interview to **Ignacio Machetti**

General Manager of the Spanish Insurance Compensation Consortium

Ignacio Machetti was born in Barcelona in 1959.

He is an economist and insurance actuary.

He has been a member of the government organization for insurance inspectors *(Cuerpo de Inspectores de Seguros del Estado)* since 1984.

He has held various positions in the General Manager of Insurance and Pension Funds (DGSFP), where he was Deputy Director-General of the Inspectorate from 1997 to 2001, and in the Insurance Compensation Consortium, where he has held the post of General Manager since January, 2001.

"Credit insurance is experiencing a recovery"

The restricted supply of credit to the economy and the disproportionate increase in the claims burden for credit insurance have been two of the adverse consequences brought about by the financial crisis. With regard to credit insurance, which is intended to guarantee collection of payment when goods are sold to third parties, the insurers in this branch sought assistance from the government through the insurance business association (UNESPA - Spanish Union of Insurance and Reinsurance Institutions). This aid is based on a limited-term agreement with the Insurance Compensation Consortium. In this interview, we learn about the details of the measures adopted, while opinion suggests that the credit insurance branch is expecting economic activity to recover in the near future.

Historically speaking, which functions has the Insurance Compensation Consortium (CCS) developed for credit insurance?

We have passed through several different phases in this area, all of them related to export credit insurance (until the Reinsurance Agreement that was launched last year). To summarize the most important developments: between 1969 and 1970, the CCS took direct charge of export risks designated as "political and extraordinary" during the period when it was handling the reinsurance of the commercial risks as well. This business was taken on by an entity known as the "Compañía Española de Seguros de Crédito y Caución" "Spanish Credit and Guarantee Insurance Company". During a short period of a few months in 1970, the CCS even took on direct responsibility for commercial risks until the formation of CESCE (Compañía Española de Seguros de Crédito a la Exportación - Spanish Export Credit Insurance Company). From 1971 onwards, CESCE took over direct cover for all export credit risks, although it did so for the account of the State in respect of political risks, and it reinsured commercial risks with the Consortium. In 1990, the Consortium stopped reinsuring commercial risks, leaving it with the sole function (which it still retains) of managing funds for the purpose of export credit insurance on behalf of the State - that is to say, a treasury function.

It is only now that consideration has been given to intervention by the Consortium as a reinsurer for all types of credit insurance, including domestic; this has been occasioned by the economic crisis and only on a temporary basis.

When reinsurers came to the conclusion that they were not prepared to continue taking losses, why was the Insurance Compensation Consortium considered as a source of assistance for credit insurance in Spain?

When the Spanish credit insurers identified restrictions in the reinsurance market at the time of the 2009 renewals, they voiced a unanimous request. This was triggered by the increase in defaults due to the economic crisis. Several initiatives were emerging in Europe specifically in France, through the *Caisse Centrale de Rèassurances (CCR, Central Reinsurance Fund)*, the public reinsurer; and in Spain, thoughts turned to the Consortium, whose efficiency as a complement to the private sector was already well proven.

This did not please the reinsurance market at first, due to fears that such an intervention would distort competition. But the market took a more relaxed approach once the terms of the Consortium's participation were laid down, including in particular its objective of remaining neutral in the market. Time has shown that this objective was achieved.

The intervention by the Consortium as a reinsurer for all types of credit insurance, including domestic, has been occasioned by the economic crisis and only on a temporary basis

Which model was followed in Europe to assist credit insurance?

As we know, support measures have been introduced in various countries but according to the insurers, they lack the flexibility and efficiency of the measures implemented here in Spain. The case which has been the subject of most analysis is that of France, where measures of this sort were apparently proposed for individual transactions affected by a reduction in guarantees; the CCR provided complementary cover, offering as much again as was guaranteed by the private insurer.

Apart from the insurance sector, which other activities are benefiting from the measures that have been introduced?

Generally speaking, all sectors of the economy that avail themselves of credit insurance and use it to guarantee that their business transactions reach a successful conclusion. Much use is made of credit insurance in Spain. In fact, the Consortium's participation was not primarily targeted at the insurance sector as such; however, the sector benefited because complementing its capacity enabled it not to exclude business sectors or individual operators from guarantees for reasons other than the high risk of debtor default. In other words, the objective was that any restrictions on cover would be based solely on an analysis of the risk, not on a lack of capacity.

How was this aid formulated in law, and how was it actually put into practice?

The Consortium's legal statutes stipulate and permanently regulate a number of its functions, but they also contain a precept which allows the Consortium to provide cover of other types on the basis of decisions adopted by a qualified majority of its Administrative Board. Such cases are always subject to the requirements that they must conform to the public interest and must accord with market circumstances. This is an arrangement for use in exceptional cases and one which gives the Consortium a high degree of flexibility, but the general principle is that of legitimacy, so interventions made in this way must be temporary or must culminate in an amendment to the law. On this occasion, conformance with the public interest was also endorsed by Royal Decree, according to Law 3/2009 on Urgent Measures Related to the Development of the Economic Situation, which explicitly authorized us to accept reinsurance in this branch subject to specified conditions.

In practice, the arrangements were implemented in accordance with a Reinsurance Agreement entered into by the Consortium and UNESPA (Spanish Union of Insurance and Reinsurance Institutions), initially valid for a temporary period; insurers operating in Spain were able to sign up to this Agreement on a voluntary basis and with one exception, all of them have done so.

What did this entail?

The Consortium's contribution was designed to provide reinsurance in two ways: proportional participation in quota share (the basic method of reinsurance in this branch) with a minimum and a maximum, and under the same terms as the other reinsurers " i.e. entirely in line with market conditions " and in addition, stop-loss protection to guarantee a percentage of the aggregate excess of claims ranging between 85% and 130% of premiums. To ensure financial equilibrium for this second arrangement, which is not a customary method in the branch, clauses were incorporated into the Agreement allowing the contributions made by the Consortium during the validity period of the Agreement to be recovered by it over time.

How did the specialist insurance sector welcome the news that it could count on support and capacity from the CCS?

Given that the support was requested by the sector itself, of course, the reaction was good. The insurers thanked the Ministry of Economy and Finance with relief for this favorable arrangement because " albeit subject to restrictions " it allowed the sector to retain a very important part of its portfolio. Once the Agreement was signed, numerous companies gave it their immediate and full support. All operators on the Spanish market signed up to it except for one, perhaps because the firm in question was already using umbrella reinsurance programs from its parent company.

What estimate can be made of the cost of this system for offering capacity to the insurance industry? Have many losses been incurred?

The aim here was to contribute capacity on a basis of neutral financing, without undesirable interference in the reinsurance market. Obviously, the Consortium's participation in quota share treaties costs exactly the same as the rest of capacity available on the market. As regards non-proportional protection, the effect should be neutral, i.e. its cost must also be similar in the medium term. The Consortium's intervention was more a matter of convenience than cost.

The real use of capacity under the terms of the Agreement has not reached the envisaged maximum, and is currently running at a figure of about EUR 80 million (net of premiums). I would

The Consortium's reinsurance capacity was designed as a proportional participation in quota share at market conditions and a stop-loss between 85% and 130% of premiums

The return to normal conditions has been faster than forecast, as all operators have already decided not to participate in 2010, with one single exception

not use the term "losses", since the Agreement made provision for them to be recovered and charged to current earnings over the next five years. Only one firm that signed up to the Agreement did not need to use the *stop-loss* cover in 2009.

We know which companies have made use of the Agreement, but do we know the branches where they used it?

Basically in all of them. I have already mentioned that much use of credit insurance is made in Spain, both for foreign transactions (between 80% and 90% of our exports are sent to Europe) and for domestic business. It has to be said that construction cover was one of the areas where most problems arose, but the fact is that all the branches have benefited because they have been able to cover more risks.

How long will the Reinsurance Agreement remain in force?

An initial maximum period of three years was stipulated, after which it will be necessary to revise the Agreement " either in order to terminate it, or to amend its terms. But it seems that the return to normal conditions has been faster than was forecast, because all of the operators have already decided not to participate in 2010, with one single exception. So for the bulk of the market, the duration of the measure has been cut down to one year. From now on, once this support has been utilized and cover has effectively been transferred, the Agreement gives the Consortium a period of five years to stabilize its joint result by participating in the technical accounts of the companies in this branch.

So, credit insurance is recovering and companies seem more ready to enter into contracts. How

The Insurance Compensation Consortium: function and mission

The Insurance Compensation Consortium (CCS) is a public corporate entity with its own legal identity which acts as a service provider to the Spanish insurance sector, into which it is fully integrated. It dates back to 1941 when it was constituted on a temporary basis to provide compensation in response to problems that originated during the Spanish Civil War of 1936.

The Consortium's functions have changed and become more extensive over the years, as have its Legal Statutes, which are subject to the same legislation as is in force for private insurance. The CCS has wide-ranging experience and is highly specialized in the functions entrusted to it, which include providing cover for extraordinary risks such as natural risks and terrorist attacks. covered by an insurance contract. It also carries out underwriting for motor insurance when it is impossible or impractical for the market to do so, and it provides accident indemnity in cases where the driver is unknown or is driving without insurance. Its reinsurance activities complement the agricultural insurance system and it plays a similar part in credit insurance, as we have seen. The CCS is also assigned the function of liquidator for insurance companies which cease to be viable.

has this development been influenced by the Government's intervention through the CCS?

The crisis is not over yet. Restrictions on credit insurance transactions in respect of conditions as well as risk selection criteria have enabled companies to stay in the black. Moreover, companies are already considering the expediency of a return to more permissive underwriting policies. In short, this public intervention has made it possible for restrictions and adjustments to be governed by strictly technical criteria, while keeping the portfolio of insureds above critical mass; otherwise, there would have been no recovery, or at least not such a speedy one.

How would you describe the current situation in the credit branch in Spain?

An exhaustive analysis is not easy. Credit insurance is essentially a product that originates from this side of the Atlantic, from Europe, and it has a particularly high level of penetration in Spain; that is why we have the world's second largest group of credit insurers here. The real experts should be asked for their view of the situation. Outside of our country, I believe that the crisis has claimed victims among insurers, and there have also been some exits from the reinsurance markets. The Spanish market has enjoyed good health. It is standing up well to the pressure, but it was prepared for this: credit insurance not only foresaw the crisis, but has also been able to begin its recovery before other sectors of the economy.

Notwithstanding all of this, and now that the Consortium's intervention is practically at an end, the companies still have much to do: we are not even in the same situation as we were before the crisis.

Credit insurance not only foresaw the crisis but has also began its recovery before other sectors of the economy