REINSURANCE

Acing your medical treaty renewal

For insurance companies, the renewal of medical reinsurance treaties is a challenging but promising endeavour that can unleash growth and profitability prospects for the year ahead. LINK Insurance's Messrs Jihad Ghanem, Jens Sonnenschein and Imad Hamoush explain that successful medical treaty renewals require an evaluation of multiple options by experienced brokers with a far-reaching vision.


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Given the typically large share of medical business in an insurer's portfolio, especially in MENA, much attention is given to medical portfolio treaty renewal by cedants and many expectations ride on the improvement of existing arrangements.

Indeed, medical treaties can potentially determine several fundamental elements of the medical portfolio management process including its growth potential, its net profitability to the insurer, its management burden and even client satisfaction and retention.

This potential can however only be unlocked if cedants are able to judiciously assess all different treaty reinsurance options and their expected impacts.

Unlocking potential

First, understanding the benefits, drawbacks and risks associated with the various types of reinsurance is essential for exploring the different levers that reinsurance offers. While most insurers in the MENA region are very well attuned to the workings of quota shares, the use of non-proportional treaties, although increasingly frequent, remains much less prevalent and knowledge of their benefits and intricacies is less widespread.

Quota share arrangements are simpler and offer several advantages. In addition to solvency relief, they are a good way to manage uncertainty whether emanating from aggressive growth plans, unexpected inflation, pandemics or changes in applicable laws. The usual absence of loss cap also affords some reassurance for cases of (extremely) negative portfolio performance.

It is also important to note that quota share arrangements often come with a higher involvement from the reinsurer compared to their non-proportional alternatives. For smaller or medium sized insurance companies, this can be very useful as it allows them to benefit from the reinsurer's pricing tools and guidance, underwriting guidelines, product development support and in certain cases, operational solutions including distribution tools which they might not be willing to invest in and develop on their own.

For larger organisations however, this proximity of the reinsurer to sensitive areas of the business cycle such as pricing and underwriting or the increased administration associated with proportional treaties can represent a burden and induce limitations which the insurer might be willing to accept.

Although a quota share arrangement can be the right solution in many cases, the inability to make a professional assessment of alternative arrangements can cause insurers to overlook the best possible approach. A proper evaluation involves taking into account portfolio, target market, associated product mix, experience, financials, growth objectives and maturity, compared to adopting alternative structures.

Non-proportional treaties for example are technically more complex in the number of variables and particularities involved. Within non-proportional structures, an insurer must, for example, carefully select whether protection is triggered by individual claim amounts or by claims aggregation per member and determine an adequate priority level offering an optimal level of volatility, protection recovery, administration and profitability.

Another particularity of non-proportional treaties is the need to choose the most adequate treaty basis – risk attaching or loss occurring – a condition which requires scrutiny.

Besides the classic quota share and excess of loss treaty structures, we are seeing the emergence of a hybrid reinsurance arrangement that could provide the best protection. Indeed, for insurers with very aggressive growth targets, quota shares might not find enough favourable capacity while excess of loss structures would expose cedants to highly destabilising risks.

In this case, a mix of quota share with excess of loss protection over the quota share retention might allow both insurer and reinsurer to optimally carry risks to accompany an aggressive growth journey.

The classic insurer-reinsurer gap

Once a decision is made to maintain, improve, reassign or transition a reinsurance arrangement, several challenges can be expected.

Reinsurers might not offer the full range of reinsurance structures or might have a different appetite for each of them, which does not help cedants leverage unbiased advice from these otherwise reliable and experienced professionals. Reinsurers might also require a convincing story before welcoming a cedant's move to an alternative treaty arrangement form as well as a sound rationale which aligns with their business objectives and strategy.

Medical treaty renewals also must factor in the divergent views between insurers and reinsurers relative to pricing. This might manifest itself in the choice of inflation assumptions or in the extrapolation and interpretation of the year's incomplete data. The latter challenge is even more critical for excess of loss arrangements on per-person-per-year basis where aggregation of claims per insured member needs to be carefully assessed against the treaty's priority level.

Underwriting guidelines are also at stake as are terms and conditions as each party in the reinsurance relationship seeks to secure the most protective terms for its business.

Do what you do best and outsource the rest

Depending on the insurer's capabilities, an experienced reinsurance broker can go a long way in supporting the conduct of a successful renewal as well as servicing the treaty's management requirements afterwards. Aggregation of data from multiple TPAs for renewals and throughout the year, data sanitisation, tracking of a target TLR, adjustment premium calculation, leveraging insights coming from granular data are all ways through which insurers can offload administrative and technical burdens and rely on dedicated competencies.

In view of the complexities in assessing the optimal reinsurance form and structure and given that reinsurers often specialise in one form or another of reinsurance, they are not always in a position to propose the entire range of protection alternatives. Insurers who do not possess the access, expertise or 360 degree vision required must rely on the expertise of a specialised reinsurance broker who can perform a thorough assessment of alternatives and unlock great value for the cedant's growth and profitability.

As explained earlier, the insurer-reinsurer gap related to reinsurer bias or reinsurer specialisation can also be a hurdle during treaty renewals. This is where the role of an experienced reinsurance broker can be crucial. Many instances of over-reinsurance have been flagged by capable advisors to help cedants achieve significantly higher returns.

First, they can offer clients wide awareness of the various ways to structure their medical treaty arrangements and providing the technical and analytical know-how to assess the impact of each in terms of advantages and drawbacks and highlighting inherent opportunities and risks. This has far-ranging impacts. Choosing a treaty structure or determining its retention level will determine the amount of solvency relief afforded by the treaty, and setting the retention level of a non-proportional treaty will greatly impact the number of net recoveries afforded by that treaty.

Second, they can support cedants in their pricing negotiations through technical and non-technical means. Technical means include various analytical models which a credible and expert broker might have developed to help challenge reinsurer assumptions or evaluations. This can be done also through tools defining a leeway for aggressive pricing on specific opportunistic accounts whenever overall portfolio profitability is ensured.

Gaps to be bridged also include the cedant's unique understanding of particular accounts, market dynamics, regulatory constraints, customer preferences and habits which might not be accessible to the reinsuring partner and where a reinsurance broker's experience might help.

This technical capability is useful in both proportional treaties where reinsurers have a prominent role influencing the pricing strategy and non-proportional treaties where broker capabilities can compensate lower reinsurer involvement.

Third, the broker can leverage multiple experiences and involvements across the region, across players within the local market, across reinsurers and even within a reinsurer's offer palette, to identify the most advantageous practice in terms of underwriting guidelines and conditions and secure an optimal framework of terms.

Additionally, a reinsurance broker with a long and credible track record of channelling healthy and well-managed reinsurance business to reinsurers can benefit from a high level of leverage with capacity providers and secure flexible conditions which might otherwise be inaccessible to cedants.

Finally, it is important to consider that a category of insurers may not resort to reinsurance capacities to protect their portfolios. In these cases of self-reinsurance, the support of a professional broker can go a long way in optimising the performance of medical portfolios.

Expert brokers can offer advanced analytical and budget management tools and provide best practices, based on arrangements, for insurers with similar profiles in the same region. Often, this professional advice can take the shape of reinsurance-based solutions that address the gaps which motivated the insurer to self-reinsure. These include reduced profit margins, restrictions on product and portfolio development capability and TPA restrictions. All this can be done while realising the benefits from reinsurance support, including solvency relief and performance stability.

As you move forward with medical renewals, it is worth considering what the famous consultant, educator, author and father of modern management Peter Drucker once said, "Do what you do best and outsource the rest".

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