



Towards measuring systemic risk and vulnerabilities in the insurance sector

- *Session I: Enhancing transparency and monitoring of the insurance industry and the way forward*

2nd OECD-Asia Regional Seminar on Insurance Statistics

26-27 January 2012, Bangkok, Thailand



Outline ...

... or questions that we will advance today:

1. How to identify vulnerabilities and systemic risk in the insurance sector?
2. Do differences between the insurance- and the banking-sector matter?
3. What kind of data do we need to enhance transparency and monitoring of the insurance sector?



Towards measuring systemic risk

Systemic risk – approaching a definition:

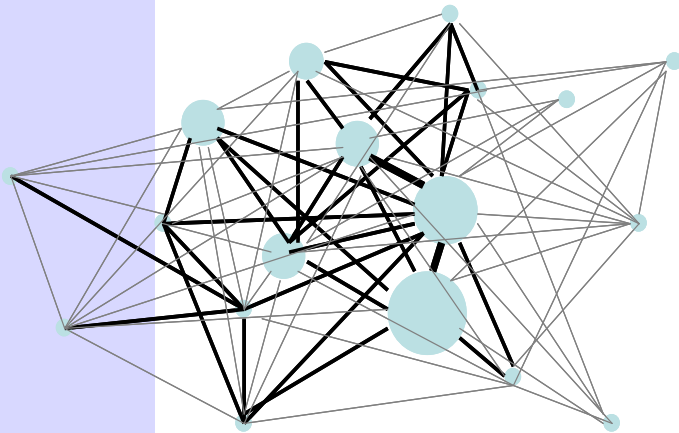
- “*Significant disruption to the wider financial system and economic activity*”

(Financial Stability Board (FSB), October 2010)

Towards an identification of ...

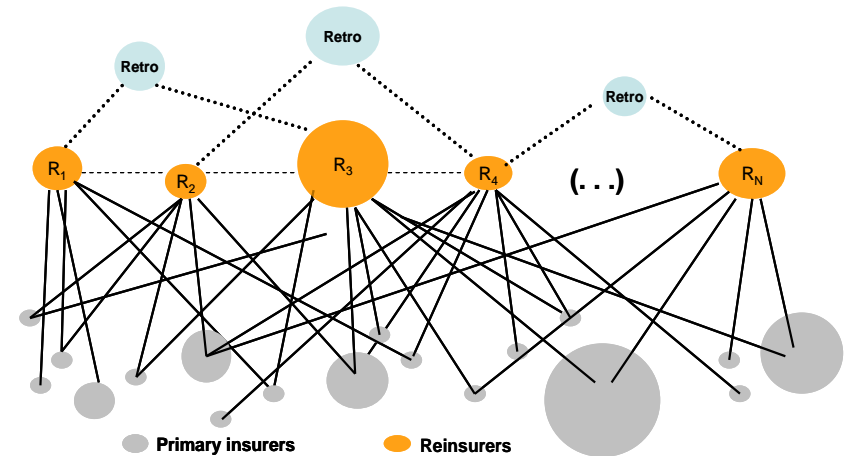
... vulnerabilities in different sectors of the financial market

The network structure of the global interbank market



Source: Haldane (2010) / IAIS

The hierarchical structure of the (re)insurance market



Source: FINMA / IAIS

Observations:

- **Banks** are part and parcel of a complex network: Network feedback mechanisms are likely to amplify shocks through the whole market
→ process can create systemic crisis
- **Insurers** are less interconnected: Fewer feedback loops; Reduced likelihood for non-linear systemic reactions; Built-in circuit breakers
→ lower probability for systemic crisis



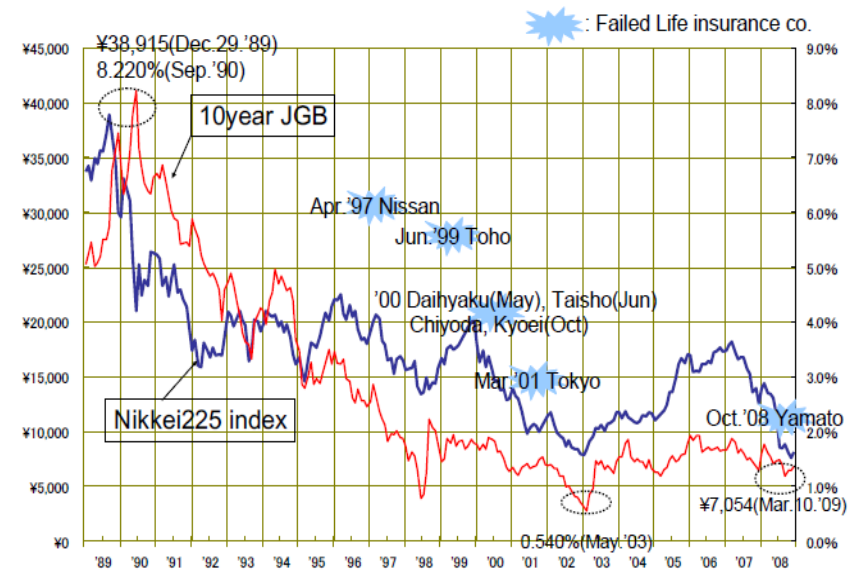
Could the failure of individual companies ...

... result in systemic risk (1/2) ?

First example

The Japanese experience:

- Prolonged low interest rates
- Adverse stock price development



Source: Makoto Okubo: Tao of Macroprudential Supervision, at IAIS September 29, 2011

Observations:

- A number of life insurance companies were insolvent
- Systemic events not observed on life market in Japan
- Most Japanese life insurers have survived, due to:
 - ✓ Other sources of profit
 - ✓ Well managed companies



Could the failure of individual companies ...

... result in systemic risk (2/2) ?

Second example – The AIG experience

- Exposures incurred by the financial products (FP) unit – a subsidiary based in London
- Bailout by US Government:

Payments to
securities lending
counterparties of AIG,
by US-Gov., bn US \$

Barclays	\$ 7.0
Deutsche Bank	\$ 6.4
BNP Paribas	\$ 4.9
Goldman Sachs	\$ 4.8
[...]	[...]
Total	\$43.7

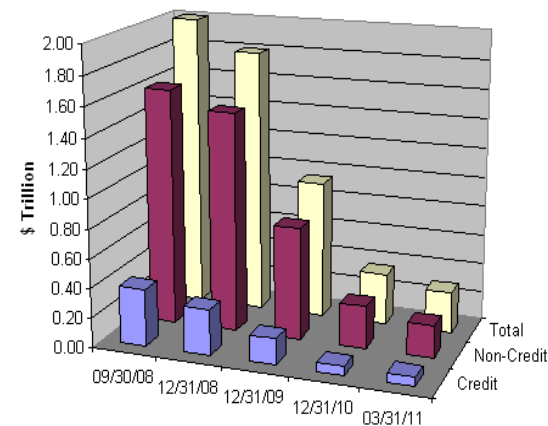
Payments to
credit default swap
counterparties of AIG,
by US-Gov & AIG

	Gov.	AIG
Soci�te G�n�rale	\$ 6.9	\$ 9.6
Goldman Sachs	\$ 5.6	\$ 8.4
Merrill Lynch	\$ 3.1	\$ 3.1
[...]	[...]	[...]
Total	\$27.1	\$35.0

Source: The financial crisis inquiry report, USA.; Specific selection by IAIS

Wind-up of AIG FP

Notional amount of derivatives outstanding



Source: <http://www.aigcorporate.com/restructuring/keyrestructuring.html>

Observations

- Exposures by FP-subsi-dary could have caused a systemic event
- Non-insurance activities triggered the challenges faced by AIG



A summary of selected contributions by ...

... the IAIS

(1) Increasingly:

- **Data** collection, analysis and support for IAIS Members regarding the use of data, e.g.:
 - ✓ Contributions on stress-tests;
 - ✓ GRMR → GIMAR
- **Systemic** considerations, **macroprudential** surveillance, **financial stability** and **vulnerabilities** assessments

(2) Ongoing key output:

- **Global Principles** (Insurance Core Principles ‘ICPs’), Standards and Guidance for insurance supervision and regulation

(3) Last but not least:

- **Implementation-** and assessment-support on IAIS ICPs, Standards and Guidance, including contributions to education and supervisory cooperation



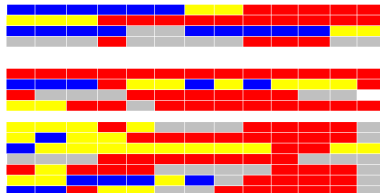
Ongoing monitoring by the IAIS ...

... on significant overall market developments

- What are the implications for the insurance sector, e.g. if rising inflation?
- Assessment from a supervisory perspective:

Risk	Potential consequences insurers	Supervisory challenges
Accelerating inflation	<ul style="list-style-type: none"> • Inadequate provisioning in long-tail lines; claims inflation 	<ul style="list-style-type: none"> • Monitoring of reserve adequacy

Source: IAIS, Key Insurance Risks and Trends (KIRT)



Source: IMF, WEO



IAIS survey on macroprudential surveillance

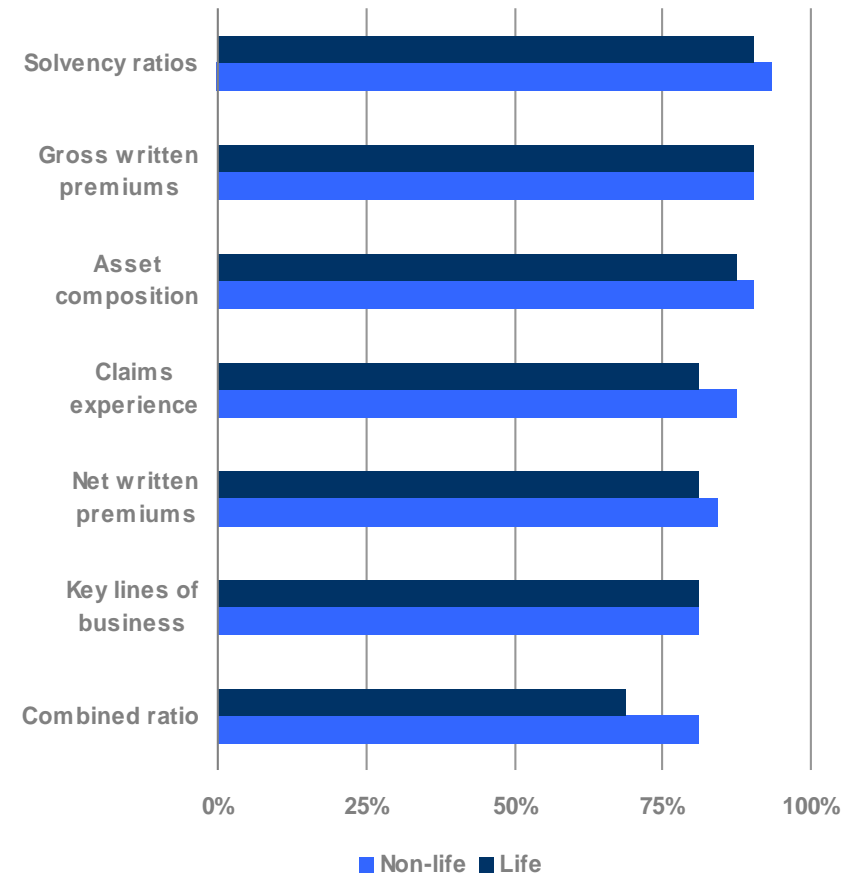
Existing insurance-specific indicators:

Regions participating

- Africa;
- Asia and Oceania;
- Caribbean, South and Central America;
- Europe;
- North America.

Selected findings

- Rather domestic focus in all regions;
- Further improvements foreseen for next two years;



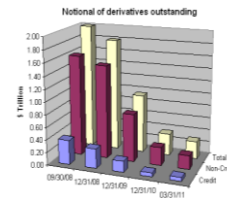


Preliminary conclusions regarding data ...

... in the light of vulnerabilities and systemic risk

Company specific data ...

- ... necessary ...
- ... but sometimes ...
- ... not sufficient ...
- ... to identify vulnerabilities and systemic risk



	Gov.	AIG
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Microprudential *and* macroprudential data collection

- Approaches need to be married
- Ideal: coordination from the beginning, e.g. this seminar

Observations

- Data collection requires national *and* international organisations
- Challenge to avoid both: gaps and unnecessary duplication (burden)



The G-SIFI debate and the IAIS

Determination of institutions ...

... to which initial FSB G-SIFI recommendations apply

- “FSB and national authorities in consultation with ...”
- “... BCBS, CGFS, CPSS, IOSCO and IAIS” (compare FSB website)

Current process on banking G-SIFIs

- BCBS looked into universe of banks: 29 have been identified
- Precise treatment of those identified will be announced later

Insurance supervisors (IAIS) perspective

- Degree of ‘SIFI-ness’ important → “non-insurance” and “non-traditional”
- IAIS is in the process of developing a methodological framework
- Several jurisdictions have been invited to provide data to the IAIS

Next steps?

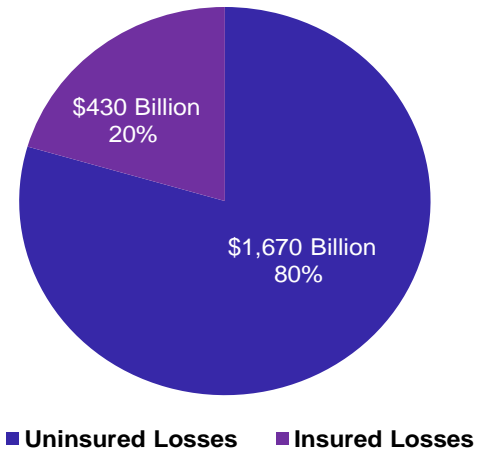
- 2012: release for public consultation - proposed assessment methodology ...
- ... together with details of proposed policy measures for any G-SII



Last but not least it is important to put “systemic risk” ...

... that may arise from the insurance sector into perspective

- **A brief illustration:** All great natural catastrophes worldwide: 1950-2010 ..
 - ... total economic loss of US\$ 2100bn ...
 - ... uninsured were: 80% (US\$ 1670bn)



- Availability of insurance ...
 - ... increases security in an unpredictable world ...
 - ... contributes to economic development
- In other words:
 - Considerations on how to improve the overall availability of insurance protection should not be lost ...
 - ... in light of the ongoing thinking regarding systemic risk



Thank you ...

Suggestions and comments are welcome!