Macro-Prudential Approaches: Monitoring the Insurance Sector

Observations from Global Financial Stability Reports and the NAIC toolbox

NAIC Financial Stability Task Force
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Context

• Review of reports of global supervisors that provide insights on macro-prudential surveillance efforts
  – Identify risks / themes and how they are being addressed

• While micro-prudential approach focuses on strength of individual firms; a macro-prudential approach focuses on stability of the financial system
Report Focus

- Integrated regulators, Central Banks, Financial Stability Regulators: Topics range from monetary policy to state of markets, to financial stability, to micro/macro prudential supervision.
  - How financial institutions impact leverage, liquidity transformation and other systemic risk
- Reference insurance sector potential impact on systemic risks, but focus on the banking sector
Broad Themes

- “Low For Long”
- Interconnectivity
- Uncertainty: New Players, Technology
- Liquidity
- Insurance Sector Reports
- Cybersecurity
- Procyclicality
Tools: Good Data

• Consistently reported, timely, automated
  – Insurance Data
    • YoY trends in investment and underwriting profitability, capital adequacy, leverage, concentrations
    • Investment allocation, business lines, guarantees, liability liquidity features, financial counterparties, NTNI activities
  – Economic and financial market data
Stress Testing

- Assess impact on the insurance industry of common exposures to financial market risks
- Assess impact on financial system of extreme events impacting a subset of the insurance sector
- Stresses
  - Regulator prescribed, others allow more firm specific flexibility.
  - Single, double and multiple hit scenarios being tested
  - Consider both direct and knock on impacts
Micro Tools, Macro Purposes

- Regulatory Capt’l
  - pro-cyclical, market risks
- Reporting requirements
- Expanded Authorities
  - Limit or separate NTNI
  - Pro-cyclical Buffers
  - Limit dividends, intra group cash flows
- ORSA
  - horizontal view
- Information sharing
- Recovery, resolution and protection schemes
IAIS Role

- Annual Reports
  - Global Insurance Market Report (GIMAR) which discusses the global insurance sector from a supervisory perspective
  - Key Insurance Risks and Trends (KIRT) Survey
- ICS, G SII Exercise & Policy Measures
- Insurance Core Principle (ICP) #24: Macro prudential Surveillance and Insurance Supervision
US Approaches: Financial Stability and Macro Prudential Surveillance
Financial Stability

• Primary Goals of NAIC Solvency Framework
  – Reduce the Likelihood of Insurer Failure
  – Maximize Amount of Assets Available to Pay Policyholders in the Event of a Failure

• Refining/Improving Group Oversight
  – ORSA Filings, Form F, Group Capital Calculation

• Micro-prudential Regulation Greatly Contributes to Financial Stability (Helps Prevent Distress and Contagion, Both Within and Outside the Group)
Macroprudential Regulation

• Financial Crisis Prompted a Macroprudential Focus
  – Basel III Counter Cyclical Buffers and Tighter Capital Requirements and Leverage Caps
  – SIFI Designation for Nonbank Financial Entities
  – Monitoring of Areas of Risk (e.g., Securities Lending Data Calls)
US Financial Stability Reports

• FSOC Annual Report, OFR Fin. Stability Report
  – Low U.S. and Global Interest Rates
    • Reaching for Yield and Increased Leverage
    • Challenges to Life Insurers (Guaranteed products)
  – Cybersecurity
  – Asset Management Products/Activities
  – Central Counterparties
  – Data Gaps (including Captives issues)
NAIC Macroprudential Monitoring

• Still Focus on Primary Goals of Solvency
  – Peer Review Process of Financial Analysis WG
  – Industry Snapshots, Tool Results and Risk Alerts
  – Capital Markets Reports, Hot Spots, Newsletters
  – Chief Financial Regulator Forum
  – Ad Hoc Queries Responding to Events (e.g., Brexit)
  – Net Spread Over Guaranteed Interest Rate Study
• Results Used by Regulators for Individual Insurers/Groups, to Modify NAIC Guidance
Should NAIC Be Doing More?

• Traditional Argument Is No, Since State Insurance Regulators Have Historically Prioritized Policyholder Protection Over Broader Market Regulation

• Is There A Middle Ground Where NAIC Can Maintain That Priority But Add Tools To Address Macroprudential Regulatory Concerns, e.g. Through Enhanced Monitoring and Reporting?

• Should This Task Force Review and Provide Summary Reports On The Various NAIC Macroprudential Monitoring Activities, And Consider Potential Enhancements?