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Solvency II: Befriend a risk manager today!

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Agenda

- Basel II: lessons and comparison
- What can risk managers learn from actuaries?
- What can actuaries learn from risk managers?
- Benefits of an integrated team

The Basel II experience

1988	Basel Accord	
2004	Basel II	
2006	CRD	
2007	Transition year	BNP Paribas 'unable to value assets' Run on Northern Rock Major losses emerge at Merrill Lynch & UBS Co-ordinated action by five central banks 'Credit crunch' first used
2008	Fully live	Concern for bond insurers Northern Rock nationalised Bear Sterns acquired by JP Morgan Chase Fannie Mae & Freddie Mac bailed out Lehman Bros files for chapter 11 AIG bailed out, Washington Mutual, Fortis, B&B RBS nationalised
2009	Enhancements to Basel II framework	Enhancements to Basel II framework

The Basel II experience

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The Basel II experience

Some statistics

- 98
- $10.8tn
- £1.5tn
- 94.4%

Lessons from Basel II

- Start early
  - resource competition, last minute expense
- Dedicated project management resource
  - under estimation of change management required
- Involve the Board fully
  - regulatory concerns about governance
- Large expenditure on data capturing (IT systems)
  - data quality issues

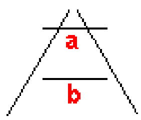
Lessons from Basel II

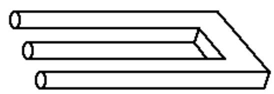
- Keynes' test (roughly right not precisely wrong)
  - over-reliance on model output
- Work on documentation (show me, not tell me)
  - third party unable to reproduce results
- Regulatory preparedness
  - absence of structured approval process

Regulatory response

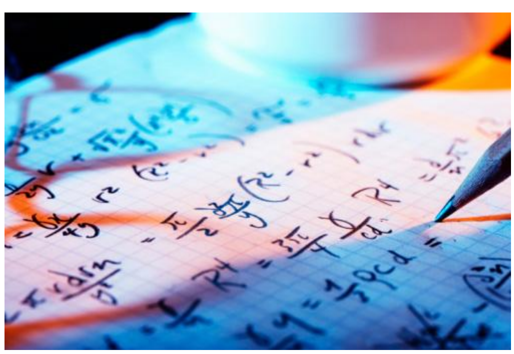
- Start early → communication
- Project management resource → communication
- Board involvement → communication
- Data capturing → internal model approval
- Keynes' test → internal model approval
- Documentation → internal model approval
- Regulatory preparedness → dry run process

Stereotypes & perceptions…





Google - Actuarial…



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Actuary by (stereo) type

- highly numerate
- introvert
- over 45
- communicates with tables and charts
- looks at own shoes when speaking to you

- process orientated
- under age 45
- communicates with diagrams and words
- looks at your shoes when speaking to you

Google - Actuary…

Of all the actuaries at the firm, none could match the zeal of Earnest T. Cromwell.

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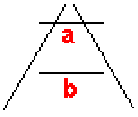
What can risk managers learn from actuaries?

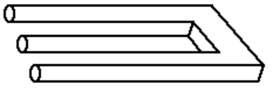
- Quantification of risk
  - risk registers should not be just qualitative
- Understanding the financial dynamics of the business
  - key drivers of risk/return

What can risk managers learn from actuaries?

- Good processes and controls are necessary but not sufficient for good risk management
  - good quality risk MI essential
- Applying a degree of rigour and mathematical analysis to risk problems

Stereotypes & perceptions…





Google - Risk management…

Risk manager by (stereo) type

- process orientated
- over age 45
- communicates with diagrams and words

- highly numerate
- under age 45
- communicates with tables and charts

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Google - Risk manager…

"We've considered every potential risk except the risks of avoiding all risks."

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What can actuaries learn from risk managers?

- Quantification of risk is not everything
  - processes and controls are important
- Communication is key
  - help the Board to understand the risks using a language they know
- Keynes' test
  - avoid over attachment to the models

Benefits of an integrated team

- Utilise the strengths of each discipline
- Create effective communication combining both process and risk quantification