insurance europe

Insight Briefing

Protectionism creates dangerous risk concentrations

Open (re)insurance markets are the only way to remove the danger

International (re)insurers play a crucial role in enabling economic growth around the world by offering financial protection and dispersing insured risks across a global network.

International (re)insurance means that the financial impact of natural and man-made disasters is not concentrated within the economies in which they occur. Of course, this is the central objective of insurance: to share risks, so that losses are more easily absorbed.

To be able to protect and contribute towards economic growth, foreign (re)insurers need to be authorised by regulators to do business and to be treated the same as local companies.

Numerous examples

Global trade dynamics have changed over the past year. Traditional free-trade champions are re-evaluating agreements, and the use of protectionist measures continues to increase in some jurisdictions. As a result, free-trade environments for (re)insurers are under threat.

Regional protectionist measures in (re)insurance actually create dangers for the very economies they aim to protect. This is because they concentrate risk, rather than allowing it to be spread throughout the global reinsurance market, which is only possible if markets are open.

A common example is compulsory cessions or "rights of first refusal". These measures oblige local insurers to cede their risks to local, often state-owned, reinsurers. They are in force in a wide range of African countries, as well as in South America — Brazil, Ecuador and Argentina — and Asia — China and Indonesia.

Some countries are, however, taking positive steps towards opening their markets, even though these steps are often limited, both in terms of scope and ambition. For example, Argentina recently introduced highly welcomed reforms that will gradually re-open the reinsurance market; however, a complete liberalisation is not yet foreseen.

A similar example is India, where the government took significant and welcome steps towards reducing trade barriers and improving access to its (re)insurance market by allowing global reinsurers to establish branches. However, some of these positive changes were then reversed in implementing regulations, which are intended to offer first preference to local market players, such as the state reinsurer, General Insurance Corporation of India (GIC Re).

Elsewhere, the Indonesian government is in the process of transforming Indonesia Re, a national reinsurer, into a "giant" reinsurance company, absorbing a range of existing local (re)insurers. With this increased capacity in Indonesia Re, there is a risk that the government may seek to further increase compulsory cessions from local insurers. In parallel, reductions in the 80% foreign ownership limitation continue to be contemplated by local policymakers, which would further restrict foreign players' access to the Indonesian market.

Increase in trade barriers slows, but continues

In its July 2017 trade development report, the World Trade

Organization found that its members implemented 74 new trade-restrictive measures in the seven months between mid-October 2016 and mid-May 2017. These included new or increased tariffs, customs regulations and quantitative restrictions. While a decrease on its previous review period, this still amounted to more than 10 new measures per month.

In August 2017, the Global Reinsurance Forum — an advocacy body comprised of 13 leading global reinsurers — identified 30 major territories that have either implemented or are in the process of implementing barriers. This is four more than in January 2016.

There is, therefore, a long list of protectionist measures in place that hinder the free transfer of risk across borders.

Limiting progress, increasing costs

When protectionist measures significantly limit the access of foreign (re)insurers to local markets they not only deprive those markets of capital and risk transfer, but also of operational expertise, skills and discipline in underwriting, access to a wider range of products, a strong risk management culture, technological developments and training. All these elements can benefit other companies and sectors, and hence the economy.

In addition, limiting domestic insurers' access to foreign reinsurance constrains their ability to optimise the management of their risk exposures and corresponding capital requirements. This ultimately increases costs for both insurers and their customers. It can also result in the accumulation of risks by insurers faced with less interesting opportunities to cede risks, thereby compromising their underwriting performance.

Dialogue between jurisdictions is key

Most protectionist practices highlighted in this briefing go against the principles of free markets and free cross-border trade. Such principles are, however, of key importance to European (re)insurers. The industry continuously engages with the European Commission and other European policymakers to help identify such practices, so that they can be addressed in bilateral/multilateral trade discussions.

Many of the issues in the Indonesian, Indian and Chinese markets, for example, may be addressed by EU policymakers in discussions on possible trade agreements between the EU and its Asian trade partners. Other issues — such as prudential ones — can be raised in bilateral regulatory dialogues. The industry strongly believes that more dialogue and cooperation at regulatory level will help support more cross-border business.

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EU-US bilateral agreement on (re)insurance: a great trade precedent

The September 2017 signing of the EU-US bilateral agreement on prudential measures for (re)insurance is a successful key milestone after years of technical and, in parts difficult, negotiations. By facilitating cross-border (re)insurance business between Europe and the US, the agreement will directly benefit policyholders, as well as economic growth in both jurisdictions.

One particularly positive aspect of the agreement is the US commitment to completely remove the regulatory collateral requirements faced by European reinsurers placing business in the US on a cross-border basis. This will put them on a level playing field with US reinsurers.

Looking ahead, a swift conclusion of the agreement and implementation of the commitments on both sides will be key. As a general principle, reinsurers from any well-regulated jurisdiction should be allowed to assume risk freely on a cross-border basis, without being subject to local statutory collateral requirements or other measures that have an equivalent effect.

Once implemented successfully, the EU-US bilateral agreement will set a great precedent globally for open markets and free cross-border trade, which are key drivers of economic development and growth.

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