Insurer Investment Forum XXII

It's a Sci-Fi World

March 24, 2022

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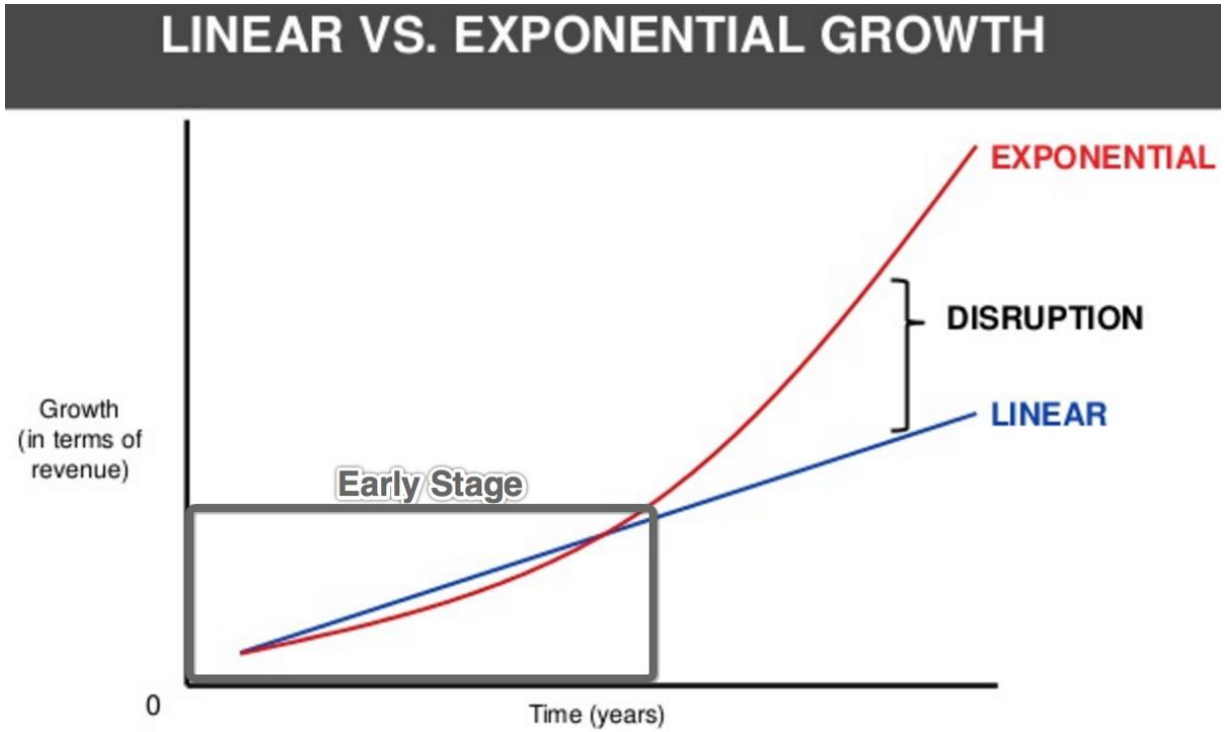
President & Chief Executive Officer

STRATEGIC ASSET ALLIANCE
THE INSURANCE INVESTMENT SPECIALIST

CAN WE JUDGE CHANGE ACCURATELY?

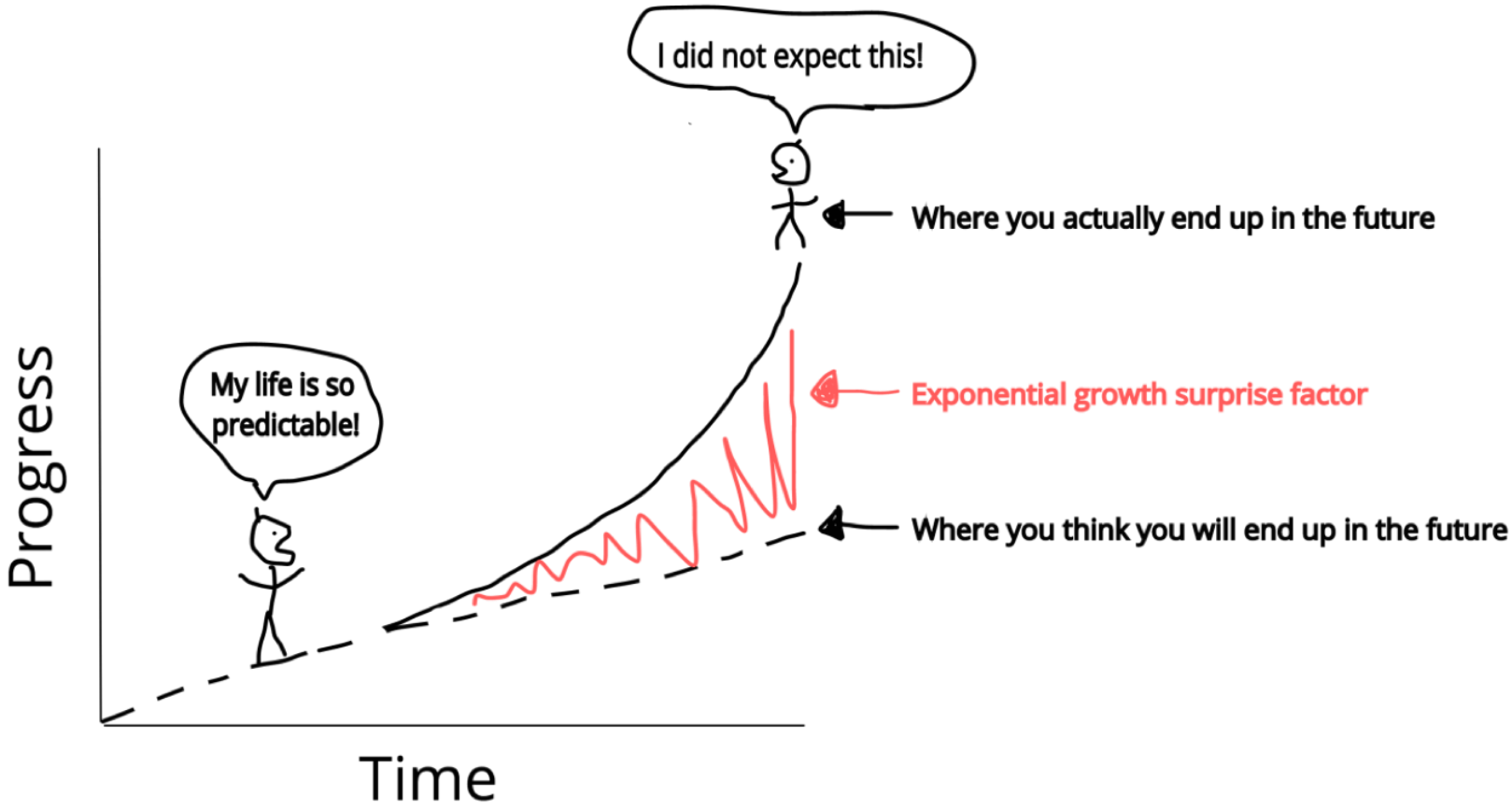
What is the pace of change?



Over time, humans have gotten proficient at predicting what will happen next, using a linear pattern as a guide. "I've always burned my hand when I put it too close to the stove top, so I know it will happen again." Obviously, that is a key skill.

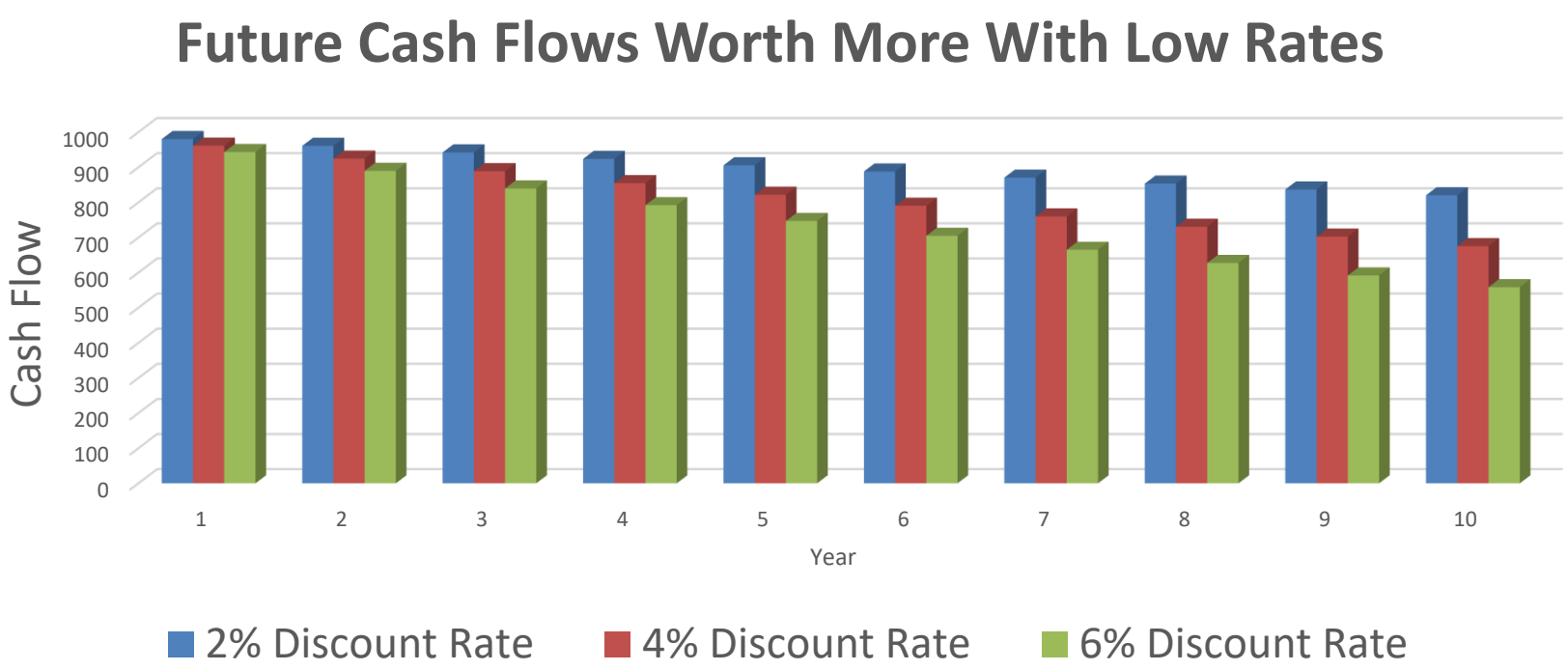
Where we are not good at predicting is when there is an exponential trend to consider. Exponential trends don't look very exponential at first. In fact, they seem slower than a linear trend. But, over time, like the allowance of the kid who gets his parents to agree to give him one penny on week one and double it every week thereafter, exponential trends can spell big change and, sometimes, disruption.

From a practical perspective



INTEREST RATES CHANGE THE VALUE OF THE FUTURE

Future is worth more

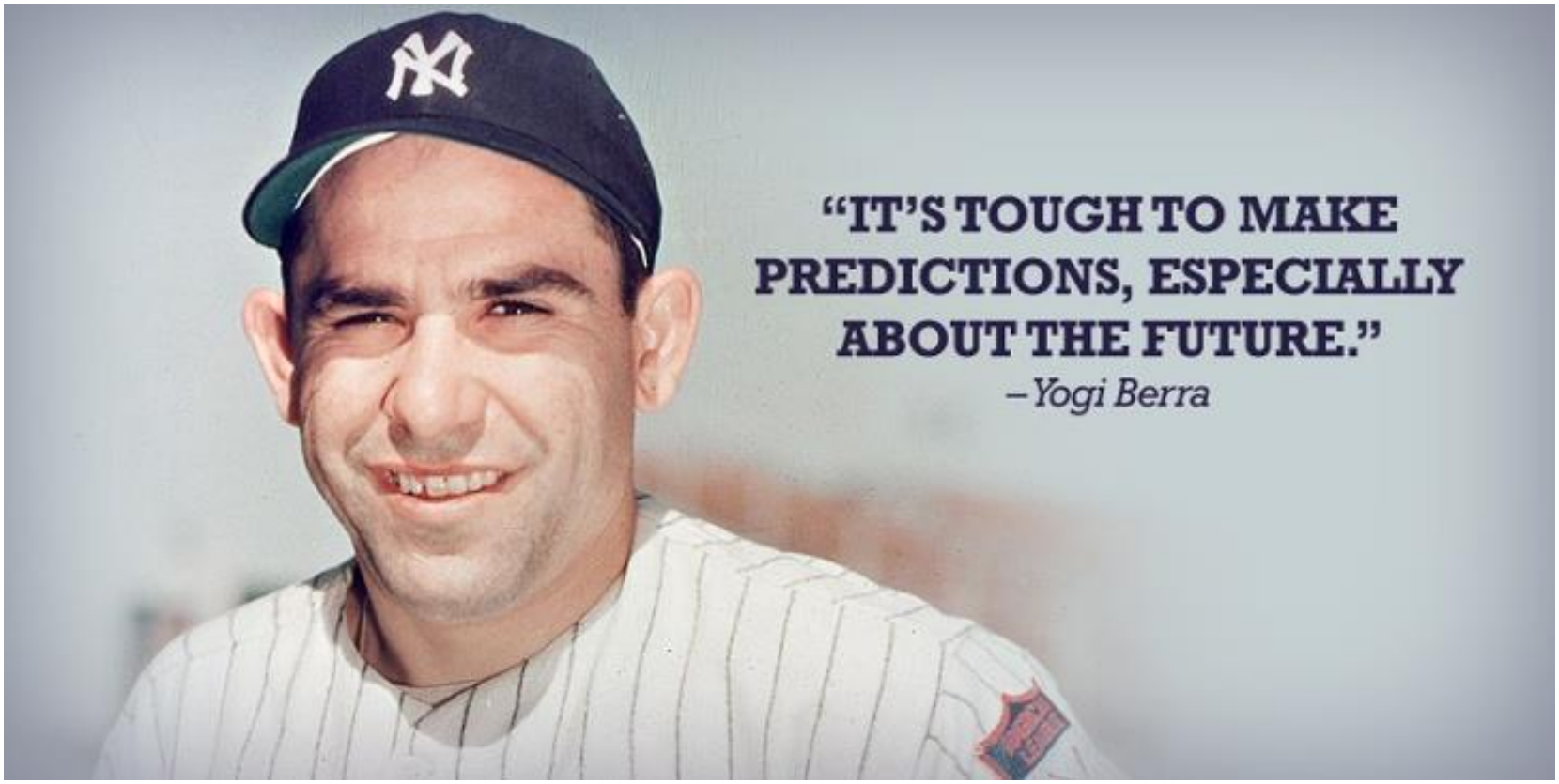


Here's a graph showing the value of receiving $1,000 after one year, two years….all the way to ten years. When we try to value those cash flows, we use the concept of present value or what amount is equivalent to receiving that $1,000 in several years from now.

This graph then notes that interest rates do change, and the higher today's interest rate, the less valuable that same $1,000 is several years from now. And, how are rates today. Way too low! So, that means because of low interest rates, the impact of future activities has a greater impact on us than when rates are higher.

HOW LONG A TIME FRAME SHOULD WE CONSIDER?

Making predictions



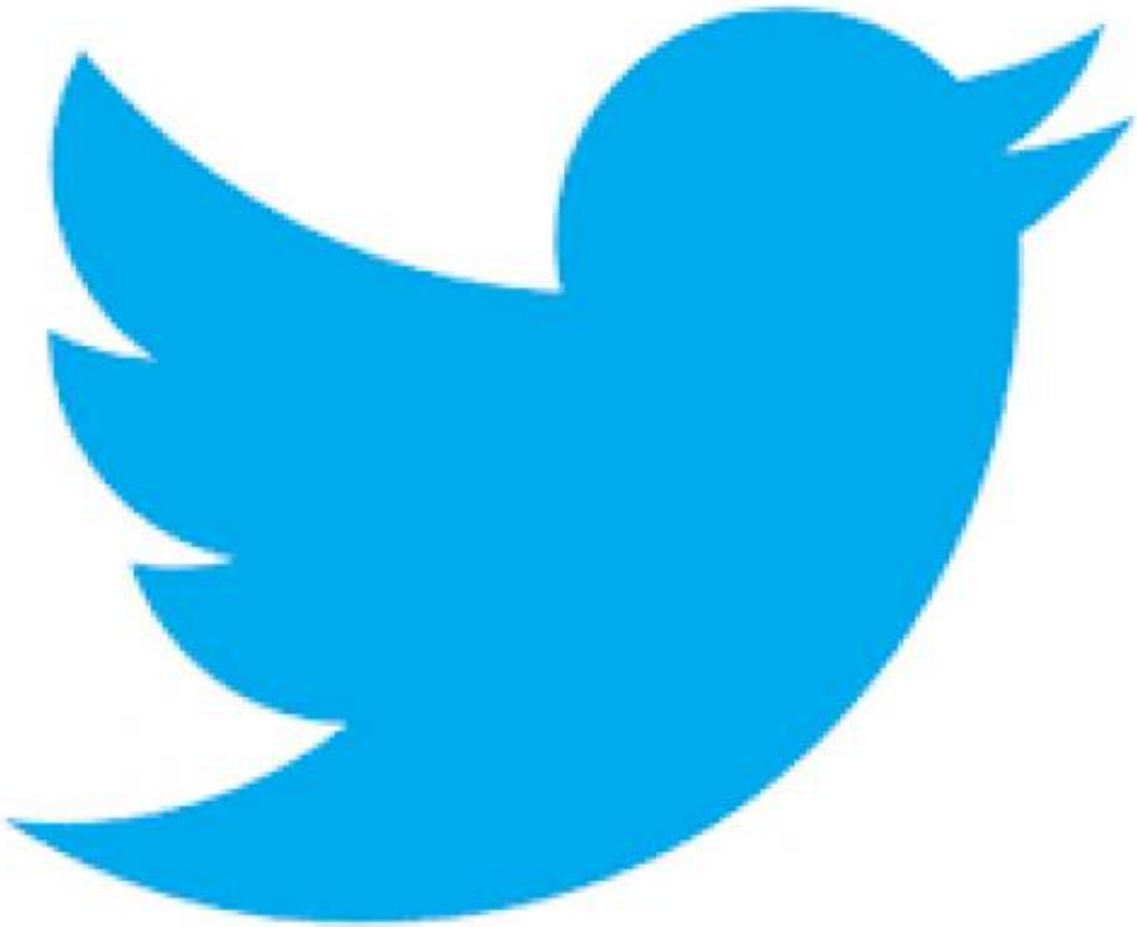
Recent history as a guide: 2004

Recent history as a guide: 2005

YouTube

Broadcast Yourself ™

Recent history as a guide: 2006



Recent history as a guide: 2007

Recent history as a guide: 2008

airbnb

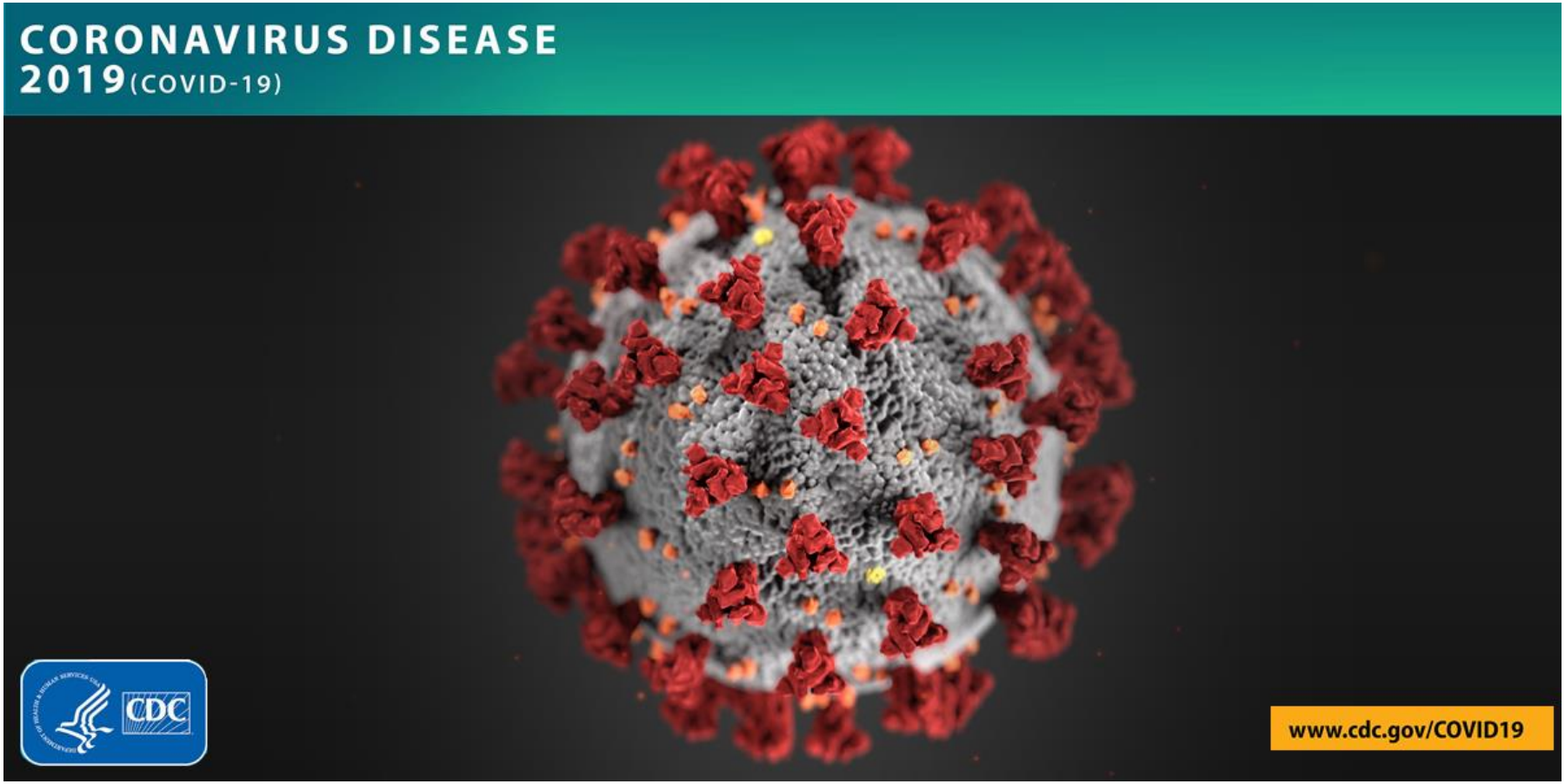
Recent history as a guide: 2010

Recent history as a guide: 2015

Recent history as a guide: 2016

Unexpected recent history as a guide: 2016

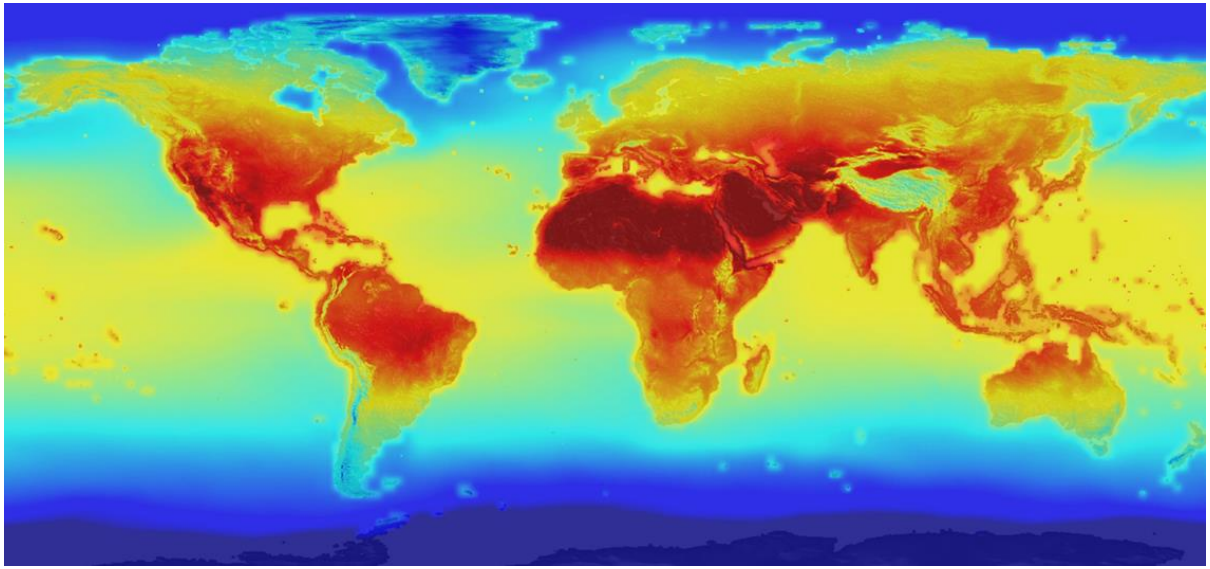
Unexpected recent history as a guide: 2019



Unexpected recent history as a guide: 2022

TRENDS TO CONSIDER

Climate Change



As a global problem, we will need a global solution. And therein lies a bigger problem – getting multiple countries to come to a firm agreement that they all comply with. This is complicated by the projected varying impact that climate change will have on the developed versus the developing world and their inherent varying levels of economic resources to address the problem.

Putting this into perspective with the impact of the Russian invasion of Ukraine: Some analyses say Russia can keep up the aggression as long as they can afford it – and that means they must be able to sell oil and natural gas, primarily to Europe. The responses to this have been sanctions, yes, but not yet on those oil and natural gas shipments. Interestingly, there are two main responses to reducing reliance on Russian carbon fuels. The Europeans are looking seriously at increasing investment in alternative energy (wind, solar) and nuclear energy. Meanwhile, the Americans are taking a different tack and looking to increase the production of oil and natural gas.

Climate Change: The ‘E’ in ESG

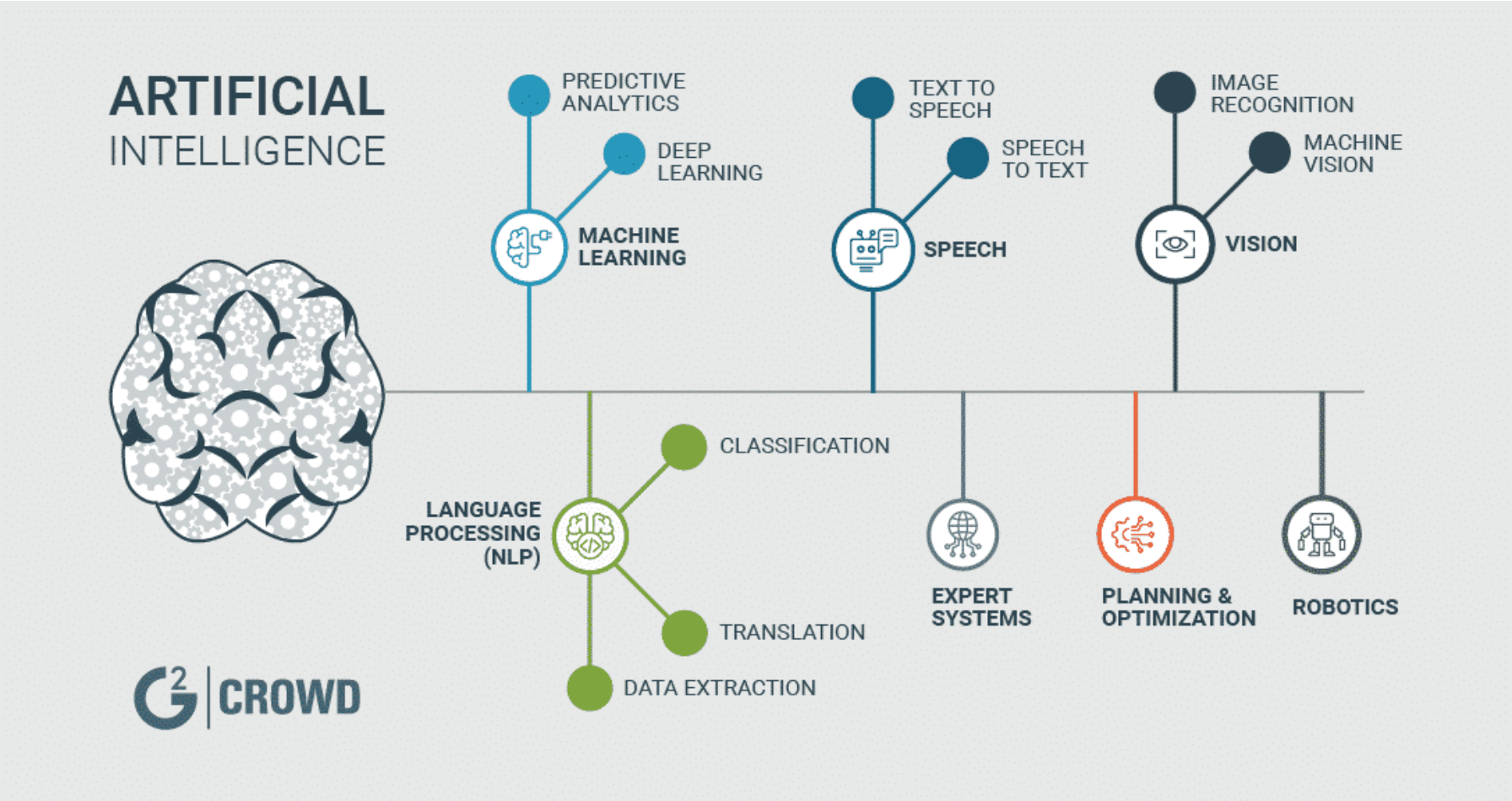
Climate Change: The ‘E’ in ESG

ESG is complicated and there can be a case made that its promotion is less about doing good and more about various players in the investment industry looking for a new line of business.

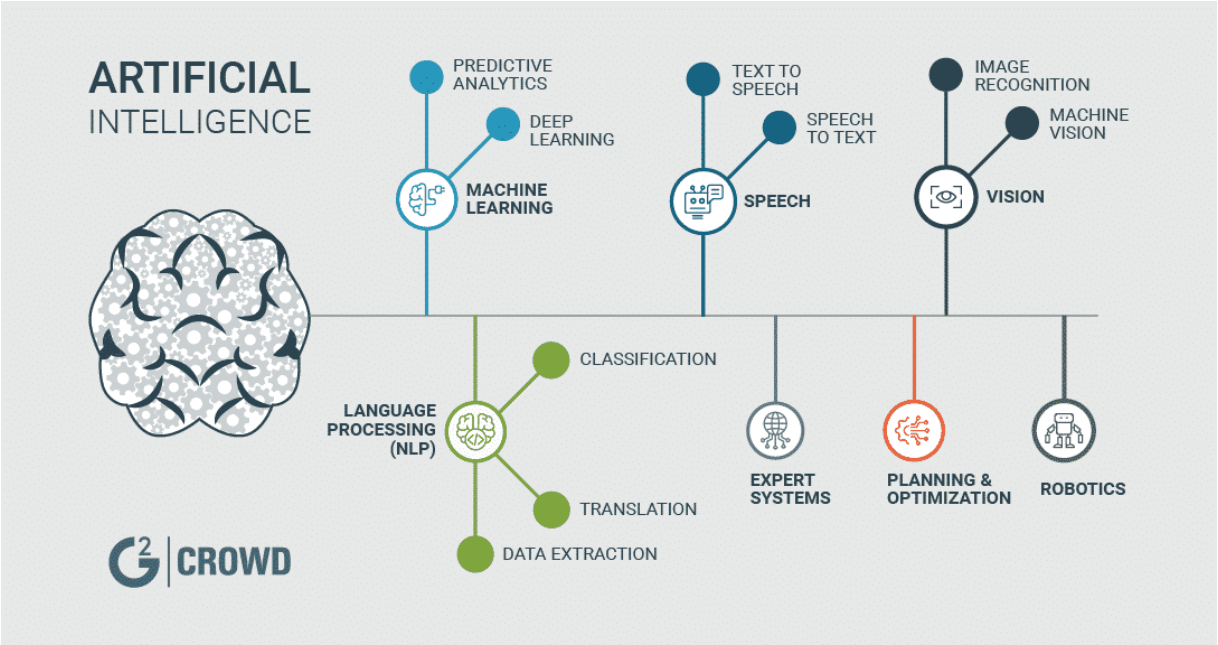
For example, studies have shown that the various rating agencies that have sprung up to provide ESG ratings promote ratings with little positive correlation amongst those ratings. In other words, agency X can provide a high ESG rating, while agency Y can provide a much lower ESG rating, all for the same company. This problem also means that funds dedicated to ESG – and attracting trillions of dollars in investments – may not really be investing in companies closely following ESG principles.

Finally, a word of caution: Investment managers and rating agencies say they have ‘always considered’ ESG. Don’t believe them. But do get them to show you how they focus on it now, because it will be an ongoing and growing issue, especially for many regulators.

Artificial Intelligence: Uses and Abuses



Artificial Intelligence: Uses and Abuses

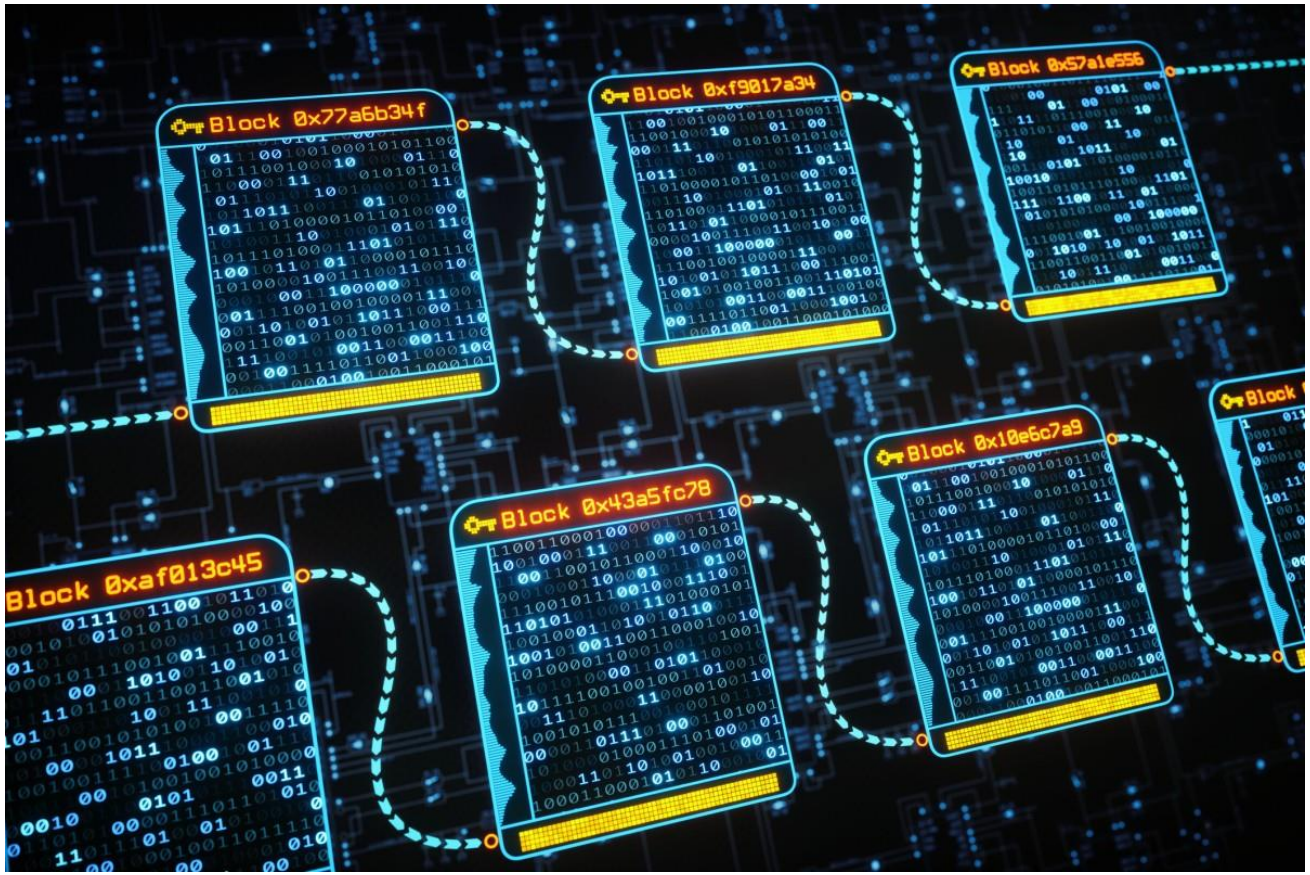


AI is more than just having a computer make decisions:

- Machine Learning allows a computer to learn without being programmed.
- Robotics focuses on getting a machine to perform laborious tasks – sometimes simple, sometimes complex
- Expert systems focus on modeling how an expert thinks and solves problems

Natural Language Processing can be used in translation, sentiment analysis, and lo/no code work, to name a few areas.

Blockchain



To simplify, a blockchain is an immutable, decentralized ledger that can be used in various ways, financial and nonfinancial. Its uses are limited by our imagination. Importantly, any blockchain is subject to a trilemma of difficulty in achieving all three: decentralization, security, scalability.

Digital Assets

The world of digital assets is sometimes linked to the term Web3, but like the early days of the world wide web, I expect that many digital asset projects will fail.

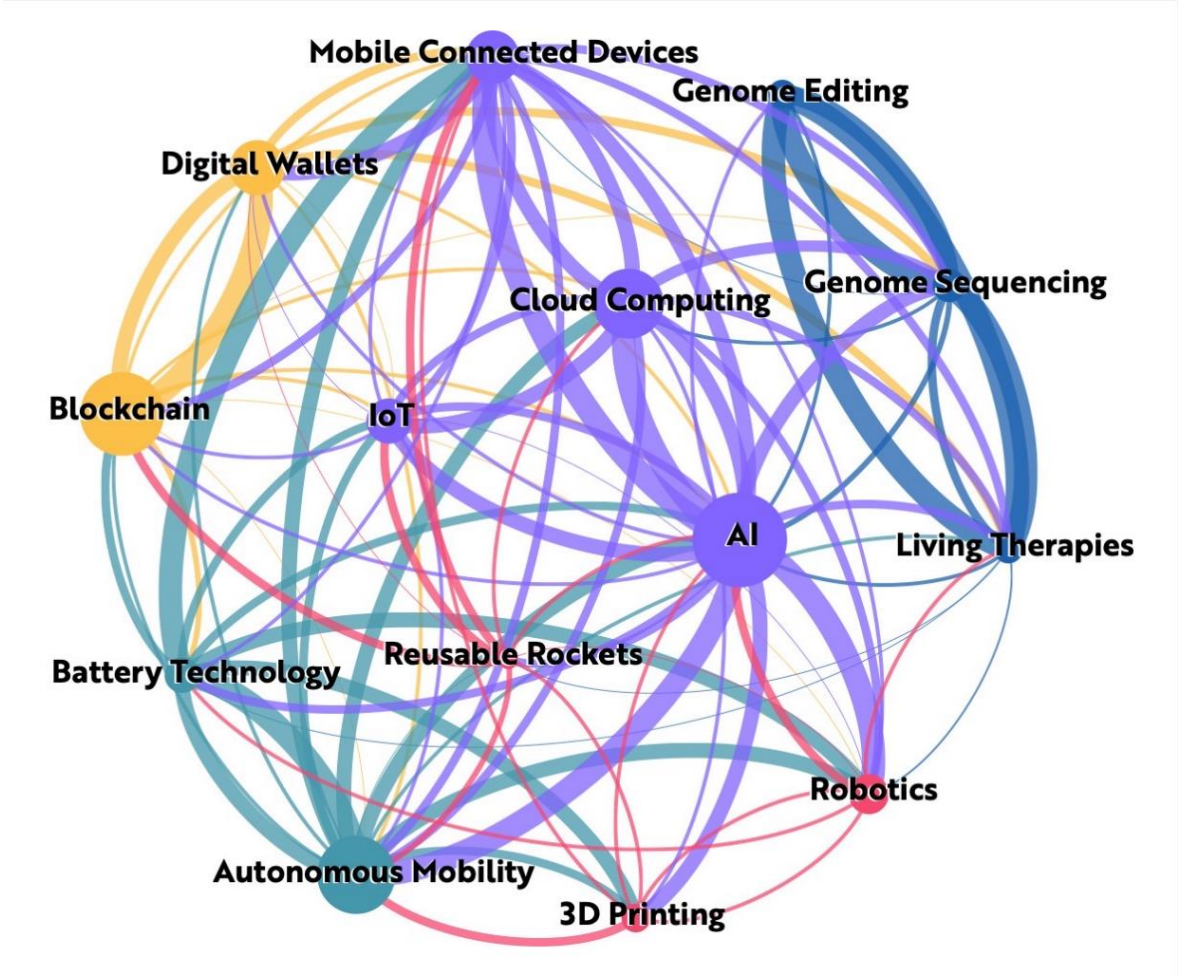
There is so much venture capital being poured into digital assets that I expect with the next five years, digital assets of various kinds: tokenized investments, DAOs (using governance tokens), premiums received, and claims paid via digital assets, and even the way banks and insurance companies do business will be materially impacted.

It will pose both opportunities and threats for all insurers.

Augmented Reality (AR)

Virtual Reality (VR)

Convergence



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