MARSH

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Property Insurance Market Update

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At a glance

AUSTRALIA

Circa AUD
$1.7 billion
Cyclone Debbie estimated loss

The combined ratio for Fire and ISR in the Australian market remained above
110%

GLOBALLY

Highest year on record for catastrophe losses
2017
estimated at USD 144 billion

Global catastrophe losses exceeded USD
$100 billion
in 2005, 2011, 2017

Pursuit of profitability drives pricing

In 2017 the Australian property insurance market was characterised by a concerted push by major insurers to improve the profitability of their portfolios through a series of pricing measures. In some cases, this led to a complete review of their underwriting appetite for certain industries.

The success of these actions was tempered by Cyclone Debbie in the first half of 2017, which is estimated to have cost insurers circa AUD 1.7 billion.

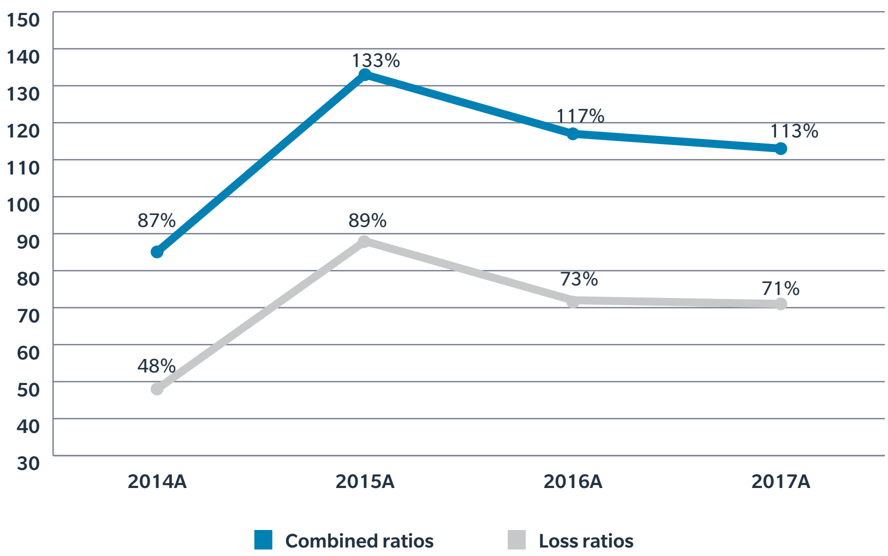
More recently, the earthquake that hit Papua New Guinea in February caused considerable damage to the Southern Highlands, a region containing a large LNG facility and other mining and energy infrastructure. The heavy losses sustained in this area is estimated in excess of AUD 1.25 billion.

With the continuation of a high industry combined ratio, which remained above 110% in 2017 for Fire and ISR (Figure 1), insurers are seeking further rate increases in 2018. This is also partly driven by stable to modest increases in reinsurance costs, reversing a five year trend.

Globally, insured catastrophe losses in 2017 resulted in the highest year on record, reaching USD 144 billion and making it the third year (along with 2005 and 2011) to have surpassed the USD 100 billion mark. Hurricanes Harvey, Irma and Maria, together with the earthquakes in Mexico and the wildfires in California accounted for much of the insured losses.

FIGURE 1

Fire and ISR



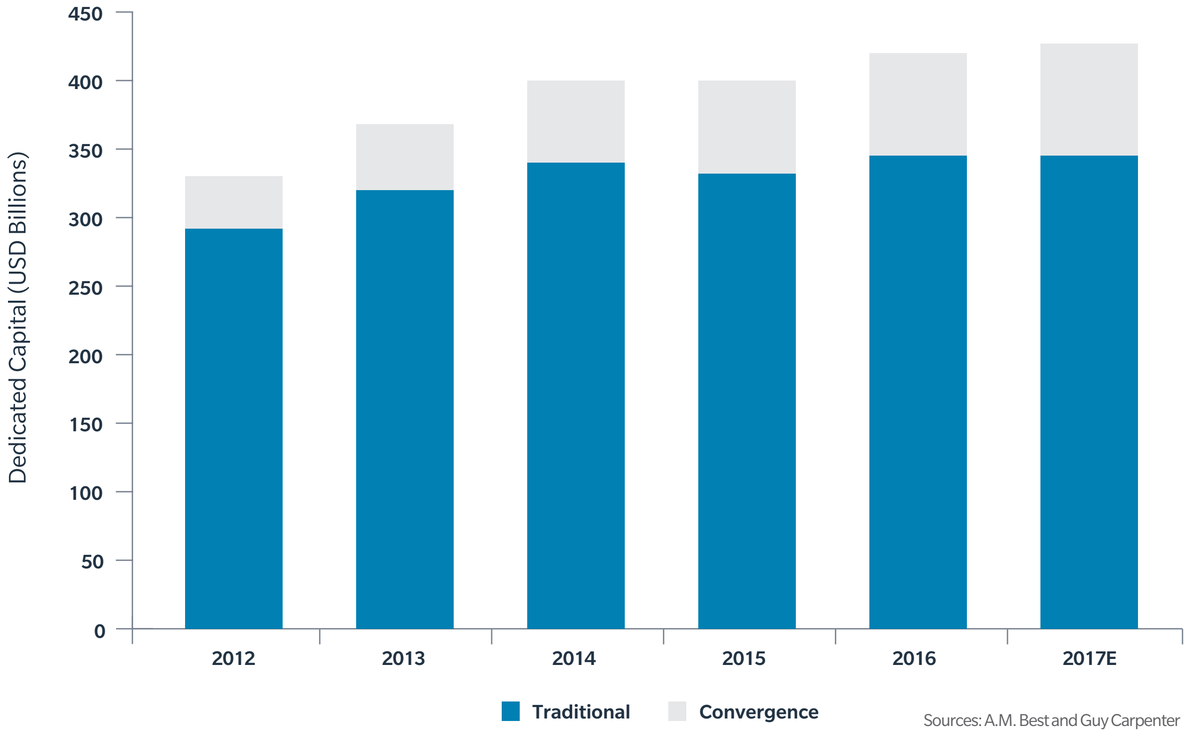
Source: Taylor Fry

It was anticipated that the reinsurance market would react strongly to these global losses and a significant firming in pricing would result. However, the capital imbalance in supply and demand has continued to hamper reinsurers' efforts to get meaningful price increases. Instead, the real pricing shifts that have emerged appear to be specific to the portfolio or geography.

Capital in the global reinsurance market increased again in 2017 albeit more modestly (Figure 2). While traditional capital remained flat, convergence capital grew 9% to an estimated USD 82 billion. The total estimated dedicated reinsurance capital at year end 2017 was USD 427 billion, a 2% increase on year end 2016.

FIGURE 2

Estimated dedicated reinsurance sector capital – 2012 to 2017



Sources: A.M. Best and Guy Carpenter

Guy Carpenter and A.M. Best Company's estimate of capital dedicated to the reinsurance sector from traditional sources was calculated using A.M. Best's proprietary capital model (BCAR) results as well as line of business allocations. The convergence capital total was derived from dedicated insurance-linked securities (ILS) managers, (re)insurance-sponsored managers and direct generalist investors. Convergence capital is deployed in industry loss warranties, catastrophe bonds, side-car capacity and collateralized reinsurance.

Industries under the spotlight

There is still meaningful competition in the low-hazard major corporate account space. Premium rates are rising modestly as insurers take a more conservative view driven by a concern over potential competition. However, insurers are still looking to grow market share in this segment and therefore willing to compete on attractive accounts.

Conversely, high-hazard industries are experiencing a relatively harsh price correction. The food and beverage industry, which utilises the building material Expanded Polystyrene (EPS), is being heavily scrutinised, while market capacity has shrunk dramatically in response to a number of major fire losses. One major insurer estimates EPS fire claims over the past 15 years to have reached AUD 2 billion in Australia.

EPS has been an issue in the Australian market for many years with the emphasis mainly on fire protection via automatic sprinklers. While protective measures continue to play a role on pricing, some insurers have been forced to withdraw completely from this market. Consequently, local competition has disappeared and capacity is now sought in Asia, London and Middle Eastern markets just to complete placements with medium to high policy limits.

The recycling industry is another that is experiencing significant rate increases. The insurance market has reacted to several years of major fire losses with most major insurers declining to participate on risks in this industry. The London market is accepting new recycling business but at a significant premium; in many cases pricing is being quoted at multiples of historical rates.

One major insurer estimates EPS fire claims over the past 15 years to have reached

$2 billion

in Australia

The complex risks market for mining, power and energy is still buoyant in terms of capacity despite several large losses (non-catastrophe) reserved from 2017. Premium rates are rising in line with general market conditions except for the businesses that suffered major claims, which have experienced more severe increases. Specifically in the downstream energy market, where the global premium pool is estimated at USD 2.1 billion, loss estimates for 2017 are approaching USD 5 billion. The widening gap has boosted expectations that a stronger market pricing correction will take place during 2018.

Mining, power and energy producers are also seeing premiums affected by commodity pricing. Rates are typically higher for business interruption as rising commodity prices result in increased revenue declarations.

In the middle market segment, there are still elements of competition but only for quality business. The traditionally-dominant insurers in this segment are taking a stronger stance on price correction and some of the major global insurers are capitalising on this opportunity to improve their market share. Premium rates are rising but at more modest levels where there is competition.

For SME buyers, who have seen premium rates rise over the past 18 months, the trend is continuing. High hazard risks are proving challenging with many clients now being placed in the underwriting agency market, which often have Lloyds as their security.

The Australian listed insurers have a very strong presence in the SME segment and we expect that to continue. Many insurance programs are placed on a package basis, and leveraging the buyer’s total premium spend is proving an ever-important strategy in mitigating premium increases.

Looking ahead

Overall, the major shift in the insurance market's dynamics is insurers' renewed focus on underwriting for profit rather than for growth. Increasingly, insurers have been showing a reduced appetite for catastrophe-exposed risks. We expect to see major insurers further control their aggregate exposures for catastrophe risks such as earthquake, flood and weather perils. This is likely to be acutely felt by buyers of insurance in North Queensland and, more generally, those above the 26th parallel.

Changes to insurers' focus are necessitating a refinement of renewal placement strategies, including:

Starting

the process much earlier than in previous years

Supplying

highly detailed information relating to risk protection and risk engineering needs

Ensuring

that policy limits and sub limits are realistic and reflect the risk profile with awareness that there will be a cost associated with any unnecessary cover(s)

Being prepared

to consider higher deductibles or look to trade increased risk for premium reductions to mitigate the impact of market conditions

For more information, visit marsh.com, or contact your local Marsh representative.

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