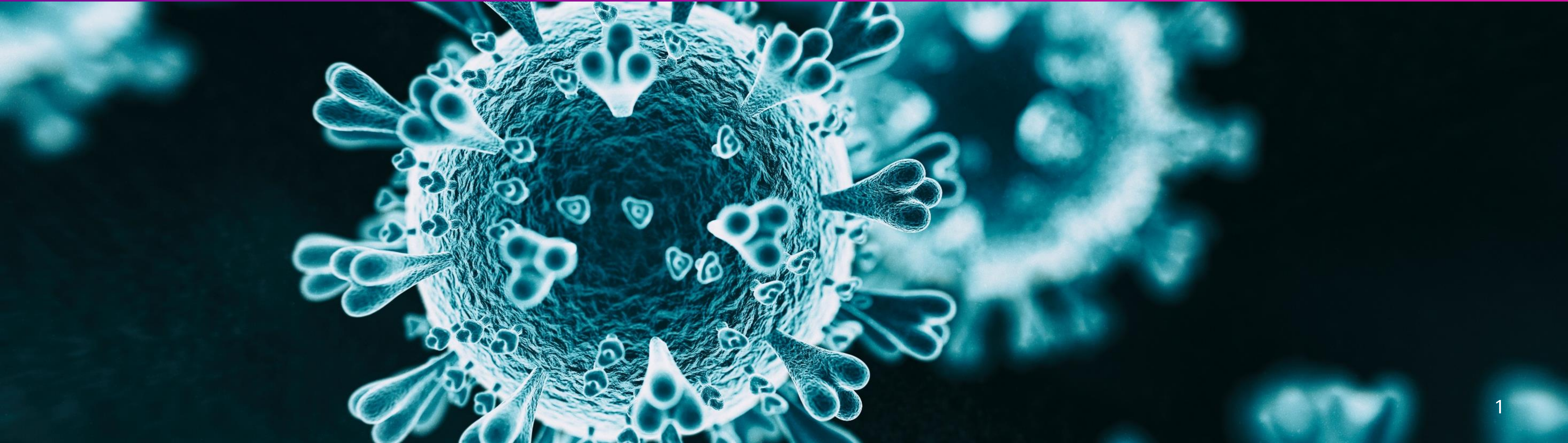
Swiss Re

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

Lessons from the pandemic

OECD Fiscal Risk Network Meeting, 22 April 2022

Esther Baur, Swiss Re Public Sector Solutions



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

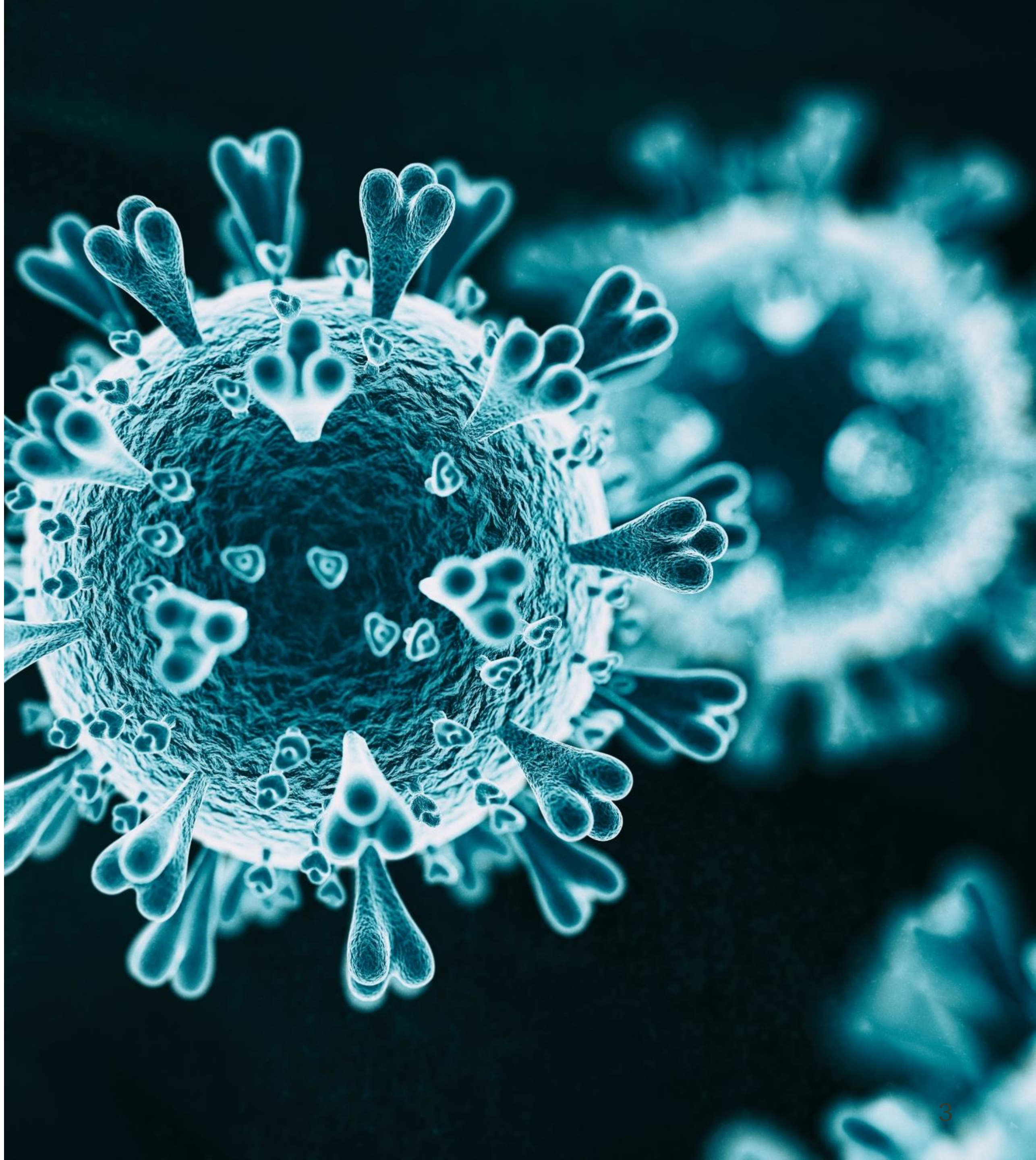
- Significant contributions from re/insurance industry, estimated at around USD 50bn overall
- Mortality, health, disability, event cancellation, credit, travel, potentially: liability
- Challenge is business interruption (BI) following mandated lockdowns --> not privately insurable
- In some jurisdictions 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**

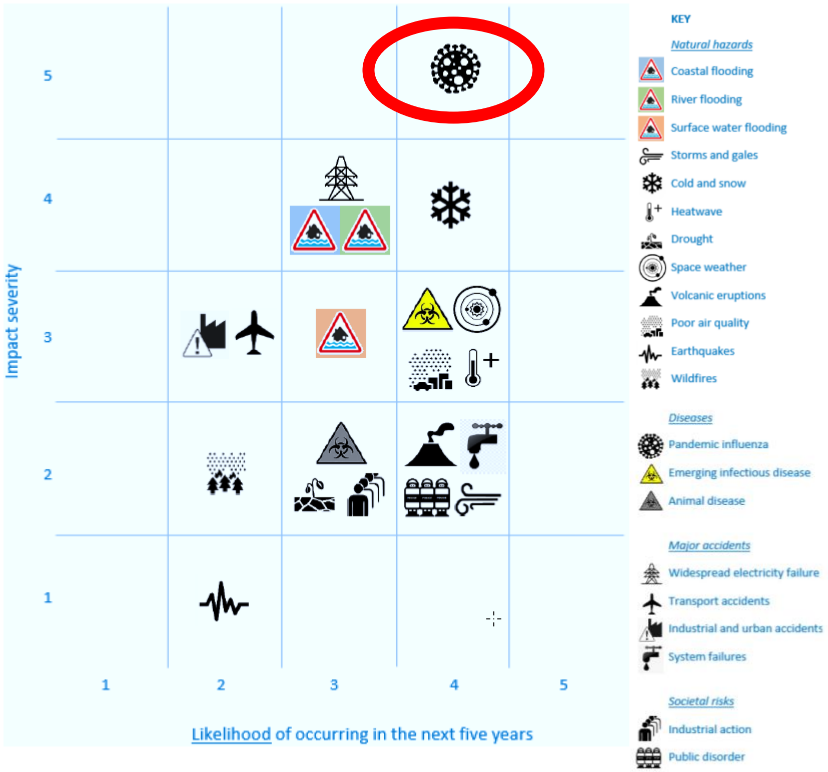
A scheme of relevance needs government back-up. The insurance industry has the tools to support effective distribution, product design and targeted claims payment.

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

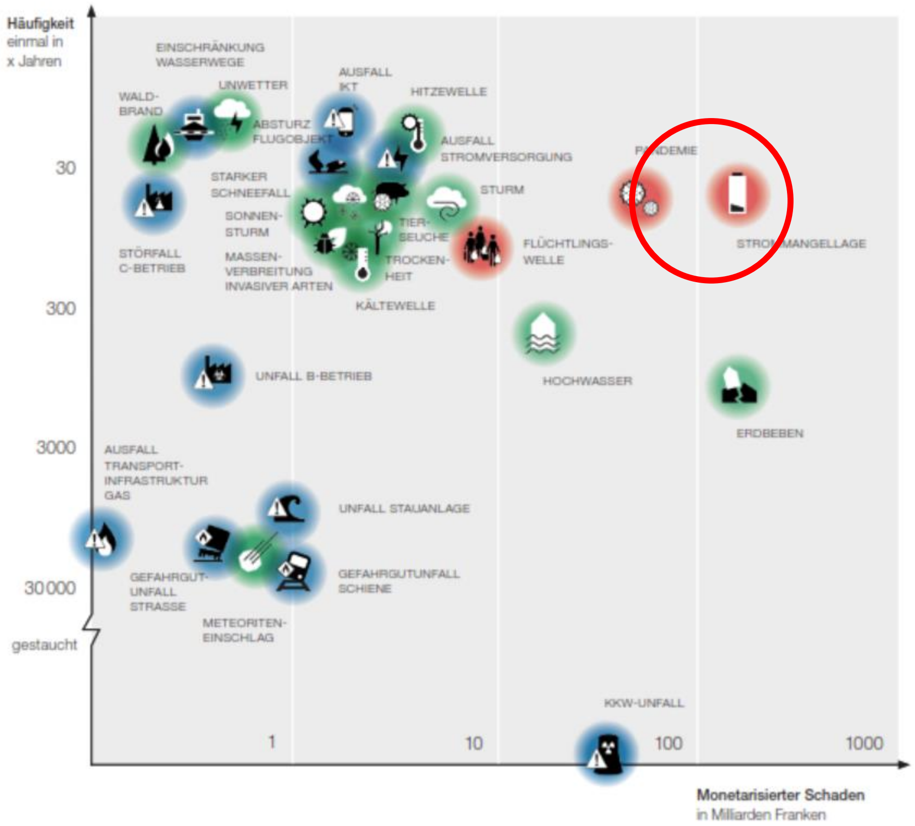


Challenges associated with financing a pandemic: unprecedented scale associated with comparatively high frequency

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

War

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

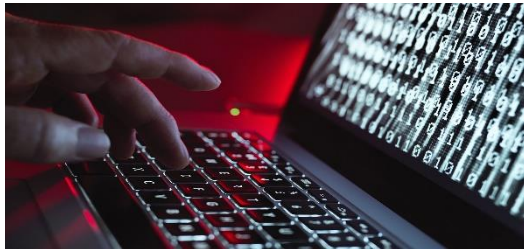
Earthquake/Flood/Drought

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

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

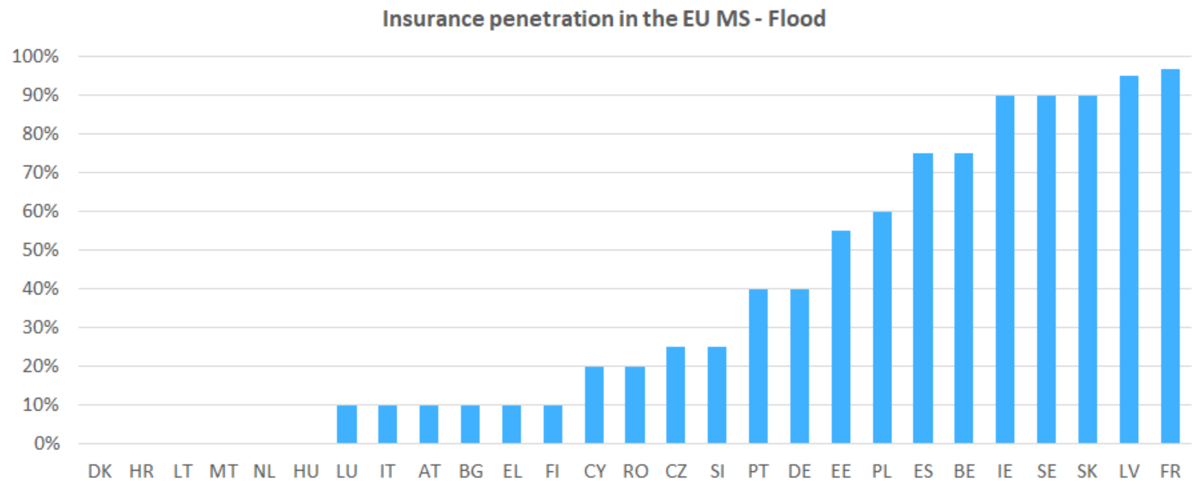
Natural disasters are insurable – protection gap in Europe is significant

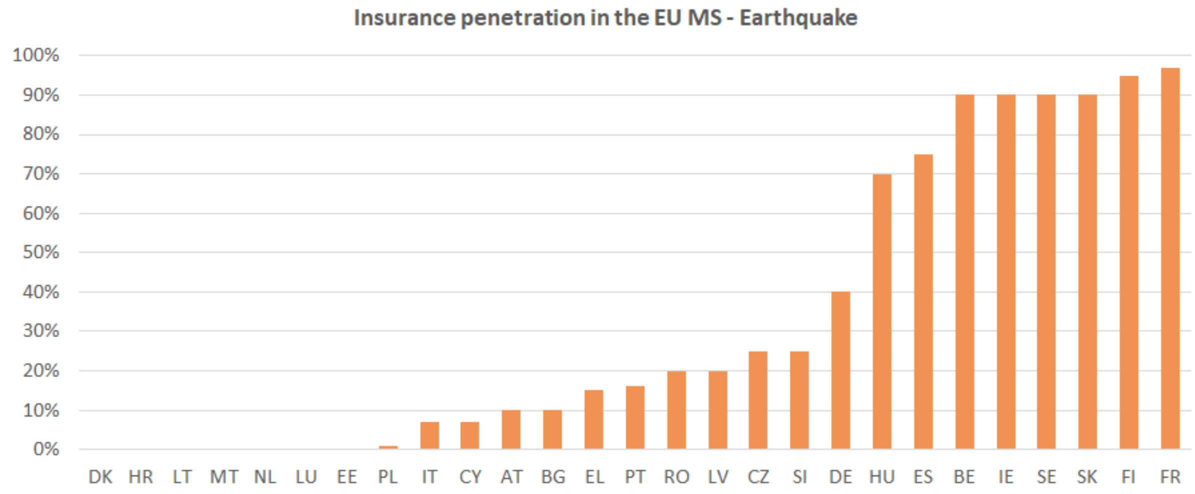
Economic loss of floods in Europe 2021: USD 40bn. Highest on record. 2/3 uninsured.

Source: Swiss Re Institute

- 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.**



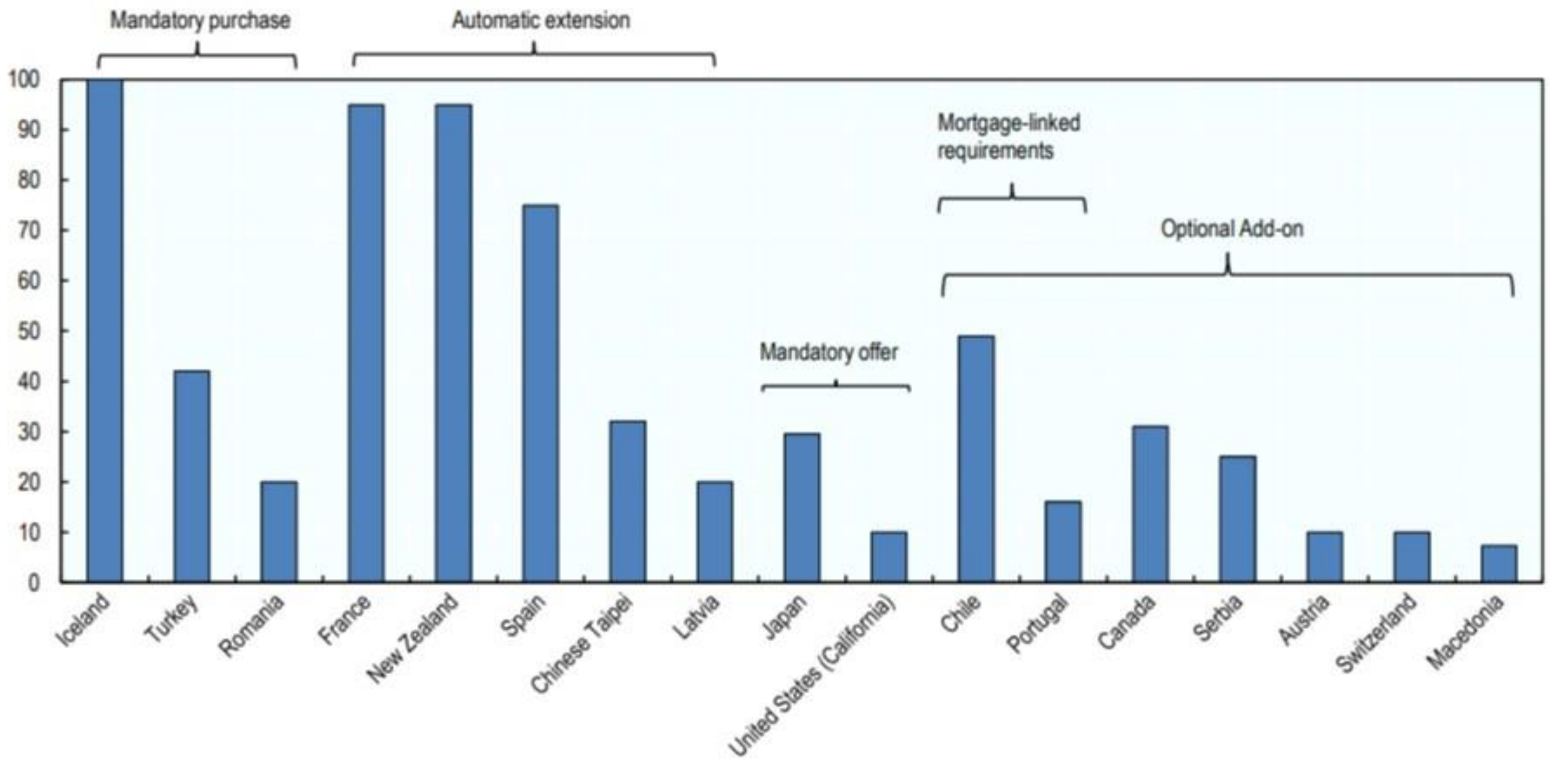


Source: World Bank. 2021. Financial Risk and Opportunities to Build Resilience in Europe

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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