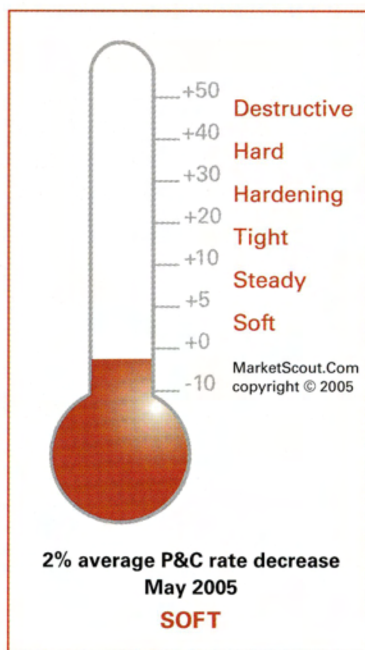
Going steady

A renewed sense of discipline among underwriters has stalled the tide of accelerating rate reductions in most classes of business and brought some welcome stability. But larger clients are still making big savings.

Previous market cycles have shown that in a soft market underwriters will slash rates in a bid to win big business, forcing their competition to follow suit. But underwriters seem to be taking a more responsible attitude during the present market cycle. Having seen scant evidence of aggressive price-cutting, Richard Kerr, chairman and chief executive of MarketScout, is wondering whether what he terms "rogue underwriters" have finally become extinct.

"There are isolated incidents of foolish underwriting but, in general, underwriters today are more professional than they ever have been," he says. "They are more analytical. They have better actuarial acumen and they take a much longer-term business view towards what they are doing."

Languishing interest rates could be the cause of part of underwriter's reticence to slash rates. When interest rates are high, carriers have been known to encourage cash-flow underwriting, capturing as much business as possible and capitalizing on the investment returns while the premium is sitting in the bank. But US interest rates are distinctly flat at present, so there is less scope for reaping high investment income.



2% average P&C rate decrease
May 2005
SOFT

Instead of plummeting, rates have simply slipped. Property/casualty rates are decreasing 2% on average, according to MarketScout data from June – down from an average zero rate increase in February. Casualty business is contributing to this, with rates dropping 2% on average and even further in some lines such as management liability, which has fallen by 4% on average.

An exception to the gradual softening is property business, where rates have remained static. June saw the start of the 2005 Atlantic hurricane season, which forecasters have predicted will be above average. Underwriters are evaluating risks more prudently so as not to be caught out a second season running. But instead of raising prices in coastal areas, which are more exposed to windstorms, underwriters are spreading any rate increases uniformly between policyholders to avoid lumbering certain policyholders unfairly.

Kerr believes rates will continue to soften slowly for quite some time before firming up again. "The rate reductions will continue at a measured and methodical pace for the next year to 18 months. But it looks like this cycle is going to be a lot more sensible than we have seen in the past," he says.

About MarketScout

MarketScout is an online insurance exchange for property and casualty business. More than 50,000 agents in the US use the exchange to place commercial retail risks. It sources markets where business can be placed and helps connect them with relevant industry expertise. By analyzing the business placed through the exchange, MarketScout is able to build up a picture of whether rates are increasing or decreasing across different lines of business.

Casualty

Paul Smith, executive vice-president at Willis North America

In general liability we are seeing decreases of 1% to 2% for smaller accounts, but decreases of up to roughly 10% for larger clients. Auto liability is seeing rate decreases of up to roughly 10% across the board. In workers' compensation we have seen single-digit decreases, typically between 4% and 5%. And in umbrella liability, rate decreases are averaging 10% or more – assuming the terms and conditions on the policy remain the same and it is a nice, clean account.

Rate decreases have varied significantly between classes within the casualty marketplace. The larger, Fortune 500 brands have more options of how much they increase or decrease their retentions and deductibles. They also have more alternative risk mechanisms available to them. On average we are seeing reductions of up to 10% there.

Smaller, commercial insurance buyers – and those that have built in more workers' compensation coverage – are only seeing rate reductions in low single digits. If a client has a greater exposure to terrorism, then naturally underwriters will be more wary of reducing the price of their coverage.

In the first quarter we saw rate increases accelerate quite sharply to 10% by March from about 2% in January. That softening was much quicker than I had anticipated. But it was not a continual slide. By May, casualty rates had stabilized just as quickly as they had softened, and they will probably stay roughly where they are for the rest of this year through to the start of next year.

Underwriters seem to be more disciplined in the present cycle. They seem to have learned some valuable lessons from the previous soft market. With interest rates so low, underwriters have to charge more reasonable prices on the front end.

There is also more capacity around now, with more and more carriers whetting their appetites for emerging markets. Some of the insurers that came in after September 11 have begun to expand their appetite and lines of business. Some such companies never used to write umbrella business, but now they are getting into that area. It is that sort of competition that is driving rates down.

Management liability

Mike Sorenson, director of specialty product lines at Acordia Risk Finance, a subsidiary of Wells Fargo

Management liability rates have been coming down since the end of 2002. Four percent is a pretty accurate number for the average rate reductions we are seeing at the moment. But for accounts that are clean – claims-free, with good corporate governance and no restatements – we are seeing reductions of between 5% and 10%.

The rate reductions are getting slower now because a lot of this business has already been aggressively corrected. The reductions we saw in the second quarter are lower than the reductions in the first quarter, for example. And the reductions in the first quarter were lower than they have been in the past two years.

Privately-held companies are the most preferred class of business. These accounts are probably seeing rate reductions of around 6% to 8%. The pricing in the public company arena has not been restricted in any way and has dropped by around 4%. Underwriters are scrutinizing companies more as a result of those cases, and are aggressively going after publicly-traded companies with less than a billion dollars in market capitalization.

Plus there is more capacity in the marketplace now, with two or three new US entrants all wanting a piece of the pie. They are marketing themselves as the carrier of choice that is willing to come in and streamline the underwriting process through technology and make it more efficient for agents and brokers.

Where these new carriers are not successful on technology advances, they figure the only way to get business is to drive prices down. But the established carriers are not letting the business go. American International Group, Chubb and Zurich all want to maintain their management liability books – especially for private company business – so they are matching premiums.

The really clean accounts might get 5% to 10% premium reductions over the coming months. But on an overall basis it will be slower than the 4% we have seen this quarter – maybe around 3%. Over the long term, I would say it is going to continue to stabilize towards zero, probably through to the New Year. ■