# Insurance-related investments strategy

## Investment update to 30 September 2024

The insurance-related investments strategy, managed by MLC Asset Management's (MLCAMs) Alternative Strategies team, uses carefully selected reinsurance managers from around the world.

Insurance-related investments are investments in natural catastrophe risks. Investors take on a role akin to the role of an insurer. They receive a yield - effectively an insurance premium - for taking the risk of a particular natural catastrophe causing losses above a certain level. As the occurrence of natural catastrophes has no expected correlation with share market movements, the strategy is an attractive source of diversification. For example, during the global financial crisis, shares fell but insurance-related investments performed well.

MLC's diversified funds' target allocations to insurance-related investments are shown in Table 1.[1] The MLC Premium and Value Separately Managed Account (SMA) Model Portfolios also have an indirect allocation through their investments in the MLC Real Return funds.

**Table 1: MLC diversified funds with allocations to insurance-related investments as at 30 September 2024**

| Fund series | % of portfolio invested in insurance-related investments |
|---|---|
| MLC MultiActive Capital Stable | 3% |
| MLC MultiActive Conservative | 3% |
| MLC MultiActive Moderate | 3% |
| MLC MultiActive Balanced Growth | 2% |
| MLC MultiActive Growth | 1% |
| MLC MultiSeries 30 | 2% |
| MLC MultiSeries 50 | 2% |
| MLC MultiSeries 70 | 2% |
| MLC MultiSeries 90 | 2% |

| Fund series | % of portfolio invested in insurance-related investments |
|---|---|
| MLC Wholesale Horizon 2 Income Portfolio | 3% |
| MLC Wholesale Horizon 3 Conservative Growth Portfolio | 3% |
| MLC Wholesale Horizon 4 Balanced Portfolio | 2% |
| MLC Wholesale Horizon 5 Growth Portfolio | 1% |
| MLC Wholesale Inflation Plus Conservative Portfolio | 4% |
| MLC Real Return Moderate | 4% |
| MLC Real Return Assertive | 4% |

**Source:** MLC Asset Management Services Limited. The allocations shown in Table 1 are based on the fund's target allocations. The amounts allocated to insurance-related investments differ based on each fund's investment objective and strategy, risk profile and strategic asset allocation (SAA).

[1] This update is for MLC's diversified investment funds listed in Table 1. Refer to the 'Important Information' section of this report for details about the funds. MLC offers diversified funds in investments, superannuation and pension. While there may be similarities between MLC's diversified funds offered in investments, superannuation and pension, this update is focused on the investment funds listed in Table 1.

## Investment objective

The strategy seeks to provide our diversified funds with sources of risk and return that are not correlated to mainstream asset classes.

## Why invest in insurance-related investments?

While insurance-related investments have a long-term return and risk profile similar to other types of fixed income investments, insurance-related investments' returns can be distinctly different over short periods because the underlying assets generating the income are linked to the insurance market. As a result, insurance-related investments provide excellent diversification benefits to other types of fixed income, capable to reduce total portfolio risk and improve the risk-return efficiency of the portfolios.

Insurance-related investments are unusual because their returns are independent of the economic factors that influence the performance of most other investments. This makes them a rare and valuable source of fixed income returns that are also largely 'uncorrelated' with returns from shares.

Another distinctive feature of these investments is the visibility regarding its risk-return profile. Unlike other asset classes, where generally the expected returns are higher when risks are higher, in reinsurance the risks of a catastrophe occurring does not change materially from year to year, but the pricing can. This provides us with the ability to dial up and down our portfolio exposure according to the relative attractiveness of the pricing.

Certain risks can be rewarded with relatively better returns. An example of this is in Florida and California in the US. Both are densely populated cities where there are large economic exposures to major natural catastrophes via expensive real estate. Florida is exposed to hurricane risks and California is exposed to earthquake risks. It therefore makes sense for the reinsurance industry to reduce some of their exposure to these risks, particularly the very low probability, high impact events (which could jeopardise their solvency). This provides opportunities for investors to be rewarded for taking these 'remote peak peril' risks, while also benefiting from diversification from mainstream asset classes.

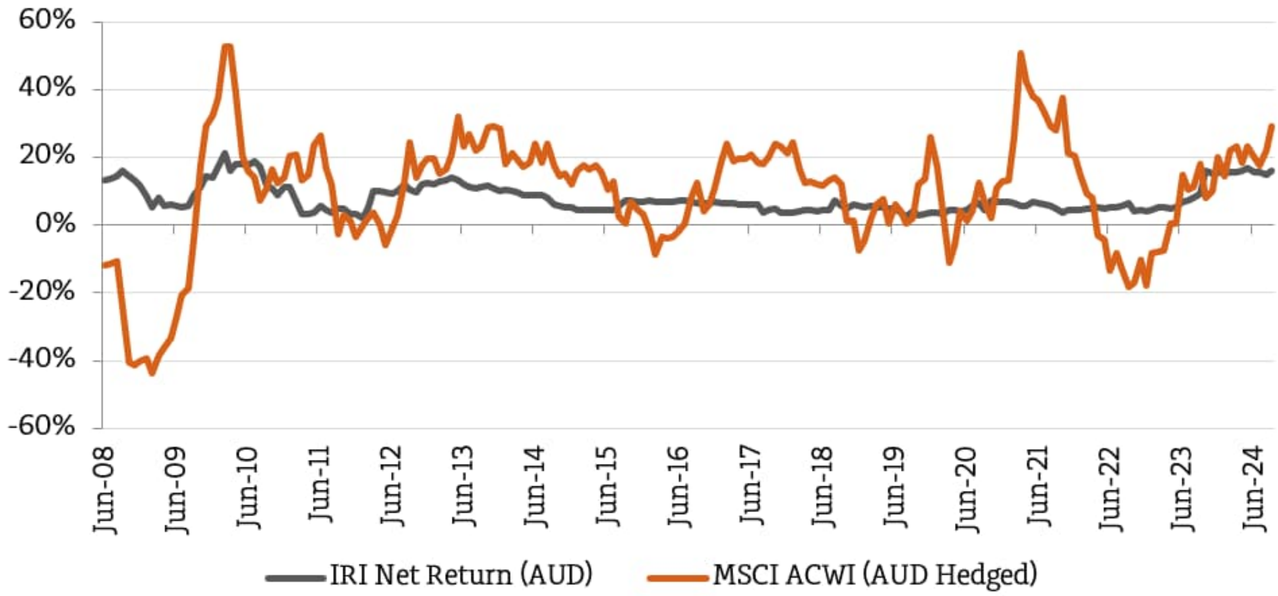
While there's no denying insurance-related investments aren't as well-known, or as liquid, as traditional asset classes such as equities and bonds, their ability to deliver relatively consistent returns irrespective of what's happening in listed markets is evident. This is highlighted in Chart 1 which shows the performance of the MLC insurance-related investments strategy since 2008. While past performance isn't reliably indicative of future performance, the strategy has produced a positive return each year and provided excellent diversification for investors from more volatile asset classes in the same period.

## Performance

The insurance-related investments strategy has worked well for our diversified funds, making an important contribution to real returns and helping to moderate risk, particularly in periods of share market volatility. The strategy has low correlation to shares and has delivered 8.2% pa (hedged into Australian dollars, net of indirect costs directly associated with the insurance-related investments and gross of all other fees and costs) from July 2007 to 30 September 2024.

### Chart 1: Performance of insurance-related investments relative to global shares to 30 September 2024

Rolling 12 month returns




**Source:** MLC Asset Management Services Limited. Insurance-related investment strategy returns are hedged into Australian dollars, net of indirect costs directly associated with insurance-related investments and are gross of all other fees and costs. Refer to Appendix 1 for more information. Past performance is not a reliable indicator of future performance.

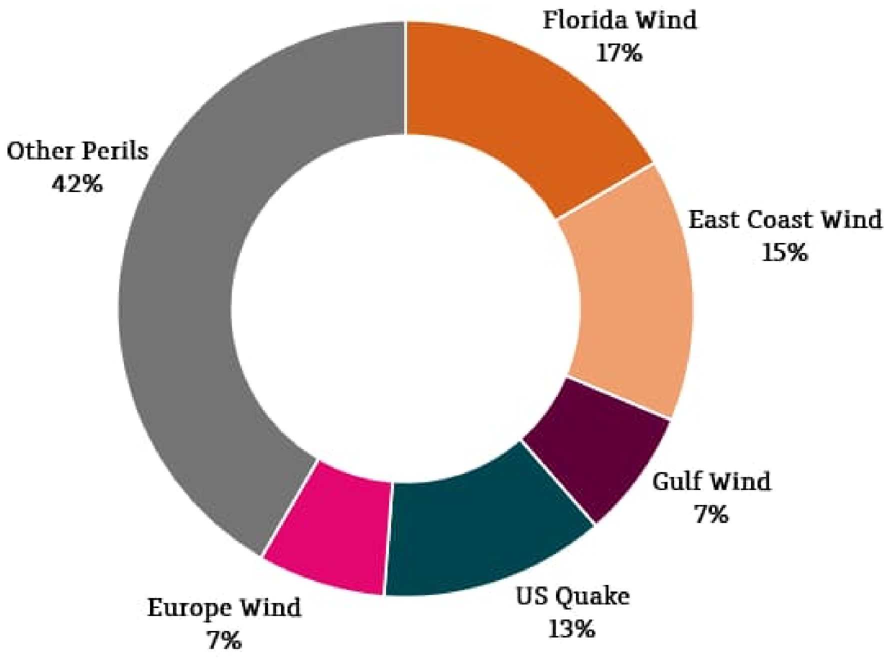
## How we manage insurance-related investments

We have appointed five investment managers with expertise in the management of natural catastrophe and weather-related reinsurance risk exposures.

Our insurance-related investments strategy consists of a combination of catastrophe bonds (~15%) as well as direct reinsurance. The direct reinsurance market is a much larger pool of exposures compared to the catastrophe bond market, which creates more opportunity. This is where investing through specialist reinsurance managers is most advantageous to our investors. These managers and their parent companies are extremely well positioned to source and sift attractive risks from insurance companies and analyse these risks accurately. One example of this is demonstrated in the research team of one of our managers, which consists of 30+ people, including seismologists and weather experts, whose job is to accurately assess the risk of loss from various events.

## Risk exposure

Chart 2: Expected risk by catastrophe type (at 30 September 2024)




Source: MLC Asset Management Services Limited. Figures have been rounded to the nearest percent. Other perils include, but are not limited to, Japan Wind and Quake, Europe Quake, US Wildfire, Mid Atlantic Wind and Caribbean Wind.

## Current strategy positioning

*Returns are net of indirect costs directly associated with insurance-related investments, and gross of all other fees and costs.*

The insurance-related investments strategy produced a return of 4.8% for the quarter and 16.0% return for the 12 months to September 2024. The primary drivers of the positive return for the quarter were premium earnings on private reinsurance contracts and income received on catastrophe bonds.

The quarter began with the strategy completing the larger mid-year June and July renewals which were focused on US regional exposures. Catastrophe risk pricing remained attractive through the mid-year renewal (May 1 – July 1) even though, according to mid-year broker reports, market-wide risk-adjusted premiums decreased by 5-10% from the historically high level of 2023.

Hurricane season begun in the September quarter and came into form with the major storms being Beryl, Debby, Helene and the recent Milton. The strategy so far appears to have experienced only small losses from these events due to our focus on more remote risks. This means premium income has more than offset these incremental losses in Q3 (and at the time of writing the same was true in mid-October post Hurricane Milton), helping produce a strong return for the quarter. Typhoons Gaemi and Shanshan across the coasts of China and Japan respectively are the noteworthy mentions in the Asia region – again with minimal losses expected to the strategy.

The underlying thesis of our insurance-related investments strategy remains strong as we continue to place emphasis on peril and geographical diversification achieved through customised portfolios with five manager relationships. The focus persists on remote risk / top layer reinsurance exposures, primarily across the US with smaller exposures to Europe and Japan as we believe this approach provides the most optimal risk-return profile.

The asset class remains very attractive on an absolute risk-return basis, with expected no loss returns in the mid-teens, especially given the diversification it provides relative to equity and bond markets.

## Appendix 1: Understanding fees that are deducted from returns in this investment update

The insurance-related investments strategy is one of a number of different strategies that form part of MLC's diversified funds. As such, the strategy only makes up a small component of the Management Fees and Costs that are charged to members when they invest in one of the diversified funds. When publishing the performance of the insurance-related investments strategy in this document, we have used figures that are gross of the Management Fees and Costs, with the exception of the Indirect Costs directly associated with the insurance-related investments. This is to ensure the performance shown isn't impacted by the total fees and costs that are charged for all of the strategies within the diversified funds. The Indirect Costs taken out of the performance shown in this report are incurred when the strategy invests in external investment funds. They aren't additional fees retained by MLC.

The asset allocation to insurance-related investments is relatively small compared to the total assets of the relevant diversified funds and are set to serve the investment objectives of the funds. The returns shown in this report demonstrate the insurance-related investments strategy's past performance over periods of time in history. These historical returns shouldn't be relied upon as any indication of the future and ongoing performance of the insurance-related strategy held by the MLC diversified funds or any other funds.