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War Risks and Insurance Premiums: How War Affects the Insurance Industry (Part 3)

In part 2 of our running series on War Risks and Insurance Premiums, NIACE shared the different types of war insurance products and the profile of buyers who purchase these policies. In the final part of this series, we will be taking a closer look at how the shipping industry is affected by conflict and subsequently higher risk premiums. Additionally, we will examine how the industry works around increased risk premiums and the impact on end consumers.

Geopolitical Instability and War Ship Insurance

Starting in October 2023, the attacks by Yemen's Houthis on cargo vessels in the Red Sea and Suez Canal have led some insurers to cease coverage for ships passing through this crucial shipping lane. In response, some shipping companies have decided to take the longer route around South Africa, increasing both insurance and overall shipping costs in the process. Insurers that continue to provide coverage vessels using the Red Sea route will likely impose substantial war risk premiums, further raising freight expenses. Although premiums are set to increase regardless of the route taken, the Economist Intelligence Unit (EIU) does not anticipate a significant rise in marine insurance claims, as traditional claims for hull, cargo, and fire risks remain predominant.

Additionally, the ongoing Israel-Hamas conflict has intensified risks for maritime trade, propelling insurers to adopt stricter underwriting practices. The Joint War Committee (JWC) has expanded the high-risk zone in the Red Sea, contributing to higher premiums to maintain favourable claim loss ratios. War risk premiums for the Red Sea have jumped from 0.07% in October 2023 to nearly 0.5% to 0.7% by the end of December. For Israeli shipowners, particularly harsh reality has seen reports of premiums surging as much as ten times. Meanwhile, premiums for the Black Sea are reported between 2.5% and 3%.

To avoid attacks, several major shipping companies are rerouting their cargo ships around the Cape of Good Hope, adding up to 15 days in transit times and increasing insurance costs. These rising premiums are further intensified by global inflation, which has already seen a year-on-year surge in hull and cargo insurance rates by 8% in 2022. Despite these elevated war risks, the overall impact on insurance claims is projected to be limited. Historically, war-related claims account for a fraction of the total marine insurance claims, with cargo, hull, and fire risks being the primary contributors. In fact, claims levels have remained stable in recent years, with a report indicating that 2023 marked the first year since 2019 with a single claim amount exceeding $30 million.

Rising Premiums and the Impact on Consumers

In light of recent geopolitical developments resulting in the surge in demand for specialised war insurance products, higher premiums and revised coverage terms for marine insurance products are widely expected to take place in the next year. Some risks currently excluded from standard hull insurance might be reconsidered if the threat level remains high. Initiatives like the program launched by Marsh, Lloyd's of London insurers, and Ukrainian state banks aim to alleviate damage claim costs for ships in the Black Sea. Shipping companies in Israel are also seeking government assistance to address escalating war insurance expenses amid ongoing conflicts.

In response to escalating conflicts in the Red Sea, UK-based insurance broker Howden in April 2024 announced that the company has begun offering war risk cargo insurance for vessels traveling through the Red Sea to insure against drone and missile attacks amid rising geopolitical tensions. The cost of insuring a seven-day voyage in the Red Sea has surged significantly (hundreds of thousands of dollars) since Yemeni Houthi rebels began attacking ships in November, to show solidarity with Palestinians in Gaza.

On April 13, Iran's Revolutionary Guards seized a container ship in the strait, just days after Tehran vowed to retaliate for a suspected Israeli strike on its consulate in Damascus on April 1. This poses an increasing threat on the global shipping industry in the Strait of Hormuz. Additionally, Iran has indicated it may close this vital shipping route outright which could see insurance for the shipping industry surge even more.

With increased pressure on the shipping industry's profit margins, continued geopolitical instability could force the shipping industry as a whole to pass on the surging costs to consumers as shipping companies continue to grapple with high shipping insurance premiums. This, coupled with persistent economic uncertainty, could have an adverse effect on the global economy which will only lead to further inflation with the end consumers ultimately paying the price for conflicts globally. Additionally, persistently high shipping costs could hamper aid and recovery efforts as aid for the victims of conflict needs to be shipped right into the heart of conflict zones which in and of itself entails higher risks which in turn pushes insurance premiums even higher. Consequently, this starts a downward spiralling loop which will only worsen if global conflicts are not resolved in due time.

Having understood the reliance of the shipping industry on specialised war insurance products, NIACE hopes that readers have gained a deeper understanding of war insurance products and the inner workings of the insurance industry. Recognising the importance of adaptability, the management of NIACE is currently monitoring developments within the industry, constantly keeping an eye out for and actively managing the company's risk so that our clients can continue to have peace of mind.

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