

Note: *This document was prepared by Grant, Jones & Stuart Insurance as a service to their clients on June 3, 2005.*

The Insurance Marketplace

Many consumers are mystified, frustrated and genuinely put off by the entire process of purchasing Insurance. This is understandable given that Insurance represents a payout of cash on a regular basis for an intangible promise to pay for an event which may or may not occur in the future. To top it off, we are usually forced to buy it, either by the government in the case of automobile Insurance, or by the banks in the case of loans/mortgages. Most of us would rather spend the money on something a little more exciting.

Given the above it makes it even more frustrating for consumers when prices fluctuate as wildly as they have over the last two decades. All types of Insurance have seen significant instability in pricing, while it always seems that the media is declaring that our business is making 'obscene' profit. Here are some of the underlying causes of price instability, which incidentally apply to other types of business than Insurance:

1. Government intervention: Automobile Insurance in particular is heavily regulated, and governments have been known to force in rate reductions without providing any statistical justification for these reductions. In provinces with either private or public automobile Insurance, auto rates have become election issues which can result in some poorly thought out rate changes.

In addition, regulations can change the entire basis of claims payments. This has occurred in Ontario Automobile Insurance 4 times over the last 15 years as government and Insurers tried to figure out a fair scheme that would not cost consumers too much money. Each time a change occurs, it takes years to find out if it really worked and in some cases losses were far higher than expected.

2. Investment markets: Insurance Companies rely heavily on investment income. In some years, this has been the only source of their profit. When interest rates and/or the stock markets decline, it can have a significant impact on profitability and the only place to recover is through increasing rates. It is important to note that if an Insurance company loses money, it can be devastating to them as it affects the amount of business they can write in the future. All Insurance Companies must abide by a formula that the amount of premium written must be backed up by a certain amount of capital. Losses will drain that capital and force an Insurance Company to 'shrink' leading to cancelled broker contracts and serious dislocation of business. Worse still, an insolvent Insurer can have serious consequences for anyone who holds a policy with them.

3. Competition: You need only look in the yellow pages or watch TV commercials to see that there is thriving competition in our business. Competition usually results in better rates for consumers, but it can have consequences that may not be foreseen. Intense competition can drive rates so low that Insurers will simply turn their backs on certain types of coverage or withdraw from the market entirely because there is no longer an opportunity for reasonable profit. Don't forget that those who provide the capital for these companies are expecting a reasonable return for their money.

For a real test of the fairness of your rates, check to see what you were paying 10 or 15 years ago for your car coverage, and then adjust the price for inflation over those years. If you have maintained a clear driving record or have had no claims on your property coverage, you should find that overall, there has been more stability than you thought.

Hopefully, this will be of assistance in understanding the way the marketplace works (or doesn't work in some cases). The key thing to remember when shopping for your insurance is to get a bit of background on the company you are looking at placing your business with. What is their track record, are they profitable, stable and do they reward loyalty if you keep your coverage with them. How long have they been in business and how have they fared on claims satisfaction surveys. This last item is one of the most important, since that is the time when you really need your company to be there for you.

As always, feel free to contact us if you have any questions about the above.

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