Agenda/Contents

Pricing
Underwriting cycle
PI market environment
Insufficient pricing for risk?

UK market loss ratio has followed a typical ‘cycle’ pattern

Source: 2004 FSA return data
How to price insurance business

Premium rate

Cost

Value to client

Competition / substitution
When pricing, what goes wrong?

Start with the gross premium
When pricing, what goes wrong?

Average non event year - ULR 68%

Source: 2004 FSA return data
When pricing, what goes wrong?

Large claims loading of 12%?

Source: 2004 FSA return data
When pricing, what goes wrong?

What allowance is made for larger event years?
When pricing, what goes wrong?

Assume commission is 15% of gross premium
When pricing, what goes wrong?

Assume management expenses are 10%
When pricing, what goes wrong?

Payment pattern implies investment income is 15% of premium (at 5% return)

Source: 2003 FSA return data
Pricing

Return on capital influencing pricing

Assuming;

- Minimum capital charge for liability business is 14%
- Required return on capital is 15%
- Risk free rate is 5%

⇒ Profit margin required is 11%
⇒ ULR is 79%
⇒ Large loss + Cat margin is 11% of premium
Large losses
1997 to 1999 underwriting years were affected by IFA mis-selling claims

Source: 2004 FSA return data
Large losses

With 1997 to 1999 excluded, we see that attritional claims account for 68% of gross premium.

Large loss loading = 12% of premium
= 15% of ultimate claims (excluding cats)

Source: 2004 FSA return data
Section two

Pricing
Underwriting cycle
PI market environment
UK premium rates have hardened since 2001

Source: 1996-2001 CBS indices (Lloyd's), non-marine
2002-2004 PwC estimates
US and UK markets had very similar cycles over the past decade

Accident year data, regulatory returns.

Source: 2004 FSA return data, 2005 SAS Schedule P
By stripping out the rate changes, assumed claims inflation is isolated

Linear trendline shows average UK claims inflation of 7.8%

Source: 2004 FSA return data, 2005 SAS Schedule P, CBS indices (Lloyd’s), non-marine, PwC estimates
Underwriting cycle

Trends

How will these claims and premium rates patterns develop in 2006, 2007....?

Source: 2004 FSA return data, 2005 SAS Schedule P, CBS indices (Lloyd’s), non-marine, PwC estimates
Section three

Pricing
Underwriting cycle
PI market environment
Allowing for sideways cover.

PI standard contracts currently leave insurers open to many claims from one source.

- IFA mis-selling
- No aggregate policy limits?
- RL aggregation clauses

**Issues**

PI market - an actuary's view
PricewaterhouseCoopers LLP

13 July 2006
Slide 21
Threats

Increasing capacity in the market

Underwriter discipline

Claims inflation
  • Solicitors fees
  • Property values
  • Court award inflation

£140m claim by the F.A. thrown out last week – a high profile award might have produced upwards pressure on rates ahead of September renewals?
Opportunities

Market growth – increasing penetration
• IT consultancy
• Media / advertising
• PR consultants, travel agents, interior designers….

£140m claim by the F.A. thrown out last week – may deter some negligence claims against solicitors?
Summary

• Are prices going forward going to be sufficient?
  - underwriting cycle
  - cats

• If competition continues, where can margins be improved?
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