Insurance Industrys Best Year in Post-Crisis Era, but New Challenges in Growth, Price Competition, Make a Repeat Performance Unlikely, Say Execs

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NEW YORK, January 16, 2014 — Property/casualty insurers will be hard-pressed to repeat the industry's stellar 2013 performance, a panel of industry chief executives agreed at the 18th annual *Property/Casualty Insurance Joint Industry Forum*, held here on January 14.

The CEOs, drawn from a cross-section of the P/C industry, said a confluence of higher rates, fewer-than-normal catastrophes, and strong stock market returns seem likely to make last year one of the best of the past decade. But it may be a bit much to expect a repeat.

The New Year presents new challenges, with growth being an important one, the CEOs said. The industry's surplus is growing, with the increase in capacity possibly leading to increasing competitiveness on coverage terms and conditions.

Many commercial insurance buyers are enjoying above average earnings, noted Peter Hancock, CEO of AIG's global property-casualty business. "Their high profits will make them more likely to self-insure in the coming year, taking business from traditional insurers," he said.

Financial performance was just one of a host of topics the executives fielded from moderator Leigh Ann Pusey, president and CEO of the American Insurance Association. Panelists also agreed that low catastrophe losses were a bit of a good break for the industry.

General Re CEO Franklin (Tad) Montross said there were two one-in-1,000 events: flooding in the Colorado mountains and severe hailstorms in Germany. "But those, as well as the biggest recorded typhoon in history—Super Typhoon Haiyan in the Philippines—didn't generate large insured losses," he said, noting that relatively few of the losses were insured.

The reason: too few people realize they need insurance, according to Michael Sapnar, president and CEO of reinsurer Transatlantic Holdings. One example is California, where fewer than half those who should have earthquake coverage purchase it. "Insurers need to find a way to sell coverage in those areas," he said.

Last year's results were also buoyed by reductions of loss estimates from claims two or more years ago. That continued a trend over the past several years, but panelists agreed that trend is ready to peter out.

There was less agreement about the impact of alternative sources of capital. In the past few years, hedge funds and pension managers have gobbled up insurance-linked securities—bonds that can default if a catastrophe strikes. The bonds often compete directly with reinsurers that write catastrophe business. Last fall, rates for cat business fell 10 percent or more thanks to the competition from cat bonds.

The movement showed "that competition works," said Daniel Glaser, president and CEO of Marsh & McLennan Cos., a major reinsurance broker. Faced with competition, Glaser said, reinsurers became innovative. "They tailored products to client needs. Quota share treaties were available where none had been, reinstatement terms improved, coverage broadened and reinsurers wrote multi-year treaties more frequently."

Transatlantic's Sapnar didn't consider those actions innovations. He called them sure signs of a soft market. "I've done that," he said, recalling his own experience from the late 1990s. "And I've gotten killed for it."

Sapnar pointed out that his firm wrote a three-year deal this year; the first in almost a decade. Sapnar wasn't sour on the cat bond trend. "Reinsurers help underwrite or manage many of the securities, and their emergence helps counteract the contraction in the number of reinsurers over the past 20 years," he noted.

“Before, the catastrophe market was like an inverted pyramid,” said Sapnar. “Many insurers bought reinsurance from the same reinsurers. In essence the cat risk was being concentrated in relatively few hands. Now, the ILS market turns the pyramid into an hourglass. Money flows to reinsurers, then gets dispersed into the capital markets.”

Whether it’s good or bad, though, is a matter of perspective, noted Stuart Henderson, president and CEO of Western National Insurance Group, a Midwest mutual. “As a buyer, you’ve got to love the reinsurance world currently.”

While the panelists agreed that insurance-linked securities have become an important force, they agreed less on whether the securities would be around a few years from now. On one hand, the number of bonds being issued has mushroomed. But bond buyers could get skittish if a major catastrophe causes a string of defaults.

Montross compared the nascent market with collateralized debt obligations (CDOs), the complex financial instruments whose abuse helped drive the 2008 financial crisis. “Back then, CDO proponents hailed the same qualities praised about cat bonds today,” he said.

“If we were at a pension [fund] convention 10 years ago, we’d be talking about CDOs and CDOs squared,” he added. “We’d be calling it a good asset class, and we’d be calling it an uncorrelated asset.”

In the end, chances for a good year will depend on the economy. Several panelists pointed out that most parts of the economy seem to be picking up, which would create more exposures for the industry to cover.

But Kishore Ponnavolu, president of MetLife Auto & Home thought the situation was a bit more complex. “We’ve made a very nice recovery over the past couple of years,” he said, “but that only brings the economy back to where it was in 2008. So we’ve basically lost six years in the process.”

Reporters who have an interest in photos from the *Forum* can contact Loretta Worters at 212-346-5545; lorettaw@iii.org

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