FinanceAsia

HD **Insurance: After shock**

BY By Rupert Walker

WC 1,382 words

PD 1 January 2014

SN Finance Asia

SC MEDFIN

PG 39

LA English

LP

As the costs of disasters grow in Asia so does the urgency to insure and mitigate the risks

The devastation wrought by Typhoon Haiyan, one of the biggest natural disasters in recent history, was a stark reminder of Asia's vulnerability to such catastrophes.

TD

However, low non-life insurance penetration in the Philippines means the majority of losses incurred from November's storm are expected to be uninsured and the effect on insurance and reinsurance companies is estimated by industry insiders to be limited.

'If we examine the gap between economic loss and insured loss for natural catastrophe events in the region compared to the rest of the world, the difference is significant. The take-up of general insurance across the region remains small even as natural catastrophe exposures continue to increase and threaten Asia's growth momentum,' said Clarence Yeung, **group** chief operating officer & chief underwriting officer at ACR Capital Holdings, a Singapore-based reinsurance **group**.

Nevertheless, the risk profile for insurance companies and reinsurers is increasing throughout Asia. The Thailand floods two years ago raised awareness of the vulnerability of supply chains - for example in the auto sector - and of industry and population concentrations on flood plains and in coastal cities.

Additional factors include aging demographics, especially in Japan, and the prevalence of outsourcing to emerging markets where IT systems are not always robust.

Economic growth is a key driver for increasing asset and risk accumulation in the Asia-Pacific region. Rapid urbanisation has also contributed, which means a higher density of **residential**, **commercial** and industrial assets, especially in areas that are exposed to typhoon, flood and earthquake hazards as well as pandemics.

The urbanisation rate of emerging Asia has increased from less than 20% in 1970 to slightly over 40% in 2010, according to Clarence Wong, director and head of economic research & consulting, Asia-Pacific at Swiss Reinsurance.

'The most vulnerable are emerging markets because there is less risk mitigation: building codes tend to be sub-standard, levees poorly constructed and warning systems inadequate,' said Sally Yim, lead insurance analyst Asia Pacific, Moody's Investors Service.

'In other words, there are more insurable risks,' agreed Connie Wong, analytical manager for insurance ratings Asia Pacific, Standard & Poor's.

Yet in general, Asian companies are less sensitive than firms in Western Europe or the US to the threat of natural disasters to their operations.

'Risk management and risk mitigation is not such a priority and commonly there is less take up of insurance in the region,' said Keith Thomas, chief executive, global corporate business, Asia Pacific at Zurich Insurance.

Factors include legal complexities, but 'mostly there is just less perceived value in insurance products'. However, more local firms are using Zurich's CAT mapping services, supported by the **firm**'s 900 risk engineers worldwide, especially to help them choose better locations for their factories.

Imprecise models and analytics

But, as Connie Wong pointed out, part of the problem is that catastrophe assessment is an inexact science, even when sophisticated models are deployed. There is too much uncertainty and a need for qualitative judgment.

Assessing natural disaster risk quantitatively and in a forward-looking manner is still a relatively young science (about 25 years) and comes with uncertainties. 'Risk modelling is improving but changing weather patterns and shifting flood plains means there is always uncertainty assessing the impact of floods,' said Thomas.

'Modelling certain natural hazard perils is more challenging than modelling others,' agreed Malcolm Steingold, Asia-Pacific CEO for Aon Benfield.

Availability and quality of data is essential to model robustness, but the inherent characteristics of some disasters make them more difficult to model even when high quality data are available.

Catastrophe models based on assessments of probable risk and return can be constructed where there is a lot of data available. Where data is scarce, then so-called RDS (realistic disaster scenario) modelling is used, so there is far greater uncertainty, according to Steingold.

Also, the effectiveness of data analytics and modelling is dependent on the level of expertise of the people undertaking the analysis.

'Even the sophisticated models in Japan and New Zealand are flawed. There are too many variables and qualitative inputs in addition to historical data, such as **property** location and loss distribution,' said Yim.

Given the lack of robust catastrophe models in many markets, there are concerns that the industry operates in an unsustainable manner. And of course, risk has to be priced adequately in order to justify the capital required to underwrite the risk, said Clarence Wong.

Important role of governments

In the face of so much uncertainty, governments can play a critical role in alleviating the worst consequences of catastrophe, and recompense victims.

They can ensure that (re)insurance companies have access to the market and are adequately capitalised to be able to fulfil their obligation in case of adverse events, and they can protect lives through effective mitigation measures including early warning and evacuation procedures.

Governments and the (re)insurance industry can also provide various financing tools, and provide risk transfer solutions.

'The key challenge, however, is in ensuring that the risk bearers gain awareness of the risks involved, and that the solutions are affordable compared to the risks involved. To this end, support from governments is important, to ensure that the financing and risk transfer mechanism is as widely applied as possible,' said ACR's Yeung.

Examples of funding instruments include microfinance, social funds and public disaster funds. For risk transfer solutions, those available include private (re)insurance, microinsurance, public/private partnerships solutions and government risk pools.

Also, governments usually step in when insurance is not commercially viable, for example a pool system in Taiwan reduces costs for individuals - and Thailand and **China** are examining the possibility of similar systems, pointed out Connie Wong. Taiwan's earthquake insurance collective pool is administered by the government but the risk is taken by insurance companies which then spread it through reinsurance.

Insurers can be forced to **buy** adequate levels of catastrophe reinsurance. In Australia, for example, regulations provide for 'minimum event retentions' for insurance companies, which not only address the **purchase** of vertical cover (direct exposure) for severity but also now provide for appropriate levels of sideways aggregate (indirect) cover to respond to the regularity of natural catastrophes.

'This development arose out of the frequent storm activity and flooding on the Australian North Eastern seaboard,' said Steingold. Japan also became a substantial **purchaser** of catastrophe (re)insurance following losses arising from Typhoon Mireille in 1991, he pointed out.

OPPORTUNITY KNOCKS FOR PRIVATE INSURANCE

Indeed, high profile disasters with widespread media coverage are likely to be the catalyst for greater penetration of potential markets in the region - especially in developing countries.

'Catastrophe (insurance) purchasing in developing economies is more reactive than in developed economies, as was demonstrated by the Thailand floods in 2011,' said Steingold.

There is clearly an opportunity for (re)insurers to write new business. 'With a rising level of natural catastrophe exposures, the demand for catastrophe insurance is certainly there. Earthquake and typhoons are well-tracked risks in Asia, while flooding is at our doorstep, if not already one of the three major natural catastrophe risks that Asia faces,' said Yeung.

One way forward is to form more public-private partnerships in the entire value chain, whether it is in research work such as flood risk mapping (ACR did a project with a Shanghai research agency), or the design of solutions that pool together resources for better catastrophe management.

'The key success factor for growth is to make simple products accessible and affordable for a larger part of the population. Innovation can help to lower the cost of insurance products and increase affordability,' said Clarence Wong.

In addition, Thomas pointed out, insurance firms can also offer insights into risk management and suggest best practices.

The bottom line is that both 'insurance and reinsurance companies have the opportunity to enter markets expanding with economic growth and characterized by low penetration, as well as to diversify their global risks', said Moody's Yim.

40% - Urbanisation rate in emerging Asia.

IN i82 : Insurance | ifinal : Financial Services

NS ghurr : Storms | gcat : Political/General News | gdis : Disasters/Accidents | gntdis : Natural Disasters/Catastrophes | grisk : Risk News | gwea : Weather

RE asiaz : Asia | tasman : Tasmania | apacz : Asia Pacific | ausnz : Australia/Oceania | austr : Australia

PUB Haymarket Media Limited

AN Document MEDFIN0020140103ea110000e

