

Highlights of the Life Convention
Dermot Corry

Implications for insurers of a sovereign debt
crisis - Irish case study

March 7th and 14th 2013

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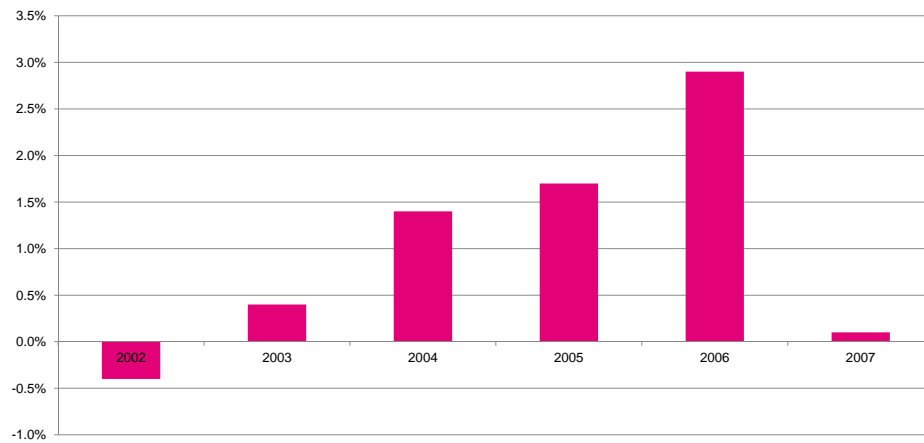
Ireland before the Financial Crisis

- Model Country
- Example to other countries
- Underdeveloped Backwater ➡ High Tech Leader
- “Celtic Tiger”
- Excellent economic statistics

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Irish Government Surpluses up to 2007



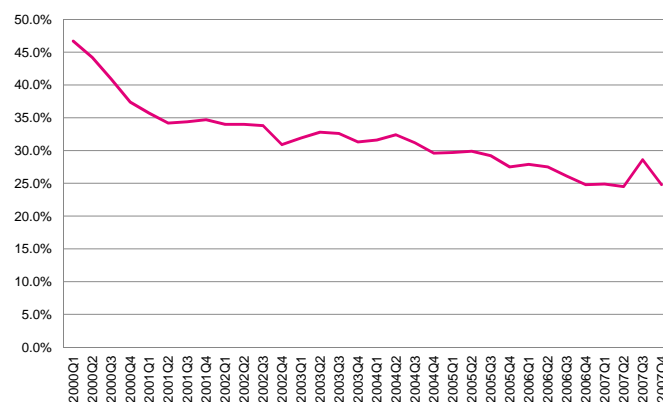
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Very low government debt up to 2007

Irish Government Debt as % GDP

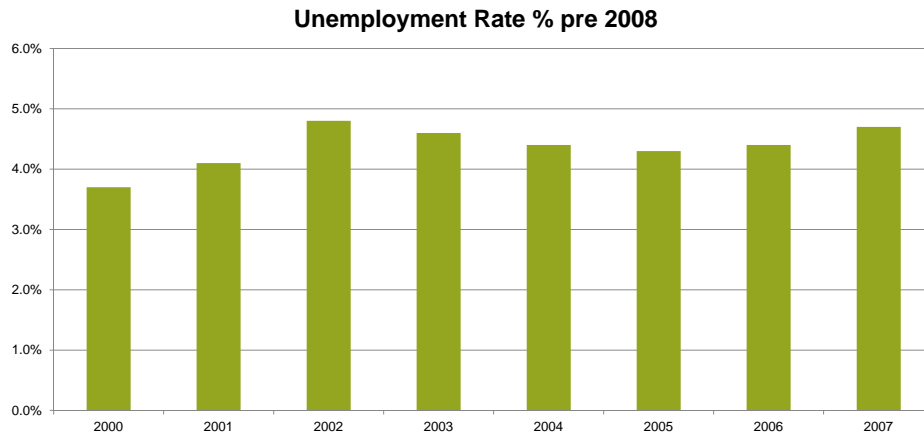


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Low Stable Unemployment

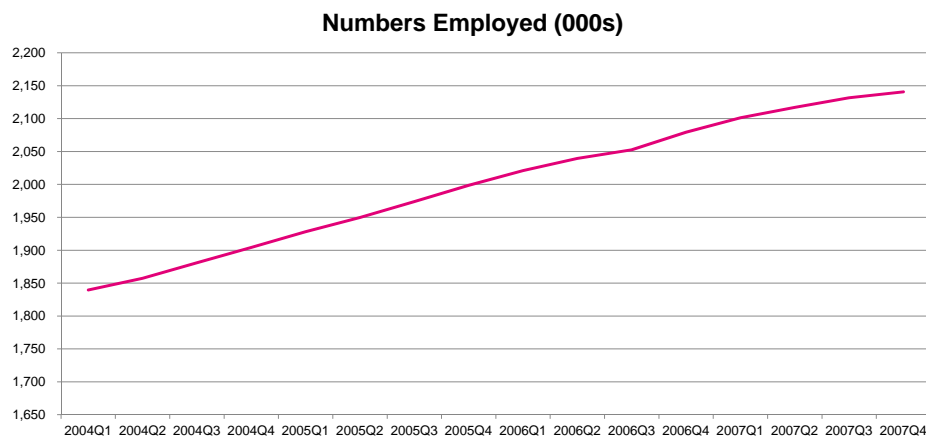


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Steadily rising numbers in employment

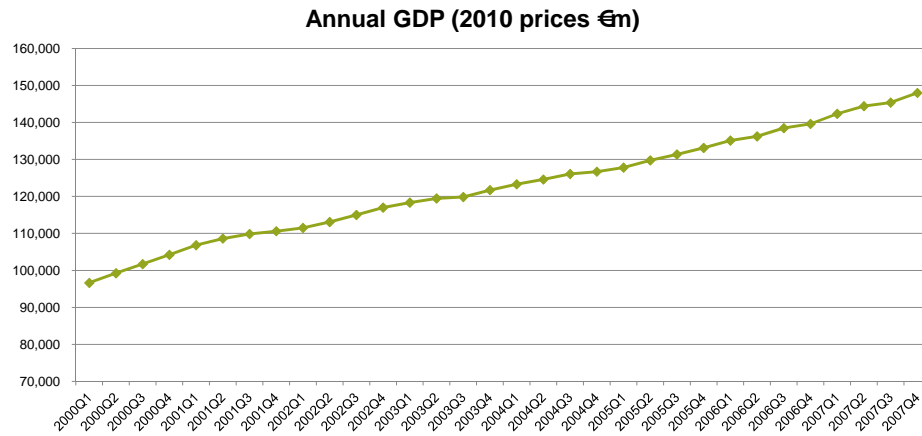


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Steady Growth in Real GDP

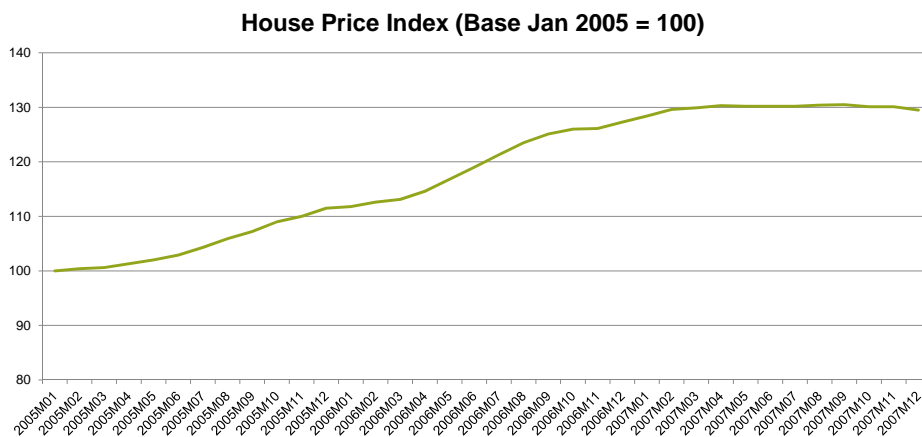


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Worrying trend in house prices

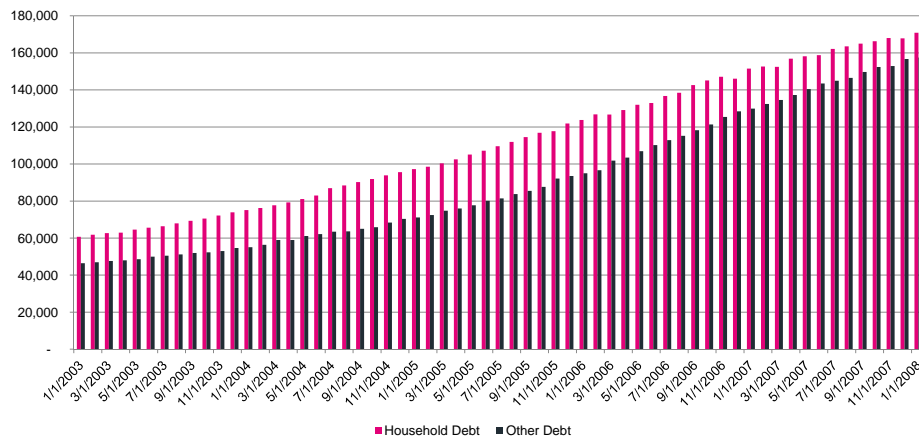


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Low interest rates drive rising debt levels



Source: Central Bank of Ireland

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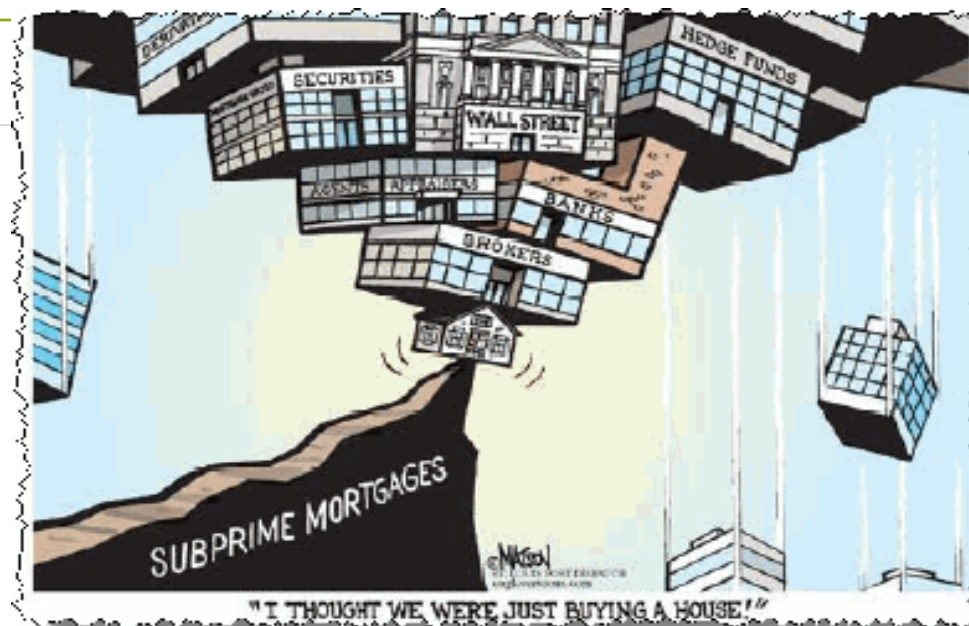
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Lehman collapse sparks chaos

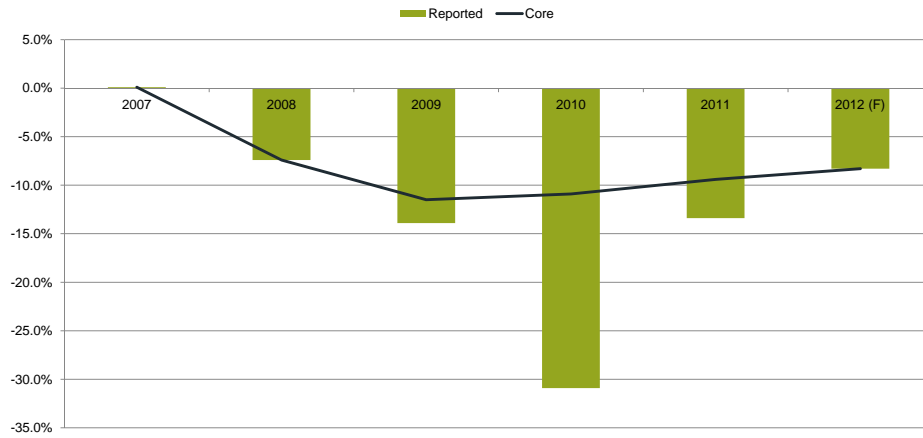


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Suddenly large government deficits (% GDP)



Sources: Eurostat / Department of Finance

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Huge impact of Bank Recapitalisation



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Your chance to participate

Ireland has 0.9% of the EU population

- A: less than 1%

- B: 1-5%

What percentage of the cost of the European Banking Crisis was borne by Ireland?

- C: 5-10%

- D: 10-20%

- E: 20%+

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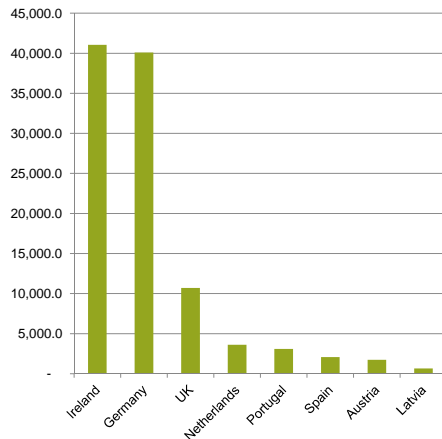
Answer

43%!

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Cost of European Banking Crisis 2007-2011 (€m)



- Source: Eurostat (Oct 2012)
- Actually understates Irish cost because it omits €20bn
- Also a bit low for others
 - UK cost to end 2012 £23bn (source The Observer)
 - If cost per person were the same as Ireland would be:

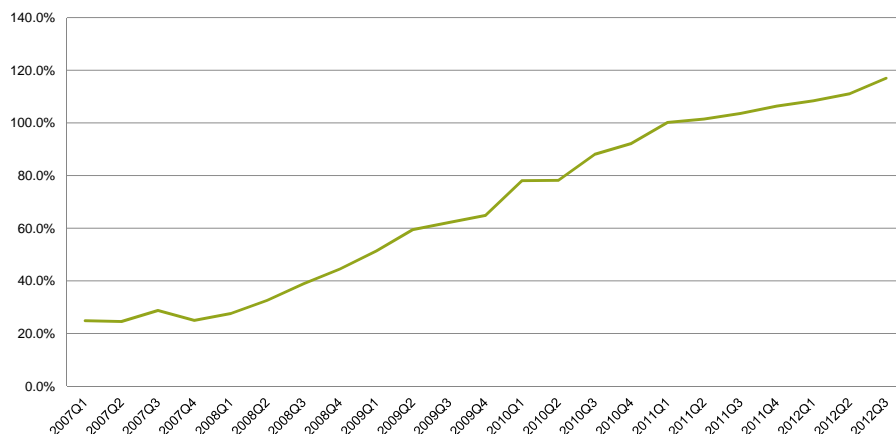
£750bn

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Government debt rises to very high levels

Irish Government Debt as % GDP

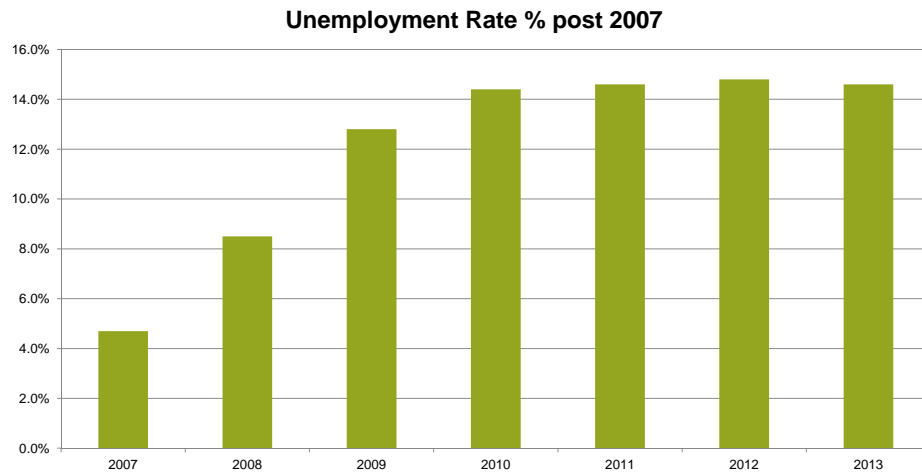


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Rapidly rising unemployment

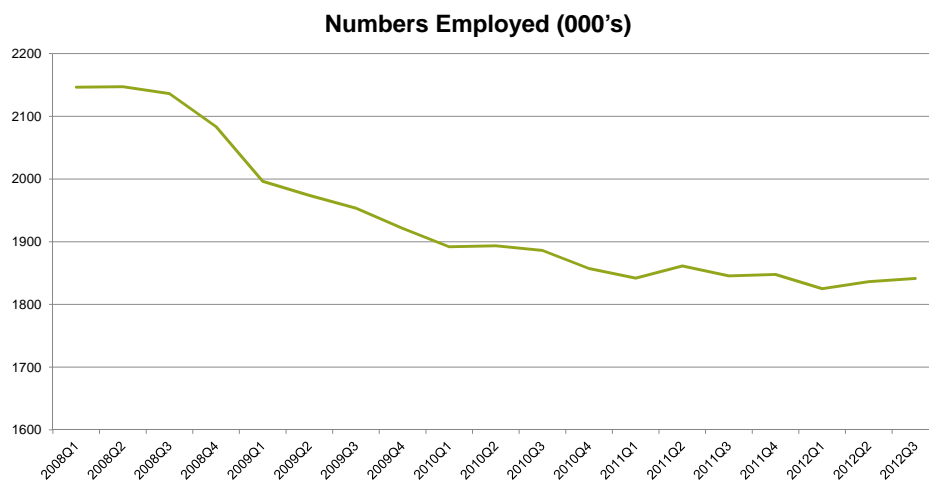


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Reversal in Employment numbers

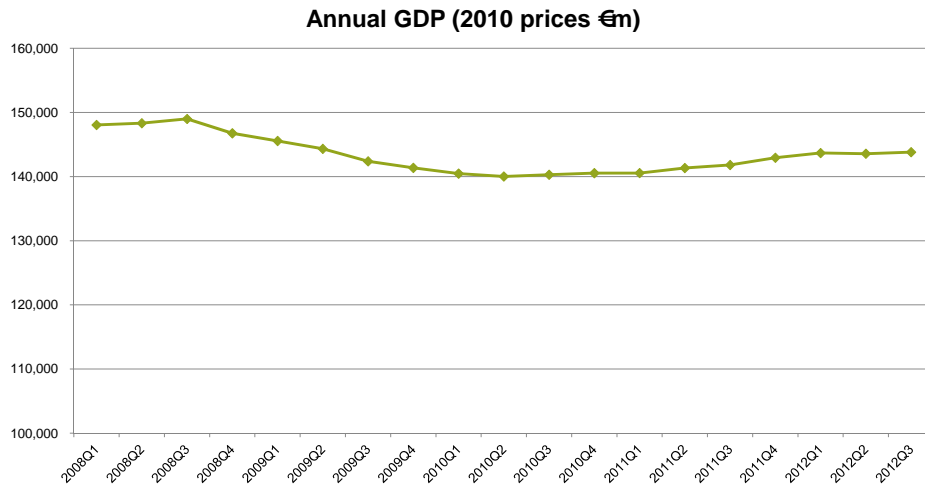


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Negative growth from 2008-2010

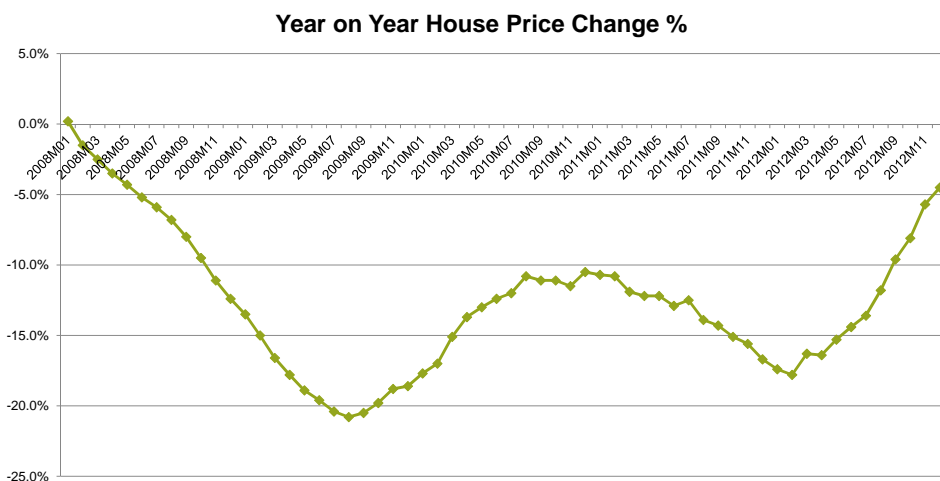


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House Prices Plummet



Source: CSO

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Eurozone Debt crisis kicks in



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Jon Berkeley

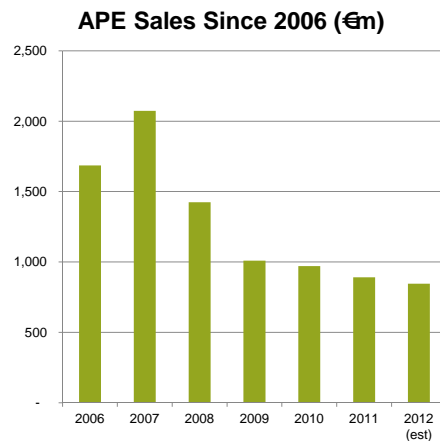


So what were the implications for life companies?

- Sales Declines
- Poor Persistency
- Reserving/Solvency issues due to bond spreads

Declining Sales – Domestic Market

- Frozen or falling salaries
- Falling profits in SMEs
- Falling investor confidence – especially property
- Cuts in Pension Tax relief
- Unemployment



Source: Milliman

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Worsening Persistency

- Irish Life comment in 2011 Annual Report

“Since 2008, the Group has experienced a deterioration in persistency as customers moved to cash products due to the fall in investor confidence.

Whilst the Group seeks to mitigate this risk through diversification of the portfolio and by offering products which will meet customer needs in these more turbulent market conditions, current market conditions are impacting on customers' risk appetite, particularly for equity and property products.”

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Causes of poor persistency

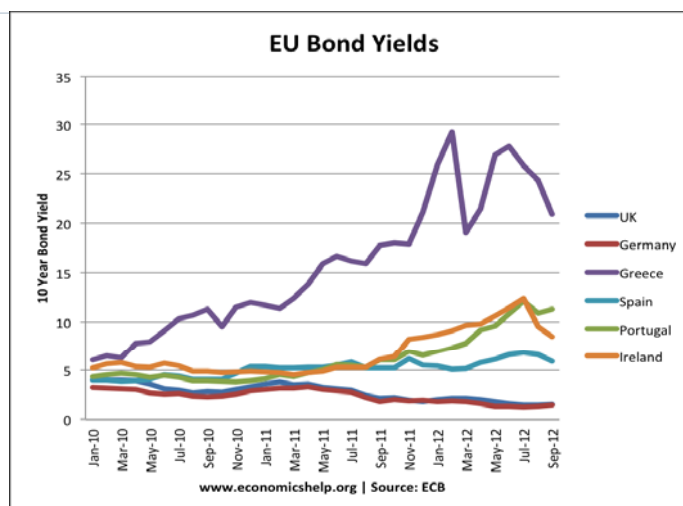
- Investor Confidence
- Unemployment
- Falling Salaries
- Changes to tax rules for pensions
- Concerns about solvency of providers
- Switch activity
- One bright spot – mortgage protection



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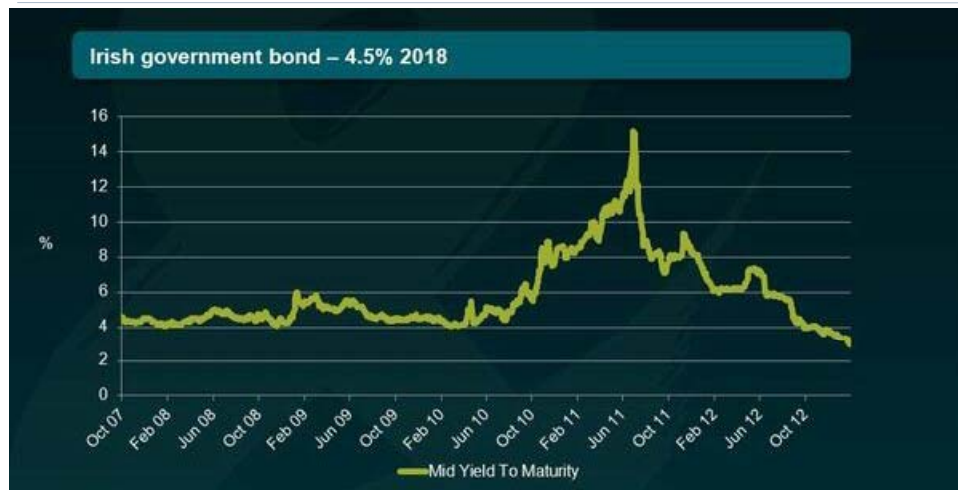
Spreads become a key issue



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Bond Yields now below 2007 levels



Source: Bondvigilantes.com

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What is the “Risk Free Rate”

- Irish bond yields were close to German pre 2008
- Insurers held a wide spread of sovereign Euro assets but overweight in Ireland
- What is the Risk Free Rate to value Irish liabilities?
 - German bonds
 - Actual portfolio adjusted for risk? Define?
 - No statistical information on sovereign default
 - Should the insurer be stronger than the Sovereign?
 - Treat Irish and overseas liabilities differently?

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- No available historic information
- Must allow for credit risk
- Part of the spread may be liquidity premium
- At least 50% likely to be credit premium
- Avoid asset concentration



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Implications for the UK?

- Government Debt is rising
 - Your own currency may not protect you forever
 - Moody's recent removal of the AAA rating
- Are you seeing a property price bubble – property prices did not fall very far and are rising again
- Are your banks really fixed – sustained losses?
- Implications for the whole economy if property/banking fails
- Sovereign exposure in insurers – very little diversification

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Questions or comments?

Expressions of individual views by members of The Actuarial Profession and its staff are encouraged.

The views expressed in this presentation are those of the presenter.

