



Specimen coursework assignment

960 – Advanced underwriting

The following is a specimen coursework assignment question and answer. It provides a guide as to the style and format of coursework questions that will be asked and indicates the depth and breadth of answers sought by markers. The answer given is not intended to be the definitive answer; well reasoned alternative views will also gain good marks.

Before commencing work on an actual coursework assignment, you need to fully familiarise yourself with the following documents:

- *Coursework assessment guidelines and instructions*
- *How to approach coursework assignments*
- *Explaining your results notification.*

Coursework assignments involve the application of knowledge to work-related questions. They require you to explore issues in the workplace relevant to the unit for which you have enrolled.

Coursework submission rules and important notes

Before commencing on, or submitting, your coursework assignment it is essential that you fully familiarise yourself with the content of *Coursework assessment guidelines and instructions*. This includes the following information:

- The maximum word limit for coursework assignments is 3,200 words.
- Arial font and size 11 to be used in your answers.
- Important rules relating to referencing all sources including the study text, regulations and citing statute and case law.
- Penalties for contravention of the rules relating to plagiarism and collaboration.
- Deadline for submission of coursework answers.
- There are 80 marks available per assignment. You must obtain a minimum of 40 marks (50%) per assignment to achieve a pass.
- The coursework marking criteria applied by markers to submitted answers.
- Do not include your name or CII PIN anywhere in your answers.

Top tips for answering coursework assignments

- Read the assignments carefully and ensure you answer all parts of the assignments.
- Ensure that each answer includes a relevant context, regardless of the country or countries to which it refers.
- You must include a context in each answer. You may use the same context for each of the three answers.
- For assignments relating to regulation and law, knowledge of the UK regulatory framework is appropriate. However, marks can be awarded for non-UK examples if they are more relevant to your context.
- There is no minimum word requirement, but an answer with fewer than 2,800 words may be insufficiently comprehensive.

Assignment

Provide a brief context for an insurer or a reinsurer, or a division of either, with which you are familiar. For **this** insurer or reinsurer, or division of either:

- Explain briefly the product range
- Analyse the underwriting benefits and challenges of extending the product range
- Make recommendations, based on your analysis, which would successfully deliver an extension in the product range.

Note:

You are recommended to discuss your own organisation, or one that is familiar to you. Your answer is confidential to the CII and will not be shared. For this exemplar answer, which is widely publicised, a fictitious company has been chosen so as not to highlight any particular company.

To be completed before submission:

Word count:	3,165
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Start typing your answer here:

Context

This answer is based on my employer, GHY plc (GHY), which is the parent company of a number of insurers with operations in various countries in Europe. GHY plc is listed on the London Stock Exchange and has a 'AA' credit rating from the leading credit rating agencies.

This assignment will focus on GHY plc's UK-based insurer which currently underwrites a range of mass market personal lines general insurance products, together with a small commercial property account focussed on landlords.

The personal lines products consist of private motor and household insurances underwritten through different brands, with each brand dedicated to a specific distribution sector. Brand A is dedicated to direct customers, whilst brands B and C focus, respectively, on insurance brokers and aggregators.

There is extensive competition in GHY's markets, with the Association of British Insurers reporting that "*The motor insurance industry last made an underwriting profit in 1994*" and "*Between Q3 2012 and Q2 2015 property insurance premiums have fallen by 9%*" (Association of British Insurers, Key Facts 2015).

This indicates the extent of competition which, even allowing for GHY's drive for effectiveness and operational efficiency, justifies extending its product range, particularly in product areas where competitive pressures may be less pronounced, so as to bring disproportionate impact to GHY's bottom line.

GHY's private motor market share is over 15%, and has broadly remained consistent in the last five years, whilst its property portfolio is 8%, with limited growth anticipated in the next few years.

Whilst GHY does not actively seek customers who have risks which it does not insure, it does receive enquiries from existing and new customers regarding such risks, e.g. motorcycle insurance. It passes such enquiries to an independent insurance broker who seeks to fulfil the customers' needs. This action both supports GHY's brands values and provides an income from the payment, by the broker, of referral and renewal fees. This business gives GHY some understanding of where it might be able to develop products, to underwrite itself.

GHY's corporate strategy is based on market-leadership:

- Our objective is to be deliver sustainable and growing cash flows supported by potential for growth
- A focus on four key metrics – cash flow, operating profit, expenses, and combined operating ratio.

This corporate strategy is not dissimilar to other major players in the UK market with, by way of example, RSA plc stating *"The history, dynamics and structure of our markets show that focused regional market leaders can successfully sustain both customer appeal (market position) and excellent shareholder performance"* (RSA, Annual Report and Accounts 2015).

Underwriting Benefits and Challenges

GHY has a project team, drawn from its various functions, which considers the opportunities and challenges from extending the product range. Such a team was responsible for the successful landlords' insurance product.

Dr Laura Cochran has identified that the underwriting perspective of a business proposition, such as would exist from extending the product portfolio, will include a number of aspects comprising:

- Products
- Target customers
- Competition
- Environment and timing
- Delivery and service

- Projections
 - People
 - Regulation
- (Cochran, 2014)

This answer will address each of these aspects.

Products

GHY, given its current size, has no appetite to develop products suitable for relatively minor sectors of the market. Even if successful with one or more such products they would likely have limited effect on GHY's results and might well deflect management resource away from its main revenue and profit-generating activities.

Additionally, GHY's Board does not wish to add to its brand portfolio, so any new products have to respect and reinforce existing brand values; in whichever of the above identified distribution channels are used.

The most obvious benefit of a new product, or an appreciable development of an existing product, is that it, as it grows, reduces the percentage contribution of the existing products. This widening of the product portfolio should reduce the likelihood that a revenue or profit shortfall in a single product will not prove too large a blow for the entire organisation's financial performance.

Design of products, whilst based on customers' needs, will also need to reflect some element of product differentiation so as to 'stand out from the crowd'. In addition, it has been articulated by Simon Ross that, to consumers, the quality and/or service aspects of a product are more important than its price (Ross, 2015).

Target Customers

GHY has several million customers so there is a natural opportunity to cross-sell appropriate additional products to them. To date, GHY has enjoyed considerable success in selling household insurance to its motor direct customers. Increasingly, GHY sees that it can optimise its marketing spend, to grow its revenue, by focussing on cross-selling as its main generator of sales. Such cross-selling opportunities justifies widening the product offering. The acquisition of new customers will remain an important source of revenue growth.

Cross-selling is described on the Marketing Donut website as:

"Many customers only know about the products they have bought from you. Simply telling your customers about all the products in your range can bring in more business" (Marketing Donut, 2016).

Deciding which products are suitable for which customers will require consideration of customers' needs and wants. When those wants and needs are identified, there will then be a process of identifying the extent to which they can be satisfied by insurance and whether such a product can be offered at a price which will attract and retain sufficient customers to justify its development.

Some potential products will fall away from consideration as the risk: reward balance for GHY will be inadequate. For example, GHY had previously identified a need for a domestic property value insurance, which would provide indemnity to the insured against a decline in the value of their property. However, property prices tend, in general, to move-up or down, in a similar pattern across the UK meaning that the risk exposure could result in numerous, high-cost, claims occurring in a relatively short=period of time. This risk exposure is outside of GHY's risk appetite, even with measures such as large deductibles and setting insured values below current market values. GHY's Board cancelled the project to develop this product.

Competition

History suggests, as far as insurance is concerned, that should a successful product be developed by one insurer it will rapidly be copied by other insurers. There is little differentiation, in the eyes of the customers, between the respective product offerings of most mass market insurers. This is not to say that specific areas, such as high net worth, e.g. Hiscox High Value Home Insurance, don't have significantly different products from the mainstream however these are relatively small markets, so outside of GHY's intended market.

However, keeping track of competitors and their product developments is a key requirement for GHY's marketing department. This intelligence allows GHY to consider early response to competitive threats and to identify potential competitive advantages.

GHY sees itself as a customer-centric marketing-led insurer. This does not detract from the importance of other stakeholders, however does reflect a strategy which places the customer at the heart of product development considerations.

This customer-centric approach is captured in the following quote from Malcolm McDonald and Hugh Wilson:

"The central idea of marketing is of a matching between a company's capabilities and the wants of customers in order to achieve the objectives of both parties" (McDonald & Wilson, 2011).

Environment and timing

The insurance cycle (Cochrane, 2014, page 3/9), with its changes in profitability from year-to-year, suggests that there can be advantages arising from the timing of the launch of new or improved products. When the market is 'hard', insurers may be more amenable to making product changes, supported as they are by relatively high profitability in their existing products. Correspondingly, a launch when the market is 'soft' might inhibit early response from competitors who are otherwise engaged in defending market share for their existing products and preserving, at least, an element of profitability in them.

Customer demand will also be a key factor. Currently the Bank of England latest inflation report (Bank of England, Inflation Report August 2016) indicates that consumer price inflation will increase in the near term, exceeding the Bank's target of 2% annual inflation, accompanied with little growth in gross domestic product and an eventual rise in unemployment. Other commentators have observed that inflation, coupled with a slower growth in wage levels, will have an effect on consumer living standards (BBC, 2016). This could indicate that widening a product portfolio, when customers may be feeling less confident and potentially less willing to purchase, may not be ideal timing.

Delivery and Service

The differences between mass market products in general insurance are generally driven by the customers' perceptions. These perceptions are created by marketing, service and personal experiences. Given the importance that most insurers state they have for customer service, e.g. Axa's commitment to "We're here for our customers when they need us", (Axa, 2016) it is surprising that the insurance industry produces so much work, in complaint handling, for the Financial Ombudsman Service (Financial Ombudsman Service, complaints data, 2016).

This level of inadequate customer service appears to be generated by a mismatch between what the consumer felt the product was for and what it actually delivered. This suggests that should GHY successfully overcome that mismatch in the design, delivery and service of its products it could gain competitive advantage. Some commentators have seen the reputational risk negativity:

"The perception (whether valid or not) that an organisation's products or services are of poor quality or over-priced can destroy customer confidence and the organisation's sales and profitability" (Atkins, Bates & Drennan, 2006).

However, the reverse, where the product strengthens customer confidence and creates sales and profitability, seems to be a worthwhile goal for GHY to pursue. It is articulated by Linda Goldzimer who stated: "...make your customer feel good about doing business with you" (Goldzimer, 1989).

Indeed, the theme of operational risk, which underpins reputational risk, creates an upside potential as it draws various risk components together. This was stated by Tony Blundell and John Thirlwell:

“... operational risk is effectively business risk, including strategic and reputational, risks, it should be an integral part of business strategy and management, the board’s primary responsibility” (Blundell & Thirlwell, 2010).

One particular challenge for GHY, and other insurers, is the changing expectations of consumers. For example, CapGemini, in its World Insurance Report 2016, have identified:

“Our findings show that Gen Y high expectations and strong preferences for digital and social media channels leads to gaps in service and, in turn, less positive outcomes” (CapGemini, 2016).

Unless GHY responds positive to the challenges created by Generation Y, and other generations, then it will likely harm its reputation. This diminishing of reputation would lead to an adverse effect on revenue, particularly if competitors were seen to be more responsive to the changing needs of consumers.

Projections

Having a clear sense of what the product is intended to deliver, including in terms of rates of sales and retention, average and total annual premiums, profitability, together with the associated costs, is fundamental to the decision whether or not to proceed towards a launch. Ideally a financial plan will be one of the earliest features considered, in the life of the project. The financial plan will allow for a decision to abort the project, before any unnecessary expenditure is incurred, to take place as early as possible. Clearly the financial plan will evolve as the project develops, as more information becomes available. The project will be subject to a number of intermediate steps, where senior management can cancel, amend or agree the continuation of the project, and a likely key issue in their determination will be the emerging financial landscape.

Projections will not be based not on a single set of figures but rather a number of potential scenarios. These scenarios might include differing sales volumes and patterns, alternative claim number and cost profiles, various cost assumptions, including reinsurance, which all leads to a ‘best’, ‘worst’ and ‘average’ range of scenarios. Within this the effect on other products, and in turn those products effect on the project delivery, will be factored into the considerations. For example, selling a breakdown and accident recovery service to existing motor insurance customers could create a ‘double hit’ on claims costs, if the vehicle accident frequency increases.

This interplay of factors, and their relative importance, is a complex area demanding skills that may be at a premium. The overarching importance of getting it right, and the by definition the potential consequences of getting it wrong, has been described by Carol Alexander as:

“Accurate forecasting of volatility and correlation is the key to successful risk management and analysis” (Alexander, 1998, page 233).

A particular challenge in creating the financials will be in arriving at credible and robust data on which to base pricing. In extending an existing product, the change may be relatively modest although still capable, if calculated incorrectly, of wiping out the product’s existing profitability. For new products, there may be a far deeper lack of data, which introduces increased caution into the pricing decisions. In part, the decisions taken and the extent to which pricing is set at a level to attract customers will be driven by GHY’s risk appetite. This may mean that, to overcome the challenge expressed by Sung Hun Seog:

“Incomplete information is one of the main characteristics of the insurance market” (Hun Seog, 2010) that GHY might undertake a ‘soft’ launch, targeted at relatively few customers, to build-up experience with the product and its financial projections, before engaging in a more extensive launch.

A ‘soft’ launch has the additional advantages, from a risk appetite perspective, that the customer service implications and the associated workload volumes can ramp-up gradually over time. However, this approach may lengthen the period before ‘break-even’ is achieved.

The sources of potential data have widened significantly in recent years with the emergence of ‘Big Data’. An example of ‘Big Data’ and its potential uses, including its integration with existing traditional data sources is available from Oracle (*Oracle, 2016*). Of particular relevance to underwriting is the extent to which data, accessed from a variety of sources, can be integrated in such a way as to assist and support risk pricing decisions. The inter-relation of sets of data, and the extent of the strength and correlation of such data, may increasingly have a profound effect of the success of GHY. To gain from ‘Big Data’, so as not be placed at competitive disadvantage, will increasingly become a subject for GHY’s Board to address.

People

There is an expectation, as identified above, that GHY either has, or can obtain, people with the relevant skills and experience to deliver a successful project. It would be unwise to automatically assume that existing staff are sufficiently capable, so consideration will need to be given to training and development. Additionally, the project team may need reinforcing through the hiring of such individuals, either permanently or short term. Short term recruitment, and the transfer of skills, could be used as part of the development of existing employees.

This is an area where specialist advice and input may be needed from an external management consulting company, such as McKinsey's.

In addition to the project team, a number of permanent tasks will be created across a number of different departments, such as underwriting, actuarial, pricing and customer service. All of these tasks will need staff to develop new skills and capabilities for the enlarged portfolio. All of these developments will be included in the project plan and its financial implications.

Throughout the above teams, an important requirement will be for, as stated by Simon Ross, a need for high-performance management teams (Ross, 2015). These teams are needed to ensure the project runs to time, cost and quality, and that the subsequent delivery to customers is consistent with GHY's brand value/s.

Regulation

The Financial Conduct Authority (FCA), through its handbook (FCA, handbook, 2016) and other documentation, sets out its requirements and expectation which GHY has to abide by. For example, GHY is only authorised to underwrite certain classes of insurance. If GHY intends moving into underwriting in another class, it would need to obtain the prior approval of the FCA. This approval process would involve the presentation of a report to the FCA setting out the financial, capital, product specification and other aspects.

Additionally, whilst GHY is committed to customer service, it will need to be able to demonstrate that it has taken into account, in its project plan, a range of different FSA issues including Treating Customers Fairly and potential conflicts of interest.

The development of an extension to a product portfolio is, as described above, a complex task which requires the integration of numerous aspects. The following recommendations are intended to assist that integration process and the delivery of a successful project.

Recommendations

1. The project needs to have a Board-level sponsor who will demonstrate the Board's commitment to both the project team and the other staff employed by GHY.
2. The project must be anchored in the strategy objectives of GHY and clearly show how it will contribute to the strategic requirements.
3. The project team must be led by an experienced project manager who has the authority, credibility and capability to engage with all those functions who will contribute to, and be effected by, the project.
4. The project team should have its own administrative support capability.

5. Members of staff, with specific skills required by the project, should be willingly seconded to the project by their line managers. Project work should be seen as essential to GHY.
6. Regular meetings between the project manager and the sponsoring director should take place to ensure that the project remains on course and, in particular, is amended or cancelled, as early as possible, if emerging information justifies such a decision.
7. Communication between the project manager and functional managers will allow for a two-way flowing of information, updates and ideas.
8. Data for product design and pricing purposes will need to be extensively researched, tested and analysed to reduce the risks inherent in a product launch.
9. The marketing function should seek out competitors' intentions and engage with potential customers to test propositions.
10. There should be a feedback mechanism both during the project phase and afterwards, to ensuring that emerging information and experience is used to develop the product.
11. Recommendations which would successfully deliver an extension in the product range.
12. . reinsurance and underwriting strategies

Conclusion

GYH has a clear sense of strategic direction which, to support revenue and profitability growth, will require the portfolio of products to be extending from time to time. This work on the product range will proceed cautiously and carefully so that the opportunities are optimised and the downside risks fully evaluated and taken into account. Risk is not avoidable; indeed, it is seen as 'part and parcel' of a growing portfolio. However, risk will be managed so that it does not produce an unacceptable level of adverse potential for future success.

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Glossary of key words

Analyse

Find the relevant facts and examine these in depth. Examine the relationship between various facts and make conclusions or recommendations.

Describe

Give an account in words of (someone or something) including all relevant, characteristics, qualities or events.

Discuss

To consider something in detail; examining the different ideas and opinions about something, for example to weigh up alternative views.

Explain

To make something clear and easy to understand with reasoning and/or justification.

Identify

Recognise and name.

Justify

Support an argument or conclusion. Prove or show grounds for a decision.

Recommend with reasons

Provide reasons in favour.

State

Express main points in brief, clear form.