ARMOUR

Run-off 2020: Trends and Challenges

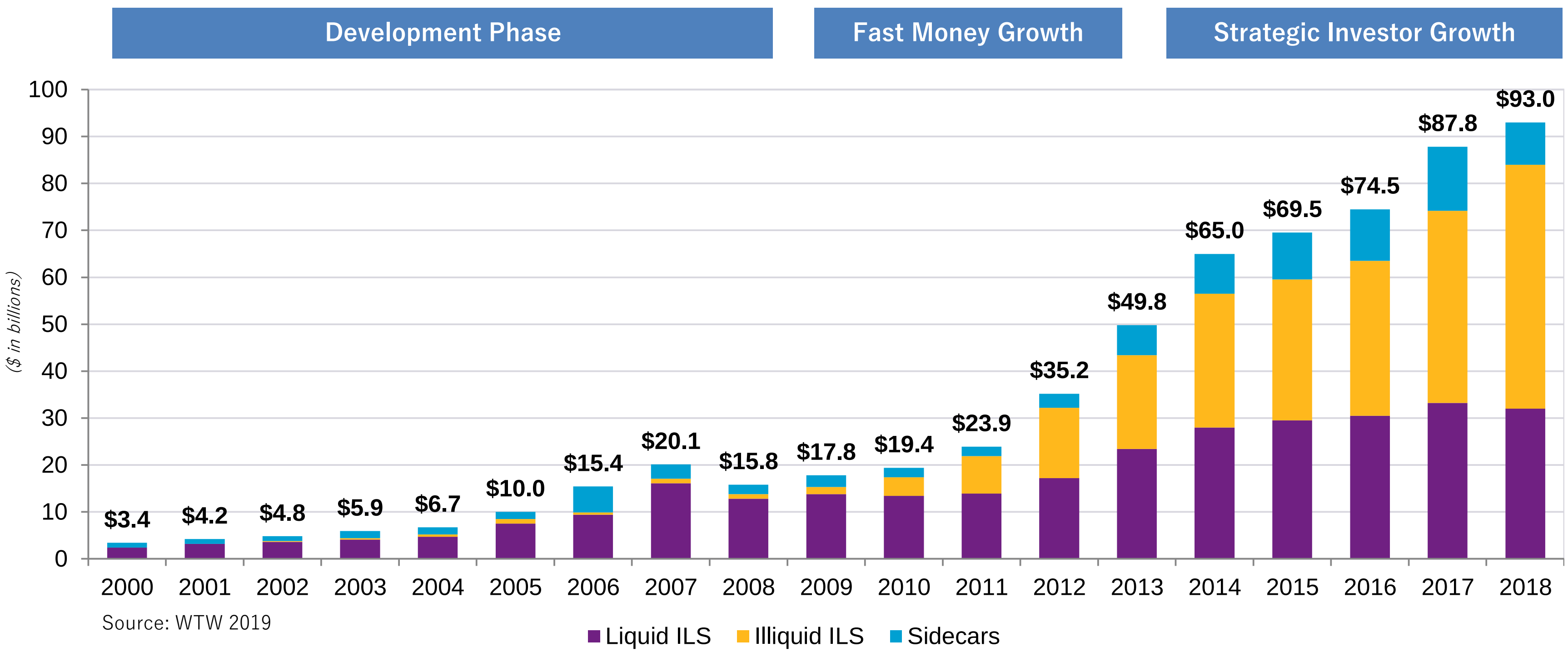
London Market Run-Off Forum 2019 - 9th October 2019

Overview of Armour

- **Formed in 2007**, Armour is a global company headquartered in Bermuda consisting of licensed (re)insurers, asset managers and service companies, specialised in the global legacy non-life insurance space
- In excess of **USD 1.5 billion of committed capital** under management across various vehicles with a diverse investor group including sponsors, pensions, endowments and insurance firms
  - Significant permanent capital vehicle (Armour Re Limited) with support from a blue chip global investor base, led by **Aquiline Capital Partners**, a New York based private equity firm investing in financial services and financial technology
  - Exclusive sub-advisor to an ILS-type investment fund
- **25+ multi-platform integrations** / migrations successfully completed from global insurance providers and legal entity acquisitions
- **USD 2.7bn of gross reserves** under management, for both portfolio companies and third parties
- **Global team of 220**+ experienced professionals (BM, US, UK, EU, CH)

ILS vs Non-Life Legacy Market

ILS: Development of Alternative Capital

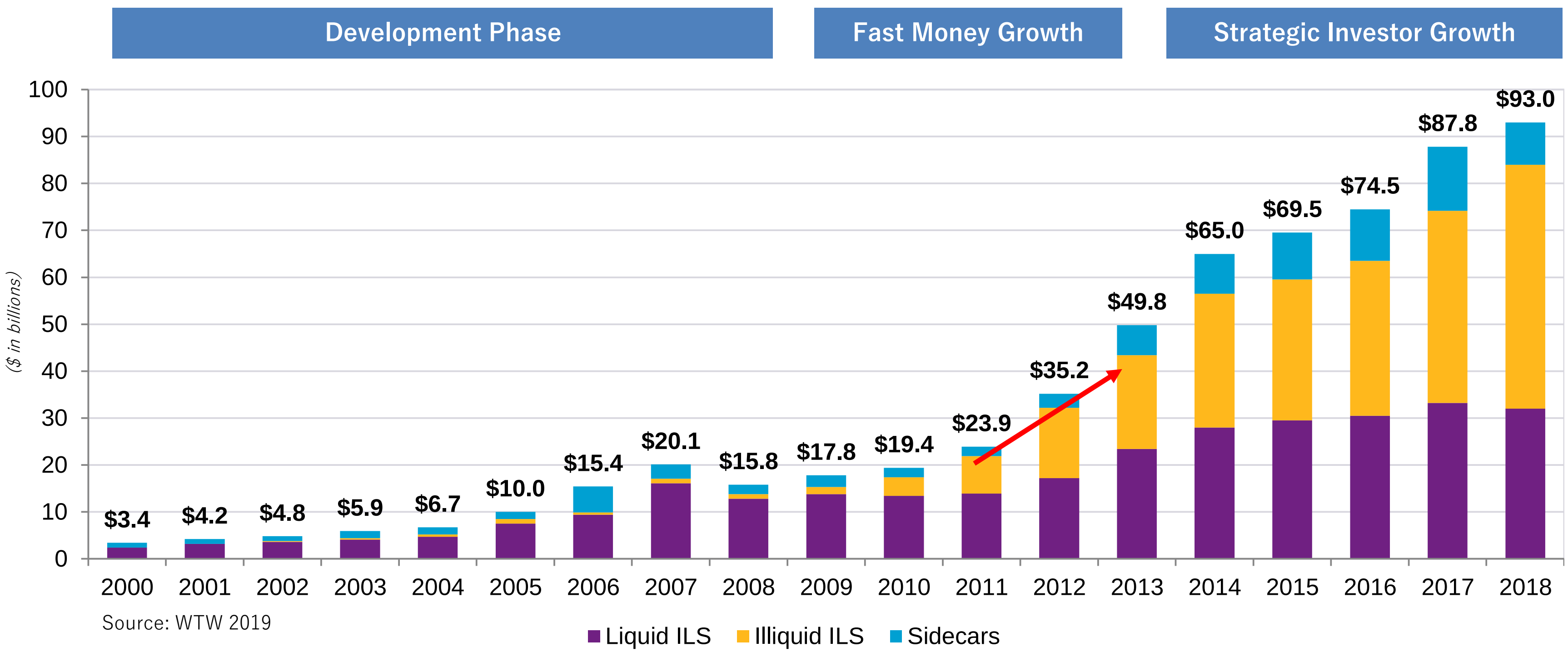


Source: WTW 2019

At what stage of development is the non-life legacy market?

ILS vs Non-Life Legacy Market

ILS: Development of Alternative Capital



Source: WTW 2019

Substantial increasase in PE-capital invested in legacy in 2017-2019 (incl. Aleph, Apollo, Aquiline, Crestview, Kelso,..), but probably not yet at cruise speed?

Demand Drivers - Value Proposition for Investors

- Low correlation to other asset classes and segments of insurance (e.g. ILS)
- Low volatility
  - Portfolio diversification
  - Historically mainly known nature of exposure, with limited downside from individual claims amounts
  - Limited exposure to natural catastrophes
- Solid historical performance
- Growing supply
- Still limited number of players, with increasing barriers to entry

Demand Issues: Infrastructure and Skillset

- Increasing demands from both regulators and sellers: consolidators have to be equipped with specialised staff and infrastructure to be able to guarantee:
    - Best in class governance, systems and security
    - Fast and smooth transition, including on-boarding and migration of portfolios, staff, etc.
    - Pro-active, efficient and transparent claims handling, assuring TCF and relevant client's policies
    - An open, frequent and constructive dialogue with regulators across jurisdictions
    - **...but still maintaing agility!**
- Access to (re) insurance vehicles in the relevant jurisdictions (UK, EU, Lloyds, US hopefully soon...)
- Solid and cost-effective capital structure
- Diversified and evolving set of skills, traditional run-off profile is no more sufficient to meet the needs of the market: «Live» underwriting, structured reinsurance, more «exotic» risk classed or regions, corporate finance, etc.
- Requirements, and therefore barriers to entry are constantly increasing!

Demand Issues: Infrastructure and Skillset

As the legacy market broadens we continue to invest in growing our operational platform and the associated governance and processes required to treat stakeholders fairly across multiple lines of business and jurisdictions. Balancing our infrastructure with the agility to react quickly to the characteristics of the increasingly varied portfolios coming to market is essential in delivering maximum value to sellers, service to policyholders and returns to investors.

Hannah Farrer Fisher
Chief Operating Officer, Armour Group Ltd

PWC Run-Off Survey 2019

Supply Drivers – Rationale for Legacy Transactions

- Risk and capital management and optimisation
  - Disposal of run-off portfolios to **unlock trapped capital to be redeployed in core business, strategic areas and growth**
  - **Solvency II** has incentivised European (re-) insurers to think strategically about the allocation of capital to classes of business and products
  - Remove volatility and accelerate finality
  - Legacy solutions as part of an **(re)insurers's capital management toolkit**
- Simplification and management of costs/resources
  - The management and servicing of non-core or older legacy can be a drag (management time, resources, old systems, costs) to current business
  - Run-off specialists have **lean and efficient service platforms**, and are expert in accelerate finality of both open claims and reinsurance contracts in an agile and cost efficient manner
- The disposal of complex or distressed legacy portfolio can also have a **positive effect** on share price for listed companies, or on **valuation** for private companies

PLUS: increased consolidation, continued low interest rate environment, soft market and pressure on profitability, Brexit, Lloyd's performance review, etc. etc. etc.

Supply Drivers – Rationale for Legacy Transactions

29% Disposing of non-core business

16% Managing claims volatility

29% Releasing capital

9% Minimising expenses

17% Early finality

Source: PwC

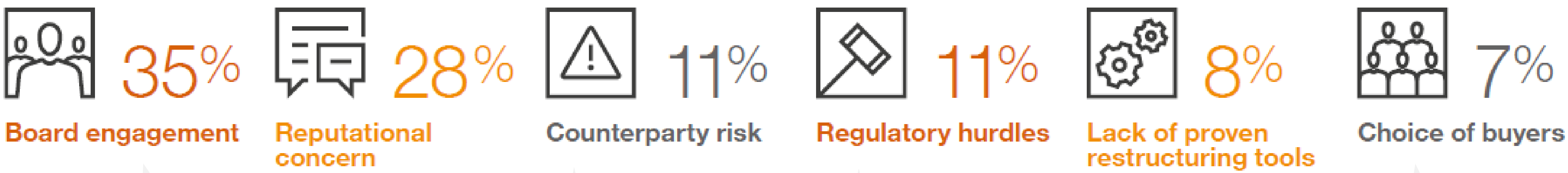
- For us it is about cleaning up legacy portfolios, **removing downside risk,** reducing the drag on the business performance and **releasing capital**. We believe that a good run-off carrier can give **more focus** and **deploy more claims management experience/expertise to specialist legacy portfolios than we can**, such that there is economic value creation in a good disposal" (from Legacy Barometer 2019, Insurance Insider)

- Zurich Legacy Solutions defines Strategies for discontinued operations under its management, with a focus on **capital repatriation**, cost minimisation and maximisation of economic benefit to Zurich. It currently has $7 billion insurance liabilities under management.

- "This transaction, which attracted a high level of interest from the market, is another step forward in our efforts to **optimize the Group's capital allocation**. It allows Generali to release capital, reduce costs, and **remove the potential source of volatility** inherent in such long-tail business lines. Further, it shows that Generali is committed to **reallocate its capital** where it can best be used, going beyond the current global review of its markets." (Generali Group)

Supply Issues - Barriers to more Run-Off Transactions

Figure 8: The biggest barrier preventing sellers from commencing a run-off transaction



Source: PwC

More Transactions, Education

PR (more run-off forums!)
Maintain discipline

PR, Structuring, Rated Vehicles, Fronting, Partnerships with reinsurers?

Patience, Lobbying

Patience (again), Continued product development

Consolidators to keep developing and provide valid alternatives.

Is the capital in the industry enough to meet the supply?

legacy market has spent the last two decades building its reputation as a safe haven for the insurance market to cede reserve risk.

J. Dickerson (Willis Re), in Carrier Management, 2019

Product Development in ILS

New Structures

New Triggers

US Wind Parametric Cat Bond

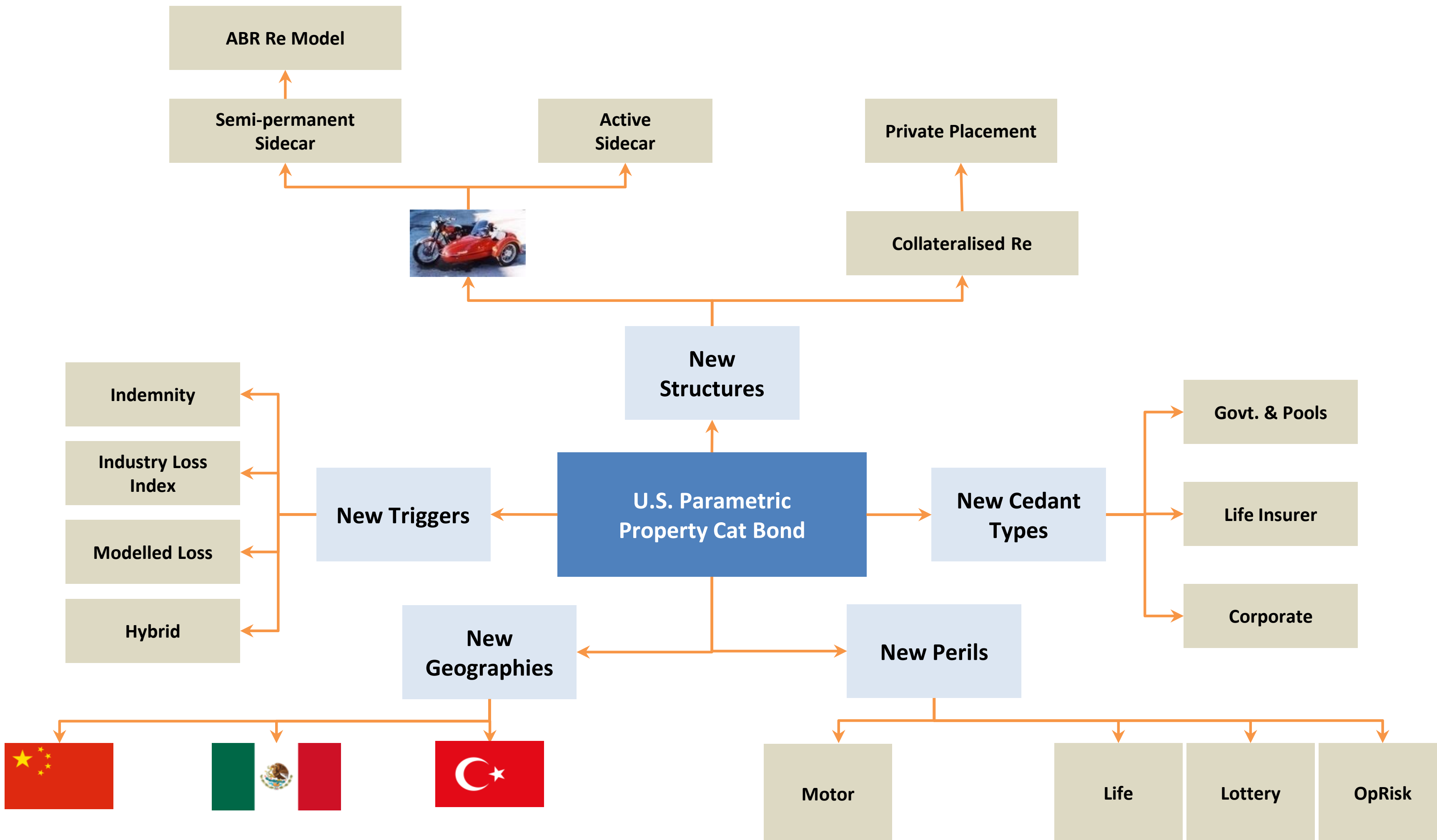
New Cedant Types

New Geographies

New Perils

Source: WTW 2019

Product Development in ILS



Source: WTW 2019

Product Development in Legacy

More convergence of «Live» underwriting, retrospective reinsurance and traditional legacy

New Structures

Constant flow of newcomers exploring legacy: more small/medium size insurers, reinsurers, ILS funds, corporates

New Triggers

US Asbestos LPT

Entity in Run-off

New Cedants (Types)

Trading or exploring:

- EU countries: Italy, France, Benelux,Germany, Nordics, Spain
- Middle East
- Asia (Malaysia)
- Australia

New Geographies

New Perils

«Younger» AYs mean more attritional-type of claims to be managed

Value Creation: «Classic» Legacy

- Portfolio Management
  - Claims management strategies developed individually for books or sub-segments, with incentives built along the value chain to settle claims fast and in a cost-effective manner
  - Proactive management and optimisation of reinsurance assets
- Expense Management
  - «Fit for purpose» structure and infrastructure concepted and built exclusively for the management of run-off portfolios
  - Lean and cost effective processes
- Investments
  - Investment strategies developed ad-hoc for the individual portfolios

Main focus for «Traditional» Run-Off Transactions

Seller / Buyer Relationship

Value Creation: «New» Legacy

- Structuring
  - Structured reinsurance and corporate finance techniques: Experience in developing solutions that optimise risk, capital and costs
  - More fluid sharing of the servicing platform
  - Alignment of interests

Increasingly critical for «younger» portfolios, with clients seeking capital efficiency disposing or sharing risk on back books, but still retaining an interest for the class/product going forward

Partnership

Pricing Environment

- Pricing remains (very) competitive, AND

Could not agree more James!

.. Recent vendor preferences for ceding less developed business is likely to have an increased impact on earnings volatility and, as such, there is a greater potential for "unknown unknowns" to be transferred from live to legacy balance sheets.

J. Dickerson (Willis Re), in Carrier Management, 2019

- Transition period, with the market adapting to more diverse, volatile and sometimes complex portfolios
- With more volatility transferred to the legacy market there is more need for pricing discipline
  - Claims savings may be more difficult to achieve, and no more sufficient to generate profits
  - More attritional claims ceded means different skills required, and no time to lose!
  - Volatility has to be identified, assessed and priced
- The «Legacy Barometer 2019» quotes Competitive Pricing as the top challenge to the legacy industry over the next 12 months

2019 Market Pipeline – Rich and (very) Diverse

- LPT of both non-core and core portfolios, often including recent years of account (sometimes including 2019)
  - Improvement of SCR position, capital redeployment
  - Performance issues – LPT as a «Stop Loss»
  - Simplification of business model
- Lloyds
  - Full Lloyds platforms, RITC, LPT, Corporate Members
- Brexit-related opportunities
  - IBT of small to mid-size UK/EU portfolios
- LPT-like solutions for Corporate Clients
  - Disposal of insurance-like liabilities (incl. Asbestos) from corporate balance sheets
- Legacy solutions to facilitate M&A transactions (support to buyer or seller)
- Reinsurance portfolios
- ILS Funds
  - Collateral trapping

Legacy 2020 and Beyond

> Although the legacy market is generally resilient and diversified enough to absorb losses, in our view the biggest risk the industry faces is the regulatory failure of one of the major legacy markets.

J. Dickerson (Willis Re), in Carrier Management, 2019

- It is a crititcal time for for the Legacy Market
    - Adapting to the post-Solvency II environment, new risks, new structures, increased demands from regulators
    - Matching increase in capital flow into the space with increased demand from sellers/cedants, maintaining structuring and pricing discipline
    - Growing number of legacy players in the Lloyds market
    - Resilience of the market is still to be stress-tested
- Any failure (consolidators, service providers, intermediaries, etc.) could affect the market as a whole
- We need to deliver as an industry, maintain discipline to improve resilience and sustain growth

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