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Regulating for solvency

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Introduction

I value this opportunity to appear today in front of you to give you an international look on the economic impact of solvency problems in the insurance industry and how solvency regulation of insurers can prevent such problems.

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What I will be presenting to you is not a theory that is based on an academic paper but actual findings presented by the Subcommittee on Policy Research and Insurance Committee on Banking, Finance and Urban Affairs to the U. S. House of Representatives.

Introduction

The important point that I can stress here is that we can learn from the experiences of the international community to prevent insolvencies of insurance companies and lessen the impact on emerging markets and economies in this region.

Scope of the Presentation

In my presentation I will address briefly the following topics:

- How the insurance industry affects economic activity?
- What solvency problems mean?
- How solvency problems could arise in the insurance industry?
- What their possible major economic impacts could be?
- How solvency regulation of insurers can prevent such problems?

HOW THE INSURANCE INDUSTRY AFFECTS ECONOMIC ACTIVITY?

- The insurance industry is an important financial intermediary.
- Risk spreading raises social welfare and promotes a greater level of economic activity by protecting policyholders from various economic losses.
- The life and health insurance industry specializes in protecting individuals and their beneficiaries from financial hardships caused by premature death and costly illness.

HOW THE INSURANCE INDUSTRY AFFECTS ECONOMIC ACTIVITY?

- The property and casualty industry specializes in protecting against losses of various types of property and against losses from injury caused to others.
- The insurance industry improves the liquidity and efficiency of credit and financial markets.

What solvency problems mean?

- The industry would have a smaller capacity to spread risks.
- The supply of insurance would fall.
- Prices will increase.
- The industry would be unable to cover its obligations to policyholders.
- The industry would channel fewer funds to credit and financial markets.

How solvency problems could arise in the insurance industry?

- Increases in Claims by Policyholders.
- Collapse of Asset Markets
- Severe Losses of Capital as a Result of downturn in the profitability
- Fraud and mismanagement

What their possible major economic impacts could be?

- Undermine the industry's beneficial financial intermediation.
- Reduce the supply of insurance
- Raising the price of insurance
- Interrupt the normal flow of funds through financial markets.

How solvency regulation of insurers can prevent such problems?

- Insurance regulators should strengthen solvency regulations governing the following areas:
- Strong Capital and surplus requirements
- Solvency margin requirements
- Prudent Investment risks management policies.
- Establishing measures of financial strength
- Statutory financial reporting
- Financial examinations.

How solvency regulation of insurers can prevent such problems?

- Monitoring Fraudulent activities by insurers and consumers.
- Accounting for uncertainty regarding reinsurance recoverables.
- Corrective actions for financially weak insurers
- The ability of guaranty funds to meet their obligations to the policyholders of insolvent insurers

Conclusion

- Strong Solvency regulations are necessary in order to prevent and reduce the risk of solvency problems in the insurance industry that can negatively impact the economy.
- Strong Regulations are necessary for promoting sound business practices in order to protect policyholders and shareholders from losses arising from the insolvency of insurance companies.