MONDAY 23 MARCH 2020

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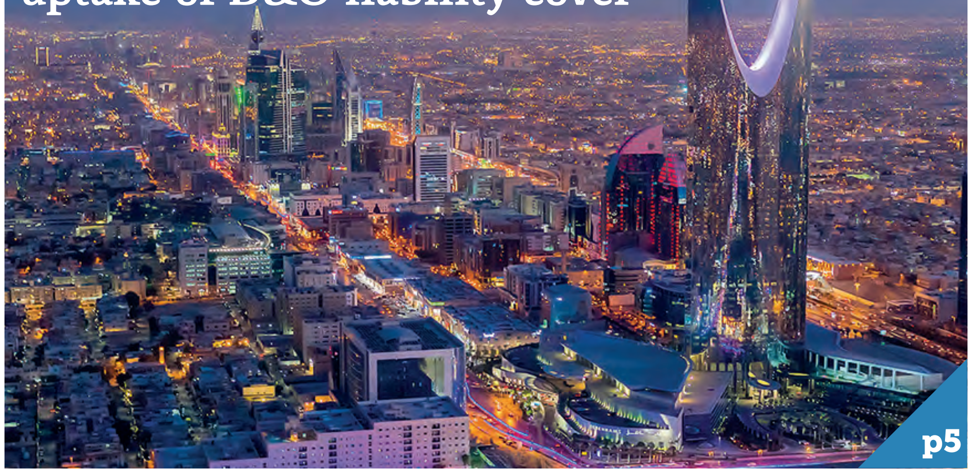

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Printed by Stroma, Unit 17, 142 Johnson Street, Southall, Middlesex UB2 5FD.

Print managed by Paragon Customer Communications.

Tokyo authorities say the Olympics will go ahead but the pandemic may force a cancellation

LILLIAN SUWANRUMPHA/ AFP via Getty Images

Swiss Re says cancelled Tokyo Olympics would cost it $250m

Underwriting impact of Covid-19 as 'entirely manageable'

Lorenzo Spoerry
Deputy editor

Swiss Re will pay out $250m in business interruption coverage if the 2020 Tokyo Olympic Games are cancelled as a result of the Covid-19 outbreak.

The Swiss giant also revealed it has a "mid-three-digit" million-dollar exposure for other events over the rest of the calendar year, which would potentially be incurred by the property/casualty (P&C) reinsurance and Corporate Solutions businesses.

Swiss Re calculated its overall market share for event cancellation insurance that could be claimed as a result of Covid-19 was close to 15%.

Assuming a $750m exposure to both the Olympics and all other events, this would put the total size of the market loss at about $5bn. UBS has previously estimated total potential business interruption losses between $7bn and $8bn, with about $4bn of this accruing to reinsurers. Munich Re has estimated the mass cancellation of major events because of coronavirus could cost it €500m ($534.8m) or more in 2020.

Japanese authorities say the Tokyo Olympics, which are due to start on July 24, will still go ahead, but many suspect the Covid-19 pandemic will force a cancellation.

The coronavirus has already led to the cancellation or postponement of a host of sporting events, including the Australian Grand Prix, the UK's Premier League, the Uefa Champions League, the National Basketball Association and National Hockey League and the Uefa Euro 2020 football competition.

The re/insurance industry's exposure to business interruption losses is likely be limited because typical business interruption coverage requires physical damage to a property to be triggered. Many policies, in addition, has explicit virus exclusions

John Dacey, Swiss Re's chief financial officer, said the impact of Covid-19 on both Swiss Re's P&C and life reinsurance operations is "entirely manageable at this point".

Rather, he pointed out, the major impact on the insurance industry is on the asset side of the balance sheet. He said Swiss Re entered 2020 with an "extremely strong" balance sheet and a "prudent" position on asset risk.

The company has also acquired hedges in February and March that have partially mitigated the impact of falling equity prices and widening credit spreads.

Japanese renewals, due on April 1, are "proceeding without any interruptions", Dacey said.

"Our reinsurance revenues are secure. On proportional coverage where primary companies' premiums are below expectations or may be below expectations, there may be some impact on our revenues, but we have yet to see anything material," he added. "There may be more impact on our primary business's revenues, but it's too early to say how much."

Japanese insurers' credit fundamentals remain unchanged: AM Best

The credit fundamentals of most insurers in Japan have not changed materially, even with the ongoing Covid-19 virus outbreak and plunging global stock markets, AM Best said, *writes Michael Faulkner*.

While the share prices of the major Japanese group have fallen as much as 40% since the start of the year, this was not a reflection of the business fundamentals of these groups and was "driven mainly by a company's sensitivity to equity price risk", according to the rating agency.

AM Best said it had "not seen any signs of significant deterioration" in the underlying profits of non-life and life insurance companies.

"Most domestic insurers maintain capital adequacy ratios and financial leverage ratios AM Best considers to be conservative relative to global peers, which should enable the companies to withstand adverse market conditions," the rating agency said.

With global financial markets expected to remain volatile over the near to medium term, AM Best said its view of Japanese insurers' financial strength would be largely subject to the development of oil prices, as well as the evolving nature of the ongoing Covid-19 pandemic, particularly in Europe and the US.

"A more pessimistic scenario would be the potential emergence of further events, such as a liquidity crisis, or the worsening of the pandemic and the result of a real and long-term disruption to the global economy," AM Best added.

NEWS

Covid-19 claims notifications 'rising for non-damage BI extensions'

Insurers yet to provide 'definitive position' on Covid-19 policy coverage, Marsh says

Scott Vincent
Editor, news serbices

Covid-19 unlikely to be covered as a notifiable disease on policies, Clarissa Franks says
DimaBerlin/Shutterstock.com

Quantification and measurement of Covid-19 business interruption claims are likely to throw up "significant issues", with most insurers yet to provide a definitive position on policy coverage, Marsh has warned.

While the requirement for physical damage is expected to limit coronavirus exposures for most property/business interruption policies, the broker said it was seeing many claims notifications for non-damage business interruption claims under extensions to policies.

Neil Greaves, leader of forensic accounting and claims services at Marsh, said coverage on non-damage business interruption extensions were typically "very policy-specific and often limited in terms of amounts and period".

Greaves said he expected significant discussions to follow regarding quantification and measurement, particularly related to wider-area damage.

For a retail business, discussions could focus on how the business would have performed even if denial of access had not occurred, given the wider disruption that has taken place.

Clarissa Franks, managing director and risk management placement leader at Marsh UK, said insurers have not yet given an overall coverage determination or stance for Covid-19 on any line of business.

Franks said the situation was rapidly evolving, adding it would be important to monitor the way governments seek to influence how insurance responds to the crisis.

"In the US, there is a rapidly gathering clamour for a federal stimulus that uses business interruption policies to pay claims, funded by government, even where coverage is excluded from those policies," she said.

Franks said property/business interruption policies could be triggered if the virus was found to be present on insured premises and provide cover for interruption for communicable disease, clean-up and decontamination costs.

"Many UK [property/business interruption] policies do not exclude pandemics but there is consistency in that all traditional policies require physical damage. It is unlikely reduced demand or disruption to the supply chain will be covered without physical damage," she said.

"However, many policies do contain certain coverage extensions that provide business interruption without physical damage. All of these have sub-limits with maximum indemnity periods, typically of around three months."

However, Covid-19 is unlikely to be covered as a notifiable disease on policies as it was not declared a notifiable disease under English law until March 5, Franks said.

Several other classes of business could generate claims, including general liability policies, which may cover customer illnesses, she added.

Pollution legal liability policies may cover clean-up costs, while employment practices liability policies may respond to discrimination claims and directors' and officers' liability policies may cover shareholder litigation, Franks said. In addition, credit insurance policies may respond to non-payment events.

Insurers running risk of unexpected Covid-19-related BI losses

The property/casualty (P&C) industry's initial forecast that business interruption losses tied to the coronavirus pandemic will be light may be overly optimistic, according to Keefe, Bruyette & Woods analyst Meyer Shields, *writes John Shutt, Los Angeles*.

Shields said the industry's loss exposure could be driven by a "combination of an aggressive bar, legitimately suffering insureds and potentially ambiguous policy language".

While it is too early to estimate industry business interruption losses, the majority of those losses are more likely to be borne by specialty carriers than standard insurers, Shields said.

Standard commercial multiperil insurers widely use the Insurance Services Office (ISO) form, which excludes coverage "from any virus, bacterium or other microorganism", he pointed out. Specialty carriers typically use less consistent, more customised policy language that is more prone to include unintended coverage.

In another sign of pressure on the industry, legislation has been introduced in the New Jersey Legislature that would require insurers to cover coronavirus-related business interruption losses for small businesses, even in cases where policies include the ISO's standard virus exclusion.

The bill would also establish a special fund that insurers could tap into to recoup those losses. Assemblyman Roy Freeman, who sponsored the bill, said insurers need to "do something above and beyond what is written into" policies.

American Property Casualty Insurance Association president, David Sampson, countered: "Gutting private contracts after the fact through government fiat is not insurance."

Meanwhile, California insurance commissioner, Ricardo Lara, has issued a notice asking all insurers in the state to give policyholders a 60-day grace period to make premium payments to ensure policies are not cancelled for non-payment owing to the Covid-19 pandemic.

Lara said the notice is directed to all admitted and non-admitted insurers that provide P&C, motor, life, health and other types of cover.

He also asked brokers agents, brokers and other licencees who accept premiums on behalf of carriers to take steps to ease customers' ability to make payments.

These steps include allowing alternate methods of payment, like online payments, and eliminating requirements for in-person payments.

Aon's Richard Dudley named Liiba chair

The London & International Insurance Brokers' Association (Liiba) has named Aon executive Richard Dudley as its new chair, *writes Michael Faulkner*.

Dudley, who is chief executive of Aon's UK global broking centre, succeeds Roy White of Marsh, who served a two-year term.

White will remain a deputy chair in the short term. Dudley's other deputies were confirmed as: Nick Cook of BMS and Alastair Swift of Willis Towers Watson.

Dudley's appointment comes as the London market grapples with the impact of the Covid-19 pandemic, as well as market modernisation and Brexit.

"Our immediate challenge is to provide support to our members and their clients as we face the coronavirus. Liiba and its members are determined to provide as close to normal service as we can while keeping to the prime minister's request we work from home where possible," Dudley said.

"We have much to do. With Brexit still very much a live issue and the Future at Lloyd's pushing ahead, this is an important time for brokers to make their voices heard.

"After the devastating floods seen in the UK this winter, climate change is also something that's occupying much of our members' time and energy. Insurance has a central role to play in both addressing the causes of climate change and helping communities and businesses recover from its near-term effects. We'll be enthusiastic contributors to the debates being facilitated by Eiopa and the OECD," he added.

Liiba has postponed its annual general meeting, which was scheduled for today, because of the coronavirus pandemic.

Market must develop more flexible solutions to the risk of vessel detention in the Persian Gulf

Iran's detention of the Stena Impero last year was one of several incidents involving shipping in the Persian Gulf

Hasan Shirvani/AFP via Getty Images

Shipowners are turning to strike and delay-type coverages to help mitigate against the high cost of marine war risk insurance in the region

Paul Park
Standard Club

The Strait of Hormuz connects the Persian Gulf with the Gulf of Oman and has always been a vital route for commercial ships to access five of the world's top 10 oil-exporting countries, as well as providing a passage to the world's largest liquified natural gas (LNG) exporter. According to the US Energy Information Administration, the daily oil flow averages 21 million barrels per day, or more than 20% of global petroleum consumption.

With only Saudi Arabia and the United Arab Emirates possessing the capability to move oil out of the Persian Gulf via pipeline, the Strait of Hormuz remains the world's most important choke point for seaborne oil and LNG.

During the course of last year a number of attacks occurred in the Gulf, not just on commercial ships but also targeting onshore facilities and military assets. The threat environment was notably heightened for ships transiting the Strait of Hormuz.

Although intended to indemnify the operator for lost earnings as a result of a physical loss, extended war loss of hire insurance is available to cover specific additional perils such as detention by a nation state

Four tankers were sabotaged in May 2019 and one month later two further tankers were attacked, apparently using limpet mines. In the months that followed, the British-flagged *Stena Impero* was detained by Iran in what was believed to be retaliatory action for the seizure by the British Royal Marines in Gibraltar of an Iranian ship suspected of carrying oil to Syria.

Processing facilities

Meanwhile, on land oil processing facilities in Saudi Arabia were targeted and significantly damaged by airborne drones and a US military base and the US embassy in Iraq were attacked in early 2020. Political tension between the US and Iran threatened to escalate into military action, with consequent risk to the safety of merchant shipping and potential for disruption or even closure of the Strait of Hormuz.

Last year was the latest year in more than three decades of intermittent unrest in the area. As well as attacks on commercial shipping, there has been a sporadic stream of rhetoric from Iran threatening to impose additional controls on shipping or block the channel altogether. But previous incidents were at a low frequency compared to 2019, with six ships attacked in a matter of weeks.

More than ever, shipowners need to evaluate their exposure to war and/or war-like events in the area and implement solutions to protect their assets and their people if a ship is attacked, detained, entrapped or otherwise restrained from trading to and from the area. One aspect of this risk assessment includes potential delays from imposition of Maritime Security Transit Corridors, where ships are obliged to wait and join scheduled convoys with a naval escort.

When looking at the risk management process, insurance is an important element. Typically, a main area of focus is securing protection against exposure to the significant costs involved in the event of a physical loss or detention. Most owners will be familiar with marine war risk insurance, which typically indemnifies the purchaser for hull or machinery damage caused by war risks, as well as detention or diversion costs.

Navigation and trade

Another area of focus is disruption to navigation and trade. It is likely any war and or war-like event in the Persian Gulf will lead to lengthy delays for ships trading in the area. The events of 2019 provide ready examples. Ships damaged by sabotage required inspection, possibly involving unscheduled drydocking and repairs before being declared seaworthy again. Ships that are detained, although not suffering physical damage, are unable to earn until released.

Even if the incident is not focused directly on the ship, it can be massively disruptive to maritime trade. Infrastructure damage to production facilities in Saudi Arabia had significant consequential effects on the volume of cargo available for transportation. Protests and strike action in Iraq meant ports were dysfunctional and ships suffered delays as a consequence.

Although generally intended to indemnify the operator for lost earnings as a result of a physical loss, extended war loss of hire insurance is available to cover specific additional perils such as detention by a nation state. However, the typical retention of the first 14 or even 21 days may be uncomfortable for owners, which prefer risk-transfer solutions that operate at a more primary level.

Other solutions are available to provide protection against the cost of ship delays at a lower level. Strike and delay cover is such a product, providing cover for delay arising from war and/or war-like events both onshore and onboard. Cover is available on an annual basis at predictable cost, without the significant additional premiums for calls to designated high-risk areas that characterise many marine war risk insurances.

Today's ship operators face more risk than their predecessors and some of that risk is less predictable. Fortunately, they also have a wider range of solutions to manage that risk and protect their interests than ever before. ■

Paul Park is strike and delay class underwriter at the Standard Club

Regulatory actions will drive uptake of D&O liability cover

Claims against directors and officers are set to increase as countries across the region align their corporate governance regimes with international standards and reporting requirements

Nicky Stokes
New Dawn Risk

Historically, directors' and officers' (D&O) insurance has not seen significant demand across markets in the Middle East. There have been a number of factors behind this. Perhaps most significantly, the region is home to a swathe of large and wealthy family-owned private companies, which have simply not seen the need for this type of risk transfer product.

With demand for D&O insurance low, pricing of the product has been relatively cheap and it has been viewed as something that is "nice to have" rather than a necessity. Furthermore, the litigation environment – a potentially key driver for claims to be brought against directors and officers – has been comparatively benign in the Middle East.

However, there are signs the situation is changing. Until recently there had been a patchwork of litigation regulation across region; requirements are different under United Arab Emirates' law from in the Dubai International Financial Centre, for example. But governments across the Middle East are keen to attract inbound investment into emerging markets and to compete with Western economies on a level playing field. To achieve this, standards of accountability and responsibility need to be approached in the same way. As a result, the regulatory burden is increasing as Middle Eastern states look to align with global standards and reporting requirements.

In Saudi Arabia there is a massive drive to regulate the financial services industry as part of the government's National Transformation Plan 2020 and Saudi Vision 2030, designed to reduce Saudi Arabia's dependence on oil, diversify its economy and develop public service sectors.

One key development among a string of reforms under Vision 2030 was the introduction of the Bankruptcy Law in 2018 to further encourage the participation of foreign and domestic investors by structuring the business legal framework and putting in placenew regulations governing businesses operating in Saudi Arabia. This is having a direct effect on directors and officers as it makes it much easier to identify where obligations have not been met. Where duties are codified into law, it is much more straightforward to bring a claim.

New regime

In another development, in December 2017 Saudi Arabia's Capital Market Authority introduced a new class action regime for

Governments across the Middle East are keen to attract inbound investment into emerging markets and to compete with Western economies on a level playing field

claims by shareholders of listed companies in the country – a first for the region. Earlier this year, the first lawsuit filed under the regime was brought against the former board of directors of Al-Mojil Group, its senior management and its auditor for alleged violations committed during the subscription in the company's shares as part of its 2008 initial public offering. We should expect more to follow.

Meanwhile, recent events have underlined the global nature of the insurance market. A combination of increasing litigation and regulatory risks, more notifications and profit pressures following years of premium reductions are prompting underwriters to carefully manage the capital they deploy for D&O risks. This has diminished insurer competition for buyers and resulted in higher rates and less favourable coverage terms for most buyers.

Rates for D&O insurance have been hardening in the UK (and latterly the US) for some time but in the past few weeks we have seen prices in the Middle East follow suit, broadly in line with US levels, with increases ranging between broadly flat up to 15% to 20%. Because the D&O market is comprised of a large number of international insurers, price changes in the region are being driven from a top-down perspective. Those that have been hit hard in terms of losses in the UK and US, for example, are looking to remediate their books elsewhere.

Saudi Arabia has kicked off a transformation of its financial services industry, bringing in new regulations to align its business laws more closely with Western standards

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Future threats

Looking ahead, risks facing directors and officers in the Middle East are broadly in line with those their counterparts are exposed to elsewhere in the world. Cyber is high on the agenda and there been a number of recent cyber events in Saudi Arabia that have hit both government ministries and petrochemical firms, generating significant losses with the potential to hit the D&O market. Saudi Aramco has seen an increase in cyber attacks since the final quarter of 2019, which the company has so far successfully countered, but is seeing a trend of increasing magnitude and frequency of incidents, a trend it expects to continue.

It is unknown at this early stage but likely we will also see a string of claims against directors and officers as a result of the coronavirus pandemic. The situation is changing rapidly but businesses in the Middle East and elsewhere should brace themselves for a likely flood of shareholder lawsuits.

We have already seen massive share price drops and if investors feel they were not fully informed about supply chain vulnerabilities or distribution problems, they may choose to litigate. While there is no guarantee these claims will be upheld, there is a potentially significant exposure to directors and officers in terms of defence costs.

Underwriters and brokers alike are tracking D&O developments in the Middle East closely. ■

Nicky Stokes is head of management liability and financial institutions at New Dawn Risk

FOCUS/ MIDDLE EAST

Civil unrest poses greatest challenge to the resilience of Lebanese carriers

Ongoing political instability in Lebanon remains a significant hurdle to reforming the country's beleaguered insurance market

Ben Diaz-Clegg and Ghislain Le Cam
AM Best

The Lebanese market faces significant challenges from the country's growing level of socio-economic instability

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Lebanon has a long history of economic and political instability. In the past, local insurers have been successful at navigating this challenging environment. However, recent civil unrest and ballooning public debt have increased the level of economic uncertainty, which is having a negative impact on the credit quality of Lebanon's insurance market.

GDP growth in 2018 fell to an 18-year low of 0.3%, according to the International Monetary Fund, and last year Lebanon's economic woes persisted, compounded by civil unrest and a tightening of liquidity by the banking sector, resulting in a significant disparity between the parallel market exchange rate and the Lebanese pound's official peg to the US dollar.

The social unrest that begun in Lebanon in October 2019 has highlighted the country's economic and political weaknesses. Shortly after the demonstrations began, Lebanon's prime minister, Saad al-Hariri, announced his resignation, leaving almost three months of deadlock during which Lebanon had no functioning government. In January 2020 Hassan Diab was appointed prime minister. The announcement was met with civil backlash, as Diab's appointment appeared to confirm the growing influence of the Hezbollah political movement, which, in turn, may have consequences for the country's ability to get foreign financing amid rising geopolitical tensions in the region.

Despite the government's best efforts to limit the outflow of US dollars, in 2019 the Banque Du Liban (BDL) reported foreign currency reserves had fallen below $30bn for the first time since 2012. In a bid to slow down the erosion of foreign currency reserves, the BDL announced foreign currency time deposits would be paid 50% in US dollars and 50% in Lebanese pounds. Since then, the Lebanese government has defaulted on its $1.2bn Eurobond, which matured on March 9, 2020. The BDL's inability to meet its financial obligations raises significant concerns regarding the adequacy of its foreign currency reserves, with a devaluation perceived as increasingly likely. This would have a substantial effect on inflation and increase claims costs for the insurance industry, putting pressure on technical performance.

Insurance overview

The Lebanese insurance industry has three main segments: life, medical and motor. Together, these accounted for almost 85% of gross written premium in 2018. Lebanon's largest gross written premium contributor, the life segment, is also one of its most profitable lines of business.

Unlike the highly fragmented non-life market, life insurance is dominated by the largest 10 players, which together accounted for 87% of the segment's gross written premium in 2018. Of these 10 companies, more than half benefit either from being part of a global insurance group or having exclusive bancassurance agreements. Those agreements give these companies a significant competitive advantage over smaller unaffiliated participants.

Bancassurance is a major distribution channel in Lebanon, particularly for life business, as it allows insurance companies to benefit from the banks' close relationships with their clients and to distribute insurance products, which can help reduce acquisition costs.

Medical insurance, the largest contributor to non-life gross written premium, has marginal technical profitability, with a five-year

The vast majority of Lebanese insurers' investments are exposed to domestic issuers and consequently to the socio-economic and political turmoil the country is experiencing

(2014 to 2018) average combined ratio of 99%, as calculated by AM Best. The profitability of the medical line has been pressured by competitive distortions, with caisses mutuelles (mutual insurers), which benefit from not being regulated by the Insurance Control Commission (ICC), imposing aggressive rates on the market. The profitability of the medical line is likely to remain under pressure, with price competition expected to remain a key feature of the segment.

The motor segment (21% of total mutual insurers in 2018) continues to have a negative impact on insurers' earnings, with significant competition and premium tariffs pressuring technical margins.

Moreover, Lebanese retail lines often demonstrate a heavy reliance on the costly broker network for distribution. That reliance contributes to inflated expense bases, with average commissions on motor policies around 25%. As a result, the expense ratio of the Lebanese motor insurance line of business is elevated, above 44% for the past five years (2014 to 2018). This contributed to poor technical results for the segment, with combined ratios of close to 103% over the same period.

Despite the difficult competitive environment within the motor and medical segments, the overall Lebanese non-life market has demonstrated its resilience. Insurers have leveraged their relationships with policyholders to offset weaker-performing motor business by cross-selling more profitable products such as fire, which in 2018 accounted for 6% of total mutual insurers. Consequently, the Lebanese non-life market has displayed an adequate level of technical performance over the cycle, demonstrated by a five-year (2014 to 2018) average combined ratio of 97%, as calculated by AM Best.

The technical performance of the non-life sector now faces additional challenges. In a highly dollarised economy, an increasingly likely devaluation of the Lebanese pound would result in inflationary pressures, which could weaken the profitability of the motor and medical lines, given both medicines and car parts are mostly imported. A small deterioration in the profitability of these two lines would be sufficient to offset the positive results achieved by smaller lines, such as fire and cargo, and move the non-life insurance technical result into the red.

Investment challenge

The Lebanese insurance market overall has an investment asset allocation that favours high levels of cash and fixed income instruments over higher-risk investments. This contrasts with the wider Middle East and north Africa region, where insurers demonstrate a much greater weight towards asset classes deemed more volatile, such as real estate and equities.

Nonetheless, the vast majority of Lebanese insurers' investments are exposed to domestic issuers and consequently to the socio-economic and political turmoil the country is experiencing.

Specifically, uncertainties regarding the credit quality of Lebanese government debt pose the most imminent threat to domestic insurers' balance sheets, with the trading value of most Lebanese Eurobonds decreasing to less than 30¢ cents on the dollar in early March, according to *Bloomberg*.

As the market values of Lebanese Eurobonds continue to fall, the risk the BDL will restructure or default on these securities increases. Either outcome would result in asset impairments, ultimately having a negative impact on the solvency of the Lebanese insurance market, given its heavy exposure to domestic fixed income securities. ■

Ben Diaz-Clegg is a financial analyst and Ghislain Le Cam is a director, analytics, at AM Best

Ripe for reform

The Lebanese insurance industry ripe for consolidation and regulatory reform. There has been long-standing pressure from industry stakeholders, such as the ICC, to strengthen the sector and align its regulatory framework with international standards.

In particular, the implementation of a risk-based capital regime, which has been under consideration by the regulator for years, could encourage market consolidation. This would partially alleviate competitive pressures on retail lines, while improving the overall financial strength of the market.

However, the ongoing political instability has been (and remains) a significant hurdle to the implementation of much-needed reforms. Bureaucracy, limited resources and the view there are more urgent issues on the government's agenda have impeded progress.

For example, the government is still to legislate for the implementation of compulsory motor third-party material damage insurance coverage. The legal framework has remained in limbo since 2015, following a collaboration between the National Bureau for Compulsory Insurance and the Association des Compagnies d'Assurances au Liban. Considering the ongoing socio-economic difficulties prevailing in the country, AM Best expects insurance industry reform will continue to be a low priority for the Lebanese government.

The increased social, political and economic instability in the country since October 2019 has exacerbated structural market issues that, in AM Best's opinion, could further weaken insurers' balance sheet strength. Since the onset of the social unrest, rated insurers have been proactive in implementing appropriate risk management actions. Measures have included triggering partial contingency plans, shifting investment exposure where possible and closely monitoring cashflows to limit the impact of a potential devaluation of the Lebanese pound.

Despite the management actions taken to date by Lebanese insurers, the mounting level of uncertainty in Lebanon implies operating conditions could rapidly deteriorate further. As the situation evolves AM Best will continue to monitor closely the ability of rated companies to meet their financial obligations as they fall due. ■

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Industry players must work together to benefit from the hardening market

It is critical insurers, brokers and reinsurers collaborate to leverage the best of their capabilities if the industry is to survive the disruption of technological and climate change

Rasaad Jamie
Global markets editor

It seems the particular way in which insurers are navigating the hard market environment today not only threatens to overshadow the potential opportunities that come with an increase in rates, but it also makes the sector more vulnerable to disruption by new entrants and the unprecedented threat posed by climate change.

The widespread dissatisfaction among corporate policyholders at the recent renewals with the reduced underwriting capacity on offer, the increase in exclusions and the lack of availability of cover for companies in certain industry sectors was acerbated by a general lack of transparency and poor communication on the part of insurers and brokers, according to surveys by the UK's Association of Insurance and Risk Management (Airmic) and Germany's Gesamtverband der versicherungsnehmenden Wirtschaft.

As technological breakthroughs continue to shape the modern world, the insurance sector is already at a disadvantage, lagging behind other industries

Changing market conditions

Corporates are only too aware market conditions are notably different from previous hard markets, which were cyclical and focused on price. These days, in addition to the reduced capacity, increase in exclusions and, in some cases, the complete withdrawal of cover, corporates risk managers are also very uneasy about changing claims behaviour on the part of insurers. This is represents a seismic shift in the insurer-corporate client relationship, according to a statement by Airmic last month.

As technological breakthroughs continue to shape the modern world, the insurance sector is already at a disadvantage, lagging behind other industries. However, compared with areas such as hospitality, airlines, transport and home entertainment, the insurance industry is yet to see a new entrant capture significant market share, according to a recent report by PwC. While there have been new entrants to the sector, incumbents have generally been able to withstand these challenges and avoid any material loss of their customer base.

Up to now, incumbents have been able to resist disruption because of three major challenges for new entrants into the re/insurance sector: the importance of a trusted brand, the high levels of customer inertia and the high business acquisition costs.

Customer appetite for new products and services in large corporate insurance, although growing rapidly, is still not as strong as they are in other sectors. In addition, legacy processes and operations, particularly in the London market, also serve as a barrier to disruptive technology intervention. Furthermore, other change factors such as talent and regulatory change are less mature in comparison to other sectors.

But things are changing, as evidenced by corporate policyholders' negative response to the way the industry is managing the hard market conditions at present.

It is clear there is a limited interim period before real disruption occurs in the re/insurance sector for insurers to address this challenge by co-operating and working closely with brokers and reinsurers to become more customer-centric, make better use of technology to improve service and provide more innovative solutions.

Competing for client ownership

But even here, there are challenges. At the same time as policyholder dissatisfaction is rapidly increasing, so too is the blurring of roles between broker, insurer and reinsurer as they compete for more complete ownership of the corporate client. Brokers are increasingly assuming tasks traditionally performed by underwriters, such as the provision of advisory services and the pricing of risks. Meanwhile, insurers and reinsurers are increasing the contact they have with their insureds and performing some of the services historically provided by brokers.

But more urgently for the re/insurance industry, more considerable pressures in the form of macro trends, notably climate change and now coronavirus, are irrevocably changing large corporate customers' risk exposures and materially shaping their expectations.

Climate change and the increased likelihood of natural catastrophes create both a risk and an opportunity for corporate risk insurers. According to a recent report by AM Best, total economic losses from catastrophes in 2018 came to $165bn and insurance only covered $85bn of this, the fourth-highest payout for a single year ever. Indeed, the nine highest payout years for catastrophe losses have all occurred since 2004.

The main message here is there are roles for all industry players in a disrupted re/insurance market, but this will involve insurers, brokers and reinsurers collaborating in a very focused way in "ecosystems" that leverage the best of the capabilities of all participants. ■

Insurers, reinsurers and brokers will need to collaborate to become more customer-focused and avoid disruption

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