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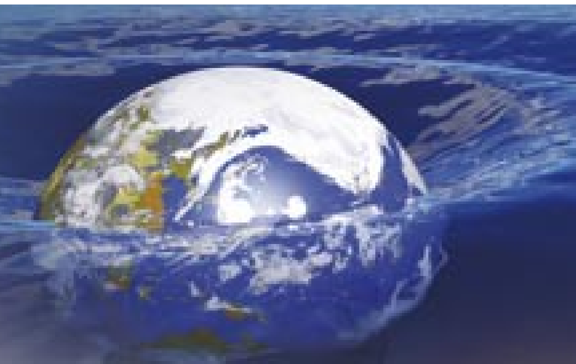
Global Warming Sends Shockwaves of Warning



Justifying climate change and its long-term effects on the insurance industry is no easy task. As insurers look at future risks, climate change trumps as a risk which requires proactive approaches, and also poses as a business opportunity.

"Our planet is catching a fever," said **Mr Werner Bugl**, Director for Strategic Business Development at Asia Capital Reinsurance Group, observing that up to 60%-70% of cat losses in mature markets are insured, compared with 3% of cat losses in Asia. "Emerging threats are a part of our future."

A Controversial Issue

Highlighting the importance of the climate change debate, **Mr David Priebe**, Chairman of Global Client Development at Guy Carpenter, said: "Climate change remains a controversial issue, without a resolution… Ambiguity reigns supreme, and hard answers will take time – if they are ever determined."

In his observation of the reinsurance market, there are three basic camps in the debate. One group believes that climate change "does not exist", the second considers the industry "powerless to change it", and the last category adamant that "we can make a difference to mitigate it."

Taking the proactive approach to the issue, **Mr Scott Ryrie**, CEO of Allianz SE Reinsurance Branch, Asia Pacific, set the tone by citing a United Nations report which projects that by 2050, 100 million people will be displaced as environmental refuges because of rising sea levels. Particularly with urbanisation, more people are living in coastal areas. Asia, with a large majority of people in this category, faces strong catastrophe exposures.

He pointed to events such as Hong Kong's black, or torrential rain, which forced the closure of schools and many public facilities in June this year, while Indonesia's capital, the so-called "Sinking Jakarta" could be submerged by 2025, according to reports.

So, what can be done about this? Mr Ryrie applauded the Taipei government for implementing Flood Diversity Projects which has cost NT$6 billion (US$180 million), so far, which aims to mitigate flood damage in parts of cat-prone, Taiwan. In addition, the use of disaster mitigation construction, warning systems and SMS alerts have been praised as positive tools to saving lives.

Are Weather-related Events Increasing?

Giving a non-insurance perspective to climate change, **Professor Johnny Chan**, Chair Professor of Applied Physics at the City University of Hong Kong, defused the "common myths" on how the world's atmosphere is changing, and discussed whether global warming is to be blamed for the increase of typhoons in the region.

From his research, he asserted that since 1960, the statistics do not indicate that weather-related events are increasing in number and severity. Rather, it is a cyclical trend, in patterns of 10, 20, or 30 years. He said that people are quick to point the finger at global warming, however, "correlation does not mean causality."

Mr Prawit Thongtanakul, Chief Operating Officer of the Thai Reinsurance Public Co, noted that in 25 years, Thailand may struggle with a higher average temperature increase of 0.75 to 1.5 degrees Celsius. This increase will have "quite a lot" of impact, particularly as rising sea levels could submerge some parts of Thailand in the next 10 years. As 60% of Thais are involved in the agriculture sector, any change

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(From Left to Right): Prof Johnny Chan, Mr David Priebe, Mr Sivam Subramaniam, Mr Werner Bugl, Mr Katsunobu Hayashi, Mr Scott Ryrie and Mr Prawit Thongtanakul

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in weather patterns could strongly affect farmers and create loss of wealth that can have detrimental effects on the overall economy.

Business Opportunities

Mr Katsunobu Hayashi, Treasurer, MSI Guaranteed Weather, said that climate change should be viewed as a business opportunity, as it can "generate additional profits, [and]… help clients build a portfolio which is stablised against climate change." He added that this is an opportunity to launch a clean energy fund and clean energy projects.

Mr Bugl agreed that the industry can develop new products and expand its business, and proposed an Asian Cat Pool to create a supra-regional platform for cat risk aggregation and management pool for the region.

While the debate over climate change continues, it is undoubted, however, that the industry needs to build a sustainable yet progressive strategy in tackling the effects of climate change.

QUIZ

To tease regulars and faithful attendees of the EAIC, here's a little quiz on EAIC trivia. The first five delegates to present the correct answers at the *Asia Insurance Review* booth will receive a complimentary CD-Rom containing all the articles published by *Asia Insurance Review* in 2007, worth US$280.

1. **Who is the Secretary General of the EAIC Secretariat?**
2. **Where is the official headquarters of the EAIC?**
3. **Who initiated the idea of the EAIC?**
4. **When was the last time Indonesia, the next host of the EAIC, hosted the gathering?**
5. **According to Swiss Re, what is the estimated size of the motor insurance market in Asia in 10 years' time?**

Political Risk Insurance:
A "Mission Possible"

At yesterday's forum, it was clear that while markets view political and terrorism risks differently, pricing and conditions should be risk-adequate.

Is political risk insurance a mission impossible? "Clearly no," said **Dr Ludger Arnoldussen**, Board Member, Munich Re. The same goes for terrorism risks, at least from enterprise management drive's standpoint, said **Mr Victor Peignet**, CEO, SCOR Global P&C. "These risks are dangerous, and they are extremely serious in our industry, but they are manageable and insurable."

Dr Ludger Arnoldussen

Mr Victor Peignet

But there are some problems in dealing with political risk, such as what it is exactly and the authority to decide whether or not a loss event has occurred, said Dr Arnoldussen. High accumulation of risks on country basis can easily arise, and loss expectations are imprecise because of the lack of data.

What makes political risk even tougher to handle is that it is continuously getting harder to predict, said **Mr CT Juang**, President, Central Reinsurance Corporation.

Mr C T Juang

A Universal Risk

Although there is no common definition, political risk is universal. It is "about risks that potentially impact business life as a whole," said Dr Arnoldussen.

"Taxes, customs duties, regulation and legislation – national and supranational orders and agreements – set the economic framework within which we all operate," he said, adding that these frameworks are not uniformly stable and may change or even fail.

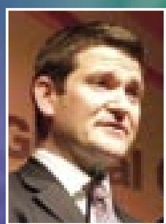
(From Left to Right): Mr David James, Dr Ludger Arnoldussen, Mr Kornelius Simanjuntak, Mr C T Juang, Mr Victor Peignet and Mr Brian O' Brien

Not a Real Threat

Though some markets consider terrorism and political risks as real threats, some do not. In Taiwan for example, Mr Juang said that such risks are not a real threat. "The risk grades of Taiwan and China were classes 1 and 2, respectively – low-risk grades," he observed, citing OECD's country risks classification report.

Likewise, the South Korean market does not view terrorism risk as a threat, hence the low demand for terrorism cover. "There is exposure, but it is not extreme," said **Mr Brian O' Brien**, Executive Vice President, Reinsurance & Innovation Dept, Samsung Fire & Marine Insurance.

Mr Brian O' Brien



Mr David James

Nonetheless, the terrorism market has developed exponentially in the last five years, and there is now global demand for terrorism insurance, both in OECD and non-OECD countries, said **Mr David James**, Senior Underwriter, Terrorism & Political Risk, Ascot Underwriting Limited.

Demands from Insurers

Given the specialist nature of this segment, successful underwriting of political risks calls for highly specialised teams with deep knowledge and experience of underwriting and claims handling of these risks, said Dr Arnoldussen. Accumulation control and regional diversification are also crucial.

Pricing Matters

Pricing terrorism and political risks requires insurers to consider the objective risk factors such as aggregation and what risk they can take, said Mr James. It also needs them to look at subjective factors such as what they think is going to happen. Though difficult, insurers must also do technical pricing, and should also benchmark inside and outside the market.

The Asian Practice

Some markets in Asia tend to accept political risks under standard insurance covers without imposing additional premium. There should be risk-adequate prices and conditions, said Dr Arnoldussen. "Political risks cannot be covered under standard policies."

再见 香港 (Goodbye Hong Kong, Welcome to Bali)

Before we bid farewell to the bright neon lights of Hong Kong, we look at the next venue for the EAIC in 2010 – Bali, the largest tourist destination in Indonesia, which is renowned for its highly developed arts, including dance, sculpture, painting, and music.

Speaking to the EAIC Daily, **Mr Teddy Hailamsah**, Chairman of the 25th EAIC, said that the conference will be specially timed so that the member cities can celebrate Insurance Day on 18 October and then delegates can make their way to the island for the EAIC. The Congress will tentatively be held between 18 and 23 October, in the Bali Convention Centre which can cater to more than 2,000 delegates.

Regarding the choice, Mr Hailamsah said: "Many have said that they prefer Bali to Jakarta. Personally, I also feel that many delegates would find Bali attractive and it is a more appropriate venue choice. After all, the EAIC is for the participants, so we will give them what they want."

He added that after discussing with the Hong Kong Federation of Insurers, the Indonesian organisers like the idea of having a small organising team and outsourcing some of the planning preparations as it provides more efficiency. The organising committee may adopt this system depending on the result of discussions with the industry.

"A pre-organising committee has already been set up in Jakarta. However, the number of members we have is quite large at this moment. If we do outsource, we still want to ask all the pre-organising committee members to participate in meetings and share ideas at the initial planning stage."

The committee, he added, is still having discussions over an appropriate theme and will take the volatile market into consideration before deciding.

Mr Hailamsah hopes to incorporate a regulator meeting at the 25th EAIC with all the 15 insurance commissioners from the East Asian countries, as well as the Asean countries that are not part of the EAIC, namely, Myanmar, Laos, Cambodia and Vietnam. He also has great plans to put together an EAIC video that will feature all the 11 cities in their different languages.

On behalf of all delegates, *Asia Insurance Review* would like to thank our gracious Hong Kong hosts for their warm hospitality and for making this an EAIC to remember. See you in Bali!

(L-R) Messrs Teddy Hailamsah and Frans Sahusilawane, members of the 25th EAIC organising committee

Pension Assets in Asia Pacific

BY THE NUMBERS

In 2007, Asia-Pacific Sovereign Pension Funds* (SPFs) grew by around 20% to US$1.8trillion, boosted by strong equity returns.

The SPFs of Japan, S Korea and Taiwan are among the region's largest.

*SPFs are managed by state authorities to meet pension payments and are financed either by individual contributions or government funds.

By 2017, the highest profit margins in the life and pensions business will be found outside mature markets.

Margins in China, India, Southeast Asia and Brazil are forecast to be 8%.

In most western markets, margins will be most likely around 5%.

Australia's Future Fund is the *fastest growing* SPF and has assets of US$44billion at the start of 2008.

Sources: Watson Wyatt, Booz & Co

In Asia ex-Japan, China's National Social Security Fund, India's Employees Provident Fund, Singapore's Central Provident Fund & Thailand's Government Pension Fund

grew more than 30% from the previous year.

In 2007, total assets of the world's largest 300 pension funds grew by over 14% to around US$12trillion.

Performing Under Pressure

Mr Patrick Liedtke, Secretary General and Managing Director of The Geneva Association, compares the insurance industry's response with that of other financial institutions to the credit crisis, in this extract of an article which first appeared on the Association's website.

At this stage, it is not easy to draw conclusions about the credit crisis because its end has not yet fully materialised, the impact of the recession in many countries is unknown, and further rounds of corrections are possible. What makes the analysis so demanding and complex is the fact that it is composed of three different elements:

- The original liquidity problems that affected the banking sector so much and provoked an acute systemic threat;
- The impact of expected credit losses from subprime mortgages on financial institutions with specific exposures such as credit derivative swaps (CDSs) and mortgage-backed securities; and
- The general impact of the asset meltdown which has accelerated dramatically since September 2008.

Still Holding Up

Most insurers have escaped the first two adverse effects largely unscathed even though they are major players in the financial markets. This is no small achievement. While interbank lending for a short time came almost to a halt in some regions, like the EU, the insurance industry continued to do business. While banks and many other financial institutions stopped trusting their peers and restricted counterparty interaction to a minimum, the insurance industry continued to share risks on a normal level. So far, we have not learnt of any major impairment in the ability of insurance companies to obtain reinsurance or problems between reinsurers and their retrocessionaires. Whereas many businesses have been complaining that their access to bank liquidity was severely impaired and that lending did not take place, no wave of complaints as to the functioning of real insurance markets has appeared. Insurers and their clients have been able to organise the transfer of risks in an orderly fashion and emergency government action has not been required.

While insurers operating in traditional ways have escaped the adverse effects described above, this cannot be said of all large complex financial institutions that conduct insurance. The kind of impact observed at some financial institutions where the core insurance business was complemented by other financial services activities or where insurance is part of other financial operations has been ruinous indeed. Most prominently, AIG and Fortis reported massive losses occurring on financial products and banking activities, and ultimately had to be saved through government intervention. Interestingly enough, their insurance operations have repeatedly been reported as sound by the supervisory authorities, whose stringent controls of insurance activities apparently lead to more careful risk management. In the case of AIG, the ability to service government debts and the losses incurred by the business unit that conducted financial guarantee business depended heavily on the soundness and continued operation of the insurance part of the company.

The Formula for Staying Strong...So Far

The main reason for this remarkable resistance of the insurance operators to the first two threats has been a combination of the resilience of the insurance business model when it comes to liquidity constraints and prudence by most operators. The already tight supervision of insurance operations played a positive role too. However, this does not mean that insurance companies are able to escape the generally negative developments of major asset classes. If the world economy were to fall into a prolonged and deep recession, the consequences for insurance could be dire indeed. Already the severe asset meltdown to date has affected the insurance industry in a very negative way.

What is interesting to note, however, is the limited involvement of the insurance sector in the credit crisis itself. The handful of companies that have suffered badly as a consequence of the credit crisis are mostly those that had special operations as financial guarantors. In this sense, they did not operate as insurance companies, but as owners of and investors in a different type of business. This is where regulators and supervisors should be alert in the future: insurance companies branching out into risky ventures or other riskier players (such as banks or financial guarantors) moving into insurance, creating possible transmission mechanisms previously unnoticed.

Insurers Are Not Banks

Insurers have not been submitted to the same systemic issues that many banks are facing today. Nor have they contributed to global financial instability. On the contrary, the insurance industry displayed resilience in the face of adverse market conditions and was in a position to absorb market volatility. It is important to note that the credit crisis does not question the business model of insurers. There is no shortage of cover for life or non-life insurance. Capacity appears to be ample and, with the exception of D&O and E&O insurance, prices in most lines of business continue to be under downward rather than upward pressure.

Regardless of how a recession scenario might play out, there is one important lesson to be drawn from the credit crisis so far: insurers are markedly different from banks and that their distinct business models expose them to lesser risks in the liquidity domain. This must be reflected in different regulation and capital requirements for both industries in the future.

3rd MENA CEO Insurance Summit

Tunis, 2 - 4 March 2009

Theme: Managing Challenges of Insurance in North Africa at the Crossroads of the Middle East Boom

Register by 30 Jan 2009 for Early Bird Discounts!

A Must-Attend Event for CEOs & Leaders!

Modelled along the successful and well-established Asian CEO Summit, the 3rd MENA CEO Summit will offer a serious two-day intensive platform for interaction, exchange of ideas, learning and finding common solutions to current challenges as well as boosting greater interaction and co-operation between the Middle East insurers and reinsurers and their counterparts in North Africa. It will also be a platform to set standards and boost professionalism in the MENA region, while identifying solutions to nurture the growth of the region's nascent insurance markets – a particular management challenge at a time of crisis of confidence in the global financial services sector.

Its regional focus notwithstanding, the Summit will also serve to project the right image and profile of the MENA markets internationally at a time of impending recession. It will be an interactive forum with Q&As and Panel discussions with active inputs from delegates.

Who Should Attend

- CEOs & Senior Management of Insurance & Reinsurance Companies (Life & Non-Life) from MENA, Asia & International markets
- Insurance & Reinsurance Brokers
- Supervisors & Regulators
- Management Consultants
- Risk Managers
- Lawyers, Technology Experts, Loss Adjusters, & Other Service Providers to the Insurance Industry
- Banks, & Financial Institutions Serving the Insurance Industry.

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For Full Programme and to Register online, please visit **www.meinsurancereview.com**

Quick Takes

On the sidelines of the EAIC, reinsurers and brokers commented on their expectations for the upcoming renewals, globally and in Asia.

"With the large claims in China, there definitely needs to be a change in underwriting perspective. I am looking forward to discipline returning to the market. Stability, of course, is necessary but discipline is very important."

Mr Funai Yasuhiro
Managing Director of Sompo Japan Re

"Globally, rates are firming; they will vary from region to region starting with the US, Europe and Japan. In emerging markets such as the Middle East, I am less optimistic about higher rates as there are too many companies chasing the business. As we go deeper into next year, rates will increase on international programmes. At year-end, there will be a recognition of losses on the asset side, and companies will rely less on investment income. The general firming will go through the insurance markets."

Mr Hans-Peter Gerhardt
Director, Paris Re Asia Pacific

"We are trying to promote the level of specialism in the market, looking at areas such as credit and political risks, and making important hires in those areas. We will be focusing on these areas, which have less competition, in the upcoming renewals."

Mr Roger Bickmore
Group Business Development Director, Kiln Group

"The financial climate is creating interesting opportunities. Competition will always be intense, so Kiln in Asia is looking to concentrate on more specialist classes."

Mr Keith Land
CEO, Kiln Group

"The renewal will involve a serious consideration on the part of our clients. They need, as much as we need, proper pricing – which they have to consider very seriously in the coming renewal dialogues. Profitability of insurers will be a key financial concern in these dialogues."

Mr Victor Peignet
CEO, SCOR Global P&C

"A large part of the market is underpriced and we are looking for improvements. We don't see many changes in Southeast Asia where there is limited cat exposure, but we feel the hard market is setting in for large capacity countries more exposed to nat cats, namely, China and Japan. We see clients getting concerned over whether they can achieve the capacities they require.

On a worldwide scale, there is certainly a hardening of terms visible. The reaction of reinsurers seem to be that capacity is directed to those markets that offer best returns for the capacities extended, especially US windstorm rates which seem to be very attractive to global players. We hope that there will be similar effects in Asia in order to improve the concerning situation that it's sometimes very difficult to achieve profitable bottom lines for risks taken in certain territories and lines of businesses."

Mr Andreas Weidlich
General Manager, Reinsurance, Arig

"Prices have to go up, and I am confident that this will occur as it is all part of macroeconomics. I also think that 2009 will be much more interesting than the forthcoming 1/1 renewals. However, I foresee that some reinsurers, especially the Bermudians, may receive more bad news."

Dr Christoph Lamby
Member of the Board of Management of R+V Versicherung AG

"In the US, it is common for rates to fluctuate following cat losses. It would be curious to see how the Chinese market responds (to nat cats) as it does not have the same level of experience in dealing with such losses, as compared to the US and other markets.

Underwriters need to assume riskas though it were their own personal money they were exposing, not just as an employee of a company. The more they do this, the more they'll be encouraged to charge the appropriate price for the risks they take, and be more selective with whom they want to take these risks."

Mr James Giordano
Chief Underwriting Officer, Canopius

"We will see price increases in capital-driven business lines, for example, US-exposed property retrocession, US reinsurance in peak zones and classes of business where loss ratios are deteriorating, such as German motor, global credit reinsurance and energy. Capacity in correlating businesses will be tight. Intriguingly, while capacity is tight, in many countries, additional reinsurance purchasing will be seen. This may be especially true in parts of the US and Europe.

Asia, as always, does not wholly follow other regional or global trends. The focus of attention is on China, given the two significant events we've witnessed. In other territories, I doubt we will see the level of deductions we saw last year, not least because the cost of capital has increased. No doubt, rate attention will be given to the applicability of the perceived increased cost of capital to the Asian region."

Mr Dominic Christian
CEO, International Division, Benfield

"I foresee significant hardening, especially for the treaty business. We are already seeing hardening on our energy accounts and expecting the property market to harden as well. For one of our energy contracts, the rate was increased by 30%, and there is potential for this to rise across the board for anything off the Gulf of Mexico."

Mr Rupert Atkin
Chief Executive, Talbot Underwriting

Luncheon of the EAIC Party

Like the characters of the similarly-titled Renoir painting, many were seen relaxing over Tuesday's lunch at the Hong Kong Convention and Exhibition Centre.

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