

Cash No Longer King: How P&C Insurers Can Capture the Bond and Equity Rotation

As of mid-2025, over \$7 trillion sits in U.S. money market funds—an all-time high. Much of this liquidity has been held by institutional investors, in particular property and casualty (P&C) insurers who have been among the fastest to increase and retain elevated cash balances in recent years. Initially, this positioning was a prudent response to macro uncertainty, Fed tightening, and volatility in both fixed income and equities.

However, the regime is changing. With the Federal Reserve initiating rate cuts in September 2024, and a year-end 2025 federal funds rate now projected around 3.75%–4.00%, the relative yield advantage of cash is eroding. P&C insurers that continue holding strategic excess liquidity risk not only diluting portfolio returns but missing critical reallocation opportunities, especially in public equities and high-quality bonds.

Insurers' affinity for cash is rational particularly so given market behavior over the last few years. Surging interest rates in 2022–2023 elevated reinvestment risk, increased unrealized losses on existing holdings, and compressed statutory capital levels. Holding cash provided optionality, yield (as high as 5.25% in 2024), and insulation from mark-to-market volatility.

But that advantage is fading. As money market yields decline into the 3.75%–4.00% range, the “strategic cash” thesis loses its luster. For insurers managing to fixed income benchmarks and surplus return targets, cash will soon become a performance drag rather than a defense.

Beyond Cash: Where Insurers Might Turn

For insurers rethinking portfolio construction, both equity and bond assets classes and subclasses (e.g. Euro stocks, High Yield or Convertible bonds, etc.) present relevant, though distinct, opportunities. Allocation decisions should reflect enterprise-wide risk budgets, RBC sensitivities, along with regulatory and ALM constraints. Here's how the landscape currently looks:

1. Equities: Targeted Participation in a Broadening Market

Equity exposure remains a minority position in most P&C general accounts—but is often critical to achieving return-on-surplus targets. As markets stabilize, several categories look increasingly attractive.

A. Growth Stocks (Tech, AI, Consumer Discretionary)

- **Why it matters:** These stocks remain underheld by institutional investors, yet are central to market leadership and innovation.
- **Examples:** Microsoft, Nvidia, Amazon—liquid, earnings-anchored names tied to secular AI and cloud trends.
- **Caveat:** Valuations are elevated; insurers must be mindful of concentration risk, especially given the “Magnificent Seven” now comprise over 30% of key U.S. indices.

B. Value & Cyclical (Financials, Industrials)

- **Why it matters:** These sectors offer dividend income, earnings stability, and are typically less rate-sensitive. Financials, in particular, benefit from steeper curves and rising credit activity.
- **Relevance to insurers:** Value and cyclical often outperform in soft-landing scenarios, which aligns with current macro signals and positioning.

C. Healthcare, Energy, and International Equities

- **Tactical appeal:** Healthcare is gaining interest due to AI-integration and long-term defensiveness. Energy and emerging markets (e.g., India, Brazil) offer diversification and potential inflation hedges. Such “tactical” sector plays are typically best fulfilled by low-cost ETF investments.

2. Fixed Income: A More Attractive Core Allocation

While equities offer upside, the bond market now presents a core opportunity, especially for insurers that have been underweight duration or wary of 2022’s volatility. As the Fed eases, yields across the curve are resetting, and the total return profile of intermediate and longer-duration (AGG) bonds is improving.

Why Bonds Now?

- **Rate cuts are here:** The Fed has already begun cutting rates, with two more cuts projected before year-end. The year-end rate is projected at **3.75%–4.00%**, down from a peak of 5.5%.
- **Total return potential:** As yields fall, bond prices rise, especially for longer maturities. A 75–100 basis point cut scenario, possibly looking forward 4-5 quarters, creates strong upside for duration-sensitive assets. (e.g. A portfolio with a duration of 4 years (intermediate) would receive approximately 4% in market value increase, in addition to the coupon rate, for each 1% (100 BPs) rate decrease.

- **Credit spreads remain stable:** Corporate credit markets remain well-behaved, with spreads near historical medians and default risk well-contained supporting both Investment-grade (IG) and select high yield allocations.
- **RBC advantages:** For P&C insurers, moving from cash into high-quality corporates or municipals with moderate duration provides capital-efficient yield pickup without adding excessive RBC burden.

Strategic Opportunities in Bonds

Segment	Rationale
Investment-Grade Corporates	Attractive yields (4.5%–5.25%), strong credit quality, minimal capital drag
Municipals (Taxable & Tax-Exempt)	Strong relative value for insurers, especially in high-tax states
Structured Credit (RMBS/CMBS)	Moderate complexity premium with liquidity, good for diversification
Short Duration High Yield	Incremental spread, suitable for insurers seeking modest risk/reward tilt

Insurance-Specific Risks of Inaction

Remaining overweight cash may seem prudent—but the real risk now is missing the turn. Insurers that wait too long may face:

- **Cash drag on surplus returns:** With underwriting margins narrowing, investment income is a critical lever. Cash returns at 3.75%–4.00% is no longer sufficient to meet return hurdles given that “claims inflation” traditionally has run ahead of CPI and headline inflation.
- **Competitive underperformance:** Peers deploying selectively into bonds or equities may outpace those that remain in liquidity.
- **Reinvestment risk:** As maturities roll off and rates fall further, reinvesting at materially lower yields may lock in long-term return deficits.
- **ALM mismatch:** Holding excess cash may distort asset-liability profiles, especially in long-tailed P&C books.

Summary Table: Reallocating Cash Strategically

Asset Class	Why It's Attractive Now
Cash / MMFs	Still useful tactically, but yields declining (3.75%–4.00% by year-end)
Investment-Grade Bonds	Strong yields + price upside from rate cuts
Short Duration High Yield	Incremental spread, modest capital impact
Equities (Value/Cyclicals)	Participation in early recovery themes
Equities (Growth)	Selective exposure to innovation and AI
Healthcare / Int'l Stocks	Diversification, Strong projected non-US stock returns and innovation potential

CapVisor Conclusion

P&C insurers have done well to preserve capital and maintain flexibility through a period of extreme macro and market disruption. However, the next 12–18 months require a different kind of discipline; one that balances caution with opportunity, and liquidity with productivity.

As Fed policy shifts and markets normalize, insurers' investment strategies must evolve accordingly. Reallocating even a portion of idle cash into strategically chosen bonds and equities may help insurers optimize total return, reduce reinvestment risk, and ensure balance sheet resilience in the next cycle.

The question for CIOs and investment committees is no longer “Why hold cash?” but rather, “How much longer can we afford to?”