2020 State of the Market Review & Outlook

Insights from Industry Leaders

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Market Overview

The impacts of an on-going global pandemic, a record-breaking number of natural catastrophes, along with civil unrest, on top of an already hard market, can be felt throughout the insurance marketplace. The Property & Casualty (P&C) market has traditionally been cyclical. Hard markets have generally been represented by rising premiums and reduced capacity. Whereas, soft markets usually see a longer period of falling. With the market firming, the expectation is that it will continue through 2021. TSIB remains committed to bringing our clients the latest information across the Property & Casualty Lines through our State of the Market report.

Rate

The U.S. commercial P&C market continues to harden and shows no signs of slowing down. All the major reinsurers and insurers are maintaining their assessment of the market pricing going forward, which is continuing to rise in 2021. Ongoing uncertainty surrounding the pandemic continues to fuel the increases and further expanding the Excess & Surplus (E&S) space. Workers' Compensation has been the bright spot for many commercial insurance buyers over the last two years. Even though premiums were decreasing in this segment, they were increasing just about everywhere else. This changed as we approached the 2nd half of 2020 when COVID-19 took hold. That is when Workers' Compensation insurers became concerned about the impact of the pandemic on losses. Rates by business class, although regulated by state, are slowly on the rise.

Capacity

Unlike previous hard markets that had similar elements in breadth and duration, this one appears different in that capacity is not scarce. Carriers are often reducing the limits they are willing to deploy on any given risk. However this is the result of tactical decisions surrounding the return on investment and not due to an overarching shortage. Larger loss limits and quota share placements are becoming harder to renew. In many cases they are being replaced with layers and shared deals with multiple carriers. Generally speaking, insureds who are not securing total available global capacity on their risk should not be the least bit concerned. Only those who buy large sets of limits have reason for concern.

Terms & Conditions

The industry had become lax regarding policy terms & conditions and were not consistent year over year. Due to the recent COVID-19 Business Interruption court decisions, the Business Interruption clause alone is often overlooked and will arguably define the property platform relative to claims.

Expect coverage terms & conditions and forms to continue tightening to include pandemic exclusions. Exclusions like Communicable Disease are more likely to be added in industries where they believe liability litigation from the pandemic is likely. Many policy extensions are automatically including this exclusion. Issues to work through may include, but are not limited to: blanket vs. specific values, special perils, Business Income language regarding infectious disease, Ingress/Egress, Civil and Military Authority, renewal form changes with restrictive wording (not willing to follow form underlying) and Communicable Disease/ Pandemic Exclusions. In addition, some Carriers are requiring enhanced surveillance cameras in order to offer coverage and on-site security during off hours.

New Market Entrant

Capital coming into the P&C marketplace continued the momentum that started in Q2 with new start-ups and expanded appetites. These trends do have some similarities to earlier start-up waves that followed major economic events in 2001. However, in the current wave, the uncertainty comes during a global pandemic on the heels of:

- major catastrophes
- a strengthening dollar
- a market meltdown
- rising equities

Notable industry veterans have commented that these new entrants will have little impact on pricing momentum, suggesting that disciplined market conditions will continue. While Capital may not have the legacy reserve concerns of incumbents, they will still face similar challenges including record low interest rates and a lack of experienced underwriting talent to meet demand

Coverage Segments

Property

With the U.S. Property market continuing to harden significantly, the following have start to appear as the new norm:

- rate increases
- low interest rates
- limited or loss of capacity
- more restrictive terms & conditions

That reality combined with increase in wildfires, civil unrest, storms, and the uncertainty around how COVID-19 Business Interruption claims will ultimately play out, has created a very complex situation. With all this, there has been a significant increase in primary submissions (including Builders Risk) hitting the marketplace, especially in the E&S segment, a trend that will continue through 2021.

Domestic Market

- 30% rate increases for standard large placements with minimal to no losses.
  - 90% & up for problematic accounts- loss ridden or catastrophe prone.
- Catastrophic peril exposures are experiencing rate increased from 10%-40%.
  - Coastal or other CAT exposed but loss-free accounts are up 25%- 50%.
  - Treaty reinsurance renewals increases are up to 20%.
- Period extensions on current policies have been a key aspect during the pandemic as contracts were put on hold.
- Non-renewing accounts, offering smaller quota-share options, or cutting capacity, requires more placements. This is creating a "wild west" coverage mentality with different terms, pricing, deductibles sub-limits, and exclusions.

Global Market

- Overall market rate expectations for 2021 are conservatively around the 10%-12% mark.
- COVID-19 has had significant impact on the London construction market in early 2020, as new projects had ongoing delays due to lockdowns.
- Syndicates are moving parts of their business outside of Lloyds, to allow them to take advantage of market conditions remains.
- Recent announcements of fresh capital including Canopius, Ark, Hiscox, Beazley, and Lancashire, will add over $2B combined capacity.
  - Even with these new entrants, incumbent markets that are industry veterans have commented that new entrants will have little impact on pricing momentum, suggesting that disciplined market conditions will continue.

The overall ending of Q4, showed market submissions have steadily increased, displaying positive strides as we head into 2021.

Primary Casualty Liability

General Liability and Product Liability markets have experienced tightening throughout the year. It tightened more toward the end of 2020, fortunately, not as drastically as the Excess segment.

Most industry analysts agree that aggregate loss reserve redundancy is gone for all lines of business, except possibly Workers' Compensation.

The rise of social inflation and impact on jury verdicts, along with the potential third-party losses associated with COVID-19, continue to force Carriers to push rates upward.

Carriers continue to tighten underwriting guidelines, non-renew poorly performing risks, or exit the casualty market altogether. Along with capacity issues and accounts with perceived higher hazard products, or accounts with poor loss experience, they can expect higher rate increases and higher retentions. Accounts without loss severity or frequency issues can typically expect less of an increase depending on the industry and product/ premises risks. Alternative program structures (Deductibles/ Retentions/ Captives/ Parametric Insurance) may need to be explored. In addition, some clients with long tail risks are converting from Occurrence form to Claims-Made to save on overall cost.

For many classes of business, lead Umbrella markets are regularly requiring increased attachment points for the underlying primary General Liability (GL) limits and increasing the primary Auto limit. Such an increase in limits traditionally increases the GL premium. Depending on whether Carriers keep the additional limits net or seek Reinsurance driving premiums higher. In addition, depending on the industry, we are starting to see Carriers mandate Pandemic or other Communicable Disease Exclusions.

Umbrella/ Excess

The Umbrella/Excess market continued to harden through the first two quarters of 2020. Third quarter renewals, especially July 1, saw further turmoil with rate increases from 15%- 100% depending on the industry. The Umbrella market continues to deteriorate as Auto Liability and General Liability claims increase in severity. This is exacerbated by social inflation and increasing anti-corporate juror sentiment, without substantial tort reform, this trend is expected to continue unabated.

Capacity continues to tighten. As recently as 2019, you could secure coverage through a handful of Carriers, but now, to build towers of more than $25MM you will need to add more layers and at increments as low as $5MM. While this reality creates more new business opportunities for Carriers, it can be a challenge to find enough Carriers to fill out large towers and coverage inconsistencies. Umbrella markets continue to scrutinize deployment of limits, looking to reduce volatility by decreasing capacity and increasing attachment points.

Markets continued to impose substantial rate increases after almost a decade of flat premiums. The rate percentage increases are more notable in the Excess layers. Excess layers used to be priced from 45%-55% off the previous layer, whereas in todays market the higher Excess layers are priced at 85%-95%. This is due to aggregate losses starting to hit these layers, as well as a capacity crunch. In addition, to pick up extra premium, Carriers are looking to change the policy condition from flat to auditable, limiting coverage enhancements while adding Occupational & Communicable Disease Exclusions on both the primary and excess programs.

> *"… in today's market the higher Excess layers are priced at 85% -95%."*

Auto

Commercial Automobile rates continue to increase for nearly all industry sectors, particularly those with larger fleets in energy services and trucking/transportation. Primary Auto for fleets over 200 are up 10%-20%. Otherwise, generally 10%-15% rate increases can be expected for smaller to mid-sized fleets with a clean loss history.

As a way to manage risk, the Umbrella & Excess markets are dictating Auto primary limit increases from $1MM CSL, to an average of $3MM and up. This allows the Umbrella layers to be farther away from frequency issues.

With respect to primary Auto in the New York/New Jersey metro areas, South Florida, and Louisiana, verdicts and awards strongly favor Plaintiffs. As losses develop in those jurisdictions, markets are seeing claims settle for 2-3 times the reserve amount. Primary layer issues carry over to Excess as Excess transportation in particular is problematic. Hired/ Non-Owned Liability coverage underwriting has tightened with Carriers scrutinizing their policyholders' internal practices.

Workers’ Compensation (WC)

Until recently, Workers’ Compensation remained a profitable and relatively stable segment. Like most things in 2020, even the remarkably stable WC market is becoming slightly volatile. Significant increases were noted in Q2 as this marked the end of 21 quarters of decreasing prices for Workers’ Compensation.

The primary driver of the uncertainty is COVID-19, with increasing medical costs (states are creating different regulatory requirements). Carriers are working to manage both short term and long term impacts of the regulatory requirements which include: Compensability of claims related to the virus, changes in workforce (i.e. telecommuting), claims due to layoffs and furloughs, delayed medical treatments, and classification changes as employees roles change.

As the landscape of WC changes with the pandemic, we would encourage insureds to increase their focus on employee safety by following all CDC and OSHA directives on employee safety. This includes training and education on injury prevention and keeping a close watch for fraudulent claims, as the issue of compensability is worked out in each state.

Directors & Officers (D&O)

Insurers are concerned that the longer the pandemic continues, the more private companies will fail. Whereas Public companies will have more financial problems that were not adequately disclosed leading to more litigation. Market-leading Carriers will continue to seek large premium increases and upward adjustments on retentions. While in some cases simultaneously cutting limits, as increases are generally more severe on Excess layers.

From the Carriers perspective, there is inadequate compensation for risks assumed, claim cost inflation, and social inflation. In addition, there is an unusually high number of open SCAs pending against D&O's, with almost 9% of all public companies being sued for security fraud in 2019.

An emerging challenge in the public D&O space involves foreign-domiciled companies that trade on the U.S. Exchange, as they may/may not have legitimate operations in the United States. As the Lloyds' market is starting to pull back from those risks, U.S. markets tend to decline covering them. From a rate perspective, companies are seeing renewal increases of 25%.

Employment Professional Liability (EPLI)

In the wake of furloughs and layoffs, this line is under increased scrutiny. Underwriters are asking companies how they determined who to let go and who to bring back due to heightened concerns around diversity. Some Carriers have instituted moratoriums on classes of business, such as hospitality and entertainment. There are a number of factors influencing the rising rates within the insurance market including: catastrophic losses, inconsistent underwriting profits, eroding investment returns, the economy, the cost of reinsurance, and more.

There are also factors that specifically impact your insurance rates, like the coverage you're seeking, the size of your business, the industry that you operate in, the location of your business, your claims history.

While litigation for workplace harassment fell slightly in 2019 as compared to 2018, overall levels of litigation for workplace claims are still at near-record highs. Additional trends, such as an aging workforce, could further the volume of legal actions filed against employers. Overall coverage, rate, and capacity will be further scrutinized in 2021 with higher SIR/Deductibles and lower limits available.

Professional Liability

Still a healthy amount of capacity and competition in the marketplace depending on what industry you are in. Unlike other sectors, Carriers are not adding COVID-19 exclusions in this sector.

Cyber

Cyber is a segment of the market where premiums are increasing but not as a result of COVID-19. Ransomware has been a problem for years but losses being paid by insurers are becoming more frequent and more severe. Premiums are trending upward along with more scrutiny around underwriting. Carriers are asking more detailed questions on controls and utilizing network scanning technology.

Sweeping regulatory changes around consumer privacy rights is driving increased concerns over more costly losses on the horizon. Board oversight of Cyber and privacy risk is increasing as a result of changing workplace dynamics (i.e. remote working). Ransomware continues to be the most frequent attack style in 2020, as cases are up 22%.

Attackers are now stealing data prior to deploying ransomware or publicly shaming companies infected to force payment of the ransom. Department of Treasury has advised that Carriers involved in paying a ransom to groups known to be on the OFAC sanctions list are subject to penalties. Penalties for violations of privacy laws such as GDPR and CCPA are steep through direct fines or private rights of action granting statutory damages. Securities class action and shareholder derivative suits following high profile cyber and privacy incidents have boards asking more questions about Cyber risk and insurance.

Notable suits include: Yahoo, Equifax, Marriot, FedEx, Capital One, and Zoom Communications.

Be prepared for Carriers to tighten up on capacity, increasing deductibles or retentions, cutting sub-limit capacity while premium increases take hold more rapidly.

"Ransomware continues to be the most frequent attack style in 2020, as cases are up 22%."

Surety

The Surety market is very dependent on construction along with the overall economy. The Architecture Billings Index (ABI), a leading indicator of future construction billings, reported historic declines in April, but has since rebounded. Although with resurging COVID-19 numbers, there is concern this uptick may be temporary. We are seeing longer warranty terms pushed into contractual agreements from Owners and Developers to Contractors and Subcontractors.

As a result of the bond guaranteeing the underlying contract(s), the Surety industry is under pressure to support longer warranties. Downward pressure on terms and conditions and rates has eased, but we do not see a hardening Surety market. There continues to be an abundance of capacity and terms & conditions are at an all-time low. The large contract Surety market is healthy but showing the most signs of tightening, in comparison to the small –middle market segment as the projects are generally smaller in nature with somewhat more traditional delivery methods, the marketplace is more competitive.

Environmental

Generally speaking, insureds with favorable loss experience have not experienced notable coverage or price changes. Those with poor loss experience are often re-underwritten, with all aspects of the policy potentially subject to added restrictions. Insurers evaluating new business are disciplined and less interested in gain share or market share. Despite the Business Interruption and Disinfection expense claims that have already been reported for pandemic-related losses, some markets have not yet broadly implemented new language (especially those not already excluding viral or communicable threats).

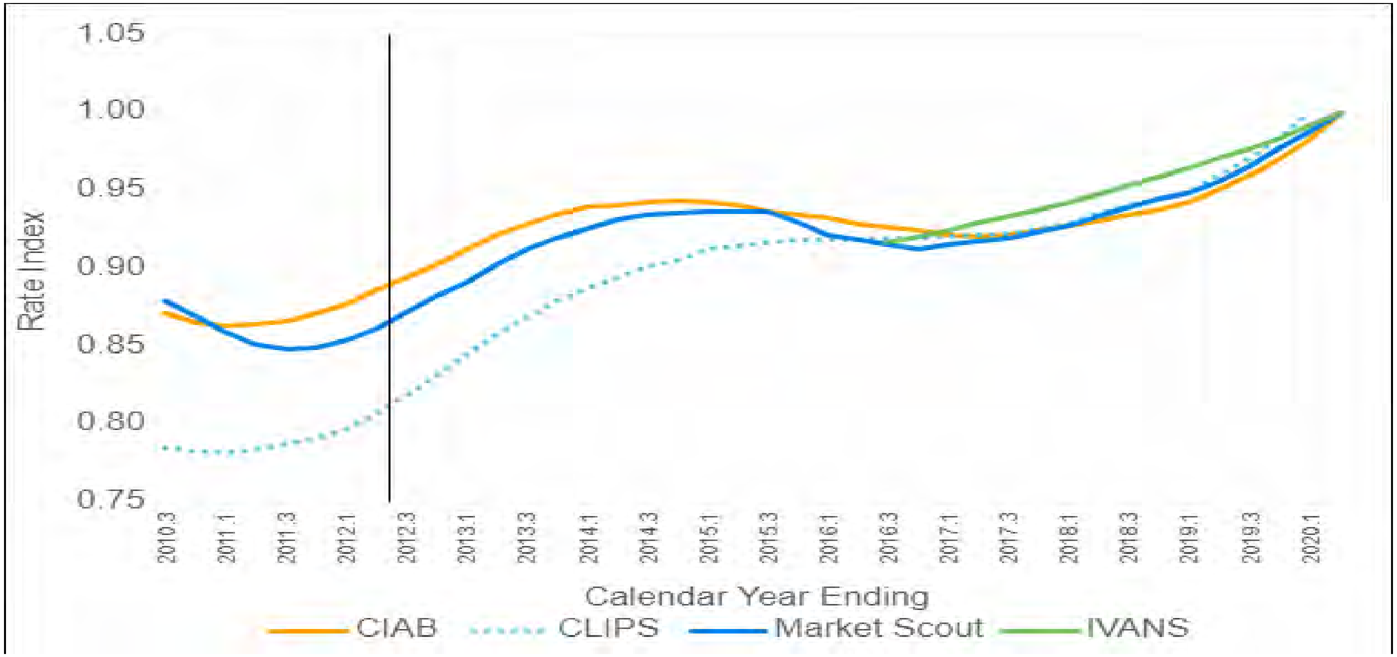
Construction Rate Changes

The chart below shows the Q4 2020 rate fluctuations for the following lines of coverage:

Lines of Coverage	Rate Change Year End
General Liability	Flat to +15%
International Casualty	Flat to +5%
Umbrella (lead)	+25% to 100% (lead) or more for higher hazards
Excess Liability	+20% to 100%
Auto	+5% to +15%
Workers' Compensation	Flat to +5%
Property- Builders Risk	+5% to +20%
Professional Liability	Flat to +10%
Contractors Pollution	Flat to +5%
Cyber	+10%
D&O Private	+5% to +25%
D&O Public	+25% to +50%
EPLI	+5% to +25%

Global Insurance Composite Pricing

This chart shows the commercial lines calendar year rate changes. This measures the ratio of rates during the 12 month period ending with the most recent available quarter (Q2).



- CIAB- Council of Insurance Agents & Brokers Property / Casualty Market Index Survey
- MB- MarketScout Commercial Lines Market Barometer Report
- IVANS Index
- CLIPS- Willis Towers Watson Commercial Lines Insurance Pricing Survey

Key Approaches

In your conversations with insureds, here are some key approaches you can take to minimize the effects of a hardening market for the next couple of years.

Plan Early- Prepare for a longer renewal process 120-150 days out with insured meeting multiple times throughout the process, as well as meet early with the Carriers.

Prepare Senior Management for impact to budget, premium, coverage, and longer quote time.

Increase Communication with both the insured and the Carriers.

Conduct loss analysis and consider multiple retention options.

Utilize technological tools to improve efficiencies and create better user experience for all parties.

Proactively provide renewal exposures and any updated applications early.

Make sure the submission is comprehensive, thorough, and current.

Carrier follow-up is crucial.

A Look Ahead

As we look ahead into 2021 and beyond, it's evident there are 6 forces that will shape the industry.

1. Product Innovation & Reallocation Of Portfolio Priorities

Across all lines, risks are changing and becoming more complex due to:

- Technological advancement
- Fast-changing customer behavior
- Cyber threats
- Economy evolution

These changes have placed increased importance on product innovation, intangible assets, and compliance.

2. Uninsured Natural Catastrophes

Catastrophe losses have doubled over time and the majority remains uninsured. Governments have intervened to provide post disaster relief for uninsured losses or even subsidize insurance or reinsurance. Unless more risk is transferred to the private sector, the long-term impact on demand will be negative.

3. Data & Analytics Reshaped Distribution

Data and analytics capabilities supported by better access to data for underwriting, claims, and portfolio management are critical for insurers to succeed in the future. An insurance factory (a mostly autonomous workforce consisting of distinct groups that deploy special data and analytics capabilities) can help insurers extract more value from the P&C value chain. Digital marketing is also a must-have competitive skill.

A Look Ahead

4. Reshaped Distribution

Brokers and other intermediaries now capture twice the value of Carriers' profit, a higher level than in other intermediated industries such as mortgages. In ten years, about 25%-30% of personal lines P&C premium could be distributed via B2B2C ecosystems.

5. Cost Reduction and efficiency gains

While other industries, such as automotive and telecommunications, have reduced unit costs by more than 50% over the past 15 years, administrative cost per policy for the P&C industry in mature markets has remained unchanged or even increased.

6. Talent Strategy

Research shows that about 23% of jobs in P&C insurance could be displaced by automation by 2030, and the remaining roles will require higher digital proficiency. A survey found that globally, the most digitally advanced insurers had 15 times more digital talent when compared with less digitally advanced insurers.

> *"Research shows that about 23% of jobs in P&C insurance could be displaced by automation by 2030…"*

A Look Ahead

2020 has been an intense year, from a pandemic to civil unrest, in addition to the natural catastrophes, including wild fires. Considering this list of disasters, the primary issue impacting the P&C insurance marketplace is uncertainty. The construction industry may emerge from the pandemic strong or relatively unscathed compared to other segments of the economy, but it also faces its share of challenges in managing exposures, delays, added costs and shutdowns.

COVID-19 has changed how people live, work, and interact in their professional and personal lives. Changes to the workplace will remain long after the pandemic subsides, including:

- Jobsite risk and safety have been redefined
- Increased use of technology (i.e. ways that make project management easier, more remote working, etc.)
- Smaller employee pool (i.e. shortage of workers)
- Supply chain disruptions
- Longer project timeframes
- Increase in off-site and modular construction

This pandemic put a spotlight on coverage gaps by showing the economic impact of uninsured risk or excluded causes of loss.

A Look Ahead

The dramatic losses in the industry over the last five years has sped up the need for new insurance solutions globally. Anticipation of a new pool of capital entering the marketplace in 2021, does not appear to be influencing incumbent market's decisions to increase rate and improve on sustainable of terms and conditions. In 2020, the casualty insurance was dominated by increasing premium rates, higher underlying attachment point(s), disappearing capacity on the high excess, and underwriting discipline.

In 2021, submission quality, managing renewal expectations, channels of communication, client diversification, utilization of technological tools, and timing will be critical. More emphasis should be placed on a strategy for the proactive mitigation of risks through comprehensive safety and quality control programs.

As the construction industry heads into 2021, leaders have recognized change is for the long term and have invested in tools, strategies, and operating procedures to come out strong and improve for future success.

How TSIB Can Help

As we begin 2021, TSIB remains close to the industry & market developments. We will continue to guide and support our clients through these future challenges. From leveraging our expertise and offering up-to-date industry appropriate solutions, together we can navigate 2021.

At TSIB, some of the ways we can help you is by:

- Differentiating your risk in the marketplace
- Providing Carriers with submissions that clearly outline the qualities of your risk, overall risk management philosophy, and risk controls (i.e. loss control/safety, contractual risk management, risk mitigation, capital expenditures, etc.)
- Focusing on Coverage Terms & Conditions language
- Benchmarking Umbrella/Excess limits

Working with TSIB not only allows our clients to leverage our in-house industry experts, but provide proprietary analytics. We guide our clients toward a better understanding of what is occurring in the market, why it is occurring, what to expect, and how we can assist you to obtain the most cost-effective program available in the marketplace.

If you haven't spoken with us yet about the next few years, now is the time to do so! Reach out to TSIB today to speak with one of our Risk Consultants who can evaluate your entire insurance program.

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