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US CASUALTY INSURANCE OUTLOOK

RT CASUALTY COMMITMENT

Retail brokers and their clients are facing a challenging and changing casualty marketplace. It is important to work with a strong wholesaler partner with specialized product and industry expertise and a proven track record. The RT Casualty team has both. In addition to brokerage services, RT Specialty employs a team of claim handling professionals to assist our clients on claim advocacy, TPA selection, claim reviews, claim disputes and case law and coverage interpretations. RT's senior management remains committed to retaining and acquiring the best talent in the industry.

"The RT Casualty team offers a deep bench of talented brokers all focused on delivering cutting-edge solutions. We are prepared to handle all challenges for our retail brokers and their Insureds in this changing marketplace," says *Chris Houska, Managing Director and President of RT's National Casualty Practice.*

CONTACT

For more information please contact your local RT Casualty broker.

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MARKET OVERVIEW

The overall North American casualty market has continued on a firming pace across most commercial lines. Deteriorating loss trends are impacting underwriting profitability. Several years of declining premium rates, against a backdrop of increased exposures and medical inflation, has pricing trending upward with a renewed focus towards underwriting discipline.

Commercial auto liability has led several of the other casualty lines in rising premiums through 2019. Specific industry segments such as transportation, real estate, hospitality, public entity and utilities have become price sensitive casualty lines, and obtaining market capacity to meet demand can be challenging.

In addition to these adverse loss trends, there are developing and on-going events with catastrophic risk potential. According to a recent report from Willis Towers Watson PLC, "The effects of the wildfire losses and opioid epidemic are being felt on a broad range of risks, and are expected to trigger upward pricing pressure across most commercial lines of business."

Underwriters are also evaluating the poor industry loss trends in the commercial auto space and their effect on other casualty lines—general liability, umbrella and excess coverages. The fact that all these lines operate in the same tort system reinforces the validity of this point. Until there is significant progress made on tort reform both at the state and federal levels, the current trend of escalating jury verdicts, driven by new concepts of torts and negligence, will continue to increase insurance losses. As a result, casualty underwriters are seeking to take on more immediate corrective actions on their account portfolios to respond to their senior management directives for improved profitability.

Carriers and brokers in the commercial insurance sector continue to stay aggressive in the M&A space in pursuit of their corporate growth goals and are seeking new technology platforms. This consolidation has been reducing the number of competitors in the commercial casualty marketplace, especially for the larger complex risks. The effect of these mergers and reduced competition provides an opportunity for the underwriter to apply increased underwriting discipline and pursue their individual account profitability objectives. Primary carriers are now in a better position to increase their pricing, requiring higher deductibles and retentions on loss sensitive programs. In turn, the umbrella and excess markets are raising their attachment points and increasing premiums to reflect the increased pricing from primary carriers.

MARKET SEGMENTS

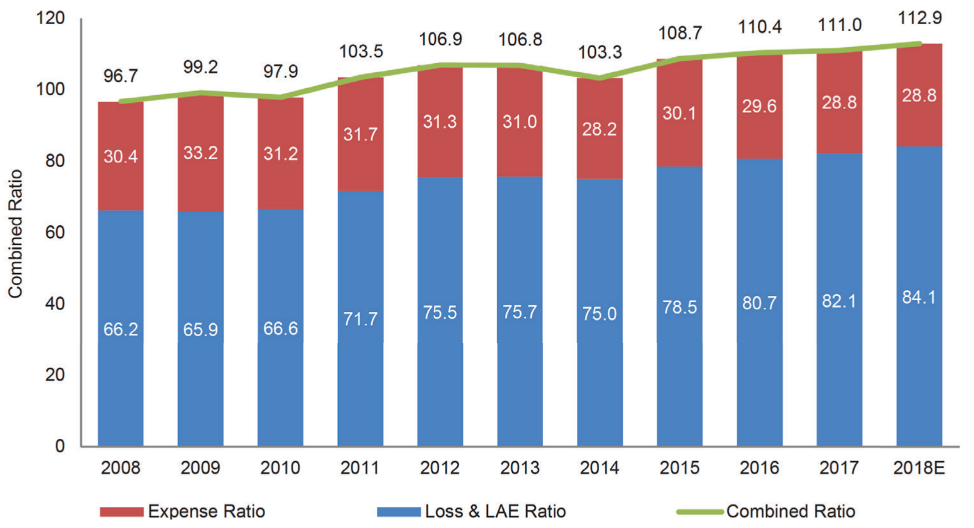
The following five sections discuss specific casualty lines and industry verticals, further expanding on their particular market conditions. Within RT Casualty, there are dedicated broker teams representing each of these segments, among other areas that have been developed for specific industry expertise and advanced product knowledge. Future issues of RT Specialty Casualty Outlook will highlight more of our specialized casualty market segments.

1. Auto Liability

Escalating losses continue for commercial auto liability which makes this class an unprofitable line of business for several of the commercial casualty insurers. Combined ratios have been exceeding 100% for eight consecutive years starting in 2011 (See page 2, Figure 1). Average claim payments continue to rise at a higher level compared to other casualty lines. Rate increases are expected to continue trending upward through 2019, along with higher retention levels for loss sensitive programs. Reductions in available reinsurance capacity have been seen in the primary buffer layers. In regard to the non-owned vehicle exposure and what used to be a standard extension to commercial auto policies, there is now a much higher underwriting focus. As a result, this specialized sector is adding to the pricing pressure along with tightening terms.

Distracted driving and sleep apnea represent major contributing factors to the increase in frequency and severity of claims. These areas

FIGURE 1: US COMMERCIAL AUTO – NET UNDERWRITING PERFORMANCE



Source: ©A.M. Best - used with permission

for concern created additional liability for employers with improper management and training of employees. Stand-alone hired and non-owned coverage remains price sensitive with limited market participation.

2. Umbrella and Excess

Market capacity is constricting for excess liability. Underwriters are quoting smaller line sizes, creating the need to incorporate additional markets and buffer layers to complete the excess placement. The lead layers from several of the lead umbrella markets are reducing their limit offerings. As an example, what was a $25 million lead layer on larger programs is now quoted at $15 million and lower. In addition, umbrella and excess markets are requiring higher attachment points, especially for average and below average accounts with losses.

In combination with the reduction of capacity, the pricing from the umbrella and excess markets has been trending at an upward pace beginning with the mid-year renewals and is expected to continue for the remainder of 2019 and into 2020. For accounts in certain challenged underwriting classes and / or poor loss history, increases can be expected to be dramatic. In some cases, insurance renewal budgeting should take into account the potential for a 2X, and up to 3X, multiple of expiring premiums.

The use of data analytics and modeling to accurately forecast expected losses and evaluate the insured's working layers will provide a proactive element with renewal negotiations. Highlighting the insured's investments in safety and risk mitigation are key components to add into the submission process. Both are critical in order to achieve the best results in this tightening umbrella and excess market.

3. Real Estate

Through the first quarter of 2019, the multifamily real estate sector continues to show the most robust growth compared to office, industrial, retail and hotel. The hottest markets are located in larger municipalities. The southeast and western regions of the U.S. account for the largest demand for rental unit investments. Refer to Figure 2 below noting the top 5 "buy" markets in the U.S based upon projected rent increases forecasted to 2022.

Lessor's Risk Only (LRO) has mainly shifted to the E&S market. The primary driver has been the historically low level of liability premiums in this class against a backdrop of increasing loss trends. For multi-family real estate, casualty markets are re-evaluating this class and placing more restrictions on coverages. Most claim activity against property owners and managers are for lack of adequate maintenance and maintaining safe premises for tenants. This is putting additional underwriting focus on the level of annual capital budgets for the large portfolio schedules. Other traditional exposures related to the larger claims include violent attacks. As a result, there are more underwriters placing coverage exclusions and / or limitation endorsements for A&B (assault and battery). Section 8 (low income housing) and senior and assisted care continue to be challenging risks. Minimum deductible levels can range from $5,000 to $10,000. There are a reducing number of casualty markets willing to underwrite the larger portfolio schedules, and as a result, there can be restrictions on the number of units for a program size and removal of per location aggregates for a single loss limit. This is putting pressure on the larger portfolio programs to stay intact on a competitive level. On certain programs, restructuring, including extracting the best properties, may be the viable alternative to achieve the overall cost benefits.

4. Construction

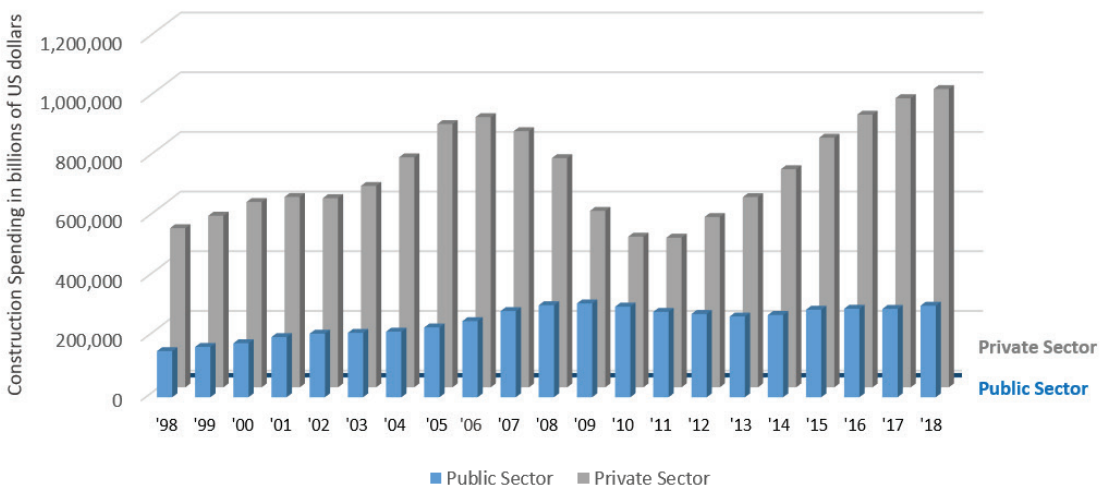
Construction spending in the U.S. for both public and private sector has continued on an upward trend from 2011 through 2018 (See page 3, Figure 3). Current challenges in the construction industry include trade tariffs

FIGURE 2: 1Q 2019 - 2022 US MULTIFAMILY PROJECTIONS

Top 5 Buy Markets	2022 Effective Rents ($ unit)	Change in Rents Present – 2022 (%)	2022 Vacancies (%)	Change in Vacancies Present – 2022 (bps)
Houston, TX	1183	+15.9%	4.3	-150 bps
Las Vegas, NV	1197	+11.5%	3.4	-90 bps
Raleigh-Durham, NC	1184	+12.8%	5.5	-10 bps
Atlanta, GA	1289	+12.0%	4.8	0 bps
Salt Lake City, UT	1087	+10.2%	4.2	-140 bps

Source: ©Ten-X Commercial - used with permission

FIGURE 3: U.S. CONSTRUCTION SPENDING, BY SECTOR, 1998 - 2018 *(in billion U.S. Dollars)*



Source: census.gov

and their effect on determining project cost, along with the industry's labor shortages and the difficulty in filling skilled labor positions. The construction insurance marketplace has remained very active with steady premium growth as a result of the year over year growth in construction spend. Casualty market capacity has, overall, been adequate to support the demand for both commercial and residential contractors, in addition to project specific and wrap-up business. After eight years of sustained growth, continuing expansion of the construction market has allowed the carriers to become more selective in their capacity deployment, resulting in reduced capacity or increased rates in certain jurisdictions. With the exception of specific geographies, casualty insurance pricing has remained relatively stable and competitive. Exceptions include New York, where rates remain high with limited carrier options. Other states, such as Florida, South Carolina, Louisiana, Texas, California, Colorado, and Oregon, have underwriting strain with residential construction and are operating in the legal environments that are challenging with construction defect claims. Underwriting submissions need to be of high quality, organized and detailed to differentiate the claim trends.

5. Hospitality & Sharing Economy

In addition to the traditional risks historically related to the hospitality industry, this segment's landscape has greatly expanded with the sharing economy and rapidly changing customer demands. Advances in guest-focused technology services for enhancing customer experiences has also created additional liability risk for the owners and managers of hotels, home sharing platforms, restaurants and delivery services. These new or unique exposures have limited loss history and little actuarial data in needed for underwriters to fully evaluate the potential total risk. With the casualty market firming and limited number of underwriting participants in this class of business, there still remains a heavy emphasis on the traditional risk and the historical loss drivers. Depending on the degree of the host liquor liability exposure, rates are rising and minimum deductibles are being imposed. Very few carriers are left offering a guaranteed cost option. Coverage restrictions include exclusions and / or limitation endorsements for A&B (assault & battery).

LOOKING FORWARD

Deteriorating loss trends will continue to be the driver of the casualty market's upward pricing. The U.S. commercial casualty market conditions are expected to continue to firm through 2019 and into 2020. Auto liability is still expected to lead the pace, and as of mid-year and going forward into 2020, primary general liability and umbrella and excess lines have been trending significantly upward into double-digit ranges, for above average accounts with good loss histories and proper management controls. Specific upward variances from this range can exist for stressed accounts with poor loss histories. There are also specific industry segments of casualty that are more challenged with higher pricing pressure, market capacity and restricted coverage terms. These include multi-family real estate, utilities and transportation. Depending on the exposure mix for specific accounts, renewal negotiations on casualty rates, terms and retentions can be similar to an insured in one of the strained industry classes. Examples include accounts with a large fleet exposure, and utility powerline servicing companies that are exposed to wildfire conditions.

The volume of submissions into the market has significantly increased. In order to maximize results and differentiate the insured's risk in this firming marketplace, there needs to be a well-thought-out "go to market" strategy. This starts with transparent communication of current market conditions and incorporates full vetting of the incumbent relationships with other potential carriers. The quality of the submission can be further enhanced by incorporating additional loss years and exposure data. In addition, the brokers need to have a well-thought-out strategy for their pricing targets to avoid immediate declinations from underwriters that would potentially respond if they were given realistic pricing expectations in this tightening market. Throughout the negotiation, program structure alternatives should be reviewed and evaluated for best terms, pricing options, and optimum retention levels.