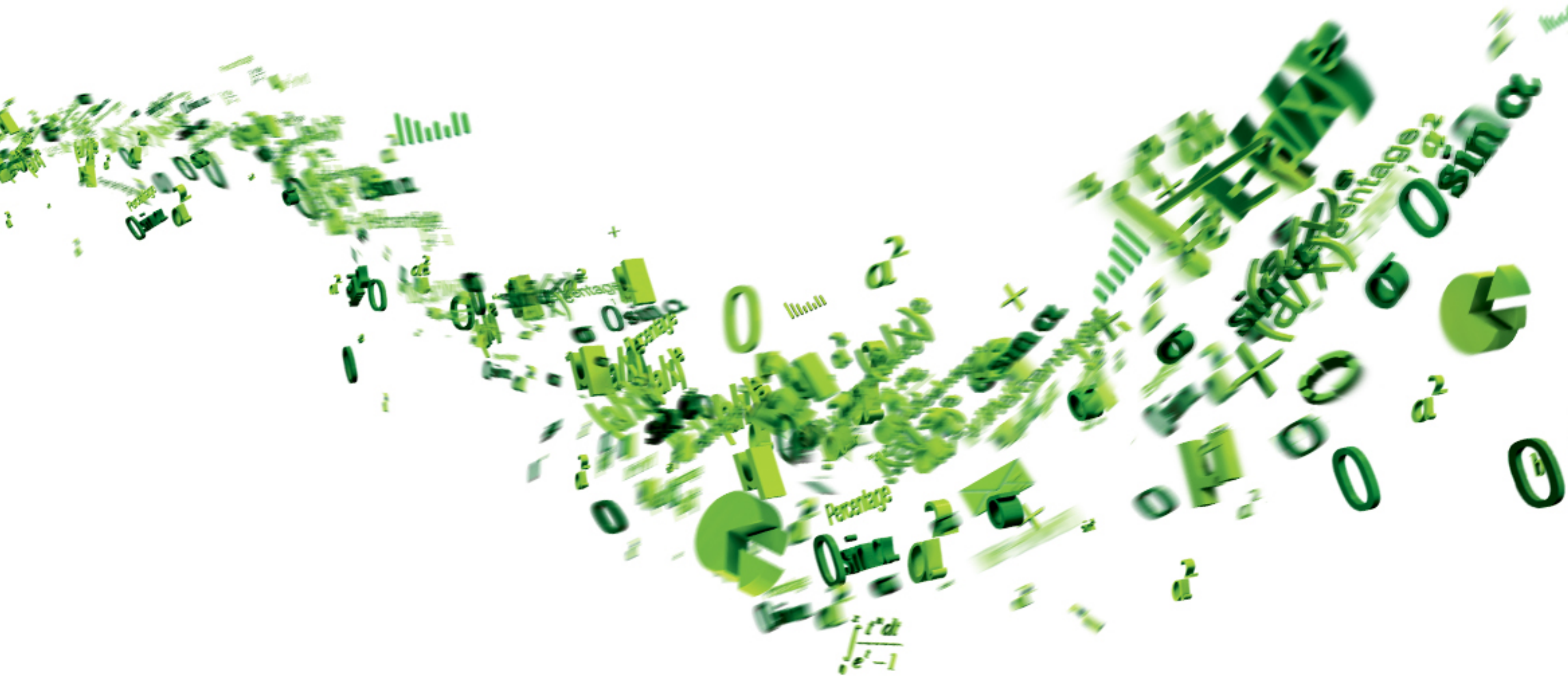


Lloyd’s Update

Redefining the Future

September 2019

Empower Results®

Contents

Foreword

Welcome to the latest edition of our Lloyd's Update report series. Three years have elapsed since our last report and a lot has happened in the intervening period. In particular, Lloyd's has had to make some difficult adjustments to address the deterioration in underlying performance exposed by the major losses in 2017 and 2018.

This remains a work in progress, but in the interim we applaud the vision for the 'Future at Lloyd's' that has been laid-out by John Neal and his executive team. The strategy is rightly built around delivering greater value to customers and the inclusive approach is building momentum for change. The ultimate outcome should be a larger and much more efficient marketplace, with an enhanced standing in the industry.

Aon is actively engaged in this process, from Greg Case's membership of the global advisory committee, to direct support of several of the Future at Lloyd's initiatives. In this changing environment, our Global Risk Specialty, Capital Advisory and Inpoint teams are working closely together to provide value-adding services to Lloyd's syndicates. These span business formation, delivery of business plans, placement of efficient reinsurance and sourcing and optimization of capital. Contact details can be found at the back of the report.

Aon would like to thank Lloyd's for its assistance with the production of this report.

Nick Frankland
UK CEO, Reinsurance Solutions, Aon

"Aon is committed to anticipating the needs of our clients and working with leading organizations around the world to innovate on their behalf. With this new strategy, Lloyd's is accelerating its own evolution and charting a path forward for London to continue playing a significant role in the global insurance market. We're pleased to contribute to this important discussion."

Greg Case

Executive Summary

The publication of this report comes at a pivotal moment in Lloyd's evolution. The 'Future at Lloyd's' initiative launched by John Neal may result in the biggest changes in the market since the Reconstruction and Renewal process of the mid-1990s.

Lloyd's has outlined a series of measures designed to enhance the market's relevance on the global stage. This is driven by customer feedback calling for better solutions for today's risks, a simpler process for accessing products and services at Lloyd's and lower costs of doing business at Lloyd's.

The proposals are ambitious and designed to result in a much more efficient and responsive market. Ultimately, the goal is to create better connectivity between capital and risk that delivers greater value to customers and supports long-term growth.

Potential outcomes include separate placement methods for complex and standardized risk, easier entry to the market for high-performing innovative businesses, more flexibility in the way that capital participates, a next-generation claims service and the creation of an 'ecosystem' of data and services.

The approach has been collaborative and the feedback has been positive. The market now awaits the blueprint for the 'new Lloyd's', which will be published at the end of September.

Much of the impetus for change stems from weak underlying operating performance. In particular, Lloyd's is intent on making inroads into the market's expense ratio, which has averaged around 40% over the last five years, a significant disadvantage relative to its comparator group.

The 'Decile 10' initiative gained a great deal of attention during 2018, as Lloyd's sought to tackle the impact of under-performing business. Management expects the remediation plans now in place to bring the market back to profit in 2019, allowing for major losses equivalent to 9% of net premium earned.

Greater differentiation is being seen in Lloyd's treatment of syndicates. Top-quartile performers now benefit from a 'light touch' regime, while loss-making businesses remain under pressure and subject to constraints. This has translated into in-market consolidation, which we expect to continue.

Lloyd's had no issues recapitalizing after recent major losses and the Central Fund was not impacted by these events. Higher capital requirements and restrictions on the use of letters of credit are reducing capital efficiency, but the market's partially mutualized structure continues to convey advantages.

The likelihood of a 'no-deal' Brexit at October 31, 2019 has increased. Lloyd's Brussels has been formed to ensure that customers across Europe can continue to access the market's underwriting expertise and financial security, whatever the eventual outcome of the political process.

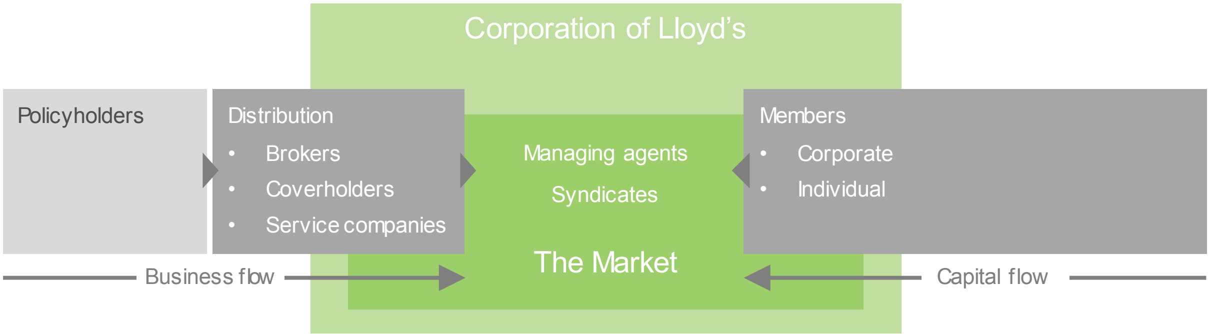
All these issues (and more) are covered in this report. We hope you enjoy the read and invite follow-up via the contacts listed at the back.

Regulation and Governance

Regulatory framework

Lloyd’s is not an insurance company. It is a unique partially-mutualized marketplace, built around a society of members which organizes itself into syndicates with a view to insuring risks. Specialist managing agents exclusively operate these syndicates on behalf of the members.

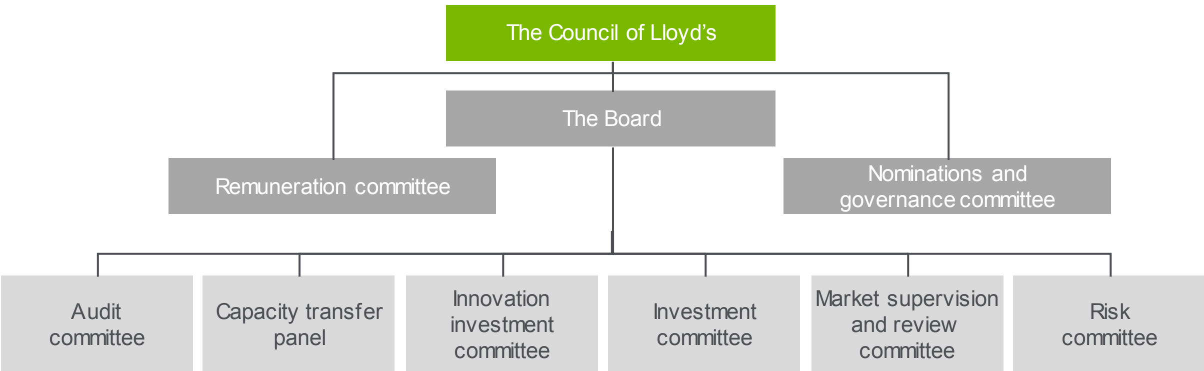
Exhibit 1: Market overview



Source: Aon / Lloyd’s.

An Act of Parliament, the Lloyd's Act 1982, defines the governance structure and rules under which the Society of Lloyd's operates. Under the Act, the Council of Lloyd's is responsible for managing and supervising the market. It delegates many of its functions to the Franchise Board whose members are appointed by the Council. The day to day powers and functions of the Council and the Board are carried out by the Corporation of Lloyd’s, which had 1,044 employees at the end of 2018.

Exhibit 2: Principal governing bodies of Lloyd’s



Source: Aon / Lloyd’s.

Ultimately, Lloyd's is regulated by the Financial Conduct Authority (FCA) and Prudential Regulatory Authority (PRA), under the Financial Services and Markets Act 2000. These bodies directly supervise Lloyd’s managing agents and monitor capital, solvency and conduct across the market.

The FCA, the PRA and Lloyd's have common objectives in ensuring that the market is appropriately regulated. Written co-operation arrangements aimed at reducing duplication of oversight activity have been established and are available via Lloyd’s website.

The Council has 18 members in three different categories, all of whom must be approved by the PRA:

- Working members – six elected broking and underwriting representatives.
- External members – six elected capital provider representatives.
- Nominated members – four independents, plus the Chairman and CEO of Lloyd’s.

The Board was created by the Council in 2003. It currently comprises the Chairman, CEO, CFO and Performance Management Director (PMD) of Lloyd's, three insurance professionals connected with the Lloyd's market and six independents.

It is proposed that the Board merges into the Council with effect from January 1, 2020, with the aim of reducing costs and simplifying governance. If confirmed, this will bring delegated functions back into the Council's remit, change its composition and reduce the overall number of members.

Role of the Corporation

The activities of the Corporation are funded by subscriptions and levies from markets participants. It has three main responsibilities:

- *Market oversight*: The Corporation has statutory and regulatory obligations to act prudently to protect Lloyd's central assets, brand, licenses and reputation. It responds by:
  - Enforcing a minimum standards framework;
  - Operating a business planning and performance monitoring regime; and
  - Ensuring sufficient capital is in place to support Lloyd's financial strength and ratings.
- *Service provision*: Principally delivering the infrastructure needed to process risks placed with Lloyd's underwriters, operating and maintaining the Lloyd's building and supervising Lloyd's international network of trading licenses and offices.
- *Market promotion*: Continually enhancing the attractiveness of the market and promoting its attributes to capital providers, distributors and clients.

Executive committee

Lloyd's senior management team has recently undergone significant changes. Key members include Chairman Bruce Carnegie-Brown (since June 2017), CEO John Neal (since October 2018), PMD Jon Hancock (since December 2016), CFO Burkhard Keese (since April 2019), COO Jennifer Rigby (since July 2019) and CRO David Sansom (interim since October 2018).

Dave Duclos was appointed Non-Executive Chairman of Lloyd's Global Networks in February 2019. He heads a Regional Executive Committee, comprising Hank Watkins for the Americas, Sonja Rottiers for EMEA and Iain Ferguson for Asia Pacific, formed to drive development of the operating model for the international network.

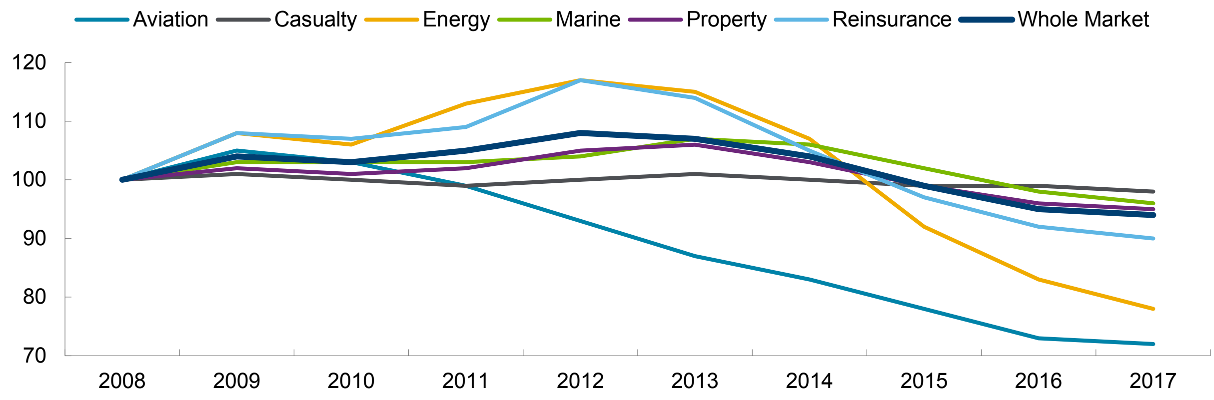
Performance Management

Lloyd's Performance Management Division is headed by PMD Jon Hancock. The syndicate business planning process is run centrally, with the aim of controlling how much business the market writes, what type of exposure is being assumed and how much capital is being deposited in support.

Background to Decile 10

The May 2012 launch of Vision 2025, a new growth-oriented and franchise-building strategic plan, coincided with the start of a five-year period of rate softening. By 2017, Lloyd's gross premiums written (GPW) had increased by a third, partly as a result of the approval of 15 new syndicates. On top of the exposure growth, the net expense ratio increased by around 3% over this period.

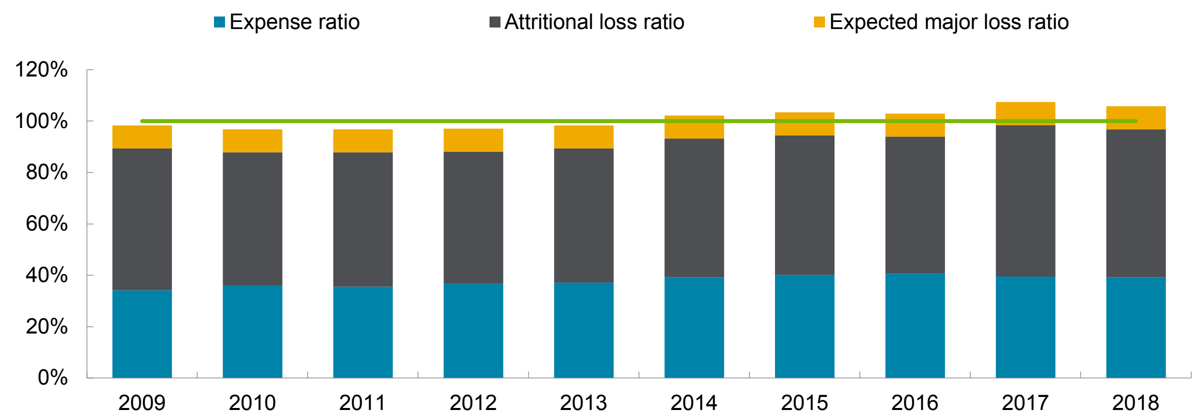
Exhibit 3: Indexed risk adjusted rate changes by pure year of account



Source: Aon / Lloyd's Statistics.

Reported results in the intervening period were flattered by benign major loss activity and favorable reserve development, but the high level of natural catastrophe activity in 2017 exposed the extent to which the market's underlying performance had deteriorated. On a normalized accident year basis, Lloyd's has been posting underwriting losses since 2014, as shown below.

Exhibit 4: Normalized accident year combined ratios



Source: Aon / Lloyd's.

Business planning for 2019

Lloyd's 2017 combined ratio lagged its comparator group by 6.6%, with the worst performing classes and syndicates placing undue strain on the market's results. Amidst only a modest post-loss pricing reaction, it was decided that capital loadings and individual interventions at managing agent level were no longer enough to drive sustainable profitability.

In May 2018, Lloyd's stated that its prudential oversight priority was the need for the market to 'close the performance gap'. Managing agents were required to focus 'Performance Review' activities in three areas:

- Syndicates that had not been profitable for each of the three previous years;
- Under-performing books in eight classes: marine hull, cargo, power, yacht, non-US professional indemnity; overseas motor and non-US direct and facultative property (open market and binder); and
- The worst performing 10% of premium for each syndicate – the 'Decile 10' review.

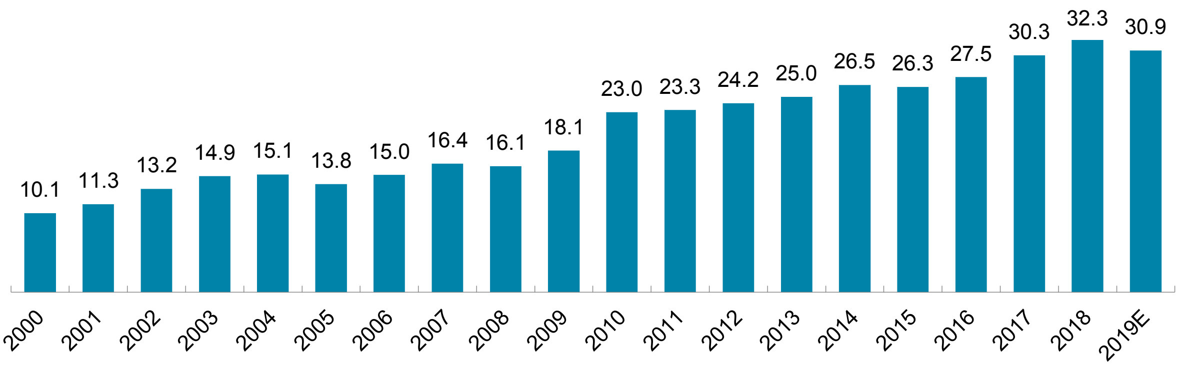
In all cases, managing agents were required to provide detailed performance improvement plans to return the classes or syndicates to sustainable profit over the near term. Failure to agree credible plans with Lloyd's would result in closure of the classes or syndicates concerned. Lloyd's also made it clear that it would reject business plans that did not contemplate a reduction in expenses for 2019. Finally, while Lloyd's stated it was broadly comfortable with the overall level of catastrophe exposure observed across the market, some additional constraints were imposed at syndicate level.

This more interventionist stance coincided with the market-wide issuance of a letter from the Director of Insurance Supervision at the PRA, asking regulated Boards to consider the sustainability of their business models and the adequacy of controls over underwriting and reserving in specialist lines.

2019 underwriting capacity

Lloyd's ended 2018 with authorized underwriting capacity of £32.3bn, around £2.0bn higher than a year earlier and double the level seen at the end of 2008. As a result of the more rigorous business planning process, the market opened 2019 with capacity of £30.9bn, a reduction of £1.4bn, or 4%.

Exhibit 5: Lloyd's underwriting capacity (£bn)



Source: Aon / Lloyd's Statistics.

Several new start-ups were placed on hold, two syndicates went into run-off (Advent 0780 and Standard 1884), almost £3bn of under-performing business left the market and remediation plans were implemented across all review classes.

On the plus side, approved plans made allowance for around £7bn of new business, with modest growth permitted for strong performers, particularly in areas of innovation such as cyber and the sharing economy. Natural catastrophe risk appetite was said to be broadly unchanged.

Lloyd's expects the remediation plans now in place across the review classes to bring the market back to profit in 2019, including an allowance for major losses of around 9% of net premium earned (NPE).

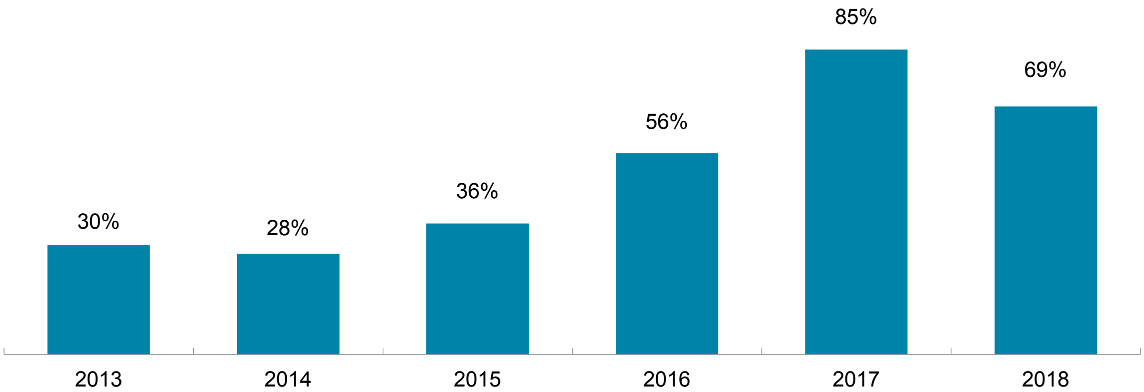
In June 2019, Lloyd's reported that positive rate momentum across 80% of the premium base had prompted almost half of the syndicates to seek approval for mid-year capacity increases.

Business planning for 2020

At a market briefing in June 2019, Lloyd’s placed its 2018 combined ratio at 103% on a normalized basis and noted a widening disparity of syndicate performance between the top quartile at 92.8% and the bottom quartile at 133.6%. There were still said to be too many loss-making syndicates and classes*.

Lloyd’s has made it clear that its approach to performance management will now incorporate the expected annual catastrophe load of 9% of NPE and that greater differentiation will be seen in its treatment of syndicates going forward.

Exhibit 6: Proportion of loss-making syndicates (% of total)



Source: Aon / managing agent disclosure.

The planning cycle for 2020 has been streamlined and the emphasis has changed. The focus on Decile 10 will continue, but conscious efforts are also being made to analyze and grow the best-performing portfolios (Deciles 1 and 2).

Last year’s Performance Review activities have been integrated into the regular planning process, allowing continuous oversight of inadequately performing syndicates and classes, ultimately backed by the threat of closure.

At the same time, 14 consistently strong performers operating with top quartile combined ratios now benefit from lesser oversight and greater control over their business plans, under a newly-introduced ‘light touch’ pilot regime.

Greater differentiation will also be seen in the management of catastrophe risk appetites, following the introduction of the Catastrophe Risk Operational Framework (CROF), a tool that allows Lloyd’s to assess capabilities in this area, with the aim of incentivizing excellence.

Lowering expenses remains a key focus. Managing agents are now required to address the acquisition cost spend as part of the planning process, manage acquisition and administration costs in tandem and embed strong governance and new minimum standards to manage acquisition costs.

Note: * Aon’s analysis indicates that 26 syndicates have reported underwriting losses for the last three years, 13 for the last four years and seven for the last five years.

Membership and Capital Setting

Introduction

Lloyd’s is a society of individual and corporate members (‘capital providers’), who organize themselves into groupings known as ‘syndicates’ for underwriting purposes. These syndicates are run by specialist Lloyd’s managing agents, who accept risk on the members’ behalf.

Syndicates may have one or multiple members and members may participate in one or multiple syndicates. Each member of a syndicate is responsible only for the proportion of each risk written on their behalf. In other words, members of Lloyd's are not jointly responsible for each other's losses.

Syndicates are not legal entities and technically are established only as an ‘annual venture’, with underwriting conducted on a year of account (YOA) basis. In practice, they usually operate from year to year, with members having the right (but not the obligation) to continue their participation.

Members must deposit capital in support of their underwriting commitments in advance of each YOA. The capital-setting process is managed by Lloyd’s in accordance with the prevailing Solvency II regime and is independently overseen and validated by the PRA.

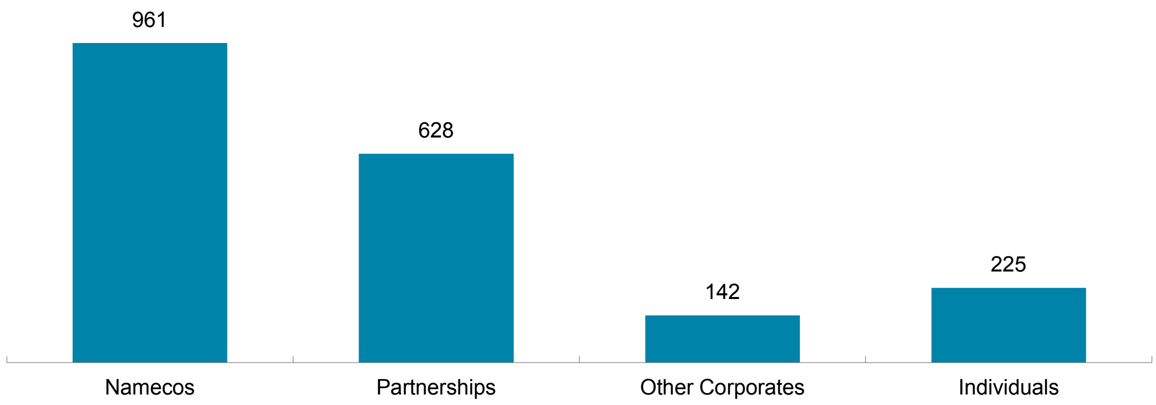
Each member may provide the required capital either by assets held in trust by Lloyd’s specifically for that member (‘Funds at Lloyd’s’), held and managed within a syndicate (‘Funds in Syndicate’), or as the member’s share of the members’ balances on each syndicate on which it participates.

Lloyd’s is responsible for managing the solvency of the membership and the market more broadly. The PRA does not regulate Lloyd’s members directly, but requires the membership as a whole to maintain continuous solvency, in line with other United Kingdom (UK) insurers.

Active membership

The number of active members of Lloyd’s has remained relatively stable at around 2,000 over the last decade. The high-level split by type of member in 2019 is shown below.

Exhibit 7: Lloyd’s active membership in 2019



Source: Aon / Lloyd’s.

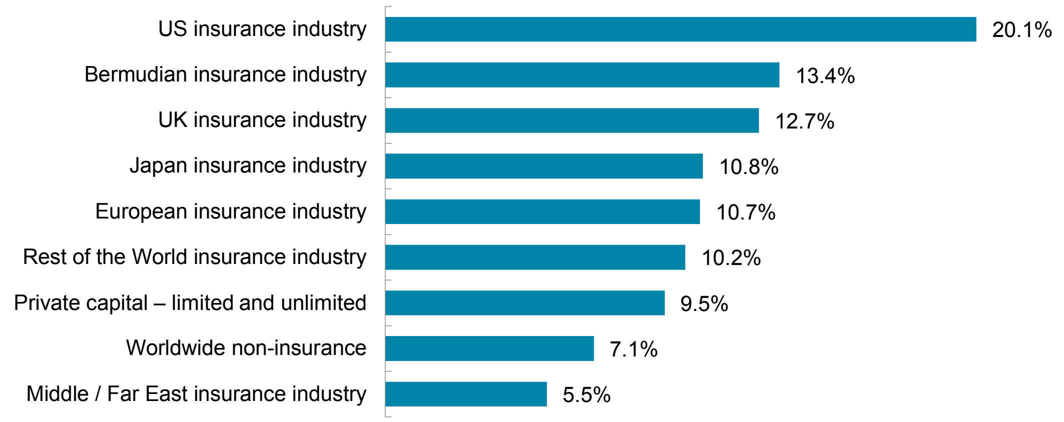
There are now 1,731 corporate members operating on a limited liability basis and 225 high net worth individuals or ‘Names’ underwriting with unlimited liability. The latter status confers tax advantages, but no new members have been admitted on this basis since March 2003.

The number of Names has fallen by around 70% over the last decade, as many have moved to limit their liability by forming Namecos and Partnerships. These vehicles can also be established by new individual and corporate capital providers wishing to participate at Lloyd's for the first time.

The various categories of corporate member undertake the vast majority of the underwriting at Lloyd’s. Traditional Names now provide less than 2% of the capital supporting the market.

Around 90% of the market's capital is provided on an 'aligned' basis, meaning there is common ownership between the corporate member and the managing agent. More than 80% is provided by multi-platform insurance companies. The recently published Lloyd's Prospectus indicated that global carriers write 57% of Lloyd's business. Private (third party) capital providers operating on both a limited and unlimited liability basis represent just under 10% of the market, as shown below.

Exhibit 8: Lloyd's capital providers by source and location (%)



Source: Aon / Lloyd's.

Members pay fees at Lloyd's discretion, notably annual subscriptions (charged at 0.36% of gross premiums written in 2019), Central Fund contributions (0.35%), Central Fund syndicate loans (0.33%), market modernization levies (0.07%) and various overseas operating charges. For new corporate members, the Central Fund contribution rate is 1.4% for the first three years.

Capital setting

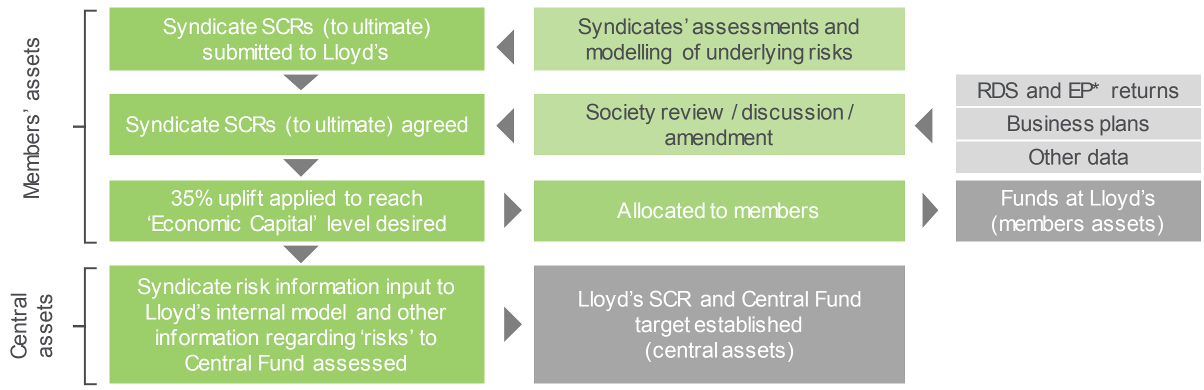
Each syndicate is required to calculate its Solvency Capital Requirement (SCR) for the prospective underwriting year, representing the amount of capital required to withstand a 1-in-200-year loss event over a one-year horizon on an ultimate view of risk.

Managing agents derive the SCRs from their own approved internal models. Submitted SCRs are subject to review by the Corporation and approval by Lloyd's Capital and Planning Group.

Approved syndicate-level SCRs drive the determination of member-level SCRs, which are based on the member's share of each syndicate. Where a member participates on more than one syndicate, a credit for diversification is provided to reflect the spread of risk.

Lloyd's also conducts detailed analysis to assess the additional economic capital required to meet its risk appetite and to support the market's ratings and global license network. This results in a capital uplift to members' SCRs (currently 35%), to arrive at a final Economic Capital Assessment (ECA).

Exhibit 9: Lloyd's capital setting process



Source: Aon / Lloyd's.
Notes: * Realistic Disaster Scenario and Exceedance Probability distributions.

Syndicates are required to keep their business plans and supporting SCRs under continuous review. All members must demonstrate that they have sufficient funds to meet their capital requirements in June and November each year, known as 'coming-into-line' (CIL).

Incurred losses and/or increases in risk profile may erode member capital between assessments. Lloyd's has the powers to require members to meet their ECA at all times, but the actual response typically depends on the extent of the shortfall:

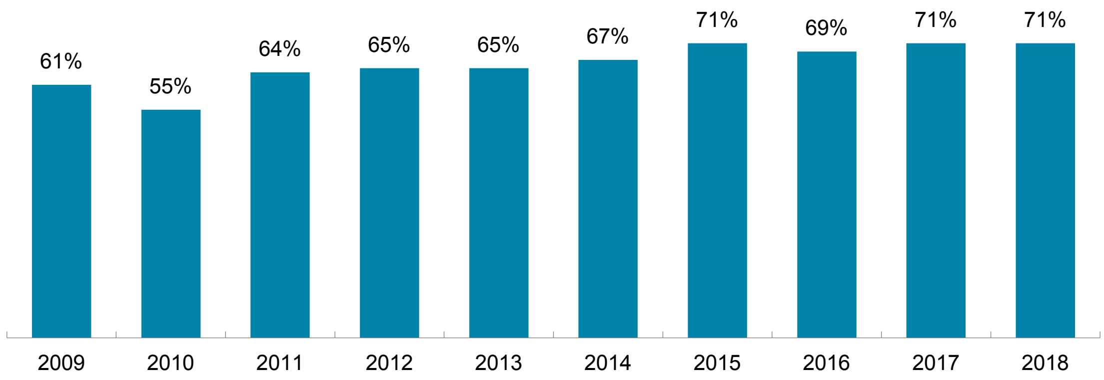
- Less than 10% of the ECA: usually allowed to persist until the next CIL date.
- More than 10% of the ECA but ultimate SCR still covered: at a minimum, Lloyd's will expect an accelerated injection of capital to reduce the shortfall to no more than 10% of the ECA.
- Shortfall against ultimate SCR: shortfall must be reduced to no more than 10% of the ECA within 30 days of notification.

If members do not recapitalize, their authority to continue to trade is restricted to the level of their available capital and can ultimately be fully withdrawn.

Capital efficiency

Tracking economic capital as a percentage of premium shows that Lloyd's has lost capital efficiency over the last decade. Lloyd's attributes this to lower pricing and Solvency II capital requirements.

Exhibit 10: Market ECA vs gross premium



Source: Aon / Lloyd's.

Under Solvency II rules stipulating that no more than 50% of the SCR is met via Tier 2 capital, Lloyd's had approximately £2bn of letters of credit (LOCs) that were ineligible for solvency coverage or rating agency capital purposes at the end of 2017.

As a result, Lloyd's has introduced restrictions on the use of LOCs, diluting a key capital advantage. Maximum utilization of LOCs has been cut to 90% of ECA for 2019, 70% for 2020 and 50% for 2021. In addition, any open year solvency deficits must now be covered by Tier 1 capital.

Capacity

The level of underwriting risk assumed by each member on a particular YOA is regulated by fixing an overall premium income limit (OPL) in relation to the member's assets. This is stated in sterling and is gross of reinsurance, but net of brokerage.

The annual stamp capacity of an individual syndicate is based on an aggregation of those parts of the OPL of each member which are allocated to that particular syndicate. The annual capacity of the Lloyd's market is determined by aggregating the stamp capacity of all active syndicates.

New investors wishing to underwrite at Lloyd's must gain the right to participate on one or more syndicates. This can be achieved by negotiating directly with the relevant managing agents, or by utilizing the services of a specialist members' agent.

Historically, allocated capacity conveyed 'freehold tenancy in perpetuity'. In recent years, allocations have tended to take place on a more flexible 'limited tenancy' basis, meaning that participations are agreed for a defined period of time.

Capacity auctions conducted in late October / early November allow existing members to buy and sell syndicate participation rights for the following year of account.

Achieving finality

Every YOA must be left open for a three-year period. The account is normally then closed via a reinsurance-to-close (RITC) transaction, based on an independent valuation of the reserves. Only at this stage can supporting capital be released.

While a YOA is open, premiums and other monies received by members are held in trust for them by their managing agents, subject to the discharge of their liabilities. These premiums trust funds (PTFs) are available to fund overseas regulatory deposits, claims, return premiums, underwriting expenses and (once a YOA has been closed) any profit payable to the member after providing for future liabilities.

An RITC transfers the responsibility for discharging all the liabilities that attach to the YOA, plus the right to any income due to the closing YOA, into an open YOA of the same or a different syndicate, in return for a premium (normally 100% of the liabilities).

If the liabilities attaching to a particular YOA cannot be quantified after three years, the YOA will be left open ('in run-off') until a RITC can be put in place, or all the liabilities are extinguished. During this time, there can be no distribution of profit to members and no release of supporting capital.

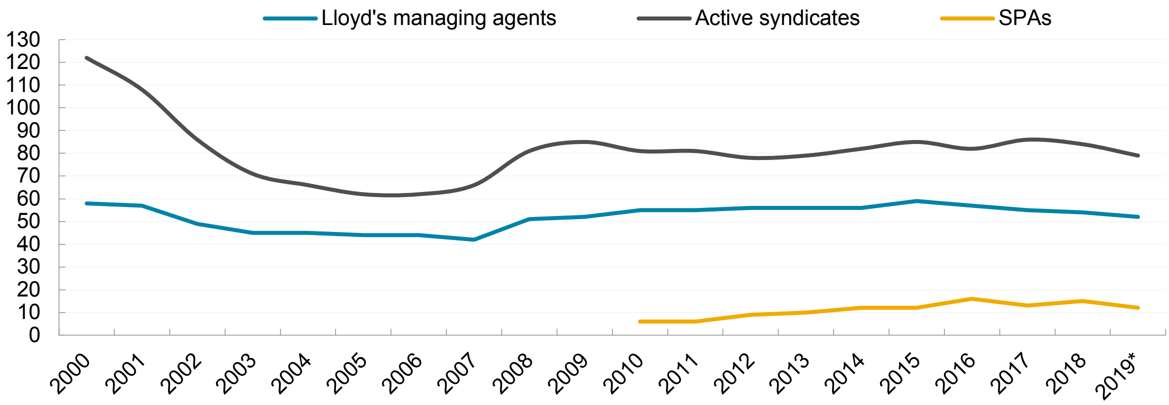
RITC transactions are reinsurance contracts. As with other reinsurance contracts, members of a syndicate for a particular YOA remain liable on policies allocated to that year, but have the benefit of a reinsurance contract under which they are entitled to recover losses from the reinsuring syndicate.

Syndicate Developments

During 2018, there were 84 syndicates and 15 special purpose arrangements (SPAs)*, overseen by 54 Lloyd's managing agents. Five syndicates have since ceased trading, namely AmTrust 0044, Advent 0780, Standard 1884, Skuld 1897 and AXIS 2007 (previously Novae). In the latter case, business continuity was maintained via the transferal of renewal rights to AXIS 1686. Four SPAs were terminated at the year-end.

Currently, there are 79 active syndicates and 12 SPAs, overseen by 52 managing agents. These numbers are likely to reduce over the medium term, driven by in-market consolidation.

Exhibit 11: Number of syndicates and managing agents

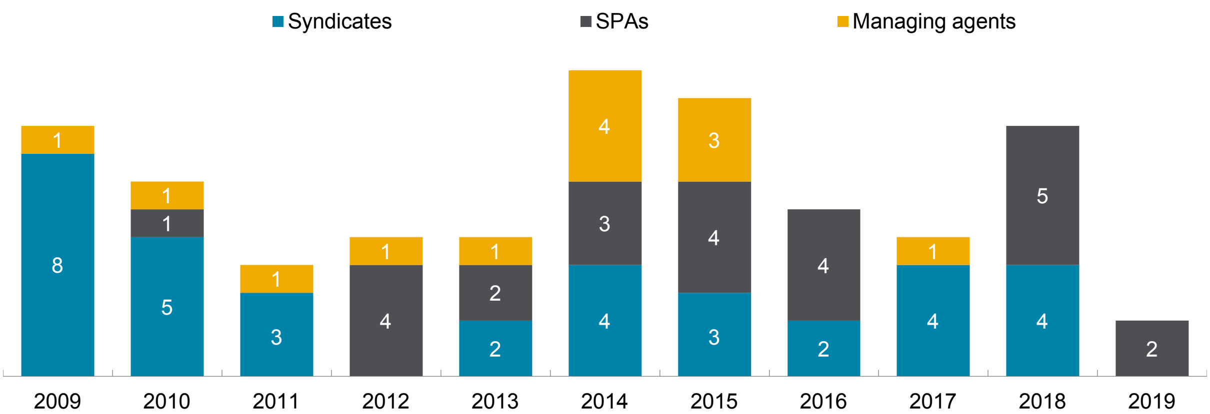


Source: Aon / Lloyd's.
Note: * At August 30.

New entrants

Establishing a new business at Lloyd's has become more challenging in recent years, due to the increased regulatory burden and high levels of competition in the market. There have been examples of new syndicates being formed, generally utilizing the services of established third party managing agents, but Lloyd's has preferred to see SPAs formed and operating alongside existing syndicates for some time (typically three years), prior to granting independent approval. For this reason, prospective new entrants have often taken the view that acquiring an established operation is the better option.

Exhibit 12: Lloyd's approvals since 2009



Source: Aon / Lloyd's.

Note: * An SPA solely provides quota share capacity to a host syndicate and is not market-facing.

New syndicates and SPAs formed over the last two years are summarized below. The only new vehicle at the start of 2019 was Apollo 1971, which is classified as an SPA. From July 1, another new SPA backed by The Medical Protection Society began trading.

Exhibit 13: New syndicate / SPA formations

Number	Managing agent	Inception	Details
1947	Pembroke	2018	New property focused syndicate; backed by GIC Re
1975	Coverys	2018	New healthcare liability syndicate; backed by Coverys
1980	Asta	2018	Launched as 'Pioneer' (previously part of Liberty 4472); backed by Liberty
3268	Asta	2018	Launched as 'Agora' (previously SPA 6126); mixed capital support
5623	Beazley	2018	Quota share of Beazley 3623 ('Beta'); mixed capital support
6131	Asta	2018	Quota share of Dale 1729 ('Magna'); backed by ProAssurance
6132	Barbican	2018	Quota share of Barbican 1955; backed by Toa Re
6133	Apollo	2018	Quota share of Apollo 1969 ('Apollo Re'); mixed capital support
6134	Argenta	2018	Quota share of Argenta 2121; backed by Hannover Re
1971	Apollo	2019	Quota share of Apollo 1969 ('iBOTT Rover); mixed capital support
TBC	Asta	2019	Quota share of Everest Re 2786; backed by The Medical Protection Society

Source: Aon.

Corporate activity

The ownership of a significant number of managing agents has changed over the last three years, driven by a combination of Lloyd's-specific deals and broader market consolidation. These transactions are summarized below. High levels of corporate activity are expected to continue over the medium term, as increasing pressure on under-performing syndicates drives in-market mergers.

Exhibit 14: Recent transactions involving Lloyd's managing agents

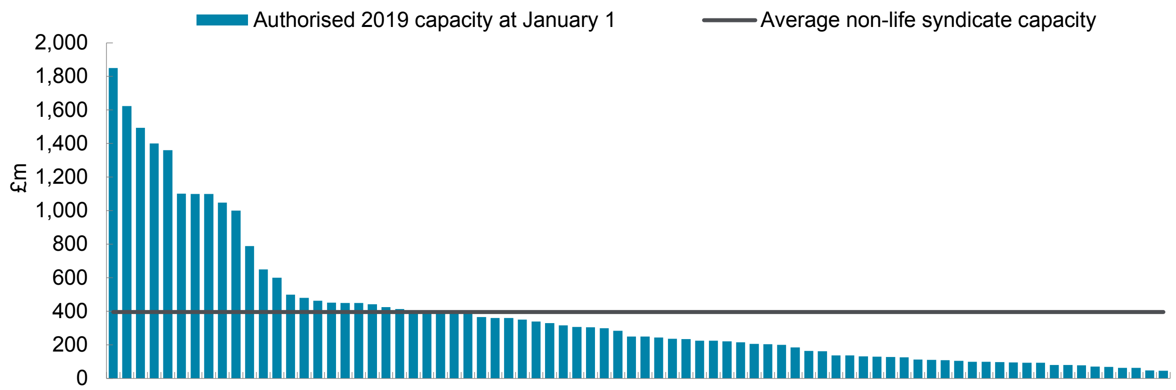
Acquirer	Target	Date announced	Syndicates affected
CPPIB	Ascot	September 2016	1414
Sompo	Endurance	October 2016	5151
Liberty Mutual	Ironshore (Pembroke)	December 2016	4000
Fairfax	Allied World	December 2016	2232
Hannover Re	Argenta	March 2017	2121
AXIS	Novae	July 2017	2007
Centerbridge	Canopius	August 2017	4444
AIG	Validus (Talbot)	January 2018	1183
AXA	XL Catlin	March 2018	2003
Hartford	Navigators	August 2018	1221
Apollo	Aspen	August 2018	4711
China Re	Chaucer	September 2018	1084, 1176
Hamilton Re	Pembroke	March 2019	4000
Canopius	AmTrust at Lloyd's	April 2019	1861
Arch	Barbican	July 2019	1955

Source: Aon.

2019 capacity distribution

The distribution of authorized stamp capacity by syndicate in 2019 is shown below. The average underwriting capacity of a non-life syndicate at Lloyd's now stands at £396m.

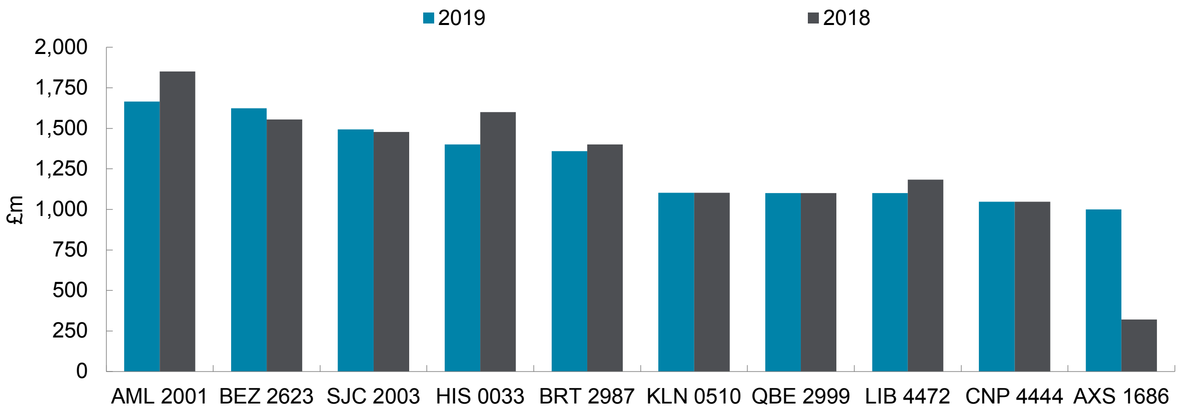
Exhibit 15: 2019 syndicate capacity



Source: Aon.

The capacity of the 10 largest syndicates in 2019 aggregates to £12.9bn, representing 42% of the total market. The sharp increase at AXIS 1686 was driven by the acquisition of Novae.

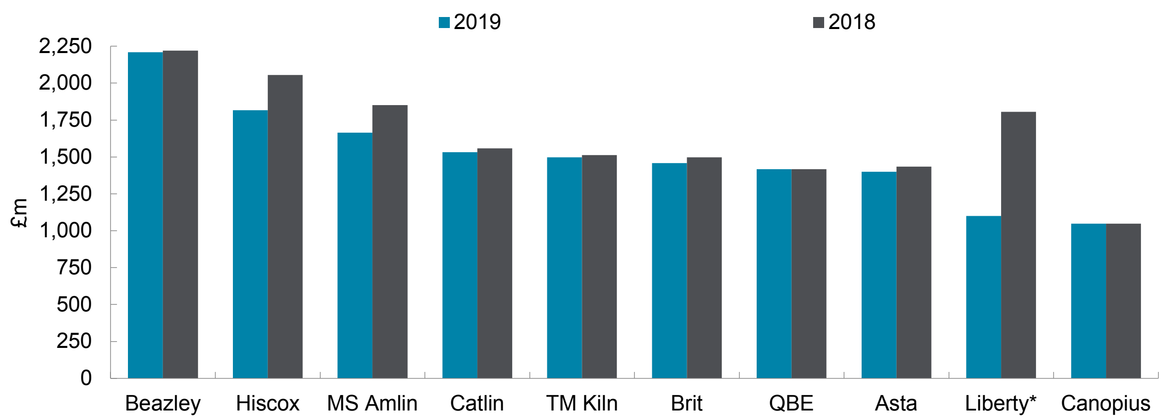
Exhibit 16: Top 10 syndicates by 2019 capacity



Source: Aon.

Capacity managed by the 10 largest Lloyd's managing agents aggregates to £15.1bn in 2019, representing 49% of the total market.

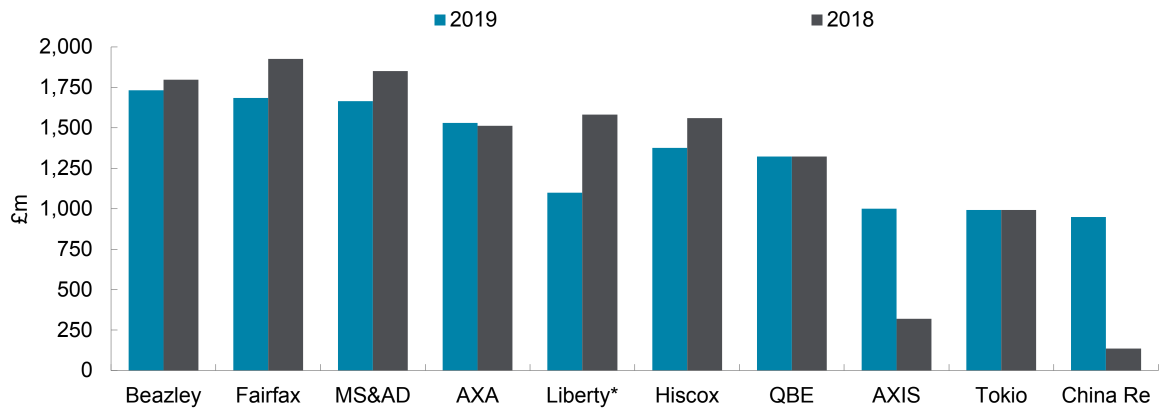
Exhibit 17: Top 10 managers by 2019 capacity



Source: Aon.
Notes: * The reduction in 2019 reflects the sale of Pembroke to Hamilton Insurance (£477m of managed capacity).

Aon estimates that the capacity supplied by the 10 largest capital providers at Lloyd's aggregates to £13.7bn in 2019, representing 43% of the total market. The sharp increases at AXIS and China Re are driven by the acquisitions of Novae and Chaucer, respectively.

Exhibit 18: Top 10 providers of 2019 capacity



Source: Aon.
Note: * The reduction in 2019 reflects the sale of Pembroke to Hamilton Insurance (£236m of supported capacity).

Business Position

Introduction

Lloyd's retains an unrivalled concentration of specialist underwriting expertise and the ability to transact direct insurance in 75 jurisdictions and reinsurance in more than 200 countries and territories. The market has operations in 25 countries and established offices in Singapore, Japan, China, Canada, Brazil, India, Belgium and the United Arab Emirates.

Underwriting activity is still mainly focused in London, but increasing volumes of premium are being sourced from around the world via delegated underwriting authority (DUA) arrangements. In China (since 2007) and Europe (from 2019), business is fronted by locally-licensed subsidiaries.

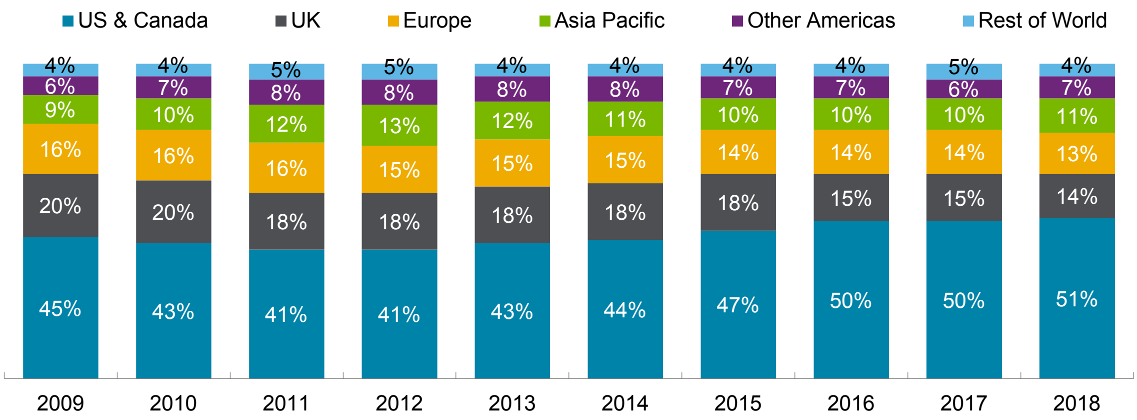
Reported gross premiums written (GPW) have increased by 60% over the last decade, reaching £35.5bn in 2018. The weakening of sterling over this period has flattered the growth rate, given that around 60% of the account is originally denominated in US dollars.

Lloyd's is estimated to have a 5% share of the $750bn global commercial non-life market, but is recently perceived to have lost ground in emerging economies and assumed reinsurance. In July 2019, CEO John Neal said he saw no reason why Lloyd's market share shouldn't double over time.

Geographic spread

The principal changes over the last decade have been an increase in the contribution from North America to around 50% of GPW and a reduction from the UK to around 15%. There is little discernible impact from the 2012 launch of the 'Vision 2025' initiative, which envisaged a 25% contribution from emerging markets by 2025. More recently, Brexit has constrained growth in Europe.

Exhibit 19: Lloyd's GPW – Geographic spread



Source: Aon / Lloyd's.

Vision 2025 had a focus on acquiring new licenses and Lloyd's has continued to build its international network, opening new offices in Mexico City, Bogotá, Dubai, Casablanca and Mumbai. However, this is a costly process and actual experience on the ground has tended to be challenging. As a result, some managing agents have recently reduced their overseas underwriting activity.

In response to market feedback, John Neal has shifted Lloyd's short-term focus to maximizing business opportunities in existing core markets, notably the United States (US), which is estimated to generate around half of global commercial non-life premium.

The emerging markets, and particularly the Asia-Pacific region, clearly represent the long-term opportunity. However, Lloyd’s strategy must recognize certain realities:

- Post-globalization / digitalization, business no longer comes to London in the way that it did
  - Customers prefer to place business in their local markets as underwriting expertise and capacity grows, particularly for more standardized specialty risks.
  - The emergence of new centers of capital (e.g. Miami, Dubai, Singapore) has given customers access to new markets operating with a significantly lower cost base.
  - The growing local strength of global insurers tends to result in greater risk retention.
- The license network is extensive, but there are gaps and growing protectionism is hindering progress. Often Lloyd’s holds only a reinsurance license and has limited local capabilities.
- Where Lloyd's has a direct license, the coverholder approach has worked well, but often there are regulatory restrictions on the type of business that can be written.
- London offices of global carriers generally seek to avoid competing with their growing local insurance networks.

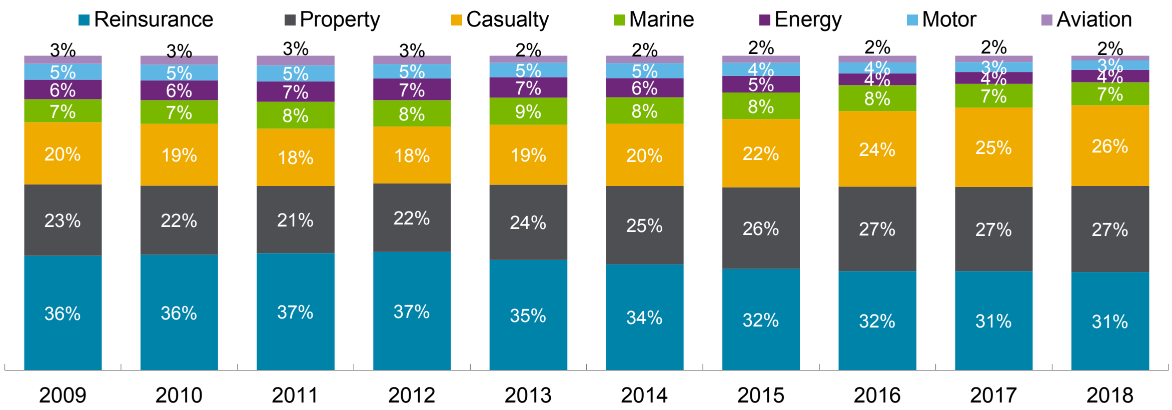
The ‘Future at Lloyd’s’ initiative envisages reaching customers overseas more quickly and efficiently via digital platforms that compensate for the lack of a physical presence on the ground. The aim is to deliver new standardized products, greater access for brokers worldwide and lower frictional costs.

Business mix

Lloyd’s direct insurance premiums have increased by around 75% over the last decade. Lloyd’s has been the leading excess and surplus writer in the US since 2011.

Growth in assumed reinsurance has lagged at just under 40% and this segment now represents 31% of the whole account, down from 36% in 2009. The reduction in market share has principally been driven by changes in the buying behavior of customers, the growth in influence of alternative capital providers and increased competition from emerging market reinsurers.

Exhibit 20: Lloyd’s GPW – Classes of business



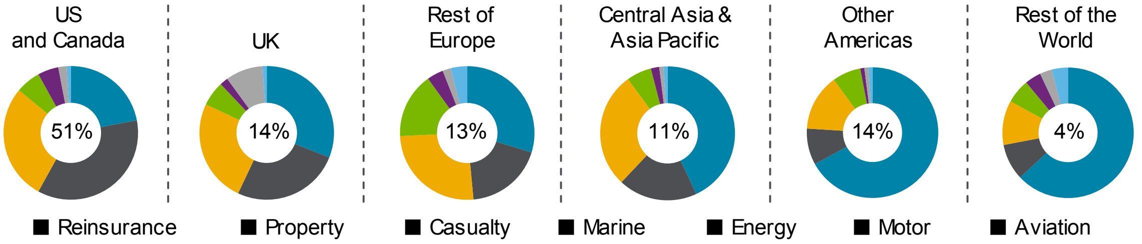
Source: Aon / Lloyd’s.

Total Insurance GPW rose by 6% to £24.4bn in 2018, split Property £9.7bn (+8%), Casualty £9.1bn (+7%), Marine £2.6bn (+4%), Energy £1.4bn (+12%), Motor £1.0bn (-2%) and Aviation £0.5bn (-20%). Growth was driven by US binders in the case of Property and by cyber, warranty and indemnity and US general liability business in the case of Casualty.

Total Reinsurance GPW rose by 5% to £11.1bn, split Property £6.4bn (+8%), Casualty £2.5bn (+14%) and Specialty £2.1bn (-11%). The latter book was split Marine £1.1bn (-7%), Energy £0.6bn (-17%) and Aviation £0.4bn (-13%).

The table below shows the breakdown of Lloyd's GPW in 2018 by class of business for each geographic region. Reinsurance features much more heavily in emerging markets.

Exhibit 21: 2018 Regional portfolio mix



Source: Aon / Lloyd's.

Brexit

The UK is now scheduled to leave the European Union (EU) on October 31, 2019. A great deal of uncertainty remains over how this happens and a 'no-deal' Brexit is now viewed as a very real possibility.

Lloyd's Insurance Company S.A. (Lloyd's Brussels) has been formed to ensure that Lloyd's partners across Europe can continue to access the market's underwriting expertise and financial security, whatever the eventual outcome of the political process.

Lloyd's Brussels is regulated by the National Bank of Belgium and licensed to write all non-life risks from the European Economic Area (EEA). The company began underwriting on January 1, 2019, on the basis that all policies are 100% reinsured back to the syndicates in London. It has a network of 19 branches and is working with over 400 coverholders and 40 Lloyd's brokers across Europe.

Lloyd's Brussels is capitalized to Solvency II standards. Supporting capital stood at EUR201m at the end of 2018, reflecting the fact that no risk is retained locally. The company carries the same financial strength ratings as Lloyd's, as it is viewed as a core subsidiary with extensive reinsurance support.

As far as legacy business is concerned, Lloyd's has publicly committed to continue honoring contractual obligations and paying valid claims, whatever shape Brexit eventually takes. It has also undertaken to legally transfer all EEA non-life business written by the market between 1993 and 2018 to Lloyd's Brussels, under Part VII of the UK's Financial Services and Markets Act 2000.

The planned transfer will need the approval of the appointed Independent Expert, the FCA and PRA, the National Bank of Belgium and the UK High Court. It is currently scheduled for October 2020 and will only be cancelled if the UK stays in the EU, or if it becomes certain that UK carriers will retain passporting rights across the single market post-withdrawal.

In the meantime, it is expected that the February 2019 publication of an EIOPA recommendation that competent authorities in the EU should apply a legal framework or mechanism to facilitate the orderly run-off of European business will result in Lloyd's approach being respected.

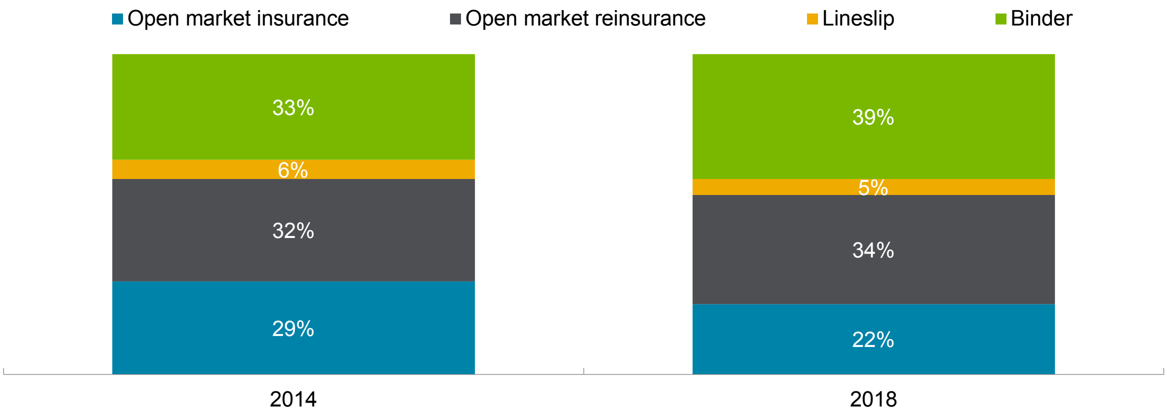
Lloyd's has introduced new mandatory syndicate loans, with the aim of eliminating the need to raise additional capital from members to fund the expansion of Lloyd's Brussels. Lloyd's will also consider how to raise capital to support the transfer of members' EEA business 'in due course'.

Distribution

There were 303 registered Lloyd's brokers at the end of 2018. The recently published Lloyd's Prospectus stated that the three largest global brokers placed 41% of Lloyd's premiums. In addition, policyholders were able to access the market via 3,936 coverholder locations and 378 service companies.

Coverholders are third parties authorized by Lloyd's managing agents to accept insurance risks on behalf of their syndicates under a binding authority. Service companies are similarly authorized, but share common ownership with the managing agent and can sub-delegate. All distributors must be approved by Lloyd's and are subject to periodic review.

Exhibit 22: Method of placement at Lloyd's



Source: Lloyd's Prospectus.

On a year of account basis, open market insurance and reinsurance business represented 56% of Lloyd's total GPW in 2018, down from 61% in 2014. DUA business written under binders and lineslips (also known as broker facilities or schemes) represented 44% of Lloyd's total GPW, up from 39% in 2014. In total, there are now around 6,000 binding authority agreements in-force across the market.

The 'Future at Lloyd's' initiative recognizes that the broker and coverholder constituencies have very different demands and expectations and that both need to be accommodated.

Ratings

All syndicates benefit from Lloyd's financial strength ratings, which apply to every policy issued since 1993. The Standard & Poor's rating carried a negative outlook from October 2017 to June 2019, at which point the outlook was revised to stable, based on portfolio remediation and improved capitalization. The Fitch rating has carried a negative outlook since June 2017.

Lloyd's Insurance Company S.A. (Belgium) and Lloyd's Insurance Company (China) Limited carry the same ratings as Lloyd's, as they are viewed as core subsidiaries backed by extensive reinsurance support.

Exhibit 23: Lloyd's financial strength ratings

	Rating	Outlook	Last affirmed
A.M. Best	A	Stable	July 10, 2019
Fitch Ratings	AA-	Negative	May 24, 2019
Standard & Poor's	A+	Stable	July 18, 2019

Source: Rating agencies.
Note: Ratings at August 27, 2019.

Only seven syndicates are now rated by A.M. Best on a standalone basis: Hiscox Syndicate 0033, Beazley Syndicates 0623, 2623, 3622 and 3623, MS Amlin Syndicate 2001 and Markel Syndicate 3000. All are at the market level of 'A' / Stable. There are no other standalone syndicate ratings in effect.

Operating Performance

Over the last decade, Lloyd's has reported an average combined ratio of 96.0%, an average investment yield of 2.1% and an average return on capital of 7.3%. Underwriting results have lagged the comparator group over the last two years, heightening the focus on addressing under-performing books of business, containing catastrophe risk and reducing expenses.

Exhibit 24: Lloyd's pro-forma results

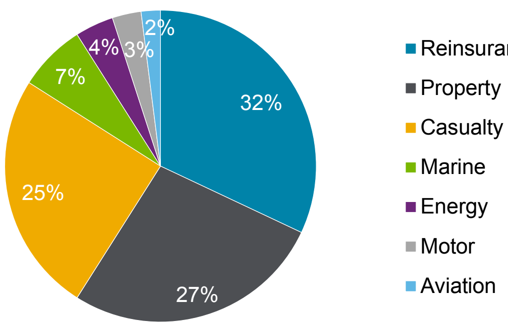
Income statement £m	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	1 Year change
GPW	21,973	22,592	23,337	25,173	25,615	25,259	26,690	29,862	33,591	35,527	5.8%
NPW	17,218	17,656	18,472	19,435	20,231	20,006	21,023	23,066	24,869	25,681	3.3%
NPE	16,725	17,111	18,100	18,685	19,725	19,499	20,565	22,660	24,498	25,178	2.8%
Underwriting result	2,389	915	-1,218	1,744	2,827	2,253	2,047	468	-3,421	-1,130	n.m.
Investment result	1,769	1,258	955	1,311	839	1,038	402	1,345	1,800	504	-72%
Pre-tax result	3,868	2,195	-516	2,771	3,205	3,016	2,122	2,107	-2,001	-1,001	-50%
Key ratios											
Cession ratio	21.6%	21.8%	20.8%	22.8%	21.0%	20.8%	21.2%	22.8%	26.0%	27.7%	1.7pp
Combined ratio	85.7%	94.7%	106.7%	91.1%	86.8%	88.4%	90.0%	97.9%	114.0%	104.5%	-9.5pp
Investment yield	3.9%	2.6%	1.9%	2.6%	1.6%	2.0%	0.7%	2.2%	2.7%	0.7%	-2.0pp
Return on capital*	23.9%	12.1%	-2.8%	14.8%	16.2%	14.1%	9.1%	8.1%	-7.3%	-3.7%	3.6pp

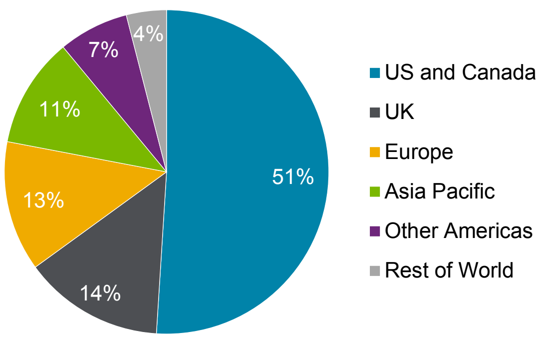
Source: Aon / Lloyd's.
Note: * Capital, reserves, subordinated loan notes and securities

Premium income

GPW rose by 6% to £35.5bn in 2018, split Insurance £24.4bn (+6%) and Reinsurance £11.1bn (+5%). The overall increase was 10% at constant exchange rates (sterling strengthened by 4% against the US dollar during the year). Average risk-adjusted renewal rates rose by 3%, only partially reversing a reduction of around 20% experienced in the period since 2010.

Exhibit 25: Lloyd's business mix





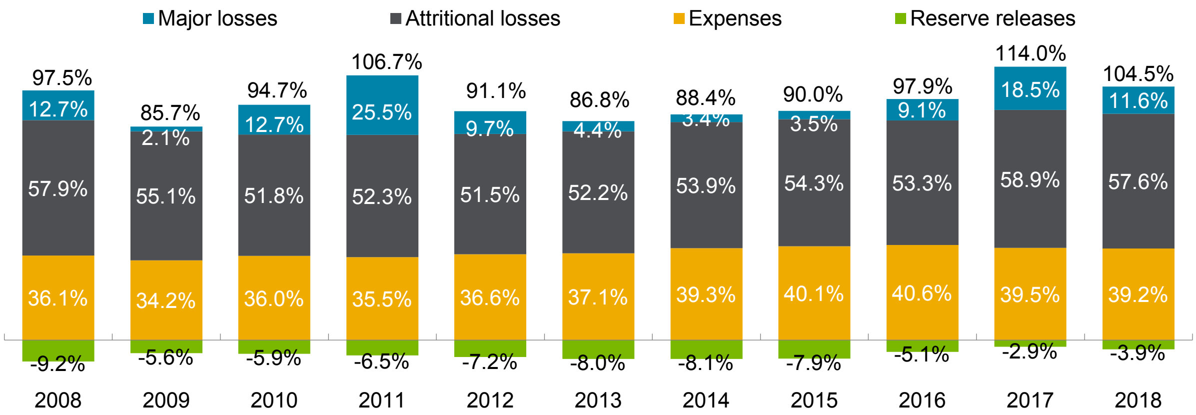
Source: Aon / Lloyd's.

The outwards reinsurance cession ratio has risen over the past two years, partly due to the cost of reinstating cover in the wake of significant catastrophe events. The total external spend increased to £9.8bn in 2018. At the syndicate level, an additional £643m of premium was ceded to SPAs in 2018, up from £589m in 2017. These amounts are eliminated from the consolidated accounts.

Underwriting performance

NPE rose by 3% to £25.2bn in 2018, the split by class of business being Reinsurance 31%, Property 27%, Casualty 25%, Marine 7%, Energy 4%, Motor 3% and Aviation 2%. An underwriting loss of £1.1bn was sustained, after a deficit of £3.4bn in 2017. This represented a net combined ratio of 104.5% in 2018, down from 114.0% in the prior year.

Exhibit 26: Lloyd's combined ratios



Source: Aon / Lloyd's.

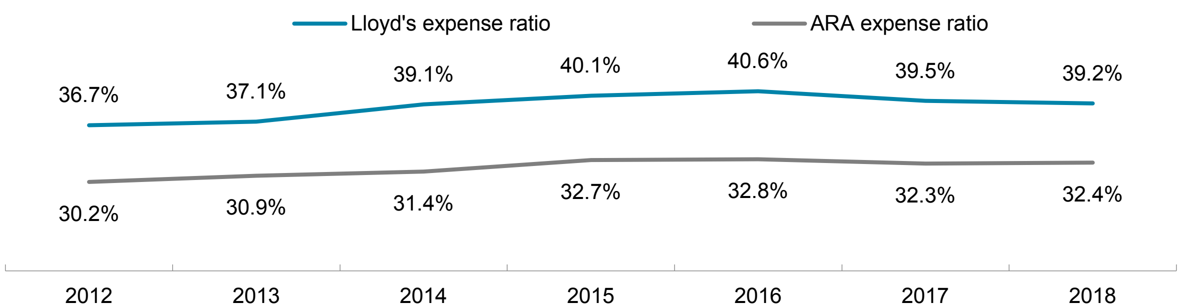
On an accident year basis, the 2018 net loss ratio stood at 69.2% (2017: 77.4%). Attritional losses improved modestly but remained at an elevated level, driven by underlying claims inflation, deductible erosion and recent softening of pricing and terms and conditions.

Major claims, defined as natural catastrophe and man-made losses exceeding £20m, cost £2.9bn net of reinsurance and reinstatement premiums in 2018, representing 11.6% of NPE. The largest losses were Hurricanes Michael (£0.8bn) and Florence (£0.5bn), California wildfires (£0.7bn) and Typhoon Jebi (£0.4bn). In 2017, major claims stood at £4.5bn (18.5%), including Hurricanes Irma (£1.6bn), Harvey (£1.2bn) and Maria (£0.8bn), California wildfires (£0.5bn) and Mexico earthquakes (£0.3bn).

Prior year reserves developed favorably overall in 2018, for the 14th successive year. Releases of £976m (£706m) represented 3.9% (2.9%) of NPE, resulting in a calendar year net loss ratio of 65.3% (74.5%). The surplus arose across all major classes of business, except Marine, with only small movements seen on the reserves held in respect of the 2017 catastrophe events.

Lloyd's expense ratio has improved modestly over the last two years but continues to track around seven percentage points higher than Aon's Reinsurance Aggregate (the ARA), as shown in Exhibit 27. The main drivers of the gap are the more fragmented structure of Lloyd's and the higher acquisition costs associated with binder and managing general agency (MGA) business.

Exhibit 27: Lloyd's vs ARA combined ratio

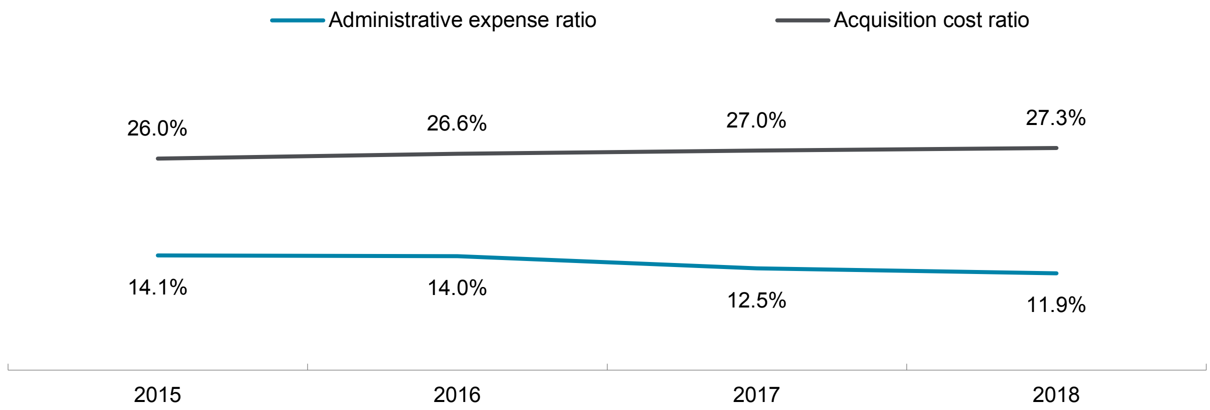


Source: Aon / Lloyd's.
Note: The ARA constituents are Alleghany, Arch, Argo, Aspen, AXIS, Beazley, Everest Re, Fairfax, Hannover Re, Hiscox, Lancashire, Mapfre, Markel, Munich Re, Partner Re, Qatar Insurance, QBE, RenRe, SCOR, Sirius, Swiss Re, Third Point Re and W.R. Berkley. Between them, the ARA companies control around 40% of Lloyd's capacity.

Recent development of Lloyd's disclosed administrative expense and acquisition cost ratios is shown in Exhibit 28. The administrative expense ratio has shown consistent improvement since 2015, while the acquisition cost ratio has steadily increased over this period.

The administrative expense ratio can be influenced by movements in exchange rates, as around 60% of premiums are denominated in US dollars, while the bulk of fixed costs are booked in sterling.

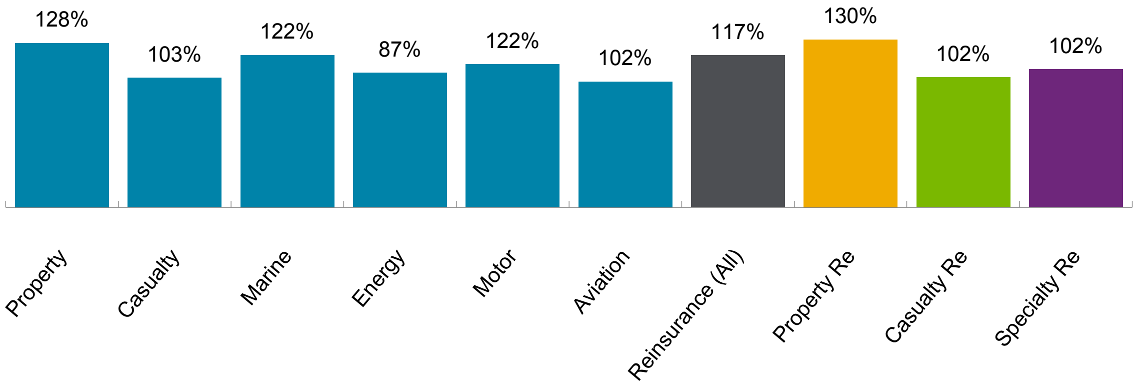
Exhibit 28: Lloyd's expense ratio split



Source: Aon / Lloyd's.

Combined ratios by class of business in 2018 are shown below. Comprehensive data summarizing historical segmental performance can be found in Appendix 1.

Exhibit 29: Segmental combined ratios

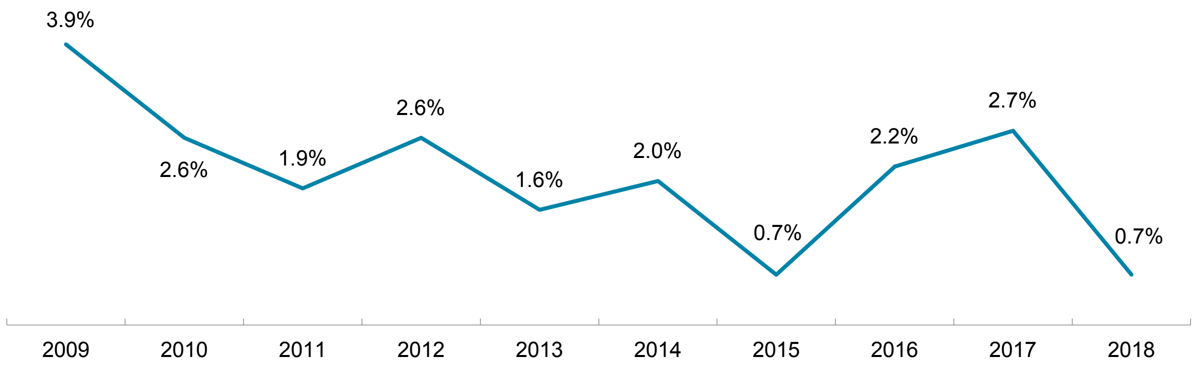


Source: Aon / Lloyd's.

Investment return

Lloyd's total investment return stood at £0.5bn in 2018, down from £1.8bn in 2017. Ordinary investment income fell by a third to £985m and realized and unrealized losses of £17m and £464m respectively were reported, compared with gains of £261m and £89m in the prior year. Total yields achieved over the last decade are shown below.

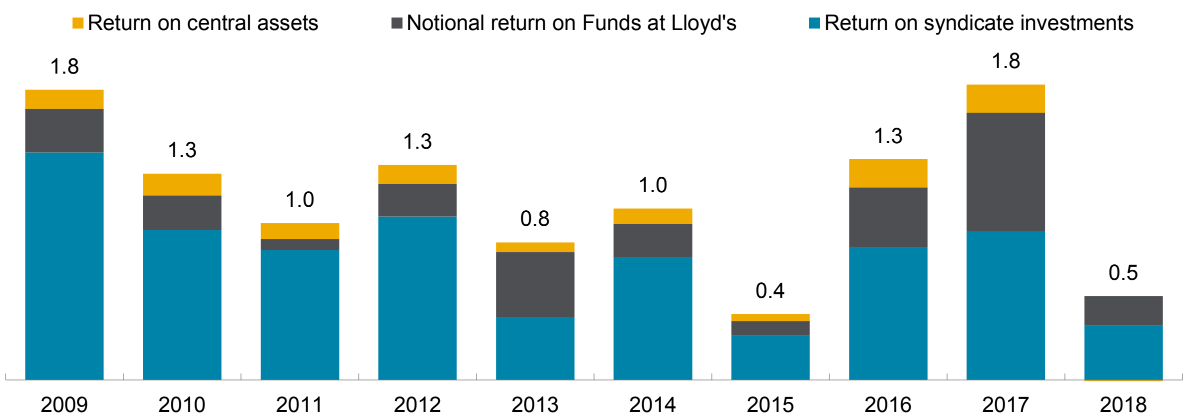
Exhibit 30: Lloyd's investment yield



Source: Aon / Lloyd's.

The three components of Lloyd's investment return are shown in Exhibit 31.

Exhibit 31: Lloyd's investment return (£bn)



Source: Aon / Lloyd's.

The 2018 return on syndicate premium trust fund assets, which are invested by managing agents, was materially lower at £333m (2017: £907m), or 0.8% (2.2%), driven by disappointing corporate bond returns and negative performance in equity and growth assets.

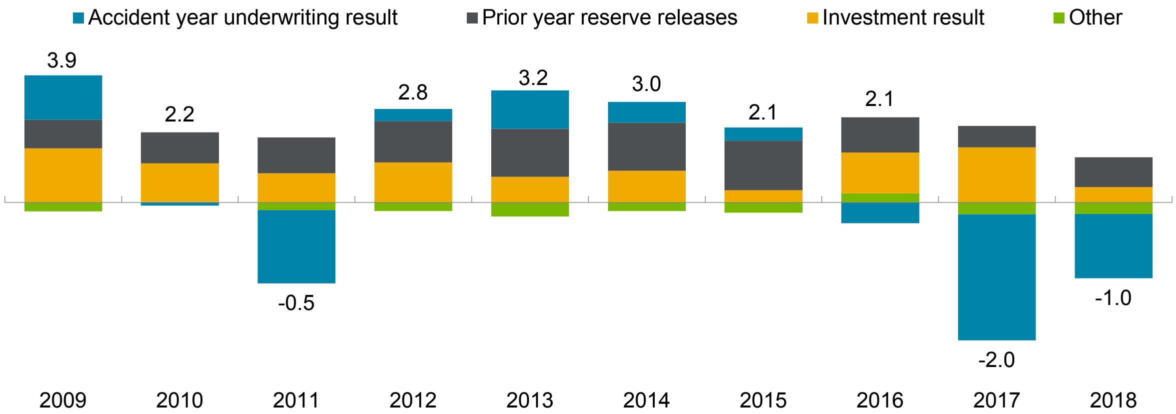
Members' capital is generally held centrally at Lloyd's. A notional return on Funds at Lloyd's (FAL) is estimated and included within Lloyd's income statement, based on the investment disposition of the relevant assets and market index returns. The 2018 return of £178m (2017: £722m), or 0.7% (3.1%), was low relative to previous years, driven by losses from equities and growth assets.

The return on Lloyd's central assets was a loss of £7m (2017: gain of £171m). Including exchange rate gains of £100m (losses of £108m) arising from currency matching assets to the US dollar component of the central solvency capital requirement, the return stood at £93m (£62m), or 2.4% (1.7%).

Pre-tax results

Other group operating expenses rose by 19% to £350m in 2018, primarily driven by costs associated with establishing the Lloyd's Brussels subsidiary and modernizing the market. Overall, Lloyd's reported a pre-tax loss of £1.0bn for 2018, after a deficit of £2.0bn in 2017.

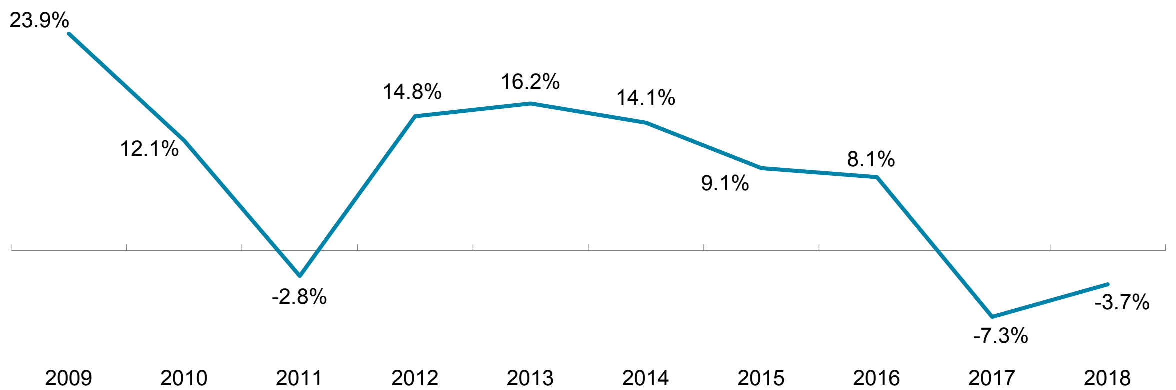
Exhibit 32: Lloyd's pre-tax results (£bn)



Source: Aon / Lloyd's.

The return achieved on total capital employed at Lloyd's over the past decade is shown below. The average is 4.1% over five years and 8.5% over 10 years.

Exhibit 33: Lloyd's return on capital



Source: Aon / Lloyd's.

Balance Sheet

Lloyd's balance sheet is assessed as 'Very Strong' by A.M. Best and risk-adjusted capitalization is at the strongest level under Best's Capital Adequacy Ratio (BCAR). Standard & Poor's expects capital adequacy to exceed the 'AA' level confidence level under its risk-based capital model over the next three years.

Exhibit 34: Lloyd's balance sheet summary

Balance sheet £m	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	1 year change
Cash and investments	46,254	48,483	51,415	51,767	51,494	54,889	56,900	67,646	67,902	71,240	4.9%
Gross technical provisions	43,544	46,428	51,918	51,517	49,277	50,786	52,556	64,295	71,270	78,318	9.9%
Reinsurers' share	9,931	10,237	12,153	12,439	10,922	10,761	10,978	14,420	20,183	23,394	15.9%
Net technical provisions	33,613	36,191	39,765	39,078	38,355	40,025	41,578	49,875	51,087	54,924	7.5%
Net resources*	19,121	19,121	19,114	20,193	21,107	23,413	25,098	28,597	27,560	28,222	2.4%

Source: Aon / Lloyd's.
Note: * Capital, reserves and subordinated loan notes and securities.

Invested assets

Lloyd's total assets grew by 9% to £118bn over the year to December 31, 2018. Financial investments rose by 8% to £60.4bn, with two-thirds of the portfolio held in US dollars. Cash fell by 10% to £10.9bn, including letters of credit and bank guarantees held in trust within members' Funds at Lloyd's totaling £8.0bn (2017: £9.5bn). The investment mix and the rating profile of the £41.7bn fixed-income portfolio are shown below.

Exhibit 35: Investment mix

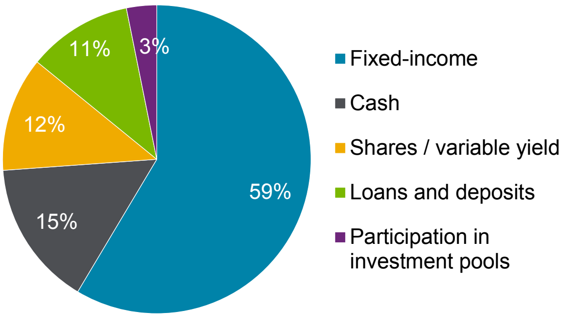
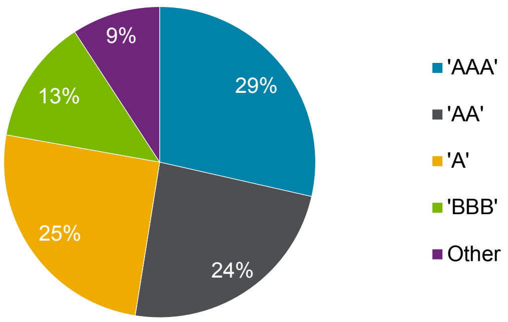


Exhibit 36: Fixed income rating profile



Source: Aon / Lloyd's.

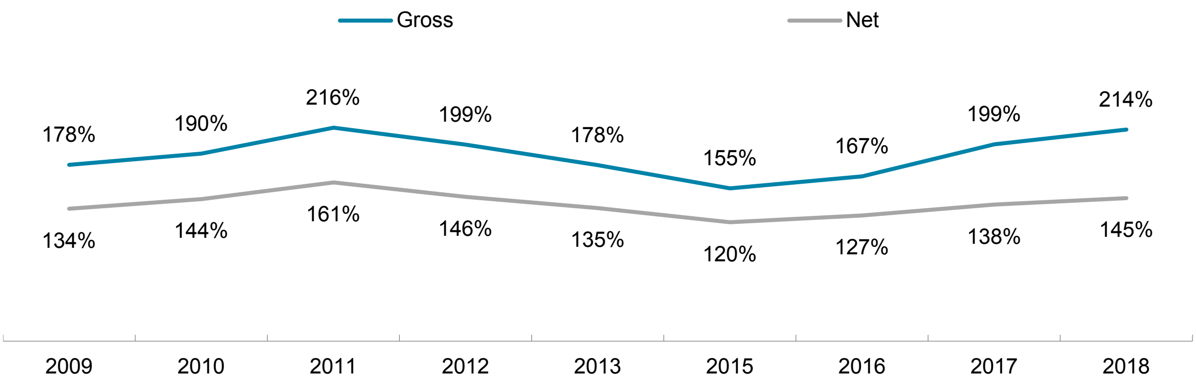
The Central Fund can take a longer-term view than the syndicates and around 40% is invested in risk assets. Third party managers are retained to manage these investments within clearly defined parameters specified by Lloyd's.

Technical reserves

Gross technical provisions rose by 10% to £78.3bn at December 31, 2018, with 64% of the total held in US dollars. Reinsurers' share of technical provisions climbed by 16% to £23.4bn, resulting in net technical provisions rising by 8% to £54.9bn.

Gross outstanding claims reserves rose by 10% to £60.5bn, of which 16% had a maturity of 3-5 years and 15% had a maturity of more than five years. Reinsurers' share of outstanding claims rose by 16% to £19.5bn, representing 78% of members' assets. Net outstanding claims rose by 7% to £40.9bn. The ratios of gross and net claims reserves to net resources over the last decade are shown in Exhibit 37.

Exhibit 37: Lloyd's claims reserve leverage



Source: Aon / Lloyd's.

All 1992 and prior non-life liabilities were legally transferred to Equitas Insurance Limited on June 30, 2009. Berkshire Hathaway is administering the run-off via Resolute Management Services Limited and provides substantial reinsurance support via National Indemnity Company (available limit $4.6bn at March 31, 2019).

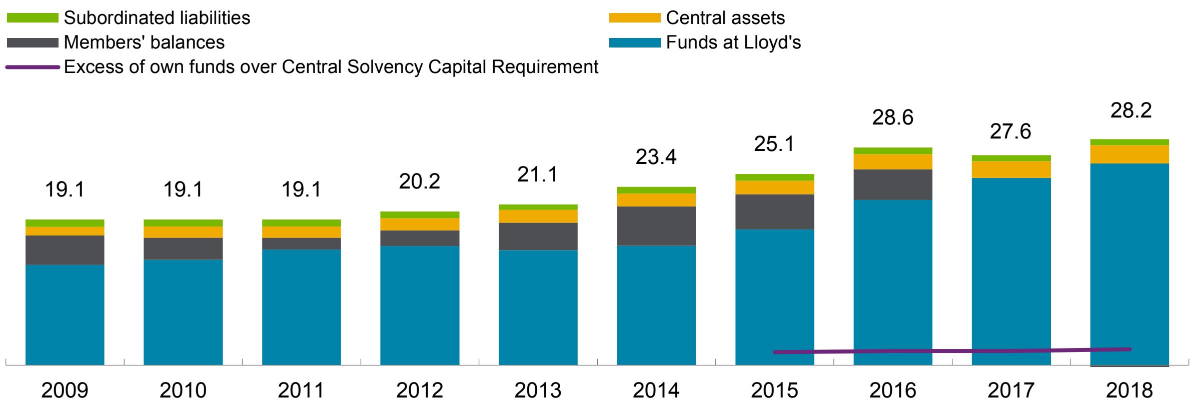
Capital

Lloyd's total net resources rose by 2% to £28.2bn over the year to December 31, 2018. Excluding £0.8bn of subordinated debt, 79% of net assets were denominated in US dollars.

Some syndicates experienced capital depletion as a result of the recent catastrophe losses. Movements in managing agency cash calls were £0.8bn in 2018 and £1.0bn in 2017. All members were able to fully recapitalize during the coming-into-line process.

The requirement to provide additional capital to continue underwriting at Lloyd's in effect provides the market with access to funds beyond those reflected in its capital structure.

Exhibit 38: Lloyd's capital base (£bn)



Source: Aon / Lloyd's.

Funds at Lloyd's (FAL) rose by 8% to £26.5bn over the year to December 31, 2018, of which £8.0bn (2017: £9.5bn), or 30% (39%) was held in the form of letters of credit and bank guarantees. This element of the capital base operates on a several liability basis.

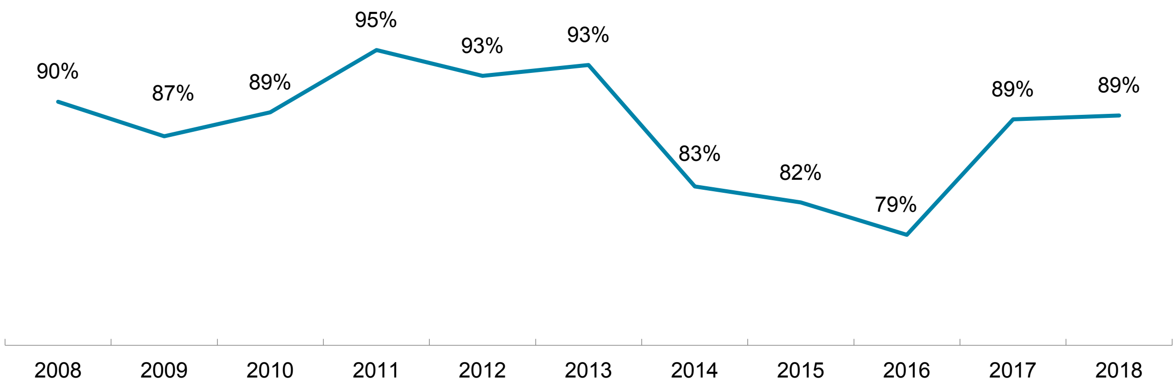
Members participating on a single syndicate are permitted to hold supporting capital within their PTFs on the syndicate balance sheet, which benefits investment returns. These 'Funds in Syndicate' (FIS) totaled £5.1bn at December 31, 2018, up from £4.1bn a year earlier.

Mutually-held central assets rose by 8% to £3.2bn at December 31, 2018. These comprised the Central Fund of £2.2bn, the Corporation's net assets of £0.2bn and subordinated debt of £0.8bn.

The Central Fund is financed by (among other things) contributions from Lloyd's members and is administered by the Council, primarily as a fund for the protection of policyholders. The fund may be supplemented by a 'callable layer' of up to 3% of members' overall premium limits in any one calendar year. These funds can be drawn from members' PTFs without the members' consent.

No payments or new commitments have been made in respect of insolvent corporate members over the last two years. There have no new losses to the Central Fund since 2008.

Exhibit 39: Premium leverage (NPE / net resources)

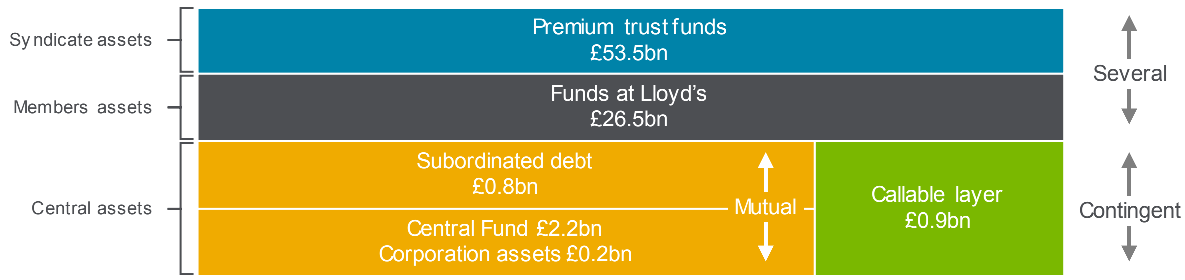


Source: Aon / Lloyd's.

The chain of security

There are three links in Lloyd's chain of security. The first is premiums held in trust at syndicate level for the benefit of policyholders. The second is members' capital, provided in support of individual underwriting participations, in line with Lloyd's requirements. The third is resources held centrally, including the mutually-supported Central Fund, backing all Lloyd's policies.

Exhibit 40: Lloyd's chain of security at December 31, 2018



Source: Aon / Lloyd's.

Once claims are agreed, Lloyd's claims service provider will notify the relevant syndicates of the funding requirements. These will be met from their PTFs through the Lloyd's central accounting system. If the PTFs are inadequate, the managing agent will make a cash call on the syndicate members, drawing-down on the members' FAL if the cash call is not met with new funds from outside Lloyd's.

If an agreed claim needs to be funded from Lloyd's central resources, an application would be made for a draw-down on the Central Fund, which would have to be approved by the Council.

Solvency monitoring at Lloyd's

Consistent with Solvency II, the FCA requires Lloyd's to calculate and monitor its SCR, representing the amount of capital required to withstand a 1-in-200-year loss event over a one-year horizon. Coverage is an ongoing and continuous requirement and testing is conducted on a quarterly basis.

This is done using the FCA-approved Lloyd's Internal Model, which has three main components: the Lloyd's Investment Risk Model, the Lloyd's Catastrophe Model (using syndicates' views of risk) and the Capital Calculation Kernel. Two SCRs are calculated, as outlined below.

- The Market-wide SCR (MWSCR) was calculated at £17.8bn on a preliminary basis at the end of 2018, up from £17.0bn a year earlier. The main elements were reserving risk (£6.7bn), attritional underwriting risk (£5.9bn) and catastrophe risk (£3.0bn).

  Eligible capital held across the market rose by £1.9bn to £26.2bn, largely due to the reduction in LOCs, split Tier 1 68% and Tier 2 32%. This represented a surplus of £8.5bn (2017: £7.4bn) and a coverage ratio of 148% (144%), well ahead of the risk appetite of 125%.

  The coverage ratio was expected to improve again in the first part of 2019, reflecting the injection of capital following losses incurred in the final quarter of 2018.

- The Central SCR (CSCR) mainly covers the risk that members may not have enough capital to meet losses (and thus hit the Central Fund), but also includes operational risk, asset risk and pension risk.

  The CSCR was calculated at £1.4bn (2017: £1.6bn). Eligible capital increased marginally to £3.5bn, of which 80% was classified as Tier 1 and 20% as Tier 2. This represented a surplus of £2.1bn (£1.8bn). Coverage improved to 249% (215%), well ahead of the risk appetite of 200%.

The Future at Lloyd's

Introduction

John Neal took office as Lloyd's CEO in October 2018 with the clear ambition of enhancing the market's relevance on the global stage. After an initial period of consultation, he spearheaded the launch of the 'Future at Lloyd's' initiative, which may result in the biggest changes seen at Lloyd's since the Reconstruction and Renewal process of the mid-1990s.

The program initiated by Lloyd's is designed to result in a bigger and more efficient marketplace. In July 2019, John Neal indicated that he saw no reason why Lloyd's share of the $750bn global commercial non-life insurance and reinsurance market shouldn't double to 10% over time.

Attracting new participants is important, but management also sees opportunities to increase existing involvement. Global carriers write 57% of Lloyd's business, but Lloyd's is said to represent less than 7% of their global business. Similarly, while the top three brokers place 41% of Lloyd's premiums, they are said to generate only 14% of their brokerage revenues from Lloyd's.

Redefining the market

On May 1, 2019, Lloyd's published a 'prospectus' which outlined a broad future vision for the market and invited stakeholders to co-develop solutions.

Customer feedback has called for better solutions for today's risks, a simpler process for accessing products and services at Lloyd's and lower costs of doing business at Lloyd's.

The prospectus recognized the need for better access, lower costs and an inclusive and innovative culture that would attract leading talent to the market.

Lloyd's offered six proposals for consideration and invited others:

- A platform for complex risk that makes doing business easier and enables efficient digital placement.
- A 'Lloyd's Risk Exchange' enabling automated, low-cost and instant purchases of insurance for less complex risks.
- A platform that provides an easy way for capital to access a diverse set of insurance risks.
- A 'Syndicate-in-a-Box' solution offering high-performing firms fast-track access to underwriting innovative business at Lloyd's.
- A next generation claims service that improves customer experience and increases trust in the market by speeding up claims payments.
- An ecosystem of services that helps all market participants develop new business and provides outstanding service to their customers.

Phase 1 of the consultation process ended on July 10. It generated 4,000 responses over a 10-week period, with around 75% of respondents said to support the overall strategy and around 65% supporting each of the six initiatives.

Lloyd's is now using this feedback to create a blueprint for the market, which will be published on September 30. The following month, work will begin on building and delivering prototypes and full services, some of which are expected to be operational early in 2020. Lloyd's has indicated that it will prioritize the complex risk platform and the claims service.

Significant internal resources are being dedicated to this initiative. London and global advisory committees comprising senior executives from across the industry have been formed to provide strategic counsel and external partners will advise on technology and implementation.

Nevertheless, execution risk remains. Redefining the market will require collaborative effort from all participants, substantial investment and the acceptance of significant cultural change.

Potential market impacts

Lloyd's plans to create a more marked divide between lead and following markets to underpin the initiative. Leaders will be rewarded for investing in differentiated underwriting, partly via fee income for services provided, while pure followers will be allowed to operate without underwriting, claims or compliance teams i.e. at much lower cost.

Among leaders, it is hoped this will foster the development of a collaborative expert underwriting community that will enhance Lloyd's reputation for providing innovative solutions to new and emerging risks. Among followers, it will remove massive duplication of effort and allow efficient third-party capital to engage in passive or 'tracker' underwriting at Lloyd's.

It is envisaged that all brokers – including retailers – will be able to access the Lloyd's Risk Exchange. This will allow a single broker to place a risk from anywhere in the world, review the options, quote the price and bind, all on a single standardized platform. The complex risk platform will support face-to-face negotiations by providing an automated back office to boost speed and efficiency.

For coverholders and MGAs, greater flexibility around capital will be relevant, the Syndicate-in-a-Box solution offers a low-cost route into Lloyd's and the Risk Exchange will streamline delegated authority business processes.

Investors that have previously found Lloyd's 'too difficult' will be encouraged by John Neal's desire to create a marketplace that can be open to different types of capital and have different return expectations and different risk time horizons.

Lloyd's believes the proposed measures have the potential to allow acquisition and administration costs for the most common risks to be cut from 30-40% today to 10-20% within five years and the time taken from request to bind and policy issuance to be cut from weeks to days.

Ultimately, Lloyd's goal is to create better connectivity between capital and risk that will deliver greater value to customers and support the overall growth of the market.

Electronic placement

Lloyd's will build on existing technology platforms established as part of the London Market Target Operating Model (TOM) modernization programme to develop the risk exchanges and claims process.

These include Placing Platform Limited (PPL), which has bound more than 250,000 firm orders since its launch in 2016 and is now used by around 140 carriers and more than 100 brokers.

Lloyd's syndicates are well on track to achieve the mandated target of accepting 70% of in-scope risks electronically by the end of 2019. For the first time, brokers will be expected to achieve a mandated target of submitting 10% of risks electronically in the final quarter of the year.

Interoperability between different technology systems remains an important issue. Further progress is required to enable the 'straight-through processing' that will allow the back-office information now being transmitted electronically to be easily shared.

Coverholder update

Lloyd's has improved its attractiveness to coverholders by introducing a single audit for all syndicates, coordinated by its delegated authority department, thereby eliminating significant duplication and cost.

Lloyd's managing agents are now participating in 'DA SATS', a central point of data collection for delegated authority business passing into the London Market from coverholders across the globe. The system aims to improve data quality and consistency, eliminate duplication, reduce rekeying and contribute to straight-through processing.

Another initiative is 'Lloyd's Bridge', an online platform aimed at cutting distribution costs by delivering direct access to the market for coverholders. It was launched in July 2018 as a pilot programme and was initially available only in the UK, Australia and New Zealand, albeit with a broader roll-out planned.

In July 2019, Lloyd’s announced plans for significant changes to its framework for third party oversight from the first quarter of 2020, supported by a new integrated online compliance system called Chorus. Lloyd’s will take a risk-based approach to approving delegated authority applications.

Going forward, third party administrators (also known as delegated claims administrators) will be approved by Lloyd's and subject to Lloyd's ongoing oversight. Sub-delegation of authority will now be allowed in certain cases.

Lloyd’s Lab

The Lloyd’s Lab has been established to drive innovation in the marketplace by connecting new products and services with capital providers. It enables new concepts and ideas to be tested in a fast-track environment, with the support and active involvement of Lloyd’s market participants.

Lloyd’s recently welcomed its third cohort of 11 new teams to the Lab, having received more than 130 applications from across the globe. They are grouped into four themes: data sharing and new sources of insight; reducing the burden of compliance and regulation; next generation claims and pricing; and risk quantification and product development.

Appendix 1: Risk Management

Introduction

The primary responsibility for risk management at Lloyd's resides with the specialist managing agents established exclusively to manage the syndicates on behalf of the members. Each is responsible for its own corporate governance. All are directly supervised by the FCA and the PRA.

Lloyd's managing agents employ the underwriters, set the risk appetite, negotiate business plans, arrange reinsurance protection and manage exposures and claims, all within the constraints of the comprehensive market oversight framework provided by the Corporation. A brief summary of the principal risk mitigation techniques utilized at Lloyd's follows.

Insurance risk

The dominant category of risk faced by Lloyd's syndicates is insurance risk (~93% of the market-wide solvency capital requirement under Solvency II). This is the risk arising from the inherent uncertainties as to the occurrence, amount and timing of insurance liabilities.

Underwriting risk

Underwriting strategy is agreed by the Board of each managing agent and set-out in the syndicate business plan submitted to the Corporation for approval each year. Approval of business plans – and setting the capital requirements needed to support these plans – is the key control the Corporation uses to manage underwriting risk.

The Corporation reviews each syndicate business plan to ensure it meets Lloyd's standards and is consistent with the capabilities of the managing agent. Once a plan is agreed, the Corporation uses performance management data to identify whether each syndicate's business performance is progressing in line with the business plan, or that variations are understood and accepted.

Reserving risk

The Corporation analyses reserve developments at line of business and syndicate levels quarterly, providing feedback to the market as necessary. Syndicates' reserves are annually subject to a formal independent actuarial opinion and are monitored by the Corporation.

Reinsurance credit risk

Managing agents are expected to have a clear and comprehensive plan for the reinsurance of each syndicate and are required to monitor and assess the security of and exposure to each reinsurer and intermediary. Reinsurance credit risk is subject to quarterly review by Lloyd's.

Catastrophe risk

Managing agents may use catastrophe modelling software to monitor aggregate exposures. The Corporation has developed a suite of Realistic Disaster Scenarios (RDSs) to measure syndicate-level and aggregate market exposure to both natural catastrophes and man-made losses.

Syndicates provide modelled output with their capital and business plans. Gross and net exposure to a single Lloyd's-specified aggregate exceedance probabilities RDS event are limited to 80% and 30% of a syndicate's capital requirement, except where specifically authorized.

Investment risk

Managing agents control asset risk through their investment strategy. Syndicate assets are held in premium trust funds and are subject to the asset rules contained in the PRA’s handbook. Asset mix is reported to the Corporation on a quarterly basis, including credit rating analysis of bond portfolios.

Asset allocation is monitored by Lloyd’s Financial Risk Committee against defined parameters, using Value-at-Risk methodology. The potential impact of changes in market value is additionally monitored through the capital-setting process.

Managing agents are required to match the duration of their syndicates’ investments with the liabilities to policyholders. The Corporation centrally monitors syndicate liquidity and conducts stress tests to monitor the impact of significant claims events. Central Fund liquidity is monitored separately.

Managing agents must ensure currency-matching. Asset / liability management is reviewed by the Corporation at both syndicate and market level. In addition, many members seek to match their capital disposition by currency against their peak exposures (the US dollar dominates).

Disclosed sensitivities to movements in exchange rates indicate that a 10% strengthening of the US dollar against the pound sterling at December 31 would have benefitted the 2018 pre-tax result by £421m and increased members’ assets by £2.6bn. This is relevant in the context of Brexit.

Having risen in 2018, interest rates are generally falling again in 2019. Disclosed sensitivities indicate that a 50 basis point reduction benefits pre-tax profit by around £340m and increases members’ assets by around £480m.

Appendix 2: Lloyd's Segmental Results

Exhibit 41: Reinsurance segment results

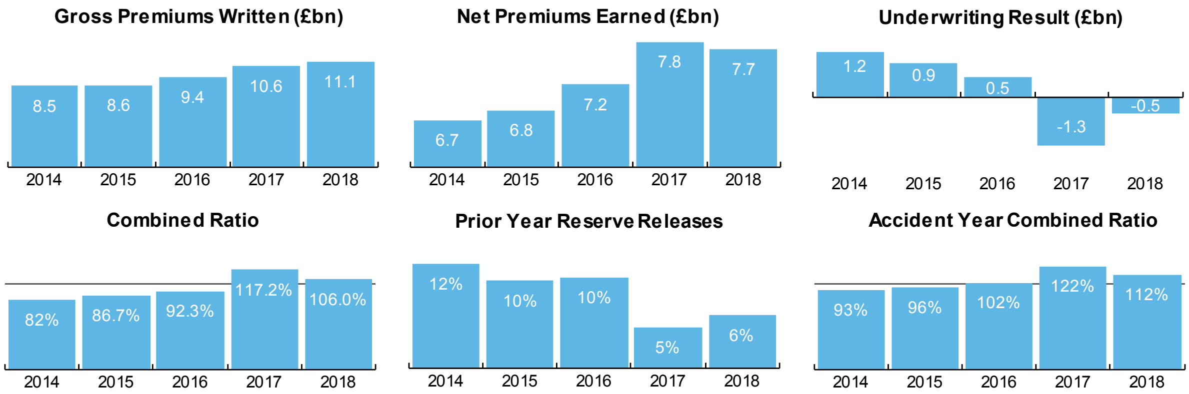


Exhibit 42: Property reinsurance segment results

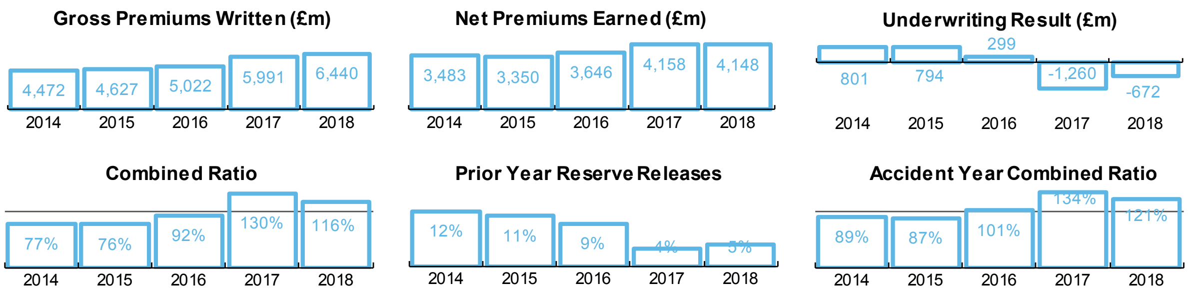


Exhibit 43: Casualty reinsurance segment results

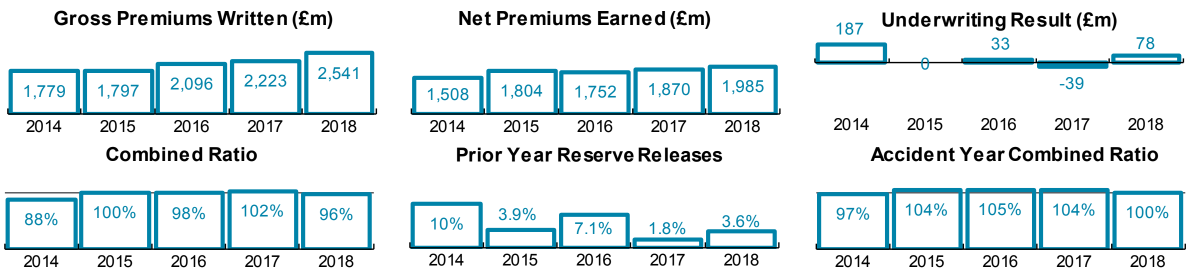
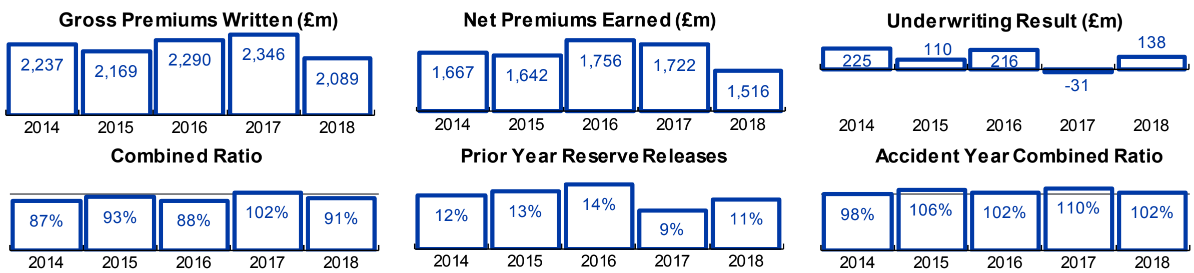


Exhibit 44: Specialty reinsurance segment results



Source: Aon / Lloyd's Statistics.

Exhibit 45: Property segment results

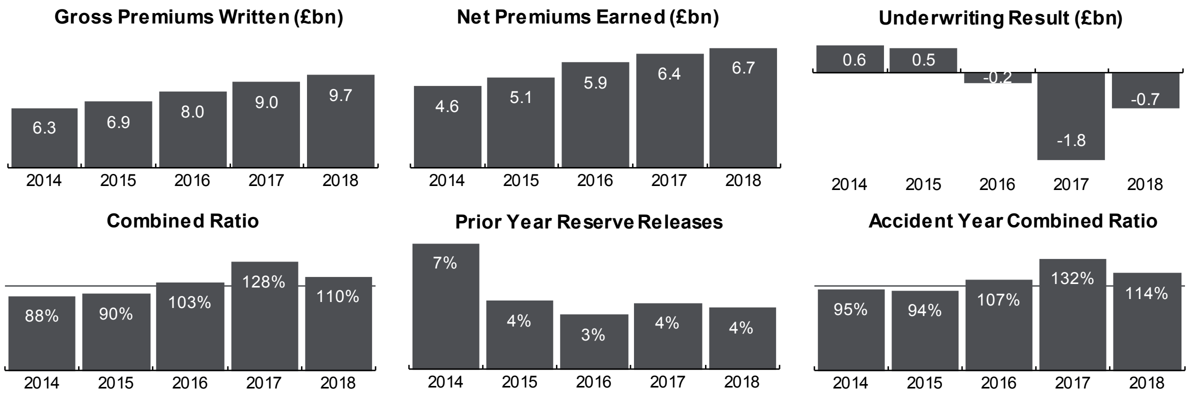


Exhibit 46: Casualty segment results

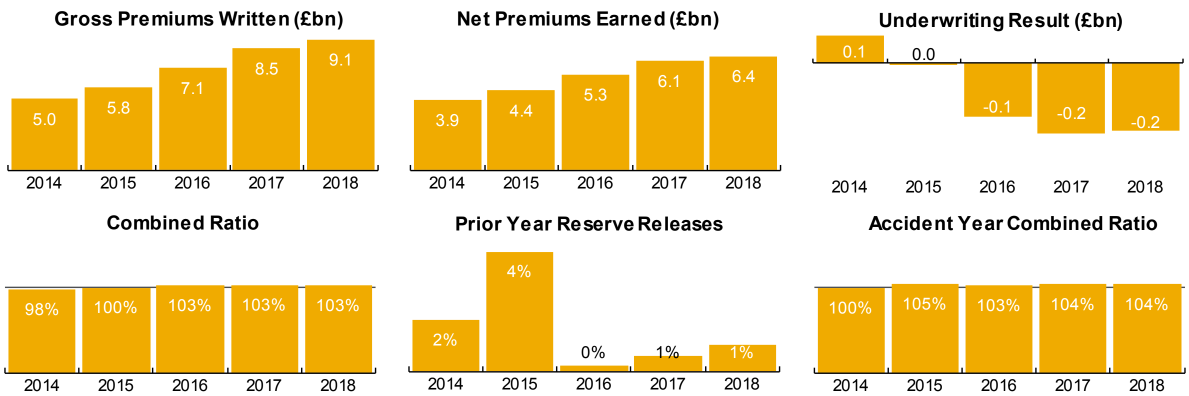
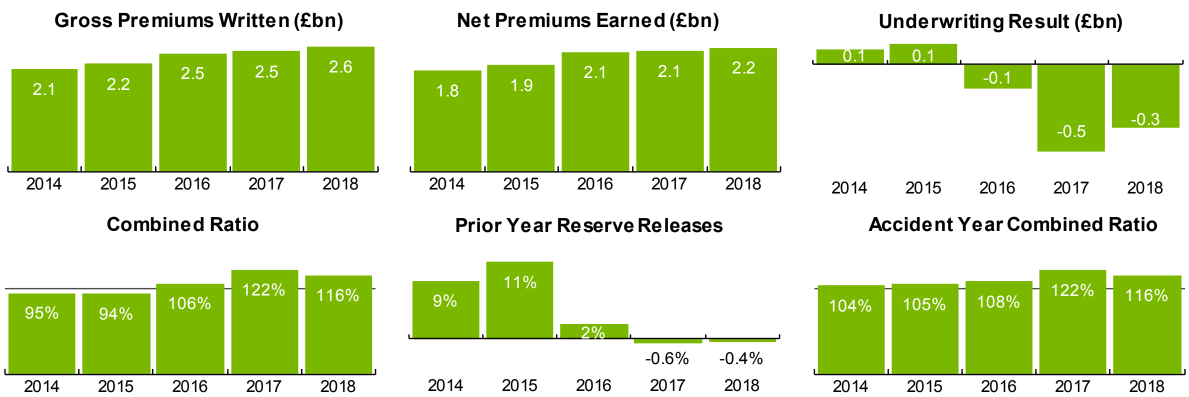


Exhibit 47: Marine segment results



Source: Aon / Lloyd's Statistics.

Exhibit 48: Energy segment results

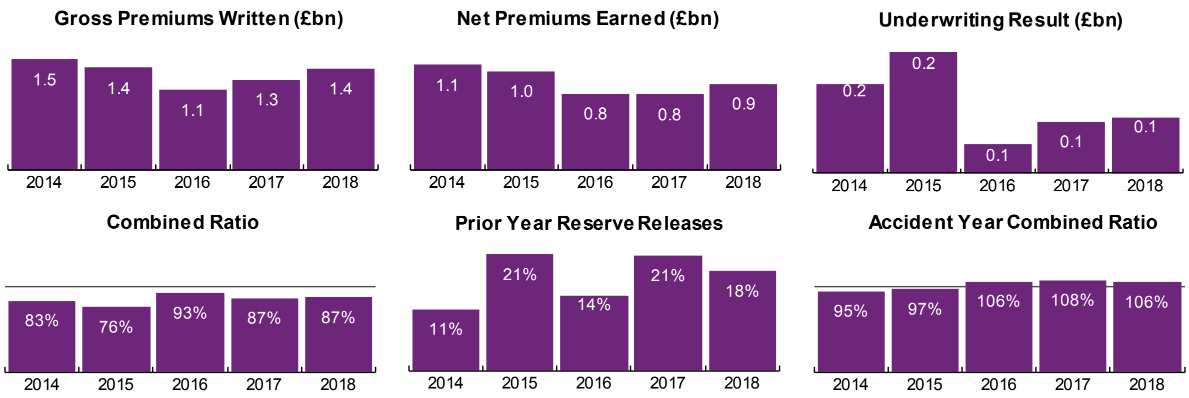
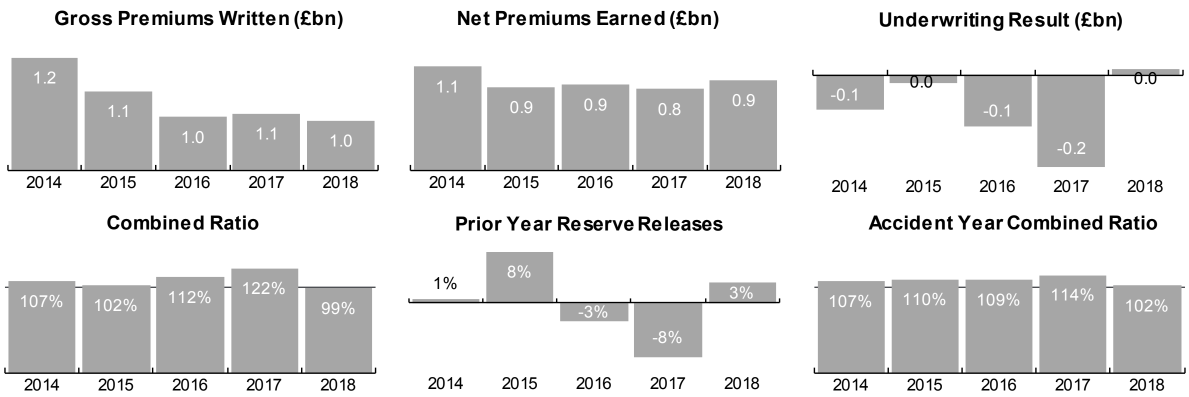


Exhibit 49: Motor segment results



Source: Aon / Lloyd's Statistics.

Appendix 3: Active Syndicate Listing

Exhibit 50: Active syndicate listing (1/2)

Syndicate number	Managing agent	Largest capital provider in 2019	2018 capacity £m	2019 capacity £m	Notes
0033	Hiscox	Hiscox (73%)	1,598	1,400	Includes sub-Syndicate 0626
0218	ERS	Aquiline (68%)	480	480	ERS sale process terminated April 2019
0318	Cincinnati Global	Cincinnati (92%)	235	234	Cincinnati Financial acquired Beaufort in February 2019
0382	Hardy	CNA	330	330	Trades as CNA Hardy
0386	QBE	QBE (70%)	317	317	
0435	Faraday	Berkshire	400	400	
0457	Munich Re	Munich Re	425	425	
0510	Tokio Marine Kiln	Tokio Marine (56%)	1,102	1,102	
0557	Tokio Marine Kiln	Private	35	35	Quota share of Syndicate 0510
0609	Atrium	Enstar (25%)	449	451	Atrium sale process terminated September 2018
0623	Beazley	Private	351	367	Operates in conjunction with Syndicate 2623
0727	S.A. Meacock	Private	80	81	
1084	Chaucer	China Re	770	789	China Re acquired Chaucer in December 2018
1176	Chaucer	China Re (57%)	47	47	China Re acquired Chaucer in December 2018
1183	Talbot	AIG	650	650	AIG acquired Validus in July 2018
1200	Argo	Argo (57%)	450	450	
1218	Newline	Odyssey Re	137	137	Ultimately backed by Fairfax
1221	Navigators	Hartford	255	244	Hartford acquired Navigators in May 2019
1225	AEGIS	AEGIS (93%)	400	407	
1274	Antares	Qatar Insurance	350	350	
1301	StarStone	Enstar	216	186	StarStone sale process terminated September 2018
1414	Ascot	CPPIB	600	600	
1458	RenRe	RenRe	443	442	
1492	Capita	Mixed	104	94	Trades as Probitas
1686	AXIS	AXIS	320	1,000	
1729	Asta	ProAssurance (61%)	132	128	Trading as Dale; ProAssurance investment under review
1856	Barbican	Credit Suisse ILS Funds	104	105	Sale of Barbican to Arch pending
1861	AmTrust	AmTrust	540	500	Expected to merge with Canopius Syndicate 4444 for 2020
1880	Tokio Marine Kiln	Tokio Marine	360	360	
1910	Argo	Argo (40%)	253	206	Trading as Ariel Re
1919	Starr	Starr	260	285	
1945	Sirius	Sirius	102	81	
1947	Pembroke	GIC Re	55	78	Hamilton acquired Pembroke in August 2019
1955	Barbican	Barbican (50%)	146	222	Sale of Barbican to Arch pending
1967	W.R. Berkley	W.R. Berkley	225	225	
1969	Apollo	Private	225	250	
1971	Apollo	Private	-	130	New for 2019
1975	Coverys	Private	34	48	
1980	Asta	Liberty Mutual	174	94	Trading as Pioneer; sale process initiated July 2019
1991	Coverys	Private	127	127	
2001	MS Amlin	MS&AD	1,850	1,665	
2003	Catlin	AXA	1,498	1,494	AXA acquired XL in September 2018
2010	Cathedral	Lancashire (58%)	306	306	
2012	Arch	Arch	200	200	Arch acquisition of Barbican pending

Exhibit 50: Active syndicate listing (2/2)

Syndicate number	Managing agent	Largest capital provider in 2019	2018 capacity £m	2019 capacity £m	Notes
2014	Pembroke	Private	150	138	Trading as Acappella; Hamilton has acquired Pembroke
2015	Channel	SCOR	225	205	
2088	Chaucer	China Re	136	132	
2121	Argenta	Hannover Re (32%)	340	340	Includes sub-Syndicate 2122
2232	Allied World	Allied World	189	162	Ultimately backed by Fairfax
2357	Asta	Nephila ILS Funds	365	391	
2468	Neon	American Financial	305	305	Neon sale process terminated June 2019
2488	Chubb	Chubb	405	405	
2525	Asta	Private	64	70	
2623	Beazley	Beazley	1,554	1,624	Operates in conjunction with Syndicate 0623
2689	Asta	Private	98	69	Trading as Verto; will partner with Syndicate 4242 for 2020
2786	Asta	Everest Re	130	110	
2791	MAP	Private	399	400	
2987	Brit	Brit	1,400	1,360	Ultimately backed by Fairfax
2988	Brit	Private	98	98	
2999	QBE	QBE	1,100	1,100	Includes sub-Syndicates 0566, 1036, 1886 and 5555
3000	Markel	Markel	500	450	
3002	Catlin	AXA	37	37	AXA acquired XL in September 2018
3010	Cathedral	Lancashire	100	100	
3268	Asta	Private	87	108	Trading as Agora
3334	Hamilton	Hamilton	121	120	Hamilton acquired Pembroke in August 2019
3623	Beazley	Beazley	213	63	
3624	Hiscox	Hiscox	400	360	
3902	Ark	Private	100	100	
4000	Pembroke	Hamilton	398	236	Hamilton acquired Pembroke in August 2019
4020	Ark	Private	300	300	
4141	HCC	Tokio Marine	175	225	
4242	Asta	Private	110	165	Trading as Beat
4444	Canopius	Canopius (77%)	1,048	1,048	Expected to absorb AmTrust Syndicate 1861 for 2020
4472	Liberty	Liberty Mutual	1,183	1,100	Includes sub-Syndicate 4473
4711	Aspen	Aspen	566	463	Apollo Funds acquired Aspen in February 2019
5000	Travelers	Travelers	300	250	
5151	Endurance	Sompo	400	400	
5623	Beazley	Private	23	63	
5678	Vibe	Soros	114	112	
5886	Asta	Private	180	215	Trading as Blenheim
6103	MAP	Private	48	48	Quota share of Syndicate 2791
6104	Hiscox	Private	56	57	Quota share of Syndicate 0033
6107	Beazley	Private	55	68	Quota share of Syndicates 0623/2623
6117	Argo	Private	96	96	Quota share of Syndicate 1910
6123	Asta	Private	20	35	Quota share of Syndicate 4242
6125	Pembroke	Patria	20	25	Quota share of Syndicate 4000
6131	Asta	ProAssurance	8	12	Quota share of Syndicate 1729
6132	Barbican	Toa Re	35	42	Quota share of Syndicate 1955
6133	Apollo	Private	35	50	Trading as Apollo Re; quota share of Syndicate 1969
6134	Argenta	Hannover Re	27	35	Quota share of Syndicate 2121

Source: Aon / Lloyd's.

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