INVESTMENT

Insurance asset management in the Middle East

A look at how insurers in the UAE and Saudi Arabia are investing and some of the things that might affect their asset allocation in the near future from BADRI's Mr Hasham Esmail Piperdy.

Insurers are often important institutional investors, particularly those that have long investment horizons and are less concerned with quarterly volatility.

As the GCC insurance market further develops, there is significant potential for insurers to play an important role as strategic investors. However, there perhaps needs to be a change in focus to a longer term horizon for investment strategy.

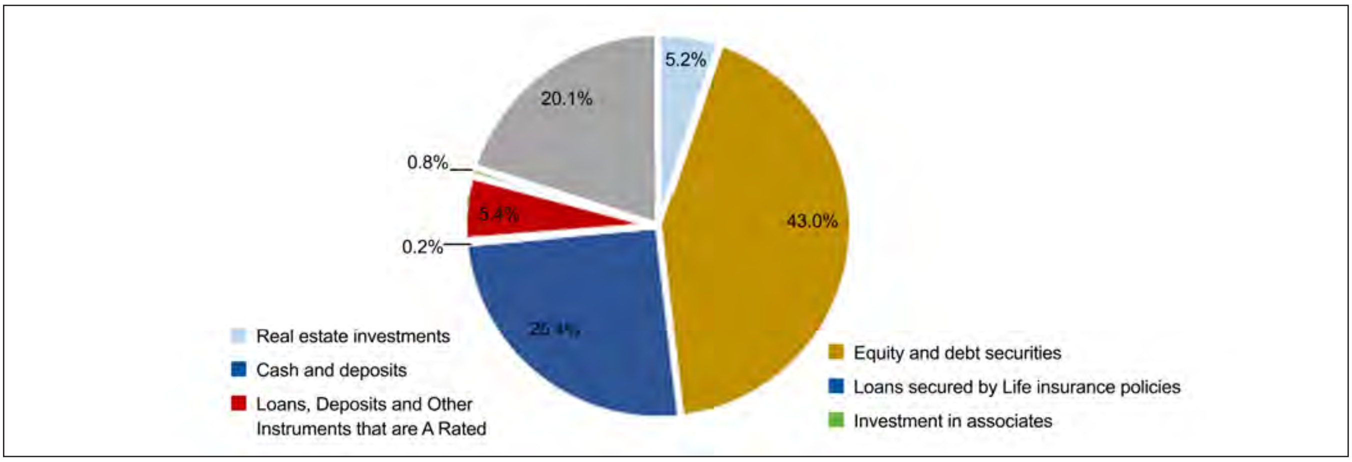
Asset allocation

There is a wide range of diversified strategies amongst UAE insurers whereas KSA insurers still hold significant amounts in cash. Liquidity risk and general loss aversion over short term horizons often weighs heavily on strategy. With turbulent global markets, this means investment returns have still been largely positive. With underwriting profits under pressure last year, were it not for positive investment returns, financial results would have been significantly worse.

UAE asset allocation

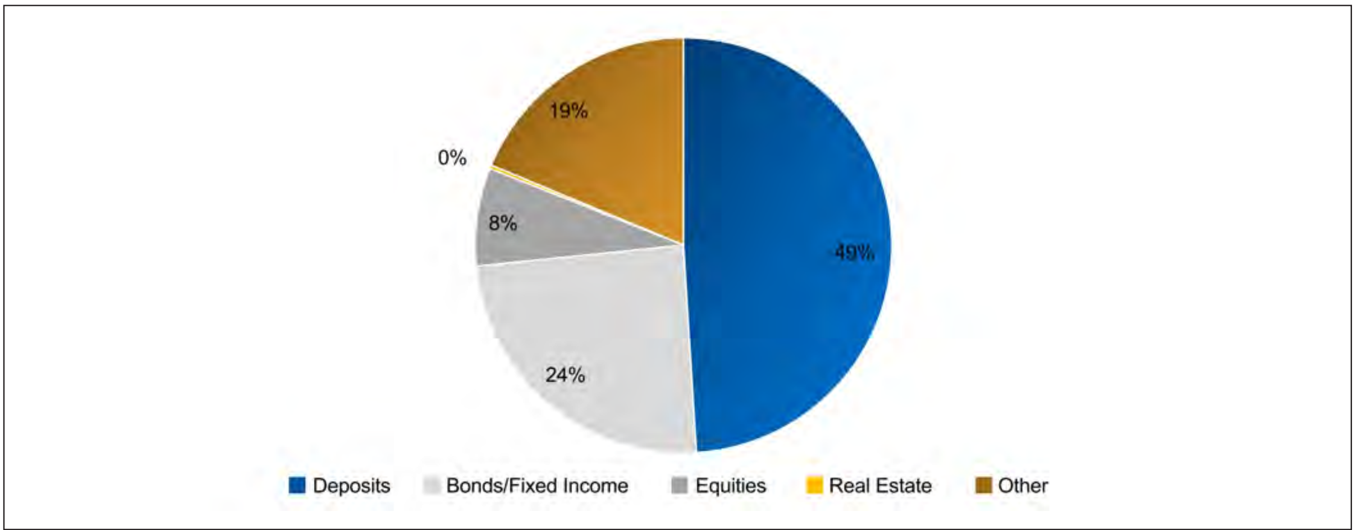
In aggregate, UAE insurers have 25% in cash with the remainder invested in a wide mix of assets. As of December 2021, there was a total of AED79bn ($21.51bn) in invested assets.

Figure 1: Invested assets by class in the UAE in 2021



Source: CBUAE

Figure 2: Invested assets by class in Saudi Arabia



Source: SAMA 2021 Market Report

KSA insurer asset allocation

In KSA as of December 2021 there were investments of SAR35.3bn ($9.4bn) on insurers' balance sheets.

Cash and deposits comprise around 50% of investments which is on the high side. Government sukuk and murabaha investments make a sizable proportion of the invested assets. This seems to be the case regardless of size of the insurer.

There is potential for diversification into alternate asset classes which may be expected to provide a higher longer-term return relative to cash, although this does come with short-term volatility as recent global equity and bond markets have shown.

Recent performance

There is a wide range of returns from -4% to +11% observed in the UAE market for this period reflecting the variation in strategies deployed.

KSA investment returns

Investment returns up to 3Q2022 ranged up to 5%, with less variation between the highest and lowest returns compared to UAE, reflecting the high cash allocation.

Drivers of investment strategy

In line with other markets, GCC insurers are subject to many regulatory constraints and controls around investment strategy. This is naturally appropriate as the objectives are primarily to ensure capital adequacy and security of policyholder benefits.

Some of the regulatory drivers include:

- Minimum levels for certain asset classes (e.g., government bonds/ sukuk)
- Maximum thresholds on certain asset classes (e.g., private equity, real estate, overseas assets)
- Restrictions on the admissibility of certain assets for regulatory solvency
- Capital charges for different asset classes in a risk-based capital regime
- IFRS17/IFRS9 new reporting standards.

ALM

Investment strategies for insurers should reflect their risk appetite but in broad terms, asset movements should at least consider returns that reasonably match the liability side of the balance sheet. In many developed insurance markets, this is an area where actuaries have supported by designing different SAAs based on the insurer's own liability profile. There is significant potential for ALM or liability-driven strategies to be developed.

SAMA's requirements for an ALM to be conducted at least annually have been a valuable source of analysis for investment committees showing how their selected strategy is aligned and how it has performed relative to their liabilities. For example, we have observed SAIBOR-linked investments undertaken to hedge against adverse shifts in the yield curve.

Absolute return targets, however, are still not uncommon mandates for investment managers.

IFRS17 and IFRS9

These two accounting standards have just come into force and will be another consideration when reviewing strategy this year. Thanks to the SAMA dry run exercises, many insurers are already aware of the potential impact on their investments.

However, another consideration is the impact of discounting technical reserves which many insurers in this region will be doing for the first time. Now there is a new potential objective to add to the investment policy i.e., hedging changes in yield curves will have more importance. The recent spike in yields by over 300bps to 400bps in only a few months has shown the importance of managing this risk.

ESG

Shariah-compliant investments are extremely important. Ideally, as an extension to this, ESG should also be much higher on the agenda than it is at present. But given the regulatory changes and challenging market conditions, insurers can be forgiven for having their hands full elsewhere.

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