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Corporate news

Hannover Re on course for further profitable growth in property and casualty reinsurance

- **Hannover Re expects improved prices and conditions for the 2020 renewals**
- **Natural catastrophe losses prompt price increases across multiple segments; Hurricane Dorian as a reminder**
- **Lower interest rates call for underwriting discipline**
- **Growth opportunities in Asia and Latin America**
- **Reduction of protection gaps offer opportunities for the industry to underline its social relevance**

Monte Carlo, 9 September 2019: The insurance industry continues to face the challenges of surplus capacities and historically low interest rates. Prices and conditions have nevertheless taken an appreciably more pleasing turn in 2019 compared to just one year earlier. Particularly on the primary insurance side, modest improvement can be observed across a broad front – which in some areas is also reflected in reinsurance business. The effects of this recovery are, however, still muted.

"In recent months we have been able to secure initial price increases across the board," Chief Executive Officer Jean-Jacques Henchoz said. "The renewed drop in interest rates and the considerable strains from large losses underscore the need for improved prices and conditions in the upcoming year's renewals. Given the challenging market environment that we are still facing, we shall continue to keep a very close eye on price and risk adequacy and will put profitability before growth."

The decline in rates in the years up to 2017 left its mark on the technical results posted by the entire industry, which came under added strain from further considerable large losses in 2018 and the need to set aside additional reserves for prior-year losses. Not only that, the return to what are once again historically low levels of interest rates is having an appreciable impact on investment income.

As a further factor, there are clear signs now that underwriting discipline is tightening up in the primary market too with a view to rehabilitating unprofitable portfolios. This is reflected in rising prices for primary insurance, which benefits proportional reinsurance in particular.

Competition on the reinsurance market nevertheless remains intense and surplus capacities are still the norm. With the profitability of the sector coming under increasing pressure, technical discipline on the underwriting side remains the top priority.

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In the various rounds of renewals held in the current year it has already been possible to push through higher prices in some areas. Particularly marked price increases were booked in programmes or regions that had suffered losses. Rates have tended to stabilise for loss-free covers, although in some areas they even moved higher. The overall picture was one of rates broadly commensurate with the risks.

Specifically, Hannover Re anticipates the following developments in the treaty renewals as at 1 January 2020:

Europe
In *Germany* Hannover Re expects to see further premium growth in the property and casualty primary insurance market for 2019. The key driver here are rate increases in the property line.

In property insurance the highest-volume lines of homeowners, industrial, commercial and agricultural risks continue to deliver above-average premium growth that reflects the ongoing need to rehabilitate the business. In addition, there are increasingly higher retentions or restrictions in the scope of cover – or, alternatively, coverage extensions for payment of additional premium. On the claims side the situation is showing modest improvement. This is due primarily to the fact that natural catastrophe losses in homeowners insurance are now within the bounds of expectations and can also be attributed to reduced large losses in fire business. That being said, neither of these sublines will post an underwriting profit this year and further remedial action is therefore still needed. With this in mind, it is Hannover Re's expectation that additional steps will be taken to improve profitability.

Results in motor insurance are likely to take a turn for the worse because average premiums are expected to remain flat against a backdrop of rising costs for spare parts and repairs.

In the *United Kingdom and Ireland* some hardening of the market can be observed on the primary side. Lloyd's of London followed a more restrictive approach with most syndicates and for selected classes of business. In turn, this led to shortage of supply for some coverages. This has caused the rate level to rise across all lines. The market for motor business had seen slight price reductions in anticipation of an adjustment to the Ogden rate, although the latest change to minus 0.25 percent was a smaller adjustment than market players had expected. In view of the pre-emptive rate reductions that had been made, however, Hannover Re now anticipates slight rate increases for the upcoming renewal season.

The market for property reinsurance in the United Kingdom and Ireland is very largely stable. Based on its good business relationships with long-standing clients, Hannover Re is able to preserve its market position. Similarly, the other lines are also characterised by a stable price level and essentially unchanged conditions.

Primary insurance in *France* continues to show modest growth, both among private customers and on the commercial side. The market climate remains intensely competitive, putting profitability in general under pressure. Thanks to its leading position in builder's risk insurance Hannover Re continues to benefit from the recovery of this sector.

In *Central and Eastern Europe* growth rates in primary insurance business consistently outperform the overall European average. The market for reinsurance is still shaped by excess capacities, as a consequence of which these markets remain fiercely competitive – especially in the motor and industrial fire lines, not least owing to the absence of exceptional large losses or natural disasters in the first six months of the year. On the whole, reinsurance prices are on a level that is commensurate with the risks.

North America

Developments on the North American primary insurance market are favourable. The rate level is rising in all lines except workers compensation by at least single digits, with increases running into comfortable double digits in loss-impacted areas. Further steady organic growth can therefore be anticipated. The markets remain competitive, as a consequence of which sufficient capacity is generally available for both property and casualty business despite the sustained trend towards mid-sized losses.

The losses incurred in prior years, most notably the wildfires in California, took a significant toll on insurers and reinsurers alike. While traditional market capacities remain largely unaffected, it is evident that a more cautious approach to managing risks is generally taking hold. Despite the sometimes appreciable price adjustments seen for loss-affected programmes, it is proving difficult to fully place them in some instances. Rate increases can also increasingly be observed under programmes that have not suffered losses.

Non-proportional reinsurance is in a stable state, holding the promise of adequate treaty conditions for the upcoming renewals as well. Further price adjustments are to be anticipated overall in property insurance. Rate increases will also become more prevalent in the casualty lines.

Issues surrounding digital coverage concepts currently occupy the North American market, in which insurtechs have become significantly more active.

Latin America

The growth trend in the countries of Central and South America continues. Stronger demand for high-quality risk protection is evident in most markets, enabling financially robust reinsurers to write business at adequate prices. Demand for catastrophe covers also remains very brisk and is still rising. Hannover Re expects to obtain improved conditions in this region on the back of a number of natural disasters.

Individual countries in Latin America continue to record varying growth rates in demand for insurance products, primarily in areas associated with the coverage of motor vehicles and real estate. Future growth is, however, heavily dependent on the broader political and economic framework conditions of each country.

Increasingly strong interest is being shown in the development of simple coverage concepts based on parametric indices. Such parametric covers – which are often comparatively affordable – are particularly well-suited to countries with a low insurance density. Solutions such as these enable governments to improve the protection available to their population against catastrophic events.

Asia-Pacific region

Hannover Re continues to pursue its successful path of recent years in this growth region with added intensity and supports clients as they develop their business and face up to the challenges of the coming years, whether it be through concepts that provide capital relief or through optimisation of the distribution and design of their products. Quick decision-making and local branches with appropriate decision-making authority establish a basis for further cultivation of these markets and testify to their significance. Hannover Re is thus able to assist the development of its customers on a regional basis and assure profitable growth.

Above all, China and India are considered very important markets here. Bearing in mind their population density, a rapidly expanding middle class and the associated increase in asset values, the level of insurance in these countries is likely to surge sharply. Appreciable rates of increase can be anticipated in the medium to long term not only in property and casualty insurance but also in the area of health and provision, a trend from which reinsurers will also benefit.

Furthermore, it is to be expected that urban densification, especially in Asian metropolitan centres, will continue to increase. This goes hand-in-hand with a need to expand infrastructure. Planning and funding as well as construction and maintenance all play a vital role here. Bearing in mind the exposure to natural disasters, the task is to design appropriate insurance solutions in order to further boost insurance density. Narrowing these protection gaps opens up opportunities for insurers and reinsurers alike to underscore their social relevance.

Natural catastrophe business

For two years in a row natural catastrophe business was impacted by immense losses in many regions around the world, the adverse effects of which can also be seen in the balance sheets of reinsurers and capacity providers on the ILS market. In property catastrophe business this has resulted overall in price increases, driven by loss-affected programmes – although the rate increases here again fell short of expectations. Even though some providers of reinsurance coverage have scaled back their capacities, supply still exceeds demand. Recent natural catastrophes such as Hurricane Dorian will result in reinsurers demanding further rate increases.

Hannover Re anticipates the following developments on individual markets for natural catastrophe risks:

North America: Slight increases in rates across a broader front were recorded in the mid-year treaty renewals. In Florida improvements of more than 20 percent were booked under loss-impacted programmes, while otherwise they remained in the single digits. The further direction of prices depends on the loss experience in the current year, although even without significant losses prices can be expected to rise within the single-digit percentage range.

Europe: The pressure on prices in European reinsurance markets has diminished in intensity. In Continental Europe and Eastern Europe high-margin business can nevertheless be generated through selective underwriting and private deals. While no indication of a fundamental shift can be discerned, the rising risk awareness among reinsurers will likely prevent further premium erosion and may even bring about modest rate increases.

Japan: Appreciable price increases have been recorded here for catastrophe covers in the current year. Three sizeable natural disasters in Japan affected not only the aggregate covers of cedants, but also their catastrophe XL programmes. Most notably, Typhoon Jebi had a considerable influence on the observed sharp rate increases. In view of the poor run-off, significant price increases will probably be seen again in Japan in 2020.

Australia/New Zealand: In New Zealand past earthquake losses have had the effect of stabilising rates against a backdrop of rising demand for capacity. Prices in Australia softened somewhat. Especially in Australia, Hannover Re is able to obtain more attractive prices than the market as whole based on its standing as a reinsurer with a very good rating, long-standing expertise and excellent business relationships.

Specialty lines

In *aviation insurance* the positive trend towards a more stable market environment in original business has been sustained; this can be attributed not only to the difficult earnings situation in prior years but also to new losses – most notably from the product liability segment. The improvements here extend to all market segments – albeit to varying degrees – with particular stand-outs being the US market for small aircraft and business jets as well as the international airlines segment. However, given that the market had been experiencing a downward slide for more than a decade, this development will have to be sustained in order to assure the long-term coverage stability of the market.

Initial signs of positive tendencies in the underlying business are now also being reflected on the reinsurance side. Hannover Re benefits directly from a rebounding market environment through its proportional participations. With an eye to its non-proportional programmes, however, the company has also been able to write better business of late than in the previous years. Despite this positive news, the fact should nevertheless not be overlooked that the sector – just as with the primary insurance market – is only at the beginning of a necessary market correction, which is why Hannover Re continues to adhere to its disciplined underwriting approach with a focus on the long term.

The *marine market* was dominated by two sizeable loss events in 2018. In the first place, Typhoon Jebi developed into a substantial loss for the Japanese marine market. Secondly, primary insurers, especially providers on the Lloyd's market, were hit by the Sassi superyacht fire. These two events served to largely stabilise the market environment and made it possible to achieve sharply higher prices in the Japanese renewals of April 2019.

The marine market was characterised by a stronger influence by Lloyd's. As a result, growth limits and in some cases also reductions in underwriting capacity were imposed by Lloyd's for several lines of business. This led to a marked hardening in primary insurance conditions, the effects of which were particularly palpable in cargo insurance and yacht hull business.

Rates in the offshore energy sector are broadly unchanged. Given the absence of major loss events and a stable oil price, demand on the customer side and the availability of supply from insurers were not subject to any significant fluctuations. For the 2020 treaty renewals no substantial changes are anticipated for reinsurance conditions and prices in this line.

Loss ratios in *credit and surety insurance* as well as the area of political risks are slightly higher than in previous years. The loss experience is characterised by a moderate rise in claims frequency – although this is still on a good level – and fairly stable loss amounts in individual cases. The elevated claim costs seen in emerging markets in previous years continue to fall, although they are still on the high side viewed from a multi-year perspective. With this in mind, prices for insurance and reinsurance should remain stable; demand for reinsurance covers in the area of credit, surety and political risks is either unchanged or trending slightly higher.

In the area of *agricultural risks* the growing need for agricultural commodities and foodstuffs as well as the increased prevalence of extreme weather events continue to stimulate demand for insurance and reinsurance solutions, especially in emerging and developing countries.

Hannover Re accesses the *insurance-linked securities (ILS)* market both to obtain protection for its own catastrophe risks and to transfer life and health or property and casualty risks to the capital market for its clients. This primarily takes the form of collateralised reinsurance, which is still the largest business segment within Hannover Re's ILS activities, but also by the issuance of catastrophe bonds.

In 2019, for example, the company has so far helped bring five catastrophe bonds to the capital market for US clients with a total volume of around USD 1.1 billion. Over the coming years Hannover Re expects demand to show moderate growth overall. The company is also itself an investor in catastrophe bonds, thereby maximising all the opportunities offered by the ILS market.

Business in the area of *structured reinsurance* continues to develop in line with expectations in the current year. Going forward, too, Hannover Re expects to see further growth in demand for innovative and tailor-made reinsurance solutions.

In this context growth opportunities on a high level are anticipated in North America, Europe and Asia. The purchasing habits of many clients have changed of late, reflecting a shift towards holistic reinsurance solutions. This trend shows no sign of abating and will mean that in the future, too, more and more customers will be calling for increasingly complex reinsurance solutions.

The planned implementation of IFRS 17 should cause demand for bespoke reinsurance solutions to trend higher, driven by the further increase in the complexity of capital and risk management faced by customers.

Outlook

The loss situation remains challenging in some parts of the market and pressure is growing as interest rates have failed to rebound. While the general picture as regards large losses in 2019 still remains to be seen, prior years have taken a toll on the industry's results.

Hannover Re therefore anticipates improved prices and conditions overall for the treaty renewals as at 1 January 2020.

As has been apparent from the renewals over the course of the year so far, broadly diversified reinsurers with a very good rating are able to profit from the current state of the market and selectively expand their portfolio, especially when it comes to large-volume covers. Hannover Re is thus satisfied with the business renewed to date in 2019.

Hannover Re identifies particularly attractive growth opportunities in Asia, first and foremost in China, and in Latin America. New connections can also be established through digital insurance solutions or by way of cooperations with insurtechs. Another focus of attention is on developments in the start-up sector. Hannover Re participates in this segment as a reinsurer and supports companies in their market entry. Furthermore, the area of cyber risks still offers considerable additional potential as awareness of the risks increases. Structured reinsurance offers further scope for growth in covers taken out for capital relief.

In the present climate Hannover Re continues to concentrate on its core competence as a traditional reinsurer, supplemented by individual coverage concepts.

"Quick decision-making channels and flexibility as well as our market intimacy are the competitive advantages that our customers value," Henchoz said. "Emerging markets, in particular, still offer vast potential in terms of the insurability of risks and medium- to long-term growth."

In view of the business development so far in the current financial year, Hannover Re considers itself well on track to achieve its 2019 targets.

Based on constant exchange rates, the company still anticipates a single-digit percentage increase in its gross premium volume and net income in the order of EUR 1.1 billion for its total business. The result will additionally be positively influenced by a one-time effect from a participating interest in the amount of EUR 100 million. Achievement of the profit guidance is conditional upon major loss expenditure not significantly exceeding the budgeted level of EUR 875 million and assumes that there are no unforeseen distortions on capital markets.