Global Reinsurance

A Rating Agency Perspective

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FitchRatings
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Key Issues

Sector Outlook Negative, Rating Outlook Stable

Profit deterioration
1. Quality of earnings expected to deteriorate as underwriting margins and investment returns continue to fall
2. Smaller companies with limited diversification are at greatest risk of negative rating action

Pricing
1. Pricing conditions to remain challenging during 2017
2. Surplus of reinsurance capacity will create further downward pressure on premium prices
3. Slowing rate of price reductions will have limited significance in improving near-term profitability

Alternative capital
1. Growth of alternative reinsurance market has slowed
2. If this trend continues, it could signify reduced appetite for reinsurance risk

M&A
1. Consolidation among reinsurers has waned as companies digest recent deals
2. M&A likely to resume in the near term as companies consider strategic options to combat market stress
## 2017/2016 Projections

<table>
<thead>
<tr>
<th></th>
<th>2017 forecast</th>
<th>2016 forecast</th>
<th>2015 actual</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Net premiums written</strong></td>
<td>102,060</td>
<td>101,050</td>
<td>99,067</td>
</tr>
<tr>
<td><strong>Catastrophe losses</strong></td>
<td>10,135</td>
<td>7,065</td>
<td>2,500</td>
</tr>
<tr>
<td><strong>Net favourable prior year reserve development</strong></td>
<td>2,990</td>
<td>3,945</td>
<td>4,833</td>
</tr>
<tr>
<td><strong>Calendar year combined ratio (%)</strong></td>
<td>99.2</td>
<td>94.2</td>
<td>86.8</td>
</tr>
<tr>
<td><strong>Accident year combined ratio (%)</strong></td>
<td>102.2</td>
<td>98.2</td>
<td>91.8</td>
</tr>
<tr>
<td><strong>Accident year combined ratio ex catastrophes (%)</strong></td>
<td>92.0</td>
<td>91.1</td>
<td>89.2</td>
</tr>
<tr>
<td><strong>Shareholders’ equity (excluding Berkshire)</strong></td>
<td>271,500</td>
<td>268,810</td>
<td>266,146</td>
</tr>
<tr>
<td><strong>Net income ROE</strong></td>
<td>8.0</td>
<td>8.5</td>
<td>9.8</td>
</tr>
</tbody>
</table>

Source: Fitch monitored universe of reinsurers
# Natural Catastrophe Events, 1H16

<table>
<thead>
<tr>
<th>Date</th>
<th>Event</th>
<th>Location</th>
<th>Economic Loss (USDbn)</th>
<th>Insured Loss (USDbn)</th>
</tr>
</thead>
<tbody>
<tr>
<td>April</td>
<td>Earthquakes</td>
<td>Japan</td>
<td>22-48</td>
<td>5.6</td>
</tr>
<tr>
<td>April</td>
<td>Storm/hail</td>
<td>US</td>
<td>3.5</td>
<td>3.1</td>
</tr>
<tr>
<td>May/June</td>
<td>Storms/floods</td>
<td>Europe</td>
<td>4.0</td>
<td>2.8</td>
</tr>
<tr>
<td>April</td>
<td>Storms</td>
<td>US</td>
<td>3.5</td>
<td>2.7</td>
</tr>
<tr>
<td>May</td>
<td>Wildfires</td>
<td>Canada</td>
<td>3.6</td>
<td>2.5</td>
</tr>
<tr>
<td>March</td>
<td>Storms/hail</td>
<td>US</td>
<td>2.0</td>
<td>1.5</td>
</tr>
<tr>
<td><strong>1H16 total</strong></td>
<td></td>
<td></td>
<td><strong>68.0</strong></td>
<td><strong>28.0</strong></td>
</tr>
<tr>
<td><strong>1H15 total</strong></td>
<td></td>
<td></td>
<td><strong>46.0</strong></td>
<td><strong>16.0</strong></td>
</tr>
<tr>
<td>10-year avg. 1H</td>
<td></td>
<td></td>
<td><strong>102.0</strong></td>
<td><strong>26.0</strong></td>
</tr>
<tr>
<td>30-year avg. 1H</td>
<td></td>
<td></td>
<td><strong>63.0</strong></td>
<td><strong>15.0</strong></td>
</tr>
</tbody>
</table>

Source: Swiss Re – except 30-year average 1H, which is attributed to Munich Re NatCatService
Reported vs. Normalised Combined Ratio: 2011-2015 Average

Major European Reinsurers
Reported vs. normalised combined ratio

(|%|)

2011 | 2012 | 2013 | 2014 | 2015 |
---|---|---|---|---|
106.0 | 90.4 | 91.1 | 90.6 | 90.3 |

Note: Average for Hannover Re, Munich Re, SCOR and Swiss Re
Source: Company reports, Fitch

Major European Reinsurance
Reported vs. Fitch normalised combined ratio

- Swiss Re reported (LHS)
- Munich Re reported (LHS)
- SCOR reported (LHS)
- Swiss Re normalised (RHS)
- Munich Re normalised (RHS)
- SCOR normalised (RHS)

Note: Reserve and natural catastrophe budgets vary annually for each company, figures rounded
Source: Company reports, Fitch
Reported vs. Normalised Combined Ratio: 2015 Bridge

<table>
<thead>
<tr>
<th>Year</th>
<th>Swiss Re</th>
<th>Munich Re</th>
<th>Hannover Re</th>
<th>SCOR</th>
</tr>
</thead>
<tbody>
<tr>
<td>2015</td>
<td>86.0</td>
<td>89.7</td>
<td>94.4</td>
<td>91.1</td>
</tr>
<tr>
<td>Nat cat from expected</td>
<td>5.1</td>
<td>5.8</td>
<td>1.4</td>
<td>4.8</td>
</tr>
<tr>
<td>Prior-year</td>
<td>99.8</td>
<td>98.7</td>
<td>99.7</td>
<td>95.9</td>
</tr>
<tr>
<td>Normalised</td>
<td>8.7</td>
<td>3.2</td>
<td>3.9</td>
<td></td>
</tr>
</tbody>
</table>

Source: Fitch
Bermuda (Re)insurers Financial Performance

Source: SNL Financial, company reports
Bermuda vs. North American (Re)insurers

Bermuda ROE Advantage Shrinking

Source: SNL Financial, company reports
Bermuda vs. North American (Re)insurers (Cont.)

CY Combined Ratios Converging

Source: SNL Financial, company reports
Reinsurance Renewal Pricing Trends

**Property** (2016)

- No loss
- Loss hit
- Cat no loss
- Cat loss hit
- US cat no loss

-30 -20 -10 0 10 20 30 (%)

**Casualty** (2016)

- XL no loss
- XL loss hit
- US motor (L)
- US motor (NL)
- US general TPL

-30 -20 -10 0 10 20 30 (%)

Source: Company and broker reports
Portfolio Price Movements: Major European

Overall Portfolio Price Movements
Softening trend continues but viewed as manageable

Source: Company disclosure
Alternative Market Capacity Growth Slows

Alternative capacity as a % of global property catastrophe reinsurance limit

Source: Guy Carpenter Estimates
Catastrophe Bond Issuance

Issuance Slipping
Catastrophe Bonds (Non-Life)

(USDbn)

Source: Willis Capital Markets & Advisory
Tough sledding ahead

- What goes up, must come down – significant maturities coming due ($7 B in 2017)
- Unless there is a paradigm shift, we believe not much more growth

Title

Source: ???
Basic Hurdles Still Exist for Cat Bonds – though changes are in the air

- Niche market
- Expensive to structure
- Lack of robust secondary market
- Seasonality
- Peak perils
- Lack of standardization
- Private placements

Outstanding Perils

Source: Willis Capital Markets (June, 2016)
Will Investors Leave When Claims Happen?
— doesn’t seem so based on past events

Par Outstanding

Source: Fitch
Evolution of Reinsurers’ Market Position

**Medium**
- XL
- Fairfax
- Everest
- Partner Re
- Alleghany
- Arch Capital
- Axis
- Aspen
- Validus
- Endurance
- RenaissanceRe

**Small**
- Ace
- W.R. Berkley
- Markel
- Allied World
- Sirius

Legend:
- Blue: Non-Life Reinsurance
- Green: Life Reinsurance
- Light Blue: Primary
Major European Reinsurers’ Solvency

Strong Level of Coverage

- **Munich Re**: 302%
- **Hannover Re**: 221%
- **SCOR**: 211%
- **Swiss Re**: 312%

The green portion represents the target range.

*223% represents coverage under Swiss Solvency Test, the regime that Swiss Re operates under.*

Source: Fitch
Equivalence

- Three elements separately assessed to determine whether equivalent
  - Reinsurance supervision
  - Solvency assessment
  - Group supervision

- Types of equivalence
  - Full (unlimited), temporary (end-2020, extendable by one year) and provisional (10 years, renewable for 10 year period)

- Third country effects
  - Non-EEA reinsurers when involved in EEA reinsurer contracts
  - Non-EEA subsidiaries of EEA (re)insurers
  - Non-EEA (re)insurers with EEA subsidiaries without EEA sub-group with EEA parent
Global Progress for Equivalence

Bermuda and Switzerland

- Full equivalence
- Provisional
  - Solvency assessment only

- Excludes captives and SPVs
- Reinsurance supervision granted temporary equivalence for 5 years

Source: Fitch

a Excludes captives and SPVs
b Reinsurance supervision granted temporary equivalence for 5 years

Source: Fitch
“..it would be unacceptable to us if firms were to use this market (reinsurance) primarily as a tool to achieve regulatory arbitrage..”

(Andrew Bulley, Prudential Regulation Authority 28 April 2016)
Longevity Continues to Develop GWP

Hannover Re

(SCOR)

Munich Re

Source: Fitch
What Could Lead to a Negative Rating Outlook?

1. Deterioration in sector profitability, even if capital remains strong
   - Run-rate combined ratio stay closer to 100% (2017 forecast is 99.2%)
   - Return on equity dropped below 10% (2017: 8.0%)

What has changed since sensitivities were first assigned?
   - Since first assigning these sensitivities in September 2014, interest rates and the risk profile of many reinsurers have reduced

Where are Negative rating actions most likely?
   - Individual negative rating actions are possible if a raised combined ratio or sub-10% ROE indicated a significant impairment in a company’s financial condition

2. Catastrophic loss with interest rate spike
   - Catastrophic loss in excess of USD70bn coupled with a sudden spike in interest rates of 300bps or more
Related Research

Fitch research can be accessed via our website [www.fitchratings.com](http://www.fitchratings.com)

1. Global Reinsurance Guide 2017 (September 2016)

2. 2017 Outlook: Global Reinsurance (September 2016)


4. Insurance Peer Review: Major European Reinsurers (August 2016)

5. Global Reinsurers’ Mid-Year 2016 Financial Results (August 2016)

6. Asian Reinsurance Markets (August 2016)

7. Latin American Reinsurance (August 2016)

8. Reinsurance in a Solvency II World (June 2016)
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