



Institute of Actuaries of Australia

# XVth GENERAL INSURANCE SEMINAR

*Evolution of the Industry*

## State of the Market.

# What comes after the dizzying heights?

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## The Journey....

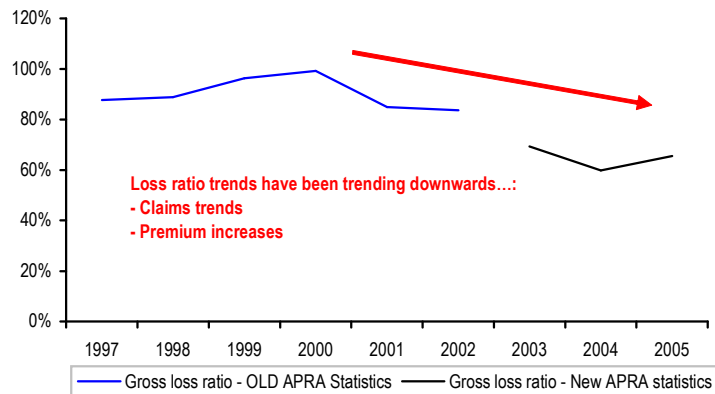
- **Recent Past: The Collapse... and Climb**
- **What Changed Profitability?**
- **Where To From The Heights?**



# The Recent Past – Collapse and Climb

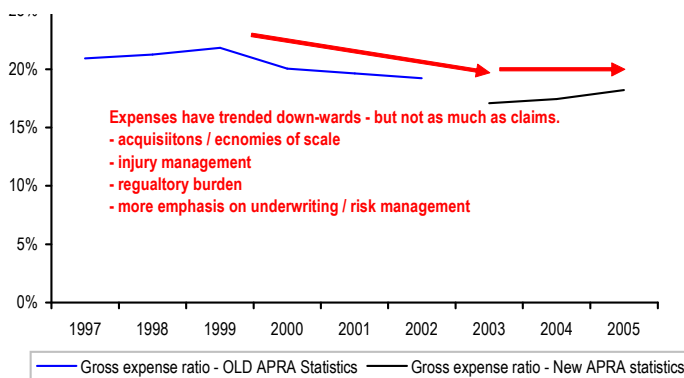
## APRA data

### Claims



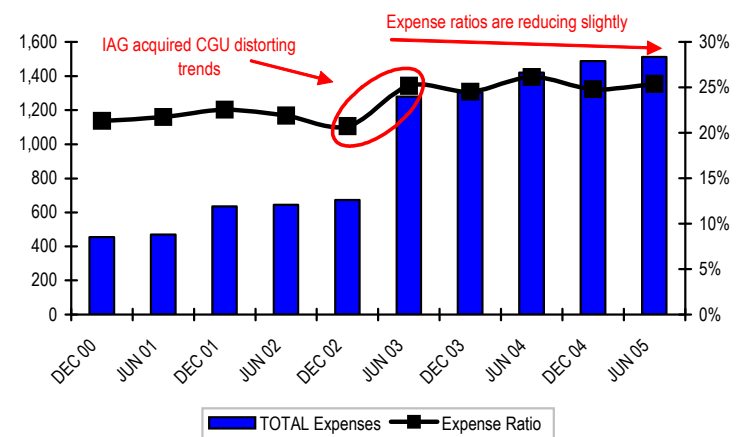
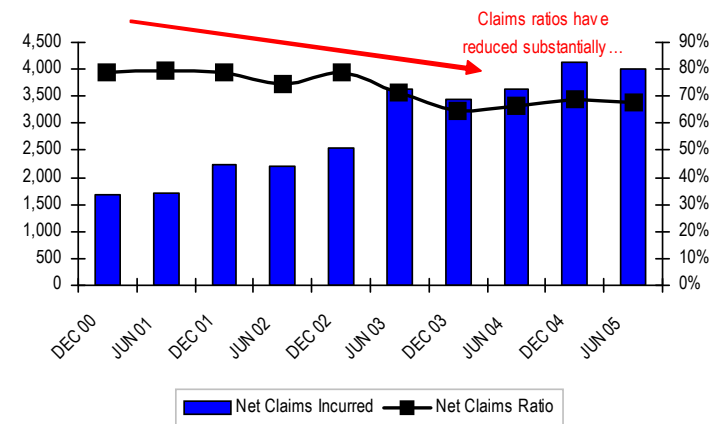
\*2003 and 2005 only include 3 quarters of data as APRA have not published statistics for all relevant periods. In 2003, \*\*APRA changed their method of collecting statistics in 2003 - no longer based on accounting results, but rather statutory results. As such there is a discontinuity. Gross claims statistics appear to be comparable.

### Expenses



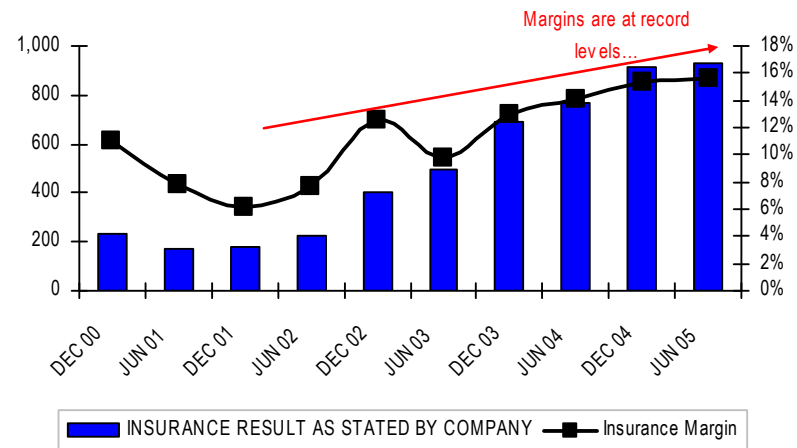
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## Listed Company Data





# What Changed Profitability?



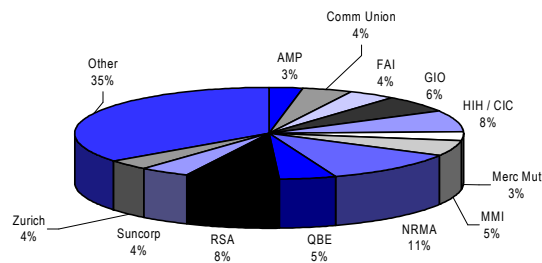
*Listed sector – Australian GWP only*

- 1. Industry Rationalisation**
- 2. HIH**
- 3. APRA Prudential Reforms**
- 4. Claims Trends**



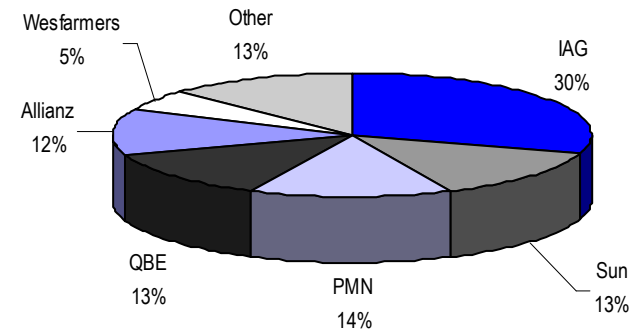
# Change: 1. Rationalisation

**1997: GWP \$13.7bn.  
Very Segmented.  
Top 5: 38% of premium.**

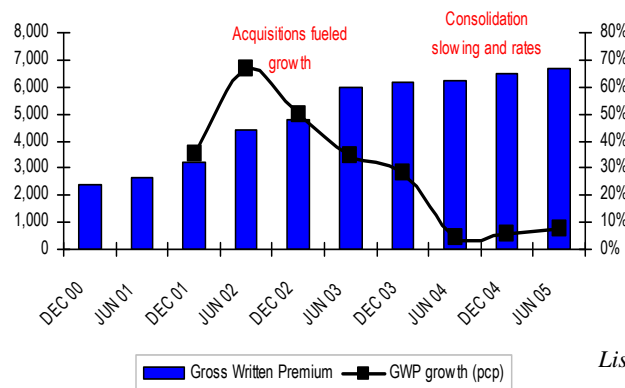


Sources: APRA Selected Statistics on the General Insurance Industry 1997, Merrill Lynch Estimates

**2005: GWP \$25.8bn. Concentrated, with top 5 accounting for 82% of premium.**



Sources: APRA, Investor Presentations listed companies, Merrill Lynch estimates



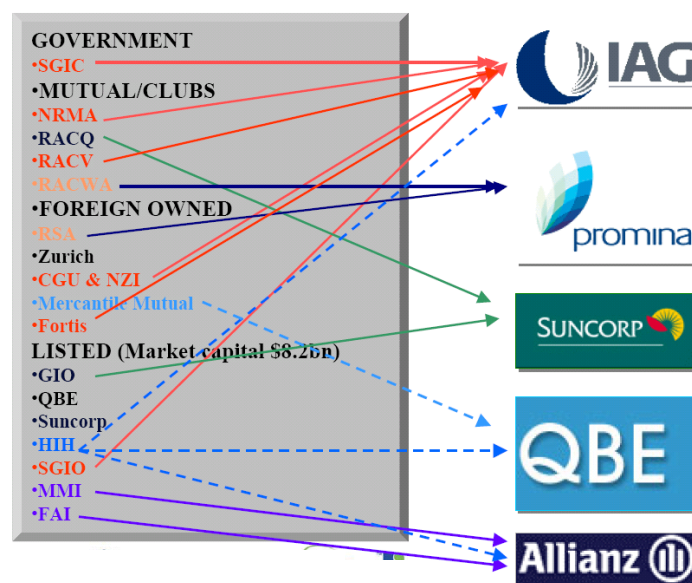
Listed sector – Australian GWP only



# Change: 1. Rationalisation cont'd...

1997

2005



Part of slide is courtesy of IAG presentation to investors, 29 Sep 2005

## •Effect

•Competition ↓

•Scale ↑

•Rationality ↑



## Change: 2. Collapse of HIH

### •HIH 2001 Corporate Collapse



#### •Reasons:

- Mis-pricing / under-reserving
- Corporate mis-adventures
- Lack of profit focus

#### •Results

- Capacity Reduced (2001)
- Liability Crisis – premium increases
- Increased focus - underwriting profits



## **Change: 3. APRA**

- **Prudential Reforms July 2002**
  - **Risk Based Capital Standards**
  - **Corporate Governance**
  - **Licence Re-authorisation**
- **Effect**
  - **Increased focus on return on capital**
  - **Sensible investment strategies**
  - **Better corporate governance**





# Change: 4. Claims Environment

<b>TORT REFORMS</b>	<b>CTP</b> <ul style="list-style-type: none"><li>•NSW 1999 Reforms</li><li>•QLD 2000, 2003</li></ul>	<b>Liability</b> <ul style="list-style-type: none"><li>•State Based Civil Liability Reforms</li></ul>	<b>Workers' Compensation</b> <ul style="list-style-type: none"><li>•WA 1999 Second Gateway changes</li></ul>	
<b>POLICY TERMS</b>		<b>Liability:</b> <ul style="list-style-type: none"><li>•Deductibles, exclusions</li></ul>		
<b>ECONOMIC ENVIRONMENT</b>		<b>Long-Tail:</b> <ul style="list-style-type: none"><li>•Workers, CTP, Liability</li></ul>	<b>Short-Tail:</b> <ul style="list-style-type: none"><li>•Motor, Householders</li></ul>	
<b>WEATHER</b>			<b>Short-Tail:</b> <ul style="list-style-type: none"><li>•Motor,</li></ul>	
<b>CLAIMS MANAGEMENT</b>		<b>Long-Tail:</b> <ul style="list-style-type: none"><li>•Workers</li></ul>	<b>Short-Tail:</b> <ul style="list-style-type: none"><li>•Motor (Motor vehicle repair models)</li></ul>	



# Where to from the heights?

- 1. Is the “cycle” dead?**
- 2. APRA Stage II Reforms**
- 3. Claims: Fair compensation & pricing**
- 4. Listed Valuation Implications**



# 1. Is the Insurance “Cycle” Dead?

**Arguments  
for and  
Against:**

<b>Cycle being dead</b>	<b>Cycle continuing</b>
<i>More rational industry?</i>	<i>Global industry/ global capital flows - particularly commercial lines</i>
<i>Consolidation</i>	<i>ROE target overseas less than Aus</i>
<i>Barriers to entry are higher</i>	<i>Claims trends as good as they have ever been</i>
<i>More regulation</i>	<i>Economy could turn</i>
	<i>Judicial / tort pressures will build</i>



# 1. Is the Insurance “Cycle” Dead?

**Evidence so far:**

- Prices:

	2004 movements	2005 to date
<b>Commercial</b>		
Property	(around 10% decline)	(5-10% decline)
Liability	-	(5-10% decline)
Professional Indemnity	-	(3%)
<b>Statutory Classes</b>		
CTP - NSW	(3%)	(5%)
CTP - QLD	(10%)	(5%)
Workers	(6%)	flat
<b>Personal Lines</b>		
Motor	4%	(flat to -3%)
Householders	5%	5-10%

Merrill Lynch Survey on Rate Movements, ML Estimates, ACCC for Liability and PI, IAG 2005 investor report, MAIC, MAA

- Structure:

- Australia is seen as attractive by many overseas- commercial
- BUT Katrina



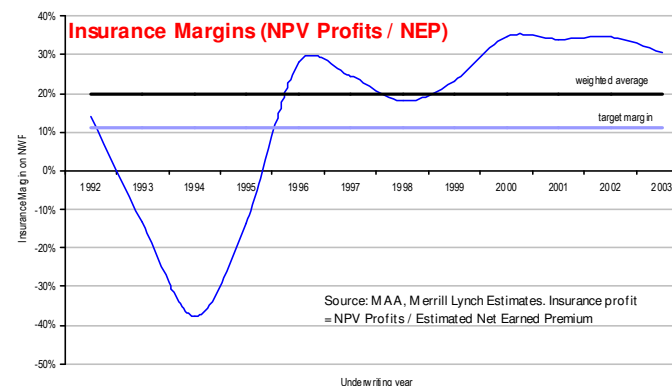
## 2. APRA Reforms: Stage II etc.

- **Changes:**
  - **Financial Condition Report / Approved Actuary**
  - **Risk Management**
  - **Group-wide regulation**
- **Effect:**
  - **framework to ensure rational industry**



## 3. Adequate Claimant Compensation

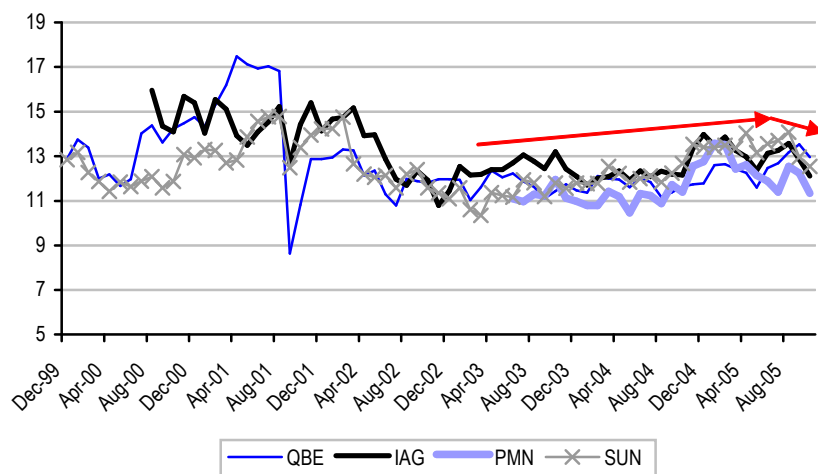
- **Tort / Legislative Reforms of long tail classes**
  - Major reduction in claims costs – all except PI
  - Likely windfall profits for insurers
- **Pressures for change**
  - **Government**
    - NSW Review CTP and Liability
    - ACCC
    - Long Term Care
  - **Regulator – “Fair” profit**
    - All statutory classes, CTP in particular
  - **Legal Profession**



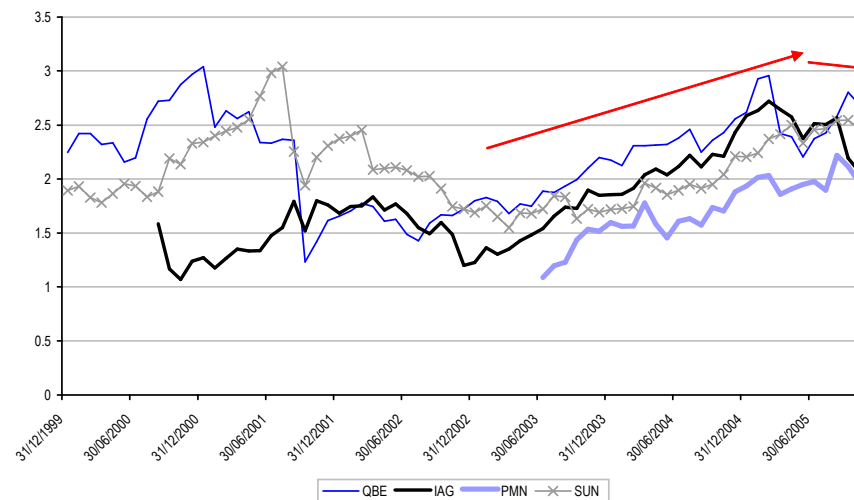


## 4. Shareholder Expectations

### Price to Earnings



### Price to Book



**Market is expecting good / rational times to continue... But with slower growth**