

2018 General Rate Application

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Agenda

1. Key Points
2. Basic Faces Significant Challenges
3. Prudent Fiscal Management is Key to Achieving Mandate
4. 2.7% Rate Request is Appropriate
5. Rate Stabilization Reserve
6. Information Technology
7. The Value Management Process
8. Expenses Favorably Impact the Rate Indication
9. Conclusion



1 – Key Points

Achieving MPI's Mandate



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Key Points

1. Basic insurance is vulnerable and faces significant challenges
 - Undercapitalized with a projected unsatisfactory financial condition
 - This puts ratepayers at risk of possible rate shock
2. The 2.7% rate request is appropriate
 - Management has taken action to reduce the ask on ratepayers
 - Driver Premium increase to demerit drivers reduces the ask on all ratepayers
3. Prudent fiscal management demands that the upper Rate Stabilization Reserve (RSR) target be established and Basic total equity be allowed to replenish with investment income
 - When Basic funds itself, it reduces risk for ratepayers and taxpayers





Achieving MPI's Mandate

MPI's Mandate is to provide universal access to affordable comprehensive auto insurance to all Manitobans

- Basic protects Manitobans from serious loss related to motor vehicles

This application puts Basic on a path to achieve long term rate stability for Manitobans

- Operational Excellence
- Strong financial condition for Basic is necessary to deliver on the mandate
 - Appropriate breakeven premiums
 - Adequate capital that protects ratepayers
 - Sound investment management practices



2 – Basic Faces Significant Challenges

Basic's Forecast Financial Conditions is Unsatisfactory

Basic Has Come to Rely on Transfers from Extension

Basic is Undercapitalized and Vulnerable

Ratepayers are at Risk

Basic Must Fund Itself



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Basic's Forecast Financial Condition is Un-Satisfactory

- The Lower RSR Target is the absolute minimum amount of total equity to achieve satisfactory financial condition
- Dynamic Capital Adequacy Test (DCAT) is a scenario test of Basic's capitalization
- The DCAT's model shows Basic maintains positive total equity with \$201 million in total equity at March 1, 2018, assuming
 - 1-in-40 probability level
 - Management Action (rebuilding fees and/or rate increases)
- 2017 DCAT Report finds the projected financial condition of Basic is not satisfactory



Basic Has Come to Rely on Transfers from Extension

- In the past three years, MPI has transferred \$176 million just to meet the minimum RSR
 - \$27.8 million in fiscal 2016/17
 - \$75.5 million in fiscal 2015/16
 - \$72.7 million in fiscal 2014/15
- MPI Board of Directors approves transfers, both the amount and timing
- The Board of Directors will explore options to restore the RSR to the optimal range, with no negative impact on ratepayers, once:
 - An adequate RSR range is established
 - There is certainty that total equity will not be rebated
 - Through a discount to premiums
 - If total equity is below the upper RSR Target





Basic is Undercapitalized and Vulnerable

- Basic insurance is not funding itself or its own reserve
- Owing only to transfers from Extension, Basic has subsisted at a minimum level of capital (lower RSR target) for the past three years
- The absolute minimum level of capital does not secure Basic's financial condition, or deliver stable rates to Manitobans
- Basic's vulnerability is not desirable or sustainable



Ratepayers are at Risk

- When Basic is operating at a minimum level of capital, the consequences of adverse financial results are more severe
- Rate stability is less attainable, given higher likelihood of rebuilding fees – over and above possible rate increases
- Combined effects of rates and rebuilding fees can result in Rate shock, which would damage Manitobans' confidence in public auto insurance.



Basic Must Fund Itself

- Long term sustainability depends on rates funding the cost of insurance and the reserve
 - Premiums must cover the costs of the benefits provided
- MPI's stakeholders, Ratepayers and Government, expect steady predictable rates
 - This means avoiding rebuilding fees and government bailouts
 - Not prudent to manage the business with the expectation of transfers from extension
 - Not prudent to set premiums below the cost of providing the benefits
- This approach consistent with AAP and makes good business sense

3 – Prudent Fiscal Management is Key to Achieving Mandate

The Facets of Prudent Fiscal Management
MPI Operations are Efficient and Effective
Basic Requires Adequate Capital Reserves
Basic Requires Appropriate Premiums



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The Facets of Prudent Fiscal Management

MPI is delivering on matters under our control:

1. Efficient and Effective Operations

This General Rate Application is key to establishing:

2. Adequate Capital Reserves
3. Appropriate Premiums





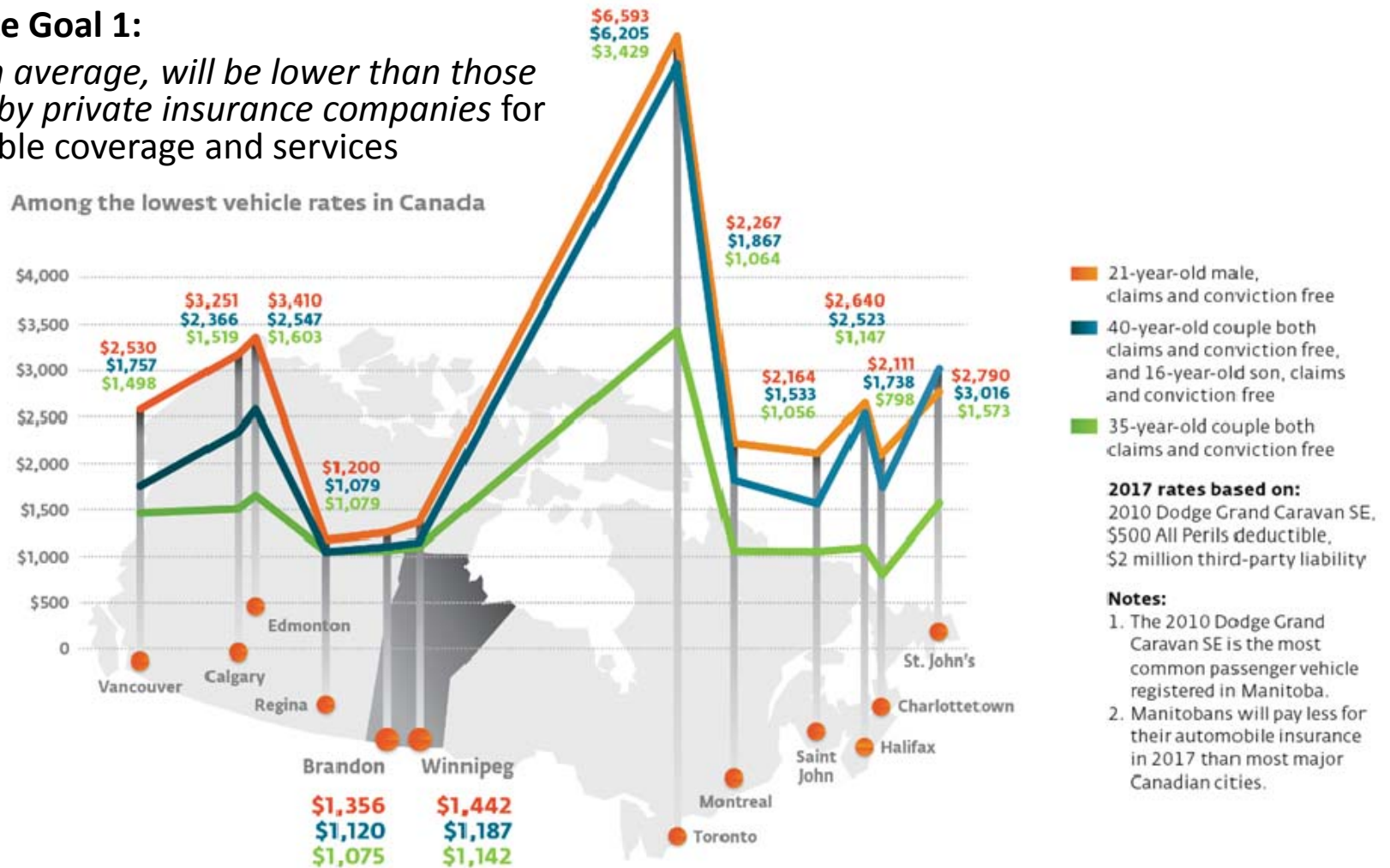
MPI Operations are Efficient and Effective

- 1.9% decrease in Total Basic Expense over 2017 GRA (rating years average)
 - Cost Containment is an ongoing priority, evidenced by many actions to reduce operating costs in the Budget
 - Stretch Target to achieve a flat budget
 - Zero base budgeting and review committee
- MPI's operations are efficient, as demonstrated by key benchmarking scores
 - Benchmarking results continue to show that MPI's business model is successful, and latest benchmarking results are favourable
 - Gross Expense Ratios beat the benchmarks, and continue to improve
- Achievement of Corporate Goals

MPI Operations are Efficient and Effective

Corporate Goal 1:

Rates, on average, will be lower than those charged by private insurance companies for comparable coverage and services





Basic Requires Adequate Capital Reserves

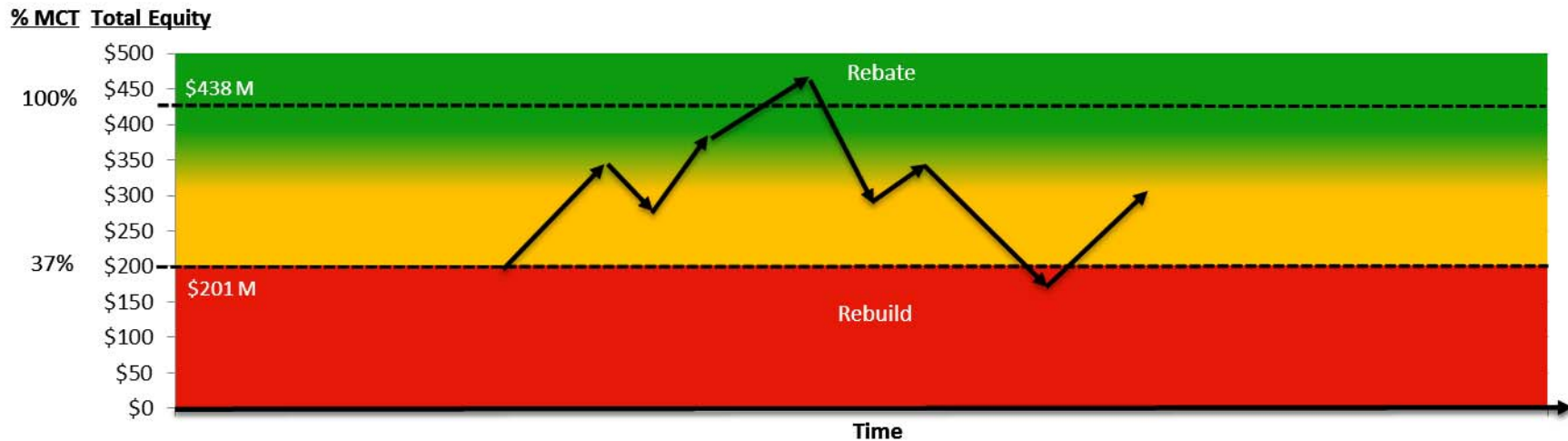
Section 18 of the MPIC Act

The corporation shall establish and maintain reserves in such amounts that, at all times, it has sufficient funds to meet all the payments as may become payable under this Act and regulations

- MPI Executive & Board of Directors must be able to meet their financial responsibilities and ensure an adequate capital reserve exists to meet its statutory obligations

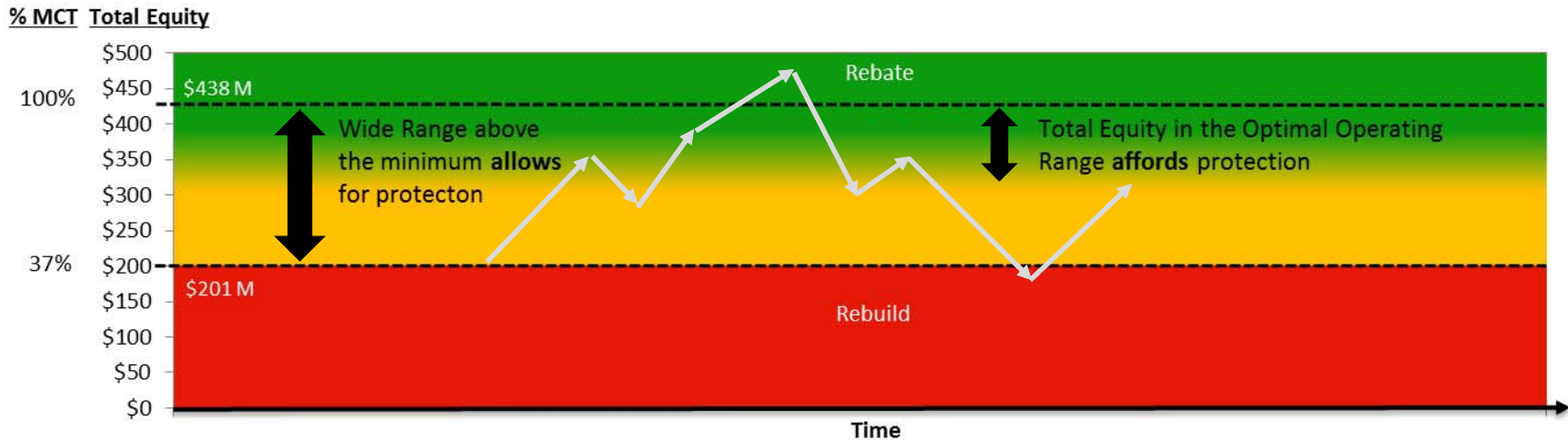
Basic Requires Adequate Capital Reserves

- The lower limit of the RSR defines the absolute minimum amount of capital required for Basic to withstand modeled adverse scenarios.
- The upper limit of the RSR defines the range
 - If total equity is below the range, action is required to rebuild total equity
 - If total equity is above the range, surplus capital is available for rebate
- When total equity is in the range, there is no ask of ratepayers



Basic Requires Adequate Capital Reserves

- At the **minimum level** of total equity (lower RSR target) Basic can withstand the modeled adverse scenarios – after “Management action” (i.e. rate increases and rebuilding fees)
- Operating above the RSR minimum promotes rate stability
 - RSR range needs to be sufficiently wide above the minimum to reflect variability in financial results, within reasonable limits
 - Total equity in the ‘optimal range’ affords the best protection from rebuilding fees





Basic Requires Appropriate Premiums

- Basic premiums are set in accordance with Accepted Actuarial Practice (AAP)
 - Using Best Estimates of costs and revenues (means without bias, neither conservative nor unconservative)
 - Basic Premiums are set to break-even with a zero profit provision

2620 Method

- .01 The best estimate present value of cash flows relating to the revenue at the indicated rate should equal the best estimate present value of cash flows relating to the corresponding claim costs and expense costs, plus the present value of a provision for profit, over a specified period of time.



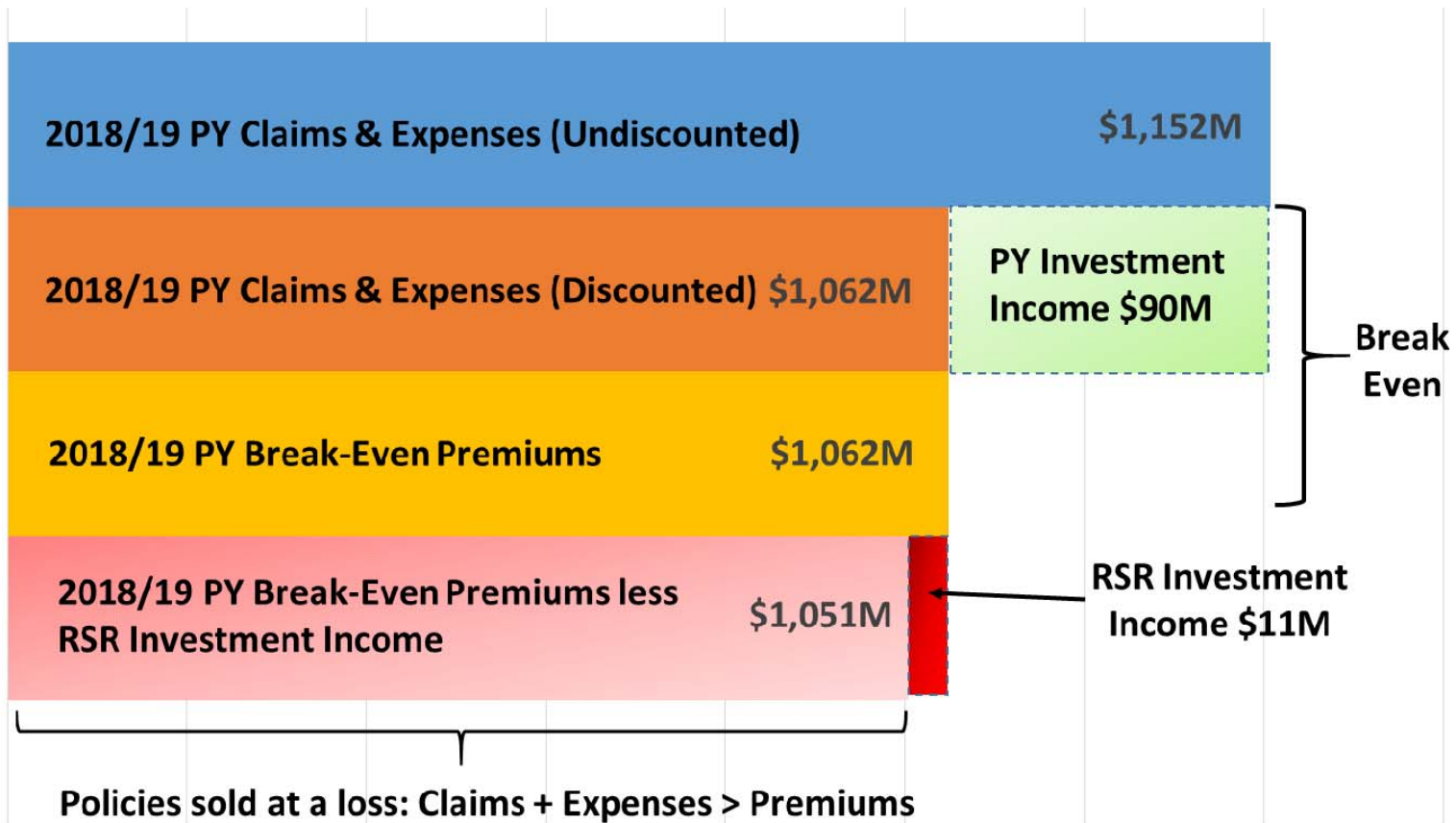
Basic Requires Appropriate Premiums

- Unlike Basic, other insurers (public and private) earn profit and/or have capital build/maintenance provisions to maintain and grow capital
- RSR Investment income is Basic's only remaining means of building total equity
- MPI's approach to rate making accounts for the circumstances of Basic and makes good business sense



Basic Requires Appropriate Premiums

- The *indicated rate* under AAP is the *best estimate* of the premium required to pay the cost of policies written this rating year





Basic Requires Appropriate Premiums

- Deducting investment income on total equity from rates would:
 1. Rebate funds to policy holders before Basic has enough capital for the RSR to be effective
 2. Rebate total equity that hasn't been earned
 3. Set policy premiums 'below cost'
 4. Impede the restoration Basic's total equity – growth in total equity relies on luck
 5. Increase the risk of rebuilding fees due to persistently low capital

4 – 2.7% Rate Request is Appropriate

2.7% Vehicle Premium Rate Increase

The Initial rate Indication

Management Action has Reduced Rates

Best Estimate Interest Rate Forecast Reduces Risk

AAP and Compliance Filing Reduce Interest Rate Forecast Risk



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2.7% Vehicle Premium Rate Increase

RM -1: Indicated Rate Change *

Line No.	Major Class	Current Average Rate	Indicated Average Rate	Indicated Rate Change
1	Private Passenger	\$1,057	\$1,086	2.7%
2	Commercial	\$755	\$765	1.3%
3	Public	\$2,003	\$2,025	1.1%
4	Motorcycles	\$775	\$796	2.7%
5	Trailers	\$72	\$80	11.4%
6	Off-Road Vehicles	\$12	\$10	-16.7%
7	Overall	\$816	\$838	2.7%

* As at the time of filing the 2018 GRA





The Initial Rate Indication

- The initial +7.7% rate indication is caused by increases in claims costs, a decrease in the assumed investment return, and the treatment of RSR investment income in rate setting.
- Claims costs (net of vehicle upgrade) are the main driver of the rate increase, contributing to approximately 6% of the 7.7% initial rate increase. The most significant claims related impacts from the 2018 GRA:
 - Continued collision severity growth > 5.0% per year
 - 2018/19 Hail forecast increased by \$12.0 million
 - 2018/19 Theft and Vandalism increased by \$7.5 million
 - 2018/19 PIPP forecast increased by \$6.6 million
- The decrease in the assumed investment return from the 2017/18 GRA (3.79%) to 2018/19 GRA (3.38%) resulted in a 0.80% rate increase.
- Not using the RSR investment income to reduce the rates in the 2018 GRA resulted in an additional 1.0% rate increase
- Non-claims related costs per vehicle (e.g. operating expenses) did not increase in 2018 and contributed to a 0.2% rate decrease.



Management Action has Reduced Rates

Initial forecast indicated:

7.7% required rate increase

Less Management Actions:

1.0% - Rodent Claims Strategy

0.9% - Physical Damage Claims Stretch Target

0.8% - Increased Allocation to Corporate Bonds

1.8% - Increase to DSR Premiums for Demerit Drivers

0.5% - Expense Reduction from Management actions (0.5%)

5.0% - Overall Management Action

Results in:

2.7% vehicle premium rate request



Management Action has Reduced Rates

New Rodent Claims Strategy

- Simplified repair process in line with Health Canada guidelines
- Cost per claim improved through: reduced labour costs, loss of use duration times, storage and towing costs, and total loss frequency

Stretch Targets for Operations and Claims

- Physical Damage Claims Stretch Target supported by:
 - Shop specific KPI's on estimating accuracy
 - All claims staff trained on estimating standards
 - Body shops trained on estimating standards
 - Shop relationship managers work with low performing shops



Management Action has Reduced Rates

Increase Allocation to Corporate Bonds Results in a 0.8% decrease in vehicle premium rate indication

- Achieved by:
 - Increase allocation from 5% to 18% of Total Portfolio
 - Increase 40 bps to fixed income portfolio
- Consistent with other public auto insurers, and is implementable
- Increased Target Allocation Subject to:
 - Approval of the Minister
 - Appropriate due diligence (ALM study will commence shortly)
- Taking on increased risk only makes good business sense with approval of:
 - Adequate upper RSR target
 - Rates that do not rebate investment income on total equity



Management Action has Reduced Rates

Increase to DSR Premiums for Demerit Drivers

- Changes to the Driver Safety Rating Scale will:
 - Generate \$17.5 million in revenue from high-risk demerit drivers, offsetting 1.8% vehicle premium increase
 - Make price of insurance more reflective of the driver risks
 - These costs are avoidable with good driving behavior
 - No premium increase with a clean year of driving for transition year
 - Affordability is maintained through financing program
 - Increase is expected to positively influence driver behavior



Best Estimate Interest Rate Forecast Reduces Risk

- Best Estimate forecast:
 - For rate setting, use 10 Yr GOC naïve interest rate forecast (actual market data as at November 30th)
 - Simple, clear, objective, market based forecast with high predictive power
 - Reduces Interest Rate Forecasting Risk with a 3 month forecast horizon
- Compliance Filing Proposal has no impact on due process:
 - Revenue requirement tested and approved by the PUB
 - Interest Rate forecast is outside MPI's control
 - Final rate indication updated and approved through compliance filing





AAP and Compliance Filing Reduce Forecasting Risk

- Increase in interest rates since filing has reduced the rate indication from 2.7% to 2.0%
- Further interest rate movement prior to November 30th will be reflected in the compliance filing

Line No.	Change in Claims Discount Rate	Claims Discount Rate	GoC 10 Yr Bond Yield	Rate Indication	Change in Rate Indication
4	-25 bp	3.53%	1.33%	3.2%	0.1%
5	-20 bp	3.58%	1.39%	3.1%	0.1%
6	-15 bp	3.63%	1.45%	3.0%	0.1%
7	-10 bp	3.68%	1.51%	2.9%	0.1%
8	-5 bp	3.73%	1.58%	2.8%	0.1%
9	Current	3.78%	1.64%	2.7%	
10	+5 bp	3.83%	1.69%	2.6%	-0.1%
11	+10 bp	3.88%	1.75%	2.5%	-0.1%
12	+15 bp	3.93%	1.82%	2.4%	-0.1%
13	50/50: +19 bp	3.97%	1.87%	2.3%	
14	+20 bp	3.98%	1.88%	2.3%	-0.1%
15	+25 bp	4.03%	1.94%	2.2%	-0.1%
16	+30 bp	4.08%	2.00%	2.1%	-0.1%
17	+35 bp	4.13%	2.06%	2.0%	-0.1%
18	SIRF: +38 bp	4.16%	2.10%	1.9%	
19	+40 bp	4.18%	2.12%	1.90%	-0.1%
20	+45 bp	4.23%	2.19%	1.80%	-0.1%
21	+50 bp	4.28%	2.25%	1.70%	-0.1%



5 - Rate Stabilization Reserve

Lower and Upper Targets have Distinct Purposes

Lower Target – Minimum Capital Level

Upper Target – 100% MCT is Prudent

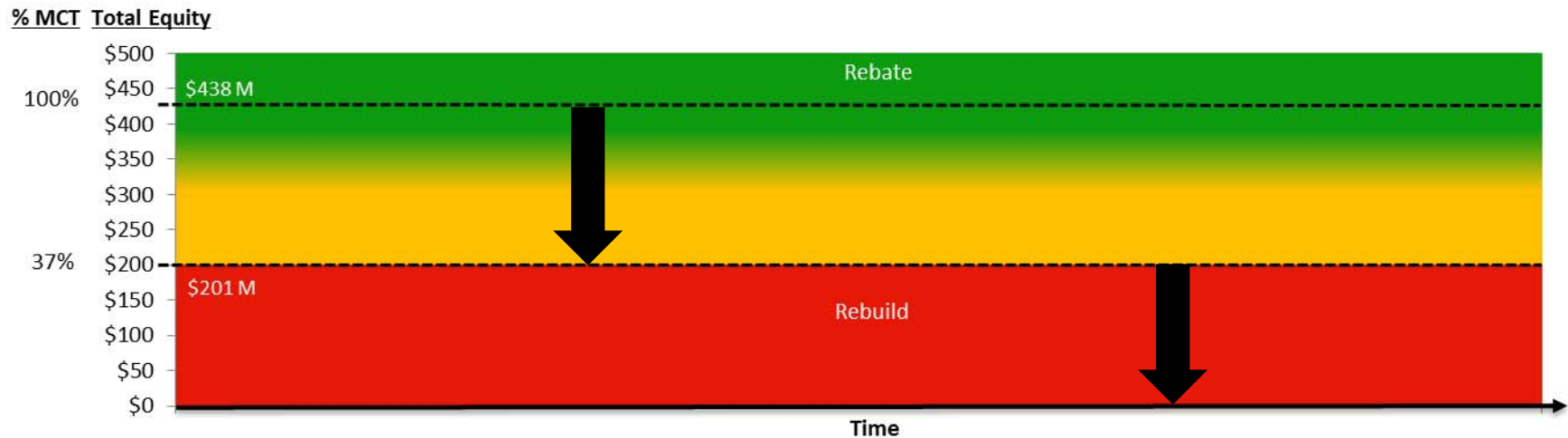
DCAT Based Upper RSR Target



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Lower and Upper Targets Have Distinct Purposes

- DCAT based Lower RSR Target is the absolute minimum capital requirement after management action
 - Test is exhausting total equity
- Upper RSR Target is required to avoid rebuilding fees and maintain capital above the lower RSR Target





Lower RSR Target is Absolute Minimum

- \$201 Million for 2018/19 to withstand modelled adverse scenarios
 - Flows from the collaborative DCAT Process
 - Methodology remains the same
- Lower RSR Target is based on a 1-in-40 year risk tolerance including management action
 - This means, Basic would expect to deplete a 2018/19 RSR balance of \$201 million once every 40 years even after rate increases and/or rebuilding fees
 - Management actions in terms of combined rate increases range from 2% to 12 % depending on the adverse scenario

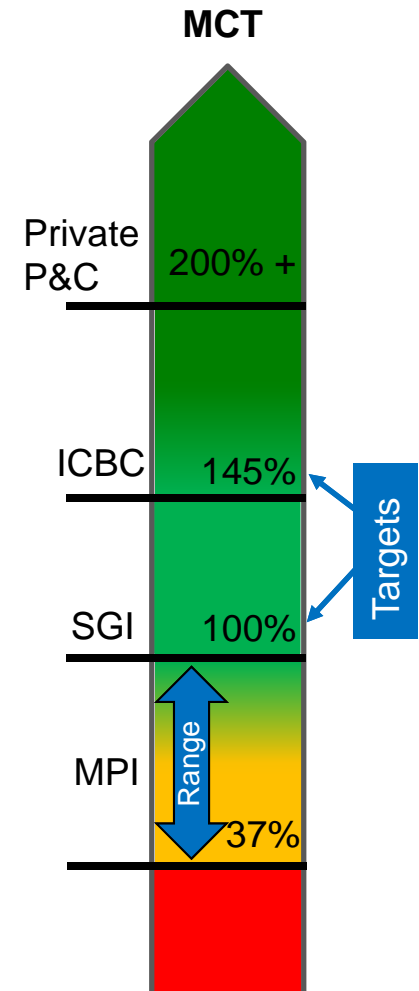


\$438M Upper RSR Target is Appropriate

- \$438 Million was determined based on 100% Minimum Capital Test (MCT)
- Minimum Capital Test (MCT) the appropriate test because it:
 - Is an industry standard capital adequacy test
 - Considers the risks facing Basic insurance
 - Provides objective assessment, relying on the breadth of information available to OSFI
 - Provides comparable measure to other public and private auto insurers
 - Capital Required is determined using evidence based test, based on MPI's balance sheet

\$438M Upper RSR Target is Appropriate

- “100%” is the appropriate MCT ratio the Upper RSR Target because:
 - Provides wide enough RSR range, but still below all other insurers (private and public)
 - Tailored to the circumstances of Basic insurance and the RSR Framework
 - At that level Capital Available is equal to Capital Required
 - Capital in excess of the amount required is available for rebate



\$438M Upper RSR Target is Appropriate

The applied for Upper RSR Target is also supported by the adapted DCAT analysis:

- The relevant consideration for the Upper Target is whether capital may fall below the Lower Target, not falling to zero
- DCAT analysis indicates that over a 3 year period an upper RSR target of \$442 million is appropriate

Line No.	Starting	3 Year Combined Scenario before Management Action	
	RSR Balance February 28, 2017	Probability	Total Equity < \$239M (37% MCT) in 2020/21
1	\$181M (29% MCT)	68.11%	1 in 1.5
2	\$200M	62.64%	1 in 1.6
3	\$250M	47.25%	1 in 2.1
4	\$300M	32.17%	1 in 3.1
5	\$350M	18.96%	1 in 5.3
6	\$400M	9.09%	1 in 11.0
7	\$438M (100% MCT)	4.67%	1 in 21.4

6 - Information Technology

IT Initiatives Have Many Drivers
The IT Strategy Drives Initiatives
CIO Scorecard Tracks MPI's Improvement
IT Staffing Strategy is Effective



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IT Initiatives Have Many Drivers

- Drivers for IT projects:
 - Strategic Planning
 - External Events (non-discretionary)
 - Societal Changes (limited discretion)
 - Technical Requirements (Non-discretionary)
- Regulatory Process and non-discretionary IT expenditures are developed on different cycles
 - Vendor releases and security updates are not always known at the time the forecast is prepared



The IT Strategic Plan Drives Initiatives

- IT Strategic Plan is contingent on Corporate Strategic Direction
 - Board of Directors is in a period of transition to develop the corporate strategic plan
 - IT supports the business, so the business direction must be set
 - Refine the value management process, and implement with a higher level of discipline
 - 2016 GRA IT Strategy remains the relevant tactical plan





CIO Scorecard Tracks MPI's Improvement

- CIO Scorecard provides an independent assessment of MPI's progress in Information Technology
- This assessment is done annually, and Mr. Geffen spoke to the Scorecard at last year's Hearing
- This year's scorecard, which Mr. Geffen will speak to, shows that MPI continues to make progress on several fronts:
 - Nearly all projects are delivered on time and on budget
 - MPI's IT Spend as a % of Operating Expense has decreased 4.5% over the last 5 years
 - MPI continues to improve its Maturity (3.9% over 5 years) driving effectiveness



IT Staffing Strategy is Effective

- Progress continues on the conversion of consultant roles to internal staff
 - 27 positions between 2016/17 and 2019/20 for \$2.4 million in annual savings
- 15 positions have been transitioned, up from 11 projected
 - Accelerated benefits realization in 2017/18

Figure IT- 9: 3.2 External Labour Strategy: Updated Projection

Line No.	Year/Net Cashflow	2016/17	2017/18	2018/19	2019/20
1	External Labour Adjustments	\$0.0M	\$0.6M	\$2.0M	\$2.4M

7 – The Value Management Process

Is Maturing
Is Thorough
Will Demonstrate Results



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Value Management Process is Maturing

- MPI's Value Management Process (VMP) is evolving, and improving over past practice
- Stronger support and decision making around initiatives
 - Being normalized throughout the corporation
- Consistent approach to demonstrate benefits
 - Adopting better ways of measuring and tracking value from initiatives





Value Management Process is Thorough

- VMP is a multi-part process with an iterative approach:
 - Thin Business Case - vetting by Management
 - High level concept, define need, project description, benefits and objectives
 - Iterative development of qualitative and quantitative elements
 - Detailed Business Case before final approval
 - Financial Analysis: costs, benefits and assumptions
 - Full documented business case
 - Business Transformation Office has accountability for IT project delivery
 - Applies an established project delivery methodology
 - Projects will be subject to Post Implementation Reviews

10 – Expenses favorably impact the Rate Indication

Material Reductions in Operating Budget
Key Assumptions and Actions



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Material Reductions in Operating Budget

- Material reductions in Operating budget (average of rating years):

Figure EXP-1: Expense Comparison – 2018 vs 2017 GRA Rating years

Line No		2018 GRA Avg. of Rating Yrs	2017 GRA Avg. of Rating Yrs	Change (2018-2017)	Change (Percent)
1	<i>(C\$ 000s, rounding may affect totals)</i>				
2	Basic Allocated Corporate Expenses				
3	Claims Expense	138,863	137,290	1,573	1.1%
4	Road Safety/Loss Prevention	13,019	14,140	(1,121)	-7.9%
5	Operating	75,195	83,146	(7,951)	-9.6%
6	Regulatory/Appeal	4,175	3,604	571	15.8%
7	Total Basic Allocated Corporate Expenses	231,252	238,180	(6,928)	-2.9%
8	Basic Direct Expenses				
9	Commissions	41,658	41,017	641	1.6%
10	Premium Taxes	32,595	32,353	243	0.7%
11	Total Basic Direct Expenses	74,253	73,370	883	1.2%
12	Total Basic Expenses	305,505	311,550	(6,045)	-1.9%





Key Assumptions and Actions

- Reducing FTE counts by 6.9% (133 FTE) by fiscal year end 2019/20 compared to the 2016/17 budgeted amount
 - 15% reduction in management FTE to be achieved by December 2017
 - Zero per cent general wage increase for management personnel in 2017
 - Zero merit increases for management personnel in 2017
 - Elimination of one management layer in 2017 and flattening of the management organizational structure
- \$2.6 million stretch target in 2017/18 and beyond
- Special Service expenses reduced by ~\$1 million in 2017/18 and beyond
- Reduction of overall building expenses throughout the forecast
- Reductions in sponsorships and low return road safety messaging with further reductions being considered
- Zero percent growth (no CPI) built into the forecast for 2018/19 and 2019/20

8 - Conclusion



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Conclusion

1. Basic insurance is vulnerable and faces significant challenges
 - Undercapitalized with a projected unsatisfactory financial condition
 - This puts ratepayers at risk of possible rate shock
2. The 2.7% rate request is appropriate
 - Management has taken action to reduce the ask on ratepayers
 - Driver Premium increase to demerit drivers reduces the ask on all ratepayers
3. Prudent fiscal management demands that the upper Rate Stabilization Reserve (RSR) target be established and Basic total equity be allowed to replenish with investment income
 - When Basic funds itself, it reduces risk for ratepayers and taxpayers