Association of British Insurers

ABI

Activities-based approach to systemic risk

IAIS Stakeholder Meeting, London

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1 February 2018

UK Insurance Industry and the ABI

The UK Insurance Industry

The UK insurance and long-term savings industry is the fourth largest in the world. It helps Britain thrive in its global role, adding £40 billion a year to the UK economy, managing investments of over £1.7 trillion, and paying nearly £12bn in taxes to the Government. It employs over 300,000 individuals right across the UK, of which around a third are employed directly by providers with the remainder in auxiliary services such as broking.

Insurance helps individuals and businesses protect themselves against the everyday risks they face, enabling people to own homes, travel overseas, provide for a financially secure future and run businesses. Insurance underpins a healthy and prosperous society, enabling businesses and individuals to thrive, safe in the knowledge that problems can be handled and risks carefully managed.

The ABI

The Association of British Insurers is the voice of the UK's world-leading insurance and long-term savings industry. A productive, inclusive and thriving sector, we are an industry that provides peace of mind to households and businesses across the UK and powers the growth of local and regional economies by enabling trade, risk taking, investment and innovation.

Founded in 1985, the ABI represents around 250 member companies, including most household names and specialist providers. The ABI's role is to:

- get the right people together to help inform public policy debates, engaging with politicians, policymakers and regulators at home and abroad.
- be the public voice of the sector, promoting the value of its products and highlighting its importance to the wider economy.
- help encourage consumer understanding of the sector's products and practices.
- support a competitive insurance industry, in the UK and overseas.

ABI

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General comments on the ABA

- ABI welcomes the IAIS' development of ABA. These are our preliminary views on the issues raised in the consultation.
- Broad interpretation of 'activity', in terms of risk exposures, is appropriate
- Materiality of the potential systemic risk is also important
- Causative links between exposures and transmission channels must be established
- In continuing to develop the ICS, IAIS should ensure it does not create incentives for procyclical behaviour, e.g. MOCE

‘Tsunami’ and ‘domino’ views

- IAIS outlines ‘tsunami’ and ‘domino’ views of risk:
  - *‘Tsunami’ – collective risk exposures of solvent firms may propagate or amplify shocks to the rest of the financial system and the real economy*
  - *‘Domino’ – failure of individual insurers has potential knock-on effects*
- ABA has the potential to address risk under both views
- Scope of ABA should not be limited to the ‘tsunami’ view, as either view could have a common underlying cause
- IAIS should take a holistic approach
  - Recognise interrelationship between liquidity risk and macroeconomic exposures
  - Consider where risks may be double-counted, or where there may be gaps
  - Include counterparty exposures which are relevant under ABA

Liquidity risk exposures

- We agree with the IAIS' assessment that insurers' liquidity risk is generally well-contained
- Insurers' liquidity risk tends to be overstated
  - Illiquid assets tend to be held to maturity against illiquid liabilities
  - Insurers are large holders of liquid assets
  - Factors such as leverage or maturity transformation are likely to be limited
  - Insurers' policies are not deposit accounts, and there are many disincentives to surrender
- Transmission channels need to be clarified:
  - Asset liquidation

Macroeconomic risk exposures

- Closely related to liquidity risk, as macroeconomic factors may lead to asset liquidation
- Factors such as leverage or maturity transformation tend to be limited
- Herding and procyclicality should be considered as part of macroeconomic exposures, rather than separately
- Transmission channels need to be clarified –
  - Asset liquidation
  - Counterparties

Policy measures

- Policy measures need to be proportionate, addressing material risk posed by potentially systemic activities to the global financial system as a whole
  - Welcome recognition of existing qualitative measures that ensure risk is managed and mitigated in a forward-looking manner
  - Qualitative measures are appropriate given long-term nature of insurance, which allows time to respond to emerging risks
  - Stress testing as a means to assessing macroeconomic exposure is sensible
- Welcome recognition of policy measures introduced by other international standard-setters

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