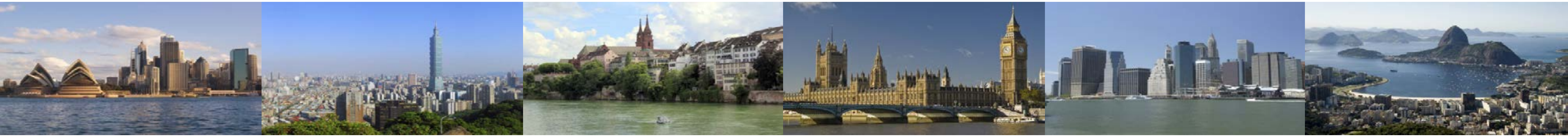
IAIS
INTERNATIONAL ASSOCIATION OF
INSURANCE SUPERVISORS

Update on Holistic Systemic Risk Framework

26 July 2018
Global Seminar
Moscow



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Introduction

- In February 2017, the IAIS announced a work plan to develop a holistic framework for assessing and mitigating systemic risk in the insurance sector at the global level, including three work streams:
  - Development of an Activities-Based Approach to mitigate systemic risk in insurance through the identification, and (further) development as needed, of relevant macroprudential policy measures;
  - Addressing cross-sectoral aspects in systemic risk assessment; and
  - Revising the Entities-Based Approach, namely the Global Systemically Important Insurers (G-SII) assessment methodology.
- In December 2017, the IAIS launched an interim consultation, focussing on the first work stream only.
- Today we will update on progress made on the development of the 2018 consultation document, which will bring all these strands of work together and propose a holistic framework.

Sources of systemic risk (1)

- Systemic risk may arise from:
  - The **collective activities / exposures** of insurers at a sector-wide level; or
  - the distress or disorderly failure of an individual insurer
- Systemic risk is **time-varying** and depends on, for instance, the state of the overall economy, the relative size of the activities and the overall resilience of financial markets.
- The next slide summarises the main vulnerabilities and exacerbating factors that are considered relevant to assess systemic risk as well as the main transmission channels through which they can potentially lead to systemic impacts.

Sources of systemic risk (2)

VULNERABILITIES and EXACERBATING FACTORS

- LIQUIDITY RISK
- MACRO ECONOMIC EXPOSURE
- COUNTERPARTY EXPOSURE
- SUBSTITUTABILITY
- OTHER

TRANSMISSION CHANNEL (depending on risk)	SYSTEMIC IMPACT (depending on risk)
ASSET LIQUIDATION	• Exacerbating market movements • Contributing to asset price volatility
EXPOSURE CHANNEL	• Transferring losses to other market participants • Constraining funding or liquidity to financial institutions
CRITICAL FUNCTION	• Interruption of insurance services to real economy or financial institutions

Example with respect to liquidity risk:

- **Vulnerability and materialisation of risk**: a sudden and significant change in the underlying value of a derivative that leads to increased collateral calls thereby increasing the liquidity risk of the insurer(s)
- **Transmission channel**: the subsequent reaction by the insurer(s) in the form of fire sales, that then has the potential to exacerbate market movements

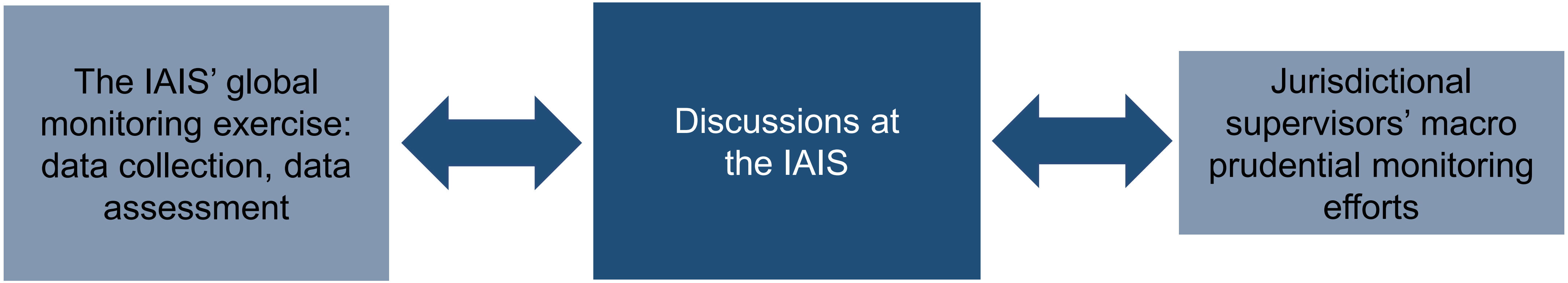
Key elements of holistic systemic risk framework

- Aim of the framework is to be able to **identify** the build-up of potential systemic risks, **prevent** systemic risk from materialising and, lastly, to **mitigate** these risks should they materialise anyway.
- The essential elements of a holistic systemic risk framework consist of three pillars:
  - **Continued global monitoring exercise by the IAIS** of potential systemic risk, involving data collection and cross-sectoral analysis to enable benchmarking and trend analysis;
  - **Application of supervisory policy measures** aimed at holistically mitigating potential systemic risk; and
  - **Robust implementation assessment by the IAIS** to ensure that policy measures are consistently applied on a global level.

Global Monitoring exercise

IAIS monitoring and coordination with jurisdictional monitoring

- An important element of the holistic framework, will be a strengthening of the feedback loop between global IAIS monitoring of systemic risk, with a focus on cross-jurisdictional issues, and macroprudential monitoring by local supervisors
  - IAIS global monitoring is complemented by findings from supervisors
  - IAIS global monitoring may provide a useful cross-jurisdictional perspective for supervisors



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Macroprudential policy measures

Macroprudential monitoring, on-going supervision and crisis management

The set of policy measures is likely to consist of three components with an enhanced macroprudential focus:

1) **Macro prudential monitoring and assessment** is considered the starting point for a supervisory approach to mitigating systemic risk and serves to inform the appropriate choice of corrective measures and the adequacy of preventive measures.

2) **Ongoing supervision**, including:
   - Existing and new policy measures, which are designed to address liquidity risk, macroeconomic exposure and counterparty risk
   - Measures that are expected to be applied only when the situation calls for additional supervisory action

3) **Crisis management**: can help reduce the likelihood and impact of a disorderly failure of an insurer or collective distress of several insurers. These policy measures are already included in the Overall ComFrame material, and include recovery and resolution planning, as well as the establishment of crisis management groups

4. Next steps and timeline

Timeline until finalisation / adoption

Date	Decision point
Late 2018	• Launch of consultation
First quarter 2019	• End of consultation period (exact date dependent on launch of consultation)
June 2019	• Consultation on revised ICPs and ComFrame
November 2019	• Holistic Systemic Risk Framework and revised ICPs and ComFrame adopted
2020	• New holistic systemic risk regime in place

Important aspects on which input is particularly welcome

- Sources of systemic risk
- Design of the holistic framework and role of global monitoring
- Scope and proportionality in the application of policy measures