May 2018
BEST'S REVIEW®
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A.M. Best's Monthly Insurance Magazine

Asset Management

Building an AUM SWAT Team

Former New York Life executive Chris Blunt leads Blackstone's new insurance asset management business with an emphasis on alternative investment vehicles.

by Jeff Roberts

The first concession his wife made was just giving her blessing.

Chris Blunt had retired in May 2017. He had left the insurance industry behind.

But then Blackstone came calling, having launched a new insurance solutions division in late 2017 solely focused on insurer assets. And the investment giant wanted the former head of New York Life's asset management unit to run it.

Blunt's retirement lasted all of seven months.

"This just came along, and it seemed too perfect to pass up," he said.

But then came Gretchen Nickel's second concession, what Blunt calls his wife's "great concession."

Photo by Kim Bjorheim

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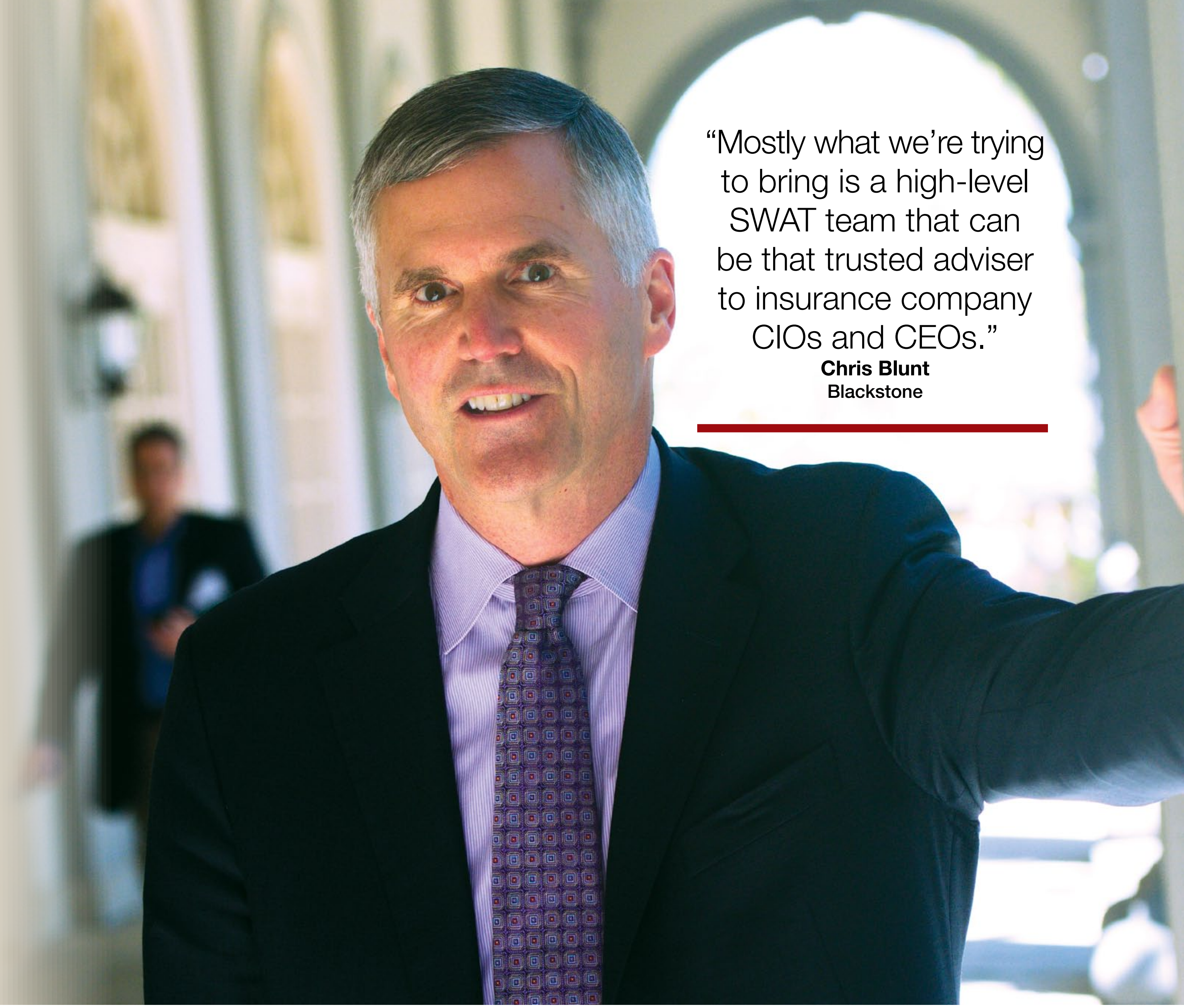
"She agreed that we can live five blocks from the office," he said of Blackstone's headquarters on Park Avenue in Manhattan.

The long hours inevitably followed. But there is much to do when you're trying to meet the insurance industry's desperate need for yield through bespoke alternative vehicles and origination capability.

That challenge lured Blunt out of retirement in January to become the senior managing director and chief executive officer of Blackstone Insurance Solutions.

His first six weeks were spent recruiting a staff. Engaging carriers. Devising alternative investment solutions it believes provide exposure to high yield with little risk and less onerous capital treatment.

"There's good tired and bad tired. Right now, it's



"Mostly what we're trying to bring is a high-level SWAT team that can be that trusted adviser to insurance company CIOs and CEOs."

Chris Blunt
Blackstone

all good tired," said Blunt, 55. "If I was a better skier or golfer, maybe I would have stayed retired."

Blackstone is betting Blunt is the right man—and it's the right time to launch the business. Insurers face "a perfect storm of significant policyholder obligations and declining investment returns in the public markets," said Tony James, Blackstone's executive vice chairman.

The objective is to penetrate the largely untapped $23 trillion industry—only about $2 trillion is outsourced to external managers—by luring yield-starved insurers to trust them with their investment portfolios, whether in part or fully.

The world's largest private equity firm will offer investment management expertise. It plans to create customized and diversified long-duration alternative vehicles. And it intends to originate debt for some clients amid an emerging shortage of high-yield, low-risk private assets in liquid markets, especially investment-grade corporate bonds.

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Key Points

$23T Opportunity: Blackstone plans to lure yield-starved insurers in the largely untapped $23 trillion industry to trust their investment portfolios to them.

Room for More: Only about $2 trillion of the industry's investible assets are outsourced to external managers.

The Goal: Blackstone's insurance business could generate $500 million annually in management fees once it reaches its stated goal of $100 billion AUM.

Blunt said. "We want to be that first call when people are wrestling with things."

Most insurance companies have only small allocations to alternatives. But low rates and the scarcity of high-quality fixed income, especially corporate debt, are driving insurers to alternative investments, Blunt said. They require specific expertise, so insurers are turning to external asset managers.

Blackstone enters a field led by BlackRock ($272.8 billion in insurer assets), Deutsche Asset Management ($190 billion) and Goldman Sachs Asset Management ($170.4 billion). The landscape has grown more competitive as externally managed assets grew 8.1% globally in 2016, according to Insurance Asset Outsourcing Exchange.

Blackstone's strategic vision is simple, if ambitious.

"This is a $23 trillion market and opportunity," Blunt said. "And we want to be the most trusted investment adviser to insurers globally."

Blackstone's stated target is to attract at least $100 billion in global insurance assets. It already holds about $23 billion thanks to a partnership with Axis Capital Holdings that created Harrington Reinsurance and its role in an investor group that acquired Fidelity & Guaranty Life for $1.8 billion.

The insurance business could generate $500 million annually in management fees once it reaches that $100 billion milestone, Bennett Goodman, chairman of the insurance solutions business, told Bloomberg Television in March.

Filling a Need

The genesis came three years ago.

Blackstone recognized a need in the marketplace through those partnerships with Harrington and Fidelity & Guaranty.

In response, it plans to create bespoke investment vehicles that produce higher returns and meet long-term policyholder obligations without altering insurers' risk profiles. It also aims to offer more capital-efficient structures.

"The No. 1 issue that any insurer is dealing with—and it's a global phenomenon—is they're having a really difficult time gaining access to high-quality credit," Blunt said. "There is a dearth in the market place, whether it's long-duration corporates or private bonds or mortgages.

"There's almost no insurance company in the world that doesn't have an interest in finding high-quality pieces of paper and an attractive yield. And it just so happens that we're in a really great position to help solve those unique needs as one of the largest alternative managers in the world and one of the largest originators of debt on the planet."

Blackstone offers private credit, infrastructure, acquisition finance and real estate debt—investment vehicles in demand among insurers.

The reaction from carriers has been enthusiastic and discussions are ongoing, according to Blunt.

"We've had a number of insurers who have raised their hands and expressed interest in being one of our initial strategic clients," he said.

For some insurers, outsourcing at least some of their asset management operations is an increasingly attractive option. Interest rates remain historically low despite recent increases. Spreads are tight. And there is a shortage of long-duration, investment-grade bonds, which traditionally account for more than 80% of life insurers' investment allocations.

Meanwhile, insurers' liabilities are growing across the life, property/casualty and health spaces.

"That's a bad combination: when your assets grow slowly and your liabilities grow fast. It doesn't take long to completely change the dynamic of an industry," Blackstone's James said. "That's created a yawning gap, and they need a way to fill it."

But Blackstone needed to find someone to run the business.

Hard Guy to Find

James had his doubts.

He was skeptical Blackstone could find all the traits required in its new insurance solutions chief executive.

It needed someone with credibility in the insurance industry. Someone who understands insurers' capital, duration, liability, liquidity, return and risk needs. Someone who could navigate the complex web of regulatory bodies and ratings firms.

And someone entrepreneurial because Blackstone views the new unit as a "startup" of sorts.

"Frankly, one of the reasons we were a bit slow to start the search is because I thought, 'Wow, this is going to be a hard guy to find,'" James said.

Then a search firm found Blunt.

The Detroit native, a self-described long-suffering sports fan, worked for New York Life for 13 years, serving as president of its investments group for two. He also was co-president of its insurance and agency group

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and a manager in its retirement income security and life and annuity divisions.

Blunt, who chairs the board of the New York City YMCA, previously worked for Merrill Lynch Investment Managers and Goldman Sachs Asset Management. He also ran GivingCapital, a wealth management solutions provider supporting charitable giving.

“He could speak to all of the needs,” James said. “He has that entrepreneurial streak. And he’s a nice guy. He’s perfect for us.”

Blunt describes his early tenure as gratifyingly challenging. His days begin by 5 a.m. and often send him to bed late.

“It’s exhilarating, and it’s a little scary at times,” Blunt said. “Given the choice, you always want to have the ball.

“I feel like I boarded a train going 300 mph. My wife says I enjoy chaos. We like to think it’s controlled chaos, but it’s definitely dynamic.”

Blunt’s staff of 25 will grow to 40 to 45 within 18 months, with an eventual ceiling of 50 to 60 employees, he said.

He made one of his first big additions in March, hiring Michael McRaith as managing director. McRaith was the first director of the U.S. Treasury’s Federal Insurance Office, serving from 2011 to 2017, and was the director of the Illinois Department of Insurance.

Blunt’s staff aims to satisfy different needs, depending on the insurer.

Maybe it’s optimizing a carrier’s alternative support portfolio with products like real estate debt or infrastructure. Maybe it’s sourcing unique private credit opportunities that it might not see directly from Wall Street. Or maybe it’s advising an insurer on its balance sheet through Blackstone’s private equity capabilities.

Blackstone, which manages $434 billion in assets overall, also plans to use risk analytics to help insurers monitor and stress test their portfolios, Goodman told Bloomberg Television.

“Insurers are the ultimate long-term investors,” Blunt said. “They’re one of the last sources of long-term capital formation left globally. We think it plays really well into our strengths.”

Blunt believes fate led him here. He views his divergent career paths—investment management, running a startup, insurance—as preparation for Blackstone.

“I described the job to my wife, and she said it sounded tailor-made for me,” he said.

His former boss, New York Life CEO Ted Mathas, captured the essence of the opportunity in a conversation with Blunt late last year as he mulled the offer.

“What he said last was interesting: ‘This is really good for the industry.’ Meaning the industry needs to find ways to get better returns but done in a prudent way,” Blunt said. “That just really hammered home the idea that maybe it’s all for a reason.”

New York Life declined an interview request, allowing “the focus to be on Chris and his new role,” said Jason Weinzimer, head of external communications for the insurer, in an email.

Blunt already has made his presence felt in just a few months.

“We had a vision, but it was a vision by a bunch of less informed people,” James said. “Chris embraced the potential. Now he’s filling in the picture.

“All the meat on the bones are his. And he’s changed a few of the bones too.”

Origination

Blackstone did have quite a head start.

Managing the Harrington Reinsurance and Fidelity & Guaranty portfolios taught at least two lessons.

Namely, Blackstone believes it can add value without changing risk profiles. And it found it can leverage resources already in place to originate credit and access high-returning alternative strategies.

Blackstone conducted extensive live testing before hiring Blunt, James said.

"For three years we've had a test tube using our own insurance companies, finding ways to mix them and match them so that they deliver higher returns with very low risk," he said. "When it's been tested in actual use in an insurance company, and then we can go to the rating agencies and the regulators and get them to sign off on it and give us better capital treatment, now we have something that no one else has.

"And no one else can really replicate it because no one else has a broad enough mix of products to create those structures."

The ability to originate debt may be Blackstone's trump card.

U.S. tax cuts have contributed to a drop in the issuance of long-duration, high-grade corporate bonds, exacerbating an already short supply.

"So insurers really have to scramble," Blunt said. "Deals are widely oversubscribed. Often they don't fit exactly the way you need them to fit within your general account portfolio."

Blackstone originated $170 billion in debt in 2017. And it plans to leverage that capability.

It will manufacture investment-grade, non-investment grade and real estate credit opportunities directly for "our best insurance clients," Blunt said. It formed a committee representing its various businesses to discuss ways to create products for insurers.

The largest carriers have their own private credit origination units, but there are only a handful, according to James.

"The needle in the haystack for insurers is higher-returning products, products that you can't buy and sell in the public markets," he said. "We were already originating a lot of this for other purposes or as a byproduct for other business. Now, we have demand.

"We can give them the higher return they want, with lower capital requirements. And that is nirvana, the magic bullet."

The Recruiting Game

The first step is recruiting clients.

Before Blackstone can manage insurers' portfolios, it has to win their trust.

That is where Blunt's connections and expertise comes in. He sees five "avenues" to attracting insurers' assets.

Blackstone will tout its standing as a leading alternative asset manager, offer more capital-efficient structures and the origination capability, Blunt said. It also will provide outsource management, taking on insurers' alternatives allocations or even their entire general accounts.

And it will seek more "Fidelity & Guaranty opportunities, where not only are we bringing investment expertise, but we're bringing some equity capital to the table," Blunt said.

Blackstone views its potential client base as running the global insurance spectrum, including life, property/casualty and reinsurance companies. But three markets stand out as obvious targets.

The first is the U.S. life and annuity space, especially midsize carriers hungry for yield. Insurers in the United Kingdom are a good fit due to the "matching adjustment" rule in Solvency II. And infrastructure and real estate products might be especially attractive in Asia.

Insurers have pushed out on the yield curve and dropped down in credit quality. The exhaustion "of the obvious low-hanging fruit" investments such as commercial mortgage-backed securities have left few options, according to Blunt.

"I would argue there's only a couple of paths from here," he said. "Insurers, particularly life insurers, are becoming much more interested in private credit.

"Their issue is finding managers that have legitimate expertise. That's the burden on us—to get out and have enough conversations with the right insurers to partner with."

Private debt exposure accounts for about 30% of the life insurance industry's bond allocation, according to Barclays. And that percentage is expected to rise.

More liquidity risk is one option, with most insurers holding long duration liabilities.

And infrastructure in particular has piqued the interest of insurers, Blunt said. Of course, Blackstone announced in May 2017 that it will form a new infrastructure business with a $40 billion fund.

For Blunt, meeting a vital industry need lured him back from retirement.

"Candidly, what drew me back is the mission driven aspect of this," he said. "Yes, it's a great opportunity to build a business and a really fun entrepreneurial opportunity.

"But equally important, I just love the idea that we might be able to move the needle a little for the whole industry, not just a single company." BR