Insight and Intelligence on the International (Re)insurance Markets

29 October – 1 November 2019

THE INSURANCE Insider

SIRC 2019

Stable 1.1 beckons in Asia with Hagibis contagion likely limited

Reinsurance pricing is likely to be broadly stable in the Asian markets at 1 January, with the rate-boosting impact of Typhoon Hagibis likely to be largely confined to Japan.

Rates have been soft when adjusted for exposure growth in most Asian markets for many years, despite some optimism running into the last renewal season, and it is hard to see a sharp correction in pricing in 2020.

Although there have been upward corrections in recent months for specific regions, perils and clients, the reinsurance market has shown an increasing degree of differentiation with no tendency for "a rising tide to lift all boats".

Concerns remain about the technical rate adequacy of much Asian reinsurance business, but the loss environment outside of Japan has been benign in 2019, and reinsurers that do not run their Japanese accounts through their Singapore and Hong Kong arms expect to deliver underwriting profits in 2019.

In addition, the twin factors that have long been negative drivers for Asian pricing remain in place. Firstly, reinsurers have traditionally taken a differentiated review of their return hurdles for Asian business, owing to their willingness to take a strategic bet on growth in the region.

Secondly, Asia has a better developed regional reinsurance market, with Asia-focused capacity that tends to undermine pricing.

Key points

- Scale of Hagibis will be key talking point, but contagion to non-Japanese markets likely limited
- Stable pricing expected at 1.1
- Concerns about technical rate adequacy remain, but 2019 ex-Japan has been benign
- The growth mindset of global players and regional capacity remain dampeners of pricing

Hagibis uncertainty

Typhoon Hagibis struck Japan on 12 October, and work to understand the loss is still in its early stages. The loss is heavily skewed towards flood over wind damage, and that has created a high degree of uncertainty.

This has been exacerbated by the damage to structures caused by September's Typhoon Faxai, model scepticism after runaway Jebi creep and opacity around the degree of flood penetration.

Rough estimates from underwriting and broking sources put losses from the storm at $5bn-$10bn, with a bias towards the top end of that range.

This would make Hagibis the second biggest Japanese wind loss in the history of the market, and a heavily reinsured loss given that the occurrence covers of the Japanese big three attach at an industry loss of $3bn-$4bn, with aggregates set to come in lower after earlier losses. Sources expect the mutuals, including Zenkyoren, to take the loss net.

Hagibis will be a major talking point at the Singapore International Reinsurance Conference, but a range of sources said the Japanese market is heavily siloed from other Asian markets, with markets like South Korea and China unlikely to feel the impact of the typhoon and $5bn+ Faxai.

Most reinsurers write the programmes of the Japanese big three on either European or Bermudian platforms, bypassing Singapore and Hong Kong.

Sources said that given the scale of the buyers involved, and the size of the Japanese premium pot, there was an expectation that payback would be confined to Japan.

For Hagibis to become a breakout loss that is felt meaningfully in the broader Asian markets, sources suggested it would have to breach the $15bn mark.

Elsewhere, sources said the year has been highly benign to date, with some forecasting combined ratios in the 80-90 percent range for Singapore reinsurance arms.

Technically weak

However, sources stressed long-term concerns about technical rate adequacy within Asian markets despite the forgiving loss environment this year.

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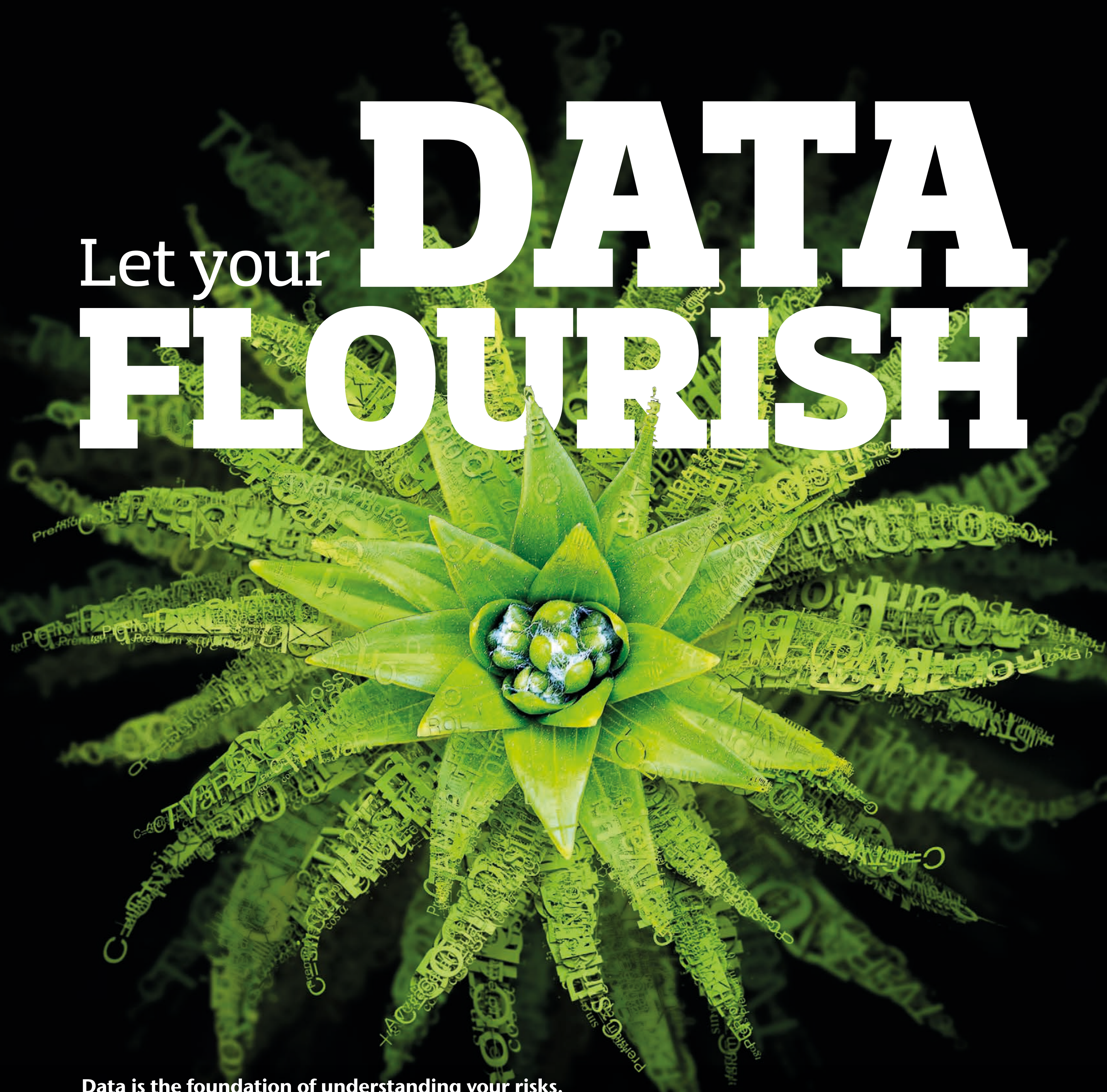

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The Future at Lloyd's (Asia)

The Lloyd's blueprint presents a picture of a market transformed.

It sketches a future for Lloyd's in which the value proposition for all stakeholders is enhanced, with more efficient distribution, lower operating costs for underwriting entities, greater ease of access for capital providers and an improved culture for staff.

The highly impressive document runs for 146 pages, with chapters on everything from risk syndication and data to the role of the Corporation and the eccentrically named syndicate in a box.

But there is no mention whatsoever of Lloyd's Asia.

The drive towards building out an international footprint that characterised Lord Levene's period as Lloyd's chairman and the push to embrace the emerging markets associated with successor John Nelson are conspicuous by their absence.

Instead, the emphasis is on improved market access for brokers via two technology platforms, with the centre of gravity very firmly in London.

And although the messaging is not present in the document itself, it has been clear from CEO John Neal's statements that increasing Lloyd's market share in its US heartland is more pressing than driving Asian volumes.

In preparation for the work to transform the market, Neal and performance management director Jon Hancock have overseen an underwriting remediation process at Lloyd's that has also taken its toll on the market's Singapore platform – which already represented less than 2 percent of total volumes written by the market.

A succession of managing agents have ended their participation on the platform, and at least some seem to have done so as a by-product of withdrawals from whole classes of business, which may have had more to do with the performance of the London portfolio than the one in Singapore.

The list of syndicates to drop from the platform over the past two years has grown. Most recently, Argo shuttered its Lloyd's Asia arm in September, but it followed a succession of other names including CV Starr and CNA Hardy. The Standard Club also went after its syndicate was closed.

In this environment, questions are being asked about the long-term role of Lloyd's Asia. With collective premiums of only $650mn, a number of syndicates operating on the platform have cost issues, and there is a challenge for them to achieve the scale and diversification required to operate in a region where margins are thinner than in Anglo-Saxon markets.

Other managing agents look likely to call time on their involvement over the next 12-18 months, and look to migrate their books back to London.

But there is clearly a future for the platform, it will just have to retool itself like the rest of the market in line with the principles of the blueprint, and find ways to exploit the opportunities created.

Reduced cost from the use of the two new placement platforms will help it to address its cost issue, and the flight of syndicates could be reversed somewhat by two syndicate in a box start-ups understood to be in train.

And then there is a definite capital opportunity under the new regime, which could be considerable given the size of the Asian capital markets.

But what is clear is that Lloyd's Asia will need to adapt to become fit for purpose in the post-Blueprint One world.

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And they stressed broader trends within the reinsurance market that have seen reinsurers become more thoughtful about their risk appetite following $225bn of cat losses in 2017 and 2018.

PartnerRe's CEO of P&C for Asia Pacific James Beedle told this publication: "My expectation is that there will be no appetite from reinsurers for business that shows rate reductions."

He also stressed that the buying stratagem of holding rates on line steady while exposures grew meaningfully would not be accepted by reinsurers this year.

"I don't think the same dollars for 10 percent exposure growth will work this year – it has to be risk-adjusted flat at worst."

Other underwriting sources speaking off the record were somewhat more bearish, but a number said they expected to see more dollars of premium on excess-of-loss deals this year – with the question being whether or not this kept pace with exposure growth.

China in particular remains a concern, with a tendency for the country to come in as the softest market, with reinsurers accepting thin to almost non-existent margins to secure volumes in the fast-growing market.

The 1 January renewals focus on the major motor quota shares – which are dominated by China Re, Munich Re and Swiss Re – and which run at virtually break-even rates, although property quota shares and surplus treaties which are more broadly marketed will also be in play. Cat treaties renew throughout the spring through to 1 July, and were still soft at the 2019 mid-year renewals.

South Korea is another area of concern for reinsurers, with big buyers like Samsung and Hyundai notoriously tough negotiators. Particularly given the low level of cat loss activity in the country, reinsurers are concerned that if they push for rate rises, these buyers will retain more or shake up their panels.

Asian exceptionalism

Scope for rate rises continues to be capped by the distinctive features of the Asian market. Reinsurers have for years seen the region as a long-term bet, with a willingness to sacrifice margin in exchange for market share that will drive growth as insurance penetration rises.

There have been question marks about the extent to which this strategy is sustainable, but apart from Swiss Re's brief drawback from China, a really meaningful withdrawal of capacity has not been seen.

And even if the global reinsurers do maintain discipline, regional reinsurance capacity is a meaningful offset within Asia.

Korean Re, GIC Re and China Re all play crucial roles in determining pricing in their home markets, and are also keen to secure growth in other countries, with other regional players like Peak Re and Asia Capital Re also committed to supporting Asian clients.

"There is an important dynamic in Asia where national reinsurers have a significant impact on home markets, and also want to build third-party accounts outside their home territory," Beedle said.

"That can create a supply-demand issue that can truncate upward rate movements."

Jebi creep no surprise: Peak Re's Hahn

The level of loss creep on Typhoon Jebi should not have come as a surprise to reinsurers, according to Peak Re CEO Franz Josef Hahn.

In an interview with *The Insurance Insider*, Hahn said reinsurers should be prepared for wind storms on Jebi's scale and for loss figures to develop quite slowly in Japan.

"The loss creep in cat losses is nothing to be surprised about in Japan. It should be included in the pricing and in the calculations that losses can develop a little bit slower than in other markets," said Hahn.

"It did not come as a surprise to us. In addition, you need to keep in mind that Faxai, Hagibis and last year's Jebi affected households, which take a little bit longer to collect. But this is something that reinsurers should be prepared for, because ultimately we regard it as a natural loss development."

Hahn's comments come after reinsurers raised questions about the wide difference between initial loss estimates of around $5bn and the final picture, which looks to be around $15bn.

It is understood that Japanese cedants and modelling firms have come under pressure to explain the level of disparity and the time taken to report accurate loss figures.

Hahn, however, said the year between the storm and final loss estimates was not an unreasonable length of time.

"I don't think that it took too long to collect the losses of Jebi, which was a major natural catastrophe that went over the entire country – cities and countryside," he said.

Hahn added that Jebi was "something like a 1-in-20 or 1-in-25-year event" and that reinsurers should therefore be ready to account for it.

"There have been price adjustments in 2019 already because of Jebi and Trami. The Japanese market has always been known as a market that gives you the chance to earn back. This works very well in Japan."

More generally, Hahn said the greatest opportunities for reinsurers in Asia Pacific lay in emerging Asian countries, a category that takes in China, India, Indonesia, Malaysia, the Philippines, Thailand and Vietnam, according to the International Monetary Fund.

While China and India led economic growth, they were followed by the next-most populous countries: Indonesia, the Philippines and Thailand.

"They are all growing at 6 percent or above," said Hahn.

"That's an economic opportunity. If we want to maintain our market share, we will be growing automatically year by year."

"Societal opportunities lie in the area of demographics," Hahn continued.

"Emerging Asian countries are young. There is a huge part of society growing into the middle class space and they all need protection; adequately tailored products that are different to those that we bought in the 1970s in Europe."

In more mature economies, however, there were still opportunities, Hahn said.

"In Japan, Australia, Hong Kong, Singapore and, in 20 years' time, also China, the opportunity is with the ageing population, and again completely different products are needed. They need new insurance and hence reinsurance products in all areas – casualty, accident and health, life."

ACR sees fast-track syndicates easing 'prohibitive' Lloyd's costs

Asia Capital Re (ACR) CEO Bobby Heerasing is eyeing the impact of the Lloyd's revamp on the cost of doing business in the market as his company looks to increase the proportion of premiums derived from outside Asia Pacific and the Middle East.

Heerasing contributed to the consultation leading up to the release of Lloyd's Blueprint One in September.

Cornerstones of the plan include a syndicate in a box proposal to expedite new entrants to the market as well as platforms for complex and more commoditised risk.

Heerasing said: "The syndicate in a box is an initiative that is positive. It is well thought out, it is meant to encourage people like us especially and gives potentially some benefits from a cost perspective and an ability to dip a toe in the water. It makes it slightly easier to do that.

"We have been evaluating and discussing this and are not likely to take it up in the short term, but I can understand why it would be attractive to other participants."

He added: "The fact they have been able to have a framework established relatively quickly I think is great. I can see it making sense for lots of people – we are a keen watcher of the Lloyd's syndicate in a box principle."

Heerasing's firm is looking to expand the proportion of premiums derived from outside Asia Pacific and the Middle East, and hopes to have increased this to about a third of the total in three to five years, from an expected 15 percent in 2019, when total gross written premiums look set to comfortably exceed $600mn.

At the end of last year Heerasing hired Nick Macfarlane from MS Amlin as head of treaty, international, as part of this push.

But Heerasing said that participation in the Lloyd's market is currently too costly.

"The attraction for partnering up and being part of the Lloyd's set-up is clear – we've also been very clear that we view the cost of operating under a Lloyd's framework to be prohibitive right now.

"The degree of oversight and duplication of oversight [between Lloyd's and the Prudential Regulation Authority] is a bit cumbersome," he added.

"But absolutely, if Lloyd's becomes that nimble, agile entity that is something that informs part of our thinking as well."

Heerasing predicts that the specialty insurance market concentrated in the EC3 post code of the UK capital will survive Brexit.

In terms of potential European expansion for ACR, he said: "Brexit obviously has implications for access to business so we are thinking about where would be the best locations. We're always thinking two years ahead."

He added: "London will continue to be a significant wholesale market and have the ecosystem to support the (re)insurance industry irrespective of Brexit – I am convinced of that.

"Lloyd's will hopefully continue to be a strong marketplace with significant talent and innovation, which benefits the whole industry."

Learning the lessons of Jebi

When Typhoon Jebi struck Japan in September 2018, modellers and insurers initially believed the storm would generate insured losses in the low single-digit billions of dollars.

The industry, however, was in for an unpleasant surprise. A fortnight after Jebi made landfall, the modellers' top estimates sat between $4.5bn and $5.5bn, but within six weeks of the storm market sources were already voicing concerns about losses stretching to $7bn. By February, estimates had reached $10bn.

Just over a year on from the event, a general consensus has emerged around a final insured loss figure of between $15bn and $16bn. The extensive creep on the loss has led to questions about Japanese catastrophe models and cedants' ability to report on their losses in an accurate and timely fashion.

Impact on reinsurers

The tripling of the loss figure from initial estimates and the length of time between those initial forecasts and a full picture emerging has had a significant impact on reinsurers globally.

Carriers found themselves with loss deterioration from Jebi stretching not just into Q1 this year but also Q2.

Among the European carriers, Hannover Re revealed that it had booked additional first-half losses from Jebi of EUR106mn ($116.3mn) net, with losses beyond that reaching the lower layers of its retro cover.

Munich Re recorded additional expenditure of $87.6mn in Q2 from the storm, while Swiss Re said it booked a "significant amount" of late Jebi claims in H1.

Scor revealed that as a result of deterioration from both Jebi and Trami it had increased its average annual expected loss on Japanese risks by around 3 percent.

In London, Hiscox was forced to strengthen reserves by $40mn in the first half after deterioration from Jebi and Michael, while Beazley said claims from Jebi and last year's Californian wildfires pushed its reinsurance segment to a first-half $11.3mn operating loss.

Sources told this publication at the Monte Carlo *Rendez-Vous* in September that Japanese cedants had faced tough conversations with their reinsurers about how such a large loss could have been underestimated early on.

Many reinsurers at the conference also sought reassurance that modelling agencies had updated their models to reflect the Jebi experience.

Learning from Jebi

The unexpected scale of the damage from Jebi has prompted both AIR Worldwide and RMS to analyse the storm and its impacts with a view to improving their models in future.

Cagdas Kafali, senior vice president of research and modelling at AIR, said that while it had initially predicted a loss of $2bn-$5bn, the company upped this to $15bn in November in its discussions with clients. In any case, there were a number of factors that contributed to the difficulty in accurately predicting Jebi damage, Kafali said.

The storm presented phenomena that were not common characteristics of typhoons, he said. These created stronger-than-expected winds, particularly in Osaka, which were not within AIR's model.

Osaka – the second most densely populated city in Japan – also presented a challenge to modellers, Kafali said, as it had not experienced a recent typhoon hit. Less data on which to base predictions was therefore available.

Kafali also cited disruption to the preparations for the 2020 summer Olympics in Tokyo creating demand surge as a factor that made predicting the insured loss difficult.

Hemant Nagpal, director of model product management at RMS, agreed Jebi had presented unique challenges and various factors prior to and after the storm had exacerbated the damage.

Nagpal said historic flooding in Japan prior to Jebi, as well as a 5.6-magnitude earthquake in Osaka in June, had made some locations more vulnerable to the impact of the storm.

"Nobody expected the claims to develop so much," Nagpal added.

He said Jebi had led to a high quantum of claims, with some still open now. The more complex claims often took longer to settle, storing up large loss disclosures for later in the process, Nagpal added.

Karen Clark & Co CEO Karen Clark, however, said existing models should have been able to predict Jebi's impact more accurately. Her firm only began modelling Japanese risk with the release of its typhoon reference model this year.

Clark said Jebi was not unique if compared with the impact historical storms would have had with modern exposures.

"Every storm is unique but the models should be able to handle that," she said.

That Jebi hit a city such as Osaka, and that it was widespread enough to create almost a million claims, should also have given an early indication of the scale of the insured damage, Clark added.

Clark dismissed preparations for the Olympics as a serious factor in pushing up Jebi losses, arguing that demand surge would "add 5 percent or 10 percent here or there" but could not multiply a loss figure by three.

Although many claims for Jebi reached insurers several months after the storm, Clark argued that models should capture the possibility for that, adding that insurers would be able to estimate how quickly claims would come in.

Both Nagpal and Kafali confirmed that the modellers were actively working with Japanese insureds to understand more about Jebi's losses with a view to improving their ability to model Japanese wind losses.

Loss development timeline

4 September 2018: Jebi makes landfall over Shikoku

10 September 2018: AIR estimates insured losses of between $2.3bn and $4.5bn

14 September 2018: RMS forecasts losses of between $3bn and $5.5bn

16 October 2018: Market sources estimate losses could reach $7bn

23 November 2018: General Insurance Association of Japan reports accepted claims amount at $5.2bn

16 January 2019: Willis Re estimates losses at $8.5bn

22 February 2019: Market sources predict losses to exceed $10bn

25 April 2019: Axis Capital increases insured loss estimate by 56.6 percent to $12bn-$13bn

28 May 2019: JMP Securities estimates losses would settle ultimately at $15bn-$16bn

Lumen Re

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Guidance through shifting sands

The CEO of Aon's Reinsurance Solutions business, Andy Marcell, explains how the broker is helping clients navigate the changing dynamics of the market

How is Aon's Reinsurance Solutions business positioning itself for continued growth?

We've been growing consistently for several years. Core to what we do is delivering value to our clients and making sure everything we do differentiates us from our competition.

When we look to 2020, we still believe there's a considerable amount of uninsured risk out there so our New Ventures Group, which focuses on areas including government de-risking and intellectual property coverage, is dedicated to generating new capacity and solutions to meet the needs of the risk world.

We've always been innovative as a firm and we will continue to push the New Ventures Group and how we integrate it with Reinsurance Solutions.

The core differentiator for our business remains its scale, its innovation and its commitment to data and analytics excellence as a way of providing value to clients.

For a broking house that doesn't have that quantity of scale and data, it's hard to deliver broad value other than on specific, individual transactions.

What do you make of the talk about reinsurers becoming increasingly tiered and the number of carriers on panels reducing?

I don't think there is a deliberate move to cut the number of reinsurers by clients. If you're a global insurer you have benchmarks in terms of the quality, rating and capital adequacy that qualifies a reinsurer to be an adequate counterparty. Beyond that, global companies are looking for relationships across the breadth of the reinsurance they purchase and they tend to favour companies that feature broadly across those programmes.

Naturally, the ability to offer broad geography and products tends towards the larger reinsurance companies. That's not to say that large companies don't have niche, specific reinsurance needs for certain lines, and they'll also go to companies they see as leaders in those segments.

Regional companies have a different view of their counterparties. They have solvency and capital requirements too, but they tend to utilise brokers to a greater extent to monitor those financial strength metrics. They often want to build longstanding relationships with their counterparties.

Other than providing insight and analytics, structure and advisory services, our job as a broker is wrapped around providing choice to our clients on the execution of any particular transaction.

> "To be relevant as a reinsurance broker you have to help your clients become more effective in executing their business plan"

What are the key talking points in the marketplace at the moment?

There are discussions around the original rate changes in the market and how long they will hold. Is the shift permanent and, if not, how long will it last? There are discussions around a tightening retro market and how that caused reinsurers to change their view of risk, the returns they were looking for and how it's now driving changes in behaviour. There are two other considerations there – one is revamped funds and the second is ILS capacity and how much will re-emerge in 2020. But the most common topic is the changes in original rates, it will certainly be on everyone's mind. There will also be talk about innovation and technology and its impact on the industry.

Is InsurTech an enabler or a disruptor?

Throughout my time in the industry there have been challenges to the traditional model – cat bonds or ILS, for example – and now people talk about auctions and blockchain.

Everyone has a view on technology. Global insurance companies have their own technology initiatives – they have large resources and a number of relationships with technology providers. Lots of those companies are also investors in technology companies.

Companies that don't have those resources can turn to their reinsurance brokers to help them analyse the plethora of providers out there and seek recommendations on which one might be best.

In this regard, we track all the InsurTechs we can and categorise them into distribution, risk selection and efficiency.

Regional companies look more to efficiency and distribution, and they also look for technology to help them select better risk. Global firms tend to follow all this themselves, and if it's an area that's truly innovative they will come and discuss it with us. In some cases we partner with them.

Pushing away from all the innovation would be the worst thing to do. We should embrace it and utilise the elements that are of value to our clients.

Can you tell me more about the client segmentation initiative?

To be relevant as a reinsurance broker you have to help your clients become more effective in executing their business plan.

The best way to do that is to identify a common set of issues around a common set of clients, and to improve the outcomes for those clients by generating a deeper understanding of their needs. That is not just around reinsurance transactions, but everything that impacts them.

For our regional clients, we're thinking about how can we help them solve problems in areas such as healthcare, asset management, pension advice and growth strategies. We have all those tools within the Aon family and our goal is to unite them in a single set of solutions. We call this Aon United. It's not a gimmick, it's real and we're working it hard. We're just doing more things in a better way for our clients.

Andy Marcell
CEO, Aon's Reinsurance Solutions business

Asian expectations

Asia Capital Re CEO Bobby Heerasing sees ample opportunity for profitable growth within the region and an increasing role for the reinsurer beyond

Asia Capital Re (ACR) looks set to achieve significant gross written premium (GWP) growth in 2019, as it recovers the catastrophe losses of 2018.

This year marked the start of a concerted attempt by the treaty-focused reinsurer to expand in fac and specialty and to diversify outside Asia Pacific and the Middle East. Expense management was also in focus, as AM Best recognised when it affirmed the carrier's A- financial strength rating in early September.

With about three months of the year left to go, ACR CEO Bobby Heerasing predicts GWP growth of as much as 20 percent in 2019. Last year the company wrote $547.5mn of premiums. However, Typhoon Jebi claims pushed it to a net combined ratio of 113.1 percent for 2018 and an overall loss of $18.3mn.

Heerasing notes: "We have a significant degree of momentum compared to where we were and are executing a plan for our shareholders that is starting to deliver.

"All the soft signals seem to be pointing in the right direction."

Typhoon Jebi

Although ACR was hit hard by Jebi, which accounted for the lion's share of its $97.1mn in catastrophe claims last year, Heerasing questions the simplistic narratives emerging around loss creep from the typhoon.

Ultimate industry-wide claims from the event look set to top $15bn, well above the $3bn-$5bn or so originally envisaged by modellers.

Poor data and laggard insurers have been frequently blamed for the increase. But Heerasing says: "We have to think of the magnitude and the scale of losses that Jebi caused. Some of our cedants were faced with having to deal with 150,000-plus claims and Jebi did hit some locations of high value, so the fac claims associated with that took time to adjust."

"The initial numbers generated from AIR and RMS set some expectation that proved to be inadequate – both have drawn lessons from those numbers," he adds.

Heerasing notes that the Japanese (re)insurance and broking community have, for over a decade, worked to improve data flow and the speed of claims adjusting, even though it could still be faster.

> "Quota share is a key part of how people manage capital and I don't see that changing, but as some of the larger cap insurers look ahead, there is a growing consciousness that excess of loss does provide good value and can enable them to build a programme that meets their needs"

Elsewhere in Asia Pacific, "micro" data on exposures remain deficient in many key markets, given the rapid growth in coastal populations and mass migration from rural communities to urban centres.

But Heerasing, the former Asia Pacific CUO at Catlin, also points out that even the rigorously modelled North American property catastrophe market is prone to loss creep.

"When we talk about North American hurricanes they're not exactly unexpected – yet most years we see between 20 percent and 30 percent creep based on initial numbers," he says.

"So loss creep is not unique to Asia.

"What we don't have, if we want to compare the situation with North American and European cities, is the same granular analysis to get to a very quick assessment of what a cat event in parts of the region would mean," he says.

While this year has so far been quieter, Asia Pacific experienced a high frequency and severity of cat events last year, including Jebi and Trami in Japan, Mangkhut in South China and flooding in India.

On the other hand, the proliferation of such events has stoked cedants' appetite for more protection.

Heerasing sees increasing demand for excess-of-loss cover in what is a traditionally quota-share dominated market.

"Quota share is a key part of how people manage capital and I don't see that changing, but as some of the larger cap insurers look ahead, there is a growing consciousness that excess of loss does provide good value and can enable them to build a programme that meets their needs."

ACR has no plans to significantly change its own retro programme, which was unaffected by last

year's cat losses, though it will increase its protection as its own GWP expands.

Nor does Heerasing expect any changes to ACR's ownership structure.

"We see no change and have no need to bring in external capital – we work extremely well with our current shareholders in terms of how we plot our journey," the executive says.

Diversification

The reinsurer last December hired Nick Macfarlane from MS Amlin as head of treaty, international, and started its push outside the region in earnest on 1 January, with the goal of having its international book comprise up to 15 percent of total GWP in the first year.

"We're bang on target – it's very encouraging," says Heerasing.

In three to five years the CEO predicts that international premiums will have grown to a third of business for the Singapore carrier.

"It is predominantly property and casualty treaty where we have been able to get our message across," he says. "We've been able to call on existing and past relationships. Clients in North America and Europe have appreciated the ability to diversify their insurance book by accessing Asian capital – it's good risk management."

He says additional overseas offices outside the region may follow but most likely not until 2021.

Heerasing also reaffirms his commitment to Hong Kong despite recent political upheaval.

"Hong Kong is and will continue to be a strong component part of our distribution network. We have a good team there and are committed to that office and that footprint – irrespective of how events have turned out.

"We still believe Hong Kong will have a strong part to play in our development going forwards."

He also says the carrier is looking at the Lloyd's market with interest to see whether its syndicate in a box solution results in a more attractive financial proposition for new entrants, including potentially ACR itself.

Within Europe "Brexit obviously has implications for access to business so we are thinking about where would be the best locations," he adds. "We're always thinking two years ahead."

ACR is also on a mission to build specialty and fac, and last year hired Ronnie Tong from Axa as CUO for facultative and specialty.

The reinsurer aims to have a 50/50 split between treaty business and fac and specialty in three to five years – at the moment the split is 65/35.

But Heerasing is at pains to stress that the carrier is seeking profitable expansion only.

"This is not growth for the sake of growth – and we are not walking in blind thinking we are suddenly going to come in and make tons of money. But we think a combination of credible, strong underwriting leaders, a clear risk appetite and an ability to deliver products that are of value and are relevant to brokers and clients, and being consistent in how we deliver them, will make this work," he says.

Within specialty, ACR sees opportunities in marine, in aviation (excluding satellite), energy, credit and surety, political risk and agriculture.

"In aviation there have been significant claims over the past 12 to 18 months and there will be more to come, alongside declining premium year on year and market exits.

"Our expectation is we are going to see consolidation in aviation. We are committed to the class – it is an area where we are investing and putting more resource in. We are unaffected by recent losses and that puts us in a stronger position than industry peers – we see more upside."

Marine, as a class of business, "has never failed to disappoint in the last 10 years", the CEO quips.

"I see significant pressure to now start driving rates upwards. We expect seven years of rate reductions to be reversed."

ACR's profitability drive is about more than "just extracting more rate" however, Heerasing stresses.

"Some will come through rates – but some of that will also come through distribution costs.

"With the advance of technology, with the advance of some of the initiatives in expense management, that will lead to reduction in frictional costs and distribution costs and that will have a positive impact for growth in insurance and reinsurance."

"How we work with our clients and brokers to reach a wider net of customers also has to form part of our thinking.

Within the region, the sprawling markets of India, Indonesia and China hold obvious promise but they are "not easy places to reach out and connect with customers unless you start using technology and reaching your customer in a more focused way", says Heerasing.

"Insurers, reinsurers and brokers have to work in partnership to inculcate the real benefits of the product."

Intermediaries are essential to increase carriers' ability "to mine data and analytics in a more forthright way to be far more targeted", he says.

Asia grows up

Heerasing believes ACR's focus on profitability is emblematic of the state of the wider Asia Pacific reinsurance industry, which has grown up significantly in the past few years.

"We are in a lucky position being in part of the world where we still see substantial underlying growth – there's at least 5 percent [annual] growth in the underlying insurance market across Asia Pacific absent an economic shock.

> "We have seen greater pressure being applied to reinsurers to demonstrate a move towards delivering real value for capital providers and shareholders"

"That growth is great but at the same time there's a concern that growth in the past was subsidised at the expense of margin.

"It's fair to say the move towards reinsurers having profitability at the core of their thinking was not going to happen overnight. It takes a while to move from a thought process of strategic growth versus the belief that Asia has to stand up on its own in terms of return on capital employed compared with the rest of the business," the CEO explains.

He continues: "We have seen greater pressure being applied to reinsurers to demonstrate a move towards delivering real value for capital providers and shareholders.

"That has gently amplified over the course of the past year. We are seeing good behaviour from the industry towards ensuring that we deliver the message to our clients that ultimately if we are going to have a very strong capital base anchored in Asia that will support clients going forward we can only do so if that capital quickly regenerates.

"It is a relationship which needs to work both ways."

He adds: "Our respective portfolios need to make an adequate return to keep capital anchored in the region so we can support our clients over the 20 years, and more, to come."

Hannover Re's Marx pinpoints Asian growth prospects

The regional MD predicts rate contagion from Japanese typhoons in windstorm-prone neighbouring markets

Hannover Re will consider partnership arrangements and pursue greater cooperation with a small group of Chinese cedants as it works to lift the proportion of business coming from Asia Pacific.

The reinsurer derived about 13 percent of its almost EUR12bn ($13.3bn) of 2018 P&C premium from the region, which is home to about 60 percent of the world's population. CEO Jean-Jacques Henchoz told this publication in August that he would look to increase that.

Hannover Re Asia Pacific managing director Michael Marx noted that the carrier would pursue different approaches to the highly heterogenous region.

"The Asean [Association of Southeast Asian Nations] market has a good potential – it is obviously not as big as India and China but with about 600 to 700 million people living in the region we are definitely looking at and pushing for opportunities," he said.

"We have different products in mind for this region and rather than expanding as a big proportional or non-proportional underwriter we are looking to add value for smaller insureds at different stages, whether in product development or product pricing."

He described these type of arrangements as "loose outsourcing" agreements.

"We will not give our reinsurance pen away but we will certainly guide direct carriers on product design and distribution," said Marx.

"We're looking at working with various partners, including affinity groups, online producers and fintechs," he added.

The company has pinpointed cyber reinsurance as a growth area across the whole region and is likely to replicate the type of arrangement Hannover Re has domestically, where it partners with fintech incubator FinLeap and its Perseus business for the provision of incident management and risk mitigation services.

"What we need to do is to find the right partners for cyber – that is something we may not invest in ourselves but outsource the arrangement to other markets as we do in Germany," he explained.

Hannover Re will also target liability, including directors' and officers', which Marx said is undeveloped in the region with the exception of Japan.

"We are looking quite a bit at distribution, at working with the right modern partners and packaging liability into property and personal accident packages and selling it online."

Indian opportunity

Hannover Re was in the first overseas cohort to gain an Indian reinsurance licence and began operations there in 2017. It had a tough year last year, aside from agricultural cover, due to flood losses and difficult market conditions.

But Marx said: "The sheer mass of country and the population gives rise to all types of opportunity.

"India needs support in the development of distribution channels and the right risk management tools of modern reinsurance.

Marx pointed out that both India and China have above-average growth potential and are major elements in its regional expansion strategy.

"In China we have adjusted our business model so we are doing business with fewer companies but in a deeper way – that has been one of the key drivers of our growth and success over past three years.

"A decade ago we tried to collaborate with everyone – now we are cooperating with far less than half of those officially licensed in China."

While it is almost impossible to compete with China Re, Marx said overseas reinsurers can offer dynamism and flexibility. He also predicted Hannover Re will benefit from local cedants' new business.

"These truly local reinsurance companies have a huge domestic market share but, as you would expect, clients will look for choice and try to reduce their concentration risk and therefore limit the exposure they would give to China Re and the like."

The famously lean carrier has shunned an extensive global footprint in favour of making senior staff travel to visit key clients and Marx said it has no plans for additional office openings in the region, where it has offices in Sydney, Tokyo, Mumbai, Shanghai, Kuala Lumpur, Hong Kong, Seoul and Taipei.

Looking ahead to next year's renewals, Marx predicted significant rate growth in Japanese property catastrophe.

"Loss creep from Jebi and the combination of Faxai and Hagibis is creating lots of pressure on our Japanese clients," he said.

"With two additional losses – and Hagibis seems to be more severe than Faxai – there will be a very marked effect on pricing on wind excess of loss, and excess of loss in more general terms, definitely for Japan.

"With regard to whether this effect will be wider, I would say a cautious 'yes', because reinsurance and ILS might face some big bills. Together with the combination of trapped capital from 2018 everyone is alert."

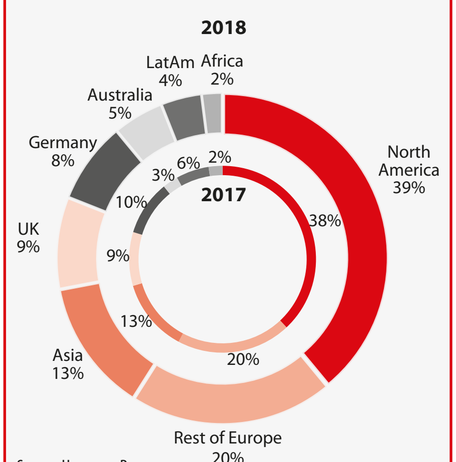
Marx predicted strong double-digit property catastrophe rate rises in Japan at the 1 April renewals, with rate contagion possible "everywhere where typhoon risk is bigger than average", including parts of China, the Philippines and Vietnam.

"There will be a new discussion about flood cover versus flood cover following typhoons. I would hope recent events would increase [cedants' appetite for] flood cover but all of these insurance companies have budgets and you can only stretch them to a limit."

He added: "I am convinced that the region is not buying enough cover vertically and horizontally.

"That also holds true for China and India – the XoL [excess of loss] premium pot of the total reinsurance market will increase – driven by China and India – as cedants buy adequate cover."

GWP split by regions



Source: Hannover Re

Reinsurers in the Lion City pushed to underwriting losses in 2018

Over half of all carriers operating in the Singaporean reinsurance space made an underwriting loss in 2018, according to data from the Monetary Authority of Singapore (MAS).

Indeed, our analysis found that reinsurance operations in Singapore worsened in 2018 as the weighted average combined ratio swelled by 34.3 percentage points, settling at 116.4 percent.

Statistics on 25 reinsurers operating under MAS supervision were collected for this analysis.

There were no new entrants to the reinsurance market in Singapore in 2018, according to the data collected. However, figures for Qatar Re have been excluded from this analysis because, as of July 2018, the reinsurer ceased writing new and renewal business from its Singaporean branch.

Qatar Re exited the Singaporean reinsurance space having only entered the market in October 2016. The series of catastrophes that hit Qatar Re's parent company – Qatar Insurance Company – drove the decision to shutter its business in the Lion City.

Meanwhile, drilling down to all active individual platforms in the Singaporean reinsurance market, the proportion of reinsurers that reported underwriting losses increased from 31 percent in 2017 to 56 percent in 2018.

Annual results for individual reinsurers diverged sharply, as the spread in underwriting results between the market's best and worst performers with active performers was 143.4 percentage points.

As for operating income, when combining the results of companies' offshore and local entities, some 11 out of the 25 reinsurers reported losses in 2018 – the same number as in 2017.

Swiss Re's Singaporean platform reported the largest operating loss of S$868.1mn ($632.6mn), while at the other end Munich Re logged a S$141.6mn operating profit for the year in Singapore.

Winners and losers

In terms of individual reinsurers' underwriting results, it is clear that Swiss Re's Singaporean operation suffered in 2018. It reported a 145.4 percent combined ratio,

> "Swiss Re's losses soared from 25.3 percent of net earned premiums in 2017 to 114.3 percent in 2018"

up 87.3 points year on year.

Its losses soared from 25.3 percent of net earned premiums in 2017 to 114.3 percent in 2018.

Looking at past data however, Swiss Re has been a relatively strong performer in Singapore, with its combined ratio in 2016 and 2017 at 89.1 percent and 58.1 percent, respectively.

Milli Re's Singaporean branch was also at the bottom of the list in 2018. Milli Re is a Turkish carrier which received a licence to operate in Singapore from the MAS in 2007 and started underwriting in 2008.

Milli Re's combined ratio climbed 49.8 percentage points in 2018 to reach 138.2 percent after the branch suffered high losses during the year amounting to over 97 percent of net earned premiums.

Meanwhile Validus Re's Singapore branch, which primarily concentrates on short-tail property and reinsurance risks, also experienced a deterioration in its combined ratio.

At 129.0 percent in 2018, Validus Re's combined ratio worsened by 45.4 percent year on year.

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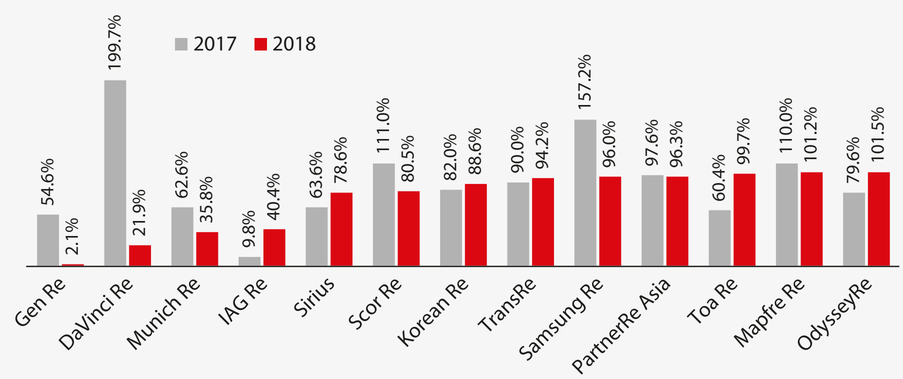
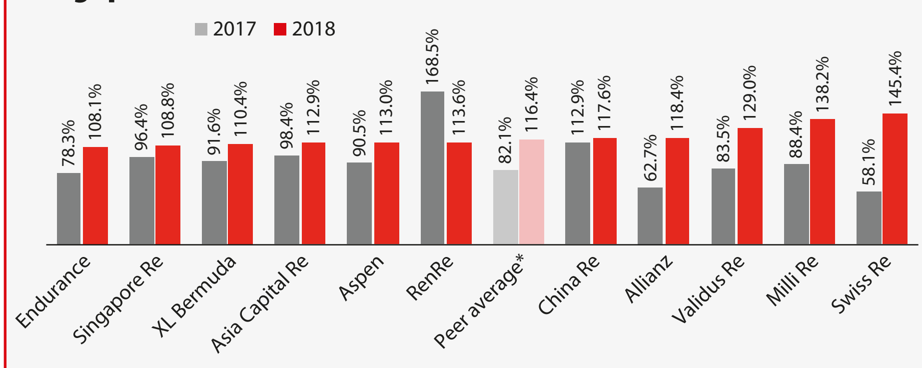
Singaporean reinsurers' combined ratio



Source: Monetary Authority of Singapore, *The Insurance Insider*
Qatar Re was excluded from this analysis as it ceased writing new and renewal business from its Singapore branch in 2018

Singaporean reinsurers' combined ratio (cont)



Source: Monetary Authority of Singapore, *The Insurance Insider*
Qatar Re was excluded from this analysis as it ceased writing new and renewal business from its Singapore branch in 2018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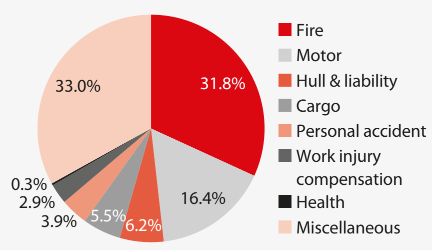
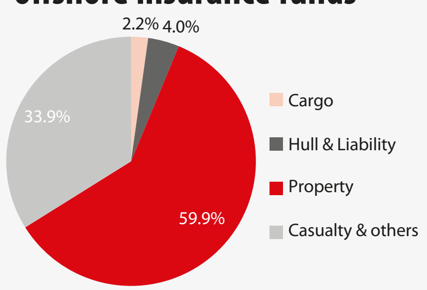
Reinsurance premiums of Singapore insurance funds



Source: Monetary Authority of Singapore, *The Insurance Insider*

Reinsurance premiums of offshore insurance funds



Source: Monetary Authority of Singapore, *The Insurance Insider*

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At the other end of the spectrum, underwriting results were unusually strong.

General Re's Singaporean operations generated a 2.1 percent combined ratio in 2018, down from 54.6 percent in 2017. The branch reported a negative figure for claims incurred, perhaps indicating a release of reserves during the year leading to a favourable effect on the overall combined ratio.

DaVinci Re – a RenaissanceRe vehicle – went from being the worst performer in 2017 to one of the best in 2018.

It reported a combined ratio of 21.9 percent in 2018, down 177.8 percentage points year on year. Similar to General Re, DaVinci Re logged a negative loss ratio in 2018 for its Singaporean branch.

Elsewhere, Munich Re's operations in Singapore logged a strong 35.8 percent combined ratio in 2018. The German reinsurer's Singaporean branch has consistently reported solid underwriting results over the past few years

It logged combined ratios fo 45.9 percent and 62.6 percent in 2016 and 2017, respectively.

Top line

Reinsurers under MAS supervision collectively reported a 2.4 percent year-on-year increase in gross written premiums (GWP), reaching a total of S$204.1mn in 2018, according to MAS figures on Singapore Insurance Funds.

Singapore Insurance Funds – or onshore policies – contain the funds established and maintained in respect of Singapore policies under the Insurance Act, while the Offshore Insurance Funds represent offshore policies, according to the MAS.

Fire premiums represented the largest source of GWP for onshore policies, taking a 31.8 percent share of all premiums in 2018. However, fire premiums remained static year on year, bringing in S$65.0mn to the market.

Singapore Re was again the largest contributor to onshore premiums as it wrote some 20 percent of the total in 2018.

As for offshore insurance policies, GWP surged in 2018 by 82.3 percent to S$8.2bn. All classes of offshore insurance increased their premiums by over 50 percent year on year.

Premiums for property insurance – the largest category for offshore policies – expanded by 59.1 percent in 2018, while premiums in the casualty class of insurance advanced by over 155 percent.

Lloyd's Asia

Elsewhere, the Singaporean Lloyd's hub, Lloyd's Asia, grew its top line for the second consecutive year. GWP in 2018 rose by 4.2 percent year on year to reach S$889.9mn.

Direct premiums for the Singapore platform grew by 12.8 percent to S$250.9mn in 2018 while total reinsurance premiums inched up by 1.2 percent to S$639.0mn.

However, Lloyd's Asia's underwriting result deteriorated in 2018. The platform's 2018 combined ratio worsened by 18.2 percentage points to 108.3 percent. By comparison, Lloyd's of London's combined ratio improved by 9.5 points to 104.5 percent in 2018.

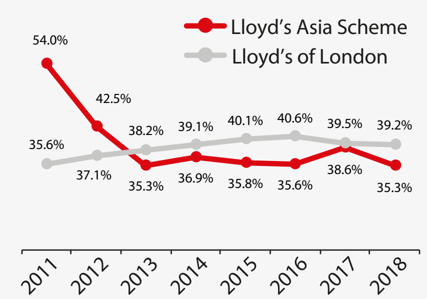
Last year's result breaks a two-year streak where Lloyd's Asia outperformed the London operations in terms of underwriting results.

Breaking down the combined ratio to its components it is clear that, while expenses have decreased year on year, losses mounted in 2018, forcing Lloyd's Asia into an overall underwriting loss.

Lloyd's Asia suffered a 73.0 percent loss ratio in 2018, up 21.5 points year on year.

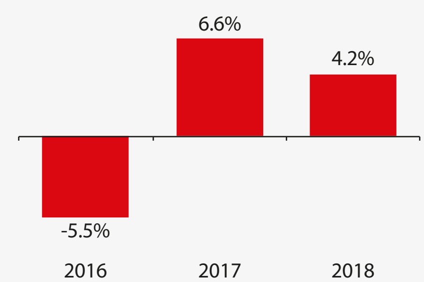
Meanwhile, expenses declined by 3.3 points to 35.3 percent of net earned premiums – the lowest expense ratio Lloyd's Asia has produced since 2013.

Lloyd's Asia expense ratio



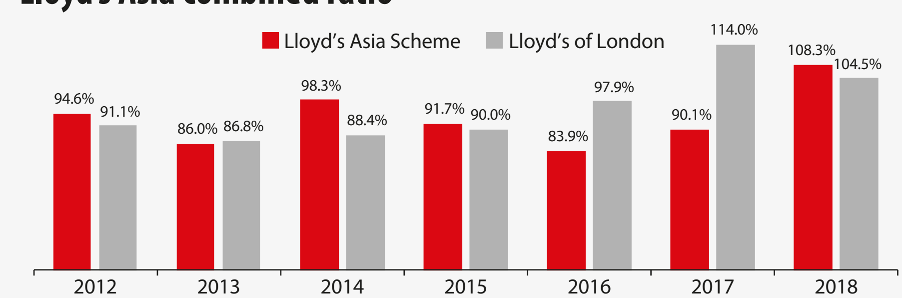
Source: Monetary Authority of Singapore, *The Insurance Insider*

Lloyd's Asia GWP growth



Source: Monetary Authority of Singapore, *The Insurance Insider*

Lloyd's Asia combined ratio



Source: Monetary Authority of Singapore, *The Insurance Insider*

Three ILS deals in Singapore's year of success

Two years ago at the 14th Singapore International Reinsurance Conference the then minister for trade and industry, Lim Hng Kiang, spoke about Singapore's plans to pay the upfront costs of structuring catastrophe bonds as the country pushed into the ILS market.

"My hope is that this grant will encourage reinsurers to issue bonds here," he added.

Lim, who remains deputy chairman of the Monetary Authority of Singapore (MAS), said at the time that the regulator was already working with parties including IAG Re to develop cat bonds.

Fast forward to today and the country has had three successes in 2019 in its drive to establish a viable alternative risk transfer marketplace, which forms part of its broader goal of being the reinsurance hub for the region.

The scheme funds 100 percent of the upfront issuance costs of cat bonds in Singapore up to a limit of S$2mn ($1.5mn) and has been key to creating what the MAS deputy chairman termed an "ILS ecosystem".

As AM Best noted in its August market segment report, Singapore has both corporate and tax frameworks to facilitate ILS issuance. ILS instruments can be issued and regulated via the special purpose reinsurance vehicle (SPRV) regulations.

"In addition, the approved special purpose vehicle scheme – which grants tax concessions to approved asset securitisation transactions – provides for tax neutrality," AM Best reported.

First out of the blocks in February was IAG, with a cat bond that provided the Australian insurer with A$75mn ($53.8mn) of annual aggregate cover for three years.

The issuer, Orchard ILS, was the first SPRV licensed by the MAS.

The regulator described the IAG cat bond issuance as a significant milestone in the development of Singapore's ILS market.

The deal was structured and placed by Guy Carpenter and David Priebe, now the firm's chairman, highlighted that Singapore's ILS grant scheme was "an excellent initiative" that "played an important part in enabling this transaction to take place".

Next up was Floridian insurer Safepoint, which in May attempted to launch a $75mn Manatee Re cat bond out of Singapore.

The transaction was designed to provide three years of cover against named storms and severe thunderstorms in an initial covered area of Florida, Louisiana, New Jersey and Texas using an indemnity, cascading per-occurrence trigger.

Originally the bond was targeting $50mn for the lower-risk class A notes and $25mn for the higher-risk class B tranche. However, ultimately the insurer had to settle for $20mn in each layer with both pricing higher than initially expected.

Security First Insurance, in contrast, tapped the cat bond market for $100mn of cover with its First Coast Re II deal, also transacted in Singapore. This was an increase on its original target of $75mn.

The four-year cover provides protection against named storms and severe thunderstorms in Florida on an indemnity per-occurrence basis with a cascading feature.

Despite being the last of the trio to be publicised the bond also claimed a first.

According to Swiss Re Capital Markets, which acted as the sole structuring agent and bookrunner, it was the first cat bond to be issued under Rule 144A for private offerings using the new ILS regime in Singapore.

Jean-Louis Monnier, who was global co-head of ILS at Swiss Re Capital Markets when he spoke with sister title that *Trading Risk* in June, said the process went "remarkably smoothly" and was quick to praise the Singaporean regulator.

According to Monnier, everyone in Singapore was "true to their word" of making the deal happen. However, he pointed out that the country is keen for knowledge to be transferred to the region and not just to be a clearing house for deals.

"What Singapore is looking to do through the scheme is to be recognised as a jurisdiction with expertise not only in the region but also globally."

It has been a consistent theme throughout the inaugural year of bond issuance.

Rajah & Tann Singapore acted as Singapore counsel on the IAG transaction. Its head of insurance and reinsurance practice Simon Goh said that this first cat bond was a "pioneer" that would help broaden Singapore's capital markets by adding a new asset class and generating a new set of service providers locally. In his view this will be needed as interest and traction in ILS picks up.

"Following this successful transaction, we are optimistic that more issuers will consider coming to Singapore," said Goh.

These successes came against a backdrop of a noticeably quiet 2019 for cat bond issuance around the globe.

First-half issuance dropped by 57 percent year on year to $3.5bn and the second half of the year has also been quieter than usual.

At the time of writing, the EUR100mn ($110.2mn) Hexagon II transaction from Covea Group was the only transaction to be issued in the second half of the year.

According to experts, though, the market is expected to pick up in 2020 due to the sheer volume of cat bonds expected to mature in 2019 and 2020.

Up to $3.1bn of cat bonds are expected to mature in the second half of this year. Analysis by *Trading Risk* showed that 22 percent, or $7.1bn, of current cat bond coverage is due to mature in the first half of 2020.

That should provide plenty of opportunity to encourage even more (re)insurers to issue bonds from Singapore.

Singapore cat bonds

Transaction	Sponsor / Ceding insurer	Bookrunner	Structuring agent	Initial size target ($mn)	Final size ($mn)	Peril and territory	Aggregate/Per occurrence	Trigger type	Length	Attachment point / initial trigger
Orchard ILS	IAG	GC Securities	GC Securities	53.8	53.8	Australian natural perils	Annual aggregate	Indemnity	Three years	$375mn
Manatee Re III 2019-1 – class A	Safepoint	GC Securities, Swiss Re Capital Markets	GC Securities	50.0	20.0	Named storm, severe thunderstorm – FL, LA, TX, NJ	Per-occurence cascading	Indemnity	Three years	$389.5mn 1E; $27mn cascaded
Manatee Re III 2019-1 – class B	Safepoint	GC Securities, Swiss Re Capital Markets	GC Securities	25.0	20.0	Named storm, severe thunderstorm – FL, LA, TX, NJ	Per-occurence cascading	Indemnity	Three years	$309.5mn 1e; $107mn 2e; $27mn cascaded
First Coast Re II	Security First	Swiss Re Capital Markets	Swiss Re Capital Markets	75.0	100.0	Florida wind	Per-occurence cascading	Indemnity	Four years	Not disclosed

Source: *Trading Risk*

A golden opportunity

Swiss Re China president John Chen on how the growth of the Chinese economy is driving insurance demand

The Chinese P&C market is ripe with opportunities for both international and domestic (re)insurers, according to Swiss Re China president John Chen.

Chen, appointed in 2016 from a senior role at People's Insurance Company of China, explained that the country's mixture of economic growth and changing regulatory environment presents a rich seam of opportunities for risk carriers.

"Total premiums written in China stood at around $5tn in 2018," Chen says.

"Its share of global premiums went from 0 percent in 1980 to 11 percent in 2018 and is forecast to reach 20 percent in 10 years' time, almost as high as the share projected for the whole of advanced Europe, the Middle East and Africa.

"China remains on track to surpass the US as the world's largest insurance market in a decade."

Chen highlighted the Chinese government's announcement on 15 October that it will allow overseas financial institutions to establish foreign-invested insurance companies on the mainland and become shareholders of those new firms.

"The regulatory change presents great opportunities for international insurance companies," Chen said.

"We have been working closely with Chinese government and industry partners over the past 20 years," he added.

"Our extensive risk expertise and strong financial capability can help China protect its economy and provide momentum for future growth to make China more resilient.

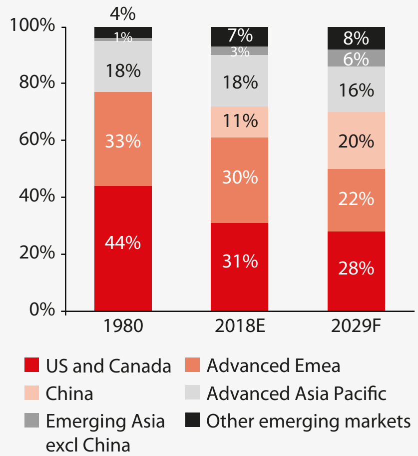
"In addition, as an international reinsurer, we can continue to play an important role in helping domestic entities to diversify their global risk."

Chen said Swiss Re saw opportunities in growing areas such as agriculture, liability, infrastructure and natural disaster cover.

Swiss Re is also looking to capitalise on national efforts to create sustainable development through products such as its environmental impact liability solution.

"Swiss Re developed a fully digital environmental risk assessment solution in line with China's Green Finance Initiative with our local partners," Chen noted.

Market shares for total DWP by main markets and region



Source: Swiss Re Institute

"It enables our clients to establish risk knowledge across various industries, establish a professional risk assessment and investigation system."

Chen added that the Belt & Road Initiative – a vast investment project in which the Chinese state aims to develop international routes to more than 60 countries – has stimulated demand for insurance.

"We haven't yet had the chance to realise our full potential in this respect, but I hope that we will have the opportunity to play a significant role in the future," said Chen.

The development of e-commerce is another source of opportunities for insurers in China, the executive noted.

"With the rapid growth of the digital economy, cyber risks are growing and becoming increasingly complex.

"Driven by regulatory requirements, cyber insurance has developed rapidly, but the market remains mostly US-focused. The market in China is still small."

However, China's development as a leader in e-commerce will soon change that, Chen said. "We estimate that total cyber insurance premiums in China were 70mn yuan ($9.9mn) in 2018. We forecast growth to 500mn yuan by 2025, a compound annual growth rate of over 30 percent."

He anticipates the Chinese government playing a significant role in driving demand for insurance and risk management as it introduces legislation around data protection.

"Meanwhile, the government may explore multi-party collaboration with (re)insurers, cyber security service companies and corporations to enhance overall cyber-security protection capabilities," Chen said.

Agriculture is another area that Chen forecast will provide opportunities.

"As the second-largest country in agricultural production in the world, the government recently issued guidelines on accelerating the high-quality development of the agriculture insurance in China, which will certainly give a positive push to the industry," he noted.

"The exciting opportunity for us is to empower our clients and partners with technology for easy access to more innovative agriculture products."

The Swiss Re China president pointed to the company's recently launched digital agricultural risk management platform as an example. It aims to improve risk management and Chinese farmers' resilience while coping with natural disasters.

In general, emerging Asia's natural catastrophe protection gap, which includes China and India, of an estimated $49bn in 2018, presents a huge opportunity for (re)insurers, Chen added.

"China's macro resilience has grown by 4 percent since 2007 on the strengths of an improved banking industry and higher insurance penetration," he explained.

"China has made significant achievements in the past years but funding the protection gap will continue to be a challenge."

Chen also noted that Swiss Re's Macroeconomic Resilience study recently ranked China in 20th place.

Overall, growth, increasing digitisation and an opening up of China's financial system present significant growth prospects for global reinsurers.

"Our business in China is riding an overall wave of growth and as economies grow, and its population becomes more affluent, the need for insurance will also grow as well," he said.

John Chen
President,
Swiss Re China

GROWING PAINS AND GROWTH SPURTS

What lessons should the reinsurance industry take from Typhoon Jebi?

Mark Morley, managing director and head of Asia Pacific, Willis Re: The key takeaway after a great deal of work around this event is that the risk landscape for Japan typhoon remains unchanged.

The average claims amount and total number of claims for this were much higher than many historical events, but we are confident that this is explained by the exceptionally high windspeeds and the proximity of the event to an area of significant exposure.

We do not believe that this loss in isolation will result in a change in view of risk by the market. However, given the very weak initial vendor model loss estimates, reinsurers will rightly be sceptical of future early estimates.

Christoph Spichtig, CEO of Scor Global P&C Asia Pacific: Jebi made landfall near the densely populated area of Osaka at high windspeeds. Had Jebi's track only slightly deviated the loss would have been much smaller.

However, the particularities of Jebi's exact track, landfall location, large number of risks affected and windspeed resulted in average losses much higher than experienced in similar events previously. High reliance was given to modelled losses and historic loss patterns without giving enough weight to the particularities of this event and then late reporting, resettlement and demand surge complicated circumstances. Jebi demonstrated the importance of taking on board all facts of a specific event and is expected to lead to a more fact-based reporting.

James Beedle, CEO of PartnerRe Asia Pacific P&C: While Typhoon Jebi subjected a highly urbanised area to extreme winds, resulting in a significant loss, over the past 85 years there have been a number of historical typhoons with similar or even higher loss potential. The key lesson to be learned is that with each new significant data point, we review the assumptions which determine our view of risk, to ensure we are using the best possible science to better understand the drivers of frequency and severity of these types of events.

Marcus Taylor, reinsurance head of Ed Broking Asia Pacific: The market still appears to be somewhat surprised by the Jebi event but I am not sure it should be. Historically, Nancy and Isewan presented similar tracks and on average Japan is impacted by 11-26 typhoons a year. But the very large number of smaller losses (in excess of a million property claims), coupled with already increased demand related to 2020 Olympics construction, has driven demand surge.

Co-insurance, where unfortunately losses are not reported to fellow co-insurers until the end of the financial year, added further complication. A number of factors inflated losses including the overlapping of events and the difficulty in allocating losses – Japan was already suffering significant flooding at the time of Jebi, which was then quickly followed by Typhoon Trami. So when we talk of lessons learned, the issues are very much secondary uncertainty associated with the loss. There is nothing intrinsically wrong with the insurance product, but if we can improve the customer experience and associated process – in this case loss assessment – then the market is open to disruption.

What's the outlook for property catastrophe rates and what do you expect the impact of Japanese losses to be in other regional markets?

Beedle: Achieving long-term sustainable pricing commensurate with the risk and volatility that we take onto our balance sheet is fundamental right now. For a number of years insurers and reinsurers have been faced with year-on-year rate erosion across Asia, whilst asset values have increased. So when we do suffer a series of losses, the impact is magnified. Consequently rates in many markets will need to correct upwards.

Morley: We anticipate a strong push from reinsurers for further rate increases, following on from the measured increases in pricing we observed elsewhere in the world at 1 June and 1 July.

Mitigating the desire by reinsurers for higher rates in Japan, the reinsurance market is maintaining a historically strong level of capitalisation, and individual reinsurers are maintaining a strong appetite for Japanese risk, especially as it is a key diversifier.

Reinsurers also enjoy stable and long-term relationships with Japanese cedants, giving them confidence that profitability will be achieved, although it is likely that there will be an increased level of differentiation from client to client when considering the renewal pricing.

Taylor: Japan will undoubtedly see some pricing correction following additional loss creep from Jebi, Typhoon Faxai and more recently Typhoon Hagibis, but the Asia markets do not like to absorb cost for other countries' losses!

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Given the challenges on loss that the market may face having Faxai and Hagibis making landfall so close together, this may impact some of the ILS markets in regards to trapped capital, with a knock-on effect on retrocession rates at 1 January. Aggregate covers should see the most significant pricing increases.

Spichtig: Challenged returns of the reinsurance markets over the past years, combined with recent losses, will further intensify the situation and reinsurance rates are expected to follow. Differentiation is made on a client-by-client basis. However, the pressure on delivering on technical rates will continue and lead to price increases in markets where correction measures are required to achieve a technical level regardless of their 2019 losses.

To what extent are casualty rates across the region fully reflective of emerging risks?

Taylor: Casualty as a class of business is growing quickly across the Asia region, though limits often remain low, reflective of the lower litigious nature of the region. There remains limited expertise in many of the casualty classes of business and thus they do not see the same capacity pressures as many of the short-tail classes.

Despite the ongoing "trade war", Asia continues to have a large export market to the US (particularly for semi-conductors, spare parts etc) and there is increasing demand for US and Canada exposures to be included in respect of product liability. Of the emerging risks in the region, they are reflective of the global picture – cyber is obviously of key concern.

Spichtig: Besides well-known emerging risks like nanotechnology, electromagnetic fields and genetically modified organisms, there are many other unknown substances that can potentially affect humans and other organisms.

One is the toxic trio (dibutyl phthalate, formaldehyde, and toluene) often found in personal care products, which may impair nervous system or cause cancer. Such types of exposures will trigger products' liability policies for third-party bodily injuries claims, if proper exclusions are not incorporated in the wordings.

There are still limited litigations around these topics, especially in Asia. Insureds' awareness is still low and willingness to accept a higher premium to cover these exposures is not present. It will likely take quite some time before casualty rates in Asia fully reflect such exposures.

Beedle: Casualty exposures vary significantly across Asia. What I think is true as a general statement is that there is increased appetite by insurers to market liability coverages and for clients to purchase, so we see this as a growth market. There are encouraging signs and we will need to remain vigilant as a market to monitor loss emergence closely.

> "The potential of the ILS market in Asia is beginning to be realised"
> *Franz Josef Hahn*

Morley: By its very definition, the term "emerging risk" describes exposures that are difficult to understand and even more difficult to quantify. But we can look to Bayer and the liability arising out of glyphosate to understand the potential downside risk arising from chemicals with as yet unknown harmful or toxic properties accumulating in the environment or our bodies – a $2bn jury award in California.

As the interconnectivity of casualty risk increases and key stakeholders, from regulators to shareholders, increase their focus on emerging risks and casualty catastrophe exposures, the ability to understand and reflect these risks in pricing will become increasingly important.

What conditions need to be met before the ILS market can really take off in Asia?

Nick Garrity, CEO of IGI Labuan: A number of major institutions have been working on building opportunities for ILS in the region – particularly in relation to disaster financing for NGOs and public entities. However, there has been very little traction.

The higher cost of ILS structures compared to traditional indemnity products is a challenge for some buyers – particularly those that make invalid comparisons between the two types of structure. You can't compare apples with pears.

ILS specialists and intermediaries need to engage more with the region, as well as risk-financing experts working for the public sector and large commercial organisations in order to realise the potential value of these products.

Spichtig: In most parts of Asia, the penetration of the ILS market has been comparatively low over the past years, mainly driven by the abundance of catastrophe capacity. Further, buyers need to build more experience with the type of protections offered by ILS market and their elements including collateral, collateral release and trust accounts, which is still not widely spread in Asia. Regulators need to be more supportive in effectively recognising and facilitating its usage by ceding companies.

Franz Josef Hahn, CEO of Peak Re: The potential of the ILS market in Asia is beginning to be realised. The Monetary Authority of Singapore is fostering a nascent hub for ILS risk transfer in Asia with a supportive regulatory system and a grant scheme to fund the upfront costs of bond issuance. This supportive environment facilitated the first catastrophe bond successfully issued in Singapore in February 2019. Earlier in 2019, Hong Kong-domiciled Peak Re completed Asia's first reinsurance sidecar transaction using the special-purpose insurer Lion Rock Re, which secured $75mn capital investment, and we are aware of numerous other Asian insurance and reinsurance companies that are working towards future bond placements.

To sustain this momentum bond issuers need to demonstrate a good track record of underwriting performance and provide appropriate data to potential investors. We want to see a two-way mobilisation: Asian risks being securitised into ILS format and Asian capital investing into the specific asset class.

Taylor: The term ILS is used quite widely as an all-encompassing "buzzword", but if you look at the wider convergent capital in the market, the major growth over the last 10 years has been in the collateralised reinsurance space.

Yet much of the regulatory focus has been on cat bonds and hasn't yet addressed collateralised vehicles. General lack of infrastructure has often been used as an excuse, but as we have seen in Singapore with the issuance of the first cat bonds, much of this knowledge is easily transferable.

General willingness to act in these markets is also a key factor – hopefully through grant schemes and tax incentives we will see more application.

Modelling is also used as an excuse, but

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the lack of understanding and education at cedant level on how this can be applied to their business is a major factor. This includes recognition by regulators, lack of reinstatements etc. Many hold a view of the ILS market of five years ago but things have moved on.

Perpetual soft market conditions have also caused many ILS markets to be wary of Asia – though we are starting to see some (having suffered through the US in recent times) looking to diversify and write Asian risks.

How is China's Belt and Road initiative (BRI) changing reinsurance dynamics in the region – and what are your expectations for its impact?

Garrity: The expertise of the international insurance market in risk financing and engineering would deliver significant value to the BRI. But the expected positive impact for the market is yet to be realised. This could be because of the long development cycles of these massive projects and the ambiguity around whether some infrastructure projects in the region are actually part of the initiative. More likely is that most of the projects that fall under this initiative have been placed with local Chinese carriers and reinsured back into China. It's an obvious growth opportunity for China, and the local (re)insurance market has been getting first pickings of these opportunities.

Morley: The BRI unquestionably offers the reinsurance industry a significant growth and income opportunity but access to the business source will likely be less expansive than previously understood as much of the traditional BRI business is being handled by the larger insurance companies in China. The standard format has been for Chinese insurance operations to work closely with local insurance companies by way of fronting agreement (where required) with most of the project being ceded back to China and co-insured by three to five local companies, depending on the size of insured value.

However, when it comes to the more complex projects or where projects fall into the exclusion of existing pro-rata contracts (delay on start-up, offshore windfarm, underground risk, etc.), in the last few years, we have seen a significant growth. That's true not only for professional facultative reinsurers, but also for international insurance companies.

Along with the steady growth of BRI, the opportunity to extend insurance coverage for BRI clients offers additional opportunities, especially in the specialty lines of kidnap & ransom, political risk, project professional indemnity (PI) and cyber.

Beedle: The BRI should be viewed not as a standalone phenomenon but as part of significant pan-Asian infrastructure spending. This is a clear opportunity for reinsurers and their clients to participate in a growing pool of income across multiple product lines, from engineering to surety.

This will also increase the number of cross-border transactions where contractors from one country are successfully bidding for contracts outside of their traditional home markets, creating opportunities for (re)insurers to support larger and more complex "interests abroad" programmes.

> "The BRI should be viewed not as a standalone phenomenon but as part of significant pan-Asian infrastructure spending"
> *James Beedle*

Spichtig: We see a trend evolving from engineering, procurement, construction and financing to more of public-private partnership, build-operate-transfer or M&A, as Chinese investors are no longer focused on lending only but also become shareholders in projects and assets through special purpose companies.

(Re)insurance requirements are expected to evolve from construction/erection all risks (CEAR) to more sophisticated and broader ranges of (re)insurance products, in order to protect the interests of the Chinese investors and their local joint ventures. These include CEAR, property, delay in start-up, business interruption, marine cargo, political risks, single-project PI and bond. The initiative will further lead to increased cooperation between Chinese and foreign companies.

Hahn: The BRI is one of the most ambitious economic development projects of the 21st century.

It is estimated to affect about 4.5 billion people in 65 countries, about 60 percent of the world's population and 30 percent of its GDP.

Total BRI infrastructure investments up to 2030 could reach $7tn, with about 70 percent of funds expected to be invested outside China. But the sheer size, scale and complexity of the envisioned investment activities – compounded by the heterogeneity of the territories involved – will entail formidable risk-management challenges in the areas of commerce, regulations, politics, terrorism and environment.

Against this backdrop, both public and private stakeholders investing along the BRI need insurance capacity and expertise in lines such as engineering, property, credit and surety, marine, energy and casualty. In addition, there are niche opportunities such as public non-payment, expropriation and political violence.

What evidence are you seeing that the recent run of natural catastrophes in Asia has changed insurers' risk appetite?

Hahn: The increased visibility of natural catastrophe losses in parts of Asia is the natural consequence of the meteoric growth in the insurance markets of the region in recent years. Typhoon Lekima, for example, resulted in economic losses in excess of $9bn in China in August this year.

This scale of loss is perhaps to be expected given the economic growth in China over the past 30 years, the increased value of assets as a result and the increased insurance penetration that now means that the Chinese insurance market generates more premium than any other market except the US. Similar rates of growth are now seen in much of developing Asia and larger natural catastrophe losses should be expected in the future.

Garrity: I have seen no material evidence that risk appetite has changed. Until the treaty market undergoes a significant shift in clients' nat cat capacity, there will not be a change driven by the direct insurers. That is why this round of treaty renewals are interesting for everyone in the market – we are waiting to see if there will be a more restrictive view of capacity allocation or pricing in the 1 January renewals.

Beedle: Asia remains the most cat-exposed region in the world, so recent cat activity isn't new to the market.

Our insurance clients manage their balance sheets and earnings volatility prudently so the changes we have seen have been more subtle than revolutionary.

Our own clients' appetite for retained

volatility has stayed constant, if not slightly reduced, leading to more purchasing from the reinsurance market.

Morley: Losses typically serve to push primary demand, which is good for reinsurers who price the ceded business correctly. Growth opportunities remain abundant, which is driving up the top line and, despite some minor contraction, available capital has been more than adequate to meet demand growth in the region.

The reality is that for international reinsurers, market access will be the big challenge. It isn't always easy for foreign companies to get a slice of the pie. In China, for example, domestic reinsurers' capacity and relevance is increasing, and their skills bases are developing at pace. It seems entirely plausible that most of the Chinese risk will end up being managed in China, and that large local reinsurers will ultimately assume a significant share of regional risk, too.

What are the opportunities and challenges for reinsurers regarding climate change?

Beedle: The opportunity, if that's the right word, is that climate change is firmly on the mainstream agenda, both politically and socially. The (re)insurance community has an opportunity to play a central role in helping communities enhance their resilience to these emerging threats and the protection gap that persists across the region. Of course the challenge with both climate and increased urbanisation is that asset values and loss potential outpace the premium levels required for sustainable pricing, leaving the market at a pricing disadvantage. Keeping ahead of this will be critical.

Hahn: Reinsurance will be vital to meeting the increased risks and in continuing to fulfil its historic role of ensuring the capital resilience of insurance companies and so ensuring societal economic resilience in the wake of catastrophe.

Those reinsurers that can provide continued access to efficient contingent capital and offer insight into the changing nature of the risk should play a vital role in meeting this challenge. Proper understanding of the changing nature of risk and quantification of this change is both a major challenge and an area in which reinsurers can provide an additional service to their cedants.

Uncertainty regarding the scale of the impact of climate change on future extreme weather events makes quantification tricky. Peak Re employs expert catastrophe modellers and mathematicians capable of analysing emerging loss and risk trends. We have also formed a partnership with the Shanghai Typhoon Institute to collaborate on research of typhoon risk in the eastern Pacific.

Spichtig: While climate change presents major physical and financial risks for the (re)insurance sector, they also create business opportunities. The increase of extreme weather events and the necessary corollary transition to a lower-carbon economy stimulate the development of climate change mitigation and adaptation solutions.

Scor has been developing underwriting capacities in the area of low-carbon energy, agriculture and natural catastrophes, to play a role both in mitigating climate change and adapting to its consequences. As an example, Scor is well positioned to support insurance of wind across the supply chain from manufacturing of turbines to transit to construction and then also after hand-over.

We have wind farm expertise supporting our Asia Pacific underwriters. While we are coming off a small base, we have quadrupled wind premiums last year. With more intense and volatile weather affecting for example energy production and crop yields, parametric insurance solutions based on weather indices become more attractive and we want to be well placed to capitalise on this opportunity.

Morley: Climate change, and combatting it, is one of the critical challenges for Asia – a region where some national economies are still heavily dependent on extractive industries like coal. They are actively having to consider what will happen when climate-related concerns begin to undermine historic economic models, although for some the range of realistic "green" economic alternatives may be slim.

Other countries and regions face a real physical threat. Rising sea levels imperil many coastal communities, while changing weather patterns may be exacerbating catastrophe risk. Reinsurers and brokers know rather a lot about climate change, perhaps more than any other sector outside academia. As brokers, our detailed understanding and analysis of physical climate risks supports governments, multi-lateral development banks, and private organisations and institutions and helps them understand and mitigate the risks of climate change.

For example, we can help those financing development projects to price climate risk accurately into the debt or equity structure of their projects and ensure that adequate insurances are part of the full spectrum of risk management.

Garrity: An increase in the frequency of natural catastrophes in the Asia region requires a change in approach from (re)insurance buyers and providers. As a result, there will be an increased penetration into existing (re)insurance products that provide financing in relation to nat cat, which will provide an opportunity for more sophisticated structures like ILS to present an alternative to traditional methods.

The good news is that the (re)insurance market already has these tried-and-tested tools at its disposal to further support the needs of companies, governments and populations for this increased risk to life and property. It is just a case of bridging the gap between the vendors and designers of these specialist products.

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Asia Pacific diversification a goal for ILS managers: LGT

Pascal Koller, partner and portfolio manager at LGT ILS, explains that the firm has been expanding in the region

Pascal, how important is the Asian market for you as an ILS manager?
At LGT ILS Partners, we maintain a diversified portfolio. The densely populated regions with significant value concentration in Asia and the southeast Pacific, such as Japan, Australia and New Zealand, represent an interesting opportunity to optimise our portfolios, away from US and European risks. As such, we have been allocating to this region for many years and have also paid our share of losses, notably after the 2011 earthquakes in Japan and New Zealand, and also the recent typhoons in Japan. These events also allowed us to prove our long-term focus as an ILS manager. In recent years, we have gradually increased our capacity and allocation in these regions, underlining our commitment to Asia. On another note, the Asian region is also an important contributor of capital in our ILS funds. We cater for institutional investors, typically pension funds and large government entities, and a part of our investor pool is located in Asia. We have investors in Japan, South Korea and Australia, to name but a few. LGT maintains local offices in Singapore, Hong Kong and Sydney, and our team acts as relationship manager to the investors in the region. And similar to our reinsurance allocation strategy, we have every intention of further growing our investor pool in Asia.

To slightly change the subject – climate change is very topical; surely you must receive questions from investors on this. How do you respond to them?
Indeed, we received questions from our investors after the catastrophe events of 2017 and 2018, and also due to the recent focus on climate change. The main questions are around the quality of the models used to assess risk and exposure, whether the uptick in event activity over the past two years might be a "new normal", and lastly if investors are still getting paid for taking property catastrophe risk. Clearly, while climate change affects us all, we believe that the reinsurance and ILS market is managing this risk to the best possible extent. The catastrophe models used to assess the risk transfer are constantly reviewed and adapted to cater for potential increases in severity and frequency. Furthermore, a typical reinsurance transaction only runs for 12 months, and so, as new insights lead to adjustments in models, the corresponding price adjustment will be seen almost immediately. Therefore, even though the industry works with modelled assessments, property reinsurance transactions are rather short-term and changes in models should not lead to any significant disruption of the reinsurance market.

Some time ago, LGT ILS established a rated reinsurance carrier in Bermuda. Can you briefly explain the motivation of running such a structure, given that you are an ILS manager?
Indeed, LGT ILS maintains a Bermuda-based commercial reinsurance carrier by the name of Lumen Re. The carrier is truly a first of its kind: we strive to combine the benefits of ILS – such as the low credit risk and the stable capital pool – with the ease and flexibility of trading traditional reinsurance. In the past, when asked to provide rated paper, as an ILS manager, we relied on a third-party reinsurer to act as fronting partner, to effectively transact on our behalf. This ultimately defeats the purpose of ILS – namely the strong capital backing and the limitation of credit risk. Whilst the limits still need to be collateralised towards the fronter, the cedant facing the fronter in turn does not get any benefits from the fact that an ILS fund is backing up the line. Lumen Re represents the perfect solution to this challenge – it retains the collateral for ILS transactions and allows our cedants to face a rated carrier. And as each transaction remains highly collateralised, our clients receive the main benefits from trading with an ILS manager.

We have talked a lot about property catastrophe risks. How important are other risk categories for LGT ILS, or even emerging risks such as cyber?
Our entire team has their background in reinsurance – we are a team of underwriters, not necessarily asset managers. As such, we fundamentally believe that the merits of ILS come into play where the traditional reinsurance model reaches its limits. Mega catastrophe events represent a significant stress test to the reinsurance industry, as some carriers are either not willing or able to fully stomach such scenarios – they have to limit their incoming risk in mega-zones, or rely on retrocession capacity. This is exactly where ILS capital comes into play. By allowing large institutional investors such as pension funds to take on such extreme catastrophe risk directly from the primary insurers, we provide our cedants with an extremely solid back-stop against a systematic risk of capital shortage. However, we also believe that ILS should really focus on such extreme catastrophe risks. Diversifying away from property cat should only be entertained in business areas where the same premise of extreme events applies – such as a pandemic for a life insurer. As such, we do not believe that ILS managers should engage in long-term transactions such as casualty, marine, energy, aviation – this is where the reinsurance model works perfectly fine and the additional capita from ILS investors is simply not required. Cyber, however, may well develop into such an extreme scenario, and we are following this space closely. As the exposure data, loss scenarios and risk models become more robust, the ILS market may well be the natural party in the value chain to absorb cyber risk.

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