

**HOLDING STEADY:** Despite shrinking market volume in the U.S. life reinsurance segment, RGA's Anna Manning watched her company stay relatively level on 2010 revenue and actually increase its market share.

# Finding the Bottom

Steady decline continues for life reinsurance cession rates, according to the latest industry survey by Munich Re.



Photo courtesy of RGA by Matthew Plexman Photography, Ltd.

by Al Slavin

Anna Manning would like to be able to point to something that indicates the declining cession rate in the U.S. individual life reinsurance market has reached a bottom.

The difficulty, as she simply puts it, is that nothing she can point to would suggest that.

An annual Munich Re survey of reinsurers revealed that the amount of individual life business ceded to reinsurers dropped to 30.2% in 2010, down from 34.2% a year earlier.

Manning, an executive vice president and the head of U.S. markets for RGA, said she won't be surprised if the overall cession rate declines again in 2011.

Just when that bottom may be reached, and its subsequent potential impact on the U.S. individual life reinsurance market, could beg a larger question.

"Right now, there are approximately a dozen life reinsurers in the market actively writing new business," Manning said. "If that cession

rate continues to fall off, how many reinsurers can have a viable presence in the U.S. market?"

William Pargeans, an assistant vice president with the A.M. Best Co., said the level of the drop-off was somewhat steeper than anticipated.

"While cession rates have been declining in recent years, we didn't expect the cession rate to fall as much as it did from 2009 to 2010," Pargeans said. "There's clearly less business being reinsured and that may be partly explained by lower term sales and direct writers retaining more risk. We'll continue to look at this trend and closely monitor recurring premium levels to see what kind of impact it will have longer term on insurers' top line growth and, ultimately, profitability."

There is some glimmer of light in terms of new business. A May 2011 survey from Limra indicated that new annualized premium from individual life sales was up 8% in the first quarter. Still, it probably is not enough to crowd out the long

## Key Points

- ▶ **The Trend:** Cession rates for the life reinsurance market continued to decline in 2010.
- ▶ **The Background:** New premium was up for direct market writers in the first quarter, but challenges persist.
- ▶ **What It Means:** Shrinking business volume will pose challenges for life reinsurance markets.

shadow of consistently declining cession rates.

The more telling data for U.S. life reinsurers was generated through Munich Re's recent *Life Reinsurance Survey*, prepared annually on behalf of the Reinsurance Section of the Society of Actuaries.

According to the survey, the volume of recurring reinsurance business declined 15.3% in 2010 to just under \$505.5 billion.

Last year marked the eighth-straight declining year for the category, which has dropped off by \$500 billion since 2004.

David Bruggeman, an assistant

vice president and actuary with Munich Re, said the other key statistic last year involved declining retrocession levels. Reinsurers in the segment generated just \$7.2 billion in retrocession cover in 2010, down from \$42.6 billion five years earlier.

“I went back and looked through the past 25 years and didn’t see retrocession levels that low,” Brugeman said.

The survey reports the concentration of recurring-business market share among the top echelon held steady again last year, but Generali USA Life Re managed an 11% increase in production and moved ahead of three competitors—Transamerica Re, Swiss Re and Munich Re—to secure the No. 2 position behind RGA. After acquiring the business of Transamerica Re from Aegon NV, Scor said it would become the second-largest life reinsurer in the United States.

That churn among the top five writers has been a constant, given that an 82.5% share of a dwindling market remains concentrated in that tier, according to the survey.



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A.M. Best Co.

### Market Analysis Is Key

Despite the fact that RGA’s new business production slipped by less than 1% to \$133 billion in 2010, the St. Louis area-based life reinsurer increased its market share by almost 4%.

Manning said RGA’s ongoing objective is in executing on what she feels has differentiated it in the North American market: It’s not just about price, but the research, analytic support and other expertise that she feels has fueled the reinsurer’s dominating presence in North America’s life reinsurance market and the U.S. facultative market.

Manning said although it’s hard to get statistics on the facultative segment because there’s no official reporting source or database, “anecdotally, we believe that we underwrite twice as much (faculta-

tive) business as our next leading competitor.”

Like other life reinsurers, RGA is also contending with the fact that many direct writers have grown more comfortable with risk and have become less apt to cede it. When they do obtain reinsurance, they are more inclined to do so through excess arrangements that protect against volatility.

“Those are two key factors contributing to the more recent falloff that you’re seeing in reinsurance cessions over the last decade,” Manning said.

According to the Munich Re survey, that cession rate for the decade peaked at 61.5% in 2002 and the volume of reinsurance business was twice its current level.

Toward the middle of the decade, a combination of rate hardening and the tightening of terms and conditions helped offset some questionable underwriting activities employed by a minority of companies, according to one seasoned executive.

Chris Shanahan, executive vice president, Mortality Solutions, for Hannover Life Re, said it had become common for some direct writers to lay off 90% of certain risks.

“There was no question that for some companies, again it was the minority, but for some companies, the fact that they weren’t keeping much of the risk led to a meaningful loosening of their underwriting integrity,” Shanahan said.

Additional controls and parameters that flowed from a tightening of terms and conditions didn’t sit well with the direct writers that hadn’t been abusing the situation. At the same time, Shanahan said, the capital

## U.S. Recurring by Company

This market breakdown shows the shifting that occurred between 2009 and 2010 among reinsurers focused on the individual life market.

(\$ million)

Company	2009		2010		Change in Production
	Assumed Business	Market Share	Assumed Business	Market Share	
RGA	\$133,591	22.4%	\$132,936	26.3%	-0.5%
Generali USA Life Re	70,023	11.8%	77,782	15.4%	11.1%
Transamerica Re	107,834	18.1%	76,039	15.1%	-29.5%
Swiss Re	114,752	19.3%	70,599	14.0%	-38.5%
Munich Re (US)	80,564	13.5%	59,157	11.7%	-26.6%
Hannover Life Re	19,361	3.2%	24,971	4.9%	29.0%
Canada Life	19,191	3.2%	19,698	3.9%	2.6%
Scor Global Life (US)	17,503	2.9%	16,535	3.3%	-5.5%
General Re Life	10,088	1.7%	10,041	2.0%	-0.5%
Ace Tempest	10,265	1.7%	6,478	1.3%	-36.9%
Wilton Re	7,168	1.2%	5,264	1.0%	-26.6%
Optimum Re (US)	4,855	0.8%	5,034	1.0%	3.7%
RGA Re (Canada)	400	0.1%	428	0.1%	7.0%
Employers Re Corp.	281	0.0%	0	0.0%	-100.0%
<b>Total</b>	<b>\$595,876</b>		<b>\$504,962</b>		<b>-15.3%</b>

Source: Munich Re/Society of Actuaries life reinsurance annual survey



Reinsurance/Capital Markets

markets began making a more serious play to provide financing directly to direct market writers, negating the need to finance reserves through a reinsurance option. He said most of the biggest writers of term insurance now deal with this in solutions that they have developed on their own.

Hannover Life Re adjusted to this market need through a strategic maneuver deployed through its financial solutions group.

“What we found is, if that’s the model, let’s not fight it,” Shanahan said. “There’s nothing wrong with it. It’s not necessarily a better answer to load up your balance sheet with all the financing needs of all these direct writers and then have to go out and find a solution for it.”

He said that capital markets and banks have become viable customers to work with, given their interest in assessing the risk on a first-dollar basis. Hannover Life Re is then positioned to work with risk committees and potentially underwrite any excess coverage that may result.

“We’ve done a couple of transactions that have a variety of flavors



“Ceding companies ... want solutions to much more than mortality risk and they want an efficient way to access these solutions.”

—Mark Hvidsten,  
Willis Re

around that,” Shanahan said. “What we’ve tried to say is that with the capabilities that we have, we need to look to utilize them in a different way or different order to meet the needs of the market.”

Shanahan said his company isn’t the only one with this approach, but has managed to eke out ahead. While it marks a growth opportunity, he described it as a solution for the top writers in the industry and not something that would necessarily yield dozens of deals each year for life reinsurers.

Hannover Life Re did manage to increase its traditional life production 29% to just under \$25 billion, leaving it well beyond that tier of top-five writers. While it was good enough for a 5% market share in

2010, Shanahan said he envisions that market share striving toward 10%. He believes Hannover Life Re’s in-force scale, platform and capabilities will enable it to compete with that top tier for business.

He also thinks that a shrinking market base may prove challenging for companies that based their infrastructure on assumptions that call for a much larger market size.

“We built our business and staffing model around the assumption that the market is like it is today,” Shanahan said. “So we’re right-sized for what we think the market opportunity is today.”

Shanahan isn’t the only one seeing opportunity in the life reinsurance market. Willis Re launched its Life Solutions Group in May to focus entirely on this segment. The team will initially focus on North America and be led by three senior vice presidents: Rick Hodgson, Mike Kaster and Brian Holland.

Mark Hvidsten, executive vice president and managing director at Willis Re, said there is a market trend toward buying less traditional mortality reinsurance.

**Direct Market Challenges**

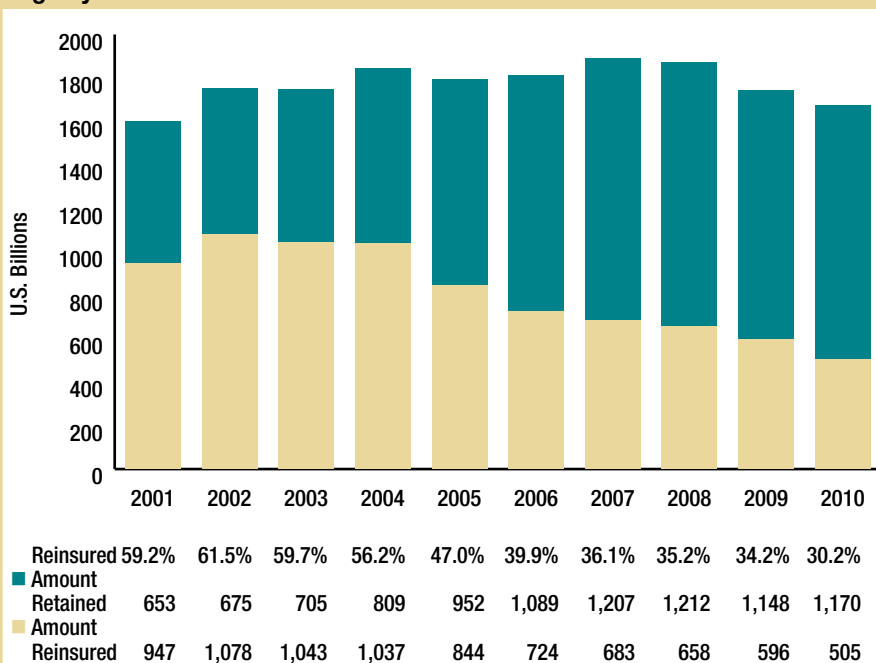
In an email response to questions, Hvidsten stated that companies are increasing retentions and the predominance of first-dollar quote share reinsurance is significantly less.

“Ceding companies require a higher level of performance and economic value from their partners,” Hvidsten stated. “They want solutions to much more than mortality risk and they want an efficient way to access these solutions.”

Hvidsten added that Willis Re’s new practice is looking to position

**Steady Decline**

Individual life insurance business ceded to reinsurers continued its eight-year descent in 2010.



Source: Munich Re/Society of Actuaries life reinsurance survey

itself as an analytical resource that can not only quantify risk, but help execute on custom-made solutions.

The kind of approach is not new to RGA. Manning cited a need for reinsurers to remain flexible, nimble and to serve as an analytical resource, given the significant challenges that face the direct market.

The past decade has seen very low growth in direct sales. However, there is a material segment of the population that does not have insurance.

Manning cited the 2010 *Trends*

*in Life Insurance Ownership* study, conducted every six years by Limra, that showed 30% of U.S. households lacked life insurance in 2010, up from 22% in 2004.

She said direct market writers are trying to balance the needs of retail customers, agents and company owners or shareholders. Regulatory reform has generated questions about the viability of existing direct products and the potential for increased compliance-related costs.

Underscoring all of this is the

need to capitalize on technology in ways that improve the underwriting selection process and generate cost efficiencies.

“Add on the aging of their traditional sales force, and direct writers will really have to find new products and new ways to distribute those efficiently,” Manning said. “We have an industry, in my opinion, where the winners are going to be those that can identify, create and deliver these innovative solutions quickly and cost-effectively.” **BR**

## What's New

### Individual life reinsurance new business production:

	U.S.			Canadian		
	2009	2010	Change	2009	2010	Change
<b>Ordinary Life</b>						
Recurring	\$595,876	\$504,962	-15.3%	\$152,343	\$153,032	0.5%
Portfolio	776,710	94,236	-87.9%	437	1,437	228.8%
Retrocession	14,817	7,226	-51.2%	731	1,380	88.8%
<b>Total Ordinary</b>	<b>1,387,403</b>	<b>606,424</b>	<b>-56.3%</b>	<b>153,511</b>	<b>155,849</b>	<b>1.5%</b>

U.S. Figures in \$US millions, Canadian figures in \$CD millions  
Source: Munich Re/Society of Actuaries Life Reinsurance survey

## Learn More



### Hannover Re AG

A.M. Best # 85070

Distribution: Direct and reinsurance brokers

### Munich Re Group

A.M. Best # 86577

Distribution: Direct and reinsurance brokers

### RGA Reinsurance Co.

A.M. Best # 09080

Distribution: Direct

For ratings and other financial strength information visit [www.ambest.com](http://www.ambest.com).

