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In our Insurance Market Update this quarter, we focus on the insurance implications of the Auckland Anniversary Flood and Cyclone Gabrielle weather events and what we believe the impact is likely to be for the New Zealand insurance market going forward.

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Severe weather hits insurers hard

- *Number of claims similar to the Canterbury Earthquakes*
- *Re-insurance costs will likely drive premium increases*

The North Island of New Zealand has experienced a catastrophic start to 2023 with the Auckland Anniversary Flood and Cyclone Gabrielle events.

We believe that claims numbers from these events will be somewhere in the vicinity of the claim volume experienced from the Canterbury Earthquakes.

However, whilst the volume of the claims could be similar, the cost is expected to be much lower but still significant. This is because the nature of the losses suffered are generally related to “partial damage” as opposed to “total loss”.

Partial damage is still disruptive requiring extensive clean-up work that can interrupt normal business trading for an extended period.

Two weather events together enough to shift the market

The likelihood of New Zealand insurance buyers facing tougher conditions in 2023 is something that we have been signalling for some time. However, the Auckland Anniversary Flood and Cyclone Gabrielle events have accelerated the market change.

After the Auckland Anniversary Flood but before Cyclone Gabrielle hit, IAG whose New Zealand brands include NZI, AMI and State announced it would blow past its group-wide internal budgets for natural disasters for the year. As a consequence of this announcement, its shares dropped by 3% wiping out approximately A\$330m of share market value.

The geographic nature of the events being in the upper North Island means that most, if not all, insurance companies writing business in New Zealand are impacted. However to date all insurance companies are reporting that they remain financially stable and have sufficient resources to meet their claim obligations to clients.

The insurer’s insurer

We have explained in previous updates that insurance companies take out their own insurance to protect their exposure to claims. This is known as reinsurance.

The reinsurance market is global and major players like Munich Re, Swiss Re and Hannover Re are all involved in providing protection to insurance companies writing business in New Zealand.

Insurance companies purchase their reinsurance protection on an annual basis, just like traditional insurance. The main renewal date for most of these programmes is 31 December each year.

Commenting on the 2022/23 renewal season, global reinsurance brokers have noted how high inflation, interest rate hikes, depleted capital, fractured energy markets, the Ukraine war and Hurricane Ian have combined to tip the reinsurance sector into “significant volatility” resulting in

// one of the hardest reinsurance markets in living memory. //

The amount of weather related losses in recent years is also a significant factor. In 2022, Munich Re reported that the global insured losses resulting from natural catastrophes was US\$120bn – that’s a whopping US\$23bn higher than the average of the last five years. Over half of these losses came from Hurricane Ian which hit the USA in September, but there were also large losses from winter storms in Europe, earthquakes in Japan and Afghanistan and flooding in Australia.

February’s tragic earthquake in Turkey and Syria which claimed over 43,000 lives, is also expected to cause insured losses in excess of US\$5bn according to risk modelling company RMS.

It is this continued run of severe catastrophic losses across the globe that has forced reinsurers to put pressure on insurance companies with increased costs and higher retentions and this will be passed on to insurance buyers by way of a ‘hard market’.

Introducing a hard market

- **New Zealand to enter the hardest insurance market conditions in well over a decade**
- **Perfect storm drives New Zealand premium increases**
- **Potential risk based pricing for floods**

We understand that the two events in January and February have caused several New Zealand insurers to exhaust the reinsurance protection they had in place requiring them to go back to the reinsurance market and purchase reinstatement cover.

The additional cost of the reinstatements (especially so early in the year) will have significant impact in increasing the costs that insurance companies need to recover from policy holders.

The cost of weather related claims, the effect of high inflation and disrupted supply chains had been impacting the results of New Zealand insurers for the past couple of years but the Auckland Anniversary Flood and Cyclone Gabrielle lead us to anticipate that insurers will move from an environment of gradual premium increases to demanding more drastic pricing uplift.

There is also the potential for coverage changes to come into the market around flood exposure. Flood has been a peril largely ignored by insurers in the past, but an expected bill in excess of \$2bn from recent events has focused their thinking.

While insurers are not yet saying that flood damage cannot be covered, we expect to see far more focus on "risk based pricing". This is where insurers take a

much closer look at an insured's exposure to flood than they may have in the past.

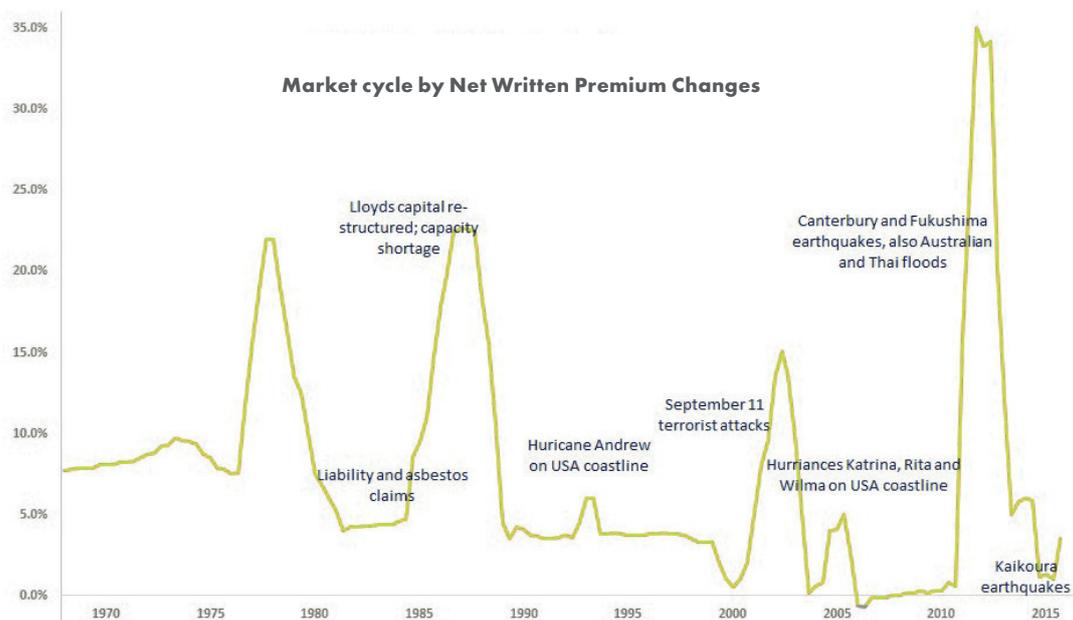
It is worth noting that in both Australia and the United Kingdom, Governments have worked with their local insurance market to try to find alternative solutions to this growing exposure. We anticipate that the New Zealand Government and local authorities will need to do the same and work with New Zealand insurers to ensure that affordable cover remains viable and available over the longer term.

Explaining a hard market

Most financial markets have cycles. The stock market has its bull and bear markets and in the insurance world these are known as hard and soft markets.

These cycles are unavoidable and have occurred many times in the past. Generally they are triggered by a single or series of catastrophic losses, but the severity of them is often linked to external factors such as the condition of other financial markets which influence where investors look to gain the best returns.

The graph shows historic market cycles and the events that contributed to them by tracking premium changes in the Lloyd's of London insurance market.



Source: theadvisers.co.nz

The graphic below shows roughly where we are within the market cycle.



What you need to consider in a hard market

When navigating a hard market it is essential to prepare with your broker detailed insurer submissions and allow plenty of time to engage and negotiate, including being willing to consider alternative programme options that optimise what is available.

The following four steps are a practical approach to being a well prepared insurance buyer.

01

Building strong relationships ahead of renewal

Your relationship with your insurance broker and their relationship with providers in the insurance market are of critical importance. It's imperative that your broker understands your organisation and knows the individual risk exposures associated with your business. This enables them to design a fit for purpose insurance and risk program, ensuring you get value for money with the correct coverage in place.

03

Provide detailed information that represents your risk profile in positive terms

Be prepared to document and detail your risk management protocols. In the current market conditions insurers will require more underwriting information. Collect and collate accurate, up-to-date building valuations and risk surveys. Insurers will also want to see your business's risk control processes, supply chain management and your risk management program. Work with your broker so that they can present your insurance needs to potential insurers in a tangible manner that will resonate and be attractive.

02

Starting renewal preparations early

The more time your broker and you and your business team have to work on the renewal of your insurance program, the more likely you will gain an effective result in this challenging insurance market. That demands putting in the time to gather the relevant and comprehensive information so that it can be presented to potential insurers well before the renewal date. Building in a longer lead time enables your broker to properly market your insurance program to and negotiate with potential insurers, presenting your business in the best possible light.

04

Being open to flexible, innovative ways of structuring your insurance programme

The insurance market isn't static but in fact highly responsive to claims impacts and events that alter the perspective on risk. Be open to working with your broker around changes to pricing, deductibles and coverage. Your insurance broker may be able to offer creative solutions for high risk businesses where the insurance market may be unwilling to deploy their capital. If you're willing to take more risk on your balance sheet, let your broker know.

Summary

Only time will tell what the final insurance cost of the Auckland Anniversary Flood and Cyclone Gabrielle will be. However, once again these events demonstrate the need to have robust insurance protection available because the worst can happen. There is no doubt that the world is experiencing more frequent and more severe incidents of extreme weather. This will continue to put pressure on global insurance and reinsurance markets who are seeking sustainable solutions. In New Zealand there will no doubt be an impact on pricing and potentially coverage.

The best tactics to navigate a hard insurance market are to engage early. Information and time are key to negotiating with insurers as well as being prepared to consider alternative options such as a higher excess to help keep costs down.

For more information

If you have any questions or want to understand the impact of these changes on your specific situation, please contact your Crombie Lockwood broker.



About Crombie Lockwood

One of New Zealand's leading insurance broking companies, we arrange business, personal and life and health insurance on behalf of over 100,000 clients throughout New Zealand. With deep connections to the communities we service around the country, our brokers draw on local understanding, insurance expertise and the resources of a large organisation to get New Zealanders' insurances sorted.

Your insurance sorted

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