Opportunities amid uncertainty

Guy Carpenter's Gina Carlson and Richard Hewitt highlight why the industry is in a strong position to face current headwinds as 1 January approaches

The reinsurance industry is built on a commercial relationship between risk and capital. In the current, palpably dynamic environment, the industry appears to have reached an inflection point.

A reassessment of not only the relationship but also of the opportunities risk and capital afford is under way. Countervailing forces are influencing the industry. Drivers of uncertainty, including macroeconomic and other relevant trends, have led to severely stressed market conditions. On the other hand, drivers of confidence – including resilient industry capital, disciplined underwriting and a firming commercial lines rate cycle – are injecting positivity into the sector.

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This past year, inflation has rightly been an area of significant focus and uncertainty for the industry, as evidenced by rising levels of consumer price indices across most regions. However, the industry's long history of data utilisation alongside advancements in technology and modelling methods puts insurers in a strong position to forecast, monitor and measure risk in a changing environment. Insurers are successfully addressing inflation's impact by adjusting exposures and updating procurement practices, increasing insurance rates and monitoring loss cost trends more frequently.

Globally, central banks have rapidly raised interest rates among other policy steps in an effort to bring inflation back within targeted levels. Yet, while this response has contributed to financial market volatility and a repricing of their assets, (re)insurers' ratings and solvency positions have proven to be robust and they are well placed to reap the benefit of higher reinvestment yields in future years' earnings. Higher interest rates are also slowing economic growth prospects for 2022 and 2023. Fortunately, the sector is considered "late-cycle", meaning its growth prospects are less influenced by short-term economic cycles. In fact, economic volatility can be expected to reduce risk appetite among insureds and spur the demand for modified and innovative product offerings.

These macroeconomic forces are coupled with all the other significant, relevant issues faced by the industry, inter alia, rising catastrophe losses, climate change, cyber threats, the Russia-Ukraine conflict and for some participants, the adequacy of returns. Forged together, these have caused a re-evaluation of risk appetites by some market participants, which has been accompanied by a fall in dedicated reinsurance industry capital, particularly for retrocessional capacity. Guy Carpenter and AM Best estimate that year-end 2022 total dedicated reinsurance capital will be 7 percent lower, with traditional capital down 8 percent and alternative capital up 1 percent. However, these mixed results create the foundation for a positive cyclical market turn.

Now is the time to invest in the sector. By understanding how macroeconomic conditions, geographic footprints and lines of business come together in specific portfolios and impact risk tolerances, Guy Carpenter can deliver bespoke solutions for today as well as address emerging challenges of tomorrow. Collectively, the reinsurance sector, through detailed and thoughtful analysis and execution, can once more prove resilient and prosper in this ever-changing risk landscape.

Gina Carlson, Senior Vice President Business Intelligence, Guy Carpenter
Richard Hewitt, Head of Business Intelligence, EMEA, Guy Carpenter