THE TRADING FLOOR INTERVIEW

Milliman actuary Steve Schreiber has been at the spearhead of many life insurance innovations. He shares his view of the resurgent life securitisation markets and expansion possibilities for longevity with *Trading Risk*…

1 WHERE DO YOU SEE THE LIFE INSURANCE-LINKED CAPITAL MARKETS SECTOR IN 12 MONTHS TIME?

I expect to see more innovative transactions as we did in several capital market deals from last year, including Swiss Re's Kortis longevity trend bond, Aetna's Vitality Re morbidity [health insurance] cat bond, and Goldman Sachs' and Swiss Re's extreme mortality offerings. These transactions helped the insurance company issuers meet their objectives and provided investors with investment opportunities potentially not correlated with their portfolios.

However, most of the $7bn life deals completed in 2010 were private deals relating to redundant reserve financing (XXX and AXXX transactions). Most of these were structured with banks providing letters of credit in support of the redundant reserves, but other approaches were also used. I expect to see these kinds of transactions continue in 2011, as they allow companies to release capital that is tied up to support very conservative reserves.

While there is some discussion about a return of XXX securitisations, insurers need to see a cost-benefit advantage for doing such transactions and bankers need to identify investors interested in investing in what is generally a very senior risk.

Certainly, I expect continued development on the UK longevity side, given the significant need for a solution, with the biggest challenge finding buyers who want to own exposure to longevity risk.

Standard & Poor's recent statement that it may be willing to rate life settlement securitisations under certain circumstances means that we could see some of these transactions this year.

2 AND IN FIVE YEARS TIME?

The big unknown is what the impact will be of various regulatory and accounting changes currently being discussed, many of which will be in the process of being brought into force in five years time. Such changes include Solvency II and IFRS in Europe, IASB and FASB convergence, principle-based reserves and new capital requirements in the US, and opportunities for reinsurers from new US collateral rules and Dodd-Frank [the Wall Street Reform and Consumer Protection Act].

But I certainly expect there to be ILS opportunities once all of the changes are understood, including possibly more embedded value or value-in-force deals, which securitise life insurers' future profits.

And I expect significant expansion of longevity trades beyond the UK, moving onto the European continent and also to the US.

"Insurers are concerned about pandemic-type risk. There's an extreme mortality need that's not being fulfilled and we need to find better solutions"

3 WHAT FACTORS ARE SHAPING THE DEVELOPMENT OF THE LIFE SECTOR CURRENTLY?

Some insurance company issuers are being slowed down by uncertainty on regulatory reform, along with uncertainty about the impact of Dodd-Frank and revised collateral rules.

I also get a lot of inquiries from insurance and reinsurance companies that are concerned about pandemic-type risk.

But these companies also have concerns about the perceived high cost and the current small market size for issuing extreme mortality bonds.

There's a need that's not being fulfilled. We need to find better solutions because these companies really are concerned about extreme mortality risks.

From the buy-side, we need more education of potential investors to help them understand the nature of the mortality and longevity risks they are being asked to take and why they should be interested in taking such risks.

4 WHAT KEEPS YOU AWAKE AT NIGHT?

Most nights, I sleep pretty well, but as consultants, we need to constantly be reinventing ourselves so I do spend some nights awake thinking about new cutting-edge services we can provide to our clients.

I think that last year was a good year, but mostly in the private redundant reserve financing market. We saw several attempts last year trying to bring life deals back to the capital markets, but progress is still slow.

And the recent catastrophes around the world will impact both the life and non-life ILS markets.

Any situation where investors see that they can lose money increases the cost of these transactions as it increases the pricing conflict between investors and issuers.

5 IF YOU COULD MAKE ONE IMPROVEMENT TO THE WAY THE INSURANCE-LINKED MARKET FUNCTIONS, WHAT WOULD IT BE?

More information. Most of the early life transactions involved a monoline wrap and very little consideration was given to secondary market trading.

As such, there is limited information available on those transactions to allow investors or potential investors to make an informed decision.

Further significant development of the life ILS market is dependent on seeing more information being made available in a uniform structure to help investors evaluate the transactions.

Such information should include annual profit/loss statements, explanations of deviations from expected results – either positive or negative, experience studies, and updated deal modelling.

CV

Steve Schreiber is a principal and consulting actuary with Milliman. He co-manages the life insurance consulting practice in the firm's New York office, including advising on redundant reserve securitisations, longevity deals and mortality cat bonds. He joined the firm in 1986