The NAIC Capital Markets Bureau monitors developments in the capital markets globally and analyzes their potential impact on the investment portfolios of U.S. insurance companies. Previously published NAIC Capital Markets Bureau Special Reports are available via its webpage and the NAIC archives (for reports published prior to 2016).

U.S. Insurance Industry's Cash and Invested Assets Continue to Grow Amid the Pandemic

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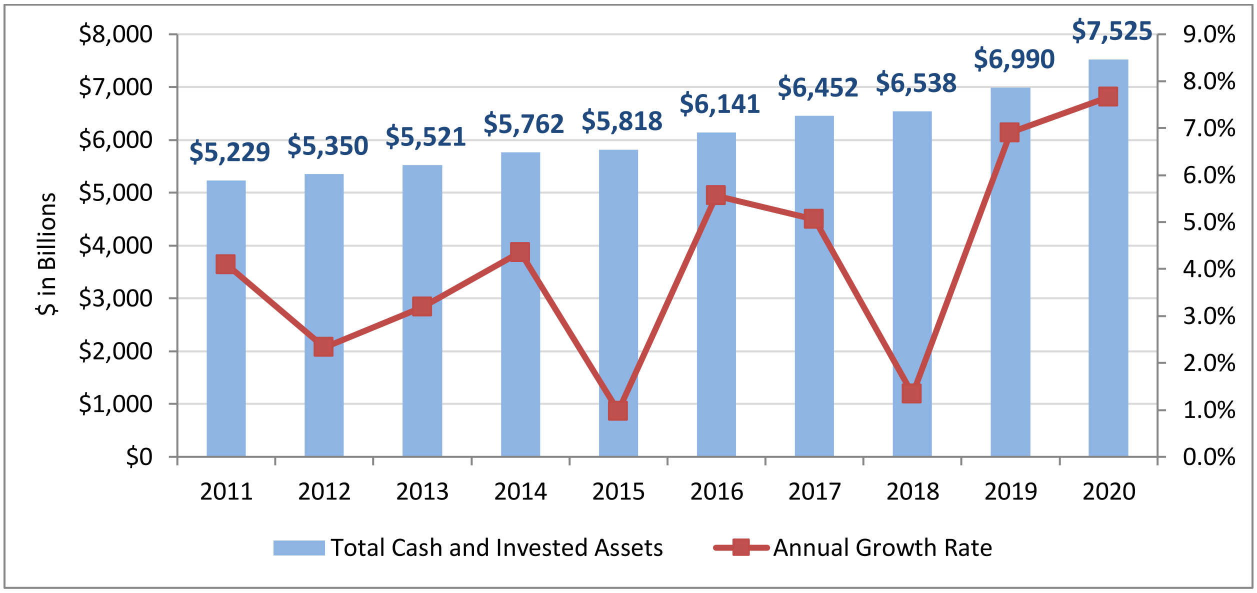
Executive Summary

- At year-end 2020, the U.S. insurance industry reported $7.5 trillion in total cash and invested assets, an increase of 7.7% compared to year-end 2019.
- The composition of the industry's assets was unchanged from prior years, with bonds and common stocks the largest and second largest asset classes, respectively. Mortgages and Schedule BA assets were the third and fourth largest categories, respectively.
- While exposure to less liquid assets (such as mortgages and Schedule BA assets) continued to increase as measured in absolute dollar terms, U.S. insurance companies enhanced their balance sheet liquidity, whereby cash and short-term investments increased 27% in 2020 in response to the uncertain operating environment resulting from the COVID-19 pandemic.
- The credit quality of the U.S. insurance industry's bond portfolio deteriorated as of year-end 2020, with bonds designated NAIC 1 and NAIC 2 declining one percentage point to 93.9% of total bond exposure and a small shift in exposure toward the lower end of the higher quality spectrum.
- Bond investment portfolios experienced credit quality deterioration following record levels of negative rating actions at nationally recognized statistical rating organizations (NRSROs) in 2020 following the impact of the COVID-19 pandemic on the credit markets.

At year-end 2020, U.S. insurance companies reported total cash and invested assets, including affiliated and unaffiliated investments, of $7.5 trillion, an increase of 7.7% compared to $7 trillion at year-end 2019. Chart 1 shows the industry's total cash and invested assets on a book/adjusted carrying value (BACV) basis from 2011 through 2020, along with annual year-over-year (YOY) growth rates. Cash and invested assets have grown steadily on an absolute dollar basis since 2011, with BACV increasing over 40% during the 10-year period. Despite the market stress and volatility resulting from the effects of controlling and mitigating the COVID-19 pandemic, the 7.7% YOY increase in cash and invested assets at year-end 2020 was the largest increase in the last 10 years and follows growth of 7% in 2019.

Chart 1: Historical U.S. Insurance Industry Total Cash and Invested Assets, Year-End 2011–2020



Note: Includes affiliated and unaffiliated investments.

Investment Portfolio Composition Remains Unchanged, but Balance Sheet Liquidity Is Enhanced

The U.S. insurance industry's composition of assets has been relatively stable over time. Bonds continue to be the largest component, representing 62.6% of total cash and invested assets at year-end 2020. Common stock investments are the second largest holding for the industry at 13.2% of total cash and invested assets, followed by mortgages at 8.3% and Schedule BA assets at 6.1%. (See Table 1.)

Table 1: Total U.S. Insurance Industry Cash and Invested Assets by Asset Class and Insurer Type, Year-End 2020 (BACV$ in Millions)

Asset Class	Life	P/C	Health	Title	Total	% of Total
Bonds	3,399,076	1,141,337	162,485	5,411	4,708,309	62.6%
Common Stock	194,670	748,602	46,681	3,135	993,087	13.2%
Mortgages	600,782	24,823	180	40	625,825	8.3%
Schedule BA and Other Assets	238,172	200,428	17,206	310	456,117	6.1%
Cash and Short-Term Investments	157,841	142,485	64,798	1,975	367,098	4.9%
Contract Loans	133,487	1	1	-	133,488	1.8%
Derivatives	121,698	577	1	-	122,276	1.6%
Real Estate	23,065	13,869	6,256	216	43,405	0.6%
Preferred Stock	15,499	16,632	670	373	33,175	0.4%
Securities Lending (Reinvested Collateral)	16,840	4,651	1,617	0	23,108	0.3%
Other Receivables	13,395	4,622	1,402	1	19,420	0.2%
Total	**4,914,524**	**2,298,027**	**301,297**	**11,461**	**7,525,308**	**100%**
% of Total	65.3%	30.5%	4.0%	0.2%	100%	

Note: Numbers in the table have been rounded.

Similar to previous years, life companies hold the largest share, or 65.3%, of the industry's total cash and invested assets in 2020, while property/casualty (P/C) companies account for 30.5%. Health and title companies together represent less than 5% of the industry's total cash and invested assets.

While the U.S. insurance industry's asset allocations do not typically change significantly from year to year, the share of bonds in the industry's portfolio at year-end 2020 declined to 62.6% from 63.8% at year-end 2019 as the low interest environment persists and insurers continue to be challenged with finding attractive yields in the fixed income market. (See Table 2.) Interestingly, cash and short-term investments increased to 4.9% of total cash and invested assets as of year-end 2020 from 4.1% as of year-end 2019. As the COVID-19 pandemic created uncertainty with respect to business prospects and the financial markets alike, insurance companies have enhanced their balance sheet liquidity with larger cash balances. U.S. insurers reported cash and short-term investments of $367 billion at year-end 2020, an increase of 27% compared to year-end 2019.

Table 2: Total U.S. Insurance Industry Cash and Invested Assets by Asset Class and Insurer Type, Year-End 2019 (BACV$ in Millions)

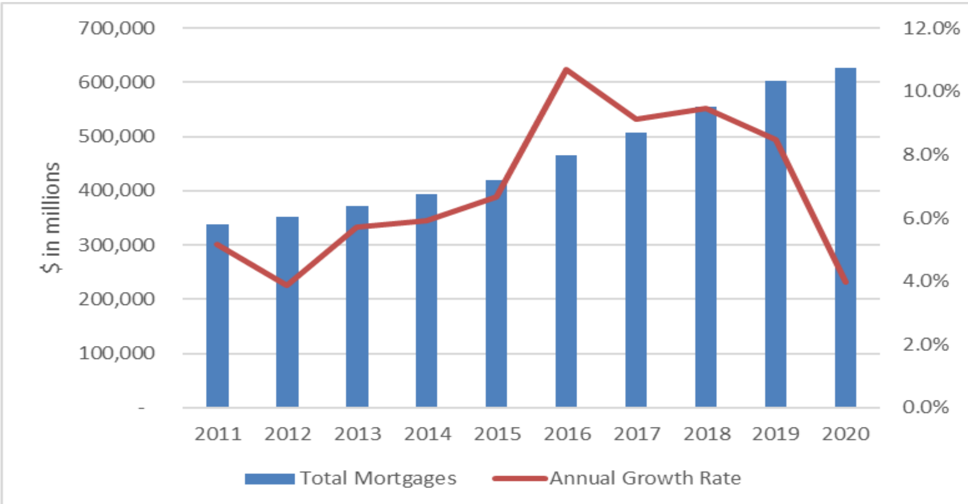
Asset Class	Life	P/C	Health	Title	Total	% of Total
Bonds	3,213,563	1,095,558	141,323	5,299	4,455,744	63.8%
Common Stock	179,092	702,843	41,339	2,735	926,009	13.3%
Mortgages	578,642	23,143	183	43	602,011	8.6%
Schedule BA and Other Assets	214,996	171,682	15,479	172	402,329	5.8%
Cash and Short-Term Investments	123,443	119,770	43,558	1,750	288,520	4.1%
Contract Loans	134,059	2	1	-	134,062	1.9%
Derivatives	79,672	340	-	-	80,012	1.1%
Real Estate	23,361	13,838	5,763	228	43,191	0.6%
Preferred Stock	13,701	14,386	605	412	29,103	0.4%
Securities Lending (Reinvested Collateral)	16,157	4,680	952	-	21,789	0.3%
Other Receivables	5,094	1,604	236	1	6,936	0.1%
Total	**4,581,779**	**2,147,849**	**249,438**	**10,640**	**6,989,706**	**100%**
% of Total	65.5%	30.7%	3.6%	0.2%	100%	

Note: Numbers in the table have been rounded.

U.S. insurance companies continue to seek more attractive and higher yields in relatively illiquid investments, such as mortgage loans, private equity and hedge funds (the former asset class is reported on Schedule A and the latter two on Schedule BA) in the prolonged low interest rate environment. Although these asset classes generally offer higher yields than public corporate bonds, they are typically less liquid and have less credit and pricing transparency. As such, they are subject to greater price volatility. While the share of Schedule BA assets in the industry's portfolio increased to 6.1% at year-end 2020 from 5.8% at year-end 2019, the share of mortgages declined to 8.3% from 8.6%. However, U.S. insurers' exposure as measured in terms of BACV to these two asset classes continues to increase, with mortgage exposure increasing 4% YOY to $626 billion and Schedule BA exposure increasing over 13% YOY to $456 billion.

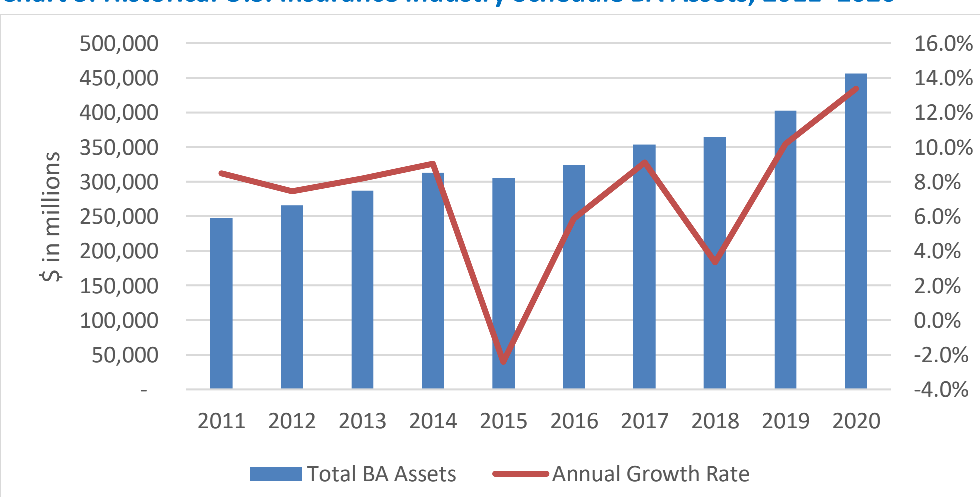
The pace of growth in mortgage exposure slowed in 2020 compared to YOY growth of more than 8% from 2016 to 2019. (See Chart 2.) Furthermore, 2020 marks the first year that the annual growth in mortgage loan exposure has not exceeded the annual growth of total cash and invested assets since the NAIC Capital Markets Bureau began tracking data in 2010.

Chart 2: Historical U.S. Insurance Industry Total Mortgages, 2011–2020



Growth in Schedule BA assets, including affiliated and unaffiliated, held by U.S. insurance companies accelerated to more than 13% at year-end 2020. (See Chart 3.) 2020 marks the second year in a row that Schedule BA assets grew more than 10% on a YOY basis. The annual growth in Schedule BA exposure has generally exceeded the annual growth of total cash and invested assets since 2011; the only exception during the time period analyzed was in 2015. Despite significant growth over the years, Schedule BA assets do not represent a significant, or core, investment for U.S. insurers, representing only 6% of total cash and invested assets. The largest asset classes reported on Schedule BA include private equity, hedge funds and real estate.

Chart 3: Historical U.S. Insurance Industry Schedule BA Assets, 2011–2020



COVID-19 Pandemic Leads to Credit Quality Deterioration in Industry's Bond Portfolio

The U.S. insurance industry's exposure to bonds increased 5.6% at year-end 2020 compared to year-end 2019, reaching $4.7 trillion. (See Table 3 and Table 4.) Corporate bonds and municipal bonds remained the two largest bond types for U.S. insurers, representing 56.2% and 10.9%, respectively, of total bond exposure. Asset-backed securities (ABS) and other structured securities, U.S. government bonds, and agency-backed residential mortgage-backed securities (RMBS) accounted for 9.7%, 6% and 5.8% of total bond exposure, respectively. The share of corporate bonds and ABS and other structured securities increased YOY, while the share of municipal bonds, U.S. government and agency-backed RMBS declined. Record levels of corporate bond issuance, both by investment grade and high-yield issuers, in 2020 likely contributed, in part, to the one percentage point YOY increase in U.S. insurers' corporate bond exposure, to 56.2% of total bonds.

Table 3: Bond Breakdown by Insurer Type, Year-End 2020 (BACV$ in Millions)

Bond Type	Life	P/C	Health	Title	Total	% of Total
Corporate Bonds	2,138,031	441,971	64,454	2,763	2,647,220	56.2%
Municipal Bonds	207,845	284,172	22,286	1,069	515,372	10.9%
ABS and Other Structured Securities	359,412	84,719	13,695	22	457,847	9.7%
U.S. Government	151,888	108,509	19,817	354	280,568	6.0%
Agency-Backed RMBS	151,383	96,052	23,840	663	271,938	5.8%
Private-Label CMBS	148,250	44,569	7,273	-	200,093	4.3%
Private-Label RMBS	75,594	16,530	2,011	1	94,135	2.0%
Agency-Backed CMBS	51,886	27,920	2,383	93	82,283	1.7%
Bank Loans	57,417	13,925	1,980	126	73,448	1.6%
Foreign Government	48,311	17,795	1,210	288	67,604	1.4%
Exchange-Traded Funds (ETFs)	5,773	4,301	3,325	20	13,419	0.3%
Hybrid Securities	2,127	71	0	-	2,198	0.1%
Bond Mutual Funds	326	284	210	3	823	0.0%
Total	**3,398,243**	**1,140,820**	**162,483**	**5,401**	**4,706,948**	**100%**
% of Total	72.2%	24.2%	3.5%	0.1%	100%	

Note: Numbers in the table have been rounded.

Within the bond portfolio, insurance companies looked to ABS and other structured securities and bank loans for additional yield. In addition to consumer ABS, ABS and other structured securities include collateralized loan obligations (CLOs), commercial ABS, lease-backed securities and other types of structured finance investments. In terms of BACV, exposure to ABS and other structured securities has increased double digits on a percentage basis in at least the last two years. Although exposure to bank loans and exchange-traded funds (ETFs) is minimal as a percent of total bonds, exposure in terms of BACV increased significantly—by 13% and 71%, respectively, in 2020 compared to 2019—and follows increases of 17% for each in the prior year. Following two years of significant growth, bond mutual fund exposure declined almost 8% to $823 million at year-end 2020.

Table 4: Bond Breakdown by Insurer Type, Year-End 2019 (BACV$ in Millions)

Bond Type	Life	P/C	Health	Title	Total	% of Total
Corporate Bonds	2,003,171	399,994	54,939	2,504	2,460,609	55.2%
Municipal Bonds	202,995	273,273	19,760	1,090	497,118	11.2%
ABS and Other Structured Securities	316,535	82,146	11,829	21	410,530	9.2%
Agency-Backed RMBS	172,018	100,438	22,243	749	295,448	6.6%
U.S. Government	147,211	117,641	17,747	368	282,966	6.3%
Private-Label CMBS	143,217	41,575	6,033	21	190,846	4.3%
Private-Label RMBS	74,951	18,261	1,581	1	94,794	2.1%
Agency-Backed CMBS	53,773	28,323	2,060	91	84,246	1.9%
Foreign Government	46,185	17,736	840	306	65,067	1.5%
Bank Loans	47,767	13,256	1,590	145	62,759	1.4%
Exchange-Traded Funds (ETFs)	3,187	2,493	2,174	3	7,858	0.2%
Hybrid Securities	2,507	100	0	-	2,607	0.1%
Bond Mutual Funds	47	322	524	-	893	0.0%
Total	**3,213,563**	**1,095,558**	**141,321**	**5,299**	**4,455,742**	**100%**
% of Total	72.1%	24.6%	3.2%	0.1%	100%	

Note: Numbers in the table have been rounded.

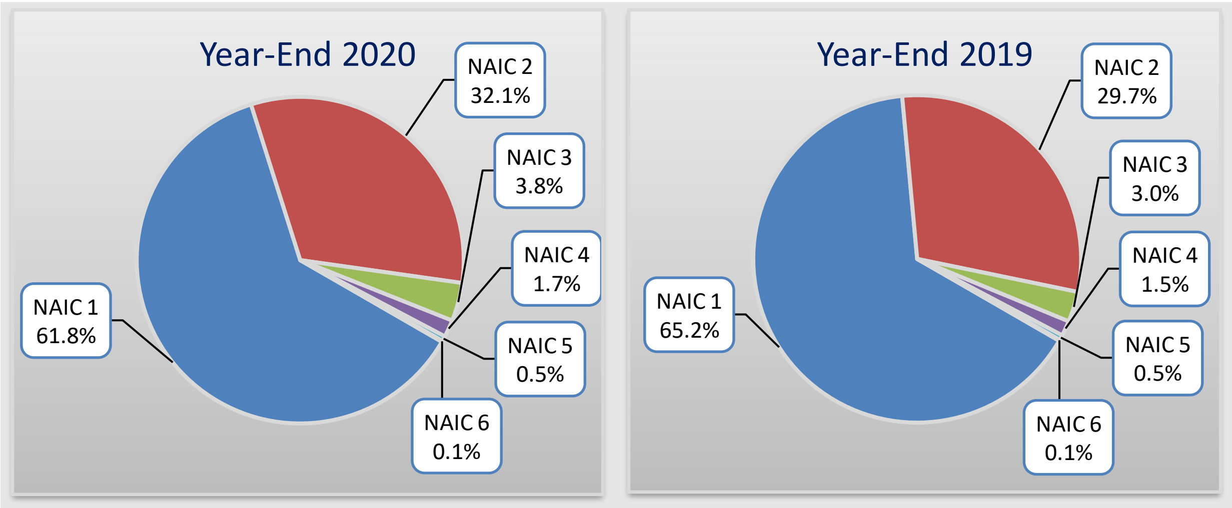
The beginning of the COVID-19 pandemic and oil price dislocation in April 2020 resulted in significant pressure on credit quality. This led to a record number of negative rating actions that reflected sudden and, in some cases, sustained declines in revenues amid deteriorating cash flows and rising leverage. In 2020, for example, S&P Global Ratings (S&P) took approximately 2,100 public rating actions on global corporate, financial and sovereign bonds where the COVID-19 pandemic, the oil price shock or both were cited as a factor, with more than 50% of the ratings actions resulting in downgrades. The majority, or 68%, of the rating actions affected high-yield issuers, which tend to have weaker liquidity and refinancing profiles. Almost 45% of S&P's corporate, financial and sovereign rated universe experienced a negative rating action, with approximately 23% of them downgraded.

In addition, in 2020, S&P lowered the ratings of more than 1,800 structured finance tranches in the U.S. due to the COVID-19 pandemic and/or the decline in oil and gas prices. The rating actions represent approximately 5% of the outstanding S&P-rated traches in the U.S. and Canada. RMBS and CLOs accounted for 37% and 27% of the structured finance rating actions.

In July 2020, the NAIC Capital Markets Bureau conducted a high-level analysis of ratings transitions to better understand the impact of the record level of rating downgrade activity on U.S. insurer investment portfolios. For more information on the analysis, please see the NAIC Capital Markets Special Report titled "U.S. Insurance Industry's High-Yield Bond Exposure at Year-End 2019 Remains at 5.1% of Total Bonds" published in August 2020.

While the U.S. insurance industry's corporate bond investment portfolio predominantly consists of high credit quality companies, which have greater financial flexibility to withstand the negative credit effects of macroeconomic shocks, credit quality deterioration was nevertheless evident in the year-end 2020 bond portfolio given the broad-based economic and credit impact of the COVID-19 pandemic. Investment grade bonds, or those with reported NAIC 1 or NAIC 2 designations, accounted for 93.9% of total bonds, declining from 94.9% at year-end 2019. (See Chart 4 and Chart 5.) Below-investment grade bonds, or those with reported NAIC 3 designations and below, increased from 5.1% of total bond exposure in 2019 to 6.1% in 2020—the highest level since the financial crisis, when it reached 6.3% at year-end 2009.

Chart 4 and Chart 5: Reported Credit Quality of U.S. Insurance Industry's Bond Portfolio at Year-End 2020 (Left) and Year-End 2019 (Right)



A shift toward the lower end of the investment grade, or higher quality, spectrum also occurred in 2020, whereby bonds with NAIC 2 designations increased to 32% of total bonds from 30% in 2019, while bonds with NAIC 1 designations decreased to 62% from 65%. In addition, on a YOY basis, NAIC 3-designated bonds increased to almost 4% of total bonds from 3%, reflecting the heightened level of "fallen angels," or issuers downgraded from investment grade to below investment grade, or high-yield, in 2020. While there was significant concern that a large amount of fallen angel debt could result in severe market dislocation, the number of fallen angels was below the peaks of prior years, including the financial crisis. In 2020, the market was able to absorb the additional high-yield debt with limited price volatility or illiquidity, due in part to central bank liquidity programs that provided support for recent fallen angel debt.

The NAIC Capital Markets Bureau will continue to monitor trends in the U.S. insurance industry's various invested asset types and report as deemed appropriate.

Questions and comments are always welcome. Please contact the Capital Markets Bureau at CapitalMarkets@naic.org.