

Property Casualty 360

Cat Primer: Model Behavior

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Insurers and reinsurers begin the dance of cat-exposure estimation by plugging their books of business into a model, often averaging the results with those from one or more of the other available models from the three primary providers: AIR Worldwide, EQECAT (EQE) and Risk Management Solutions. They then incorporate calculations and indications from their own internal models, if they have them.

Following this output of data, companies choose the result that best suits the purpose of the modeling exercise—to purchase reinsurance, to please rating agencies, or to convince regulators that they need to hike prices, experts explained.

Jayant Khadilkar, a partner at privately held reinsurance broker and risk/capital management advisor TigerRisk in Stamford, Conn., said companies need a thorough understanding of what goes into the model, how they work, and how to translate the results.

“Models are a great tool, but they are just that—a tool,” said Mr. Khadilkar, who is also a former AIR executive. “Understanding the uncertainty in the model output and using the output in a way that informs business decisions—and still reflects that uncertainty—is extremely important.”

Models can be a “validation of your own decision-making,” said Frank Pierson, executive vice president and chief technical officer at New York-based reinsurance brokerage firm Holborn Corp.

Mr. Pierson said he would never advise a client to use one model over another. Each are “trying to do the best job” but come up with “very different answers with different points of view.”

And no matter how good the model, none are fail proof. “You just can’t snap your fingers and get away from risk,” Mr. Pierson said.



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