Strategic thinking under Solvency II

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Milliman Breakfast Briefing
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Strategy and large boulders

Why we are all a little like Indiana Jones

Liquidity

Quality of own funds

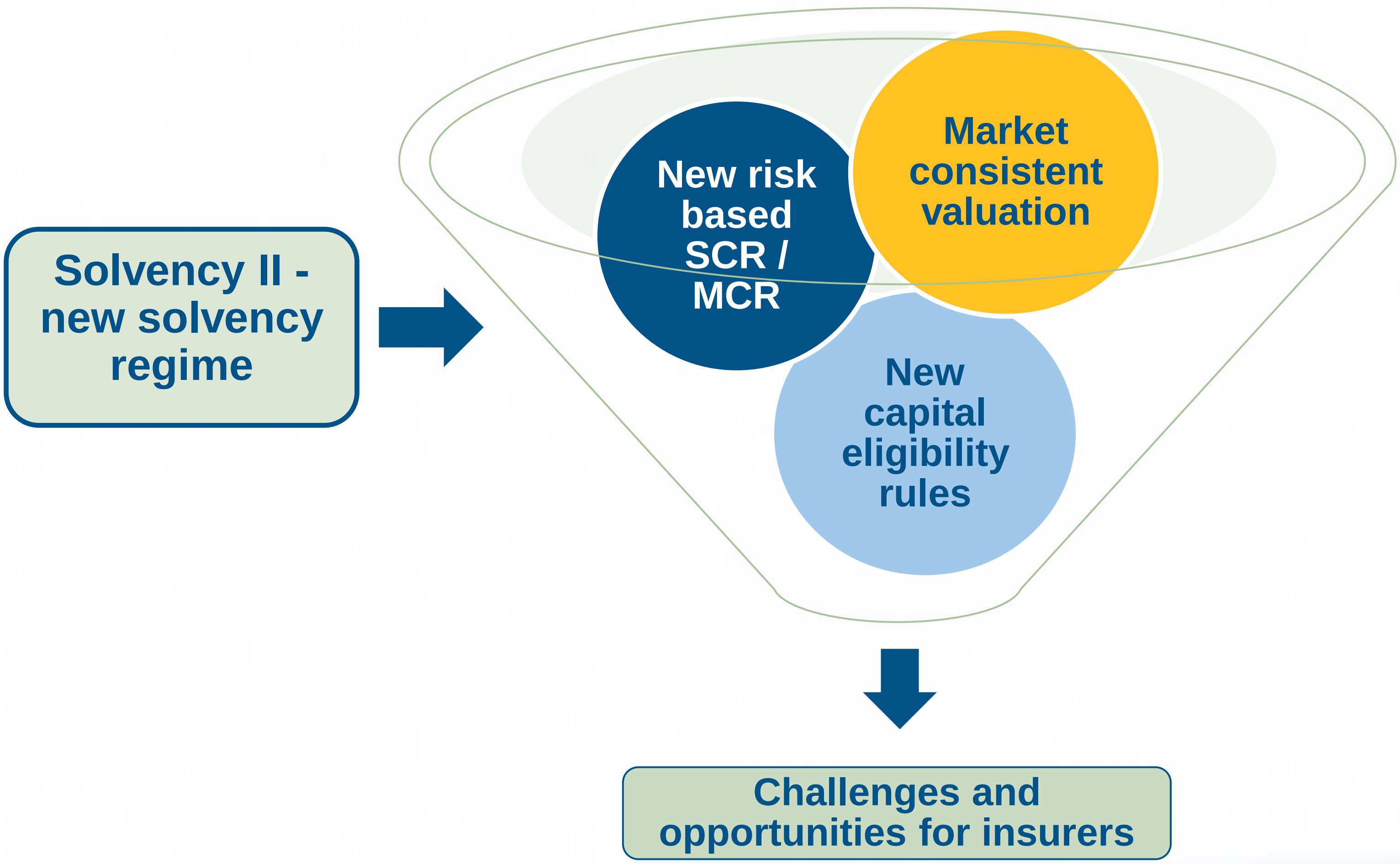
Product Strategy

Investment Strategy

Capital Efficiency

Reinsurance Strategy

Managing capital in a Solvency II world



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Why we may all be like Jerry Maguire

Solvency I

Solvency II

Solvency Cover 200%
Excess capital €100m

Solvency Cover 229%
Excess capital €225m

Dividend considerations

Do you have more capital than you need?

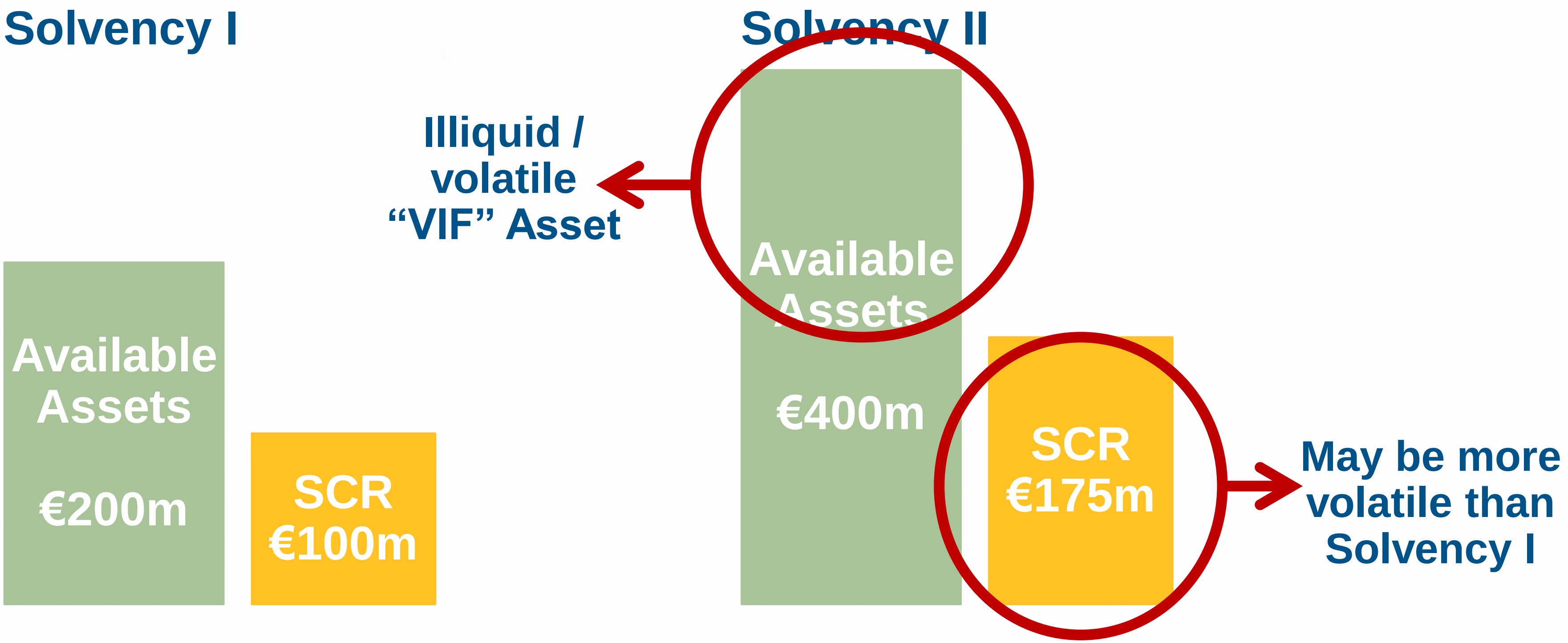
Dividend / Capital Management Policy

Medium term capital plan

ORSA

Liquidity and volatility may be bigger constraints under Solvency II

Drivers of improved Solvency II position?



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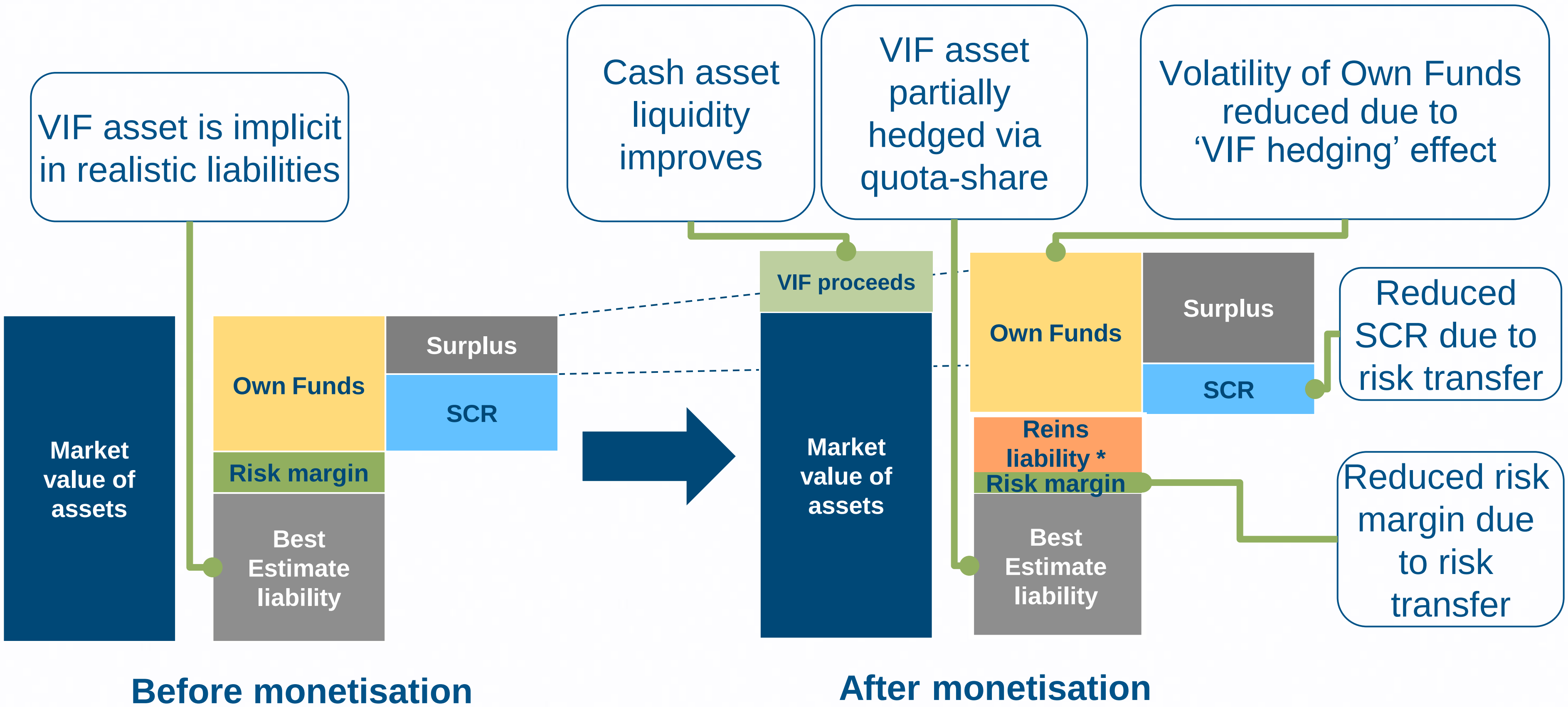
Reinsurance

VIF monetisation



No brainer? Increased liquidity and reduced volatility.
Reduced profitability? Additional risks?

* Strictly speaking, the reinsurance liability would be reflected as a negative reinsurance asset

Investment Strategy

Solvency I prescriptive rules

	%TR Individual	%TR Aggregate
Government Bonds	100%	100%
Listed shares / Bonds	5%	55%
Unlisted shares / Bonds	1%	2.5%
Unit trusts	5%	10%
UCITs	10%	20%
Cash / deposits	20%	100%
Land / Property	5%	25%
Computer Hardware	5%	5%
Gold	0%	0%
Works of Art	0%	0%
Bordeaux en primeur	0%	0%

Matching of linked liabilities with linked assets
Close matching of liabilities by nature, currency, duration.

Prudent Person Principle…

(What would your Mammy do?)

SCR should reflect any mismatch

Term of liabilities changes (Best Estimate, Lapses…)

Likely to require change to investment strategy, plus challenge in transitional period.

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Investment strategy flexibility - example

Unit Linked Matching

1. Shareholder is invested in units
2. Choice of underlying assets therefore delegated to policyholder
3. Assets chosen typically have the highest volatility, highest SCR shocks, and hence highest capital costs.

<u>Counterintuitively - "under-matching" linked liabilities can:</u>

Reduce risk , Reduce your SCR (perhaps significantly)
Reduce volatility of the balance sheet, increase liquidity…

Feels like another "no-brainer". But many potential pitfalls to navigate.

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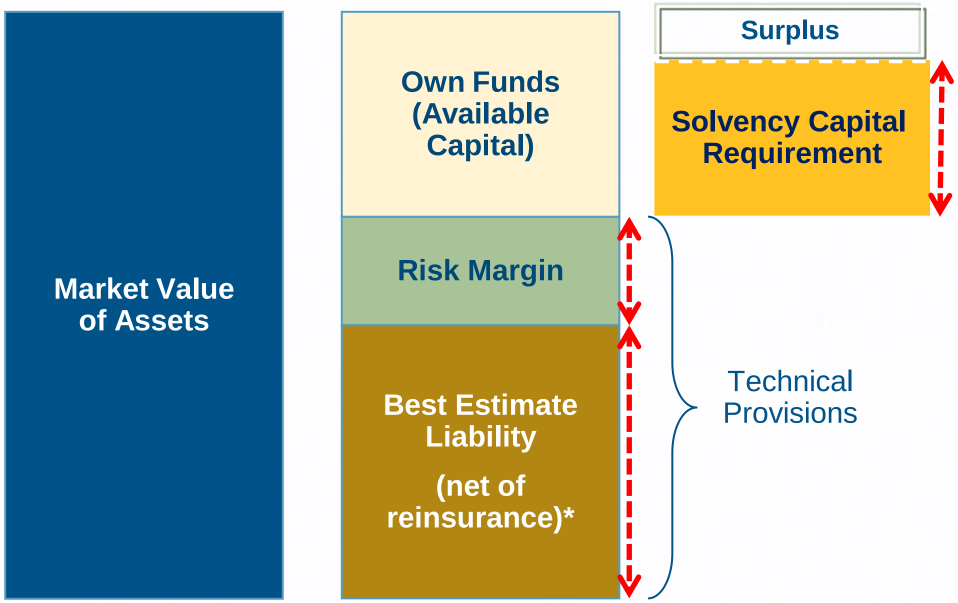
Reinsurance

Optimising traditional reinsurance strategy

Theoretical optimisation:

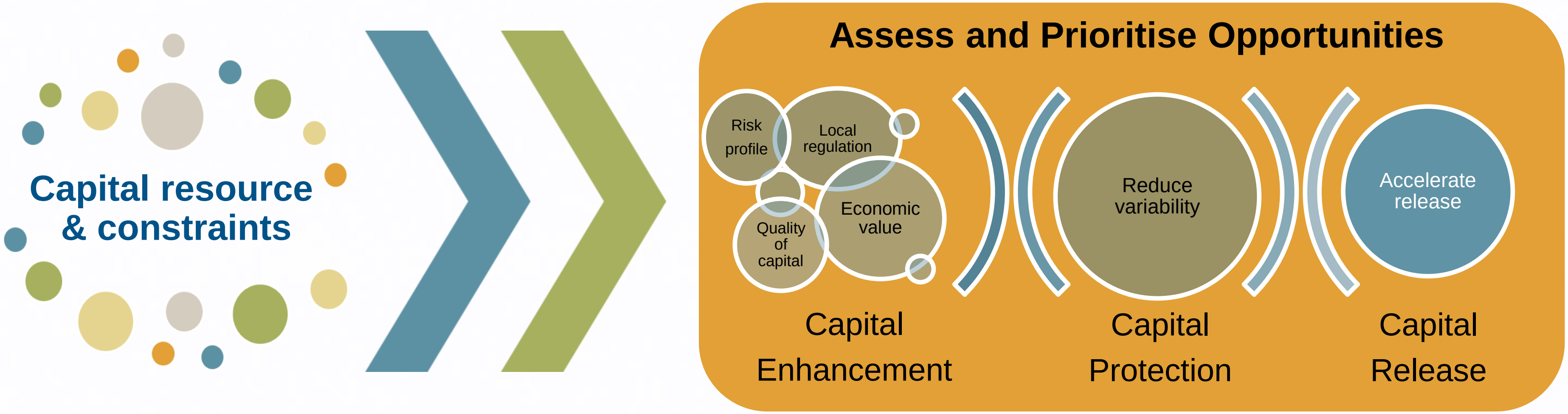
1. Maximise balance sheet value
2. Minimise SCR
3. Subject to constraints of risk tolerance, local restrictions, increased counterparty risk etc.



Scenario testing a range of carefully chosen reinsurance structures can identify opportunities for capital optimisation.

* Strictly speaking, this would be reflected as a reinsurance asset

Strategic implications of Solvency II
Final thoughts



Insurers need a consistent and systematic approach for the identification, evaluation and prioritisation of opportunities

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Plug for two papers