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Association of Bermuda Insurers and Reinsurers

*Private Reinsurers:
Meeting Florida's Catastrophe
Market Needs*

CAS Conference, June 2007



Association of Bermuda Insurers & Reinsurers

Association of Bermuda Insurers and Reinsurers

- **23 Class 4 Companies**
- **Highly capitalized, distinct regulation**
- **Headquarters in Bermuda with operations in Bermuda, the US and Europe**
- **Worldwide business enterprises**
- **1,500 employees Bermuda; 17,000 worldwide**

World Wide Rankings

- **Standard and Poor's reinsurer rankings:**
 - **Bermuda 13 of the top 40**
 - **More than either Europe or the US**
- **Benfield top 20 P/C Reinsurers**
 - **Bermuda 7 of the top 20**
 - **Tied with Europe for 7 of the top 20**

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2005 Data, 2006 S & P Report

Bermuda Market Impact

- **Largest property cat reinsurance market**
 - **Supplies 40% of the US market**
 - **Supplies 50% of FL capacity**
- **25% of Lloyds capacity**
- **Important in large commercial risk market**
- **Diversifying reinsurance market**
- **Global players**

*Market Diversification**

- **AM Best, top 10 groups 72% of market**
- **Bermuda carriers are now 15 of the top 35, with two in the top 10**
- **Growth of Bermuda leads to market diversification**
- **Good for the cedents**
- **Bermuda carriers lead to market choice, less concentration**

*AM Best Reinsurance Report, August 06

Private Reinsurance Market Works

- **After shock loss, raise capital**
- **After two horrific years, reinsurers stepped up with ADDITIONAL capacity**
- **Capital markets committed to providing capacity**
- **Capital attracted by rising prices**
- **Markets forgiving of shock losses**
- **New products created**
- **Temporary capital available to meet supply/demand imbalance**

Non-US Capital Raising

- **Post Katrina:***
 - **\$32 billion in capital raised**
 - **\$21 billion of that to Bermuda**
 - **\$10 billion to Bermuda start ups**
 - **\$5-6 billion in “side cars”**
 - **\$5 billion in cat bonds**

* Dowling and Partners; Lehman Brothers; Renaissance Re, Benfield, RAA, 2006/2007 Reports

Cat Bond issuance and Side Car creation continues

Cat Bonds and more . . .

- **\$10 billion in Cat Bonds over last decade, many of them still providing protection**
- **\$5 billion issued 2006**
- **That's double the number issued in 2005**
- **Additional ILW market**
- **Derivatives trading begins . . . again**

Enough About Supply . . .

- **2006 demand increase ENORMOUS:**
 - Rating agency, new scenario tests, more capital to support same amount of business
 - Two years of adverse loss experience
 - Cycles -- different frequency assumptions
 - Cat modeling changes, RMS reports 1/250 year event test increased \$55 billion
 - Capital to support that amount \$82 billion

So what is Capacity?

- **World Insurance Forum survey (2005)**
- **Reinsurance broker commentary 2007**
- **Reinsurance + securitizations + ILW's by non insurers like hedge funds + other**
- **Industry retentions: personal lines and commercial lines**
- **\$50-\$60 billion private sector reinsurance capacity attaching to large US event (on top of retentions)**

Florida is Unique

- **50% of most expensive hurricanes (demographic adjustments) have hit FL**
- **40% of major hurricanes (category) have hit FL**
- **40% of worst hurricanes (intensity) have hit FL**
- **Dade and Broward counties overdue for landfall, major hurricane**
- **\$2 trillion in insured property values**
- **Florida has a hurricane risk problem**

2007 Broker/Carrier Reports

- **Reaching market equilibrium**
- **Post KRW adjustment complete**
- **Cat reinsurance prices fall 10 to 15%**
- **Capacity increased by up to 25%**
- **Slight excess of capacity for Florida**
- **Capacity “healthy”**
- **Shortfalls not expected**

Florida Changes

- **More buying higher limits excess of Cat Fund than before**
- **Buyers looking for subsequent event covers**
- **More interest in commercial coverage**
- **Some interest in credit protection coverage for Cat Fund default**
- **Exploring multiple year covers**

Florida Cat Fund Expansion

- **Fundamental problem: PRICE CONTROLS.**
- **Cat Fund has been used as a tool for rate suppression since inception.**
- **Voted against a “risk charge”, original Advisory Committee meeting, insurers supported; public officials opposed**
- **As a tool for rate suppression, the Cat Fund distorts the market, it provides subsidized reinsurance**

Cat Fund Commentary

- **But Florida fund is here to stay-- How can it be used correctly?**
- **Provide coverage when market shortfalls exist at market prices**
- **Original January bill composed of:**
 - **Temporary expansion**
 - **Optional coverage below retention sold at market rates**
 - **Optional coverage above 06 limits sold at market rates**

Optional Coverage

- **Purely optional coverage sold at market rates legitimately addressed the 2006 concerns**
- **That was consistent with past expansion which had been modest**
- **Enacted law, sells the \$12 billion excess layer at 2-3% rate on line, below the 15 to 20% rate on line originally provided**
- **This change was made to deliver on a promise of rate reductions to consumers**

Temporary Coverage?

- Transition . . .
- **When the optional coverage layers are intended to sunset in three years, how do you deal with rate shock?**
- **Since the coverage was sold at below market prices, how do you transition back to a private market without increasing consumer costs?**
- **The temporary program is most likely a permanent program**

Making Consumers Happy

- **Will the new law do the trick?**

Tillinghast Study for AIF

- **Post event bond issues could range up to \$50 B for major 07 hurricane**
- **Per household assessments could range from \$1,700 for moderate storm to \$14,000 for major storm, spread over 10-30 years**
- **These assessments compare with average premium savings in 07 of \$265 per household**
- **Even a series of smaller storms leads to assessments that exceed savings**

Tillinghast, Who Benefits?

- **Effect of law is to have lower risk areas of state subsidize higher risk areas of the state**
- **Statewide, assessments exceed by factor of 10 the average savings**
- **Tallahassee cost is 100 times average savings**
- **Orlando cost is 69 times average savings**
- **Tampa cost is 23 times average savings**
- **Miami cost is 3 times average savings**

Milliman Study for PCI

- **Legislation did not materially increase FHCF capacity**
- **Sped up utilization of that capacity**
- **Prior law would cover four seasons at about \$16 B per season**
- **New law would cover two seasons at \$28 B per season**
- **Two back to back seasons likely to exhaust capacity**

Milliman continued . . .

- **Bond issuance may test capital markets appetite**
- **Largest municipal bond issues ever, \$26 billion for a 1/25 storm**
- **AM Best increased the risk charge for FHCF recoveries**
- **Policyholders in future years will pay higher premiums to pay for bond debt**
- **Transfers cost of claims from those in high risk areas to those in less risky areas**
- **Transfers cost of claims from property policyholders to car owners and commercial entities**

Cat Fund Not Sustainable

- **Public support for the Cat Fund will be impaired post event once charges are imposed**
- **Dramatic expansion of the Cat Fund with mandatory purchase at below market rates imperils the Cat Fund's finances**
- **It is not sustainable**
- **Proponents admit that, take the gamble**

Federal Bailout

- **Ticking time bomb waiting for a federal bailout**
- **Is that politically possible?**
- **It's a gamble**
- **Most likely type of federal bailout:**
 - **A LOAN**
 - **Floridians don't escape the cost of paying the debt**

Florida policy makers

- **What can you do?**
 - **Provide insurers with rating freedom – prices must be based on hurricane risk!**
 - **Stop creating political risk**
 - **Continue to promote and fund loss reduction measures**
 - **Control land use**
 - **Assist targeted consumers with financial aid to pay risk based premiums**

Consumer Subsidies

- **Current rate suppression via price controls distorts the insurance market, drives away private capital**
- **Florida will be served by thinly capitalized single state carriers as national writers continue to shrink**
- **Better approach, eliminate price controls, attract private capital and subsidize the cost of insurance directly to targeted home owners**

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