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2013 EXPECTED TO BE A BETTER YEAR FOR THE INSURANCE INDUSTRY HOWEVER PREMIUM RATE INCREASES TO CONTINUE

Sydney, 31 January, 2013 – Australian insurers reported improved operational results in 2012 on the back of lower levels of catastrophe activity however consumers and businesses could continue to see premium increases as the low interest rate environment impacts investment returns used to support claims, according to the *2012 J.P. Morgan Taylor Fry General Insurance Barometer* released today.

The joint report, covering the 2012 financial year, reveals an overall improvement in combined ratios[1] in commercial and domestic insurance lines, particularly property classes.

"The 2012 year was better for the insurance industry (despite the adverse impact of interest rate movements), primarily due to lower levels of catastrophe activity than 2011," said Siddharth Parameswaran, J.P. Morgan senior insurance analyst.

For straight domestic insurance lines, the combined ratio was 89%, improving from 98% in 2011. In the commercial classes the combined ratio was 98%, an improvement from 2011 where the industry made underwriting losses.

"The 2013 outlook for the Australian economy appears more robust than international markets so this should once again mean relatively greater growth prospects for Australian insurers. However the big concern for insurers comes from low yields on fixed interest investments that insurance companies in Australia typically hold backing their liabilities. For long tail products, where claims generally take longer to settle, in particular this can make substantial differences to returns in the absence of adequate premium rate increases," Mr Parameswaran added. "The flood experience of the last few days in Queensland and Northern NSW, coupled with some of the bush fire losses may temper reported trends however."

"Looking forward, the industry forecasts combined ratios in domestic insurance lines to improve 87% in 2013, driven by improvement in householders and motor insurance," said Evelyn Chow, Taylor Fry actuary, however noting those estimates were given before the impact of the floods and bushfires which could well temper that expectation.

"Similarly, in commercial insurance the industry is forecasting an improvement in combined ratios to 94% in 2013," she added.

Two classes of concern for 2013 and onwards include NSW CTP, where regulatory and government pressures have constrained premium rate increases despite claims and investment yield pressure, and public liability insurance.

[1] Combined ratios are claims costs incurred net of reinsurance + all other expenses/net earned premium

Industry actual and forecast combined ratios – 2010-2014

	2010A	2011A	2012A	2013F	2014F
Domestic classes					
Domestic motor	90	93	95	93	95
Householders	96	107	83	78	79
CTP (NSW)	105	106	92	101	101
CTP (QLD)	103	70	87	92	94
Weighted average sub total	*95*	*98*	*89*	*87*	*89*
Commercial classes					
Fire & ISR (Commercial property)	98	134	90	83	87
Commercial motor	92	91	99	97	95
Public & Product Liability	80	86	110	107	113
Workers compensation (WA only)	91	94	92	95	95
Workers compensation (TAS, NT & ACT)	89	104	103	96	95
Professional indemnity	101	98	92	90	90
Directors & officers	91	85	102	100	100
Weighted average sub total	*92*	*106*	*98*	*94*	*95*

Source: 2012 J.P. Morgan Taylor Fry Barometer and J.P. Morgan Deloitte General Insurance Surveys (2010-2011)

Premium rates trends

The Barometer revealed a two-speed market on premium rates which is expected to continue in 2013, with rate increases in domestic insurance ahead of movements in commercial insurance and soft trends in long-tail products, where claims generally take longer to settle, reported across the board. Some of those increases are driven by increased coverage being provided by the industry in the form of flood coverage that was not widely available previously.

The industry in 2012 had shown strong rate increases in domestic insurance of more than 9% driven predominantly by the home insurance category, while showing slightly lower increases in commercial insurance of more than 5%.

"For 2013, the industry is forecasting similar increases in domestic insurance classes, driven by home insurance once again (due in part to expanding coverage). In commercial insurance classes, the industry is once again expecting an increase in premium rates," Mr Parameswaran said.

Ms Chow from Taylor Fry added: "The biggest concern in commercial insurance centres around the longer tail products, where claims generally take longer to settle and rates have not been rising in any significant way for sometime, but where investment yield reductions are posing a threat to profitability. Substantial capacity, particularly from overseas appears to be stalling prospects for insurers to make up for sharply declining profitability in those lines."

Historical premium rate movements and expected rate movements – 2010-2014

(%)	2010A	2011A	2012A	2013F	2014F
Domestic classes					
Domestic motor	4	2	3	4	3
Householders	11	10	15	12	5
CTP (NSW)	10	8	4	6	5
CTP (QLD)	13	-6	2	7	4
Weighted average	8	5	9	8	5
Commercial classes					
Fire & ISR (Commercial property)	-1	7	9	7	6
Commercial motor	4	4	6	4	5
Public & Product Liability	-3	-1	1	3	3
Workers compensation (WA only)	-1	-4	4	4	2
Workers compensation (TAS, NT & ACT)	0	2	8	6	5
Professional indemnity	-4	1	1	3	4
Directors & officers	-2	0	2	4	4
Weighted average	-1	3	5	5	5

Source: 2012 J.P. Morgan Taylor Fry Barometer and J.P. Morgan Deloitte General Insurance Surveys (2010-2011)

Claims trends

Catastrophe claims on a global basis reduced to below trend in 2012 and gross insurance losses in Australia fell significantly compared to 2011.

"In Australia, weather changes can be a significant driver of catastrophe costs. Overall, 2012 estimates for catastrophes were less than what the industry perhaps forecasted at the start of the year," Mr Parameswaran said. "That seems set to reverse in 2013 based on the early experience to date".

"Claims trends in property and short tail products, where claims are generally paid shortly after the incident or loss occurs, improved significantly in 2012, driven by lower catastrophe activity," he added.

Issues confronting underwriters & brokers

The Barometer found 67% of respondents stated regulatory changes and compliance are the major concern for underwriters reflecting changes under the new APRA capital adequacy framework which came into effect on 1 January 2013.

This was closely followed by the impact of low interest rates on profit trends (58% of respondents) and increased market competition (50% of respondents) as key concerns particularly in commercial insurance.

For brokers, all participants raised the issue of attracting and retaining quality staff as a key issue, followed by the issue of excess competition and capacity in the market.

Issues confronting reinsurers

Respondents reported some structural changes in the reinsurance market as a result of the changing supply and demand for reinsurance. Reinsurers indicated a lack of appetite to cover catastrophe losses in Property Proportional which was the cause of the deterioration in 2012.

The most important issue unanimously identified by reinsurers was around regulation and regulatory changes. A majority of participants also raised concerns about the abundance of reinsurance capacity in the market from both existing and new entrants now becoming an over-arching issue across the reinsurance classes.

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About the survey

This is the first edition of the *J.P. Morgan Taylor Fry General Insurance Barometer*. The publication builds on data from nineteen editions of the J.P. Morgan Deloitte General Insurance Survey. The Barometer provides a detailed overview of the current state of the Australian general insurance industry and the industry's expectations.

The report conveys analyses on the key elements of the industry from the perspective of direct underwriters, reinsurers and brokers, including: detailed product information for the current period and industry expectations for the next two years covering issues such as premium rate trends, capacity changes, claims trends, loss and expense ratios; perceptions of product profitability; distribution trends; practitioner views on key issues affecting the industry and particular classes; and brokers' perceptions of underwriters.

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About Taylor-Fry

Taylor Fry is an independent, market-leading consultancy specialising in the provision of actuarial, financial modelling, statistical and related policy advice to the general insurance industry, corporations and governments. We are currently made up of 24 fully qualified actuaries and 15 actuarial analysts with offices in Sydney and Melbourne. Taylor Fry's consultants have deep experience in the general insurance industry and our expertise is well-sought after both in Australia and overseas. We offer high quality, custom-built solutions, that are clear, understandable and practical. Information about Taylor Fry is available at www.taylorfry.com.au.

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