

EU-wide Insurance Stress Test 2016

Daniel Pérez

Principal Expert Financial Stability, EIOPA

Project Manager EIOPA 2016 Insurance Stress Test

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Background of the Insurance Stress Test Exercise



Persistent low risk free rates and increased volatility on the equity markets characterize the current EU financial sector, making market risks the main source of concerns for the insurance industry stability.

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| Background | <ul style="list-style-type: none">• Challenging macroeconomic environment – need to follow up on previous exercises• Keep the burden on industry and NCA in the Solvency II enforcing year at its lowest• Engage in pre-launch consultation and workshop – streamline design and methodology |
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| Risks in the spot | <ul style="list-style-type: none">• Liaise with ESRB• Persistent low yield environment – equity volatility – reassessment risk premium• Market risks rather than insurance risks (need to prioritise) |
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| Target | <ul style="list-style-type: none">• Specific business lines: Life excluding Health and Unit Linked• Long-term business performed by solo undertakings (no insurance groups)• Enlarged target market coverage (75% Gross Life TP – proportionate approach) |
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| Aim | <ul style="list-style-type: none">• To identify the risks and vulnerabilities of the European insurance sector based on a common analytical framework.• No PASS/FAIL EXERCISE but an assessment of the sensitivity of insurers to adverse scenarios. |
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Framework: A focused exercise collecting quantitative and qualitative information under 2 scenarios



Two scenarios designed to investigate: *i)* What is the scale of the challenge posed by such environment? *ii)* What is the scope of the challenge posed by such environment? *iii)* What is the timeline for serious problems to emerge?

Scenario 1 - LY

- It is devoted to assess the vulnerability of insurance undertakings to a prolonged low yield environment
- It covers until the end of the existing contracts in the current insurance portfolios. Given the focus on those insurers providing long term guarantees this may go beyond 60 years in many cases.
- It assumes a lower UFR as one of the possible consequences if yields were to remain low for a considerable amount of time. There is no link with the ongoing consultation on the methodology to derive the UFR and this aspect is underlined by not assessing the probability of the scenario.

Scenario 2 - DH

- It is devoted to investigate how and to what extent low interest rates combined with negative market shocks affect insurance undertakings
- The scenario has been calibrated using the European Central Bank's (ECB) financial shock simulator and consists of a set of prices' shocks for a large spectrum of assets triggered by two simultaneous events: a shock in government bond prices and a drop in the risk free rate curve.
- It is a low probability event, at the same time its likelihood cannot be fully ruled out
- The scenario is accompanied by a qualitative questionnaire, which investigates the second round effects.

Key aspects in the design of the exercise



- Approaching solo undertakings primarily running long term business allows a better delimitation of the vulnerabilities created by the low yield environment at country level.
 - Support at consolidated basis will be qualitatively considered in the analysis phase
- Reference date 1 January 2016:
 - The stress test based on the Solvency II day-1 templates used for the supervisory reporting purposes. The additional information that is required for the stress test as well as the information which is required for the supervisory reporting purposes, but is either simplified or not required for the stress test, is clearly identified.
- EIOPA Stress Test 2016 is not a pass-or-fail exercise.
 - Its main focus is on assessing vulnerabilities and the potential systemic impact of shocks to the financial and economic environment.
 - As such, there are no requirements for recalculating solvency position post stress and some scenarios may include elements not prescribed in the regulatory framework.
 - The starting balance sheet of the ST reproduces the Solvency II balance sheet in the pre-stress situation.
 - However under the assumptions of two hypothetical adverse scenarios, it is considered more appropriate in assessing potential vulnerabilities at the European level to use a different assumption for the ultimate forward rate (UFR) in the low for long scenario and a particular application of the transitionals.
 - Consequently, the balance sheet after the scenarios which is relevant from a financial stability perspective would not be fully appropriate to assess the compliance with the legally enforceable SII capital requirements.
 - Given the purpose of the exercise the severity of the stress scenarios goes beyond the Solvency II capital requirements.
 - Further technical information can be found on EIOPA's and ESRB's Website – see link: <https://goo.gl/OXC5xr>

- The launch of the exercise was one week earlier than initially planned to allow the participating undertakings for more time to complete the test.
- The stress test technical specifications and templates are published on EIOPA's Website: <https://goo.gl/P3ZIeu>
- EIOPA will publish on a weekly basis Questions & Answers addressing possible queries of the participating companies on consistent basis. This process may imply updates of the stress test material such as specifications and templates to ensure they are fully consistent and appropriately interpreted.
- To ensure consistency of results, a two-step data validation procedure will be undertaken: first, at national and afterwards at EIOPA level
- To limit the industry burden EIOPA collects at the same time information on the Solvency II equity and Long Term Guarantees (LTG) measures. (Art. 77f of the Solvency II Directive)
- EIOPA will publish the list of participating companies, however, the results will be disclosed in an anonymized and/or aggregated way
 - Solvency II requires insurance companies to publicly disclose data related to their solvency positions as of 2017
 - EIOPA in cooperation with the NCAs is investigating the legal basis for possible enhancement of the disclosure of stress test results

Preliminary Participation & Timeline



- Preliminary EU average Market share: 77% Gross life technical provisions (excluding Health and Unit Link)
- +200 Insurance companies from 30 countries EU/EEA members;

TIMELINE EIOPA 2016 INSURANCE STRESS TEST

24 May	Official launching of stress test Publication of stress test package in EIOPA webpage
1 June	Online seminar for NCAs on ST package (processes, specifications, scenarios, templates)
June (Every Wednesday)	Publication of updated ST documents (Q&A, Templates, Specifications, etc.) Last publication of 29-06-16;
30 June	Online seminar for NCAs on data submission and validation

TIMELINE INSURANCE STRESS TEST DATA VALIDATION

15 July	Deadline for submission from ST participants to NCAs
End August	Data validation at National level
September	Meetings of central validation team in Frankfurt

TIMELINE INSURANCE STRESS TEST DRAFTING OF REPORT

30 November	BOS meeting (For approval of report and communication material)
5-9 December	Publication of stress test report



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Thank you

Daniel Pérez

email: daniel.perez@eiopa.europa.eu

phone: +49-69-95111965
