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Cat Bonds Alternatives Allocation Update

Q3 2026

In a Nutshell

Strong El Nino conditions suppress Atlantic hurricane activity in Q3

Summary

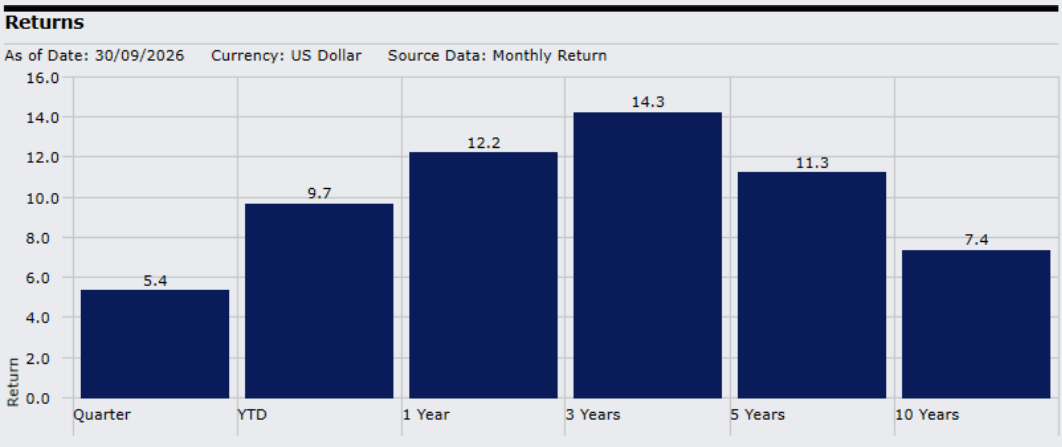
Cat bonds delivered another strong quarter due to a lack of hurricane activity in the Atlantic. The Cat bond index was up over 5% (in USD terms) in Q3, bringing the YTD return to nearly 10%. Cat bonds remain a powerful source of both return and diversification in balanced portfolios.

The Atlantic hurricane season has been very quiet this year due to strong El Nino climate conditions. For the first time since 1966, not a single hurricane formed by the end of September. Accumulated Cyclone Energy (ACE), a measure of total storm activity, is a fraction of its usual levels. Hurricane Isaias became the first hurricane to make landfall on 9th October, although it is unlikely to have any impact on Cat bonds. By contrast, activity has been much higher in the Pacific Ocean which is less relevant for Cat bonds. We caveat the above with the fact we are not yet through hurricane season.

The total yield on the index remains around 9%. Spreads have tightened due to a lack of storm activity. Helping to offset this is a higher collateral yield following recent interest rate increases by central banks. We retain the Cat bond allocation at 5% in balanced portfolios.

Performance

The SwissRe Cat bond index gained 5% this quarter in USD terms. The Cat bond index has compounded at 14%pa over the past three years (to end Sept 2026). Over the past ten years, Cat bonds have delivered a 7.4%pa annualised return with very low levels of volatility, making them an attractive source of diversification within balanced portfolios.

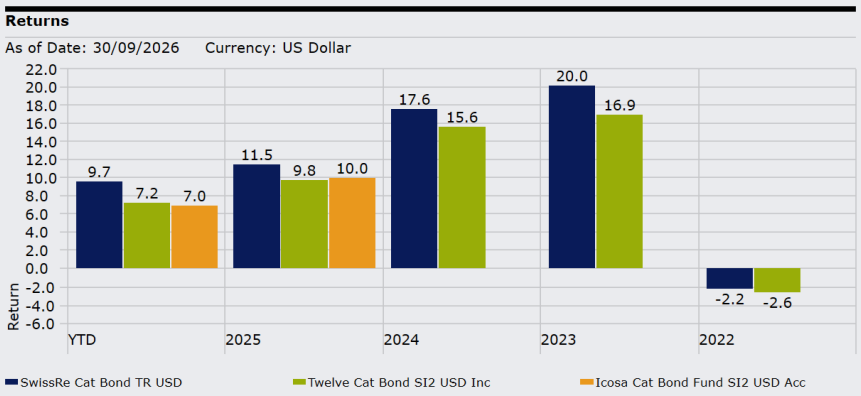


Source: Morningstar

Cat bonds delivered extremely strong returns over the past three years

Our two Cat bond funds (Twelve and Icosa) are up over 7% YTD (to end Sept). Their returns are slightly lower than the index as they have a lower percentage in higher-yielding US hurricane risk (roughly 2/3 of the index).

This follows three excellent calendar years between 2023-25. For example, the Twelve Cat bond fund was up 17% in 2023, 16% in 2024 and 10% in 2025. Icosa is a newer fund with a more limited track record, although the fund manager previously worked on the Twelve fund.



Source: Morningstar

Cat bonds are on track for another strong year

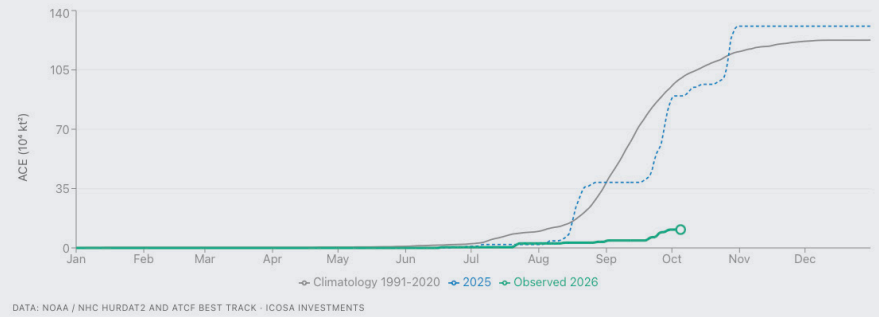
Active managers offer greater diversification (and hence lower risk) compared to the index, which is not investible.

Hurricane Season 2026 (so far)

The Atlantic hurricane season is the dominant risk (or peril) in Cat bond markets. Peak hurricane season occurs between August and October each year. The 2026 Atlantic hurricane season forecasts were for a below average season due to the impact of strong El Nino climate conditions, which we discussed in detail last quarter. However, storm activity has been even lower than forecast.

So far, there has only been one Atlantic hurricane that has made US landfall: Isaias. There have been no major hurricanes (category 4/5) at the time of writing in mid-October. Icosa, one of our chosen Cat Bond managers, commented on the slow start to the storm season:

"The Atlantic hurricane season has so far been exceptionally quiet. For the first time since 1966, not a single hurricane formed by the end of September; all named storms remained tropical storms. Accumulated cyclone energy (ACE), which combines the strength and duration of all storms, stood at only a small fraction of the long-term average for this point in the season at the beginning of October (see chart below). A key factor is this year's pronounced El Niño phase. The associated increase in wind shear has so far dampened storm activity in the Atlantic."

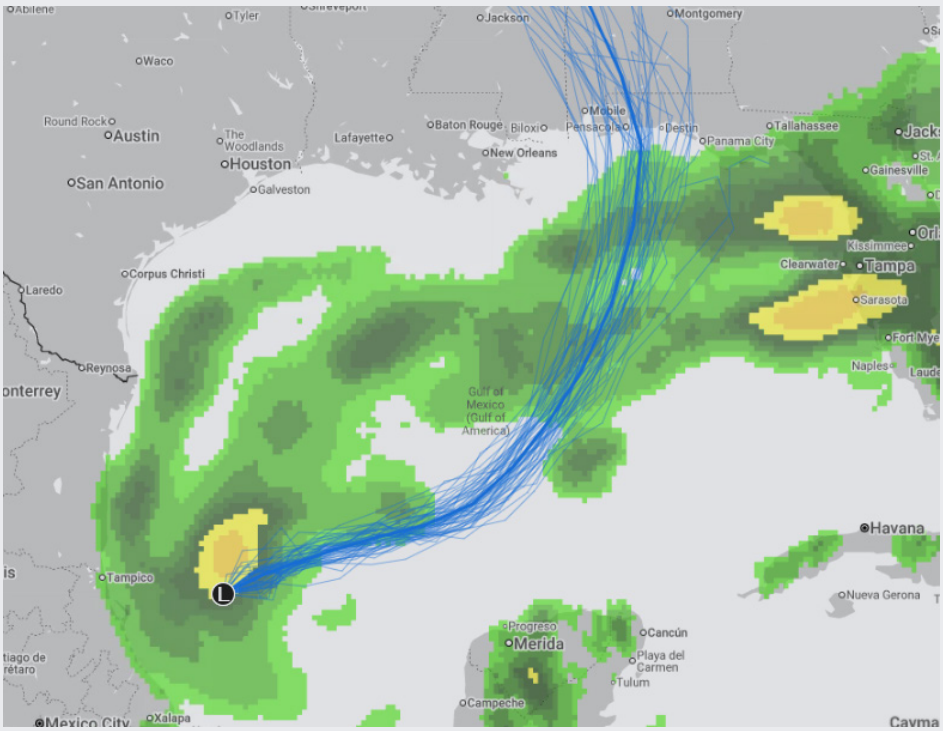


Source: Icosa

Storm activity (ACE) is a fraction of the 30yr average

We caveat all the above commentary with the fact that hurricane season is not yet over!

Hurricane Isaias made landfall on 9th October as a category 2 hurricane in the section of US coast called the Florida panhandle. It was briefly a category 3 hurricane at its peak before weakening as it approached land. Most estimates of loss for the insurance industry put damage estimates in the region of $5bn, which would have no impact on Cat bonds.



Source: Google DeepMind

Google Deepmind's AI model was a good guide to eventual landfall location and strength

By contrast, the Pacific Ocean has seen above average activity this year. This is less relevant for Cat bonds as the majority of Cat bond insurance is on the US east coast around Florida. The chart below shows the same Accumulated Cyclone Energy (ACE) tracking well above average for the Pacific.

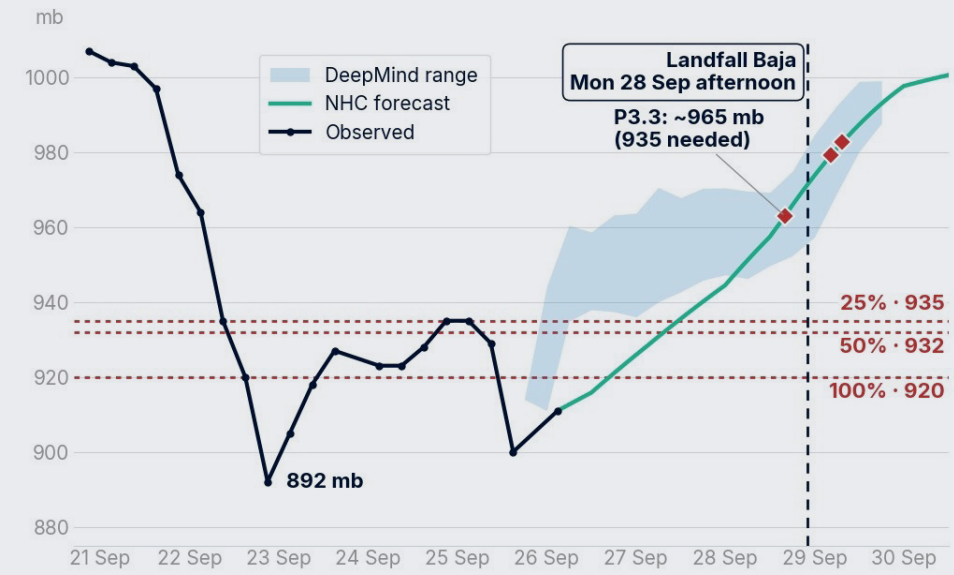


Source: Icosa

Storm activity (ACE) is above average in the Pacific Ocean

There have been two major recent hurricanes off the western coast of Mexico: Polo and Simon. Both storms threatened to trigger the IBRD CAR Mexico 2024 bond issued by the World Bank. This has a parametric trigger based on the central storm pressure as it reaches landfall. The pressure reading would need to fall beneath certain levels to trigger a pay-out. As a reminder, the lower the pressure the stronger the storm.

Hurricane Polo formed on September 20th and intensified into a category 5 hurricane in less than two days, which makes it one of the fastest intensifications ever observed in the East Pacific. It remained offshore for several days, before weakening and making landfall at the end of September. It passed over the Baja coast of California as a category 2 storm with 110mph winds, before making landfall in Mexico. The storm's minimum pressure at landfall was higher than the trigger required (935mb) for a pay-out on the bond, as the dotted lines in the chart below show.



Source: Icosa

How a parametric trigger works based on central storm pressure

Hurricane Simon was also closely watched by Cat bond managers in early October, after it reached category 4 offshore. It tracked along the same western coast but did not make landfall.



Source: Wikipedia

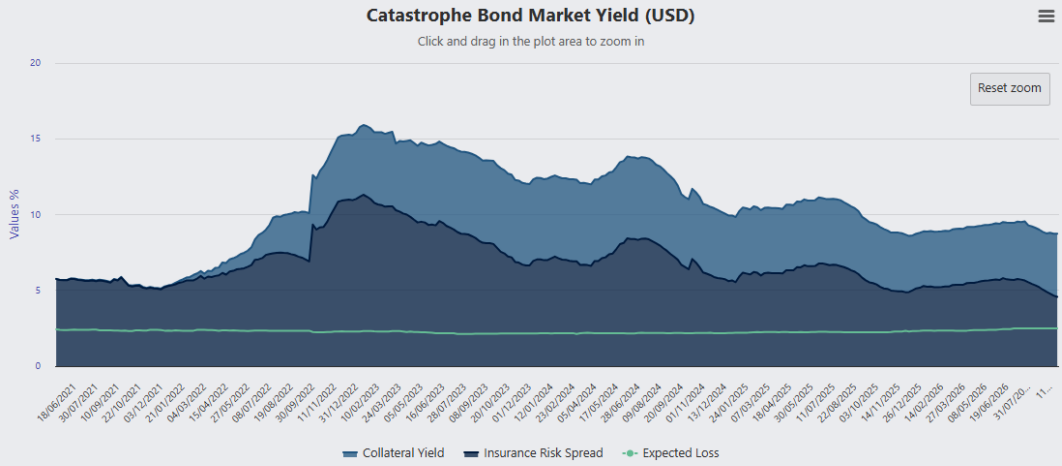
Hurricane Simon was a strong hurricane but remained offshore

Valuation / Yield

Yields on Cat bonds remain attractive at around 9%. The risk-free rate increased in line with recent rate hikes (a positive factor), whilst spreads have tightened because of a lack of major hurricanes making US landfall. Yields are still high in nominal terms, but they are closer to historical averages rather than the very attractive levels seen in recent years. In early 2023 spreads reached 11% and total yield 16%, for example. We have benefited in recent years from this spread compression (hence the strong returns).

As a reminder, the overall yield on a Cat bond comprises two elements:

- Risk free rate – has risen to 4.2% as central banks have increased rates.
- Credit spread – spreads have tightened to 4.6%, below the long-term average (6%).



Source: Artemis.bm (Oct 2026)

Spreads have tightened due to a lack of storm activity this season

Positioning

The Cat bond allocation in balanced portfolios remains 5%. We own two specialist Cat bond funds: Icosa and Twelve Securis. Icosa is a specialist Cat bond boutique set up by Florian Steiger, who was previously a portfolio manager at Twelve Capital. Icosa AUM has grown to over $1bn in just two years, which is great progress. Twelve Capital recently completed a merger with rival ILS firm Securis, forming the new combined firm Twelve Securis. Their fund is now over $4.5bn in size – one of the largest dedicated Cat bond funds.

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