

Equity Markets' Volatility and U.S. Insurance Industry Exposure (9/02/2015)

Stocks around the world continued to be volatile as September began, on the heels of their worst month in more than three years. Driving the sell-off were continuing concerns that China's slowdown will weigh on the global economy, along with investor uncertainty with regard to the timing and magnitude of an anticipated increase in interest rates by the Federal Reserve. Coming off a steep decline in August, the Standard & Poor's (S&P) 500 Index fell 2.96% to 1,913.85 on Sept. 1, the third-worst drop this year, possibly setting a sour tone for September — historically the worst month of the year, in which the index has fallen 1.1% on average going back to 1927 — although stocks staged a partial rebound in the following session. Equities in Asia also were volatile, as the Shanghai Composite index dropped nearly 5% intraday after manufacturing reports pointed to a deepening Chinese economic slowdown, but then recovered on news of additional government intervention.

Table 1 shows the recent performance of major stock markets around the world, as measured by benchmark indices. The data show that all major markets are in a so-called correction, typically defined as a decline of 10% or more from their prior peak, except the U.S., which has been wavering near the edge of correction territory. Further, the data show that stocks in Hong Kong and mainland China are down 26% and 39%, respectively, from their prior peaks, signifying bear markets (typically a 20% or greater decline).

World Stock Market Indices' Performance as of Sept. 2, 2015

Index	QTD	YTD	1 yr.	3 yr.	Peak to			
					Aug. 2015 Trough	From Peak to Date	Peak Date	
Americas								
S&P 500(U.S.)	-5.5%	-5.3%	-2.7%	38.6%	-12.5%	-8.7%	5/20/2015	
S&P TSX Composite(Can.)	-6.9%	-7.4%	-13.3%	13.4%	-19.0%	-13.6%	9/3/2014	
Europe								
Financial Times 100(U.K.)	-6.7%	-7.4%	-10.9%	6.5%	-19.0%	-14.6%	4/27/2015	
DAX(Eur./Ger.)	-8.2%	2.5%	5.7%	44.1%	-24.6%	-18.9%	4/10/2015	
Euro Stoxx 600(Eur.)	-9.5%	0.7%	0.6%	29.6%	-20.0%	-16.9%	4/15/2015	
Asia								
Nikkei 225(Jap.)	-10.6%	3.7%	15.5%	104.7%	-15.5%	-13.6%	6/24/2015	
Hang Seng Index(H.K.)	-19.3%	-10.3%	-14.4%	8.7%	-27.0%	-25.9%	4/27/2015	
Shanghai Composite(China)	-26.1%	-2.3%	39.5%	54.3%	-44.9%	-39.0%	6/12/2015	

Because most U.S. insurers' common stock holdings are U.S.-based, it is reasonable to estimate the potential mark-to-market impact of the stock market decline on U.S. insurers' capital and surplus using the 12.5% peak-to-trough decline in the S&P 500 Index. Table 2 shows the unaffiliated common stock exposure of U.S. insurers in relation to their total capital and surplus as of year-end 2014 and as of June 30, 2015. It also shows the hypothetical

percentage impact on capital and surplus of the decline in stocks from their peak to the August market trough. Because insurers' aggregate exposure to common stocks is relatively modest compared to other assets such as bonds, the expected impact of a significant stock market sell-off on insurers' capital and surplus is modest, even in the case of property/casualty (P/C) insurers, which are the most heavily exposed to stocks. The common stock exposure of individual insurance companies relative to total capital and surplus varies greatly, however, depending on investment allocations and capital structure; it significantly exceeds total capital and surplus in a relatively small number of cases.

U.S. Insurers' Common Stock Exposure Relative to Total Capital and Surplus

U.S. \$ mil., as of 12/31/14	Fraternal	Life	P/C	Health	Title	Total
Unaffiliated Common Stock	2,774	29,506	245,717	8,537	639	287,174
Total Capital and Surplus	12,580	429,509	862,810	116,419	4,251	1,425,570
Unaffiliated Common Stock as Percentage of Total Capital and Surplus	22.1%	6.9%	28.5%	7.3%	15.0%	20.1%
U.S. \$ mil., as of 6/30/15	Fraternal	Life	P/C	Health	Title	Total
Unaffiliated Common Stock	2,853	27,777	249,369	8,516	800	289,314
Total Capital and Surplus	13,034	433,540	865,254	116,007	4,451	1,432,287
Unaffiliated Common Stock as Percentage of Total Capital and Surplus	21.9%	6.4%	28.8%	7.3%	18.0%	20.2%
<i>Estimated Mark-to-Market Impact on Total Capital and Surplus of a 12.5% Decline in Market Value of Unaffiliated Common Stock</i>	-2.7%	-0.8%	-3.6%	-0.9%	-2.2%	-2.5%

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