

Ready, set...

Insurers are ready to enhance reserving
and realise significant business benefits

Insurance market review 2020
The future of reserving

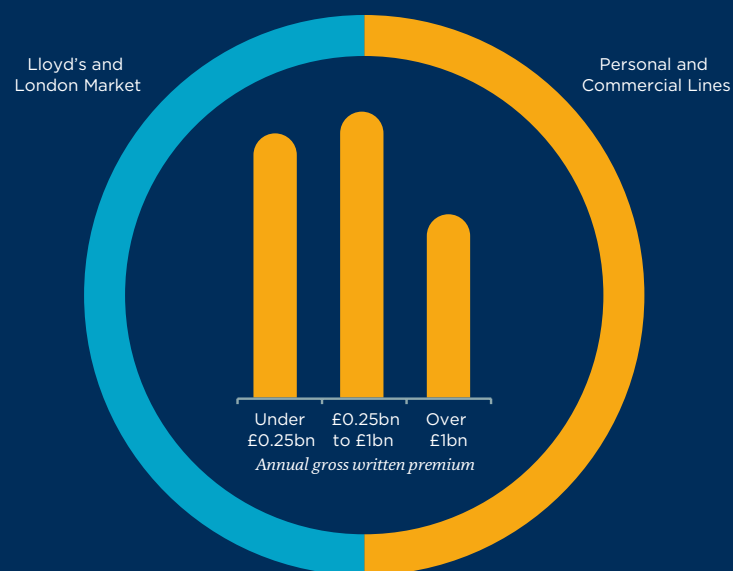
...Go!

We interviewed over 80 people across 36 UK general insurers to discuss:

- The reserving status quo.
- What their ideal process would look like.
- Key barriers to change.

This included interviews with Chief Actuaries, CFOs, CROs, Heads of Reserving and reserving practitioners, representing a cross-section of the UK general insurance market.

The graphic below provides further details of the firms that took part.



We would like to thank all of the firms who participated in LCP's 2020 insurance market review on the future of reserving.

If you would like to discuss any aspect of the review please contact Tom Durkin on +44 (0)20 7432 6606 or email tom.durkin@lcp.uk.com. Alternatively contact the LCP partner who normally advises you.

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Executive summary

Insurers see significant opportunities to enhance and streamline reserving. For 69% of firms, a major objective is to spot reserving trends earlier and to reflect these quickly in other business critical decisions.

We met with over 80 people across 36 UK general insurers to understand their reserving priorities and key challenges. We interviewed board members, other users of the reserves and those involved in preparing the reserves, to understand their different perspectives.

We found that firms are generally satisfied with traditional reserving approaches, but are ready to significantly improve benefits to the business from the reserving process:

- Earlier identification of trends is a top priority for 69% of firms, who are looking to ensure that all business critical decisions are based on the latest available information. Over two-thirds of these firms are planning to improve this over the next 12 months.
- Many firms describe their ideal reserving process as having significant automation, whilst retaining human oversight of key judgments. This provides a “best of both worlds” approach, and enables the reserving team to maximise time spent on value added analysis.
- The ability to drill down into the data and analysis is a very common feature in firms’ ideal reserving processes. Firms are looking to increase focus on the story behind the numbers, with a different level of detail for different users.

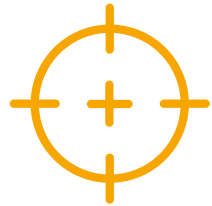
- A smaller number of firms are using or exploring individual claims reserving and alternative techniques including machine learning. To ensure success, any new approaches should be focused on key business requirements, easy to use, and readily explainable to the wider business.
- Managing competing priorities is the greatest barrier to change, with 75% of firms saying this is preventing them from enhancing their reserving processes. Overcoming this short-term barrier will enable insurers to build a long lasting reserving process that ultimately saves time. Other key barriers include data availability.

This report sets out key findings from the review including, on page 12, an overview of the overall ideal reserving process arising from the discussions. On page 13 we set out a practical approach for how you could achieve this.



Tom Durkin, Partner
Head of Insurance Consulting

Key findings



Earlier identification of trends is a top priority for **69% of firms**

See page 5

The ability to **“drill down”** or **“slice and dice”** into the data and analysis is a crucial part of an ideal reserving process for the majority of firms

See pages 7 and 8



Automation

features heavily in the ideal reserving process

See page 7



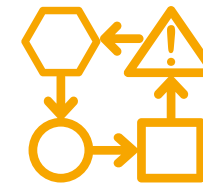
Most firms are satisfied with traditional reserving approaches, but are ready to improve benefits to the business from the reserving process

See page 8



Many firms are looking to improve reserving feedback loops, to quickly identify what is driving performance and reflect this in business critical decisions

See page 9



The top 3 priorities for 2020 are:

- Improving data quality
- Identifying emerging trends
- Quantifying and communicating uncertainty

See page 11



Competing priorities is a key barrier to change for **75%** of firms

See page 10



Less than one-third of firms cite lack of business engagement as a key barrier to change

See pages 10



Setting your **“levelling-up” path** for reserving is a zero risk approach to developing your ideal reserving process

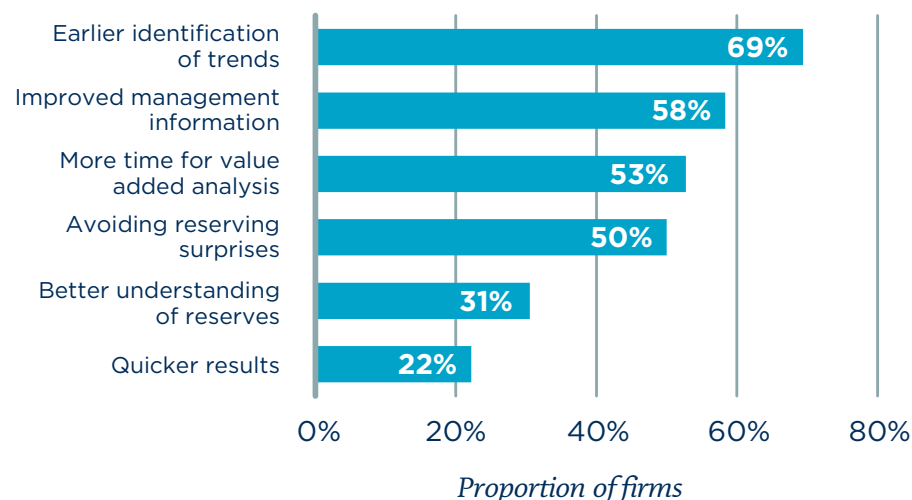
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Firms' top reserving priorities

We asked firms which of the following eight objectives are top priority and which they could (at a push) live without.

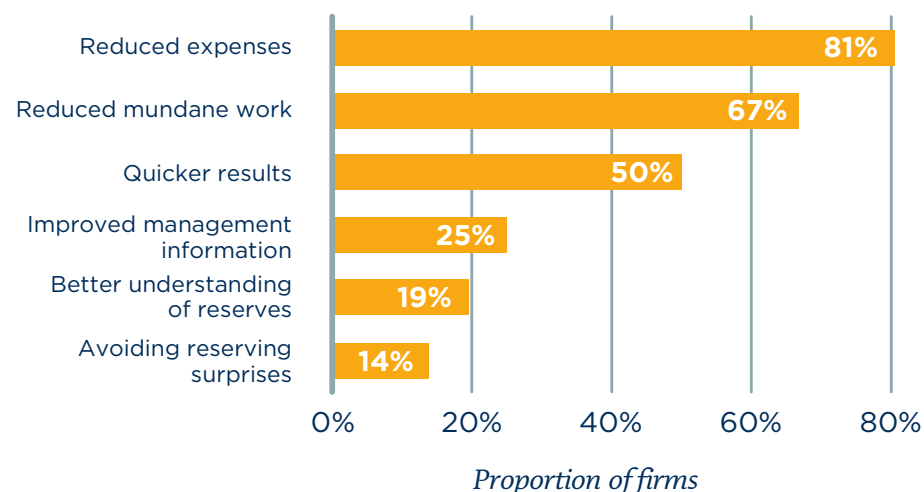
- Earlier identification of trends
- Avoiding reserving surprises
- More time for value added analysis
- Quicker results
- Reduced expenses
- Reduced mundane work
- Improved management information
- Better understanding of the reserves

The six top priorities:



- Earlier identification of trends is a top priority for 69% of firms, who are looking to ensure that all business critical decisions are based on the latest available information.
- Improved management information (MI), more time for value added analysis and avoiding reserving surprises were also top priorities for over half of firms. Many saw these objectives as complementary – for example, improving MI also helps improve understanding of the reserves.

Six things that insurers could live without (at a push):

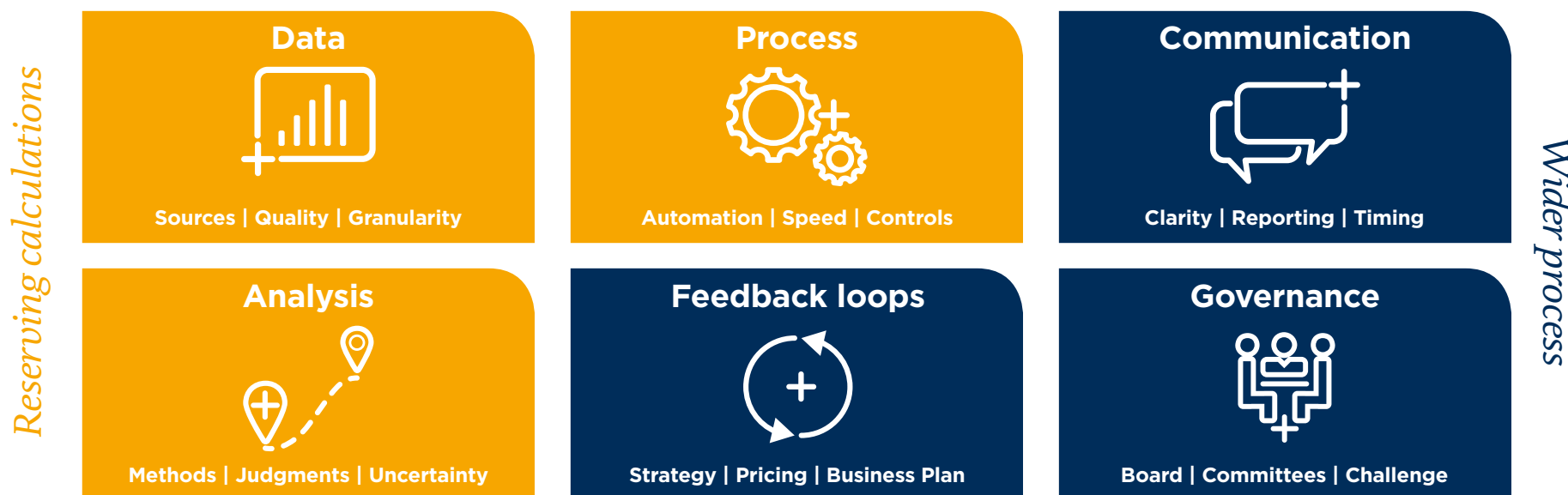


- 81% of firms could live without reducing the expense of running the reserving process, reflecting the significant value that many placed on the reserving work.
- 50% of firms could (at a push) live without quicker results. This is perhaps surprising, as it contrasts with other financial services where real-time calculations are the norm. On exploring this further, this finding reflected firms not needing the end-to-end reserving process to be quicker, although having quicker intermediate results at their fingertips would be welcome.

Features of the ideal reserving process

We asked firms to describe features of their ideal reserving process

Firms described their ideal reserving process covering the six areas summarised below. Three of the areas – data, process and analysis – focus on the reserving calculations. The other three – communication, feedback loops and governance – cover the wider reserving process.



The following sections summarise the themes from the interviews in each of these six areas.

Features of the ideal reserving process



Data

- **A single reliable data source.** The starting point for the ideal reserving process is to have high quality data available quickly, without the need for manual processing. Ideal features include a seamless link between claims and policy level information, and readily available transactional data.
- **Ability to “drill down” or “slice and dice” the data.** This is a major theme running throughout – including across data, analysis and communication of results. Firms recognise the significant time savings this offers, and value being able to deep dive into the data to understand emerging trends.
- **Improved data quality.** The two most common areas for improvement are reinsurance data, and where insurers are reliant on external third parties such as bordereaux and binders.
- **Enriched data using external sources.** In each case, the source of external data is highly specific to the type of insurance. For example, marine insurers mentioned detailed ship tracking data. Motor insurers mentioned weather patterns and data from the Ministry of Justice Claims Portal.
- **Better benchmarking.** The ideal process includes more tailored benchmarking against other insurers – looking beyond the raw benchmark numbers for the reasons behind any similarities or differences.



Process

- **Automation.** The ideal process includes a “best of both worlds” blend of automation and human oversight. Most firms mentioned automation of standard reserving approaches to give more time for more complex areas. Some mentioned the need to manage the risk of automation leading to overconfidence in the results or the junior team becoming de-skilled.
- **Faster process.** Many firms would ideally have faster reserving calculations, but few are targeting “real time” results. A key focus is on streamlining the process, for example by reducing overlap between early and fast close. However, as mentioned on page 5, 50% of firms could (at a push) live without quicker end-to-end results.
- **Early warning indicators.** These would ideally be automated metrics that flag any trends and anomalies that start to emerge in the periods between the main quarterly reserving cycles. This enables firms to quickly understand and respond to any new features in the data, without having to wait for the next reserving cycle.
- **Better allocation of results to different levels of granularity.** Firms would ideally use fewer approximations when allocating results, to avoid the risk of inconsistencies between different views on the book.
- **Reduced reliance on Excel.** Firms recognise both the flexibility and the risks of relying on Excel for the reserving process. Ideally, many would reduce or eliminate its use from the core parts of reserving.

Features of the ideal reserving process



Analysis

- **Traditional reserving methods.** The majority of firms are satisfied with traditional reserving methods, such as development factor modelling. Where these are working well, there is little impetus to change the underlying calculations, but firms are ready to improve the process around the calculations.
- **Alternative reserving methods.** A small number of firms are using or targeting alternatives to traditional reserving techniques to help enhance their reserving. Examples include individual claims or stochastic reserving, or analysis of unstructured text.
- **Easier sensitivity testing and what-if scenarios.** The ability to quickly consider the impact of different assumptions on the reserve estimates is a key feature in many insurers' ideal reserving processes. This is seen as a valuable way to understand the underlying uncertainty in the reserves.
- **Clearer view on the key drivers of change between reserving cycles.** For example, this could come from clearer actual versus expected analysis, or from analysis of the most material assumptions.
- **Ability to drill down.** This major theme features again in the ideal process for many firms. This time, drilling down into the results from the analysis.



Communication

- **Story behind the numbers.** Nearly all senior users of the reserving results mentioned including a greater focus on the story behind the numbers – considering the “why” as well as the “what”.
- **Communication tailored for each user.** Being able to seamlessly switch between different levels of detail for different users was a common requirement.
- **Clear communication of uncertainty.** Many firms mentioned the ideal process would include an increased use of tangible scenarios to explain uncertainty. This is consistent with their aim, mentioned to the left, of making it easier to calculate these scenarios.
- **Reserving dashboard.** Some firms are targeting a reserving dashboard, to allow the business to explore and drill down into the results. Others raised potential risks of this approach, such as the end user misinterpreting or misusing the results.
- **Automated reporting.** Automation in reporting covered all aspects, eg producing the reserving committee packs or the main reserving report. Other examples included automated early warning flags, such as an automated flag to identify emerging trends in case reserves.

Features of the ideal reserving process



Feedback loops

- **More effective feedback loops.** Many firms are looking for the findings from the reserving process to feed quickly into other business functions (and vice versa), including pricing, claims, strategy and risk. Examples cited include:
 - Using reserving to test and continually improve the accuracy of case estimates.
 - Reserving being a key feed into business planning.
 - A clear link between emerging trends identified from reserving, and what this means for the wider business.
 - Quicker identification of what is driving performance.
- **Closing the feedback loop.** Some firms have actuaries and other members of the team working across multiple areas to help facilitate stronger links between the different areas. For example, individuals working across pricing and reserving.



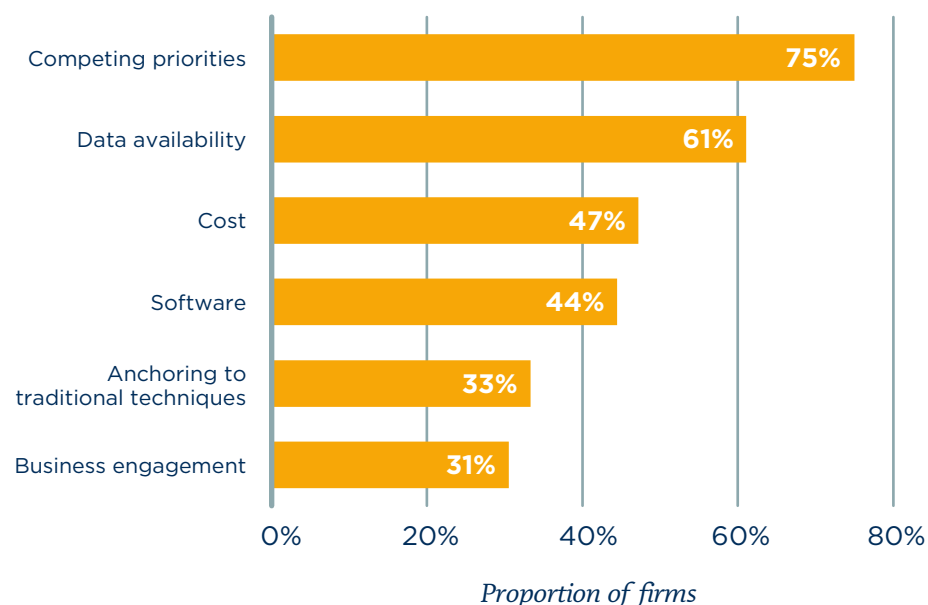
Governance

- **Overall working well.** Most firms are satisfied that their reserving governance is well established and working well. However, some firms are looking to improve the quality of board challenge.
- **Sub committees.** In firms with the most effective reserving processes, the majority of challenge is by sub-committees, with board oversight of the overall process. This enables the main board to focus on what the numbers mean for running the business.
- **Understanding trends.** A number of firms are looking to increase their focus on trends and/or underlying business performance, rather than the point in time balance sheet.

Barriers to change

We asked firms about the key barriers to change in their reserving process.

Key barriers to change



- Managing competing priorities is the greatest barrier to change, with 75% of firms saying this is preventing them from enhancing their reserving processes. Overcoming this short-term barrier will enable insurers to build a long-lasting reserving process that ultimately saves time.
- Data availability is the second key barrier, with 61% of firms citing this. Firms mentioned a range of reasons for this, including:
 - A requirement to improve overall data quality to provide a foundation for more enhanced reserving techniques.

- Lack of historical data capture meaning high quality data is not available.
- Challenges around managing legacy data systems.

Challenges around data are particularly prevalent when relying on external third parties, such as binders and bordereaux data. Data related to outwards reinsurance is also a key area of challenge – for example, where the level of granularity differs between the gross and net data.

Firms are addressing data challenges through improving data systems, and integrating disparate data sources. Firms are also introducing stricter “upstream” controls around data, for example prohibiting binding of risks until a certain level of data quality is met.

- The 44% of firms that said software was a key barrier to change were mainly personal and commercial lines insurers. Many of these firms would welcome enhanced reserving software to more readily modernise and streamline their reserving process.
- In contrast, the 33% of firms that mentioned anchoring to traditional techniques as a key barrier were mainly Lloyd’s and London Market insurers.
- Less than one-third of firms cited lack of business engagement as a key barrier to change – reflecting the significant value that many firms place on the insight gained from the reserving work.

Areas of focus for 2020

We asked about firms' plans for 2020, covering top priorities, other high priorities and areas where firms are satisfied with the current process.

Top priorities for 2020

- Ensuring good data quality
- Identifying emerging trends
- Quantifying and communicating uncertainty
- Robustness of reinsurance estimates

Other high priorities

- Overall efficiency of reserving and roll forward processes
- Gaining real insight from actual vs expected analysis
- Effective coordination of different reserving processes (Solvency II, TPs, GAAP, IFRS17 etc)

Satisfied with current process

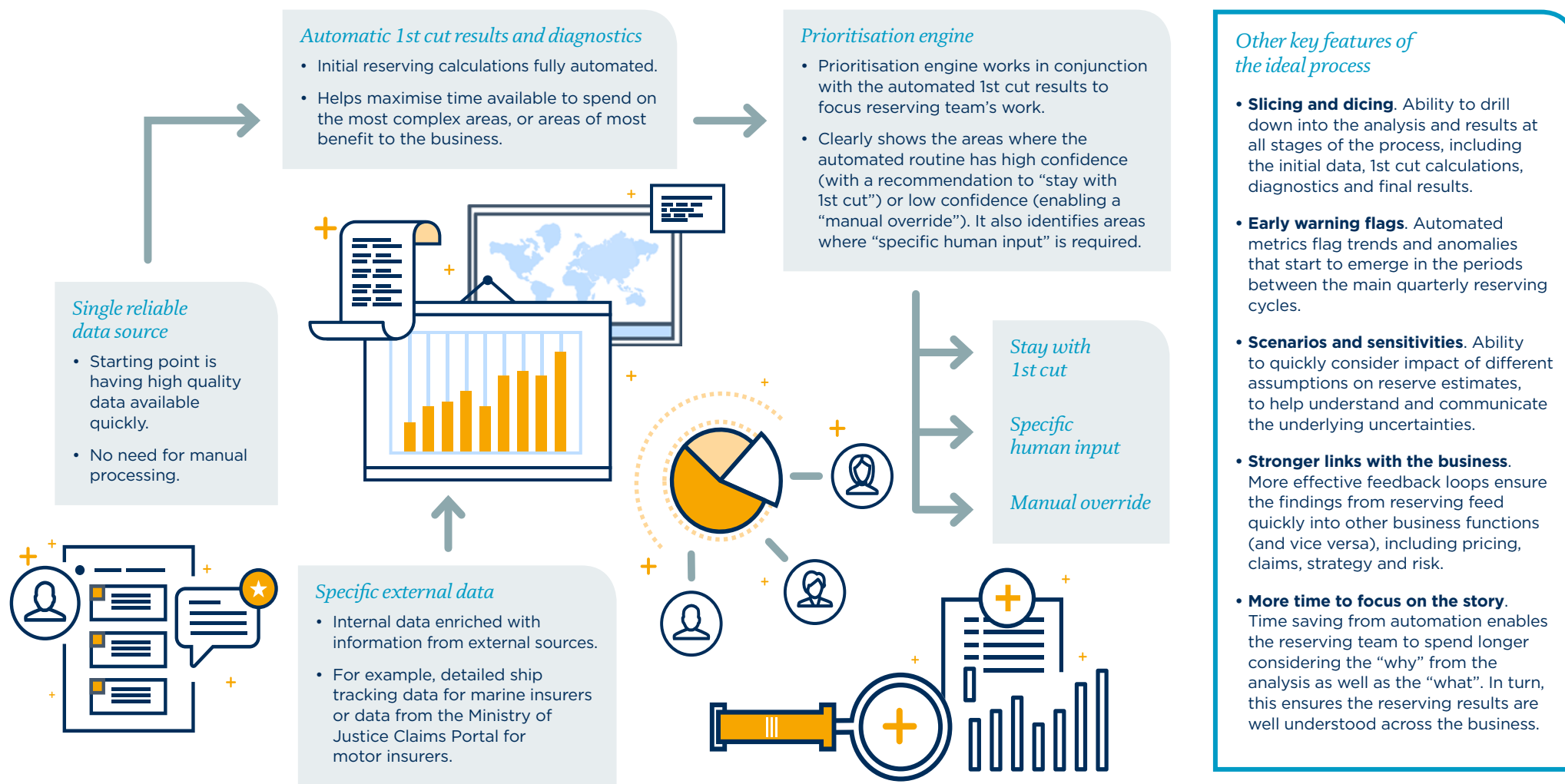
- Quality of external input
- Pre-empting challenge from regulators and auditors
- Ease of incorporating new classes of business
- Quality of interaction with claims, pricing and underwriting teams

- Unsurprisingly, there is significant overlap between firms' ideal reserving processes and their top shorter term priorities for 2020. The shorter term focus is typically on specific developments that help the firm move towards the overall ideal process. For example, firms described tangible developments they have planned to improve data quality, such as streamlining the process of linking claims level and policy level data to ensure this is available earlier in the reserving cycle.
- There were also differences between the shorter term areas of focus and the longer term ideal. For example, gaining insight from actual vs expected analysis is a key area for short term improvements (under "other high priorities" above), but was rarely mentioned as part of the ideal process. This may reflect the planned developments being incremental improvements rather than significant changes to the analysis.

- Most firms are satisfied with the ease by which the reserving process can be updated for changes in the business such as introducing a new class of business – although in many cases this was due to new classes being rarely introduced rather than the process being particularly slick.
- Firms are generally satisfied with the quality of interaction with the claims, pricing and underwriting teams. As mentioned on page 9, firms are also looking to improve feedback loops – in these cases, they were satisfied with the flow of information into the reserving process, but were looking to improve the feedback loop out of reserving back to the wider business.

The overall ideal reserving process

Bringing the results of our market review together, the diagram below illustrates what an ideal reserving process could look like.



Setting your levelling-up path

A “levelling-up” approach splits the journey towards your ideal reserving process into distinct tangible steps. Each step brings measurable benefits within a short time horizon.

Levelling-up in steps helps ensure that business as usual priorities do not prevent you from achieving long-term enhancements.

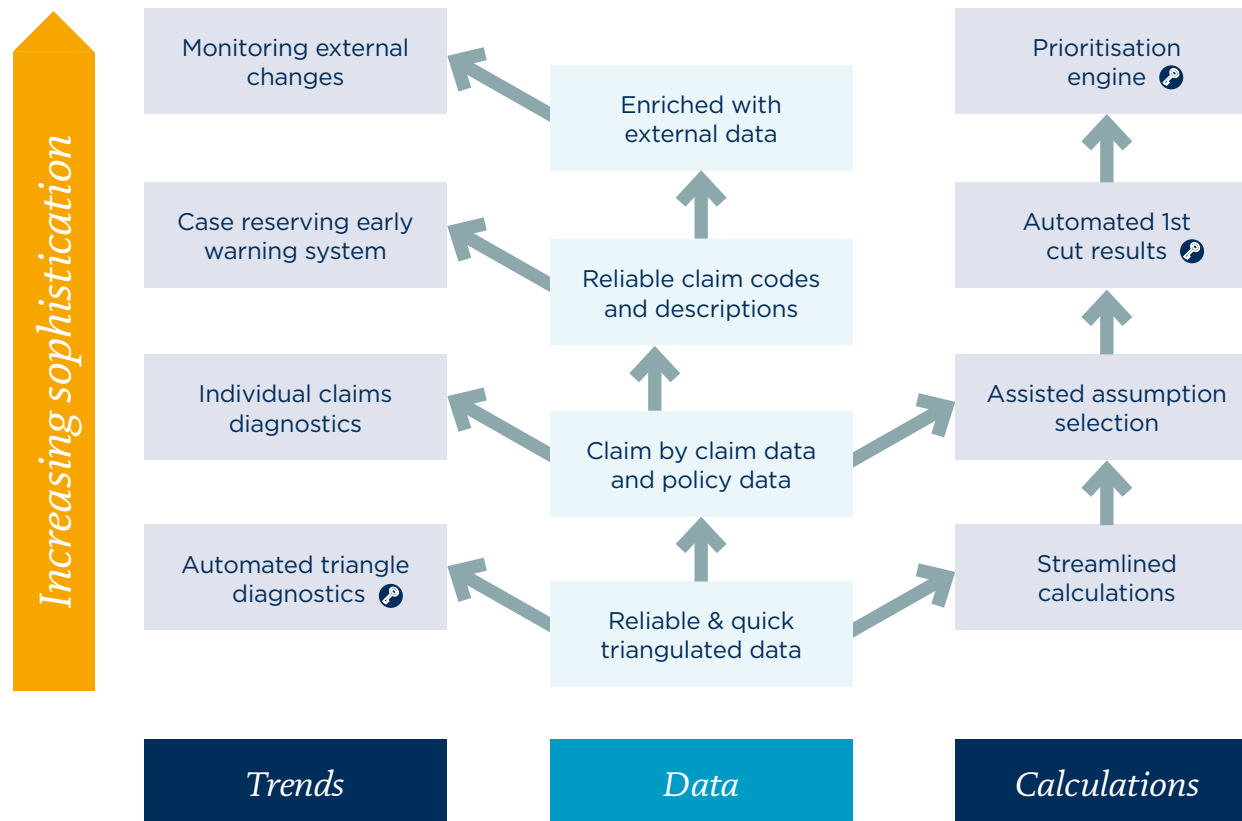
Critically, you can progress at the pace that suits your team and wider business, pause development at any time and, in fact, do not need to reach the top of your levelling-up path to materially enhance the reserving process.

The optimal levelling-up path for your firm will depend on a range of factors including your current process, your short-term priorities and your longer-term goals.

The diagram to the right shows an example levelling-up path based on our work with a number of insurers.

Key areas of focus in many cases are automated triangle diagnostics, automated first cut results and implementing prioritisation engines to direct the reserving team’s focus on the most important parts of the analysis.

Example levelling-up path



Key targets for many firms moving towards their ideal reserving process.

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