

IN SEARCH OF...UNDERWRITING RISK APPETITE

2016 CAGNY Spring Meeting

MAY 23, 2016

Don Mango, Guy Carpenter

Risk Appetite and Tolerance

Appetite



Yum

Jeremy Piven: Mercury Rising

Monday, January 12, 2009 | FoxNews.com
By Roger Friedman



Jeremy Piven

AP

Tolerance



Yuck

Is it REWARD Appetite and Risk Tolerance?

Begin at the Beginning

Merriam-Webster Definition of Tolerance

- 1: capacity to endure pain or hardship
- 2a: sympathy or indulgence for beliefs or practices differing from or conflicting with one's own
- 2b: the act of allowing something: toleration
- 3: the allowable deviation from a standard; especially the range of variation permitted in maintaining a specified dimension in machining a piece
- 4a (1): the capacity of the body to endure or become less responsive to a substance (as a drug) or a physiological insult especially with repeated use or exposure <*developed a tolerance to painkillers*>; also the immunological state marked by unresponsiveness to a specific antigen
(2) : relative capacity of an organism to grow or thrive when subjected to an unfavorable environmental factor
- b: the maximum amount of a pesticide residue that may lawfully remain on or in food

Begin at the Beginning

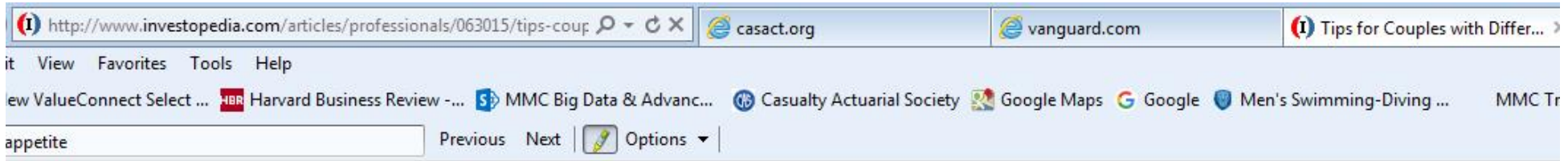
Merriam-Webster Definition of Appetite

- 1: any of the instinctive desires necessary to keep up organic life; especially: the desire to eat
- 2a: an inherent craving *<an insatiable appetite for work>*
- 2b: taste, preference *<the cultural appetites of the time — J. D. Hart>*
- So we also hear Risk Preferences bandied about — sounds like that is just a synonym for Appetite

Definitions from the Investor World

- Investopedia: 'Risk Tolerance'
 - *The degree of variability in investment returns that an individual is willing to withstand. Risk tolerance is an important component in investing. An individual should have a realistic understanding of his or her ability and willingness to stomach large swings in the value of his or her investments. Investors who take on too much risk may panic and sell at the wrong time.*
- IMF: 'Investor Risk Appetite'
 - *The willingness of investors to bear risk, defined as the inverse of the price of risk. So when an investor's risk appetite falls, they require larger expected excess returns to hold risky assets.*

Trip to Krazytown



Tips for Couples with Differing Risk Appetites

By Barbara A. Friedberg | June 30, 2015

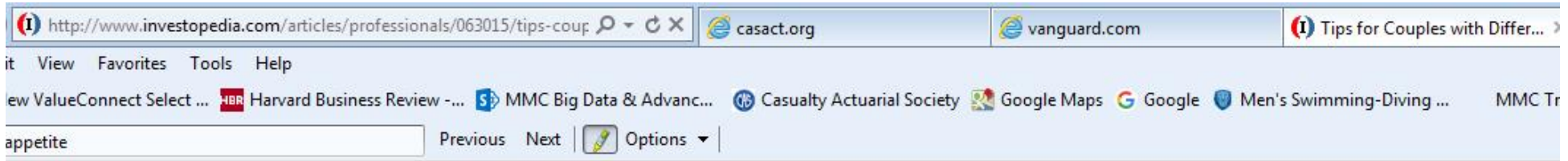


You may have heard the term **risk tolerance** bandied about when the conversation turns to investing. But what does it actually mean?

Risk tolerance is the degree of variability in investment returns that an individual is willing to withstand. As an important component in investing, it's vital to understand you or your client's willingness and ability to stomach drastic

swings in investment portfolio value. Why? Because investors who assume too much risk may wind up panicking and selling at the wrong time. Similarly, investors who are risk averse may wind up missing out on market gains. (For more, see: [What Is Your Risk Tolerance?](#))

Trip to Krazytown



Tips for Couples with Differing Risk Appetites

By Barbara A. Friedberg | June 30, 2015



You may have heard the term **risk tolerance** bandied about when the conversation turns to investing. But what does it actually mean?

Risk tolerance is the degree of variability in investment returns that an individual is willing to withstand. As an important component in investing, it's vital to understand you or your client's willingness and ability to **stomach** drastic

swings in investment portfolio value. Why? Because investors who assume too much risk may wind up panicking and selling at the wrong time. Similarly, investors who are risk averse may wind up missing out on market gains. (For more, see: [What Is Your Risk Tolerance?](#))

Risk Appetite and Tolerance Statements

AM Best SRQ

Please state any overall risk appetite and risk tolerance statement(s) that have been established or approved by a Board or senior management that apply to the rating unit and provide guidance in providing policyholder security and creating stakeholder value. **The risk appetite and risk tolerance statements may be a mix of qualitative and quantitative statements.** Organizations that are subject to Own Risk and Solvency Assessment (ORSA) requirements, or have chosen to align their assessments with these requirements, may provide these as a response. If no such statements have been formally approved by a Board or senior management, please answer "None".

Even RIMS is Confused

“Exploring Risk Appetite and Risk Tolerance”

Definition Challenges

Since the terms “risk appetite” and “risk tolerance” often are used interchangeably and different definitions abound (see “Selected Definitions of Risk Appetite and Tolerance” below), this tends to add confusion when discussing the concepts both internally and externally.

https://www.rims.org/resources/ERM/Documents/RIMS_Exploring_Risk_Appetite_Risk_Tolerance_0412.pdf

Selected Definitions of Risk Appetite and Risk Tolerance

SOURCE	RISK APPETITE DEFINITION	RISK TOLERANCE DEFINITION
ISO Guide 73:2009 <i>Risk management vocabulary</i>	<p>Amount and type of risk that an organization is willing to pursue or retain.</p> <p><i>Note: ISO 31000 does not include this risk appetite definition in the guidance standard.</i></p>	<p>Organization's or stakeholder's readiness to bear the risk after risk treatment in order to achieve its objectives.</p> <p><i>Note: Risk tolerance can be influenced by legal or regulatory requirements.</i></p>
COSO <i>Strengthening Enterprise Risk Management for Strategic Advantage, 2009</i>	A broad-based description of the desired level of risk that an entity will take in pursuit of its mission.	Reflects the acceptable variation in outcomes related to specific performance measures linked to objectives the entity seeks to achieve.
BS 31100:2008	The amount and type of risk than an organization is prepared to seek, accept or tolerate.	<p>The organization's readiness to bear the risk after risk treatments in order to achieve its objectives.</p> <p><i>Note: Risk tolerance can be limited by legal or regulatory requirements.</i></p>
KPMG <i>Understanding and articulating risk appetite, 2009</i>	The amount of risk, on a broad level, that an organization is willing to take on in pursuit of value.	Risk thresholds, or risk tolerances, are the typical measures of risk used to monitor exposure compared with the stated risk appetite.
Towers Perrin, <i>What's Your Risk Appetite, Emphasis 2009</i> by J. David Dean and Andrew F. Giffin	<p>The amount of total risk exposure that an organization is willing to accept or retain on the basis of risk-reward trade-offs:</p> <ul style="list-style-type: none"> • Reflective of strategy, risk strategies and stakeholder expectations • Set and endorsed by board of directors through discussions with management 	<p>The amount of risk an organization is willing to accept in the aggregate (or occasionally within a certain business unit or for a specific risk category):</p> <ul style="list-style-type: none"> • Expressed in quantitative terms that can be monitored • Often expressed in acceptable/unacceptable outcomes or levels of risk
ECIIA and FERMA, <i>Guidance on the 8th EU Company Law Directive, article 42, 2011</i>	The level of risk that the company is willing to take: high return-high risk; low risk-low return, or a portfolio of different exposures. Risk appetite is strategic and relates primarily to the business model.	The maximum amount of risk that the company can bear despite controls. Risk tolerance is more operational and relates primarily to the company's targets.

RIMS is Confused

“Exploring Risk Appetite and Risk Tolerance”

For the purpose of this paper, we will use the following definitions:

Risk appetite *is the total exposed amount that an organization wishes to undertake on the basis of risk-return trade-offs for one or more desired and expected outcomes.*

As such, risk appetite is inextricably linked with—and may vary according to—expected returns.

Risk appetite statements may be expressed qualitatively and/or quantitatively and managed with respect to either an allocated individual initiative and/or in the aggregate. T

Think of risk appetite as the amount that an organization actively ventures in pursuit of rewards—also known as its goals and objectives.

RIMS is Confused

“Exploring Risk Appetite and Risk Tolerance”

Risk tolerance is the amount of uncertainty an organization is prepared to accept in total or more narrowly within a certain business unit, a particular risk category or for a specific initiative.

Expressed in quantitative terms that can be monitored, risk tolerance often is communicated in terms of acceptable or unacceptable outcomes or as limited levels of risk.

Risk tolerance statements identify the specific minimum and maximum levels beyond which the organization is unwilling to lose. The range of deviation within the expressed boundaries would be bearable.

However, exceeding the organization’s established risk tolerance level not only may imperil its overall strategy and objectives, in the aggregate doing so may threaten its very survival.

This can be due to the consequences in terms of cost, disruption to objectives or in reputation impact.

Our story so far

- In all other aspects of life, there are clear and distinct differences between the terms “Appetite” and “Tolerance” ...
- ...except (apparently) when it comes to Risk
- The terms are used interchangeably in public documents, regulations, rating agency standards, company policy statements, ...
- This is known as **conflation**

Problem Statement

- Appetite = what you seek to stay alive or crave or desire = reason for being
- Tolerance = what you are willing to put up with, necessary evils
- Insurers assume risk as their reason for being, other types of firms don't
- Because of the conflation of the terms, those other types of firms are sometimes making appetite statements that should probably be tolerance statements
- Maybe only insurers, who assume risk as their reason for being, should issue **risk appetite** statements
- For insurers, that would really mean **Underwriting Risk Appetites**
- It's the only type of risk we actively, deliberately seek

If You Want to Use Quantitative Risk Tolerance and Appetite Statements *Four Out of Five Dentists*

- Actually useful framework from The Institute of Risk Management (UK) (<https://www.theirm.org/>)
 - Like RIMS over here
- www.theirm.org/media/464806/IRMRiskAppetiteExecSummaryweb.pdf

Risk Tolerances and Appetites

IRM Framework

- Risk Universe = maximum amount of volatility if we did nothing

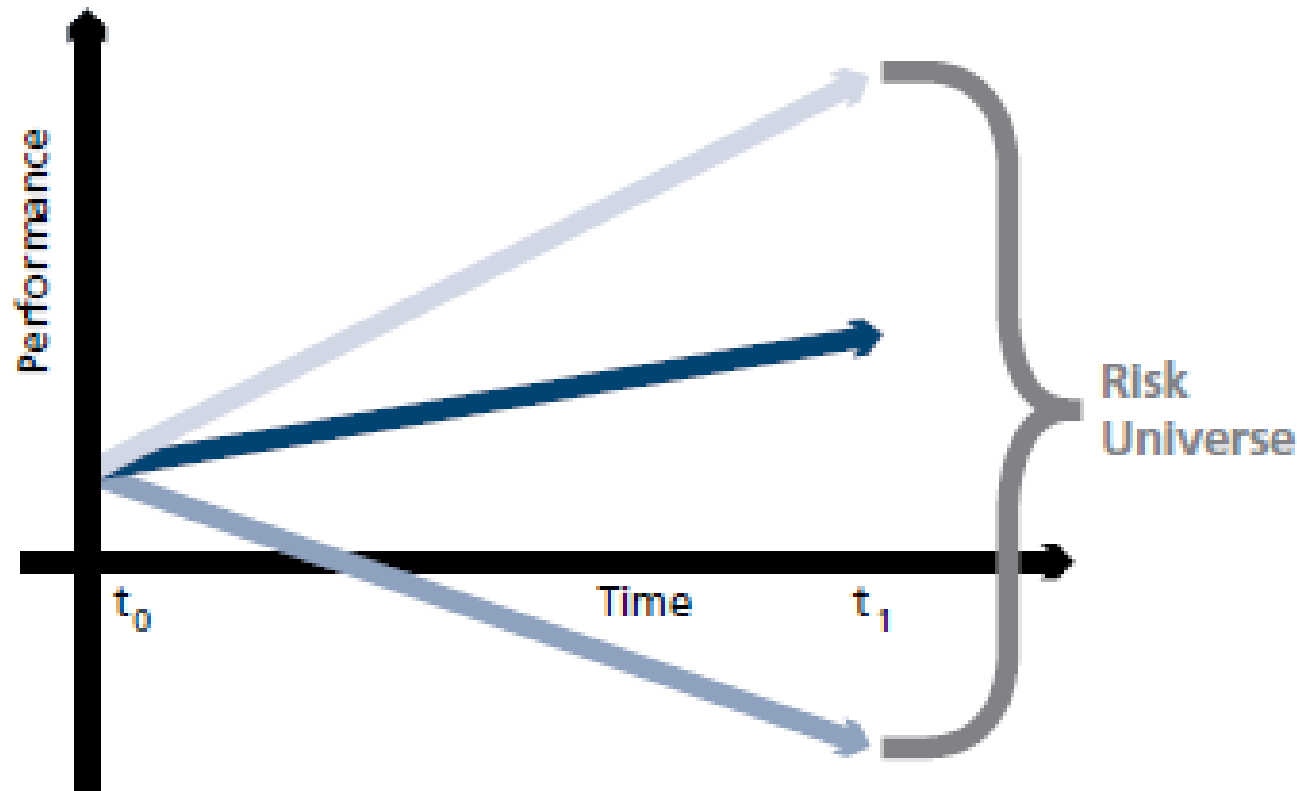


Diagram 3

Risk Tolerances and Appetites

IRM Framework

- Risk Tolerance = maximum amount of volatility we are willing to tolerate in order to pursue this business

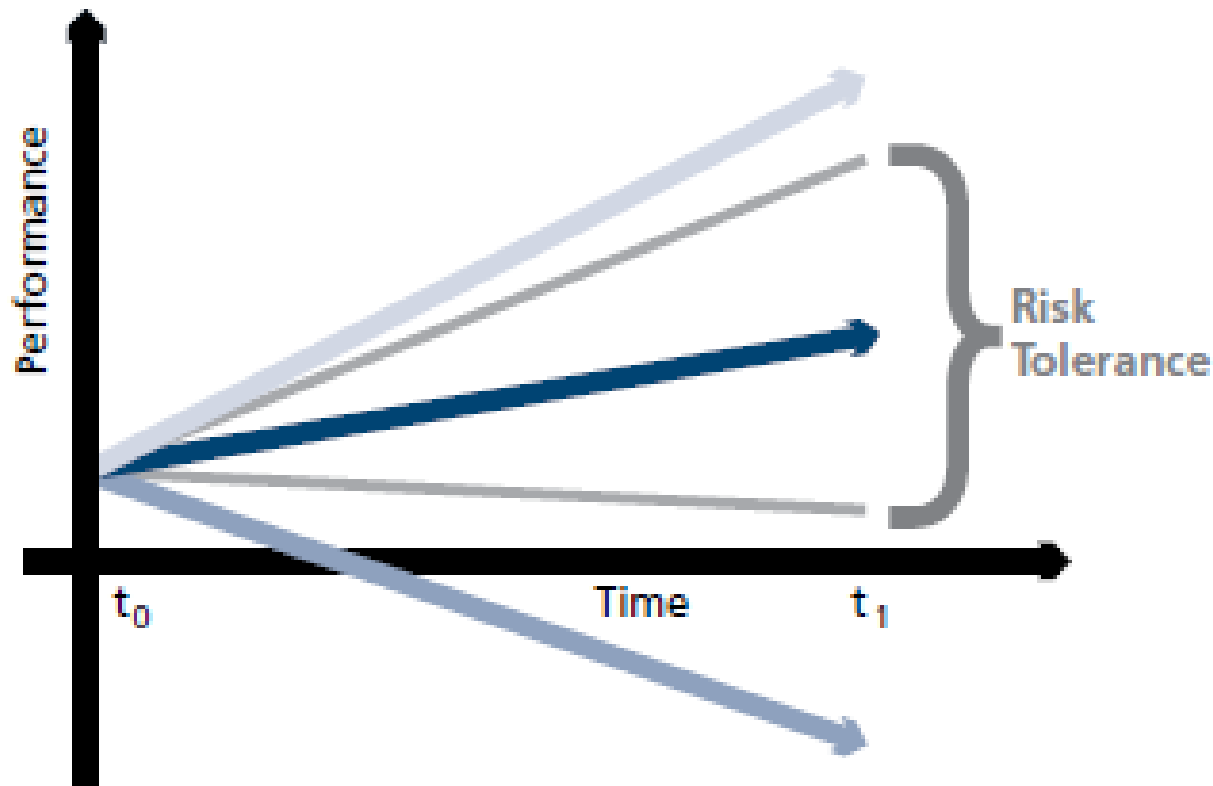


Diagram 4

Risk Tolerances and Appetites

IRM Framework

- Risk Appetite = reasonable expectation of volatility, given competition and market practices

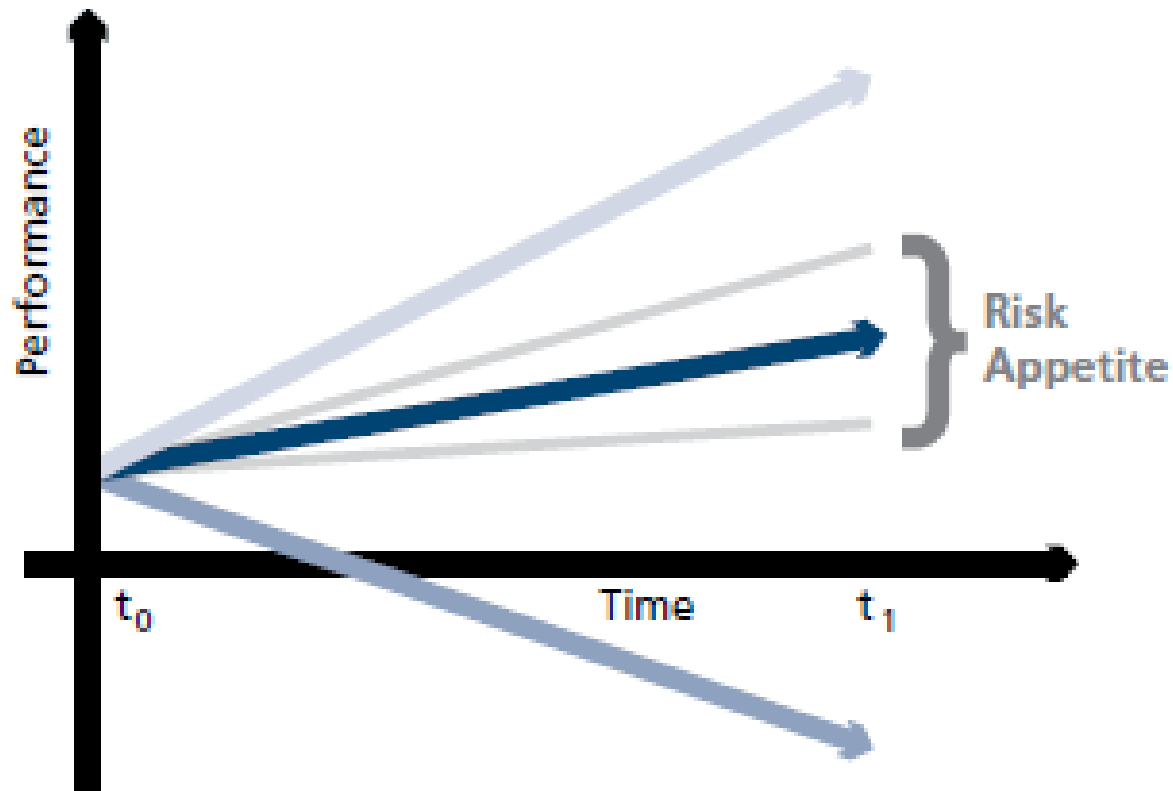


Diagram 5

Feeling Brave
Now?

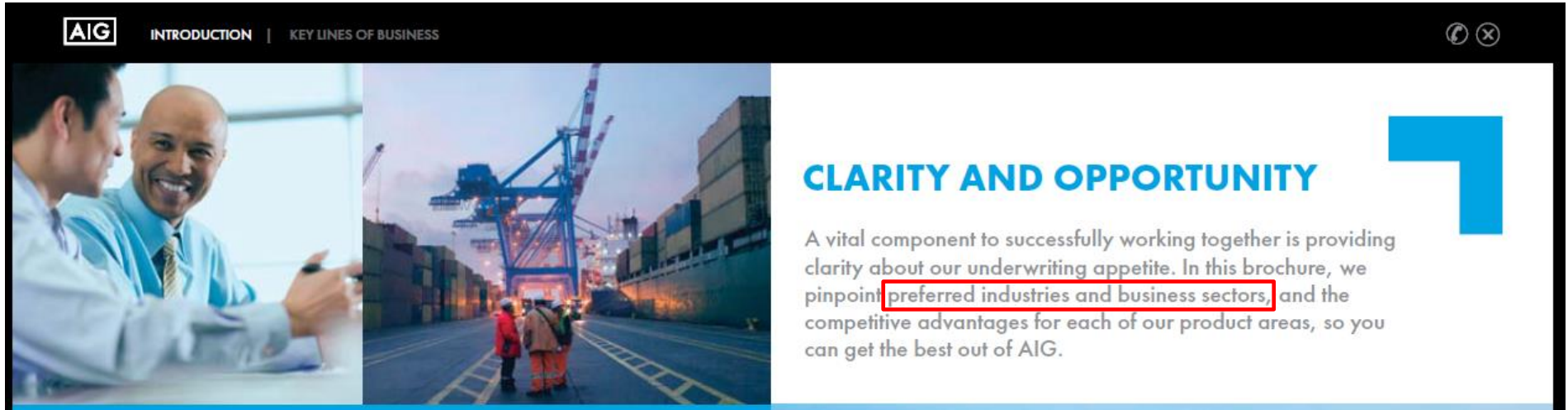
Good!

Then let us
go...



...UNDERWRITING RISK APPETITE!

AIG US Underwriting Appetite



The image is a screenshot of a digital brochure from AIG. At the top left is the AIG logo. To its right are the navigation links 'INTRODUCTION' and 'KEY LINES OF BUSINESS'. In the top right corner are icons for a refresh button and a close button. The main content area is split into two columns. The left column contains two images: the top one shows two men in business attire smiling and talking, and the bottom one shows a large industrial port at night with cranes and shipping containers. The right column has a large blue L-shaped graphic on the right side. The text in this column reads: 'CLARITY AND OPPORTUNITY' in large blue letters, followed by a paragraph: 'A vital component to successfully working together is providing clarity about our underwriting appetite. In this brochure, we pinpoint preferred industries and business sectors, and the competitive advantages for each of our product areas, so you can get the best out of AIG.' The phrase 'preferred industries and business sectors' is highlighted with a red rectangular box.

Not exactly Underwriting **Risk** Appetite...

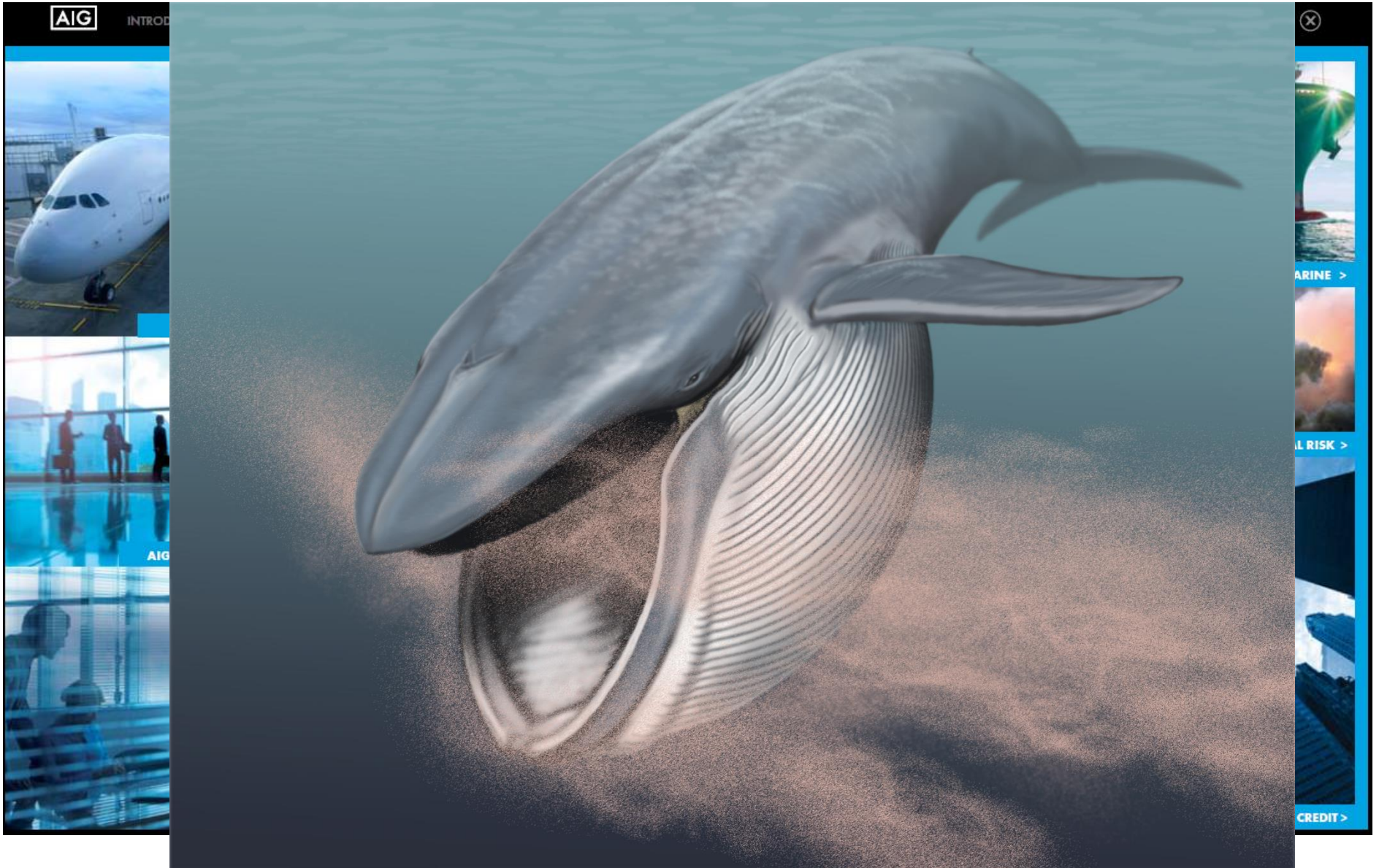
...and it mentions **Preferences**

http://www.aig.com/Chartis/internet/US/en/AIG-US-UnderwritingAppetite-v7_tcm3171-593717.pdf

AIG Underwriting Appetite = ...?



AIG Underwriting Appetite = ...!!



Axis Underwriting (Australia)



MELBOURNE 03 8660 7000 SYDNEY 02 9216 7200 BRISBANE 07 3117 3707

[Home](#) [Risk Appetite](#) [Services](#) [Our Organisation](#) [News](#) [Contact](#)

Risk Appetite

[Home / Risk Appetite](#)

Commercial Strata

Residential Strata

Hospitality

Legal Expenses

Liability

Property

Risk Appetite Matrix



<http://axisunderwriting.com.au/risk-appetite/all-offerings/>

Axis Underwriting (Australia)



MELBOURNE 03 8660 7000 SYDNEY 02 9216 7200 BRISBANE 07 3117 3707

[Home](#) [Risk Appetite](#) [Services](#) [Our Organisation](#) [News](#) [Contact](#)

Risk Appetite

[Home](#) / [Risk Appetite](#)

Risk Appetite

When it comes to hard to place and high hazard risks, Axis is a leader in the Australian underwriting market. Whether it's property, commercial strata, hospitality, bed & breakfast or liability, Axis is here to help.

Backed by [Lloyd's](#), our alternative market approach assesses risks on an individual basis to ensure your client receives the protection they need.

Property

Risk Appetite Matrix



Axis Underwriting (Australia) Risk Appetite Matrix

Risk Appetite Matrix

The Axis Risk Matrix lists some of the more common occupations that we underwrite. If you can't find what you're looking for, [contact](#) our team of underwriters for a tailored solution to your general insurance need.

*** To discover our risk appetite, click the shortcut alphabet below or scroll down.**

A B C D E F G H I J K L M N P R S T U V W

A	PROPERTY	LIABILITY
Abattoir	✓	✓
Abrasives	✓	✓
Adult products/ sex shops	✓	✓
Agricultural equipment	✓	✓
Air Compressors	✓	✓
Alarm equipment – fire & burglary alarms	✓	✓
Aluminium goods NOC	✓	✓
Aluminium windows	✓	✓
Amusement equipment	✓	✓
Artificial flowers	✓	✓
Artificial jewellery	✓	✓
Asian restaurants	✓	✓

Axis Underwriting (Australia) Risk Appetite Matrix

Risk Appetite Matrix

The Axis Risk Matrix lists some of the more common occupations that we underwrite. If you can't find what you're looking for, [contact](#) our team of underwriters for a tailored solution to your general insurance need.

*** To discover our risk appetite, click the shortcut alphabet below or scroll down.**

A B C D E F G H I J K L M N P R S T U V W

A	PROPERTY	LIABILITY
Abattoir	✓	✓
Abrasives	✓	✓
Adult products/ sex shops	✓	✓
Agricultural equipment	✓	✓
Air Compressors	✓	✓
Alarm equipment – fire & burglary alarms	✓	✓
Aluminium goods NOC	✓	✓
Aluminium windows	✓	✓
Amusement equipment	✓	✓
Artificial flowers	✓	✓
Artificial jewellery	✓	✓
Asian restaurants	✓	✓

Axis Underwriting (Australia) Risk Appetite Matrix

Risk Appetite Matrix

The Axis Risk Matrix lists some of the more common occupations that we underwrite. If you can't find what you're looking for, [contact](#) our team of underwriters for a tailored solution to your general insurance need.

*** To discover our risk appetite, click the shortcut alphabet below or scroll down.**

A B C D E F G H I J K L M N P R S T U V W

A	PROPERTY	LIABILITY
Abattoir	✓	✓
Abrasives	✓	✓
Adult products/ sex shops	✓	✓
Agricultural equipment	✓	✓
Air Compressors	✓	✓
Alarm equipment – fire & burglary alarms	✓	✓
Aluminium goods NOC	✓	✓
Aluminium windows	✓	✓
Amusement equipment	✓	✓
Artificial flowers	✓	✓
Artificial jewellery	✓	✓
Asian restaurants	✓	✓

Mitsui Sumitomo A&H Lloyds Syndicate 3210 Underwriting Appetite

Target Industry Group

- Specialist scheme accounts in the UK and Internationally adopting Lloyd's Coverholder methodology
- UK and International Corporate clients
- UK Commercial clients
- Lloyd's Direct and Facultative business
- Affinity Groups and Associations

Limited Risk Appetite and Industry Groups

- Professional Sports and Entertainers
- Security firms
- Airlines
- Ships Crews
- Stand Alone Medical Expenses / Private Medical Insurance
- Loss of Licence
- Sickness / Illness

Excluded Appetite

- Retail Holiday Travel Schemes
- LMX
- US Cat treaty
- Professional Sports Teams

Risk Location

- UK
- Europe
- Australia
- Worldwide sub Lloyd's licensing
- Limited US risk exposures

Limits

- Any one life up to £2.5 million
- Any one event up to £25 million / \$50 million / €37.5 million
- Any one aircraft up to £10 million

What can we conclude?

- A tangled web of price adequacy, capital provider willingness to absorb volatility, underwriting expertise, ...
- The few who are articulating it seem to be aiming for sectors and classes of interest
- Seems like the area is ripe for modernization....

Increase In-Appetite Submissions

IVANS Market Appetite

What is IVANS Market Appetite?



- > A search tool for agents integrated into their agency management system and daily workflow.
- > Enabling you to communicate your appetite when agents begin searching for a market to submit their new and renewal business.
- > Agents will win more new business and better support their existing clients with the best options available.
- > You will receive more in-appetite submissions resulting in greater profitable premium growth.

Market Selection Today

Agents pursue a market based on immediate awareness of carrier appetites and other influencing factors, including:

- > Carriers' historic behavior with similar risks
- > Underwriter responsiveness in past transactions
- > Relationships with carriers/appointed access
- > Communications from carriers
- > Colleagues' perception of carrier appetite

Commercial Insurance is an Inefficient Network

COMMUNICATION

Agents and brokers are inundated with appetite marketing materials from carriers

WORKFLOW INTEGRATION

Carriers aren't integrated into agents' management systems and workflow

PERCEIVED KNOWLEDGE

Results show most agents don't know the right markets and specific underwriters for a risk a significant percentage of the time.

SUBMISSION MISALIGNMENT



Costing the Industry Billions Each Year

INDUSTRY FINANCIAL IMPACTS

- > Brokers send roughly 25 million submissions to carriers each year, 15 million are declined.
- > Average cost per submission \$133
- > Annual industry cost of approximately \$2 billion each year in avoidable expense

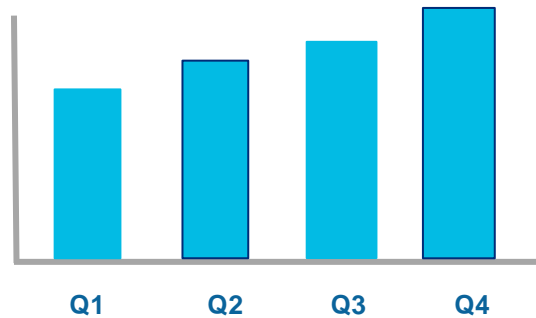
SUBMISSION MISALIGNMENT



What Carriers Want to Achieve

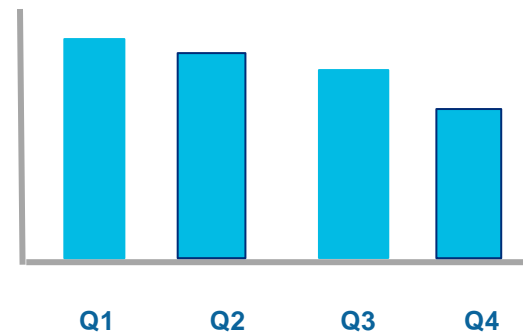
BUSINESS GROWTH

Premium Written



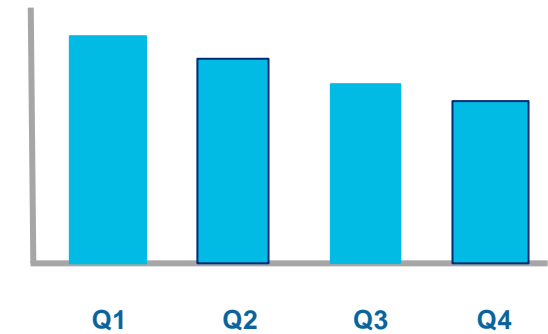
PROFITABLE RISKS

Loss Ratio



EXPENSE REDUCTION

Expense Ratio



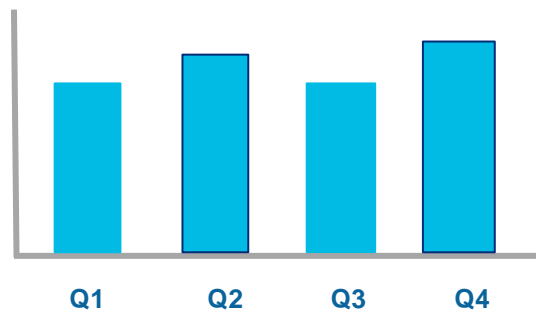
ANTICIPATING CHANGES IN THE MARKET

- > Trends are identified early and quickly
- > Simplified information allows the carrier to proactively make changes
- > Submission mix can be changed quickly
- > Agents easily understand carrier changes in desired appetite
- > Underwriters quote new and more profitable business
- > Carriers realize new opportunities and avoid potential losses

Today's Reality

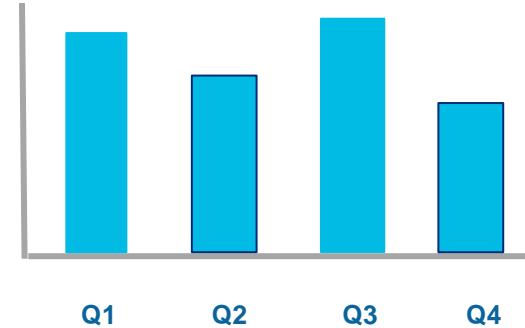
BUSINESS GROWTH

Premium Written



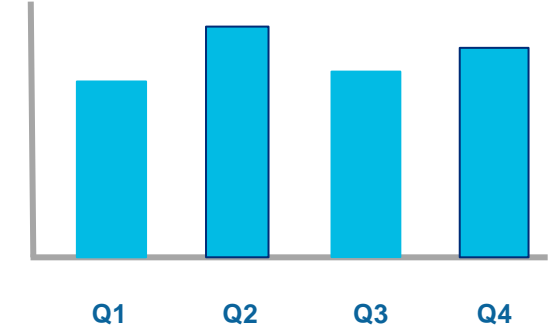
PROFITABLE RISKS

Loss Ratio



EXPENSE REDUCTION

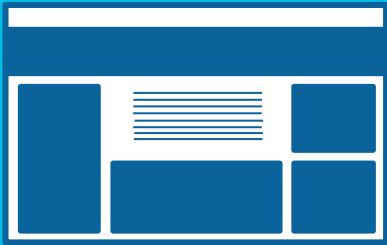
Expense Ratio



REACTING TO CHANGES IN THE MARKET

- > Reactionary to market trends and changes
- > Complex, unorganized data is difficult to understand
- > Can take a year or more to change and communicate submission mix
- > Agents become confused and disillusioned, leading to submission misalignment
- > Underwriters continue to quote less profitable business
- > Carriers miss opportunities of revenue growth potential

How Do You Communicate Your Appetite?



Web Pages



Broker Guides



Conversations



Webinars

All of these efforts have not significantly changed the outcome of submission alignment for carriers over the past 20 years.

An Award Winning Industry Solution

IVANS Market Appetite has been recognized by the Business Intelligence Group as a winner in the 2016 BIG Innovation Awards. The annual business awards program recognizes those who have brought new ideas to life and seek to change the way organizations and individuals interact with the world.

IVANS Market Appetite will be available to more than 350 carrier partners with access to all 35 IVANS agency management systems partners in the United States representing more than 280,000 users



How IVANS Market Appetite Works

SEARCH

Market Appetite Search

SIC

NAICS

Issuing location

Search

Add Account

An agent with new or renewal business conducts a search based on industry code and location.

MARKET PARTICIPATION

Windsor National CARRIER ★ APPOINTED
Auto BOP Crime GL Property Inland Marine Umbrella Workers Comp
Show Details

Midwest Coastal CARRIER ★ APPOINTED
Auto BOP Crime GL Property Inland Marine Umbrella Workers Comp
Show Details

Specialty Brokers WHOLESALER ★ APPOINTED
Auto BOP Crime GL Property Inland Marine Umbrella Workers Comp
Show Details

Carrier appetite for risks are displayed based on:

- > Stated participation (paid)
- > Inferred participation (assumptions based on past behavior)

SUBMISSION ALIGNMENT

Midwest Coastal CARRIER ★ APPOINTED
Auto BOP Crime GL Property Inland Marine Umbrella Workers Comp
Show Details

Agents have confidence that markets they are directed to will quote their submissions.

Carriers drive the kinds of submissions they are asking for and grow within target markets.

A Unique Value Unlike Ever Before

- > Presented inside of the agency management system at the **exact moment** an agent starts searching for markets
- > **Stated and controlled** by you, driving new in-appetite submissions into your pipeline
- > Promoting your brand, industries, and lines of business to **increase awareness and differentiate** your company from others
- > Customized search views to be **visible only for your appointed agencies**
- > Leveraging the **strength, depth and data resources of IVANS** to identify new agencies that have the business you want to write

Be Part of the Solution

- Advocate for and insist on clarity
 - Appetite = what you seek to stay alive or crave or desire = reason for being
 - Tolerance = what you are willing to put up with, necessary evils
- Fight the conflation
- Focus on clarifying your company's **Underwriting Risk Appetite**
- Look into modernization like IVANS Market Appetite

Thank You



GUY CARPENTER