CHAPTER 3

THE INSURANCE SECTOR—TRENDS AND SYSTEMIC RISK IMPLICATIONS

SUMMARY

This chapter describes major insurance sector developments over the past decade and assesses changes in the systemic importance of insurers. Insurance firms play an important role as providers of protection against financial and economic risks and as financial intermediaries.

The chapter shows that across advanced economies the contribution of life insurers to systemic risk has increased in recent years, although it clearly remains below that of banks. This increase is largely due to growing common exposures to aggregate risk, caused partly by a rise in insurers' interest rate sensitivity. Thus, in the event of an adverse shock, insurers are unlikely to fulfill their role as financial intermediaries precisely when other parts of the financial system are failing to do so as well. The higher common exposures do not seem to be driven by marked changes in insurers' investment portfolios, although smaller and weaker insurers in some countries have taken on more risk.

The findings suggest that supervisors and regulators should take a more macroprudential approach to the sector. Doing so is necessary if supervision is to go beyond guarding against the solvency and contagion risks of individual firms and take on the systemic risk arising from common exposures. Steps that would complement a push for stronger macroprudential policies include the international adoption of capital and transparency standards for the sector. In addition, the different behavior of smaller and weaker insurers warrants attention by supervisors.