

# Making the Right Choice: An Arranger's Perspective

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Capital Markets & Advisory

# INTRODUCTION

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- **In this presentation, we will address the key motivations for sponsors**
  - a/ to do an ILS issuance
  - b/ in their selection of the jurisdiction of the SPRV
  
- **We have focussed on cat bonds, as these are the most visible transactions but our comments will apply equally to sidecar and collateralized reinsurance using transformers**
  
- **The key message is that:**
  - We anticipate a slow yet regular growth in the ILS markets in Europe in the years to come
  - There is a need for a flexible, yet secured jurisdiction in Europe today

# KEY MOTIVATIONS TO A CAT BOND ISSUANCE

## Catastrophe Bond Basics

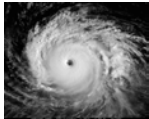
- Catastrophe bonds offer multi-year reinsurance capacity for fixed income investors
  - Banks, hedge funds, specialist funds
- Sponsors (issuers) are typically insurers and reinsurers
  - But several corporate or government entities have also participated



## Catastrophe Bond Benefits

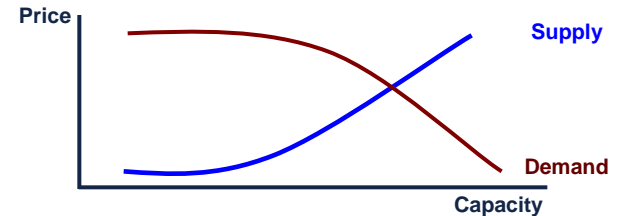
### Expedited Recoveries

- Mechanistic recoveries possible with non-indemnity triggers



### Diversification of Capacity

- Can have lower marginal cost in an absolute sense



### Full Collateralization

- Hedge of systemic credit risk inherent in (re)insurance markets



### Full Syndication

- Pay less with broadest investor group



### Multi-year Reinsurance Protection

- Ability to lock-in terms typically between 3 – 5 years



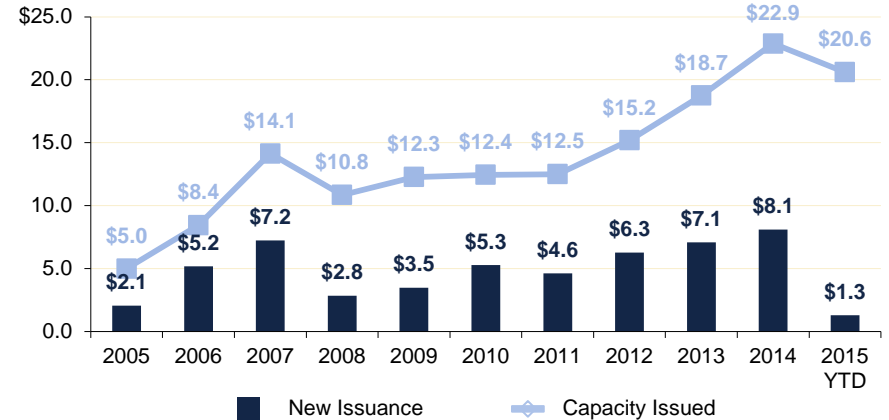
# STATE OF THE CAT BOND MARKET

*2014 set the record for cat bond issuance*

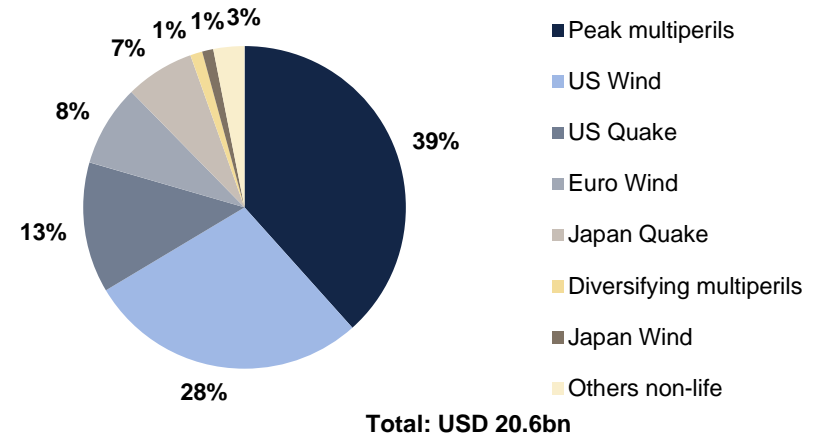
## Non-Life Cat Bond Market Update

- **6 non-life cat bonds issued since the beginning of the year**
  - For a total capacity of \$1.3bn
  - 3 other bonds currently in the market
  
- **Continued growth is expected in 2015**
  - Very strong Q2 anticipated with multiple issuances both in the US and internationally
  - Ready supply from continued AuM growth and reinvestment of maturities
  
- **Product is more accommodating to a wider range of sponsors**
  - Given the increased flexibility in terms and conditions
  - Declining spreads expand the economically viable perils
  
- **Sponsors locking in low ROLs for multi-year period**
  
- **In addition some investors and sponsors are treating sidecars more like cat bonds as the products begin to converge**

## Non-Life Cat Bond Issuance / Outstanding Volume



## Total Non-Life Capacity Outstanding by Peril



# MORE FAVOURABLE CONDITIONS FOR SPONSORS

*In 2014 fall in spreads and attractive terms and conditions encouraged active sponsor participation*

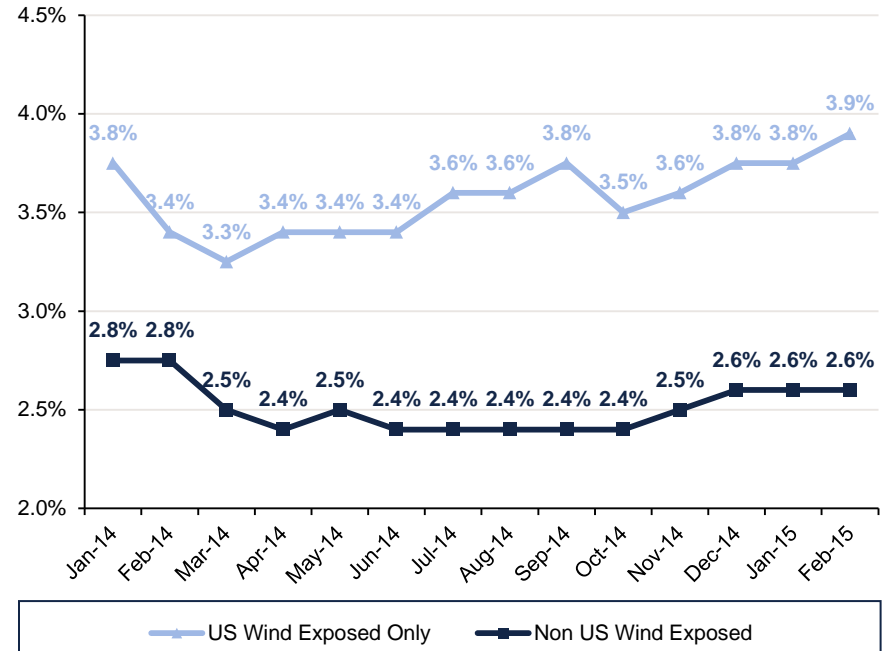
## More Favourable Terms & Conditions

- Sponsors leveraged the unique strengths of cat bond structures to improve the quality of their overall reinsurance protection
  - Broadening of the subject business with inclusion of more unmodelled perils to match more closely traditional reinsurance
  - Variable reset allowing continuity of coverage over time
  - Longer risk periods ensuring tight spread levels for the medium term
  - Selective sponsors benefit from this advantageous environment to access the market through private placements (AmTrust)
  
- A number of first time features were successfully brought to market
  - Growth factor calculation based on projections to cover fast growing companies (Citrus Re)
  - Dual aggregate/occurrence cover (Gator Re)
  - JPY-denomination (Aozora Re)
  - Indemnity European Windstorm primary book (Lion I Re)

## Attractive Pricing Environment

- Spreads remain stable at record low levels for all classes of risk
  - For certain regions and risk levels, pricing stayed inside of traditional reinsurance
  - We do not anticipate material spread changes in the near term

### Evolution of spreads at 1.0% Expected Loss is shown below:



# OUTSTANDING EUROPEAN CAT BONDS

■ 30 cat bonds currently outstanding the market sponsored by European (re)insurers

■ USD 5.1bn currently outstanding sponsored by European (re)insurers

(in millions)

Sponsor	Issuer / Tranche	Date		Amount	Expected Loss	Risk Spread	Trigger	Risk
		Issue	Maturity					
SCOR	Atlas IX Capital Limited 2015-1	02/09/15	01/07/19	\$150	7.00%	3.76%	PCS	US Wind & Quake, CAN EQ
Catlin	Galileo Re Ltd. 2015-1	02/01/15	01/08/18	\$300	13.50%	8.60%	PCS / PERILS	US EQ & Wind, CAN EQ, EU Windstorm
Amlin	Tramline Re II Ltd. 2014-1	12/22/14	01/01/19	\$200	9.75%	5.71%	PCS	Named Storm, US EQ & Euro Wind
Generali	Lion I Re Ltd.	04/24/14	04/28/17	€190	2.25%	1.00%	Indemnity	Euro Wind
Munich Re	Queen Street IX Ltd 2014-1	02/26/14	06/08/17	\$100	5.50%	2.92%	Index	US Wind & Australia Cyclone
Catlin	Galileo Re Ltd. 2013-1	10/30/13	01/09/17	\$300	7.40%	2.59%	PCS / PERILS	US EQ, US Wind, CAN EQ, EU Windstorm
AXA	Calypso Capital II Ltd. 2013-1	10/15/13	01/08/18	€165	2.90%	1.18%	PERILS	Euro Wind
AXA	Calypso Capital II Ltd. 2013-1	10/15/13	01/09/17	€185	2.60%	0.96%	PERILS	Euro Wind
SCOR	Atlas IX Capital Limited 2013-1	09/11/13	01/17/19	\$180	3.25%	0.92%	CDC Mortality Index	US Extreme Mortality
Swiss Re	Mythen Re Ltd. 2013-1	07/02/13	07/09/15	\$100	8.00%	3.01%	PCS	US Wind
Groupama	Green Fields II Capital Ltd. 2013-1	07/01/13	01/09/17	€280	2.75%	0.85%	PERILS	France Windstorm
Amlin	Tramline Re II Ltd. 2013-1	06/27/13	07/07/17	\$75	3.25%	1.21%	PCS	US & Canada Quake
Munich Re	Queen Street VIII Re Ltd.	06/26/13	06/08/16	\$75	6.50%	2.92%	Multiple Non-Indemnity	US Wind & Australia Cyclone
Allianz	Blue Danube II Ltd. 2013-1	05/22/13	05/23/16	\$175	4.25%	0.96%	Multiple Non-Indemnity	US, Mexico & Caribbean Wind, US Quake
TCIP	Bosphorus 1 Re Ltd.	04/25/13	05/03/16	\$400	2.50%	0.99%	Parametric Index	Turkey Quake
Zurich American	Lakeside Re III Ltd.	12/28/12	01/08/16	\$270	8.00%	2.09%	Indemnity	US & Canada Quake
Swiss Re	Mythen Re Ltd. 2012-2	11/05/12	01/05/17	\$120	8.50%	2.20%	PCS	US Wind & UK Mortality
SCOR	Atlas Re VII Limited	11/01/12	01/07/16	\$60	8.00%	1.86%	PCS / PERILS	US Wind & Quake

# OUTSTANDING EUROPEAN CAT BONDS (Cont'd)

(in millions)

Sponsor	Issuer / Tranche	Date		Amount	Expected Loss	Risk Spread	Trigger	Risk
		Issue	Maturity					
Swiss Re	Mythen Re Ltd. 2012-2	11/05/12	11/10/16	\$80	11.75%	4.28%	PCS	US Wind
SCOR	Atlas Re VII Limited	11/01/12	01/07/16	€130	3.65%	1.50%	PCS / PERILS	Euro Wind
Munich Re	Queen Street Re VII Ltd.	10/31/12	04/08/16	\$75	8.60%	2.71%	PERILS	US & Euro Wind
Hannover Re	Eurus III Ltd.	09/13/12	04/07/16	€100	3.75%	1.59%	PCS / PERILS	Euro Wind
Munich Re	Queen Street VI Re Ltd.	07/17/12	04/09/15	\$100	10.35%	2.90%	PCS / PERILS	US Wind & Euro Wind
Swiss Re	Mythen Ltd. 2012-1	05/03/12	05/07/15	\$250	11.00%	2.44%	PCS / PERILS	US Wind & Euro Wind
Swiss Re	Mythen Ltd. 2012-1	05/03/12	05/07/15	\$50	8.50%	1.23%	PCS	US Wind
Swiss Re	Mythen Ltd. 2012-1	05/03/12	05/07/15	\$100	8.00%	0.99%	PCS	US Wind
Allianz	Blue Danube Ltd. 2012-1	04/03/12	04/10/15	\$120	6.00%	0.59%	PCS	US Wind & Quake
Allianz	Blue Danube Ltd. 2012-1	04/03/12	04/10/15	\$120	10.75%	1.77%	PCS	US Wind & Quake
Munich Re	Queen Street V Re Ltd.	02/27/12	04/09/15	\$75	8.50%	1.95%	PCS / PERILS	US Wind & Euro Wind
SCOR	Atlas VI Capital Ltd. 2011-2	12/12/11	04/09/15	€50	8.00%	3.30%	PERILS	Euro Wind
Swiss Re	Successor X Ltd. 2011-3	11/08/11	11/10/15	\$50	11.25%	3.76%	PCS / PERILS	US Wind & Euro Wind
Swiss Re	Successor X Ltd. 2011-3	11/08/11	11/10/15	\$80	16.25%	6.70%	PCS	US Wind
Munich Re	Queen Street IV Capital Ltd.	10/27/11	04/09/15	\$100	7.50%	1.94%	PCS / PERILS	US Wind & Euro Wind
ERDF	Pylon II Capital Ltd.	08/11/11	05/05/16	€65	5.50%	2.49%	Parametric Index	France Windstorm
ERDF	Pylon II Capital Ltd.	08/11/11	05/05/16	€85	9.00%	4.69%	Parametric Index	France Windstorm
Swiss Re	Kortis Capital Ltd.	12/22/10	01/15/17	\$50	5.00%	0.55%	Parametric Index	Longevity Divergence

# REGULATORY TREATMENT

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*If structured properly, a cat bond can give regulatory credit*

- **The recognition of a cat bond will be similar to that of a traditional reinsurance protection: the sponsor's cat exposure will be lowered by the nominal amount of the cat bond and the charge for catastrophic events will be reduced**
  
- **To qualify for treatment as a reinsurance contract under Solvency II, a cat bond needs to be:**
  - Issued by a vehicle in a Solvency II approved jurisdiction
  - Approved by the regulator in that jurisdiction, approval which will be granted if certain conditions are met, such as:
    - The SPV needs to be fully funded at all times
    - Claims from investors need to be subordinated to the claims of the sponsor under the reinsurance agreement
    - There needs to be an effective risk transfer for the sponsor
  
- **Depending on the internal model of the sponsor, there could be a potential reduction in the capital credit:**
  - If there is significant basis risk – in the case of a parametric cat bond
  - If the sponsor already receives significant credit from the diversification module
  
- **Under Solvency II, a cat bond will not generate an additional credit risk charge (contrary to unfunded traditional reinsurance) as long as the collateral is invested in certain high quality assets**

As per the EIOPA guidelines, European (re)insurance companies will need to locate their SPRVs in a Solvency 2 or Solvency 2 equivalent jurisdiction to obtain regulatory credit



# CONSIDERATIONS AROUND THE CHOICE OF THE SPRV JURISDICTION

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## Reactive and Well Connected Regulator

- **Accessible and reactive regulator**
  - In particular, a fast approval process is REALLY appreciated by clients
  - Easy access to the regulator and well defined incorporation rules are key
- **Well connected with other European regulators**
  - To facilitate regulatory approval by the local regulators of the cedant (i.e. IVASS in Italy, ACPR in France)

## Efficient And Transparent Business Environment

- **Established business environment, highly knowledgeable in the insurance space**
  - In particular, with regards to SPRV managers and local counsels
- **Stable, predictable legal environment**
  - Clarity and quickness in the court ruling
- **Bilateral tax agreement with European countries**
  - To ensure the absence of possible withholding tax
- **Proximity to Europe**
  - Same time zone, while not necessary, is helpful

# CONCLUSIONS

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- 1 There is a need for a flexible, yet secured, ILS jurisdiction in Europe
- 2 Becoming a recognized ILS jurisdiction is likely to be a long and progressive process
- 3 There may not be room for many jurisdictions to coexist but client-oriented jurisdictions should prevail
- 4 Getting momentum early will be key

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