



Inflation risk for insurance companies

Presentation for the DNB insurance day

22 September 2022



Introductions



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Inflation risk and the impact on life insurers

A view on the potential impact and insurers' response

A presentation by Gareth Sutcliffe

22 September 2022

Agenda

1. Inflation and Interest rates:
 - Where are we now?
 - How did we get here?
2. Impact of higher inflation and interest rates
3. Could interest rates stay high?
4. If rates and inflation stay high, how might life insurers respond

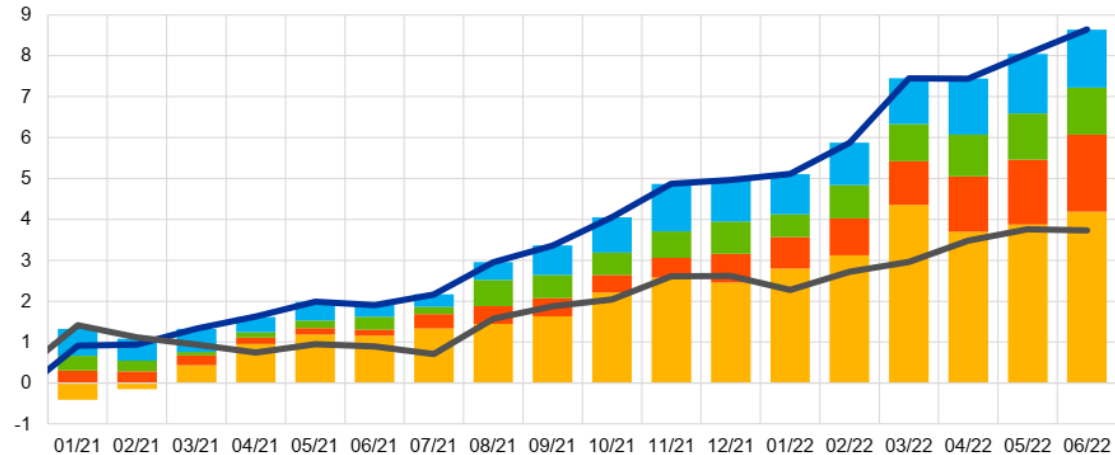
Inflation and Interest rates: Where are we now?

Euro area inflation

Headline inflation and its main components

(annual percentage changes; percentage point contributions)

- Headline HICP inflation
- HICPX
- Energy
- Food
- Non-energy industrial goods
- Services



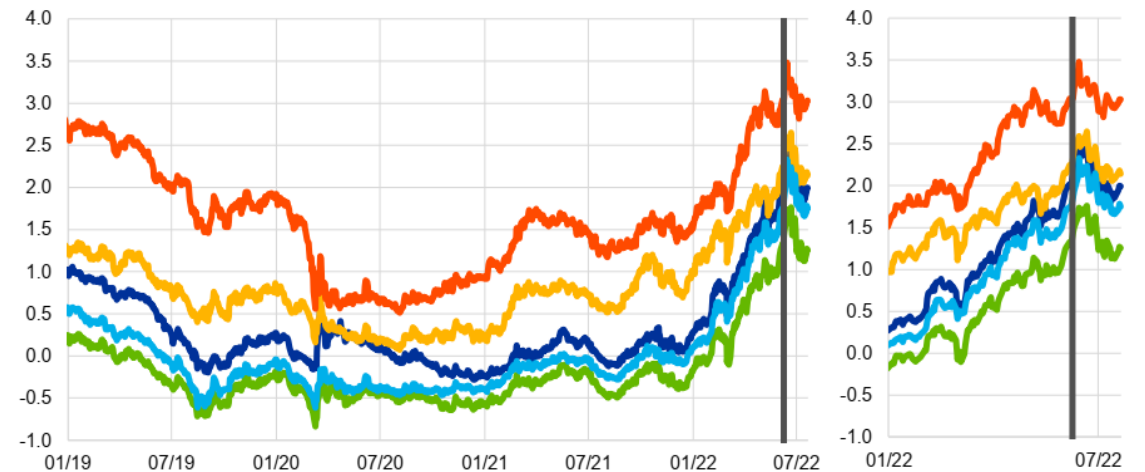
Sources: Eurostat and ECB calculations.
Note: The latest observations are for June 2022.

Ten-year sovereign interest rates

Ten-year sovereign bond yields and the ten-year OIS rate based on the €STR

(percentages per annum)

- GDP-weighted euro area average
- United Kingdom
- United States
- Germany
- Ten-year euro area overnight index swap rate



Sources: Refinitiv and ECB calculations.
Notes: The vertical grey line denotes the start of the review period on 9 June 2022. The latest observations are for 20 July 2022.

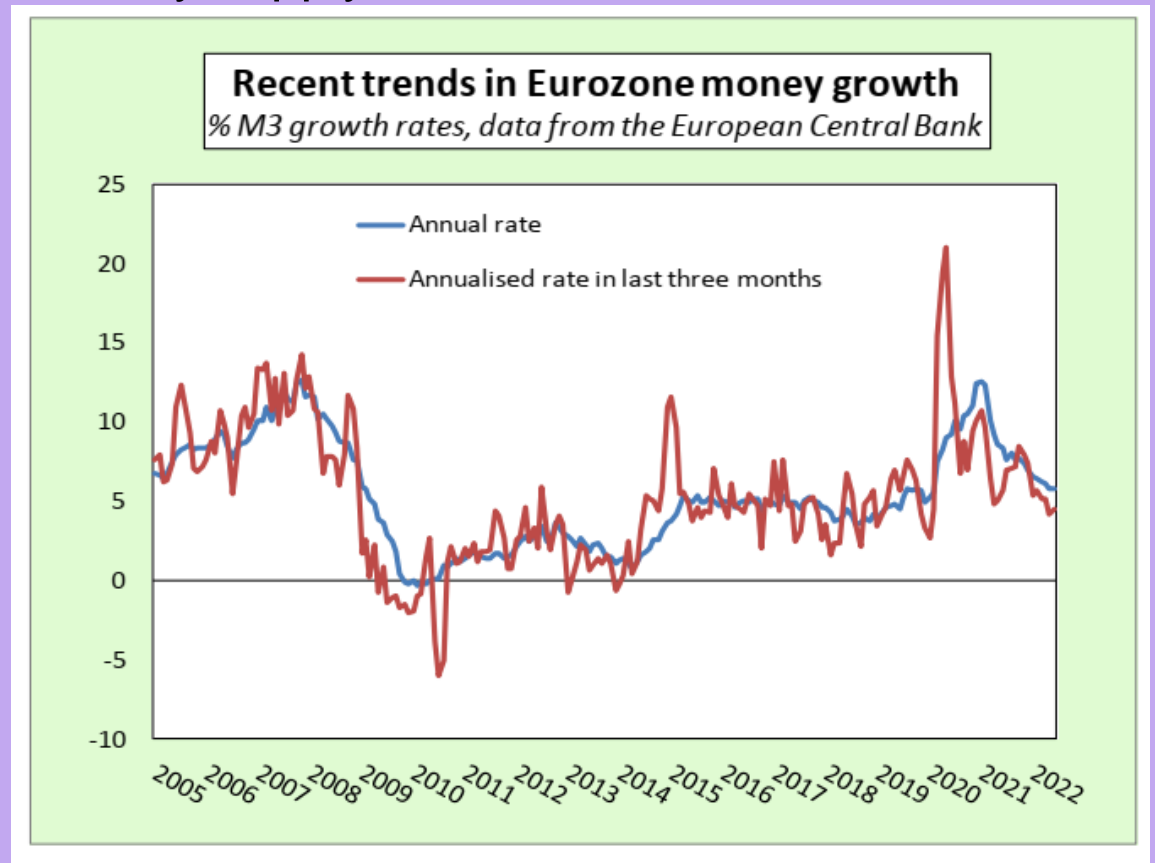
Inflation and Interest rates: How did we get here....

Cost push?



Source: <https://www.bankofengland.co.uk/monetary-policy-report/2022/august-2022>

Money supply?



Source: Institute of International Monetary Research (August 2022, monetary update)

<https://mv-pt.org/monthly-monetary-update/>

Will inflation or interest rates stay high?

5-year forward, 5-year inflation market view



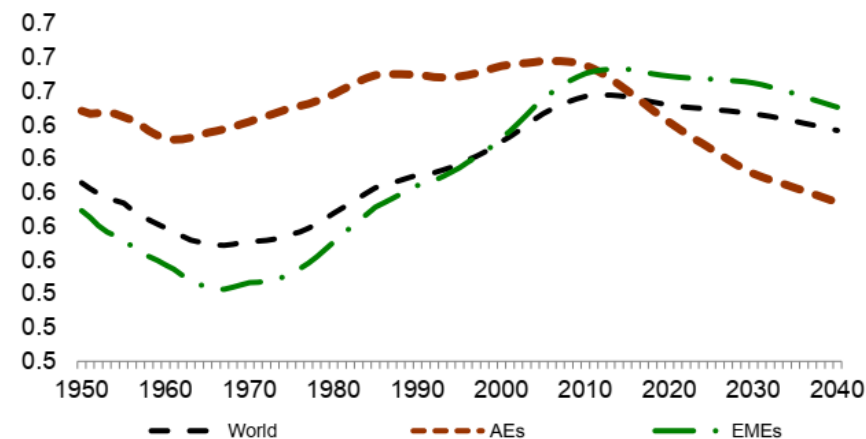
Source: <https://www.bankofengland.co.uk/monetary-policy-report/2022/august-2022>

Falling working populations => higher inflation?

Working age population rose in AEs and sharply in EMEs, but should now begin falling

Working age population / total population

Graph 5



Source: UN World Population Database.

Goodhart & Pradhan, 2017, <https://www.bis.org/publ/work656.pdf>

Question (via Yellenge)

If inflation does stay high.... what are you most afraid of?

- a) Costs and claims of the company increasing faster than the insurance premiums
- b) Higher interest rates following the inflation rates will decrease value of assets
- c) Increasing uncertainty and higher risk capitals
- d) High costs of living will lead to lower insurance premium volumes
- e) Nothing



Impact of high inflation and interest rates



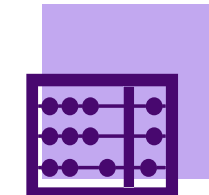
Impact on BEL:
Higher rates => lower liabilities
Higher Inflation => increase liabilities



Expenses higher
and more volatile

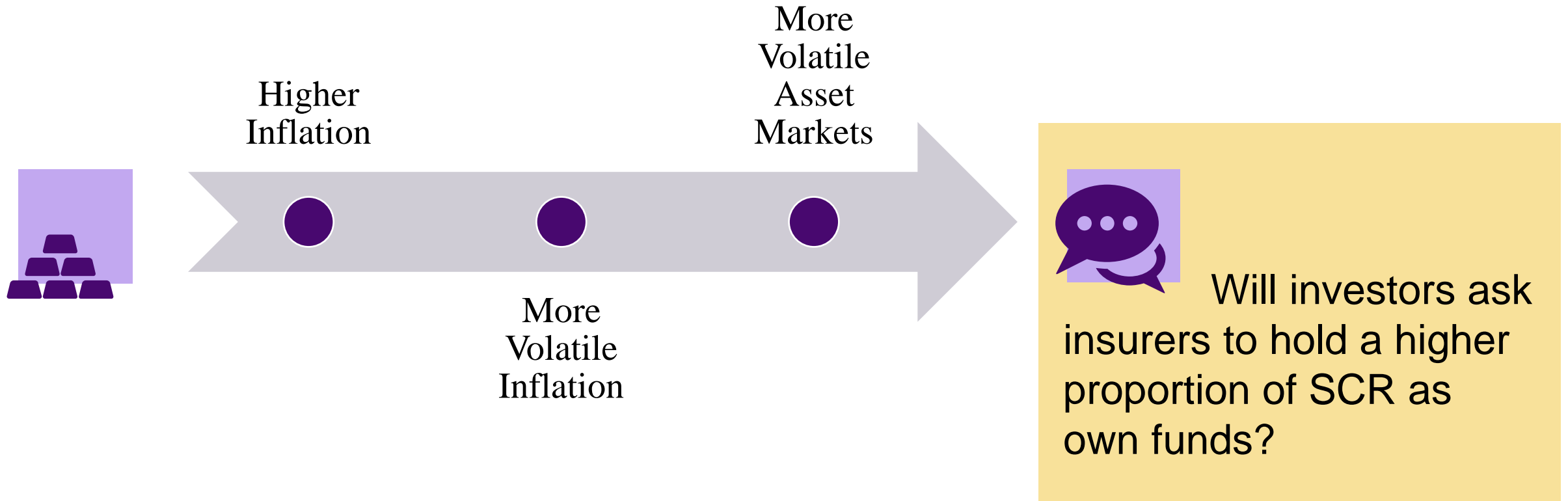


Less impact from UFR



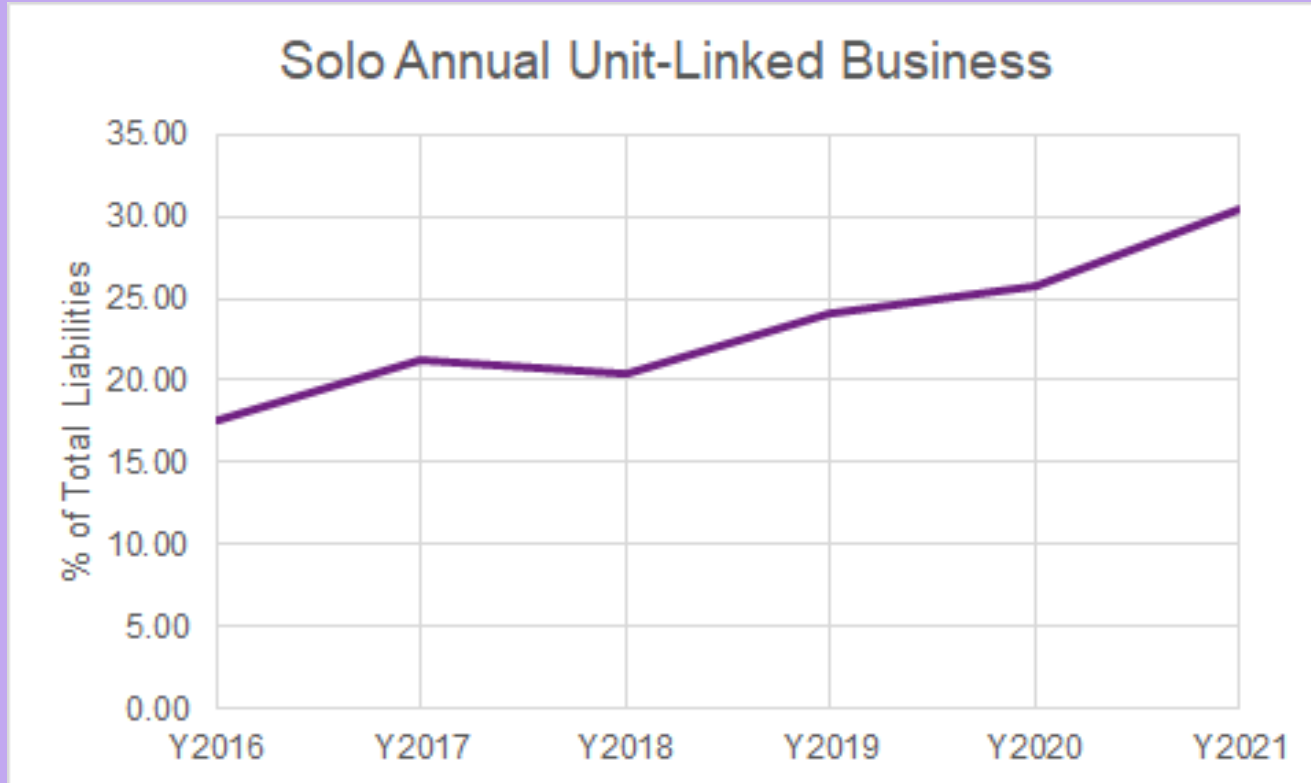
Less effective volatility
adjustment

Impact of high inflation and interest rates



How could insurers respond?

In many parts of Europe there has been a drive towards offering fewer guaranteed products



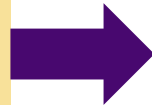
Source: EIOPA



How could insurers respond?

Return of the Guarantee?

Could higher rates lead to the return of the guarantee?



Guarantees cheaper to offer

Demand products with protection / guarantee features

Differentiation between insurance savings products and asset managers

But maybe some things will be different



Shorter guarantee terms?

Reprice guarantee frequently

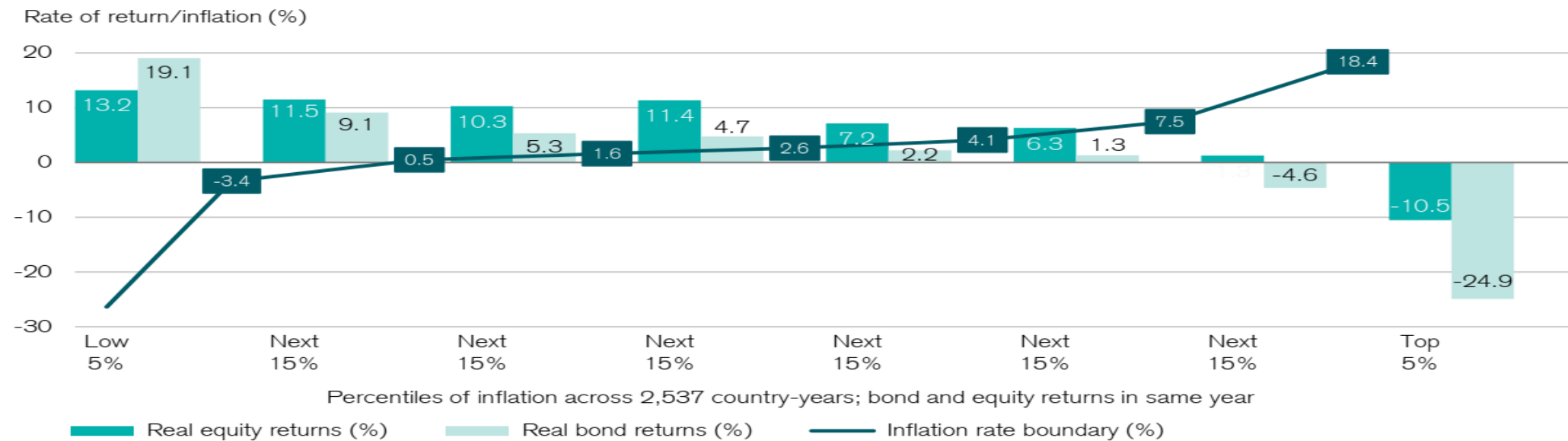
Requires slick ALM / pricing / communication

How could insurers respond?

Changes in asset allocation?

- Recent trends have been towards greater private credit assets
- Higher inflation may promote more diversification and investment in inflation resilient assets

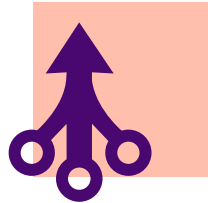
Figure 5: Real bond and equity returns versus inflation rates, 1900–2020



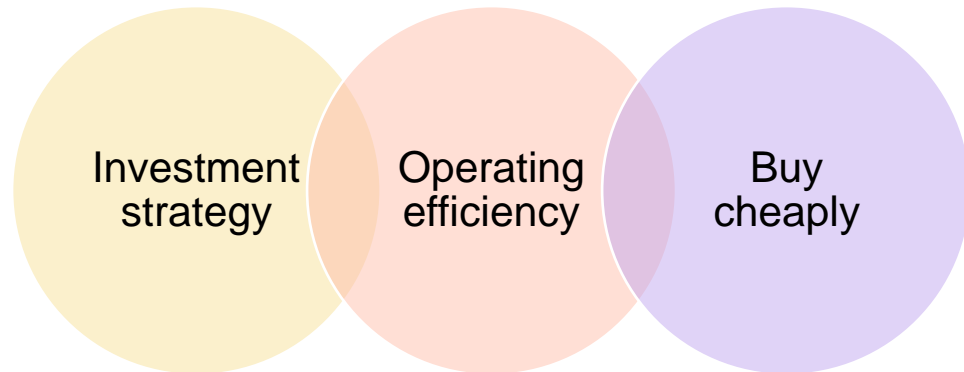
Credit Suisse Global Investment Returns Yearbook, 2021

<https://www.credit-suisse.com/about-us-news/en/articles/media-releases/credit-suisse-global-investment-returns-yearbook-2021-202103.html>

How could insurers respond?



European Insurance Consolidators Strategies



Less competitive consolidators?

Higher interest rates

- Less onerous back books
- Improved own fund position
- Fewer back books for sale?

Higher inflation

- Rising expenses
- Even more automation

Higher rates + inflation

- Less competitive advantage for PE firms
- Competitive advantage from efficient operations

Thank you



Inflation risk for non-life insurers

A view on liabilities

A presentation by Shalabh Mathur

22 September 2022

Agenda

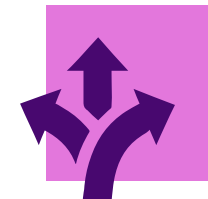
1. Inflation – Impact on Non-life insurance (a view on Liabilities)
2. Active management of inflation risk
3. Approach in Forecasting inflation

The problem

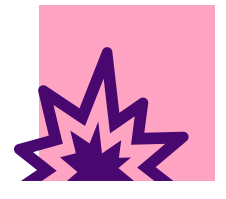
Increased inflation is affecting multiple areas of insurance businesses, ranging from a wide concern around inflation to more specific issues.



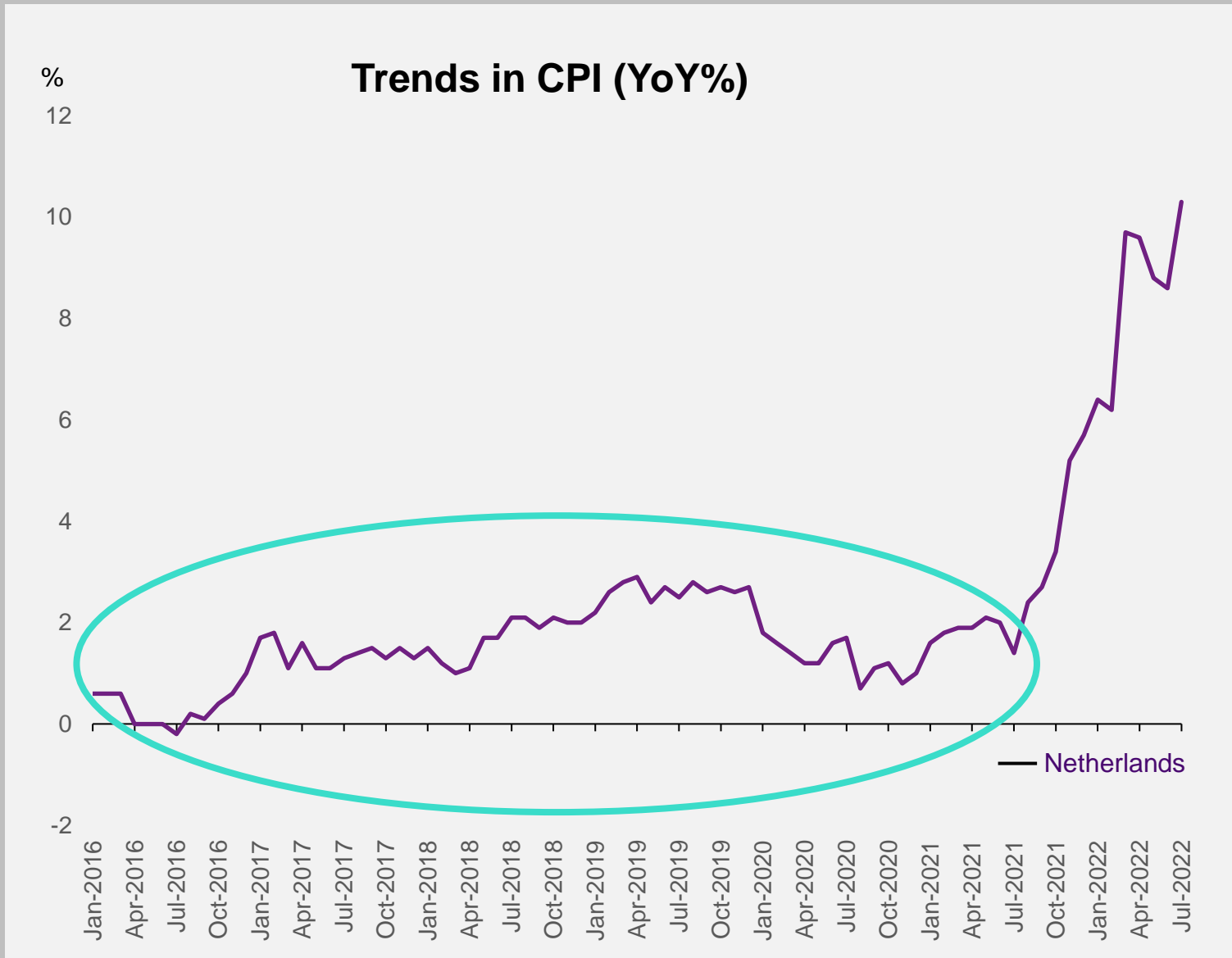
Increased materiality



Increased uncertainty



Market pressure



*Source: CBS

How does inflation impact non-life insurance business?

Impact on outstanding claims, expenses and reserve risk

Risk of a “vicious cycle”
(under-reserving and under-pricing)

Level of Premiums and expenses in future underwriting years

Sufficiency of reinsurance cover

Effect on solvency coverage

Impact on financial statements under LGAAP, IFRS17 and Solvency II

Relation to interest rates

Impact of inflation by Line of Business

Investment decisions



If you know which parts of your business are impacted by inflation and how, you can manage risks more effectively.

Question (via Yellenge)

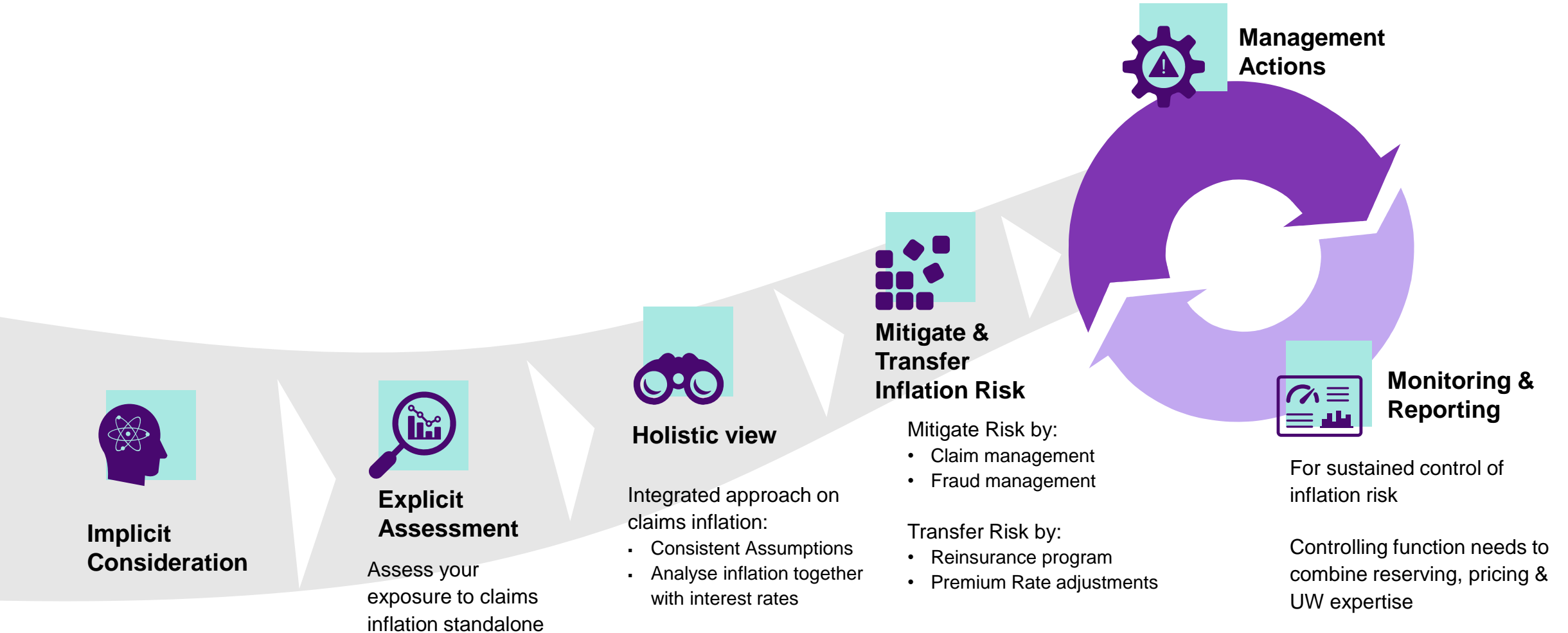
Is your company well prepared to capture inflation uncertainty into your non-life business process?

- a) Yes, we are well prepared
- b) Not for now as we need to understand the risk better
- c) We think this is not a material risk for our business
- d) I don't know



Inflation Roadmap

For better Governance



Forecasting inflation

The approach we use for the Claim Cost Index

	T1	T2	T3
CPI	8.2%	4.5%	2.1%
Wages	2.9%	3.2%	2.5%
Legal	4.7%	4.5%	3.9%
Medical	7.5%	6.5%	5.0%
Materials	9.4%	5.2%	3.2%



	Liability
CPI	40%
Wages	30%
Legal	10%
Medical	20%
Materials	0%



	Liability
Social Inflation	2.5%
Frequency	1.1%



	T1	T2	T3
GL	6.3%	4.7%	3.1%

General
economeric
indices



Insurance
coverage
weightings



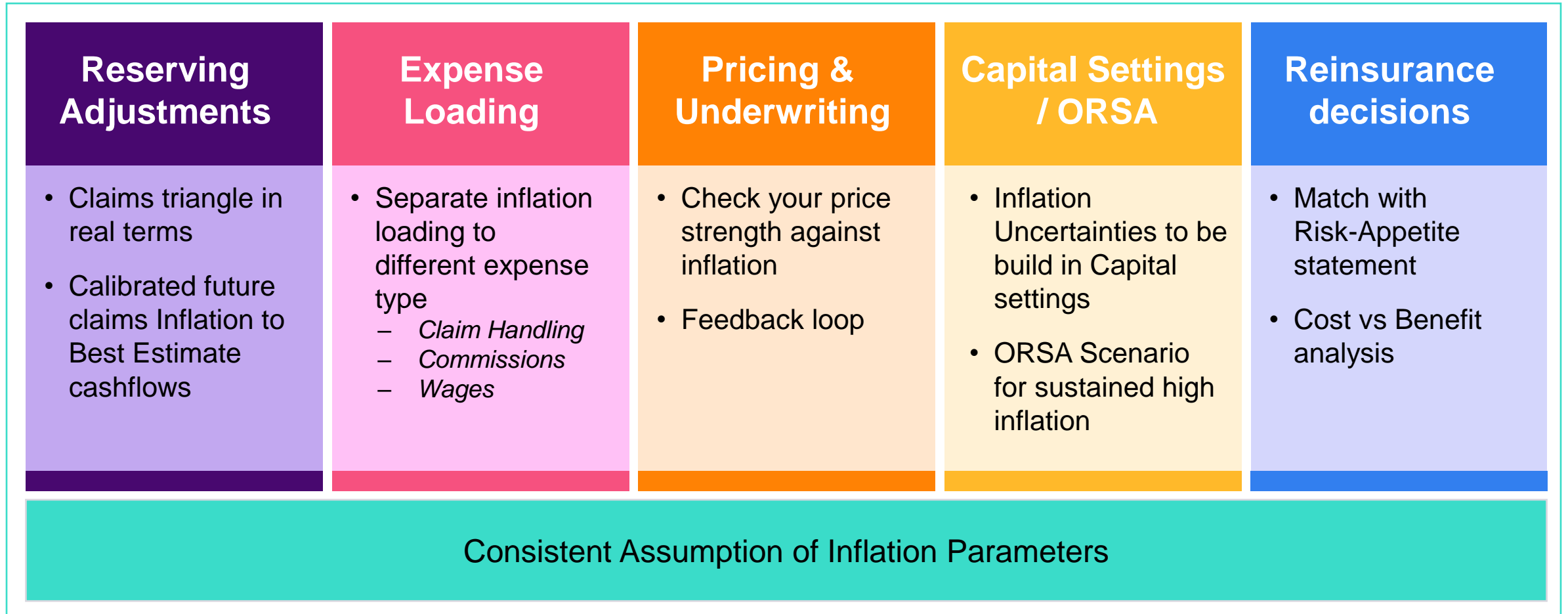
Insurance
specific
adjustment



Insurance
coverage specific
forecast

Accounting for inflation

Explicit consideration



Thank you

Questions ??