Managing Risk to Reputation
Discussant Response

Enterprise Risk Management and Corporate Governance for Insurance Firms, EDHEC Business School

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Managing Risk to Reputation

1. The role of reputation for re/insurers
2. Influence of reputation on ratings
3. The model proposed and its practical implementation

"It takes 20 years to build a reputation and five minutes to ruin it.

Warren Buffet, Chairman and CEO, Berkshire Hathaway

1. The role of reputation for re/insurers

Reputation = Experience   Expectations

Insurance = (nothing more than) a promise to pay > reputation is critical

- Exacerbated by maturity of contract obligation, offset by lack of customer liquidity (vs banking)
- Policyholder purchase decision is based on brand, reputation, [credit rating]

Reputation is a significant part of intangible value

- But many insurers trade below book value

Reputation is key for capital markets

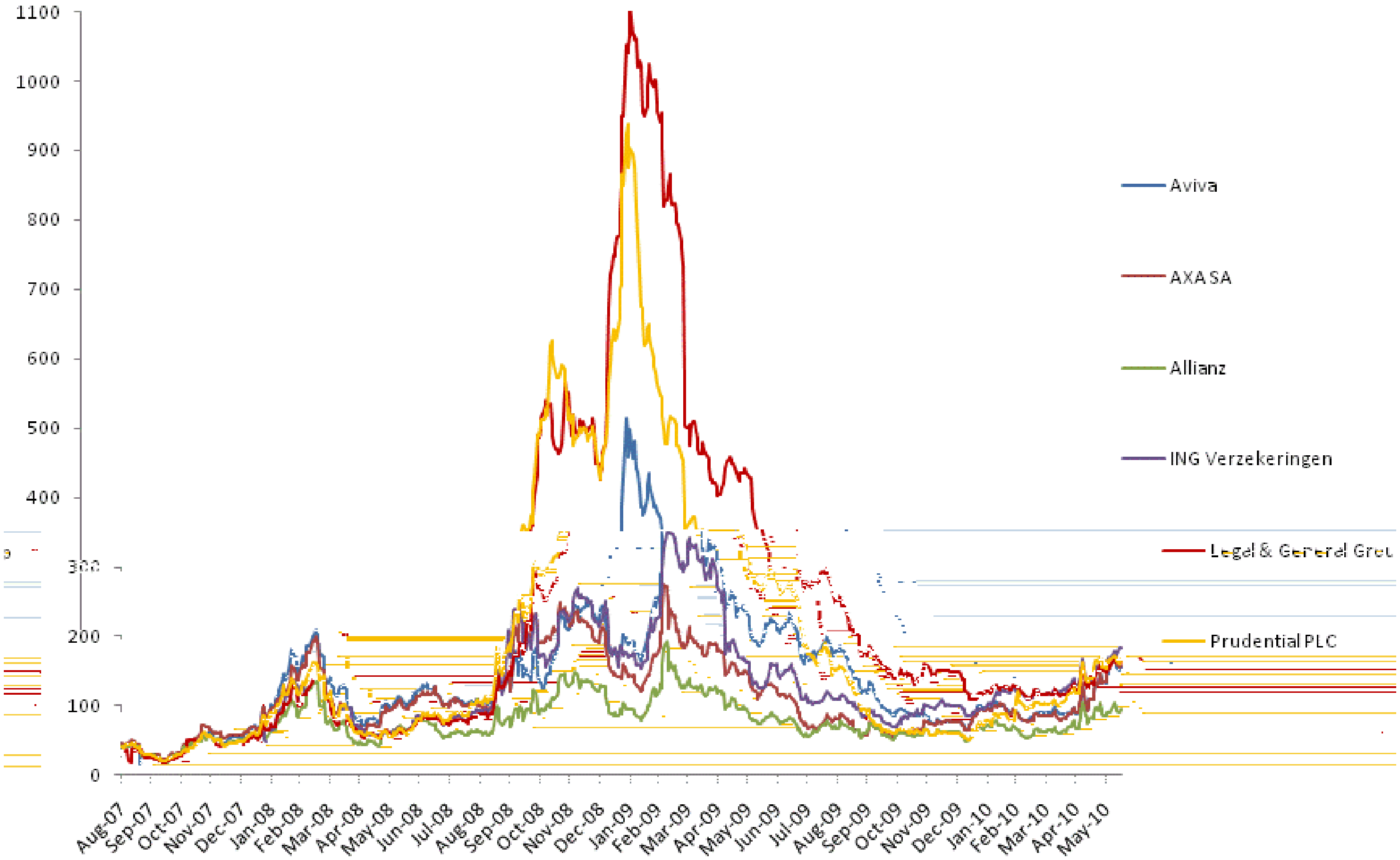
- particularly for poorly-understood and opaque sectors
- Perception and reputation moves markets, reality (usually) catches up afterwards

Risks to reputation change over time

- Spring 2009 : Capitalisation is the main risk
- Summer 2010 onwards : Exposure to periphery eurozone investments

1a. Reputation and CDS Spreads European Insurers

Strong spread tightening in the crisis, huge rebound



Source: Bloomberg

2. The influence of reputation on ratings

Following the break-up of the transaction, Moody's said that ..... the negative outlook .....reflects Moody's view that the potential exists for **reputational damage to Prudential** as a consequence of the failed bid, in terms of future capital markets access, franchise and market position (i.e. potentially future lower new business sales/greater outflows of existing business), as well as some uncertainty surrounding the future strategic direction of the Group.

Action, April 2011

Risk Management

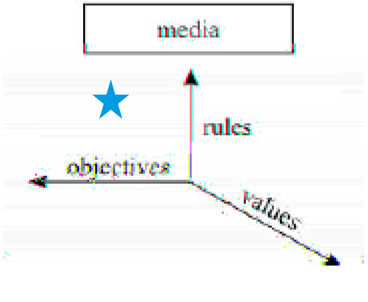
protecting the interests of its policyholders and other stakeholders. Taking risks, whether in underwriting, investments, sales practices, acquisitions, or other areas, is a necessary activity for an insurance company. However, it is vitally important that management (and the board of directors) understand the risks assumed and engage in active measures to manage those risks in order for the company to maintain its financial performance and flexibility, **reputation**, market position, and confidence in the capital markets.

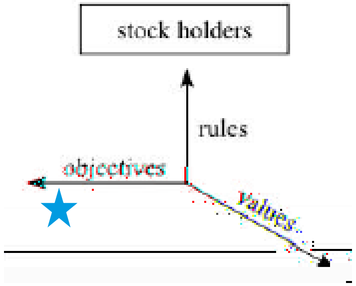
Methodology, May 2011

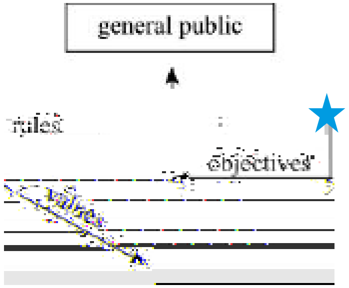
3. The theory and an insurance example

3 x dimensional space in which organisations must position themselves for all stakeholders and for many factors

An example   Orphan asset settlements for UK Life funds







The challenges

Evaluating the position for each variable with respect to each stakeholder

Aggregating these positions

3a. The model proposed

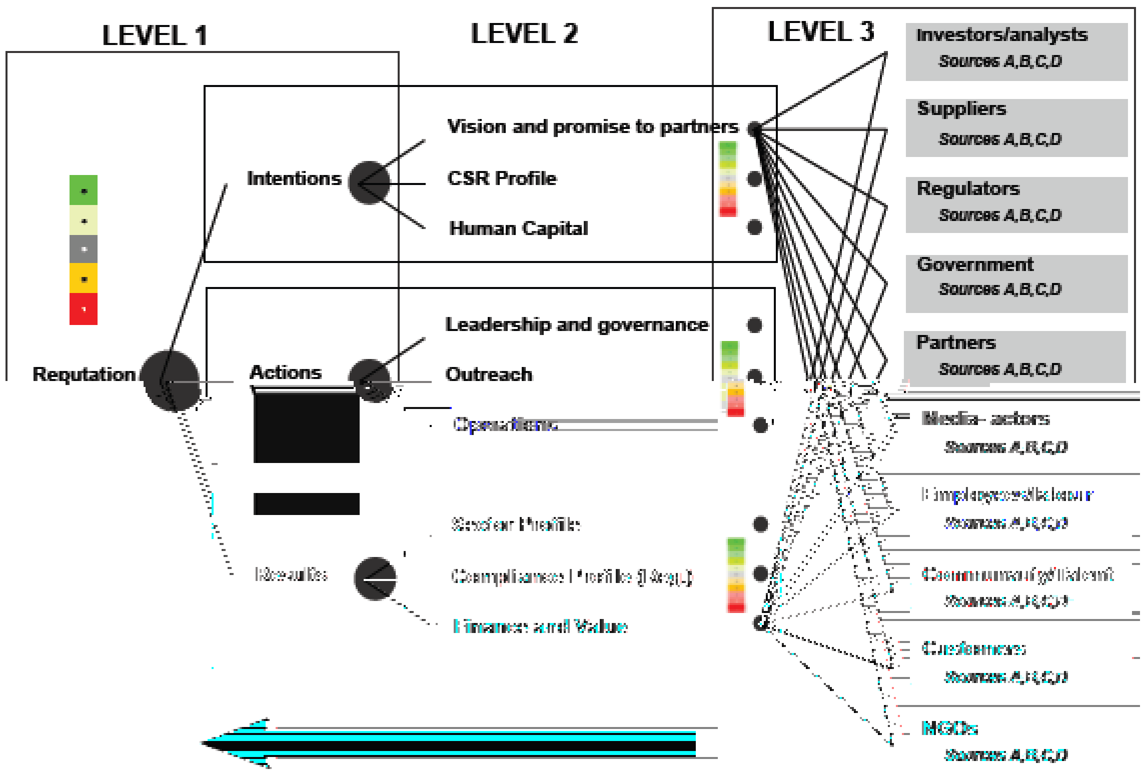


Figure 11: General model to build reputation index

3c. Practical implementation : challenges and benefits

Challenges

Time involved to evaluate 9 drivers through all 3 levels, for a variety of stakeholders

Instability of such assessments over time

Complexity : modeling and assessment of individual factor significance / pair-wise relativities induces

Benefits

Objective assessment of the nine drivers and an evaluation of the global reputation index for a firm

optimise resilience of the index given a given budget

How well would such a system fit into existing ERM?

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