

Marsh News

News for Marsh clients in Australia



Australian insurance market review

The insurance market is rapidly changing from the environment that followed the events of September 11, 2001.

As we approach the renewal period of June 30, we are seeing insurers actively competing for business and this increased competition is creating a more favourable insurance market for clients in a number of classes of insurance, especially clients with quality risks.

Premium rates in some classes of insurance, such as Property insurance, are generally reducing. In the lines that have performed more poorly over the past few years such as Public and Products Liability and Directors' and Officers' Liability insurance, the rate of premium increases has moderated or started to level off, particularly where there had been compound increases in the last two years.

This increased competition is creating a more favourable insurance market for clients in a number of classes of insurance, especially clients with quality risks.

This change in the market is not a result of pricing finally reaching acceptable underwriting levels, but rather the result of competitive forces that are at work once again in both the local and global markets.

This issue

- The benefits of providing good risk information

What has caused this new-found competitiveness in the marketplace?

There are a number of factors that have created the changing marketplace environment including:

- Substantial improvements in insurer underwriting results (premium versus claims) following the significant increase in global premium levels post September 11, 2001. This has been seen in both the Australian and overseas insurance markets.

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- Lower levels of claims recorded. In particular, catastrophe insured losses have been lower than average over the past two years.
- Improvements in the investment marketplace have helped insurers and reinsurers start to achieve increases in investment yields

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and realise capital gains. This, in turn, has contributed to positive financial returns for insurers.

- The return to profitability has enabled insurers to build a surplus once again.
- New capacity has been brought to the marketplace by new entrants who are free of claim reserve issues and latent legacy exposures.

As a result of the improved financial results reported by most insurers at the end of 2003, we are now seeing a more confident and robust global marketplace seeking growth opportunities. Many of these underwriters, in particular Lloyd's of London, have shown a renewed interest in offering increased capacity and competitive terms on a range of risks for Australian clients in the first quarter of 2004.

This is good news for clients who, in many cases, have had to go overseas in recent, renewal campaigns to search for necessary capacity in completing the placement of their insurance programs. This was because there was either insufficient capacity in Australia or an unwillingness by

Australian underwriters to offer terms, or the more traditional overseas markets were not offering terms that were acceptable.

While underwriters are prepared to be competitive, they will also remain cautious by retaining a measure of discipline as a result of greater internal underwriting

controls that are now imposed and the new regulatory environment in which insurers now operate.

Trends in major classes

Property

Property rates stabilised and, in some cases, began to reduce in the second half of 2003. That trend has continued in the first quarter of 2004, with rates falling in the vicinity of 10-15% and sometimes higher for high-risk accounts or where premiums had previously increased substantially. Most Property insurers have enjoyed excellent financial returns in recent years. As a result, we are now seeing Property insurers actively competing to retain quality accounts and maintain market share, particularly on renewal business, and aggressively seeking new business opportunities to meet budget growth targets.

There has been an increase in capacity in the marketplace, particularly in London where we have seen meaningful competition amongst insurers for some time. This has been to the advantage of policyholders, especially those who continue to demonstrate good risk

management practices, conduct risk profile analyses and can control and reduce the frequency of losses. A strong link between risk and price is, therefore, likely to continue.

The changing marketplace means we are seeing greater flexibility by insurers, which has been shown in an easing in policy restrictions, an opportunity to adopt a manuscript style wording and an ability to increase program policy limits and sub-limits. However, insurers are still reluctant to reduce retention levels or deductibles.

Public and Products Liability

The state of the marketplace and the pace of change continues to be different for the Public and Products Liability market compared to the Property market.

In 2003, we saw the Public and Products Liability market contract further with across-the-board, double-digit premium increases. However, we are now seeing this class of insurance beginning to change favourably to the insureds' benefit.

More underwriters are now prepared to look at offering terms. This has meant that the rate of increase in premiums has slowed. We are also seeing that insurers are focusing on individual account characteristics, including risk management practices and incident experience rather than imposing blanket across-the-board increases when pricing primary Public and Products Liability business. At the end of the first quarter of 2004, we were generally experiencing rate variations of plus or minus 10% on renewal business depending on individual risk profile circumstances.

Even though Public and Products Liability insurance is a long-tail class of insurance, it is beginning to show profitability as insurers become more confident in delivering improved underwriting results. The effects of the various state and federal tort reform legislation are also beginning to result in a more favourable Public and Products Legal liability environment in Australia. However, the full impact of tort reform on the insurance industry will not be seen for some time yet.

Although this class of insurance is continuing to experience premium increases for the more difficult risk profile accounts, they are at a reduced rate. There are also new entrants in the Australian primary Public and Products Liability market who will add much needed local competition, albeit in a measured form.

Umbrella and Excess Liability capacity is not an issue this year except for the unusual or difficult risks. Pricing for Umbrella and Excess lines has stabilised and slight reductions have occurred in some infrequent cases.

The market environment generally remains flat in maintaining current limits of liability. Even though there is an increased ability to offer greater capacity, insurers are not generally offering greater limits.

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Crime/Fidelity

This class of insurance has been difficult for both insurers and insureds and this year is not proving to be any different.

This class of insurance is still highly specialised and carefully underwritten even though there have been substantial increases in premiums and retentions over the last three years. Premiums vary depending on specific account characteristics. Limits of Liability continues to be restricted with clients obtaining higher limits and acceptable terms based on their own quality internal systems and adequate corporate governance procedures.

Few insurers are willing to enter the market despite the significant changes to the cover form and pricing. The leading three insurers in Australia control over 70% of the corporate market share. This class of insurance has, in recent years, still not generated a premium pool significant enough to cover industry losses. This will be the reason that this class will remain difficult with few alternative options available.

Professional Indemnity

Market conditions have started to improve for some professions in 2004, but still remain difficult for many other professions.

Due to new provisions imposed on underwriters by the Australian Prudential Regulatory Authority (APRA), some insurers were either unable or unwilling to write new business throughout much of 2003.

New capacity has entered the market in 2004, which has increased competition. However, insurers remain quite specific about the types of risk which they will underwrite.

Most existing insurers appear to have been successful in negotiating reinsurance treaties on reasonable terms at 31 December 2003, which has led to some insurers starting to look for new business in 2004.

Insurers also appear to be reasonably convinced that premium rates have returned to levels where sustained underwriting profits and an acceptable return on equity margins can be achieved. As a result, premium rate increases are starting to level off with average increases now generally being kept to around 10% unless there has been either significant growth in the client's business or a deteriorating claims experience.

However, many professions still continue to find it extremely difficult (and in some cases impossible) to obtain cover at any price. Or, if cover can be obtained, it is often subject to reductions in available limits or substantial policy restrictions. Many professions are also required to demonstrate to insurers evidence of having implemented comprehensive risk management programs prior to obtaining cover.

Directors' and Officers' Liability

Market conditions for Directors' and Officers' Liability have started to improve but continue to remain challenging for companies in many industry segments.

Competition has returned to the marketplace for high-quality companies in solidly performing industry segments, which can demonstrate good corporate governance and sound financial performance.

The small-to-medium enterprise (SME) market segment is particularly competitive amongst insurers at present. Larger corporate entities have also started to receive some relief from the significant increases in premiums, which have occurred over the past two years.

The average increases are now generally being kept to below 15% unless there has been either a deterioration in the financial performance or claims experience.

Companies with poor financial performance continue to find it difficult (and in some cases impossible) to obtain cover or are subject to reductions in available limits or substantial policy restrictions.

Workers Compensation

Western Australia

Western Australia is the country's largest privately underwritten Workers Compensation system. After several years of significant premium increases the last couple of years have seen premiums stabilise.

There are only five or six major Workers Compensation underwriters operating in Western Australia and they can load or discount Gazette Rates (Gazette Rates for all industries are published annually and remain in place for 12 months with effect from 30 June) depending on their assessment of the risk.

Insureds whose claims experience and Occupational Health and Safety (OH&S) practices are good are currently receiving premium reductions.

The current Government has recently tabled the Workers Compensation Reform Bill 2004 that proposes far-reaching amendments aimed at improving benefits to injured workers. This legislation could come into effect before the end of 2004. If it does, independent actuarial estimates predict that the cost of Workers

Larger corporate entities have also started to receive some relief from the significant increases in premiums, which have occurred over the past two years.

Compensation claims could increase between 9% and 13%. These increases would, of course, be passed onto the insurance buyer by the underwriters.

Government Administered States (New South Wales, Victoria, South Australia and Queensland)

New South Wales and Victoria have been engaged in detailed reviews of injured worker benefits and entitlements, scheme operation and premium methodology over the last few years. These reviews have triggered significant changes. In both states we are starting to see premium increases as a result.

However, employers with good OH&S and injury management practices are not experiencing increases of the same magnitude as employers with poor claims experience.

The South Australian scheme has also reported a deficit. As such we are starting to see premium rate increases being introduced to manage this blowout in unfunded liabilities.

In both Queensland and Victoria, changes have been made to the

rules surrounding succession of claims experience. Past claims experience will not apply where businesses have been acquired unless the organisations divesting and/or acquiring are deemed to be related under the Corporation's Act. This provides relief to organisations acquiring new businesses.

Other Classes

Marine, Motor and Personal Accident classes of insurance continue to be competitive. However, reductions in premiums cannot be expected to be significant given that these short-tail classes of insurance have not had the same large increases that the Property class has experienced in the last three years.

How sustainable is a more favourable insurance market environment?

The consolidation of the global insurance market both in Australia and overseas, and a more financially accountable regulatory environment have been influencing factors in the change in the marketplace.

Today, the global insurance market dynamics are such that if there was a sharp deterioration in insurers' loss ratios, underwriters would react more quickly to correct the position and avoid posting poor financial results.

There is also a heightened awareness that changes in the marketplace are an absolute (continued page 6)

The benefits of providing good risk information

The last twelve months has produced positive and now sustainable corrections in Global Insurance Markets. Whilst many classes of insurance have been favourably affected, Property Insurance has produced the most favourable outcomes for major clients.

Despite these positive developments, underwriters in both Australia and elsewhere in the world continue to demand

ensures that underwriters receive relevant and meaningful information about an organisation's current risks.

Such investment decisions should be made well before the insurance renewal cycle starts in earnest. That way, if the investigations discover adverse risk factors, there is time to find a workable resolution.

Insurers are generally positively disposed towards a client investing their own time, as well as using independent expertise, to help them understand the risk.

clarity in terms of an organisation's risk profile supported by the provision of accurate and highly professional underwriting information.

In this market, it can be helpful to go further and arrange a joint oral presentation (involving the consultant, broker and client) to support the written submission. Insurers are generally positively disposed towards a client investing their own time, as well as using independent expertise, to help them understand the risk.

Even if all aspects of a risk improvement plan cannot be implemented in time for the renewal discussions, a firm commitment timetable can be presented to insurers.

The last three years has witnessed an increasing preference for underwriters to obtain their own view as to a client's risk profile by the involvement of in-house risk specialists.

Organisations who invest in showcasing their risk profile and risk management efforts to insurers are more likely to extract the best from the emerging competitive trends in the market.

Whilst Marsh remains supportive of underwriters seeking to expand the value that they add to the insurance transaction we can provide a range of specialist risk consulting services that are truly independent of the underwriting process.

Even if all aspects of a risk improvement plan cannot be implemented in time for the renewal discussions, a firm commitment timetable can be presented to insurers.

Marsh's Risk Consulting practice can prepare an Underwriting Information Report which

It also removes uncertainty as to how well written submissions are considered and allows questions to be asked and answered. The cost of the investment is usually re-paid many times through better renewal terms.

For more information please contact your Account Executive or Roger Estall on 02 9375 9806 or email roger.j.estall@marsh.com

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requirement to achieve acceptable financial returns for shareholders. However, it is critical to balance this need for acceptable financial returns with the need to maintain a level of underwriting discipline.

The continued financial improvement and health of the reinsurance sector (especially the ability of direct insurers to collect reinsurance recoverables) underpins the marketplace's ability to continue to deliver lower premium rates and ease policy restrictions.

Another key driver in determining future market conditions is the adequacy of reserving past losses by insurers, and in particular, any unknown latent risk issues that could arise in the future.

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Summary

In order for market conditions to remain favourable, the impact of global economic factors must allow insurers and reinsurers to continue to post improved financial results. Perhaps to an even greater degree, these improved market conditions rely on the absence of significant natural and man-made catastrophe losses.

Clients who favourably differentiate their risks, practice risk management, maintain a disciplined and timely renewal process strategy and continue to improve the quality of underwriting information, will achieve greater benefits in the current market environment.

In order to manage the potential vagaries for future changes in market conditions it is good practice and prudent for clients to develop and maintain an effective tri-part relationship with program insurers and their account management team.

Disclaimer: This newsletter is only for general information and is not a substitute for specific advice. We accept no responsibility for any person or corporation acting on this information without prior consultation with us.

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