Slim Pickings For Services Industry Risks

Prolonged soft market, down economy drives fierce competition for shrinking business

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The hardening market predicted to arrive by the end of 2009 failed to materialize for insurers writing services industry risks as competition remains fierce, forcing carriers to cut the prices on their coverage menus.

The struggling economy and excess capacity among insurers have combined to create a situation that has carriers in the standard and excess and surplus lines markets competing hard for less available premiums among struggling services industry buyers, and experts do not all agree on when rates are expected to harden.

Generally, those who spoke with *National Underwriter* expect to see some improvement in rates by the end of 2010, which would bring to an end what all agree has been an unusually long soft market for the property and casualty industry in general.

WITH UNEMPLOYMENT SKY HIGH and discretionary spending way down, restaurants are seeing cuts in sales and payroll, leaving carriers to fight over a smaller portion of insurable exposures.

But one wholesale broker said he is approaching 2010 as if there will be no rate hardening--as if the current conditions will be the market reality for insurers for the foreseeable future.

In addition, with standard markets continuing to write more service industry risks usually handled by E&S players, competition promises to keep prices down.

One wholesale broker said she has seen standard markets taking on some limited liquor liability risks, which is generally unheard of even in softer markets.

One of the two major factors prolonging the soft market is the amount of capacity still available. Kyle Stevens, president in the Dallas office of Western Security Surplus Insurance Brokers, cited an overflow of capacity, and said new players continue to find the necessary capital to expand into the service markets.

Barbara Carter, a branch manager at wholesale brokerage Burns & Wilcox in Birmingham, Ala., said reinsurance rates for 2010 did not go up as expected. Instead, she noted, buyers saw reductions in rates, which will help to prolong the soft market.

Ken Laderoute, vice president of underwriting for Burns & Wilcox, said that from a capacity standpoint, he does not expect to see any turn towards a hard market until combined ratios get to around 105 or 110. That is generally what it takes to bring on rising prices, he noted, adding the market will eventually "get to a certain point [where] this has to stop, [but] that hasn't happened yet."

Aside from an abundance of capacity, the recession is impacting the services industry, and therefore the insurers writing those risks. All those interviewed by NU agreed that the recession does not appear to be ending for the services industry despite government claims of a recovery, which will keep demand for coverage depressed and prices down.

Regarding the possible turnaround of the economy, Mr. Stevens said, "we're not noticing any change as of today," adding that the effects of the recession are not over at most of the bars he insures.

Others echoed Mr. Stevens' comments. Mr. Laderoute said the economy is affecting consumers' discretionary

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spending, which is impacting restaurants, hotels and other services businesses. “By and large, people are still not going out,” he said. He added that there have been very few new restaurant openings, and Ms. Carter said receipts are not what they were in 2007 and 2008.

Although fast-food restaurants were cited as a diamond in the rough for the service industry in the last *NU* review of the sector, as consumers shop for cheaper meals, Richard Kerr, chief executive officer at MarketScout--an online exchange which puts out the monthly “Market Barometer” survey on insurance pricing trends--noted that even McDonald’s is reporting lower revenue. “If McDonald’s can’t make it, how is ‘Jimmy Jack’s Burgers’ going to make it?” he said.

Noting that a recovery does not appear to be in sight for many restaurant owners, Mr. Kerr observed that “all these business owners are scared.”

For insurers, the continued decline in business for restaurants, bars and other service industry risks means fewer available premium dollars. Mr. Laderoute noted that policy counts may even be up, but the average premium per policy is down because of declining sales and payroll.

Mr. Stevens said in traditional soft markets, insurers are able to generate premium even with reduced rates, but they are unable to do so in this market due to the economy, and so they are fighting even harder for what premium is out there.

The end result has been what all three wholesale brokers interviewed by *NU* characterized as a slugfest between standard carriers and the E&S market.

“It’s gotten more competitive,” Mr. Laderoute observed. He said there was a short spike in rates late in 2009, but “that deteriorated again to the position of pretty strong competition.”

He said E&S carriers, to compete with standard markets, are cutting rates to areas where his brokerage will not go.

Mr. Stevens--who writes mostly risks with liquor liability that are avoided by the standard markets--said E&S and specialty carriers are battling it out for those risks as well. He said there are “only a few players in this niche, but the ones who really write this stuff…get very, very aggressive on price, to the point where we back off.”

But Mr. Laderoute sympathized with E&S carriers to some degree. “If you’re a carrier,” he said, “how far can you let your market share slip? You can back off and not compete that way, but at some point you have to compete on some level to maintain your book of business.”

As for the standard carriers, Ms. Carter said, “they’re buying business and leaving money on the table.” She added she is losing risks to the standard market that are being written at a third of the normal price.

And it is not just price that’s being affected—it is risk appetite. Ms. Carter said standard markets are writing service industry risks they have traditionally avoided—new-venture restaurants, facilities with losses or a history of poor management, and even some with limited liquor liability.

“I’ve never seen standard markets write liquor liability the way they have in this market,” according to Ms. Carter.

For wholesale brokers, the strategy to survive in this market becomes superior service. Ms Carter said her brokerage is working to improve turnaround time on quotes, including quoting risks subject to the receipt of more information.

Mr. Laderoute said while some are predicting the market to turn in 2010, he is approaching business as if the current conditions are now considered “normal” for the service industry sector.

To survive and thrive, he said his brokerage is working at demonstrating underwriting expertise in certain lines to create “centers of excellence.” He said he does not believe the standard markets have the same levels of experience or knowledge in service industry risks as the wholesalers and E&S companies possess. “We do a good job,” he said. “We just need to step up our level of service.”

The understanding of risks taken on by insurance companies is what was supposed to be different about this soft market cycle. To some degree, experts agree that the underwriting is smarter this time around.

Ms. Carter said standard carriers in territories in which she writes business are bringing in E&S people to help write the new risks they are taking on.

Mr. Kerr said companies are taking aggressive stands in this soft market, but he said it is “not rogue underwriters doing this. They know what they’re getting into.”

Some, such as Mr. Stevens, have less faith. He said he does not believe many lessons were learned from previous soft markets. “Companies will say that,” he stated, adding that while some remain true to their underwriting beliefs, other markets will preach that message while getting very aggressive. He called it “a real lack of underwriting integrity and discipline.”

Looking forward, Mr. Kerr said prices are beginning to moderate in the insurance industry overall, but not at the pace that had been anticipated. But he said the market has improved compared to six months ago.

Throughout 2010, Mr. Kerr said, premium reductions should moderate, and then flatten. By the end of the year, he predicted, rates should begin to turn higher. “We will come out of this,” he concluded. “It’s just going to take a while.”

“I think we all missed [the end of the soft market] by about six months,” he added.

Ms. Carter said people will have to be put back to work before the market can improve. With people working, she said, discretionary spending will rise and more people will take vacations and go out to eat.

Until then, underwriters should expect slim pickings in terms of rates for the year ahead.

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