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AllianzGI Insurance Snapshot: Italy is different

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For professional investors only

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Italy was one of the solvability "losers" during the CoViD crisis. Compared to the other countries whose insurers suffered, Italy is quite different.

First of all, Italy – with one exception – is not using the Transitional measure on Technical Provisions (TTP), hence no "support" from that side. We will analyse the TTP closer in our next episode. Second, Italy does not have a big Duration Gap either, when compared to most of the other countries with diminished Solvency Ratios during the crisis. Only Spain and the UK – the countries using the Matching Adjustment – naturally have a smaller Duration Gap than Italy. From an ALM perspective, therefore, we would expect a reduced volatility of the Own Funds.

So, what could be the cause for such a dramatic loss in Solvency Ratio in Italy? It seems that the Volatility Adjustment (VA) did not have the same positive effects in Italy as for NL and DK. To understand this, we must take a closer look at the asset allocation of Italian insurers. The most obvious, compared to all other countries, is the massive overweight of BTP exposure (41.4%) and the overall home bias (57.4%). Now this explains a lot! When we look at the spread volatility of BTPs during the crisis, we can clearly see that they "outperformed" the other government bonds. Compared to NL and DK, therefore, Italian insurers lost far more in asset value due to this spread widening. At the same time, the excess spread widening in Italy's country-specific VA reference portfolio was not significant enough to trigger its activation under the current framework. This implies that for the liabilities, on the one hand, only the increase in the EUR-currency VA was applicable, while for the assets, on the other hand, the spread widening in local investments hit way harder. Paired with a Liability duration 5 years shorter than in NL and DK, the VA mechanism was far from (over-)compensating the losses incurred through the BTP-spread widening.

It seems obvious that in the current discussion started by EIOPA on the "2020 review", the VA is playing a major part. The latest proposal* towards changes in the VA is targeted at the extreme impacts we have seen at both ends of the spectrum:

- for countries like NL and DK, the overshooting effect will be minimised,
- for countries like IT, a smoother transition of recognising country-specific spread will be introduced.

We have now seen and discussed the (non-) impact of the VA, and want to take a closer look at the TTP in our next instalment.

LOOKING FORWARD TO FUTURE DISCUSSIONS ON THIS CHANNEL!

Value. Shared.

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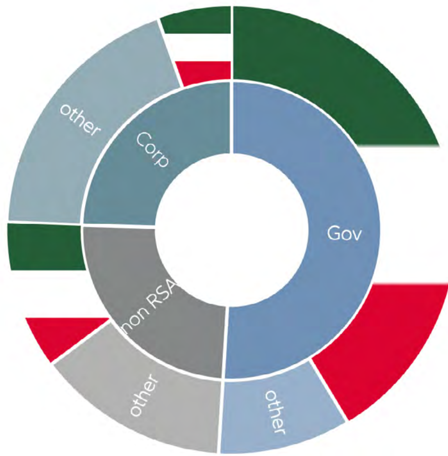
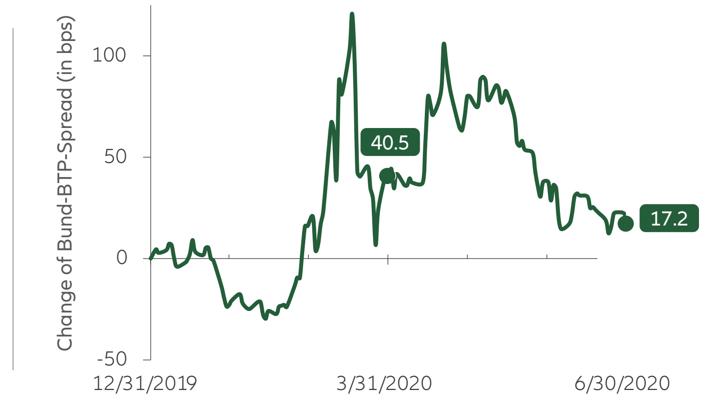
Average Portfolio of Italian Life and Other Undertakings and YTD change of Bund-BTP-Spread





Sources: EIOPA Insurance Statistics (SQ Exposures 2020); Life and Other undertakings only; Bloomberg; own presentation.
*European Commision, Proposal for a Directive of the European Parliament and of the Council amending Directive 2009/138/EC, 22 Sep 2021.

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