GUY CARPENTER

Guy Carpenter Views

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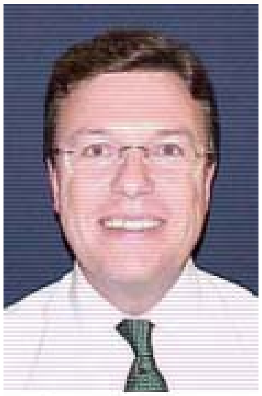
Singapore's Reinsurance Market Poised for Future Growth



Andrew Harris is a Principal at Guy Carpenter and is responsible for Asian treaty reinsurance business.

Singapore has long been recognized as a leading reinsurance center for Southeast Asia, and companies from around the world are currently doing business in this market. To further strengthen the country's position, the Monetary Authority of Singapore (MAS) recently issued a proposed amendment that will increase its oversight of non-domiciled insurers, reinsurers, and brokers providing cross-border services to Singapore.

Guy Carpenter Views speaks with Andrew Harris, Principal, Guy Carpenter, about these new regulatory requirements as well as about current market conditions and opportunities that are likely to develop going forward.

Evolution as a Reinsurance Center

Guy Carpenter Views: Could you briefly discuss some of the reasons behind Singapore's evolution as a key regional reinsurance center? What is the current market composition? Who are the market's clients?

Andrew Harris: There are many factors that have led to Singapore's status as Southeast Asia's premier reinsurance center, including the country's strategic location, ease of market access, governmental support, political and economic stability, cost-effectiveness vis-à-vis other regional centers such as Hong Kong, solid transportation infrastructure, well-educated work force, and the fact that four major languages are spoken here.

The Monetary Authority of Singapore (MAS), the insurance industry's regulator, has taken a number of steps over the years to strengthen the country's appeal as a regional reinsurance hub. Foreign reinsurance companies have been welcomed into the market, and they have been encouraged to establish full branches rather than subsidiaries. A previous 49 percent cap on foreign shareholding has been removed, and the extent to which global reinsurers currently participate in the market is substantial. The MAS has also offered various tax rebates and incentives to entice reinsurers in Singapore to take on new risks.

As of June 2003, approximately 20 reinsurers were operating in Singapore – one domestic company, two subsidiaries, and the remainder branch offices of multinational companies headquartered in the United States, Europe, Japan, and London. This is a reduction from the late 1990s, when more than 40 reinsurers were located in this country. After September11, 2001, many reinsurers withdrew from the international reinsurance market or closed overseas offices such as those in Singapore as cost-saving measures.

Clients of this market are both Asian and multinational insurers located throughout the Asian region, together with captives.

The Pre September 11, 2001 Market

GCV: How would you characterize Singapore's reinsurance market in the decade prior to the September 11 terrorist attacks? What was the impact of such events as the London market turmoil and the Asian financial crisis?

AH: In the decade preceding the September 11 terrorist attacks, the Singapore reinsurance market experienced a period of steady growth, benefiting from London market instability and growth in the region's "tiger" economies.

The London market turmoil, in particular, led to numerous changes in Singapore's reinsurance arena because of Lloyd's substantial contraction from Asia and the need for Asian clients to look beyond this traditional market for coverage.

On the other hand, the Asian financial crisis caused the non-life insurers operating in the Asian region to experience diminished growth, thus impacting proportional reinsurers.

Market premium incomes nevertheless continued to grow, albeit at lower levels but with the implementation of more stringent underwriting guidelines for certain classes of business and in specific territories.

By the time the terrorist strike occurred on September11, 2001, Singapore's reinsurance market had an oversupply of capacity that resulted in "soft market" conditions; and reinsurers were responding to increased client demands by adding more specialist class underwriters.

Impact of September 11 Terrorist Attacks

GCV: How was this market affected by the September 11 terrorist attacks in the United States? Did reinsurance coverage remain available and affordable?

AH: As a direct result of the terrorist attacks, reinsurance companies around the world began excluding from their contracts coverage for acts of terrorism. Reinsurers in Singapore were no exception. Although the market was not directly affected by the terrorist attacks in the United States, as of January 1, 2002, all new insurance and reinsurance policies issued or renewed in the country contained a terrorism exclusion.

During 2002 and 2003, individual Asian market non-life insurance bodies/regulators, such as the General Insurance Association in Singapore, introduced market terrorism exclusion clauses, many of which were based on international market wordings.

Demand for such terrorism coverage has been quite muted from original insureds, particularly when the London market has supplied the quotations, which most clients consider too expensive for the coverage provided.

Some markets, such as Malaysia, established terrorism market pools; but we understand these have only generated modest premium volumes to date.

New and Evolving Exposures

GCV: Please provide a brief overview of current market conditions. What has been the impact of such developments as SARS, the war in Iraq, and corporate governance issues (e.g., Enron)? Are insureds looking for new forms of coverage?

AH: Following some challenging years in the aftermath of the London market turmoil and the September 11 tragedy, Singapore's non-life market had begun to stabilize. Significantly higher reinsurance premium rates and improved risk management measures to reduce claims costs helped to reverse the poor market loss experience of the preceding few years.

In this environment of relative market stability, SARS appeared as a completely unexpected insured exposure. Very few of the Singapore reinsurers anticipated losses arising from this type of epidemic. It has become apparent that only a modest number of insurance policies with business interruption coverage provided for such infectious disease coverage, but these policies have produced significant claims for insurers and reinsurers alike in both Hong Kong and Singapore. Typical insureds most affected have been the hotel industry and medical institutions, such as public and private hospitals.

Original insureds, insurers, and reinsurers have worked together in their respective markets to clarify coverage issues, the extent of loss, and the quantum of claims. Recently, a total of US$16 million was paid to the Mandarin Oriental group of hotels for their SARS claims in Hong Kong.

In the majority of cases, insurers are now excluding this type of coverage with specific clauses as agreed by the international reinsurance market, although specific sub-limited coverage can be purchased by insureds for an additional premium.

Also creating ripples in this otherwise calm market environment is the increased exposure that Asian directors and officers now face. In the wake of the Enron debacle and other recent corporate scandals, Asian governments have issued new regulations governing the actions of corporate leaders. Most Asian publicly listed corporations have already obtained D&O coverage, and insurers/reinsurers are reporting growing levels of interest in this business, coupled with a substantial increase in claims.

Recent Regulatory Developments

GCV: What are the key objectives and provisions of the MAS's new authorization and approval frameworks, which took effect on January 1, 2004?

AH: To strengthen its supervision of insurance services delivered in Singapore, the MAS has developed authorization and approval frameworks to regulate the activities of non-domiciled insurers, reinsurers, and brokers wanting to do business in the country. These frameworks, effective January 1, 2004, set forth the minimum requirements that participants must meet in order to provide – or to continue to provide – insurance, reinsurance, or broking services to Singapore without having a physical presence in the country.

The authorization framework establishes the requirements for both reinsurers currently offering reinsurance to Singapore and those that wish to operate in Singapore in the future.

The approval framework, in turn, establishes requirements for all marine, aviation, and transit (MAT) insurers, MAT direct brokers, and all MAT reinsurance brokers offering cross-border services to Singapore. Only those MAT insurers and brokers that are licensed under the laws of countries specified by the MAS may apply for approval.

In reviewing an application for authorization or approval, the MAS will take into account such criteria as capitalization level, financial soundness, and credit rating.

All authorized and approved insurers and reinsurers must disclose to their Singapore customers their authorized or approved status, the type of insurance or reinsurance business for which they are authorized or approved, and the extent to which they are subject to MAS oversight. They also must file their annual returns in accordance with MAS formats and deadlines.

GCV: How is the MAS helping to ensure that Singapore's authorized and approved insurers and reinsurers have the financial strength to cover their expected and unexpected losses?

AH: In addition to developing the authorization and approval frameworks, the MAS has established a risk-based capital (RBC) framework under which all authorized reinsurers and approved MAT insurers will be required to maintain reinsurance and insurance deposits, respectively, with the MAS.

The amount of these deposits will be based on business written or liabilities incurred with respect to cross-border business written from Singapore. The minimum deposit will be either S$5 million (S$1.7 = US$, as of Jan., 2004), 30 percent of gross premiums written in the previous financial year, or 30 percent of gross liabilities incurred at the end of the previous financial year, whichever is higher.

GCV: What types of reinsurers will be operating in Singapore once the authorization and approval frameworks take effect?

AH: Now that the new MAS regulatory frameworks have taken effect in January 2004, insurers registered in Singapore will be dealing with three types of reinsurers: registered reinsurers, authorized reinsurers, and reinsurers that are not regulated by the MAS.

Registered reinsurers, those companies that have a physical presence in Singapore, will be permitted by the MAS to engage in the widest range of activities.

GCV: Once the new MAS frameworks go into effect, will insurers be required to deal with only authorized and approved reinsurers?

AH: Strictly speaking, no. Insurers registered in Singapore will remain free to transact business with reinsurers that are neither authorized nor approved, but this has yet to be fully clarified by the MAS.

GCV: What are the key requirements of the approval framework for MAT insurance and reinsurance brokers?

AH: All approved MAT insurance and reinsurance brokers are required to maintain professional indemnity insurance coverage of at least S$1 million; to establish an Insurance Broking Premium Account (IBPA) for premiums collected in Singapore; to place business only with approved or registered MAT insurers; and to disclose to clients their status, the nature of their relationship with the insurer, and the insurance premium charged.

Product Trends and Pricing

GCV: What types of reinsurance products are most in demand? How are they being purchased and structured? What new products are being introduced?

AH: There is still a strong demand for traditional products, with the majority of our business involving property and marine coverage. Specialist areas such as life, accident, and health have also begun to develop over the past few years; but monetary limits are still relatively modest in comparison to larger and more developed insurance markets.

For all classes of both treaty and facultative business, the greatest increase in demand has been for excess of loss reinsurance. Reinsurers have been actively competing for this business, and at 2003 renewals, leaders requested minimum shares of 30 to 50 percent on each excess of loss program. Consequently, many of these programs were oversubscribed once pricing was finalised.

A number of Singapore-based reinsurers are concentrating on providing excess of loss protection for catastrophic perils, having removed these perils from their proportional treaties. Those reinsurers that continue to provide proportional coverage for catastrophes are doing so only with minimum primary rates that are considerably higher than the prevailing market rates.

Reinsurers and brokers are also promoting a number of new products that include a financial element. An example would be finite risk funding covers or coverage for catastrophe events. With the uncertain

Asian financial marketplace, these products are generating a high level of interest. However, their complex pricing structure has meant that not many such products have been sold.

In the past few years, there has been much more of a demand for directors and officers reinsurance; and as I mentioned earlier, most publicly listed Asian corporations now have this coverage.

GCV: How would you characterize Singapore's role in the alternative risk transfer (ART) market? What has been the impact of efforts by the MAS to strengthen this role?

AH: The MAS has been promoting Singapore's role in the ART market and has held numerous ART conferences to augment everybody's awareness. In addition, the MAS has issued some framework guidelines for ART that cover such areas as contract wording, accounting treatment, and the collection of adequate information with which to assess a company's financial position.

Despite the promotion of ART by the MAS, this market was slow to take off due to the complexity of pricing these products. However, it is slowly gathering momentum.

GCV: What about the price of reinsurance? Has this changed much over the past few years?

AH: On average, prices at 2003 renewals reflected increases of between 10 to 15 percent over 2002. Facultative rates have been softening, however, and further price reductions were expected at 2004 renewals.

As we enter the 2004 renewals, we are seeing some reductions in pricing; and large well-managed individual property risks are securing significant rate reductions, ranging from 25 percent to 50 percent. This type of pricing fluctuation is a concern to all parties in the insurance/reinsurance industry.

Singapore's Captive Insurance Industry

GCV: What are some of the reasons behind Singapore's development as a captive domicile?

AH: As of the end of 2003, 51 captives have been formed in Singapore. Among the reasons for Singapore's development as a captive domicile are its efficient legal framework and effective business environment. In addition, some tax incentives exist that are appealing to the large institutions that typically form captives. Singapore's consistent monetary policy also remains an attraction.

Guy Carpenter's Role

GCV: What is Guy Carpenter's role in the market? How is this role likely to change in the future?

AH: Guy Carpenter plays a leading, proactive, and integral role in the market, with a large and quickly expanding portfolio supported by a growing team of industry specialists.

We have a fully integrated treaty and facultative reinsurance operation, with a staff of more than 25 professionals providing advice and transactional capabilities across a wide breadth of business classes, including property, engineering, marine, accident, and liability.

Our advisory role is likely to be further enhanced by the more widespread use of dynamic financial analysis, as buyers and their needs become increasingly sophisticated. Guy Carpenter has the expertise and the resources necessary to respond to the growing needs of clients throughout Asia.

The Future

GCV: Are you optimistic about the growth of this market? What are some of the new opportunities that are likely to develop for reinsurers in the region? How is Guy Carpenter preparing for the future?

AH: We're very optimistic. Guy Carpenter expects solid and continued growth in Asia, not only in the traditional areas such as property catastrophe but also in specialty areas such as health care and FINPRO products.

Singapore is our regional reinsurance center for Southeast Asia, so as countries such as Malaysia, Indonesia, Philippines, Thailand, and the Indian subcontinent become deregulated, opportunities for the market continue to grow.

Guy Carpenter is preparing for the future by having in place a network of offices across all of Asia, employing the most experienced and knowledgeable brokers in the industry supported by a cohesive team of service support staff second to none.