Gareth Arnold talks to Liz Frederick, Head of ILS, Kane (Cayman) Limited

How would you summarise the current state of the ILS market, and in particular the cat bond market? Catastrophe bond issuances in the first half of the year were sluggish, with fewer bonds formed than expected. During this period, however, we also saw a marked increase in other alternative risk transfer structures, such as transformers, sidecars and collateralised reinsurance transactions. Additionally, we have seen an increase in cat bond issuance during Q3, which leads us to believe that activity during Q4 issuances will be quite robust.

There has been strong growth in the private collateralised reinsurance arena in recent years. Such structures have become increasingly cost effective and efficient, which has raised their market appeal. For example, in terms of time to market, whereas a cat bond can take eight to ten weeks to bring to market, these collateralised products can be issued within one or two days.

What are the key factors that have been influencing ILS activity? One of the major factors in the first half of the year was the string of catastrophes in the run-up to and during this period, including the Australian typhoon, the New Zealand earthquake, the Japanese earthquake and the US severe spring storms. During this period a number of cat bonds matured; however, rather than returning to market, many sponsors held back to see how this would affect the sector. This is not surprising as this has been one of the highest loss years on record for ILS/ILW transactions.

Another factor was the change to the RMS US Wind model, which increased severity of events and expected losses for a number of US regions. Many of the sponsors were left trying to understand how these changes would impact their cat bond transactions.

In terms of the transactions witnessed to date in Q3, the majority of these have focused on perils outside the US, such as Japanese quake and European windstorm.

What developments would you say would help to bolster the overall ILS market? In the first half of 2011, we witnessed a very interesting market dynamic. While cat bond numbers were low, we had a significant number of structures maturing resulting in a huge amount of capital becoming available with little in the way of supply. To grow the market, you have to have the products or the investors will go elsewhere.

To help develop the market further we need to extend its remit into other perils, make the existing market more efficient, and offer other types of structure that will heighten its investor appeal. This is perhaps why we have seen a rise in private structure deals this year, as sponsors seek alternative structures.

Also, the standard re/insurance market is offering very attractive rates at present, which is having a knock-on effect on ILS interest. If the market were to turn significantly this would increase sponsor interest in ILS structures.

How has the manager's role evolved to meet these changing market requirements? The manager must be much more proactive in terms of the structuring and ongoing management of the vehicles. Previously, the role was viewed as a straightforward administrative function as it was assumed such structures operated like Swiss clocks and required little active management. This is not the case, and the manager must constantly oversee all aspects of the transaction and be able to respond quickly and effectively to any market developments that impact it. This requires much broader expertise and more extensive understanding not only of the structures, but the dynamics of the markets which affect them. The manager is now much closer to the structure, the client and the market than ever before.

In what way have ILS transactions evolved in recent years? In the last five years, we have seen an expansion in the perils covered. Previously dominated by US windstorm and California quake, the market has grown to include perils such as European wind, Japanese quake, US winter storms, US wildfire etc. which has attracted more sponsors. We have even seen a move into healthcare.Additionally, there has been an increase in transparency in the ILS field. We have seen a rise in the amount of information provided to noteholders during the structuring process and prior to the deal closing. We are witnessing much more information being exchanged and much more quickly as well.

As a result of this, there is much more interaction and involvement on the part of the manager.