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Hotel Sea Princess
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Using Reinsurance to help with capital management

Graham Bancroft

Munich RE

Institute of Actuaries of India

Where

Reinsurance for Capital management is used as a tool in most markets

It is accepted globally as a legitimate approach by

- Regulators
- Auditors
- Insurers
- Shareholders
- Rating agencies

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When

Reinsurance can be used when the following needs arise:

M&A Opportunities

- Frequent M&A activities in Asia
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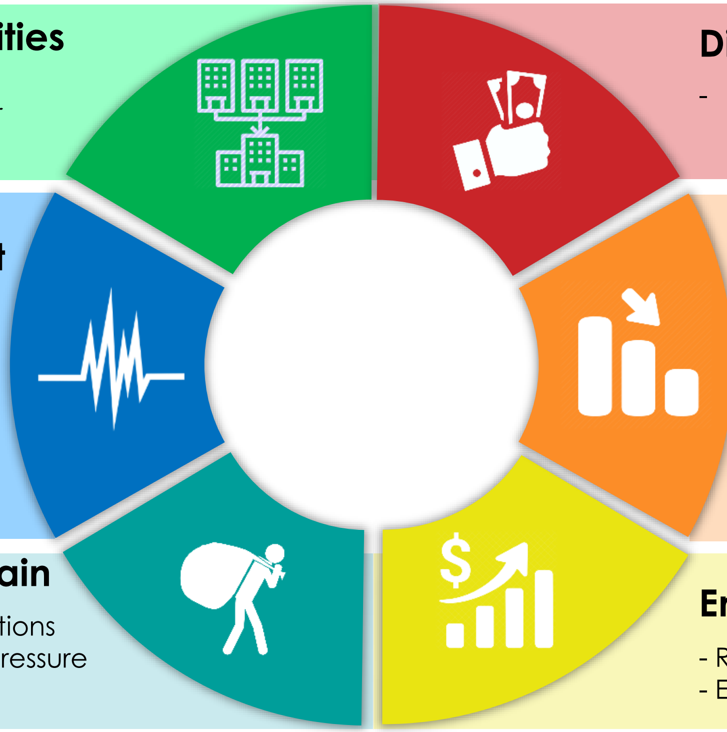
Dividend Upstream

- Multinational and regional insurers would demand dividend upstream to meet shareholder expectations



Earnings Volatility Management

- Contingent financing against adverse interest rate / asset value movement
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Pressure on Solvency

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New Business Strain

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Enhanced Return

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When

If you have Pressure on Solvency, options are:

Reinsurance is one of a number of options which can be used ..

Assets: **Reduce Required Capital**: De-risk	**Re-allocations within investment portfolios** ▪ Sale of participations ▪ Reduction of equity ratio
Liabilities: **Reduce Required Capital**: De-risk **Reduce Liabilities**	**Reduce business volume** ▪ Reduction of, or exit capital intensive lines of business **Restructure products & their management** ▪ Reduce product &/or mismatch risk, hedge **Risk transfer mechanisms** ▪ **Reinsurance: reduce liabilities & required capital**

Increase Capital	**Capital structure**
	▪ Increase equity, hybrids, subordinated debt
	▪ Increase income:
	  ▪ **Reinsurance: provide funding/income**
	  ▪ Sale of blocks/companies
	  ▪ Reduce sales of high strain business

Why

If capital is needed, Reinsurance has advantages..

Comparison of options – complementary tools

	Equity	Hybrid	Sub Debt	Securitization	Reinsurance
Size	Med - Very Large	Medium	Medium	Large	**Small - Large**
Capital treatment	Tier 1	Tier 1-2	Tier 1-2	Tier 1	**Tier 1**
Required capital	Neutral	Neutral	Neutral	Reduce	**Reduce**
Cash provided	Yes	Yes	Yes	Yes (or contingent)	**Optional**
Duration	Permanent	Med - Long	Med - Long	Long	**Short - Long**
Cost	High	Med - High	Medium	Low (for big deals)	**Low - Med**
Collateral	Last call on value of company	preferred call on value of company	preferred call on value of company	Block of business	**Block of business**
Time to place	Med	Med	Med	Med - Long	**Short**
Commit to future capital at fixed terms	No	Yes - debt that converts to equity	No	Cat Bonds	**Yes (but for limited time horizons)**
Trigger		Fixed durations, Tier 1 level trigger experimental		Insured event	**Can be at insurers option**
Counterparty risk	No	No	No	No	**Depends on structure**

Who

Stakeholders who benefit from reinsurance

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Policyholders

- **Policyholders' Protection.** Long term financial viability of insurers ensures benefit payments are honored in the future.
- **Policyholders' Confidence.** Ability to withstand volatilities in the market sends a positive signal to policyholders.
- **Better Products to Consumers.** Cost savings can be translated into better products that will benefit policyholders.
- **Policyholders' Expectation.** Bonus declaration can be smoothed for par policies.

Regulator

- Maintains the **life insurance market strength**
- **Protects the solvency** of healthy insurance companies if volatile movements are experienced
- **Help the market to become more competitive** and **reduce the policyholder protection gap.**

Primary Insurers

- Achieve **better return** and **profitable business expansion**
- To hedge **against earnings/surplus volatility**
- To maintain a **healthy level of solvency**

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Who

Regulators across the region approve of and benefit from reinsurance ..

- Using reinsurance to help companies capital position is widely supported by regulators around the region
- We work closely with regulators, helping to share best practices and we work closely with clients to help them through the approval process
- We have introduced new capital approaches for the use of reinsurance with Singaporean, Malaysian, Philippine and Indonesian regulators

Munich Re takes reputation risk very seriously

What

Reinsurance types used for capital management are no different than normal:

1

Yearly Renewable Term (YRT)

- Sometimes referred to as “risk premium reinsurance”
- Reinsurance premiums paid to cover **mortality and morbidity risks, some lapse risk may also be transferred**

2

Coinsurance

- Reinsurance premium is a pre-defined share of the **gross premium**
- Reinsurance recoveries may **cover all benefits** including mortality/morbidity, surrender, maturity, etc.
- Reinsurance Commission can be incorporated
- **Cash transaction** - Reinsurer builds up their reserves and assets on their portion of the risk

3

Modified Coinsurance (ModCo) or Coinsurance deposit back (CoDB)

- Coinsurance where **ceding company keeps assets**
- More regulatory friendly as assets stay with the ceding company

Transaction 1

What

Use of reinsurance for capital purposes - Australia

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AMP

AMP in Reinsurance Deal with Munich Re

DOW JONES NEWSWIRES

October 27, 2016 by DOW JONES INSTITUTIONAL NEWS — Leave a Comment

By Robb M. Stewart

MELBOURNE, Australia--AMP (AMP.AU) has moved to sharply reduce the capital intensity of its wealth-protection business in Australia through a deal with Germany's Munich Re AG to reinsure half of the 750 million Australian dollars (US$574 million) in annual premium income of its AMP Life retail portfolio.

Advancement of future profits into cash leading to stronger capital and solvency position.

In October 2016, Munich Re executed a cash financing transaction with **AMP Australia** (public information)

Motivation was to reduce the **capital intensity and earning volatilities** from its protection business

Reinsured 50% of inforce retail portfolio with **A$750m** of annual premium income. Receive upfront reinsurance commission of **A$530m**.

AMP Chief Executive: "transaction helps to improve earnings stability, free up capital, and help bring into focus the growth potential of AMP"

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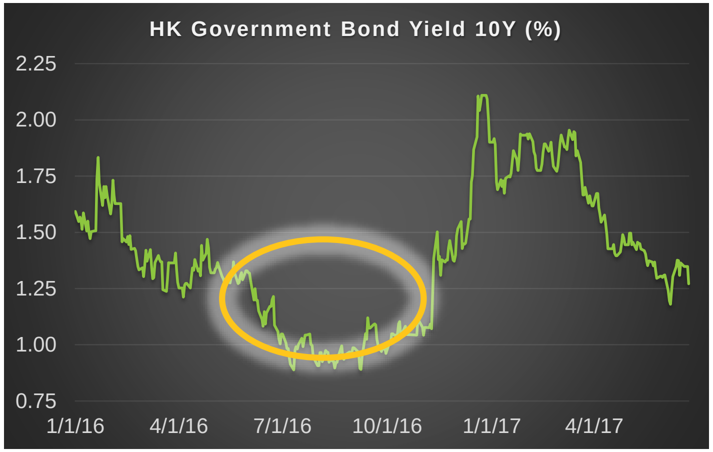
Transaction 2

What

Use of reinsurance for capital purposes – HK



Source: Trading Economics

Another widely accepted solution to advance future profits.

L A

Liabilities durations are longer. Decrease in interest rates -> higher increase in liabilities than assets -> **solvency deteriorates**

Use cash financing on inforce portfolio to **convert future profits** into physical cash

Cash received increases available capital -> **improving solvency ratio** (as balance sheet asset)

Munich Re has executed **13 times in Hong Kong in the last 4 years**;

What

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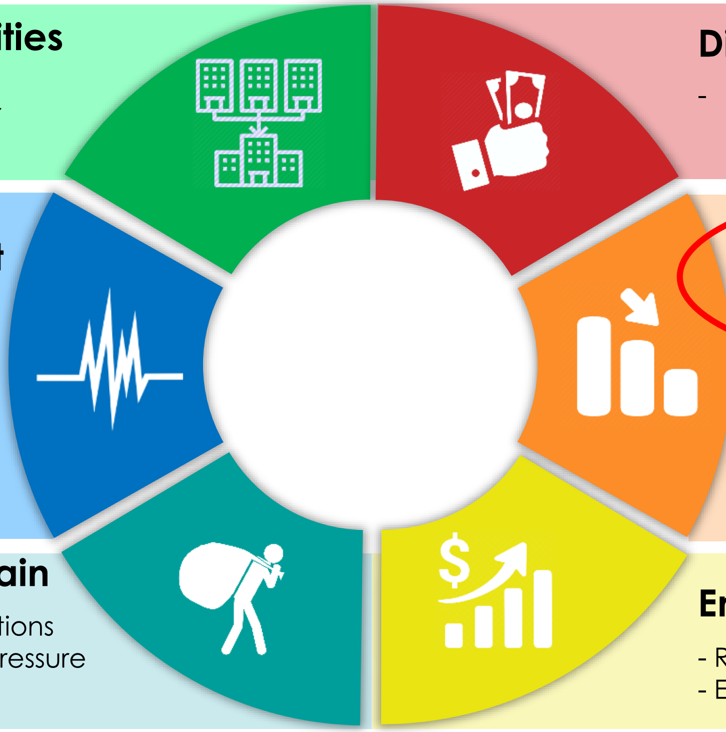

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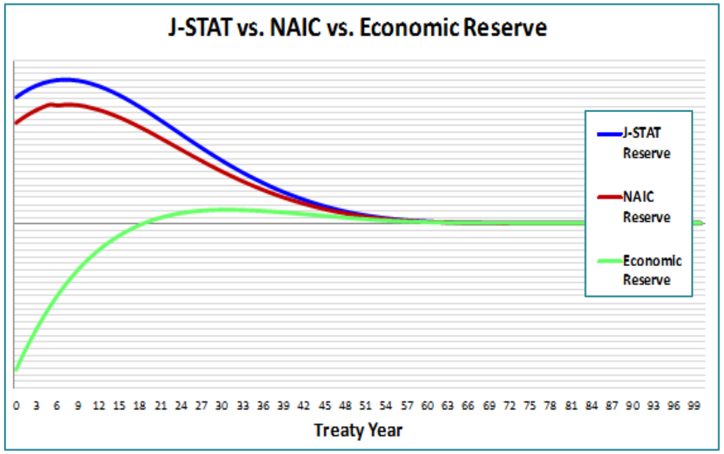
Use of reinsurance for capital purposes – Japan



Fostered capital strength allowing dividend repatriation to parent company and repurchase of common stock.

Munich Re executed a **reserve relief** transaction in **Japan**

Motivation was to **release conservative statutory reserves** from its hospital cash portfolio. **Client solvency ratio very strong -** over 500%

CEO: “We improved our capital position by entering into a new reinsurance agreement which released approximately ¥130 billion of regulatory reserves.” (1.2 billion USD)

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Transaction 4

What

Use of reinsurance for capital purposes - Singapore

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Universal Life Reserving

Surrender Value

Best Estimate

MCL

Regulations are subject to change. Our solutions allowed for the flexibility of being recaptured if it is proven to have no benefit to the client.

Reinsurance allows companies to **hold lower reserves**, e.g. Universal Life in Singapore

When **interest rates rise** or **credit spread widens**, the burden of surrender value floor is removed

Significantly **improve Capital Adequacy Ratio** when economic variables move against the insurer

Client Solvency Ratio is good now , but structure in place **to protect against future volatility**

What

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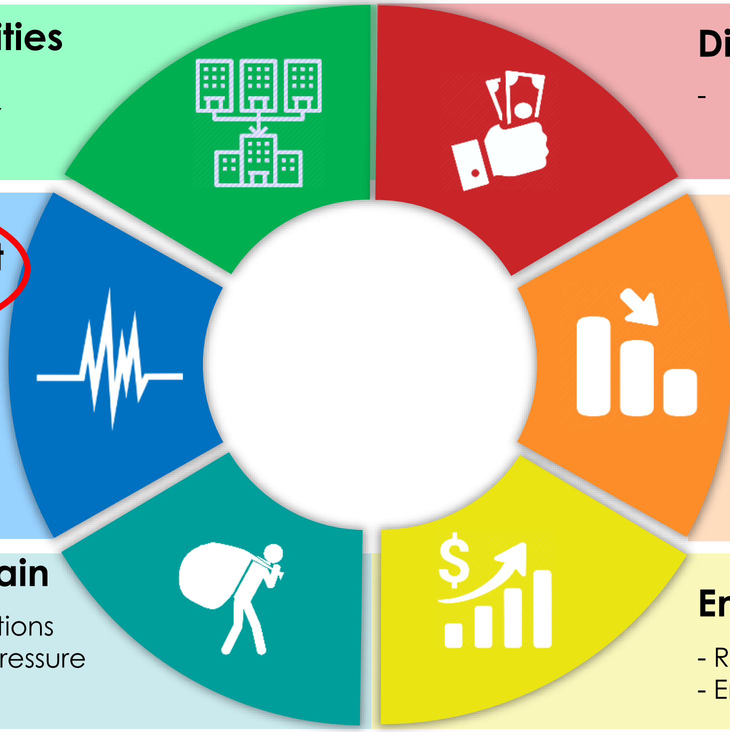

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What

Use of reinsurance for capital purposes - Malaysia

Reduce insurer's **liquidity** concerns from expenses and commissions payments in line with actual production

Enhance **product design** to benefit policyholders i.e. higher premium allocation on Unit-Linked products

Improve **return** on capital and pricing thresholds. Overall solvency strong

Transfer **cash** from reinsurer to insurance companies

Why Malaysia?

Minimum Allocation for Investment Linked Policies

Minimum proportion of premium that will need to be retained in the unit fund before deduction of any charges w.e.f. 1.1.2019

Minimum Allocation Rates:

Policy Years 1-3	60%
Policy Years 4-6	80%
Policy Years 7-10	95%
Policy Years 11+	100%

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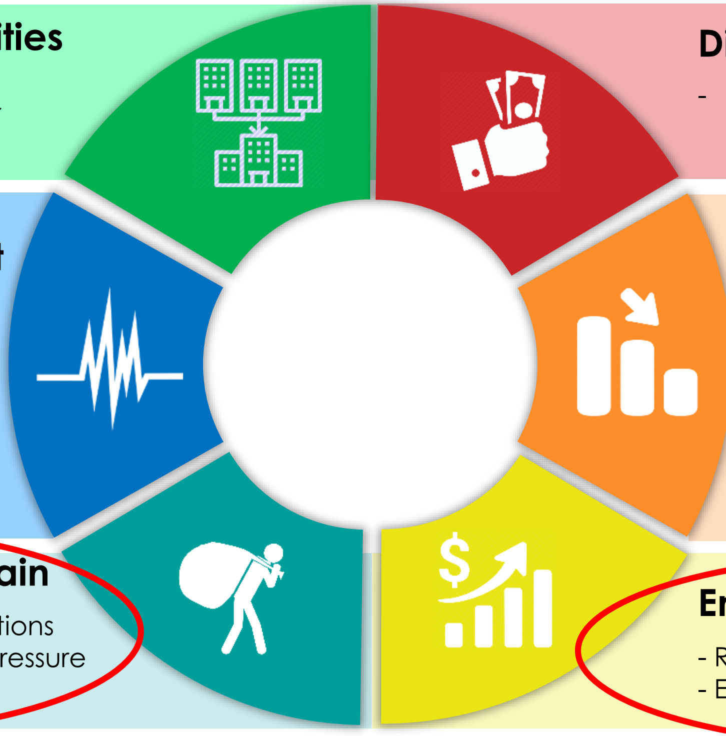

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Possible approach

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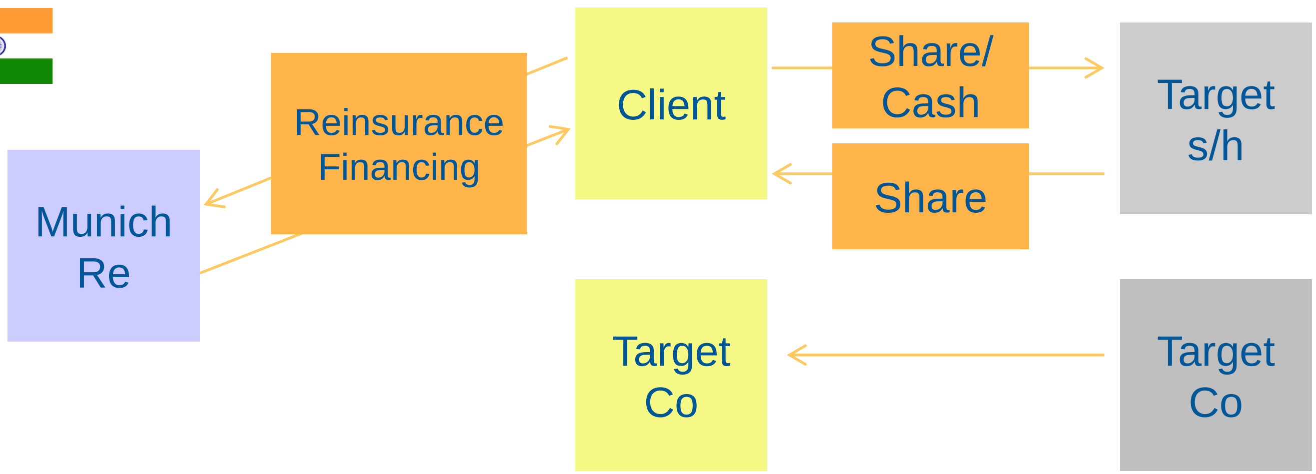
Use of reinsurance for capital purposes – India



Client wants to fund an **acquisition.** Inforce business has large negative reserves floored by zero - client **wants to release trapped value**

Coinsurance reinsurance transaction **funds the needed amount** to bid for target.

Reinsurance is a viable option to raising capital from debt or issuing stock.

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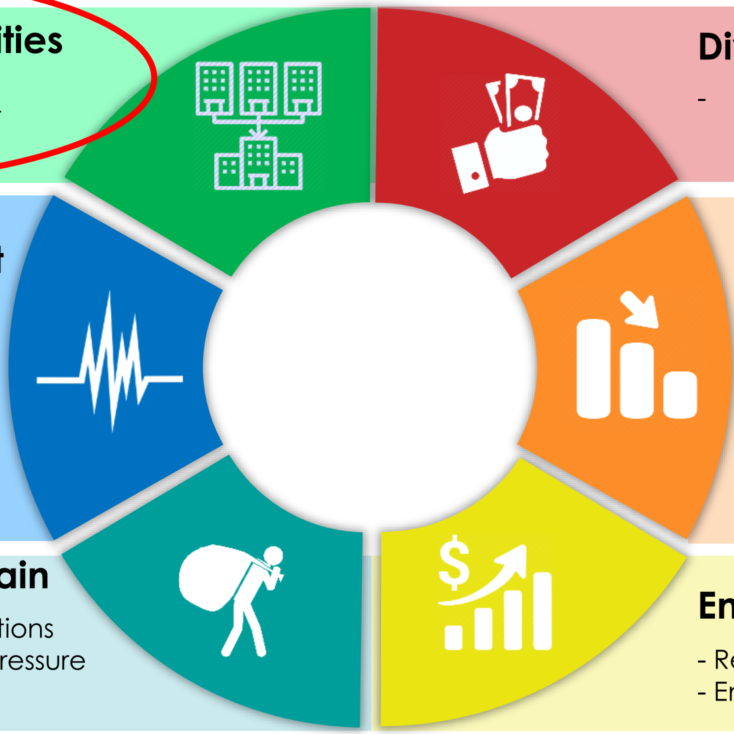

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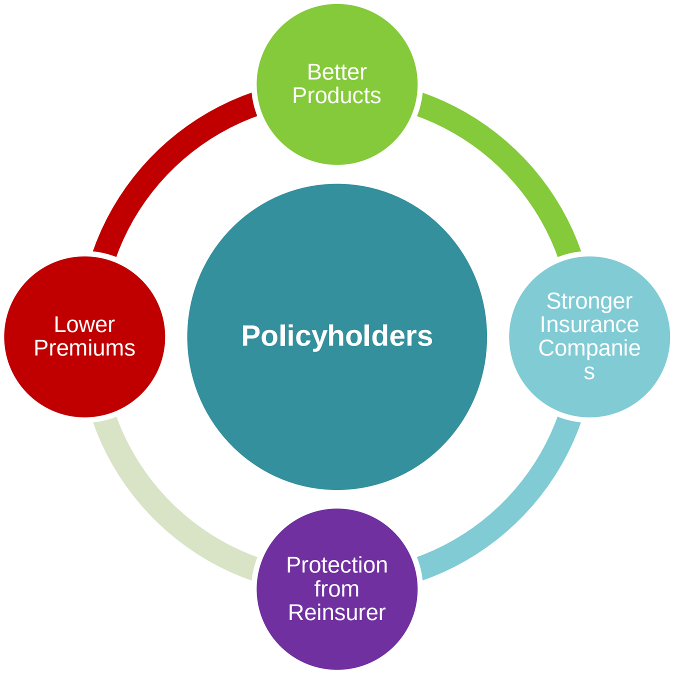

- Reinsurance used for capital purposes is **common and popular** in the region, from developed markets to emerging markets
- It is a **genuine reinsurance contract** satisfying risk transfer requirements
- Reinsurers have the **expertise and knowledge** to construct these structures – each one **custom designed** for your needs
- Benefits to policyholders include increasing **policyholder protection**, increasing **policyholder confidence** and enjoying **better products.**
- Benefits to the industry include **improving capital efficiency** and **strengthening solvency position**
- Munich Re has **global expertise** and **has successfully concluded over 65 capital transactions** across the Asian, Middle East and African markets