TAYLOR FRY

Our class-by-class insights for insurers

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Welcome

Ready for your yearly dose of RADAR insight? Join us as we deep dive into our class-by-class roundup, latest trends, impacts and hot topics across Australia's insurance landscape. Overall, insurers have enjoyed a strong result in the nine months* to June 2024, but there's plenty of nuance to explore. With a sharp focus on industry integrity, the big themes are customers, AI and climate.

Drawing on the latest data released by the Australian Prudential Regulatory Authority (APRA), combined with deep industry know-how and experience, we unpick each major line of business across three years of results to help insurers benchmark their performance, and assess their strategies and goals.

For a quick overview, scan our Snapshot section on page 8 with all the key takeaways from each class, then head to Profitability, where you'll find our view on what's driving industry performance now and in the future (hint: transparency, accountability and the treatment of all customers are high on the agenda).

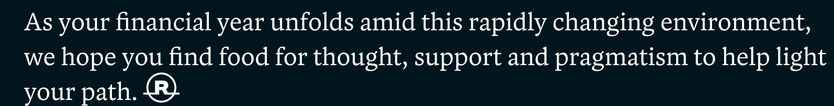
Want the nitty gritty? Delve into each class of business at your leisure. This year, Cyber joins the pack, on page 34, an indication of growing demand and an expanding marketplace. We look forward to further analysing this line of business as it matures.

In our Spotlight section, we piece together the affordability puzzle on page 54, one of the most urgent topics for insurers and their customers, to draw out the key ingredients towards a sustainable future.

In minimising the life-altering impacts of climate change, what does transitioning to a low carbon economy mean for insurers? Find out on page 50, as well as the critical role insurers can play.

Lastly, as businesses scramble to achieve productivity improvements and realise AI's potential, we look at the new risks AI introduces and the implications for insurers across governance, underwriting and products. Read all the details on page 58.

As your financial year unfolds amid this rapidly changing environment, we hope you find food for thought, support and pragmatism to help light your path.



Scott Duncan
Principal

*The latest APRA data excludes the September 2023 quarter. See next page for details.

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The fine print – a word on APRA's statistics

APRA introduced its new reporting framework on 1 July 2023, leading to changes in the information it publishes. Important changes to consider when reviewing this year's RADAR publication:

1. **No class-by-class data exists for the September 2023 quarter** (shown by a gap in our charts for that period), with data incorporating the new reporting framework starting from the December 2023 quarter onwards.
2. **The new APRA statistics mask more items** than the previous APRA statistics. In some cases, this creates difficulty in providing comprehensive commentary on the drivers of 2024 experience. For example, for direct insurers, other insurance service expenses are masked, which means we're unable to comment on movements in expenses at an industry level.
3. **Experience up to 30 June 2023 is on a different basis** to 2024 experience. Where possible, we've mapped the new and old line items to support comparison over time. However, this mapping is imperfect. For example, under the AASB123, discount unwind was included in the claims expense line. Under AASB17, discount unwind is included in the insurance finance expense line, which applies after the insurance service result. This mapping means the loss ratios and expense ratios included in the pre-30 June 2023 raw APRA statistics don't match those shown in this report.
4. **APRA hasn't published institution-level statistics**. Differences in the level of consolidation by region in each insurer's annual accounts means we're unable to comment on performance by insurer, specific to their Australian operations.

Snapshot

HOUSEHOLDERS

- **Affordability** and **availability** pressures grow > risks insured **reducing** > consumers without home insurance
- Multifaceted and collaborative approach critical to address issues after **double-digit premium increases**

COMMERCIAL PROPERTY

Key concerns for insurers:

- Fire claims
- Inflationary pressures
- Climate change impacts

Underinsurance an issue due to recent high levels of inflation

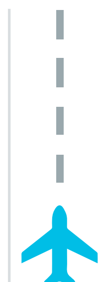
DOMESTIC MOTOR

Insurers are passing on cost pressures through **higher premiums**

Cost and repair times increasing for insurers with narrower pool of repairers

Customers on high alert after **successive price increases** > higher sensitivity to repair delays, poor service, broken price promises and adverse claim decisions

TRAVEL



- Monthly outbound travel volumes reached **pre-pandemic levels**
- New insurers **> competition intensifying**
- Attention shifting from restoring **profitability to growth**

CYBER

No.1 issue keeping directors awake at night – **cybercrime and data security**

Benign claims experience and increased competition **> softening market**

Accumulation risk top of mind

PUBLIC LIABILITY

Affordability and availability concerns for recreational, construction and youth-care sectors

Consideration of discretionary mutual funds on the rise in lieu of public iability insurance

Worker-to-worker and sexual abuse claims remain key issues

COMPULSORY THIRD PARTY

NSW: the Transitional Excess Profits and Excess Losses framework has **returned ~$450M** in excess insurer profit to motorists through levy reductions

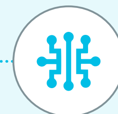
QLD: RACQ Insurance exited market in 2023 > risks distributed to **Suncorp, Allianz and QBE**

PROFESSIONAL INDEMNITY & DIRECTORS AND OFFICERS

Litigation funders view Australia as open jurisdiction

Softening market for D&O, up to 30% premium reductions

Risk profile for Medical indemnity insurers changing – increase in representation claims, nervous shock claims, changes in delivery of healthcare



Policy wording and underwriting practices under review because of **'silent AI' exposure**

LENDERS MORTGAGE INSURANCE

Switching low fixed-rate to high variable-rate mortgages **> mortgage defaults rising**

Unemployment, interest rates and property prices will **affect outlook**

WORKERS COMP

Many privately and publicly underwritten schemes – **rising claim numbers** and increases in claim duration

Key driver – increase in psychological claims:

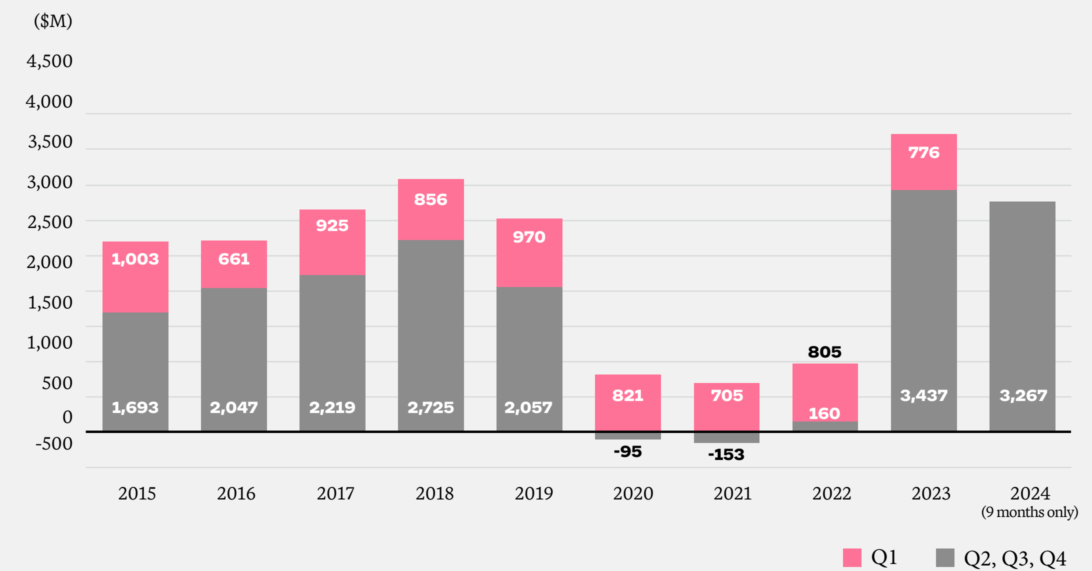
Longer return to work than physical claims

Pre-existing mental health vulnerabilities > higher likelihood for lodging a claim

Profit ability

The latest APRA data shows the general insurance industry recorded its strongest result in more than 10 years, with a profit after tax of $3.9 billion over the nine months* to 30 June 2024. This follows a full year profit after tax of $4.6 billion over the year to 30 June 2023.

What do these results say about the industry? Here are the five things you need to know ...



1. Direct insurers recorded a $3.3 billion profit after tax

This result was for the nine months to 30 June 2024, in line with the $3.4 billion recorded in the nine months to 30 June 2023.

This result was driven by:

- Premium increases in personal lines matching increases in claims costs
- Catastrophic losses coming in below expectations
- Investment returns of $3.4 billion in the nine months to June 2024, $0.8 billion higher than the same period last year.

Annualised return on capital (based on the nine months to 30 June 2024) for direct insurers was 14%, 2% lower than 2023 levels, and still a very healthy result.

2. Underwriting result highlights

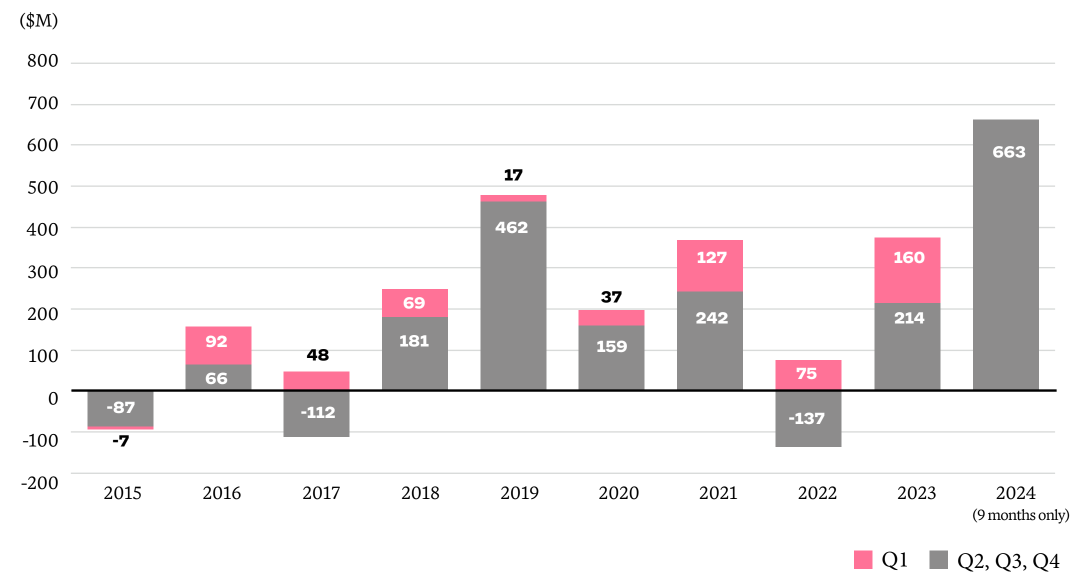
Householders recorded an insurance service result of $0.5 billion in the June 2024 quarter. This follows losses of $0.7 billion and $0.2 billion in the December 2023 and March 2024 quarters respectively. Future profitability will depend on the level of catastrophic activity and whether recent price increases are sufficient to cover the increase in claims costs, particularly as labour shortages for skilled workers continue to increase repair costs.

Domestic Motor recorded an insurance service result of $0.6 billion in the nine months to 30 June 2024, up from $0.3 billion over the same period last year. While the cost of spare parts and accessories seems to have peaked, repair costs are on the rise due to labour shortages and increases in repair times. The technology embedded in new vehicles and the shift to electric vehicles is changing the nature of repairs for the industry.

Reserve releases had a large impact on 2024 industry performance with Lenders Mortgage Insurance (LMI), Compulsory Third Party, Professional Indemnity and Workers Compensation all benefiting from a reassessment of prior year claims costs. LMI is a standout class as the reserves built early on in the pandemic continue to be released. LMI insurers have not seen an increase in claims due to property price increases, low unemployment and government support during COVID-19.

*The latest APRA data excludes the September 2023 quarter. Go to page 6 for more information.

Reinsurers profit after tax, split by quarter



3. Reinsurers recorded a $0.7 billion profit after tax

This result was for the nine months to 30 June 2024, the best result in more than 10 years.

This result was driven by:

- Reinsurers being more selective of risks, which contributed to the better claims result
- Catastrophic losses coming in below expectations
- Investment returns of $0.3 billion in the nine months to June 2024, in line with the same period last year.

Annualised return on capital for reinsurers was 19%, 10% higher than 2023 levels.

4. The industry continues to be adequately capitalised

Measured with reference to APRA's Prudential Capital Amount, for direct insurers, the coverage ratio increased from 172% at 30 June 2023 to 178% at 30 June 2024. For reinsurers, the coverage ratio increased from 185% to 201%.

5. In our view, some of the key themes driving future industry performance are:

Transparency, accountability and the treatment of all customers

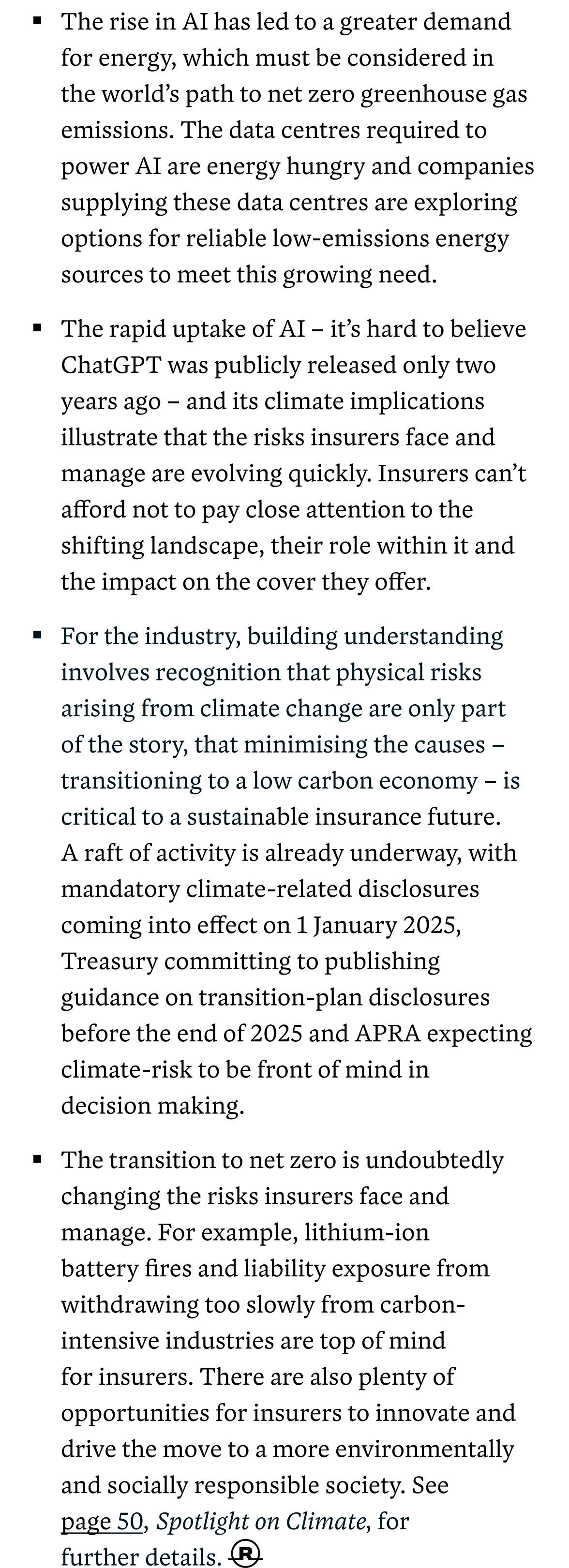
The Parliamentary inquiry into insurers' resposnes to 2022 major floods claims, with its focus on the three P's – policyholder treatment, pooling mechanisms and prioritising preparation – needs to be considered in conjunction with:

- The introduction of the Financial Accountability Regime for insurers on 15 March 2025, which crystalises responsibilities and strengthens accountability requirements
- The Design and Distribution Obligations and Unfair Contract Terms protection for consumers introduced in 2021
- Any changes to the General Insurance Code of Practice.

There's heightened focus on treating all customers fairly in all situations. Many of the recommendations arising from the flood inquiry are relevant outside home insurance, and the industry is actively considering what this means for other products and their processes. As part of the increased focus on customers, senior management and Boards are increasingly demanding information on customer outcomes to complement the usual metrics on financial performance.

Silent AI

Reflecting on the lessons learned from silent cyber, insurers are getting on the front foot to clarify coverage and build out underwriting requirements to include questions on the use of AI. To emphasise the importance of addressing this issue in a timely manner, ChatGPT – a large language model – was launched in 2022 and reached one million users in just five days. For comparison, Facebook launched in 2004 and took 10 months to reach one million users. The insurance industry is no stranger to AI and is well versed in the opportunities offered by AI and the potential risks. The focus now is on understanding the opportunities for new products and how AI changes the risk landscape for existing products. See page 58, *Spotlight on AI*, to read more.



Climate – power demands and transition to net zero

- The rise in AI has led to a greater demand for energy, which must be considered in the world's path to net zero greenhouse gas emissions. The data centres required to power AI are energy hungry and companies supplying these data centres are exploring options for reliable low-emissions energy sources to meet this growing need.
- The rapid uptake of AI – it's hard to believe ChatGPT was publicly released only two years ago – and its climate implications illustrate that the risks insurers face and manage are evolving quickly. Insurers can't afford not to pay close attention to the shifting landscape, their role within it and the impact on the cover they offer.
- For the industry, building understanding involves recognition that physical risks arising from climate change are only part of the story, that minimising the causes – transitioning to a low carbon economy – is critical to a sustainable insurance future. A raft of activity is already underway, with mandatory climate-related disclosures coming into effect on 1 January 2025, Treasury committing to publishing guidance on transition-plan disclosures before the end of 2025 and APRA expecting climate-risk to be front of mind in decision making.
- The transition to net zero is undoubtedly changing the risks insurers face and manage. For example, lithium-ion battery fires and liability exposure from withdrawing too slowly from carbon-intensive industries are top of mind for insurers. There are also plenty of opportunities for insurers to innovate and drive the move to a more environmentally and socially responsible society. See page 50, *Spotlight on Climate*, for further details.

House holders

The starkest indicator from available APRA stats is that consumers appear to be turning away from home insurance as cost-of-living pressures bite. The number of risks insured retreated by around 3% over the three quarters to June 2024, compared with the equivalent period the year before. This is the largest year-on-year drop in insured risks since at least 2013, and follows a 19% year-on-year increase in average written premium. These increases in premiums don't yet appear to be translating to improved industry profitability, with net combined ratios sitting around 105% over the available period.

Catastrophe costs steady

According to the Insurance Council of Australia (ICA), total catastrophe costs remained steady against 2022/23 levels, at around $2.19 billion. The most significant event during this period was the Christmas and New Year storms in Queensland, New South Wales and Victoria, which resulted in losses of $1.33 billion. Other notable weather events included Tropical Cyclone Jasper, the Valentine's Day storms in Vic, and severe weather in April across NSW and Qld. Encouragingly, most insurers indicated that catastrophe losses remained within their reinsurance program allowances, supporting overall financial performance.

Gross written premium | Reporting quarter

($M) 0 – 4,500; ($) 0 – 1,400

Sep 21, Dec 21, Mar 22, Jun 22, Sep 22, Dec 22, Mar 23, Jun 23, Sep 23, Dec 23, Mar 24, Jun 24

Gross written premium — Average written premium

Net combined ratio | Reporting quarter

(%)	Net loss ratio	Net expense ratio
Sep 21	65%	28%
Dec 21	93%	28%
Mar 22	79%	28%
Jun 22	61%	30%
Sep 22	71%	25%
Dec 22	98%	23%
Mar 23	82%	24%
Jun 23	62%	25%
Sep 23		
Dec 23	101%	28%
Mar 24	78%	30%
Jun 24	52%	28%

Total gross loss ratio and contribution from prior years

(%)	Total gross loss ratio	Gross loss ratio: contribution from prior years
Sep 21	57%	0%
Dec 21	83%	0%
Mar 22	166%	-1%
Jun 22	78%	0%
Sep 22	67%	2%
Dec 22	88%	1%
Mar 23	83%	4%
Jun 23	54%	4%
Sep 23		
Dec 23	92%	3%
Mar 24	67%	0%
Jun 24	48%	2%

> "Educating policyholders about preventive measures could help reduce claims and position insurers as proactive partners in risk management.

Preventable perils create big losses

At the same time, insurers continue to face challenges from working perils, particularly water and fire damage. Water damage, primarily caused by the failure of flexi-hoses, has led to significant losses, especially when homeowners are away during holidays. This issue is preventable, and measures such as regular maintenance inspections and the installation of pressure-limiting valves could significantly reduce claims. This is an opportunity for insurers to take a more proactive stance in preventing these losses.

Fire damage is an even greater concern, driven largely by the increasing use of lithium batteries. These batteries are highly flammable, and not only a growing cause of fires but significantly worsen fire severity. The industry has begun responding by advocating for changes to strata codes regarding the safe charging of electric vehicles and bikes on common property. However, as consumers continue to purchase and store lithium battery-powered items at home, the cost impacts of fire losses are expected to remain high.

Pressure builds on premium pricing

The inflation outlook for home insurance remains uncertain, with some insurers still reporting double-digit inflation for home policies. This may be exacerbated by the government's ambitious home-building plans to construct 1.2 million new homes over five years, which, combined with a reduced intake of skilled migrants, could push labour costs higher. These factors are likely to continue placing upward pressure on home insurance premiums and lead to bottlenecks in skilled labour, slowing down claims resolution times.

Increases slower in the north

The ongoing rollout of the ARPC Cyclone Pool in northern Australia is beginning to deliver lower premiums for customers, especially in moderate and high cyclone risk areas. Although overall premiums in the north are continuing to increase, they're rising at a slower rate than the rest of Australia. Insurers are also furthering efforts to encourage private risk mitigation in line with the objectives of the pool.

Strata focus

Residential strata insurance has also come under scrutiny, particularly concerning broker commissions and strata manager payments. While recent reforms have introduced more transparency, further regulatory action is possible as media and public scrutiny on these issues continues to grow.

Regulatory trends

On the political and regulatory front, NSW has announced plans to phase out the Emergency Services Levy, which is expected to reduce premiums for affected lines, particularly domestic property, by an average of 18%. However, insurers should prepare for intense scrutiny of their pricing practices during this transition, as seen in previous attempts to remove the levy.

The Parliamentary inquiry into insurers' responses to 2022 major floods claims has resulted in a raft of recommendations relating to how insurers assess and manage claims, and how they communicate with customers. Recommendations include standardisation of flood definitions, transparency on pricing structure, considerable strengthening of the General Insurance Code of Practice and consideration of a flood pool. While it's likely this report will result in some material changes for the insurance industry, the exact nature of those changes is unclear, given: the Government will need to respond to the recommendations; Coalition members of the committee penned a dissenting opinion; and a federal election is looming.

Looking ahead, the Senate Select Committee on the Impact of Climate Risk on Insurance Premiums and Affordability is due to deliver its report on 19 November 2024. The committee is focused on how the pricing of climate risks can be redistributed across the economy. Insurers may need to refine how they construct and communicate risk pricing models. For instance, homes with flood-proofing or fire-resistance upgrades may need explicit discounts.

What insurers can do ...

Help shape future regulations

The growing political focus means insurers must engage more actively with regulators. By providing insights into the practicalities of climate risk pricing, insurers can help shape future regulations, balancing affordability with risk sensitivity. Additionally, they should prepare for greater compliance demands, including increased reporting requirements relating to climate risk exposure and mitigation efforts.

Strengthen communication

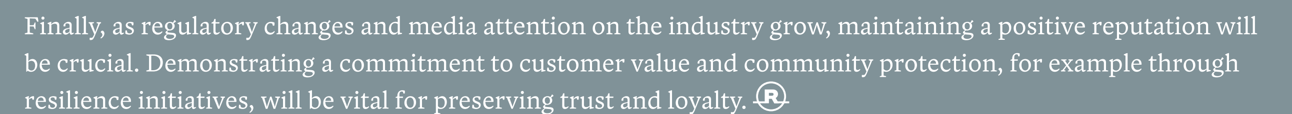
Beyond regulatory engagement, insurers should review and, where necessary, strengthen their communication with policyholders, particularly regarding risks such as lithium battery fires and water damage. Educating policyholders about preventive measures could help reduce claims and position insurers as proactive partners in risk management. This could extend to offering incentives for resilience measures, such as discounts for homes that have had recent maintenance, and checks of flexi-hoses and related items.

Review reinsurance cover

While recent catastrophe experience has been favourable, insurers can't rely on this trend continuing, especially as climate change leads to greater volatility in experience. Rising global catastrophe activity, including a more active Florida wind season, could drive up reinsurance costs, requiring careful management of reinsurance coverage levels. Insurers may need to explore alternative risk transfer mechanisms, such as catastrophe bonds, to maintain financial resilience.

Demonstrate customer commitment

Finally, as regulatory changes and media attention on the industry grow, maintaining a positive reputation will be crucial. Demonstrating a commitment to customer value and community protection, for example through resilience initiatives, will be vital for preserving trust and loyalty.



Compulsory Third Party

Gross earned insurer premiums in **New South Wales** have increased over the previous three years to levels similar to 2019 (see top chart opposite). Reductions in claims frequency assumed over time by the State Insurance Regulatory Authority (SIRA) have been offset by increased average claim size. The latest quarterly actuarial monitoring indicates that experience trends are upwards for claims frequency and average claim size, suggesting premium rates may come under pressure.

TEPL impacts – a varied story

The Transitional Excess Profits and Excess Losses (TEPL) framework has, to date, returned around $450 million of excess insurer profit to motorists through levy reductions, although almost 85% of that relates to the first accident year (AY2018) of the new scheme. SIRA practice is to recoup profits that are more than 80% likely to emerge, so it's unsurprising that the subsequent years (which are more uncertain) have delivered less through TEPL. However, AY2019 has generated only one-third of the excess profit of AY2018 at the same point of development (certainty). Without the subsidy from TEPL, current premiums would be around $30 more expensive for motorists.

New South Wales scheme movements

Recent scheme changes are emerging in the claims experience:

- The 20-month waiting period for claims below 10% whole-person impairment to lodge a claim for damages has been removed bringing forward both recognition and payments
- The entitlement period over which at-fault claims and not-at-fault threshold claims can receive statutory benefits has increased from 26 weeks to 52 weeks for accidents after 1 April 2023, increasing average cost and propensity to make a statutory benefit claim
- The insurer decision regarding liability for statutory benefits has been extended from three months to nine months.

Sunshine State of play

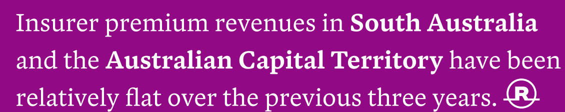
In **Queensland**, insurer RACQ Insurance exited from the scheme during 2023. The RACQI business was allocated to the remaining insurers, which saw the Suncorp portfolio increase in size by around 25%, Allianz increase by almost 40% and QBE more than double in size (to a market share of 15%). In the bottom chart opposite, we show these market shares comparatively, at March 2023 and June 2024.

Overall vehicle numbers in Queensland are increasing by around 3.0% per annum (2.3% per annum for class-one vehicles), which has seen insurer gross earned premium increasing steadily over time. As for average insurer premium, it's currently $186 – which is similar to the average premium three years ago, and is lower in real terms. Conversely, the total premium paid by motorists (currently around $370) has increased over the same period. This is due chiefly to an increase in the levy paid to the National Injury Insurance Scheme Queensland for catastrophic injuries. All insurers are currently priced at the ceiling.

Taylor Fry's latest scheme actuary report indicates claim frequency is generally reducing over time, and average claims size – while somewhat variable quarter to quarter – is averaging around $130k per claim over the past three years.

Elsewhere around the country

Insurer premium revenues in **South Australia** and the **Australian Capital Territory** have been relatively flat over the previous three years.

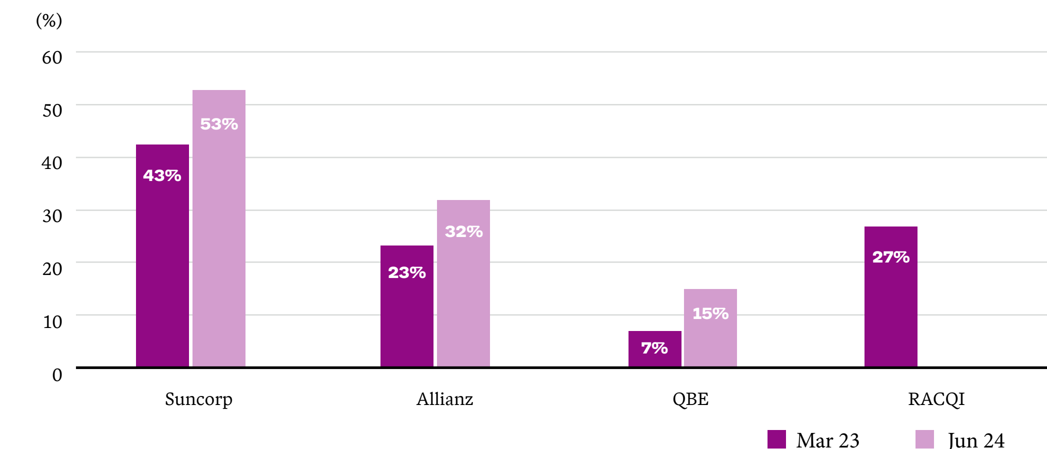


The Transitional Excess Profits and Excess Losses (TEPL) framework has, to date, returned around $450 million of excess insurer profit to motorists through levy reductions.

CTP | Gross earned premium

Source: APRA, insurer revenue (with interpolation/extrapolation for missing Sep 23 quarter in FY2024 APRA data)

Qld CTP | Market share



Source: Motor Accident Insurance Commission

Workers Compensation

Gross earned insurer premium revenue in the privately underwritten workers compensation jurisdictions has shown strong growth over the past three years – a combination of wages growth and increases to underlying premium rates. In the chart opposite, you can see how the data tracks across this period.

Top trends in claims and premiums

The largest of the privately underwritten schemes, Western Australia, has experienced increasing trends in claims. Key takeouts from the June 2024 WorkCover WA scheme status report:

- **2024 claim numbers were almost 6% higher than the previous year**
- **Claims with more than 60 days in time lost have increased by 23%**
- **Claim payments and insurer case estimates in 2024 each increased by almost 15%.**

The average recommended premium rate for FY2025 was 1.732% of wages, an increase of 0.3% from FY2024 but still lower than the FY2023 rate of 1.822%. The recommended premium rate rose by around 15% in the five years to 30 June 2022, whereas the actual (achieved) premium rate grew by around 27% over this same period.

Understanding drivers and the role of mental injury

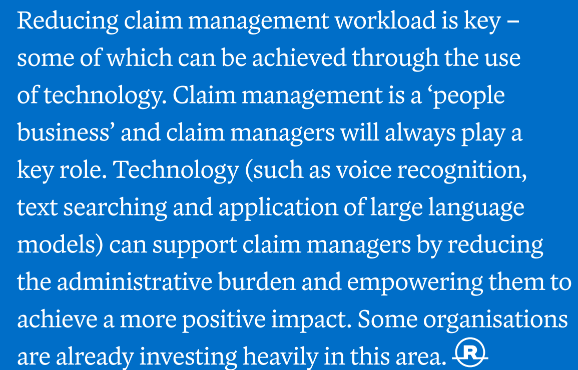
While some of the elevated claim experience in Western Australia relates to greater exposure, some relates to a worsening in claims experience. This trend (rising claim numbers and extended claim durations) is also evident in many other workers compensation schemes – privately and publicly underwritten.

One of the drivers of this experience is an increase in claims for psychological injury (primary and secondary). Claimants suffering work-related psychological injury on average take longer to return to work than claimants with a physical injury and have higher average cost. Research by Taylor Fry also indicates that people with pre-existing mental health vulnerabilities have higher likelihood of lodging claims for workers compensation in the first instance, whether for physical or psychological injury.

Workload solutions critical for a 'people business'

The uptick in claim numbers and claim duration has amplified demand for claim management staff across schemes and insurers. In the past, this has created a vicious cycle – increased workload on claim managers leading to claim cost increases if claims don't receive the attention they need when they need it.

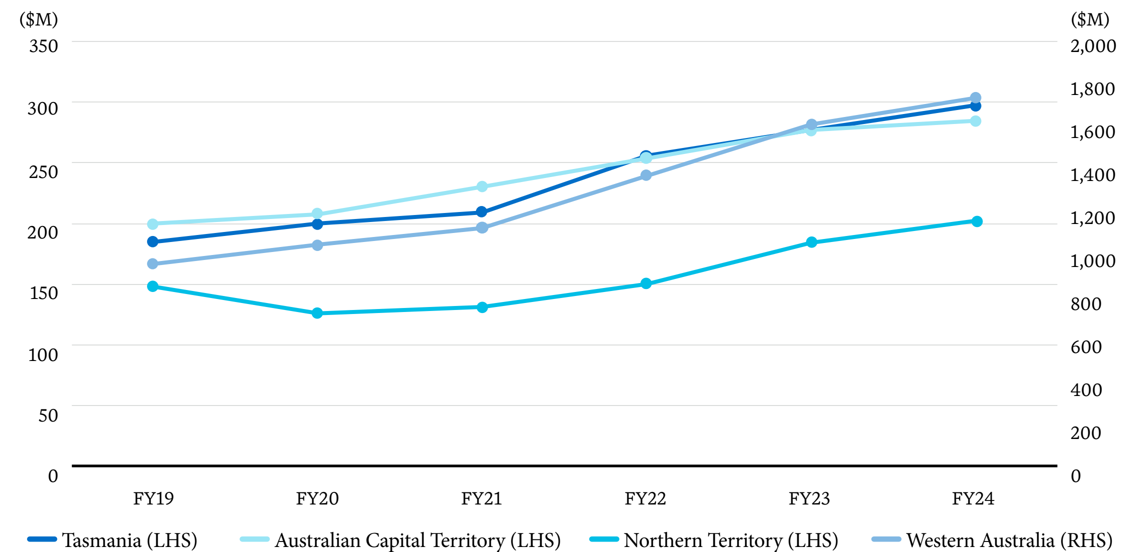
We understand experienced claim managers are particularly hard to find – which makes a material difference in managing claim outcomes. Attracting new people into the industry may be a longer-term solution – but in the short term it may mean less experience and potentially poorer return-to-work outcomes.



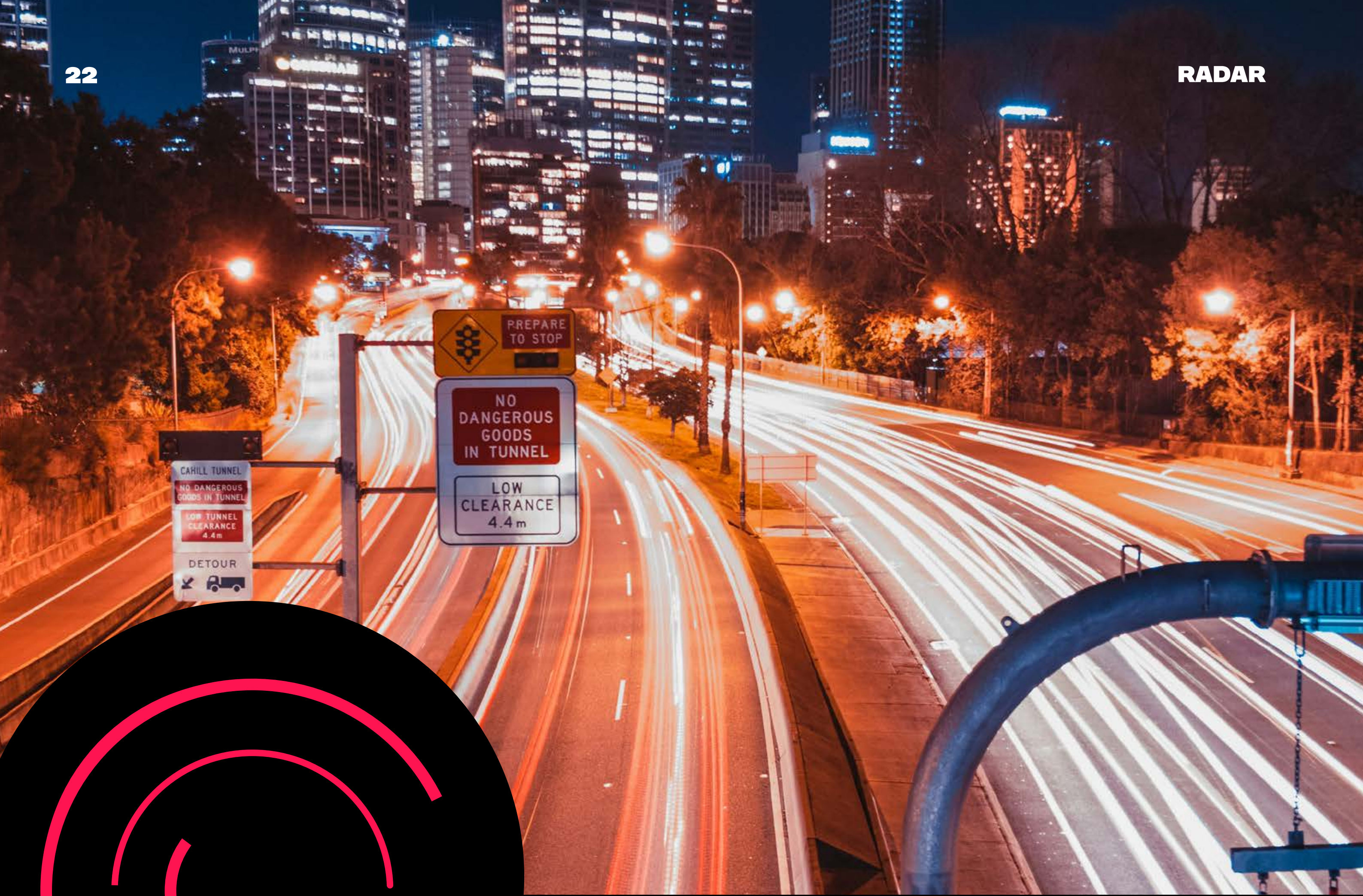
Reducing claim management workload is key – some of which can be achieved through the use of technology. Claim management is a 'people business' and claim managers will always play a key role. Technology (such as voice recognition, text searching and application of large language models) can support claim managers by reducing the administrative burden and empowering them to achieve a more positive impact. Some organisations are already investing heavily in this area. ®

> Research by Taylor Fry indicates that people with pre-existing mental health vulnerabilities have higher likelihood of lodging claims for workers compensation, whether for physical or psychological injury.

Gross earned premium | Reporting quarter



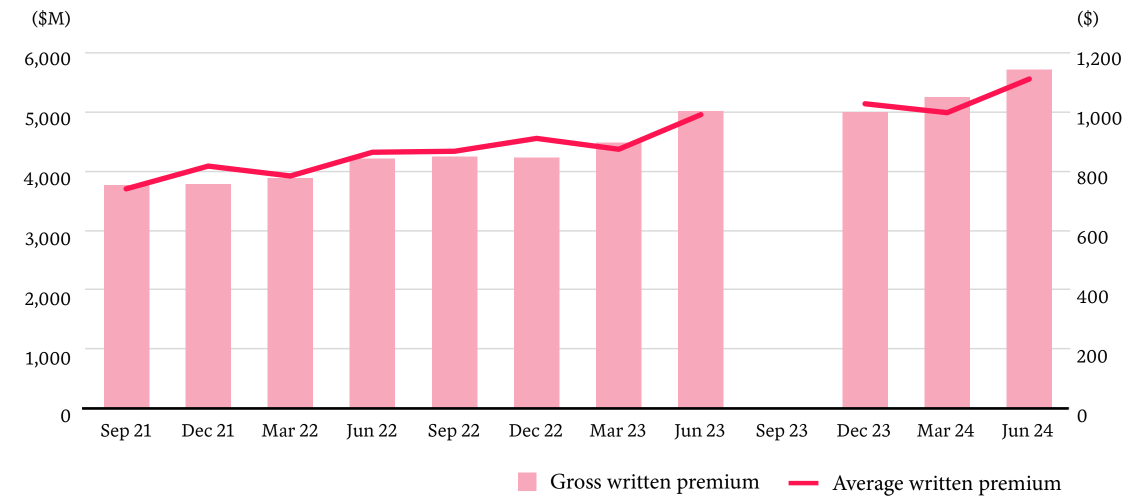
Source: APRA, insurer revenue (with interpolation/extrapolation for missing Sep 23 quarter in FY2024 APRA data)



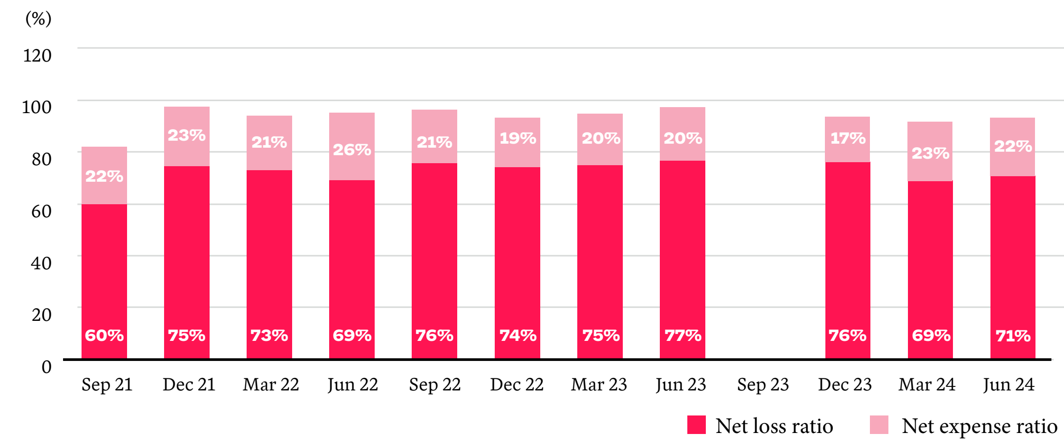
Domestic & Commercial Motor

Solid growth in premiums combined with a relatively benign period for natural disasters have led to strong profit margins for Domestic and Commercial Motor portfolios. Comparing the half-year to June 2024 with the previous year, we see nearly 20% increases for domestic and commercial insurance revenue (gross earned premium), driven mostly by increases to average premium levels. Loss ratios and combined ratios appear to have materially improved, albeit potentially impacted by accounting changes.

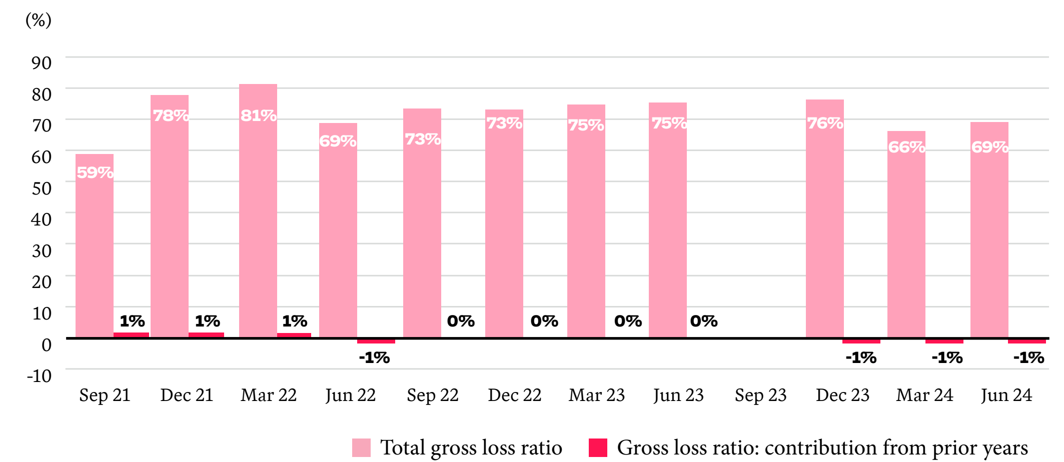
Gross written premium | Reporting quarter



Net combined ratio | Reporting quarter



Total gross loss ratio and contribution from prior years



The rapid changes in technology and tools are demonstrating the tremendous value in having systems that can be hooked into new tools as they develop.

While claims cost inflation has been a marked feature of these lines for the past couple of years, pressures appear to be easing and insurers have been able to pass on costs, with premium growth outpacing cost growth for most insurers. A mixed bag of other front-of-mind issues include:

- Cost and repair times increasing for insurers who have narrowed their pool of repairer suppliers
- Falling second-hand car prices leading to some favourable trends, such as market valuations, meaning sums insured don't have to remain as high, which defrays other pricing pressures
- Third-party claims showing significantly higher cost growth for some insurers.

Times are changing

Sectoral change is apparent. Increasing numbers of electric vehicles has exposed a lack of capacity in the skills and supply chains needed to repair these vehicles, leading to avoidably higher repair and replacement costs, as well as delays.

Looking ahead, insurers will need to manage these emerging supply-side challenges of ensuring affordable prices and an appropriate variety of suppliers that can deal with changes in today's vehicles. Technology and electric vehicles are a focus, with insurers indicating manufacturers must do more to make parts available and provide guidance on circumstances when EVs (particularly their batteries) can be repaired safely.

Accounting changes have occupied a reasonable amount of insurer time. A swathe of policies have been recognised as onerous (contributing an additional 1% loss ratio to Domestic Motor over FY24) for some insurers, and assessment of onerous contracts can be challenging, given the complexities of pricing.

Fraud firsts

The year has also presented some firsts, for example fraudulent claims making use of generative AI to doctor vehicle images and other evidence, as Allianz discovered in the United Kingdom. More broadly, the Insurance Council of Australia has announced a fraud initiative to identify fraud through multiple claims for the same event across insurers in a privacy-respectful way. Whether fraud risks are old school or due to emerging technologies, increasing claim sizes mean that incentives, and the need for vigilance, have grown.

Conversely, insurers have experimented with artificial intelligence to better detect potential fraud. This game of cat and mouse seems likely to intensify in the short term.

Are you technology ready?

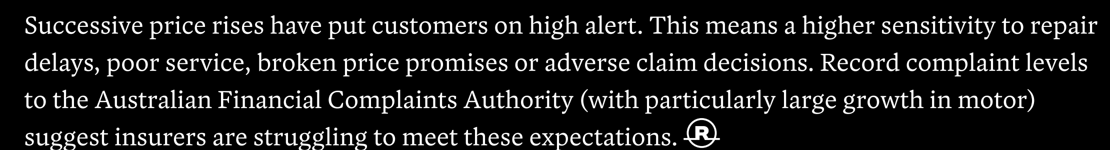
Longer term, while some companies are ready to take the plunge on certain technology solutions, the rapid changes in technology and tools are demonstrating the tremendous value in having systems that can be hooked into new tools as they develop. This applies to all areas, including supply chains and fraud detection, but claims and policy management have perhaps experienced the most rapid developments. In many cases, this means phasing out legacy systems for those that can better integrate with cloud services, as well as those that can surface different kinds of data quickly and efficiently.

Technical options for managing claims continue to grow, and with it the opportunity to incorporate analytics into claims management. Whether by optimising allocations across the repairer network, streamlining processes or automating customer updates, this will remain an area of continued investment.

A (cautious) fleet of possibility

Underwriting of commercial lines continues to evolve, including Commercial Motor. While profit margins can't hope to reach the heights achieved in the pandemic, the market continues to grow, with GWP for the six months to June 2024 40% higher than two years before. This includes continuing growth in the number of policies written and suggests the delivery economy continues to expand. This creates opportunities for insurers, who are seeking greater understanding of driving patterns and risks for different types of fleets. However, increased use of personalisation and risk adjustment means businesses will have more incentive to shop around and so high profits are not guaranteed.

Focus on customer expectations



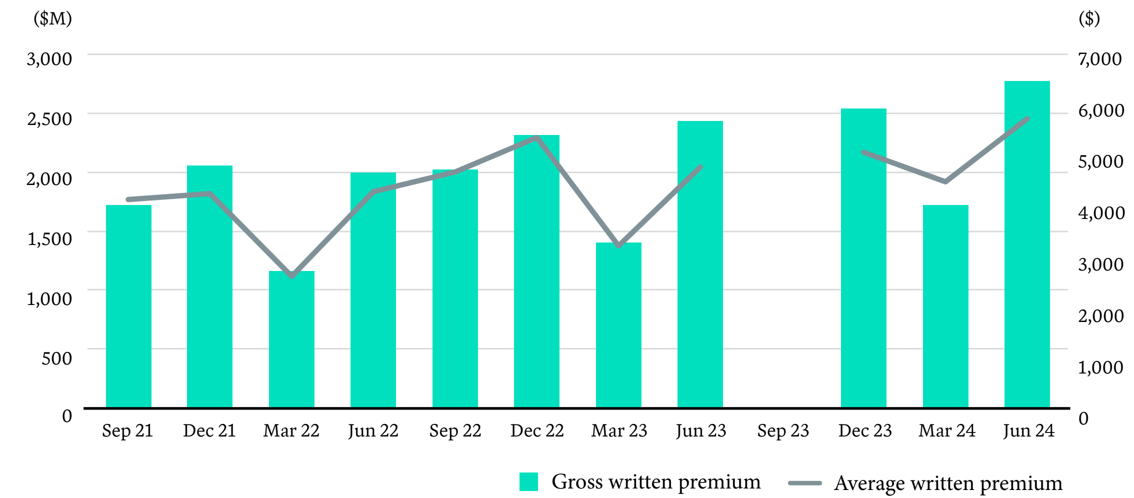
Successive price rises have put customers on high alert. This means a higher sensitivity to repair delays, poor service, broken price promises or adverse claim decisions. Record complaint levels to the Australian Financial Complaints Authority (with particularly large growth in motor) suggest insurers are struggling to meet these expectations.

Commercial Property

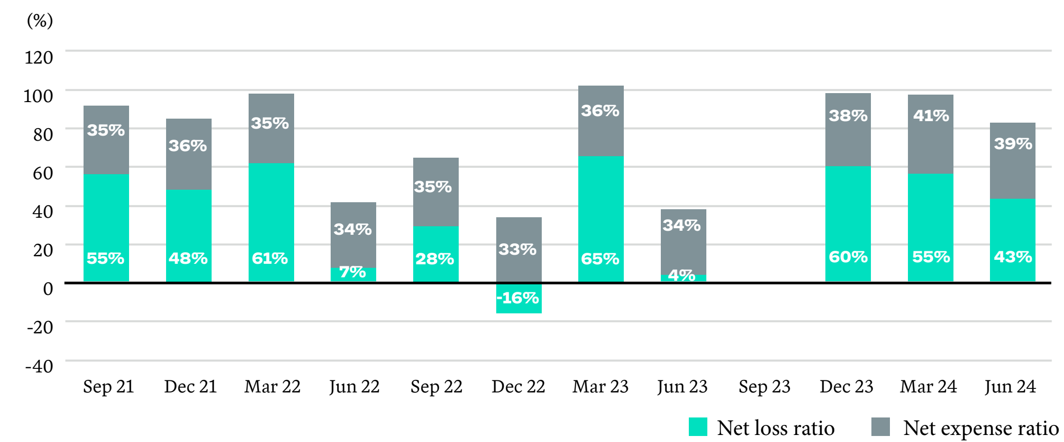
A combination of inflation, natural peril risks and evolving reinsurance capacity are shaping market conditions for Commercial Property. The class has seen a sharp year-on-year rise in premiums, largely driven by inflationary pressures. Premium increases are tracking around 15% year on year in the latest available data, in line with the high rate of increase in the past couple of years.

This mirrors the increases observed in domestic property insurance, but the commercial sector has managed to maintain better overall profitability with combined ratios sitting below 100% and gross loss ratios under 50%.

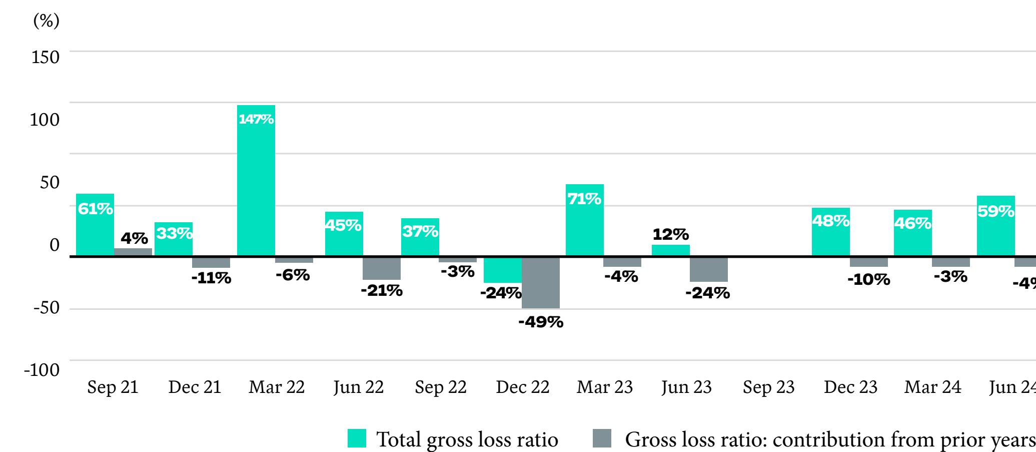
Gross written premium | Reporting quarter



Net combined ratio | Reporting quarter



Total gross loss ratio and contribution from prior years



The insurance cycle ... appears to be entering a more favourable phase, especially for reinsurance capacity.

Shared challenges with Householders

Like the domestic property insurance market, commercial insurers face several common challenges:

- **Fire claims** – The rising prevalence of fire claims, particularly those caused by lithium battery fires, poses a growing concern. Commercial properties with extensive electronics or stored battery-powered goods face higher risks, increasing the frequency and severity of fire-related claims.
- **Natural peril risks** – As climate change continues to drive more volatile extreme weather events, commercial properties are also vulnerable to natural disasters such as floods, storms and bushfires. This has led to higher premiums and more stringent underwriting criteria for businesses in high-risk locations.
- **Inflation** – The broader inflationary environment, affecting building materials and labour costs, continues to impact claims expenses. For commercial properties, underinsurance has become a critical issue. Property valuations often fail to keep pace with rising replacement costs and this leads to significant coverage gaps.

Turning insurance cycle

To more commercial-specific trends, the insurance cycle for this class appears to be entering a more favourable phase, especially for reinsurance capacity. Reports indicate reinsurers are increasing their capacity for Asia-Pacific commercial property risks, which should help place downward pressure on premiums. While the market remains relatively hard, these shifts in the reinsurance landscape may signal a moderation in future rate increases, especially for property catastrophe reinsurance.

Business interruption

In 2021 and 2022, the legal resolutions of business interruption (BI) test cases related to COVID-19 BI claims allowed insurers and policyholders to move forward, although complaints continue to be addressed through the Australian Financial Complaints Authority (AFCA).

By early 2024, AFCA resolved 62% of COVID-19-related BI complaints, with 161 complaints remaining open, 110 of which were on hold because they could be affected by class actions still pending in the Federal Court. These class actions began in 2021 and targeted insurers including QBE and IAG. Considering the outcomes of the test cases, the insurers involved made applications to the Federal Court that the class actions be declassed, meaning the actions stop being class actions and proceed as individual claims. In September 2024, the Federal Court handed down judgment substantially agreeing with the insurers and stating an intention to declass the representative proceedings. As such, it's likely many group members and registrants will opt out due to the time and fees involved in pursuing individual actions.

Inflation and underinsurance

With significant inflationary trends over the past year, many commercial properties may be underinsured. This gap between insured values and actual replacement costs is a growing concern, as underinsurance can result in insufficient claims payouts during major losses. Ensuring valuations accurately reflect the current market is crucial for businesses to maintain adequate coverage.

Risks of long-term office vacancies

The office sector, particularly in central business districts, continues to face elevated vacancy rates. The ongoing shift toward hybrid work has reduced demand for office space, creating long-term vacancies in many urban centres. For insurers, this presents a unique risk. Properties that remain vacant are more likely to suffer from deferred maintenance, increasing the risk of claims related to property damage, theft or even fire. Insurers may respond by tightening underwriting for vacant office buildings or increasing premiums for properties in areas with high vacancy rates.

Beyond the horizon

The Australian commercial property insurance market in FY2024 experienced a challenging, yet more stable environment compared to its domestic counterpart. While premiums have continued to rise, profitability remains strong, partly due to disciplined underwriting and increasing reinsurance capacity. However, common challenges such as fire risks, inflation and natural disasters continue to shape the outlook for the market. As the reinsurance cycle turns, businesses may begin to see some relief in premium rates, but the risk of underinsurance and volatile natural peril impacts will remain critical areas for insurers and policyholders alike.

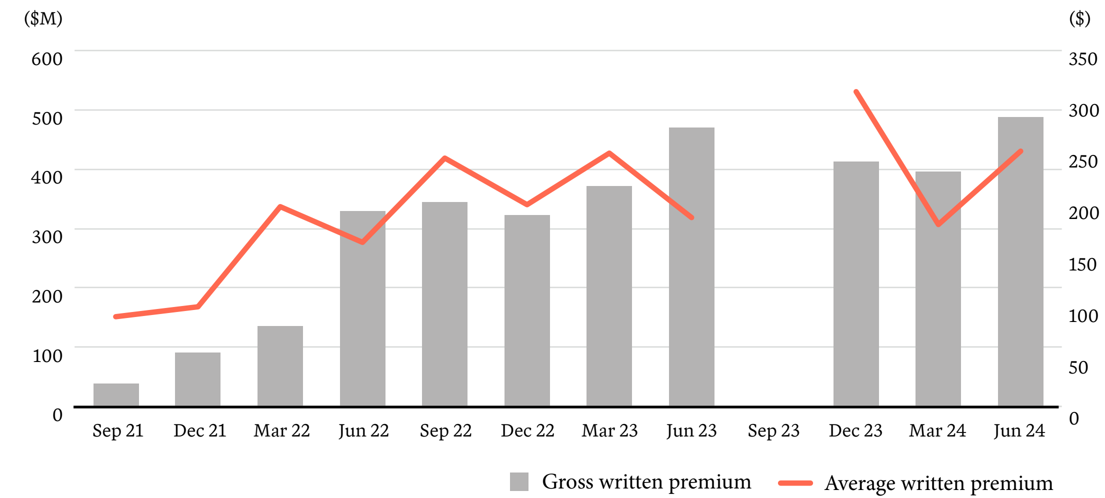
Travel

The travel insurance market has well and truly shaken off COVID-19. Monthly outbound travel volumes are now at pre-pandemic levels – with total premium volume and average written premium continuing to track at higher levels than before the pandemic.

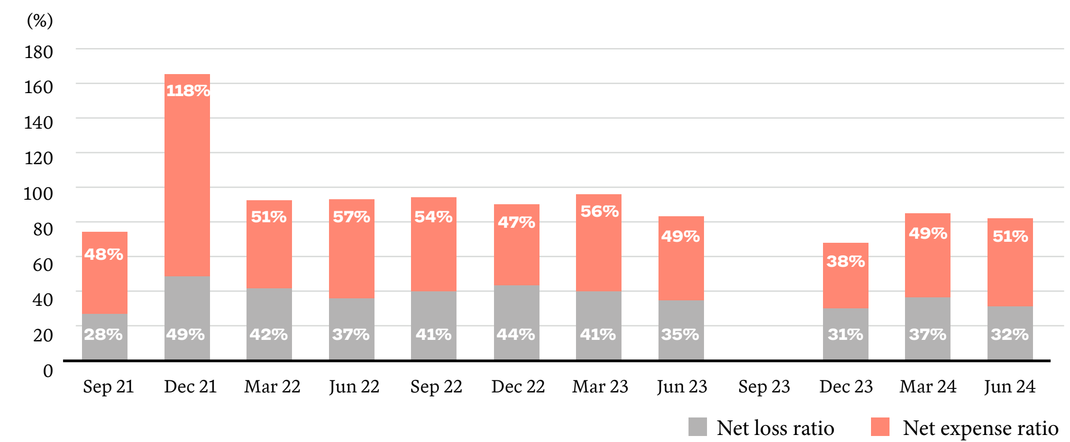
In fact, gross written premium (GWP) in the six months to 31 March 2024 was 40% higher than GWP in the six months to 31 March 2020, while average written premium was 50% higher for these same periods. GWP in the quarter ending 30 June 2024 was also the highest on record, and 4% higher than the 30 June 2023 quarter. The claims environment over the year has also been benign, with no high-profile catastrophe events impacting the industry, and combined ratios tracking lower this year (averaging 79% over the three most recent quarters) compared to 90% at the same time last year.

Travel insurance has also benefitted from the favourable reinsurance renewal season in FY2024. With international travel growing around 5% per annum in the years before COVID-19, travel insurers will be watching closely for a return of this trend.

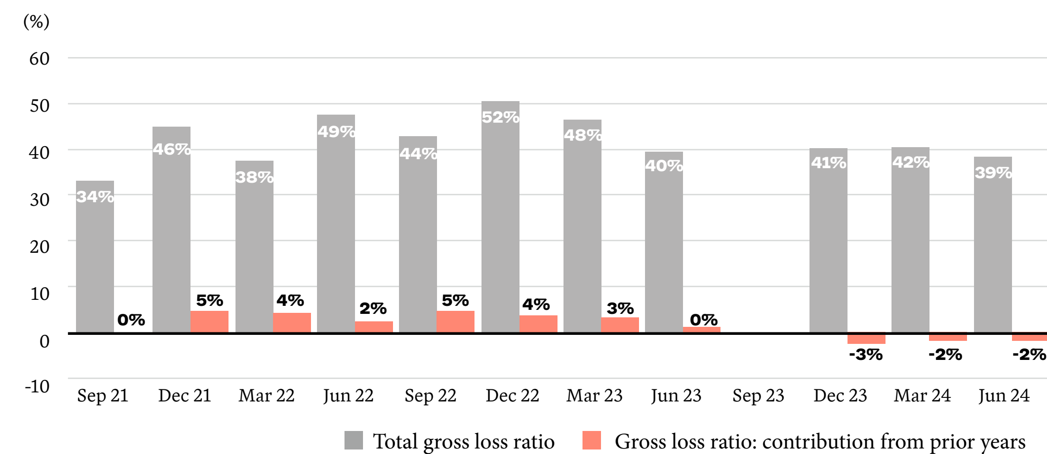
Gross written premium | Reporting quarter



Net combined ratio | Reporting quarter



Total gross loss ratio and contribution from prior years



A focus on growth rather than profitability is trending ... Some market participants are either considering or have implemented rate reductions to achieve increased market share.

Competing forces

Competition has been ramping up across the year, too. The entrance of Italian insurer Generali Group into the market via its acquisition of the Flight Centre account will add to the competitive dynamics of Australian travel insurance. Previously, the account was held for decades by Cover-More, part of Zurich Insurance Group. Flight Centre reached the new deal with Europ Assistance, a subsidiary of Generali, Europe's third largest insurer.

In addition, new entrants have been competing for a foothold in the industry, tailoring their offerings and marketing themselves to target specific segments of the market. These strategies include appealing to younger travellers or travellers that value only medical cover, accompanied by high spend on branding and social media engagement.

With rate increases now providing sufficient coverage of claims costs, a focus on growth rather than profitability is trending in the travel insurance industry. Some market participants are either considering or have implemented rate reductions to achieve increased market share, and are looking at different channels of distribution in response to evolving consumer trends.

More clarity for customers over exclusions

In May 2024, a survey of policyholders co-commissioned by the Department of Foreign Affairs and Trade and the Insurance Council of Australia revealed a general lack of understanding of exclusions embedded within travel insurance policies. Further, a majority of those surveyed had a poor understanding that exclusions may apply following events such as natural disasters and terrorism. This suggests some improvement is needed to establish clarity for customers. With climate change a potential contributor to previously unheard-of events (e.g. the flooding of Auckland Airport last year, increasing frequency of serious turbulence events during air travel), and a highly uncertain geopolitical landscape (e.g. conflicts in the Middle East and the Caucasus), customer understanding of these exclusions is key, particularly as:

- The systemic nature of these events can affect many travel customers for an insurer
- Customers exposed to these events would typically be in a vulnerable position and require extensive support.

Tailoring key amid cost-of-living crisis

Affordability of travel insurance should also be a key consideration for insurers this year, with rate increases occurring amid increased cost-of-living pressures. It will be important for insurers to emphasise the critical role of insurance in seeing travellers home in a crisis.

Know your customer and make it easy

A key factor for success in this increasingly competitive market is ensuring products offered are:

- Customised to the characteristics of the individual traveller
- Marketed and distributed in a targeted way
- Easy to understand and purchase, with minimal frictional costs, while product features and exclusions are set out simply and clearly.

The future of travel as our climate changes

Looking forward, insurers will need to consider the changing nature of travel and how a warming planet affects customer needs, for example:

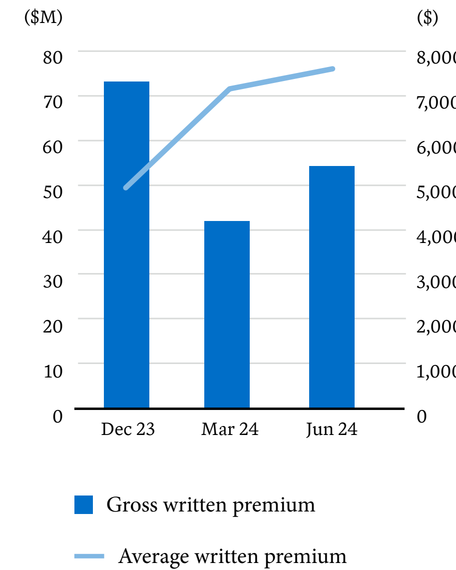
- The increasing intensity of climate-related weather events may see customers place greater value on the protection insurance provides
- Action to curb greenhouse gas emissions (e.g. Denmark is implementing a flight tax from 2025) may put overseas trips financially out of reach for some policyholders
- Segments of travellers may eschew international travel due to the emissions intensity of aviation.

Future-focused insurers will be assessing their resilience against different emissions and government climate policy settings.

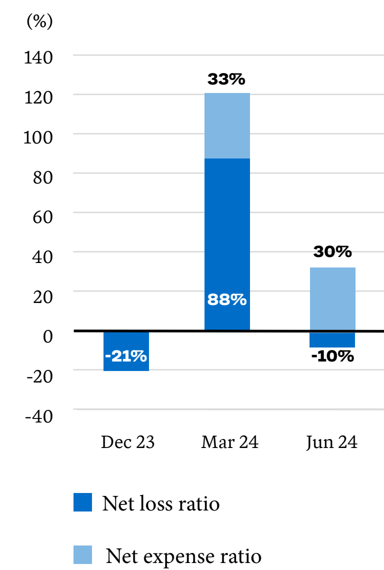
Cyber

High-profile cyber incidents impacting millions of Australians dominated headlines in 2022 and 2023, while the industry experienced poorer claims experience and skyrocketing premiums. This year, more benign claims experience, tighter cyber controls (spurred by increased awareness and regulatory scrutiny), and additional capacity have led to a softening market. Headwinds on the horizon include the threat of accumulation risk from a large-scale, catastrophic global cyber incident.

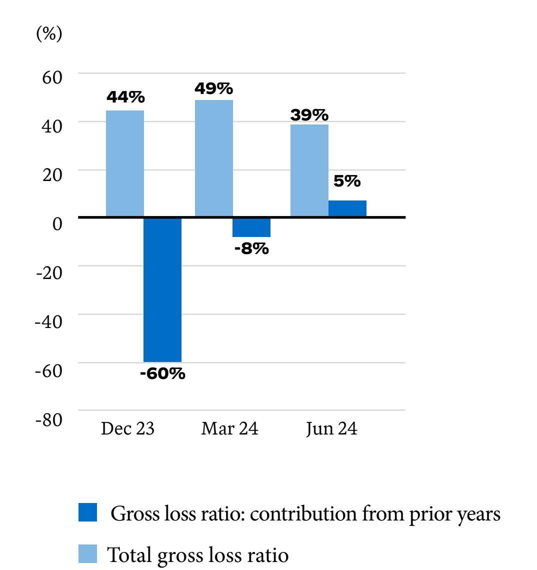
Gross written premium
Reporting quarter



Net combined ratio
Reporting quarter



Total gross loss ratio and contribution from prior years



Crime a top concern for boards and government

Cyber security concerns have loomed large in corporate Australia over the past couple of years. According to the Australian Institute of Company Directors half yearly directors sentiment survey, cybercrime and data security have consistently been the top issue 'keeping directors awake at night' since the first half of 2021. Joe Longo, chair of the nation's corporate regulator, the Australian Securities and Investments Commission, said in November 2023 that "cyber security and cyber resilience must be a top priority" for all organisations.

Cyber has also been top of mind for regulators and policymakers, with a flurry of activity, including increased fines for poor cyber controls, new obligations for providing 'critical infrastructure' and a brand-new cyber security strategy for the nation. In recognition of the unique insight the insurance industry offers on what occurs during a cyber incident, insurers have been increasingly consulted on cyber initiatives, including the cross-border Counter Ransomware Initiative – a US-led project established in 2021 to combat the growing threat of ransomware.

In recognition of the unique insight the insurance industry offers on what occurs during a cyber incident, insurers have been increasingly consulted on cyber initiatives ... [but] convincing cash-strapped SMEs during a cost-of-living crisis to purchase cyber insurance remains an ongoing challenge.

Premiums, capacity and an SME challenge

Businesses looking to incorporate cyber insurance as part of their cyber toolkit experienced fast-growing premiums and low policy limits over 2022 and early 2023, but more recently market conditions have improved. Premiums for this class have stabilised (and in some cases reduced), while overall cyber market capacity has increased.

Recent new entrants to the Australian cyber insurance market include US cyber specialist Coalition (November 2023), IAG's underwriting agency Cylo (May 2024), and HDI Global (June 2024). Much of the focus of new entrants has been on the small and medium enterprise (SME) market, with estimates of take-up about 20%. Convincing cash-strapped SMEs during a cost-of-living crisis to purchase cyber insurance remains an ongoing challenge. The industry also still has a way to go to convince SMEs of the benefits of a relatively new and rapidly evolving insurance product.

Rising third-party costs?

To date, most of the cyber claims in the Australian market have been for first-party costs. Concerns remain in the industry – especially from more established market players – about the potential for rising third-party costs. The increased regulatory focus on cyber controls and cyber risk across entities' supply chains, as well as expected changes under the Privacy Act (including the introduction of a direct right of action), suggest we're likely to see more class-action activity in Australia over the coming years.

Malicious potential

Accumulation risk remains a looming threat. The CrowdStrike outage in July 2024 is certainly a reminder of the potential for a malicious cyber incident to disrupt the economy at large, despite the event not causing wide-scale losses for the global cyber insurance industry. Estimates of loss resulting from the outage around the world are between $300 million to $1.5 billion, due to policy coverage terms and waiting periods.

In response to some industry leaders suggesting cyber threats may become uninsurable, calls have grown across various jurisdictions to explore public-private collaboration to mitigate for large-scale losses.

A maturing class

Reflecting the maturity of this line of business, APRA published general insurance statistics for Cyber for the first time this year. With only three-quarters of data to June 2024, we believe it's far too early to draw any definitive conclusions on the non-Lloyd's cyber market, but some initial statistics include:

- **Gross written premium** – $168 million (three quarters), and we expect the annual figure will be around $250 million
- **Gross loss ratios** – 45% (three quarters), driven in large part by reserve releases from prior periods
- **Number of risks** – 38,000 (three quarters), resulting in an average gross written premium of $5,400, noting the larger risks are mostly underwritten by Lloyd's.

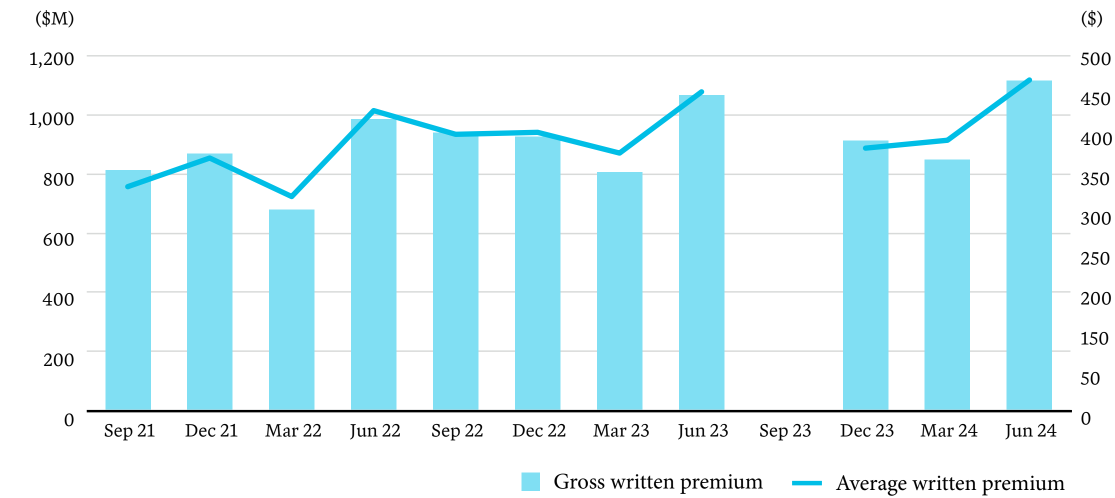
Each new quarter's data release will provide the industry with more insight – so watch this space!

Public liability

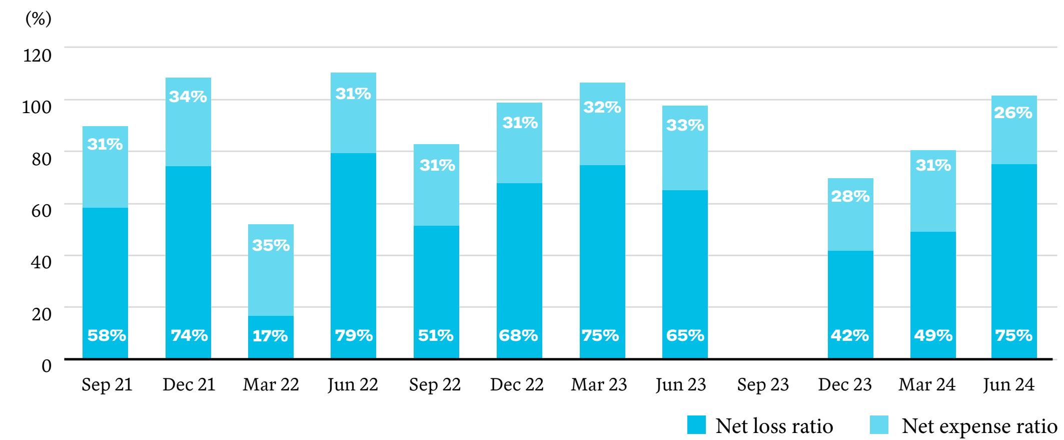
Headline profitability for Public Liability has been reasonable, with insurers reporting an overall 84% net combined ratio for the nine months to June 2024. Despite this, specific risk factors have resulted in isolated sectors of the market (including the recreational, construction and youth care sectors) being less attractive to insurers due to adverse claims and perceived risk management deficiencies. For relevant sectors, insurers have responded by pushing up premiums, offering more restrictive terms or, as a last resort, withdrawing from the market.

Given public liability insurance is often a legal requirement, businesses have at times felt compelled to consider alternative options (such as discretionary mutual funds), where traditional insurance cover isn't readily available. It's crucial businesses looking at options carefully consider the pros and cons of the alternative cover. For their part, insurers maintain that appropriate risk management and mitigation is the key to businesses being able to sustainably secure affordable public liability insurance.

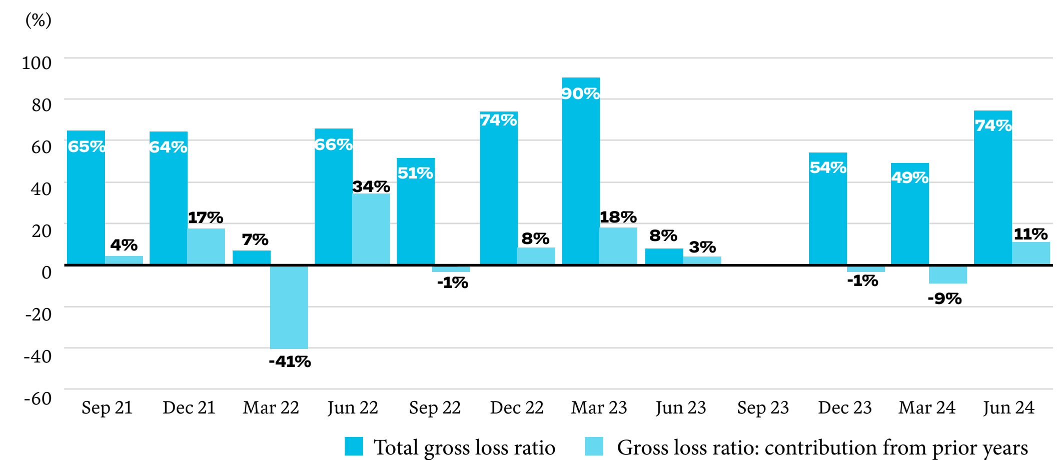
Gross written premium | Reporting quarter



Net combined ratio | Reporting quarter



Total gross loss ratio and contribution from prior years



It's crucial businesses looking at options [to traditional insurance] carefully consider the pros and cons of the alternative cover.

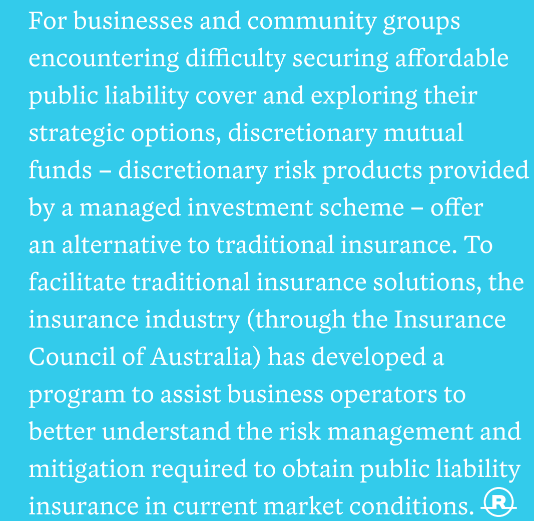
Affordability and availability a continuing concern

For certain sectors of the economy, affordability and availability of public liability insurance continues to be an area of concern. In particular, businesses operating within the amusement, leisure and recreation industries are experiencing significant increases in premium, as well as deteriorating terms and conditions of cover. Similarly, businesses operating within the construction industry have experienced premium increases as insurers respond to a deteriorating claims environment and perceived risk management deficiencies.

The widespread use of labour-hire companies in the construction industry has exacerbated the adverse claims environment, with 'worker to worker' claims (which arise when subcontractors and labour-hire employees are injured at work) at an average size more than double other bodily injury claims.

Sexual abuse liability claims remain high

Ultimately, this can be traced back to the Royal Commission into Institutional Responses to Child Sexual Abuse, which released its final report in 2017. Following the royal commission, greater focus was placed on the risk management obligations of institutions involved in caring for children. Claims activity for the National Redress Scheme (established in response to the Royal Commission) continues to accelerate, with more than 15,000 claims received by the scheme over the year to June 2024, compared to about 11,000 claims received for the prior year. As a result of the increased frequency and size of abuse claims, several insurers have withdrawn from the market, negatively affecting the ability of foster care and youth homelessness services providers to secure much needed insurance coverage.



Help at hand to improve traditional insurance uptake

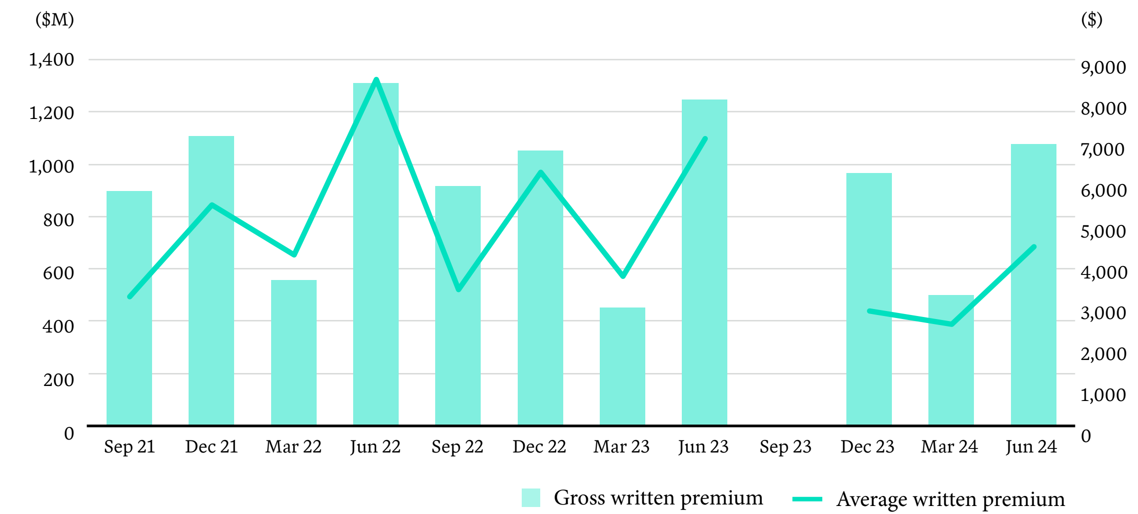
For businesses and community groups encountering difficulty securing affordable public liability cover and exploring their strategic options, discretionary mutual funds – discretionary risk products provided by a managed investment scheme – offer an alternative to traditional insurance. To facilitate traditional insurance solutions, the insurance industry (through the Insurance Council of Australia) has developed a program to assist business operators to better understand the risk management and mitigation required to obtain public liability insurance in current market conditions.

Professional Indemnity & Directors and Officers

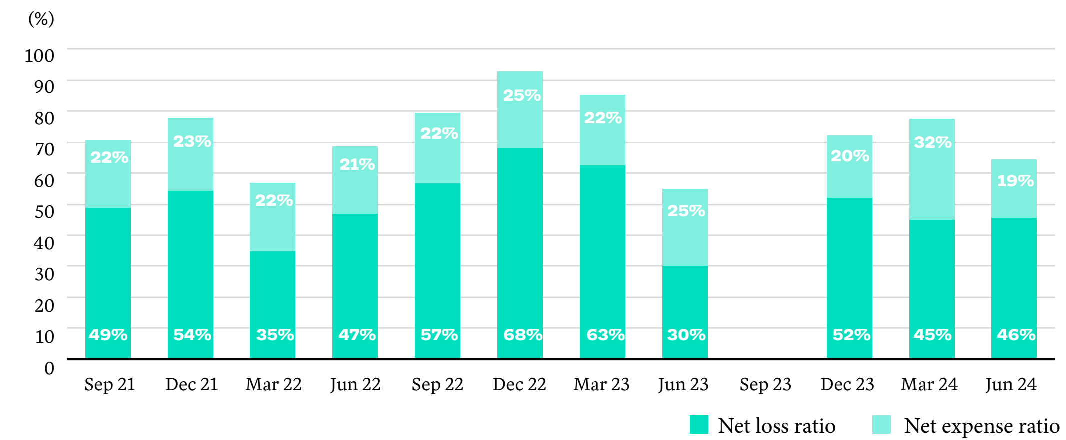
Reserve releases from prior years underpin the 2024 insurance service result. Over the nine months to 30 June 2024, the insurance service result was $507 million, up from $406 million over the same period last year.

Class action promoters continue to pursue a broad range of claims. While class-action filings over the six months to 30 June 2024 were below average, experience to September 2024 suggests this was a temporary reprieve. Litigation funders continue to view Australia as a receptive jurisdiction and – combined with the ability for plaintiff lawyers to obtain contingency fees in class-action proceedings filed in the Federal Court and in some states – class actions remain a prominent feature of Australia's legal landscape. We expect this to continue unless a change of government occurs next year, bringing with it tighter requirements for litigation funders, similar to those introduced in 2020 by the previous Morrison Government but later wound back by Labor.

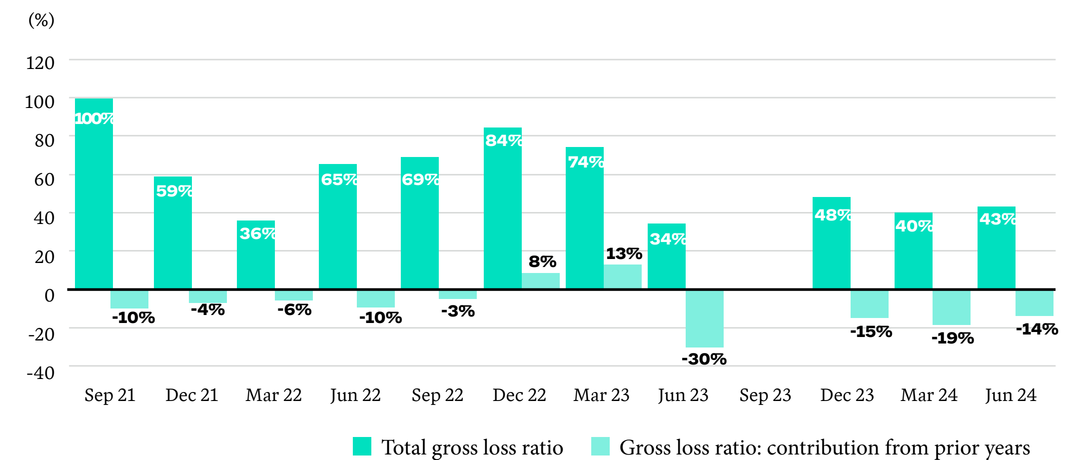
Gross written premium | Reporting quarter



Net combined ratio | Reporting quarter



Total gross loss ratio and contribution from prior years



Just as silent cyber led to unanticipated cyber-related losses for traditional lines of business, left unaddressed, silent AI has the potential to generate unanticipated AI-related losses.

Big premium reductions in D&O

For directors and officers insurance, an increase in capacity has placed downwards pressure on rates, with premium reductions of up to 30% reported. This recent experience contrasts starkly against the premium rate increases and restrictions on cover in place just a few years ago. Defence cost sub-limits remain an area to watch, as legal costs in defending actions continue to grow.

Technology and patient rights top of mind

In Medical Indemnity, the healthcare landscape continues to evolve with a focus on new technology, patient-centred care and new modes of delivering healthcare. The Australian Health Practitioner Regulation Agency's attention on improving public safety has generated a greater awareness of patient rights. The latest quarterly statistics show an increase in notifications about medical practitioners. This has resulted in an uptick in regulatory matters, incurring legal costs, and is an area insurers will be watching closely. In line with previous years, nervous shock claims from dependants remain elevated but aren't increasing, which is good news for insurers.

Attention builds on risk selection

The construction industry is under pressure with insolvencies on the rise. Architects and engineers face greater scrutiny over building and fire safety defects. As a result, underwriters are focused strongly on risk selection. Appetite differs greatly by the type of construction, whether contracts cover design risk vs build risk only and whether in-house or external design teams are used. We expect this heightened risk focus to continue into 2025.

Outlook for PI insurers

Looking ahead, insurers are focusing on ...

- **Data security** – Cyber and data-breach class actions present a material risk. The federal government has agreed in principle that individuals should have more direct access to the courts to seek remedies for breaches of the Privacy Act through a direct right of action. This would enable people to seek compensation, if they suffer loss or damage through a breach of their privacy. We expect this change will impact all businesses that collect, hold and use personal information.
- **Technology and fraud** – Large language models present a terrific opportunity to improve efficiency, but they also present new sources of claims. No model is perfect. For example, a lawyer's use of artificial intelligence (AI) to prepare a briefing could result in significant errors and adverse outcomes for the client. Furthermore, fraud is on the rise, supported by this new technology. In telehealth, deepfake means it may be difficult for a patient to determine whether they're talking to an actual doctor.
- **Economic environment** – Despite high but moderating inflation, cost-of-living pressures and recent increases in the number of insolvencies, Australia has managed to avoid a broader economic downturn. Insurers are focused on the financial services sector, particularly if the economic environment deteriorates. What we have learned from past downturns is that financial planners, accountants and lawyers typically come under pressure when people incur losses.

How insurers are preparing

Insurers are reviewing their policy wording and considering their exposure to 'silent AI'. Just as silent cyber led to unanticipated cyber-related losses for traditional lines of business, left unaddressed, silent AI has the potential to generate unanticipated AI-related losses.

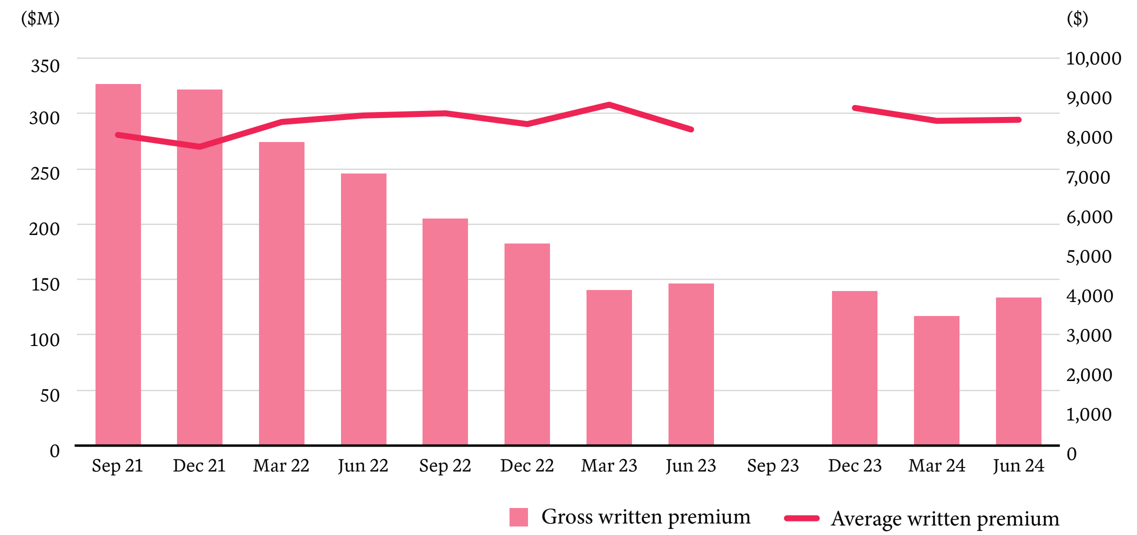
A greater focus on risk selection is evident across the board, with close examination of individual past claims experience and type of activity.

Insurers are investing to lift pricing sophistication. As capability and capacity improves, investment in pricing is seen as key for insurers to achieve profitable and sustainable growth.

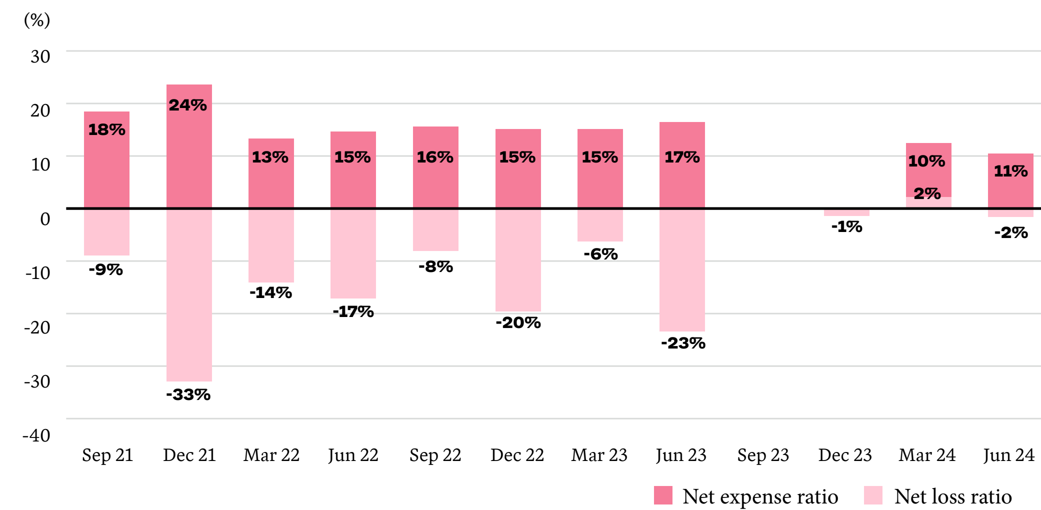
Lenders Mortgage Insurance

Lenders mortgage insurers have enjoyed favourable claims experience in recent years, benefitting from the advantageous economic environment and strong property prices. However, mortgage defaults (a lead indicator for lenders mortgage insurance claims) have started to rise, driven by the effect of rising interest rates, particularly as borrowers switch to variable-rate loans once fixed-rate arrangements expire.

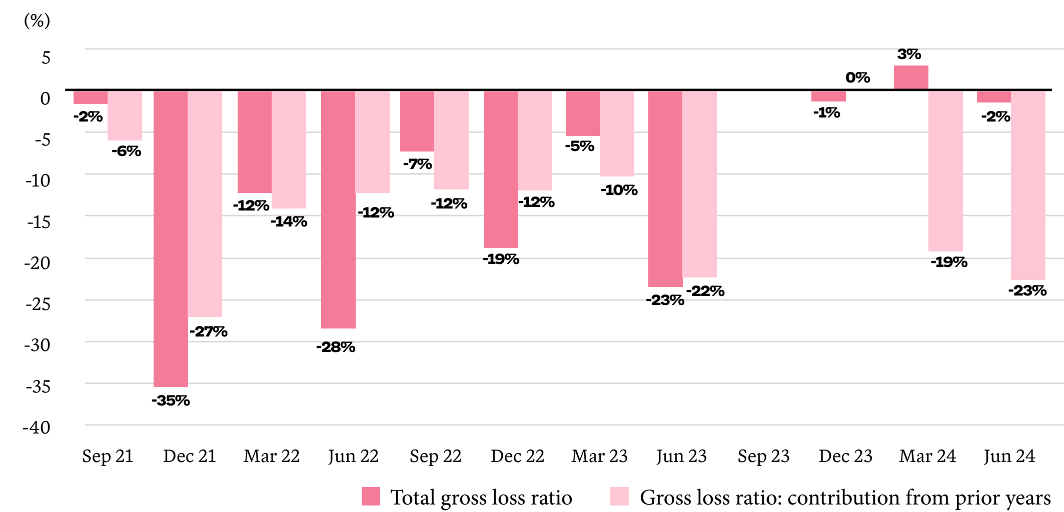
Gross written premium | Reporting quarter



Net combined ratio | Reporting quarter



Total gross loss ratio and contribution from prior years



Ultimately, the outlook for lenders mortgage insurers will depend heavily on the unemployment rate, as borrowers typically continue to make repayments if they have a job.

Another impact of rising interest rates is a decline in the rate of advance payments (which provide a safety buffer for lenders mortgage insurers) borrowers are making on their loans. This increases the risk of further loan defaults, which may in turn see a spike in lenders mortgage insurance claims towards the end of 2024 and in 2025.

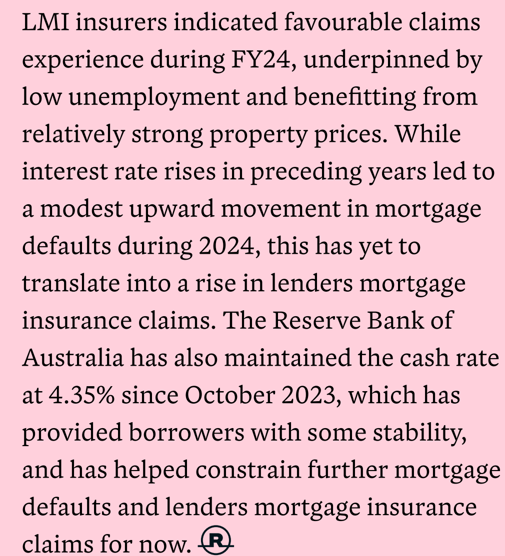
Ultimately, the outlook for lenders mortgage insurers will depend heavily on the unemployment rate, as borrowers typically continue to make repayments if they have a job. Importantly, the unemployment rate was 4.1% at June 2024 (up from 3.5% over the prior year), with further modest increases in unemployment expected over the remainder of 2024. Given these figures – combined with the rise in mortgage defaults and associated risks – a corresponding rise in lenders mortgage insurance claims may indeed follow, especially if economic conditions deteriorate.

Tricky launch for new accounting standard

Implementation of AASB17 posed challenges, with the long-term nature of lenders mortgage insurance necessitating the use of complex general measurement models (GMM) to measure insurance contract liabilities. The extended earning patterns for premium and profit under the GMM resulted in most lenders mortgage insurers experiencing a one-off contraction in retained earning balances on transition to AASB17, which may also have negatively impacted capacity to pay dividends.

Safeguard against rising defaults

As fixed-rate arrangements expired, borrowers felt the full force of interest rate hikes. A series of rate rises during 2022 and 2023 increased the risk of mortgage defaults, as borrowers on variable-rate loans were faced with sharp rises in loan repayments. However, back in October 2021, APRA increased the minimum interest rate buffer it expects banks to use when assessing the serviceability of home loan applications from 2.5% to 3%. This provided an extra layer of protection against rising defaults and claims for lenders mortgage insurers.



Claims stability, for now

LMI insurers indicated favourable claims experience during FY24, underpinned by low unemployment and benefitting from relatively strong property prices. While interest rate rises in preceding years led to a modest upward movement in mortgage defaults during 2024, this has yet to translate into a rise in lenders mortgage insurance claims. The Reserve Bank of Australia has also maintained the cash rate at 4.35% since October 2023, which has provided borrowers with some stability, and has helped constrain further mortgage defaults and lenders mortgage insurance claims for now.

Spotlight on Climate

Insuring the climate transition

To truly minimise the life-altering impacts of climate change, our world needs to transition to a low carbon economy. We explore what this means for insurers and the critical role they can play towards a sustainable future for us all.

The insurance industry and its stakeholders, understandably, tend to focus on the physical impacts of climate change – driven by devastating floods and bushfires across the country and made more likely by a warming climate. Cost-of-living pressures and concerns about rising premiums due to climate change are adding to the burden on Australians.

While the Senate resolved in May to establish a Select Committee on the Impact of Climate Risk on Insurance Premiums and Availability, managing the physical impacts of climate change is only part of the solution. Minimising the effects of climate change is key and to do this the world must transition to a low carbon economy. How? Among urgent global actions, we must expand the production of renewable energy, electrify everything from transport to residential energy use to manufacturing, and reduce emissions using public and active modes of transport.

New opportunity for insurers

In 2021, the Net Zero Insurance Alliance (NZIA) launched, in recognition of insurers as facilitators of risk and economic activity, and their crucial role in managing the transition to a low carbon future. At its peak, the NZIA had about 30 members, each committing to transition their underwriting portfolios to net-zero greenhouse gas (GHG) emissions by 2050 and publicly reporting their progress annually.

Last year, following a United States Republican-led backlash against Environmental, Social and Governance investment, including claims the Alliance could be violating anti-trust laws, members steadily began leaving the Alliance. The breakdown of the NZIA caused concerns about how insurers would now progress against net-zero goals.

Enter April this year, when a successor to the NZIA was born – the UN-led and convened Forum for Insurance Transition to Net Zero (FIT). FIT established *"a new structured dialogue and multistakeholder forum to support the necessary acceleration and scaling up of voluntary climate action by the insurance industry and key stakeholders".*

Learning from the challenges of the NZIA, the FIT will seek input from consultation groups, and its work will be guided by a team of legal experts on antitrust and competition laws, sustainability, insurance and finance. Australian insurer IAG is one of the founding members.

Closer to home

Locally, insurers wanting to play their part, and/or minimise potential reputational risks associated with backing the status quo, can take their lead from the Insurance Council of Australia's (ICA) Climate Change Roadmap. This roadmap, first launched in 2022, provides guidance for ICA members on their potential role in the decarbonisation of the Australian economy.

In 2023, the ICA surveyed a cross-section of its members (representing more than $48 billion in gross written premium). More than 85% of respondents had set organisation-wide net-zero targets by 2050 or earlier, with more than 60% also having set interim targets.

Australia's largest insurers have been disclosing their climate change targets and transition goals using the recommendations of the Taskforce for Climate-related Financial Disclosures (TCFD) for several years, and it's a helpful reference for the insurance industry generally. In the following table, we summarise these insurers' latest publicly available targets and commitments.

Insurer	Scope 1 & 2 emissions* target	Scope 3* (Underwriting)	Scope 3* (Investments)	Investments in the transition	Other transition highlights
IAG	Net zero by 2030	▪ Working to improve data maturity and understanding of insurance-associated emissions baseline – continuing to test and refine its approach to reducing these emissions ▪ Working on ways to identify, assess and integrate climate resilience, decarbonisation, and other sustainability criteria, into its underwriting decisions, guided by its commitment to the UN Principles for Sustainable Insurance	▪ Target to reduce scope 1 and 2 normalised carbon footprint and weighted average carbon intensity for Australian and Global listed equity investment mandates by 25% by 2025 and 50% by 2030 versus 2020 relevant index level baselines ▪ Planning to update its investment emissions interim targets in FY25 to reflect the latest advancements in climate science and responsible investing	▪ $200 million investment in green bonds ▪ Firemark Ventures (IAG's corporate venture capital arm) is actively considering investments in the climate technology sector to support its climate goals	▪ Founding partner of the FIT ▪ Partners with the Aboriginal Carbon Foundation
Suncorp	Net zero by 2030	▪ Limits exposure to thermal coal extraction and generation, oil & gas exploration and production – with an exemption for companies with businesses consistent with net zero by 2050 ▪ Will release a Climate Transition Plan in FY25 that details interim 2030 commitments for relevant portfolios	▪ Limits exposure to thermal coal extraction and generation, oil & gas exploration and production – with an exemption for companies with businesses consistent with net zero by 2050 ▪ Will release a Climate Transition Plan in FY25 that details interim 2030 commitments for relevant portfolios	▪ Targets 5% of shareholder funds invested in social and low carbon impact investments ▪ Invested in four impact investments (including low carbon assets e.g. energy infrastructure and energy-efficient real estate) ▪ Purchases green bonds	▪ Launched the Suncorp Climate School to promote climate transition and improve climate literacy across the Suncorp Group ▪ Partnered with the Australian Collision Industry Alliance, a national not-for-profit dedicated to advocating for careers in collision repair to ensure industry sustainability
Allianz	Net zero by 2030	▪ Target of reduction of 45% emissions intensity in corporate property and casualty portfolio by 2030, reaching net zero by 2050 ▪ 30% reduction in absolute carbon emissions in motor retail portfolio (certain markets; does not include the Australian market) by 2030	▪ Target of a reduction of 50% in investment emissions by 2030, reaching net zero for proprietary investments by 2050	▪ Increase Climate Solutions investments by at least €20 billion from current level (€31 billion in 2023) until 2029	▪ Launched its inaugural Net Zero Transition Plan in September 2023 ▪ Board remuneration tied to achievement of climate targets
QBE	Net zero by 2030	• Committed to a net-zero underwriting portfolio by 2050	• Member of the Net Zero Owners Alliance, committed to transitioning its investment portfolio to net zero by 2050 • Prioritises engagement over divestment – for top 20 highest emitters in investment grade corporate credit portfolio, focused on challenging them to set short-, medium-, and long-term science-based emissions reduction goals	• In 2023, invested $117 million in green bonds • Reducing equity carbon emissions by moving from passive strategies to tailored mandates with external developed market equity managers	• First insurer in Australian market to offer policies with 'cradle to grave' coverage across renewable energy product lifecycle

**Scope 1* are direct GHG emissions that occur from sources that are owned or controlled by the company (e.g. emissions from combustion in owned or controlled vehicles).*
**Scope 2* are emissions from the generation of purchased electricity consumed by the company. **Scope 3* are all other indirect emissions.*

Sources: IAG, QBE, Suncorp, Allianz (Sustainability Report 2023; Inaugural Net Zero Transition Plan).

Increasing scrutiny of transition activities

The expectations on the rest of the industry to disclose their activities towards reducing carbon emissions will likely increase, with the introduction of mandatory climate-related reporting legislation being passed by Parliament in September. With first disclosures commencing in 2025, the legislation includes transition-related disclosures on:

- **Scope 1, Scope 2 and Scope 3 emissions**
- Climate-related **transition plans** (which lays out the entity's targets, actions, or resources for its transition towards a lower emission economy, including actions to reduce its GHG emissions or adaptation activities to manage physical climate risks)
- **How the entity plans to achieve any climate-related targets**, including any GHG targets.

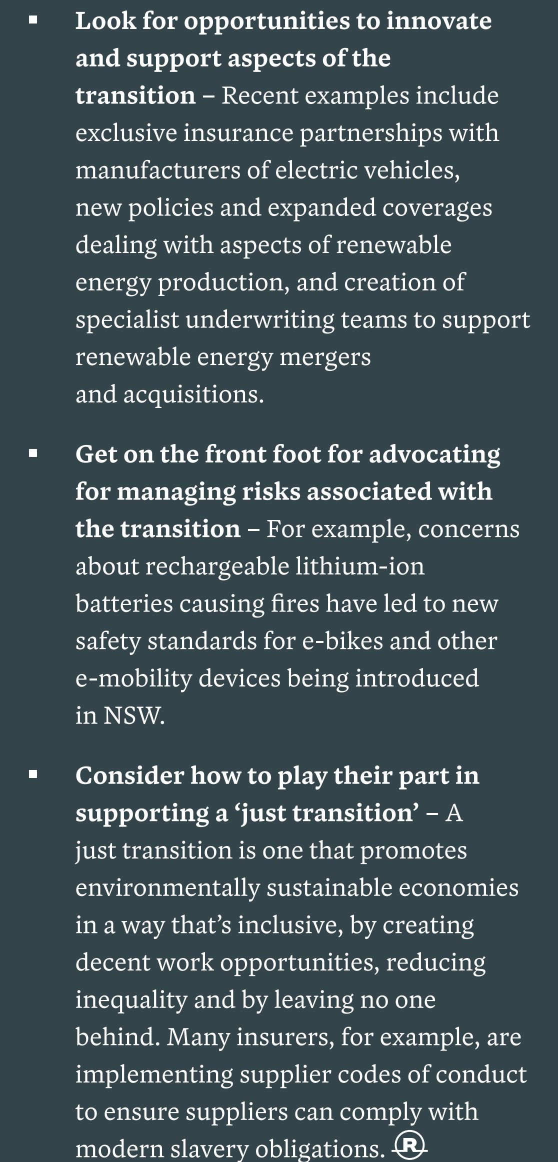
To support transition planning, the Treasury has committed to developing and publishing best-practice guidance on transition-plan disclosures before the end of 2025. Insurers wanting to get ahead of the curve can look to the guidance issued by the global Transition Plan Taskforce.

Watch out for ...

Upcoming policy and regulatory activity related to climate transition

- ASIC will soon be releasing guidance on mandatory climate-related disclosures. APRA's 2024-25 Corporate Plan (released in August 2024) notes APRA will be gradually increasing expectations for regulated entities to consider climate-related risk in financial decisions (including in underwriting and investing) and aligning them with emerging best practice globally.
- ASIC's 2024-25 Corporate Plan (also released in August 2024) notes the corporate watchdog will continue to undertake surveillance activity and take enforcement action where necessary to prevent harms from greenwashing (as well as other sustainable finance-related misconduct).
- The Australian Sustainable Finance Institute is partnering with the Australian Government to develop a sustainable finance taxonomy. A sustainable finance taxonomy is a set of definitions of economic activities and assets that contribute to key sustainability objectives. The initial taxonomy, due to be finalised by the end of this calendar year, will support mobilisation of private capital towards sustainable activities.

What happens now? A checklist for insurers



In addition to preparing for increased regulatory and stakeholder scrutiny, insurers can:

- **Look for opportunities to innovate and support aspects of the transition –** Recent examples include exclusive insurance partnerships with manufacturers of electric vehicles, new policies and expanded coverages dealing with aspects of renewable energy production, and creation of specialist underwriting teams to support renewable energy mergers and acquisitions.
- **Get on the front foot for advocating for managing risks associated with the transition –** For example, concerns about rechargeable lithium-ion batteries causing fires have led to new safety standards for e-bikes and other e-mobility devices being introduced in NSW.
- **Consider how to play their part in supporting a 'just transition' –** A just transition is one that promotes environmentally sustainable economies in a way that's inclusive, by creating decent work opportunities, reducing inequality and by leaving no one behind. Many insurers, for example, are implementing supplier codes of conduct to ensure suppliers can comply with modern slavery obligations.

Spotlight on affordability

Unlocking the price puzzle

One of the most urgent topics for insurers and their customers is the cost of insurance. Understandably, finding clarity and pragmatic solutions aren't easy tasks, especially amid the many voices on the subject. We break through the noise to draw out key ingredients towards a sustainable future.

Insurance affordability is, rightly, having a moment. The Department of Prime Minister and Cabinet is setting up a taskforce to explicitly study insurance affordability. The Australian Reinsurance Pool Corporation (ARPC) has released research showing the improved affordability for properties at risk of cyclone. State governments have been examining reducing levies on insurance to help improve affordability. The Insurance Council of Australia and the Actuaries Institute have each done work explicitly looking at affordability issues. The 2024 Australian Actuaries Home Insurance Affordability Index shows the proportion of households in insurance stress (premiums more than four weeks of income) growing from 12% to 15%. Even APRA is dipping its toe into affordability concerns. Executive Board Member Suzanne Smith noted recently, *"Our focus on financial stability … sees us increasingly uncomfortable with the widening insurance gap being created by declining availability and affordability."*

Affordability is affecting domestic lines in particular, such as home, contents and motor, but it's also having an impact in commercial insurance for SMEs.

A look back to move forward

Navigating a path towards affordable insurance requires an understanding of the factors that have led to the pressures. It's undoubtedly true that insurance prices have been climbing quickly. Insurance prices paid by households – as measured in the Consumer Price Index – have grown by more than 15% in the past year, the first time the CPI insurance component has been significantly above 10% for two decades. This is not only true for CPI (which tracks the price of insurance 'services') but also the Living Cost Indexes (which track gross premiums).

CPI insurance component – significantly above 10% for the first time in 20 years

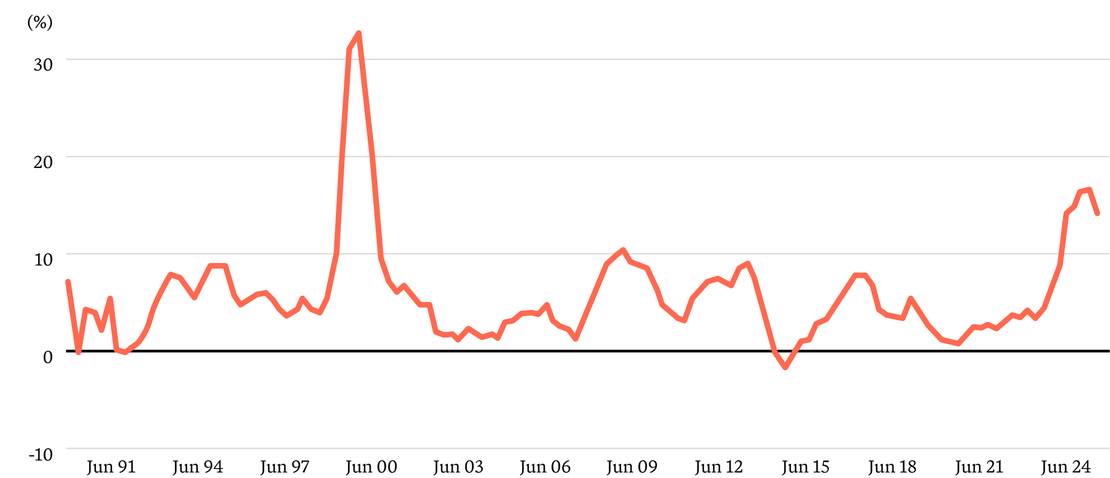


Chart source: ABS

In the past year, insurance prices paid by households have grown by more than 15%.

Drivers of these increases include:

- **High inflation for insurance input costs** – Home construction costs and car repair costs have seen rapid escalation. Increasing amounts of embedded technology, plus new challenges related to repair of electric vehicles are notable in motor.
- **Natural hazard risks have continued to increase** – This article does not have space to treat fully, but issues tied to each of frequency, severity and exposure are well documented.
- **Relatedly, reinsurance costs have seen a couple of years of price increases** – In some cases, reinsurance price rises have led to insurers taking on more risk themselves.

Finding context beyond the average price of insurance

Importantly, affordability is much broader than just looking at the average price of insurance.

Household budgets

Affordability must be viewed in the broader context of household budgets. The cost-of-living squeeze has reduced pandemic-related financial buffers, and households that don't own property are facing an extremely tight and expensive rental market. Changes such as the removal of emergency services levies on insurance doesn't automatically mean insurance is more affordable, given households will likely be levied in other ways (higher council rates, for example).

A change in spending behaviour?

A natural question is how affordability affects changes in coverage – the extent to which more people are forgoing insurance, removing coverage options or taking on exorbitant excesses. Evidence on this is mixed. Insurance tends to be a high-priority purchase (and indeed home insurance is typically mandated for mortgage-holders by lenders), so households may cut other goods and services first.

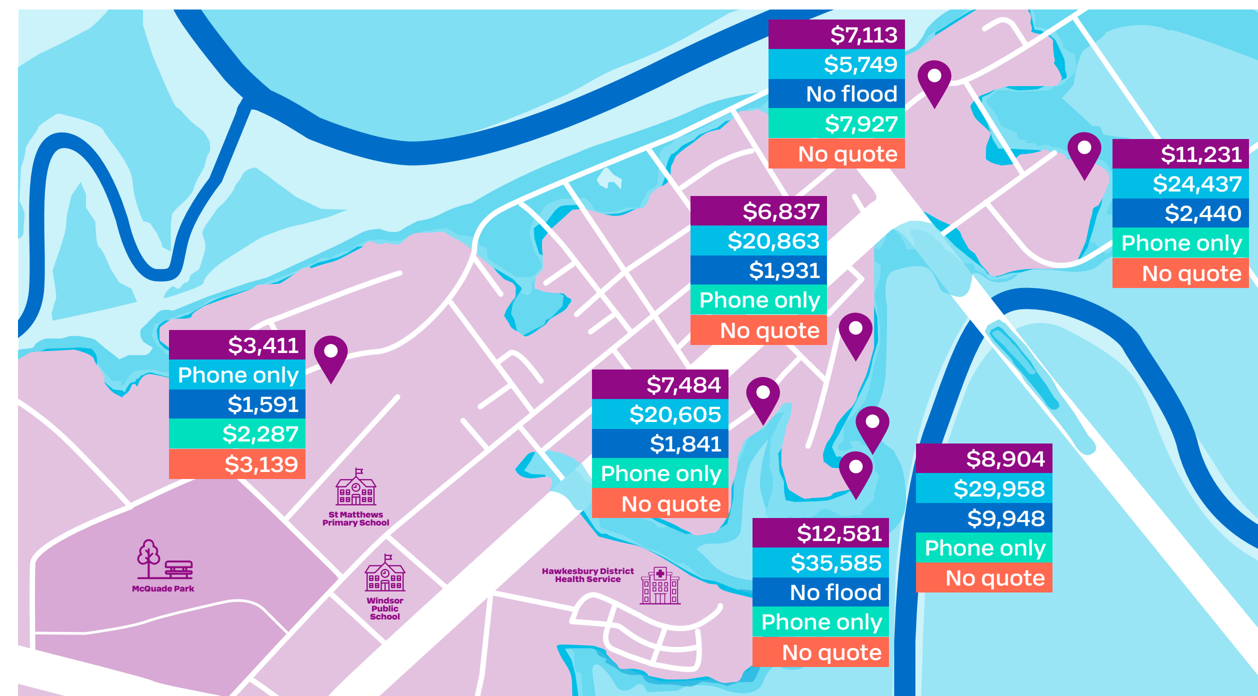
But the NAB consumer sentiment survey suggests steady increases in people changing their insurance spending decisions. Better industry data on coverage and related gaps will be important – it remains to be seen if data collections such as those at the ARPC can be used to inform such discussions.

Vulnerable groups

Average prices don't capture the full dynamics of insurance pricing for cohorts, particularly those with high natural hazards exposures. As individual-level pricing continues to develop, people with high-risk properties or poor risk records are seeing much larger increases. As pooling benefits reduce and natural hazard risk forms a greater share of total risk, vulnerable groups will see acute affordability challenges. These can be difficult to address without industry-level reform. Flood risk is a particular issue.

The image below shows variation in similar sum-insured costs for a basket of insurers within a single suburb (Windsor NSW, a commonly flooded suburb). The large variation shows the extent to which prices are highly personalised as well as differences in where insurance is offered. Even within a suburb, affordability isn't a simple question.

Insurance price offerings for selected houses in Windsor – Prices based on sum insured of $600k for building and $100k for contents



Map source: https://www.ses.nsw.gov.au/hawkesbury-nepean-floods

For each of the seven areas within Windsor, we consulted five insurers, each represented here by a separate colour.

Finding context beyond the average cost of insurance

If these are the puzzle pieces, what does it mean for the future? Happily, most experts believe the biggest increases are behind us. More capacity appears to be entering the reinsurance market, too, easing insurer pressures. But even if premium inflation drops to near zero, it still means high prices related to increases in the recent past will endure, as will interest in affordability.

Action by government

Government will be an active player in the process. The Parliamentary inquiry into insurers' responses to 2022 major floods claims reported in October this year and provides a suite of recommendations. While much of the report focuses on flood response and claims handling, it also proposes recommendations around affordability, including the funding of mitigation (and its recognition by insurers), and discusses the role of government-backed reinsurance arrangements.

The Insurance Affordability and Natural Hazards Risk Reduction Taskforce has also been recently established. With focus likely to be on natural hazards risk, this may span standardisation of definitions, targeting spending to reduce community risks as well as hazard risk reduction. Expansion of the ARPC cyclone reinsurance pool remains a possible policy response.

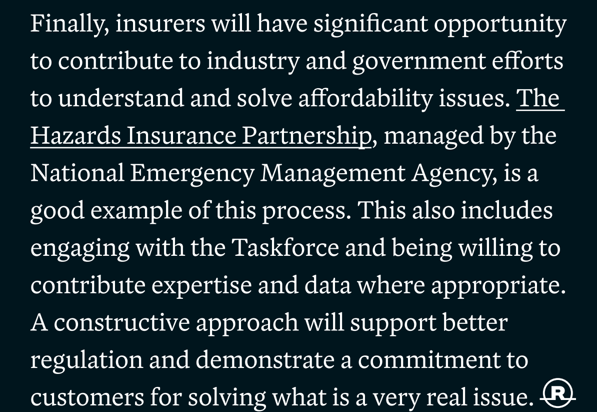
Reputational risks for insurers

There are implications for insurers, too. One of the largest insurer risks is reputational. Profitability continues to improve on domestic lines and it's easy to imagine a situation where higher prices combined with a period of lighter natural hazard events could lead to accusations of profiteering in a cost-of-living crisis. Insurers will need to communicate such dynamics clearly, and find ways to show customers they're treating affordability concerns seriously.

Another issue tied to reputation is the treatment of vulnerable customers – in this case those faced with high premiums and more limited financial resources. Often these will overlap heavily – areas most exposed to flood and storm risks are often related to those on lower incomes. Much thinking exists on this – the ANZIIF general insurance claims handling framework and the General Insurance Code of Practice provide guidance on key areas of customer service. However, complaint statistics from the Australian Financial Complaints Authority, and the findings in the recent flood inquiry report, suggest significant work is needed, with increases in general insurance complaints spanning claims handling, settlement amounts and claim denials. Aggressive handling of claims for vulnerable customers will be portrayed negatively, with potential to trigger regulator scrutiny. Insurer processes also need to be improved (by AI as well as human power) to ensure responsive service.

Collaboration critical for effective solutions

Finally, insurers will have significant opportunity to contribute to industry and government efforts to understand and solve affordability issues. The Hazards Insurance Partnership, managed by the National Emergency Management Agency, is a good example of this process. This also includes engaging with the Taskforce and being willing to contribute expertise and data where appropriate. A constructive approach will support better regulation and demonstrate a commitment to customers for solving what is a very real issue. ®



Spotlight on AI

AI's impact on insurance

In an atmosphere of rapid technological advancement – and general hype – excitement abounds for the potential of AI to enhance businesses. But along with productivity improvements, AI introduces new risks. We take a look at the implications for insurers across governance, underwriting and products.

AI systems are imperfect, they ingest and transform personal information, they're vulnerable to modification and misuse by malicious users, and they can produce outputs biased against certain groups of people.

Insurers are swept up in this in several ways:

- Like other organisations, they're looking at a range of applications, from user experience through to claims management.
- Uniquely, rapid AI adoption also impacts insurers' core business, changing the profile of underwritten risks, particularly across lines such as liability and indemnity, and presenting opportunities for underwriting new products that specifically address AI-related risks.

Navigating the associated governance challenges will be critical for the industry, especially in an environment where:

- **Regulators** are clarifying how existing regulations and legislation apply to AI-specific contexts and are developing AI-specific codes to capture residual risks
- **Consumers** are evolving their expectations of how their data is used and applied
- **Shareholders** are exposed to potential risks to organisational profitability and reputation if AI is not adopted and managed appropriately
- **Insurers** need to review their AI risk and governance practices to ensure they meet the needs of regulators, consumers and shareholders.

It's fundamental – current regulation applies

The need to develop new regulations for AI is a significant focus internationally and locally, although there's some debate on the need for AI-specific legislation. In Australia, a fundamental principle is that our legislation applies to AI in the same way it does to all other technologies – that is, legislation is *technology neutral*. The use of AI in insurance sits under a comprehensive regulatory framework, and insurers are already expected to manage risks related to their use of AI under their current regulatory obligations, such as those outlined by the:

- **Australian Securities and Investments Commission** – ASIC's 2024-25 Corporate Plan continues to include monitoring the use of AI by licensees, including assessment of risk management and governance practices and contribution to the Government's development of AI-specific regulation (pg 20).
- **Australian Prudential Regulatory Authority** – APRA's 2023-2024 Corporate Plan notes the growing use of AI is transforming how financial services are structured and delivered to end users. The regulator has indicated that new requirements to mitigate risks of AI are not anticipated, instead pointing to existing prudential standards intentionally designed to be principles based and technology neutral, inherently extending to the use of AI.

Filling in the gaps

Additionally, insurers have their own sophisticated risk management frameworks and processes, which are also subject to a stringent regulatory regime. Use of AI will to some extent be covered under the existing risk management framework, but there may be gaps that need to be addressed, along with further updates for any future AI-specific legislation. International AI frameworks and standards can provide a reference for areas that may need strengthening or modification. The relative risks in deploying AI will vary. For example, use of AI in back-office processes (such as streamlining invoice processing) is likely to be significantly lower risk than uses in pricing (which has legal requirements to prevent discrimination) or automation of call centres (where there is potential for harmful impacts on vulnerable customers).

Insurers will need to make sure their risk management frameworks appropriately identify higher-risk applications with suitable guardrails in place, while protecting innovation in lower-risk areas from disproportionately restrictive risk policies.

While the specifics will differ across insurers, areas requiring more careful assessment will include:

- Direct customer-facing tools and processes
- Applications with the potential to differentially impact on vulnerable customers
- Applications that may impact on insurer risk profile or solvency.

Underwriting AI risk – a need for clarity

Insurers face challenges in managing AI risk for existing lines. Increasing use of AI by insureds means insurers' risk profiles are changing, with low visibility of exposure due to varying rates of AI adoption, and uncertainty due to ambiguous policy wordings and limited exclusions relating to AI coverage.

For liability classes, additional complexity arises because use of AI has immediate implications for establishment of liability, including determining what an appropriate level of duty of care is and complexity in proving negligence or a breach of that duty of care.

How use of AI impacts existing lines of business

The risks for development and use of AI by insureds could leave insurers significantly exposed within the existing lines of insurance business they write. The table below illustrates the risks of AI use by class of business.

Insurance product	Impacts of AI
Directors and Officers (D&O)	A heightened risk of **claims for financial loss** due to reliance on advice/outputs from AI models, as use of AI in corporate decision making increases.
Professional Indemnity	Added risk of **alleged negligence or breach of duty** as advice and/or services may make use of AI (insureds' own model or use of third-party models).
Product Liability	AI is increasingly incorporated into physical products (e.g. drones, cars and household appliances), so added to existing risks are the risks of **design issues** relating to AI, including performance of the AI models used.
Cyber Liability	A heightened risk of **more advanced, larger-scale cyberattacks** from malicious use of AI (although offset by the use of AI in cyber defences), along with risk of data breach from AI models trained on large amounts of data.
Workers Compensation	Impact on claims management and claims costs, due to changes to the underlying risk of: ▪ **Physical harm** e.g. increased use of robotics in manufacturing, or intensification/acceleration of pace of work due to increased surveillance via AI model. ▪ **Psychological harm** e.g. lack of transparency and explainability of AI-based recommendations may cause anxiety and stress to workers.
Motor	The direct impact of increased use of self-driving technology, which includes AI systems, will likely lead to an **increase in repair costs**. The **risk profile** will also change as semi-autonomous and autonomous vehicles account for a larger proportion of cars on the road. The impact on motor insurance relating to autonomous vehicles is still emerging, with questions remaining on attribution of liability (to the owner, manufacturer or developer of the autonomous driving system) for injury or damages from an accident.
Compulsory Third Party (CTP)	An indirect impact of AI on CTP claims may emerge with **changes in frequency of claims** and **severity of injuries** as motor safety advances and autonomous vehicles become more mainstream.

Insurers are starting to define their response to the evolving landscape by clarifying coverage and addressing silent AI coverage – where policies provide cover for harm related to the use of AI, despite not specifically being designed to do so – by revising policy language and building out their underwriting requirements.

We've identified four approaches insurers could take using their existing products to manage the new risks AI is creating:

1. **Carve-outs** – Exclude coverage related to AI risk from existing products. For example, AON has made changes to some of its D&O coverage by augmenting definitions of key terms such as 'loss' and 'insured person' and enhancing typical exclusionary language to carve back coverage for AI-related exposures.
2. **Riders** – The addition of provisions to explicitly make this cover available within existing products.
3. **Bundles/packages** – Changes to existing products and the emergence of new products covering specific AI-related risks mean insurers can better package and customise their offerings, similar to how the cyber insurance offerings evolved.
4. **New product opportunities** – Offering AI insurance solutions to explicitly underwrite the risks of AI.

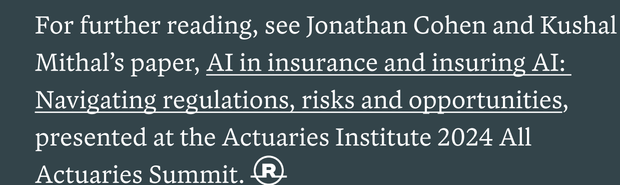
Dawn of a new era – new risks, new products

Beyond choosing to exclude coverage related to AI risk from existing products or affirmatively making cover for AI risk available within existing products, fresh opportunities are emerging in the form of new products to explicitly underwrite the risks of AI.

Examples include a liability product from *Munich Re* which provides AI developers a performance guarantee for AI models, a warranty product from Canadian startup *Armilla AI* that covers the investment cost of the vendor's (insured's) customers if the AI model fails, and liability cover from US-based provider *Vouch* for lawsuits associated with an insured's AI product.

A rapidly evolving technological environment for AI coupled with uncertainty due to a changing regulatory landscape may well lead to insurers offering new products covering AI risk.

Where to from here? Insurers have led the way for many years not only in managing their own risks associated with AI but also in underwriting others' AI risks. As AI is increasingly integrated into business throughout the world, insurers have a unique opportunity to build on this important role, combining their hands-on experience with data-informed decisions to support the continuing growth in AI by pre-empting and managing emerging risks.



For further reading, see Jonathan Cohen and Kushal Mithal's paper, AI in insurance and insuring AI: Navigating regulations, risks and opportunities, presented at the Actuaries Institute 2024 All Actuaries Summit. ®

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

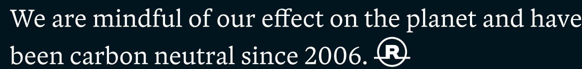
Our actuarial and analytics consultants support our clients in making strategic decisions to enhance the financial health of their organisations, and benefit communities, people and society.

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.

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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