

Insurance Times: Casualty Actuarial Society panelists see 2001 effects continuing
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SAN DIEGO -- Many of the events that made 2001 the worst year ever for property/casualty insurance will continue to keep the industry in a hard market throughout of this year, panelists said at the Spring Meeting of the Casualty Actuarial Society (CAS) recently held here.

Gregory J. Ciezadlo, vice president, Farmers Insurance Group, described several of the key drivers in personal lines insurance. Since 1995, auto repair costs and housing construction material costs have both exceeded the rate of inflation. Also, pricing and underwriting problems were exacerbated by the decline in the NASDAQ, Dow Jones and interest rates since March 2000.

Another influence is the increase in tort liability from asbestos, mold, aftermarket parts, lead, construction defects, catastrophes, etc. Overall average jury awards rose from \$419,000 in 1994 to \$1,168,000 in 2000, he said.

In Texas, paid losses for water damage claims alone rose from \$370 million in 1997 to over \$1 billion in 2001. Ciezadlo said,

"When you add the catastrophe losses from the September 11th attacks into the mix, you have the worst year ever in 2001 as the industry recorded an after-tax loss for the first time in history."

Ciezadlo explained the reasons cycles still occur: a lag between emerging trends and insurers' ability to react in the market; the continued reliance on investment income to offset underwriting losses; insurers' reluctance to "lead the pack;" incentives in place that are based on the past, not on the future; new and unusual events or coverage, such as tort liability crises in the '70s and '80s and mold; and catastrophes.

The industry reacts to these cycles by increasing prices, limiting new business, modifying and excluding coverages and instituting more sophisticated segmentation systems, such as insurance scoring using credit information, complex tiering plans and introduction of rating plans in homeowners focused on the individual not the property, he said.

According to Ciezadlo, the personal lines market will remain hard, due to price increases by market leaders and an uncertain investment future.

The future is even more bleak for reinsurers, according to Kenneth A. Kurtzman, senior vice president and chief pricing officer, Swiss Re Underwriters.

Reinsurers Susceptible

While the drivers of the cycle are the same (interest rates, loss trends, catastrophe losses, etc.) Kurtzman said that "reinsurers are more susceptible to each of these than primary companies, basically due to the flow of information -- reinsurance companies only know that primary companies tell them."

Kurtzman showed that since 1975, a direct market cycle comparison reveals that the principal driver of a reinsurance company's profitability is the primary company's profitability.

Kurtzman also told the group that many changes have taken place in the reinsurance marketplace, including the addition of about \$20 billion in new capital (\$9.1 billion from new and existing Bermuda companies, \$5.2 billion from U.S. reinsurers and \$5.7 billion from those outside North America) as well as exits from the marketplace such as the run-off of Scandinavian Re and Overseas Partners, spin-off of St. Paul Re and Zurich Re and the exit from international reinsurance by CNA Re and Hart Re.

Kurtzman observed that the industry is mid-way through this hard market and that he has "every expectation it will be at its peak through 2003."

Jeffrey H. Post, president and chief executive officer, Fireman's Fund, reviewed the specific causes for hard markets in recent years -- the stock market decline of the mid-70's; the liability crisis and emerging

environmental and asbestos (E&A) issues in the mid-80's; and Hurricane Andrew and the property capacity crisis in the early 90's.

He cited several reasons for the current hard market: balance sheet shortfalls (E&A reserve shortfall, non-E&A reserve shortfall, 9/11 disclosure, potential reinsurer insolvencies and aggregate excess of loss hangover) and income statement issues (realized gains, fixed income yields, terrorism exposure, underwriting results).

Post said that the industry is "undisciplined" with "consistent financial underperformance." He said that this provides challenges to actuaries to act with integrity and honesty -- and the need for actuaries to educate their underwriting and marketing people.

Since actuaries are trained in statistics, they have become the "financial conscience of an insurance company," according to Post.

The panel was moderated by Wayne H. Fisher, executive vice president and risk officer, Zurich North America.

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