Navigating reinsurance strategies

Identifying and responding to key trends

Offshore reinsurance trends and regulatory changes

The reinsurance market in Bermuda and the Cayman Islands is experiencing significant growth, driven by the increasing popularity of sidecar models and the expansion into new lines of business. Sidecar models, which allow reinsurers to bring in third-party capital to support a wider range of risks, are becoming more prevalent. These structures provide reinsurers with additional capacity and diversification benefits, while also giving investors the opportunity to participate in the reinsurance market.

These trends are occurring against a backdrop of regulatory changes. Bermuda has recently strengthened its regulatory regime to enable a more robust, risk-sensitive capital regime, which has resulted in increased reporting and governance requirements for reinsurers. Meanwhile, the Cayman Islands is seeking to attract more reinsurance business from the United States by pursuing National Association of Insurance Commissioners qualification.

> **“For offshoring, the first step is to do a feasibility study to look at why it makes strategic and financial sense for you to set up offshore, what are the operational implications, and how different jurisdictions compare.”**
>
> Anam Khan, Partner, KPMG in Bermuda

While this would provide reinsurers with a more flexible regulatory framework, particularly for affiliated reinsurance transactions, it also requires them to navigate a complex web of their cedants’ state-level regulations as well as their own regulations and reporting requirements. These regulatory changes can create challenges for reinsurers, particularly when it comes to ensuring that all stakeholders are aligned around the intent and objectives of the transaction.

The growth of asset-intensive life reinsurance

Asset-intensive life reinsurance has become a significant driver of growth in reinsurance markets in recent years. These transactions involve the transfer of long-term life and annuity liabilities, along with the associated assets, from a ceding insurer to a reinsurer. This allows the ceding insurer to free up capital and improve its risk profile, while providing the reinsurer with a stable stream of income and the opportunity to generate attractive returns.

There has been a shift in the approach to these transactions, from liability-driven to asset-driven. In the past, reinsurers would typically assume a block of liabilities and then construct an asset portfolio to match those liabilities. However, more recently, reinsurers have been starting with a portfolio of assets and then seeking out liabilities that match those assets. This shift has been driven in part by the low-interest-rate environment, which has made it more challenging for reinsurers to generate attractive returns on traditional fixed-income investments.

By starting with a portfolio of higher-yielding assets, such as private credit, reinsurers can potentially generate better returns and improve their overall profitability. However, this approach also introduces new risks and challenges related to the valuation and risk management of these assets. Reinsurers need to have robust processes in place to ensure accurate valuation and effective risk mitigation.

The changing environment for deals

The reinsurance deal environment has been impacted by recent changes in interest rates and economic uncertainty. While rising interest rates can potentially improve the profitability of asset-intensive life reinsurance transactions, they also introduce new risks and challenges. Higher interest rates can lead to increased lapses and surrenders on life and annuity policies, as policyholders seek out higher-yielding investment opportunities. This can impact the profitability of reinsurance transactions and require reinsurers to adjust their pricing and risk management strategies accordingly.

> **When you go from deal modeling to valuation, something always comes up. The everlasting challenge is in the depth and sophistication of the valuation model."**
>
> Tom Kelly, Partner, KPMG LLP (US)

Economic uncertainty, driven by factors such as inflation and geopolitical risks, can also impact the deal environment. Reinsurers may become more cautious in their pricing and risk selection, leading to a slowdown in deal activity or a shift towards smaller, more targeted transactions. In this environment, it is critical for reinsurers to have a clear understanding of their risk appetite and to maintain discipline in their pricing and underwriting. They also need to have strong relationships with ceding insurers and other counterparties, to ensure that they can source attractive deals and manage the associated risks effectively.

Data privacy and security in cross-border reinsurance transactions

Data privacy and security in cross-border reinsurance transactions, especially when it comes to personally identifiable information (PII), is a significant challenge. It can be difficult for reinsurers to identify and manage PII according to varying definitions across jurisdictions. It gets even more complicated in multijurisdictional transactions, where different countries may have their own specific rules and regulations regarding data protection. Reinsurers must take care to limit the receipt of PII wherever possible and ensure the security of sensitive data.

Reinsurers must have robust data management strategies and work closely with their legal and compliance teams to ensure regulatory compliance. This may involve implementing strict access controls, regularly training employees on data privacy and security protocols, and having clear procedures in place for responding to potential data breaches. As the reinsurance industry becomes increasingly global and data-driven, managing risks will be critical to the success of cross-border transactions and maintaining the trust of regulators and counterparties. Reinsurers that can adapt to these changes and maintain a disciplined approach to pricing and risk management will be well-positioned to capitalize on emerging opportunities.

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