Alternative Risk Markets

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Swiss Re

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Alternative Risk Markets

- Scope
- Accessing the Capital Market
- Cat Bonds
- Sidecars
- ILWs
- Derivatives (OTC & Exchange Traded)
- Club Deal/Private Deal
ILS Market Size

Non-traditional Investors
- 16 USD billion outstanding
- Cat Bonds
- Quota Share/Side Car Vehicles
- Private Deals
- Collateralized Insurance, ILWs and Futures
- New Perils?
- Credit and Motor Insurance

Traditional Fixed Income Investment Grade Investors
- 25 to 30 USD billion
- Life Cat
- Embedded Value
- Surplus Relief e.g. Reg XXX
- Life Settlements
- 35 to 40 USD billion
- Life
- Non-life

Source: Swiss Re Capital Markets
Market Segmentation: Basic Terms

- **Cat Bond**: source of collateralized excess of loss (re)insurance capacity raised in a private placement offering.

- **Sidecar**: source of proportional (re)insurance capacity raised in a private placement offering.

- **Industry Loss Warranty or ILW**: catastrophe protection where the payoff depends in whole or in part on whether industry losses from an event exceed a predetermined amount.

- **Club Deal/Private Deal**:
  - Transaction with either a handful investors or even a single capital markets investor.
  - Investors take risk on in derivative, securities or reinsurance form.
**Total non-life bonds outstanding, by year**

As of July 1, 2008  
Not including Sidecars  
Source: Swiss Re Capital Markets
Diversity of Risks

Risks Securitized from 1997-2008*
in USD billions

*As of 5 March 2008
Not including sidecars
Source: Swiss Re Capital Markets

securitization, ILW, collateralised quota shares and sidecars add to the flexibility of capital in the industry
Who Participates in the ILS market?

A diverse range of institutional investors participate in the ILS sector

- Dedicated Fund: 44%
- Money Manager: 22%
- Bank: 13%
- Hedge Fund: 14%
- Insurer: 3%
- Reinsurer: 4%
- Dedicated Fund: 44%

Market size ≈ USD 15.4 bn

As of May 30, 2008
Not including sidecars
Source: Swiss Re Capital Markets
Focus on Cat Bonds: Typical Structure

1. The Sponsor enters into a financial contract with a Special Purpose Vehicle (SPV)

2. The SPV hedges the financial contract by issuing Notes to investors in the capital markets

3. Proceeds from the securities offering are invested in high quality securities and held in a collateral trust

4. Investment returns are swapped to a LIBOR-based rate by the Swap Counterparty
Focus on Cat Bonds: Trigger Types

- An indemnity transaction is based on the actual losses of the sponsor.
- An industry index transaction is based on an industry-wide index of losses (e.g., Property Claim Services or “PCS” in the United States).
- A pure parametric trigger is based on the actual reported physical event (i.e., magnitude of earthquake or wind speed of hurricane).
- A parametric index is a more refined version of the pure parametric trigger using more complicated formulas and more detailed measuring locations.
- In a modeled loss transaction, losses are determined by inputting actual physical parameters into an escrow model which then calculates the loss.
- In a Modeled Industry Trigger Transaction (“MITT”), industry index weights are set post-event using modeled loss techniques.

* Increased acceptance of indemnity triggers

*Developed and patented by Swiss Re*
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Secondary Trading & Cat Bond Returns

* Source: Swiss Re Capital Markets. Both Life and Nat Cat perils represented.
** "SRBB Cat Bond Index", calculated by Swiss Re Capital Markets, is an equally-weighted basket of nat cat BB-rated cat bonds traded by Swiss Re Capital Markets, calculated on a weekly basis; past performance is no guarantee of future results
Underlying data for Lehman BB Index provided by Lehman Brothers
Underlying data for "SRBB Cat Bond Index" is based on indicative prices only
ILS Developments

- Closer to traditional reinsurance
- Structural improvements
- Use by government and PPPs
- New perils