

to their cash reserves, maintain their liquidity, bemoan climate change and hurricane losses but on the whole give a positive outlook. The international reinsurance industry, with few exceptions, has posted major losses in the Third Quarter of 2008 as catastrophe claims in the wake of the Atlantic hurricane season take their toll and the global credit crisis punished stock values wiping billions of dollars off of share prices.

The probable impact of this for the next two years is that capacity, good capacity, is going to be costly and fairly inflexible. Event limitations, whilst not new to some cedants, will probably be universally applied as financial markets have now found that there is indeed a glass ceiling and investors will expect reinsurers to put a fixed limit on their exposures to natural catastrophes.

For primary insurers, premiums are going to be under massive pressure, particularly for companies that rely on vehicles and property sales fuelled by bank loans. In developed markets some premium shrinkage should be expected in the 2009 underwriting year, attributable to a reduction of finance for residential construction projects, devaluation of property values and generally less of the type of household consumerism that is fuelled by easy access to finance. So much of a developed market's premium income is derived from credit transactions.

Africa as a Continent will suffer from the global credit crisis. Economic growth forecasts for Africa have been revised downwards by as much as 20% following the global credit crisis. Demand for base metals and minerals will reduce as developing nations curb their rampant consumerism, we should expect to see less project finance availability, developing nations and NGO donor aid will be decreased, and Africans working in developed countries will be sending less money home.

It should be expected that catastrophe events will continue to be experienced with the same frequency and severity as this year and therefore reinsurers will need to stand firm in their pricing models in order to provide reserves for future catastrophe claims.

In one month the outlook for reinsurance capacity and pricing has changed from favourable to challenging. This situation is likely to continue into 2010. However, primary

insurers who are able to show a history of consistent underwriting profitability over the past three years should be able to continue to enjoy good levels of support from reinsurers.

Entire insurance industry affected - Achim Klennert, Managing Director, Hannover Re Africa Group



"High loss activity and financial turmoil has affected the entire insurance industry in 2009."

Despite the extreme turbulence in current financial markets, we are positive about market needs expected to arise in 2009.

In response to the turmoil in financial markets, Hannover Reinsurance Group (Africa) has repositioned the company's investment portfolio by disinvesting from equities and reinvesting the proceeds in government bonds and short-term cash to ensure solid capitalization and a sustainable long term outlook with continual access to capacity. In addition, the company will not be exposed to significant negative implications as a result of the international financial market crises.

High loss activity and financial turmoil has affected the entire insurance industry in 2009 and we will focus on ensuring availability of secure and viable insurance in the region. The international environment has been affected by global economic instability which also saw Hannover Re Global's profits for the third quarter of 2008 decline in the wake of the capital markets crises and the burden from catastrophe losses, which were higher than anticipated.

The year 2008 has definitely tested the resilience of financial services companies but we have remained strong in our claims paying ability and commitment to clients and markets, positioning ourselves to take advantage of business opportunities expected to arise for 2009.

Difficult year ahead - Mark J Haken, Cotswold Reinsurance Services (Pty) Ltd



"We are on the verge of a significant swing towards a prolonged period of technical precedence."

Professional reinsurance companies are forever grappling with the dilemma – technical underwriting versus premium income (growth). Models to calculate correct technical rates for all manner of risks are becoming ever more sophisticated, so the internal debates between the actuaries and the marketers are ongoing and predictable. It's certainly of no use being technically "correct" with no premium, but equally ineffective to write large volumes of premium with huge underwriting losses. The pendulum swings between the two extremes, and I predict we are on the verge of a significant swing towards a prolonged period of technical precedence.

Such a swing will be accompanied by real and substantial increases in excess of loss rates, and reductions in levels of commissions on any proportional treaties which are not producing meaningful underwriting profits. Facultative business will certainly be more closely examined and scientifically rated, all of which will put enormous pressure on the primary market to significantly increase insurance rates.

The reasons for this gloomy prediction are several and varied: -

1. There are the current year's underwriting results in the local market. We have been beset with several very large single risk losses as well as two medium sized catastrophes in the Western Cape and KwaZulu-Natal. Local professional reinsurers will struggle to operate at combined ratios of below 100% this year

2. The hurricane season in the N Atlantic is as yet unfinished, and has already yielded losses in excess of US\$ 52 billion according to Wikipedia. Whilst they will not all be insured losses, they will have an impact on reinsurer's results.

3. Access to additional capital is virtually non-existent in the current markets so extra care needs to be taken to protect that which they have.

4. Whereas the investment and underwriting environments are often counter cyclical, in 2008 they are simultaneously deteriorating, with investment returns likely to be minimized or even negative.

5. The ongoing consolidation of the local insurance market – the acquisition of MUA by Santam, the tribulations of AIG and the imminent sale of M&F – has the effect of reducing the pool of premium which is available to reinsurers.

6. The expected increased incidence of losses which inevitably accompanies an economic downturn such as we are in the throes of experiencing. Losses increase for a multiplicity of reasons not least being cost cutting on risk management measures and spurious or "self inflicted" claims.

7. Finally, I surmise that the full impact of the sub-prime crisis has not been fully quantified or recognized by the international (re)insurance market, and consequently there will be a need to take cognizance of that.

Thus the only source of respite for the reinsurance market will be via their underwriting accounts as this is the area over which they are able to exercise most control. That said, the renewal season will be tough and eventually expensive for the insurance companies and that cost will inevitably be passed on to the already beleaguered insuring public. I hope I'm wrong.....

Outlook Remains Stable - Fitch released an outlook for the global reinsurance sector, which we reproduce for your interest

Fitch Ratings' rating Outlook on the global reinsurance sector remains Stable. The agency believes that individual companies' operating performance, capitalisation, and anticipated market conditions, despite their deterioration over the past year, will continue to support current ratings over the next 12-18 months.

“The sector will continue to generate reasonable returns on capital.”

Fitch believes that the non-life reinsurance sector will generate an underwriting profit in 2008, assuming normal catastrophe-related losses. Non-life reinsurers have generally maintained underwriting discipline. Given pressures such as declining investment income and capital flows out of the sector, Fitch believes this discipline is likely to be maintained over the next 12-18 months.

“While underwriting margins are likely to continue to erode over the near-term, unless there is a major catastrophe event, the sector will continue to generate reasonable returns on capital,” says Mark E. Rouck, Senior Director in Fitch's Insurance rating group. “Fitch does not see a ‘tipping point’ in the foreseeable future at which reinsurers' operating performance and market conditions no longer support a Stable rating Outlook.”

For life reinsurers, Fitch believes that market conditions and individual companies' performances will remain largely unchanged over the near-term. The agency has heightened concerns about life reinsurers' asset quality in the face of deteriorating credit and financial market conditions but these concerns do not appear significant enough to affect the rating outlook.

Nevertheless, market conditions in both life and non-life reinsurance are closer to those that would cause Fitch to revise its rating outlook to Negative than they were at this time

in 2007.

“The reinsurance sector is not emerging from the last twelve months completely unscathed,” says David Stephenson, Director in Fitch's Insurance Rating Group. “Underwriting and investment conditions are clearly less favourable than they were a year ago, and capital cushions have been partially eroded. While Fitch does not expect the cyclical deterioration in market conditions to be deep or prolonged enough to change its Rating Outlook to Negative, the deterioration is closer to such conditions than it was a year ago.”

For non-life reinsurers, conditions

that could push the outlook to negative include deep and prolonged soft market conditions, especially if coupled with investment market or “shock” catastrophe-related losses. While the agency does not believe that projected market conditions over the next 12-18 months constitute a “deep and prolonged” soft market they are closer to such conditions than they were a year ago.

For life reinsurers, the outlook could change to negative if widespread declines in asset-quality or fundamental changes in factors affecting product demand, such as a significant change in regulatory reserving requirements or a dramatic increase in the use of substitute products, were expected. Although the agency does not believe that asset-quality will deteriorate to the point that it affects the rating outlook, asset-quality in the first half of 2008 has deteriorated. ◆

Fitch's special report, entitled “2008-2009 Global Reinsurance Review and Outlook” is available on Fitch's website www.fitchratings.com.

