



# Retro and Retakaful

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The International Takaful Summit 2009

2<sup>nd</sup> July, 2009

- Setting the Scene
- Retrocession Market Risk & Catastrophe Losses Update
- Importance of Retrocession Protection as a part of Enterprise Risk Management
- Market Status
- Market Environment & Peak Exposure Solutions

- **Retrocession** - the provision of Retakaful to professional Retakaful providers
- Retakaful market is expanding, over **10 International Retakaful operators or 'windows'** throughout Asia, the Middle East and North Africa
- Who provides the **retrocession cover** – Retakaful operators to each other or conventional? Darura applies
- **Potential spiral effect?**
- Long-term aim; an **integrated Takaful chain** participant to Takaful operator to Retakaful operator to Retakaful retrocessionaire.
- **90% of required Treaty capacity** can be provided by the Retakaful market. Natural Hazard is not a major concern but is there value in the creation of a large risk facility to encourage retention of contributions within the Takaful sector for non-accumulating peak risks? Fiscal stimulus opportunities?

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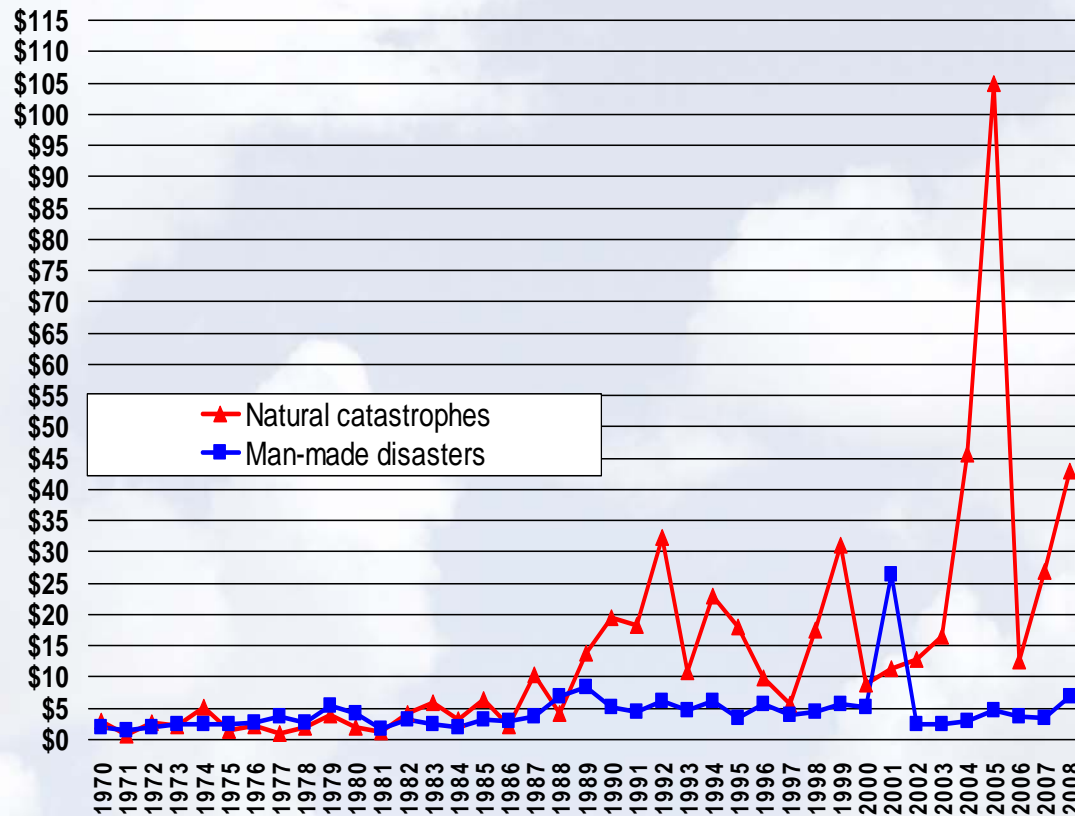


# Retrocession Market Risk & Catastrophe Losses Update

# Global Insured Event Losses, 1970–2008 (Property and Business Interruption)

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Source: Swiss Re, *sigma*

- Graph shows global event losses affecting insurance and takaful industries since 1979, the year of the establishment of the first Takaful operator
- Offshore Energy and Marine have contributed significantly to 2005 figure (US \$2-5 billion estimate)
- Natural Catastrophe aggregate losses for 2008 totalled US \$44.7 billion

## Retrocession Market Risk & Catastrophe Losses Update

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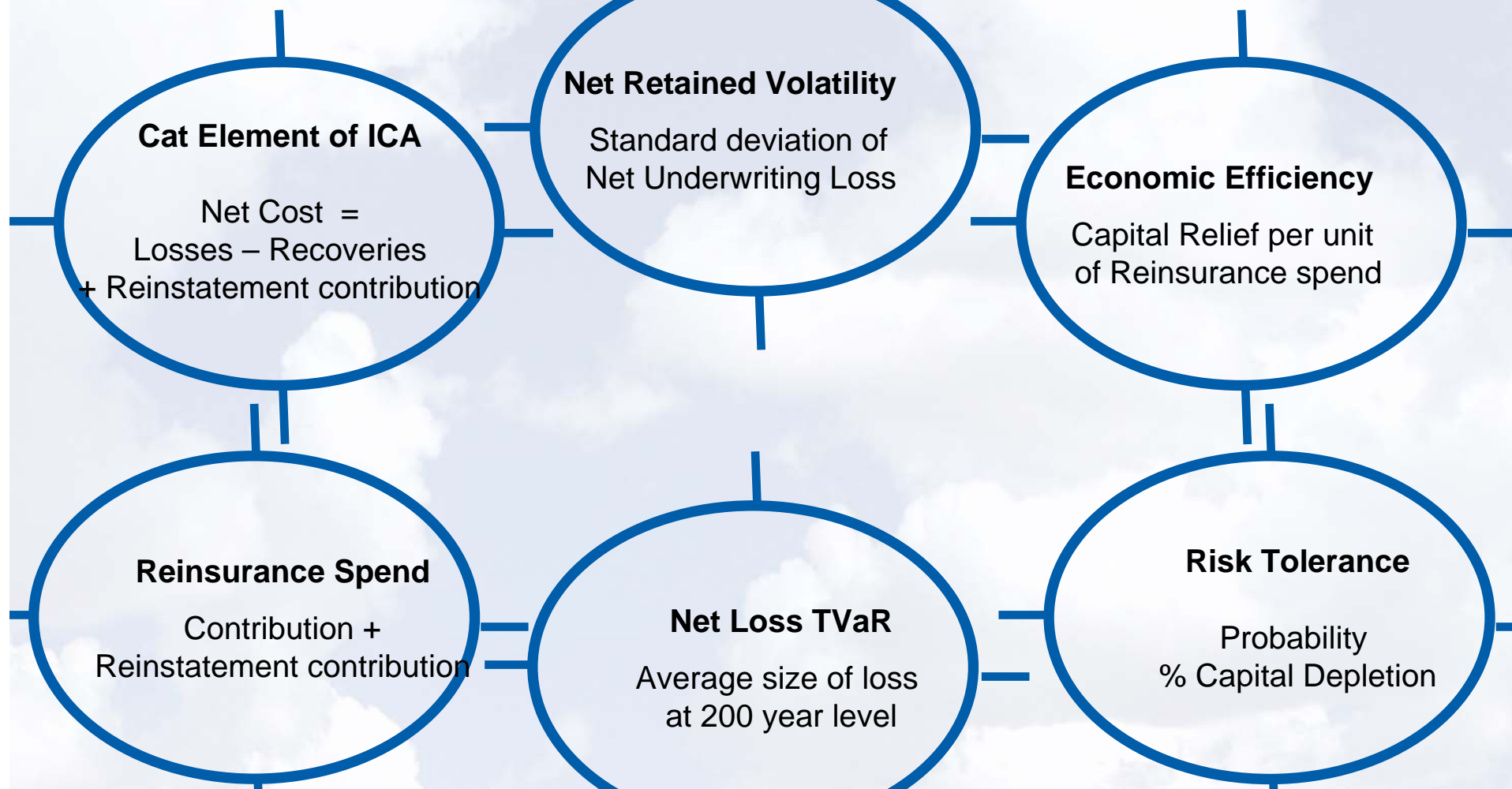


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# Importance of Retrocession Protection as a part of Enterprise Risk Management

- Historically retrocessional protections have been secured that provide
  - Continuity
  - Stability
  - Cost efficiency
- Capital market turmoil has emphasised
  - Importance of prospective enterprise risk management
  - Necessity of an anticipatory and complementary retrocession strategy
- Key success metrics need to be examined



**Importance of Retrocession Protection as a part of ERM**

## Key Success Metrics

- Quantitative risk assessment and profiling
- Stochastic modelling of risk
- Catastrophe portfolio management
- Rating Agency regulatory and account impacts
- Loss reserve risk
- Capital adequacy and return on capital

## Defining Risk Appetite

- A strong surplus might allow purchase of retrocession strictly for economic efficiency against a single large event loss
- Risk appetite may be less bold and protection of capital against a number of major losses may be management's primary concern
  - but without jeopardising economic efficiency
  - Management of results volatility is also a consideration



# Market Status

# Global Cumulative Retro Event Ultimate Net Loss Capacity

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USA / London / Europe

Bermuda

Currency: US\$

<b>Total</b>	<b>2,360,000,000</b>

<b>Total</b>	<b>5,725,000,000</b>

\* Others would include Greenlight Re, 'smaller' Lloyd's Syndicate participations, GIC Re, Toa Re, Sompo, QIC International

## Market Status

# Global Cumulative Retro Per Risk Ultimate Net Loss Capacity

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- Estimate of the theoretical maximum market capacity for single per risk excess programme in a peak territory

Market Segment	Maximum Per Programme Capacity
US	\$225,000,000
Bermuda	\$150,000,000
Europe	\$75,000,000
London	\$250,000,000
<b>Total</b>	<b>\$700,000,000</b>

Please Note: US market segment includes domestic direct writers

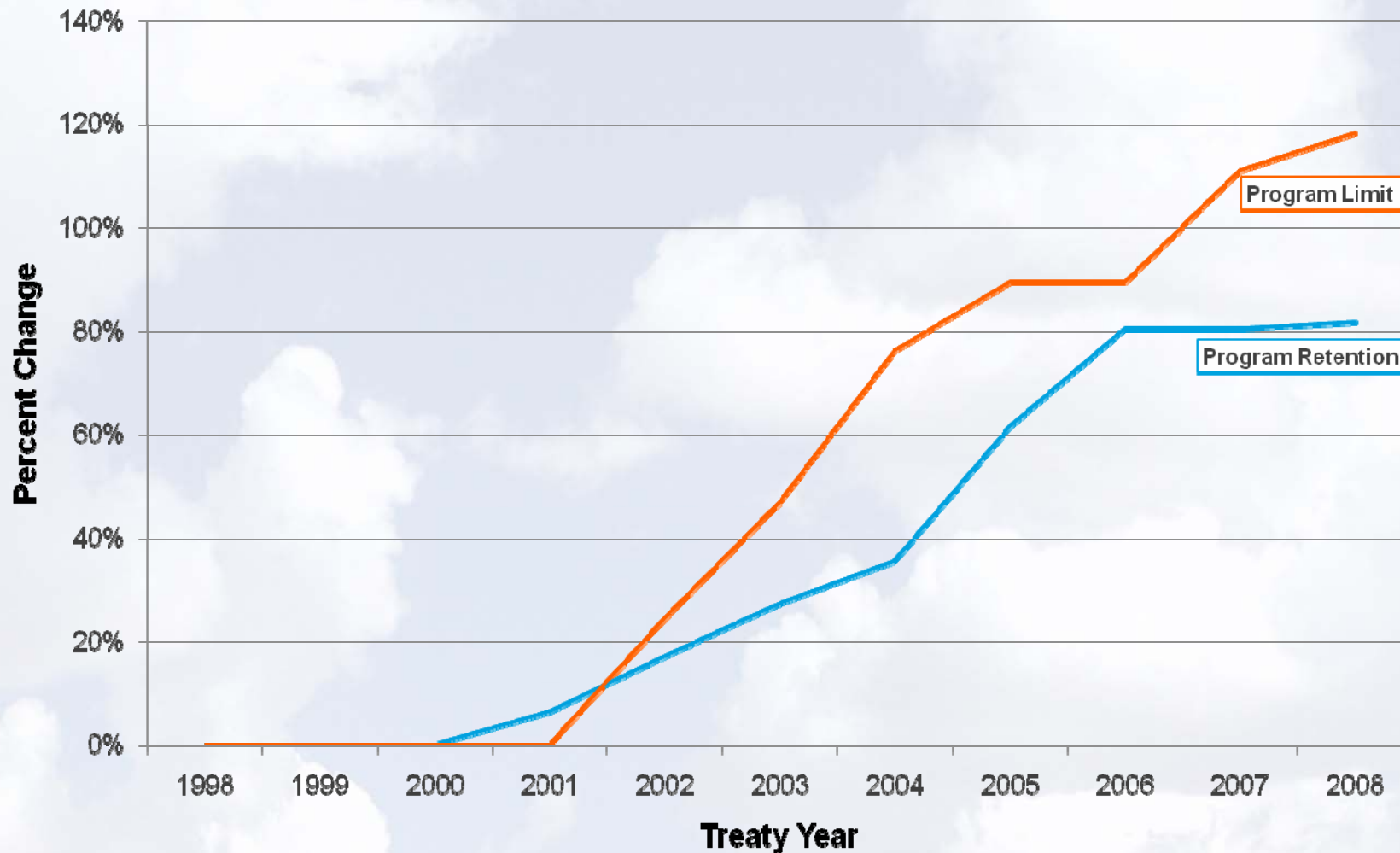
## Market Status

# Per Risk Peer Company Review

## Cumulative annual retention and limit change

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### Market Status

## ■ Pricing:

- Driven by individual carrier loss experience and exposure change
- Current expectations are risk adjusted price change of +5% to +10%
- Reinsurers' cost of capital will pressure capacity layers with low ROL
- Property facultative pricing expected to firm


## ■ Capacity:

- 2008 signed line = 2009 available capacity for most programme layers
- Insurers balancing security concerns vs desire to diversify counter-party credit risk
- New capacity is limited for layers exposed to critical catastrophe perils
- Non-cat exposed capacity is readily available

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# Market Environment & Peak Exposure Solutions

- Treaty Property retrocession market has materially reduced in terms of available capacity, with resulting pricing at historic highs
- “Worldwide” capacity still perceived to represent best value but very limited (confined to a handful of significant markets plus some followers)
- Optimum capacity is achieved for Pro Rata, Direct and Facultative portfolios. The inclusion of Excess of Loss acceptances severely restricts capacity
- New capital (“sidecars”) not currently being deployed into retro ventures – prospective view is no significant change unless there is a major Natural Hazard loss
- ILS currently expensive, with limited providers, but expected to regenerate over time

## Market Environment & Peak Exposure Solutions

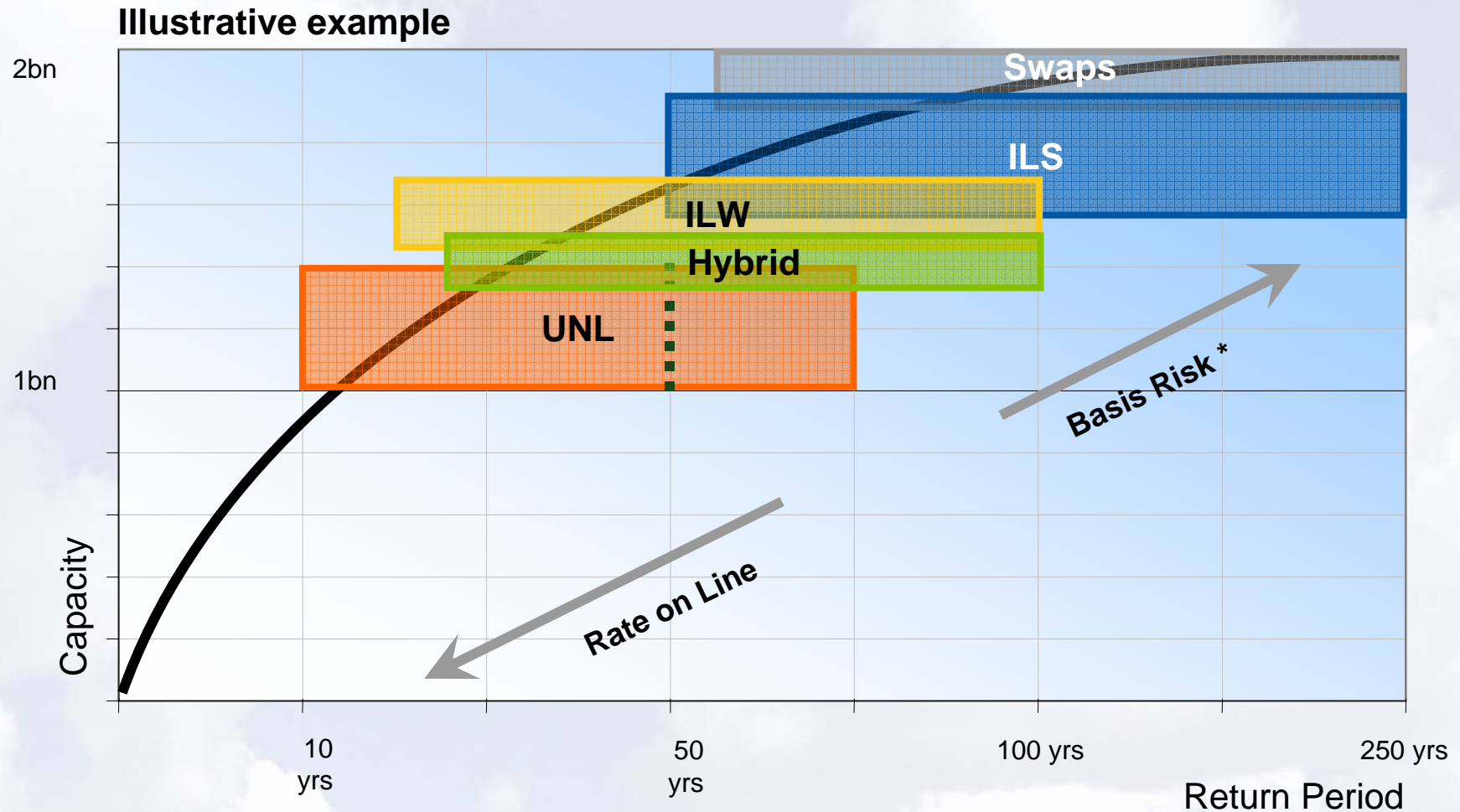
- Additional buyers coming to the market prompted by
  - Increased attritional loss development
  - Poor investment returns
  - Continued dollar weakness
  - 33% fall in equity markets since June 2008 affects both buyers and sellers
  - ILS market still seen as “ineffective” hedge
  
- Aggregate products – significantly increased demand
  - Plenty of interest but very few sellers
  - Cat aggregate is very small
  - Scarcity charge built into pricing

- Finite or structured retrocession
  - Very little currently available
  - Plenty of interest but very few sellers
  - Very few completed transactions owing to accounting uncertainties
  
- Maintain flexibility
  - Alternative adjustment features
  - Proportional reinsurance
  - Facultative solutions
  - Aggregate solutions
  - Cat swaps
  - ILS solutions

# Blended Purchase to achieve \$1bn of Capacity Incorporating Peak Exposures

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\* With the exception of Swaps

## Market Environment & Peak Exposure Solutions

# Significant Purchase for Peak Territories Ultimate Net Loss Solutions

- Direct and Facultative Traditional Ultimate Net Loss
  - Favourable economic match with Retakaful operator's economic requirements
  - Accesses primary E&S reinsurance markets
  - Territorial scope needs to be specific if placement is to be optimised

## Market Environment & Peak Exposure Solutions

# Significant purchase for Peak Territories Ultimate Net Loss Solutions

- Treaty (excluding D&F) Ultimate Net Loss
  - Decreased value for money than for Whole Account but this disadvantage is offset by increased numbers of sellers of capacity which increases supplemental purchasing opportunity
  - Such capacity may increase post major loss activity (e.g. Sidecars)
  - Named territory purchasing helps pricing

## Market Environment & Peak Exposure Solutions

# Significant Purchase for Peak Territories

## Hybrid Solutions

- RepliCat, SelectCat and SynthCat all help to bridge the gap between the retro market and the direct reinsurance markets
- SelectCat and SynthCat can be optimised to minimise basis risk
- Such products provide increased access to the direct markets at a minimal loading and therefore the pricing is more directly aligned
- Used mainly for International purchases to date
- Capacity can become more limited in a hard market environment
- Could work well conceptually with a territorially specific D&F placement

## Market Environment & Peak Exposure Solutions

# Significant Purchase for Peak Territories Industry Loss Warranty Solutions

- Significant capacity always available for peak exposures worldwide
- Significant activity – our experience is that this is up on 2008, despite press commentary
- Spot purchasing opportunities often provide best value
- Currently, most economic benefit seen above the 30 year return period

## Market Environment & Peak Exposure Solutions

# Significant Purchase for Peak Territories Insurance Linked Securities Solutions

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- Recent financial markets turmoil has impacted investor appetite and pricing, but interest is now regenerating
- \$200m issuances for both USA Hurricane and Euro Wind are now deliverable
- Shelf issuances will improve economics
- Investor appetite has increased for the lower attachment (e.g. USA Hurricane @ 50 years)

## Market Environment & Peak Exposure Solutions

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# Retro and Retakaful

- The combination of traditional retrocession, hybrid solutions and capital markets enables optimal access to available Natural Hazard capacity
- Property retrocession market can provide substantial Event and Risk capacity but pricing is at an historic high
- Retrocession strategy is gaining traction as an important part of Enterprise Risk Management in the eyes of investors and analysts
- Global financial crisis – should the fiscal stimulus plans of the Islamic community provide an opportunity to maximise retention of projects within the Takaful system through increased co-operation between national Operators?

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