Reinsurance and Other Forms of Risk Transfer

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Agenda

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1. Why reinsurance?
2. Reinsurance from a regulator´s point of view
   a) Capital Effects
   b) Risk Transfer
3. Alternative Risk Transfer

Catastrophes and Large Single Risks

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Source: Nile International, Daily Telegraph

New risks and growth support

Source: Munich Re

Reinsurance Classes

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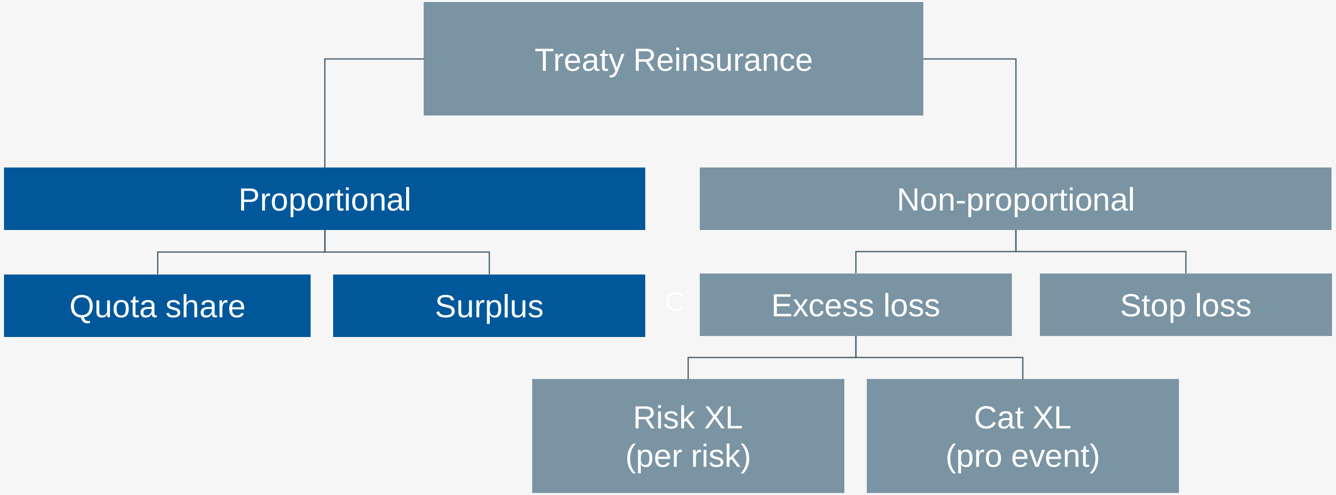

The size of the risk is steering reinsurance

The size of the loss is steering reinsurance

Source: Munich Re

Formula approach vs. risk approach

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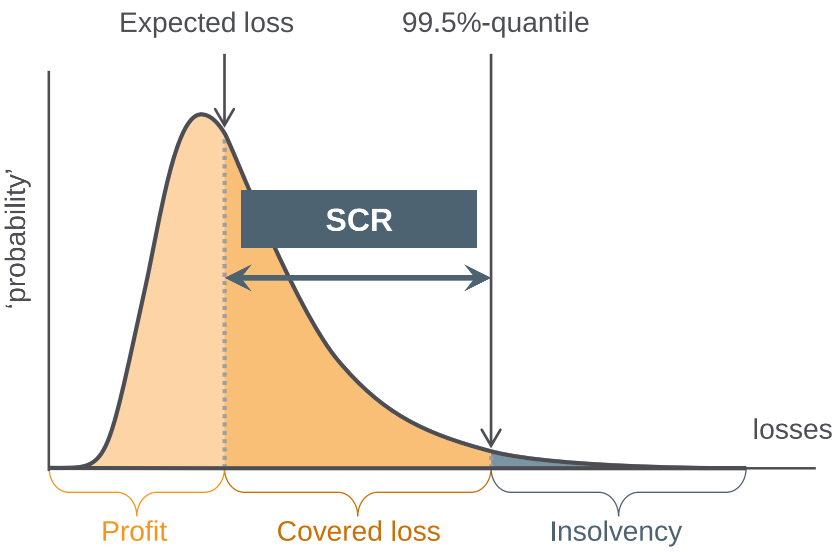
Formula-based Capital Requirement

x% of last 12 months´ net premiums

y% of last 36 months´ net losses

Risk-based Capital Requirement



Source: Munich Re

Example: Solvency II

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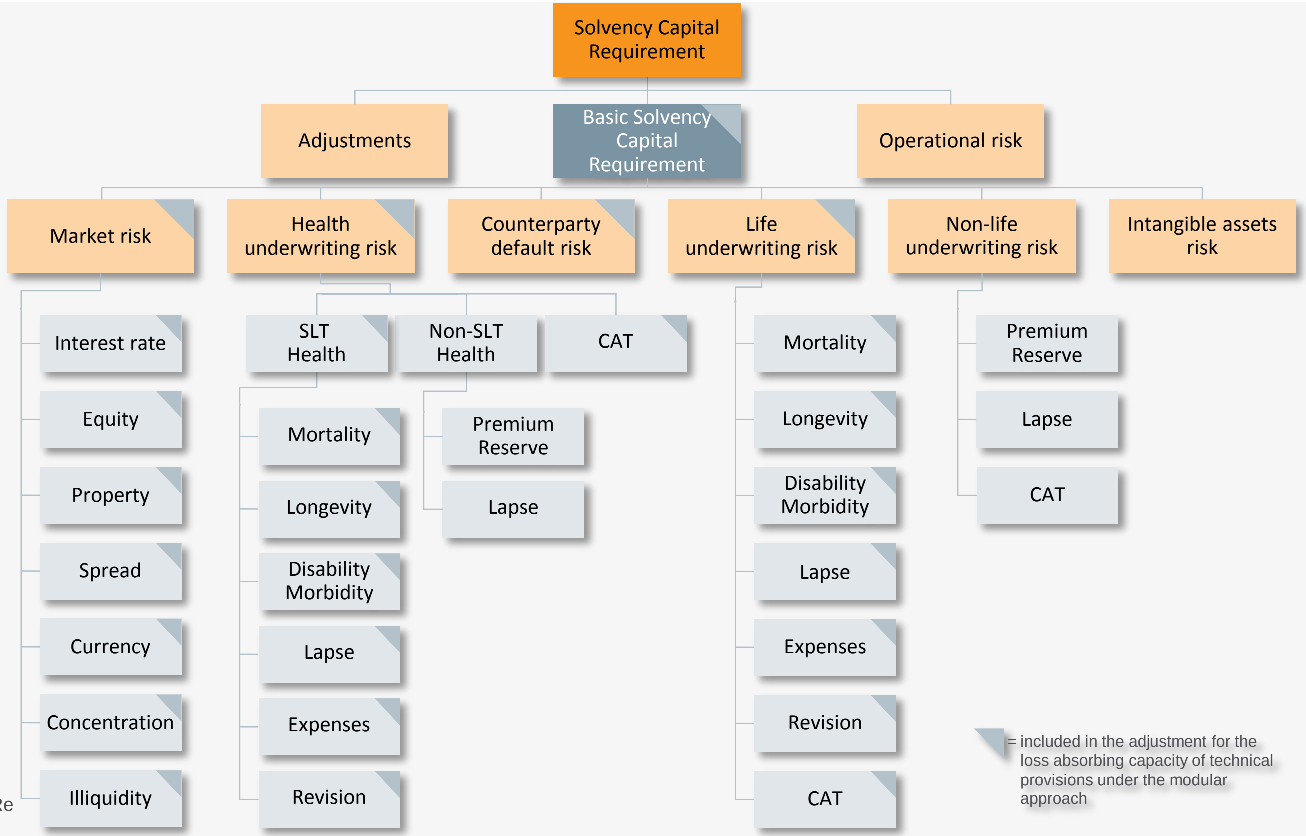

Source: Munich Re

Munich Re`s approach

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European Reinsurance Directive 2005/68/EC Article 2 para. 1(q) **European Solvency 2 Directive 2009/138/EC Article 210 para. 3** **Versicherungsaufsichtsgesetz* §167 para. (1)**	General definition of finite reinsurance
European Reinsurance Directive 2005/68/EC Article 45 **European Solvency 2 Directive 2009/138/EC Article 210, para. 1**	Member states mandate to release further guidance
Versicherungsaufsichtsgesetz* §167 para. (2) and §170 **Finanzrückversicherungs-verordnung****	Additional guidance published by German Federal Ministry of Finance Step 1: Undertakings shall implement additional criteria and processes for FinRe classification Step 2: For risk transfer assessment the Expected Reinsurer's Deficit should be calculated

* Act on the Supervision of Insurance Undertakings (VAG)
** Finite Reinsurance Ordinance (FinRVV)

Source: Munich Re

Definition

"'finite reinsurance' means reinsurance under which the explicit maximum loss potential, expressed as the maximum economic risk transferred, arising both from a significant underwriting risk and timing risk transfer, exceeds the premium over the lifetime of the contract by a limited but significant amount, together with at least one of the following two features:

(i) explicit and material consideration of the time value of money,

(ii) contractual provisions to moderate the balance of economic experience between the parties over time to achieve the target risk transfer."

Munich Re`s approach

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To classify a treaty as Traditional Reinsurance or as Financial Reinsurance we need a full understanding of…

… the main intention of the contract and economically linked contracts…

Questions are e.g.

- Does the treaty serve to circumvent any local regulatory, accounting or tax guidance?
- Is the contract economically linked to others? Does it e.g. serve to counterbalance bad results of another contract?

… all structural elements and treaty features of the contract(s) and…

Questions are e.g.

- Are there any loss- or result dependent conditions?
- Does the contract contain provisions that adjust premiums or limits?

… the effect of these elements and features on the risk transfer.

Question

- How much is the economic risk transfer limited by these contract features?

All facts and circumstances are taken into consideration.

- FinRe classification approach is principle-based and assesses all facts and circumstances holistically
- A quantitative assessment only is not sufficient. A qualitative analysis has to be done as well.

Source: Munich Re

Munich Re`s approach

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Note 1

If the contract is classified as FinRe, additional quantitative tests are mandatory by German regulations: The so-called ERD-test is performed to assess if the contract can be accounted

- as (re-) insurance (i.e. still sufficient risk is transferred)
- or not (i.e. risk transfer is not sufficient) → deposit accounting

Note 2

The assessment and the classification done by Munich Re is by no means an indicator on how an insurance authority, auditors or other (re-)insurers would classify such a contract.

Source: Munich Re

Common Types

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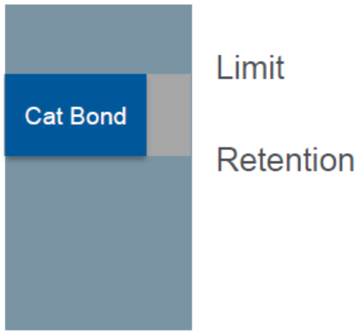
Securitized insurance risk mainly appears in two different transaction types:

Cat Bond

Reinsurance Program



Excess-of-Loss (XL) Risk Transfer

Sidecar

Reinsurance Program

Quota Share (QS) Risk Transfer

Source: Munich Re

How a Cat Bond works

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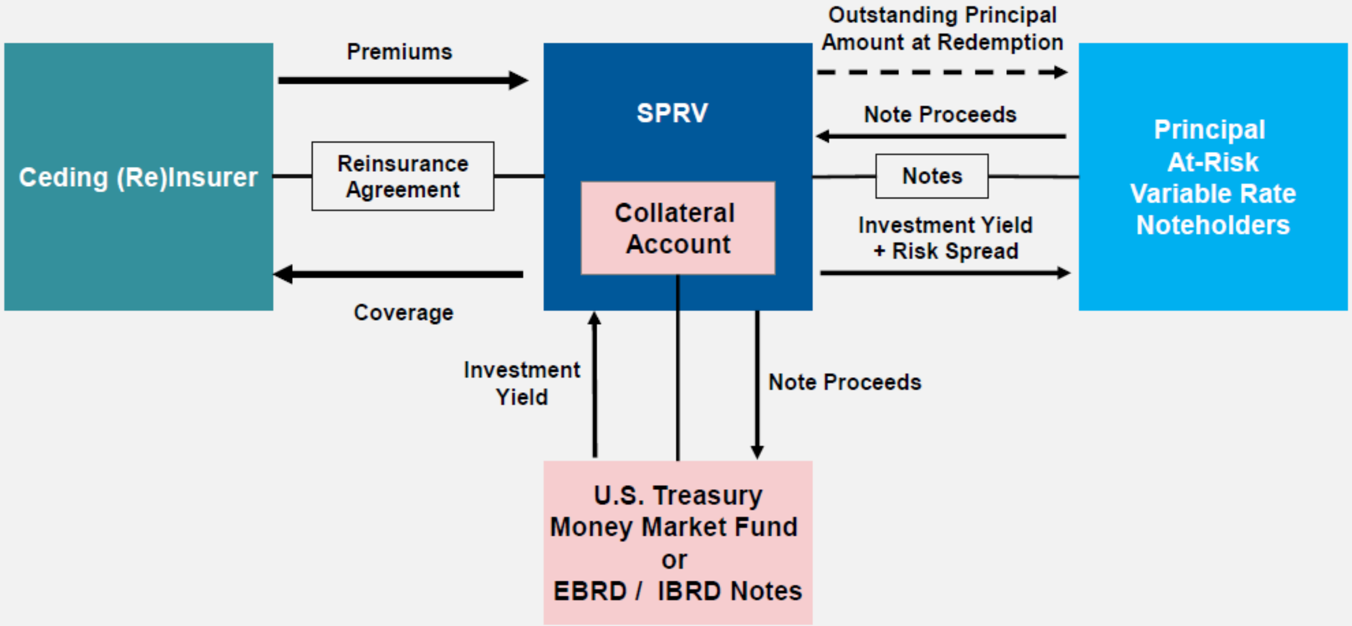

Source: Munich Re

Characteristics

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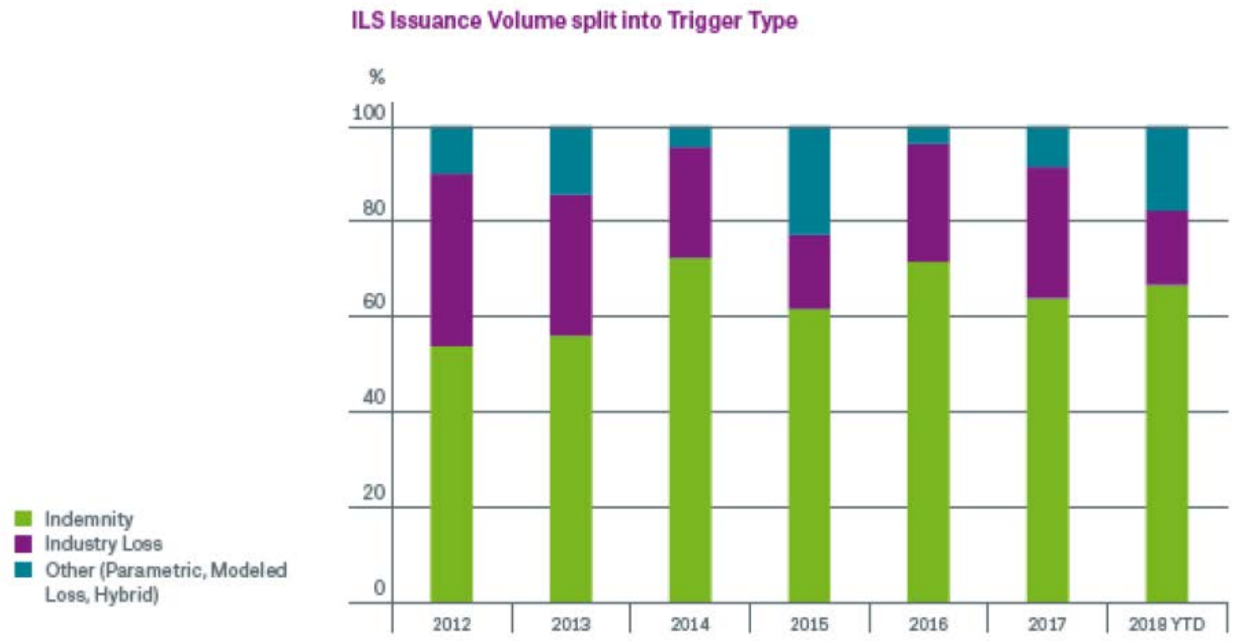
	Indemnity	Industry loss (pure or weighted)	Modelled loss	Parametric (pure or weighted)
Description	Ultimate net loss of the sponsor	Industry loss estimate (e.g. by PCS)	Simulated loss in a reference portfolio	Function of an objective data (e.g. wind speed, ground acceleration)

Source: Munich Re

Trigger Types



Source: Munich Re

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Any questions?

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