CENTER FOR INSURANCE
POLICY AND RESEARCH

Reinsurance Brief

Continued Discipline, Capacity Rebound, Pent-up Demand

Mid-year Renewal Insights–Property CAT Reinsurance

September 2023

Shaveta Gupta
CAT Risk and Modeling Advisor (CAT CoE)

NAIC
NATIONAL ASSOCIATION OF
INSURANCE COMMISSIONERS

Summary

- **Continued Discipline**—Reinsurers are being prudent and cautious in deploying capital.
- **Rebound in Overall Capacity**—Reinsurers are showing appetite to support current terms and grow in target areas.
- **Pent-Up Demand**—Insurers are accepting the increase in price for favorable terms and conditions.

The global reinsurance market plays a critical role in managing catastrophic risk for companies worldwide, especially in the U.S. The P&C reinsurance market in the U.S. features a mix of domestic and international reinsurers. The market is characterized by its dynamic nature, influenced by regulatory changes, natural catastrophes, and evolving market conditions.

At mid-year renewals, challenging risk environment and investor pressure continues for global reinsurance markets to generate sufficient returns to meet cost of capital requirements. Even though inflation has eased as compared to the last 12 months, it remains a concern alongside other economic and geopolitical factors.

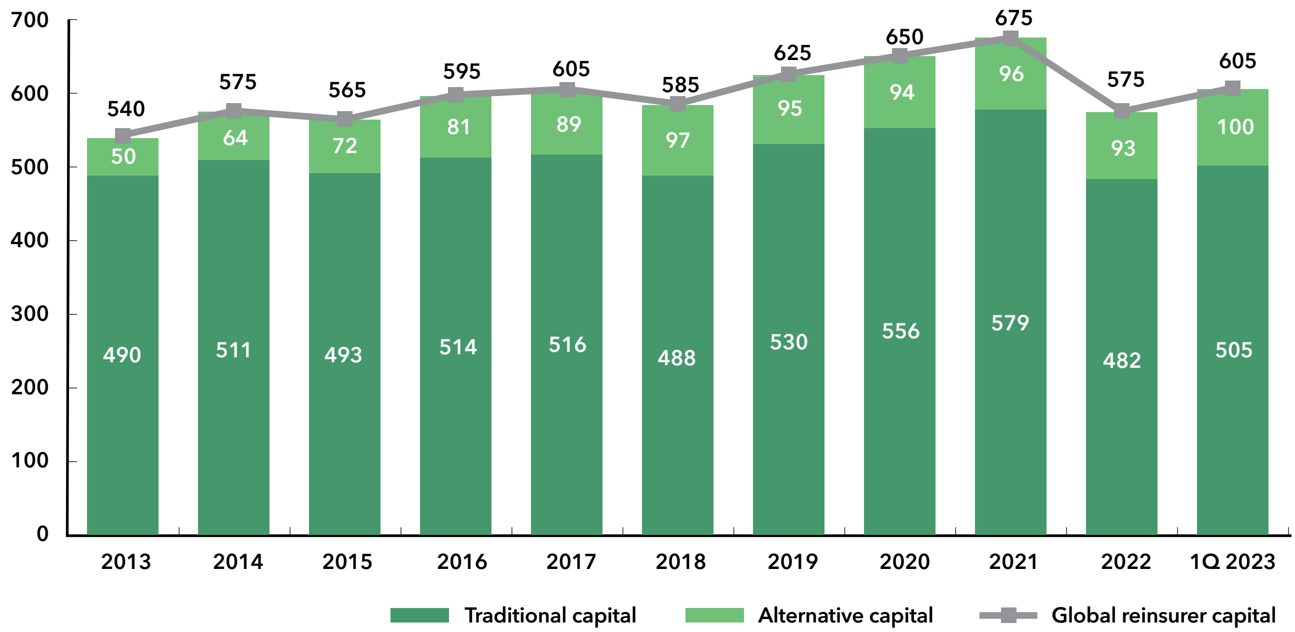
Reinsurers continue to be prudent and cautious in deploying capital, maintaining underwriting discipline by moving away from lower and middle layers and tighter coverage terms and conditions within the property catastrophe market. This trend is likely to continue for a longer period as compared to some of the past cycles of hard reinsurance market conditions.

Conditions have improved slightly as compared to January 2023 renewals that saw mismatch of supply and demand. Mid-year renewals witnessed moderate rate activity, rebound in overall available capacity, and insurers accepting the increase in price for favorable terms and conditions.

NAIC Disclaimer

Capacity Rebound

As per Aon's latest analysis, reinsurer capital increased by 5%, or $30 billion for the first quarter of 2023, as earnings were strong and catastrophe bond markets rebounded. Though capacity still has not returned to 2022 mid-year levels, reinsurers have shown appetite to support current terms and grow in target areas.



Sources: Company financial statements/Aon's Reinsurance Solutions/Aon Securities, LLC

Reinsurer appetite remains strongest at the top end of programs but constrained in the lower-middle layers of catastrophe programs, and catastrophe losses in the first half of this year suggest the burden of high frequency catastrophe events have now shifted toward insurers, with fewer ceded losses for the reinsurance market.

As per the rating agency AM Best, reinsurer capital adequacy generally remains strong under risk-based regulatory and rating agency capital models, which also considers a more economic view (interest rates, investment, and asset risk) of the current situation in addition to the catastrophe risk. Based on market performance, further recovery of reinsurers' shareholders' equity is expected in the second quarter of 2023. Reinsurers are seeing improvement in financial results and operating performance for the first half of 2023 as compared to the 4.5%-5% average return on equity (ROE) observed for the last five years.

Demand

As per the latest reinsurance market dynamics report from Aon, demand for property catastrophe reinsurance protection for 2023 remains strong and is now expected to increase by high single digits globally or as much as 10% for U.S. catastrophe as insurers look to reduce net exposure and/or secure capacity ahead of 2024.

While headline inflation has begun to ease in most key markets, it remains a key factor driving demand, with increased claims cost now being felt across property and casualty lines. Combined with anticipated updates to vendor catastrophe models (one of the key tools used by the market to estimate catastrophe exposures), inflation is likely to support increased demand for reinsurance protection into 2024.

"For Property CAT, a strong demand for limit persists, but market corrections have rebalanced the supply/demand disparity faced by many regions a year ago." **—Guy Carpenter**

Pricing

The latest mid-year renewal report from Guy Carpenter indicates firm pricing with a wide range of risk-adjusted rate changes seen throughout individual layers. The same report sighted that global property catastrophe reinsurance risk-adjusted rate increases ranged from +10% to +50%, with loss-impacted clients often seeing even higher pricing.

In the US, property catastrophe reinsurance risk-adjusted rate increases were on average the highest in 17 years, with loss-free accounts generally up +20% to +50%. The preliminary year-to-date Guy Carpenter US Property Catastrophe Rate-on-Line Index, an alternative measure of price change that incorporates the impact of structural adjustments and current views of risk on actual dollars paid, increased 35% for January through July renewals.

"The preliminary year-to-date Guy Carpenter US Property Catastrophe Rate-on-Line Index increased 35% for January through July renewals."**—Guy Carpenter**

Regional Coverage Trends

"Generally more appetite for nationwide carriers than the Florida domestics which have been financially strained by insolvencies over the last 12–18 months."—**Gallagher Re**

Retention levels generally increased at mid-year, although the availability of capacity led some insurers to explore opportunities to revisit retentions set when capacity was more constrained. Having taken significant increases in retention levels at renewals in 2023, retention levels are expected to stabilize now.

Florida – Tort reform and state reinsurance support helped attract capacity to Florida, which showed encouraging signs of a return to stability at mid-year. The reform should also help attract additional reinsurance capacity to the state going forward.

As per Gallagher Re, mid-year 2023 painted a very different picture in the sunshine state. There was generally more appetite for nationwide carriers than the Florida domestics, which have been financially strained by insolvencies over the last 12-18 months.

Considerably higher rates-on-line available on Florida homeowners' reinsurance layers below the CAT fund and significant rate increases higher up the towers, attracted back a wide range of reinsurers (Berkshire Hathaway, DE Shaw, Arch, and Ariel Re). This was a drastically different story as compared to the 2022 renewal cycle, where many companies were not able to fill layers at the bottom end of programs.

"Increases in retention levels and the lack of aggregate covers has left insurers with significantly reduced reinsurance protection for frequency perils like severe convective and winter storms."—**Aon**

US Regionals – The impact on U.S. regional and mutual insurers observed a combination of increased reinsurance costs, higher program retention levels and the reduction of aggregate reinsurance protection from the market.

The increased frequency of secondary perils is a particular challenge for regional insurers. Losses from U.S. convective storms in the first quarter of 2023 alone were more than $5.5 billion, representing an active start to the year.

Increases in retention levels and the lack of aggregate covers has left insurers with significantly reduced reinsurance protection for frequency perils like severe convective and winter storms.

Outlook for January 2024

Despite the devastating earthquake in Turkey and Syria, elevated severe convective storms in the U.S., and the Canadian and Maui wildfires, catastrophe activity in 2023 to date was relatively stable for the mid-year renewal. AM Best reported that the first half of 2023, reinsurers are seeing promising results as compared to the prior two years and an improvement in operating performance. There is still uncertainty and concerns due to other factors related to economic and social inflation and market volatility.

Catastrophe activity in the remainder of 2023 will be key for January 2024 renewals especially for the North Atlantic hurricane season. The U.S. weather service NOAA has effectively doubled its forecast outlook for activity in the 2023 Atlantic hurricane season, now predicting a 60% chance of an above normal season, double its 30% prediction from back in May. As per many industry analysts, if the hurricane season is more impactful in terms of loss activity, pricing could end up higher for January renewals.

"A developing track record of stronger results may draw new capital commitments ahead of the January 2024 renewals, subject to the outcome of Atlantic hurricane season."
—Aon

References:

1. Aon: Reinsurance Market Dynamics
2. Guy Carpenter: Reinsurance Market Continues to Recalibrate at Mid-Year 2023 Renewals
3. Gallagher Re: 1st View: Continuing Discipline
4. AM Best: Global Reinsurers Face Challenges Even as Conditions Improve
5. 2023 Hurricane Season Forecasts & Predictions