

## Early Warning Signals in Insurance Companies

A two-day course for experienced analysts offering an insight into the causes and early warning signals of credit deterioration and failure in both local and international property and casualty (non-life), life and reinsurance companies. We assume experience of core analytic skills regarding insurance companies.

### TARGET AUDIENCE

The workshop is targeted at an advanced level for experienced credit risk managers, fixed income investors and regulators who are already familiar with the key analytic tools for analysing insurance companies. The workshop aims to cover a wide variety of troubled insurance companies in short case studies.

For analysts seeking a more in-depth overview of how to analyse insurance companies, we recommend our intermediate level workshops: Insurance Company Analysis and Intensive Insurance Analysis. We also have introductory level workshops: Introduction to Insurance Financial Statements.

### COURSE OBJECTIVES

The aim is to equip participants with the knowledge and skills to proactively:

- Apply a structured analytic approach, incorporating qualitative, quantitative and market indicators, to identify vulnerable exposures
- Highlight the key vulnerabilities of the different types of company, and different business lines within the life, P&C (non-life), and reinsurance sectors
- Review real case studies of failed and deteriorating insurers to identify key recurring themes
- Stress test insurance company solvency and earnings for investment or underwriting losses, over-valuation of assets and under-reserving
- Recognise the key challenges of credit exposures to vulnerable insurance companies and the triggers that might lead to downgrades or refinancing problems.

### CONTENT

#### ANALYTIC OVERVIEW

*Section Aims:* This section identifies key themes and credit issues for exposures to insurance companies.

##### Signs of Distress

- Common themes in troubled insurance companies: external vs. internal factors; contagion risk
- Symptoms of a company's deteriorating credit standing: financial, non-financial and market indicators.

##### Structured Analytic Approach

- Focus on key issues: payback, risks and structure
- Sources of payback: ability to refinance in normal vs. stressed conditions; the level, volatility and location of cash-flow, challenges to downsizing assets, likelihood of government or parental support
- Risks to repayment: Key macro, sector and company-specific business and financial risks which might jeopardise repayment
- Structure: structural subordination – policyholder priority, the diverging recovery prospects of stakeholders in distressed insurers and holding companies; overview of legal processes for failed insurers
- Case study:* Payback sources for a distressed insurance group.

#### OPERATING ENVIRONMENT

- Section Aims:* This section focuses on key macro-economic and sector trends, which are likely to erode creditworthiness.
- Investment and economic cycles – impact of recession, inflation and financial crisis on main sectors
- Underwriting cycles; trends in catastrophe losses, litigation, mortality / longevity

- Differing vulnerabilities to adverse scenarios by sector: life, P&C and reinsurance
- Changes in regulation, tax or accounting; implications of EU Solvency II and IFRS
- Exercise:* Vulnerable Lines of Business in certain adverse scenarios.

#### MANAGEMENT AND SHAREHOLDERS

*Section Aims:* This section focuses on management and strategy and risk management challenges in troubled markets.

- Risky or inappropriate strategies, signs of desperation
- Significance of ownership structure: mutuals, conglomerates etc.
- The importance of franchise
- How to recognise weak management and lack of integrity
- Disclosure and corporate governance concerns
- Case study:* Inappropriate strategy and management behaviour causing a major insurer to fail.

#### BUSINESS RISK

*Section Aims:* This section focuses on challenged business models and insurance companies with significant exposure to losses from their operations.

- The significance of size and age of firm. Good vs. bad growth
- Business models – exposure to higher risk sectors: variable annuities, D&O, financial and mortgage guaranty
- Performance risk: negative spread, volume and margin pressure
- Investment risk: stress testing write-downs, key asset / liability management (ALM) challenges; asset valuation challenges; effectiveness of hedges, concentration risks; aggregation of exposures across asset and liability classes
- Underwriting risk: pricing and data challenges; catastrophe and concentration risk
- Reinsurance risk: credit and dispute risk; over-reliance on reinsurance; gaps in cover
- Reserve adequacy: legacy exposures and loss reserve triangles in non-life; reserving for embedded guarantees or longevity risk in life
- Regulatory risk: relative vulnerability of sectors
- Case studies:* Insurers with investment and underwriting risk challenges.

#### FINANCIAL RISK

*Section Aims:* This section will focus on the adequacy and quality of capital, liquidity and financial flexibility.

- Capital adequacy: reliability of regulatory solvency formulae; ability of capital to withstand underwriting, investment or other shocks
- Quality of capital – tangible vs. intangible net worth; capital with restricted use; mix of debt, equity and hybrid capital
- Leverage: limits to an insurance company's ability to leverage
- Double leverage: challenges of a leveraged holding company
- Importance of financial flexibility.
- Liquidity: potential cash-flow shocks; liquidity of investments
- Case study:* Insurers with weak solvency and/or poor quality of capital.