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Navigating hard and soft market cycles

The opening keynote address at WICA 2023 took a look at global insurance market cycles – and how to get smart about navigating them.

By Paul McNamara

Liberty Specialty Markets, Asia Pacific head of casualty and professional and financial risks Marcus Thomas kicked off the main sessions at Thursday's WICA conference with a broad overview of the insurance market with the theme 'The insurance cycle: Why hard and soft markets exist - and how to navigate them'.

Mr Thomas delved briefly into the three most recent hard market cycles – from 1985 to 1987, from 2002 to 2004 and from 2019 to 2023 to try to establish whether external events were the root cause of these hard markets.

He touched on the 9/11 attacks in the US, COVID-19 and the collapse of significant companies as triggers that may be linked to sharp turns in the insurance cycle. One suggestion is that while these might not trigger market cycles themselves, they can contribute to 'fear events' that do initiative market cycle turns.

While the precise causes of 'super cycles' may be elusive, it is the 'long tail' they leave behind causing macroeconomic disturbances that insurers need to be wary of since that is often where the risk lies.

To round off the keynote, Mr Thomas dug out his crystal ball and gave delegates some hints about navigating the future of market cycles.

This included the use of analytics – and the need to have fully-coordinated units in order to have value. He also pointed to AI – which he predicted would not replace expertise in the P&C market, even in the

medium term. Indeed, he predicted that expertise would become even more highly prized.

One critical factor in navigating choppy waters that will remain is the ability to attract and retain talent.

"The cycle will continue in perpetuity," said Mr Thomas. "But we are getting better at managing it."

Living in a digital pandemic

War and conflict was a major theme of the first day of the WICA 2023 conference – with the first panel focusing on the biggest implications for the insurance industry.

By Paul McNamara

'The international security outlook and insurance implications' was the theme of the opening session of the war and conflict focus of the first day of the WICA conference. The panel discussion looked at war, political conflicts, pirating, aviation and cyber and was chaired by Federation of Defense & Corporate Counsel president-elect Craig Marvinney.

He was joined by CTBC Business School Professor Johnny Chang, Oppenhof & Partner partner Christof Gaudig, Zapiola Guerrico Abogados senior partner Martin Zapiola Guerrico and Mr Jesse McNeilly from Australia.

Professor Chang began with the clear message that, "Most insurance excludes war risk – so it may not be the solution we are looking for," but went on to highlight the ramifications that the 'long tail' of conflict can have on commerce.

Four out of every 10 leading semiconductor firms are in Taiwan – and the nation is responsible for 68% of the world's semiconductor market. "You can imagine if there is a conflict between Taiwan and China what could happen. The economic cost could be huge," he said.

Mr Gaudig amplified this. "The problem is that what we are facing is not a classical war. It is a hybrid conflict. The real question is where does it start? When do war exclusions kick in?" he said.

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The onus is on the insurer, he said, to prove that war has started and that the exclusions have kicked in – and this can be tough to establish.

In addressing cyber war, Mr Guerrico said, “Cyber attacks are very real and very much a problem. Initially, Latin America thought that cyber war was a developed world problem. Now we have discovered that we are not safe.”

Mr McNeilly offered another perspective. “There are shades of grey in conflict,” he said. His first-hand knowledge of Russia president Vladimir Putin’s invasion of Ukraine is that Ukrainians turned the invasion into a hybrid war rather than the blitzkrieg that the Russians had originally planned. Bringing it back to insurance, he said, “But people still need protection from their homes.”

Mr Guerrico summed the cyber war situation up neatly when he said that cyber has spread so far that it now affects individuals living in third-world countries. “We are just learning how to cope with it. We are living in a digital pandemic,” he said.

L-R: Mr Martin Zapiola Guerrico, Professor Johnny Chang, Messrs Christof Gaudig, Jesse McNeilly and Craig Marvinney.

The law struggles to define total loss

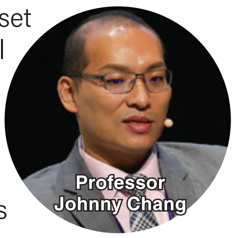
‘Insurance response to risk of conflict’ was the captivating title of the second war and conflict panel on the first day of WICA 2023. Panellists offered more questions than answers, providing much food for thought.

By Paul McNamara

The ‘insurance response to risk of conflict’ panel discussion promised to look at coverage issues ranging from marine, aviation and war risks exclusions, total losses including the concepts of actual and constructive total loss and more besides.

Chaired by King’s College London Professor Ozlem Gurses, the panel included 7KBW KC Peter MacDonald Eggers, University of Reading Professor Rob Merkin and CTBC Business School Professor Johnny Chang.

Professor Chang set the tone for the panel when he described the different view of the definition of war. While the broad definition of war is ‘any hostile action’ rather than armed conflict between states, the restrictive view is ‘the legal categorisation of the state of affairs existing between states when forced is used to vindicate rights or settle disputes between them’.



The net result is that whether or not a state of war exists can only be decided on a case-by-case basis.

Mr MacDonald Eggers delved into what formulates war and political risks and shared the view that war risks commonly include ‘war, civil war, revolution, rebellion, insurrection’ and many other states.

Political risks, meanwhile, can include capture, seizure, arrest, restraint, detainment, confiscation and expropriation – although he stressed that the two states are not mutually exclusive and acknowledged the difficulties in interpretation.

Professor Chang outlined how most commercial lines of insurance exclude war risk. Mr Merkin spoke of instances when a peril that insured is at the same time excluded - and indicated that the exclusion clause will prevail. He also delivered an illuminating snapshot of a case in which the University of Exeter in 2014 found an unexploded bomb dropped by the Nazis in 1940.

When the bomb was subject to a controlled detonation, the resultant damage to surrounding property was not covered because it was deemed to be a war risk.

Mr MacDonald Eggers gave valuable insights into the concept of total loss – both actual total loss and constructive total loss – but admitted that “the law struggles to deliver a definition for total loss in non-marine insurance.”

No such thing as peace and war, only ‘unpeace’

Conflict has been around since before man could walk upright. Technology is simply making it more pervasive – and harder to navigate - as the third panel on the first day of WICA 2023 discovered.

By Paul McNamara

In the conflicted modern political and commercial landscape, the issue of conflict manages to weave in cyber, ransomware, terrorism and piracy.


Mr Craig Marvinney

Navigating this complex reality is a nightmare, as session chair Federation of Defense & Corporate Counsel president-elect Craig Marvinney discovered in a panel that included 7KBW KC Peter MacDonald Eggers, University of Reading Professor Rob Merkin, Oppenhof & Partner partner Christof Gaudig, Lander & Rogers partner Melissa Tan and Mr Jesse McNeilly from Perth, Australia.

‘The extended nature of risk’ was an early focus in the panel discussion and touched on issues ranging from ‘planes left on the tarmac for long periods during wartime through to whether it was permissible to pay insurance claims to sanctioned entities.

“If someone is sanctioned, you’re just not allowed to pay out a claim,” said Mr Gaudig and acknowledged that, “It’s a very difficult issue.”

While an insurance policy may be quite in order, it would be illegal to pay funds to an entity that has been sanctioned or failed to meet anti-money laundering standards. However, if traditional western insurers refuse to offer such cover for sanctioned individuals and entities, it could open up a market for players in the BRICS markets to fill the void.

Mr MacDonald Eggers touched on some of the complexities in cyber risk – such as the structure and form of cyber risks as well as the difficulties defining certain concepts. What exactly constitutes a computer system, for instance?

He also delved briefly into the issue of double insurance and new cyber risk policies – and pointed out some of the challenges of ransomware – such as whether the payment of ransoms is recoverable and permitted, the piracy/terrorism distinction and sanctions legislation.

The general consensus was that it was impossible to mitigate the effects of cyber attacks and our efforts must focus on prevention.

Ms Tan pointed out that, “No one has put in legislation that payments are illegal.”

While the subject of the ransomware may decide not to pay – they can be subject to pressure from ‘downstream’ – perhaps customers who are also exposed. Cyber criminals are very sophisticated, Ms Tan said, “They tailor their extortion tactics to play on your emotions – that you have responsibility to your customers.”

Looking at cyber during physical combat, Mr McNeilly offered the insight that, “There is tons of disinformation going on in the battlefield – where units might be, what they are capable of – and stories of fake war crimes.” Speaking from his own personal experience, he said, “This can re-shape the entire war.”

Ms Tan summarised the situation when she said, “In the cyber space, there is no such thing as peace and war. It’s known as ‘unpeace’.


L-R: Messrs Martin Zapiola Guerrico and Jesse McNeilly, Ms Melissa Tan and Mr Christof Gaudig

Long-term affordability can only come from reducing risk

Australia, also known as the lucky country, has not been so lucky with natural catastrophes – which seem to be conspiring to make parts of the nation uninsurable. A panel on 'bearing the risk of climate change – the Australian experience' on the first day of WICA 2023 delved deeply into the issues.

By Paul McNamara

Australia's exposures to Nat CAT were the focus of a panel chaired by Mediation and Insurance Law mediator Chris Rodd and featuring NIBA former CEO Dallas Booth, ARPC CUO Michael Pennel and ICA COO Kylie Macfarlane.

The first question that the panel sought to answer was why Australian insurance premiums were going up so much and so fast. Ms Macfarlane stated quite plainly that what insurers do is price risk – and if the risk increases, then so must the price of covering it.

The main drivers of premium cost increases, she said, were increasing Nat CAT, inflation, the cost of reinsurance as well as state taxes, levies and surcharges. The harsh reality is that this makes insurance unaffordable for many people – particularly in northern Australia.

Mr Booth indicated that it is simply not possible to widen the insurance pool so that the whole of the country pays to compensate the north – because insurers are free agents and would compete with each other on price to make such a situation untenable. Making customers in cyclone-free Tasmania pay for cover in cyclone-prone northern Australia simply would not work.

Ms Macfarlane suggested that we might be at risk of asking the wrong question. "This isn't about bringing down insurance premiums. It's about reducing the risk."

The focus, therefore, must be on risk mitigation – looking at issues such as land use, building codes and ensuring that structures are more resilient. She indicated that the federal government's investment in the Disaster Ready Fund was a welcome move – and she encouraged the state and territory governments to match that commitment.

Mr Pennel gave instructive insights into the ARPC's new Cyclone Pool. The driving force behind it, he said, was to answer the questions, "How do we make sure we bring the price of insurance down? And how do we help with mitigation?"

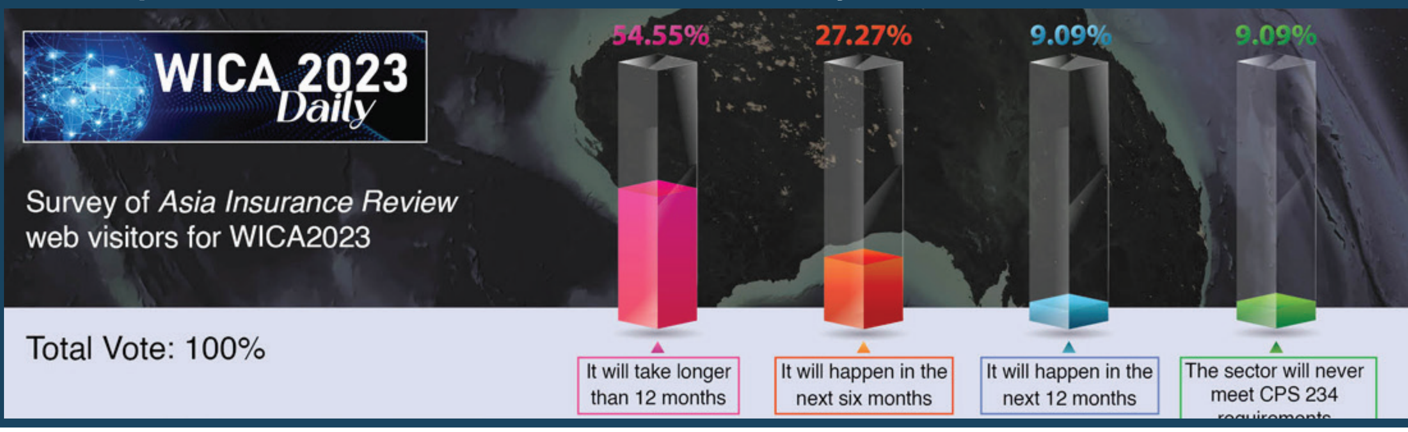
But Mr Pennel was clear, "The goal of the Cyclone Pool is to cover cyclone damage. It is not a flood pool."

Borrowing from the modus operandi of traditional reinsurers, he indicated that the Cyclone Pool was structured in such a way that in the long term it would break even – and even-out annual fluctuations. The goal was not to make a profit – and already ARPC had seen premium costs in northern Australia come down.

Mr Pennel said, "It's also to do with increasing the competition in these markets. There used to be two or three insurers in northern Australia offering cover. Now there is up 10."

L-R: Messrs Dallas Booth and Michael Pennel, Ms Kylie Macfarlane and Mr Chris Rodd

How much longer before the Australian (re)insurance sector is fully compliant with APRA's prudential standard on information security, CPS 234?



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