The Legal Protection Insurance Market in Europe

October 2013

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In its latest publication RIAD, the International Association of Legal Protection Insurance, updates its key data on the European legal protection insurance market. This brochure summarises the most important information and provides a brief overview of the latest developments and trends.

The data covers the years 2002-to-2011. Data is extracted from the INSURANCE EUROPE statistics, EUROSTAT, and national publications of the countries' supervisors or insurance associations.

The countries included in the report are: Austria, Belgium, Bulgaria, Croatia, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Italy, Latvia, Luxembourg, Malta, the Netherlands, Poland, Portugal, Slovenia, Slovakia, Spain, Switzerland, Turkey and the United Kingdom. Sweden is not included due to lack of data.

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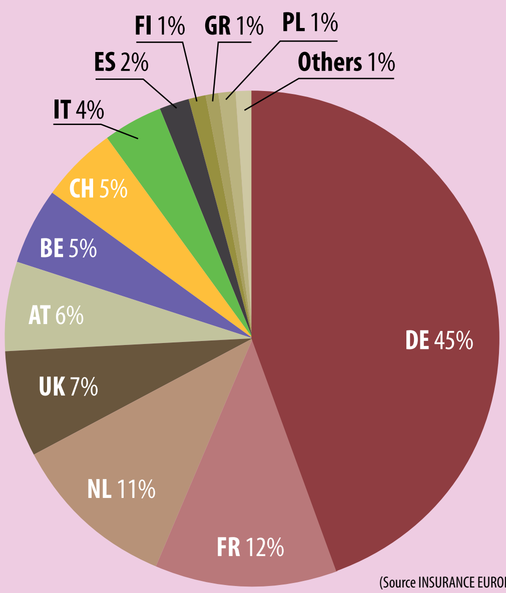
1 Premium Income and Market Shares

The distribution of total premium income for 2011 (€7,432m) by country confirms the predominance of the German market which accounts for 45% of the European total. This high market share relates not only to the size of the market but also to a high penetration rate of the legal protection insurance in Germany. The two biggest subsequent markets are France and the Netherlands, which account for, respectively, 12% and 11% of the European legal protection market. The remaining markets account for less than 10% of the European market (United Kingdom[1] - 7%, Austria - 6%, Belgium - 5% and Switzerland 5%). Since 2008, the Dutch market has overtaken the United Kingdom which was previously the third biggest market. This evolution reflects the sharp slowdown in the premium income of the United Kingdom over the last few years.[2]

All other markets account for 5% or less of the European market. Combined, the four leading markets (Germany, France, the Netherlands and the United Kingdom) account for 75% of the European market. ■

Breakdown of legal protection premium income per country in 2011



(Source INSURANCE EUROPE)

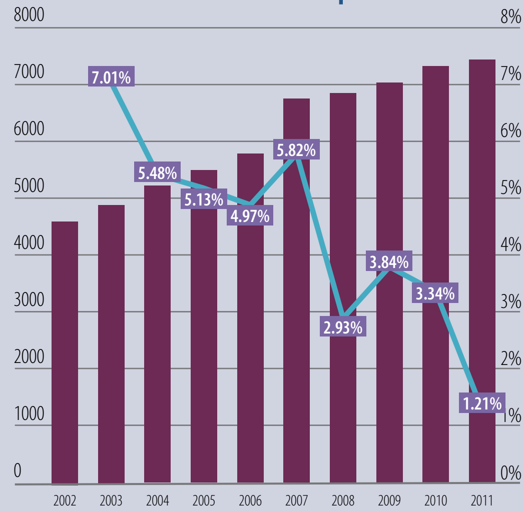
[1] Please note that the market share of the United Kingdom is slightly underestimated as the data does not include the Lloyds market which accounts for approximately 20% of the UK legal protection insurance market.

[2] As indicated further on, the slowdown observed in the UK is likely to be related to the increase of the business written offshore.

2 Growth Rates of Premium Income

In 2011, the legal protection insurance market amounted to €7,432m compared to €7,319m in 2010. This represents growth (at constant exchange rates) of 1.2% which is well below the average growth rate of 5.5% observed over the last decade and below the 3.3% increase recorded in 2010.

Premium income in legal protection insurance in Europe



(Source INSURANCE EUROPE)

The slowdown recorded since 2008 can be partly explained by the severe economic crisis that affected European business and that decreased demand for almost all types of non-life insurance cover. This is particularly true for legal protection insurance, in particular cover for businesses, which tends to reflect the evolution of general economic activity. However, the serious falloff in the premium growth rate observed in 2011 is rather new compared to the growth rate above 3% recorded in 2009 and 2010 and primarily finds its explanation in a decrease of the premium income observed in some large EU markets like the United Kingdom and Spain that recorded respectively a decline of -15.3% and -28.2% in 2011. The drop observed in the UK in 2010 and 2011 does not seem to reflect a decrease in the market size of this country but rather an increase of the business which is written offshore in Guernsey, Gibraltar or in Continental Europe. Therefore, at the aggregate level it is likely that the drop recorded in the UK is partly compensated by some rise in other EU countries. However, a part of the slowdown observed in the UK might also partly be related to the austerity program of the British government which started in 2011.[3]

[3] According to some estimates made by some of RIAD members, it is likely that the UK market has grown in 2011 by approximately 5%. However, given the lack of precise figures and the fact that some of this increase is reported in data of other countries, we have not been able to amend the data accordingly.

In 2011, only 6 countries out of 23 recorded a higher growth rate than in 2010 while they were twice as much in 2010. It can therefore be concluded that the slowdown in the evolution of the aggregate premium income is not the result of a few countries but a general trend observed in most countries.[4] In 2010 only three countries recorded a decrease in the premium income compared to 2009, they are six in 2011. The size of these drops are also stronger than those recorded in 2010 with negative growth rates reaching -29.2% in Poland, - 28.2% in Spain or -15.3% in the United Kingdom. The highest growth rates were recorded in Estonia, Turkey, Denmark, Luxembourg and Czech Republic which all recorded growth rates close to or above 10%. These double digit growth rates are explained by the fact that the legal protection insurance market in some of those countries is less developed and still in a catch-up phase following the economic growth for some of these countries. In the specific case of Luxembourg, the evolution of the legal protection market reflects also the influence of the increase in contract sold outside of the country. ■

3 Share of Legal Protection Insurance in Non-Life Premium Income

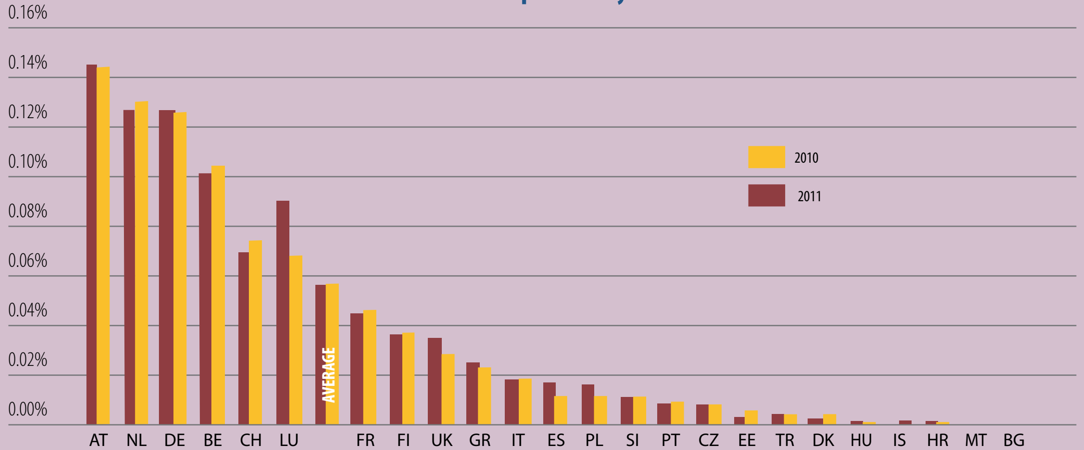
Legal protection insurance represents only a small fraction of the total non-life insurance market, accounting for less than 2% of the total non-life insurance premium income and has varied between 1.5% and 1.8% during the period 2002-2011.

Between 2002 and 2010, this share has constantly increased, reaching its highest level in 2010 at 1.79%. For the first time over the last decade, the ratio has slightly decreased to 1.76%, reflecting a higher growth rate in the total non-life market (3%) than in the legal protection market. ■

4 Penetration Rate of Legal Protection Insurance

The ratio of legal protection insurance premium income to GDP (at market price), also known as the penetration rate, does not represent the contribution of the legal protection branch to GDP but is an indicator of the relative importance of legal protection insurance. On average, in 2011, the legal protection premiums represented 0.058% of the GDP compared to 0.059% in 2009 which is the highest level recorded over the last ten years. The strong increase in the ratio observed in 2009 does not reflect a strong increase in the legal protection insurance premium but is rather an indicator of the economic recession observed in Europe (the EU 27 GDP (at market prices) decreased by 5.4% in 2009). However, in 2010 and 2011, the EU GDP grew at a faster rate (respectively 4.8% and 2.9% at market price) than the legal protection premiums income (3.3% and 1.2% respectively) explaining the slight drop in the ratio. The data per country show very different levels of legal protection insurance development in Europe. The highest levels are recorded in the most advanced economies, specifically in Austria, Germany, the Netherlands, Belgium, Luxembourg and Switzerland. Lower levels are mainly found in Eastern countries (Croatia, Bulgaria, Estonia, Hungary, and Turkey). Very low levels are also observed in more developed markets such as Denmark, Malta or Island. ■

Penetration rate per country in 2010 and 2011



(Source INSURANCE EUROPE)

Note: Denmark is underrepresented due to partial data

[4] It should be underlined that the freedom for companies to sell insurance services across the border in Europe does not always allow a perfect comparison of the national markets. As the business written off in a country A might be recorded in the accounts of a company that report in a country B, national evolution of the legal expense business are not always easy to analyse and interpret.

5 Legal Protection Insurance and Service Provision

Legal protection insurance not only gives the policyholder the possibility of being reimbursed for lawyer fees and other costs related to litigations but they have broadened their service offering by extending their activities to related services such as the provision of legal advice by lawyers employed by the insurance company or by external lawyers. The legal protection insurer may also support the client with out-of-court settlements or directly represent the policyholder in courts or administrative proceedings. However, since all these external services are strictly regulated by national law the range of services provided by insurers in the different countries varies substantially. Generally, legal advice and the settlement of claims out-of-court can be provided without legal restriction while in most countries the representation of the policyholder in courts and/or administrative proceeding is forbidden or submitted to legal restrictions which vary from country-to-country. Restrictions are strongest in Germany where legal protection insurers are only allowed to pay claims and are not entitled to give any legal advice, settle claims out-of-court, or represent clients in court or administrative proceedings. The provision of legal advice by insurers is also forbidden in Poland. ■

6 Legal Protection Insurance and the Financial Crisis

Legal protection insurance is a long-tail business that requires legal protection insurers to invest massively in assets in order to cover their commitments to policyholders. Insurers generally invest in assets with well defined cash flows and risk profiles and largely limit the risk profile of their investments in line with their commitments to policyholders.

In 2011 the total investments of insurers amounted to more than €7,700bn invested in company shares, bonds and other assets. In general, insurance companies report a fairly diversified sovereign bond portfolio across EEA countries, Japan, Switzerland and the United States. The largest part of the portfolio is invested in bonds, i.e. 41% in debt securities and other fixed-income securities (Source INSURANCE EUROPE - Key Facts).

Along the year 2012 and especially in the first semester, legal protection insurers as well as all other institutional investors have had to work in a very difficult economic environment but actions taken by both policy makers and monetary authorities, mainly in the second part of 2012, have gradually reduced tail risks and relieved market stress.

Generally, yield of most safe assets were particularly low and very often below the inflation interest rate reducing return on investment for insurers and making it more difficult for insurers to cover their commitment to policyholders. Interest rates may have a huge impact on long-term lines of business where investment income is a major source of earnings. However, the interest rate risk inherent to long-tail lines of non-life business such as the legal protection insurance can be dealt with by prudent management of assets and liabilities, although long-tail business remains vulnerable to unexpected increases in claim inflation.

With regard to the liquidity risk, it should be noted that, in contrast to other financial services providers, insurers are characterised by the inversion of their cost/revenue cycles. This means that insurers are primarily funded by policyholders' premiums, making them less exposed to liquidity risk and to any problems accessing credit markets.

However, in the context of the recessionary pressure in a number of economies in the EU combined with the rising unemployment, a prolonged period of subdued growth could have negative effects on insurance demand in particular regarding those that may be considered by customers as less essential. This impact could be further amplified by the slowdown in growth in other world regions thereby affecting insurers by a lower global demand and by their subsidiaries abroad.

The negative rating outlooks generated by the low-yield environment, on the one hand, and sovereign risk in Europe, on the other, are making capital raising an increasingly expensive option for the insurance sector. Many insurers are therefore paying increasing attention to earnings retention, also with a view to the potentially higher future capital needs that will result from the forthcoming introduction of the risk-based requirements of the Solvency II framework.[5] ■

[5] ECB Financial Stability Review

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