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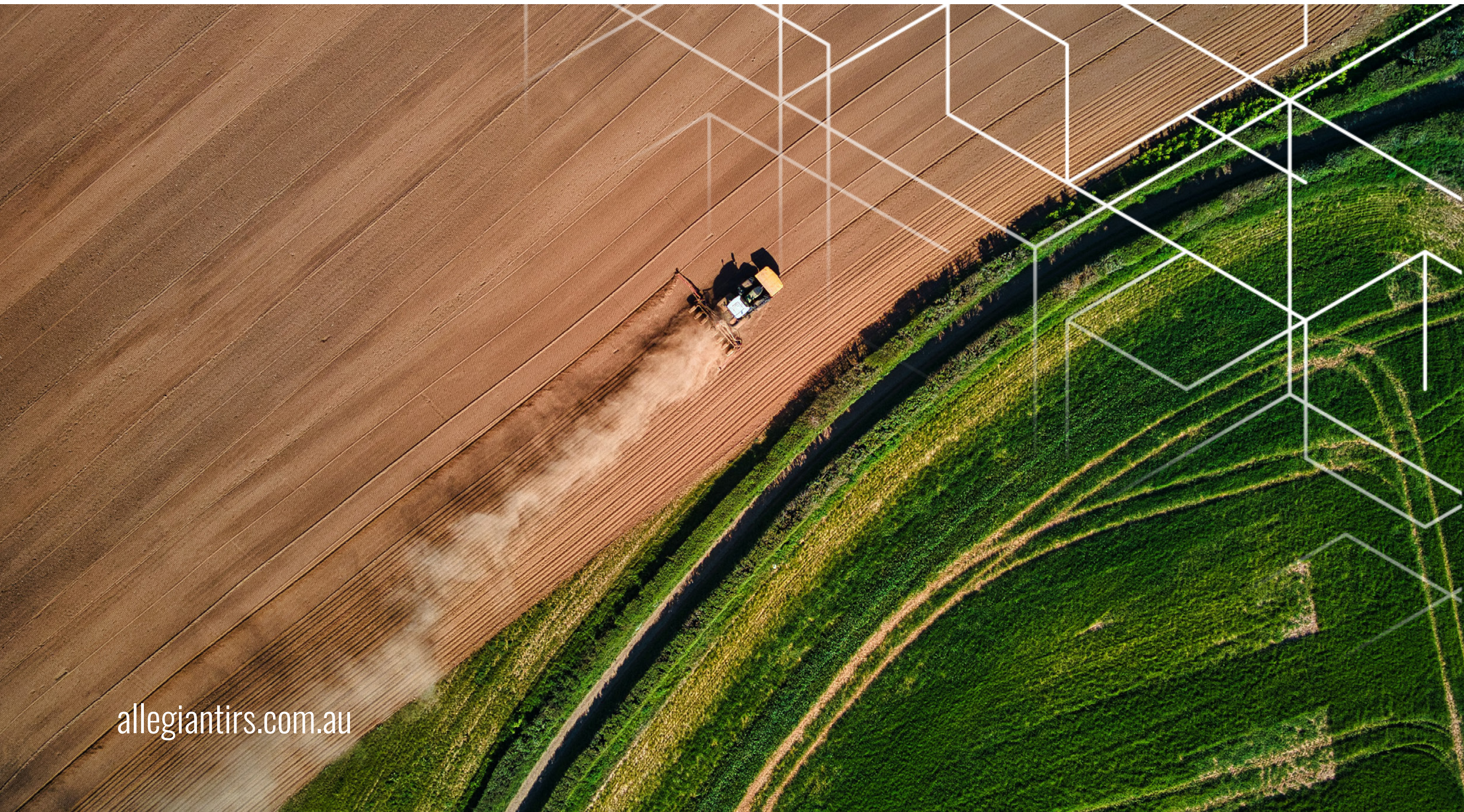
Insurance Market Trends and Outlook

Q1 2023



Looking forward, the current volatile macroeconomic environment will continue to present hurdles for the insurance market worldwide. Continued global pressure from natural catastrophe losses, high inflation and financial economic volatility are ensuring that we will continue to see further unpredictability in the rating rationales and risk acceptance of insurers.

We are in the perfect storm. Underwriting and investment pressures on global insurers are driving ongoing mitigation measures and in consequence we envisage that the hard market conditions will continue for the foreseeable future.

Macro and market components underpinning the volatile insurance market:

Macroeconomic	Insurance market
Depressed economy	Continuous hardening market
Extended and unpredictable inflationary pressures	Significant ongoing natural catastrophe events
Rising interest rates	Declining capacity and increased rates in the reinsurance markets
Ongoing financial stability risks – reduced profit margins	Reduction in shareholder equity

Inflationary pressures continue to be a major contributor to poor underwriting performances as inflation pushes up the cost of claims and expenses. In Australia, inflation was 6% for the June 2023 quarter, down from a 30-year high of 7.8% in December 2022, with Swiss Re predicting that inflation is set to continue.

While the severity of recent natural catastrophe events is one key influencer on high inflation, other contributory components are noted as:

- The pandemic;
- War in Ukraine;
- Supply shortage, rising costs of construction industry; and
- Exiting a decade of low or negative interest rates.

Property catastrophe reinsurance rates rose to an approximate 20-year high in January 2023 renewals. This is off the back off global economic average losses from natural disasters for the past five years being in excess of $100 billion, with 71% of losses in North America, 12% in Asia Pacific and 11% in Europe. Swiss Re reported in 2021 that natural catastrophe losses reached around $112 billion, making 2021 the fourth highest since 1970. In 2022, this was surpassed with global insured losses reaching $125 billion.

It is forecast that the average annual loss from these natural disasters will continue to trend upwards by 7%.

The volatility of the current economic environment is driving insurers to continuously evaluate, and carefully fine-tune their risk selection criteria and processes for assessing premium adequacy.

Australian Prudential Regulation Authority March quarter results note

In Australia the general insurance market is principally regulated by the Australian Prudential Regulation Authority (**APRA**), which monitors and reports on the general insurance performance each quarter. This reporting provides useful insights into the insurance market including its profitability and sustainability which ultimately impacts the premiums able to be offered to insureds.

Key performance statistics – December quarter 2022 v March quarter 2023

	December quarter 2022	March quarter 2023	Quarterly change
Number of insurers	89	90	1
Gross earned premium	$16.5b	$16.4b	-.04%
Net earned premium	$11.6b	$11.7b	0.6%
Gross incurred claims	$10.2b	$14.4b	40.6%
Net incurred claims	$7.6b	$9.2b	20.4%
Underwriting result	$1.6b	-0.1b	-
Investment income	$1.0b	$2.1b	106.1%
Net profit after tax	$1.3b	$1.1b	-18%

For the March quarter 2023, insurers saw a $100 million reduction in profit, representing an 18% decrease. Whilst insurers have attempted to address poor operating losses over the past few years through increased premiums and de-risking portfolios, the underwriting loss of $100 million is evident that further correction strategies will be deployed to ensure profit stabilisation.

To drive profits, insurers are starting to seek growth in their written premiums to leverage off the improved investment markets. As a result, we are seeing increased competition for those "preferred risks" as well as ongoing reduction in exposures for those insurances in high-risk industries or accounts that aren't performing profitably.

The Outlook – Major Classes

Professional Indemnity Insurance

The professional indemnity insurance sector has experienced remarkable shifts, largely due to the increasing number of lawsuits, heightened regulatory scrutiny, and evolving business practices. Industries including, but not limited to, architecture, engineering, and consulting, are facing mounting liability exposures. Consequently, the need to ensure insurance platforms are providing claim certainty is more critical than ever. To manage risks effectively, insurers are adopting stringent underwriting criteria, ongoing revision of premium adequacy, and the implementation of rigid claims procedures. Insureds are advised to conduct detailed risk assessments, stay informed about emerging liabilities, and consider ongoing risk transfer mechanisms to protect their businesses adequately.

Property Insurance

Property insurance has faced significant challenges in the wake of heightened natural catastrophes and weather related events. The increase in property damage and losses has prompted insurers to reevaluate their risk models, leading to adjustments in premium rates. Adding another layer of complexity to obtaining premium adequacy is the inflationary pressures on the cost of construction materials and demand for labour, due to shortages. Property owners must prioritise risk mitigation strategies, such as upgrading fire protection solutions, implementing disaster preparedness measures, and engaging in transparent communication with insurers to secure the most favourable terms for ongoing risk transfer solutions.

Liability Insurance

The liability insurance landscape is rapidly evolving, with changes in legal landscapes, societal attitudes, and the continued influx of cyber threats. As a result, insurers are reassessing liability policy terms and coverage limits to adapt to these new challenges. Insurance underwriting practices are focusing on insureds' operational capabilities to employ proactive risk management practices, and accurately identify key risk mitigation strategies required to maintain a robust level of risk protection. For insureds to have the flexibility in their program to meet their current and ongoing needs, they must maintain constant open dialogue with insurers to tailor liability coverage to their specific needs.

Navigating the volatility

Considering the volatile insurance market, both insurers and policyholders must adopt adaptive strategies to thrive in this ever-changing landscape. Insurers are increasingly investing in advanced technologies, such as data analytics and artificial intelligence, to enhance risk assessment capabilities. To escalate underwriting profitability, insurers are maintaining rigorous underwriting practices on stressed or high-risk insurances. It is critical for insureds to focus on proactive risk management, embracing innovative risk reduction measures and diligently reviewing accurate data to ensure the risk transfer capabilities of the insurances are in line with the risk maturity inherent within the organisation.

Conclusion

The insurance market's volatility will be with us for the foreseeable future. To successfully navigate these challenges, professionals and businesses must prioritise risk management, engage in transparent communication with insurers, and stay informed about emerging risks. By embracing proactive approaches and maintaining flexibility, stakeholders can effectively tackle uncertainties in the insurance market and secure the protection they need in the face of evolving risks.

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