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Low Levels of Risk Retention

Market observers have tended to describe local insurers in the Gulf region as being "risk traders" rather than "risk takers" due to their high cession rates.

Indeed, much of the insurance in the local market is a pure front for the international reinsurance markets. As described by Lloyd's, the practice of fronting is common even though some authorities in the region have expressed their disapproval. "In agreeing to front a large insurance programme, the local insurer is undertaking a significant risk. At the underlying insurance level, the policy issued by the local insurer is usually for 100% of the risk," it added. New regulations aimed at combat fronting across the commercial spectrum were supposed to have come into force in the UAE last November. However, till now, no such action has been taken.

Mr Andreas Weidlich, General Manager of Reinsurance at Arig said that, while compulsory cessions to domestic or regional participants in the market may have nationalised gross premium, it has done little for the industry.


Mr Andreas Weidlich

He attributed this to two reasons. Firstly, much of the "national retention" continues to end up in the books of the global reinsurers. "This could be in the form of retro or as inwards facultative reinsurance in the treaty programmes of local primary insurers. Even when increased shares are distributed within the same market, risks will not be spread but tend to accumulate.

"Secondly and more relevantly, it is the ultimate net exposure to risk which will drive a company's professionalism. If my balance sheet is more exposed because I decide to run higher net retentions, I need to make sure the additional risk is worth my while and write it at sound terms.

"Going forward, the answer may not lie in protecting markets, but in opening them. Local insurers need international expertise, and global players cannot do without local know-how. If that means that primary insurers have international shareholders – then so be it."

So what can be done to raise net retention?

Regulations

Elaborating on the regulatory role, Mr Weidlich recommended: "We have seen governments introduce minimum risk transfer benchmarks as a qualifier to allow for expense accounting. Why not use a similar approach and require minimum net retention to distinguish true reinsurance from fronting, and allow those cessions different treatment? This would be a strong incentive for smaller companies to merge, to develop in-house resources, make better use of capital and compete based on healthy professional. Risk retention should be at the core of our industry."

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MEIR Magazine - September 2008

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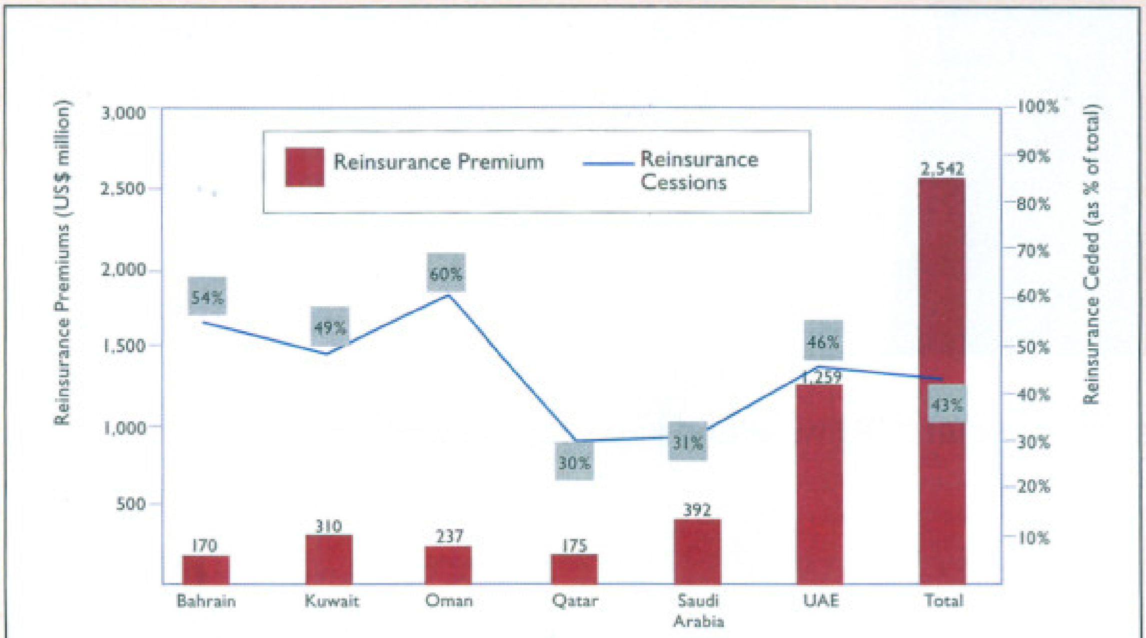

Source: Arig