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Study of Insurance Economics

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Creating & Managing Economic Value in Insurance Companies

Mel Carvill

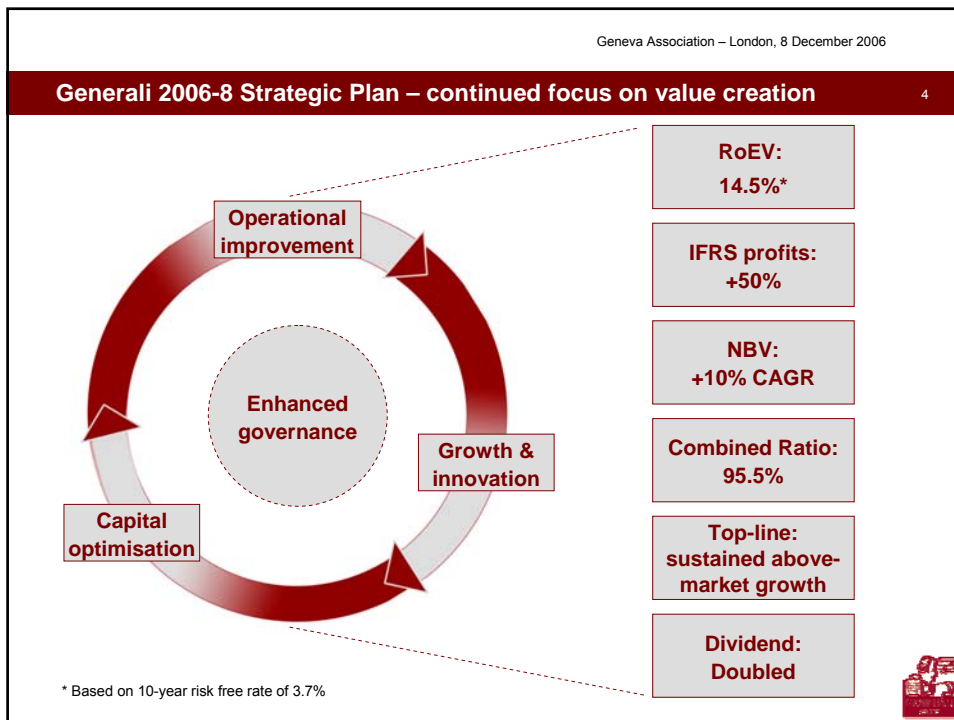
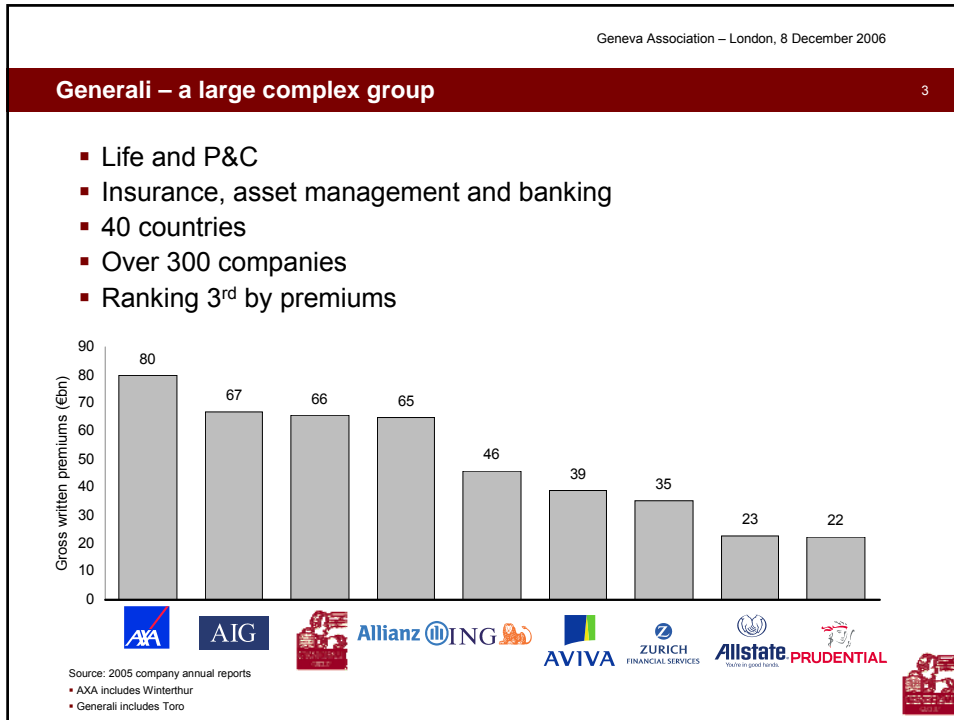
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- ▶ **Generali**
 - Measuring Economic Value
 - Managing and Creating Economic Value
 - Conclusion





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Generali

► **Measuring Economic Value**

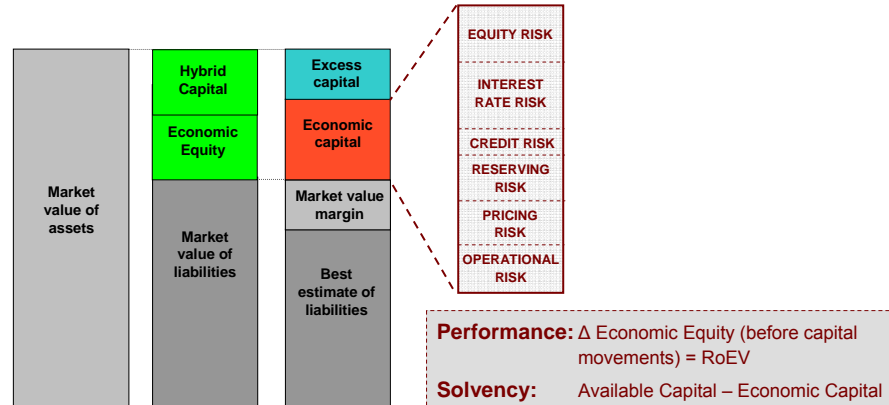
Managing and Creating Economic Value

Conclusion



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Using the Balance Sheet to measure solvency & performance 6




Market value of assets	Hybrid Capital Economic Equity Market value of liabilities	Excess capital Economic capital Market value margin Best estimate of liabilities
Assets	Available Capital	Solvency

Performance: Δ Economic Equity (before capital movements) = RoEV

Solvency: Available Capital – Economic Capital

DEFINITIONS:

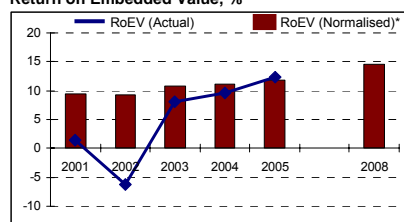
- Best Estimate Liabilities: expected value of stochastic cash flows to policyholders + senior debt at MV + other liabilities (IFRS value)
- Market Value Margin: cost of capital to support unhedgeable risks (CRO Forum)
- Economic Capital: based on Internal Model calibrated to 99.75% confidence over one year



Performance & Solvency measures aligned to capital markets

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Return on Embedded Value, %



- RoEV (Normalised)* rising trend due to impact of value based pricing initiatives, cost synergy programs and capital optimisation
- RoEV suffered during capital markets weakness 2001-2003
- With Cost of Equity ~9% insurers target sustainable ~15% RoEV to meet market expectations

* Normalised investment return and tax rate assumption, reviewed annually on 1 January



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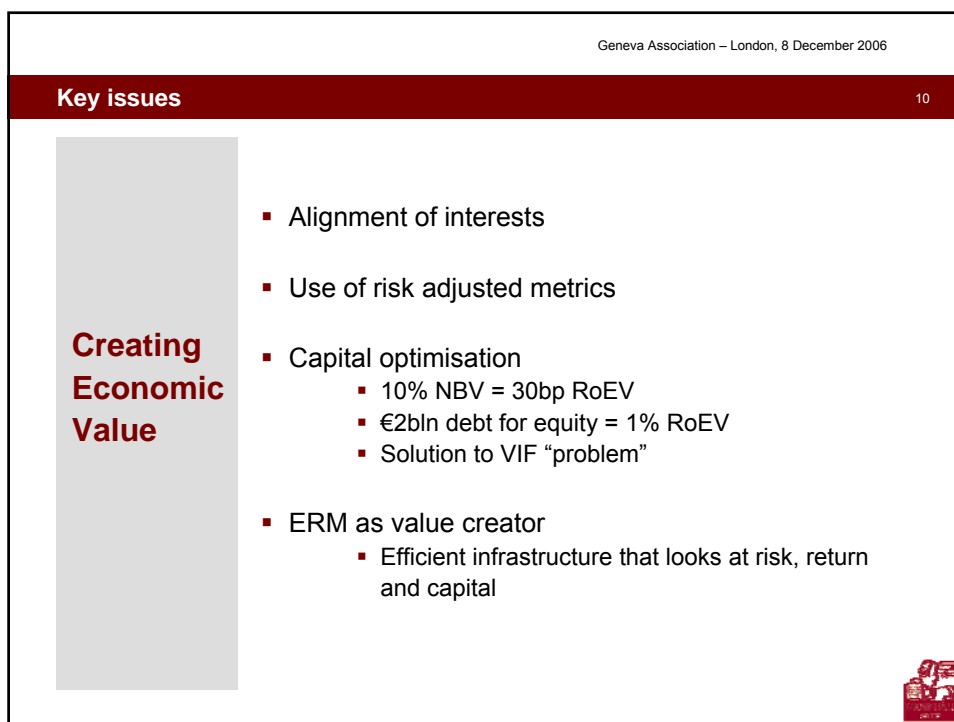
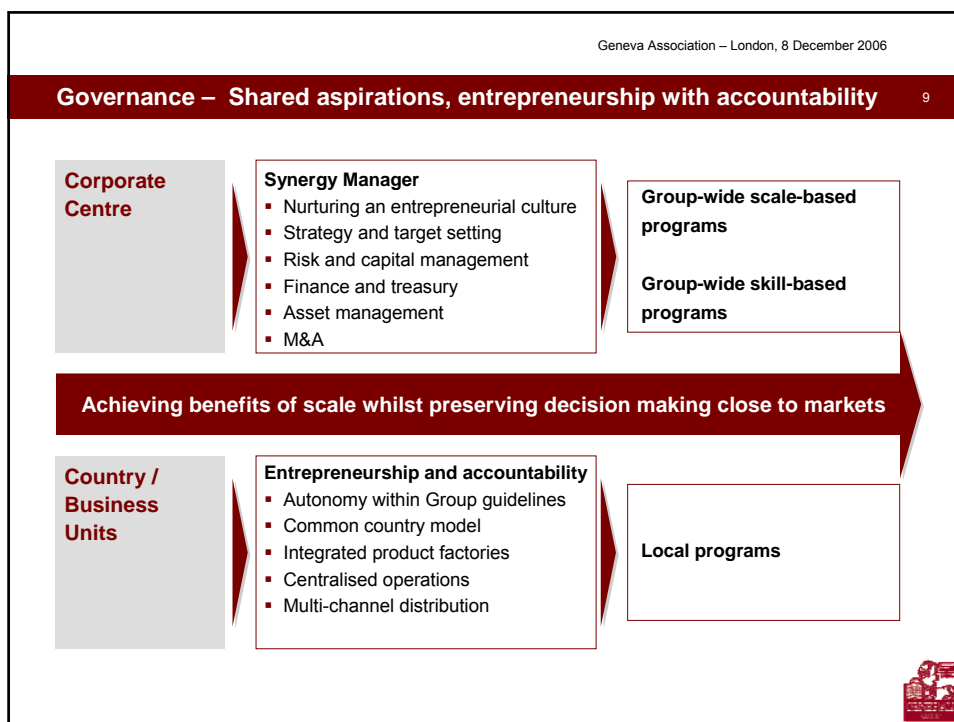
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Measuring Economic Value

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Three pillars 11

**Creating
Economic
Value**

- Operational improvement:
 - Common country model
 - Cross-border synergies
 - Scale based
 - Skill based
- Capital optimisation
 - Leverage (share buy-back / hybrid debt)
- Growth and Innovation
 - Product & Distribution innovation
 - Direct channels (web based, worksite marketing)
 - Aligned incentives with distribution network
 - New markets
 - CEE, China, India




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Some challenges to creating and managing value 12

**Some
Challenges**


- Centralisation vs decentralisation
- Need for global and local view
- Overcoming the silo mentality
- Fully integrate risk management into business decisions
- Regulation
- Minorities



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Recent Strategic Initiatives linked to creating value 13

Some of the value creating initiatives linked to capital and risk management	▪ Strategic Asset Allocation	▪ Lengthen bond durations ▪ Disciplined risk-based approach to credit and equity exposure
	▪ Life guarantees	▪ Introduced “at maturity” guarantees in Italy to replace “annual” guarantees in Italy
	▪ Strategic	▪ Exit Group Life business in Switzerland ▪ Exit Industrial Risk market in Germany ▪ Exit London Market business
	▪ Strategic Planning	▪ Focus on value versus volume (2003-5) ▪ Focus on risk reward relationship (2006-8)



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Measuring Economic Value

Managing and Creating Economic Value

▶ **Conclusion**



Conclusions

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**Creating &
Managing
Economic
Value**

- Focus on risk adjusted metrics
- Alignment of interests
- Business opportunities
- Efficiency
- Capital management

