

Business Interruption Insurance Impact of Global Downturn

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Introduction

Key questions have arisen due to current economic conditions:

- Impact on premiums and coverage
- Increase need to address supplier risk
- Insurers reluctant to expand cover and actual quietly reducing cover
- Claims – still occurring but are they being paid
- Insurable industries and countries
- CFO's attitude to BI cover and alternative approaches

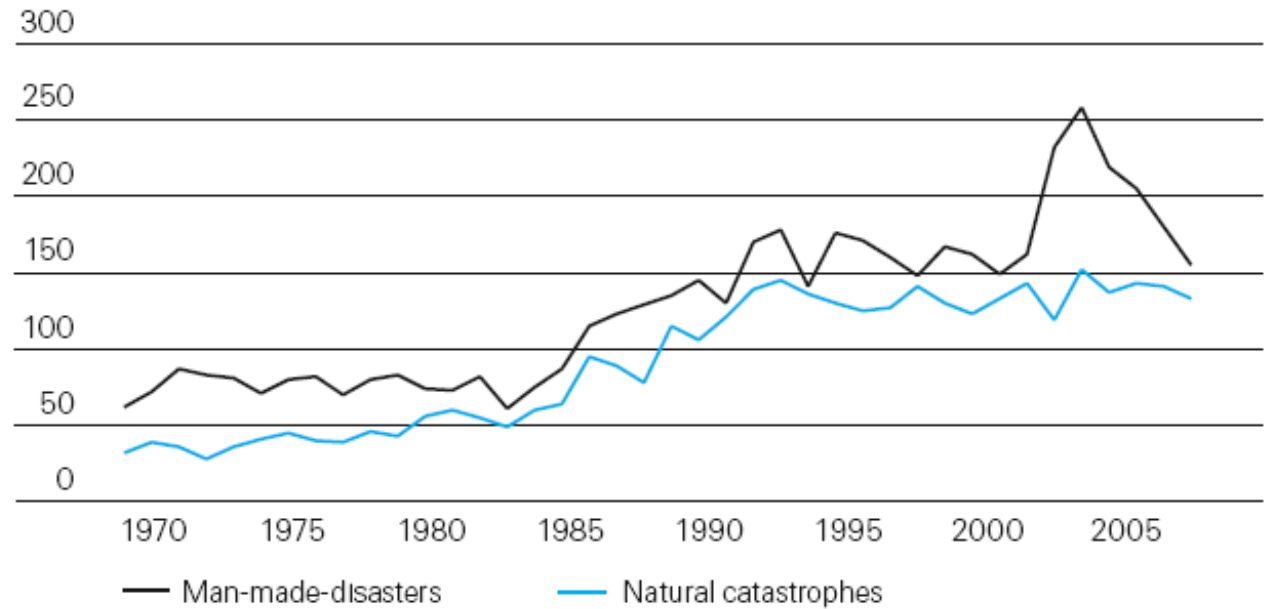
Business Interruption is a high ranking business risk

TABLE 1 2005–2009 TOP 20 RISK CONCERNS

RANK	2005/06	2006/07	2007/08	2008/09	CHANGE FROM 2007/08
1	Corporate governance	Corporate governance	Brand and image	Brand and image	–
2	Systems	Systems	Systems	Corporate governance	↑ 1
3	Brand and image	Human resource	Corporate governance	Systems	↓ 1
4	Human resource	Brand and image	Human resource	Human resource	–
5	Legal	Legal	Information management	Legal	↑ 2
6	Liquidity	Information management	Business interruption	Information management	↓ 1
7	Information management	Lack of innovation	Legal	Liquidity	↑ 6
8	Business interruption	Business interruption	Lack of innovation	Market environment	↑ 1
9	Capital structure	Impact of regulation	Market environment	Business interruption	↓ 3
10	Lack of innovation	Market environment	Impact of regulation	Intellectual property	↑ 6
11	Computer crime	Computer crime	Physical assets	Capital structure	↑ 4
12	Intellectual property	Physical assets	Liability	Impact of regulation	↓ 2
13	Liability	Capital structure	Liquidity	Physical assets	↓ 2
14	Physical assets	Liability	Computer crime	Lack of innovation	↓ 6
15	Market structure	Intellectual property	Capital structure	Liability	↓ 3
16	Impact of regulation	Liquidity	Intellectual property	Computer crime	↓ 2
17	Internal fraud	Internal fraud	Natural disasters/climate change	Natural disasters/climate change	–
18	Market risk/treasury	Credit	Market risk/treasury	Market risk/treasury	–
19	Credit	Market risk/treasury	Environmental	Credit	↑ 4
20	Environmental	Environmental	Internal fraud	Environmental	↓ 1

Business Interruption Losses in 2009

Figure 1
Number of events 1970–2009



Source: Swiss Re, sigma catastrophe database

Business Interruption Losses in 2009

Table 2
Catastrophes in 2009 by regions

Region	Number		Victims		Insured loss (In USD m)	
		in %		in %		in %
North America	54	18.8%	543	3.7%	12 655	48.2%
Europe	32	11.1%	874	5.9%	7 697	29.3%
Asia	125	43.4%	9 386	62.9%	2 436	9.3%
South America	13	4.5%	547	3.7%	50	0.2%
Oceania/Australia	7	2.4%	706	4.7%	1 297	4.9%
Africa	26	9.0%	932	6.2%	180	0.7%
Seas/Space	31	10.8%	1 928	12.9%	1 955	7.4%
World total	288	100.0%	14 916	100.0%	26 270	100.0%

Source: Swiss Re, sigma catastrophe database

Business Interruption Losses in 2009

Table 8

The 20 most costly insurance losses in 2009

Insured loss⁷

(In USD m)	Victims ⁸	Date (start)	Event	Country
3 372	25	24.01.2009	Winter storm Klaus, winds up to 170 km/h, heavy rain	France, Spain
1 350	15	10.02.2009	Thunderstorms, winds up to 145 km/h, hail	US
1 193	11	23.07.2009	Hail storm Wolfgang, winds up to 130 km/h	Switzerland, Austria, Poland et al
1 130	2	09.04.2009	Tornadoes, storms, winds up to 105 km/h, hail	US
1 079	173	07.02.2009	Victorian bush fires, winds up to 100 km/h	Australia
1 050	1	10.06.2009	Thunderstorms, winds up to 128 km/h	US
995	6	25.03.2009	Thunderstorms with hail	US
800	–	20.07.2009	Storms, heavy rain, hail	US
760	2	26.05.2009	Hail storm Felix, winds up to 90 km/h	France, Germany, Belgium
615	5	08.10.2009	Typhoon Melor/No 18, winds up to 204 km/h	Japan
570	–	07.05.2009	Storms, thunderstorms, winds up to 145 km/h; floods	US
569	–	01.04.2009	Losses to crops due to drought	Canada
565	23	26.01.2009	Winter storm, snow, ice, power outages	US
502	296	06.04.2009	Earthquake (M _w 6.3), aftershocks	Italy
500	–	05.06.2009	Storms, hail, heavy rain; floods	US
430	37	07.09.2009	Flash floods after heavy rain	Turkey
422	1	01.08.2009	Hail, storm, winds up to 100 km/h	Canada
400	854	26.09.2009	Typhoon Ketsana/No 16, winds up to 160 km/h; floods	Philippines, Vietnam, Cambodia et al
ns ⁹	–	08.06.2009	Collision between vessel and platform	Atlantic Ocean, North Sea
ns ⁹	–	21.08.2009	Leakage of gas, oil at oil field; explosion on drilling platform	Indian Ocean, Timor Sea

Source: Swiss Re, sigma catastrophe database

Contingent Man-made Losses – East Java continues



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REUTERS



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Contingent Man-made Losses – East Java continues



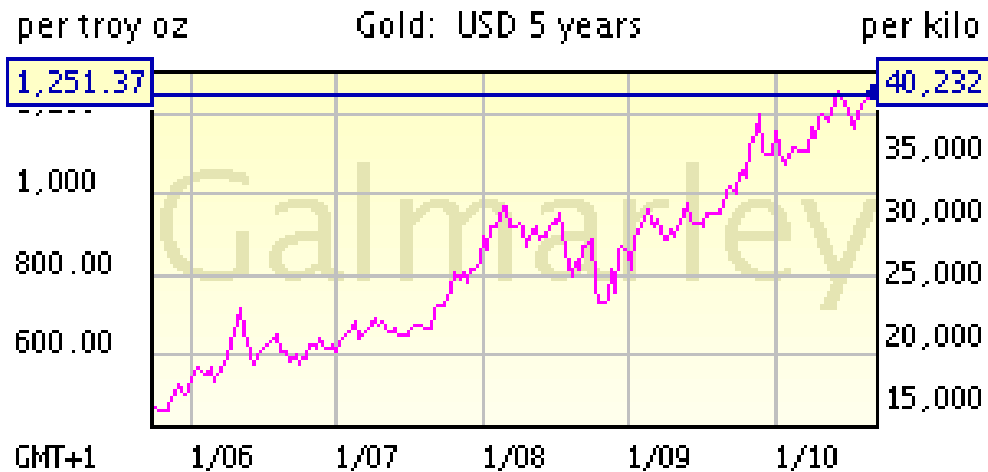
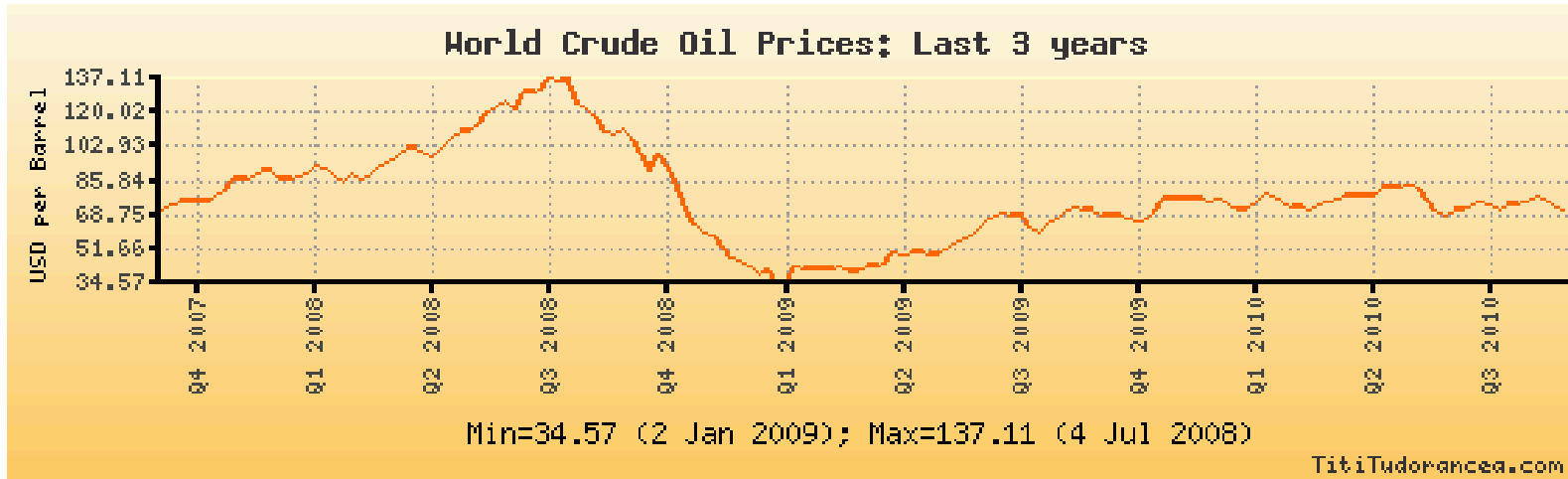
Contingent Man-made Losses – Deepwater BP



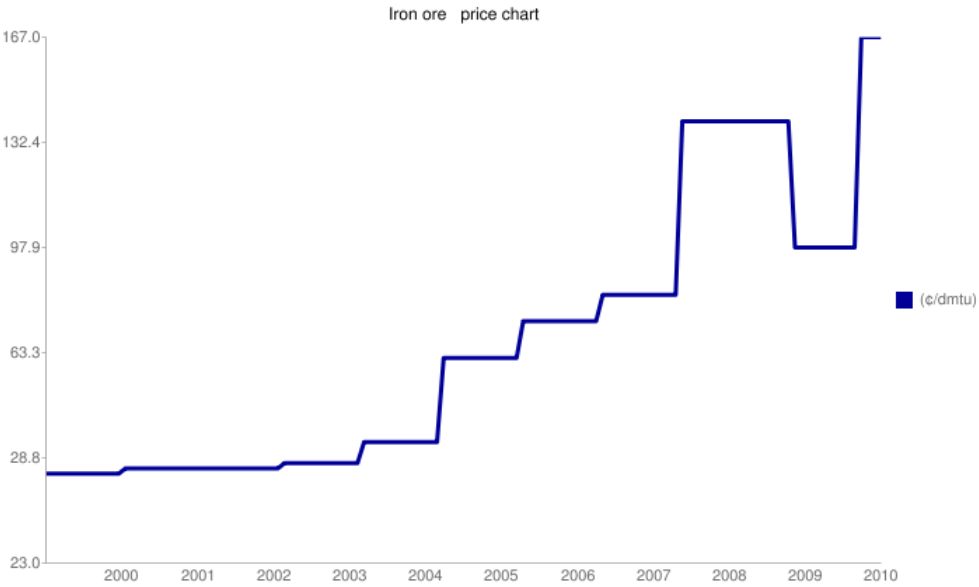
Overview of GLC

- Downturn in Finance, Retail, Mining, manufacturing and Construction
- Unemployment increased
- Change in ratio of part timers and consultants
- Reduced supplier base – insolvencies
- Lack of Investment confidence
- Write down of Insurer investments – gap in net assets

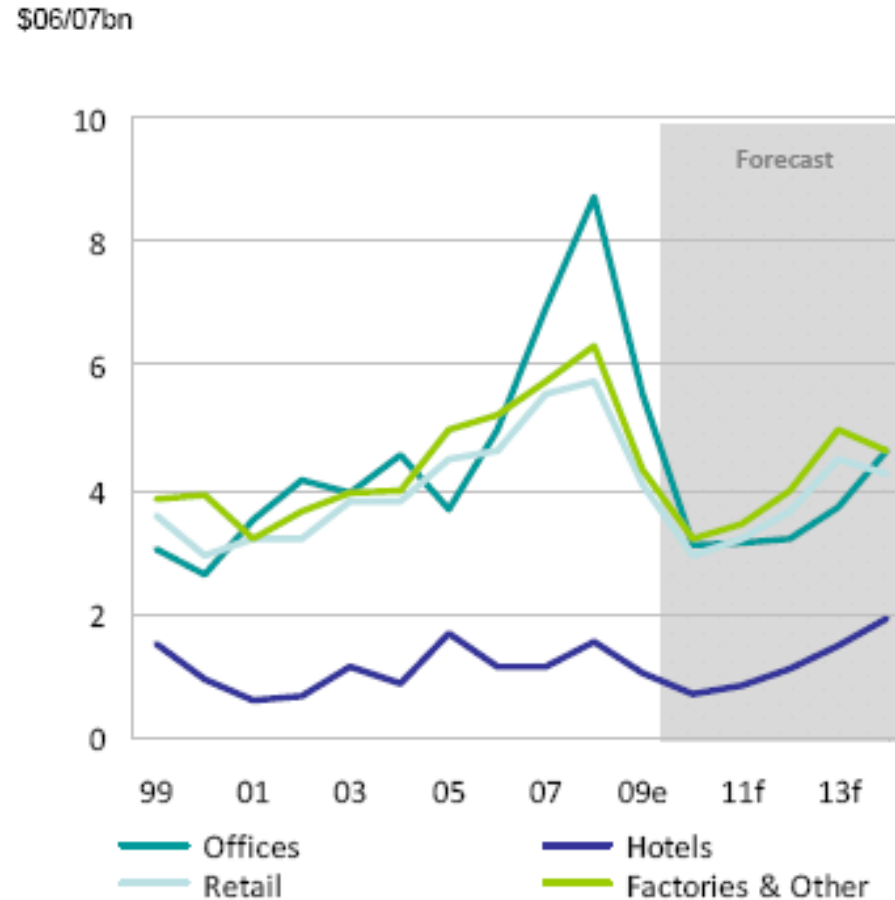
Commodity Trends



Commodity Trends (continued)



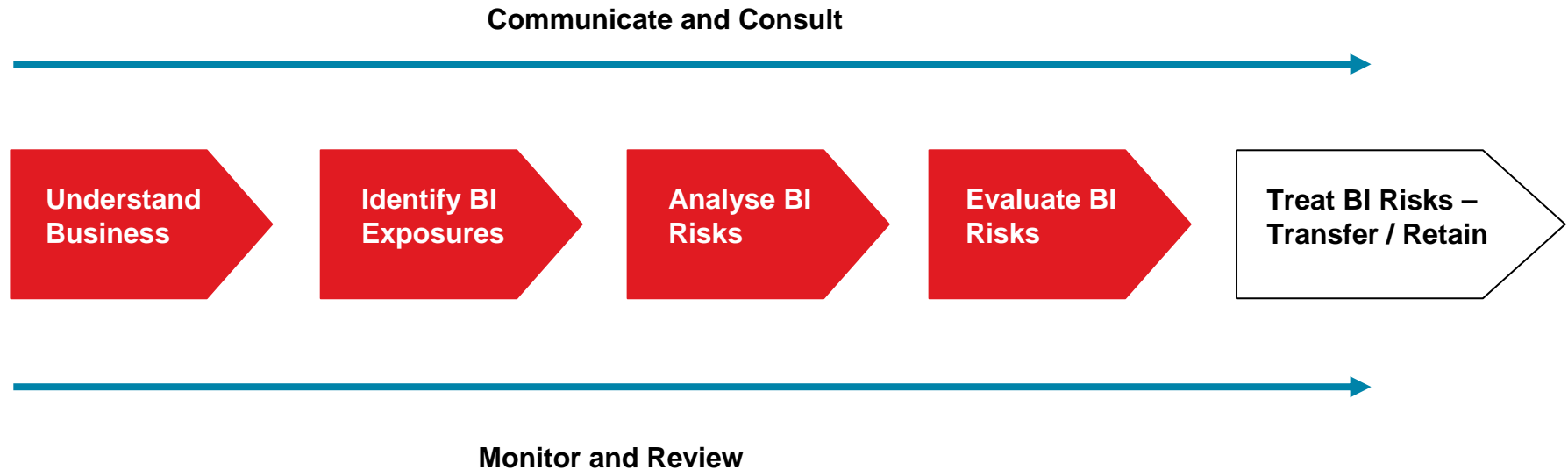
GLC Impact on Commercial and Industrial Property



Source: BIS Shrapnel, Value of Commencements, Building in Australia July 2009. Year end June

BI Approach Flowchart to Events and GLC

BI Risk Management Process



The 4 Pillars of Business Interruption Insurance

- **Pre Loss**

1. Policy Declared Value and Sub Limits
2. Policy Structure
3. Policy Wording

- **Post Loss**

4. Claims Management

Impact on Business Interruption Insurance

Pillar 1 – Declared Values and Sub Limits

▪ **Gross Profit and Revenue**

- Declining revenues
- Longer recovery periods
- Insurers reducing cover by capping of commodity prices (oil and gold especially)
- CFOs wanting reduced insurance costs hence transferring risk back to the balance sheet

▪ **Payroll**

- Change in payroll structure
- More casuals and part timers
- Bigger employment pools
- Reduced pay increases

Impact on Business Interruption Insurance

Pillar 1 – Declared Values and Sub Limits (continued)

- **Sub Limits** (such as Supplier & Customer)
 - Underestimate the values
 - Insurers want quantification before providing cover
 - Deepwater and East Java show contingent losses are sizeable and have a long tail
 - GLC has created greater reliance on reduced suppliers
 - Insurers will restrict limits
 - Unspecified minimal limit
 - Specified needs quantification
 - Single suppliers uninsurable
 - Lack of nexus between ERM work on supplier chain management and insurance limits
 - Insurers have single policy deductibles so does cover exist

Impact on Business Interruption Insurance

Pillar 2 – Policy Wording

- Overall Insurers are reducing risk transfer by limiting cover through wording changes)
- Examples of Policy wording changes:
 1. Supplier & Customer
 - No unspecified suppliers
 - No more the supplier of a supplier (or customer)
 - Suppliers limited to country of insured
 2. Prevention of Access
 - Excluded an insured peril – e.g. flood or storm
 - Limited the coverage to approximately 1km
 - Selected insured locations
 3. Utility
 - The wording “in the network” is disappearing hence, no domino effect

Impact on Business Interruption Insurance

Pillar 2 – Policy Wording (continued)

4. Contagious diseases

- Elimination of the clause (more SARS/Asia than GLC)
- “In the vicinity” words are now replaced by set kilometres

5. Accumulated Stocks

- Elimination of the clause (mining use stocks to mitigate)
- Limited to finished goods so WIP now an uninsured risk
- Promotes the wrong behaviour and conflicts with the underlying duty of care

■ Case Studies

- Racecourse – track became an excluded asset with no discussion
- Soda Ash Manufacturer – domino effect on loss of supply of electricity

Impact on Business Interruption Insurance

Pillar 3 – Policy Structure

- Insurers raising retention levels at renewal
- Introducing one policy deductible which impacts sub limit cover
- No different period of indemnity for type of cover
- No Gross Profit cover on DSUs – only Holding Costs

Impact on Business Interruption Insurance

Pillar 4 – Post Loss Issues

- Insurers pressure to low claims provisions
- Reduce Claims costs (Loss Adjusters, Accountants and Lawyers)
- Slow in making payments – retain cash
- Wording issues are more the focus than quantification
- Trends – GLC is to blame for everything
- China example:
 - 3yrs pre loss growth exceeding 10%
 - Loss in 2009
 - Insurer predicts loss due to GLC
 - Growth after loss period Claw Back
 - Many extra costs to prove assertions wrong

Impact on Business Interruption Insurance

Summary

- GLC has created increased risk transfer to Insured's Balance Sheet
- Subtle and growing changes by Insurers
- Whilst risk insured takes on more risk costs the trade off of reducing insurance costs is not happening
- Word of warning and review your:
 - Declared Values
 - Policy Wording
 - Policy Structure

Questions?