

Life Conference - We Can Work it Out  
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## Who would be a Product Actuary

Top 10 issues and how they fit together

Tuesday 22<sup>nd</sup> November 2011

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## Agenda

- The context
- The issues
- The fit
- The issues revisited
- So who would be a product actuary

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## Context

- Demand drivers - ageing population / savings gap / protection gap
- Economic conditions
- Highly competitive established industry
- Shareholder demands – growth, cost & resource pressure
- Wholesale industry change now occurring

Change brings opportunity

Change brings some huge challenges

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## (Some of) the issues ...

### Regulatory change

- Solvency II
- Retail Distribution Review
- Pension Reform / NEST
- Tax changes
- ECJ gender ruling
- With Profits (CP11/05)
- Product Intervention
- Other distribution: MiFid, PRIPs
- TAS

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## A summary of the issues

What it is

When is it happening?

Does it matter

Implications

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## Solvency II

### What it is

- Wholesale change to the regulatory capital of insurance companies

### When is it happening?

- 2012?
- 2013?
- 2014?
- ....

### Does it matter

- Absolutely!

### Implications

- Wide ranging
  - Capital management
  - Pricing
  - Reporting
  - Analysts view of the company

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## Solvency II Implications (strategic and commercial)

### In principle:

- Another driver for decisions
- Large diversified insurance groups should survive and prosper
- Smaller monoline players may find it increasingly challenging

### But there will be

- A lot of internal change to be able to manage the business in a different environment
- New metrics required for pricing
- Shifts in product offerings and pricing
- Use test needs to be satisfied
- Incentives to divest legacy books / acquire diversifying portfolios

### Which means

- Critical to be at least as good at optimising the capital position as key competitors
- Increased focus on capital optimisation to secure competitive advantage
- Diversification benefits will need to be understood
- New diversification opportunities will be sought
- New reinsurance strategies explored
- Risk and capital profiles of portfolio and plans will need to be understood, along with their sensitivities
- Approval process will change, with a focus on risk adjusted return
- Marketing teams will have to work with new metrics and constraints
- Additional members to the marketing and pricing team

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## Pension Reform

### What it is

- New regulation changing the way that employer sponsored Pension schemes will operate

### When is it happening?

- Starts in October 2012 for the largest employers
- All employers will be included by 2016

### Does it matter

- Yes!
- Impact on every single person in employment

### Implications

- For providers of Corporate Pension schemes a change to:
  - Volume
  - Admin
  - Pricing? Profit? Risk?

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## Pension Reform Impact on scheme value

Value lever	Impact	Net effect on value?
<b>Volume</b> (premium, AUM)	<ul style="list-style-type: none"> <li>• More members of a lower quality, but</li> <li>• Risk of levelling down of existing schemes</li> </ul>	↑
<b>Price</b> (AMC)	<ul style="list-style-type: none"> <li>• Pressure from NEST comparison (NEST charges a 0.3% AMC and a 1.8% of premium charge)</li> </ul>	↓
<b>Persistency</b> (surrender, PUP)	<ul style="list-style-type: none"> <li>• Higher turnover of members</li> <li>• Risk of some existing schemes moving to NEST</li> <li>• Scheme segmentation may improve persistency</li> </ul>	↓
<b>Commission</b>	<ul style="list-style-type: none"> <li>• Initial commission on new members to existing schemes</li> <li>• Lack of clawback on turnover of staff</li> <li>• High capital strain</li> </ul>	↓
<b>Expenses</b>	<ul style="list-style-type: none"> <li>• Economies of scale</li> <li>• High costs of proposition development</li> <li>• Spreading overheads reduces unit costs</li> </ul>	↑

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## Retail Distribution Review

### What it is

- One of the most fundamental changes to the buying and selling of financial products in the UK's history. That's all!

### When is it happening?

- Live from 1<sup>st</sup> January 2013

### Does it matter

- Significant impact for financial advisers
- Consequent impacts on providers

### Implications

- Product design
- Value levers
  - AMCs
  - Persistency
  - Commission
  - Expenses

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## RDR Background

New regulation to increase confidence and trust for customers by:

- Modernising the way advice is paid for
  - Fees or facilitated adviser charging. Indemnified commission banned.
  - Ongoing remuneration can be switched off by the client at any point (on post-RDR policies)
  - Legacy commission banned other than trail
- Greater clarity of advice services being provided
  - Clear description and labelling of services to customers. Advisers are either "Independent", "Restricted" or offering "Simplified Advice"
  - Limitations of advice made clear to customers e.g. only use certain providers or products
- Raising professional standards of all advisers
  - Increase in minimum qualification standards to QCF level 4 (equivalent of 1st year at university)
  - Adherence to consistent professional standards, including a Code of Ethics

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## RDR Implications (strategic and commercial)

Value lever	Impact	Net effect on value?
<b>Volume</b> (premium, AUM)	<ul style="list-style-type: none"> <li>Fewer qualified advisers expected</li> <li>Reduction in headline APE</li> <li>May be more difficult to gain market share</li> <li>Product mix</li> </ul>	↓
<b>Price</b> (AMC)	<ul style="list-style-type: none"> <li>Uncertainty over charging structures</li> <li>Downward pressure on AMC</li> <li>Price to be main factor?</li> </ul>	↓
<b>Persistency</b> (lapse, PUP)	<ul style="list-style-type: none"> <li>Increased churn pre RDR implementation</li> <li>Long term persistency to improve</li> </ul>	↑
<b>Commission</b>	<ul style="list-style-type: none"> <li>No indemnity commission for new schemes</li> <li>Scope for changing or removing commission payable on in force business.</li> </ul>	↑
<b>Expenses</b>	<ul style="list-style-type: none"> <li>Volume impacts</li> <li>Bespoking / value added service provision required</li> </ul>	↓

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## ECJ Gender Ruling

### What it is

- Removal of gender as a rating factor for insurance

### When is it happening?

- 21<sup>st</sup> December 2012

### Does it matter

- Yes – if you write annuity or protection business

### Implications

- Annuity and protection rates will harmonise
- Mix of business risk

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## ECJ Gender Ruling

### Background

- In March 2011 the ECJ ruled that using gender to discriminate for the purposes of insurance business was no longer legal
- It argued that having premiums that differed by gender contradicted the wider European principle of gender equality
- This overturned a previous opt-out to gender equality rules, which allowed gender to be used if it could be statistically supported
- Annuity and protection business will be affected more significantly than other lines of life insurance business

### Implications

- Implementation
- Pricing decision
- Price volatility
- Timing
- Underwriting
- Mix risk
- Retrospective?

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## Tax changes

### What it is

- Life office taxation will change
- Protection in particular will be impacted

### When is it happening?

- 2013

### Does it matter

- It depends!
- XSI / XSE position and products written will dictate its impact

### Implications

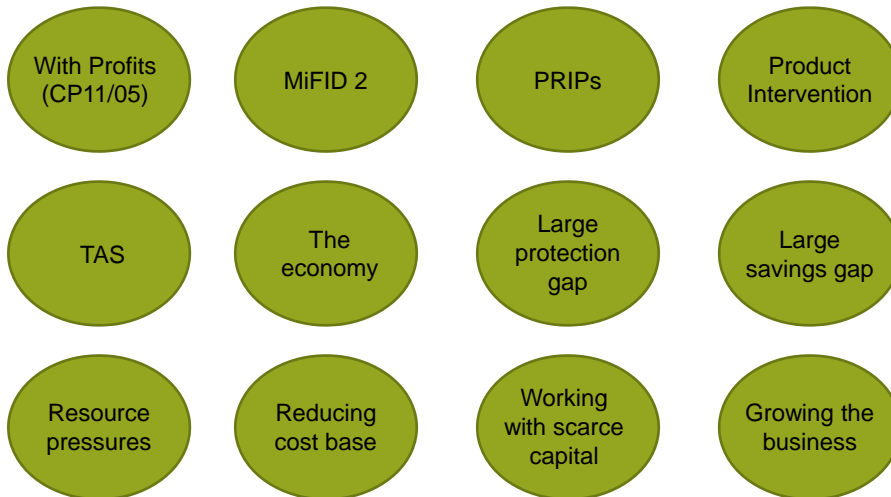
- Price could increase significantly for protection business
- Other lines of business will be affected only to a minor degree

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## And another thing....



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## The Fit?

1. These issues add up to such a fundamental change and are so inter-related that they must be considered together and will collectively radically reshape the industry
2. These are a series of discrete changes which need to be worked through but can be safely ring fenced and dealt with case by case – they will mean change but most of the industry will work in exactly the same way it does now

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- **The fit**
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- So who would be a product actuary

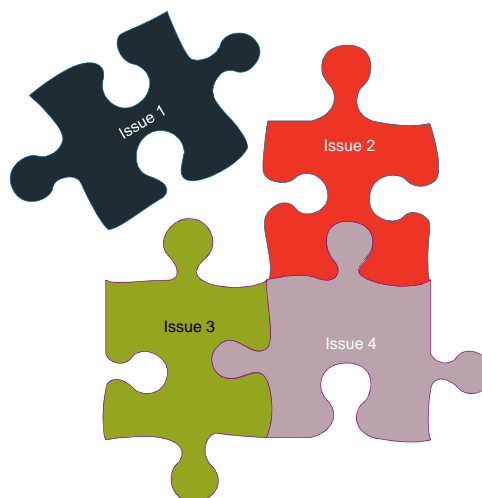
## So how do they fit together ...



## The Fit

### 5 different lenses to be used

1. Time
2. Product
3. Value chain
4. Risks
5. Actuary



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## Fit 1: Time

### Milestones

	2011	2012	2013	2014	2015	2016
SII			▲	▲		
RDR			▲			
Pension reform			▲			
ECJ gender ruling			▲			
Tax changes			▲			
TAS	▲					



It's one thing after another!

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## Fit 1: Time Business Plan

Business Plan		2011	2012	2013	2014
Sales	Channel A				
	Channel B				
	Channel C				
	Total				
Profit	Channel A				
	Channel B				
	Channel C				
	Total				
Capital	Channel A				
	Channel B				
	Channel C				
	Total				

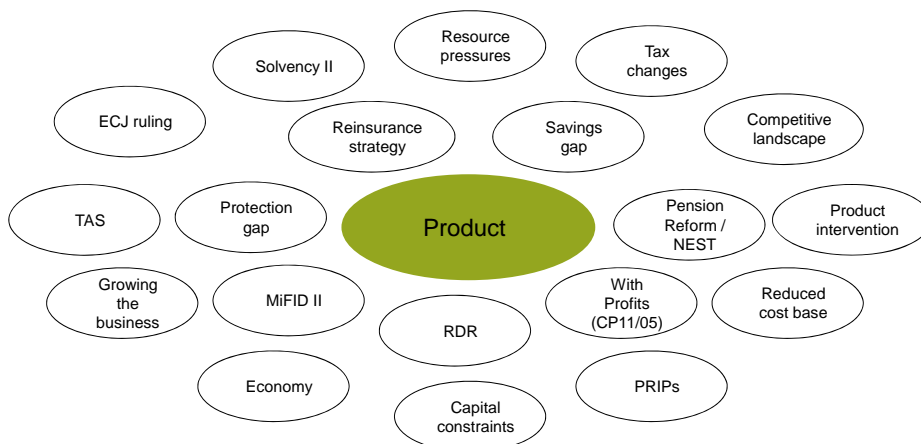


How does my business plan need to change?

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## Fit 2: Product The issues



Everything is centred around the product

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## Fit 2: Product

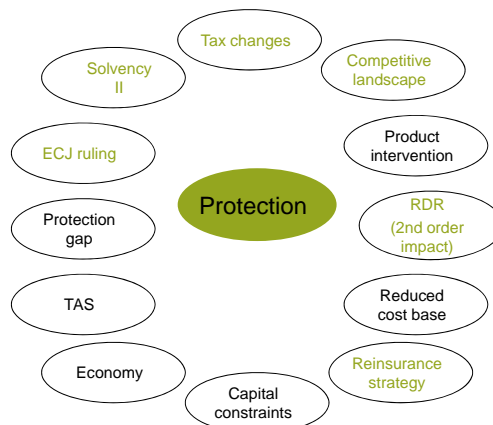
### A look at Protection: Key issues

#### Solvency II

- EPIFP
- Contract boundaries
- Diversification
- Optimal reinsurance strategy
- Gaining competitive advantage

#### ECJ ruling

- Harmonised premiums
- Mix of business risk
- Pricing versus reserving basis, inc Use Test



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## Fit 2: Product

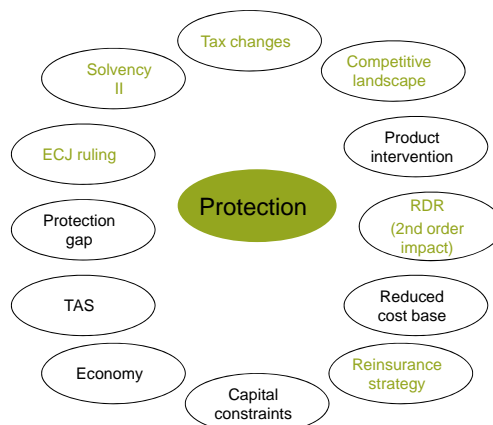
### A look at Protection: More key issues

#### Tax changes

- Premiums increase by 10-15%
- Level playing field for all providers?

#### RDR

- Fewer advisors
- Greater focus on protection?



Protection outlook – net impact?

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### Fit 3: Value

#### The value chain

	Strategy	Product Design	Pricing	NB Acceptance	Capital requirements	Administration	Claims
Solvency II	M	M	M	L	H	L	L
RDR	H	H	H	L	H	M	L
NEST	H	M	M	H	L	M	L
ECJ gender ruling	L	L	H	M	L	L	L
Tax changes	L	L	H	L	L	L	L

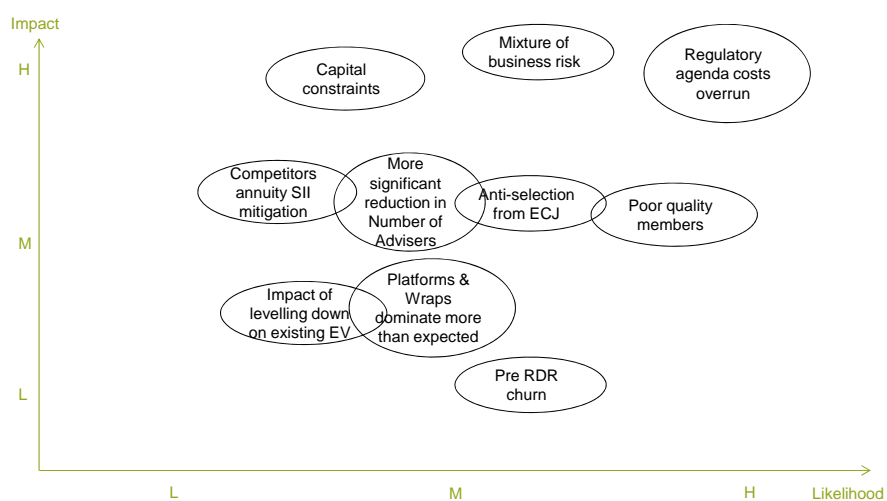
Impacts across the value chain

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### Fit 4: Risks

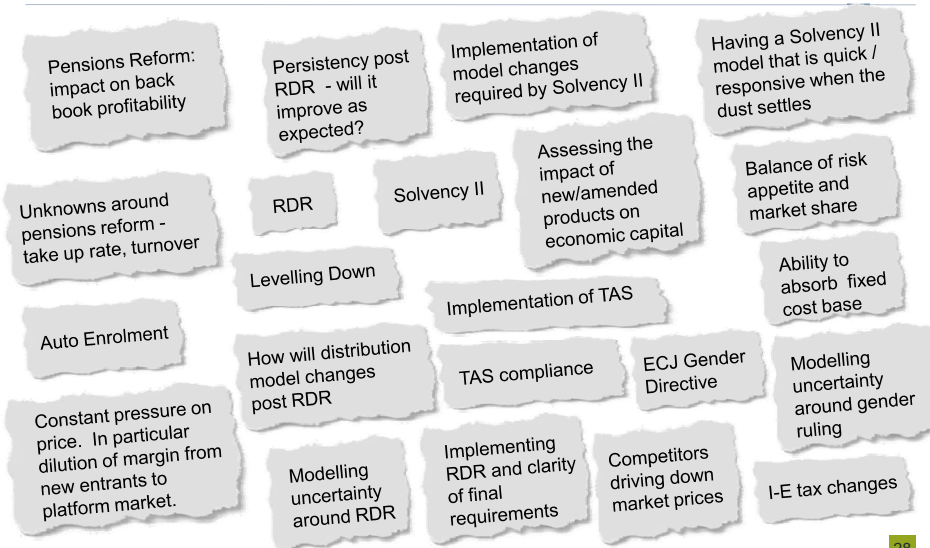
#### The risk map



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## Fit 5: The product actuary's sleepless night



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## Fit 5: The actuary The product actuary role

- Capital manager
- Actively considers diversification
- Actively manages business mix
- Works with new metrics
- Design products that are RDR compliant
- Fewer levers to manage volume
- Resource constrained
- Cost constraints
- Explain how it all works to senior stakeholders!

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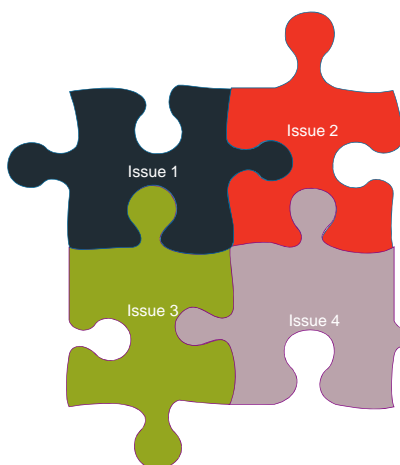
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## And how do they really fit together



- By time
- By product level – due to the significant interlinking of issues
- By impacting on all parts of the value chain
- By changing the risk outlook
- All of which can cause a product actuary sleepless nights

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## So who would be a product actuary ...?



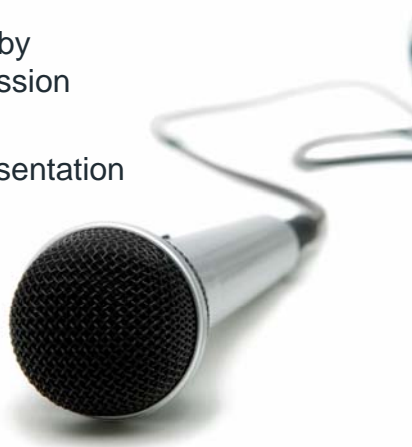
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## Questions or comments?

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