

# INVESTMENTS 101

A Primer for Insurance Investment Decision-Makers

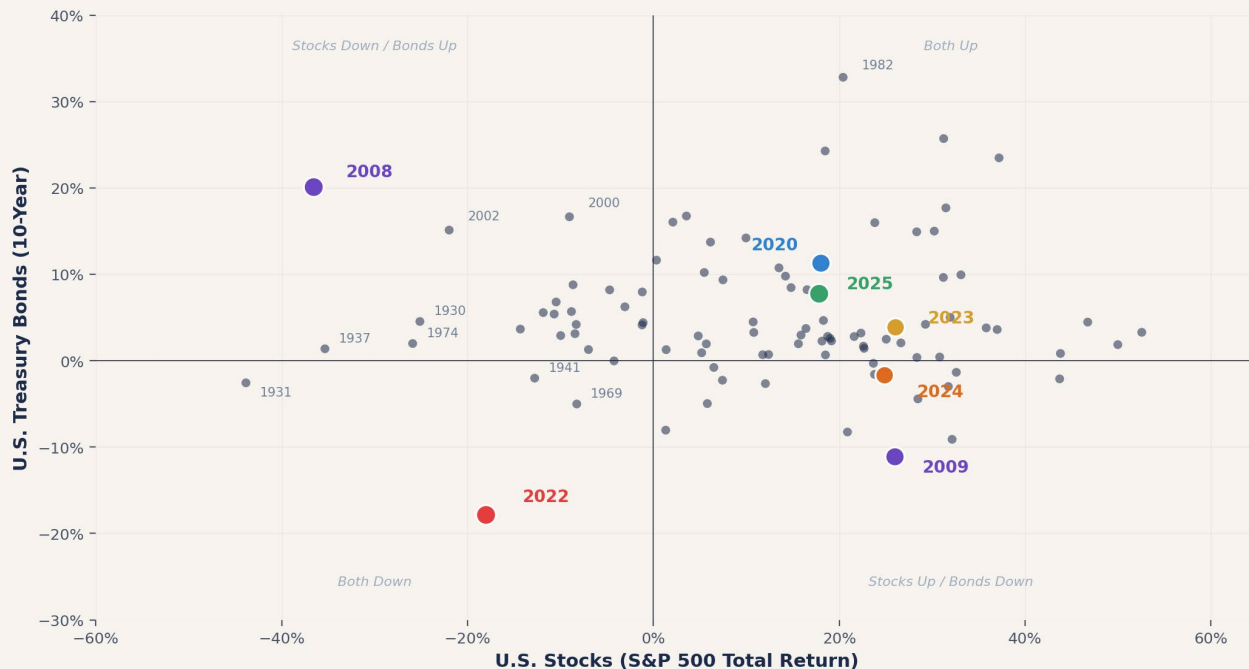
---

Insurer Investment Forum | March 24, 2026



# 97 Years in One Picture

Stock & Bond Returns — 1928 to 2025



Source: Damodaran/NYU Stern (S&P 500 incl. dividends; 10-Year UST total return). 1928-2025.

## What You're Looking At

Each dot is one year. X-axis = stock returns. Y-axis = bond returns. Most years land upper-right. The outliers are where the lessons live.

## The Story in the Dots

**2008:** Stocks -37%. Bonds +20%.  
Diversification worked as designed.

**2009:** Mirror image. Stocks +26%, bonds -11%.  
Risk was rewarded.

**2020:** Both up. The Fed flooded the system.  
Everything rallied.

**2022:** Both down. Rarest outcome in 97 years.  
No place to hide.

**2023-2025:** Stocks recovered fast. Bonds still  
finding their way back.

# At the End of the Day, There Are Only Two Risks

*Everything else — volatility, tracking error, duration, spreads — is a means to measure these two.*



## LOSS OF PRINCIPAL

1

**You get back less than you put in.**

A credit default, a forced sale at a loss, a downgrade that craters market value. This is the risk everyone thinks about first — and the one most investment policies are built to prevent.

**Managed through:**

Credit quality limits, diversification, duration constraints, liquidity reserves



## LOSS OF PURCHASING POWER

2

**Your money comes back, but buys less.**

Inflation silently erodes value. A portfolio earning 3% in a 4% inflation environment is losing ground every day — even though the account statement looks fine. This is the risk most boards underestimate.

**Managed through:**

Real return targets, TIPS, equity exposure, growth-oriented asset allocation

**The tension:** Avoiding Risk #1 often guarantees Risk #2. The board's job is finding the right balance — not eliminating one at the expense of the other.

# Why Do Insurers Invest?

## \$ The Insurance Float

Members pay premiums before claims are paid out. That gap creates **investable assets** — the float.

The investment portfolio earns income on this float, directly supporting the organization's ability to:

- Price competitively
- Retain and attract members
- Build surplus for adverse events

## Investment Income Is the Differentiator

Member Contributions → Premium Revenue

Premium Revenue → Investment Portfolio

Investment Income → Claims & Surplus

*Without investment income, pricing must be higher — risking member attrition.*

# The Enterprise Risk Framework

*Investment risk is just one piece of the puzzle — it must complement your business risk.*



## Operational Risk

People, systems,  
processes, fraud



## Underwriting Risk

Pricing, loss  
frequency & severity



## Reserve & Reinsurance Risk

Adequacy,  
collectability



## Investment Risk

Market, credit,  
liquidity, inflation

**NET POSITION / SURPLUS — The Foundation That Supports All Risks**

# Every Investment Is One of Two Things

*This is the simplest and most important framework in investing. Everything else is detail.*

## LENDER

You lend money. They promise to pay it back — with interest.

### **Bonds**

Treasuries, corporates, munis, MBS

### **Loans**

Bank loans, direct lending, private credit

### **Cash & Equivalents**

T-bills, money market, CDs

OR

## OWNER

You buy a piece of something. You share in profits — and losses.

### **Stocks**

U.S. equity, international, emerging markets

### **Real Assets**

Real estate, infrastructure, commodities

### **Private Equity**

Venture, buyouts, co-investments

# What Is Fixed Income?

## Bonds = IOUs with a schedule

When you buy a bond, you're lending money. The borrower promises to pay you back your principal at maturity plus regular interest payments (coupons) along the way.

<b>Par Value</b>	The face amount — what you get back at maturity
<b>Coupon</b>	The annual interest rate paid on par value
<b>Maturity</b>	When the bond comes due and principal is returned
<b>Yield</b>	Your total expected return, factoring in price paid

## Why Insurers Love Bonds

- ✓ Predictable cash flows
- ✓ Capital preservation
- ✓ Liability matching
- ✓ Regulatory acceptance
- ✓ Lower volatility

# Fixed Income Sectors

*Not all bonds are created equal. Each sector offers different risk/return trade-offs.*



## U.S. Treasuries

Full faith & credit of U.S. government. The risk-free benchmark.



## Agency / GSE

Fannie Mae, Freddie Mac, FHLB. Implicit government support.



## Corporates

Issued by companies. Higher yield, higher credit risk.



## Municipals

State & local government debt. Often tax-exempt.



## Structured Products

ABS, MBS, CMBS. Cash flows backed by pools of assets.



## Short-Term / Cash

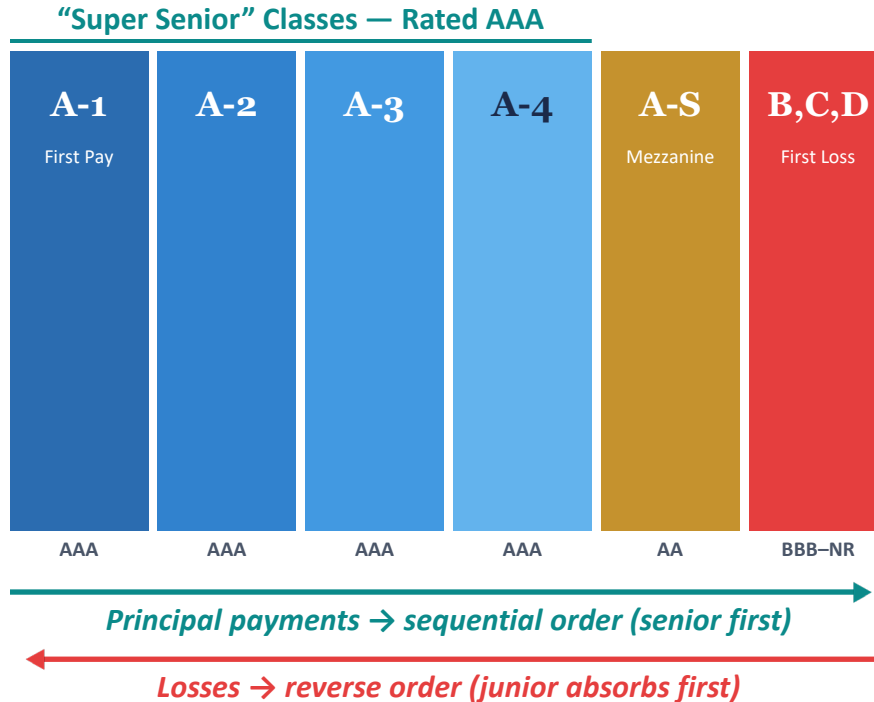
T-bills, commercial paper, money market. Liquidity first.

# The Capital Structure

How structured products turn one pool of mortgages into securities with different risk profiles.

**ASSET POOL**

Mortgage loans bundled into a trust (REMIC). Cash flows from borrower payments fund each tranche.



## Why Position Matters

Senior tranches get paid first and absorb losses last. That’s why they’re rated AAA — even if the underlying loans aren’t.

## Board Takeaway

When your manager says “structured products,” ask: **where in the stack are we?**

Senior AAA is a different animal than mezzanine or subordinate.

Adapted from NEAM. For illustrative purposes only.

# Understanding Credit Ratings

The rating scale is the market's shorthand for credit risk. Know where the line is.



## Key Concepts



### Rating Agencies

Moody's, S&P, and Fitch assign ratings based on ability and willingness to pay. Most investment policies require at least two ratings.



### Investment Grade (IG)

BBB-/Baa3 and above. Lower default risk. Most state insurance regulations and investment policies restrict portfolios primarily to IG securities.



### High Yield (HY)

BB+/Ba1 and below. Higher yield compensates for meaningful default risk. Spreads widen sharply in downturns — correlation to equities increases.

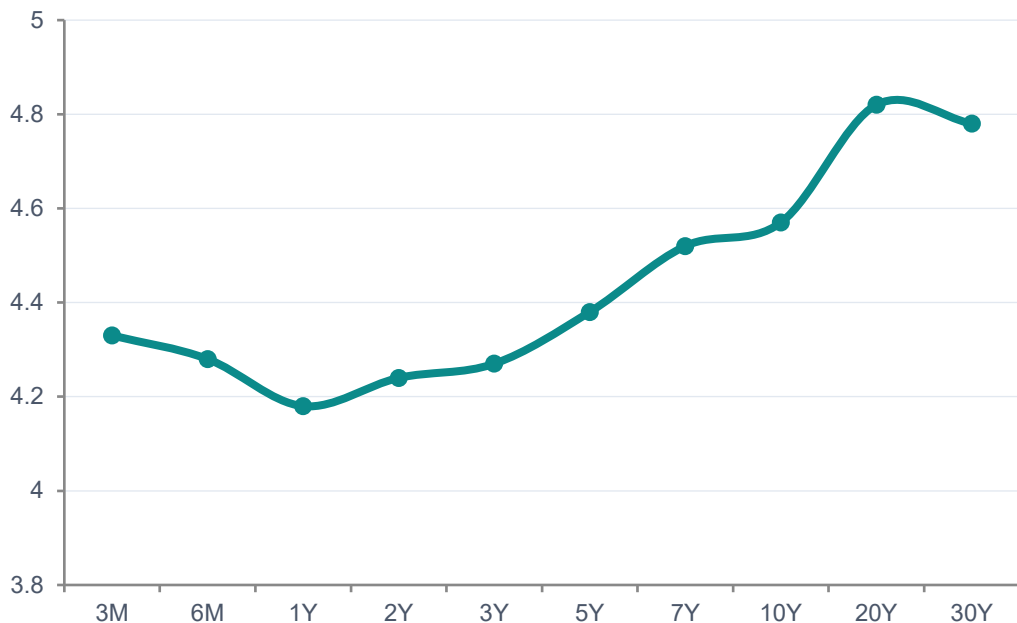


### Downgrades & Fallen Angels

A bond downgraded from IG to HY (a 'fallen angel') often loses 10-15% of its value as forced sellers exit. This is a real governance risk.

# The Treasury Yield Curve

As of December 31, 2025 — the foundation for all fixed income pricing.



## Key Concepts

### Duration

Measures sensitivity to rate changes. Longer duration = more price volatility.

### Spread

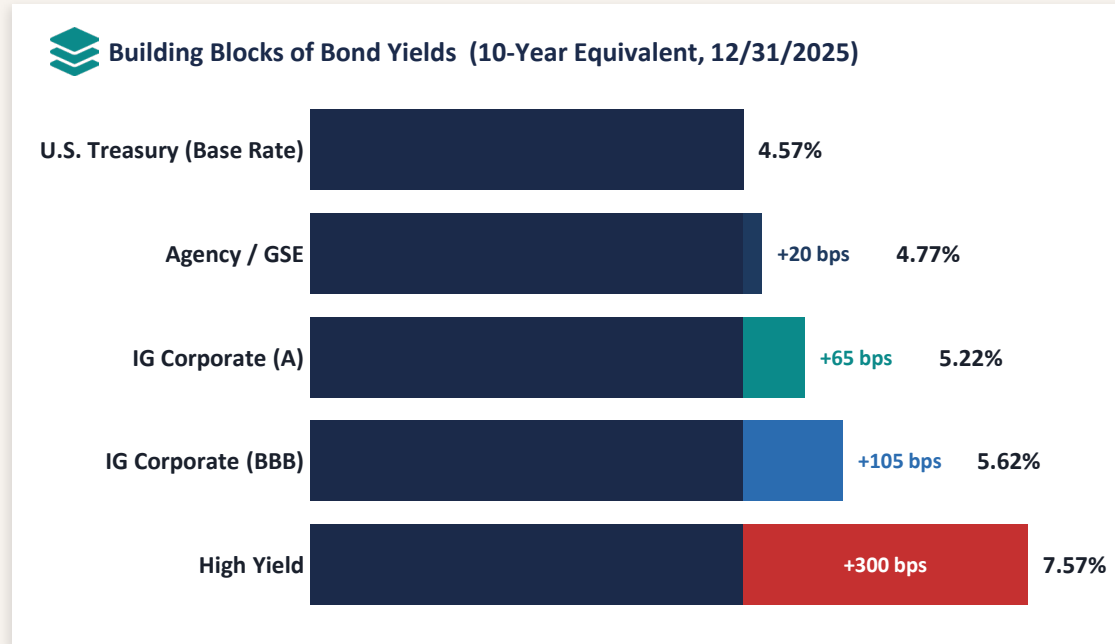
The yield premium over Treasuries. Compensation for credit & liquidity risk.

### Shape

Normal (upward), flat, or inverted. Signals market expectations about growth.

# How Bonds Are Priced: The Spread

Treasuries set the floor. Every other bond adds a "spread" — extra yield to compensate for additional risk.



Sources: U.S. Treasury, Bloomberg (approximate OAS as of 12/31/2025)

## What Drives Spreads?

- Credit quality** Lower rating = wider spread
- Liquidity** Harder to trade = wider spread
- Market sentiment** Fear widens, confidence tightens
- Supply & demand** More issuance can push spreads wider

## Board Takeaway

When spreads are **tight**, you're taking on credit risk without much reward.

*At 12/31/2025, IG corporate spreads sat near 15-year lows.*

1 basis point (bp) = 0.01%. 100 bps = 1.00%. So "+65 bps" means the bond yields 0.65% more than a Treasury of similar maturity.

# Fixed Income Risk Factors

*Five risks every board member should understand.*



## Interest Rate Risk

Bond prices fall when rates rise. Longer bonds are more sensitive. This is the dominant risk in most portfolios.



## Credit Risk

The borrower may not pay you back — or the market may worry they won't. Downgrades can hurt even without default.



## Liquidity Risk

Not all bonds trade easily. Smaller issues, lower-rated credits, and structured products may be hard to sell quickly.



## Reinvestment Risk

When bonds mature or get called, proceeds may be reinvested at lower yields. This quietly erodes portfolio income.



## Inflation Risk

If inflation outpaces your yield, your real return is negative. You're losing purchasing power while technically earning income.

# Income Drives Total Return

>90%

of bond total return  
has come from income

## Pull-to-Par

Bonds converge toward par as maturity approaches. Price declines from rising rates can self-correct — if you hold.

## Key Insight

Income is the quiet engine. Since inception of the Bloomberg Agg, over 90% of cumulative total return has come from coupon income — not price appreciation.

**Two Levers of Total Return: Interest Rates (duration) + Credit Spreads (sector allocation)**

Source: LPL Research, Bloomberg. Bloomberg U.S. Aggregate Bond Index since inception (1976). Past performance is not a guarantee of future results.

# Beyond Bonds — Risk Assets

*Higher potential return. Higher potential pain. Here's why that matters.*



## Public Equity

- S&P 500, Russell, International
- Long-term real growth engine
- Volatile — can lose 30%+ in a year

Most pools limit equity to 20-40% of surplus. Volatility demands a long horizon.



## High Yield & Loans

- Sub-investment grade bonds
- Bank loans (floating rate)
- Spread-driven returns

Spreads compensate for default risk. Bank loans pay floating rates — coupons reset with the market, reducing interest rate sensitivity.



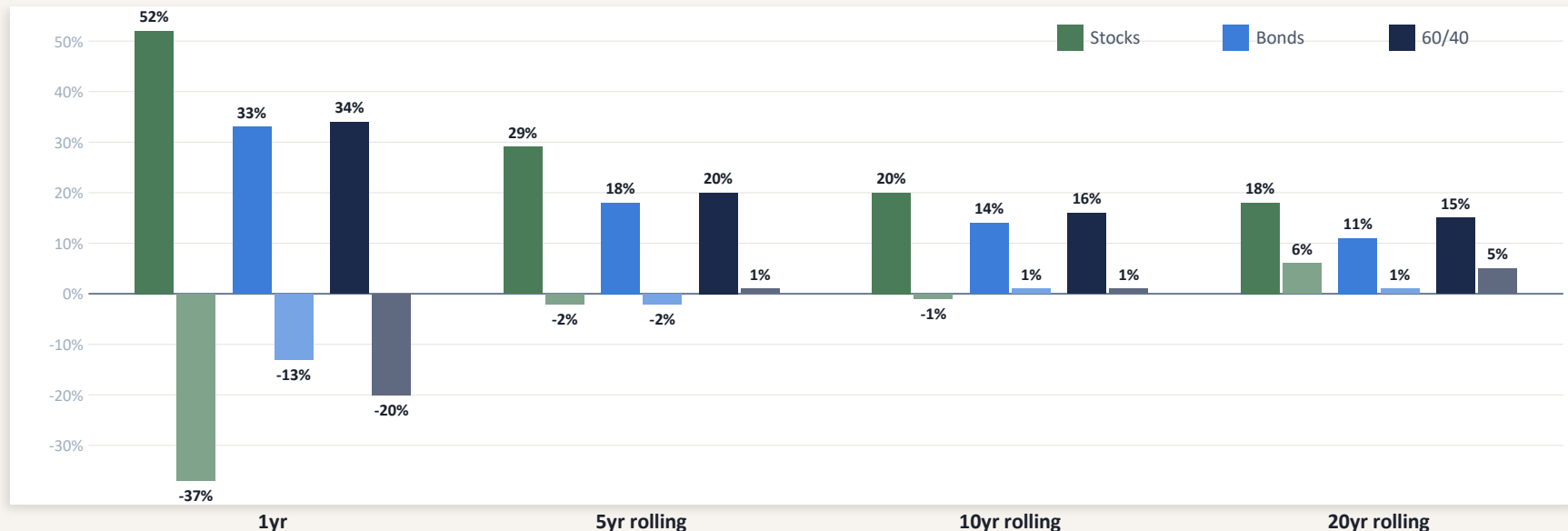
## Alternatives

- Private Equity / Venture
- Direct Lending / Infrastructure
- Real Assets / Commodities

Illiquidity premium possible, but complexity, fees, and lock-up periods add operational burden.

# Time, Diversification & The Volatility of Returns

Range of stock, bond & blended total returns — 1950–2025



	Avg. Annual Return	\$100K Over 20 Years
Stocks	11.7%	\$908,783
Bonds	5.2%	\$277,814
60/40 Portfolio	9.4%	\$606,792



## Time narrows the range.

Over any 20-year period since 1950, even the worst stock return was +6%. The worst 60/40 was +5%. Patience isn't a platitude — it's the data.

# Why Diversification Works

*Assets that don't move in lockstep reduce overall portfolio risk. That's the entire premise.*

## Correlation

Measures how closely two assets move together. Ranges from +1 (perfect lockstep) to -1 (perfect opposite).

**+1.0 → No diversification benefit**

**0.0 → Unrelated movements**

**-1.0 → Maximum offset**

You don't need negative correlation to benefit. Anything below +1.0 helps. Most asset class pairs fall between +0.2 and +0.7 — enough to matter.

## Why This Matters Today

Adding international equity to a U.S.-dominated portfolio works because U.S. and non-U.S. stocks don't move in perfect sync. Same logic applies to adding high yield or bank loans alongside investment-grade bonds.

### The Catch

Correlations rise in a crisis. In 2008 and March 2020, nearly everything fell together. Diversification reduces risk over time — it doesn't eliminate drawdowns. The slide you just saw (rolling returns) proves the time dimension matters.

### Board Takeaway

Diversification isn't about finding the magic asset. It's about combining assets with different return drivers so the portfolio doesn't live or die by one bet.

# How Bond Markets Actually Work

*Here's why that matters.*

## Equities

~5,000 U.S. stocks available

Exchange-traded (NYSE, NASDAQ)

Real-time pricing, live quotes

Average trade size: <\$10K

Anyone can buy 1 share

## Fixed Income

GE alone has 1,000+ bond issues

Over-the-counter (OTC) — no exchange

Phone/chat-based quotes, dealer market

Average trade size: \$500K+

Pro-rata allocation among accounts

# The Investment Performance Continuum

Where does your organization sit? Most insurers land somewhere in the middle.

## Book Yield / Income Only

Focus: stability of income  
Risk tolerance: low  
Measure: book yield

## Constrained Total Return

Focus: income + moderate growth  
Risk tolerance: moderate  
Measure: total return with guardrails

## Total Return

Focus: maximize risk-adjusted return  
Risk tolerance: higher  
Measure: benchmark-relative total return

◀ Conservative

Aggressive ▶

## Why does this matter?

In a rising-rate year (2022): **Book yield investors felt no pain. Total return investors lost 13%.**

Over 3 years (2022-2024): **Total return investors recovered and outperformed.**

# Capital Market Assumptions

*Every investment policy is built on a set of forward-looking return and risk estimates. Know where they come from.*

## What Are CMAs?

Projected returns, volatilities, and correlations for major asset classes over 10-15 year horizons. Produced annually by firms like J.P. Morgan, BlackRock, and others. They're the inputs that drive your strategic asset allocation.

## How They Feed Policy

Asset allocation targets in your IPS are calibrated to these projections. If a CMA says U.S. large cap will return 5.25% with 14% volatility, that shapes how much equity the policy allows — and what surplus growth you're banking on.

## The Accuracy Problem

CMAs are best guesses, not contracts. They're typically most accurate for middle-risk assets (IG bonds, balanced portfolios) and wildly off for extremes (gold, EM equity, commodities). That asymmetry matters.

## Board Takeaway

Ask your investment manager or consultant: "What assumptions is our current allocation based on? When were they last updated? And how far off have prior assumptions been?" If nobody can answer those questions, you're governing blind. We'll test this directly in this morning's second case study.

# The Governance Trap

*Why boards get stuck — and how to recognize it when it happens to yours.*

## Status Quo Bias

“We’ve always done it this way” is the most expensive sentence in governance. When an IPS goes unreviewed for years, the default isn’t neutrality — it’s drift. Markets move, liabilities shift, and an untouched policy quietly becomes a misfit.

## Anchoring & Recency

Boards anchor to whatever happened last. After 2022, “bonds are risky” became gospel. After a strong equity run, “why don’t we own more stocks?” Recent experience crowds out the base rate — and portfolios get repositioned at the wrong time.

## Analysis Paralysis

Faced with uncertainty, boards defer. “Let’s table this until next quarter” feels prudent but is itself a decision — to do nothing. In a changing environment, inaction has a cost. Every quarter of delay is a quarter of unrealized opportunity.

## Board Takeaway

These traps are universal — every board falls into them. The antidote isn’t smarter people; it’s better process. Scheduled policy reviews, decision logs, pre-commitment to action triggers, and explicit “what would change our mind?” questions at every meeting. Today’s case studies are designed to surface these dynamics in real time.

# Benchmarking

A benchmark is the yardstick. Without one, you can't distinguish skill from luck — or complacency from competence.



## What Is a Benchmark?

A market index that represents the opportunity cost of your investment strategy. It answers: 'How would we have done if we'd just bought the index?'



## Common Fixed Income Benchmarks

Bloomberg U.S. Aggregate (broad market), Bloomberg Intermediate Gov/Credit (most common for insurers), ICE BofA 1-5 Yr (short duration). Match the benchmark to your portfolio's duration and sector targets.



## How to Use Benchmarks

Compare total return vs. benchmark over rolling periods (1, 3, 5 years). Examine attribution: was outperformance from duration bets, sector allocation, or security selection? Persistent underperformance demands a conversation.

## Board Takeaway

Ask your manager: 'What benchmark are we measured against, and why?' If the answer is vague, that's a finding.

# Fees & Costs

Every basis point paid in fees is a basis point not earned. Know what you're paying and what you're getting.



## Management Fees

Typically 15-40 bps for fixed income, 40-100+ bps for equity/alternatives. Negotiate based on assets under management. Fees compound — 25 bps/year on \$100M is \$250K annually.



## Transaction Costs

Bid-ask spreads on bond trades (2-10 bps for IG, much wider for HY/munis). Unlike equities, there's no 'commission' — cost is embedded in the price. Ask for trade cost reporting.



## Custody & Administration

Custodian fees (2-5 bps) for safekeeping, settlement, and reporting. Performance measurement, compliance monitoring, and consulting fees add to the all-in cost. Total costs typically run 25-60 bps.



## Fee Governance

Request a full fee inventory annually. Compare fees to peers and industry benchmarks. For alternatives, scrutinize 'two and twenty' structures — management fee + performance fee + fund expenses can exceed 300 bps.

# Asset-Liability Management

The portfolio exists to pay claims. Every investment decision should start with the liability profile.



## Match Duration to Liabilities

If your average claim pays out in 3 years, your portfolio duration should be in that neighborhood. A mismatch means rate changes help one side and hurt the other.



## Cash Flow Matching

Structure bond maturities and cash flows to align with expected claim payments. This reduces forced selling and reinvestment risk. Laddered portfolios are the simplest approach.



## Surplus vs. Operating Assets

Operating reserves need short-duration, high-liquidity investments. Surplus (capital beyond requirements) can tolerate more duration and risk. Treat them as separate pools with separate mandates.



## The Dual Exposure Problem

Risk pools face a unique challenge: a catastrophic event hits both the claims side (more payouts) and potentially the portfolio side (market stress). Your ALM framework must account for this correlation.



## Segmented Approach

Many insurers use a 'bucket' strategy: Bucket 1 (liquidity, 0-1 yr), Bucket 2 (core, matching liabilities), Bucket 3 (surplus, longer-term growth). Each has its own risk/return target.

# Surplus Is Your Risk Budget

*Your surplus level determines how much investment risk you can responsibly take. Everything flows from this.*

## The Core Equation

Surplus = Assets minus Liabilities. It's the cushion that absorbs investment losses without threatening your ability to pay claims. More surplus means more capacity for duration extension, credit risk, or equity exposure. Less surplus means stay short and stay safe.

## Risk Pool Reality

Risk pools face dual exposure: a catastrophic event can spike claims and stress the portfolio simultaneously. A wildfire or hurricane doesn't just increase payouts — it can trigger broader market volatility. Your surplus must account for both sides of this correlation hitting at once.

## Surplus as Strategy

A well-funded pool has options: extend duration for higher income, add selective credit exposure, or allocate a portion of surplus to growth assets. An underfunded pool has none of those options — it needs liquidity and capital preservation above all else. Surplus isn't just a balance sheet line; it's the source of strategic flexibility.

## Board Takeaway

Before every asset allocation discussion, ask: "What is our current surplus ratio, and what does a 10-15% portfolio drawdown do to it?" If the answer makes you uncomfortable, your allocation is too aggressive for your financial position — regardless of what the policy permits.

# Regulatory & Statutory Context

The rules of the road — and the answer to 'why can't we just buy more stocks?'



## NAIC & Risk-Based Capital

The NAIC's RBC framework assigns capital charges by asset class. Treasuries: 0%. IG corporates: 0.3-1%. Common stock: 15%. Higher-risk assets consume capital that could otherwise support underwriting.



## Statutory Accounting (SAP)

Insurers report investments under SAP, not GAAP. Key difference: bonds held to maturity are carried at amortized cost (book value), not market value. This is why 'book yield' matters for income planning.



## State-Specific Limits

Most states impose asset class ceilings — e.g., no more than 20% in equities, limits on below-IG bonds, concentration limits per issuer. Your IPS must operate within these guardrails.



## Risk Pool Considerations

Public entity pools may face additional restrictions under state statutes governing public funds. Some states have approved investment lists. Know your specific legal authority before expanding asset classes.

# Where Are We Now

*A snapshot of the environment your investment decisions are operating in — as of early 2026.*

## Rates & Yields

The 10-year Treasury sits near 4.6%. IG corporate yields are in the 5-6% range — the most attractive entry point in over a decade for fixed income buyers. But reinvestment risk looms if rates fall.

## Credit Spreads

IG corporate spreads near 15-year lows. You're taking on credit risk without much extra compensation. High yield spreads are similarly compressed. Translation: the market is pricing in very little stress.

## Global Uncertainty

Tariff escalation, geoeconomic fragmentation, and climate-related claims are all rising. The WEF's 2026 Global Risks Report flags state-based conflict and extreme weather as top short-term risks — both of which hit insurer balance sheets directly.

## What This Means for You

Yields are attractive, but spreads don't reflect much risk. Global uncertainty is elevated. Your assumptions were built in a different environment. This is the backdrop for every case and exercise today — and for every investment committee meeting you'll attend this year.

# Putting It Together

## Strategic Asset Allocation — Matching Your Portfolio to Your Enterprise



### **Start with your business risk**

Lower business risk = capacity for more investment risk. Higher business risk = stay conservative.



### **Income is the cornerstone**

Investment income fuels competitive pricing and surplus growth. Protect this engine.



### **Diversify thoughtfully**

Spread across sectors, durations, and (where appropriate) asset classes. Concentration kills.



### **Match your time horizon**

Surplus invested long-term can tolerate volatility. Operating funds need stability.



### **Measure what matters**

Book yield for income stability. Total return for true performance. Know which lens you're using.

*The goal: an investment strategy that complements — not compounds — your enterprise risk.*

# The Investment Policy Statement

The IPS is the single most important governance document for your investment program. If you don't have one — or haven't reviewed it recently — that's problem #1.



## What It Is

A written document adopted by the board that establishes the objectives, constraints, and guidelines for managing the investment portfolio. It's your investment constitution.



## What It Should Contain

Return objectives, risk tolerance, time horizon, liquidity needs, permissible asset classes and sectors, credit quality minimums, duration limits, concentration limits, benchmark(s), and reporting requirements.



## Why It Matters

The IPS creates accountability. It prevents ad hoc decisions, protects the board from hindsight bias, and gives the investment manager clear guardrails. But a well-written policy isn't self-executing — the board must monitor whether the manager is actually utilizing the tools the policy provides. Without it, you're governing by opinion.



## Living Document

Review the IPS at least annually. Update it when your financial position changes, when market conditions shift materially, or when the board's risk tolerance evolves. Document every revision and the rationale.

# Fiduciary Duty & Standard of Care

You don't need to be an investment expert. But you are legally obligated to act like a responsible one.



## Prudent Person Standard

You must manage investment assets with the care, skill, and diligence that a prudent person in a similar position would use. The standard isn't perfection — it's process. Can you demonstrate that decisions were informed, deliberate, and documented?



## Duty of Loyalty

Investment decisions must serve the members and the organization — not personal interests, political agendas, or relationships. This includes conflicts of interest with service providers. If a board member has a material relationship with a manager or broker, it must be disclosed and managed.



## Duty of Care

You must stay informed. This means reading reports, asking questions, attending meetings, and understanding what your investment manager is doing with the portfolio. "I trusted the advisor" is not a legal defense. Delegation is permitted; abdication is not.



## The Stakes

A breach of fiduciary duty can expose the organization — and individual board members — to personal liability. An IPS that hasn't been reviewed in years, an allocation that no longer matches liabilities, or a manager that hasn't been formally evaluated: each is a governance gap with real legal exposure.

# Roles & Responsibilities

Everyone has a job. Clarity here prevents gaps, overlap, and finger-pointing when things go sideways.



## Board / Trustees

Set investment policy (IPS). Approve asset allocation. Hire/fire managers and consultants. Monitor performance. Exercise fiduciary oversight. You don't pick bonds — you set the framework.



## Staff / Management

Implement board-approved policy. Coordinate with investment manager and custodian. Prepare board reporting. Flag policy exceptions. Manage day-to-day cash needs. First line of operational oversight.



## Investment Manager

Execute investment strategy within IPS guidelines. Make security selection and timing decisions. Report performance vs. benchmark. Provide market commentary and strategic recommendations. Accountable for results.



## Custodian & Consultants

Custodian: Holds assets, settles trades, provides independent valuation and reporting. Consultant: Provides independent performance measurement, asset allocation advice, manager search and evaluation.

# Questions & Discussion

---

Insurer Investment Forum | March 24, 2026

