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We're Not in Kansas Anymore

by John H. Nelson & Chuck Eckert

While the Atlantic and Gulf coasts have remained relatively quiet YTD for a third consecutive tropical storm season, the spring and early summer months brought violent storms and record rainfall to most of the Midwest. Surging flood waters inundated communities across Wisconsin, Minnesota, Iowa, Nebraska and Missouri. The majority of the insured water damage was not covered by private insurers, but rather the National Flood Insurance Program. However, the wind and hail damage attributed to record tornado activity and strong thunderstorms pushed estimated privately insured catastrophic losses to over \$5 billion — or \$2.7 billion more than second-quarter 2007.

The U.S. property & casualty insurance industry's net income after tax fell to \$8.2 billion in first-quarter 2008 from \$16.2 billion in first-quarter 2007. In addition to the 49 percent decline in net income in first-quarter 2008, the industry posted \$0.6 billion in net losses on pure underwriting, which is an \$8.9 billion adverse swing from the \$8.3 billion in net gains on underwriting in first quarter 2007, according to Insurance Services Office (ISO) and the Property Casualty Insurers Association of America (PCI).¹

The combined loss ratio for the industry rose to 99.9 percent in first-quarter 2008 from 91.7 percent in first-quarter 2007, making it the industry's worst first-performing first quarter since 2002. Catastrophic losses were also the highest for any first quarter since 1994. The insurance industry strives to achieve an underwriting profit and positive investment income on premium float. The current three-plus year soft insurance cycle, coupled with deteriorating underwriting results and a bear equity market will no doubt spell trouble down the road for insurers.

According to David Samson, President and CEO of the Property Casualty Insurers Association of America, "Seasonal patterns in the data suggest that insurers' rate of return will continue to decline further this year. Insurers' profitability in the first quarter usually exceeds their profitability later in the year, partly because of the timing of weather-related catastrophic losses. The Atlantic hurricane season runs from June 1 to November 30, and the "experts" are predicting an unusually active hurricane season this year."¹ At the time of this article, Tropical Storm Fay is soaking Florida with 25+ inches of rainfall in some counties.

According to the Council of Insurance Agents and Brokers' first-quarter 2008 market survey, rates for commercial insurance policies declined an average of 13.5 percent. Real US Gross Domestic Product (GDP) increased 1 percent. Declining insurance premiums combined with RGDP increases are often an indication of intensifying competitive pressures that lead to lower prices. However, property CAT capacity remains scarce in some coastal and earthquake prone areas. These figures are consolidated estimates for all private property & casualty insurers based on reports accounting for at least 96 percent of all business written by private U.S. property & casualty insurers.

The nearly four-year soft insurance cycle appears to be winding down. Our property casualty market outlook remains favorable throughout the remainder of 2008, but guarded for 2009. We will keep you advised of all material developments.

¹ "P/C Industry Net Income and Overall Profitability Drop by Half in First-Quarter 2008 on Deterioration in Underwriting and Investment Results," June 24, 2008, Insurance Services Office website, accessed July 25, 2008 at www.iso.com.

* Additional statistical information provided by the Property Casualty Insurers Association of America website, www.pciaa.net, by Dr. Robert P. Hartwig, CPCU, President, Insurance Information Institute.



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