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Post-event Report

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INTRODUCTION

Welcome to the Artemis ILS New York 2018 conference report, which provides insight into some of the debates that took place between speakers and attendees during Artemis' second event in the region.

The event was held in New York City, in midtown Manhattan at a purpose built event space, Convene, on West 46th Street. Some 295 attendees registered for the event, and the waiting list for spaces exceeded 70 by the day of the conference.

Artemis' second ILS New York conference was even more successful than our first in the region, and attendees were treated to insightful and thought provoking discussions from leading industry figures throughout the day.

Held in early February, 2018, the event followed fast on the heels of the large loss experience of 2017 and the key January renewals season, and the audience heard how well the ILS market responded to events, ultimately evolving into a more sophisticated provider of global re/insurance and risk capital.

This year's event had a focus on building the future of ILS, with speakers and attendees exploring the entry of ILS into new regions and risks, expanding its influence in the natural catastrophe space in both developed and emerging markets, as well as discussions around investing in the space from both the sponsor and investors side of the equation.

Specifics of the ILS market and how the role of capital markets in re/insurance has changed were explored, with speakers from all parts of the risk transfer chain providing concrete examples of both the influence of ILS now, and its potential to impact the future of risk transfer.

Artemis ILS New York will be back in February 2019. We hope to see you there!

Steve Evans
Founder & Editor, Artemis.bm



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The first session of the day was led by Tom Johansmeyer, Assistant Vice President, PCS Strategy and Development, Verisk Insurance Solutions, and focused on distribution and accessing risk. To kick things off, Johansmeyer questioned panel participants on whether they felt distribution is broken and inefficient.

"It's not broken, it works, but it could be a whole better," replied panellist Alan Punter, Consultant, Capital Markets, RFIB, highlighting the many frictional costs that exist in the way the industry has traditionally done business.

However, in the view of the ultimate end buyer, "it is broken," said panellist Kevin Mahoney, Senior Vice President, Venbrook Insurance Services. He continued to note that from the buyers' side there perhaps isn't contract certainty and that people don't really understand what they're buying. But, while it might be viewed as broken from the end buyers side, from the brokers side, "it's kind of the necessary evil to get the trade done."

"I wouldn't jump to it is broken, necessarily, incredibly inefficient, yes, but I'm not convinced it's broken at the point," said Mahoney.

The inefficiency of the risk transfer value chain is often debated in the ILS space, particularly in recent times as capital markets backed capacity has looked to get closer to the original source of risk. And while it might well be inefficient and overly costly throughout various parts of the chain, Skip Cooper, President of AmWINS Group, Inc., underlined how the chain helps the average client understand their protection.

"Until you can get transparency that can be analytically considered and priced, it's very difficult for people that aren't insurance people to take a risk that they don't know about. I think all those pieces in the chain, a lot of times contribute to helping clarify that and making sure people are buying what they hope they're buying," said Cooper.

Cooper argued that when it comes to capital markets trying to price business, there's a need for clarity around the exposure and a way to analyse that numerically, otherwise the lack of insurance knowledge suggests people don't sufficiently understand the risks.



Tom Johansmeyer –
"Is there a distribution opportunity to match ILS capital with the original insured?"

"I think that's really where ILS can come in, just take the certainty of the payout," said Mahoney, adding that "if we can get back to where more of that dollar can get to the insured, we can start running those risks (California earthquake, for example) and it can still be profitable."

With California earthquake and wildfire risks in mind, alongside other frustrating exposures such as cyber and terror, where it's ultimately challenging to get original retail protection, Johansmeyer asked panellists, "Is there a distribution opportunity to match ILS capital with the original insured on more than the niche corporate cat bond basis that we've seen?"

"I think someone has to build the portfolio. The ILS capital guys aren't going to get involved or want to get involved in all the distribution and admin that is necessary. But they can come closer to the risk, but I don't think they are going to come right to it," said Punter.

Cooper, added, "There's a lot of steps in the process that aren't free, and you start building that up. I see the chain becoming more efficient, it definitely needs to be more efficient, but I don't see it going away."

"Whether it's traditional or ILS markets, it's hard to eliminate people that are bringing value. I do think that where we'll head is that people that aren't bringing value will have to work for less or be gone."

He continued to discuss the 2017 catastrophe events, underlining the fact that the participation of ILS into the reinsurance industry contributed tremendously to the ability of carriers to absorb one of the costliest catastrophe loss years on record.

"One of the beauties of this and one of the smoothings of our industry pricing volatility, is that the capital markets wants to come in and wants to analyse risk on a real exposure of risk, it's not emotional, it's mathematical," said Cooper.

Mahoney responded: "Imagine the next evolution of that being direct to the insured. And the competitive advantage that insureds would have if they're able to access ILS capital. If the insured can want, and see and understand that competitive advantage I think they would jump all over it."



"But how do they find each other?" said Cooper.

"The match making part is the tough bit, and that's obviously what distribution is, and it's important to remember that without distribution there is no thing," said Johansmeyer.

With 2017's catastrophe experience and the January renewals season still fresh in everyone's mind, the influence of ILS capital and its response to losses was unsurprisingly discussed throughout the event, including the first panel of the day.

Panellists explained that owing to the presence of ILS some 20% of the industry loss fell outside of the traditional space, which showed that ILS capacity really is a good way to stabilise the rated paper industry.

The second panel of the day focused on underwriting, and, led by Rick Pagnani, Chief Executive Officer (CEO) of Mt. Logan Re Ltd., began by exploring the response of the ILS market to 2017 catastrophe events and whether the reaction of ILS was a surprise.

"Anybody who has been following the evolution of what's happening with ILS and the capital markets, shouldn't be surprised. This is what we've been saying for years, we just haven't had the loss events to prove that out. But certainly, to everybody that has been in the market now for a long time, it's not a surprise," said Kathleen Faries, Head of Bermuda Branch, Tokio Millennium Re.

In the aftermath of 2017 catastrophe events, re/insurance and ILS sector commentary has suggested that there will be some winners and some losers. And while Faries was eager to point out that the clear winner from recent events is the end buyer, there isn't so much a clear loser, but more there's the "seriously challenged" that need to understand how to live and make a profit in the changing market landscape.

"It's very good that we've got a stable, flatter market that's better for buyers and they can rely on that. It was clear that ILS investors aren't scared by losses, and so I think we can have confidence now in that capital markets pool, so a lot of good things happened," said Faries.

Laura Taylor, Managing Partner and Chief Financial Officer (CFO), Nephila Capital Ltd., agreed, saying that the "ultimate winner is the policyholder."

"This is a good thing. There was opportunity in the market post-event, capital flowed in quickly, easily and efficiently, and for the first time we've got an efficient market. So, I think there is a threat, but I really view it as an opportunity."

"We've been talking about change as prices have been softening over the years, and maybe this is now, finally, the time that people are going to really adopt it and start changing the model," said Taylor.

John Parry, the CFO of the specialist Lloyd's of London insurance and reinsurance marketplace completed the day's second session, and suggested that while the third and fourth quarter catastrophe experience was a test, things could have been far worse.

"There's been some demonstration of the resilience of the industry, but I think that's got to be a moderate level of comfort given that these losses weren't as significant as they could have been."

"I think as a test case for the ILS market it's there, but I don't think it is going to put anybody off and there's more capital that's going to be attracted to the industry," said Parry.

Pagnani agreed that had hurricane Irma, for example, followed some of the worst-case scenarios that were being reported as it approached the coast, the conversations at the conference would have been a lot different.

"The market did respond well, but I would argue it was not truly tested or stressed, but it did behave well," said Pagnani.

The day's second panel then moved on to explore market disruption, in light of the rise of InsurTech and technological advances, such as the blockchain, that are looking to disrupt the insurance value and distribution chain, ultimately highlighting inefficiencies in the model.

"It's a fascinating subject, but it is a little bit depressing for our industry because the odds are really against us," said Faries, drawing on what she describes as the industry's "vested interest in complexity."

She added: "We've built up this industry to be very complex, and we like bespoke, complex solutions, so it is very hard to see our way through that. But, I do think, with blockchain for example, we are going to see incrementally people doing things. It's happening, and I think the right thing to do is to get the industry together, to think about how we do this together."

Taylor agreed, and highlighted the lack of investment in technology in the underwriting process, a very costly element of the risk transfer chain where she feels there's an opportunity to increase efficiency and bring down cost.

"Insurance and reinsurance companies have focused on automating or investing technology in finance, and in actuarial and operations and you're seeing cost-savings there. But, there's been almost zero investment of technology into the underwriting equation, and in fact, underwriting costs are the highest they've been for some time," said Taylor.

Parry also shared some thoughts on disruption, stating that "in terms of the distribution chain and the time that an MGA, broker, wholesale broker, carrier, quota-share, or reinsurer spends time reconciling data, that is no value add and surely that is a great opportunity for blockchain or other technology to do that.



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Rick Pagnani –
“The market did respond
well, but I would argue
it was not truly tested
or stressed, but it did
behave well”

"But in terms of them assessing the risk, insurance, it's a data rich industry, whether we mine it enough or not, but it is never going to tell you everything about the future, otherwise no one would buy it."

Another theme that was evident throughout the day was the expansion of ILS, both in terms of new perils and territories, but also in terms of where it already plays a part but has the potential to become more meaningful and influential.

"As an industry we're always looking for risks that are underserved. For us, we've been focusing on weather and climate as one of those risks. Both businesses and governments have exposure to this, and if you look at it on a global basis, the exposures are large enough that they could be securitised. And that ranges from governments looking to protect against famine, to crop failure, or helping finance renewable energies, it can be very broad," said Taylor.

Parry, added: "ILS I think is going to go beyond natural catastrophe soon, it has already started and getting securitisation around pandemics, space weather, terrorism, I think there's plenty of stop losses that could appeal to the ILS market, pretty soon."

The potential for ILS to participate in complex risks like cyber was brought up by an audience member towards the end of the second panel, and Pagnani explained that while some in the sector might be zeroing in on it, overall, we're not there.

"If you look at the actual supply of third-party capital to tackle this, I think it's reflective of the fact that we're not quite there yet. You've got to convince the capital markets that you can price it adequately and you can aggregate it, etc. I think we are moving toward it, there's an opportunity, and I think cyber is a perfect opportunity where third-party capital should come to bear," said Pagnani.

After a second coffee and networking break, event attendees heard ILS market experts discuss investing in the space, in a session led by Luca Albertini, CEO, Leadenhall Capital Partners LLP, exploring various sub-sectors of the industry.

Albertini began by highlighting the broad range of instruments available to investors interested in the ILS space, noting that "new innovations come every year with new ideas."

Adding that "what might take off, is more of whatever the protection buyers do want to buy, given what is available is plentiful and reasonably priced."

He continued to underline positive evolutions in the sector, including the rise of indemnity protection, which, while bringing underwriting challenges does "take ILS capital closer to what buyers actually want to buy."

The traditional 144A catastrophe bond remains the second-largest element of the ILS sector, after the collateralized reinsurance market, and experienced a record-breaking level of issuance in 2017, with further growth expected in 2018.

Albertini questioned panellist Andreas von Reitzenstein, Sub-Head Underwriting, Credit Suisse, on the importance of the 'old fashioned' 144A structure.

“Over the last 15 - 20 years, we’ve seen the cat bond market, especially the regulated 144A cat bond market, come in and bridge the gap between the liquidity needs of a capital markets environment and the capital needs to the insurance or reinsurance community.

“144A is obviously a way to have a standardised product which gives access to a large capital base, it helps the industry,” said von Reitzenstein.

Coming from the sponsor side, fellow panellist Judith Klugman, Global Co-Head of ILS, Swiss Re Capital Markets, said that most sponsors understand the difference between the capital, the 144A market and the traditional market, noting that she would love the collateralised reinsurance more closely akin to the traditional market.

“They see that those are really two different markets, that are on two different cycles, and what they get through the 144A capital markets, is they get true transparency into pricing. And that is somewhat fundamentally different than the traditional market,” said Klugman.

Liquidity was highlighted through the session as an important element of the 144A market, and while this clearly benefits the investor base, Klugman noted that from the sponsors perspective, they’re getting “price discovery, and a very broadly distributed transaction.”

The third panel of the day also featured Andries Hoekema, Global Head of Insurance, HSBC Global Asset Management, who provided some thoughts on investing in the space from an asset managers perspective, underlining the importance of data and understanding the tail risk.

“We like to allocate on the basis of comparing equities and bonds, and cat or other ILS-type assets, on the basis of expected returns. And if you want to have expected returns, you first need to have this idea of the relative value, on a very long-term basis, of the asset class compared to other asset classes. And secondly, you need an idea of current valuation.

“To really get the flood gates open when it comes to traditional asset managers piling into the asset class, these are the two things you need to do. 144A is a great starting point and I think it could well be that the development over the coming years, will be one where traditional asset managers will start dipping their toes into the water in these more liquid asset classes,” said Hoekema.

The panel discussed a broad range of interesting and relevant topics surrounding investing in the ILS world, underlining the persistent importance and attractiveness of the sector as a



Andreas von Reitzenstein –
“144A is obviously a way to have a standardised product which gives access to a large capital base, it helps the industry”

diversifying and uncorrelated asset class, as well as its increased sophistication and maturity that’s supported by its response to 2017 catastrophe events.

Liquidity in the marketplace was discussed throughout, as was the secondary trading element of the ILS world, which included the exploration of both live and dead cat trading, before Albertini questioned panellists on the use of rating technology in the industry.

“Is there a better use of the rating technology that we can use to explain ourselves better to our counterparties, to protection buyers, outside of the cat bond world? Is this a new form of investing that we can see more of in the coming months?” said Albertini.

von Reitzenstein responded, noting that “if you look at the rating agencies, and if you look back 20 years, especially after 2005, I think the rating models have improved massively.

“So, the rating agencies have been doing a better job, there are more and more solvency models, which also protects the insurance companies, and also the reinsurance companies today are probably much safer than they used to be 10 years ago, which is a good thing.

“I think for the ILS community it is important to recognise that the rating plays a role, and if you want to access broadly in the insurance and reinsurance space, you also need to come up with a model to provide a rating. And you can do it via Lloyd’s, you can set up your own carrier, there are various options to do it, but the constraint is your own book, your own portfolio.

“As an ILS manager it doesn’t help if you get an A.M. Best rating, because you’re not the risk taker, the risk taker is the fund, or the vehicle. So, you would need to get the rating for the fund, so it makes it quite complicated and then there’s some movements in the funds and some volatility, so it will be very difficult to convince a cedent of security of your portfolio. I think that’s a constraint and it is not easy to get around that.”

Each session of the day included debates around ILS market growth and its expansion into new territories and perils, and Klugman explained that for reinsurance giant Swiss Re, the challenge they think about is really funding the protection gap (disparity between economic and insured losses post-event).

“So, as I see the growth in where the 144A market really can add a lot of value to potential sponsors, is those sponsors that aren’t actually getting protection for their cat needs. That is



Andries Hoekema –
“Traditional asset managers will start dipping their toes into the water in these more liquid asset classes”



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where we really see the growth, and that is where a broadly distributed, fully-transparent, that has full price discovery, where that really provides the value add," said Klugman.

After lunch, John Seo, Co-Founder, Managing Principal, Fermat Capital Management, LLC. led the fourth session, which looked at the future of risk transfer and included Michael Bennett, Head of Derivatives & Structured Finance, World Bank Treasury; Cory Anger, Global Head of ILS Origination & Structuring, GC Securities; Jennifer Montero, CFO, Citizens Property Insurance Corporation, Florida; and Brian Warren, the Director of Risk Management at Microsoft Corporation.

As noted previously, filling the so-called protection gap was one of the many themes discussed throughout the day, and Seo continued this trend by telling the audience how both the World Bank and Microsoft are relevant to this part of the ILS space currently, and in the future.

"It is very clear that the World Bank has finally entered this market, and entered in a big way," said Seo, highlighting that the global entity was working on its fourth transaction during the Artemis ILS NYC 2018 conference.

Bennett, commented: "The World Bank has been in disaster risk management advisory for a very long time, but only in the last ten years have we moved from just providing advice to actually executing risk transfer transactions. We started doing that essentially in the reinsurance area, and in 2014 we set up a separate bond programme under which we can issue cat bonds in our own name."

While the protection gap is certainly a global issue, something that was highlighted recently by the lack of flood protection in the U.S. after hurricane Harvey, dangerously low levels of insurance penetration can be seen most notably in emerging, often poorer parts of the world that are very susceptible to a range of natural catastrophe risks.

This is something the World Bank has identified, and, something which is evidenced by the fact its natural catastrophe-focused deals have benefitted member countries that are typically poor, under-developed and highly vulnerable to natural catastrophe risks.

Furthermore, its pioneering 2017 deal, which was the world's first pandemic bond, is designed to benefit as many as 75 of the world's poorest countries in the case of a pandemic outbreak.

"You won't ever see us putting the Bermuda SPV business out of business, we're not looking to dominate, generally, the cat bond market, but we do have room to grow," said Bennett.

The potential for the World Bank to grow in the ILS market, while at the same time expanding the remit of the asset class is clear, and Bennett was eager to note that the World Bank loves the transparency of the ILS market, adding that it removes restrictions.

As the World Bank looks to deepen its relationship with the ILS market, Seo noted the "possibility that the World Bank can help certain key, critical players in the U.S. market."

Citizens property Insurance's Jennifer Montero, spoke in depth about the hugely challenging and detrimental assignments of benefits (AOB) issue in Florida, a trend that over time has mitigated the positive rate impact for reinsurers in the state, that's driven in part by the participation of ILS capital.

The fourth panel of the day featured Microsoft's Director of Risk Management, Brian Warren, who is in charge, among other things, of insurance buying for all of Microsoft. Warren explained that both cyber risks and natural catastrophe risks are a threat to the company's data and infrastructure, which is expanding all the time.

"We wanted to look at the earthquake coverage again, because we hadn't really looked at it in a long time. And we saw in this past year that the industry really has passed a maturity milestone, with surviving the last year of natural catastrophes and still having capital coming back in, so the marketplace seemed like a good thing to explore," said Warren.

Later in the session, Seo questioned Warren on cyber risk and the potential for a cyber equivalent of a seismograph, in a sense, where technology reports back breach attempts, etc.

"This is pretty blue sky, actually, but looking at the paradigm of how ILS has developed around earthquake and hurricane, we just naturally thought, 'what would we have to do to have an equivalent type of system,'" said Warren.

In line with the theme of the day, building the future, Cory Anger of GC Securities discussed some opportunities in the space, highlighting room for the World Bank to grow and the organisations attractiveness, as well as the benefits the World Bank brings to the market.

"I don't think the risks will stop just on natural disaster risk, we spend a lot of time on that. I think what we're trying to do with ILS, is not just replicate what's already there, but maybe let's take a backwards step and re-evaluate exactly how we want to protect some of these risks. A big challenge for this room, is collateral release, in the sense of being able to take on longer duration liability, and how do we manage that. Because there is a much larger pool of risk if people are willing and able to take longer development period.

"You have to understand that when you translate these products down the system, because what I think is a theme of today and it is frankly a theme going on in the industry, you have to think differently about the implementation of the products.

"Part of this unlocking and particularly moving down in the retail system, has to be we can't be beholding of taking the structures that worked for insurers and reinsurers in property cat and expect that the same structures are going to work on all these other risks where this is a need. And I do think that if we can, and we can collectively, structurers, cedents, risk takers, can take off that framework and be a little more creative, more stuff will come out. I think if we can be more thoughtful that way we'll see tremendous innovation," said Anger.

To end the day, attendees were treated to an expert Q&A panel, which featured session leaders Luca Albertini, Tom Johansmeyer, and John Seo, as well as panellist Kathleen Faries.

The final panel of the day covered a number of burning industry issues, drawing on previous discussions and also delving deeper into the need for greater efficiency, as well as some exploration of the data and technology side of the marketplace.

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**Cory Anger –
 "I think what we're
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Albertini noted the rise of technology and advances with artificial intelligence, but using the 2008 financial crisis as an example, was eager to remind the audience of the importance of actually looking into what is being covered, not becoming too reliant on data and ultimately remembering the necessity for, and value of underwriting skill.

Faries, added: "The ideal would be that we get rid of a lot of the busy work that underwriters do. Trying to dig at data, trying to get the information needed, being unable to get it from brokers so having to dig through the data. So, to not be doing that but instead be actually adding value by looking at these things in a deeper way. Because there is still a lot of room for things to get more efficient on the simple stuff."

The final session also explored parametrics, and Seo said that he thinks "you're going to hear more about parametrics as you see coverage where the timely payment is super valuable."

Johansmeyer, commented: "We did some market research on this, on reputational risks on parametrics, and we found that in addition to speed-to-payout, what seems interesting is where you have certain predictable fixed costs that come after an event. So, in addition to needing money now, if you know what those things are going to cost then you're inherently reducing your basis risk.

"So, you think about product recall, for example. I know I'm going to spend X amount on legal costs, X amount on PR, and so on, you can generally get a sense of what the cost is going to be. So, you're basically taking easily understandable and anticipatable cost that would occur post-event.

"In the end it works out great, parametric is easy to understand, it's a nasty risk that nobody wants to underwrite and doing it on an indemnity basis would be brutal. So, fast diffusion, predictable cost, low basis risk, and it gets you out of the woods while you solve the real problem."

Moving on from parametrics, Albertini highlighted that a lot of money is looking to enter the industry, but "we can't accept all that is coming," and, "we have an insurance gap.

"So, we have primary insurance companies that say, 'I want perfect protection,' indemnity, and then you have governments and corporations that say, 'I need fast money,' which is parametric, and so on.

"For us, the important thing is to be ready to analyse the risk in whatever form and then there is not one solution, but maybe a basket of solutions for many people, and try to understand how to close this gap would actually help our sector. So, definitely we are very motivated to control the brain power to make it work.



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**Luca Albertini –
 "For us, the important thing
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 risk in whatever form"**

“Every one of us should have the brain at work, looking at one particularly example, looking at a basket of examples. It’s something that we should have dedicated resources on within ILS, because it’s within our interest, it’s increasing the diversification opportunity, reducing the insurance gap and deploying more money, which is what we get paid to do,” said Albertini.

The potential for ILS to play a meaningful role in other exposures and territories, particularly outside the highly competitive natural catastrophe space, was debated by speakers and attendees throughout the day. But speakers were eager to remind the audience that much can still be done in the natural catastrophe arena, most notably in emerging markets but also in developed ones, such as U.S. flood.

The ability and willingness of the capital markets to participate in the National Flood Insurance Program (NFIP) was brought up in the day’s final panel, with attendees and speakers debating the availability and utilisation of data, and how large events help to calibrate the model.

Seo, said: “This is something that has always blessed the ILS market. The ILS market, predictably, comes into play after a large loss, and the wonderful thing about a large loss with all its messiness and all its chaos, and all the unexpected things that happen, is that that can be used to calibrate the model.”

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

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

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

Artemis ILS New York will be back in February 2019. We hope to see you there!



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