Lloyd’s and Bermuda

Casualty Actuarial Society – Reinsurance Seminar

3 June 2019

Quick introduction

- **PwC UK Non-life Actuarial Leader**
- **Ex-Head of Actuarial Services at Lloyd's**
- **Over 20 years market experience**

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Agenda

- A Brief History of Lloyd's
- Recent Performance
- Current Landscape
- Regulation inc. Brexit
- What about the Future…….
- Q&A

A Brief History of Lloyd’s

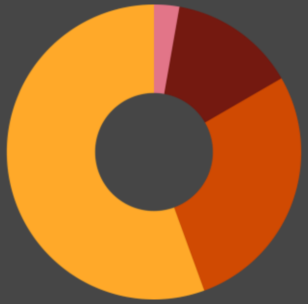
What is Lloyd’s

….. Lloyd’s is a marketplace

- Lloyd’s is not an insurance company. It is an insurance market of members
- Started in 1688 In Edward Lloyd’s Coffee Shop
- These members join together as syndicates to insure risks in return for receiving premiums
- The Lloyd’s market is the world’s leading specialist insurance market, and insures the world’s newest and most complex risks – offers bespoke services
- The syndicates underwriting at Lloyd’s form one of the world’s largest commercial insurers and a leading reinsurer
- Lloyd’s accounts for more than half of

“The London Market”…….

What exactly is the "London Market"? *



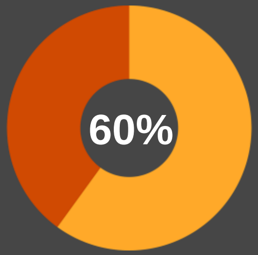
It is the largest global centre for commercial and specialty risk

52,000 interconnected risk professionals

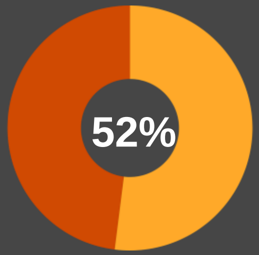
On average, the London Market pays $100m of claims on a daily basis

Accounts for 28% of global cyber insurance premiums

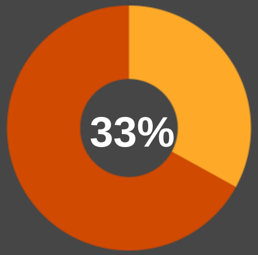
Over $91 billion of Gross Written Premium



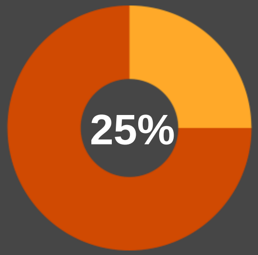
Aviation:
60% global market share



Energy:
52% global market share



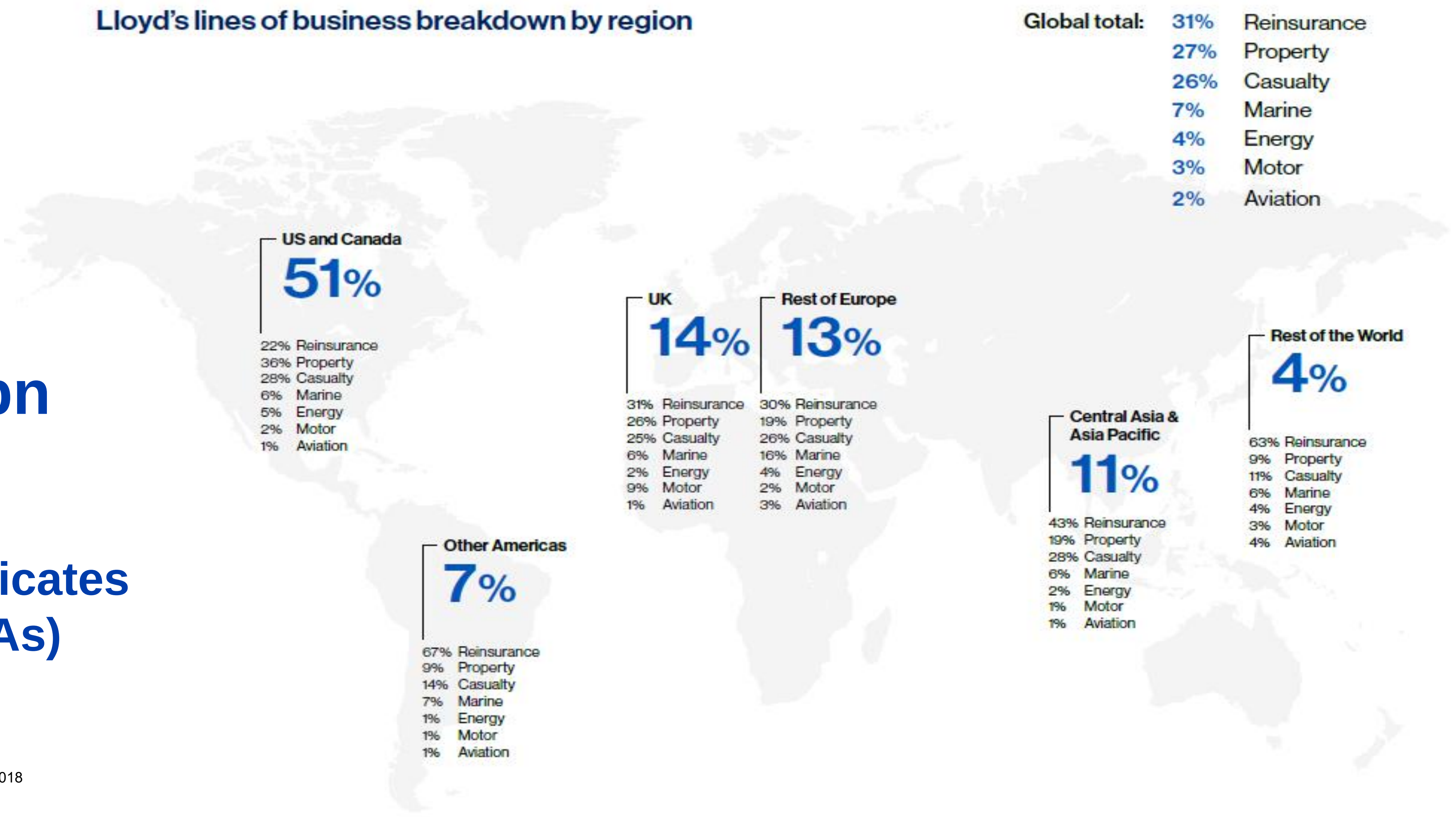
Marine:
33% global market share



The London Market accounts for 25% of the City of London's GDP

* All data from London Matters reports

And what does Lloyd's look like today?

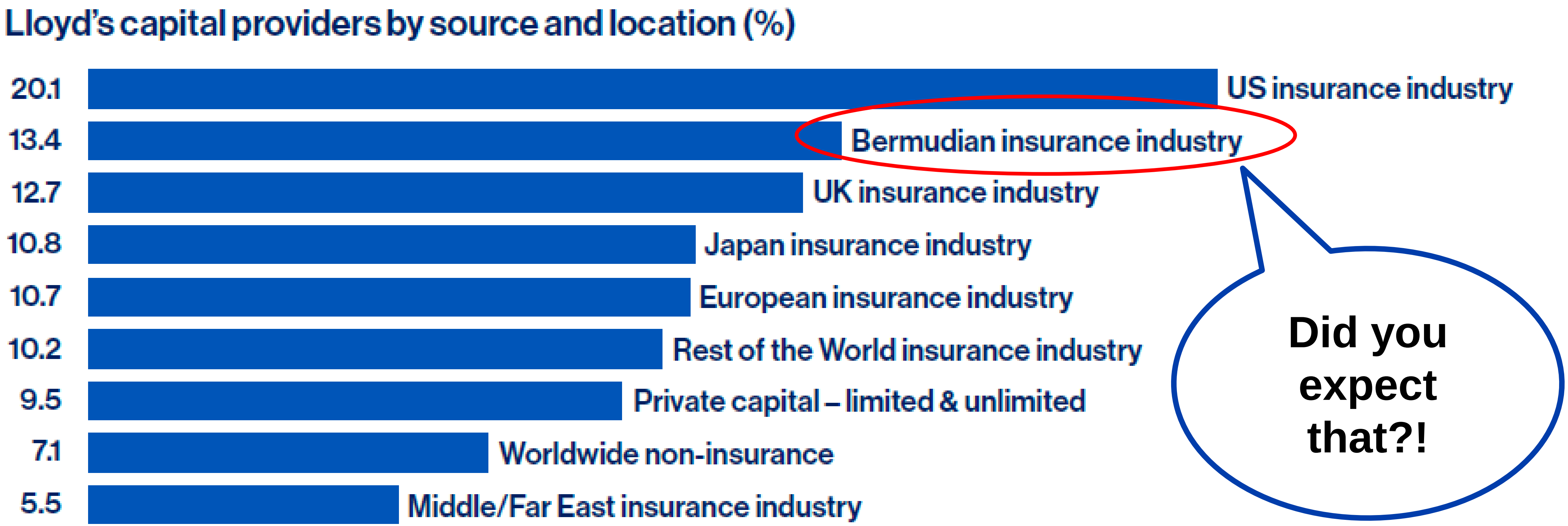


£35.5bn GWP

99 Syndicates (inc. SPAs)

Notes: Based on GWP
Source: Lloyd's Annual Report 2018

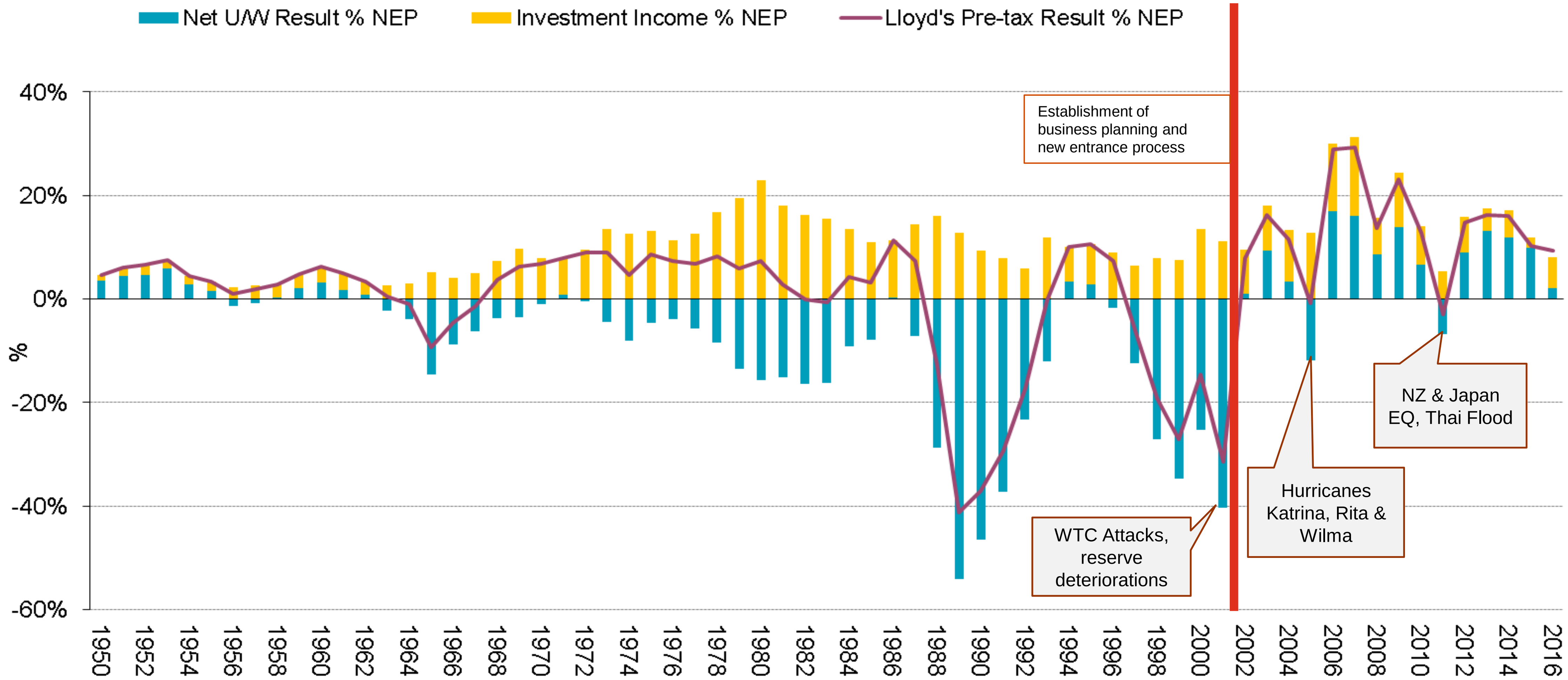
No longer individual “names”…..so who does back Lloyd’s?



Source: Lloyd’s Annual Report 2018

Recent Performance

Since 2001, Lloyd's has successfully focused on underwriting profit…



Major losses: Hurricane Betsy (1965), 1974 Super Outbreak 148 tornados in one day, Piper Alpha (1988), Hurricane Hugo (1989), the San Francisco Earthquake (1989), Exxon Valdez (1989) North European storms (1987 and 1990), Typhoon Mireille (1991), Hurricane Andrew (1992), Northridge Earthquake (1994) , WTC (2001), Hurricanes Charlie, Francis, Ivan (2004), Hurricanes Katrina, Rita, Wilma (2005), New Zealand, Chile Earthquake (2010), New Zealand, Japan Earthquake, Thailand Flood (2011)

Source: Lloyd's Annual Reports, Statistics relating to Lloyd's 2001; Lloyd's data for 1950 – 1999 on three year accounting from 2000 onwards on annual accounting basis.

…but recent years have been challenging

2018 for Lloyd's has had another "poor" performance year

	2014	2015	2016	2017	2018
Pre-tax result (£bn)	3.0	2.1	2.1	(2.0)	(1.0)
Combined ratio	88.4%	90.0%	97.9%	114.0%	104.5%
Investment return	2.0%	0.7%	2.2%	2.7%	0.7%
Gross written premiums (£bn)	25.3	26.7	29.9	33.6	35.5
Net resources (£bn)	23.4	25.1	28.6	27.6	28.2
Pre-tax ROC	**14.1%**	**9.1%**	**8.1%**	**(7.3%)**	**(3.7%)**

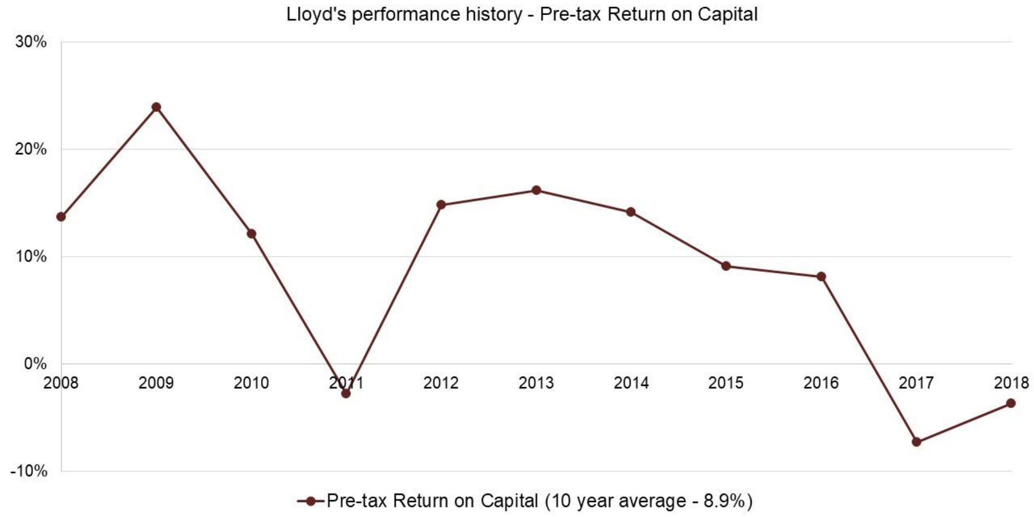
5 year average	**3.4%**
10 year average	**7.3%**

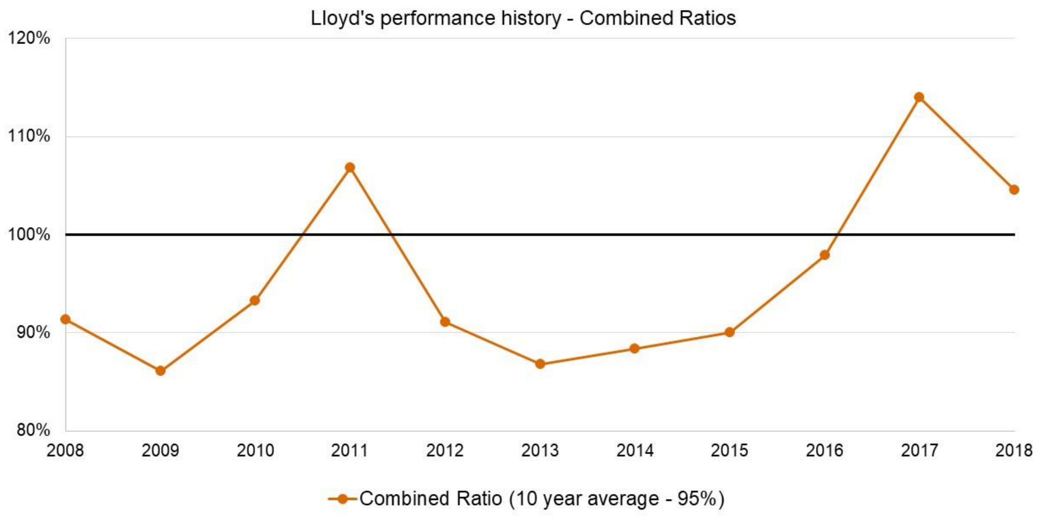
Source: Lloyd's 2018 Annual Results, Analyst Presentation

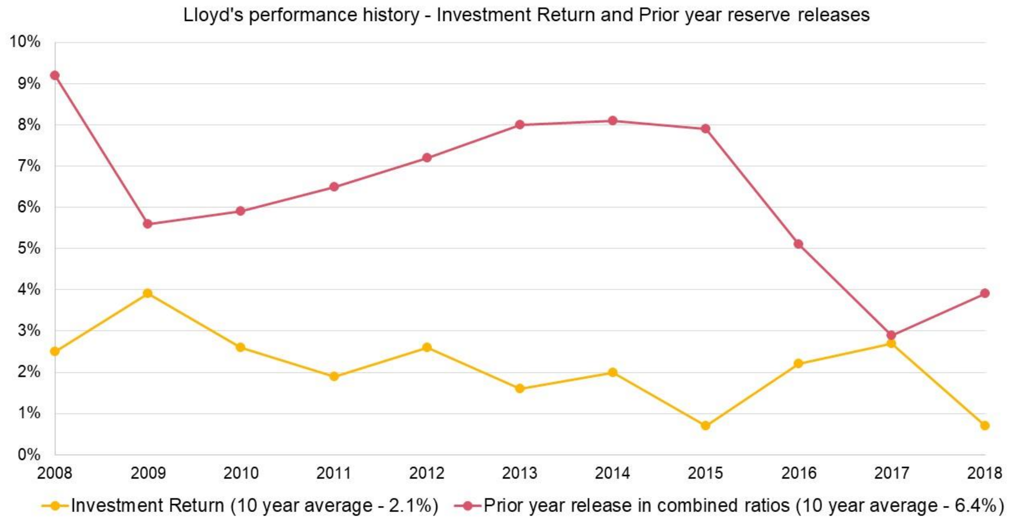
2018 performance

Lloyd's has had another challenging performance year

- A combination of soft market conditions, greater than average major losses activity and poor equity returns has meant that Lloyd's has had worse than an average performance year
- In the last 10 years, the Pre-tax Return on Capital in particular has been volatile





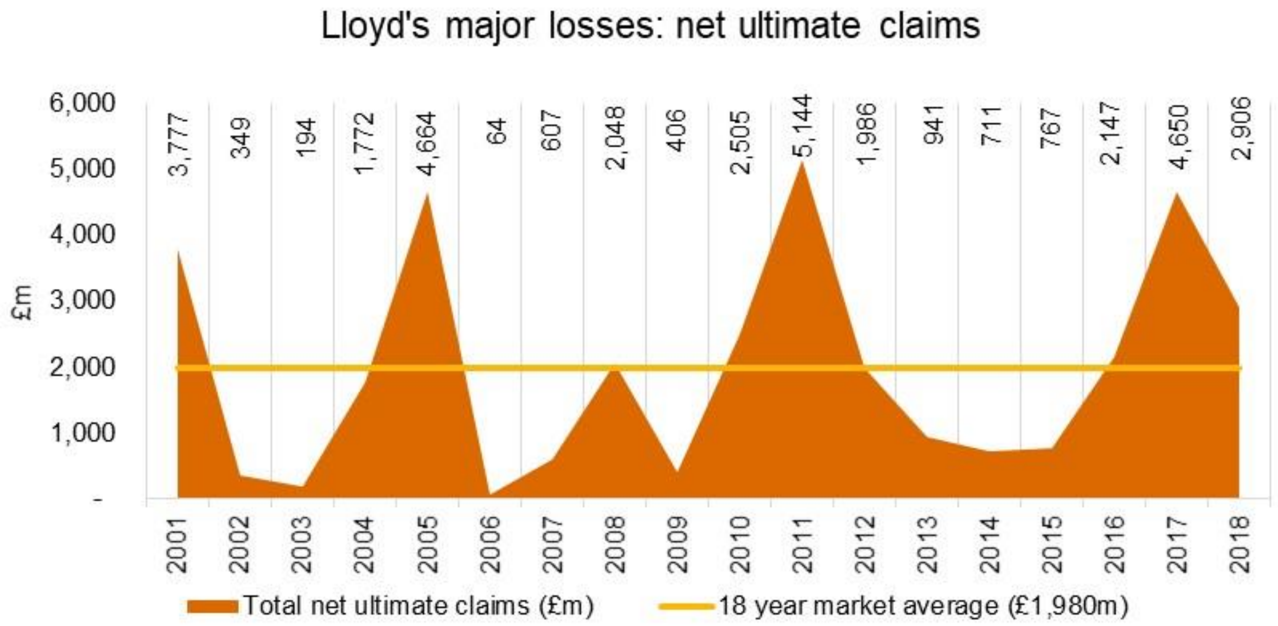


Source: Lloyd's analyst results presentations

Major losses experience

2018 was another adverse major loss events year resulting in £2.9bn of cat claims

- £2.9bn of major claims in 2018 were a significant driver of the overall loss made by Lloyd’s
- Lloyd’s has now experienced three consecutive years of poor major losses experience, albeit the impact on 2018 (11.6%) was lower than on 2017 (18.5%)
- The major losses impacting the 2018 year included:
  - Hurricane Michael (£800m)
  - California Wildfires (£700m)
  - Hurricane Florence (£500m)
- Approximately **70% of Syndicates** (excl. life and run off) have a **combined ratio that is greater than 100%** with majority being in the 100-120% range

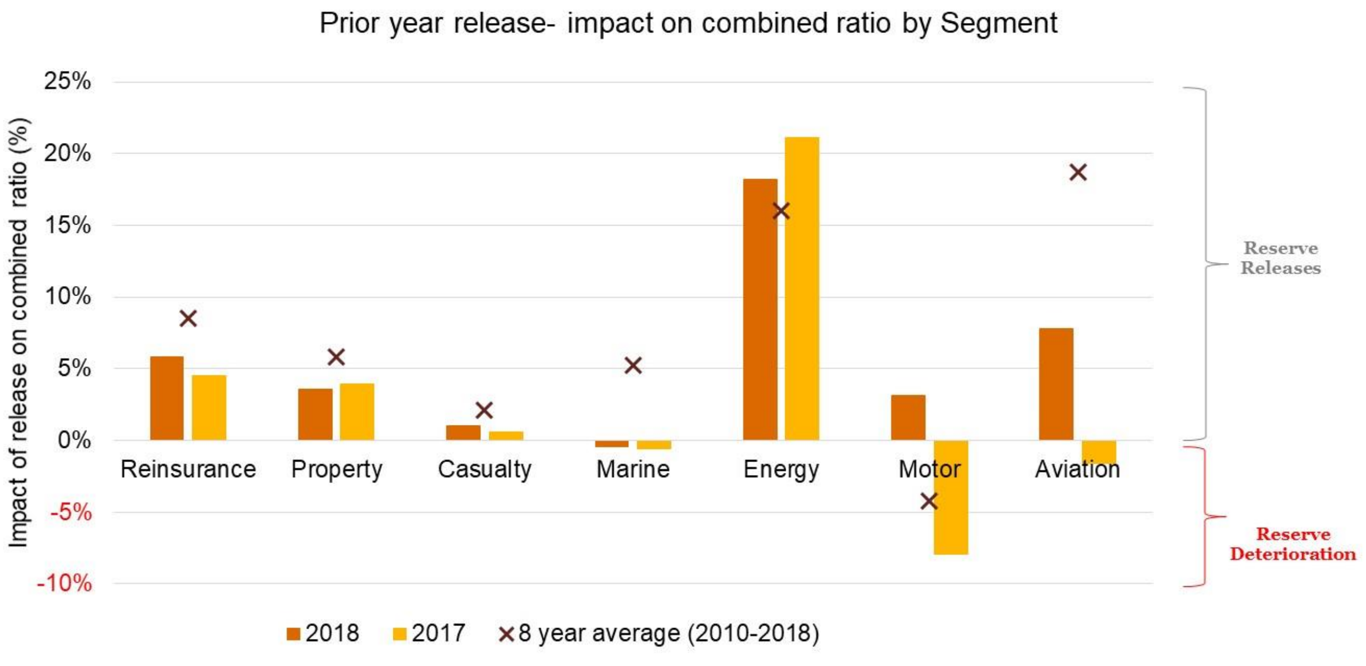


Source: PwC analysis of Lloyd’s year end results

Prior year reserve releases have actually increased

Lloyd's has seen an increase in prior year releases from 2.9% to 3.9%........

- The increase in prior year release is driven by most lines with the exception of Energy and Property
- Reserve releases were seen on all segments except Marine in 2018
- Lloyd's view is that there is over-reserving in short-tailed classes compensating for under reserving in some long-tail classes.
  - This is consistent with PwC's view
- Whilst the market continues to see reserve releases:
  - these are significantly below the recent average;
  - And are consistent with a reduction in reserve strength



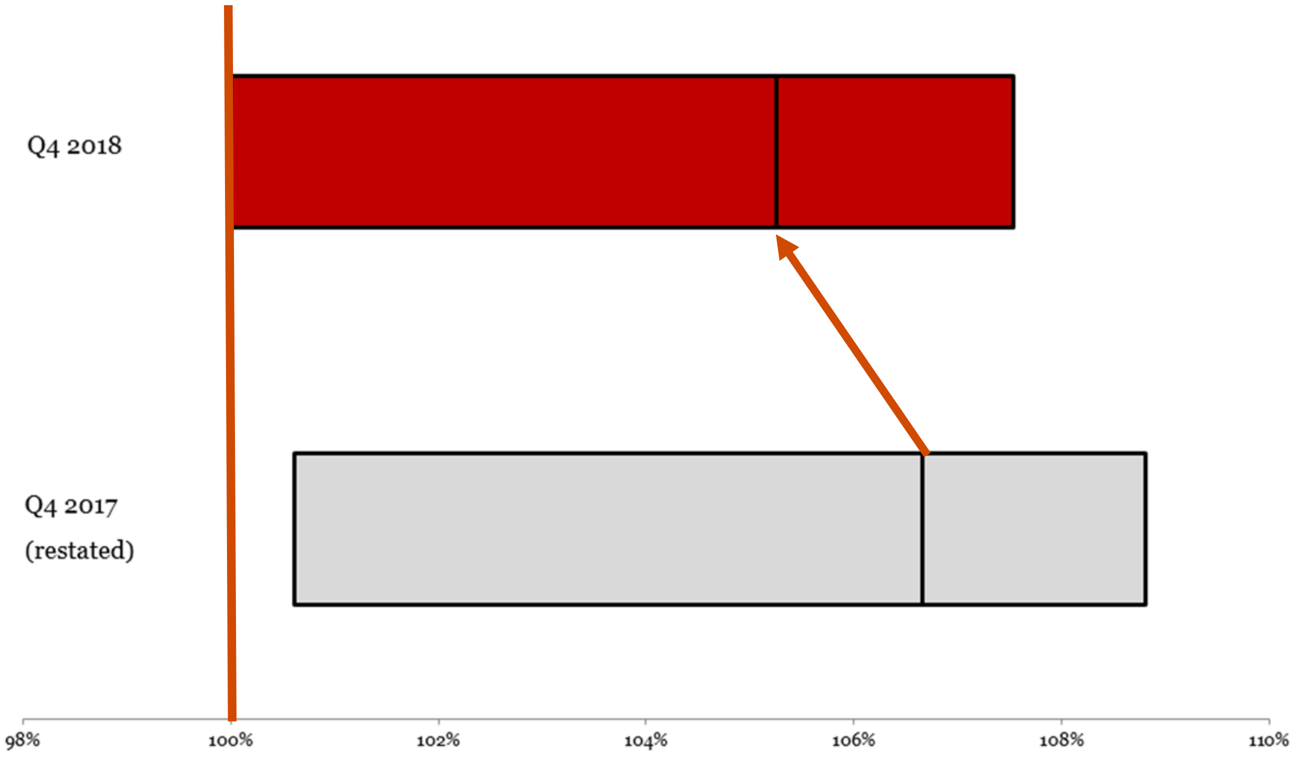
Source: PwC analysis of Lloyd's year end results between 2010-2018

Prior year reserve releases have hit reserve strength

….seen a decrease in reserve strength from over 6% to approximately 5%

- The level of margin within reserves has reduced
- The number of firms with “no margin” has increased.
  - Note: these may be part of a group and margin held “elsewhere”
- The boxes are the interquartile ranges and the lines the median
- **This does not mean the Market is under reserved** but future reserve releases are now less likely, especially in magnitude
- The most recent years of account have less margin than older business

PwC view of London Market reserve strength (adjusted for Ogden and cat)
(Net booked reserves as a proportion of actuarial best estimate)



Source: PwC analysis

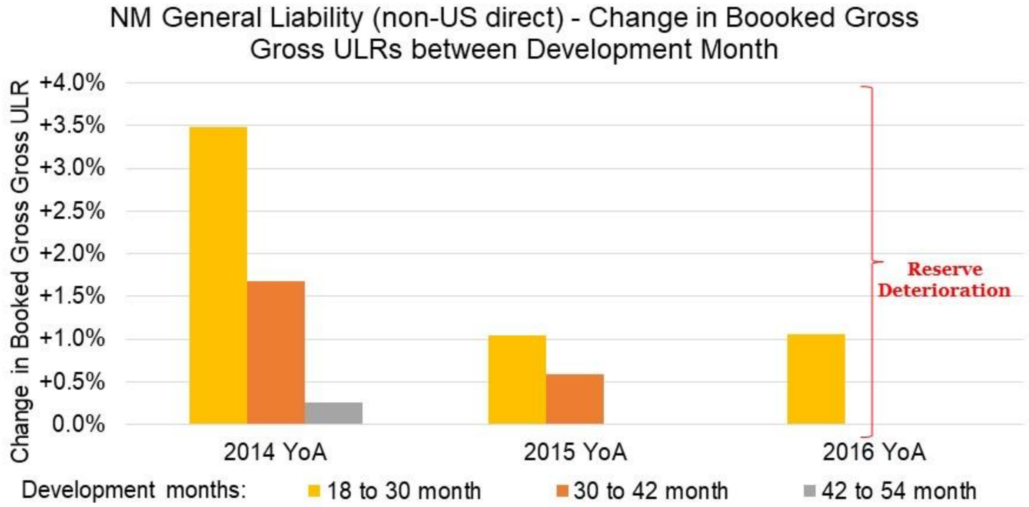
Prior year reserve releases are not across all classes

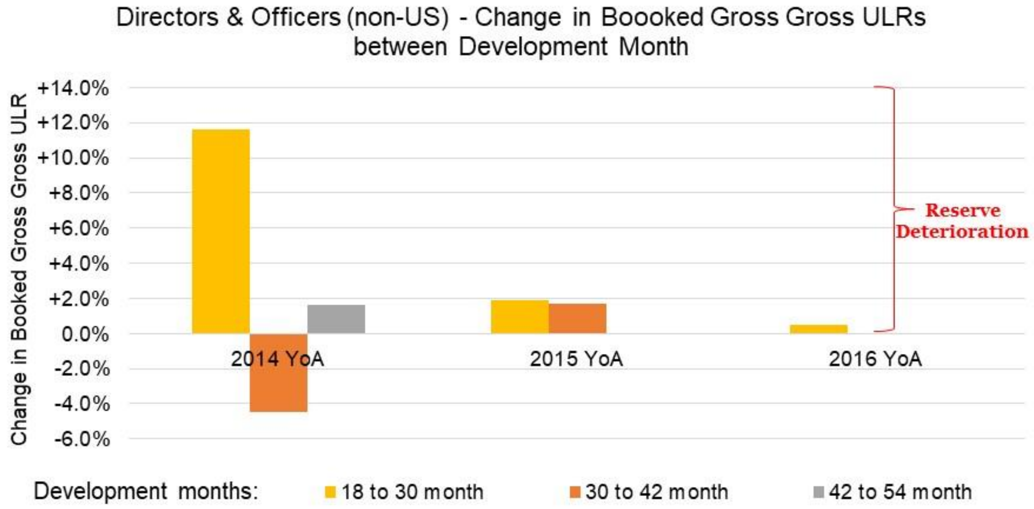
"Casualty" has had a reserve releases but underlying this is some adverse experience……

- For Casualty, albeit there is an overall reserve release, our analysis has highlighted significant reserve deterioration on some material lines such as
  - NM General Liability; and
  - Directors & Officers (non-US)

  [Note: These are not the only lines to show this!]

- This is in line with analysis performed by Lloyd's that found that Casualty classes have not developed in line with reserving assumptions
  - In Casualty Lloyd's has seen constant strengthening on recent years offset by releases on back years

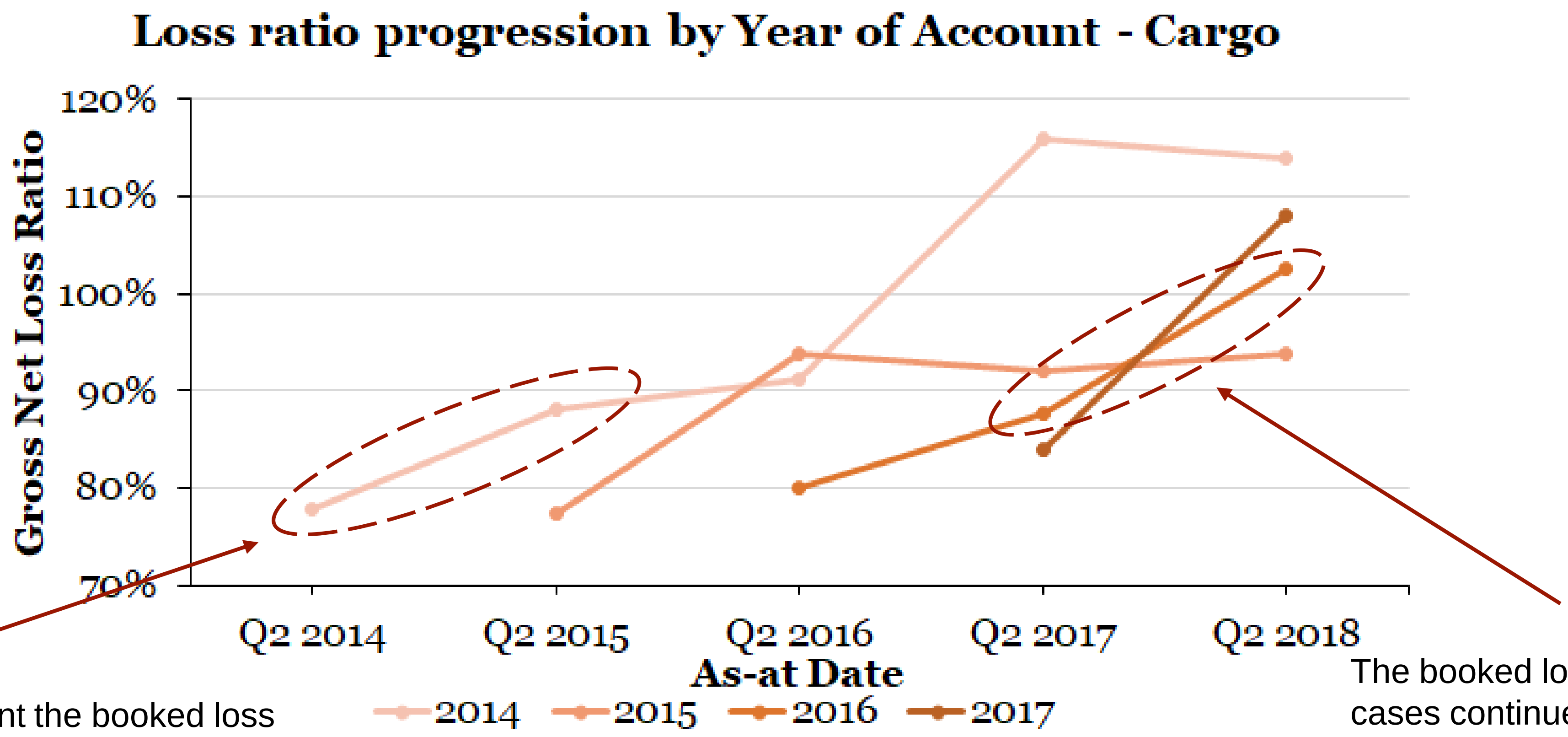




Source: PwC analysis of market data, based off 2016 Q2 to 2018 Q2 Performance Information Packs

Prior year reserve releases

…..and “Soft Market” effects still impact a number of lines too



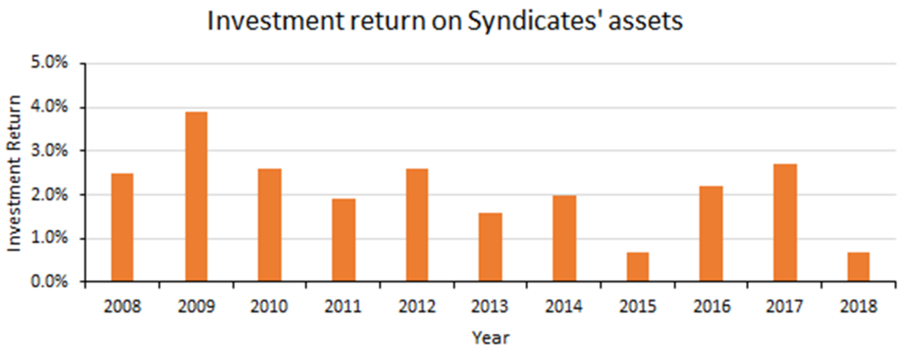
For each year of account the booked loss ratio increases from the initial planned loss ratio, implying optimism in the business plan

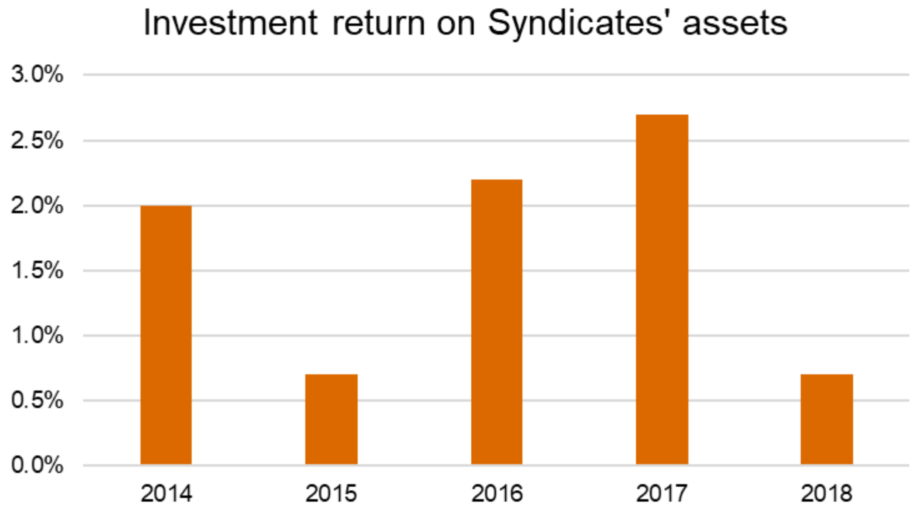
The booked loss ratio has in cases continued to increase, implying that optimism continues into the reserving process, resulting in reserve deterioration

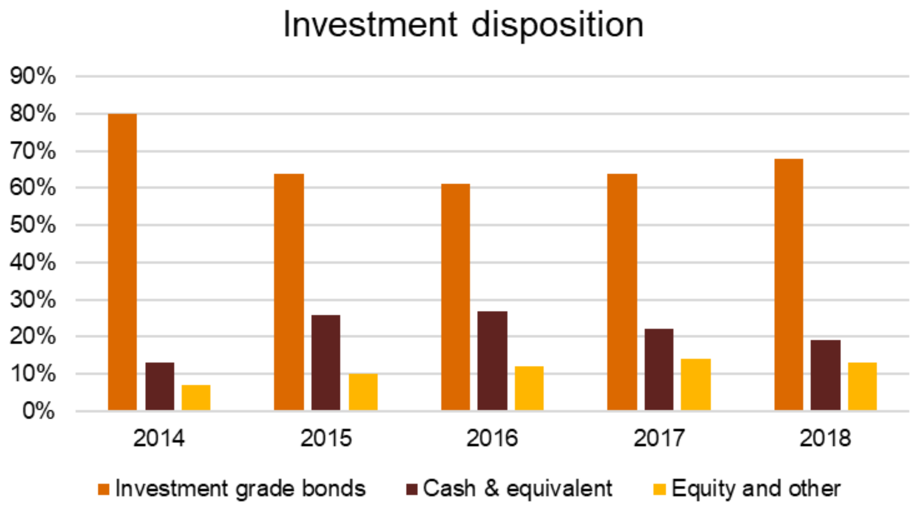
Investment Returns have not been great either!!

Lloyd's experienced a significant reduction in investment returns

- Lloyd's market investments generated a 0.7% return as at year end 2018 in comparison to 2.7% in 2018.
- This was significantly below the 5 year average.
- Lloyd's attributed the reduction in investment returns as at year end 2018 to losses arising from equity and risk assets, part offset by positive returns in cash, government and investment grade corporate bonds.
- Over time, Lloyd's has increased its investment in equity and risky assets which is likely to create volatility in returns.
- Lloyd's attributed its low returns in 2015 to equity assets as well as low returns on bonds.







Source: PwC analysis of Lloyd's year end results

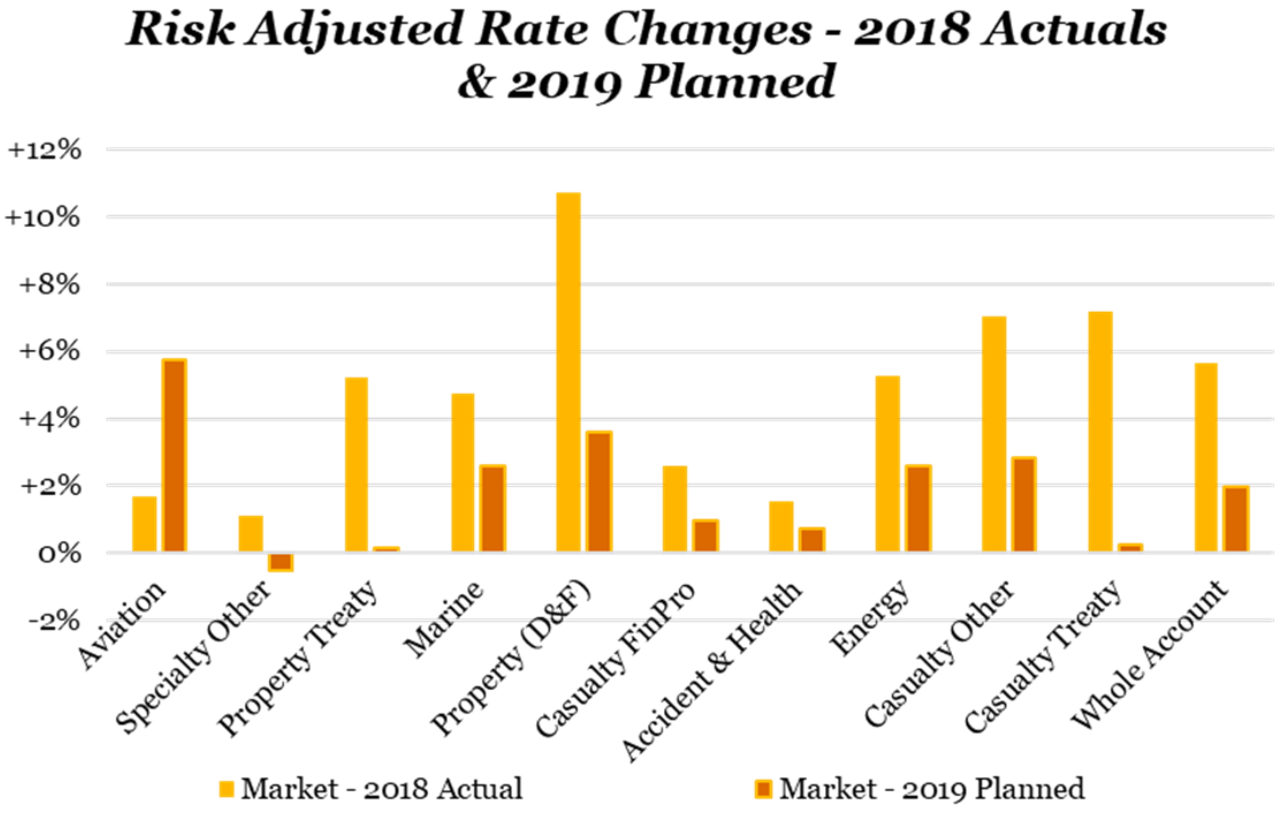
Current Landscape

What has been happening with rates?

Rate hardening of circa 5% experienced in 2018, with rate hardening expected to continue into 2019, albeit at lower levels

- 2018 rate hardening particularly strong across open market US & non-US direct property books (≥20%) – much lower rate hardening experienced within binder and reinsurance property books

- Rate hardening expected to result in improved underwriting profitability – aware of no loss making 2019 plans – compared to nearly a third in 2018

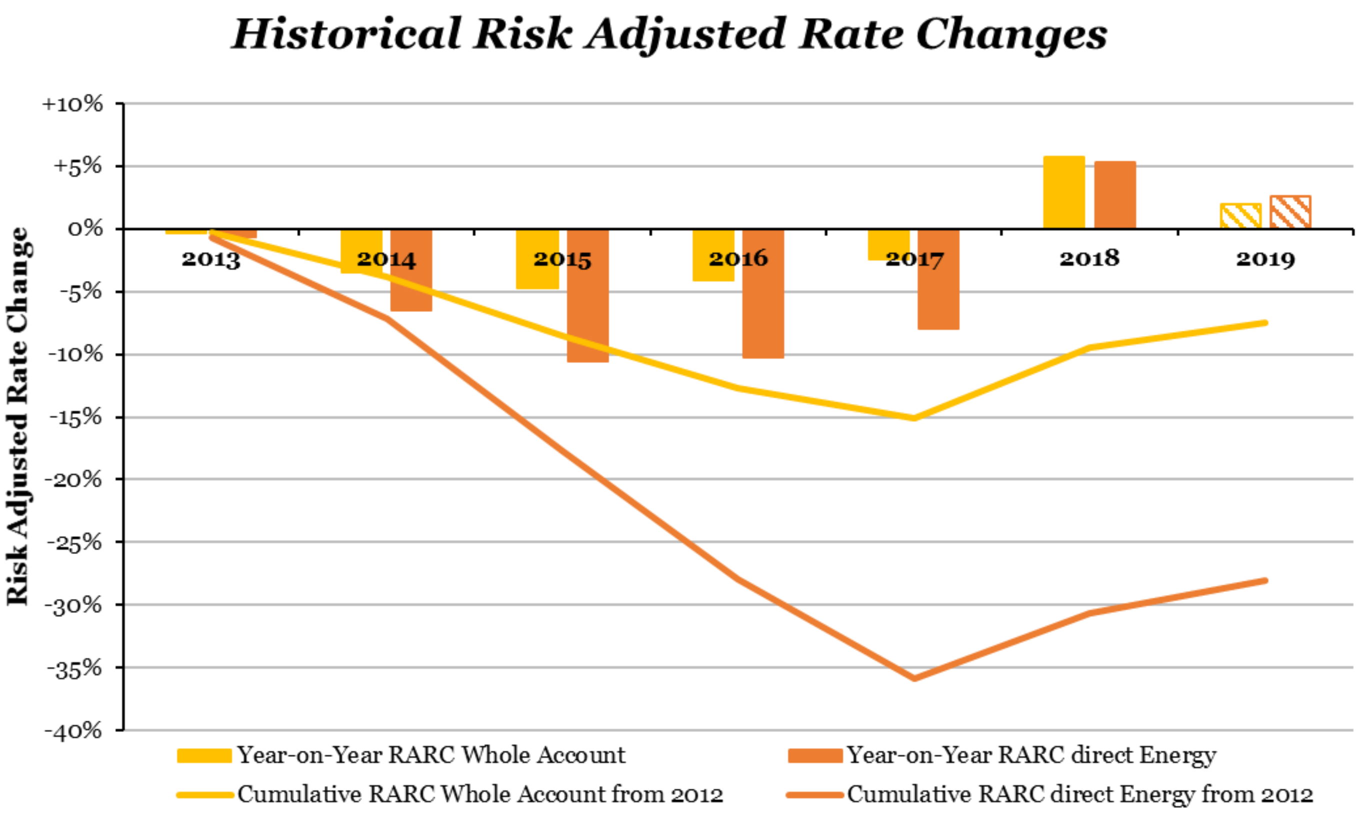


Source: PwC analysis of market data, 2018 risk adjusted rate changes to August 2018

What does this look like over a longer period?

However given the softening of rates in previous years, the market remains soft, particularly in specific classes

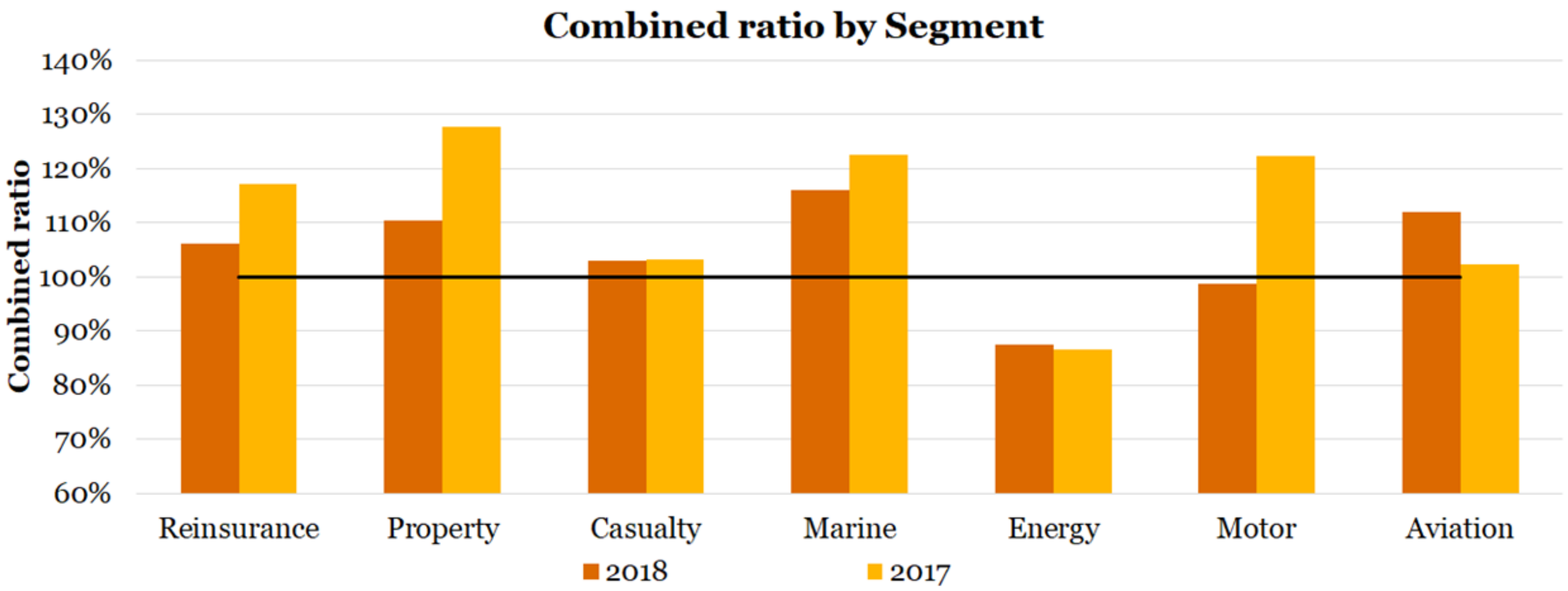
- Rates are significantly lower than compared to 2012
- Certain business have been particularly impacted, e.g. direct Energy, where recent rate increases are more than offset by significant pressure on rates in previous years
- Therefore, given the softening of rates in previous years, **the market remains soft**



Source: PwC analysis of market data, 2018 risk adjusted rate changes to August 2018

What does this mean for profitability?

Despite the improved rates, most segments in the market continue to be loss making

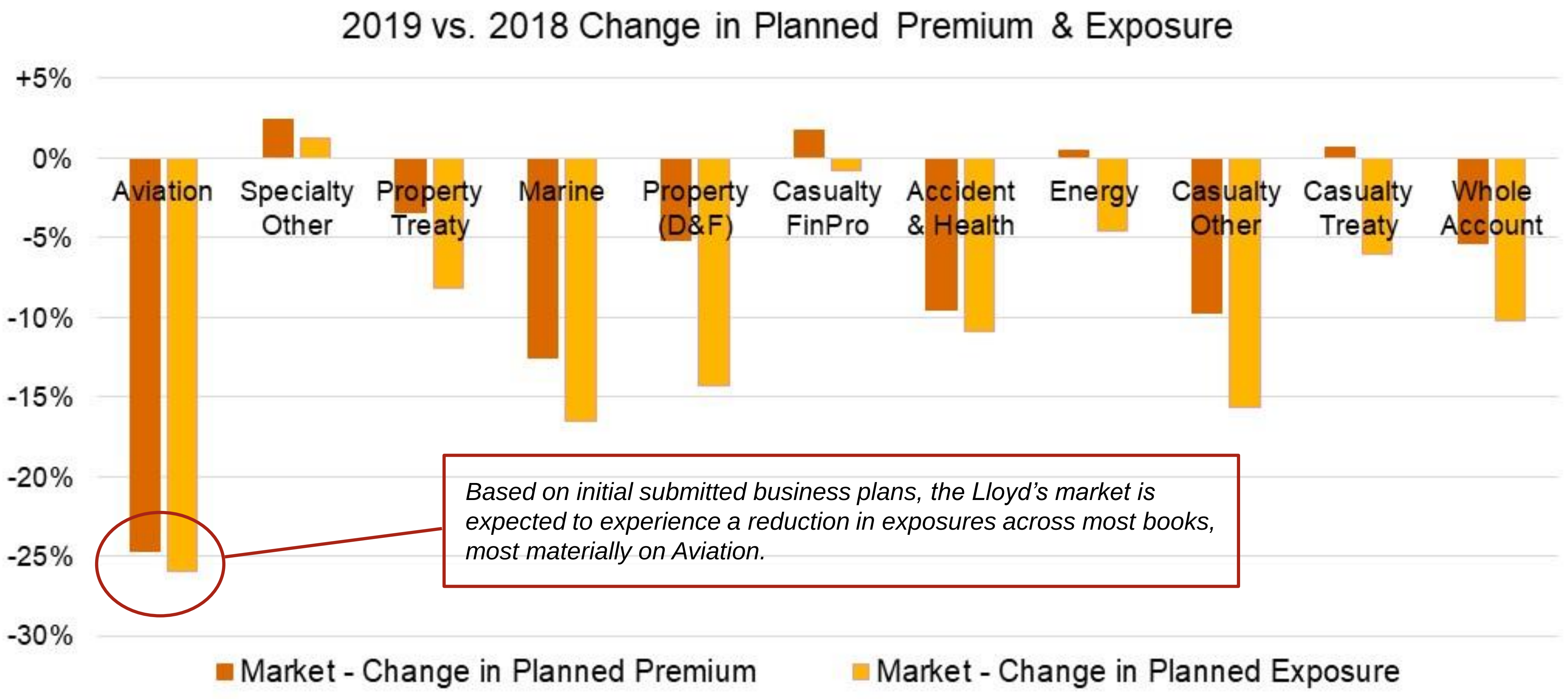


- Despite rate hardening and prior year releases, most segments are loss making, with the exception of Energy and Motor
- Known major catastrophe losses in 2018 could be expected to contribute towards this adverse experience on segments such as Reinsurance and Property
- Aviation has had material adverse experience. PwC analysis suggests that whilst some rate hardening is expected, exposures in this segment are likely to reduce materially

Source: PwC analysis of Lloyd's year end results

And the impact on exposures?

Planned premium is down in many lines – and significantly so in some



Based on initial submitted business plans, the Lloyd's market is expected to experience a reduction in exposures across most books, most materially on Aviation.

Source: PwC analysis of market data, based off initial 2019 YoA Lloyd's submissions

Regulation inc. Brexit

The PRA has written many letters to the Market

And has been taking action too!

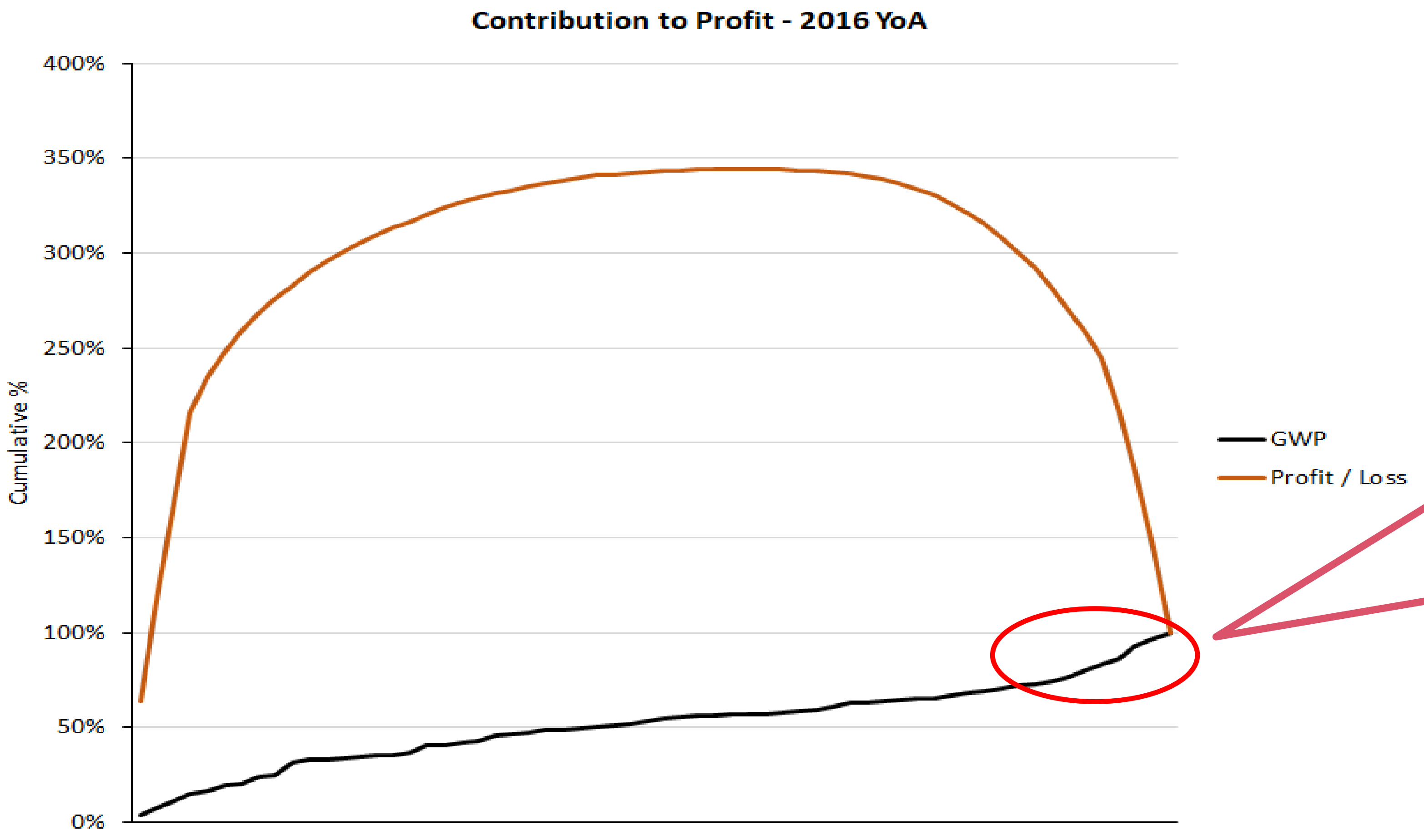
1. *Reserving is key to market results*
2. *More recent years appear less well reserved and are under pressure*
3. *This will happen if:*
   You underestimate rate reductions and are optimistic in pricing new business…
4. *…and/or don't adequately allow for changes in distribution/sources of business*
5. *It is vital you get proper MI and challenge on these areas as a minimum*

> "Firms should stand ready to demonstrate the robustness of their underwriting and reserving governance frameworks"

PRA 'Dear CEO' letter on soft market conditions

Lloyd's have instigated the "Decile 10" Review

"Whale charts" show that a small number of classes erode a LOT of profit



The bottom "10%" has a big impact and Lloyd's have targeted these classes….the **"Decile 10"**

Source: PwC analysis of Lloyd's market data

At least Solvency II is go and harmonises capital over Europe

Brexit Impact on Insurers

- **Political and regulatory uncertainties** relating to any transitional agreement and the content of a free trade agreement
- **New regulatory perimeters** - firms will have to undertake extensive due diligence to satisfy and meet regulatory requirements
- Key risks around **contract certainty** (ability for firms to satisfy contractual obligations without full authorisation), conduct risk and demonstrating head office substance in a new jurisdiction
- Particular uncertainty for **EEA firms operating in the UK** writing significant retail business and requirements to establish a full legal entity, as opposed to a third country branch

"It works both ways!!"

Outbounds – life and non-life

Ireland

Aspen

Aviva

Beazley

Chaucer

Equitable Life

Everest Insurance

Legal & General

NEON Underwriting

North P&I Club

Royal London

Standard Life

The Standard Club

Travelers

XL Group

Belgium

Lloyd's

MS Amlin

QBE

Netherlands

THE UK P&I Club

Steamship Mutual

Chesnara

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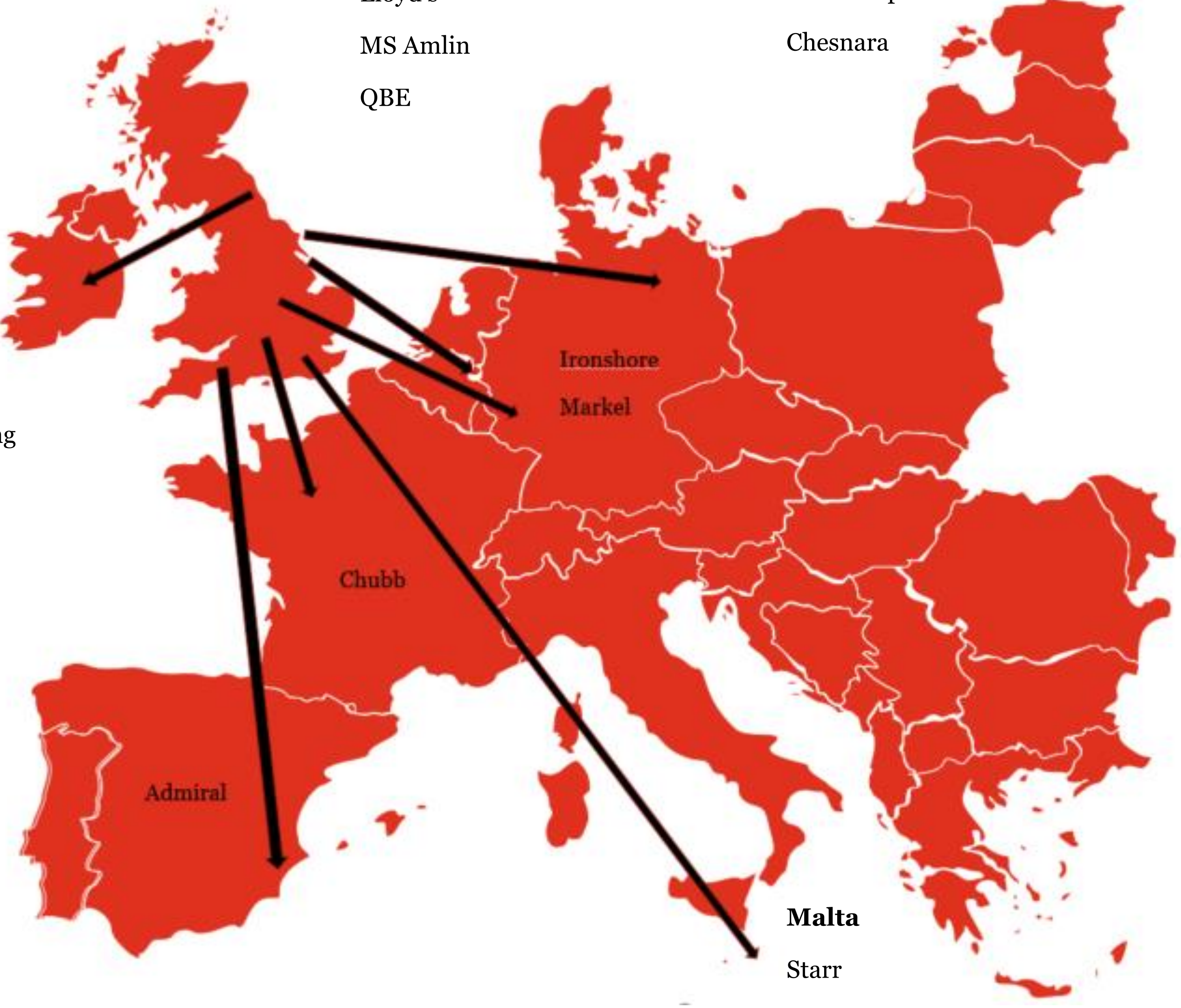
Liberty Speciality

Markets

RSA

Tokio Marine



Malta

Starr

Compre

Inbounds – non-life

Ireland

Allianz

Arch Reinsurance

AXA

.....

Belgium

AG Insurance

Cigna

....

Sweden

Forsakring

If

Sirius

Luxembourg

Globality

iptiQ

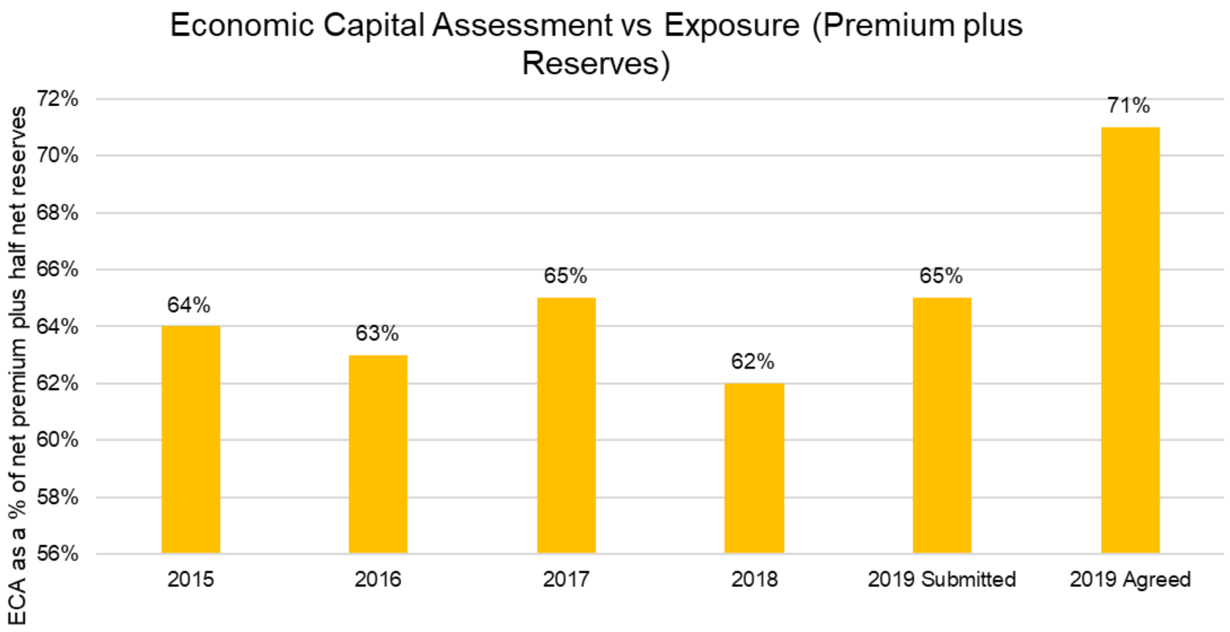
Swiss Re Europe

...

Actually, market conditions have hit capital the hardest!

Syndicate capital requirements have increased by circa 10% for 2019

- Lloyd's view of risk has increased resulting in a material increase of £800m (+5%) in the Market Wide Syndicate Capital Requirements ("MWSCR")
- Over the year, there was also a large increase in capital loadings at a syndicate level which reflected the challenging market
- Ultimate capital loadings increased from £251m (year end 2017) to £1,476m (year end 2018), representing a 10% increase, with loadings applied to 75 syndicates (up from 21 for the previous year)
- 77% of loadings related to either Premium Risk, Reserve Risk, or optimism in business plans. This reflects Lloyd's view of challenging market conditions and potential risks associated with a soft underwriting and reserving cycle

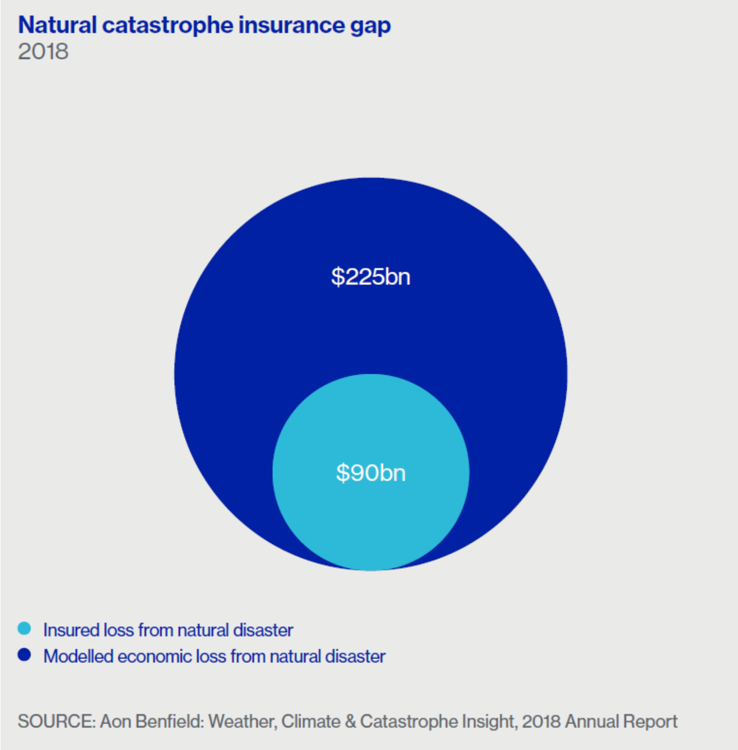


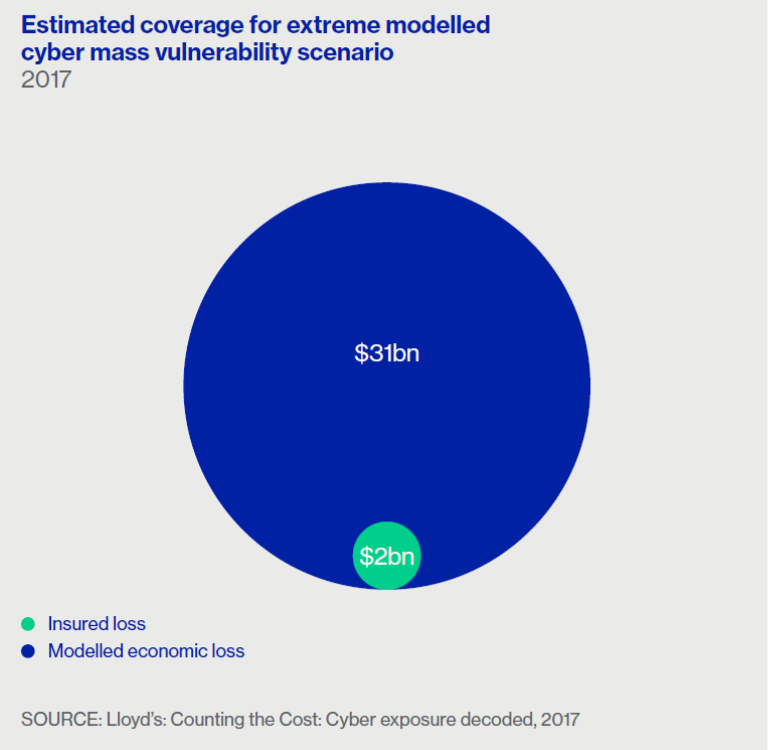
Source: Lloyd's Syndicate Capital Briefing 28 February 2019

What about the future?

Lloyd’s is tackling issues head on….

And has launched the new prospectus





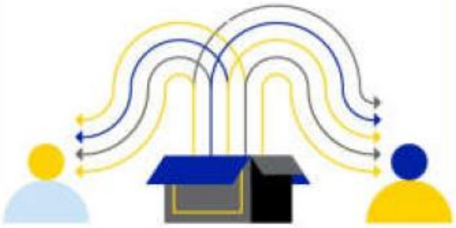
….some of the potential solutions are fundamental….

Complex risk platform
A culture, process and structure that supercharges innovation in response to customer needs

Standardised risk exchange
A risk exchange through which your risks can be placed in minutes at a fraction of today's cost

Capital platform
A structure that enables new sources of capital to simply and effectively access a diverse set of insurance risks on the Lloyd's platform

Syndicate in a box
A streamlined system for syndicates to bring new products and business into the market



Claims solution
An automated claims process that speeds up settlement to improve customer experience and increase trust in the market

Ecosystem of services
Access for all market participants to an ecosystem of products and services that help them develop new business and provide outstanding customer service

….so there will be change…..and possibly radical change!!

Summary / Q&A

Summary & Questions

Lloyd's has an amazing history and strength but is expecting changes ahead!

- Lloyd's has a rich history and is central to the London Market
    - **Reinsurance is a key part of Lloyd's business**
- Like many other global insurers, **recent results have been challenging**
- Lloyd's are actively remediating poor performance….via the **"Decile 10"** process
- The general regulatory environment is also more challenging
- And we know **the world**, technology and risk environment **is changing**
- Lloyd's realise that……and have always shown **initiative, innovation and resilience……**
- ……..so are taking some potentially radical steps to change as the World does

So watch this space!!!!

Thank you

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