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Insurance: 2014 property insurance market outlook: Prop. owners expect to see premiums flatten in 2014

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Just like any other industry, the property insurance market works in a cycle: Prices rise; referred to as a "hard market," and prices fall; referred to as a "soft market." Unlike other industry though, the property insurance cycle is very hard to forecast due to a few factors which will be discussed in this report.

What is a hard market and what is a soft market?

Here are a few factors that signal when we are in a hard market:

* Insurance premiums rising;
* Insurance companies writing less policies;
* Stricter underwriting guidelines.

Here are some factors that signal when we are in a soft market:

* Insurance premiums decrease;
* Insurance companies writing more policies;
* Easing of underwriting guidelines.

What drives the market to harden or soften?

It works in the following cycle (see figure):

Increase in losses: An increase in losses, usually caused by a catastrophic disaster, which then takes the industry to

Decreased reserves: Reserve is the money insurance companies are required to put aside for losses. When losses are up, the reserve goes down. This leads to

Higher premium: In order get their reserves back to a positive, insurance companies raise their premiums.

Stricter underwriting/less competition: In order to stop bleeding and reduce claims, insurance companies tighten their underwriting criteria, and write less policies. This means there is less competition; thus less options for property owners. As in any other industry, when competition is low, prices go even higher.

Decrease in losses: After being very selective on the types of risks the insurance companies write, and handpicking only the better stuff, losses decrease.

Increase reserve: When losses are down, reserves are up.

Lower premium: Once the reserve is back into the positive side, the insurance companies start lowering premiums.

Easier underwriting/more competition: With a decrease in losses and lower premiums, underwriting criteria loosens up too, and insurers underwrite more policies, which increases competition and then leads to even lower prices.

And then the cycle starts all over again!

Where are we now?

A typical insurance cycle usually takes between 2 and 10 years. It's not hard to tell that we are currently somewhere in the hard market: Building owners have seen their premiums rise and underwriting being stringent since Hurricane Sandy. But where exactly in the hard market are we now?

We are currently at the lower right corner of the cycle. We are in-between stricter underwriting/less competition and Decrease in losses.

What we can expect for 2014

In 2011 we started seeing the market hardening. Hurricane Sandy at the end of 2012 made it worse all the way into 2013. The good news is that property owners can expect to see premiums to flatten in 2014. The 2013 hurricane seasons was the softest in more than 30 years and it was generally a good year for insurers compared to 2012. This obviously put their reserves in a more stable position. Barring any unforeseen turbulence in the financial industry, property owners should expect to see a flattening in premiums in 2014.

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