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EUROPEAN INSURANCE

AND OCCUPATIONAL PENSIONS AUTHORITY

# EIOPA Stress Test 2011

Press Briefing  
Frankfurt am Main,  
4 July 2011

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1. Objectives
2. Initial remarks
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*Overall objective of the exercise:*

- Assess the **resilience** of the EU insurance sector to major shocks
  - Understand evolution of capital position of insurers in **adverse situations**
  - Evaluate the **overall stability** of the insurance market
- ➡ Regulation requires EIOPA to “initiate and coordinate Union-wide stress tests”

*What **is** the EIOPA stress test?*

- An important **supervisory** and **risk management tool**
- A test of **“what if” scenarios** to explore insurance companies vulnerabilities

*What is the EIOPA stress test **not**?*

- A solvency exercise
- A second guess of capital requirements

- Stress test **based on** EU future risk-based regulation - **Solvency II**
- **Assets and liabilities** valued on a **market** consistent basis
- Macroeconomic scenarios provided by the ECB
- Shock scenarios developed by EIOPA to highlight risks of particular relevance to insurers

## *Three Scenarios*

- **Baseline** (severe stress)
- **Adverse** (more severe market deterioration in the main macroeconomic variables)
- **Inflation** (increase in inflation -> rapid increase interest rates)

## *Risks*

- **Market** (interest rate, equity, real estate)
- **Credit** (spread risk: investment grade, high yield)
- **Insurance** (natural catastrophe, pandemic event, reinsurance)

## Overview of Applied Scenarios

Risk modules	Baseline scenario	Adverse scenario	Inflation scenario
<b>Market Risk</b>			
<b>Interest rate</b>			
<3M	-40 bps	-125 bps	+125 bps
>3M	-20 bps	-62.5 bps	+62.5 bps
<b>Equities</b>	-7.5%	-15%	0%
<b>Real estate Residential</b>	-3.8%	-11.6%	0%
<b>Real estate Commercial</b>	-12.5%	-25%	0%
<b>Credit Risk</b>			
<b>Spread risk</b>	Spread increases as a function of rating (AAA to B), from 0.125-1.5%-points	Spread increases as a function of rating (AAA to B), from 0.25-3.0%-points	
<b>Investment Grade</b>	+15.7% increase in spreads	+31.4% increase in spreads	0%
<b>High-yield</b>	+19.15% increase in spreads	+38.3% increase in spreads	0%

## Overview of Applied Scenarios - continued

Insurance Risks																					
<b>Non-Life Insurance related stresses</b>	The greater of the following: (1) the largest one-in-two-hundred natural catastrophe probable maximum loss (PML), where only a 70% recovery rate from reinsurers can be assumed; (2) a shortfall arising for all non-life claims reserves by assuming a 2 percentage point higher claims inflation than presumed for existing best estimate calculations without recourse to reinsurers.																				
<b>Life Insurance related stresses</b>	The greater of the following: (1) An additional 1.5 deaths per thousand lives, assumed to follow from a pandemic event where the recovery rate from the two largest reinsurers on the panel is only 50%; (2) An increase of 23% in mortality improvement rates, over and above the developments already factored into the best estimates, with no recovery from reinsurers.																				
<b>Sovereign Risk</b>	Country specific yield curve movements were defined on the basis of macroeconomic assumptions for EU-Member States, Norway, Iceland, Switzerland and Liechtenstein. The magnitude of the resulting adverse yield curve movements was calibrated to reflect the outlook per country and would therefore affect the pricing of sovereign bond holdings in insurance undertakings asset holdings.																				
<b>Aggregation of Risks</b>	The risk sources market/credit risk and insurance risks are added using the following correlation matrix. <table border="1" data-bbox="550 1135 1381 1276"> <thead> <tr> <th><i>i</i></th> <th><i>j</i></th> <th>Market and Credit</th> <th>Life</th> <th>Non-Life</th> </tr> </thead> <tbody> <tr> <td>Market and Credit</td> <td></td> <td>1</td> <td></td> <td></td> </tr> <tr> <td>Life</td> <td></td> <td>0.25</td> <td>1</td> <td></td> </tr> <tr> <td>Non-Life</td> <td></td> <td>0.25</td> <td>1</td> <td>1</td> </tr> </tbody> </table>	<i>i</i>	<i>j</i>	Market and Credit	Life	Non-Life	Market and Credit		1			Life		0.25	1		Non-Life		0.25	1	1
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Market and Credit		1																			
Life		0.25	1																		
Non-Life		0.25	1	1																	



## Sovereign Bond Stress

Basis point increase in yields [\[1\]](#):

Belgium	78.0
Bulgaria	81.0
Czech Republic	34.5
Denmark	16.5
Germany	0.0
Estonia	39.0
Ireland	258.0
Greece	255.0
Spain	165.0
France	48.0
Italy	136.5
Cyprus	136.5
Latvia	55.5
Lithuania	64.5
Luxemburg	78.0
Hungary	114.0
Malta	136.5
Netherlands	22.5
Austria	24.0
Poland	67.5
Portugal	246.0
Romania	91.5
Slovenia	39.0

Slovakia	33.0
Finland	10.5
Sweden	6.0
United Kingdom	28.5
Iceland	42.0
Liechtenstein	0.0
Norway	6.0
Switzerland	0.0

[\[1\]](#) Envisaged sovereign risk for EU countries are ECB macroeconomic assumptions whereas EEA countries are assumptions similar to the EBA market risk test for long term maturities.

- **Coverage**: 221 (re)insurance groups and companies in the European Union, European Economic Area, Switzerland
- **58 groups and 71 individual undertakings** reported results (aggregated group reporting)



Achieved goal of minimum coverage of 50% by premium income per country

Represents **approximately 60% of the market share**

## Capital

### Aggregated Figures

	in EUR billion	in %	
Eligible capital before stress	577		
Minimum Required Capital (MCR) before stress	152		
Solvency Surplus	425		
MCR coverage ratio		380%	
MCR coverage ratio in baseline scenario		320%	
MCR coverage ratio in adverse scenario		281%	
MCR coverage ratio in inflation scenario		342%	
Impact on eligible capital	in EUR billion	as a percentage of eligible capital	Solvency deficit of undertakings not meeting the MCR (in EUR billion)
Baseline scenario	92	15.9	2.6
Adverse scenario	150	26.0	4.4
Inflation scenario	58	10.0	2.5
Sovereign Stress Scenario	33	5.6	3.4

## Aggregate MCR Threshold Impact

Scenarios	Number of insurers failing MCR	Number of insurers failing MCR in %	Solvency deficit of undertakings not meeting the MCR (in EUR billion)
<b>Baseline scenario</b>	11	9%	<b>2.6</b>
<b>Adverse scenario</b>	13	10%	<b>4.4</b>
<b>Inflation scenario</b>	10	8%	<b>2.5</b>
<b>Sovereign Stress Scenario</b>	6	5%	<b>3.4</b>

- **Asset:**

- ✓ Adverse developments in equity prices, interest rates and sovereign debt markets

- **Liability:**

- ✓ Non-life risk more critical
- ✓ Increased claims inflation
- ✓ Natural disasters
- ✓ High sensitivity to reinsurance

***Range of outcomes depends on the business model employed by insurer (life vs. non-life)***

- Overall the **European insurance sector remains robust** in the occurrence of major shocks
- **90% of the groups/undertakings** tested continue to comply with the Minimum Capital Requirements even in the most adverse scenario
- **Main vulnerabilities** identified:
  - ✓ Adverse developments in yield curves and sovereign bond markets
  - ✓ Higher than expected rate of severe natural catastrophes combined with limited recourse to reinsurance facilities

- **EIOPA** to continue to **monitor** the evolution of **markets** and the main **vulnerabilities** identified
- **National supervisors** to discuss the main findings of the stress test with insurance groups and undertakings
- Results of stress test to be embedded in the individual plans and strategies to **implement Solvency II**
- **Insurance undertakings** to develop strategies to deal with given scenarios and main vulnerabilities



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## Thank you

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