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Retakaful and Retrocession

A Property Market Perspective

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The International Takaful Summit 2012

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Agenda

- Setting the Scene
- External Influences
- Where are we in the Market Cycle?
- Retakaful and Retrocession Market Catastrophe Losses Update and effect on Reinsurance and Retakaful Market Capitalisation
- Lessons Learned
- The Modern market and Peak Exposure Solutions

Setting the Scene

- **Retrocession** - the provision of Retakaful to professional Retakaful providers

- Retakaful market is expanding, over **15 International Retakaful operators or 'windows'** throughout Asia, the Middle East and North Africa. **13 of these are A rated by the global Rating Agencies.** No increase in Number during past 12 months.

- Who provides the **retrocession cover** – Retakaful operators can cover each other or utilse conventional capacity? Darura must apply while sector continues to develop.

- **Potential spiral effect** of a small number of Retakaful Operators offering each other cover if the market insists on Retakaful Operators offering retrocession?

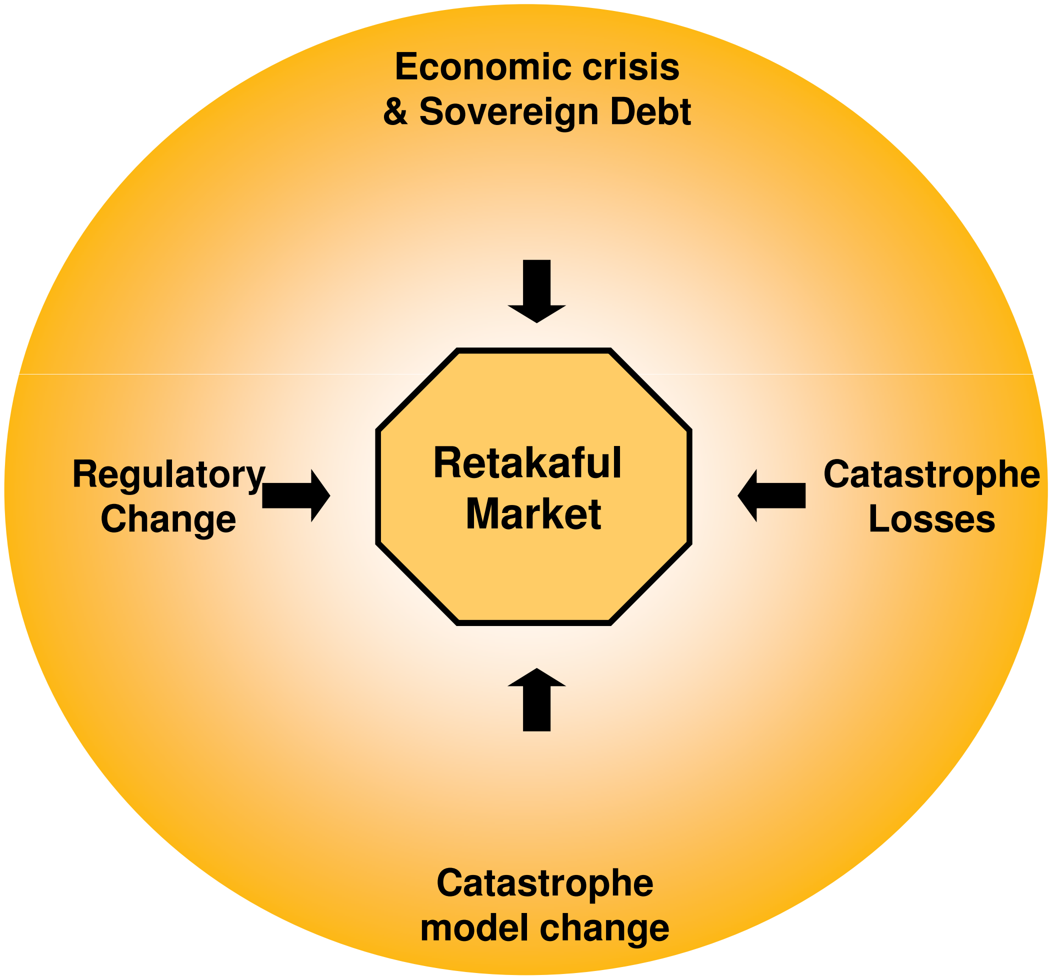
- Long-term aim; an **integrated Takaful chain** participant to Takaful operator to Retakaful operator to Retakaful retrocessionaire but capital required.

- **All of required standard line Treaty capacity** can be provided by the Retakaful market. The Retakaful Operator must rely on the conventional retrocession market as a matter of necessity

- **Retakaful and Reinsurance are International businesses** – subject to both Internal and External pressures

External Influences and the effect on the Market Cycle

External factors



Economic Crisis & Sovereign Debt

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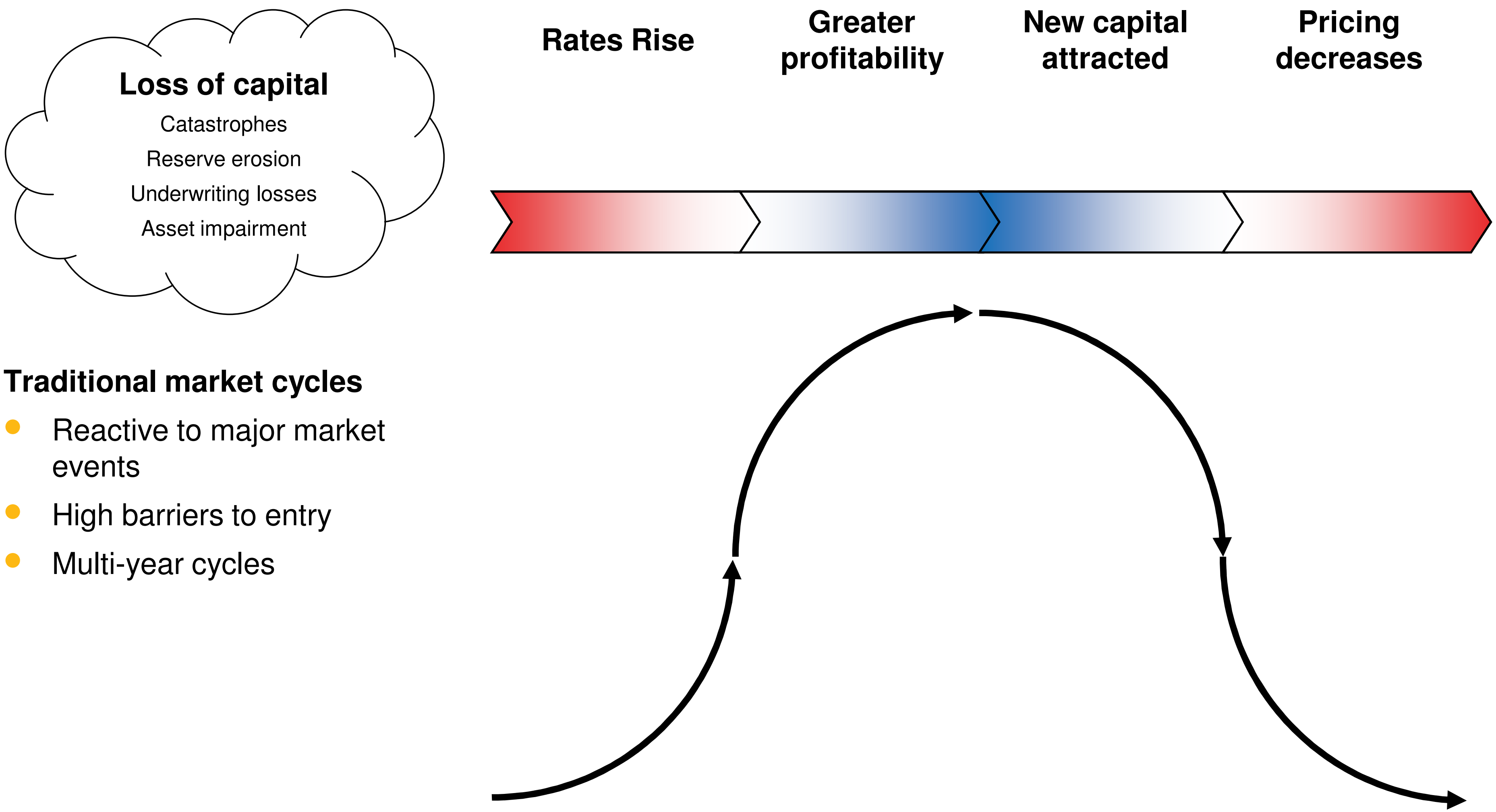
- **Economic Crisis**
  - Asset impairment
  - Investment difficulties
  - … but no evidence that traditional re/insurance holds systemic risks

- **Impact of the Eurozone Debt Crisis on Insurer / Reinsurer / Retakaful Operator Solvency?**
  - Implicit and explicit threats to insurer / takaful /retakaful security
  - Issues if one or more sovereigns exiting the Euro or suffering further downgrade
  - But … the sector has proven itself resilient

- **Insurers / takaful operators are different from Banks**
  - Insurers are significant investors in Eurozone sovereign / financial sector debt;
  - However, exposure differs from banks in many key respects

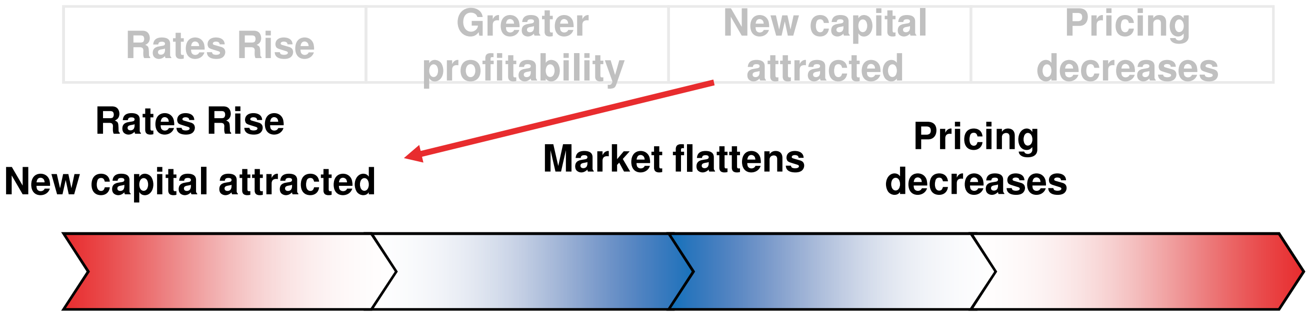
Retakaful market cycles



Traditional market cycles

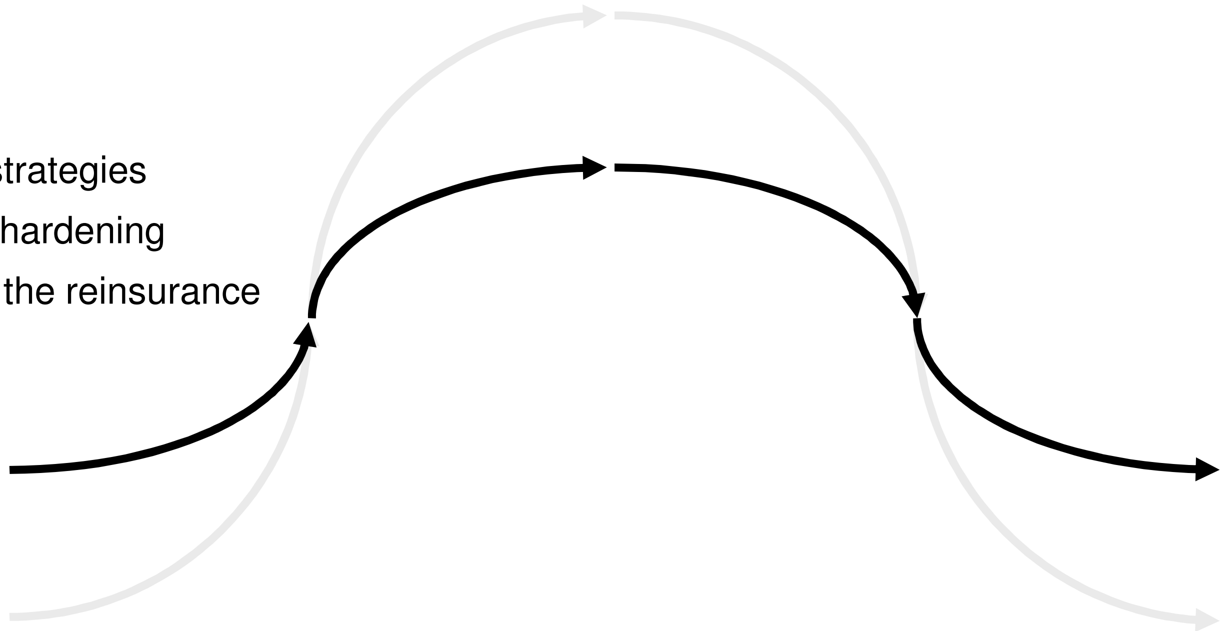
- Reactive to major market events
- High barriers to entry
- Multi-year cycles

Retakaful market cycles



Is there still a macro cycle?

- Reduced barriers to entry
- New products and investment strategies
- New capital anticipates market hardening
- Continued over-capitalisation if the reinsurance market is considered



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International Market Update

- Events of 2011
- Global Distribution
- Effect on reinsurers
  and retakaful operators
- What have we learned?

International Market Update
- Overview

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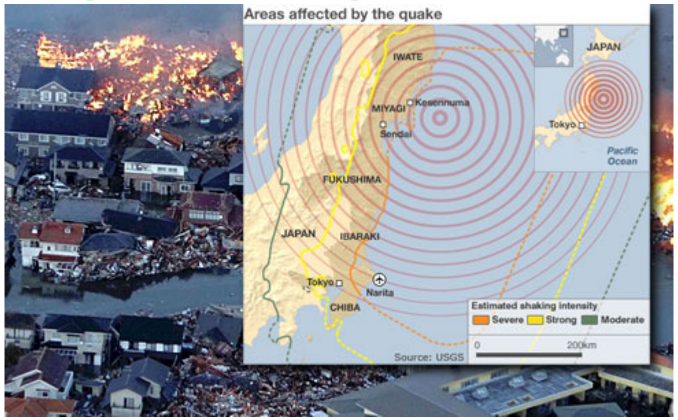
New Zealand Earthquake

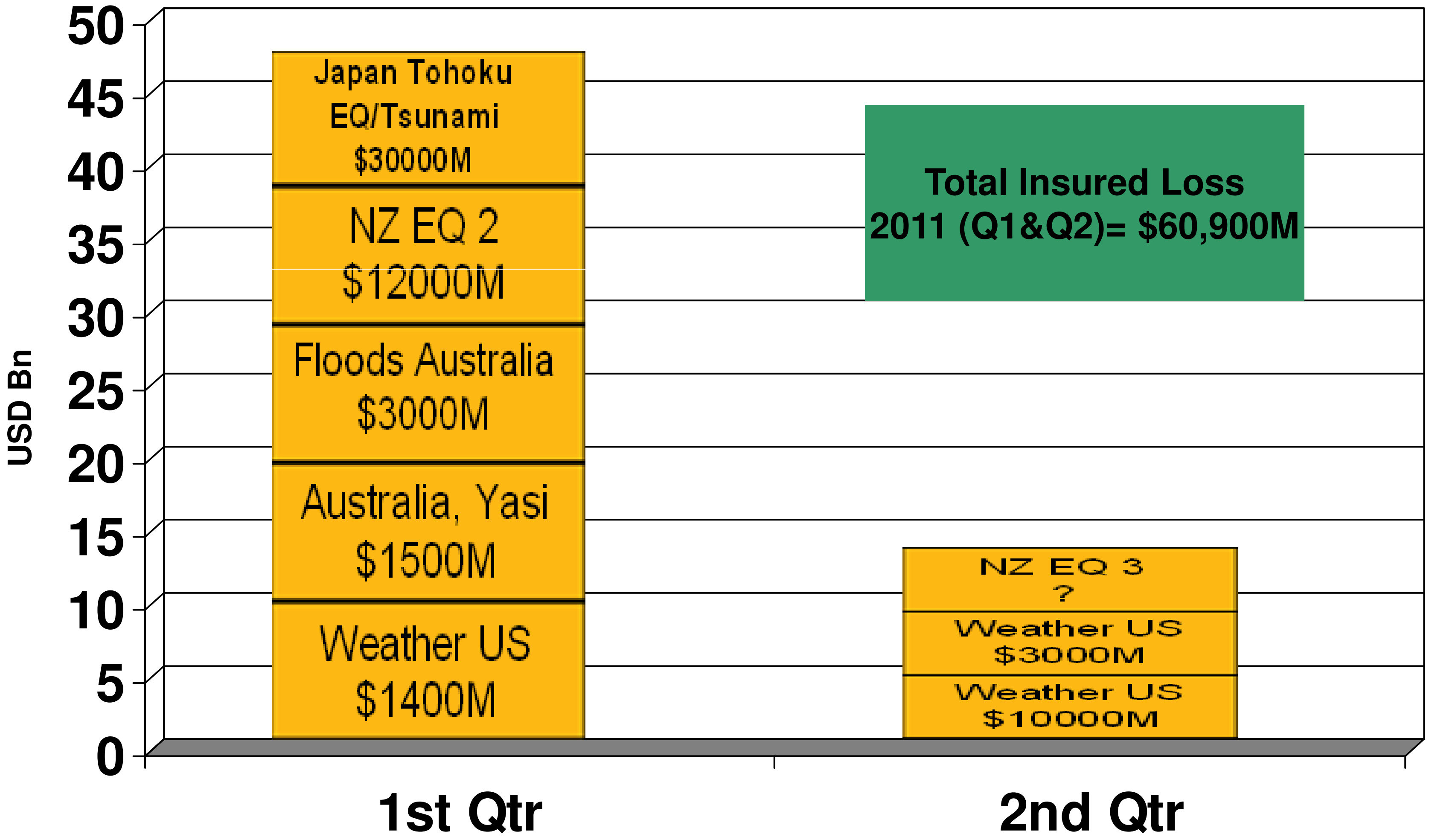
Australian Flood

Japan Earthquake



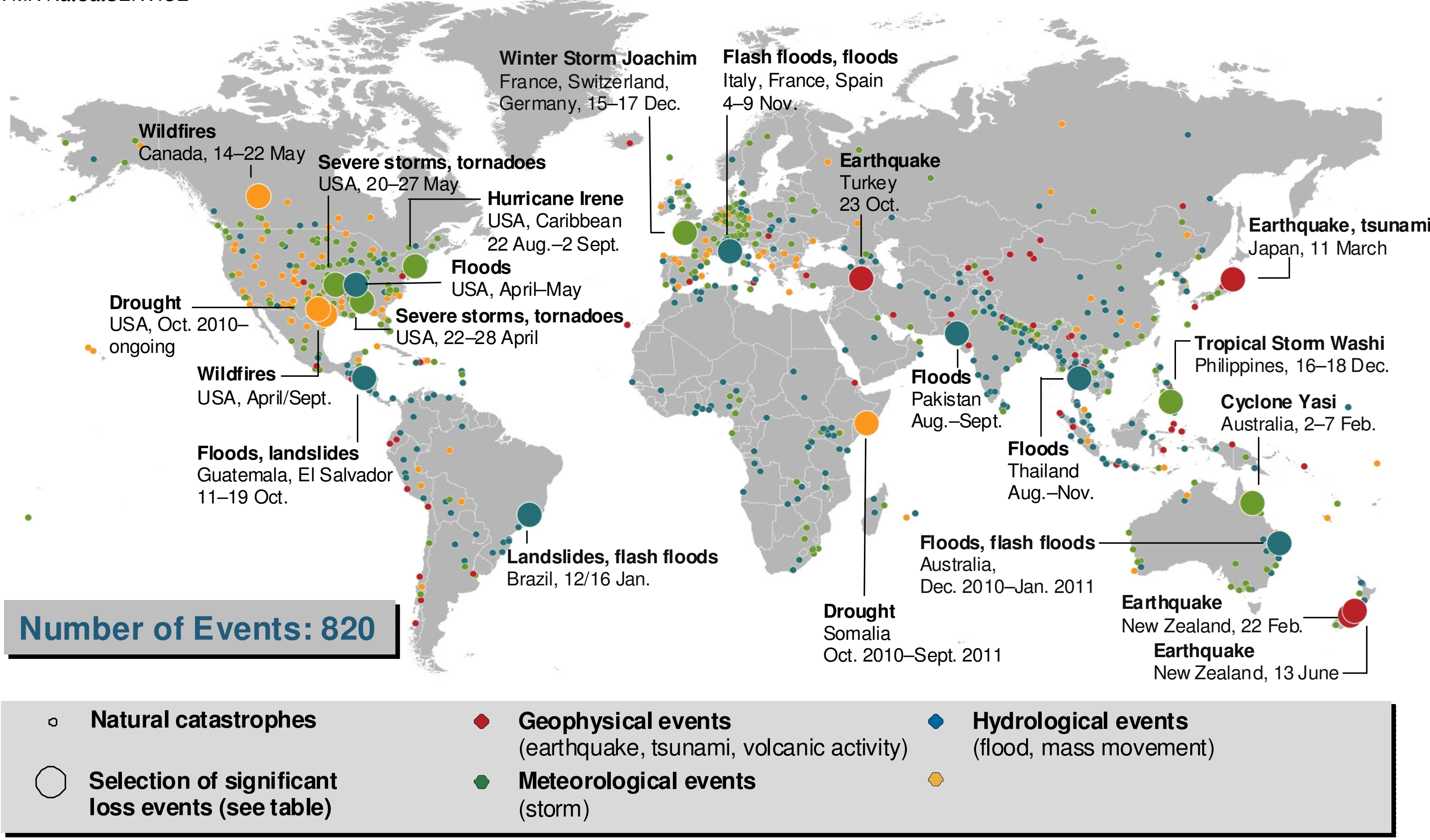
Thailand Flood

2011 position 12 months ago



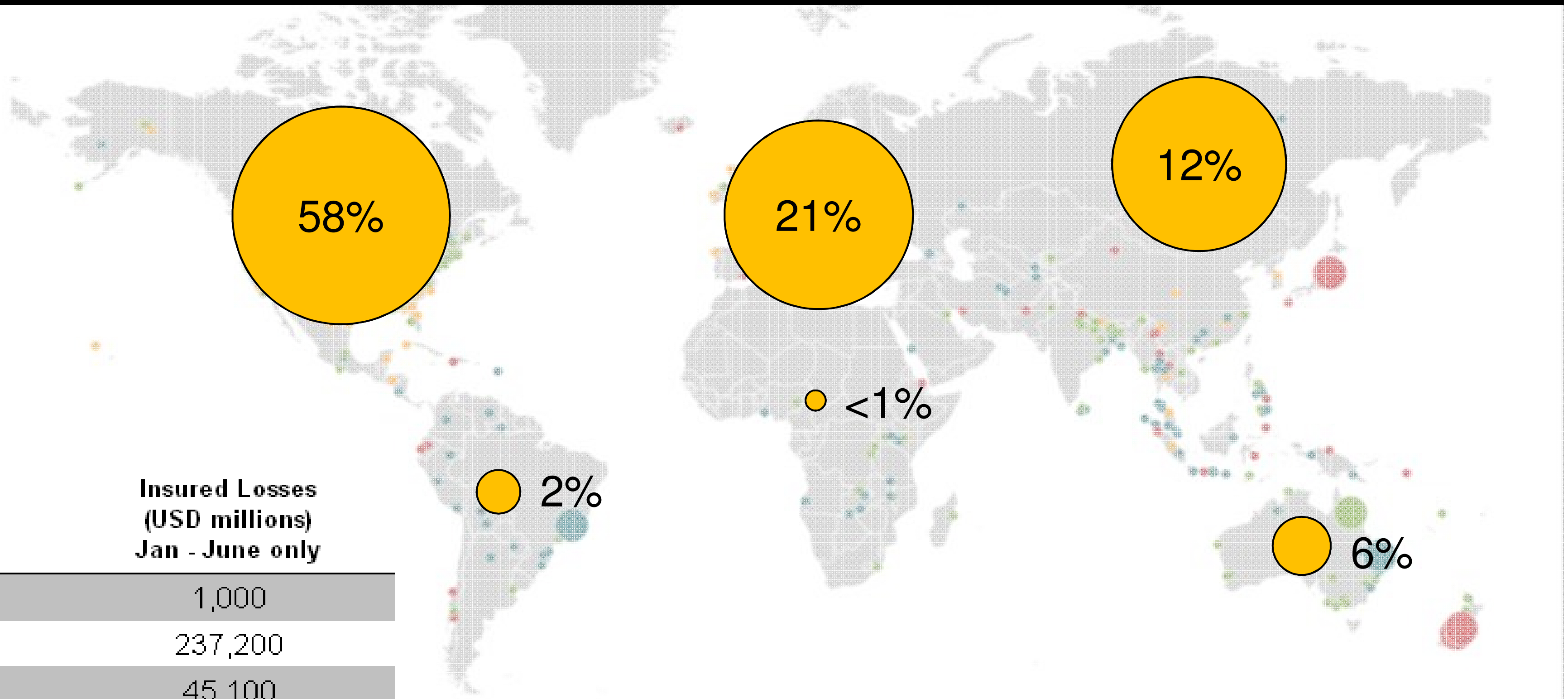
Catastrophic losses
- Events of 2011

Source: MR NatCat*SERVICE*



Global Natural Disasters: 1980 – 2011

Insured losses 1980 - 2011 (January – June only): US 389 bn
% Distribution of Insured Losses Per Continent excluding 2 H/Y Thai Floods



Continent	Insured Losses (USD millions) Jan - June only
Africa	1,000
America	237,200
Asia	45,100
Australasia	25,100
Europe	80,900

Source: MR NatCat*SERVICE*

Global Natural Disasters: 2011

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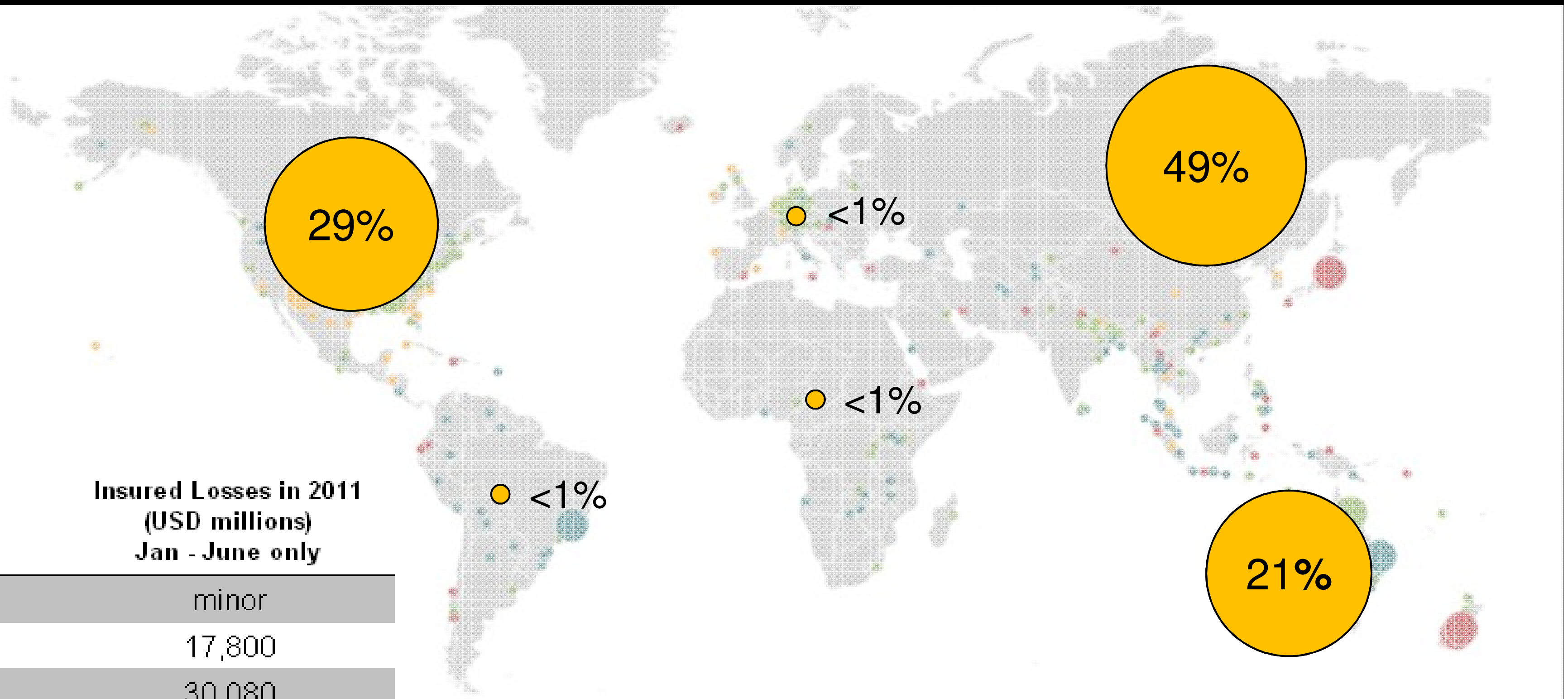
Insured losses 2011 (January – June only): US$ 60 bn

% Distribution of Insured Losses Per Continent excluding 2 H/Y Thai Floods



Continent	Insured Losses in 2011 (USD millions) Jan - June only
Africa	minor
America	17,800
Asia	30,080
Australasia	12,900
Europe	100

Source: MR NatCat*SERVICE*

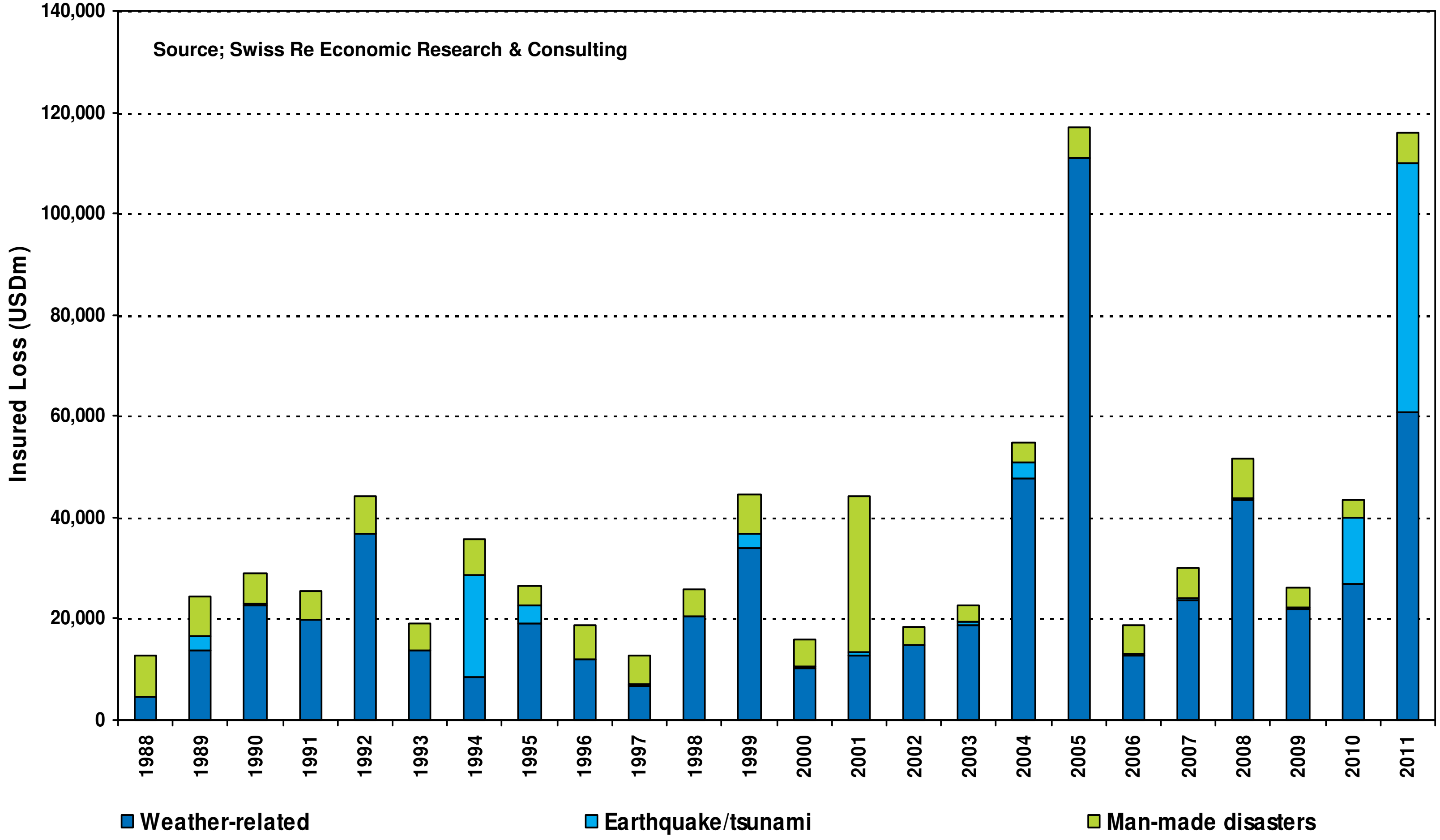
Loss Activity

Significant loss activity over 21 months (estimated market losses):

	Date	Event	USD
–	Feb 2010:	Chile EQ	8.0bn
–	Mar 2010:	Melb Hail	1.0bn
–	Mar 2010:	Perth Hail	1.1bn
–	**Sep 2010:**	**NZ EQ**	**5.0bn +**
–	Jan 2011:	Qld Floods	2.3bn +
–	Jan 2011:	Qld Cyclone	1.2bn +
–	**Feb 2011:**	**NZ EQ**	**10.0bn +**
–	Mar 2011:	Japan EQ	30.0bn
–	Apr 2011:	US Tornadoes	14.0bn
–	Oct 2011:	Thailand	17.5bn+

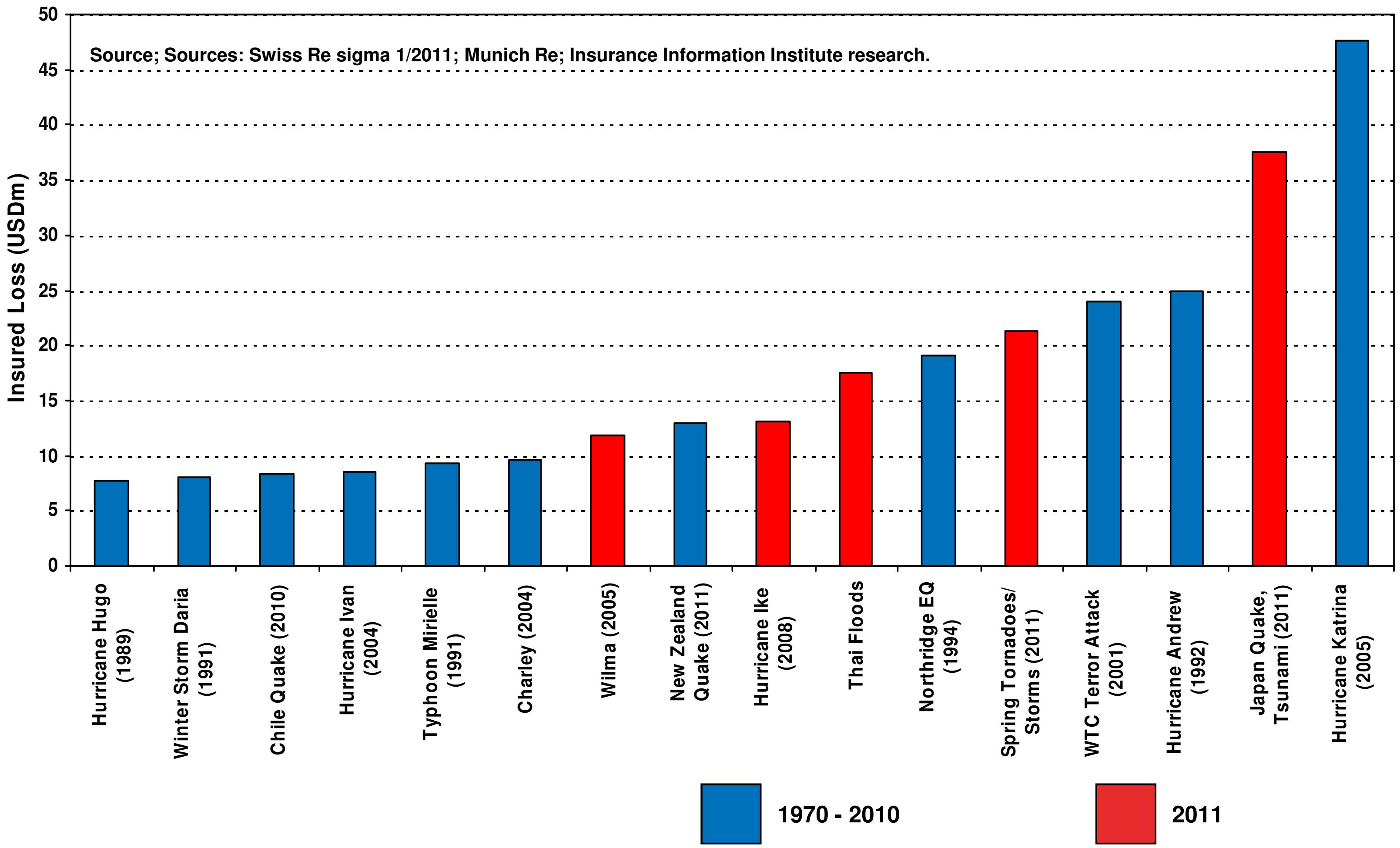
Total of above USD 90.1bn to Reinsurance market, USD 75bn in 2011 alone

Catastrophic losses
- 1988 to 2011

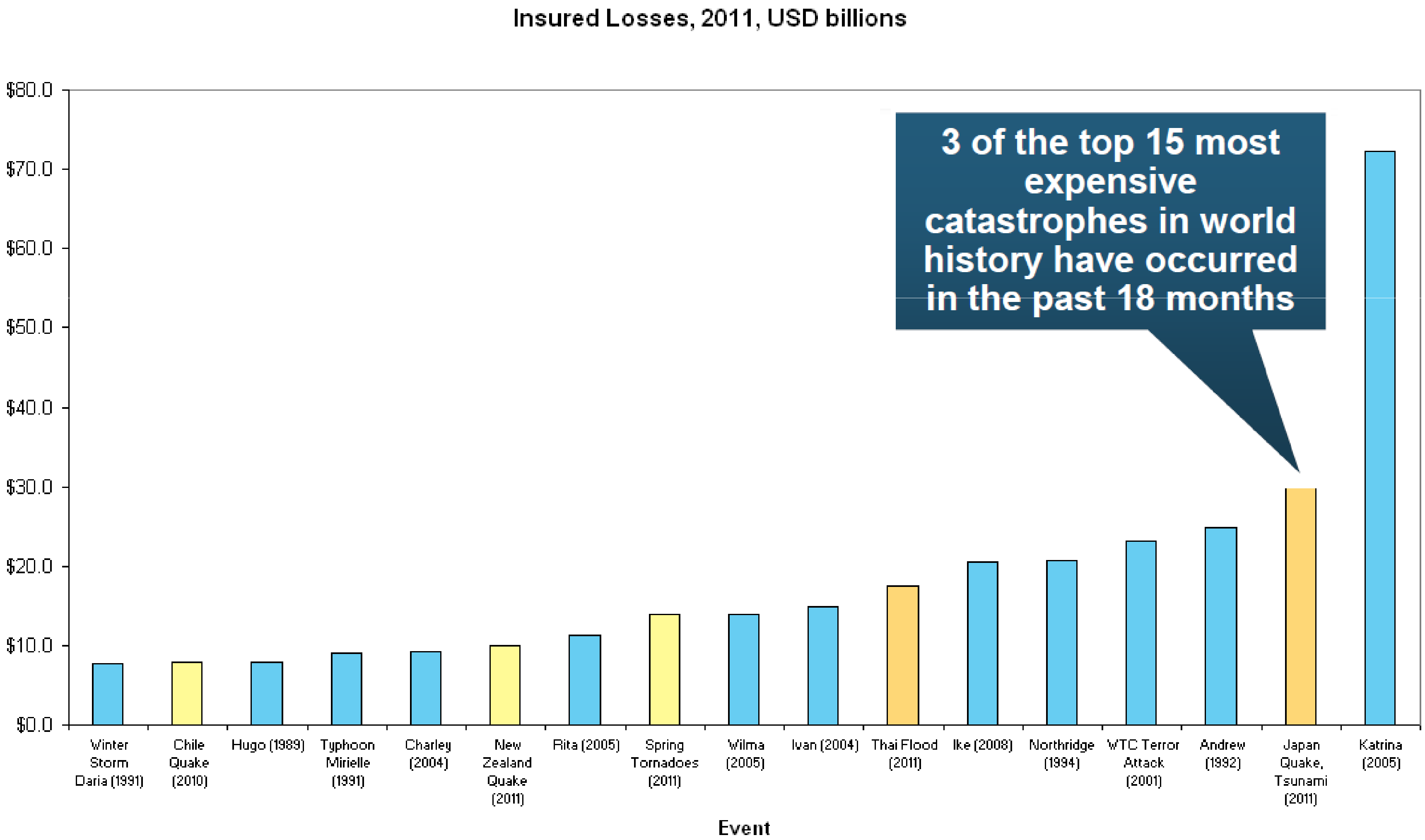


Catastrophic losses

- Most Costly World Insurance Losses, 1970-2011



Top 17 Insurance Losses: 1970 – 2011



Catastrophic losses

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Event	Loss (USD)	Issue
Australia Floods	3 bn	Little modelling or exposure monitoring
Japan EQ & Tsunami	35 bn	Only partially modelled
US Tornadoes	19 bn	Extreme frequency
New Zealand EQ	20 bn	Significant modelling issues
Hurricane Irene	4 bn	Extreme flooding
Thailand	17.5 bn	Little modelling or exposure monitoring

- **2011; the highest loss year on record for economic losses**
  - USD 380bn in economic losses globally
  - USD 270bn in 2005 previous highest
- **USD 105 bn in insured losses globally**
  - 2nd only to 2005 (inflation adjusted)
  - > 5x 30 year average of USD 19bn

Reinsurer's Catastrophe Losses

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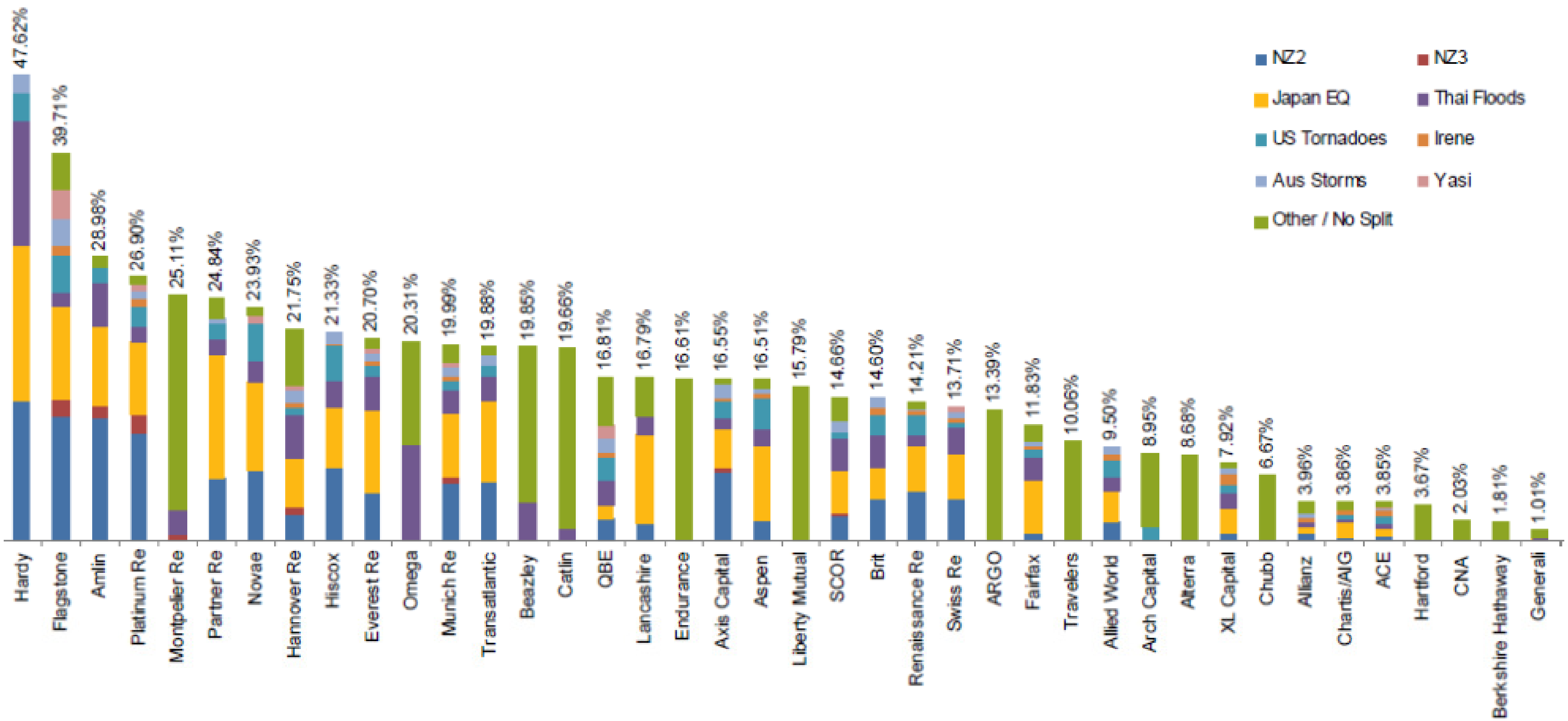
- Full Year 2011 Catastrophes as % of Opening Shareholders Funds



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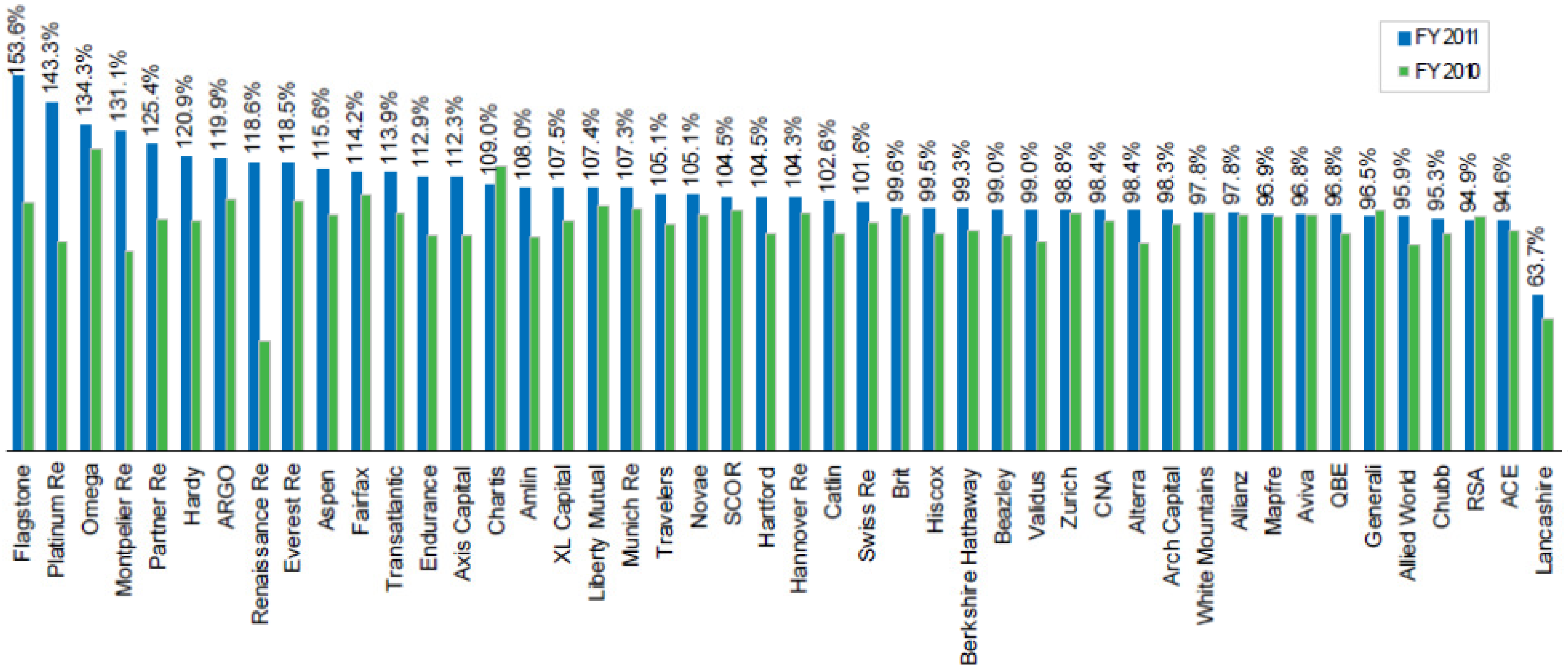
Reinsurer’s Underwriting

- Full Year 2011 vs 2010 Combined Ratio



Catastrophic losses
- What have we learned?

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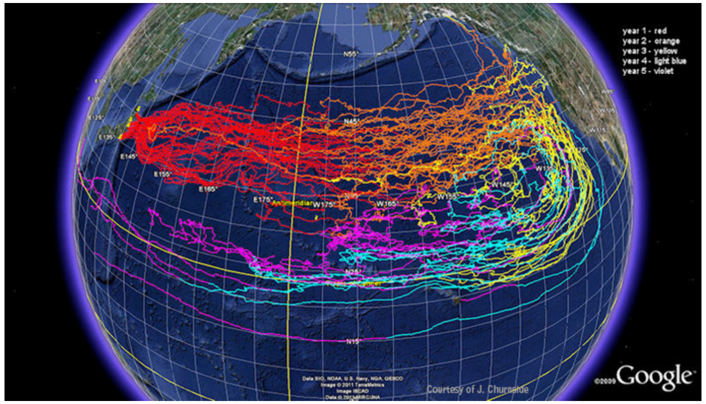
- **Insured losses still a small percentage of economic loss**
  - An long-term theme that commercial insurers struggle to address
  - Opportunity for the takaful segment
- **The "tail" is always bigger than we think**

- **Track exposure for Interests Overseas and ensure Retakaful protection is adequate**

- **It's easy to understate "time element" losses**
  - Denial of access
  - Business Interruption
  - Contingent Business Interruption
    - A global contagion?

- **Catastrophe models have under-performed**
  - Coverage
  - Secondary and contributing perils

Sendai Airport, source; National Geographic



Source; NOAA

Where are we in the global market cycle?

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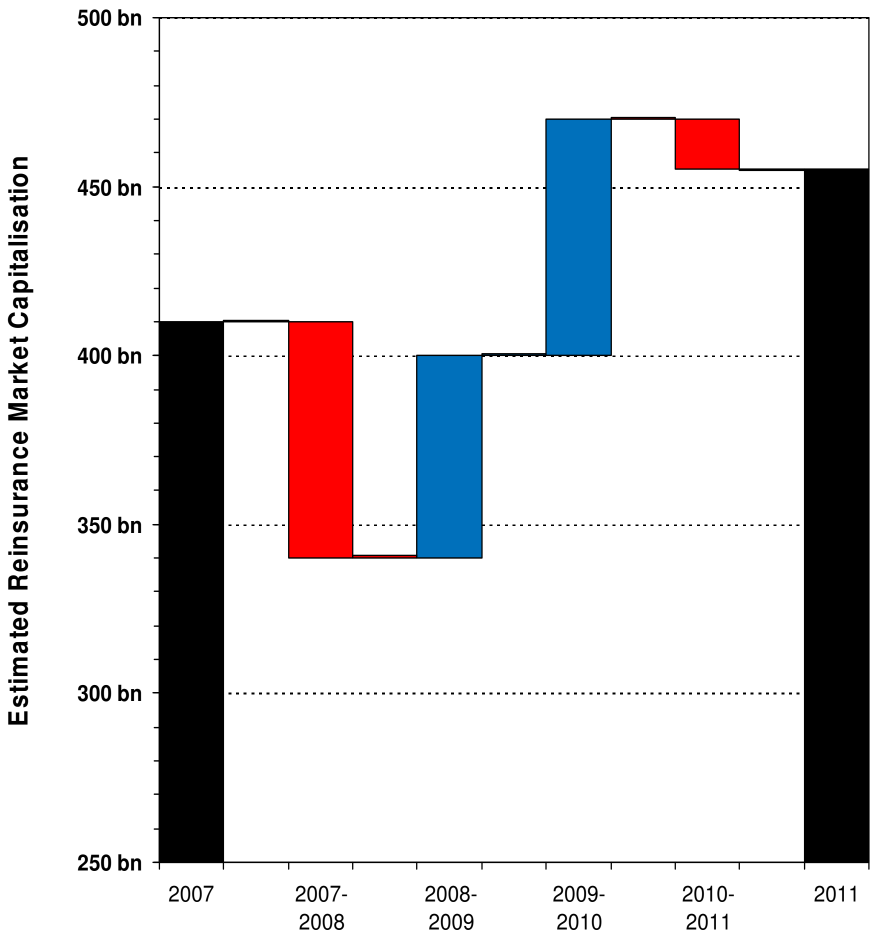
- **Where are we in the market cycle**
  - AM Best "Critically, the market seems poised for a turn" January 2012
  - Hardening in response to major losses
  - … but only spotty increases in loss free territories
- **Reinsurers under pressure**
  - Over USD 90 bn of losses to the reinsurance sector in 2 years
  - Manageable from a capital perspective
  - Market's capital remains strong for 2012
- **Not a "proper" hard market**
  - No dislocation
  - Capacity remains available
  - Little in the way of capital impairment
- **Are we entering an era of "Micro-cycles"?**
  - Dependant on line of business
  - Dependant on geography
  - Not necessarily industry-wide
- **Capital Markets playing an increased role in the major catastrophe programmes**



Where are we in the insurance / takaful market cycle?
- Selected recent renewals

Territory	Loss free excess of loss	Loss affected excess of loss	Comments
Australasia	+15 to +35%	+40% to +75%	Significant losses
Australasia (inc. NZ)	-	+80 to +150%	
China	0% to +15%	-	EQ exposure driving pricing
Europe	+1% to +4%	-	Broadly loss free, other than Nordic
France	0% to +3%	-	
Nordic	+5% to +10%	+25% to +50%	
Japan	+20% to +30%	+30% to +50%	In addition to prior year increases
Taiwan	> +30%	-	Concern over EQ and CBI
US Nationwide	+2.5% to +10%	-	Losses and model change

Property Catastrophe pricing trends – Overall Summary

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Property rates					
Territory	Pro rata commission	Risk loss free % change	Risk loss hit % change	Catastrophe loss free % change	Catastrophe loss hit % change
Australia	0%	0% to +10%	various	0% to +10%	+5% to +25%
Caribbean	0%	0%	various	+5% to +10%	N/A
China	N/A	0% to -5%	+10% to +25%	0% to +15%	N/A
Latin America	+1% to -5%	-5% to +5%	+5% to +25%	0% to +5%	N/A
Middle East	0%	+5% to +10%	+10% to +15%	+10%	+20% to +35%
South Africa	0%	+5%	+10%	+5%	+10%
U.S. – National	0%	0%	+2.5% to +7.5%	0% to +5%	+2.5% to +7.5%
U.S. – Regional	N/A	0%	+2.5% to +7.5%	-10% to +5%	+5%

Where are we in the retrocession market cycle?

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Middle East and Asia Pacific

- **Retrocession capacity** for the Middle East and Asia Pacific based reinsurers has shown an increase
- **Political Violence** limitations are being implemented
- Scrutiny of **Interests Abroad** coverage afforded to Takaful and Retakaful Operators within the region
- **Named territories**. Complete transparency regarding territorial breakdown required by many markets – catastrophe accumulation and International sanctions are particular issues
- **Increased retention** or deductible being imposed by leaders
- **Prices have increased but competition remains** in the market. More established leaders have sought to spread price rise across the programme whereas new entrants are happier to load price increase on the lower layers and require a smaller rise in price higher up the programme.
- **Correlation** between detailed / transparent exposure data and programme price benefit remains low
- **Capital Markets** and Collateralized Markets playing an increased role

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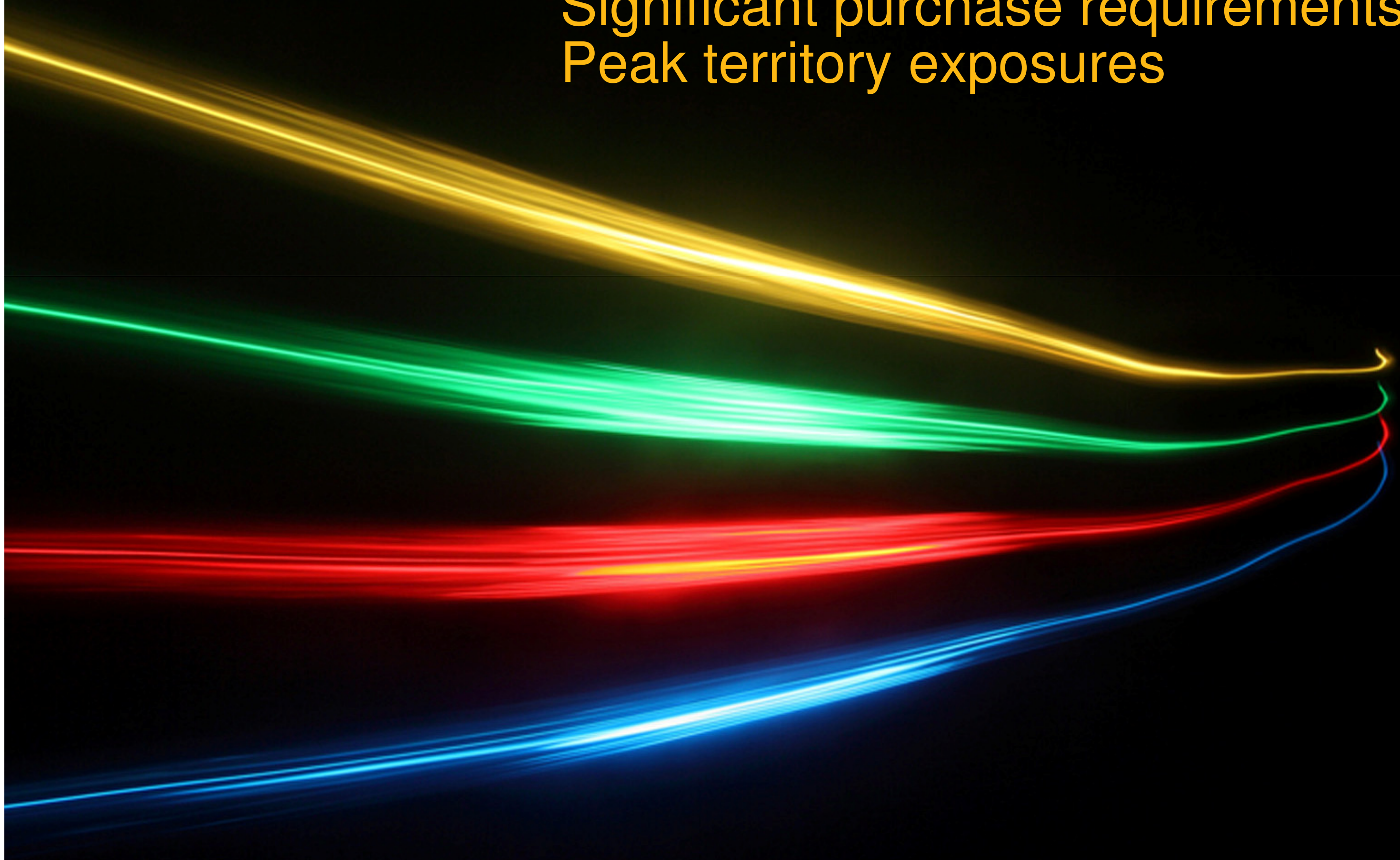
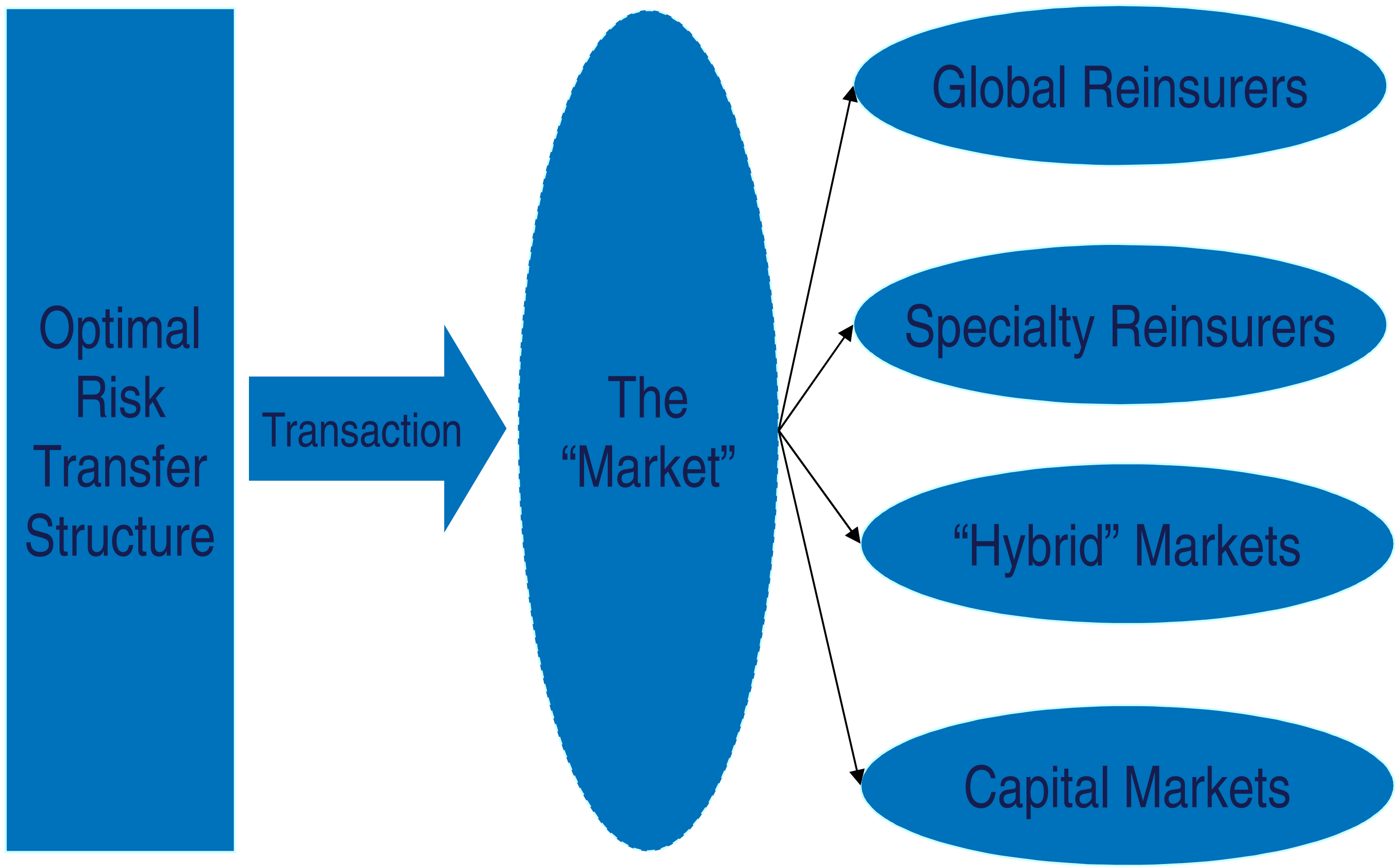
The Modern Market

Significant purchase requirements - Peak territory exposures



The Modern Market



Blended Purchase to achieve $1bn of Capacity Incorporating Peak Exposures

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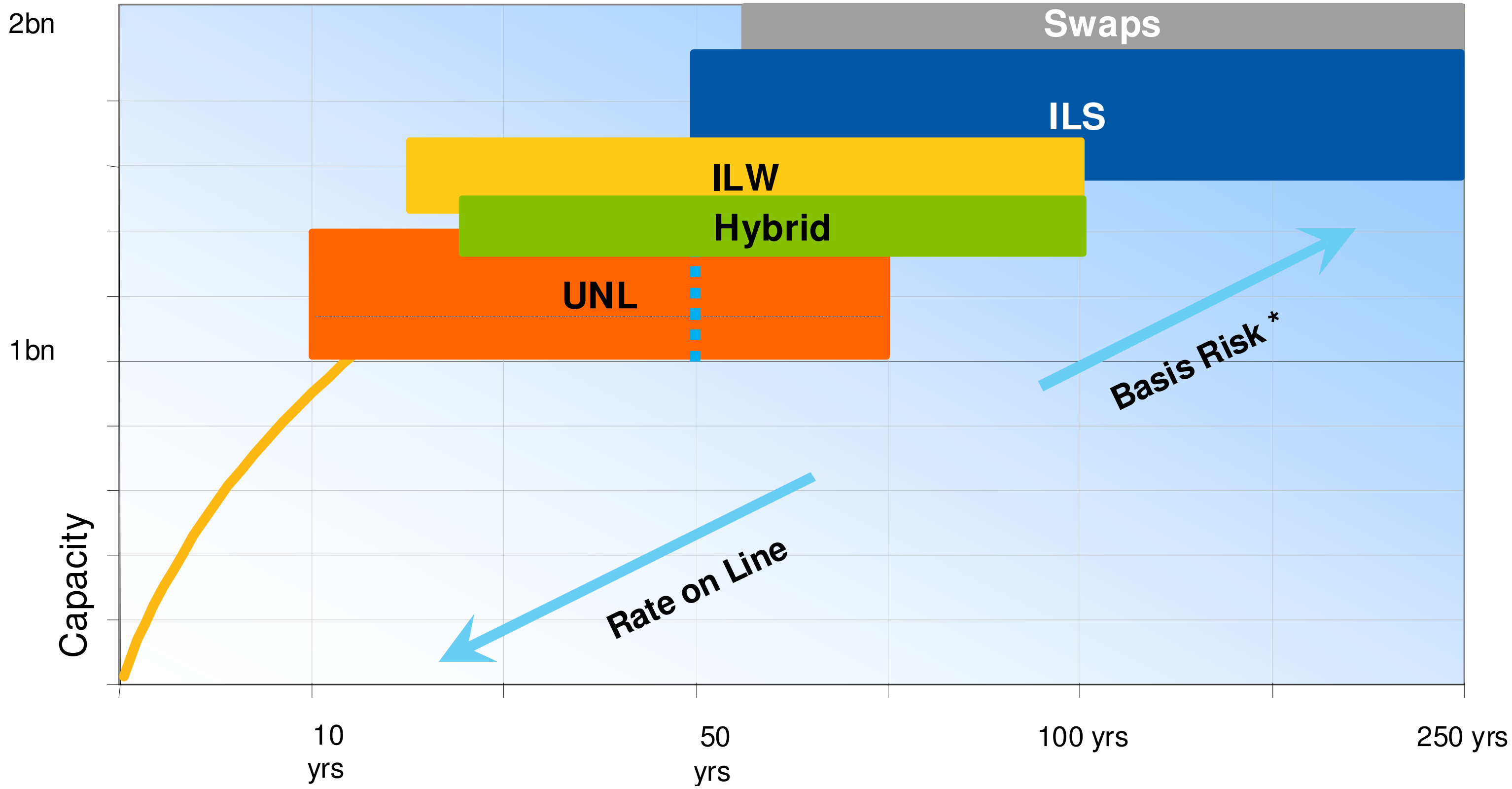
Illustrative example



*** With the exception of Swaps**

Summary of 'Takeaways'

- **Market capitalisation** has proved adequate to cope with the frequency of large claims encountered 2010 / 2011. Loss activity has been modest in 2012 to date
- **The reinsurance market** is likely to remain comparatively soft as a consequence, with rates stable but differential pricing available through a targeted approach by Reinsurers and Retakaful Operators
- **The regional retrocession market** has hardened in terms of price, but choice remains in terms of structure and conditions
- **Influx of capital** from the Capital Markets seeking an alternative home and offering new capacity where risk is not directly correlated with their main exposures. But untested potential volatility and reaction to major catastrophe events.
- **There is adequate capacity** for foreseeable requirements – UNL, Hybrid, Industry Loss Warranty, Insurance Linked Securities, Cat Bonds
- **External factors** such as the Eurozone crisis, and potential falls in bond values could present a future challenge to reinsurers / retakaful operators
- **Anticipate the unexpected!**