ISO chief warns insurers on hard market's return

Citing evidence the U.S. property/casualty insurance industry's hard market may be coming to a close, an industry leader is warning insurers not to sow the seeds of their own destruction by abandoning sound underwriting and pricing that led to recent improved results.

"The firming in insurance markets that benefited results through six months is in danger of becoming a thing of the past," said ISO chairman, president and CEO Frank J. Coyne.

In his keynote address to insurance executives attending the 7th Annual ISOTech Conference, Coyne said ISO's analysis of rate changes on renewal for commercial policies shows "rate increases versus year-ago levels peaked at 12.9 percent in July 2002 and have been on a downward slide ever since."

A third-quarter survey by the Council of Agents and Brokers shows "about a third of large- and small-account premiums were flat or down as much as 10 percent, while the same was true for 28 percent of medium-sized accounts."

"If the next soft market is not already upon us, the hard market certainly is coming to a close," said Coyne.

That hard market resulted in significant strengthening, with written premium at first-half 2003 up 11 percent over the year-ago period, while the industry's first-half annualized return on net worth bounced back to 9.7 percent from a low of 1.8 percent in 2001, said ISO's chief executive officer.

"We project the industry's combined ratio (the measure of losses and other underwriting expenses per dollar of premium) for 2004 will improve to 101.0 percent, nearly 15 points better than the 115.9 percent combined ratio for 2001. But we also project premium growth will slow significantly from 14.3 percent in 2002 to 6.1 percent for 2004," Coyne said.

"With each improvement in profitability, the property/casualty industry has a history of reverting to hyper competition for market share," said Coyne, citing the industry's strong recovery in the mid-1980s "when a period of sustained profitability seemed possible — at least to some. But once again a hard market had sown the seeds of its own destruction, and the industry slipped into the most protracted soft market in history."

"Insurers have paid dearly for failing to adhere to disciplined underwriting and cost-based pricing," Coyne reminded the 750 insurance executives in attendance.

"As insurance markets lurched from hard to soft and back again, commercial policyholders have increasingly turned to alternative mechanisms (captives, pools and risk-retention groups)," said Coyne. Alternative mechanisms' share of the U.S. commercial insurance market has grown from about a quarter in 1985 to nearly 50 percent today.

Insolvencies are also increasing, he said. In the first three years of this decade, an average of 33 property/casualty insurers failed each year, compared with 12 per year in the 1970s and 27 per year in the 1980s and 1990s, said Coyne.

Despite the industry's history, insurers can achieve sustained profitability through sound risk assessment, underwriting and cost-based pricing but "not slavish devotion to growth and naïve reliance on investment gains from fickle financial markets," said Coyne.

"The most nimble and farsighted will survive and thrive if they execute against core fundamentals." ❒