

Jorgovanka Tabaković: Current situation and challenges in supervision of the domestic insurance market

Introductory address by Dr Jorgovanka Tabaković, Governor of the National Bank of Serbia, at the Insurance Gathering "Serbian Insurance Days", Aranđelovac, 29 November 2017.

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Dear ladies and gentlemen, esteemed representatives of the insurance industry, state institutions, corporate sector and university, dear international guests,

I have the pleasure of introductory address at this gathering, the first large-scale event fully dedicated to insurance business. First of all, I would like to extend my full support to the organisers' idea to contribute, by this event, to putting insurance business in its rightful place, not only in the country's financial system, but also in the lives of each one of us, as citizens and beneficiaries. This important and yet unjustifiably neglected activity, managed to remain healthy in its core and to continue its slow, but still unstoppable development. Though the pace of that development is not what we, workers in the financial sector, would like it to be, insurance is definitely looking at a bright future. As the Governor of the National Bank of Serbia, the insurance supervisor for already thirteen years, I will briefly recapitulate for you today our vision of insurance business, issues that are topical and pending, and desirable ways to address them, as well as other aspects and challenges of our supervisory work.

Insurance business in Serbia has seen some drastic changes and improvements since the National Bank of Serbia assumed the role of its supervisor. This business is still constantly changing and aligning with the European standards. All entities that failed to meet the criteria of such alignment left the insurance business, making room for new market players, mostly as subsidiaries of internationally recognised insurance undertakings. Therefore, in the last decade the insurance business was very dynamic also in terms of foreign direct investment. Insurance undertakings founded by foreign owners started from very high pecuniary founder's stakes, and with the growth of their business, became also serious investors in government bonds and other financial instruments; not so rarely they even founded their own subsidiaries and invested in real estate construction. Today, the Serbian insurance market comprises seventeen insurance undertakings and four reinsurance undertakings. Six undertakings are engaged in both life and non-life insurance, while four are exclusive life insurers and seven exclusive non-life insurers. In addition to insurance and reinsurance undertakings, the market consists of nineteen banks, seven lessors and one public postal operator, which are licensed for insurance agency. There are also eighty six legal persons engaged in insurance brokerage/agency and ninety four entrepreneurs – insurance agents.

Financial indicators are still modest, if observed in absolute amounts, but it is certainly commendable that all of them have recorded stable growth for a number of years. Thus, total insurance premium in the first half of 2017 equalled RSD 48.8 billion (or EUR 404 million), up by 8.1% relative to the same period last year. The share of non-life insurance in the structure of the premium was 77.5%, while life insurance accounted for 22.5%. Of individual insurance types, the largest share in the total premium was that of motor liability insurance (32%), followed by life insurance (22.5%), property insurance (20.9%) and full coverage motor vehicle insurance (8.5%). The balance sheet total of insurance undertakings increased to RSD 230.9 billion (or EUR 1.9 billion) in mid-2017, up by 10.3% relative to the end of the second quarter a year earlier. Debt securities available for sale made up 44.1% of assets of insurance undertakings, debt securities with fixed income 14.5%, property, plant and equipment 8%, receivables 7.6%, cash and short-term deposits 6%, while debt securities recognised at fair value through profit and loss account made up 3.7%. The liabilities were composed of technical provisions (70.3%) and capital and reserves (20.7%). Insurance undertakings meet the capital adequacy criteria, as stipulated by valid regulations, and are solvent and liquid. In this sense, the insurance market is

stable and capable of servicing liabilities to policyholders, insurance beneficiaries and injured parties.

The regulatory framework for the insurance industry was thoroughly reformed, modernised and upgraded in 2014/15. Since then, the National Bank of Serbia has introduced an entirely new dimension in its supervisory activities given that we prepared the insurance legislation in its entirety, whereby we rounded up the supervision process. Having become aware of such possibilities, as well as of the need to improve insurance regulations and supervision, I personally set up and led a working group that prepared the reform Law on Insurance in 2014, which was adopted by the Serbian Parliament by end-2014 at our proposal. Back then we also received positive opinions on proposed solutions from all relevant stakeholders – the Serbian Government, the European Commission, insurance sector representatives, companies and science workers, and we were even more bound by that to continue on this path. This we did the very following year by adopting a set of bylaws to the Law on Insurance. During the two and a half years of implementation, these regulations yielded numerous positive effects which have been spoken of a good deal, but I would like to use this opportunity to underline that our expectations have been fulfilled, namely that we now have a regulatory framework which has resolved a number of disputable issues, defined mechanisms enabling better protection of users, stimulated investment and the development of new insurance products, raised and accurately defined the capital adequacy criteria, modernised insurance administration systems, as well as ensured better transparency of work, i.e. more fair business conditions in this sector. Everything we have achieved in this manner allows us not only to have a better insurance sector now, but also to build on those foundations and continue with modernisation and alignment with contemporary European standards.

Insurance supervision conducted in the past two and a half years essentially differs from the same activity performed in some earlier periods. This is why I will use this opportunity and present to all of you some specific results of our work, as well as positions on certain issues which have arisen while performing that activity. Above all, we invested effort into reforming the regular financial reporting system of insurance undertakings as well as the system of their reporting to us, as the supervisor. In this way we obtained concise and reliable information on the grounds of which it is possible to identify potential problems fast and easy. We delivered a clear message to this industry's representatives, at times including through unpopular measures, that neither manipulations in the financial statements, nor major errors in them would be tolerated. This enabled us to reduce by far the level of supervisory intervention in on-site inspections of reliability of business books and financial statements, giving us the opportunity to devote our resources and time to new topics, introduced by the challenges of the contemporary environment. Therefore, in our supervisory activities today we address business planning, market behaviour, and many other areas of business operation of insurance undertakings, seeking, as supervisors, to guide those operations towards good and useful business practice. Business plans, for example, were for years prepared only as a matter of form, while today we invest joint efforts into producing quality documents useful both for insurance undertakings themselves, helping them in their business organisation and also serving their supervisor to keep track of the defined business models and objectives. The dissemination of information to insurance policy holders is a new obligation, which insurance undertakings continue to perceive with certain resistance, but luckily this is rarer and rarer, as acting jointly we understand the importance of the issue and how much it contributes not only to better consumer protection but also to rising quality and credibility of insurance industry. Additional costs of pre-contractual information, which many market participants tried to avoid, must in fact be perceived as investment in consumers, whose personal satisfaction will make them more loyal in the future, and that is the most important resource of any business entity in the contemporary environment.

The NBS on-site supervisions are more efficient today, with very clearly defined objectives and outcomes. Special attention is devoted to the sale of insurance, as we believe it is the reflection of this industry in front of citizens. That is why any form of unauthorised operation, false presentation or non-adjusting of insurance products to the real consumer needs must not be allowed. Only sound growth based on a satisfied consumer is desirable. The principle of voluntary insurance, apart from exceptional cases defined by the state, is guaranteed. No one has the right to breach these principles for the sake of quick profit, as such breach would jeopardise the reputation of the entire industry. In that sense we endorse actions of the Association of Serbian Insurers, but we also expect them to be more intensified in the future. Insurance promotion, by means of pointing to the benefits for citizens, is the right path for the development of this industry. Also, internal mechanisms of the professional association may deter all those who breach the proclaimed values. The supervisor's objective is not insurance promotion nor is it our intention to delve in it. However, everything which makes the industry, with appropriate and noble motives, will receive our support. The sales method is a crucial element in life insurance development as it is a kind of substitute to long-term savings, while in case of property insurance one needs to pay special attention to compensation claims, which, in fact, are the best promotion before the citizens. Naturally, we must never forget about the injured parties who, without the status of insured persons, find themselves, with no fault of their own, in a property or life threatening situation. The compensation right of these persons is and must remain inviolable, which is why this aspect will remain to be intensely present in our on-site supervisions.

Off-site insurance supervision of the National Bank of Serbia is a high-quality innovation which surely marked this year. Our goal was to find some specific aspects of business of insurance undertakings, which are not of particular interest in standard supervision, but are nonetheless very important for citizens. In that way, we tried to provide better protection to, for instance, students of primary and secondary schools, hotel guests, citizens paying for public utilities, public transport commuters and other persons that are or can be in the role of the insured. Through such supervision, we first learned about the business of the insurance undertakings selected as representative in those segments, after which we established the standards of good business practices, which we then recommended to the entire market with the aim of improving it. I particularly wish to emphasise that insurance undertakings have recognised this intention of ours, to which they not only responded appropriately, but even chose to voluntarily take part in the proliferation and promotion of such practices. In this way, we managed to together create better work conditions for all market participants, which should in the first place be working based on uniform principles, and to which their supervisor should apply the same standards and criteria. We are very pleased with the achieved results. Some poor practices have been entirely done away with, others have been improved, while some brand new, good and desirable practices are becoming the standard for doing business. Off-site insurance supervision has thus greatly stepped out of the mould of a passive collector of various reports and data, bringing the scope of its activity to the level the modern insurance market requires and deserves.

Perspectives of insurance supervision are inextricably bound to Serbia's path towards Europe. The National Bank of Serbia particularly supports the commitment of the Serbian Government to European integration and acts as an active participant in this process, through negotiations, mainly in the area of financial services, but also through a wide array of other activities aimed at harmonising regulations and creating an economic environment that is more favourable and secure for both companies and citizens. It is already well known that the regulatory objective of the Serbian insurance sector and its supervision is the Solvency II regulatory framework. Countries in the European Union already started implementing it last year, whereas we, as a country aspiring to access the Union, have another fresh challenge before us. We are profoundly aware of this fact, which has been taken into utmost consideration in all our activities to this day. The Insurance Law that we have today has already integrated some elements of the Solvency II regulatory framework, and we have established a strategy for the path to full harmonisation. In view of the new deadlines to complete the national legal framework entirely built on European

standards, our plan is to prepare new regulations by 2020 or 2021 to meet this objective. What remains until then is for us to prepare well and also to prepare the market under our supervision. For this reason, we have already conducted a preliminary stress test, and plan on implementing a number of quantitative impact studies and defining an optimal model of legal amendments and secondary legislation, which will implement the Solvency II framework by the stated deadline. The question, however, is when they will be applied. A number of future provisions is also expected to have a delayed effect. What lies before us is certainly a complex task of meeting European standards, all the while maintaining the stability of the domestic insurance market.

At the moment, perhaps the largest challenge is improving regulations concerning compulsory traffic insurance. This is a task undertaken by the Ministry of Finance, though with the wholehearted help and coordination of other public institutions, including the National Bank of Serbia. At our initiative, the insurance sector was directly involved in this task through the Association of Serbian Insurers. Therefore, it is very good to have all the relevant parties gathered here today, where one of the central topics for further discussion will, in fact, be compulsory traffic insurance. My close associate will also take part in these discussions, but something I wish to tell you personally is that market participants must reach a consensus about sensitive matters, for this is the only way that we can ultimately get regulations that are applicable in practice. The lack of such applicability is precisely the greatest drawback of a large number of provisions under the current Law on Compulsory Traffic Insurance. Once that job is done, we will have a well-rounded and high-quality regulatory framework for insurance, paving the way for further improvements of regulations, which have already been mentioned.

In addition to all what has been said, the National Bank of Serbia makes effort, within its main competences, to have a continuous influence on the business and investment climate in Serbia, as well as overall price and financial stability. Bearing this in mind, my today's address would be incomplete without at least several words about the results that we have achieved in this field. Starting from this year, the inflation target has been reduced to $3\% \pm 1.5$ percentage points, and inflation is successfully maintained within its bounds. Low and stable inflation that Serbia has today and has had for the past several years, is imperative for the preservation of the real value of wages and pensions, and the creation of predictable terms of business for all market participants. By continuously lowering the key policy rate since May 2013, we have opened room for the recovery of lending activity and for further economic growth. Falling interest rates are one of the factors of acceleration of economic growth, while at the same ensuring considerable saving for the economy, citizens and the state. Economic growth is also propped up by net foreign direct investment in Serbia which, as I have already mentioned, has been exceptionally important for the insurance industry. By making these efforts, we have managed to strengthen credibility among all stakeholders that consider the avenues for investment in Serbia. Adding to this anchored inflation expectations, a relatively stable exchange rate, a stable and resilient financial system, growing confidence in the domestic currency along with a rise in dinar household borrowing and elevated dinar savings, we certainly have the results that we can be proud of. We have achieved all this owing to our own commitment, bravely facing the challenges of the international environment and global financial trends. That this is not only our opinion is confirmed by concrete and publicly available information, as well as increasingly better assessments of credit agencies and relevant international institutions. We have reduced the budget deficit, met all the criteria set before us by the International Monetary Fund, and have recently completed the last, eighth review of the current arrangement with this institution.

Finally, I wish to emphasise the good cooperation that the National Bank of Serbia fosters with the Association of Serbian Insurers, which we will continue to streamline towards the development and modernisation of domestic insurance. May this conference be a step towards that goal, but also a step towards much broader cooperation involving other institutions of our country, as well as countries of the region and the European Union. The exchange of ideas, experiences and knowledge is always a process that brings multiple benefits to both sides. Therefore, today, by proclaiming this conference open, I wish that it should become a traditional

event, contributing in the best way to enhancing the quality of insurance in Serbia – first and foremost to the benefit of all our citizens and economic entities related to insurance, either as employees or business partners, or as beneficiaries of its services. The National Bank of Serbia will remain an unbiased, quality and reliable supervisor of the insurance business.

Thank you.