Alberto Corinti

Member of the Board of Directors, Italian Insurance Supervisory Authority (IVASS)

EU insurance firms and their expected role to channel premiums into long-term savings

In line with its traditional objectives, insurance is a process providing efficient protection against risks. In this context, insurance firms can certainly represent a driver for long-term savings and a mechanism for a stable and sustainable funding of the economy. However, we can neither expect that insurance plays a role in transforming short-term savings into long- term investments, nor in supporting the economy without a proper assessment of the associated investment risks.

Any financial mediation role of insurance should always be the product of a sound insurance process and should not become an objective per se. We have to acknowledge, however, that regulations might not always strike the right balance between prudential objectives and social and economic ones. Solvency II is a good prudential framework, but some consider it an obstacle to the release of financial guarantees and to the investment in long-term assets, particularly in the current scenario of low interest rates.

My view is that the Solvency II framework relies on features, such as the market consistent valuation, that we should not abandon, as they ensure proper and early risk identification and assessment. At the same time, however, the framework needs adjustments to avoid unduly penalizing long-term business. The first adjustment relates to the need to reduce balance sheet volatility, which could produce solvency indicators that do not reflect the long-term nature of the business.

The review of LTG Solvency II measures should allow increased stability of the balance sheet without jeopardizing the predictive characteristics of its indicators. Elements like the Volatility Adjustment, for example, should be better designed to reflect the capacity of firms to protect themselves from short-term spread volatility and to earn a risk premium on longer durations, avoiding unjustified capital relief.

Another area for improvement is the elimination of any undue capital charge penalization. Much has already been done in this field, but proper calibration needs an on-going monitoring and regulators should regularly review their conclusions in line with market developments. At the same time, a proper risk measurement should always inform the definition of financial requirements. Also proper capitalization is key for long-term business. The revision of interest rate capital charge is necessary in this regard.

Besides prudential regulation, insurance product design too is relevant in order to foster long-term guarantees and investments. For example, increased flexibility in the allocation of profits in certain life contracts or the increase of the illiquidity features of certain contractual liabilities could represent important factors to sustain long-term business.

> *Any financial mediation role of insurance should always be the product of a sound insurance process.*

Finally, we should not forget that a number of other factors not related to the regulation are also necessary. For example, the availability of well-structured long-term financial instruments in transparent markets is a precondition for incentivizing insurers to invest in long-term assets. Prudential regulations can only be part of the solution.

It is certain, however, that the focus should be centered on solutions that could soften, within prudential limits, the impact of the current low interest rate scenario on insurers and allow them to continue to play their role as providers of protection and long-term investors. A regulatory approach that simply provides disincentives to the release of long-term financial guarantees is not, I think, a desirable solution.