

Brexit Implications for UK and Continental European Insurers

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Brexit's direct impact on the UK and Continental insurers in which we invest is expected to be modest near-term given diverse footprints across geographies and business lines. Subsidiaries tend to be locally based, operating independently throughout Europe, the UK and across the globe. For those passporting across borders, the renegotiation of contracts and relocating of offices could be costly, albeit reasonable within the context of earnings. In addition, any economic growth slowdown should be manageable from an operational perspective as existing policies often comprise a significant portion of earnings, and specific coverages (*e.g.*, property and liability) are considered essential for individuals and businesses. Furthermore, low inflation could mitigate future claims costs for a number of insurers.

Brexit's indirect impact is likely to be more meaningful given insurers' sensitivities to capital markets and interest rates. Under the new, more conservative, mark-to-market Solvency 2 (S2) regime in Europe, capital ratios may be more volatile as, *e.g.*, rates decline and credit spreads widen. **However, capital and liquidity remain key strengths for the insurers in which Spectrum invests.** UK insurers are expected to continue to comply with S2.

Life insurers are inherently more exposed to market forces than property & casualty (P&C) names given higher investment leverage. However, insurers also have the benefit of being long-term, buy and hold investors of mostly high quality investment grade fixed income securities. Falling interest rates are a headwind, though asset-liability management is generally sound ([see: Low Interest Rates Manageable for Insurance Cos.](#)). Of note, insurers are not forced sellers amidst market volatility and the industry weathered the Global Financial Crisis well, while balance sheet strength is generally more robust today. Insurers have also disclosed manageable capital ratio sensitivities to stress under S2, and hold substantial buffers to offset an uptick in impairments or capital needs.

The reinvestment headwind in the low rate environment is gradual, and unlikely to be a major operational challenge near term. However, as margins on traditional life & savings products decline, new business sold continues to shift towards more asset-light, fee-based and protection (P&C-like) products – reducing macro sensitivities. The major UK and Continental European insurers have been navigating the macro backdrop for decades, and they continue to do so today. **Spectrum's UK and Continental European Insurance investments maintain solid credit fundamentals supported by ongoing regulatory developments, healthy capital, strong diversity and robust risk management practices.**

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