Research Note:

The ILS market 1.7.2015 – a snapshot

Cat bond market as a proxy for the general ILS market:

- While the reinsurance (RI) market is generally transacting privately and objective market pricing data is hence not readily available (the global reinsurance brokers collect renewal information through their networks, but a substantial amount of data manipulation is needed to distil the information, and the final results are typically published only as a top-level figure), detailed pricing information is available in the 144A public cat bond segment of the general ILS market.
- Though differences in pricing and other parameters temporarily exist between the cat bond segment and the transformed reinsurance market, market efficiency leads to a relatively close coupling of the various parts of the ILS market, with the cat bond market often acting as a leading indicator for developments in the general reinsurance market.
- Current situation: While in 2013 and 2014 the RI market often seemed more attractive than the cat bond segment, 2015 pricing is more or less on par between both segments, with RI contracts often having the disadvantage of broader coverage terms (covered peril types, hour clauses, …) which are not always adequately reflected in the quantitative risk models. Hence investors must take care not to incur higher risk with optimistic modelling when engaging in the RI market.
- Because of the transparency of market information the cat bond market shall serve as a proxy for the current status of the ILS asset class in this analysis.

The cat bond market as of July 2015:

<u>Methodology:</u>

- The analysis is based on the price and market information of the cat bond universe as published by Aon Benfield. The weekly Aon Benfield price information is one of the most important and complete sources of ILS market information and widely recognized by market participants.
- As the measure of return of the individual securities, the average of the bid price and offer price yield was used.

- The analysis was performed for the whole market and the subset of the market with remaining time to maturity of greater than one year. The latter analysis was performed to minimise the seasonality effects on securities for which the remaining risk does not amortise linearly over time, which applies especially to the most important peril in the market, namely US hurricane.

Results:

	Market Size [USD G]	Expected Loss	Yield to Maturity
All Bonds	22.9	1.72%	5.19%
Bonds > 1 year remaining term	17.75	1.69%	5.06%

Observations:

- The current market prices close to a multiple of 3
- As expected, the multiple figure is driven by the low-yielding segments of the market. At an expected loss level of 3% to 3.5%, the multiple is around 2.5, asymptotically dropping to 2 for risk levels of 5% and above.
- Transactions with US perils, especially US hurricane, pay a higher multiple at any risk level than every other peril type.
- While in the cat bond universe a risk level of 3% expected loss or above is only available with US perils, this does not necessarily hold for the reinsurance market as a whole, where junior layers are brought to the market covering various regions and lines of business. However, the general trend of non-US risk paying below US risk remains, meaning that non-US contracts at a risk level of 3% to 3.5% expected loss will generally pay a multiple of 2.5 at most.

Solidum Partners, 8.7.2015

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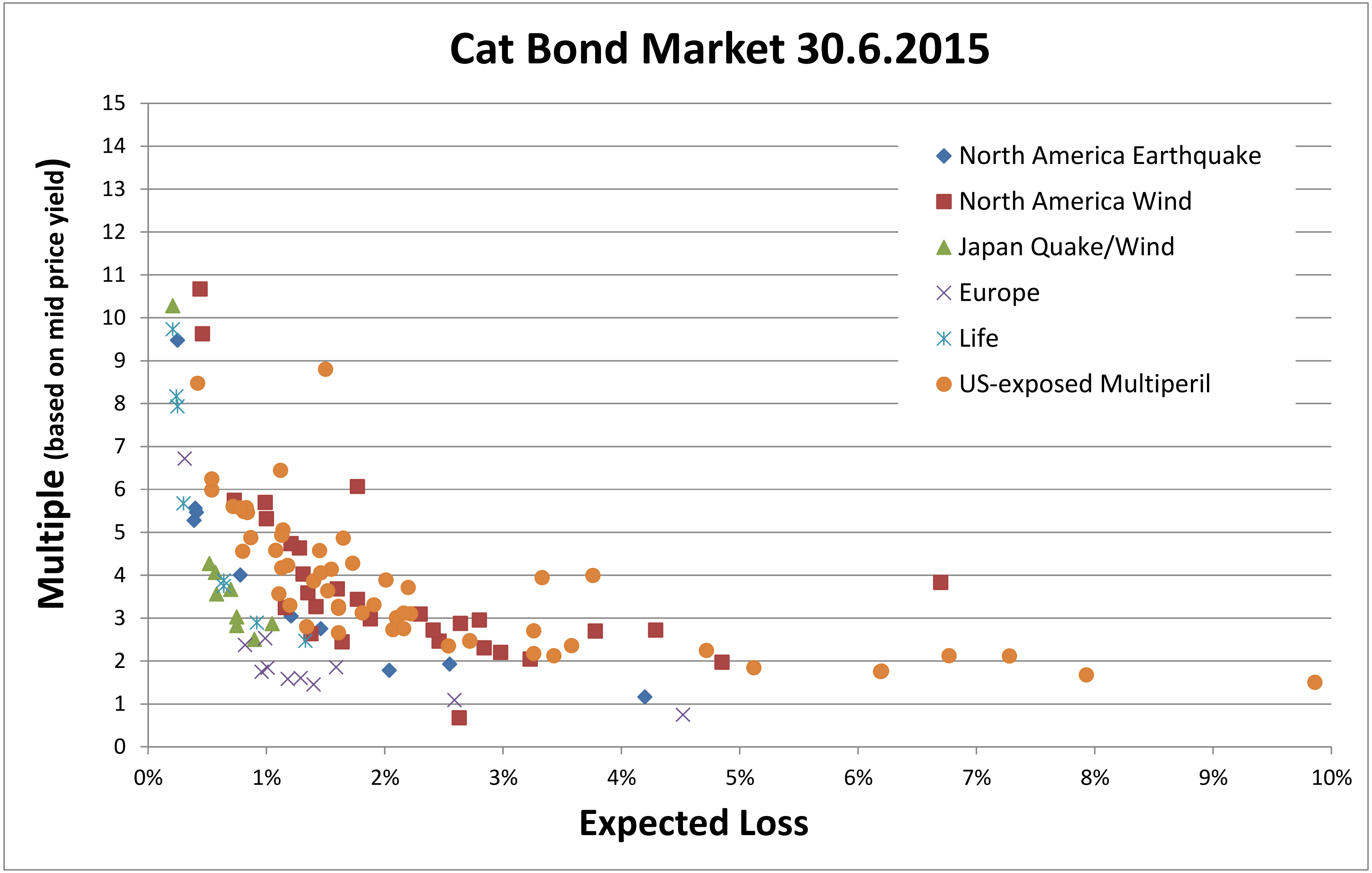

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