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INITIATIVES TO ADDRESS DATA GAPS REVEALED BY THE FINANCIAL CRISIS:

ECB STATISTICS ON

INSURANCE CORPORATIONS AND PENSION FUNDS

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Abstract

Non-bank financial intermediaries have rapidly increased their importance in the euro area over past 15 years. Among them, two sub-sectors play an important role reflected by the steady growth of their balance sheet totals, namely the investment funds and the insurance corporations and pension funds (ICPF). Both are now covered by enhanced statistics. The paper presents the statistics for the latter sub-sector which the European Central Bank (ECB) has developed in close cooperation with the euro area National Central Banks. Given the ICPF crucial role in portfolio decisions of households and the interaction between insurers and pension funds, banks, other financial intermediaries, and more broadly financial markets, the importance of more detailed and timely data for this sector has risen. These statistics are being developed under a "short-term approach" based on available sources, mostly supervisory authorities, i.e. without implementing a new data collection from reporting agents, with the main objective to set up a framework for timely quarterly estimates of euro area statistics. For its further development, and in the light of increasing user needs in particular for financial stability analysis purposes, the ECB cooperates closely with the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) in order to ensure consistency of future reporting requirements under Solvency II and to minimise reporting burden.

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Introduction

Non-bank financial intermediaries have rapidly increased their importance in the euro area over past 15 years. Among them, two sub-sectors play an important role reflected by the steady growth of their balance sheet totals, namely the investment funds and the insurance corporations and pension funds (ICPF). Both sectors are now covered by enhanced statistics. The former is described in an ECB Monthly Bulletin article (please refer to ECB, 2010a). The paper presents the statistics for the latter sub-sector which the ECB has developed in close cooperation with the euro area National Central Banks (NCBs). These statistics are being developed under a "short-term approach" based on available data sources, mostly supervisory authorities, i.e. without implementing a new data collection from reporting agents, and with the main objective to set up a framework for timely quarterly estimates of euro area statistics.

1. Importance of the euro area Insurance Corporations and Pension Funds

Euro area insurance corporation and pension funds (ICPF) are important investors in the financial markets. They account for 12% of the financial assets of the euro area financial sector (end-2009 data) and have significant links and interconnections with the different sectors of the euro area economy. In particular, ICPF hold 18% of the debt securities issued by euro area general government and 28% of the mutual fund shares issued by euro area investment funds. In parallel to this active role as providers of financing, euro area ICPF liabilities are one of the main components of euro area households' financial wealth (accounting for 30% of the total), competing with deposits in attracting households investments. In addition, their role as providers of insurance is essential for the smooth functioning of the euro area economy. ICPF balance sheet data are, moreover, used for different types of analysis, namely monetary and financial stability analysis.

Concerning monetary analysis, ICPF directly hold monetary assets, but these account for only a small portion of the sector's total financial assets and of monetary financial institutions (MFI) liabilities composing monetary aggregates. ICPF play an important role as a counterpart to the flows into and out MFI balance sheet positions and, as mentioned, compete with MFI in attracting savings originating from households. ICPF data are also relevant for the analysis of the economic activity and the monetary transmission mechanism, for instance through ICPF investments in securities, their impact on the financing conditions of the non-financial private sector and, also as an important and increasing part of the wealth portfolio of the household sector.

From a financial stability perspective, the role of ICPF as investors in financial markets, the growing links and interconnections with the financial sector and their relevance as providers of insurance (for households and firms) make the new statistics relevant for the assessment of the stability of the financial system[1]. As long-term investors, ICPF are well placed to play a

[1] For further details please refer to ECB (2009) and ECB (2010b).

stabilising role with lower levels of liquidity risk than banks. At the same time, possible under-funding by ICPF may affect the real economy in times of adverse asset price developments. The same is true in the event of low interest rates, which are applied to discount future liabilities. Furthermore, the sector is also relevant for the monitoring of systemic risk, given the growing interaction with financial markets and financial intermediaries, and the special role of reinsurance. Finally, concentration has grown over time in the insurance sector and financial conglomerates have emerged.

2. New Insurance Corporations and Pension Funds statistics

Given the scarcity of timely, harmonised and comprehensive data on euro area ICPF,[2] the ECB launched at the end of 2007 an initiative to improve the statistical coverage of the ICPF sector, as part of a broader strategy to enhance the statistical coverage of the non-bank financial intermediaries sectors. A task force was mandated to consider compilation issues, in particular to further define a reporting scheme for ICPF statistics from NCBs to the ECB relying on available national data. User requirements from monetary policy and financial stability analyses were taken into account. In parallel, ICPF statistics were also geared towards enhancing the input (as a 'building block' for the ICPF sector) to the compilation of euro area accounts. These accounts are an integrated statistical framework that provides a systematic description of the euro area economy for the financial and non-financial sectors.

For the enhanced statistics, NCBs transmit to the ECB quarterly data on ICPF assets and liabilities for the total sector and, if available, broken down into the two sub-sectors insurance corporations and pension funds. The required data cover end-quarter stocks as well as quarterly transactions (change in stocks adjusted for reclassifications, exchange rate changes and price revaluations) and should be reported to the ECB by 85 calendar days after the reporting period[3]. There are some requirements that may be met on an annual basis if no quarterly data are available. NCBs may report available annual data or best estimates on splits of (i) the balance sheet by sub-sector; (ii) net equity of households in insurance technical reserves (i.e. unit-linked and non-unit-linked business); and (iii) net equity of households in pensions reserves (i.e. defined contribution, defined benefit and hybrid schemes). The reporting scheme showing all the series to be provided by the NCBs to the ECB is presented in Annex I.

National statistics are provided by the NCBs to the ECB on a best efforts basis and may include estimates. The main national data sources for outstanding amounts are supervisory data, complemented by information directly reported by ICPFs. Financial accounts estimates are also used to support the compilation of ICPF statistics. These main sources are

[2] Data on ICPFs have been part of euro area accounts since their publication in June 2006 for annual accounts and in June 2007 for quarterly accounts (see ECB Monthly Bulletin, Statistics section, Table 3.5)

[3] This timeliness will move to 80 calendar days by end-2010, to align with tighter deadlines for the compilation of euro area accounts.

complemented with other NCBs' statistics including MFI balance sheets, securities issues statistics or balance of payments statistics, mostly to compile net transactions. The ICPF statistics are based on a host approach[4], at market value (except for deposits and loans which are at nominal value) and on a non-consolidated (solo accounts) basis.

Since October 2008, the ESCB has worked on implementing the new ICPF statistics and particular attention has been given to the promotion of a sound methodological framework. The treatment of reinsurance, for example, was discussed to ensure an effective and harmonised treatment across euro area countries. The derivation of transactions, one of the major difficulties of NCBs compilers and was the main topic of a workshop held in October 2009. Another workshop is scheduled to take place in October 2010, and will follow-up on the derivation of transactions and to discuss data quality issues.

The quality of the data transmitted is regularly monitored through internal-to the ECB consistency checks. In addition to this, a cross-checking with alternative sources was performed, in order to assess the consistency of the ICPF dataset and statistics on, other financial sub-sectors (MFI, investment funds, money market funds, financial vehicle corporations), securities issues and euro area accounts. The results for outstanding amounts data were, in general, positive and some of the detected discrepancies were solved by NCBs. A similar exercise is being conducted for transactions.

The quality of the euro area results depends on the coverage achieved at the national level. Concerning outstanding amounts, the coverage of the euro area instrument totals by national data is close to 100%. For the compilation of euro area aggregates, estimates by the ECB encompass missing breakdowns for residency, sector counterparts or maturity. Regarding missing residency or sector counterparts, the main data gaps are in holdings of securities, quoted shares and unquoted shares and other equity, where, respectively 36%, 33% and 84% of the counterpart allocation have to be estimated by the ECB. Concerning the missing maturity breakdown, the gaps relate to the longer-term maturities. Only the maturity breakdown of deposits is estimated by the ECB (the amounts missing account for 10% of the instrument total) since, for the other instruments, the gaps are still too large.

In respect of the data on transactions, the coverage is lower in comparison to reported stock data, while it has substantially improved since the workshop held in October 2009. NCBs rely more heavily on estimates for the compilation of transactions than for the compilation of stocks. Estimates are fine-tuned and the resulting data are of an improved quality.

A regular publication of ICPF quarterly stock data is tentatively planned to start in mid 2011.

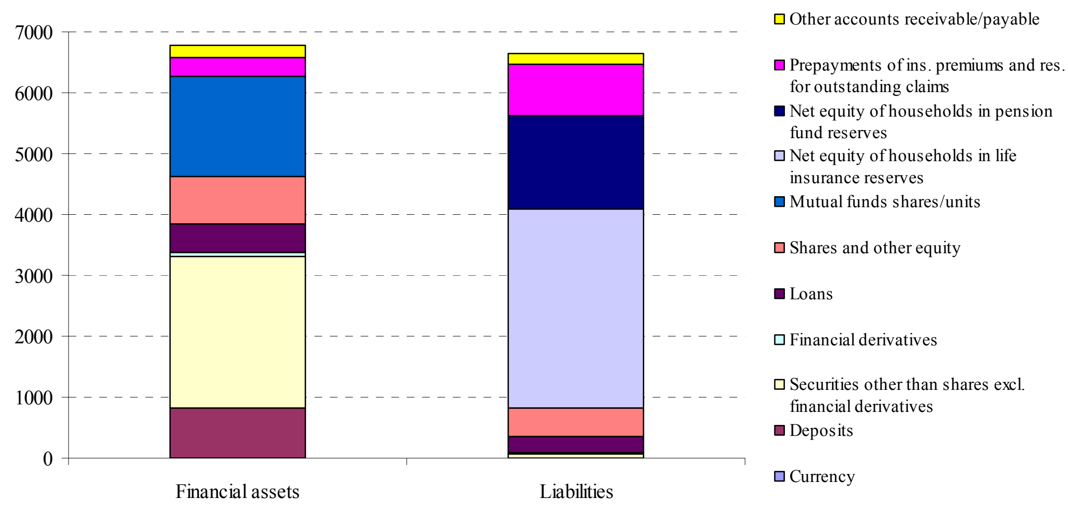
[4] Macroeconomic statistics following the System of National Accounts and the European System of Accounts concepts are based on the host approach (residency of individual institutional units, e.g. Citibank Germany is a German resident)) while supervisory data are based on home approach (e.g. Citibank Germany is consolidated with its mother company).

3. First results on the data[5]

Euro area ICPF invest mainly in securities other than shares, which account for 37% of their financial assets (see chart 1). The importance of mutual funds shares has increased through time as the investments in shares and other equity were reduced (the weight of each instrument in the ICPF balance sheet is, respectively, 24% and 12%). Deposits account for 12% of total financial assets. On the liabilities side, insurance technical reserves account, as expected, for a large share of the liabilities (85% of the total). These reserves may be further split by type of business: the shares of life insurance reserves, pension funds reserves and non-life insurance reserves are, respectively, 58%, 27% and 15%.

Chart 2 presents the euro area ICPF balance sheet by counterpart sectors. Euro area counterparts account for 86% of euro area ICPF financial assets. In particular, other financial intermediaries of the euro area (where investment funds are included) represent 28% of total financial assets, mainly as issuers of mutual funds shares. Euro area MFI and euro area general government are further important counterparts (22% and 18% of total financial assets) as issuers of securities and, in the case of MFI, also deposits. On the liabilities side, euro area households have the largest share (78% of total liabilities) as a counterpart for life insurance and pension reserves.

Chart 1 – Euro area ICPF balance sheet structure – by instrument (2010Q1, EUR bn)



Source: ECB

[5] This section is based on the latest stock data available in August 2010, for reference period 2010Q1.

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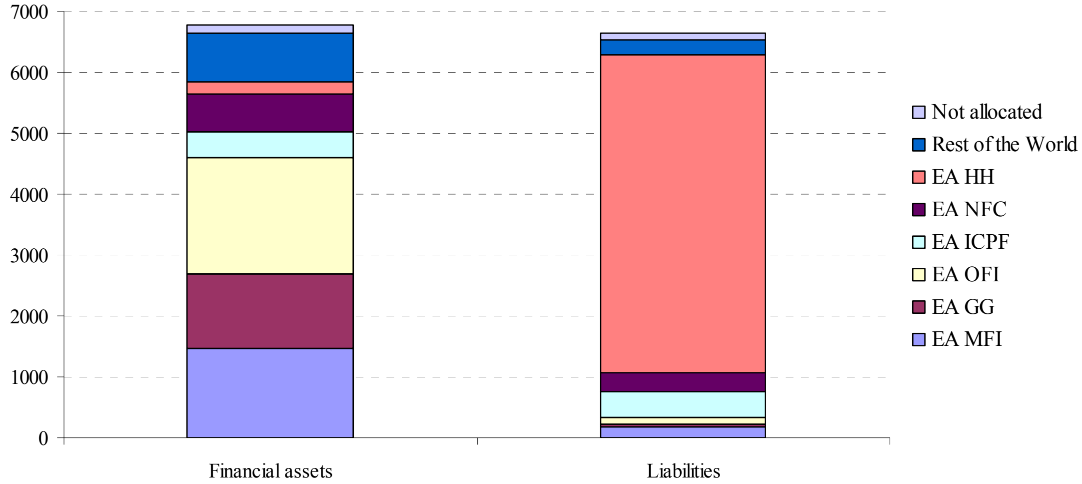
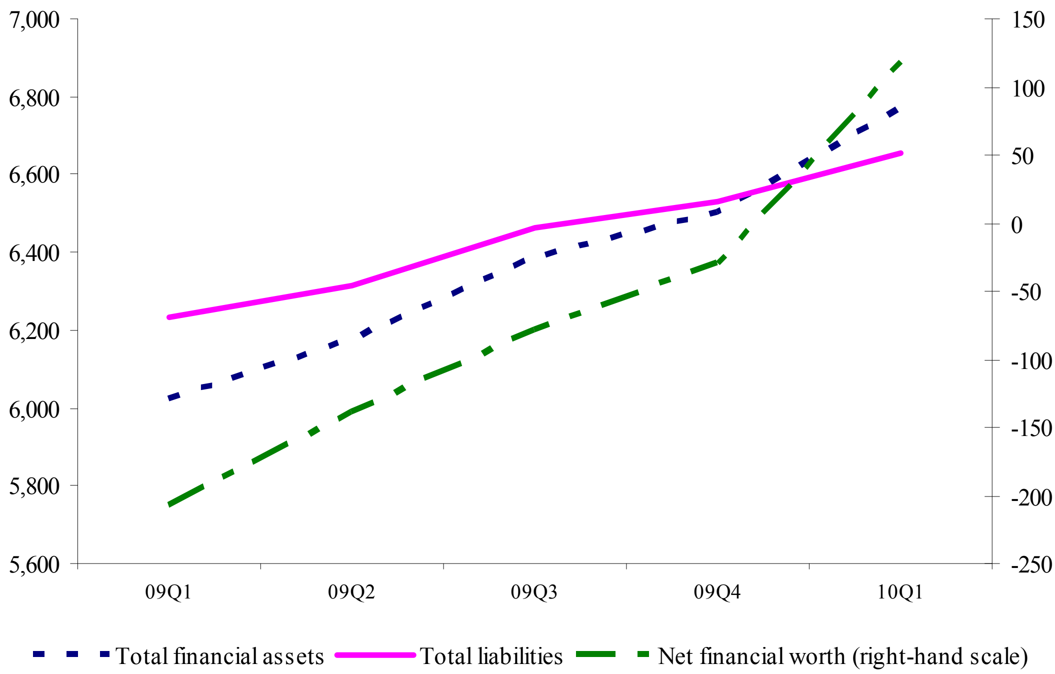
Chart 2 - Euro area ICPF balance sheet structure – by counterpart sector (2010Q1, EUR bn)



Source: ECB

Chart 3 - Euro area ICPF balance sheet developments (2009Q1-2010Q1, EUR bn)



Source: ECB

According to the available results, the financial position of euro area ICPF has been improving through 2009 (chart 3) and net financial worth (which measures the difference between financial assets and liabilities) reached a positive value in 2010Q1 of EUR 118 billion. During the period 2009Q1 to 2010Q1, financial assets increased 12% (EUR 748 billion), mainly due to mutual funds shares/units[6] (which increased by EUR 501 billion, 45% of the initial stock) and, also, securities other than shares (EUR 218 billion, 10% of the initial stock) against euro area counterparts, in particular general government, MFI and other financial intermediaries (respectively, EUR 127, 42 and 55 billion). These positive developments were partially compensated by an increase of 7% in liabilities incurred (EUR 422 billion) in particular related to developments on life insurance products.

Regarding the sub-sector split, insurance corporations account for 80% of the total financial assets of the ICPF sector. The relative low weight of pension funds (which have shares in total ICPF that vary widely across countries) reflects institutional differences across countries. First, only autonomous pension funds[7] are included in the ICPF statistics; thus, countries where private pension schemes are mainly provided through non-autonomous pension funds, linked in particular to non-financial corporations and MFI, have a smaller pension funds sub-sector according to the ICPF statistics. Furthermore, countries where social security is particularly developed tend to have a smaller pension funds sub-sector.

Furthermore, despite similarities between insurers' activities (namely, life insurance) and pension funds activities, their investment policies are different. Insurance corporations invest mainly in securities (40% out of total financial assets) followed by mutual funds shares (20% out of total financial assets). Conversely, for pension funds, mutual funds shares represent the main important investment class (40% out of total financial assets) and securities other than shares account for 20% out of total financial assets.

4. Challenges ahead

The ICPF stock data much improve the current situation on ICPF data availability for the euro area: the combination of timeliness, frequency, instrument detail and geographic and sector counterpart breakdown allows different users to enhance their analysis. Some further improvements for outstanding amounts and, for selected transactions data are underway. Nevertheless, further improvements are needed, in particular due to the growing importance

[6] Partially related to the reorganization of the investment strategies of some large PF that replaced their investments in shares and securities by investments in mutual funds shares/units.

[7] Apart from insurers (insurance and reinsurance) the statistics cover *autonomous* pension funds, i.e. funds that have autonomy of decision and keep a complete set of accounts. Non-autonomous pension funds set up by, for example, credit institutions or non-financial corporations are not covered since they are not separate institutional units.

of the sector for financial stability analyses in view of the European Systemic Risk Board's and of ECB's own financial stability analysis (e.g. the Financial Stability Review).

The main new challenges ahead to the ICPF statistics are:

i. Separate balance sheets for Insurance corporations (IC) and Pension funds (PF) sub-sectors

Aggregate data for the ICPF sector can hide important differences across types of institutions. Sector-wide assessments need, therefore, to be complemented with, in particular, an analysis of sub-sectors, allowing for a more accurate and detailed analysis. Initially, in the context of ICPF short-term approach, the split between insurance corporations and pension funds sub-sectors data was only requested at annual frequency and with a longer time lag (9 months after the reporting period). Moreover, the analysis of data for euro area countries (the majority of countries already report these data on a quarterly basis) showed that the two sub-sectors have different investment behaviours and their respective country's distribution is uneven. Following user requests, the ECB reviewed the available national data for the split of insurance corporations and pension funds sub-sectors and compiled euro area aggregates for stock data, covering, for the time being, the main balance sheet items (namely, instrument totals). Further improvements on national data will help enhance the euro area aggregates for the two distinct sub-sectors.

ii. Statistics for all EU Member States and EU counterparts country breakdown

The ECB's future tasks in supporting the ESRB will be to help assessing systemic risks for the entire European Union (EU27) as well as individual EU countries. Hence, ICPF statistics for non-euro area EU countries will be needed[8]. In addition, the current geographical breakdown would have to include also non-euro area EU countries. The EU counterparts (euro area and non-euro area) may have to be split by country in the future.

iii. Balance sheets by type of business (non-life, life – unit-linked and non-unit-linked, reinsurance, defined benefit pensions and defined contribution pensions)

The different types of business (non-life, life – unit-linked and non-unit-linked, reinsurance, defined benefit pensions and defined contribution pensions) entail different investment policies, different risk profiles and different money holding behaviours and are, therefore, relevant for analysts. The requirement was not included in the ICPF short-term approach but will need to be re-considered in a steady state approach.

iv. Further improvement of timeliness

[8] Some EU non-euro area countries have already developed (or are currently developing) these statistics.

For the timely use of the ICPF statistics as input to the euro area accounts, work is underway to provide a regular NCB data transmission at 80 calendar days after the reference period. It is expected that this objective can be met from 2011 onwards. A demanding challenge for a steady-state approach would be to fulfil the users' request for monetary analysis. With a view to enhancing the value for analysis and related communication, different (and complementary) sets of statistics need to be analysed together and reported in the same briefing material. This implies that ICPF core aggregates would be expected to become available with a timeliness around 50 calendar days after the reference period. This option of a timely provision of ICPF data will be considered in the longer-term.

Other relevant improvements would be the distinction of investments between, for example, "*Available for sale*" and "*Held to maturity*", since the impact on the ICPF' assets of valuation changes in investments held can differ substantially depending on how they are accounted for on their balance sheets. In addition, group level information and intra-group transactions (complementing the available solo data) and information on the residual maturity (in addition to the original maturity approach currently followed) would be needed to assess risks confronting groups as a whole and liquidity risks.

v. Integration of statistical and supervisory reporting

Following the agreement between the ECB and NCBs, a close cooperation with the European Level-3 Committees (and future European Supervisory Authorities) has been pursued and deepened, in particular for the ICPF sector with the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS). The CEIOPS is developing under Solvency II Directive, adopted in 2009, new supervisory reporting templates for insurance undertakings.[9] The templates are seen as a key element to meet user needs, i.e. both the expected requirements of the ESRB and of financial stability analysis, as well as those for monetary policy purposes, as the supervisory templates cover reporting of solo and consolidated accounts (and investments). In contrast to the low frequency, insufficient timeliness and lack of detail and harmonisation of the current supervisory data, ICPF statistics are expected to much improve with the new Solvency II requirements. For example, the current draft templates contain a security-by-security reporting, with a quarterly frequency and a timeliness of 4 weeks to 6 weeks. Solvency II reporting may also provide a significant part of the statistical data needed for the requirements outlined above, in particular (a) the separate balance sheets for insurance corporations and pension funds sub-sectors, (b) separate data for *all* EU countries, (c) separate data for EU country counterparts and (d) some distinctions by type of

[9] These are scheduled to be formally enforced in early 2011 for implementation in 2012 and first reporting in 2013.

business (e.g. life insurance). Overall, many ECB requirements could be met on the basis of the draft Solvency II templates. In the future, the future EIOPA intends to also work on the Pension Funds Directive in a similar direction. Therefore, in order to minimise the reporting burden for insurance corporations, and in the future for pension funds, and to ensure the best possible consistency of data used by different institutions for analytical purposes, close cooperation between the ECB and CEIOPS (and its successor EIOPA) will continue.

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