under the U.S. bankruptcy law is more beneficial to cash lenders: In the event of bankruptcy, cash lenders can typically sell their collateral, rather than be subject to an automatic stay as would be the case for a collateralized loan. "[1]

Repos can be bilateral, where there is a direct agreement between two counterparties whose custodian banks settle the trade, or they can be tri-party, where there is a third-party custodian bank settling the trade between two counterparties. The Bank of New York Mellon (BNY Mellon) and JPMorgan Chase are the two primary third-party custodian bank intermediaries for tri-party repos. $53 billion02/2019A>21e1 1q0.012 0 612 -792 re 612.792 reW*nBT/7516( )-59(a)-239(683(b)25

U.S. Insurer Exposure – Year-End 2018

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In exchange for securities lent, U.S. insurers receive cash and/or securities as collateral. They may, in turn, invest any cash received in securities so that collectively, all cash and securities become known as "reinvested collateral." Insurers can earn investment income on reinvested collateral, but in doing so, they must consider not only the credit risk of the additional investments, but also the asset/liability management risk relative to the lent securities.

As of year-end 2018, reinvested collateral held by U.S. insurers totaled about $50 billion in book/adjusted carrying value (BACV) based on data as reported in Schedule, DL Part 1 and in Schedule DL, Part 2. In comparison, reinvested collateral was about $55.6 billion at year-end 2017 (representing a 10% year-over-year [YOY] decrease) and $53 billion at year-end 2016. Since 2009, reinvested collateral has ranged from a low of $47 billion to a high of $63 billion. Table 1 shows the trend in historical U.S. insurer expo1.43 554.15 Tm0T-37(3(h)i2(ex(($)7(50T)-24(i)16(n)2121(3I(r)-7(ei)14(n)255(o)27(m)13(p)25(a)-20(r)-7(i)1

Repos

U.S. insurer exposure to repos and reverse repos has also traditionally been less than 1% of total cash and invested assets on an aggregate basis. Similar to securities lent, U.S. insurers report only the total amount of securities *associated* with repo activity; that is, the insurers did not necessarily lend out the full amount of the securities reported. They may have only lent a portion of the reported line item for which they received collateral from a counterparty (i.e., they represent securities initially sold in exchange for cash). As of year-end 2018, reported data showed that U.S. insurers had about $19.5 billion in BACV of securities associated with repos and reverse repos (in aggregate) compared to almost $21 billion at year-end 2017, representing a 6% YOY decrease. Table 3 shows the historical exposure going back to year-end 2013. As reverse repo activity has been relatively insignificant for U.S. insurers, it recommendations were published in reports by the FSB dated August 2013 and updated in a November 2015 report, relative to addressing financial stability risks arising from securities lending and repos. These recommendations, however, have yet to be implemented. More discussion about these report recommendations is included in the aforementioned, previously published, (July 2018) NAIC Capital Markets special report.

Chart 2: Value of Securities on Loan

Source: FSOC 2018 Annual Report

Total bilateral U.S. repo market activity was about $2.2 trillion as of year-end 2018 compared to a pre-crisis peak in 2007 of $4.5 trillion, according to data from the Securities Industry and Financial Markets Association (SIFMA). The triinsurance company and the cash is to be returned to the borrower; this helps identify potential liquidity constraints within the securities lending program.

Conclusion

Reinvested collateral from securities lending as well as repo activity has historically comprised less than 1% of total cash and invested assets. Insurers engage in securities lending as an investment strategy for short-term financing and to obtain additional yield income (on reinvested collateral held in exchange for securities lent to counterparties), and they engage in repo activity mostly to raise short-term cash and access low-risk cash flow.

While banking regulators have coordinated to establish procedures to monitor activity for the sake of financial stability, insurance regulators have made efforts to monitor this activity for solvency.

The NAIC Capital Markets Bureau will continue to monitor trends in the securities lending and repo markets and report as deemed appropriate.

Useful Links:

NAIC Capital Markets Primer – Securities Lending, June 2018

FSOC 2018 Annual Report