

2015 Insurance Market Outlook: Putting It Into Perspective

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For many companies, insurance is one of their largest costs. When you add up premiums for Property & Casualty, Workers' Compensation, Employee Benefits, Life Insurance and other lines of coverage, it can often total 5% of revenues or more.

It is critical to understand not only how to manage these costs, but also how to forecast your costs as you look into your next fiscal year.

The purpose of this article is to give you some perspective on where the insurance industry is today and how the current financial situation and underwriting objectives will affect you in 2015.

Insurance Company Economics

Insurance companies are in business to accept risk in exchange for premiums. Like any other business, they want to make money and earn a fair return for



their shareholders. Absent a decent return, they will not be able to attract additional capital and the insurance industry thrives on capital or surplus.

Insurance companies make money in two ways:

1. Underwriting
2. Investments

An underwriting profit is earned when losses plus expenses divided by premiums is less than 100%. This factor is called a *combined ratio*. If an insurance company has a combined ratio of 98%, it means they are making a 2% underwriting profit. If the ratio is 105%, it means they are losing 5%.

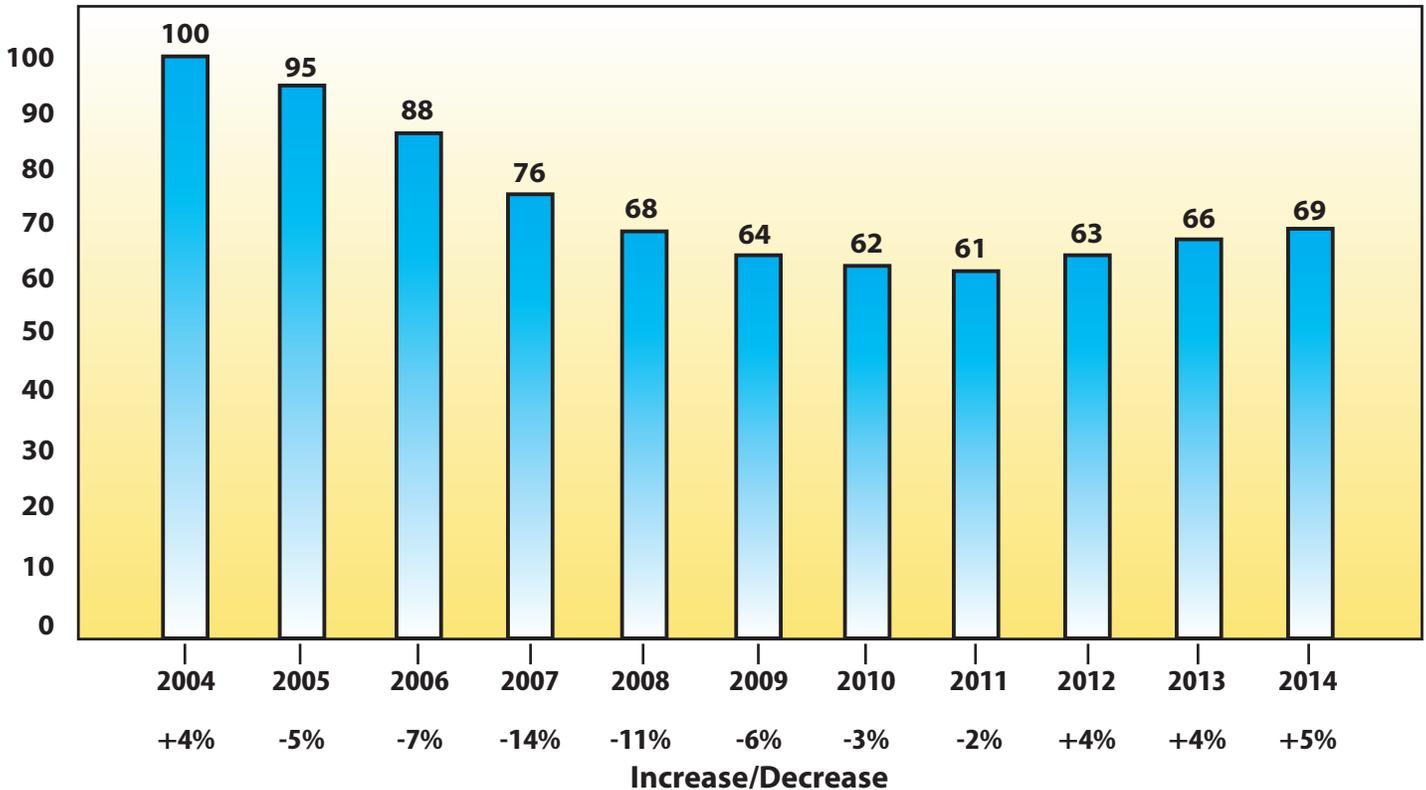
Table 1 - Insurance Cycle

\$ in Billions

Description	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Net Written Premium	\$421.10	\$425.90	\$443.80	\$440.60	\$434.90	\$418.40	\$423.80	\$438.0	\$456.90	\$477.7
Combined Ratio	98.1	100.9	92.4	95.5	105	101	102.4	108.1	103.2	96.1
Investment Income	\$39.6	\$49.7	\$52.3	\$55.1	\$51.5	\$47.1	\$47.6	\$49.1	\$48.0	\$47.4
Operating Income	\$44.1	\$45.1	\$84.6	\$73.4	\$30.6	\$45.0	\$38.2	\$15.4	\$33.3	\$64.3
Policyholder Surplus	\$391.4	\$425.8	\$447.1	\$517.90	\$457.30	\$511.50	\$556.90	\$553.70	\$586.8	\$653.3
Return on Avg. Net Worth	9.4%	9.6%	12.7%	10.9%	0.1%	5.0%	5.6%	3.0%	5.1%	10.3%

Source: Insurance Information Institute (iii.org)

Table 2 - Average Property & Casualty Rate Changes



Insurance companies also earn money investing the policyholders' surplus and cash reserves they have set aside to pay future claims. It is not uncommon for an insurance company to have an underwriting loss, but to make up for it with their investment income (especially when interest rates are high).

If you look at **Table 1**, you will note that from 2008 to 2012, the industry's "Return on Average Net Worth" was poor. This was attributable to a lousy combined ratio and a low level of investment return (the majority of an insurance company's portfolio is invested in debt obligations; they can only invest about 20% in equities).

The industry needs to attract capital (surplus) to continue to grow. Ideally, in order to do that they need to earn 10% or more. When returns deteriorate like they did from 2008 to 2012, underwriters try to get more rate (increase premiums). This is reflected in the rate increases illustrated above in **Table 2**.

2013 was a different story. Unlike 2012, which was a

bad "cat" year (losses from catastrophes...remember Hurricane Sandy?), 2013 was a light "cat" year and the combined ratio reflects that.

Underwriters realize that 2013 was somewhat of an aberration. They still feel they need about 5% rate increases on preferred accounts; however, they are not pushing the price increases as hard as they were at this time last year.

So what should you expect to see in 2015?

Allied Lines

This includes Property, General Liability, Auto & Umbrella. If you look at **Table 2**, you will note that Property & Casualty rates have increased nearly 15% since 2011; however, they are still over 30% lower from where they were in 2004. While most underwriters we talk to want an additional 5 points of rate or more, the positive results of 2013 are moderating those rate increases. On average, preferred accounts should be able to negotiate close to flat rate renewals and possibly even minor rate

decreases.

Professional Liability – Also Known As Errors & Omissions Insurance

The market for architects, engineers, lawyers, CPAs and other professionals remain competitive with a large number of companies competing for preferred accounts. Recognize that coverage, risk management, and claims handling differ greatly between insurance companies. While you may be able to save money by going with a “bare bones” insurer, it is not



recommended.

Like the Allied lines, preferred professional liability risks should be able to negotiate renewal terms plus or minus 5% from expiring rates. If you operate in what is considered a higher risk profession, such as geotechnical engineering, or attorneys specializing in class action cases, or if you have adverse loss experience, the market is much narrower. It is suggested that your terms be negotiated early and your program marketed if necessary.

Executive Risk

Executive Risk includes Directors & Officers (D&O) Liability, Employment Practices (EPLI) and Fiduciary Liability. The last economic downturn saw many companies going out of business or generating poor results, which resulted in downsizing and layoffs. As you can guess, this increased the number of claims covered by D&O and EPLI policies and the results suffered accordingly. Underwriting tends to be reactive as opposed to proactive and the adverse loss experience is driving rates for these lines higher. On average, we are expecting D&O to increase 5-10% and EPLI 10-25% or more. Fiduciary Liability should be flat to +5%.

Risk Management Seminar Series



Sexual Harassment Prevention Training

Friday, December 5, 2014

7:30am Registration,

8:00am - 10:00am Program

CPR and First Aid Training - Get Certified and Be Prepared!

Friday, December 19, 2014

7:30am Registration

8:00am - 3:30pm Program

Reserve Early, Seating is Limited!

To register, click on the ‘register now’ button in the announcement email, or contact Bethany Mongold at mongold@cavnac.com or call 619-744-0540.

NOTE: Due to the popularity of our seminars and limited space available, we regret we cannot provide refunds or credits with less than 72 hours advance notice of cancellation.

Workers' Compensation

The good news is that Workers' Compensation results in California have improved significantly since 2011. This is due in major part to average rate increases of about 35% since 2009 (see Table 3). It should also be pointed out that average charged rates are still over 50% less than they were in 2003! The Combined Ratio has improved from the mid-140s experienced in 2009-2011 to a projected 113 for 2013 (see Table 4).

Of course, the bad news is that the combined ratio is 113,

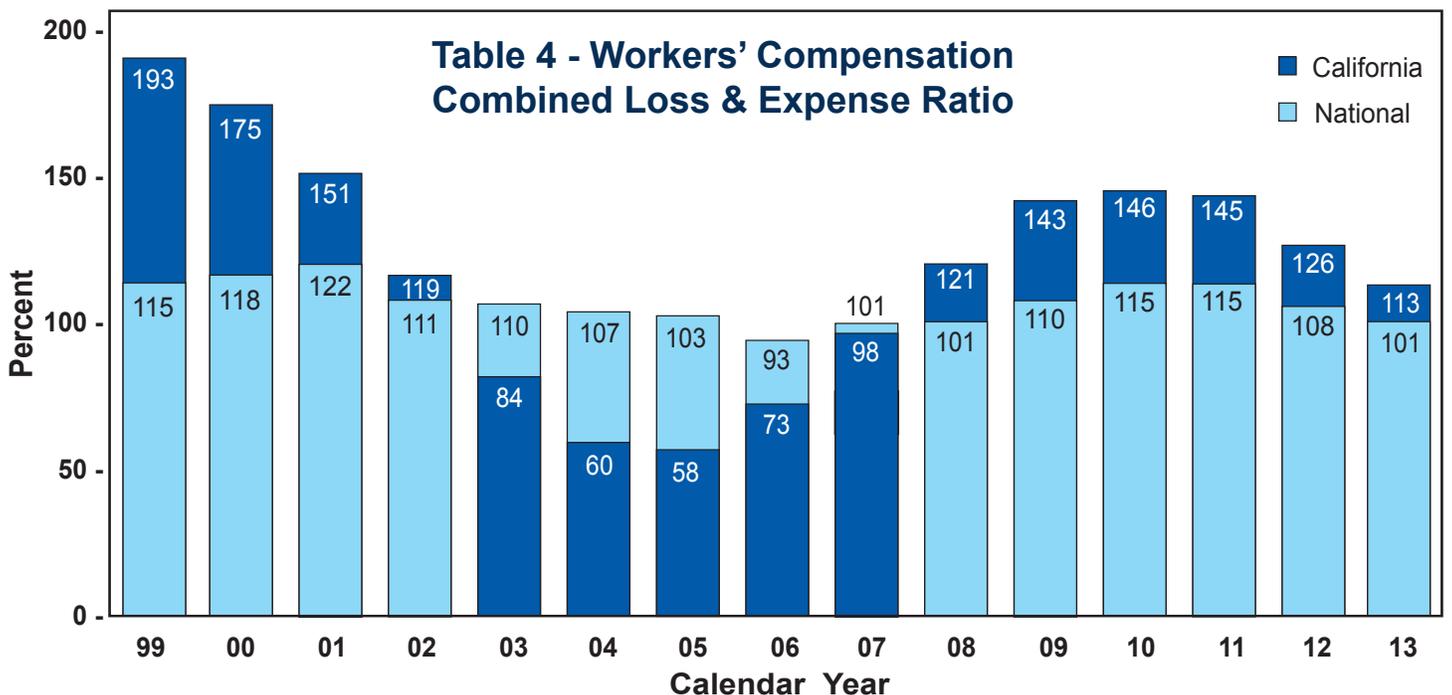
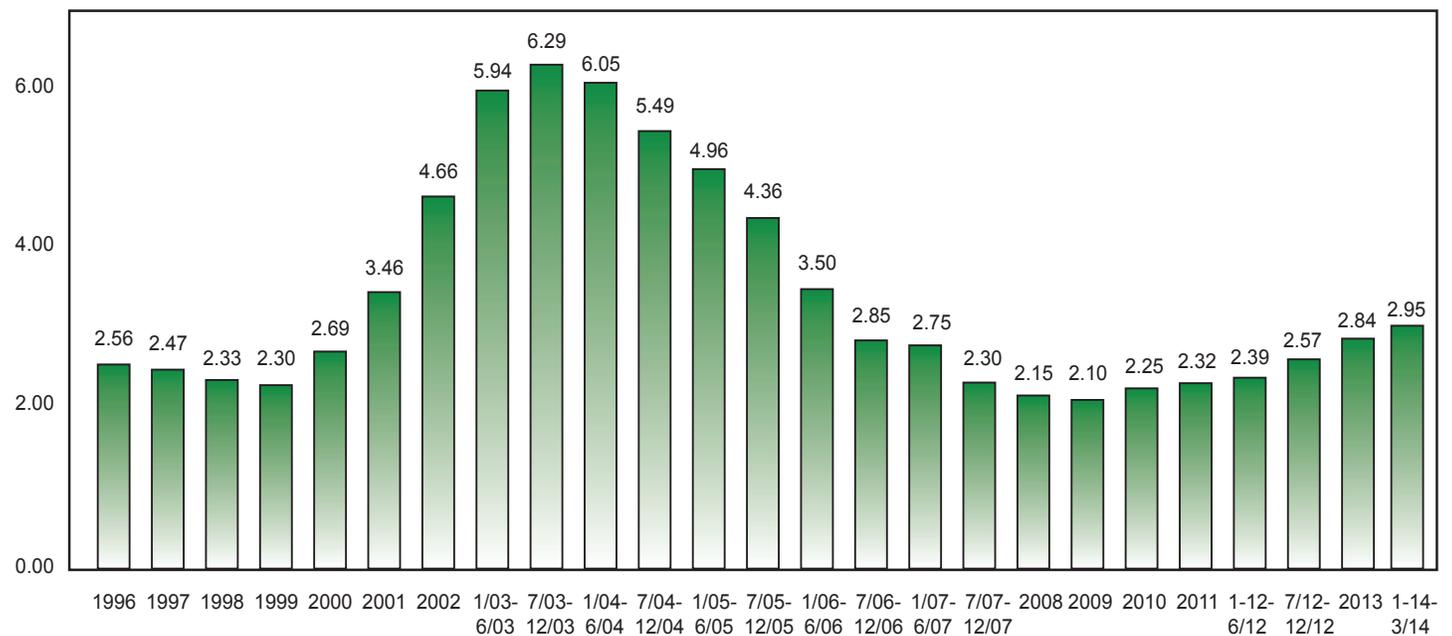
which means the industry still needs some additional rate to return to profitability.

While the Workers' Compensation Insurance Rating Bureau (WCIRB) has yet to publish its recommended loss costs, it is estimated it will be in the 7-8% range. Most of the insurance companies we work with have filed for or announced similar rate increases.

While every insurer will publish their own rates, on average rates in California should increase 5-10%. National results have been marginally better, but each state will vary.

**Table 3 - California Workers' Compensation Industry
Average Charged Rate per \$100 of Payroll**

\$ Dollars





Conclusion

The insurance industry is in a better financial position today than it was a year ago mainly due to the positive results in 2013 and the early positive predictions for 2014.

The industry, however, has not forgotten the mediocre returns experienced from 2008-2012. Most underwriters still want more rate, however, preferred risks should be able to negotiate flat renewal pricing or possibly modest rate decreases. The exceptions as mentioned above are with Workers' Compensation and Executive Risk.

While the health of the insurance market will directly affect what you pay for insurance, a much more important element is your Risk Profile. When an underwriter considers your account, they will evaluate your overall operations, your HR practices, safety culture and overall safety practices as well as your loss history.

A positive Risk Profile will result in substantially better pricing than a lousy Risk Profile. This underscores the importance of proactively managing your cost of risk. While you can't control the insurance marketplace, you directly control your Risk Profile.



A Healthier Thanksgiving

Thanksgiving meals usually include an abundance of unhealthy food options, making it easy to stray from proper nutrition until the start of the new year. But if you opt for a healthy Thanksgiving meal instead, it doesn't mean it can't also be enjoyable. With a few changes, you can make your "Turkey Day" an extension of your year-round commitment to good health.

Begin with the elephant in the room: food. You can probably stand to forgo a luxury or two come turkey time. But don't worry; you can still enjoy a delicious meal with the added bonus of feeling much better afterward. Plus, Thanksgiving is just the start of the holiday season, so there will be a lot of large meals to come.

Start by having breakfast. While many

Americans make it a habit to wait to eat until the holiday meal is set out, eating a small meal in the morning can give you more control over your appetite, allowing you to be more selective in your food and beverage choices later on. Keep in mind that you can always have leftovers the next day.

When moving on to Thanksgiving's centerpiece—the turkey—be sure to go skinless. Just 1 ounce of turkey skin contains 80 calories and 2 grams of fat. Also, be sure to use fat-free chicken broth to baste the turkey and to make the gravy.

Next, turn your attention to the side dishes. Substituting skim milk or half-and-half for whole milk and cream in recipes is an obvious choice, as is omitting bacon and cheese from

any casseroles, but how about complementing these sides or ignoring them altogether in favor of steamed or roasted vegetables and cornbread?

If you must have a holiday favorite, make sure it is just that, and not something you consume regularly during the year. And be sure to police your portions, since there are definite consequences to having too much of a good thing.

Once you've made smarter choices regarding your turkey and your side dishes, you may be wondering if there is anything else you can do. There is!

Take a walk early in the day and then again after dinner. It is a wonderful way for families to get some physical activity and to enjoy the holiday together. For those who have the day off after Thanksgiving, plan an additional workout. You will feel like your old self in no time, ready to manage your diet and exercise regimen right away, instead of waiting until Jan. 1.

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Ebola Outbreak Reaches U.S.

The recent deadly outbreak of Ebola in West Africa—the worst in history—has seized the world's attention, along with news that the virus has shown up in the United States.

Ebola is an acute viral illness characterized by the sudden onset of fever, debilitating weakness, muscle pain, headache and sore throat. People often confuse the illness' early symptoms with cold or flu symptoms.

Ebola is not a respiratory disease like the flu, so it is not transmitted through the air or through contaminated food or water. Ebola can only spread to other humans via contact with their bodily fluids, including saliva, sweat, blood and vomit, so people can only get Ebola from touching the bodily fluids of a person or animal that is sick with or has died from Ebola, or from exposure to contaminated objects, such as needles.

Though the Ebola outbreak has shown up in America, health officials have stressed repeatedly that the general public is at very low risk for contracting the virus, and they are instructing health workers on the proper precautions to take if they are called upon to treat an infected patient.

Can You Really Boost Your Immunity?

As cold and flu season rolls around, there are a bevy of products you can turn to that purport to help boost your immunity. But how well do they actually work?

Since the function of the immune system is to react to challenges and develop new defenses, it can be improved. Every time you catch a cold or get vaccinated, your immune system builds a new army of killer T-cells, ready to fight off a future recurrence of the same pathogen.

But there is no nutritional supplement, superfood, or mind, body or spirit technique that will do this for you. Harvard Medical School has stated, “The concept of boosting immunity actually makes little sense scientifically. In fact, boosting the number of cells in your body—immune cells or others—is not necessarily a good thing,” and can lead to autoimmune disease in the case of your immune system.

So while you can’t supercharge your immune system, you can take precautions to prevent getting sick. These include practicing good hygiene (like regular hand-washing), getting vaccinated (including flu shots), practicing food safety, being knowledgeable and vigilant when traveling to foreign countries, drinking clean water and practicing safe sex.

Lower Winter Fuel Costs



Budgeting money for the holidays is always important, but many people often forget about the increased energy costs associated with winter until they get hit with the bill. Use the following recommendations from the Department of Energy to keep your costs in check this year.

- Cover drafty windows with heavy-duty, clear plastic sheets, or tape clear plastic film to the inside of your window frames.
- Seal the air leaks around utility cut-throughs for pipes, in gaps around recessed lights in insulated ceilings and in unfinished spaces behind cupboards and closets.
- Maintain a regular service schedule for your heating systems. Replace filters once a month or as needed.
- Set your thermostat as low as is comfortable. Turning it back 10 degrees at night or before leaving your home can save around 10 percent of your heating bills.
- Finally, use LED holiday light strings to save on the price of seasonal decorations.



Sweet Potato Casserole

Skip the marshmallows this year. This five-ingredient sweet potato casserole is low in fat and rich in flavor, and makes for a perfect side to complement your Thanksgiving meal.

- 2 tbsp. low-fat milk
- 1½ tsp. brown sugar
- 1 tsp. ground cinnamon
- ¼ cup quick cooking oats, dry
- 1 can low-sodium sweet potatoes, drained and chopped

Preheat oven to 350° F. In a small bowl, combine milk, brown sugar, cinnamon and oatmeal. Mix well and set aside. In a medium-sized baking pan, add the sweet potatoes so they cover the bottom of the pan. Add the oatmeal mixture on top of the sweet potatoes. Bake for 20 minutes. Serve hot, or refrigerate and serve cold.

Yield: 6 servings. Each serving provides 94 calories, 0.5g of fat, 0g saturated fat, 0mg of cholesterol, 30mg of sodium, 5g of sugar and 3g of fiber.

Source: USDA

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SPOTLIGHT ON



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WARRIOR FOUNDATION FREEDOM STATION

Serving Military Heroes in Transition

The Warrior Foundation-Freedom Station vows to be the leading force in assisting, honoring and supporting the military men and women who have so bravely served and sacrificed for our country. They are committed to supporting their warriors in a variety of ways, providing quality-of-life items and numerous support services designed to assist them and their families during recovery.

The Warrior Foundation-Freedom Station assists four main groups of warriors: the Seriously Injured (SI) just returning home from war; those suffering from post-traumatic stress disorder

(PTSD) or traumatic brain injury (TBI); those undergoing physical or occupational therapy, and warriors who have been medically retired and remain in our community.

To serve this last group in particular, Warrior Foundation-Freedom Station pioneered a new approach and opened Freedom Station - a unique recovery transition center and housing facility that provides injured warriors with the acclimation time, guidance and resources to successfully make the transition from military service to civilian life.

For more information about Warrior Foundation-Freedom Station, go to www.warriorfoundation.org.