News Comment:

Taiwan Nonlife Insurers Can Absorb Earnings Hit From Recent Earthquake

April 8, 2024

Taiwan Ratings Corp. said today that it expects Taiwan's nonlife insurance sector to face manageable final costs from a major earthquake that struck the island's east coast on the morning of April 3, 2024.

In our view, Taiwan insurers have generally adequate reinsurance protection against their property catastrophe risk, given that Taiwan is in an earthquake-prone zone. We believe that such reinsurance protection significantly reduces the impact of major events on the sector's net combined ratio. For example, reinsurance coverage helped the sector to record a net combined ratio of 101.2% and gross combined ratio of 115.1% in 1999, when a major 7.6-magnitude earthquake inflicted severe damage throughout Taiwan. Similarly, the sector recorded a net combined ratio of 100.8% compared with a gross combined ratio of 106.6% in 2001, when Typhoon Nari brought significant property losses to the island.

Local nonlife insurers maintain a largely stable appetite for fire and natural event property risk retention, which should further limit their final costs from the recent earthquake. Moreover, Taiwan has a moderate level of penetration for earthquake insurance coverage among citizens, covering around 38% of the island's residential property as of Jan. 31, 2024. Therefore, we forecast the sector's net insured loss to represent a manageable fraction of the overall costs of the earthquake to Taiwan.

However, the challenges Taiwan nonlife insurers face in order to maintain their capital buffers are more complicated now than they were 25 years ago. The industry is exposed to more claim risks under wider insurance coverage; reinsurance costs have risen following previous catastrophe events; and potential losses on commercial property and business interruption coverage are higher today than decades ago due to the rise in coverage to industrial and technology companies.

At the same time, some insurers face reduced flexibility to utilize their contingency and catastrophe loss reserves to offset the earnings impact of new catastrophe events. That's because they have already used these reserves to offset COVID insurance losses in 2022. We estimate the ratio of these reserves to total available capital ranges from 4% to 19% as of Dec. 31, 2023. Insurers with lower ratios were more severely affected by COVID losses.

We continue to assume that Taiwan's nonlife insurers can maintain their current capitalization if the net combined ratio deviates by 5-10 percentage points from our base case assumption of 95% for the sector in 2024. The reinsurance claim-settling process following catastrophe events usually takes a long period to finalize losses, and it is too early to conclude
the actual claim losses facing the sector. Some insurers with a thinner capital buffer could face some difficulty managing their capital stability; however, we believe that most nonlife insurers have a sufficient capital buffer to manage the potential final losses from the recent earthquake. Moreover, most insurers benefit from financial support from their parent groups to ensure their long and short-term credit stability.

The report does not constitute a rating action.
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