Brainstorm questions

- What are the risks?
- What is critical?
- What can we do?
- What can go wrong?
- What do we expect?

Fear is the risk

- Cease future profits and capital loss
  - Increasing surrenders from our interest sensitive portfolios.
  - Lower than expected sales activity, Low agent retention rate.
  - May need to sell assets and realize capital losses.
- Uncertainty around insurer solvency
  - Policyholders will react rapidly to fears about the ability of the insurer to meet all its obligations.
  - Quickly become a vicious cycle in which surrenders in each successive block of business puts additional downward pressure on liquidity and capital levels.
- Peer Companies' offers
  - Performance relative to the peer companies.
  - High yield products from other financial institutions.

Liquidity is the most critical

- Pressure on liquidity resources
  - Need to cover incremental cash demands from policyholders due to the substantial increase in surrenders.
  - The risk of a potentially overwhelming "run on the bank".
- Fragile capital position
  - Decline in statutory surplus due to higher realized capital losses as assets are sold at losses to meet higher surrenders.
  - May also suffer from higher credit defaults and impairments due to the poor economy, losses on equity investments.
  - Mass withdrawals if the perceived solvency of the industry came into question due to the reporting of large unrealized investment losses.

Risk mitigation

- Use interest rate derivatives
  - Boost portfolio yields and associated policyholder crediting rates.
  - Reduce capital loss and offset unrealized losses.
- Changes to the investment strategy
  - Buying shorter maturity assets as the yield curve flattens or inverts.
  - Increasing the allocation to cash and short-term assets.
- Retain policyholders
  - Subsidize the crediting rates to be within 1-2% of new money rates.
  - Ease the liquidity risk.
- Introduce new money rate product
  - Provides competitive product to sustain sales and agency field force.
  - May accelerates surrenders for existing portfolio rate products.
- Asset–intensive Reinsurance

Communication is more important

- Agents and Brokers
  - Provide training for our Agents so that they will be able to deliver a strong message to our policyholders.
  - The messages should be consistent for both institutional and retail clients but tailored to address their specific needs and concerns.
- Core Messages
  - Financial strength, demonstrated by remaining AAA-rating and strong surplus position as interest rates peak.
  - Stability, long history of being a best rating insurance company.
  - We could offer subsidized crediting rate.
  - We may offer new money rate versions of our life products.

Surrender assumption may be wrong

- Surrenders modeled as function of interest rates
  - Lack of dynamic lapse historical data.
  - Other factors, such as unemployment rate.
  - Different product features, including NLG, variable accounts.
- Lapses reflect behavioral assumptions
  - Policyholder decision-making may not be fully economic.
  - Unable to get the same life insurance due to the deteriorated mortality.
- "Fear factor' lapses due to public perception of strength
  - Potential of industry-wide contagion effect.
  - Downgraded by the rating agencies.

Risk is opportunity

- Interest Rates increase gradually
  - Portfolio rates gradually catching up with new money rates.
  - In-force products move out of spread compassion.
- Interest Rates don't spike high enough
  - Interest rate derivatives expire worthlessly.
- We can never fully eliminate risks
  - We can be prepared to respond dynamically to spike interest rates.
  - We can use multiple strategies to mitigate the risk.
  - We can increase the resilience of capital position to a spike in interest rates.
  - We can maintain financial strength and retain in-force businesses.