Insight and Intelligence on the 2016 Reinsurance *Rendez-Vous* de Septembre

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ProSight owners consider exit

The two funds behind US specialty carrier ProSight are gearing up to sell the business after waiting right until the end of the typical private equity life cycle, *The Insurance Insider* has learned.

Goldman Sachs' private equity arm GS Capital Partners owns a controlling 50.1 percent stake in the insurer, with TPG Capital and staff believed to hold the balance.

Goldman has hinted at a sale a number of times, with discreet enquiries made to identify a buyer, but a more concerted effort to divest is now believed to be underway.

The work is in its early stages, but the investment banking arm of Goldman Sachs is expected to secure the sell-side mandate.

Banking sources were divided on ProSight's options. Some believed that Goldman will look to run a dual-track IPO and sales process.

CEO Joe Beneducci has always been adamant that ProSight's future lay in the public markets, and Kinsale – which is now trading up towards twice book – has demonstrated investor appetite for specialty insurance stocks with strong operating results.

Others stressed, however, that ProSight had a more chequered record where top line growth has not been matched by the bottom line and the business has moved into the red over the last 18 months – necessitating a sale to trade or private equity.

Goldman Sachs' private equity arm is expected to bring the business to market in the final quarter of this year or the first three months of 2017.

The investment firm is also currently marketing its almost 20 percent stake in legacy-to-live carrier Enstar, with both pieces of corporate activity likely to reflect its need to close off a 2007 fund that houses the investments.

ProSight Specialty Group, the immediate parent company for the three rated US platforms, has shareholder surplus of $517mn. The overall group also owns a Lloyd's platform.

Syndicate 1110 had a stamp capacity of £210mn ($280mn) for 2016, which remained unchanged from the previous year and implies around £145mn of funds at Lloyd's using a rule of thumb estimate.

ProSight has grown at a breakneck speed since it was founded, substantially levering its balance sheet in the process.

In 2011, the firm's US platforms wrote just $251mn of business. By 2015 this had increased almost threefold to $724mn.

The Lloyd's platform also wrote £212mn of gross premiums in 2015, although around two thirds of this was US programme business routed through the syndicate via reinsurance arrangements as a capital efficiency tool.

This implies gross written premiums of roughly $830mn for the whole group.

Capital has not grown at anything like the same rate, giving ProSight a significant advantage versus its peers in terms of underwriting leverage. This in turn renders the business attractive to private equity firms looking to extract maximum value from the capital base.

Profitability has, however, been an issue. The US business fell to a modest loss in 2011 before producing slim profits in 2012 and 2013.

In 2014 there was a strong upswing in US profits to $37.3mn, with ProSight Specialty Group achieving a double-digit operating return on equity. The business seemed as if it could be on course to improve its underwriting result and take advantage of that leverage boost to give the private equity owners a good run into an exit.

But the results turned against ProSight in 2015, with a $13.8mn full year loss in the US business. This continued in the first half of 2016 with a $5.0mn loss, leaving the owners needing to sell out at a time when the numbers have moved in the wrong direction.

The difficulty for ProSight and its

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INSIDE

The Andrex market

The power of a good metaphor should never be underestimated.

We journalists are connoisseurs of the form, sifting, sorting and storing neat similes away in our memory banks for future use. Sometimes it's just for the sheer joy of words and the images they can conjure up.

For instance back in the fourth quarter of 2005, when Katrina, Rita and Wilma (KRW) had done their worst, the then independent reinsurance broker Benfield coined a phrase that perfectly described the market of the day.

It called the post-KRW environment a crème brulée. It was perfect, for the famous French dessert had a hard caramelised top that sat above a soft and creamy underbelly. I was so taken with the metaphor I put a picture of one on the cover of *Reinsurance Magazine*.

KRW had landed hard on the US cat market, singeing it to the point that a whiff of burning could be detected as programmes were totalled and overtopped.

But while KRW had burnt off the top of US cat it had not displaced anything like enough capital to change pricing in the rest of the world. We had true market differentiation for the very first time. It was a tasty concoction, with plenty of profits to go round for everyone able to reload capital.

KRW also landed into a soft market for money in general, with capital and sources of funding abundant and the pre-financial crisis asset boom in full swing. Start-ups and sidecars soon chipped away at the pleasing crunchy brulée parts of the crème and by 2008 it was indistinguishable from a soft crème caramel.

The trouble is that, barring brief pauses for the 2010-11 cats, that crème caramel has been getting soggier and slightly less sweet year on year.

It's time for a new metaphor.

> "Welcome to the longest and strongest soft market of any of our careers"

Last week we kicked off the Monte Carlo season with our 11th pre-Monte Carlo executive briefing in London.

As chair my job is always to do a bit of scene-setting. I've been doing this for the last eight years and because the market has softened overall in every single one of them the tone of my intro has become progressively downbeat as time has advanced.

So this year, instead of rattling off the usual litany of things that were wrong with the market I decided to resort to visual humour.

I explained that in the Insider offices we had started circulating amusing pictures of cute puppies as a way of providing light relief from our day job of confronting the increasingly unpalatable truths that abound.

So we set ourselves a challenge – could we find a metaphor in the modern medium of humorous dog photography that would adequately express the state of today's reinsurance market without causing alarm and any more undue stress?

Yes we could.

The image we found was from a famous UK ad campaign for Andrex (Scottex to some) toilet tissue that has become synonymous with the brand since the 1970s.

In it, a cute beige labrador puppy is nuzzling a roll of Andrex under the slogan "soft, strong and very, very long".

"Welcome to the longest and strongest soft market of any of our careers," I announced to a stunned crowd of 400.

One only hopes this Andrex market proves anything like as absorbent as its namesake.

Unpleasantness is accumulating at an alarming rate and when the reckoning arrives the clean-up will be prolonged and highly challenging.

In such tough times any everyday comforts we can find will be highly prized. No wonder my stunt was met with nothing more than a muffled ripple of nervous laughter.

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owners now is that the narrative of rapid growth followed by improved operating performance and enhanced returns is not in place.

Meanwhile, the carrier's Lloyd's platform, which it acquired in 2011, is yet to turn a profit.

The syndicate has, however, been creeping towards breakeven point, reporting a £3.2mn loss for 2015 in an improvement on the £5.5mn loss it recorded in 2014, while the top line has surged from £53mn in 2010 to £210mn in 2016.

Goldman Sachs is likely to argue to prospective acquirers that ProSight would offer a sizeable US specialty market presence focused on programme insurance business, ensuring entry to an attractive sector with relatively little exposure to the weakest areas of pricing such as reinsurance and big ticket risks.

In addition, the business has a Lloyd's platform complete with managing agency at a time when there is significant scarcity value in such assets.

All this, along with the underwriting leverage, could make the firm attractive to a diversifying Bermudian, or to Asian money.

It is also possible that Goldman will break ProSight in two to realise maximum value. However, given the extent to which the US and Lloyd's businesses are interdependent, a long-term reinsurance deal might be necessary to persuade a buyer to take on the managing agency.

ProSight was created in 2009 by Goldman Sachs and TPG and was used as an acquisition vehicle for listed carrier New York Magic, with former Fireman's Fund executive Beneducci heading up the company.

New York Magic was taken private in the second half of 2010 after a deal was agreed that valued the business at $230mn, or roughly book value.

ProSight then acquired failing Lloyd's bantamweight TSM for a nominal consideration in 2011.

The Lloyd's unit in particular has had issues with staff departures, with most of the senior roles turning over twice in the time that ProSight has held the asset.

And last year in the US ProSight lost Tim McAndrew's marine team – considered by many to be the core of New York Magic – to StarStone.

Goldman Sachs and TPG declined to comment. ProSight could not be reached.

Insurers turn to legacy-to-live reinsurance to free up capital

There is a growing interest from insurers in structuring reinsurance transactions that help release capital tied up in reserves, in a bid to make their balance sheets more efficient and maximise returns, *The Insurance Insider* can reveal.

According to sources, structures under consideration include loss portfolio transfers (LPTs), adverse development covers (ADCs) and hybrid reinsurance deals that combine retroactive solutions with an ongoing cover.

Where insurers have often looked at traditional run-off solutions to shed liabilities on business lines they have exited, the emerging strategy can also be applied to portfolios of business in which they are still active.

A senior reinsurance broker told this publication his firm is working on new transactions after completing a deal earlier this year.

"You can do a legacy deal and a traditional deal all in one go for a client. It's about getting more utility out of reinsurance," he said.

Transactions have to be structured with separate sections for the retroactive and prospective elements of the cover because of the different accounting treatments applied.

"But overall you're getting more leverage with the reinsurer because of the size of the transaction," the executive continued.

The potential demand is likely to be a key driver behind the evolution of the total return reinsurer model to target legacy and live business, as demonstrated by Enstar's Aligned Re start-up and the vehicle that former Ace reinsurance buyer Bill O'Farrell is working on with Arch.

In the pervasive low interest rate environment, the cost of holding reserves on the balance sheet for live or legacy business is effectively higher because insurers are unable to generate adequate investment returns.

"Insurance companies are only getting 1 or 2 percent on their money, but some offshore entities can do better than that," said a senior industry source.

"If you can create the right vehicle you can actually entice companies to shed their long-tail reserves and free-up capital. And if interest rates stay where they are I think you'll see more of these deals," he added.

Reputational risk

Historically, one deterrent to insurers trying to free up capital with legacy solutions has been the reputational risk in relation to willingness to pay claims.

The aggressive commutation strategies employed by some traditional run-off practitioners have left live carriers wary of damage to their brand if they transfer prior-year liabilities from their balance sheets.

But there are already examples of where innovative partnerships between live and legacy carriers can help prevent such issues, and achieve the goal of improving capital efficiency.

Earlier this year, Enstar agreed a deal to write a 50 percent reinsurance of a $2.2bn legacy book belonging to Allianz.

The transaction, which relates to an old Fireman's Fund book, sees the Bermudian write a quota share, while the German insurance giant's Allianz Re unit keeps 50 percent of the book and employs Enstar to help manage the legacy claims.

By keeping significant "skin in the game" on the legacy book, Allianz retains an element of control over the way the claims are being paid. Sources have suggested the approach can also be applied to live books of business, where some or all of the claims process remains in the hands of the cedant, but the liabilities are housed on the offshore balance sheet and provide float for the reinsurer's asset management strategy.

As well as LPTs, insurers can also get significant capital efficiencies from ADCs, which are viewed as particularly "BCAR friendly" in terms of the relief they provide under AM Best's capital adequacy ratio adjustment model.

High profile examples of ADC covers include Liberty's deal to buy $6.5bn of aggregate limit for its US workers' compensation, asbestos and environmental liabilities from Berkshire Hathaway two years ago. The latest examples of legacy-style reinsurance deals to free up capital are not restricted to long-tail liabilities however.

This summer, Sirius' legacy arm Global Solutions is understood to have been involved in a reinsurance transaction that helped facilitate Florida Specialty's acquisition of Mount Beacon.

The deal is thought to have involved Sirius assuming a legacy book of homeowners' business for the Florida carrier, as it looked for a clean slate without the capital commitment to build its platform of ongoing business.

Insider View: From a position of strength

Combining ongoing reinsurance support with a legacy-style solution is nothing new in itself.

Indeed, Berkshire Hathaway has been the master of such transactions, including the adverse development cover (ADC) and 20 percent P&C quota share it wrote for Swiss Re when the reinsurance giant was capital-constrained in the aftermath of the credit crisis.

Meanwhile, earlier this year Australian carrier IAG entered into a new ADC with the investment conglomerate's reinsurance platform after signing a 10-year 20 percent quota share deal with the firm only last summer.

However, students of Berkshire Hathaway's reinsurance strategy over the years will be well aware that Ajit Jain and his team will usually only enter such arrangements if the economics of the deal are stacked heavily in their favour.

And both examples are of insurers looking for a solution to free up capital from a somewhat distressed position.

However, today the prospect is of a growing number of transactions that involve carriers with strong balance sheets looking to take advantage of a willing reinsurance market to make their capital model more flexible and efficient.

With no prospect of investment conditions significantly improving in the near- to medium-term, insurers can look offshore to transfer reserves that can be more efficiently housed on the balance sheets of traditional and total return reinsurers hungry for growth.

They can also use their position to leverage buying power by combining legacy and live transactions with those counterparties willing to write them.

Marlin goes live with MS Amlin as main lead

Aon Benfield's $600mn Latin American facultative facility, Project Marlin, is now binding risks with support from half a dozen Lloyd's insurers, *The Insurance Insider* can reveal.

Most of the facility, which provides Aon Benfield with a 15 percent line on Latin American fac business, is led by MS Amlin – in a deal brought to the table by Mitsui Sumitomo's Syndicate 3210.

The other participating markets are understood to be Travelers, facilities stalwart Barbican, StarStone, Neon and Hiscox, which is ceding a significant share of its line to the Brazilian state-owned reinsurer IRB.

Aon Benfield had originally been targeting a launch at the start of this year, but ran into delays and chose to modestly scale back the scope of the portfolio as the project progressed.

The final deal with the Lloyd's insurers excludes aviation, as well as personal accident, fidelity, surety and life, dragging down the subject premium from $700mn closer to around the $600mn mark.

Aon's reinsurance broking arm is likely to be criticised by some corners of the market as the big three intermediary again brings forward an initiative likely to charge brokerage more than the current status quo.

According to the original marketing documents, obtained by *The Insurance Insider* in January, the broker was set to charge a 12.5 percent work transfer or MGA fee and a coverholder brokerage of 5 percent, in addition to a standard open market slip commission. However, in this instance – and unlike with some other facilities in the market – the criticism rings hollow as Lloyd's carriers are being asked to pay to access business entirely new to their market.

The Marlin book is dominated by property exposures. The marketing documents showed that $367mn of the portfolio was property, with a further $146mn coming from marine and energy lines.

In-scope business also includes $49mn of casualty premiums, $26mn of professional liability business and some power and motor risks. The initiative is being led by Aon Benfield's chief broking officer for Latin America Pablo Muñoz, Aon ReSolutions managing director Andrew Matson and Jon Hughes, senior broker with the firm's Global ReSpecialty team.

In a statement to *The Insurance Insider*, Matson said: "The idea behind Marlin was to engineer a mechanism to join two groups together for their mutual benefit.

"For Latin American clients it brings new high quality and diversifying capital to the table, while it allows the Lloyd's carriers to access regional business that would never come to London in an expense-efficient way."

After being approached for comment, MS Amlin CUO Simon Beale said in a statement: "The facility provides international markets with direct access to the Lloyd's market, underpinning its status as the global hub for specialist risk solutions."

Insider View: Project Marlin

From one perspective Project Marlin is another data point that helps demonstrate the inevitable progression of facilitisation, as brokers carve up the market and leverage their position to hold up their own margins.

But the development is in many ways much more interesting than that paint-by-numbers view that you could hear in any bar in EC3.

This is because it is an example of premium that Latin American brokers were quite happily placing with their local underwriting counterparts being packaged up and matched with willing but previously inaccessible London-based capital.

Marlin takes advantage of the leap forward in data quality and the normalisation of portfolio underwriting to create a capital bridge between London and Peruvian risks. In so doing, it levers down prices for its clients, serves up new highly rated paper, and – most interestingly – offers one possible answer to Lime Street's great distribution challenge.

Vision 2025, with its emerging market Lloyd's start-ups and boots-on-the-ground approach, may be facing in totally the wrong direction.

Instead, the solution could be the greater use of data-driven facilities in partnership with the brokers, mobilising the market's unparalleled network of licences; or virtual distribution plays like Aon Carrier Link for Lloyd's that offer underwriters a greater level of control.

Both answers to a regionalising specialty market will continue in tandem no doubt, vying for mastery.

Latin America is just one of the world's regions under-served by London capacity. We have no specific information, but you can bet Aon has further initiatives in the pipeline.

Farmers cat programme set to renew down 5%

Farmers, the biggest US catastrophe reinsurance programme placed between 1 July and 1 January, has priced with a risk-adjusted rate reduction of around 5 percent, *The Insurance Insider* understands.

Sources told this publication that the $1.6bn excess $400mn core treaty remains unchanged, with an underlying second event cover and some cascading features on higher layers.

It is understood that exposures are down somewhat year-on-year at Farmers, which traditionally places its cover months ahead of its 1 January inception.

Indeed, with terms only just out in the market, underwriters are talking about it as a late placement this year.

In an illiquid market with few pricing indicators more reliable than conference rhetoric, Farmers tends to be a closely scrutinised renewal as a predictor of the US cat market at 1 January.

Some, however, believe that it would more appropriate to see it as the tail of the mid-year renewals rather than the leading edge of 2017.

At around 5 percent down, the deal is somewhere in the middle of the pack when benchmarked against mid-year US cat renewals. There is no longer any question that US cat reinsurers have given most of the ground up that they will be forced to. But it remains to be seen how quickly the market reaches a stage where there are genuine as-expiring renewals – and just how close it comes this year.

Most reinsurers concede privately that they will have to let the brokers have a few more points this year, but seem determined to hold it to that and ensure that the appreciable slowing of rate reductions continues.

InsurTech capital could disrupt insurance market: Aon Benfield

Capital influxes from InsurTech businesses could fundamentally change the structure of the insurance industry, according to Aon Benfield.

Speaking at a press conference at Monte Carlo yesterday, the broker's global analytics CEO Paul Mang said entrepreneurial capital from start-ups could significantly disrupt traditional companies in the sector.

Insurance ventures had attracted more than $9bn of capital over the past few years from both traditional venture capital firms and insurers' corporate venture units, Mang continued.

Nascent start-ups are spotting opportunities for growth despite the perceived challenges dogging the industry, he added.

"They are not investing the $9bn to look at what we are doing now; they are investing to see what the industry could look like going forward," Mang said.

Aon Benfield CEO Eric Andersen also touched upon the increased use of facilities in the industry and the importance of internal analytics in providing broader risk pools for carriers.

Andersen added that facilities granted customers increased claims certainty and access, and would be an area of continued focus for the broker in future.

Dominic Christian, executive chairman of Aon Benfield International, noted that facilities had evolved from single-track ventures into strategic large-scale enterprises dependent on data in a way that was not possible before.

> "We have to differentiate quite strongly between facilities that are around just because we can be, because we are in a soft market, and those which are strategic in form"
>
> *Dominic Christian*

Aon Benfield had sought to talk to regulators and Lloyd's while developing their facilities in order to manage regulatory risk, Christian continued. He added that those facilities that simply take advantage of soft market conditions stood in stark contrast to longer-term strategic initiatives.

"We have to differentiate quite strongly between (facilities) that are around just because we can be, because we are in a soft market, and those which are strategic in form," Christian said. "Those that aren't are much more attached to the regulator."

CEO Andersen added that, thus far, simple commission structures had been used to charge carriers participating in facilities as they were easier to disclose to clients, but that it was possible the company would consider other ways of splitting out fees for data services in the future.

The broker also forecast continued expansion in reinsurance demand – including in the key property catastrophe market – after noting a modest increase in purchasing for the first time in some years in 2015.

Overall premium ceded went up from $73bn in 2014 to $80bn last year.

Regulatory changes were driving some of the increase, said the firm's international market analytics head Mike Van Slooten.

He added it was difficult to quantify potential increased demand, and noted that some buyers were still consolidating programmes and removing premium from the market.

But the balance has tipped, he continued. "The gap between reinsurance supply and demand has narrowed."


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Quota shares offer cedants expense relief: Scor

Increased demand for quota share covers in the last year reflects cedants' need to lay off some of their costs to reinsurers as the soft market bites, according to Scor's P&C CEO Victor Peignet.

Speaking at the reinsurer's Monte Carlo press conference, the executive commented:

"We have seen in the last six to nine months that the quota share premium that has come to the market has increased considerably."

Peignet added that the incremental increase in reinsurance demand was also a function of cedants' need to take out volatility that investors would not tolerate with lower returns on equity (RoEs).

"If your RoEs are reducing, then they need to stabilise [those returns]," he said, continuing that reinsurance was the obvious mechanism to achieve that.

Peignet went on to say that the number of market players was much more of a problem than the excess capacity currently in the industry.

"When you have too many mouths to feed and some are more starving than others, while others will eat anything, all of this can create problems," he said.

"Let's focus on the number of players, which in my opinion is the real problem."

Peignet added that some specialty lines had been hit by the instability in the macroeconomic environment.

"You can see that people working in certain lines of business such as trade credit and surety, marine, and energy, are really affected by the slowdown," he said.

The executive added that it was obvious why shipping and trading lines were under pressure when one looked at what was occurring in those industries.

"The number of countries that are not able to launch infrastructure projects anymore, some of them now have debt levels that are totally out of proportion with their capabilities.

"Those double effects mean that the difficulties in these lines of business will be with us for a long time," he continued.

The Scor executive also told attendees that he did not think that the UK would leave the European Union.

Adding that he was speaking in a personal capacity, Peignet said: "I don't think it will happen."

Scor CEO Denis Kessler said that reinsurers could weather many storms, including Brexit and the low interest rate environment.

He argued that the industry had proven time and again that it was resilient.

"We've faced a lot of headwinds and when it reverts [back to a high interest rate environment] then we will benefit."

Reinsurance growth to be only 1%: Munich Re

Munich Re has predicted that the global reinsurance market will grow at a rate of just 1 percent per year between now and 2018.

At the end of 2015 total ceded premiums were around EUR251bn ($282bn), having grown at a rate of approximately 2 percent a year since 2009.

But at Munich Re's press conference at the Monte Carlo *Rendez-Vous*, board member and reinsurance chief Torsten Jeworrek said declining reinsurance appetite in Asia is one of the main reasons for subdued growth.

In the Asia Pacific region, Munich Re expects primary insurance premium to grow at an annual rate of 6 percent to 2018 but reinsurance premium to experience zero growth.

China's new C-Ross solvency regulation, which has decreased the amount of capital required for motor business in particular, has had a negative impact on reinsurance buying, he explained.

"There will be reduced reinsurance volumes in the Chinese markets in the coming years," Jeworrek said. "The need to cede in the reinsurance market will probably reduce," he added.

More widely, available reinsurance capacity is still high, which continues to suppress rates and premium growth, the executive continued.

"In the July renewal we saw positive signs that the speed of rate reductions did not accelerate further," Jeworrek said. "Hopefully, this is the first sign of stabilisation in the market."

Looking longer term, Munich Re highlighted cyber reinsurance and epidemic reinsurance as growth areas.

Thomas Blunck, board member responsible for special and financial risks, said: "The level of digitalisation has gone so far that the loss exposure goes beyond [existing] cyber covers. We are now talking about physical loss, reputational loss, business interruption and bodily injury."

Munich Re is trying to push the development of cyber reinsurance as a standalone cover so that carriers can offer more bespoke solutions for different industries and can attain a better understanding of the risk, Blunck continued.

"We would like to grow in this area, but very cautiously," he said. "We're entering with very low limits. Our average capacity [for cyber] is one 20th of what we normally do for property business."

This limit will increase as understanding of the risk grows, Blunck said.

Growing into niche areas will position Munich Re well if and when the market turns, Jeworrek added.

The executive said cat losses like those seen in the first half of this year would not be enough to turn the soft reinsurance market.

"My view is that there is permanently enough capacity in the market [to absorb cat losses]," he said.

The reinsurance market will need to see deteriorating earnings, a drying up of reserves and then additional cat losses for there to be any impact on the current pricing environment, Jeworrek added.

ACR will emerge stronger after ownership change: Gerhardt

Asia Capital Re (ACR) has not suffered heavily from the uncertainty caused by its auction process and will be in a better competitive position on the other side of a sale, CEO Hans-Peter Gerhardt has told *The Insurance Insider*.

Gerhardt was speaking in an interview at the Monte Carlo *Rendez-Vous*, the day after this publication broke the news that ACR's backers had agreed a deal in principle to sell the reinsurer to Chinese provincial government-owned entity Shenzhen Qianhai Financial Holdings for $1bn.

The ACR CEO point blank refused to discuss Shenzhen Qianhai Financial, or to confirm whether or not a deal was in place.

"I cannot talk [about] specifics at this stage," he said. "It wouldn't be appropriate. As you would expect, given the length of time since the board decided to initiate this process, we are drawing towards the concluding stages of what we were doing."

Gerhardt stressed that the sale of the business, once approved by the regulators, would remove an obstacle that ACR has always had to deal with in the decade since it was founded.

"ACR has been owned by a group of financial investors and after a deal it should pass into the hands of a strategic owner, which creates certainty for staff and clients, and allows us to take a long-term approach to running the business," he said. "This will be a great next step for ACR."

"We are trying to bring a secure and very bright future to the company – to both clients and employees."

There had been some short-term strain placed on the business, but the company has weathered this well, Gerhardt said.

"I have worked very closely with clients to answer questions and assure them of our future, and we haven't lost meaningful business over this process," he said. "Clients have been very loyal."

Over 90 percent of ACR's cedants have been with the company for more than five years, something that Gerhardt said demonstrated the mutual loyalty of the relationships.

He stressed the continuity in offerings that its client base could expect when its current owners, including 3i and Marubeni, have sold out.

"ACR doesn't expect any change in ownership will reduce its risk appetite or capacity – it should give us the opportunity to do more for clients."

He continued: "The staff have taken the same loyal approach, with internal transparency as well as incentives that we have put in place helping us to keep attrition well below Singapore standards."

Gerhardt, who became CEO in November last year, argued that the bigger challenge for ACR was the struggle to hit return hurdles in a hugely competitive market.

"Over time the company needs to shift business mix from overweight proportional property treaties to more specialty lines business, and facultative and excess-of-loss," he explained. "That shift will give greater margin, even if we have to accept more volatility."

The former Paris Re CEO also gave an early indication that he intended to re-examine the reinsurer's almost exclusive focus on Asian markets.

"We will keep our 'In Asia. For Asia' approach, but we may need to refine the model and extend our reach more broadly once the dust settles," he said.

Gerhardt said that a single region focus was even harder in Asia than elsewhere as it was difficult to balance major cat exposures in Japan and China with other territories.

He went on: "The regional business model is a real challenge in an age of scale when you're competing with the mammoth reinsurers."

Looking ahead to 1 January, the CEO of Singapore's biggest reinsurer forecast a challenging market for risk carriers.

However, he said that he expected evidence to emerge that Asia was following the trajectory taken by the US, with a moderation of rating pressure.

"We are in a soft market now that is reaching its trough," he said. "I am confident that reinsurers in Asia are realising that margins are thin and that there is simply not room for further concessions."

Stone Ridge pursues Lloyd's access

Top 10 ILS manager Stone Ridge Asset Management is working to establish or acquire a Lloyd's corporate member, a vehicle that would allow it to invest in London market syndicates, sources told sister title *Trading Risk*.

The move continues a trend of ILS managers seeking access to Lloyd's, which provides the benefit of leveraged access to its rated platform.

Corporate members are used to provide syndicates with capital to support their Funds at Lloyd's requirements – effectively meaning investors take a synthetic capital stake in the syndicates and share in their net results across the three-year system of Lloyd's accounting.

One advantage of taking this route into Lloyd's is that it does not require full collateralisation against capital commitments. Instead, the capital requirement is tailored to the individual member's portfolio and calculated by Lloyd's.

If its plans are enacted, Stone Ridge would become the fourth ILS manager with direct market access, rather than just reinsuring Lloyd's carriers.

Nephila was the first to set up a syndicate in late 2013. Turnkey provider Asta assisted with the launch of Syndicate 2357, which began writing in 2014 with £72.5mn ($96.2mn) of stamp capacity, which has grown to £121.7mn for the current year.

Securis then set up a corporate member that began investing in 2015 and has since set up a special purpose syndicate with Novae. The US property excess and surplus lines syndicate has $94mn of total capacity, of which $75mn is ceded to Securis.

Finally, Credit Suisse Asset Management gained its own syndicate – Arcus Syndicate 1856 – this year, graduating from a special purpose syndicate that had supported Barbican. It has £90mn of stamp capacity in its inaugural year and retains a relationship with Barbican, allocating a portion of the portfolio to a quota share with its fellow Lloyd's insurer.

Stone Ridge has grown quickly since its launch in early 2013. It runs two mutual funds and one illiquid fund that invests in cat bonds and reinsurer sidecars, with collective net assets of $4.76bn as of 30 April 2016.

Stone Ridge declined to comment.

'Brexit-proof' R&Q prepared for UK's EU exit

Randall & Quilter (R&Q) plans to use its multiple platforms to position itself for new business, regardless of how the UK's Brexit negotiations play out.

The specialist legacy-to-live manager took the decision nearly four years ago to redomicile its group headquarters to Bermuda. Since then R&Q has been developing a number of underwriting platforms, including its Lloyd's turnkey managing agency, a class 3A reinsurer in Bermuda and R&Q Insurance Malta. It has also acquired A-rated Accredited Surety and Casualty Company, a US admitted insurer.

As chairman and CEO Ken Randall explained, the Maltese platform means that regardless of the outcome of the UK's Brexit negotiations, R&Q will be able to continue to undertake deals throughout Europe.

"We are very Brexit-proof in that we are Bermuda-domiciled and supervised as a group by the Bermuda Monetary Authority. We also have our primary European Union (EU) insurer/consolidator based outside of the UK in Malta," he said.

In the UK, there remains a level of uncertainty as to how the decision to leave the EU will impact the insurance sector, including the effect on cross-border legacy transfers.

"In the event that it is not possible to continue transferring UK legacy portfolios to Malta, we will look at using one of our existing UK companies as a future consolidator for such business," Randall explained.

He added that his hope was that the current terms of trade would be maintained.

"We are unable to say with any certainty what the outcome for Part VII transfers will be given the early stage of Brexit negotiations. The best outcome would be the continuation of the status quo, which would make sense given the standardisation of solvency regimes through Solvency II," he said.

R&Q works with a number of insurers that are not licensed to underwrite EU-domiciled insurance risks. Its Maltese insurer, which has a Solvency II capital ratio of more than 250 percent, provides a facility to enable such carriers to continue holding EU risk but without the need for an EU presence.

Randall noted that the Maltese regulator was "accessible, responsive, well-resourced and keen to attract business". In addition, the Malta Financial Services Authority had proven prompt at producing solvency certificates for the business R&Q has transferred in, which is a vital part of its model.

Indeed, Randall said he was so pleased with the firm's Maltese operation that he is considering launching a second vehicle in the country.

"Given the number of transfers and transactions we work on at any one time, it will be useful to transfer non-UK business into a second vehicle to avoid having to continually update the independent expert during the Part VII process, which can be protracted," he explained.

"This will reduce work on supplemental expert reports and potentially speed up approvals."

AM Best holds negative reinsurance sector outlook

AM Best has retained its negative outlook for the reinsurance industry as ongoing market conditions continue to hinder positive ratings development.

The ratings agency said overall trends in the market remained negative despite the deceleration of rate declines, as underwriting margins and investment incomes continued to shrink.

An unsustainable flow of net positive reserve development, as well as pressure from convergence capital, will continue to dog the industry over the long term.

In addition, carriers are unlikely to receive any relief from the low interest rate phenomenon in the near future, as central bankers wait to decipher the full impact of the Brexit vote and the degree of economic growth in the US, the agency said.

However, AM Best noted that the impact of Brexit would probably be negligible for reinsurers, as trade restrictions between the UK and EU are not likely to impact the industry.

In addition, AM Best acknowledged that further market consolidation or strategic tie-ups with alternative capital sources had become more likely, as companies sought balance sheet scale to retain and win clients.

Returns are also likely to remain dependent on the continued benign catastrophe experience, net favourable loss development and stable financial markets to produce even low double-digit results.

Looking to the Asia Pacific region, AM Best said reinsurers there needed to grow alternative revenue sources, as the industry was struggling to meet top- and bottom-line targets.

While some reinsurers in the region have diversified into life, agricultural and other lines, the long-term profitability of the diversification remains to be seen, while overseas expansion continues to be challenging, the agency continued.

In Europe, cedants are taking advantage of the market conditions, with retention ratios down slightly year-on-year while cessions have jumped 17 percent – in contrast to markedly lower rises in premiums.

Perils adds Australia to database

Catastrophe insurance data provider Perils has extended its coverage into the Asia Pacific region for the first time with the inclusion of Australia.

CEO Luzi Hitz said the company's target was to expand into other territories in Asia Pacific. The company will make available insured property sums exposed to bushfire, earthquake, flood, hail, and tropical and extratropical cyclones in the country.

Perils will provide loss data for any events above a market loss of A$500mn ($380mn).

Data is collected from primary insurers in Australia at a Cresta postcode zone and line-of-business granularity level.

Perils product head Eduard Held said: "This will have a positive effect on the modelling and management of Australian catastrophe risk by both improving our understanding of it and by further enhancing its tradability.

"We are confident that the addition of Australia will stimulate significant new developments within its risk transfer market," he added.

Perils data can be used for industry loss triggers on industry loss warranty or insurance-linked security products.

"Perils opens up new opportunities for insurers, industry and the government and represents a significant step forward in data-driven capital innovation," said Julie Batch, chief customer officer at IAG.

"Creating vehicles that help develop alternate capital structures and encourage and support new investors to the region is critical for the health of the industry."

Qatar Re: Outlook on the upcoming renewals

What characterises the current market environment and what is Qatar Re's overall approach to it?

The surplus of capital, the paucity of returns in the capital markets and the lack of catastrophe losses have been endlessly discussed in the insurance press. We have chosen to call current market conditions "permasoft". Unless a radical event dramatically affects technical or investment results, we should not expect to see a spike in rates any time soon.

Cedants and reinsurers alike have become more sophisticated in their risk selection and in their capital modelling and have thus built more efficient portfolios. This has meant that many have been able to produce returns, albeit ones that are more and more vulnerable to unpredicted losses. Listed companies, however, are reluctant to surrender top line because of the impact it has on investor sentiment, and thus prop-up their bottom line with reserve releases.

The Prudential Regulatory Authority in the UK said recently that whilst it hopes many of the reserve releases are the product of conservative reserving in prior years, it is concerned that some are over optimistic and may not mirror the past.

In this market environment, the smaller and more agile reinsurer with less of a legacy has the advantage of not having to defend their top line. Working from a smaller base we have the privilege of being selective about the risks we write and that fit our portfolio.

Where do you see your primary focus areas for driving business forward?

Currently the most promising opportunities are in the area of project-based reinsurance, which are single, one-off transactions that can each represent a significant increment to our income.

Examples of these opportunities are where we provide capital relief, quota-share backing behind managing general agents or loss portfolio transfer cover. Much of our book is high-frequency, low-severity business, often associated with insurance innovators who have a distinct market approach to product design, pricing and distribution.

We have built our intellectual capacity to write these risks across many classes and geographies. The underwriters we have taken on board qualify through their unique knowledge and expertise. We aim to provide them with an inspiring and open environment that frees them up from the silo mentality of many of our competitors. This allows them devote their talent to these deals alongside their more regular transactional books.

What lines of business and geographies will you be focusing on specifically?

Leaving aside the project-based reinsurances where we continue to see a large potential, some of our more transactional business may retreat this year because of market conditions. Whilst our large share in agricultural business is expected to decline, our broader balance sheet and recognition as a reliable, long-term reinsurer enables us to write more long-tail business, such as casualty.

> "The smaller and more agile reinsurer with less of a legacy has the advantage of not having to defend their top line"

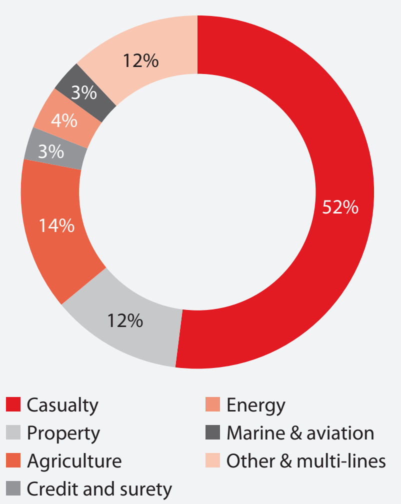
In concert with the licensing of our Dubai International Financial Centre branch earlier this year, we have built a team of facultative underwriters, mainly engineers and chemists, who have built careers in the insurance industry centred around risk assessment and technical knowledge. In combination with our parent's deep roots in the region we aim to bring much-needed leadership capacity to a disrupted market. The team will concentrate on property, engineering, energy and marine business for the Middle East and North Africa and Asia.

In the Far East and for the treaty side we have completed our groundwork and await confirmation of our branch status for our current representative office in Singapore. The growth and the increasing scope, scale and complexity of the risks emerging in Asia have been met by an over-supply of insurance and reinsurance capacity across the standard classes. We believe the region remains underserved in some niches (such as credit and surety reinsurance and structured finance) where we intend to grow by virtue of strong local connections and expertise.

Our move to become a Bermuda-headquartered reinsurer enhances the opportunity to firmly grow our footprint in North America, where we are still underweight. We will continue to grow our catastrophe business, but given the increasing recognition of our presence in Bermuda, we can see a steady pipeline of North American programme business, solvency relief deals and we also hope to start to build a small presence in the casualty line.

Alastair Speare-Cole
Chief Underwriting Officer, Qatar Re

Gross written premiums by line – 2015



Source: Qatar Re

Alternative capital has already captured significant market share in the property catastrophe space. But where else will it make inroads, and are perceptions towards it changing? *The Insurance Insider* put these questions and others to its virtual roundtable participants…

What kind of impact do you expect alternative reinsurers to have beyond the property cat market? In what lines of business will it be most felt?

The answers to this question varied based on the participants' perspective – some had a "glass half-full" view of the small steps being taken by the alternative market into new perils, while others had a more pessimistic take on the prospects for a space still dominated overwhelmingly by catastrophe risk.

"Alternative capital is already alive and kicking beyond property catastrophe reinsurance," said **Mike Krefta**, chief underwriting officer at Hiscox Re. Krefta pointed to vehicles – such as the carrier's own Kiskadee platform – that are already accepting other perils such as risk excess of loss, specialty lines and so on.

Within the cat bond space, several senior structurers pointed out that to date in 2016 the insurance-linked securities (ILS) market has already taken on deals covering banking operational risk, mortgage insurance and weather.

"Rarer and new perils should arrive either later this year or next year," said **Bill Dubinsky**, head of ILS at Willis Capital Markets & Advisory (WCMA).

Michael Popkin, co-head of ILS at JLT Capital Markets, said the firm expected to see parametric opportunities covering business interruption, contingent business interruption and adverse weather, along with life insurance-related transactions.

The ILS market could well make inroads in shorter-tail risks where demand for capacity is either very large or not met by traditional reinsurance, provided the risks can be modelled, added **Jean-Louis Monnier**, Swiss Re's head of P&C structured solutions for the UK and Africa.

> "The move [by ILS] into reinsurance will level off if rates continue to soften"

"Extreme mortality, terrorism and cyber are such risks that have either been securitised or could be in the future," he said.

Luca Albertini, CEO of Leadenhall Capital Partners, agreed that having widely accepted modelling would be the key limitation on the market's expansion into new perils, but noted potentially meaningful appetite for additional cover such as flood in key developed economies, together with operational risk, terrorism and cyber.

Other panellists noted that hedge fund reinsurance vehicles, which are now most often formed in partnership with existing underwriting franchises, are already making their influence felt in longer-tailed lines of business.

Michael Halsband, counsel at Drinker Biddle, said partnerships with specialty underwriting partners could allow alternative capital to grow into lines such as cyber or financial risk.

However, he said the correlation of these risks to the broader credit markets might be too direct.

"Shorter and medium-tail legacy casualty portfolios, if sufficiently seasoned, are more likely to be the next evolutionary step, so long as perceived portfolio certainty outweighs any potentially correlated market volatility," he added.

"Perhaps equally promising are other short-tail, homogenous personal lines – think auto – highly capable of being modelled, and for which extensive underwriting data has long been available."

Despite these promising new shoots of alternative growth outside the catastrophe markets, other roundtable participants

CONTINUED ON PAGE 19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sounded a more cautious note on the ability of the market to expand its horizons.

Brian Young, CEO of OdysseyRe, said that the capital structures and collateral release mechanisms of third-party vehicles were not flexible enough to assume business with any kind of tail over a sustained period of time.

Victor Peignet, CEO of Scor Global P&C, warned that ILS funds seeking ratings to compete on longer-tail risks would have to prove themselves for many years before having a shot at business placed with tier 1 reinsurers.

"I am sceptical that the fee structure of a typical ILS manager would allow them to make the required investments," he said. "There are exceptions but they are rare and there won't be many more in the foreseeable future."

Finally, **Amit Kumar**, senior analyst at Macquarie Group, pointed out that the alternative market had sprung up to target the perception that reinsurers were using property cat margins to subsidise other lower-priced lines of business. The alternative market's growth should level the playing fields, he added.

"The culmination of this process would be an efficient allocation of capital."

How much more market share do you think the ILS market can win within the property cat heartland?

Scor is one of the largest users of alternative capital represented in our roundtable, sourcing about half of its core retro programme from the alternative market.

Peignet said he did not expect this to change notably if market conditions continued as they were.

"Buyers don't put all their eggs in the same basket," he said. "I suspect that many buyers, like us, are unlikely to greatly increase their allocation to alternative capacities."

However, Scor's use of the alternative market already puts it ahead of the curve.

Darren Redhead, CEO at Kinesis, calculated that the $75bn alternative market had about a 20 percent market share of the $375bn of property cat limit placed.

The executive previously believed that the alternative market was reaching a ceiling on its growth, but he now thinks that the ILS sector is quickly heading toward a 30 percent market share.

"With recent innovations like (re)insurance companies starting funds using their own balance sheets to provide leverage, my view has altered," he explained. "Market share will continue to increase, but in conjunction with traditional carriers."

Stephan Ruoff, group CEO of Tokio Millennium Re, agreed that conditions were becoming tougher for alternative capital without rated paper and collateral relief, given a trend towards multi-year placements. However, he also suggested alternative providers could make up 30-40 percent of reinsurance capacity within the next few years if market conditions marginally improved.

Ruoff said that any push from ILS carriers for further market share would be tied to expected returns.

"The move into reinsurance will level off if rates continue to soften," he said. "This is why you now see managers with significant assets looking to expand beyond reinsurance and into the managing general agent (MGA) primary market. At first this was a way to get closer to the risk and access to a larger market, but now it is about better returns."

> "If ILS managers can manage the value chain more effectively than current players, there are few limits to their expansion into the primary property insurance market"

How far do you expect ILS managers to expand into the primary property insurance market?

It seems the jury is out on this one for now. Nephila Capital is notably leading the charge as it sets up infrastructure to write insurance risk, with other ILS funds skirmishing around the edges of the market. But with the sector's expansion into primary business at such an early stage, few are sure how it will play out.

"Opinion remains divided on how these pioneers will fare," said Dubinsky.

Various participants warned that there were a number of hurdles to succeeding in the primary market.

Hiscox Re's Krefta pointed to the complexities of dealing with regulators and managing claims for ILS funds entering the fray.

"Investor appetite will ultimately decide how far they expand," he concluded. "Returns are tougher in insurance than reinsurance and recoveries on most insurance lines are unlimited, unlike reinsurance."

Redhead predicted that expansion will come via partnerships with existing traditional players "who are able to leverage their balance sheets to assume attritional exposures, while the ILS players assume the catastrophe risk".

Leadenhall Capital has not yet explored the primary market in any detail, as Albertini said at this stage the company did not feel the need to compete directly with its reinsurance clients.

Ruoff took a more optimistic view, although he did note that there would be challenges and that finding the right business in the relationship-driven MGA market could be risky without experience.

"In the end, it's all about linking risk to capital and if ILS managers can manage the value chain more effectively than current players, there are few limits to their expansion into the primary property insurance market."

How many ILS managers do you expect to ultimately gain ratings?

Again, the panel diverged on this question, as the market's response to what is still a new development remains split.

Krefta questioned what the differentiating point of ILS capital would be if more franchises became rated players.

"ILS has been a hotbed of innovation and ideas providing choice for clients and a wake-up call for traditional players," he said. "I also seriously doubt whether most of those ILS players are ready for the additional cost, regulatory oversight and supervision and complexity a rated entity brings. They risk ceding their cost advantage and any sense of distinctiveness."

However, Popkin at JLT Capital Markets argued that these developments simply gave ILS managers more options to deploy capital in an efficient manner, as barriers have broken down between the markets.

He forecast more rated vehicles would emerge either through mergers, joint ventures or start-ups.

"Convergence shall continue as the rise of the reinsurance manager will ultimately result in a model where ILS managers and reinsurance underwriters become variations of one another."

However, Swiss Re's Monnier said the carrier believed further rated start-ups

CONTINUED ON PAGE 21


The name that the
biggest names depend upon.
Total Assets: US $ 12 billion
Net Worth: US $ 5.7 billion
(including US $ 3.5 billion on fair value change account)
Global Ranking (2015):
14th among Global Reinsurers (A M Best)
18th among Global Reinsurers (S & P)
Ratings:
Financial Strength: A- (Excellent) A M Best Company
Claims Paying Ability: "AAA(In)" by CARE
Website: www.gicofindia.in
Contact us at info@gicofindia.com
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GIC Re
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Global Reinsurance Solutions
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IRDAI Registration No.: 112
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would be limited.

"They focus on costs but it remains to be seen how they will perform in the long term."

Can the traditional market sustain multi-year offerings to compete with the cat bond market?

Our question was disputed by Popkin, who said competition between the two markets was not a "zero sum game".

But others saw the potential for advantages to be contested.

Kinesis CEO Redhead noted that many carriers still resisted longer-period policies, but said their rated balance sheet would permit them to sustain these offerings.

"In my view it's one of their main competitive advantages, along with the ability to offer multiple limits."

However, Leadenhall CEO Albertini said he expected multi-year covers would remain a small portion of traditional balance sheets, as flexibility was key.

> "I suspect that many buyers, like us, are unlikely to greatly increase their allocation to alternative capacities"

"Also I am not sure any board would like to explain to its shareholders that they cannot take advantage of changed market conditions because a big loss has been materially reinstated at the old market rates," he explained.

More ominously for traditional carriers writing such business, Macquarie analyst Kumar said he was not a fan of multi-year deals written at this stage of the cycle.

"This could end up being a slippery slope for the traditional market."

Does anyone believe ILS money is naïve anymore?

For our final words from the panel, we turned to an old chestnut of a question that would have prompted very different answers just a few years ago. Now, however, the responses were more moderate.

The bluntest response came from Kumar: "Yes. Those who have buried their head in the sand."

This view was heard from an ever-smaller minority, WCMA's Dubinsky said.

"Most reinsurers, brokers and cedants now accept the ILS investors as simply a growing and evolving part of the reinsurance industry, welcome in Monte Carlo, Bermuda, Baden-Baden and wherever else reinsurers congregate," he said.

"Most reinsurers incorporate ILS at multiple points in their strategy, or as the saying goes, 'If you can't beat them, join them.'"

However, others said that the true test of the market would come after a major catastrophe loss, and that there was likely to be a wide range of investor responses as the ILS market expanded its reach.

Peignet recounted that one of his colleagues at Scor was surprised to find an ILS pitch book on the desk of his parents, "who still aren't quite sure what their son does for a living".

"Another one reported that her dentist was advised by a banker to invest in ILS," he added. "Certainly some [capital] is naïve, and some quite sophisticated. We won't know how much until there is a loss or a shock."

And as Redhead pointed out, the question of what will happen after an event applies equally to traditional carriers.

"I think we all question post-event reaction of all capacity in the market. After the next 'tail' event we suffer as an industry, when we need to build additional capacity, how much of the existing investor base will stay or increase its capacity?"

Tom Parsons, divisional portfolio manager at Tokio Marine Kiln, said that the relationship nature of the reinsurance business could have led to accusations of naivety.

"One of the problems for new ILS entrants is they don't have the long-term relationships and access that traditional (re)insurers have, so they just have to accept whatever risks they can get access to. These are usually the less profitable ones, hence why it's easy to accuse ILS money of being naïve."

Drinker Biddle counsel Halsband added that it could have appeared that ILS capital was "speaking in a different language than the professional (re)insurers," but by no means was it ever naïve. "As the ILS market has evolved and matured, the level of sophistication only continues to grow."

Finally, Monnier pointed out that small size of the ILS market compared to other fixed income markets has kept it to a fairly sophisticated investor base.

"Government bond markets are in the trillions, while this market is only about $75bn, so it has clearly not attracted masses of naïve investors."

Contributors

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Divisional portfolio manager – Tokio Marine Kiln

Victor Peignet
CEO – Scor Global P&C

Michael Popkin
Co-head of ILS – JLT Capital Markets

Darren Redhead
CEO – Kinesis

Stephan Ruoff
Group CEO – Tokio Millennium Re

Brian Young
CEO – OdysseyRe


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Reactions
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Cross section of a pine trunk – just as trees grow stronger and more durable as they add annual rings, our experience and reliability grows stronger and deeper year on year.
experience

The interview: Philippe Derieux, deputy CEO, Axa Global P&C

What's your methodology for buying reinsurance?

Our buying strategy has changed over time, given the Solvency II framework, which is necessary for the capital calculations and requirements. The pressure has increased on that, but it's not really that new.

But the principle of how we buy reinsurance hasn't changed over the last five years – our principles are to protect the balance sheet, avoid extreme risks, and comply with Solvency II and optimise the capital requirements.

We also want to mitigate the volatility around our profits each year, avoiding severe impacts so that we can provide stability for our shareholders.

The third point is to help the development of our local subsidiaries to use more reinsurance to protect them and help them to develop, both for emerging territories and for emerging risks. This is so that when we start a new venture, we know we can go into it with a reasonable level of risk.

Is there a difference between insurers that buy their reinsurance line by line, and those that purchase using a cross-line approach?

I'd describe it as a two-step process: first we check each line by line for its own merit, as it's important to check the profitability and the balance of each kind of business, and then we look at how we can find the appropriate reinsurance programmes, given the balance in the portfolios.

I think that the large global insurers are all doing the same sort of things. There'll be some differences of course, but we're pretty well aligned in that sense with others in the market.

Do you include ILS funds in your strategy?

Yes of course, providing it's a good alternative to the traditional reinsurance market. If we look specifically at cat bonds, we're keen to maintain our cat bond usage, providing it makes sense in terms of price and so on.

However, at this stage the cat bond market isn't very competitive compared with the traditional reinsurance market, so we do not intend to renew or issue new cat bonds in these market conditions.

The fixed costs are awfully high today – it's something that needs to be improved to make the market more attractive.

A good mix between cat bonds and traditional reinsurance is the best course of action, but it very much depends on the type of programme and the layers you are targeting. I don't think that cat bonds can ever replace traditional reinsurance.

> "We need a secure reinsurer with a good, solid balance sheet, and that means they cannot under-price their risk forever"

There has been talk of the reinsurance market being tiered – do you see it as a two-tiered or three-tiered market?

The market has indeed become somewhat tiered. But as far as we're concerned, it's not really a question of tiering, it's a question of relationships and the capacity to provide certain services.

We consider the reinsurers who are real partners for us, those who have aligned interests with us, which means they may be much smaller reinsurers. They have to be close to our way of thinking in terms of risk assessment and so on.

And with our emerging country markets, we need partners which can be with us for the medium- to long-term, so we can build the business together.

Where do you see reinsurance rates heading in the coming months?

We are expecting rates to continue to decline but not a lot, we are aware of the fact we are reaching the floor now. The decreases we'll see will likely be single-digit ones.

Each line, country and region will be decided on merit, so I don't expect to see uniform decreases across the board, but we're not expecting any increases. It's difficult to guess what will happen exactly, but in the absence of huge catastrophes and any other surprises, the market will remain soft.

How much further do you see the trend of global insurers cutting back on their reinsurance spend going?

Many insurers have retained more risk when compared with the 1990s. Having said that, if you look at the current climate evolution, the emergence of new risks such as cyber and the ramping up of regulations, my guess is that primary carriers will buy more reinsurance in future.

What are your biggest fears for the reinsurance market?

I don't really have any fears at the moment. But if pushed, my fear would be if the declining trend in pricing in reinsurance continues. What if we were to discover that there is in fact no floor and prices continue to fall, and fall again?

The impact of that on insurance would not be good. Even though we don't want to pay too high a price for our reinsurance, we need a secure reinsurer with a good, solid balance sheet, and that means they cannot under-price their risk forever.

What do you think about the shift which has seen some reinsurers move into direct markets?

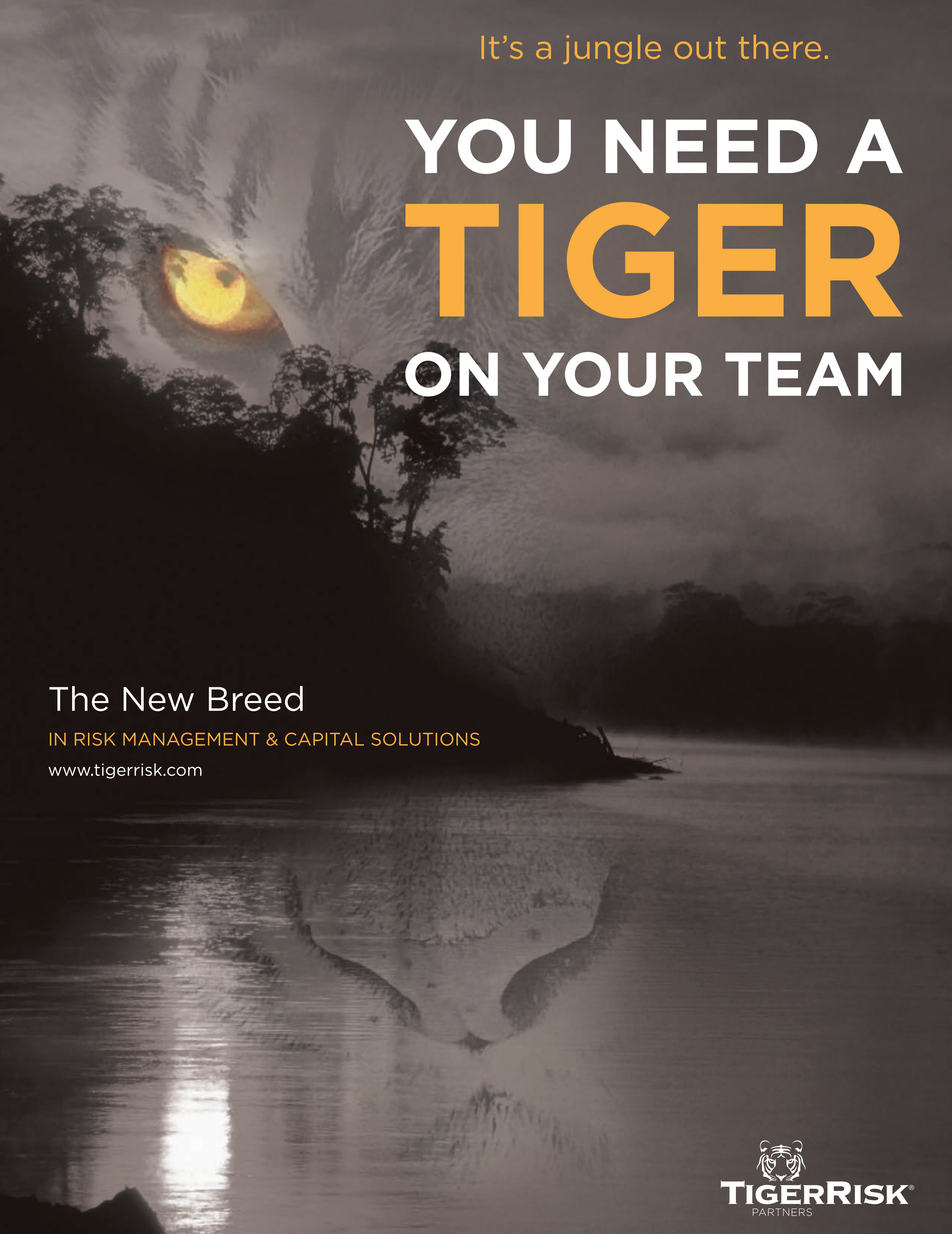
This has been a trend now for a couple of years, because insurers have reduced their reinsurance covers by retaining more risks.

Reinsurers have therefore tried to find a way to compensate, including going to the direct market.

I think there's a limit to that though as they don't have the structure and the networks to really compete in the direct markets.

Having said that, for our reinsurance purchase we do take into account this factor when allocating capacity to the reinsurers.

Philippe Derieux
Deputy CEO, Axa Global P&C



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The interview: Alice G Vaidyan

Can you describe the domestic Indian (re)insurance market? What skill gaps are there which require international players to come in and assist? And where can the domestic players add their experience?
The domestic Indian (re)insurance market is about $3.2bn and GIC Re has a 48 percent share of the market. Significant opportunities exist in property, agriculture, liability and cyber.

The entry of foreign reinsurers will benefit the Indian market in terms of capacity, newer products, price realignment and talent/skills infusion. We are talking about an industry that is expected to grow from $70bn in full-year 2015 to around $350bn-$400bn in 2020.

What is your take on the growth expectations of the Indian reinsurance market for the next two years?
The general insurance industry grew 13.8 percent in full-year 2015 and is expected to expand at an even greater pace this year. We are expecting a threefold jump in agriculture insurance premium to $2.2bn this year on the back of the newly introduced crop scheme Pradhan Mantri Fasal Bima Yojana.

With the economy accelerating over the next two to three years, the industry would benefit from both higher growth and an increased contribution from investment income. Low insurance penetration, rising middle class income and the vast protection gaps for life and property risks make the long-term picture compelling and explain the interest from all the top reinsurers.

How do you see the role of the (re)insurer growing to help address the gap between economic and insured losses?
A recent Swiss Re study put the global property protection gap at $221bn a year. Clearly this is a massive opportunity – this level of strain on public finances in the emerging world is unsustainable and must be pre-funded by the wider risk community.

As reinsurers, we should be at the front of such efforts and must use our balance sheet strength, technical ability and innovation to expand coverages and narrow the gap between economic and insured losses for catastrophe risks.

Putting capital to work quickly, incubating start-ups and underwriting innovation must figure prominently on reinsurers' agendas in order to become relevant in these markets. However, bridging this protection gap is not going to be easy and we must contend with issues like perception of risk, financial literacy, affordability, reliance on sovereign funding post-disaster and lack of trust in insurers.

What in particular is GIC Re doing to help disaster-proof India and other emerging markets?
Disaster risk reduction is a major challenge facing India today. Six of India's biggest cities figure in a list of the top 25 cities exposed to natural catastrophes, according to the Global Climate Change Vulnerability Index. With planned urban development not keeping pace with the rising demand, ad-hoc growth has resulted in people living in high-risk zones and increased the level of risks in the cities as a whole.

There is a cognisance of the fact that pre-event sovereign risk transfer is better than post-disaster financing among the political decision-makers, and we regularly engage the government of India on this issue. GIC Re has looked at catastrophe bonds for disaster financing and floated the idea of a basic cover for every citizen against natural catastrophes. We have the opportunity to build more disaster-resilient and inclusive societies and we must seize this or risk becoming irrelevant.

GIC Re has reported significant top-line growth for the past few quarters – culminating in 21 percent growth to $2.8bn in the 12 months to 31 March. Is this sort of growth sustainable?
It is true that we saw 21 percent growth last year but it is also true that our underwriting losses were down 15 percent and our combined ratio improved by 2 percentage points. This clearly is a reinsurer working in the right direction with a continued push towards growth – both top-line and bottom-line.

Given the dynamics of the domestic market, growth is not a concern for us, profitability is. Our entire focus is on four strategic priorities: achieving underwriting profitability through a greater technical thrust; diversification across product lines and geographies, with segments like agriculture, cyber, liability and life set to see a greater commitment; optimising and prioritising our client relationships and being seen as a market-friendly reinsurer; and a nimbler approach to capital and risk management.

The Insurance Regulatory and Development Authority of India (Irdai) has introduced a number of measures to improve the sustainability and credibility of the country's reinsurance market – are these helpful developments?
Irdai's role in finding the optimal point in what appears to be a very difficult trade-off – minimum rates on one side, maximum security on the other – and its management of competing demands has served the Indian insurance industry well.

Today, any regulatory framework has to be forward-looking and focused on anticipating future trends. As such, new regulations should incite the development of active risk management at the level of each insurance and reinsurance company. Regulation should be as close as possible to the business plan and risk profile of each company and try to assess if the capital management of each company is fully consistent with its business plan. The recent developments are a step in the right direction and should continue to evolve.

Irdai has also directed Indian carriers to reveal details of executive remuneration from next year. Is this forced transparency a welcome development?
Disclosure is a key concept in good corporate governance and executive remuneration disclosure is required in order to achieve accountability and openness.

However, in today's business environment, executive remuneration packages have become increasingly complicated, and accountability may correspondingly suffer.

Executives walk away with large rewards despite bad company performance, since many remuneration packages provide an insufficient connection between pay and performance. These are issues which I hope will be widely and better discussed following this directive.

Alice G Vaidyan
Chairman-cum-managing director, GIC Re

Dogged determination: (Re)insurers still standing ahead of *Rendez-Vous*

John Haley: Positive signs

Victoria Carter: Industry will adapt

Market conditions remain difficult, but there is still cause for optimism, delegates heard at *The Insurance Insider's* annual Pre-Monte Carlo Executive Briefing.

Speaking at the event on 7 September, Willis Towers Watson CEO John Haley insisted that the reinsurance industry was maintaining profitability in spite of ongoing soft market conditions.

Haley said he recognised the tough conditions buffeting reinsurers, but pointed to positive signs from Willis Re's reinsurance market report, released on the same day.

The report showed that underlying returns on equity fell by 0.4 percentage points to 4.5 percent, as an increase in natural catastrophes hit carriers' bottom lines.

Haley said: "No investor, I suspect, would describe that performance as enviable, but we can take heart in the fact that the reinsurance industry is still achieving a return, despite difficult market conditions and a rise in catastrophe losses."

The executive also remarked on the merger of Willis and Towers Watson, which completed earlier this year.

He said the deal had not been one of scale, but one of scope, which had helped facilitate a smooth transition to a joint company.

Goldman Sachs' head of insurance Emea Paul Miller also focused on the issue of M&A in the industry. He noted that while activity on the consolidation front had been muted so far this year, it reflected the sector's strong share price performance.

"The low-yield environment has made stocks with high dividend yields or high capital returns – such as this sector's insurance companies – highly investable, while the defensive and uncorrelated nature of the industry is also attractive to investors," he said.

"I'd also observe and say that compared to other sectors, this one is comprised of focused, high-performing companies with motivated and highly incentivised management teams," he added.

Miller went on to explain that M&A had been relatively depressed in 2016 following the flurry of deals the previous year as a result of management concerns about how achievable synergies are. "Another significant challenge is that it's difficult to create the synergies to offset the premium paid," he said.

A further issue that may have put the brakes on M&A activity is the perceived integration challenge in what is "fundamentally a people business".

There is also an extent to which some smaller, successful companies have been backed by investors to maintain their independence and specialist status.

Nevertheless, Miller stressed the powerful logic for consolidation and scale, which went beyond just generating cost savings.

Looking ahead, the investment banker said that the future earnings capacity of businesses was unclear.

"Our belief is that consolidation will continue to make sense and be sought, but only when the valuations allow and management teams and boards are

Continued on page **28**

Continued from page **27**

comfortable about the future earnings capacity of targets and their ability to realise the benefits of scale once integrated," he said.

Meanwhile, vice chairman of Guy Carpenter's international operations Victoria Carter expressed confidence in the market's ability to adapt to wholesale change, as tectonic societal and economic shifts reshape the reinsurance industry.

Carter said the increasing movement of people towards urban centres, technological developments, a growing aging population and heightened global interconnectivity could galvanise as well as threaten (re)insurers.

The non-life market would reap the benefits of urban expansion, as populations become wealthier and require broader cover, in addition to the risk transfer opportunities presented by investment in infrastructure.

Instead of fearing change, insurers should embrace it, Carter added, to help make the disruptive factors a "safe reality".

The theme of embracing new opportunities was reiterated by Aon Benfield CEO Eric Andersen, who implored reinsurers to embrace risks that were not being served sufficiently.

He said that major industries such as pharmaceuticals, financial institutions and automotive had big issues that they were worried about, such as product liability, professional liability and product recall. However, these are risks that are not being covered.

"We're really not there, but we used to be there," he said.

"The reality is that those risks didn't go away, we just pushed them back to the customer," he continued, adding that they were finding ways to finance themselves, such as making use of captives.

Elsewhere, Axis Re CEO Jay Nichols said that collaborations and joint ventures provided a way for the insurance industry to strip back the costs in its distribution chain.

"We have a value chain issue," Nichols said. "We're pulling a lot of dollars out to transport risk to capital."

He pointed to the fact that transferring risk from insurance buyers via a lengthy chain of agents, insurers, reinsurance brokers, reinsurers and sidecar investors to the ultimate institutional investors strips on average $0.61 out of every dollar of premium.

In comparison, distribution costs in other commoditised industries might be less than 5 percent.

Nichols added that he believed the pressure to reduce costs would drive more use of joint ventures, rather than mergers and acquisitions.

"Joint ventures are much more efficient solutions for the industry," he said, pointing to TransRe's agreement to write business on behalf of Berkshire Hathaway subsidiary Gen Re as an example of the consolidation of products, rather than companies.

Change in the reinsurance industry would occur eventually, but vestiges of the industry would still remain, he added.

Eric Andersen: Embrace risks

Paul Miller: M&A will return

The ILS manager interview: LGT ILS Partners

Who are your investors and what is the motivation of your client base to allocate to insurance-linked securities (ILS)?
We manage the ILS allocation for institutional investors, mostly pension funds and, to a small degree, asset managers such as banks and family offices.

Historically we have had a strong focus on Europe, but more recently we have expanded our client base to North America with a bespoke US offering, as well as Asia – both in Japan and Australia.

In the current market environment, pension funds allocate a smaller, strategic percentage of their asset base to ILS to benefit from the uncorrelated returns. But if the opportunity arises in the aftermath of a severe event, investors are expected to lift their allocation to meet the increased demand from buyers.

How reliable is ILS money – what will happen if there is a major event, the financial market sees an upswing or if interest rates increase?
Institutional clients are professional investors and the draw-down risk of insurance-linked investments – the potential loss as a result of a catastrophe event – is well understood by them.

A pension fund typically allocates between 2 percent and 4 percent of total assets to ILS, so even a very severe event resulting in a drawdown of 30 percent of this allocation would only have a minor effect on the total asset base of such investors.

Furthermore, investors fully understand that significant events also present opportunities. As such, many investors are prepared to increase their allocation to meet the increased demand from buyers.

As for the scenario whereby investors lose interest in ILS and move to other asset classes, we believe it is unlikely this would be prompted by a loss event. It may instead be a healthy signal to the reinsurance market – if rates are too low to generate a sensible risk-adjusted return, it could be helpful for the market to reduce overall capacity, so again, we do not see any form of threat from such a scenario.

After all, what this means is that the "wall" between reinsurance and financial markets has been torn down and capital is moving much more freely between the different markets.

If reinsurance markets require more capital, such capital will be made available instantly – always depending on rates, of course.

You are competing against traditional reinsurers – why should a primary carrier purchase cat capacity from an ILS manager?
We provide fully collateralised protection against extreme catastrophe events. As such, we only compete against reinsurers for the business lines where the reinsurance concept of a "promise to pay" is not efficient and where counterparty credit risk becomes a significant business risk for the capacity buyer.

> "We expect that the cat bond market will remain stable, but unless there is some severe event activity, we do not expect significant growth in the near future"

Under revised solvency capital requirements, a capital charge is added for credit risk. Collateralised cover simply provides the most efficient hedge to primary insurers against extreme events, as such protection comes without counterparty credit risk. Hence, the question ought to be why a primary carrier should purchase cat capacity from a reinsurance provider?

How do you think the new Solvency II requirements will affect the market?
The new solvency capital requirements are finally taking counterparty credit risk properly into account. Traditional cover results in credit risk, whereas fully collateralised protection releases more solvency capital and is hence more efficient, particularly for extreme catastrophe events.

As a result, we are seeing increased interest for such collateralised capacity, especially from European carriers. Over time, we are expecting a shift from traditional capacity towards ILS markets.

What are the reasons for the current slow growth of the cat bond market, and what is your forecast for its future development?
The collateralisation of the cover, the liquidity and the pricing transparency of cat bonds are attractive. But the structuring fees and the much slower time to market are clearly negative elements around cat bond transactions.

Collateralised reinsurance offers the same benefits as cat bonds – i.e. full collateralisation – but is otherwise transacted like traditional reinsurance.

Whilst on this basis, collateralised reinsurance looks very attractive in the current rate environment, certainly from an issuer's point of view, the pricing of cat bonds is arguably even more attractive, making a clear case for these instruments, and considering the returns from other asset classes, the appetite for liquid ILS exposure will likely persist (or grow) for some time.

And what keeps you awake at night?
We believe that we are well set up when it comes to extreme loss events – we focus on our exposure accumulation and constantly inform clients about the draw-down expected from a major event such as a severe hurricane or earthquake.

Yet, whilst we typically only cover natural perils, one of our concerns is the "unexpected" losses, i.e. the surprise event where the market has limited loss experience.

In the end, I suppose we share the same concerns as our peers from the traditional reinsurance market.

Pascal Koller
Partner at LGT ILS Partners

The Insurance Insider's 2015 P&C executive pay league

Collective remuneration for the 30 highest-paid executives in the P&C (re)insurance industry dropped 10.4 percent year-on-year to $339mn in 2015, *The Insurance Insider*'s executive pay league has shown.

Our annual survey includes more than 200 named executives across 37 publicly listed P&C (re)insurers and ranks them in order of total compensation for the year, which encompasses base salary, cash bonuses, stock and option awards and other benefits such as pensions.

The decreasing trend appeared in wider markets as well as in the (re)insurance industry.

By way of comparison, CEOs of S&P 500 companies received average annual income of $12.4mn in 2015, down 8.1 percent from the prior-year's figure of $13.5mn, according to data compiled by the American Federation of Labour and Congress of Industrial Organizations.

The top 10

The drop in average total earnings was also noticeable in the top 10 earners, as 2015's elite group reported remuneration packages ranging from $12.5mn to $29.7mn, compared to a range of $14.0mn to $33.5mn for the 10 highest earners in 2014.

Greg Case, Aon's president and CEO, topped our executive pay league for 2015, rising from 10th place the previous year.

The executive received total remuneration of $29.7mn in 2015, more than double the 2014 figure of $13.9mn.

The sharp increase was predominantly driven by a boost in stock awards, which jumped from $9.9mn to $25.6mn.

Second place was taken by Chubb's Evan Greenberg, who rose by two positions from the year before with remuneration of $20.4mn in 2015.

Despite being the second highest earner in the P&C (re)insurance industry, Greenberg's compensation grew by just 3.6 percent year-on-year, compared to a 10.6 percent rise the year before.

Jay Fishman, the late chief executive of US peer Travelers, received the third highest remuneration of the group at $20.0mn.

However, his total pay in 2015 was lower than in the year before, shrinking by 2.1 percent, compared to double-digit earnings increases in 2014 and 2013.

Another executive whose remuneration declined was William Berkley, chairman and CEO of WR Berkley. Berkley was paid $16.1mn in 2015, 8.7 percent less than in the previous year, due to the executive's non-equity incentive plan compensation shrinking by 13.8 percent to $9.3mn.

Nevertheless, Berkley rose by one position in the rankings in receiving the group's fourth highest pay package.

The second broker to make an appearance in the top 10 was Marsh & McLennan Companies, through its CEO Dan Glaser.

With $15.6mn of total earnings, ranking him in fifth place overall, Glaser was also the fifth and final executive to earn more than $15mn in 2015.

Drops in rankings

Meanwhile, the only US specialty (re)insurer to hold a position in the elite club of top earners was AmTrust.

The carrier's president and CEO Barry Zyskind dropped five positions from being the second highest earner in 2014 to take seventh place in 2015 with compensation of $13.9mn, down 37 percent from the year before.

Allstate president, chairman and CEO Thomas Wilson also had a lower ranking than in 2014, taking eighth position with $13.9mn in earnings.

The only Bermudian representative in the top 10 was XL Group, whose CEO Mike McGavick earned $12.7mn in 2015, securing ninth place in the list.

P&C (re)insurance giant AIG rounded off the top 10, with the company's CEO Peter Hancock climbing 11 places in the rankings after receiving compensation of $12.5mn in 2015. The carrier also had two executives among the top five biggest fallers, as executive vice presidents David Herzog and William Dooley each slipped by six places.

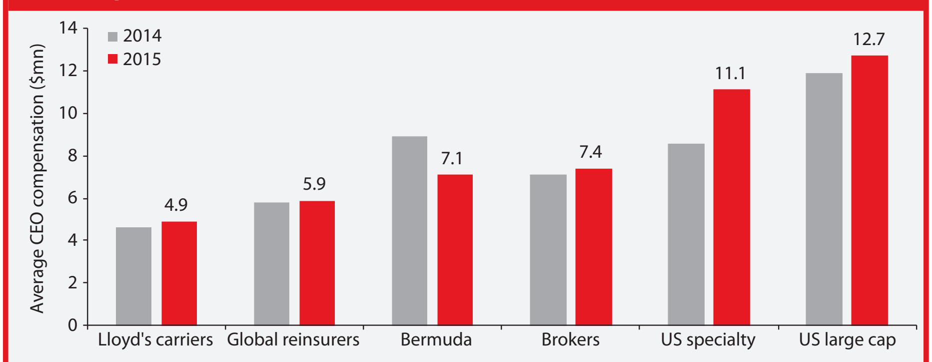
The largest drop, however, was suffered by Aspen CEO Chris O'Kane, who fell 11 positions to 42nd place in 2015.

Turning to the biggest risers, Everest Re CEO Dom Addesso made the second largest jump behind Aon's Christa Davies, climbing 26 positions to rank 20th in 2015, as his total annual remuneration expanded by 25.7 percent year-on-year to $8.2mn.

John Keogh, vice chairman and COO of Chubb, was among the top five climbers after moving up 12 places to rank as the 28th highest earner in 2015, with $7.5mn in total remuneration for the year.

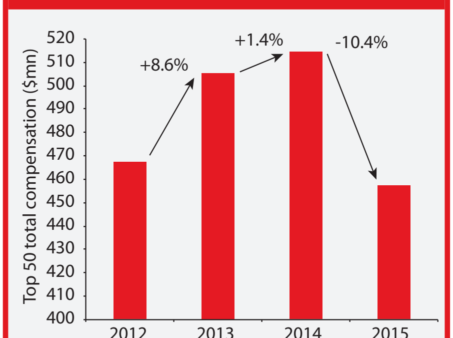
Meanwhile, fellow US carrier Travelers saw its vice chairman (now CEO) Alan Schnitzer climb 11 positions to 33rd place, earning a total of $6.9mn in the year.

Average CEO compensation



Source: *The Insurance Insider*, company reports

Top 50 pay plummets…



Source: *The Insurance Insider*, company reports

Top 30 highest paid P&C (re)insurance executives in 2015

Rank	Name	Company	Position	Total ($)	Ranking change	Last year's ranking
1	Gregory Case	Aon	President and CEO	29,735,220	9	10
2	Evan Greenberg	Chubb	Chairman, president and CEO	20,381,147	2	4
3	Jay Fishman	Travelers	Chairman and CEO	20,013,433	0	3
4	William Berkley	WR Berkley	Chairman and CEO	16,139,411	1	5
5	Daniel Glaser	MMC	President and CEO, MMC	15,596,717	4	9
6	Christa Davies	Aon	EVP and CFO	14,712,974	42	48
7	Barry Zyskind	AmTrust	President and CEO	13,942,205	-5	2
8	Thomas Wilson	Allstate	Chairman, president and CEO	13,873,693	-1	7
9	Michael McGavick	XL Group	CEO	12,712,353	3	12
10	Peter Hancock	AIG	CEO	12,497,975	1	11
11	Thomas Motamed	CNA	CEO	11,686,132	2	13
12	Dinos Iordanou	Arch	Chairman and CEO	10,614,241	3	15
13	Christopher Swift	The Hartford	Chairman and CEO	10,022,419	New entry	
14	Stephen McGill	Aon	Group president Aon Plc, chairman and CEO – Risk Solutions	9,275,750	18	32
15	Dominic Casserley	Willis Towers Watson	Legacy Willis Group CEO	9,013,163	3	18
16	Albert Benchimol	Axis	CEO, president and director	8,899,897	New entry	
17	Brian MacLean	Travelers	President and COO	8,672,673	5	24
18	Philip Fasano	AIG	EVP and CIO	8,397,689	New entry	
19	Robert Berkley, Jr	WR Berkley	President and COO	8,260,166	3	22
20	Dom Adesso	Everest Re	President and CEO	8,161,716	26	46
21	Kevin Hogan	AIG	EVP – Consumer	7,918,157	-2	19
22	Kevin O'Donnell	RenaissanceRe	President and CEO	7,853,835	11	33
23	Peter Zaffino	MMC	President and CEO, Marsh	7,796,754	4	27
24	Stephen Catlin	XL Group	Executive Deputy Chairman	7,765,883	2	26
25	S Craig Lindner	American Financial Group	Co-CEO and co-president	7,695,853	4	29
26	Carl Lindner III	American Financial Group	Co-CEO and co-president	7,642,021	2	28
27	Scott Carmilani	Allied World	President, CEO and chairman	7,622,454	-4	23
28	William Dooley	AIG	EVP, investments	7,591,563	-7	21
29	John Keogh	Chubb	Vice chairman and COO; chairman, Ace Overseas General	7,518,919	11	40
30	Douglas Elliot	The Hartford	President	7,431,487	New entry	
	Total pay			**339,445,900**	**-10.4%**	

Source: *The Insurance Insider*, company reports

US large-cap CEOs still the highest paid

US large-cap CEOs saw their average remuneration grow 6.7 percent year-on-year to $12.7mn in 2015, as the segment once again led the (re)insurance industry in terms of executive compensation.

These firms paid the lowest amount as a proportion of net income, at 0.6 percent on average, but this is primarily due to their large size.

Christopher Swift, chairman and CEO of The Hartford, received the largest pay boost, as his remuneration increased by 85.8 percent to $10mn.

However, Chubb chairman, president and CEO Evan Greenberg remains the most richly rewarded executive of the large-cap group, with pay equivalent to 0.7 percent of his firm's earnings.

The former Ace chairman and CEO took over the helm at Chubb following its $28.3bn acquisition by Ace.

The deal, which completed in January, created the world's largest publicly traded P&C insurer.

Greenberg was the second best paid CEO in the sector overall in 2015 with total compensation of $20.4mn, up 3.6 percent from the year before.

AIG CEO Peter Hancock also received a 3.6 percent pay increase in 2015 to $12.5mn, despite investors voicing discontent with the company's performance and growing pressure on management to break up the firm.

As part of a wider streamlining strategy, Hancock revealed cost-cutting measures that will cull 23 percent of its top 1,400 senior management personnel.

Hancock's compensation was the lowest of the US large caps as a proportion of net income, at 0.56 percent.

THE INSURANCE Insider

2016 EVENTS

LMCC Breakfast Briefing

28 September 2016 (08:00 – 10:00)
The City of London Club, Old Broad Street, London, EC2N 1DS

Guest speaker:
Paul Jardine, Executive Vice President & Chief Experience Officer, XL Catlin
LMCC members only

L100 Breakfast Briefing

29 September 2016 (08:00 – 10:00)
The City of London Club, Old Broad Street, London, EC2N 1DS

Guest Speaker:
Chris Moulder, Director of General Insurance, Prudential Regulation Authority
L100 members only

Trading Risk New York *Rendez-Vous*

4 October 2016
New York Athletic Club, New York, NY 10019
www.trading-riskrendezvous.com

Speakers include:
Scott Belden, Senior Vice President, Reinsurance, Travelers
John Forney, CFA, President & Chief Executive Officer, UPC Insurance
Dirk Lohmann, CEO & Managing Partner, Secquaero Advisors
Michael Millette, Managing Partner at Hudson Structured Capital Management
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The Xchanging London Market Conference

10 November 2016
Etc venues, 155 Bishopsgate, London, EC2M 3YD
www.xchanginglondonmarket conference.com/

Speakers include:
Andrew Horton, CEO, Beazley plc
Julian James, President, Allied World Europe
Shirine Khoury-Haq, Director, Operations, Lloyd's
Sean McGovern, Chief Compliance Officer, Head of Regulatory & Government Affairs, XL Catlin
Kurt Karl, Chief Economist, Swiss Re
Malcolm Newman, CEO, Paris-London Hub, SCOR
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Solvency II: greater risk-driven management

On 1 January 2016 the Solvency II regulatory regime took effect. Some celebrated; others were weary from the months and years of preparation.

But, to borrow a turn of phrase from Winston Churchill, this is not the end of Solvency II, it is not even the beginning of the end, but it is the end of the beginning.

The impact of Solvency II goes well beyond its strict regulatory assessment. Solvency II creates an environment for greater risk-driven management of the (re)insurance companies doing business in and with Europe.

While the solvency capital requirement (SCR) and minimum capital requirement are the thresholds used by regulators to trigger action on specific entities, the solvency ratio (own funds over SCR) is fast becoming an important metric for comparing companies.

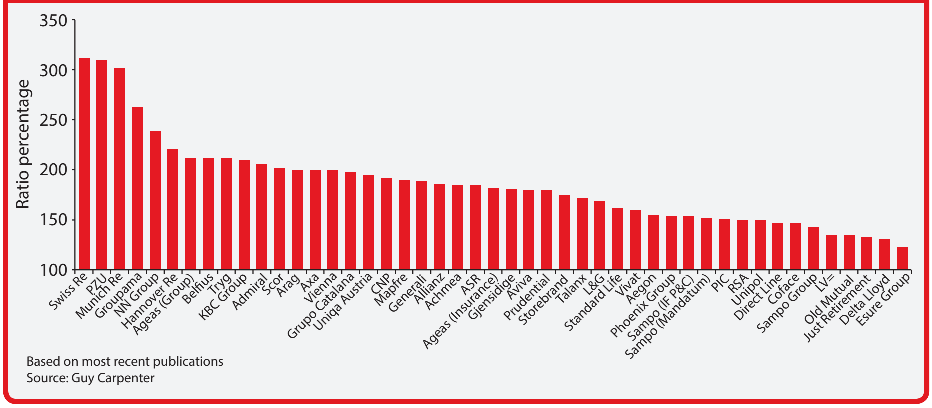
Today, many companies publish their solvency ratios without being required to do so, and some others actually specify target solvency ratio ranges as part of their risk appetite and financial targets.

Solvency ratios are another metric for investors to use when assessing the relative financial strength of companies – and (re)insurance buyers can do the same when assessing counterparty risk.

Some larger quoted companies use the capital regime to strengthen their self-regulation. By setting target ranges and minimum levels well above 100 percent, these companies create their own parameters for self-intervention in instances when they will buy back shares or simply cut the dividend. We have seen examples of companies recapitalising after their SCR moved below a minimum range, illustrating the focus investors may start to have on this metric.

However, the effectiveness of a single ratio as the basis of comparisons should not be overstated. For example, how comparable is a standard formula-based ratio to one calculated on an internal model?

Solvency II ratios at end-Q1 2016



Based on most recent publications
Source: Guy Carpenter

What about different use of transitional arrangements, or matching adjustments? As Solvency II is still being introduced at different rates, various stakeholders have to pay attention to individual company standards for reporting solvency ratios.

Volatility

Another shortcoming of a single ratio is that it provides no insight into the resilience of an entity's capital position. This became relevant when market volatility spiked in the first quarter of 2016 and companies disclosed how much their Solvency II ratios fell in the period.

This environment produced varying outcomes in the first half of 2016, with an additional sharp increase in volatility caused by catastrophe losses. Timely and accurate reporting of this volatility has increasingly become a management responsibility.

Today, reinsurance as an alternative form of capital is more at the centre of risk management. Insurers have increased efforts to understand and quantify all material risks and are using reinsurance not only as a tool to manage capital and their SCR ratio, but also to manage earnings volatility as reflected in their risk appetite statements and risk tolerance levels.

Risk management and risk profile

With the transition from Solvency I to Solvency II, insurers have to contend with a more complex and comprehensive risk management framework than just premiums and reserves. This new framework encompasses the full range of risks exposing a (re)insurance portfolio, including an examination of existing risk mitigation frameworks.

Insurers are more heavily focused on reviewing their diversified risk profile with more active risk and portfolio management, with each portfolio segment examined on its own merit.

The stronger focus on risk management is pushing (re)insurers to review the varying contributions to capital needs and earnings. For those companies that have decided to develop an internal model, the alignment with all requirements can be challenging. There is a need to provide a clear view of the risk for a range of risk classes not just limited to the most obvious.

Solvency II is not limited to the calculation of the required capital. It creates an environment for a more global and robust approach to risk, from risk selection and pricing to capital needs and allocation.

Andrew Cox
Managing Director, Guy Carpenter

Matthew Eagle
Head of GC Analytics – International

Eddy Vanbeneden
Managing Director, Guy Carpenter

Capitalize on Complexity

Insurers are challenged by regulatory and rating agency changes that significantly alter capital requirements. Many of these developments go beyond regulation, necessitating greater risk-informed management for businesses. Our strategic advisory teams help clients manage these demands and grow their business, profitably.

Strategic Advisory

Rating Agency Advisory | Regulatory Advisory | Enterprise Risk Management

GUY CARPENTER

Leading the Way Forward