Swiss Re sigma study predicts robust growth for third party asset management as insurers seek to bolster investment performance

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Swiss Re's new sigma study predicts robust growth for the outsourcing by insurance companies of their asset management operations. The study estimates that the combined markets for third party asset management (TPAM) in the US and Europe will grow by an average of 10% per year over the next decade.

At the end of 2001, global insurance assets totalled approximately USD 11.5 trillion, of which 82% were held by life insurers. Managing these assets in the current climate of declining equity markets, low interest rates and record levels of corporate bond defaults is a significant challenge for the industry.

In response, insurance companies are increasingly turning to outside experts who offer specialist skills in insurance asset management to help them improve their returns and manage the risks associated with the investments they hold. Besides the turmoil in the financial markets, several factors are stimulating insurers' demand for third party asset management, including:

- Pressures on chief investment officers to deliver solid returns, maintain adequate diversification and manage operational risk
- Increased scrutiny from rating agencies
- The need for asset managers to follow an growing number of sectors
- The demand for specialist expertise in matching insurers' assets against their liabilities (so-called "asset-liability management")
- Keeping abreast of changing accounting rules and regulations

Currently, American insurers employ third party managers to oversee USD 300 billion of investments. Insurers in Europe outsource about USD 140 billion of assets to the TPAM market, which is less established than in the US but, according to *sigma*, likely to grow faster.

US and European insurance investments outsourced, year-end 2001

	Total Insurance Investments, USD billion	Estimated third party Investments, USD billion
US	3947	approx. 300
Total Europe	4502	approx. 140
Germany	839	25-50
UK	1430	20-40
France	784	20-40

Note: Total insurance investment figures for Europe are preliminary.
Source: Comité Européen des Assurances (CEA), European Insurance in Figures 2002, pp. 57, 138; A.M. Best; and Swiss Re estimates.

The TPAM market is very competitive and highly fragmented

The market is very competitive and, in the US, highly fragmented with 10 providers each managing at least USD 10 billion of insurance as-sets and another 11 each managing at least USD 5 billion. Competition between banks, insurers, and independent asset management firms keeps TPAM fees relatively low. For fixed income mandates of USD 100 million or more, managers typically charge 15-20 basis points (1 bp = 0.01%); for active equity mandates of this size, fees are typically 30-35 bp.

In Europe, TPAM has a lower penetration than in the US. This is principally because European insurance asset managers must maintain a local presence, in some cases for legal reasons. This creates a cost barrier to entry, reducing competition between providers and strengthening the major European institutions who already have a foothold in the market.

Top five providers globally

The top five third party asset managers globally, at the end of 2001, were Deutsche Asset Management (including Zurich Scudder In-vestments) with USD 34.3 billion under management, BlackRock (USD 30.6 billion), Conning Asset Management (owned by Swiss Re) with USD 27.6 billion, AXA's Alliance Capital (USD 19.9 billion) and Wellington (USD 19.6 billion).

More choices for insurance assets: hedge funds and private equity

In seeking to bolster investment returns and diversify their portfolios, insurers are not confined to the stock and bond markets. In recent years, large insurers have increased their asset allocations to alternative investments such as hedge funds and private equity. Hedge funds have the potential to earn solid returns, in some cases at low risk. Insurers' world-wide holdings of hedge funds are, according to sigma, estimated to be USD 10-15 billion. Private equity, which involves investing in companies whose shares are not publicly traded, embraces the full range of enterprises from start-ups to mature companies subject to buy-out. Despite current setbacks, private equity has historically earned higher returns than the stock market, though at greater risk. *sigma* estimates that European and American insurers hold USD 25- 35 billion in private equity investments. In total, insurers' alternative investment holdings are poised to grow by more than 10% annually in the coming years.

Challenging environment offers asset managers the chance to stand out.

The current investment environment requires insurers to place new emphasis on their asset management operations. Investment risk management - an area at which some insurance third party managers excel - will become more of a priority for top management. In this environment, superior asset managers will have the opportunity, and the need, to distinguish themselves and prove their worth to clients.

Notes for editors:

Swiss Re is one of the world's leading reinsurers with over 70 offices in more than 30 countries. For 2001, Swiss Re reported a net loss of CHF 165 million, largely due to the 11 September event. Gross premiums in 2001 were CHF 28.5 billion. At the end of June 2002, Swiss Re's shareholders' equity amounted to CHF 18.3 billion and the total balance sheet stood at CHF 168 billion. Swiss Re is rated "AA+" by Standard & Poor's, "Aa1" by Moody's and "A++" by A.M. Best.

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