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GUY CARPENTER OLIVER WYMAN

9th Sept 2009

The Casualty Market A Broker's Perspective

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Economic Backcloth

Challenging Times

Sub-Prime & Credit Crunch – Impact on Insurance

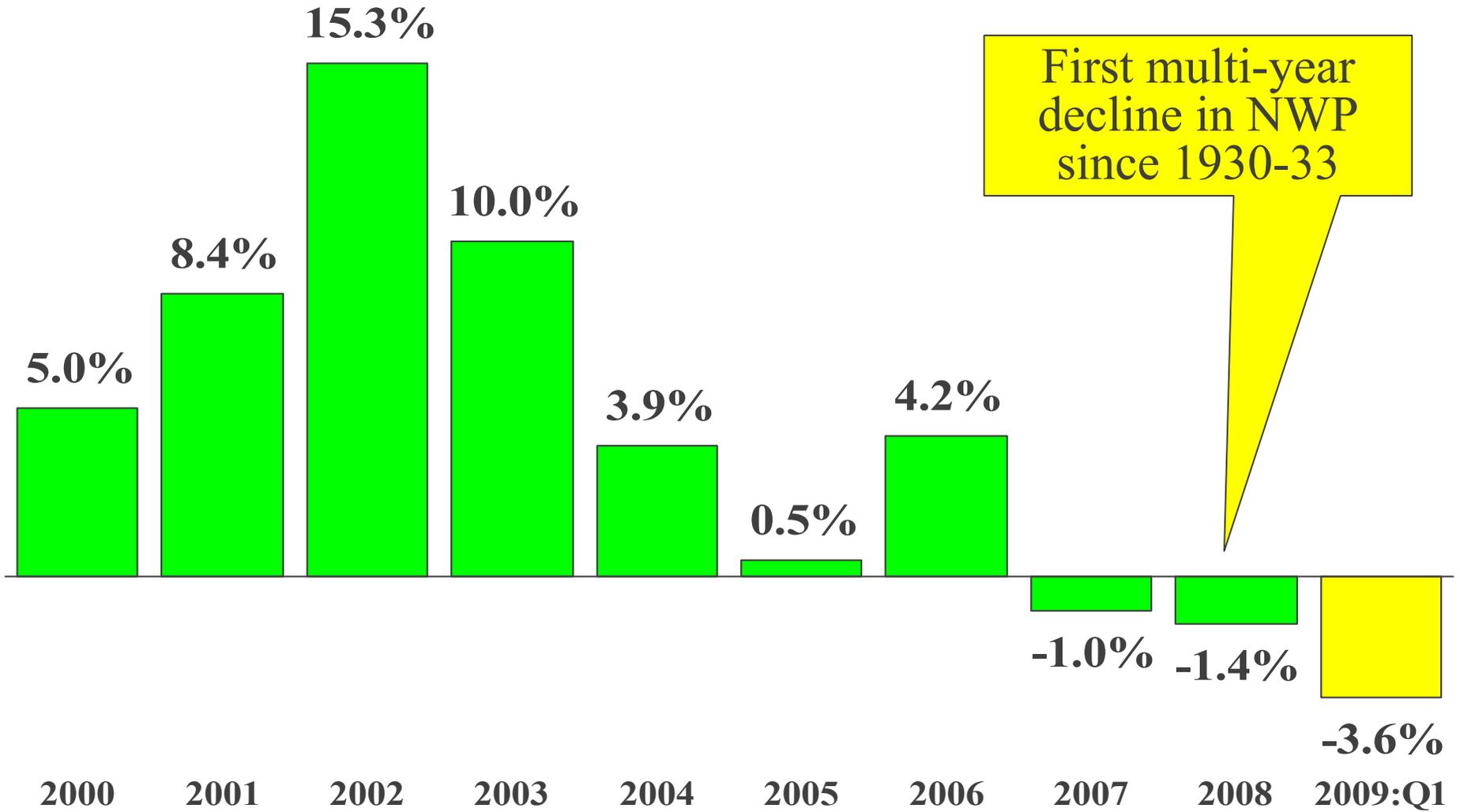
- Inventory, cargo, logistics, travel, people, leisure all caught up in “ripple” effect
- Aircraft & Ships mothballed but Capital projects brought forward
- Orders shrunk, cancelled or deferred coupled with Short time working
- Replacement & Maintenance programmes deferred or delayed
- More Banking covenant & Supply chain defaults
- Sale or closure of clients non-core business activities
- More Regulatory oversight
- Solvency II + Securities Risk + FOREX volatility could = More conservative investment strategy, change in insurers risk appetite & capital allocation strategies.
- More Business to Business disputes.
- More Litigation and Large claims challenges.
- Credit Crunch plaintiffs go looking for deep pockets.
- Divergent insurer behaviour “Dash for Cash” versus “Dash for Profit”.
- Insured’s looking for more syndication of risk - Smaller layers, broader panels, reduced lines
- Arson, Cyber, Extortion, Fraud, Recall, Theft - incidents rise
- Rise of the Tort of Nuisance



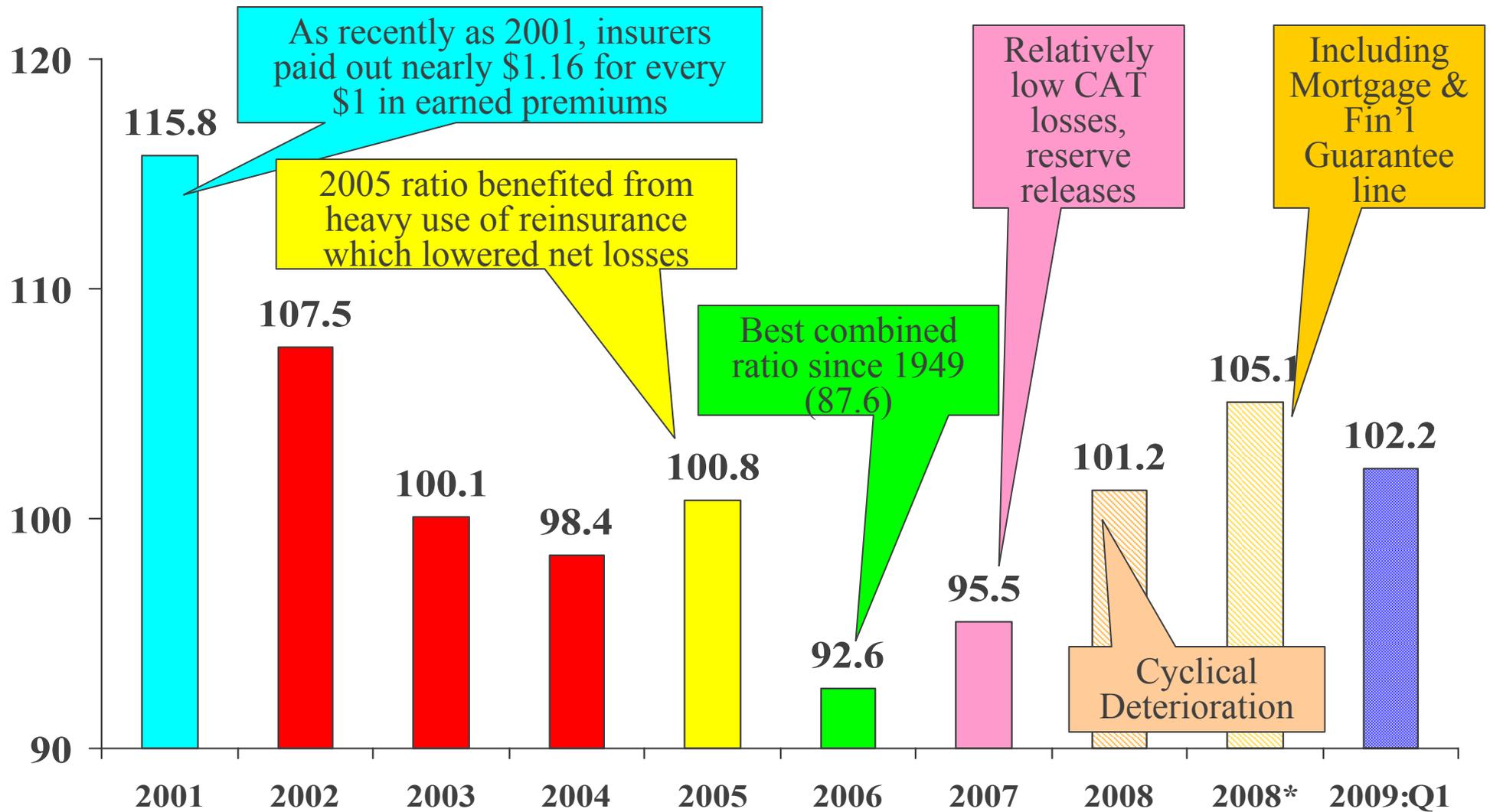
What Does the “New Normal” Economy Look Like?

- High levels of unemployment/ underemployment
- Low levels of investment return
- Exchange rate volatility
- Low levels of new borrowing
 - Affects housing, autos, other consumer durables
- Low levels of consumer demand/business investment
 - Significant increase in the personal saving rate, but virtually all used to pay down outstanding debt

Year-to-Year Change in Net Written Premium, 2000-2009:Q1



P/C Insurance Industry Combined Ratio, 2001-2009:Q1



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Casualty Trends

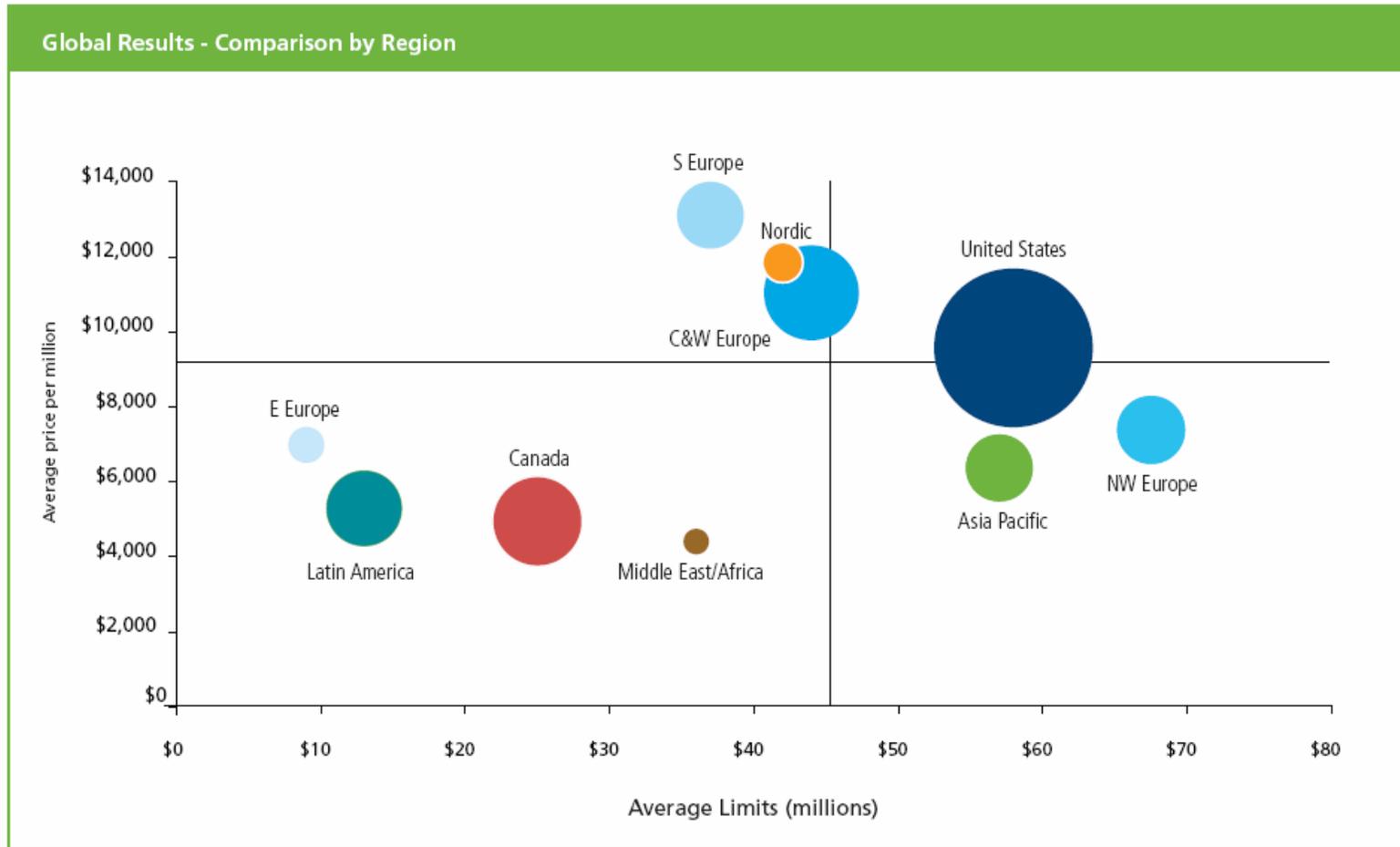
Covers, Limits & Prices

Cover

- “this Financial Interest clause (for non-admitted cover for the parent subsidiaries overseas where non-admitted is illegal) is fine but how do we pay the plaintiff?”
- “we need to look at Excess Product Guarantee for end-products rather than just components”
- “we need full Contractual Liability cover because our end-customers have arbitrarily imposed and/or increased the liability caps”
- “but I need my PPL insurer to cover my joint & several liability risk for my partners activities within the unincorporated Joint Venture”
- “so the Toxic Mould exclusion takes out cover for Avian & Swine Flu?”
- “why are you selling me an ELD policy when my PPL policy already covers pollution risks?”
- “but I need evidence of PI cover to secure this contract”
- “but why do we have a Deliberate Act exclusion on our Corporate Manslaughter extension?”

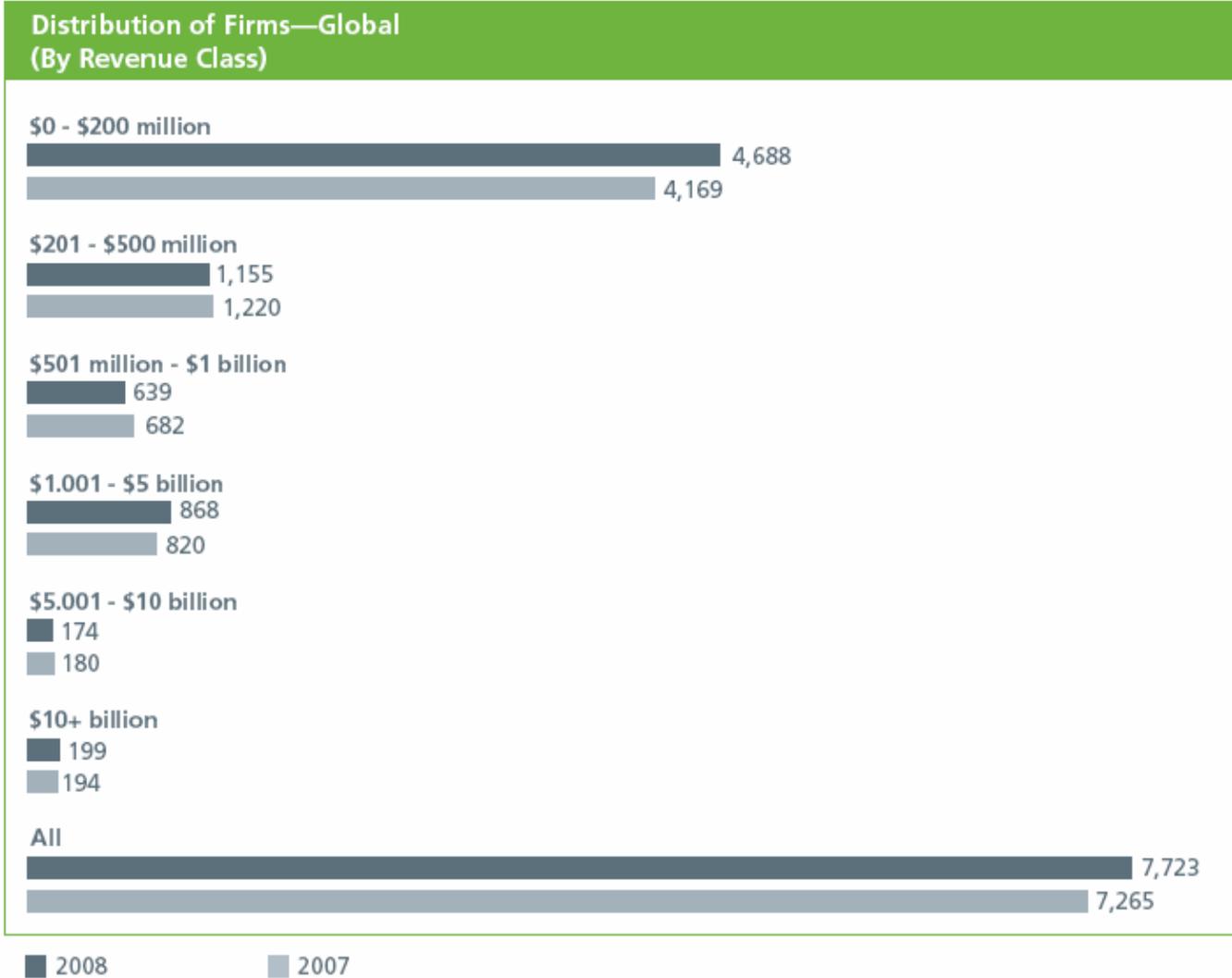
The Global View

- Wide disparity of limits purchased and pricing
- Full population comparisons only

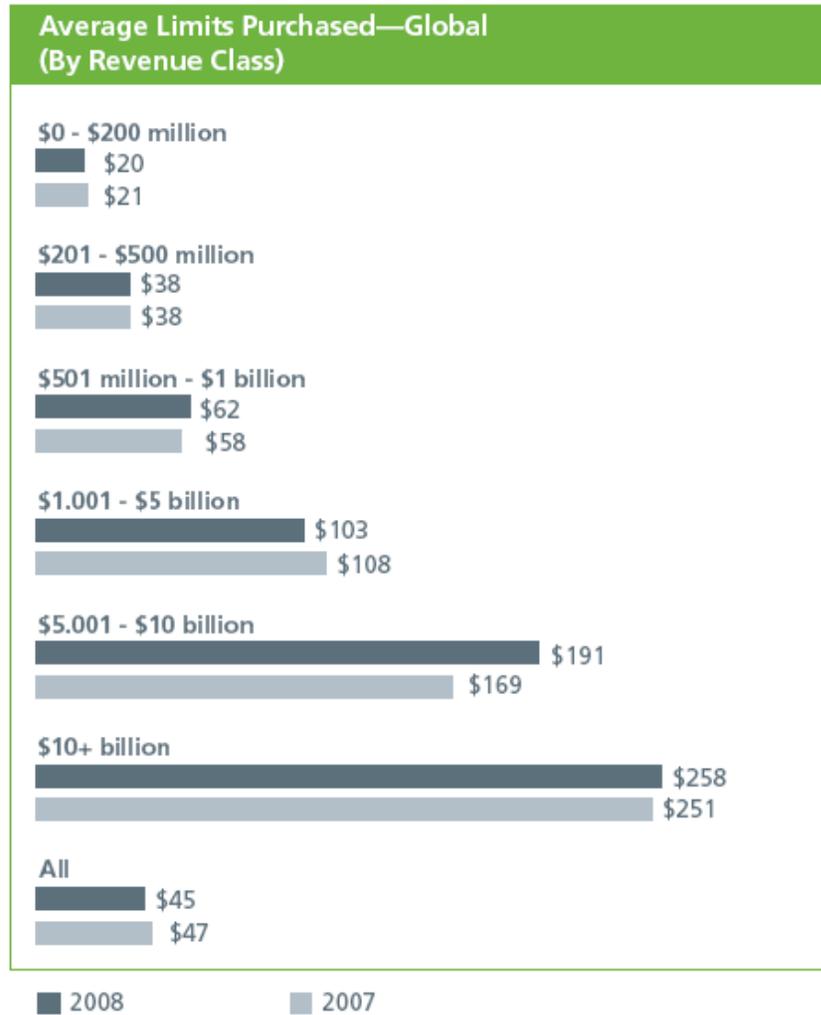


Bubble size depicts population relative

Total Survey Population



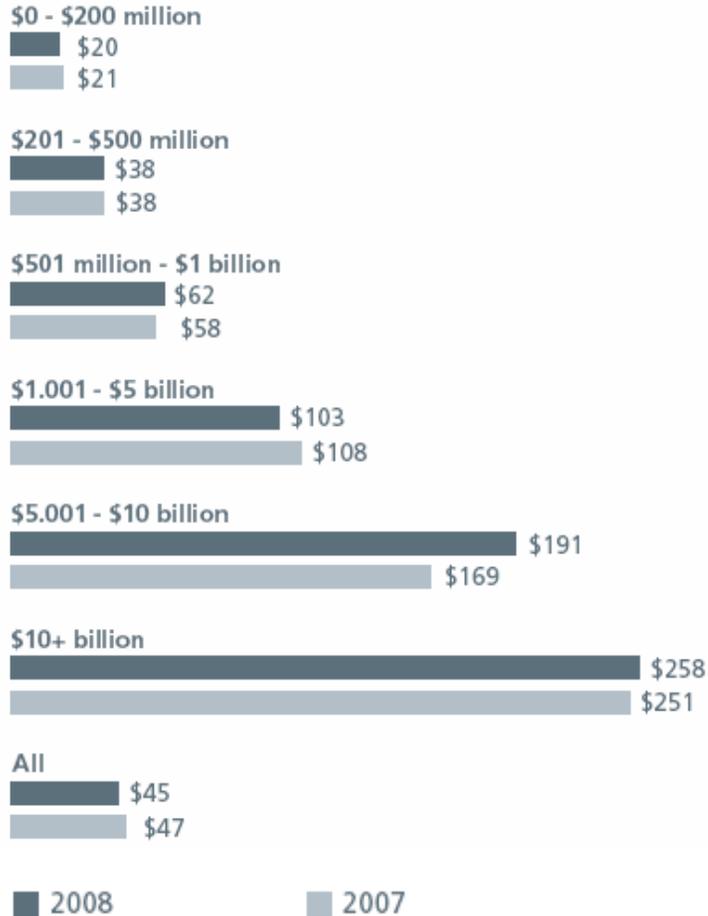
Global Results: 2008 vs. 2007



Global Results: 2008 v 2007

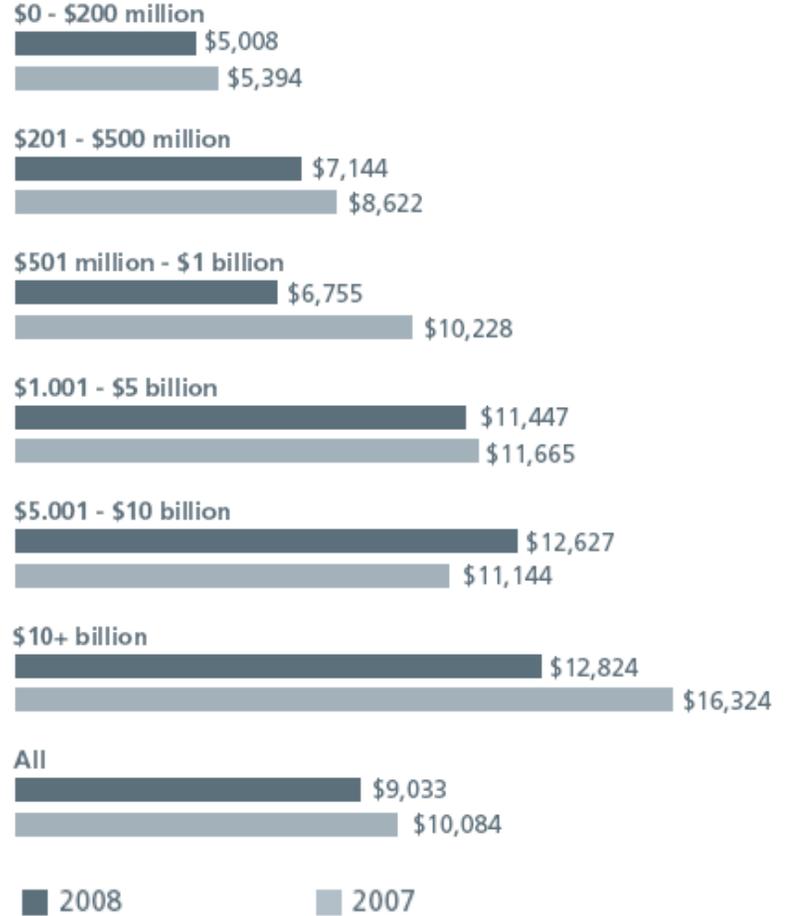
(Full Population)

Average Limits Purchased—Global (By Revenue Class)

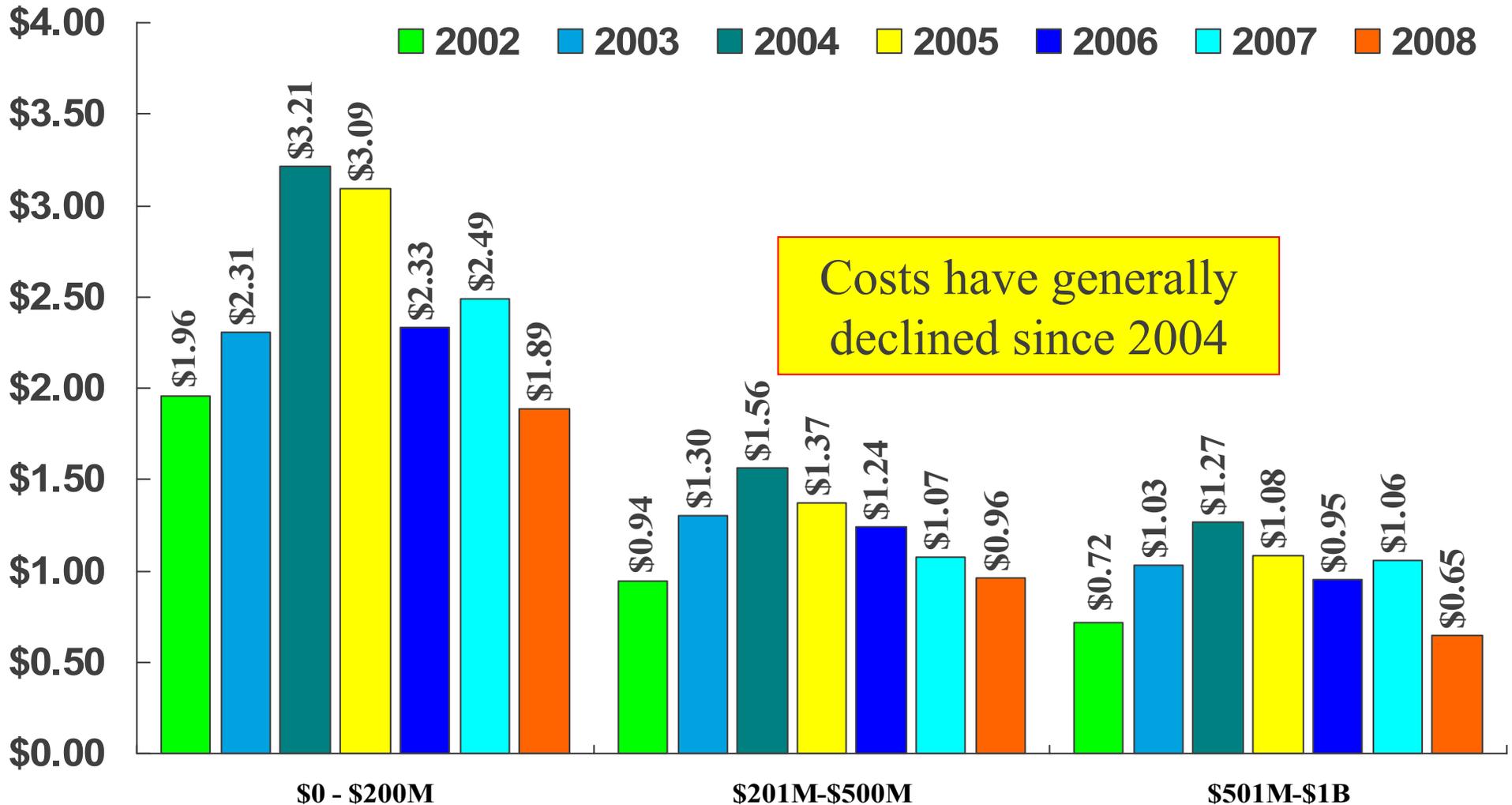


(Full Population)

Average Price Per Million of Coverage—Global (By Revenue Class)



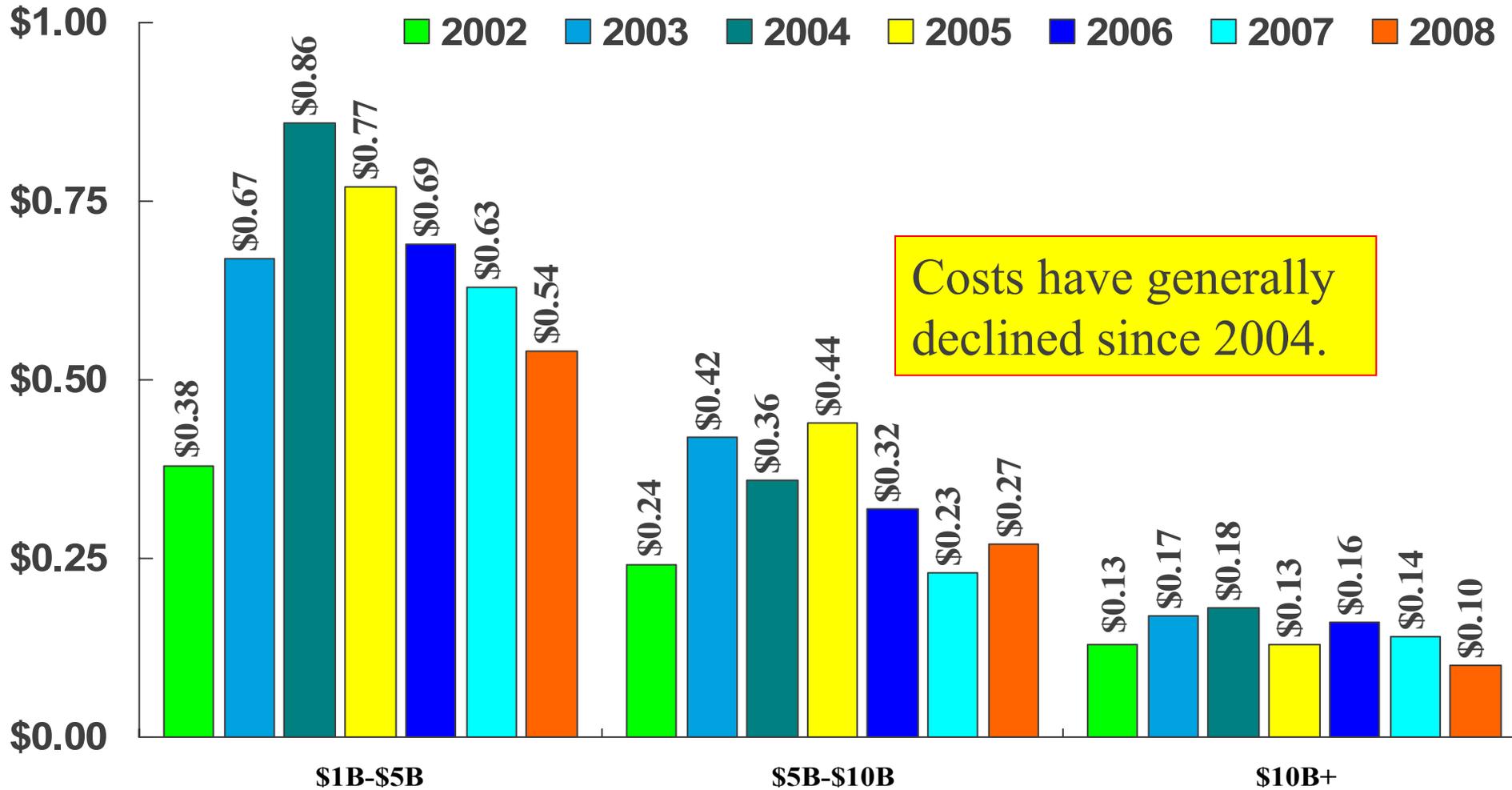
Liability: Average Yearly Cost* Small and Medium-Sized Businesses, 2002-2008



*per \$1,000 of revenue, across entire liability program (full population)

Source: Marsh, 2008 Limits of Liability Report

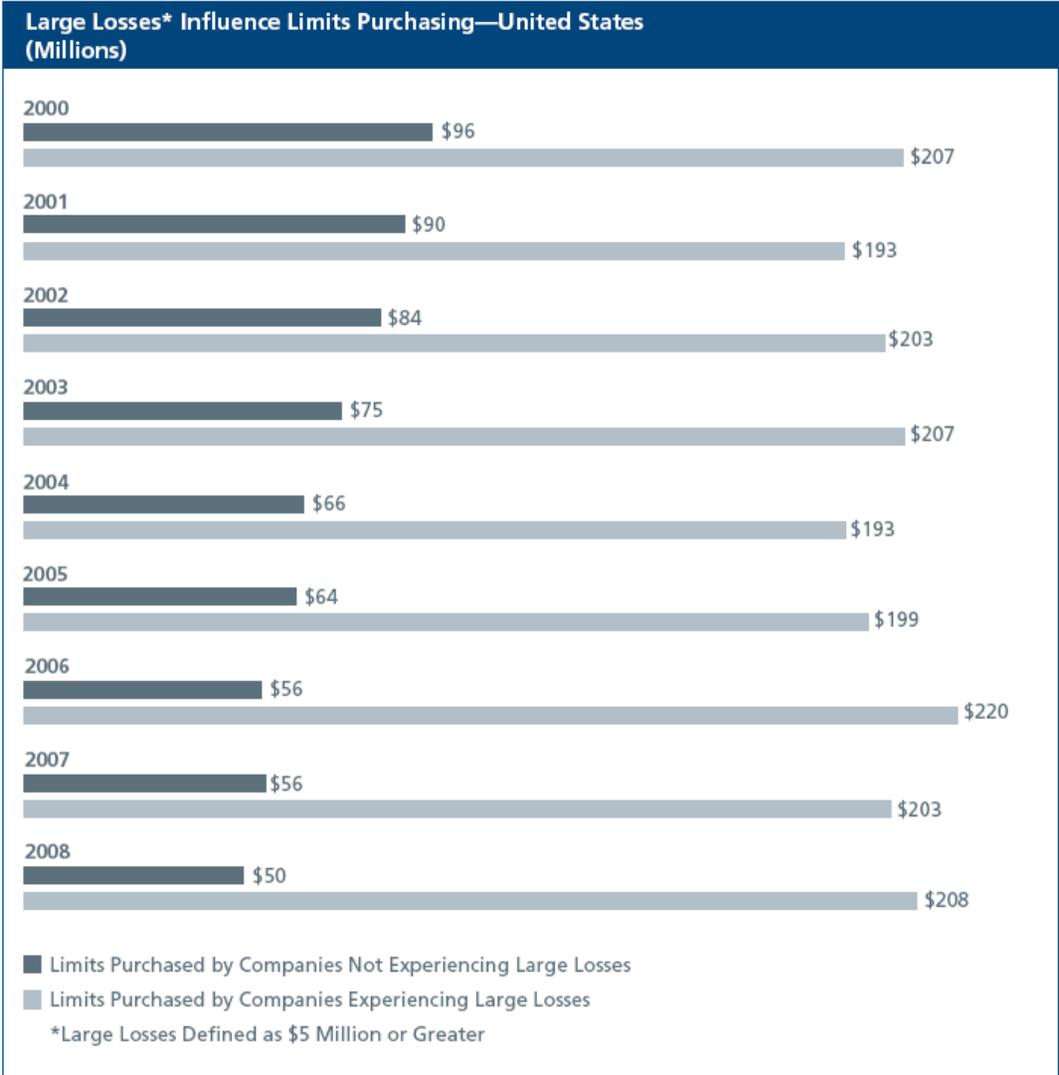
Liability: Average Yearly Cost* Medium and Large Businesses, 2002-2008



*per \$1,000 of revenue, across entire liability program (full population)

Source: Marsh, 2008 Limits of Liability Report

The \$5 Million Loss: Learning From Experience



European Companies: With vs. Without Operations in North America

Europe—Companies with/without North American Operations

REGION	WITH NORTH AMERICAN OPERATIONS		WITHOUT NORTH AMERICAN OPERATIONS	
	AVERAGE LIMITS (MILLIONS)	PRICE PER MILLION	AVERAGE LIMITS (MILLIONS)	PRICE PER MILLION
Northwestern Europe	€91	€13,025	€50	€4,361
Central & Western Europe	€53	€12,263	€18	€9,095
Southern Europe	€40	€12,878	€21	€13,257
Eastern Europe	€1	€12,060	€7	€6,963
Nordic	€51	€14,784	€18	€7,949
EUROPE TOTAL	€56	€12,765	€23	€8,209

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The Casualty Market

Today

The Perfect Storm? ("no, not the George Clooney movie")

- 2001
 - Dot Com Crash, falling Investment yields
 - Heavy "Nat Cat" & Large P&C losses
 - 7 years of rate reductions
 - Consistently poor Combined Ratios
 - Insurer insolvencies
- 2008/9
 - Sub-Prime Crisis, Credit Crunch & falling Investment yields
 - Above average "Nat Cat" & Large P&C losses
 - 5 years of rate reductions
 - Combined ratios at or close to 100%
 - AIG rescue

"Can you spot the difference"?

Casualty – June 2009

- Policy holder surplus down but remains healthy - scope for further reserve releases now impaired
- Products & people exposure reducing BUT Injury Cost inflation still at +8% per annum
- Capital re-allocation strategies may change insurers appetite by class
- Claims challenges and battle of Coverage Counsel now the norm
- Social aspects heightened – enhanced awareness, deep pocket philosophy, collapse of social security systems
- Legal costs at 40% of bodily injury settlements not a sustainable model
- Primary & Excess Rates “bottoming out” but still competition for selected risks
- Captive premium levels under pressure
- US law firms actively recruiting Europeans to join US class actions
- Legislation will continue to drive harmony via EU wide directives but speed of change is dependant upon whether legal systems are based on codified Napoleonic civil code and Roman law or Statute and Common law which are driven largely by case law
- Implementation of EU environmental legislation will drive higher recognition and responsibility for pollution. Stand alone pollution markets likely to compliment or replace CGL form. CGL policy coverage could change as a result
- Increased incidence of Product Recall and Product Counterfeiting activity as the manufacturing supply chain becomes increasingly focused on the Far East
- Contract Certainty/EOC now embedded with 21 day ABI “on-time” at 91% BUT “document accuracy” at under 10% for top-end commercial arena remains an ongoing challenge

Large London Market Casualty Loss Events

Sector	Geography	Event	Year	Cost Estimate
Raw Materials	USA	US Auto	1997	USD29m
Life Sciences	USA	US Prods	1998	GBP21m
Chemicals	Far East	RoW Prods	2003	GBP28m
Technology	USA	US Prods	2004	USD15m
Leisure	USA	US PPL	2005	USD11m
Premises	UK	“Buncefield”	2005	USD250m+
Food Mft	UK	Salmonella	2006	USD35m+
Construction	UK	Collapse	2007	GBP75m+
Utilities	USA	Explosion	2008	USD1bn+
Technology	USA	Open Source	2008	USD100m+
Utilities	UK	Water Act	2009	GBP35m

Coinsurance (Subscription) Market Practices The 5 x BIPAR Principles

- For?
 - Breaking Cartels is good
 - Leader panels are dwindling
 - Reflects true technical pricing of each insurer
 - Reflects different insurer RoC needs
 - Treating Customers Fairly
 - Aviators already do this
 - Already common in EU
- Against?
 - Hard Market challenge
 - Wide variation of terms & conditions emerge
 - Non-concurrency issues emerge
 - Claims challenges increase
 - Broker fees increase
 - Multiple releases on claims needed
 - Already common in UK

Risk Management 2009 – “don’t forget the basics”



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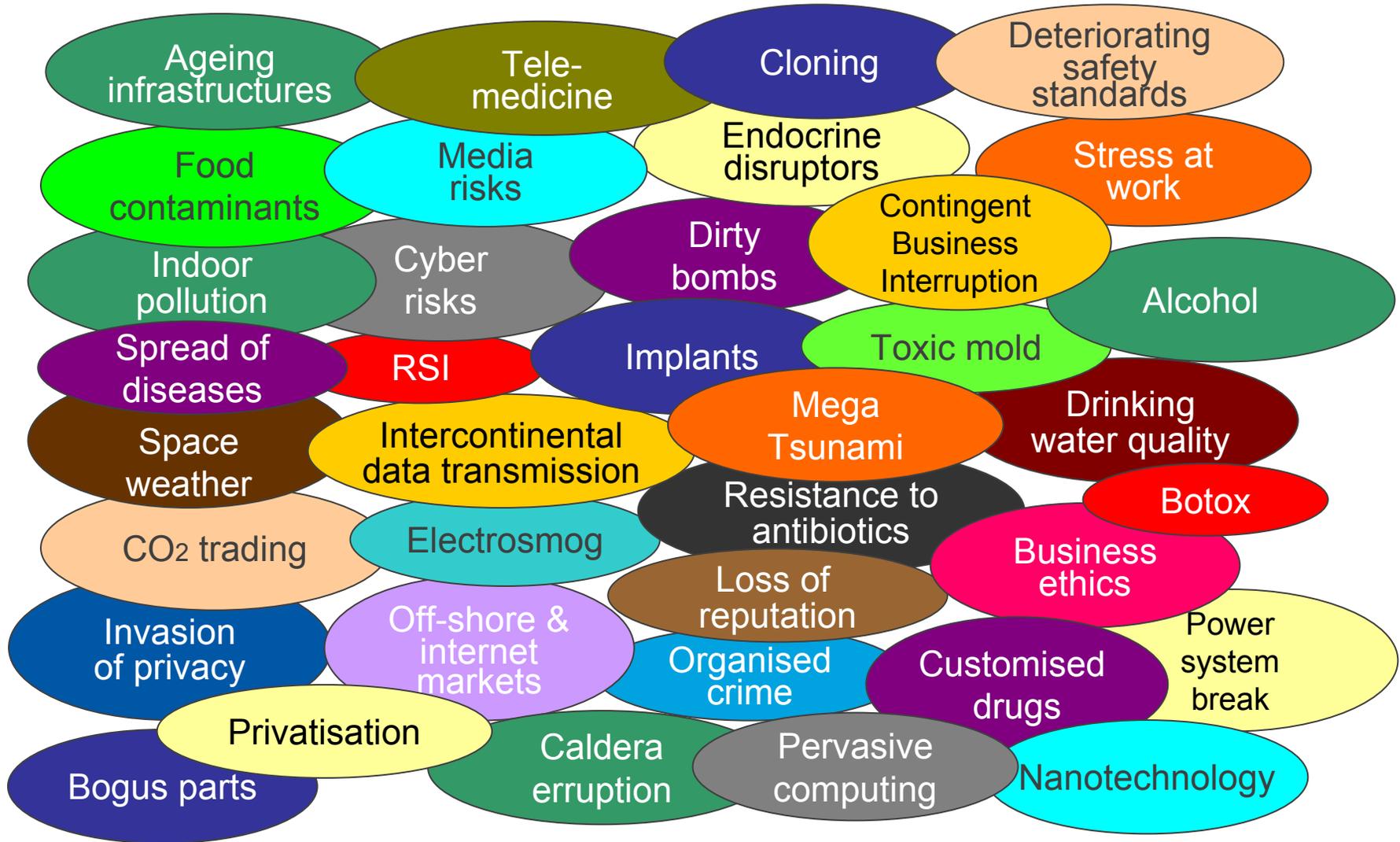
Casualty

Hot Topics

Casualty 2009 Hot Topics

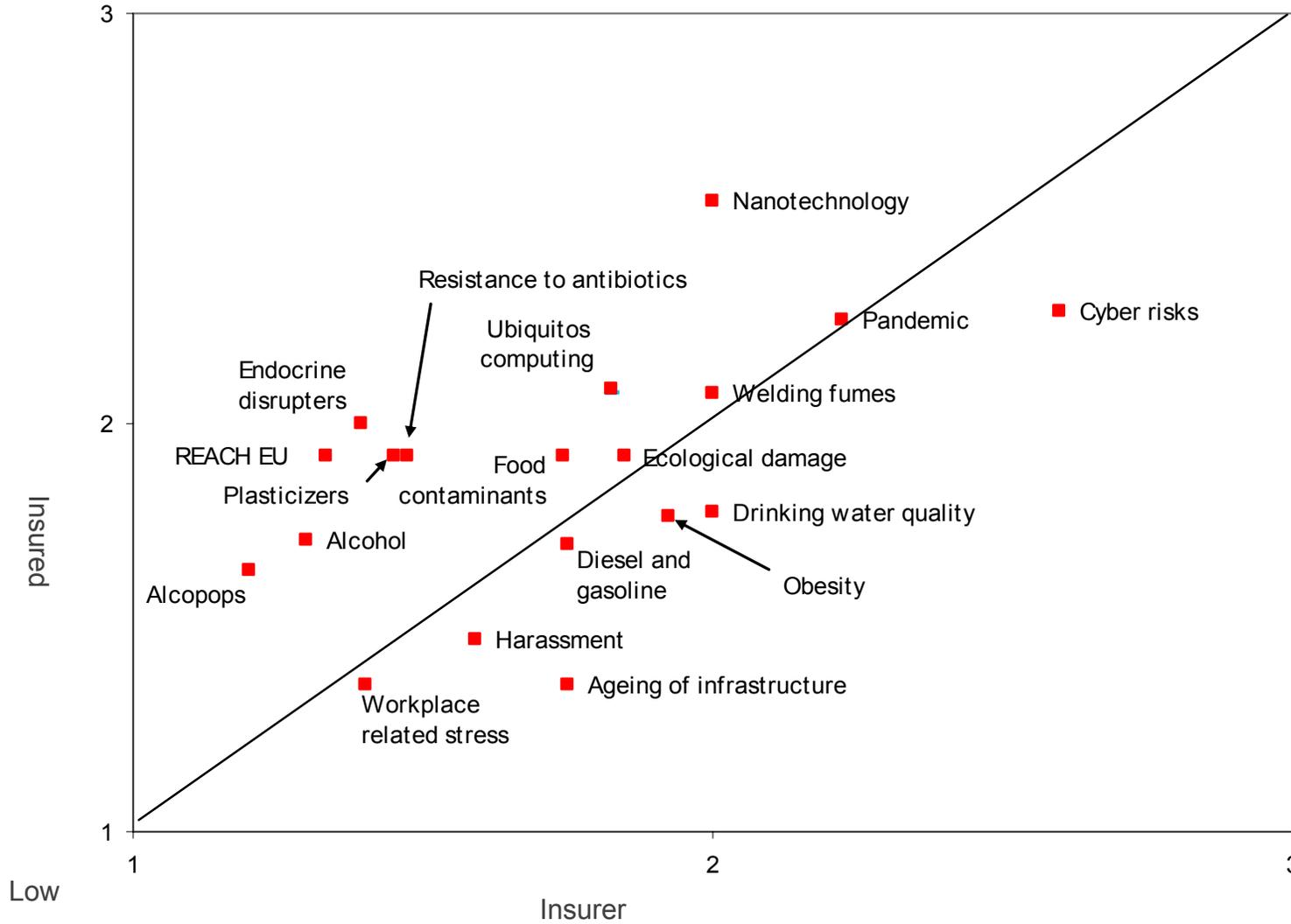
- Global programme regulatory and tax challenges
- Tax Liability for “non-admitted” excess of loss
- “DIC” challenges ie Faute Inexcusable – what is a good local standard?
- Use of Capital (Historic v Prospective liabilities) & Solvency II
- Collateral Alternatives
- House of Lords 17/10/07 rules Pleural Plaques are not compensatable BUT?
- Asbestos “trigger” litigation (Bolton v MMI etc) coming to a head
- “Bartoline v RSA & Others” – TP pollution clean-up costs
- Law Commission Review (2010) – Insurance contract law, non-disclosure, warranties (Qayyum ansari v New India Ins 2009)
- Ministry of Justice (MoJ) paper CP8/07 published 20/4/07
- Ogden 6 (2007) – new rules for loss of future earnings and non-mortality contingencies

Landscape of Emerging Risks



Perception of Emerging Risks Insurer v Insured

High



Environmental - Traditional Coverage Forms and Gaps

“We have it covered”

	General Liability	Property	D&O	Business Auto	Site Pollution/ Env. Liability
Underground Storage Tanks	Likely excluded	Likely excluded	Likely excluded	Likely excluded	Scheduled primary or excess of UST policy
Waste Disposal	Likely excluded	Likely excluded	Likely excluded	Likely excluded	Add optional Non Owned Disposal cov.
Material Transport	Limited coverage possible	Likely excluded	Likely excluded	Limited coverage	Add optional 1 st Party or Contingent Trans.
Hostile Fire	Limited coverage possible	Likely excluded	Likely excluded	Likely excluded	Pollution coverage is all peril risk policy
Business Interruption	Likely excluded	Likely excluded	Likely excluded	Likely excluded	Add optional loss of rents / extra expense
Fuels/Chemical Storage	Likely excluded	Limited coverage possible – named peril	Likely excluded	Likely excluded	Liability coverage is provided for releases
On-Site Clean-Up/ Remediation Costs	Likely excluded	Limited coverage possible, sublimit \$25k	Likely excluded	Likely excluded	Covered unless specifically excluded due to known liability
Waste Storage On-Site	Likely excluded	Likely excluded	Likely excluded	Likely excluded	Liability coverage is provided for releases
Prior Environmental Claim/Loss/Violations	Likely excluded	Likely excluded	Limited coverage for shareholder suits	Likely excluded	Covered unless specifically excluded due to known liability

The Fallacy of Predictions

(or why we should think before we speak!)

- “no more boom and bust” – Gordon Brown, 1997
- “640k ought to be enough for anybody” – Bill Gates, 1981
- “no matter what happens, the US Navy is not going to be caught napping” – US sec of Navy, Dec 4, 1941
- “radio has no future, X Rays are clearly a hoax, the aeroplane is scientifically impossible” – President, Royal Society, William Thomson, 1897
- “the atom bomb will never go off – and I speak as an expert in explosives” – US Admiral William Leahy, 1945
- “I think there’s a world market for about 5 computers” – Thomas J Watson, Chairman IBM, 1961

Casualty Hot Topics in 2020?

- Social security systems collapsed - Long term healthcare no longer affordable
- Weak casualty pricing predominates
- Computer underwriting models unable to cope with rapid change in world of risk
- Toxic Torts – Alcohol, Benzene, Endocrine Disrupters, Obesity
- Novel Toxic Torts – IPR (Open Source), Lifestyle Products, Nano-particles, Pervasive Computing
- Bio Mechanical Engineering & Robotics developments
- “Post-Carbon” technology solutions introduced in a rush
- Aging Infrastructures under stress or unable to cope
- Climate Change/Emissions lawsuits
- Regulation overload
- Contractual liability stresses within supply chains
- US style class-action litigations now the norm
- Can “Occurrence form” survive capital market angst or uncertainty factor
- Aging population still at work
- Hypersonic and Space travel for the general public
- Asbestos has “peaked” – Nano-particles & EMF cell damage just emerging

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Contractual Risk Management

Stress in supply chain

Contractual Flows

