

SPIAO Extended Conference **FSCO, LLOYD'S OF LONDON & PREPARING** **FOR A CHANGING MARKETPLACE**

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FSCO, LLOYD'S OF LONDON & PREPARING FOR A CHANGING MARKETPLACE

AGENDA

- FSCO Regulations
- Lloyd's of London Introduction & Overview
- Composition of Lloyd's
- Lloyd's Security
- Lloyd's Changes & Its Impact Today
- Overall Changing Marketplace
 - Property, Casualty, Lloyd's
- How You can Prepare for these Changes
- Adjusting Your Approach to the Market

FINANCIAL SERVICES COMMISSION OF ONTARIO

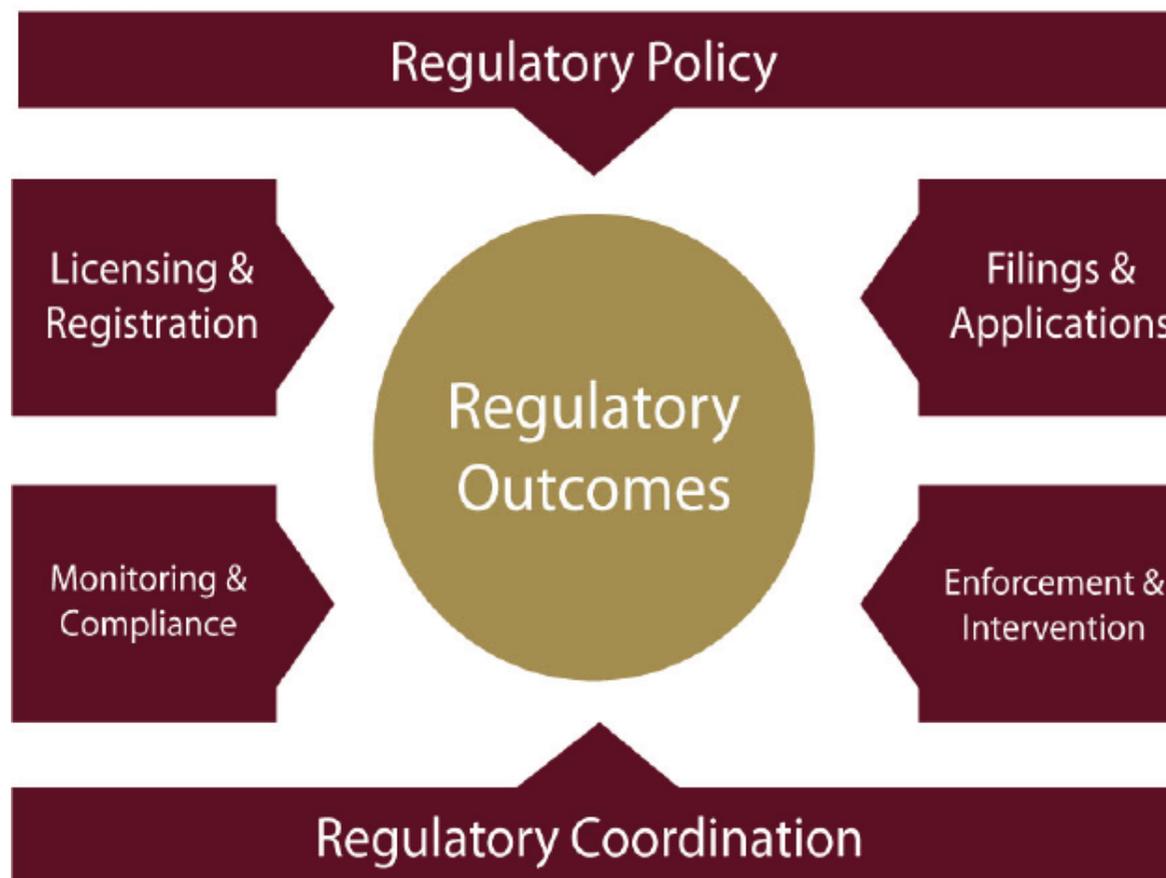
Regulations

- FSCO's legislative mandate is to provide regulatory services that protect the public interest and enhance public confidence in the sectors it regulates.
- In the **insurance sector**, FSCO is primarily a market conduct regulator, supervising the treatment of consumers and the conduct of business of insurance companies, agents, adjusters, and service providers.

FSCO Regulations

FSCO's Core Regulatory Activities

FSCO performs the following core regulatory activities in order to fulfil its legislative mandate.



FSCO Regulations

FSCO & Lloyd's of London News

- **The aftermath of 'firm action' in Lloyd's market** (*Canadian Underwriter: February 8, 2019*)
- **These Lloyd's syndicates have shut down** (*Canadian Underwriter: March 27, 2019*)

LLOYD'S OF LONDON

Description

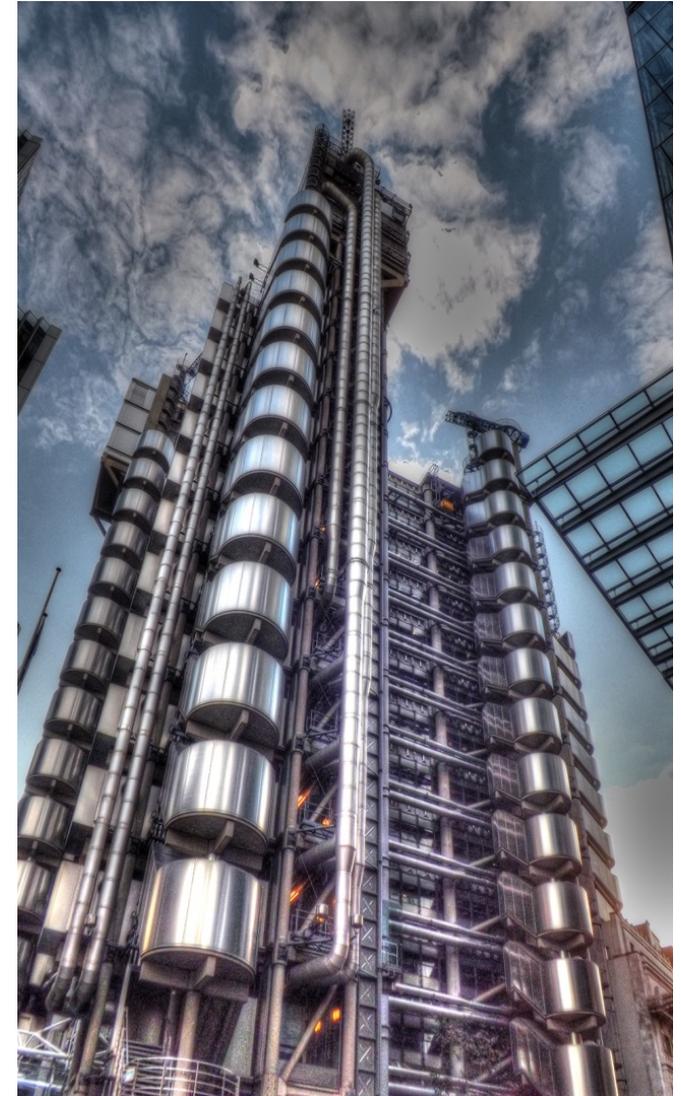
- Lloyd's of London is *not* an insurance company.
- Rather, it is a marketplace where insurance buyers and sellers come together.
- Lloyd's began as a coffee house in the 1600s. Ship captains, vessel owners, traders and others interested in shipping gathered at the coffee house to buy or sell what is now called ocean cargo insurance.



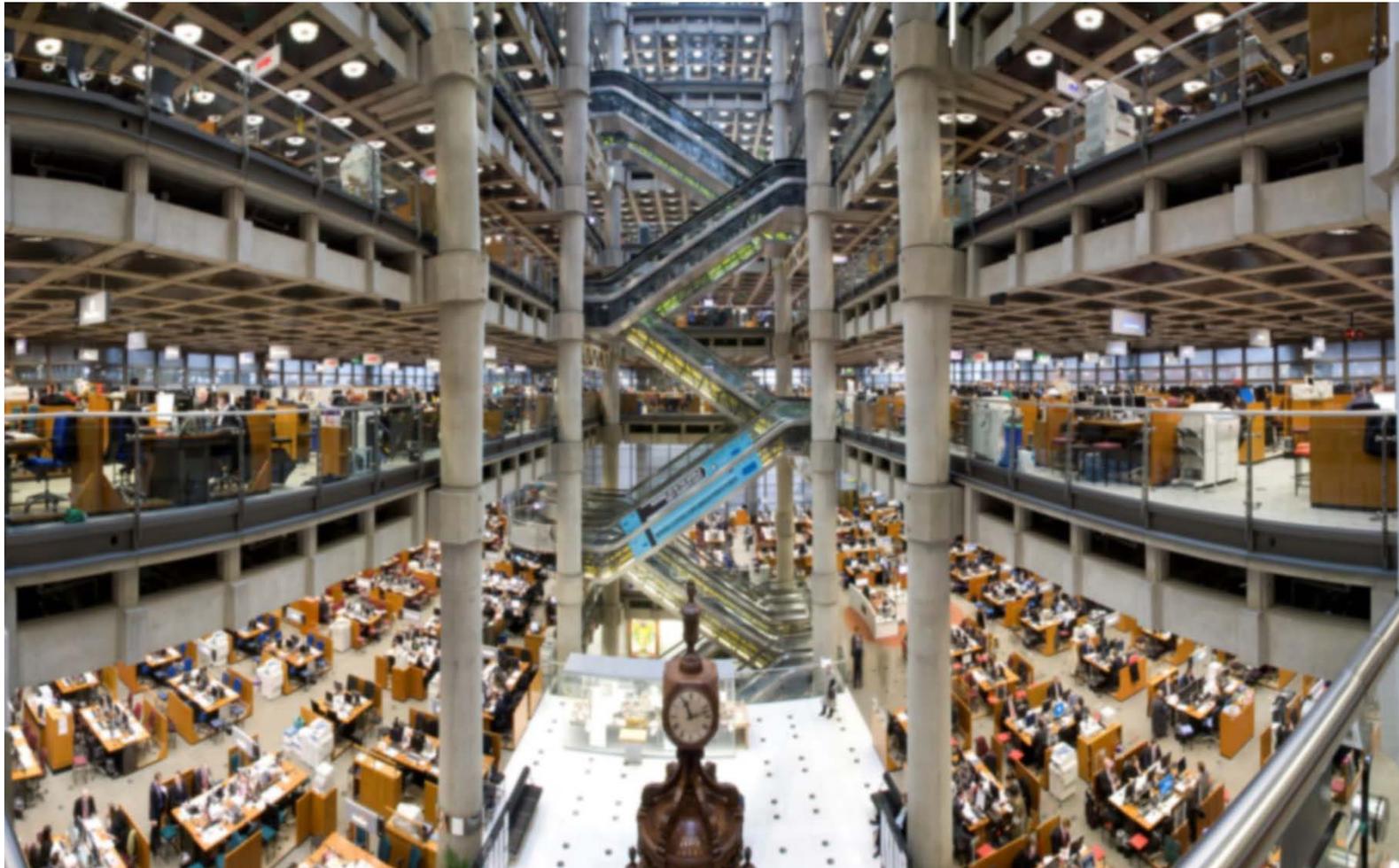
LLOYD'S OF LONDON

Description

- These days, brokers and underwriters convene at the Lloyd's office building in East Central London.
- Consists of 80+ (re)insurance syndicates. Insurance companies also have “boxes in the room”.
- S&P A + (strong), unique chain of security - syndicates assets (premiums), member's funds (capital in trust) and Lloyd's Central Assets.
- 86% of Lloyd's business comes from outside the UK.



LLOYD'S OF LONDON



LLOYD'S OF LONDON

Composition

LLOYD'S SYNDICATES

- The syndicates are the backbone of the Lloyd's marketplace.
- A syndicate functions like a little insurance company, assuming risks and paying claims.
- Each syndicate is made up of one or more **members** (may be individuals or corporations). Members provide the \$ capital that allows the syndicate to operate.
- When Lloyd's syndicates assume risks, they operate by **subscription**. This means that each syndicate assumes only a percentage of each risk. In some cases, a syndicate may assume only a small amount (such as one or two percent) of the total risk. In others, it may assume a larger chunk, such as 25% or 50%.

LLOYD'S OF LONDON

Composition

MANAGING AGENTS - work on behalf of syndicates, overseeing their day-to-day business affairs.

- They hire and supervise underwriters, adjusters, accountants, and other essential staff.
- A managing agent may oversee more than one syndicate. In some cases, the managing agent may be the same company that provides the capital for the syndicate.

BROKERS - Insurance brokers act as intermediaries between insurance buyers and syndicates.

- To conduct business in the Lloyd's marketplace, a broker must be accredited by the Corporation of Lloyd's.
- An insurance buyer cannot communicate directly with a Lloyd's broker. Instead, he or she must work through a local broker or agent.

LLOYD'S OF LONDON

Composition

COVERHOLDERS

- Coverholders operate under *binding authority* granted to them by managing agents.
- Some coverholders are authorized to issue documents such as insurance binders and certificates of insurance. They may also have the authority to collect premiums and settle claims.
- By contracting with coverholders, Lloyd's managing agents can operate worldwide without having to establish a local office. In some countries, coverholders are called *managing general agencies* or MGAs.

LLOYD'S OF LONDON

Financial Security

- Annual Solvency Tests for all syndicates & members:
 - Must demonstrate that they meet the regulatory criteria for solvency. If they cannot do so, they will not be allowed to continue trading or may be required to provide further capital.
 - Any solvency test consists of two parts:
 - a) valuations of both the assets and the liabilities of the insurer, and
 - b) confirmation that the assets exceed the liabilities by an adequate margin.
- A syndicate's assets include the capital provided by its members, premium received and investment income. Its liabilities are the claims and expenses it will be called upon to pay.

LLOYD'S OF LONDON

What if Things Go Wrong

LLOYD'S CORPORATION - an independent organization and regulator. Acts to protect/maintain the market's reputation, provides various services and original research, reports and analysis to the industry's knowledge base.

Lloyd's **Chain of Security**, provides financial security to policyholders and capital efficiency to members. There are three links in the Chain of Security

1. **Syndicate Trust Fund:** funds held in trust-mainly for policyholders. Payment of claims take precedence over distribution of profits
2. **Members' funds:** held in trust. Underwritten for their own account and can be used to pay claims.
3. **Central Fund:** the last line of defense (subject to Council approval). A fund to protect policyholders in case underwriting member is unable to meet his/her liabilities out of Syndicate Trust Funds, funds deposited at Lloyd's, reserves, and personal assets outside of Lloyd's. Every Lloyd's member makes an annual contribution to this fund

LLOYD'S OF LONDON

Market Changes

LOOKING BACK AT 2017

Continued growth in available capacity: increases in incumbent capacity, new entrants, increased reinsurance purchase. Lloyd's Gross Written Premium (GWP)* has grown from £26bn (2013) to £34bn (2017).

Declining rating environment: on going London overcapacity, recognition of worldwide competition.

Relaxation of technical underwriting: opportunity to enhance coverage (ex. Drones and EIL), reduce attachment points (lower limits), offer increased limits etc.

LLOYD'S OF LONDON

Market Changes

LOOKING BACK AT 2017

Reinsurers pricing unpredictable: technical versus budget driven.

Record M&A activity (underwriting & broking): growth/market share/cost savings.

GWP* total gross premium written by an insurer before deductions for reinsurance and ceding commissions.

LLOYD'S OF LONDON

Market Changes

LOOKING BACK AT 2017

Poor underwriting results: 2017 Lloyd's combined ratio underwriting loss was 114%. Due to above average CAT season (HIM losses) but also poor underlying performance.

Regulatory pressure: Prudential Regulatory Authority (Owned by the Bank of England and is the UK's financial services regulatory body for banks, insurers, credit unions, major lenders) issued 'Dear CEO' letter to all London insurers including Lloyd's.

LLOYD'S OF LONDON

Market Changes

LOOKING BACK AT 2017

Security Rating Pressure: S&P and Fitch placed Lloyd's on negative watch in 2017.

Combined ratio *The sum of two ratios, one calculated by dividing incurred losses plus loss adjustment expense (LAE) by earned premiums (the calendar year loss ratio), and the other calculated by dividing all other expenses by either written or earned premiums (i.e. trade basis or statutory basis expense ratio). Used in both insurance and reinsurance, a combined ratio below 100 percent is indicative of an underwriting profit.

LLOYD'S OF LONDON

Market Changes

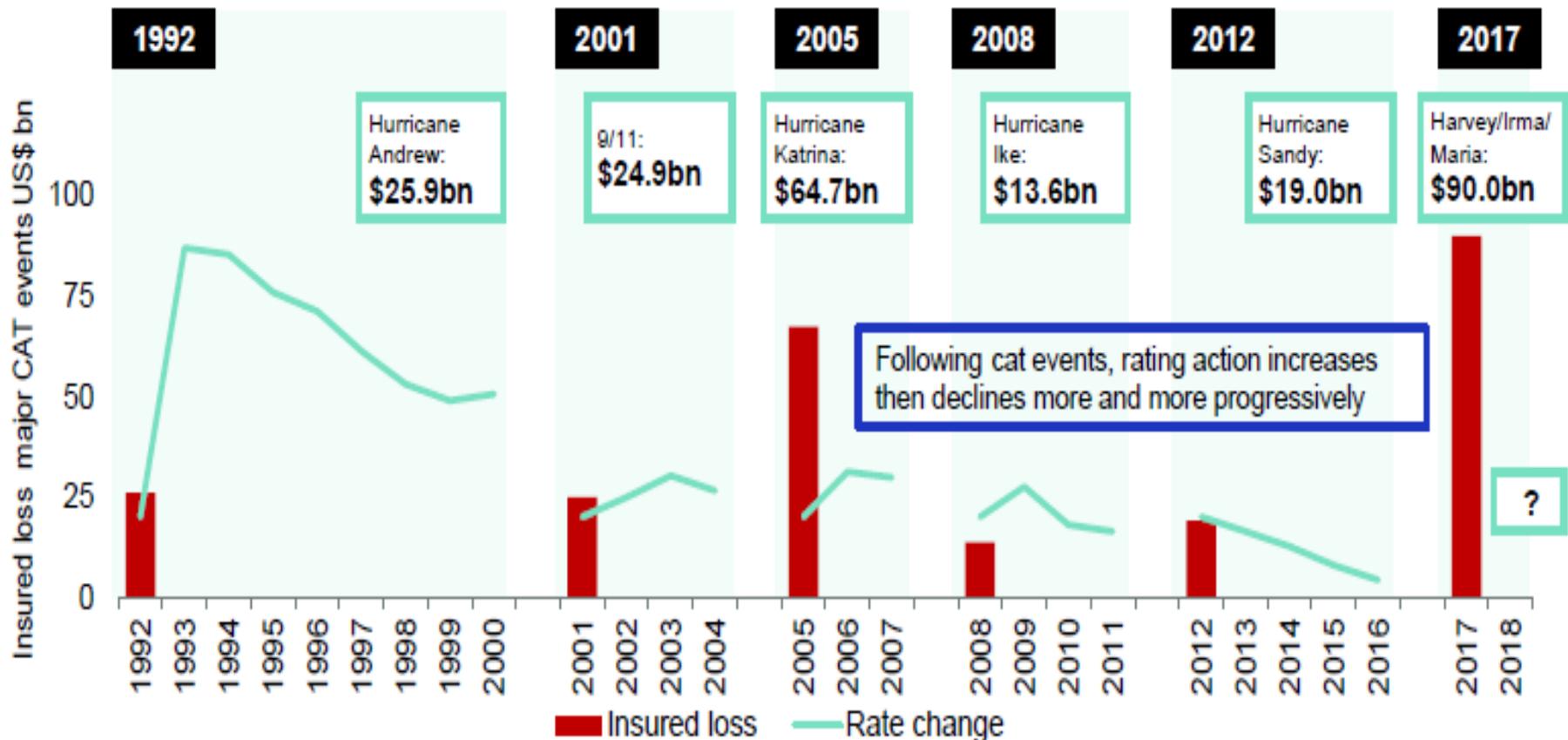
LLOYD'S REACTION - 2018

- May 2018 - closer scrutiny of 2019 business plans.
- Failure to agree to an acceptable business plan would lead to run off of the syndicate.
- Lloyd's Corporation placed a focus on:
 - Loss making syndicates
 - Each syndicates' bottom performing 10 portfolios
 - Poor performing classes across the market as a whole (8 classes including property, cargo, marine hull,.....)
- Goal for 2019 – Gross Written Premium to reduce by 5%.

LLOYD'S OF LONDON

'The cycle' will not solve profitability challenges

Graph shows recent **headline** catastrophe events



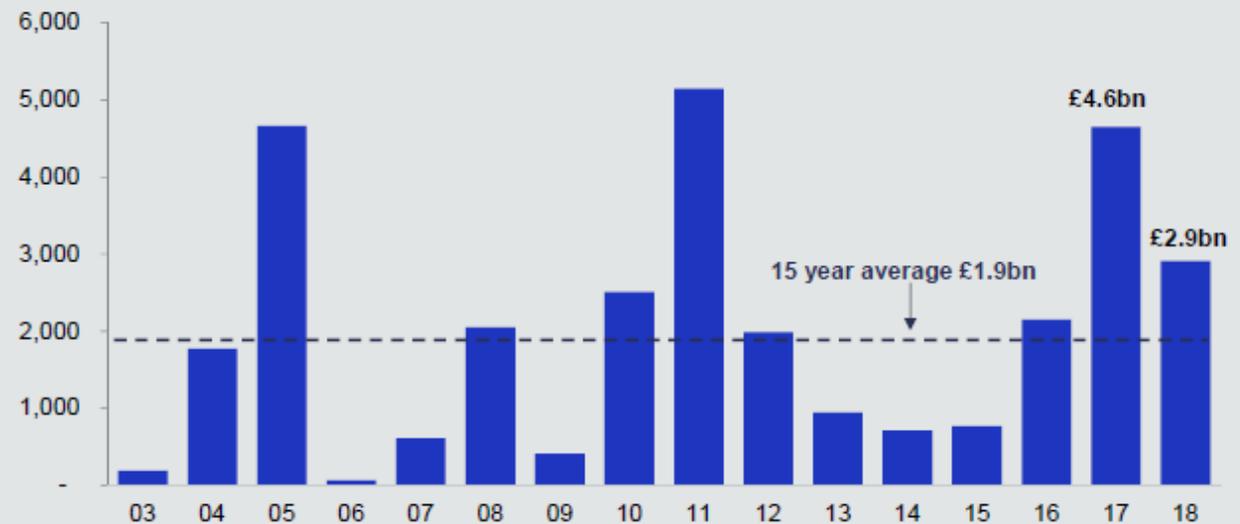
LLOYD'S OF LONDON 2018 RESULTS

LLOYD'S

Second consecutive year of major claims above the Lloyd's market long-term average

Largest major claims, net (£bn)	2017	2018
Hurricane Florence	-	0.5
Typhoon Jebi	-	0.4
Hurricane Michael	-	0.8
California wildfires	0.5	0.7
Hurricane Harvey	1.2	-
Hurricane Irma	1.6	-
Hurricane Maria	0.8	-
Mexico earthquakes	0.3	-
All other	0.2	0.5
Total	4.6	2.9

Lloyd's major claims (£)



Source: Lloyd's market results, 31 December 2018 (previous losses indexed); claims in other currencies translated at the exchange rate prevailing at the date of loss. CR: combined ratio.

LLOYD'S OF LONDON

Market Changes

CASUALTY CLAIMS DRIVERS

- Liability claims are 'long tail' ex. minors, abuse claims.
- Inflation, especially in relation to future care costs (medical / non medical), defence costs.
- Low discount rates.
- Joint and Several liability ex. MVAs / road design and maintenance, planning.
- Climate change ex. Flooding, wildfires, coastal erosion.
- Changing legal environment ex. Enquiries, Class Actions, litigation following catastrophic events or systemic failings. Watching for cyber, terrorism, defamation and environmental.

LLOYD'S OF LONDON

Market Changes

LLOYD'S INDUSTRY SUMMARY

- The earlier Global Financial Crisis resulted in low interest rates, low inflationary pressures and environment of low investment returns.
- Capital markets looked to insurance which historically enjoyed attractive returns. This in turn has driven down pricing.
- Relatively benign claims experience pre-2017 masked underlying attrition and large loss pricing issues.
- Lloyd's is facing renewed focus on:
 - price,
 - deployment of capacity,
 - data and analytics,
 - operating and cost efficiencies.

MARKET UPDATE

A Changing Marketplace

PROPERTY

- This is not a hard market. We are seeing a ‘transitional’ market where insurers are returning to underwriting ‘discipline’ where the focus is on profitability and improving the overall combined ratios.
- We have just gone through 20+ years of declining rates, with a couple small blips around wind events. For many insurers, property lines have had combined ratios in excess of 100% for at least the last two years.
- ‘As is’ renewals are becoming increasingly rare. Most insurers are starting at 10% rate increases for clean accounts and moving upwards from there. It is becoming increasingly difficult to get that 10% increase much below the 6% to 8% range.
- Capacity is generally available and not a concern for most risks but insurers are starting to price it correctly.

MARKET UPDATE

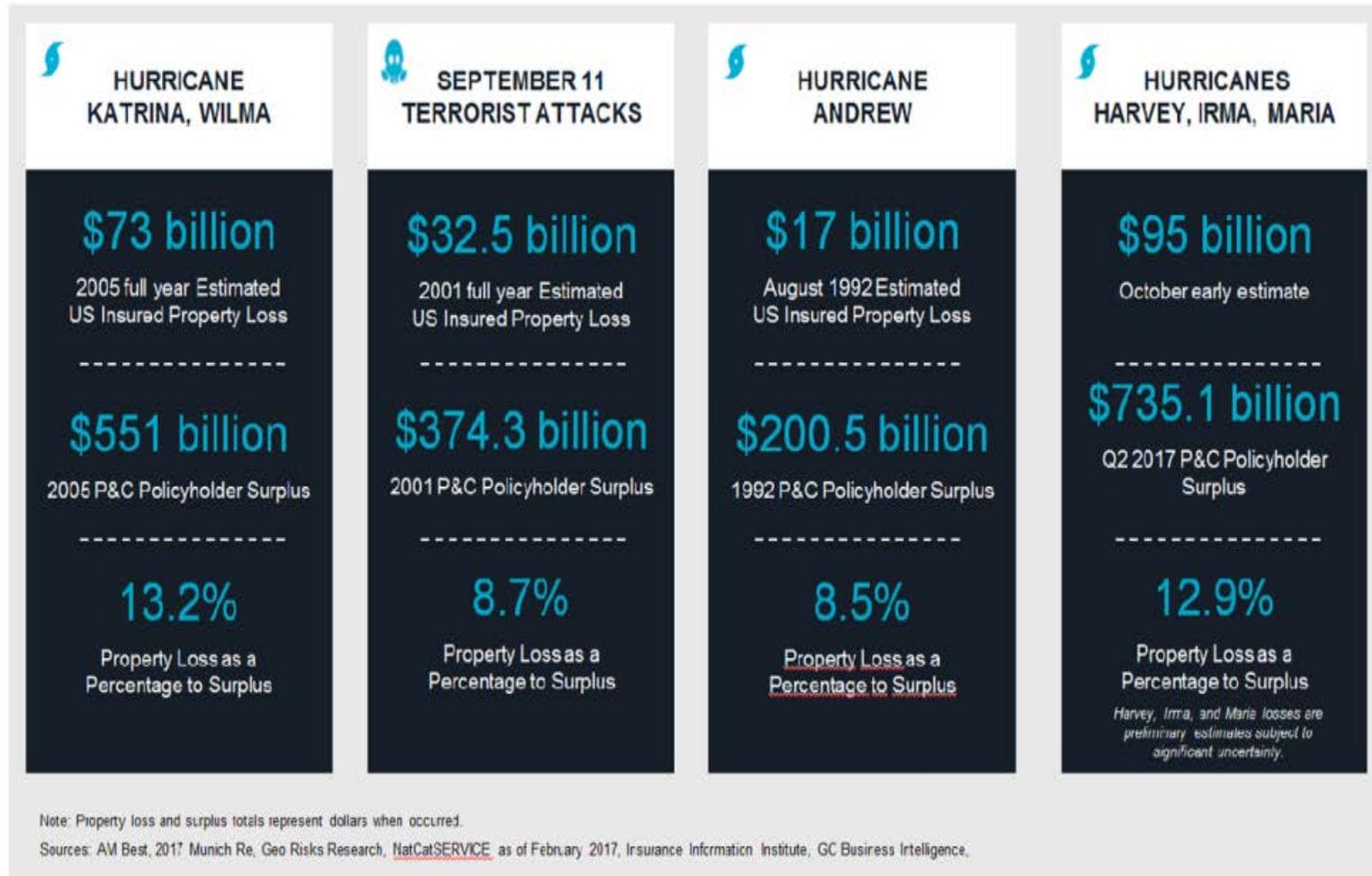
A Changing Marketplace

PROPERTY

- Clients that ignore or don't complete 'priority' risk recommendations will find a direct impact on renewal underwriting and rates / deductibles and capacity.
- Loss ratios, loss trends and loss types will weigh heavily into underwriting decisions. Even loss ratios below 50% will now likely attract some level of rate or deductible increase above the market increase.

MARKET UPDATE

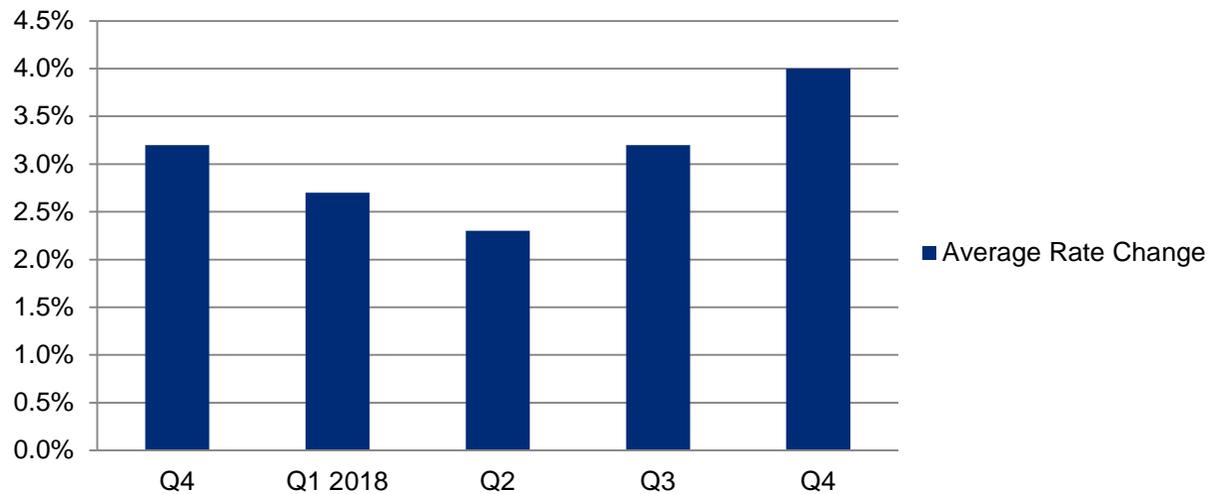
A Changing Marketplace



MARKET UPDATE

A Changing Marketplace

Global Insurance Pricing Change – Property



MARKET UPDATE

A Changing Marketplace

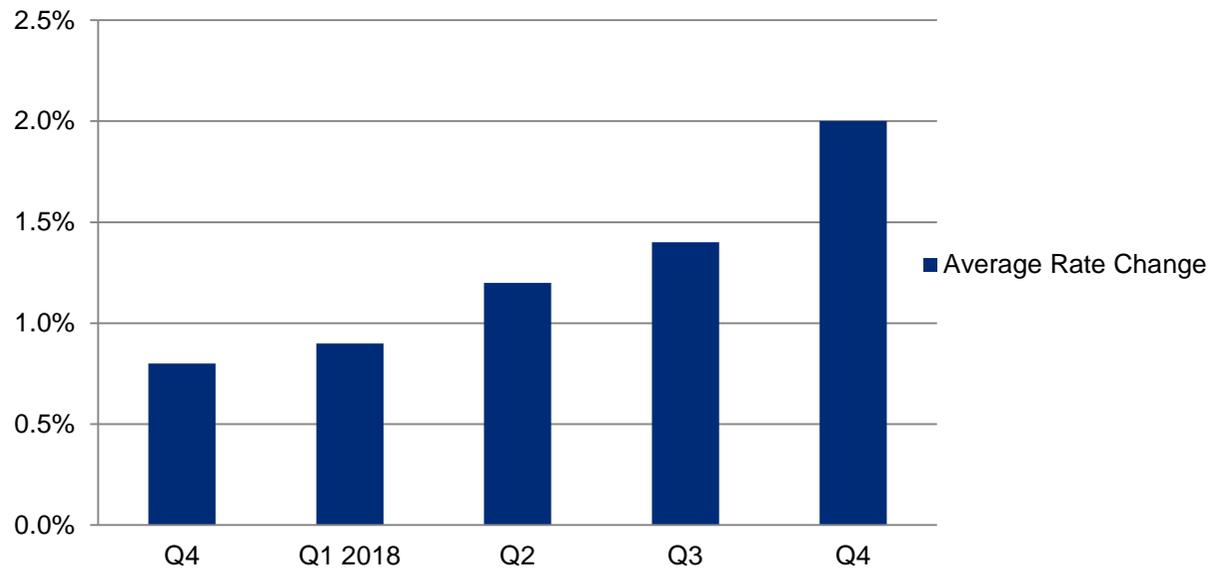
CASUALTY

- Premiums are increasing as the market transitions.
- We are witnessing greater underwriting discipline for highly exposed risks and those industries with a history of large losses such as Mining, Utilities, Municipalities, Energy, Auto.
- Insurers are reviewing their portfolios by Region, Industry, Exposure on an account by account basis.
- Market is looking for rate increases as it focuses on profitability.

MARKET UPDATE

A Changing Marketplace

Global Insurance Pricing Change – All Lines



MARKET UPDATE

A Changing Marketplace

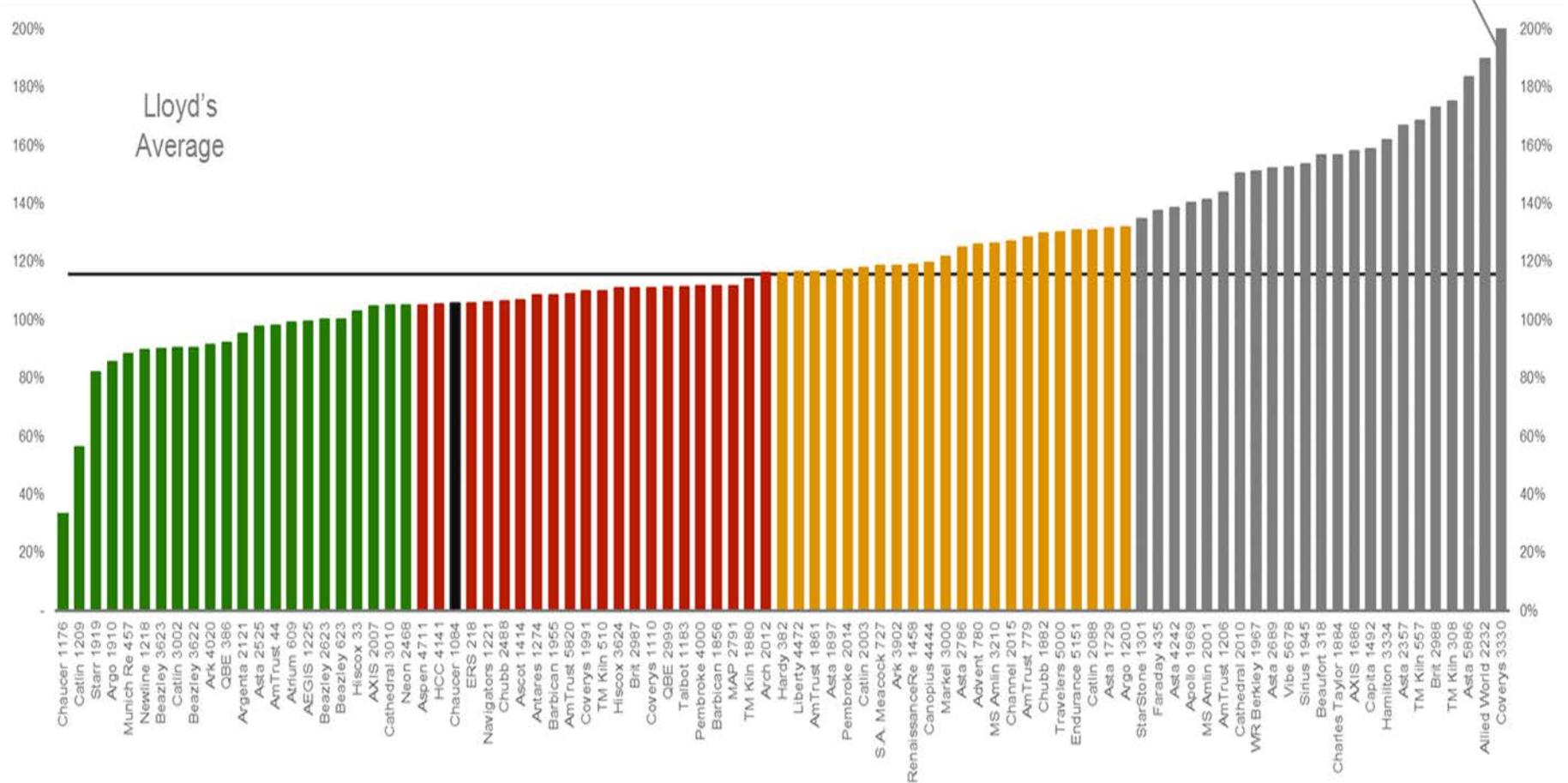
LONDON:

- The London market has seen the most meaningful shift in underwriting methodology particularly driven by:
 - Lloyd's business plan approvals
 - Poor results
 - New electronic placement platforms – delayed receipt of binding documentation
 - Brexit
- London remains a key source of capacity
- London market is at a critical inflection point given the heightened focus of Lloyds' on Syndicate performance. For clients, it means uncertainty and a market in a state of potentially significant change.
- Rate increases between flat for low exposure industries to >10% for higher exposed industries.

MARKET UPDATE

A Changing Marketplace

2017 Syndicate Combined Ratio



MARKET UPDATE

How to Prepare



Communicate: Work with your broker to request early preliminary expectations from insurers. Start early and maintain regular communication.

Differentiate: Identify positive underwriting characteristics to help differentiate you from others in your sector. Be prepared to address any underwriting concerns.

Meet: Underwriting meetings are even more important and it may be a worthwhile investment to have a couple of one-on-one meetings with your broker in advance of renewal.

Access: Your broker should approach both domestic and international insurers.

Evaluate: Evaluate most appropriate limits and deductibles to generate optimal pricing.

Negotiate: Work with your broker to understand the broader relationship with each insurer.

MARKET UPDATE

A Changing Marketplace



RED FLAGS

What to look for before your renewal becomes problematic:

- Changing risk profile – volatility in the business.
- Losses – obtain full loss picture with narrative around large losses.
- Who are your markets? Have they given any indications of change in underwriting approach or appetite?
- Recommendations not being implemented.
- Ensure all subjectivities have been adhered to.
- Have you provided your broker with full underwriting information (including COPE details)?
- Do you and your broker have a go-to-market strategy? Plan B?

MARKET UPDATE

Adjusting Your Approach to Insurance In A 'Disciplined' Market



- Begin thinking about your renewal sooner.
- Start with **good communication internally** to obtain underwriting updates; and **externally** with your broker to develop a good overall plan to start engaging markets.
- Communicate clearly and often with insurers. Have discussions in person whenever possible as it's too easy for underwriters to hide behind email on difficult renewals. .
- Work with your broker to present a fully comprehensive submission to the market and make it as detailed as possible. We need to differentiate you from others within difficult sectors. Tell the markets Your Story.
- All values and COPE information should be available in XL format.

MARKET UPDATE

Adjusting Your Approach to Insurance In A 'Disciplined' Market



- If approaching other markets, obtain full Loss history (10 years is best)
- Provide narratives on large contentious claims and explain how you have dealt them via risk management or move forward strategies; similarly with frequency issues.
- Provide **enough time** for insurers to do their analysis, ask questions, and for you to provide detailed responses.
- Rethink your RFP timelines to accommodate more analysis and negotiation.

MARKET UPDATE

In the News

The logo for Business Insurance, featuring the words "BUSINESS" and "INSURANCE" stacked vertically in white, uppercase, sans-serif font, centered within a solid blue square.

BUSINESS
INSURANCE

Business Insurance – May 16

Commercial insurance prices rise 3%: Marsh

Average commercial insurance prices increased 3.0% during the first quarter of 2019, according to the Global Insurance Market Index released Thursday by Marsh LLC.

Pricing for property risks increased 4.7% on average globally, slightly above the rates recorded in the previous four quarters, Marsh said, noting “property rates have increased globally every quarter since the catastrophe events in the fourth quarter of 2017.”

LLOYD'S OF LONDON & MARKET UPDATES

Q & A DISCUSSION

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