

For information
on 16 January 2003

Legislative Council Panel on Financial Affairs

Meeting on 16 January 2003

**Business environment of the Hong Kong
insurance industry and the difficulties encountered by
some professional and business sectors in obtaining insurance coverage**

Introduction

This paper sets out the present business environment of both the worldwide and Hong Kong general insurance markets as well as the Administration's response to the matters raised by the Honourable Bernard Chan regarding the difficulties encountered by some professional and business sectors in obtaining insurance coverage.

Business Environment

Worldwide General Insurance Market

2. In the international scene, the last two years have been very stressful for the general insurance industry, particularly the reinsurance industry. Insurance capacity has contracted due to a combination of weak investment returns, keen competition among insurers and unprecedented losses. In 2001, worldwide general capital funds in the insurance industry decreased by about US\$90 billion. The contraction for 2002 was projected to be approximately the same amount if the current state of stock markets continues. This would mean some US\$180 billion, or 25%, decrease in global capital funds of the

general insurance industry since early 2000. The about US\$30 billion new capital infused after the 911 events has not been enough to make up for the decrease. Apart from a shrinking in capital fund, the 911 events in the United States (US) in 2001 had caused an estimated US\$50 – 70 billion loss to general insurers worldwide.

3. As a result, insurers worldwide have raised their premium rates, particularly in commercial lines and reinsurance business. Moreover, they have become more conservative in underwriting risks. The hardening of the international insurance market is projected to continue in 2003, given the global shortage of quality capital for the insurance sector and increased risk exposures after the 911 events.

Hong Kong Insurance Market

4. Hong Kong has one of the most open insurance markets in the world. As at 30 November 2002, there were 197 insurers authorized to carry on insurance business in Hong Kong. Among these, 150 were authorized to carry on general insurance business. The Hong Kong general insurance industry, similar to that in many other countries, has been hit by the sluggish economy, shrinkage of investment returns and keen competition. The overall underwriting loss of general insurers amounted to HK\$1,379 million, HK\$872 million and HK\$473 million in 1999, 2000 and 2001 respectively. For the first nine months of 2002, the general insurance industry recorded an underwriting profit of HK\$604 million.

EC Insurance Business

5. As at 30 November 2002, there were 73 authorized insurers writing

Employees' Compensation (EC) insurance business in Hong Kong. In the past few years, EC insurance business had experienced continuous and significant underwriting losses. The underwriting loss for this statutory line of business was HK\$1,370 million in 1999, HK\$1,091 million in 2000, HK\$1,039 million in 2001 and HK\$315 million for the first nine months in 2002. Such losses are attributable to inadequate premium rate, an intensely competitive and fragmented EC insurance market, and substantial increase in common law damages and statutory benefits.

6. In the light of the significant underwriting losses and in response to the suggestion of the industry, in December 2000 the Office of the Commissioner of Insurance (OCI) conducted an industry-wide survey to gauge the performance of EC insurance business in two areas, i.e. construction and non-construction businesses. The survey revealed that for construction EC business, the underwriting result deteriorated by 487% from a loss of HK\$98 million in 1996 to a loss of HK\$576 million in 1999. Over this 4-year period, the number of claims reported increased by 20%. The average amount paid per claim increased by 91% and the amount of the largest claim settled increased by 90% (up to HK\$14 million in 1999). On the other hand, the average premium rate dropped by 28% in the same period.

7. As for non-construction EC business, the underwriting result deteriorated by 1,673% from a loss of HK\$42 million in 1996 to a loss of HK\$740 million in 1999. Over the period, the number of claims reported increased by 37%, the average amount paid per claim increased by 19% and the amount of the largest claim settled increased by 40% (up to HK\$21 million in 1999). On the other hand, the average premium rate dropped by 22% in the same period.

8. The results of the OCI's survey show that during the relevant period while the claims had risen substantially, both in terms of number and amount, the premium rate had on the contrary dropped by 28% and 22% in respect of construction and non-construction EC business respectively. This underlines how competitive the market had been.

9. With the amount of losses and against the background of developments in the global market highlighted above, Hong Kong EC insurers raised the premium. For the first nine months of 2002, EC insurance business recorded an increase of 33% in gross premium. Moreover, many insurers had stepped up their risk management in underwriting EC insurance policies, for example, requiring the wage roll of employers to be certified and to have more regard to the safety measures at the work place in setting the premium. These measures have improved the underwriting performance of this line of business with the underwriting loss reduced from HK\$421 million for the first 9 months of 2001 to HK\$315 million for the same period in 2002.

Motor Insurance Business

10. As at 30 November 2002, there were 68 authorized insurers writing motor insurance business in Hong Kong. Motor insurers in Hong Kong had also suffered heavy underwriting losses in recent years: HK\$166 million in 1999, HK\$407 million in 2000 and HK\$108 million in 2001. The main reasons for such losses are inadequate premium rate and increase in compensation. From 1996 to 2001, the average premium per vehicle had fluctuated between \$5,067 and \$5,797. Relevant statistics are at Annex.

Market Outlook

11. Despite the losses incurred by the general insurers in the statutory lines of business, they are compensated by profits in other profitable business, and other pre-financing arrangements such as new capital injection. Moreover, the Insurance Authority imposes stringent solvency and asset requirements for general insurers. The overall insurance industry is financially sound.

Difficulties in obtaining insurance coverage

12. The Hong Kong insurance industry is not immune to problems faced by the global market, including the tight reinsurance capacity available. In addition, the increasing amount of court award for personal injury has increased the operating costs of insurers. In light of the difficult business environment, particular in the case of general insurance, insurers have increased premium rates and tightened underwriting measures.

13. The hardening of the general insurance market has drawn a number of complaints from the insuring public, mainly motorists and employers of specific sectors. For EC insurance, the complaints are mostly related to smaller companies in the construction, engineering and diving sectors. For motor insurance, they are mostly related to motor cycles, public light buses (PLB) and taxis. In the past two years, the OCI received a total of 24 such complaints. In some cases, the complainants faced genuine difficulties in obtaining insurance coverage. In other cases, the issue was related more to the level of premium rates. With the assistance of the relevant Government department and the insurers, all complaints had been resolved.

14. As mentioned in paragraphs 2 to 4 above, given the global development,

the current business environment and the losses in the past, insurance premium would remain high. This is not inconsistent with the worldwide trend. Insurance business is a risk-assessing and pricing business. Hong Kong has an open insurance market and there is no barrier for new qualified companies to enter the market. We believe that the level of premium rates should be best left to market forces. In line with the practice in other jurisdictions with a well-developed insurance market (UK, Australia and Singapore), OCI does not interfere with premium setting by insurers. OCI is debarred under section 26(3A) of the Insurance Companies Ordinance from intervening into the premium setting by insurers.

15. For persons facing genuine difficulties in obtaining insurance coverage, they may seek the assistance of brokers, who are specialists in finding the appropriate insurance for their clients. In this regard, the OCI has been in close liaison with the two broker associations and has drawn up a list of brokers for public inspection. Moreover, a list of brokers who may help employers in securing EC insurance is now available at the Labour Department. In the longer term, the Administration will explore the feasibility of encouraging employers from a specific sector to purchase EC insurance on a collective basis.

16. The Administration will continue to ensure that insurers operate in a business-friendly environment and on a level-playing field. We will also work closely with relevant stakeholders to promote road and occupational safety, which would ultimately help to lower the premium rates for motor and EC insurance policies.

Financial Services and the Treasury Bureau/OCI

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Motor Insurance Market

	Total gross premium (\$ <i>billion</i>)	Underwriting performance (\$ <i>million</i>)	No. of vehicle covered	Average premium per vehicle (\$)
1996	2.69	(82.7)	496 266	5 426
1997	2.81	(346.3)	484 922	5 797
1998	2.78	(383.9)	489 393	5 674
1999	2.35	(176.3)	456 006	5 144
2000	2.47	(324.9)	448 368	5 508
2001	2.77	(121.0)	546 072	5 067
2002 (<i>Jan-Sept</i>)*	2.23	(80.4)	N/A	N/A

*: Provisional figures.