

Life insurance companies' investment abroad and the internal rate of return on Chilean annuities

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Abstract

The Chilean insurance industry has experienced significant growth in recent years through annuity sales, requiring life insurance companies to actively manage longevity and reinvestment risks. As a result, the regulator opened up investment options in international instruments in order to diversify portfolios and increase the expected internal rate of return on annuity policies. We analyse both the determinants of Chilean life insurance companies' investment abroad and what effect investment abroad has on the internal interest rates paid on annuities. We fit regression models by OLS fixed effects and GMM to information on 15 life insurance companies for the period of March 2008-September 2019. Investments abroad persist over time and managers are seen to actively allocate these. Furthermore, companies with greater investments abroad are more likely to increase annuity payouts in the range of 2.2% to 4.2%. Finally, we find that a more competitive insurance market could increase pension payouts from 3.1% to 3.7%. Policymakers may use these results to continue diversifying portfolios and to manage the structure of the life insurance market to further increase annuitants' welfare.

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