

**Workshop on the new UAE regulations**

# **Impact of new UAE Insurance regulations on insurance companies' ERM**

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# Agenda



- 1. Risk profile and ERM capabilities**
- 2. New regulations and their impact**
- 3. Impact on industry performance**
- 4. Some final thoughts**

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**1. Risk profile and ERM capabilities**

2. New regulations and their impact

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# Risk profile varies by market and by company



## RISK PROFILE



## RISK PROFILE DEPENDS ON:

- Line and type of business
- Market profile (growth, competition etc)
- Investments
- Liquidity
- Operating environment (regulation, legislation etc)
- etc

# Matching risk profile to ERM capabilities

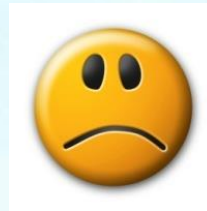


# Matching risk profile to ERM capabilities



A company's risk management capability needs to meet its risk profile

## RISK PROFILE



Risk management capability well below company's risk profile

## RISK MANAGEMENT CAPABILITY



# Matching risk profile to ERM capabilities



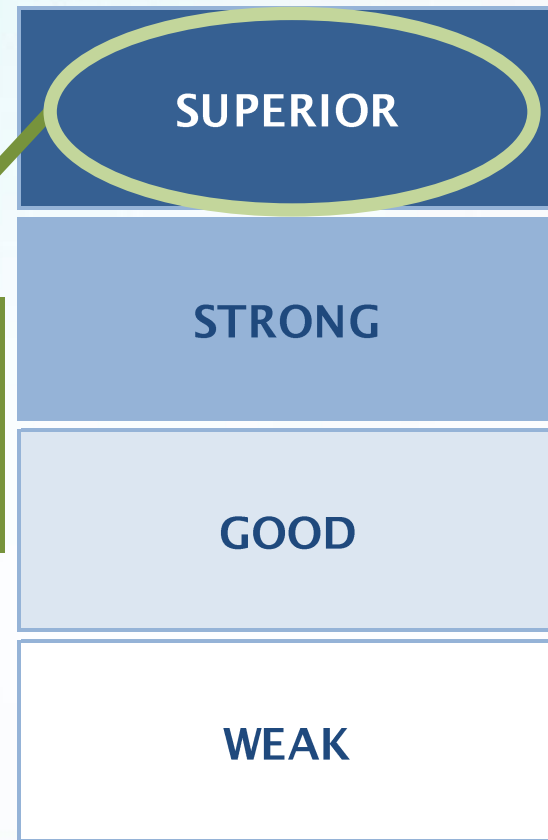
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## RISK PROFILE



Risk management capability well above company's risk profile

## RISK MANAGEMENT CAPABILITY





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**2. New regulations and their impact**

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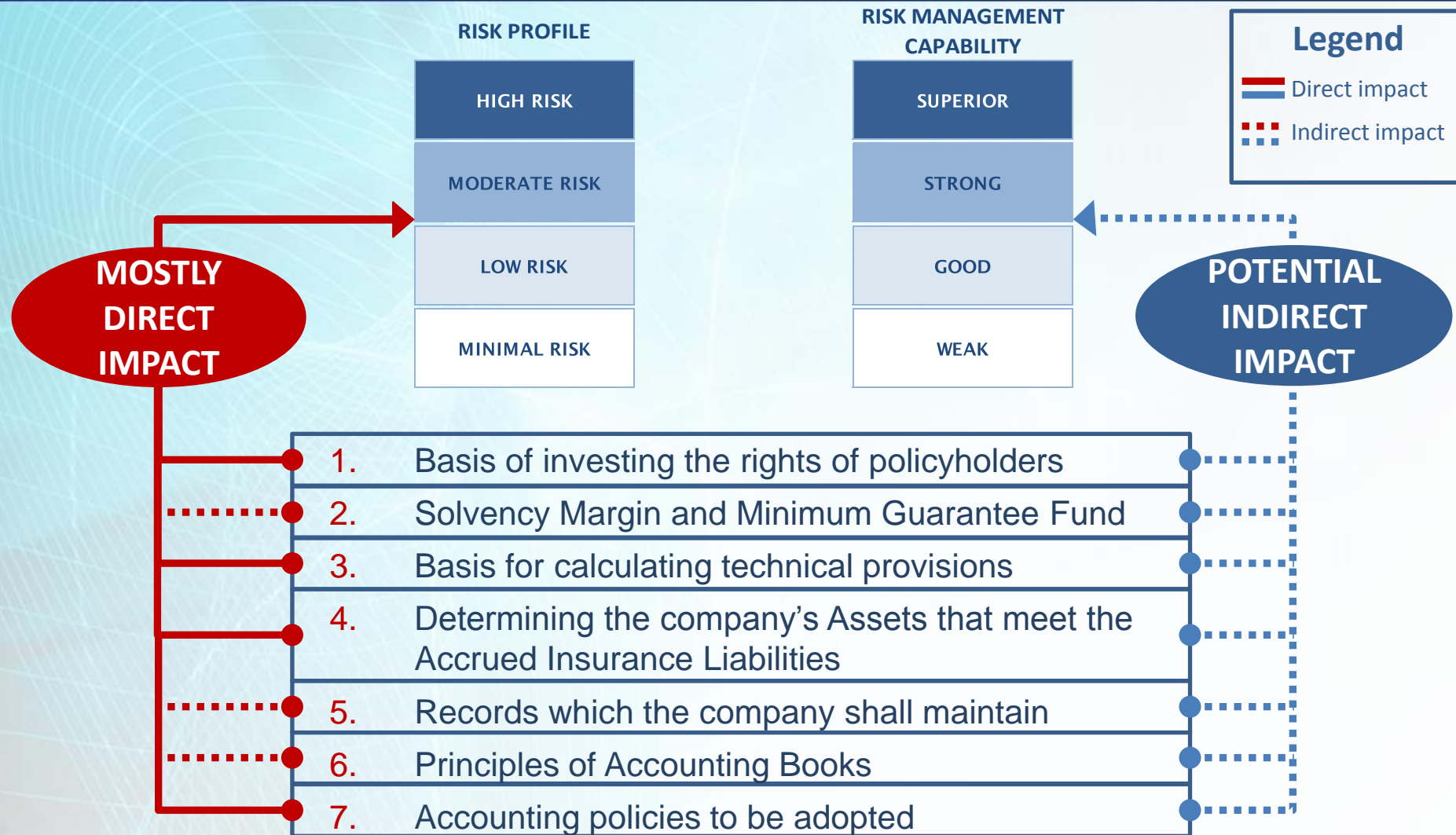
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# The new UAE regulations



1. Basis of investing the rights of policyholders
2. Solvency Margin and Minimum Guarantee Fund
3. Basis for calculating technical provisions
4. Determining the company's Assets that meet the Accrued Insurance Liabilities
5. Records which the company shall maintain
6. Principles of Accounting Books
7. Accounting policies to be adopted

# ...and their impact on companies' Risk Profile and ERM capabilities



1. Basis of investing the rights of policyholders **AND**
4. Assets that meet the Accrued Insurance Liabilities



### KEY PROVISIONS OF NEW REGULATIONS

- Introduction of new limits per category of investment
- Companies must have investment and risk management policies which will be in line with the company's risk appetite
- Assets need to match the insurance liabilities assumed
- Companies will establish investment committee
- Need to document Contingency funding
- Companies to conduct stress testing
- Investment for Accrued Liabilities to be in line with "prudent person" principle

### ELEMENTS OF RISK PROFILE

#### Investments

##### HIGH RISK

Low rated fixed income  
Concentrations, illiquid  
High % in equities  
Speculative derivatives

##### MEDIUM RISK

Mostly highly rated  
Mostly liquid  
Moderate % in equities  
Minimal speculation

##### LOW RISK

Mostly highly rated  
Mostly liquid  
Moderate % in equities  
Minimal speculation

#### Liquidity

##### HIGH RISK

Investment portfolio illiquid  
No outside sources of liquidity  
Mismatch in liquidity available vs. liquidity demands of product portfolio

##### MEDIUM RISK

Relatively well matched asset/liability portfolio  
Riskier assets matched to surplus  
Liabilities more protected from surrender charges

##### LOW RISK

No upcoming debt maturities  
Strong cash/cash flow available  
Sticky liabilities less likely to surrender

### POTENTIAL IMPACT ON ERM

- Companies forced to define proper risk appetite
- Companies establish independent investment committees

### IMPACT ON RISK PROFILE

- Significant de-risking of some investment portfolios
- Improved liquidity

# 2. Solvency Margin and Minimum Guarantee Fund



## KEY PROVISIONS OF NEW REGULATIONS

- Introduction of new Solvency Template for calculation of regulatory / solvency capital
- Minimum Capital Requirement (MCR) not linked to riskiness of operations
- Minimum Guarantee Fund (MGF) and Solvency Capital Requirement (SCR) linked to the new Template
- Companies obliged to have in place a documented risk management framework
- Companies to submit Solvency Template annually – template to be validated by the Actuary

## CURRENT MARKET PRACTICE

- Few companies have capital management tools (capital, ALM, cat-models)
- In most cases capital requirements are defined as “solvency capital” requirements
- Some cases whereby capital models are the responsibility of technical staff alone

## POTENTIAL IMPACT ON ERM

- Gradual improvement of understanding of riskiness of investment operations
  - Possibility of companies adopting new Template as internal capital model
- OR**
- View new regime as an additional inconvenience

# 3. Basis for calculating Technical Provisions



## KEY PROVISIONS OF NEW REGULATIONS

- Companies to appoint Actuary who is registered by the Authority.
- The Actuary to:
  - Review and approve the Technical Provisions
  - Assess the quality of the data
  - Provide the IA with annual report with current and future risks
  - Be professionally liable for the advice
- The Company shall report quarterly to the Authority and submit annually to the IA

## ELEMENTS OF RISK PROFILE

### Data quality

#### HIGH RISK

Poor data quality  
Data outdated  
Inappropriate for decision

#### MEDIUM RISK

Some data missing  
Some data miscoded/bulk

#### LOW RISK

High quality data  
Obtained quickly  
Adequate for decision  
Regular testing of data

## POTENTIAL IMPACT ON ERM

- In the medium-to-long term companies can develop the ability to link pricing with experience. This can lead to review of:
  - Risk appetite
  - Strategy

## IMPACT ON RISK PROFILE

- Improvement in data quality
- Independent verification of data

5. Records which the company shall maintain
6. Principles of Accounting Books
7. Accounting policies to be adopted



### KEY PROVISIONS OF NEW REGULATIONS

- Retention of records for at least 10 years
- Accounting to be in accordance with IFRS for all companies
- Quarterly and annual audited reporting (quarterlies with “limited review” of external auditors)

### ELEMENTS OF RISK PROFILE

#### Data quality

##### HIGH RISK

Poor data quality  
Data outdated  
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Some data missing  
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##### LOW RISK

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### POTENTIAL IMPACT ON ERM

- Only as a side-effect

### IMPACT ON RISK PROFILE

- May arise out of introduction of IFRS and difference in valuation of both assets and liabilities

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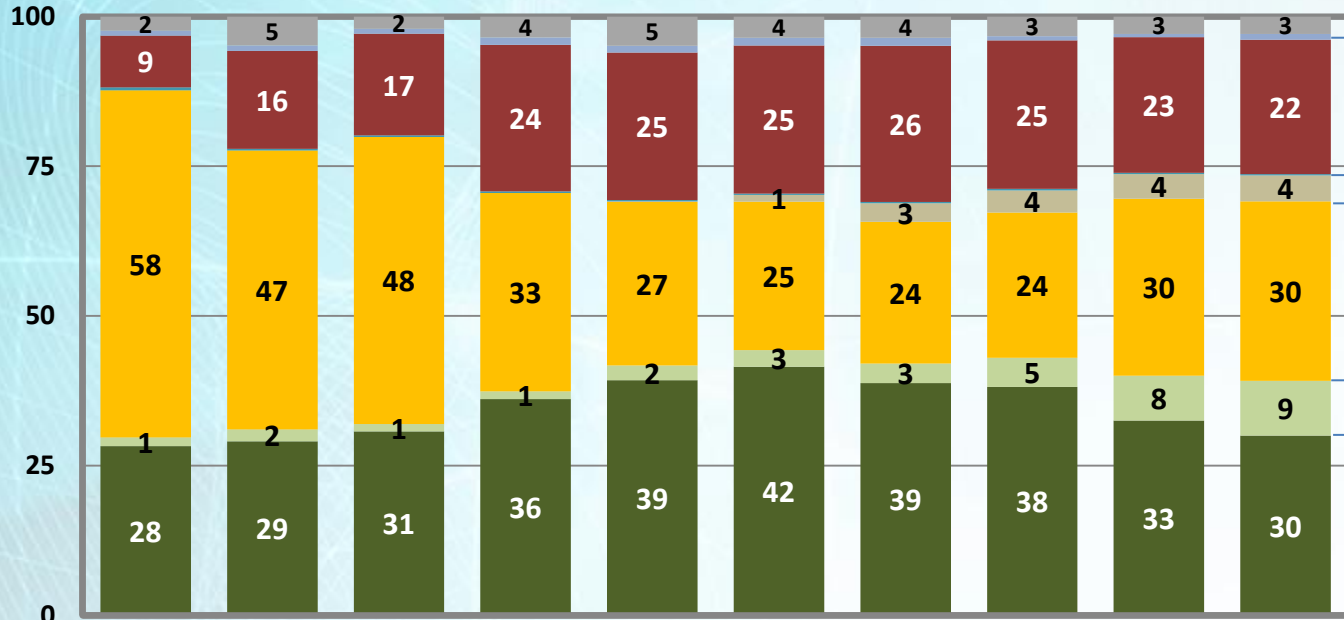


# No impact on asset allocation for the industry as a whole



**ASSET ALLOCATION ALL UAE COMPANIES (%)**

**NEW LIMITS**



< 30%

< 30% in UAE + < 20% abroad < 30%\*

> 5%

■ Cash ■ Bonds ■ Shares ■ UL Assets ■ Loans ■ Real estate ■ Affiliates ■ Other

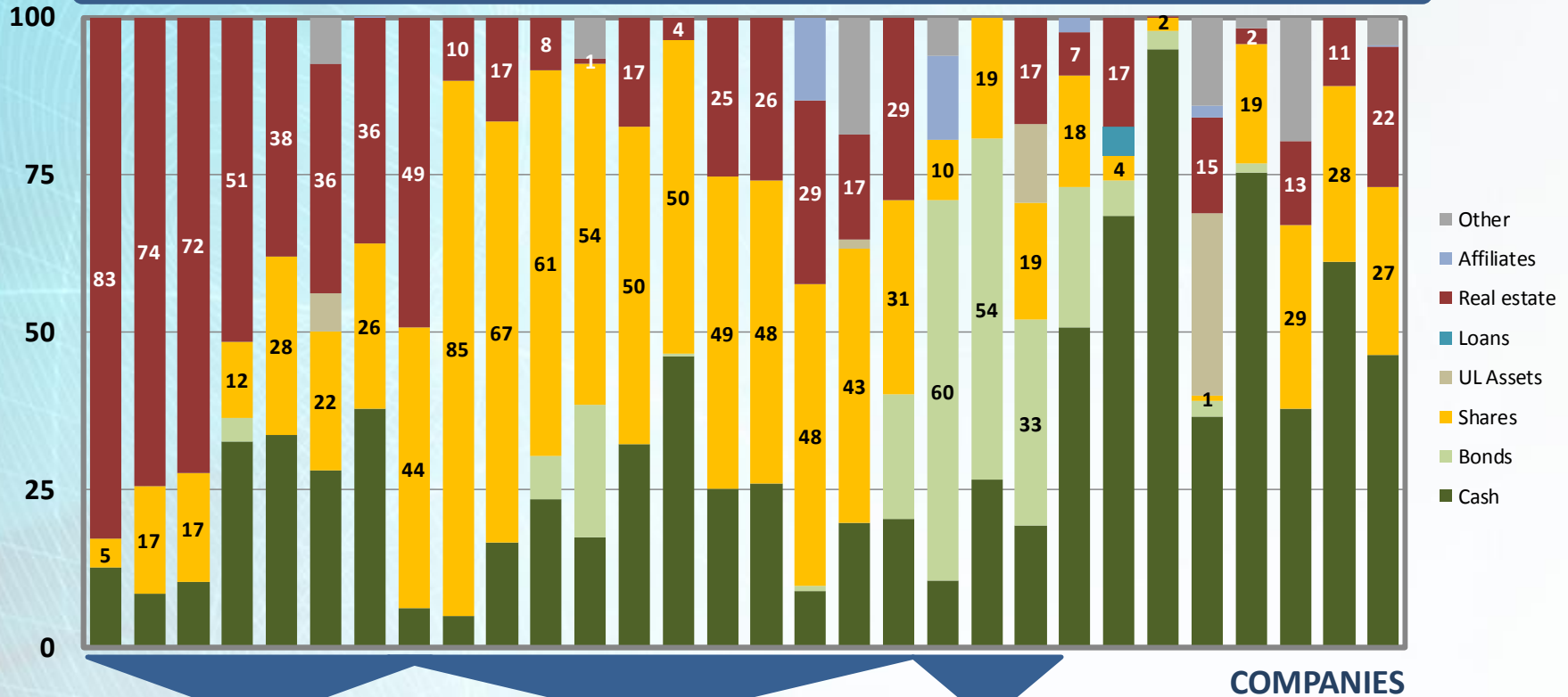
Source: AM Best - Statement File Global

\* For Government Bonds the limits are:  
 - 100% for UAE Government issues and  
 - 80% for other "A" rated sovereigns

# Significant impact for several companies



COMPANY-SPECIFIC ASSET ALLOCATION 31/12/2014 (%)



EXCESSIVE REAL ESTATE  
8 companies

EXCESSIVE EQUITIES  
12 companies

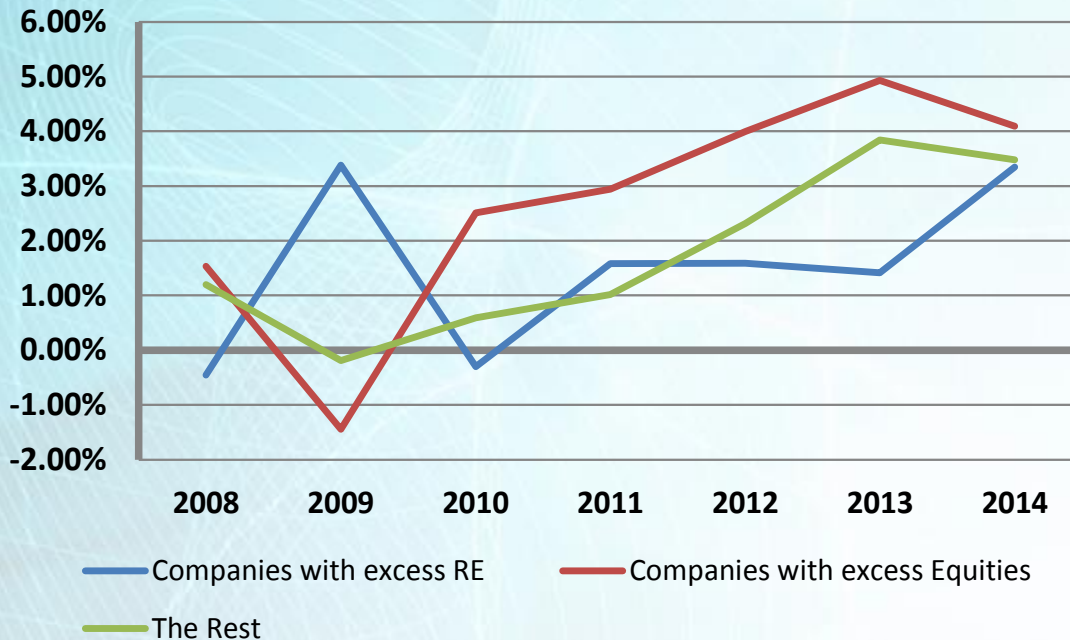
EXCESSIVE BONDS (?)  
3 companies

Source: AM Best - Statement File Global

# Asset reallocation will reduce investment volatility



HISTORICAL INVESTMENT YIELD  
BY INVESTMENT STRATEGY



Source: AM Best - Statement File Global

- Reallocating assets to comply with new regulation will reduce investment volatility
- Some companies will have to realise capital losses due to the illiquid nature of both Real Estate and local Equity markets
- However, this is unlikely to be the main driver for renewed focus on technical profitability

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# Story of two companies



## COMPANY "A"

## COMPANY "B"

<b>GWP</b>	100,000	100,000
<b>Claims reserves</b>	380,000	380,000
<b>Reinsurance</b>	XoL	Q/S
<b>Effective cession rate</b>	5% of GWP 2% of claims reserves	98% of GWP 98% of claims reserves
<b>Rationale</b>	Consistent with our risk appetite	Consistent with our previous practice

**Question: Which of the two strategies should the regulatory regime encourage?**

# Story of two companies



## COMPANY "A"

**GWP** 100,000  
**Claims reserves** 380,000  
**Reinsurance** XoL  
**Effective cession rate** 5% of GWP  
 2% of claims reserves  
**Rationale** Consistent with our risk appetite

## COMPANY "B"

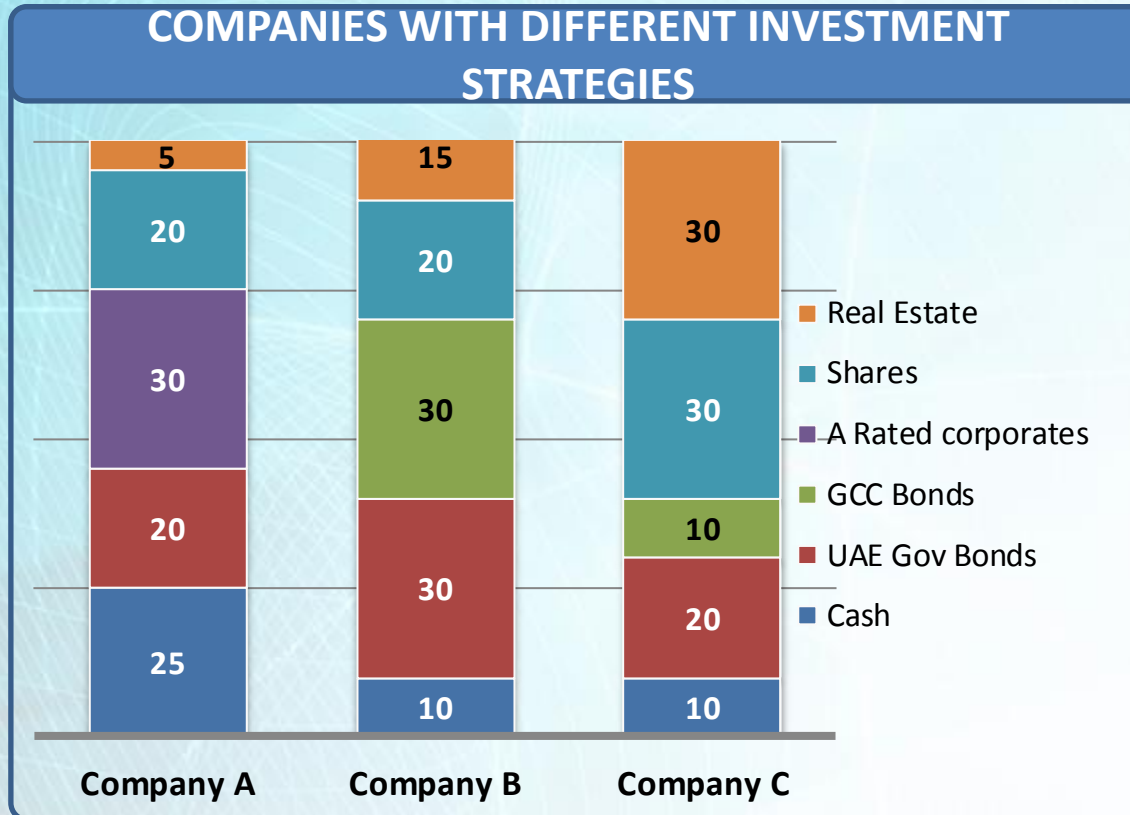
**GWP** 100,000  
**Claims reserves** 380,000  
**Reinsurance** Q/S  
**Effective cession rate** 98% of GWP  
 98% of claims reserves  
**Rationale** Consistent with our previous practice

### RESULTS OF THE SOLVENCY TEMPLATE

U/W risk NL	74,480	38,000
U/W risk Life	0	0
Investment Risk	0	0
Credit Risk	1	9,820
BSCR	74,480	39,248
Operational Risk	11,400	11,400
SCR	85,880	50,648
MGF	28,627	16,833

**Risk factor = 2.088% !**

# Story of three companies



- All three strategies are acceptable under new regime
- Key factors in decision making:
  - Availability of capital
  - Regulatory capital requirements
- Company B likely to have the lowest regulatory capital requirements for its investments (dependent on liquidity charges)

# Hurdles to implementation



- Available skill set in the market could result in IA and the companies depending on advisors for a long time
- Entrenched practices and opinions among current insurance Board Members
- Market inertia

**FAILURE TO IMPLEMENT WILL BE WORSE THAN NEVER HAVING ISSUED THE NEW REGULATIONS**