

Syndicate Capital Briefing

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3 February 2020

Agenda

- Capital Market Messages - for the connoisseur
- 2020 SCR reviews
- Priorities for 2020

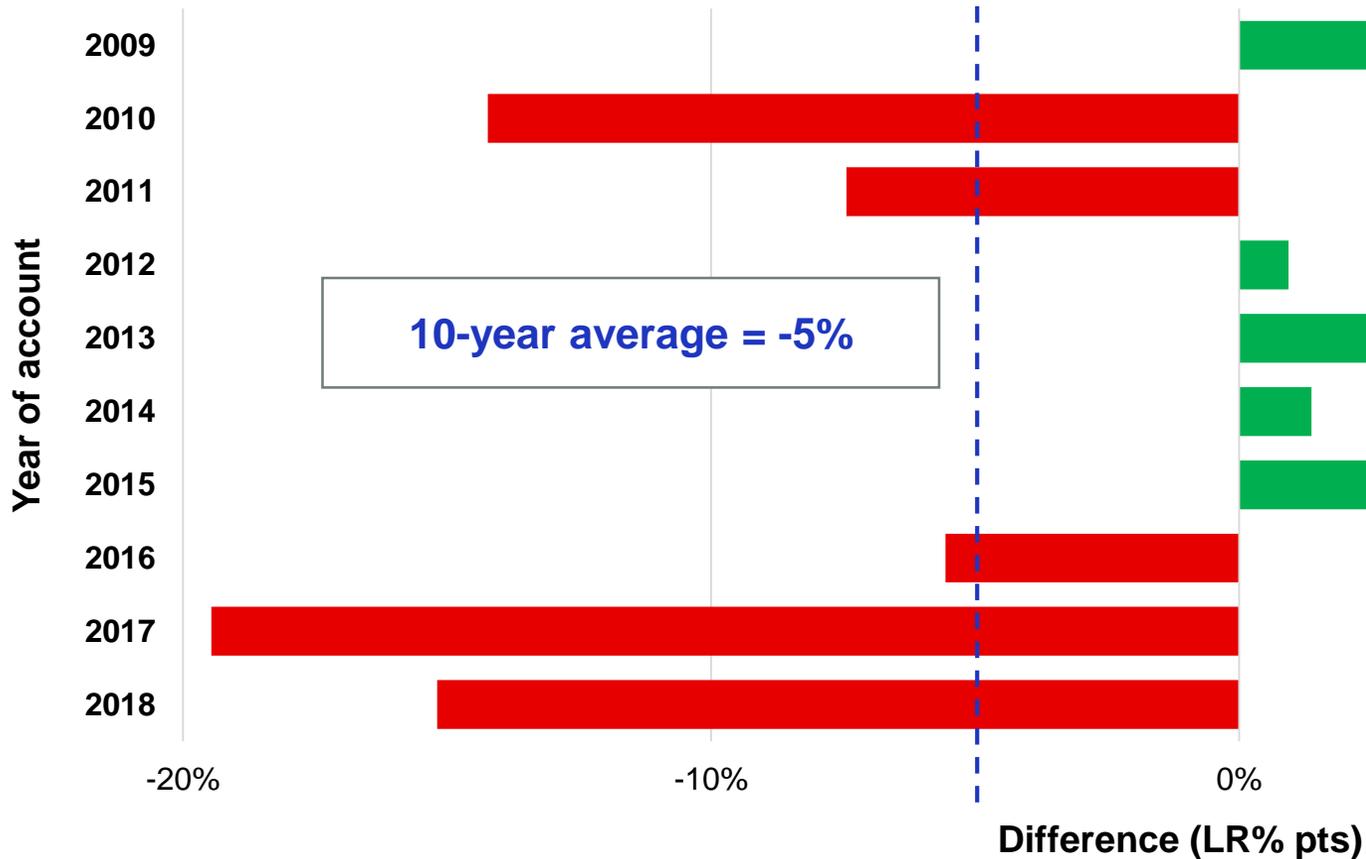
Capital Market Messages - for the connoisseur

A reminder of the key objectives for 2020

- 1 A better combined ratio than 2019
- 2 Expense ratio lower than 2019
- 3 Robust capital assumptions on expected performance
- 4 Capital movements clearly linked to risk profile
- 5 Plans which are logical, realistic and achievable

Plans continue to look ambitious against track record

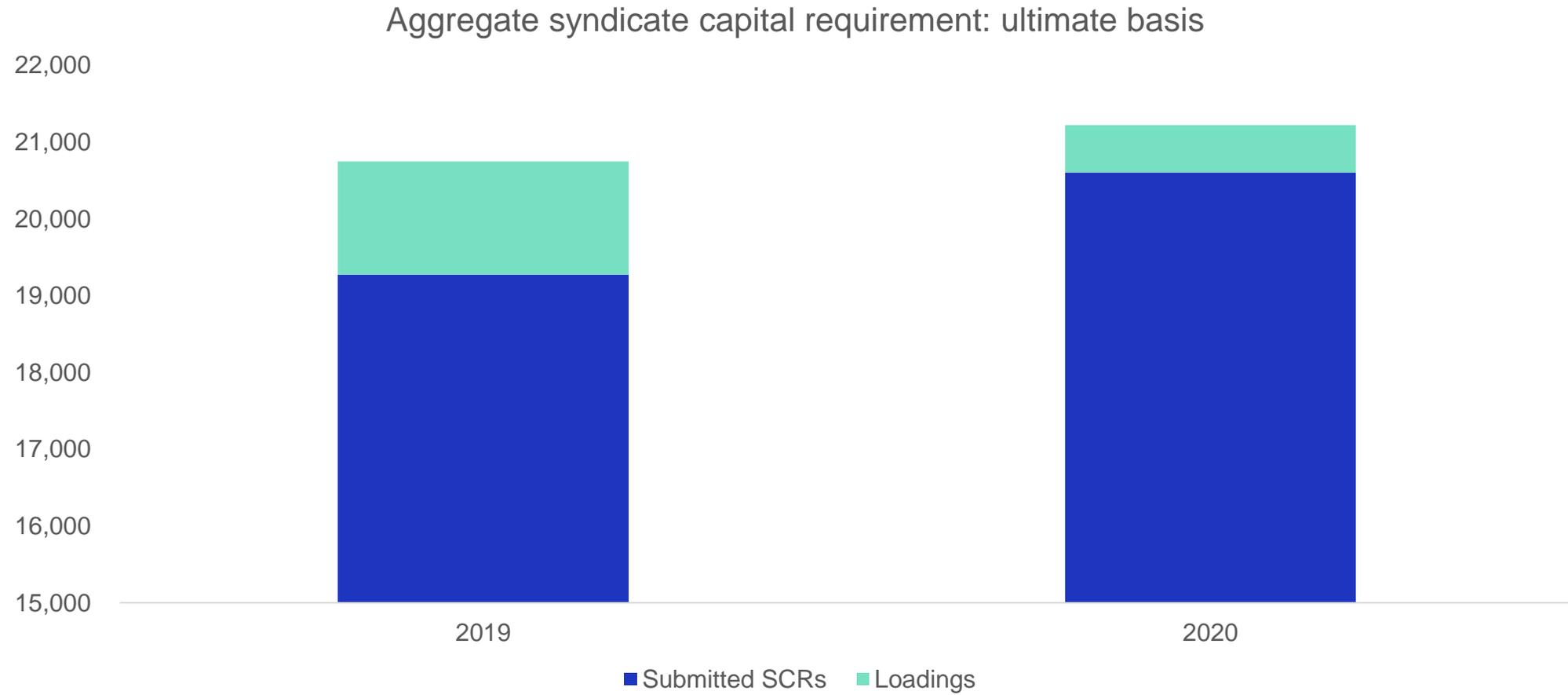
Difference between plan loss ratio and Lloyd's ultimate loss ratio



Combined ratio			
	SBF to model self-load	Lloyd's uplift	Total uplift
2019	1.0%	1.5%	2.5%
2020	2.6%	0.4%	3.0%

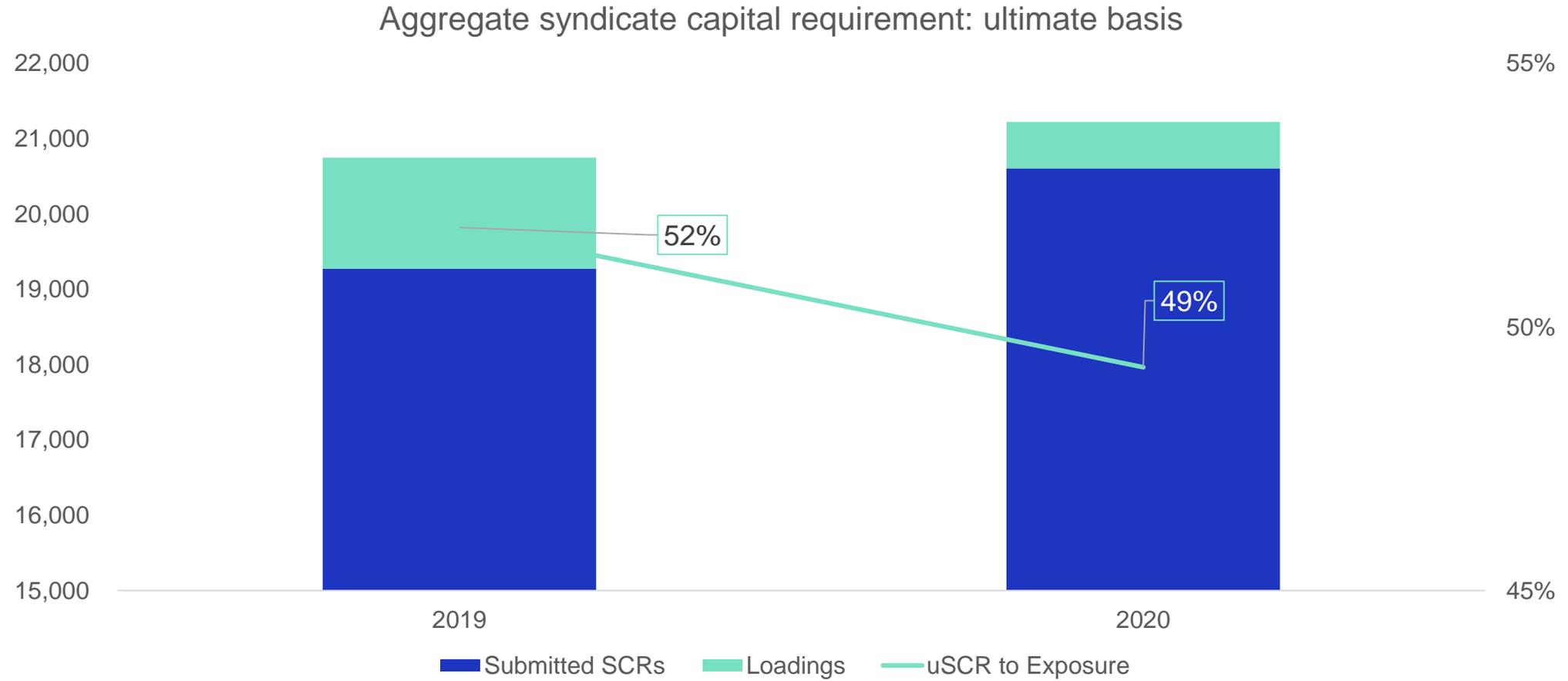
Required capital represents an increase on 2019

- an expected result in a growing market



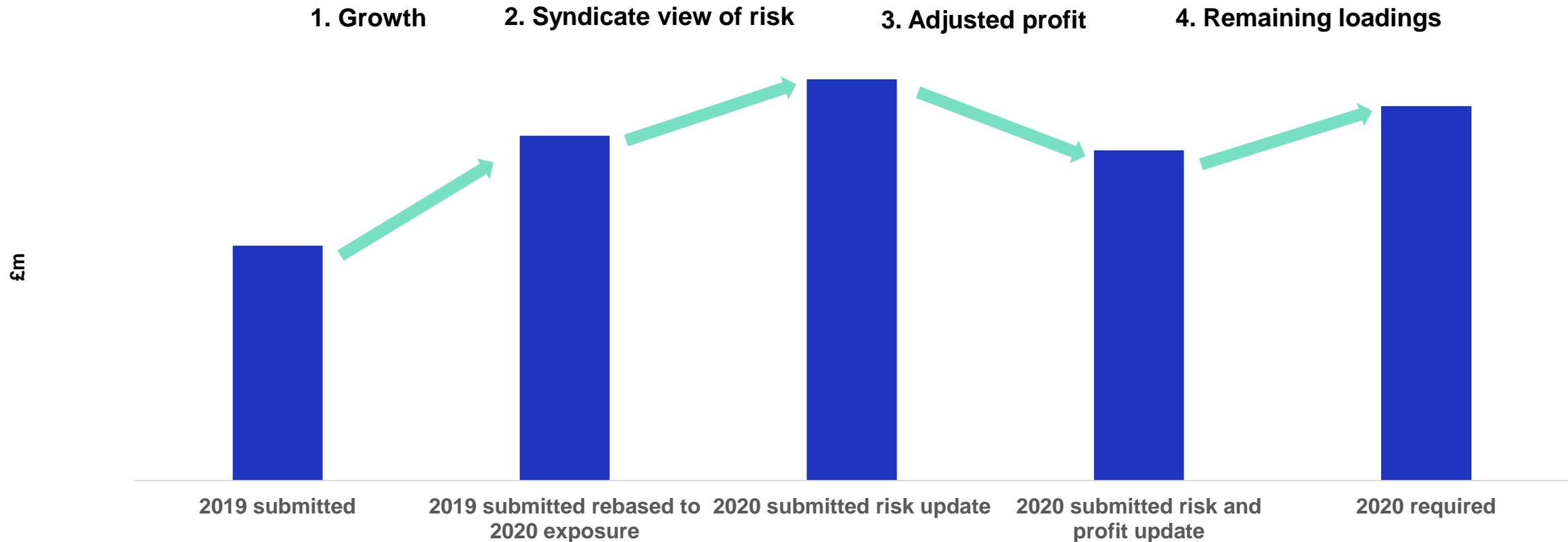
Required capital represents an increase on 2019

What message does this give on risk profile evolution?



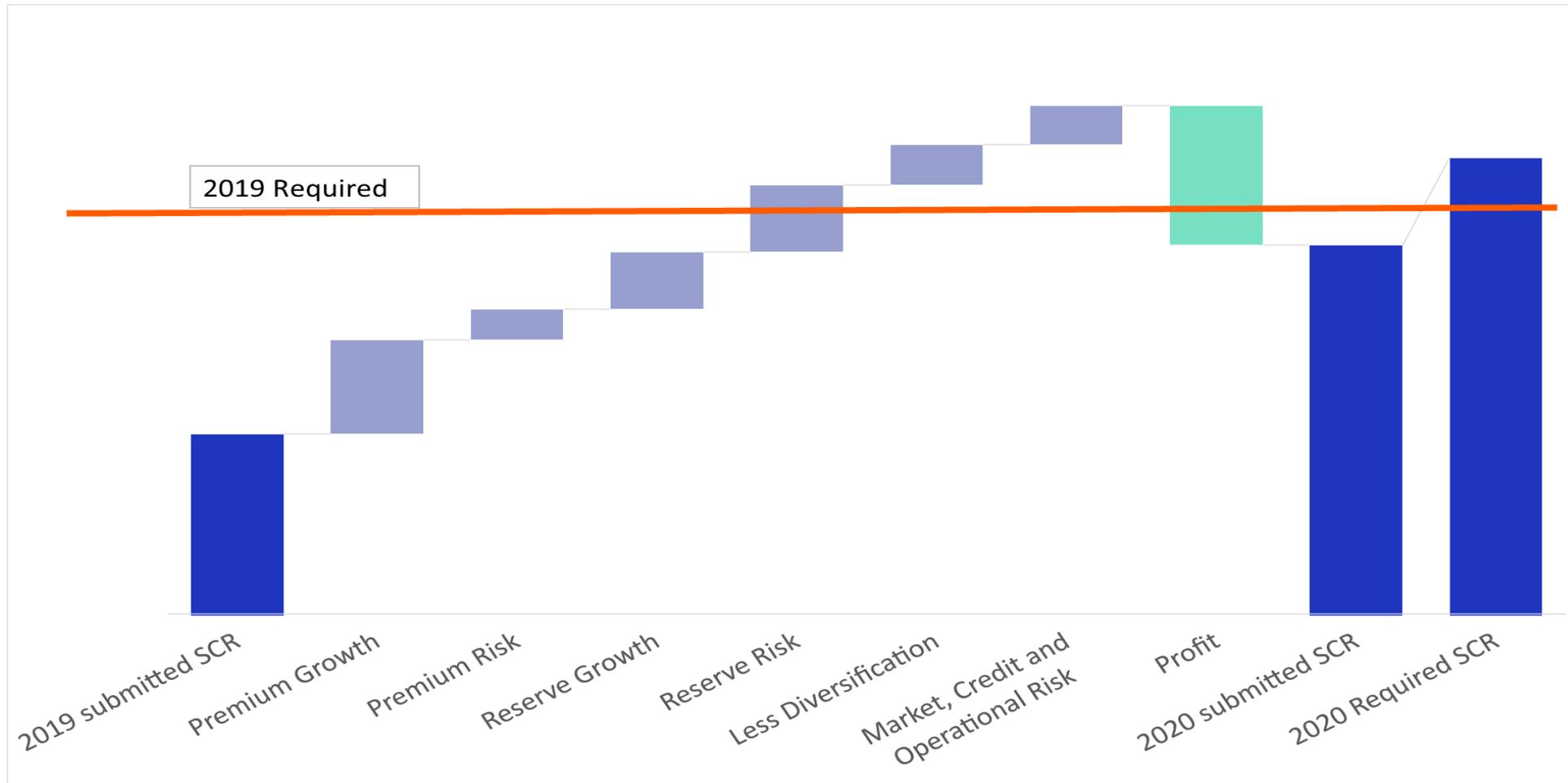
Syndicates have better reflected risks in their capital submissions for 2020

Increased view of risk is offset by increased profit (and risk margin)



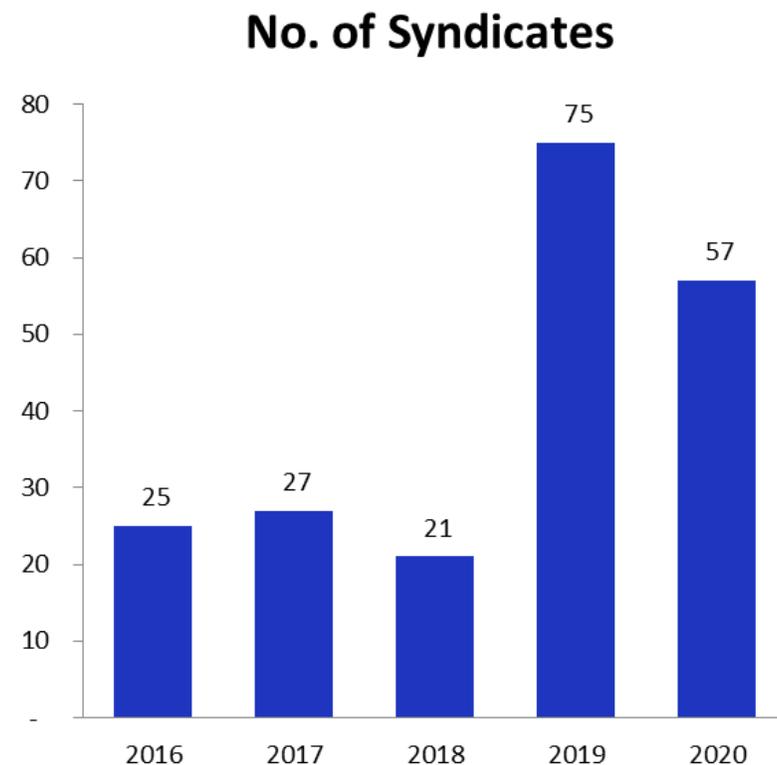
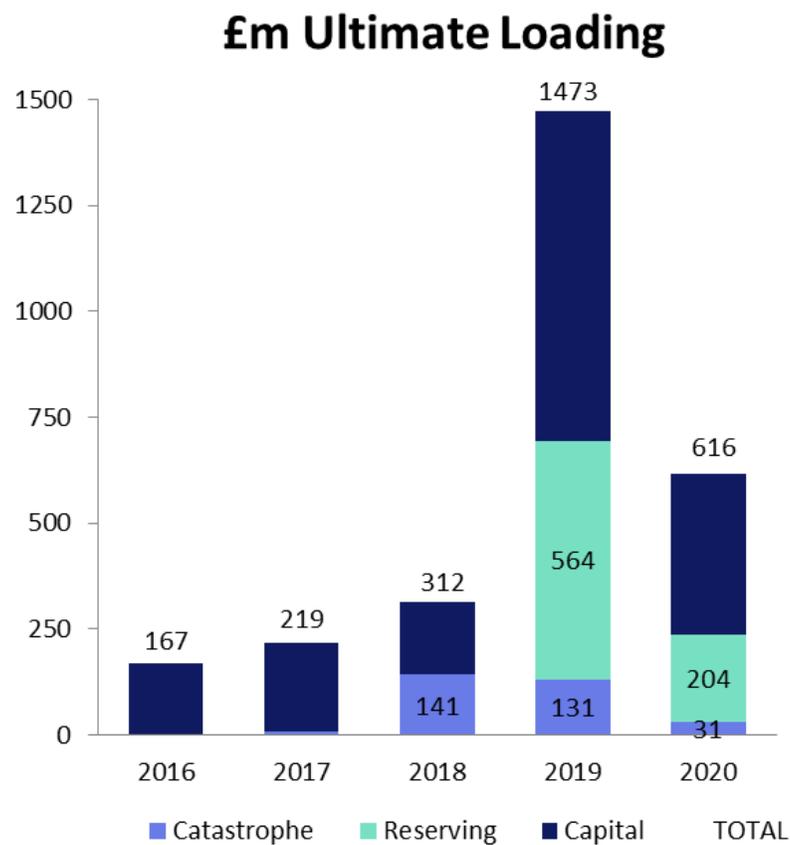
Links to risk profile require a more detailed analysis

We don't set an expected direction, we look to understand drivers



A smaller amount of loadings have been applied for 2020

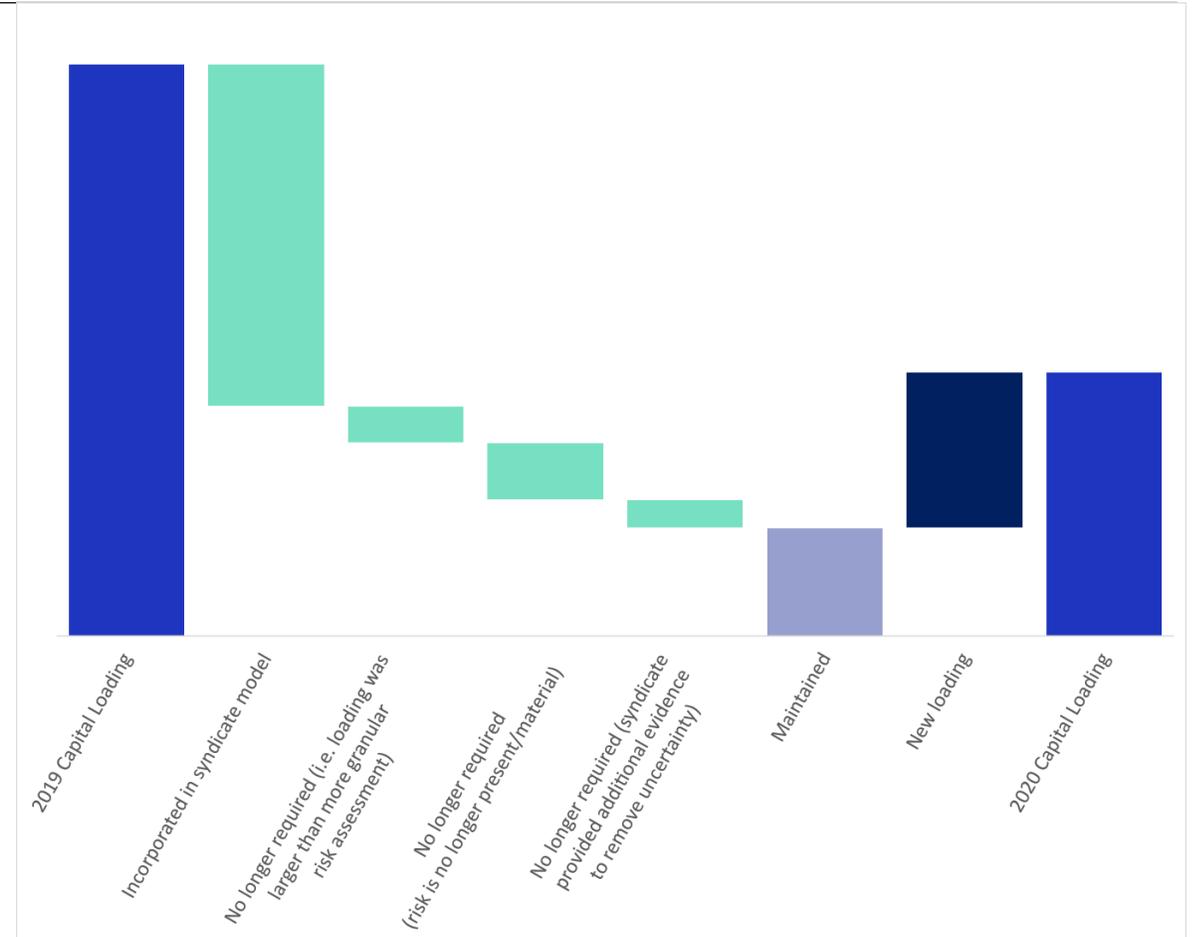
- the majority of 2019 loadings have been accepted and incorporated by syndicates for 2020



... still applied to a large number of syndicates

A smaller amount of loadings have been applied for 2020

- 80% of loadings incorporated into modelling or maintained
- Applied loadings generally indicate an issue that needs model change
- Common issues addressed through market working groups in 2019
- Pragmatism is welcome, though any management adjustments should be temporary
- Indicative loadings communicated in 2020 less “sticky”



Current process includes differentiated oversight based on submission quality

- factors that could lead to an 'easier' capital review

Strong validation

**Complete analysis of
change**

**No indication of 'cherry-
picking' change**

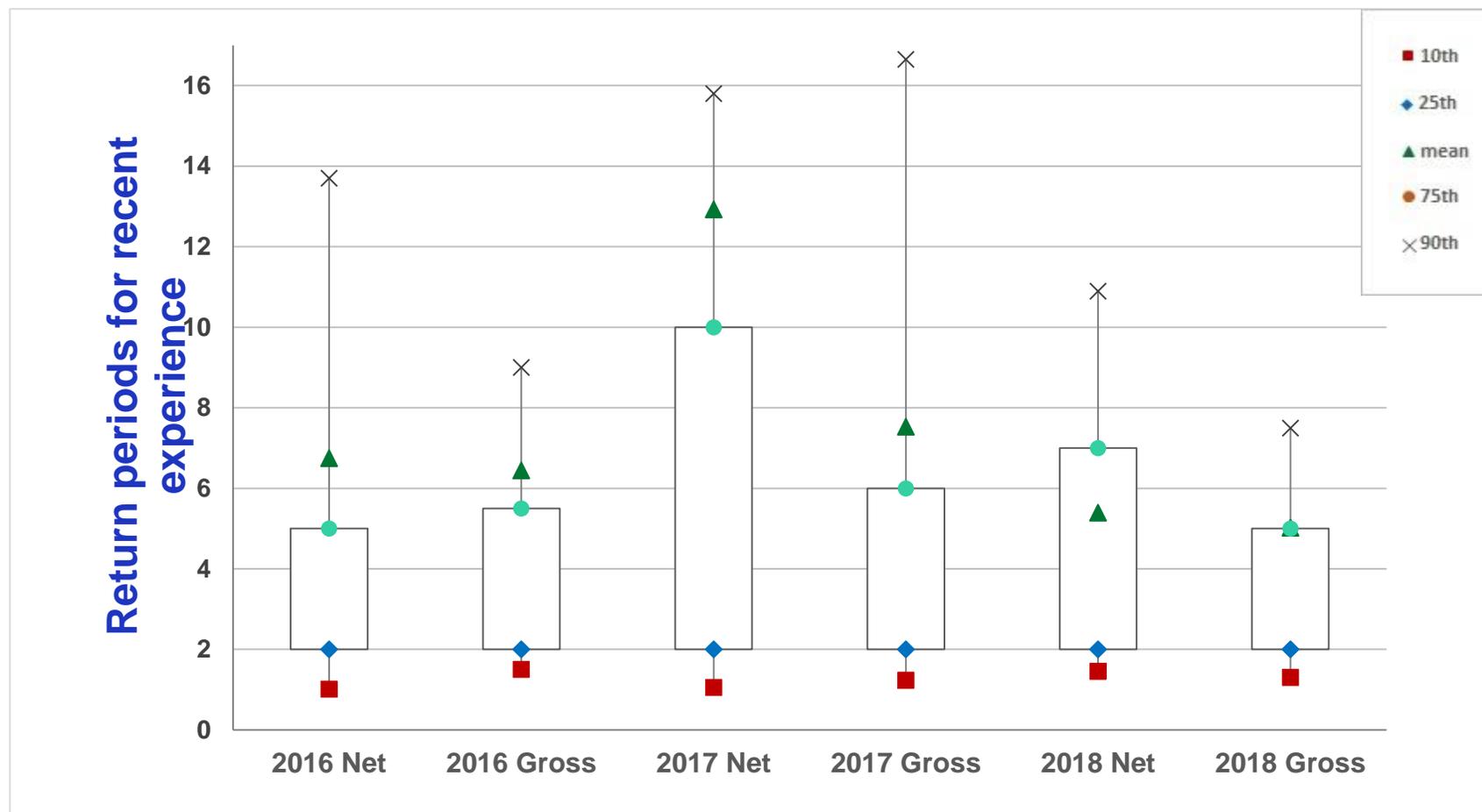
**Incomplete analysis of
change**

**Inconsistencies in
submission**

Indication of model drift

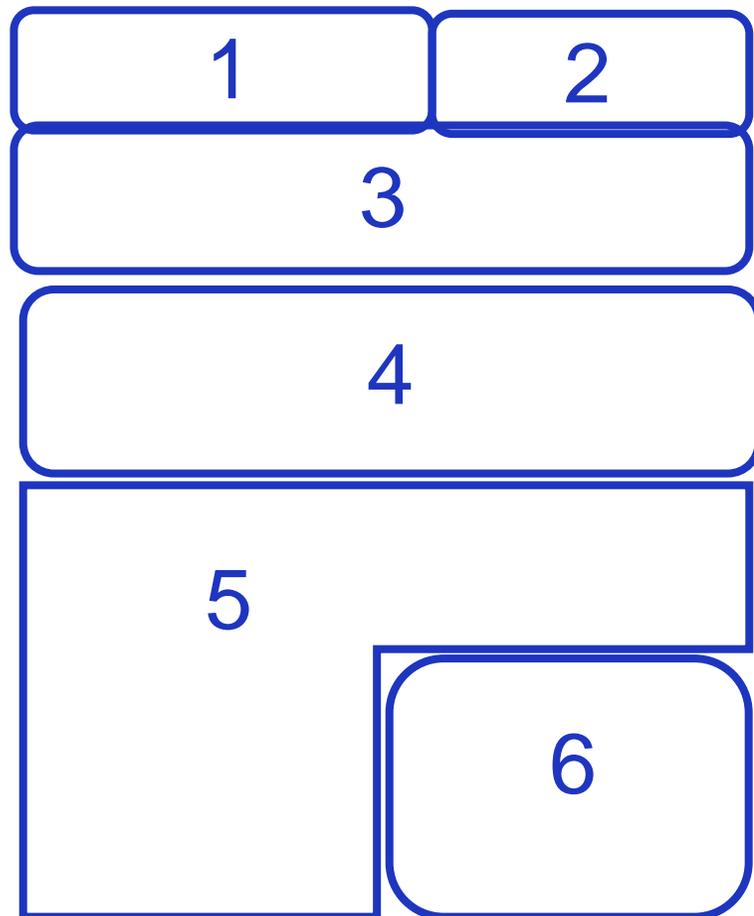
Recent experience provides useful context on risk profile changes

- Calendar year experience ex cat across the market



Current process includes differentiated oversight based on submission quality

- What are we looking for?



1. Which Syndicate is it, what is the capital and how has this moved?
2. What are the return periods of recent years and extreme events?
3. What is the review level and high-level conclusions?
4. What is the breakdown of capital and any issues by risk type?
5. How has the SCR and risk type output varied over time compared to exposure?
6. How does the SCR and risk type output compare to the market over time?

3 Robust capital assumptions on expected performance

Priorities for 2020

4 Capital movements clearly linked to risk profile

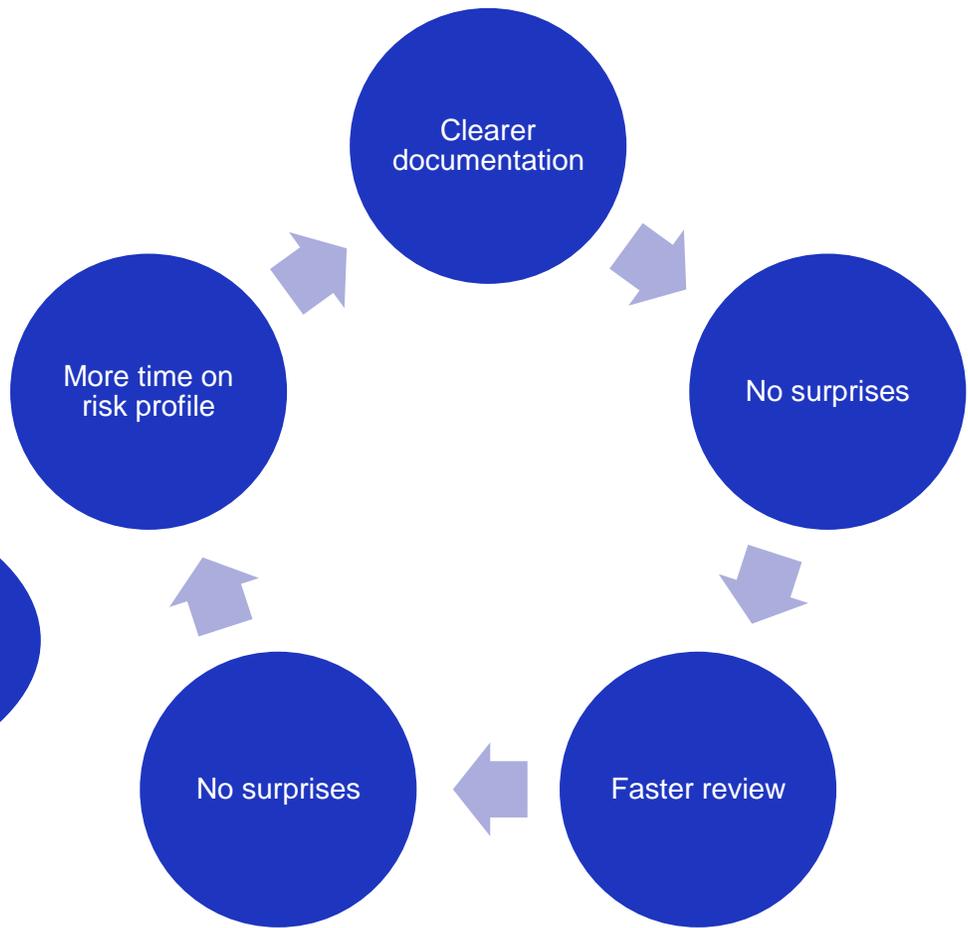
In summary

+ Process and guidance improvements

I've always seen modelling as a stepping stone...



...To articulating a clear understanding of risk profile evolution



2020 SCR reviews

Stream-lined process



Lower Capital Loadings: Engagement over the year to address loadings and clear tests on thematic loadings



Phased approach with faster reviews



Improved communications – in terms of quality and timing

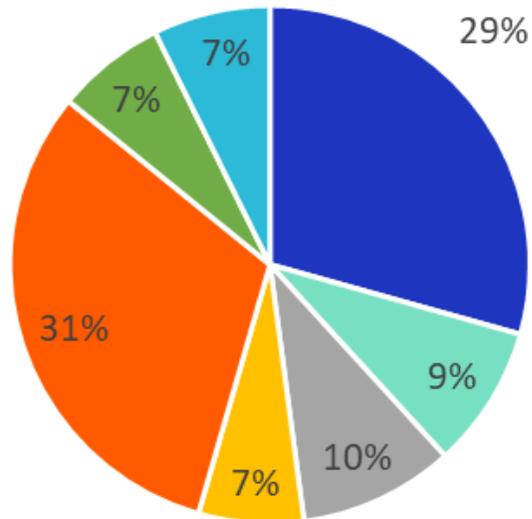


Fewer appeals on capital

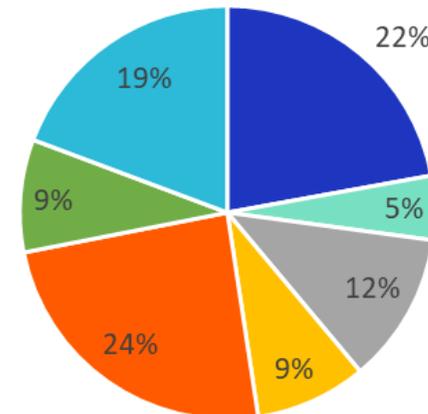
Loadings applied across a range of risk areas - Amounts

Reminder – the 2019 pie was much bigger than the 2020 pie is

2019 Reviews



2020 Reviews

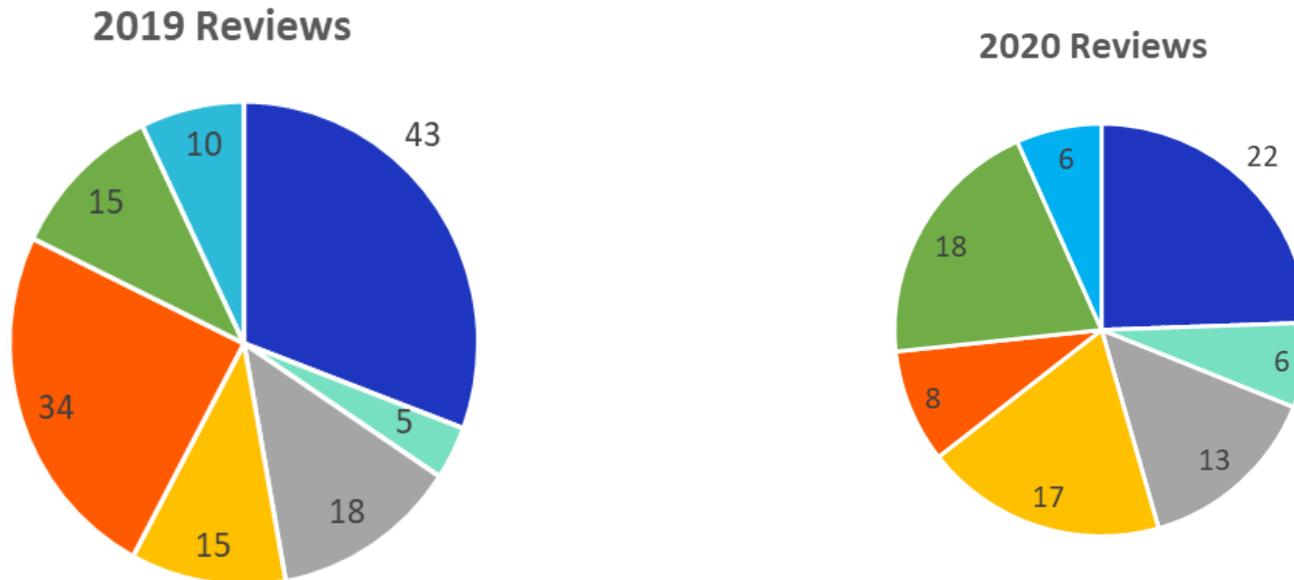


■ Premium and reserve risk ■ Catastrophe Risk Appetite ■ Market Risk ■ Other modelled risks ■ Prospective loss ratio assumptions ■ Other Reserving loadings ■ New syndicate/Solvency II

- Prospective loss ratio assumptions still most significant driver in terms of amounts of loadings, but reduction in proportion
- Similarly premium and reserve risk loadings reduction
- Main increase for SII/new syndicate loadings

Loadings applied across a range of risk areas - Counts

Reminder – the 2019 pie was a bit bigger than the 2020 pie is



■ Premium and reserve risk ■ Catastrophe Risk Appetite ■ Market Risk ■ Other modelled risks ■ Prospective loss ratio assumptions ■ Other Reserving loadings ■ New syndicate/Solvency II

- Prospective loss ratio assumption loadings only applied to 8 syndicates – large reduction
- Similarly premium and reserve risk loadings large reduction
- Negative contributions of market risk loadings decrease as expected
- Increases in other reserving loadings (mainly data issues) and other modelled risks

Targeted action to address common areas of loading in 2019

Additional templates on market risk and dependencies – fewer loadings

➤ Negative contribution of market risk

- Additional template was filled in by syndicates with negative market risk (on one year or ultimate)
- Most syndicates with negative contribution to ultimate market risk were loaded – one year negative market risk generally accepted
- main reason lack of common inflation driver across insurance and market risk → might be understating dependency (also within insurance risk)
- Encourage syndicates to investigate dependency between market and insurance risk – esp. with exposure to FinPro classes (flagged in focus area return)

➤ Insurance Risk Dependencies

- Additional template was filled in by syndicates that failed the SST → fewer than last year
- They did in general not fail the additional tests and no loading was applied

Common areas of loading in 2020 to be investigated

Contributions of minor risk types to capital very low or unexplained movements

- **Contributions to capital of minor risk types – credit risk and operational risk**
 - 17 of syndicates were loaded for these risk types (but generally by small amounts)
 - Reason was a low contribution of these risk types to capital – almost entirely diversify away

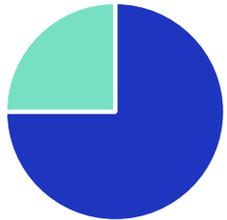
REMEMBER:

- Not only standalone risk type movements but also contributions to capital need to be analysed and validated
- If there are changes in risk profile (e.g. more benefit from reinsurance, additional business being taken on) we expect to see a capital impact of this on the minor risk types
- If there is a risk – e.g. contribution of credit risk or operational risk to your RST – we expect this to be reflected adequately in your capital contributions
- Simulation error not accepted as reason for movements/low contribution - link to risk profile.
- Review guidance on model stability, market working group

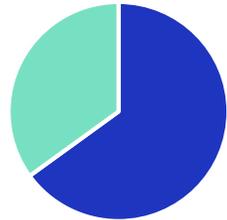
Phased approach with faster reviews

-... but more to do

Capital approvals

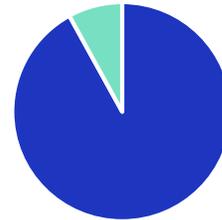


75% of eligible syndicates had capital approved in **4 weeks**



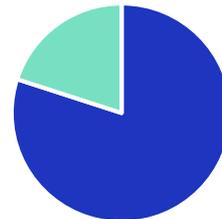
65% of eligible syndicates had capital approved in **6 weeks**

Approval letters



85% of letters were sent within 24 hours (up from 57% in 2019)

Proposed Loadings



80% of proposed loadings were sent within a week of the date we told you

More stream-lined – but faster overall?

Most syndicates on a 6 week timetable

80% of syndicates needed to submit additional capital information

- Review time was then 6 weeks
- Change of process highlighted focus on **Quality of Analysis of Change**
 - Clearer guidance on analysis of change
 - Setting out Lloyd's expectations on explanations of capital movements
- Shift to more **Continual Review** throughout the year → pilot this year

Improved Communication

Still more we can do

- Transparency on review level
- Questions condensed to potential loadings to focus efforts prior to CPG
- Prompt response from syndicates and significant amount of loadings was removed
 - indicative loadings were almost £2bn and only £616m were agreed by CPG

Improved communication resulted in very few appeals

- Communications straight to CEO
- Time pressure on any response is high
- Piecemeal questions rather than complete list



Validation preview

- Validation should not be running the same battery of tests every year but be tailored to risk profile
- Validation should at least cover model changes
- Validation should be a useful tool
 - it should help with the top-down view and taking a step away from the model
- Validation feedback on individual reports has now gone out
- Thematic market-wide review into Reverse Stress Tests and testing against experience this month
- No separate submission of 3-year validation plans



Don't carry out analysis of change/validation on auto-pilot – should be led by the changes

Priorities for 2020

Priorities for 2020

Minimal change this year, prepare for more fundamental change

1 Model changes – new guidance in force

2 Improved submissions – review of guidance

3 Fast-track approach

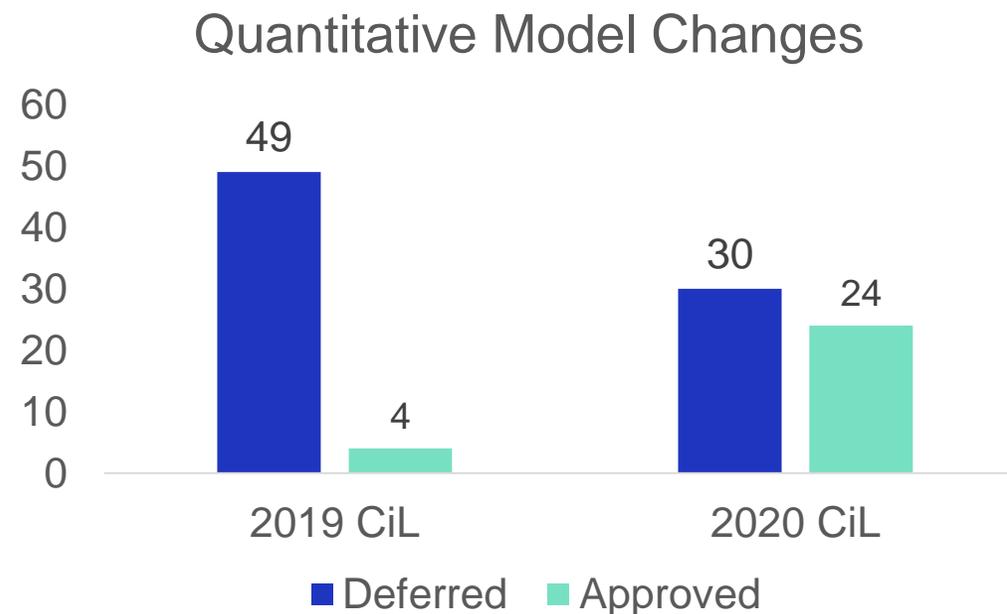
4 Revamp of the LCR forms - preparation

Improve Major Model Change Application Process

In last years' briefing we said we wanted to:

➤ **Give a better service:**

- Reasonable turnaround times – guidance now states 8 weeks for complete applications
- Defer less model changes in submissions
 - Fewer deferred changes this time
 - Most of them reviewed in December



Improve Major Model Change Application Process

In last years' briefing we said we wanted to:

- **Reduce the NUMBER of REVIEWS (in particular MMC Applications accompanying submissions)**
 - We have updated the guidance to:
 1. Exclude data changes - agents to specify metrics to determine when a data change becomes a risk profile change
 2. Include a “Non-functional” change category - i.e. one that is not expected to change capital
 3. Clarify batching of changes
 4. Clarify that an LCR submission does not automatically trigger a model change
 - Methodology/design changes submitted no later than 8 weeks prior to an LCR submission, only risk profile/accumulation with LCR submission
 - Benefit has not affected the last years' review yet (guidance only in force from 1/1/2020):
 - Last year 87 MMC applications received (with 53 of these in September), this year 94 (with 54 in September)
 - Expecting a lot of activity this year, had around 40 notifications of MMCs already

Improve Major Model Change Application Process

In last years' briefing we said we wanted to:

➤ **Increase efficiency of the process**

- We have updated the guidance to clarify what an application should include
- Encouraged a consistent application of the standard
 - An initial completeness check within 2 weeks with early feedback on missing information
- Released a new model change template (MCT) with extra information by risk type
 - To request less extra information and facilitate analysis of change
- Reduced number of MCT submissions from three to two
- Internally – standardisation of review, clearer process, more documentation – but more can be done

What you need to do

- Adapt your model development plans to send us any methodology/design major model changes by end June (or earlier), so that they can be approved before September
- Make COMPLETE model change applications, see checklists in guidance
- Review how changes are batched – sufficient detail to understand the movement
- Use the new MCT, in particular the waterfall charts and make sure the analysis you send us ties up with it
- Send us sufficient analysis of changes – board level material and more granular analysis
- Focus validation on the model changes – MMC application should have specific validation included
- Update model change policy in line with latest model change Guidance (effective 2019 YE)

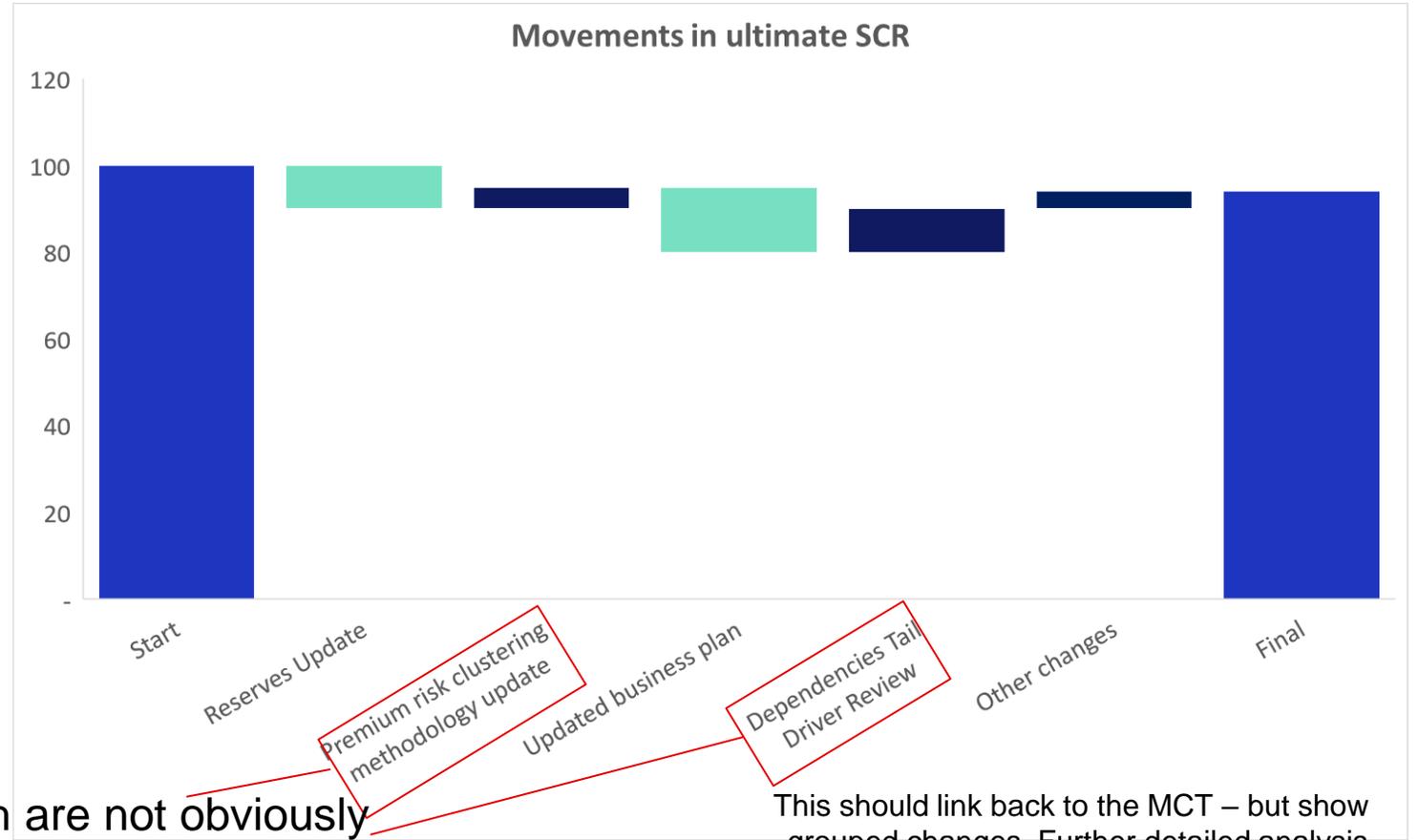
Deadlines – 31st March for model change policy and new MCT (by risk category)

What are we expecting of your submissions in 2020?

Overview

- Top down view – step back from the model
- Model changes need to be explained in terms of risk profile
- Direct our attention to the changes/movements that matter – don't let us guess

Example – board level waterfall highlighting the main changes over the year – can be produced with new MCT



Model changes which are not obviously linked to risk profile will be questioned more

This should link back to the MCT – but show grouped changes. Further detailed analysis should be more granular.

What are we expecting of your submissions in 2020?

Good analysis

- A sufficiently detailed Analysis of Change providing information to allow a technically proficient reviewer to understand the drivers of change in capital
- NOT just a few lines in LCR Form 600 – measures there show what we look at
- Explanation not description
 - What the movements in key metrics are and why they have occurred
- Validation linked to AoC

A model is just a model...

I.e. a representation of reality. You have to give outputs meaning by linking it back to risk profile.

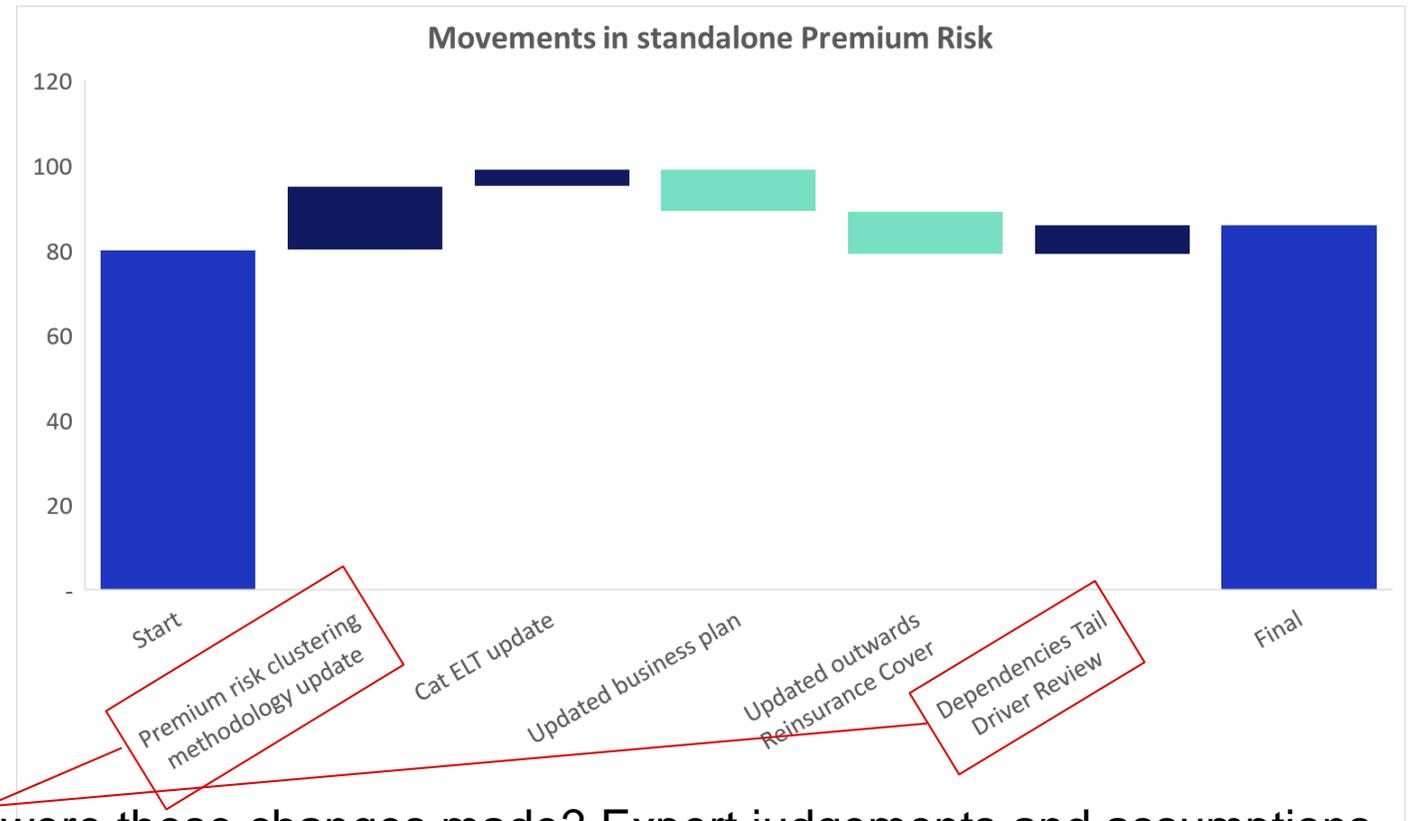


Analysis of Change: updated guidance will be provided in 2020

What are we expecting of your submissions in 2020?

Risk type analysis

- For each risk type – start drilling further
- Analysis by risk type on standalone basis – but analyse changes in contribution to capital too
- Include ratios in form 600 in your analysis → they feature in our reviews
- Reasoning esp. on parameter changes should be linking to risk profile. Not sufficient:
 - “Underwriter changed view”
 - “an extra year of good experience”



Why were these changes made? Expert judgements and assumptions involved? Validation of the changes?

What are we expecting of your submission?

Examples of Analysis of Change – individual changes

Good: Link to risk profile

Capital increased by 3% due to risk profile changes in the updated 2020 SBF. The premium risk increase relating to this was £20m, which was mainly driven by changes in class A, B and C.

In the 2020 SBF, class A has increased line sizes from £20m to £50m in line with strategy to increase market share. The parameterisation of large losses in this classes has been updated to allow for this increase in line sizes, as well as updating frequency assumptions considering increased volumes but also potential for aggregations. The associated RI programme has also been updated with higher retention, moving from £10m to £20m.

A secondary impact of this was a reduction in RI credit risk – however, the impact on capital of this was immaterial.

Given the change RI credit risk could also have increased (due to more business being written at higher line sizes) – i.e. particularly important that the movement is explained and reasoned, more details can be helpful (e.g. premium split or policy count by line size bands).

Not sufficient: Only a description of individual changes is provided

“Capital increased by 3% when the 2020 SBF was updated.”

Template like below might be helpful:

Description of change
Rationale for change
Data / risk profile / parameter changes?
Methodology changes?
IT / structural changes?
Expectation of change: total capital / risk categories (mean and 1:200, uSCR and 1-yr)
Actual impact of change
Validation performed
Supporting analysis
Governance (change made by, reviewed by, sign-off, dates)

What are we expecting of your submission?

Examples of Analysis of Change – Premium Risk by Class

Class comparison from SuppQ used in our analysis:

Class Name (in order of size by net premium)	2021 CiL				Premium Risk (Ultimate) (inc-cat)				Movement		2021 CiL	2020 CiL	Change in contribution percentile
	Net Premium	Mean Net Claims	99.5th Claims / Mean	Contribution / Mean	Net Premium	Mean Net Claims	99.5th Claims / Mean	Contribution / Mean	Mean Net Claims (%)	99.5th: mean ratio (%)	Contribution %ile to Premium Risk	Contribution %ile to Premium Risk	
1. Property Treaty	200.0	160.0	238%	136%	200.0	160.0	255%	136%	0%	-6%	83%	83%	0%
2. Casualty Treaty	100.0	80.0	374%	154%	110.0	88.0	382%	154%	-9%	-2%	82%	82%	0%
3. Marine - Cargo	90.0	72.0	436%	218%	90.0	72.0	340%	180%	0%	28%	95%	95%	0%
4. Casualty - US	80.0	64.0	264%	123%	80.0	64.0	300%	145%	0%	-12%	74%	74%	0%
5. Casualty non-US	70.0	56.0	237%	119%	70.0	56.0	245%	119%	0%	-3%	73%	73%	0%
6. D&O	70.0	56.0	532%	183%	70.0	56.0	550%	183%	0%	-3%	92%	92%	0%
7. Property Binders	60.0	48.0	413%	282%	60.0	48.0	413%	350%	0%	0%	89%	97%	-8%
8. Marine Hull	20.0	16.0	1011%	645%	50.0	40.0	1011%	645%	-60%	0%	98%	98%	0%
9. Aviation	10.0	8.0	408%	199%	10.0	8.0	420%	199%	0%	-3%	91%	91%	0%
10. Med Mal	5.0	4.0	191%	116%	5.0	4.0	200%	116%	0%	-5%	75%	75%	0%
Total	705.0	564.0	165%		745.0	596.0	178%		-5%	-8%			

Increase in 99.5th in material class

Significant decrease in 99.5th in material class

Reduction in contribution

Reduced volume with stable volatility – counter-intuitive

Any material classes with material movements will be investigated, also counter-intuitive movements.

Disclaimer – figures are dummy figures and not necessarily internally consistent.

Continual Review and Fast-track approach

Shift to more continual review to improve approval times and increase predictability of capital requirements

- Exploring possibility of a “Fast-track approach”
- Pilot for 2021 SCR reviews
 - Establish selection criteria
 - Capital “pre-agreed” if no material change in September/October

Re-vamp of the LCR forms for 2022 SCR submission

Preparation planned in 2020

Aims are:

- Incorporate the IMO information and avoid having two submissions
 - Simplify/restructure forms that are challenging for the market and/or not well-used by Lloyd's
 - Explore ways that syndicates can provide granular modelling information to avoid the Lloyd's work in understanding the difference between syndicate and central view
- CALM working group to get your views

Takeaways

Get involved

CALM Working groups

1. Reserving Thematic Tests of Uncertainty

- Review of the reserving thematic tests used in the 2020 LCR reviews, in particular the Actual versus Plan ULR test and the LCR Roll Forward test

2. 2020 LCR Guidance:

- main purpose is for market to give early feedback on draft versions of guidance, in particular highlighting difficulties with implementation or areas of ambiguity (clarity on how AoC and market risk are presented)

3. 2021 LCR Forms:

- Incorporate IMO information and avoid having two submissions
- Simplify/restructure forms that are challenging for the market and/or not well-used by Lloyd's
- Explore ways market can provide granular modelling information to aid understanding the difference between syndicate and central view

Feedback – with new SCR guidance and re-vamp of the forms now is the time to give us any feedback you have

Timeline

Three main (linked) themes: Market working groups, market communications, market guidance

Q1

- LCR guidance and Reserving Thematic Tests working groups kick off
- Capital briefing (3rd February)
- Validation critical feedback responses (21st Feb)
- IMO returns (24th Feb)
- March reassessment templates (2nd March)
- Model change policy updates and new MCT submission (31st March)

Q2

- Communication of validation thematic review outcomes
- LCR form working group kick off
- Fast track requirements communicated
- Validation briefing (30th April)
- Capital Market messages (4th June (TBC)): Setting out expectation of market movements
- Draft SCR guidance and requirements circulated for comment, finalisation in June
- Communication of syndicates selected for deep dives/Fast Track Pilot
- Launch of new Cyber and Liability exposure management scenarios
- Exposure management return on 3 new Cyber scenarios (in-force 1/1/2020 exposures)

Q3

- NED Forum (23rd Sept)
- LCR submissions begin– fast track pilot in place
- Exposure management model completeness return
- Exposure management return on 3 new Cyber scenarios and 6 new Liability scenarios (in-force 1/7/2020 exposures)
- Exposure management return on 3 new Cyber scenarios (projected exposures, with 2021 SBF)

Time for questions

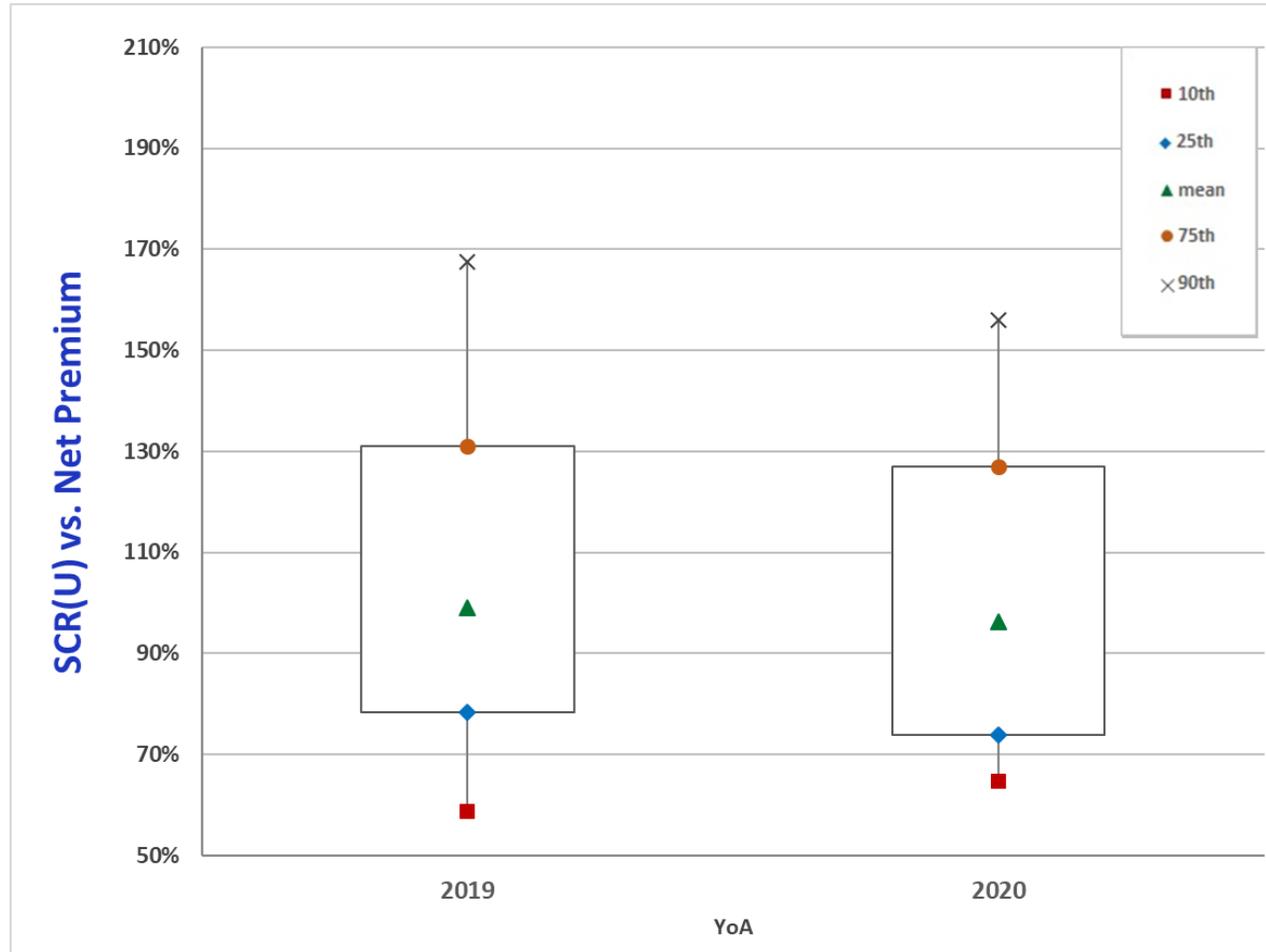
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Appendices

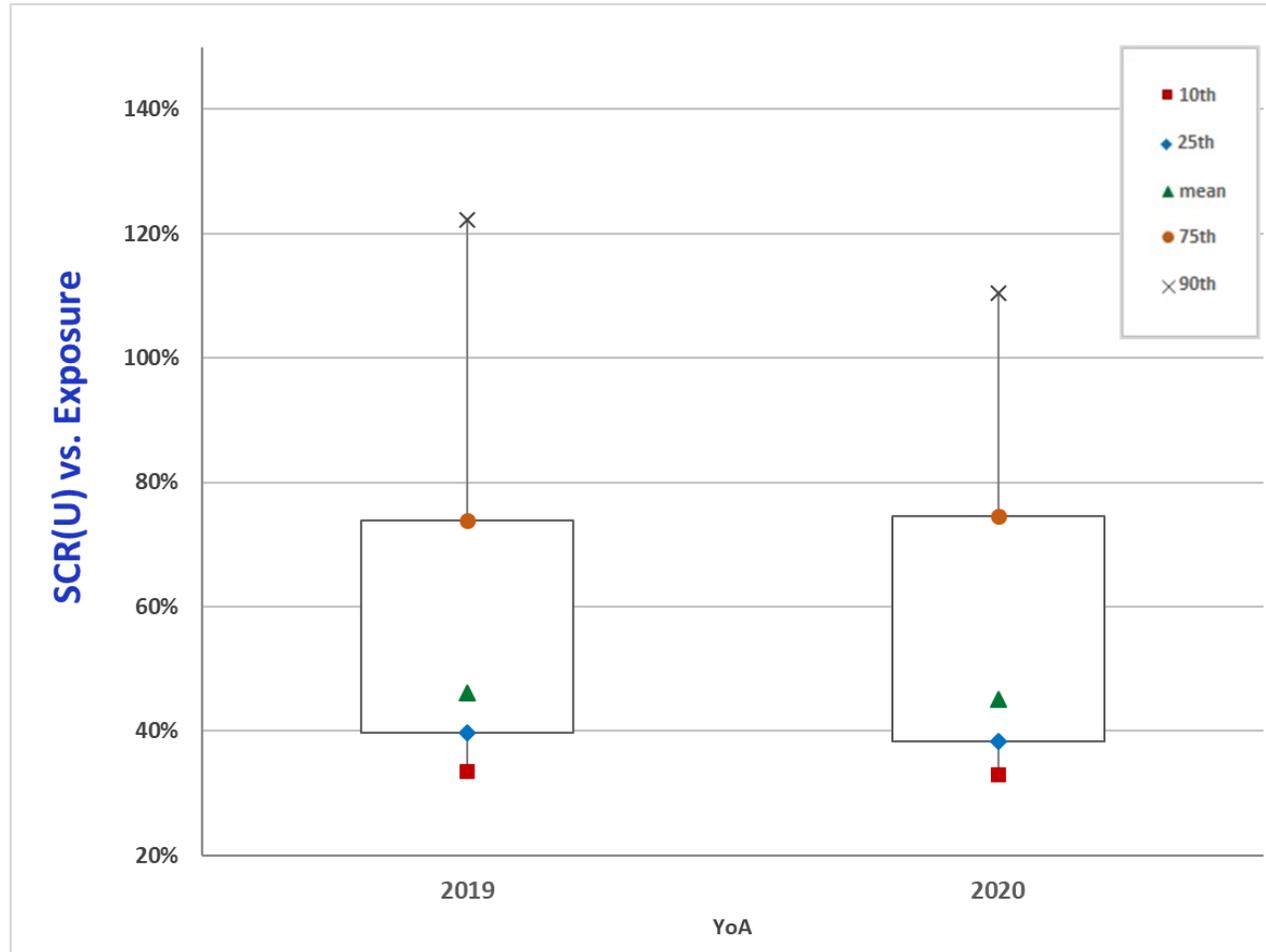
Ultimate SCR vs. net premium



Ult SCR: F309

Net PI: F313 table 1
col D row 1

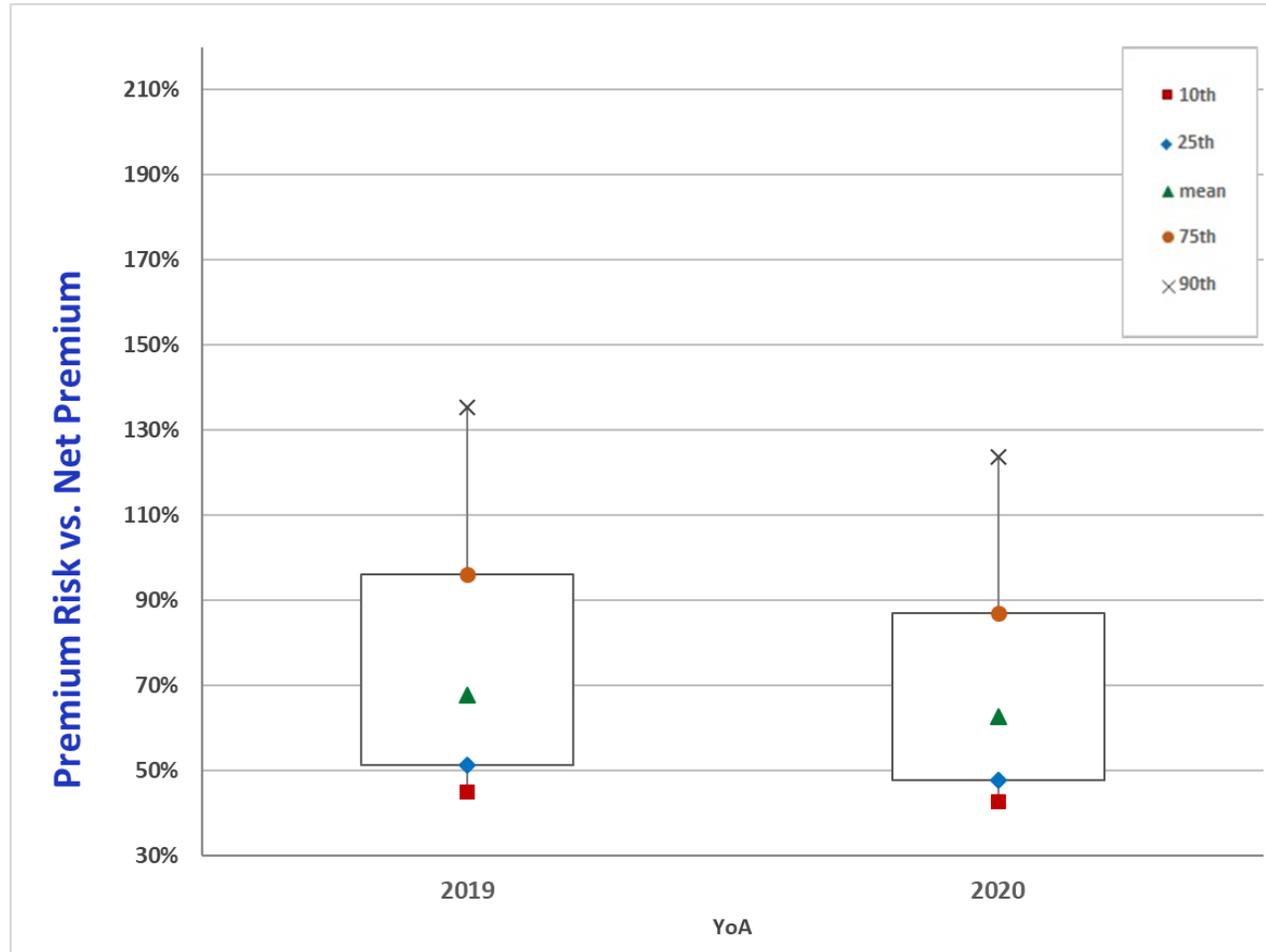
Ultimate SCR vs. exposure (net premium + 1/2 net reserves)



Ult SCR: F309

Exposure: Net PI +
0.5*Net Reserves

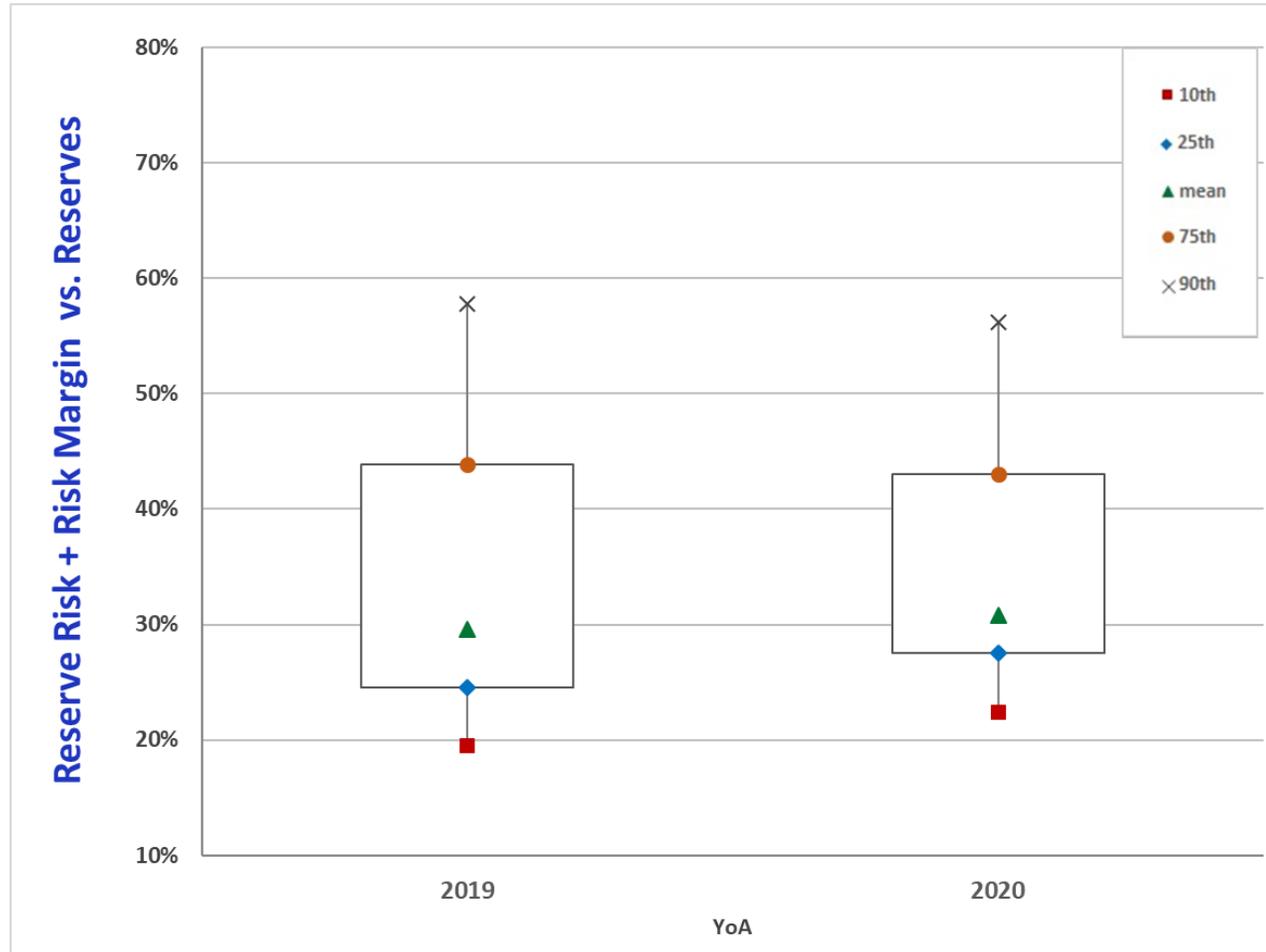
Premium risk vs. net premium



Ult premium risk (pre diversification): F309

Net PI: F313 table 1 col D row 1

Reserve risk + risk margin vs. reserves

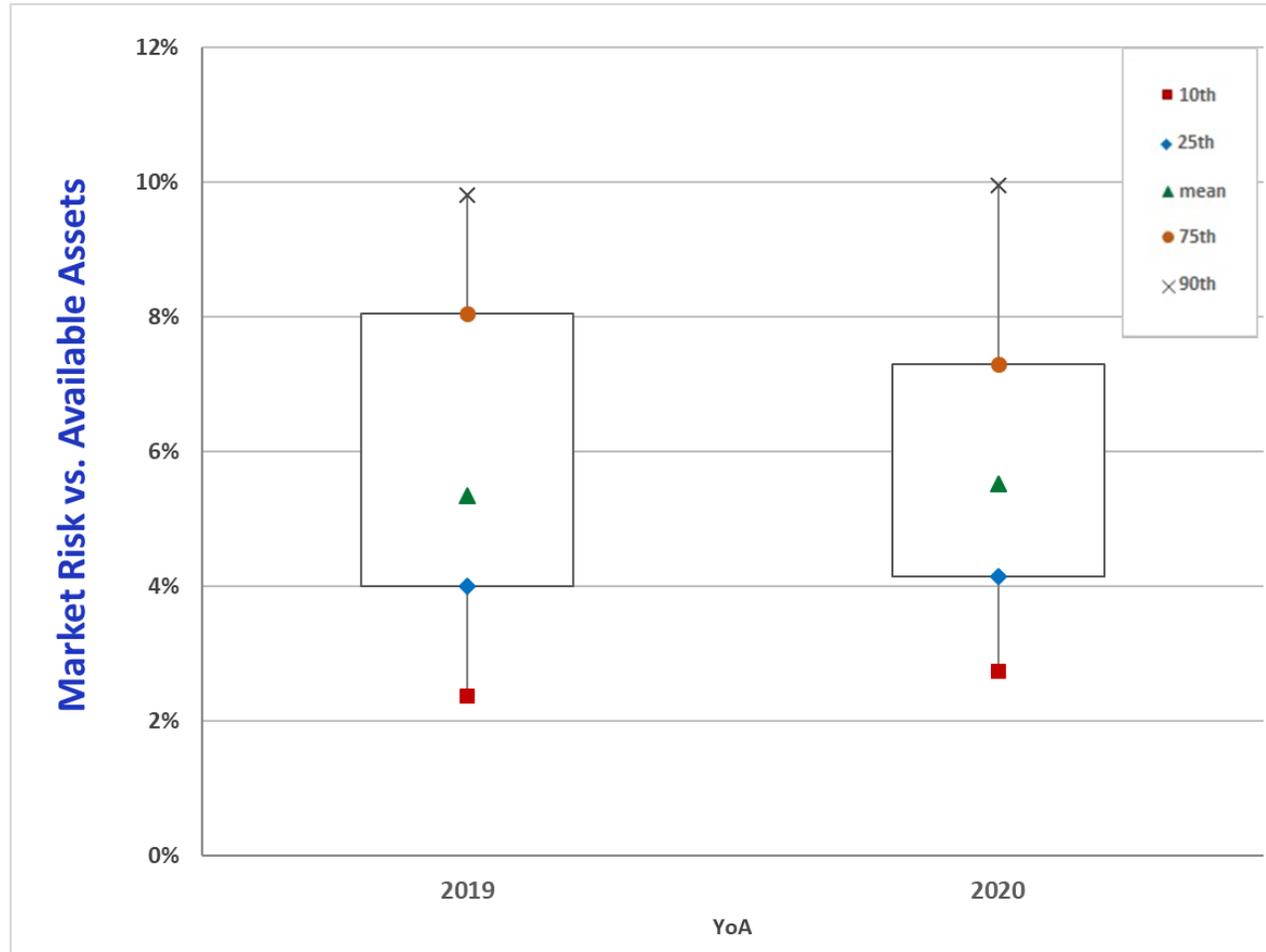


Reserve risk (pre Diversification) F309

Risk margin: F312 col P total

Net Reserves: F312 cols H+I-J Total less Proposed YOA

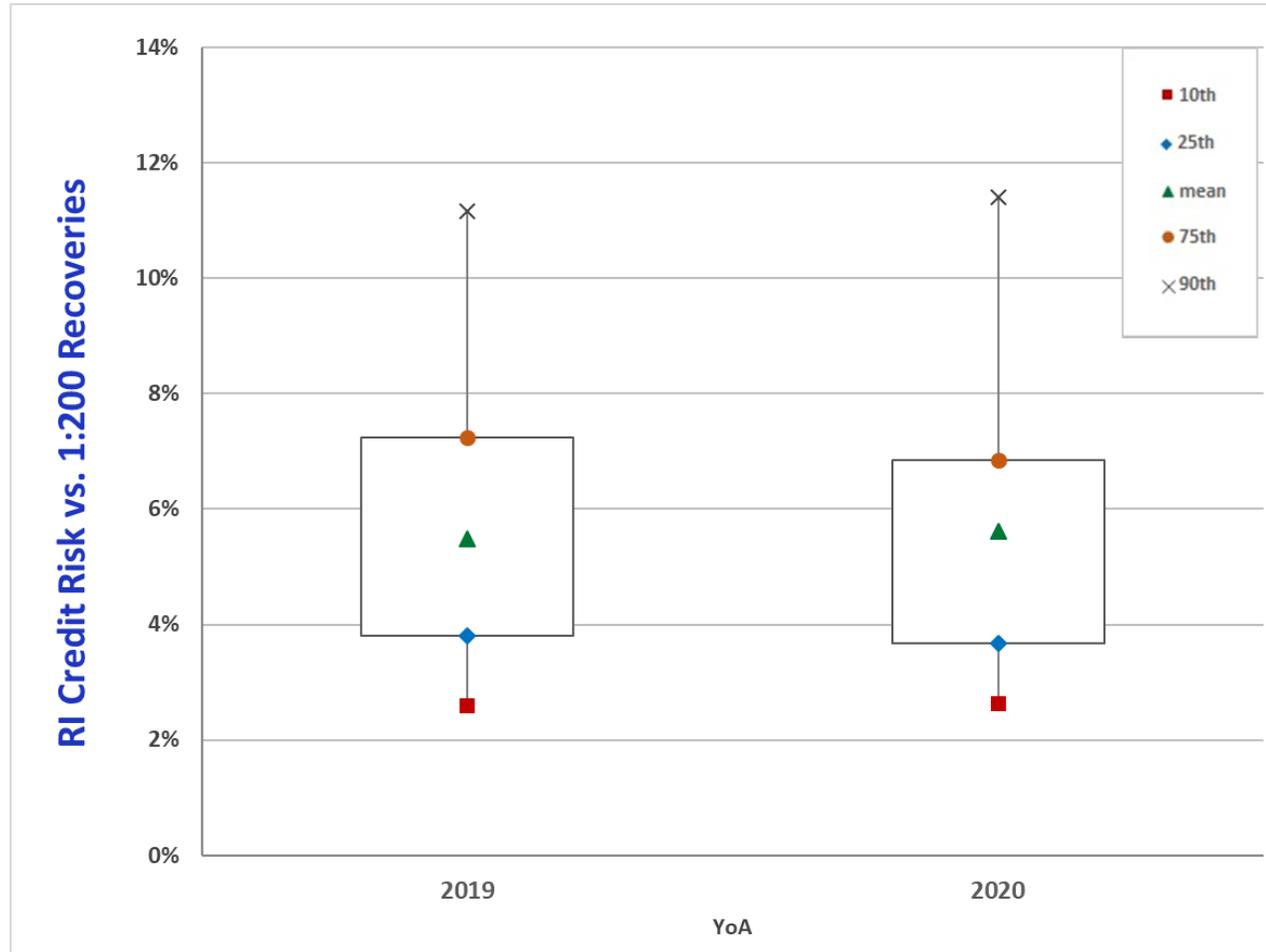
Market risk vs. available assets



Market risk (pre Diversification): F309

Available assets:
F312 col Q Total less
Proposed YOA + F313
table 1 col D row 1

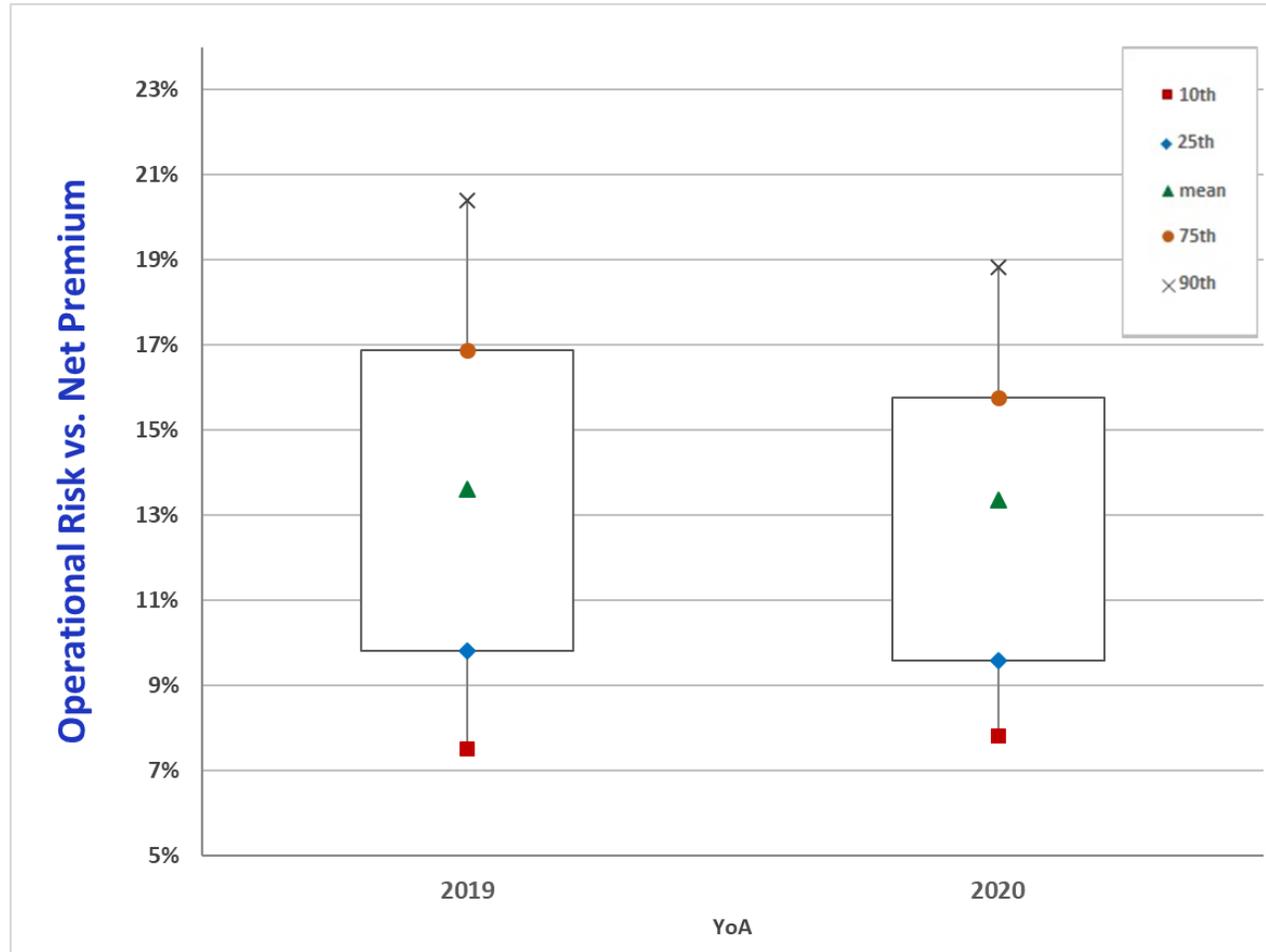
RI credit risk vs. 1:200 recoveries



RI credit risk (pre Diversification): F309

1:200 Recoveries (approximated): F311 table 1 col G row 4 less row 3

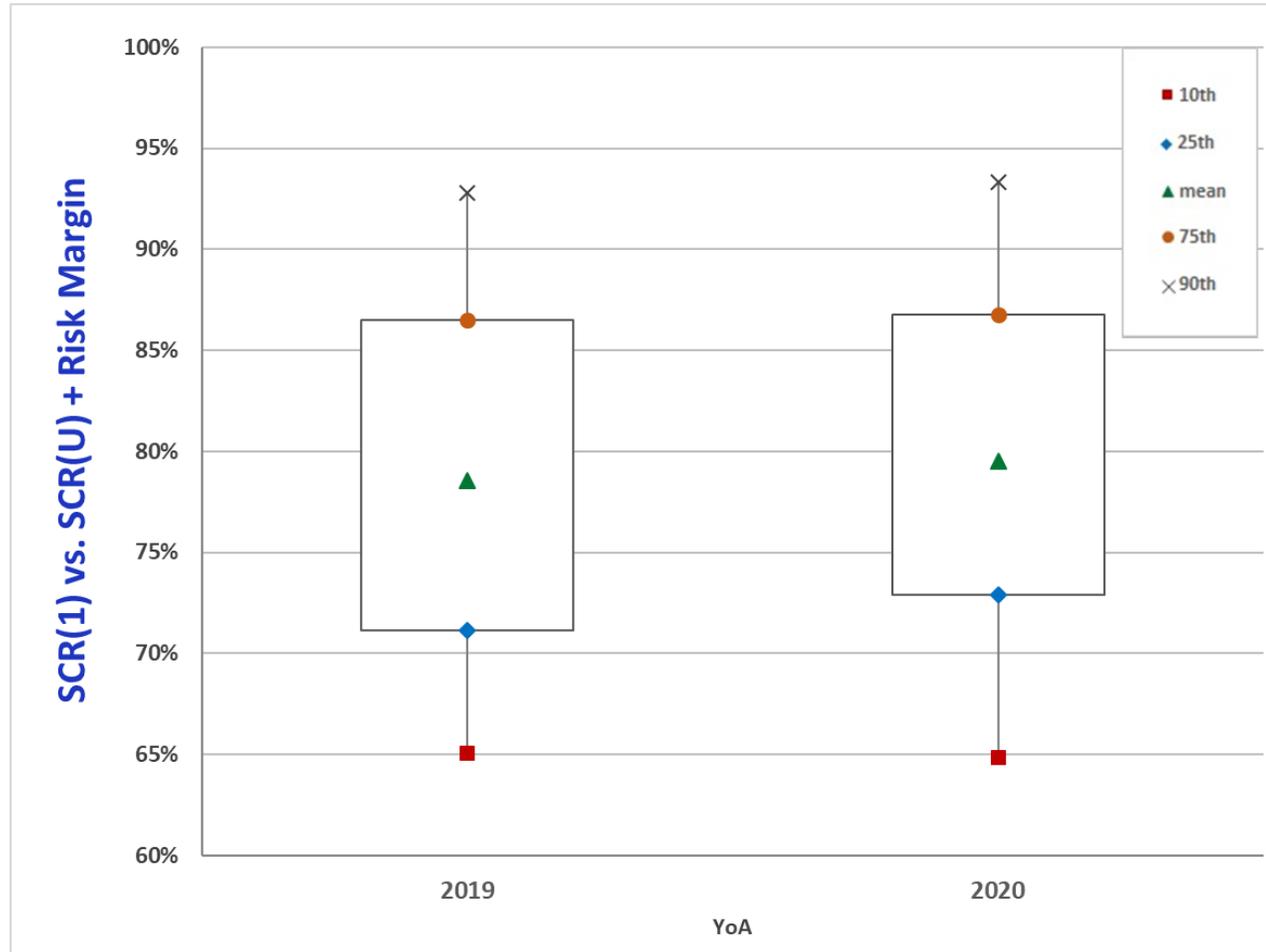
Operational risk vs. net premium



Operational risk (pre Diversification): F309

Net PI: F313 table 1 col D row 1

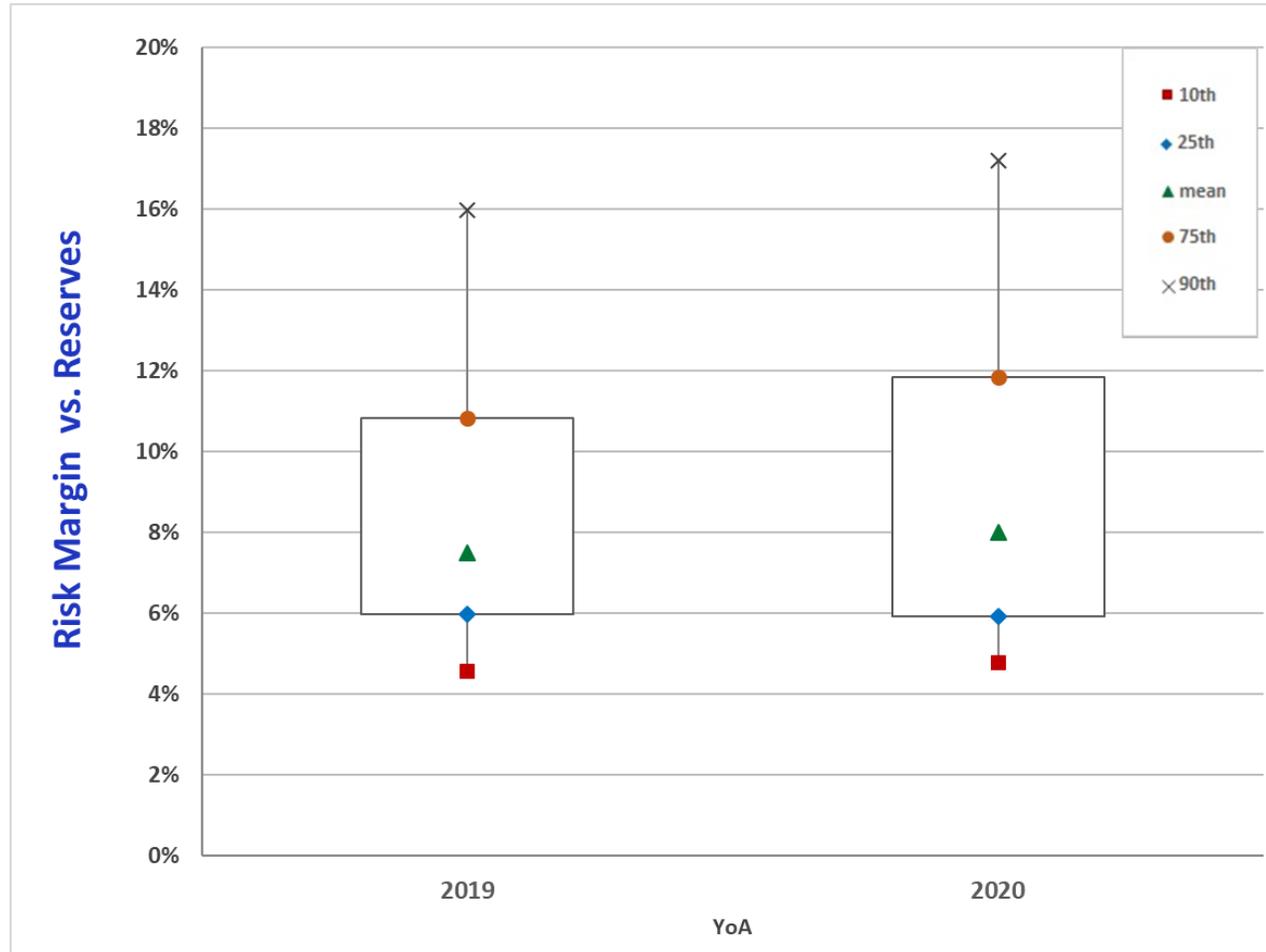
SCR(1) vs. SCR(U) + RM



Ult SCR: F309
1Yr SCR: F309

Risk margin: F312 col
P total

Risk Margin vs. Reserves

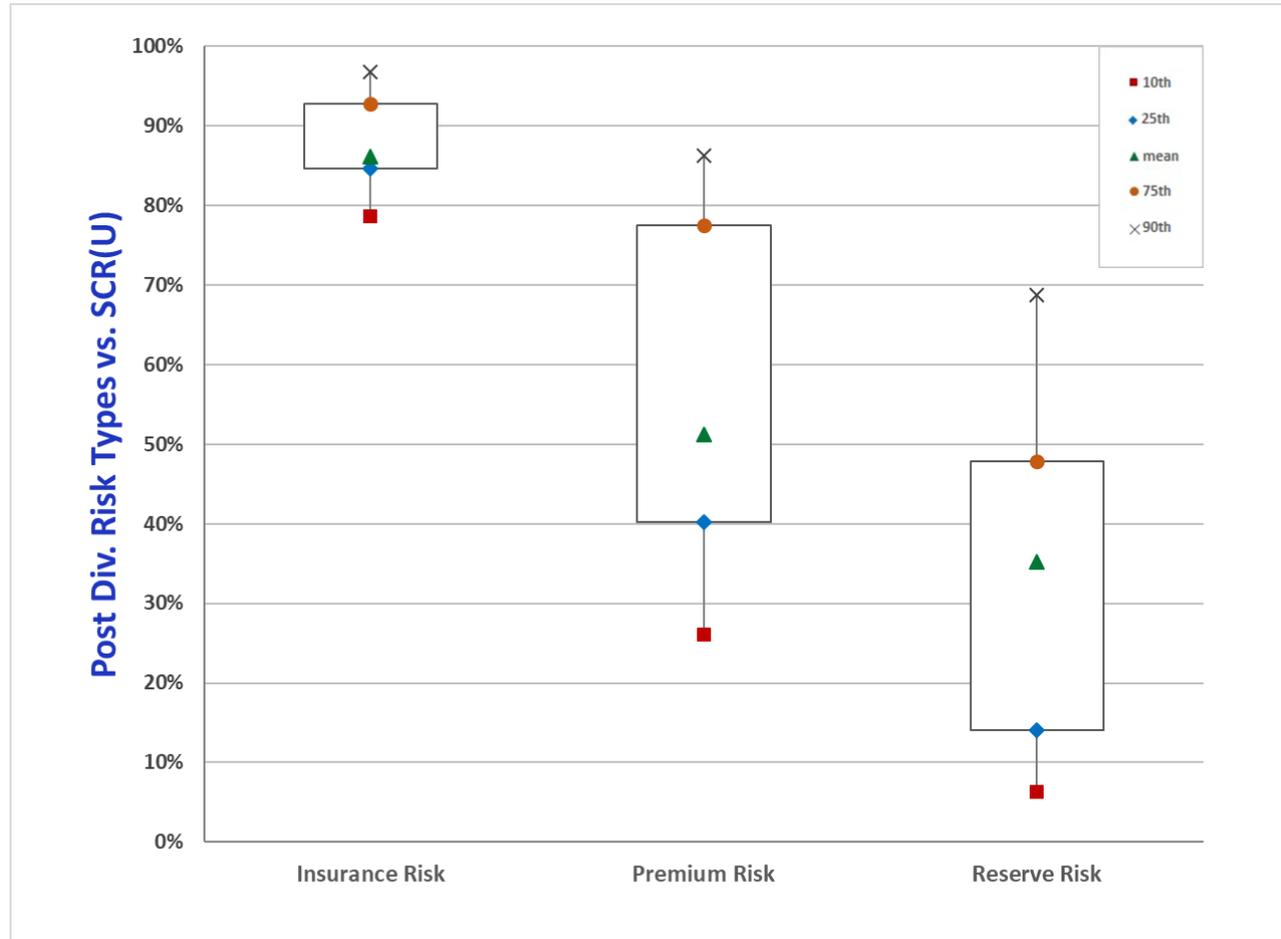


Risk margin: F312 col P total

Net Reserves: F312 cols H+I-J Total less Proposed YOA

Post Diversified Risk Types vs. SCR(U) part 1

Note: Amounts are pre-loadings

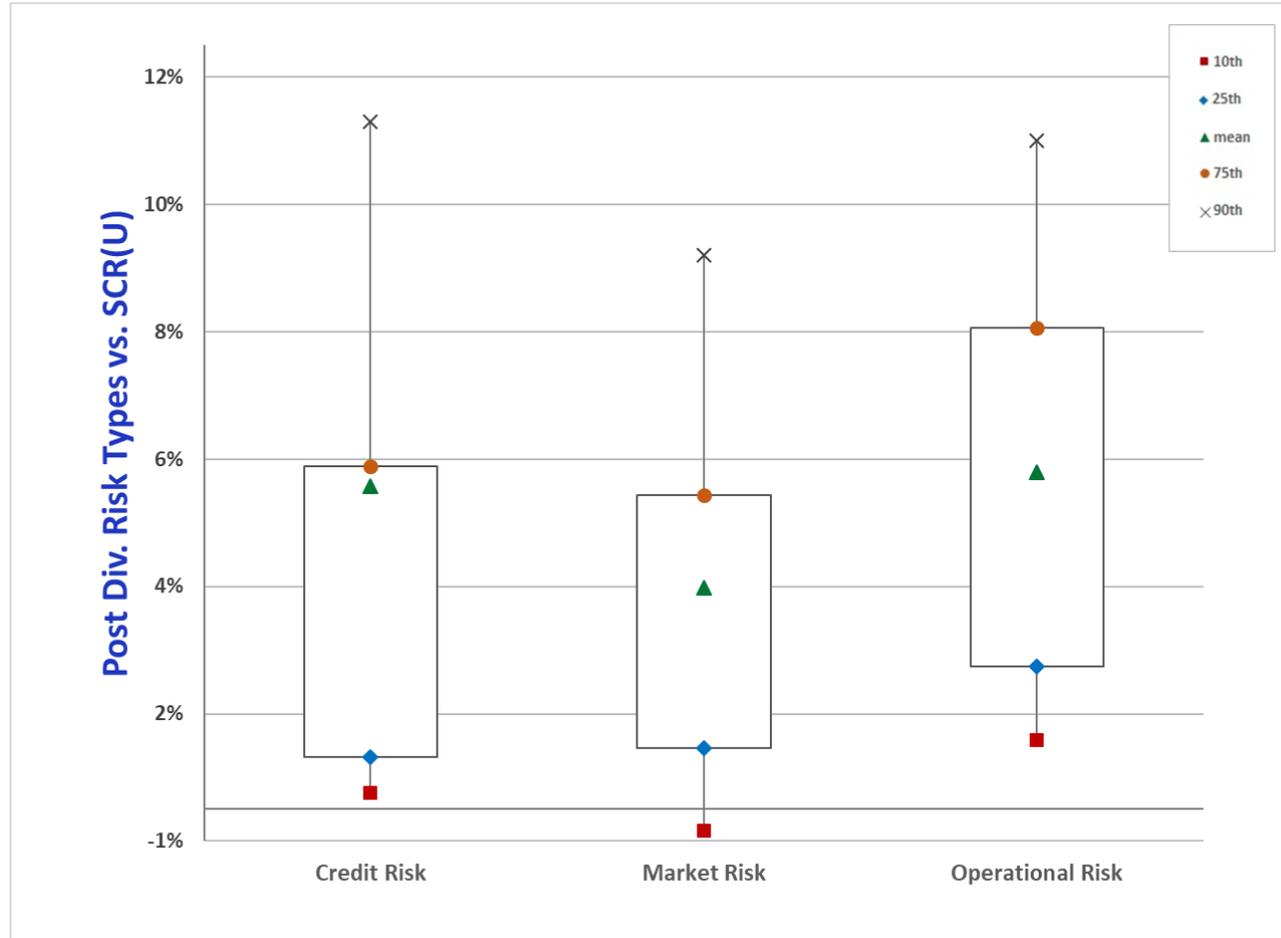


Post Div. Insurance Risk & Ult. SCR : F309

Post Div. Premium & Reserve Risk: F541

Post Diversified Risk Types vs. SCR(U) part 2

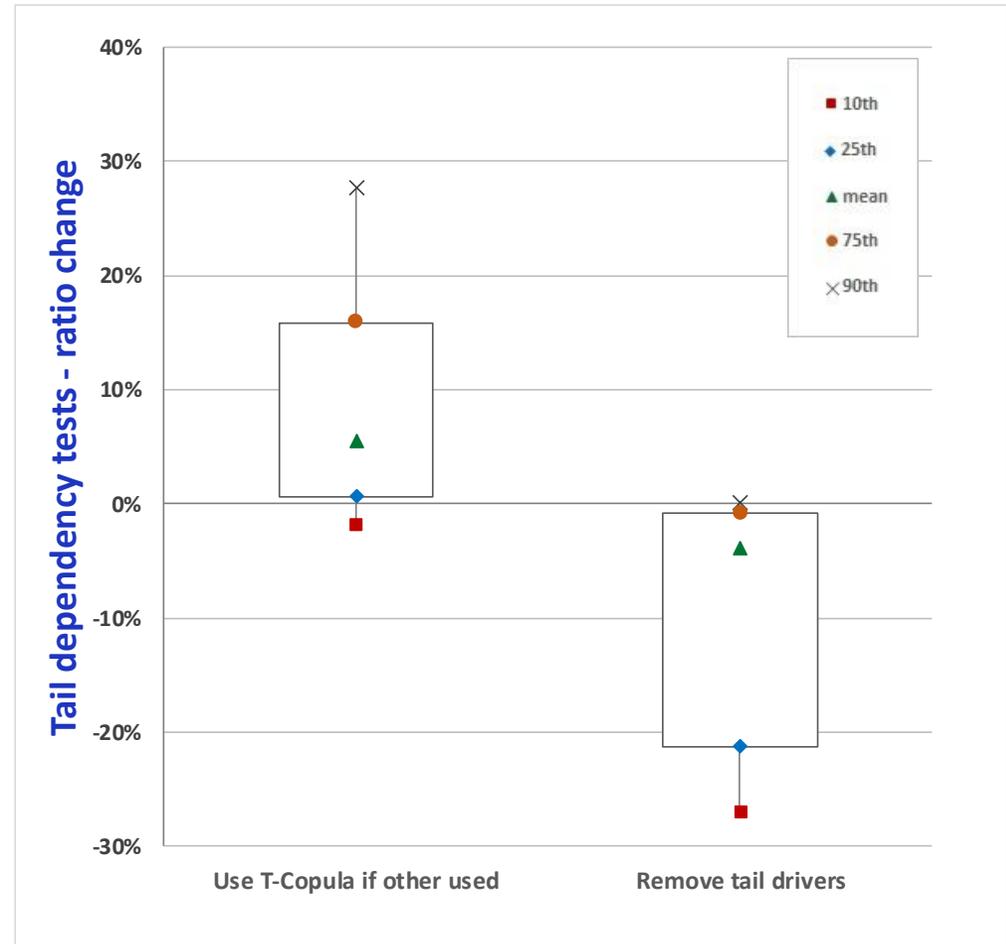
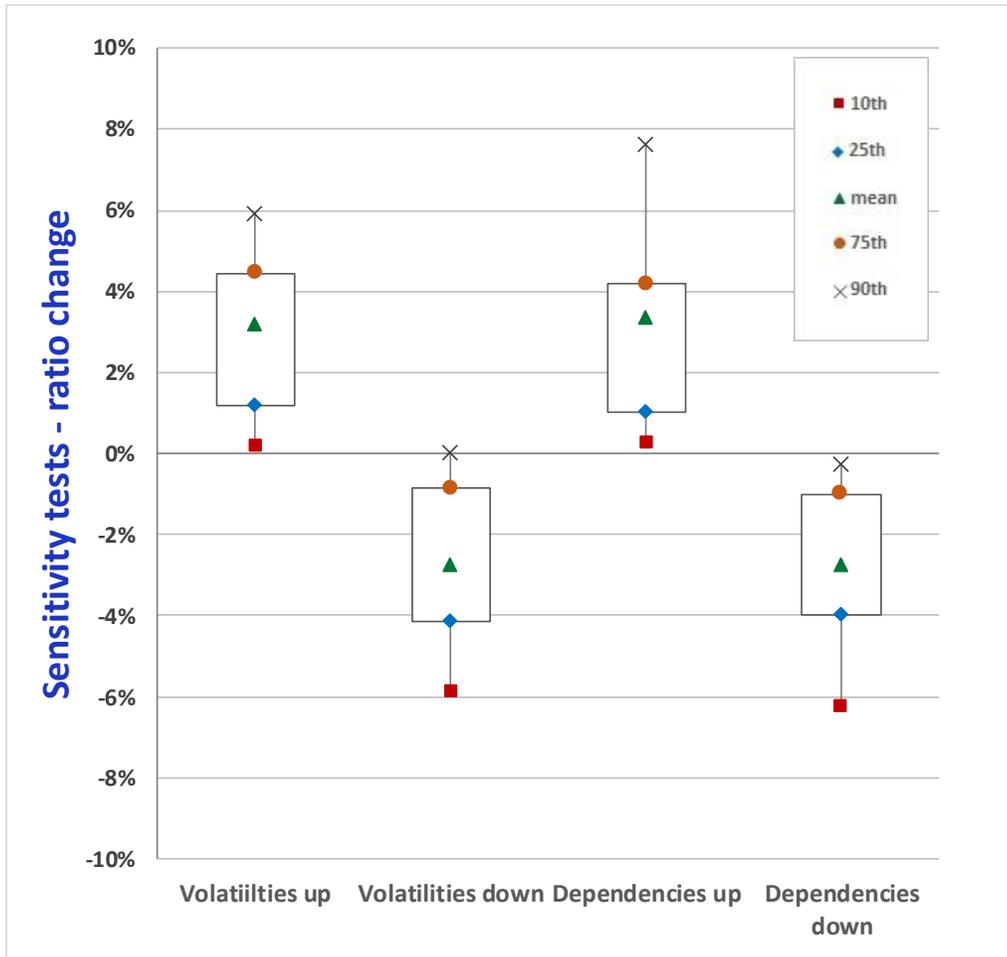
Note: Amounts are pre-loadings



Post Div. Credit,
Market Operational
Risk & Ult. SCR : F309

Sensitivity tests - ratio change

Please note: The impact of the tail drivers will be subject to further investigation going forward



Data taken from returns provided in May 2019