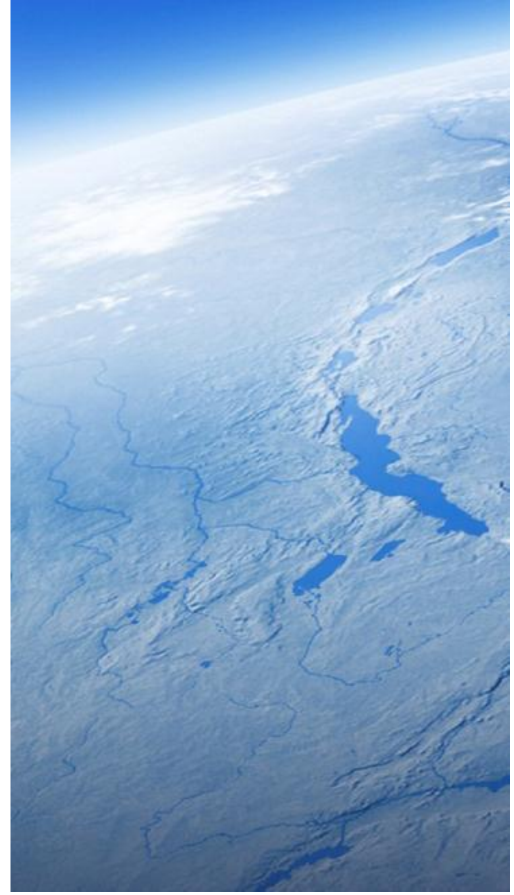
CURRENT ISSUES IN GENERAL INSURANCE:
LLOYD'S UPDATE

Jerome Kirk & Henry Johnson – Lloyd's

2 May 2013

AGENDA

- Year-end 2012
  - results
  - reserves and reserving
  - capital
- Capital Setting
  - last year
  - going forward
- Solvency II
- Summary & Questions

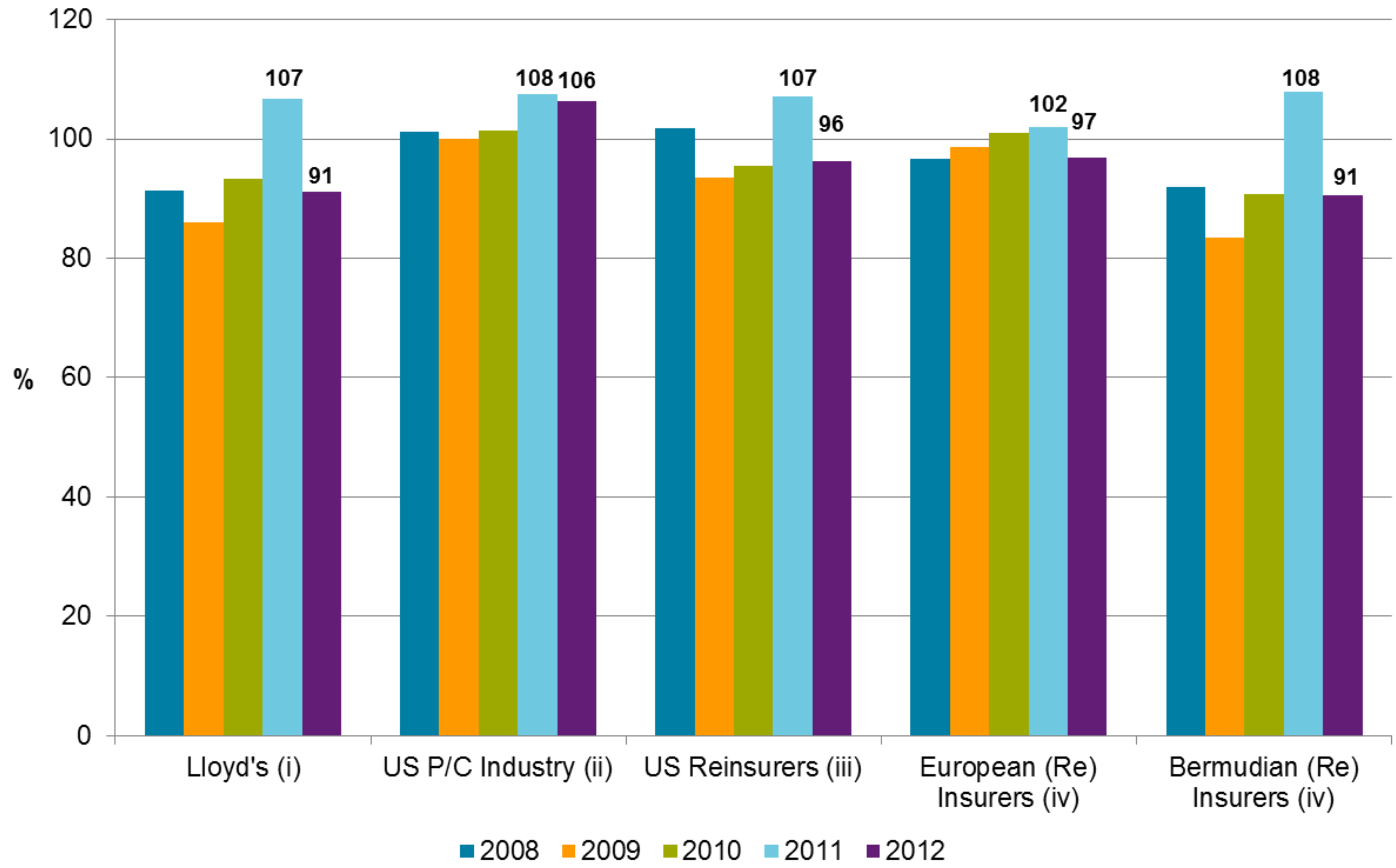

YEAR-END 2012

STRONG UNDERWRITING RESULT SEES RETURN TO PROFIT….

£m	2011	2012
Gross written premiums	23,477	25,500
Combined ratio	106.8%	91.1%
Investment return	955	1,311
Result before tax	(516)	2,771
Return on capital (pre-tax) %	(2.8)	14.8

... WITH LLOYD'S PERFORMING FAVOURABLY AGAINST PEERS

COMBINED RATIO



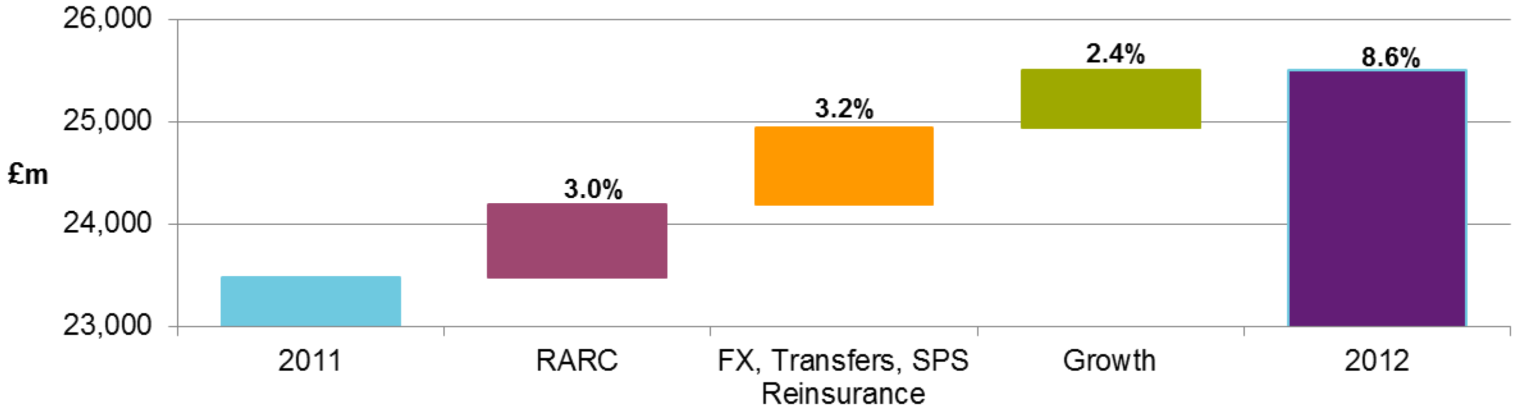
Sources: i) Lloyd's pro-forma financial statements, ii) Insurance Information Institute, iii) Reinsurance Association of America (iv) Company data (8 European companies: 17 Bermudian companies)

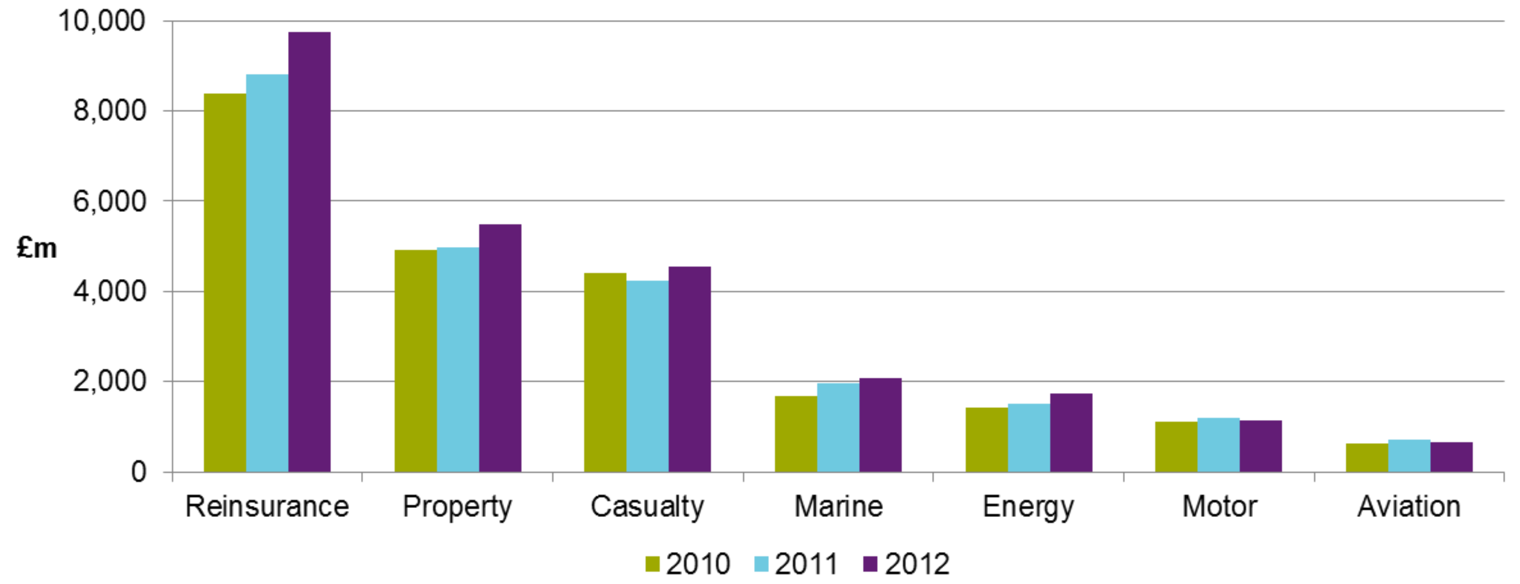
WHICH SEES A HEALTHY RETURN ON CAPITAL OF 12% OVER FIVE YEARS

	2008	2009	2010	2011	**2012**
Pre-tax result £bn	1.9	3.9	2.2	(0.5)	**2.8**
Combined ratio (%)	91.3	86.1	93.3	106.8	**91.1**
Investment return (%)	2.5	3.9	2.6	1.9	**2.6**
Gross written premiums £bn	18.0	22.0	22.6	23.5	**25.5**
Net resources[1] £bn	15.3	19.1	19.1	19.1	**20.2**
Pre-tax ROC (%)	13.7	23.9	12.1	(2.8)	**14.8**
Pre-tax ROC 5 year average (%)					**12.1**

Source: Lloyd's pro forma financial statements, 31 Dec 2012
[1] Capital, reserves & subordinated loan notes and securities

THE UNDERLYING PREMIUM GROWTH IS 2.4%



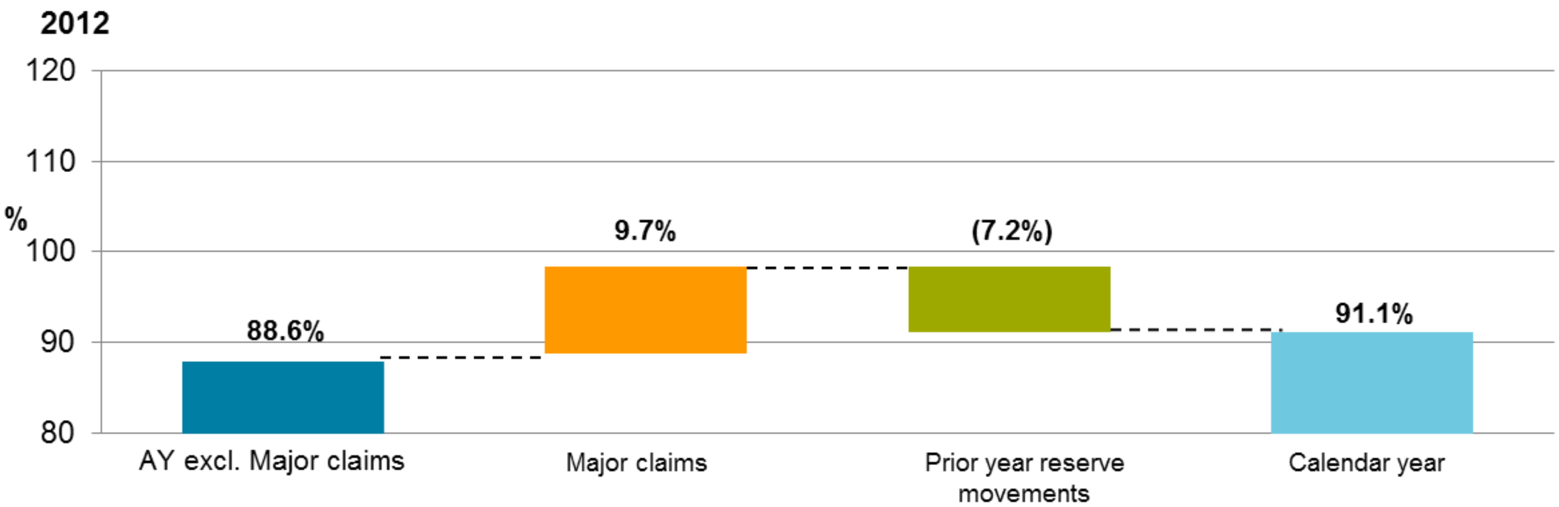


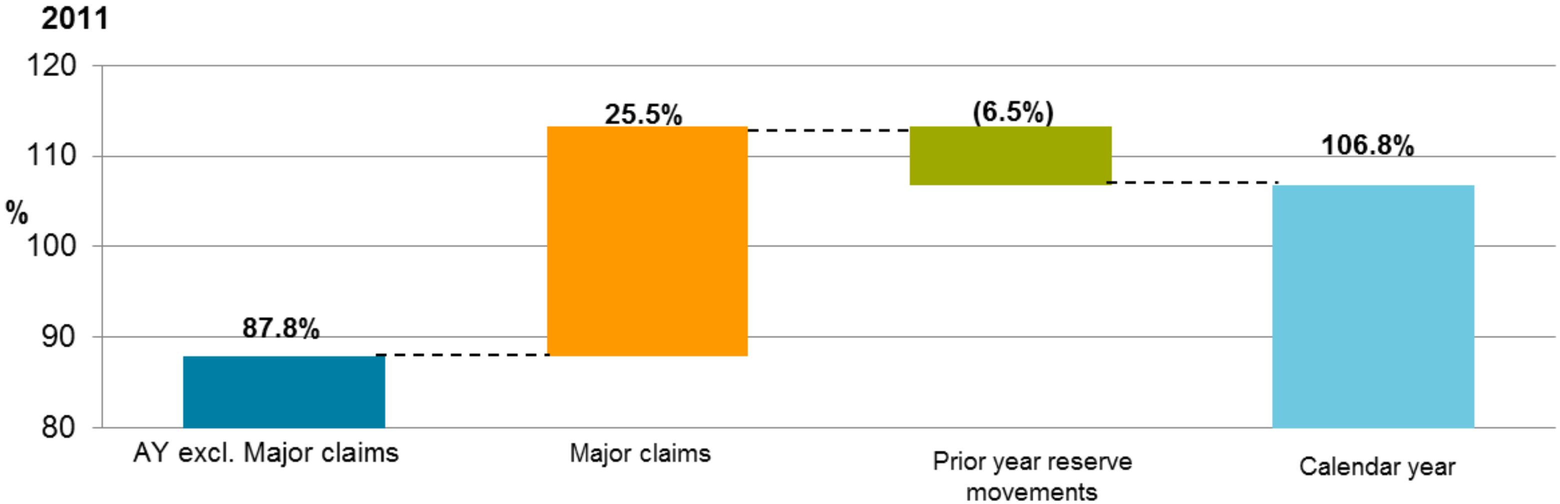
Source: *Lloyd's pro forma basis*

*RARC: Risk Adjusted Rate Change; FX: Impact of translating business written in foreign currency at average rates of exchange * SPS: Special Purpose Syndicates*

AS WITH RECENT YEARS, THE RESULTS ARE ASSISTED BY PRIOR YEARS RELEASES….

COMBINED RATIOS

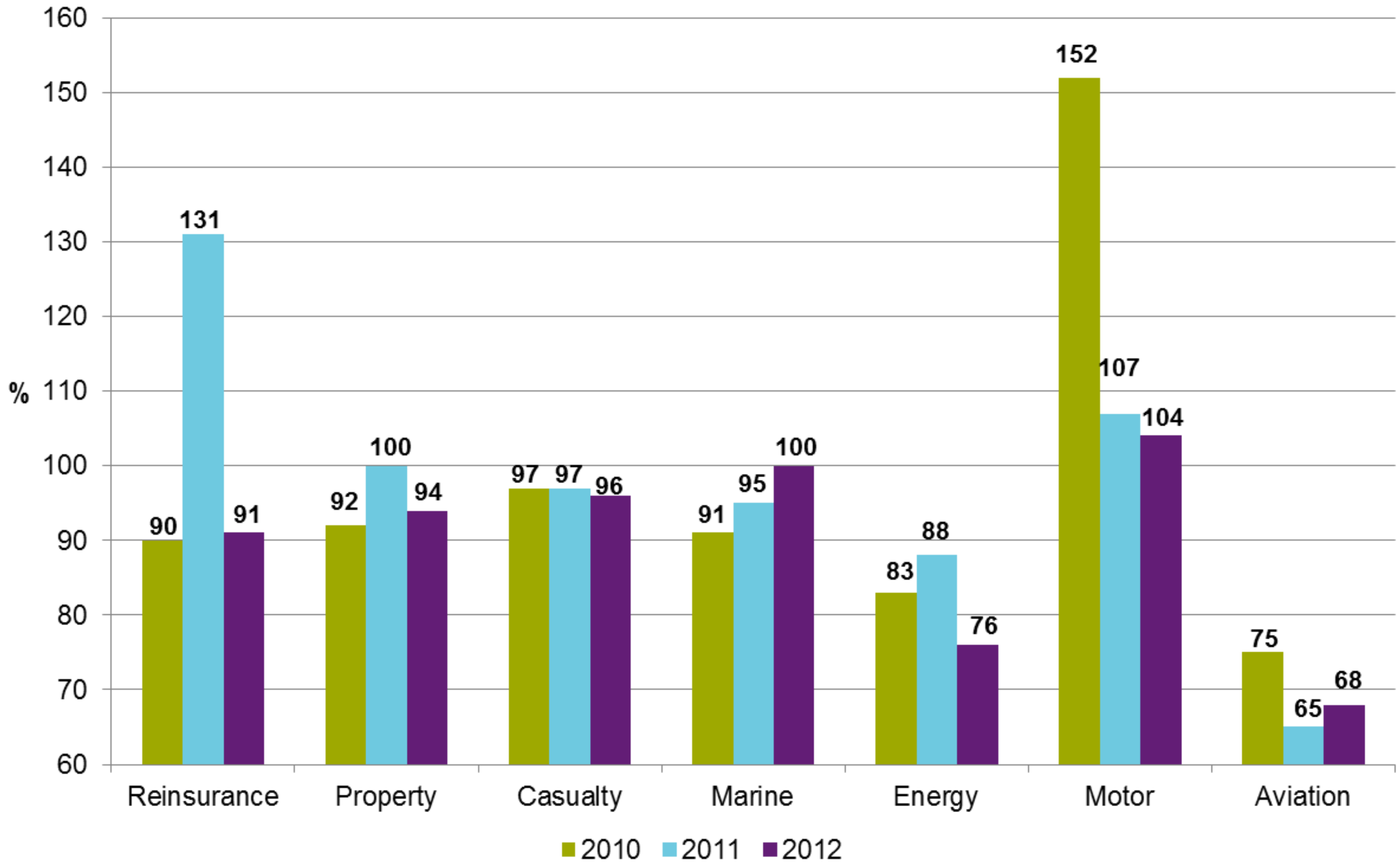




Source: Lloyd's pro forma basis

MOST CLASSES WERE PROFITABLE WITH MARINE IMPACTED BY SANDY & COSTA CONCORDIA

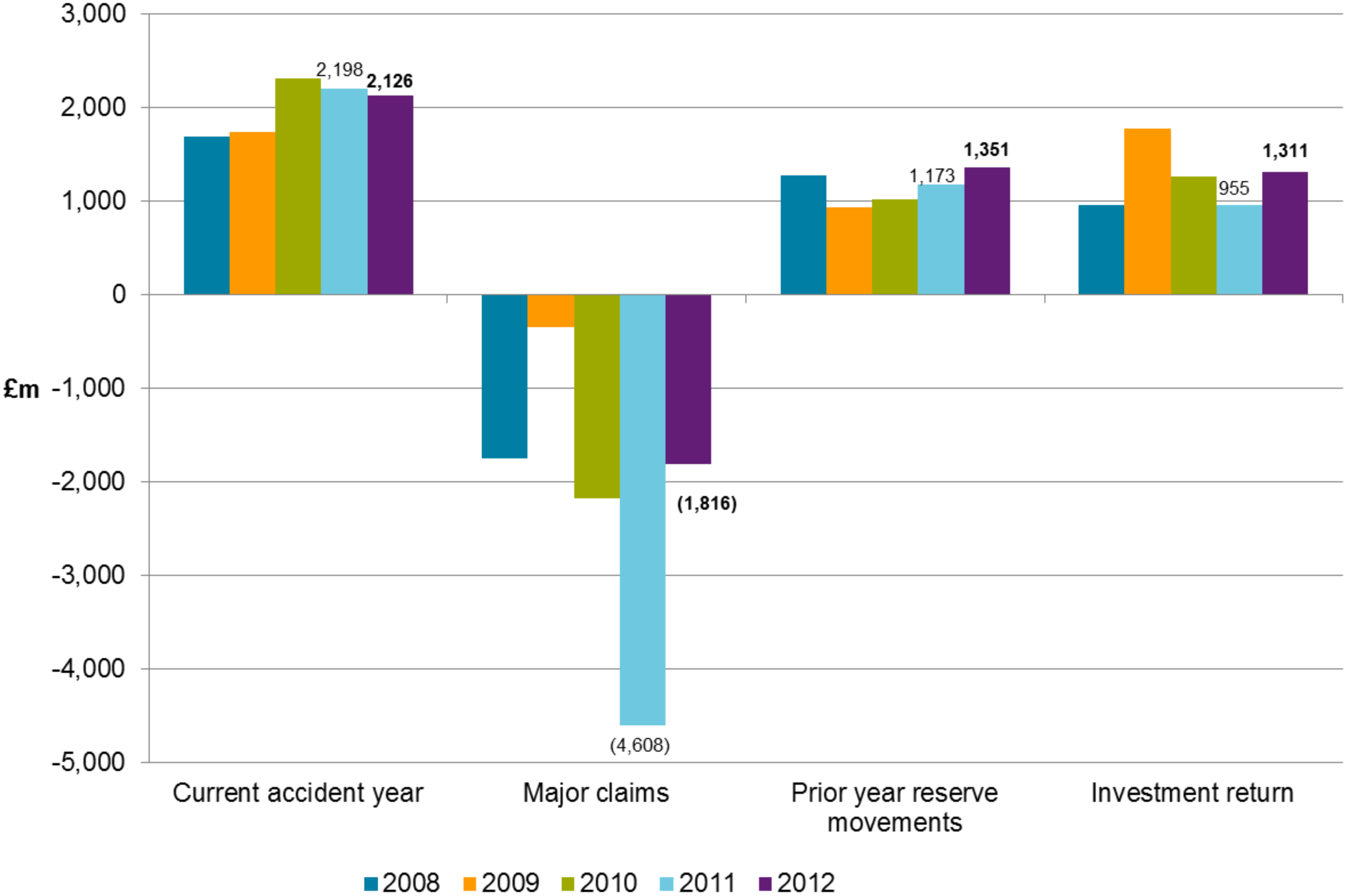
CALENDAR YEAR COMBINED RATIO



NEP:	£6.7bn	£4.0bn	£3.5bn	£1.7bn	£1.1bn	£1.1bn	£0.5bn

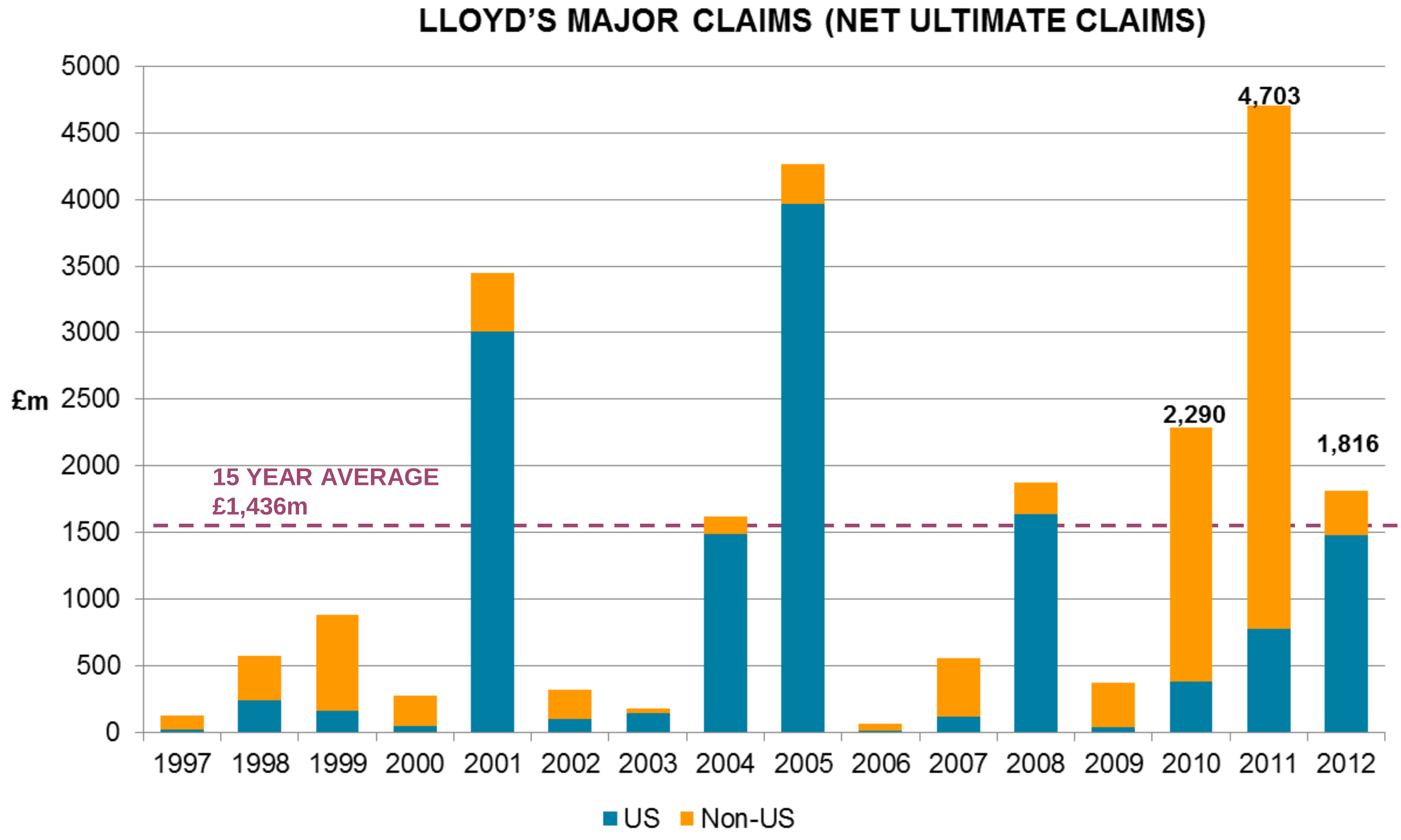
Source: Lloyd's pro forma basis at syndicate level, Dec 2012
NEP: Net Earned Premium

AND CAN SEE THAT RECENT PROFIT & LOSS VOLATILITY IS DRIVEN BY MAJOR CLAIMS…



Source: Lloyd's pro forma financial statements

... WITH 2012 DOMINATED BY US MAJOR CLAIMS EVENTS



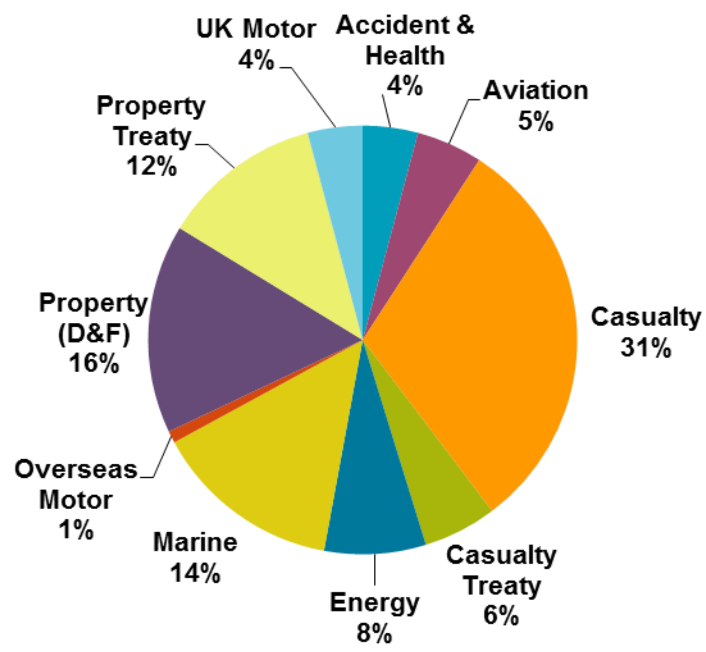
Source: Lloyd's pro forma basis. Indexed to December 2012
Claims in foreign currency translated at the exchange rate prevailing at the date of loss



RESERVES

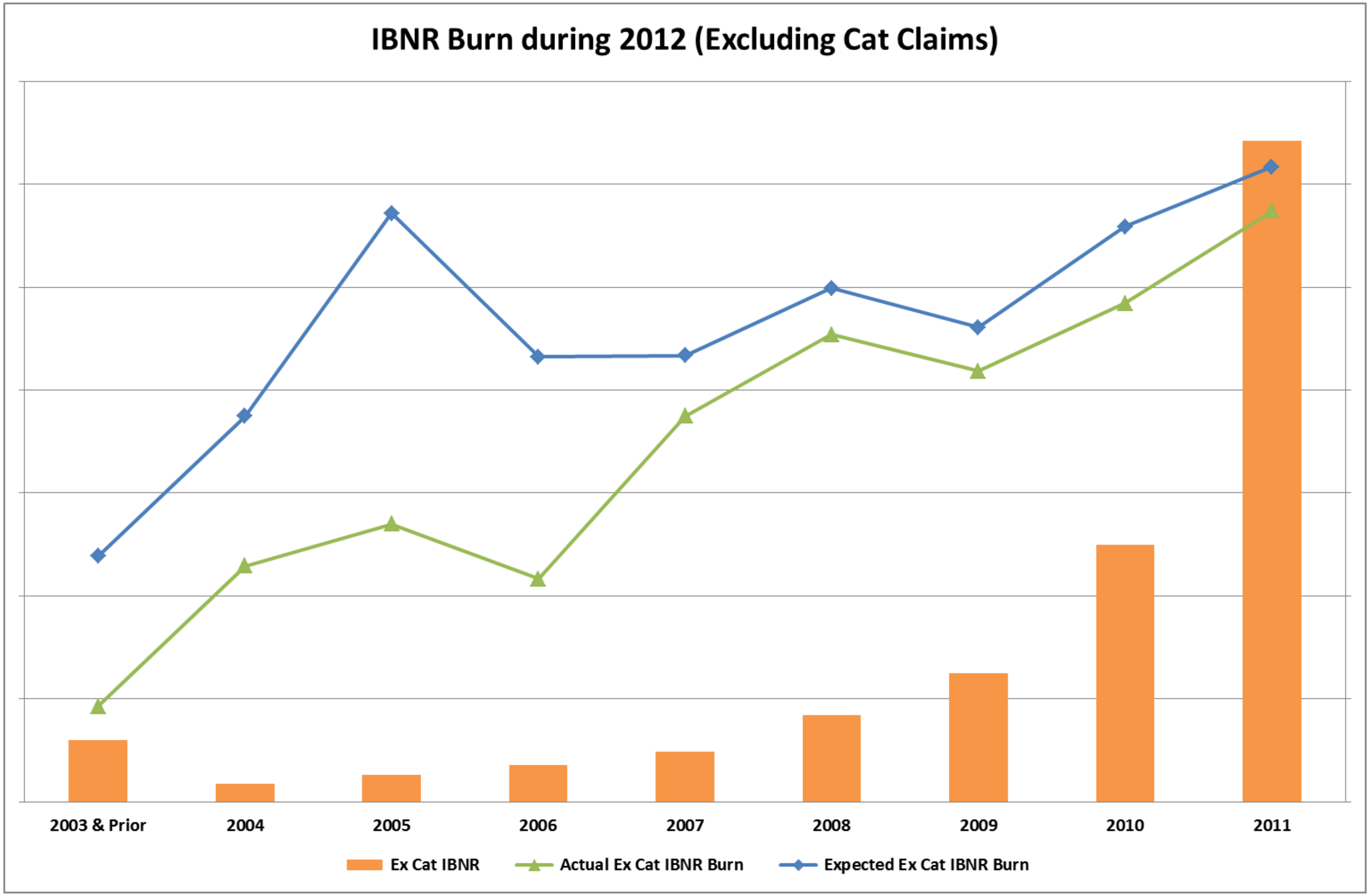
EARNED RESERVES ARE SLIGHTLY LOWER AT YEAR-END 2012

	Net of Reinsurance (excl. ULAE) £m	
High level COB	Earned Reserves	Unearned Reserves (net of DAC)
Casualty	9,731	1,181
Property (D&F)	3,898	1,732
Marine	3,915	1,151
Property Treaty	3,652	682
Energy	1,983	750
Casualty Treaty	1,809	172
Aviation	1,422	363
Accident & Health	1,069	415
UK Motor	1,093	384
Overseas Motor	235	87
Total	**28,808**	**6,917**
Total as at 2011 year-end	*29,053*	*6,398*



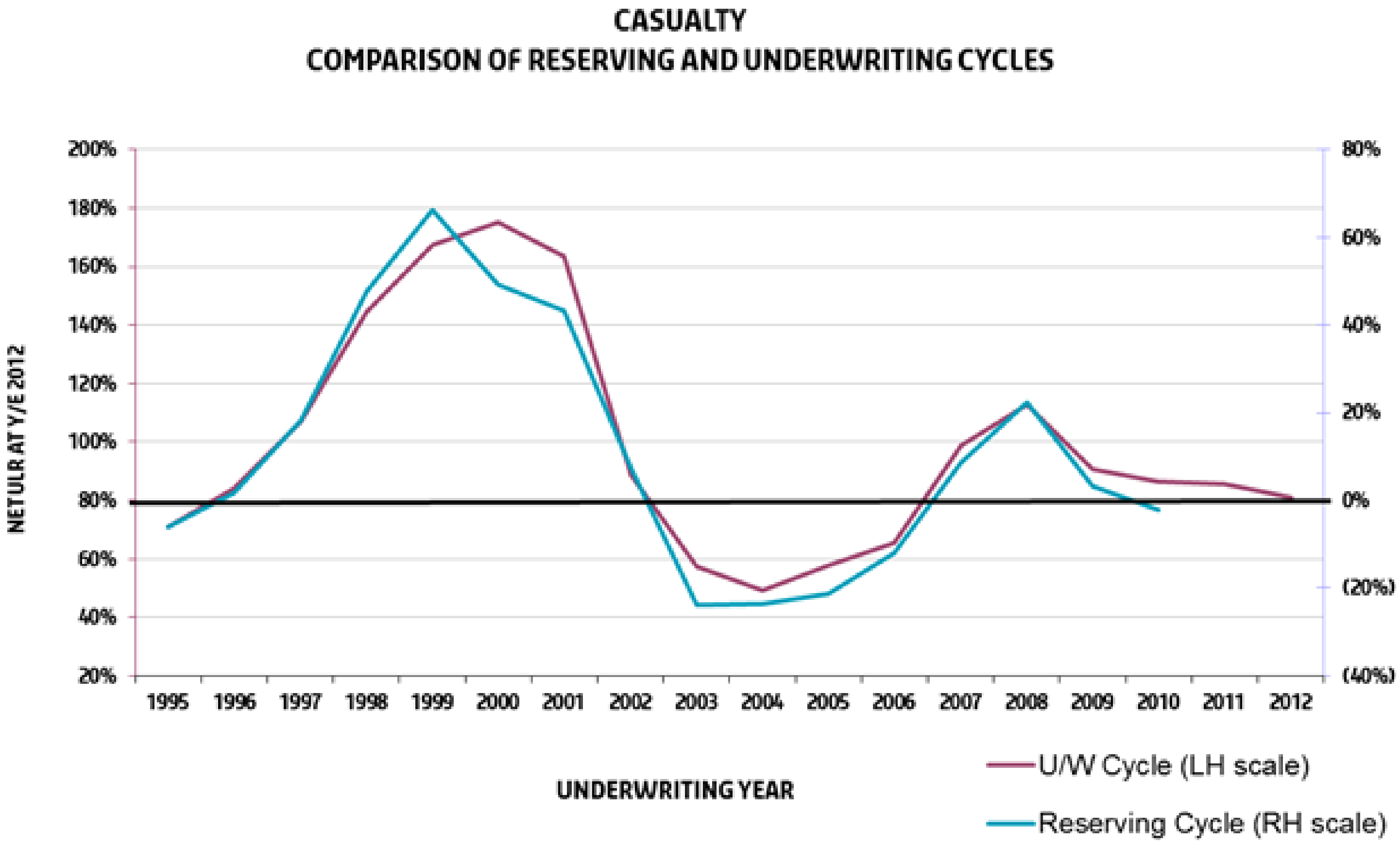
Source: Lloyd's TPD database. All figures as at year-end 2012 exchange rates.

THE RESERVE RELEASES ARE SUPPORTED BY BETTER THAN EXPECTED EXPERIENCE



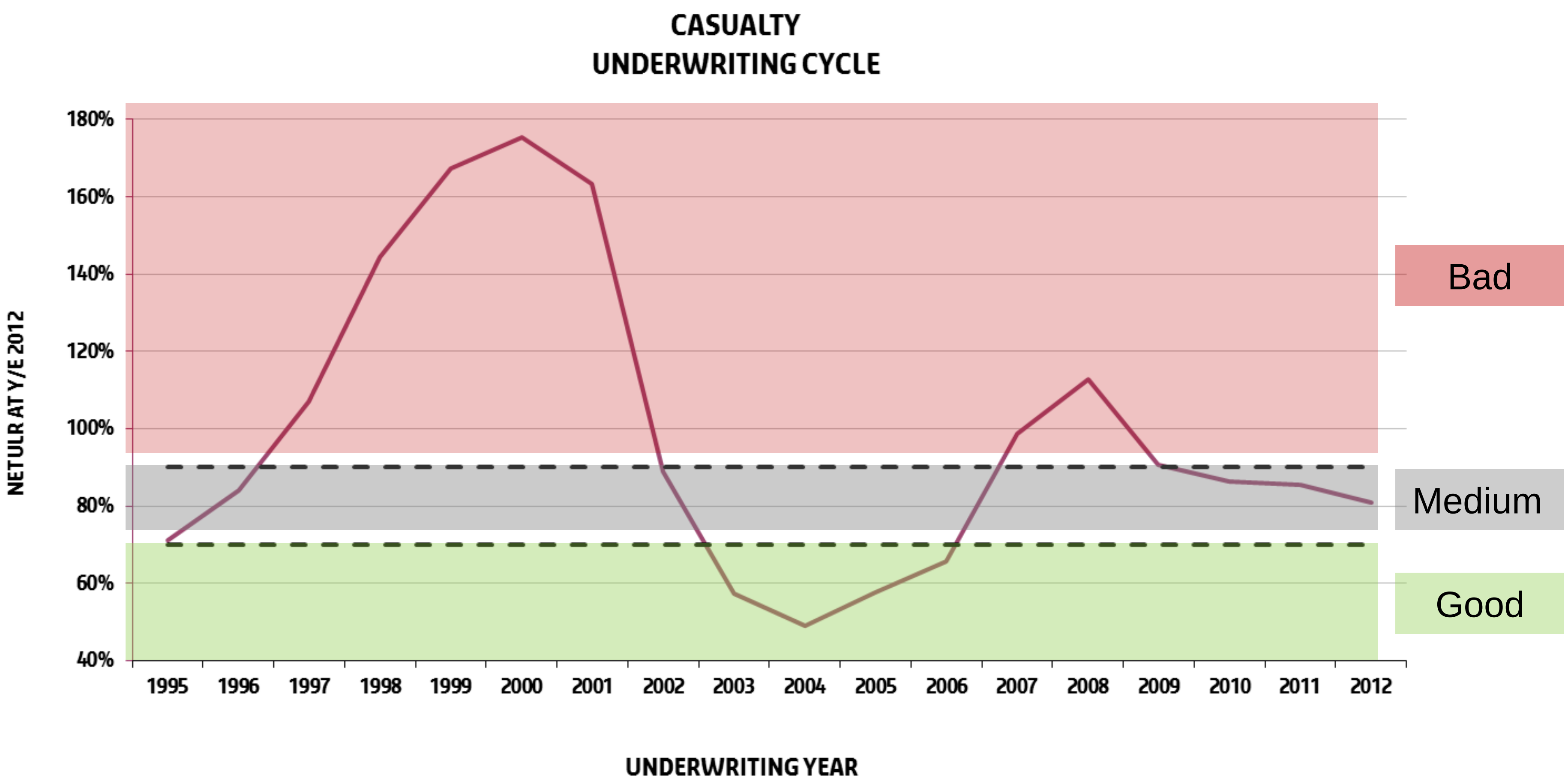
Source: MRC Q4 2012 Early Warning results

AND NO NEW CONCERNS IN TERMS OF THE RESERVE CYCLE



Source: Lloyd's Provisional TPD – currently excludes 1 syndicate

WHAT ARE THE IMPLICATIONS OF A PERIOD OF 'MEDIUM' YEARS?



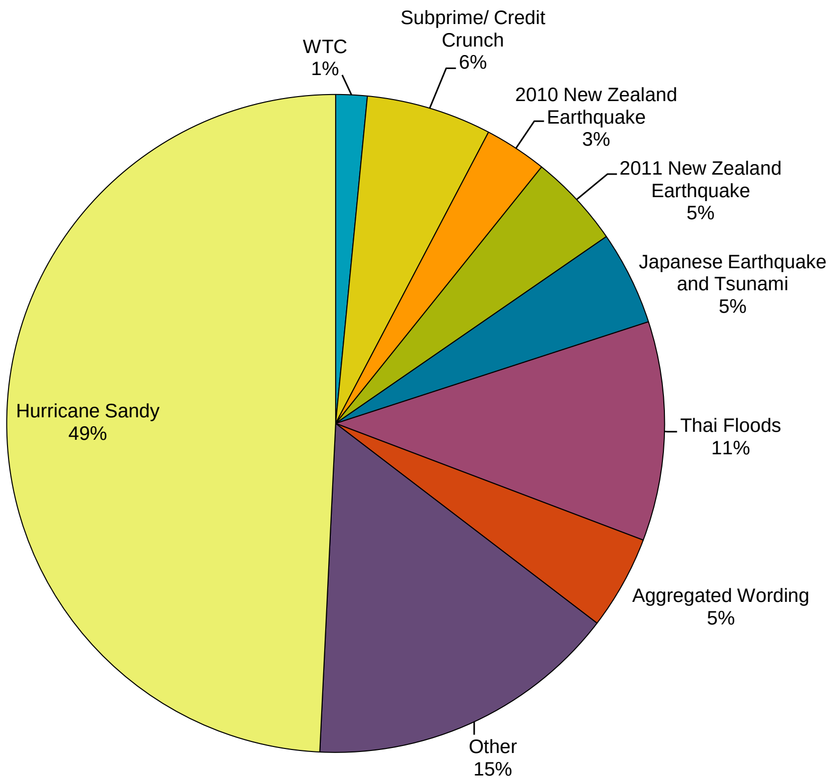
Source: Lloyd's provisional TPD database – Excludes one syndicate. Net of reinsurance

MORE EMPHASIS ON REFINING RATHER THAN OVERHAULING BOOKS

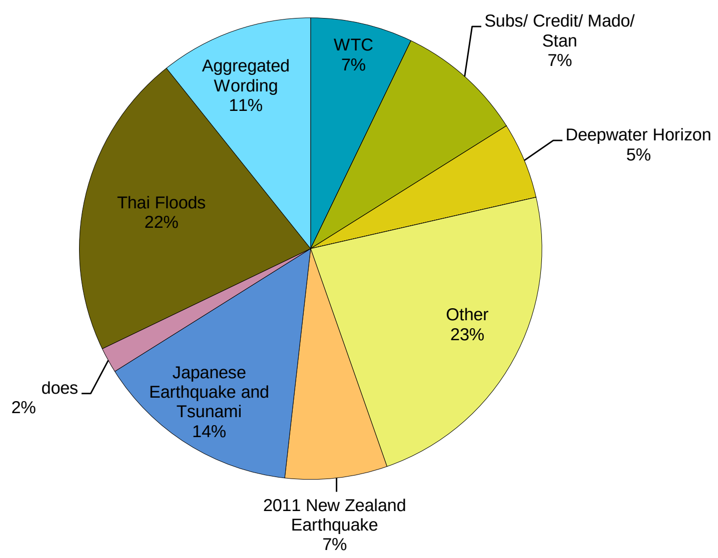
- Some key principles:
  - controlled growth
    - focus on “good performance”
    - or genuine new opportunities
  - removing underperforming elements
    - or re-underwriting
  - review of reinsurance efficiency
  - keep an eye on T&Cs
  - keep an eye on costs

AS EXPECTED, LARGE LOSS WORDINGS ARE DOMINATED BY THE RECENT CATS…

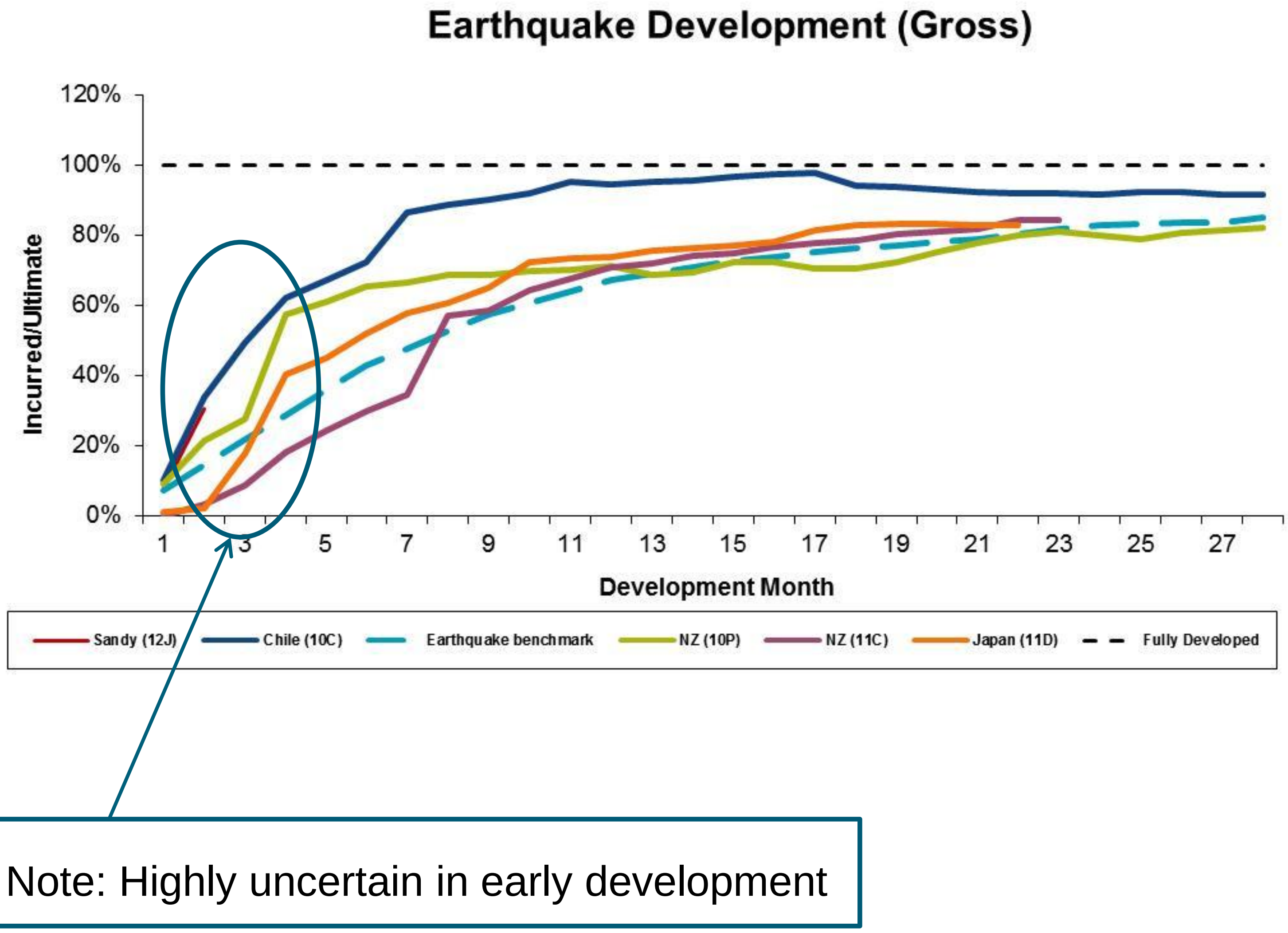
2012 - WORDING ≥3



2011 - WORDING ≥ 3



… AND THE OLDER EVENTS SEE CONTINUED STABILITY IN THEIR RUN OFF



WHICH CONFIRMS FEW “LONG TAIL” ISSUES

- Year-end 2012 saw:
  - reduction in wordings relating to previous events
  - with new wordings introduced mainly for the 2012 events

Event	2011	2012	Comparison
WTC	4	1	(3)
Subprime/ Credit Crunch	5	4	(1)
Deepwater Horizon	3	0	(3)
2010 New Zealand Earthquake	0	2	2
2011 New Zealand Earthquake	4	3	(1)
Japanese Earthquake and Tsunami	8	3	(5)
US Tornadoes	1	0	(1)
Thai Floods	12	7	(5)
Hurricane Sandy	N/A	32	32
Aggregated Wording	6	3	(3)
Other	13	10	(3)
Total	**56**	**65**	**9**

Source: Lloyd’s SAO analyses – Wordings of severity 3 or 4

OVERALL THERE REMAINS COMFORT IN THE WAY RESERVES ARE DEVELOPING…

- Non-cat loss development in calendar-year 2012 has performed better than expected
  - this is a continuation from recent calendar years
  - and is across most classes and most underwriting years and in particularly the older years (1993-2006)
- There are no “new” non-cat reserving issues on top of:
  - UK Motor
  - Italian Hospitals
  - PPOs
- There are always a few syndicate specific and general issues but currently they are all minor

… WITH PPOs AS POSSIBLY THE LARGEST ITEM OF CONCERN

- Current PPOs need to be valued
  - including discounting and inflation assumptions
- And known claims that could become PPOs
  - these are treated in a similar fashion to potential increases
  - can look at value of claim if PPO / not PPO (inc probability of each)
  - general expectation is PPOs will cost insurer more
- And PPO pure IBNR
  - we do expect consideration of "PPO IBNR"
  - highly uncertain but need to be clear on assumptions
- Asked for specific comments in SAO reports

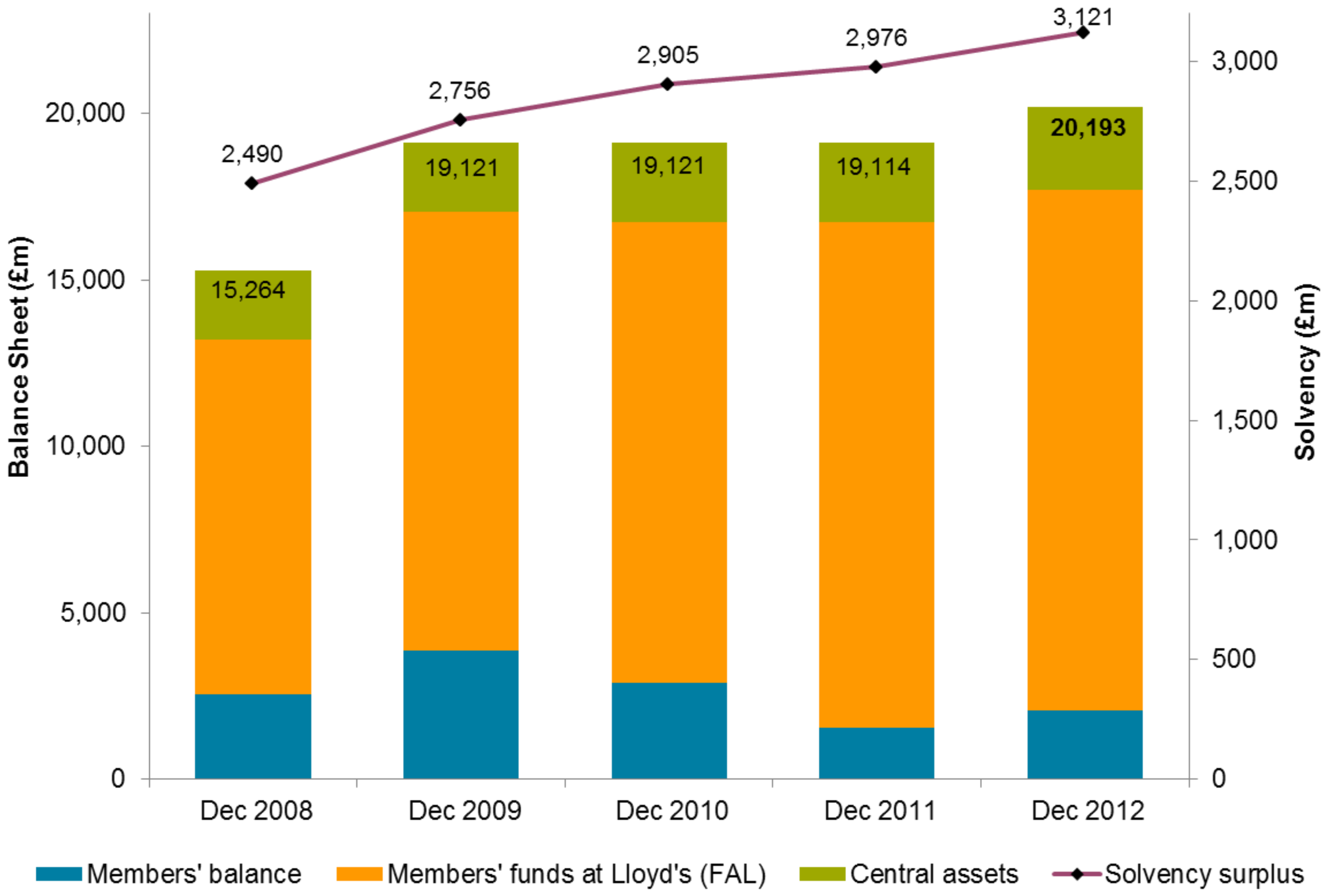


CAPITAL

THE POSITIVE RESULTS HAVE SEEN NET RESOURCES INCREASE TO OVER £20BN …

£m	Dec 2010	Dec 2011	**Dec 2012**	**YTD %**
Cash and investments	48,483	51,415	**51,767**	1
Reinsurers' share of unearned premium	1,458	1,557	**1,759**	13
Reinsurers' share of claims outstanding	8,779	10,597	**10,680**	1
Other assets	11,890	12,979	**13,885**	7
Total assets	70,610	76,548	**78,091**	2
Gross unearned premiums	(10,525)	(10,605)	**(11,314)**	7
Gross claims outstanding	(36,303)	(41,313)	**(40,203)**	(3)
Other liabilities	(5,061)	(5,516)	**(6,381)**	15
Net resources	19,121	19,114	**20,193**	6
Represented by: Members' assets	16,744	16,726	**17,708**	6
Central assets	2,377	2,388	**2,485**	4
	19,121	19,114	**20,193**	6

… WITH SOLVENCY SURPLUS NOW ABOVE £3BN



AND IN TERMS OF THE CHAIN OF SECURITY:

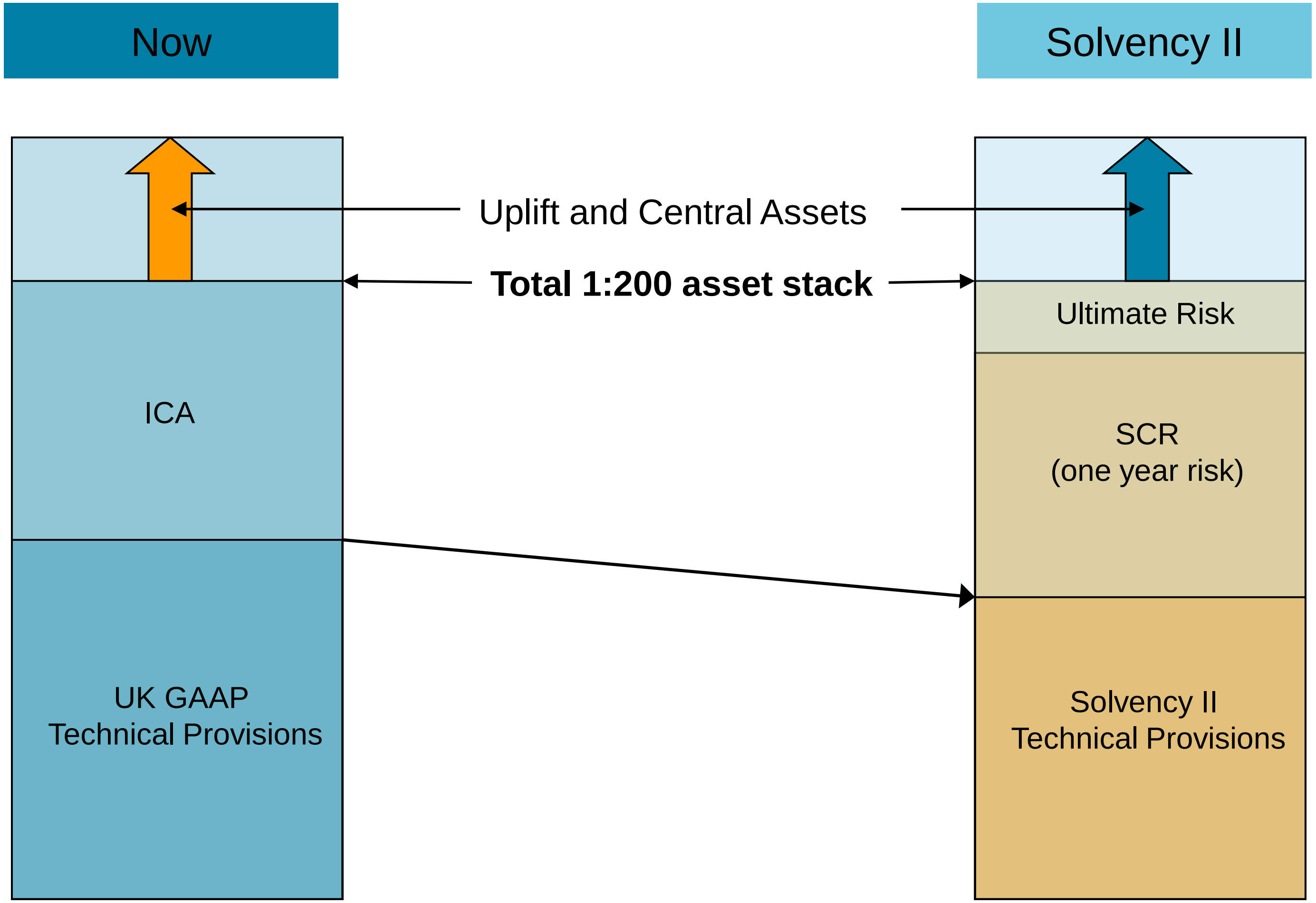
First link	Syndicate level Assets **£41,126m**		All premiums received by a syndicate are held in its premium trust funds and are the first resource for paying policyholder claims from that syndicate.	1
Second Link	Members Funds at Lloyd's **£15,660m**		Each member provides Capital to support its underwriting at Lloyd's. Each managing agent produces an Individual Capital Assessment stating how much capital it requires to cover its underlying business risks at a 99.5% confidence level.	2
Third Link	Central Fund **£1,459m** Corporation **£133m** Subordinated Debt/ Securities **£893m**	Callable layer **£745m**	The Central Fund is available at the discretion of the Council of Lloyd's to meet any valid claim that cannot be met by the resources of any member. It is funded by members' annual contributions and subordinated debt issued by the Corporation in 2004 and 2007.	3

Source: Lloyd's pro forma financial statements, 31 December 2012



CAPITAL SETTING

CAPITAL NOW SET USING A "SOLVENCY II" BASIS WHILST ENSURING EQUIVALENCE TO ICAS

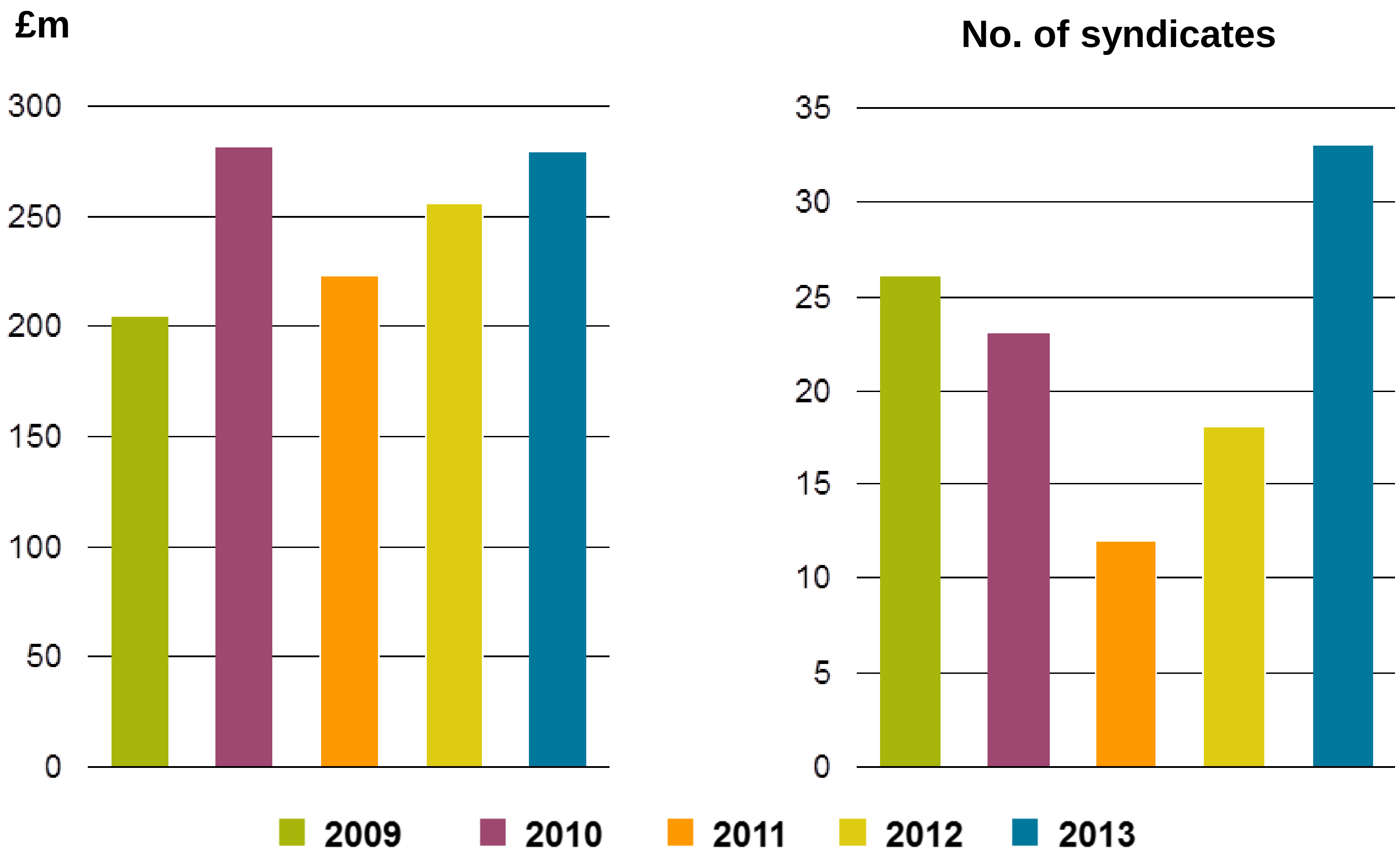


DURING THE 2013 REVIEW, THE REQUIRED CAPITAL INCREASED FOR SEVERAL REASONS

- Reserve margins restricted to SAO view
- Business plan assumptions
  - expected loss ratios
- Parameters understated
  - diversification between insurance risk and other risks
  - diversification between classes of business
  - market risk
  - catastrophe risk; LCM peak perils and worldwide

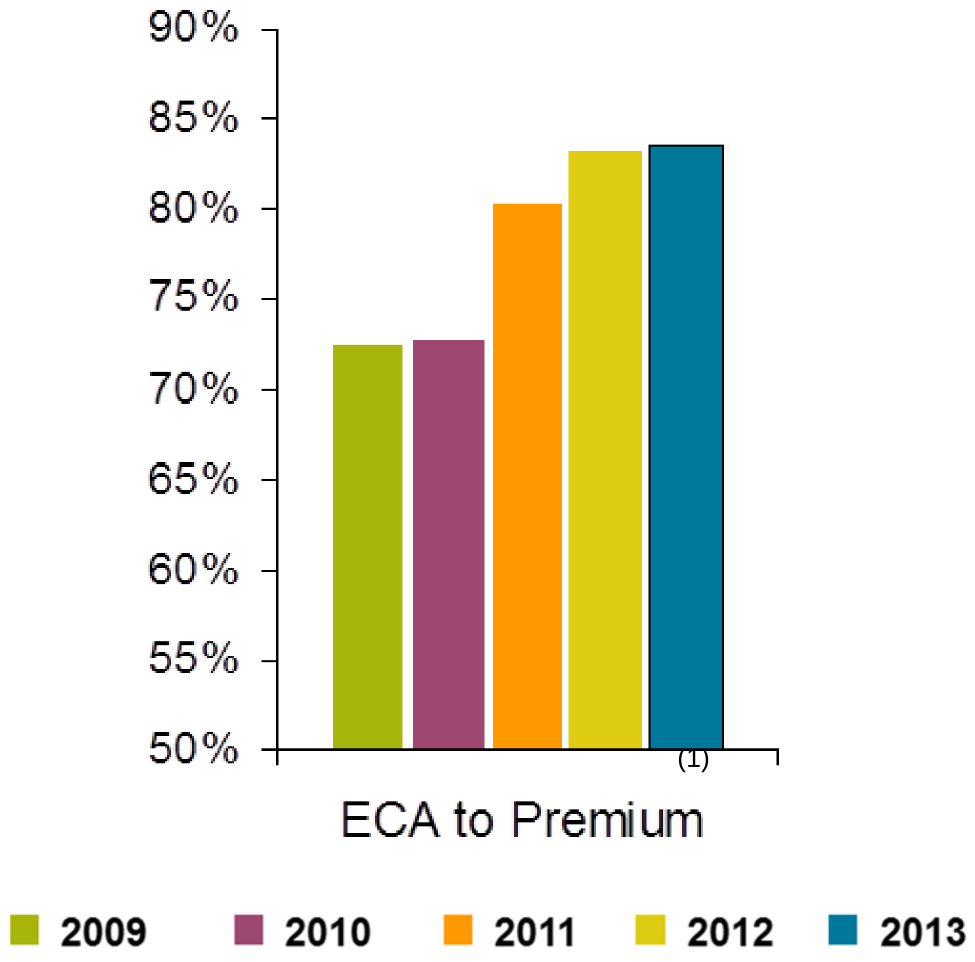
- Diversification was the item that caused the most discussions

RESULTING IN A SIMILAR IMPACT TO THE PREVIOUS FULL REVIEW (BY AMOUNT)



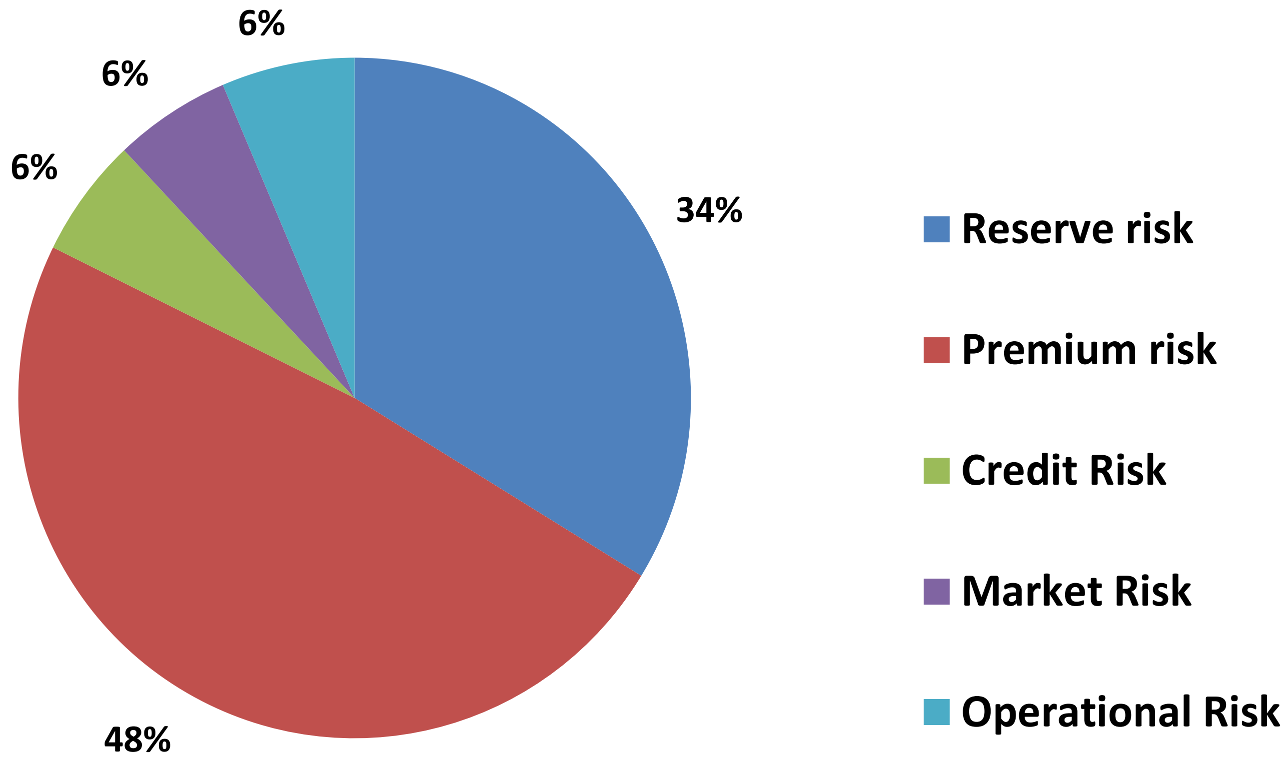
Increases to final submitted ICA / uSCR following Lloyd's review

ECONOMIC CAPITAL REMAINS AT 83% OF GROSS PREMIUM



(1) Excludes reserve margin credit

AS EXPECTED, INSURANCE RISK DOMINATES SYNDICATE ICAS



Note: Insurance diversification apportioned between Reserving and Underwriting Risks

Source: Lloyd's ICA pro-forma

DIVERSIFICATION WILL BE A FOCUS OF THE 2014 REVIEW

- Lloyd's view when setting syndicate capital:

"*Each risk component makes a positive contribution to the SCR.*"

- Corollary: "*That includes market risk*"
- Rationale: at the 99.5th, almost everything will be "pear-shaped"
- The Market did not always agree
  - diversification was the most frequent reason for loadings
  - this will set a cap on the overall diversification credit
- A similar approach was adopted under ICAs

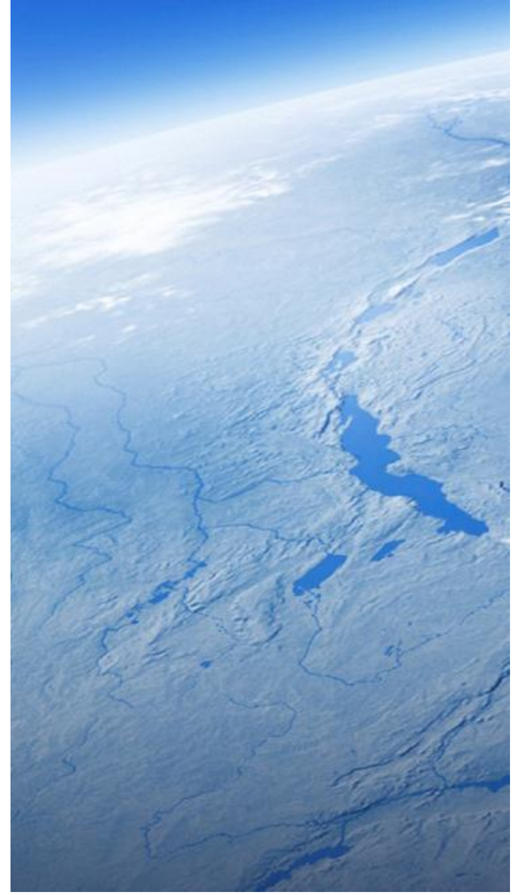
WE HAVE MERGED THE CAPITAL AND BUSINESS PLANNING PROCESSES

- The new Capital and Planning Group (CPG) has formed
- Jointly sponsored by the Director, Performance Management and Director, Finance and Operations (or Luke & Tom)

- CPG has the authority:
  - to approve Syndicate Business Plans including any Franchise Guideline dispensations
  - to approve Syndicate Capital Requirements on both a one year and ultimate basis before economic uplift
  - to communicate decisions made by the group to key stakeholders within Lloyd's and to Managing Agents

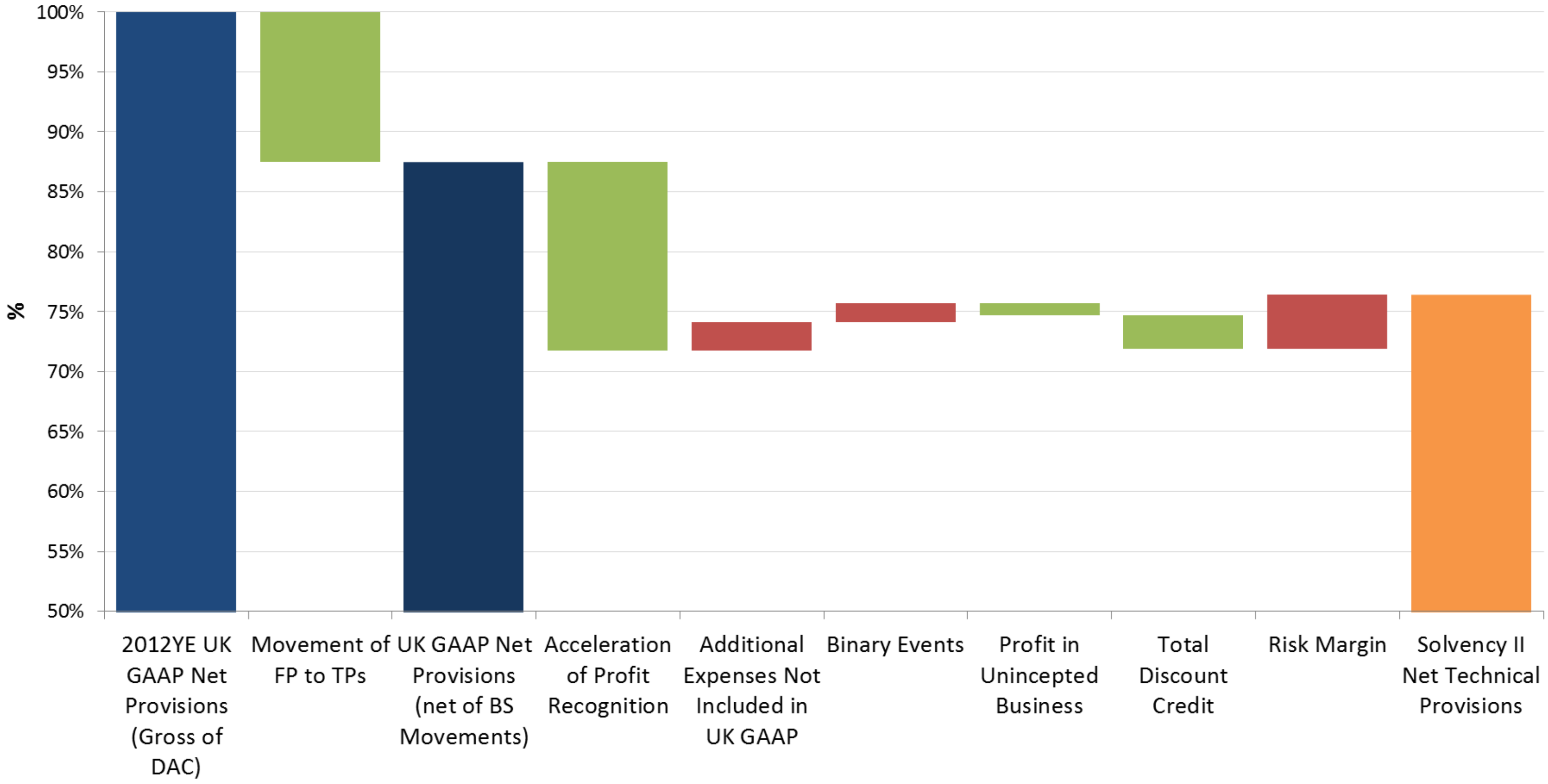
WITH THE KEY DATES SLIGHTLY DIFFERENT FOR THIS YEARS REVIEW

Submissions deadline	SBF and LCR	Required submissions
4 July 2013	• Provisional 2014 SBF • Draft 2014 LCR	• Aligned and non-aligned syndicates
12 September 2013	• Final 2014 SBF	• Aligned and non-aligned syndicates
	• Final 2014 LCR	• Non-aligned syndicates • Any aligned syndicates that have third party capital backing • Special Purpose Syndicates (SPS)
19 September 2013	• Final 2014 LCR	• Aligned syndicates


SOLVENCY II

THE IMPACT ON TPS IS STILL SIGNIFICANT – AND WILL IMPACT CAPITAL



Source: Lloyd's QMC/ TPD returns

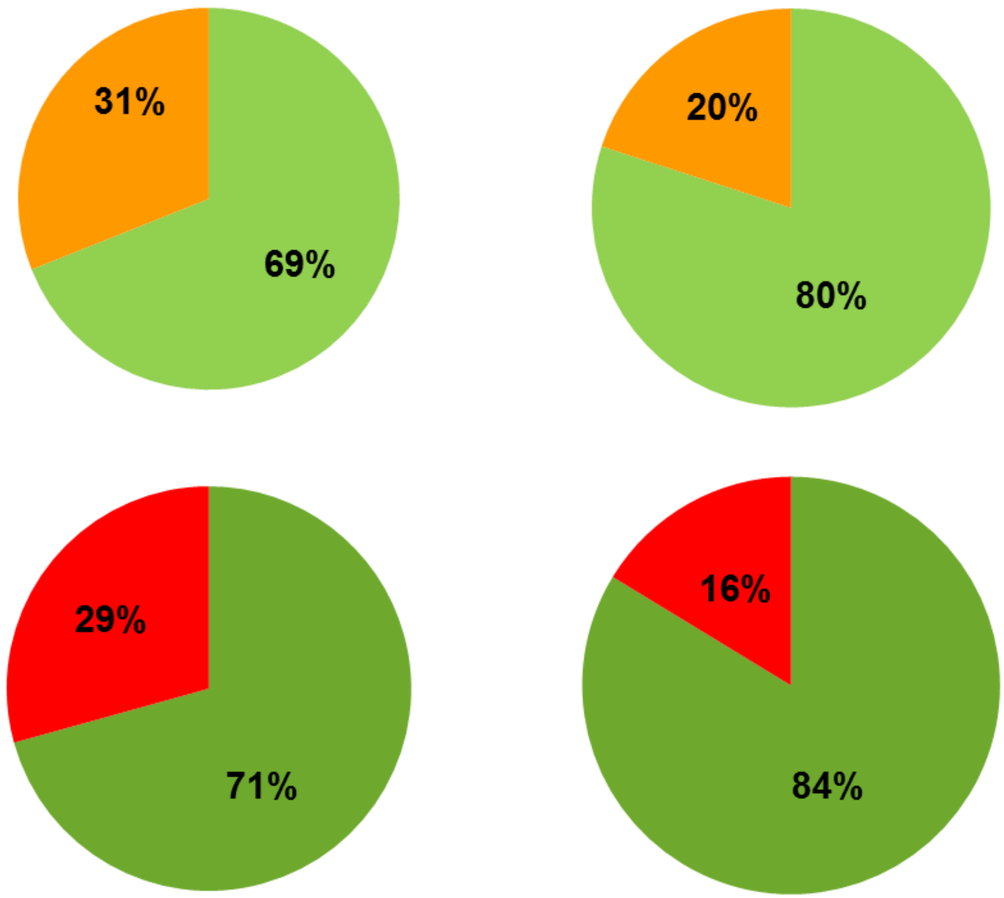
FAS ASSESSMENTS COMPLETE AND POSITION AS AT 31 JAN CONFIRMED TO AGENTS

By Agent

By 2013 SCR

RAG RATINGS @ 31 JANUARY

DROP ASSESSMENTS TO 31 JANUARY



	Meets principles
	Does not meet principles

COMMON ISSUES DRIVING "FAILS" ON PRINCIPLES

AREA/PRINCIPLE	ISSUES OUTSTANDING
ORSA	• Stress & scenario testing • Forward looking assessment • Clear conclusions and management actions
Validation	• Evidence of feedback loop and follow up/tracking of validation failures • Validation report does not provide sufficient evidence of validation work performed and conclusions
Model Change	• Clear rationale for change triggers • Clear approach for the aggregation of minor changes
Use Test	• Q4 2012 interviews did not support understanding of model or effectiveness of board training • Evidence of actual model use outside of running SCR
Documentation	• Submitted documents do not support controls and processes established • Documents do not explicitly cover tests and standards requirements

HAVE SEEN NO REVISED SII TIMETABLE ISSUED BY EUROPEAN COMMISSION

- Current stance by EC is no ‘Quick Fix 2’ legislation proposed
  - would mean technical application of new regime at 1 January 2014 but **unlikely to** be enforced in practice
  - earliest practical start date still 1 January 2016 but could be later
- PRA will not extend interim requirements beyond ICAS+ transition
  - permits firms to use Solvency II calibrated models to meet ICAS
  - aligns with Lloyd’s “soft landing” approach for managing agents
- EIOPA’s focus now on applying “interim measures”
  - published 27 March 2013 for consultation
  - aim for harmonised transition
  - and does cover many aspects of the directive……

GIVEN 2014 FULL IMPLEMENTATION NOW "COMPLETELY UNREALISTIC"

Lloyd's does want to

- Apply a pragmatic approach which enables cost effective completion of the programme
- Continue to use SCR models for capital setting
- Leverage the benefits of Solvency II without being held to the entirety of the Solvency II tests and standards
- Assist agents in developing and enhancing the most valuable aspects
- Complete a robust assessment and review of Lloyd's existing minimum standards to ensure alignment with Solvency II

But we don't want to

- Enforce full compliance an expected 3 years ahead of implementation
- Lose the good work done to date and allow it to lapse

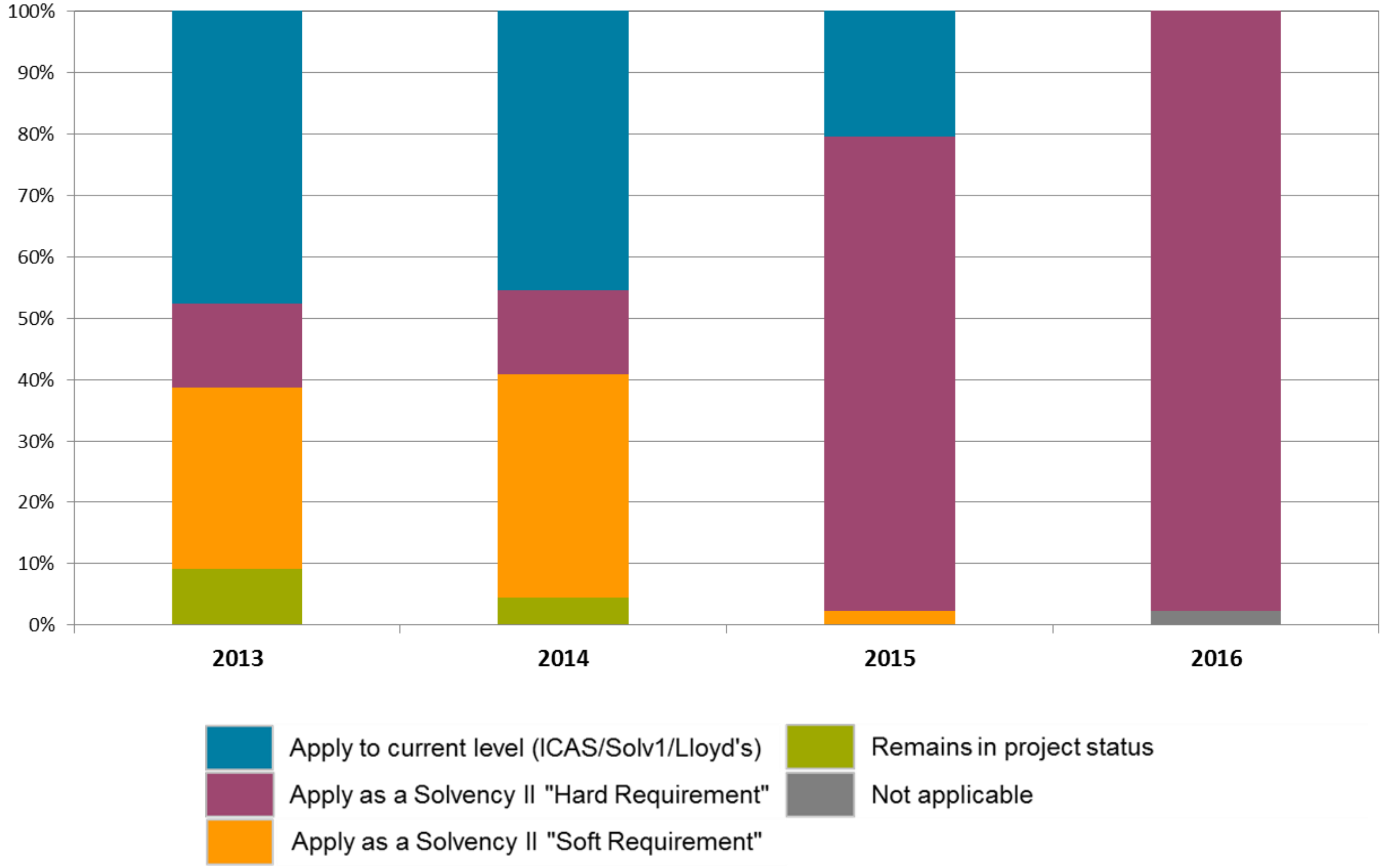
DELAY REQUIRES MODIFIED APPROACH - TO BE IN LINE WITH THE INTERIM MEASURES

- Assume at this stage that Solvency II rules will ultimately apply
- Lack of certainty but plan assuming a 1 Jan 2016 start date
- Options discussed internally as well as with the LMA and PRA
  - “Full Stop” and “Full Steam Ahead” considered and dismissed
- **“Soft Landing”** deemed appropriate approach to take
- Phased implementation - least painful and most efficient
  - avoids full burden of Solvency II compliance in advance of go live
  - does not lose good work already done
- Quantitative requirements apply immediately to support use of Solvency II models
- Qualitative requirements phased in over 2013 to 2016

SOFT LANDING IN 2013 DOES NOT REQUIRE FULL COMPLIANCE WITH ALL TESTS AND STANDARDS

- Agents to continue to run and embed processes as per operating model
- Quantitative submissions using Solvency II internal models to meet ICAS+
- Key supporting qualitative processes live and evidenced:
  - ORSA
  - Model Validation
  - Model Change governance and reporting
  - Documentation controls and updates
  - Actuarial Function Report
- Lloyd's will continue to provide and follow up on feedback
- Maintain compliance with principles <u>AND</u> close gaps to tests and standards
- Board declaration and confirmation of status required in October 2013

PROPOSED PHASED APPROACH TO SII – BY NUMBER OF DRY RUN "SCORING" ELEMENTS



THE UPDATED 2013 TIMETABLE IS NOW LIGHTER THAN PREVIOUS EDITIONS

	JANUARY	FEBRUARY	MARCH	APRIL	MAY	JUNE	JULY	AUGUST	SEPTEMBER	OCTOBER	NOVEMBER	DECEMBER
QUANTITATIVE SUBMISSIONS	TPSF 10 January GQD return		VBAL 7 March SII Balance Sheet @31/12/12 IMSCR 7 March 2013 SCR Re-assessment	TPSF 4 April TPD @ 31/12/12 TPSF 11 April GQD Return		VBAL June LIM Asset Data Dry Run @31/12/12	TPSF 11 July GQD Return IMSCR 4 July * Draft SCR via LCR		VBAL 5 Sept SII Balance Sheet @30/6/13 IMSCR 12/19Sept * (non aligned/aligned) Final SCR via LCR	TPSF 10 October GQD return	VBAL 1 November LIM Asset Data @30/09/13	
QUALITATIVE SUBMISSIONS			GRMU 28 March ORSA Submission	GRMU 19 April Actuarial Function			GRMU 4 July Model Change Report		MVAL 26 Sept * Validation Report	DFA 4 October Board confirmation		
WORKSHOPS/ BRIEFINGS	IMSCR 18 January SCR Briefing DFA 22 & 25 Jan 2013 Planning Workshop	27 & 28 February	GRMU 19 & 20 March Use test Workshop	17 & 18 April Directors Briefing 3 & 4 April	14 & 15 May 23 & 24 May	11 & 12 June	16 & 17 July	6 & 7 August	SREP 17 & 18 Sept Reporting Workshop	GRMU 15 & 16 Oct ORSA/ Model change w'shop	12 & 15 November Directors Briefing 20 & 21	11 & 12 December

KEY: Unassigned workshop

NOTES:

(1) Boxes with a solid fill represent a hard test submission

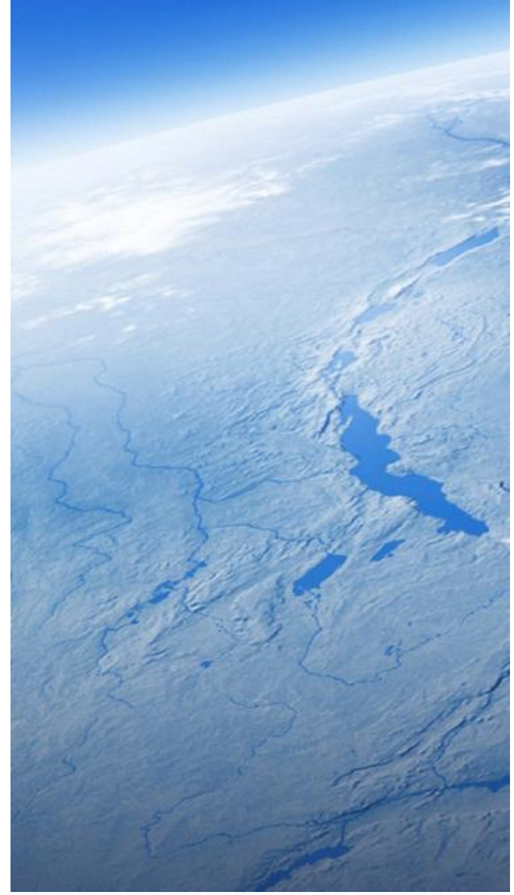
(2) Boxes with a patterned fill represent a soft test submission

(3) A red date signifies a provisional date *(to be comfirmed in Q1)*

SUMMARY AND QUESTIONS

SUMMARY

- Results returned to strong profit
  - despite Hurricane Sandy
  - includes continued trend of reserve releases
    - but leaving reserves in strong position
- Current underwriting - limited growth?
- Capital set using SII approach
  - ultimate SCRs plus SII TPs
  - maintain equivalence to ICAs
- Awaiting developments on SII implementation
  - Lloyd’s proposed soft landing approach
  - to be aligned with Interim Measures



ANY QUESTIONS?

FIDENTIA