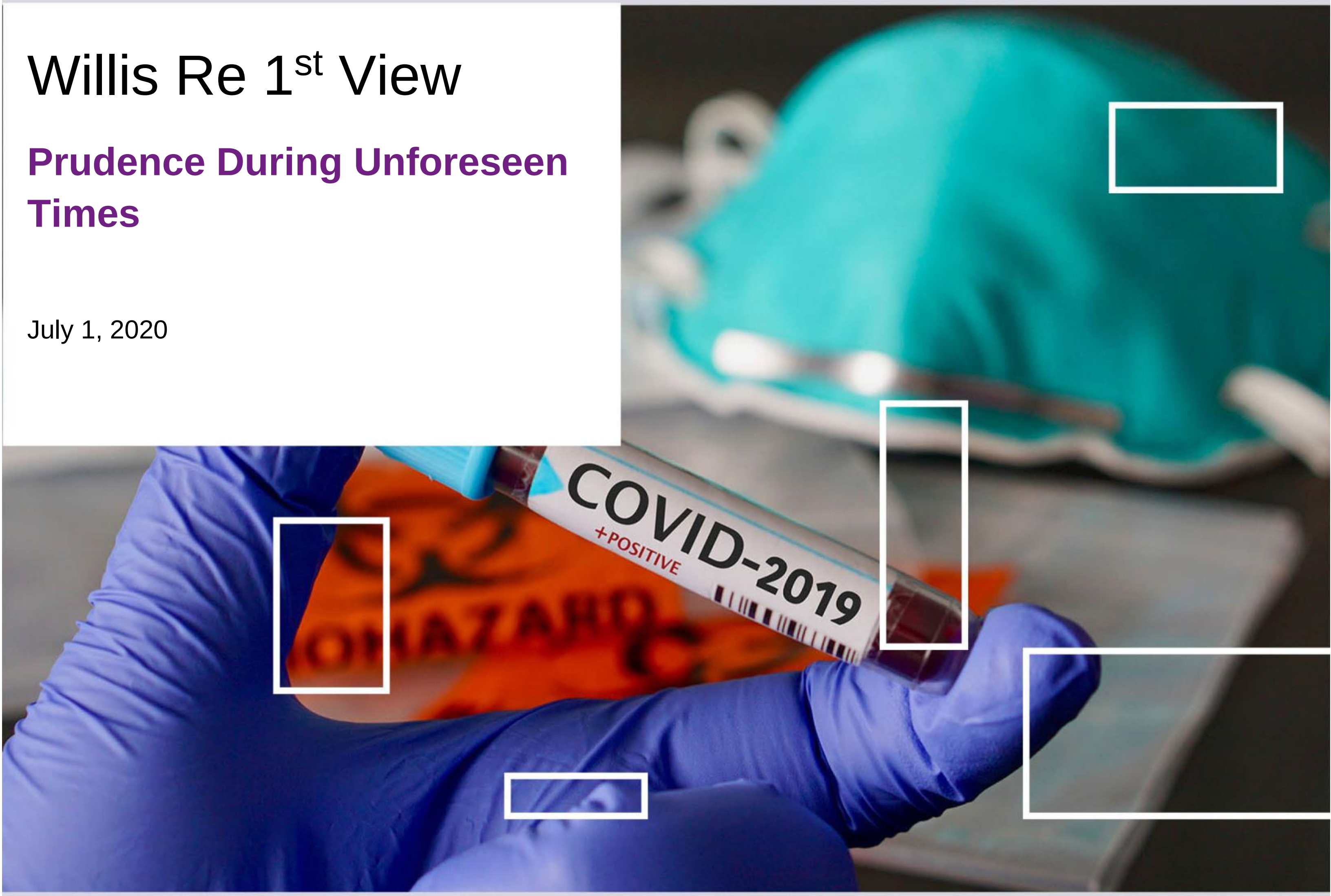
Willis Re

Willis Re 1st View

Prudence During Unforeseen Times

July 1, 2020



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1st View

This thrice yearly publication delivers the very first view on current market conditions at the key reinsurance renewal seasons: January 1, April 1 and July 1.

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Prudence During Unforeseen Times

Q2 2020 has witnessed a remarkable recovery in the capital base of the global reinsurance market as investment markets rebounded and investors showed real appetite to commit additional equity and debt to both incumbents and starts up companies. Current estimates of the reduction in the capital base of the global reinsurance industry are now down only 5% by the end of June when compared to the end of December 2019 and the 30% drop witnessed at the end of March 2020. A combination of investments recovering, circa $16bn of new COVID-19 related capital raises and cash conservation strategies have driven the rapid recovery.

In addition to these three factors, a number of companies are seeking to deploy alternative risk transfer mechanisms to offload back-year liabilities to free up capital. Consequently, the global reinsurance market is currently not capital-constrained but is increasingly focused on underwriting profitability.

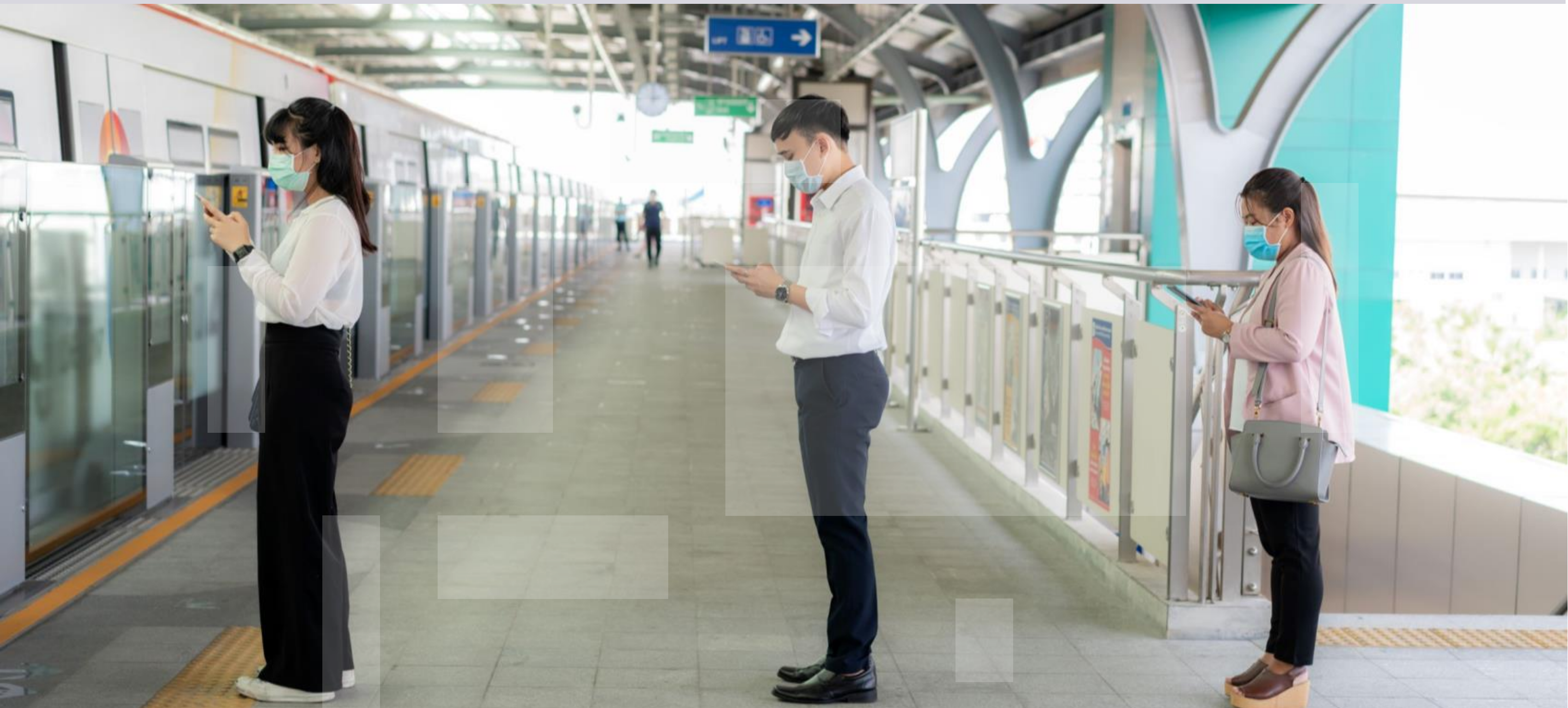
This approach, outlined in previous 1st View updates, has gained momentum and was in clear evidence during the 1st June and 1st July renewals.

The global reinsurance market is currently not capital-constrained but is increasingly focused on underwriting profitability

COVID-19 loss uncertainty remains a major topic with only $7bn of losses announced to date versus top-down market insured loss estimates in the range of $30bn to $130bn. There is a growing realization that the full extent of COVID-19 related losses will take time to fully emerge which will allow reliable claims reserves to be set, as well as dispersing losses across multiple quarters. Some commentators are suggesting that COVID-19 related loss developments will drag onto 2022 or 2023. COVID-19 exclusionary language is now widespread across many lines, either in original policy wordings or in treaty contracts, and was a key element in obtaining reinsurers support. However, a bit like price changes, the exclusions were not managed in a 'one size fits all' approach with a bespoke methodology client by client.

The longstanding underlying issues of rate inadequacy in some lines of business, driven by poor loss records and loss creep, remain the key drivers of market hardening pressures as they have done over the last couple of years. The recent civil unrest in some mature markets has given rise to concerns over SRCC exposures with reinsurers looking to apply the same underwriting approaches they have developed over the years in less well-developed markets, but to date the impact remains relatively muted.

While the market is now showing signs of more persistent hardening, the approach from reinsurers remains logical and measured with clear differentiation between clients, lines of business and territories. In

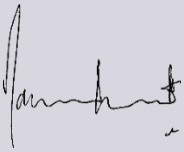


many cases where reinsurers are supporting their clients through proportional reinsurance contracts, they have been prepared to leave reinsurance treaty terms and conditions largely unchanged if the primary business being ceded is showing significant improvements in original pricing and conditions. Furthermore, the price adjustments seen in the International treaty market continues to lag many areas of the US treaty market.

Despite a reduction in over-placements on some lines of business and territories, ultimately insurers were able to secure sufficient reinsurance capacity at the 1st July and 1st June renewals. Strong client centric underwriting, which was less of a feature in the market dislocations seen in 2001 and 2005, was evident on a wide range of placements but in some cases, and in particular in Florida, private placements and differential terms appeared for the first time in many years.

One area that is more disrupted is the ILS market. Investors have continued to withdraw capacity from several funds and been much more selective in deploying capital, with the stronger, well-established reinsurers and funds proving the beneficiaries of the limited new capital that was available. The bearish view of investors, already wary following the 2017/18 loss creep, was a result of COVID-19 being the first reinsurance loss that showed a true correlation between the asset and liability sides of reinsurers' balance sheets. The retrocession market therefore quickly became more complex due to its historic high share ceded to ILS market. As a consequence, mid-year retrocessional buying was more muted as buyers sought other means to manage their exposures and balance sheets.

Overall, the global reinsurance market is maintaining an increasingly determined but logical underwriting approach. Capacity remains sufficient for clients seeking well-structured reinsurance placements and the buyers who have cultivated long-term relationships with their reinsurers are reaping the benefits not available to companies viewed as less appealing or distressed. Facing the rigors of the North Atlantic Hurricane season and the development on COVID-19 related losses, the global reinsurance market finds itself better positioned to provide stable long-term support than many may have dared to hope only three months ago.



James Kent, Global CEO, Willis Re
July 1, 2020

Property

Commentary by territory

Australia

- Abundant capacity available, however reinsurers were firmer in their demands on terms and conditions.
- Any perceived rate discounts were immediately declined, and flat renewals more difficult to achieve. Rate increases, even on non-loss affected Catastrophe layers, became more prevalent and a requirement for many reinsurers.
- Reinsurers were prepared to cut capacity or decline renewals if perceived pricing adequacy was not achievable. This capacity could be replaced, but often with reinsurers waiting for improved terms.
- A number of reinsurers actively sought to move away from loss affected lower layers and move further up the program.
- Significant rate increases for subsequent event and aggregate covers, due to both significant loss activity and general reduction in reinsurer appetite for these covers.
- Reinsurers focused on wordings and are reluctant to accept any expansions of coverage. Communicable Disease exclusions became mandatory in order to complete placements.

Caribbean

- Reinsurers were much firmer in their demands for improved terms and conditions.
- Capacity is still available but limited for growth depending on the territory and its correlation with US exposures.
- Reinsurers continue to scrutinize wordings and are firm on the inclusion of Communicable Disease Exclusions.
- Upward movement of original rates has been tempered by the economic uncertainty that faces the region.

China

- Market hardening but leading terms remained competitive.
- Firm Order Terms with sharp risk-adjusted price reductions saw a shortage of following capacity.
- Multi-year excess of loss capacity continued to compete with traditional quotes.
- Infectious disease exclusions are unavoidable in the market, e.g. LMA5394.

Latin America

- Traditional leading reinsurers have been more aggressive in seeking price increases.
- No changes in available capacity and ILS or alternative capital has not been required. However, capacity on new layers has been harder to find than on renewal layers.
- Pro-rata commissions flat to two-point reduction dependent on historic performance.
- Chile observing higher rate increases than the rest of the region due to October-November 2019 Riots losses affecting Property programs and the renewal of key Property Mortgage accounts.
- Some reinsurers continue to seek limitations to terms and conditions in respect of SRCC, such as limits on the

number of reinstatements on XLs or Annual Aggregate Limits in Pro-rata Treaties.
- Infectious disease exclusions have become a requirement and reinsurers require more detailed information about Pandemic exposure in original policies. There is also more focus on Cyber exclusionary language.

Middle East

- Infectious disease exclusions imposed across all lines in all territories despite modest loss expectations.
- Considerable uncertainty on economic outlook arising from pandemic lockdowns compounded by oil price collapse.
- Reinsurer appetites steady but clear signals of a firming market.

South Africa

- Catastrophe XL programs have been unaffected by catastrophe losses this year.
- Continued pressure on catastrophe deductible levels though as the market has enjoyed low retention levels.
- Capacity available was static from 1st January.

United Kingdom

- Despite efforts from reinsurers to push pricing upwards during the quoting stage, Firm Order Terms landed with low-to-mid single digit risk adjusted increases for loss free Catastrophe treaties.
- Given the predominately personal lines nature of this renewal season and a continued absence of large loss activity in the UK, there were few loss-affected Catastrophe XL renewals at 1 July.
- Contagious disease exclusions are being added to all contracts. However, cedants are pushing back against LMA 5394 leading to a variety of different clauses being applied.
- The impact on the market of COVID-19 related BI losses is not yet fully understood, with FCA test case being closely monitored by all parties and greater clarity expected in advance of the 1st January 2021 renewal season.

United States – Florida

- Contracting retrocession market, liquidity preference by investors, and secondary trading of 144A catastrophe bonds reduced reinsurer supply of capacity for Florida focused programs.
- Reluctance to quote early as reinsurers finalized their own view of risk and cost of capital.
- Authorizations delayed as reinsurers anticipated non-concurrent terms/price increases, several cedants reissued firm orders and engaged in private deals.
- Reinsurers looked to control market dynamics by applying tight deadlines on quotes and authorizations. Terms and conditions being pushed by lead reinsurers to remove cascading features, add Loss Adjustment Expense caps, and require co-participations in the program to align both parties' interests.
- Larger percentage increases observed on upper layers and layers impacted by loss creep. Lower layers observed pressure as a result of significantly reduced reinsurer appetite, especially on associated reinstatement premium protection covers.
- New capacity difficult to acquire at June 1, often requiring noteworthy premium increases. All factors led to an average rate increase of 20%-30% with some significant outliers by layer.

United States – Nationwide

- Pro-rata seeing pressure on ceding commission and occurrence limit multiples. Reinsurers are pushing back on the need for high occurrence limit multiples and seeking improved PML to Premium metrics.

- As the Q2 renewals progressed, reinsurers hardened their position with regard to Communicable Disease (CD). By June, the market was broadly applying CD exclusions using LMA clauses as the most standard, however some bespoke exclusions do exist. For pro-rata accounts some treaties did not contain any CD exclusions with reinsurers following the fortunes.
- On top layers reinsurers were seeking higher minimum rates on line, especially when correlated with peak Catastrophe exposures. Treaties with more regional specific exposure were more insulated from this impact.
- While capacity remained sufficient for traditional catastrophe structures, reinsurer support for non-traditional structures such as cascading and top/drop layers constricted considerably.
- Some new capacity was available from new market participants as well as additional capital inflows into existing reinsurers seeking to take advantage of a hardening market.

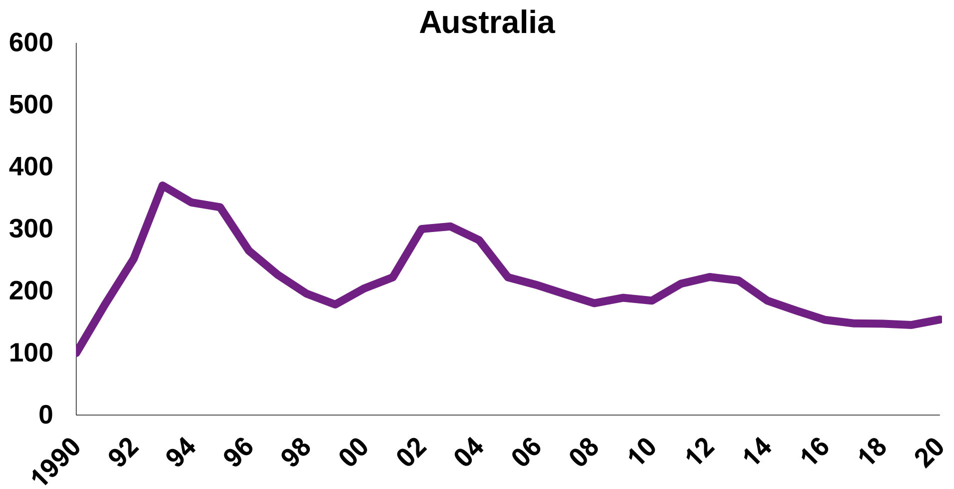
Property rate movements

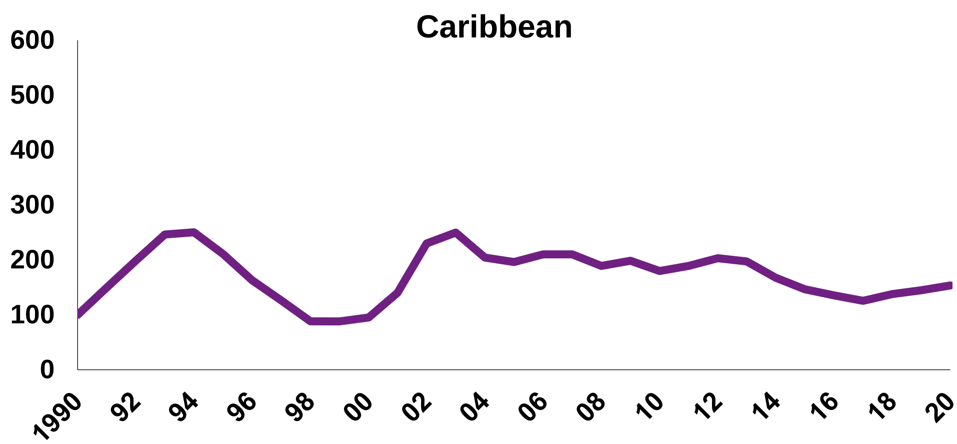
Territory	Pro rata commission	Risk loss free % change	Risk loss hit % change	Catastrophe loss free % change	Catastrophe loss hit % change
Australia	N/A	0% to +5%	+5% to +20%	+2% to +10%	+10% to +20%
Caribbean	-2% to 0%	0% to +5%	+5% to +15%	+2% to +10%	+10% to +20%
China	N/A	-15% to 0%	N/A	N/A	-10% to +10%
Latin America	-2% to 0%	0% to +5%	+5% to +10%	+5% to +15%	+10% to +20%
Middle East	-2.5% to 0%	0% to +5%	+10% to +15%	+5% to +10%	N/A
South Africa	N/A	0%	N/A	-11% to +16%	N/A
United Kingdom	N/A	N/A	N/A	2.5% to 5%	N/A
United States - Florida	-3% to 0%	+5% to +10%	+5% to +20%	+20% to +30%	+25% to +35%
United States - Nationwide	-2% to 0%	+5% to +20%	+10% to +30%	+5% to +20%	+20% to +30%

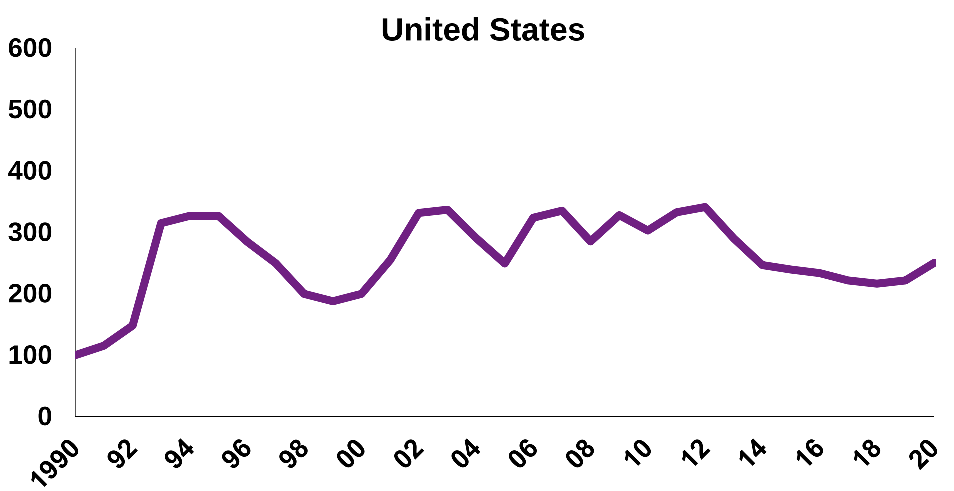
Note: Movements are risk adjusted.

Property catastrophe pricing trends

The charts on these pages display estimated year-over-year property catastrophe rate movement, using 100 in 1990 as a baseline.







Casualty

Commentary grouped by territory

Australia

- The Australian Government reacted quickly to COVID-19 in both social distancing policies and economic support schemes. The OECD estimates a reduction in 2020 GDP of only -5% for Australia.
- Reduced activity & subsequent business closures led to reduced GWP for insurers across most Casualty Lines of Business. Claims activity is yet to fully play out, however some insurers anticipated an increase in small claims frequency for certain Lines of Business.
- The effects of COVID-19 was a major discussion point in most casualty treaties, however after thorough review of the underlying risk, reinsurers generally took a pragmatic approach to underwriting the risk as presented, based upon attachment point & Line of Business.
- There were some instances of reinsurers seeking to limit their exposure to future COVID-19 claims and exclusionary language was imposed on some of the treaties designed to protect against systemic and accumulation risk.
- Casualty rates and some attachment points continued to be under upwards pressure, with any perceived gap between technical rates and achieved rates an ongoing focus of reinsurers. Treaties with adverse loss development saw additional pressure on rates.
- There was a notable shuffling of reinsurers shares on certain treaties with some relationships ending, however for the most part, long term partnerships continued to be important to most reinsurers and buyers alike.

Global – Cyber

- Aggregate Stop Loss pricing trending up as small/medium account loss ratios have increased reducing the buffer between expected loss ratios and stop loss attachments.
- Reinsurance market in US and London market hardening in line with casualty lines but International market remains flat.
- Less support in London market for Managing General Agents.

International – Motor Liability

- There are only a limited number of mid-year renewals in the International arena.
- Despite not being directly exposed to COVID-19 effects, there are signs that the reinsurance market is hardening.
- Excess of Loss rates have increased as much as 25% on loss affected accounts and in the UK, following changes to the Ogden rate.
- Terms and conditions are under scrutiny as well as price, with renewed focus on 'contract certainty'.
- Mixed responses from reinsurers regarding capacity. While some pulled back, others see opportunities.
- Evidence that COVID-19 is having a positive impact on accident frequency and hence on insurance market loss ratios is being tempered somewhat by early signs of increasing claims inflation as lock-downs delay repairs and increase credit hire charges. Although it is also logical to expect the reduced mileage during lockdown to lead to a

reduction in the number of high-value BI claims, these cases tend to take longer to emerge and there is little evidence yet of this anticipated trend becoming a reality.

United States – General Third-Party Liability

- Significant firming of insurance pricing continues, accelerated by COVID-19 environment.
- Reinsurers are still divided, some have increased capacity for a hardening casualty market, others are still wary due to prior year development concerns.
- Client differentiation continues to exist, with significant capacity for those deemed as best in class underwriting carriers and pressure on terms and conditions for others.
- Communicable Disease exclusions being applied on a case by case basis depending on underlying classes of business. Reinsurers applying less pressure when carriers are taking strong positions on original business. Wholesale market responding faster on Communicable Disease than Retail market.
- Continued pressure from reinsurers to reduce outsized gross capacity that a carrier can deploy.

United States – Healthcare Liability

- Reinsurance pricing on healthcare liability continues to firm, although it varies by MPL sub-line of business, original rate change, loss experience, treaty limit and structure.
- Hospital and facility business experienced larger increases than physician and other provider business.
- There was an increased focus on premium to limit balance with reinsurers closely evaluating limit need.
- Carrier response to the COVID-19 pandemic is a critical focus of reinsurers. They have largely followed underlying coverage; standalone nursing home exposures have consistently required exclusions / coverage limitations.
- Overall reinsurance market capacity has reduced somewhat, although ample capacity remains for healthcare liability.

United States – Motor Liability

- Renewals saw a continued 'flight to quality' with the best performing, established programs attracting the best terms, conditions and support. Limited interest for startups and/or new programs.
- Excess of loss rates remain under pressure depending on loss experience. Capacity remained stable.
- Pro rata renewals saw continued downward pressure on ceding commissions.
- Some reinsurers have reduced their appetite and even withdrawn from certain segments like long haul trucking due to poor underwriting experience and continued adverse development.

United States – Professional Liability

- Overall reinsurance market is split into two contingents: those looking to seize opportunity and capitalize on underlying rate movements and those pulling back as a result of continued prior year development.
- Impact of COVID-19 and broader economic conditions are a concern but to date, largely being addressed via questions around underwriting strategy.
- D&O treaties are seeing widest range of outcomes with terms being differentiated by cedants' ability to demonstrate their strategy for improved results, driven by

rate improvements and reductions in deployed limits but also tightening of terms and conditions.
- Miscellaneous E&O is generally renewing with relative ease given less disruption in the underlying business.

United States - Workers' Compensation

- We view the Workers' Compensation reinsurance market as two distinct markets. The working layer market and the catastrophe market.
- The working layer capacity is single life exposed and pricing is established by actuarial weighting of exposure and experience developed rates.
- Working layer pricing continues to increase as reinsurers are offsetting the primary rate decreases as loss costs in excess layers did not decline with the overall industry loss costs. Capacity remains tight but relatively unchanged.
- On the higher attaching catastrophe layers, reinsurers have been quoting slightly higher rates on line, but they are supporting firm order terms at the expiring costs.
- Contract terms have tightened with little working layer capacity available to aggregate communicable disease claims. On catastrophe layers the market is supporting aggregation of these claims.
- The pricing and capacity trends we saw with the January 1 renewals have continued with the July renewal period. However, these terms come with more restricted communicable disease coverage.

Casualty rate movements

Territory	Pro rata commission	XL - no loss emergence % change	XL - with loss emergence % change
Australia	-2.5% to 0%	0% to +5%	+5% to +10%
Global - Cyber	-2% to 0%	-2% to +10%	N/A
International - General Third-Party Liability	N/A	0% to +5%	+5% to +10%
International - Motor Liability	0% to +2.5%	0% to +5%	+12.5% to +25%
United States - General Third-Party Liability	-2% to 0%	0% to +20%	+10% to +30%
United States - Healthcare Liability	0%	+5% to +15%	+20% to +40%
United States - Motor Liability	-2% to 0%	0% to +5%	+5% to +15%
United States - Professional Liability	-1% to 0%	0% to +5%	+5% to +15%

Note: Movements are risk adjusted.

Territory	Pro rata commission	Risk loss free % change	Risk loss hit % change	Catastrophe loss free % change	Catastrophe loss hit % change
United States Workers' Compensation	-3% to -2%	+2% to +5%	+5% to +10%	0%	N/A

Note: Movements are risk adjusted
For workers' compensation risk layers are working layers that include single claimant coverage are actuarially priced and based on both exposure and experience; catastrophe layers that commonly require two or more claimants in the same loss occurrence are primarily priced based on capacity charges.

Specialty

Commentary by line of business

Capital Markets

- Retrocession buyers continue to seek increased capacity from the Cat bond market
- Some primary sponsors chose not to renew Cat bonds given higher spreads and difficulty in transacting in 'work from home environment'
- Further increasing of spreads has been observed following increased global Cat activity and loss development from 2017-2019
- More orderly secondary market following dislocation in Q1 driven by COVID-19
- Very small number of catastrophe bonds face loss exposure to COVID-19

Global — Marine

- Reinsurers are under a lot of internal pressure to achieve increased rates.
- The Marine and Energy market in London is slowly getting harder.
- Pro Rata – from reinsurers' perspective, internal management pressure was for improved commission terms but long-term relationships held sway.
- An otherwise benign renewal was met with unchanged commissions.

Global — Non-Marine Retrocession

- COVID-19 is proving to be a further catalyst for all round market hardening, almost irrespective of Line of Business.
- Significant degree of uncertainty on whether COVID-19 losses will filter through to the reinsurance and retrocession market.
- Reinsurers introducing tighter terms and conditions whilst price hardening has accelerated from those increases applied to programs at 1/1 and 1/4.
- ILS capacity, which has dominated the Retrocession market in recent years, with an approximate market share of 55%, is expected to be constrained in the short- and medium-term due to loss uncertainty, trapped collateral and reduced inflows of capital.
- The ILW market saw an uptick in limit purchased throughout the quarter due to COVID-19/rating agency pressures. Pricing increases were material in some instances where demand outpaced supply.
- Sidecar/Collateralized Quota Share capacity continuing to see a flight to quality in cedant in terms of performance, transparency in reporting and terms and conditions.

Global — Personal Accident / Life Catastrophe

- COVID-19/Pandemic Exclusions being applied unilaterally.
- Loss affected programs, mainly due to travel cancellations, are seeing large increases.
- Still abundant capacity in the market to complete placements at firm order terms.

Global – Political Risk

- Although the of ultimate impact of COVID-19 and the slump in oil price is impossible to predict, a marked increase in Political and Credit Risk losses is expected.

- Underwriters have gone through the process of re-underwriting Non Binding Indications and in some cases, pulled quotes.
- For existing business, portfolios have and will continue to be reviewed and monitored, with special attention given to those industries and countries deemed at elevated risk.
- New deals are being written, but the number of new enquiries being considered are reduced. The expectation is overall premium income to the market will be down 20% to 30%.
- Reinsurance capacity has been reined in, with some reinsurers not prepared to consider new programs and others reducing on existing participations.
- Pricing of reinsurance programs has been very broad, making consensus on placements difficult. As a result, we've seen a number of shortfall covers being requested.

United States – Medical Excess

- COVID-19 did not have significant impact on the Excess Medical Reinsurance market. With the exception of some long-term hospital ICU stays, most COVID-19 claims were below excess attachment points.
- Continued increase in frequency and severity of large medical and pharmacy claims, resulting in market hardening.
- More high cost gene and cell therapies are in the pipeline for approval during the next year, with costs ranging from $1M to $3M per therapy.
- Many markets tough on medical reinsurance claim reimbursements, including denials of Experimental and Investigational treatments.
- Market turmoil continues as a couple of reinsurers have exited the market.

Specialty rate movements

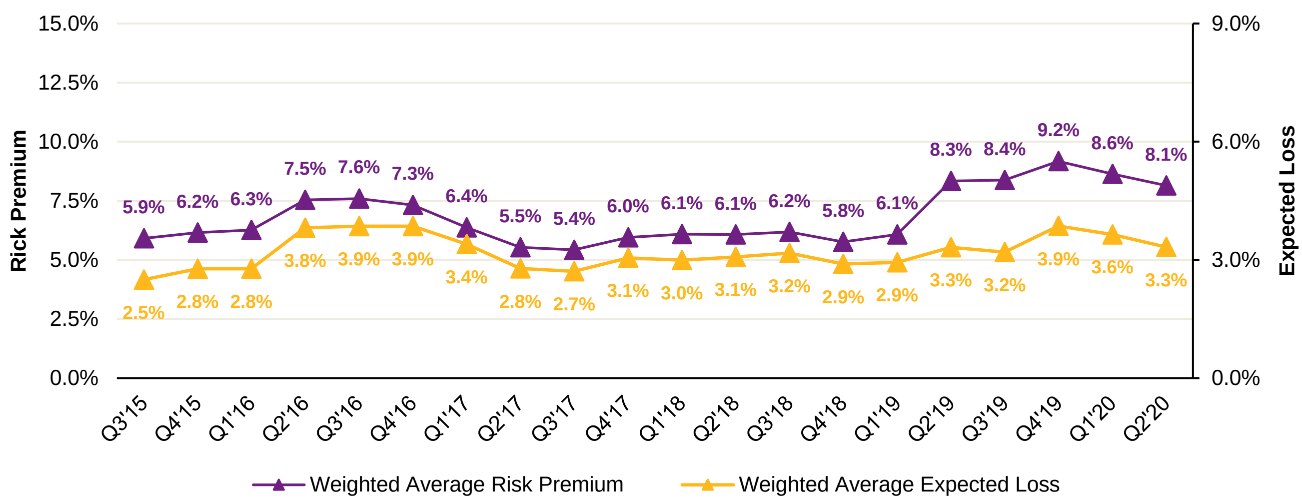
Territory	Pro rata commission	Risk loss free % change	Risk loss hit % change	Catastrophe loss free % change	Catastrophe loss hit % change
Global – Marine	0%	0%	0%	0%	0%
Non-Marine Retrocession	-5% to -2.5%	+10% to +15%	+15% to +25%	+10% to +20%	+15% to +35%
Personal Accident / Life Catastrophe	N/A	+5% to +10%	+15% to +50%	0% to +5%	+10% to +20%
Political Risk	-1%	+5% to +15%	+10% to +30%	N/A	N/A
United States - Medical Excess	0%	0% to +15%	+10% to +50%	N/A	N/A

Note: Movements are risk adjusted.

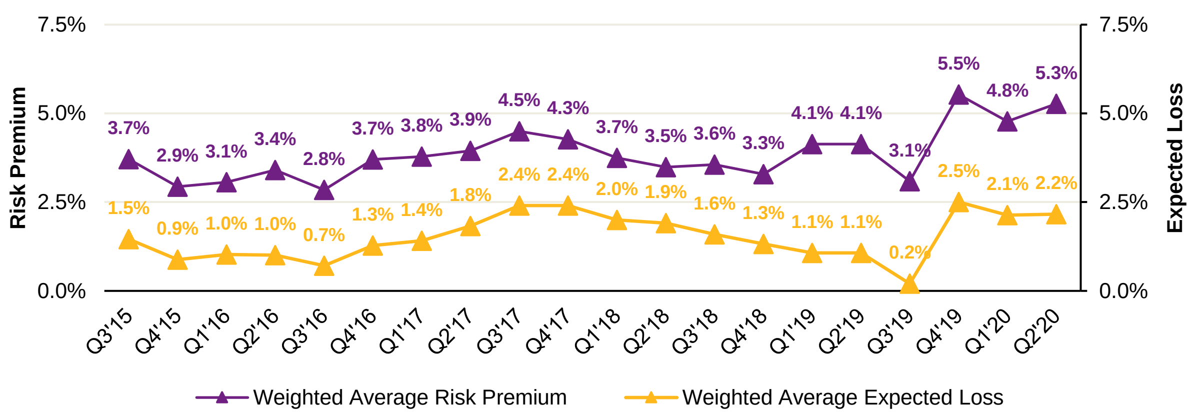
ILS Update

The charts below show the changes in the average risk premium and expected loss for both U.S. wind and non-U.S. wind publicly traded Cat bonds, along with the capacity development of the Cat bond market, and a comparison of the yield on Cat bonds as against two other comparable investment classes.

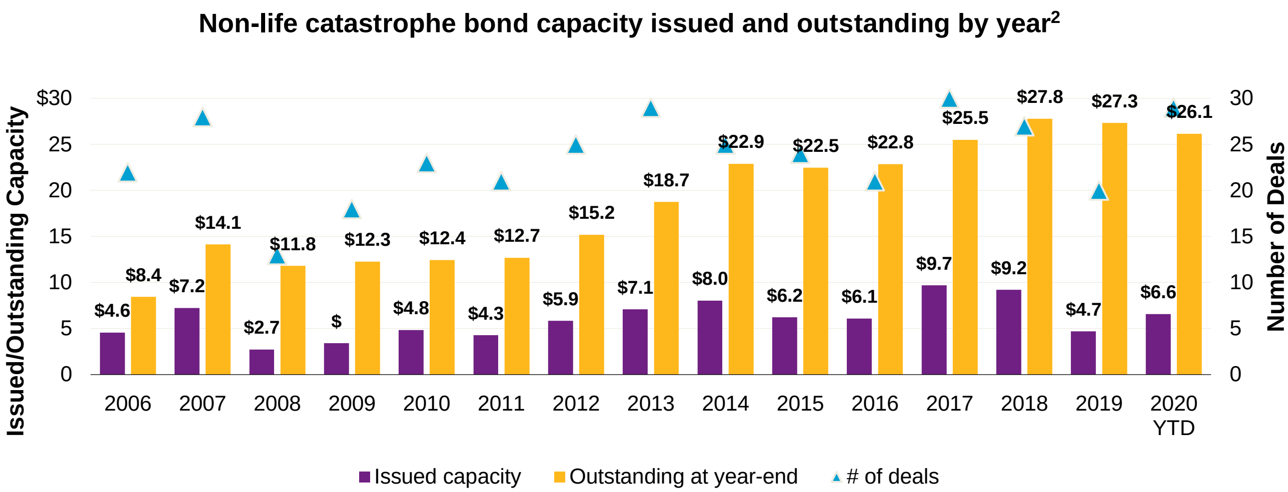
Quarterly long-term U.S. wind exposed weighted average risk premium and expected loss



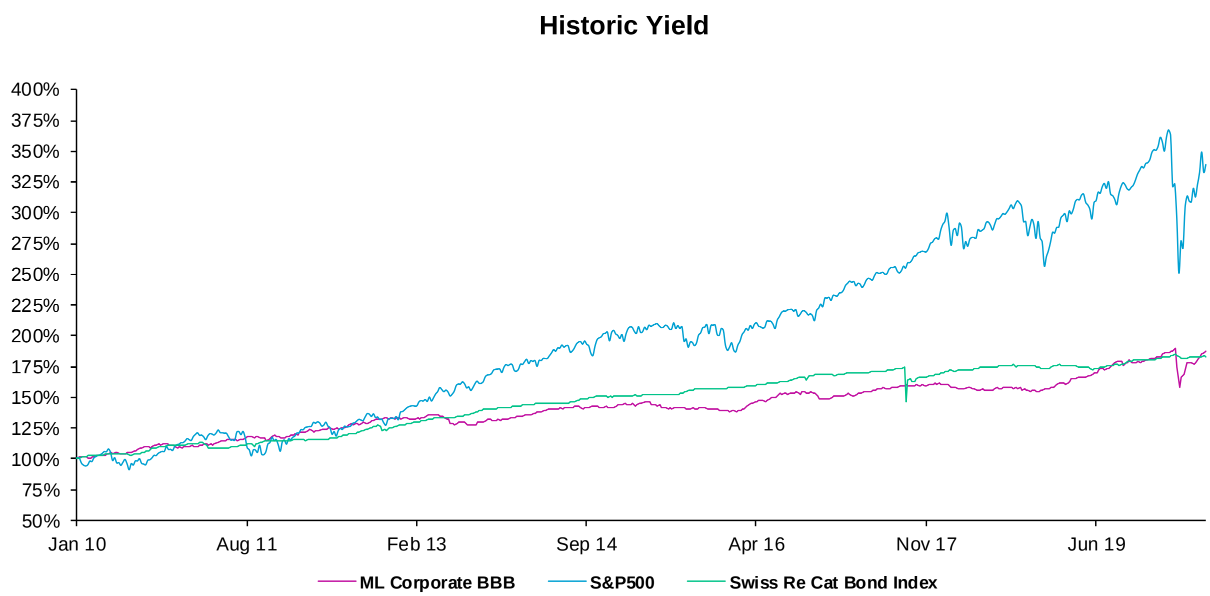
Quarterly long-term non-U.S. wind exposed weighted average risk premium and expected loss[1]



Source: Willis Re Securities Transaction Database as of 7/30/2020. Aggregate data exclude private ILS deals.
LTM = Last 12 months. Aggregate data are for primary issuance and do not reflect secondary trading.
[1] Note that the sharp decline in Q3 2019 expected loss and risk premium is caused by a lack of non-U.S. wind issuances since Q4 2018. Of those that were issued, size, expected loss and spread were relatively low, causing the drop-off in measurement.



Source: Willis Re Securities Transaction Database as of 7/30/2020. Aggregate data exclude private ILS deals.
[2] All issuance amounts reported in or converted to USD on date of issuance. Outstanding amounts adjusted for actual principal losses.



Global and local reinsurance

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For more information, visit willisre.com or contact your local office.

Inquiries

Annie Roberts
Global PR Leader
Investment, Risk & Reinsurance
+44 (0)20 3124 7080
annie.roberts@willistowerswatson.com

Charlie Hinchliffe
Reinsurance Broker, VP
Investment, Risk & Reinsurance
+44 (0)20 3124 8981
charlie.hinchliffe@willistowerswatson.com

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