HOW CAN AMAN UNION MEMBERS ADDRESS AN EVOLVING REINSURANCE MARKET?

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Background

As a statement of qualifications, I should mention that I have been an export credit and political risks insurance and reinsurance broker for almost thirty years, working with specialist underwriters in the London and international insurance market. Earlier this year my previous employer was acquired by an American company who displayed no enthusiasm for the kind of business I was working on, and I was therefore at liberty to find a new home for it. I now work for RFIB Group, an London based international insurance and reinsurance broker which has three key attributes, so far as I am concerned : it is wholly owned by UK interests (the majority by its staff) and likely to remain so; it is strong in general reinsurance capability; and it has a well established Export Credit and Political risks unit. I might have added a fourth attribute, which is that it is very strong in the Middle East and the Maghreb, which account for 16% of its revenues.

So far as the private credit and political risk insurance sector is concerned, this is a relatively young class of business, and I've been lucky enough to be part of it for most of its existence. Looking back I find it curious to reflect that when I started in the business, the one of the biggest demands for Export Credit business came from sales of basic commodities to East Germany. It never occurred to us that there would come a time when the communist state of East Germany would cease to exist. When the Soviet Union collapsed I remember wondering if the new World Order would mean the end of political risk – there were a lot of so-called "experts" at the time that were predicting that sort of outcome. Fortunately (or unfortunately, depending on whether you make a living from this business) the events of the last twenty years showed greater demand for our product than ever. During that time I have worked on the reinsurance arrangements of a dozen or so Export Credit Agencies, and four Multilateral credit and political risks insurance providers, for both treaty and facultative reinsurance. This does not make me an expert – there are experts in the audience today that are better qualified than I to cover this subject and I suspect that they be qeueing up to pick holes in my remarks after I've finished – but it does make me an experienced observer of the reinsurance market.

During 2009, I was tasked to seek an export credit reinsurance treaty on behalf of an agency in the public sector, whose briefing to me included the directive that the two obvious candidates to provide it - Coface and Atradius – were not to be approached. I should mention that these two reinsurers are the most prominent in our field, not only as reinsurance providers but also as providers of expertise, training services and buyer information. This was not particularly welcome news for me because I soon realised that I was about to enter every credit reinsurance brokers nightmare – trying to place a new treaty in the middle of a Credit Crunch, and not able to speak to the market leaders. I went down the list of obvious alternatives : Swiss Re had taken the decision to come out of the business entirely (they reversed that decision a few months later, but not before they'd lost a few of their underwriting staff). Munich Re were only working with existing customers and not open to new ones. Euler Hermes do not provide reinsurance except to their own operations. There are other reinsurers in this class but mainly owned by US interests, which for reasons that will become apparent later made them unattractive.

After several weeks of having doors shut on me I did what most brokers do when the established market cannot or will not help – I went and made a new market with new people. It ended well.

What I want to do today is to draw on that experience a little and share it in discussing give some tips about how to prepare yourself for the partnership with the reinsurer. But before I do that, I want to talk a bit about the market.

The Marketplace

The subject title of this discussion talks about an evolving market. From the outside it may appear monolithic, but it is important to remember that the marketplace for credit reinsurance is constantly changing, not only in terms of participants coming into and leaving it, but also in terms of appetite and underwriting philosophy. The way I see it, there is a first division of reinsurers in this class, Atradius Re, Coface, Swiss Re and Munich Re, and of these, Atradius Re and Coface bring additional value to the process besides reinsurance, in terms of technical assistance, training, buyer information and so forth. Ranked alongside these carriers are other substantial insurers and off the top of my head I list Transatlantic Re, Axis, and. There are several new entrants in the marketplace, and this is what one tends to see in any class of business after a couple of catastrophic years : newcomers enter the marketplace to take advantage of the potential improvement in trading conditions – for example, Ariel re and (dare I say it) Catlin's new operation in Zurich, Switzerland. These are only a few examples – there are a great many insurers I haven't listed who will provide credit reinsurance. Some of these are to be found in the Lloyd's market. But most of them would not be regarded as leading reinsurers, only followers.

I will break off for a moment here and talk about Lloyd's, because I often find that the Lloyd's market is a mystery to a great many people in the industry. Lloyd's is not an insurance company, but a bourse in which insurers insure risks negotiated with them by brokers, who are acting as professional buyers and syndicators of insurance on behalf of policyholders. It has its origins in a coffeehouse 300 years ago in London – the coffee house was frequented by merchants and shipowners who used it as a meeting place to make bargains for the carriage of cargos. These men of commerce might often arrange to share the risks on a marine adventure amongst themselves, and modern insurance practise as transacted in the London market can be traced back to those early risksharing syndications practised three centuries ago. Many insurance companies run an underwriting operation in Lloyd's, because there are significant advantages in doing so : Lloyd's insurance is licensed in very many countries for example, and also, all insurers underwriting in Lloyd's share the same rating -A+

The reason it is called Lloyd's is that the coffee house where it started was run by a man called Edward Lloyd. He didn't participate in the insurance business. He made the coffee for those who did.

In Lloyd's today there are around 20 insurers that write export credit and political risks insurance; most of these are happy to reinsure risks facultatively, and there are three of four who have appetite for treaty reinsurance.

So the marketplace for credit reinsurance – both for treaties and for facultative reinsurance – is substantial, and constantly evolving. This points us to our first problem, which is how to identify who the main players are. The next problem is, which ones will make the best partners? We'll return to that later, but meanwhile, we should think a little about what is reinsurers and ceding companies expect of each other.

Basic Information for Reinsurers

Reinsurers derive benefit from working with credit insurers across the world in that it brings business to them that they would not otherwise see. This helps them balance their books : it is true that some of the original risks they are covering will aggregate, but in general the book of original business that comes their way is spread into new markets. It also gets round the problem of licensing, in countries that do not permit the original risks to be placed with nondomestic carriers. So there is a good business case for specialist reinsurers to seek out partnerships in new territories. But this does not mean they will throw caution to the wind. In every class of business, but perhaps particularly in export credit and political risks, the thing that the reinsurer examines most closely is the ceding company, and the reinsurer's focus on the ceding company does not waver during the business relationship. This is because, at the end of the day, the reinsurer's risk and reward lie in the underwriting decisions that the ceding company makes.

What the reinsurer is looking for, naturally, is a ceding company that is writing a profitable portfolio, but it is also looking for signs that it has the infrastructure - both in terms of human resources and technical processes - to keep it that way. The first thing I am usually asked to provide is a list of all the ceding company's buyers, with the limits issued, the volume of business insured, and the countries in which the buyers are domiciled.   The reinsurer will look at these as it tells him a quite a lot about how the ceding company goes about its business.

For example, an analysis of the top twenty buyers gives the reinsurer an opportunity to check whether he agrees with the limits the ceding company has issued for them, and to raise a query of he disagrees.

The amount of business actually insured under each limit will inform the reinsurer whether the limits issued are actually being used - and if there is underutilisation, the willingness of the ceding company to manage its book by reducing or cancelling unused limits.

The data can be organised to produce indicators about which risk category of country the book is exposed, the average size of buyer limit, the volume of limits insured in different bands.

The next thing the reinsurer asks to see is the claims history. I should add that all insurers expect to pay claims, and all reinsurers expect to pay claims as well.

Based on this data the reinsurer has begun to form an impression about the profile of the business that he will be sharing but there are other factors the reinsurer will examine, along with the underwriting process of the ceding company, the quality and experience of the staff that are performing that role, and the authority that each underwriter has. Also, the business plan? How are products to be marketed, which customers targeted, where will the ECA be in 5 years time? How underwriting decisions are arrived at, how they are priced, and what external sources are used to corroborate a particular decision, are of interest, but in this context there is one key advantage that each credit insurer in this room has, which perhaps could be made more of, and that is local knowledge. The credit insurance agencies that makes up the family that is the Aman Union have far greater intuitive knowledge of and easier access to information about business conditions in their territories than is available to any of the major western credit insurers. This is something I believe could be exploited far more and it's something I want to look at again a little later.

One topic I am frequently questioned about when introducing a new credit insurer to potential reinsurers is the quality of its IT: a ceding company that can produce accurate information about its overall book, in a timely manner, shows that it is in control of its business. Reinsurers often ask for information to assist them to manage their own books, or respond to a regulatory requirement. A swift and accurate response from the ceding company always impresses.

The products : credit and political risks policies the World over are generally designed to do the same thing, but there are some variations in the scope of cover offered. Furthermore, the language in which the policy is issued will, naturally, be in the language of your country. There is nothing the matter with this, but it pays to invest in accurate translations of your products into good English of your product range. As an aside, one of the benefits of working with private sector reinsurers and brokers is that it enables the ceding company to keep abreast of the latest developments in coverage and wordings.

There are a couple more topics that always come up.

The first is a point that I am almost always asked when working to secure reinsurance support for an Export Credit Agency. Many reinsurers ask about an ECA's mandate to underwrite business in the "national interest". The term "national interest" is one that private sector insurers often find un-nerving. Many of them wonder if an ECA ever comes under pressure from its own government to assume risks that they would never otherwise consider. Clearly, it is the job of every ECA to encourage and serve its exporters, but I've not seen any evidence of an ECA yielding to political pressure to accept risks that would normally be considered unacceptable from a commercial standpoint. But the frequency with which the question is asked shows that it is a topic on which some reinsurers need constant reassurance.

It is important that this audience understands the impact of sanctions legislation in the context of credit and political risks reinsurance. In order to avoid any suspicion that they may be breaking the law, a great many insurers and indeed brokers have made it company policy not to participate in risks involving country that contains persons or business that are sanctioned, regardless of what the sanctions laws actually say. This is particularly true of reinsurers with US ownership, or even with board members that are US citizens – and the majority of insurers and potential reinsurers in our class of business fall into that category. As a result, we try to work with reinsurers that are unaffected by US sanctions,

Brokers?

Should you use a broker to talk to the reinsurance markets? Naturally I need to declare an interest here - I have earned my living as a broker for almost thirty years. A great many ceding companies get along just fine without one. And it's fair to say that there is no advantage in using a broker if the broker does not bring value to the process, and equally fair to say that some brokers disappoint. But if a broker is doing his job properly, he or she will bring commercial advantage to the ceding company. A specialist commercial and political risks broker will be in a position to deploy both experience and up to date technical knowledge to the benefit of the ceding company, and should strive at each treaty renewal to enhance the reinsurance program in the ceding company's favour, build and manage the relationship between the ceding company and a wide range of reinsurers, and enhance their understanding of the ceding company's business plan and aspirations. Furthermore, a broker costs the ceding company nothing. Finally, the rules at Lloyd's require that a Lloyd's insurer is approached via an accredited Lloyd's broker.

A Collective Approach?

I was recently asked if there was a way that that Aman Union members could approach the reinsurance markets collectively. It's my belief that they can. A collective approach of ceding companies to the reinsurance market has been done before and I know of at least one scheme which is currently running.

In fact, I think that for some members of the Aman Union, being part of a collective approach is the only way they are going to be able to tap into a decent reinsurance program. The reason for this is quite simply that for several of the Aman Union's members, the reinsurance income they would yield individually to the market is too small to be interesting to reinsurers. In this connection we need to understand that credit reinsurance treaties can be complicated and are always service intensive, so a treaty with small premium volume is costly to administer and unprofitable for reinsurers to underwrite and service. The other problem is that although some Aman Union members have a long and distinguished track record in the business, having been established for many years, and represent some of the Union's more advanced economies, other member insurers are small and comparatively recently established and lacking in experience - these agencies do not just need reinsurers, but technical assistance and perhaps even training. But without reinsurance, it is very hard for some of these smaller agencies to grow. But a collective approach would bring premium volume, spread of risk, to the process and if properly administered there would be significant savings in the cost of servicing.

I went to some lengths to explain the considerations that the conventional reinsurance community take into account when considering a new ceding company. My own experience is that sometimes it is very hard to break the ice with reinsurers in introducing new ceding companies. Too often it's easy to forget that both reinsurer and ceding company are in the same business. I heard it suggested that if the members created a pooling arrangement among themselves, whereby each member ECA were to participate in the reinsurance of all the other members, then each ECA would have access to at least some reinsurance from the other. I suppose the only good thing about this idea is that it certainly delivers the fraternity that the Aman Union hopes to symbolise, but it is hard to see how it could work in practise: the obvious objection being that the shareholders of each ECA - many of them being the taxpayer - would be expected to reinsure the business of the exporters of a competing country.

But if we stay with the notion of fraternity for a moment, and recall that each ECA member of the Aman Union is also a member of either ICIEC or Dhaman or indeed both, then maybe ICIEC and Dhaman have a role to play. As I understand it, the Aman Union was not set up to be a talking shop, but to provide robust and useful benefits to its members. And if you look at the charter's list of twelve objectives for the Union, the word "reinsurance" appears in no less than five of them. And since it is my understanding that several of the Union's members are already reinsured to some extent by either ICIEC or Dhaman, then surely that function can be consolidated into a scheme that takes advantage of ICIEC and Dhaman's existing reinsurance relationships.

It wouldn't be difficult to create a reinsurance facility, underwritten jointly by ICIEC and Dhaman, which would accept treaty business from Aman Union members. This "Aman Union ReInsurance Facility" could then negotiate its own reinsurance into the reinsurance markets, where they have many relationships with potential reinsurers.

I should say right away that I have no idea if all Aman Union members would be eligible for reinsurance by, for example, Dhaman. I suspect that a great many other issues will crop up. For example, some of the ECAs that might cede to an arrangement of this sort might be viewed as less developed than others, and if there isn't a good mix in the portfolio, then perhaps it will not be such a good proposition for the facility's reinsurers - so some participation by the more established agencies might be desirable to balance the portfolio. Another question that I think might arise would be whether or not all of the participating ceding companies would need to standardise their products and I think the answer to that is “No” – in fact, one would hope that each participating ECA would continue to develop its products in the way that serves its customer base best.

Tomorrow we will hear more about the Aman Union Credit Information Database, which I believe is one of the most important initiatives in our industry. It is critically important for the Aman Union's members, because it will crystallise and make accessible the single most important characteristic that each member of the Aman Union has to offer. I mentioned it earlier : local knowledge, knowledge of the business and political environment, and knowledge of the buyers that you are insuring. What is frequently commonplace information to the members of the Aman Union is simply unavailable to many in the industry in Europe. And I think the success of any collective approach by Aman Union members to the reinsurance markets would greatly enhanced by the creation of this Information Database.