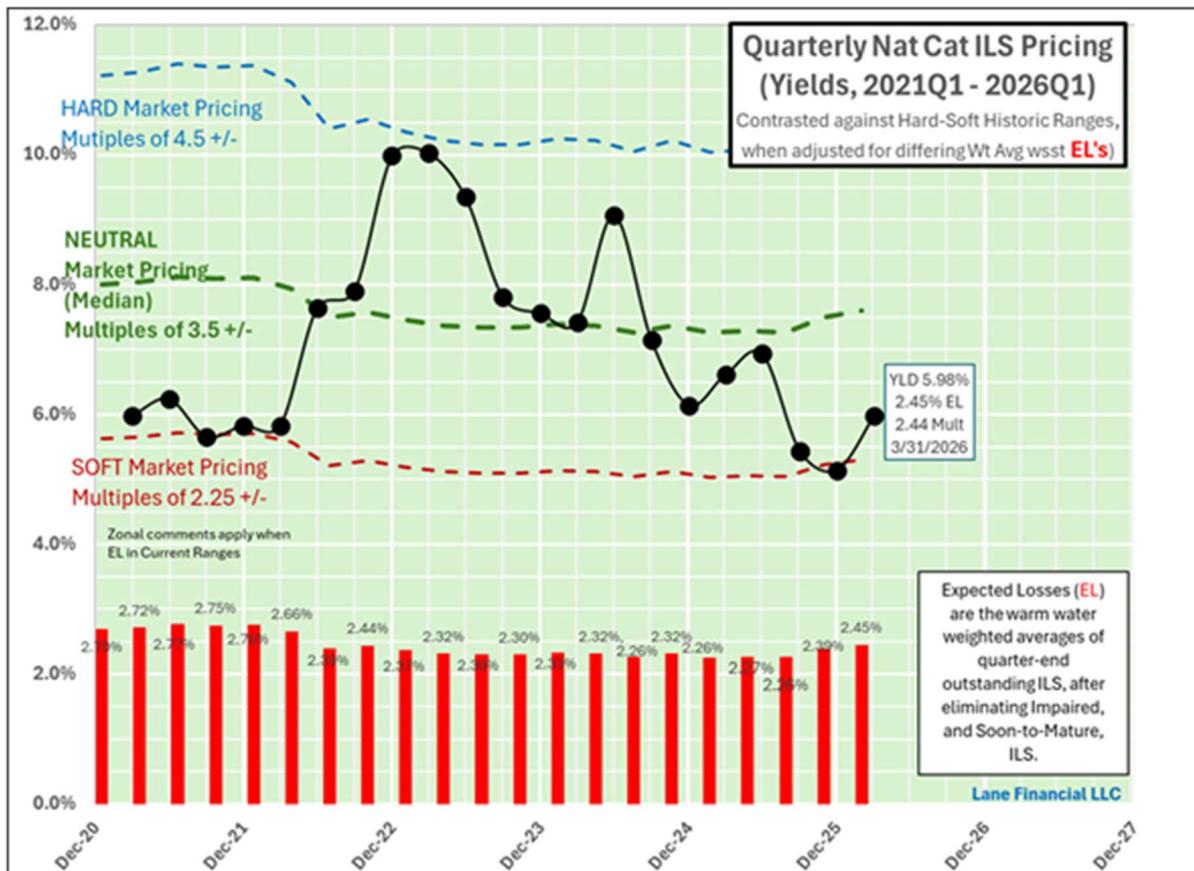


Good News, Bad News and Old News By Morton Lane, President

The good news is fairly simple. As the quarter-end yield chart shows, the outstanding, non-impaired, Nat Cat ILS are no longer as soft as at the end of Q4 2025. Yields, the secondary market proxy for Rate-on-Line premium levels, are half-way back to the neutral zone. The yield on the outstanding set of ILS at each quarter-end¹ has risen from 5.14% to 5.98% against a rise in the Expected Loss [EL] from 2.39% to 2.45%, a net gain in the underwriting margin of 0.77%



¹ The numbers here are as at 12/31/2025. They differ by a few single digit bps from those in the prior paper, which was prepared a few days before the 31st.

(77 bps). This is good, but not great, news for investors in ILS. It is certainly better than seeing softer prices descend below the historical thresholds shown on the chart.

The other side of the coin contains the bad news. As yields have risen, bond prices have fallen. The average bond price of the outstanding Nat Cat ILS at the end of 2025 was \$102.9. Currently the average is \$101.7. By this measure the investor has lost \$1.2 points (120 bps) from his total return calculation. That represents a significant drag on first quarter underwriting results. So, the secondary market is saying, from here on the outlook is slightly better, but to get to this point the first quarter results have already been eroded below expectation.

All of the above has the usual caveat that realized losses during the year will be at expected levels.

The third element of the investor's total return is the interest rate earned on collateral - the money market, or treasury, rate. At year-end, when looking ahead, we had predicted one drop of 25 bps in the Fed Funds rate early in the year followed by another, maybe 50 bps, after the president's replacement for Chairman Powell arrives at the Federal Reserve. Combined with the year end underwriting rate we predicted a total return of approximately 6.0% for ILS investors in 2026.

Since then, the Fed outlook has changed. The president's nominee, Kevin Warsh, has found his nomination process deadlocked indefinitely by Congress. More importantly, a man-made disaster – The US/Israeli war on Iran – has shifted the US inflation rate outlook considerably. Depending on the war's resolution and duration the interest rate outlook for the rest of the year remains cloudy at best. The market itself is no longer pricing in interest rate cuts. It actually sees the prospect of steady rates until mid-or year-end when costs of the war will feed through and may require increases in the Fed Funds rate.

Given the uncertainties - Warsh may or may not be able to give the president a 50 bps cut, and he may or may not have to reverse course as war costs feed through the system – we stand pat on our prediction. Expected Nat Cat ILS total returns for 2026 around 6.0%, net of losses being at expected levels.

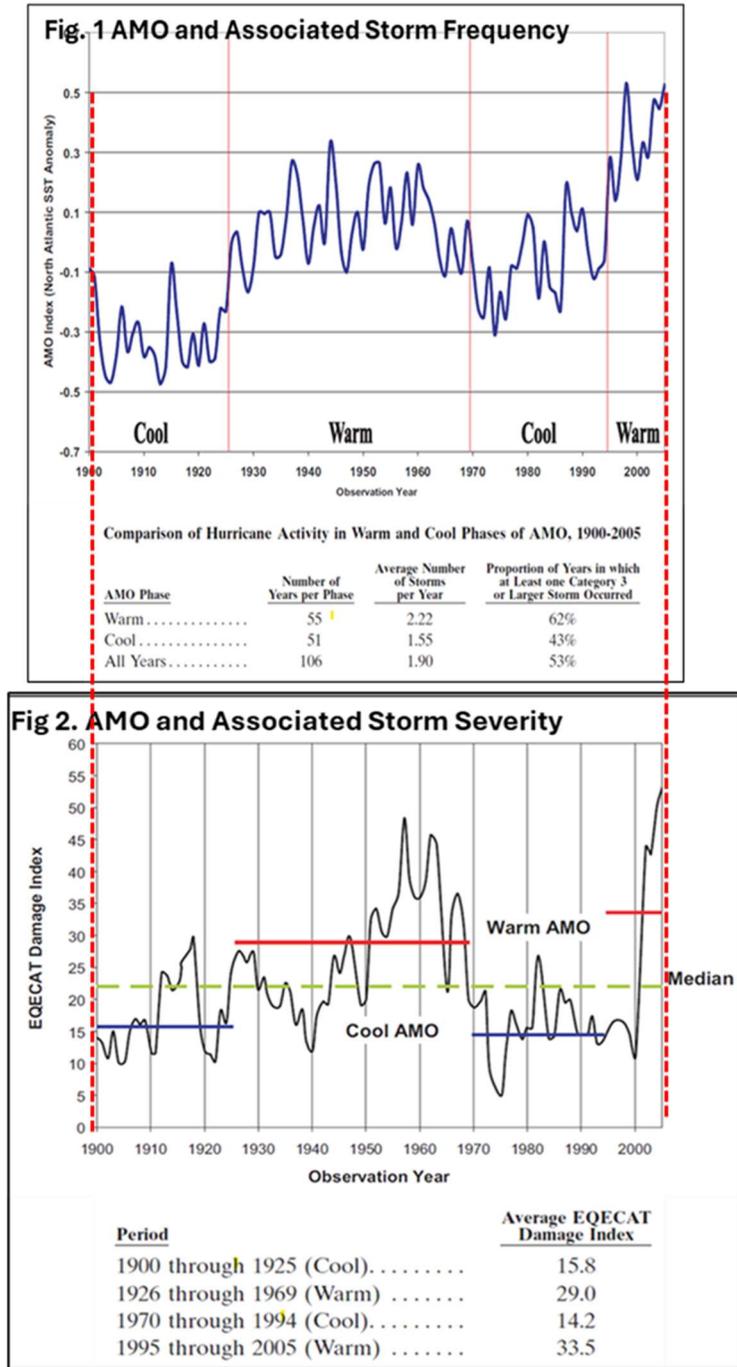
Old News

Twenty years ago the nascent ILS market changed its earliest practices when distributing price indication sheets. Instead of quoting a single EL (and associated statistics) in the Offering Circular [OC] and investor presentations, it started to quote two ELs for ILS deals with US wind exposure. However, in the last couple of years the industry appears to have reverted to showing a single EL on its price indication sheets. It provokes the question why the first change and why the change back (probably to the new EL rather than the old one)? Enquiring minds might want to

know. In this “Old News” section, we seek to explain in a series of graphics. Going back to 2006, an ILS deal modeled by EQECAT (Calabash Re A1, series 2006-1, CUSIP #128044AA2) broke

records with precedent by issuing the first deal to provide investors with two ELs (each with their associated statistics such as attachment probability [PFL] and probability of exhaustion). Their rationale is explained in the OC and is captured here with two graphics used therein – Fig 1 and 2.

The upper panel (Fig. 1) shows a measure of frequency for land falling US hurricanes and the lower panel (Fig. 2) shows the severity of such storms. The measures are EQECAT Indices and are in the lower panel directly related to the sea surface temperatures in the North Atlantic. It shows that while prior models by them, and their competitors – RMS and Verisk (formerly called AIR) – chose the median or “Long Term” view of that temperature and fed that into their loss models there was, in the scientific community, a recognition that there existed some Atlantic Multidecadal Oscillation [AMO] around the long term. Furthermore Fig 2 shows that we might be entering a warm phase – see red horizontal bars - and given their insight that there appears to be more hurricane activity when the sea surface temperatures are higher, investors might like to know. Therefore, they provided both a long-term EL and a short-term EL



– initially labelled SSST and WSST for Standard and Warm sea surface temperature models. All competitors quickly followed suit, and every subsequent ILS involving US Wind received the two different risk measures. It was up to the investor to decide which EL he believed and the

presumption made by many was that the market would be set by the more conservative measure. Whichever was chosen there was of course only one premium level that one received – whatever model you believed.

It was said by some junior colleagues that Dennis Kusak, EQECAT’s manager at the time, thought that the work he had done on ocean floor bathymetry which affected storm surge modeling would be more consequential in the long run than the two EL practice. But the world thought otherwise. WSST models appear to be here to stay.

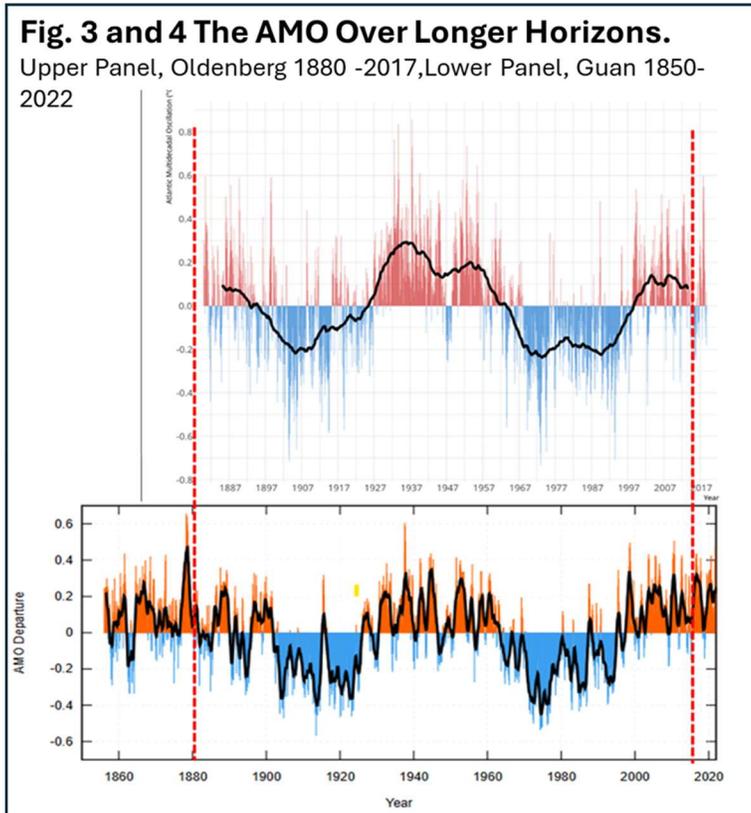
Other Points of View

Outside of the ILS market, the debate about climate change became more intense – and political. Was the undeniable rise in sea surface temperatures in the North Atlantic and elsewhere, just a normal oscillation, or a shift to a new elevated plateau of high temperatures? It mattered where you stood on that subject beyond the insurance world.

Two scientists decided that the measure needed to be improved and that the range of historical reference needed to be extended. (This was not motivated by ILS concerns, but for the larger world context.)

In 2009, Oldenberg et al proposed different measures, as did Guan and Nigam. They also managed to find new data. EQECAT’s graphics covered the period 1900 – 2006. Oldenberg

managed to get back to 1880 and Guan back to 1850. Their two views of AMO shift the focus somewhat, when compared to the Calabash OC. There are a number of observations that we can make from Fig. 3 and 4. Note, first, that the vertical dotted red lines are used to align and synchronize the horizontal time scales. First, it is clear that under either measure the cool and warm oscillation phases are almost identical. Second, it appears to be the case that the warm phases tend to be longer than the cool phases, perhaps 30-40 years compared to 20-30 years. Thirdly, it is clear that neither the warm nor the cool phases occur without the odd



year or two pointing in the opposite direction. The debate about whether the climate, as evidenced by the North Atlantic sea surface temperature, is the new permanent plateau or simply a normal oscillation is likely to go on and on.

Back to a single EL

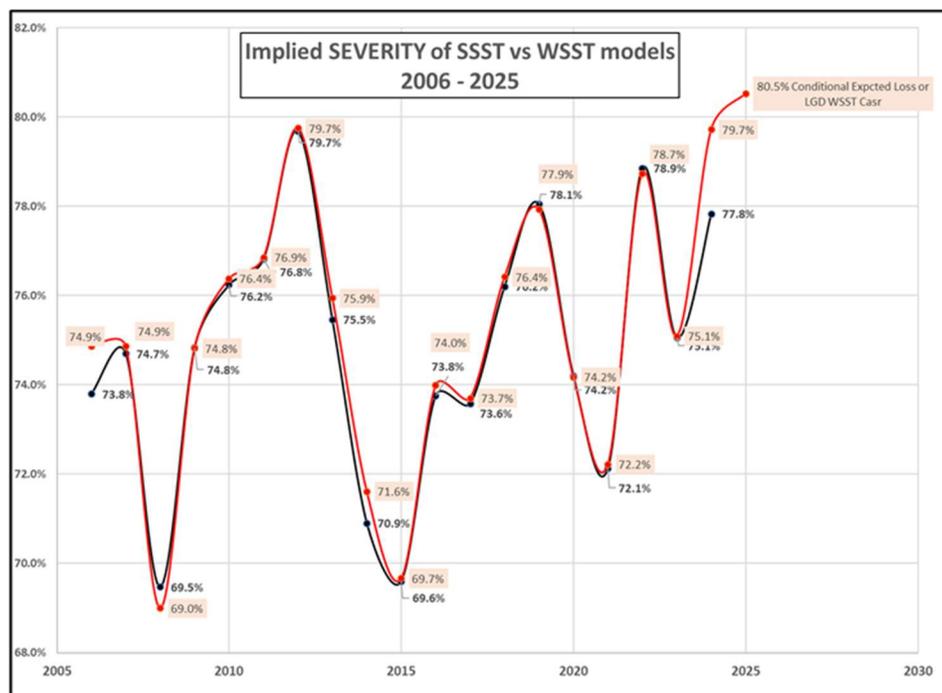
Meanwhile, back in ILS land, some providers of price indication sheets have decided to return to providing a single EL and appear to have chosen the WSST case rather than the pre-2006 SSST case². It is unlikely that it is to recognize the new plateau idea. It is more likely that it is for efficiency of reporting. The modelers still produce the results for both cases - warm and standard - but one has to have access to the OC or the models themselves to find both sets of statistics. If one has that access it is interesting to view how those models have shifted over the years.

We illustrate the pattern by comparing the components of EL.

Recall that, $EL = PFL * CEL$

Or more generally, Expected Loss = Frequency * Severity.

Severity is the expected loss, conditional on their being some loss (CEL). Frequency is the probability of some loss, even if it is a tiny or a large loss.



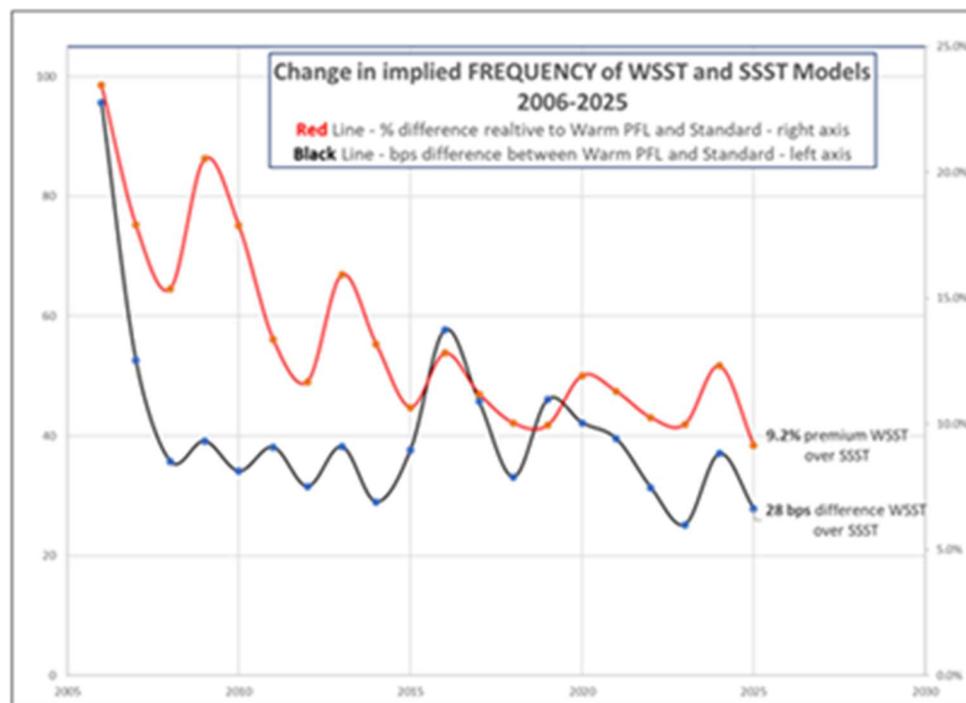
So, what was the difference between the WSST and the SSST models of severity during the last twenty years? Answer – none. See Fig,5.

Using our annual summaries of issues (forthcoming) we plot the lines for the CEL of each year's issue. There is no significant difference in the two lines. While severity of the collective issuance each year may

² The EL shown is not always footnoted to say which single EL is chosen, nor, if it is the original EL or a reset EL.

have differed from one year to the next, the severity (CEL) each year was almost identical whether derived from the standard or warm case. The only years where there is a difference is 2006 when half the issues had only a single EL and 2024 when the two EL practice was discontinued.

Looking to frequency, what is the difference between the number of landfalling storms expected to make US landfall in the warm versus the standard phase? There are two ways to measure the increase. It can be measured as the difference between the two PFLs in basis points. Or, that difference can be expressed as a % increase over the standard, lower, EL. Both are shown in Fig. 6.



Clearly here there is a difference. But, notwithstanding, both point in the same direction. In 2006, 96 bps were added to the standard PFL measure, or an increase of almost 25% to the standard PFL. There was clearly worry that the warm sea surface temperature would produce a lot more storms, albeit with the same severity of

impact. If the standard underlying belief was that 2 hurricanes a year would make landfall in the US (close to the statistical average) the concern expressed was that there would be 5 storms every 2 years, rather than the standard 4.

By 2025 that initial fear had been tempered. Now, the probability difference was set at 28 bps, or a 9.2% increase in premium. To be sure -- there had been a steady increase in the underlying EL assumed in the ILS market. But the difference in PFL meant that that extra landfalling storm would arrive once every five years instead of every other year. We have become comfortable with the warm water phase in the North Atlantic. That, it appears, is why we have returned to single EL reporting in the price indication sheets.