Q&A: Dr Jamie Rodney

Dr Jamie Rodney, executive director, ILS at Twelve Capital, says a reshuffle within the ILS market is being driven by defensive tactics

Do you think increased cat bond volumes in 2020-2021 signal a structural shift within the ILS market?
I am not sure if it is structural, but there's been a reshuffle. In part, reallocation has been driven by investor demand for performance and liquidity, as well as cat bonds being the most defensive area of the ILS space.

From 2011 to 2017, ILS expansion was primarily driven by collateralised reinsurance.

However, the increase in 2020 cat bond volumes was mainly driven by reinsurance fundamentals. For example, uncertainty over retro capacity and a spike in rates brought a number of reinsurers to the cat bond market for the first time.

We are seeing a broader range of retro style products now, and a widening to broader worldwide coverage. That is one driver in the short term.

In 2021, we are seeing investor demand resulting in a normalisation of cat bond pricing compared to last year's record levels, thus also supporting new issuance volumes.

Has this year's demand-led trend left rates at a sustainable level?
Cat bond rates have normalised compared to the record levels seen in 2020, back to where we were in 2019. This is at a market level – for some specific deals, it might vary. But relative to other investment classes, cat bonds still look very attractive.

Discipline in the cat bond market has evolved over the past few years. The market uses risk-based pricing and modelled losses to support this level of discipline.

What is your firm's take on what climate change models show us about future ILS risk?
Since late 2017 we have partnered with climate tech company Reask, using artificial intelligence to study climate signals and how climate variability is impacting North Atlantic Hurricane risk. We try to understand how the activity observed in recent years stacks up against different simulated variations of history.

We concluded that under extreme climate scenarios we're likely already living close to the future expected climate frequency.

We might have been a little more unlucky in recent years. Of all possible simulated climates, the one we observed was somewhat more extreme than expected – what we could be moving into, over the next 20 years or so, is simulated to be very much in line with what we've observed in the past few active years (as illustrated in the chart). As long as we know the downside, we can adjust and reprice risk. We just need to make sure we understand the limitations of models.

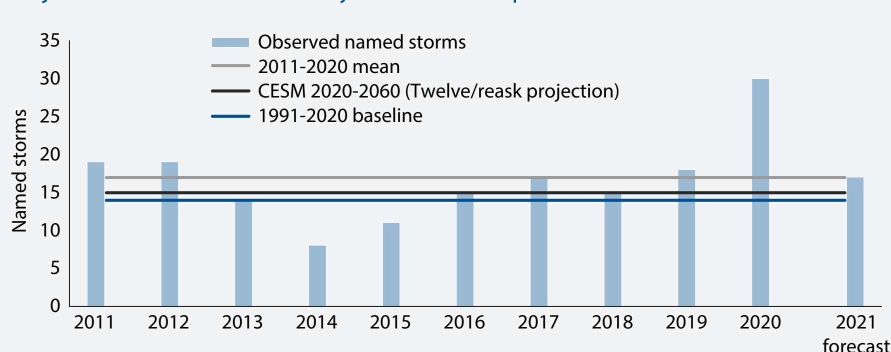
How easy will it be for the cat bond market to do more green deals?
That boils down to how you define green. One of the most challenging aspects of working in an ESG framework is how to define the targets. For example, the idea of using cat bond investment proceeds for green purposes is a concept that is simple to grasp and implement.

But if you shift to thinking about what the asset is covering, that question becomes a lot more challenging and convoluted. If you focus on what cat bond pay-outs are being used for, you could get a large dispersion in results from deal sponsors – some provide limited transparency on this.

But the (re)insurance market is very aware of these challenges, and recently launched a new insurance net zero group.

From Twelve's point of view, we are looking at ESG issues at a corporate level. For cat bonds our ESG assessment aims to evaluate both the issuer and the instrument from a sustainability perspective. In addition, we are actively developing our engagement and stewardship strategy to help drive transparency throughout the risk-transfer chain, from issuer, instrument all the way through to final pay-out.

Projected named storm activity in line with experience



Source: Twelve Capital