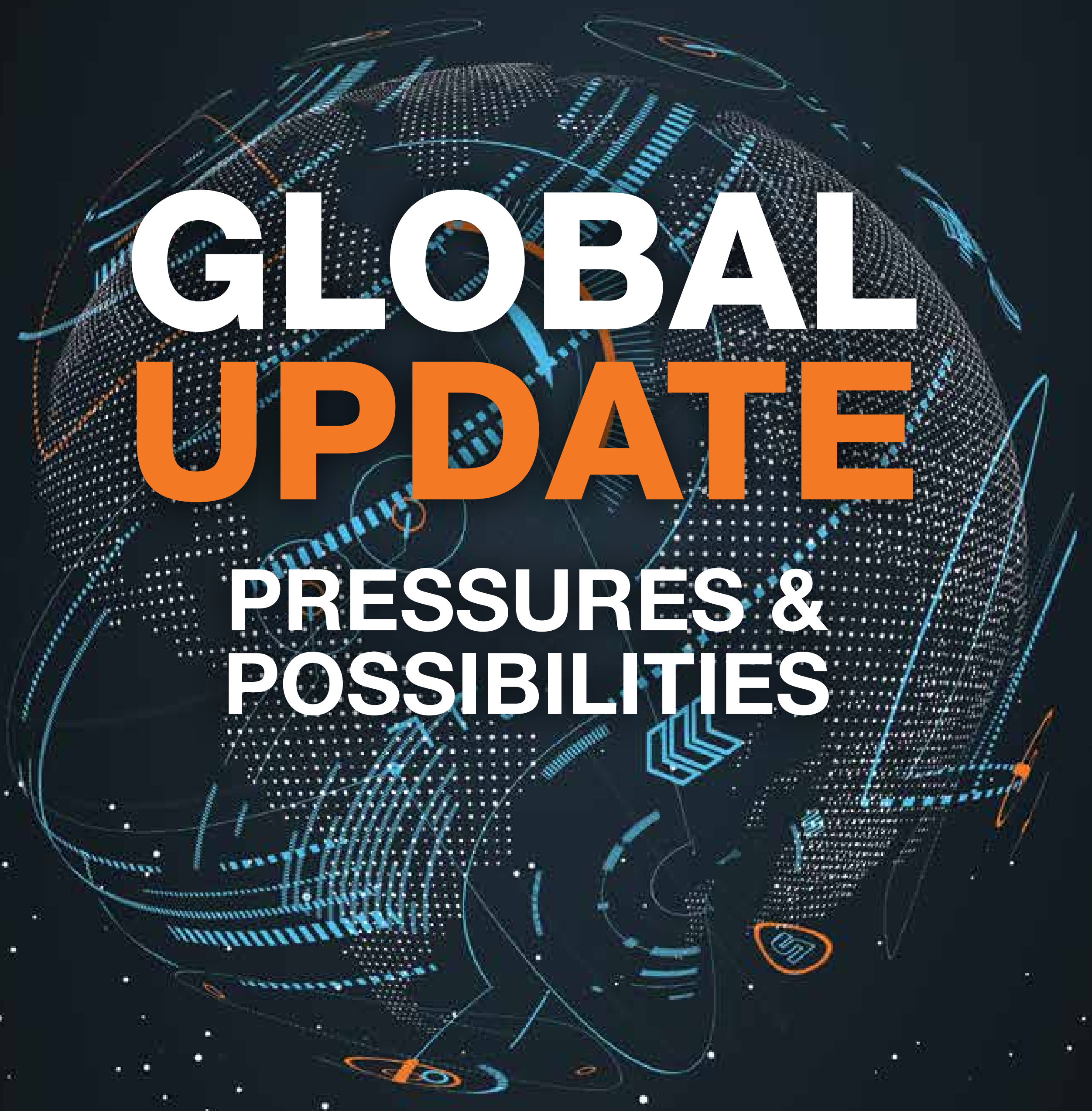

GLOBAL UPDATE

PRESSURES & POSSIBILITIES

By Jennifer C. Rankin

What effect will changing—and challenging—economies, politics, and regulations have on life insurance companies worldwide? For some particulars, read on.

These are both promising and challenging times for life insurance companies around the world, which are coping with low interest rates, political pressures, regulatory changes, and more. Although profitability is under pressure, every region offers some sort of opportunity. Forward-looking insurers are monitoring developments and positioning themselves for success.

Let's start with the global economy. In the report, *Global Insurance Review 2017 and Outlook 2018/19*, Swiss Re analysts say that although a recession is unlikely this year, we can expect only moderate economic growth. For 2018, they expect real gross domestic product (GDP) to exceed two percent In the U.S. and Euro area, to slow to about one percent in Japan, to reach roughly 1.5 percent in the U.K., and to hit 6.8 percent in China. "Emerging markets are performing better, especially in Asia, but growth in commodity-exporting regions is also accelerating as energy and metal prices rise. Inflation is fairly subdued globally, but with low unemployment rates in some countries—in the U.S., U.K., and Germany, for example—the risk [of] inflation needs to be monitored."

Trouble in China, however, could dim prospects for global economic growth, according to Swiss Re. "A hard-landing in China, the risk of which remains at about 20 percent, would significantly impact global growth. A key concern here is elevated corporate debt levels. In addition to [this risk], China's financial market liberalization efforts could increase its vulnerability to external shocks. For example, should the [U.S. Federal Reserve Bank] accelerate monetary tightening, there could be capital outflows which would pressure the renminbi."

Analysts expect interest rates to remain quite low in many markets. "The European Central Bank (ECB) is expected to increase the repo rate in 2019 at the earliest and the Bank of Japan (BoJ) will likely keep rates close to zero over the forecast horizon. The U.S. [Federal Reserve Bank] is expected to continue to raise rates gradually, three times in both 2018 and 2019." Many central banks also are scaling back on the asset purchase programs they launched almost a decade ago in response to the global recession.

For life insurance and annuity companies, interest rate increases cannot come fast enough. Higher interest rates reduce rate compression, which occurs when insurers reinvest the low yields from their fixed income portfolios into assets that return even lower yields in a sort of death spiral. They also improve product profit spreads. Moreover, as product performance improves, the consumer enjoys a better value proposition. Should interest rates rise significantly this year, the benefits will not accrue immediately. That is because it will take a few years for current assets to mature and to be reinvested at the higher rates.

INDUSTRY PERFORMANCE

According to Swiss Re, global life premiums grew about three percent last year—up from two percent in 2016—supported by the robust performance of savings products in emerging markets, particularly in Asia. Swiss Re predicts that premiums will increase almost four percent annually over the next two years.

In the advanced markets—North America, Western Europe, developed Asia-Pacific, and Oceania—profitability remains under pressure. "In the ongoing low interest rate environment," say Swiss Re analysts, "low government bond yields remain a significant headwind for life insurers. The challenge is particularly pronounced in Europe and Asia, where over 40 percent of surveyed insurers cite low yields as their top investment portfolio concern. This reflects the legacy of existing life insurance obligations with embedded guarantees, and the restricted ability to offer sufficiently attractive returns on new business to compete with alternative retail savings products. According to surveys by Standard Life,

Swiss Re predicts that [global life insurance] premiums will increase almost four percent annually over the next two years.

many insurers in Europe, Japan, South Korea and Australia are barely generating sufficient investment returns to meet their obligations to policyholders."

To offset the low interest rate environment, insurers need higher investment returns. To secure just that, they are investing in riskier and less liquid asset classes. Almost 60 percent of insurers in developed Asia-Pacific, for example, say they intend to increase overall investment risk, according to Swiss Re.

The emerging markets—Central and Eastern Europe (CEE), emerging Asia, Latin America, Africa, and Middle East, Central Asia and Turkey—continue to provide growth opportunities for insurers, with emerging Asia driving premium growth. Prospects finally are improving in Latin America and Africa, where oil and commodity prices are strengthening. Swiss Re expects life premium growth in the emerging markets to achieve 12 percent this year and 11 percent in 2019.

While local-national business conditions and government policies are unique, insurers worldwide currently face three overarching challenges—rising protectionism, evolving regulations, and international standards.

EY put the C-suite on notice with its *Top Priorities for U.S. Boards in 2018* report, which emphasizes the importance of anticipating and planning for economic, geopolitical and regulatory changes. "In the first few months of 2018, U.S. stock indexes experienced the highest levels of volatility since 2014. Long-standing trade agreements, tax and regulatory systems, and defense treaties are being renegotiated, transformed or absolved. And the International Monetary Fund (IMF) has warned that rising U.S.-China trade restrictions are threatening to derail growth and undermine confidence."

When the consultancy asked executives what they believe to be the greatest near-term risk to the growth of their core business, they said political uncertainty (48 percent), geopolitical tensions (43 percent), changes in trade policy and protectionism (36 percent), disruptive forces (36 percent), and currency movements (35 percent).

NATIONAL FERVOR

Protectionism is a recent and important development in countries around the world—the U.S., the U.K. and a handful of Western European countries, in particular. "After years of increasing globalization," write the Swiss Re analysts, "the political landscape/debate has become increasingly impacted by protectionism (U.S.) and compartmentalization (Brexit). Escalation to an outright trade war has the potential to harm global growth if the U.S. stance becomes more aggressive. Fortunately, there is no uniform increase in protectionism globally. For example, in Latin America the trend is toward more liberal trade regimes."

Political analysts say voters supported Donald J. Trump for U.S. president in 2016 in part as a backlash against globalization, which compels corporations not only to seek new markets, but also cheap labor, light regulation, and low taxes abroad. He and his supporters also believe longstanding American trade policies have contributed to the country's US$ 500 billion+ annual global trade deficit in goods and services. In a recent *New York Times* op-ed, Peter Navarro, assistant to the president for trade and manufacturing policy, compares low U.S. tariffs on imports to the high tariffs imposed by Japan, Canada and other countries on U.S. exports. He also expresses concern about countries that are not fully meeting their NATO funding commitments.

"Going forward," writes Navarro, "President Trump will pursue two goals on behalf of the American nation and people. First, trade must be not only free but also fair and reciprocal. Second, President Trump reserves the right to defend those industries critical to our own national security." During the past several months, the U.S. has withdrawn from the Trans Pacific Partnership (TPP), raised tariffs on imports from Canada and China, and insisted upon a renegotiation of the North American Free Trade Agreement (NAFTA).

Voters in the U.K. are also in a nationalistic mood. In June 2016, 51.9 percent of the country's participating electorate voted to leave the European Union (EU), the largest single market in the world, in a moved dubbed the Brexit. Negotiations with the EU officially started in June 2017, with the goal of completing the withdrawal agreement by October 2018. The official exit day is March 29, 2019, according to the European Union (Withdrawal) Act of 2018.

The repercussions of Brexit are beginning to unfold. Shortly following the vote, the Bank of England introduced quantitative easing (QE) and lower interest rates, devaluing sterling and allowing a rise in inflation that outpaced wage growth for most of last year.

According to Swiss Re analysts, "Passporting arrangements between the U.K. and the rest of the European Union (EU) will no longer apply post Brexit, and insurers are preparing their organizations accordingly. Without some form of transitional arrangement, U.K. insurance market premiums could fall by around eight percent. In the event of a cliff-edge exit, the premium loss for the U.K. market could be almost double that." Passporting rights allow banks to reside in the U.K. and sell their products and services (including insurance) throughout the EU.

At present, billions of euros in cross-border insurance policies are on the books. On June 28, 2018, the European Insurance and Occupational Pensions Authority (EIOPA) reminded insurers in the EU that they must tell their customers about the consequences of Britain's departure from the EU. "National supervisory authorities are required to ensure that insurance undertakings and insurance intermediaries take appropriate contingency measures to ensure the continuity of services for cross-border insurance contracts," EIOPA said in a statement. "Customers should be made aware in a timely manner of the implications of these measures both for existing and for new contracts concluded before the withdrawal date."

According to the *New York Times*, Britain and the EU have agreed on a transition deal to 2020 to ensure business continuity. Until it is ratified, however, there is a risk of a disorderly Brexit. On June 27, the Bank of England (BoE) said that insurers in Britain and the EU may not be able to service their existing contracts—pay claims or receive premiums, for instance—without local authorization after March 2019 without a transition. "This could affect around 27 billion pounds (US$ 35 billion) of insurance liabilities and 10 million U.K. policyholders," says the BoE, as reported by the *New York Times*. "Around 55 billion pounds of insurance liabilities and 38 million European Economic Area policyholders could also be hit." The British government is willing to extend authorization of EU financial firms operating in the country beyond

LOOKING AHEAD THE EMERGING MARKETS

Based on the latest available data, Swiss Re analysts estimate that life and health premiums in the emerging markets rose by about 17 percent in 2017. Performance varied across regions. Sustained robust growth in emerging Asia was the most important driver, supplemented by a healthy recovery in Central and Eastern European (CEE) markets. On the other hand, growth remained weak in Africa, and decelerated sharply in Latin America and the Middle East.

The outlook for insurance in the emerging markets remains favorable, with total insurance premiums projected to expand by more than 10 percent in both 2018 and 2019. Of that, non-life premium growth is forecast to be steady at between six and seven percent, while life premiums are projected to increase by double-digit rates.

After healthy gains in both 2016 and 2017, life premium growth in the emerging markets is expected to ease back to its trend rate of around 10 percent over the next two years. China will continue to dominate, supported by a favorable policy environment. The Chinese government has set a target to grow total insurance (non-life and life) penetration to five percent by 2020 from around three percent in 2014. Supportive government policies to boost demand include tax rebates as well as a drive to promote protection, health and pension products, which could result in a changing portfolio mix for insurers. In the rest of emerging Asia, life premium growth is expected to be steady as economic conditions stabilize. It is noteworthy that insurers in the region are promoting protection products more, given the still low interest rates.

Life premiums in Latin America are expected to increase by three to four percent per annum in 2018 and 2019, helped by a modest economic recovery in Brazil. Growth in Colombia, Chile and Peru will remain solid. In Mexico, recent changes in income tax laws provide greater tax benefits on long-term savings products, which should boost demand.

In CEE, lower growth of around five to six percent is expected in the coming two years, reflecting the large share of Russia. Elsewhere in the region, life business should rebound assuming steady economic growth.

In the Middle East, low penetration rates and increasing awareness should continue to boost demand, particularly in the UAE and Saudi Arabia.

In sub-Saharan Africa (SSA), life premium growth is forecast to stay low at around two to three percent given the weak economic recovery in South Africa, as low consumer confidence affects willingness to lock into long-term life insurance saving products. Elsewhere in Africa, particularly in the East and West where life penetration levels remain very low, the outlook for the sector is brighter.

Source: Swiss Re Institute

March 2019 to ensure continuity in contracts; the EU, however, has not indicated that it will reciprocate. According to the *New York Times*, some insurers operating in Britain are dealing with Brexit uncertainty by opening new hubs in the EU, but they may not be able to transfer all European contracts to them before March 29, 2019.

In the report *Brexit: What Now for U.S. Insurers?* Andrew N. Mais, senior manager, Deloitte Center for Financial Services, takes a close look at the possible ramifications of the Brexit. While it will affect the U.K. and Europe more directly and immediately, he believes the Brexit definitely will be felt outside those regions—particularly by companies with global operations. "It is too early to call out the detailed implications of [the] Brexit and the timeline for those changes," he writes. "However, it does raise a great deal of uncertainty for companies and increases the challenge of doing cross-border business. The challenges are numerous, with strategic, financial and operational implications." Although the report cites implications for U.S. insurers, they are applicable globally.

According to Mais, the Brexit has several financial ramifications. First, it increases pressure on central banks to maintain low interest rates. This prolongs the period of low investment returns, which requires revisions to investment strategies and allocations. It also increases the need for tighter asset liability management as well as improved underwriting and pricing models.

The Brexit may cause foreign exchange and currency volatility, which has clear short-term earnings implications for foreign insurers with EU operations. Possible increased collateral requirements to cover open positions may lead to liquidity challenges. Hedging strategies may be impacted as well. Finally, the cost of raising capital may rise because of associated volatility and possible reduction in available funds.

In addition, the Brexit will increase regulatory uncertainty for the foreseeable future, according to Mais. Prior to the Brexit, the prospect was for a lengthy debate on various measures, including capital standards; this vote may extend that process. If prolonged uncertainty becomes the new normal, there will be a concomitant increase in risk.

Regulatory fragmentation is another concern. Strong national regulators may reassert control over country-specific regulatory requirements, slowing the process toward creating a level playing field. And meeting the requirements of differing regulatory authorities may increase the cost of compliance.

A third concern is regulatory arbitrage. At a time of heightened volatility and uncertainty, regulators may drop standards because of the need to make their countries attractive as a place to do business. This may increase the risk profile of insurers, making it more important to maintain effective risk management and not rely on local regulators.

In addition to these financial and regulatory challenges, insurers may have to address various operational issues from the Brexit. Examples include:

- **Tax Changes**. If the U.K. stops adhering to global tax policies previously agreed upon by the EU, such as base erosion and profit shifting (BEPS) or cross-border cooperation (CBC), insurers will need to revise their business practices. (Editor's note: The Organization for Economic Co-operation and Development (OECD) and Group of 20 (G20) nations are sponsoring the BEPS project, which is focused on corporate tax transparency and the risks to tax revenues, tax sovereignty and tax fairness posed by corporation engaging in BEPS behaviors. These behaviors exploit gaps and mismatches in tax rules to artificially shift profits to low or no -tax locations where there is little or no economic activity.)
- **Business costs**. Insurers must review current policy terms and conditions, then prepare and distribute new policy information based on U.K. or EU location. Supplier costs may rise with possible loss of open EU market. Insurers may face uncertainty on Solvency II equivalence for the U.K. Finally, insurers may need to reconfigure information systems to reflect the new reality—assets may need to be differentiated between U.K. and EU, for example.
- **Company operations**. Passporting arrangement changes may affect product distribution and regulatory costs. Probable changes in the right to work cross-border in all current EU countries may lead some insurers to relocate or bilocate to serve their client base properly. Bilocation may result in a need for separate boards and governance structures. Relocation or bilocation could raise tax issues, including employment tax. Insurers may need to provide new training for staff based on the domicile.

Current protectionist tactics mostly revolve around the movement of goods and people. Where does that leave services—more specifically, financial services? For decades now, globalization has ruled in the sector. Spurred by the successes of the original American International Group (AIG) and multinational behemoths of Europe, the opening of formerly closed markets like China, and the limitations of mature markets, life insurance companies around the world began to explore markets outside their own back yard. International accounting and regulatory standards began to emerge in their wake. Some industry analysts wonder what might happen to these international agreements in the face of increasing nationalism and protectionism.

After years of increasing globalization, the political landscape/debate has become increasingly impacted by protectionism and compartmentalization.

REGULATORY CLIMATE

A good example of international cooperation is IFRS 17. In May 2017, the International Accounting Standards Board (IASB) wrapped up a decades-long project to create a new international accounting standard for insurance contracts. The new standard—IFRS 17—replaces IFRS 4, which allowed different jurisdictions to employ a wide variety of accounting practices. IFRS 17 takes effect on January 1, 2021. Some countries—most notably the U.S.—have chosen not to adopt it. The U.S. Financial Accounting Standards Board (FASB) will make targeted improvements to its existing generally accepted accounting procedures (GAAP) methodology instead.

IFRS 17 introduces a common, global, high quality standard for the recognition, measurement, presentation and disclosure requirements for insurance contracts. The primary goals are standardization and transparency. Although the U.S. has opted to stick with GAAP, the FASB and the IASB continue to work together wherever possible.

IFRS 17 creates a standardized and more transparent approach to measuring insurance liabilities. The new standard does come with challenges. First, it is a major departure from current accounting practice. In addition, life insurers with long-term liabilities and embedded policyholder guarantees are likely to face more volatility in reported equity capital and profits. Economic mismatches between assets and liabilities will become more visible.

From an operational standpoint, IFRS 17 is likely to require a significant investment in new data capture, systems and processes. "For international insurers with overseas subsidiaries," write the Swiss Re analysts, "the added complexity of having to prepare financial statements under various valuation frameworks—GAAP, Solvency II, IFRS and more—will only add to the operational challenges. According to a recent global survey, over 60 percent of insurers plan to invest in both new accounting and actuarial systems to meet the demands of the new framework, although only 15 percent have actually started implementation projects."

IFRS 17 is just one business issue with which life insurers around the world must grapple. Although it has been almost a decade since the global financial crisis, its repercussions are still with us. As a result, regulators continue to push for consumer protections; solvency, accounting and reporting

LOOKING AHEAD THE ADVANCED MARKETS

Last year, life industry performance in the advanced markets was mixed, according to a Swiss Re analysis of the latest data.

In **North America**, premiums are estimated to have declined last year, driven mainly by lower premium income in the U.S., particularly of individual annuity premiums due to uncertainty around the finalization and implementation of new Department of Labor (DOL) fiduciary rules. In Canada, on the other hand, premium development contributed positively to regional performance.

For **Western Europe**, estimates indicate that after adjusting for inflation, life premium income stagnated in 2017. Based on partial-year data, real premiums are estimated to have remained flat in the U.K. and to have declined in France. In Germany, premiums fell slightly, due largely to weaker sales of single-premium business.

In **developed Asia-Pacific**, life premium income is estimated to have risen modestly in 2017 (about one percent), driven by a sharp pick-up in Japan following a decline in 2016, and strong growth in Hong Kong, Singapore and Taiwan. In Hong Kong, individual life policies, especially non-linked whole life and non-linked endowment products, remain popular with mainland China residents.

Source: Swiss Re Institute

standards; global frameworks; and more. The most pressing of these are the General Data Protection Regulation (GDPR), Solvency II, principle-based reserving (PBR), ComFrame, and Own Risk and Solvency Assessment (ORSA).

One of the most significant new laws is the General Data Protection Regulation (GDPR) that the European Union (EU) implemented in May. This piece of legislation, which affects anyone doing business with EU citizens, expands the EU's existing protection principles governing citizens' data. Its core objectives are to strengthen individuals' rights, give increased attention to cyber security and technological capacity, and extend supervision and sanctions across consumer data. A major GDPR provision requires companies to request consent to contact an individual.

GDPR compliance will affect almost every area of insurance company operations. Failure to comply could result in significant fines and reputational damage. The changes having the most effect on the insurance sector, according to EY's October 2017 *Global Insurance Trends Analysis,* are:

- **Enhanced data subject rights**. The GDPR will create multiple new rights for individuals and strengthen some existing rights, including the right to be informed about how personal data is being used; to be forgotten when personal data is no longer necessary in relation to the original purpose or when the individual withdraws consent; to have access to his/her personal data and to transfer it to another controller; and to question automated decision making and profiling.
- **Comprehensive extra-territorial applicability**. GDPR applies to all companies processing the personal data of EU-based subjects, regardless of the company's location. It imposes restrictions on personal data transfer outside the EU to non-EU countries or international organizations so that the level of protection of individuals covered by the GDPR is not undermined.
- **Significantly high penalties**. Organizations in breach of GDPR can be fined in two ways. For unlawful international transfers or the inability to respond to Data Subject Access reports, a company faces a fine of four percent of its annual turnover, with a minimum fine of 20 million euros. For a failure to report breaches within 72 hours, a company faces a fine of two percent of annual turnover, with a minimum fine of 10 million euros. The most serious infringements include not having sufficient customer consent to process data.
- **Enhanced accountability**. Organizations must prove they are accountable by adopting privacy-by-design (designing data protection into business processes and systems); by establishing a culture of monitoring, reviewing and assessing data processing procedures; and by undertaking Privacy Impact Assessments when conducting risky or large scale processing of personal data.
- **Data protection office (DPO)**. If an organization conducts large scale systematic monitoring or processes large amounts of sensitive personal data, it must appoint a DPO.
- **Breach notifications**. Organizations must notify authorities of data breaches without undue delay or within 72 hours, unless the breach is unlikely to be a risk to individuals. If there is a high risk to individuals, those individuals must be informed as well.

There are three major areas of operational impact on insurers, according to EY. The first is managing data transfer between EU and non-EU states and organizations. The second is seeking and justifying the collection, storage, access and retention of data held in a variety of ways, in multiple locations, and often held/provided by third parties. Finally, restructuring of process designs and improving data usage explicability. Factoring in data protection has the potential to disrupt everything from marketing materials to customer service training. Exacerbating these challenges is the presence of legacy contract engines and systems in most companies, many of which do not provide a single customer view. These systems can be hard to change and many have a low quality of data.

CAPITAL IDEAS

Rigorous solvency requirements are unfolding around the world. These include Solvency II in the European Union (EU), various risk-based capital (RBC) regulations, and high capital requirements in general.

In January 2016, the Solvency II (SII) directive took effect in Europe. SII introduced more stringent capital adequacy requirements for assets as well as specific measurement and disclosure/reporting requirements. Over the last 18 months, "large insurers have generally coped well," according to Swiss Re analysts. "Beyond the enhanced compliance requirements, insurance companies have sought to mitigate the impact of credit and government spread volatility on their solvency ratios through asset reallocation, asset/liability management actions and a new design for their asset management mandates. Most of the major European insurance groups have increased their solvency positions compared with their reported capital positions."

In addition, several countries have implemented second-generation and/or high RBC standards recently—among them, Singapore, China, Hong Kong, Thailand, and Mexico. Last year, the China Insurance Regulatory Commission (CIRC) announced it was requiring insurance companies to conduct internal reviews of solvency data to ensure accuracy and compliance; this requirement aims to rectify issues of false and incorrect data as well as to strengthen supervision, risk management, and data quality standards.

> **One of the most significant new laws is the General Data Protection Regulation (GDPR) that the European Union (EU) implemented in May.**

The CIRC also has established an advisory committee for the China Risk Oriented Solvency System (C-ROSS). The committee will develop and implement C-ROSS and work on international coordination.

Last year, 46 states in the U.S. adopted the new principle-based reserving (PBR) methodology, the purpose of which is to show an insurer's true risks and obligations. The previous formulaic approach often resulted in redundant reserves for many products. Insurers have until January 2020 to transition to PBR; at that time, all new policies for term life, universal life, whole life and variable life must follow the new reserving rule. "The impact on the primary [life insurance] industry is difficult to evaluate, not the least because of the heterogeneity of current reserve financing practices," according to Swiss Re. "For some products like term life, PBR is expected to be favorable via lower reserving needs. Consequently, some commentators expect premiums to be lowered as a result. At the same time, the high cost of implementation, even if spread over time, may be challenging to absorb, especially for smaller insurers."

In the meantime, the International Association of Insurance Supervisors (IAIS) continues its work on a risk-based global insurance capital standard, with full implementation to begin in 2019, after testing and refinement with insurance supervisors and internationally active insurance groups (IAIGs). The final requirements are on track to be issued this year. The project is called "Common Framework for the Supervision of Internationally Active Insurance Groups" or ComFrame.

ComFrame is built and expands upon the high-level requirements and guidance currently set out in the IAIS Insurance Core Principles (ICPs), which generally apply on both a legal entity and group-wide level.

The ICPs are the globally accepted requirements for the supervision of the insurance sector. They are structured to allow a wide range of regulatory approaches and supervisory processes to suit different markets and the range of insurance entities and groups operating within these markets.

According to the IAIS, "IAIGs, however, need tailored and more coordinated supervision across jurisdictions due to their complexity and international activity. This necessitates a specific framework to assist supervisors in collectively addressing group-wide activities and risks, identifying and avoiding regulatory gaps, and coordinating supervisory activities under the aegis of a group-wide supervisor."

A key part of the ComFrame project is the development of a risk-based, global insurance capital standard (ICS) for IAIGs. In June 2017, the IAIS executive committee adopted ICS Version 1.0 and began to field test it. The committee recently adopted ICS Version 2.0, which will undergo a five-year testing period, followed by an implementation phase.

According to Fitch Ratings, the IAIS also is working on a new method for assessing systemic risk. The existing methodology takes an entity-based approach, which focuses on the failure of an individual insurance company and what effect that failure may have on the wider financial markets. The IAIS wants to take an activities-based approach, believing it will more thoroughly address the issues.

The Group of 20 (G20) nations is monitoring systemic importance as well. Following the 2008-9 financial crisis, the G20 established the Financial Stability Board (FSB). Shortly thereafter, the FSB designated nine insurers—AIG (U.S.), Allianz (Germany), Aviva (U.K.), AXA (France), Generali (Italy), MetLife (U.S.), Ping An (China), Prudential Financial (U.S.) and Prudential (U.K.)—as global systemically important insurers (G-SIIs). There have been no changes to the list, which the FSB updates annually.

In the meantime, the concept of systemic importance is under siege in the U.S. In 2010, again in response to the financial crisis, then-president Barack Obama signed into law the Dodd-Frank Wall Street Reform and Consumer Protection Act. Dodd-Frank established the Financial Stability Oversight Council (FSOC), which designated American International Group (AIG), Prudential Financial and MetLife as non-bank systemically important financial institutions (SIFIs). MetLife fought its SIFI designation; in 2016, a U.S. district court judge rescinded it.

Last year, current U.S. president Donald Trump issued an executive order to review the SIFI designation process used by the FSOC. In November 2017, the U.S. Department of the Treasury published a report in which it stated that it considers designation as a U.S. SIFI "to be a 'blunt instrument' for addressing potential risk to financial stability." As a result, according to Fitch Ratings, the FSOC has begun to consider using an activities-based framework to assess the potential risk posed by non-bank financial companies. In September 2017, the FSOC rescinded AIG's SIFI designation; it is expected to re-evaluate Prudential Financial's SIFI designation at any moment. There appears to be no legal mechanism, however, by which U.S. federal regulators could enforce G-SII rules on AIG, MetLife or Prudential Financial, even though they each remain on the current G-SII list, according to Fitch Ratings.

Insurers face growing regulatory pressures to improve their risk management practices. A major concept in play is Own Risk and Solvency Assessment (ORSA), which requires insurers to evaluate how much of their capital is subject to what risk levels and to submit written documentation to regulators. In some jurisdictions, the term ICAAP (International Capital Adequacy Assessment Process) is used to refer to ORSA initiatives. The IAIS has introduced a set of practices for enterprise risk management (ERM) that includes an ORSA requirement. In the U.S., there is the National Association of Insurance Commissioners (NAIC) ORSA initiative, which took effect in January 2015. In addition, Pillar 2 of Solvency II sets ORSA benchmarks. Finally, insurance regulators in various countries—among them, Malaysia, Singapore and Australia—have introduced ERM standards with an ORSA requirement. In 2014, Canadian insurers began to comply with the ORSA requirements set by the country's Office of the Superintendent of Financial Institutions (OSFI). In addition to these regulator-driven ERM schemes, insurers have their own longstanding ERM processes.

GLOBAL ACTIVITY

Countries around the world are taking steps to enhance or implement risk- and economic-based solvency regulation regimes. They also are embracing international best practices, fine-tuning asset and liability matching (ALM), updating mortality tables and more. Among the examples cited in EY's October 2017 *Global Insurance Trends Analysis* and various news feeds are:

- **Africa**. In August 2017, South Africa enacted Financial Sector Regulation, a new law that paved the way for the 2018 enactment of Insurance Bill, a risk-based capital (RBC) framework. And a number of other countries—among them, Kenya and Nigeria—also plan to move to RBC solvency frameworks.
- **Brazil**. Insurers are working to implement enterprise risk management (ERM) frameworks aligned with Solvency II. Industry watchers expect Brazil's regulator SUSEP to implement Own Risk and Solvency Assessment (ORSA) requirements by 2019.
- **Canada**. Last year, Canada fully implemented its E-21 Operational Risk Management guideline, which provides consolidated guidance for operational risk management across all federally regulated financial institutions (FRFIs).
- **European Union**. The European Insurance and Occupational Pensions Authority (EIOPA) continues to draft and publish for review sets of advice to the European Commission (EC) on specific parts of Solvency II.
- **India**. Last year, the Insurance Regulatory and Development Authority (IRDA) revised rules to bring greater transparency in the sale processes of web aggregators. It also eleased more stringent rules on time lines for investigation and settlement of claims."
- **Japan**. The country's new standard mortality table took effect in April 2018.
- **Mainland China and Hong Kong**. Recently released final ALM standards for life and non-life insurers. Work is underway at Hong Kong's new regulator Insurance Authority (IA), which was launched last year. The China Insurance Regulatory Commission (CIRC) continues the comprehensive review of C-ROSS (also known as C-ROSS Phase 2) it started last year.
- **Mexico**. The new (2017) insurance and surety institution law mandates that insurers adopt standards in line with Solvency II for capital and reserves, corporate governance and financial disclosures. Post-implementation of this new solvency regime, Mexican ORSA reports will include results of the Dynamic Solvency Test.
- **Middle East**. In UAE, insurers must comply with new risk-based solvency requirements by 28 January 2018, and local media reports say that Saudi Arabia is working on a new regulatory framework to strengthen capital requirements.
- **Russia**. The Russian central bank is pushing ahead with its roadmap to introduce a Solvency II-like risk-based model of insurance supervision, possibly by the end of the decade.
- **United States**. The current administration is reviewing major provisions of the Dodd-Frank, including the decision-making process of the Financial Stability Oversight Council (FSOC), and jettisoning others.

As you can see, a major driver for recent regulatory developments is enhancing financial stability in the insurance sector. In 2018, the hard work continues. Countries are implementing local-national regulations and considering international standards. While international standards hold the promise of comparability, transparency and trust, they also pose big challenges to companies' existing structures, strategies and footprints.

Not everyone is on board with global standards. As we saw earlier, FASB is placing a higher priority on improving U.S. GAAP standards than on converging them with the IASB's new global insurance contract standard. In addition, on December 7, 2016, the U.S. House of Representatives passed the Transparent Insurance Standards Act of 2016 (H.R. 5143), a bill defending the U.S. state-based insurance regulatory system against international encroachment. The bill requires the U.S. Treasury Department and Federal Reserve to consult with Congress and state regulators before approving any international insurance standards. "Importantly," according to A.M. Best, "the bill could impact the proposed International Association of Insurance Supervisors' international capital standard that U.S. insurers have opposed. The bill says any international standard that establishes capital standards for insurers must be 'consistent with capital requirements set forth in the state-based system of insurance regulation.'"

Complying with all of these regulatory initiatives is very demanding from an operational and cost standpoint. In addition, there are overlapping mandates from different regulatory bodies, which often are in conflict and/or competition with each other. Multinational insurers face not only these challenges, but also the complexity of cross-border supervision and regulation.

They also face the rising cost of regulatory compliance. In 2017, Accenture surveyed 150 compliance officers at banking, insurance and capital markets firms in 13 countries in North America, Europe, Asia-Pacific and Latin America. Eighty-nine percent of these executives expect continued cost increases in their compliance departments over the next two years. Of those, nearly half (48 percent) anticipate increases of 10 to 20 percent and nearly one in five expect increases of more than 20 percent.

LOOKING AHEAD

So, what's in store for life insurers around the world for the remainder of the year and for 2019? Munich Re expects life insurance growth rates to normalize at an average of 5.6 percent (3.9 percent in real terms) over the next two years.

A major driver for recent regulatory developments is enhancing financial stability in the insurance sector.

"USA and China are the drivers of this trend," according to its recently published *Insurance Market Outlook for 2018/2019*. "According to provisional figures, in 2017 premiums in the U.S. fell by more than four percent in real terms. The reason for this was a decline in annuity business due to political and regulatory uncertainties. For 2018 and 2019—supported by rising interest rates—we are expecting a return to positive growth, with a significant impact on global figures. With a global market share of close to 20 percent, the U.S. is currently the most important life insurance market. China already ranks third behind the U.S. and Japan, with a market share of over 12 percent. Given the catch-up potential that continues to be seen here, it is no wonder that China's high growth rates of almost 20 percent (over 15 percent in real terms) are also an important driver for global premium growth.

"In Western Europe and the developed markets of Asia, we project moderate growth as a result of sustained low interest rates, whereas in the emerging markets—with the exception of sub-Saharan Africa, which is influenced by developments in South Africa—we are expecting the trend to be toward higher growth. In Eastern Europe, the extremely high growth rates seen in Russia in past years are likely to slowly level off, while in Latin America we expect to see a recovery again, following low growth in 2017 due to recession."

Swiss Re believes the emerging markets will play a significant role moving forward. "Global life insurance premiums in real terms are forecast to rise by around four percent annually over the next two years. The major driver will remain the emerging markets, where stable, robust economic growth; expanding populations; urbanisation; and, a rising middle class underpin the positive outlook." It expects life premium growth in the emerging markets to be around 10 percent in 2018 and 2019; a more modest one to two percent in the advanced markets, after adjusting for inflation; and two to three percent in developed Asia-Pacific.

As you can see, life insurers have a lot on their plates. Political upheavals around the world are changing some of the ground rules for trades in goods and services. Some countries are embracing global regulatory standards while others prefer to stick with their own rules. The persistent low interest rate is pressuring profitability in virtually all markets. Nevertheless, favorable demographics and loosening restrictions on entry are providing opportunities for success worldwide. Resource will keep you posted as events unfold.

RESOURCES FROM SCOR

SCOR: Creating a Community of Trusted Partners

SCOR Global Life recently launched SCOR Life & Health Ventures. Through this venture, SCOR reinforces its commitment to innovation at the service of its clients, providing financing capacity and partnering with innovative companies around the world. The venture's mission is to create a community of trusted partners that will bring value to SCOR Global Life's clients by offering cutting-edge technology in this continuously-evolving Life insurance environment.

These strategic partnerships and investments will further enable SCOR Global Life and its clients to develop innovative offerings for existing and future policyholders by:

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- Improving the health and wellness of policyholders by empowering them with their health;
- Enhancing the underwriting process by using new data sources and predictive models;
- Enabling digital distribution by supporting distribution professionals and implementing direct-to-consumer offerings for Life insurers;
- Developing tailored solutions addressing specific client needs from the sales process to claims management.

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For more information, visit
www.scor.com/en/scor-lh-ventures.

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Available data:

- US Property/Casualty, Life/Health and Health
- US Market Share
- US Reinsurance
- US Loss Reserves
- US Investments
- US Expenses
- Global Life and Non-Life
- Solvency II
- Non-US Region-Specific (Canada, UK, Asia-Pacific, Latin America, Middle East North Africa)

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