

Report on Bachelor / Master Thesis

Institute of Economic Studies, Faculty of Social Sciences, Charles University in Prague

Student:	Bc. Cristina Dorofti
Advisor:	doc. PhDr. Ing. Ing. Petr Jakubík Ph.D., Ph.D.
Title of the thesis:	The Impact of a Prolonged Period of Low Interest Rates Environment on Solvency And Profitability of Insurance Companies

OVERALL ASSESSMENT (provided in English, Czech, or Slovak):

The title of thesis is self-explanatory. The author deals with a very relevant and topical issue of the effect of low-yield environment on profitability and financial stability of insurance undertakings in Europe. The empirical evidence on this issue is scarce in existing academic literature and so the contribution of this work is very clear.

I enjoyed reading the thesis as it is not only contributive but also well structured, the empirical analysis is rigorous and the style of text is very nice too.

I have several minor comments, but these should be taken only as suggestion in case the author aims to use the text for PhDr thesis defense. Therefore **I strongly recommend the thesis for defense.**

As for the first introductory/theoretical part, I have several minor comments:

- On p. 10, the author claims that ROE and ROA „were developed with the aim of protecting policyholders’ interest, ergo expose insurers’ ability of paying out claims.” ROE and ROA serve as indicators of profitability to investors rather than supervisor. The insurer can experience losses (and they often do) and still be a perfectly safe business for policyholders as long as it is solvent and liquid.
- I would leave out the second paragraph on p. 15 about the monetary policy easing as it is not very rigorous and evidence-based.
- On p. 16 under the Figure 2.4.2. I see a rather too bold statement: „Generally, insurance companies are supposed to underperform due to the interest rate risk they are exposed to. Low interest rates rises the value of their liabilities and decrease the amount of returns earned from investments making it more difficult to find a profitable match in terms of duration which pushes them to seek higher/riskier yields jeopardizing their resilience on the long run. This leaves insurers with fewer alternative options.“ It is a matter of ALM quality and business specialization of the insurer and many factors plays it roles. The claim holds for insurer providing traditional insurance products with guarantees and with duration mismatch in its balance sheet. Insurers with closed IR gap or insurer focused on unit-linked products can profit even from IR declines (which was the case of many of the Czech insurers).
- I miss any citation/source in the very interesting last paragraph on p. 19 about Japanese insurance undertakings reallocating its investment portfolios.
- There is a short comment on Solvency II. The text would benefit from some expansion of that part (long term guarantees package etc.) as the topic is very relevant in context of prolonged period of low yield environment.

As for the first empirical part, I have several minor objections as well:

- The 4.1 section is overlapping with whole previous literature review part. I believe this happened as a consequence of putting a self-contained paper into the thesis.
- I might miss that but I couldn’t find some details on the data/variables: what currencies-interest rates pairs did the author choose for which insurer (some insurers operates in many countries and face different interest rate environments)? Are those averages or end-of-period data?
- I do not understand the choice of model specifications regarding the interest rate variables. It does not make sense to me the test a model with both nominal interest rate and inflation and then use a separate model with only real interest rate as an explanatory variable. The former employs inflation twice while the latter does not control for it at all. I would prefer a specification with real interest rate and inflation variables and another one with nominal interest rate (but without inflation).

Report on Bachelor / Master Thesis

Institute of Economic Studies, Faculty of Social Sciences, Charles University in Prague

Student:	Bc. Cristina Doroffi
Advisor:	doc. PhDr. Ing. Ing. Petr Jakubík Ph.D., Ph.D.
Title of the thesis:	The Impact of a Prolonged Period of Low Interest Rates Environment on Solvency And Profitability of Insurance Companies

- The relationship between interest rate and current profits is highly non-linear. As I already mentioned, ALM (hedging) and business lines are complex and a linear model cannot precisely fit the relationship. That being said, I do not question the main message of the text, but I would avoid too strong conclusions on the effects of further declines of interest rates on profitability.

SUMMARY OF POINTS AWARDED (for details, see below):

CATEGORY	POINTS
Literature (max. 20 points)	20
Methods (max. 30 points)	26
Contribution (max. 30 points)	30
Manuscript Form (max. 20 points)	16
TOTAL POINTS (max. 100 points)	92
GRADE (1 – 2 – 3 – 4)	1

NAME OF THE REFEREE: *Kalclav Hansenblea*

DATE OF EVALUATION: *15.9.2015*


Referee Signature