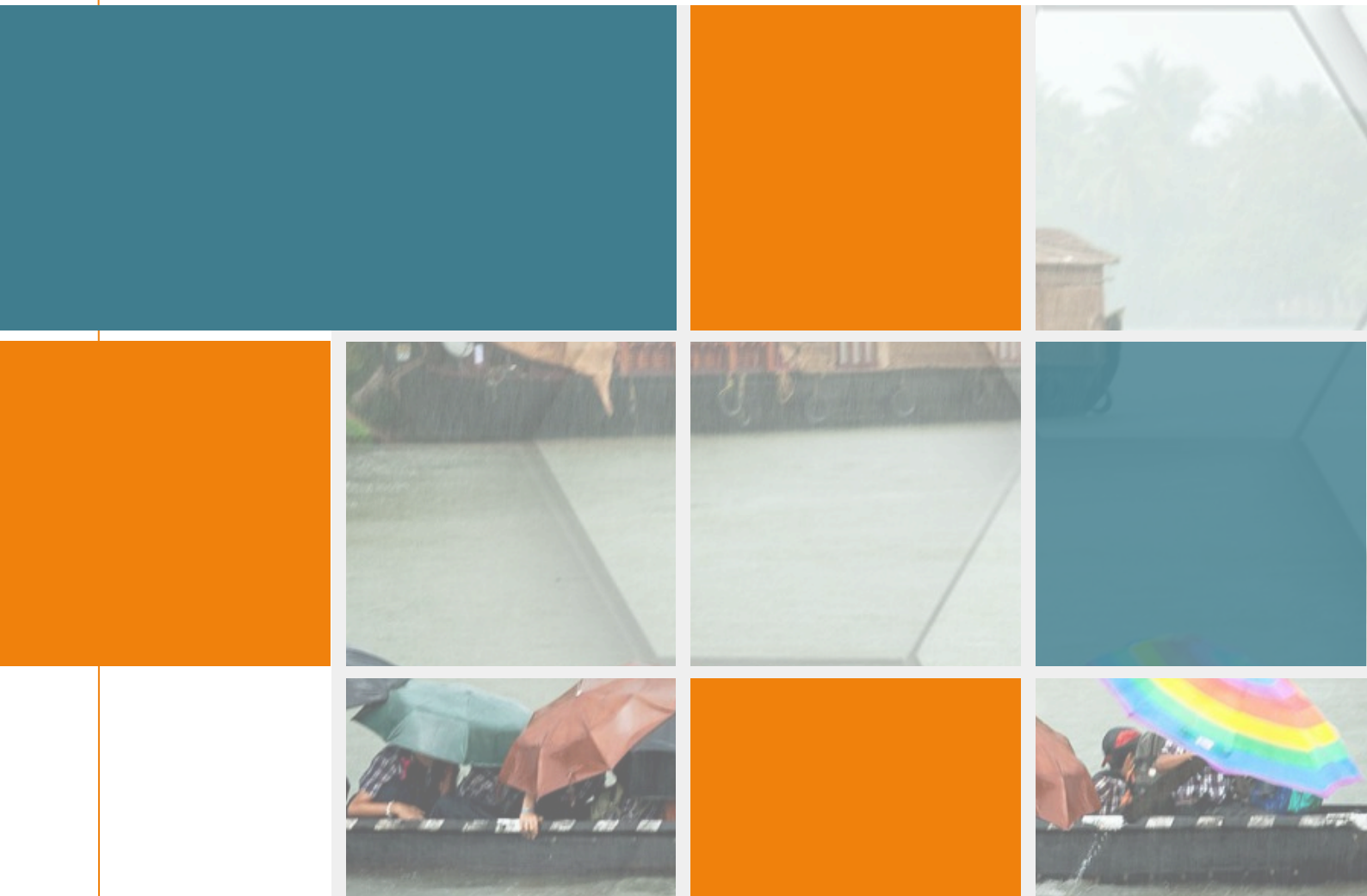


Regional Risk Pools: Optimisation Options for Risk Ceding and Retention

Non-technical Summary

June 2024





Global Shield
Solutions Platform

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GLOBAL SHIELD PROGRAMME ON RESILIENT RISK POOLS

Regional Risk Pools (RRPs) offer countries a unique value proposition. Offering parametric insurance products across member countries provides these countries not only with rapid financial recourses after disasters, but also co-benefits with respect to risk analysis, risk awareness and wider risk management. By facilitating a collective approach to risk management, RRP allow member countries to obtain access to cost-efficient insurance coverage and enhance the overall capacity for risk management.

In order to support RRP in enhancing and scaling up their offerings across member countries, the Global Shield Solutions Platform established the Global Shield Programme for Resilient Risk Pools (GSRRP), a support mechanism of the GSSP, which was launched at COP28 in 2023. Offering RRP a range of CDRFI support measures, the GSRRP enhances their financial management capacities. This, among other benefits, helps them limit their exposure to the volatility of reinsurance premiums.

Therefore, this study was commissioned to assess alternative solutions to risk transfer/retrocession to the international capital/reinsurance markets to become less exposed to fluctuating reinsurance premiums. It will inform the work of the GSRRP by providing potential support measures to the GSRRP and RRP to optimise their exposure to the private capital/reinsurance markets.

About the Global Shield Solutions Platform

The Global Shield Solutions Platform (GSSP) is a multi-donor grant facility and one of the financing vehicles under the Global Shield against Climate Risks. With the mandate to foster the actual development and use of Climate and Disaster Risk Finance and Insurance (CDRFI) solutions, the GSSP contributes to effectively addressing losses and damages exacerbated by climate change.

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ACRONYMS

ARC Ltd.	African Risk Capacity Limited
CCRIF SPC	Caribbean Catastrophe Risk Insurance Facility Segregated Portfolio Company
GSRRP	Global Shield Programme for Resilient Risk Pools
GSSP	Global Shield Solutions Platform
KPI	Key Performance Indicator
mn	Million
MoU	Memorandum of Understanding
PCRIC	Pacific Catastrophe Risk Insurance Company
RRP	Regional Risk Pool
SPC	Segretated Portfolio Company
SEADRIF	Southeast Asia Disaster Risk Insurance Facility
USA	United States of America
USD	US Dollar

This paper summarises and interprets the findings of the qualitative and quantitative assessment of the potential risk retention / transfer optimisation options across the four RRP, namely the African Risk Capacity Insurance Company Limited (ARC Ltd.), CCRIF SPC (formerly Caribbean Catastrophe Risk Insurance Facility, CCRIF), the Pacific Catastrophe Risk Insurance Company (PCRIC), and the Southeast Asia Disaster Risk Insurance Facility (SEADRIF). This work was presented and discussed with the RRP and a broader stakeholder group at the Climate Risk Finance Forum held at the Frankfurt School of Finance & Management on 11 and 12 April 2024.

1. INTRODUCTION

Regional Risk Pools (RRPs) allow sovereign governments to benefit from lower cost risk transfer solutions than would have been possible individually, resulting in improved risk financing and contingency planning for the benefit of vulnerable communities.¹ They encourage a collective approach to disaster risk management by facilitating member countries and the humanitarian sector access to insurance coverage that is linked to joint and collaborative contingency planning.

RRPs retain part of the risk according to their risk bearing capacity and risk appetite, providing a diversification effect by pooling the risk of member countries. The remaining risk is transferred to international private capital / reinsurance markets. Thus, RRP can smoothen fluctuations in international reinsurance markets by instead partially employing own risk capital. RRP are thus able to secure risk transfer to the international private capital / reinsurance markets at lower costs than would have otherwise been possible to mitigate the impact of events with large payout requirements. However, risk bearing capacities of regional risk pools are limited.

RRPs have been lately confronted with significantly increased cost for reinsurance. Following interviews and workshops held with RRP and technical experts throughout 2023, GSSP launched its Global Shield Programme for Resilient Risk Pools (GSRRP), aiming to strengthen the financial management capacities of RRP including limiting their exposure to the volatility of reinsurance premiums, which can lead to significant benefits in terms of cost savings, improved profit margins, and enhanced capital efficiency. It is also a cornerstone for the long-term success of the RRP that they are well capacitated to defend their perspective on the level of risk versus their reinsurers and their clients.

Thus, the improvement of existing and the assessment of new risk management approaches such as risk pooling across or risk transfer to other regional risk pools, or a global risk pooling facility may be an effective strategy to increase the benefits of diversification and to reduce the cost of (and reliance on) reinsurance for RRP.

To substantiate those assumptions, research was commissioned by GSSP and undertaken by WTW to contribute to an **optimisation regarding RRP's risk strategy in relation to retention of risks and risk transfer as well as to inform the RRP and the GSSP on potential complementary support measures.**

This **non-technical paper outlines support needs for RRP** to operationalise the optimisation options for risk ceding and retention. The options include:

- (1) To **establish a donor coordination and support group** working on a coherent basis with the RRP.
- (2) To **invest in strategic technical, actuarial support and modelling capabilities** in the RRP and at joint level to help defend their view of risk to the insurance market.
- (3) To **protect RRP from retention losses and unlock deployment of own capital**, (i) the development of new, or the deployment of existing, sovereign guarantee mechanism(s) and / or (ii) the creation of a capital pool to protect pool retention losses could be considered. Such mechanisms help shield against significant retention losses, providing a safety net, so that available capital is deployed less conservatively.
- (4) Phased **development of a dedicated reinsurance facility** that offers lower cost reinsurance to RRP because of further internalisation of diversification and lower profit margins. The effectiveness is constrained by the amount of available capital.

[1] Martinez-Diaz, L., Sidner, L., McClamrock, J. (2019), The Future of Disaster Risk Pooling for Developing Countries: Where do we go from here?, World Resources Institute.

[2] Tesselar, M., Wouter Botzen, W.J., Aerts, J. (2020), Impacts of Climate Change and Remote Natural Catastrophes on EU Flood Insurance Markets: An Analysis of Soft and Hard Reinsurance Markets for Flood coverage, Atmosphere, 11, 146, doi:10.3390/atmos11020146.

2. REGIONAL RISK POOL CHARACTERISTICS AND CHALLENGES

The research assessed the characteristics of three of the RRP. Due to insufficient information, SEADRIF was not included. While the three RRP **share similarities, there are notable differences** in their capital management and risk ceding strategies.

ARC Ltd, CCRIF and PCRIC are all set up as **corporate insurance entities** in their respective jurisdictions and regulated as "captive insurers"; they primarily serve member countries rather than the general public. All RRP have the capacity to use segregated accounts / portfolios ("cells") under their insurance licenses, though only CCRIF currently utilises multiple underwriting cells to segregate lines of business.

All three RRP use different approaches for **premium setting**. ARC Ltd.³ sets its prices to members often before knowing its reinsurance costs, due to their relatively dynamic portfolio and late renewals. More strict engagements with clients around renewal timelines led to premium loss of USD 9mn in 2022. CCRIF focuses on understanding reinsurance pricing in advance and tailoring coverage to client needs rather than premium availability. PCRIC uses standardised pricing across clients, determined by precedent and adjusted for reinsurance price changes. All new products sold in 2023 / 24 were priced according to the cost of facultative reinsurance.⁴

All three RRP have different approaches to **capital management**. Most of ARC Ltd.'s risk capital is in the form of debt rather than equity, potentially constraining its deployment to cover risk retention as the loan repayment deadline approaches. Consequently, it has an increasing reliance on reinsurance with limited potential to accumulate its own capital. CCRIF follows a conservative strategy. The segregated cell structure dilutes the value of diversifying geographies and perils, allied with a general tendency towards conservatism in capital deployment it constrains the pursuit of new opportunities at scale. Additionally, CCRIF faces challenges due to the clash between its tropical cyclone risk and the peak global catastrophe risk zone in the southeastern USA. This increases the volatility of its access to reinsurance and exposes it to external shocks beyond its own business and operational region. PCRIC's challenges lie in its growth and access to capital. As PCRIC expands and introduces new products to a relatively small number of clients with small coverage sizes, there may be limited reinsurance market appetite for these diverse risks. Moreover, despite being fully diversified for global reinsurers, the small volume of its portfolio presents significant challenges in attracting market interest. PCRIC aims to minimise maximum probable loss while looking towards future refinement of capital management with increased underwriting.

All three pools rely heavily on **reinsurance** to manage their catastrophe risk exposures: ARC Ltd and CCRIF allocate a significant portion of their premiums to reinsurance, with varying degrees of success in claims recovery. PCRIC, on the other hand, faces challenges related to its reinsurance market engagement and aims to redesign its approach to enhance risk appetite and influence pricing.

All pools **use catastrophe risk and dynamic financial analysis models** to quantify their underwriting risks and to plan for an effective balance between retaining risk and transferring or ceding risk to reinsurance. CCRIF and ARC Ltd have well-established and documented processes and procedures covering all aspects of underwriting, reinsurance purchasing and capital management; PCRIC is in the process of developing similar procedures as it grows.

[3] ARC Ltd's client engagement approach, for sovereigns at least, is led out of ARC Agency, the grant-funded sister entity of the ARC Group and goes far beyond purely insurance matters.

[4] Facultative reinsurance means negotiating reinsurance coverage separately for the individual insurance policy or risk.

The RRP's all prioritise the **stability** of the underlying **insurance policy pricing**, using pool capital as a buffer to handle any big fluctuations in the cost of reinsurance or a year of heavy losses from claims. However, it is important that their pricing is based on sound calculations (actuarial adequacy). CCRIF has managed to keep its losses relatively low compared to the premiums it collects, suggesting adequate pricing. ARC Ltd, however, has seen its losses exceed its premiums in recent years (net loss ratio), indicating that its pricing might not be enough to cover its costs. PCRIC's net loss ratio is provisionally estimated to be well below 100% (i.e., losses below its premiums suggesting adequate pricing), although it represents the smallest sample and has not been operating as long.

Considering their capital positions and risk ceding strategies, **key challenges** have been identified:

- **Uncertainty** around the **willingness of donors** to deploy additional risk capital at scale.
- In view of limited financial resources, both the **form and terms of the capital** provided and the **potential impact on the level of support available for insurance premiums** are critical to the benefits of RRP's.
- None of the pools has a **clear path to recapitalisation**, particularly in the time frame of 1 to 2 years. This reduces each Board's **appetite to retain risk**, particularly at the bottom of the portfolio risk structure⁵ and **leads to purchase of reinsurance in these working layers with high cash cost**.
- All pools are **under-resourced relative to their current operations** and / or pursuit of growth. This is especially true on the technical side, where **definition of risk** (and defence of that definition) and **financial analytics** capabilities are critical to optimise capital deployment. This is exacerbated by climate variability and climate change increasing the level of uncertainty and thus potential additional buffers priced in by reinsurers.
- Innovating around reinsurance purchasing is challenging. Pool Directors are concerned about the existential risks of underperforming reinsurance programmes; technical resources are already maximised, particularly in the renewal phase; constant changes in underlying portfolios can make optimisation challenging; and bringing new products into an existing reinsurance programme can pollute that programme and, rather than gather diversification and scale benefits, can erode value for money instead.

For effective cross-pool risk sharing, it would be essential to standardise and harmonise different risk assessment and financial modelling methods. Using a shared modelling platform such as OASIS would facilitate this process. This approach would also facilitate the RRP's in maintaining and justifying their unique risk perspectives and develop tailored products for their clients.

When identifying support needs, it is essential to start by considering what is achievable, the timeframe, and any additional conditions. This may be challenging for stakeholders in the face of uncertainty. However, it is essential for the RRP's optimisation of capital management, especially at the governance level, to better understand the potential extent of available support.

[5] The "bottom" of the portfolio risk structure refers to more frequent, smaller losses that are typically less catastrophic but more common. They occur more often which can steadily diminish financial reserves. Transferring the risk of these working layers comes at a high cash cost.

3. POTENTIAL SHARED OPTIMISATION OPTIONS FOR RISK CEDING AND RETENTION

To address the challenges outlined above, the following options for risk ceding and retention have been considered.

Risk swaps⁶ are transactions between two insurers, where each insurer seeks to balance its portfolio of risks by swapping some of that risk with the other insurer, whose portfolio is uncorrelated. Through this exchange, both insurers simultaneously reduce their peak exposure⁷ and gain new diversified risk. While theoretically efficient, in practice challenges including differing risk assessments and pricing assumptions make risk swaps unattractive. The biggest concern for RRP's, though, is the justification of continued participation, particularly if they have not made a claim for several years. While each may argue the swap brings benefit to their clients and region, this is undermined when a large payout is made to non-client countries elsewhere in the world.

Co-insurance involves multiple insurers jointly underwriting primary insurance policies on the same terms. In the context of the RRP's, existing reinsurance partners are unlikely to co-insure alongside a pool, and co-insurance between pools faces similar challenges to risk swaps. Instead, a new **global facility** could offer co-insurance, allowing pools to offer new covers at scale and increase scale on existing covers. Such a facility would allow pools to take on more risk without impacting their reinsurance programmes. However, challenges include establishing rules for underwriting and rating to ensure that allocation of capital was transparently fair and equitable between the RRP's, regulatory compliance, and managing operational complexities for pool clients.

Reinsurance is already, and will very likely remain, the primary method for risk sharing among the RRP's. Various forms of reinsurance, including insurance-linked securities (ILS)⁸, have been utilised by the pools, with annual aggregate excess of loss⁹ treaties being the most common. Opportunities should be explored to optimise reinsurance through collaborative approaches and considering the potential use of a new **global facility to enhance the efficiency of risk transfer across all RRP's**. Collaborative approaches may include developing shared tools and metrics for optimising reinsurance purchasing, sharing experiences, and creating shared tools to constrain uncertainty in risk analytics.

Shared reinsurance across the pools is deemed unfeasible, despite potential technical benefits. CCRIF does not currently share reinsurance across its segregated portfolios and PCRIC did not include new insurance policies (starting in late-2023) under their existing reinsurance agreement but purchased (relatively expensive) facultative cover. In both cases, risk segregation takes precedence over risk ceding optimisation within the same pool that would likely persist, even more strongly, across multiple pools.

[6] Also known as portfolio swaps or reciprocal exchange.

[7] The maximum level of risk exposure that an insurer faces at any given time.

[8] Insurance-linked securities are used to securitise insurance risks as fixed-interest securities, transfer them to the capital market and trade them there.

[9] Aggregate losses for the respective Risk Pool that exceed a certain stated retention level are transferred to reinsurance.

A new global reinsurance facility could offer **facultative cover** to allow RRP to write larger risks that would otherwise unbalance its portfolio; provide **extra capacity on upper layers of cover**¹⁰ where the benefits of diversification can be best captured, although this would require significant own risk capital available within a new facility; provision of **capacity for lower, working layers of cover**, which are typically more tightly priced but where the majority of reinsurance costs are assumed and / or provide **multi-year capacity for sequential losses in the retention layer**.¹¹ The global facility could also be a **technical hub and shared testbed** for new initiatives across the RRP, developing new risk transfer products as well as risk management services through, e.g., deploying risk models and data in support of climate-resilient investment approaches at the sovereign level, and promoting integrated sovereign disaster risk reduction and disaster risk financing strategies.

Direct capitalisation of the RRP reduces the need for risk transfer, lowering overall costs. However, the return on investment must be considered. Reinsurance costs decrease with greater capitalisation, but capital deployment must align with long-term needs, not just high reinsurance price periods.

The priority must be to unlock the already-available capital at the pools before consideration of additional capital. Subsequently, one option for a global facility might be to manage a donor-funded pot of **contingent grant capital**, allocated to RRP individually to be drawn down for relatively soft triggers such as consecutive retention losses, with additional capacity for extreme events. This contingent capital could be in the form of guarantees, reducing donor capital volatility.

→ A reinsurance facility offers self-sustainability and capital sharing but can be administratively heavy. Direct capital provision or contingent capital can benefit the Risk Pools more directly and with less administrative burden. **The most impactful approach likely involves both capital provision and flexible reinsurance issuance to enhance pool sustainability and offer affordable insurance solutions.** While growing pools will require more capital, reinsurance will remain essential even in times of elevated costs on the international reinsurance markets. A new facility will require technical capacity, presenting an opportunity for the Risk Pools to share resources, particularly for risk analytics. **Shared resources would be powerful for developing a balanced view of risk for climate perils, which is crucial to containing uncertainty and thus reinsurance costs.**

[10] I.e., ones likely to pay only on a very unlikely event.

[11] The retention layer typically refers to the portion of risk that the insurer, here the respective RRP, decides to retain rather than transferring to a reinsurer. The provision of multi-year capacity through the global facility for sequential losses in this retention layer ensures that RRP have sufficient cover to deal with losses that occur in successive years.

4. RECOMMENDATIONS

Four key recommendations have been made for review and potential action as outcomes from this research and with regards to the RRP's potential optimisation of risk ceding and retention, both individually and as a group.

1. Provision of capital

- Additional capital will be required if risk pools are expected to strengthen their role in offering member countries' access to needs-based financial protection and thus are expected to grow, to avoid becoming more and more thinly capitalised and thus ever more reliant on reinsurance. Each pool will require capital on their own balance sheets for this purpose. This could be achieved through a combination of donor grant funds (much preferred over loans) and a capital accumulation margin being added to insurance premium (the current pricing of which does not allow for significant or rapid capital accumulation).
- However, any new capital provision should be accompanied by efforts to unlock conditions for fuller deployment of existing capital, a key barrier to which is the challenge of raising new capital in the event of heavy losses.
- The priority on the capital provision side should thus be a mechanism which provides for **guaranteed re-capitalisation after pre-agreed levels of capital erosion** (e.g., back-to-back retention losses), conditioned on pools having met agreed capital coverage KPI benchmarks,¹² pursuing appropriate ceding vs retention optimisation, and maintaining adequate inwards premium pricing.
- The mechanism could include access to existing donor guarantee facilities and / or a new capital pool. The capital pool would need a replenishment process to maintain the primary function of guaranteeing recapitalisation for the pools; triggered drawdown by one pool should not affect the ability of other pools to draw down if trigger conditions are met.
- Any shared donor capital fund should complement, not replace, bilateral resource mobilisation by the pools. Further, an evaluation should be made as to the opportunity cost of using funds for capital support versus, for example, premium financing for pool clients so that the optimal mix of funding mechanisms is identified and pursued.

2. Consideration of a new global reinsurance facility

- The criticality of reinsurance to the operations and financial security of the pools has been clearly demonstrated in the research, as has the relatively high pricing currently being endured by the pools and the consequences of that for underwriting performance.
- A first step before considering a new dedicated reinsurance vehicle to serve the pools should be the creation of a **shared technical resource facility** to support the pools in their optimisation of access to the global reinsurance markets.
- A new global reinsurance facility would provide reinsurance to the pools, backed by its own (new) capital (potentially co-funded between donors and impact-driven private risk capital) and accessing the reinsurance market on a globally diversified basis to boost its own deployable capital.
- Such a facility could offer one or more products, beginning with those most valuable to the pools and commensurate with available underwriting capacity.

[12] Capital coverage KPI benchmarks are specific metrics used to assess the financial health and stability of an organisation, particularly its ability to cover its liquidity requirements in case of severe losses in the insurance portfolio. The KPIs identified should include: changes in the insured portfolio; uncertainty in future hazard frequency / severity and, therefore, expected loss; reinsurance / risk market dynamics; consecutive heavy loss years; testing for softer criteria. It is also recommended that stress testing, rather than multi-year dynamic modelling, be used to evaluate different options under different current and potential future circumstances. For further detail: [link to Report](#)

- Highest value to the pools would provide the offering of shares of facultative excess of loss covers where market pricing is relatively high. This includes, but may not be limited to, coverage for new insurance products offered by the pools, large blocks of reinsurance cover for a single country / peril, and cover after a reinsurance loss year when prices to the affected pool are likely to spike.
- A second area of concentration could be offering fair and stably priced quota share cover in the lower risk layers, which would be valuable in reducing the cash cost and volatility of that cost of reinsurance for the pools, and would not require as much underwriting capacity, i.e., own risk capital, in the new facility as offering reinsurance cover in the higher risk layers.
- A final focus could be on multi-year retention covers which would provide an alternative way of protecting a pool's capital base after heavy losses.
- Creating a Lloyd's syndicate¹³ managed by a Managing General Agent or building on the Global Parametrics / Natural Disaster Fund model / platform are examples of lighter-touch approaches for a new global reinsurance solution; either of these, or a similarly designed new entity, could accommodate shared public and impact-driven private capital, and start-up resources would be low compared to a full reinsurance entity.
- The lightest touch option for a new facility would be if it were to act as a "following" market, by offering either a share (say 10%) or fixed limit amount of any pool reinsurance placement once it was within agreed parameters and taken at the market price. While participating in the reinsurance programme would put some downward pressure on reinsurance pricing (by increasing the supply of reinsurance), pools would mainly benefit through profit share: if the market price proves to be profitable, which has been the case so far, not only the reinsurance market but also the global facility would receive its fair share of the profits. The incurred profits could be returned to the pools. Over time, as experience grows, a more active policy could be pursued, increasing shares in times of a hard market (and excess profit to reinsurers), reducing in a soft market.
- If offering specific products or, indeed, acting as quoting market at all, the facility would need significant technical capacity in risk analytics and structuring of insurance programmes to both operate a viable and sustainable book of business and to design and purchase its own reinsurances.
- Finally, qualitative considerations are likely to be at least as important as quantitative ones in assessing value and viability; for example, the governance structure for such an entity would need very careful consideration, with the pools (and their respective members), donors providing capital, and private sector partners (if any) all likely requiring representation in decision-making.

[13] A Lloyd's Syndicate is a traditional market facing business unit at Lloyd's, supported members of Lloyd's. Members are the insurers for their share of any risk written by the syndicate. <https://www.lloyds.com/join-lloyds-market/underwriter/syndicate>

3. Establishing a shared technical resource base to complement in-house modelling and analytics

- All pools are **under-resourced on the technical side relative to their respective ambitions and those of their stakeholders**, not only in closing the protection gap through broader use of disaster risk financing and insurance, but also in expanding the use of risk information to inform comprehensive disaster risk management.
- Of particular concern at present, highlighted by the research, is a widening of the gap between the pools' view of risk and that taken by the reinsurance markets, leading to higher reinsurance pricing but also potential under-pricing of insurance products by the RRP's themselves. Establishing a sound view of the risks being taken on and then shared, including uncertainties around that view, is the foundation for an efficient and sustainable underwriting business; for parametric insurance, most of the work is of a technical and quantitative nature, and requires appropriate resources to maintain.
- Some, likely significant, part of the divergence in view of risk is driven by the role of climate uncertainty, and an early focus of shared technical resources should be towards improved identification and quantification of uncertainties in portfolio risk profiles for pools' climate perils, based on the best-available science. **Armed with such information, pools will be better positioned to defend their own view of risk versus the reinsurance market.**
- Further than establishing a sound view of risk, translating that view into a robust and optimised risk management strategy internally, and defending the view of risk against reinsurers are the routes to lower reinsurance costs and more efficient deployment of own capital.
- Underestimation of risk by the pools should also be a concern; it leads to systematic and hidden under-pricing of primary insurance and can also expose the pool to unknown retention of tail risk above the reinsurance structure.
- Shared resources cannot replace in-house resources but can foster collaboration and cross-learning and achieve economies of scale in key areas of technical work. A technical resource pool should foster exchange of knowledge and, potentially, staff between the pools.

4. Establishing a level playing field of technical information

- For support needs to be fairly and accurately assessed, on an ongoing basis, across the pools, stakeholders and the pools themselves must have a shared understanding of the state of their businesses, their capital adequacy and the degree to which their risk ceding and retention mix is optimised, amongst other things.
- In addition to quantitative information, such as the establishment of key metrics and KPIs mentioned above, the fulfilment of which would be a prerequisite for support, qualitative information is also important; solutions must be pragmatic and agreeable to the Risk Pools, not only at the technical and operational level but also at the governance level.
- The research suggests that in particular a capital coverage KPI benchmark (range)¹⁴ agreed between pools and stakeholders could encourage more existing capital to be put at risk during periods of higher reinsurance pricing or other times of duress.
- A process should be supported to **independently capture and analyse a fixed set of information**, along the lines developed by the research, using defined techniques, and applied uniformly across all the pools. The outputs from such work, to take place at least annually, should be subject to a peer review process including representation of all end-user groups, and at least key elements, but preferably all, should be made available in the public domain (notwithstanding commercial sensitivities).

[14] (Net retention at the RRP level at X-yr return period minus net premium income) divided by available capital, a metric to assess the level of risk at the RRP level by setting potential losses in relation to available capital.

5. IDENTIFICATION OF SUPPORT NEEDS

1 Establishing a support group for pools at the donor level, to better coordinate donor interactions with the pools and their governance structures

- In addition to existing donor coordination groups for individual Risk Pools, donors should establish a coordination and support group to liaise with the Regional Risk Pools collectively on a uniform basis. The RRP Joint MoU established a modality to engage as a group to further their shared interests; a counterparty group on the donor side would be highly beneficial in furthering collective goals.
- The above recommendations assume that pools share donor resources to implement the proposed solutions – funded via existing initiatives as well as potentially via GSSP. In the event that the recommendations are adopted, a coordinated set of information, including financial information, would need to be agreed to create a level playing field on which to base decisions regarding, among other things, resource allocation and performance target setting.

2 Investment in strategic technical support

- An urgent need for coordinated resources for technical support both at the individual pool level and on a shared basis has been identified. Such support must be strategic, not ad hoc, and should support more transparency in and consistency across models and analytical techniques, amongst other things.
- Climate risk uncertainty seems to be the dominant cause of the divergence in view of risk between pools and markets seen in recent years; this will persist beyond the hard market if not addressed and should be a particular focus of support resources in the first instance.
- The form of a technical support facility requires further careful consideration, particularly including the risk pools themselves to ensure complementarity with the initiatives they are pursuing both on a stand-alone and on a group basis.

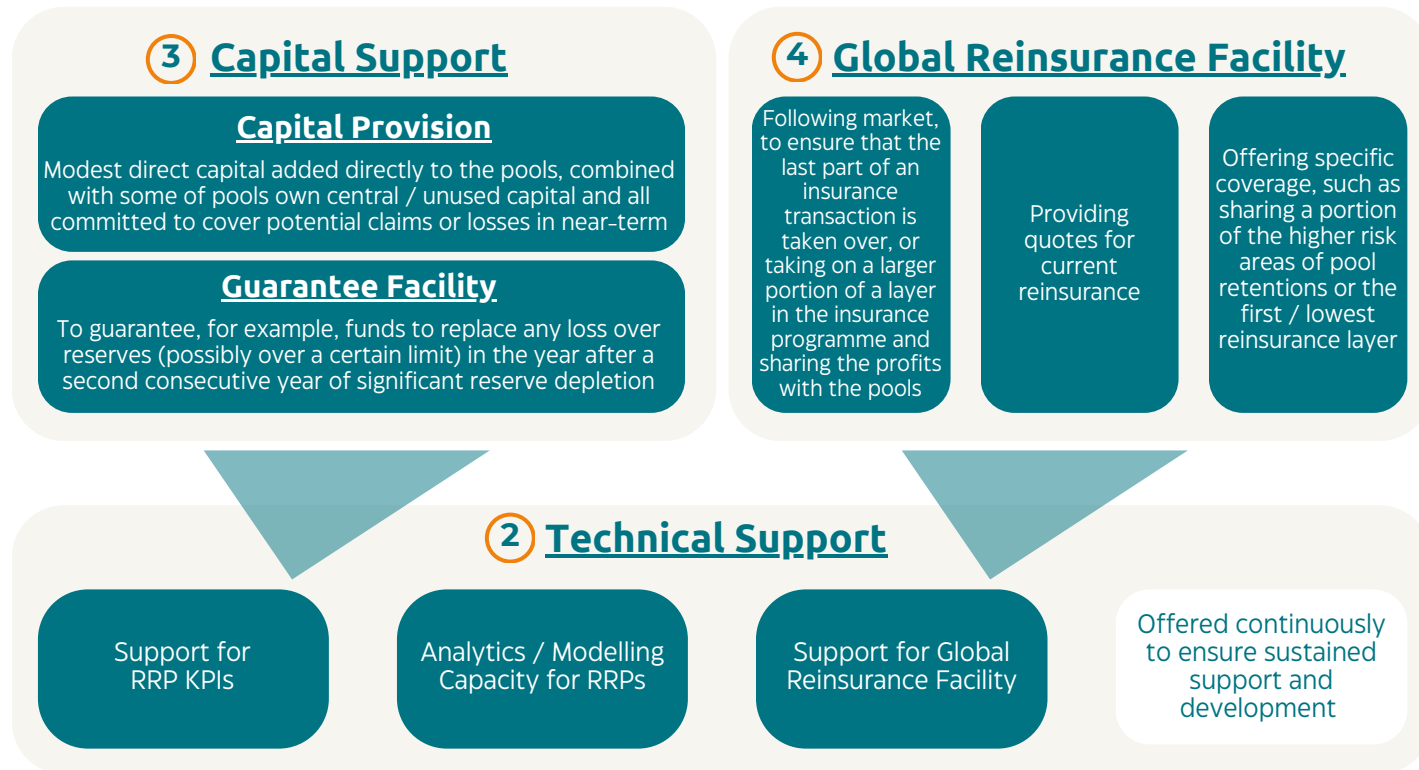
3 Development of new, or deployment of existing sovereign guarantee mechanism(s) and / or creation of a capital pool to protect pool retention losses and unlock deployment of own capital

- Many donors already offer guarantee facilities; support is necessary for identifying and establishing a shared guarantee mechanism which operates effectively for and across the pools. This should be trigger-based, the trigger being some level of capital erosion through successive retention losses, with the guarantee being consistent with the need of each pool to stabilise its capital base.
- Alternatively, a new capital pool could be established and funded, with similar trigger-based access; this would require new capital commitment(s) and thus might be considered as a second phase of capital support. A shared pool of capital between the RRPs would spread timing risk, but commitments would have to be in place such that all RRPs would have access to capital should their trigger conditions be met.

- Trigger based replacement of lost capital beneath the reinsurance programme should be conditional on key performance metrics being within agreed ranges, including capital adequacy and appropriate primary premium pricing, as well as efficient deployment of current capital. The research strongly recommends that capital be provided in the form of grants rather than loans, and expectations around pools raising premiums to aggregate capital more quickly after a series of large pay-outs must be managed, given the sensitivity of their client bases to premium price increases.
- Pools will also require additional capital to support growth of coverage for their clients, which is the desired outcome for all stakeholders. The timeframe for this varies between the pools and each would need to make their individual case based upon both agreed common metrics and KPIs and individually developed growth projections and broader business cases.

4 Phased development of a dedicated global (reinsurance) facility

- The ultimate impact of a dedicated reinsurance facility / hub would be constrained by the level of financial commitment – in the form of investment in technical and operational resources as well as risk capital – from donors and other potential capital providers / investors.
- A phased approach should be established, with resource needs moderate to start, and growing with each phase, which can build upon the previous one. A sound governance structure would need to be in place from the start and must include pool representation alongside capital contributors and other stakeholders. The pools have different governance and operational structures, each serving as a useful model, and other “light” reinsurance vehicles used in the market could also be appropriate.
 - A **first phase** could be **capitalisation of a facility which would act as a “following” reinsurer**, taking a certain fixed share or fixed limit on pool reinsurance programmes at market terms as described above. Such a vehicle could have a very light administrative and operational footprint, useful examples being Lloyd’s syndicates operated by a Managing General Agent, or the Natural Disaster Fund operated by Global Parametrics.
 - A **second phase** would be dependent on **building technical capacity and adding capital**, so that the new reinsurance facility could take larger shares on existing reinsurance programmes, or could offer large shares on specific products to pools where the market is not providing appropriate support; this could include for new products and for multi-year protections of lower / retention layers.
 - A **third phase** could be to **expand the capital base**, and therefore the value to the pools, by attracting impact-driven private funds, allowing underwriting at higher volume, including more products and participation on existing reinsurance covers at a scale which brings consistently better pricing to the pools.



6. MOVING FORWARD

The findings and recommendations of this Paper serve as a compass for the GSRRP to work with RRPs to better protect them from losses and make the best use of their financial resources, while also highlighting the key role of donors in providing (new) financial resources in a transparent manner.

The research highlights:

- The need for **greater donor coordination and steering of RRPs through jointly agreed KPIs;**
- The need for **a more sustainable and systematic support programme that provides a clear path to recapitalisation;**
- The need for **increased optimisation of risk capital for all RRPs through the establishment of a new global (reinsurance) facility.**

