



# The FAQs

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REINSURANCE. YOU KNOW IT'S A NECESSARY PART OF YOUR BUSINESS. YOU ALSO KNOW IT'S EXPENSIVE. IT'S RIGHT UP THERE WITH LOSSES AND PAYROLL ON YOUR BALANCE SHEET.

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So yes, it's important, but do you still have questions about reinsurance? If so, you're not alone.

Reinsurers and reinsurance brokers say clients ask questions frequently. While those questions vary by company size, structure, line of business, even location, reinsurers and brokers receive some common inquiries – and have several answers.

## Why is my reinsurance so expensive?

Hands down, this is the first question anybody asks. If we go back to right after hurricanes Katrina and Wilma, the market as a whole had suffered huge losses. Lloyd's of London had dramatically changed its realistic disaster scenario that helps determine whether a syndicate is appropriately capitalized. A.M. Best began changing how it viewed capitalization of the insurers it regulates and RMS made a dramatic change to its cat model.

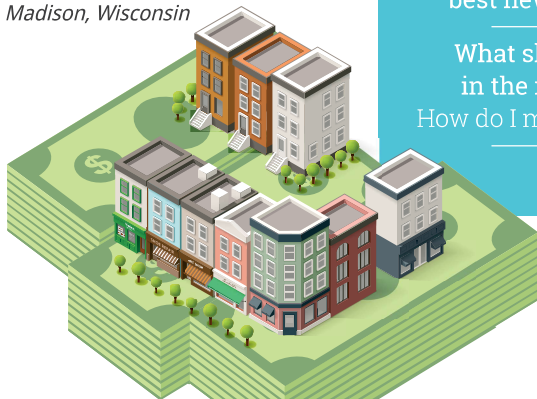
There was a confluence of events and catastrophe reinsurance pricing was going up 30 percent, 50 percent. Suddenly, you had companies in the Midwest that hadn't had losses or historically much change in pricing from one year to the next saying, "Wait a minute, why do we have huge increases in the price of our cat programs?"

[Regardless of location, insurers] are still part of the larger web of the insurance world, and it sometimes comes back to bite them. Sometimes, people are impacted by events outside of their control.

*Mary Ivy Noone*  
Senior Vice President  
BMS Re US  
Philadelphia, Pennsylvania

It depends on the company. It depends on loss exposures, loss histories, financial conditions, and cash flow. How much risk can they retain? How much risk do they want to cede to a reinsurer? If a company writes a lot of smaller risks that are widely dispersed, it will have a much different exposure and loss history than a company that writes in a major metropolitan area. That is a much more concentrated risk and it will impact cost.

*Terry Wendorff*  
President & CEO  
Wisconsin Reinsurance Corporation  
Madison, Wisconsin



## What's happening in the reinsurance marketplace?

Since 2012, we've seen property cat prices decrease at each renewal – on a risk-adjusted basis – for loss-free programs, albeit at a diminishing rate. Each year, we hear brokers and underwriters alike lament that we are “nearing the bottom” in terms of pricing. While we haven't found anyone who would reject this statement,


the consensus among most buyers is that their risk-adjusted property cat rates will go down yet again in 2018 – assuming they have a loss-free year. They are probably correct; it seems that for every reinsurer ready to walk away because of price, there are still two reinsurers willing to take a larger share of the program at that price. Let us not forget the new sources of capital starting up every month that cannot yet get a seat at the table.

While there are many factors to consider when discussing property cat pricing, it seems to have a little more room before we actually hit the bottom.

*Jeff Thomas*  
Vice President & Account Executive of Business Development  
American Agricultural Insurance Company  
Schaumburg, Illinois

There continues to be stiff competition for primary business, particularly for commercial lines with declining rates. Auto is an exception, being the one market segment experiencing healthy rate increases. Regarding the U.S. reinsurance market, conditions have been fairly stable during the past few renewal periods with rates and ceding commissions changing little on the average. This follows a few years of fairly significant rate reductions.

*Steve Levy*  
President of the Reinsurance Division  
Munich Reinsurance America  
Princeton, New Jersey



### Added Questions

Reinsurers and reinsurance brokers say insurance company clients pepper them with several other questions. Those questions include:

- How do we become stronger/more financially stable?
- Should we grow? What is the best way to use reinsurance to help us grow?
- Can you help us clarify our risk appetite?
- Other companies are doing X, should we be doing that as well?
- Why do different catastrophe models produce different results?
- How do I bring in the best new board members?
- What should we be doing in the innovation space?
- How do I manage rapid change?



## The Interconnection

There are a couple of ways to approach reinsurance. One is purely transactional – the reinsurance-is-a-once-a-year-conversation-that-happens-at-renewal approach ... unless something bad happens. The other is more relational – the throughout-the-year-partnership method.

While neither is right or wrong, it seems the continual, partner-like approach is gaining steam. **Casey Gibbs**, director of reinsurance marketing for **Grinnell Mutual Reinsurance Company**, believes it is.

“When I started here not that many years ago, it was the one-time-a-year deal,” he says. “Everybody came out in the fall, we gave them their prices, and everyone moved on.”

But just as the world has become more interconnected, Gibbs says so have reinsurance and insurance entities. “They are so interlaced, I don’t think we can look at either by themselves anymore,” he says.

“Reinsurers are learning X and taking it to the mutuals; mutuals are learning Y and bringing it to the reinsurers,” he continues. “We’re taking that combined knowledge to be better tomorrow than we are today.”

Therefore, Gibbs says relationships must be top priorities. “It isn’t a one-way street,” he says, “It’s a partnership really and truly.”



## Are we buying the right reinsurance program?

Essentially, companies are asking, “What is the most efficient way to buy reinsurance given our risk appetite?” The answer is different for everybody, but figuring it out lies in several things. It lies in an understanding of the company history as a buyer of reinsurance and its desire to have continuity with reinsurers. It lies in an analysis of the company’s exposures and in an analysis of various types of reinsurance structures to find which ones would most efficiently transfer the company’s risk to the reinsurance marketplace. And it lies in an understanding of how the company’s pricing for the program is positioned relative to other programs in the marketplace.

Overall, the answer to the question is found through a series of analyses blended with an appreciation for the company’s buying philosophy. It is a fascinating question to tackle, but it’s important for us to understand the blend of analytics and company preferences. We often have situations where an insurer will believe the analytics we show them, but they will modify our recommendations based on longstanding relationships.

*John DeMartini*  
Executive Vice President  
JLT RE  
Philadelphia, Pennsylvania

This is a question that is always out there. How does an insurance carrier select and execute the optimal reinsurance structure/program? It takes some very in-depth, deep-dynamic financial analysis that includes variance rating, exposure rating, and multi-model cat review. We use a number of different economic capital modeling techniques to identify the optimal structure, and, of course, peer review, too.

It is important to consider all the possibilities – treaty, facultative, insurance-linked securities, and other sources of capital. We’re interested in providing anything that jumps out as the best answer for the client. We spend a lot of time making sure we have access to information that puts us in a position to give mutuals the best terms and conditions available to them.

*Chris Delhey*  
Senior Managing Director  
Aon Benfield  
Chicago, Illinois

## What makes a good business summary for the reinsurance marketplace?

The best summaries cover a little history and are cohesive outlines of the classes of business written as well as historical and proposed changes. They help reinsurers understand where you have been, where you’re going, and why. [Insurer] data

presented in the same manner that the treaty is structured is a huge assistance for reinsurers during reviews. Items such as treaty terms, subject premiums, and estimated adjustments for rate changes not only help move a program through the system, they increase the credibility when final answers are assigned.

*Kevin Fry*  
Senior Vice President & Chicago Branch Manager  
Renaissance Reinsurance U.S.  
Schaumburg, Illinois

## How do I effectively communicate my company's view of risk and capital performance to rating agencies?

A.M. Best currently views the industry's capital as strong, so most companies will continue to be viewed as having strong levels of capital. However, individual companies may be viewed differently because of the nature and volatility of their exposures. We work with clients to help them "own" their risk in supporting capital management decisions and activities. This allows them to effectively communicate their credit story to Best and other ratings agencies.

Insurers must be proactive in addressing how they manage their capital on a risk basis. Capital models are increasingly becoming relevant to the A.M. Best discussions as Best moves to a stochastic-based capital model. Furthermore, enterprise risk management becomes more pronounced in the ratings process, putting more emphasis on formal procedures around corporate risk appetite, risk tolerances, and governance. Risk tolerance statements need to be well defined and informed by capital modeling. Key risks such as property cat losses will need to be quantified with a clear "management view." Other cat scenarios, including casualty catastrophe risks, will need to be identified, quantified where possible, and effectively mitigated.

*Jay Woods*  
Managing Director  
Guy Carpenter & Company  
New York, New York

## Is my reinsurer doing anything to make my business (and my gross result) better?

In recent years, reinsurance conversations have tended to focus heavily on improving/protecting net results. Clearly, this is a valuable consideration for an insurance company and needs appropriate focus; however, there have been fewer discussions

about how reinsurers can help improve a company's gross book of business. While reinsurance products can certainly protect net results for the short term, managing your gross underwriting result and profits allows you to better control your own destiny for the long term. Reinsurers share in an insurance company's results and only get paid via underwriting profits. Finding a reinsurance partner than can help guide you to success in generating gross underwriting profits is the best bet for the long term.

*James Whamond*  
Senior Vice President, Treaty - the Mutual Practice  
Gen Re  
Stamford, Connecticut

## What are you seeing relative to cyber? What kind of assistance can you provide relative to the risk?

From a reinsurance perspective, there are a number of solutions to reinsure standalone cyber risk, including quota share as well as catastrophe reinsurance protection, in the event that something happens that may cause aggregation potential. [We] have a dedicated team working full time to understand the evolving risk and opportunity.

*Edward Kelley*  
Senior Vice President & Deputy General Counsel  
Transatlantic Reinsurance Company  
New York, New York

Cyber coverage will be moving toward risks such as extortion and social engineering to address the rise in ransomware attacks and email schemes. Clients want a simple yet comprehensive cyber solution that includes coverage for data breach, damage to data and software, business interruption, extortion, network security, and media liability.

We've worked to offer a full array of services that we can provide mutual insurers with respect to cyber, ranging from traditional reinsurance to assistance in designing cyber coverages they can offer their customers.

*Steve Levy*  
President of the Reinsurance Division  
Munich Reinsurance America  
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*Tim Zeilman*  
Vice President & Counsel of Strategic Products  
Hartford Steam Boiler Inspection & Insurance Company  
Hartford, Connecticut

Because of space considerations, IN magazine could not include all responses or all questions.



# Reinsurance Put to Work

WHEN WILDFIRE DEVASTATED TENNESSEE IN 2016, THE IMPORTANCE OF A REINSURANCE RELATIONSHIP BECAME EVEN MORE APPARENT.

**LINDSAY ROBISON**

When **Marie Hurst** left for the **Sevier County Farmers Mutual Insurance Company** office the morning of November 28, 2016, the company's secretary/treasurer's truck was dusted with a greyish-white substance. When she headed home from the Sevierville, Tennessee-based office that afternoon, there was so much of the substance in the air that she could barely see the buildings across the street.

Because it was a very-late-fall day in a mountain location, many people would probably assume Hurst was in the middle of a snowstorm. But on that particular Monday, even the morning low temperature was too warm for snow, and snow is rare for Tennessee in November anyway. What was covering her truck and filling the air was ash and smoke – the results of a wildfire Hurst calls the most damaging event in Sevier County Mutual's century-long history.

"It never entered my mind that we would have this much fire damage, or a fire at all," Hurst says. "We're this small mountain community, a tourist area, and an all-around beautiful place. [The fire] was a heart-wrenching scene. As a Sevier County native and insurance agent, it was terrible, and it was out our front doors."

Months without rain and two misguided teens are said to be to blame for the fire. And a day full of high winds allowed the flames to spread, well, like wildfire. Fourteen people died, 175 sustained injuries, and more than 2,400 structures were destroyed. Overall damages came in at an estimate of more than \$500 million.

When the flames finally smoldered and the smoke and ash cleared from the skies, nine Sevier County Mutual policyholders suffered devastating losses that added up to \$750,000 of the total damage estimate. While only a fraction of the overall cost, three-quarters of a million dollars could be a distressing amount for an insurance company of Sevier County Mutual's size – \$950,000 in direct written premium.



Because the farm mutual has had more good loss years than not, the company's decision makers kicked around the idea of retaining this event. They ultimately decided using its reinsurance policy would be in the company's best interest. While no one wants to have to use

reinsurance dollars, Sevier County Mutual is a successful story of reinsurance put to work.

Less than an hour northwest of Sevierville in Knoxville, Tennessee, **Gordo Watson**, general manager of **Farmers Mutual of Tennessee**, was far enough away that he couldn't see the smoke and ash like Hurst could. Like much of the country, he watched it unfold on the news.

However, being only about 30 miles away from where the fires ignited, FMT insures policyholders who were in danger of physical harm and property losses – which isn't shocking. What might be surprising is that Watson was watching the fire not only with primary insurer attention but with a reinsurer eye as well.

Even though FMT is a small farm mutual company itself – \$11 million in direct written premium – it offers a reinsurance program to even smaller farm mutual insurance companies

across Tennessee, Sevier County Mutual among them. Therefore, when Hurst's company called its reinsurer for help, FMT's number was the one dialed.

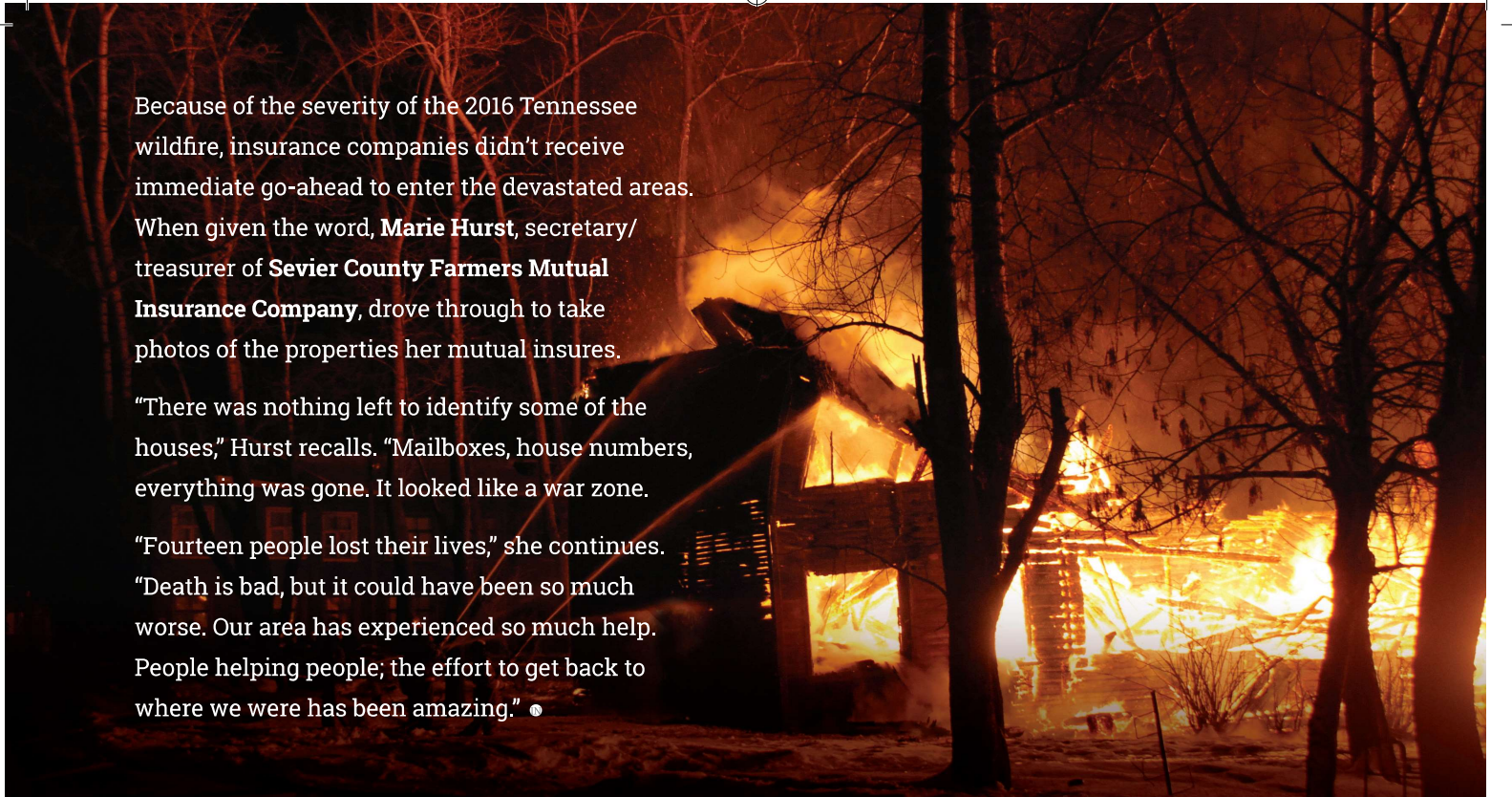
Watson says FMT has offered this reinsurance partnership to Tennessee mutuals for as long as he can remember. "We have always considered the relationship with county mutuals as part of our company mission," he says. "We decided to do this years ago to help keep county mutuals around, to make them better, and to keep them strong.

"This gives them some consistency in their numbers," he continues. "They're not going to have one bad year and then have to pay it all back to reinsurance the next year. This program helps smooth it out."

How the program works is that county mutuals file their claims with FMT. FMT, which has a reinsurer partner of its own – **Farmers Mutual Hail Insurance Company of Iowa** – will pay the county mutual in need. Next, FMT files a reinsurance claim. FMH then pays its share back to FMT.

"The contract we have with FMH is pretty set. In general, it is fifty-fifty" Watson says. "There is part of our program that is excess of loss. It protects them on the aggregate side as well as individual side, when losses are more than what a mutual can handle alone. Our reinsurer tells us it's difficult to get a program like this anymore. Most folks now are looking for a quota share." Most also go directly to a larger reinsurer or reinsurance broker.

"Our county mutuals might be able to find cheaper reinsurance,"



Because of the severity of the 2016 Tennessee wildfire, insurance companies didn't receive immediate go-ahead to enter the devastated areas. When given the word, **Marie Hurst**, secretary/treasurer of **Sevier County Farmers Mutual Insurance Company**, drove through to take photos of the properties her mutual insures.

"There was nothing left to identify some of the houses," Hurst recalls. "Mailboxes, house numbers, everything was gone. It looked like a war zone.

"Fourteen people lost their lives," she continues. "Death is bad, but it could have been so much worse. Our area has experienced so much help. People helping people; the effort to get back to where we were has been amazing." ●

Watson says, "but for an overall program and the fact of pooling this with ten other companies, it is a great value."

**Renee Walters**, senior reinsurance underwriter for FMH, agrees with Watson's belief about this three-pronged relationship. "We do have some clients in other states doing the same thing," she says. "But it is definitely not as common as the direct relationships we have with companies. It is a unique relationship, but it is a relationship that works well."

Interestingly, last year's event is one of only a few times that the claims part of the relationship has been activated.

"We haven't collected reinsurance and have paid very little out to county mutuals for twenty years," Watson says. "As we know, weather patterns have changed, and we did use [reinsurance] in 2011 and 2012 when we had terrible losses weather wise. But we did get to see that the program works, and it worked well."

Same went for the fire in 2016. By the time all claims were squared away, Watson says FMT paid one-third of the \$750,000 total. Everyone was happy with the process – even if they wished it hadn't happened.

Nearly a year later, the experience hasn't changed much for the three-party relationship. If rates had to change, it wouldn't be surprising; not with a loss like this one. The companies have discussed costs and how to keep them as minimal as possible, but those discussions happen yearly regardless of a loss.

"From my perspective, Sevier County Mutual and FMT handled all of this so professionally," Walters says. "I have to compliment the way they handled the catastrophe. They were prepared, they were professional. Sevier County was there for their insureds, FMT was there for Sevier County, and we were there, too." ●



## Relationships Are Key

**Renee Walters**, senior reinsurance underwriter for **Farmers Mutual Hail Insurance Company of Iowa**, says she remembers the fire in Tennessee like it was yesterday. Even though she was several states away from the flames, her first reaction was concern. Not of what it might cost FMH in terms of reinsurance losses, but of worry for the safety of those with whom she's built relationships.

"I called to check on the welfare of the employees [at Farmers Mutual of Tennessee and Sevier County Mutual]," Walters says. "Insurance is insurance. Property is property. It can be sentimental, but it can be replaced. Our friends and our relationships, they can't be. They were the number one concern."

Second on her to-do list was to let those in Tennessee know FMH was on standby, ready to help in whatever way possible. "If they needed help financially, handling claims, getting more people on the ground, we'd be there for them," Walters says. "It's sharing each other's tough times. When you're dealing directly in a catastrophe, you can forget about what is available to you and everything you need to do. Our role is to help companies through the process.

"It takes a village," Walters continues. "Reinsurance is much more than helping pay a claim." ●

# Twenty-Five Years Later

HURRICANE ANDREW'S MILESTONE ANNIVERSARY IS A REMINDER OF THE STORM'S IMPACT ON THE INDUSTRY.

 LAUREN ANDERSON

Sam Miller remembers the devastating scene after Hurricane Andrew hit the coast of Florida 25 years ago. He describes the widespread damage as incredibly shocking and amazing. "If houses survived, the roofs didn't. There were holes in roofs everywhere you looked," he says.

In 1992, Miller was running the Florida Insurance News Service, now known as the Florida Insurance Council. Shortly after Andrew made landfall on August 24, 1992, Miller had the opportunity to fly over the damaged area. It was his first time witnessing the extent of the damage left behind. For months following the disaster, he traveled around South Florida as co-director of the Hurricane Insurance Information Center.

"Debris removal was an incredible problem," says Miller. "If your home wasn't destroyed by Hurricane Andrew, you were surrounded by piles of trash that were higher than your house."

Hurricane Andrew provided a hard-learned lesson for the insurance industry – it wasn't prepared for a storm of that magnitude. Insurance claims payouts for Andrew totaled \$15.5 billion at the time – \$24 billion in 2016 dollars, and it remains the second-costliest natural disaster in U.S. history, after Hurricane Katrina.



"The cost of Hurricane Andrew is only part of its legacy," wrote Lynne McChristian, Florida representative for the Insurance Information Institute, in a 2011 white paper. "The storm revealed that Florida's vulnerability to hurricanes had been seriously underestimated, and that wake-up call was responsible for many of the insurance market changes that have occurred in coastal states over the last two decades."

One of those changes that occurred nationally throughout the next 25 years was a greater use of reinsurance. Insurers threatened to withdraw from the state following Andrew, which could have canceled massive numbers of existing policies.

"The losses were so incredible, [insurance] companies could not immediately recharge for the next hurricane season. It was a crisis," says Miller.

To stabilize the insurance marketplace, the state developed the Florida Hurricane Catastrophe Fund. The cat fund provided an added layer of coverage for insurers. Mandatory participation was required of every insurance company operating in Florida.

Another development came from the state in 1992. The Florida Residential Property and Casualty Joint Underwriting Association was created to provide property insurance to homeowners unable to get policies from private companies. It merged with the Florida Windstorm Underwriting Association in 2002 to become Citizens Property Insurance Corporation.

## Florida Insurance Landscape

### Then

Tiny windstorm pool

Insurers could easily buy reinsurance to avoid payouts from a multibillion-dollar storm

State Farm and Allstate had a 50 percent market share of Florida homeowners insurance, with out-of-state insurers handling most of the rest

### Now

Citizens Property Insurance covers 1.4 million policyholders, roughly 20 percent of the market, and a much higher percentage in coastal areas

Billions paid by insurers to shore up a state Hurricane Catastrophe Fund for added coverage beyond what they can buy in reinsurance

Beyond Citizens and State Farm, the list of top 10 insurers is led by small, Florida-based companies



"The whole insurance system in Florida was rewritten. Everything was affected by it," says Miller. "[Hurricane Andrew] demonstrated that the modern Florida just won't work the way our insurance system was set up."

For years following the hurricane, what is now Citizens was the leading property/casualty insurer in the state, providing coverage to more than 1.4 million policyholders with nearly \$500 billion in risk exposure. Today, according to I.I.I., Citizens is the ninth largest commercial insurer, a list now dominated by small, Florida-based companies.

"At the time, the role of the private market both in reinsurance and in primary insurance was shrinking," Miller notes. "Now it's expanding again, which is really wonderful."

A greater use of reinsurance is just one of the many lasting impacts Hurricane Andrew had on the insurance industry. Since 1992, Florida has strengthened its building codes, ensuring homes are more likely to withstand hurricane-force winds.

"An intense hurricane has a way of motivating people to invest in retrofitting their homes," McChristian wrote. "[It] makes them want to actively engage in the types of preparation that reduces their risk."

Another improvement is storm forecasting accuracy. Technology advances have enabled weather experts to make predictions about hurricane paths and intensities five to seven days ahead.



That compares to the three-days-in-advance warnings meteorologists could give 25 years ago.

The insurance industry received praise for moving quickly to settle claims from Hurricane Andrew. About 90 percent of all 700,000 claims had been settled within six months of landfall; about 95 percent of claims within nine months; and nearly 99 percent within a year – a record for insurers at the time.

"We were given a lot of credit in the media and by hurricane victims because the industry came in and worked so hard to quickly settle these claims that went on for months and months and months," says Miller. "I think it's important for the industry to remember how good a job it did." 5



## A Little Like Reinsurance

**GeoVera Insurance Group** is a unique organization that specializes in residential coverages that other insurers often shy away from: residential earthquake and residential windstorm hurricane insurance coverages. What also makes GeoVera unique is that while it can operate on its own, a key segment of its business is to take the earthquake and windstorm hurricane portions of risk from a partner primary insurer – on GeoVera paper. That allows its partners to keep policyholders who have these risks.

It sounds a little like a reinsurance relationship, doesn't it?

In fact, when GeoVera got its start, company executives pondered the reinsurance route. "We decided early on that we did not want to operate as a reinsurer," **Karen Padovese**, GeoVera's chief operating officer, says. "Reinsurers require significantly more capital than our general-agency-type structure. GeoVera accesses reinsurance capital the way a managing general agency does."

Despite not going the reinsurance company route, reinsurance is often what brings GeoVera and its partner insurance companies together. Reinsurance brokers working with insurers

in earthquake- and hurricane-prone areas will explain GeoVera as a potential option, telling them how "it isn't reinsurance but it will help manage exposures that concern them," according to Padovese.

While GeoVera started its business in California and Florida, it's opened up to western states, parts of Louisiana, Texas, and many of the states along the Eastern

Seaboard. It's also expanded its lines of business beyond traditional homeowners insurance.

"We're always looking for new products and new partners, but we'll always be homeowners based," Padovese says. "It always goes back to cat-exposed homes. That is what we stay true to, to make sure we have the money to pay the claims and spread the risk." 5

**"I always tell new employees, 'We're not in the catastrophe business because we really love insuring homes along coastlines and close to earthquake faults. But when you have data and technology advantages allowing you to aggregate exposures to show reinsurers where they are, you can make a business out of it.'"**

— **Karen Padovese**  
Chief Operating Officer  
GeoVera Insurance Group



# Weighing the Alternatives

ALTERNATIVE CAPITAL MAY BE A GROWING SEGMENT IN THE REINSURANCE MARKET, BUT MIXED FEELINGS ABOUT IT STILL EXIST.

 LINDSAY ROBISON

An elephant and an 800-pound gorilla walk into a room. While this sounds like the beginning of a joke, it's not. In the current reinsurance marketplace, the elephant and gorilla are one and the same, and they are no laughing matter. They represent the serious subject of alternative capital.

"Alternative reinsurance capital is just what it sounds like," says Robert Hartwig, Ph.D., co-director of the Darla Moore School of Business's Risk and Uncertainty Management Center at the University of South Carolina and the immediate past president for the Insurance Information Institute. "It is another source of capital that is available to protect primarily against catastrophic risk."

Why is alternative capital the mixed-animal metaphor?

Because feelings about it are also mixed. Not everyone is excited about or wants to tap into the alternative capital reinsurance market, but it is a force within the space.

This capital comes in several forms. "Alternative reinsurance capital is characterized by two twists on the traditional reinsurance arrangement," according to an I.I.I. white paper written by Hartwig and the organization's chief actuary James Lynch. "First, a new breed of investor is seeking out the reinsurance market – hedge funds, sovereign wealth funds, pensions, and mutual funds.

"Second, the deals are structured differently," the white paper continues. "The new arrangements – catastrophe bonds, collateralized reinsurance, and reinsurance sidecars – tend to isolate the investment from the rest of the capital supporting a reinsurer, thereby allowing the capital to enter and exit the market quickly."

Two decades ago when alternative capital really started making headway, market veterans welcomed this new option. "They were viewed as a complement to the traditional market," Hartwig says. "There was a significant shortage of reinsurance in the post-Hurricane-Andrew world. Prices spiked, capacity was limited, and the capital markets provided a sort of safety value by providing an alternative force."

Reinsurers tapped into the alternative funds. "Ultimately, some of the biggest users of alternative capital were reinsurers," Stephen Korducki, president of BMS Re US, says. "They set up sidecars and other mechanisms to transfer risk."

As the world moved past the major catastrophes of the early- and mid-2000s and experienced the financial crisis that began the low-interest-rate environment, alternative capital providers started to see the industry as a prospective way to diversify their own investment portfolios.

William Dubinsky, managing director and head of insurance-linked securities at Willis Towers Watson Securities, uses a large pension fund as an example. "Equity investments in the United States, Europe, and Asia are going to be highly correlated," he says. "But an earthquake in Tokyo and an equity market decline are largely uncorrelated. A large earthquake will almost certainly not cause the equity market to collapse.

"If [the pension fund] invests one billion dollars in a reinsurance risk, they are diversifying," he continues. "They could lose a substantial portion quickly, but within the context for a one-hundred-billion-dollar portfolio it isn't a huge loss."

The potential payout far outweighs the almost-blip-on-the-radar risk, which has drawn providers to the market.

An Aon Benfield report from late 2016 showed alternative capital hitting close to \$80 billion within the market. While that amount makes up only about 15 percent of the market total, Aon Benfield also reported that alternative capital's increase outpaced traditional reinsurance by nearly 5 percent.

"I think the general view is that alternative capital has gone from complement to competitor in the reinsurance market," Hartwig says.

This competition has led to a soft reinsurance market that has meant options and – for many primary insurers – lower costs for their reinsurance portfolios. Dubinsky says he believes it will keep the market relatively soft. If a large catastrophic event, such as a major hurricane in Florida, were to happen again, "the influx of alternative capital has made it much more likely that a hard market will not be quite as hard, and it will be shorter," according to Dubinsky.

He believes alternative capital is nothing but an opportunity for insurers while it is an opportunity and a threat for reinsurers.

Hartwig says alternative capital is still met with mixed feelings for many insurance companies, especially for a large portion of NAMIC members.

"[Alternative capital] is viewed positively in the sense that there are more options in terms of accessing capital," he says. "At the same time, for companies that make up the lion's share of NAMIC members, long-term relationships with reinsurers are extremely important."

Alternative capital providers are on **Norfolk & Dedham Mutual Fire Insurance Company's** radar but not yet in its portfolio, according to **F. Timothy Hegarty**, the organization's chairman. "It's a trend we've seen for the last eight or ten years," he says. "It has tended to control and even depress pricing, so from the standpoint of a reinsurance buyer, we like that it's kept prices stable.

"But you can get into some situations when coverages get confusing," he continues. "When you have reinsurers you've worked with for years, you can sit down and more likely talk things out."

**Stuart Henderson**, president and CEO of **Western National Mutual Insurance Company**, echoes much of Hegarty's sentiments. Although he knows about the options available to

Western National through the alternative capital markets and knows of some primary insurers taking advantage of them, he's not led his organization in that direction.

"Most of the time when I am talking with other CEOs of NAMIC companies, they're not doing anything with alternative capital either," Henderson says. "But we are the beneficiaries of the competition."

**Brian Taylor**, president and CEO of **Municipal Mutual Insurance Company of West Virginia**, is on the same page. He says he's received information from his company's reinsurance broker as well as from A.M. Best. While he's glad to have the information and is paying attention, his company hasn't tried that option.

Korducki agrees with the relationship aspect, adding that "if you look at [alternative capital] on a relationship-driven-to-transaction-driven spectrum, every company picks a point on the line. Some companies want longstanding relationships; others are purely transactional, saying 'get me solid protection at the best price.'"

Yet, some people have called alternative capital's stickiness into question. "There is no guarantee that an alternative capital provider will remain in the market after it suffers an extreme loss," Hartwig says.

Because the market hasn't suffered Hurricane-Katrina-like losses since Hurricane Katrina more than a decade ago, alternative capital providers' resiliency in the market has gone relatively untested.

"Until something happens, it's hard to predict what the reactions of alternative capital providers will be," Korducki says. "But all indications show that they certainly have the resources to stay in should they want to." 