



The strength to cover the world's  
leading businesses and financial centers.

INSURANCE | REINSURANCE | FINANCIAL

Visit [www.xlcapital.com](http://www.xlcapital.com)

*The XL Capital group is rated A+ by AM Best\**

\*Rating as of 15 August 2006



FUNDAMENTAL STRENGTH – CAPITAL AND PEOPLE

As seen in

**BusinessWeek**

Special Advertising Sections

© Copyright 2006 The McGraw-Hill Companies, Inc.

Special Advertising Section

# Reinsurance: the Bedrock

## Reinsurance underpins insurance, which underpins a growing world.

On the David Letterman television program two years ago, Dave asked his musical director, Paul Shaffer, if he knew anything about insurance. "No, but I know about reinsurance," Paul quipped. That a bandleader would have even heard of reinsurance, traditionally an invisible pursuit, says a great deal about the way extreme events have propelled themselves into our psyche over the past few years.

Still, the process of insuring risk, when deconstructed, isn't all that complicated. Very few commercial projects get underway without insurance. And very few insurance companies write policies without reinsuring part of the risk. For their part, reinsurance companies accept a share of those risks, and then distribute them further to other reinsurance companies – a process called retrocession. The global reinsurance industry can be seen as a giant economic hazard-control mechanism by which a network of global capital spreads, and thereby blunts, the potentially disastrous effects of risk.

Sharing risk among well-capitalized reinsurance companies allows insurance companies individually to underwrite a small percentage of many different



Robert J. Cooney  
President and CEO  
Max Re Capital Ltd.



Brian O'Hara  
President and CEO  
XL Capital Ltd.



Donald Kramer  
Chairman and CEO  
Ariel Reinsurance Co. Ltd.

# Barbados

For  
Global Insurance

*Looking for a prime location?*

## Look at Barbados!



- **State-of-the Art Legislation**
- **Tax Treaty Business Environment**
- **Banking, Custody & Insurance Management Services**
- **Segregated Cell Accounts**
- **Branch Office Structures**
- **Financial Engineering ART Products**
- **Corporate Flexibility & Simplicity**
- **Competitive Cost Structure**
- **High Quality Professional Services**
- **Excellent Quality of Life**



**Barbados Investment and Development Corporation**

Website: [www.bidc.com](http://www.bidc.com)

Email: [bidc@bidc.com](mailto:bidc@bidc.com)

Tel: (212) 867-6420

## Special Advertising Section

risks. That increases the chance that any of the companies, and broadly all of them, will be able to meet the day-to-day claims and the occasional enormous insured losses that those who buy insurance can incur.

Measured against its power, reinsurance is the bailiwick of a relatively small number of companies worldwide. Some have accumulated capital measured in tens of billions of dollars and euros and hold assets worth a great deal more. Other companies are smaller, while some are yet-smaller niche specialists who take on specific risks. The combined financial weight of the reinsurers is the foundation on which global commerce stands.

Reinsurance companies operate on every continent, with offices in major cities around the world, where their insurance company clients are to be found. Many of the largest companies have been active in Europe and North America for generations. Lately, a dynamic concentration of reinsurance capital, both intellectual and financial, has developed in Bermuda.

Technology has changed the way reinsurance operates. "In the past decade, the global reinsurance industry has embraced quantitative risk management initiatives and computer modeling techniques that allow them to better deal with the volatility and uncertainties associated with catastrophic events," says Donald Kramer, chairman and chief executive officer of Ariel Reinsurance Co. Ltd., a post-Hurricane Katrina, billion-dollar start-up reinsurer. Kramer successfully started three major reinsurance companies. The use of computer technology is now so great

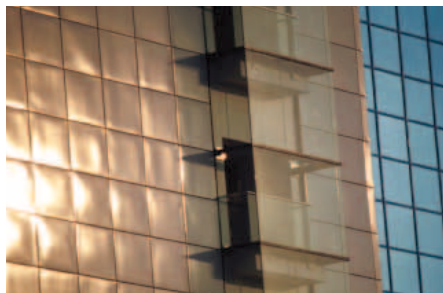
in this field that computers outnumber staff by as many as 10 to 1 in some companies.

Not long ago, the number of mega-catastrophes about which detailed facts were available was limited. Hurricane Andrew in 1992 and the Northridge, Calif., earthquake a year later were the largest. Then came the events of Sept. 11, 2001; the collapse of the World Trade Center produced the largest insured loss in history. After that, in 2004, four named hurricanes hit Florida in quick succession, costing tens of billions more. Then came 2005 and Hurricane Katrina, which will cost \$60 billion by the time all claims are paid, of which reinsurance will have paid half.

The reinsurance sector survived each of these events. Not every reinsurer stayed in the business, but few, if any, valid claims went unpaid. Thus far, the global reinsurance model has worked.

The reinsurance industry is not, however, perfect, nor is it without its challenges. As a better understanding of risk and its economic consequences has been gained, it has become clear, especially after Katrina, that, for safety's sake, the reinsurance model requires some companies to put up more capital for each dollar of premium they write. Many companies have been rearranging their books of business in the wake of these conclusions and of the insistence by the ratings agencies that companies now meet higher capital standards to maintain their reputations.

The basic reinsurance concept has traditionally been "post-event funding." Reinsurers, particularly catastrophe reinsurers, take premiums and invest them until claims following a disaster deplete their assets. The reinsurers then approach the capital markets and often



## Special Advertising Section

shareholders to recharge their war chests. Some companies have taken the opportunity of attracting more than was lost, to allow them the ability to write greater volumes of business in the tight market conditions that routinely follow large catastrophes.

Another reinsurance model has presented itself: a form of pre-event funding known as securitization, in which bonds are issued against suitable investments or bank commitments. When catastrophe losses exceed stated trigger points, the bonds might be lost — but so far few have been, despite seven of the 10 most costly catastrophes in history having occurred in the 21st century.

Another recent development has been the interest in reinsurance shown by hedge fund managers. “As reinsurers, after Katrina, looked

for ways to take the sting out of some of the risks they carried, hedge fund managers were looking for new fields in which to invest,” says Robert J. Cooney, chairman, president, and chief executive officer of Max Re Capital, itself set up in part by hedge fund capital back in 1999.

The result of the meeting of those divergent needs was a series of new reinsurance companies, the “Class of 2005,” many of which were owned, in part or completely, by hedge fund managers and, often, their clients.

Curiously, the seismic economic effect of great events is felt most strongly the further down the safety net one looks. Governments nominally underpin all economic behavior and the global financial infrastructure. Reinsurance companies are but one step up, yet they often present

a volatile earnings profile dictated by the low frequency and high severity of catastrophes.

In almost no industry is it acceptable, let alone traditional, for some companies to lose a third or more of their capital once in a while. Yet meeting the costs of a cataclysmic earthquake or windstorm can clobber earnings and sometimes even capital at reinsurance companies. Renewed funding restores their vigor, and the cycle begins anew.

---

### **Ariel Reinsurance Company Ltd.**

[www.arielre.com](http://www.arielre.com)

### **Max Re Ltd.**

[www.maxre.bm](http://www.maxre.bm)

### **XL Capital Ltd**

[www.xlcapital.com](http://www.xlcapital.com)

---

*Produced By:* **The Custom Publishing Group Inc.,**  
[www.custpub.com](http://www.custpub.com)

*Written By:* **Roger Crombie,** [crombie@northrock.bm](mailto:crombie@northrock.bm)

*Designed By:* **AAC Saatchi & Saatchi,** [www.aac.bm](http://www.aac.bm)

*Please Visit:* [www.businessweek.com/adsections](http://www.businessweek.com/adsections)



## TALENT EXPANDS POSSIBILITIES



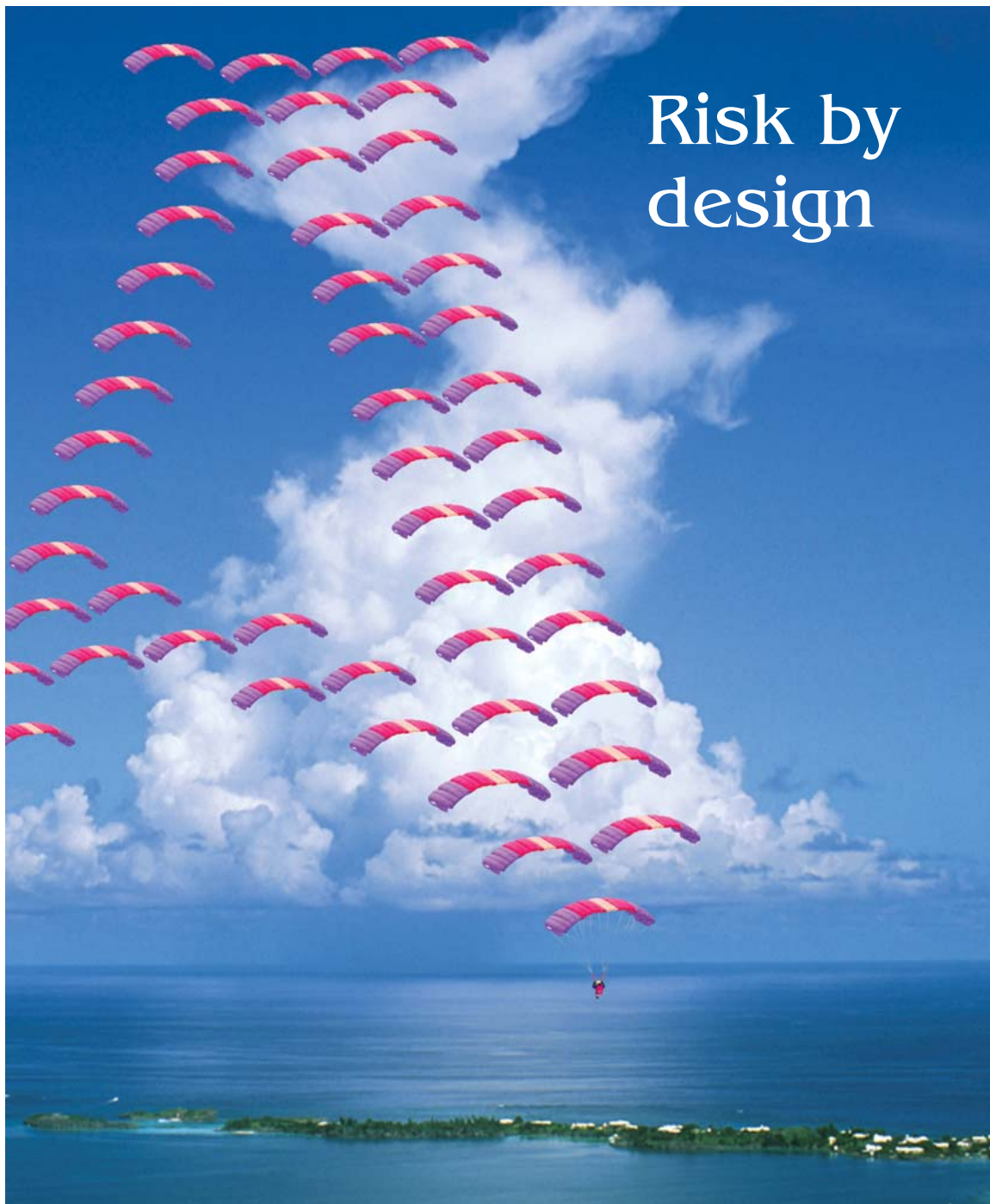
[www.maxre.bm](http://www.maxre.bm)

At Max Re, we've recruited some extraordinary talent to drive our business. From offices in Bermuda and Ireland, we underwrite a wide range of Property and Casualty Reinsurance and Insurance transactions, as well as Life and Annuity Reinsurance. Expanding the possibilities with innovative risk control, focused expertise and new approaches to established convention.

---

PROPERTY & CASUALTY    INSURANCE/REINSURANCE    LIFE & ANNUITY

A.M. Best's A- (Excellent)    Fitch A (Strong)



# Risk by design

Photo courtesy of the Bermuda Department of Communication and Information

  
**ArielRE**  
The SPIRIT of Reinsurance.

**Ariel Reinsurance Company Ltd.**  
T 441 295 5485 F 441 295 4750  
[www.arielre.com](http://www.arielre.com)