When it rains, it pours

Jo McIntosh

This article looks at how local and global events can affect your insurance coverage and specifically the effect on standing timber insurance. We then discuss what steps you can take to optimise your insurance arrangements and costs.

They say when it rains, it pours, and that certainly has been the case recently in the New Zealand insurance market. The Insurance Council recently advised that there have been $2.5 billion of insured losses in New Zealand over the last 12 months, saying '2017 has been a huge year for New Zealand with earthquakes, floods and fires hitting us hard.'

The Kaikoura earthquake accounted for around $2 billion, with other claims such as the Port Hills fire and weather-related damage from cyclones Debbie and Cook also having significant effects. We have had our fair share of natural catastrophes, exacerbated by other recent events, including the devastating Christchurch earthquake, which the Insurance Council have estimated the costs so far as $19 billion.

An interesting insurance market

New Zealand is an interesting insurance market. We are fortunate to have one of the highest uptakes of property insurance in the world and traditionally, insurance is more affordable here than in other parts of the world. For example, it appears that up to 85 per cent of Houston home owners did not have flood insurance. The effect on New Zealand's insurance rates and capacity as a result of these local events is developing, as well as the increased frequency and cost of global ones such as hurricanes Harvey and Irma.

Tim Grafton from the New Zealand Insurance Council recently commented that we are currently in renewal and reinsurance season. However, the past 12 months of experience in New Zealand will have more of an effect on reinsurance costs than what is happening around the world. He continued to add that the jury is out on the effect the four hurricanes and earthquakes in Mexico will have on global reinsurance costs.

> 'I do not think it will be enough to affect the global market, which is awash with capital.
> The earthquakes in Mexico would bring total insured losses of around US$2 to $3 billion and most of that would come from commercial losses as Mexico is under-insured in personal residential property.
>
> Insured losses from the recent hurricanes are still unclear but early indications are within $30 to $40 billion. Reinsurers indicated they estimated there would need to be over $100 billion in insured losses suffered for there to be a significant market shake that would affect New Zealand. Reinsurers and insurers would predominantly base their risk assessment on local historical events such as the Canterbury and Kaikoura earthquakes.'

Reinsurance

Most New Zealand retail insurers have significant reinsurance arrangements to protect their financial position and ensure they can pay claims. While these reinsurance structures differ between insurance companies, most have a loss limit on the amount they pay for a natural catastrophe such as an earthquake. Once a claim goes over the nominated loss limit, the reinsurance is activated and the reinsurer pays above this limit. A significant portion of the money which has been flowing into New Zealand over the last few years to pay for rebuilding and claims is from these reinsurance recoveries.

Like most of us, the retail insurers have an annual insurance renewal. They need go to the global insurance markets to arrange their reinsurance programmes for the following year. Generally this has proved to be progressively more expensive for New Zealand retail insurers, particularly in the property market. While there is still insurance capital available, the costs are generally increasing as reinsurers harden their position on New Zealand and price the risks to reflect their exposures and loss experience as well as to generate a return.

This increased reinsurance cost ultimately flows through to the price you and I pay for our insurance.

Market effects

In terms of standing timber insurance, fortunately this policy line mainly sits outside the property insurance pool as far as insurers are concerned. However, there have been losses and there is some pressure on reinsurance costs. As a result, many of you will have seen a modest rise in rates over the last two years. This upward pressure on standing timber rates has been offset by increased insurer competition and generally the premiums we are paying today remain below that paid in 2011.

The liability insurance market is also being kept in check by very good local competition, unless you have had claims or are in a particular sector not favoured by liability insurers. Pricing is currently relatively stable. Most of the pricing movement is tending to be in the property insurance market. Property pricing is generally increasing for the reasons discussed above.

Certain regions, such as Wellington particularly, are facing large premium increases and pressure on terms due largely to earthquake risk. There are some property risks which are perceived as so unattractive that they may struggle to find an insurer. Insurers are underwriting risks with much more care and paying great attention to the construction, age and location of property. For some property owners the terms of cover may also, for example increased natural disaster excess conditions.

Timing is everything

Because we are in a hardening market cycle for property insurance at the moment, the insurance industry was particularly disappointed with the government's introduction of two new tax increases and the cumulative effect this will have on insurance costs. From July this year, there was a 40 per cent increase in the Fire Service Levy used to fund the fire service. The fire service benefits all New Zealanders and it is unfair to have only those who insure pay for these costs.

On top of this, from 1 November there was a 33 per cent increase in the Earthquake Commission levy applied to house and contents insurance. Both of these levies also have GST applied to them. This affects commercial premiums but also means people with house and contents insurance will be levied and taxed over $450 without even counting the 15 per cent GST applied to the premium that the insurer charges.

The worry is that people will start cutting back on insurance and deliberately under-insuring by reducing values or limits or, at worst, not purchasing any insurance at all. New Zealand is very prone to natural disasters. We certainly do not want an increased number of New Zealanders exposed to great hardship if they are under insured or not insured in a natural disaster.

The Insurance Council has said 'Does New Zealand continue to go down the path of making it increasingly difficult for low income people to protect themselves, or should we really be addressing our vulnerability? General taxation should fund the Fire Service which benefits everyone, insured and uninsured alike. The Crown balance sheet is now strong and can bear the $1.75 billion exposure that the EQC levy seeks to fund.'

What you can do to minimise these effects

It is very important for you to consider your risk exposure and manage this exposure with astute insurance placement. Talk to your adviser in advance of your insurance renewal and get an indication on pricing so that you can budget and plan. Make sure you have read and understood the policy and coverage offered.

For those with commercial property insurance, it will be vital to talk to your adviser well in advance of your renewal. You will want them to work with you to prepare a quality submission to insurers. This may mean you will need to provide extra information such as detail on construction, earthquake strengthening and details about how a building compares to the New Building Standard which is usually expressed as a percentage. If purchasing new property check in advance with your adviser that it is insurable, get an indication on premiums and understand what information will be required.

Finally, please do not cut corners and or take the risk of not insuring or under-insuring. Having worked with clients following losses, it is stressful enough and tough enough without the very real benefit of insurance assistance. I am proud of the work Aon have done with our clients, the planning and conversations over the years has resulted in them having good cover in place, at a time when they really needed it. As a specialist forestry broker, Aon keeps abreast of developments and works with you to optimise your risk and insurance.

You need a good umbrella.

Jo McIntosh is an Executive Director of Aon and specialises in insurance for forestry and horticulture.