

Why do my insurance premiums change when my business has not?

The insurance market is cyclical (typically in periods of circa ten years) in much the same way as the property market. This cycle is the reason why your premiums may go up even if your business has shrunk, or down even after you have had a claim.

The insurance cycle is comprised of two halves – a hard market and a soft market. A hard market is characterised by high insurance premiums, and a soft market by low insurance premiums.

In order to explain how the cycle affects you, I will explain what drives it through hard and soft markets. The good news is that, in our opinion, at the moment asbestos consultants and contractors are experiencing a very soft market, so insurers (and therefore premiums) are at their most competitive.

Insurers run a commercial business, and of course they work to make a profit. The prevailing economic climate has affected their profit in two main ways - since April

2007 insurers have seen a steady increase in the number of claims being notified as a result of the economic climate. Insurers also make a profit by investing premiums, and their investment income is down.

This gives a clear indication that premiums might rise across the market to offset losses – equating to a shift towards a 'hard market'. However, this has not yet happened. Some sectors, such as valuation surveyors and solicitors, have experienced this shift, but the market as a whole has not moved. We have been in a soft market for approximately six years, but when speaking to underwriters there is uncertainty about when it will shift to a hard market. Although most underwriters expected the shift after the economic downturn this has not happened, and there is a general suspicion that something like a catastrophic event in the USA may cause a high volume of claims in the Lloyd's market that trigger the shift.

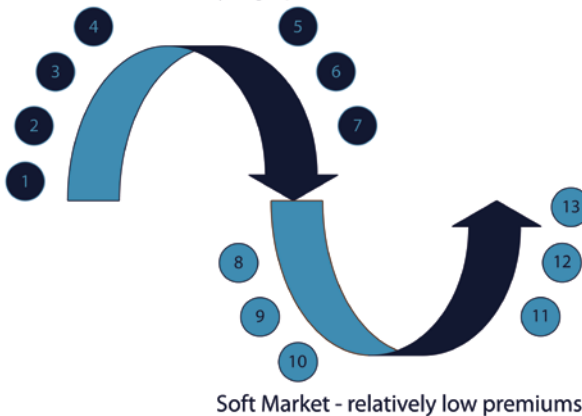
As we see it, the typical sequence of events which affect the cyclical shifts in the market, and thus your premiums are:

- 1) An increase in claims occurs, often caused by an economic downturn/catastrophic event
- 2) These claims cause insurers to lose money, and so they may withdraw from certain industry sectors
- 3) This results in less competition, so prices start to rise
- 4) Insurers in a certain industry sector can be more selective in the business they underwrite, only taking "safe businesses" or charging a higher premium if they are not keen to take on a business due to its risk profile
- 5) This increase in selectivity is compounded by more restrictive policy wordings designed to minimise insurers' losses
- 6) A decrease in losses results
- 7) This means that there are higher underwriting profits
- 8) With higher profits, new insurers look to enter the market
- 9) More insurers mean more competition to write your business, and a decrease in premiums occurs
- 10) With profits made and competition high, policy wordings are broadened to offer wider cover in order to win business
- 11) With broader wordings come more claims
- 12) More claims result in higher underwriting losses
- 13) Higher losses mean insurers exit the market.

And so the market cycles.

It's important that whoever buys insurance for your firm understands this cycle and the relative pressures on premiums. Accurately communicating your firm's risk profile will mean improving the fit of cover, and ensure the premiums that you are quoted more closely reflect the risk they relate to.

Hard Market - relatively high premiums



If you'd like more information on current market conditions, or to discuss how to manage the buying process most effectively, please do give me a call.

Phil Davis 020 7648 7210
Howden Insurance Brokers