



Structuring of Insurance-Linked Securities (ILS) and its Application in Natural Catastrophe Risk Assessment

Christine Dietrich

Clariden Leu, Zurich, Switzerland (christine.dietrich@claridenleu.com)

Capital markets play a crucial role in natural catastrophe risk transfer and risk mitigation processes. Currently, with total investments exceeding USD 12bn in natural catastrophe bonds, there is a need for better understanding of the science of natural catastrophes and its applications. This paper explains the structuring of Insurance-Linked Securities (ILS), its applications, and its associated difficulties.

Diversification of risks in insurance is a principal benefit derived by capital market investments. In addition, the profitability of ILS funds is less volatile than other asset investments. However, financial transactions are often heavily dependent on vendor catastrophe models. Due to the complexity of the financial transactions associated with the structuring of Insurance-Linked Securities (ILS), the risk assessment processes are in turn often difficult to replicate. The resultant product is thus subject to considerable uncertainties.