A life insurer's ALM - a practical approach

Bruno Pfister, CFO

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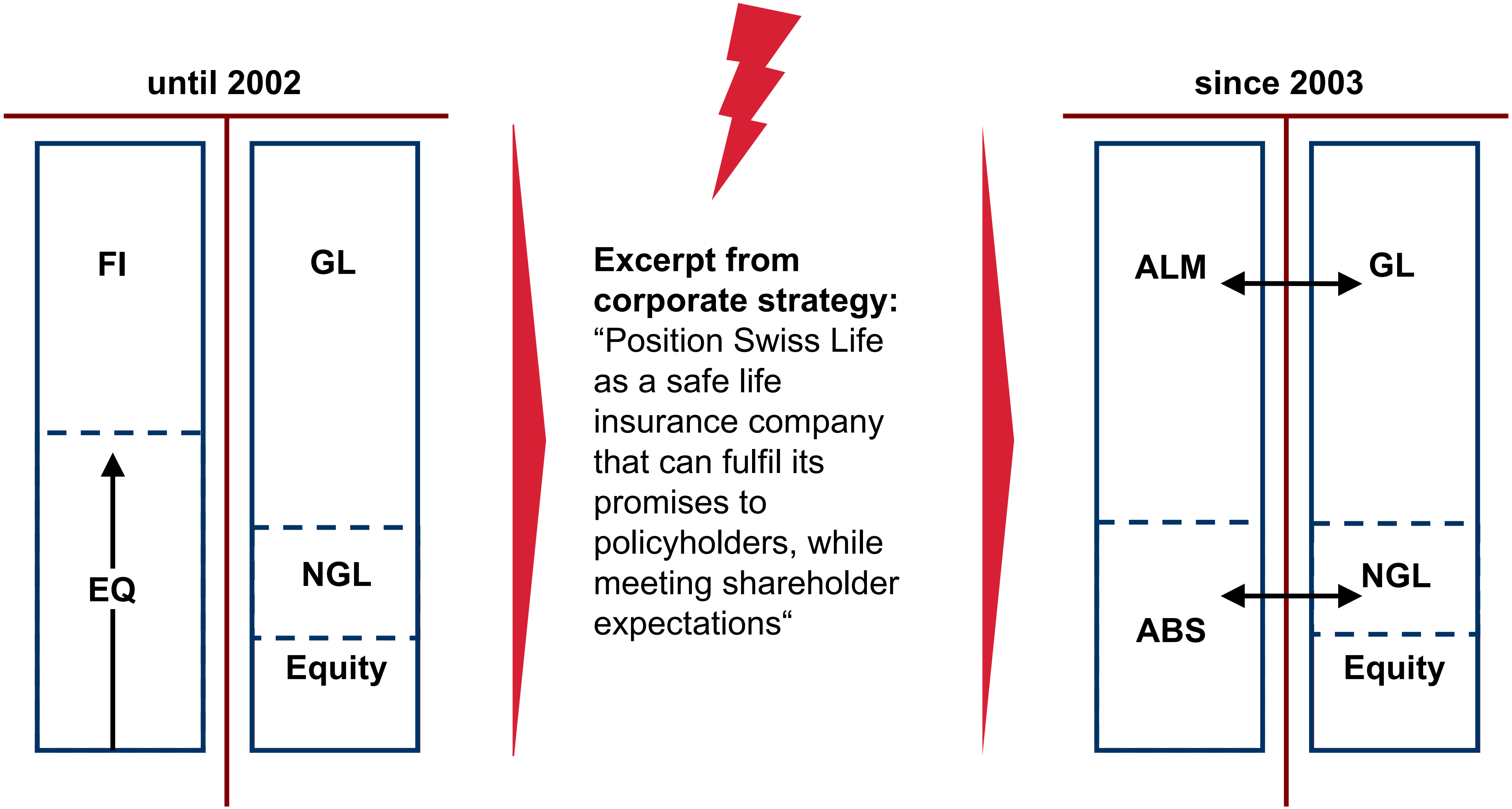
Agenda

1. Introduction
2. Elements of asset & liability management
3. Putting the pieces together
4. Further development

Change in business model leads to different balance sheet structure

Conceptual



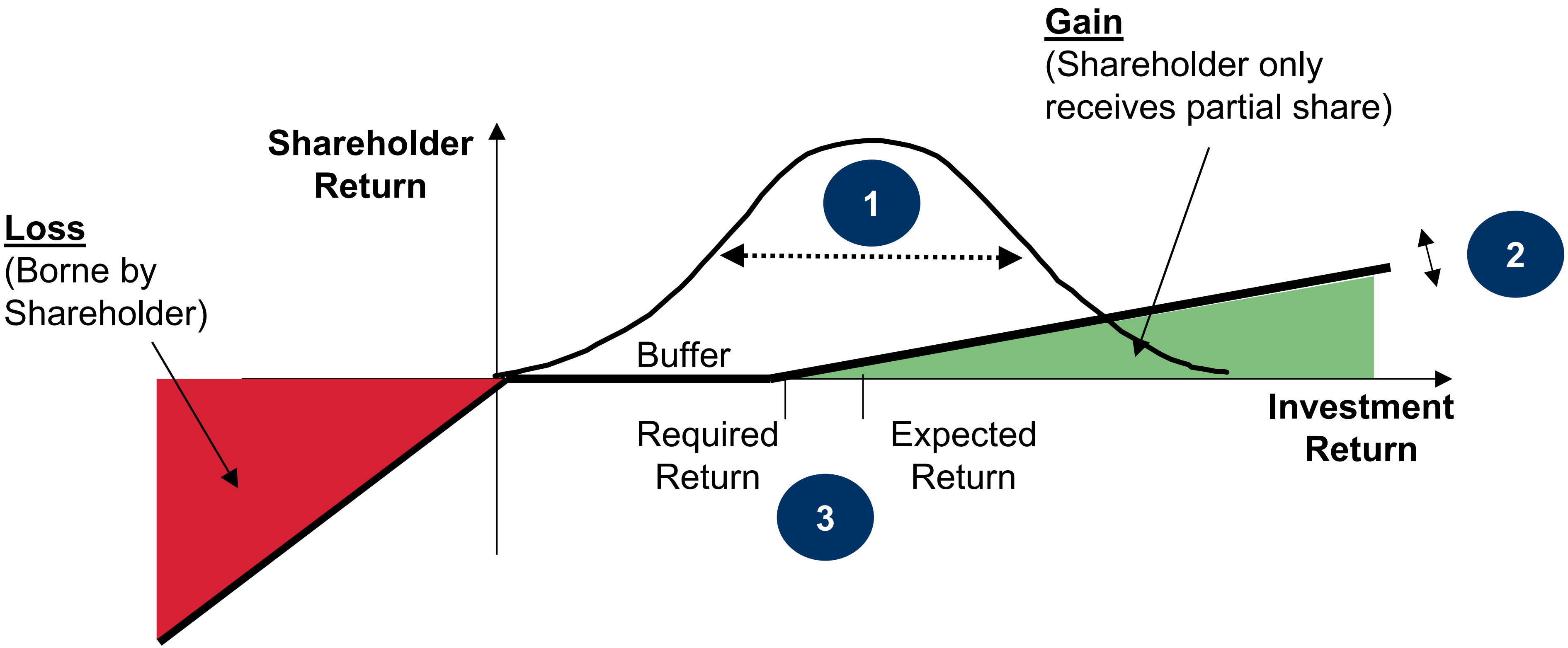
Excerpt from corporate strategy:
“Position Swiss Life as a safe life insurance company that can fulfil its promises to policyholders, while meeting shareholder expectations“

Note: FI: fixed income; EQ: equity; ALM: ALM portfolio; ABS: absolute return portfolio; GL: guaranteed liabilities; NGL: non-guaranteed liabilities

Agenda

1. Introduction
2. Elements of asset & liability management
   - 2.1 Overview
   - 2.2 Credit policy & liability modelling
   - 2.3 Risk budget
   - 2.4 Balance sheet constraints
   - 2.5 Strategic asset allocation
3. Putting the pieces together
4. Further development

Asymmetry of Returns and ALM Targets

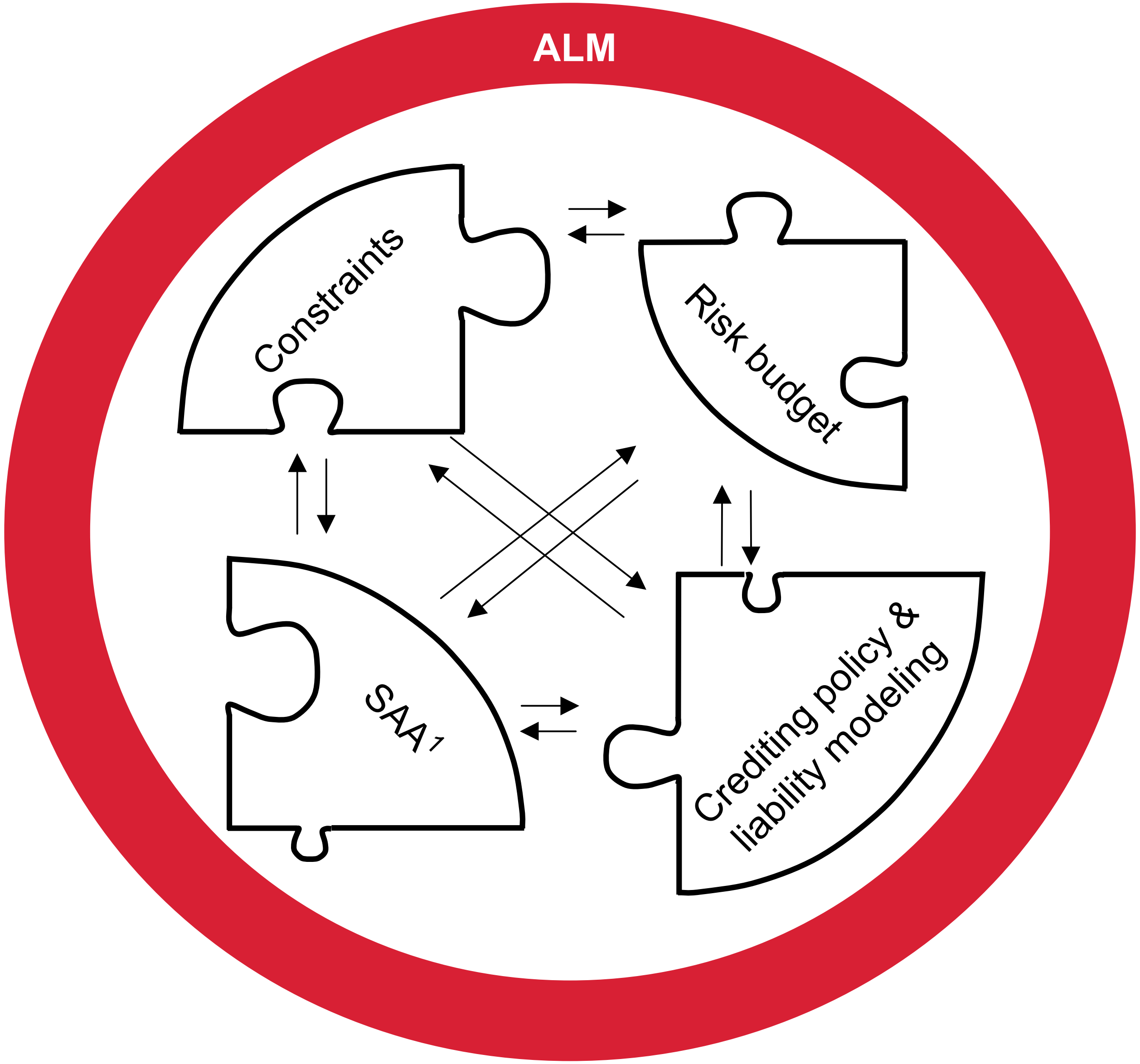


Target 1
Asset allocation
(Risk/Return)

Target 2
Crediting policy

Target 3
Product Principles

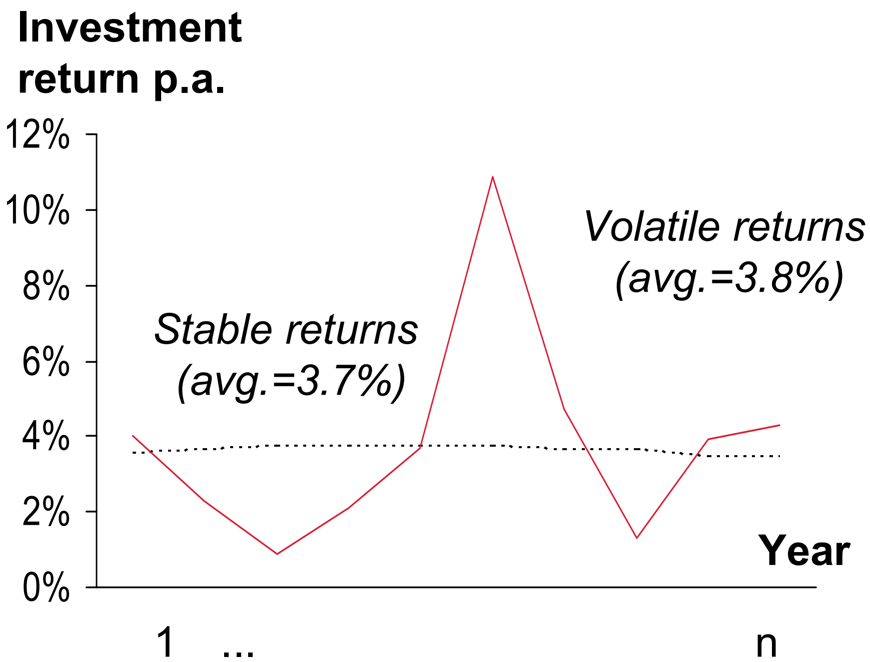
Different ALM elements are interrelated



¹ Strategic Asset Allocation

High investment return volatility reduces value compared to stable (yet lower) returns

Illustrative, in CHF million



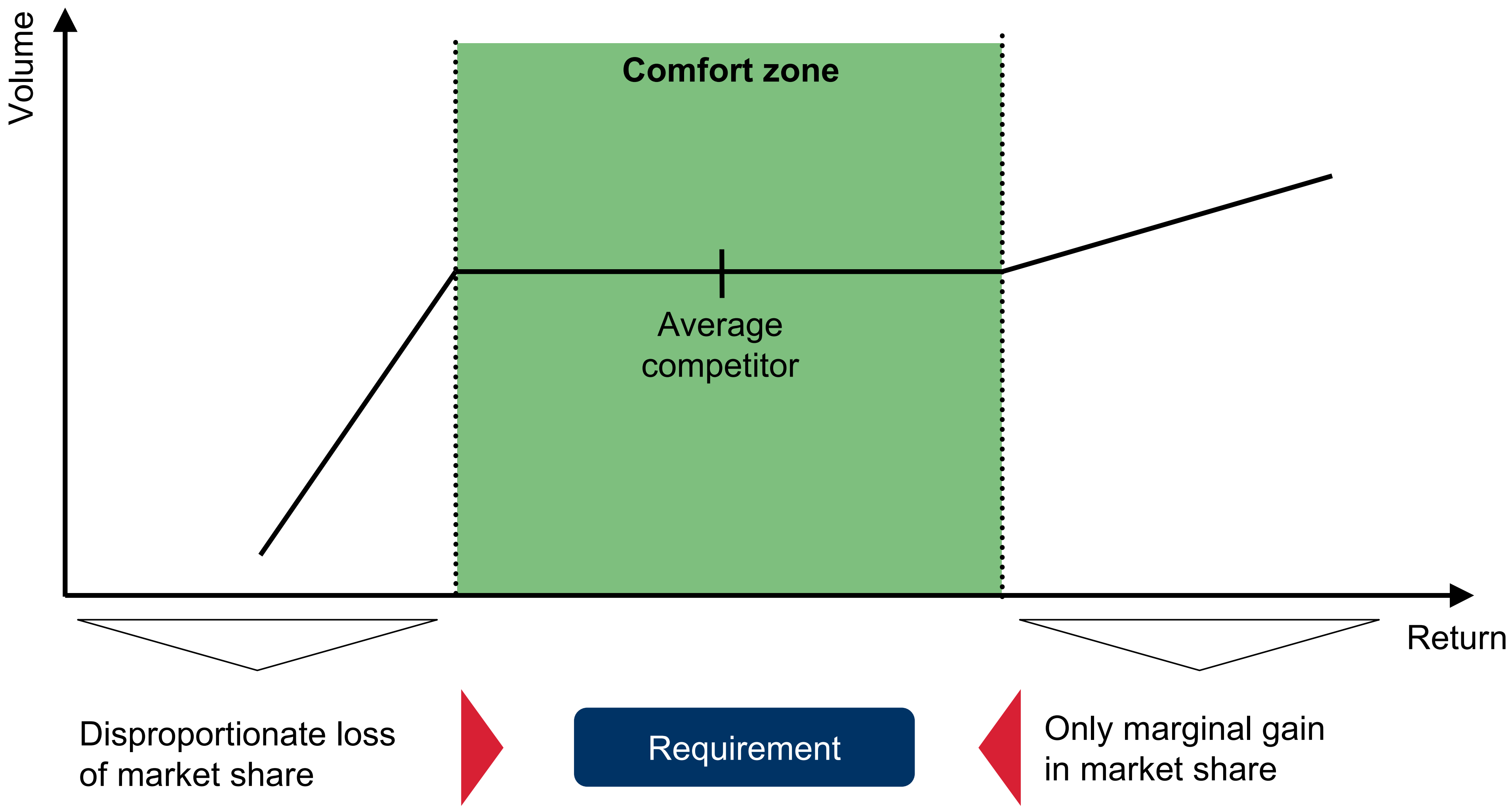
Sensitivity analysis

	New business p.a.	Average lapse rate (%)	NPV
Stable returns	500	2%	2'000
Volatile returns	400	4%	1'000

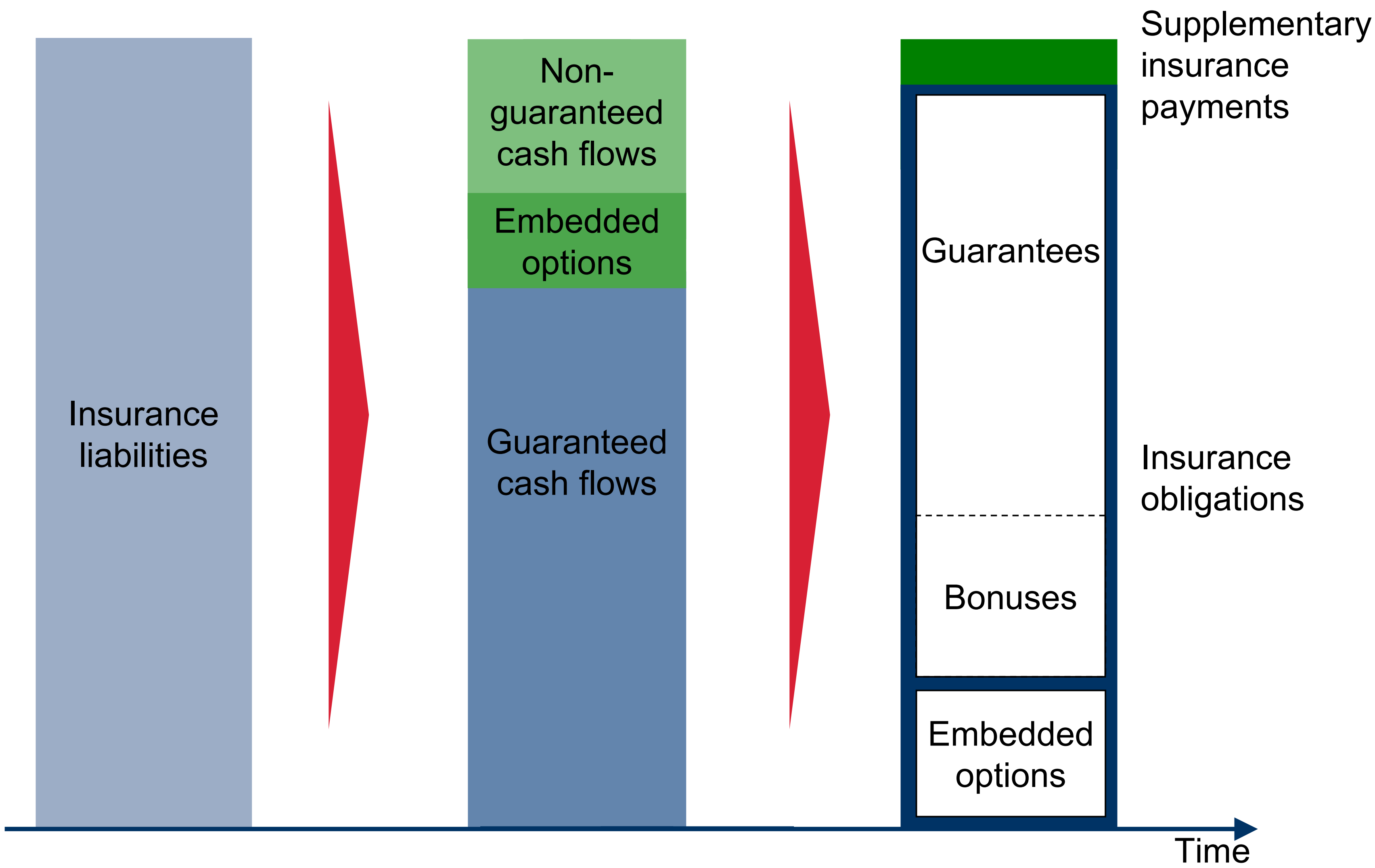
Volatile investment returns therefore cause lower average new business, higher lapse rate and lower valuation

Note: All values based on business cycle macro-economic environment

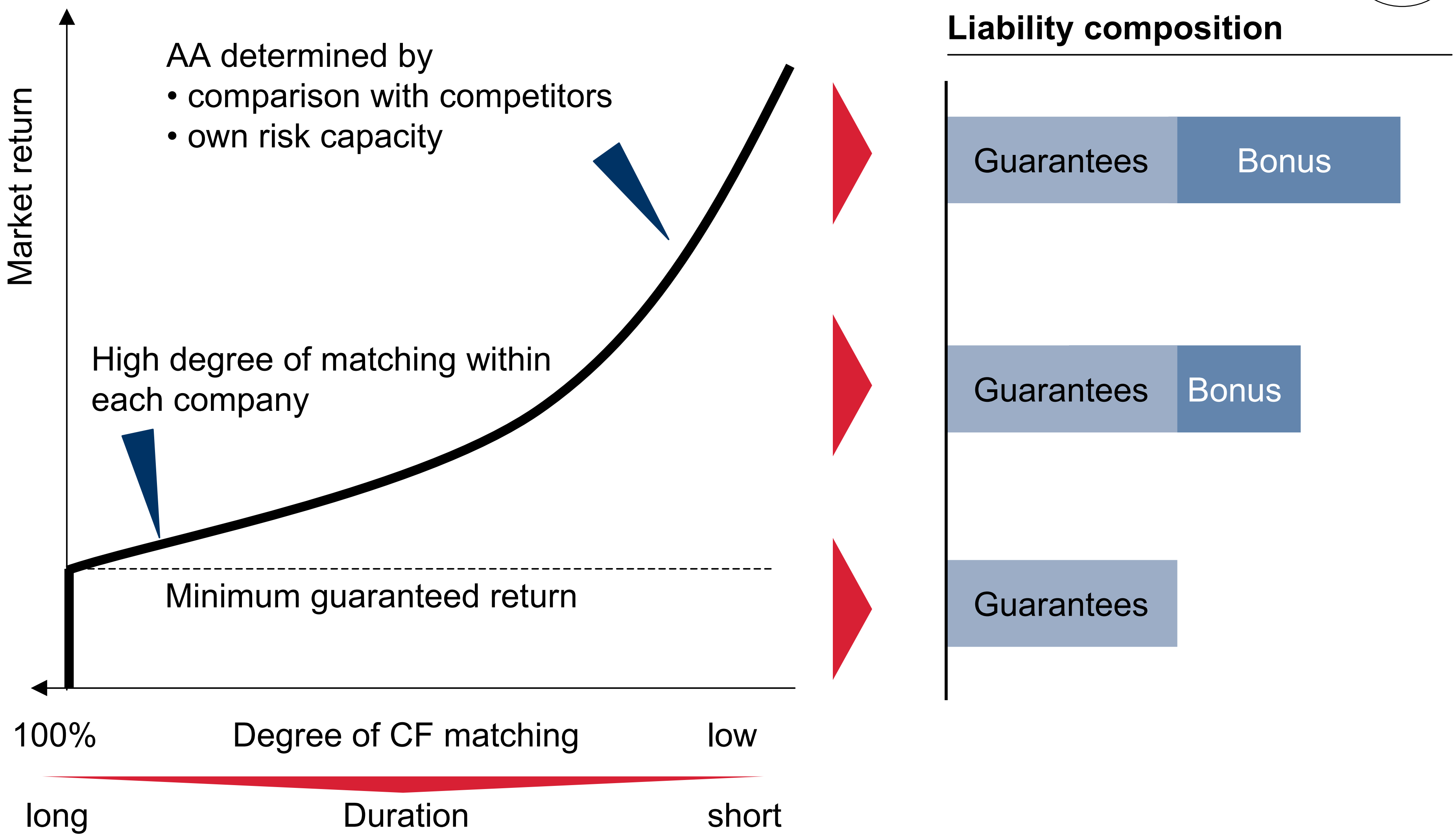
Crediting policy takes into account competitors' behavior



Changes in liability notation lead to the expression of "insurance obligations"



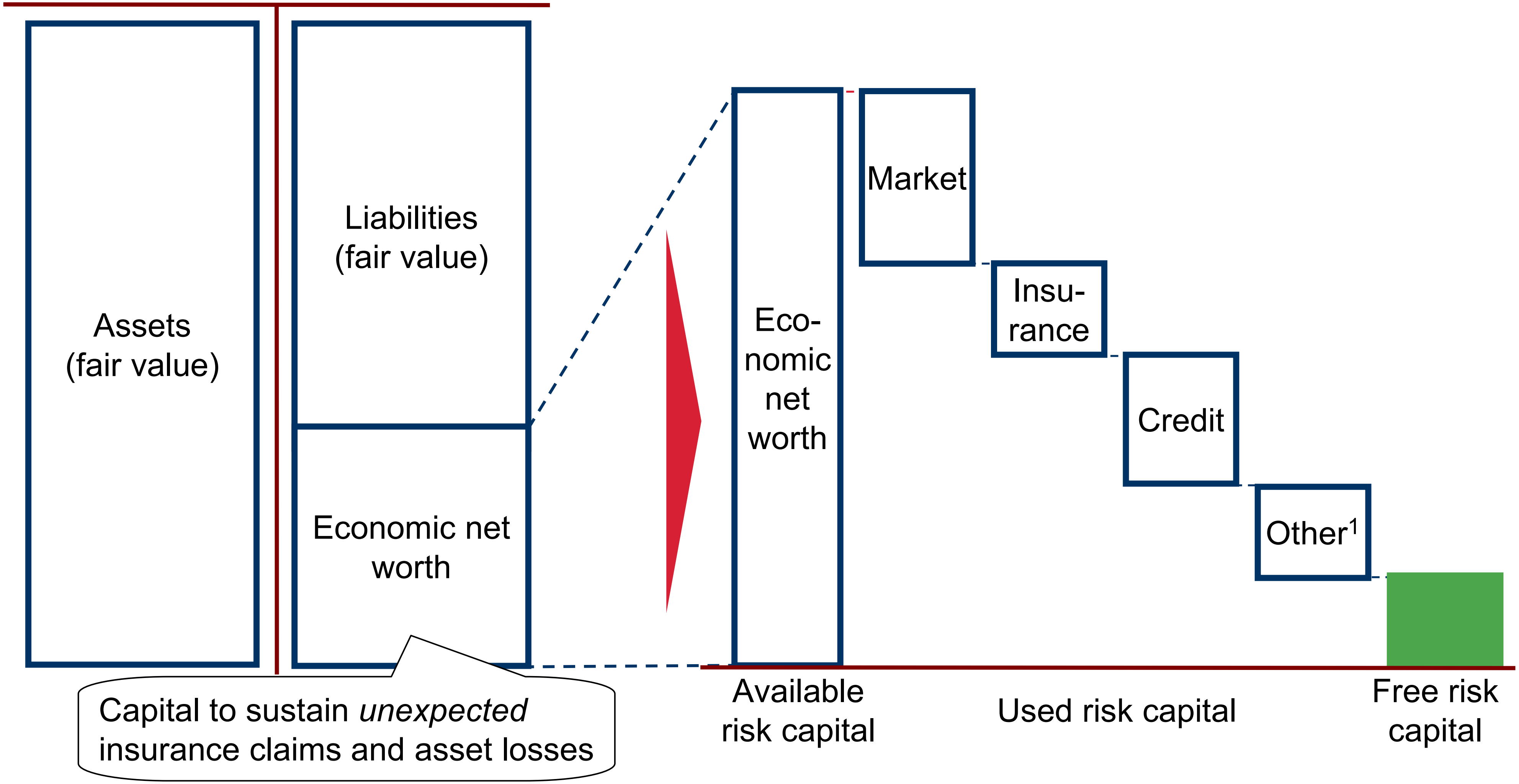
Liability cash flows are complex in reality and vary with market returns



Risk budget defines the free risk capital

Conceptual

Marked-to-market balance sheet **Risk budget**



[1] I.e. operational, business and strategic risk

Note: Waterfall shows risk contribution of individual risk types net of diversification effect

The SST[1]-target capital needs to be determined

Analytical model
(expected shortfall as risk measure)

Market risks

Insurance risks

Scenario aggregation

e.g.,
- pandemic
- financial distress
- reinsurance defaults

weighted average of scenarios with results from analytical model

\+

Credit risk charge

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Risk margin

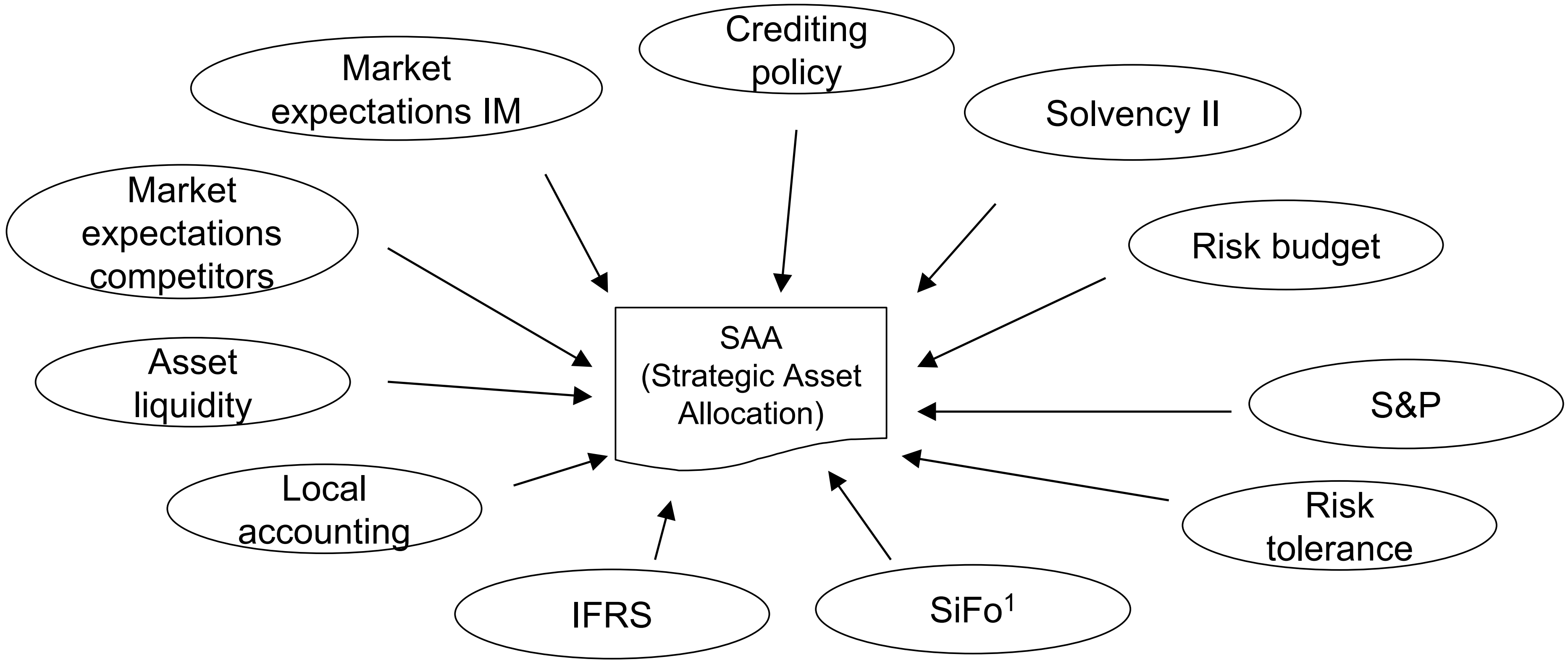
=

Target capital

[1] Swiss Solvency Test

The SAA is influenced and/or constrained by various factors

Illustrative



Inputs have different weightings leading to a situation where we might end up having one single input as a must and thus a “killer” constraint for the SAA

[1] SiFo (security fund): Regulatory coverage ratio of assets to liabilities

Risk/return considerations and non-economic constraints determine SAA

Risk

- Risk budget
  - Economic net worth
  - Free risk capital
- Measures to generate further risk capital
- Risk tolerance

Non-economic constraints

- Security fund
- Solvency margin
- Target capital
- IFRS accounting mismatch
- Earnings at risk

SAA

- Expected return & risk by asset class
- Feasibility
- Competitor behavior
- Portfolio optimization

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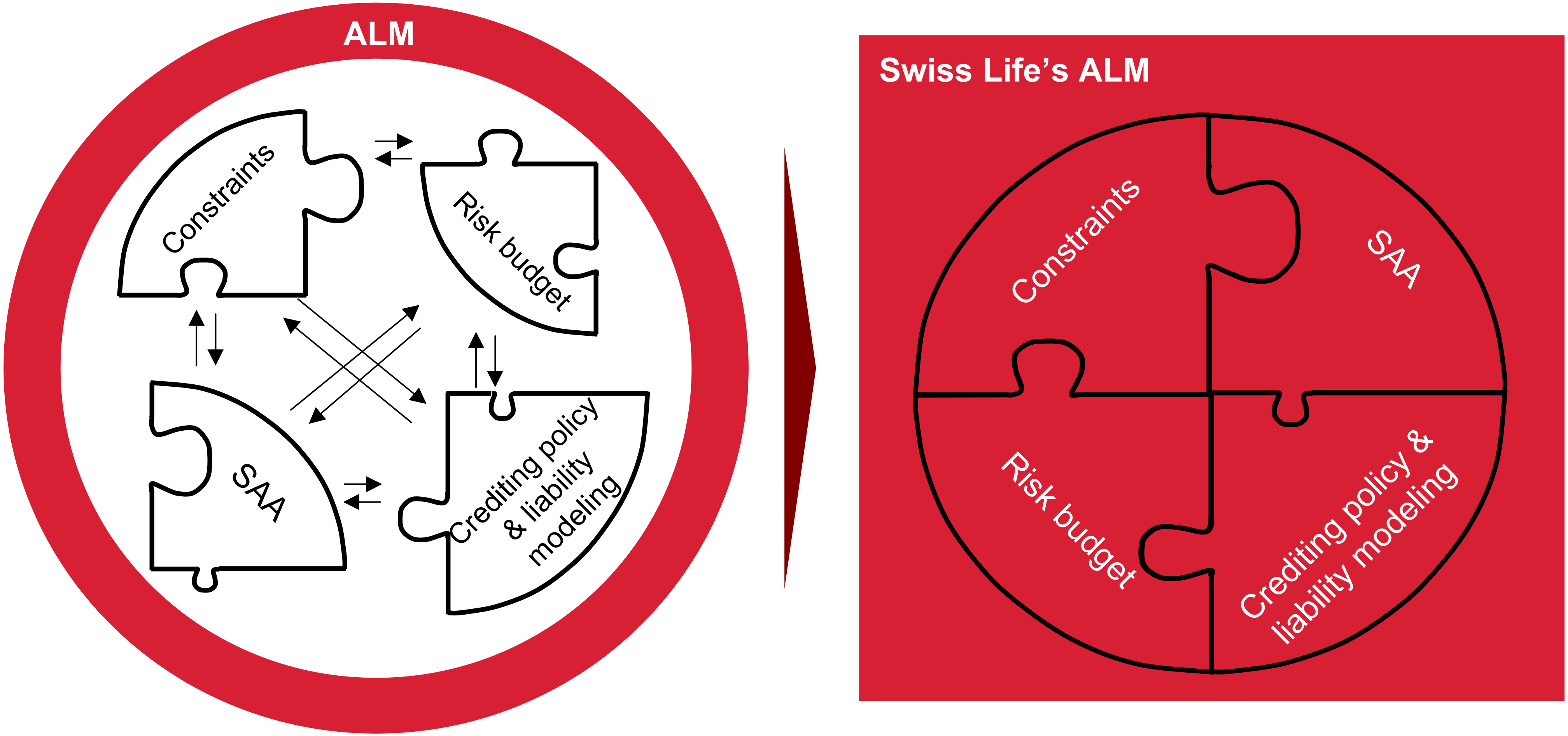
Closed-looped system is necessary to appropriately weight all elements

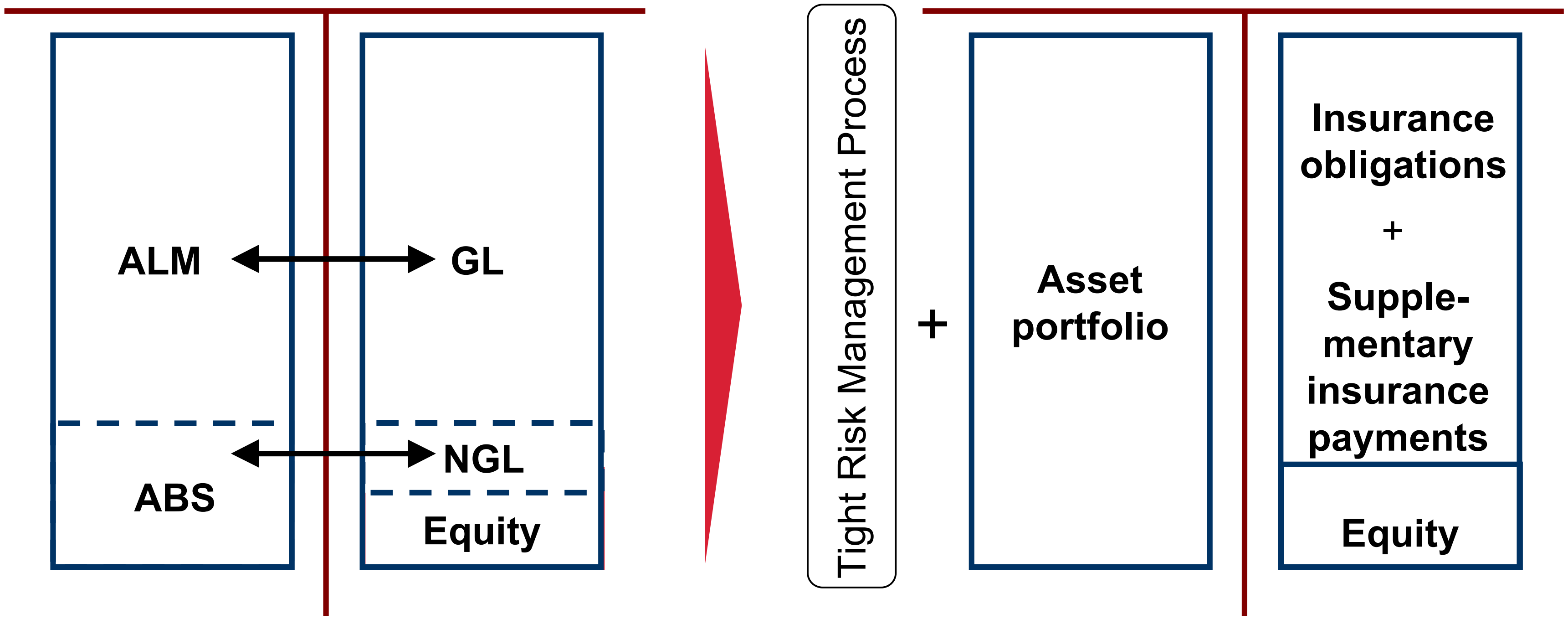


- Each ALM element by itself might be controllable
- The art of ALM lies in balancing out every element with the others
- Communication among the involved departments is crucial

The new business model will be implemented in a holistic approach

Conceptual

New business model | **Implementation approach**



Benefits through holistic approach

- Simplicity through only one portfolio on asset side
- Without neglecting liability structure in AA

Note: ALM: ALM portfolio; ABS: absolute return portfolio; GL: guaranteed liabilities; NGL: non-guaranteed liabilities

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Further development

- Roll-out to all business units
- Achieve further know-how development and transfer between headquarters and business units
- Further improvement of cooperation between involved departments
- Monitor development of SST/Solvency II

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SwissLife

Iris Welten Head Investor Relations	Tel. E-mail:	+41 (43) 284 67 67 iris.welten@swisslife.ch
Fabrizio Croce Manager Investor Relations	Tel. E-mail:	+41 (43) 284 49 19 fabrizio.croce@swisslife.ch

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