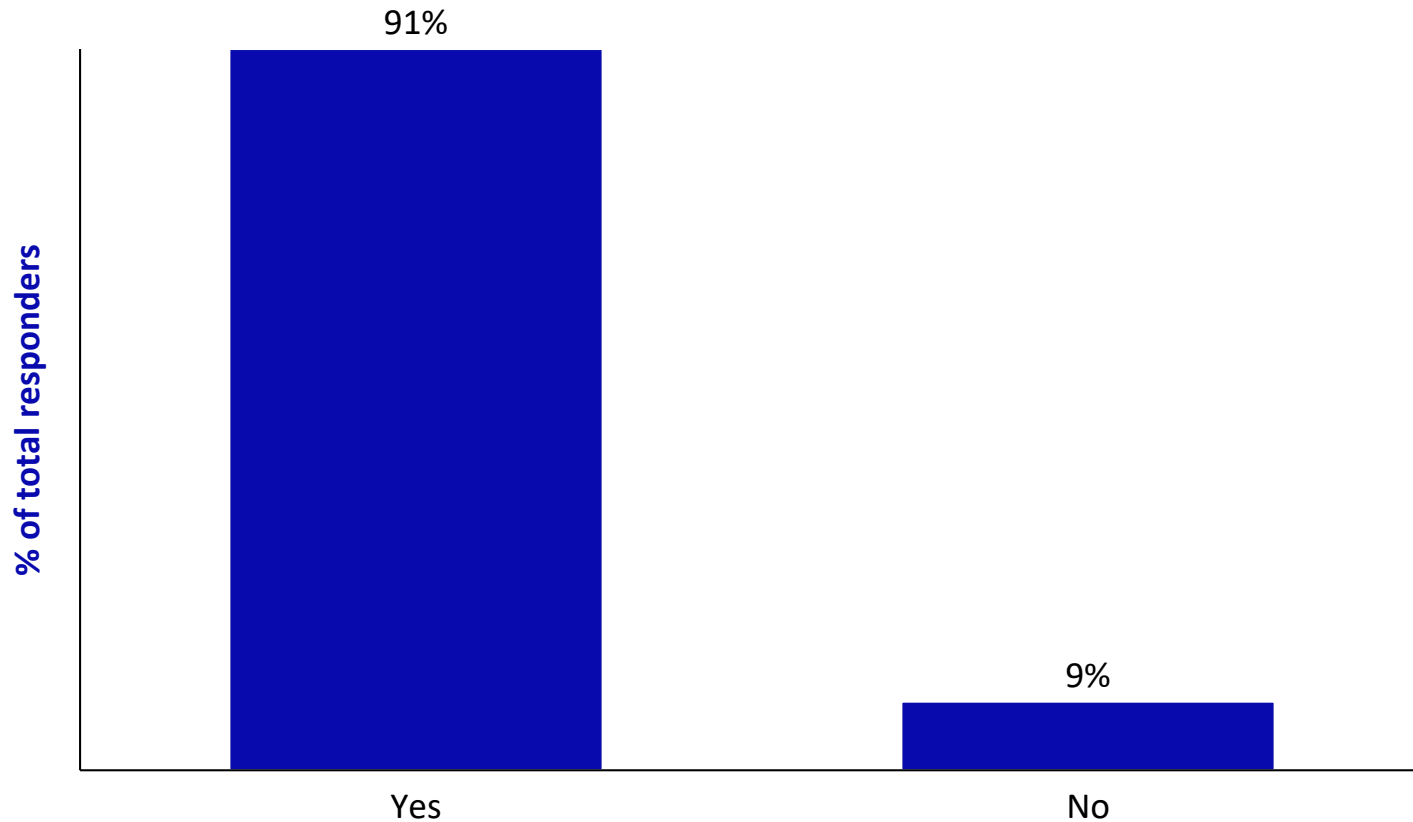
Q6 - Do you expect the 10-year rate to continue to decline? (single choice)



# READINESS FLASH SURVEY RESULTS

Based on 23 responses received as of 3/11/20

**Q7 - Are you operating under an expectation that rates could remain at these levels for the remainder of 2020? (with implications for cash flow testing and financial reporting) (single choice)**



# **APPENDIX**

## **INDUSTRY CONCERNS ON LOW RATES**

# WHAT ARE YOUR **TOP CONCERNS** REGARDING A LOW RATE ENVIRONMENT?

Based on interviews with task-force members

Theme	Summary of interview takeaways
<b>Pressure on profitability &amp; solvency</b>	<ul style="list-style-type: none"> <li>• <b>Margin compression and unattractive investor proposition:</b> Burden of existing guarantees (back-books) and external constraints on new business pricing (e.g., minimum credit rates in tax code) will further pressure profitability or make product non-tenable; lack of future profitable opportunities to deploy capital</li> <li>• <b>Solvency:</b> concerns over industry-wide solvency that could have knock-on effects to own business model via (i) state guarantee funds or (ii) ability of insurance industry to meet its promises to customers</li> <li>• <b>Uncertainty on regulatory relief,</b> especially from cash flow testing requirements (heard by both NY and non-NY based firms), in most adverse scenarios</li> <li>• <b>Competitive reactions:</b> potential for risk-taking behavior from others will price-out less aggressive players</li> </ul>
<b>Ability to deliver a compelling consumer value proposition</b>	<ul style="list-style-type: none"> <li>• <b>Diminished insurance differentiators:</b> lower value of tax advantages, more limited ability to offer guarantees</li> <li>• <b>Lack of affordable solutions:</b> low rates drive higher pricing on long-term contracts (or reduce income available), reduce affordability for customers; concerns on industry's ability to continue to meet needs</li> <li>• <b>Uncertain consumer responses:</b> no consistent view on dramatic consumer behavior will shift and impact to new sales volumes (range in expectation from new business goes to zero to limited impact expected)</li> <li>• <b>Relevance to distribution:</b> ability to provide sufficient opportunity (income) to captive agent force and maintaining relevance to independent distribution</li> <li>• <b>Viability of current business model:</b> expectations from some firms that, in most adverse scenarios, industry would largely be forced to shift to in-force management / runoff model</li> </ul>
<b>Impact on other stakeholders &amp; markets</b>	<ul style="list-style-type: none"> <li>• <b>Preparation of regulators, guaranty associations, and other stakeholders:</b> Broad belief that other industry participants would not be sufficiently prepared for a low rate scenario</li> <li>• <b>Impact to corporate bond markets</b> – how will corporate bond market react if rates go near/to zero?</li> </ul>



# WHAT ACTIONS HAS THE INDUSTRY TAKEN TO-DATE?

Based on interviews with task-force members

Theme	Summary of interview takeaways
<b>Several companies have repositioned in reaction to the current rate environment</b>	<ul style="list-style-type: none"> <li>• Changes to hedge strategies and investment portfolio</li> <li>• Changes to product portfolio, such as exiting some product constructs, transition to lower capital / less interest rate sensitive products</li> <li>• Expense management to compensate for margin pressures</li> </ul>
<b>Most companies have undertaken financial analysis of low rates</b>	<ul style="list-style-type: none"> <li>• Wide range in views on what is a low rate environment               <ul style="list-style-type: none"> <li>– Varying views on “how low” (current vs. lower vs. negative) and “how long”</li> <li>– Few companies have undertaken significant efforts to explore implications of negative rates</li> </ul> </li> <li>• Profitability and cash flow testing key concerns cited from these efforts; all companies stated that they are comfortable with their own solvency position (although several raised concerns at the industry level)</li> <li>• Some, but not all, have developed “playbooks” to identify actions if rates reach a certain level</li> </ul>
<b>Only a handful have done a non-financial reviews to prepare for a low rate environment</b>	<ul style="list-style-type: none"> <li>• While many companies cited concerns on the customer value proposition, few have actively prepared for scenarios with limited or no new business</li> <li>• Analysis / review of potential impact to product attractiveness or distribution sales mix</li> <li>• Previous or ongoing research into experience in non-US markets</li> </ul>
<b>Moderate confidence in self-readiness, but unsure about industry readiness</b>	<ul style="list-style-type: none"> <li>• Majority of companies noted they are better positioned than most peers; however, nearly all Task Force members stated understanding what else their organizations should consider is a top goal for their participation</li> <li>• Broad view that the industry as a whole – including both insurers and other stakeholders – is not sufficiently prepared</li> </ul>

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