SHORT-TERM INSURERS

Facing a catastrophe

More than just catastrophe claims are behind the disastrous underwriting results recently announced by a number of short-term insurers. The economic recession and plain bad underwriting also played their part.

There has nevertheless been a surprising increase in catastrophe claims, which include "natural disasters" mainly through wind, storm and water damage of one sort or another.

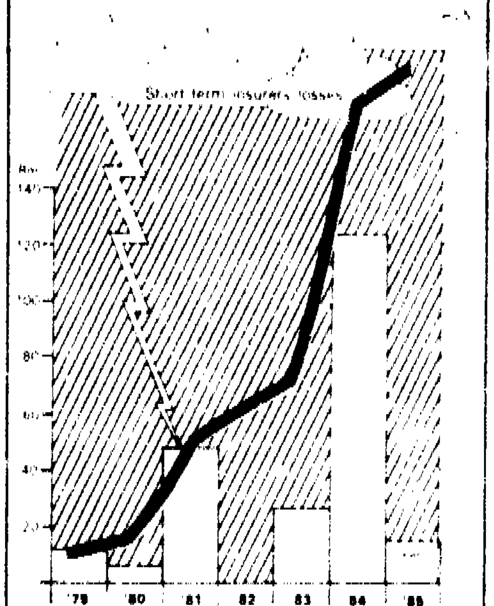
The figures speak for themselves, as shown in the accompanying graph. The cost of major catastrophes accumulated steadily from R11,8m in 1979, and just R5,2m in 1980 to R123m in 1984. In the five-year period estimated claims for natural disasters amounted to a staggering R214m. The biggest catastrophes included the Springs hailstorm (R24,3m), cyclone Domoina (R37,3m), and the Cape storms (R23,6m).

Rodney Schneeberger, MD of the SA Insurance Association (Saia), says this does not include all storm damage. "It includes those events we classify as a 'catastrophe' only. Once the association advises its members accordingly, then the insurers keep records of all the claims they receive for the respective events, even if it is only for, say, R50."

Records for the rest of claims related to water, storm and wind damage are not separated out from the underwriting accounts. Such claims would be for isolated events, that might affect an individual house, for instance, or a block of flats. But various estimates for the five-year period put them at between R200m-R300m. At a conservative estimate, therefore, all claims arising from natural disasters must exceed R400m for the 1979-1984 period.

The latest insurance company reports make startling reading as well. Compared to the half-year to June 1984, when most companies reported underwriting profits, for the second half of the year major insurers reported losses: Commercial Union R2,6m, Guardian National R2,4m, SA Eagle R0,8m, and Mutual & Federal a whopping R16,4m.

THE CLOUDS GATHER



As one insurer admitted: "The companies are bleeding badly, very badly indeed."

And catastrophe claims are only one side of the picture. As Swiss Re manager, Gareth Bradburn, points out: "Reinsurers bear the bulk of catastrophe losses by a long, long way."

Claims are also increasing in a number of other categories that more directly affect the insurers: fidelity guarantee business — covering thefts from employers, for example; fire insurance under what are euphemistically called "liquidation fires," where a proprietor sets fire to what he can't sell; and personal lines business, especially in the case of car thefts and house burglaries.

All, of course, related to the pressures of the current recession.

But much of the insurers' troubles stem from bad underwriting. It was they who previously slashed premiums to the bone in a bid for market share; and it was they who selectively passed over risks to their reinsurers in a manner that meant, for a time at least, losses would be exported.

While it is debatable whether natural disasters are an increasing trend, what is certain is that there has been a massive expansion of townships and industrial sites over recent years. At the same time, according to John Posnett, Deputy MD of Mutual & Federal, commercial and industrial premiums were slashed over a period of about seven years to 30% in real terms. Reinsurers

Financial Mail Jg. 95 Nr. 13 P. 147 Dat. 85.3.29

also cut their rates in competition.

But, last year, in what was described as a "fight for survival," reinsurers reversed the trend dramatically. Capacities were reduced, commissions they paid to insurers were slashed — so much so, in fact, that some insurers ended up paying out more commissions than they received — while reinsurers limited certain perils that could be ceded to them.

In other words, direct insurers were forced to take on more of the risk, while at the same time paying more for the privilege of passing some of it on.

John Posnett admits: "Certainly, we are in a bad claims cycle as far as natural catastrophes are concerned. The cost at R123m for 1984 is 460% up on 1983." He adds, "If nothing else, this indicates current insurance rating levels, particularly for business risks, are hopelessly inadequate."

Stricter measures

And it is doubtful there will be any improvement this year. Already there has been storm damage in Natal in February, estimated at about R15m. And no doubt reinsurers will respond to the flood of claims by even more stricter measures this next December. So it looks like the direct insurers will just get more of the same thing.

Posnett adds: "For the direct insurers the increasing price of treaty reinsurance is imposing a growing burden on the bottom line which cannot be ignored."

Meanwhile, the numbers of claims generally are expected to rise further as a result of the recession. On the other hand, there are indications that investment returns, invariably used to supplement underwriting losses, are starting to tail off. ■