



FEBRUARY 2021

US PROPERTY INSURANCE OUTLOOK

MARKET OVERVIEW

The year 2020 challenged the commercial insurance market in numerous ways, accelerating an already hardening market that started in 2018. Beyond the typical hard-market drivers of increased catastrophe losses and lower investment yields, the market faced compounding challenges with COVID-19, political and social unrest and heightened concerns around climate change—all on a global landscape. Specific to the commercial property market over the last two years, renewals experienced increased pricing, capacity reductions and restructuring of layered placements, along with tighter terms and conditions.

Midway through Q1 of 2021, market conditions continue to tighten. Insurance carriers remain focused on improving underwriting results, with scrutiny surrounding building valuations, complete and correct COPE information, policy form language and adequate retention levels (i.e., deductibles). However, while underwriting appetite changes have caused capacity restrictions for certain classes of business, the industry balance sheet remains strong. Capitalization for insurers, reinsurers and facilities has proven markedly resilient. This contrasts with past hard-market cycles, where insurance and reinsurance capacity reduced in availability.

Future loss development from COVID-19 and record catastrophe events in 2020 are contributing factors to the continued property pricing increases and strict policy terms expected in 2021. Additionally, the market is moving through adjustments that started from a lower base amount compared to previous market cycles in the past. Even with these conditions, factors helping to stabilize the market include an increased market share of excess and surplus lines capacity, new alternative capacity channels and lower than expected January 1 treaty reinsurance renewals, as rate increases were in the single-digit range.

LONDON MARKET

London-based capacity continues to increase and will operate with a total market stamp capacity of approximately \$48 billion in 2021,

an increase of 9% year-over-year. Over 50 syndicates obtained business plan approvals to increase their capacity as of January 1. Overall, the London market is successfully raising new capital and expects to continue expansion into the U.S. property market.

Lloyd's continues to lead the industry in developing stand-alone coverage solutions designed to affirmatively cover potential areas of exposure that may be present due to restrictive underwriting terms prevalent in the standard and domestic markets. Examples include specialized coverages to address pandemic business interruption exposure and developing facilities to offer coverage for strikes, riots and civil commotion (SRCC).

Contrasting the optimism surrounding increased capacity and new product offerings, a mid-January ruling by the United Kingdom Supreme Court regarding business interruption and COVID-19 caused new uncertainty for insurers and reinsurers. The U.K. Supreme Court largely affirmed the ruling issued in the Financial Conduct Authority (FCA) test case, and is widely considered a victory for policyholders on many of the most significant legal issues. The U.K. ruling runs counter to the majority of U.S. court decisions which by and large have been in favor of insurers. While it is too early to measure the financial impact for the London market and the industry as a whole, the U.K. ruling may be critical to determining the long-term implications of COVID-19 for property insurers.

CATASTROPHE LOSSES

Insured losses from U.S. natural catastrophes in 2020 are estimated to be \$67 billion—a significant increase from 2019, which had \$26 billion of insured losses according to Munich Re.¹ The costliest single event was Hurricane Laura, hitting the Louisiana coast as a Category 4 storm and creating an estimated \$10 billion in insured losses. Last year's Atlantic hurricane season set records with 30 named storms, 12 of which made landfall, exceeding both the previous record of 28 named storms in 2005 and the previous record of 9 landfalls set in 1916. Tropical cyclones, with overall insured losses estimated at \$26 billion, were only second to the costliest natural catastrophe type

THE RT PROPERTY COMMITMENT

"As the Excess and Surplus Lines (E&S) segment of the insurance industry continues to grow, the RT Property Team has raised the bar even higher, delivering focused, creative solutions for our retail brokers and their insureds. RT's team of exceptional wholesale property brokers is on the way to further growth in 2021, following another successful year in 2020.

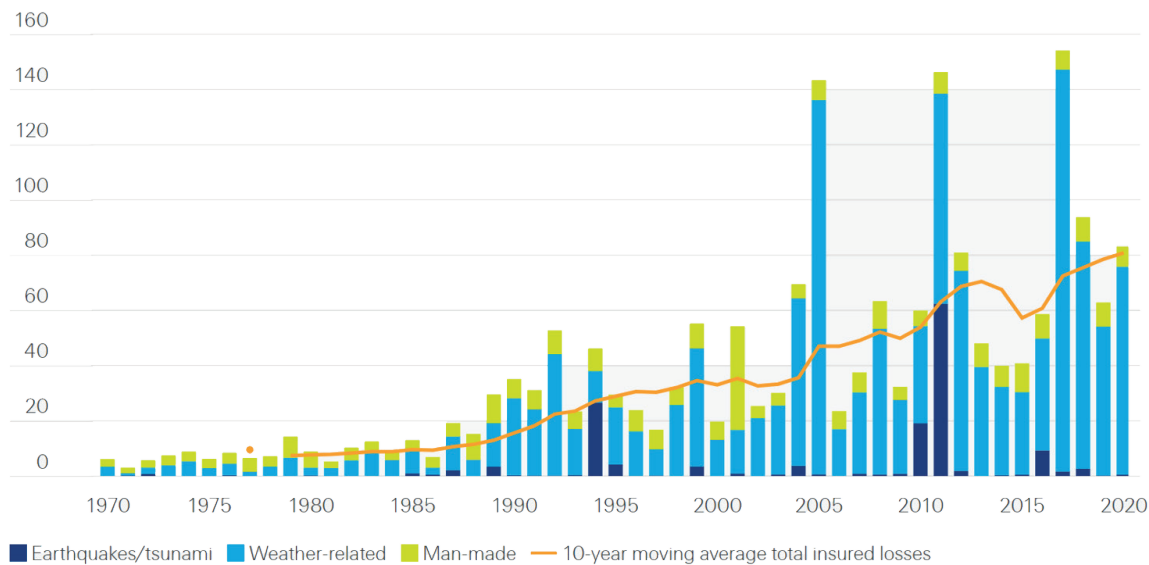
Our exceptional track record is a testament to our motto: 'Out-Think. Out-Work. Out-Execute. Repeat.' By combining the talent of our expanded team of property brokers with our expertise in modeling capabilities, coverage and form knowledge, along with our claim advocacy, RT Property will continue to be one of the fastest growing property teams in the country!" states Brenda (Ballard) Austenfeld, President of RT's National Property Team and Managing Director.

CONTACT

For more information, please contact your local RT Property broker.

¹Record Hurricane Season and Major Wildfires – The Natural Disaster Figures for 2020, January 7, 2021, Munich Re, [munichre.com](https://www.munichre.com)

Figure 1: Insured Losses, 1970 - 2020, in USD Billion at 2020 Prices



Source: Swiss Re Institute

in 2020: severe convective storms. Severe convective storm losses in the United States are estimated to have cost insurers \$30 billion for 2020. An August 10 “derecho” —a fast-moving line of thunderstorms—caused insured losses of \$5 billion, making it the costliest convective storm disaster in 2020. Catastrophe modeling and years of consecutive increased losses indicate the cost of insuring this peril will continue to rise and further the need for reinsurance against what was once viewed as an attritional peril.

Despite hurricanes and convective storms accounting for an estimated two-thirds of insured losses, wildfires in the U.S. set distressing records of their own in California, Colorado and the Pacific Northwest. The area burned in California during 2020 was over four times larger than the 2015–2019 average, and five of the individual fires in 2020 rank in the top 6 on the list of the largest fires in California since the 1930s, according to data published by the California Department of Forestry and Fire Protection (CAL FIRE). Colorado experienced three of its largest fires on record, and Oregon recorded its worst year ever, with over 4,000 homes lost. Total insured losses for 2020 are estimated to be \$11 billion. Increasing insured losses from natural

catastrophes have been trending upward for nearly five decades (Figure 1). Early predictions by Colorado State University call for another above-average Atlantic Hurricane season, while losses resultant from secondary perils are forecast to increase as well, according to Swiss Re.

REINSURANCE

January 1 treaty reinsurance renewals for property insurers resulted in modest price increases versus initial forecasts, which predicted much higher outcomes. Cedents able to demonstrate favorable loss experience and prudent underwriting typically benefited from capacity negotiation and favorable pricing terms. In contrast, those with successive years of losses, changing risk profiles and overall poor performance experienced more significant pricing corrections relative to their peers.

The Howden Market Report recently summarized their January 4, 2021 reinsurance update, depicting “strong capitalization... with dedicated reinsurance capital estimated to have increased marginally to \$416 billion in 2020, as growth amongst traditional sources and catastrophe bonds offset the remaining trapped capital in the collateralized market.

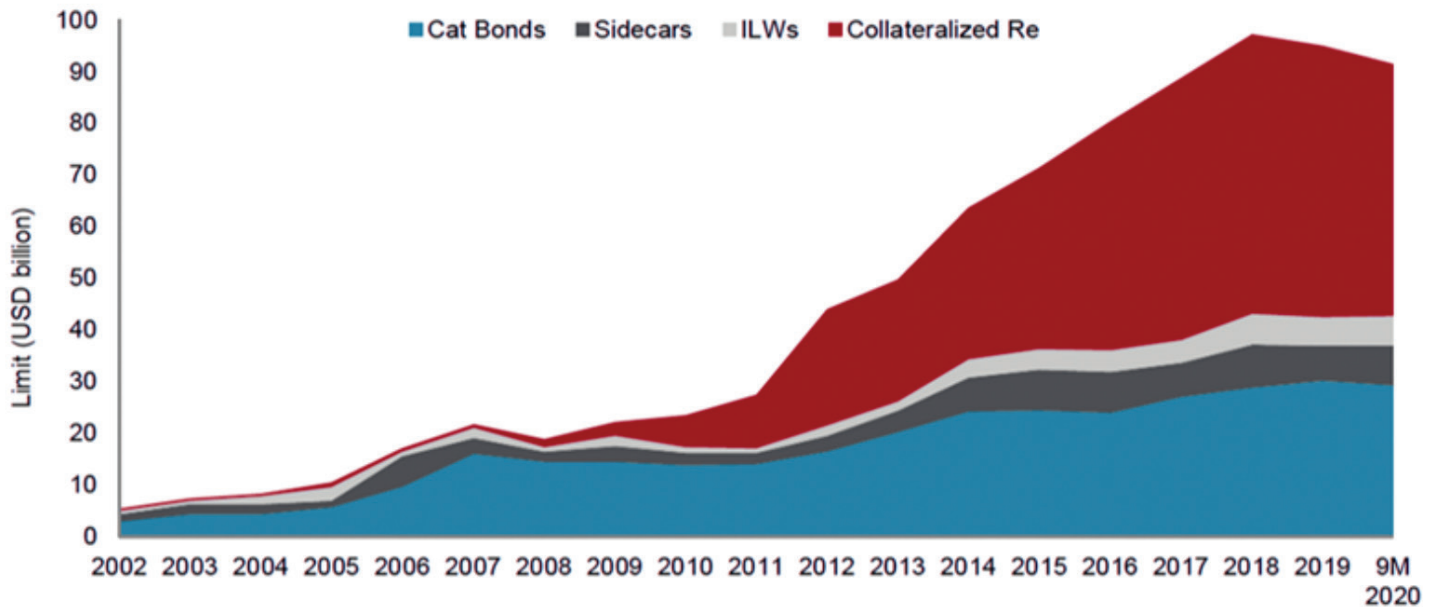
Additionally, incumbents and new players raised close to \$20 billion of capital in 2020 to replenish buffers and take advantage of market opportunities, with more to come this year.”²

Serious attention was given to program pricing, structures and underlying terms and conditions (i.e., communicable disease and silent cyber exclusions). Initially, COVID-19 was heavily emphasized in treaty renewal discussions, yet it has been reported that concerns about the potential loss projections were muted to some extent by a review of the closed transactions, resulting in negotiations that were primarily motivated to look through the uncertainty.

Additional pricing concerns were driven by consecutive years of above-average catastrophe losses and record activity during the 2020 Atlantic hurricane season, despite 2020 not reaching the record payout levels of 2017. These concerns have been compounded by the devastating wildfires along the U.S. Pacific Coast and increasing severe convective storm activity in the Midwest. Property reinsurance markets reevaluated pricing levels to account for the ever-increasing frequency and severity of weather events. As a result, cedent insurers are, in most instances,

²The Howden Market Report, *Hard Times*, January 4, 2021, Howden, [howdengroupholdings.com](https://www.howdengroupholdings.com)

Figure 2: Alternative Capital Deployment



Source: Aon Securities, Inc.

taking higher net positions rather than paying reinsurers what they consider to be uneconomical prices for frequency protection.

The Howden Market Report also noted, “Despite the draw of a more attractive pricing environment for the traditional reinsurance sector, the investor appetite to back collateralized reinsurance or sidecar transactions was held back in some quarters by heightened risk aversion following successive years of losses and lackluster performance. Persistent adverse development on prior years, concerns about COVID-19 business interruption claims, 2020 U.S. catastrophe events, and increased scrutiny around climate change drove risk premium higher [for collateralized reinsurance and sidecar markets].”² See Figure 2 above for the Aon graph that measures the composite of funds for alternative capital deployment and note the reduced levels for collateralized reinsurance and sidecar transactions into the third quarter of 2020.

COVERAGE SPOTLIGHT: EARTHQUAKE

As earthquake capacity continues to constrict with both insurance carriers and MGUs alike, aggregate management has become equally, if not more important than, specific risk characteristics. Markets are less willing to gross up their position on accounts with facultative reinsurance, offering just their net line, which requires more carriers to participate on nearly all sizeable placements. Historically, older properties (specifically those built prior to 1984 and especially those built before 1956) have been price drivers, yet as the aforementioned factors push account pricing beyond the typical Average Annual Loss (AAL) multiples, unfavorable risk characteristics have become somewhat muted. Before COVID-19, the California Department of Insurance reported only 1 out of 10 commercial buildings being insured for earthquake coverage. The proportionately low number of buyers who do purchase earthquake coverage are largely driven by debt requirements. Thus,

there is little expectation that capacity constraints will be eased by changes in buying behavior. Carriers who have written critical earthquake for a long time are rightsizing their metrics after more than a decade of soft market pricing, yet they are not seen to be overly opportunistic at this time. Some MGUs, on the other hand, are leveraging their position as large capacity providers and delivering heavy rate increases where possible. Builder’s Risk earthquake placements remain one of few segments to avoid these adverse pricing impacts. Upon completion of the project, aggregate usage will not remain, as the completed assets are moved to separate, permanent property coverage.



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