Systemic risk from insurance product features – Executive Summary

Background

This Executive Summary provides the key highlights from the Systemic Risk from Insurance Product Features (SRIPF) paper published by the International Association of Insurance Supervisors (IAIS) on 16 June 2016.

Significance of the paper

This paper describes the conceptual thinking on how insurance product features can give rise to systemic risk. Because of this, it has a direct impact on how global systemically important insurers (G-SIIs) are identified. The paper translates the features of insurance products into indicators that the IAIS uses in its methodology to identify G-SIIs. The paper does not cover the other systemic risk drivers for insurance.

“NTNI” label

The term “NTNI”, which means “non-traditional non-insurance”, has become a commonly used term since it was first mentioned in the G-SII policy measures and assessment methodology papers published by the IAIS in July 2013. With the new approach on SRIPF, the IAIS has decided to stop using the NTNI label, as it was found to be confusing and there was some conceptual overlap between NTNI and “interconnectedness”, which was another category of indicator used to identify G-SIIs.

Key concept

Insurance products that have features that expose insurers to substantial:

1. macroeconomic risk (through the exposure transmission channel); and/or
2. liquidity risk (through the asset liquidation transmission channel)

contribute to their higher systemic relevance.
Examples of product features that can give rise to systemic risk

<table>
<thead>
<tr>
<th>Product feature</th>
<th>Risk</th>
<th>Transmission channel</th>
<th>Potential systemic risk impact</th>
</tr>
</thead>
<tbody>
<tr>
<td>Guaranteed investment returns on unit-linked insurance policies¹</td>
<td>Macroeconomic risk</td>
<td>Exposure</td>
<td>Insurers that offer such products have a common exposure to macroeconomic risk. Insurers often use derivatives to manage the asset-liability profile of such products. A sudden fall in investment returns will affect multiple insurers and their derivatives counterparties.</td>
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<tr>
<td>Immediate payment of surrender values with low penalties</td>
<td>Liquidity risk</td>
<td>Asset liquidation</td>
<td>If there is mass policy cancellation, insurers would be forced to liquidate their assets quickly, depressing asset prices and increasing asset price volatility. This would disrupt trading and funding in key markets, potentially triggering losses for other firms with similar asset holdings.</td>
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</tbody>
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¹ Unit-linked insurance policies offer benefits that are directly linked to the performance of the underlying investment fund(s).