Trends On Global Reinsurance Market: Ratings Should Withstand Weak Conditions, For Now

Ekaterina Tolstova
Associate
Insurance Ratings

23 June 2016

S&P Global Ratings

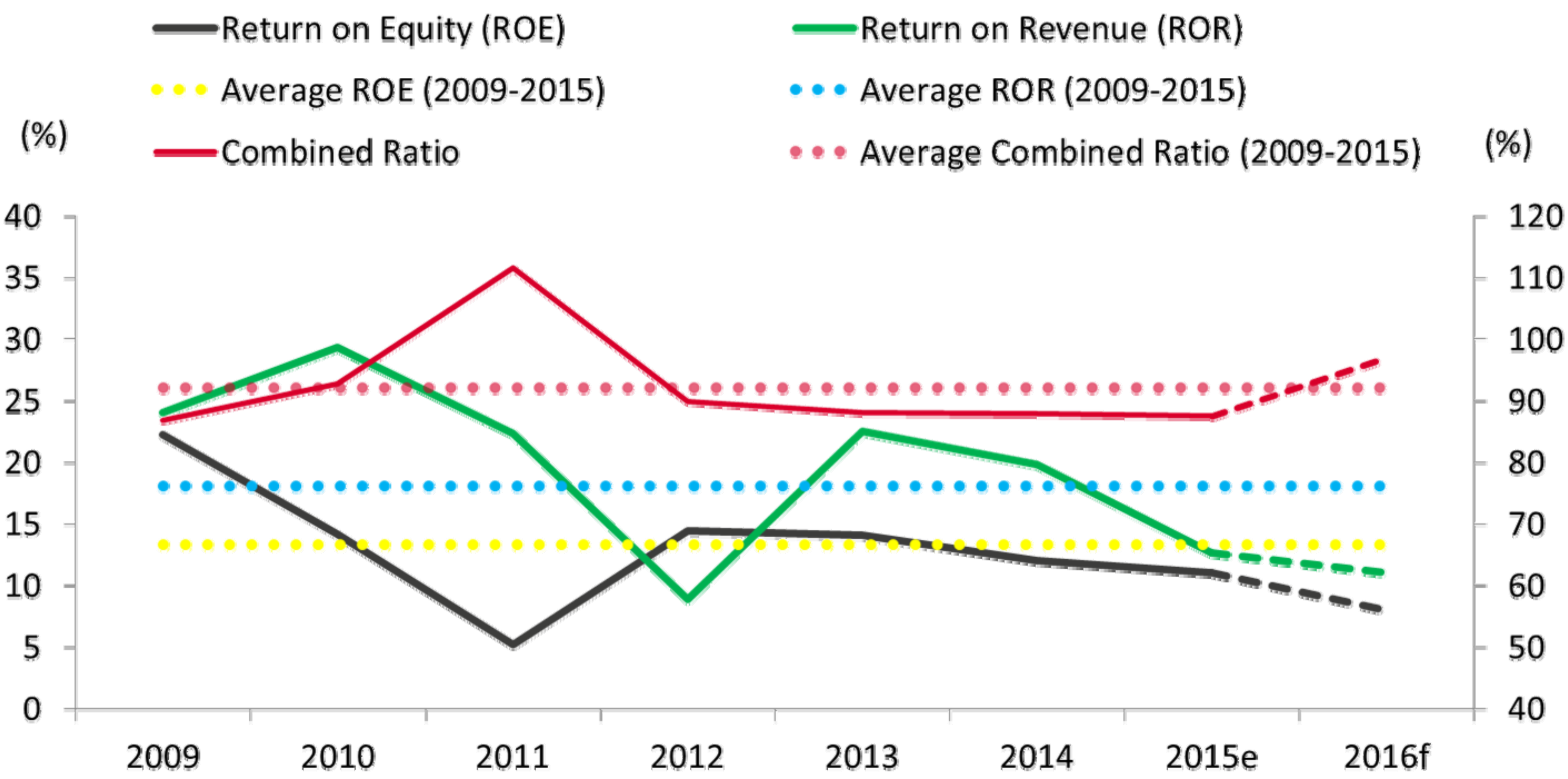
Various Factors Driving Weak Business Conditions

Reinsurers' Business Models Being Hit On All Fronts

Potential driver	Trend for 2016	Observations
Pricing	Negative	Pricing continues to decline across the board; average price reductions of up to 5% are expected in 2016, with wide variation across lines and regions.
Cedant demand	Neutral	The recent drop in reinsurance demand appears to have plateaued in 2016; with no rebound in sight.
Organic growth	Negative	Opportunities for organic growth are few; some pockets present a glimmer of hope for profitability, but these windows of opportunity close quickly as competition among reinsurers heats up.
Loosening of terms and conditions (T&C)	Neutral to negative	Large reinsurers seem to have largely resisted client demands for more generous T&Cs. Although reinsurance terms have loosened in some areas, these were areas that could be priced for.
Low investment returns	Negative	"Lower for longer" is a reality for investment returns. Reinvestment rates remain paltry and we expect investment returns to remain painfully low for some time.
Insurance-linked securitization (ILS) capacity	Neutral to negative	The influx of ILS capacity slowed in 2015 as low prices in the traditional market made it more cost-effective, in some cases. However, total ILS capacity remains at record levels and is still affecting catastrophe pricing.
Merger and acquisition (M&A)		

Profitability Is Likely To Be Hit

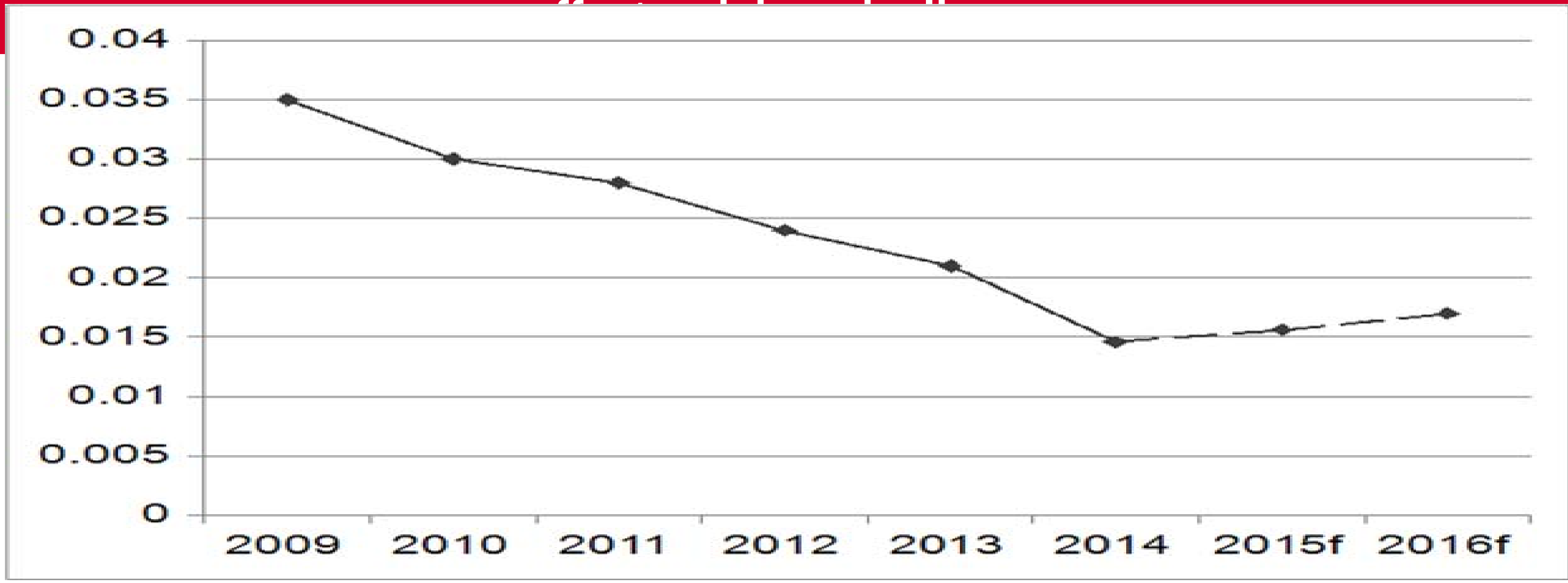
The Industry May Struggle To Meet Return Targets As Underwriting Margin Decreases



S&P Global
Ratings

Investment Returns Won't Mask The Pain

We expect reinsurers' investment yields to improve, but not enough to



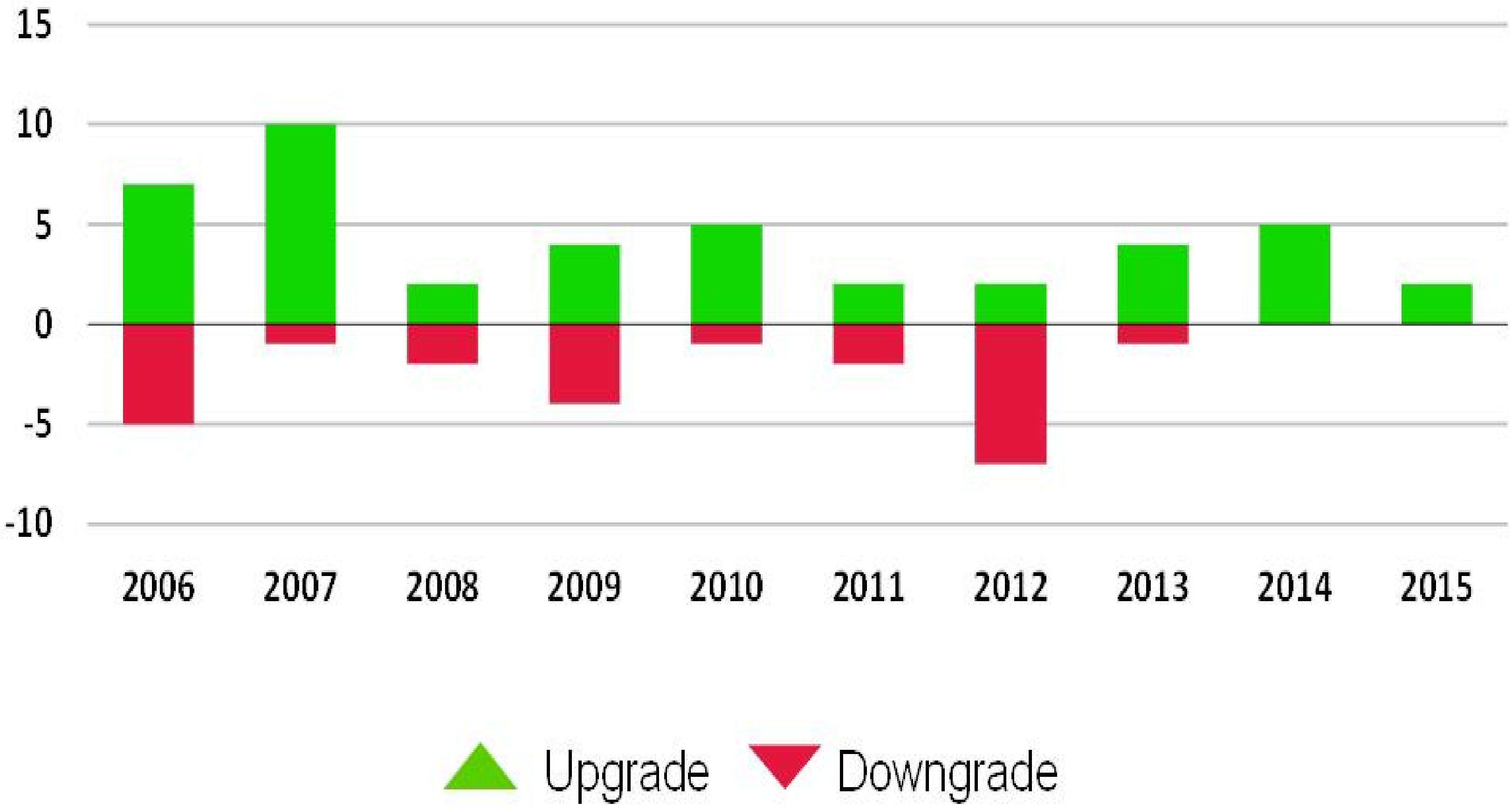
- **We forecast modest increases in interest rates in 2016, which should lead to slightly improved yields over time**
- **Reinsurers may also look to augment investment portfolios to improve returns**
  - **Extending duration of asset portfolio**
  - **Taking more liquidity risk via longer-term assets (e.g. infrastructure, real estate)**
  - **Higher allocations to risk assets (equities, HY corporate debt, ABS)**

Defense Provides Stability, But Pressure Remains

We Foresee A Rocky Road Ahead For The Industry

- Business conditions remain weak, and reinsurers will continue to struggle to generate the returns of the past
- Consolidation should continue, but won't alleviate the competition as pricing will continue to fall in 2016
- Reinsurers have responded appropriately with defensive measures, buying some more time for the cycle to turn
- We have a stable rating outlook for the sector, with an expectation for few rating actions over the next 12 months
- Those with scale, diversity, expertise and scope are best placed to withstand pressures
- Smaller, more concentrated reinsurers will need to carve out competitive position while protecting capital and bottom line, and could be candidates for future consolidation or marginalization

Ratings Distribution & Trends: Global Reinsurance



Data as of December 31 of each year; 34 interactively-rated companies and groups.
Source: S&P Global Ratings.

S&P Global
Ratings

Thank you