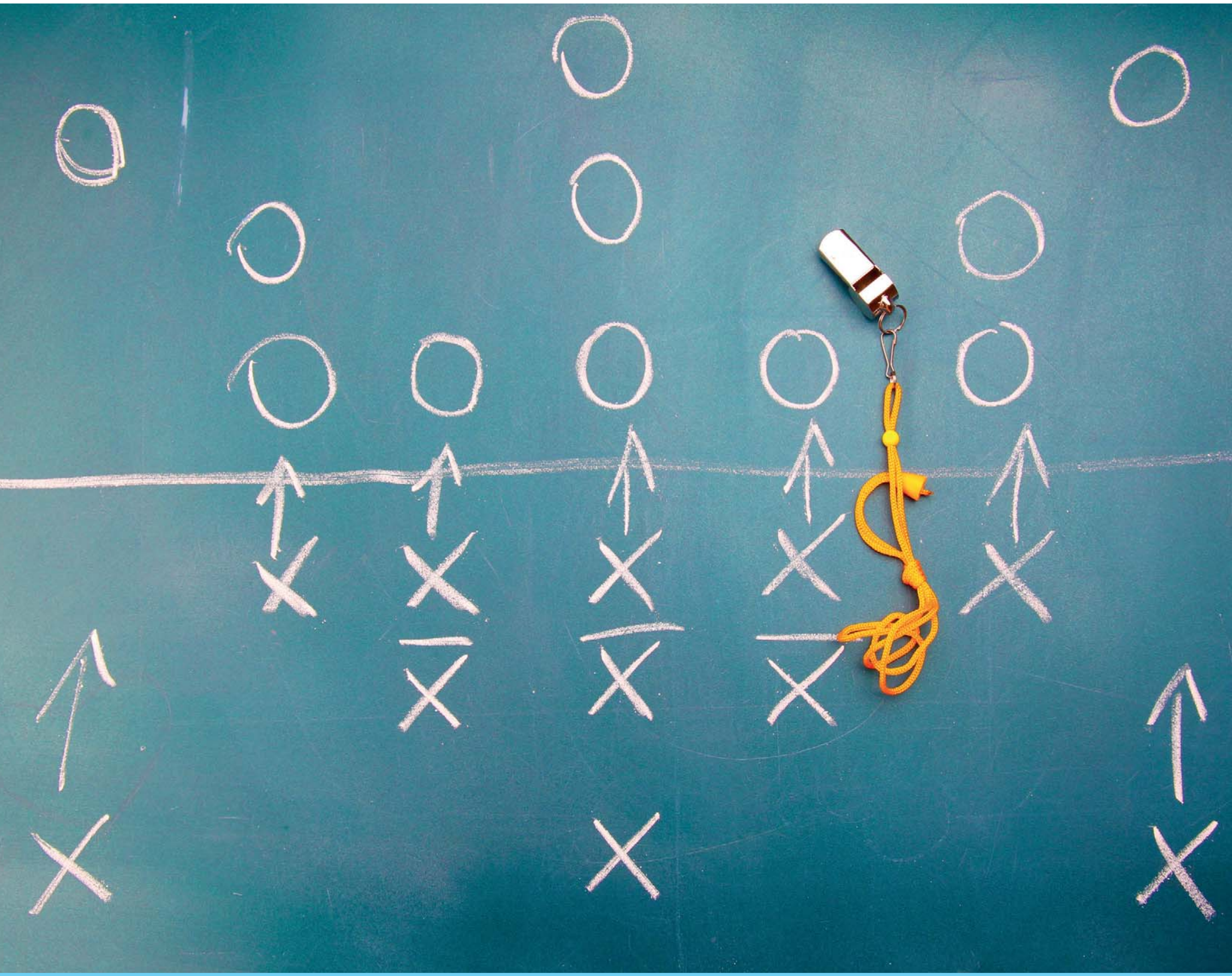
GLOBAL REINSURANCE HIGHLIGHTS 2015



Defense Provides Stability, But Pressure Remains

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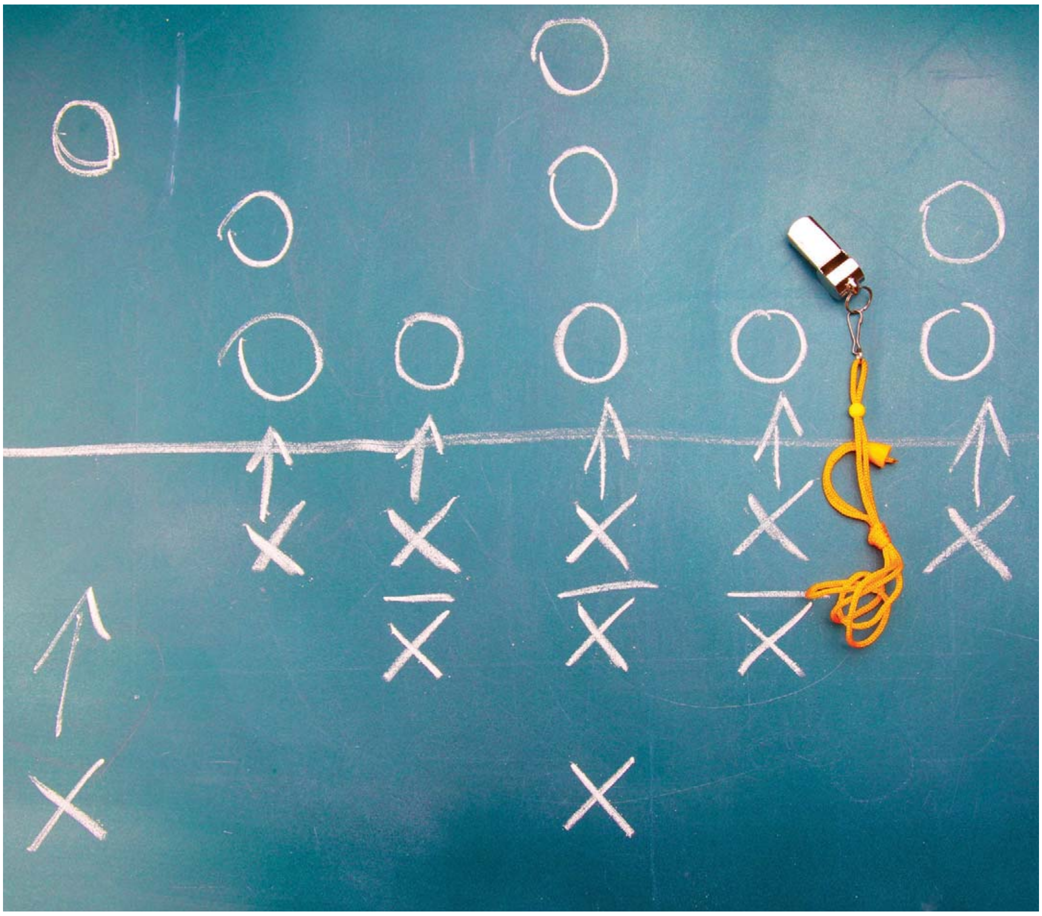
Global Reinsurance Highlights

2015 Edition



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Global Reinsurance Highlights

2015 Edition

Defense Provides Stability, But Pressure Remains

Dennis Sugrue

Legendary University of Alabama football coach Bear Bryant famously said "Defense wins championships". While there is no annual competition for the champion of global reinsurance, it is fair to say that defense is at the forefront of many management teams' minds, especially given that competitive pressures are squeezing reinsurers' business models. The defensive strategies employed over the last 12 months appear to be doing the trick, for now. Make no mistake, though, credit conditions in the global reinsurance market remain negative as double-digit declines in pricing persist in many lines and regions around the world, investment yields remain anemic in this lower-for-longer reality, and both traditional and alternative capital continues to flood the capacity supply. But reinsurers have built on the industry's recent successes—robust capital and strong risk management—to take defensive actions to insulate themselves from these market pressures in the hopes of riding out the cycle for better times.

In our lead article *"Defensive Plays Help Global Reinsurers To Maintain Resilience As Credit Conditions Remain Negative,"* we explore some of the defensive moves that management teams have taken, including portfolio steering, prudent risk selection, and in some cases consolidation, which have bought them some time to continue to play in the current market. And although credit conditions have not improved over the last 12 months, we believe that these protective actions have helped to bring about some stability to ratings in the sector.

The recent wave of M&A in the sector is a headline-grabbing defensive strategy, which we address in *"The Reinsurance Shark Tank—Only The Strong Will Survive"*. Here, we review the drivers for the deals in the reinsurance market, and how they impact the competitive landscape. Reinsurers are not the only ones in on the act either, so we look at how the consolidation in the primary and broker markets could increase competition among reinsurers.

"Lessons From Large U.S. Cedants In The Game Of Reinsurance Arbitrage" takes a look at empirical evidence that the largest U.S. cedants are centralizing their purchasing and buying less coverage despite lower reinsurance costs, exacerbating the price softening we've observed in recent years.

The boundaries between alternative and traditional capital continue to blur. In *"Are Alternative Capital And Reinsurance Two Sides Of The Same Coin?"* we explore how reinsurers are adapting to alternative capital by providing innovative solutions and lower prices to buyers to maintain market share. We continue to caution that any growth of the alternative market should not come at the expense of looser underwriting discipline and less due diligence.

The current buyers' market is pushing down the top line, while interest rates and therefore investment yields are likely to remain below historical levels for some time to come. *"For Reinsurers, An Ever Tougher Competitive Landscape Makes Profits Harder To Find"* demonstrates that underlying profitability has been declining for the last three years, and reinsurers are having to look deep into their playbooks in order to hold the line. Reserve releases have provided a shot in the arm for the industry over the last five years, but will they be sustainable? *"Property/Casualty Reinsurers With Strong Reserve Margins Are In A Better Position To Withstand The Prolonged Soft Market"* explains our view that reinsurers with aggressive reserving practices may not continue to support earnings with releases after a string of benign catastrophe loss years. Meanwhile, CFOs and CIOs may be tempted to take on a bit more asset risk to squeeze a bit more yield out of their conservative portfolios. We don't see widespread shifts to riskier assets, as *"Asset Risk For Reinsurers Nudges Higher As Low Yields Continue To Bite"* demonstrates. But we see some tweaks in certain players' asset portfolios to maximize yield. In our view, the sector remains well capitalized to absorb the additional risk assumed so far.

For the third year in a row, we have utilized survey information to examine trends in catastrophe risk exposure, the largest risk for the industry. We have identified a divergence in reinsurers' strategic reaction to the softening catastrophe market in *"Discipline Is Necessary As Reinsurers Adjust Their Exposure To Catastrophe Risk"*. While most reinsurers allowed their cat exposure to contract, a few took on more exposure this year. An increased focus on cat risk weakens a reinsurer's risk position by increasing potential volatility. Profitability in the sector is likely to become more vulnerable to natural catastrophes; therefore, we anticipate that operating performance could deteriorate further at reinsurers that are more exposed to cat risk.

Through our industry and country risk assessments for the reinsurance industry, we capture risks associated with operating in the reinsurance market. *"Insurance Industry And Country Risk Assessment On The Global Property/Casualty Reinsurance Sector Is 'Intermediate'"* explains that pricing declines and low yields are pressuring returns for non-life reinsurers, but they remain acceptable and there's no evidence of widespread increased risk-taking, yet. Barriers to entry are evolving, and market growth prospects are limited in the short term, although not enough to lead to a change in view. Meanwhile, *"Global Life Reinsurance Sector Carries A Low Insurance Industry And Country Risk Assessment"* illustrates some of the benefits for reinsurers with material life reinsurance books, namely the high barriers to entry, strong operating results, and long-term opportunities for growth as the industry supports the effort to fill the global protection gap in life insurance.

We believe that Global Reinsurance Highlights captures the key issues facing reinsurance management, investors, and other stakeholders. We hope that you will enjoy the 2015 edition and welcome your feedback on possible enhancements for future years.

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Sector Trends: Defensive Plays Help Global Reinsurers To Maintain Resilience As Credit Conditions Remain Negative

By Dennis Sugrue, Taoufik Gharib, David Laxton and Tracy Dolin

- Global reinsurers continue to face elevated competitive pressures and industry risk. We expect many to find it difficult to maintain strong profitability over the next 24 months.
- In response to these industry threats, reinsurers have taken steps to protect their balance sheets and market positions such as changing their business mix, buying more retro, and consolidating to improve scope or diversification.
- Extremely strong capital adequacy, robust risk management, and portfolio steering, combined with these defensive measures, mean that we see less than half of our ratings on reinsurers as being overexposed to market pressures.
- We expect to see only a few rating actions over the next 12 months.


Reinsurance M&A: The Reinsurance Shark Tank–Only The Strong Will Survive

By Taoufik Gharib and Dennis Sugrue

- Global reinsurers have seen the future, and it requires greater scale and diversification for them to remain relevant.
- We expect reinsurance M&A momentum to continue for the rest of 2015 and into 2016 as the remaining small and midsize reinsurers race to find consolidation partners.
- Investors have shown more interest in emulating the Berkshire Hathaway model, but the success of this strategy remains to be seen.
- The consolidation among reinsurance brokers and GMIs will have a direct effect on competition in the reinsurance market.




Cedants' View: Lessons From Large U.S. Cedants In The Game Of Reinsurance Arbitrage

By Tracy Dolin, Sridhar Manyem, Taoufik Gharib and Gary Martucci

- Empirical research findings point to a buyers' market for reinsurance.
- To remain relevant, traditional reinsurers have been behaving like insurance-linked securities players.
- Large cedants are balancing reinsurance optimization and top-line growth.
- The divide between tier 1 and tier 2 reinsurers is becoming more severe.


Cat Exposure: Discipline Is Necessary As Reinsurers Adjust Their Exposure To Catastrophe Risk

By Charles-Marie Delpuech and Miroslav Petkov

- Balance sheet exposure to catastrophe risk has contracted for most reinsurers, but a few are taking on more exposure this year.
- Reinsurance utilization at the 1-in-250-year return period has increased as reinsurers optimize their cost of capital and benefit from cheaper access to third-party capital.
- An increased focus on technical profitability means that reinsurers' operating performance is more sensitive to large catastrophe claims as evidence shows that cats are more likely to cause underwriting losses.
- According to our stress tests at the 1-in-250-year return period, the most exposed groups are London-based players, which show lower capital adequacy in our rating analysis, and some North American reinsurers that have a larger-than-average appetite for catastrophe risk.


Asset Allocations: Asset Risk For Reinsurers Nudges Higher As Low Yields Continue To Bite

By Anvar Gabidullin and Mark Button

- We've seen an increase in reinsurers' exposure to equities in the past 12 to 18 months, but it's still moderate and within risk tolerances.
- Exposure to credit risk has remained stable year-on-year, in aggregate, but we have seen some subgroups taking a bit more credit risk during the year.
- We believe that the reinsurers in our peer group can meet additional capital requirements arising from greater exposure to risk assets due to the continued strength of their capital positions.


ILS: Are Alternative Capital And Reinsurance Two Sides Of The Same Coin?

By Maren Josefs and Gary Martucci

- As capital has entered the reinsurance market, it has created opportunities for buyers.
- The covered perils are increasing and event definitions are becoming broader.
- We continue to caution that any growth of the alternative market should not come at the expense of looser underwriting discipline and less due diligence.


Reserve Review: Property/Casualty Reinsurers With Strong Reserve Margins Are In A Better Position To Withstand The Prolonged Soft Market

By Olivier Karusisi and Miroslav Petkov

- Reinsurers in the sector have found it difficult to increase prices since 2007, and some have released reserves in recent years to support reported profits.
- Claims, especially those related to catastrophes, have also been relatively low over the past two years, making it harder to justify raising rates.
- We expect a reduction of reserve releases attributable to natural catastrophe events, because there have been relatively few catastrophe claims in 2013 and 2014.


Peer Benchmarks: For Reinsurers, An Ever Tougher Competitive Landscape Makes Profits Harder To Find

By Charlotte Chausserie-Lapree and Dennis Sugrue

- Industry players are moving actively to counteract the pressures on their profitability.
- Despite strong headline earnings reports, our analysis finds performance has been deteriorating since 2012.
- The industry's adjusted combined ratio for 2014 of 96% was 5.5 points worse than the reported figure, and on the high end of our expected range.
- We have observed an overall improved capital redundancy as strong retained earnings led to TAC growth in 2014, despite an increase in capital returned to shareholders.

SOUNDBITES



P/C Reinsurance IICRA: Insurance Industry And Country Risk Assessment On The Global Property/Casualty Reinsurance Sector Is "Intermediate"

By Taoufik Gharib, Dennis Sugrue and Olga Ryabaya

- The trend toward greater scale highlights how hard it will be for management teams to defend their market positions.
- We expect continued low interest rates at least in 2015 to dampen the sector's investment returns, and thus its returns on equity.
- Because business and consumer confidence is a key factor in our forecast for the next two years, a 'Grexit' could easily weaken the upturn we are currently contemplating.
- Alternative capital is having the most acute impact in the U.S. property catastrophe market but is tip-toeing into the U.S. commercial property markets as well.


Life Reinsurance IICRA: Global Life Reinsurance Sector Carries A Low Insurance Industry And Country Risk Assessment

By Johannes Bender and Dennis Sugrue

- We expect the industry's profitability to remain favorable, and we estimate an industrywide average ROE of more than 10% for 2015–2017.
- Barriers to entry for the global life reinsurance sector are high. We assess regulatory barriers to entry as moderate and operational barriers as high.
- Long-term growth for the global life reinsurance industry can come from primary insurance markets in underpenetrated regions.

Defensive Plays Help Global Reinsurers To Maintain Resilience As Credit Conditions Remain Negative

SHUTTERSTOCK / OSTILL

By Dennis Sugrue, Taoufik Gharib, David Laxton and Tracy Dolin

Credit conditions for the global reinsurance sector remain negative—competition is fierce, alternative capital continues to grow, pricing is declining, earnings are under pressure, and consolidation has begun. Global reinsurers are searching their playbooks for options and strategies to cope with the myriad challenges. Standard & Poor's Ratings Services considers that the defensive actions they have already taken have helped to prove the industry's resilience. Therefore, although we expect companies' competitive positions, earnings, and capital bases to remain under pressure over the next 12 months, we anticipate few positive or negative rating actions.

No Relief In Sight As Business Risks Continue To Increase

The competitive landscape for reinsurers remains difficult and there appears to be little respite on the horizon. Certain risks are elevated as competitive pressures pile up and pricing declines, although the decline is slower than we previously expected. We are mindful of the temptation for reinsurers to take increased risks to maintain their profitability, though we don't see this as a widespread issue now. We also anticipate that growth prospects could weaken, while at the same time barriers to entry are shifting.

Management teams are digging deep into their respective playbooks to find defensive strategies to counter these pressures. Their actions appear to be working and the industry is demonstrating its resilience. We continue to view industry risk as intermediate (see "Insurance Industry And Country Risk Assessment On The Global Property/Casualty Reinsurance Sector Is 'Intermediate'"). But if we were to revise down our assessment, we expect fewer than one-half of rated reinsurers would see a rating change.

Pricing continues to decline across most lines of business and regions. Broker and industry reports demonstrate that pricing for many property/casualty (P/C) excess-of-loss lines around the world has declined by up to 20% (see Table 1). However, we see some signs that pricing is leveling off; rate declines in property-catastrophe lines were less severe than expected, at 5% to 10%. We saw declines of 15% to 25% in 2014.

Despite these rate reductions, reinsurers have indicated to us that, for the most part, prices are sufficient to allow them to meet their return targets. Our earnings expectations remain low compared with the sector's historically strong performance, but should enable most players to maintain capital levels in the current pricing environment.

In 2014, we highlighted a change in reinsurance buying habits at large cedants. Improved risk management and stronger balance sheets had enabled them to buy less reinsurance and purchase on a centralized basis. We believe that this has dampened growth prospects for the industry. The trend is filtering down beyond global carriers and now affects buying habits at some regional and national insurers, particularly in the U.S. and Europe.

Barriers to entry for reinsurance are changing and a divide is forming. While the use of alternative sources of capital breaks down barriers, the recent increase in mergers and acquisitions (M&A) raises them.

Aon has estimated that the influx of alternative capital at June 30, 2015, stood at $69 billion overall. This increases competition by making it easier for the industry to pair capacity with risk. Reinsurers in catastrophe lines of business, particularly in the U.S., have been most damaged by this influx. However, some alternative capital providers, such as hedge funds and some insurance-linked securitization (ILS) arrangers, are seeking a way to pair capital market capacity with noncatastrophe lines of business characterized by low severity but high frequency of losses, such as short-tailed casualty or motor.

The recent spate of consolidation is reducing the number of players and raising the price of admission for reinsurers. Given the increasing sophistication of reinsurers' clients, reinsurers must prove that they have the size, expertise, and reach to remain relevant.

We consider operational barriers to entry remain moderate, but continue to monitor these evolving dynamics.

The Best Offense Is A Strong Defense

In response to the competitive threats and industry changes mentioned above, reinsurers have undertaken defensive maneuvers over the past 12 months which have successfully insulated many from the renewed competitive pressures and bought them time.

M&A has proved a newsworthy, and popular, strategy

A growing list of companies has chosen to look for scope and diversification through mergers or acquisitions. We consider that this trend toward consolidation confirms the difficulties management teams face in the current soft market.

Combining forces offers companies potential for cost synergies, diversification of product offerings and risk exposure, and increased capacity. Several of the companies involved—Renaissance Re Holdings Ltd., Platinum Underwriters Holdings Ltd., Lancashire holdings Ltd., and Montpelier Re Holdings Ltd.—were mainly short-tail or catastrophe-focused companies and as such were most acutely exposed to the market's increased competitive pressures. By diversifying their scope and increasing their scale, these companies may have bought themselves some breathing space. We do not believe that the wave of consolidation is over, and expect to see more small and midsize reinsurers combine or be purchased.

Some firms are reallocating their business mix to reduce capital needs

Prices in excess-of-loss business, particularly catastrophe, have declined more sharply than those for proportional reinsurance or primary insurance business over the past two years. Our analysis of reinsurers' business mixes indicates that many are responding by increasing the amount of primary and proportional lines they write. As well as benefiting from more-resilient pricing, these lines are also typically less capital-intensive. This helps reinsurers to improve internal, regulatory, and rating agency capital adequacy measures.

On average, 61% of reinsurers' net premium written was proportional or primary business in 2014, up from 54% in 2013. Data from Aon indicates that during 2014, seven reinsurers in our peer group reduced the amount of reinsurance they wrote year-on-year and nine saw their primary insurance business outpace their reinsurance growth.

Reinsurers are employing a number of strategies. Swiss Reinsurance Co. Ltd. and SCOR SE have increased their focus on direct corporate and specialty insurance; Arch Capital Group Ltd. moved into the mortgage insurance arena; and other companies are looking for diversification through acquisition. Partner Re Ltd., for example, originally looked at merging with AXIS Capital Holdings Ltd. to balance its reinsurance business with some primary insurance, before eventually agreeing a sale to EXOR SpA.

Reinsurers have also taken advantage of the softening market to pass on the rate declines to their retrocessionaires and to buy more protection. Average use of reinsurance and retrocession for catastrophe business in the sector has increased from 29% in 2013 to 34% in 2014.

Table 1: 2015 Reinsurance Pricing Movement At January And July Renewals

	January 1, 2015	July 1, 2015
Property per risk		
Australia	0% to -5%	-5% to -12.5%
Canada	-10% to -20%	N/A
CEE	-5% to -20%	N/A
China	-25% to -30%	-15% to -20%
Europewide	-10% to -15%	N/A
France	0% to -5%	N/A
Germany	0% to -5%	N/A
Latin America	0% to -12.5%	0% to -15%
MENA	-5%	-10%
Nordics	-5% to -10%	N/A
Turkey	-10%	N/A
U.K.	-15%	-10%
U.S.	-10% to -15%	-5% to -20%
Casualty excess-of loss		
Australia	-5% to -10%	-5% to -10%
Europe TPL	-2.5% to -5%	N/A
Europe motor	-2.5% to -10%	N/A
France	0% to -3%	N/A
Lloyd's	-10% to -15%	N/A
U.K. Motor	0% to -5%	N/A
U.K. TPL	-5% to -20%	N/A
U.S. Motor	-5% to -15%	-5% to -15%
U.S. Professional indemnity	-5% to -15%	-5% to -10%
U.S. TPL	N/A	-5% to -10%
Specialty per risk		
Aerospace	0% to -7.5%	N/A
Engineering	-15%	N/A
Global trade credit	-20%	N/A
Personal accident/life catastrophe	N/A	-5% to -20%
Political risk	N/A	-10%
U.S. Healthcare	N/A	0% to -5%
U.S. Medical excess	N/A	0% to 10%

N/A: Not applicable. CEE: Central and Eastern Europe. MENA: Middle East and North Africa.
TPL: Third-party liability; movements are on non-loss-affected accounts. Source: Willis Re

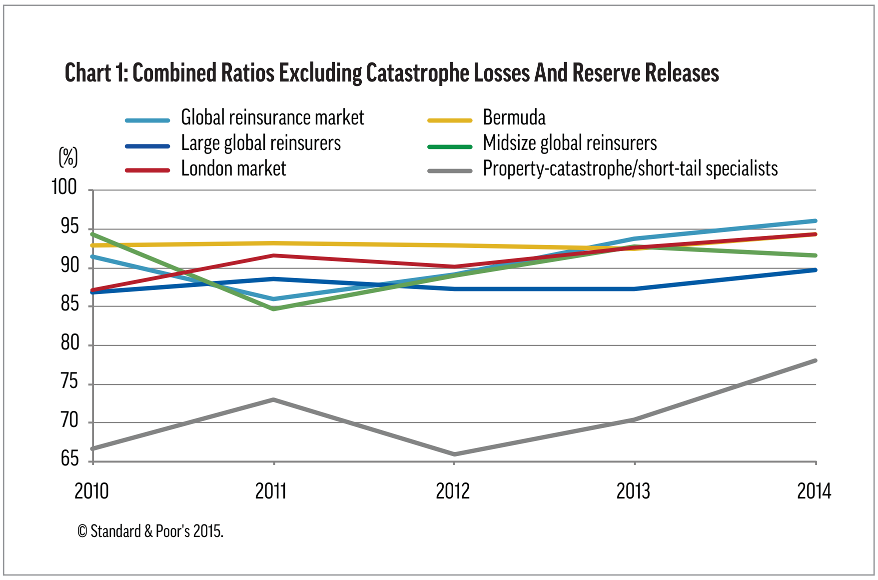
Alternative capital comes of age

The sector has come to see alternative capital as a permanent element in the competitive landscape, and many reinsurers are using it to their advantage. Most, if not all, rated reinsurers have established access to third-party capital, either by establishing sidecars, issuing catastrophe bonds, forming ILS funds to manage assets for third parties, or partnering with hedge funds to write business backed by their capital. By making use of these capital sources, traditional reinsurers can maintain their relationships with clients and write more gross premium. In most cases, they also gain some non-risk-bearing fee income. Although the amount is low in terms of return on equity (ROE) for most reinsurers, it does add some income diversification.

Reinsurers are also offloading some of the pricing pressure to the capital and unrated reinsurance markets by increasing their use of collateralized reinsurance (that is, reinsurance that has collateral posted against it to reduce credit risk) or retrocession protection.

Asset portfolios show reinsurers' tactical acceptance of greater investment risk

Investment income has fallen by 30% over the past four years, causing reinsurers to tweak their asset portfolios to arrest the decline (see "Asset Risk For Reinsurers Nudges Higher As Low Yields Continue To Bite"). We see these changes as tactical and within existing risk tolerances. Evidence suggests that reinsurers are taking on marginally more investment risk to



generate greater returns by increasing their investment in higher-risk assets such as equities.

Some reinsurers are increasing their asset durations or investing more of their portfolio in lower-rated issuers, which increases liquidity or credit risk. However, the sector's overall duration and credit quality remained unchanged in 2014 (3.1 years and 'AA-', respectively). In our opinion, the industry's extremely strong capital base allows it to absorb any capital strain from these moves.

Defensive Plays Have Only Bought Time

Despite management maneuvers, earnings deterioration appears to be unavoidable. Pricing continues to decline, investment returns remain well below historical levels, and the benefits to be gained by reserve releases should diminish following a series of benign catastrophe loss years. The results in the first half of 2015 support our view, as many companies are reporting weaker underlying results (adjusted for catastrophes and releases) than experienced in 2014.

We forecast a combined (loss and expense) ratio of 95-100% in 2015 and 97-102% in 2016, assuming 10 percentage points (ppts) for catastrophe losses and 6 ppts of benefit from reserve release, and ROE of 8-10% over the same period. This represents a marked deterioration compared with the sector's recent strong performance (see Table 2). The industry should be able to withstand these weakened earnings for the next two years, but we do not think these levels are sustainable over the longer term.

A deeper review of reinsurers' recent performance supports our expectation of continued deterioration. By stripping out reserve releases and catastrophe losses, we can observe the clear erosion of reinsurers' underlying earnings (see Chart 1). Pricing continues to decline, although more slowly than we originally expected, and we anticipate that underlying loss ratios will continue to increase.

There is no solace to be found in investment returns: we forecast low investment returns for the sector, and expect interest rates to rise only slowly from the end of 2015 (see Chart 2). Reinsurers have historically relied heavily on investment returns to support earnings. In the benign or average catastrophe years since 2008, investment income has historically contributed more than two-thirds of net income. When catastrophe activity has been high, investment income provided an even higher proportion of net income. Over the past four years, this contribution has diminished because investment returns fell by 30% over the period. We expect this trend to continue in 2015 and level off in 2016.

Reserve releases contributed significantly to reinsurers' strong earnings in 2014. The industry aggregate reserve releases as a proportion of total premiums has reduced for the third year in a row, as we anticipated. However, we've seen a number of companies actually increase their reserve release in 2014. The benefit to reinsurers' combined ratios was 8 ppts on average. This reverses the recent trend for reduced benefits from reserve releases over the previous three years. We suspect that 2014 was a blip caused by some companies trying to offset current-year losses.

Due to conservative reserving practices at most reinsurers, we expect reserve releases to provide some aggregate benefit in the next two to three years, but not at the level we've seen recently. A high proportion of the reserves released in recent years came because reserves set aside after natural catastrophes can generally be released about two to four years after the event. Given the low level of catastrophe losses in 2013 and 2014, we anticipate that reinsurers' ability to release catastrophe reserves will be significantly reduced (see "Property/Casualty Reinsurers With Strong Reserve Margins Are In A Better Position To Withstand The Prolonged Soft Market").

Capital Strength Should Remain

Despite the earnings deterioration we forecast, we anticipate that the sector will

Table 2: Standard & Poor's Global Reinsurance Earnings Forecasts

	(%)								
	2009	2010	2011	2012	2013	2014	2015f	2016f	Average 2010-2014
Combined ratio	86.8	92.6	105.6	88.1	86.4	86.4	95-100	97-102	91.8
Return on equity	22.2	14.1	5.2	14.4	14.1	16.4	8-10	8-10	12.8

f: Forecast. NB: Aggregate industry results.

continue to maintain extremely strong capital adequacy.

The sector's ability to generate record levels of capital has served it well during this time of relative famine. This trend has continued in 2014—even though reinsurers have further increased the amount of capital returned to shareholders, overall capital adequacy has improved (see Chart 3) and the industry's shareholders' equity and total adjusted capital have grown modestly.

Although we might otherwise expect pricing declines to erode the sector's excess capital cushion, our forecast pricing for 2015 and 2016 indicates to us that most reinsurers will display resilient capital adequacy. As we observed during 2014, we expect management teams to manage their portfolios and reallocate capital away from poorly priced lines to protect capital adequacy. That said, even without such actions, in a stress scenario in which catastrophe rates fall by 10% and pricing across all other lines declines by 5%, we would expect to revise our capital adequacy assessment for only two of our rated reinsurers.

Reinsurers also appear to hold capital buffers that could withstand a less gradual reduction in capital. Our annual surveillance of reinsurers' catastrophe risk exposure indicates that the industry's average exposure to a 1-in-10-year event is about 80% of its average earnings over the past two years, and its exposure to a 1-in-250-year event is roughly 33% of its shareholders' equity (see "Discipline Is Necessary As Reinsurers Adjust Their Exposure To Catastrophe Risk"). Following such a large event, we estimate that the sector would in aggregate hold capital adequacy in the 'A' range.

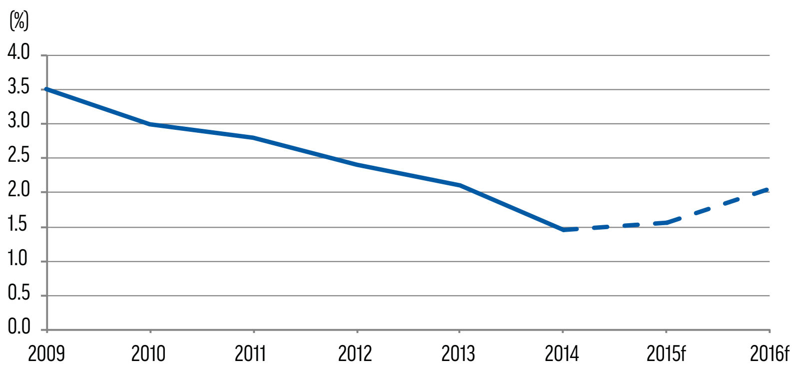
> **"Credit conditions remain negative for the global reinsurance sector and the subgroups most exposed to catastrophe cover are suffering the most."**

Headwinds Are Stronger For Some Subsectors

We see some diverging trends among subgroups and between individual peers. Short-tail catastrophe writers, London-based players, and Bermuda-based reinsurers are more exposed to earnings and capital pressures than the large and midsized global peer groups. Our current ratings on the companies in these peer groups generally reflect these trends, which we are monitoring closely.

M&A activity to date has largely revolved around these subgroups. We suspect that this reflects the more challenging road ahead for these players and we expect some of the companies operating in these subsectors to become potential targets or acquirers as the industry looks for further consolidation.

Chart 2: Reinsurance Sector Investment Yield Forecast



f: Forecast

In aggregate, capital adequacy has improved. However, those with the largest capital cushions—the Bermuda and short-tail property-catastrophe subgroups—saw them dented in 2014 (see Chart 3). Meanwhile global players were able to boost their capital adequacy. We chiefly attribute this trend to Bermuda-based reinsurers' greater activity in returning capital to shareholders during 2014.

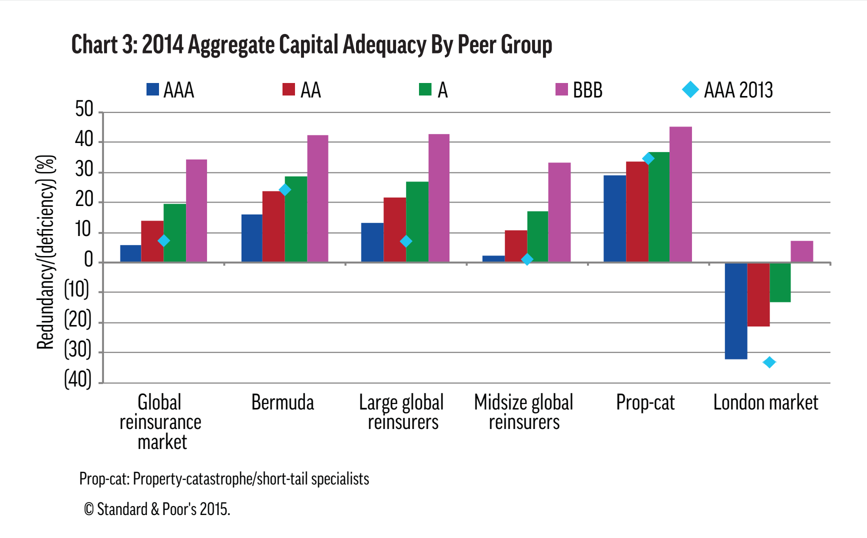
We continue to see a divergence in capital adequacy among peer groups. North American reinsurers carry more excess capital than their European counterparts, particularly those in London. London-based reinsurers appear less resilient to catastrophe events as a result. However, we take some comfort from the strength of European reinsurers' capital modeling capabilities. We have performed an in-depth review of seven European reinsurers' internal capital models. We have assessed all of them as "good" under our economic capital model criteria (ECM). This compares favorably with our assessments of the ECMs of seven other primary insurers around the world, three of which we assessed as "good" and four as "basic."

Unsurprisingly, earnings at property-catastrophe players deteriorated faster than the rest of the sector and other peer groups (see Chart 1). These companies bore the brunt of the pricing reductions in catastrophe business.

Short-tailed property-catastrophe players have also been most active in releasing reserves to support their results over the past five years, followed closely by Bermudians. Releases at short-tailed property-catastrophe players have augmented reported combined ratios by an average of 13.6 ppts over this period, and Bermudians' releases benefitted their combined ratios by an average 10.5 ppts. As these companies write more catastrophe cover than many peers in the market, we would expect to see a more profound deterioration in their reported combined ratios in coming years as releases on catastrophe losses dry up.

Global Reach Cannot Be Acquired Quickly

Reinsurers with global scope, underwriting expertise, and significant capacity to offer to increasingly demanding clients will be best-placed to withstand the negative pressures. That said, there is no quick route to acquiring these qualities. With size



comes responsibility, and some of the newly formed groups will need to ensure that they deploy their capacity and extend their reach responsibly and profitably, or they risk increasing competitive pressures further.

In our view, credit conditions remain negative for the global reinsurance sector and the subgroups most exposed to catastrophe cover are suffering the most. These companies have proven resilient so far, but will find it more difficult to compete over the next two years. The remaining players could become candidates for further consolidation or buyouts.

On the whole, we consider that the industry's flexibility thus far has protected it during difficult times. The defensive actions that reinsurers have taken in order to pass price declines on to others—which include returning excess capital, in some cases consolidation, and strong risk management (including portfolio steering, reallocation of business mix, and optimization of reinsurance and retrocession protection)—mean that fewer than one-half of the reinsurers we rate are overly exposed to these negative conditions. Therefore, we expect to take few rating actions over the next 12 months.

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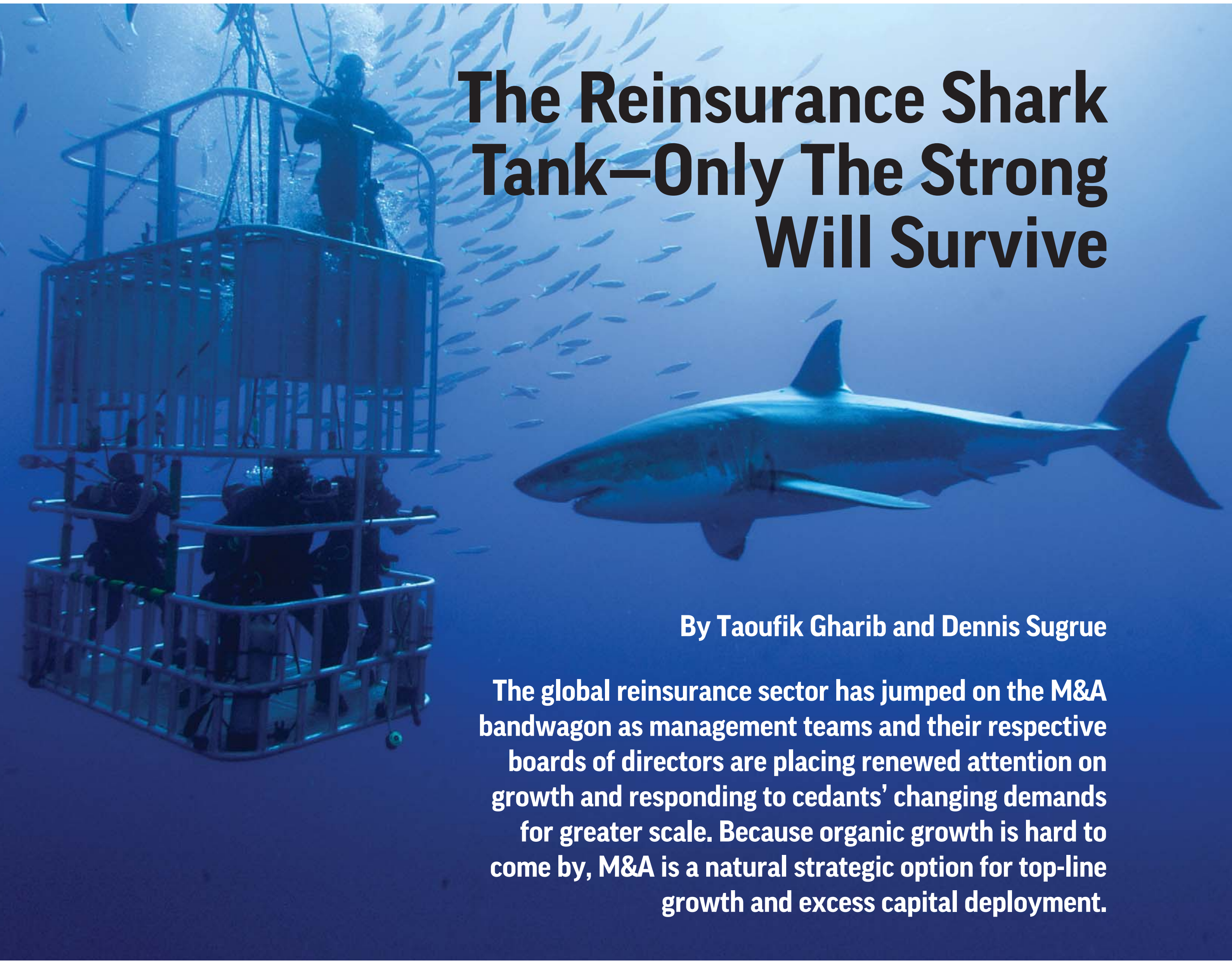


The Reinsurance Shark Tank—Only The Strong Will Survive

By Taoufik Gharib and Dennis Sugrue

The global reinsurance sector has jumped on the M&A bandwagon as management teams and their respective boards of directors are placing renewed attention on growth and responding to cedants' changing demands for greater scale. Because organic growth is hard to come by, M&A is a natural strategic option for top-line growth and excess capital deployment.

IMAGES: SHUTTERSTOCK / STEFAN PIRCHER

So far, 2015 is shaping up as the year of the mergers across many industries. According to financial software company Dealogic, U.S.-targeted mergers and acquisitions (M&A) reached a half-year record high of more than $1 trillion in the first half of 2015, the first time on record any nation has broken the $1 trillion mark in a half-year period. Since the 2008 financial crisis, multinational corporations have strengthened their balance sheets, hoarded cash, and seen their stock prices rally, which boosted their market valuations. On the other hand, the recovery of developed economies has been tepid, accompanied by a recent decline in oil prices, appreciation of the U.S. dollar, and pressure from investors' focus on top-line growth. In combination, these factors have acted as a catalyst for the M&A activity so far in 2015.

The global reinsurance sector is no exception and has jumped on the M&A bandwagon as management teams and their respective boards of directors are placing renewed attention on growth and responding to cedants' changing demands for greater scale. Because organic growth is hard to come by, M&A is a natural strategic option for top-line growth and excess capital deployment. During the past nine months, the re/insurance sector has been very active, with nine major M&A deals that totaled approximately $57 billion. On average, buyers have paid 24% more than market value. The highest premium of 38% was offered by Tokio Marine & Nichido Fire Insurance Co. Ltd. for its proposed acquisition of HCC Insurance Holdings Inc. About half of these acquisitions were all-cash transactions and the rest were a blend of cash, stock, and debt.

Major M&A deals have been announced during the past three quarters and are reshaping the reinsurance sector in a consolidation wave that Standard & Poor's Ratings Services anticipated. This trend confirms the challenges that global reinsurers' management teams face in the current soft market, including an ongoing downtrend in pricing and underwriting conditions exacerbated by an influx of third-party capital that poses an additional threat to traditional reinsurance players. Against this backdrop, reinsurers are increasingly seeking M&A transactions to alleviate some competitive market pressure and achieve profitable growth, cost savings, and capital efficiencies (see Table 1) .

We believe competitive pressures will remain elevated in reinsurance for the next 12 to 24 months, and we don't see the recent spate of consolidation as a panacea to alleviate that burden. In fact, we believe the trend toward greater scale highlights how hard it will be for management teams to defend their market positions. Few of these competitive pressures will abate as long as capital remains at or near all-time highs.

Strategic Or Defensive Moves?

On the surface, it seems that the barriers to entry for the reinsurance sector are low. However, it takes more than just capital to build a successful franchise with a defendable and sustainable competitive position to weather the vagaries of the underwriting cycles. Newcomers need to have a credible management team, a robust and diversified business model, established broker and client relationships, financial security, increasingly larger balance sheets, and a solid track record that takes time to develop. For example, many reinsurers from the "class of 2001" and "class of 2005" reached the end of what they could achieve as independent companies and decided to pair up with larger balance sheets as an exit strategy.

Cedants want to be sure that their reinsurers will be around to pay claims, and increasingly to be able to offer large reinsurance capacity and solutions to complex risks. The recent consolidation of small and midsize reinsurers to strengthen their competitive positions, bolster their balance sheets, and establish themselves as viable long-term players underscores the difficulty reinsurers have in ensuring that longevity. The recent spate of consolidations is reducing the number of players and raising the price of admission for reinsurers that seek to demonstrate their larger scale, scope, relevance, and staying power to increasingly sophisticated clients.

With the announcement of its $1.9 billion takeover of Platinum Underwriters Holdings Ltd. in November 2014, RenaissanceRe Holdings Ltd. kick-started the consolidation wave. Given the strategic fit, the successful execution of this transaction will accelerate RenaissanceRe's expansion into specialty and casualty reinsurance by adding Platinum's profitable book of diversifying business.

> **"The consolidation among reinsurance brokers and GMIs will have a direct effect on competition in the reinsurance market."**

After its failed attempts to acquire Aspen Insurance Holdings Ltd. in 2014, Endurance Specialty Holdings Ltd. completed its $1.8 billion buyout of Montpelier Re Holdings Ltd. in July 2015. This transaction will expand Endurance's breadth of distribution by adding a Lloyd's platform and third-party capital operation Blue Capital. Endurance's increased market presence and larger balance sheet should somewhat shield it from increasingly competitive market conditions in its lines of business.

RenaissanceRe's and Endurance's acquisitions of Platinum and Montpelier, respectively, are strategic and enhance their value proposition and market footprint. But these deals are also defensive in nature as both acquirers are seeking scale and breadth to differentiate their offerings from more-commoditized reinsurance capacity.

Reinsurers who are involved in this wave of M&A have listed a number of benefits to the proposed deals to justify the cost: increased scale, product diversification, cost synergies, and capital efficiency. We see some potential benefits to each of the individual deals, if executed correctly. However, we would classify all of these transactions as primarily defensive in nature, as the management teams have taken the view that combining forces with another player will make their companies more viable to compete in the coming years.

Emulating The Berkshire Hathaway Business Model

Lately, we have seen an increased interest by investors in emulating the Berkshire Hathaway Inc. (BRK) business model. Through their investment holding companies, they are acquiring re/insurers with strong operating cash flows that ultimately will be upstreamed to the parent company. Re/insurers receive premiums up front and pay claims later. This collect now and pay later re/insurance model generates cash flows or "float" that the BRK copycats invest.

Through this scheme, these investment holding companies gain access to capital with minimal cost. The BRK business model is hard to duplicate and it is becoming a crowded trade in an already saturated reinsurance market. We expect more similar deals to come to the market during the next 12 months, which will likely continue to put pressure on reinsurance pricing given these holding companies' lower cost of capital relative to standalone, publicly traded reinsurers'.

Canada-based Fairfax Financial Holdings Ltd. has followed the BRK model for decades. Similar to BRK, Fairfax's insurance and reinsurance companies operate on a decentralized basis, with autonomous management teams applying a focused underwriting strategy to their markets. In addition, Fairfax's investments are centrally managed at the group level, seeking to invest assets on a total-return basis, which includes realized and unrealized gains in the long term.

With its $1.9 billion purchase of Brit plc, which closed in July 2015, we recognize the potential diversification benefit to Fairfax if this acquisition is well executed. Brit is a leading underwriter in the Lloyd's market and has a strong track record of underwriting profitability, which should enhance Fairfax's operating performance and contribute to the re/insurance float to the parent company.

The Chinese and Italian acquirers—Fosun International Ltd., China Minsheng Investment Corp., and EXOR SpA—who are newcomers to the reinsurance market are following suit. In May 2015, Fosun announced the acquisition of the remaining interest in Ironshore Inc. that it does not already own (about 80%) in a $1.8 billion transaction. Fosun paid about $464 million for the initial 20% back in August 2014. In July 2015, China Minsheng Investment reached a definitive agreement with White Mountains Insurance Group Inc. to buy Sirius international Insurance Group Ltd. for about $2.2 billion. Finally, after many attempts, on August 3, 2015, EXOR clinched an agreement to acquire PartnerRe Ltd. for $6.9 billion.

None of these three transactions has closed yet. Therefore, it is still unclear how these to-be-acquired entities will operate under the new ownership. Questions involve the prospective capital management, investment strategy, growth strategies, upstreaming of dividends, composition of the board of directors, and direction of the enterprise risk management framework, including any changes to risk tolerances and aggregation processes.

We could take negative rating actions on these reinsurers if we believe the change of ownership will weaken their business or financial risk profiles. There is still uncertainty surrounding how, under the new ownership, their investment strategies could be altered and potentially become more aggressive, or their competitive position could be undermined by a significant strategic shift in their business mix to lines or regions in which they don't already have expertise and relationships.

Reinsurers Aren't The Only Ones Joining The M&A Game

Insurance M&A has been rampant outside the reinsurance market as well, with a number of large deals announced in recent months in the U.S. healthcare market and the global multiline insurance (GMI) arena. There has also been continued consolidation in the non-life broker market during the past two years. The consolidation among reinsurance brokers and GMIs will have a direct effect on competition in the reinsurance market. We believe this will exacerbate the reduced reinsurance purchasing from GMIs that we've observed in recent years. Expense savings and lower cost of capital could push pricing down further.

Unlike in the global reinsurance sector, however, we do not expect a large round of M&A deals among the GMIs. These insurers have successful standalone strategies and do not face the same competitive pressures. We believe the motivations behind some of these deals were compatible business platforms and customer reach rather than a need to grow in scale or to diversify. In fact, ACE Ltd.'s $28.3 billion acquisition of the Chubb Corp. makes it more nationally concentrated. Conversely, we view Tokio Marine's $7.5 billion bid to acquire HCC as a continuation of its global business expansion and portfolio diversification strategy after acquiring Philadelphia Consolidated Holding Corp. and Delphi Financial Group Inc. a few years ago.

The result of many large transformational M&A deals is larger and more-diversified balance sheets. We've noted for some time that GMIs and large insurers are optimizing and rationalizing their reinsurance purchasing (see "Lessons From Large U.S. Cedants In The Game Of Reinsurance Arbitrage"). We expect that, in the longer term, this increased scale and spread of risk will increase these companies' ability to reap the benefits of diversification within their portfolios and justify buying less reinsurance despite softer pricing. For example, following the completion of the $4.1 billion merger between XL Group plc and Catlin Group Ltd. in May 2015, the combined group publicly stated that it has room to optimize its $2.8 billion in ceded premiums further and has increased purchasing power over its reinsurers.

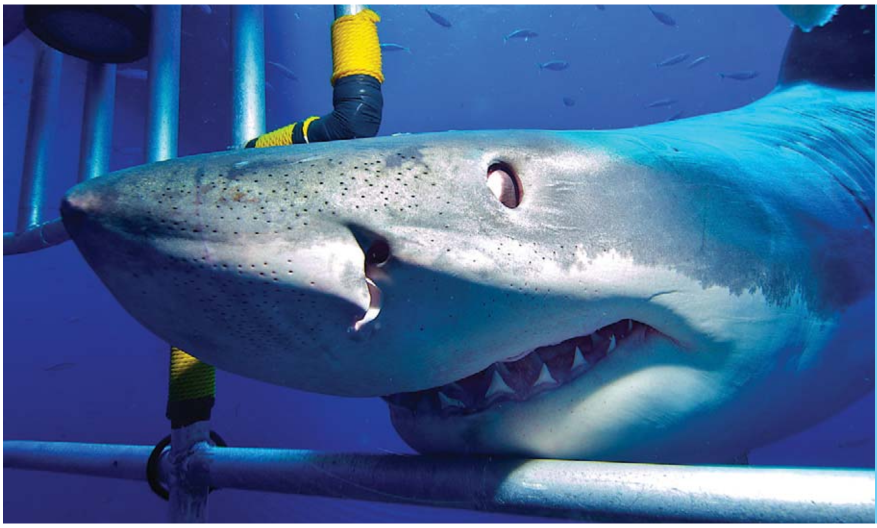
Similarly, Tokio Marine's acquisition of HCC brings a significant book of business (8% of the consolidated group's premiums) with little overlap in risk profile. Tokio Marine's recent expansion into the U.S., which now represents roughly 25% of its premiums, could help reduce the group's peak exposures. In the event of a large loss in Tokio Marine's home market of Japan, it is likely that its U.S. business exposure to such an event would be relatively small, and could generate profit to offset the Japanese losses. This earnings diversification and loss mitigant can somewhat reduce the group's need for reinsurance coverage in Japan, effectively shrinking the amount of premium to be written by the global reinsurance market.

The benefits that companies generally

Table 1: Major M&A Re/Insurance Deals

Announced	Closed	Acquirer	Acquiree	Bil. $	Terms of the transaction	Premium paid for the acquisition (%)
24-Nov-14	2-Mar-15	RenaissanceRe Holdings Ltd.	Platinum Underwriters Holdings Ltd.	1.9	Cash and stock	24.0
9-Jan-15	1-May-15	XL Group plc	Catlin Group Ltd.	4.1	Cash, stock, and debt	23.5
16-Feb-15	8-Jul-15	Fairfax Financial Holdings Ltd.	Brit plc	1.9	All cash	11.2
31-Mar-15	31-Jul-15	Endurance Specialty Holdings Ltd.	Montpelier Re Holdings Ltd.	1.8	Cash and stock	19.0
3-May-15	1Q - 2016	Fosun International Ltd.	Ironshore Inc.	2.3	All cash	NA
10-Jun-15	4Q - 2015	Tokio Marine & Nichido Fire Insurance Co. Ltd.	HCC Insurance Holdings Inc.	7.5	Cash and debt	37.6
1-Jul-15	1Q - 2016	ACE Ltd.	The Chubb Corp.	28.3	Cash, stock, and debt	30.0
27-Jul-15	NA	China Minsheng Investment Corp.	Sirius International Insurance Group Ltd.	2.2	All cash	NA
3-Aug-15	1Q - 2016	EXOR SpA	PartnerRe Ltd.	6.9	All cash	23.0
			Total	**56.9**	**Average**	**24.0**

NA: Not available



"The benefits that companies generally hope to attain from transformational combinations—diversification, expense savings, and greater scale—can have an impact on the prices they charge for coverage."

hope to attain from transformational combinations—diversification, expense savings, and greater scale—can have an impact on the prices they charge for coverage, particularly in their reinsurance divisions given the pricing pressures in that market. The premium charged for an insurance contract is a function of the expected loss on the contract, the expenses allocated to that contract, and a profit margin. Return on risk-adjusted capital is the profit margin that the insurer earns on the capital allocated to this risk. A company that has significantly improved its diversification could see a decrease to the risk capital and therefore theoretically could accept lower margins to earn the same return—this could increase the latitude for price decreases further. Perhaps even more meaningful in this equation is the benefit of reduced expenses that in theory could be passed on to clients in the form of lower pricing. Expense synergies were an important consideration, though not the main driver, for the management teams of ACE and Chubb and XL-Catlin in their assessment of their respective deals. ACE estimates expense savings of $650 million following the tie-up with Chubb, and XL-Catlin expects to cut $250 million during the next few years. For some companies involved in M&A which are also operating in a highly competitive or softening market, an ability to lower prices without sacrificing profit could be an important competitive advantage. However, should companies pull this lever it could also add to pricing declines in the reinsurance market as peers feel the pressure to keep up.

M&A activity in the broker market is also likely to place more pressure on pricing and profitability in the reinsurance and primary markets. A recent string of transactions among brokers of all sizes has accelerated consolidation in a market already dominated by the 'Big 3' (Aon plc, Marsh Enterprises LLC, and Willis Group Holdings PLC). More than 230 deals were announced in 2014—a record number—and the frenzy has continued in 2015 culminating in the announcement of Willis's intention to merge with Towers Watson for $18 billion.

The existence of fewer options for re/insurers to distribute their products shifts the balance of power to the side of the brokers and buyers, making it easier for them to demand lower premium rates. As single firms account for a larger proportion of a re/insurer's distribution, they have more leverage to increase commissions and fees, raising expenses for the re/insurers and squeezing profitability.

At a time when organic growth is proving to be challenging for many re/insurers, acquisition is a quicker route to growth for some. When acquiring well-capitalized companies with minimally overlapping risk profiles, this strategy can provide some excess capital on which the acquirer can write more business, potentially increasing competition in those lines.

A Tough Year Ahead In The Search For Scale

We believe the reinsurance M&A momentum will continue for the rest of 2015 and into 2016. The current reshaping within the reinsurance sector, most of which is taking place among the small and midsize reinsurers, will not result in a meaningful reduction of industry capital. This reflects our belief that the primary motivation for these transactions is to achieve the scale that management teams deem necessary to compete in the global market. Thus, significant capital returns are unlikely in these deals.

The trend in M&A highlights players' need for scale and diversification because cedants are increasingly looking to partner with reinsurers that can offer large capacity across multiple geographies and have the expertise to write tailored products. We expect further consolidation in the market as smaller reinsurers are squeezed more than globally diversified groups and look to gain scale to compete.

The industry is undergoing a reconfiguration that will result in fewer but larger reinsurers. The path to that result is strewn with challenges in executing and integrating new transactions, growing into new capital bases, and competing against a different set of peers. Profitability and capital preservation will be difficult to achieve as pricing declines continue and investment yields are slow to rise.

We foresee another competitive and difficult year for the reinsurance sector. It is unlikely in the next 12 to 24 months that we will see profitability return to the strong levels of the past five years, that pricing will improve enough to turn the market across the board, or that competition will subside. In the meantime, for reinsurers, there seems to be a Darwinian concept at work, as only those strong enough to adapt or evolve will survive. ■

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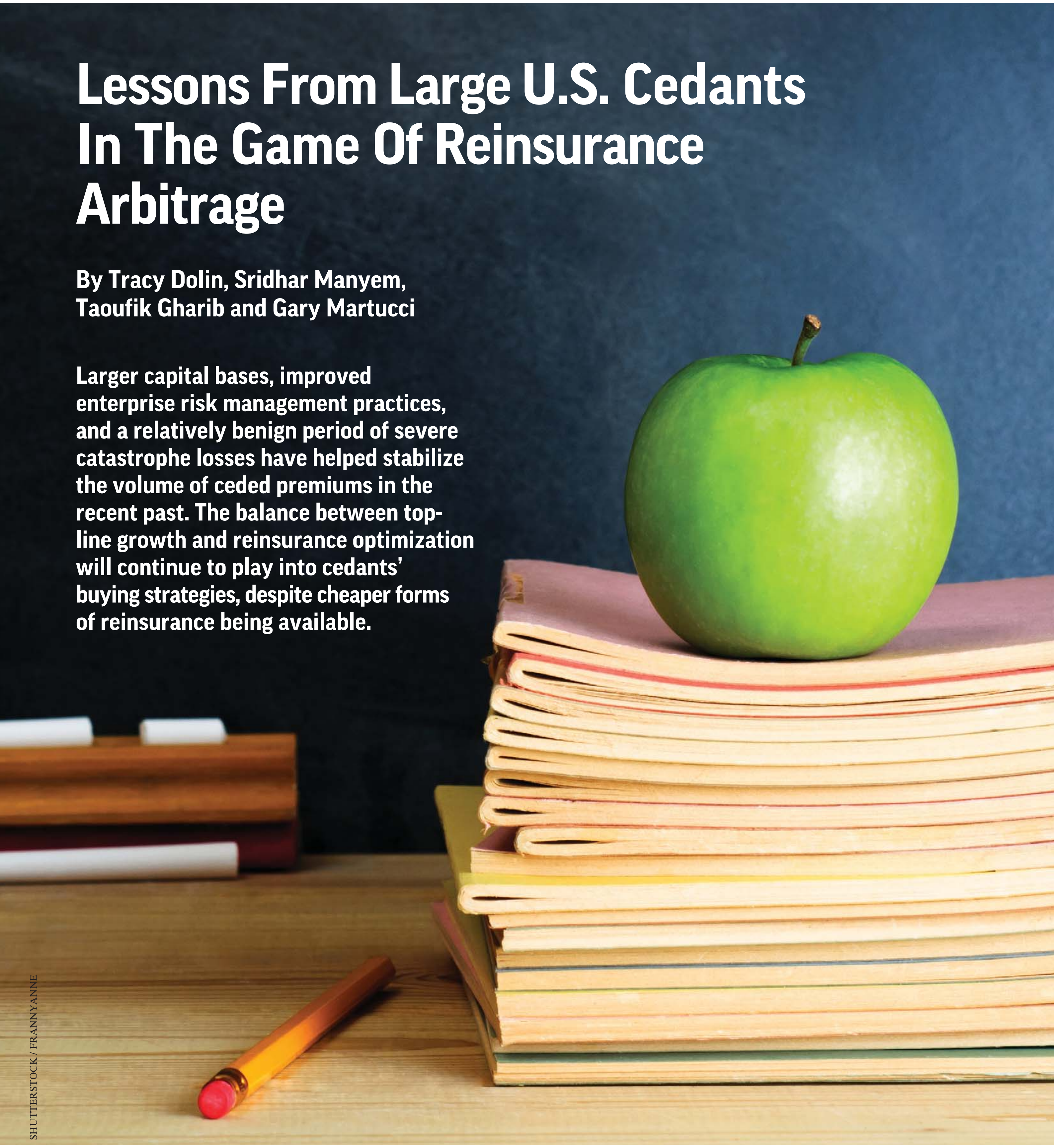
Lessons From Large U.S. Cedants In The Game Of Reinsurance Arbitrage

By Tracy Dolin, Sridhar Manyem, Taoufik Gharib and Gary Martucci

Larger capital bases, improved enterprise risk management practices, and a relatively benign period of severe catastrophe losses have helped stabilize the volume of ceded premiums in the recent past. The balance between top-line growth and reinsurance optimization will continue to play into cedants' buying strategies, despite cheaper forms of reinsurance being available.



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Reinsurance pricing declines have not reached their trough, and have been intensified by traditional players' ample capacity and third-party capital. Insurers of all sizes are experiencing top-line pressure that may limit demand.

In a buyers' market, not all large U.S. cedants have approached their reinsurance purchasing power equally. Reinsurance pricing declines have not reached their trough, and have been intensified by traditional players' ample capacity and third-party capital. Unlike smaller primary writers, larger insurers do not rely on reinsurance leverage for capital relief. At the same time, insurers of all sizes are experiencing top-line pressure that may limit demand.

The trickle-down of soft reinsurance property pricing to the primary market is uneven and most apparent among larger commercial property accounts. Although reinsurance arbitrage (profiting by exploiting pricing differences between reinsurance and direct insurance) exists, large U.S. cedants have not changed their underwriting appetite and have not set their risk tolerances based on the availability of reinsurance. Although cedants' reinsurance strategies differ, the common dominator is that reinsurance optimization does not translate into underwriting dilution. Although it is unlikely, Standard & Poor's Ratings Services could take rating actions if we start to see insurers rely on cheaper forms of reinsurance to support excessive growth, poor underwriting standards, or insufficient risk management.

Buyers' Market = Cedants' Paradise

When it comes to reinsurance purchases, insurers have never had it so good. They are operating from strength on both the demand and supply sides. From a demand perspective, North American insurers have seen their surplus steadily increase and reserve positions remain adequate. This additional capital cushion leaves room for insurers to keep risks (and the profits associated with these risks) on their own balance sheets. In addition, insurers, especially the larger ones, have been steadily combining and centralizing reinsurance purchases. Historically each business unit and/or line of business would buy reinsurance on its own to protect its results; now those purchasing decisions have been moved to the holding companies for cost savings (i.e., economies of scale),

> **"A prevailing soft pricing cycle is favoring cedants that grab better deals during the renewals."**

portfolio optimization, improved views of risk capital, and capital allocations.

From a supply perspective, the story is all too familiar as well. The reinsurers' market is currently overflowing with excess capital that can absorb losses, a situation exacerbated by intense competition. For example, low interest rates have forced investors to look for yields outside the traditional fixed income space. These investors with alternative capital have been attracted to catastrophe risks that they view as mostly isolated from systematic risks. This is evident in the increased funds flowing in from catastrophe bond issuances and collateralized reinsurance vehicles that have increased the supply of capital allocated to catastrophe risk. As a result, a prevailing soft pricing cycle is favoring cedants that grab better deals during the renewals.

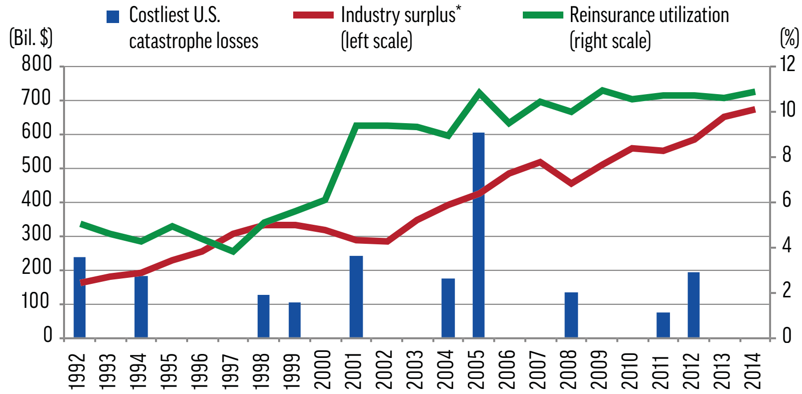
Reinsurance utilization (ceded premiums over gross written premiums) jumped in 2001, as the events of September 11 and unrealized losses in 2000 (10-year treasury yields increased to 6.66% from 4.72%) caused a decline in statutory surplus (see Chart 1). Similarly, ceded premiums were at historical highs in 2004–2005 as insurers woke up to Hurricanes Charley, Frances, Ivan, and Jeanne in 2004 and Katrina, Rita, and Wilma in 2005. Consequently, 2005 was a watershed year for the reinsurance industry.

The combined ratio for reinsurers was 130% compared to 100.5% for primary insurers in 2005. This caused significant market disruptions and increased pricing that made risk-adjusted returns attractive to new capital. This in turn resulted in the 'class of 2005'. On the flip side, the lack of meaningful losses in recent times, increases in reinsurers' surplus driving increased competition, and the influx of external capital have created the perfect conditions to foster competitive pressures and softer pricing for reinsurers.

Reinsurance's Identity Crisis

The line between the reinsurance and insurance-linked securities (ILS) markets has become blurred. As they contend with competitive pressures, traditional reinsurers are beginning to behave like third-party capital suppliers. Traditional reinsurers are starting to borrow underwriting terms from the ILS market in the forms of multiyear policies and inclusion of non-modeled perils in traditional reinsurance treaties. Cedants can get the best of both worlds by skipping the costs and time of setting up special purpose vehicles, marketing their securities, running independent modeling, paying legal fees, and providing related documentation

Chart 1: Reinsurance Utilization Versus Industry Surplus And Costliest U.S. Catastrophe Losses



*ISO data.

required for an ILS placement beyond the requirements for an individual reinsurance placement.

For example, in 2015 Allstate Corp. took advantage of terms and conditions in the traditional reinsurance market to purchase seven-year property-catastrophe coverage with the flexibility to adjust its layer position annually, after being rebuffed by the ILS market. Allstate was also successful last year in securing multiyear contracts in the first six layers of its per-occurrence excess catastrophe reinsurance treaty. Similar to last year, on July 1, 2015, ACE renewed its U.S. terrorism coverage (excluding nuclear, biological, chemical, and radiation coverage) with the same structure (i.e., limits, retention and co-participation) as its global natural catastrophe program, although it purchased terrorism coverage on an aggregate basis without a reinstatement. In most of ACE's programs that have a more-than-$1 billion attachment point, biological and chemical terrorism coverage is included for personal lines exposures in states mandating this coverage.

On April 1, 2015, ACE Ltd. established an internal hedge fund-backed reinsurance platform (ABR Reinsurance Ltd.) through a joint venture with BlackRock Inc. ACE owns a 10% minority stake with $800 million of capacity from a private placement. As a large buyer of reinsurance, with $5.8 billion of ceded premiums during the 12 months ended June 30, 2015, ABR Re is just one of many avenues ACE is utilizing to improve efficiencies. ABR Re is not the first hedge fund-backed reinsurer, but its registration highlights more momentum toward shortening the chain between the capital market and insurers, bypassing intermediaries, and putting pressure on established reinsurers on cedants' panels.

Reinsurance Buying Trade-Off

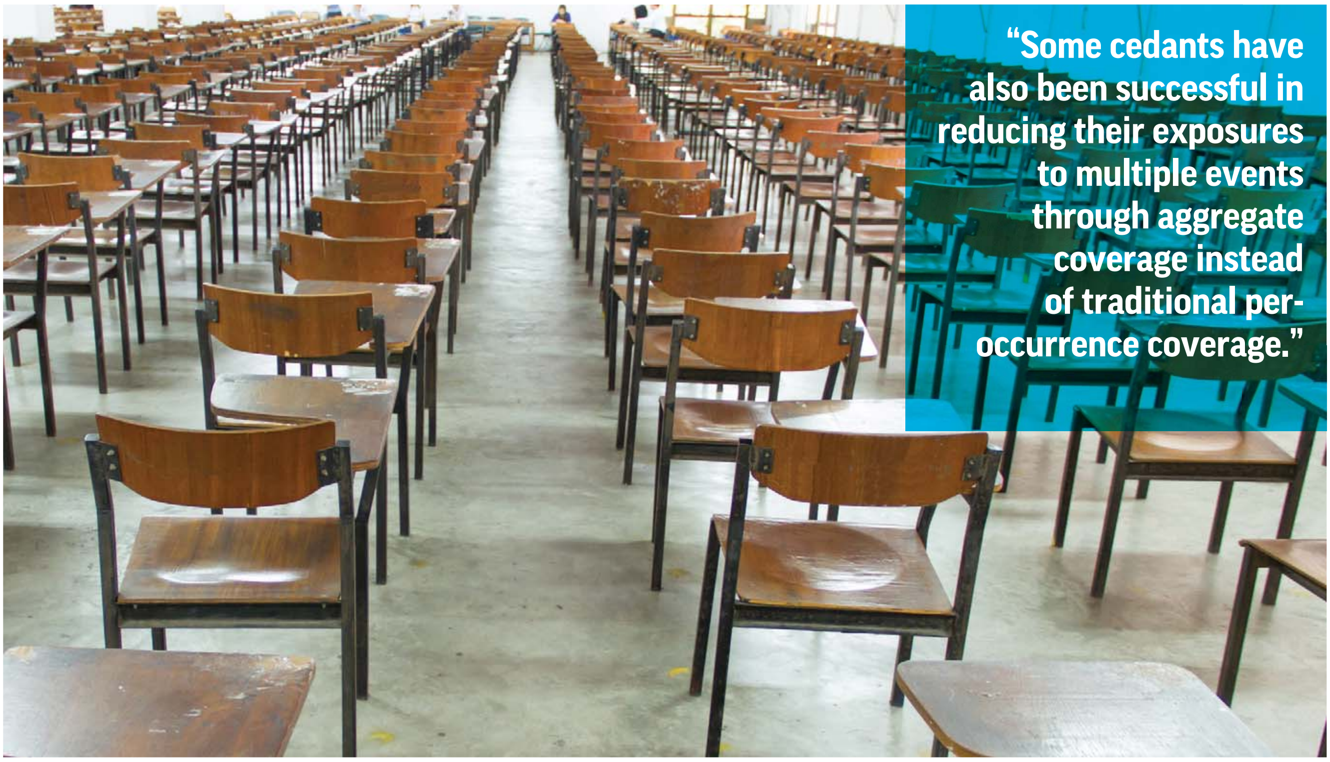
Primary insurers are benefiting from reduced reinsurance costs that are not evenly passed down to the insureds (especially for large accounts), creating opportunities for arbitrage. Nevertheless, primary writers are not compromising their underwriting standards. Reinsurance technically helps cedants to free up capital to underwrite more risk and increase top-line growth. Conversely, we have not seen a trend by cedants to increase their top line through reinsurance leverage.

Despite the low net premiums written-to-surplus ratio in the recent past (0.74x for 2014 versus a 15-year average of approximately 0.94x) and ample reinsurance capacity, primary insurers are favoring profitability over top-line expansion with the available capital. Although primary pricing remains adequate, it is softening with variations by line of business.

From a cedant's point of view, larger capital bases, improved enterprise risk management practices, and a relatively benign period of severe catastrophe losses have helped stabilize the volume of ceded premiums in the recent past. The balancing act for the cedants has been between reinsurance optimization and top-line growth. Many cedants have resorted to higher retentions

Table 1: Nonlinear Relationship Between Reinsurance Costs And Purchases

Property-catastrophe reinsurance buying strategy	Popularity	Uptake	Cost accretive	Comments
Higher retentions	Mixed	Travelers (07/01/2015), Chubb(04/01/2015), AIG (2012), Erie (01/01/2015)	Yes	Rate on line (ROL) is more expensive on the lowest layer of the tower.
Lower co-participation	Low	Erie (01/01/2015)	Mixed: depending on layer	Most insurers have low co-participation.
Higher layers purchased	Mixed	Travelers (01/01/2015), ACE (07/01/2015), Allstate (06/01/2015), AFG (01/01/2015)	No	ROL is cheaper. Cost savings from raising retentions more than pays for higher layer purchases.
ILS participation (i.e., CAT bonds)	High	Allstate (coverage until 2017 and 2018), Chubb (three bonds expiring between 2016 and 2020), Travelers (expiring in June 2015 and May 2016), AFG (coverage until Dec 2016), AIG.	Yes	Cost accretive because insurers can lock in rates for mutliple years and add additional perils.
Collateralized reinsurance	Mixed	ACE (07/01/2015: Approximately 21% of the coverage was placed with reinsurers providing upfront collateral equal to the limit of their participation and without a reinstatement).	Yes	Ratings agnostic. (Uncollatoralized reinsurance usually requires 'A-' rating for placement).
Multiyear policies by traditional reinsurers	Mixed	Allstate (2014 & 2015), Hartford (catastrophe treaty has terms extending beyond one year). Most ILS are multiyear policies.	Yes	Cost accretive because insurers can lock in rates for mutliple years.
Favorable terms and conditions	Mixed	Allstate (06/01/2015), ACE (07/01/2015).	Yes	Longer hours clauses, addition of non-modeled perils, forfeit reinstatement premiums, etc.
Increased use of aggregate coverage (versus traditional per occurrence)	Mixed	Hartford (01/01/2015), Travelers (07/01/2015), ACE (07/01/2015)	No	Costs more but is now cheaper and more available than in harder market years. We have also seen an increase in second event/third event coverage.



“Some cedants have also been successful in reducing their exposures to multiple events through aggregate coverage instead of traditional per-occurrence coverage.”

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in recent renewals, although not all players consistently use this strategy.

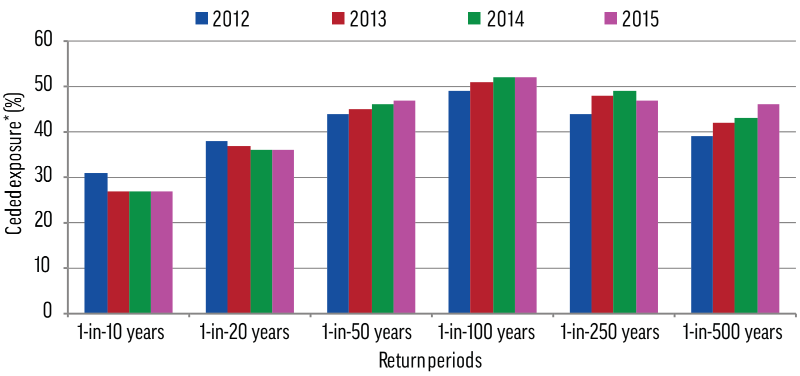
A nonlinear relationship exists between reinsurance pricing and buying. This is partly because most property-catastrophe reinsurance treaties are written on an excess-of-loss (XOL) basis, as opposed to a proportional (pro-rata) basis. Structural considerations aside, we also observed an improvement in the quality of reinsurance purchases on a cost-neutral or accretive basis (i.e., insurers are getting more bang for their buck because costs are either the same or slightly better but they are getting more from reinsurance contracts). Increasingly, traditional reinsurers have offered similar features to those offered in the ILS market.

Many cedants are bargaining for multi-year or multi-peril contracts from traditional reinsurers, ceding higher layers in the existing reinsurance structure and adding top-up features such as expanded geographic or peril coverage. Some cedants have also been successful in reducing their exposures to multiple events through aggregate coverage instead of traditional per-occurrence coverage (see Table 1).

A major hurricane (category 3 or greater) has not affected the U.S. since 2005. From a frequency standpoint, the weather has also been unusually kind for the insurance industry during the past two years. We sense a level of complacency among primary writers with respect to commercial property pricing due to benign catastrophe activity. Our proprietary data shows that cedants have been more tolerant to take a hit on their earnings from catastrophe frequency losses by retaining more of the probable losses in the lower risk-return periods such as the 1-in-10 and 1-in-20-year probable maximum loss (PML; see Chart 2). (We define ceded exposure as gross PML - net PML/gross PML per each risk return period on an aggregate all-perils worldwide basis.)

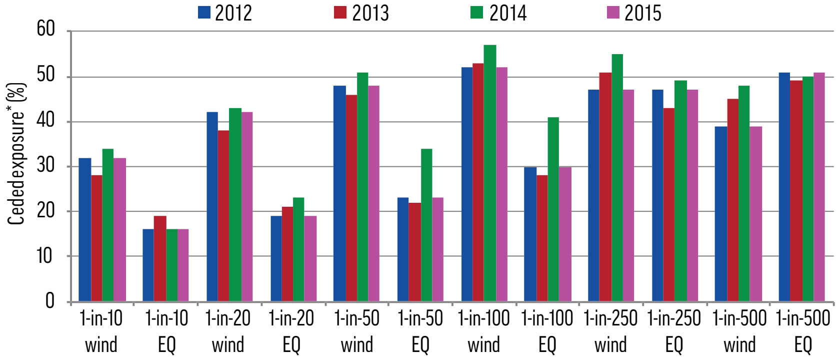
From a capital erosion perspective, the existing large capital base seems robust enough to keep the temporary earnings volatility at bay. On the other hand, we have observed cedants buying more reinsurance coverage relative to the higher risk-return periods of 1-in-250 and 1-in-500-year PMLs. The rationale

Chart 2: Ceded Exposure Over Several Return Periods



*Ceded exposure = weighted average of ([gross PML - net PML]/gross PML per risk-return period).
PML: probable maximum loss

Chart 3: Ceded Exposure For North American Wind And Earthquake Over Several Return Periods



*Ceded exposure = weighted average of ([gross PML - net PML]/gross PML per risk-return period).
PML: probable maximum loss, EQ: earthquake

of this move is to take advantage of lower reinsurance rates on line and reduce the severity risks from a large catastrophic event. Peak reinsurance protection remains at the 1/100 risk-return period.

Overall, top-line pressure and capital preservation is propelling the trade-off between higher retentions and severity protection (through the purchase of higher layers). Cedants are much more concerned about frequency risk from wind perils than earthquake peril (see Chart 3). However, as the stress levels increase, it appears that at a 1-in-500 stress level the amount of exposure ceded for an earthquake event is greater than the amounts ceded for a wind event. Severity risks from earthquakes are much more uncertain, as the 2011 Great Tohoku Earthquake illustrated.

The Gap In The Two-Tiered Reinsurance Market Is Growing

Cedants do not view reinsurers equally, and the divide between tiers 1 and 2 is becoming more severe. There are varying degrees of reinsurance culling among cedants. Although efficiency alone might be a compelling reason to reduce reinsurance panels, other considerations, including credit quality, reinsurance product offerings, and the size of a reinsurer's balance sheet, naturally impel cedants in that direction. On the flip side, some cedants favor wide-ranging reinsurers to spread out counterparty risk. Despite diverging views regarding optimal reinsurance panel sizes, one thing is for certain: cedants tend to view tier 1 reinsurers as strategic partners.

Cedants prefer reinsurers that have a claims-paying track record rather than those that are pure sources of capacity. Tier 1 reinsurers remain more relevant to cedants because of their long-standing relationships, value-added services, and complex risks. We do not believe that the balance will tilt in favor of third-party capital, because these players' commitment to the marketplace is confined to commoditized products (i.e., cat risk) for now, and their future claims-paying capabilities are less certain.

Tier 1 reinsurers have leveraged their status in the eyes of cedants by leading reinsurance programs and repackaging risk. The market will always need reinsurance program leaders to establish the underwriting blueprints, even though third-party capital is beginning to participate in a form-following function. Private placements are a hallmark of top-tier reinsurers' playbooks. This group assumes higher limits and/or more aggressive coverage terms through these private placements and subsequently repackages some of these risks through retrocession to tier 2 reinsurers and third-party capital instruments. In some circumstances, retrocession is the only gateway for tier 2 reinsurers to access large cedants' risk, albeit indirectly.

The strength of tier 1 reinsurers' balance sheets allows this group to offer adverse development coverage (ADC) treaties exclusively to cedants for long-tail lines of business, a narrow but increasingly prevalent practice. Berkshire Hathaway, Munich Re, and Swiss Re are a part of this select few. ADC treaties are a win-win for cedants and reinsurers alike. ADC placements by tier 1 reinsurers are attractive to cedants because they are trading high reserving risk for low credit risk, providing a form of capital relief.

For reinsurers, ADCs are attractive because of their immediate access to investment float. Cedants, however, need to exhaust paid claims up to the reference attachment point before ADCs will be triggered. This means from a cash-flow perspective, cedants will not see one dollar of reinsurance recoverables for multiple years. Therefore, we doubt hedge fund-backed reinsurers' entry into this type of product will be very successful given feasible concerns about counterparty risk.

Price Alone Does Not Drive Reinsurance Utilization

The bifurcation of reinsurance optimization strategies among large cedants highlights differing levels of strategic risk management sophistication and risk tolerances. The balance between top-line growth and reinsurance optimization will continue to play into cedants' buying strategies, despite cheaper forms of reinsurance being available. One of the pillars of our stable outlook on the primary P/C sector hinges upon insurers' focus on underwriting profitability over market share pursuits. We do not believe insurers are changing their risk tolerances and/or underwriting guidelines just because cheaper forms of reinsurance are available. ■

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Discipline Is Necessary As Reinsurers Adjust Their Exposure To Catastrophe Risk

SHUTTERSTOCK / PHOTOCREO MICHAL BEDNAREK

By Charles-Marie Delpuech and Miroslav Petkov

Some reinsurers are putting their faith in taking on increased cat risk, while others appear to be looking to expand in other lines of business. We predict that those that misjudge their exposure could be left isolated after the next large event, and discipline is necessary as reinsurers face difficult decisions.

Insured catastrophe losses in 2014 have been estimated at $35 billion, around half the 10-year average of $64 billion for the global reinsurance industry (Source: Swiss Re). Two years of low claims have contributed to the current record high levels of capital in the industry and thus to the recent downward trend in catastrophe risk pricing.

In analyzing reinsurers' catastrophe exposure, we have identified a divergence in reinsurers' strategic reaction to the softening markets. While most reinsurers allowed their exposure relative to capital to contract, a few took on more exposure this year. In our view, an increased focus on catastrophe risk weakens a reinsurer's risk position by increasing volatility in earnings and on the balance sheet. We consider underwriting profitability in the sector likely to become more vulnerable to natural catastrophes; therefore, we anticipate that operating performance could deteriorate in reinsurers that are more exposed.

Most Reinsurers Display Little Appetite For Increased Balance Sheet Exposure To Catastrophe Risk

The earnings-at-risk metric (the aggregate 1-in-10-year net modeled loss impact on the last two years' average profit before catastrophe losses and tax) indicates that most rated reinsurers would likely absorb aggregate losses from events modeled to occur every 10 years or so through earnings generation alone (see Chart 1). Although investment returns have fallen and reinsurers are reporting higher accident-year combined ratios, indicating weaker underwriting results, their capital bases remain secure against such high-probability/high-frequency events. The average exposure has fallen only slightly, to 0.73 x annual profit before tax, from 0.75 x last year.

In fact, our analysis suggests that, for most reinsurers, exposure to more-frequent events—those with a 1-in-10-year or 1-in-50-year return period—has reduced. (A return period is an estimate of the likelihood of an event; it describes the frequency of an event of a certain magnitude.) We calculate a reduction of 10% to 20% for a third of reinsurers. Changes to the market might explain some of these changes; primary insurers have increased their retention levels to more-frequent events and optimized their use of reinsurance, even as the cost of reinsurance has fallen.

Overall, the capital-at-risk exposure (the aggregate 1-in-250-year exposure net of reinsurance-modeled loss impact on shareholders' equity) has decreased to 33% at the start of 2015 from 35% at the start of 2014, a change we do not consider significant. In our view, the reduction stems from lower aggregate exposure to 1-in-250-year events and increased excess capital. However, strengthening of the U.S. dollar against other currencies has also contributed to the changes.

Nevertheless, there is greater variation at the individual reinsurer level. Some have seen material reductions and some are taking up more exposure this year (see Chart 2). Balance sheet exposure to catastrophe risk has contracted for most reinsurers; a third of rated reinsurers have seen a reduction of 3 percentage points or more.

The largest reductions typically come from reinsurers that have less-diversified profiles, which have started to reallocate capital to other lines of business, such as U.S. casualty. Some reinsurers have also adjusted down their catastrophe risk limits in reaction to the pressure to lower prices, reducing their capital-at-risk.

Those reinsurers that have increased or managed their exposures to be almost flat are typically well-diversified reinsurers; we consider that these are probably more able to support the incremental capital cost of additional catastrophe risk exposure and thus benefit from lower technical price constraints. Where less-diversified reinsurers have adopted such strategies, the additional volatility to both their balance sheet and earnings positions may weaken our view of their risk positions, even though any score change in the short term is unlikely.

Operating Performance Has Become More Sensitive To Large Catastrophe Claims

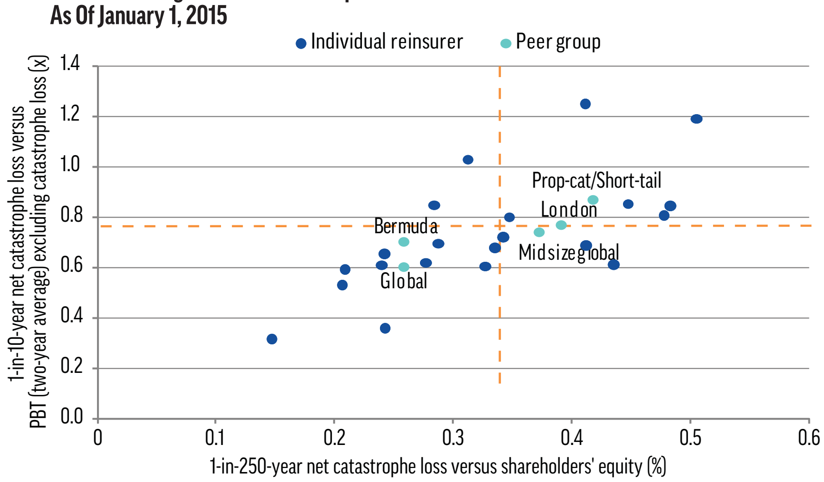
We do not expect to see investment returns rise far from their current record lows. Therefore, reinsurer profitability is increasingly sensitive to single catastrophe claims. A close analysis of the sector's 2014 results demonstrates how vulnerable its underwriting profitability is to catastrophe exposure. On average, we found that a catastrophe loss with a 19 percentage point impact on the combined ratio would cause the sector to suffer an underwriting loss (over the past five years, the average catastrophe loss had a 12 percentage point impact on the combined ratio). For most reinsurers, this means that the return period for incurring an underwriting loss is now between 1-in-10 to 1-in-20 years (see Chart 3). The average return period for an underwriting loss has increased from 1-in-25 years since year-end 2012, showing that reinsurers are more vulnerable now. We anticipate that if rates in other reinsurance lines decline further, it could also amplify the potential impact of catastrophe claims on reinsurers' overall profitability as their profit margins continue to be eroded.

High Capitalization Gives Sector Resilience Against Extreme Events

In our view, the sector has greater capacity to sustain significant catastrophe losses than ever before, following another year in which there were relatively few large claims. Capital positions have continued to improve during 2014 and the sector retains its extremely strong capital position (above the 'AAA' capital requirement). The stress tests we perform (net 1-in-10, 1-in-50, 1-in-100, 1-in-250-year shocks) against Standard & Poor's capital position show an aggregate position after a 1-in-250-year stress at "strong" (see Chart 4).

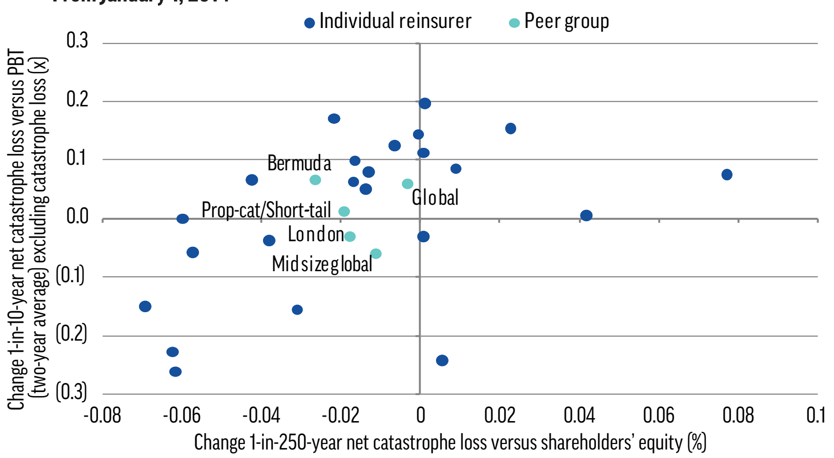
The reinsurers that appear most exposed

Chart 1: Earnings At Risk Versus Capital At Risk Positions As Of January 1, 2015



PBT: Profit before tax. Prop-cat: Property-catastrophe.

Chart 2: Earnings At Risk Versus Capital At Risk Positions Evolution From January 1, 2014



PBT: Profit before tax.

Chart 3: Reinsurers' Technical Profitability Exposure To Catastrophe Risk—Average Break-Even Probability By Peer Group

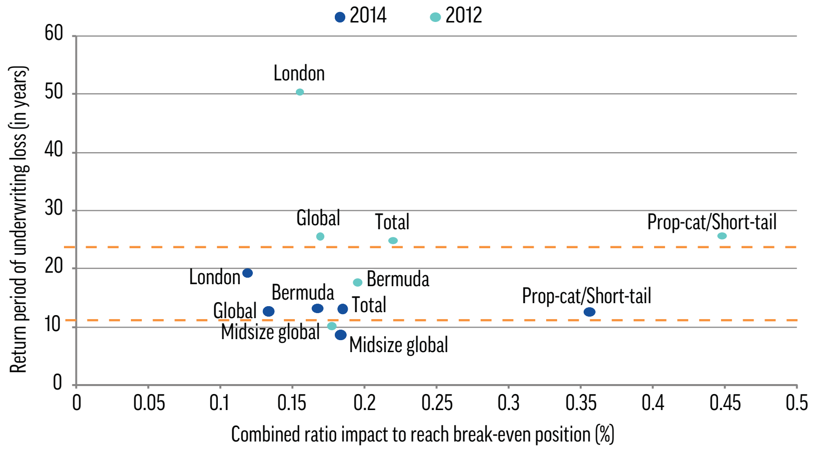


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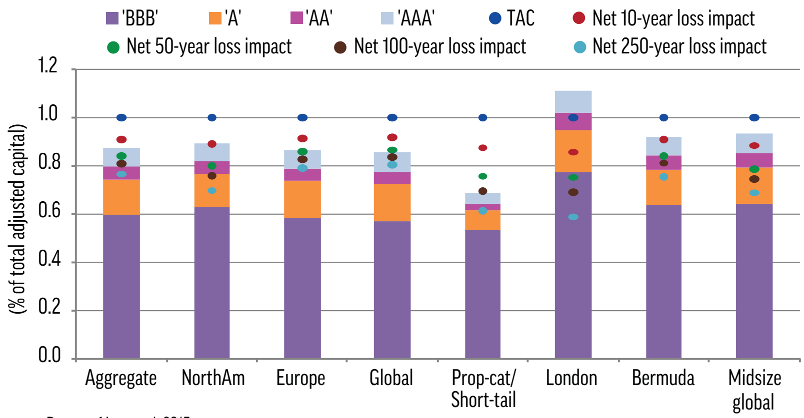
Chart 4: Catastrophe Loss Impact On Standard & Poor's Total Adjusted Capital At Different Return Periods



Data as of January 1, 2015.

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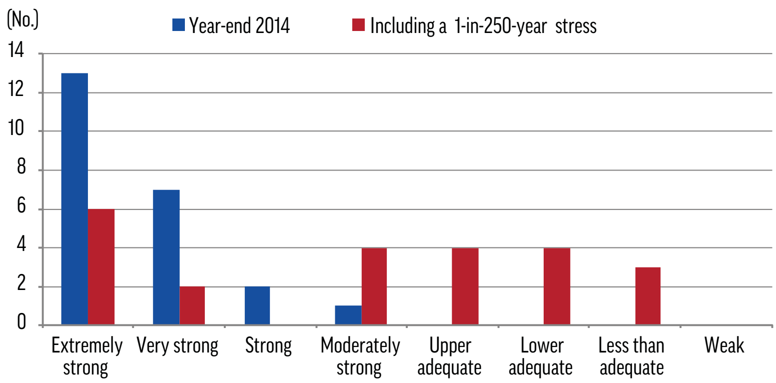
Chart 5: Global Reinsurance Sector Capitalization—After A 1-In-250-Year Aggregate Loss, Before Any Management Action



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to these extreme scenarios are London players, which demonstrate lower capital adequacy in our rating analysis, and some North American reinsurers that have larger-than-average appetites for catastrophe risk. Should an extreme loss occur, our ratings on those companies that have the weakest capital positions after the event are likely to come under the most pressure. We would expect such a company to be in a relatively weak position to be able to retain existing business and substantially benefit from any subsequent rate improvement. Such reinsurers might also find it difficult to recapitalize as shareholders may find it quicker and easier to reinvest in the market using alternative capital, such as catastrophe bonds. Meanwhile, we expect reinsurers with the strongest capital positions to sustain their capital adequacy position, even in these extreme scenarios (see Chart 5).

Using Retrocession For Tail Protection Can Optimize Returns

As of January 1, 2015, use of retrocession for tail protection (that is, to cover low-probability, high-severity exposures at a 1-in-250-year return period) across all perils had increased, reflecting the cheaper retrocession rates available globally and the increased use of third-party vehicles such as catastrophe bonds and sidecars (see Chart 6).

A similar dynamic can be seen in Chart 7, which shows the overall average increase in recoveries (at 1-in-250-year return period) to 34% from 29% in 2014. The sector increasingly relies on sound risk management approaches to improve risk-reward analysis when considering whether to remove tail risk from the balance sheet. We expect this trend to continue as an influx of alternative capital continues to weigh on retrocession prices and reinsurers seek to redeploy capital efficiently. Not surprisingly, our data show that, historically, reinsurers that mainly focus on writing catastrophe protection are more likely to take risk higher in the layers and tend to purchase more retrocession protection than the more-diversified global reinsurers.

Reinsurers Are Holding On To U.S. Windstorm Risk

At least five of the reinsurers we rate have increased their exposure to U.S. windstorm exposure by 10% or more this year. U.S. windstorm remains the largest risk, globally; on average, it comprises 32% of the global exposure, up from 30% in 2014 (currency effects also contributed to the change). We understand that most reinsurers still consider

> "The sector increasingly relies on sound risk management approaches to improve risk-reward analysis when considering whether to remove tail risk from the balance sheet."

U.S. windstorm exposure to be adequately priced, although we believe that profit margins have become razor-thin.

Conversely, rate declines in Japan, combined with worsening terms and conditions on reinsurance contracts, have encouraged most reinsurers to reduce their exposure to the region.

We consider that having a global presence might help a reinsurer to ease localized pricing pressure in competitive areas. To some extent, we expect reinsurers' risk profiles to gradually rebalance, favoring those regions where they can generate the most adequate risk-adjusted returns. That said, we recognize that significantly rebalancing risk profiles will take time and may reduce diversification (see Chart 8).

Reinsurers' Experiences Of The Softening Market Could Diverge Considerably

As reinsurance markets soften, reinsurers' attitudes to catastrophe risk are diverging. Some reinsurers are putting their faith in taking on increased catastrophe risk, while others appear to be looking to expand in other lines of business. We expect that this divide could widen as rates soften further. Those that misjudge their exposure could be left isolated after the next large event. This reinforces our view that discipline is necessary as reinsurers face difficult strategic decisions when adjusting their exposure to falling catastrophe rates.

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Chart 6: Average Tail Protection By Peril
(% Recoveries At 1-In-250-Year Return Period)

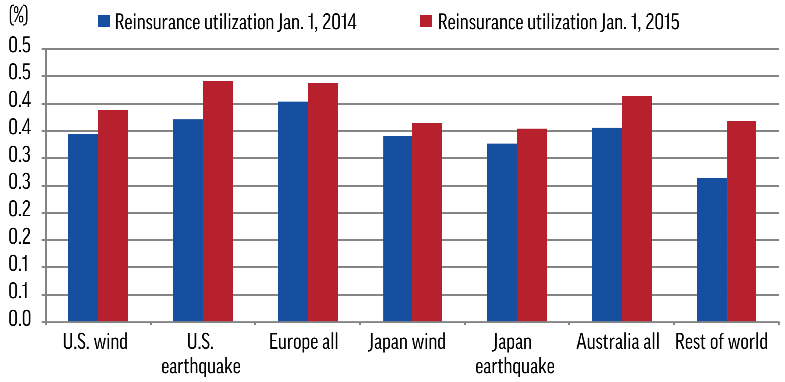


Chart 7: Average Tail Protection By Peer Group
(% Recoveries At 1-In-250-Year Return Period)

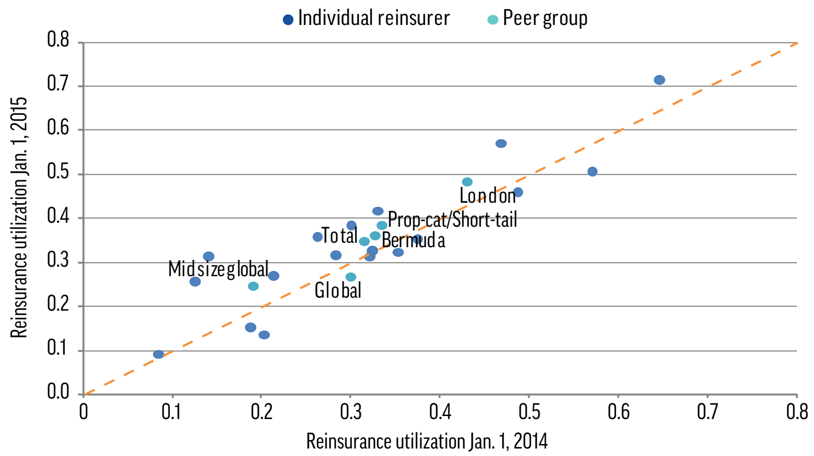
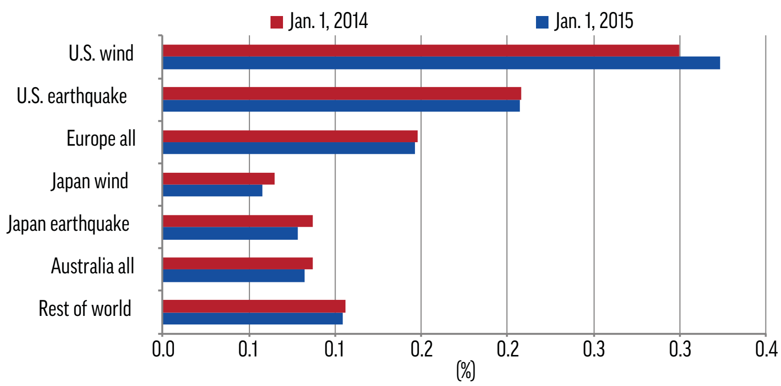


Chart 8: Reinsurers' Average Global Exposure Profile
At A 1-In-250-Year Return Period (Undiversified Exposure)



Asset Risk For Reinsurers Nudges Higher As Low Yields Continue To Bite

SHUTTERSTOCK / O.BELLINI

By Anvar Gabidullin and Mark Button

As reinsurers search for ways to offset pricing declines and low yields, the continued strength of its capital positions means the sector can meet additional capital requirements arising from further increases in exposure to risky assets. A similar increase in equity assets over the course of 2015 would reduce capital adequacy but should not be a cause for concern.

Ultra-low interest rates and compressed credit spreads are diminishing returns on fixed-income portfolios for insurers and reinsurers alike. Standard & Poor's Ratings Services has observed a 30% reduction in average net investment yield over the past four years for our global reinsurance peer group of 24 companies, collateral damage from accommodative central bank monetary policy since the global financial crisis. This means that reinsurers are more dependent than ever on generating profits from their insurance underwriting to deliver their targeted return on equity.

In response, companies are increasingly looking at ways to halt the decline and, indeed, bolster their investment income. Reinsurers are considering their options, such as increasing credit or liquidity risk, lengthening asset durations, or increasing their allocations to higher-risk assets such as equities. This search for yield, however, comes at the expense of deploying greater amounts of risk capital to mitigate the potential volatility in asset values.

In fact, over the past 12 to 18 months, we've seen an increase in exposure to higher-risk assets within reinsurers' portfolios. However, the increase is moderate and the overall exposure is generally still within reinsurers' risk tolerances. Plus, higher asset values across the investment spectrum are giving pause to chief investment officers. The MSCI World Index is up 20% in the past 12 months, and over 100% since the 2009 market trough, while interest rates remain only slightly off their historic lows.

Reinsurers Take Limited Duration And Liquidity Risk

Most reinsurers generally have a robust investment framework with close matching of assets and liabilities, particularly for the core/strategic portfolio of assets backing their insurance liabilities. Investment risk is often higher in the tactical portfolio of assets backing shareholder funds.

In terms of asset duration, in anticipation of likely interest rate increases in the U.S. and the U.K., reinsurers are generally refraining from increasing their portfolio duration, to reduce the risk of locking into low rates. We have found that the average duration for the reinsurance peer group remained stable at about 3.1 years in 2014 and 2013. This compares with an average liability duration of about 3.6 years, although the range is wide—about two years for short-term property catastrophe-focused companies and more than five years for reinsurers with longer-tail casualty exposure.

Although the average asset duration has remained relatively stable for the peer group over the past 12 months, a quarter of the peer group has increased their asset duration by a year or more over the past 24 months. This will increase their exposure to a rise in interest rates, which we expect to happen gradually over the next two years.

We're also seeing that reinsurers have limited appetite for taking on significant liquidity risk, possibly through investing in real estate, infrastructure, or other less-liquid long-dated investments. That's because of the shorter duration and less predictable nature of their liabilities relative to primary life insurers, particularly for reinsurers exposed to material catastrophe risk. Reinsurers have kept the proportion of real estate assets in their portfolios at less than 5%. Investment professionals at a number of reinsurers have expressed to us their interest in infrastructure as an asset class, in theory. However, competition for these investments has skyrocketed over the past 12 months, driving prices to a level that makes infrastructure unattractive in practice.

Regulatory capital requirements are also significantly shaping asset allocation decisions. For example, in Europe, ahead of the Solvency II regulatory framework that comes into effect on January 1, 2016, European reinsurers are likely to review the risk-return profile of their investment portfolio to ensure efficient deployment of capital resources.

Credit Risk Exposure Is Generally Stable

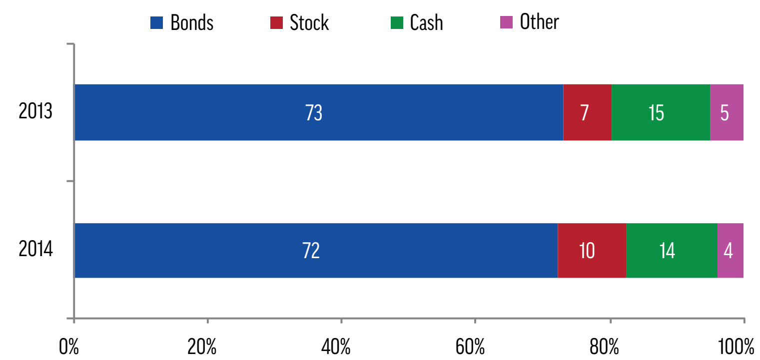
Reinsurers' portfolios are positioned relatively prudently, with about 72% of their assets held in fixed-income instruments at year-end 2014 (see Chart 1). Our data show that the sector's aggregate exposure to credit risk has remained stable year on year; the average rating of bond portfolios has stayed at 'AA-'. The proportion of fixed-income investments with a rating of 'BBB' or better has remained at about 94%. The average credit risk charge in our capital model is broadly unchanged, according to our estimates.

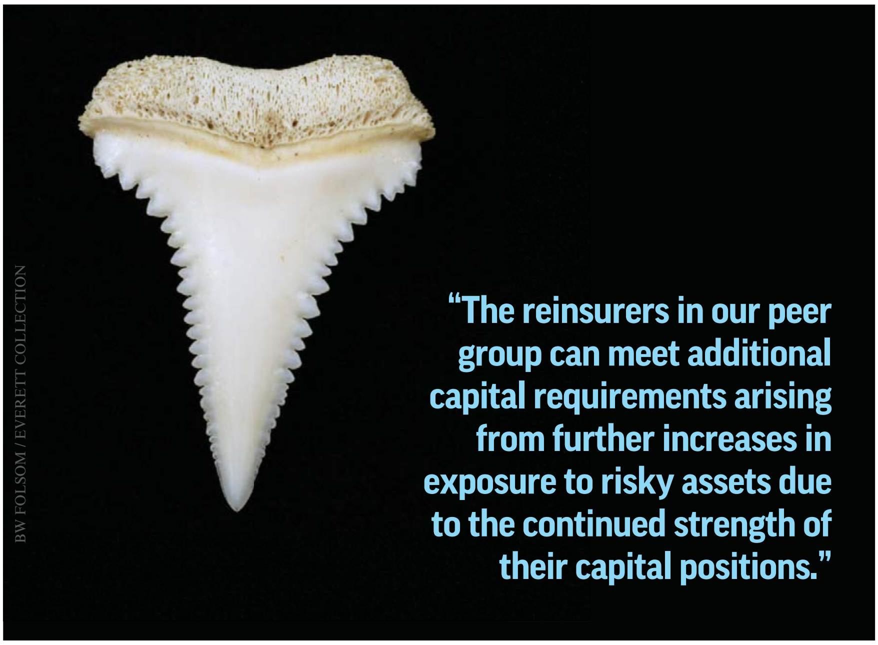
Some subgroups have taken on a bit more risk than others. Property-catastrophe short-tail specialists had a somewhat higher proportion of speculative-grade and unrated debt, at 12% (14% in 2013), than the industry as a whole. However, these players have offset this by increasing their proportion of 'AAA' debt over the year, effectively creating a 'barbell' approach to their credit exposure. We also note that, on average, the London-based reinsurers have moved down the credit curve in their fixed-income portfolios, increasing their exposure to 'A' rated issuers by 5% and unrated issuers by 1% at the expense of 'AA' rated (-4%) and 'AAA' rated (-2%) securities. This change in credit risk profile is only marginal, in our view.

Equity Exposure Has Nudged Up

The proportion of equity holdings in reinsurers' asset portfolios increased to 10% in 2014 from 7% in 2013, indicating a material increase in market risk exposure,

Chart 1: Investments By Asset Class





albeit from a modest base. Although equity appreciation accounts for some of the increase, most comes from reinsurers reallocating funds into equities from other asset classes. That said, we believe that overall investment leverage has remained moderate. We found that the proportion of higher-risk assets—equities, real estate, and speculative-grade fixed-income exposure—stayed at less than 30% of capital for the global reinsurance peer group in 2014.

The emergence of the hedge fund reinsurance model, where companies aim to combine their underwriting portfolio with a hedge fund investment strategy, typically seeks to take more aggressive bets across a wider spectrum of asset classes. While targeting higher investment returns, it also typically results in higher volatility and a higher risk of material investment losses.

Reinsurers’ Capital Strength Sustains Their Investment Risk Exposure

We reflect exposure to riskier assets in our ratings analysis through our assessment of capital adequacy and risk position, where we analyze the proportion of higher-risk assets relative to capital. An increased allocation to riskier assets may bolster returns, but puts additional strain on capital.

We generally believe that the reinsurers in our peer group can meet additional capital requirements arising from further increases in exposure to risky assets due to the continued strength of their capital positions. We estimate that a similar increase in equity assets over the course of 2015 should be easily absorbed, given the current average redundancy to ‘AAA’ of 6%.

Investment Yields Are Likely To Improve, But Only Marginally

We don’t expect a material recovery in investment income. Standard & Poor’s economists expect interest rates to remain low at least until 2017 (see Table 1). We expect net investment yields (excluding realized and unrealized gains/losses) for reinsurers to improve in 2015–2017, but only by up to 50 basis points; they will remain well below the historical norms.

We do not expect a significant widening of credit spreads in the next two years. In 2014, despite considerable geopolitical turmoil, the ending of the U.S. Federal Reserve’s monthly asset purchases, and the steep decline in the price of oil, corporate borrowers fared very well by historical standards. In the full year, 60 global corporate issuers defaulted, considerably lower than the 81 in 2013, and the lowest number since 2011. That said, continued external risks, such as geopolitical tensions and central bank monetary policy, add to the potential for volatility in returns, and hence investment losses. In addition, the likely turn of the interest rate cycle in the U.S. and U.K. could lead to unrealized losses on bonds. We therefore believe that reinsurers need to maintain their current capital strength to absorb potential volatility. ■

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Table 1: 10-Year Bond Yield

	Yearly Average (%)							
	Germany	France	Italy	Spain	Netherlands	Eurozone	U.K.	Switzerland
2013	1.6	2.2	4.3	4.6	2	3	2.4	1
2014	1.2	1.7	2.9	2.7	1.5	2	2.6	0.7
2015(f)	0.6	0.9	1.9	1.8	0.7	1.3	2	0.1
2016(f)	1.2	1.4	2.3	2.3	1.2	1.7	2.6	0.4
2017(f)	1.6	1.9	2.8	2.8	1.9	2.2	3.1	0.9

f: Standard & Poor’s forecast. Source: Standard & Poor’s.

Are Alternative Capital And Reinsurance Two Sides Of The Same Coin?

By Maren Josefs and Gary Martucci

Capital has been flowing easily into this space and the benign natural catastrophe losses during the past few years lead us to expect the alternative capital market to continue to innovate and push boundaries, but growth should not come at the expense of looser underwriting discipline and less due diligence.

SHUTTERSTOCK / KHAKIMULLIN ALEKSANDR

The boundaries between alternative and traditional capital keep blurring. The reinsurance sector is adapting to this influx of alternative capital more by providing innovative solutions and lower prices to reinsurance purchasers.

Currently there is about $24 billion in catastrophe (cat) bonds outstanding. So far this year more than $5 billion of cat bonds has been issued, of which Standard & Poor's Ratings Services has rated $1.30 billion (see Table 1).

Thus far in 2015, the issue amount of publicly placed cat bonds has not been as strong as in 2014, and there has been an increase in the use of private cat bonds ("cat bond lite") and collateralized reinsurance. In total, Aon Securities Inc. estimates alternative capital invested in the reinsurance market at $66 billion as of June 30, 2015, up from $59 billion (12%) as of June 2014. Although the progression may not be linear, during the next few years, we believe the cat bond market will continue to grow—by 10% to 20% per year—as investors accept new risk models assessing perils across the globe (on at least a parametric basis). For us, there's no reason to think this market is going away any time soon.

The Market Is Not For Re/Insurance Companies Only

We have seen an extended use of cat bond structures not only by re/insurance companies but also by local government-sponsored agencies in the U.S. and other sovereigns or cross-country catastrophe funds. According to the weighted average of the rate online that single-peril bonds have paid in different states, issuers generally have achieved cost savings by issuing cat bonds (see Chart 1). In Florida, the rates online for storm protection have remained stable during the past year and we have seen

Table 1: July 2014–July 2015 Rated Insurance-Linked Securitizations

Transaction name	Cedant	Series	Class	Term (years)	Issuance amount (mil. $)	Covered peril	Covered region	Rating	Interest spread	Multiple to expected loss
Golden State Re II Ltd.	State Compensation Insurance Fund	2014-1	A	4.3	250	Earthquakes	California	BB+	TMM + 220 bps*	8.8
Kilimanjaro Re Ltd.	Everest Reinsurance Co.	2014-I	C	5	500	Earthquakes	U.S. and Canada	BB-	TMM + 375 bps	2.57
Chesterfield Financial Holding LLC	RGA Reinsurance Co.	2014-1	A	20	300	Embedded value		A-	450 bps	N/A
Vitality Re V Ltd.	Aetna Life Insurance Co.	2015-I	A	3	140	Medical benefits claims	U.S.	BBB+	TMM + 175 bps	175
Vitality Re V Ltd.	Aetna Life Insurance Co.	2015-I	B	3	60	Medical benefits claims	U.S.	BB+	TMM + 210 bps	8.75
East Lane Re VI Ltd.	Certain member companies of Chubb Corp.	2015-I	A	5	250	Named storms, earthquakes, severe thunderstorms, winter storms, volcanic eruptions, meteorite impact, and wildfire	U.S.	BB	TMM + 375 bps	3.02
Kizuna Re Ltd.	Tokio Marine & Nichido Fire Insurance Co. Ltd.	2015-1	A	4	289	Earthquakes (including tsunamis and volcanic eruptions if caused by an earthquake)	Japan	BBB-	TMM + 200 bps	111.11
Benu Capital Ltd.	Axa Global Life, France		B	4.7	163	Extreme mortality	France, Japan, and U.S.	BB	3m EURIBOR - 43.5 bps (floored at zero) + 255 bps	N/A
Benu Capital Ltd.	Axa Global Life, France		A	4.7	147	Extreme mortality	France, Japan, and U.S.	BB+	3m EURIBOR - 44.5 bps (floored at zero) + 335 bps	N/A
Everglades Re Ltd II	Citizens Prop Ins. Co.	2015-I	A	3	250	Named storms	U.S.	BB-	TMM + 515 bps	3.93

N/A: Not applicable. *bps: basis points

Florida companies take advantage of the lower premiums by buying more protection.

In addition, we have rated the California State Compensation Insurance Fund's $250 million bond, which covers potential workers' compensation claims triggered by an earthquake loss (see Golden State Re II Ltd. 2014-1 Class A Notes, published Sept. 16, 2014, on RatingsDirect). China Property and Casualty Reinsurance Co. dipped its foot in the cat bond market by issuing a $50 million bond providing coverage on an indemnified basis from earthquakes in China. We expect to see further issuance from initiatives such as Flood Re in the U.K., the African Risk Capacity in Africa, and other governments such as New Zealand that see the benefits of transferring the financial risk of natural catastrophes into the capital markets before the event happens.

The Definition Of A Covered Peril Is Changing And Terms Are Widening

Besides hurricane risk (e.g., hurricanes [including named tropical storms], typhoons, cyclones), earthquake risk is one of the prominent risks to be transferred using cat bonds. Cedants are looking for protection, and this year, there were issuances providing coverage against earthquakes not only in the U.S., Japan, and China, but also in Italy and the Caribbean. The latest bond coming to market will cover earthquake risk in Turkey.

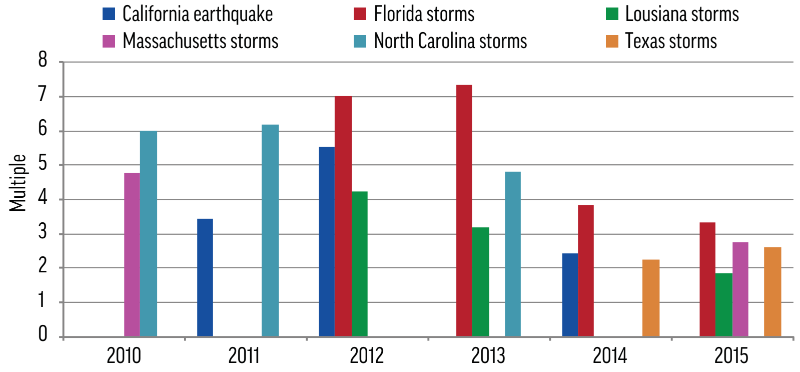
In addition, volcanic eruptions, meteorite impact, and wildfire (outside of California) were included in some transactions as new covered perils. For these types of peril, modeling is an issue. The probability of these events occurring has been for the most part calculated deterministically, and is very small (e.g., the 1908 meteor strike in Siberia is considered a one-in-1,000-year event and the likelihood of a similar event affecting the covered area of a bond is even more remote). Under the current market conditions, cedants found it easier to buy protection for these perils and align the coverage with traditional reinsurance contracts.

Event definitions have expanded as well. For example, a recent transaction widened the event definition for named storms and earthquakes in the U.S. by increasing the duration of the event to 240 hours, from 168. Expanding the time clause in the event definition is common in a soft reinsurance market.

Issuers have also been testing the market by lengthening and shortening the maturities of their issuances. Five-year issuances are no exception, although a seven-year maturity deal failed to be placed, but a six-month deal covering one hurricane season was placed successfully.

A further sign that the insurance-linked securities (ILS) market is currently a buyer's market is the inclusion of early termination provisions, which make the terms and conditions more flexible for the issuer. This is in addition to the variable reset options that have been part of most issuances for the past two years. Most issues that started using the variable reset have had their first resets by now, and cedants have used the optionality to adjust the layers to better fit into their annual protection buying.

Chart 1: Weighted Average Multiple Over Expected Loss By Single Peril And Single State



This chart includes information from Bloomberg and Artemis for issues not rated by Standard & Poor's.

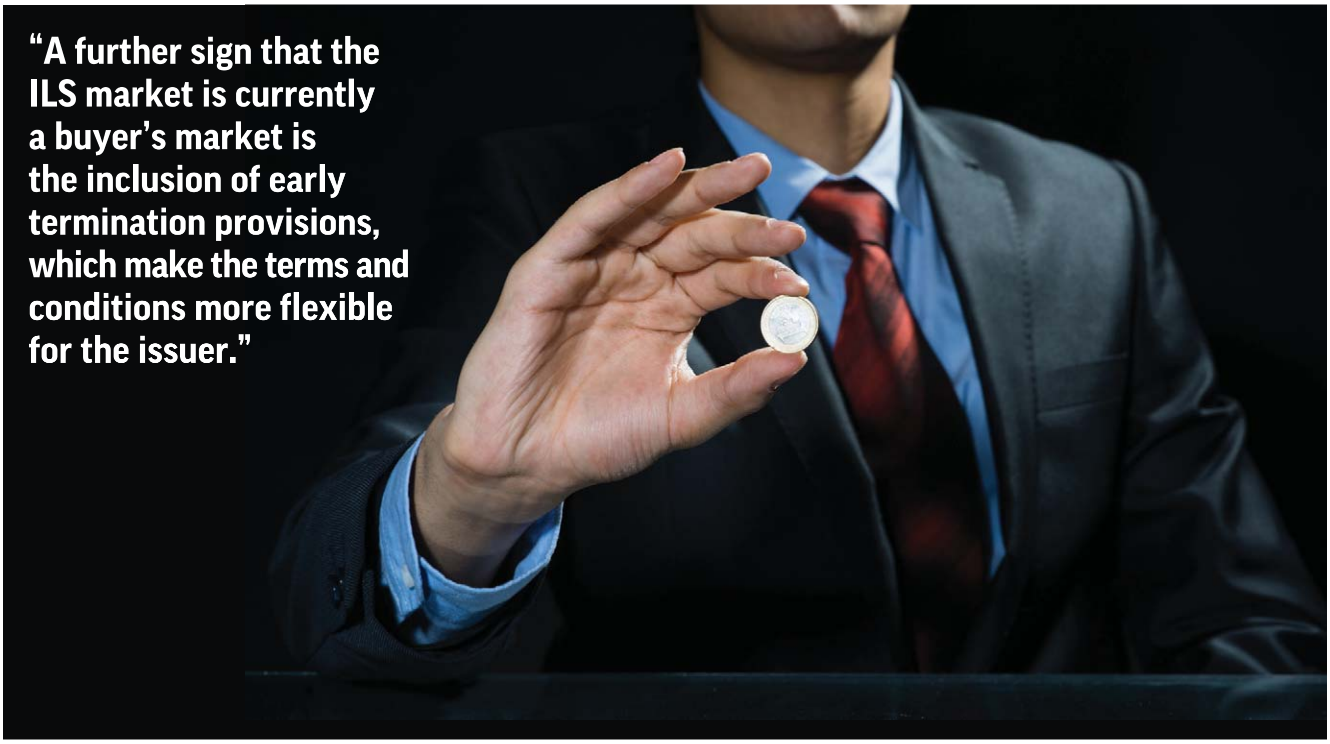
Are Risks And Returns Being Assessed Prudently?

We continue to see a drive to reduce costs and increase speed of execution to connect risks with appropriate counterparties. As everyone tries to jump on the reinsurance bandwagon, is there a risk of the ILS market overheating and new investors getting burned? Our main concerns in the long-term remain the lack of liquidity compared to other asset classes (although it is improving, we are not sure there will be much left immediately before and after a big event), investors' understanding of the risks they are underwriting using thorough due diligence (such as running own-risk analysis and reviewing legal contracts), and an increasing demand for diversifying perils that might push rates and returns lower than the technical price should be.

Many of the diversifying perils do not even make it into the tradable cat bond format, as sophisticated investors value the illiquidity premium they can earn by writing the same risks via collateralized reinsurance contracts or private cat bonds. It is our understanding that several large ILS fund managers declined to participate in the new diversifying deals with a low coupon of around 2% (which market observers argue to be a minimum return target for ILS investors). However, for some funds, the coupon on these issues does not provide enough return to compensate for the risk they would take, which includes immense uncertainty in modeling.

Nevertheless, these bonds are being placed successfully. This leads us to conclude that there are investors for whom the diversification benefit is more important than the return they will earn. If these end investors are pension funds, the long-term effect should not be of any concern for the whole market. But if these are opportunistic investors, a portion of this capital could leave the market once yield on other assets increases.

In addition, more structures are coming to market where investors do their own risk modeling and the risk analysis is no longer part of the security offering documents. Sophisticated ILS funds have always been able to perform their own risk analysis. But how are new investors accessing the market? If their capital is flowing into the market through the ILS funds, they do not necessarily need in-house modeling. However, some investors might follow the lead of other ILS funds when making



investment decisions. In this case, they might be missing certain aspects of the risks they are buying into and might cause market disruptions once they incur losses.

We believe that one of the reasons the ILS market was less affected by the financial crisis was that unlike for other asset classes, a third party provided an independent risk analysis and a higher degree of due diligence. Ratings were an additional benefit in the due diligence process, especially from a pricing and structural standpoint and in the review of the transaction documents to ascertain that these structures adhere to our criteria. Trends to reduce issuance costs and shorten the time to market by placing deals without third-party due diligence are a further indication that the level of scrutiny might be diminishing. In addition, the spectrum of instruments in which ILS funds with guidelines to invest in rated instruments only can invest is becoming less diversified, restricting their investment opportunities. What this will mean in practice will be seen only in the aftermath of a big natural catastrophe that affects a number of bonds.

There Is Room For Non-Property/Casualty Issuance As Well

Although most of the disruption caused by the alternative capital inflow occurred on the property-catastrophe reinsurance side, there has also been some activity on the life side in the past 12 months. We rated the principle-at-risk notes issued by Benu Capital Ltd. that provide AXA Global Life with protection against extreme mortality in France, Japan, and the U.S. (see Benu Capital Ltd. published April 24, 2015), and the notes issued by Chesterfield Financial Holdings LLC (see Chesterfield Financial Holdings LLC, published December 16, 2014) that allowed Reinsurance Group of America Inc. to capture a portion of the profitability from a specified block of life insurance business (embedded value or value-in-force [VIF]). VIF securitizations could be a future source of capital (or capital relief) for insurance companies. These securitizations tend to be long term, and since the financial crisis, investors in the insurance sector have tended to shy away from issuances with maturities longer than three to five years.

Chesterfield Financial was the first VIF transaction we rated in the past two years and although it had a 20-year maturity, the expected life was between six and seven years. For investors to gain interest in these transactions, we believe sponsors will have to minimize asset risk and have the primary risk transferred to investors to be related to the covered business. Because most investors have significant credit risk, an asset with primarily insurance risk could be attractive to them, even with longer terms to maturity. There are insurance companies with mature large blocks of business that could find accessing the capital markets a viable way to raise capital, in our opinion.

The past 12 months have also seen a lot of activity in the placement of private longevity swaps between corporate pension funds and large life reinsurers or banks. We believe that it is now only a question of time until we see a deal trying to access the capital markets, too.

Growth Will Continue, But Caution Is Needed

Given the ease and efficiency with which capital has been flowing into this space and the benign natural catastrophe losses during the past few years, we expect the alternative capital market to continue to innovate and push boundaries, which will ultimately transfer into the cat bond market. As we welcome this innovation, we continue to caution that any growth should not come at the expense of looser underwriting discipline and less due diligence. ■

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Property/Casualty Reinsurers With Strong Reserve Margins Are In A Better Position To Withstand The Prolonged Soft Market

SHUTTERSTOCK / DUDAREY MIKHAIL

By Olivier Karusisi and Miroslav Petkov

After the next big catastrophe event, reinsurers that were prudent in how they handled reserves could see less volatility in their annual results, but if they have consumed a significant proportion of their reserve surplus to protect profits in recent years, their financial risk profile might be in danger.

Price competition for global property/casualty (P/C) reinsurers has been fierce for the past few years and Standard & Poor's Ratings Services sees no signs of the trend reversing course in the near future. An abundance of third-party capital also increases the sector's capacity. As a result, margins have become tight enough to strain reinsurers' ability to maintain their market positions while remaining profitable.

The problem has been exacerbated by the low investment returns seen in recent years. While returns were strong, many reinsurers balanced tight underwriting margins, or even technical losses, against the income from their investments. Since the market started softening in 2007, we have observed that some global reinsurers have supported their combined ratio by releasing more of their reserves instead. (Lower combined ratios indicate better profitability. A combined ratio of greater than 100% signifies an underwriting loss.)

Conservative Reserving Offers A Long-Term Competitive Advantage

We expect those reinsurers that chose to retain prudent reserves for longer to have maintained a cushion on which they could draw. Those that released reserves more quickly, by contrast, may find that they have exhausted their ability to support current reported profits from past reserves. In our view, the market is still soft enough that those who raise rates first might not find the rest of the market following suit; they would therefore likely lose market share.

The wide disparity in terms of reserve releases practiced by P/C reinsurers makes it difficult to compare their underwriting results (see Chart 1). Over a reinsurance cycle, we expect reinsurers that use conservative reserving practices to generate more stable underwriting results. We attribute the lack of spikes in their releases to the fact that conservatively reserved companies will likely take longer to release prior period reserves when there is strong evidence of positive claims development. Conversely, more aggressive reinsurers realize favorable reserve development sooner and then experience more reserve volatility over time.

In recent years, more companies have been quicker to realize those reserves. Given that reinsurers may be offsetting current-year losses against reserve releases, their reserving strategies affect their current-year reported performance. Therefore, we consider that reinsurers with strong reserve margins will experience less volatility in their financial results and at the same time will be able to maintain their respective market positions.

Standard & Poor's identifies two sources of favorable reserves development in the reinsurance sector.

Reserve prudence in respect of catastrophe losses

Natural catastrophe losses tend to be settled over just two to four years, a relatively short period of time. This allows reinsurers to release reserves for claims where the booked amount is higher than the settled amount. Therefore, the 2011 and 2012 catastrophe claims are currently maturing, which we think partially explains the increase of reserve releases in recent years.

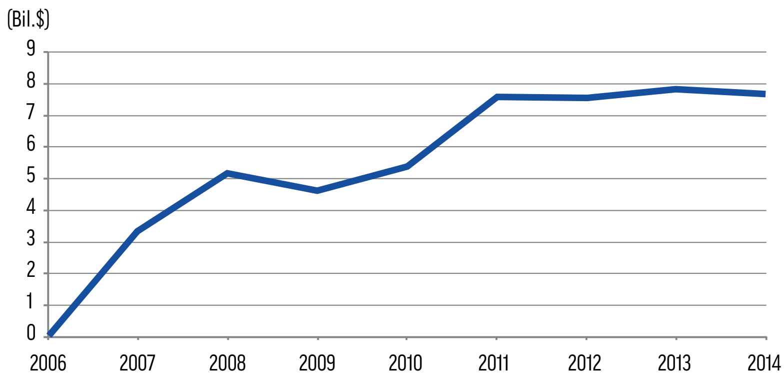
That said, any major catastrophe event is likely to carry reserve uncertainty, such as exposure to inherent political risk. As we saw after the New Zealand earthquakes in 2010–2011, natural catastrophe claims can also take longer than expected to fully mature. For example, in New Zealand, uncertainty regarding reserve adequacy assessments increased because of the various wordings used in different policies and after several court rulings on land zoning, which defines the type of settlement (for example, cash or repair).

Going forward, we expect a reduction of reserve releases attributable to natural catastrophe events, because there have been relatively few catastrophe claims in 2013 and 2014.

Few shocks in long-duration lines of business in recent years

In these lines, which include third-party liability, reserve releases are generally linked to fairly longstanding claims as loss developments tend to develop slowly over time. For example,

Chart 1: Reserve Releases In The Reinsurance Market



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> "In response to the softening market, reinsurers have eased their terms and conditions in long-duration lines, but we anticipate that the effect of the changes will take time to emerge."

there may be long delays before court rulings are available or settlements may be larger than previously expected. In recent years, the reinsurance sector has experienced very few shocks that led to major unfavorable claims development.

In response to the softening market, reinsurers have eased their terms and conditions in long-duration lines, but we anticipate that the effect of the changes will take time to emerge.

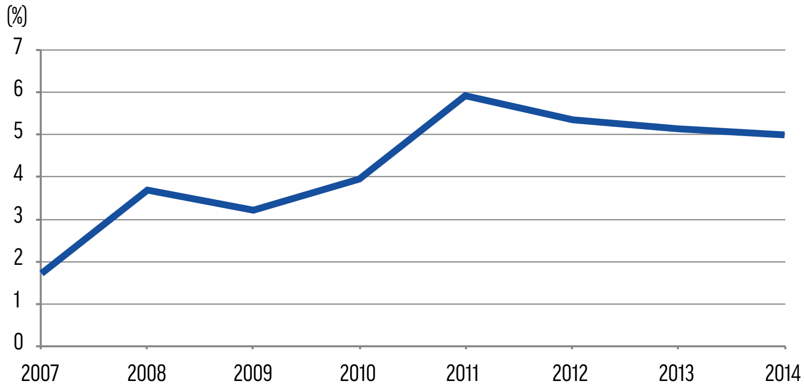
There Is A Degree Of Subjectivity In Determining Reserve Adequacy

The contribution of reserve releases to the market's combined ratio has steadily increased since 2007, although it dipped slightly in the past few years (see Chart 2). However, the historical pattern of reserve releases may be of limited use in assessing reserve adequacy because the amount of loss payments may diverge, in some cases significantly, from estimated figures. Hence, we consider it best to include an in-depth analysis of a company's claims history and exposures when assessing its reserve adequacy.

Standard & Poor's uses companies' data and various actuarial methodologies, as described in our criteria, to conduct our in-depth reserve analysis within the reinsurance sector (see "Assessing Property/Casualty Insurers' Loss Reserves," published on November 26, 2013). We have observed a wide range of reserve margins between 0% and 15% of the P/C booked reserves we analyzed.

Based on our analysis, we anticipate that after the next big catastrophe event or liability shock, reinsurers that were prudent in how they handled reserves could see less volatility in their annual results. However, if they consume a significant proportion of their reserve surplus in protecting their reported profit, we would consider their financial risk profile had been eroded.

Chart 2: Impact Of Reserve Releases On The Market Combined Ratio



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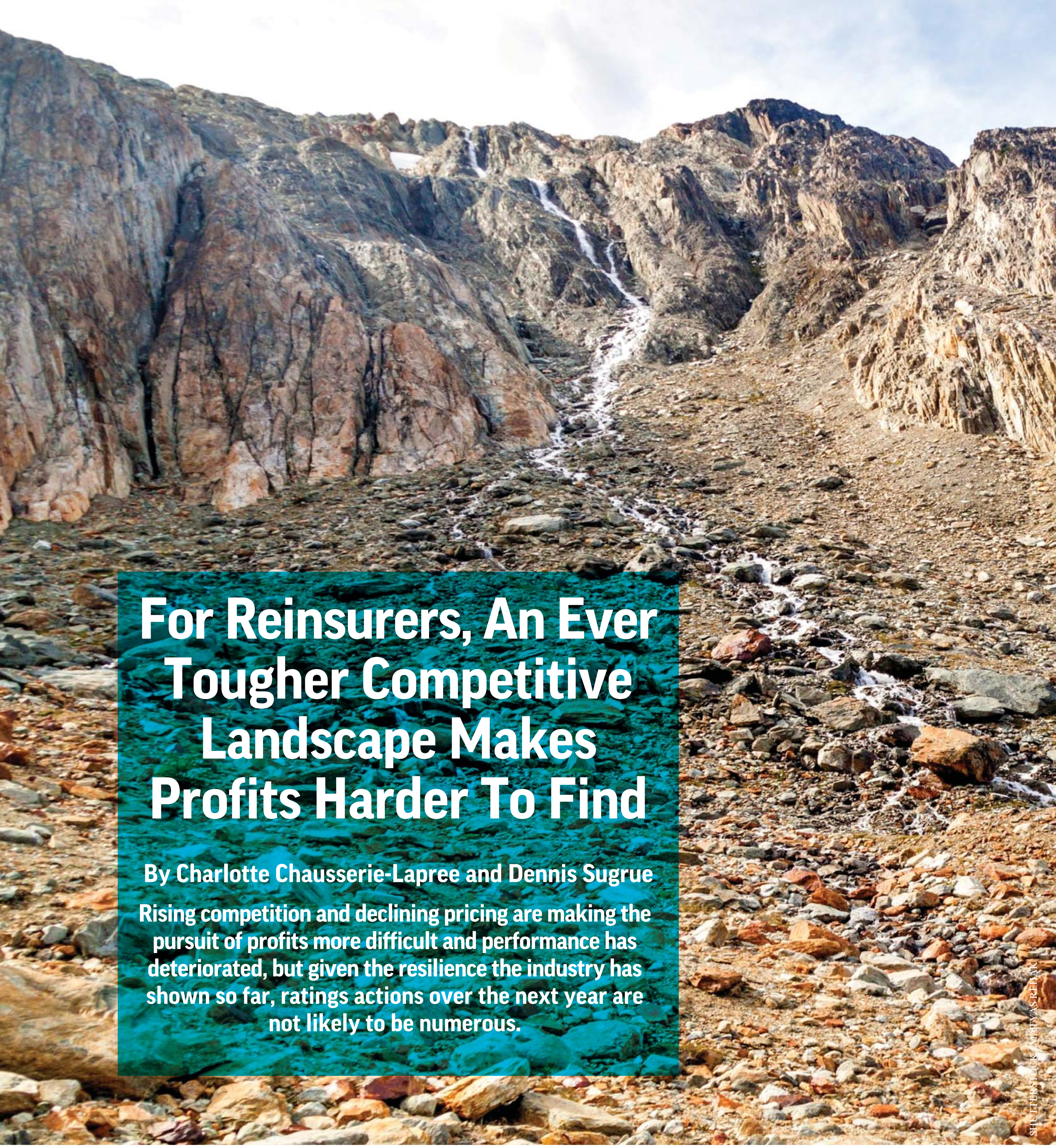


For Reinsurers, An Ever Tougher Competitive Landscape Makes Profits Harder To Find

By Charlotte Chausserie-Lapree and Dennis Sugrue

Rising competition and declining pricing are making the pursuit of profits more difficult and performance has deteriorated, but given the resilience the industry has shown so far, ratings actions over the next year are not likely to be numerous.

SHUTTERSTOCK / MATYAS REHAK

Standard & Poor's Ratings Services continues to see negative credit conditions for the global reinsurance sector. With competition increasing among traditional reinsurers and alternative players, and with capital levels remaining at record highs, pricing continues to decline. That's making it ever more difficult to generate sustainably strong profits. But that doesn't mean the industry faces an inevitable round of credit-damaging losses.

Our analysis of peer groups within the reinsurance sector confirms that despite these tough conditions, reinsurers are taking defensive actions to protect themselves. Given our belief that these actions have been mostly effective and have boosted the industry's resilience, we expect few rating actions in the sector over the next 12 months.

Of course, not all players will fare equally. Reinsurers that are well capitalized, diversified, and able to offer significant capacity to clients are best positioned to navigate this tricky landscape. Those that can adapt and remain relevant to their clients should be able to meet return targets. Others will struggle to generate returns and defend their competitive position, and they could become takeover targets as the industry further consolidates.

Persistent Pricing Declines May Affect Reinsurers' Competitive Positions

The industry continued to chalk up materially lower rates through the major renewal dates in 2014, with price declines of 10% to 20% in many lines of business around the world (see "Defensive Plays Help Global Reinsurers To Maintain Resilience As Credit Conditions Remain Negative"). Our analysis of reinsurers' business mix and reinsurance and retrocession purchasing indicates the industry is taking actions to reduce the impact of these pricing declines. On the whole, we see a shift away from excess-of-loss business to proportional reinsurance or primary business, where price declines are much more muted.

Reinsurers are also taking advantage of low catastrophe rates by buying more retrocessionary coverage and passing on the rate declines to their retrocedants. Over 2014, we observed an average increase in purchase of protection for tail events (that is, extreme events in the "tail" of the distribution curve) to 34% in 2014 from 29% in 2013.

Underwriting Margins Are Deteriorating, But Reserve Releases Still Have A Positive Impact

Headline earnings for the reinsurance sector were strong again in 2014, continuing the trend of the last few years. But a closer look shows performance has been deteriorating across the sector since 2012. The pain isn't going away because we expect to see further premium rate declines, and we anticipate that earnings will continue to weaken.

Reported earnings in 2014 were very much in line with 2013's strong results, with the industry generating a weighted average combined ratio of 90.5% in both years (the more the combined ratio is below 100%, the higher the level of profitability). The five-year average combined ratio has been a very strong 91.5%. Reinsurers' results benefited from benign catastrophe losses, which accounted for only 2.6 percentage points (ppts) and 4.3 ppts of the average combined ratio in 2014 and 2013, respectively. The five-year average is 12.1 ppts.

Additionally, reserve releases have benefited the group's combined ratio by an average of 8 ppts over the last five years, with 2014 and 2013 releases accounting for 8.1 ppts and 7.5 ppts of combined ratio improvement, respectively (see Chart 1). 2014 has reversed a trend of decreasing benefit from reserve releases since 2010.

However, the impact of increased reserve releases masks the deterioration of underwriting results. If we adjust reinsurers' combined ratios by adding back reserve releases and the removing impact of catastrophe losses, it shows these underlying results have deteriorated since 2012 (see Chart 2). On this basis, we estimate an adjusted combined ratio of 96.0% in 2014, 5.5 ppts worse than the 90.5% average reported figure. This adjusted result is in the upper end of our forecast range for the sector's adjusted combined ratio that we published in September last year (see Table 1).

Many of the reinsurers that have benefited greatly from reserve releases in recent years are those with significant catastrophe exposure. This is to be expected because uncertainty concerning catastrophe losses and the reputation risk associated with being a negative outlier in a catastrophe event typically lead to initial reserve estimates that are well above the

Table 1: 2014 Adjusted Combined Ratio

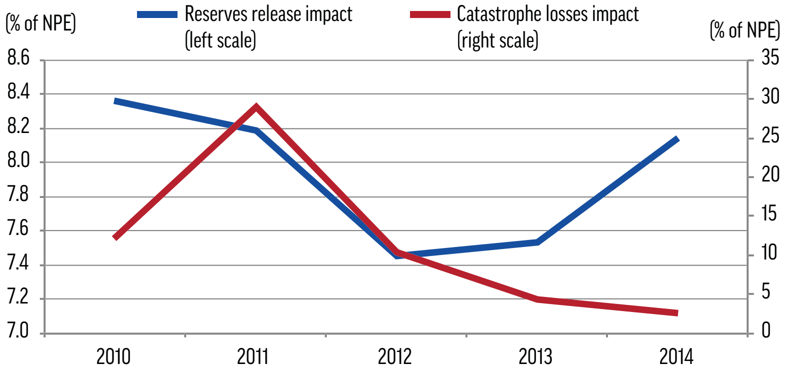
	Standard & Poor's forecast	Actual
Reported combined ratio	95-100	90.5
Less: Catastrophe losses	10	2.6
Add: Reserve releases	6	8.1
Adjusted combined ratio	91-96	96.0

Table 2: Reinsurance Industry Aggregate Standard & Poor's Capital Charges at 'AAA' Stress Scenario

	$mil.							
	TAC	Assets	Premium	Reserves	Catastrophe	Liability	Diversification benefit	Diversified RBC
2014	231,542.9	66,560.9	46,420.1	55,103.1	26,762.2	153,448.8	(17,553.2)	202,456.5
2013	220,733.0	69,600.8	42,323.0	54,509.6	27,418.2	145,917.7	(16,582.5)	198,936.0
Year-on-year change (%)	4.9	(4.4)	9.7	1.1	(2.4)	5.2	5.9	1.8

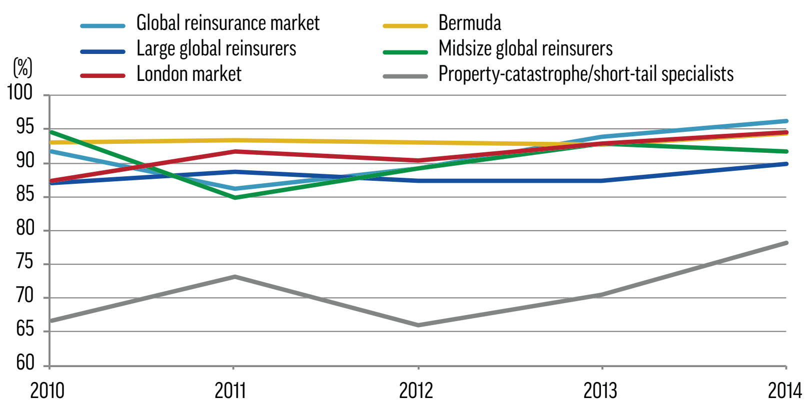
TAC: Total adjusted capital. RBC: Risk-based capital.

Chart 1: Historical Impact Of Catastrophes And Reserve Releases On Combined Ratios



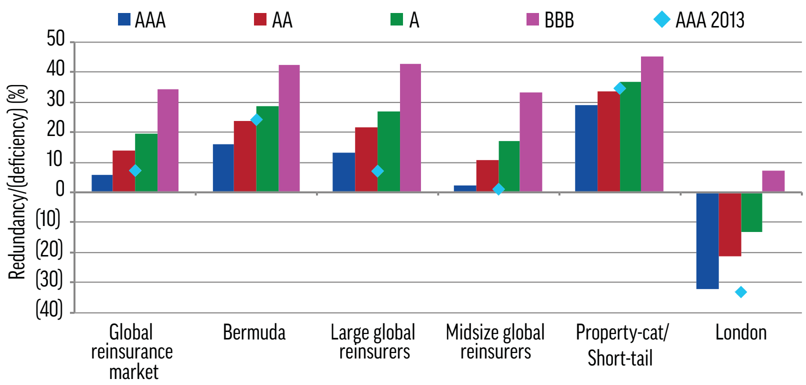
NPE: Net premium earned.

Chart 2: Combined Ratios Excluding Catastrophe Losses And Reserve Releases



Global reinsurance market adjusted combined ratio is calculated on a weighted average basis.
Peer groups' adjusted combined ratios are calculated on a simple average basis.

Chart 3: 2014 Aggregate Capital Adequacy By Peer Group



Cat: catastrophe

amount of claims eventually paid. The short-tail nature of these claims means payments are usually made within two to four years, and any excess reserves can be released through earnings in subsequent years. Given the string of relatively benign catastrophe years in 2013 through the first half of 2015, we expect these companies will be less able to release reserves of this magnitude in coming years.

We expect to see further rate reductions and lower—though not disappearing—reserve releases over the next 12 to 24 months. Therefore, we expect continued pressure on reinsurers' underlying earnings.

Excess Capital Will Likely Allow Reinsurers To Remain At Their Current Capital Adequacy Rating

Capital adequacy remains extremely strong for the reinsurance sector. Indeed, we have observed an overall improved capital redundancy as strong retained earnings led to total adjusted capital (TAC) growth in 2014, despite an increase in capital returned to shareholders. We expect reinsurers will keep generating enough earnings to maintain extremely strong capital over the next 12 to 24 months, even given the earnings challenges mentioned above.

Capital requirements grew in 2014, although not enough to outpace the increase in TAC (see Table 2). We note that on average, exposure to catastrophe relative to TAC is slightly down in the industry because many companies pulled back from writing cat business amid falling rates. Some peers have actually increased their capital and earnings exposure to catastrophes (see "Discipline Is Necessary As Reinsurers Adjust Their Exposure To Catastrophe Risk"), but these remain within their stated risk tolerances.

We've observed an increase in non-cat premium capital charges, which indicates to us that capital previously used to support the catastrophe business has been reallocated to other lines. One result of this reallocation is an increase in the diversification benefit, as measured by our model, for the industry.

While the industry's capital adequacy improved in 2014, it hasn't been uniform across the various subgroups (see Chart 3). Large European and London market reinsurers operate with a lower level of excess capital than property-catastrophe writers or Bermudian reinsurers, with the latter having a relative concentration

> **"We expect to see further rate reductions and lower—though not disappearing—reserve releases over the next 12 to 24 months."**

on high-severity lines that are more capital-intensive. We also suspect that many Bermudian companies hold excess capital as a marketing tool for attracting potential clients, particularly in a time when size seems to matter for cedants. London market reinsurers benefit from the collective Lloyd's capacity in many of their big-ticket catastrophe contracts, due to the subscription nature of that market. The difference in the excess capital held by London players and Bermudians narrowed slightly in 2014 as the latter reinsurers' excess capital positions declined largely due to increased capital returns to shareholders.

In our view, European players generally have a more diversified product portfolio and are consequently subject to a higher non-cat premium charges. However, that's partly offset by a diversification benefit that reduces risk-based capital requirements.

Few Signs That Reinsurers Are Hunting For Higher Investment Yields

In addition to rate declines that are weakening underwriting results, reinsurers have to cope with low investment yields. Reinsurers have thus far demonstrated some restraint in searching for yield because in aggregate, asset durations and credit risk have remained largely stable from 2013 to 2014 at 3.1 years and 'AA-' average rating, respectively. We do see some divergence among individual companies, however. Some players have extended their asset duration over the last two years, with a handful extending it by a year or more over the period, increasing their vulnerability to a rise in interest rates. We also note that on average, the London market players have moved down the credit curve in their fixed-income portfolios, increasing their investments in 'A'-rated issuers by 5% and unrated issuers by 1% at the expense of 'AA'-rated (-4%) and 'AAA'-rated (-2%) securities.

We have also observed a general move toward higher-risk investments: The equity share rose to 10% in 2014 from 7% in 2013 (see Chart 4). At this stage, these slow moves are not likely to affect negatively our ratings because the sector holds sufficient capital to absorb any increased charges, and all these tactical moves are within companies' stated risk tolerances. We see these investment tweaks as one way to offset the crunch on underwriting margins.

Average Catastrophe Exposure Has Remained Largely Stable, Though It Varies Among Players

Catastrophe risk continues to weigh heavily on reinsurers' financial risk profiles, and it's a primary reason behind the average "moderately strong" financial risk position in the sector. On an aggregate basis, we didn't see a material change in the amount of catastrophe risk exposure in the industry during 2014. However, we do see some divergence within the peer group (see "Discipline Is Necessary As Reinsurers Adjust Their Exposure To Catastrophe Risk"), because four or five companies have increased their earnings and capital

Chart 4: Asset Allocation

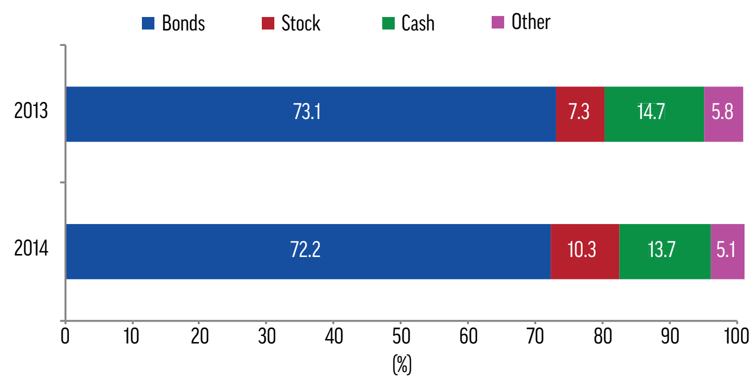
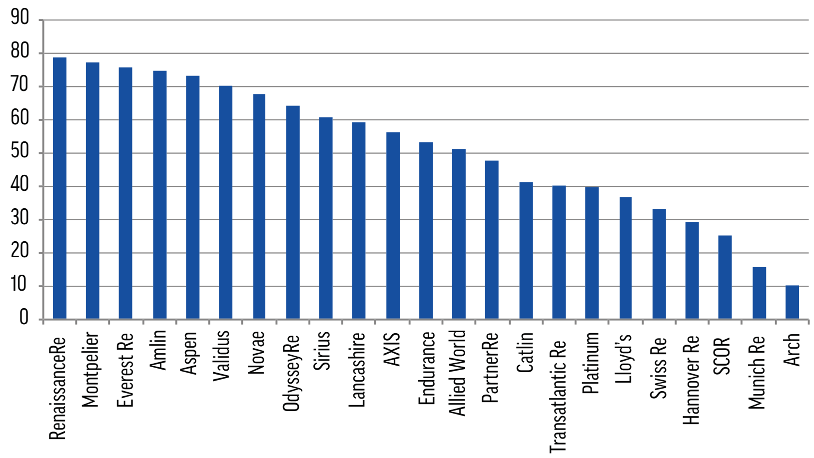


Chart 5: Relative Ranking Of Reinsurers' Catastrophe Exposure*



*Based on five metrics that assess the relative exposure to catastrophe risk, reinsurers are ranked against each other. The cumulative ranking index is defined as the weighted sum of the relative position on each of the five individual exposure metrics.

exposure to catastrophe risk, while a handful have reduced it.

Despite these moves, we observe no material change in the relative riskiness ranking of reinsurers' catastrophe exposure (see Chart 5). However, during 2014 a number of reinsurers exhibited relatively lower catastrophe risk than the peer group, which we recognized by assessing their risk positions as "moderate" rather than the "high" score for the rest of the sector (see Tables 3 and 4). We believe these companies' modeled exposure, modeling capabilities, and historical track record of less volatility from cat losses sets them apart from the peer group.

Softer Pricing Will Remain A Problem For Coming Years

Standard & Poor's view on the global reinsurance sector trends is clearly influenced by the excess capacity and heightened competition that are affecting pricing and shaping the landscape. Capital levels will remain at or near all-time highs, and the continued influx of

Table 3: Ratings Score Snapshots*

Company name	Financial strength rating	Outlook	Anchor	Business risk profile	IICRA	Competitive position	Financial risk profile
Bermuda							
Allied World Assurance Co. Holdings AG	A	Stable	a-	Strong	Intermediate Risk	Strong	Moderately Strong
Arch Capital Group Ltd.	A+	Stable	a	Strong	Intermediate Risk	Strong	Strong
AXIS Capital Holdings Ltd.	A+	Stable	a+	Very Strong	Intermediate Risk	Very Strong	Moderately Strong
Endurance Specialty Holdings Ltd.	A	Stable	a-	Strong	Intermediate Risk	Strong	Moderately Strong
Maiden Holdings Ltd.	BBB+	Stable	bbb+	Satisfactory	Intermediate Risk	Adequate	Upper Adequate
Platinum Underwriters Reinsurance Inc.**	A+	Stable	a-	Strong	Intermediate Risk	Strong	Strong
Sirius International Group Ltd.	A-	Negative	a-	Strong	Intermediate Risk	Strong	Strong
Large global reinsurers							
Hannover Rueck SE	AA-	Stable	aa-	Very Strong	Intermediate Risk	Very Strong	Very Strong
Lloyd's	A+	Stable	a+	Very Strong	Intermediate Risk	Very Strong	Moderately Strong
Munich Reinsurance Co.	AA-	Stable	aa-	Very Strong	Intermediate Risk	Extremely Strong	Very Strong
SCOR SE	A+	Positive	a+	Very Strong	Low Risk	Very Strong	Strong
Swiss Reinsurance Co. Ltd	AA-	Stable	aa-	Very Strong	Intermediate Risk	Extremely Strong	Very Strong
London Market							
Amlin plc	A	Stable	a-	Strong	Intermediate Risk	Strong	Upper Adequate
Aspen Insurance Holdings Ltd.	A	Stable	a-	Strong	Intermediate Risk	Strong	Moderately Strong
Catlin Group	A	Stable	bbb+	Strong	Intermediate Risk	Strong	Lower Adequate
Hiscox Insurance Co. Ltd.	A	Stable	a-	Strong	Intermediate Risk	Strong	Upper Adequate
Midsize global reinsurers							
Everest Re Group Ltd.	A+	Stable	a	Strong	Intermediate Risk	Strong	Strong
PartnerRe Ltd.	A+	Negative	a+	Very Strong	Intermediate Risk	Very Strong	Moderately Strong
Transatlantic Reinsurance Co.	A+	Stable	a	Strong	Intermediate Risk	Strong	Strong
Property-catastrophe / short-tail specialists							
Lancashire Holdings Ltd.	A-	Stable	a-	Strong	Intermediate Risk	Strong	Upper Adequate
Montpelier Reinsurance Ltd.**	A-	Credit Watch Positive	bbb+	Satisfactory	Intermediate Risk	Strong	Moderately Strong
RenaissanceRe Holdings Ltd.	AA-	Stable	aa-	Very Strong	Intermediate Risk	Very Strong	Strong
Validus Holdings Ltd.	A	Stable	a	Strong	Intermediate Risk	Strong	Strong

*As at August 13, 2015. IICRA: Insurance Industry and Country Risk Assessment

** Platinum and Montpelier no longer have SACPs following their acquisitions by RenaissanceRe and Endurance, respectively. Subscores for these companies are as of the time of acquisition alternative capital is also increasing supply.

We expect softening pricing will pressure the sector's operating performance in 2015 and 2016 compared with recent years, with our aggregate combined ratio forecast at 97% to 102% in 2015 and 99% to 104% in 2016, compared to the historical weighted average of 91.5%. Most reinsurers are clearly taking actions to remain competitive and cushion these pressures. Consolidation, increased retrocession, and diversifying into other lines and regions are the general trends we observe as the sector reacts to pricing declines and excess capital. We carefully assess the effectiveness and sustainability of these efforts in our ratings. ■

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Table 4: Ratings Score Snapshots (Continued)*

Company name	Capital & earnings	Risk position	Financial flexibility	Enterprise risk management	Management & governance	Holistic analysis	Liquidity
Bermuda							
Allied World Assurance Co. Holdings AG	Very Strong	High Risk	Adequate	Strong	Satisfactory	0	Strong
Arch Capital Group Ltd.	Very Strong	Moderate Risk	Strong	Strong	Satisfactory	0	Strong
AXIS Capital Holdings Ltd.	Very Strong	High Risk	Strong	Strong	Satisfactory	0	Adequate
Endurance Specialty Holdings Ltd.	Very Strong	High Risk	Adequate	Strong	Satisfactory	0	Adequate
Maiden Holdings Ltd.	Strong	Moderate Risk	Less than Adequate	Adequate	Fair	0	Adequate
Platinum Underwriters Reinsurance Inc.**	Extremely Strong	High Risk	Adequate	Adq, Strong Risk Controls	Fair	0	Strong
Sirius International Group Ltd.	Extremely Strong	High Risk	Adequate	Adq, Strong Risk Controls	Satisfactory	0	Exceptional
Large global reinsurers							
Hannover Rueck SE	Extremely Strong	Moderate Risk	Adequate	Very Strong	Strong	0	Exceptional
Lloyd's	Very Strong	High Risk	Strong	Strong	Strong	0	Strong
Munich Reinsurance Co.	Extremely Strong	Moderate Risk	Strong	Very Strong	Strong	0	Exceptional
SCOR SE	Very Strong	Moderate Risk	Strong	Very Strong	Strong	0	Exceptional
Swiss Reinsurance Co. Ltd	Extremely Strong	Moderate Risk	Strong	Very Strong	Satisfactory	0	Exceptional
London Market							
Amlin plc	Strong	High Risk	Strong	Very Strong	Satisfactory	0	Strong
Aspen Insurance Holdings Ltd.	Very Strong	High Risk	Strong	Very Strong	Satisfactory	0	Strong
Catlin Group	Moderately Strong	High Risk	Adequate	Very Strong	Satisfactory	1	Exceptional
Hiscox Insurance Co. Ltd.	Stong	High Risk	Strong	Strong	Strong	0	Exceptional
Midsize global reinsurers							
Everest Re Group Ltd.	Extremely Strong	High Risk	Strong	Strong	Satisfactory	0	Strong
PartnerRe Ltd.	Very Strong	High Risk	Strong	Adq, Strong Risk Controls	Satisfactory	0	Strong
Transatlantic Reinsurance Co.	Extremely Strong	High Risk	Adequate	Strong	Satisfactory	0	Strong
Property-catastrophe / short-tail specialists							
Lancashire Holdings Ltd.	Very Strong	Very High Risk	Adequate	Strong	Satisfactory	-1	Strong
Montpelier Reinsurance Ltd.**	Extremely Strong	Very High Risk	Adequate	Strong	Satisfactory	0	Adequate
RenaissanceRe Holdings Ltd.	Extremely Strong	High Risk	Strong	Very Strong	Strong	0	Strong
Validus Holdings Ltd.	Extremely Strong	High Risk	Strong	Strong	Satisfactory	-1	Adequate

*As at August 13, 2015

** Platinum and Montpelier no longer have SACPs following their acquisitions by Renaissance Re and Endurance, respectively. Subscores for these companies are as of the time of acquisition

Insurance Industry And Country Risk Assessment On The Global Property/Casualty Reinsurance Sector Is "Intermediate"

SHUTTERSTOCK / MATT TROMMER

By Taoufik Gharib, Dennis Sugrue and Olga Ryabaya

Pricing and low investment yields are pressuring returns for reinsurers, but they remain acceptable and widespread evidence of increased risk-taking is not apparent.

Standard & Poor's Ratings Services has an "intermediate" insurance industry and country risk assessment (IICRA) score on the global property and casualty (P/C) reinsurance sector. We base this assessment on our weighted average views of "low" country risk and "moderate" industry risk for the sector (see Chart 1).

For comparison, primary P/C insurance markets with intermediate IICRA scores include the U.S., Japan, the U.K., Ireland, and South Africa.

One of the key risks facing the global P/C reinsurance sector is increasing competition among the traditional reinsurers. In addition, the influx of alternative capital (also referred to as convergence capacity, third-party capital, and collateralized reinsurance) has increased significantly during the past few years and has contributed to the general oversupply of reinsurance capacity. Both of these factors are pushing down reinsurance prices and top-line premium volume and have potential to dent reinsurers' profitability in 2015 and 2016.

Standard & Poor's believes competitive pressures will remain heightened in reinsurance, and we don't expect the recent spate of consolidations to alleviate that burden. In fact, we believe this trend toward greater scale highlights how hard it will be for management teams to defend their market positions.

Country Risk: Low

We base our assessment of low country risk on an approximation of the weighted average country risk scores for the major countries where the lion's share of the sector's business is written (e.g., Germany, the U.S., Bermuda, Switzerland, the U.K., and Japan). This reflects the fact that reinsurers' exposures have continued to be highly geographically diverse and heavily weighted to developed markets, most of which present low to very low country risk owing to their stable political environments, financial systems, payment cultures, and rule of law. We believe the domicile of a reinsurer has relatively little impact on the aggregate industry and country risks it faces, and therefore we don't differentiate by domicile.

Despite its insulation from individual country risks, the global P/C reinsurance sector can still feel the impact of wider macroeconomic trends. We expect continued low interest rates at least in 2015 to dampen the sector's investment returns, and thus its returns on equity (ROE) (see Table 2).

In general, the global reinsurance sector's premium growth or contraction correlates with movements in global GDP. The global economy seems to have improved slightly in 2015, and we expect that trend to continue next year, with the U.S. picking up speed followed by Europe. However, the emerging-market economies have slowed down. Risk of inflation shock could also be a drag on P/C reinsurers' profitability by adversely affecting reserve levels on prior years' business, but our expectation that inflation in major developed economies (see Table 3) will remain controlled in the next two years mitigates this risk to the sector for now.

After a soft first quarter, in part due to weather, the U.S. economy's rebound will probably be modest, given the dollar's strength and still-depressed oil prices. Standard & Poor's forecasts the U.S. economy to expand 2.3% in 2015, down slightly from 2.4% in 2014. With job gains recovering and prices a bit warmer, we think the Fed will raise rates in September, although it will probably keep the pace of rate hikes very slow, with the federal funds rate likely to end the year between 0.5% and 0.75%. Standard & Poor's maintains its view that the risk of a recession over the next 12 months is 10% to 15%.

The eurozone economy is at a tipping point. On one hand, Standard & Poor's projects 1.6% GDP growth in the eurozone this year and 1.9% in 2016, on the back of stronger consumer demand. We continue to assume that the current recovery is likely to gain momentum in the coming two years. On the other hand, we recognize that the resolution of the Greek crisis remains uncertain. We think the possibility of Greece leaving the eurozone has declined to less than 50%, but the risk of an exit is still high if the Greek government doesn't successfully implement what looks to be an ambitious program. We believe that in a worst-case scenario of a Greek exit, the risks of contagion to other eurozone countries are less elevated than in 2010–2011. Still, such a shock could lead to increased risk aversion among investors, lenders, and consumers. Because business and consumer confidence is a key factor in our forecast for the next two years, a 'Grexit' could easily weaken the upturn we are currently contemplating.

> **"Competition among the reinsurers will continue to be fierce and market growth prospects will be restricted in the short term, even without the surge in third-party capital."**

China's slowdown also remains front and center. Growth remains below the authorities' 7% target as the property and stock market corrections continue. The pace of activity in Japan and India is picking up, reflecting stronger investment and bucking the regional trend. However, in many small and midsize open economies in Asia-Pacific, growth remains soft amid weak external demand. Monetary settings continue to ease, with several central banks' policy rates at all-time lows. Whether they follow the U.S. Fed higher, and what this means for the region's new borrowers, remains to be seen.

As global commodity prices have fallen, Latin American economies (which are generally commodity exporters) are suffering from lower rates of GDP growth. The largest country in the region, Brazil, is in recession. Standard & Poor's expects that Brazil's GDP could contract 1.5% in 2015 before recovering modestly next year. Mexico, the second-largest economy in the region, is likely to grow only 2.5% in 2015 and accelerate mildly to 3% in the following year. The tepid economic performance of these two sovereigns, which account for the bulk of GDP in the region, brings down the weighted average growth rate of Latin America to less than 0.5% in 2015 from 1.1% in the previous year (see Table 4). (Note: All economic forecasts were current at the time of printing.)

Industry Risk: Moderate

We base our evaluation of the global P/C reinsurance sector's "moderate" industry risk on the assessment of five industry-related subfactors: profitability (as measured by ROE), product risk, barriers to entry, market growth prospects, and the institutional framework.

The global P/C reinsurance industry still faces many challenges, including mounting competitive pressures amid weakening profitability, downward pressure on reinsurance pricing, overcapacity, a steady inflow of alternative capital, and diminishing benefits from reserve releases, along with persistently low investment yields and limited growth in developed markets.

Competition from the glut of third-party capital is only adding fuel to the fire. Traditional reinsurers are already competing in an attempt to deploy their excess capital. In addition, large cedants (insurance companies) are rationalizing their reinsurance spending as they increasingly make purchasing decisions at the group level rather than at individual operating units. This portfolio-optimization approach is streamlining reinsurance programs and reducing the number of reinsurers large primary insurers use for protection. As a result, we believe that competition among the reinsurers will continue to be fierce and that market growth prospects will be restricted in the short term, even without the surge in third-party capital.

Alternative capital is having the most acute impact in the U.S. property catastrophe market but is tip-toeing into the U.S. commercial property markets as well. The role of alternative capital in the catastrophe reinsurance segment increased in 2014. The insurance industry issued a record $8.8 billion in catastrophe bonds (of which Standard & Poor's rated $4.1 billion), and collateralized reinsurance rose to nearly $30 billion, according to estimates from broker Aon Benfield. Aon Benfield also estimates that all alternative capital vehicles, which take the form of sidecars, insurance-linked securities, and catastrophe funds, totaled $64 billion in 2014, or 18% of global catastrophe capacity.

A rising supply of catastrophe protection naturally pushes down pricing. Traditional catastrophe reinsurance premiums are seeing the most severe rate declines, and catastrophe bonds' return on expected losses (the measure of pricing in this market) is near all-time lows. Competition is also intense in most other lines of business, as rates decrease on excess-of-loss covers and ceding commissions rise on pro rata treaties.

Chart 1: Industry And Country Risk Scores

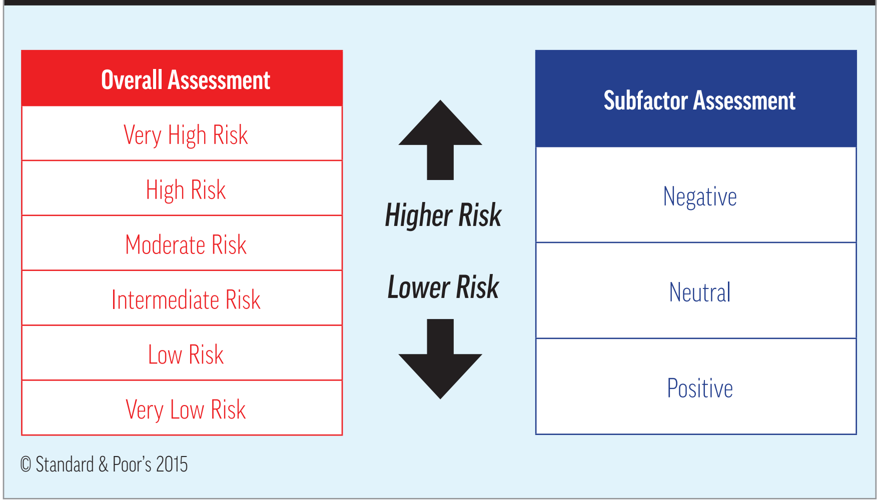

Table 1: Global P/C Reinsurance IICRA

Sector	IICRA	Country risk	Industry risk	Industry risk components				
				Profitability	Product risk	Barrier to entry	Growth prospects	Institutional framework
Global P/C Reinsurance	Intermediate	Low	Moderate	Neutral	Negative	Neutral	Neutral	Neutral

Table 2: Economic Outlook–Interest Rates, Equity, And Bond Markets

	(%, except S&P 500 Index)		
	2014	2015f	2016f
U.S. 10-year Treasury note yield	2.5	2.2	2.8
U.S. three-month Treasury bill rate	0.0	0.1	0.9
German 10-year bond yield	1.2	0.6	1.2
U.K. 10-year bond yield	2.6	2.0	2.6
AAA corporate bond yield (U.S.)	3.2	3.1	4.1
U.S. federal funds rate	0.1	0.2	1.3
European central bank policy rate	0.2	0.1	0.1
Bank of England policy rate	0.5	0.5	0.8
S&P 500 Index	1,931	2,109	2,178
f: Forecast			

Return on equity (neutral)

We view the prospective profitability of the global P/C reinsurance sector as neutral. The global P/C reinsurance sector generated an average ROE of 13% during the past five years (2010 to 2014). We expect low interest rates to continue to put pressure on reinsurers' investment yields in the coming years. We expect the reinsurance sector to generate an ROE of 8% to 10% in 2015 and 2016.

During the past five years, investment returns have contributed to the sector's ROE, but the contribution has been diminishing because of persistent low interest rates. The reinsurance sector's operating results benefited from strong underwriting cycle management and strong results in benign catastrophe years. Partially offsetting these strengths are volatility in operating results in above-average catastrophe years and significant reliance on prior years' favorable reserve releases to bolster earnings.

The top 28 reinsurers produced an average combined ratio of 94.5% during the past five years (2010 to 2014). On average, the sector's underwriting performance benefited from 5.9 percentage points of favorable reserve releases, which were embedded in their combined ratios, during the same period. The favorable prior-year developments have come largely from short-tail lines and the latest set of hard market years for casualty reinsurance (i.e., 2002 to 2005). We believe that the remaining redundancies associated with these hard market years are limited, and that recent benign catastrophe loss activity will constrain reinsurers' ability to release property catastrophe reserves. As a result, we expect the ongoing benefits of favorable reserve developments to decrease relative to the past few years, and we forecast a combined ratio of about 95% to 100% for the sector in 2015, and 97% to 102% in 2016.

We're alert to the possibility that reinsurers may be tempted to take on additional risk to maintain profitability in a soft market, as we've seen in the past. We're seeing some evidence of this, as reinsurers are increasingly offering more multiyear contracts, widening some terms and conditions, and paying higher ceding commissions of as much as 35% to 40% in some lines. However, this is at the margins and is not widespread. We believe that reinsurers' overall strong enterprise risk management (ERM) capabilities have helped them manage their risks and exercise underwriting discipline during this softening market. ERM capabilities have also enabled the sector to generate strong earnings, as evidenced by their resilience to natural and manmade catastrophes and financial crises during the past decade.

We anticipate, however, that reinsurers' ERM capabilities will face some tests in 2015 and 2016, particularly with regard to underwriting controls and strategic risk management. With the continuation of rate decreases in property catastrophe and other lines of business, relative risk-adjusted returns for various risk exposures will shift. This could force reinsurers to implement some strategic changes based on the guidance of their ERM functions. Furthermore, as the market softens, the pressure on underwriting, catastrophe, and reserving risk controls will grow. Over the next two years, we could see which carriers' ERM frameworks actually translate into tangible actions.

Product risk (negative)

Due to the inherent volatility in many P/C products, which ultimately affects ROE, we view product risk as negative. That's because the P/C reinsurance sector often serves as a backstop for high-severity P/C risks—such as catastrophe and, to a lesser extent, terrorism risks—from the P/C insurance sectors. To cope with these risks, global reinsurers tend to be strongly capitalized and maintain sophisticated ERM programs.

The global P/C reinsurance sector's operating performance has faced significant exposure to volatility from natural catastrophe losses. Indeed, the top 28 reinsurers in the world have seen an average annual 12.7 percentage point negative impact on their P/C reinsurance combined ratio during the past five years due to natural catastrophe losses. The impact on the combined ratio was especially severe in 2011 and reached 30.4 percentage points for these reinsurers. As a result, many reinsurers have factored in a catastrophe load (average annual loss, or AAL) of 8 to 10 percentage points in the combined ratio in their annual budgets to provide a cushion against this volatility.

We believe that the sector is also exposed to unpredictable settlements in the casualty lines of business. The industry has experienced volatility from adverse claims settlements in the past. Although volatility on this front hasn't been significant in recent years, the threat remains. Historically, volatility in results has arisen from unpredictable claims settlements for reinsurers, particularly in the U.S. regarding asbestos and environmental claims, workers' compensation, professional liability, and medical malpractice.

Barriers to entry (neutral)

Our neutral assessment incorporates two main factors, regulatory and operational barriers, both of which we view as "moderate". Given the global scope of this sector, we consider various regulatory regimes when assessing regulatory barriers to entry. Most global reinsurers are domiciled in major developed markets, such as Germany, the U.S., the U.K., Switzerland, and Bermuda.

Our assessment also considers the relatively moderate operational barriers to entry that expose P/C reinsurers to competition from new reinsurers, although we've observed that these barriers to entry are evolving. It's challenging for new entrants to establish a defendable and sustainable competitive position, and few have been successful. We recognize that it is relatively easy for a start-up P/C reinsurer or third-party capital provider to enter the market to write property-catastrophe business in the wake of a capital event or when seeking higher returns. However, any new entity needs to have a credible management team with a solid track record and a robust business plan.

We believe that accessing the noncatastrophe lines of business in the U.S., and especially in Europe, requires a stronger business model, established relationships, financial security, an increasingly larger balance sheet, and a track record that takes time to develop. Cedants want to be sure that their reinsurers will be around to pay claims, and the recent consolidation of small and midsize reinsurers to strengthen their competitive positions and establish themselves as viable long-term players underscores the difficulty reinsurers have in ensuring that longevity. The recent spate of consolidations is reducing the number of players and raising the price of admission for reinsurers that seek to demonstrate their relevance and staying power to increasingly sophisticated clients. We believe operational barriers to entry remain moderate but will continue to monitor these evolving dynamics.

"Any new entity needs to have a credible management team with a solid track record and a robust business plan."

Table 3: Economic Outlook—Consumer Price Index (CPI) Inflation

	(%)		
	2014	**2015f**	**2016f**
U.S.	1.6	-0.1	2.2
Eurozone	0.4	0.2	1.2
Germany	0.8	0.6	1.7
France	0.6	0.4	1.4
Italy	0.2	0.3	0.9
Spain	-0.2	-0.3	1.1
U.K.	1.5	0.2	1.7
Switzerland	0.0	-1.2	0.0
Brazil	6.3	8.4	7.2
Mexico	4.1	3.5	3.5
Australia	2.5	1.9	2.4
China	2.0	1.3	1.8
Japan	2.7	0.9	1.1
Singapore	1.0	-0.4	1.7
Turkey	8.9	7	6.4

f: Forecast.

Table 4: Economic Outlook—Real GDP Growth Or Contraction

	(% change)		
	2014	**2015f**	**2016f**
U.S.	2.4	2.3	2.7
Eurozone	0.9	1.6	1.9
Germany	1.6	2.0	2.2
France	0.2	1.3	1.6
Italy	-0.4	0.5	1.0
Spain	1.4	3.0	2.6
U.K.	2.8	2.6	2.8
Switzerland	2.0	0.7	1.7
Brazil	0.2	-1.5	1.5
Mexico	2.1	2.5	3.0
Australia	2.7	2.6	2.9
China	7.4	6.8	6.6
Japan	-0.2	0.9	1.3
Singapore	2.9	3.0	3.3
Turkey	2.9	3.0	3.2

f: Forecast.

Market growth prospects (neutral)

Overall, gross premiums written for the top 28 reinsurers have grown by 3.0% annually on average during the past five years. We believe that the competitive pressures from alternative capital and changing cedant behavior are dampening short-term market growth prospects, and thus we expect premiums to be broadly flat to slightly down, by 3% or so, in 2015 and 2016. Over the longer term, we believe reinsurers are well positioned to support increased insurance penetration in developing markets. Taken together, these trends inform our view that overall market growth prospects are neutral.

The improvement in the developed economies could somewhat boost the reinsurance sector's premium growth in 2015 and 2016. However, continued pricing pressure in a competitive environment would likely limit growth. Despite the saturation of the developed markets, we've seen some pockets of growth in mortgage, accident and health, and in cyber reinsurance products.

Our economic forecasts show that that growth in emerging markets has slowed. Insurance penetration in these emerging markets is generally low, but growing. The compounded effects of economic growth (although at a lower rate) and increasing insurance penetration provide opportunities for growth. In response, many global reinsurers have incorporated these emerging economies in Latin America, the Middle East, Africa, and Asia-Pacific into their growth and diversification strategies. Due to their global scope and knowledge base, along with their ability to partner with local carriers rather than compete with them, we believe reinsurers are better placed than many primary insurance peers to benefit from increasing insurance penetration globally.

> **"Many global reinsurers have incorporated these emerging economies in Latin America, the Middle East, Africa, and Asia-Pacific into their growth and diversification strategies."**

Institutional framework (neutral)

Our view of the institutional framework is based on our assessment of the regulatory framework and regulatory track record in the markets where most global P/C reinsurers are domiciled, including the U.S., the U.K., France, Germany, Switzerland, and Bermuda, which we view in aggregate as "intermediate". In addition, the governance standards and transparency of these domiciles present no deficiencies. Accounting standards and disclosure practices, including whether a reinsurer has adopted U.S. generally accepted accounting principles or international financial reporting standards, are generally of high quality and reliable. ■

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Table 5: Top 28 Global Reinsurers' P/C Reinsurance Business

	2014	2013	2012	2011	2010	Five-year average
P/C reinsurance gross premiums written (GPW) Mil.$	97,239	100,953	97,207	90,697	86,515	94,522
Change in GPW	-3.7%	3.9%	7.2%	4.8%	NA	3.1%
P/C reinsurance net premiums written (NPW) Mil.$	90,602	93,834	88,121	81,727	77,726	86,402
Change in NPW	-3.4%	6.5%	7.8%	5.1%	NA	4.0%
P/C reinsurance net premiums earned (NPE) Mil.$	88,322	90,278	86,249	78,587	76,100	83,907
Change in NPE	-2.2%	4.7%	9.7%	3.3%	NA	3.9%
Retrocession utilization	6.8%	7.1%	9.3%	9.9%	10.2%	8.7%
Expense ratio	30.1%	29.1%	28.7%	28.9%	29.0%	29.2%
Loss ratio	57.3%	58.6%	61.2%	82.7%	66.8%	65.3%
Calendar combined ratio	87.4%	87.6%	89.9%	111.6%	95.8%	94.5%
Prior year (favorable)/unfavorable reserve development Mil.$	-4,330	-6,424	-5,960	-4,476	-3,797	-4,997
Impact on the combined ratio	-4.9%	-7.1%	-6.9%	-5.7%	-5.0%	-5.9%
Accident year combined ratio	92.3%	94.7%	96.8%	117.3%	100.8%	100.4%
Natural catastrophe losses Mil.$	3,702	6,012	8,362	23,891	9,513	10,296
Impact on the combined ratio	4.2%	6.7%	9.7%	30.4%	12.5%	12.7%

NA: Not available. Top 28 reinsurers: Munich Re, Swiss Re, Hannover Re, Korean Re, PartnerRe, SCOR, Everest Re, TransRe, GenRe, Maiden Re, AXIS Re, Catlin Re, XL Re, CCR, Odyssey Re, Arch Re, Toa Re, RenRe, Deutsche Re, Endurance Re, Aspen Re, Sirius Re, Validus Re, ACE Re, AWAC Re, W.R. Berkley Re, Platinum Re, and Lancashire Re.

Global Life Reinsurance Sector Carries A Low Insurance Industry And Country Risk Assessment

By Johannes Bender and Dennis Sugrue

Standard & Poor's Ratings Services assesses industry and country risk in the global life reinsurance sector as low. Our assessment reflects our view of the risks that life reinsurers operating in the global marketplace typically face.

The rationale behind our assessment of the global life sector's strengths includes:

- Strong profitability;
- Focus on biometric products results in low dependence on investment income and relative insulation from interest rate risk;
- High barriers to entry based on specialized international market expertise, underwriting capacities, and data and client stickiness; and
- Sound mid- to long-term growth prospects in emerging markets.

The rationale behind our assessment of the sector's weaknesses includes:

- Declining cession rates in main markets, particularly the U.S.;
- Potential increased risk-taking from growth in longevity and health; and
- Some earnings volatility potential from assumption changes in biometric products.

We consider both industry and country risk for this sector to be low. Primary life insurance markets that have low insurance industry and country risk assessments (IICRAs) include France, the U.S., Australia, Canada, and the U.K. (see Table 1). We believe one important difference is the global life reinsurers' main focus on biometric risks, whereas most primary life insurance markets write material savings business, including selective investment guarantees.

In our view, life reinsurance is less risky than property/casualty (P/C) reinsurance (see Table 2). Because both industries are global, we consider country risk to be identical; however, we believe industry risk in the life market is lower. In particular, we think that barriers to entry and profitability are more favorable for the life reinsurers than for the global P/C reinsurance sector that is facing visible pressure on prices and profitability due to a continued influx of capacity and capital.

Country Risk: Low

We derive our low country risk assessment for the global life reinsurance sector from an approximation of the weighted-average scores of each of the five country-related subfactors in the major countries where life reinsurers operate: economic, political risk, financial system risk, payment culture, and rule of law. Global reinsurers typically write business in multiple countries around the world, resulting in a high level of geographic diversification. More importantly, the domicile of the reinsurer has relatively little impact on the aggregate industry and country risks it faces.

Despite its insulation from individual country risks, the global reinsurance sector can still be influenced by wider macroeconomic trends (see Tables 3, 4 and 5). Divergent growth trends between developed and emerging economies could open opportunities for life reinsurers to increase their market penetration in the faster-growing emerging markets, at least in the long term. We also believe that interest rates will remain low, continuing to depress the sector's investment returns somewhat, as well as its returns on equity (ROEs), although the sector's dependence on investment returns is visibly lower than that of the primary life insurance sector.

Industry Risk: Low

We base our assessment on our view of five industry-related factors. We see barriers to entry and profitability (measured by ROE) as positive, and product risk and growth prospects as neutral. We assess the institutional framework as moderately strong.

Our industry risk assessment is particularly sensitive to changes in our assessment of the sector's profitability and barriers to entry. A positive revision of our industry risk assessment to very low is unlikely at this stage and would likely hinge on a significant increase in the industry's growth potential both in mature and emerging markets, leading us to change our assessment of market growth prospects to positive.

Deterioration in our industry risk assessment is possible if we perceive that product risk increases significantly, driven by aggressive growth in new and unknown risks such as health and longevity. We could also revise our industry risk assessment to intermediate if the sector experiences strong mortality or morbidity assumption changes in its biometric products that would sustainably affect profitability.

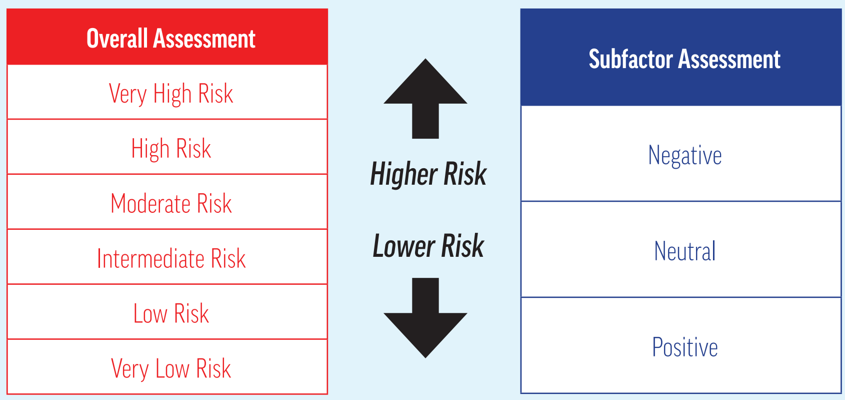
Return on equity (positive)

We regard the historical and prospective profitability of the global life reinsurance market as positive. We believe the industry's profitability benefits somewhat from the high barriers to entry and limited international competitors. We expect the industry's profitability to remain favorable, and we estimate an industrywide average ROE of more than 10% for 2015–2017. This is backed by our assumption that the operating return on embedded value will be about 8% to 12%, and that the new business margin will be about 3.5% to 4.0%, based on the value of new business premiums in 2015–2017.

Although we believe investment income will gradually decline by about 10 to 20 basis points per year in 2015–2017, we believe the industry is less dependent on investment income than are primary life insurance markets, and can thus continue to perform strongly in line with our expectations. In 2014 the industry's main competitors reported new business margins of between 3.8% and 4.3%, indicating continued strong profitable new business generation.

We do not expect to see excessive risk-taking among global life reinsurers, although we expect an increase in risk-taking within companies' risk tolerances and appetites. Greater risk-taking reflects shrinking market volumes of traditional mortality business, which is causing the sector to take on newer and less-understood risks.

Chart 1: Industry And Country Risk Scores



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LIFE REINSURANCE IICRA

The life reinsurance sector has experienced periods of aggressive pricing. The most dramatic price rationalization occurred after 2003, and poorly priced mortality risks from before 2003—although deteriorating—still impair some reinsurers' profitability. Coupled with lower cession rates in the U.S., this has fueled much of the industry consolidation during the past decade. Nevertheless, we view global life reinsurers' enterprise risk management (ERM) practices as generally strong to very strong, and we expect increased pricing discipline and advances in pricing and underwriting technology to minimize the risk that the industry will repeat these aggressive practices.

Product risk (neutral)

We assess the potential for product risks to trigger ROE volatility as neutral. The global life reinsurance industry generally focuses on writing mortality or protection business, and writes limited amounts of savings products that have related guarantee risk. Thus, main risks taken by the industry include mortality, longevity, and morbidity risks. This insulates reinsurers from investment risk to a greater degree than in primary insurance markets. We therefore view asset-liability management risks as low. Nevertheless, significant changes to assumptions, such as on mortality or morbidity, can create some earnings volatility.

For example, Australian disability business written in prior years experienced some dislocation, including higher-than-expected claims and lapses in 2013 with an estimated pretax loss for the global life reinsurance industry of about $1 billion. We also observe that life reinsurers take increasingly larger longevity and health risks in view of declining cession rates in mortality business in mature markets that can somewhat change risk profiles over time. Although there is a natural hedge between longevity and mortality, this might not correlate in the various regions, and underwriting experiences and data in new regions might not be as pronounced.

Life reinsurers' past aggressive pricing of mortality business and poor experience with variable annuity risks remain a drag on earnings for some companies. Nevertheless, we consider the scope of this business to be limited, and have incorporated it into our expectations for industry profitability in 2015–2017. We also believe that most adverse developments from Australian disability were reflected in 2012–2014 results.

Barriers to entry (positive)

We consider barriers to entry for the global life reinsurance sector to be high. We assess regulatory barriers to entry as moderate and operational barriers as high.

Given the global scope of this sector, there are numerous regulatory regimes to be considered when assessing regulatory barriers to entry. Most global life reinsurers are domiciled in major developed markets such as the U.S., France, Germany, and Switzerland, where the regulatory frameworks are demanding, but do not prevent market entry.

Our view of operational barriers to entry as high recognizes that the global life reinsurance market is dominated by a few international diversified groups that have specific international market expertise, underwriting capacities, and key underwriting data developed during their long histories. We believe that the top six players make up more than 90% of the total market (see Table 6). We expect new entrants to find it difficult to build organically the expertise, client relationships, and underwriting data necessary to succeed in this market. We also feel that the market holds few viable targets that would enable a new entrant to develop a foothold through acquisition.

Market growth prospects (neutral)

We view market growth prospects in the global life reinsurance sector as neutral. The motivation for life reinsurance and cession rates from primary insurers can vary widely among regions and can be somewhat opportunistic. Classic risk transfer, product partnering, and capital relief are the main motivations for life reinsurance in our view. For 2014 we estimate the total market to be about $58 billion. The global life reinsurance market is still strongly dominated by mature

Table 1: Global Life Reinsurance Industry And Country Risk Relative To Life Sectors In Other Countries

				Industry risk components				
	Industry and country risk assessment	Country risk	Industry risk	Profitability	Product risk	Barriers to entry	Growth prospects	Institutional framework
Global life re	Low risk	Low risk	Low risk	Positive	Neutral	Positive	Neutral	Neutral
France	Low risk	Low risk	Intermediate risk	Neutral	Neutral	Positive	Neutral	Neutral
U.S.	Low risk	Very low risk	Intermediate risk	Neutral	Neutral	Neutral	Neutral	Strong
Australia	Low risk	Very low risk	Low risk	Positive	Positive	Neutral	Neutral	Very strong
Canada	Very low risk	Very low risk	Low risk	Neutral	Negative	Positive	Neutral	Very strong
U.K.	Low risk	Very low risk	Intermediate risk	Neutral	Neutral	Neutral	Neutral	Very strong

Table 2: Global Life And P/C Reinsurance IICRA Comparison

				Industry risk components				
	Industry and country risk assessment	Country risk	Industry risk	Profitability	Product risk	Barriers to entry	Growth prospects	Institutional framework
Global life re	Low risk	Low risk	Low risk	Positive	Neutral	Positive	Neutral	Neutral
Global P/C	Intermediate risk	Low risk	Moderate risk	Neutral	Negative	Neutral	Neutral	Neutral

markets, particularly in the U.S. and U.K. The sector has consolidated in recent years in response to shrinking mortality cession rates in some major markets, particularly the U.S.

However, the U.S. market has contracted by nearly two-thirds in the past 10 years due to higher retentions by the primary market. We therefore believe that mature markets will remain stable at best in view of growth prospects at least in the mortality business. Nevertheless, growth can also emanate from mature markets, as it did in the largest life reinsurance longevity market in the U.K. because of increasing demand for reinsurance, particularly in defined-benefit pension schemes. We believe growth momentum from longevity swap deals in 2015–2016 will remain strong for the sector in the U.K.

We also believe that regulatory developments such as Solvency II and other initiatives toward economic principles can be a growth potential for capital relief-motivated transactions in the short term. Primary insurers that seek to optimize their balance sheets and strengthen capital adequacy in 2015–2016 globally may benefit, even in mature markets.

Emerging markets—particularly Asia, Latin America, Africa, and Eastern Europe—remain relatively small in terms of their contributions to the overall volume of the global life reinsurance sector. We estimate emerging markets represented less than 30% of the total market in 2014. We believe that long-term growth for the global life reinsurance industry can come from primary insurance markets in underpenetrated regions. We also believe global life reinsurance writers are well placed to play an important role in developing these markets.

Institutional framework (moderately strong)

We regard the sector's institutional framework as moderately strong. Accounting standards and disclosure practices are generally of high quality and reliable. We assess the regulatory oversight and regulatory track record of the markets where most global life reinsurers are domiciled (U.S., France, Germany, Switzerland) as intermediate or strong. In addition, we do not consider governance and transparency to be weak. ■

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Table 3: Economic Outlook—Interest Rates, Equity, And Bond Markets

	(%, except S&P 500 Index)		
	2014	**2015f**	**2016f**
U.S. 10-year Treasury note yield	2.5	2.2	2.8
U.S. three-month Treasury-bill rate	0.0	0.1	0.9
German 10-year bond yield	1.2	0.6	1.2
U.K. 10-year bond yield	2.6	2.0	2.6
AAA corporate bond yield (U.S.)	3.2	3.1	4.1
U.S. federal funds rate	0.1	0.2	1.3
European central bank policy rate	0.2	0.1	0.1
Bank of England policy rate	0.5	0.5	0.8
S&P 500 Index	1,931	2,109	2,178
f: Forecast			

Table 4: Economic Outlook—Consumer Price Index (CPI) Inflation

(%)	2014	2015f	2016f
U.S.	1.6	(0.1)	2.2
Eurozone	0.4	0.2	1.2
Germany	0.8	0.6	1.7
France	0.6	0.4	1.4
Italy	0.2	0.3	0.9
Spain	(0.2)	(0.3)	1.1
U.K.	1.5	0.2	1.7
Switzerland	(0.0)	(1.2)	(0.0)
Brazil	6.3	8.4	7.2
Mexico	4.1	3.5	3.5
Australia	2.5	1.9	2.4
China	2.0	1.3	1.8
Japan	2.7	0.9	1.1
Singapore	1.0	(0.4)	1.7
Turkey	8.9	7.0	6.4
f: Forecast			

Table 5: Economic Outlook—Real GDP Growth or Contraction

	(% change)		
	2014	**2015f**	**2016f**
U.S.	2.4	2.3	2.7
Eurozone	0.9	1.6	1.9
Germany	1.6	2.0	2.2
France	0.2	1.3	1.6
Italy	(0.4)	0.5	1.0
Spain	1.4	3.0	2.6
U.K.	2.8	2.6	2.8
Switzerland	2.0	0.7	1.7
Brazil	0.2	(1.5)	1.5
Mexico	2.1	2.5	3.0
Australia	2.7	2.6	2.9
China	7.4	6.8	6.6
Japan	(0.2)	0.9	1.3
Singapore	2.9	3.0	3.3
Turkey	2.9	3.0	3.2
f: Forecast			

Table 6: Long-Term Rating Of The Top Six Reinsurers

	Long-term rating/ outlook	GPW (bil. $)
Munich Reinsurance Co.*	AA-/Stable	17.1
Swiss Reinsurance Co. Ltd.	AA-/Stable	12.4
Reinsurance Group of America Inc.	AA-/Stable	9.1
Hannover Rueck SE	AA-/Stable	7.9
SCOR SE	A+/Positive	7.8
General Reinsurance Corp.**	AA+/Watch Negative	3.2
Total		57.5

*Excludes Munich Health. **Net premiums written. GPW: Gross premiums written

Top 40 Global Reinsurance Groups Ranked By Net Reinsurance Premiums Written

				Net reinsurance premiums written (Mil. $)	
Ranking	**Company**	**Country**	**Footnote**	**2014**	**2013**
1	Swiss Reinsurance Co.	Switzerland	1	31,640.0	30,478.0
2	Munich Reinsurance Co.	Germany		31,180.9	36,757.5
3	Berkshire Hathaway Re	U.S.	2	16,568.0	14,368.0
4	Hannover Rueckversicherung AG	Germany	3	15,293.5	17,101.0
5	SCOR SE	France		12,324.0	12,570.6
6	Lloyd's	U.K.	4	10,415.7	11,329.2
7	Reinsurance Group of America, Inc.	U.S.		8,669.9	8,254.0
8	China Reinsurance (Group) Corp	China	2	7,771.9	7,365.9
9	PartnerRe Ltd.	Bermuda		5,719.9	5,396.5
10	Everest Reinsurance Co.	Bermuda		5,256.9	5,004.8
11	Korean Reinsurance Co.	Korea		3,582.1	3,574.7
12	Transatlantic Holdings Inc.	U.S.		3,410.1	3,248.0
13	MS&AD Holdings	Japan	5	3,320.4	3,655.5
14	Sompo Japan Nipponkoa Holdings Inc.	Japan	6	2,853.0	3,036.7
15	Mapfre Re	Spain		2,678.6	2,958.3
16	Tokio Marine Group	Japan	7	2,496.1	2,757.9
17	Maiden Re	Bermuda		2,458.1	2,096.3
18	General Ins. Corp. of India	India		2,216.1	2,211.0
19	AXIS Capital Holdings Ltd.	Bermuda	8	2,127.5	2,114.7
20	R+V Versicherung AG	Germany	9	2,073.4	2,045.9
21	Catlin Group Ltd.	Bermuda	8	1,962.4	1,697.8
22	XL Re Ltd.	Bermuda		1,810.7	2,045.3
23	Toa Re Co. Ltd.	Japan		1,746.7	1,951.9
24	QBE Insurance Group Ltd.	Australia		1,571.0	1,575.0
25	Caisse Centrale de Reassurance	France		1,557.5	1,668.1
26	Odyssey Re	U.S.	10	1,466.8	1,633.9
27	Arch Capital Group Ltd.	Bermuda	11	1,266.0	1,313.0
28	ACE Tempest Reinsurance Ltd.	Bermuda		1,197.0	1,274.7
29	Validus Holdings Ltd.	Bermuda	12	1,163.3	1,278.3
30	Aspen Insurance Holdings Ltd.	Bermuda	13	1,124.0	1,082.0
31	Endurance Specialty Holdings Ltd.	Bermuda		1,073.8	1,116.4
32	Allied World Assurance Co. Holdings Ltd.	Bermuda	14	903.2	893.0
33	Sirius Group	Bermuda	15	882.5	876.6
34	RenaissanceRe Holdings Ltd.	Bermuda	8	837.5	1,001.6
35	IRB-Brasil Resseguros S.A.	Brazil		810.6	799.4
36	Deutsche Rueckversicherung AG	Germany		772.2	893.5
37	Taiping Reinsurance Co., Ltd.	Hong Kong		735.6	437.2
38	Berkley (W.R.) Corp.	U.S.		651.3	749.6
39	Montpelier Re Holdings Ltd.	Bermuda		650.9	603.1
40	African Reinsurance Corp.	Nigeria		624.4	569.1
	Total:			**194,863.2**	**199,784.4**

NA = Not Available
NM = Not Meaningful

1. 2013 Combined Ratio differs from GRH 2014 due to restatement in Swiss Re's annual accounts.
2. Adjusted Shareholders' Funds are for the group as a whole, including both its primary and reinsurance operations. Adjusted Shareholders' Funds are the same number for 2013 and 2014.
3. The combined ratio includes primary business.
4. Net Premium Written, pretax operating income and the combined ratio relate to reinsurance business only; all other items include direct business. The data presented is based on the published pro forma accounts for the Market, which represents an aggregation of all syndicates participating at Lloyd's. As such, some premium included for Lloyd's may also be included by other groups that consolidate their Lloyd's operations.
5. 2014 Net Reinsurance Premium written is the sum of the three major companies in the group without consolidation adjustment. 2013 data is the sum of three major companies.
6. Previously called NKSJ Holdings.
7. Figures represent Tokio Marine & Nichido Fire Insurance Co and exclude the group's other reinsurance subsidiaries.
8. Adjusted shareholders' funds represent the group as a whole, including both its primary and reinsurance operations.
9. Pretax Operating Income and Return on Revenue slightly differ from GRH 2014 due to correction of a typo. Figures include intra-group reinsurance business.
10. Net reinsurance premium written and pretax operating income represent reinsurance business only. Other figures include primary and reinsurance business.

Pretax operating income (Mil. $)		Combined ratio (%)		Total adjusted shareholders' funds (Mil. $)		Return on revenue (%)	
2014	**2013**	**2014**	**2013**	**2014**	**2013**	**2014**	**2013**
2,904.0	3,977.0	85.5	85.7	33,989.1	31,535.3	8.1	11.8
3,927.7	5,534.9	92.7	92.1	35,260.5	34,366.0	10.0	11.9
NA	NA	92.7	90.2	129,000.0	129,000.0	NA	NA
1,484.9	1,356.7	95.0	95.1	10,014.0	8,963.0	8.9	7.3
922.7	801.3	91.4	93.8	6,921.8	6,801.6	7.3	6.2
1,941.8	2,178.4	81.3	80.1	35,085.6	33,618.1	16.1	17.4
941.9	544.6	NM	NM	7,023.5	5,935.5	8.8	5.3
727.7	554.0	98.3	98.8	3,443.2	3,304.6	8.4	7.1
838.4	813.9	86.2	85.3	7,048.9	6,709.5	13.7	14.3
1,302.8	1,248.9	82.8	84.5	7,451.1	6,968.3	22.8	23.6
140.4	245.6	99.8	97.1	1,859.5	1,594.3	3.8	6.6
581.2	521.0	89.6	89.8	5,130.0	4,500.0	15.9	14.6
NA	NA	NA	NA	31,571.8	29,207.8	NA	NA
NA	NA	NA	NA	16,794.6	17,124.5	NA	NA
243.4	213.8	92.9	96.5	1,433.5	1,390.3	9.2	6.7
2,207.5	1,425.4	NA	NA	21,517.9	20,046.4	NA	NA
179.0	155.2	97.9	97.5	1,240.7	1,123.8	7.5	7.4
452.1	385.5	109.7	108.3	2,079.3	1,836.6	17.7	14.4
NA	NA	81.3	82.8	5,821.1	5,868.0	NA	NA
307.1	398.7	101.4	97.8	6,840.9	6,872.4	12.8	16.4
157.9	134.6	66.8	75.0	3,991.5	3,783.0	8.1	7.5
NA	NA	73.3	81.4	NA	NA	NA	NA
175.7	181.9	93.7	95.3	2,476.5	2,434.9	9.5	9.0
30.3	32.0	87.8	83.6	2,302.8	1,634.0	1.8	1.8
644.6	704.1	69.9	71.6	6,156.4	6,635.1	37.8	36.6
543.1	577.6	77.5	76.3	3,983.2	3,730.7	31.9	31.1
659.6	705.7	73.6	70.2	5,354.6	5,020.8	43.5	48.6
746.0	755.3	72.3	65.9	NA	NA	45.0	47.2
486.6	589.8	NA	NA	3,588.0	3,704.1	398.7	512.0
353.7	330.8	77.6	76.4	3,419.3	3,299.6	27.7	26.1
336.8	313.8	74.6	76.8	3,185.2	2,886.5	29.3	25.6
NA	NA	77.4	75.8	3,778.3	3,519.8	NA	NA
200.1	170.7	76.5	82.5	2,018.6	1,881.7	22.0	18.3
NA	NA	37.9	32.6	3,465.7	3,504.4	NA	NA
335.8	260.7	63.8	79.5	1,203.1	1,136.2	30.2	28.7
0.6	-79.9	108.1	115.6	789.0	838.0	0.1	-8.3
15.9	14.8	89.3	96.5	576.0	502.3	2.1	3.1
115.7	110.4	96.0	97.0	4,589.9	4,336.0	15.2	13.6
208.6	277.5	65.6	56.1	1,648.2	1,642.1	30.1	41.8
120.3	87.2	89.9	93.3	722.2	664.3	17.7	14.2
24,234.0	**25,521.8**	**89.0**	**89.1**	**422,775.4**	**407,919.5**	**12.9**	**13.2**

11. 2013 numbers differ from GRH 2014 due to a segment reclassification in 2014. During the 2014 first quarter, Arch formed a mortgage segment, consisting of mortgage insurance and reinsurance business. Prior to the formation of the mortgage segment, such amounts were reflected in the reinsurance segment.

12. 2013 figures except Net Premium Written differ from GRH 2014 due to restatement in line with S&P's definitions for GRH publication.

13. 2013 Pretax Operating Income, Combined Ratio and Return on Revenue differ from GRH 2014 due to restatement for consistency across Aspen Group entities.

14. 2013 numbers differ from GRH 2014 due to exclusion of non-reinsurance related portions. Adjusted shareholders' funds represent the group as a whole, including both its primary and reinsurance operations.

15. 2013 Pretax Operating Income and Return on Revenue differ from GRH 2014 due to the exclusion of foreign currency losses on investments from the pre-tax operating income and other income lines, consistent with GRH definitions.

Notes on the tables

To bring you the 2015 edition of Global Reinsurance Highlights, Standard & Poor's Ratings Services sought data on around 150 reinsurance organizations from over 40 countries. As in previous years, the data is based on survey responses from reinsurance organizations worldwide.

To ensure consistency, we requested that respondents complied with clear guidance on the definition of the financial items required. In addition, Standard & Poor's attempted to verify the veracity of the data submitted with reference to publicly available data sources, insofar as this was possible.

Our aim in producing this data is to provide market participants with an indication of the ongoing reinsurance capacity available in each market. Hence, we try to exclude intragroup reinsurances as far as possible. Companies that have not been able to exclude intragroup reinsurance are highlighted in the footnotes on pages pages 74 and 75.

One of the challenges has been to separate reinsurance from primary insurance business, especially when the reinsurance operation is a division within a company and not a distinct operation. While, generally speaking, all the premium data relates to a company's reinsurance premiums written, in some cases the other metrics will also include primary business. These cases can be identified through the footnotes to the tables, although if we believe the metrics provided by the company are not representative of the company's reinsurance operations, we have marked

Rating as of July 21, 2015	Company	Footnotes	Net reinsurance premiums written (Mil. $)		
			2014	2013	Change (%)
AUSTRALIA					
AA-	Swiss Re Life & Health Australia Ltd.		866.7	694.2	24.8
AA-	Munich Reinsurance Co. of Australasia Ltd.	1	463.1	457.3	1.3
AA-	Hannover Life Re of Australasia Ltd.		380.4	344.3	10.5
AA+	General Reinsurance Life Australia Ltd.		189.6	195.3	-2.9
AA+	General Reinsurance Australia Ltd.		60.8	69.8	-12.9
A+	SCOR Global Life Australia Pty Ltd.	2	44.5	13.1	239.4
	Total:		**2,005.1**	**1,774.0**	**13.0**
BAHRAIN					
A-	Trust International Insurance & Reinsurance Co. B.S.C.	3	286.6	251.0	14.2
A+	Hannover Re Takaful BSC		201.1	127.4	57.9
	Total:		**487.7**	**378.3**	**28.9**
BERMUDA					
A+	Everest Reinsurance (Bermuda) Ltd.		2,773.2	2,633.1	5.3
BBB+	Maiden Re		2,458.1	2,096.3	17.3
A	Validus Reinsurance Ltd. (Bermuda)		1,022.1	1,028.3	-0.6
A+	Arch Reinsurance Ltd.	4	969.8	1,063.2	-8.8
AA	ACE Tempest Reinsurance Ltd.		934.9	991.1	-5.7
A+	XL Re Ltd.		693.3	794.0	-12.7
AA-	Renaissance Reinsurance Ltd.		639.1	769.2	-16.9
A-	Platinum Underwriters Bermuda Ltd.	5	492.1	567.1	-13.2
A+	Partner Reinsurance Company Ltd.		462.6	446.8	3.5
A+	AXIS Specialty Ltd.	7	401.1	500.5	-19.9
AA-	Hannover Re Bermuda Ltd.	6	395.0	314.1	25.8

the metric as N.A. (not applicable). For companies that report in currencies other than the U.S. dollar, we have converted the reported data at year-end exchange rates.

Standard & Poor's has endeavored to collect the data underlying each group or entity's combined ratio in order to calculate this metric in a comparable manner. The combined ratios presented in Global Reinsurance Highlights have been calculated as: (net losses incurred + net underwriting expenses)/net premiums earned.

The combined ratio of any entity that writes purely life reinsurance has been marked as N.M. (not meaningful), as Standard & Poor's does not consider this to be an accurate measure of a life reinsurer's profitability. For those groups or entities writing both non-life and life reinsurance business, the combined ratio reflects non-life business only.

The main group and country listing for each entity surveyed is representative of that group or company's total reinsurance business written, whether it be life, non-life, or a combination of both.

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Pretax operating income (Mil. $)		Combined ratio (%)		Total adjusted shareholders' funds (Mil. $)			Return on revenue (%)	
2014	2013	2014	2013	2014	2013	Change (%)	2014	2013
80.5	-214.8	NM	NM	950.2	873.2	8.8	8.4	-28.8
-384.3	-104.1	NM	NM	486.1	550.0	-11.6	-64.3	-20.5
-29.5	14.4	NM	NM	390.1	400.3	-2.6	-6.7	3.7
-10.3	19.4	NM	NM	92.7	103.9	-10.8	-4.6	9.5
43.9	45.0	80.1	68.5	319.9	343.4	-6.8	43.0	59.1
-4.0	0.6	NM	NM	70.8	40.7	73.8	-8.4	4.2
-303.6	**-239.4**	**80.1**	**68.5**	**2,309.7**	**2,311.7**	**-0.1**	**-12.8**	**-12.3**
9.6	16.8	96.4	93.2	386.2	305.1	26.6	3.5	6.8
19.0	12.9	119.5	112.9	141.4	122.7	15.2	9.3	9.3
28.7	**29.6**	**106.2**	**100.0**	**527.7**	**427.8**	**23.3**	**6.0**	**7.7**
744.1	701.2	81.2	81.8	3,017.7	2,953.5	2.2	25.5	25.6
179.0	155.2	97.9	97.5	1,240.7	1,123.8	10.4	7.5	7.4
485.0	531.9	63.7	63.2	3,329.6	3,511.8	-5.2	43.0	41.8
613.0	655.3	72.6	66.5	3,989.5	3,773.3	5.7	50.3	54.0
599.8	611.7	72.3	65.9	NA	NA	NA	44.6	48.5
NA	NA	59.2	54.7	NA	NA	NA	NA	0.0
NA	NA	51.1	43.0	1,800.0	1,800.0	NA	NA	NA
163.1	204.4	75.1	67.6	1,738.0	1,746.7	-0.5	28.2	32.5
395.4	442.0	54.9	40.2	3,655.0	3,685.9	-0.8	56.6	67.5
NA	NA	50.5	66.0	4,298.2	4,452.8	-3.5	NA	NA
227.7	149.5	58.1	63.6	1,471.5	1,046.6	40.6	52.7	43.2

GLOBAL REINSURERS BY COUNTRY

Rating as of July 21, 2015	Company	Footnotes	Net reinsurance premiums written (Mil. $)		
			2014	2013	Change (%)
AA	ACE Tempest Life Reinsurance, Ltd.		262.1	283.6	-7.6
AA-	DaVinci Reinsurance Ltd.		258.5	340.1	-24.0
A	Catlin Insurance Co. Ltd.	7	234.7	288.9	-18.7
A	Aspen Insurance Ltd.		222.9	200.9	11.0
A-	International General Insurance Co. Ltd.	8	184.4	181.2	1.7
A+	MS Frontier Reinsurance Ltd.		172.1	158.7	8.4
A-	Lancashire Insurance Co. Ltd.	9	128.3	121.7	5.4
NR	Hiscox Insurance Co. (Bermuda) Ltd.	5	115.7	206.8	-44.1
AA	Top Layer Reinsurance Ltd.		24.3	34.9	-30.4
	Total:		**12,844.2**	**13,020.7**	**-1.4**
BOSNIA AND HERZEGOVINA					
NR	Bosna Re		16.5	17.7	-6.4
	Total:		**16.5**	**17.7**	**-6.4**
BRAZIL					
NR	IRB-Brasil Resseguros S.A.		810.6	799.4	1.4
BBB+	AGCS Re Brazil		103.2	62.5	65.0
brAA-	Austral Resseguradora S.A.		74.5	60.7	22.7
brA+	Terra Brasis Resseguros		12.8	4.8	168.0
	Total:		**1,001.1**	**927.4**	**7.9**
CANADA					
AA-	Munich Reinsurance Co. of Canada		204.8	193.9	5.7
A+	SCOR Canada Reinsurance Co.		117.0	150.0	-22.0
	Total:		**321.8**	**343.9**	**-6.4**
CHINA					
A+	China Property & Casualty Reinsurance Co. Ltd.		4,647.6	4,596.6	1.1
	Total:		**4,647.6**	**4,596.6**	**1.1**
CROATIA					
NR	Croatia Lloyd		16.6	19.7	-15.9
	Total:		**16.6**	**19.7**	**-15.9**

Pretax operating income (Mil. $)		Combined ratio (%)		Total adjusted shareholders' funds (Mil. $)			Return on revenue (%)	
2014	2013	2014	2013	2014	2013	Change (%)	2014	2013
146.2	143.6	NA	NA	NA	NA	NA	46.7	42.2
NA	NA	29.4	39.6	1,453.8	1,562.4	-6.9	NA	NA
109.5	93.6	36.6	50.5	4,064.2	3,870.4	5.0	19.6	20.9
224.8	151.6	32.2	30.3	2,250.5	2,070.6	8.7	60.6	44.2
24.5	24.7	87.1	86.3	275.8	257.7	7.0	12.2	13.0
73.6	85.3	57.8	50.1	996.7	919.8	8.4	43.4	54.0
258.6	202.6	22.1	48.7	1,094.8	1,287.1	-14.9	54.8	41.3
68.3	111.1	46.3	51.0	896.6	947.2	-5.3	47.5	52.4
NA	NA	21.6	20.4	121.8	101.0	20.6	NA	NA
4,312.7	**4,263.7**	**71.4**	**68.9**	**35,694.6**	**35,110.5**	**1.7**	**33.3**	**34.5**
1.1	1.5	80.7	83.4	16.1	17.5	-8.2	6.8	8.4
1.1	**1.5**	**80.7**	**83.4**	**16.1**	**17.5**	**-8.2**	**6.8**	**8.4**
335.8	267.9	63.8	79.5	1,203.1	1,136.2	5.9	30.2	29.5
-13.2	-14.9	113.9	200.7	78.0	48.6	60.5	-13.2	-82.7
11.0	3.0	79.9	87.1	85.3	58.1	46.8	13.8	5.3
-2.5	-5.1	130.4	272.3	37.0	40.9	-9.5	-20.8	-77.7
331.0	**250.9**	**49.0**	**75.6**	**1,403.4**	**1,283.8**	**9.3**	**25.4**	**25.3**
54.5	40.5	85.5	94.7	247.9	256.0	-3.2	24.6	18.1
7.6	3.5	93.5	97.7	134.2	140.6	-4.6	5.6	2.1
62.1	**44.0**	**88.5**	**96.0**	**382.1**	**396.6**	**-3.7**	**17.4**	**11.4**
283.6	252.0	99.6	99.8	2,393.7	1,949.5	22.8	5.7	5.6
283.6	**252.0**	**99.6**	**99.8**	**2,393.7**	**1,949.5**	**22.8**	**5.7**	**5.6**
-1.7	5.7	115.2	78.9	39.9	55.0	-27.4	-6.1	17.4
-1.7	**5.7**	**115.2**	**78.9**	**39.9**	**55.0**	**-27.4**	**-6.1**	**17.4**

GLOBAL REINSURERS BY COUNTRY

Rating as of July 21, 2015	Company	Footnotes	Net reinsurance premiums written (Mil. $)		
			2014	2013	Change (%)
CZECH REPUBLIC					
A+	VIG Re		287.3	342.6	-16.1
	Total:		**287.3**	**342.6**	**-16.1**
FRANCE					
A+	SCOR Global Life SE		2,275.7	2,315.8	-1.7
A+	SCOR SE		1,914.6	1,858.7	3.0
A+	SCOR Global P&C SE		1,867.2	2,117.6	-11.8
AA	Caisse Centrale de Reassurance		1,557.5	1,668.1	-6.6
	Total:		**7,615.0**	**7,960.2**	**-4.3**
GERMANY					
AA-	Munich Reinsurance Co.		25,272.4	31,445.1	-19.6
AA-	Hannover Rueckversicherung AG		10,469.4	11,437.8	-8.5
AA+	GR-AG		2,973.9	2,981.1	-0.2
AA-	E+S Rueckversicherung AG		2,189.5	2,970.3	-26.3
AA-	R+V Versicherung AG	10	2,073.4	2,045.9	1.3
AA	Allianz SE	11	555.6	511.9	8.6
A+	Deutsche Rueckversicherung AG	12	530.6	576.0	-7.9
A+	DEVK	13	315.5	303.5	4.0
	Total:		**44,380.3**	**52,271.5**	**-15.1**
GHANA					
NR	Ghana Reinsurance Co Ltd		29.0	28.1	3.3
	Total:		**29.0**	**28.1**	**3.3**
HONG KONG					
A	Taiping Reinsurance Co Ltd.		735.6	437.2	68.3
NR	Peak Reinsurance Company Limited		279.7	97.0	188.5
A+	SCOR Reinsurance Company (Asia) Ltd.	14	58.4	70.6	-17.2
	Total:		**1,073.8**	**604.7**	**77.6**
INDIA					
NR	General Ins. Corp. of India		2,216.1	2,211.0	0.2
	Total:		**2,216.1**	**2,211.0**	**0.2**

	Pretax operating income (Mil. $)		Combined ratio (%)		Total adjusted shareholders' funds (Mil. $)			Return on revenue (%)	
	2014	2013	2014	2013	2014	2013	Change (%)	2014	2013
	4.7	6.5	96.2	96.6	162.3	171.0	-5.1	1.5	1.8
	4.7	**6.5**	**96.2**	**96.6**	**162.3**	**171.0**	**-5.1**	**1.5**	**1.8**
	218.8	254.7	NM	NM	1,000.5	1,148.3	-12.9	8.7	9.6
	498.4	369.0	106.2	126.7	3,396.5	3,648.6	-6.9	21.5	16.8
	341.6	476.4	94.6	98.9	2,820.3	2,969.8	-5.0	16.5	19.3
	644.6	704.1	69.9	71.6	6,156.4	6,635.1	-7.2	37.8	36.6
	1,703.4	**1,804.2**	**91.5**	**99.5**	**13,373.6**	**14,401.8**	**-7.1**	**19.8**	**19.5**
	2,662.7	4,864.1	96.0	94.6	36,192.0	37,418.1	-3.3	9.3	13.5
	1,013.6	1,069.3	107.3	102.6	8,458.2	8,213.3	3.0	8.3	8.2
	339.8	192.1	99.9	117.4	4,336.9	4,389.6	-1.2	10.8	5.9
	377.5	138.1	102.9	113.9	2,804.9	2,558.3	9.6	15.2	4.2
	307.1	398.7	101.4	97.8	6,840.9	6,872.4	-0.5	12.8	16.4
	56.8	59.6	93.2	91.9	NA	NA	NA	10.8	10.7
	-0.4	-77.7	110.6	123.7	634.6	679.4	-6.6	-0.1	-12.4
	119.6	154.2	94.5	99.5	1,268.0	1,393.5	-9.0	22.6	27.3
	4,876.7	**6,798.4**	**97.4**	**97.2**	**60,535.7**	**61,524.6**	**-1.6**	**9.7**	**11.4**
	5.3	15.2	79.3	80.7	69.4	75.1	-7.7	11.6	34.4
	5.3	**15.2**	**79.3**	**80.7**	**69.4**	**75.1**	**-7.7**	**11.6**	**34.4**
	15.9	14.8	89.3	96.5	576.0	502.3	14.7	2.1	3.1
	46.7	104.4	101.2	138.3	688.4	652.7	5.5	18.9	62.0
	-2.1	9.3	65.1	43.0	248.4	238.7	4.1	-2.6	12.9
	60.6	**128.5**	**90.0**	**92.8**	**1,512.8**	**1,393.7**	**8.5**	**5.5**	**18.0**
	452.1	385.5	109.7	108.3	2,079.3	1,836.6	13.2	17.7	14.4
	452.1	**385.5**	**109.7**	**108.3**	**2,079.3**	**1,836.6**	**13.2**	**17.7**	**14.4**

GLOBAL REINSURERS BY COUNTRY

Rating as of July 21, 2015	Company	Footnotes	Net reinsurance premiums written (Mil. $)		
			2014	2013	Change (%)
IRAN					
NR	Iranian Reinsurance Company		13.1	8.4	55.3
	Total:		**13.1**	**8.4**	**55.3**
IRELAND					
A+	SCOR Global Life Reinsurance Ireland Ltd.	15	3,409.6	2,614.6	30.4
AA-	Hannover Re (Ireland) Ltd.		1,975.2	2,357.7	-16.2
A+	Partner Reinsurance Europe SE		1,558.6	1,668.6	-6.6
A+	AXIS Re SE		853.6	855.3	-0.2
A+	XL Re Europe SE		575.6	605.3	-4.9
NR	Atradius Reinsurance Ltd.		484.9	492.8	-1.6
A+	Arch Reinsurance Europe Underwriting Ltd		50.7	45.8	10.8
	Total:		**8,908.2**	**8,640.0**	**3.1**
JAPAN					
A+	Sompo Japan Nipponkoa Ins Inc	16	2,853.0	2,159.6	32.1
AA-	Tokio Marine & Nichido Fire Insurance Co. Ltd.		2,496.1	2,757.9	-9.5
A+	Mitsui Sumitomo Insurance Co. Ltd.		1,635.2	1,790.5	-8.7
A+	Aioi Nissay Dowa Insurance		1,513.0	1,694.1	-10.7
A+	Toa Reinsurance Co.		1,383.4	1,434.0	-3.5
	Total:		**9,880.7**	**9,836.2**	**0.5**
KAZAKHSTAN					
BB+	Eurasia Insurance Co.		80.7	78.2	3.2
	Total:		**80.7**	**78.2**	**3.2**
KENYA					
NR	ZEP Re		105.9	84.0	26.1
	Total:		**105.9**	**84.0**	**26.1**
KOREA					
A	Korean Reinsurance Co.		3,582.1	3,574.7	0.2
	Total:		**3,582.1**	**3,574.7**	**0.2**

	Pretax operating income (Mil. $)		Combined ratio (%)		Total adjusted shareholders' funds (Mil. $)			Return on revenue (%)	
	2014	2013	2014	2013	2014	2013	Change (%)	2014	2013
	15.1	17.4	86.6	80.2	89.9	93.1	-3.4	57.2	70.8
	15.1	**17.4**	**86.6**	**80.2**	**89.9**	**93.1**	**-3.4**	**57.2**	**70.8**
	12.6	382.1	NM	NM	510.8	572.7	-10.8	0.4	14.5
	107.3	56.9	104.9	109.8	1,765.2	1,874.2	-5.8	4.7	2.1
	279.6	176.4	71.6	76.4	2,168.8	2,247.9	-3.5	17.0	10.0
	NA	NA	85.3	93.9	609.3	574.8	6.0	NA	NA
	NA	NA	74.7	93.9	NA	NA	NA	NA	NA
	36.1	68.8	92.7	88.7	389.9	449.3	-13.2	7.6	13.2
	NA	NA	74.2	116.4	NA	NA	NA	NA	NA
	435.6	**684.3**	**88.2**	**95.2**	**5,444.0**	**5,718.8**	**-4.8**	**5.6**	**9.0**
	NA	NA	NA	NA	16,794.6	10,359.1	62.1	NA	NA
	2,207.5	1,425.4	NA	NA	21,517.9	20,046.4	7.3	NA	NA
	NA	NA	NA	NA	18,586.7	16,810.0	10.6	NA	NA
	409.6	81.2	NA	NA	8,993.6	8,293.6	8.4	NA	NA
	140.8	106.9	95.6	97.0	1,858.1	1,879.1	-1.1	9.6	7.0
	2,757.9	**1,613.6**	**95.6**	**97.0**	**67,750.8**	**57,388.3**	**18.1**	**9.6**	**7.0**
	30.5	39.0	61.4	58.2	338.8	346.4	-2.2	26.8	32.9
	30.5	**39.0**	**61.4**	**58.2**	**338.8**	**346.4**	**-2.2**	**26.8**	**32.9**
	8.5	8.4	92.0	92.1	143.6	105.7	35.8	7.5	9.1
	8.5	**8.4**	**92.0**	**92.1**	**143.6**	**105.7**	**35.8**	**7.5**	**9.1**
	140.4	245.6	99.8	97.1	1,859.5	1,594.3	16.6	3.8	6.6
	140.4	**245.6**	**99.8**	**97.1**	**1,859.5**	**1,594.3**	**16.6**	**3.8**	**6.6**

GLOBAL REINSURERS BY COUNTRY

Rating as of July 21, 2015	Company	Footnotes	Net reinsurance premiums written (Mil. $) 2014	2013	Change (%)
KUWAIT					
NR	Kuwait Reinsurance Co. K.S.C.		103.8	129.1	-19.6
	Total:		**103.8**	**129.1**	**-19.6**
LEBANON					
NR	Arab Reinsurance Co.		59.3	66.5	-10.9
	Total:		**59.3**	**66.5**	**-10.9**
LUXEMBOURG					
AA-	Swiss Re Europe S.A.		6,104.5	7,200.5	-15.2
	Total:		**6,104.5**	**7,200.5**	**-15.2**
NIGERIA					
A-	African Reinsurance Corp.	17	434.0	390.9	11.0
	Total:		**434.0**	**390.9**	**11.0**
PANAMA					
BBB	Istmo Compania de Reaseguros Inc.		112.5	125.7	-10.5
	Total:		**112.5**	**125.7**	**-10.5**
POLAND					
NR	Polskie Towarzystwo Reasekuracji S.A.		36.7	92.0	-60.1
	Total:		**36.7**	**92.0**	**-60.1**
QATAR					
A	Qatar Reinsurance Co LLC		178.2	131.1	35.9
	Total:		**178.2**	**131.1**	**35.9**
RUSSIA					
BB+	Ingosstrakh Insurance Co.		59.5	72.7	-18.2
NR	Transsib Re		14.4	20.6	-30.3
NR	Russian Re Co. Ltd.		9.9	15.6	-36.6
	Total:		**83.8**	**108.9**	**-23.1**

	Pretax operating income (Mil. $)		Combined ratio (%)		Total adjusted shareholders' funds (Mil. $)			Return on revenue (%)	
	2014	2013	2014	2013	2014	2013	Change (%)	2014	2013
	-1.7	6.4	101.3	95.0	137.1	145.3	-5.7	-1.5	5.0
	-1.7	**6.4**	**101.3**	**95.0**	**137.1**	**145.3**	**-5.7**	**-1.5**	**5.0**
	-1.7	2.1	110.9	103.2	92.6	96.2	-3.7	-2.4	2.8
	-1.7	**2.1**	**110.9**	**103.2**	**92.6**	**96.2**	**-3.7**	**-2.4**	**2.8**
	496.8	216.6	76.3	94.2	2,033.5	1,566.8	29.8	21.0	5.6
	496.8	**216.6**	**76.3**	**94.2**	**2,033.5**	**1,566.8**	**29.8**	**21.0**	**5.6**
	111.8	76.9	79.6	83.1	668.6	612.3	9.2	23.6	18.3
	111.8	**76.9**	**79.6**	**83.1**	**668.6**	**612.3**	**9.2**	**23.6**	**18.3**
	12.3	11.8	91.7	93.8	161.4	152.8	5.7	9.8	9.5
	12.3	**11.8**	**91.7**	**93.8**	**161.4**	**152.8**	**5.7**	**9.8**	**9.5**
	0.1	-9.5	98.9	112.8	63.8	69.8	-8.6	0.1	-10.2
	0.1	**-9.5**	**98.9**	**112.8**	**63.8**	**69.8**	**-8.6**	**0.1**	**-10.2**
	27.7	11.2	108.2	118.5	225.6	166.2	35.8	17.0	9.1
	27.7	**11.2**	**108.2**	**118.5**	**225.6**	**166.2**	**35.8**	**17.0**	**9.1**
	-31.9	21.3	180.6	90.9	420.4	672.4	-37.5	-76.7	32.1
	-2.9	0.3	111.3	83.8	12.4	20.2	-38.4	-19.2	1.2
	-1.3	-0.4	114.3	103.0	13.7	21.7	-36.7	-11.4	-2.8
	-36.1	**21.1**	**156.1**	**91.3**	**446.5**	**714.2**	**-37.5**	**-53.1**	**20.6**

GLOBAL REINSURERS BY COUNTRY

Rating as of July 21, 2015	Company	Footnotes	Net reinsurance premiums written (Mil. $)		
			2014	2013	Change (%)
SIERRA LEONE					
NR	WAICA Re		22.5	15.3	47.3
	Total:		**22.5**	**15.3**	**47.3**
SINGAPORE					
A-	Asia Capital Reinsurance Group Pte Ltd		371.7	489.7	-24.1
A+	SCOR Reinsurance Asia-Pacific		281.2	253.0	11.1
NR	Singapore Reinsurance Corporation Ltd.		43.1	41.8	3.1
	Total:		**696.0**	**784.5**	**-11.3**
SLOVENIA					
BBB+	Pozavarovalnica Sava, d.d.	18	89.1	124.1	-28.2
A-	Triglav Re		70.4	77.9	-9.7
	Total:		**159.5**	**202.0**	**-21.1**
SOUTH AFRICA					
AA-	Munich Reinsurance Co. of Africa Ltd.		248.6	234.8	5.9
AA+	General Reinsurance Africa Ltd.		176.0	186.5	-5.7
BBB+	Hannover Reinsurance Africa Ltd.		144.2	124.4	15.9
BBB+	Hannover Life Reassurance Africa Ltd.		138.3	159.6	-13.3
NR	Swiss Re Life & Health Africa Ltd.		137.5	132.3	4.0
A-	African Re Corp. (South Africa) Ltd.		53.7	52.3	2.7
	Total:		**898.3**	**889.9**	**0.9**
SPAIN					
A	Mapfre Re, Compania de Reaseguros, S.A.		2,597.0	2,886.5	-10.0
A-	Nacional de Reaseguros S.A.		423.9	427.1	-0.7
	Total:		**3,020.9**	**3,313.6**	**-8.8**
SWITZERLAND					
AA-	Swiss Reinsurance Company Ltd.	19	9,755.1	11,122.1	-12.3
A+	SCOR Switzerland AG	20	1,104.7	1,281.8	-13.8
AA-	New Reinsurance Co.		1,018.6	1,228.2	-17.1
AA-	Tokio Millennium Re AG	21	953.4	773.6	23.2
A+	Deutsche Rueckversicherung Schweiz AG		244.0	318.9	-23.5

	Pretax operating income (Mil. $)		Combined ratio (%)		Total adjusted shareholders' funds (Mil. $)			Return on revenue (%)	
	2014	2013	2014	2013	2014	2013	Change (%)	2014	2013
	1.9	1.2	91.5	90.3	33.6	29.9	12.4	9.1	9.5
	1.9	**1.2**	**91.5**	**90.3**	**33.6**	**29.9**	**12.4**	**9.1**	**9.5**
	25.4	33.9	83.0	68.9	696.8	700.3	-0.5	5.5	7.6
	24.4	49.7	103.0	85.3	282.4	345.4	-18.3	8.5	12.0
	1.5	1.6	58.2	61.5	179.1	177.4	1.0	2.9	3.2
	51.3	**85.2**	**89.1**	**74.2**	**1,158.3**	**1,223.2**	**-5.3**	**6.4**	**9.4**
	31.2	20.9	89.3	93.4	313.8	339.0	-7.4	20.1	11.4
	2.2	5.5	96.7	92.7	82.9	72.9	13.7	2.9	6.6
	33.4	**26.4**	**91.8**	**93.2**	**396.7**	**411.9**	**-3.7**	**14.4**	**9.9**
	32.8	37.8	96.1	86.3	237.6	227.7	4.3	9.7	10.7
	27.4	38.3	NM	NM	91.3	78.7	16.0	13.8	18.5
	0.9	12.3	100.4	90.2	64.8	70.2	-7.6	0.8	11.5
	9.6	27.3	NM	NM	52.7	50.6	4.1	6.5	15.9
	3.4	14.3	NM	NM	31.0	32.8	-5.2	2.3	10.1
	8.5	10.3	107.8	102.7	53.6	52.0	3.1	12.6	15.8
	82.6	**140.3**	**98.8**	**89.4**	**531.1**	**511.9**	**3.7**	**8.2**	**13.4**
	244.0	214.1	93.0	96.3	1,195.7	1,280.2	-6.6	9.6	6.9
	47.5	48.4	75.6	91.6	321.8	392.4	-100.0	10.7	10.2
	291.5	**262.5**	**90.3**	**95.7**	**1,517.5**	**1,672.6**	**-9.3**	**9.8**	**7.3**
	2,192.2	6,187.7	84.3	77.7	17,594.9	16,901.8	4.1	21.4	41.5
	292.6	384.8	80.9	77.6	1,498.3	1,594.3	-6.0	28.3	30.7
	130.7	216.4	93.7	98.1	829.5	913.4	-9.2	11.6	15.5
	74.5	142.6	97.4	79.5	1,199.3	1,273.1	-5.8	9.0	20.4
	4.3	8.7	104.1	102.1	242.0	262.9	-8.0	1.6	2.5

GLOBAL REINSURERS BY COUNTRY

Rating as of July 21, 2015	Company	Footnotes	Net reinsurance premiums written (Mil. $)		
			2014	2013	Change (%)
NR	SIGNAL IDUNA Rueckversicherungs AG		157.5	178.4	-11.7
A+	XL Re Latin America Ltd.		87.9	111.1	-20.9
A-	Echo Rueckversicherungs-AG		67.5	52.2	29.5
AA-	European Reinsurance Co. of Zurich	19	15.5	-117.1	-113.2
	Total:		**13,404.1**	**14,949.1**	**-10.3**
TAIWAN					
A	Central Reinsurance Corp.		480.9	491.4	-2.1
	Total:		**480.9**	**491.4**	**-2.1**
TURKEY					
trAA+	Milli Reasurans T.A.S.		354.6	373.7	-5.1
	Total:		**354.6**	**373.7**	**-5.1**
U.K.					
A+	Lloyd's	22	10,415.7	11,329.2	-8.1
A	Aspen Insurance U.K. Ltd.		893.1	861.6	3.7
A+	QBE Re (Europe) Ltd		313.1	425.6	-26.4
A+	QBE Insurance (Europe) Ltd.		247.1	204.2	21.0
AA-	Tokio Millennium Re (UK) Ltd		218.2	188.1	16.0
AA-	Great Lakes Reinsurance (U.K.) PLC		188.7	194.6	-3.0
A+	SCOR U.K. Co. Ltd.		153.9	189.9	-19.0
AA+	Faraday Reinsurance Co. Ltd.		115.0	123.5	-6.9
	Total:		**12,544.9**	**13,516.6**	**-7.2**
U.S.					
AA+	National Indemnity Co.	23	25,905.0	5,022.7	415.8
AA-	Swiss Reinsurance America Corp.		4,291.1	4,518.8	-5.0
A+	Transatlantic Reinsurance Co.		2,986.8	2,977.0	0.3
AA+	Berkshire Hathaway Life Insurance Co. of NE	24	2,629.0	3,225.0	-18.5
AA-	Swiss Re Life & Health America Inc.		2,525.9	3,424.7	-26.2
AA-	Munich Reinsurance America, Inc.		2,325.2	2,544.4	-8.6
A+	Everest Reinsurance Co.		2,121.8	2,024.4	4.8
A-	Odyssey Reinsurance Co. (U.S.)		2,022.3	2,075.9	-2.6
AA-	Munich American Reassurance Co.		1,451.5	261.1	455.9

Pretax operating income (Mil. $)		Combined ratio (%)		Total adjusted shareholders' funds (Mil. $)			Return on revenue (%)	
2014	2013	2014	2013	2014	2013	Change (%)	2014	2013
10.0	10.4	98.6	99.1	173.1	190.4	-9.1	5.8	5.2
NA	NA	77.7	123.7	NA	NA	NA	NA	NA
-4.0	2.9	106.6	74.1	83.6	73.4	13.9	-6.0	5.8
-29.8	-321.1	360.4	28.5	4,029.8	3,592.5	12.2	-17.5	139.6
2,670.5	**6,632.5**	**86.0**	**81.3**	**25,650.6**	**24,801.7**	**3.4**	**19.2**	**35.6**
23.5	16.9	109.9	98.6	430.6	487.2	-11.6	4.7	3.4
23.5	**16.9**	**109.9**	**98.6**	**430.6**	**487.2**	**-11.6**	**4.7**	**3.4**
1.1	5.0	114.1	113.5	324.4	328.3	-1.2	0.3	1.3
1.1	**5.0**	**114.1**	**113.5**	**324.4**	**328.3**	**-1.2**	**0.3**	**1.3**
1,941.8	2,178.4	81.3	80.1	35,085.6	33,618.1	4.4	16.1	17.4
81.6	6.2	90.6	99.3	999.0	1,006.4	-0.7	8.9	0.7
21.0	132.0	89.1	72.4	716.7	825.8	-13.2	6.3	29.6
-11.2	38.7	100.9	115.4	379.3	266.1	42.5	-4.1	13.8
20.3	27.2	95.8	90.7	325.7	346.2	-5.9	9.9	16.6
19.8	16.0	120.7	120.3	559.9	570.3	-1.8	7.9	6.3
5.4	15.1	93.7	91.7	240.4	238.0	1.0	3.3	7.5
-45.7	112.0	110.8	30.9	607.2	632.7	-4.0	-54.5	74.8
2,032.9	**2,525.7**	**83.8**	**82.2**	**38,913.9**	**37,503.6**	**3.8**	**14.2**	**16.9**
1,339.0	1,335.6	88.7	76.0	93,117.0	96,399.9	-3.4	4.3	12.4
511.9	734.7	85.4	70.6	4,259.8	4,619.3	-7.8	24.9	35.8
695.8	745.9	90.3	89.4	4,770.5	4,718.9	1.1	20.5	21.6
-337.0	1,015.9	NM	NM	3,283.0	2,701.4	21.5	-10.4	26.5
-811.3	103.6	NM	NM	1,461.0	1,644.0	-11.1	-31.7	5.5
655.2	633.8	88.3	90.2	5,254.8	5,288.0	-0.6	18.3	18.5
437.3	609.4	87.9	85.3	2,893.0	2,814.3	2.8	18.9	27.7
351.7	438.2	83.9	82.4	3,248.7	3,108.0	4.5	17.2	20.6
-60.5	-31.8	NM	NM	737.9	789.9	-6.6	-3.6	-6.5

GLOBAL REINSURERS BY COUNTRY

Rating as of July 21, 2015	Company	Footnotes	Net reinsurance premiums written (Mil. $)		
			2014	2013	Change (%)
A+	Partner Reinsurance Co. of U.S.		1,203.9	1,139.4	5.7
AA	General Re Corp.		1,111.7	1,013.2	9.7
AA+	General Re Life Corp.		1,029.1	1,027.1	0.2
A+	SCOR Reinsurance Co.		798.2	755.6	5.6
A+	Axis Reinsurance Company		754.4	756.3	-0.3
A+	XL Reinsurance America Inc.		394.2	481.3	-18.1
A+	Toa Reinsurance Co. of America (The)		351.5	403.1	-12.8
AA-	Hannover Life Reassurance Co. of America		287.6	412.4	-30.3
A+	Arch Reinsurance Co.		245.5	204.0	20.3
A	Navigators Insurance Company		195.0	174.9	11.5
A+	SCOR Global Life USA Reinsurance Company		184.3	908.2	-79.7
A+	QBE Reinsurance Corp.		168.3	179.1	-6.0
A+	SCOR Global Life Americas		110.0	98.1	12.1
A+	SCOR GLOBAL LIFE Reinsurance Company of Delaware		51.3	37.9	35.4
	Total:		**53,143.5**	**33,664.6**	**57.9**
U.A.E.					
NR	Emirates Retakaful Ltd		76.3	NA	NA
BBB	Takaful Re		20.4	17.5	16.6
	Total:		**96.7**	**17.5**	**452.7**
VIETNAM					
NR	PVI Reinsurance Company		20.4	11.7	75.4
	Total:		**20.4**	**11.7**	**75.4**
	GRAND TOTAL:		**191,467.9**	**183,192.7**	**4.7**

NA = Not Available
NM = Not Meaningful

1. 2013 Adjusted Shareholders' Funds differ from GRH 2014 due to company's revision of its methodology for measuring fast close claims provisions on life reinsurance business and recognition of an error that had led to understatement of these claims in prior reporting periods.

2. 2013 Net Reinsurance Premiums Written and Return on Revenue differ from GRH 2014 due to the alignment to final 2013 financial statements. Last year's submission was based on draft financial statements.

3. Figures represent non-consolidated position. 2013 Return on Revenue is restated in line with S&P's definitions for GRH publication.

4. 2013 numbers differ from GRH 2014 due to a segment reclassification in 2014. During the 2014 first quarter, Arch formed a mortgage segment, consisting of mortgage insurance and reinsurance business. Prior to the formation of the mortgage segment, such amounts were reflected in the reinsurance segment.

5. Combined Ratio for 2013 differs from GRH 2014 due to the restatement of net technical expenses.

6. 2013 figures differ from GRH 2014. Hannover Re Bermuda Ltd changed its reporting currency to US Dollar.

7. Adjusted shareholders' funds represent the group as a whole, including both its primary and reinsurance operations.

8. 2013 numbers differ from GRH 2014, figures now reflect IGI Company whereas previous years reflected IGI Holdings

9. Net Reinsurance Premium Written and Combined Ratio relate to reinsurance business only; all other items include primary and reinsurance business.

10. Pretax Operating Income and Return on Revenue are slightly differ from GRH 2014 due to correction of a typo. Figures include intra-group reinsurance business.

11. Figures represent Allianz SE standalone, not consolidated with other Allianz Group entities. Adjusted shareholders' funds represent the company as a whole, including both its primary and reinsurance operations.

12. Combined Ratio and Total Adjusted Shareholders' Funds differ from GRH 2014 due to correction of a formula regarding life/non-life business split.

Pretax operating income (Mil. $)		Combined ratio (%)		Total adjusted shareholders' funds (Mil. $)			Return on revenue (%)	
2014	2013	2014	2013	2014	2013	Change (%)	2014	2013
184.9	131.1	91.8	96.7	1,420.0	1,332.0	6.6	14.3	10.8
711.4	981.6	93.9	74.4	11,706.6	11,561.7	1.3	41.3	55.4
177.5	182.3	NM	NM	702.5	667.2	5.3	15.2	15.1
70.0	66.2	93.9	95.1	704.3	676.4	4.1	9.0	8.3
NA	NA	95.6	81.8	864.9	822.7	5.1	NA	NA
NA	NA	88.2	84.8	NA	NA	NA	NA	NA
70.6	76.3	89.8	90.6	716.3	693.4	3.3	17.6	17.4
32.5	21.7	NM	NM	212.1	196.9	7.7	13.2	6.2
46.6	50.4	79.1	79.1	1,365.1	1,247.5	9.4	18.6	25.5
21.1	0.2	89.0	99.9	1,027.2	902.2	13.9	8.4	0.1
27.7	54.4	NM	NM	377.6	422.6	-10.6	13.6	5.8
4.5	-6.2	101.0	107.3	826.8	814.7	1.5	2.3	-3.0
14.3	-43.5	NM	NM	151.7	151.8	-0.1	10.5	-35.1
-5.5	-5.5	NM	NM	46.5	51.3	-9.4	-9.4	-12.6
4,137.6	**7,094.3**	**88.8**	**83.4**	**139,147.3**	**141,624.2**	**-1.7**	**7.0**	**18.8**
2.2	NA	98.7	NA	122.2	NA	NA	2.8	NA
-8.3	-5.2	122.8	134.0	82.3	91.5	-10.1	-36.2	-18.8
-6.1	**-5.2**	**103.9**	**134.0**	**204.5**	**91.5**	**123.5**	**-6.1**	**-18.8**
1.6	0.8	90.4	92.7	34.6	33.4	3.7	7.7	5.9
1.6	**0.8**	**90.4**	**92.7**	**34.6**	**33.4**	**3.7**	**7.7**	**5.9**
25,135.6	**33,476.5**	**90.0**	**89.7**	**408,298.7**	**398,444.9**	**2.5**	**12.7**	**17.6**

13. 2013 Adjusted Shareholders' Funds differ from GRH 2014 due to an incorrect value which had been entered last year.

14. 2013 Pretax Operating Income and Return on Revenue differ from GRH 2014 due to the alignment to final 2013 financial statements. Last year's submission was based on draft financial statements.

15. 2013 Return on Revenue slightly differs from GRH 2014 due to the prior year expense reclassification.

16. Sompo Japan and Nipponkoa merged on Sept.1, 2014, hence 2014 figures are not comparable with 2013 figures.

17. 2013 Net Reinsurance Premium Written, Combined Ratio and Return on Revenue differ from GRH 2014 due to the alignment to final 2013 financial statements. Last year's submission was based on draft financial statements.

18. All figures include intragroup business except Net Reinsurance Premium Written.

19. 2013 Pretax Operating Income, Combined Ratio and Return on Revenue differ from GRH 2014 due to company's exclusion of intra-group reinsurance business in this year's submission.

20. 2013 Total Adjusted Shareholders' Funds differ from GRH 2014 due to the alignment to final 2013 financial statements. Last year's submission was based on draft financial statements.

21. 2013 Net Reinsurance Premiums differ from GRH 2014 due to the alignment to final 2013 financial statements. Last year's submission was based on draft financial statements.

22. Net Premium Written, Pretax Operating Income and Combined Ratio relate to reinsurance business only; all other items include direct business. The data presented is based on the published pro forma accounts for the Market, which represents an aggregation of all syndicates participating at Lloyd's. As such, some premium included for Lloyd's may also be included by other groups that consolidate their Lloyd's operations.

23. Operating figures are adjusted to remove assumptions from an affiliate, a large reinsurer, General Reinsurance Corporation. 2014 numbers include assumptions from affiliate, GEICO Corporation, contracts effective 1/1/2014.

24. 2013 Net Reinsurance Premiums and Return on Revenue differ from GRH 2014. Company corrected the figures for 2013 in its submission for GRH 2015.

Insurer Financial Strength Ratings

A Standard & Poor's Insurer Financial Strength Rating is a current opinion of the financial security characteristics of an insurance organization with respect to its ability to pay under its insurance policies and contracts in accordance with their terms. Insurer Financial Strength Ratings are also assigned to Health Maintenance Organizations (HMOs) and and similar health plans with respect to their ability to pay under their policies and contracts in accordance with their terms.

This opinion is not specific to any particular policy or contract, nor does it address the suitability of a particular policy or contract for a specific purpose or purchaser. Furthermore, the opinion does not take into account deductibles, surrender or cancellation penalties, timeliness of payment, nor the likelihood of the use of a defense such as fraud to deny claims. For organizations with cross-border or multinational operations, including those conducted by subsidiaries or branch offices, the ratings do not take into account potential that may exist for foreign exchange restrictions to prevent financial obligations from being met.

Insurer Financial Strength Ratings are based on information furnished by rated organizations or obtained by Standard & Poor's from other sources it considers reliable. Standard & Poor's does not perform an audit in connection with any rating and may on occasion rely on unaudited financial information. Ratings may be changed, suspended, or withdrawn as a result of changes in or unavailability of such information, or based on other circumstances.

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'pi' ratings, denoted with a 'pi' subscript, are Insurer Financial Strength Ratings based on an analysis of an insurer's published financial information and additional information in the public domain. They do not reflect in-depth meetings with an insurer's management and are therefore based on less comprehensive information than ratings without a 'pi' subscript. 'pi' ratings are reviewed annually based on a new year's financial statements, but may be reviewed on an interim basis if a major event that may affect the insurer's financial security occurs. Ratings with a 'pi' subscript are not subject to potential CreditWatch listings.

Ratings with a 'pi' subscript generally are not modified with '+' or '-' designations. However, such designations may be assigned when the insurer's financial strength rating is constrained by sovereign risk or the credit quality of a parent company or affiliated group.

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A Standard & Poor's Insurer Financial Enhancement Rating is a current opinion of the creditworthiness of an insurer with respect to insurance policies or other financial obligations that are predominantly used as credit enhancement and/or financial guaranties in Standard & Poor's rated transactions. When assigning an Insurer Financial Enhancement Rating, Standard & Poor's analysis focuses on capital, liquidity and company commitment necessary to support a credit enhancement or financial guaranty business. The Insurer Financial Enhancement Rating is not a recommendation to purchase, sell, or hold a financial obligation, inasmuch as it does not comment as to market price or suitability for a particular investor.

Insurer Financial Enhancement Ratings are based on information furnished by the insurers or obtained by Standard & Poor's from other sources it considers reliable. Standard & Poor's does not perform an audit in connection with any credit rating and may, on occasion, rely on unaudited financial information. Insurer Financial Enhancement Ratings may be changed, suspended, or withdrawn as a result of changes in, or unavailability of, such information or based on other circumstances. Insurer Financial Enhancement Ratings are based, in varying degrees, on all of the following considerations:

- Likelihood of payment capacity and willingness of the insurer to meet its financial commitment on an obligation in accordance with the terms of the obligation;
- Nature of and provisions of the obligations; and
- Protection afforded by, and relative position of, the obligation in the event of bankruptcy, reorganization, or other arrangement under the laws of bankruptcy and other laws affecting creditors' rights.

Insurer Financial Strength Ratings

An insurer rated 'BBB' or higher is regarded as having financial security characteristics that outweigh any vulnerabilities, and is highly likely to have the ability to meet financial commitments.

AAA

An insurer rated 'AAA' has EXTREMELY STRONG financial security characteristics. 'AAA' is the highest Insurer Financial Strength Rating assigned by Standard & Poor's.

AA

An insurer rated 'AA' has VERY STRONG financial security characteristics, differing only slightly from those rated higher.

A

An insurer rated 'A' has STRONG financial security characteristics, but is somewhat more likely to be affected by adverse business conditions than are insurers with higher ratings.

BBB

An insurer rated 'BBB' has GOOD financial security characteristics, but is more likely to be affected by adverse business conditions than are higher rated insurers.

An insurer rated 'BB' or lower is regarded as having vulnerable characteristics that may outweigh its strengths. 'BB' indicates the least degree of vulnerability within the range; 'CC' the highest.

BB

An insurer rated 'BB' has MARGINAL financial security characteristics. Positive attributes exist, but adverse business conditions could lead to insufficient ability to meet financial commitments.

B

An insurer rated 'B' has WEAK financial security characteristics. Adverse business conditions will likely impair its ability to meet financial commitments.

CCC

An insurer rated 'CCC' has VERY WEAK financial security characteristics, and is dependent on favorable business conditions to meet financial commitments.

CC

An insurer rated 'CC' has EXTREMELY WEAK financial security characteristics and is likely not to meet some of its financial commitments.

R

An insurer rated 'R' is under regulatory supervision owing to its financial condition. During the pendency of the regulatory supervision, the regulators may have the power to favor one class of obligations over others or pay some obligations and not others. The rating does not apply to insurers subject only to nonfinancial actions such as market conduct violations.

NR

An insurer designated 'NR' is NOT RATED, which implies no opinion about the insurer's financial security.

Plus (+) or minus (-)

Ratings from 'AA' to 'CCC' may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.

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