There are a number of challenges ahead for reinsurers and, according to Cameron Green and Warren Dresner, the current reinsurance market is a tough place to be. What follows are their reflections on the current state of the reinsurance market and their predictions for 2014.
These factors have been compounded by muted demand from buyers arising from the longer-term trends of better regulation, which in turn has led to better understanding and management of tail risk, as well as the trend of major insurance groups to retain more reinsurance premium volume and risk on their own growing balance sheets.

The impact of overcapacity has been most clearly evidenced by the up to 25 per cent risk adjusted rate reductions seen on US property catastrophe renewals at 1 January 2014 and the more modest, but still significant, rate reductions of up to 15 per cent on international property catastrophe renewals. This is a trend that we expect will continue in 2014 for buyers of reinsurance in Australia and New Zealand.

The influence of the growing capacity from the capital markets has been more pronounced on US property catastrophe placements where a combination of traditional, collateralised and securitised capacity has been utilised throughout more program structures. International property catastrophe placements still reside predominately with traditional reinsurers, however, we are seeing an increasing appetite from collateralised markets for Australia and New Zealand business, both on traditional programs as well as on aggregate and alternative reinsurance structures, where these markets have a willingness to innovate and think outside the traditional reinsurance square.

The Australian Prudential Regulation Authority (APRA) have a keen interest in counterparty security and currently maintain strict rules regarding the need for collateral for reinsurance to be held onshore. APRA do recognise that prescription-based rules have the ability to stifle innovation and as they become more comfortable with collateralised products and markets, significant opportunities will exist for more innovation in our market, with further flow on benefits from the growing use of capital markets capacity.

“Mother Nature rested in 2013, with natural catastrophes accounting for around half of what was experienced in 2012.”
“Faced with these market headwinds, reinsurers are adopting a variety of defensive strategies.”

High regulation in Australia and New Zealand continues. Since the Life and General Insurance Capital (LAGIC) changes, insurers are looking at both the vertical and horizontal requirements and many are buying more reinsurance as a consequence. APRA is also placing an increasing emphasis on an understanding of catastrophe risk at the Board level.

Soft market conditions are not, however, unique to property catastrophe business. With reinsurance rates across nearly all classes of business falling during 2013. Pricing margins on excess of loss business continue to be compressed. While we have seen a movement away from proportional reinsurance in Australia and New Zealand, the increased exchange commissions available in the current market could be cause for a re-think. Australian and New Zealand clients will also need to consider whether pushing terms and conditions would be in their best interests, given their businesses and their overall reinsurance placements.

Faced with these market headwinds, reinsurers are adopting a variety of defensive strategies. Larger reinsurers are using their balance sheet strength and technical ability to offer more capacity and more complex, multi-class, multi-year deals. We have seen other reinsurers expand into specialty lines and many have developed multi-channel capacity offerings, seeking to use their underwriting expertise to deploy capacity on behalf of capital markets.

Some smaller reinsurers are entering into pooling arrangements that provide them with the opportunity to access business they might not otherwise see. Our predictions for the reinsurance market in 2014 include:

- Greater use of multi-year reinsurance as buyers look to increase the certainty, stability and control of the reinsurance placement.
- Efforts to maximise the use of both traditional and collateralised markets to achieve client-specific pricing and coverage goals.
- Rates for casualty classes of business will continue to fall as there is nothing suggesting an increase in loss frequency or severity in casualty.
- Increased focus on casualty catastrophe exposures, particularly maximum event scenarios and the impact of class action litigation.
- Increased scrutiny from APRA and the Reserve Bank of New Zealand regarding the understanding of catastrophe risk at the Board level.
- Despite the fact that some reinsurers are starting to walk away due to price concerns and that others may look to cut back capacity if prices fall too far, there is still plentiful capacity available.

The year 2014 is going to test the skills of reinsurers and intermediaries alike as buyers look to exact continued price and coverage benefits in a softening reinsurance market.

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