

RECORD, Volume 29, No. 1*

Washington, D.C. Spring Meeting
May 29–30, 2003

Session 30PD Special Risk Management Issues For International Operations

Track: International

Moderator: REJEAN S. BESNER
Panelists: KATHERINE A. ANDERSON
SIMON R. CURTIS
DAVID INGRAM

Summary: Companies operating in international markets have additional issues to consider from a risk management point of view. Fluctuations in exchange rates, political and sovereign risks, regulatory issues, capital management and human resources considerations are among these. This session gives attendees the opportunity to understand how multinationals currently deal with these issues and how they are functionally structured to handle the risk management process.

Attendees gain considerable insight into the way that multinationals manage the special risks created through foreign operations. The session helps them understand the approaches, processes and tools used to ensure that risk management procedures for foreign operations are as strong as those used domestically

MR. REJEAN BESNER: I'm chief actuary with the International Reinsurance Division of Transamerica Re based in Charlotte. Insurance is becoming more of a global business, but, at the same time, entering and working in different markets brings a number of considerations in terms of risk management that are very different from your domestic business.

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Note: The chart(s) referred to in the text can be found at the end of the manuscript.

I am very pleased that we have a panel that has tremendous experience in working in other markets and dealing with such issues. We're going to start with David Ingram. David is a consultant for Milliman and David is going to talk about the subject more from a broad perspective. He will also touch on more developed markets, such as doing business in Europe. Then we'll follow with Simon Curtis from Manufacturers Life. He's going to talk specifically about the company's experience in Asia. Finally, Kathy Anderson from ING will give us a perspective on doing business in Latin America.

MR. DAVID INGRAM: I'm going to start with a broad discussion about risk-management culture and how important that is to an international operation, as well as giving a case study of how one international company conveys their risk-management culture throughout their organization and the aspects of their culture that they find important to them. Then I'm going to do a quick overview of international issues. Finally I'll talk about a few developed country risk-management issues.

We want to talk about risk-management fundamentals. You have to start by thinking about the culture of risk management. I'm going to define the risk-management culture ideas. Then I'll talk about the development of a company set of risk management best practices that can be used as a device to communicate the risk-management culture throughout the organization, and also emphasize the particular importance of this to an international organization that crosses many lines.

First of all, what is the culture of an organization? Well, it really is the shared thoughts and beliefs, that is, the idea that the organization has about what they are. There are certain kinds of statements you can ask people at the company that has a strong culture to complete and you'll get the same or very similar answers. Examples of these statements are, we always do this, or we're really good at this, or we would never do this. If you go to a company and ask those questions and get very different answers, then they have a fundamental problem in the fact that they haven't communicated their culture in any way throughout the organization.

Culture includes all the different ideas and aspects of the company. The company may have a culture saying in sales. "We always grow our sales at least five percent" was one of the cultural icons at one of the companies I was at. Culture includes what kind of product lines we'll be in, where we want to position ourselves on financial ratings and so on. All those things involve the culture of the company.

What I'm calling the risk-management culture incorporates the idea of financial strength, or the risk of insolvency, or the exposure to earnings volatility. Not necessarily all those things; a company may focus their risk-management culture around just one of those things. But a risk-management culture involves the

awareness of risk and the importance of risk management at all levels. It means embedding those risk-management ideas into every decision as a second nature.

When you say those things to people that haven't experienced a risk-management culture at all, you kind of get a blank stare. They wonder how could you possibly move from where they are to doing that. I've been around long enough that I've seen several regimes of expense management pass through companies that I've been in. What happened when it became expense-management time is that the company strengthened its expense-management culture. What it did was try to get everybody in the company to think about all the decisions in terms of how much does it cost, and can we achieve the same objective at a lower cost. You have a lot more reports about expenses. In some places, they beat people up over their budgets once a month, and there was something in the bonus program that had to do with expense management.

Now, is there anybody who has not been in a company that's had all those elements? That's what I'm calling an expense-management culture. A risk-management culture would be to take the exact same elements and feed them through the company decision-making process. Whenever you're looking at a new decision, you think in terms of being able to clearly articulate how much risk it creates, and if the same objective is achievable with a lower risk. You would also frequently track those risks and treat those risk-management reports as an integral management tool. If you go over the risk exposure limits that you have, you're called on the carpet and asked to explain it; the same way you'd be called on the carpet in an expense-management culture to explain budget variances. Also, part of your bonus structure will be focused around risk management.

What are the particular aspects of that risk-management culture beyond those kinds of awarenesses? I've got a sample set of statements about risk management developed by some Milliman consultants in the United States and the U.K., who are working in risk management. They looked at the different risk-management best practices in banking and added, from our own experience, best practices from insurance.

I'm going to give you a set of a dozen risk management best practices for insurance companies that you can use to build and strengthen a risk management culture.

1. Board and senior management are responsible for risk management.
2. Senior management understands all firm activities and understands the basis of the risk-management system.
3. Authority and responsibility are clearly defined and risk measurement and management are independent from the risk taking function.
4. All material risks are identified and measured. Exposures are aggregated and management attends to the largest exposures.

5. There are risk limits for all material risks and a system for enforcing the limits is part of an internal control structure that is relevant to the risks of the firm.
6. The firm has staff with sufficient expertise to perform the risk-management functions and adequate systems support.
7. Risk surplus is allocated to business units and products and is used for capital budgeting purposes.
8. Stress testing is a part of the risk-management process.
9. New products and ventures trigger consideration of potential new risks and new risk-management procedures.
10. Financial reporting allows management to view the risk-adjusted returns of business units, products and activities.
11. Product pricing and rate setting reflects the risk-adjusted return.
12. The firm has a process for quickly resolving identified risk management weaknesses.

Those could be applied to any company in any business in any country. But, with international companies, risk sometimes comes across as the great unknown. I won't tell you which chief financial officer (CFO) said this, but I was told, "I want a list of the 20 most significant unknown problems on my desk by 8 a.m. tomorrow." The risk management paradigm is a way of getting you prepared for that request.

What you want to be able to do through your risk-management culture in an international operation is to understand the approach, the risk taking and risk controls in each territory that the company operates. Companies will have different approaches for what they want to do in those areas. Some companies want uniformity throughout the world. They want every operation in every country to have the same idea about risk taking and the same idea about controls. Other companies will tailor their operations to particular markets, and try to figure out the way that you do the best in each market. They want to know what the risk taking approach is and what the level of controls are in each market so that the corporate area can be aware of what's going on that way.

You have to be able to understand where you would place each of your operations on a grid so far as whether they're lower orientation or higher orientation towards risk taking, and lower or higher orientation towards control. By putting different operations on that grid, you'll be able to figure out where to focus your attention. Clearly, if anybody turns out to be a low control orientation and high risk taking, you want to spend some time with those people. People that are low risk taking and high control orientation, you may want to spend some time with them also because you may find that they have trouble meeting their business objectives if they're not taking any risk and they're controlling them an awful lot. There are things to think about by putting your organization on this kind of a grid.

When you think about this, you also think about the corporate area of the parent company as to risk and control style. Is it the same within each business unit within the home country of the parent company? Are there different risk and control styles in the various markets and industries that you're participating in? You also look down at the personalities of the people you have in management in each of the companies. You want to look at that risk and control style as well.

I'm now going to give an example of how one company incorporates a risk-management culture throughout their worldwide operation. It's a large diversified company. I've been asked not to mention their name directly here. The risk management at that company is a very strong fundamental value. They have a risk-management system that they apply in the same way in each territory and they have a risk-management review of any new initiatives. They actively work to make sure that they keep their risk-management culture alive and growing.

In their risk-management system they have what they call limits and flags. The limits are risk limits for every different kind of risk that each business unit has set for them each year. They have to operate their business within those limits during the year, track them on a timely basis within the year and publish reports of their status relating to the limits. Those reports are widely distributed not just within their own business unit, but also within other business units, and are available to the risk managers of the other business units as well.

The risk limits are created at a fairly low level within a business and within a country. The risk limits roll up so that if there's a credit risk in this business unit and there's a manager that's in charge of two business units, he will have a credit limit that is the sum of the credit limits for the two units below him. It will roll all the way up to the president of that company, the division managers at the parent company and so on and so forth. Everybody up the chain of command has these risk limits, and everyone is evaluated, in part, on how they stay within those risk limits. One of the things that's done during their planning process every year is to re-evaluate those limits and decide whether they're going to continue operations at those limits, expand them or contract them.

The other part of their risk management system is something they call flags. The flags include a very macro level of risk in each business, including local regulatory risks, political risks and the regular kind of credit market underwriting risks that you see as the fundamental financial risk. They have flags for their portfolio quality and flags for business performance. Annually, they review those flags and that is the information that they used to update the risk limits that are set for each area. Whether or not one of the flags has been raised that year will influence the decision-making on how to renew the limits.

When a new initiative is proposed within a business unit in any part of the world there is a 10-step process, and this same 10-step process, instead of reports to

develop, forms to fill out and so on, are practiced everywhere in the world for getting approval for a new project. The approval has go/no-go checkpoints. Every one of those 10 steps is not a go/no-go checkpoint. I think there are three go/no-go checkpoints within that 10-step process, and one of them is a business review at a local level.

There's a risk-management review at a local level and then a corporate sign off. I don't know exactly what the size of the project consideration is for going to corporate, but a very high number of projects throughout the world are submitted for corporate review. An important part, at the very earliest stages, of this 10-step process is the identification of the risk measures and proposed risk limits. The risk-management actions that will be taken, such as hedging and reinsurance, are also important.

Before the company commits resources to developing a new project, such as a product or a new marketing system, it has to identify the way in which the risks are going to be managed. It's quite a contrast to an experience I've had within a company where the risk review was done after the marketing material was printed.

The review committee for the business-level review in each country would consist of a number of people including the chief actuary, the chief risk officer, the CFO and the chief marketing officer. Most of these things are new products. When I worked on new product committees, I was usually the one financial representative. It was 10 marketing people and me. Now there's only one marketing person on that company's committee, and it's all financial people otherwise. So it ends up being the marketing person convincing the financial people that the new initiative should be going forward.

Installing this risk management process is an integral part in each acquisition that the company does. They plan on doing a first-stage installation of their risk management process within 90 days of acquiring any new business or company. One of the first things they do is establish a risk-management officer position. The second thing they do is give that person the password to get onto an Intranet site where they have stored all the risk-management reports that all the other business units have been developing and all the templates for all the reports that are needed to be presented for all the new initiatives. In addition to those Web sites, which are really a kind of self-study course in the company's risk management culture, they do have global risk officer meetings where they get together and share their recent triumphs and problems in fulfilling their jobs.

There is a flow chart of the structure that supports this process. You have the chief risk officer, who has dotted-line relationships with the risk officers in each of the profit centers within a business unit.

There is also a list of the different things that are done by different levels of people in the organization supporting the risk management culture.

In international risk management, there are many issues, such as macro economics, changing markets, regulation, financial reporting, currency, control, communication, limited data, ostrich thinking on some major risk, expertise and staying power/time frame.

I have been asked to talk about developed country risk. Macroeconomics risks are not usually thought to be significant in the developed countries, but several developed countries (aka the EU) have been creating some macro uncertainty with their creation of a new currency. The exchange rates of the dollar to the Euro have gone from 110 percent down to 80 percent, up to a 120 percent where it stands now. Those kinds of jumps in major currencies can cause disruptions. I don't think anybody has any idea of how that's going to settle out and how that exchange rate will evolve over time. Those fluctuations affect markets and marketing efforts as well.

In addition, regulation is usually pretty stable in developed markets, but right now, particularly in Europe, regulation is evolving rapidly. The insurance regulators in Europe are often hand-in-hand with the bank regulators if they aren't the same people, and they are working to bring the regulatory systems for the two parts of the financial services industry together. That will mean major changes for the regulatory paradigm for insurance companies and we're waiting to see how that's going to emerge.

Developed country financial reporting is under tremendous flux as well with the EU leading the charge to international accounting standards. The stability that you would historically think of in developed countries is much less evident right now. Another thing in relation to financial reporting is that there are new capital requirements. The EU capital requirements were very simple. It was a percentage of face amount and a percentage of reserves. Currently, the EU regulators are trying to move away from that, and exactly what they're moving to is not settled yet. That puts a real kink in the process of trying to figure out how to put together long-term business plans because you don't know what the real capital requirement is going to be.

Finally I am going to mention currency risk in developed markets. I believe it's a pretty common practice in international companies to try to project expected profits and hedge that amount in the base currency of the company. That works well. However, I've seen some issues with companies that are trying to list in EU and U.S. stock exchanges, and they cannot hedge in both directions at once so they end up with currency risk in the financial reporting due to the instability of the relationship with the dollar and the Euro.

The other issue I've heard from people who have worked in subsidiaries of international organizations is that one of the things that many companies don't think to do is to hedge expected future capital contributions. I've heard the story more than once from people who are working for subsidiaries saying, "We were supposed to get X amount of capital next year, but the currency exchange rates moved and we're going to get X divided by three." That's another concern in risk management in international companies.

MR. SIMON CURTIS: I'm going to focus my remarks on Asia. I'm also going to focus my remarks from the perspective of the corporate center of an international insurer because that's where my experience is. I'll be giving information on managing international operations and risks from the perspective of the people in the head office.

I'm going to start by giving you a brief overview of where ManuLife does business, what our products are and what our risk is. I'm going to give you this information so that when I get into Asia there's some context as to some of my remarks, the importance of that business and managing it appropriately.

ManuLife does life business and a number of different product lines in a number of different territories. Effectively, we have a fairly complex set of products and portfolios to manage worldwide. We're very active in really three geographic areas: the United States, Canada and Asia. In each of these areas we have a fairly wide range of products, ranging from individual life through to variable annuities, traditional annuities, group products and we have a very big reinsurance operation, which is a retro reinsurer that does business worldwide, although largely based from the United States.

ManuLife really doesn't have a single home geography. We really are a four-legged stool if you count our reinsurance. We have about 35 percent of our income coming from our U.S. operations. Our next biggest would be our Canadian operations with about 27 percent of our income. We are Canadian domiciled but, as you can see, it's not our dominant geography.

Interestingly, our Asia operations are as big as our Canadian operations. So when we talk about international operations at ManuLife, you could argue that we're talking about over 70 percent of our operations being international versus our home territory. If you consider North America more as a home market, we're still talking about having 26 percent of our income, a quarter of our balance sheet and income, coming from operations in Asia. So it is a very key market to us. It's very important, therefore, that we have very good controls and understanding of those markets, and have a very good process for doing business in those markets.

In terms of types of business and where our income comes from, we are also diversified. Although we're predominantly an individual life company, we have pensions operations, group life and health, annuity operations and reinsurance operations. I should make the point that, probably similar to many other companies, those savings and pensions operations were considerably bigger two years ago before equity markets started going down. So we have quite a geographic diversification and also have a diversification by product line in these various territories.

ManuLife has been in Asia a long time. We've been there, basically, for more than 100 years, primarily focused on Hong Kong as the primary hub for our operations. But we have been in and out of many other countries over that time. So we have quite a history of operations in Asia. Today, we're present in eight countries, and of those eight territorial operations four of them have been founded within the last 10 years. We've had a historical presence, but we've also been growing it quite strongly in the last 10 years. If you talk to people in Asia, people probably would think of us as one of the top three in terms of multinational insurers with a presence in Asia. It's a big part of our balance sheet, and in terms of the Asian market, we're a big international presence.

We don't do business in Europe, Latin America and other territories. That is actually a conscious decision. One of the key issues is in terms of being able to manage the business. We are very conscious that, as an organization, we want to be disciplined and able to keep control of our operations. We want to stay focused in where we do business. And, although we would like to, at one level, be a worldwide company, we really feel that it's a much better for us to actually focus on specific geography, such as Asia, and grow those rather than try to move into other markets.

One of the important things about being an international company is to stay disciplined. There's a real temptation to start looking around and say, "Well, that would be a neat place to go and this would be a very interesting opportunity today." But, you have to stay focused and do what you're good at. You really need good people on the ground, which is another reason for us focusing on Asia. We have an in-built advantage, which is that we have people on the ground there to actually grow those operations. We're growing from a strong base. In terms of just our Asian operations, we have over 20,000 agents across the region and manage 22 billion Canadian dollars, which is probably around 15 billion U.S. dollars.

In terms of where we do business, the hub of our Asian operations is in Hong Kong. Basically, all of our Asian operations except for Japan are run out of a regional office in Hong Kong. We operate in China, Vietnam, Philippines, Indonesia, Singapore and Taiwan out of Hong Kong, and have a stand-alone Japan operation.

The only territory that is relatively new to us is Japan, where we entered about three or four years ago through buying into a mutual company that was,

effectively, going insolvent. So like many North American insurers we made a deal with one of the struggling Japanese mutual companies. All the other operations, effectively, been grown from scratch.

So now I will talk about risk in Asia, and many of the comments that I'm going to pass on today were taken from a presentation that our Asian GM did about a month ago. These reflect his comments and my addition of some comments from our corporate perspective. There are several key challenges that we believe we face in Asia.

The first is really a strategic and competitive challenge. There are always a number of competitors or other companies trying to enter many of these countries because they're quite attractive. So strategically and competitively, one of the key issues is to keep an eye on your competition. Not only in terms of them taking market share, but also as new entrants into territories. Often, the way they try and enter the market is by basically stealing management talent and staff away from existing companies. One of the key risks that you see in Asia is that if you lose a senior manager in an operation, they can take a large portion of the staff and agents with them. In Asian territories, there's often tremendous loyalty up through certain management people. So you have a bit of a risk there in terms of losing almost whole sides of operations to competitors if you're not careful.

Strategic risk, again, is this temptation to try and continually expand and go into all markets and all territories. The issue is to be strategically disciplined and choose where you want to do business. I can't emphasize that enough. The successful companies in Asia are those that, perhaps, grow more slowly. They grow slowly in terms of trying to expand geographically and get into all the different businesses, but they focus on certain territories and businesses and grow those. They don't become flag planters trying to set up operations everywhere at once. Eventually, most of those companies don't succeed and end up withdrawing from a number of the territories that they go into at tremendous financial cost.

A second key risk is reputation and political risk, and I'll have a very interesting example of that later on, which has received a lot of publicity in the United States and elsewhere. You're exposed to pressures and situations in Asia through the judicial system, the legal system and the government system that you just wouldn't encounter in North America. Business decisions and your ability to do business are often influenced by factors well beyond your control.

The third area is regulatory risk, which I'll come back to later.

Asset mix and asset risk make up the fourth risk. Assets can be a real challenge in Asia that I will discuss later on.

Currency is an issue, and David touched on that. Managing exchange rates and trying to determine what is the right currency strategy to follow is always a bit of a challenge. From our point of view, we always currency match our liabilities, but the currency to hold your surplus assets in is always an interesting question.

Physical security is a big issue in some of the territories where we do business. We have a very big operation in Indonesia. And, as you know, Indonesia has had several terrorist incidents in recent years, so physical security can be a risk and can be quite an issue for the expatriates that work in our operations in certain areas.

Litigation risks are another challenge, and are somewhat related to the reputation and political risks.

Employee development and expertise is a key risk in Asia. One of the key things in an underdeveloped market is that basically you have to recruit, grow and develop and train your own staff. Quite often, just when they're trained and ready to go, someone else comes along and takes them.

Then the whole issue of plague, war and pestilence; SARS being a good example of one of the interesting challenges that we face in Asia right now.

I think the best way to really get across some of these points is to give you a quick case study on one territory, which is Vietnam. We entered Vietnam, working on getting a license in 1993. It's turned out to be, I guess, one of our better operations. I have a view of strategy and successful strategies often being the result of good happenstance as opposed to great thinking, and this is one that worked out very well for us. We showed very early interest in Vietnam. In the early '90s it was really below everyone else's radar screen. When we got a license in 1999, we were actually the first foreign company to get a license. I believe only three foreign companies have been licensed to date. It's a market that we've managed to grow very quickly and very successfully to the extent that, after four years, we're already operating with over 6,000 agents and 130,000 clients. It actually is making money.

That is very unusual for startup operations in underdeveloped countries. Often, they take a very long time to break even and show a profit. But this one has had such rapid growth that it's actually been profitable quickly. You have to be prepared for operations to take a long time to get on their feet, and also you have to be prepared for them being successful and growing very quickly. In many ways, being successful and growing very quickly, from a macro risk point of view, can pose more risks to you if you haven't set it up the right way in advance. Unsuccessful operations just tend to drain you of money and eventually shut down. With successful operations, you have to, obviously, deal with the consequences of your success.

Next I will give you descriptions of types of strategies that we followed in Vietnam and the risks that they actually mitigated. The first is a bit of a model that we followed throughout our growth models in the various Asian territories. It is to run with a professional agency force. In many ways, this is the key. This is the key kind of component of our whole business model in all these territories. We always make sure we have a very professional distribution system.

The risks that this mitigates are numerous. It gets you away from market conduct issues. It tends to give you a competitive advantage if you make the time and investments in it because local competitors, particularly, are often formidable competitors. But quite often, where they are quite weak is in terms of having a professional agency force. It can be very important for reputational risks and in terms of customer service.

Another key component of our strategies when we enter new territories is to try and go for a fast-growth strategy. It needs to be taken into the context of my earlier point that the worse thing you want to do is be a flag planter. It's better to pick a territory, go in, make the investment and try to grow it quickly.

Over time, it actually reduces your investment because of the fact that if you can get these operations to break even more quickly, you reduce the capital inflow that you have to make into these territories. The reality is when you're dealing with underdeveloped countries, the last thing you want to be doing is converting a lot of U.S. or other western currency dollars into local currency investments to capitalize these operations. So you basically want to be able to get them to be self-sustaining as quickly as possible.

Another area that we focus on is product. We try and go for simple products and we try to go for products that have relatively low guarantees; products that are adjustable. This helps from many points of view. We intended to use a par platform in Asia because of the fact that it gets to low guarantees and it will allow us to deal with pricing issues. When you get into new territories and aren't sure what the right pricing factors are, and you've got investment return implications, this is a good strategy. Having adjustable products are helpful, particularly if they're asset-intensive. Again, it helps deal with some of the competitive and capital issues as well.

Another key area is focusing on regulatory relationship management. That's a key accountability that we try and make sure all our local GMs really take on. Local regulatory relationships are very important to all these territories. Again, in many of these territories, the regulations are in a constant state of development. If you have good regulatory relationships, you can actually have a significant impact on the regulations.

Another area I've always concentrated on is a very conservative investment strategy. We don't, as a rule, invest that much of our surplus into local currency beyond what's needed. We also tend to stick to a very conservative investment strategy, and I'll talk more on that later.

The last key point is standardization. We actually have a sort of an administration platform for our whole Asian region in terms of IT hardware platform and software platform. We have very strict controls and policy platforms. All of this is run out of our regional office in Hong Kong. We find this very beneficial in terms of keeping control of those operations. It minimizes business interruption. It's cost efficient because it reduces the need to deploy expatriates in all these different territories. Expatriates are hugely expensive. One or two expatriates in Vietnam in an office of a hundred people could end up being potentially half your expense base if you're not careful. So deploying expatriates is very expensive, but, at the same time, you have to maintain control in these operations. So the need for standardization and platforms that can be put in robustly and then managed, to a large extent, from outside of the territory are quite useful.

So that's what we've done in one territory. Now I'll quickly go through five other examples of risk challenges that we faced in Asia and how we managed them. The last two are current topics, which I thought might add an interesting perspective. The first three are more systemic things that you get all the time.

First, assets and yields are a big issue, obviously, in any market. But, they're particularly an issue in developing markets. What we find in these markets, and this includes China, is that there are often limited long-term fixed-rate assets and there are limited investment grade assets. Long bonds also often don't exist in these markets, and many of the assets that you can buy are with counterparties with whom you really don't want to be taking credit positions. In addition, local equity markets are almost uniformly unattractive. This is not only because of volatility, but also because of very poor performance. Alternative assets really carry high risk. Some companies make a conscious thing to do large-scale unusual investments in joint ventures with the government on infrastructure projects. Those carry a lot of risk and we have not actually done that, although some companies do. Another interesting thing in Asia is that, for those countries with currencies that are pegged to the dollar, as the market develops, there's always the risk that it will become unpegged and flow downwards.

In terms of the strategies for assets and yields, we tend to try and reduce the risk through the product design. As I mentioned earlier, we tend to go for par products or other pass-through products and products with low cash value. We don't try to build up the asset intensity of these operations. What we try to do is build up the risk side of these operations. We try to make money by taking mortality risks, or morbidity risks, which are actually easier to manage in these territories than asset risk. We currency match our liabilities, but we often hedge the surplus or our investment of surplus in non-local currency. We also do not compromise our

underlying investment principles. We don't do exotic things, such as infrastructure projects, in countries that we wouldn't do in our home markets.

A very important thing from our perspective is that our reserving basis has a very accurate reflection of the investment return versus credited rate picture. The Canadian GAAP model that we work under, as a Canadian company, uses an asset-based valuation method. So it's always tied to the assets you're using, which has a very salutary effect in making sure that we are understanding the emerging yield picture and that we're not using inappropriate investments.

Another critical area of challenge is the regulatory environment. Often the regulators are quite unsophisticated. There is a tendency to be interventionist. Many of these markets are coming from fairly authoritarian regime backgrounds. Sometimes, the regulatory framework is not as interventionist, but it can move quite quickly. For example, in China, there are strict product-design limitations and regional licensing. In Hong Kong, there is increased licensing and board governance. In the Philippines, tax changes and the tightening of education savings market regulations are issues. In Indonesia, tax assessments can be troublesome. In Singapore, there is the Financial Advisor Act and agent licensing. Also, risk-based capital can be a challenge as well as corporate governance. In Taiwan, disclosure and risk-based capital are challenges. Finally, in Vietnam, regional expansion can be challenging. The key point here is that it is very important in all of these territories to be engaged with the regulators. In a developing market you have to get engaged with them and, in many ways, they want to be engaged with you because, as they're trying to develop their regulations, in many ways, you're free local expertise on hand that they wouldn't otherwise have access to. So usually it's to your advantage to be involved. The regulators want you to be involved, and usually you have expertise that they want. So it's a key thing that we have local management do, particularly the expatriates and the senior local management.

A third key issue in Asia is the recent significant economic challenges. The regional economy has had several years of economic ups and downs, which could really have a negative impact on your business franchise. The way we deal with it is to push the agent productivity and make sure that our operations have critical mass. Again, the best way to deal with this is to have strong operations. To have a flag-planting operation in a country where the economy goes sour is a recipe for disaster in terms of trying to stay in that market. We have a relentless focus on trying to stay profitable in these operations. We don't manage them any differently than we would our other business units. The fact that they're remote and face all of these different challenges doesn't change the financial disciplines that we try and impose on these businesses.

An interesting challenge for us, which I just thought I'd mention, is SARS. We have 1.5 million policies in force in Hong Kong, and have 1 million policyholders there. You can imagine in a population of eight million, when there's been 250 SARS

deaths, we'd have a fair number of SARS deaths. In fact, we've had 17 policy claims for SARS in Hong Kong, three in Singapore and a large number of medical claims. The interesting thing about SARS from a financial-condition analysis point of view is that the impact is not the claims impact. Those claims are under \$1 million. But, business continuity has been significantly hit. Basically, although it's getting better lately, for two months we had to triple back up all of our administration infrastructures. In other words, we had to split our administration teams into four separate locations because if one person got sick in one location, the entire office would have to shut down under the local health regulations to stop the spread of the disease and get people into quarantine. So there was a huge issue with business continuity.

When risk managers make business continuity plans, they generally don't worry about the people going down, but rather about the location being impaired or hardware going down. SARS is the case where the thing that was going down was the people. I don't think anyone had really planned for that. There was a huge economic impact. The economy has completely slowed down there. That economic impact directly went on to the sales where agents and customers were reluctant to meet. It seemed strange to be in a situation where agents did not want to go out and meet people to whom they could sell, but that's the situation we were in. You have to then look at other ways to sell, such as Internet selling and better telephone techniques.

There are also issues in terms of employee morale and trying to keep people motivated at work. Then you get into political issues, such as when the government thought one way to potentially deal with the SARS economics slow down would be to give everyone a contribution holiday from the mandatory pension plans, which were established a year ago. We just finished paying all the agents 5 percent commissions and then the government was talking about a contribution holiday. That got withdrawn.

Now I'm going to give you a bit of an anecdotal story on Indonesia. This is an example of what you might call political-litigation risk. Indonesia often hits the news as one of the most corrupt, inhospitable places to do business. We have been there since the 1980s and had never had any business issues at all. But after the 1997 economic collapse in Asia our local partner ended up going bankrupt. That meant their ownership sharing in the company got taken over. Now, there's really two ways you could do things. The local way is where you don't go through any legal system and you end up buying out your partner despite the fact they're bankrupt and they can make some money and the creditors get nothing, or you can go through the court system, which virtually no one did.

We went through the court system. Our local partner got no money out of that, obviously, and then for a year and a half we ended up virtually losing our company because of it. There was a claim filed under a policy that we denied because it was

a fraudulent claim, but it was a relative of the local partner who filed the claim, and somehow had our company virtually declared insolvent because we refused to pay the claim. That went through the judicial system. The judge basically took the company out of our hands. The judge appointed a receiver or an administrator who happened to be a business associate of our former partner.

So at this stage, we effectively have lost complete control of our local company all over one denied claim. Ultimately, we got this overturned, but one of the reasons it was overturned was because of the support we were able to bring in from the Canadian government, the World Bank and the International Monetary Fund (IMF). One of the strategic things we had done in Indonesia was to have the World Bank as a 5 or 10 percent partner in our company. So there was an immediate interest in that situation and the IMF brought a lot of pressure to bear in Indonesia to clean up this practice and using this as a test case.

But the key issue there is that we stuck to our North American business standards and really made sure that we had proper support lined up from other parties that could help us. But that's just an example of what can happen in dealing in a country such as Indonesia. I'm not trying to cast dispersions on Indonesia at all. I think everything has eventually worked out, but it's just an example of dealing in jurisdictions that don't necessarily have the same robust developed framework that you have in North America.

The message I want to leave is that if you're an international company that's working and developing international operations around the world, you really need to have a very disciplined financial risk management culture. It has to be a real cultural imperative in the company around risk management controls, risk management oversight, financial discipline and making sure you got that culture shared worldwide. You also have to have a strong corporate core to overlook these things.

MR. BESNER: Kathy Anderson is CFO and chief actuary of ING Latin America. In terms of risk management, Latin America is a particular challenge. In recent years it has certainly been pretty volatile, so I'm sure there are some interesting lessons to share from working in the region.

MS. KATHERINE ANDERSON: I'm going to split my presentation into three sections. I'm going to start off by giving a picture of ING worldwide, just to show how big they are across the world and put in perspective how Latin America fits into the ING world.

In the second section I will talk a little bit about some special-risks issues that we have to deal with in the Latin America area. I'll finish with a case study that includes Argentina, which has been an interesting 18 months of managing a lot of risk. We'll compare that to Peru, which in the last 18 months has been actually relatively stable.

ING consistently ranks in the top twenty global financial institutions.

As to our core activity, we are primarily involved in insurance, followed by banking. We also are building an asset management section, which is the smallest core area. Geographically, we're in 65 countries. We group those 65 countries into three regions, our largest being Europe. That is followed by the Americas, which includes the United States, Canada and the Latin American region, which I oversee. Finally, our smallest area is Asia and the Pacific countries.

In Latin America, we're primarily in five countries. We do have tiny businesses in some other countries, but not of much interest. We are very big in Mexico. We're the largest insurer in that country. In Chile, Brazil, Peru and Argentina, we're a little bit smaller. In Brazil, we have a joint venture. We only are half owner, but it's also the largest insurance company in the country.

Anderson Chart 1 shows our market share and market rank by country and product type. We are in a lot of product lines. In some countries, such as Argentina, we are more of a life insurance company only. In Peru, we do most of our business in the pension line.

We're really a life insurance company for the most part, but in Latin America, the mix changes a little bit. We have a lot of auto and property and casualty (P&C) business in Latin America. As you might remember, ING bought the Aetna operations in Latin America and that really created a different mix of business for us to manage.

ING, as you know, is based out of the Netherlands and a lot of the international decisions actually filter all the way up to the Netherlands. It's a long process to go through sometimes.

Now I will talk a little bit on special risk issues that we face in Latin America. The first one is local competition. The number of international players in these emerging countries is growing significantly. Chart 2 shows growth over a 10-year period. The top line in each of the categories is where we were at in the year 2000. As you go down, it's five-year increments. So in Mexico, there was a very small international participation in 1990, but is much higher as of 2000 and today. That's both life and the non-life operations.

This is very important because without international players, mostly in Brazil right now, they're experiencing a lot of local influence. The way they practice local business is not the same way an international company would. So we buy into these countries and we try to impose ING standards or international standards and we can't compete. So we invest all of this money into a country to struggle on meeting our pricing thresholds and qualifying for an ING core country. We're in 65

countries, and the declared core countries get much more attention and much better treatment by the parent company. This is a very important element for us.

Macroeconomics is another issue. As David mentioned, some of these international companies try to group all of their businesses so they can do some kind of comparison. ING tries very hard to compare their 65 countries and the businesses into those countries to decide where to invest more. They want to know who's really performing. So we actually try to set these macroeconomic assumptions, such as interest rates, inflation, unemployment and the exchange rate, in a similar way to have a similar definition in all countries. That doesn't work. As we heard from Simon, the emerging countries are much more volatile.

For example, one thing that ING uses is a nine-month rolling average on the foreign exchange rates looking backwards. That's not always a good definition for Latin America, especially if we look at Argentina. For Argentina, I had to go nine months back after the crisis hit and my exchange rate really was pretty close to one-to-one because looking nine months backwards we were one-to-one. So that's what ING was using to compare Argentina to other countries when there was no current basis, other than that is how they measure the exchange rate.

We also have to do, as most companies do, a plan. So we do three-year plans, which is an interesting thing in Latin America as well. Most of our businesses down there are acquired. So trying to get the local people to understand they need to look three years out to see what they can accomplish, and they'll be held to those three-year projections has been a real challenge, because you can't project these things 12 months ahead much less 36 months ahead. Although ING tries very hard to compare all their countries, it's a very difficult thing for us in Latin America.

To give you an example of the volatility of exchange rates, in Latin America, they announced that we had decreased our earnings from last year. We actually did not decrease our earnings from last year on a local basis. On a local currency basis, we actually exceeded our earnings from last year. But, when you exchange it back to the Euro, in the last nine months all five of our countries devalued. The devaluation was a bigger impact than the increase in the earnings that we had.

In Chile, just this past month, the regulators decided to reinterpret the regulation for universal life (UL) products, and you're no longer allowed to have surrender charges. They made it retroactive. So every in-force UL policy we have, they no longer have surrender charges. So we immediately had to direct our actuaries' attention from working on annuities, which has its own issues, to the life business. They had to redevelop three products very quickly to be products for which we can actually manage the risk. So now we introduced persistency bonuses and other ways to keep these policyholders from lapsing their policies.

Asset/liability management (ALM) is a very difficult issue in Latin America. Assets are all short and there's a big concentration risk. There's very little available in Latin America. Some of them are opening up. Peru is now going to allow us to have 20 percent international investments. So now we can go to the United States and bring a little bit more diversity into our portfolio.

The only issue I am going to mention related to product design is in Mexico, because right now I'm reviewing a new health product that is being introduced. There is some uniqueness in Mexico. For example, we have to cover accidents because of alcohol use. It's just a cultural thing. We have to cover all injuries in auto accidents that occur through alcohol, which we wouldn't do in the U.S.

The use of capital is the one that I'm going to use for a case study. It's an interesting scenario, and an interesting challenge for us. Before I go into the case study, I'm going to actually limit it and give you some assumptions that will simplify the situation. One country competes against 64 other countries to get capital from ING, and capital is limited more so than in the past. So they have to make decisions and we have to show them the risk that they're buying into by making a greater investment in Latin America.

A lot of the decision of how to use capital comes down to asking and answering some questions. What is the risk appetite? If they're opportunistic and believe Argentina is at the low end of the cycle now, and they have a big risk appetite, they would want to invest in Argentina. It's very cheap to invest in Argentina. But if you want long-term returns that you can count on, you might not want to be in Argentina because the historical cycle is pretty volatile in that country.

Now I'll discuss concentration or breadth. We make a lot of decisions based on the fact that we are too heavily invested already in a certain product type or product line, or we're too invested in a particular country that is more volatile. So we make all these decisions setting our strategy, and they come into play whenever we request capital and make our case.

So here are the assumptions. You want to assume that capital is limited. Otherwise, we would invest in every opportunity that sounded good, and we'll assume we can't do that. I want to make the assumption that it has been decided that we're going to invest in Latin America. We're building in emerging countries. We believe in Latin America's future so we are going to invest in that region.

For the purpose of this case study, I'm going to say we've already invested in Mexico, Brazil and Chile. So my current alternatives with the capital that I do have are to either invest it in Argentina or Peru. The question is which one should we give the money to and which one can really deliver the returns that we need.

I also have to assume all management teams are different, all cultures are different and communication sometimes is more difficult with some management teams.

But in this case, I would assume that the country puts forth their best reason for needing the capital. There are a lot of reasons they could put forth, and we'll assume they put forth the best one.

So we start with Argentina, and Argentina's buildup is a little bit longer than Peru's. I want to give you a feel for what has happened in the last 18 months. Why would we want to do it? The country is in chaos right now. The economy is horrible. They finally do have a new president, although that's only because the other candidate backed out and so the one that was left is now president.

So why would we want to? Well, one reason is Argentina is a very large country in Latin America. If you have a presence there, you are more likely to be considered a leader in the Latin American marketplace. We are already there. We are one of the only solvent insurance companies left in Argentina. That is a benefit for us. Even if it takes a while to recover, as long as we can stay solvent and build on our success to date, it will be there when the economy evolves. We do have a great reputation. One reason is because we're still solvent. We still employ a lot of people. Those are all reasons why ING is loved in Argentina right now.

There is a large population in Argentina, and they're very underinsured. The potential for insurance companies to build in Argentina is pretty large. As I mentioned, it's currently pretty cheap to do this in Argentina. The unemployment rate in Argentina right now is more than 50 percent. So, you can retain your people. We haven't given raises throughout the whole crisis so it's very easy to retain talent other than expatriates. That's an exception.

But why would we be concerned about investing in Argentina? First of all, there's the current instability, which I'll review. Historically, it is a volatile country. How long is it going to take them to get a president that can solve these problems and turn around the economy? We have the short-term/long-term return issue that I had mentioned.

Here's what happened in the last eighteen months. In 2001, there was a lot of speculation about Argentina being severely in debt and having a government in place that was chronically overspending and they were just calling more and more loans from the IMF. Well, at the very end of 2001, the IMF froze the money that they were going to give them. Then we had five presidents in one month. We did finally get a president that's in place. He'll be leaving for the new president that was just appointed this month, I believe. But we did finally get a president that stayed longer than a week in office. He took a lot of action that will, ultimately, actually hurt the situation even more. In the end, it's going to be a good historical case study because how they get themselves out of this situation will be interesting.

They did end up defaulting on their loan. They defaulted on the majority of the loans that they had with the IMF, which is the largest default in history. They unpegged the peso to the dollar. That immediately caused it to go two-to-one and it

deteriorated from there. But the government didn't want everything to go two-to-one. This was a big problem. So they had multiple exchange rates. They used one-to-one in some scenarios. For exports, they used 1.4 to one, and for the general public, they used two-to-one. So they had all these different exchange rates occurring at the same time.

Then they started getting a lot of negative press and the president wasn't solving the problems. He started having compassion for the consumers and he decided he should take some steps to help them out, which were really not the best steps. He made the banks exchange the loans on a one-to-one basis. This is a problem because these were the assets of the banks. But the liabilities of the banks went on a free float, so we've had severe bankruptcies of all the banks. A lot of the Spanish banks that were in the country at that time have withdrawn since. But it was a severe situation for the banks on their balance sheet.

They also decided to tell the utility companies that they could only exchange one-to-one. So they did not get to collect all these extra pesos that they were actually entitled to. They knew that the banks were having problems because as soon as they did the one-to-one on the loans, the banks had this mismatch on the balance sheet and they tried to take care of the banks.

So the next step that the government took was to freeze checking and savings accounts. So consumers can't touch their money over certain limits. They knew they had to have a little bit of money to spend. They also made a distinction between checking and savings because if you put it in a savings account in the past 10 years, you must truly be saving. So they froze the savings at even a lower level. Then they restricted withdrawals because they did want you to have some cash flow ability as a consumer, but they didn't want a run on the banks. So, they limited you to 1,000 per month, and later raised that to 5,000.

They really wanted it to be a peso-based economy as opposed to a U.S. dollar economy. So, they outlawed all U.S. dollar contracts. They forced the pesofication. They made the two parties either renegotiate the contracts or the government stepped in and renegotiated it. This was actually interesting with ING, because we had a contract with ING Real Estate and they didn't want to pesofy. I was able to say, "But the government says you have to pesofy." So I actually did get to negotiate a better price for our real estate.

Then they were looking for places where they could get more money, and one of the only profitable industries in Argentina at the time was the oil industry. They decided that would be where the government could get some more money so they started levying 15 to 20 percent new tax on them.

Then companies started having financial problems and started laying off people. Unemployment was skyrocketing, and the government put a freeze on that. They

would not allow anyone to be fired for 180 days, and after the 180 days, when people could be fired they had to be paid double severance. This is still in effect. We know that very well, as we try to make decisions. You really have to balance. Employees are getting double severance or are staying on the payroll.

They finally decided they needed free elections. They wanted to get a president that everybody supported. That has now happened. There's a problem though, so it will be interesting in how it all plays out. The president that won actually advanced to the final round of elections with only 20 percent of the vote. Nobody got 50 percent or more so the top two had to go to a runoff. The other contender was the person who ran Argentina before. He eventually stepped down because he was at risk of losing and wanted to save face. The whole purpose was to get a president that the people supported, but the president actually only got 20 percent of the vote in the first election and he was placed into office now without ever getting the majority of the vote, so that causes a problem.

The consequence of all those actions was severe inflation. It's actually less than what we had predicted. We predicted 50 to 100 percent inflation and it has actually been a little bit more controlled than that, although we're still behind in the numbers. Prices went up almost immediately when all this started happening, and a lot of it was speculative; nothing other than your concern about the future causes price increases. There were a lot of riots. Security issues came up for us during that time as to how to get our people out of the country if it really goes bad. I wouldn't go down there for that period of time. Consumers really just didn't believe in banks. They didn't believe in the government. There was a lot of dissatisfaction in the country. Most of the foreign-owned banks, as I mentioned, withdrew from the country. Unemployment continues to increase even to this day. Interest rates are really high. They are trying to get people to invest and nobody wants to invest in the country.

So that's currently, but Chart 3 shows it historically. This is a story that's been repeated in Argentina multiple times. We were at the same place 10 years ago. But we had a good 10-year run. When you look at short-term versus long-term, 10 years ago you would have invested in Argentina. If you would have got out eight years after investing, you would have done great. There were great returns, businesses grew well and the economy was wonderful. It was the leading country in Latin America. But, if you didn't get out before December 2001, you're right back where you were 10 years ago, and potentially have lost an awful lot of money. So it is a historical issue with Argentina, but it is an opportunistic country, too, with short-term returns.

The company I'm using for this case study is a life-only company, with 70,000 clients and tied-agent distribution. They want capital because they believe the economy is going to rebound. It's either going to be one year or three years, but it's going to rebound. They believe they need to position themselves better to take advantage of this economy recovering. They've asked us for capital to revise their

life portfolio and introduce new product lines such as annuities and health business. So we always ask them to let us know how much capital they need and what are their short and long returns.

I actually don't agree with Chart 4. Long-term, to me, is not 10 years. Long-term would be more like 30 years, but for this example I did use 10-year returns. Then we always ask for optimistic and pessimistic scenarios as well, which are the scenarios we have here.

It's also important to compare the information to status quo. I'm already in Argentina, and unless I choose to get out, I'm going to have to give them capital to run their business. Already you have committed on giving them \$6.5 million this year to run their business. These are the type of returns that we see in their strategic plan. They're going to give me 12.5 percent return on my money in 10 years.

We do look at optimistic volatility that could possibly come into play over this time period in which we're spending more money. The best estimate is the one we considered making a decision off of with the other pieces giving us additional information. That's Argentina.

In Peru, as I mentioned, the last 18 months has been rather stable. They've been one of our best businesses in Latin America in terms of meeting or exceeding results. Their economy is healthy. They're not having great inflation. There is a little bit of bobbling around in the political field right now, but it's been a good country for us. Why would we want to invest there? They have produced consistent profit for us. They have a good economy right now. Their regulatory and political risks are very low key today, but that could always change. We also have a good brand reputation in Peru as well. It's a unique case in Peru, however. After we bought the company, we kept their name. So it's not actually ING, it's Integra, but they're very well recognized as Integra and that's why we don't change their name to ING.

We do have concerns there. There is limited growth. It's a rather small country compared to some of the other South American countries, with only 26 million people. Because they are small, they're not a big influential country in Latin America. Sometimes they will actually have lingering effects from the other countries' problems. So Argentina's and Brazil's problems will impact Peru ultimately in the future. Presidential elections will be coming up there and we'll see how volatile it becomes at that time. Over the long-term, what is this country going to mean in the Latin America strategy? If you're in the emerging countries, and that's a strategy for you, how important is Peru versus some of the other big countries in the region?

So in the situation here, we have a pension, life and annuity company, which sells a little bit of P&C business as well. The company has 800,000 clients. We're

positioned very well in Peru. They want capital to enhance their life and annuity portfolios. As I mentioned before, we are very big in the pension line. Our other lines are small compared to the pension, so they want to build that up to scale. But if they do that, they also need to redo their systems for the product distribution and the administration systems. They need money to do that.

Chart 5 is what they showed us. This manager team takes a different approach than Argentina. This happens in the requests that we make. They said they need 16 million, period. They just need 8 million more than status quo, and depending on what happens in the economy, they change their return levels based on that as opposed to changing how much capital they need to get. Remember in Argentina, they were requesting 5 million additional capital above the 6.5 million, and Peru is asking for 8 million above their 8 million. So we have a difference in the amounts requested.

In Chart 6 we put them side-by-side to try to draw some conclusions on where best to put our money. If we look straight at the numbers, a direct conclusion may be Peru is the better answer. But Argentina, as I mentioned, are at a low point in their cycle. There is potential to make a lot of money in the next 10 years in Argentina, and they have a much bigger influence on the Latin America region. So there are a lot of their reasons why you might choose Argentina. Also, you look at status quo because if we choose to invest in one and not the other, then we're leaving somebody behind. We combine these results. We give Peru's proposal and Argentina remains status quo, or we have Argentina's proposal and Peru remains status quo. It's one combination or the other.

In today's world, this is unfortunate. I put up the worse case scenario because I think most companies are much more risk-averse today than they have been in the past because of the recent two to three years. So the most likely question I hear when I'm asking for capital is what is the worst thing that can happen. They don't want anything else to go wrong. They want everything to go well. But they don't ask anymore what's the best situation that could happen, which is an important question, too. You do have things that can go well for you, too. Even though we've had a tough two to three years, things can go well.

Which would you pick? Argentina or Peru? Argentina wants five; Peru wants eight. You have all the different backgrounds. Argentina certainly has greater potential for us in our South America strategy, based on size and historical role but has economic cycles. Although Peru has been very good lately, they could do exactly the same thing as Argentina. They could actually take a big economic drop, and we have to anticipate that. All the exchange-rate issues that have been mentioned are great.

Chart 7 is to emphasize the exchange rate issue, because we don't hedge Latin America. We do hedge the U.S. dollar and the Euro, but we don't hedge Latin America. Everything is measured in Euros in ING's world. So their contribution to

me this year is in Euros. When I return the money back to them in 10 years, it's in Euros. So if I give money to Argentina and Peru today and one devalues and the currency of one gets stronger, the results could make the amount of money I made for ING a lot different than what was expected.

For exchange rates, I just said, "What if one year from now we have what we had a year ago?" I said, "What if they all rebound and Argentina goes from 2.75 back to the one-to-one, but Peru actually deteriorates and goes to 3.65?" What happens in that scenario? Argentina, by far, is the better investment choice if you're just looking at the return on that part in Euros.

So with that, should we select Argentina or Peru? The return priority, as I mentioned, is very critical in this decision. Which one has better short-term versus long-term and vice versa, and which one is more important to the organization? As I said, the capital is limited, but I didn't say how much capital we have. Sometimes what happens is we have less capital than we need, and ING will select a country, but they'll say, "I can't give you ten. I'll give you six. What can you do with six?" You do need capital, but you just don't get what it takes to make your plan so you have to adjust. Sometimes that helps make the decision a little bit easier.

But in the real world, we have 65 countries that capital can go to, or you could give it back to the shareholders. But we would typically not do that. We'd obviously invest, and we are investing in Latin America and we continue to invest in it. I think it's really tough sometimes with all these issues coming together and in trying to make the best decisions.

So I think there are three things that make it easier. First, know your strategy before you go in and see the results of this analysis. Second, understand the scope of all the risks. There are many risks in Latin America. Last on my list, is avoid analysis paralysis.

FROM THE FLOOR: When you make these decisions, how much of it is based on what is most exciting?

MS. ANDERSON: I can tell you a lot of my decisions are made on what's most exciting, but that's not how ING makes their decisions, unfortunately. So I am a layer that Latin America goes through because Latin America has to convince me we have a good enough story to ask for capital, or to get permission to do a new product line. I get excited. That's one reason I'm in Latin America. I love the challenges of Latin America and all these unique things that come up. We do filter it up. They are much more serious. They look at the numbers in much greater detail, and we do a lot of analysis for them. They look at it in every angle that they can think of.

MR. AARON SCHLAFLY: Ms. Anderson, do you do any sort of risk adjustment when you're looking at these returns? Or do you simply look at 18 percent?

MS. ANDERSON: This is actually controversial in our world. We do make adjustments by country. Our thresholds are set sort of by formula. We have the risk-free rate of the country and that, depending on the country, could be a one-year bond, a 10-year bond or whatever we decide is the risk-free rate of that country. We add on top of that a cost of capital of ING, and we add on top of that a country risk. That country risk varies between 1 and 3 percent. It used to go as high as 8 percent, which it may go back up to now because we've had some significant risk.

The controversy is whether the risk-free rate of the country and the country risk we add on the end is a double count.

MR. CURTIS: We actually do it the same way.. Again, it is the same issue. In some of the growing economies and the less-developed economies in the Philippines and Indonesia, you end up with a 25 or 30 percent discount rate. Then the question is, is that fair because you're working with base interest rates, which may be 15 percent as opposed to 5 percent in North America on risk-free investments. So you've got that exact debate as to whether you're double hitting them for a risk premium. But having said that, if you're operating in a country like Indonesia, you would want to get a 25 to 30 percent return probably.

FROM THE FLOOR: What's the reason for Vietnam to be able to break even faster than the other countries in Asia? Also, do you see the potential for a market for variable annuities?

MR. CURTIS: I'll start with the second question first. Variable annuities tend to need a stock market in a country that's mature enough to support it. So we've introduced variable annuities in Taiwan. Hong Kong has a mandatory provident-fund pension scheme, which is of a group type 401 (k). But we haven't really introduced variable products in the other territories. But, if the markets were strong enough, we probably would, because, obviously, that's a way to deal with some of the investment-risk issues.

In terms of the first question, I guess the key learning from Vietnam would be if you can be the first foreign country company into a market and start quickly, even if others catch up with you and overtake you, you're always going to be one of the front runners. That was our big success in Vietnam. We were the first foreign company to be licensed and, as a result, we had a big running start. I think Prudential U.K. got licensed quite quickly and overtook us, but we're sitting there with a 15 percent market share and it's going to be very hard for other entrants coming in to catch up.

Chart 1

ING's has #1 Insurer position in Latin America

Current Markets	Pension		Life		Health		Auto		P&C		Mutual Funds	
	Mkt Share	Mkt Rank	Mkt Share	Mkt Rank	Mkt Share	Mkt Rank	Mkt Share	Mkt Rank	Mkt Share	Mkt Rank	Mkt Share	Mkt Rank
Mexico	9%	5	16%	3	28%	1	23%	1	28%	1		
Chile	13%	4	13%	1	22%	2	7%	6	5%	9		
Brazil	2%	12	5%	5	42%	1	13%	3	10%	4	1%	20
Peru	32%	1	20%	2					8%	3		
Argentina			13%	2								

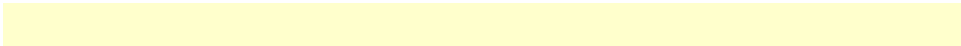


Chart 2

Local Competition ... it's Changing

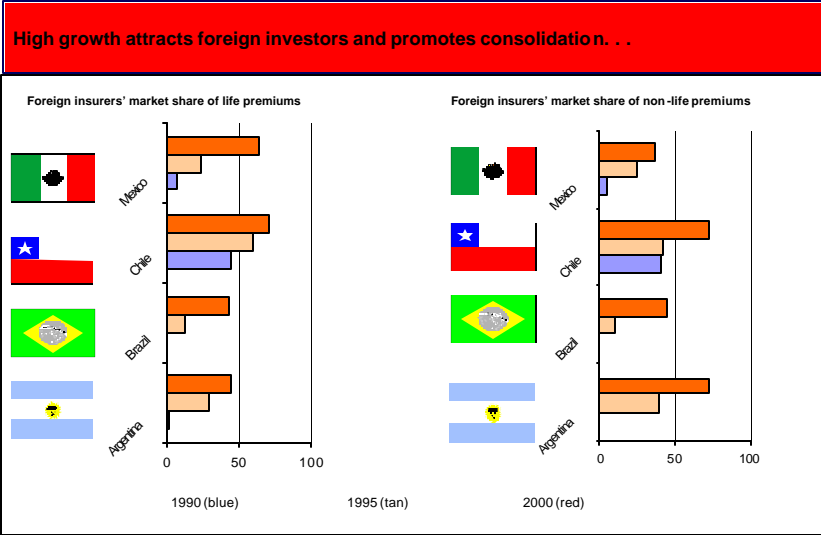


Chart 3

1. Argentina – Case Study

- Historical Volatility**

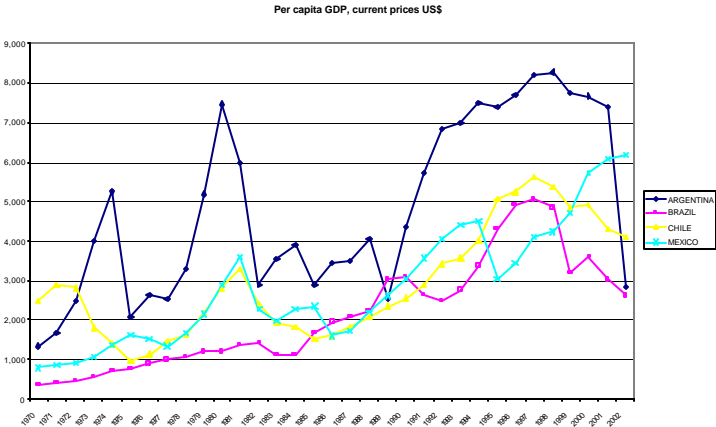


Chart 4

1. Argentina – Case Study

	Capital Required (MIn \$US)	Short-term Returns (3 yrs)	Long-term Returns (10 yrs)	Comments
Best Guess	\$11.5	Zero	14.0%	3-year recovery
Optimistic Scenario	\$9.5	6.5%	18.0%	1 – year economic recovery
Pessimistic Scenario	\$17.5	Negative	Negative	Ongoing instability
Status Quo (2 life products & riders)	\$6.5	Negative	12.5%	Best Guess Only; Should also look at other scenarios

Chart 5

2. Peru – Case Study

	Capital Required (Mln \$US)	Short-term Returns (3 yrs)	Long-term Returns (10 yrs)	Comments
Best Guess	\$16.0	11.0%	18.0%	Ongoing good country situation
Optimistic Scenario	\$16.0	20.0%	18.0%	Regulatory changes delayed
Pessimistic Scenario	\$16.0	Negative	4.0%	Regulatory changes; more competition
Status Quo	\$8.0	2.0%	8.0%	Best Guess Only; Should also look at other scenarios

Chart 6

Use of Capital – Case Study

(\$USD)	Arg Proposal	Peru Proposal	Arg Status Quo	Peru Status Quo	Arg Worst Case	Peru Worst Case
Capital Required (mln)	\$11.5	\$16.0	\$6.5	\$8.0	\$17.5	\$16.0
ST Return (3 years)	Zero	11.0%	Neg	2.0%	Neg	Neg
LT Return (10 yrs)	14.0%	18.0%	12.5%	8.0%	Neg	4.0%
Total LT Return (mln)	\$1.61	\$2.88	\$0.81	\$0.64	Losses	\$0.64

Chart 7

Use of Capital - Case Study

	Argentina	Peru
Q3 2002 FX	2.75	3.53
\$USD Return	\$1.61	\$2.88
ROIC	14.0%	18.0%
Q3 2001 FX <small>(note: change in 1 year)</small>	1.00	3.65
\$USD Return	\$4.43	\$2.79
ROIC	38.5%	17.5%



