

The Actuarial Profession

making financial sense of the future

GIRO Convention

7-9 October 2009

Edinburgh

Workshop A11 – Lloyd’s Issues

Jerome Kirk

Henry Johnson

Agenda

- First Half Update
- Capital
- Solvency II
- Reserves and Year-end
- Performance Management Data (PMD)
- CSU Benchmark
- Questions

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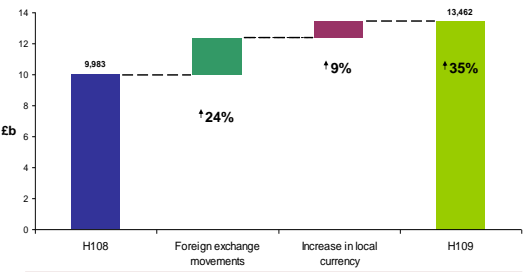
Solid half year results

	6 months to June 2009	6 months to June 2008	12 months to Dec 2008
Gross written premiums	£13,462m	£9,983m	£17,985m
Combined ratio	91.6%	89.0%	91.3%
Investment return	£708m	£346m	£957m
Profit before tax	£1,322m	£949m	£1,899m
Return on capital (annualised)	17.5%	14.7%	13.7%

Source: Lloyd's pro forma financial statements, June 2009

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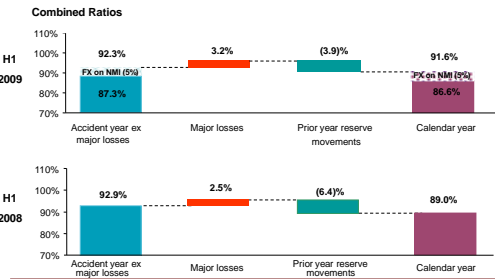
Premium increase driven by currency movements and partly by new business



Note: Attribution to foreign exchange movements and increase in local currency stated on a compound basis
Source: Lloyd's

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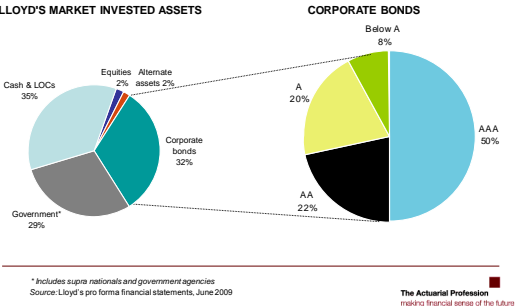
Few natural catastrophes and continued prior year releases



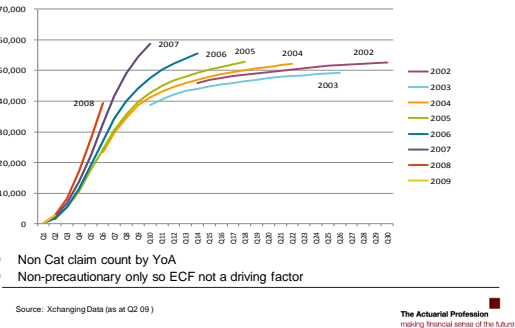
Source: Lloyd's pro forma financial statements, June 2009

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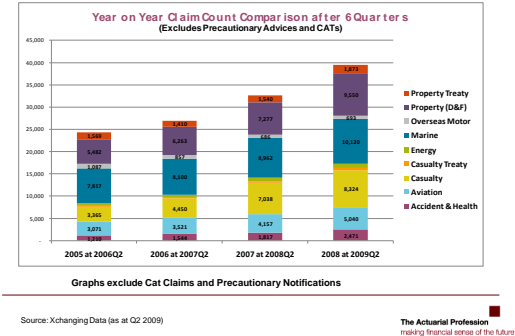
Investments remain geared towards higher security



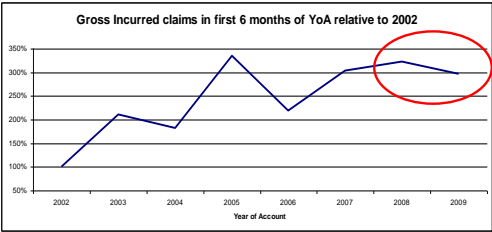
Claim frequencies continue to increase..



...in all classes of business



...but the trend in incurred claim amounts has stabilised

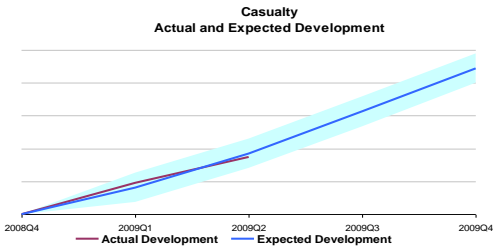


- Current levels are high versus 2002
- Only an indication – not the best predictor

Source: Lloyd's MRRQ database

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Lloyd's Early Warning - Casualty
Actual v Expected for H1 2009

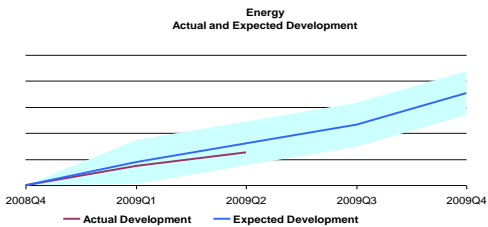


- No issues – appears to be tracking well

Source: Lloyd's Early Warning System

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Lloyd's Early Warning – Energy
Actual v Expected for H1 2009

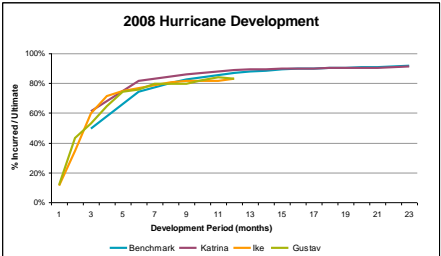


- No issues – appears to be tracking well

Source: Lloyd's Early Warning System

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...and 2008 hurricanes continue to develop within estimates



Source: Lloyd's QMR and Xchanging data

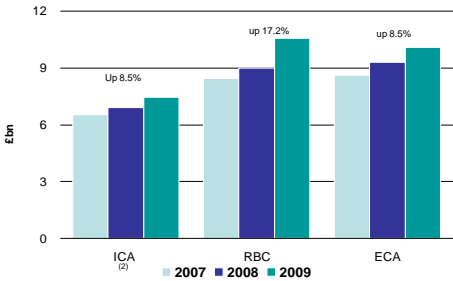
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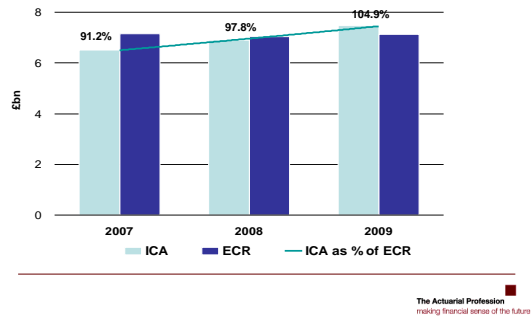
Have seen aggregate capital increase over recent years



(1) All figures based on 1 January for each year of account
(2) Excludes new syndicates for 2007

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Aggregate ICAs higher than ECR in softening market



Key considerations for 2010 ICA review

- Guidance/process substantially unchanged
 - treatment of reserve margins has changed
 - bottom line credit against ECA
 - more in line with FSA approach
- Anticipated review focus
 - catastrophe exposure
 - rate changes & exposure
 - recession / impact on claims environment
 - historical performance against plans
 - discounting / market risk
- New benchmark tool

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Already a long way through 2010 process

Date	Non-Aligned	Aligned
Initial SBF submission	19 June	24 July
Initial ICA pro-forma	10 July	24 July
Full ICA documentation	10 July	28 August
Final SBF	18 September	16 October
Final ICA pro-forma	18 September	16 October

← Now

← Now

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Emerging issues so far

- Catastrophe exposure
 - Rate changes & exposure
 - Recession / impact on claims environment
 - Historical performance against plans
 - Discounting / market risk
- plus
- Sense checking of results and/or over reliance on model outputs

linked to validation under S2

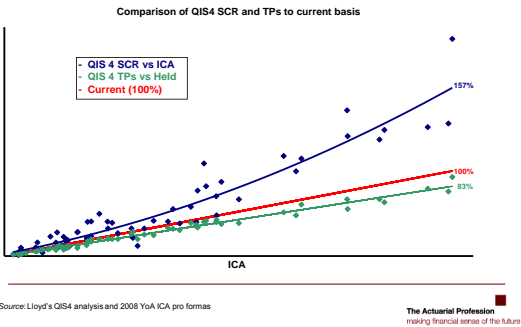
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Solvency II - where is Lloyd's at?

- Application of SII at Lloyd's
 - "Association of Underwriters known as Lloyd's"
 - agreement in principle with FSA on approach
 - will be looking for internal model approval
- Society level
 - programme governance
 - CSU / ERM developments key
 - close liaison with LMA
- Syndicate level
 - guidance / support from centre
 - completed QIS4 / gap analysis
 - Lloyd's account managers

SCR increase depends on size but decrease in TPs does not



Solvency II – what is coming next?

- Consultations / lobbying
 - continue lobbying on level 2 proposals
 - removal of geographical diversification
 - treatment of non-life cat risk
 - prudence
- Society level
 - ongoing CSU / ERM projects
 - develop further guidance
 - gap analyses/implementation plans/technical provisions/QIS5/dry run
 - consider timings and resource implications
- Syndicate level
 - gap analysis feedback → implementation plans

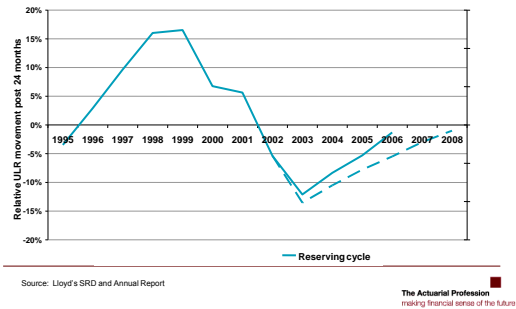
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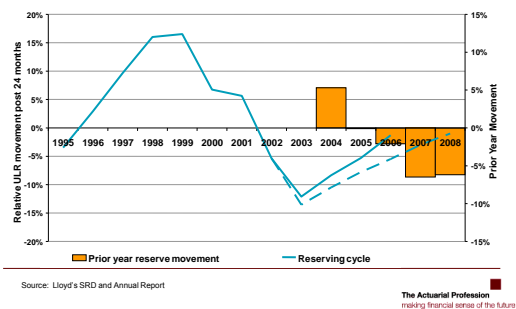
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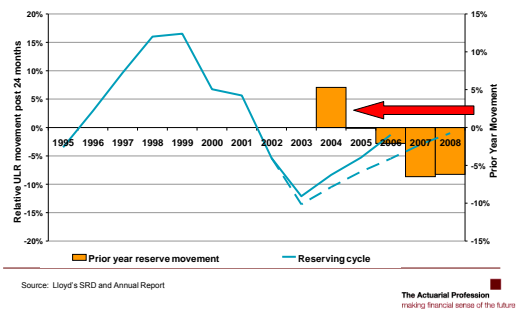
Reserve Cycles and Surplus



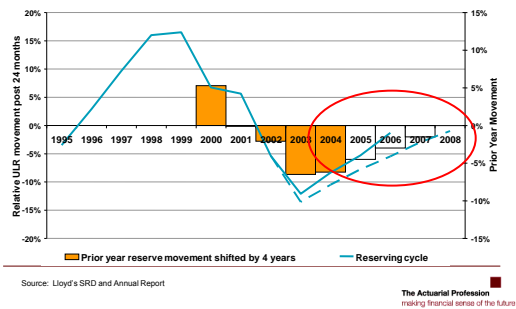
Reserve Cycles and Surplus



Reserve Cycles and Surplus



Reserve Cycles and Surplus



Reserve Cycles and Surplus

- Reserve cycle
 - 2008 year of account "on the line"
 - casualty reserve cycle is more severe
 - may have already crossed the line
 - **need to consider implications for pricing**
- Lloyd's estimate reserves surplus exists
 - but is diminishing
 - expect reducing prior year surplus over coming years
- Look forward 2-3 years
- Lloyd's will actively review and investigate areas of reserving concerns

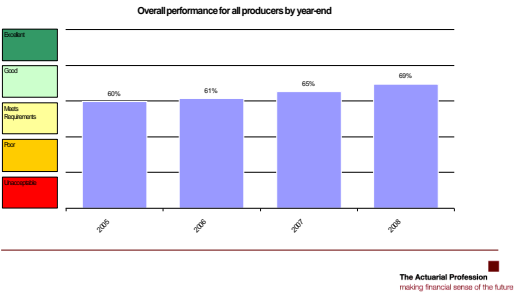
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Year-end 2009

- Valuation of Liabilities rules issued 30 September 2009
 - additions to incorporate GN20/33
 - changes relating to winding up of LATF
 - discounting only on basis consistent with GENPRU 2.2.107 (2) R
- Dates for submission of SAOs and reports equivalent to last year
- Reports comply with GN12 not TAS R this year-end
- Will hold signing actuaries forum in December
 - open to actuaries from managing agents
 - ideas for discussion topics welcome

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SAO report quality continues to improve
- something to be proud of



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Performance Management Data

- Collect robust and accurate risk level information
 - link to use test for underwriting information under Solvency II
- Monitor the performance of syndicates relative to their business plans
 - information to take decisive action where there are prudential concerns
- Enhance the performance framework that has been in place since 2003
- Reduce the risk of a call on the central fund
 - which in turn adds protection to policyholders

More information on <http://www.lloyds.com/PMD>



PMD project successfully delivered

- Project successfully delivered ahead of schedule
 - First returns received 15 April 2009
- PMD provides more information on
 - Geographical split, broker information, distribution channels, line sizes
- First Management Information (MI) Packs played back to the market in August
 - Current focus is to improve data quality and to provide more guidance to the market

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PMD Rate Changes

- Syndicates report on premium changes for all renewal business written at Lloyd's
- Information is reported to Lloyd's on a policy level

170	180	190	200	210	220
Expiring 100% Prem	Deductible Change	Breadth of Cover Change	Other Change	Pure Rate Change	Current 100% Prem

Look at some worked examples

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Key principles

- All values captured in PMD are in monetary amounts
- Changes due to deductible, and due to breadth of cover are on expiring terms
- Changes due to breadth of cover focus on changes on the coverage for perils.
- Changes in deductible and changes in breadth of cover have to be treated independently
- When changes of exposure of the same kind are added (e.g. changes in the indemnity size) these have to be priced on last year's pricing basis adjusted for this year's changes in policy terms

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PMD – Example 1

- Expiring Terms - 1 hotel, Fire and flood cover @ £100 per hotel
- Change of Terms – None
- Current Terms - Same 1 hotel, Fire and flood cover @ £105
- Risk Adjusted Rate change = 5%

170	180	190	200	210	220
Expiring 100% Prem	Deductible Change	Breadth of Cover Change	Other Change	Pure Rate Change	Current 100% Prem
100	+0	+0	+0	+5	+105

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PMD – Example 2

- Expiring Terms - 1 hotel, Fire and flood cover @ £100 per hotel
- Change of Terms – Flood cover change of -£40, deductible change of +£50 on expiring terms
- Current Terms - Same 1 hotel, Fire cover only and adjusted deductible @ £90 per hotel
- Risk adjusted rate change equals X%

170	180	190	200	210	220
Expiring 100% Prem	Deductible Change	Breadth of Cover Change	Other Change	Pure Rate Change	Current 100% Prem
100		Completed during talk			+90

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PMD – Example 3

- Expiring Terms - 2 hotels, Fire and flood cover @ £100 per hotel
- Change of Terms – 1 new hotel added. Deductible change worth +£95 per hotel, Fire cover removed worth -£90 per hotel (on expiring risk).
- Current Terms - 3 hotels, modified flood cover @ £80 per hotel
- Risk adjusted rate change equals Y%

170	180	190	200	210	220
Expiring 100% Prem	Deductible Change	Breadth of Cover Change	Other Change	Pure Rate Change	Current 100% Prem
200		Completed during talk			240

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PMD – Example 4

- Expiring Terms - One ship, sum insured £10m, rate 2%
- Change of Terms – One ship added with sum insured £12m. Piracy cover added @ rate 0.08%.
- Current Terms - Two ships, sum insured £22m, rate 2.1%
- Risk adjusted rate change equals Z%

170	180	190	200	210	220
Expiring 100% Prem	Deductible Change	Breadth of Cover Change	Other Change	Pure Rate Change	Current 100% Prem
200,000		Completed during talk			462,000

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The new CSU Benchmark system is now in use in the 2010 ICA review

- Based on the Capital System Upgrade (CSU) platform
- Replaces RBC as a benchmark
- System works like a typical ICA stochastic model
 - allows reviewer to drill down into the calculation to look for differences
 - simulation based
- Insurance risk is core element
 - but results are presented for total including all risk types
- ICA (not ECA) level – i.e. pre economic uplift

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Other risk types are incorporated

- Other risk types and diversification have been included by means of a market average loading
 - alternative approaches would be syndicate specific
- Separate benchmark for market risk
 - differentials between syndicates
 - not used in overall benchmark, only reviews
- Overall figures are directly comparable to total ICA as presented
 - will look at "insurance risk only" as well

Drill down is possible

- The insurance risk component can be shown in underwriting and reserving components
 - pre and post diversification
- A range of drill down is available including:
 - 2010 underwriting profit
 - year end net reserves
 - 1:200 ULR
 - 1:200 reserve deterioration
 - probability of breakeven
- Assumptions (e.g. ULRs) can be flexed away from market average benchmarks

CSU benchmark - next steps

- Actively use in ICAs
- Continue to refine
 - only first iteration
 - but now a working model
- Present / discuss workings with CALM
 - make an outline technical specification available
- Fully replace RBC as benchmark

Summary

- First Half Update
 - strong results / claim frequencies up but not amounts
- Capital
 - similar ICA process / few changes / as expected
- Solvency II
 - great progress / focus turns to dry run & implementation plans
- Reserves and Year-end
 - reserve cycle turned / reducing reserves surplus / year-end 2009 process similar to 2008
- Performance Management Data (PMD)
 - live project / feedback to agents / focus on data
- CSU Benchmark
 - in use / working model now / will replace RBC

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Questions



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