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For the Spanish insurance market 1981 results in the automobile field were much better than those of previous years. Nevertheless, some difficulties have arisen with regard to market growth, which is not expected to be higher than 18%, although it is necessary to bear in mind that the inflation rate has not exceeded 15%.

In other fields, the situation continues as I have described in previous reports. The insurance bill is at Parliament, and it seems that some 700 amendments have been submitted to the commission. It appears improbable, though, that the basic contents of the bill will be altered, but it is possible that when approved, it will be too "weak" to meet the real needs of the market, with many companies under the solvency safe margin.

Due to reasons unrelated to the insurance market, discussion of the bill in the Parliament has been delayed, but it may be approved during this year and start in force at the beginning of 1983. If, for any reason, the bill is not passed by Parliament, it will be evident that the insurers opposing it (for reasons that I don't begin to understand) have performed a very unfavorable service to the country.

It has been said (and was recently made public by the head of the Insurance Department of the Ministry of Finance) that more than 70 companies are in a situation of insolvency and that, should the liquidation of many of them become necessary, it might affect substantially the interest of the insureds.

What is the reason for the precarious situation of these insurance companies? It usually is said that the number of insurance companies is too large, but this statement is more illusory than true. There are many little companies operating in very limited fields, like the health insurance services, which are not necessarily those in the most difficult situation.

The problem affects mainly those insurance companies that have operated very irresponsibly in automobile insurance, profiting from the laxity of the requirements they have to fulfill with regard to the payment of losses. In addition, every time results improve slightly, as they have now, they start a campaign of "captation" of new businesses, paying very high commissions that necessarily produce losses, although the "prudent" insurers derive a profit from the same situation.

The main reason for this lies in the lack of an external audit of insurance companies. This negligence enables the companies to offer annual reports without confirmation of their authenticity. Some companies, including those outside the insurance sector, have been known to show profits, even sizable profits, when they were practically bankrupt. It is clear that Spanish insurance needs to be concentrated. There is no need for an excessive number of companies, although the difficulties come mainly from the 100 companies that effectively operate competitively. But much more than a problem of concentration, it is a problem of fulfillment of the legal requirements and of the apparent weakness of the insurance department to ask for it. It is also fair to point out that the department lacks the means to take care of a market that is becoming quite important; in addition to visiting companies and handling the administrative functions of the department, a mere 30 inspectors have to manage some public insurance bodies, recently emerged, that are in themselves big insurance concerns.

Other Concerns

I want to remark on another problem that might be more serious in the future. I am referring to possible difficulties in life insurance companies, where the losses may be quite high in the event of real insufficiencies in the reserves. To protect policyholders, the new law requires a higher paid up capital in life insurance. But the new requirements have little effect on the companies that are currently operating, as they have a six-year term to adapt to the new law.

In any case, the process of deterioration is not rapid, due to the improvement of automobile insurance results as a consequence of decreased use of cars because of high petrol prices. According to the market results already known, there was a loss of 4500 million pesetas in 1979 and a profit of 5212 million pesetas in 1980, due fundamentally to investment income. I do not doubt that results of the whole market will improve in 1981, but this will affect mainly the "prudent" insurers, not those that are insolvent.

Also important is news of a possible solution to the problem created by the liquidation of a savings institution, Fidecaya, which is under the management of the insurance department and to which I referred in my previous report. It is possible that its premises and staff may be absorbed by an important Spanish banking group, with the remarkable help of the government through a long-term loan. If this situation has been confirmed (January 31 was the limit date), an important step will have been taken to improve the image of the insurance department as an authority capable of solving the problems that may arise in the future.

In any case, our insurance market may need some kind of institution, created with the participation of the leading insurance companies, to collaborate in the liquidation or reorganization of the companies with difficulties. This would be similar to the sort of "Intensive Care Unit" that has been organized by the banks with the strong financial help of the Banco de Espana.

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Rumours persist that Eagle Star will be taken over, and Lloyd's are a little nearer to their badly needed Parliamentary reform bill, but some brokers are still fighting hard to preserve their links with underwriting agents.

Any time after June 3, Allianz can increase its 28% stake in Eagle Star and put in a bid to take over the company. Thus they would comply with stock exchange rules which bar them from bidding for Eagle Star or increasing their stake beyond 30% until 12 months after their "dawn raid" last year. Why does Allianz want Eagle Star? Two major factors are the stagnancy of their home business in Germany and the bargain price at which Eagle Star's shareholders value the business.

Inevitably, McKinsey's comes into the story. In 1980 it issued a report predicting a decline in the share of the German insurance market held by the Allianz type of composite company. The German market is, of course, rigidly controlled, and these conditions favour an attack by specialist companies and mutuals, which have been increasing their market share at the expense of the composites. If the EEC insurance services directive becomes law, competition will be even fiercer with the entry of foreign insurers. Allianz, as a market leader with about 17% of the German market, will be particularly vulnerable to competition; in the motor market, for example, they were forced to cut rates in 1980 in order to be able to report that "for the first time in many years, the group's market share in motor insurance showed no decline."

Given Allianz's problems in expecting growth in their home market, foreign expansion becomes an obvious priority. Indeed, the pace of overseas acquisitions has been breathtaking: 1977—Austria's sixth largest insurer taken over; 1979—a big Australian takeover and two U.S. companies bought (North American Life & Casualty of Minneapolis and Fidelity Union of Dallas) plus a new Canadian operation; 1980—South African and Australian takeovers. All of these Allianz holdings are either 100% or majorities, so the 1981 minority shareholding in Eagle Star looks suspiciously like the prelude to a full bid in 1982.

But the problem with most large overseas insurance takeovers is that they dilute the shareholders' earnings per share. The extraordinary part of the Allianz/Eagle Star story is that Allianz can afford to pay nearly double the market price of Eagle Star shares and still improve both its earnings per share and its solvency margin. The fundamental reason for this is the difference in sentiment towards insurance shares on the German and UK stock market. Despite being, by UK standards, not a very profitable insurance company, Allianz shares are rated on a 3½% dividend yield and a price earnings ratio of around 19. Eagle Star, even with its impressive profit record, is valued on the London market to give a dividend yield of 5½% (on indicated dividend) and a price earnings ratio of around 13. As for solvency margins, Eagle Star enjoys the exceptionally high margin of 85%. One major factor in the London distaste for insurance shares is the bout of rights issues which followed the 1974-75 stock market collapse, and although this must affect the price of some insurance shares (Royal, even after its recent rights issue still has one of the lowest solvency margins) Eagle Star's margin is so high that it will have no problems on this score in the foreseeable future. Certainly it compares favourably with Allianz's solvency margin of 35%. All in all, it is not surprising that many experts, including stockbrokers Tilney & Co., expect Allianz to bid for the balance of Eagle Star's shares after June this year.

1981 Results Better than Expected

Last year's results for the Big Seven property/liability companies seem to be coming through rather better than expected. True, some companies are reporting lower profits—Commercial Union down from £103 million to £82 million and Royal down from £122 million to £118 million—but many experts were prepared for something worse, and General Accident's profits were up from £40 million to £44 million. Once again, UK results were staggeringly good; adding together the UK business of CU, GA and Royal shows that the underwriting just about broke even, so that the investment income was virtually sheer profit. These breathtakingly brilliant UK results were even more remarkable considering the appalling December weather, which meant exceptionally heavy claims for UK insurers.

Elsewhere, U.S. results were, of course, poor, though not

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