

# LIMA Programme

## Functions and Form of Reinsurance

11 September 2023  
Nkejane Mofokeng

NOT IF, BUT HOW



01

Historical Journey

03

South African Examples

02

Solvency Capital Requirements

04

Motivations

# Historical Journey

01





- Origins in Marine
  - 4-3000BC loan contracts to insure ships
  - Further developments end of Middle Ages
  - End of 14th century insurance policies around the Mediterranean



- First REINSURANCE contract 1370
  - Cargo from Genoa to Bruges
  - Reinsured the hazardous part of the trip (Cadiz to Bruges)

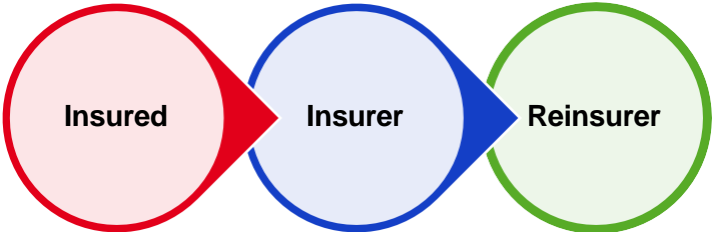


- Edward Lloyd's coffee shop (1648 – 1713)
- Guidon de la Mer (1671)
- First legal Regulations (beginning 17th century)
- First Reinsurer (founded in 1843)
- Industrial Revolution – boosting Reinsurance



Exchanging  
the uncertainty about future expenses  
(caused by claims)  
against the certainty  
of paying a premium

# The Insurance Value Chain





# Solvency Capital Requirements

02



# Basic Solvency Capital Requirements

## Solvency Capital

### Premium

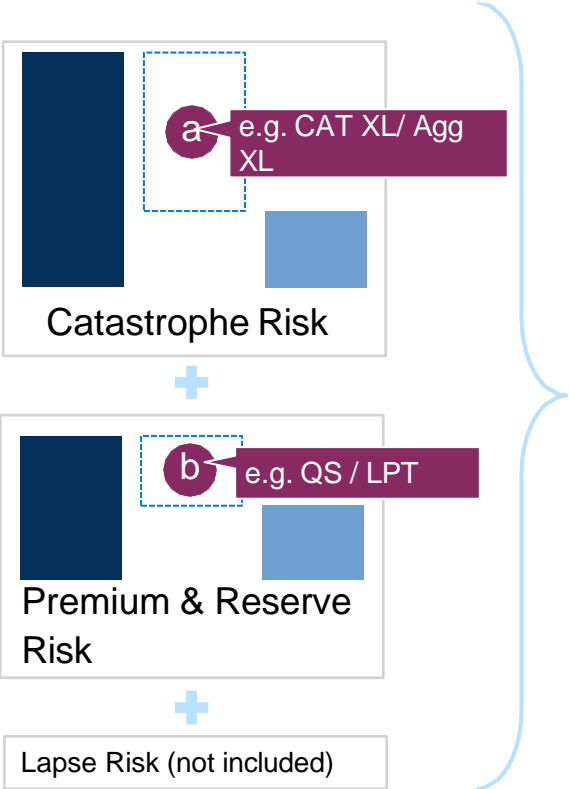
- Loss Ratio
- Expense Ratio
- Combined Ratio
- Reinsurance Utilisation Ratio

### Claims

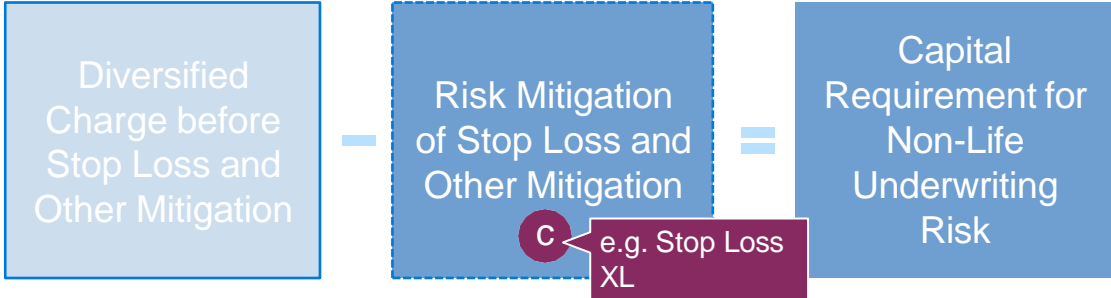
### Costs

- Reserve Ratio
- Solvency Ratio
- Return on Equity (**Risk Adjusted**)

# Basic Solvency Capital Requirements



The SAM capital relief from a reinsurance treaty is driven by the design of the individual treaty and the effectiveness of the overall reinsurance programme.



Bespoke design is key to ensure that appropriate capital relief is achieved at an efficient price.

# South African Examples

03



# South African Examples

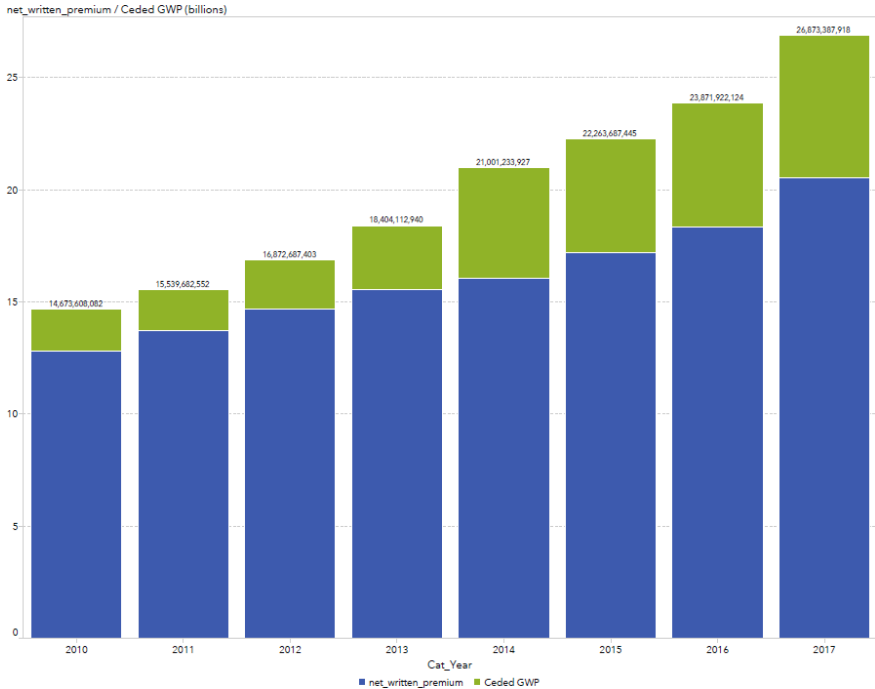
## Insurer A Income Statement 2018

	Notes	Audited Year ended 31 December 2018 R million	Audited Year ended 31 December 2017 R million	Change
<b>Gross written premium</b>		33 109	29 720	11%
Less: reinsurance written premium		9 041	8 027	
<b>Net written premium</b>		24 068	21 693	11%
Less: change in unearned premium				
Gross amount		2 019	648	
Reinsurers' share		(763)	(285)	
<b>Net insurance premium revenue</b>		22 812	21 330	7%
Interest income on amortised cost instruments	9	91	136	
Interest income on fair value through income instruments	9	2 205	1 184	
Other investment income	9	523	15	
Income from reinsurance contracts ceded		1 889	1 794	
Net (losses)/gains on financial assets and liabilities at fair value through income	9	(1 136)	427	
Investment income and fair value losses on financial assets held for sale	9	-	175	
Other income		246	127	
<b>Net income</b>		26 630	25 188	6%
Insurance claims and loss adjustment expenses		18 442	20 466	
Insurance claims and loss adjustment expenses recovered from reinsurers		(4 615)	(6 400)	
<b>Net insurance benefits and claims</b>		13 827	14 066	(2%)
Expenses for the acquisition of insurance contracts		4 524	4 218	
Expenses for marketing and administration		4 465	3 652	
Expenses for investment-related activities		67	67	
Amortisation and impairment of intangible assets		69	71	
Impairment of loans		5	-	
Investment return allocated to cell owners and structured insurance products		179	563	
<b>Total expenses</b>		23 136	22 637	2%

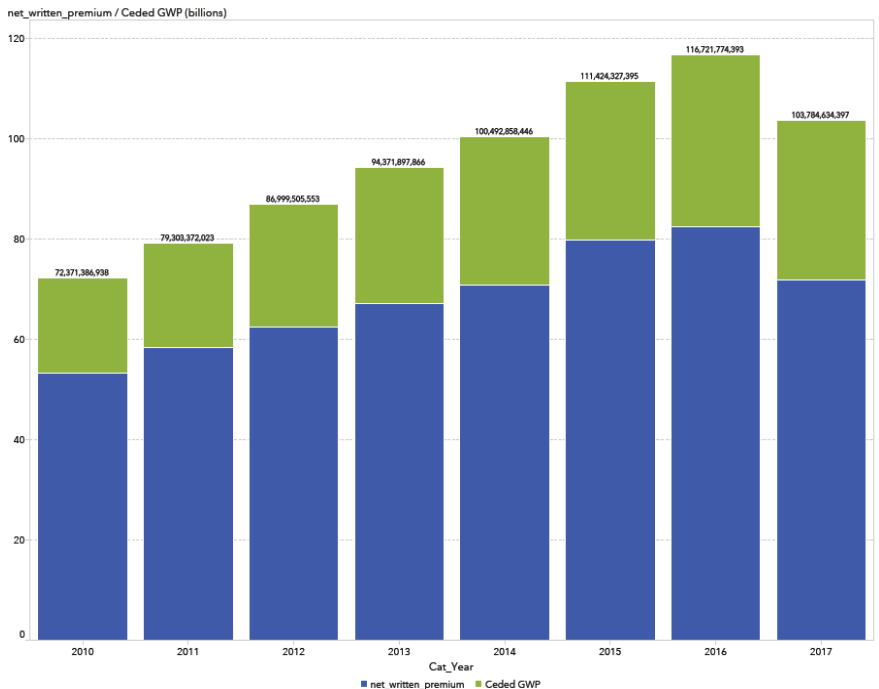
- Reinsurance expenditure represents a significant expenditure for largest insurer in South Africa
- What does this say about their reinsurance strategy?
- How has reinsurance impacted the results?

# South African Examples

## Insurer A Historical Reinsurance Utilization

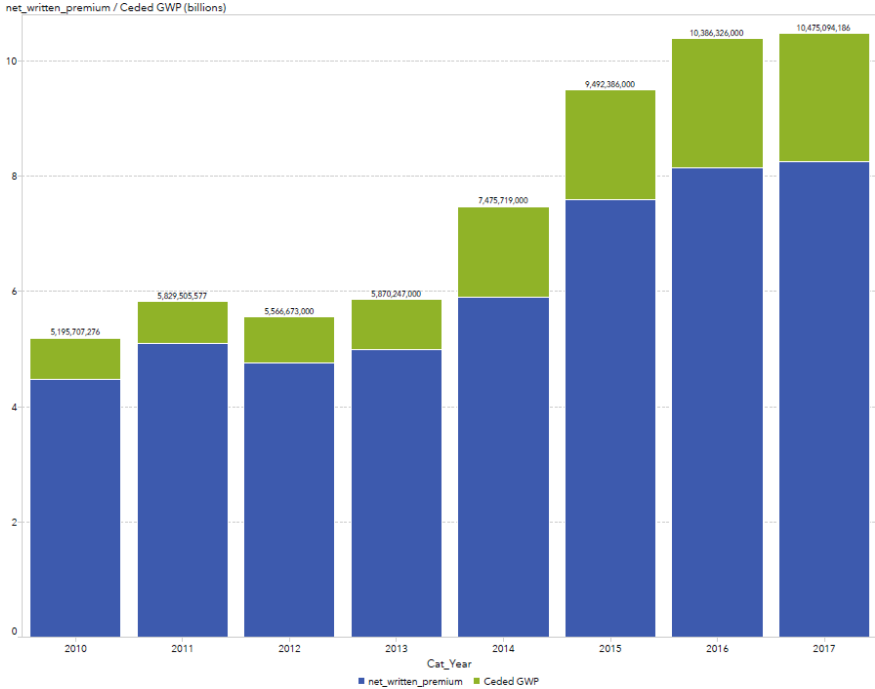


## RSA Industry Reinsurance Utilization

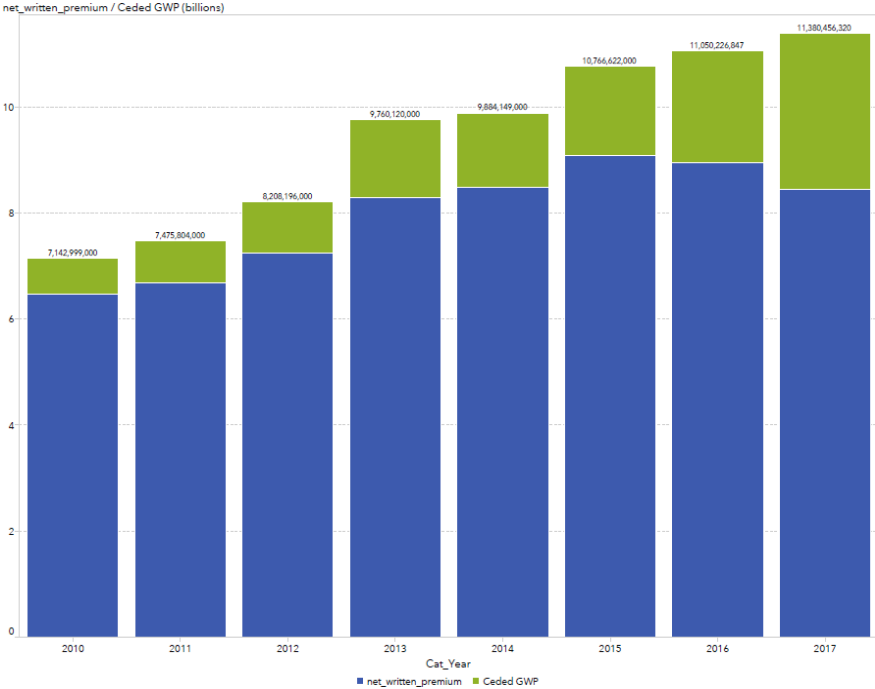


# South African Examples

## Insurer B



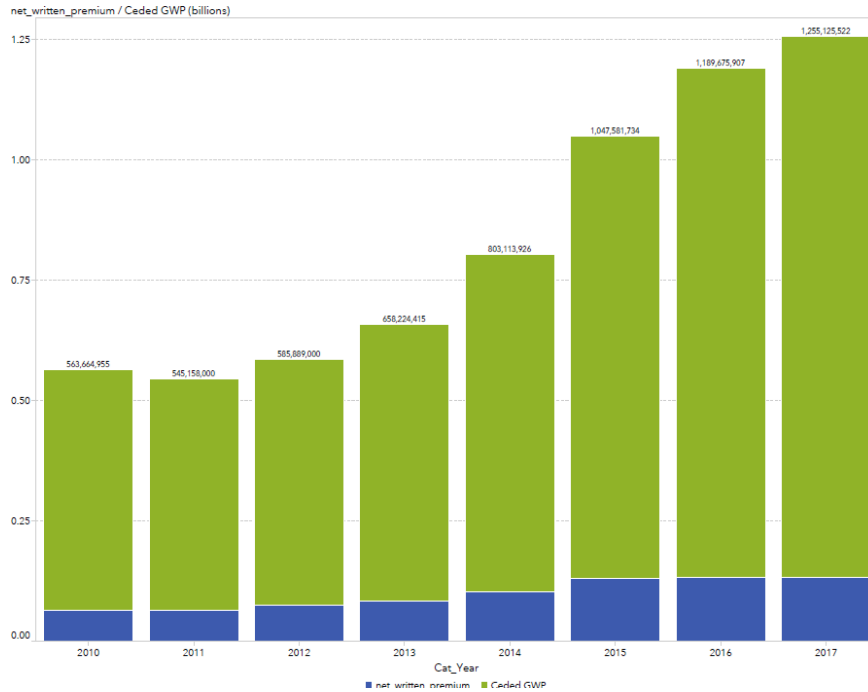
## Insurer C



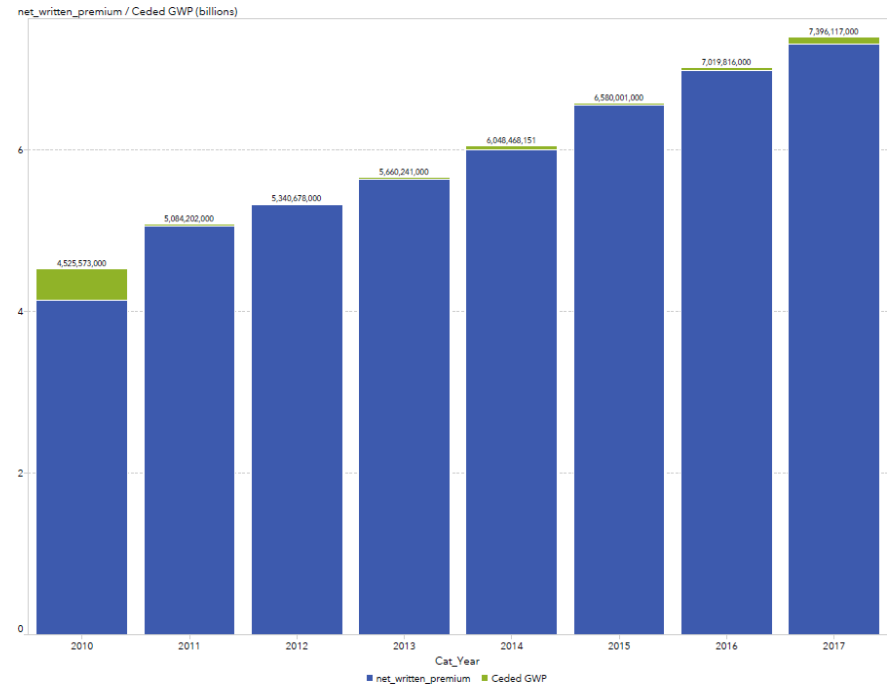


# South African Examples

## Insurer D

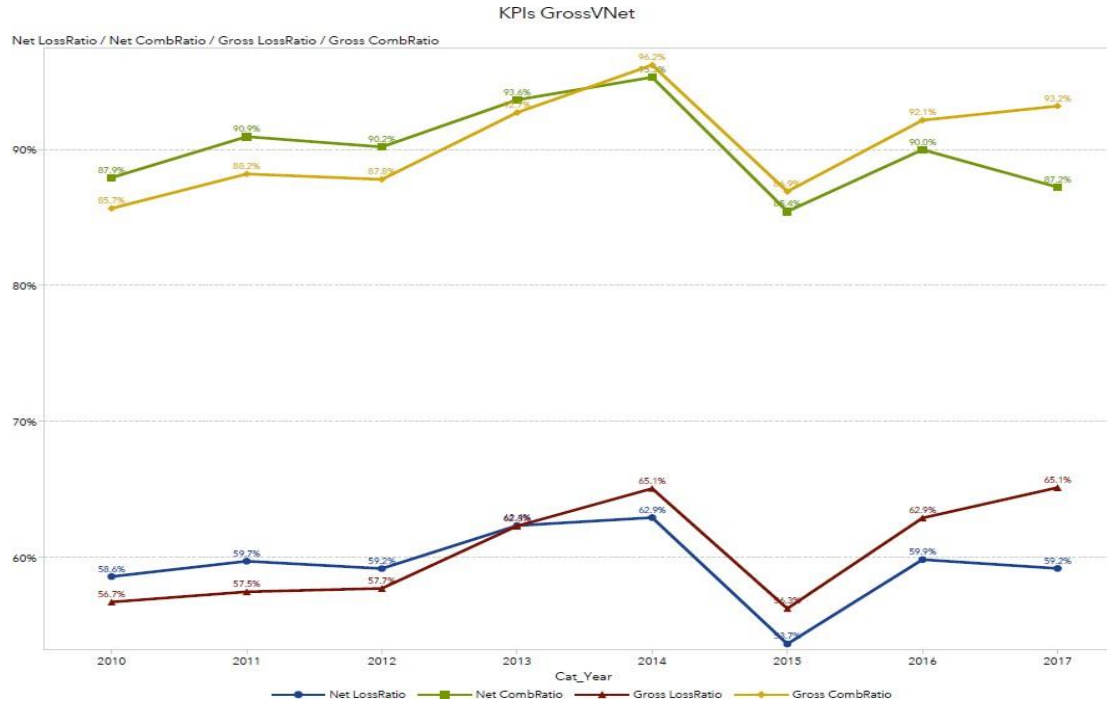


## Insurer E



# Impact of Reinsurance on RSA Insurers' Loss Ratios

## Comparison of Gross v Net Loss Ratio



- Reinsurance has had positive impact on loss ratio

# Benefits of Reinsurance

## Risk Transfer, Capital Management



- Protection against catastrophes – the risk of claims accumulation
- Provision of capacity for complex or large risks
- Financial support – the risk of capital challenges

## ... And So Much More

- Technical Expertise
- Research & Development
- Global Innovation Initiatives, e.g. Cyber Risks, Data Analytics, Predictive Underwriting
- Training and Consulting Services



# Motivations

04



# Understanding your motivation

This is key to designing bespoke Reinsurance Solutions to meet your needs



Business growth and expansion



Protect business plan



Avoid negative movement on planned figures



Earning smoothing and stability of returns



Solvency capital relief



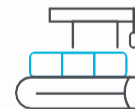
Financial (improve valuation, dividend protection)



Capital (additional capital need, efficient use of capital)



Discontinuation of business



Mergers & Acquisition situations



Disaster risk:

- Alternative capacity need due to regulatory restrictions, non-availability of capacity etc.
- Immediate liquidity need post-event

## I. Factors Affecting Reinsurance NEEDS

### 1. Growth Plans

- Rapid growth causes a drain on capital
- New book of business generally less stable than mature book
- New markets requiring higher limits of coverage

### 2. Types of Insurance Sold

- Insurance products offered vary in loss stability
- Personal v. Commercial insurance
- Surplus requirements/risk-based capital
- Higher levels of product diversification equate to more stable loss ratios

### 3. Geographic Spread of Loss Exposures

- Higher levels of geographical diversification equate to more stable loss ratios
- Regulatory, Legal environment
- Natural perils

### 4. **Insurer size**

- Small primary insurers need proportionately more reinsurance than large primary insurers to stabilize loss ratios

### 5. **Insurer Structure**

- Stock vs mutual companies: access to capital markets

### 6. **Insurer Financial Strength**

- A financially strong insurer needs less reinsurance than a weaker one

### 7. **Management's Risk Tolerance**

- Senior management's willingness to assume risk
- Must balance interests of the organization's various stakeholders



## II. Factors Affecting RETENTION SELECTION

### 1. Maximum the primary insurer can retain

- Regulatory requirements
- Primary insurer's financial strength

### 2. Maximum level of risk primary insurer is comfortable with

- Uncertainty of loss scenario probabilities
- Personal attitude (risk tolerance) of decision makers
- Importance of stability of annual results
  - Ex: publicly held stock co may be pressured by market to retain less than they legally/financially could to lessen chance of volatile YoY earnings

### 3. Minimum retention required by reinsurer

- To ensure ceding company has a meaningful stake in the outcome of the gross results of the reinsured business
- To encourage sound loss control, underwriting, and claims handling practices

## III. Factors Affecting Reinsurance **LIMIT SELECTION**

### 1. **Maximum Policy Limit**

- Review policy limits profile; note % of policies in higher limit bands
- Treaty vs Facultative: cost considerations

### 2. **Loss Adjustment Expenses**

- Consider: Liability vs Property

### 3. **Property Catastrophe Exposure**

- Computer modeling to estimate expected losses at various return periods for specific natural perils
- Review ground up loss estimates at key return periods, e.g. 100-year, 250-year return periods are key benchmarks.

### 4. **Clash Cover**

- Limits should be set considering the highest limits offered by the insurer and the likelihood that multiple policies will be involved in a single occurrence.

# Structured solutions at MRoA

We have the tools to ensure that a deal is completed within months and not over years



**We drive business together with you**

- We don't believe that "one size fits all" – we partner with you to ensure the best solution for your business.
- Each potential solution will have its own features and considerations.

## Potential Different Solutions

- Quota share
- Aggregate XL
- Retrospective covers (LPT/ADC)
- Contingent covers (variable triggers)
- Stop Loss XL

## Features & Considerations

- Risk transfer
- Flexibility
- Counterparty default risk
- Alignment of interest
- Gearing effect

## Our value proposition

- Strong deals teams with a wealth of expertise
- Well capitalised and strong credit rating
- Exceptional global consulting services



# Thank you for your attention!

11 September 2023  
Nkejane Mofokeng

NOT IF, BUT HOW

