

AM BEST

IFRS 17 and its impact on financial reporting, profitability measurement, and market comparability

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Agenda

Who, What, When, Where

New Look Liabilities

Similar but Different Performance Metrics

Spotlight on Reinsurers

Impact on AM Best's financial strength analysis for (re)insurers

Key takeaways

Who, What, When, Where

Who – International Accounting Standards Board (IASB)

What – International Financial Reporting Standard (IFRS) 17

When – Issued in May 2017, amended in June 2020 for initial implementation in January 2023; Effective dates vary by territory

Where – Most IFRS reporters across Europe, MENA, APAC, Canada – Notable exception is US

Terminology and Concepts Unique to IFRS 17

Measurement Models

- General Measurement Model (GMM)
- Variable Fee Approach (VFA)
- Premium Allocation Approach (PAA)

Balance Sheet

- Liability for Remaining Coverage (LRC)
- Liability for Incurred Claims (LIC)
- Best Estimate Liability (BEL)
- Risk Adjustment for Non-Financial Risks (RA)
- Contractual Service Margin (CSM)
- Loss Component

Income Statement

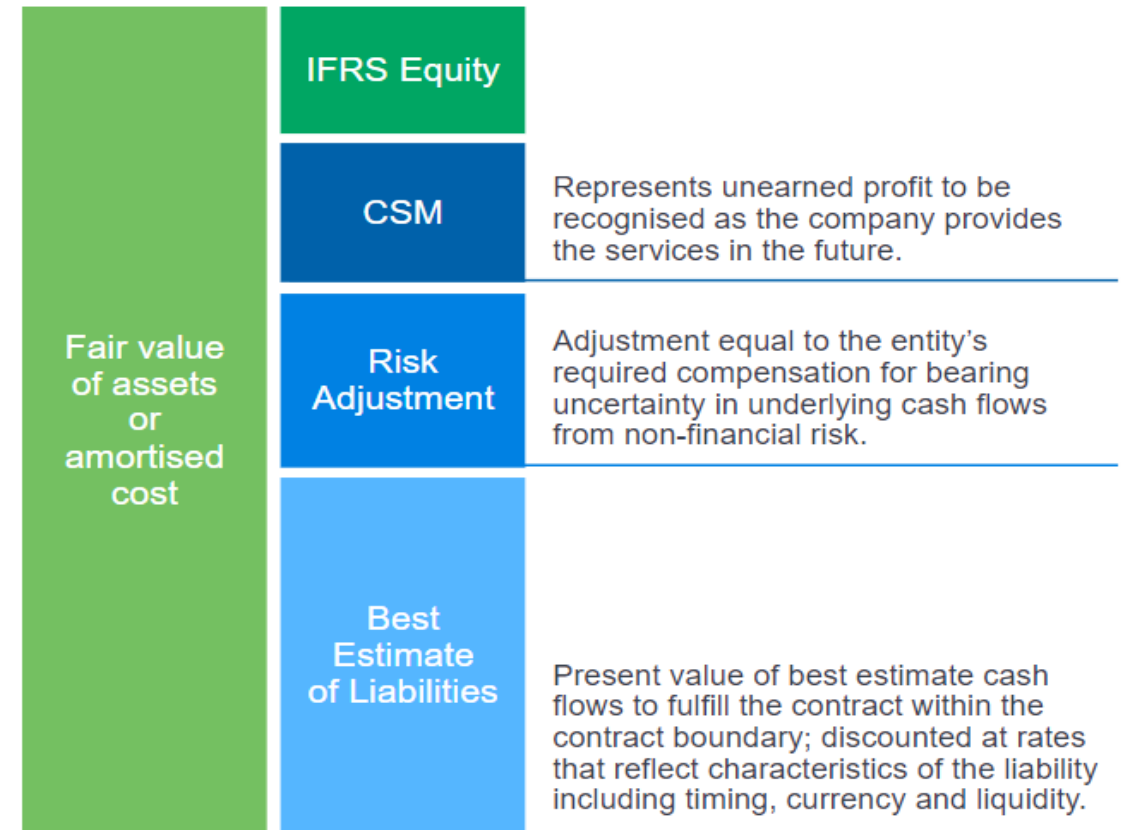
- Insurance Services Revenue (ISR)
- Changes related to past, current, future services – as part of disclosures

Concepts

- Onerous contracts

New Look Liabilities

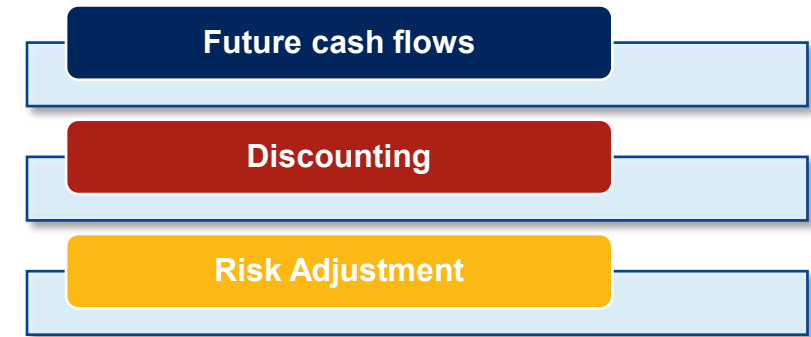
- Discounting of future cash flows for insurance contracts
- Introduction of the risk-adjustment (RA)
- A new component, the Contractual Service Margin (CSM), is the present value of unearned profits on contracts expected to be earned as insurance services are provided
- While new, this is similar to value of in-force (VIF) in embedded value reporting
- AM Best gives partial credit for life CSM as available capital – with a haircut (volatility and lack of fungibility)



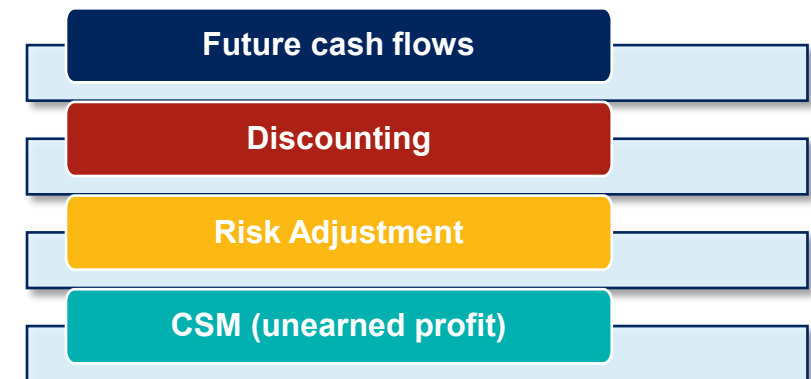
New Look Liabilities

- Liability for Incurred Claims (LIC) consists of a best estimate claims reserve + a risk adjustment (RA)
- Some companies hold reserve margins partly in their best estimate in addition to the RA
- Liability for Remaining Coverage (LRC) also includes the RA and, in addition, the CSM
- (Although this depends on measurement model – i.e. no CSM under PAA)
- Future cash flows for insurance contracts are discounted
- Discount rates used by companies vary

Liability for Incurred Claims (LIC)



Liability for Remaining Coverage (LRC)



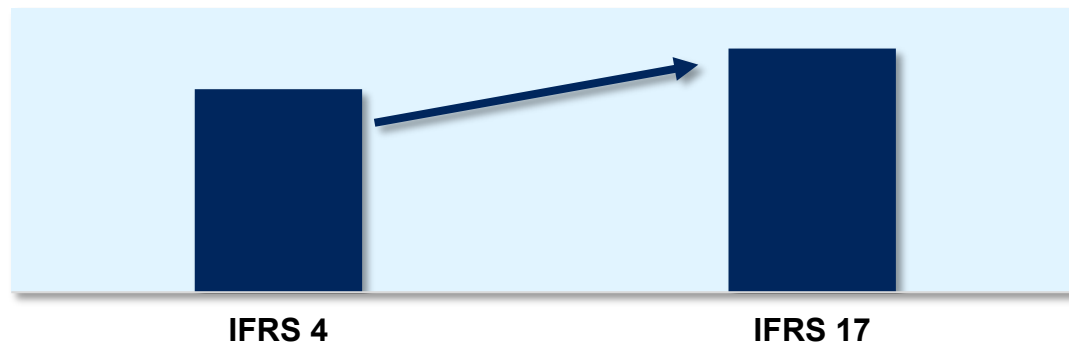
Similar but Different Performance Metrics

- Profits and revenues are recognised in the income statement as services are provided
- This moves life reporting onto a more similar basis to non-life reporting
- The alignment of profits and revenues is a big improvement for life reporting
- Overall profitability not materially affected by new standard – but timing of profit recognition can be especially for life companies
- Return on equity (ROE) metric is comparable to non-IFRS 17 reporters – and now more meaningful for life companies
- For non-life, the combined ratio is still a key metric – but comparability is challenging due to:
 - Discounting
 - Non-attributable expenses
 - Less useful split between loss and expense component of the combined ratio

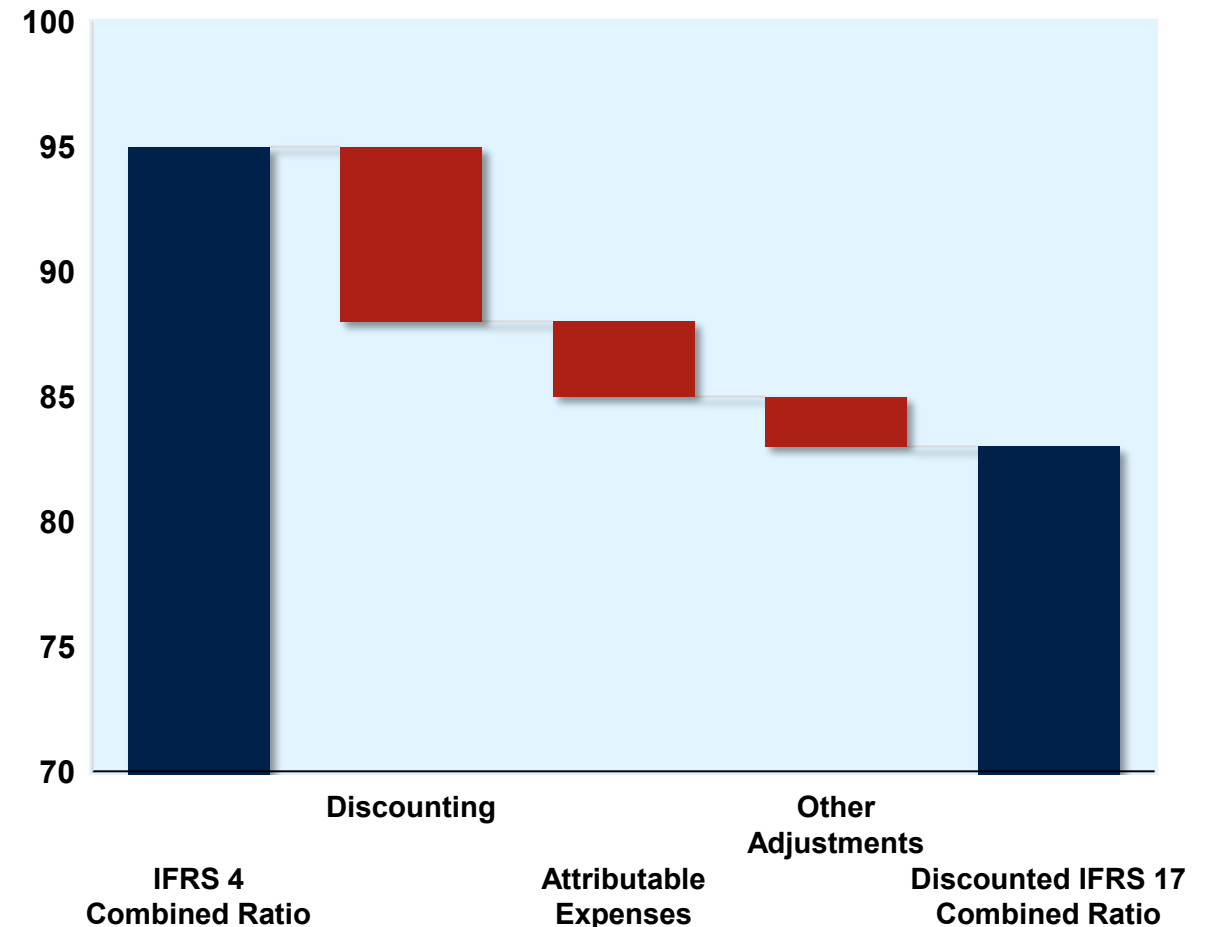
Spotlight on Reinsurers

- Reported IFRS equity has (typically) declined for reinsurers with significant life books
- Value instead recognised in the Contractual Service Margin (CSM)
- Combined ratio significantly lower due to discounting
- ROE impacted by lower equity but largely comparable

Return on Equity (Income/IFRS Equity)



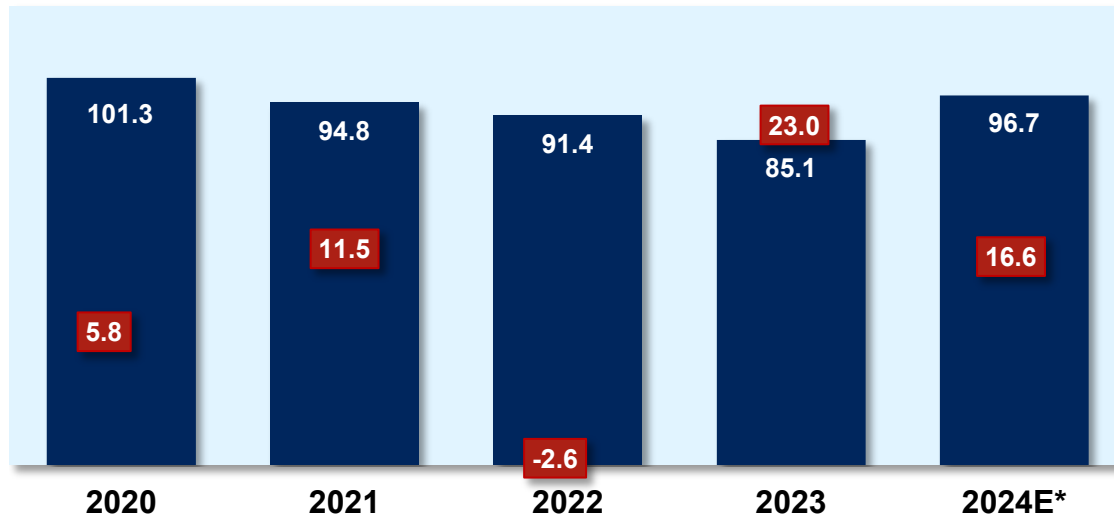
Favourable Movements in Combined Ratio



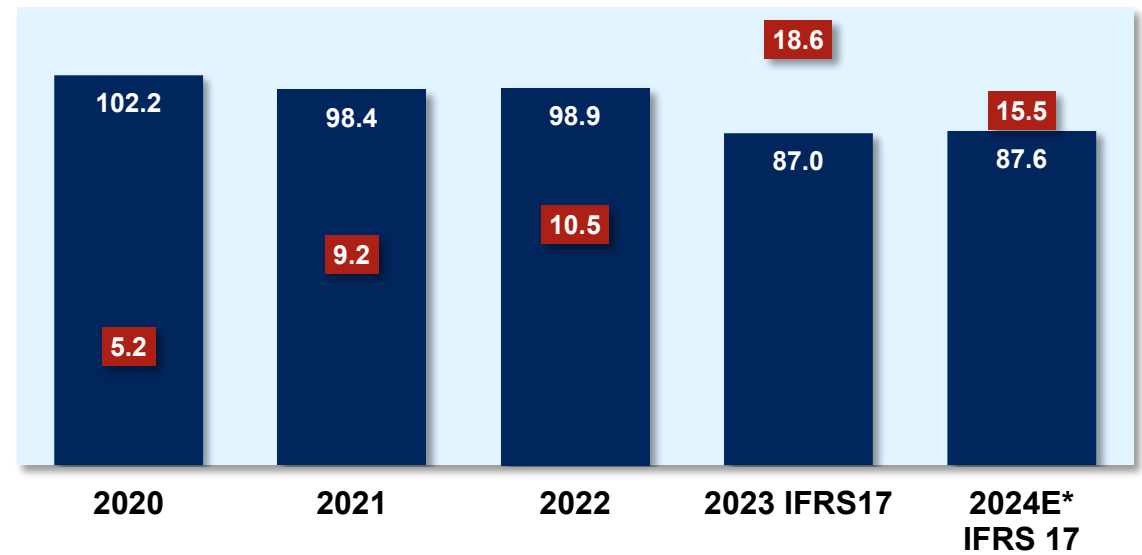
Spotlight on Reinsurers

Segment Comparison

US & Bermuda



Europe



■ Combined Ratio

— Return on Equity (ROE)

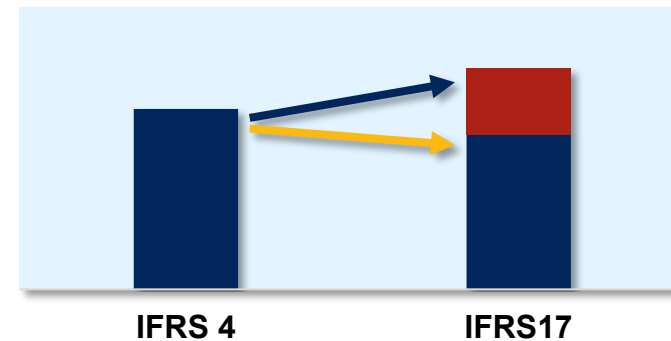
Notes:
 * 2024 AM Best Estimation.
 Europe IFRS 17 comprises Munich Re, Hannover Re and SCOR.

Spotlight on Reinsurers

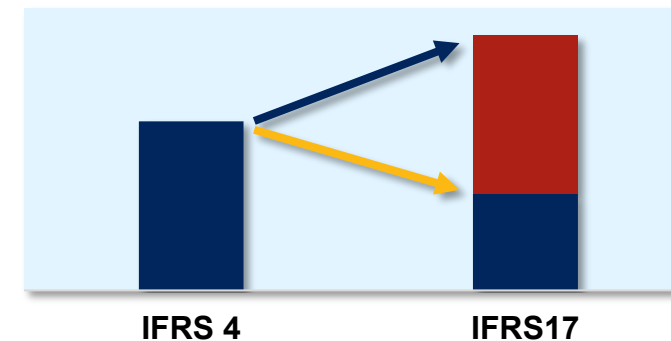
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■ Capital & Surplus ■ Contractual Service Margin
(For illustrative purposes only – Not to scale)

Reinsurer #1



Reinsurer #2



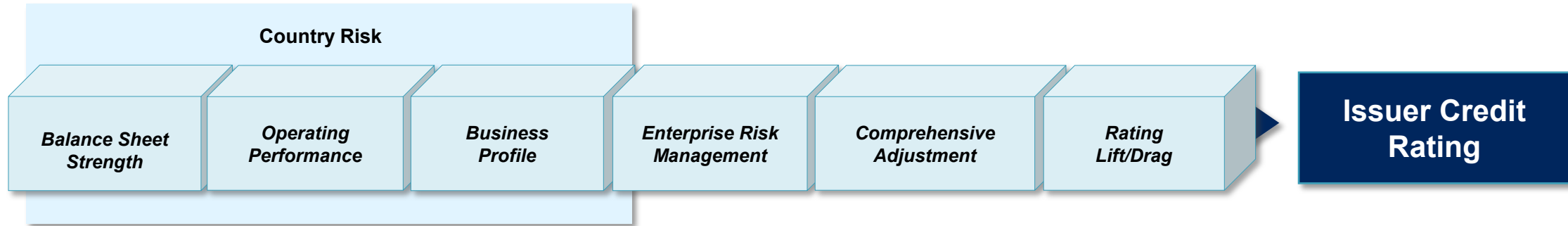
Spotlight on Reinsurers

- The differences between insurance service revenue (ISR) and written premiums (WP) make market rankings difficult
- For reinsurers, ISR is typically lower than WP

Non-IFRS 17 Rank	IFRS 17 Rank	Company	Life & Non-Life (USD m)		Total Shareholders' Funds	Combined Ratio (%)
			Reinsurance Premiums (GPW)	Reinsurance Revenue (Gross)		
1		Swiss Re	40,503		16,371	94.1
	1	Munich Reinsurance		32,921	32,863	85.2
2		Berkshire Hathaway	27,453		567,509	84.0
	2	Hannover Rück		26,995	12,164	94.0
3		Lloyd's	22,075		56,869	80.2
	3	SCOR		17,575	5,213	85.0
4		Reinsurance Group of America	14,281		9,171	N/A
5		RenaissanceRe Holdings	12,340		9,455	78.0
6		Everest Re Group	11,460		13,202	86.4
7		Arch Capital Group	9,113		18,353	81.5
8		PartnerRe	9,102		8,424	81.7
	4	China Reinsurance (Group)		5,986	14,453	93.5
9		MS&AD Insurance Group Holdings	5,777		13,814	98.7
10		General Insurance Corp of India	4,544		10,283	111.7

IFRS 17 – Impact on Financial Strength Analysis

Building Block Approach



- AM Best uses a building block approach to assess a (re)insurer's financial strength
- Audited financial statements are a key input to the rating process
- AM Best already rates (re)insurers who report under a variety of standards
- Changes in reporting do not mean changes in financial strength and the rating process should be agnostic to accounting standards
- However, new presentation of the underlying information can lead to new insights and new challenges in financial strength analysis

Key Takeaways

- Ratings are agnostic to accounting standards
- Enhanced KPIs under IFRS 17, more particularly in life segment
- Potential for improved comparability of KPIs within IFRS 17 universe
- Comparison across accounting standards will continue to require interpretation
- AM Best expects implementation to evolve over the next few years

Q&A