

# Lloyd's Non-Executive Director Forum 2023

20 November 2023

# Opening Remarks

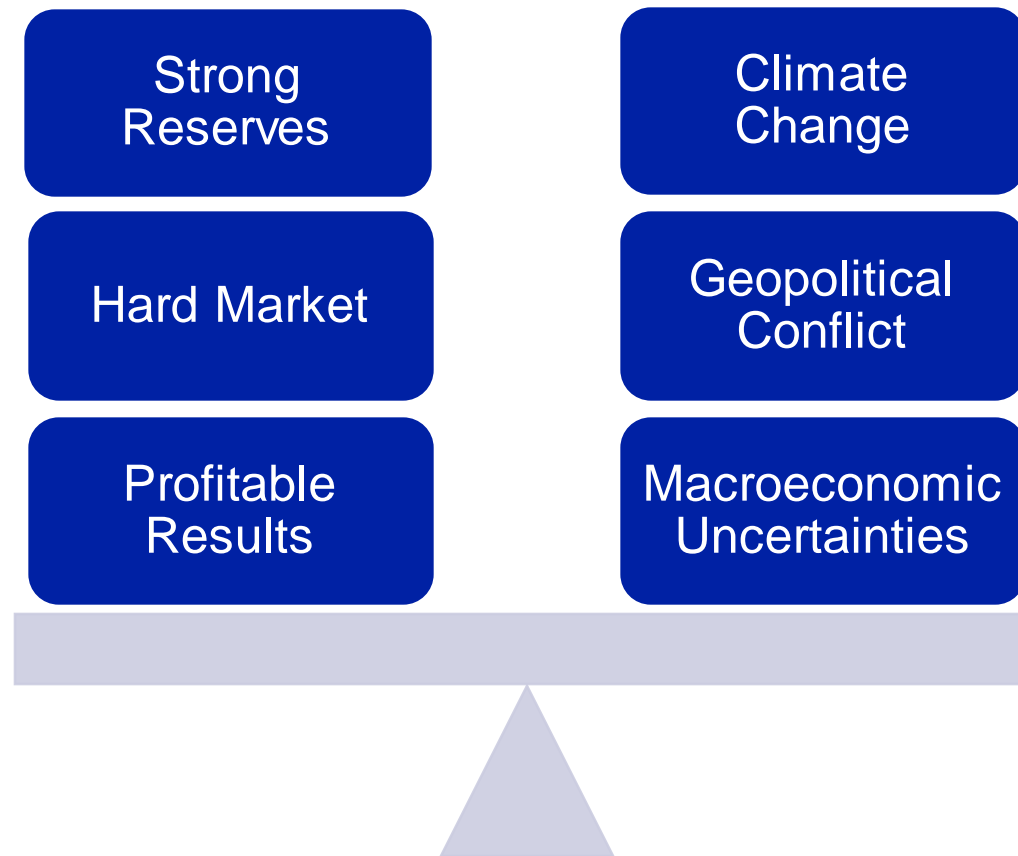
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Mirjam Spies

Chief Actuary

# It's a great year for the London Market – but a difficult environment

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# Agenda

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## Opening Remarks

1. **Appropriateness of Market Reserves**
2. **D&O US: Class of business review**
3. **Inflation**
4. **Risks on the Horizon**
5. **Investments**

## Final Remarks

## Questions & Answers

# Appropriateness of Market Reserves

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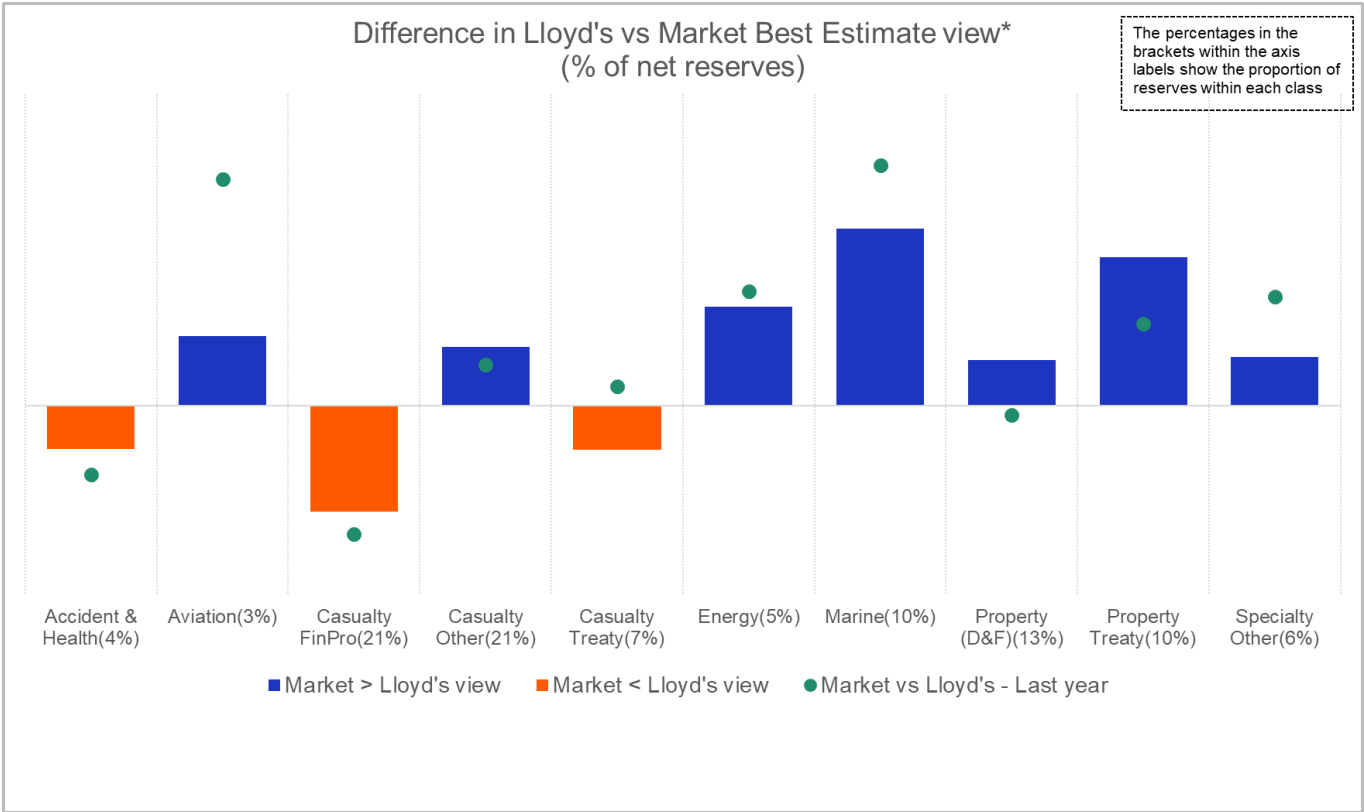
Shriya Parekh

Senior Actuary, Reserve Modelling

# We remain confident that aggregate market reserves are appropriate

Best estimate reserves are sufficient at total level but there are some concerns at class level

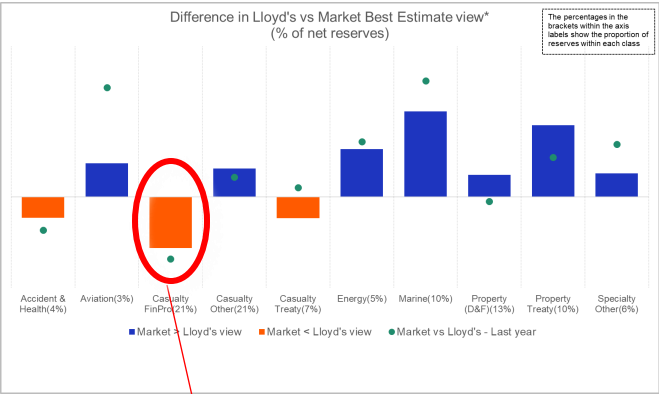
The market's best estimate reserves in aggregate continue to be in excess of our independent view.



# Class level concerns

## Drivers of difference

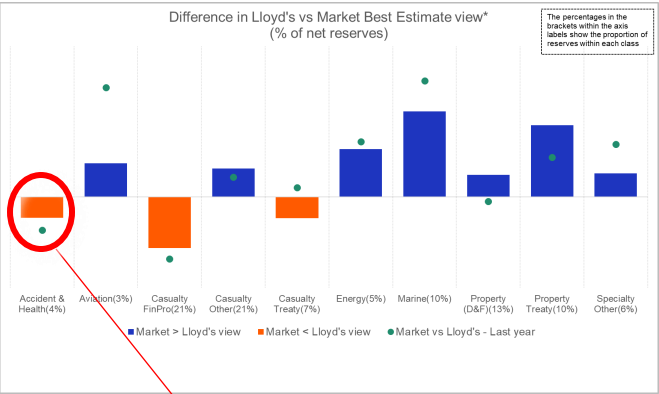
**Our best estimate for the following classes continue to be in excess of the market, although the two views are closer than last year.**



**Casualty FinPro:**

- Allowance for remediation actions?
- We have investigated D&O US in further detail this year.

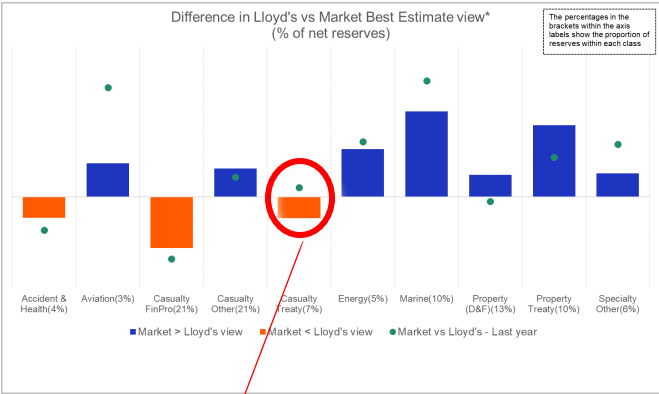
**Our best estimate is now in excess of the market.**



**Accident & Health:**

- Delays driven by Covid?
- Changes in underwriting?
- Divergence between experience and plan loss ratios.

**Our best estimate is now in excess of the market.**



**Casualty Treaty:**

- Allowance for remediation actions?
- Delays driven by Covid?
- A class we need to focus on going forwards.

# Focus Areas from 2022YE Global Central Reserving Exercise

Where should attention be focused?

The impact of remediation action	Stressed inflationary environment	Uncertainties
Risk Adjusted Rate Change	Transition to a new phase	Are these considered? To what extent? Quantified?
Business Mix	Updates to assumptions	What are the limitations?
Terms and Conditions	Differences between classes and geographies	Geopolitical risks and Climate Change
Changes in risk profile and impact on assumptions	Changes to the data	Underwriting cycle
Stage in the underwriting cycle and price adequacy	Feedback loops within the organisation	Secondary impacts
Impact on profitability		

**We recommend consideration of and allowance within Reserving for the key issues listed.**



# D&O US

## Class of business review

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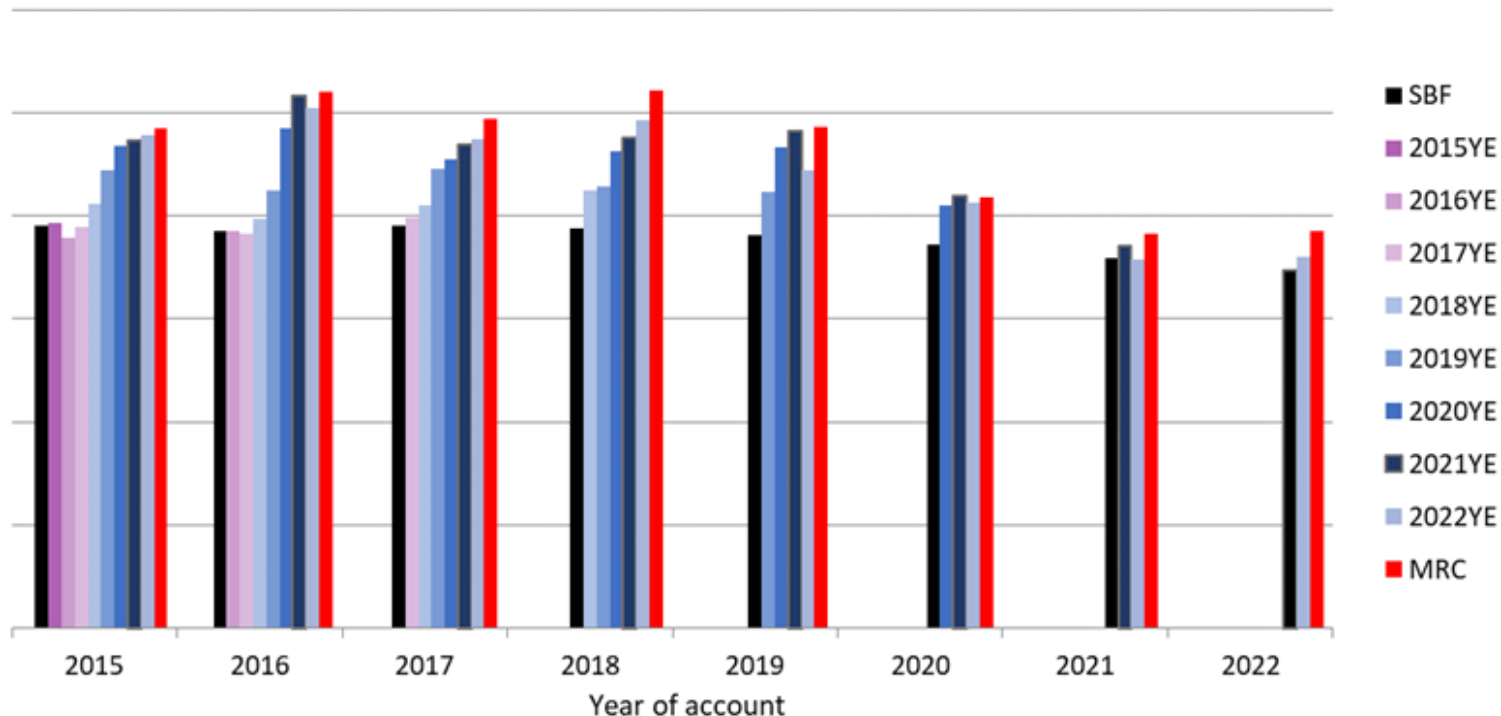
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# Casualty FinPro concerns

## Lloyd's vs Market

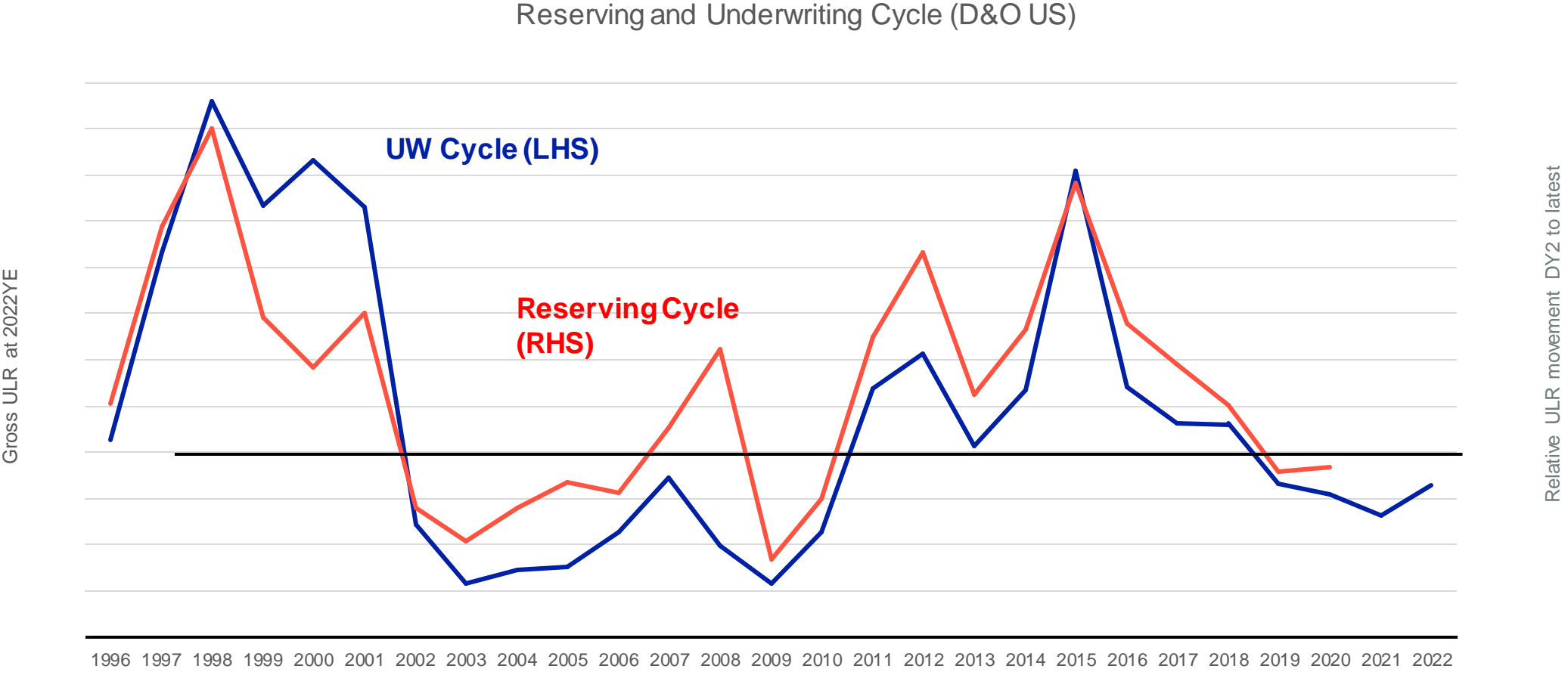
Market Gross Net Written Loss Ratio over time - Casualty FinPro



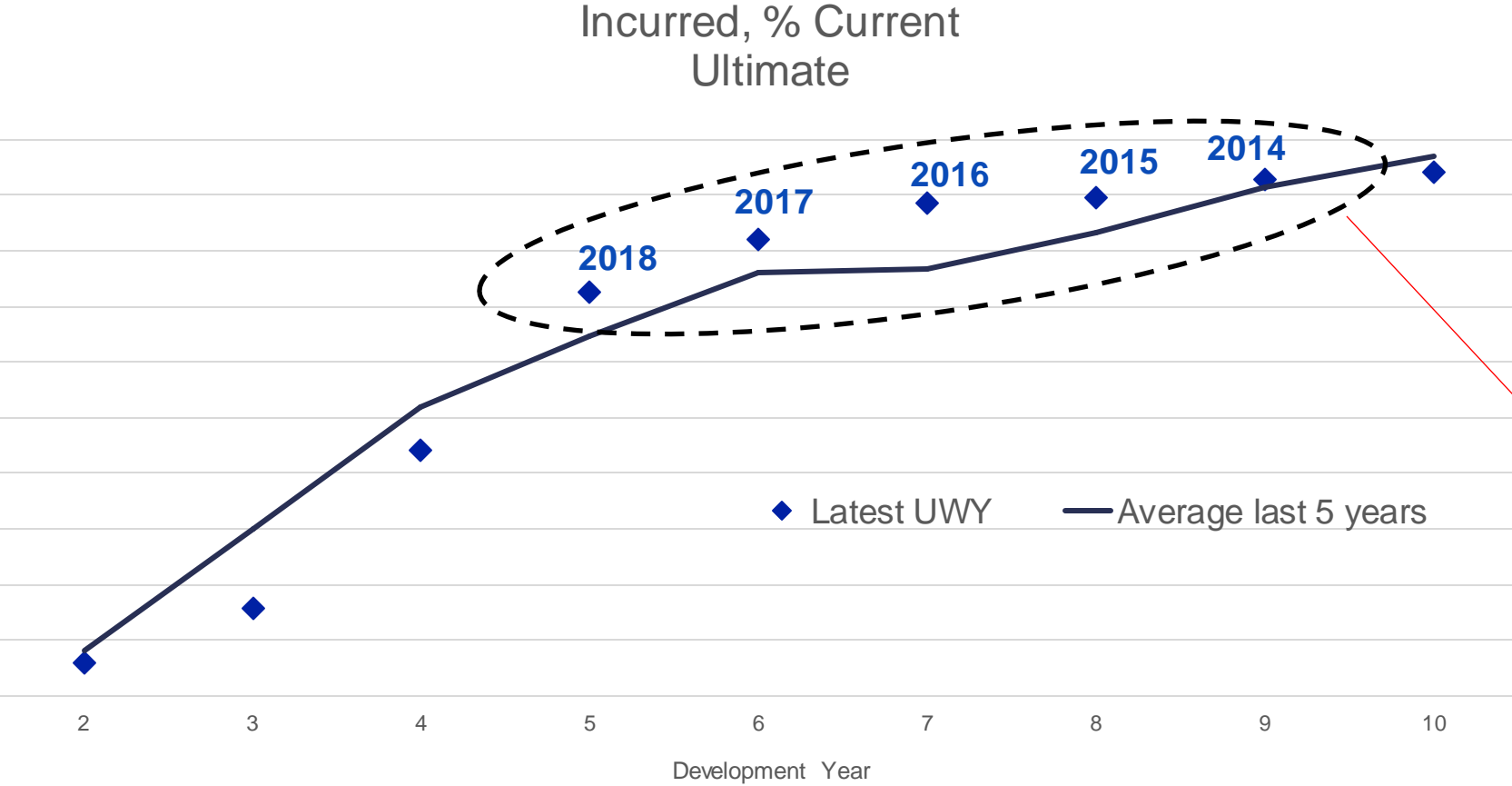
- We continue to see potential reserve deficiencies on almost all Casualty FinPro classes.
- Market's view still remains higher than initial estimates and SBF, bringing it closer to the Lloyd's independent view.
- Market continues to have a very positive outlook.
- Loss ratios are reducing significantly on recent years of account but still deteriorating.

# Reserving vs Underwriting Cycle

## Reserving cycle still exists!



# Reserving Methodology



**Soft market years – optimism in the current year ultimate selection when compared to historical experience?**

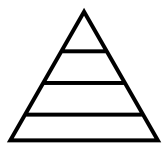
# Examples of MI

- **AvE is used consistently across managing agents and widely shared with management.**
- **Limited evidence that longer term trends, cross-cycle, are being considered sufficiently.**
- **No clear use of high-level early warning indicators other than AvE.**

	Year of Account	Avg IBNR burn during Yr 3	Avg Reserve burn during Yr 3
"BAD"	1997-2001	95%	18%
"GOOD"	2002-2006	30%	8%
"GOOD"	2009-2010	16%	7%
"BAD"	2011-2018	47%	15%
	2019-???	14%	7%

"GOOD" - lower %

"BAD" - higher %



**Segmentation**



**Frequency / Severity**



**Validation**

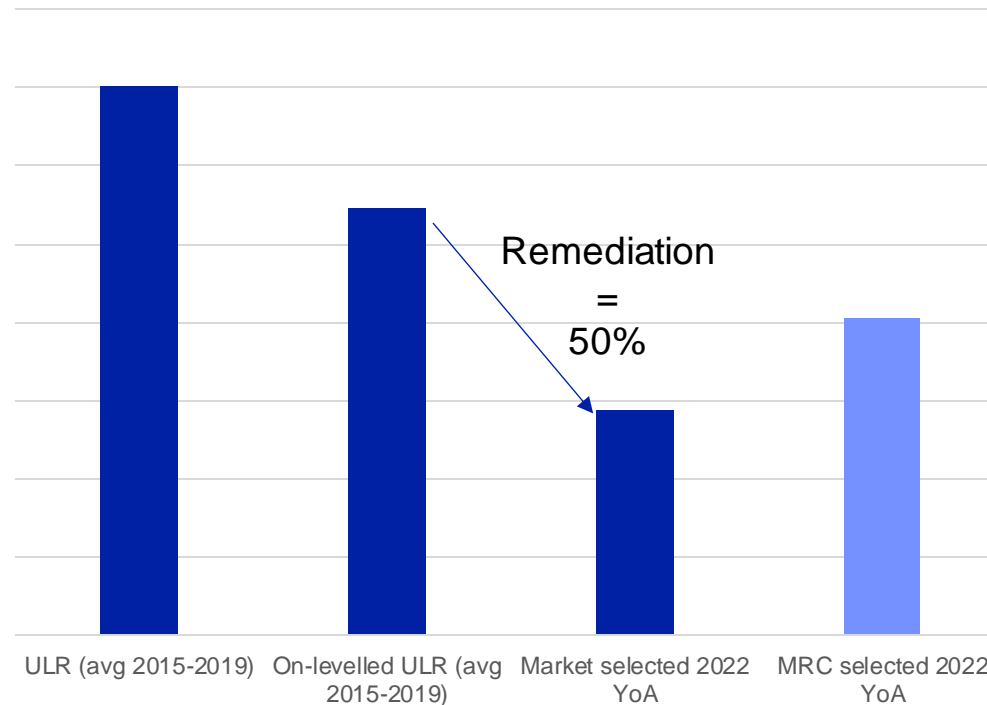


**Benchmarking**

# IELR Assumptions

## Survivorship Bias?

Loss Ratio Comparison at 2022 YE



**Judgements should be Transparent & Communicated**

# Challenge the Reserving Function

Reserving function needs to be transparent

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## Board considerations:

- **How is reserve function monitoring reserve appropriateness? Are you seeing a full suite of metrics?**
  - Consider trends over the entire cycle?
  - Is AvE the only early warning indicator?
  - Does the reserving function routinely share early warning outcomes?
  - Has the underwriting cycle been taken into account and have lessons been learnt?
- **Where have judgements been made that deviate from the history?**
  - Does the reserving function signpost deviations to historical trends?
  - What validations are considered where judgements differ from history?
- **If the book has been changed/remediated how much credit has been taken? Has new business been considered for increased uncertainty?**
  - Consider both hardening and softening markets.
  - Do you know which areas are changing?
  - How is this considered from a reserving perspective?

# Inflation

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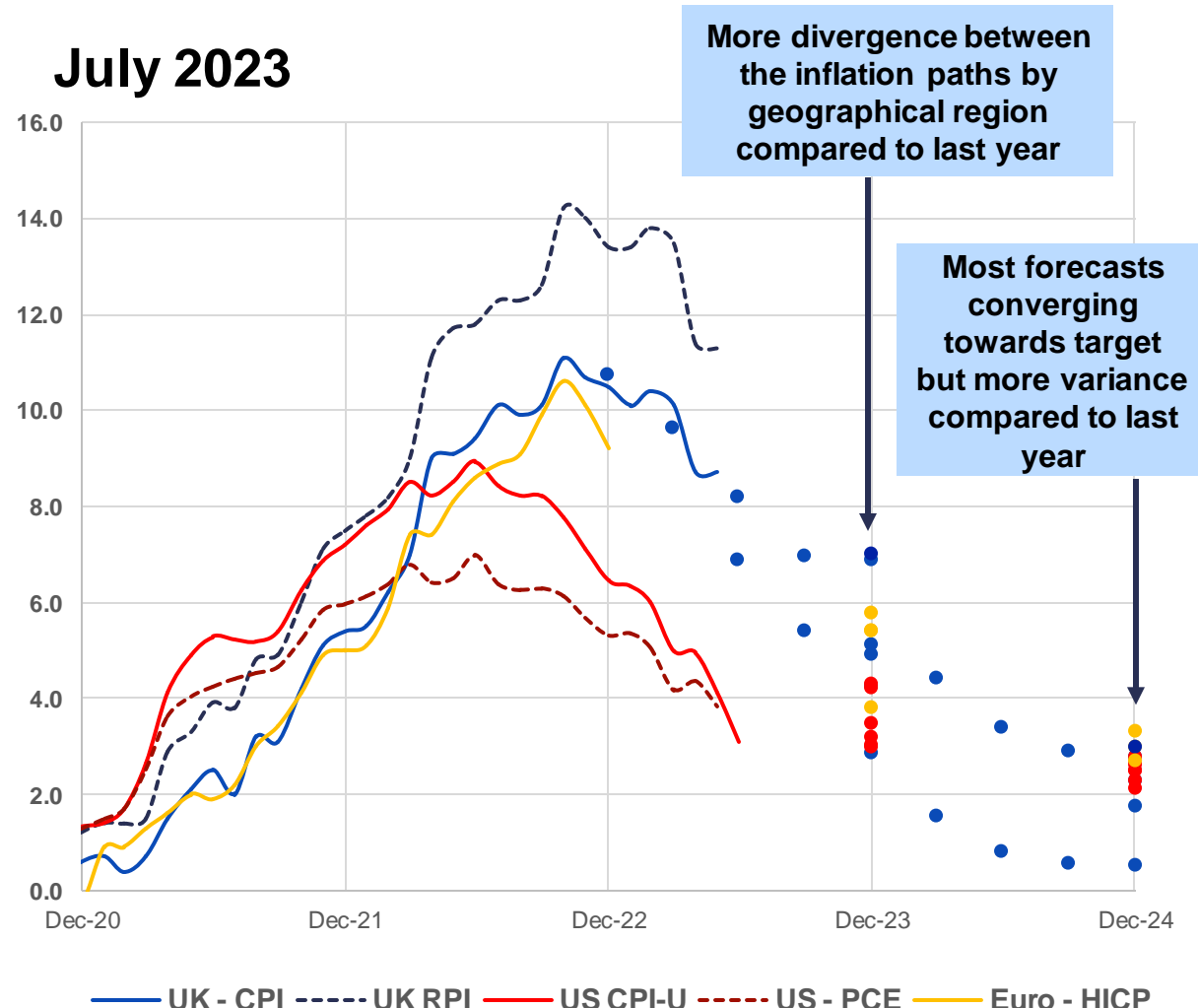
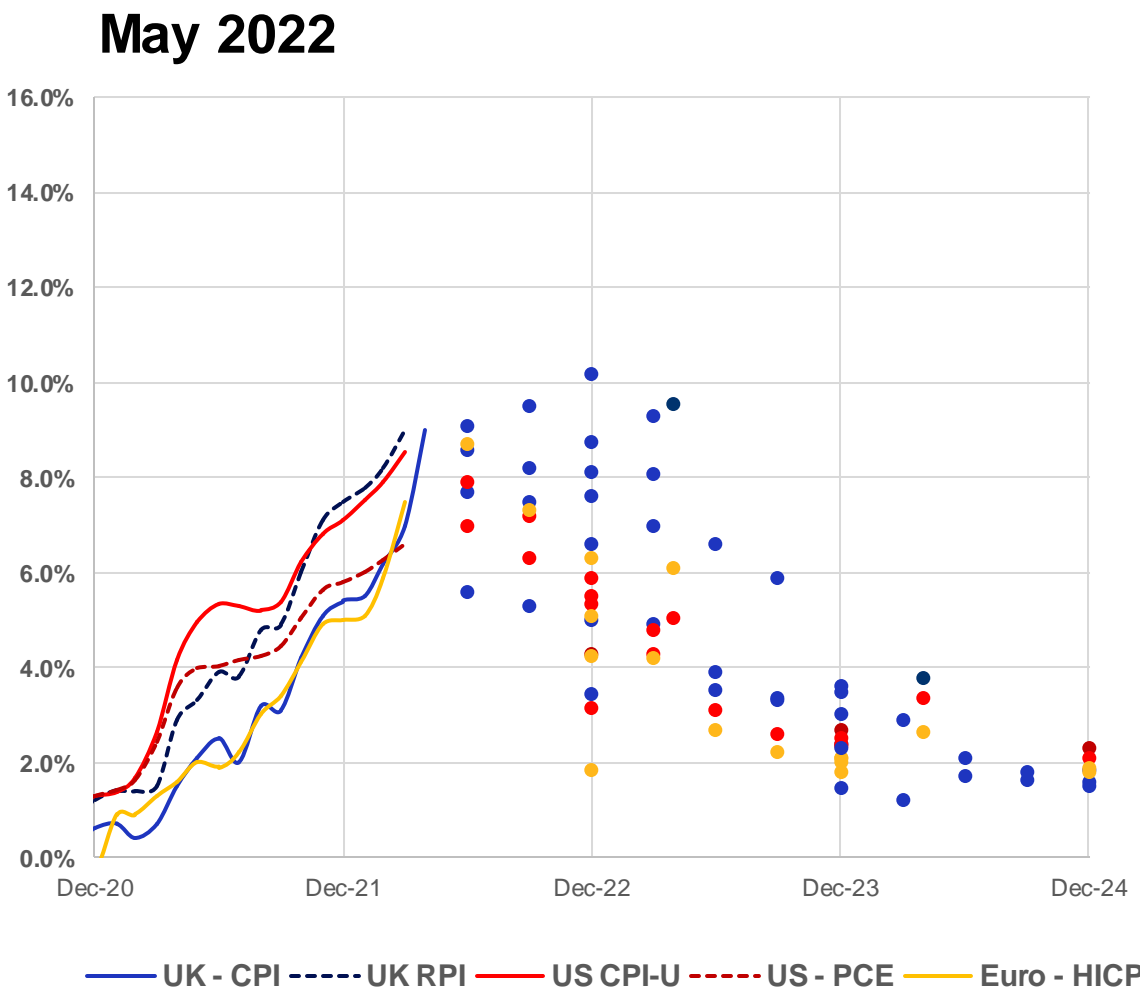
Nikhil Shah

Senior Manager, Syndicate Reserving



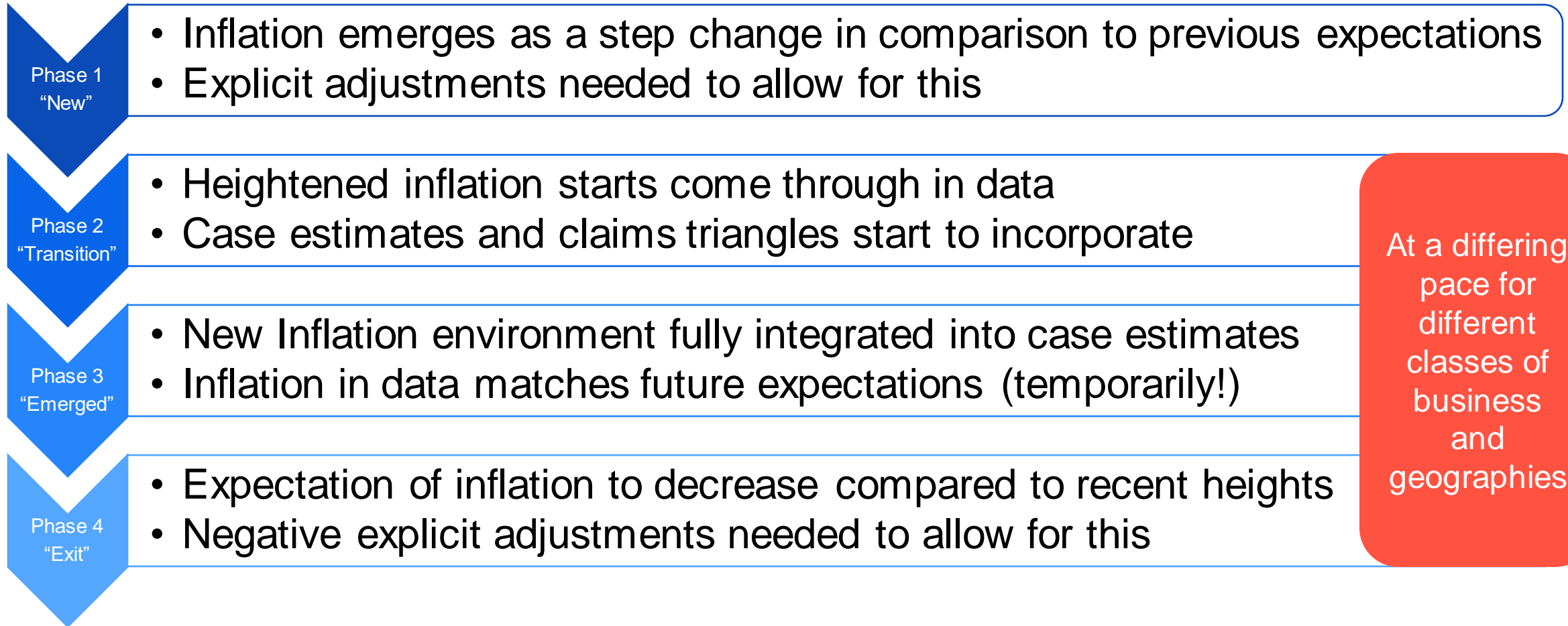
# Inflation: The latest view

Realised inflation has been higher and more persistent than expected last year for UK and Europe



# Inflation: Entering a new phase

The evolving nature of claims inflation create a complex problem



# Inflation: "Phase 2"

## Phase 2

- Inflation is beginning to emerge in the claims data, at differing pace by LoB and region
- Previous forecasts for inflation (upon which assumptions were set) are diverging from expectations



Work with Claims teams to determine what is and isn't in the data – how does economic inflation drive claims inflation, are there any lags?



Determine what additional allowance needs to be made for 'Incurred But Not Enough Reported' as well as pure IBNR



Benign AvE experience may be due to claims inflation not emerging in the data at the pace assumed



Consider duration and level of inflation – mean reversion?



Feedback loops critical between planning and capital

# Inflation: Good practice from existing framework

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**Governance and challenge:** Governance framework for inflation; cross-functional oversight and board challenge



**Feedback Loops:** Reserving team considers/validates inflation oversight by other functions.



**Validation:** To gain comfort in respect of inflation assumptions



**Uncertainties:** And how these are considered, including additional loads; a range of estimates, and selecting pessimistic views

# Assessing Inflation Allowances

Inflation assumptions need to be considered

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## Board considerations:

- **Monitoring data:** Are you monitoring the emerging claims data for inflationary impacts? Is AvE the only early warning indicator?
- **Lag effect:** Are you aware of if there is an underlying lag effect in claims inflation for classes where trends may not be observed?
- **Case estimates:** Are you aware if all case estimates have been updated consistently and holistically so that your reserving function only needs to consider inflation in the IBNR?
- **Benchmarks:** Are benchmarks selected appropriate given the risk profile? Are you monitoring changes in economic indices and any other benchmarks being used?
- **Drivers of inflation:** Have you identified the specific drivers of claims inflation by class?

# Risks on the horizon

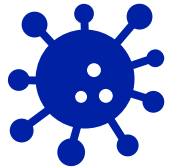
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# Sources of potential uncertainty on the horizon

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**Pandemics**



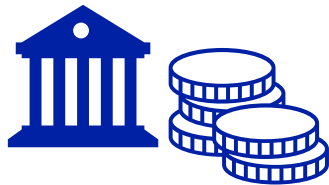
**Geopolitical tensions**



**Cyber**



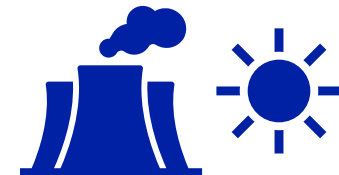
**Forever Chemicals**



**Banking sector crisis**



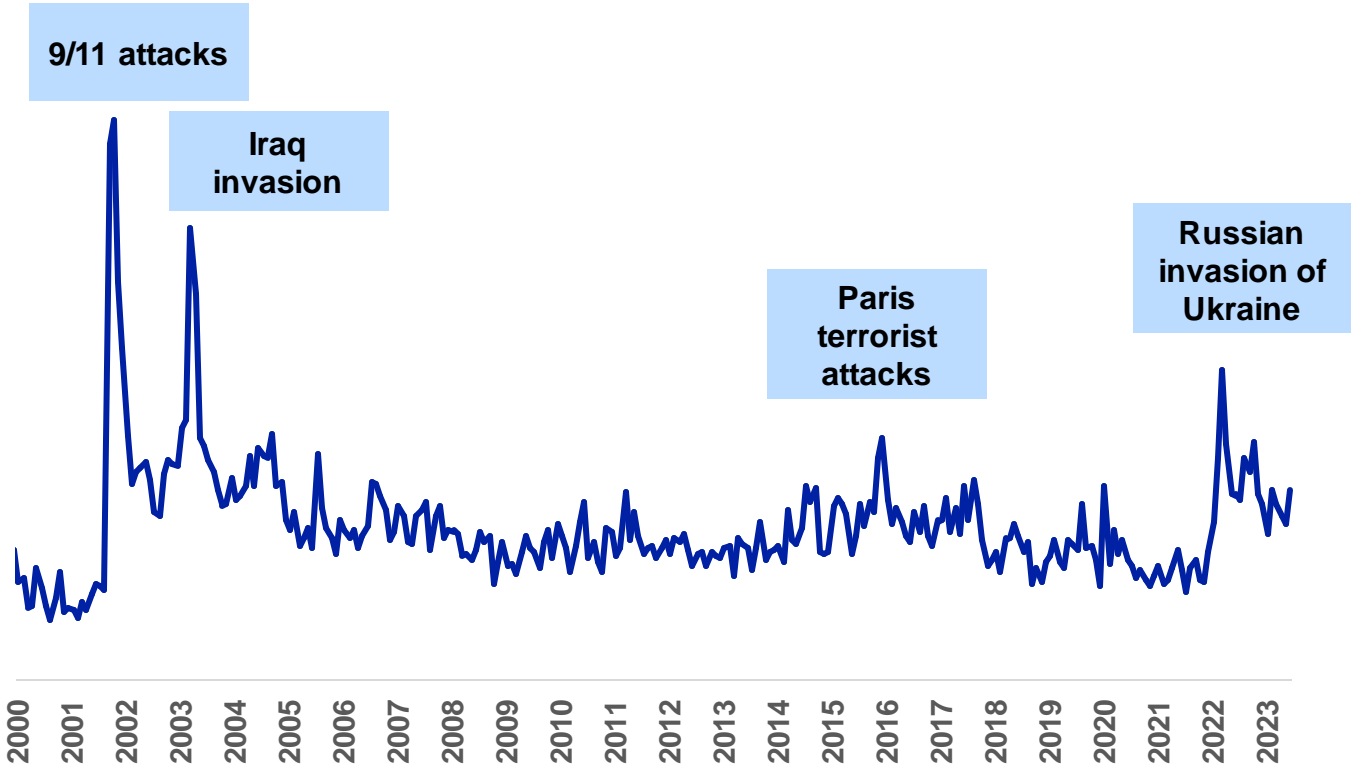
**Recession**



**Climate change**

# Geopolitical Risks – Primary Impacts

## Geopolitical risk index



Risk	Likelihood
1. US-China strategic competition	High
2. Russia-NATO conflict	High
3. Global technology decoupling	High
4. Major cyberattack(s)	High
5. Gulf tensions	High
6. Major terror attack(s)	Medium
7. Emerging markets political crisis	Medium
8. North Korea conflict	Medium
9. Climate policy gridlock	Medium
10. European fragmentation	Low

Source: [Blackrock geopolitical risk dashboard](#)

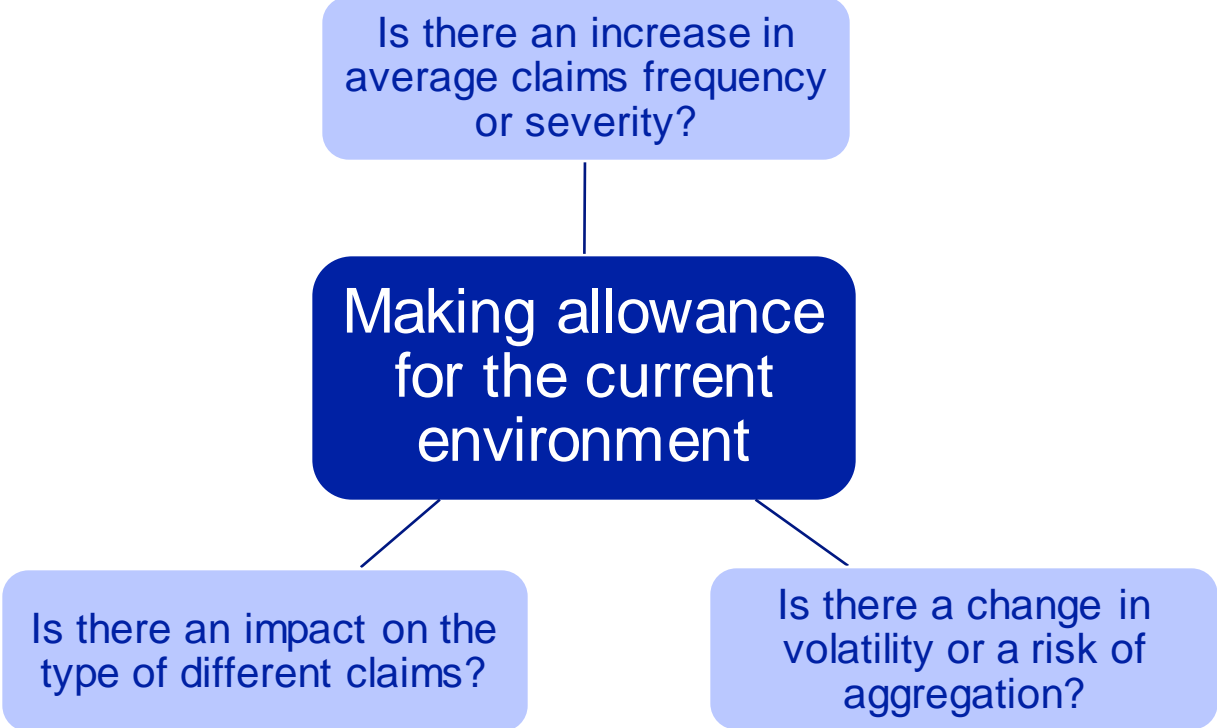
Source: Dario Caldara and Matteo Iacoviello



# Geopolitical Risks – Secondary Impacts

Allowance for the unstable global economic, political and social environment impacts within capital and reserving

Economic Environment	Political and Social environment
Increased Fraud	Claims events arising from social and civil unrest
Increased Propensity to claim	Impact of government and regulatory decisions
Increased claims costs driven by inflationary environment	Emergence of new claims types and movements



# Ukraine Crisis – key uncertainties

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**How are you comfortable that reserves/capital for Ukraine are appropriate?**

We have set out below some of the key areas of uncertainty you should consider in answering this question.

Coverage

Notices of  
Cancellation

Asset  
Location

Sanctions

Reinsurance

Data

Nature of  
the War

# Climate Change

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## Physical Risk

- Exposure changes vs. climate changes – what is driving the trends we see?
- Do vendor models sufficiently reflect today's (and the near future's) hazard?
- Which “non-peak” perils are becoming more material?

## Litigation Risk

- Are the new exposures and impacted classes of business understood?
- Has consideration been given to new and evolving cases / case law?
- What are the implications of untested contract wording?

## Transition Risk

- What are the implications of ESG investments?
- Is there any change to the underwriting, particularly with uncertain new technologies and emerging risks?
- Are there any changes to the investment strategy?

# Investments

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Angel Kansagra / Annika Hofmann

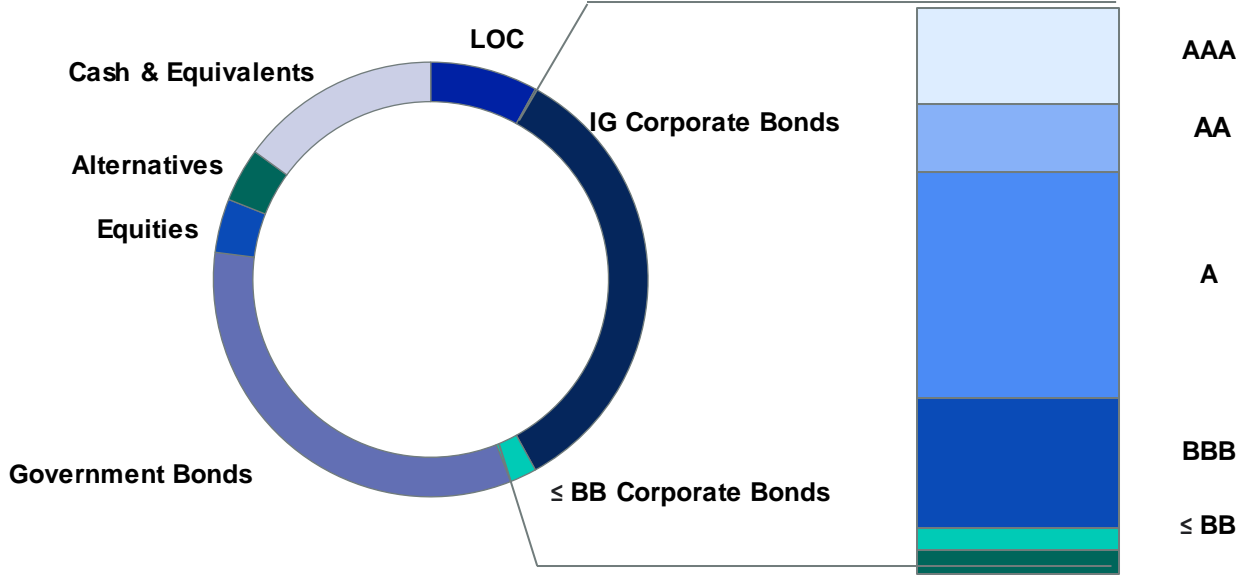
LTIM

# Lloyd's market investment portfolio

Managing portfolio risk and return opportunities

### Conservative asset allocation

### Corporate bond portfolio



### Short duration to minimise P&L volatility

Duration	
Asset (PTF)	Liability
2.0 years	3.4 years

Is enough risk appetite being utilised?

What about balance sheet & liability volatility?

Is the investment strategy optimised for capital?

Duration, credit/risk assets, FX?

# Know and monitor your risks

## Lloyd's Oversight Framework – Key Principles

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Investment Objectives & Risk Appetite



Responsible Investing



Parameters and Guidelines



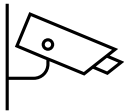
Asset Liability Monitoring



Stress Testing



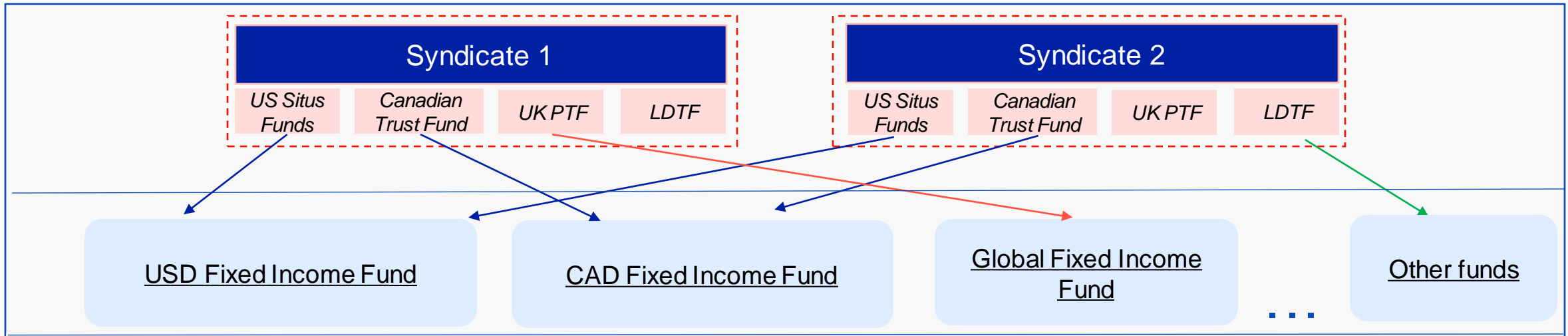
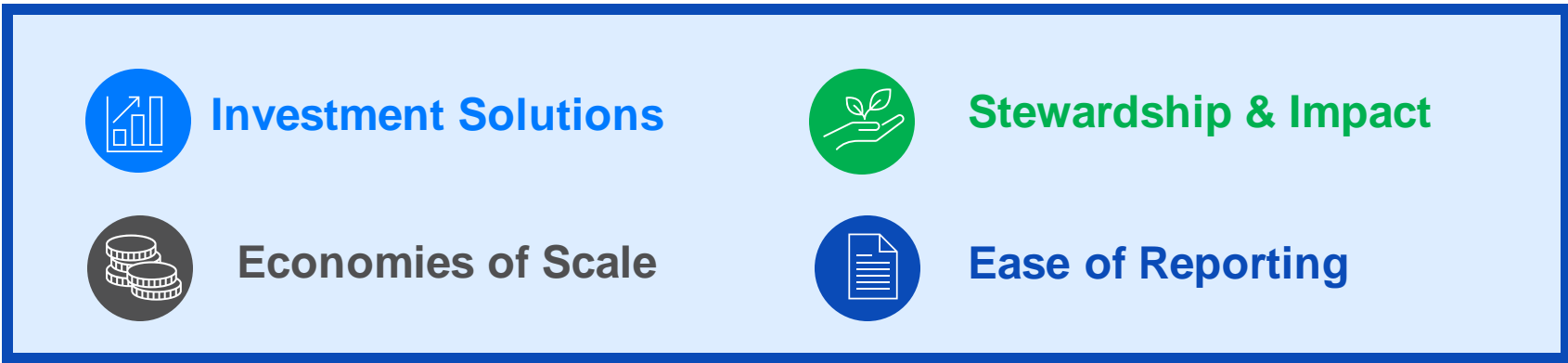
Governance



Monitoring & Reporting

# Lloyd's Investment Platform





Making it easier to generate risk-adjusted investment returns on capital held at Lloyd's



Syndicates can subscribe to multiple funds on the platform. Funds are comingled mutual funds issuing units to investors

# Current Investment Solutions

Meeting the investment requirements & needs of the market

	Investment Solution	Target Features	Target capital
Private Assets	 <b>Private Impact Fund</b>	<ul style="list-style-type: none"> <li>✓ Access to Private Equity returns</li> <li>✓ Climate Change &amp; Social Impact</li> <li>✓ FAL Eligibility: Evergreen fund structure, quarterly dealings</li> <li>✓ Article 9 SDFR classification</li> </ul>	<ul style="list-style-type: none"> <li>• Mid-size and large capital providers</li> <li>• FAL-focus</li> <li>• USD &amp; GBP share class</li> </ul>
	 <b>US Mid-market Direct Lending Fund</b>	<ul style="list-style-type: none"> <li>✓ Access to Private Credit returns</li> <li>✓ FAL Eligibility: Evergreen fund structure, quarterly dealings</li> <li>✓ Floating rate income</li> </ul>	<ul style="list-style-type: none"> <li>• Mid-size and large capital providers</li> <li>• FAL-focus</li> <li>• USD</li> </ul>
Public Assets	 <b>USD Enhanced Yield Liquidity Fund</b>	<ul style="list-style-type: none"> <li>✓ Higher target return over cash/MMF</li> <li>✓ High Liquidity: Settlement t+1</li> <li>✓ High Quality: Low Solvency 2 capital charge</li> <li>✓ ESG Considerations</li> </ul>	<ul style="list-style-type: none"> <li>• All market participants, especially syndicates</li> <li>• FAL &amp; PTF</li> <li>• USD</li> </ul>
	 <b>CAD Core Fixed Income Solution</b>	<ul style="list-style-type: none"> <li>✓ Enhanced Fungibility: Reduced operational complexity / cash drag within Canadian Trust Fund structure</li> <li>✓ Access to wider range of CDS cleared assets through a local manager</li> </ul>	<ul style="list-style-type: none"> <li>• All market participants, especially syndicates</li> <li>• PTF</li> <li>• CAD, USD</li> </ul>

**More funds to be launched in 2024**



# Final Remarks

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Mirjam Spies

Chief Actuary

# Summary



**“So far so good” - we are in a strong position but need to keep our actuaries on their toes!**

## **Key take-aways:**

1. Longer-tail casualty lines remain in focus, as many uncertainties affect them more (inflation, secondary effects of the emerging risks, legal challenges)
2. Hard market generally means reserve strength is high – but when the market softens later deteriorations are more likely.
3. Understand how much credit has been taken for remediation – and if there is bias to new business
4. Stay on top of the world changing quickly (like inflation phase 2, wide-spread impacts of geopolitical risks, understanding impacts of climate change).
5. Scrutinise your investment strategy – is it optimised? Has it changed given the current market conditions? Are you taking your responsible investment policy into account in your investment decisions?

# Questions

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# Key Contacts

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