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**Difficulties of valuation of Russian insurance companies in the M&A deal**

**A presentation to AEB event “Insurance and M&A”  
by Vladimir Novikov**

**27 October 2011**

**TOWERS WATSON** 

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- Technology and Administration Solutions
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## Talent and Rewards

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- Insurance Consulting
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- Risk Management

**Mergers and Acquisitions:** From target evaluation to integration implementation

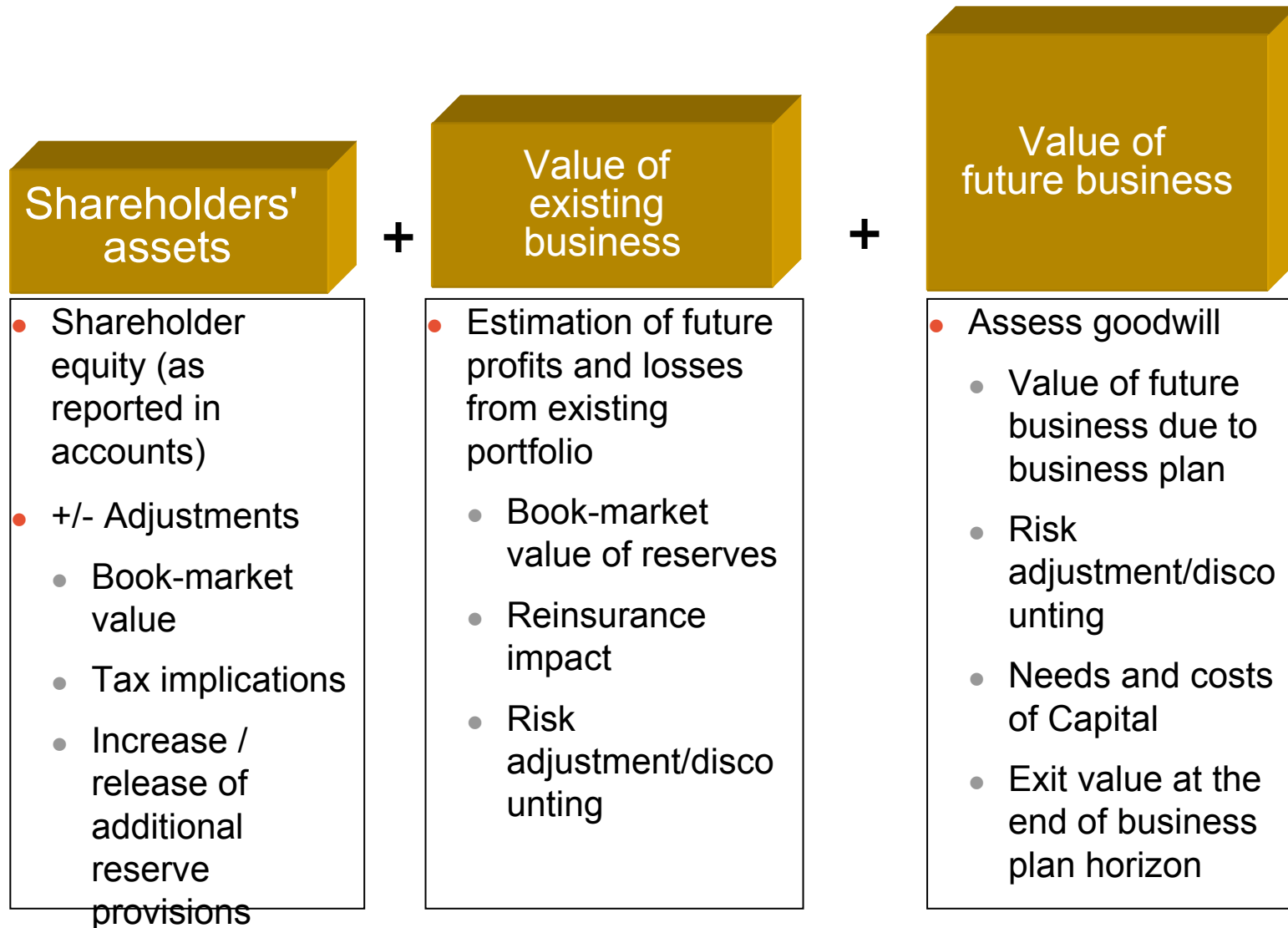
# M&A opportunities/needs in Russian market

- Long-term fundamentals
  - Large, fast growing, under-penetrated market
  - Improving business and regulatory climates
  - Potential for higher profit margins
  - Early mover advantage
- What do domestic companies need – value of partnership
  - Capital
  - Knowledge & experience
  - Brand

# Multidiscipline due diligence – central point of the deal

- **Strategic Due Diligence**
- **Operational Due Diligence**
- **Financial Due Diligence**
  - Actuarial valuation
  - Review of liabilities
  - Financial projections
  - Financial risk assessment

# Valuation of insurance company



## Shareholders assets - difficulties

- **Quality of assets**
- **Absence of basis for market valuation**
- **Volatile environment**
- **Price/ liquidity dependence**

## **Value of existing business - difficulties**

- **True profitability of major lines of business**
  - **Absence of pricing technique with good predictive power in mass market – CASCO, VMI, Household**
  - **High (and often out of management control) acquisition and operational expenses**
  - **Improper business metrics and risk monitoring**
  - **Hidden dividend policy**
  - **As a result – low or even negative return on capital ratio**
- **Simplified reserves calculation**
  - **Using only statutory method of calculation**
  - **Absence of liability adequacy testing/independent actuarial review**
- **Poor risk management**
  - **Price /underwriting/claims handling control and discipline**
  - **Absence of internal controlling/risk management procedure**
  - **Poor actuarial expertise**

## Value of future business - difficulties

- Common actuarial issues of valuation are applicable to Russian market
  - How much is one year worth?
  - How many years are valued?
  - What are the risks?
- But the main issue in Russian context is company's ability to achieve its business plan assumptions and targets:
  - Price levels, loss and expense ratios are assumed to be better than those which can be proved by statistical data,
  - Absence or limited access to market benchmarks,
  - Current level of risk management, corporate governance and actuarial expertise is not enough to ensure the fulfillment of business plan.



# Measures to improve value of Russian insurance company – potential M&A target

Should be implemented proactively

- **Strong Pricing policy**
  - Using advanced actuarial technique for crucial LOB
  - Discipline and enough power to change the rates
- **Modern reserving**
  - Application of several methods to reach best estimate
  - Regular Liability adequacy testing
  - Independent actuarial review
- **Asset – liability matching procedure**
- **Plan of reduction of expenses/ salvage and subrogation income increasing**
- **IFRS regular reporting (market valuation of assets)**
- **Sound ERM (enterprise risk management) system**
  - Optimal risk mitigation policy (including reinsurance)
  - Formal risk management procedure in place (E.g. similar to ORSA )

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