

# Solvency II: From Measurement to Management

## *Why liabilities have taken a backseat in the financial modelling business*

**MBE recently attended the latest instalment in a series of workshops hosted by the Institute and Faculty of Actuaries on Solvency II for Life Actuaries. What made this event particularly significant was the fact that it was the first workshop after the Solvency II 'go-live' date.**

A number of industry experts presented on the underlying topic of Solvency II: From Measurement to Management.

What became clear from all of the discussions at the event was that assets have now come to the fore in the minds of most insurers. Most of the discussions on Solvency II before its implementation were on the technicalities of modelling liabilities, but this focus has shifted and two main topics emerged from the workshop:

- Optimising balance sheets
- Asset modelling requirements and implementation

### *Optimising balance sheets*

After the initial rush to meet the requirements of Solvency II, a number of insurers have now moved on to optimising their balance sheets and asset allocations. To this end, Special Purpose Vehicles (SPVs) are gaining popularity in matching complex cash flows and capital requirements. There has also been an increasing trend of insurers moving into the loans business to achieve equivalent results.

These types of assets come with their own complexities and risks, and care should be taken when utilising these investment vehicles. When investing in illiquid assets, for example, the corporate governance structures that would be needed and the skills required to manage and price these assets can be tricky and should be considered.

Companies wishing to set up their own SPVs should be aware of the challenges of doing this, including the time and cost involved. Common pitfalls encountered in this process include:

- Finding a balance between the rating level to set for the asset and the economic value of the instrument
- Finding a balance between the number of notes to create and the complexity of managing the notes
- The method to use in setting the rating and how to validate it

Banks and consultancies can provide valuable assistance in setting up and managing SPVs on behalf of insurance companies.

### *Asset modelling requirements and implementation*

One specific aspect of Solvency II that the industry is still coming to grips with is the increased reporting and modelling requirements on assets held by insurance companies. Actuaries have traditionally focused on liability modelling, with a significant part of the effort of Solvency II preparation going into setting up the structures and processes to model and report on them. This focus has now shifted to the complexities involved in the asset modelling and reporting.

It can be a challenge for insurers and consultants to choose the right software to use for their modelling, the complex calculations required and obtaining the necessary data.

Pre-Solvency II, the focus was only on the market value and yields of assets held by insurance companies. This focus has now shifted and the modelling requirements have become increasingly complex, with basic programs such as Excel being unable to handle these increased requirements. It therefore has become necessary to look to other software packages in order to create models.

The main difficulty cited in asset modelling is obtaining data of sufficient quantity and quality. The increased modelling and reporting requirements have brought with them increased data requirements, and companies have experienced significant difficulties in obtaining the required data. One of the speakers described the situation as being similar to the situation seen in the industry 15 years ago with liability modelling; it is, however improving.

It was clear from the workshop that there is a large amount of development happening in the asset space. Companies are exploring new opportunities and are trying to streamline their operations. This is a new area for a number of companies and having an experienced partner to work with has clear advantages in a space with significant risks.

MBE has also experienced the challenges in these areas and as a result we have developed solutions and tools to assist insurers and asset managers to obtain quality look through data and to assist in their asset modelling requirements. By partnering with industry leaders in asset data aggregation and rating agencies, MBE can provide a unique solution to enable their clients to manage their assets effectively and meet regulatory reporting requirements.



**Solvency II implementation has brought about increased co-operation between insurers, asset managers and consultants as they strive to manage data requirements and meet deadlines**