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Post-event Report

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INTRODUCTION

Welcome to the Artemis ILS 2018 conference report, which provides insight into some of the debates that took place on the day during Artemis’ third event in the region.

The event took place at Singapore’s Suntec Convention Centre in Suntec City, with over 170 delegates gathering to hear leading ILS and reinsurance market participants from around the world discuss ILS in Asia.

The day was a resounding success, and attendees were treated to insightful and educational debates from ILS and reinsurance market experts positioned in varied parts of the chain, including risk modellers, brokers, investors, sponsors, and other industry service providers.

Singapore continues to move forward with plans to establish itself as the first ILS hub in Asia, and speakers highlighted the potential for Singapore to offer a range of ILS and catastrophe bond options for entities seeking risk transfer.

The event provided an overview of the development of ILS across the world, before exploring the potential for the asset class to play a meaningful role in Asia, ultimately helping to narrow the region’s protection gap.

Attendees heard how ILS already has a presence in Asia, with some of the catastrophe bond market’s most prolific sponsors being domiciled in Japan. However, broader Asian expansion has been limited, and speakers were eager to discuss the need for greater education of risk transfer, as well as increased awareness of the benefits of insurance and reinsurance-linked protection.

The day also featured discussions around the different types of ILS structures and the benefits of different strategies for both investors and sponsors, while hedging for ILS was also explored.

To end, attendees heard about the future of the ILS market both globally and in Asia, as well as where the next phase of ILS growth might come from.

Artemis ILS Asia will be back in Singapore in July 2019. We hope to see you there!

Steve Evans
Founder & Editor, Artemis.bm
Jacqueline Loh, Deputy Managing Director of the Monetary Authority of Singapore, opened the conference with a talk exploring the development of the insurance-linked securities (ILS) market, which she described as a “remarkable story of innovation.”

“Twenty years later, the global ILS market continues to thrive. Emerging from the hurricane losses, earthquakes in Mexico, as well as wildfires in California, 2017 has been widely billed as the global financial crisis equivalent for the ILS market, as it registered the largest losses for more than a decade. Yet, the ILS market has remained largely resilient,” said Loh.

The permanence of ILS capital has now been realised, and as the asset class continues to expand, specialist ILS funds are eager to seek opportunities for diversification in their investment portfolios, and Loh told the audience that “Asia is poised to be the next frontier for ILS growth.”

However, the economics of ILS in Asia remains challenging, continued Loh, something that includes the dangerously low levels of insurance penetration across many Asian countries, underlining its position as an emerging, or developing marketplace.

"Yet, it is likely that ILS will achieve a breakthrough in the coming years, as the protection gap in Asia widens," added Loh.

Both the frequency and severity of natural catastrophe events have increased in Asia, which, combined with low insurance penetration levels has led to rising economic losses that ultimately fall on local and national governments.

"ILS, together with other risk management solutions, including reinsurance and government pools, has significant scope to play a larger role in reducing the financial impact of natural disasters.

"The presence of a fully-fledged ILS market and ecosystem in the region will be very important to encourage the development of risk financing instruments. However, there is currently no established market in Asia for ILS. So, as the leading financial centre in Asia, Singapore is well positioned to fill this need.

"Asia holds promise for the next phase of growth for ILS, given the region’s growing needs, and Singapore can play an important role to facilitate this growth as an ILS domicile," said Loh.

Following Loh’s opening remarks, the audience was treated to a keynote speech from Lorenzo Volpi, Partner at London-based specialist ILS asset manager, Leadenhall Capital Partners LLP.

He provided an update on the global ILS space, and explained that more broadly, Asia is already an important part the global re/insurance landscape, in terms of both life and non-life exposures.
“Life as a market is much bigger than non-life, but then when we think about Asia, Japan is actually the second biggest market for life in the world, after the U.S. Then, if you think about the non-life market, usually we have the highest penetration in the U.S., around 50%, Europe is around 35%, and Asia is about 15%,” said Volpi.

In the property catastrophe sector, explained Volpi, Asian perils account for roughly 11% of the outstanding catastrophe bond market, while roughly 12% of 2018 issuance, so far, is exposed to Asian perils, although these are all currently Japanese risks.

Asian peril catastrophe bonds play a vital role in the ILS landscape, providing investors and investment managers with diversification within their portfolios. But while investors from all corners of the world desire diversification, when considering the response of the investor base to 2017 catastrophe events, Volpi explained that Asian market participants were more conscious than their U.S. and European counterparts.

“It was quite interesting to see that in Asia, institutional investors, more than optimistic types of players, were actually very conscious. When you look at Japan and Korea for example, investors wanted to almost start their due diligence from scratch again, after such a bad year.

“So, rather than adding money immediately to take advantage of the opportunity, which is what occurred in Europe and the U.S., in Asia, for different reasons, including the nature of the region, and that people want to understand every detail of what occurred and what they’ve done, they wanted to remind themselves why they actually invested in ILS,” said Volpi.

When discussing ILS, and also the broader insurance and reinsurance sectors’ development and expansion, it’s evident that catastrophe risk models play an important role in the understanding of different perils and regions, ultimately supporting the development of markets by providing a view of potential losses and enabling risks to be priced.

The day’s second keynote speech, delivered by Jinal Shah, Managing Director, Capital Markets Solutions at global catastrophe risk modelling specialist, RMS, underlined just this, with a particular focus on how models help ILS investors and portfolio managers respond to major loss events.

Shah underlined the importance of keeping models up-to-date, alongside model consistency and the confidence this can give to industry players, using the events of 2017 as an example.

“Maria certainly taught the cat modelling industry to constantly keep models updated and to maintain robust processes during real-time events, for the generation of wind fields and losses,” said Shah.

“It’s a simple fact that models for peak regions, like Florida, are more consistent and constrained, while for other regions we expect to see more divergent view of risk,” he added.
The necessity of risk models in assisting the development of an ILS market in Asia is clear, and Shah underlined how ongoing, frequent updates and continued development of the models can support continued ILS market growth.

As noted earlier in the day, the protection gap (disparity between economic and insured losses post-event) in Asia is widening, and while the development of models for more Asian territories and perils would certainly help to narrow this gap, more challenges exist than just limitations with risk models.

This was the topic of the first panel session of the day, which was led by Chris Caponigro, Head of Business Development at Mt. Logan Re Ltd., and who was joined by Brendan Plessis, Executive Vice President (EVP), Head of Emerging Markets at XL Catlin; Mansi Kalra, Programme Manager, NatCatDAX; and Yen Chin, Director of Business Development at AIR Worldwide.

“Given the ever-growing appetite in the capital markets to assume insurance risk, low penetration in many geographies of the world could perhaps be assisted by this abundance of efficient capital,” said Caponigro.

He continued to underline important reasons for a lack of insurance penetration in some parts of the world, including Asia, adding that there is “plenty of capital markets capacity, reinsurance capital, insurance capital to support risks when they are properly underwritten, the data is available, the modelling tools are available.”

Plessis expanded on points raised by Caponigro, explaining that, “The data suggests that the ILS market in this region is still relatively untapped. There’s a protection gap here that needs to be addressed. There are clear challenges here, and this is why today is so appropriate. One, we need to attract more capital; two, we need to collect more and better quality risk data; and thirdly, most importantly, we need to promote better collaboration,” said Plessis.

Parts of Asia are home to some of the lowest levels of insurance penetration in the world, and, these same regions are typically highly susceptible to a range of natural disaster events, including droughts, cyclones, earthquakes, flooding, and other severe, adverse weather events.

In poorer, more vulnerable parts of the world, such as developing Asia, the financial cost from natural catastrophe events is often borne by the government amid a lack of insurance take-up, a trend that hinders both economic and social development.

Plessis stressed that “insurance isn’t selling as it should be,” highlighting a lack of “understanding about the value of insurance and reinsurance, globally.

“We need to do a better job of educating,” he added.

Programme Manager at Singapore-based Natural Catastrophe Data and Analytics Exchange (NatCatDax) Alliance, Mansi Kalra, also underlined the need for more data in order to better understand the Asian protection gap.

“He need to collect more data, and, to understand the protection gap we also need to understand why and where there is a protection gap,” said Kalra, adding that in order to properly understand the protection gap in Asia, there needs to be a better understanding of the marketplace.

“In urban regions, we need to understand more about economic exposure, more of a risk-based pricing, and then as we move towards suburban or rural regions, then we need to see how that has to be tapped, whether it is microinsurance or other sectors,” she said.

The need for improved data was highlighted throughout the first panel of the day, and Caponigro questioned the panelists on exactly what the role of better data and analytics would be in trying to address Asia’s trend of underinsurance.

“I think data and analytics have a huge role to play in terms of bridging the insurance gap,” said Kalra.
Adding, “If we see insurance penetration today, what we do is the first thought that comes into our mind, is to compare the direct written premiums with the gross domestic product of the country, but that’s not an accurate representation of the insurance penetration. You have to compare it with the actual economic exposure on ground.”

Educating the region on the values of risk transfer was also a theme of the opening panel session, and something highlighted by AIR Worldwide’s Yen Chin, who’s role in developing markets includes places such as Indonesia, the Philippines, and Southeast Asia.

In such places, “we come across the terms protection gap quite a lot. And to define that, we see that the need is mainly on the commercial side, on infrastructure, for example. This is where we try and work with government bodies to try and identify the values to see what the losses are, potentially.

“With the protection gap, we try and identify the difference between developing countries and the developed countries. So, for the developing countries we see that insurance is more of a luxury rather than a necessity, so therefore how do you motivate people to take up insurance? It’s all about education,” said Chin.

Moving away from the protection gap, the next panel session of the day explored the numerous different ILS structures available in the marketplace, including catastrophe bonds, both traditional 144A and private, as well as fully rated and fully collateralised reinsurance, sidecars, and so on.

The panel was led by Scott Cobon, Client Service Director, ILS at Artex Risk Solutions, and featured Michael Stahel, Partner & Portfolio Manager, LGT ILS Partners Ltd; Steve Britton, Managing Director, Global ILS Management, Aon Risk Solutions; and Stefan Krauchi, Founder, ILS Advisers.

Stahel highlighted the benefits of different ILS structures, underlining that rated paper can make it simpler for ILS funds to trade with smaller and regional insurance companies, which might find a fully-collateralised deal more daunting.

Such an approach could perhaps be more suited to Asia, where local insurers and reinsurers could well be more open to ILS markets if they require less manpower and expertise than with a fully-collateralised structure, for example.

From an investor perspective, Krauchi explained that catastrophe bonds are very standardised, adding that it’s very easy to understand how it works for the majority of ILS investors.

“Another important point for the collateralised is that it’s transparent and has quite a long track-record. If you think that the first cat bond was issued 24 years ago, that is quite some time and so investors can see the track-record in the market. Another one is the liquidity. I think many investors appreciate the liquidity of the cat bond, especially compared with some other collateralised products, that’s also helpful.
“And, the last point I think that is important, the perils are mostly perils that are quite well researched and have models available, and those are the advantages from an investor point of view,” said Krauchi.

As noted earlier, in parts of Asia there’s a real lack of adequate and available risk data, which in turn hinders the development of catastrophe models, which subsequently limits the expansion of ILS capital into such areas.

“ILS investors, typically, like modellable risk, and certain asset classes haven’t been really modelled, yet, by the modelling agencies,” said Britton.

As well as a lack of comprehensive data and models for some parts of Asia, one of the issues with certain forms of ILS, such as the catastrophe bond and collateralised reinsurance space, is that the process can be very expensive and cumbersome, explained panellists.

Discussing the potential to lower costs and improve the efficiency of some ILS processes, Stahel noted that regulators could help with this issue by potentially being more flexible and more open to innovation.

“If you could get a fund with almost a dual regulation. So, it’s an investment fund, on the one hand, but it’s regulated as an SPI that is eligible to conduct collateralised reinsurance. You could get rid of everything in between, and the fund could conduct the reinsurance transaction with an insurance company. That would be the perfect solution. We’ve discussed this with all the regulators that were open to such discussions, but this takes an enormous amount of time.

“I think this would help the entire ILS space to really make a huge leap forward,” said Stahel.

Panel lead, Cobon, noted that with this new hybrid approach, where ILS structures have different models to be able to deploy their capital, “are these structures moving away from what collateralised reinsurance was successful in doing, in terms of efficient access to risk?”

“I think it’s the complete opposite. I think it improves access to risk, I think it opens more access to risk,” responded Britton.

To end the session, Cobon asked panellists if there’s scope to replicate the success of other ILS domiciles in Singapore.

“Singapore, why not? I mean, Singapore has a sovereign rating of AAA, that’s higher than one of the ratings for the USA. Singapore has a reputation as good hands, safe, regional centre,” said Britton.

Krauchi, added, “We think it is very good if there are new domiciles being added, that will help to bring new cedants to the picture. I think from an investor perspective, if the addition of an additional domicile leads to the pie becoming bigger, then it makes sense.”

“Singapore will be a global hub for transactions with a focus on Asia. Ultimately, I think it’s really down to the sponsor,” said Stahel.

Singapore as an ILS domicile was the topic of the day’s third panel session, led by Jonathan Paradine, CEO, Singapore Branch, RenaissanceRe, and which featured Rod Brown, Partner, Mayer Brown JSM, Singapore office; Benjamin Yeo, Managing Director, Financial Institutions Group, DBS Bank; and Stephanie Magnus, Head of Insurance, Baker & McKenzie Wong & Leow LLC.

“It’s very refreshing to see the country continues to evolve. They have a great reputation, they have a great regulatory environment, they are well respected globally, but they haven’t stopped innovating. And it’s very exciting to see some of things they are trying to do in the ILS space,” said Paradine.

He continued to highlight how well Singapore connects the dots. Having an ILS initiative in the works, combined with tax incentives, the InsurTech sandbox approach and the NatCatDAX, all of which underlines the region’s commitment to developing an “ecosystem that allows options for the country.”
Magnus explained to the audience that the SPRV framework for the ILS vehicle itself has actually been in place since 2008 in Singapore, which combined with the MAS’ grant scheme, supports the development of Singapore as an ILS hub for Asia, and the wider world.

“So, you’ve got the framework in place already, the insurance legislation as well as the securities legislation to support an ILS offering. And, then, given where the MAS wants to take it with the ILS grant scheme, it’s quite exciting and quite interesting,” said Magnus. Yeo, expanded on the fact Singapore has already started to establish itself as a global risk transfer hub, with a view of ILS supporting future expansion.

“The mainstream insurance plus the reinsurance, those are capabilities that Singapore as a market has built up, and it’s built it up really well. And, taking that to the next level, expanding that to include ILS, that’s something that I think would be the next stage of growth for Singapore as a risk transfer hub,” said Yeo.

Brown also noted how beneficial the insurance and reinsurance ecosystem is in Singapore, underlining the region’s commitment to both actively and progressively create a sound operational landscape for insurers, reinsurers, brokers, lawyers, and everyone else in the value chain.

“Singapore was quick to realise there is a lot of competition in this space and the renewed energy I’ve seen from the MAS and the government, is in no doubt, a response to people like the UK adopting a new directive and changing their laws. And I think for Singapore, it’s been sort of an awakening,” continued Brown.

Yeo, added, “From 2016 to now, the overall interest has increased significantly. The fact that we have seen a cat bond transaction out of London, that has led people to consider the possibility of also doing something similar in our part of the world.

“We are starting to see investors in Asia express an interest in this asset class, and I think that people are starting to realise the benefits of ILS, of cat bonds being uncorrelated with fixed income instruments, in general.”

But despite the increased interest from both the investor and sponsor base, panellists stressed the importance and challenge of getting the first deal done.

“In my very humble opinion, I think the issue is, until someone does one, no one really wants to be the first person. We’re very fortunate here, we’ve got a fantastic regulator in the MAS, but someone is going to have to go through that first, it’s going to be a tough process,” said Brown.

“The first is always tough, you’re breaking new ground,” added Magnus.
There’s clear potential for Singapore to establish itself as a regional, and possibly global hub for ILS business, but Paradine was eager to express hope that its development would produce more risk.

“Because right now, capital is not the problem in our industry, risk is the problem. There’s not enough risk to feed the capital. It’s finding the ability to transfer more risk to the capital, in an efficient way, is the way the world’s going,” said Paradine.

Matching risk and capital in an efficient manner was the theme of the final panel session of the day, led by Steve Emmerson, Head of ILS and Insurance at Tullett Prebon, and which featured Lawrence Cheng, Managing Director, Underwriting, Co-head of P&C Reinsurance at Peak Re; Chi Hum, Global Head of Distribution at GC Securities; and Rajiv Punja, Founding Principal and Ex-CEO of Arcus 1856 Syndicate, a Lloyd’s Syndicate backed by Credit Suisse Insurance Linked Strategies.

The panel explored the broad range of ILS structures that are now available, exploring how different mechanisms and vehicles enable third-party investors to access a wider set of risks in more regions than before, and in an increasingly efficient manner.

Speakers provided a brief overview of the ILS space in both the past and presently, while offering some insight into what it might look like five-to-ten years down the line, globally, and more specifically in Asia.

“The clients and the investors have both matured, in terms of utility of this instrument, in terms of managing their capital, and it goes to capital efficiency,” said Hum.

While ILS investors and sponsors alike have matured, alongside the creation of innovative structures and solutions, outside of Japan and Australia, ILS has yet to influence the Asian marketplace in the same way it has in more developed markets.

Punja explained that in his experience, the problem in Asia is that it’s very hard to compete “because the traditional reinsurance product is super cheap, it’s as simple as that.”

Hum, expanded on this point, “The traditional pricing is a huge hurdle, and from an ILS perspective, we need to find areas where we’re not competing directly. Because there’s advantages to our money, in terms of structuring and risk taking, that we can bring to the table.”

Cheng highlighted a need for more research and development surrounding Asian perils and called on catastrophe risk modellers to assist the market and develop solutions that enable sponsors and investors to better understand more peril regions across the continent.

“The biggest economic loss we’ve ever had in the world, was in 2011, the Japanese, Tohoku earthquake with the New Zealand earthquakes, with the Thai floods, that’s created a lot more losses than what we’ve seen in 2017, in the U.S,” said Cheng.

Punja, added, “The risk gap will close as risk distribution mechanisms for insurance change, that’s the thing that scares insurance companies the most. But it’s the thing that they focus on the least, in my opinion.”

Punja’s comments centred on the rise of technology, but one of the currently available structures explored throughout the day, and often underlined as the type of solution that could facilitate the matching of underserved, or unserved Asian risks with ILS capital, is the parametric trigger.

Designed to pay out when predefined parameters are met, such as sustained windspeeds passing through a predetermined location at a given time, a parametric trigger structure requires less advanced modelling capabilities than an indemnity structured trigger, for example.

Emmerson told the audience that the parametric trigger approach is likely to be the focus of Asia, which, would also put Singapore in a good position with regards to secondary trading within the catastrophe bond market.

“One interesting point, in terms of Asia and the future of Asia, is that industry loss-based, or parametric-type bonds do trade, generally speaking, more frequently than the more complex indemnity-based bonds. And, going forward, in view of what we’ve heard about Singapore as a domicile, and concerns raised about secondary trading, if the focus, which is naturally going to be the case, I believe, is on those alternative triggers to indemnity, I think you’re on to a head start with the secondary trading,” said Emmerson.
After a final coffee and networking break, the audience was treated to a keynote speech on hedging for ILS, delivered by the CEO of AlphaCat Managers Ltd., Lixin Zeng.

Before delving into hedging for ILS, he started by discussing the efficient nature of ILS capacity, underlining that both globally and in Asia, “the fact ILS has gained a meaningful market share in this business, is because it’s a low-cost provider of capital.”

Zeng explored the importance and impacts of hedging underwriting risk on ILS fund returns and discussed how portfolio theory approaches to hedging can have benefits.

Audience members heard what hedging options are available in today’s market, and Zeng provided examples of different strategies and explained the rationale for different hedging approaches.

Interestingly, the keynote speech then turned to last year’s catastrophe events and whether capital providers have been frequently discussing differentials in performance in 2017 around hedging, and if they are making decisions about how to allocate capital based on the actual performance.
Zeng explained that the events of last year have prompted a lot of these types of discussions.

"Especially whether or not, or the amount of hedge they bought last year actually are directly related to its relative performance. The majority of investors that have given us feedback, made it clear that they prefer us not to use hedge, just for the sake of maintaining relative performance.

"Obviously, they encourage us to use price hedging, but if you have peril hedging that actually costs you expected profit, their view is that they can control the risk themselves by deciding how much they invest with us.

"That said, there is a minority. They wouldn't say this explicitly, but we get the sense that people do care about downside relative performance more than upside performance on a long-term basis. The vast majority of feedback is of the former category," said Zeng.

To end the day, Paul Schultz, CEO of Aon Securities, discussed the future of ILS both in general, and in the Asia-Pacific region. He drew on some of the previous talks from the day, highlighting a dangerous lack of insurance penetration across the majority of the region, noting a need to tackle the affordability issue as well as a growing need for education around risk transfer in order to narrow the protection gap.

"And when you look at the future, in terms of demographics, in terms of population, in terms of the concentration of value in different types of locations, certainly Asia is very substantial today, but even more substantial going forward.

"It truly is staggering when you look at some of these numbers, and so solutions are going to have to be made available. I think ILS has a role to play, alongside the other participants in the industry,” said Schultz.

One of the issues in Asia, explained Schultz, is the complexity with some of the perils and types of risks, and also the fact that when compared with other parts of the world, the availability of both data and modelling is perhaps not as strong, which ultimately hinders market development.

But despite this, three of the top ten cat bond issuers are from Japan, said Schultz, highlighting the opportunity with parametric trigger structures for market penetration in difficult markets, a model already used in the Asia-Pacific region and that can be replicated and expanded.

Discussing Singapore as an ILS domicile, Shultz said, “From a business perspective, being closer to home makes transactions, makes trading easier, it’s basic deduction. The challenge here is going to be striking that balance between the pro-business side of a domicile, and what’s necessary and important from a regulatory and government perspective.

“There’s some challenges, but clearly the motivation, the foundation, the basis and all of the reasons to do this, are so compelling, that again, I think we just have to find a way to strike that balance in the middle.”

Ultimately, said Schultz, investors are going to want to access Asian risks, driven by diversification outside of the highly competitive U.S. property catastrophe space.

"The education process, the availability, the affordability of the products cannot simply be led by the industry, and the industry being collectively the insurance, reinsurance, and ILS markets. There has to be a public sector component to it, there has to be some education, there has to be ways of increasing the affordability and the access to these types of products," he added.

“We have tremendous momentum in ILS. Really, the future is bright,” concluded Shultz.

To all our attendees, thank you for joining us, we hope you enjoyed the day and will attend again next year in July for ILS Asia 2019.

To all our speakers, thank you for travelling so far to participate, for providing insightful and thought-provoking discussions and for engaging positively with the Asian market attendees.

Finally, we’d like to thank our kind sponsors of the event, without whom the day would not have been possible.

Artemis ILS Asia will be back in Singapore in July 2019. We hope to see you there!
Rated A/Excellent by A.M. Best

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