A 100-150 bps rise in rates would help life insurers: Fitch

By Editorial Staff *Thu, Jan 8, 2015*

Conversely, if interest rates decline to levels seen in 2012 and stay there much beyond 2015, Fitch would likely change the outlook for life insurers to negative, the ratings agency said in a release.

The rating outlook for the U.S. life insurance industry is stable for 2015, according to Fitch Ratings. In addition, the fundamental sector outlook is stable. Fitch's outlook considers the industry's very strong balance sheet fundamentals, strong liability profile, and stable operating performance.

But Fitch also expressed "ongoing concerns" over the impact of persistent low interest rates that "will pressure interest margins and reserve adequacy in 2015." Fitch expects relatively stagnant earnings growth in 2015 due to a moderate decline in interest margins, which will offset growth in fee and underwriting income.

Fitch forecasts "modest improvement" in the macroeconomic environment, which should allow life insurers to sustain recent improvement in industry balance sheet fundamentals and financial performance. Fitch expects credit-related investment losses in 2015 to remain below pricing assumptions and historical averages based on strong corporate bond fundamentals and further improvement in the real estate market.

Fitch expects reported statutory capitalization, which exceeds both pre-crisis levels and rating expectations, to be sustained over the coming year driven by retained earnings, various capital management initiatives, and modest growth in in-force business. Further, Fitch continues to view the industry's liquidity profile as very strong.

Concern over equity market risk tied to legacy variable annuity (VA) guarantees has decreased due to improved equity market conditions in recent years, but is expected to remain a drag on profitability over the near term. Longer-term, Fitch remains concerned about tail risk associated with VA guarantees, which could cause a material hit to industry earnings and capital in unexpected, but still plausible, severe stress scenario.

Fitch believes that a rise in interest rates by 100 bps to 150 bps could have positive implications for our sector outlook for U.S. life insurers. Conversely, if interest rates decline to levels seen in 2012 and stay there much beyond 2015, Fitch would likely change the outlook to negative based on weakened earnings profile and anticipated capital impacts associated with reserve strengthening.