

Some thoughts on the Euro...

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The possibilities for positive technical margins for reinsurers are not at all clear. The management of costs and resources therefore takes on a vital importance for reinsurers. This is why it would be advantageous to increase the funds which are available and to optimise their management. There is no doubt that in the coming years exceptionally good financial management will be an absolute necessity for the reinsurance sector.

Someone said, when referring to the birth of the Euro, that between yawns we are living through some fascinating events. For reinsurance the Euro seems to offer, in addition to the elimination of exchange rate risks, possible simplifications in the carrying out of its business. The 11 founding nations bring together a good part of the world's ceded and assumed reinsurance, this means that after the implementation of the Euro there will be a sizeable reduction in transactions and costs.

The 20th century is ending with contradictory expectations for reinsurance, as was the case at the beginning of the century. At the beginning of the century reinsurance had become consolidated in Europe and the United States. The first World War was however to prove a severe test for an industry which had been in existence for little more than 50 years when hostilities began. Three of the nations at war: Germany, the Austro-Hungarian Empire and Russia had developed a considerable reinsurance capacity.

Germany, with more than 40 reinsurance companies, already formed the principal market for assumed reinsurance at the beginning of the century. The reinsurance business did not only come from Europe however, the commercial ties and the offices of the main German reinsurers also extended to the United States and Latin America. German industry had understood better than any other the role of reinsurance as a means of international penetration, together with the possibilities and perspectives of an activity independent of direct insurance.

The Austro-Hungarian Empire had also developed a professional reinsurance industry before the Great War. In addition to this, the large direct insurance companies had carried out a broad policy of international inwards reinsurance.

The case of Russia is particularly singular. Count Witte, the Treasury minister (1892-1903) tried, perhaps for the first time in the history of reinsurance, to promote the creation of professional reinsurance companies on the part of the state in order to help balance the trade figures. Even though this policy was to fail, it produced an interest in international reinsurance on the part of Russian companies which quickly flourished, achieving a volume of assumed foreign reinsurance, especially from the United States, greater than the volume of Russian reinsurance ceded abroad.

The war and posterior events: the October Revolution, German hyperinflation etc. would have immediate and dramatic consequences for reinsurance.

Although the interruption of reinsurance relations was not immediate at the onset of hostilities, and in fact between Germany and some countries they were never interrupted, the Allies finally prohibited German reinsurance.

The dismemberment of the Austro-Hungarian Empire also had serious repercussions for reinsurance; although in the case of Italy these were extremely positive since, together with Trentino, it was to receive two reinsurance jewels: Assicurazioni Generali and Riunione Adriatica (RAS).

For its part, Denmark, which already had an incipient reinsurance industry was to be benefited by the emigration in 1918 of the Russian companies with a base in St. Petersburg.

The rest of the Russian companies disappeared with the revolution. This was an event of great importance because they had managed to almost double their income between 1913 and 1917. Their subsidiaries in the United States found themselves in an unsustainable position given that the United States did not recognise the USSR. These subsidiaries were wound up between 1920 and 1923 and their assets were managed by the Federal Insurance Bureau.

The end of hostilities brought with it a sharp fall in commercial and industrial activities which affected the insurance sector and, in consequence, also the reinsurance sector. Many companies were liquidated. Marine business was especially affected, and the British reinsurance market, heavily dependent on this line, suffered badly, both due to lower income levels and due to competition in rates which came about in order to attract new business so as to alleviate the reduction in business volume. This policy had disastrous effects for many companies which saw themselves heading towards bankruptcy.

The upheavals which were suffered by the reinsurance sector in that first quarter of the 20th century were of such importance for an industry so young that they had consequences which are still felt today. The bankruptcies, liquidations or the

financial difficulties which many companies experienced prevented some reinsurers from honouring obligations which they had acquired.

Some of the clauses which are included in the texts of contracts which are in force nowadays, such as the special cancellation clause in case of war, have come from those events. The introduction of economic clauses such as those relating to reserve deposits are especially important. Up until the period immediately after the 1st World War reinsurance contracts did not include these types of guarantees and operated in the same way as facultative business.

With the advent of the Euro, and placed by the reinsured under the meticulous scrutiny of recognised ratings agencies, there would seem to be occasion to reflect on the possibilities of abandoning some practices, at least in the European union, such as these deposits which might

not seem to be necessary nowadays in order to guarantee the obligations of reinsurers who have been carefully selected by cedants.

In addition to this, the fall in interest rates considerably reduces the possibility for cedants of obtaining a substantial difference between the interest which is actually received and that which was agreed. It is even possible that cedants could be negatively affected if they do not achieve efficient and rapid management of funds, or if they are caught off-guard by a brusque fall in interest rates to below that stipulated in the contract.

Although the revenues which cedants are able to obtain nowadays from these deposits are meagre, and they do not in any case normally constitute very significant amounts, reinsurers are left with a large part of their resources scattered and to which they do not have free access.

If it is true to say that the risks which are handled by insurers are

becoming increasingly vulnerable both in terms of loss intensity and of loss frequency, then the risks which are received by reinsurers are even more unbalanced and dispersed. The possibilities for positive technical margins for reinsurers are not at all clear. The management of costs and resources therefore takes on a vital importance for reinsurers. This is why it would be advantageous to increase the funds which are available and to optimise their management. There is no doubt that in the coming years exceptionally good financial management will be an absolute necessity for the reinsurance sector.

Of course, the elimination of reserve deposits, if this were to take place, should be carried out in a gradual and progressive manner over a period of various years so that cedants do not suffer any detrimental effects. ■