

The background of the slide features a complex overlay of financial data. It includes several line graphs with fluctuating lines, some with upward and downward arrows indicating trends. There are also numerous numerical values and percentages scattered across the scene, such as '15.22', '95.84', '79.60', '63.85', '37.93', '12.47%', '+15.22', '4.59', '27.08', '11.77', '78.64', '13.51', '58.49%', and '78.24'. The overall color scheme is a monochromatic blue, giving it a professional and data-driven appearance.

## INVESTING IN THE INSURANCE SECTOR

**Insurance Private Debt's attractiveness and resilience explained in six charts**

**March 2023**



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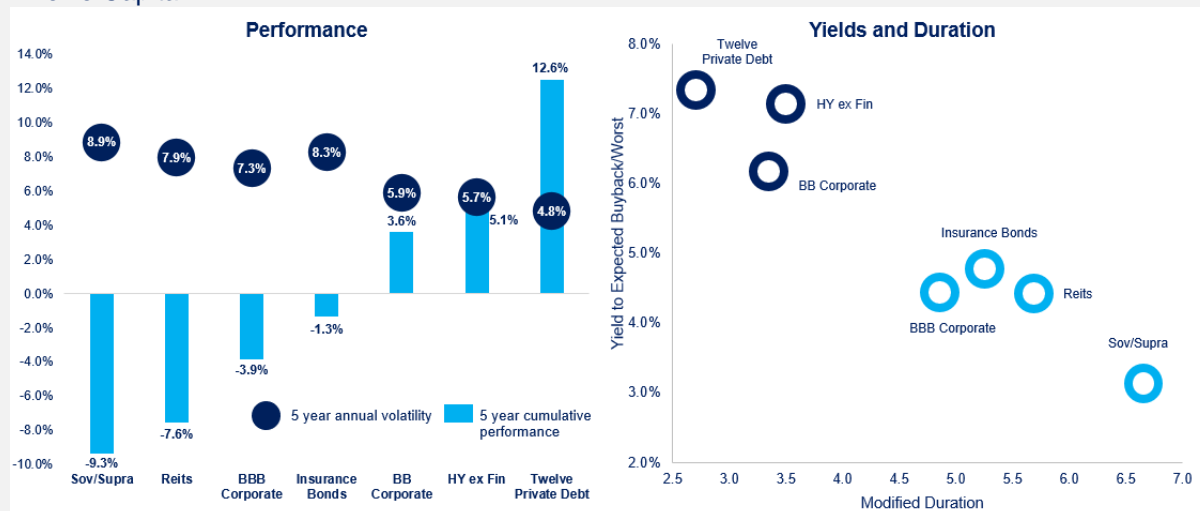
## Executive Summary

- Higher interest rates and wider spreads offer an attractive entry point
- Insurers’ resilient capital positions typically show positive correlation to higher interest rates
- Low debt leverage and high interest coverage are a competitive advantage in a higher interest rate environment
- The insurance sector is expected to grow steadily even during recession as policyholders aim at narrowing the protection gap
- High inflation is absorbed by premiums growing at a faster pace
- The sector has strong ESG credentials, underpinned by low greenhouse gases intensity and strong governance frameworks

Twelve Capital believes its Insurance Private Debt offering shows attractive risk/return opportunities thanks to higher spreads and yields, together with insurance issuers’ resilient capital positions, low leverage ratios and solid ESG credentials. Twelve thinks that in particular smaller and mid-sized insurers show more resilient credit profiles in an inflationary and recessionary environment relative to general corporate issuers.

## Convincing returns compared with other asset classes

Figure 1: Past performance, current yields and duration of a Private Debt portfolio\* managed by Twelve Capital



Source: Bloomberg, Twelve Capital. As at 31 January 2023. BB Corporate: Bloomberg Pan-Euro HY BB Rating Only, HY ex Fin: Bloomberg Pan-European HY ex Fin Total Return, Sov/Supra: Bloomberg Pan-European Aggregate Sovereign/Supranat AA Total Return Index, BBB Corporate: Bloomberg Pan-European Aggregate Corporate Baa Statistics Index, Reits: Bloomberg Euro-Aggregate REITS Total Return Index, Insurance Bonds: Bloomberg Pan-Euro Corporate Insurance Index Past performance is not indicative of future returns. The money invested can both increase and decrease in value and you may not get back the full invested amount. \*Inception date 10/2015, size EUR 68m, contains also liquid bonds.

The increase in interest rates and the corporate spread widening of 2022 offer attractive investment opportunities in the Insurance

Private Debt space, with newly issued transactions offering yields between 8% and

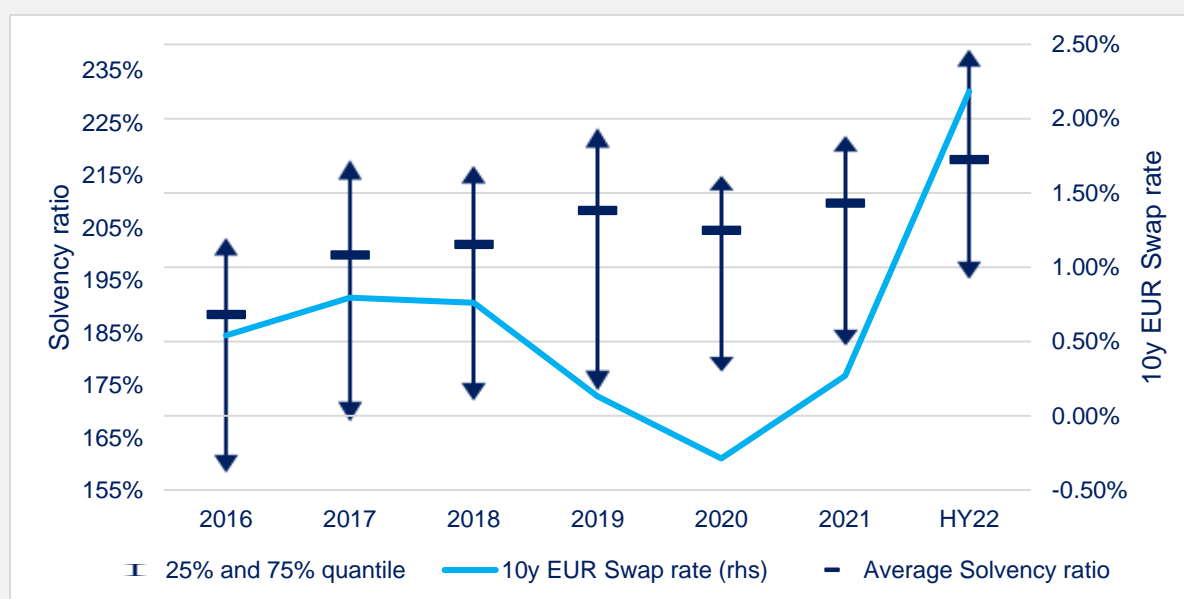
12%.<sup>1</sup> Looking backward, Private Debt products managed by Twelve Capital have delivered attractive returns with typically lower volatility compared to various corporate indexes. The yield achievable with Insurance Private Debt portfolios managed by Twelve Capital compares well with high-yield fixed income, while showing shorter duration and allocating to a sector that is better positioned in

an inflationary, rising rate environment and in periods of recession.

Lastly, our portfolios are conservatively positioned in term of credit risk and the historical annual cost of default are broadly in line with S&P's and Moody's long-term default statistics for BB rated credits.

## Resilient capital positions that typically benefit from rising interest rates

Figure 2: Solvency ratios and 10y EUR Swap rates



Source: Twelve Capital, Bloomberg, Companies' reporting. As at 31 December 2022.

The solvency position of the c.a. 100 issuers we monitor in Europe and Bermuda has improved since 2016 by 30 percentage points on average. This is a reflection of positive economic earnings, improved product features, investment de-risking, and calibration of the solvency formula. Moreover, in 2022-2023 we flag that insurance is one of the few sectors where underlying creditworthiness is typically positively correlated to increasing interest rates. This contributed to stronger solvency ratios, which means more remote likelihood of default and coupon deferral.

In fact, in economic regulatory frameworks such as Solvency II, higher interest rates reduce the

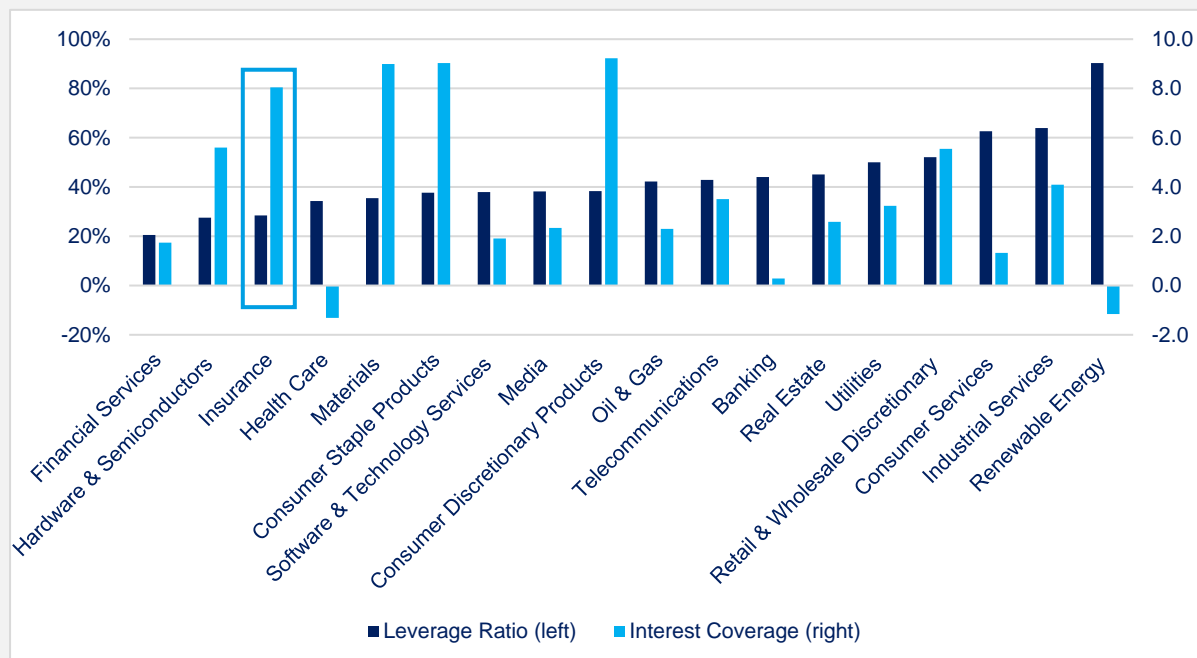
market value of assets but the discounted present value of liabilities also diminishes. With asset duration typically being shorter than liabilities, economic own funds have increased. At the same time capital requirements decrease, particularly for life companies, thanks to lower cost of guarantees and options.

However, exemptions exist, for example for some traditional life savings providers that would be more exposed to lapsation risk in a higher-rates environment.

<sup>1</sup> Past performance is not indicative of future returns. The money placed in the fund can both increase and decrease in value and you may not get back the full invested amount.

## Low debt leverage and comfortable interest coverage ratios

Figure 3: Leverage and interest coverage



Source: Bloomberg, Twelve Capital. As at 31 January 2023.

Insurance companies typically have lower debt leverage and stronger interest coverages than general corporates. The chart shows that small and mid-sized insurers have one of the lowest debt-to-capital ratios and they comfortably cover debt interests' cost with adjusted operating earnings. These specificities are key in periods of rising interest rates when financing costs increase and in recession, when corporate revenues tend to shrink.

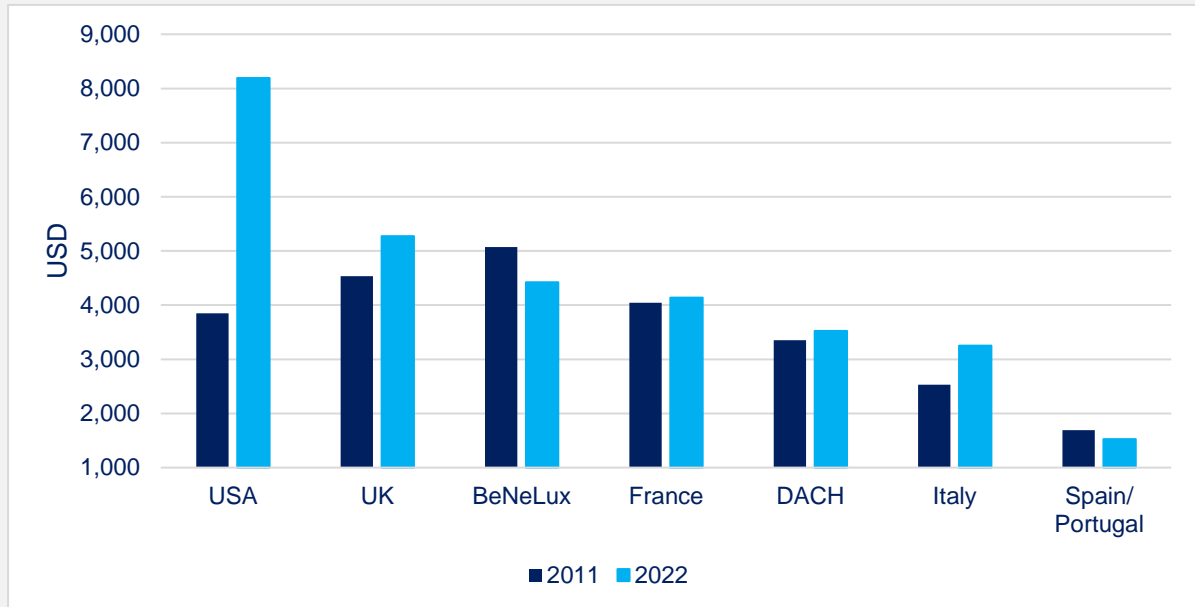
Insurers have a specific cash flow profile: they first collect premiums, invest them and receive the proceeds, and then they register a pay out to policyholders in case of claims. For this reason, insurance companies do not need

senior debt financing to operate. They do typically raise regulatory compliant subordinated debt to build capital buffers. Conversely, corporates typically rely on debt capital markets to finance the set-up and research and development of their operations.

Moreover, insurance in the developed markets we target is a mature business underpinned by positive cash flow profiles and sustainable profitability. In fact, the sector has reported positive RoE through the cycle and also during periods of financial and economic turmoil.

## Insurance spending per capita is on an upward trend through the cycle

Figure 4: Premiums per Capita 2011-2022



Source: Swiss Re Sigma research, Twelve Capital. As at 31 December 2022.

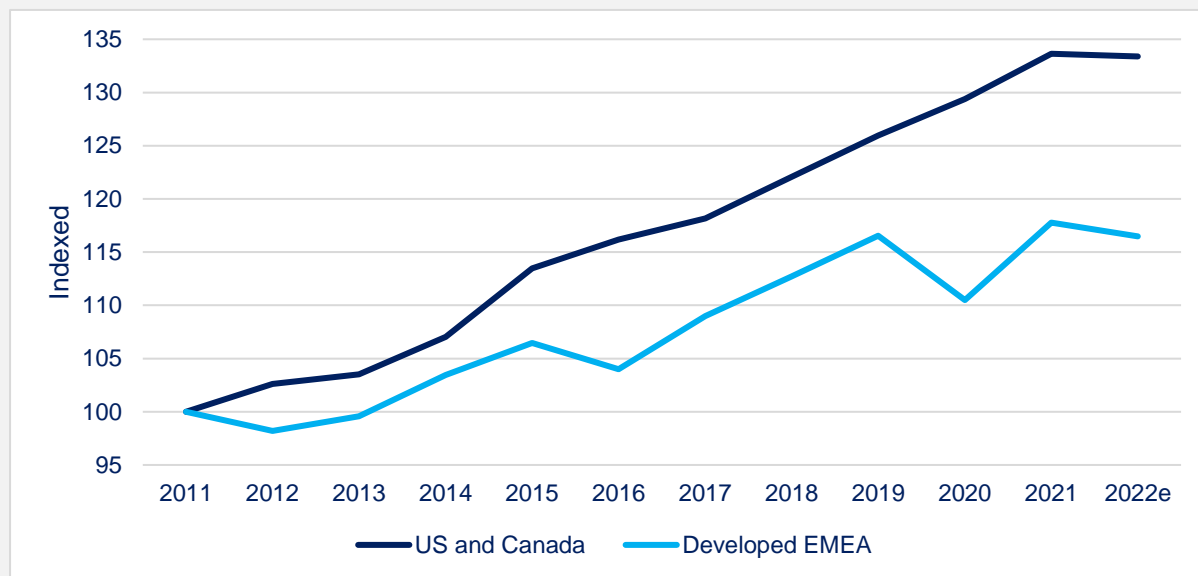
Insurance spending per capita has generally increased over the past ten years in mature markets. We believe policyholders tend to fill the protection gap by increasing their coverage against natural perils, by expanding their complementary health coverages and by complementing state-backed retirement programs.

In periods of recession most businesses see shrinking revenues, as individuals and corporates tend to cut the spending on non-necessary items. This is not the case for

insurance, as during recessions we observe that policyholders tend to stick to their insurance coverages in order to reduce the risk of large and unplanned spending in case of claims. Moreover, many insurance products such as Motor Third Party Liability, property and term-life covers on mortgaged homes, or complementary health are mandatory in many countries and therefore sheltered by potential drops caused by lower spending in a recession.

## Insurance premiums have grown faster than inflation

Figure 5: Premium Growth Net of Inflation



Source: Swiss Re Sigma research, Twelve Capital. As at 31 December 2022.

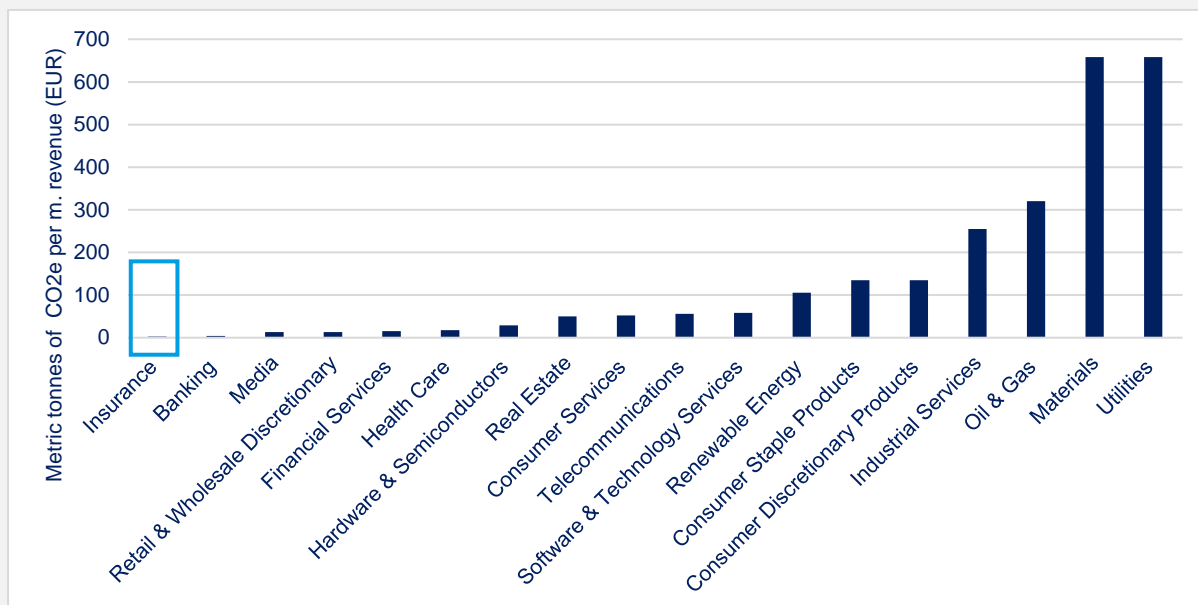
In the markets where our Private Debt targets operate, premium growth has largely outpaced the level of inflation over the past years. Over the long run, the cost of insurance claims tend to grow in line with inflation. The fact that premiums grew ahead of inflations suggests that insurers managed to defend their margins and profitability over the past decade. This is positive for the sector's creditworthiness and for investors. We believe this trend to continue in the next years, although to a lesser extent in a scenario of protracted high inflation.

Past years' growth has been particularly strong in property and casualty insurance and in north

America. When digging into specific lines of business we see strong increases in pricing in commercial risks, hurricane coverages in exposed areas such as the South-East of the USA, and cyber. We would flag that many contracts have embedded automatic clauses that allow for adjusting premiums rates upward at the renewal of the policy in order to capture the effect of higher inflation.

## The insurance sector has strong ESG credentials

Figure 6: Greenhouse Gas Intensity\*



Source: Bloomberg, Twelve Capital. As at 31 January 2023. \*Intensity measured as metric tonnes of carbon dioxide equivalent (CO2e) divided by revenues in millions normalised to Euro.

The sector has a very low carbon footprint when looking at greenhouse emissions relative to revenues (GHG level 1 and 2). Moreover, insurers contribute to foster climate resilience globally by managing the challenges of climate change. Insurers are not only instrumental in closing the protection gap for natural disasters but also for pension and health coverages.

When looking at governance aspects, the highly regulated insurance sector is traditionally equipped with strong governance frameworks and subject to strong oversight by authorities. Lastly, insurers are amongst the largest institutional investors with influence on the strategy, governance and ESG choices of the companies they invest in.

### Key risk associated with investments in Insurance Private Debt include

**Concentration in one industry risk:** When a portfolio is reliant on one industry or market segment (i.e., insurance industry), this creates concentration of credit risk. Thus, it increases the likelihood that a single impact can have a big effect.

**Counterparty risk:** The counterparty in a credit, or trading transaction may not fulfil its part of the deal and may default on the contractual obligations.

**Interest rate risk:** In particular fixed rate securities may be affected by changing interest rates which may reduce or increase the market value of a bond.

**Liquidity risk:** Potentially, certain instruments may not be liquidated in a reasonable time frame.



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