

FT REPORT - WEEKEND MONEY: Lloyds acts like a beacon once more to investors

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Investing in Lloyds of London is in fashion once again as wealthy investors try their hand at personal underwriting in an attempt to find returns that are not correlated with equity markets.

"Names" - the private investors who underwrite Lloyds with their own money - insist the performance of the world's largest insurance market has improved markedly since the early 1990s when it was pushed to the brink of bankruptcy by a deluge of claims. While the risk of personal underwriting is still quite high, it is unlikely that today's investors will face the fate of the thousands who lost their fortunes when they underwrote huge losses incurred mainly from asbestos claims, analysts say.

"Serious high net-worth individuals are beginning to come into the market," says Michael Deeny, chairman of the Association of Lloyds Members, the Names trade group. "You do have to accept that this is a high-risk business. But Lloyds turned a corner at the beginning of this decade. Its performance has improved tremendously and the level of risk has been reduced."

About 2,500 private investors now underwrite about 16 per cent of the £15bn Lloyds has in capacity.

The costs of investing in the market are high, as investors must have at least £400,000 in assets, which is used as collateral, and about £200,000 in cash, which is used to buy the rights to participate in the profits of syndicates. In addition, another £7,000 to £10,000 in cash is required to start a limited liability partnership (LLP).

Each September, auctions are held to determine who underwrites what percentage of a particular syndicate's capacity for the following year. Last September, the highest price paid for capacity was 71p for £1 worth of underwriting capacity in Syndicate 386, the non-marine liability syndicate which has reported strong returns in recent years. The lowest was 0.14p per pound of capacity in Syndicate 4040, a writer of employers' liability insurance. "If you are new to the market, you might have to spend £200,000 in cash to buy £1m worth of capacity," says Deeny.

High net-worth investors are attracted to the market for several reasons. Losses are now capped as investors can now underwrite a group of syndicates through a LLP, which means the maximum loss they face will be restricted to the amount of capital pledged upfront.

A second benefit is that assets invested in Lloyds can be used twice to achieve returns. For example, an investor could put up say, a buy-to-let property or a share portfolio as collateral. This allows the investor to earn a double return on their asset. The structure also permits wealthy investors to keep assets used as collateral or to fund the purchase of capacity rights out of their inheritance tax net after two years. Also, any losses can be offset against income tax.

Another perk is that yearly profits of up to £235,000 can be transferred tax-free into a self-invested personal pension.

Since 2001, when Lloyds reported a loss of £3.1bn in the wake of the attacks on the World Trade Centre, the market's results have been strong. Deeny reports that he and many of his fellow Names even made small profits in 2005 - the year Lloyds reported a loss of £103m for hurricane-related claims. Lloyds' results were particularly strong in 2002, a year the FTSE 100 fell by 24.5 per cent.

The only way to go about investing in the yearly cycle of a Lloyds' syndicate is to approach one of the two main member agencies - Argenta Private Capital and Hampden Private Capital. These

groups can set up LLPs and at auction represent clients looking to invest in particular syndicates.

About 30 of the 66 Lloyds syndicates are open to private investors.

How to make a Name for yourself

Interested in investing in Lloyds? First contact Hampden Private Capital (www.hampden.co.uk) or its rival Argenta (www.argentapl.com).

These member agencies channel private investors' money into the Lloyds underwriting market. Next September, they will represent clients at the three auctions which allocate the underwriting of the 30 Lloyds syndicates open to private investors in 2009.

Investments must be made for at least three years to be economic. The policies you underwrite in a particular year are "live" for three years, which means you can face past losses.

A limited liability partnership can be set up by Argenta for £7,500. The agency charges a 1 per cent fee on capacity of up to £1m and 0.5 per cent on capacity from £1m to £1.5m. About £350,000 in capital permits underwriting about £875,000 worth of capacity. It cost £175,000 to acquire this amount of capacity at the 2007 auctions.

If you make a profit in an underwriting year, Argenta will claim 5 per cent of it.

If you were to earn a profit of 12.5 per cent in a particular year, your gross profit on capacity of £875,000 before fees and commissions would be £109,375.

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