REINSURANCE COUNTERPARTY CREDIT RISKS

MARK FLOWER
On behalf of the working party

RCCR

Agenda:

- Who, why, what, where?
- What did we do?
- Other avenues?
- Wiki

Who?

The working party:

- Mohamed Afify
- Ian Cook
- Mark Flower
- Visesh Gosrani
- Gillian James
- Pantelis Koulovasilopoulos
- Jason Lincoln
- David Maneval
- James Robinson
Why should I care?

RCCR can significantly impact a cedant’s:

- P&L
- Cash flow
- Balance sheet
- Capital
- Credit rating

Some quick revision…

Common practice driven by reserving methods:

- ‘Bad debt paper’
- Based on rating agency default factor tables
- Notional x Factor = Provision
- (Most of) these tables are for corporate bonds

What to consider?

Issues with this common practice when moving towards prospective ICAs etc:

- 007 is not a reinsurer
- Rear view only
- Accumulations, causations, correlations
- Temporal / cyclical impacts
- RCCR impacts more than reserving
Where should it impact my thinking?

RCCR should feature in your:

- Reinsurance purchasing
- Reserving
- Capital modelling
- Risk management
- Contingency planning

What have we done?

Three things:

- Paper
- Model
- Workshop

Our paper

RCCR – Practical suggestions for pricing, reserving and capital modelling:

- Issues with current approaches
- Explored wider fields, proposed new approach
- Illustrative model and worked example
- Causation and correlation
- Commercial considerations, latest developments
The ‘banking’ approach

Common approach at core of credit models:
- Default intensity curve (market consistent)
- Theory is intuitive
- RCCR application is challenging

Default intensity curve (bps)

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Our ‘banking inspired’ model
- Cash flow simulation
- Defaults based on intensity curves
- Intensity curves imputed from investment data
- Models impact of market shocks and cycle
- Very straightforward
Our ‘banking inspired’ model

Addresses several issues:

- Key dynamics captured
- Prospective assumptions used
- Fits an ERM framework

Useful perspective and thought process

Our workshop (D8)

We’ll be looking at the model in more detail:

- Framework
- Practical application
- Hurdles
- Benefits
- Comparison

Other avenues to explore?

- Other investment data?
- Predictive power of equities?
- D&O and Credit underwriting?
- ‘High risk debt’ analysis by Arium?
- Best’s impairment rate & rating transition study?
And finally…

Google shared documents:

- Worked well initially, but…
- Struggled with lengthy papers
- Forget spreadsheets
- Ghosts in the machine!
- Has its uses but also limitations