EUROPEAN INSURANCE
AND OCCUPATIONAL PENSIONS AUTHORITY

Press Release

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EIOPA ANNOUNCES RESULTS OF THE 2016 EU-WIDE INSURANCE STRESS TEST

- *A supervisory snapshot of the life insurance market in Europe to assess vulnerabilities and resilience to severe market developments – not a pass or fail exercise*
- *Focus on two major market risks: A "low-for-long-yield" and a "double-hit" scenario*
- *236 insurance undertakings at solo level from 30 European countries participated*
- *In the pre-stress situation participating undertakings appear adequately capitalized on an aggregate basis*
- *Impact of stress scenarios shows that the low interest rate environment and a pronounced reassessment of risk premia pose a significant challenge for European insurance undertakings*
- *"Double-hit" scenario to have a negative impact on the undertakings balance-sheet of 160 billion euros and "low-for-long" an impact of 100 billion euros*
- *Revealed vulnerabilities require a coordinated supervisory response*
- *When the viability of the business model is at risk, EIOPA recommends National Supervisory Authorities (NSA's) to consider requesting the cancellation or deferral of dividend distribution*

Frankfurt, 15 December 2016 – The European Insurance and Occupational Pensions Authority (EIOPA) announced today the results of its 2016 EU-wide stress test for the European insurance sector. This year's exercise assessed insurers' vulnerabilities and resilience to two severe market developments: A prolonged low yield environment and a "double-hit" scenario. The "low-for-long" scenario reproduced a situation of entrenched secular stagnation driving down yields at all maturities for a long period of time, while the "double-hit" scenario reflected a sudden increase in risk premia combined with the low yield environment. The severity of the scenarios goes beyond the Solvency II capital requirements.

In the first vulnerability assessment conducted after the implementation of the Solvency II regulatory framework, participating undertakings calculated the impact of these severe stress scenarios on their balance sheets with reference to 1 January 2016.

The exercise involved 236 insurance undertakings at the solo level from 30 European countries, with market coverage of 77% in terms of the relevant business (life technical provisions excluding health and unit linked) and included medium- and small-sized undertakings.

On the **baseline (pre-stress)**, results indicated that on an aggregated level undertakings were adequately capitalised from a Solvency II perspective with an overall Solvency Capital Requirement (SCR) ratio of 196%. More than 70% of the participants had SCR coverage above 160%. Only two undertakings, representing 0.02% of the total assets in the sample, had a SCR ratio below 100%. The overall SCR ratio falls to 136% (32 undertakings below 100% representing 26% of the total assets) if all Long-Term-Guarantee (LTG) and transitional measures are excluded. The quality of own funds was generally high with Tier 1 unrestricted own funds accounting for 90% of the total.

The **impact of both stress scenarios** is of similar magnitude in terms of the reduction of the average assets over liabilities ratio, however not equally spread among undertakings or national markets. The different identified levels of vulnerabilities were corresponding to the different market characteristics and/or balance sheet structures.

The **"double-hit"** has a negative impact on the undertakings balance sheets of close to EUR 160 billion (-28.9% of the total excess of assets over liabilities) with more than 40% of the sample losing more than a third of their excess of assets over liabilities. In the absence of LTG and transitional measures, such impact would apply to almost 70% of the sample.

The **"low-for-long"** resulted in a fall in the excess of assets over liabilities of about EUR 100 billion and undertakings representing 16% of the sample would lose more than a third of their excess of assets over liabilities (25% if LTG and transitional measures are absent).

These results provide a quantified estimation of the insurance sector vulnerability to the low interest rate environment and to a pronounced reassessment of risk premia. Furthermore, they also confirm that the LTG and transitional measures provide the financial stability cushion intended, potentially acting in a countercyclical manner, but supervisory vigilance is required in order to avoid a misestimate of the risks due to the longer-term type of concerns implied by the scenarios tested.

The revealed vulnerabilities deserve a supervisory response. In order to ensure coordinated supervisory actions, EIOPA issued Recommendations to the National Supervisory Authorities (NSA's). The NSA's actions include, when needed:

- To ensure that undertakings align their internal risk management processes to the external risks faced
- To review and assess undertakings' models regarding the behaviour of management and policyholders
- To review the clauses of the guarantees, their typologies, and the optionalities they carry to assess if the valuation of the technical provisions can be considered proportionate and prudent
- To request a reduction in the maximum guarantees or in unsustainable profit participations offered
- To request a cancellation or deferral of dividend distribution when the viability of the business model is at risk
- To ensure that the vulnerabilities identified at solo level are appropriately recognised and dealt with at the group level

EIOPA, in its coordinating role, will support the NSAs and undertakings in the follow-up of these Recommendations.

Gabriel Bernardino, Chairman of EIOPA said: *"The results of this year's EIOPA stress test confirmed the significant challenges for the European insurance sector triggered by the current macro-economic environment. The Stress Test 2016, conducted for the first time after the implementation of the Solvency II framework, provided indeed a "high-resolution" picture of the vulnerabilities of the sector requiring particular supervisory attention. EIOPA will closely monitor the implementation of the*

Recommendations by the NSA's in order to ensure a coordinated response to situations that may pose a threat to the viability of the supervised entity and, collectively, to the system as a whole."

The Report on the results of the 2016 EIOPA Insurance Stress Test can be viewed on EIOPA's Website: https://goo.gl/PkRLKD

Notes for Editors:

Insurance Stress Test 2016 comprises three scenarios:

1. Baseline, i.e. the pre-stress valuation of the balance sheet
2. "Low-for-long" focused on a prolonged low yield environment
3. "Double-hit" - this scenario has been developed in cooperation with the European Systemic Risk Board (ESRB) – Link to ESRB Website: https://www.esrb.europa.eu/home/html/index.en.html

Participation in the Stress Test 2016

- 236 insurance undertakings at **solo level** from 30 European countries – see list of companies in the Report of the results
- **Market coverage of 77 % in terms of the relevant business** (life technical provisions excluding health and unit linked) was achieved including medium- and small-sized undertakings. The undertakings in sample hold EUR 6.3 trillion in assets, almost 60% of total assets held by EU/EEA insurers. The overall technical provisions for the sample are EUR 5.2 trillion, accounting for 91% of total liabilities (of EUR 5.7 trillion).

Solvency Capital Requirement (SCR) represents economic capital to be held by (re)insurers to ensure that they will be able to meet their obligations to policy holders and beneficiaries over the following 12 months with a probability of at least 99.5%.

Long-Term Guarantee (LTG) measures represent the measures under the Solvency II regime aimed at ensuring an appropriate supervisory treatment of long-term guarantee products.

Transitional measures represent the measures under the Solvency II regime aimed at to soften the immediate impact of the new rules so that, for example, large increases in technical provisions or capital requirements can be brought in gradually, allowing undertakings to fund them gradually rather than all in one go.

Technical provisions refer to the calculated value, under specific methodologies, of the amount needed to meet obligations to policyholders.

Unit linked business refers to contracts where the investment risk lies with the policyholder/unit holder. However, there are specific products where some kind of guarantee is given.

Tier 1 unrestricted own funds refer to the category of available funds with the highest loss-absorbing capacity. The eligibility of these funds to cover the SCR or the MCR is not subject to any limit.

The **European Insurance and Occupational Pensions Authority (EIOPA)** was established on 1 January 2011 as a result of the reforms to the structure of supervision of the financial sector in the European Union.

EIOPA is part of the European System of Financial Supervision consisting of three European Supervisory Authorities, the National Supervisory Authorities and the European Systemic Risk Board. It is an independent advisory body to the European Commission, the European Parliament and the Council of the European Union.

EIOPA's core responsibilities are to support the stability of the financial system, transparency of markets and financial products as well as the protection of insurance policyholders, pension scheme members and beneficiaries.