

# Responding To Risk

## Enterprise Risk Management Seminar

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Wednesday 13 September 2017

Actuaries Institute • Sydney





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# Insurance-Linked Securities (ILS) impact on the reinsurance market

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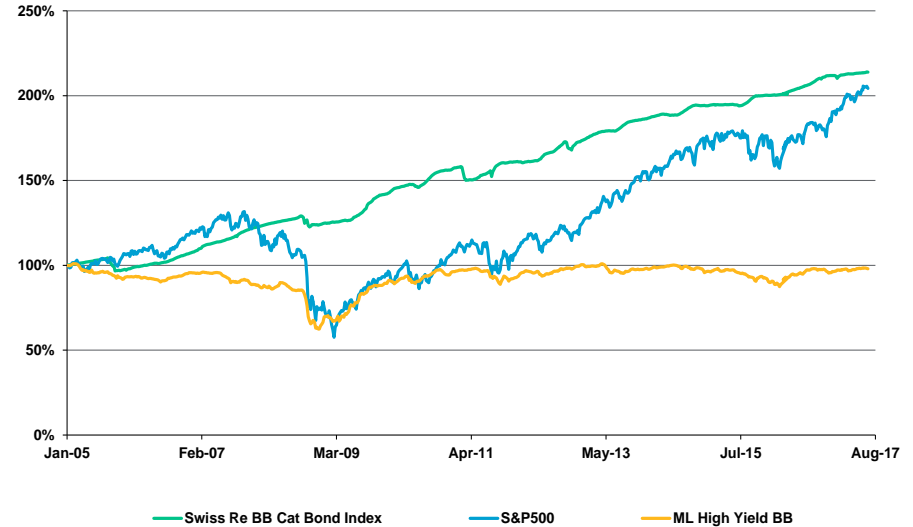
*This presentation has been prepared for the Actuaries Institute 2016 ERM Seminar.  
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# Low global interest rates... attractive returns and low correlation

Nominal 10-Year Sovereign Yields

Percent





## Better links between risk and capital



### What sellers want....

- Absolute returns
- Diversified returns
- Well-modelled risk
- Liquidity
- Short tail

### What buyers want....

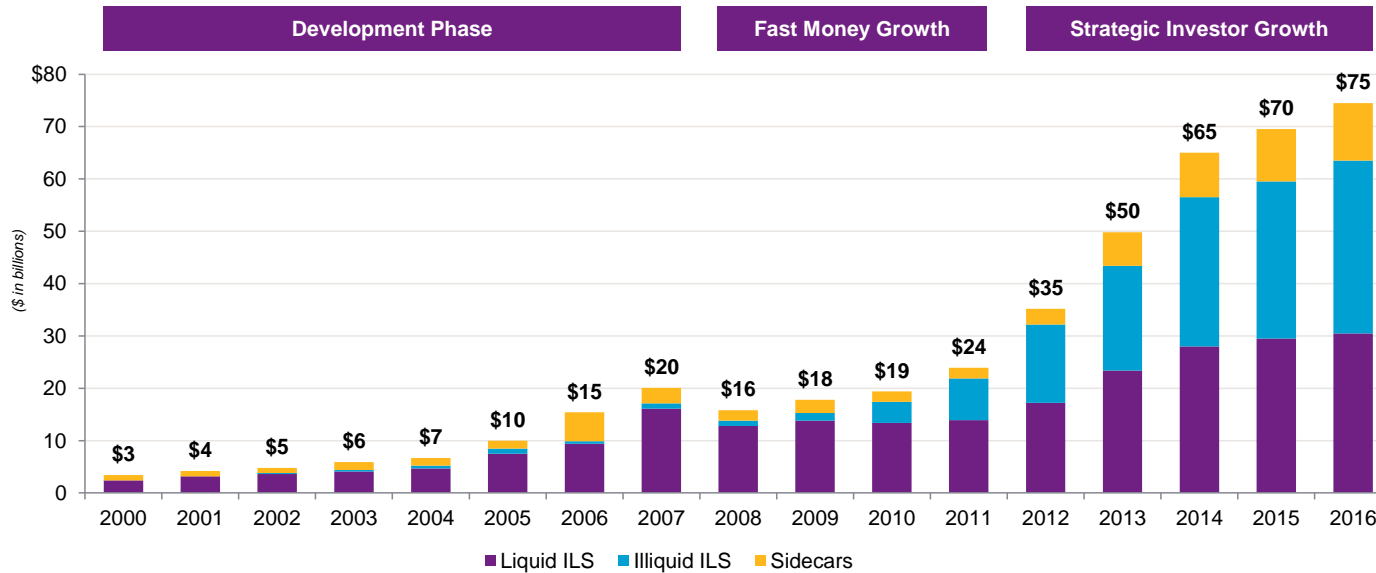
- Indemnity
- All perils
- Cost-efficient capital
- Certainty of payment
- Multi-year

- Sentiment is changing and increased flexibility leads to significantly increased opportunity



## Continued market growth and increasing flexibility

- Significant growth entering the sector
- Accelerated growth in Collateralised Re and Sidecars in last 4 years





## ILS risk appetite – an alternative model for assessing risk

### Traditional Reinsurance Model

- Global (overweight US)
- Predominantly equity funded
- Ability to leverage
- Crave diversification
- Might want a 10% return

### Alternative (ILS) Model

- To date ... predominantly US (and cat) focused
- Inability to leverage
- Diversification largely ignored
- Pension fund and other money
- Might want a 5% return

### Simple example for \$100 layer in the USA:

#### Traditional approach

E(Loss) = \$25

Capital allocated = \$70

Cost of capital = \$7

Cost of writing business = \$32

#### Alternative approach

E(Loss) = \$25

Capital required \$100

Cost of capital = \$5

Cost of writing business = \$30



## ILS risk appetite – an alternative model for assessing risk

### Traditional Reinsurance Model

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Simple example for \$100 layer in ~~the USA~~ Australia:

#### Traditional approach

E(Loss) = \$25

Capital allocated = ~~\$70~~ \$10

Cost of capital = ~~\$7~~ \$1

Cost of writing business = ~~\$32~~ \$26

#### Alternative approach

E(Loss) = \$25

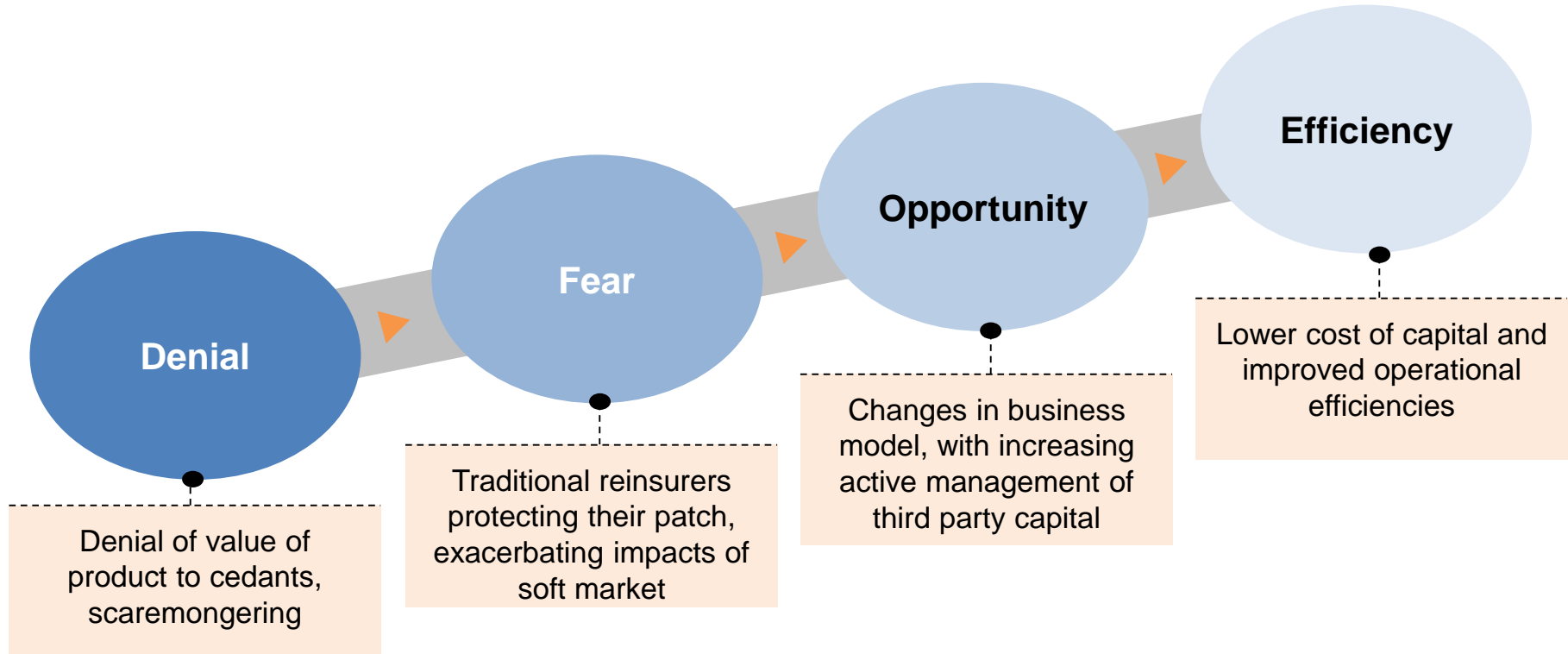
Capital required \$100

Cost of capital = \$5

Cost of writing business = \$30



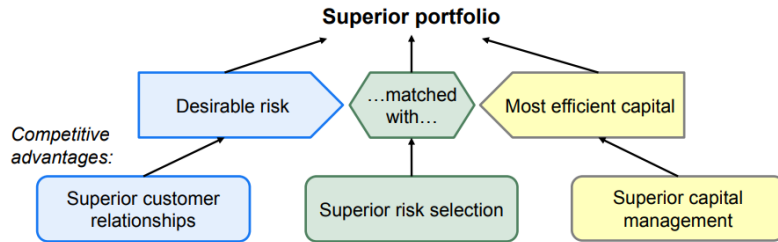
## What has been the reinsurance industry response?





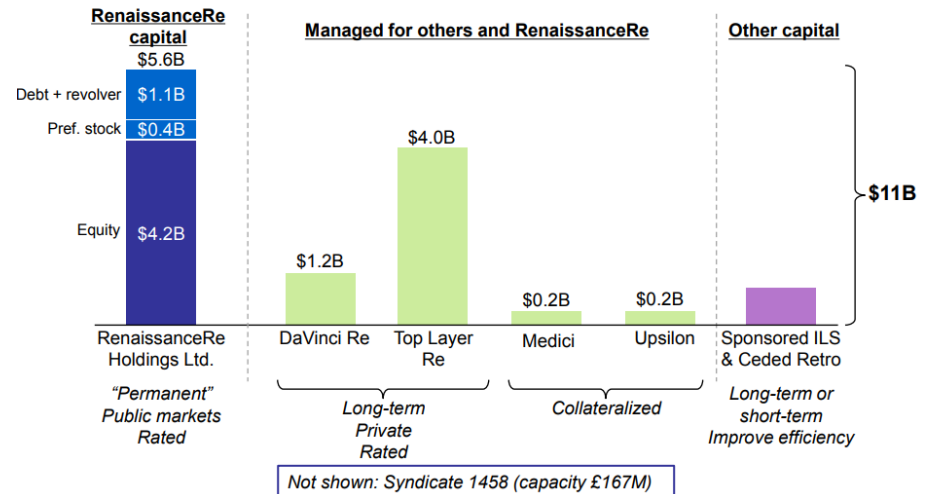


# Example: Renaissance Re capital management



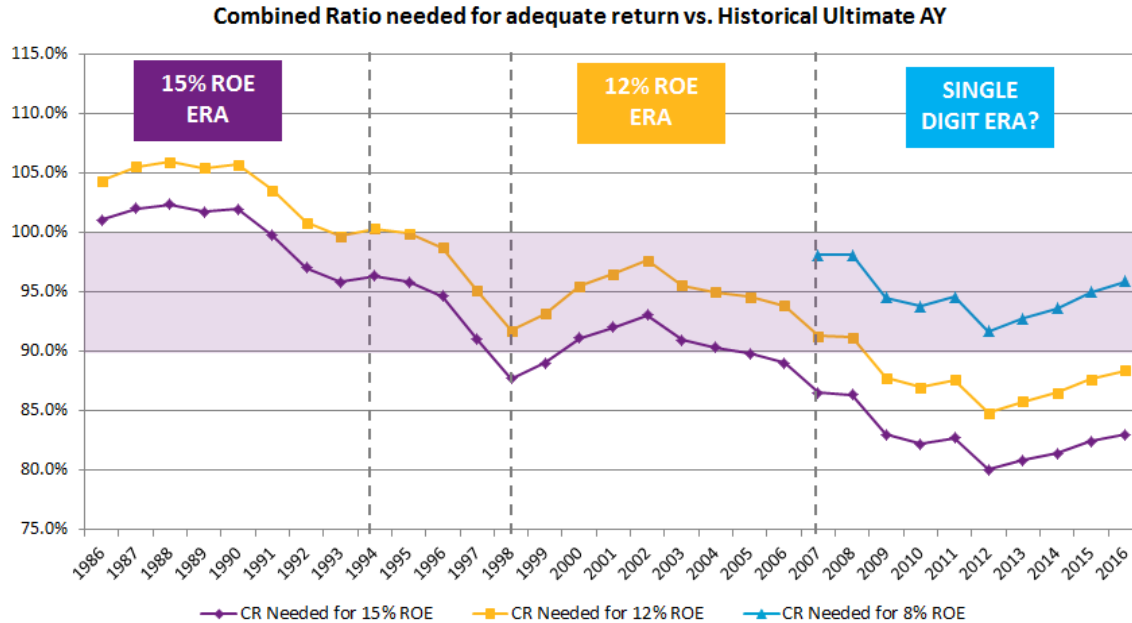
Build flexible platform *RenaissanceRe*

### Flexible model to match risk with efficient capital





## A new paradigm for reinsurers



- With a lower cost of capital, are single digit ROEs sufficient for investors?



## Summary

- Capital used to be scarce – not so much anymore
  - Clients will continue to seek value in other attributes
    - underwriting skill, product knowledge, distribution, claims, etc.
- ILS has become a meaningful part of the industry and is likely to remain so into the future
- Reinsurers have been forced to operate much more efficiently

*... a new paradigm for reinsurers*