



New RMS Model 9.0

According to Press Release in August, new models will likely result in reduced earthquake loss scenarios in the US:

- 10 to 25 percent on average for insurers across all lines; reductions will be higher for residential and lower for commercial.
- In California, reductions will be 5 to 15 percent for commercial and 25 to 35 percent for residential with greater reductions in San Francisco than in Los Angeles. LA could now account for more than 60 percent of insurer CA risk.
- Most of US and Eastern Canada will see moderate decreases.
- Pacific Northwest, Southeast and Western Canada expected to increase in certain areas.



PROPERTY INSURANCE MARKET UPDATE OCTOBER 2009

The global financial crisis which began in late 2008 has played a key role in the profitability and underwriting results of insurance companies over the last 12 months. According to ISO, from a profitability standpoint, the first quarter of 2009 was the worst first quarter results in 20 years. In addition to the devastating financial market conditions, the worldwide economic crisis put pressure on the insurance industry in the form of lower demand for insurance, which has resulted in lower net written premiums.

On the upside, 2009 has proven to be a very good year thus far from a Catastrophe (CAT) loss standpoint. In stark contrast to the \$26 billion in CAT losses in 2008, if the current hurricane season comes to an end without event and the financial markets regain stability, carriers stand to make a substantially profit in 2009. The turn around in investment results will contribute to profitability across the industry similar to 2006 and 2007 levels. Forecasters are predicting lower Atlantic hurricane activity particularly given the development of El Nino conditions in the Pacific. With increased profitability and abundance of capacity, the likelihood of a stable or even soft market is high.

With that said, there is still pressure on the profitability and returns for the insurance industry. There is concern in the industry that a single, major property and/or financial loss could send the property market into a hard market. Volatility in the investment market would only exacerbate the situation.

To complicate matters, the losses from Hurricane Ike, which made landfall in September 2008 as a Category 2 storm, caused much more in insured losses than the models had predicted. Part of the problem was that many of the properties in Texas were poor-quality construction, which was not only not contemplated by RMS but caused them to sustain damage even at relatively low wind speeds of less than 70 miles per hour. The lessons learned from Hurricane Ike could take up to two years to be reflected in the models. Much like what occurred after Hurricane Katrina, this may contribute to insurers adopting even more conservative approaches to underwriting CAT exposed risks.



With all of these factors in play, there is little consistency in renewal results. Rates, premium increases, available capacity and even insurer appetite are all over the board. New CAT capacity comes at a premium, while non-CAT limits are plentiful and rates declining. Between January 1 and July 1, 2009, renewals on middle market accounts with minimal CAT exposures remained competitive, with many enjoying rate decreases or even flat renewals. However, accounts with exposures for windstorm and California earthquake have seen increases in the range of 5 to 15 percent for that same time period. For accounts that were more than 20 percent CAT exposed or had had windstorm losses, increases could be even higher.

Since July 1, the property market seems to have stabilized, particularly as respects to CAT exposed risks. It appears that middle market risks with CAT exposures that require earthquake or wind coverage are receiving the brunt of the increases. This is partially due to the fact that with limited amount of CAT capacity available, many standard and excess and surplus lines markets are not as interested in offering capacity to small or medium accounts where they may not get the amount of return that they require. In other words, carriers are not willing to offer inexpensive CA earthquake or wind capacity regardless of whether the actual exposure is minimal.

Carriers are beginning to adopt the RMS 9.0 modeling system. Some carriers are in the process of implementing the new model but many are still in the test phase. It is widely anticipated that the newly updated model, which has adopted new ground motion attenuation relationships from the Next Generation of Attenuation (NGA) models, will lead to lower U.S. earthquake insured loss estimates for commercial and residential properties. The average reduction for insurer loss estimates across all lines of business will be 10 to 25 percent depending on the specific characteristics of the insured property. Residential-type properties will benefit from a bigger reduction than commercial properties, and high-rise construction will have a bigger reduction than low-rise construction.

The turmoil surrounding AIG, which was formerly one of the largest property insurers in the United States, has put an additional strain on the property market. AIG P&C has announced its separation from the parent company and the introduction of their new brand named Chartis. As a result of the turmoil, Chartis has taken a more conservative underwriting approach, cutting back on CAT aggregates and raising rates on certain CAT-exposed risks. However, by doing so, there has been a leveling of the playing field wherein other markets have had the greater opportunity to participate in primaries. In the end, greater competition is beneficial to clients who will have greater access to more markets.

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