



Macroeconomic Impact on Reinsurance

Presentation to the Casualty Actuarial Society

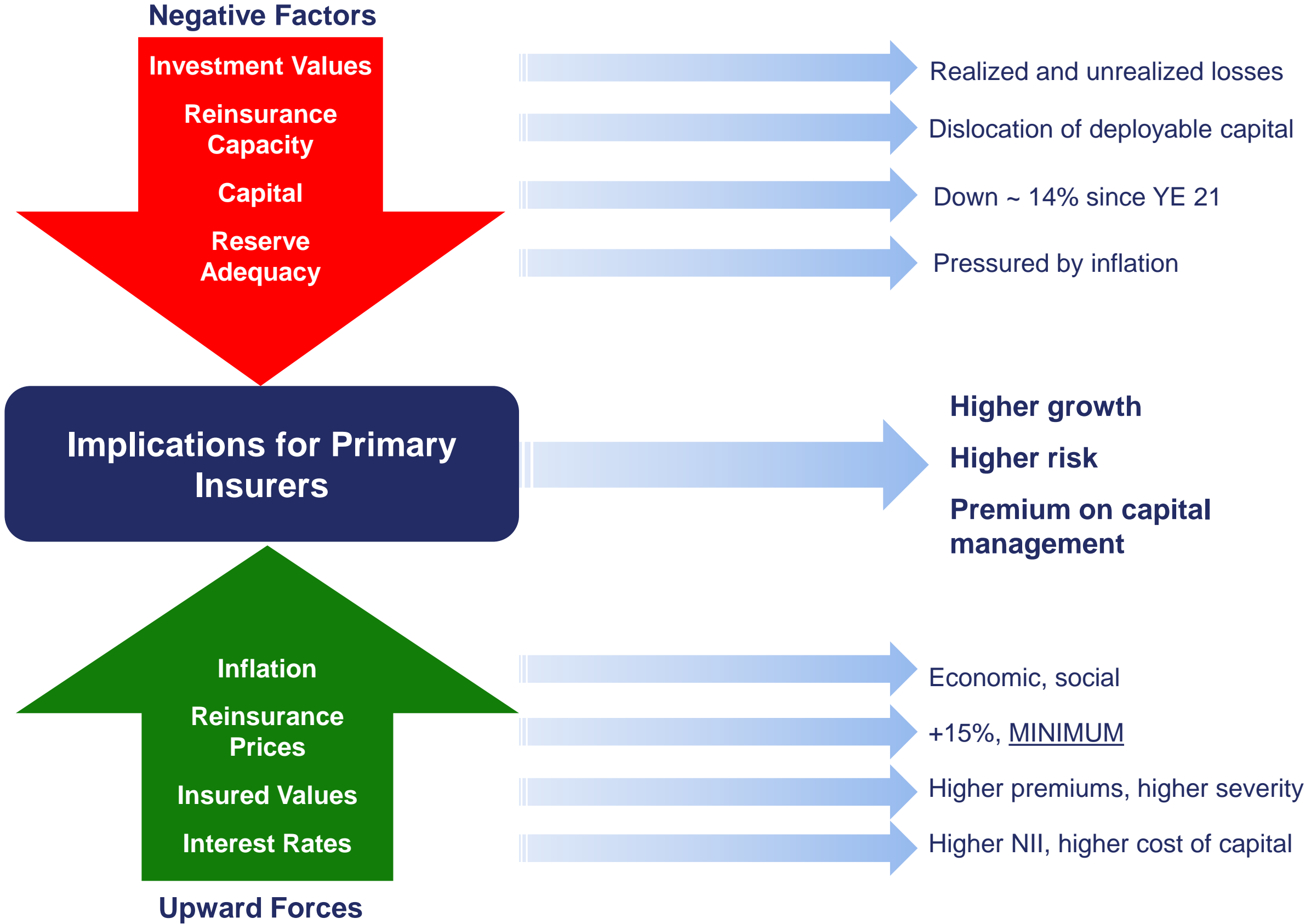
June 2023

Agenda

1. **New Market Realities!**
2. **First It Was Inflation**
3. **Reinsurance Market Reset**
4. **What Happened to the Capital Account?**
5. **Implications for Primary Insurers**

NEW MARKET REALITIES

Insurers Are Adapting to a New World!

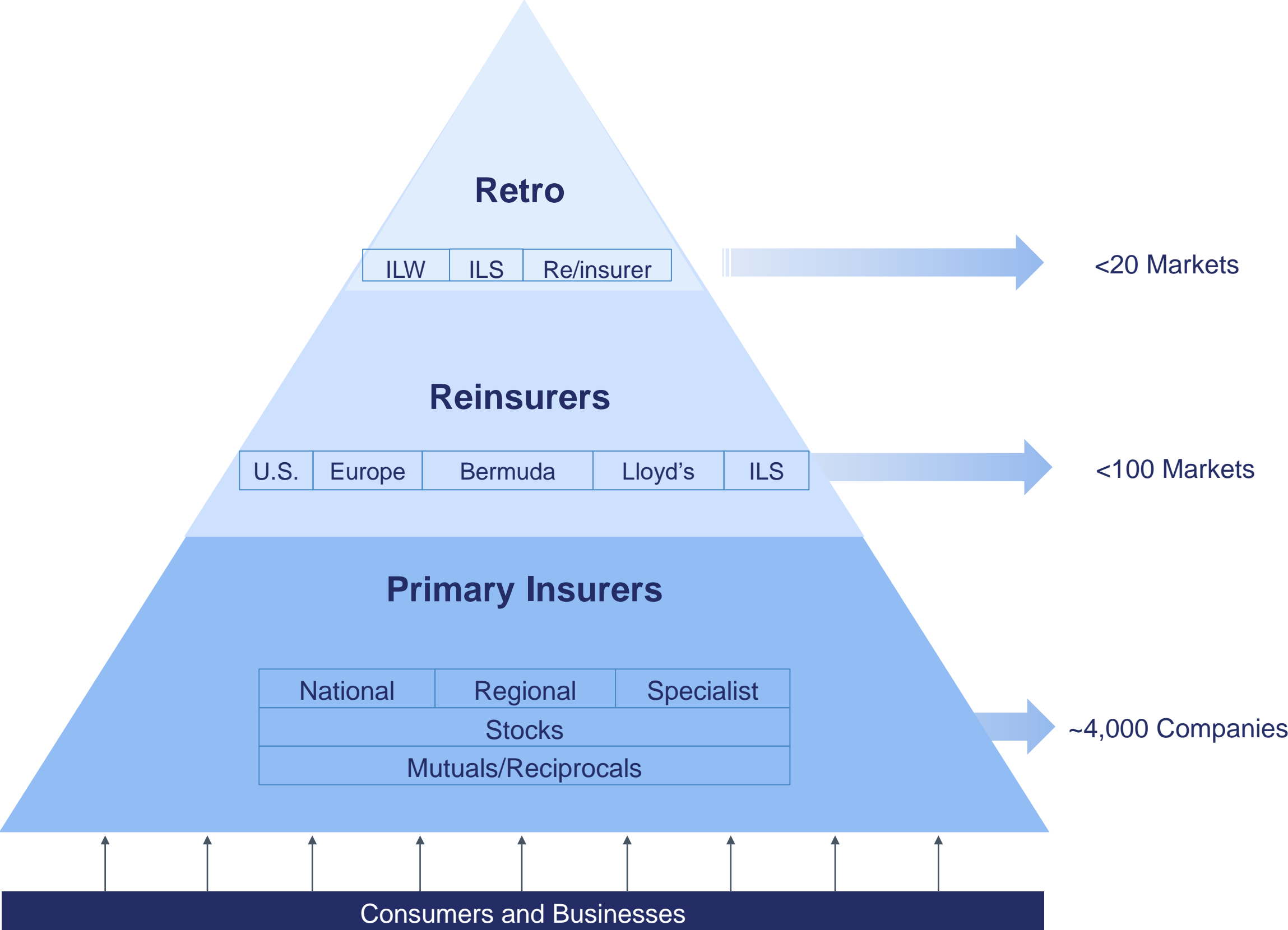


Risk Transfer Challenged with Capacity Constraints

Functioning Market



Dislocated Market



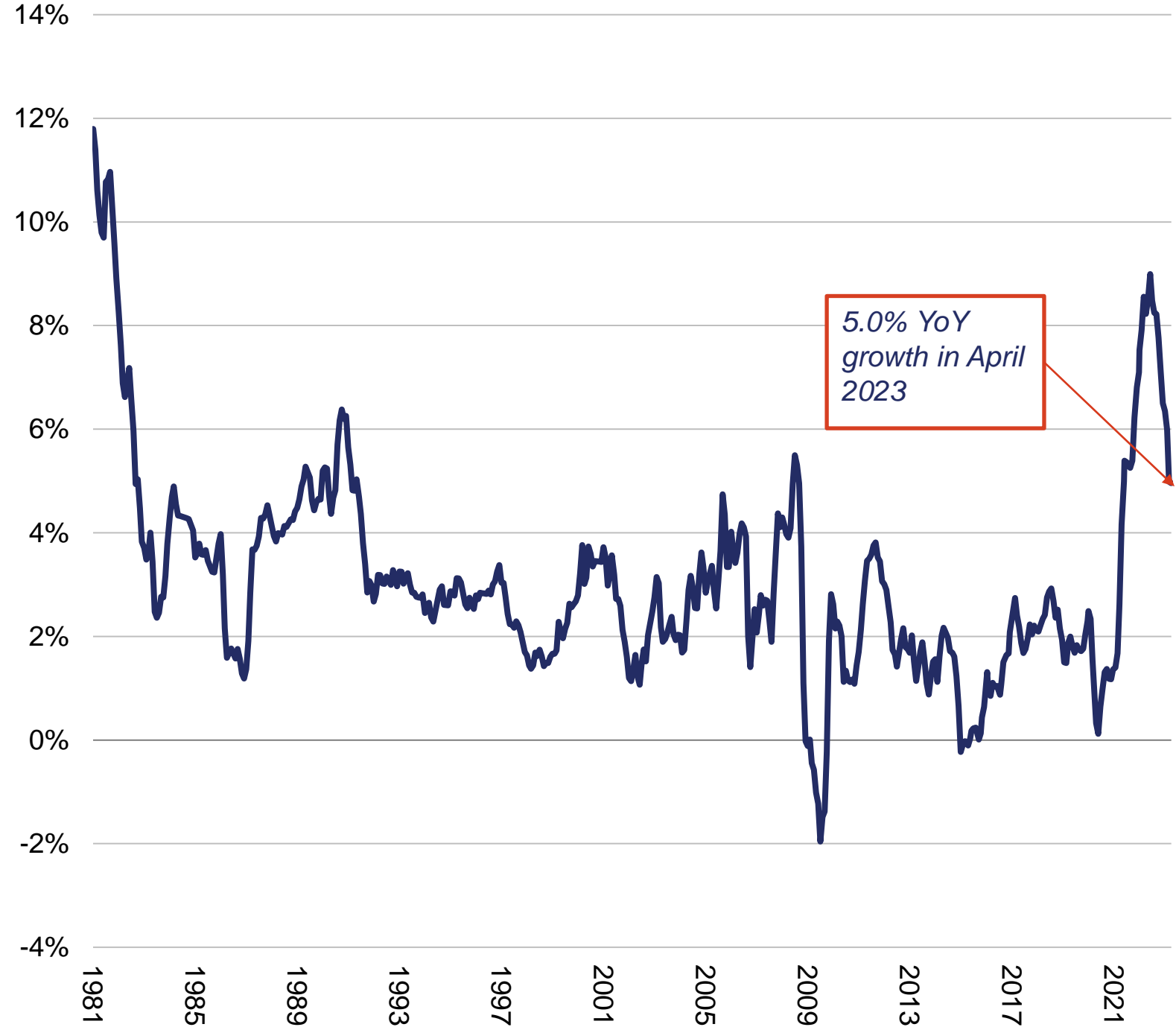
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FIRST IT WAS INFLATION

Inflation May Have Peaked, But Far from 2-3% Target!

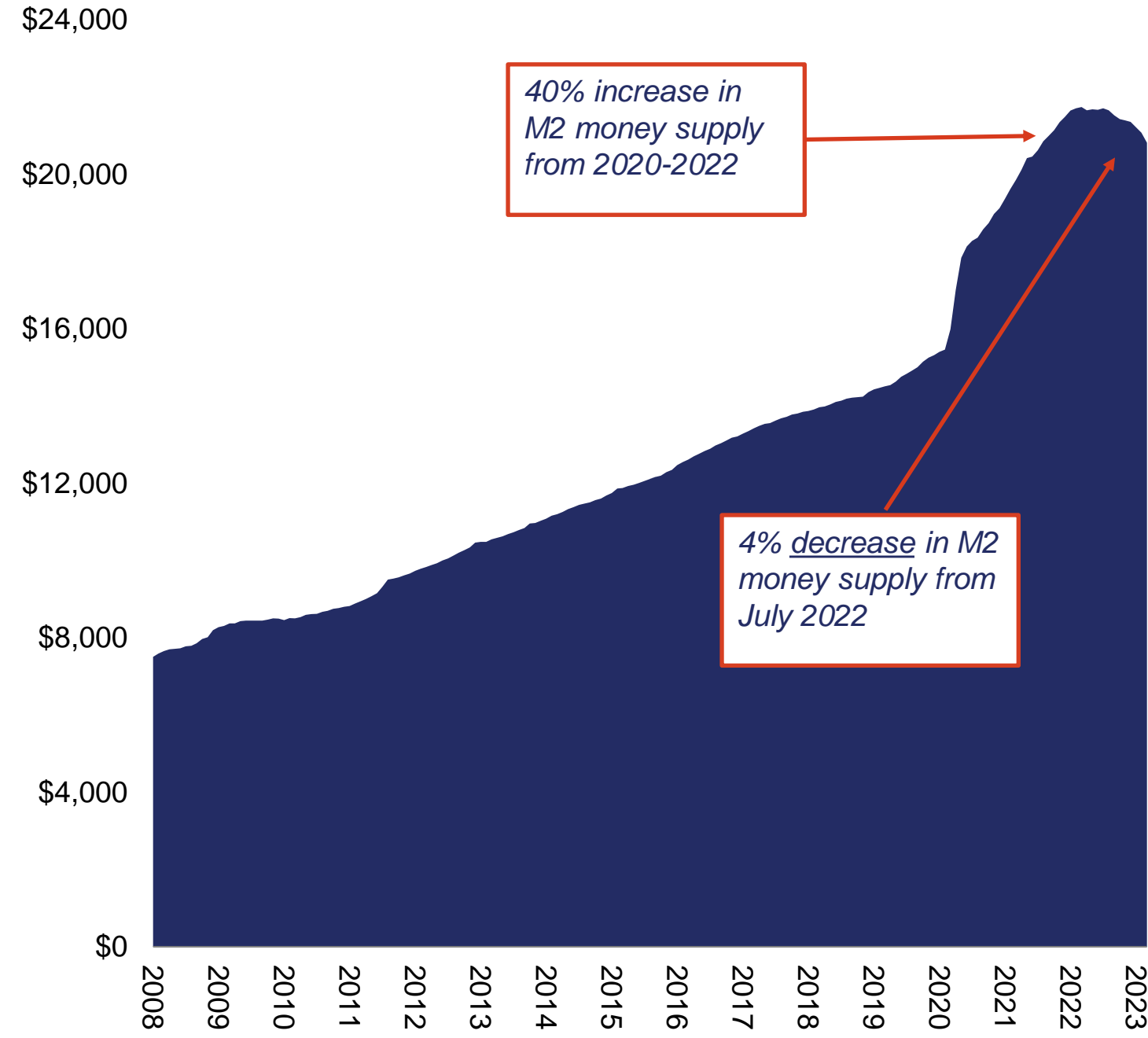
CPI All Items

Year-over-year % change



M2 Money Supply

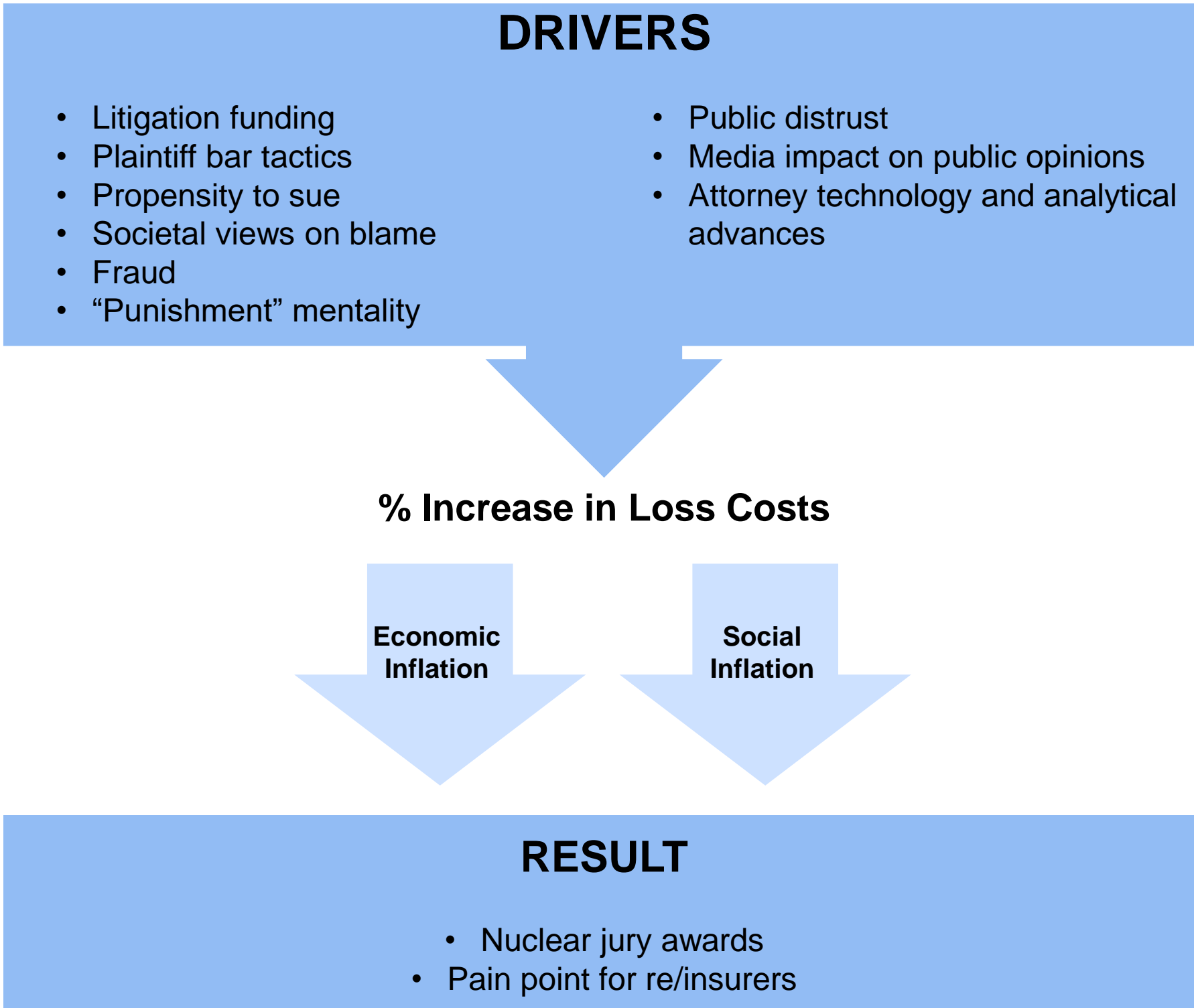
\$ in billions



Prepared by Conning, Inc. Left source: Bureau of Labor Statistics, U.S. Department of Labor (2023). Right source: Board of Governors of the Federal Reserve System federalreserve.gov, M2 Money Supply (2022)

Social Inflation—In the Headlines and Not Going Away

Social Inflation: The increase in loss costs ABOVE the rate of economic inflation



Recent Comments/Headlines on Social Inflation

*“Two trucking companies hit with **\$1 billion verdict** in death of Jacksonville teenager”*

Florida Times-Union, 8/24/21

*“**Social inflation**: The ultimate pain point of US liability insurance”*

Insurance Business Magazine, 5/17/21

*““The Fallout of High-Value Verdicts - **Jury awards have gotten out of hand**. Insurers and their corporate customers need to pressure legislators to rein in **nuclear verdicts**”*

A.M. Best, November 2021

*“Florida has a **social inflation problem** that can't be solved by rate because it is ultimately impossible to know how much to charge to cover fraud.”*

RenaissanceRe, 2022Q1 Earnings Call

*“The reserve adjustments that we made in 2019, 2018, 2020 through the P&C Re and CorSo, I think reflected our view that **the social inflation** was an issue and our continued view that it's not going away, it's not getting better. **It may even be getting worse.**”*

Swiss Re, 2022Q2 Earnings Call

Inflation Is Much More Leveraged for Reinsurers

Suppose a company has a per occurrence retention of \$1.25 million:

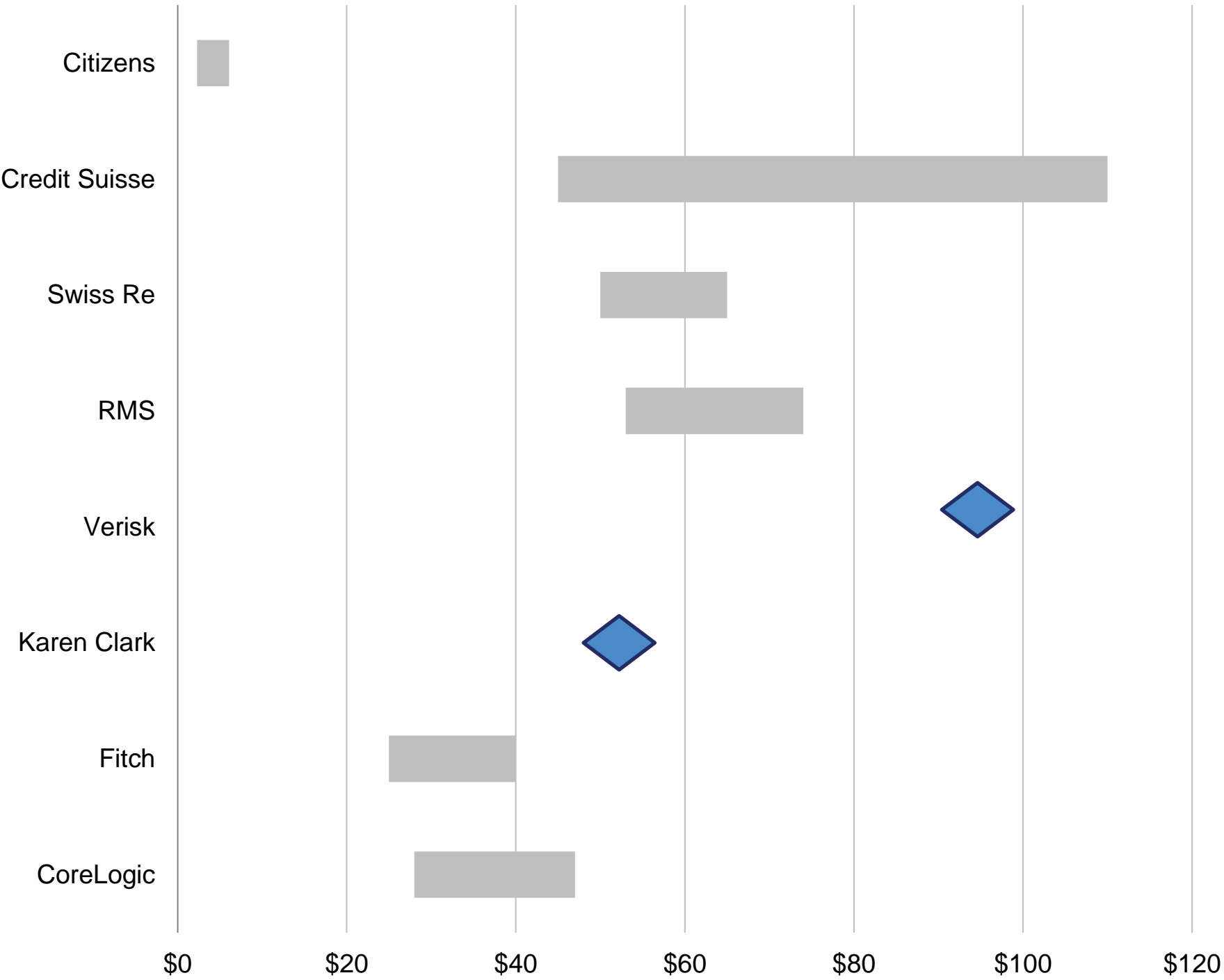
	Total Losses	Retained Losses	Reinsurers' Losses
Sample Claim	\$1,500,000	\$1,250,000	\$250,000
3% Trend	1,545,000	1,250,000	295,000
Change (\$)	45,000	0	45,000
Change (%)	3.0%	0.0%	18.0%

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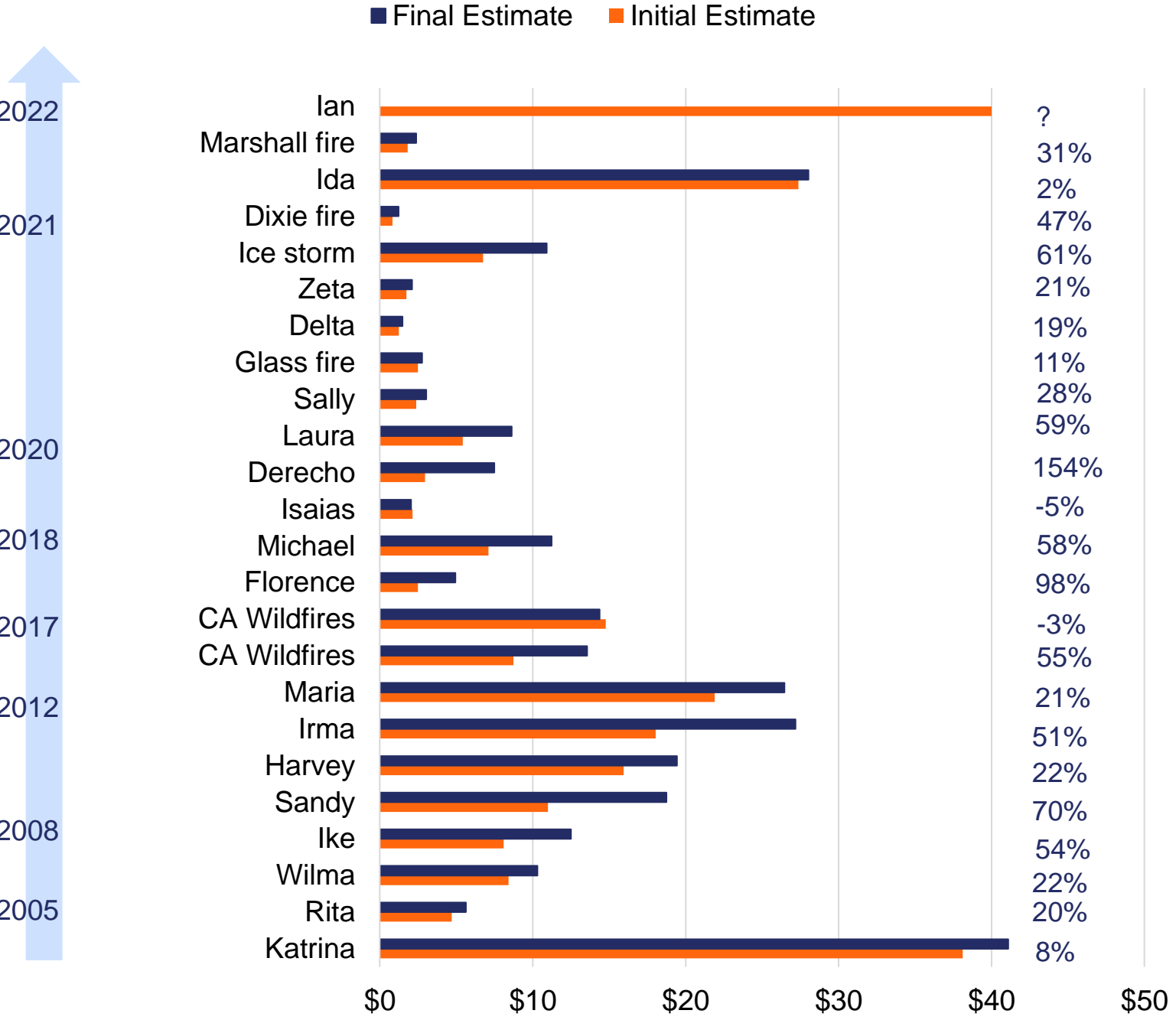
REINSURANCE MARKET RESET

Hurricane Ian—The Last Straw

Insured Loss Estimates for Hurricane Ian \$ in billions



Catastrophe Loss Creep = Aggregate 29% \$ in billions

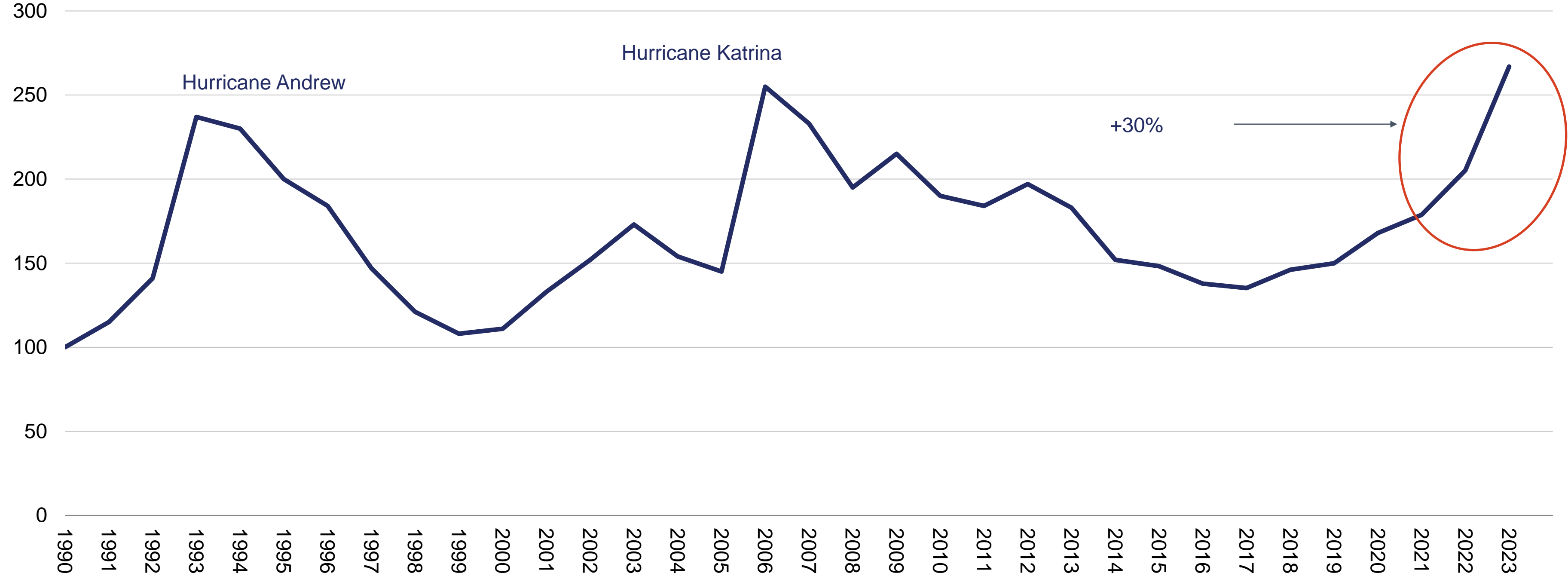


(Left) Prepared by Conning, Inc. Source: company press releases, public filings, and news articles

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Property Cat Rates Soar at 1.1.2023 Renewals

U.S. Property Catastrophe Reinsurance Rate-on-Line Index

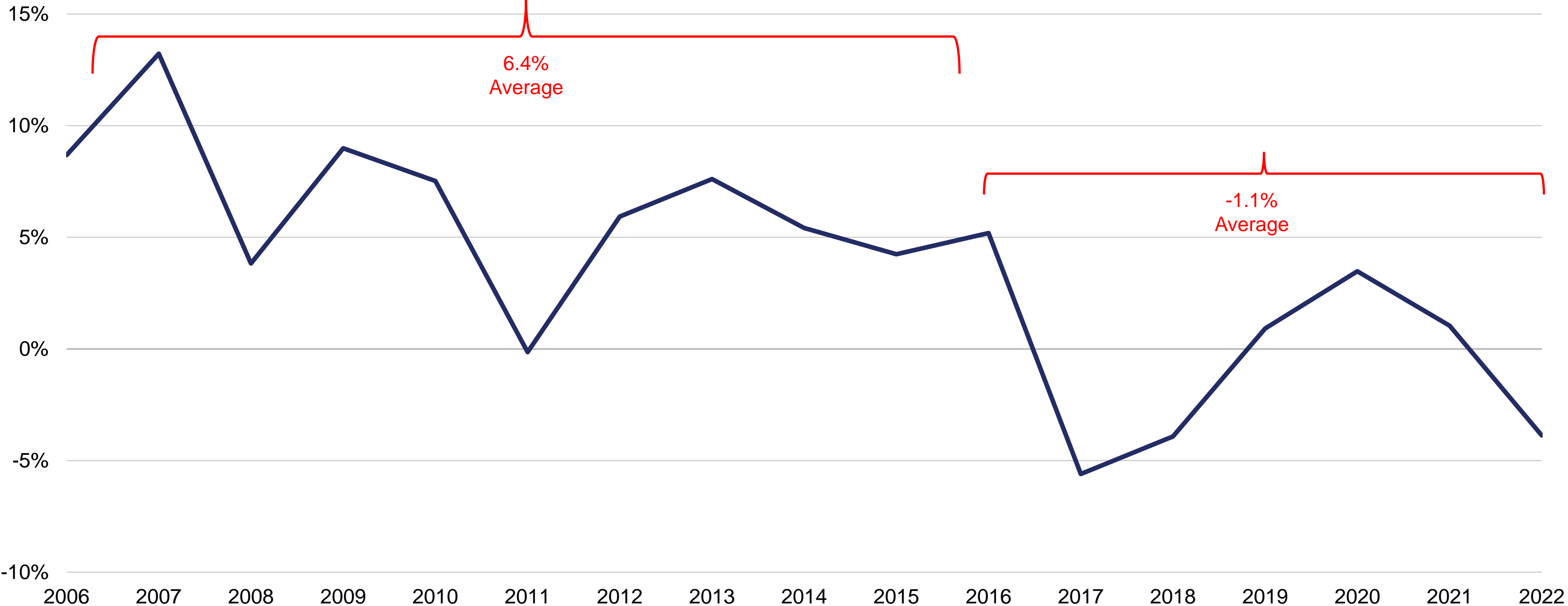


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“The Guy Carpenter ROL Index (“Index”) is a measure of the change in dollars paid for coverage year-on-year on a consistent program base. The Index reflects the pricing impact of a growing (or shrinking) exposure base, evolving methods of measuring risk and changes in buying habits, as well as changes in market conditions. The Index provides context for evaluating actual movement in dollars flowing into the system to measure changing views of risk, exposures and other factors. Guy Carpenter & Company, LLC provides the Index only as general information. Specifically, we do not guarantee its accuracy, and it should be understood to be general insurance/reinsurance information. Guy Carpenter & Company, LLC makes no representations or warranties, express or implied or otherwise.”

Recent ILS Performance Leaves Investors on the Sidelines

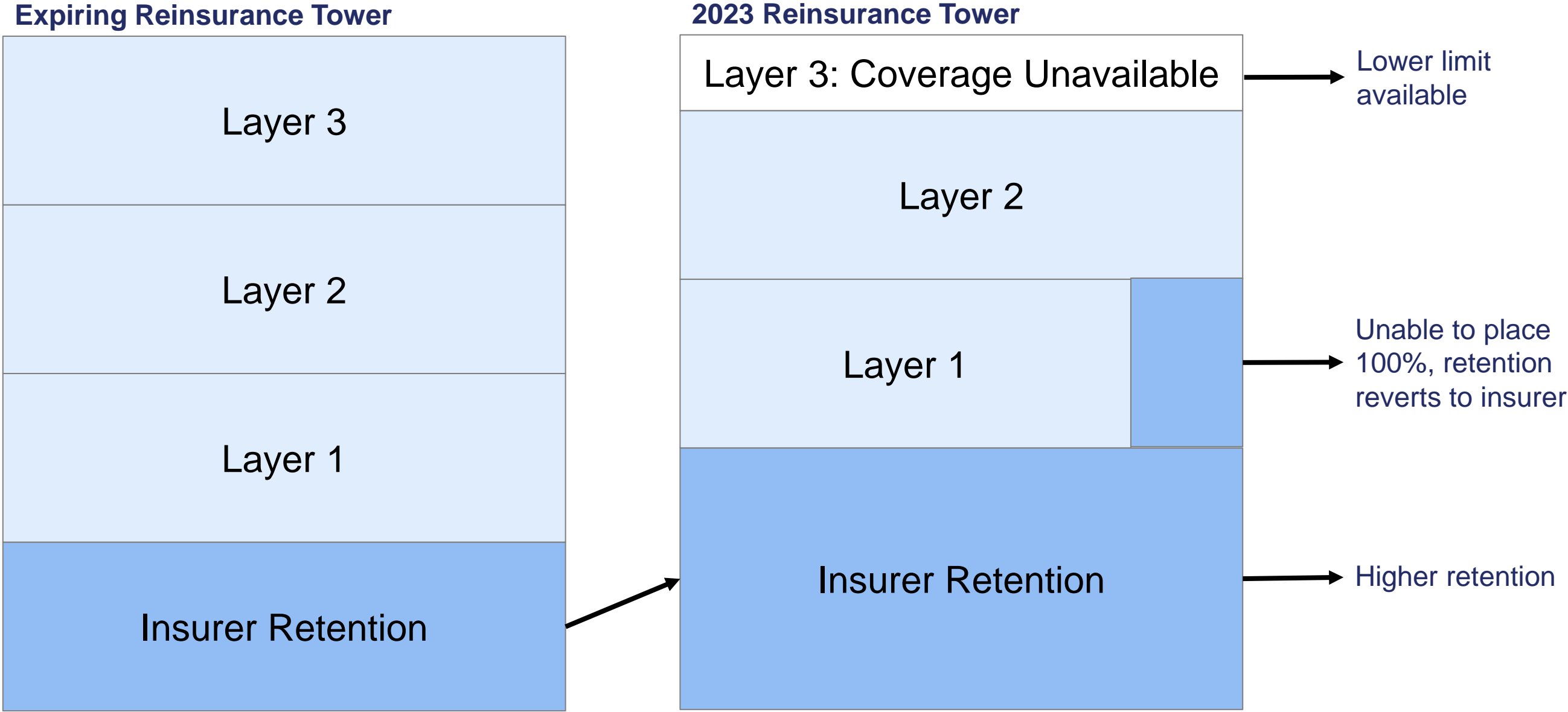
Annual Insurance-Linked Securities Returns



Prepared by Conning, Inc. Source: Artemis <https://www.artemis.bm/eurekaledge-ils-advisers-insurance-linked-securities-fund-index/>—used by permission

Reinsurance Reset: Higher Retentions, Lower Limits, Coverage Gaps

Reinsurance Illustration



WHAT HAPPENED TO THE CAPITAL ACCOUNT?

Fed Rate Hikes to Combat Inflation: Decline in Bond Values

U.S. 10-Year Treasury Yield



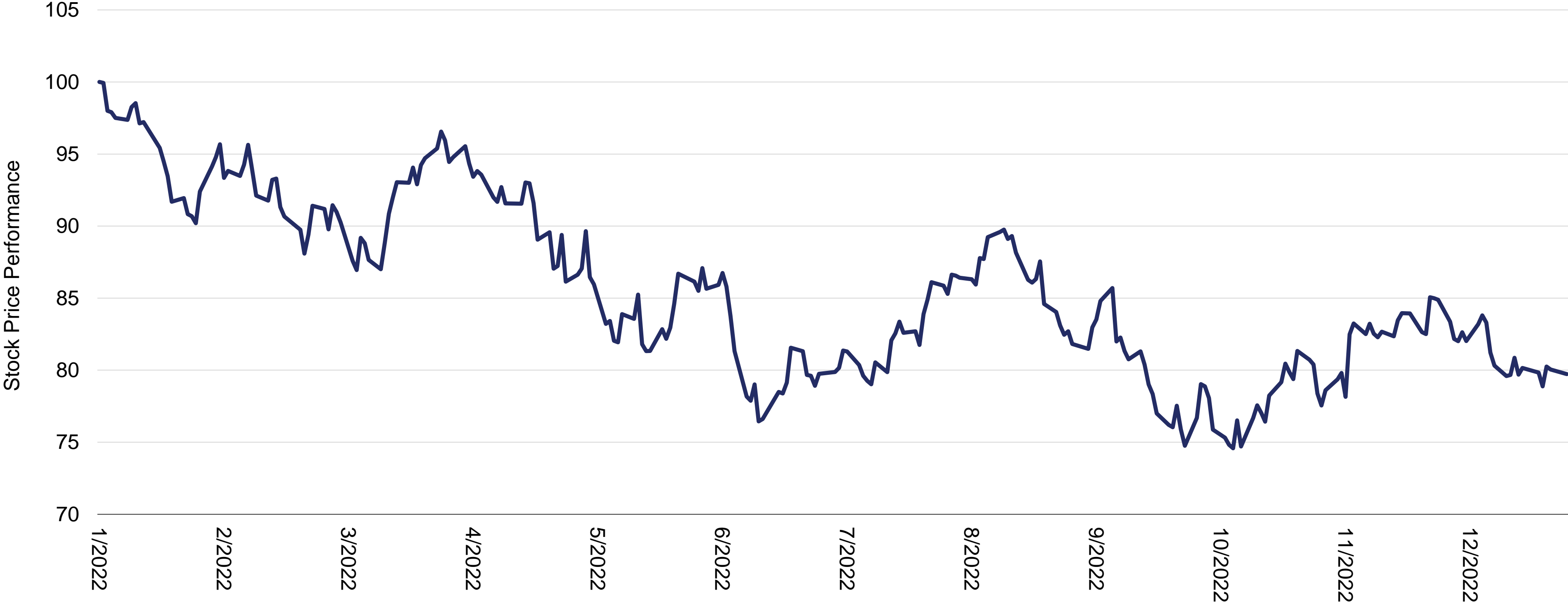
FOMC = Federal Open Market Committee of the Federal Reserve

Prepared by Conning, Inc. Sources: U.S. Department of the Treasury (2023) and Federal Reserve Bank of Philadelphia, Survey of Professional Forecasters <https://www.philadelphiafed.org/surveys-and-data/real-time-data-research/survey-of-professional-forecasters> (2023)



Realized and Unrealized Equity Market Losses

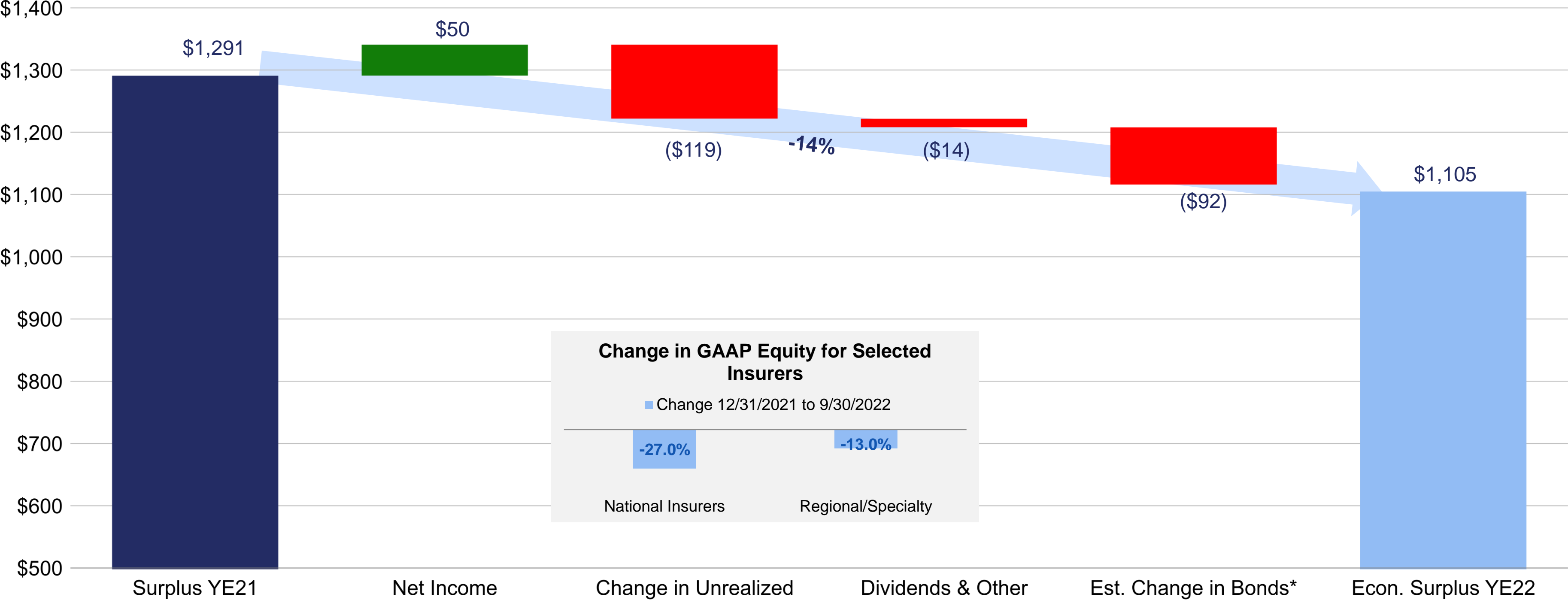
Insurance Stock Indices Compared to S&P 500 January 3, 2022, to January 3, 2023



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Significant Decline in “Economic” Surplus in 2022

Change in Economic Capital
\$ in billions

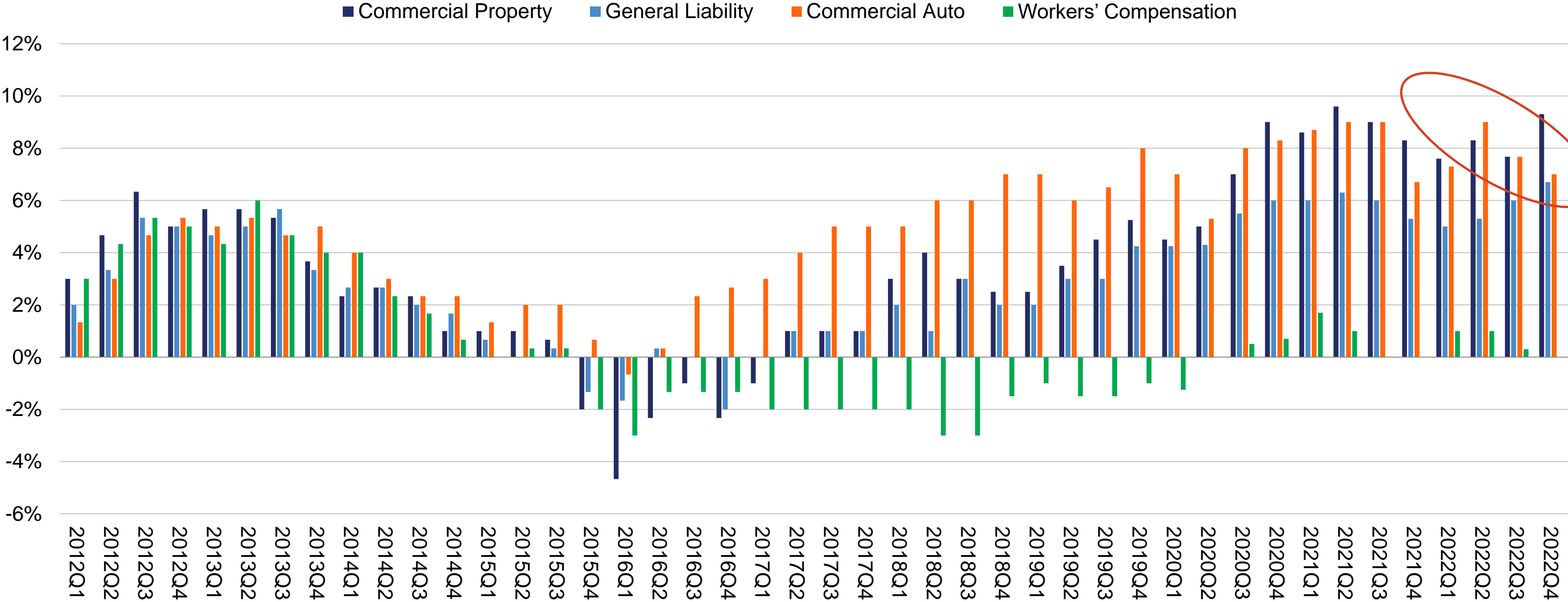


Note: Estimated change in bonds = 10% decline since year-end, tax-effected.
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IMPLICATIONS FOR PRIMARY INSURERS

Rates Will Remain Firm Despite Recent Flattening

Average Renewal Pricing, Commercial Lines

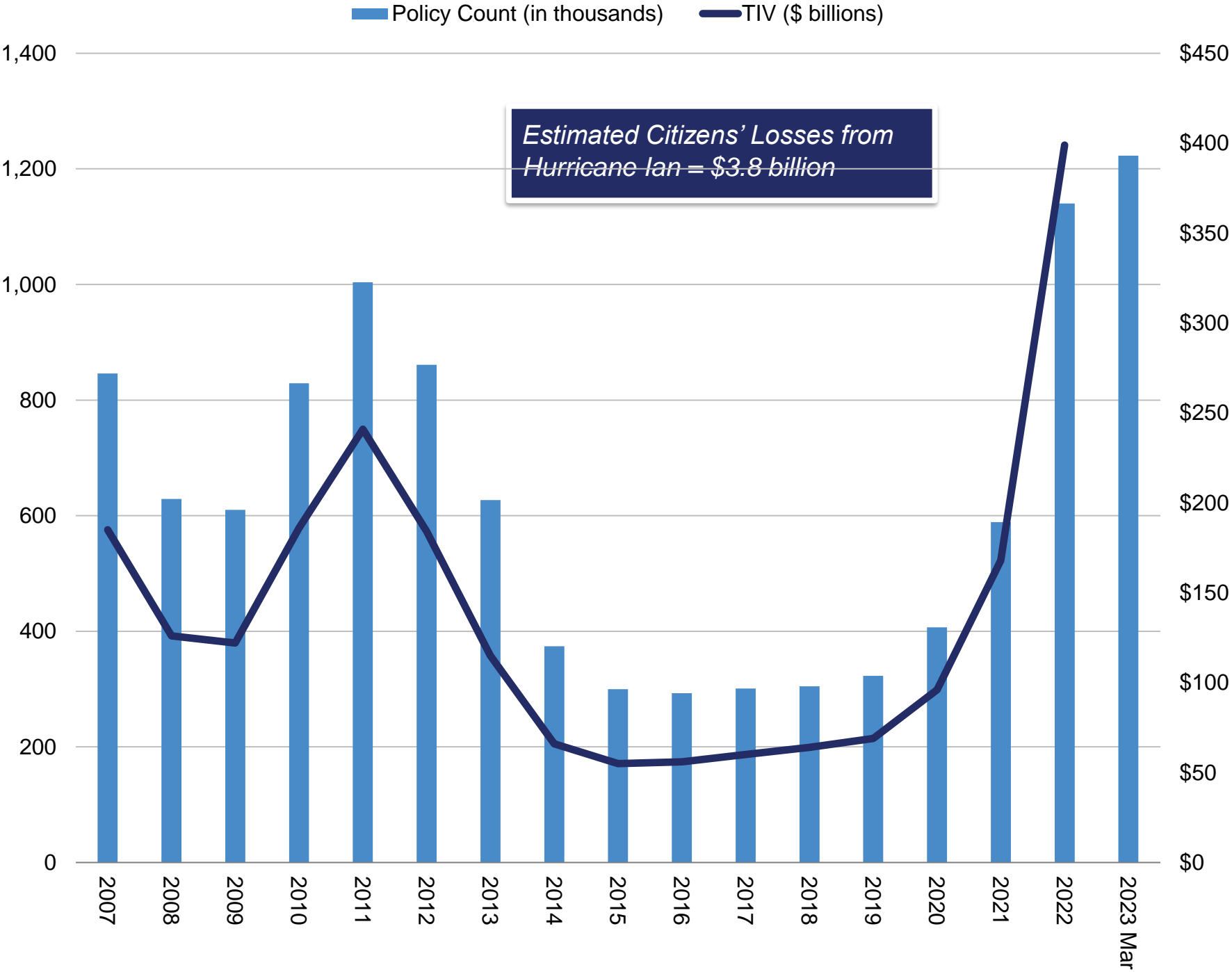


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Leakage from Private Market in FL and from Admitted Market in CA

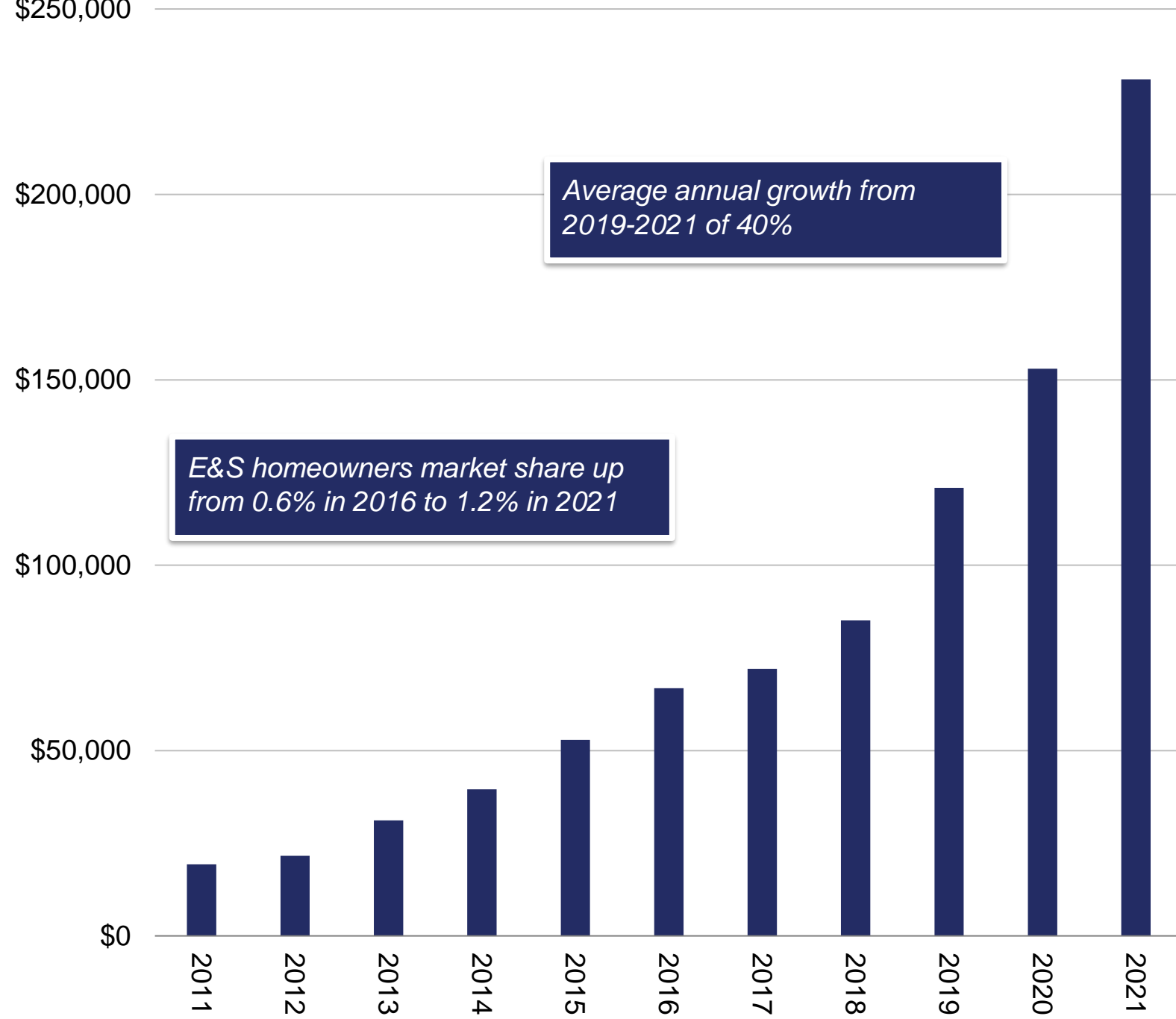
Citizens Property Policy Count and TIV Trends

Data as of March 31, 2023



California Homeowners E&S Premium

\$ in thousands

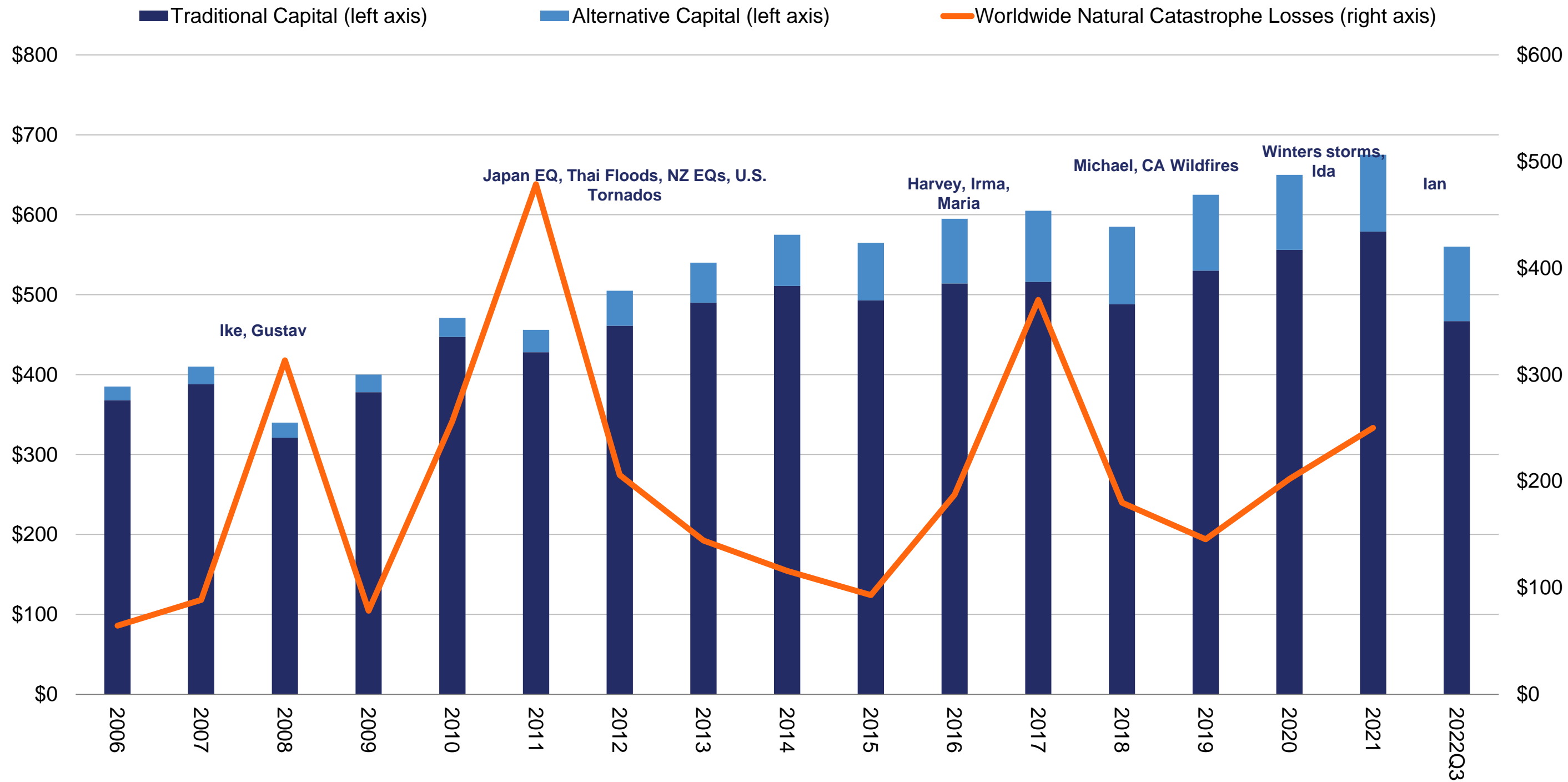


Prepared by Conning, Inc. Sources: Citizens Property Insurance Corporation of Florida <https://www.citizensfla.com> and Copyright 2023 S&P Global Market Intelligence LLC



Capital Entered in Prior Dislocations—What About 2023?

\$ in billions



Reinsurer Formations

Pre-2006: RNR, PRE, AWAC, AXS, Arch, AHL, ENH, VR, TPRE, FGS, LRE, MRH, Platinum, Tempest, Cat Ltd., Mid-Ocean, LaSalle, Global Capital Re, IPC Re, Ariel Re

2006-2017: None

2018-2022: Vermeer, Geneva Re, Conduit, Convex, Vantage

2023: ??

Prepared by Conning, Inc. Sources: Aon Reinsurance Analytics, Aon Securities Inc. and Swiss Re Institute, sigma 4/2021

Why No New Capital or Reinsurer Formations?

Ten Factors Limiting New Capital (Isn't Now the Best Market in a Generation?)

1	Difficult to Raise Capital	Cost of capital increased, availability decreased
2	Return Profile	Do investors want enormous volatility for just average returns?
3	Lack of Franchise Value	Can a new entity be valued at > book value?
4	Hard Markets Too Short	Short-lived hard markets with new capital and competition driving rates down
5	New vs. Existing	More attractive to invest in existing companies and sidecar vehicles
6	Recent Track Record	Investors stung by above-average losses in 5 of last 6 years
7	Rise of Secondary Perils	Diversifying perils become peak exposures
8	Inflation and Loss Creep	Accelerating severity with both economic and social inflation
9	Model Reliability	Too much reliance on models with inherent limitations
10	Management Expertise	Is there sufficient pool of bankable management talent?

Polling Question

You can only choose one!

- A. Over the next 3-5 years the insurance markets will adapt and become less dependent on reinsurance and related capital market instruments.
- B. The next 3-5 years will see a (near) continuation of current conditions and represent a golden-era for reinsurers.

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