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The French life insurance market during the health crisis

Although the French life insurance market was impacted by the health crisis, it nevertheless showed its resilience. During the first lockdown, gross inflows slowed temporarily and redemptions increased briefly before dropping sharply and then reverting to their long-term average level at the end of 2020. Net inflows recovered in 2021, with strong momentum in unit-linked contracts.

The market continued its transformation that began in the low interest rate environment and that has favoured unit-linked products. This trend, which has not abated since, represents a shift in the product offering towards long-term, equity-oriented investments that better channel savings to the financing of the economy. These developments also change the nature of the product, which should drive continued efforts to make customers aware of the risks involved.

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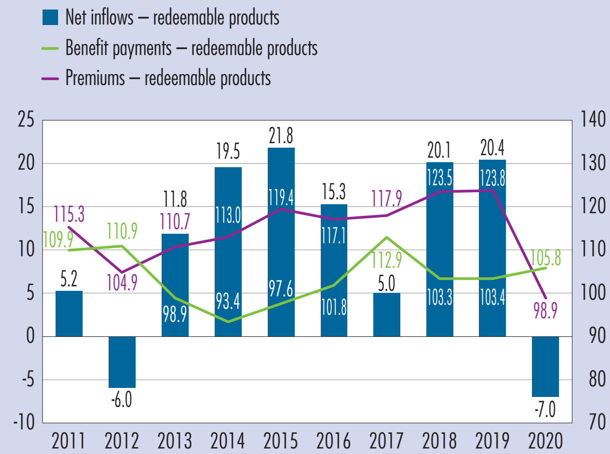
JEL code
G22

EUR 7 billion
net outflows from redeemable products in 2020

EUR 23.9 billion
net inflows into unit-linked products in 2020

EUR 98.9 billion
premiums earned from redeemable products in 2020

Premiums, benefit payments and net inflows from redeemable products
(EUR billions; left-hand scale: net inflows, right-hand scale: premiums and benefit payments)



Source: *Autorité de contrôle prudentiel et de résolution* (ACPR – Prudential Supervision and Resolution Authority).

1 The French life insurance market showed its resilience during the crisis

Life insurance in France: a long-term savings product

Life insurance is a long-term savings product available in various forms:

- Funds invested in euro-denominated instruments with a capital guarantee and interest accrued upon payment. These funds make up a major part of the investments of French households (Banque de France, 2021a) and are the leading savings product in France ahead of interest-bearing bank deposits. They account for 38% of household financial wealth.

- Funds invested in unit-linked products for which the insurer guarantees the number of units only, and not their value. The risk that market values may fluctuate is borne by the policyholder, i.e. the insured.

- More recently, multi-product policies under which part of the funds can be invested in a euro-denominated product with the remainder invested in a range of financial assets (unit-linked type instruments).

Many savers have life insurance (39% of households in metropolitan France in 2018 according to the *Institut national de la statistique et des études économiques* – Insee, 2018). However, life insurance policies are becoming increasingly concentrated among those with higher incomes – in 2015, the 10% of households with the highest incomes owned almost 80% of the funds invested in life insurance (Arrondel and Coffinet, 2019).

BOX

Reasons for taking out a life insurance policy

Generally, there are three reasons for having a life insurance policy (Clerc et al., 2021).

- First, there is the benefit of a specific tax regime: if the policy is held for more than eight years, income from payments of less than EUR 150,000 is subject to a tax rate of 7.5% rather than 12.8%. Life insurance policyholders also benefit from tax allowances in the event that policies are redeemed after eight years. Part of the capital corresponding to contributions made after the age of 70 can also be free of tax. Life insurance also offers a reduced rate of taxation for payments made before the age of 70 when financial assets are transferred upon the policyholder's death (Cofinet and Mouliom, 2018).

- Second, life insurance provides savings for retirement and protection against the risk of death or dependency. Thus, 44.3% of households with the reference person aged 60 or over held a life insurance product in 2018, compared with 23.7% of households in which the reference person was 30 years old or less (Insee, 2018).

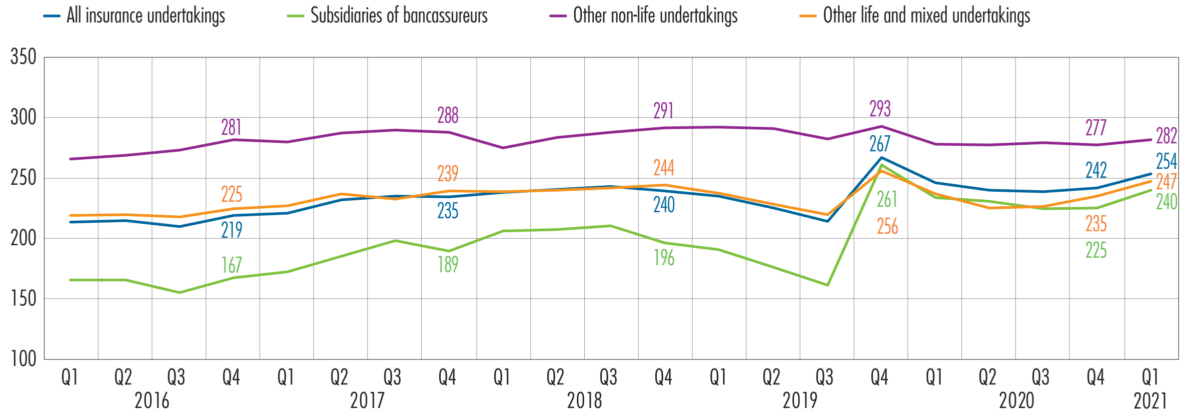
- Third, in principle, a life insurance product invested in euro-denominated funds has a higher rate of return than an interest-bearing bank deposit. There is a trade-off between the security of a product (guaranteed capital) and its return (return on invested capital): in general, the safest products generate the lowest yields.

Despite the unprecedented impact of the health crisis on economic activity and markets, insurance companies were not weakened

The response of most governments to the Covid-19 epidemic included restrictions that impacted economic output. Global activity thus contracted by 3.5% in 2020 according to the International Monetary Fund (IMF, 2021). In France, the Banque de France estimates that GDP contracted by 8% in 2020 and that activity will return to pre-Covid levels at the end of 2021 (Banque de France, 2021b).

In this unfavourable and uncertain environment, stock market values fell sharply at the beginning of 2020, heightening volatility in the equity markets. Indeed, after peaking at 6,111 points on 29 February 2020, the CAC 40 endured a dramatic correction, crashing to 3,754 points on 18 March. However, this correction was short-lived and the economic turmoil prompted by the health crisis was not compounded by a financial crisis, thanks notably to the support measures taken by national and European authorities.

C1 Average solvency capital requirement (SCR) coverage ratio
(%)



Source: *Autorité de contrôle prudentiel et de résolution* (ACPR – Prudential Supervision and Resolution Authority).
Note: Fourth quarter figures are obtained using annual data for the quarterly population.

Therefore, insurance undertakings,[1] which had robust solvency ratios prior to the health crisis (an average solvency capital requirement [SCR] coverage ratio of 267% at the end of 2019 – ACPR, 2020), were able to preserve their financial positions. Their SCR coverage ratio slipped to 243% at the end of 2020 before recovering to 254% during the first quarter of 2021 (see Chart 1). The Decree of 28 December 2019, which authorised insurers to include their profit-sharing reserve (PSR) in own funds for the purposes of calculating their solvency ratio, helped maintain levels of capital.

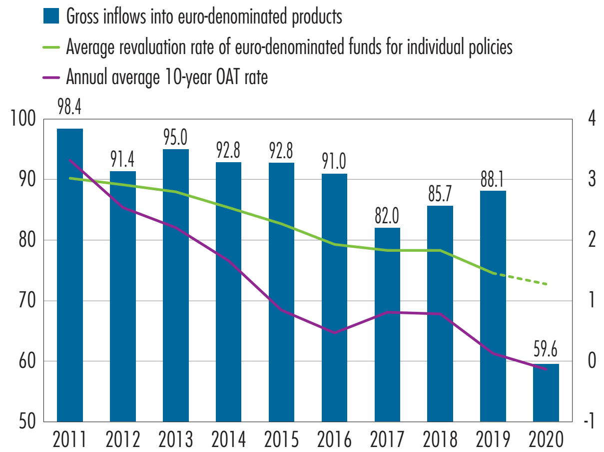
The low-interest rate environment: an unfavourable climate for life insurance

The – limited – decline in the solvency ratio is mainly due to trends in interest rates: the 10-year French Treasury bond (OAT – *obligations assimilables du Trésor*) rate was 0.13% on average in 2019 and –0.15% in 2020. This change in rates affected insurers' returns on their financial investments, the majority of which are in bonds.

The 10-year OAT rate first dropped into negative territory in July 2019 and, with the exception of March and April, stayed there until the end of 2020. Furthermore, the EUR 1,850 billion pandemic emergency purchase programme (PEPP) launched by the European Central Bank to address the consequences of the economic crisis, pushed back the prospects of rising interest rates.

This environment weighs heavily on insurance undertakings' investments, forcing down returns on the bonds in their portfolios. Insurers have passed on part of these reduced returns to the rates offered to their policyholders (see Chart 2).

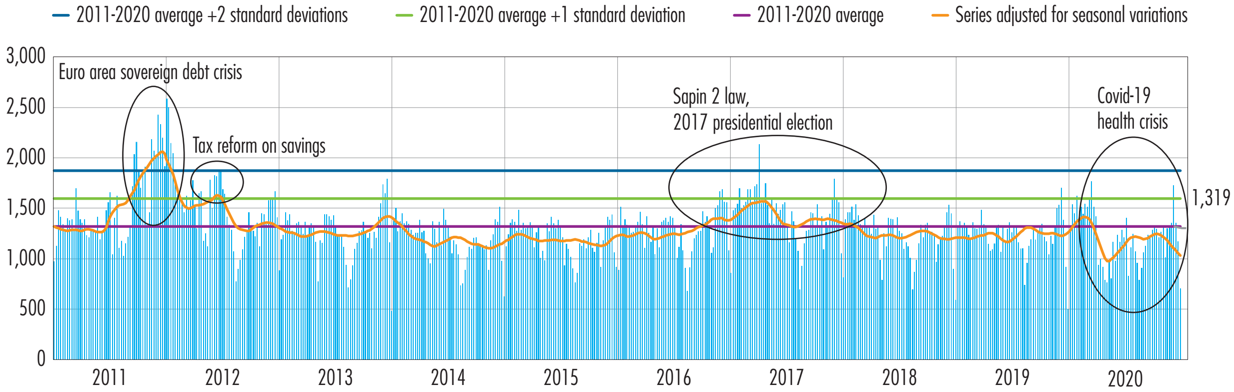
C2 Gross inflows into euro-denominated products and average revaluation rate of euro-denominated funds for individual policies
(left-hand scale: inflows in EUR billions; right-hand scale: rate in %)



Source: *Autorité de contrôle prudentiel et de résolution* (ACPR – Prudential Supervision and Resolution Authority).
Note: The dotted part of the green curve corresponds to ACPR estimates.

1 The life insurance market is relatively concentrated. The five largest contributors (four of which are bancassureurs) accounted for 50% of premiums collected in 2020. The top 15 accounted for 80%.

C3 Weekly redemptions on redeemable products
(EUR millions)



Source: *Autorité de contrôle prudentiel et de résolution* (ACPR – Prudential Supervision and Resolution Authority).
Note: The 2011-2020 average is calculated from 1 January 2011 to the end of February 2020. The last point is for 31 December 2020.

Redemptions kept in check during the health crisis

The onset of the health crisis could have triggered a wave of redemptions, like those observed during previous periods of stress such as the sovereign debt crisis from mid-2011 to early 2012, the tax hike on life insurance products in June 2012, the implementation of the Sapin 2 law at the end of 2016 and the beginning of 2017, or the uncertainty associated with the electoral campaign period of early 2017.

However, after the first weeks of heightened redemptions in mid-March 2020, the phenomenon did not intensify (see Chart 3). In contrast, redemptions fell sharply in April 2020 during the first lockdown period before returning to a level close to their long-term average (at EUR 1,319 million).

2 The structural transformations of the life insurance market could favour economic recovery

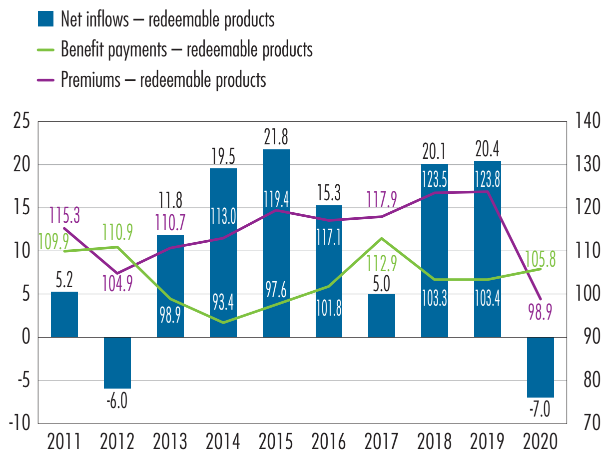
A temporary decline in net life insurance inflows in 2020 due to outflows from euro-denominated products

In 2020, the decline in gross inflows combined with the slight increase in benefit payments (up 2.4% for a total of almost EUR 106 billion) explained record net outflows of EUR 7.0 billion. This is in contrast to the previous two years when strong gross premiums resulted in net inflows of over EUR 20 billion, after redemptions had stabilised following the sharp spike in 2017 (see Chart 4).

However, these figures reflect a two-fold dynamic: (i) major net outflows of EUR 30.9 billion from euro-denominated products, largely offset by (ii) robust net inflows into unit-linked funds (EUR 23.9 billion; its highest level since 2017; see Chart 5 below).

The substantial net outflows observed in 2020 were not linked to the health and economic crises. Indeed, after

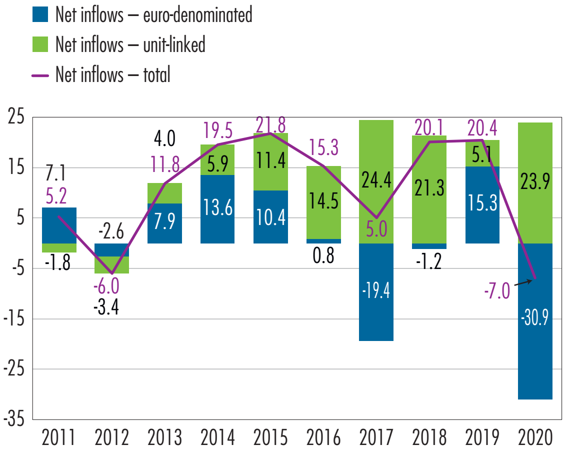
C4 Premiums, benefit payments and net inflows from redeemable products
(EUR billions; left-hand scale: net inflows, right-hand scale: premiums and benefit payments)



Source: *Autorité de contrôle prudentiel et de résolution* (ACPR – Prudential Supervision and Resolution Authority).

C5 Annual net inflows by product type

(EUR billions)

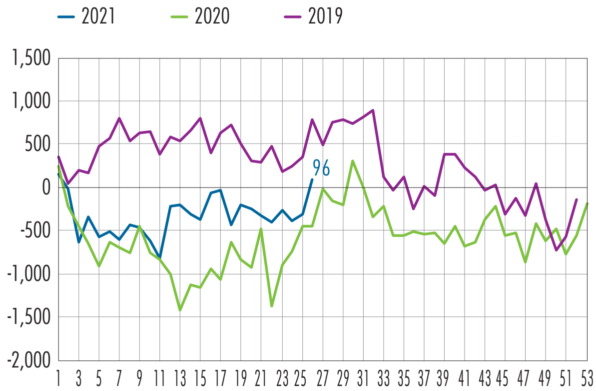


Source: *Autorité de contrôle prudentiel et de résolution* (ACPR – Prudential Supervision and Resolution Authority).

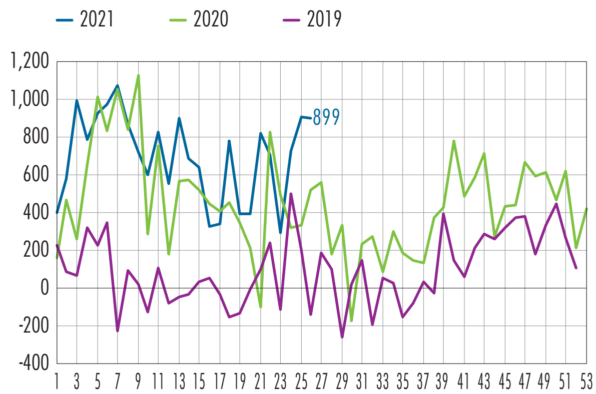
C6 Weekly net inflows by product type

(EUR millions)

a) Euro-denominated redeemable products



b) Unit-linked redeemable products



Source: *Autorité de contrôle prudentiel et de résolution* (ACPR – Prudential Supervision and Resolution Authority).
Note: The x-axis shows the number of the week in the year.

exceptional net inflows into euro-denominated funds during the first three quarters of 2019, the trend reversed during the summer of the same year when interest rates became negative (see Chart 6). In 2021, the strong momentum of unit-linked policy inflows, largely encouraged by insurance undertakings due to the limited profitability of euro-denominated funds (whose net inflows are relatively stable), has contributed to a substantial increase in total cumulated net inflows of around EUR 9 billion at mid-2021.

Since 2012, the revaluation rate (a measure of a cost to insurers) has remained higher than the average 10-year OAT rate (a measure of their revenue). This trend weighs on the offerings of life insurance products invested in euro-denominated funds. Faced with a situation in which bond portfolios (for new bonds) are becoming less lucrative than policyholders' guaranteed euro-denominated contracts, insurers are putting strategies in place to encourage policyholders to invest in unit-linked funds (see Chart 2 above).

Unit-linked products boosted by new subscriptions

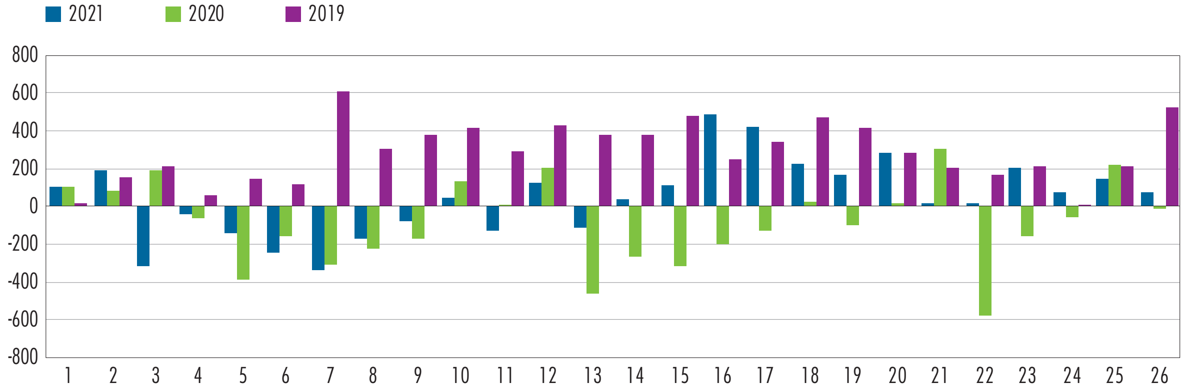
Unit-linked products account for an ever greater proportion of gross life insurance inflows, rising from 15% of weekly premiums on average in 2011 to almost 50% in mid-2021. Unit-linked net inflows amounted to EUR 23.9 billion in 2020, making it the second most successful year after 2017 for this type of product since 2011.

The EUR 1.1 billion of arbitrages from euro-denominated products in 2020 was not the main cause of the high inflows into unit-linked funds, but contributed to it. In 2021, net arbitrages have been relatively neutral. The first quarter leaned slightly in favour of unit-linked products while the second quarter saw a marked shift towards euro-denominated products (see Chart 7 below).

Investments in unit-linked products remained dynamic despite the hit to the stock market from the correction caused by the health crisis. Historically, the proportion of funds invested in unit-linked products tended to rise when the CAC 40 was up but fall when the CAC 40 was down. However, between end-September 2019 and end-March 2020, the proportion of gross inflows accounted for by unit-linked products increased from 28% to more than 40% even though the CAC 40 lost 23% over the same period. This development is mainly

C7 Net weekly arbitrages from unit-linked to euro-denominated products

(EUR millions)



Source: *Autorité de contrôle prudentiel et de résolution* (ACPR – Prudential Supervision and Resolution Authority).
Note: Net positive arbitrages are towards euro-denominated products.Net negative arbitrages are towards unit-linked products.

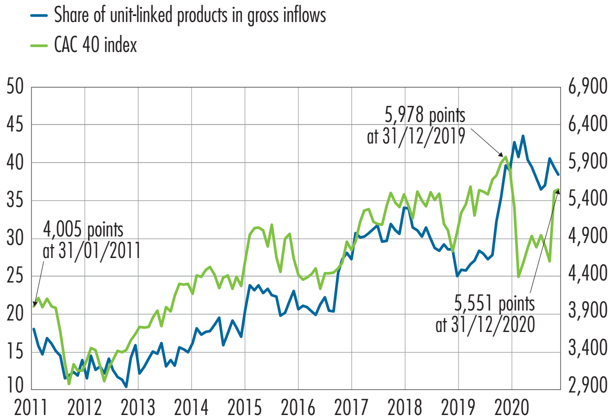
associated with the momentum behind unit-linked products resulting from insurers' promoting them through their product offerings (see Chart 8).

An accumulated savings surplus during 2020, but with little directed towards life insurance products

Savings inflows into life insurance products dropped sharply between mid-March and early June 2020. Gross weekly premiums hit their lowest level since 2011 in the week from 18 to 24 May 2020 and for the first time fell below EUR 1 billion. The share in gross inflows (euro-denominated and unit-linked) of the top six bancassurance groups declined during the lockdown months from 54% in February 2020 to a little under 41%

C8 Share of unit-linked products in gross inflows and the CAC 40 index

(left-hand scale: share in %; right-hand scale: index in points)



Source: *Autorité de contrôle prudentiel et de résolution* (ACPR – Prudential Supervision and Resolution Authority).

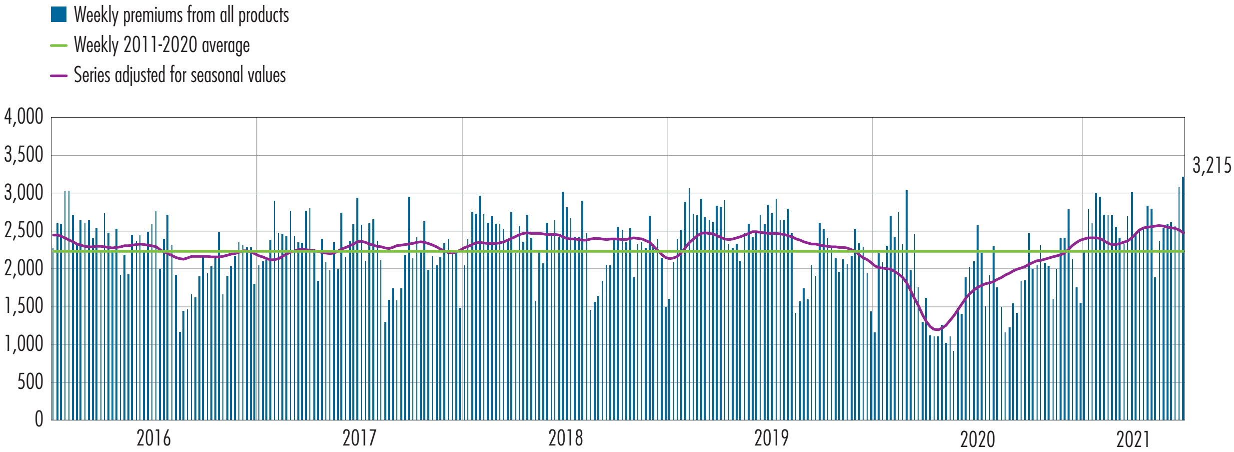
in April 2020. It recovered in July to 54% but changed little by the end of the year (51% in November 2020 compared with over 70% in November 2020). Gross premiums returned to a level close to their long-term average (EUR 2,231 million) during the second half of 2020 and were relatively unaffected by the second lockdown (see Chart 9 below).

The savings accumulated during the months of crisis thus went into highly liquid and non-interest-bearing deposits rather than investments in life insurance products. While life insurance gross inflows were declining, household deposits were increasing. They rose by EUR 149 billion in 2020, up 9.8% year-on-year, compared with a 5.5% increase between end-2018 and end-2019. The largest increase was in sight deposits (mainly current accounts), which rose by 17%, ahead of deposits redeemable at less than three months' notice such as ordinary passbooks (up 15%) and *livret A* passbooks (up 8%). As for the profile of savers, 70% of surplus savings between February and August 2020 were accumulated by the wealthiest 20% of households, which accounted for more than 70% of life insurance products (Bounie et al., 2020).

During the first half of 2021, unit-linked products maintained their strong momentum

Net inflows during the first half of 2021 were driven by the strong momentum in unit-linked products, maintaining the trends observed since the end of 2019. At the end

C9 Weekly premiums from redeemable products (euro-denominated and unit-linked)
(EUR millions)



Source: *Autorité de contrôle prudentiel et de résolution* (ACPR – Prudential Supervision and Resolution Authority).

of June 2021, net inflows into all redeemable life insurance products came to around EUR 9.2 billion. Euro-denominated products were hit with net outflows of approximately EUR 8.6 billion, whereas redeemable unit-linked products saw robust net inflows of around EUR 17.7 billion; the highest level of weekly net inflows observed since 2011. Redemption volumes, which have remained stable since the second half of 2020, confirm the confidence that savers have in life insurance products. Euro-denominated products account for 80% of redeemable product redemptions, partly due to the limited range of euro-denominated policies offered by insurers (mentioned above).

In the context of a changing life insurance market, customers must be able to understand the opportunities and also the risks associated with the products on offer. It is thus important to note the importance of insurers' duty to provide advice to their policyholders, particularly with regard to the risks incurred on unit-linked products.

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