The Impact of the Current Financial Crisis on the Run-off Market
Karen Newbury & Steve Goodlud
KPMG LLP (UK)

Agenda

- Introduction and scene setting
- Discussion
  - What are the key issues for the run-off market arising from the financial crisis?
  - What is the impact of the financial crisis on run-off strategy?
UK non-life run-off market

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<tbody>
<tr>
<td>Lloyd’s (1993 onwards)</td>
<td>7.2</td>
<td>7.5</td>
<td>5.2</td>
<td>2.9</td>
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<tr>
<td>Equitas (Lloyd’s 1992 &amp; prior)</td>
<td>4.6</td>
<td>4.5</td>
<td>4.8</td>
<td>4.4</td>
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<tr>
<td>Other solvent run-off</td>
<td>15.6</td>
<td>16.4</td>
<td>9.5</td>
<td>9.1</td>
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<tr>
<td>Total</td>
<td>30.4</td>
<td>32.1</td>
<td>20.7</td>
<td>16.8</td>
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<tr>
<td>Run-off share of technical provisions</td>
<td>11.8%</td>
<td>10.9%</td>
<td>10.3%</td>
<td>10.1%</td>
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<tr>
<td>Total run-off market</td>
<td>42.2</td>
<td>43.0</td>
<td>31.0</td>
<td>27.0</td>
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<td>US$ : UK£ exchange rate</td>
<td>1.584</td>
<td>1.775</td>
<td>1.943</td>
<td>1.964</td>
<td>1.949</td>
</tr>
<tr>
<td>US Federal Funds rate</td>
<td>2.00%</td>
<td>4.50%</td>
<td>5.125%</td>
<td>5.125%</td>
<td>2.00%</td>
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| Source: AM Best 2009, KPMG LLP (UK) 2009, Lloyd’s 2009

Equitas – A run-off case study

![Equitas run-off case study chart]

Objectives for run-off management

- There are a number of objectives for run-off portfolio management:
  - Maximise return to shareholders
  - Achieve finality to the business
  - Timetable
- These objectives may have different priorities for each stakeholder.
Run-off strategy (1)

- There are six conventional strategies to achieve finality to discontinued business for the risk carrier:
  - Ordinary course run-off to expiry.
  - Accelerated run-off through commutation.
  - Reinsurance (loss portfolio transfer) bringing economic finality to the risk carrier, subject to credit risk. Run-off continues under the control of the reinsurer.

Run-off strategy (2)

- Part VII transfer. Run-off continues under the control of the transferee.
- Sale of the company. Run-off continues under the control of the acquirer.
- Scheme of arrangement.
- One further decision is whether to outsource the run-off to a service provider.

Finality transactions
Run-off mergers and acquisitions

Discussion

Key issues arising from financial crisis

- Investment write downs and investment income
- Liquidity and finance
- Resources and costs
- Liabilities
  - Discontinued financial guaranty business
Impact on run-off strategy

- Pressure for liquidity
  - Greater number of commutations
  - Discount rates
- Use of restructuring mechanisms to assist in access to capital
- Only the largest players may have the ability to absorb the short term losses in pursuit of longer term gains
- Greater scrutiny by regulators: capital and Solvency II