IS YOUR INSURER LIQUID ENOUGH TO PAY OUT?

Why Reinsurance Matters

To the average person, understanding how their insurance provider is reinsured might seem a little academic or even entirely irrelevant. Yet given that insurance is built on trust, especially the confidence that your insurer will remain sufficiently liquid to pay your claims, it is important for consumers to understand how effectively their insurers re-insure themselves.

Understanding how your insurer is reinsured, for how much and with whom should be important considerations when choosing an insurance provider.

At its most basic, reinsurance is insurance for insurance companies. Reinsurance allows insurers to transfer part of the financial risk of underwriting consumers' cars, homes, businesses or other possessions or risks to another party or a number of other parties.

When an insurance company sells a life policy designed to pay out on the death of the policy holder in accordance with the details of the policy, the insurer is legally required to hold enough funds in the business to pay out all the claims that are statistically likely to be made on its life book. While this requirement protects consumers by ensuring the insurer has sufficient liquidity to cover its exposure, it also puts a cap on the amount of business that an insurer can take on.

To help insurers provide sufficient cover to manage all the risk in a market, insurers can transfer some of their responsibility to pay clients out to third parties, called reinsurers. By transferring some of its risk to reinsurers, the insurer can reduce the amount of capital that it must retain to keep regulators satisfied that it has sufficient liquidity to cover likely client liabilities

In short, reinsuring some of their liabilities with a reinsurer allows insurance companies to take on more clients or insure larger risks than their capital holding, or liquidity, would ordinarily allow.

Also, by transferring risk to another company, reinsurance allows insurers to reduce the likelihood of being entirely responsible for, especially, large, unforeseen or catastrophic payouts that they would be challenged to manage on their own.

Reinsurance contracts, between primary insurers and reinsurers, have been a standard mechanism practiced by the insurance industry for centuries. Reinsurance is critical to the efficient and safe functioning of the global insurance industry, helping insurers maintain financial stability while increasing their ability to take on risk and grow market share. Reinsurers also help insurers maintain accountability and manage catastrophes while also still achieving profitability and sustainability.

There are several globally recognised reinsurance companies, including well-known names like Munich Re, Swiss Re, Africa Re and Continental Re who actively operate in Nigeria. Coronation Insurance reinsures various parts of its risk book with all four of these reinsurers in line with global best practice.

The design of reinsurance contracts vary based on the needs of the parties involved. A common example of a reinsurance structure shares premiums and losses between primary insurers and reinsurers. Alternately, reinsurers agree to pay out above a specified limit in return for a fee.

Coronation Insurance stands out in the way it structures its reinsurance contracts, using advanced analytics to present a data-driven view of the behaviour of its various risk books. Using big data to accurately balance it exposures for severity and frequency of loss, Coronation Insurance is able to generate the intelligence required to structure cost effective reinsurance contracts that accurately target real risk. This not only ensures that the risks that Coronation takes on for its clients will be covered, but it also helps manage the cost of covering these risks. This is ultimately reflected in more competitive client premiums.

Today, however, large risks, like natural disasters or climate change are increasingly taken on by institutional investors through catastrophe bonds and other alternative risk-spreading mechanisms. The result is that many insurance products increasingly blend reinsurance with what was traditionally considered investment banking.

Backed by a corporate culture supported by the highest professional qualifications and deep experience, the effectiveness of Coronation Insurance's reinsurance structures were particularly evident during the 2021 Lagos rain storm as well the 2020 EndSars riots which engulfed the country. Losses in both of these catastrophes were both numerous and severe, challenging the reinsurance structures of many insurers. The rigour of Coronation Insurance's analytically-informed reinsurance structures, however, meant that Coronation was almost unique in the Nigerian market in its ability to cover all of its client's risks, despite the scale of devastation and loss caused by these catastrophes.

Emerging risks such as climate change present uncertain outcomes for individuals and businesses and the impacts could be devastating. Political unrest is also a perennial risk in Africa. Since both these risks have the potential to be catastrophic they present considerable liquidity risk to individual insurers.

It is therefore important for the insuring public to understand the exposure of their insurers as well as how effectively their reinsurance programmes are structured to ensure that they can continue to meet their obligations to their customers.