

# **CRO PANEL: Perspectives on ERM**

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# Enterprise Risk Management: Potential Issues

- Key word is “Enterprise”
  - i.e. look at the whole company, both sides of the balance sheet
- Two potential key issues:
  - Consistency between different sides of the balance sheet
    - i.e. liabilities vs. assets
  - Possible interactions between risks on the liability side & asset side

# Consistency of risk/reward

- Corporate Bonds
  - Spread: OAS = Option Adjusted Spread
  - Microsoft (AA+) 5 year bonds: OAS = 20 bps
- Cat Risk
  - ROL= ?

# Consistency in assessing tail risk

- Cat risk
  - 100+ years of historical data
  - Assess 100 yr/250 yr PMLs
- Asset risk
  - Most widely used risk model
  - Looks at 3-5 years of data (recency bias)
  - Exponentially weighted (more recency bias)
  - Assumes normal distributions with mean/covariance framework
  - 2008 crisis is already a distant memory,

# Potential for Interactions

- How might asset side & liability side interact?
  - i.e. both get hit at the same time, double-whammy
- What external factors could negatively impact both?
  - Is correlation approach the best?
  - Event/scenario driven approach?

# Asset/liability sides of the B/S

- Life Insurers in 2007-2009 Credit crisis
  - Some got hit on both sides of B/S
    - A few took TARP Money
  - Assets: structured/”risky” bonds
    - Embedded equity market risk
    - CDOs etc.
  - Liabilities: Variable annuities and similar products
    - Embedded equity market risk
    - Effectively sold equity put options to policyholders
    - Risk not fully hedged

# Example: Stock Price History



# Could P/C (re)insurers be hit with a double-whammy?

- What are some potential candidates?
- Cat risk and Muni bonds?
- Inflation?
  - Inflation sensitive liabilities
  - Nominal bonds
- Surety insurance and corporate bonds
  - Enron scenario