

Current Issues in General Insurance
Jerome Kirk – Lloyd's

Lloyd's Update

12 May 2011

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Agenda

- **Year-end 2010**
 - Results
 - Findings
- **2011 to date**
- **2012 Capital Setting**
- **Quick Solvency II update**
 - Dry run
 - Lobbying
- **Summary & Questions**



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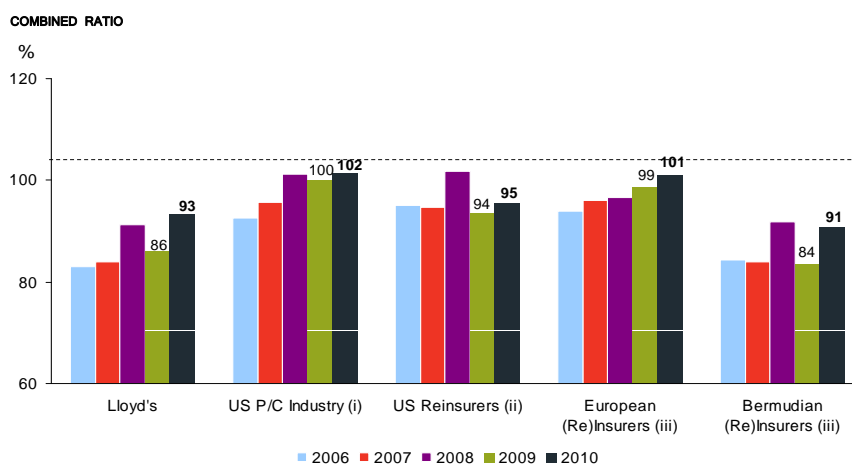
2010 saw solid result in challenging circumstances...

£m	2009	2010
Gross written premiums	21,973	22,592
Combined ratio	86.1%	93.3%
Investment return	1,769	1,258
Profit before tax	3,868	2,195
Return on capital (pre-tax)	23.9%	12.1%

Source: Lloyd's pro forma financial statements, 31 Dec 2010

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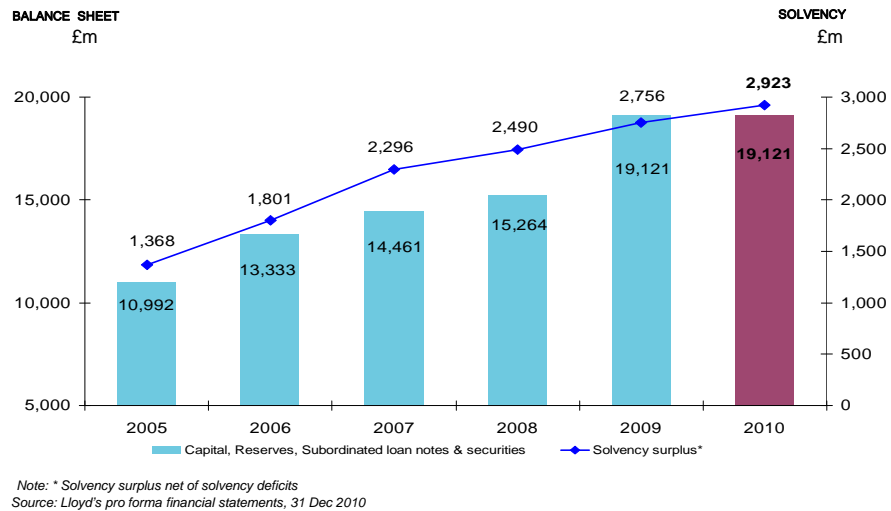
...and our performance compares well against our peers



Sources i) Insurance Information Institute (estimate-2010), ii) Reinsurance Association of America, iii) Company data (8 European companies; 17 Bermudian companies)

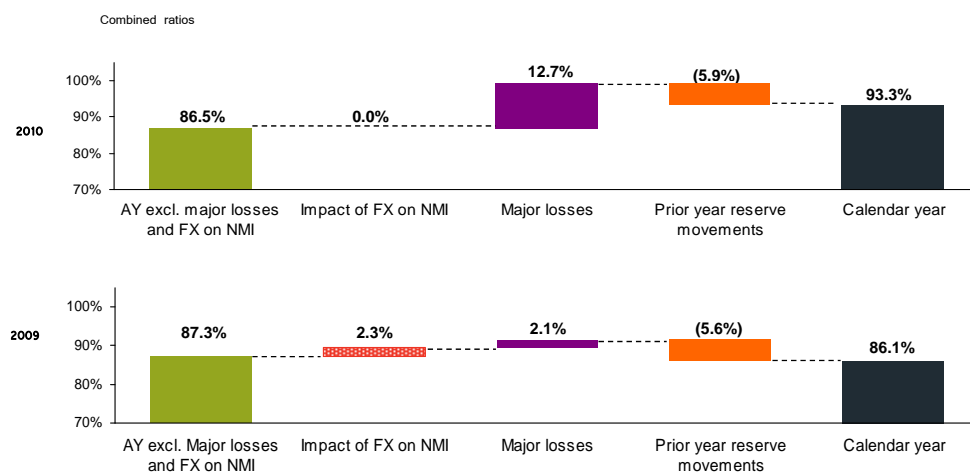
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Solvency coverage is now at record levels



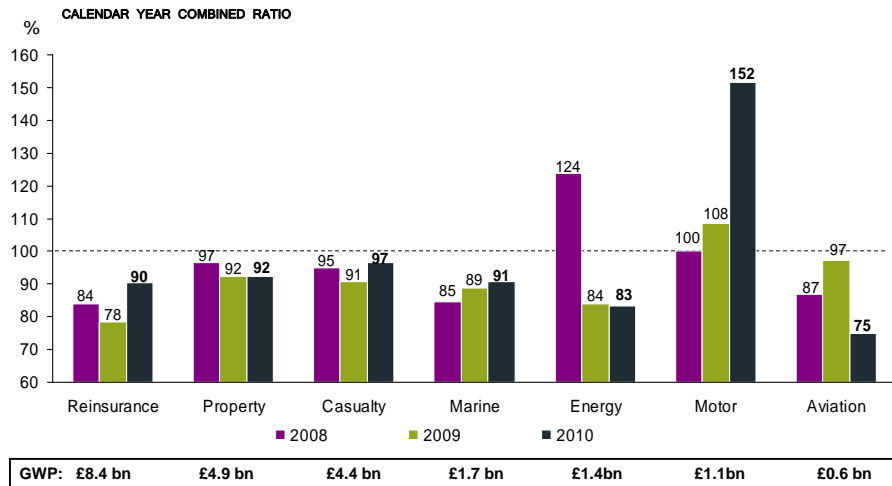
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The full year underwriting remains in profit despite significant catastrophe losses...



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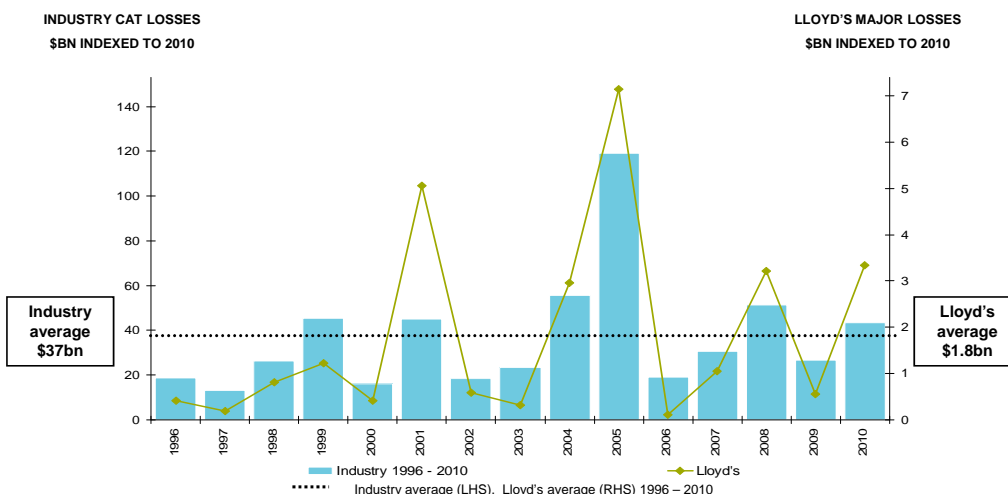
...with resilient profits in major classes but UK motor did face a hostile claims environment



Source: Lloyd's pro forma financial statements, 31 Dec 2010; GWP: Gross Written Premium

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2010 saw insured industry cat losses of \$43bn

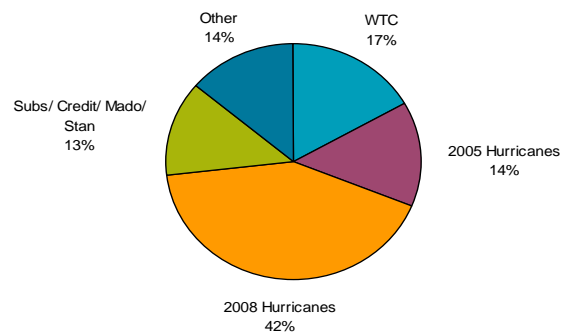


Source: Industry - Swiss Re, Sigma No 1/2011; Lloyd's - Net ultimate claims for major losses per syndicate QMRs, Source: Lloyd's pro forma financial statements, 31 Dec 2010

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The 2009 SAO Large Loss Wordings were dominated by a small number of losses....

- Year-end 2009 saw:
 - only 1 “high” severity wording
 - 2008 windstorms were the largest by number (42%)

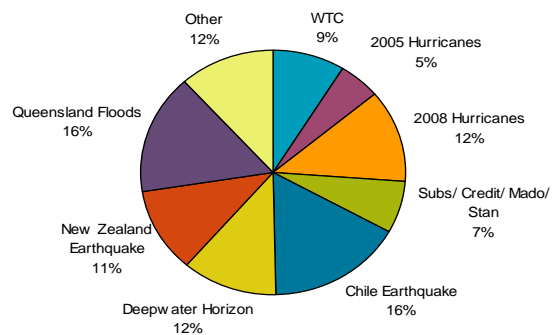


Source: Lloyd's 2009 SAO analysis

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...but year-end 2010 has seen a different picture

- Year-end 2010 saw:
 - 3 “high” severity wordings
 - Wordings relating to a number of new losses – as expected



Source: Lloyd's 2010 SAO analysis

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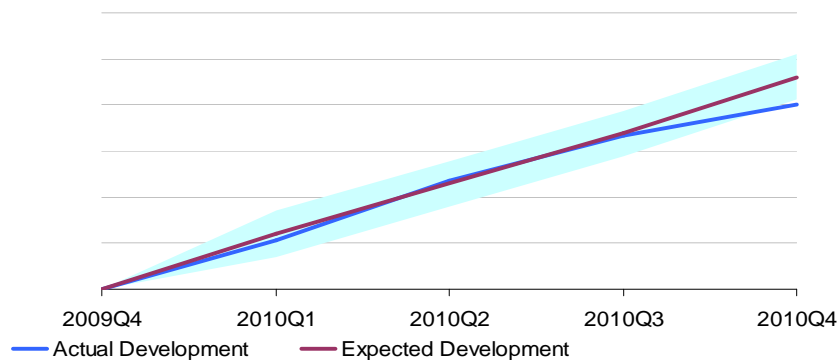
The results are bolstered by further reserve releases

- Fourth year in a row of significant reserve releases
- Releases have been seen over
 - most “back” years of account...
 - ...but with more pressure on more recent years
 - and most classes
 - especially property and reinsurance
- Surpluses have been generated by favourable experience
 - Consistent with Lloyd’s “Early Warning” results....

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The 2010 experience on back years was, in general, favourable....

Actual and Expected Development
Whole Account - Claims

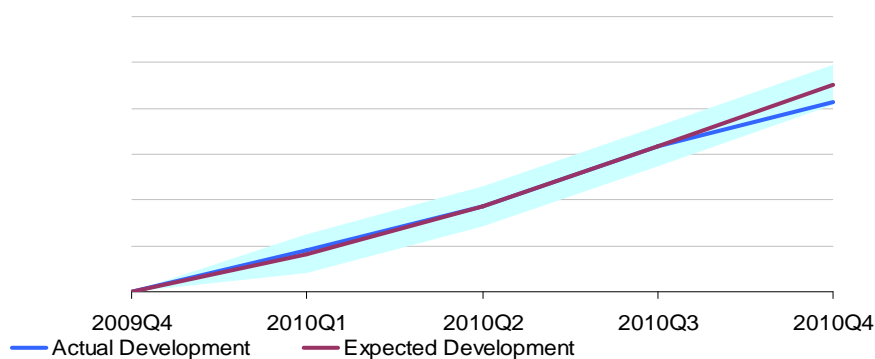


Source: MRC Early Warning exercise. MRC projections vs MRRQ incurred data converted at y/e 2009 exchange rates. Figures are gross of reinsurance

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....with casualty following a similar pattern to the whole account....

**Actual and Expected Development
Casualty Account - Claims**

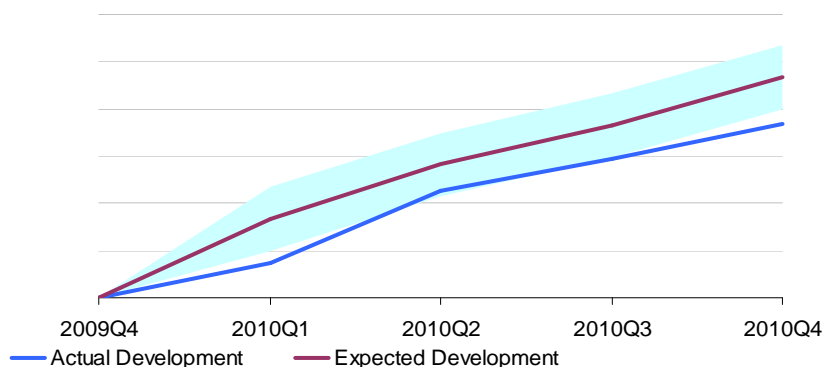


Source: MRC Early Warning exercise. MRC projections vs MRRQ incurred data converted at y/e 2009 exchange rates. Figures are gross of reinsurance

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...and property treaty was constantly lower than expected

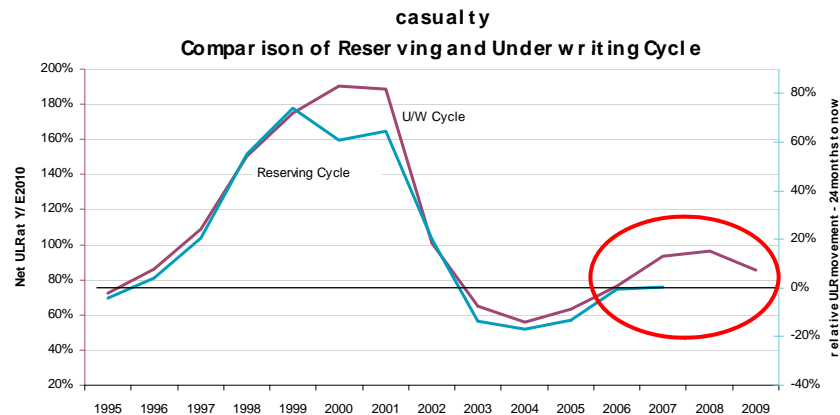
**Actual and Expected Development
Property Treaty Account - Claims**



Source: MRC Early Warning exercise. MRC projections vs MRRQ incurred data converted at y/e 2009 exchange rates. Figures are gross of reinsurance

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During 2010 Lloyd's maintained the focus on reserving cycles.....



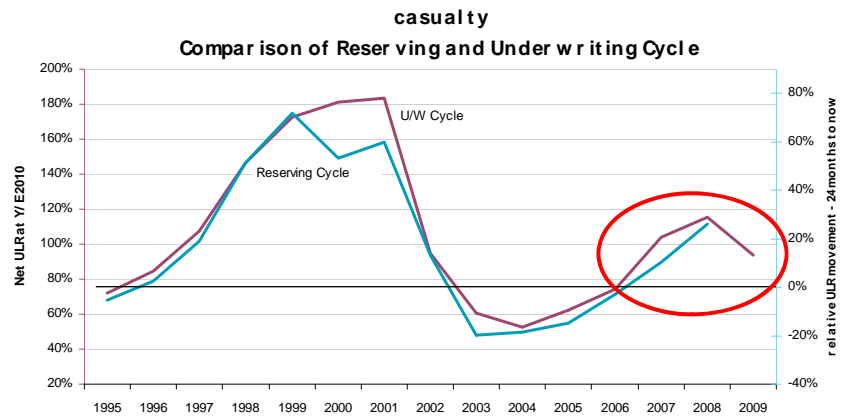
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...including writing to CFOs on Reserving in Dec 2010

- Looking to Managing Agents to ensure standards of governance are met
 - includes telling Boards that Lloyd's level of concern exists
 - Signing Actuaries must also play a part
- Further benchmarking analysis extends central best estimate from market total to syndicate
 - allocations of market level best estimate by 50 class line of business – not allocating a deliberately conservative number
- Portfolios differ, but needs an explanation that goes beyond just saying “portfolio differs”
- Expecting CFOs to discuss with Boards
- FSA wrote a similar letter to CEOs in March 2011

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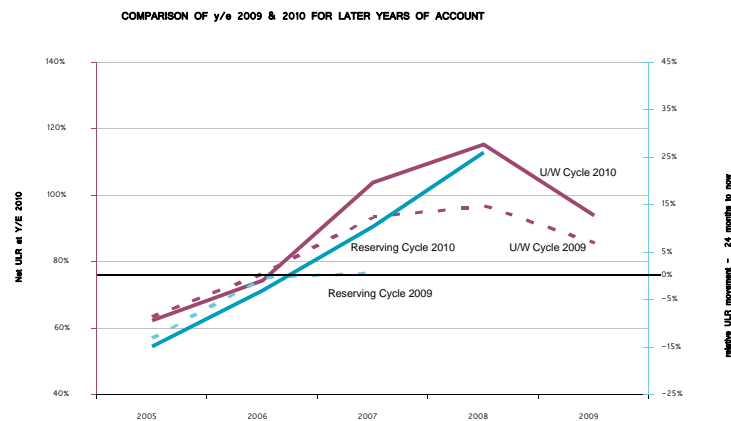
Casualty has seen a significant movement – a positive response to Lloyd's concerns?



Source: Lloyd's provisional 2010 SRD database

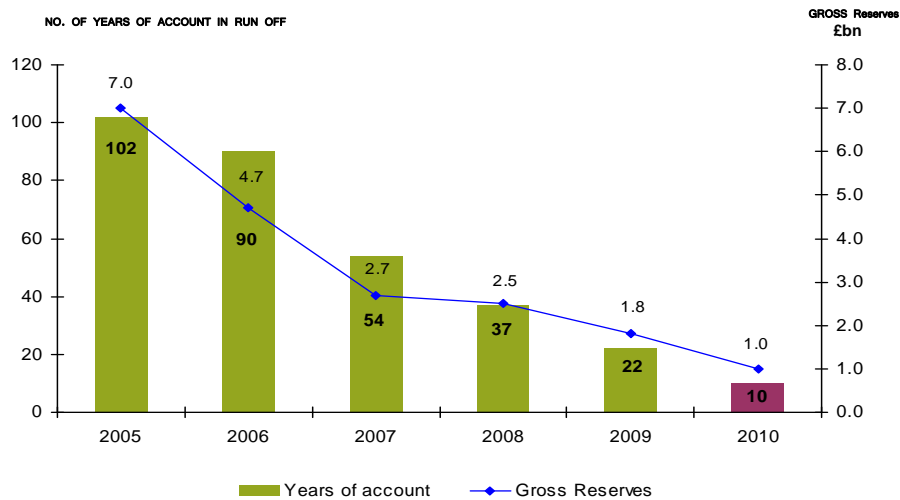
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The movement is marked when only focussing on the later years of account



Source: Lloyd's provisional 2010 SRD database

Finish the results section with the good news that the level of Open Years continue to decline



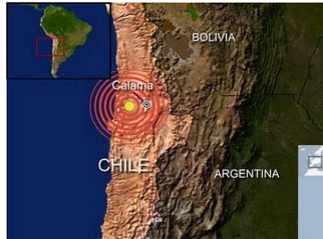
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But not a great start to 2010....



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But not a great start to 2011.....



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....already been several significant Catastrophes

- There are already estimates of industry losses
 - with many insurers publishing own impact
- Lloyd's issued a Major Loss Return on 14th March
 - return received on 20th April
 - trade off between speed of reporting and accuracy
 - return now received and results are being analysed
- There will be an impact on the profit release process
- Will be issuing a statement soon with estimated loss amounts...
 - uncertainty will remain in estimates
 - and even more SAO large loss wordings?

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And what about the rest of 2011?

“Based on current and projected climate signals, Atlantic basin and US landfalling tropical cyclone activity are forecast to be about 25% above the 1950-2010 norm in 2011. There is a moderate (55%) likelihood that activity will be in the top one-third of years historically.”

TSR April Update

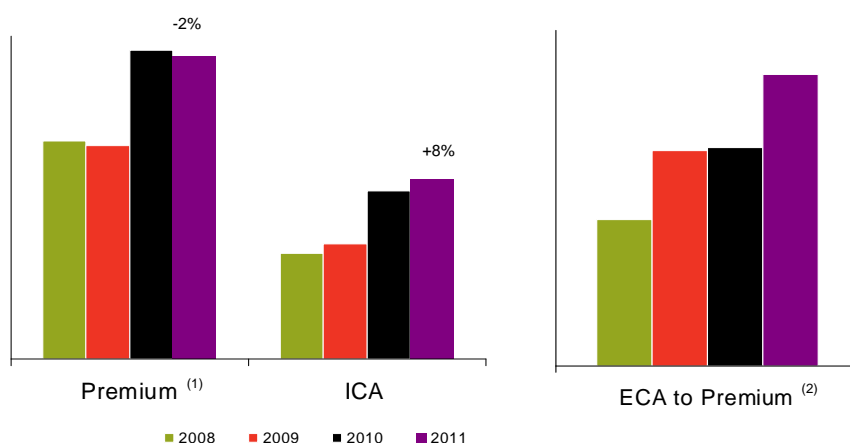
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2011 YoA saw capital moving in line with changes in market conditions



⁽¹⁾ Gross premium, net of acquisition costs

⁽²⁾ Excludes reserve margin credit

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2012 will once again see a streamlined ICA process

Approach

- Similar streamlined approach as seen for 2011 capital setting
 - intended to free up market resources for Solvency II dry run
 - no full ICA documentation required
- Heavily dependent on Lloyd's ICP benchmark movement
 - worked well for 2011
- Tier 1 syndicates (ICA < £125m)
 - full pro-forma unless electing benchmark
- Tier 2 syndicates (ICA > £125m)
 - full pro-forma
 - analysis of change (in September)
 - more detail for “big” syndicates

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With no change in underlying basis...

- 2010 ICA guidance still holds
- 35% uplift remains
- Treatment of reserve margins
 - discretionary 75% maximum credit
 - reliance on both SAO and Lloyd's reserve reviews
- Statutory requirement to keep ICA under continuous review remains
- Reminder that the pro-forma information is key to process
 - ensure it makes sense
 - last year time was lost by both market and Lloyd's due to issues here

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...and with the following timetable

Date	Non-Aligned	Aligned
Initial ICA	8 July	8 July*
Final SBF	9 September	9 September
Final ICA	9 September	9 September
Coming into Line	28 November	28 November

- * may be based on rollover of 2011 or initial 2012 plan if submitted
- Tier 1 syndicates have option to elect the benchmark movement at times during process

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2011 is based on 7 “new” workstreams...

2010 Dry run	2011 Workstream
<i>New for 2011</i>	Internal Model SCR
<i>QIS5 and new for 2011</i>	Valuation & Balance Sheet
TP and QIS5	Technical Provisions & Standard Formula
SQS, CVP & EMD	Model Validation
SOG, MSG & ORSA	Governance, Risk Management & Use
SREP	Reporting & Disclosure
<i>DOC and new for 2011</i>	Documentation & Final Application

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...with three key deliverables

- Article 101 – the model must be able to calculate a Solvency Capital Requirement (SCR)
 - **Action – deliver SCR by October 2011**
- Article 112(5) – there are adequate systems in place for identifying, measuring, managing and reporting risk
 - **Action – deliver ORSA by 16 December 2011**
- Articles 120-126 – the model meets the tests and standards on use, statistical quality, profit & loss attribution, calibration, validation, documentation and external models & data
 - **Action – evidence that standards are being met throughout process and deliver ‘application pack’ by 16 December 2011**

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With guidance and support from Lloyd's

Workshop timetable							
Dates	Workstream	Format	Topic	Dates	Workstream	Format	Topic
07 Feb 2011 11 Feb 2011	ALL	Briefing / Workshops	2011 Planning Workshops	08 Aug 2011 09 Aug 2011	Technical Provisions & Standard Formula	Debrief: Introduce	Technical Provisions I (Year End) TPs II (Half Year & Projected)
01 Mar 2011 03 Mar 2011	Governance, Risk Management & Use	Introduce:	Governance & Use		Internal Model SCR	Debrief:	Model Walkthroughs Insurance Risks & Other Risks
15 Mar 2011 16 Mar 2011	Model Validation	Introduce:	Core Validation I	23 Aug 2011 24 Aug 2011	Governance, Risk Management & Use	Debrief: Introduce:	Governance & Use; Risk Process & Use I Risk Process & Use II
04 Apr 2011 06 Apr 2011	Technical Provisions & Standard Formula	Introduce:	Technical Provisions I (Year End)	01 Sep 2011 02 Sep 2011	Model Validation	Follow up: Debrief:	Core Validation I Core Validation II
	Internal Model SCR	Debrief: Introduce:	Model Questionnaire Insurance Risks & Other Risks	14 Sep 2011 15 Sep 2011	Valuation & Balance Sheet Reporting & Disclosure	Debrief: Introduce:	Valuation Methodology Reporting Framework Reporting Systems
09 May 2011 10 May 2011	Model Validation	Introduce:	Core Validation II				
17 May 2011 18 May 2011	Governance, Risk Management & Use	Introduce:	Risk Process & Use I	03 Oct 2011 04 Oct 2011	Governance, Risk Management & Use Documentation & Final Application	Introduce: Debrief: Follow up:	ORSA Documentation Process Final Application Process
13 Jun 2011 17 Jun 2011	Technical Provisions & Standard Formula	Introduce:	Standard Formula (QIS6 or QIS5)	19 Oct 2011 20 Oct 2011	Free session		
	Internal Model SCR	Introduce:	Consolidation & Comparative Analysis	07 Nov 2011 10 Nov 2011	Governance, Risk Management & Use	Debrief: Follow up:	Risk Process & Use II ORSA
22 Jun 2011 23 Jun 2011	Valuation & Balance Sheet Reporting & Disclosure	Introduce:	Valuation Methodology Reporting Framework	23 Nov 2011 24 Nov 2011	Free session		
04 Jul 2011 05 Jul 2011	Model Validation	Debrief: Introduce:	Core Validation I Validation Policies & Criteria	05 Dec 2011 08 Dec 2011	Free session		
19 Jul 2011 20 Jul 2011	Documentation & Final Application	Introduce:	Documentation Process Final Application Process	15 Dec 2011 16 Dec 2011	Free session		

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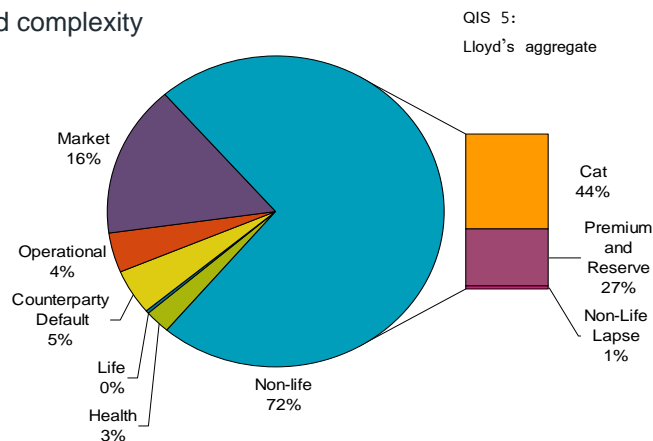
SAOs under Solvency II

- Solvency II introduces the concept of an Actuarial Function
- Syndicates (or Managing Agents) will require an Actuarial Function
- Duties of Actuarial Function are **close to** providing an opinion on Technical Provisions for Solvency
- Current SAOs provide an opinion of Technical Provisions for Solvency
 - but is relied upon by auditors for accounts...
 - ...given the similarity between financial reporting and solvency bases
- However not the same similarity under Solvency II
- What does this mean for the provision of SAOs?
 - many possible solutions
- Currently considering options and are consulting with stakeholders

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QIS5 results - “too big and unbalanced”

- The results have led to lobbying activities that aim
 - to focus on large issues
 - to avoid complexity



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Non-Life Cat Risk – recognition of geographical diversification

- Geographic diversification (GD) of risks is an important feature for any insurer writing in multiple regions
 - e.g. no reason to expect event in Central Asia given one in Western US
 - GD in premium/reserve risk – just as important for cat risks
- Proposal through reinstated European NL Cat Task Force:
 - recognition of diversification across 18 regions, by peril
 - independence for some perils/regions, small link for others
- Rather than SCR calculated using sum of premiums across all regions, SCR for a peril would become:

$$SCR_{peril\ i} := \sqrt{\sum_{a,b} Correlation_{region\ a, region\ b} SCR_{i,a} SCR_{i,b}}$$

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Market Risk

– introduction of matching for capital

- QIS5 calculates currency risk charge based on difference between total assets and total liabilities in each currency (non-domestic/EUR)
 - liabilities are pure obligations only – no allowance for capital requirement
- Where solo insurers hold excess assets (i.e. capital buffer) in a currency, standard formula penalises severely
 - effectively introduces an incentive to poorly match currency
- Lloyd's proposal for solo entities taken into a CEA proposal
 - consider proportion of assets and liabilities in particular currencies
 - only charge based on extent to which these proportions are mis-matched
 - makes allowance for holding excess capital in the currency of obligations

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Summary

Year-end 2010 Results

- Strong results with catastrophe losses offset by continued reserve releases

2011

- Already seen significant catastrophe losses
- Focus will remain on reserving
- 2012 capital will be set on a streamlined basis again

Solvency II

- Key priority for 2011 with dry run in full swing
- Continue to lobby including technical items in standard formula

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Questions or comments?



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