Diversification is the key to surviving a crisis

Canada Life Re, a division of The Canada Life Assurance Company, has operations in Canada, the US, and Europe. It has over C$20B of capital and AA ratings from most of the agencies. Jeff Poulin, a fellow of the Society of Actuaries (US) and the Canadian Institute of the Actuaries, was appointed CEO in May 2017, but he has been working for the reinsurance company since 1991 and in 2018 , he received the 2018 American Council of Life Insurers (ACLI) Forum 500's Distinguished Service Award. Although currently confined in his house in Florida, Jeff took time to talk to us about the business and the impact of the current crisis.

Canada Life Re has grown strongly in life reinsurance in Europe – for example the €12 billion longevity transaction with Aegon. What makes Europe, and in particular the Netherlands, so attractive?
"At Canada Life Re, we try to focus on well-established markets with properly defined regulations and rules. The US has been our main market, but Europe is a close second. We have been active in Europe for over 20 years and have been in the longevity market for at least 15 years.

We tend to focus on transactions where we think we have an advantage from a capital standpoint as we are a well-diversified group. Longevity aggregates well with our US mortality business. As for the Netherlands, we have found that the Dutch are very pragmatic, have great actuaries and are looking for transactions that make good business sense. I have found that if you come up with a great idea that is advantageous for a Dutch company, they tend to be more open than insurers from other European countries in pursuing these opportunities."

Are there different needs throughout Europe with regard to different types of reinsurance structures, and if so, driven by what?
"Yes, the products are different from country to country and despite Solvency II, we find the various regulators administer the rules somewhat differently. Most countries are very focused on savings with little protection being sold.

MORE AND MORE EUROPEANS ARE SEEING REINSURANCE AS A CAPITAL TOOL AS MUCH AS A RISK TOOL

We also work with health carriers in some countries, but not in others. We tend to focus on relatively large transactions where we have some capital advantage. Savings products have significant asset risk, so we look at reinsuring the tail risk on these. Renewable products tend to have lapse risk or contract boundary issues and we like to focus on this as well. Tail longevity risk is also something we can look at. With the internet, there are more and more innovative products or innovative ways to sell products. More and more Europeans are seeing reinsurance as a capital tool as much as a risk tool. We prefer focusing on these types of transactions."

Longevity risk is not easy to diversify. How does Canada Life Re model the correlation between countries?
"I agree, it is a hard risk to diversify. We do have overall risk limits on all our products regardless of any diversification. Our company does not want to put more than a certain amount of its capital at risk for a specific risk. We have longevity transactions in four different European countries and are looking to add more. There are differences between the countries. For example, the Netherlands has a more homogeneous experience than the UK. We assume it is because of its healthcare system. There is less difference in health access between the rich and the poor in the Netherlands than in the UK.

We have observed relatively good correlation between our mortality experience and our longevity experience and are spending more time studying this. We do see the benefits even though most of our mortality is in the US and our longevity in Europe and the mortality business is on a younger population on average."

What is the impact of the COVID-19 pandemic on your mortality portfolio?
"COVID-19 is a terrible event and without the various government interventions it could have been much worse. We still do not know where this will go or whether it will come back, but it does show why you should buy reinsurance. We write mortality reinsurance mostly in the US, but also in Spain, France and a few other European countries. The current pandemic has not had a very significant effect on our mortality yet.

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In the US which is our biggest market, approximately 5% of our population is over 70, so we expect some extra claims but not a dramatic change from our expected mortality. At this point, we think it could cause a 4% to 6% increase in claims this year.

Our longevity book is likely to benefit from the pandemic and should offset our extra claims in mortality. This somewhat points to the diversification point I was making earlier."

Looking at health reinsurance, how does Canada Life Re manage the combined pandemic exposure?
"We have written a large amount of health reinsurance in the US. We also have some in Europe. Contrary to what someone would think, claims are actually down for our book at this point.

People in the US that have COVID-19 are not always covered, so the cost is shared by government or hospitals and because of the virus, everyone that can has postponed non-essential surgeries or appointments. We expect that there may be a surge after things go back to normal, but for the time being, claims are down.

In Europe, it is similar. Government programs seem to take most of the cost of COVID-19 and regular health insurance is down. Disability claims seem to be increasing and the virus could have a relatively significant impact on this business, but our disability portfolio is small."

Most Dutch health insurers don't use reinsurance to mitigate their health risk. Do you see opportunities for Dutch health insurers to manage their medical expense risk?
"I do. In the US, we write health reinsurance mostly to ease the capital associated with it – similar to Europe under Solvency I. Under Solvency II, our European transactions have been more of a financing nature. If the expenses in the first year are higher than they are in renewing years (commissions + set up cost), we can help with the financing of that cost and be repaid from future years."

What will be the effect of the COVID-19 crisis on the life reinsurance market?
"I suspect it will have many effects, in particular the asset implications on certain industries – airlines, hotels, restaurants, energy companies – and as a result, I suspect there will be impairments of assets in the coming months which will affect life insurers who tend to invest in long-term assets. Life insurers are likely to try to find solutions to help with these losses or help improve their capital position. Smart reinsurers will be offering these solutions.

I believe people will look at their mortality exposure differently and may buy more protection coverage than before. Pandemic covers may become more in demand and the pricing will be more expensive. Furthermore, I can see that insurers will want to choose well-diversified and strong reinsurance partners to deal with as certainty of payment is always heightened in periods of crisis."

How can Canada Life Re manage the accumulation of the various risks mentioned?
"We benefit from a very strong parent with a lot of liquidity and with exposures in different countries and to different products on the direct side, which is a large advantage. As a reinsurance division within a large international insurer, we tend to focus on the risks that diversify us well at the parent level.

We also have other lines of business that do not expose us to a pandemic, but benefit from the crisis: like our property catastrophe business which is seeing more demand and higher reinsurance prices without incurring losses from the current crisis. Moreover, as mentioned, we have internal limits and conduct stressed scenarios that limits the amount of capacity we will offer on a given risk."

What are your thoughts about the Dutch market and what are the differences with other countries?
"This is a loaded question, but as I said, I like the Dutch market and the Dutch people. I find the market is innovative and receptive to new ideas. It seems more concentrated in a few insurers than other European markets. The people are more technical than any other continental European markets – more like the British or the Irish. You understand your numbers well. Pensions are a big part of the market in the Netherlands and the longevity is very sizable.

Pricing is as tight as it is in the UK, which shows how well Dutch insurers negotiate their reinsurance. The regulator is quite technical and tough by European standards, and tends to follow the rules, or has a strict interpretation of the rules more so than in other jurisdictions.

Generally, the Dutch market offers a great array of protection products that are good offerings to the consumers. Other European countries tend to offer products that are sometimes 'gimmicky' or that are not good value for the consumer. We do not see that in the Netherlands."

What do you think is the biggest threat or opportunity for the international reinsurance market, but more specifically the Dutch market?
"For me, reinsurance works well if it is an international business. Reinsurers take various risks in various countries and need to be diversified and amalgamate these risks for it to work on a long-term basis. Reinsurers need to have a large amount of capital and resources in their home country to make sure they honour all their commitments around the world.

The biggest threat I see is drastic changes in regulations or taxation in one of the countries we have business. On the life insurance side, we make very long-term commitments to our clients, sometimes they are 30 or 40 years+ commitments. We can do tests and scenarios to make sure that we have enough capital and reserves to cover the worst-case scenarios.

What is very hard to predict or prepare for, are not pandemics, economic crisis or other catastrophes, it is a potential change in required capital or a change in taxes that suddenly makes our contracts prohibitive. As an international reinsurer, we must make sure we understand the current regulatory environment and the current tax environment, but it is extremely hard to predict changes to it. Therefore, at Canada Life Re, we like dealing with well-established countries with proper rules. Having a good technical regulator that understands your business well is actually an advantage." ■