

October 23, 2019

2020 GENERAL RATE APPLICATION  
Undertaking #21 Transcript Page 1154

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**Undertaking #21**

MPI to provide an explanation for the pattern change in the minimum capital required in PF-3.

**RESPONSE:**

The October 4 reforecast had a reduction in interest rates causing an increase in corporate bond values that triggered the application of an investment asset rebalancing rule in Q3 of 2022/23. This rebalancing event did not occur in the original 2020 GRA forecast. More specifically, corporate bonds exceeded the maximum target weight in Q1 and Q2 of 2022/23. As a result, corporate bonds were rebalanced to target weight in Q3 of 2022/23.

This rebalancing resulted in an increase of percentage weighting to equity investments. When calculating capital required under the Minimum Capital Test, equity investments carry a larger risk factor than corporate bonds.

Also, the capital requirement for interest rate risk increased in the revised 2022/23 forecast. The reduction in corporate bonds resulted in a larger dollar duration gap relative to interest rate sensitive liabilities.

Please see Appendix 1 for the initial and updated forecasts. For more information on RSR rebalancing rules, please see Part VI Investments INV.11.2.

**Appendix 1:  
Rebalancing Forecasts**

Line No.	(All figures in \$000s, unless otherwise noted)	Initial Forecast				Revised Forecast			
		2019 - 2020 Forecast Base Year	2020 - 2021 Forecast Year	2021 - 2022 Forecast Year	2022 - 2023 Forecast Year	2019 - 2020 Forecast Base Year	2020 - 2021 Forecast Year	2021 - 2022 Forecast Year	2022 - 2023 Forecast Year
1	Capital Available:								
2	Capital available (from page 30.62 - capital available)	314,023	358,810	400,205	461,826	342,698	363,261	375,186	408,296
3	<b>Total Capital Available</b>	<b>314,023</b>	<b>358,810</b>	<b>400,205</b>	<b>461,826</b>	<b>342,698</b>	<b>363,261</b>	<b>375,186</b>	<b>408,296</b>
4	<b>Capital (Margin) Required at Target:</b>								
5	<b>Insurance Risk:</b>								
6	Premium liabilities	98,382	102,340	106,305	110,464	97,833	101,174	105,093	109,202
7	Unpaid claims	210,461	219,212	228,455	237,641	214,933	227,998	238,282	248,089
8	Catastrophes								
9	Margin required for reinsurance ceded to unregistered insurers	0	0	0	0	19	25	25	25
10	<b>Subtotal: Insurance risk margin</b>	<b>308,843</b>	<b>321,552</b>	<b>334,760</b>	<b>348,105</b>	<b>312,785</b>	<b>329,197</b>	<b>343,400</b>	<b>357,316</b>
11	<b>Market Risk:</b>								
12	Interest rate risk	36,695	39,882	43,234	48,478	47,935	47,830	48,741	59,206
13	Foreign exchange risk	23,499	25,813	27,718	29,746	20,198	20,744	20,938	30,919
14	Equity risk	96,030	107,396	115,463	124,054	81,500	79,533	74,891	119,946
15	Real estate risk	30,891	30,360	31,447	32,864	23,056	22,194	22,971	24,061
16	Other market risk exposures	0	0	0	0	0	0	0	0
17	<b>Subtotal: Market risk margin</b>	<b>187,115</b>	<b>203,451</b>	<b>217,862</b>	<b>235,142</b>	<b>172,689</b>	<b>170,301</b>	<b>167,541</b>	<b>234,132</b>
18	<b>Credit Risk:</b>								
19	Counterparty default risk for balance sheet assets	43,527	49,509	51,992	54,615	41,983	45,859	50,337	49,532
20	Counterparty default risk for off-balance sheet exposures	1,272	1,264	1,257	1,250	1,272	1,264	1,257	1,250
21	Counterparty default risk for unregistered reinsurance collateral and SIRs								
22	<b>Subtotal: Credit risk margin</b>	<b>44,798</b>	<b>50,774</b>	<b>53,249</b>	<b>55,865</b>	<b>43,255</b>	<b>47,124</b>	<b>51,594</b>	<b>50,782</b>
23	<b>Operational risk margin</b>	<b>73,974</b>	<b>78,087</b>	<b>81,783</b>	<b>85,804</b>	<b>72,775</b>	<b>75,271</b>	<b>77,748</b>	<b>85,703</b>
24	<b>Less: Diversification credit</b>	<b>70,871</b>	<b>76,004</b>	<b>80,207</b>	<b>84,889</b>	<b>68,283</b>	<b>69,946</b>	<b>71,419</b>	<b>84,866</b>
25	<b>Total Capital (Margin) Required at Target</b>	<b>543,859</b>	<b>577,860</b>	<b>607,447</b>	<b>640,027</b>	<b>533,221</b>	<b>551,947</b>	<b>568,864</b>	<b>643,067</b>
26	Minimum Capital (Margin) Required (line 59 / 1.5)	362,573	385,240	404,965	426,685	355,481	367,965	379,243	428,711
27	Phase-in of Capital (Margin) Required	0	0	0	0	0	0	0	0
28	<b>Total Minimum Capital (Margin) Required</b>	<b>362,573</b>	<b>385,240</b>	<b>404,965</b>	<b>426,685</b>	<b>355,481</b>	<b>367,965</b>	<b>379,243</b>	<b>428,711</b>
29	<b>Excess Capital (Net Assets Available) over Minimum Capital (Margin) Required</b>	<b>-48,550</b>	<b>-26,430</b>	<b>-4,760</b>	<b>35,141</b>	<b>-12,783</b>	<b>-4,704</b>	<b>-4,057</b>	<b>-20,415</b>
30	<b>MCT (BAAT) Ratio (Line 09 or line 19 as a % of line 69)</b>	<b>86.61%</b>	<b>93.14%</b>	<b>98.82%</b>	<b>108.24%</b>	<b>96.40%</b>	<b>98.72%</b>	<b>98.93%</b>	<b>95.24%</b>