The Regulatory Agenda: Pricing & Underwriting

Jenny Xu and Nick Silk

01 October 2019
Agenda

• PRA’s Financial Risk Frameworks

• Insights from recent reviews: personal, commercial and corporate sectors

• Relevance for actuaries

• What’s next?
Financial Risk Frameworks

Review Areas:
- Assets / Investments
- Capital Management
- Reserving
- Reinsurance
- Liquidity
- Pricing & Underwriting

Thematic review agreed by Senior Management

Prompted by horizon scanning analysis

Pricing & Underwriting FRF Review

Agreed part of annual supervisory cycle

Risk identified by line supervision

01 October 2019
Firms projecting underwriting outperformance despite expectation that premiums will be flat or falling and that the market in aggregate will post an underwriting loss.
Although risk adjusted rate change is positive, rate adequacy is below 100% for all three main lines of commercial business – as a result, the market in aggregate may struggle to meet its profit targets.
**Market Conditions**

**Personal**  **Commercial**  **Corporate**

**Risk Adjusted Rate Changes throughout Calendar Year**

- London Market
- Lloyd's
- Total
- 1/1 Renewals

Improved RARC in 2018 but 1/1 renewals show adverse trend in 2019

**Renewed rate strength minus new business rate strength**

- 2015
- 2016
- 2017
- 2018

New business generally viewed More favourably
The PRA’s primary aim is to answer the following question – **to what extent does the firm’s pricing capability, in the context of its business strategy, raise prudential concerns?**
What are we looking for? In Context

Strategy

Underwriting & Pricing

Reserving

Direction-Setting & Challenge

Consensus view of Ultimate Loss Ratio

Summary MI Performance vs Plan

Model Updates

Rate Change

Detailed MI Supports Decision-making

Summary MI Provides Account Overview
Our reviews are NOT focussed on....

- Cutting Edge Systems
- Market-Leading Models
- Use of AI and Machine Learning
- Charge exactly Technical Price
Live Polling

• Which of the following areas represents your top priority for development in pricing/underwriting over the next five years? (company actuary or other)
  • IT/Systems/tools improvements
  • Data: improve the quality or introduce new sources or applications
  • Exploration of new pricing techniques
  • Better analytics or Management Information
  • Recruitment of skilled resources
  • Culture/tradition barrier
  • Other

if you work outside a company, what is your view based on all the firms that you have come across

VIP Portal
https://vip.gatherdigital.com/apps/2234
All photos sourced from https://unsplash.com/ (free to use images not copyrighted)
To assist peer comparison, we pick a range of peers, not just the ones we have concerns.
our reviews are tailored to the business models and key risks for each sector.
Findings – Management Information

**Good Practice**
- Data, analysis, content and timing fit for purpose
- Evidence of driving decisions
- Standards to cover MI for delegated business

**Poor Practice**
- Limited signposting, narrative & top-down view
- Over-engineered or missing key metrics
- Not credible data (c)
- Out of date & backward looking (c)

**Context:** MI includes the detailed information used to inform decision-making as well as the higher level information summarising account performance provided to senior management.
Context: The decisions and processes we are interested in are all relevant activities firms take to make underwriting/pricing decisions. This include setting up clear strategy and plan, carry out regular and ad hoc rate reviews, rate changes, especially focused on the overall calibration and validation of the pricing assumptions.
Firm’s culture and tradition tends to influence how people interact each other. PRA is not trying to define how people shall interact, but we think effective feedback loop between key functions is very important.
Live Polling

what is your self-assessment of your firm’s overall capability in pricing and underwriting (if you work outside a company, what is your view on the average capability of the firms that you have come across)?
Could do better?
Capable?
Highly effective?

https://poll.gatherdigital.com/results/54c6cd64-9144-40db-942d-842620183eea
PRA carry out deep drive FRF reviews on all key activities.
To understand the whole picture of how a firm or an account is doing, we combine all the information we have from pricing, business planning, reserving and capital.
Future Plans – What next?

• We will continue to use pricing & underwriting reviews as part of our supervision to inform our view of risk

• Potential topics for additional focus in 2020 include:
  - A more detailed review of how pricing links to the claims function
  - Exposure management, particularly for liability lines where there are more significant challenges in monitoring accumulations
  - Governance for the application of AI and machine learning to pricing, where relevant (and engage with other regulators via FCA, EIOPA / IAIS)