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Current Developments in Insurance Risk Securitization Markets

Simon Harris

Agenda

- Insurance Securitisations
 - Why and Where Next?
 - Barriers to Growth
- Moody's approach to evaluating Insurance Linked Notes :
Focus on Life Insurance
 - How we rate insurance-linked notes
 - Assessing the impact on Insurers' Ratings
- What the markets/investors think



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Securitisations – Why....

- Banking Industry is extensive user of securitisation technology
- The rationale for Insurance Securitisations continues to evolve over time....
 - Several key themes have historically been prevalent
 - We expect that Risk Transfer will become increasingly key
- Non-life and Life Cat securitisations have been and will continue to be focussed on risk transfer

Significant Life Insurance VIF deals

Year	Sponsor	Deal Name	Country	Rationale for deal
1998	NPI Ltd	Mutual Securitisation	UK	Capital Raising
2003	Friends Provident	Box Hill Finance	UK	Regulatory Improvement
2004/5	Various	Various	US	Regulatory Improvement
2006	Aviva plc		UK	Cash flow financing
2007	Bank of Ireland	Avondale Securities SA	Ireland	Regulatory Improvement



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.....and where next

- Increasingly, Insurance securitisation is likely to focus on Risk Transfer. Drivers for this
 - Solvency II
 - Risk Mitigation as a substitute to Capitalisation
 - Reduced rationale for regulatory arbitrage
 - Risk Management Techniques
 - Along with Solvency II, many Groups now have a stronger focus on holistic risk management
 - Balance sheet management
 - 'Accelerating the Balance Sheet'

“Going forwards VIF Securitisations are set to be more a part of Balance Sheet / Risk Management Toolbox”



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Insurance Securitisations – Barriers to Growth

- Insurance securitisation barriers
 - Lack of high quality, homogeneous data for many life insurance products
 - Investor concerns over insurance as an asset class
 - Cost relative to other Balance Sheet mechanisms
 - Insurer conservatism on often complex financing structures

“Complexity, cost and investor conservatism
remain hurdles to growth”



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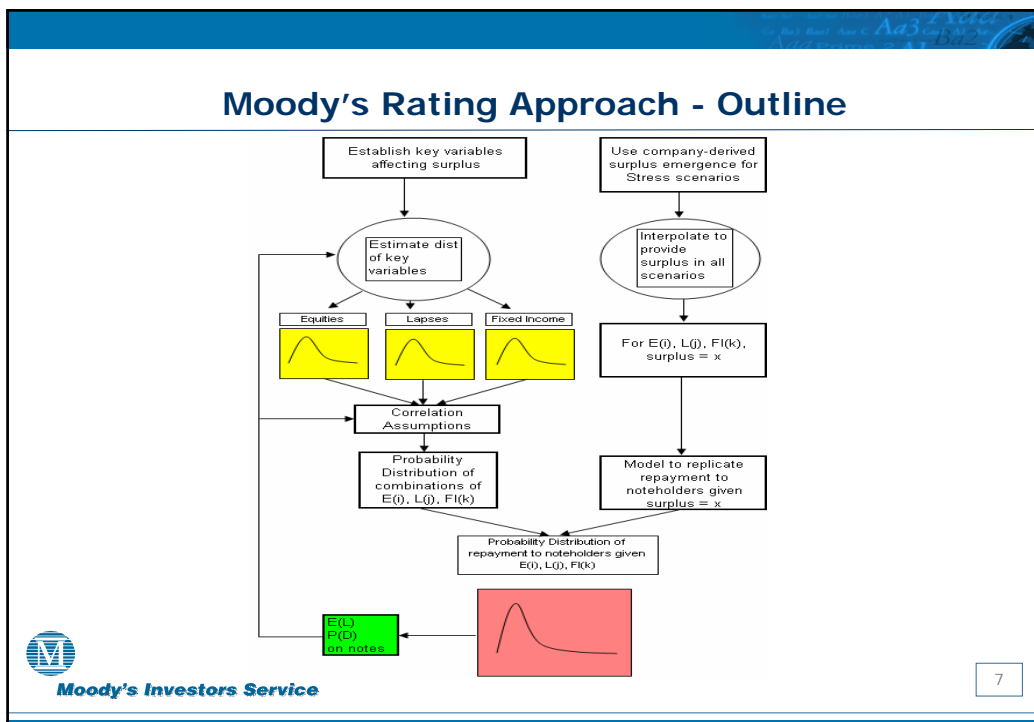
Rating Life Securitisation Notes

- A combined application of insurance, actuarial and structured finance techniques
- Moody's has developed an in-house stochastic modelling approach simulating possible returns from a securitised block
 - 'Building block' approach allows flexibility of approach whilst ensuring consistency of application
- Rating committee considers outputs on the basis of E(L) / P(D) on note structure
- No definitive set of assumptions
 - Rating committee will consider outputs using a number of different sets of assumptions
- Depending on transaction structure, rating may be constrained by Sponsor debt rating



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- ### Rating Life Securitisation Notes – Key Committee Discussion Points
- Sensitivity of E(L) and P(D) to key parameters
 - Structural Elements that can distort results eg
 - Sponsor ability to weaken surplus emergence
 - Changes to waterfall payments as structure matures
 - Effect of any positive (warranties, support mechanisms) or negative linkages to sponsor
 - Regulatory treatment of securitisation structure
 - Impact of Financial Guarantee
- Moody's Investors Service**

Life Securitisations – The Impact on IFSR

- IFSR reflects ‘security of policyholders’ claim’
- Impact of a securitisation on IFSR a function of
 - Materiality (size of deal relative to insurer)
 - Type of risks securitised
 - Use of proceeds
 - Treatment of associated debt securities (Operating vs Financial Leverage)

“Operating Leverage treatment requires

- A) Effective risk transfer
- B) No sponsor recourse”



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Potential Impact of Securitisation on Life Rating Metrics

Characteristic	Directional	Potential influence	% weight in overall rating
Market position	N/A	N/A	15%
Distribution	N/A	N/A	10%
Product risk	↑	Elimination of risk relating to ‘high risk’ products could allow re-categorisation of these products	15%
Asset quality	↑	If securitisation restricted the downside exposure to assets which Moody’s considers as “high risk”, these assets could potentially be re-classified.	5%
Capital adequacy	↑	Impact on economic or regulatory capital position would be expected to be positive; however this will only be reflected to the degree that Moody’s views this as permanent.	10%
Profitability	↓	Likely to deteriorate as part of the previously emerging profit pool is now diverted to repay securitisation notes and the deployment of proceeds may not replace these earnings immediately	15%
Liquidity & ALM	↑	Improved due to the liquidation of an intangible asset and well established ALM capabilities would most likely be demonstrated during the securitisation process.	10%
Financial flexibility	↔	Expect most to be structured along operating leverage principles. Change in the composition of a company’s business mix, as well as the impact on prospective cash flows available to the holding company, would be key.	20%



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What investors think..

- Right now, anything new or unusual is a challenge..
- Even in good times, investors often struggle
 - Complexity of structures
 - Lack of consistency between even similar deals requires substantial investment in understanding each new deal
 - Many deals are only sold to investors within the industry! (how much risk is being transferred out?)
- But, diversification (eg catastrophe risk) is attractive to many



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Insurance Securitisations - Conclusions

- Insurance Securitisation remains a key topic of interest for the industry...but barriers to growth exist
- Moody's will analyse future life transactions using our internally constructed stochastic modelling approach
- IFSR impact of transactions variable but depends on size, treatment of associated leverage and use of proceeds
- More work required to comfort investors on such deals



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