Aon Benfield

Insurance-Linked Securities

Q1 2017 Update

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First Quarter 2017 Catastrophe Bond Transaction Review

Catastrophe bond issuance for the 2017 calendar year made a robust start. In the first quarter of 2017, USD2.17 billion of limit was placed—just short of the all-time record USD2.21 billion that came to market in the first quarter of 2016. This is in contrast to the weak second quarter of 2016 where the record first quarter issuance was followed by the lowest level of second quarter issuance since 2011. As the preliminary view on primary catastrophe bond issuance for 2017 is USD8 billion, Q2 2017 is expected to match the brisk issuance pace of Q1.

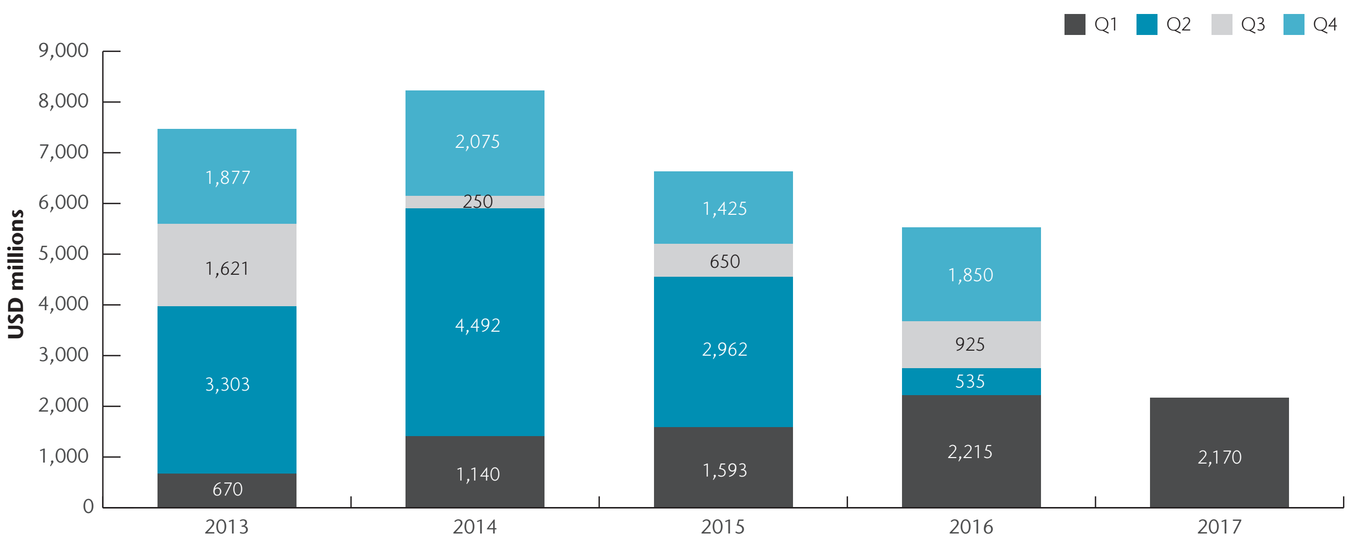
In the first quarter of 2017, USD2.0 billion of catastrophe bond limit matured; however, there was an expansion in the overall market, as new issuance slightly outpaced maturities. Of greater significance, however, is the further USD4.2 billion set to mature in the second quarter. Investor capacity remains poised to replace maturing capital with strong demand for new issuances.

The majority of issuance in Q1 2017 came from returning sponsors to the catastrophe bond market.

Downward pressure was seen on interest spreads—a trend that was particularly pronounced for sponsors that issue similar deals year-over year—and sponsors were able to capitalize on strong market demand to upsize transaction sizes.

Looking ahead, and with strong demand for new issuances investor capacity remains poised to replace the USD4.2 billion of limit that is set to mature in Q2 2017.

Catastrophe Bond Issuance by Quarter



Source: Aon Securities Inc.

First Quarter 2017 Catastrophe Bond Issuance

Beneficiary	Issuer	Series	Class	Size (millions)	Covered Perils	Trigger	Rating	Expected Loss[1]	Interest Spread
First Quarter									
XL Insurance (Bermuda) Ltd	Galilei Re Ltd.	2017-1	A-2	$50.0	US HU & EQ, EU Wind, AUS CY & EW	Industry Index	Not Rated	9.55%	13.25%
			B-2	$50.0				4.98%	8.00%
			C-2	$150.0				3.02%	6.25%
			D-2	$150.0				2.03%	5.25%
			E-2	$125.0				1.45%	4.50%
Aetna Life Insurance Company	Vitality Re VIII Limited	2017-1	A	$140.0	US MBR	Indemnity	BBB+ (S&P)	0.01%	1.75%
			B	$60.0			BB+ (S&P)	0.19%	2.00%
Heritage Property & Casualty Insurance Company and Zephyr Insurance Company, Inc.	Citrus Re Ltd.	2017-1	A	$125.0	FL, GA, NC, SC HU	Indemnity	Not Rated	3.65%	6.00%
ICAT Syndicate 4242	Buffalo Re Ltd.	2017-1	A	$105.0	FL/LA HU	Indemnity	Not Rated	1.15%	5.25%
			B	$59.5				11.41%	16.25%
Sompo Japan Nipponkoa Insurance Inc.	Aozora Re Ltd.	2017-1	A	$480.0	JP TY	Indemnity	Not Rated	0.90%	2.20%
Allstate Insurance Company	Sanders Re Ltd.	2017-1	A	$375.0	US HU, EQ, ST, WS, VE & MI	Indemnity	Not Rated	0.97%	3.00%
State Farm Fire and Casualty Company	Merna Re Ltd.	2017-1	A	$300.0	US (New Madrid) EQ	Indemnity	Not Rated	0.41%	2.00%
Total Closed During Q1 2017				$2,169.50					

1 *Expected loss represents initial one-year annualized figures with WSST sensitivity when applicable*

Source: Aon Securities Inc.

Legend

AUS – Australia
FL – Florida
HI – Hawaii
LA – Louisiana
JP – Japan
US – United States
EU – Europe

CY – Cyclone
EQ – Earthquake
HU – Hurricane
OP – Other Perils
ST – Severe Thunderstorm
MBR – Medical Benefits Ratio
MI – Meterorite Impact
VE – Volcanic Eruption
WF – Wildfire
WS – Winter Storm

To start the year, XL Bermuda Ltd closed the second part of its USD1.275 billion transaction, Galilei Re Ltd. with the USD525 million Series 2017-1 installment of the issuance. The Series 2017-1 notes issued under the program provide annual aggregate protection against worldwide weighted industry insured losses for a four-year term.

Citrus Re Ltd. Series 2017-1, issued on behalf of Heritage Property & Casualty Insurance Company, was the sponsor's fifth issuance in the catastrophe bond market. The USD125 million single class of notes provide protection on an indemnity basis for losses arising from named storms in the initial covered areas of Florida, Georgia, North Carolina and South Carolina. The notes included several features new to the insurance-linked securities market, including loss adjustment expenses being covered on an indemnity basis and a mechanism that allows for a risk spread adjustment based on changes in the ceding insurer's exposure mid-way through each annual risk period. The transaction priced 50 basis points below the low end of the initial pricing guidance.

The USD375 million Sanders Re Ltd. Series 2017-1 transaction, on behalf of Allstate Insurance Company and its affiliates, provides collateralized reinsurance protection on an indemnity basis for losses arising from named storm, earthquake, severe thunderstorm, winter storm, volcanic eruption and meteorite impact and covers the District of Columbia and 48 states of the U.S. (excluding Florida and initially New Jersey). Investor demand allowed the transaction to upsize from USD300 million and price at 3.00 percent; 25 bps below the lower end of the initial price guidance of 3.25 to 3.75 percent. The transaction is the largest ever to secure U.S. hurricane coverage for five wind seasons on an indemnity basis.

The Merna Re Ltd. Series 2017-1 transaction, on behalf of State Farm Fire and Casualty Company ("State Farm"), is the third catastrophe bond transaction from the Merna Re Ltd. program and sixth overall on behalf of State Farm to exclusively cover New Madrid Earthquake exposure. The single class of notes provide USD300 million of collateralized reinsurance protection on an indemnity per occurrence basis for losses arising from earthquakes (including fire following). The New Madrid Covered Territory was expanded to include the state of Oklahoma. The transaction was well received by the market, pricing at the lower end of initial price guidance at 2.00 percent. This represents an 11 percent reduction from the initial risk interest spread of Merna Re Ltd. Series 2016-1, which covers similar exposure and risk levels and priced in March 2016.

Aozora Re Ltd. Series 2017-1, on behalf of Sompo Japan Nipponkoa Insurance Company ("SJNK"), is the third catastrophe bond transaction from the Aozora Re Ltd. program covering Japan typhoon. The single class of notes provide USD480 million of collateralized reinsurance protection on an indemnity per occurrence basis for losses arising from typhoon. The transaction achieved both an upsize from initial target size, and priced at the lower end of revised price guidance at 2.00 percent. This represents a 20 bps reduction from the Initial Risk Interest Spread of Aozora Re Ltd. Series 2016-1, which covers similar exposure and risk levels and priced in March 2016.

Buffalo Re Ltd. Series 2017-1, on behalf of ICAT Syndicate 4242 ("ICAT"), is the first catastrophe bond transaction from the Buffalo Re Ltd. program and an infrequent offering on behalf of a Lloyd's syndicate, covering U.S. named storm and earthquake exposure. Two classes of notes provide USD164.50 million of collateralized reinsurance protection on an indemnity per occurrence basis with cascading coverage offering protection when one tranche is fully eroded. Revised price guidance saw both an upsize in issuance size and a reduction in pricing spread with both tranches ultimately pricing at the lower end of revised price guidance.

Aon ILS Indices

The Aon ILS Indices are calculated by Bloomberg using month-end price data provided by Aon Securities Inc.

During the first quarter of 2017, all Aon ILS Indices posted gains, although only the U.S. Earthquake index posted a gain from the same time period the prior year. The BB-rated Bond and U.S. Earthquake Bond indices achieved the greatest growth with returns of 1.03 percent and 1.20 percent, respectively. The Aon All Bond index and U.S. Hurricane indices followed with returns of 0.98 percent and 0.65 percent, respectively. The Aon ILS Indices performed with mixed results relative to benchmarks, but did outperform the 3 to 5 year US Treasury Notes Index and the CMBS 3-5 Year, Fixed Rate Index.

The annual returns for all Aon ILS Indices outperformed the prior year's annual returns, driven by tightening spreads in the secondary market and the absence of a major catastrophe. The 10-year average annual return of the Aon All Bond Index, 7.70 percent, continued the trend of outperforming comparable benchmarks and reinforces the value of a diversified book of pure insurance risks for investors' portfolios over the long term.

Aon ILS Indices[2]

Index Title	Return for Quarterly Period Ended March 31		Return for Annual Period Ended March 31	
Aon ILS Indices	2017	2016	2017	2016
All Bond Bloomberg Ticker (AONCILS)	1.03%	1.81%	6.21%	5.66%
BB-rated Bond (AONCBB)	0.98%	1.43%	4.50%	4.28%
U.S. Hurricane Bond (AONCUSHU)	0.65%	0.72%	6.97%	6.36%
U.S. Earthquake Bond (AONCUSEQ)	1.20%	1.09%	4.95%	3.26%
Benchmarks				
3-5 Year U.S. Treasury Notes (USG2TR)	0.58%	2.50%	-0.63%	2.62%
3-5 Year BB U.S. High Yield (J2A1)	1.26%	2.85%	9.94%	0.62%
S&P 500 (SPX)	5.53%	0.77%	14.71%	-0.39%
ABS 3-5 Year, Fixed Rate (R2A0)	1.22%	1.38%	2.68%	1.72%
CMBS 3-5 Year, Fixed Rate (CMB2)	0.67%	2.36%	1.34%	2.34%

Source: Aon Securities Inc. and Bloomberg

[2] *The 3-5 Year U.S. Treasury Note index is calculated by Bloomberg and simulates the performance of U.S. Treasury notes with maturities ranging from three to five years.*

The 3-5 Year BB U.S. High Yield index is calculated by Bank of America Merrill Lynch (BAML) and tracks the performance of U.S. dollar denominated corporate bonds with a remaining term to final maturity ranging from three to five years and are rated BB1 through BB3. Qualifying securities must have a rating of BB1 through BB3, a remaining term to final maturity ranging from three to five years, fixed coupon schedule and a minimum amount outstanding of $100 million. Fixed-to-floating rate securities are included provided they are callable within the fixed rate period and are at least one year from the last call prior to the date the bond transactions from a fixed to a floating rate security.

The S&P 500 is Standard & Poor's broad-based equity index representing the performance of a broad sample of 500 leading companies in leading industries. The S&P 500 Index represents price performance only, and does not include dividend reinvestments or advisory and trading costs.

The ABS 3-5 Year, Fixed Rate index is calculated by BAML and tracks the performance of U.S. dollar denominated investment grade fixed rate asset backed securities publicly issued in the U.S. domestic market with terms ranging from three to five years. Qualifying securities must have an investment grade rating, a fixed rate coupon, at least one year remaining term to final stated maturity, a fixed coupon schedule and an original deal size for the collateral group of at least $250 million.

The CMBS 3-5 Year, Fixed Rate index is calculated by BAML and tracks the performance of U.S. dollar denominated investment grade fixed rate commercial mortgage backed securities publicly issued in the U.S. domestic market with terms ranging from three to five years. Qualifying securities must have an investment grade rating, at least one year remaining term to final maturity, a fixed coupon schedule and an original deal size for the collateral group of at least $250 million.

The performance of an index will vary based on the characteristics of, and risks inherent in, each of the various securities that comprise the index. As such, the relative performance of an index is likely to vary, often substantially, over time. Investors cannot invest directly in indices.

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Secondary Trading Update

The secondary markets continued to decrease in activity in the beginning of Q1 2017, as investors were more focused on bond maturity and primary issuance activity. According to FINRA's Trade Reporting and Compliance Engine (TRACE), there were 175 trades totaling USD211.7 million during the period. This represented a decrease in trade volume of 44 percent, and dollar volume of 31 percent compared to Q1 2016. When compared to more recent TRACE reported trading activity, the decrease in trade volume was less dramatic and consistent with recent trends, with trade volume decreasing 13 percent from Q4 2016 and dollar volume increasing five percent since Q4 2016.

Trading activity was inconsistent until March, as many bonds matured within the first few weeks of the first quarter. Throughout the month, as new issuances were frequently announced to the market, investors were given plenty of opportunity to utilize their freed-up capital. Additionally, investors looked to move bonds in the secondary market to create room in their portfolios for the new issuances. Two bonds reported 10 trades or more; Caelus Re Ltd Series 2016-1 and Bosphorus Re Ltd. Series 2015-1.

In March, Florida Citizens Property Insurance filed an optional termination notice allowing for an early redemption of the USD300 million Everglades Re II Ltd. Series 2015-1 catastrophe bond. Prior to filing the notice, Florida Citizens had to receive approval for such an action from its board; early redemption meant that both of the company's catastrophe bonds would expire in 2017, allowing the company to re-enter the catastrophe bond market and take advantage of the current pricing environment.

3 *Note that this is an underestimate of total market volume as trades in bonds rated below investment grade are capped at $1 million and foreign trades as well as trades by non-US broker dealers are excluded*

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