Marine Underwriters to become (better?) portfolio managers

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Overview

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3. IUMI tells you all what Marine insurance is about
4. Professional background of Marine underwriters versus investment management
5. Market and portfolio analysis
6. Investment strategy – Markowitz vs. Keynes
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2. Three (三) Questions:

(a) Why do the IUMI stats of the global Marine insurance market show such bad market results?

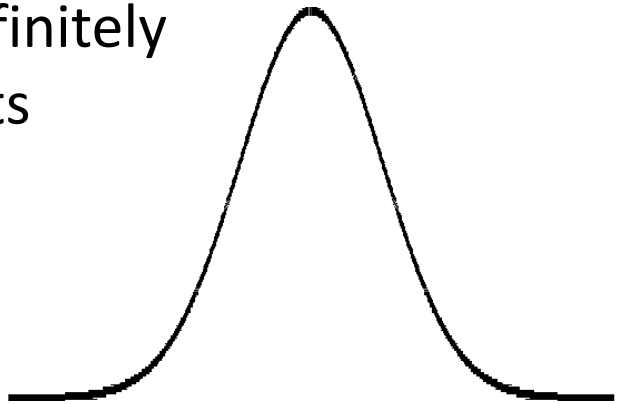
(b) Will the Marine insurance cycle repeat itself?

(c) “Why do you in Marine insurance leave it so late to turn around the book?”

2.1. Take away #1:

Within our market results there are definitely some markets/players who make profits among those who drive the losses

(Bell curve)



2.2. Take away #2:

“Cycle Management” might be partly outdated by “survival of the fittest”

Quote: Tom Boldt IUMI 2013: “this cycle is different”

3. IUMI tells you all what Marine insurance is about

Observation #3 – despite IUMI's truly great achievements…

Neither the

- better transparency of global Marine insurance market results

nor the

- better education on individual Marine risks
- benchmarking by economists
- search for drivers behind the business
- introduction of Solvency II etc.

have improved our reported market results

(…and nor will my talk…)

4.1. Professional background of Marine Underwriters versus investment Management

Investment manager:

- "A person or organization that makes investments in portfolios of securities on behalf of clients in accordance with the investment objectives and parameters defined by these (clients).
- An Investment Manager may be responsible for all activities with the management of client portfolios, from buying and selling on a day to day basis to portfolio monitoring, settlement of transactions, performance management and regulatory and client reporting"*

*http://www.investopedia.com/terms/i/investment-manager.asp

4.2. Core Process in Portfolio Management

5.1. Market and Portfolio analysis: The Marine insurance deli's

Duration of risks and contracts:
- Short term
- Mid term
- Long term
- Mixed

LOB's/Classes:
- Cargo
- Hull
- (US-) Inland
- Liabilities (Hull/Cargo/P&I)
- War, political risks
- Loss of earnings, profit
- Combination of these

Claims patterns:
- Frequency/attritional
- Severity/large
- Event (Cat)
- Mixed

Players:
- Locals
- Globals
- Monoliners
- Composites
- R/I'ers direct
- Self insurance

UWR Capacities:
- Low
- High
- Mixed

Markets iro capacities and origin of bizz:
- National
- International
- i.e. London, Nordic etc
- R/I concepts

5.2. Market and portfolio analysis: “Investment into portfolios of securities”

Take away #4:

No Marine underwriting unit presently has the option to access the total Global Marine portfolio in order to create an optimum global spread of risks

Take away #5:

The Marine insurance world is much more a global conglomerate of deli’s than a chain of Hamburger restaurants where you can order the same burger everywhere

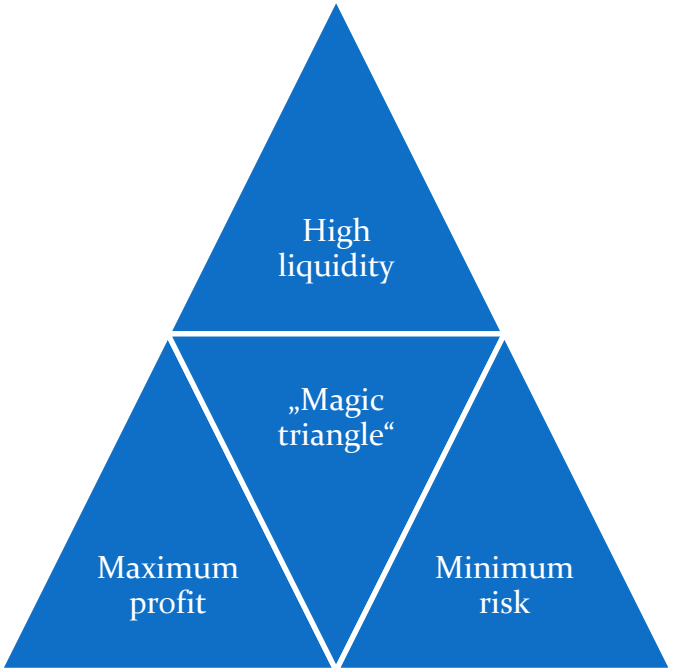
6.1. Investment strategy – “investment objectives and parameters” - Markowitz versus Keynes

Offensive or defensive risk classes

Talmut:

- One third into real estate
- One third into business
- One third into cash

Diversification versus concentration?



6.2.Put all your eggs into one basket?

- A broad range of investments *among* asset classes
- *Within these,* a broad range of subclasses
- Marine traditionally writes co-insurance

"To carry one's eggs in a great number of baskets without having the time or opportunity to discover how many baskets have holes is the surest way of increasing risks and loss" (Keynes)

Take away #6: Your Marine portfolio strategy will be determined by the clients you can reach, your local or global market presence, your team capabilities, your UWR-capacity, your principal's direction (offensive/defensive/grow/turn-around) and you will have to decide whether you concentrate or diversify "your baskets"

7.1. Investment plan – Solvency II* and Portfolio Strategy

- **Pillar 1**
  Quantitative capital requirements
- **Pillar 2**
  supervisory review with Risk management, risk governance and systems and controls
- **Pillar 3**
  Transparency on risk appetite, strategy and public disclosure

* See IUMI 2007 and 2008 conference papers on www.iumi.com

7.2. Capital Coverage and CR targets (example)

Risk classes	Income Currency Units	Capital Coverage factor	Capital required	Return Target example	= Target CR*	Return Target example	= Target CR*
				15%		10%	
A-low	100	30%	30	4,5	95,5%	3	97%
B-med	100	50%	50	7,5	92,5%	5	95%
C-high	100	100%	100	15	85%	10	90%

* important: Excluding non technical results!

Take away #7: Solvency II – to write a „boring“ good performing account without surprises? (as this takes the pressure off your Target CR)

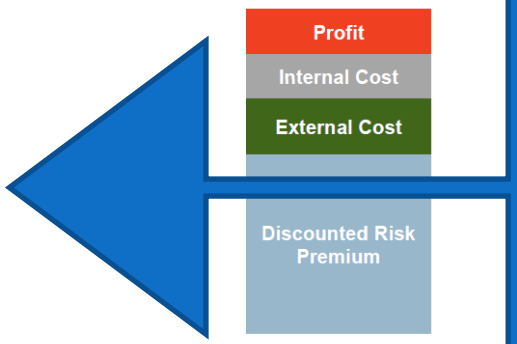
7.3. IUMI 2008 Anne Chevalier - Solvency II and Technical Pricing

Pricing Steps

Adjustment of historical cedant's premiums and claims to 2008 level

Expected loss ratio estimation

- Attritional loss ratio
- Large loss ratio
- Event loss ratio



Other cost components (commission, internal costs)

Allocation of risk-based capital and calculation of return on capital

Should have/do:

- Technical pricing tool
- Slice the portfolio into risk classes with similar LR character and define target loss ratios
- Benchmark situation as-is versus targets

8.1. Execution and UWR Process – Pricing effects – with Technical Pricing

Risk fix cost-ratio 30%*	Target Technical Premium	Risk units/Price per RU	Subline Capital coverage factor*	10% profit target* (example)	= Claims ratio target with 30% cost for profit*	Exposure Accumulation factors	Other soft facts such as client criteria
A - low	100	1	30%	3	67%	x	y
B - med	100	1	50%	5	65%	x	y
C - high	100	1	100%	10	60%	x	y
total	300**			18	64%		

* assumptions **for 300 risk units

8.2. Example of actual results Commercial rates with fixed claims and 30% assumed cost

Risk fix cost-ratio 30%*	Actual Commercial Premium	100 Risk units/Price per RU	Original Target Profit is 10% on technical	Actual loss ratio (real)	Claims in currency units*	Cost assumed 30%*	Loss Profit Absolute
A - low	90	0,9	3	65%	58,5	27	4,5
B - med	70	0,7	5	85%	59,5	21	-10,5
C - high	40	0,4	10	20%	8,0	12	20
total	200**	0,67	18		126	60	14

* assumptions **for 300 risk units

8.3. Example of pricing effects after renewal with different price factors per risk group

Risk fix cost-ratio 30%*	Actual Commercial Premium	Price effects at renewal	New Commercial Actual Premium	Former price per risk unit	Risk units/Price per RU	Claims load assumed as being stable	Cost assumed stable*	„As-if“ Loss Profit absolute
A - low	90	./. 5%	85,5	0,9	0,86	58,5	27	0
B - med	70	+10%	77	0,7	0,77	59,5	21	-3,5
C - high	40	./. 20%	32	0,4	0,32	8,0	12	12
total	200		194,5	0,67	0,65	126	60	8,5

* assumptions

8.4. Example of pricing effects with different price factors and a change in portfolio mix

Risk fix cost-ratio 30%*	Actual Commercial Premium	Price effects	New Commercial Actual Premium	Former price per risk unit	Risk units/Price per RU	Claims load assumed as being stable*	Cost assumed stable*	„As-if“ Loss Profit absolute
A - low	90	./. 5%	85,5	0,9	0,86	58,5	27	0
B - med	70	+10%	77	0,7	0,77	59,5	21	-3,5
C - high	20	./. 20%	16	0,4	0,32	4	6	6
total	180**		178,5	0,67	**0,71**	122	54	**2,5**

* assumptions **for 250 risk units as C-risks are ./. 50 units

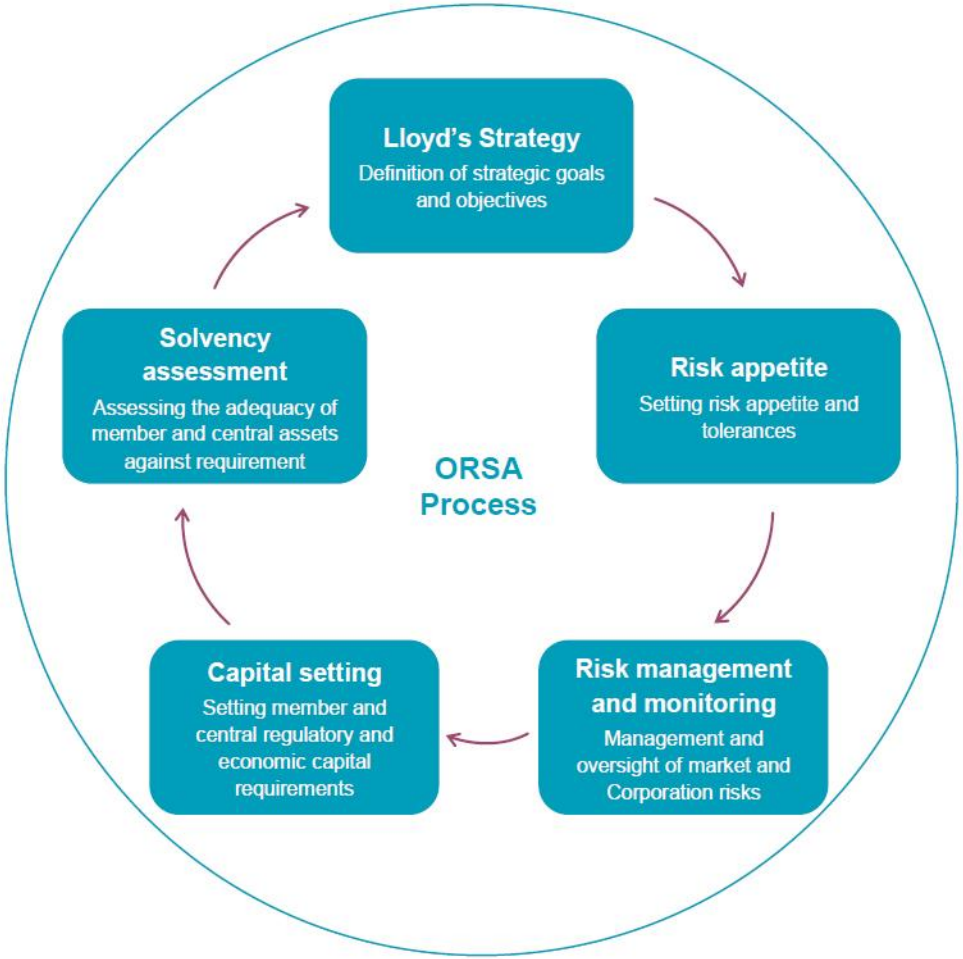
9.1. Mark Twain and ORSA?*

‘The Own Risk and Solvency Assessment shall be an integral part of the business strategy and shall be taken into account on an ongoing basis in the strategic decisions of the undertaking.’ **(Solvency II Directive, art.45(4))**

***Further study as examples:** (among others…)

- NAIC OWN RISK AND SOLVENCY ASSESSMENT (ORSA) GUIDANCE MANUAL As of March 2013
- Willis Re: The Own Risk and Solvency Assessment (ORSA): What Is It, and Why Is It Good for You? January 2012
- Deloitte: Forward Focus - Insurance issues and insights from Howard Mills - The Own Risk and Solvency Assessment (ORSA) - A regulatory guidepost to the future

9.2. Example: Lloyd's Society ORSA Framework (2011)*



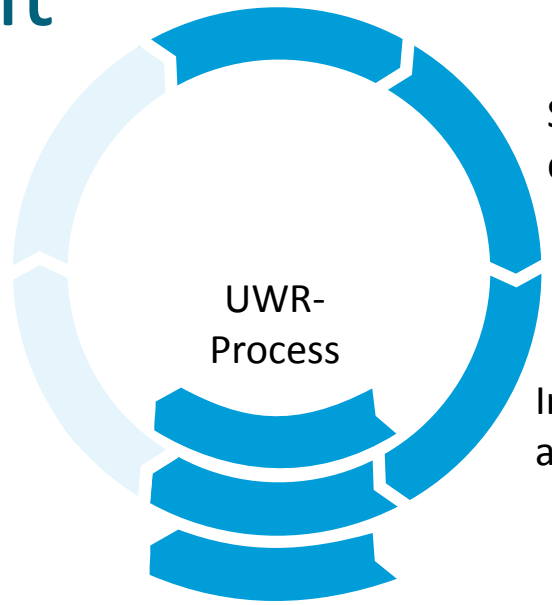
*** Lloyd's Solvency II Own Risk and Solvency Assessment (ORSA) Guidance notes September 2011**

9.3. Elements of Core Process of Marine Portfolio Management

Monitor continously and simulate

„as if“ forward looking :

- Sales – new/renewed/lost/lapsed
- UWR – pricing/exposure/quality etc.
- Claims – frequency/severity/event (CAT)
- Exposures & Accumulation
- Portfolio composition, line sizes plus „Compliance effects“ on portfolio parts



„(久)“. Mark Twain - The Tragedy of Pudd’nhead Wilson:

„Put all your eggs in one basket –
and watch the basket“

V. Bergeest: If you put all your eggs into a basket, monitor and anticipate „as-if“ and objectively, what hatches from the eggs

and iro the rules of the game:

…IUMI is not FIFA…

Thank you IUMI – thank you Hong Kong

Sincerely yours

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