RADAR 2019

Our class-by-class insights for insurers

FY2019

WELCOME

Welcome to Taylor Fry's RADAR, our take on the most important trends and happenings affecting insurers today.

On the following pages, we draw on the latest APRA data, combined with our knowledge and decades of experience inside the industry.

Across three years of results, our analyses break down each line of business to help insurers benchmark their performance, and assess strategies and goals.

We also summarise investments and solvency over the same period to give you an overview of how the market is tracking more broadly.

By highlighting the changes, challenges and opportunities in insurance, we offer you a clear picture of the industry, where it's headed and your place within it.

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DOMESTIC MOTOR

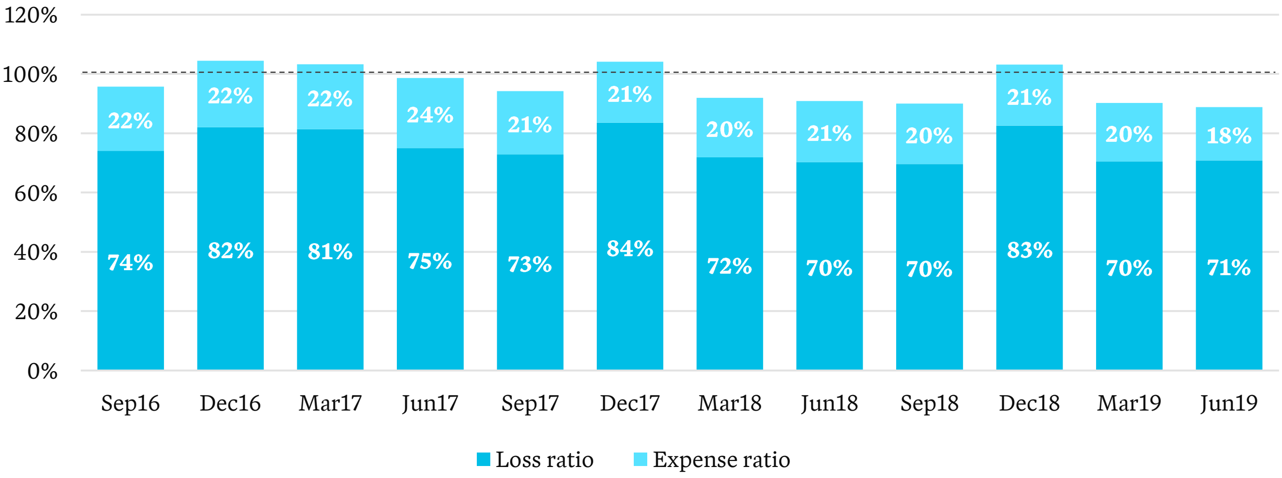
Claims costs are being driven up by the increasing cost of repairs on new technology, though claim frequency is flat. Premium increases are broadly in line with claims inflation, resulting in a stable profit outlook. Weather-event claims continue to be a key factor, with a large hailstorm in Sydney in December 2018 having a material negative impact on insurer profits for the relevant quarter, but loss ratios have stabilised since.

The increasing cost of car repairs is driven by new advanced driver-assistance systems (ADAS), which are expected to be in 40% of vehicles by 2020. Despite the proposed increase in safety these features add, insurers are yet to benefit from noticeable decreases in claim frequency.

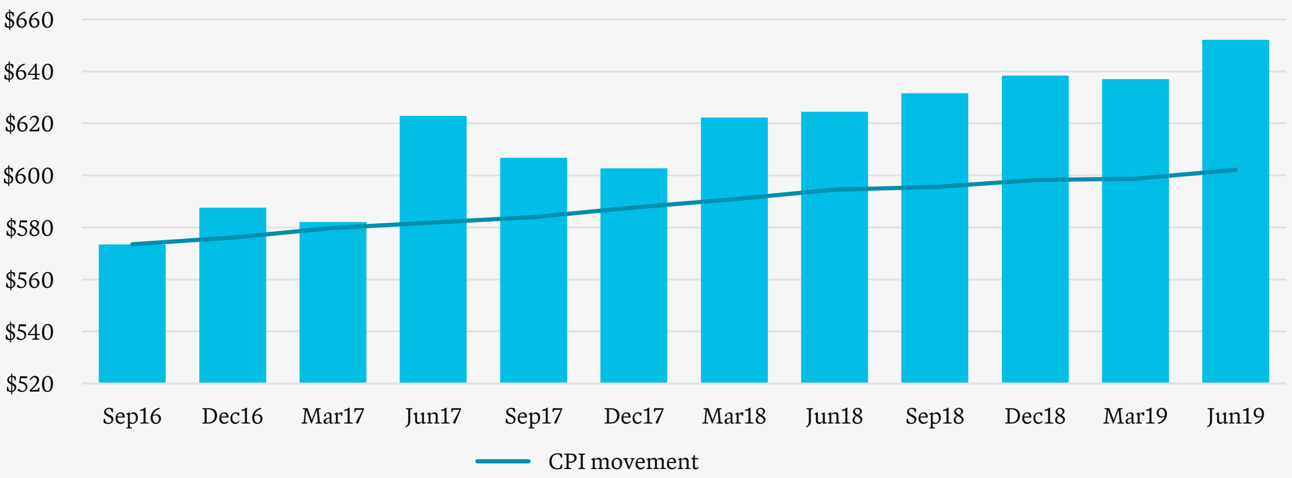
There has been increased regulatory focus on consumer outcomes for purchasers of personal lines products in the aftermath of the royal commission. This may prompt insurers to review their pricing strategies, particularly regarding new versus renewing customers.

Some insurers are already including comparative pricing information in anticipation of it being a requirement in the upcoming General Insurance Code of Practice. This may have a negative impact on renewal rates, with consumers more likely to shop around once they have greater visibility over premium changes.

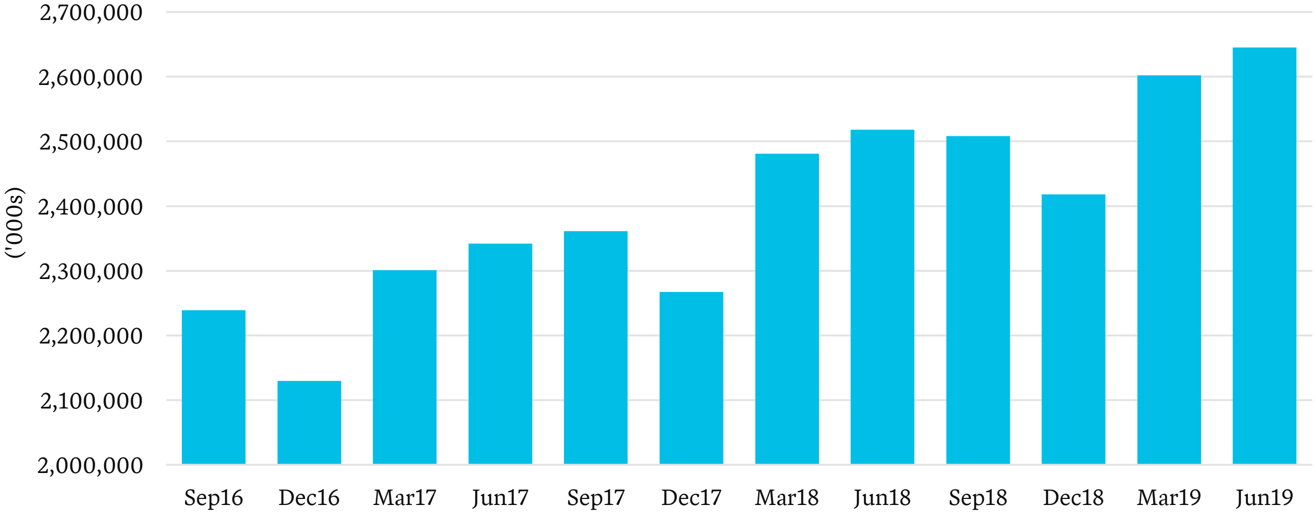
Combined ratio
Reporting quarter



Average premium
Reporting quarter



Total premium volume ($)
Reporting quarter



HOUSEHOLDER

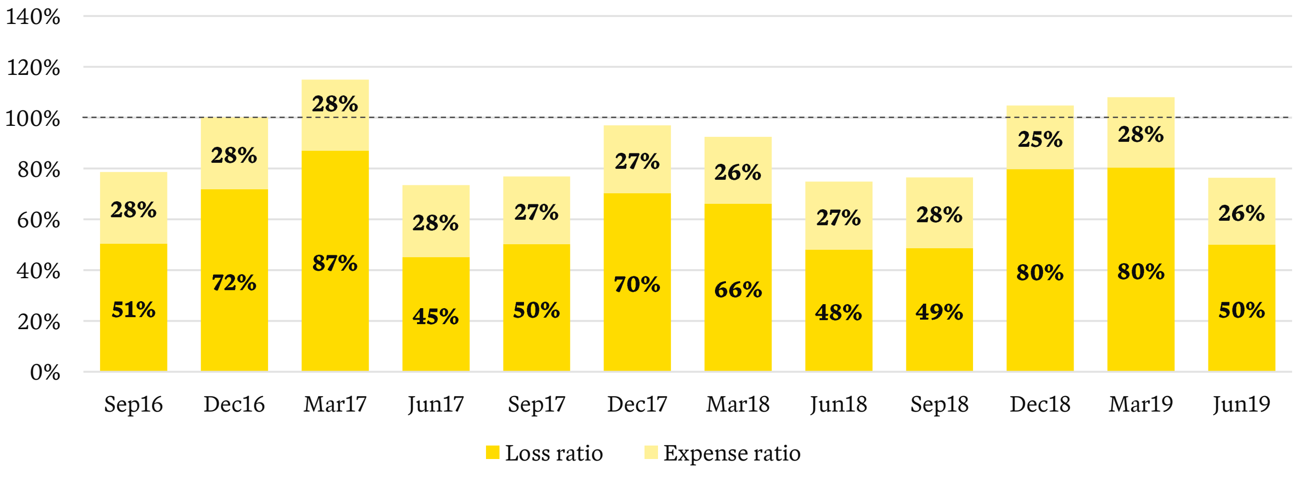
The industry remained profitable in the year to June. This was despite the adverse impact of the Sydney hailstorms and Townsville floods, which pushed up loss ratios in NSW and Queensland in the December 2018 and March 2019 quarters.

➘
Affordability, underinsurance and non-insurance continue to remain an issue, often resulting in instances of consumer hardship, which received particular focus in the aftermath of catastrophic events. However, prudent risk management and more granular approaches to pricing assisted insurers in maintaining profitability.

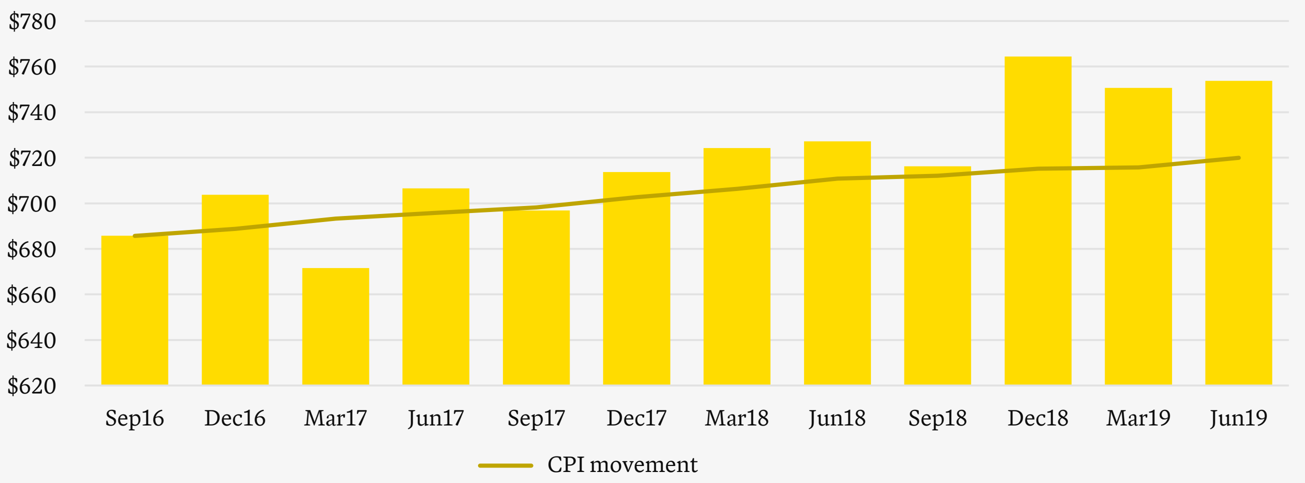
➘
The ACCC released an updated report on the Northern Australia Insurance Inquiry in July. Although it included several new recommendations, which aim to improve the efficiency of the householders market in northern Australia, insurers were disappointed to see little focus on weather-event risk mitigation.

➘
Flood exclusions may be challenged if proposed changes to unfair contract terms are adopted. This may result in insurers removing customer choice to opt out of flood cover and requiring large premium increases for policyholders in high flood-risk areas.

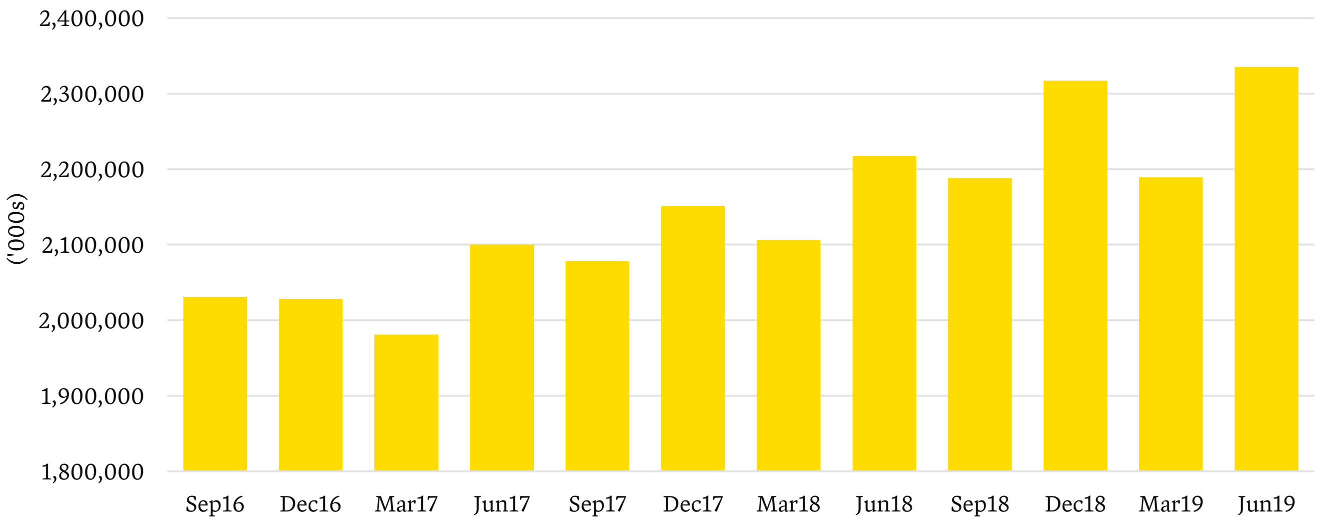
Combined ratio
Reporting quarter



Average premium
Reporting quarter



Total premium volume ($)
Reporting quarter



COMPULSORY THIRD PARTY

The combined ratios for all jurisdictions together have been increasing over the past three years, although they remain below 100%. The increase in gross loss ratio over the latest half year was most marked for NSW, but it is still tracking lower than the other jurisdictions.

➘

NSW CTP claim numbers for the 2017 scheme are lower than expected, but the proportion of minor injury claims has been higher than anticipated. The regulator is currently reviewing the definition of minor injuries. Further, while much of the estimated cost of the new scheme is associated with awards for damages through common law, it is too early to gauge the volume of these claims.

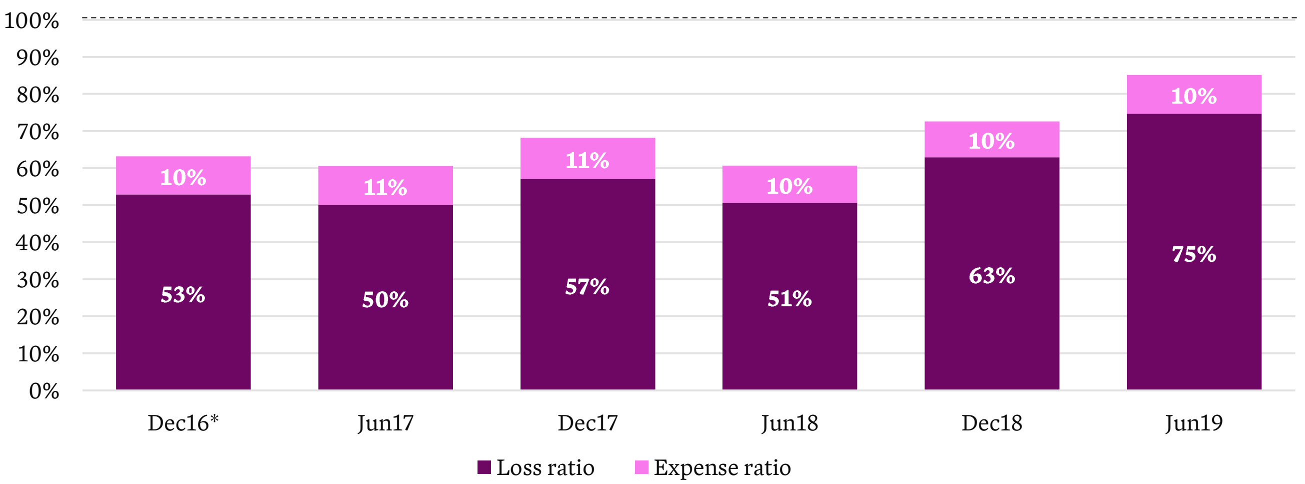
➘

Insurer profits in the Queensland CTP scheme are falling, as the regulator's steps to reduce the width of the premium bands and reduce margins in the ceiling that allow for future superimposed inflation take effect. The Government is also introducing legislation later this year to address 'claim farming' in the scheme.

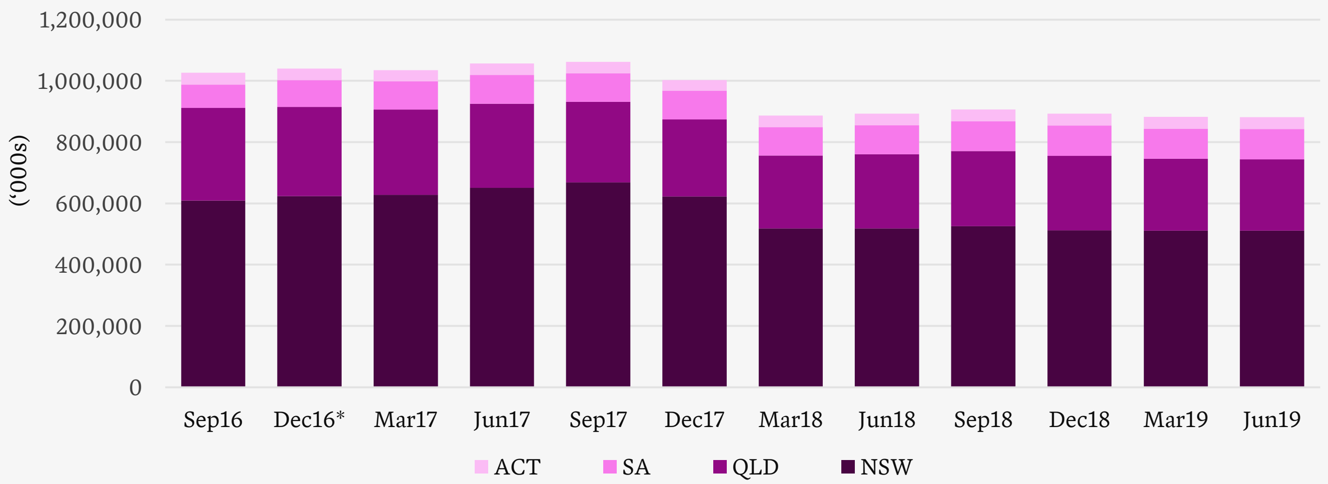
➘

Within weeks of the SA CTP market becoming competitive (1 July 2019), all participating insurers were selling Class 1 policies at the lowest price permitted by the regulator. It is almost certain scheme design caused insurers to compete aggressively, but it will be some time before the impact on profitability is known.

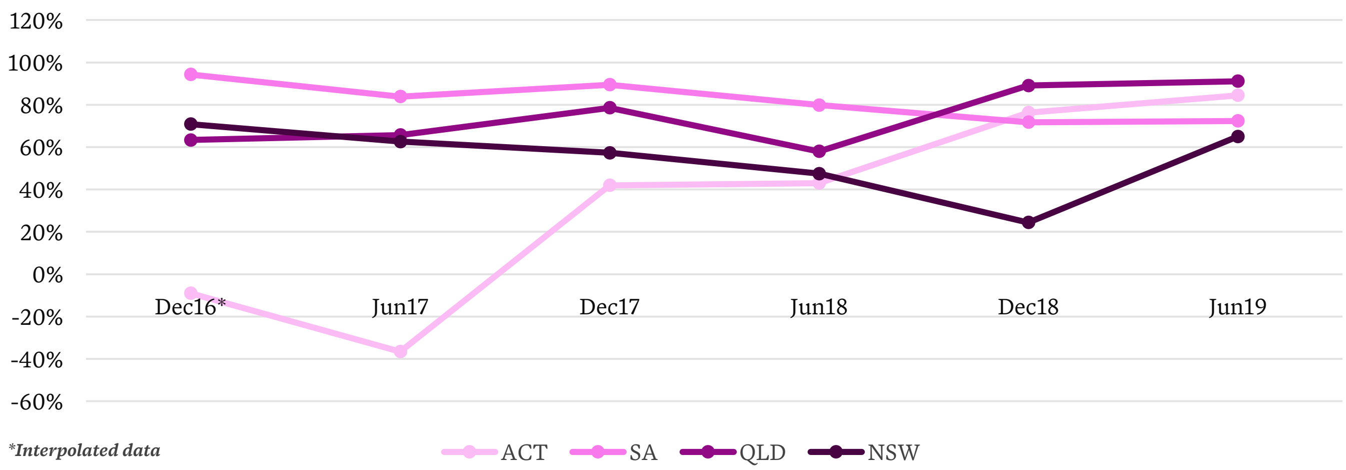
Combined ratio
Reporting half year



Gross earned premium
Reporting quarter



Gross loss ratio
Reporting half year



**Interpolated data*

WORKERS COMPENSATION

Claim frequency has continued to reduce, but many jurisdictions experienced increases in claim duration, which was partly influenced by tighter economic conditions. Low wage growth is being reflected in the premium pool, increasing competition among insurers who seek to meet top-line growth targets.

↘

Combined ratios for all jurisdictions together have exceeded 100% over the past year, with ACT and NT experiencing gross loss ratios in excess of 100% over the last reporting quarter. For WA, despite continued claim frequency reductions over recent years, reported gross loss ratios have trended upwards. This has culminated in the highest half-year loss ratio for three years.

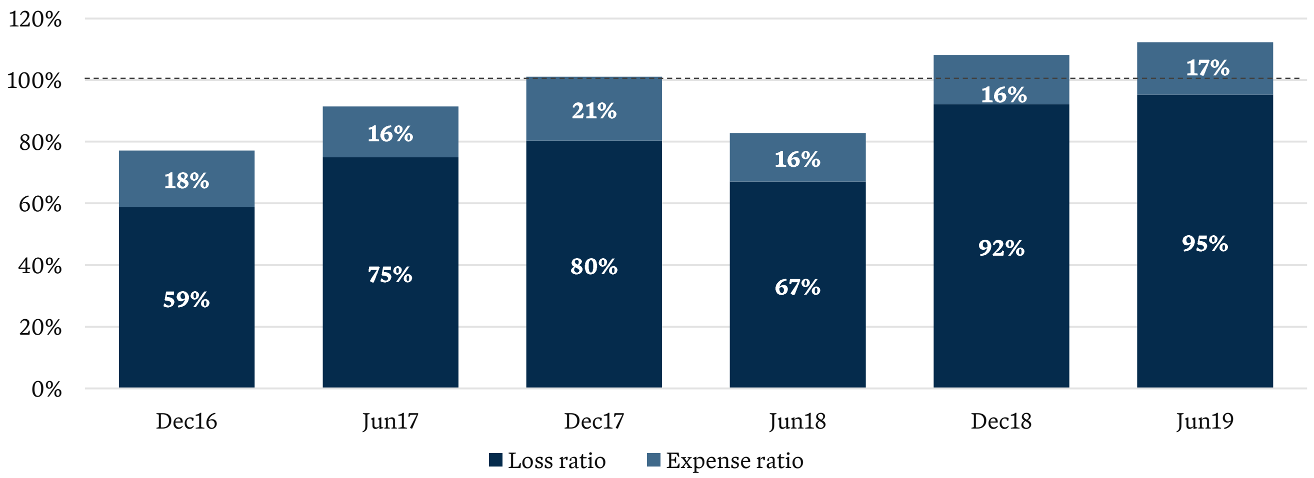
↘

Competition among insurers in the privately underwritten jurisdictions has led to some insurer premium rates being lower than those recommended by scheme regulators, increasing the risk of underpricing.

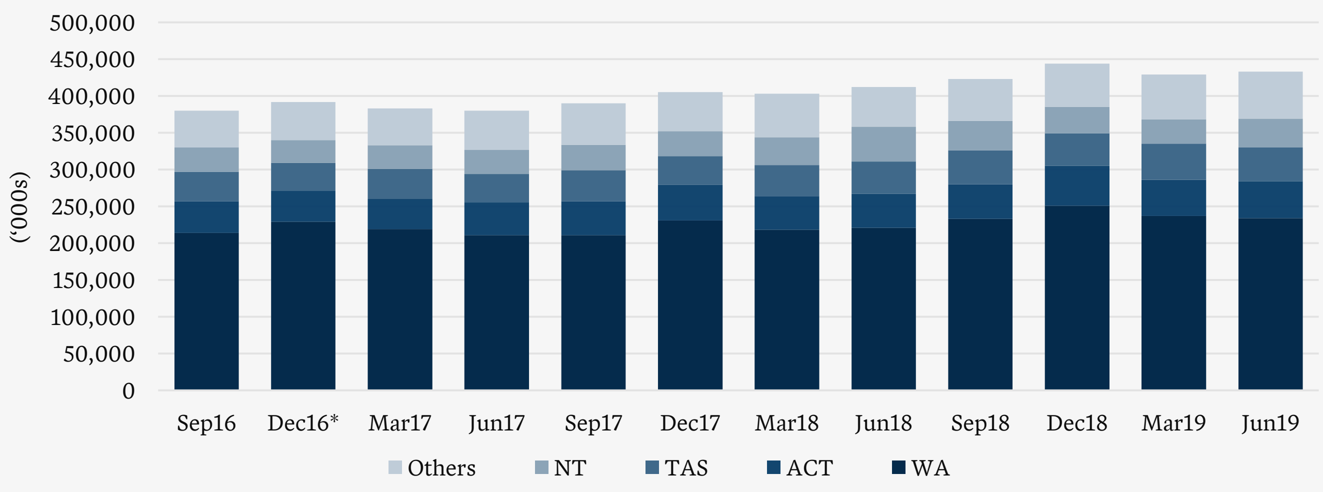
↘

Silicosis – an industrial disease caused by exposure to airborne crystalline silica dust – has been receiving public attention for being diagnosed among stonemasons, attributed mainly to the dry cutting of artificial stone used for benchtops. While recent publicity has related mainly to new silicosis cases in Queensland and Victoria, it seems likely that risk factors for silicosis are similar around Australia.

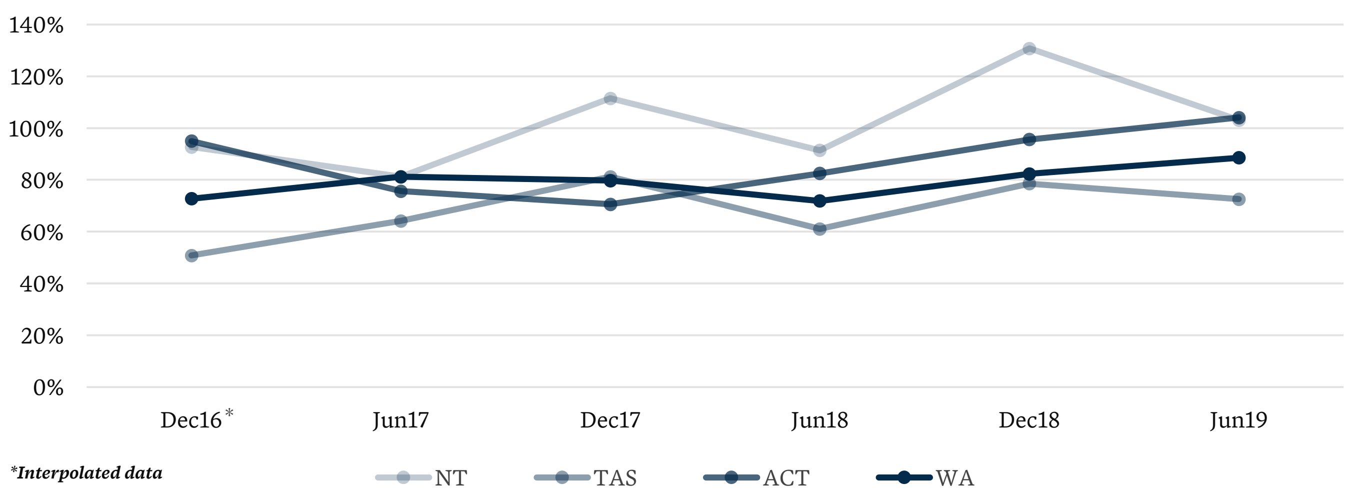
Combined ratio
Reporting half year



Gross earned premium
Reporting quarter



Gross loss ratio
Reporting half year



**Interpolated data*

COMMERCIAL MOTOR

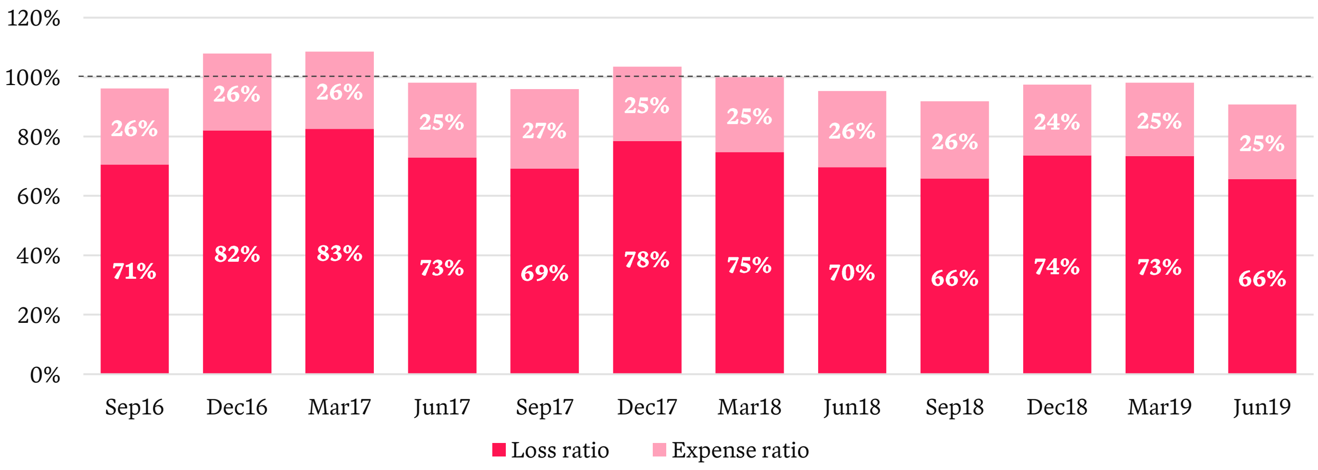
Market conditions for insurers of commercial classes have been enhanced over the past year by an easing of the downwards pressure on premium. The resulting increases in commercial motor rates were well in excess of claims inflation. This contributed to improved profitability, with the net underwriting combined ratios for FY2019 the lowest since FY2014.

➘ Although claims inflation is currently benign, there is some concern over future inflationary impacts associated with the cost of repairs on high technology vehicles.

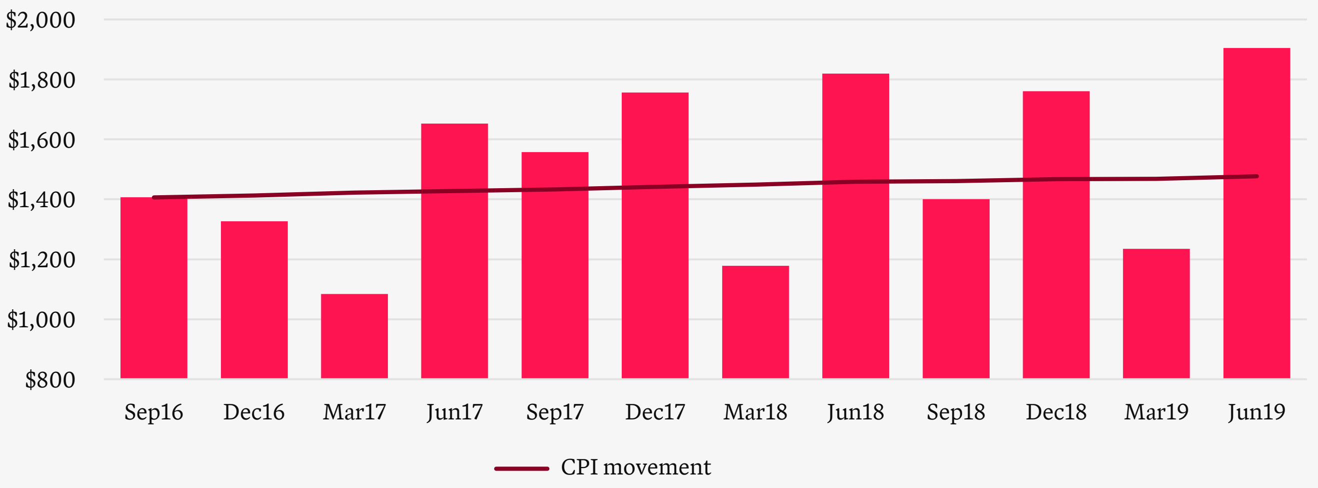
➘ The cost of imported parts is linked to the AUD exchange rate, which weakened considerably during FY2019.

➘ There may be potential impacts on distribution arrangements through changes to commission structures following the royal commission.

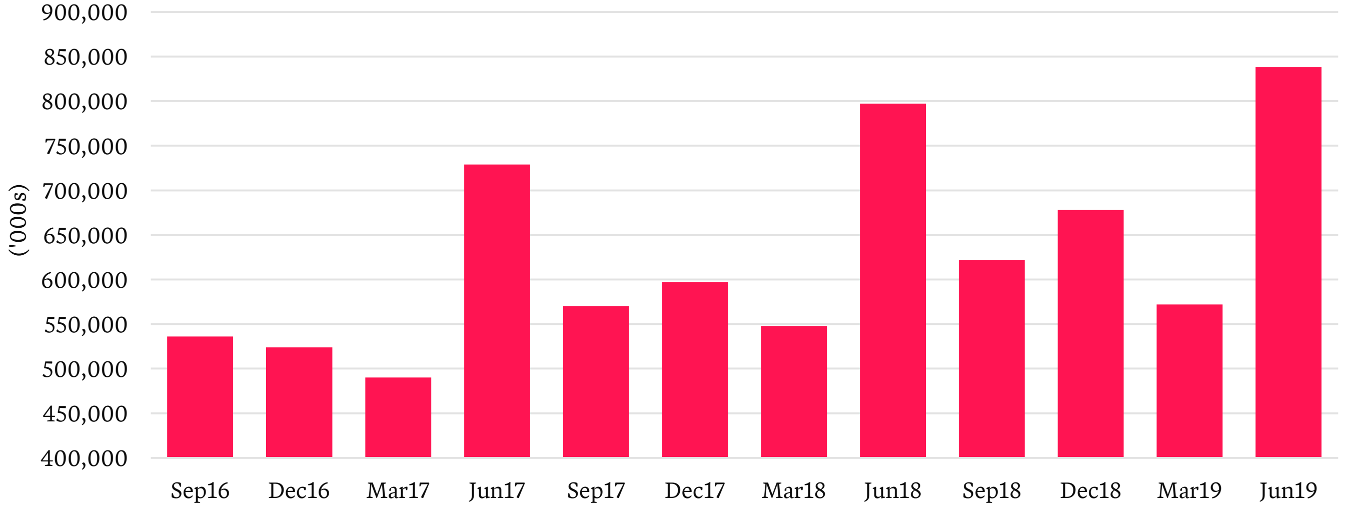
Combined ratio
Reporting quarter



Average premium
Reporting quarter



Total premium volume ($)
Reporting quarter



COMMERCIAL PROPERTY

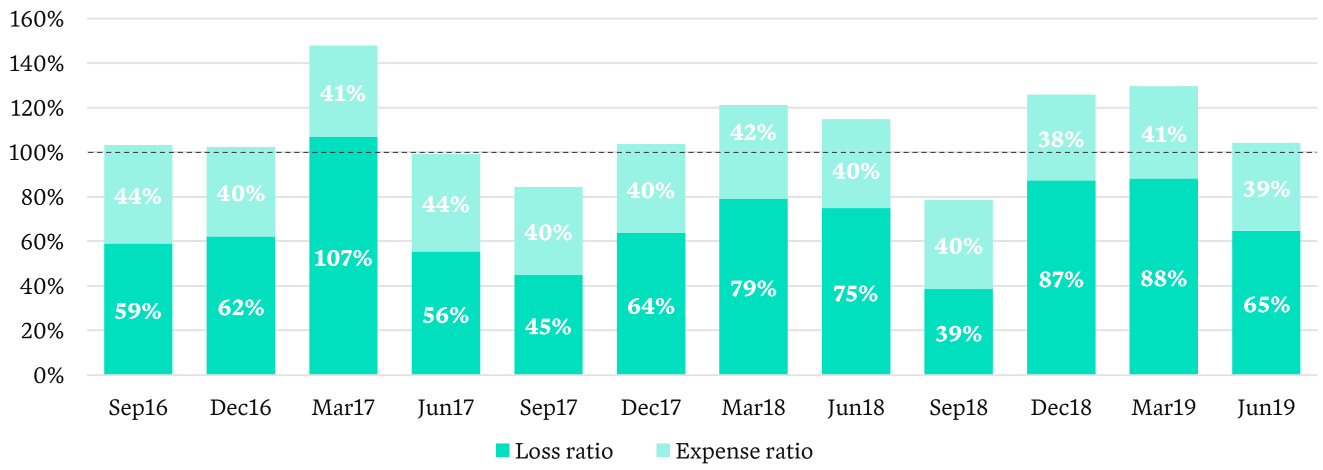
The gross loss ratio for FY2019 of 69%, was in line with the previous FY2018 figure of 67%, despite the adverse impact of the catastrophic Sydney hailstorm and Townsville flood events. Overall, the business remains unprofitable, with the annual combined ratio exceeding 100%.

↘ The insurance cycle turned in 2017, with premium increases currently exceeding claim inflation. This suggests profitability will improve in the absence of catastrophic event activity.

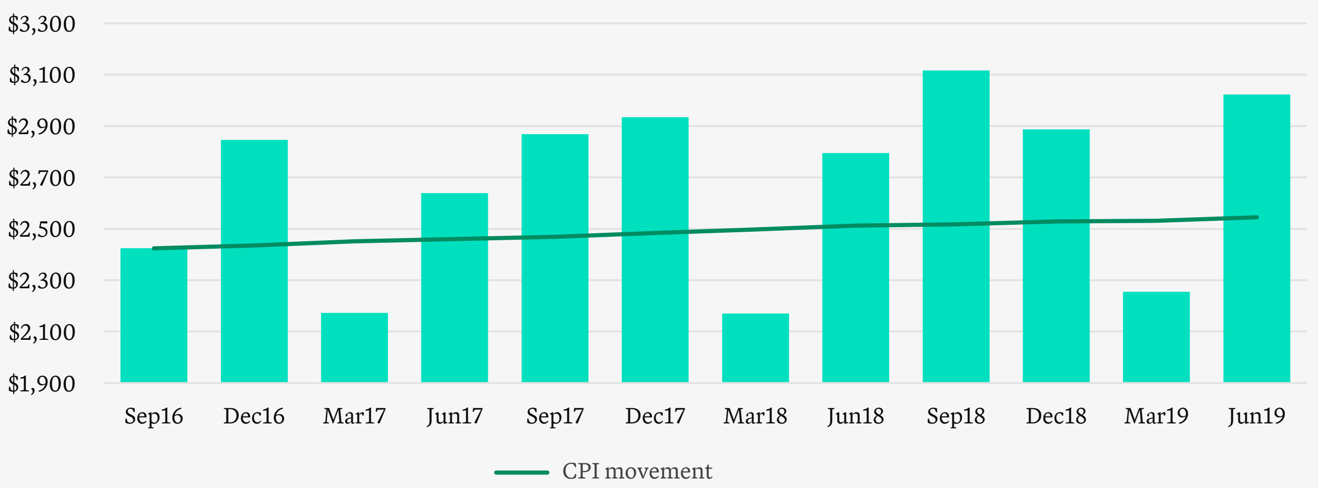
↘ Insurers are also being more selective, with perceived poorer risks being singled out for larger premium increases.

↘ Despite the hardening market, underwriters are struggling to achieve rate increases at the level required to restore profitability in the short term.

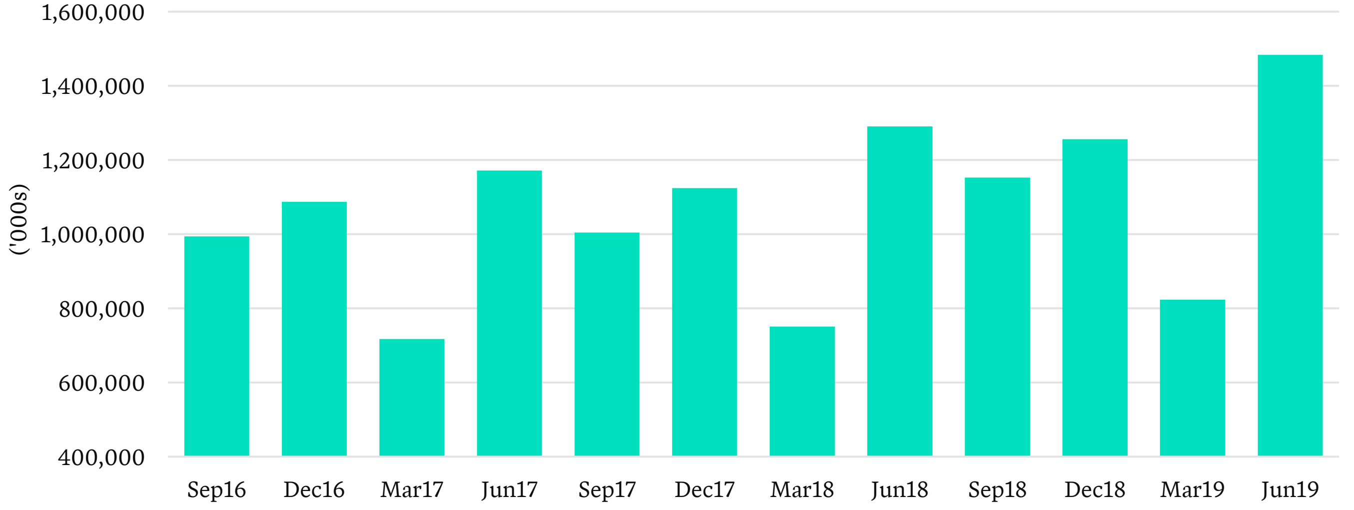
Combined ratio
Reporting quarter



Average premium
Reporting quarter



Total premium volume ($)
Reporting quarter



PUBLIC & PRODUCTS LIABILITY

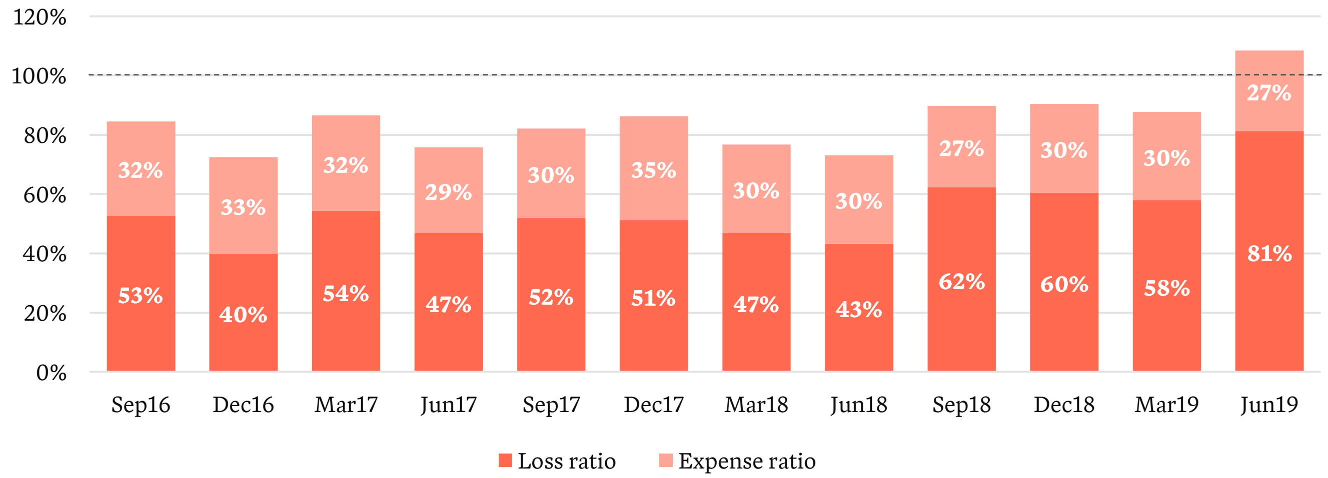
Profitability deteriorated during FY2019, particularly in the June quarter. However, this was primarily due to reserve strengthening, which added approximately 10% to the net loss ratio in FY2019, as compared to a 10% reduction attributable to reserve releases in FY2018.

↘
The reserve strengthening during FY2019 contrasts with several years of reserve releases in the preceding years. This may flag a turning point in the ‘reserving cycle’ leading to increases in estimated losses in future reporting periods.

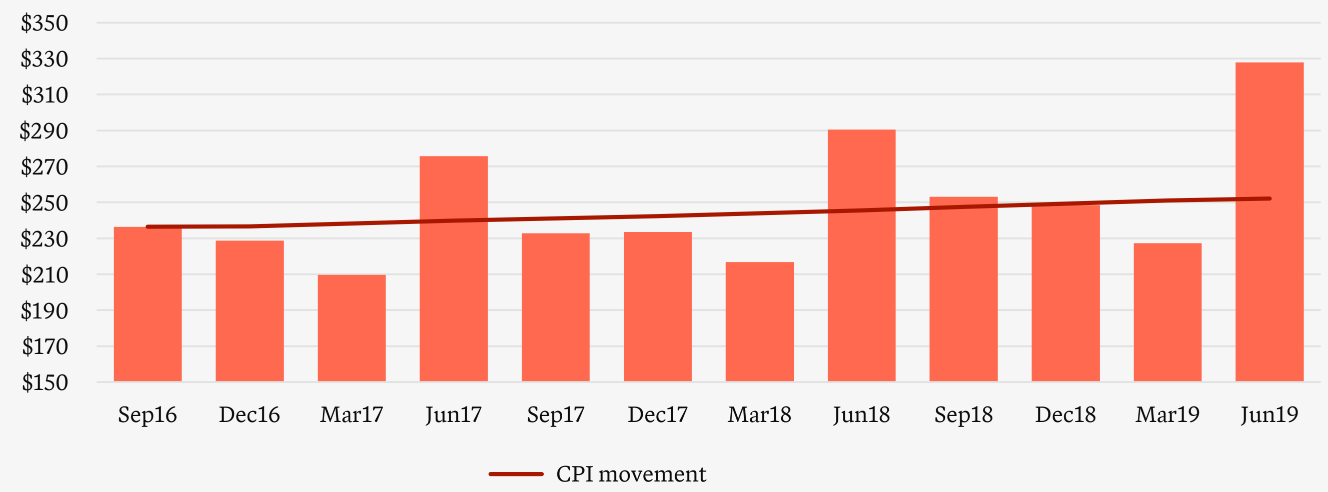
↘
Despite the deterioration in reported profitability, underlying risk trends remain satisfactory, with claim frequency holding steady.

↘
The construction industry has been the least profitable sector from an underwriting perspective, with the ultimate loss ratio having deteriorated in recent accident years.

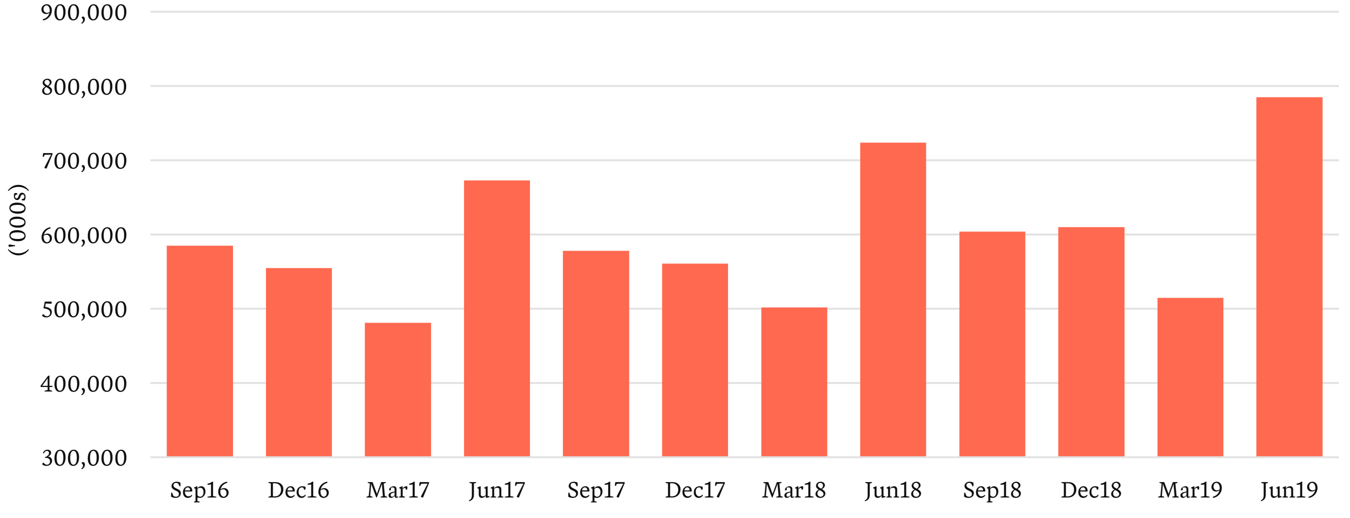
Combined ratio
Reporting quarter



Average premium
Reporting quarter



Total premium volume ($)
Reporting quarter



PROFESSIONAL INDEMNITY

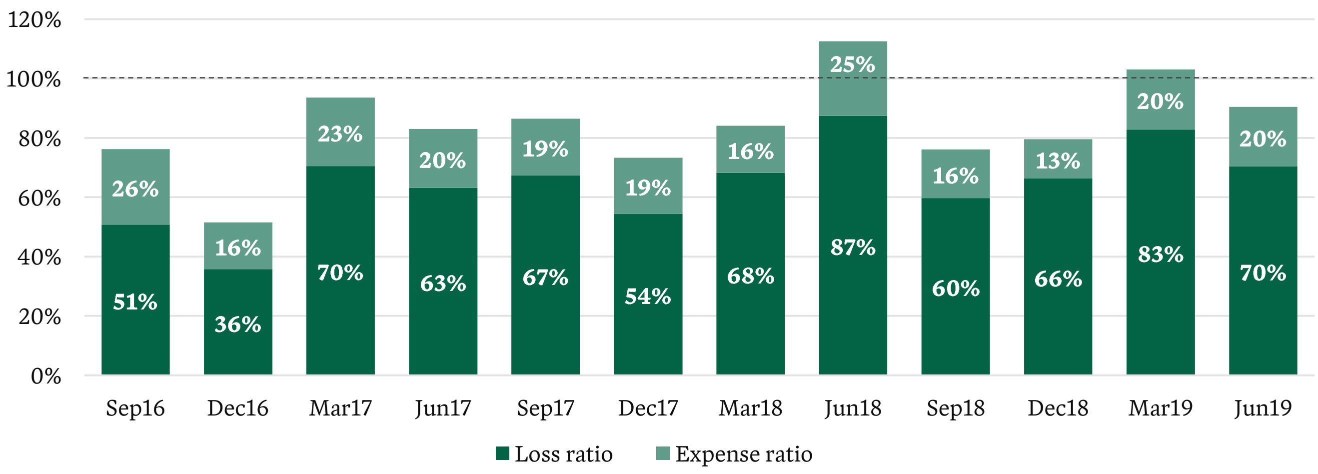
The Professional Indemnity market is hardening, with contraction of overall capacity from Lloyds and selective withdrawal from insurers operating in this market. Ongoing claim inflation and frequency concerns continue to put upward pressure on premium rates, with significant increases in average premium observed over the past three years, most notably in the latest quarter.

↘ Loss ratios over the past 10 underwriting years for medical malpractice have been increasing. This has been influenced by rising litigation rates against doctors, with a steady year-on-year increase in patient complaints to regulatory bodies.

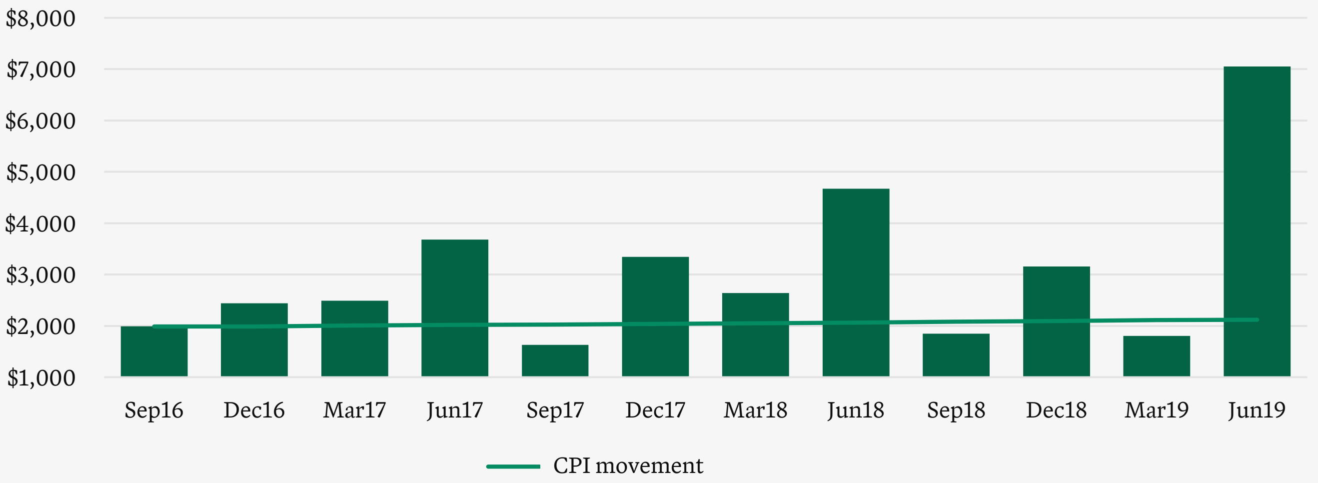
↘ Pressure also continues to mount for D&O, with securities class actions showing no signs of abating. There have also been premium increases and a withdrawal of capacity for those involved with the cladding and building defect crisis, including building certifiers, surveyors, architects and engineers.

↘ Insurers are using various strategies to reduce exposure to poor performing or higher risk segments. These include introducing royal commission exclusions, most notably in the financial services sector, and setting higher deductibles or attachment points for coverage.

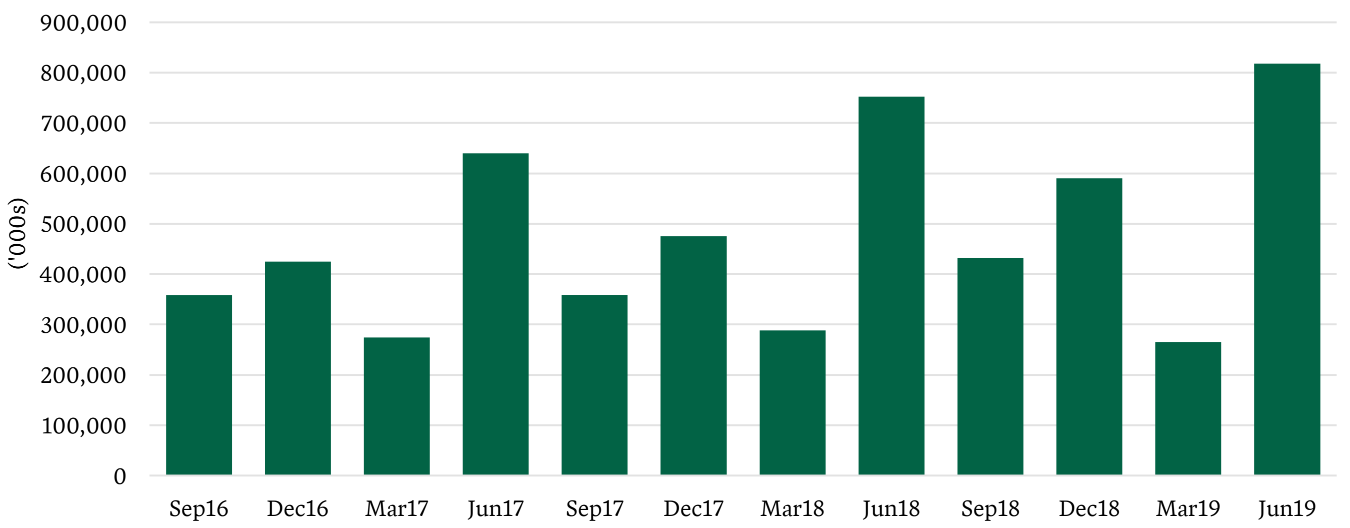
Combined ratio
Reporting quarter



Average premium
Reporting quarter



Total premium volume ($)
Reporting quarter



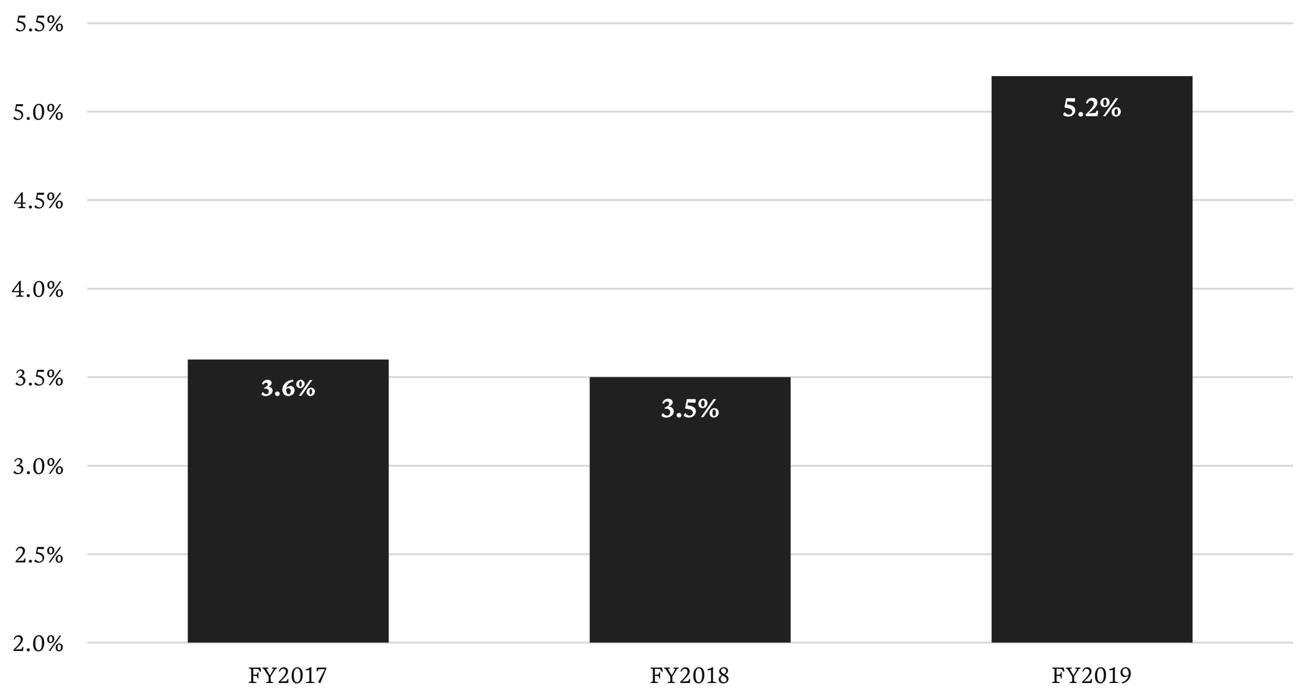
INVESTMENTS

Insurers attained an average investment return of 5.2% p.a. during FY2019, which represents a significant improvement on returns achieved over the prior two years.

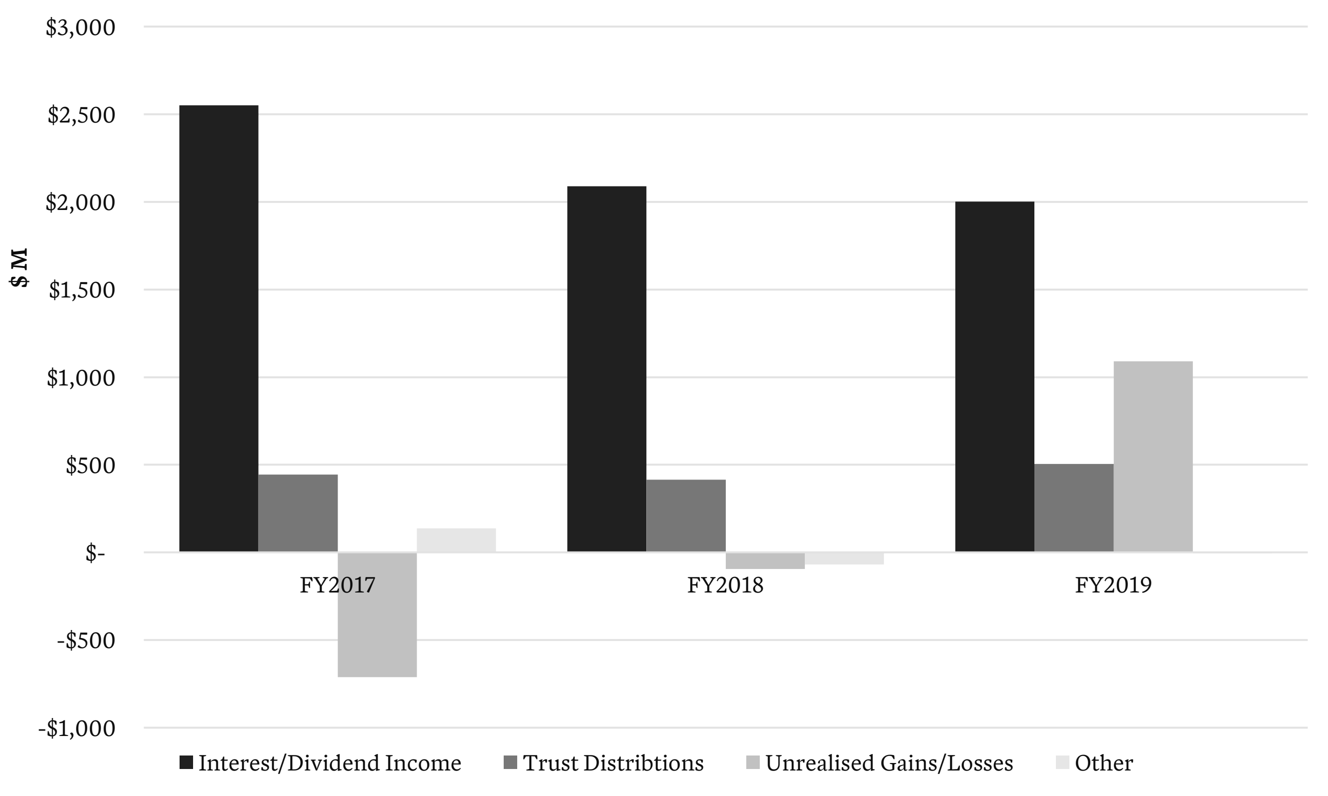
The improved return was attributable to unrealised gains on investments resulting from falls in interest rates, which were more than sufficient to offset a drop-off in interest income.

This one-off boost to investment returns also assisted insurers in counteracting the effects of increased liabilities due to a contraction in discount rates.

Investment returns
Reporting year



Investment income breakdown
Reporting year

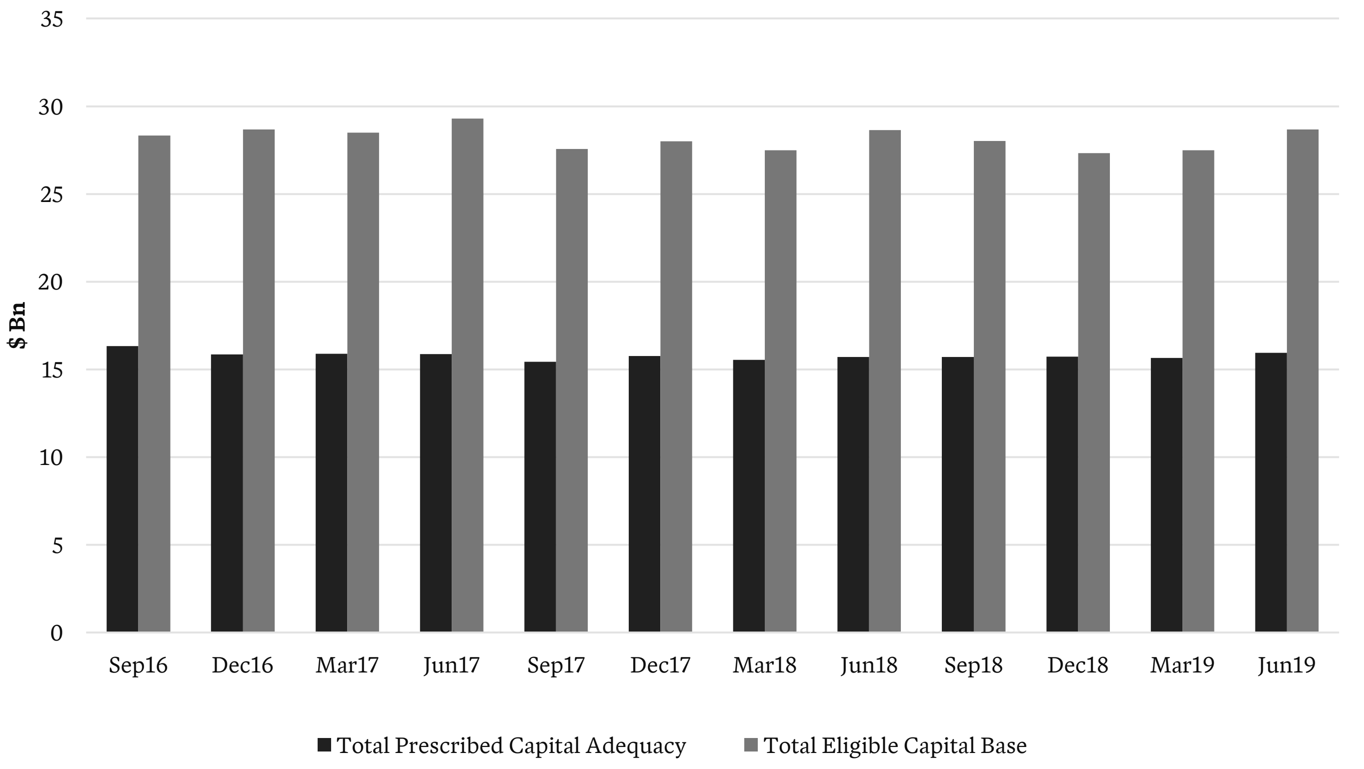


SOLVENCY TRENDS

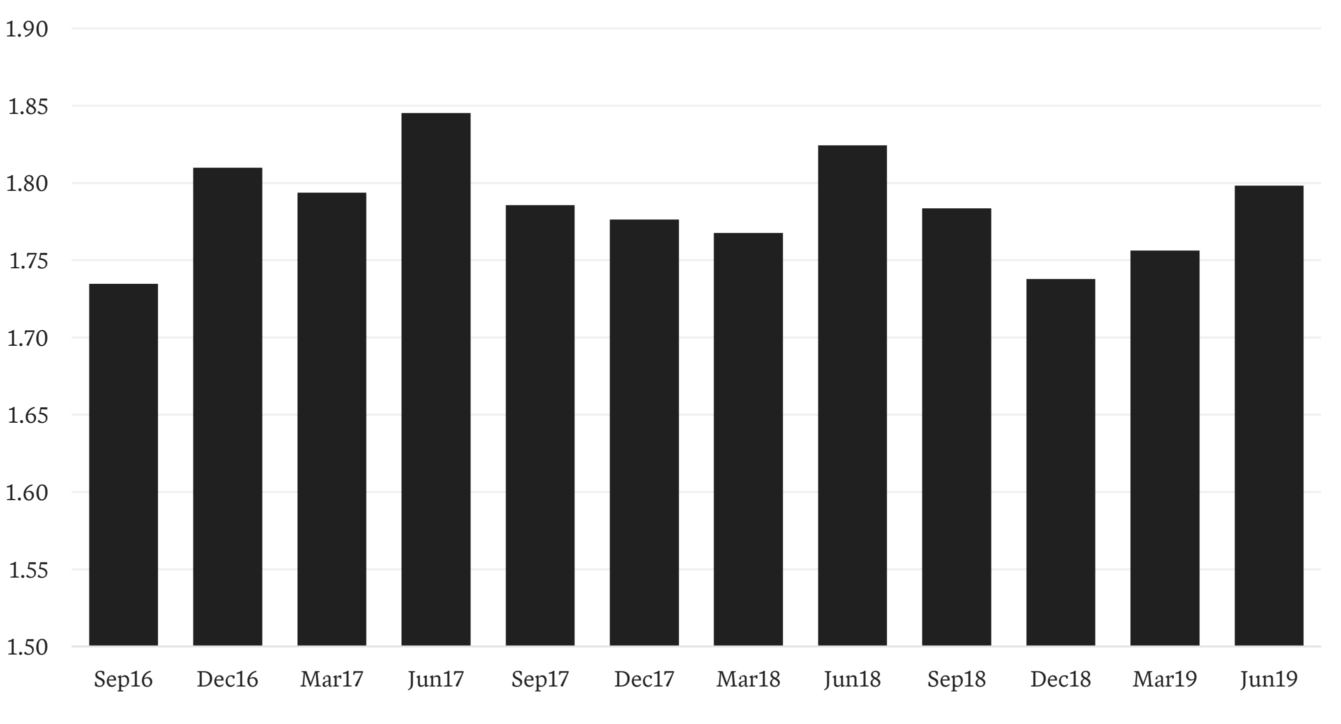
Overall industry solvency improved during the June quarter, with the Prescribed Capital Amount (PCA) Coverage Ratio reaching 1.80, the highest level for the past 12 months.

The improved solvency over the June quarter was attributable to insurers achieving growth in capital base during a period when PCA was relatively flat.

Capital base vs Prescribed Capital Amount
Reporting quarter



Prescribed Capital Amount coverage ratio
Reporting quarter



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We help business and government leaders see a clear way forward.

Taylor Fry's actuarial and analytics consultants support our clients in making strategic decisions to enhance the financial health of their organisations, and benefit communities, people and society.

We are creative problem solvers – from physicists and engineers to mathematicians and computer scientists. This variety strengthens our advice to meet the needs of our clients and their customers.

Our innovations have led to changes in government policy in Australia and New Zealand, and continue to break new ground, particularly in the social sector. Qantas liked our approaches in analytics so much, it bought a 51% stake in our business in 2015.

Across our offices in Sydney, Melbourne and Wellington, we value our people as individuals, offering a flexible working environment, with limited hierarchy and where everyone shares equally in the rewards.

We are mindful of our effect on the planet and have been carbon neutral since 2006.

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