



# Insurance Industry



## Course Overview



Explore what insurance companies do and their key products



Learn how insurers make money and what pooling risk is



Review an insurer's income statement and balance sheet



Explore main types of insurance – P&C and life insurance



Identify key life insurance products and reinsurance types

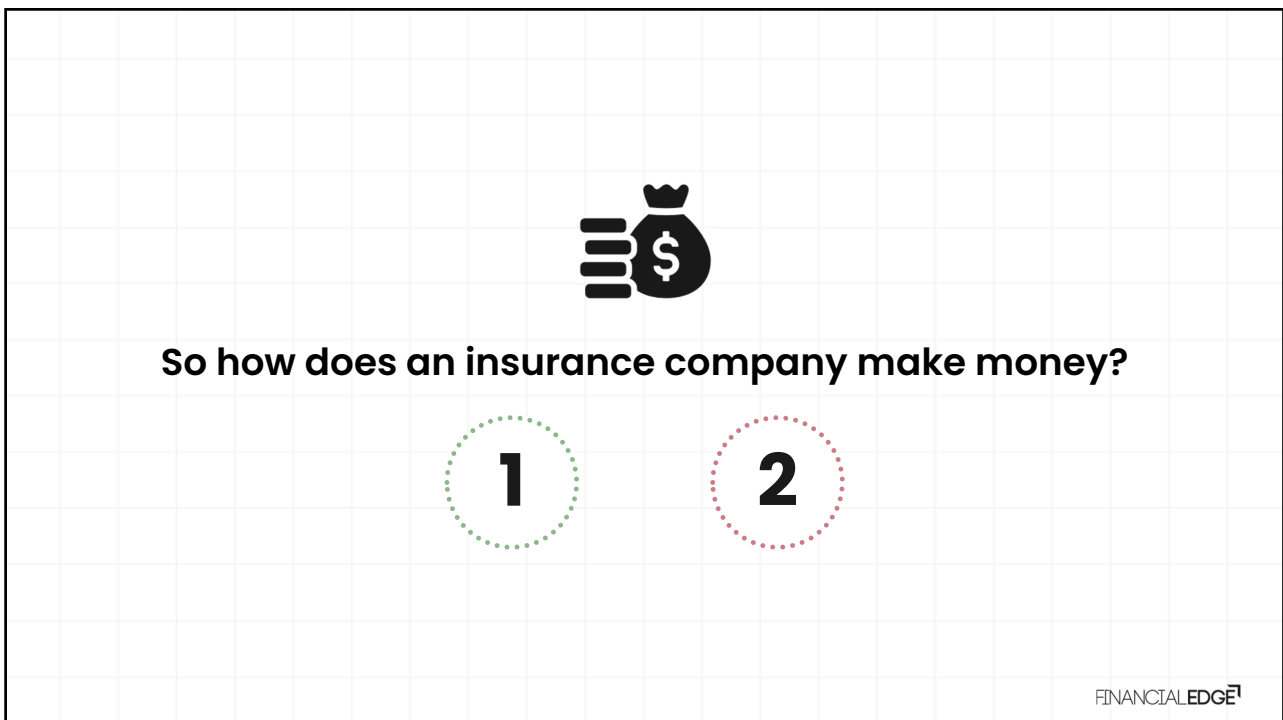
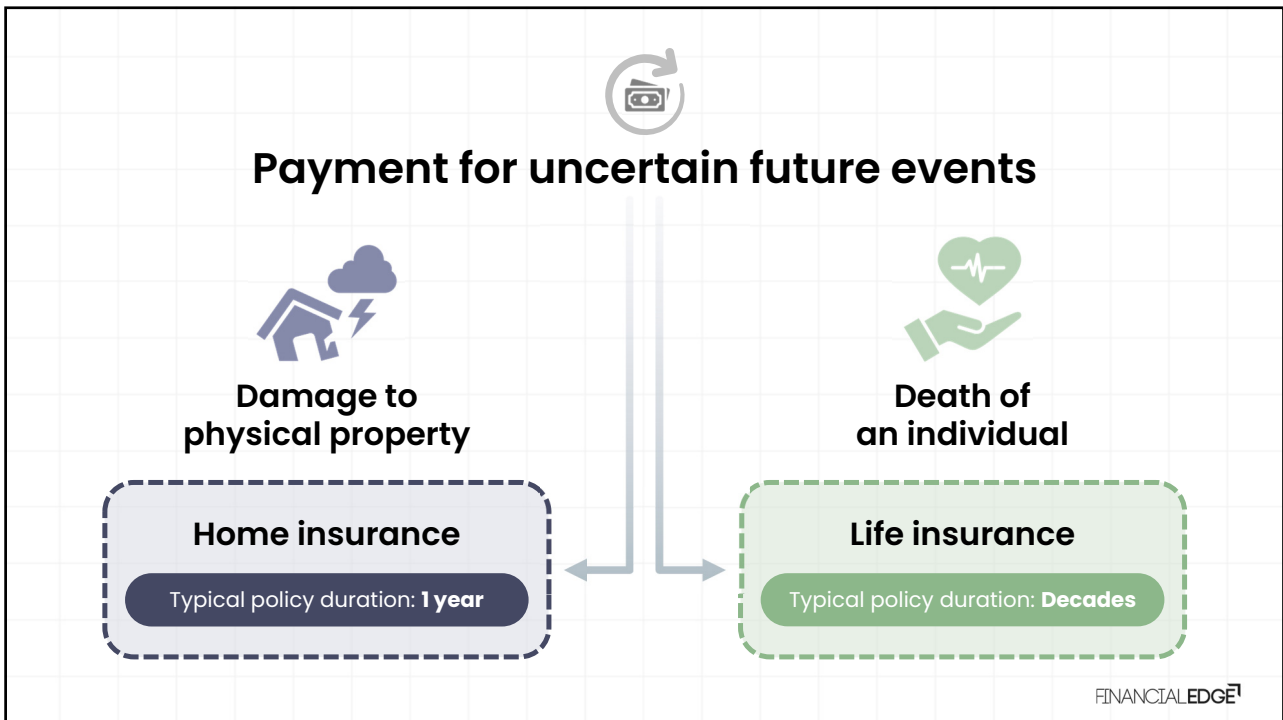


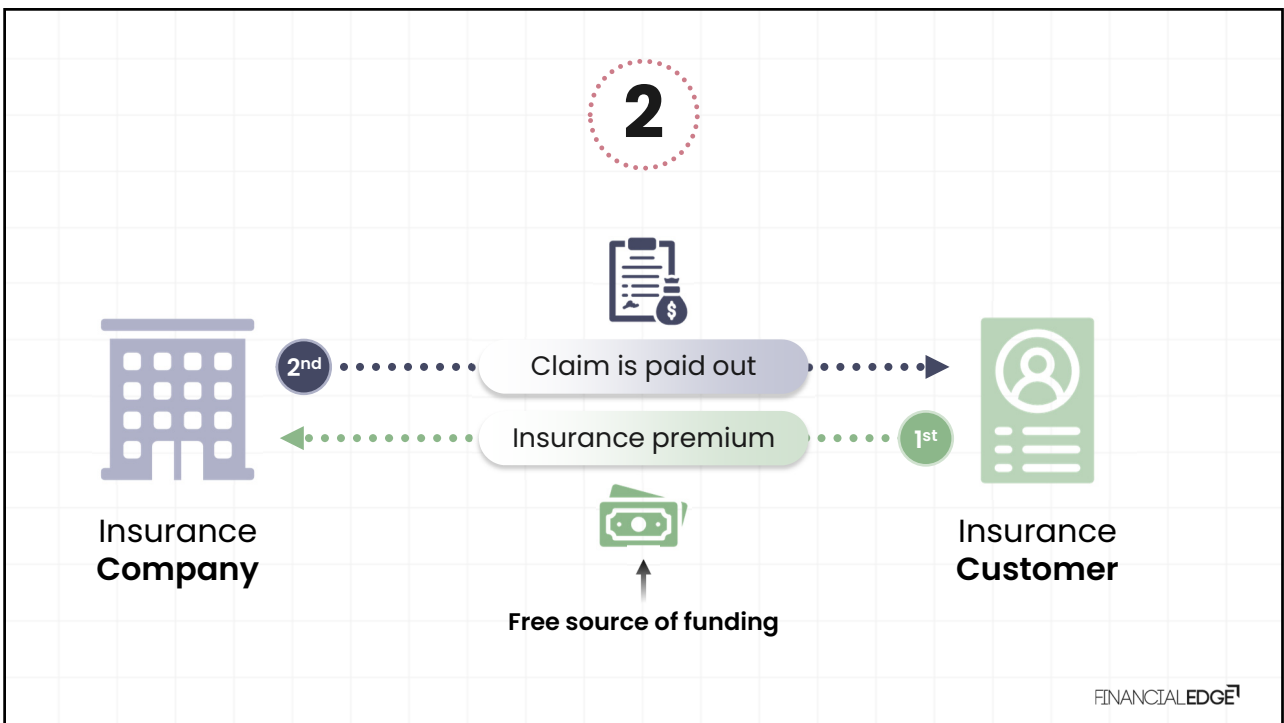
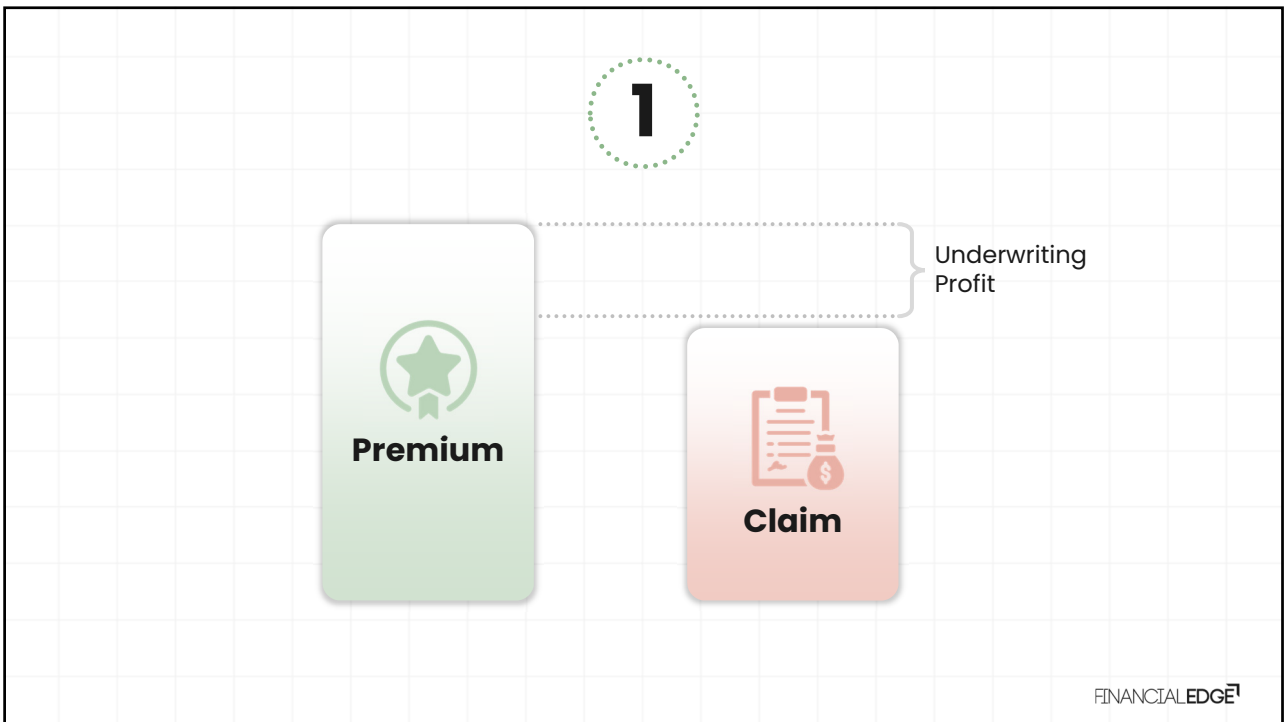
Recognize the main risks facing insurers

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## How an Insurance Company Works

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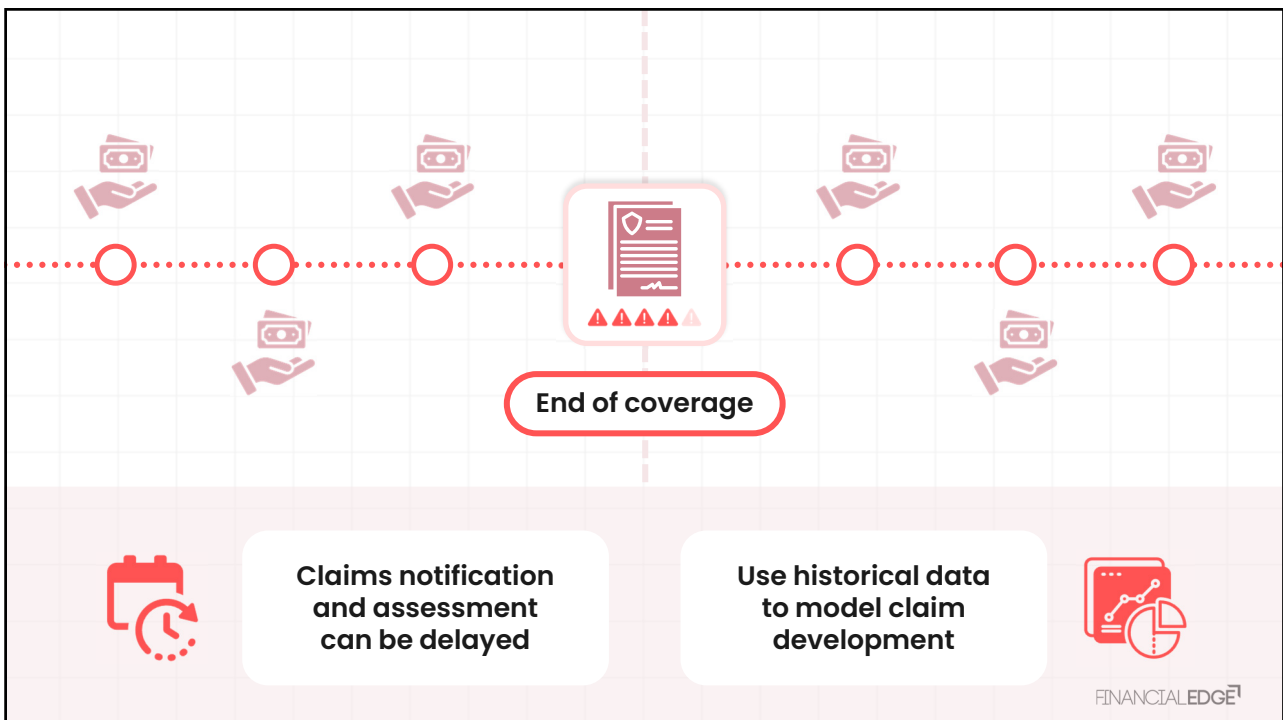
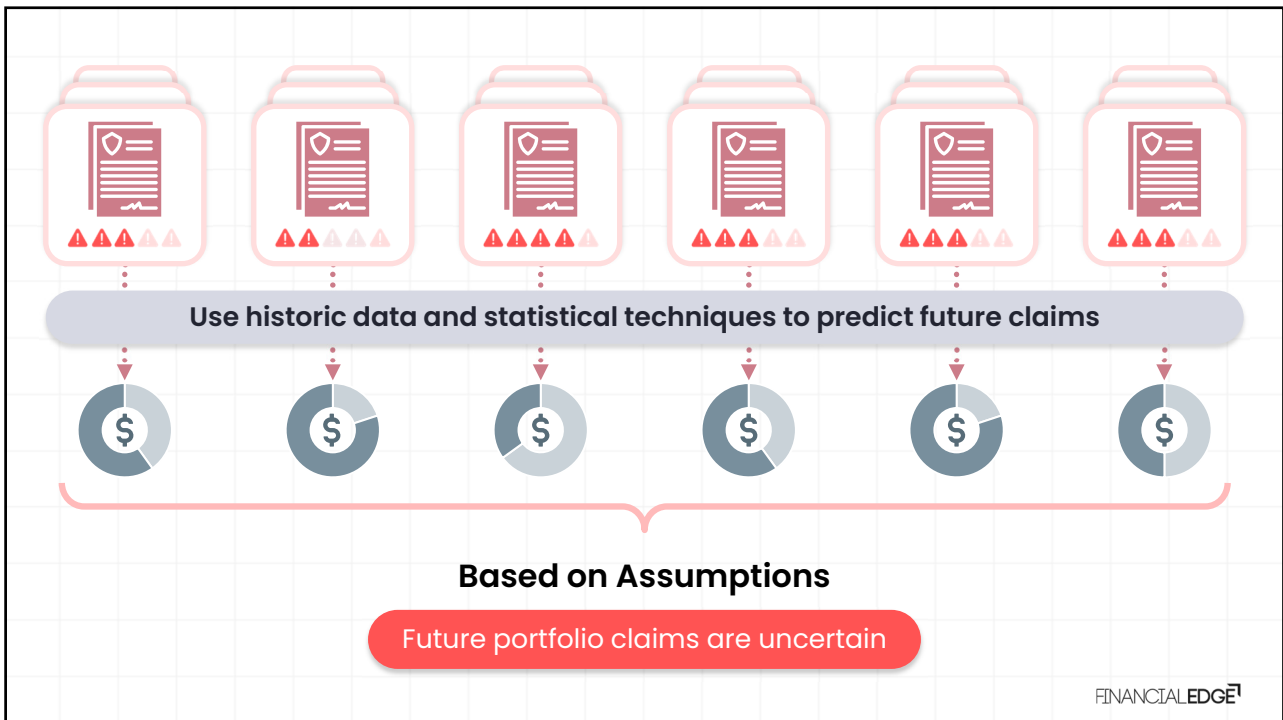


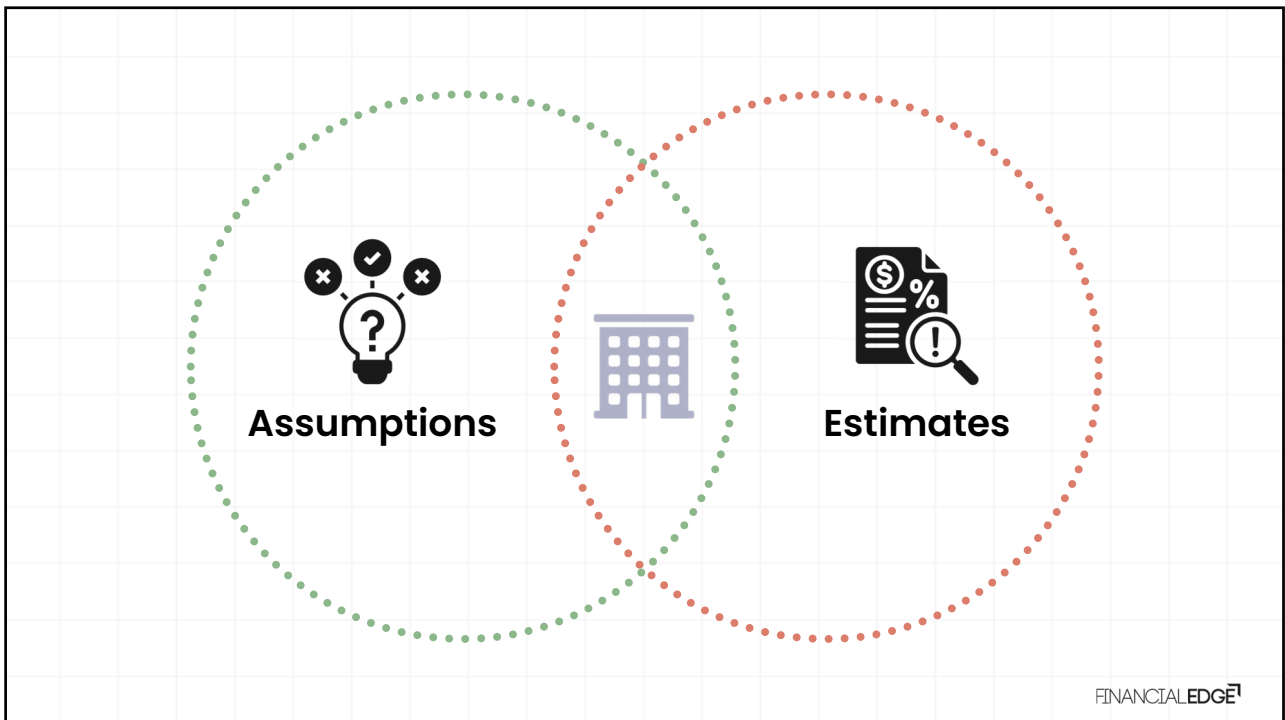
# Insurance Portfolios



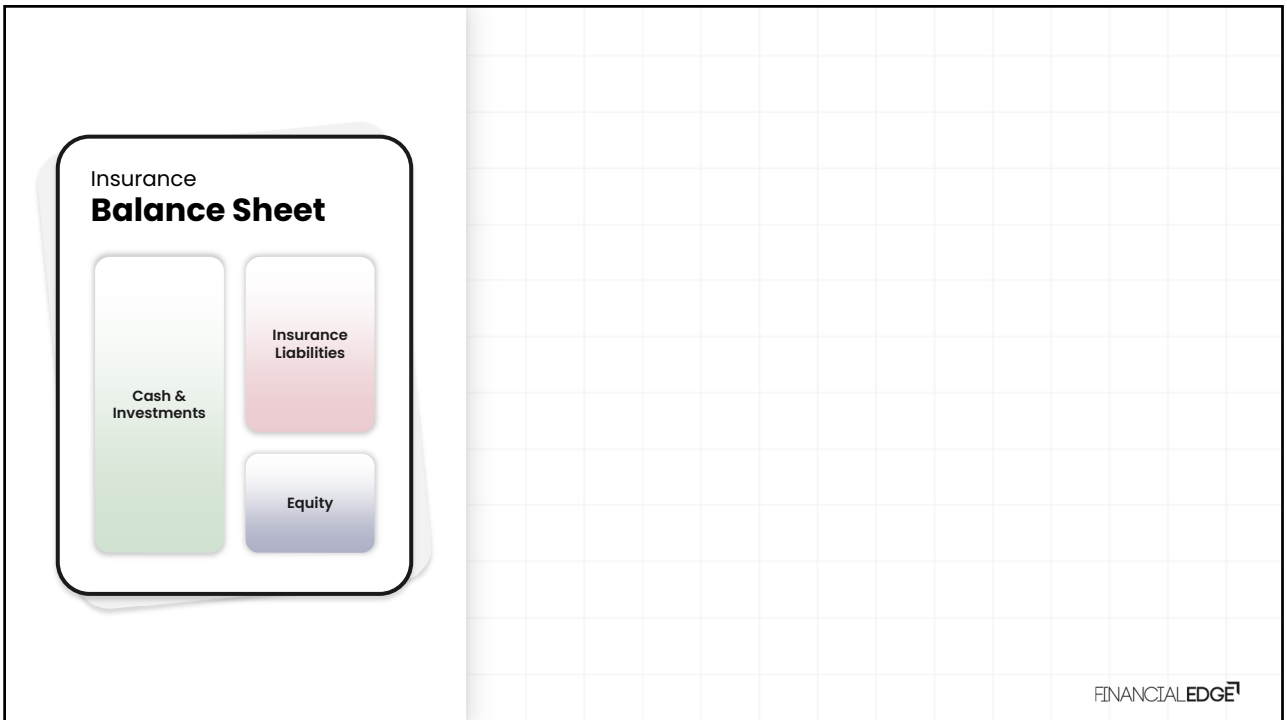
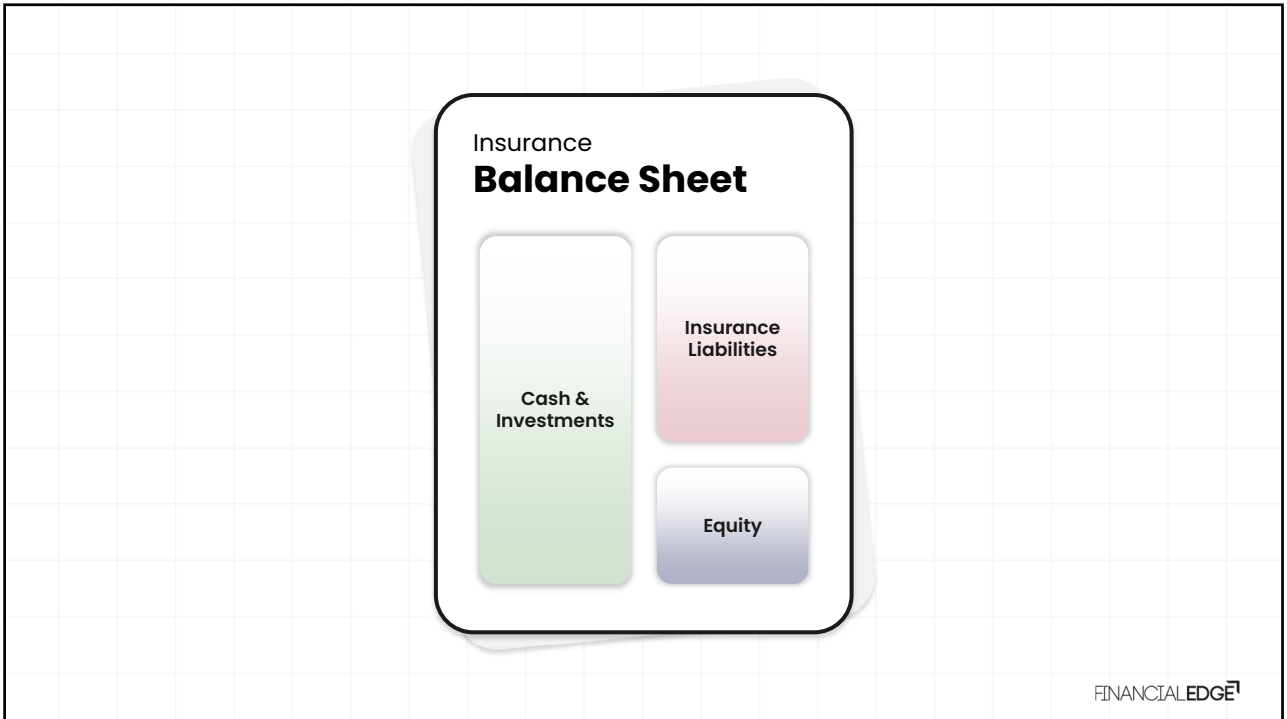
← MANAGE & DIVERSIFY RISK ACROSS A WHOLE PORTFOLIO →







# Simple Insurance Balance Sheet



Insurance  
**Balance Sheet**

Cash & Investments	Insurance Liabilities
Equity	

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Insurance  
**Balance Sheet**

Cash & Investments	Insurance Liabilities
Equity	

## Insurance Liabilities

**Upfront premium received is insurer liability**

Similar to a customer deposit

1

**Future underwriting profit** on the insurance contract

2

**Future claims** of the insurance contract

**INSURANCE PREMIUMS**


**Future profit & claims**

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Insurance  
**Balance Sheet**


Cash & Investments	Insurance Liabilities
	Equity

## Cash & Investments



**All cash & investments of the insurance company**






**Premiums invested to generate an investment return**

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Insurance  
**Balance Sheet**

Cash & Investments	Insurance Liabilities
	<b>Equity</b>


## Equity




**Regulatory requirement**



The insurer receives annual premiums and **invests them to generate returns**



At year-end, **profits are paid out** to shareholders



Without equity or reserves, there's no cushion for **unexpected losses**

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# Simple Insurance Income Statement

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## Insurance Income Statement

Premiums Earned
Claims Expense
Underwriting Profit
Investment Return
Operating Expenses
Pre-tax Profit
Tax Expense
Net Income

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Insurance  
**Income Statement**

Premiums Earned
Claims Expense
Underwriting Profit
Investment Return
Operating Expenses
Pre-tax Profit
Tax Expense
Net Income

**Premiums Earned**

Company's revenue earned as coverage is provided

**Claims Expense**

Insurer's cost of sales, based on incurred losses

**Underwriting Profit**

Effectively gross profit & is an important profit measure

**Loss Ratio =  $\frac{\text{Claims Expense}}{\text{Premiums Earned}}$**

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Insurance  
**Income Statement**

Premiums Earned
Claims Expense
Underwriting Profit
Investment Return
Operating Expenses
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Tax Expense
Net Income

**\$100m**  
Year 1 policies

YEAR START

**Record \$100m insurance liabilities initially**

**90%**  
Loss ratio

**\$10m**

Underwriting profit

**\$90m**

Claim payouts

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Insurance  
**Income Statement**

Premiums Earned
Claims Expense
Underwriting Profit
<b>Investment Return</b>
<b>Operating Expenses</b>
Pre-tax Profit
Tax Expense
Net Income

**Investment Return**

Profit generated from investments and cash balance in the balance sheet

**Operating Expenses**

This will include their staff, IT and head office costs

**Expense Ratio =  $\frac{\text{Operating Expenses}}{\text{Premiums}}$**

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Insurance  
**Income Statement**

Premiums Earned
Claims Expense
Underwriting Profit
Investment Return
Operating Expenses
<b>Pre-tax Profit</b>
<b>Tax Expense</b>
<b>Net Income</b>

**Pre-tax Profit**

Underwriting profit plus investment return less operating expenses

**Tax Expense**

After deducting tax expense, we reach net income

**Net Income**

Profit for shareholders

**Return on Equity =  $\frac{\text{Net Income}}{\text{Equity}}$**

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## Insurance Sectors – HOLD OFF

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### P&C Insurance

Damage to property  
or business



### Health Insurance

Sickness of  
policyholder



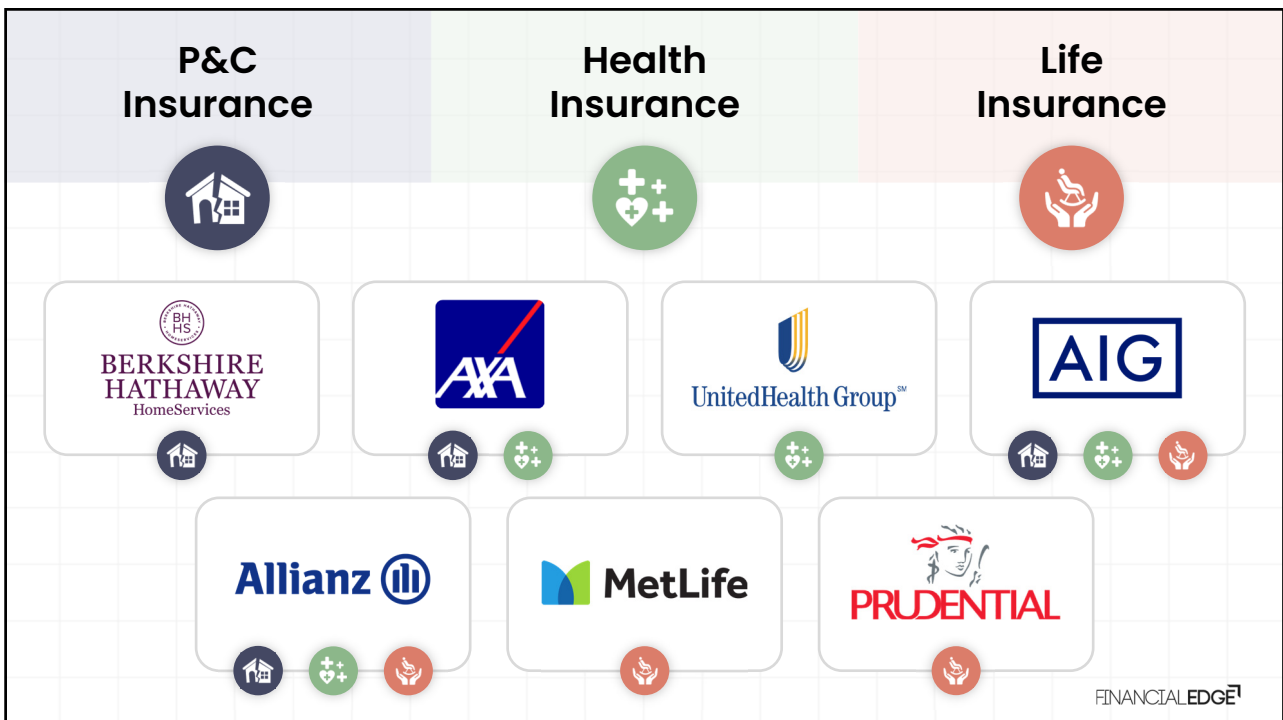
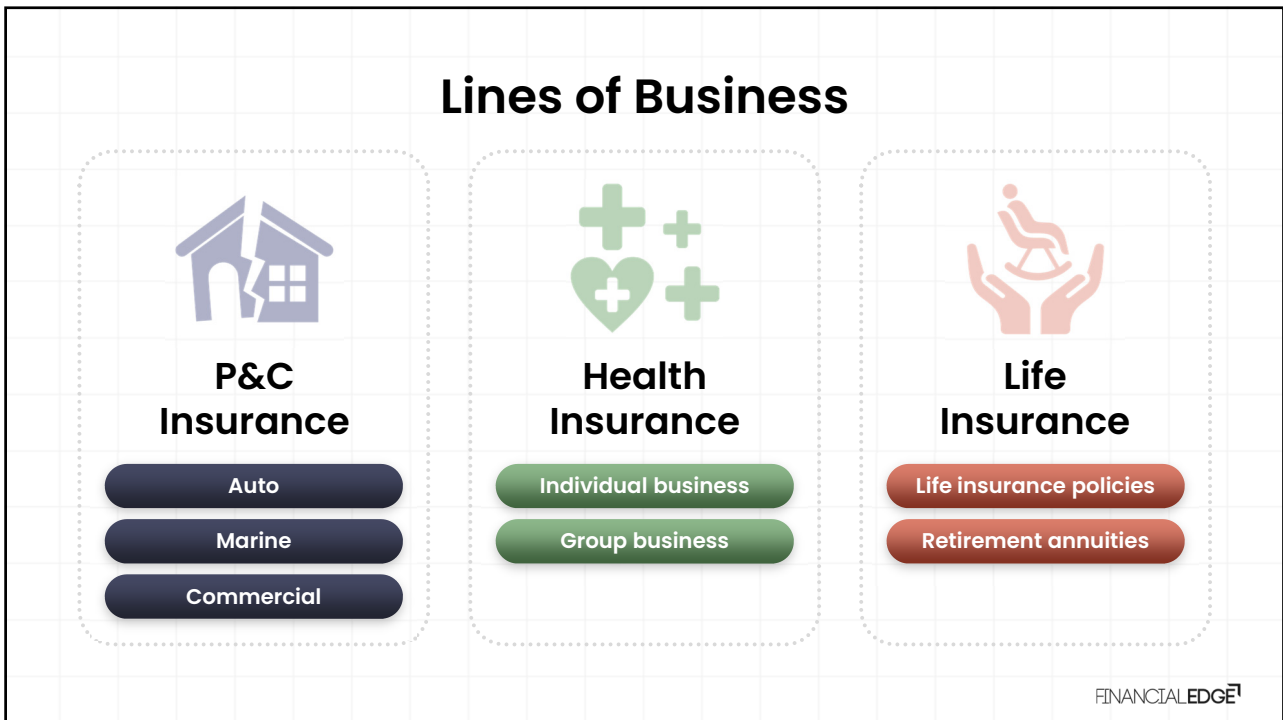
### Life Insurance

Death of  
policyholder

Typical policy: 1 year

Typical policy: Decades

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## Life Insurance

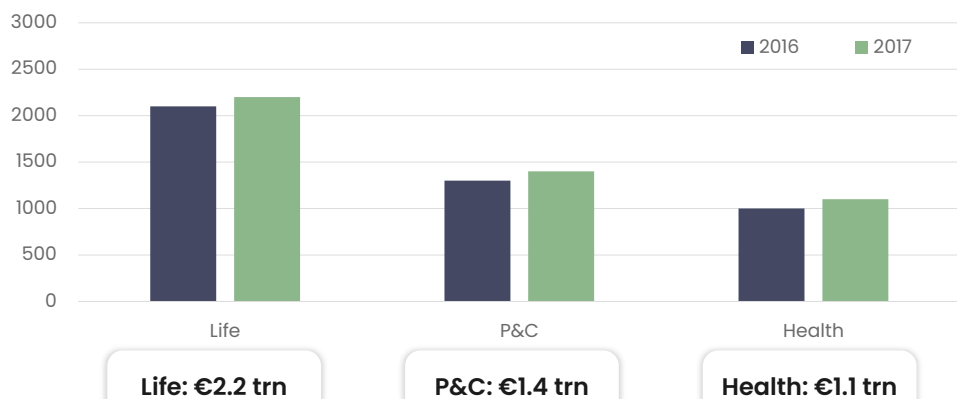
### LIFE INSURANCE POLICY

Pays out **on** the death of the policyholder

### RETIREMENT ANNUITIES

Pays out **until** the death of the policyholder

## Global Insurance Market €BN



Source: McKinsey & Company

# Life Insurance Products

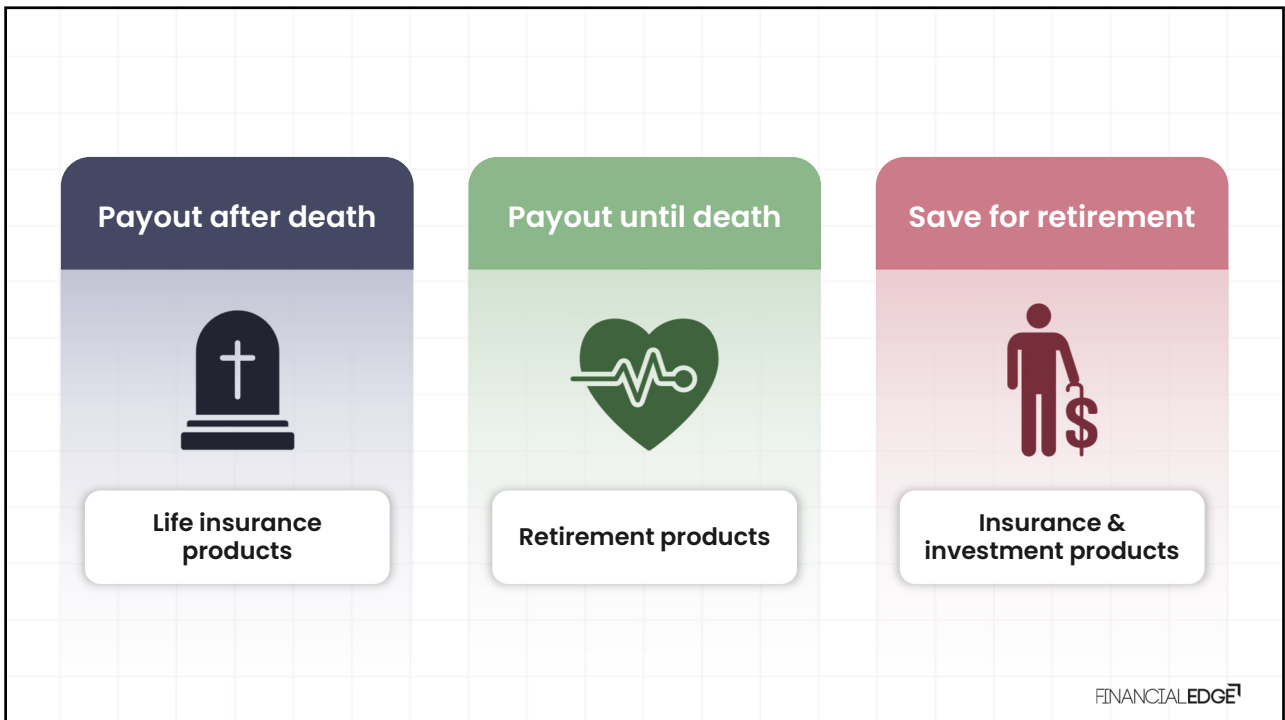
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Range of products


Risks transferred  
to insurer

Profit generation  
methods


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**Risk Products**



**Spread Products**




**Fee Products**




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**Risk Products**





**Spread Products**




**Fee Products**




## Risk Products

 **Uncertainty around claim timing or amounts** 

 **Underwriting Profit = Premiums - Expected Claims**

<p><b>Term Life Policy</b></p> <p>Pays a fixed amount at the policyholder's death</p>	<p><b>Critical Illness Policy</b></p> <p>Pays a fixed amount if the policyholder has a serious illness</p>
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**Insurer still faces investment risk, but insurance risk is primary**

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Risk Products

Spread Products

Fee Products

## Spread Products

Products with a built-in savings component

**Spread = Investment Return - Guaranteed Rate**

**Fixed Annuities**

Policyholder pays a lump sum; insurer pays fixed yearly amounts until death, with a fixed rate built in

**US Whole Life Policies & European Participating Life Policies**




Insurer invests premiums; part of returns go to the policyholder's savings, which funds the death benefit

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Risk Products

Spread Products

Fee Products

## Spread Products

Products with a built-in savings component

**Fixed Annuities**

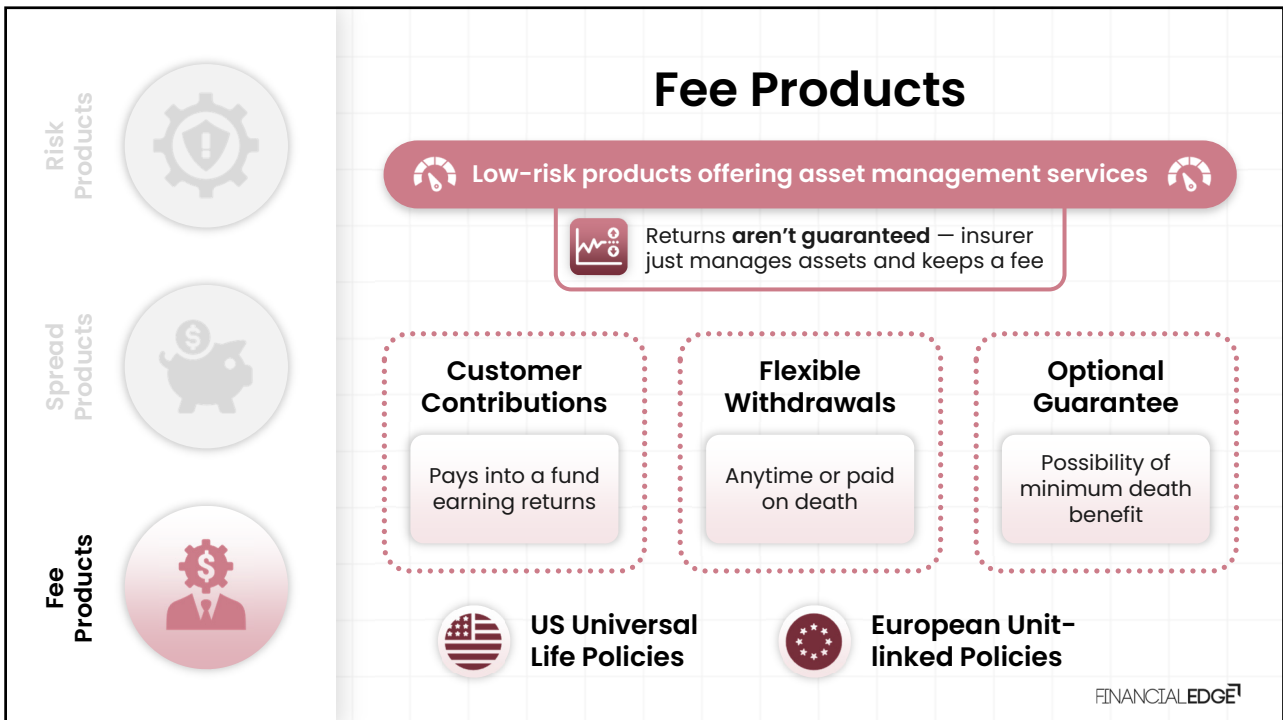
Policyholder pays a lump sum; insurer pays fixed yearly amounts until death, with a fixed rate built in

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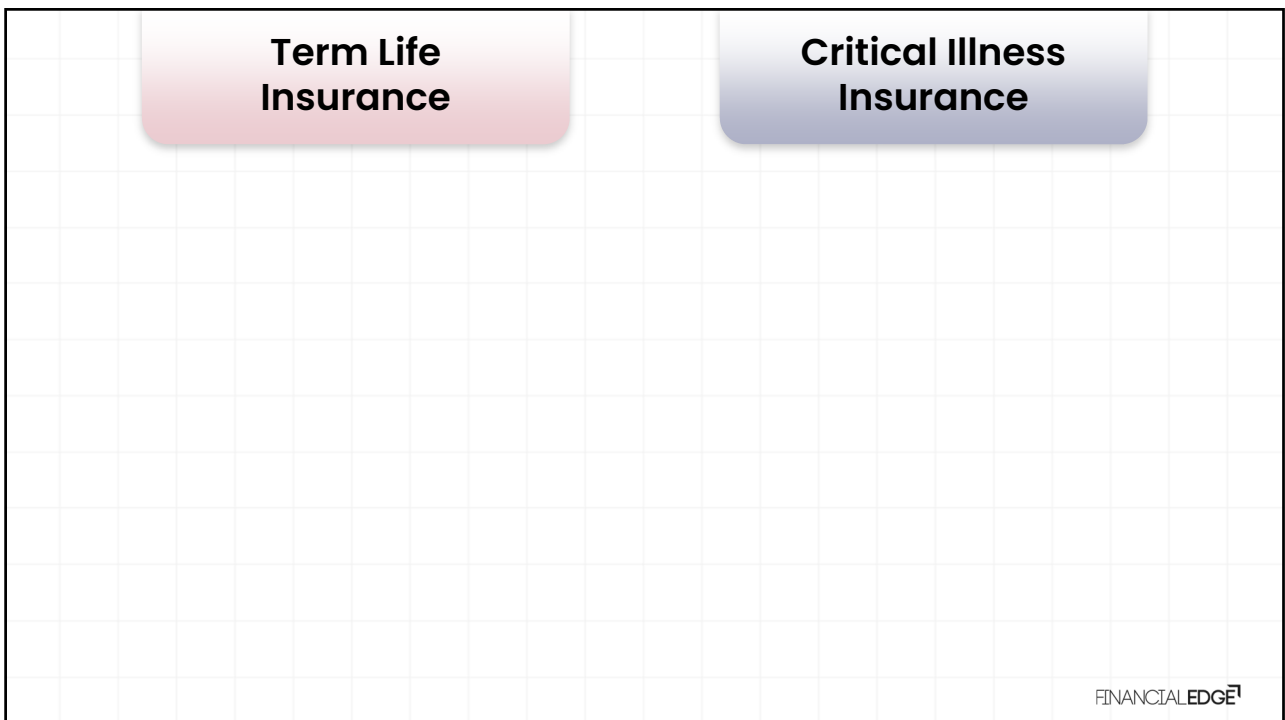
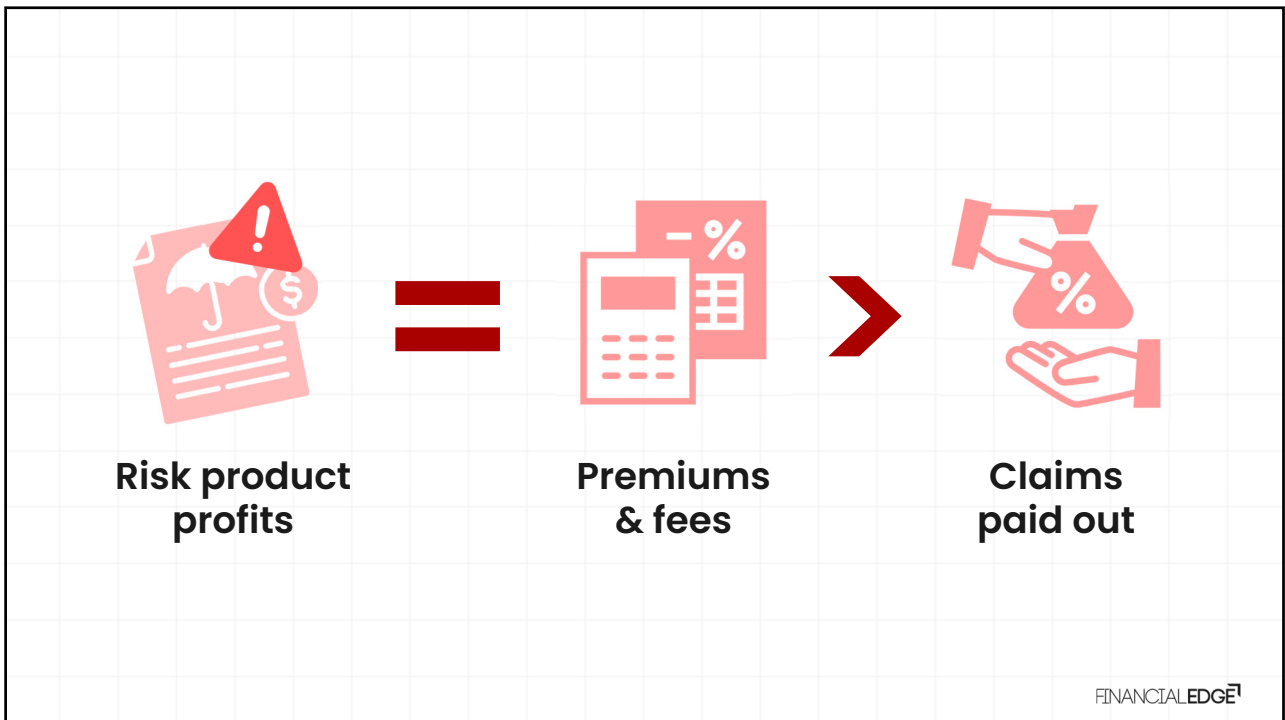
Insurer still faces longevity-timing risk, but investment risk is primary

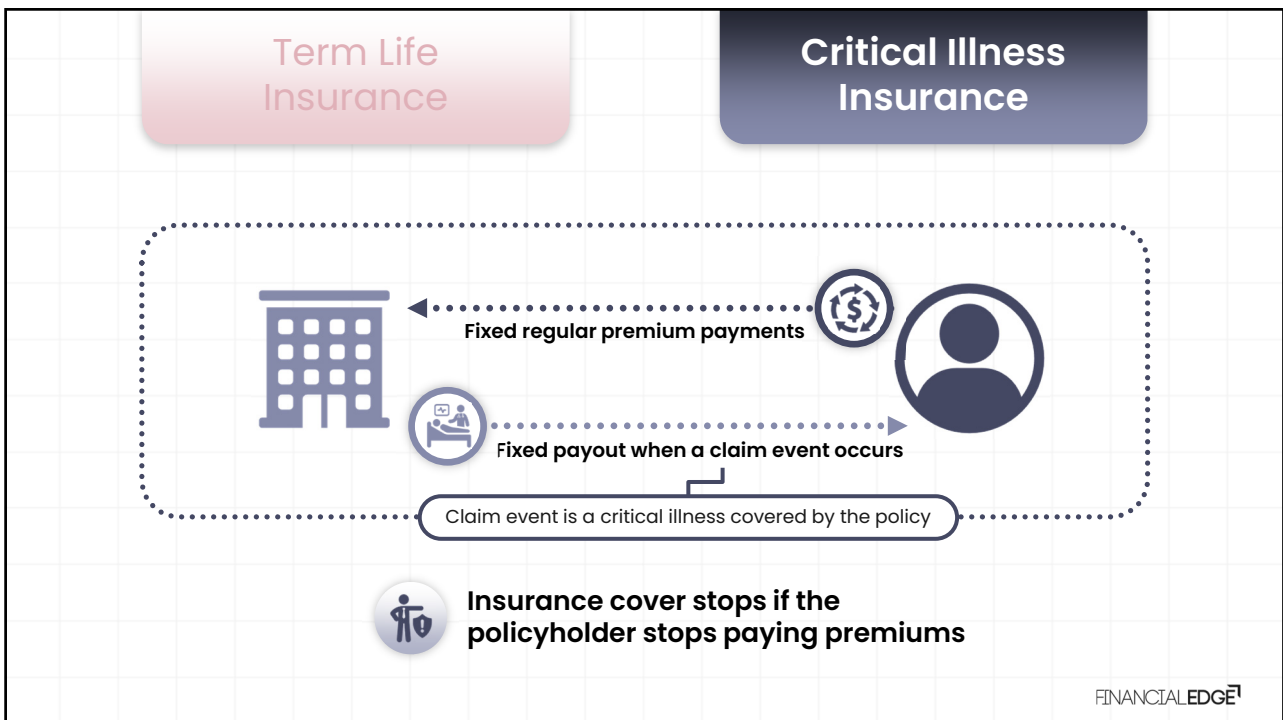
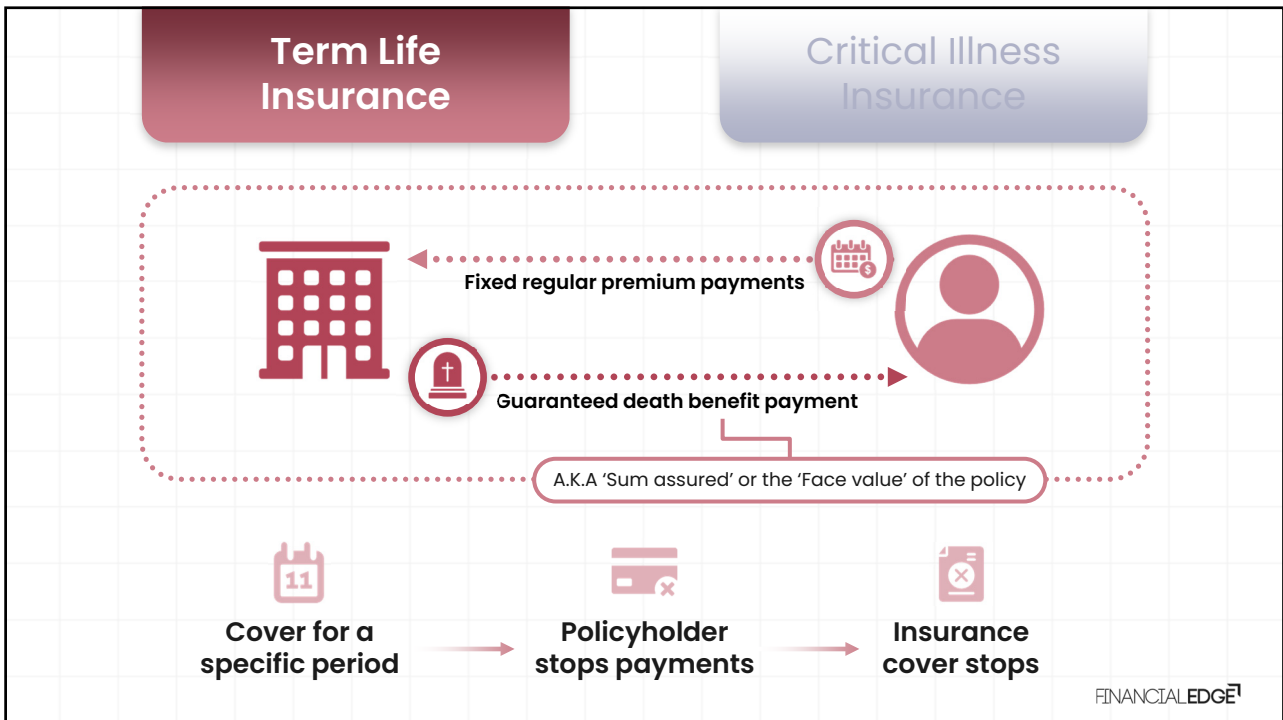
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# Risk Products – Examples

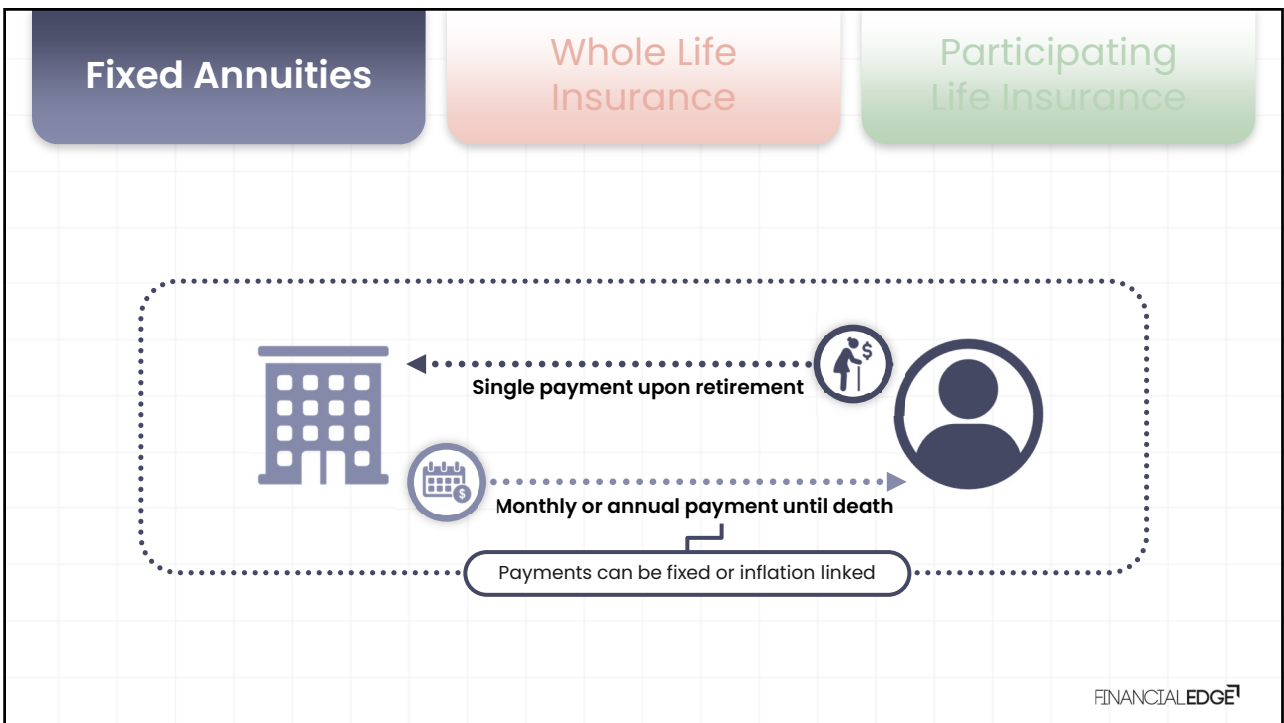
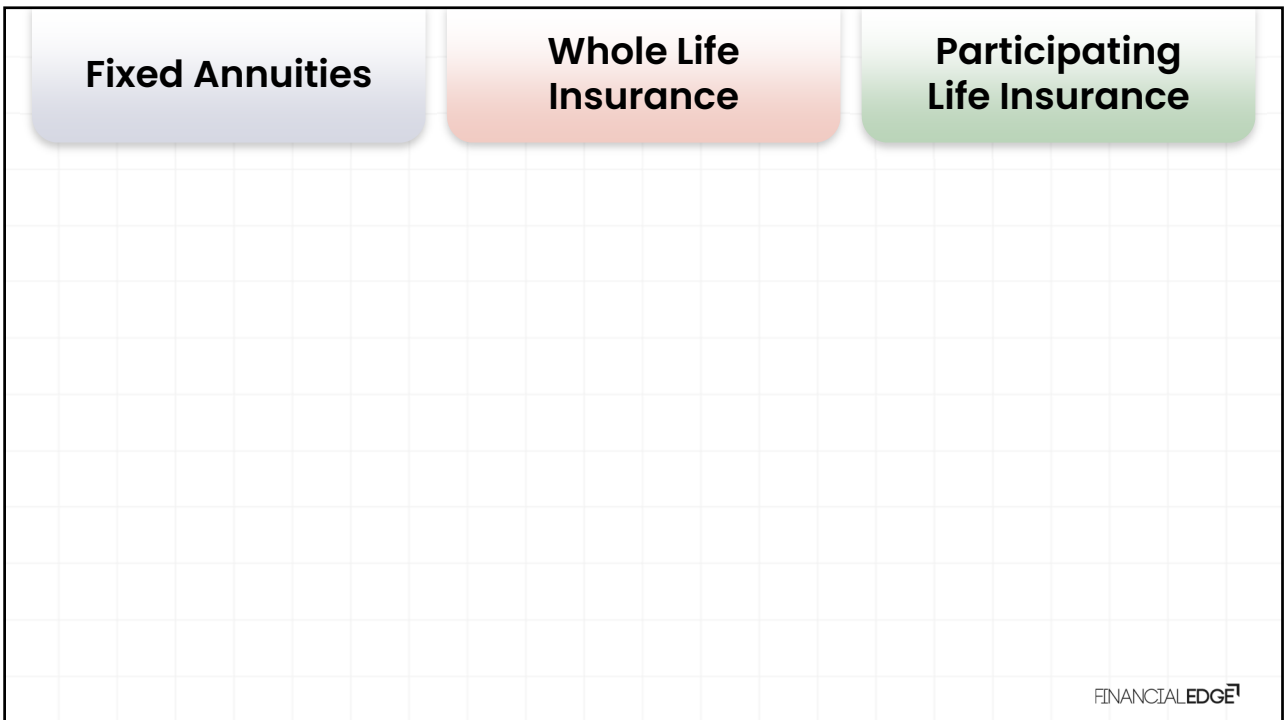
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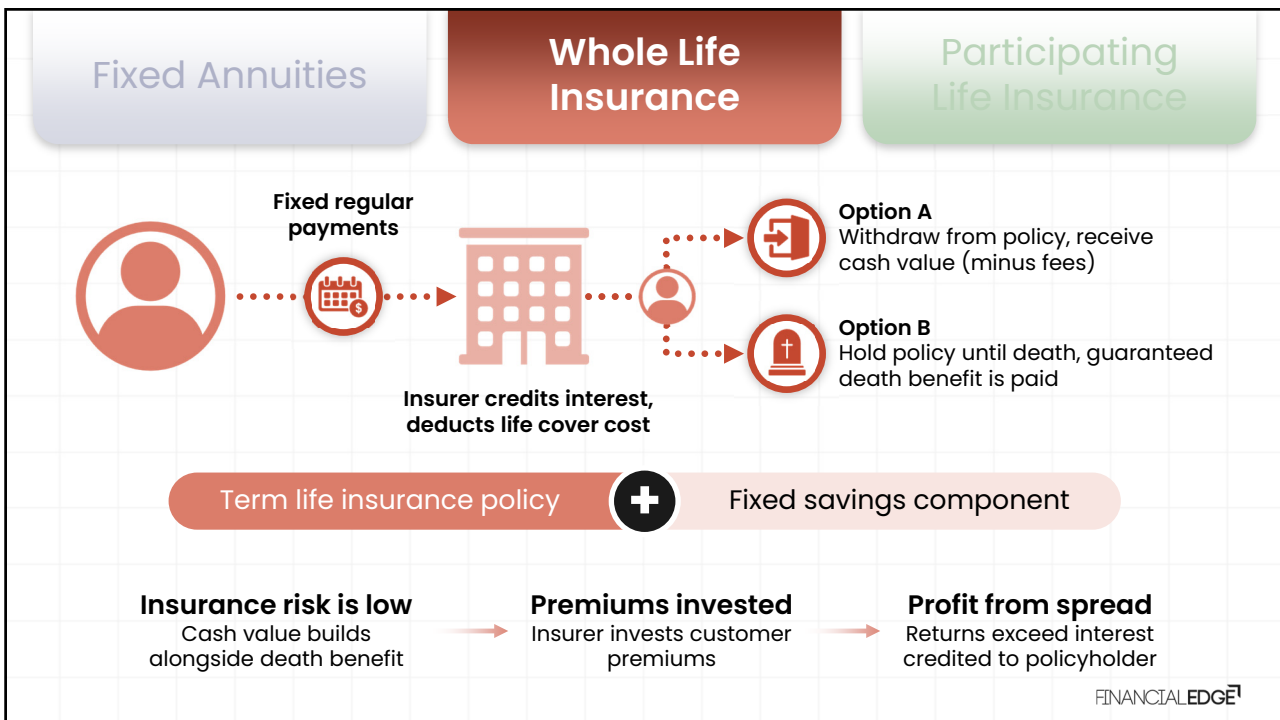
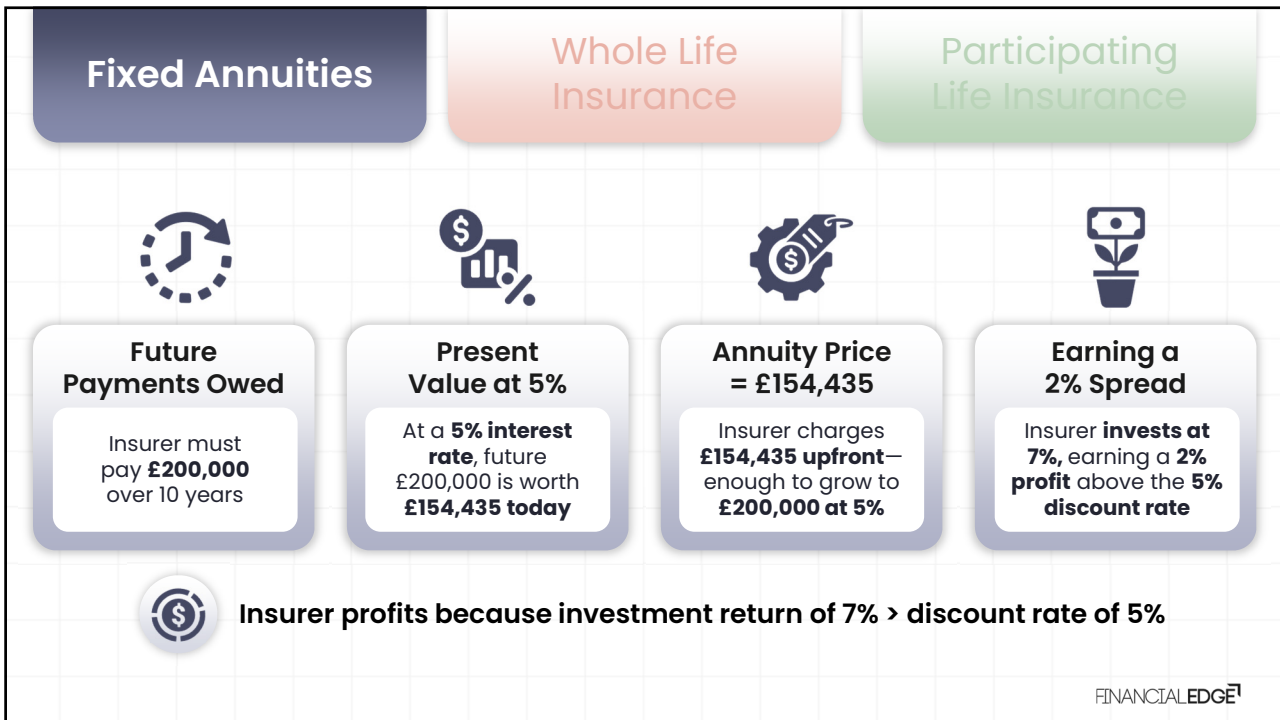


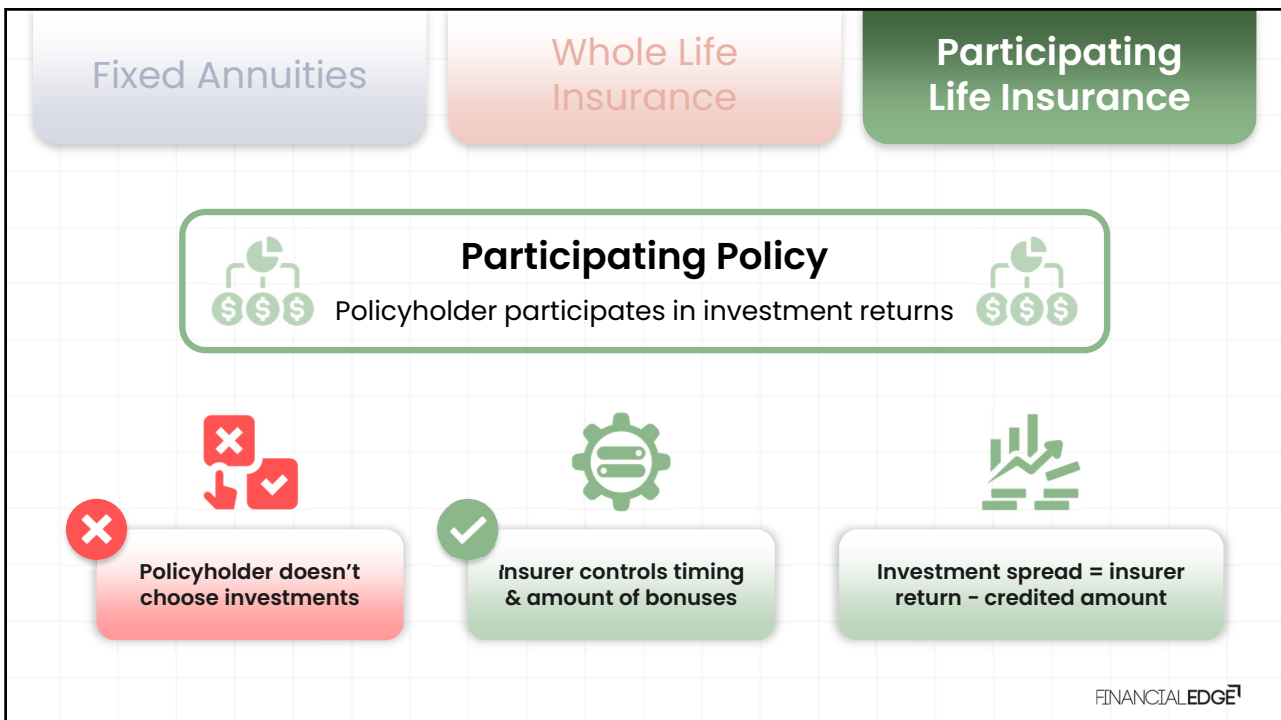
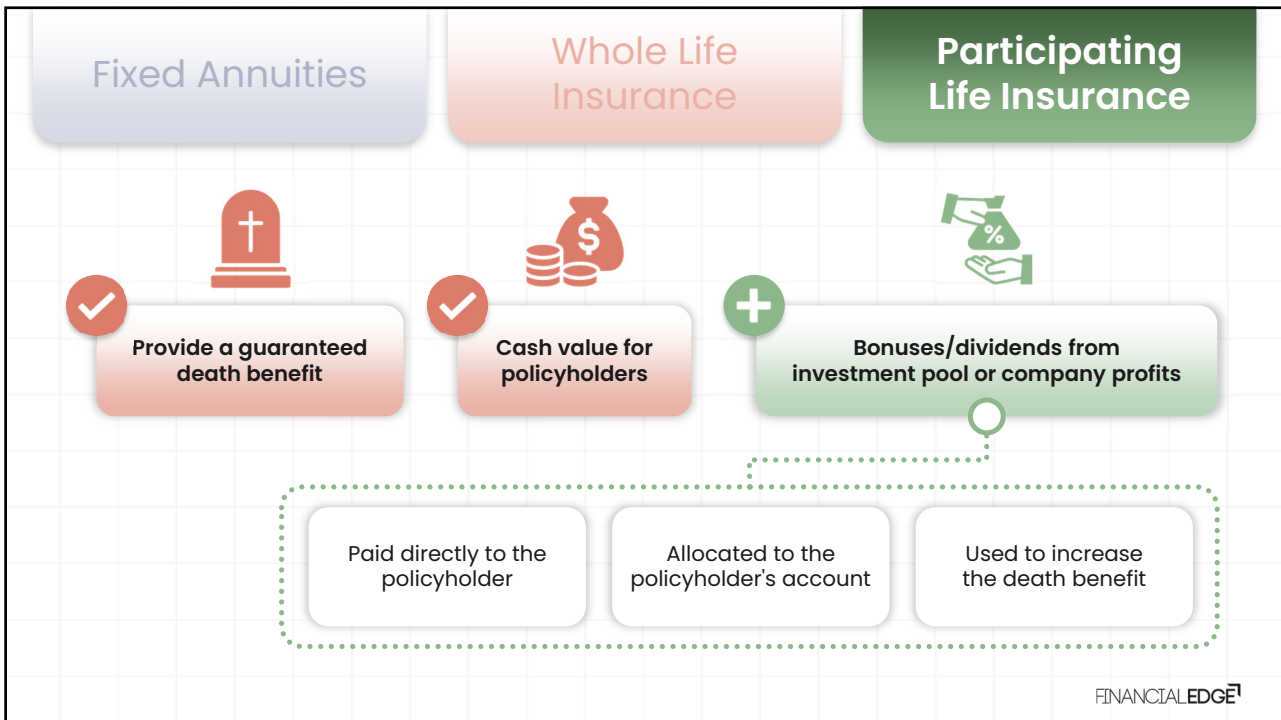


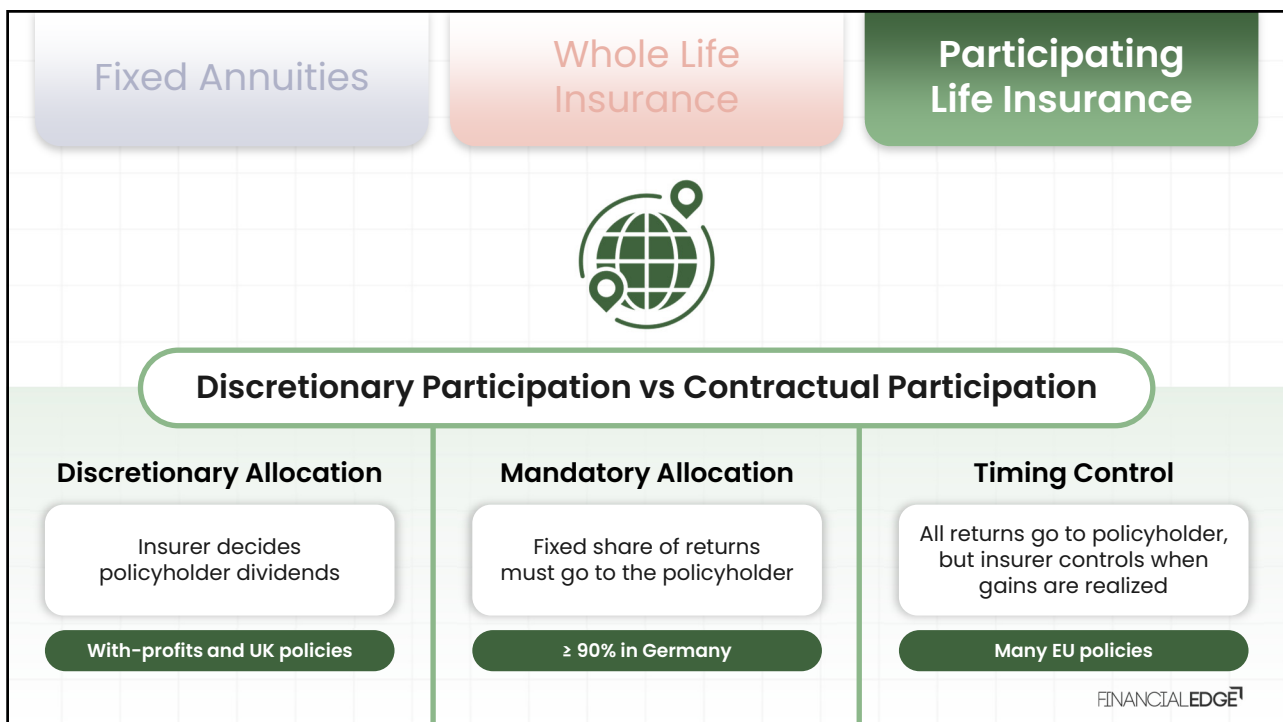
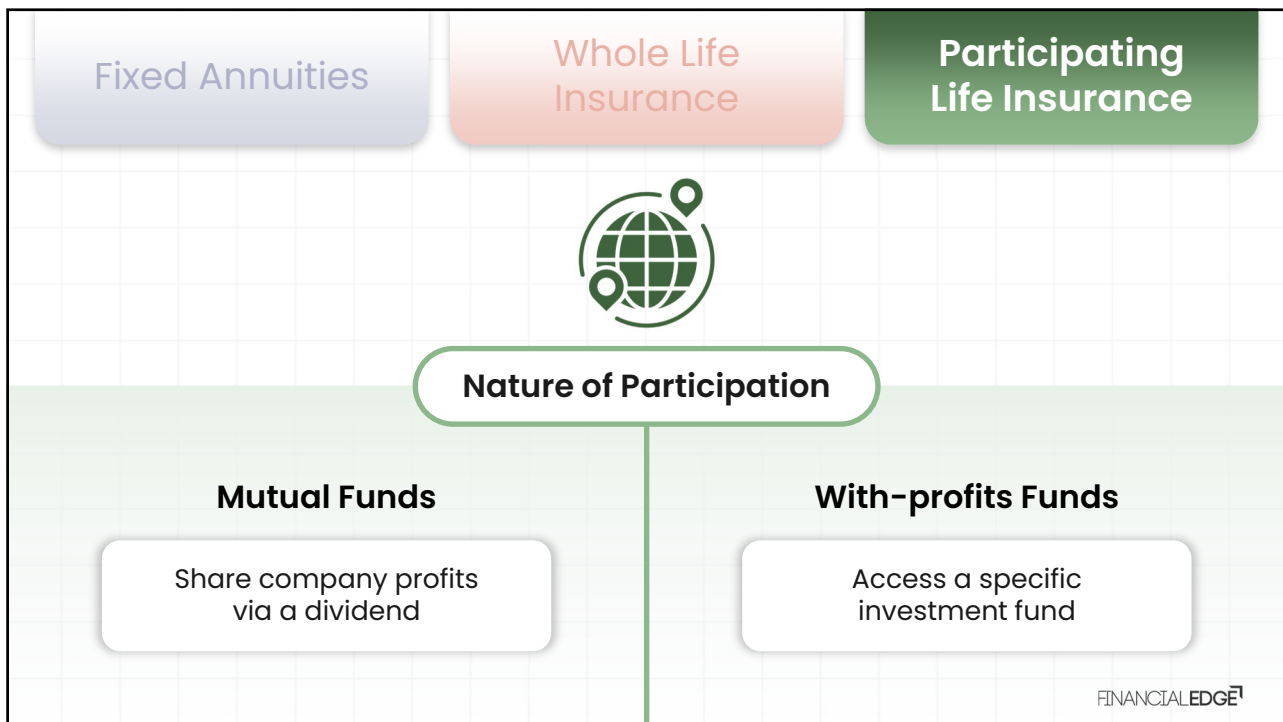
## Spread Products – Examples

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## Fee Products – Examples

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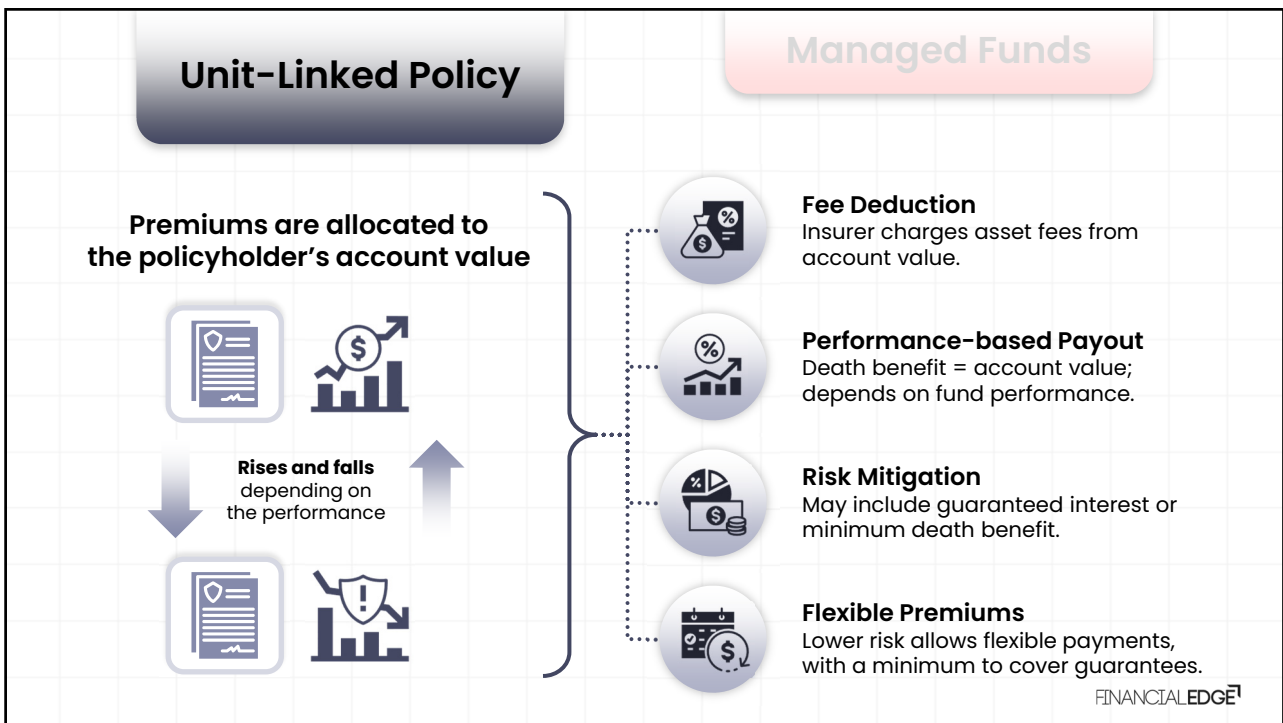
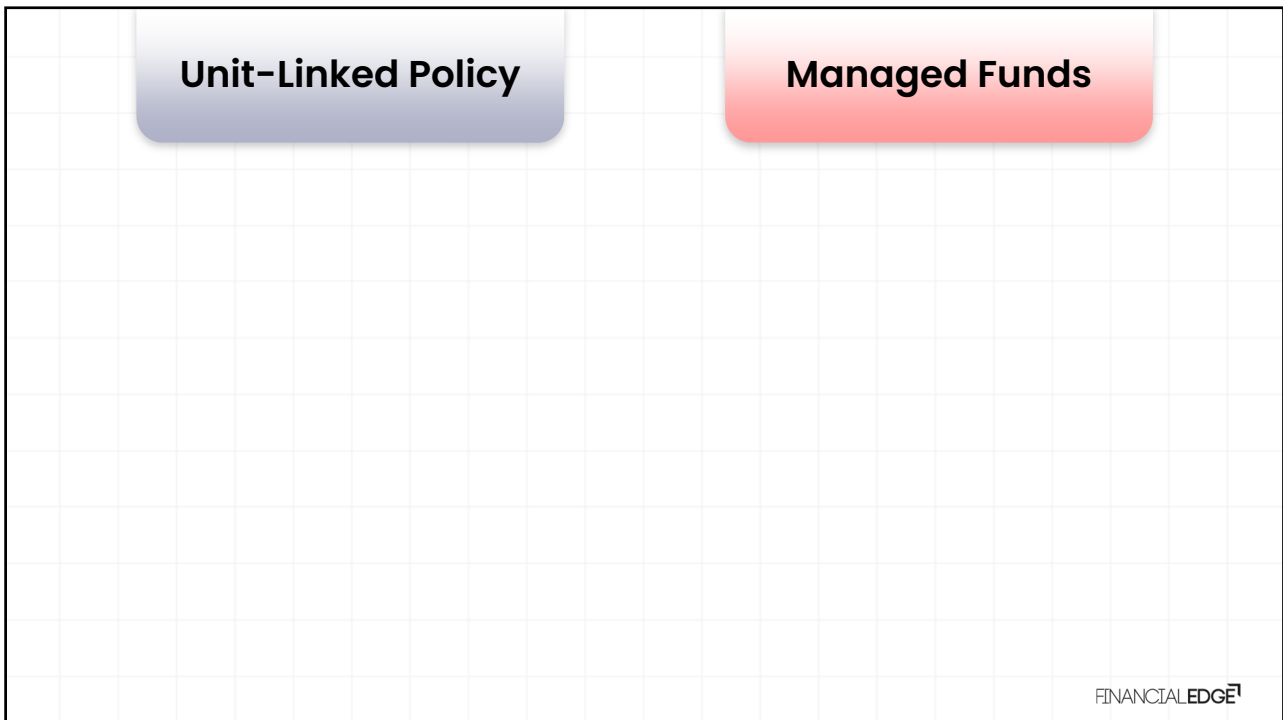
**Fee product  
profits**

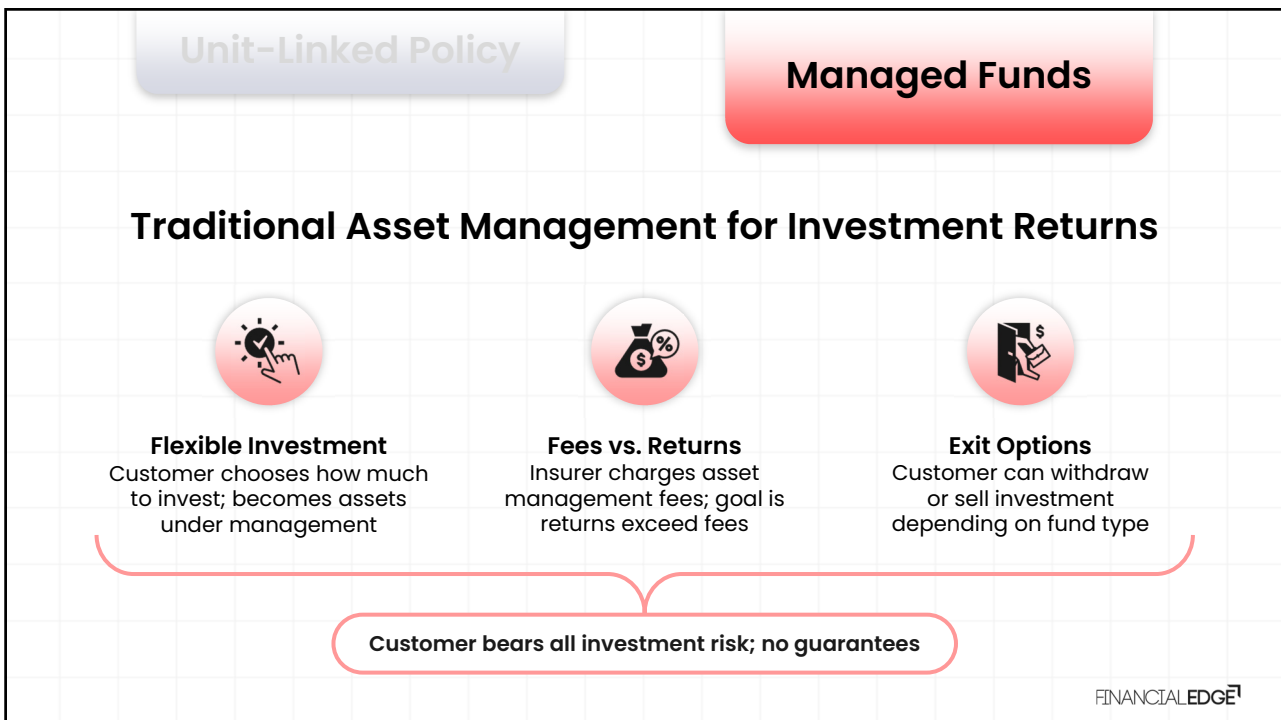
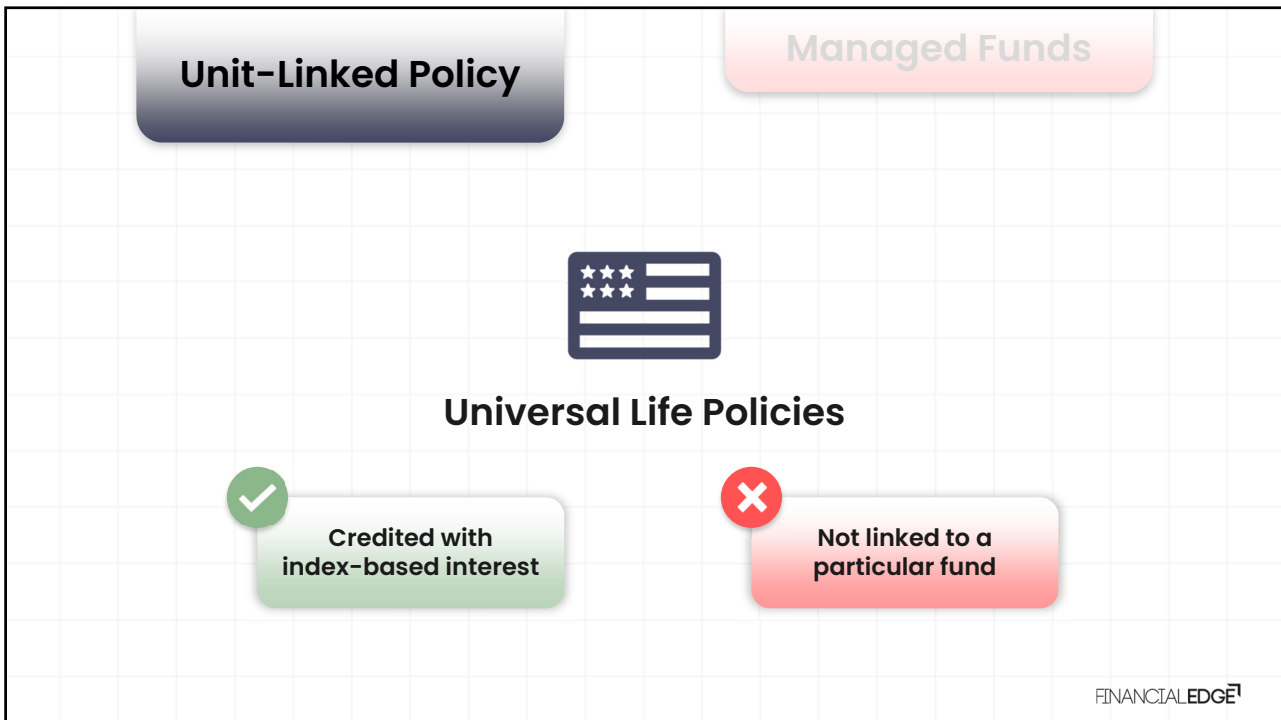


**Asset management fees  
charged to the policyholder**

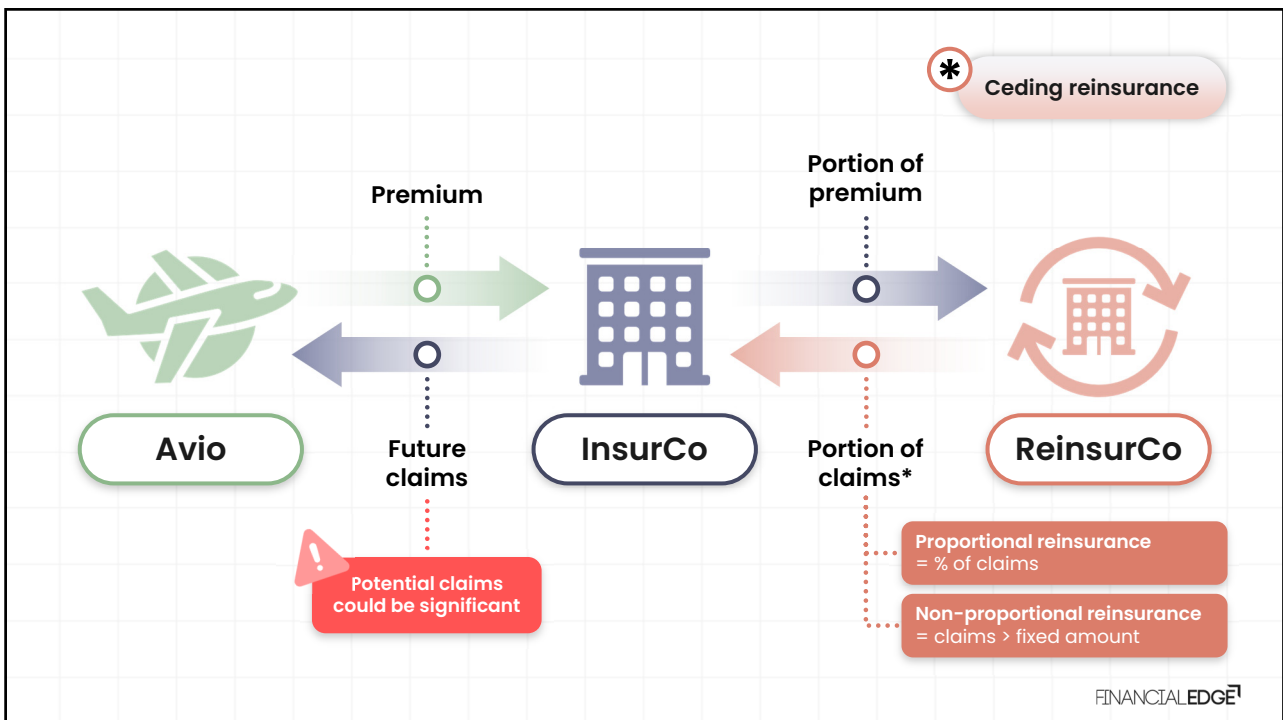
**Investment risk is on the policyholder**

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# Reinsurance



## Reinsurance is commonly used in...

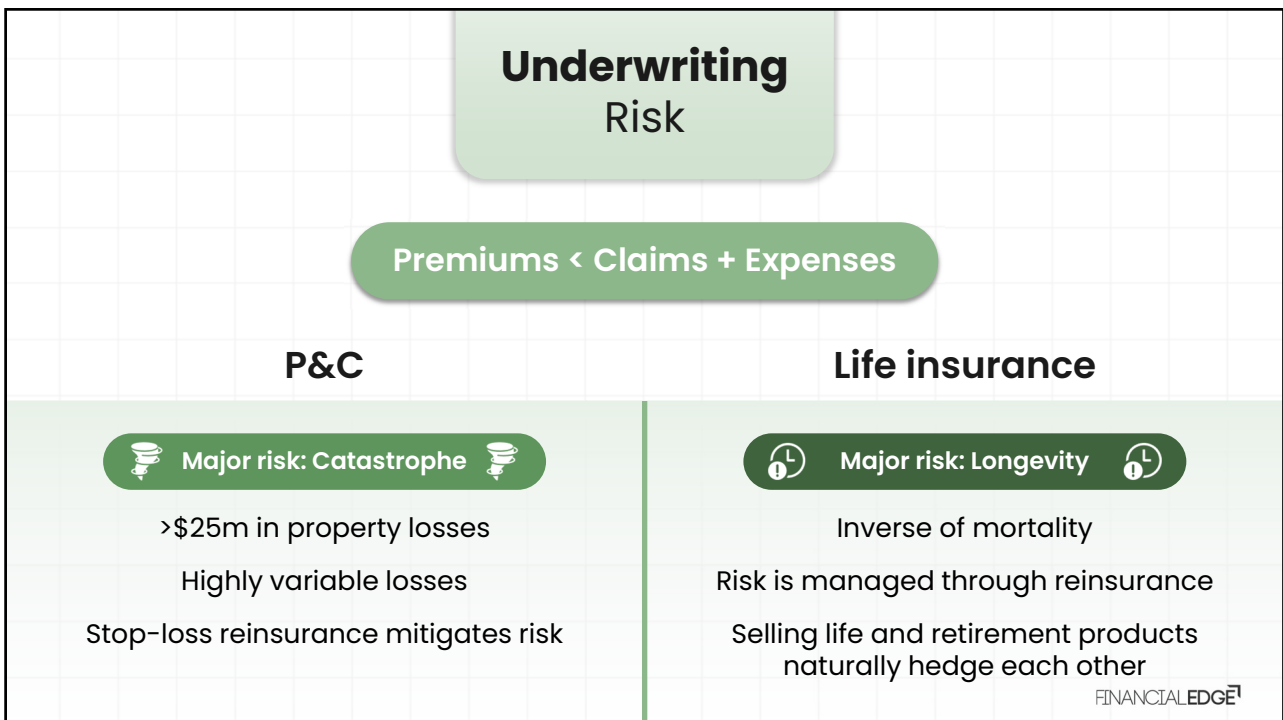


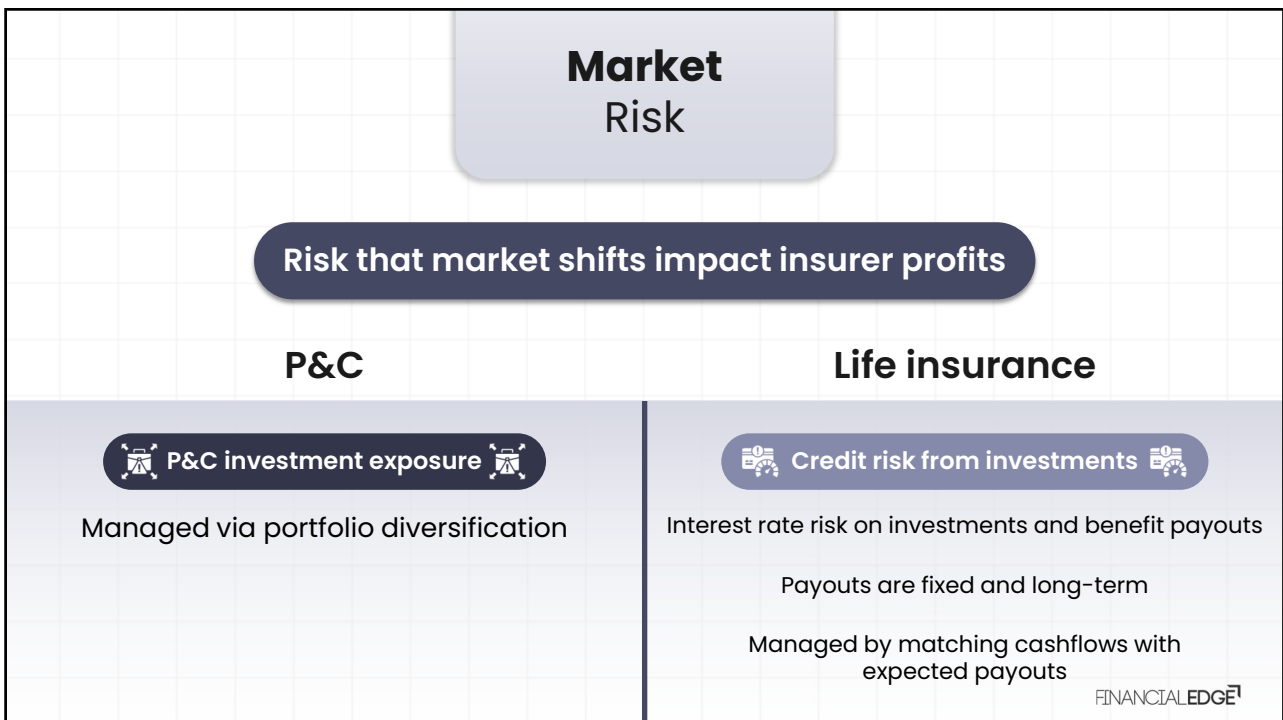
Property & Casualty (P&C)

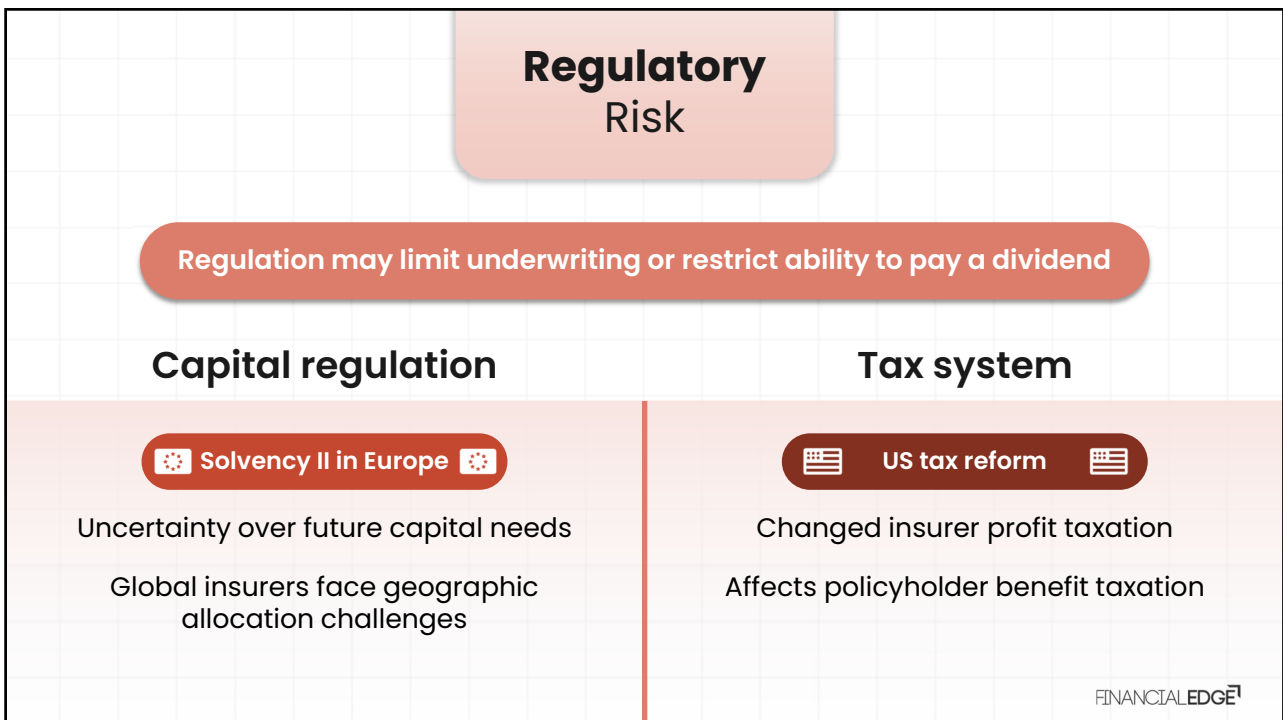


Commercial

## Risks in Insurance







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