November 13, 2023

Market Segment Outlook: New Zealand Non-Life Insurance

We are assigning a Stable outlook on the segment, based on expectations of solid premium growth, among other factors

AM Best is assigning a Stable outlook to New Zealand's non-life insurance segment. Key factors supporting the outlook include the following:

- Expectations of solid premium growth, owing to strong, ongoing rate improvement, particularly in the property and motor segments
- Resilient performance despite significant weather-related claims and high inflation
- A good buffer in risk-adjusted capital to absorb some volatility, supported by a strong regulatory framework

The following factors partly counter the positives:

- Increasingly volatile weather conditions, which continue to pose challenges to non-life insurers in New Zealand
- Reinsurance capacity tightening and reinsurance rate increases, which are expected to drive increased volatility in primary insurers' earnings

Solid Growth Prospect Despite Economic Slowdown

Gross written premiums (GWP) for New Zealand's non-life market have grown moderately in recent years, following stagnation during the COVID-19 pandemic. Non-life GWP increased by 6% in 2021 and 10% in 2022, according to data published by the Reserve Bank of New Zealand (RBNZ). The positive trend is expected to continue into 2024, due to record-high inflation and ongoing strong rate adjustments, particularly in the property and motor segments. A further boost to premium volume has come from the re-opening of New Zealand's borders, following the lifting of pandemic-related travel restrictions, which should help revive the tourism sector and boost the travel insurance market.

New Zealand's gross domestic product (GDP) growth rate slowed significantly to 2.7% in 2022, after growing 6.1% in 2021. The International Monetary Fund has projected a further slowdown in 2023 to 1.1%. However, the unemployment rate has remained low. Inflation, which hit 7.2% in 2022, has started to cool off and is projected to fall to 4.9% in 2023 and 2.7% in 2024. With inflationary pressures gradually easing, the non-life industry is expected to see GWP growth exceeding general inflation in the coming years, driven mostly by higher claims costs in recent periods and subsequent rate adjustments by primary insurers.

Resilient Performance Against a Backdrop of Significant Weather-Related Claims and High Inflation

New Zealand's non-life segment has a history of strong and stable technical performance, with the combined ratio ranging from the low to mid 90s from 2018 to 2022. Earnings in 2023 are expected to be materially impacted by significant weather-related claims, owing to January's Auckland Anniversary Weekend floods and February's Cyclone Gabrielle. These two events, considered New Zealand's most significant weather events of the century thus far, are expected

Analytical Contacts:
Yi Ding, Singapore
+65 6303 5021
Yi.Ding@ambest.com

Victoria Ohorodnyk, Singapore
+65 6303 5020
Victoria.Ohorodnyk@ambest.com

2023-146

to have a significant impact on the industry's bottom line in 2023. Combined insured losses are estimated at between NZD 3 billion (USD 1.8 billion) and NZD 4.2 billion, comprising both personal and commercial lines losses, according to the RBNZ.

Non-life insurers in New Zealand typically buy catastrophe excess-of-loss reinsurance with a coverage limit up to an expected 1-in-1000-year loss, which is materially higher than in other non-life markets globally. This is driven by New Zealand's regulatory capital requirements where insurers must have capital reserves or reinsurance protection sufficient for a 1-in-1000 event. As a result of the high utilisation of catastrophe reinsurance, reinsurers are likely to bear most of the claims costs arising from the flooding and cyclone events during the first quarter of 2023. However, net retention costs plus reinstatement premiums have typically exceeded normal profits for property insurers in New Zealand thus far in 2023. Following these major events, reinsurance rate increases could dampen primary insurers' earnings in the coming years. The need to have a high level of reinsurance coverage exposes primary insurers to elevated reinsurance pricing risk, particularly given the general reduction in capacity for property aggregate and event frequency covers in the global reinsurance market.

In light of the ongoing pressures of claims inflation, weather-related losses, and reinsurance pricing, non-life insurers are expected to implement significant premium rate increases to offset the impact. In addition, they are likely to place more focus on risk differentiation and risk-based pricing for policies with exposures to catastrophe events. As they adjust their premium rates, insurers with the ability to price at a more granular level are likely to have competitive advantages.

Furthermore, rising interest rates will have a positive impact on insurers' investment returns, with a beneficial impact on overall earnings.

Increasingly Volatile Weather Conditions

In recent years, increasingly volatile weather conditions (including storms, flooding, cyclones, and hailstorms) have posed challenges to the segment's profitability. The annual cost of extreme weather events has risen steadily over the past five years. Data released by the Insurance Council of New Zealand (ICNZ) showed that extreme, climate-related weather claims hit a record high of NZD 351.2 million in 2022. This figure ballooned to NZD 3.6 billion in the first nine months of 2023, driven by the flood and cyclone events.

Non-life insurers' technical performance is highly correlated with the occurrence of large weather and catastrophe events—for example, the 2023 weather events and the Canterbury earthquakes in 2010/2011, which resulted in an accumulated loss of almost NZD 23 billion. The increased likelihood of extreme, large catastrophe events could expose the non-life insurers' earnings to elevated volatility.

To alleviate the pressure on the private sector and maintain affordability of insurance cover for consumers, government participation is expected to grow. Currently, the support for earthquake risk is provided by Toka Tu Ake EQC, a government-owned organisation that provides insurance cover for the first NZD 300,000 of losses on residential properties in 2023 (NZD 150,000 in 2022) for each earthquake event. Discussions about a similar national scheme for other natural perils (such as flood) are ongoing. The increased climate risk has also led to government intervention in catastrophe-exposed locations, including the recent initiative to offer a buyout of 700 properties that fall under the risk category where weather event risk cannot be sufficiently mitigated.

Good Buffer in Risk-Adjusted Capital to Absorb Some Volatility

The capital adequacy of New Zealand's non-life market remains robust. Whilst the recent weather-related events have affected insurers' earnings, their financial stability is not materially impacted owing to the comprehensive reinsurance coverages in place. The risk-adjusted capitalisation of New Zealand's non-life insurers provides them with a buffer to absorb some volatility in earnings. This is typically supported by conservative investment strategies and robust reinsurance programmes, placed with good credit-quality partners.

Non-life insurers' capital adequacy is subject to uncertainty, as major weather events could have a delayed impact on subsequent reinsurance renewals. Given the limited scope to reduce the coverage limits of insurers' catastrophe excess-of-loss reinsurance, the continued cession of material losses to reinsurers may result in further upward pressure on reinsurance rates and a tightening of terms and conditions, which could lead to insurers retaining more risk on their balance sheets. Insurance companies affiliated with larger business groups may be in a stronger position to contend with future events, as additional capital can be downstreamed from parents if required.

The New Zealand IFRS 17 and Interim Solvency Standard 2023 became effective on 1 January 2023. The interim standard, which will be in force for around three years, is designed to streamline solvency calculations and facilitate sound solvency management in line with the implementation of NZ IFRS 17. The capital solvency of non-life insurers in New Zealand is not expected to change materially following implementation of the Interim Solvency Standard, as non-life insurers typically take a conservative capital management approach and hold buffers above the minimum regulatory requirement.

Major Regulatory Changes to Strengthen the Framework for Insurers

Regulatory changes are expected to remain a key focus for non-life insurers in New Zealand. There are a number of ongoing and upcoming regulatory developments, including the Conduct of Financial Institutions (CoFI) regime and a review of the Insurance Prudential (Supervision) Act (IPSA), which will likely have an impact on insurers.

CoFI is expected to commence in March 2025, with licensing starting in July 2023. It introduces a new regulatory regime to ensure that registered banks, licensed insurers, and licensed non-bank deposit takers comply with the fair conduct principle when providing relevant services to consumers. As part of the conduct and culture review of the past five years, internal reviews of conduct and governance have been a top priority for non-life insurers in New Zealand, and insurers have identified potential issues and responded with remedial actions. Non-life insurers are therefore in a better position to comply with the new licensing requirements, given the work that has been completed to date.

RBNZ continues to review the IPSA, with an omnibus consultation that was published in September 2023. This review is being undertaken to ensure that the legislation is appropriate to support the more proactive and intensive approach to supervision. Non-life insurers in New Zealand are expected to review their practices against these proposals and implement any changes they identify.

GUIDE TO BEST'S MARKET SEGMENT OUTLOOKS

Our market segment outlooks examine the impact of current trends on companies operating in particular segments of the insurance industry over the next 12 months. Typical factors we would consider include current and forecast economic conditions; the regulatory environment and potential changes; emerging product developments; and competitive issues that could impact the success of these companies.

A Best's Market Segment Outlook can be Positive, Negative, or Stable.

Best's Market Segment Outlook	
Positive	A Positive market segment outlook indicates that AM Best expects market trends to have a positive influence on companies operating in the market over the next 12 months. However, a Positive outlook for a particular market segment does not mean that the outlook for all the companies operating in that market segment will be Positive.
Negative	A Negative market segment outlook indicates that AM Best expects market trends to have a negative influence on companies operating in the market over the next 12 months. However, a Negative outlook for a particular market segment does not mean that the outlook for all the companies operating in that market segment will be Negative.
Stable	A Stable market segment outlook indicates that AM Best expects market trends to have a neutral influence on companies operating in that market segment over the next 12 months.

We update our market segment outlooks annually but may revisit them at any time during the year if regulatory, financial, or market conditions warrant.

Published by AM Best

BEST'S MARKET SEGMENT REPORT

A.M. Best Company, Inc.
Oldwick, NJ
CHAIRMAN, PRESIDENT & CEO **Arthur Snyder III**
SENIOR VICE PRESIDENT & TREASURER **Cynthia Young**
SENIOR VICE PRESIDENTS **Lee McDonald, Thomas J. Plummer**

A.M. Best Rating Services, Inc.
Oldwick, NJ
PRESIDENT & CEO **Matthew C. Mosher**
EXECUTIVE VICE PRESIDENT & COO **James Gillard**
EXECUTIVE VICE PRESIDENT & CSO **Andrea Keenan**
SENIOR MANAGING DIRECTORS **Edward H. Easop, Stefan W. Holzberger, James F. Snee**

AMERICAS
WORLD HEADQUARTERS
A.M. Best Company, Inc.
A.M. Best Rating Services, Inc.
1 Ambest Road, Oldwick, NJ 08858
Phone: +1 908 439 2200

MEXICO CITY
A.M. Best América Latina, S.A. de C.V.
Av. Paseo de la Reforma 412, Piso 23,
Col. Juárez, Alcadía Cuauhtémoc, C.P. 06600, México, D.F.
Phone: +52 55 1102 2720

EUROPE, MIDDLE EAST & AFRICA (EMEA)
LONDON
A.M. Best Europe - Information Services Ltd.
A.M. Best Europe - Rating Services Ltd.
12 Arthur Street, 8th Floor, London, UK EC4R 9AB
Phone: +44 20 7626 6264

AMSTERDAM
A.M. Best (EU) Rating Services B.V.
NoMA House, Gustav Mahlerlaan 1212, 1081 LA Amsterdam, Netherlands
Phone: +31 20 308 5420

DUBAI*
A.M. Best - MENA, South & Central Asia*
Office 102, Tower 2, Currency House, DIFC
P.O. Box 506617, Dubai, UAE
Phone: +971 4375 2780
*Regulated by the DFSA as a Representative Office

ASIA-PACIFIC
HONG KONG
A.M. Best Asia-Pacific Ltd
Unit 4004 Central Plaza, 18 Harbour Road, Wanchai, Hong Kong
Phone: +852 2827 3400

SINGAPORE
A.M. Best Asia-Pacific (Singapore) Pte. Ltd
6 Battery Road, #39-04, Singapore
Phone: +65 6303 5000

Best's Financial Strength Rating (FSR): an independent opinion of an insurer's financial strength and ability to meet its ongoing insurance policy and contract obligations. An FSR is not assigned to specific insurance policies or contracts.

Best's Issuer Credit Rating (ICR): an independent opinion of an entity's ability to meet its ongoing financial obligations and can be issued on either a long- or short-term basis.

Best's Issue Credit Rating (IR): an independent opinion of credit quality assigned to issues that gauges the ability to meet the terms of the obligation and can be issued on a long- or short-term basis (obligations with original maturities generally less than one year).

Best's National Scale Rating (NSR): a relative measure of creditworthiness in a specific local jurisdiction that is issued on a long-term basis and derived exclusively by mapping the NSR from a corresponding global ICR using a transition chart.

Rating Disclosure: Use and Limitations

A Best's Credit Rating (BCR) is a forward-looking independent and objective opinion regarding an insurer's, issuer's or financial obligation's relative creditworthiness. The opinion represents a comprehensive analysis consisting of a quantitative and qualitative evaluation of balance sheet strength, operating performance, business profile, and enterprise risk management or, where appropriate, the specific nature and details of a security. Because a BCR is a forward-looking opinion as of the date it is released, it cannot be considered as a fact or guarantee of future credit quality and therefore cannot be described as accurate or inaccurate. A BCR is a relative measure of risk that implies credit quality and is assigned using a scale with a defined population of categories and notches. Entities or obligations assigned the same BCR symbol developed using the same scale, should not be viewed as completely identical in terms of credit quality. Alternatively, they are alike in category (or notches within a category), but given there is a prescribed progression of categories (and notches) used in assigning the ratings of a much larger population of entities or obligations, the categories (notches) cannot mirror the precise subtleties of risk that are inherent within similarly rated entities or obligations. While a BCR reflects the opinion of A.M. Best Rating Services, Inc. (AM Best) of relative creditworthiness, it is not an indicator or predictor of defined impairment or default probability with respect to any specific insurer, issuer or financial obligation. A BCR is not investment advice, nor should it be construed as a consulting or advisory service, as such; it is not intended to be utilized as a recommendation to purchase, hold or terminate any insurance policy, contract, security or any other financial obligation, nor does it address the suitability of any particular policy or contract for a specific purpose or purchaser. Users of a BCR should not rely on it in making any investment decision; however, if used, the BCR must be considered as only one factor. Users must make their own evaluation of each investment decision. A BCR opinion is provided on an "as is" basis without any expressed or implied warranty. In addition, a BCR may be changed, suspended or withdrawn at any time for any reason at the sole discretion of AM Best.

Version 041423