Insuring the "Uninsurable"

Gallagher

Insurance | Risk Management | Consulting

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CORE360™ INSIGHTS

Do not be misled, more operational risk is insurable than you may know. Let me explain. Regardless of your ownership structure (i.e., public vs. private), your organization likely has a process to identify the inherent risk factors that may adversely affect your business. Traditional insurance typically requires direct physical damage and/or bodily injury to trigger coverage for a financial loss attributed to these risk factors. Because of this, many key operational risks are thought to be uninsurable, even though coverage is available. These risks include:

- Decline in general economic conditions and disposable income levels
- Increased prices for, or unavailability of, raw materials and/or commodities
- Changes in federal or state legislation and regulation
- Volatile weather events (i.e., humidity or aridity, heat or cold, drought or excess precipitation, high winds or the absence of wind, snow or absence of snow, etc.)
- Significant decline in key economic indicators such as unemployment rate, housing starts, strength of U.S. dollar (or other currencies), autos manufactured, the yield curve, etc.

Many organizations have been financially impacted by a flood, wildfire or some other catastrophic exposure, yet their losses were not fully recoverable through their property insurance.

The fact of the matter is that all of these risks may be insurable through what is known as Parametric Insurance. By studying your historical earnings volatility related to weather, macro and microeconomic events, Gallagher can help you understand the correlation between the event (or set of events) and subsequent financial damage to your organization.

One of the most powerful differences between Parametric Insurance and traditional insurance—aside from the obvious flexibility in coverage—is the claim adjudication process. Once the "Parameters" are established and agreed to by the insurer, the coverage trigger is based on the preagreed parameters that are known to cause financial harm (i.e., event and valuation) so claim payments become streamlined. As long as the predefined incident occurs (such as a weather or economic event), the policy pays out at the preestablished valuation. This streamlined payout simplifies the claim adjudication process and accelerates payout from many

months (or years) to just weeks, or even days in certain situations. Below is a summary of other important differences between Parametric Insurance and traditional insurance:

CONDITIONS	PARAMETRIC INSURANCE	TRADITIONAL INSURANCE
Coverage Trigger	Event equaling or exceeding predefined threshold	Direct physical damage and/or bodily injury
Claim Process	Accelerated settlement based on predefined amount	Involves loss adjuster and quantifying damages
Recovery	Predefined amount	Indemnification of actual loss
Structure	Highly customized with multi-year, multitrigger options	Contract wording standard with some customization through endorsement
Term	Single or multi-year; up to 5 years	Annual; multiyear available, but not common
Form	Insurance or derivative	Insurance contract
Basis Risk	Correlation of external index and actual loss; Modeling accuracy very important	Given indemnification structure, policy conditions, deductible and exclusions

While the examples above are geared more towards minimizing key operational risks, Parametric Insurance has historically, and continues to be, an important weapon in your overall risk management program arsenal as it relates to nonphysical damage, business interruption exposure. Many organizations have been financially impacted by a flood, wildfire or some other catastrophic exposure, yet their losses were not fully recoverable through their property insurance. Parametric Insurance could be the right solution to avoiding such a financial calamity in the future.

Gallagher's team of actuaries, mathematicians and Alternative Risk Transfer ("ART") specialists work with you to identify, quantify and minimize these risks by customizing risk transfer programs to access contingent capital at some of the most thought-leading insurers throughout the world. I will give you a call to discuss how Parametric Insurance may apply to minimizing risks within your organization and answer any questions you may have regarding this valuable tool.

Learn More About Our CORE360™ Approach to Improve Your Organization's Risk Management Performance

*Gallagher **CORE**360™ is our unique, comprehensive approach of evaluating our client's risk management program that leverages our analytical tools and diverse resources for customized, maximum impact on six cost drivers of their total cost of risk. We consult with you to understand all of your actual and potential costs, and the strategic options to reallocate these costs with smart, actionable insights. This will empower you to know, to control and to minimize your total cost of risk and improve your profitability. Please contact your Gallagher Advisor to learn more.*

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