During the past quarter central banks (finally!) pivoted towards rate cuts, French OATs won the spread Olympics, and life insurers dealt with shifting investor behaviour towards policy guarantees and target maturity products.
Below is DWS selection of the top themes to consider this quarter:

Upcoming insurance events and key dates

- **December 2024: full implementation of Solvency UK reform**. After the reform of Matching Adjustment (in June 2024), streamlined rules on internal model capital calculations, as well as on reporting and disclosure requirements will likely be in focus;
- **October 2024 – February 2025**: **EIOPA consultations on technical standards after Solvency II Review.** The topics include, among others, liquidity risk management and best estimate valuations of life liabilities;
- **11-12 February 2025: DB/DWS Insurance CIO roundtable.** The second edition of the CIO roundtable will try and repeat the success of this year's inaugural event, that saw the participation of 22 Continental insurer CIOs, representing €3tn in assets under management. Reinsurance/P&C/life topics will be at the forefront, in a highly interactive, panel-focused setting.

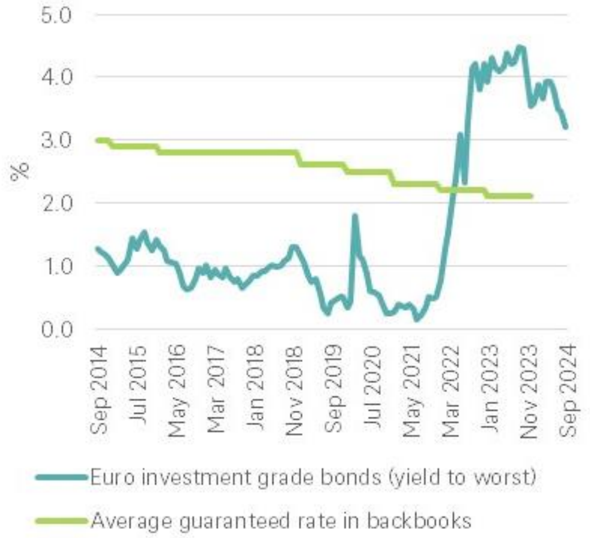
Insurance market and product trends

The quarter saw a continued interest in yield-oriented saving products, while the non-life segment continued to register healthy premia increases. Heightened M&A activity characterized the summer, and more may be in the pipeline…

Product design innovations and underwriting trends:

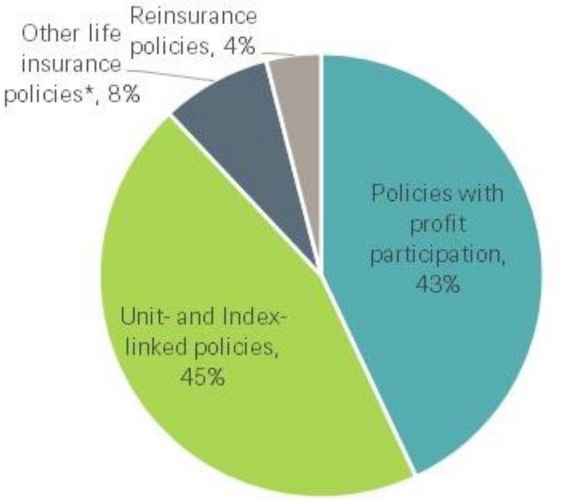
Life "with profit" vs product innovation: The high interest rate environment has given life businesses a (pun intended) new lease of life, boosting return on investments for saving products. Morgan Stanley's chart below speaks more than a thousand words: Euro IG (European lifers core fixed income allocation) yields sit comfortably above the 2.1% European average guarantee rate. Underwriting appetite for protection, though, gave way to a hunger for yield, translating in robust growth of unit-linked (e.g. target maturity funds) and index-linked products. According to Milliman's latest SFCR analysis capital-light products currently represent 45% of European lifers technical provisions, surpassing the 43% of with profit products, and this gap has most likely widened in the past few months. Some insurers played defence by blending different with-profit vintages. The result was the emergence of new products, often times mixing old 2% with profit policies (mostly invested in high quality government and corporate bonds) with newer (riskier) policies targeting a 4% (or higher) yield.

A new lease of life for with profit life policies?



Source: Morgan Stanley, as of December 2023, Bloomberg, as of September 2024

…or are capital-light products taking over?



Source: Milliman, as of September 2024, based on end-2023 SFCR data of European life insurers (ex "Health similar to life techniques" business)

Non-life hardening cycle and service inflationary vulnerabilities: global inflation pressures have driven premium rates higher (+3.9% in 2023, vs +0.8% in 2022), as insurers seek to offset rising claims costs, especially in property and motor lines. Sigma and Swiss Re expect hard market conditions to continue this year but to ease heading into 2025 as claims inflation softens. The persistence of services inflation could continue to impact casualty lines like motor and general liability, with still-high wage and healthcare costs in advanced economies feeding into persistent claims inflation.

Alternatives democratization: during the last few months Generali (in France) and Zurich (in Germany) partnered with alternative asset managers to launch European Long-Term Investment Funds (ELTIFs), targeting high net worth individuals. Appetite for UK's Long-Term-Asset-Fund (LTAF) is also growing among both insurers and pension funds. LTAFs are seen as an effective tool to diversify policy holder investments and access long-term assets that would otherwise not be permissible under UK authorized retail fund structures.

Insurance M&A activity: "movers and shakers" in Q3 2024:

Unicredit to acquire CNP/Allianz stakes in Italian life JVs: Unicredit announced they will exercise their purchase rights with regard to the stakes in CNP Unicredit Vita and in Unicredit Allianz Vita that the company does not already own. In 2023, the two JVs generated gross written premia of €7.5bn, and their technical reserves amounted to €44.9bn. By internalizing the business, Unicredit intend to take full control of the bancassurance supply chain, and of the profitable commission business linked to it.

Phoenix Group and Schroders to launch new private markets investment manager: Schroders partnered with UK savings and retirement firm Phoenix to launch a private markets investment manager: Future Growth Capital (FGC). FGC will channel as much as £23.7bn of pension savings into the asset class. The firm will invest in UK as well as global private markets, as it seeks to support the objectives of UK's "Mansion House Compact" initiative.

AXA entered into exclusive negotiations with BNP Paribas for the sale of its investment unit: the combined entity will oversee assets worth €1,500bn, with €850bn managed in long-term assets on behalf of insurers as well as pension funds. The deal includes a long-term partnership agreement which will allow BNP to manage a large part of AXA's assets. The agreed price for the acquisition and the set-up of the partnership is of €5.1bn, and the transaction is expected to close in mid-2025.

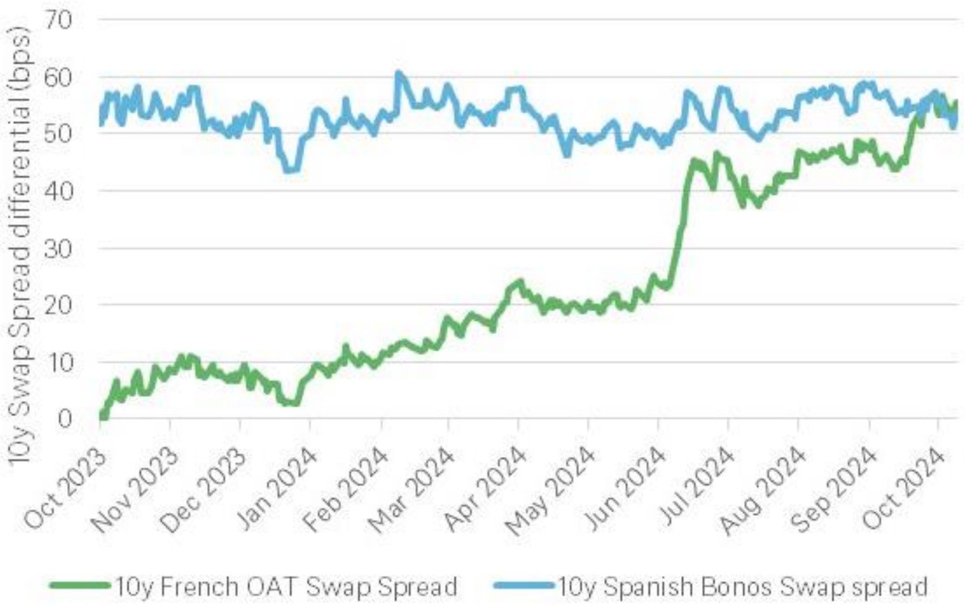
Market Pulse: investment strategies and trading ideas

Following the start central banks rate cutting cycles, Q3 was characterized by unexpected sovereign bond volatility, investment grade credit resilience and the continued growth in bond ETFs flows. We see curve steepeners and long-duration Euro investment grade credit as interesting pockets of opportunities in the months ahead.

Q3 Investment strategies:

French OATs won the summer spread Olympics: following snap elections and concerns around the French fiscal deficit levels, OATs have become increasingly popular among insurers, especially lifers. Spanish 10-year Bonos, on the other side, started trading inside the OAT-swap spread, on the back of more favourable GDP growth dynamics.

Paris Spread Olympics



Source: Bloomberg, as of October 2024

US and UK Inflation-linked bond premia: the gap between nominal and real yields in the US TIPS and UK Linkers markets provided a good (albeit temporary) entry point for insurers wishing to hedge (mostly long-dated) inflation-sensitive liabilities. SPIRE repack notes were used by Continental insurers to harvest extra yield and lock EUR-hedged cash flows for the duration of the bond tenors.

Investment Grade technicals have become increasingly supportive: as the rate-cutting cycle is in full swing, insurers reached for duration in the corporate bond market. Demand from target maturity funds and other yield-oriented bank/insurance strategies provided a strong tailwind and a cushion against spread volatility. Fundamentals in the asset class remain relatively healthy.

Far East trade winds: thanks to diverging monetary policies, Euro-hedged Japanese and Australian bonds have become increasingly attractive from a relative valuation standpoint, whilst also providing a diversifying effect to most insurance allocations.

Bond ETFs and liquidity: In a recent research piece, Oliver Wyman highlighted how bond markets are becoming increasingly automated, enabling specialist slides of risk or blends to be packaged into cheaper bond ETFs (according to SSGA, the average fee of bond ETFs is markedly lower than that of bond mutual funds, pricing at 0.29% vs 0.63%, respectively). This observation seems to be validated by Morningstar data, showing how the share of US bond funds managed in ETF format has surged from 21% to 28% since the Fed started raising rates. As a result, ETFs are increasingly becoming the primary source of bond liquidity in the US, although European insurers may be slower in their adoption, due to IFRS and other mark-to-market sensitive dynamics.

Q4 Trading Ideas... and key risks:

Core Sovereign Rates steepener: as the cutting cycle is forecast to continue, we expect rate curves to normalize, and therefore have a curve steepening bias. A number of insurers have increased their interest rate exposure over the summer which has translated in a strong bid for duration, although we note how recent volatility in rate cut expectations can be a key risk.

Monetary Policy Expectations

Institution	Current policy rate	Expectation Q3 2025	Comment
Fed	4.75-5.00	**3.75-4.00**	We expect further rate cuts on the back of weakening labor markets and solid inflation figures. We raise our expectations to four rate cuts until end of forecast horizon.
ECB	3.50*	**2.50**	We expect further cuts at each projection meeting. Four in total until Sep'25.
BoE	5.00	**3.75**	Despite the risk of persistent inflation, we have seen the first rate cut in August 2024 and expect five more cuts within 12 months.
BoJ	0.25	**0.75**	Despite the rate hike in July, the stance and the communication of BoJ remains opaque. We expect two more hikes until Sep '25.

Forecasts are based on assumptions, estimates, views and hypothetical models or analyses, which might prove inaccurate or incorrect. Past performance is not a guarantee of future results Source: DWS as of October 2024

Long duration Euro investment grade (IG) credit: a steepening curve should reduce the lure of cash and push money market flows and liquidity into longer durations. Current Euro IG technicals are quite supportive, both on the demand (positive flows) and on the supply sides (primary issues were well oversubscribed in past months). Euro IG spreads relative valuations are also attractive vs US IG spreads, due to the slightly higher rating / slightly shorter duration profile;

Mid-duration performs best after normalization

* Return of respective ICE BofA US Treasury indices for each maturity bucket // Forecasts are based on assumptions, estimates, views and hypothetical models or analyses, which might prove inaccurate or incorrect. Past performance is not a guarantee of future results // Sources: Bloomberg Finance L.P.; DWS Investment GmbH; as of: September 2024

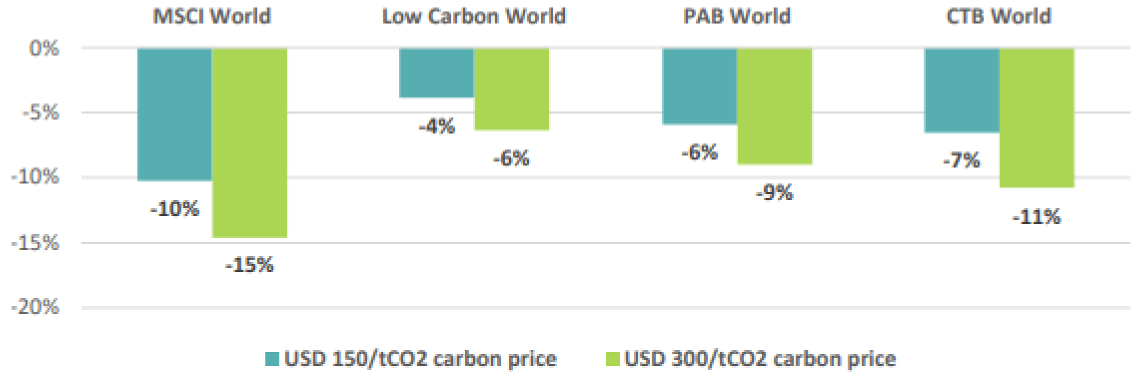
Euro High Yield (HY) caution: current EUR HY spreads have become quite tight given the high level of uncertainty about geopolitics and fundamentals for some sectors and issuers. The carry from the asset class is interesting for income-oriented insurers, although we are interested to see where the default rate heads, as that may have an effect on opportunistic investors vs capital preservation-focused players.

Key Risks:

- **Financial stability** can be impacted by inconsistent actions of the Fed, which might result in stress on the financial system;
- **Geo-political shocks** are still a risk, especially in the middle east. US elections will be front and center this quarter, as is the evolving situation in China;
- **Eurozone:** Potential risks to the macroeconomic outlook for the Eurozone include a delayed recovery in private consumption, weaker global demand, geopolitical tensions, and repercussions from the ongoing US-China trade war;
- **UK:** Revival of inflation dynamics would hurt the economy and the credibility of current monetary/fiscal policies;
- **US:** Growth momentum to weaken quicker than expected because of lagging effects from restrictive monetary policy. This could warrant further rate cuts when labor market weakens;
- **Emerging Markets:** Potential further U.S. measures to weaken global trade would harm in particular EM Asia. In Latin America, the main risks stem from domestic political events and changes.

ESG Developments

Estimated loss in equity market value under carbon price stress test scenarios



Forecasts are based on assumptions, estimates, views and hypothetical models or analyses, which might prove inaccurate or incorrect. Past performance is not a guarantee of future results. Source: DWS CROCI analysis as of September 2024

- **Stress Testing equity markets with higher carbon prices**: the DWS insurance advisory and the CROCI teams published a new study measuring the potential impact of climate transition stress tests on equity valuations. The findings suggest that the MSCI Europe index valuations could be hit by an 18% decline, compared to 8-10% for other ESG-aware European stock indices. The report is available at the following link.
- **Sustainability-linked misses**: Enel failed to reach a sustainability KPI. As a result, some of the company's sustainability-linked bonds experienced a 25bps coupon step-up**.** While the event is by no means positive for ENEL, it adds to the credibility of the company's targets, and can be seen as an important step in signaling a maturing ESG market.

If you are interested in any of the topics and would like to learn more, please reach out to me or your DWS relationship management partner.

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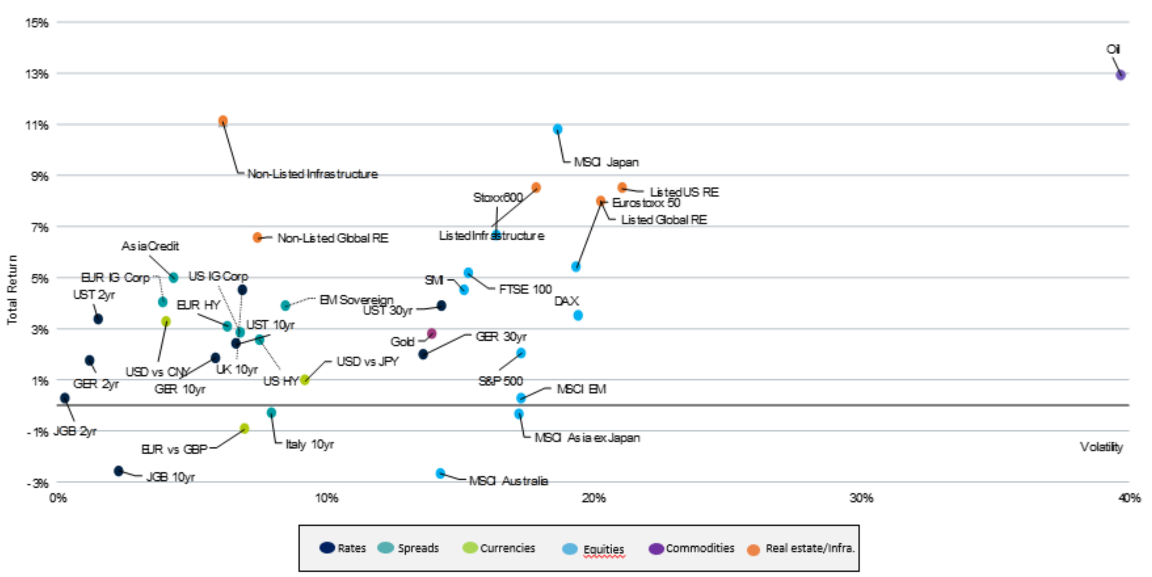
Appendix: DWS Market Outlook

Forecasts are based on assumptions, estimates, views and hypothetical models or analyses, which might prove inaccurate or incorrect. All data, outlook and perspective indicated below as of October 2024.

Risk[1]-return scatterplot



[1]Expected volatility is determined based on historical 10-year weekly returns data. Exponentially weighted moving average (EWMA) model with a 5-years half-life is used. Alternative investment may be speculative and involve significant risks including illiquidity, heightened potential for loss and lack of transparency. Forecasts are not a reliable indicator of future returns. Forecasts are based on assumptions, estimates, opinions and hypothetical models or analysis which may prove to be incorrect. No assurance can be given that any forecast or target will be achieved. DWS expectations/forecasts as of September 5, 2024. LC is local currency. Source: Bloomberg Finance L.P., DWS Investment GmbH as of September 30, 2024

Expected asset-class returns

	Current level Sep 30, 2024*	Strategic Forecast Sep 2025	Expected Total Return
Capital market yields (sovereign bonds)			
United States (2-year)	3.64%	3.60%	3.37%
United States (10-year)	3.78%	4.05%	2.40%
United States (30-year)	4.12%	4.15%	3.89%
Municipals**	69.54	75.00	2.42%
Securitized / MBS**	118 bps	120 bps	3.48%
Germany (2-year)	2.07%	2.00%	1.77%
Germany (10-year)	2.12%	2.25%	1.85%
Germany (30-year)	2.46%	2.50%	1.96%
Italy (10-year)	132 bps	180 bps	-0.31%
United Kingdom (10-year)	4.00%	4.00%	4.53%
Japan (2-year)	0.39%	0.70%	0.28%
Japan (10-year)	0.86%	1.40%	-2.57%
Currencies			
EUR vs USD	1.11	1.08	-4.40%
USD vs JPY	144	140	0.97%
EUR vs JPY	160	151	-3.48%
EUR vs Gbps	0.83	0.84	-0.92%
GBP vs USD	1.34	1.29	-3.12%
USD vs CNY	7.02	7.16	3.28%
Spreads (corporate & EM bonds) in bps***			
EUR IG Corp	116	95 bps	4.06%
EUR HY	348	400 bps	3.09%
US IG Corp	84	85 bps	2.84%
US HY	295	375 bps	2.56%
Asia Credit	132	125 bps	4.97%
EM Sovereign	361	390 bps	3.88%

	Current level Sep 30, 2024*	Strategic Forecast Sep 2025	Expected Total Return
Equity markets (index value in points)			
United States (S&P 500)	5,762	5,800	2.05%
Germany (DAX)****	19,325	20,000	3.49%
Eurozone (Eurostoxx50)	5,000	5,100	5.39%
Europe (Stoxx600)	523	540	6.67%
Japan (MSCI Japan)	1,622	1,760	10.78%
Switzerland (SMI)	12,169	12,350	4.49%
United Kingdom (FTSE 100)	8,237	8,350	5.17%
Emerging Markets (MSCI EM)	1,171	1,140	0.27%
Asia ex Japan (MSCI AC Asia ex Japan)	762	740	-0.33%
Australia (MSCI Australia)	1,656	1,550	-2.67%
Benchmark rates in percent			
United States (federal funds rate)***	4.75-5.00	3.75-4.00	-
Eurozone (deposit rate)	3.50	2.50	-
United Kingdom (repo rate)	5.00	3.75	-
Japan (policy rate)	0.25	0.75	-
Commodities in U.S. dollars			
Gold (Spot price)	2,635	2,810	
Gold (Future price)	2,733		2.81%
Crude Oil (Brent Spot price)	72	80	
Crude Oil (Brent Future price)	71		12.88%
Carbon	65	80	23.02%
Real Estate / Infrastructure			
Listed US RE			8.50%
Non-Listed US RE			6.00%
Listed Global RE			8.00%
Non-Listed Global RE			6.55%
Listed Infrastructure			8.50%
Non-Listed Infrastructure			11.10%

*current value is based on last trading data // ** Municipals: High yield OAS; Securitized/ MBS: FNMA 30y - 7y U.S. Treasuries; ***Federal funds rate // ****DAX is a Total Return Index, no dividend yield added // ***** yield spreads are quoted in terms of one yield versus that of U.S. Treasuries, except EUR IG and EUR HY which are quoted against Bunds // Alternative investment may be speculative and involve significant risks including illiquidity, heightened potential for loss and lack of transparency. Forecasts are not a reliable indicator of future returns. Forecasts are based on assumptions, estimates, opinions and hypothetical models or analysis which may prove to be incorrect. No assurance can be given that any forecast or target will be achieved. DWS expectations/forecasts as of September 5, 2024 // Source: Bloomberg Finance L.P., DWS Investment GmbH as of September 30, 2024

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