

Thriving on Change

16th

**General
Insurance
Seminar**



9-12th Nov 2008
Hyatt Regency Coolum



PIDO – Challenges for the Actuary

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**Presented by -
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Introduction

Contents

1. The Market
2. Actuarial reserving challenges
3. Other challenges for actuaries

Approach

- Review literature
- Compile and analyse historical performance
- Interview experts

Excluded Medical Indemnity



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1. Market



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Profile

- What is PIDO?
- Around \$950 million GWP
- Participants – plenty of capacity
- Soft market
- Penetration
- Market not yet mature



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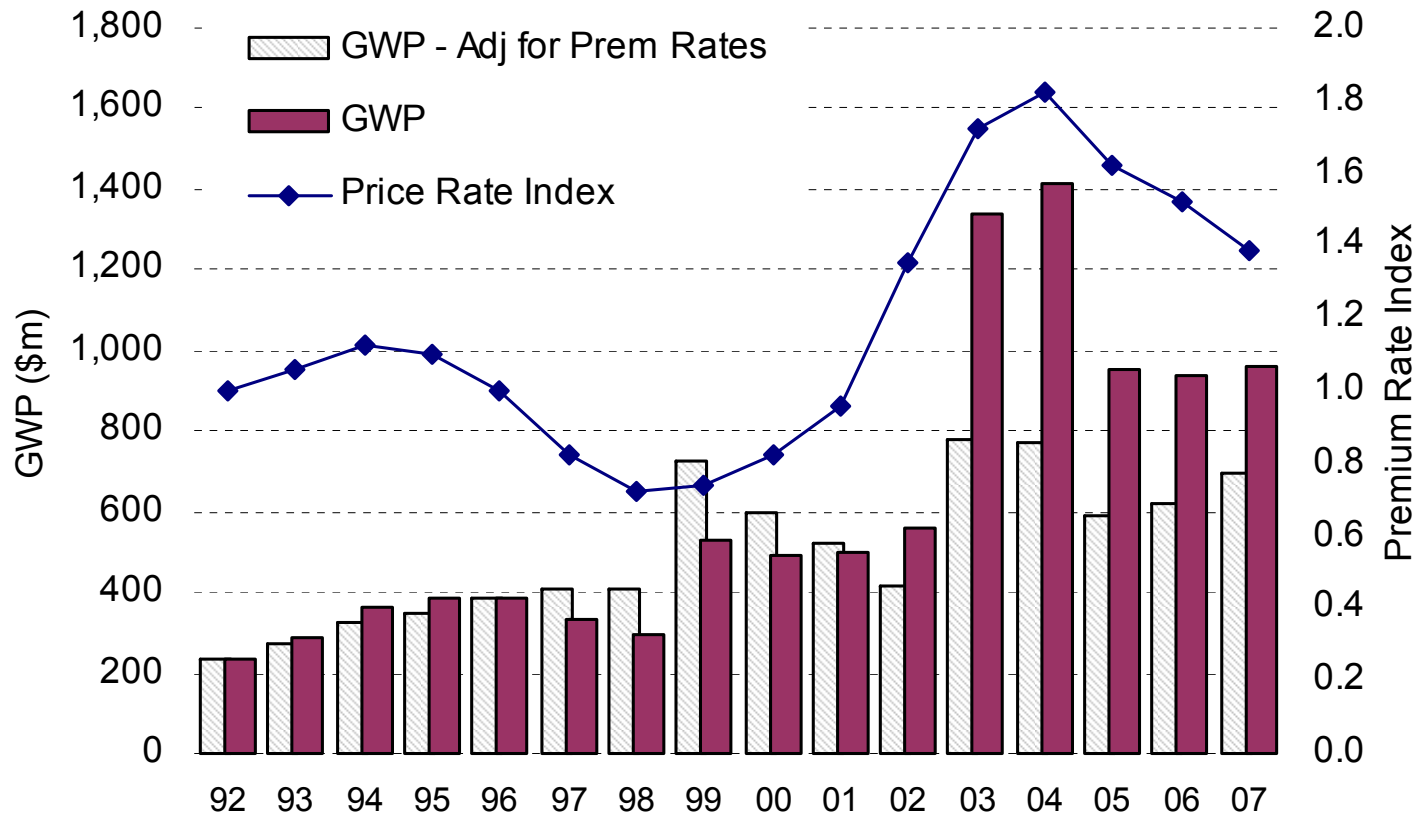
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Exposure



Source: APRA Statistics, JP Morgan Surveys

- Hard market in 2003/04 and recent soft market clearly evident



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Nature of Claims

- **Claims made**
 - Delays from notification to payment
- **More lumpy than other classes**
 - Low proportion of claims successful
 - High legal costs
- **Significant systemic claims risk**
 - Depends on economic cycle
 - Differs by profession and company



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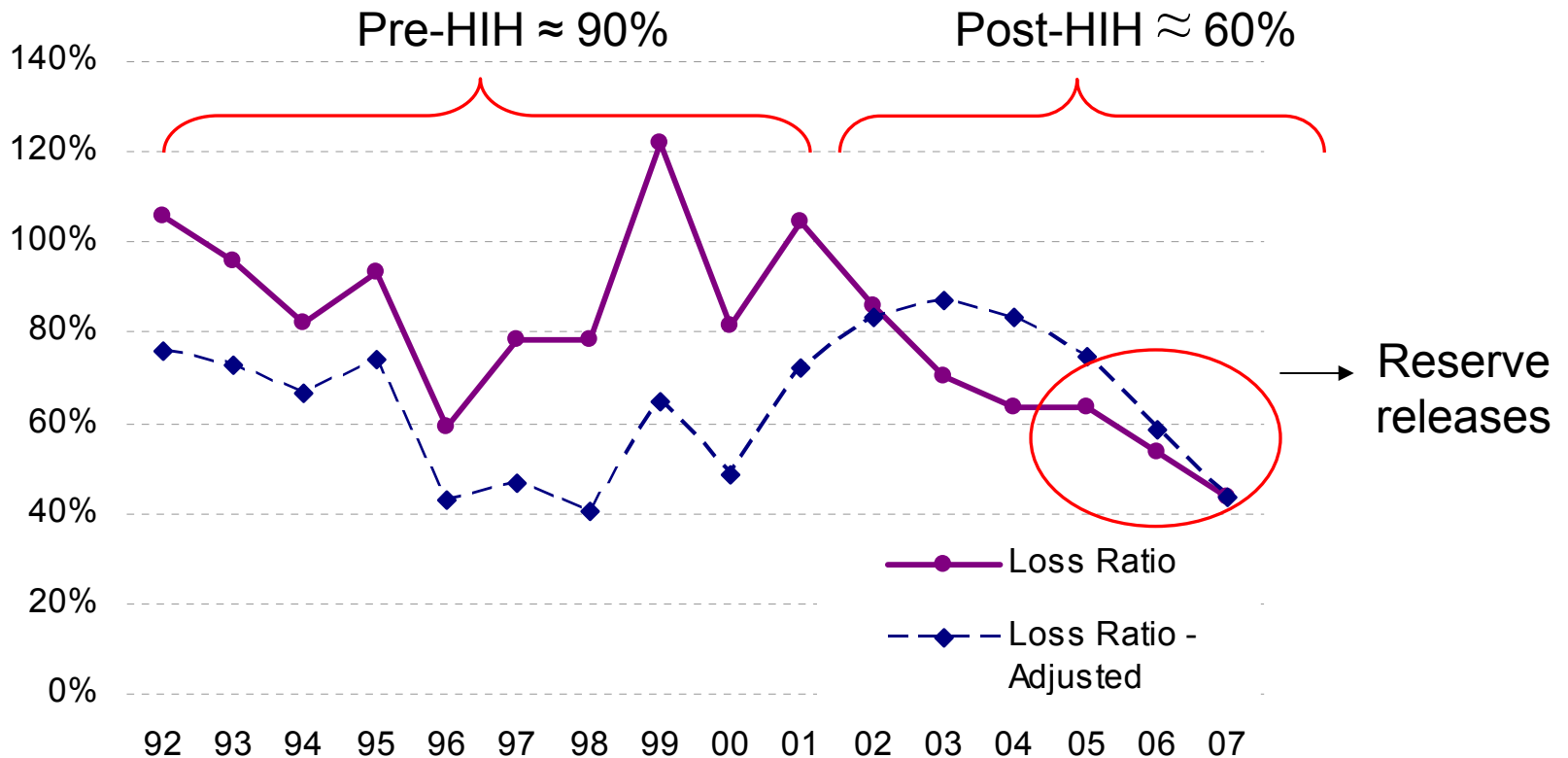


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Profitability

Financial Year Loss Ratios



Source: APRA Statistics



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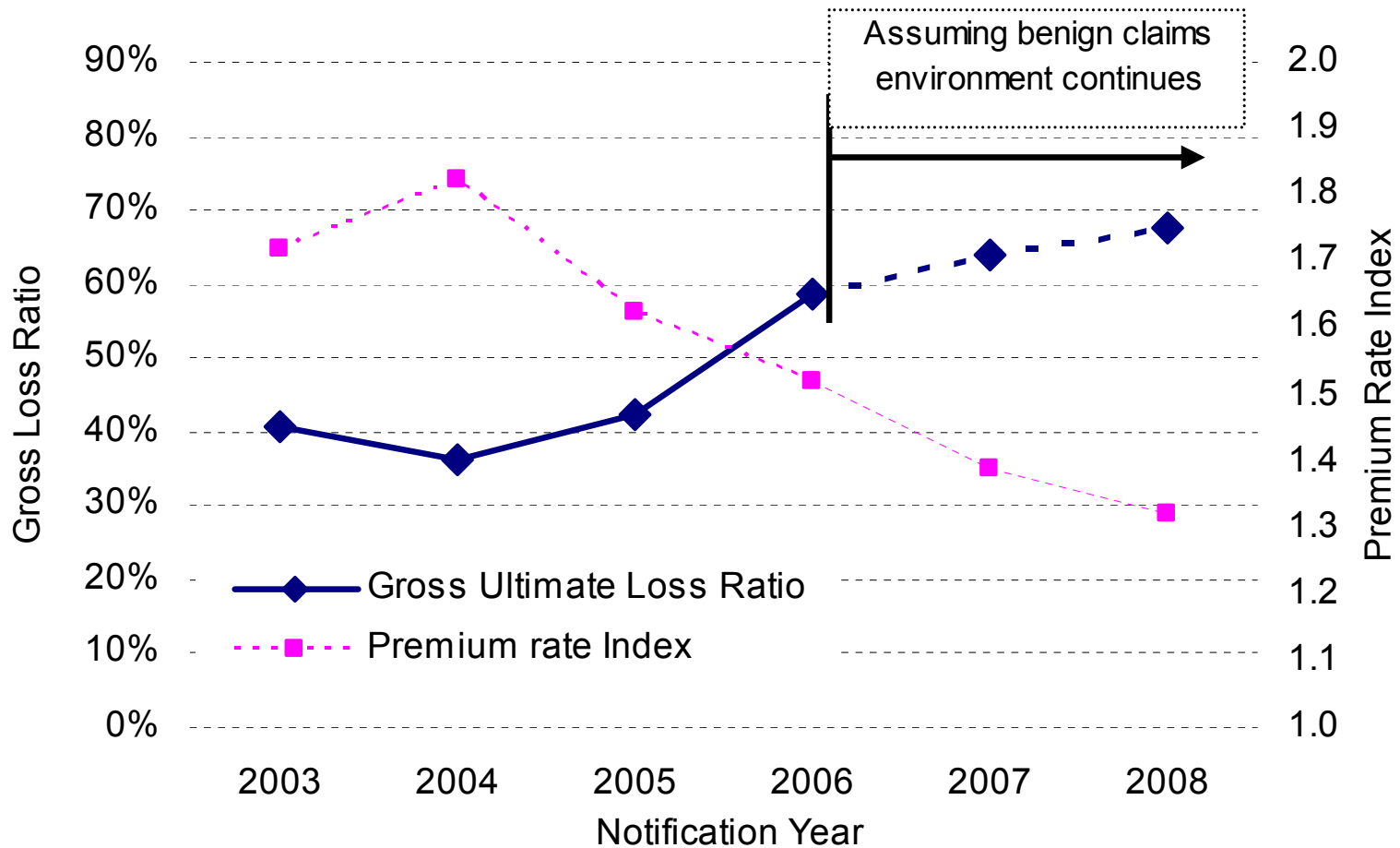
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Are current premiums adequate?





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Recent Claims Issues

- **Financial crisis**
 - Pockets where deterioration occurring -> more expected
 - But largely too early to quantify
- **Class actions and Side C**
 - Litigation funding
 - Securities actions coverage
 - Probably not sustainable
- **Tort reform**
 - Proportionate liability & causation



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2. Actuarial Reserving Issues



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Reserving Cycle

- Significant PIDO reserves releases in the last 3 years
- Has this influenced the pricing cycle?
 - Some say Yes!
- Should releases have been made earlier?
- Does pure BF produce central estimate reserving for claims with significant systemic risk?

We propose....



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Adjusted BF

- Include a “claims index” – *like the price index*

Illustrative Example

Assumed loss ratio in 2000 (pre claims index) 100%

Notification Year	Gross Earned Premium	Proportion of cost reported	Price Index	Claims Index	Pure BF Loss Ratio	Proposed Loss Ratio	Pure BF IBNR	Proposed Method IBNR
	\$m						\$m	\$m
2000	30	99%	70	100	100%	100%	0.3	0.3
2001	40	94%	81	90	87%	78%	2.1	1.9
2002	50	92%	115	70	61%	43%	2.4	1.7
2003	55	90%	147	70	48%	34%	2.6	1.8
2004	55	85%	155	70	45%	32%	3.7	2.6
2005	60	71%	138	70	51%	36%	8.9	6.2
2006	50	60%	129	80	54%	44%	10.9	8.7
2007	45	44%	118	100	59%	59%	15.0	15.0
2008	45	25%	112	125	63%	78%	21.1	26.4
Total	430				60%	52%	67.0	64.6



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Is it really Claims Made Reserving?

Mostly Yes, but need to consider

- Section 54
- Continuous coverage
- Run-off cover



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3. Other Challenges for Actuaries



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Current Challenges

- Heterogeneity & complexity of risk
- Changing global environment
- Limited portfolio size and data
- Difficulties in measurement of exposure and price movements



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Things the actuary can do

- Ensuring adequate large loss allowance and appropriate ILFs
- Ensuring adequate capital allocation and profit margin
- Robust measurement of price movements
- Allowance for changing environment



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Things the actuary can do (cont'd)

- Aggregation of exposures
 - Measurement by segment
 - Catastrophic impact of current financial crisis
 - Scenario testing
- Diversification benefits



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Questions