Could insurance provide an alternative to fiscal support in crisis response?

Lessons from the pandemic

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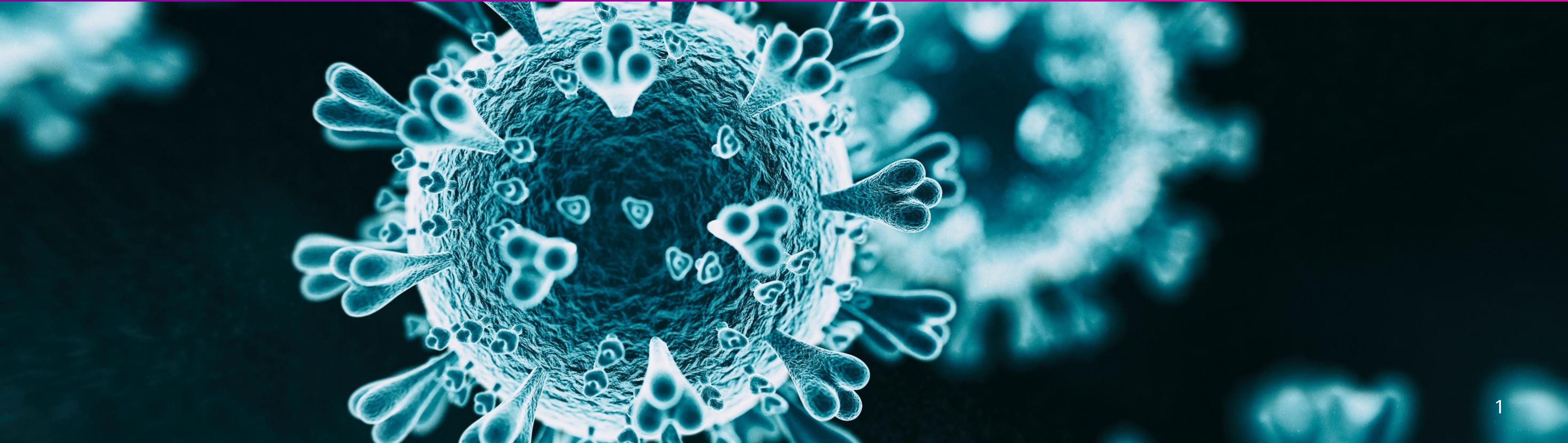


The economic impact of COVID-19 and the contributions from re/insurance

Economic impact of COVID-19:
USD >12 trn since 2020

Contributions from re/insurance

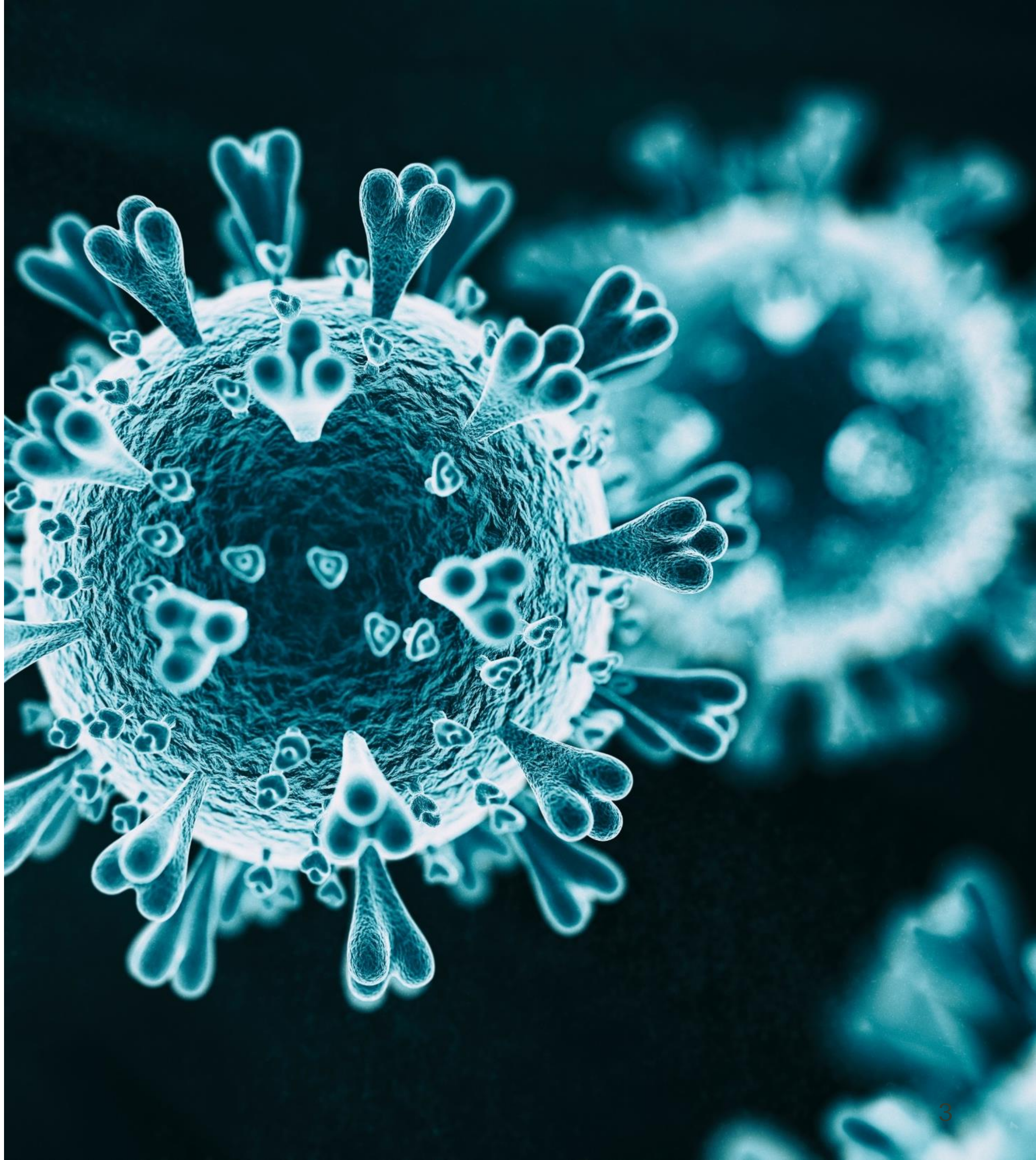
- Significant contributions from re/insurance industry, estimated at around USD 50bn overall
- Mortality, health, disability, event cancellation, credit, travel, potentially: liability
- Challenge is business interruption (BI) following mandated lockdowns --> not privately insurable
- In some jurisdictions without employment related support mechanisms such as the UK and the US the issue is not only BI, but also unemployment/furlough benefits

BI following pandemics: the challenges for insurance

- The economic impact of COVID-19 exceeds the capital of the global insurance industry by far
- There is no geographic diversification, unlike for other large risks
- Lockdowns are the decisions of authorities; these are difficult to model (high uncertainty both in terms of probability of occurrence and size of loss)
- Correlation with other insurance risks (life, credit) and financial markets reduces capacity of re/insurers and capital markets
  - ➢ **A truly systemic risk**
  - ➢ **Business interruption following pandemics cannot be privately insured**

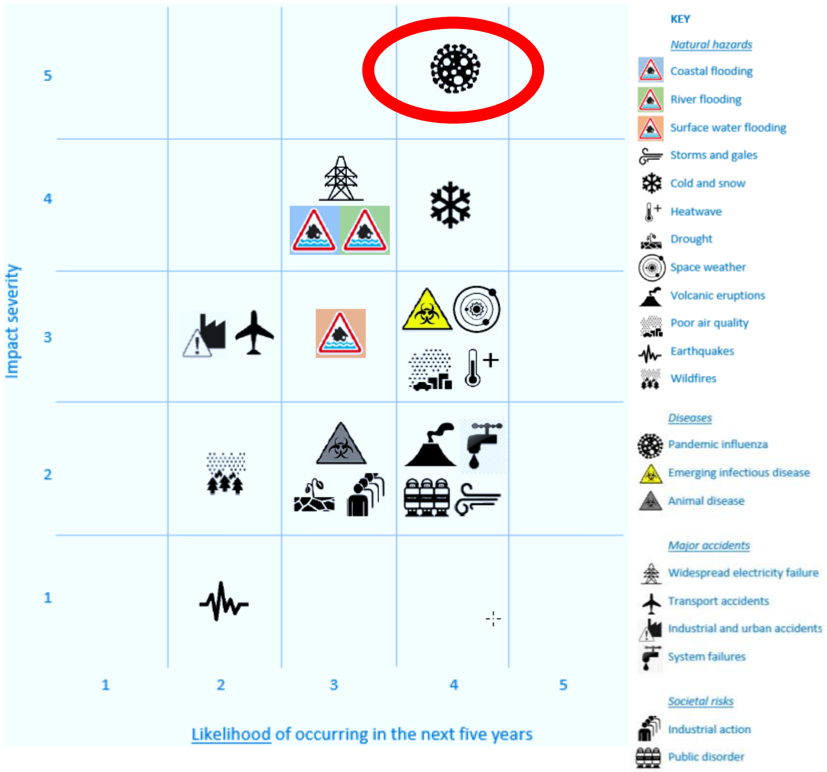
A scheme of relevance needs government back-up. The insurance industry has the tools to support effective distribution, product design and targeted claims payment.

All subsequent considerations relate to the establishment of a comprehensive pool scheme, not the design of possible (niche) products!

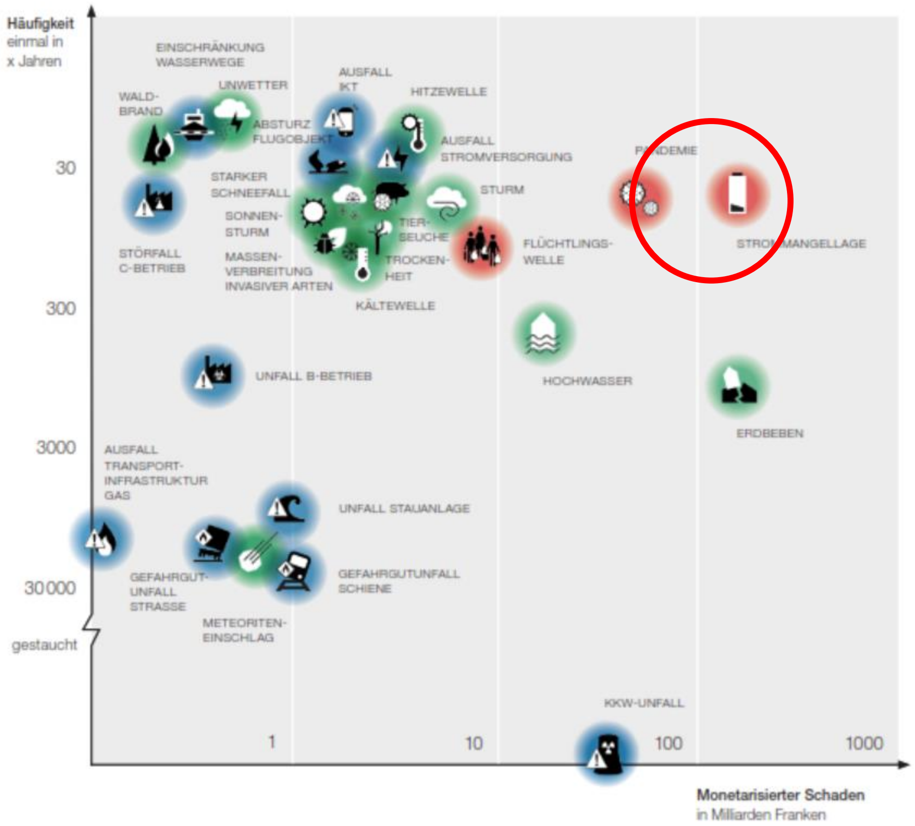


Challenges associated with financing a pandemic: unprecedented scale associated with comparatively high frequency

Example National Risk Registry UK



Example National Risk Registry Switzerland



Considerations for a public-private insurance scheme for BI following pandemic

- Despite the challenges regarding the insurability of pandemic risks, **the insurance industry can play a part** in a government-sponsored insurance solution.

- A financial risk transfer solution has several benefits when compared to ad-hoc or ex-post financing:
  - Compensation on the basis of **pre-agreed rules** are preferred over ad-hoc decisions. This provides legal certainty for victims of the pandemic and can be the basis for additional borrowing.

- Beyond risk transfer, the insurance industry can deliver **essential services**:
  - Infrastructure and expertise related to distribution, loss assessment and loss adjustment are already in place

Key considerations

1. **Transparency and clarity for:**
   Insured interest, insured perils, event definition, risk allocation btw. insured, insurers and the govt.
   - ➢ Given the enormous loss potential, an insurance solution should focus on "survival of enterprises"
   - ➢ Loss adjustment mechanisms need to be highly efficient to handle a large amount of simultaneous claims. This calls for a simple product.

2. **Economic sustainability:**
   The total premium pool needs to be sufficient to cover risks and associated costs.

3. **Universal application:**
   Considering the large circle of affected stakeholders, the risk transfer solution should cover all companies (obligatory insurance).

Insurance PPPs for large-scale risks do exist: different risks, different solutions

Earthquake/Flood/Drought

- Quantifiable, diversifiable
- Significant private capacity
- Various existing PPPs
- Still big protection gaps

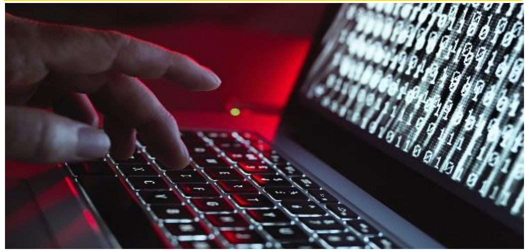
War

- Huge loss potential, not quantifiable
- Loss dependent on gov't action
- Not insurable, no private capacities

Terrorism

- Difficult to quantify
- Globally diversifiable
- Some private capacity
- Various existing PPPs

Cyber Risks



- Huge loss potential
- Difficult to model
- Some risks insurable, some not
- Some private capacity
- Initial PPPs

Nuclear liability risk

- Huge loss potential
- Limited private capacity
- Global pool system

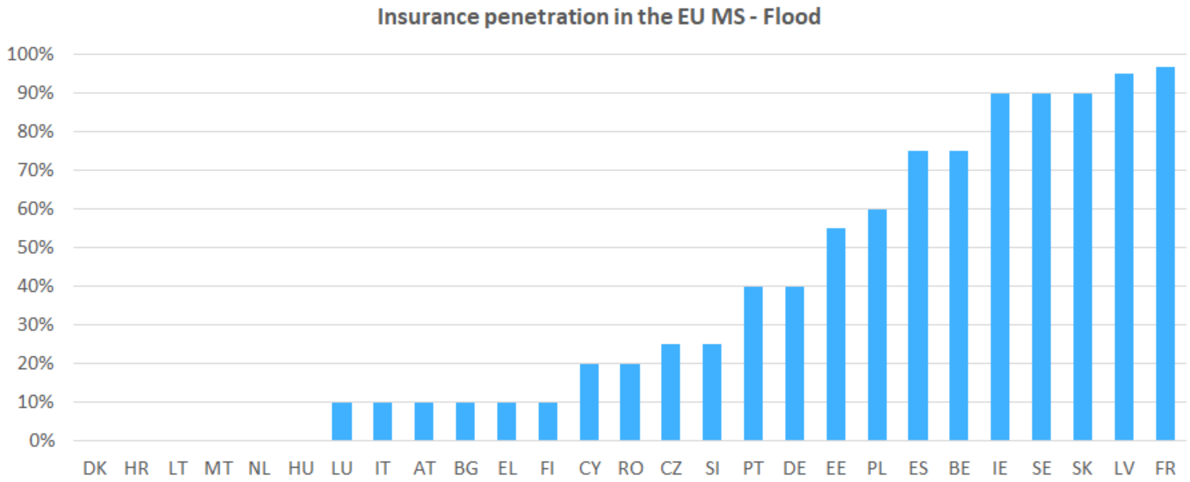
Pandemic BI

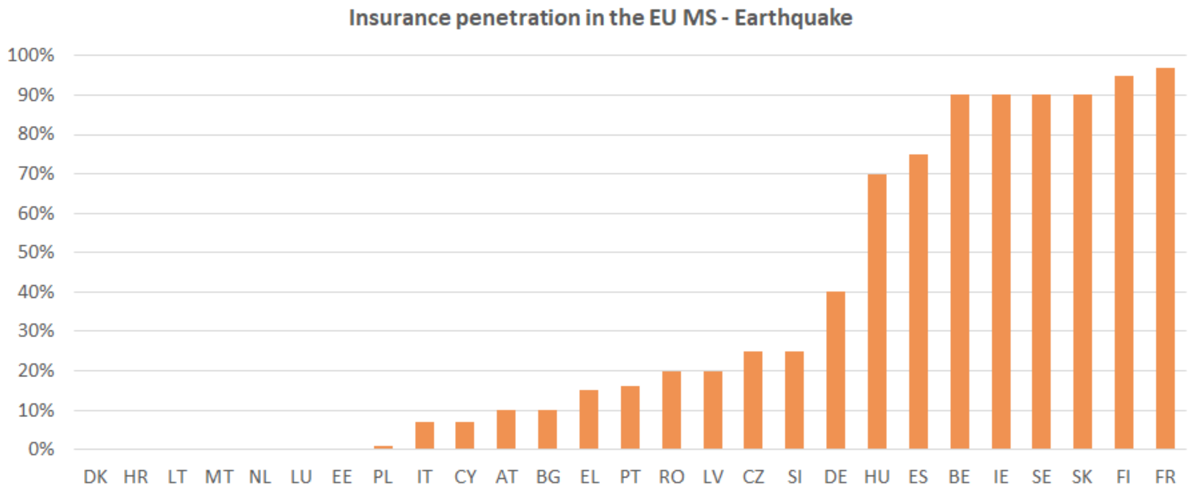
- Huge loss potential
- Loss dependent on gov't action
- No diversification
- Limited private capacity
- Initial PPP discussions

Natural disasters are insurable – protection gap in Europe is significant

Economic loss of floods in Europe 2021: USD 40bn. Highest on record. 2/3 uninsured.

Source: Swiss Re Institute





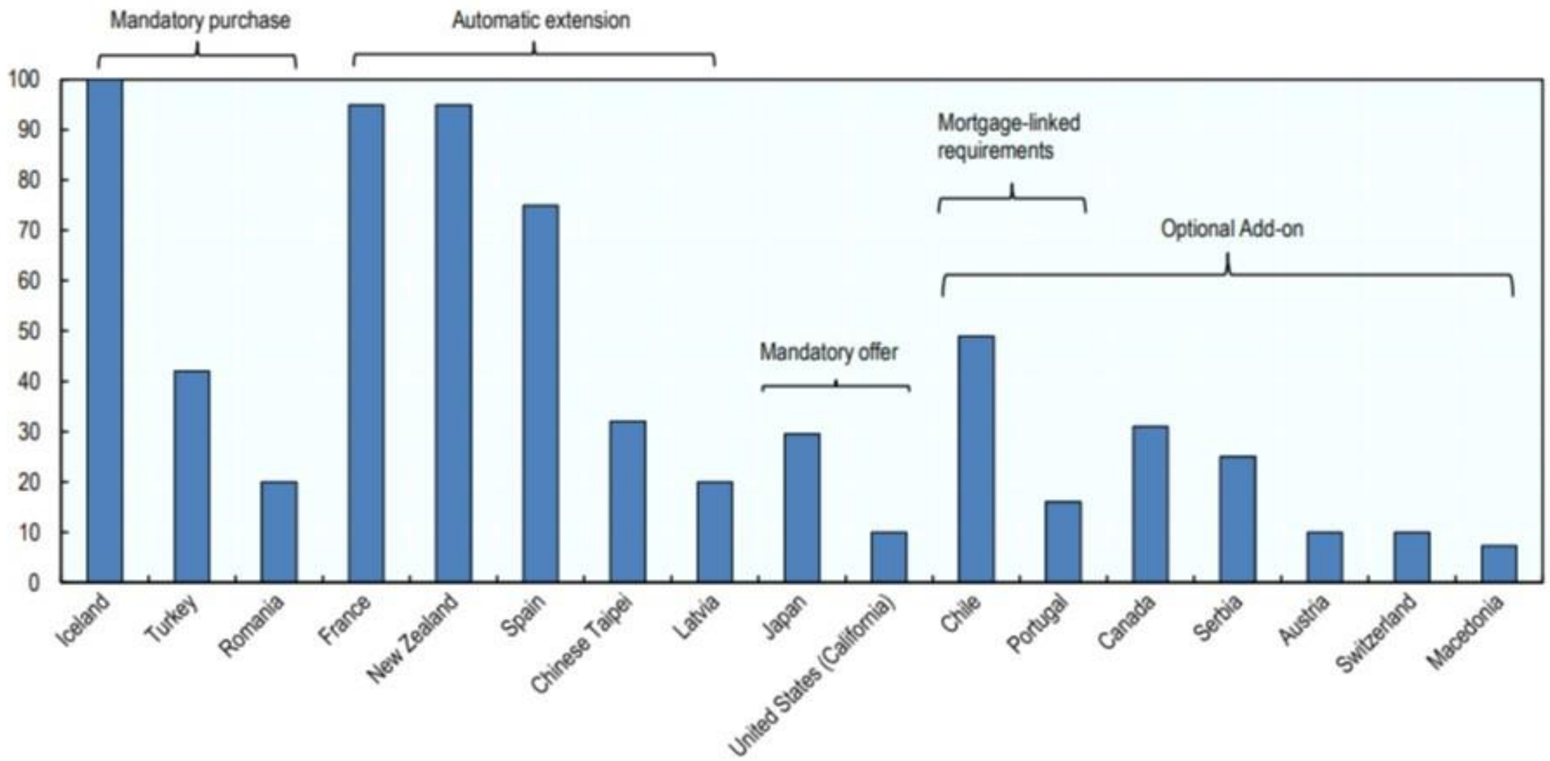
Source: World Bank. 2021. Financial Risk and Opportunities to Build Resilience in Europe

- According to World Bank, in 16 out of 27 EU countries **insurance penetration for** flood or earthquake risk is **below 20%.**
- Incentivizing private insurance can **reduce government liabilities** by **50%** for **very extreme events** and by up to **67%** for **smaller events.**

Appendix

Example: Earthquake protection gap

Figure 5.1. Residential earthquake insurance penetration based on type of offer/level of compulsion



Source: Responses to the OECD questionnaire on the financial management of earthquake risk.

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