

Reinsurers ride out difficult first quarter

Pricing outlook remains unclear despite large losses

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Natural catastrophes hammered U.S. reinsurer profitability during the first three months of the year, but it is still unclear whether those losses will lead to significantly higher prices for most reinsurance buyers.

Reinsurers remain well-capitalized and the size of any broad rate increases may still hinge on the Atlantic hurricane season, which began last week.

Reinsurers surveyed by the Reinsurance Assn. of America reported a combined ratio of 129.3% for the first three months of 2011, compared with 102.2% written by a similar group for the same period last year. The Washington-based trade association surveyed a group of 19 reinsurers licensed to write business in the United States (see chart page 26).

Many of the reinsurers surveyed write international business and some had significant exposures to recent catastrophes such as the Japanese earthquake and tsunami, and flooding in Australia. In addition, domestic catastrophes, such as the series of tornadoes that tore through several U.S. states in the first three months of the year, hit reinsurers' results.

While the exact losses from the catastrophes remain unclear, reinsurers have posted significant loss estimates over the past several months. And modeling firms expect the Japanese earthquake alone will cost the insurance industry more than \$30 billion. The collective loss ratio for the quarter exceeds 100%.

Although the losses are significant, they don't compare with 2005 when hurricanes Dennis, Katrina, Rita and Wilma caused nearly \$60 billion in insured losses, leading to sharp increases in insurance and reinsurance rates.

"It's different because it's not at the point where everything is falling apart," said Doug Mewhirter, an equity research associate at RBC Capital Markets in Richmond, Va. "It's a bunch of things that are adding up...it'll take a while to play out."

Policyholders' surplus reported by the reinsurers in the RAA survey was \$107.55 billion during the first quarter this year, down less than 1% from the same period last year.

Reinsurers say they can handle the hits they've taken so far.

"The losses we've had are within the realm of what we can manage and what we've anticipated," said Bob Shine, chief underwriting officer in New York of the North America property/casualty unit of XL Capital Ltd.'s XL Insurance, in discussing the reinsurance situation. He said XL has not had to do much to change its overall business plan for 2011, although it might be less likely to give rate decreases or more likely to look for increases in certain lines of business to improve profit margins.

XL Reinsurance America posted a profit of nearly \$9.4 million during the first three months of this year, compared with \$12.4 million during the same period of 2010. It was among 12 insurers reporting a quarterly profit of the 19 U.S. reinsurers tracked by RAA.

Everest Re Co., another reinsurer surveyed by the RAA, lost \$124.8 million in the first three months of 2011, compared with a \$11.3 million loss in the comparable period last year.

Its Bermuda holding company, Everest Re Group Ltd., had warned investors in recent months about its losses relating to the earthquake that occurred near Christchurch, New Zealand, last year, storms and flooding across Australia, and the devastating earthquake in Japan. "Nonetheless, given the strength of our balance sheet and our core earnings, we have ample capacity to withstand the events that occurred during the first quarter," Joseph V. Taranto, CEO of Everest Re Group, Ltd., said in a statement.

"We've had a large level of natural disasters this year," said Brett Horn, associate director at the investment research firm Morningstar Inc. in Chicago. "It's still a little early to be completely confident that the pricing cycle has turned, but the disasters (that have hit reinsurers) so far have certainly been an impetus in that direction."

Early this year, U.S. reinsurers didn't ask for significantly higher premiums from their clients, many of which have annual contract agreements due for renewal in the coming months. The RAA found that reinsurers collectively wrote \$7.1 billion in net premiums in January, February and March, compared with \$6.4 billion in net premiums during the same period last year.

"These premiums don't reflect the impact of the (reinsurers' recent catastrophe) losses and the subsequent change in pricing," said Amit Kumar, vp of Macquarie Securities Group in New York. He said reinsurer results in the second quarter will provide more information.

"While recent catastrophes can affect reinsurers' profits for the short term, the better companies are focusing on improving their long-term profitability and results," said Dean Evans, senior vp of equity research at Keefe Bruyette & Woods Inc. in New York.

"Obviously all this (speculation about a possible turn in the market) is determined on whether there's an Atlantic hurricane that hits land," Mr. Evans said

"With pricing increases, you'll see a modest profitability improvement, but for the most part that's largely going to be offset by the underlying trends you've seen for a while now," he said.