Learning lessons from recent CAT events

*Middle East Insurance Review* sat down for an exclusive interview with **SCOR CEO and Chairman Denis Kessler** as he discussed some of the lessons learnt from costly recent natural catastrophe losses, which might yet see 2011 becoming one of the most expensive year for reinsurers.

By Ridwan Abbas

The estimated US$70 billion losses from natural catastrophes and man-made disasters in the first half of this year have made 2011 the second-costliest calendar year on record, topped only by the events of 2005 when Hurricane Katrina hit the US Eastern Seaboard. The severe loss events of recent times have brought about emerging trends in the reinsurance sector, said Mr Denis Kessler.

Firstly, some recent events like the floods in Australia and earthquakes in New Zealand, have brought an increased attention to what have always been referred to as non-peak territories. Indeed, the severity of losses arising from these events means that more focus needs to be placed on other areas of the portfolio – aside from the “peak perils” of US hurricanes, US earthquakes, European windstorms and Japan earthquake.

According to Mr Kessler, “increasing attention is being paid to non-peak territories, and it is important to manage exposures in the various different parts of the world.”

Operating in 160 countries worldwide, SCOR certainly understands the specific features of each territory. Mr Kessler pointed out that SCOR’s model is not one of standardised products, but of localised approaches.

**Don’t underestimate business interruption**

A second lesson to be learnt from recent events is the fact that the business interruption component of policies cannot be underestimated.

“Business interruption could be more important than one could think especially with very large disruptions, as was the case in Japan,” Mr Kessler said.

The loss potential arising from disrupted supply chains became apparent for the industry in the wake of the Japanese disaster. Prior to that, not many would have explicitly factored in the consequences of automobile makers in the US claiming for failed delivery of Japanese parts when calculating loss estimates.

**Multiplication of CAT events**

Aside from the rising interconnectedness of risks, the multiplying of natural catastrophe events has also been costly for reinsurers.

“You can have a flash flood somewhere with the multiplication of tornadoes,” said Mr Kessler, “and sometimes you get severe hailstorms like in Brazil... so you have to add these up to well-known natural catastrophes. And the unfortunate lesson we have learnt is that these events are localised and quite expensive, and seems to be occurring more frequently than before.”

The key thus lies in experience in the underwriting of natural catastrophes. “You have to know the market, you have to be there on the spot,” he said.

**Over-reliance on models**

The urge to rely heavily on models should thus be curbed in light of the above scenarios. While the industry has just started to work with a new Version 11 of the RMS model, it is wise to recognise the limitations of models in the wider scheme of risk management.

“We are now waiting for new models and some of the past models had underestimated the measure of exposures. So we have to be careful in terms of our reliance on models,” he said.

Despite the challenges, Mr Kessler believes that the industry remains in its strong capital position even as it is faced with a rare scenario of pressure on both its assets and liabilities.

“Most of the time you have bad news on the liability side, or you have negative development on the asset side due to low investment returns. But we have been through a period where there are problems impacting both sides. Despite that, the balance sheets of reinsurers show that we remain in a strong position.”

SCOR’s own resilience was recently validated when A.M. Best upgraded its rating from A- to A, citing “the continuing resilience of SCOR’s risk-adjusted capitalisation, its consistent operating performance and the quality of its enterprise risk management”.

The company said it is on track to meet targets stated in its strategic plan, “Strong Momentum”, and expects gross premium of EUR10 billion (US$13.8 billion) in 2013, up from EUR6.7 billion in 2010.