Title: On the exposure of insurance companies to sovereign risk – portfolio investments and market forces[1]

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On the exposure of insurance companies to sovereign risk - portfolio investments and market forces[1]

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Highlights of the paper „On the exposure of insurance companies to sovereign risk"

- Since the onset of the European sovereign debt crisis, sovereign risk has been one of the main threats to financial stability. While most recent research investigates the link between sovereign risk and the banking system, this paper analyzes the transmission of sovereign risk to insurance companies.
- We use a firm level panel dataset that covers large insurance companies, banks and non-financial firms from nine countries over the time period from 1 January2008 to 1 May 2013.
- We find that domestic sovereign risk significantly increases insurer risk as perceived by markets. While the impact on insurers is similar to the effect on banks, it is substantially larger than for non-financial companies.
- The link to domestic sovereigns was stronger for insurers that have subsequently been identified as systemically important by the Financial Stability Board.
- Based on European data, we show that risks in sovereign bond portfolios are an important driver of insurer risk, which is not reflected in current insurance regulation (incl. Solvency II in Europe).

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Multinational Finance Society. Furthermore, the authors would like to thank J.P. Morgan for its permission to use the published sovereign bond data in this research project. The opinions expressed in this discussion paper are the authors' personal opinions and do not necessarily reflect the views of the Deutsche Bundesbank or its staff. Any remaining errors are our own.

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