UK P&C Insurance

Equity

Asleep at the Wheel: A Study into the Impact of the Recession on Commercial Insurance Risks

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- **Report Aim** — In this report we set out a summary of the key findings from an in-depth study into the impact of the recession on the nature of the risks to which UK corporates are exposed.

- **Analysis** — This analysis has been conducted by Mactavish, an independent research firm that focuses on risk and insurance. Their report is the product of extensive interviews with CFOs, risk managers and operational management across a wide spectrum of medium and large companies and insurance underwriters across four sectors — Manufacturing, Retail, Construction and Financial Services — that have been particularly affected by the downturn.

- **Key Conclusions** — The main conclusion of the Mactavish investigation is that the disruption and dislocation of the last 18 months, and the ensuing changes to business models, has significantly increased risks to which companies are exposed. Yet, at the same time, both companies and insurance companies are proceeding as they were before, and it is debatable whether the insurers are even aware of this systematic change in the risk landscape.

- **Implications** — If Mactavish is right, then there is likely to be a pick-up in insurance claims across commercial lines, from business interruption to product and employers liability, none of which is being priced for given the inherently backward-looking focus of the insurance industry. The fact that claims have not picked-up yet is of limited comfort given the long-duration nature of the exposures and the fact that the pace of change has accelerated and is still ongoing.

- **Why This Matters To Investors** — We think P&C analysis tends to spend too long focusing on demand and supply, when it is underlying claims costs that are the biggest drivers of the cycle and industry pricing behaviour. In this respect, claims issues drove the re-evaluation of pricing in 2002-2004, with 'hard market' margins then boosted to 'excess' levels by a period of very benign claims conditions; in turn, outsize margins have been competed away on recent accident years at the same time as loss costs have grown at a faster pace than GDP. With reliance on reserve releases from the benign years of dubious sustainability, we believe that this leaves the P&C industry with absolutely no slack to absorb any further margin erosion. In other words, a sharp increase in commercial claims could be the “straw that broke the camel’s back”, driving a substantial shake-out, but with real differentiation between the insurers that are prepared and those that are not. We see this as a key theme for 2010 and 2011 in a number of the more cyclical P&C markets, of which UK commercial insurance is very clearly a prime example.

See Appendix A-1 for Analyst Certification and important disclosures.

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Introduction

This report contains a summary of a detailed report produced by an independent research firm, Mactavish, which has undertaken an extensive study into the impact of the recession on the UK commercial insurance risk landscape.

Severity of the current recession has brought with it an unprecedented level of change to UK corporate risk profiles

The background to this study is the recognition that, over the last two years, many companies have been forced to respond to rapid and overwhelming changes in trading conditions, and that this has caused a systemic shift in the corporate risk landscape. The Mactavish study arose from the realisation that the impacts of economic upheaval would likely be severe and lasting. Beyond the headlines, a plethora of nitty-gritty operational change is taking place, and Mactavish set out to investigate such changes and the consequences for risk and those who manage it. The findings have exceeded all expectations in both the materiality of such shifts to the risk landscape, and a widespread lack of readiness to address them.

What is Mactavish?

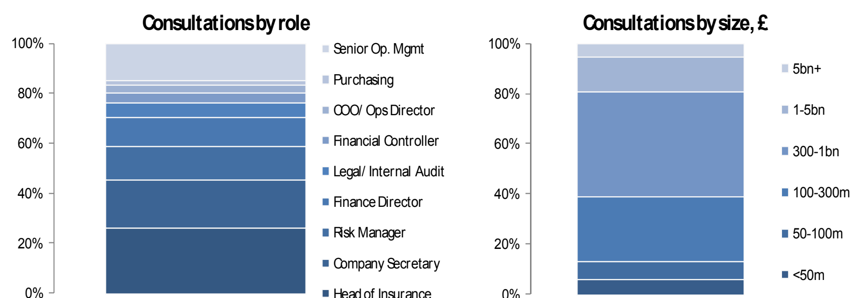
Study suggests materially increased risk but little recognition to date from either companies or their insurance providers, and predicts volatile consequences.

Mactavish is a research firm specialising in commercial risk and insurance. In particular, the study's interest lies in analysing changes to high-severity risk and developments in higher frequency loss types where the aggregate impact is also material.

What has been its approach?

Part of a large-scale, ongoing 2010 programme, this Mactavish study has to date comprised in-depth consultations with operational and financial management in c.250 large and mid-size independent UK companies (defined as broadly above £50m in turnover, of which this sample represents over 7.5%). It has also included c.40 interviews with senior underwriters driving insurer policy in relation to these sectors, across all critical risk categories. The report initially focuses on four UK sectors: Independent Manufacturing, Construction, Retail and Financial Services.

Figure 1. Customer Research Breakdown



Source: Mactavish

The overall approach was to consider for each sector:

- Systemic changes and challenges emerging across the sector value chain and the potential impact on specific operating risks throughout the system;
- Emerging corporate responses to such developments, whether operational, strategic or financial;

- Associated developments in insurance capital and service requirements, and the extent to which such requirements are being met.

By far the most in-depth research of its type, the study seeks to identify and analyse the detailed operational reality underlying recent commentary from the CBI and others on the significance of lasting change requirements to companies' financial and operational working practices. The report then considers the implications of this change for the corporate insurance industry given critical limitations to the current risk disclosure and underwriting model. In addition, it supports an emerging regulatory focus on the adequacy of risk identification, reporting and management within the corporate governance framework.

Why does this matter to investors?

While commercial insurers have, by and large, had a "good" recession — in that they have emerged relatively unscathed and certainly in far better shape than most other parts of the financial services industry — investors remain somewhat unconvinced about prospects for the sector.

In the risk rally of 2009, this was not surprising given limited direct operational or balance sheet gearing into an improving economy. Nonetheless, this does not tell the full story, with the limited enthusiasm for P&C insurers reflecting a number of profitability headwinds that make the earnings outlook somewhat weak, including lower bond yields, dubious reliance on 'old year' releases and a deeply lacklustre pricing environment. In this latter respect, the attempts of some insurers to 'talk prices up' have singularly failed to gain traction and we see little prospect of this changing any time soon.

However, beyond the short-term earnings concern, there is also a suspicion that the end of the cycle that started back in 2000 may not be the 'soft landing' for profitability that might have been hoped for a few years ago. In this respect, the biggest driver of profitability over the last decade has not been pricing but underlying claims costs, with liability-driven problems forcing a re-evaluation of risk in 2002/2003, followed by a period of extraordinarily benign conditions for claims costs, but with excess margins competed away in the last three years at the same time as losses have started to creep up again. All of this leaves the P&C sector with little room to absorb any further pick-up in claims costs, let alone the structural shift envisaged by the Mactavish research.

Of course, the issue of underlying claims trends has been a repeated feature of discussions between management, investors and analysts over the last two years. And, to be fair, the overwhelming response of P&C insurers to date has been that the overall impact of the recession has been fairly benign.

While it may be the case that insurance management are indeed firmly on top of this issue, if the Mactavish study is right, then it is likely that the impact of the recession has yet to work its way through the system, with the potential for the changed risk environment to have much greater impact in 2010 and 2011. As such, we think this is an area that investors need to be on top of, as these trends could have a material impact on stock prices over the next 18 months, not only at a sector level, but also in differentiating between those insurers that are prepared for this outcome and those that are not.

Analysis of Sector Operational & Risk Changes

Increased pace and scale of concurrent change measures seen in all investigated sectors

This section of the report considers the basis and importance of an altered business change dynamic from an insurance perspective.

Corporate strategies and operational methods rarely stand still for long regardless of economic circumstances, and innovations will always mix success with failure. Alterations to risk profiles tend to be relatively gradual and evolutionary, as losses begin to emerge from long term change. This supports an insurance underwriting approach predominantly based around historical loss analysis and balancing portfolio exposures. However, the Mactavish investigation suggests that the materiality and prevalence of current change will increasingly stress this system over the next 1-3 years.

Net impact to increase complexity and underlying risk across several traditional insurance risk classes

Mactavish research suggests that the focus of headlines on bailouts and company failure rates actually underestimates the aggregate significance of current operational change. Instead, their report points to new and increasingly systemic impacts felt throughout all industry segments studied, as even relatively robust and larger firms are forced to adjust for the long-term.

Business in 2010 is far more interconnected, and specialised, than even 10 years ago, and this increases the scope for financial and operational difficulties in one part of an industry to reach out across the value chain and even into apparently unrelated segments, fundamentally shifting the risk landscape as they go.

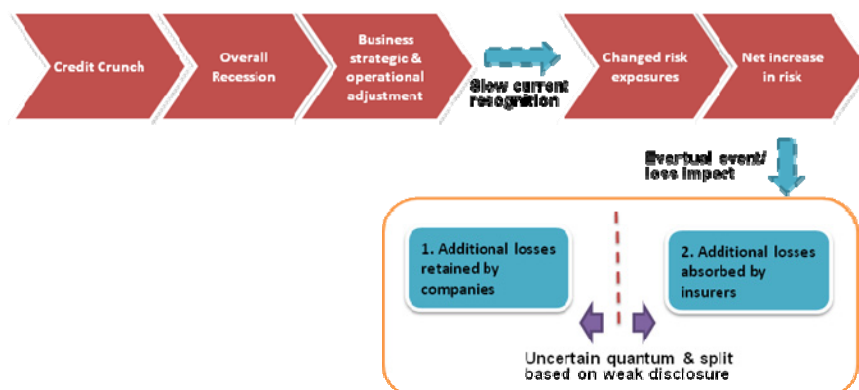
A central thesis of this report is that severe economic shocks have altered the gradual view of loss pattern change through a combination of noticeable effects:

- Prompting new operational responses;
- Increasing the scale and pace with which existing measures are adopted;
- Increasing the propensity for multiple change measures to be adopted concurrently, making likely a second round of innovation as some inevitably fail.

Increased consequences of limitations to individual risk disclosure model

The Mactavish report further contends that this challenge shines a brighter spotlight upon the day to day disclosure and underwriting process, requiring understanding to be built at the point of policy underwriting (rather than the point of claim) regarding the ultimate risk impacts of such new operational change. Thus the burden on risk disclosure increases in the current climate, as do the consequences of any limitations to the traditional risk assessment model. Such risk change, and greater uncertainty over the transfer of new or altered risks where disclosure is weak, can be viewed as a natural consequence of business disruption resulting from the credit crunch and ensuring recession, as shown in Figure 2 below.

Figure 2. Increased risk as final, largely unrecognised, chapter of credit crunch



Source: Mactavish

The Mactavish study explores each step of this argument more fully both in the main report and the summary findings set out below.

A number of recent strands of commentary further support the importance of the subject of corporate risk scrutiny and the adequacy of its governance. These include the CBI's finding that business leaders increasingly expect the severity of this recession to change attitudes to corporate leadership and funding for a generation, forcing many companies to fundamentally rethink working models. The Financial Reporting Council's proposed changes to the UK Corporate Governance Code specifically advocate significant risk management and risk reporting reform, and similarly the long-term implications of the recent Walker report on corporate governance and risk stewardship are likely to extend beyond Financial Services. Finally, Law Commission reform on insurance law currently under consideration suggests very limited recognition amongst companies of the legal burden placed on them around risk disclosure. The Mactavish study aims to analyse the real operational detail underlying these concerns.

Critically, however, it is first necessary to flesh out what we mean by the increased change found within the research. The following case studies provide an introduction to some key findings by sector detailed in the main Mactavish report, and provide real evidence of the materiality involved. In each case, a subsequent sector-specific report will be published later in 2010, expanding upon specific risk observations and considering the emerging insurance industry response.

Sector Research Highlights

Sector One – Independent Manufacturing

Research focuses on independently owned and British domiciled manufacturing firms, across a wide range of product segments. We largely sought to exclude those subsidiaries of overseas owned multinationals where the UK entity's risks may have been predominantly managed by the parent.

A sample of the key change themes raised by respondents is set out below.

More and faster outsourcing creating supply chain complexity and new supply and quality risks

1. Increased speed and scale of low cost outsourcing trend and/ or overseas Joint Ventures

By no means a new trend, raised by around half of all manufacturing respondents as a current project with many choosing the recession as the right time to either finally take the plunge towards overseas manufacturing, or to scale up existing plans to realise much needed financial benefits faster. Findings suggest a current surge in outsourcing, increasingly including design & support activities previously considered core and maintained in the UK.

"We need to be very careful in considering developing markets, often in partnership with local providers. It is inevitably a more complex logistics chain, and creates real challenges in managing regulatory differences and people from new cultures" (Insurance Manager, Independent Manufacturing, £100m-£300m)

Diversification to limit revenue loss Respondents split between those that have undertaken a long term, multi-year scoping exercise to identify, select and build relationships with overseas partners, taking time to gradually transfer expertise, tooling and management capacity, and those where economic necessity and apparent spare capacity in Asia in particular have encouraged a more rapid transfer of production.

Major risk issues emerging centre around a) ensuring resilience of a much less visible and harder to control supply chain and b) ensuring that quality controls throughout the supply chain, testing and contractual arrangements reflect less tightly controlled risk. As an existing but accelerated trend, underwriters are very much aware of the increased risk potential in both areas, although a worryingly small proportion of buyer respondents had really analysed or communicated additional risk management requirements.

Diversification to limit revenue loss creating new and changed product/ professional indemnity exposures

2. Increased product development and diversification into new & unfamiliar products / services / territories

The response of many surveyed firms (again half the manufacturers consulted) to a drop in demand has been to seek to expand into new product/ service areas or target market segments where demand is thought to be potentially more robust, e.g. electronic component manufacturers moving into renewable energy markets and automotive suppliers shifting away from a troubled core business. Since product risk (i.e. the damage a defect can wreak) is inherently end-use driven; even subtle changes here can drastically alter the underlying risk an insurer takes on. This creates a very specific duty of risk disclosure, which many have not yet considered.

"We are investigating a lot of new opportunities, particularly as regulations change. Of course there are greater risks — new segments, new locations and in dealing with both suppliers and customers with whom we're less familiar" (Group Financial Accountant, Independent Manufacturing, £100m-£300m)

Similarly, even where companies remain focused on core manufacturing competencies, we have encountered numerous examples of a) increased rates of product innovation and b) extending pure 'product' provision into a wider service offering, both to support differentiation in a declining market. The former increases the risk of product failure, which is greater on new than old model products as any design bugs are ironed out. The latter can introduce a whole new category of professional indemnity risk associated with product assurances or support advice, which many manufacturers are not used to addressing or purchasing insurance coverage for.

Such examples can be extreme: one large business in a high-risk technology product segment had doubled its rate of new product launches in 2009, whilst cutting manufacturing lead times by 75%. From a quality management perspective, twice as many new products in less than 25% the development period causes significant additional strain and directly raises risk. Even where such changes are more subtle, they often move companies closer to the cutting edge of their industry's innovation curve, where risk tends to concentrate.

Raft of structural and efficiency measures throughout supply chain disturbing well-established risk profiles

3. Systemic supply chain disruption reducing resilience through widespread operational rationalisation

Given the complexity and inter-connected nature of most modern manufacturing supply chains, the degree of disruption caused by business failure/ insolvency amongst suppliers in one part of an industry system across the remainder of that system is widespread.

Significant impacts arise not just from outright failure, but also broader rationalisation measures taken to maintain business viability across all stages of the product supply chain: headcount reductions, site closures, stock reduction, reduced customer batch/ order sizes, shorter lead times, efforts to improve sourcing efficiency, etc.

"There has definitely been a big impact all over the industry. There was a situation recently where a supplier of a key component went bankrupt. The company then refused to release the design and the tooling — it really made us realise our vulnerability to certain suppliers went far beyond what we'd previously realised.' (Internal Audit Manager, Independent Manufacturing, £300m-£1bn)

All of this impacts risk, particularly resilience to interruption across the supply chain from raw material to end-product customer, creating a systemic disruption to previously established risk and loss profiles. In addition, product quality control infrastructures may also become more stretched.

Details are often confidential by nature, but c.85% of manufacturer respondents raised concern with changes of this nature impacting the risks they faced, either directly within their own business or via supplier and/ or customer relationships. Specific examples discussed included enforced single sourcing (in place of 2-3 previous suppliers); the elimination of buffer stock or any production overcapacity throughout the value chain; consolidated production and distribution centres increasing risk accumulation; rapidly bringing on scale of new supply capacity, etc.

Given the already notorious difficulty of business interruption underwriting judgements, and the increasing proportion of total property damage loss costs they represent (some senior underwriters interviewed for this work put this figure as high as 70%), myriad changes of this nature prompt a clear need to re-scrutinise supply chains across the segment as little assumed knowledge remains reliable.

Many firms forced to accept new and routinely undisclosed additional liabilities

4. Shake-up also changed liability distribution across value chain

As greater competitive pressures prompt operational response measures, they can also give rise to new contractual stress, as both large customers and distressed suppliers can seek to renegotiate liability terms.

"We are routinely now receiving pressure from customers whereby they try to transfer what feels like unlimited liability for the entire project. It's getting much harder to negotiate." (Internal Audit Manager, Independent Manufacturing, £100m-£300m)

Over a quarter of manufacturing respondents believed that they have, as a result of increased pressure, been forced to accept more liability in current contract negotiations than under expiring contracts. In these cases, despite best efforts to impose standardised contracts and control liability creep, some additional liabilities were being assumed in relation to design risk, product warranties, recall costs, consequential loss, etc.

Critically, many respondents where this is the case did not consider themselves obliged to clarify any such change to liability insurers or undertake any additional proactive disclosure, and thus the new underlying exposure often remains undetected.

Figure 3. Case Study One

Case Study One (Electronics Manufacturer)

- Response to increase innovation & shorten product R&D cycle – total range re-launch in early 2010
- Consolidation of UK distribution & warehousing operations from six sites to one sole location
- Recession as prompt for expansion of existing headcount reduction programme
- Exiting value segment entirely to focus on mid and high end products
- Expanded manufacturing outsourcing to China, leaving only the most specialist assembly in UK
- Large scale expansion of independent retailer channel to reduce large retailer dependence.

Source: Mactavish

Figure 4. Case Study Two

Case Study Two (Materials Manufacturer)

- Dominant exposure to two hard-hit core markets (automotive and construction) caused company to enter new customer segments and increase speed of international diversification to protect revenue
- Activity diversification also extended into new product material areas and partially into providing a 'packaged' service offering, creating entirely new professional indemnity risk potential
- Greater international spread and decentralised divisional structure felt by management to exacerbate central risk management and information disclosure challenge
- Increased recent pressure from major customers to extend the scope and scale of product guarantees provided, causing increased liability potential.

Source: Mactavish

Sector Two — Construction

Certainly amongst the very hardest hit sectors by the recession, research again focused on UK-headquartered firms and covering all key sub-segments: housebuilding, commercial property, civil engineering & public works, as well as support service providers, material suppliers etc. The demand impact in the first half of 2009 in particular was brutal and well publicised, devastating not just construction firm revenues, but impacting across the whole value chain. Public sector stimulus spending has picked up a relatively small proportion of the overall slack, whilst creating numerous operating challenges as companies race to take advantage.

The below selection summaries three of the change themes raised in the study:

Prevalence of flux in work undertaken creating new risk exposures and risk management needs must adjust accordingly

1. Diversification of work mix, increased Joint Ventures and flight to public sector leaving many companies working in unfamiliar territory

Over 60% of sector respondents discussed a material completed or current move towards bidding for new types of work, often public sector or involving new Joint Ventures, in order to substitute other sources of demand. Even where changes to work type are minor, contract structures, liability arrangements and governance / specification regime all pose new and unfamiliar challenges to management.

"Public sector work will simply not be the panacea: we have lost out from several projects being shelved, and it's a very different environment for us" (Risk & Insurance Manager, Construction, £100m-£300m)

Examples of more significant shifts into entirely new areas of required competency were also worryingly commonplace, with firms often bidding in new geographical areas and/ or for types of work well outside of their traditional fields of expertise. This may create exposure to new risk types (e.g. asbestos exposure or the risks associated with working in derelict buildings are clearly much more prevalent in refurbishment and infrastructure work vs. new building). The challenge to control both contracts and practical risk management in this scenario is very much increased.

"Contractors are now routinely winning bids they're not qualified to do' (Group H&S Manager, Construction, £500m-£1bn)

Whilst the Mactavish report is of course not questioning inherent construction sector competence, such factors clearly change the risks to which companies are exposed, and suggest that underwriters must analyse afresh both the mix of work firms undertake and the controls (both contractual and operational) in place to limit risk. Historic understanding of activities is a decreasingly reliable indicator of future risk.

Many respondents also believe a second round of company failures is likely as public sector funding runs dry before private sector recovery.

Increased negotiation over contractual liabilities creates risk uncertainty

2. Increased potential for previously excluded liabilities, as contracts become less standardised, Joint Ventures more common, and contractual terms come under increasing negotiation pressure

Almost all respondents recognised an increasing level of difficulty at an industry level in controlling contract terms under current conditions, in particular around liability capping. Negotiation between multiple desperate bidders and those controlling scarce budgets clearly increases the need to compromise and erodes the ability to institute standardised terms. A significant minority (c.30%) reported specific changes already instituted, which have increased contractual risks undertaken.

"There is already far less standardisation across our contract mix nowadays, as firms try to cap their liabilities and it gets harder and harder to negotiate" (Insurance & Risk Manager, Construction, £300m-£1bn)

In addition, c.35% of sector respondents report an increasing tendency to engage in JV activity to increase the scope of viable bid work. This group included several firms that had historically maintained a clear policy to avoid such arrangements due to the difficulty of cultural alignment and risk/ liability sharing. The message in short was that concerns over such risks are a luxury that cannot be currently indulged.

A significant proportion of respondents reported an expectation of increased liability disputes to emerge over the coming 12 months.

Direct negative risk impact of cost-cutting measures on several key sector risks

3. Intense cost cutting systemically increasing risk across the sector

General recessionary cost pressures have been extraordinarily pronounced amongst construction businesses, with significant aggregate funding impacts on areas such as health & safety risk management. Specific examples raised included sometimes drastic reductions in H&S headcount and budgets, and rationalisation of regional site management resource (e.g. redundancies expanding a single site supervisor's area of site responsibility five-fold). At least some knock-on impact on site practice compliance and injury incidence must be expected.

"Staff are under pressure in branches, rushing around with less people, so at an industry level we can definitely conclude that Health & Safety risks have increased" (Company Secretary, Construction, £1bn-£5bn)

This is exacerbated by massive increase in competition for remaining work and increasingly common 'suicidal' bidding practices, with typically 10+ bidders per tender vs. 2-6 bidders 18 months ago:

- Objective to maintain cash flow rather than assure profitable work within core competence areas;
- Less pre-qualification checks being undertaken;
- Increasing importance of price as bid decision criteria, increasing likelihood of corner cutting and downstream liability disputes.

We have also seen the emergence of new recessionary risk exposures, such as large-scale mothballing (one housebuilder consulted reported mothballing over half of all sites in 2009) increasing the need for site protection against vandalism/ arson/ risk to public, etc.

Although not likely an immediate issue, and not limited purely to construction firms, several companies in this segment raised the issue of overtrading risk, as once growth does return to the segment, the pressure on many much leaner organisations to rapidly scale up activities could stress risk management infrastructures even more.

Figure 5. Case Study Three

Case Study Three (Building Firm)

- Huge drop in revenue & profitability – newly loss making in 2008/9
- Rationalised operating regions with significantly reduced site supervision as managers cover 2-3 times more sites spread much more widely, including an unprecedented number of mothballed sites
- Cuts made to Health & Safety budgets and resources in place, further stretching control and oversight infrastructure
- Change in work focus away from new build to regeneration work – different operational requirements and local authority contract / governance structure altering risk exposure.

Source: Mactavish

Figure 6. Case Study Four

Case Study Four (Housing Developer)

- Collapse in speculative housing market prompted large scale redirection to social housing as well as headcount and cost reduction measures
- Adaptation requirement to new contracting framework and to manage increased lead developer liability potential: detailed fixed build specifications and far greater up front contractual definition as part of initial tender process
- Major disruption to established supply base to comply with public funding conditions creates new quality risk potential. Enforced move away from long-term supply relationships to social housing approved suppliers regardless of perceived cost/ quality comparison
- Specific concerns emerging around residual liability for defects given lower margin environment and severe competition driven cost pressure – increased need to scrutinise product sourcing for long-term quality implications.

Source: Mactavish

Sector Three — Retail

Another severely affected sector, practically all retail respondents (excepting those in counter-cyclical, low-budget product categories, and those dominated by value food products) reported a damaging demand impact through 2008/9 as low economic confidence drastically curtailed consumer spending. Research covered a wide selection of retail businesses: clothing; food; fuel; online/ catalogue specialists; generalist retail; low-budget and niche product specialists. Although there was a diverse set of findings in terms of the range of change measures being undertaken, the degree of financial and operational strain identified amongst UK retailers was extremely pronounced, with significant risk changes occurring and being only gradually recognised.

Again, the section below sets out a sample of three key change themes.

Increased retailer exposure to product risk arising from multiple shifts in supply network

1. Fundamental shifts markedly increasing retailer product risk exposure

Retail segment traditionally relatively insulated from product risk (both damage claims arising from products sold and the cost of recall), given their ability to pass liability up the supply chain to product designers, manufacturers, distributors and even component suppliers.

However, nearly three quarters (74%) of retail respondents pointed to recent changes that have materially increased this risk:

- Increased direct retailer involvement in product design;
- In some segments, growth of own brand retailer product share;

"The mix of what we sell has changed dramatically… …we are currently managing a very large product claim (>£10m), which came from a range of products deemed to be traditionally very low risk… …We now source extensively from the Far East… …we realise that there is simply no prospect of getting money out of them [specific Chinese suppliers]" (Insurance Director, Retail, £1bn-£5bn)

- Increased need to re-negotiate supplier liability terms, shifting established liability divisions and requiring retailer vigilance;
- Increased sourcing from low-cost country manufacturers where subrogation (passing on liability for the loss to the upstream manufacturer) is thought to be substantially difficult if not impossible (and contractual measures to manage such risk are often hard to enforce);
- Recognition of upstream cost pressures impacting the challenge of managing product quality risk in general (either through reduced quality control resource, suppliers sourcing cheaper raw materials or through the initial establishment of new, lower-cost manufacturing locations, or suppliers changing their sub suppliers of components without notification).

Of those who raised having undertaken the measures above, only around half had previously recognised a direct impact on risk prior to specific consideration during this research consultation. The extent to which such changes to risk have been quantified or communicated to insurers is therefore very limited indeed.

The minority of retailers that were unconcerned by these developments tended to be focused purely on very low-risk product categories.

Supply chain disruption had a major impact on retail sector resilience to business interruption risk in particular

2. Significantly re-shaped product supply chains impacting retailer operational resilience

Nearly 90% of retailers consulted pointed to important supply chain rationalisation measures having been instituted within the past two years, which have altered BI resilience. Common examples included the following:

"Since 2007 our business has experienced a lot of changes and we have many people new in their position who don't always have the experience to deal with what are often new risks. Our sales went down, we had to review our costs, and decided to close 50% of our distribution capacity and reduce the numbers of suppliers by two thirds… …at the same time we're moving more towards a JIT approach, which we are aware is more risky, but is a necessary step in terms of cost efficiency" (Company Secretary, Retail, £300-£1bn)

- Consolidation of multiple distribution centres / warehousing operations into substantially fewer or even a single site, increasing risk aggregation and reducing redundancy;
- Consolidation of supplier base driven by cost objectives, often without any specific consideration being given to business continuity drivers;
- Increased and more stringent adoption of 'Just in Time' methods and often significantly reduced stock inventories throughout the supply chain since the inception of the recession (in some cases to less than 50% of pre-recession levels), again reducing resilience;
- Reduced facility management resource, e.g. moving from dedicated facility managers at each warehouse (overseeing procedural, housekeeping and safety compliance) to as little as one per five warehouse sites.

Credit insurance contraction caused both widespread concern and a secondary impact on quality risk

3. Credit risk — reduced availability representing the critical near-term risk for many retailers, with knock-on product quality & supply reliability concerns

Credit insurance market contraction is particularly pronounced in retail given a number of retailers surrendering to bankruptcy (although the issue is far from limited to this sector). Around half of retail respondents raised this point as a key concern.

Sudden withdrawal of credit insurance availability against a retailer highlights the dependence of many firms on what is a highly volatile form of working capital, which financial management may be unaware is even being purchased against them until they have to deal with the consequences of its withdrawal.

"Last year no one wanted to work with us because it was impossible to buy credit insurance on our risk. As we were moving our supplier base to the Far East, we had to work with the few suppliers who agreed to sell to us — it's far from ideal". (Finance Director, Retail, £100-£300m)

Retail examples raised included immediate demands from suppliers for up-front payment (or drastically reduced payment terms, e.g. from 90 to 15 days) for extremely significant sums (some into the tens of millions) to continue supply, adding further strain to already difficult cash flow conditions.

Companies are also being newly required to spend time and senior resource liaising with credit insurers to convince them to continue offering cover to their suppliers based on financial health.

The most direct risk consequence is that such withdrawal can leave already vulnerable retailers unable to access a sufficiently wide base of suppliers, with the highest-quality suppliers opting to align with retailers in the best financial health (especially in troubled segments where competing retailers are all chasing a shrinking pool of viable potential suppliers). A significant minority (over 20%) of retail respondents were actively concerned about the potential downstream impact on product quality due to limited supplier choice arising from a negative financial perception and credit insurance withdrawal.

Figure 7. Case Study Five

Case Study Five (High Street Retailer)

- Severe revenue drop in 2009 led to closure of a substantial number of retail locations
- Project to review supply base resulting in >60% reduction in the number of suppliers used whilst identifying a number of new areas of single-source dependency
- Consolidation of multiple distribution centres to a single site, increasing risk accumulation as well as intended efficiency gains
- Growth in 'own branded' products sold combined with increased upstream product design involvement expand product liability scope – objective to triple to c.50% value share
- Rapid expansion of Far East product sourcing programme – previously unknown quality issues emerging and subrogation difficulty already experienced alongside cost savings

Source: Mactavish

Figure 8. Case Study Six

Case Study Six (Diversified, multi-channel retailer)

- Implemented ~£50m cost saving programme in 2009, including large scale redundancy programme and reduced opening & office working hours
- 25% reduction in total supplier numbers whilst expanding into many new relationships and geographic regions to secure additional cost advantages. New relationships increase both quality control and supply continuity challenge during ramp-up phase
- Additional complexity created by unprecedented speed of changes to product mix sold given altered consumer behaviour, exacerbated by reduced inventory throughout supply chain
- Significant product claim activity in relation to Chinese supplier and undisclosed upstream changes to manufacturing process, with expensive cost subrogation efforts unsuccessful
- Increased emerging technological concentration of risk given rapid online channel growth and greater systems reliance throughout business – creating new risk quantification challenges

Source: Mactavish

Sector Four — Financial Services

Marked FS sector reluctance to recognise impacts on operational risk despite obvious areas of turmoil

Financial services is perhaps the most challenging sector of interest given its centrality to the emergence of recession and the severity of the emerging regulatory shake-up. Research focus was on mid-sized financial institutions. While the Mactavish research sample was diverse, a number of critical areas will be analysed in a subsequent sector report.

A selection of the key points from the research are set out below:

1. Risk guardians in Financial Services are less willing than those in the other sectors investigated to accept, once challenged, that the credit crunch and recession necessitate review of how operational risks are managed

"Risks aren't changing; there are just changes in profitability" (Finance Director, Asset Management, £50-£100m)

Mactavish's research has highlighted a number of emerging notifications and insurance claims that have affected many different financial institutions: breach of investment mandates; mis-selling of investment products; errors and omissions claims because of volatile markets exacerbating trading errors; losses relating to a lack of proper due diligence on Madoff, with claims being made under Fidelity, PI and D&O insurances; employee fraud increasing because of the recession; claims against funds for imposing 'gates' and preventing redemptions; mortgage and valuation fraud involving solicitors, banks and building societies; claims against banks for custodial issues and Stanford; misrepresentations concerning the pricing of Collateralized Debt Obligations; negligent investment advice; failure to discharge oversight/fiduciary responsibilities properly leading to D&O claims; and vicarious liabilities for actions of outside service providers.

In addition to this changing insurable risk arena, the business environment is also undergoing wide-ranging environmental change, from the increasingly onerous regulatory obligations imposed by the FSA to the virtual seizure of the 'shadow banking' system.

The Mactavish study would therefore expect companies in the sector to accept, once challenged, the need to routinely review the way operational risks are managed given this backdrop. However, compared with manufacturing, retail and construction, the acceptance for such review is not widespread.

Perhaps the most surprising finding is the prevailing view Mactavish encountered that business models were essentially robust and did not need to adjust in light of the credit crunch and recession. Some firms are making changes to how specific operational risks are managed, but the majority did not think that a review of operational risk management was warranted. Half of all respondents explicitly argued that their businesses were simple, 'vanilla' organisations and that exposures to low-frequency, high-severity risk were not significant, nor were these exposures changing because of the downturn.

This finding is particularly concerning as it suggests a naive or complacent attitude within the sector to managing operational risk, particularly when contrasted with other sectors. Further, a vocal minority of respondents clearly stood out from this position: they believed that far-reaching changes to operational risks were emerging (either new risks or simply developing a better understanding of established risks as losses emerge) and were highly critical of the endemic complacency suggested by this view.

This also chimes with a key thrust of emerging FSA stress-testing policy, which lies in encouraging FS firms to take a more active and holistic approach to identifying unexpected risks to their business. The FSA has criticised a "collective failure of imagination" felt to historically characterise the sector's risk assessment approach

Although as a result of this reticence, precise clarity over future changed strategies and operations in order to better manage operational risk was harder to establish, this naivety or complacency alone should be of concern to insurance underwriters, as those consulted were specifically responsible for operational risk management and / or insurance disclosure.

Real challenge to convince underwriters of business model simplicity given high degree of current concern in several risk areas

2. Potentially damaging disconnect in perceived risks between financial services management and the underwriting community

There has been a marked shift in perception among underwriters of the risks faced by even relatively simple financial institutions and the interconnected complexity of how risks can spread throughout the sector.

"Buyers thinking that it's business as usual is extremely short-sighted — we're seeing already that it's not and there will be a lot more to come" (Senior Financial Institutions Underwriter)

While the majority of financial services respondents argued that their businesses remain fundamentally low-risk and straightforward, underwriters have reassessed the sector and it is one of few areas where the insurance market has already hardened somewhat. Insurance buyers in financial services therefore face a battle to counter external perception of risks within the sector and their businesses.

Overall, it is clear that most buyers have not yet made any real effort to communicate changes to operational risk at a granular level. Even where this effort has been undertaken, it has not yet been successful in allaying fears of increased risk exposures.

Expectations of new, large-scale claims issues in 2010 are commonplace among insurers. Hot topics include product mis-selling, valuation/ mortgage fraud, shareholder D&O lawsuits, and emerging cyber-crime risks.

With external understanding of financial services products and operational details typically limited, this disconnect should eventually lead to insurance capital being both less easy to access and increasingly costly. This perception gap will likely not narrow unless buyers in financial services become more willing to articulate changes to business risk and risk management practices.

A number of risk areas where research suggested detailed exposure understanding – and external disclosure - remains limited

3. Spotlight needs to be shined on poorly understood risk exposures in financial services, given expectations of significant changing loss patterns

Insurable risk is not as high up the agenda of most mid-sized financial services management teams as are market risk, credit risk or regulatory compliance.

Many of those responsible for insurance consulted in this study profess to have limited understanding of exposures within key, potentially high-risk classes. In particular, respondents raised Professional Indemnity (PI), Directors & Officers (D&O) cover and cyber-liabilities (both the crime and business interruption aspects of online operations) as key areas of exposure concern. The most common, uncertain PI risks (e.g. around mis-selling, breach of investment mandates or unsuitable investment advice) were raised in half of all financial services sector buyer consultations.

"Liabilities around structured products will be one of the next big battlegrounds" (Director of Operations, Investment Management)

Topics of increased underwriter interest vary by sub-sector but signify a real step-change in concern. To take an example, among building societies, key priorities to address unease included explaining controls around valuation practices and arrears management in light of Treating Customers Fairly regulations set in place by the FSA. These changes represent a real and rapidly increasing risk; however, in most cases buyers have not yet addressed related disclosure.

"Clearly mis-selling will be big issue for a lot of companies, especially with regard to partner or third party products. I'm not certain what would happen in our case in the event of a PI claim" (Head of Risk Management, mid-size Asset Management)

In addition, a minority of FS buyers speculated that in addition to the initial recessionary impact on fraud claims, for example, there would also be a secondary round of claims emerge (a 'fraud double bubble'), caused by both latent discovery of previous fraud and the impact of shifting regulatory goalposts. Although some of the expected new losses described are already emerging as (often well publicised) claims, given the 'long-tail' nature of the insurance classes involved, there will likely be an extended lag before the full impact is known.

Overall, there is a wide range of different potential claim types where the more forthright respondents have suggested an increase in underlying risk. This is not just limited to the most high-profile media issues of mis-selling or mortgage fraud.

Risk of regulatory overload?

4. Regulatory burden being imposed on financial services firms unprecedented in its scope

Unsurprisingly, over half of all financial service respondents raised a major concern that the regulatory burden on their business (chiefly FSA compliance) had drastically increased during the past year, together with concern over potential retrospective application of rulings. This was particularly pronounced in the Building Society & financial advisory segments given the implications of such FSA initiatives as the Retail Distribution Review and Mortgage Market Review.

"We may have to pull out of certain business areas to in order to secure resource to be able to comply with regulations" (Operational Risk Manager, Financial Services)

Interestingly, a number of respondents went further in suggesting that operational risk management efforts are being hindered in the short term by the huge diversion of resources to comply with a sharply increased regulatory burden.

Regardless of how well-directed measures prove in the long term, if operational controls are hindered whilst adaptation is ongoing (and as companies wait for FSA direction), it is a reasonable hypothesis that immediate risk will actually increase.

Figure 9. Case Study Seven

Case Study Seven (Building Society Segment)

- Impact of bailouts and extensive and imminent further consolidation expected
- Ratings agency downgrades
- Significantly increased regulatory oversight impacting compliance activities with further future clarification expected: Retail Distribution Review, Mortgage Market Review, arrears management / Treating Customers Fairly etc.
- Walker report governance and risk management implications
- Severely restricted access to wholesale markets
- Marked increase in competition for retail deposits
- Already public fraud losses with significant expectation of further incidents to come to light – e.g. around mortgage valuation, solicitors and potential mis-selling
- Implications of Profit Participating Deferred Shares giving holders a share of future profits – akin to 'semi-demutualisation'

Source: Mactavish

Impact of changes on insurance risk

Across the sectors under investigation set out above, Mactavish research observes a wide array of significant strategic and operational changes being newly introduced, either as a direct response to perceived new challenges or as the trigger for previously considered measures to be brought forward and/ or amplified.

There are two critical overall conclusions Mactavish draws from this analysis:

- Significant material change is occurring to operating practices across all sectors, with the thrust of these shifts suggesting a higher level of underlying risk and a greater risk management challenge than during more benign economic times.
- This fact raises the disclosure burden on all parties in the insurance system, highlighting weaknesses in the traditional model and increasing the ultimate cost to companies of inadequate disclosure.

Insurance buyer response to change

Insurers have not yet been successful in driving any overall insurance rate hardening, and buyers continue to undervalue insurance as a capital tool

Market conditions remain favourable, fostering complacency and a low priority of insurance

Outside of a few isolated pockets of difficulty (e.g. credit insurance and some specialist PI), customer renewal experiences and expectations remain broadly flat, with a few encouraged by broker statements to expect further savings at next renewal. Likely as a result, this study has uncovered a relatively high level of buyer satisfaction with insurance suppliers (both incumbent insurers and brokers), very similar to the findings of Mactavish research in 2000/2001 before a significant change of heart by 2002/3 after market conditions shifted.

"Insurance doesn't keep me from going to sleep at night. I just don't think it's that important" (Financial Director, Financial Services, £50m-£100m)

More concerning is the tendency for comfort with favourable market conditions to have led to a de-prioritising of insurance risk across the senior corporate agenda. After an apparent upswing in Board interest following the cost increases of the last hard market, Board involvement appears in many cases to have reverted to a cursory cost approval role.

"Unless we can achieve a massive further reduction on our insurance premiums, I don't necessarily want to spend any more time focusing on insurance." (Financial Controller, Independent Manufacturing, £100m-£300m)

Insurance today remains viewed as, in effect, cheap capital by comparison with challenging debt and equity markets. However, it can be cogently argued that customers should view its importance in terms of the coverage limits provided, rather than premium spend at any given time. Focusing instead on cost alone suggests limited recognition of the role of insurance as contingent capital within the corporate finance mix, where the insurance industry overall has struggled to communicate its value.

65% of buyers do not review insurance submissions as de facto contract on which business relies

Companies' scrutiny of insurance submission materials remains deeply insufficient

Regardless of the mix of roles responsible for insurance, a surprisingly large majority (65% of corporate buyer respondents) have at most cursory involvement in preparing and reviewing insurance submission documents, despite it forming part of the legal contract against which any future claim would be assessed. Detailed submission verification remains the exception rather than the rule. The level of resource applied has not noticeably increased in response to the increased need represented by increased operational changes.

"The standards of presentation are worse than ever" (Senior PDBI underwriter)

Submission preparation remains for many companies a task largely conducted in relative isolation by the broker, typically working with much-reduced fees themselves and typically dedicating relatively little additional time investment to update and review such documents year to year.

"The quality of submissions is not improving... I am surprised that customers think their brokers know the risks well and present them properly." (Head of Casualty)

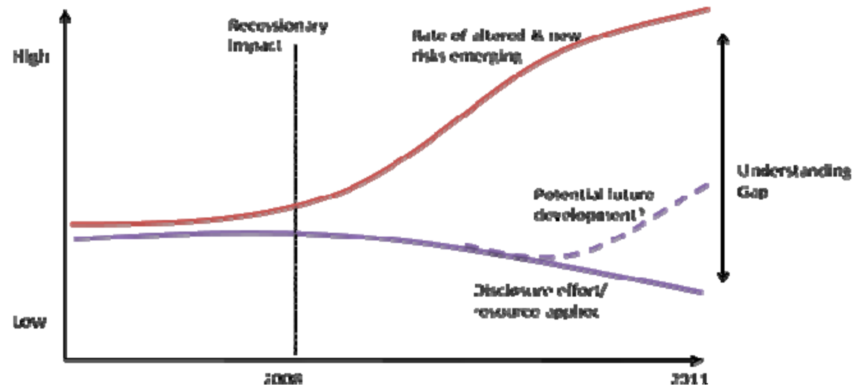
This supports the underwriter view below that submission information routinely lacks material detail to obtain reliable coverage at the best terms and price, and must increase the likelihood of material error of the sort that could render a high value claim questionable. This seems a reasonable point around which corporate shareholders might raise valid questions.

Even buyers who recognise this increasing gap feel powerless over how to address the risks created without better industry support

For the most part, even amongst those buyers recognising this concern, no remedial action on disclosure is yet being taken. Further, with insurance market conditions favourable and other operational and financial concerns typically more pressing, addressing such a thorny issue remains far from a high priority.

For almost every corporate respondent, the process of recognising the risk profile impacts and linking through to re-considering both internal risk management and external risk transfer requirements remains either early stage or non-existent.

Figure 10. Growing Risk Understanding Gap Is Clear



Source: Mactavish

Increase in cost and difficulty of raising new debt & equity increases firms' dependence on insurance

Despite current low priority, insurance is an increasingly important form of capital and neglecting disclosure carries significant risk

The UK legal framework around insurance disclosure remains, in the eyes of many legal commentators, weighted in favour of the insurer, in particular in relation to the duty and burden of required disclosure on customers.

"There is little doubt that the current arrangements for insurance law are often little understood, even by relatively informed buyers of insurance, resulting in unexpected, unfair and unjust outcomes – more so with some insurers than others" (Construction Industry Council)

Whilst overdue reform is possible in due course, its initial focus is on personal lines customers rather than corporate insurance, and thus imminent change is unlikely. The Law Commission's own consultation paper on the subject makes this point clearly, and draws upon corporate evidence (as example shown to the left) from its own research to suggest many companies are unaware of the requirements placed on them by law.

Buyers should also expect that in a rising loss environment and a hardening market cycle, insurer attitudes towards claims assessment are likely to strengthen.

Companies routinely underestimate risk of claim delay/ reduction/ repudiation based on limited or inaccurate disclosure

In addition, the Mactavish research programme also uncovered specific case evidence to suggest that disclosure detail adequacy, and the policy wording specifics that result from it, can be a key determinant of coverage and claims outcome for all high severity, low frequency risk classes.

Benign current insurance market conditions present buyers with a limited opportunity to prepare for more testing market conditions, and through better risk disclosure to limit their exposure to subsequent volatility of pricing and coverage availability. This opportunity should not be spurned.

Insurance supply response to change

Insurers recognise potential for increased loss costs and customer claim acrimony

Widespread recognition of importance of current risk alterations outlined above

Review of these findings with underwriting policy makers demonstrated strong agreement with the relevance of such change to key risks, and concern regarding both long-term loss pattern impact and uncertainty arising from disclosure gaps.

Figure 11. Underwriting Responses

Sample underwriting response to change issues set out

- *" The huge increase in the risk of suppliers going bust has had a massive impact on UK companies' risks" (Senior PDBI underwriter)*
- *" Manufacturing and retail risk has been drastically increased by the increasing complexity of supply chains" (Head of PDBI)*
- *" Retailers' product liability is changing dramatically... often because the manufacturer is in the Far East, subrogation is impossible." (Senior Product Manager)*
- *" We have had a lot more issues recently which come down to workmanship and standards" (Head of CAR)*
- *" Contractual liability just frightens me at the moment." (Head of CAR)*
- *" We have seen such a huge amount of notifications and pretty much paid claims coming out of the mortgage fraud area. It will clearly get worse before it gets better" (Senior Underwriter, Financial Institutions)*
- *" Information about new products or services should absolutely be in the broker presentation, but generally we do not get that level of detail. That is a problem." (Head of Casualty)*
- *" We just do not tend to get the level of details required to understand the BI element of supply chain risks." (Senior PDBI manager)*
- *" Supply chains are increasingly complex, and insurance arrangements are usually spread between different insurers which can significantly delay payments for the duration of negotiations... the lead insurer needs to build a strong case to be able to convince the co insurers to pay the claim" . (Senior PDBI underwriter)*

Source: Mactavish

"The standards of presentation are worse than ever... often the data provided is not checked... In particular, Business Interruption numbers are very rarely properly disclosed, which could become a massive issue for insurance buyers in a hardening market". (Head of Property Damage & Business Interruption)

As noted above, underwriters criticise the quality and detail of formal submission information, and the lack of ability to obtain additional detail from the broker. Concern lies in particular around low loss frequency classes where there is little indicative claims data.

There are also structural factors at work. Underwriting remains in large part driven by historic-looking actuarial models and a portfolio-based approach. Despite its sophistication, such an approach is not well-suited to dealing with rapid, discontinuous change — like that now being experienced across corporate Britain.

"The placing brokers are too busy to answer questions; they just go for the line of least resistance. Sometimes we literally get given the business description and the turnover and we are lucky if we get anything else." (Head of Casualty)

The insurance underwriting world also remains organised first and foremost around risk silos and areas of underwriting specialism, rather than around operational or sector-led expertise. Although efficient, another impact is to dilute sector knowledge and limit individual underwriter exposure to operational management.

These factors encourage awaiting claims-led evidence of change suspected as a result of piecemeal evidence, rather than enabling a more certain assessment of likely impacts before they emerge.

Structural realities within underwriting model slow response to emerging changes and encourage a volatile ultimate response

Inevitable underwriter assumptions & reactivity both drive volatility of outcome

In the absence of better information, this research suggests underwriting responses necessarily rely on often worst-case assumptions, the lack of information thus punishing better risk-managed companies

"When writing product liability risk (for retailers sourcing from the Far East), I will have to apply the (much higher) rating of a manufacturer to the whole retailer where I feel they might be exposed to some manufacturing liabilities". (Senior Casualty underwriter)

Secondly, the dominant theme of underwriting response to these findings was resignation to a lack of detail requiring them to wait for altered claims patterns to emerge before structuring a policy response. Again, this encourages a stronger response since insurers must seek to recoup incurred losses up to that point

The more severe and sudden is the emergence of new or altered losses, the more severe and broad is likely to be the rational underwriting response. Mactavish contends therefore that inaction on disclosure and limitations in the fundamental risk placement and underwriting model will both work to create a coming insurance 'hard market' far more uneven and frequently painful than would be achievable were the capacity and will sufficiently available across all parties to fundamentally re-communicate and re-assess changing corporate risk.

"There is just a lot of information about the insured that underwriters will never hear about until the claim comes through." (Head of Casualty)

Again, the last hard market is instructive here, as by far the most extreme volatility was created in the food sector where the simultaneous double-trigger effect emerged due to both a) constrained insurer capacity and market-wide rate increases and b) specific new exposure concerns around composite panelling insulation.

Addressing disclosure challenge as insurance key broker and insurer differentiator in 2010

Current limitations create real scope for provider differentiation

It seems likely that both brokers and insurers which take the lead in disclosure and addressing emerging risks with new product innovation will be placed in an ever more advantageous competitive position during 2010.

Despite resource limitations and continuing pressure on fees, Mactavish would expect brokers to differ significantly in their ability to both flag this challenge to buyers not currently feeling great insurance related pressure, and to help those buyers through the difficult challenge of gathering, structuring and disseminating better risk information before hard pressure emerges in earnest. Continuing to encourage a somewhat 'head in sand' approach for as long as the premium going remains good increases the likelihood of significant future dissatisfaction, increasing the risk of broker switching once the market turns.

Taking this lead in 2010 is also likely to best position insurers to better select individual clients and protect themselves against emerging risks whilst also taking maximum advantage of the eventual upturn in market rates when it arrives.

Summary of Conclusions

The findings above, for the sectors under investigation, set out a clear conclusion of a markedly increased rate of corporate change arising from recessionary pressures, and a firm conclusion that the net impact is to raise underlying risk. This arises from both increasingly complex and inter-connected industry value chains and the concurrence of operational change measures arising from the unprecedented difficult trading conditions.

In general terms, Mactavish's central observation is not a positive one: these changes have not yet been reflected in the assessment or communication of risk, putting coverage at risk. Few buyers review insurance submissions despite their significance, and the report reflects on a significant body of evidence which suggests that case-by-case risk disclosure standards are not improving to compensate for change, and in many cases are becoming less satisfactory.

Customer Implications

The total cost of risk to companies should drastically increase if action is not taken to reassess and communicate risks in light of the changes to the risk landscape. This should manifest itself through increased insurance spend, additional uninsured loss costs, and greater risk of claims disputes arising from material misunderstanding of risk & coverage.

- Significant combinations of strategic and operational change, both within individual companies and across multiple companies within a single supply chain, have introduced material new risks to earnings for many companies;

- Inadequate disclosure by buyers and their brokers is likely to mean that fewer of these new risks are properly insured, leaving shareholders carrying the risk of loss;

- Spurning the short-term opportunity to prepare whilst market conditions remain favourable creates avoidable volatility and should drive significantly increased cost of risk for all buyers in the long-term.

Insurer Implications

This research suggests that underwriters for the most part under the current system lack the detail necessary to proactively assess the impacts of new and shifting risk exposures. Mactavish thus draws three conclusions:

- Due to major current shifts in the risk landscape, the reliability of historically-focused rating models is far lower than in the recent past. Systemic under-pricing looks inevitable through 2010 as underlying risk increases and rates suffer continued downward pressure. This introduces a new risk to the earnings of property & casualty insurers over the coming years.

- Some parallels can be drawn between large property & casualty insurance institutions lacking the ability to fully understand changing risk exposures with past failures of financial institutions to understand risks assumed. While loss impacts naturally lag economic changes by several years, some turmoil in corporate insurance is to be expected as a latter phase of the financial crisis. Although diversified insurance organisations that have withstood the crisis thus far are unlikely to fail as a result, Mactavish expects significant changes to earnings patterns of those heavily exposed to business insurance risk to emerge until closer partnerships with their customer base can be constructed.

- Third, that once it finally arrives, a combination of the eventual hard market cycle together with significant changes to loss profiles already emerging suggests a potential 'perfect storm' of volatile corporate insurance market conditions over the next 2-3 years. Mactavish would expect this to be reflected in significant loss ratio deterioration, harsh subsequent pricing increases, capacity limitations and damaging sector coverage 'blackspot' areas as insurer understanding plays catch-up.

Ongoing research programme

This cross-sector paper is the first instalment of an ongoing programme of Mactavish research to be published during 2010. Subsequent pieces will analyse emerging individual sector issues more deeply, and revisit these cross-sector themes and associated underwriting policy later in the year to assess how both corporate experience and insurer policy play out. Following initial scoping interviews already completed, the study will also be extended into French and German markets in 2010.

Notes

Appendix A-1

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