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Market Bulletin

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Title	Lloyd's new Credit Risk underwriting framework
Purpose	To inform the market of updates to Lloyd's approach towards Credit Risk (insurance) oversight
Type	Event
From	Rachel Turk, Chief of Market Performance
Date	28 July 2026
Deadline	To be adopted progressively throughout 2026-2027
Related links	Lloyd's Supplemental Requirements and Guidance Risk codes - Lloyd's

Executive Summary

Over the past couple of years, there has been a marked increase in credit-related activity across the market, both from existing participants expanding their underwriting in this space and from a growing number of new entrants with specialist credit strategies. The increase in credit related activity and interest in Lloyd's, aligned with the development of a more sophisticated Lloyd's risk appetite for this class, necessitates a revised approach to managing this particular segment of the portfolio.

Currently, credit & political risks account for just over 4% of total gross written premium and have grown at a CAGR of more than 40% over the past three years. These classes bring additional complexity to the market with considerations such as:

- counterparty default risk
- concentration risk
- correlations between underwriting exposure and asset valuations
- correlation between macroeconomic / systemic stress events
- complexity of understanding capital requirements especially for monoline syndicates

To date, Lloyd's had adopted a rules-based approach towards the oversight of the class, which included some high-level expectations around syndicates underwriting expertise, how much credit business a syndicate can write as a proportion of their overall gross written premium, and requirements in respect of certain characteristics and clauses credit products should have. However, the current rules do not:

- take into account the potential diversification and non-correlated growth of the credit class, compared to the traditional Property and Casualty (P&C) portfolio.
- appropriately address or support the growth aspirations of those with demonstrable expertise within the class,
- acknowledge the wide array of products and complexities within the class and the different maturity and expertise required to underwrite them sustainably, and
- provide clarity and understanding of the systemic (catastrophe) potential that the class brings to Lloyd's, not just from an underwriting (liabilities) perspective, but also across the balance sheet due to correlations (assets and capital).

In light of the above, Lloyd's is implementing a comprehensive framework to enhance Credit risk oversight in response to the market evolution, including ensuring appropriate capitalisation and sound expertise. There are three main workstreams, that are detailed below, with key deliverables and timelines. The complete framework will be in place during H1 2027.

1. Workstream 1: Portfolio Segmentation

- <u>Aim:</u>

- To segment the Lloyd's Credit portfolio to the appropriate level of granularity, regarding product and asset classes, to understand portfolio composition, and the sophistication/maturity expected from a syndicate writing a portfolio based on its features, size and diversification.

- <u>Deliverables:</u>

- **New suite of Credit risk codes**, with the following granularities:
    - Whole turnover trade Credit
    - Single situation Credit
    - Single situation Contract Frustration
    - Significant Risk Transfers and portfolio transfers (non-mortgage)
    - Mortgage Indemnity
    - Surety Bond RI

- ❖ Status & Timeline: Completed (launched for 2026 CPG season).

- **New Credit Risk return**, giving Lloyd's access to the following risk features, per portfolio:

    - Top 20 obligors
    - Top 10 Countries
    - Sovereign v Private and Secured v Unsecured
    - Duration/Maturity and earnings pattern
    - Sectors

  ❖ Status & Timeline: Completed in January 2025 (to be collected at 1/1 and 1/7 each year alongside RDSs).

- **Future enhancements**, giving access to the (additional) following risk features (in discussion with LMA and potential vendors):

    - Full list of obligors
    - Probability of Default (PD)
    - Loss Given Default (LGD)
    - Exposure at Default (EAD)
    - Duration
    - FX
    - Jurisdiction
    - Policy features

  ❖ Status & Timeline: Ongoing (discussions taking place within Credit and Political Risks market and survey launched with the LMA).

We consider the above data granularities and dimensions to be sufficient for the following purposes:

- Validate/challenge internal syndicate views of specified return periods.
- Understand data and modelling capabilities (linked to Class of Business Review & Assurance (COBRA) as outlined below).
- Consistent view of both sides of the balance sheet.

2. Workstream 2: Capability Assessment

- Aim:

  - To understand and manage the sophistication and maturity by syndicate across the relevant PBO Principles necessary to write the distinct Credit products, depending on credit portfolio mix (product), materiality (at syndicate and market level) and % of overall GWP.

  - The relevant PBO Principles are:
    - Underwriting
    - Exposure Management
    - Outwards Reinsurance
    - Capital
    - Investments

- Deliverables:

  - **Class of Business Review and Assurance (COBRA):** This is a questionnaire devised with Lloyd's Principle owners, asking specific questions around Credit risk. This will allow Lloyd's to understand a syndicate's sophistication to write the class, against the feature of the portfolio they intend to write, having regard to complexity and materiality.

    ❖ Status & Timeline: Completed in Q1 2026 (questionnaire completed and agreed with PBO Principle owners).

  - **Capability Categorisation**: Syndicates categorised as meeting the below criteria would be expected to compete a COBRA and demonstrate appropriate capability:

    1. Materiality and concentration, based on how material a syndicate is to the market, to be examined by written premium and line size at risk code level, as well as how material the Credit class and correlated classes (e.g. D&O) is for the syndicate's Solvency Capital Requirement (SCR).

    2. Syndicate portfolio diversification.

    3. Credit portfolio composition, specifically the complexity of the products being written, with the most complex ones being Significant Risk Transfer and Mortgage Indemnity.

       For example, a mono-line Credit syndicate writing Whole Turnover Trade Credit would be expected to demonstrate to Lloyd's the capabilities required to both manage the associated risks and actively shape its intended portfolio.

       This is expected to support CPG and new entrants' pipeline by providing a capability-based view of syndicates.

- Timeline:

  COBRA Pilot to be deployed in H1 2026 with selected group of systemically relevant syndicates (i.e. mono-line syndicates and those with large Credit portfolios) to refine the process ahead of deployment more widely throughout 2026-2027.

  From the 2027 Capital Planning cycle (i.e. September 2026), syndicates that meet one of the above criteria and have not undergone a COBRA process must put themselves forward for Lloyd’s to validate their capabilities, as a condition to their business plan for the class being approved, within a timeframe to be agreed with Lloyd’s.

  In practice, where a new mono-line syndicate seeks to operate at Lloyd’s, or where a syndicate includes risk codes ST and FM in its SBF (including where these were part of prior years’ plans), or where a syndicate is identified by Lloyd’s Market Performance as material to the overall class, Lloyd’s expects a COBRA to take place and appropriate capabilities to be demonstrated as a condition of business plan approval.

- Status: On track.

3. Workstream 3: Market and syndicate risk appetite

- <u>Aim:</u>

  - To replace GWP based risk appetite with a quantitative (modelled) view of tail risk, across the market through the development of relevant RDSs (progressively retiring the less relevant Political Risk RDSs).

  - We desire to create consistency within the market across both liabilities and assets. In turn enabling:

    - More informed syndicate capability assessments
    - Ability to support syndicate growth aspirations
    - A better understanding of syndicate exposures
    - Consistent aggregation to inform market-wide risk appetite and franchise guidelines or similar thresholds (e.g. Nat Cat appetite of 35% of ECA)
    - Lloyd's to have better ability for asset and liability stress testing

- <u>Deliverables:</u>

  - **New suite of Credit and Political Risks RDSs**

    These newly created scenarios span a range of return periods and have been developed in partnership with the LMA and the newly established Credit and Political Risk RDS Working Groups. Through this work, Lloyd's has agreed with the market to prescribe "stress factors". However, where syndicate models reflect a more mature view of risk (e.g. categorised as leading under COBRA), syndicates may instead apply their own stress factors, provided the underlying assumptions are clearly explained to Lloyd's.

    These RDSs will replace the four existing Political Risk RDSs, with three scenarios as follows:

    - **Political Risk scenario**
      - This scenario is to follow similar methodology of existing PR RDSs.
      - To be completed by syndicates writing PR risk code.
    - **Credit scenario**
      - This is to be completed by all syndicates writing some form of non-payment insurance i.e. risk codes CR, CF, FG, FM, SB, ST, WT and the stress factors prescribed include:
        - Probability of Default (PD)
        - Loss Given Default (LGD)
        - Exposure at Default (EAD)

❖ Status & Timeline: The activity was completed in Q2 2026 (ready for rollout in 2027).

- **Develop Appropriate Lloyd's risk appetite guidelines**

  This will help define Lloyd's Credit risk appetite, in a similar fashion to Lloyd's natural catastrophe risk appetite (i.e. X% of ECA + profit) at syndicate and market level, using the Credit scenario, once is formally deployed.

  - ❖ Status & Timeline: Ongoing (to be completed H1 2027).

- **Facilitate the harmonisation of assets and liabilities MI to be able to have a cross-balance sheet stressed view of Credit risk**

  At present, credit risk is typically assessed within silos with asset credit risk through investment and counterparty exposures and liability credit risk through underwriting performance by class of business.

  This harmonisation exercise would involve aligning data definitions (e.g. obligor, sector, credit rating, geography, maturity etc.), exposure hierarchies (i.e. ultimate parent, instrument, counterparty, named obligor), and stress calibration approaches. This would create a uniform approach to categorisation and the same/similar level of granularity required to perform correlation and stress tests consistently, enabling correlation analysis between asset defaults, counterparty exposure, and liability performance under common macroeconomic or sectoral stress scenarios.

  The outcome would be a consolidated "cross balance sheet credit risk view" capable of identifying concentration and contagion risks e.g. where the same financial institution is both an investment holding and/or counterparty and/or contains similar obligor exposures. In turn, this harmonised view and accompanying MI would inform Strategic Asset Allocations decisions across the Central Fund as well as exposures across the consolidated Chain of Security by quantifying systemic exposures as well as potential diversification benefits, improving oversight and enabling efficient capital deployment within Lloyd's Risk Appetite, as well as to inform asset allocations across Lloyd's chain of security.

- **Define and run scenarios through the Lloyd's Internal Model (LIM)**

  These will be scenarios where there is a growth in the credit portfolio (on both sides of the balance sheet), where the impact on a syndicates capital can be modelled (based on a chosen dependency between market risk and premium risk).

  - ❖ Status & Timeline: This assessment will be carried out during the 2026 capital setting process and included as a validation exercise as part of the wider assessment of Credit Risk under the "New Entrant (Credit)" Focus Area for the 2026 Validation.

4. Transition guardrails

Whilst the above workstreams are developed, we are enforcing the below guardrails, which we consider to be sufficient to mitigate risks associated with new entrants in the class:

- **Portfolio segmentation**
  - Through the Credit Risk Return launched this year, Lloyd's has full visibility of a new entrant's portfolio and can establish whether it represents a diversifying GWP comparatively against the Lloyd's established Credit portfolio, across the following dimensions:
    - Products
    - Top obligors
    - Countries
    - Sovereign v Private and Secured v Unsecured
    - Duration/Maturity and earnings pattern
    - Sectors
  - The above has allowed Lloyd's to understand the features of the portfolios proposed by new entrants to date and conclude that the proposals presented are accretive to the Lloyd's portfolio, as each new entrant specialising in the class diversifies our existing GWP and exposure base.
- **Capability Assessment**
  - Each new entrant would need to be reviewed by the relevant technical teams at Lloyd's to validate the syndicate's proficiency across the Principles identified for the COBRA. Once the COBRA is formalised, mono-line syndicates will be the first ones to demonstrate their capabilities as part of the pilot group.
- **Syndicate and market view of risk**
  - Whilst a risk appetite is developed, as described in the following section, Lloyd's is managing tail exposures during the "transition" to address the capital risk that this gap creates. Specifically, existing Franchise Guidelines are being used to set capital for new credit syndicates and mitigate potential risk to the Central Fund.

5. Additional requirements and considerations

<u>Definitions</u>

Credit and Financial Guarantee insurance is defined as contracts of insurance (which includes any indemnity, guarantee, bond, contract of surety or other similar instrument, and references to "insurance" including reinsurance) where the insurer agrees to indemnify the insured against loss, or pay or otherwise benefit the insured in the event of any of the following:

1. the financial failure, default, insolvency, bankruptcy, liquidation or winding up of any person whether or not a party to the contract of insurance
2. the financial failure of any venture
3. the lack of or insufficient receipts, sales or profits of any venture
4. the lack of or inadequate response or support by sponsors or financial supporters
5. a change in levels of interest rates
6. a change of rates of exchange of currency
7. a change in the value or price of land, buildings, securities or commodities or any other tangible or intangible assets
8. a change in levels of financial or commodity indices
9. any liability or obligation under an accommodation bill or similar instrument

Included within Financial Guarantee are the following classes products:

- Single Situation Contract Frustration (Risk Code CF)
- Single Situation Credit Risk (renamed from Trade Credit) (Risk Code CR)
- Whole Turnover Trade Credit (Risk Code WT)
- Significant Risk Transfers and Portfolio Transfers (Risk Code ST)
- Mortgage Indemnity Insurance (Risk Code FM)
- Surety Bond Reinsurance (Risk Code SB)

Guidance on the definitions for the coding of each of the above risk codes and products can be found in Lloyd's 'Risk Codes Guidance and Mapping Notes' on Lloyds.com.

For the purposes of allocating a risk code, where a risk falls within the definition of Financial Guarantee, it should only be assigned to the FG risk code where the risk cannot be properly allocated to one of the other risk codes specified for Financial Guarantee business. For example, Salvage Guarantee and Maritime Liens cannot be assigned to one of the other available risk codes and so risks in these classes would be coded FG.

Where a managing agent is considering a risk but is uncertain as to whether it falls within the definition of Financial Guarantee insurance, the managing agent should discuss it with its Syndicate Performance Manager.

<u>Assignment of policy</u>

All Credit and Financial Guarantee policies (in whichever of the risk codes listed above) must contain a condition that only allows assignment of the policy with the prior written agreement of underwriters. Where assignment of a policy does take place, the obligations placed upon the original insured by the terms of the policy must be transferred so that they become obligations of the assignee.

It is acceptable to allow for the proceeds of a policy to be paid to a third party provided that the obligations on the insured under the terms of the policy remain with the insured.

Insolvency of the Insured

All policies must contain an exclusion in respect of any loss arising from the insolvency of the insured. In a number of territories or classes it is recognised that market practice may mean that a full exclusion is not achievable (examples of such classes include Japanese contingency, aviation contingency business, and (re)insurance of Export Credit Agencies). In such cases Lloyd's, on a request received from the managing agent (either as part of the business plan agreement process or for individual risks outside the business plan), may agree with the managing agent the use of clauses that do not provide a full exclusion. Lloyd's will also agree the scope of business that can be written on this basis.

Delegated underwriting

Other than where delegation is to a service company coverholder, Lloyd's is unlikely to agree plans for the writing of Credit and Financial Guarantee business in any of the products listed where the risks are bound by way of delegated underwriting. This includes, in particular, binding authorities and line slips.

Accelerated payments

Where policies provide for the insured to be indemnified for the non-payment of a financial obligation by the obligor where the obligation in question involves the obligor making a payment at a future date or a number of payments over time (for example the re-payment of a loan in instalments) then it will be usual for the insurance backing the obligation to pay out over time in accordance with the original payment schedule. Lloyd's may agree in appropriate cases to the inclusion of provisions for the making of accelerated payments at the sole election of the insured. As a general rule, however, underwriters should, in each case, have the opportunity to agree or decline to make the accelerated payments.

Fraud

Subject to any local legal or regulatory requirements, all policies must contain a clause, or clauses, to the effect that the insurer shall have at least the remedies available under the Insurance Act 2015 in relation to fraudulent misrepresentation and fraudulent claims.

In s8/Schedule 1, the Act sets out that if a qualifying breach of the duty of fair presentation was deliberate or reckless, the insurer (a) may avoid the contract and refuse all claims, and (b) need not return any of the premium paid.

In s12 the Act sets out that if the insured makes a fraudulent claim, the insurer (a) is not liable to pay the claim, (b) the insurer may recover from the insured any sums paid by the insurer to the insured in respect of the claim, and (c) in addition the insurer may by notice to the insured treat the contract as having been terminated with effect from the time of the fraudulent act.

Contracts of surety

Underwriters are reminded that, while underwriters at Lloyd’s can provide reinsurance to non-Lloyd’s firms in respect of business they undertake as licensed surety bond providers (Risk Code SB), Lloyd’s does not currently permit the direct writing of these contracts of surety, without prior approval from Lloyd’s Market Performance team. Additionally, licensing restrictions apply to this class in most jurisdictions.

Proposals that are unlikely to be agreed

In view of the nature of the risks involved, managing agents should note that Lloyd’s is unlikely to agree plans that involve the writing of the following types of risks:

- Where the underlying risk is a tradeable instrument or a contract for difference.
- Where the primary risk is price risk rather than credit risk, for example:
    - Currency fluctuation risk.
    - Commodity price fluctuation risk.
    - Any Agricultural revenue protection product (under risk code AG or HA), with the exception of U.S. Multi Peril Crop Insurance reinsurance that is subsidised by the Federal Crop Insurance Corporation.
    - Financial market fluctuation risk.
    - Property/land price fluctuation risk.

6. Further information

If managing agents write or wish to write these perils/products and have any questions regarding the additional risk codes or the process to follow, they should contact Lloyd’s Head of Specialty at mateo.rubio@lloyds.com and/or the Class Underwriting Performance and Solutions team at underwritingoversight@lloyds.com.