Market Update

Fall 2021

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Market Overview

The U.S. commercial property & casualty (P&C) market continues to harden, driven by increasing loss trends in liability lines, historic low interest rates, more large weather-related loss events, and other compounding factors. With no changes related to these drivers on the horizon, the marketplace will continue to be characterized by a high level of uncertainty.

The P&C market has traditionally been cyclical. Hard markets have generally been represented by rising premiums and reduced capacity, while soft markets usually see a longer period of falling rates and expanding capacity. However, many experts believe the current market to be more underwriting driven, an anomaly that has not followed the path of traditional cycles.

Key Approaches to Minimize the Effects of a Hardening Market

McGriff is dedicated to helping our clients succeed in a changing marketplace. Key strategies include:

1. Plan early. Identify key areas of concern in the program and develop a plan to address them with multiple options, at least 120 but up to 150 days in advance.
2. Prepare senior management for potential impacts to budget/premiums, coverages, and longer quoting timelines. Even the earliest renewal submissions may come down to the wire for finalization.
3. Effective communication with both the insured and insurers.
4. Set realistic budgets with multiple options.
5. Conduct a loss analysis and consider multiple retentions and structures, including captives, if warranted. Many carriers now require 10+ years of losses, summarized.
6. Meet with carriers early to understand all issues and thoroughly examine potential options. Seek underwriter commitment to general renewal terms early in the process.
7. Proactively provide renewal exposure updates, any supplementary applications, and all supporting documentation early in the renewal process, but by no later than 90 days pre-renewal.
8. Ensure exposures are current and the submission is comprehensive and thorough, to remain top of mind amidst increasing underwriting submissions.
9. We are seeing the most drastic premium/rate changes from incumbent non-renewals in any layer/structure. If an underwriter or underwriting management expresses concern about loss ratio and references the potential for non-renewal due to losses, class of business, or particular risk characteristics, attempt to work through issues early via risk control, higher deductibles and rates.
10. Prepare to address short-term and long-term impacts related to COVID-19 as well as protocols and procedures to mitigate potential losses or impact on business operations.

Property & Casualty

Q2 2021 was the 15th consecutive quarter of increased premiums with respondents reporting an average increase of 8.3% across all-sized accounts. Premiums increased for all lines of business for the 5th consecutive quarter, though price increases for all lines moderated in Q2 2021 compared to previous quarters. The only exception was Cyber, which recorded the highest premium increase out of all lines, 25.5%, surpassing the17.4% increase in Umbrella by a significant margin.[1]

General Liability

The Primary General Liability market continues to experience tightening, albeit not as drastically as other lines of coverage.

- For accounts with a good loss history, we are seeing 5%–10% increases as a starting place, especially in the middle market/admitted space.
- Difficult classes are starting to see higher increases and coverage restrictions, including full Assault & Battery and Abuse/Molestation exclusions, among others.
- Many carriers are declining to look at Professional and Healthcare accounts if the insureds have had COVID-19-related deaths or cases in their facilities. We expect an average 25% to 35% increase in the rate and higher deductibles.
- For higher hazard products with clean loss histories, the increase will likely be 10%–20%+. On accounts with losses, +20% is the likely starting point.
- Most carriers are adding Communicable Disease exclusions for GL & Excess, although a few admitted markets may remain silent for certain industries.

Commercial Auto

The Commercial Automobile market remains very challenging. Rates continue to increase across nearly all industry sectors, particularly those with larger fleets. Those increases are primarily tied to fleet size, scope of operations, perceived strength of risk control measures (or lack thereof) and claims history.

- Overall, 10%–20% rate increases are typical starting points and common among fleets with good experience and fleet safety programs.
- Expect 25%–40%+ increases for fleets with loss frequency and/or severity issues.
- Additionally, clients with poor experience are often urged (or required) to take on larger deductibles.
- Monoline auto markets continue to dwindle, reducing competition further.
- In a continuing trend, umbrella/excess markets are requiring higher liability attachment points of anywhere from $2 million to $5 million depending on the size, type and radius of the fleet.

Umbrella/Excess Liability

The underlying reasons for rate increases have not changed and reflect the same elements reported in 2020.

- Capacity management by the market has been a trend over the last 12–18 months with limits becoming compressed. Few markets are offering lead umbrellas over $10 million (unless supported by primary and mostly only for the best risks) and in the case of high hazard, large fleets or losses, leads may be limited to $5 million with only a handful of E&S markets willing to participate.
- Depending on class, risk characteristics, losses, etc., we expect increases in the range of 10%–50%+.
- In the middle market space, +10% is likely the starting point, but standalone umbrellas with low hazard and no losses will likely see increases of 15% to 30%+.
- Increases for high hazard, large fleets, or accounts with losses could be in the 30% to 50%+ range with incumbents.
- Excess layers on large ($100 million to $500 million) towers are seeing significant reduction in capacity, causing more carriers to fill the program and leading to 100%+ increases in some layers with markets pushing minimums per million of limit and layer.
- Coverages such as Assault & Battery and Sexual Abuse/Molestation are difficult to obtain.
- Some carriers in certain industry groups are pressing for higher attachment points for their underlying limits (e.g. $2 million per occurrence/$4 million aggregate primary GL and Auto vs. $1 million per occurrence/$2 million aggregate limits).

Property

With the property market continuing to harden significantly, McGriff teams are working with our clients to navigate the market tumult. Rate increases, limited or loss of capacity in some cases, and more restrictive terms and conditions appear to be the norm.

The hard market was with us even before the pandemic. That reality, combined with continued uncertainty around how COVID-19 claims will ultimately play out, has created a very complex situation. The markets continue to struggle with how to best determine adequate rate levels and how to use capacity.

- Rate increases vary, but property continues to increase by at least 15%–25% for all locations/capacity and coverage limits.
- Accounts with losses are seeing rates climb by 25%+ or higher depending on loss frequency and severity.
- Marine rates are in the 5%–10% range depending on loss history.
- Single carriers with limited CAT exposure and a decent loss history are looking at +10%–20%.
- As the admitted markets tighten their terms, the Excess & Surplus market share is rising.
- On the E&S side, we expect the rate range to start around +15%, but the top end will vary.
- In certain CAT areas, some markets are requiring named storm sub-limits mandated by reinsurers.
- CAT-prone accounts and/or loss-problem accounts might see 30%+ rate increases.
- Certain classes such as forest products and frame habitational are still in disarray and could see rate increases at 30%+ and even much higher.
- We are seeing continued scrutiny related to insurance-to-value reporting (coinsurance issues).
- The overall tightening with terms will continue (Ingress/Egress, Civil and Military Authority limitations, renewal form changes with restrictive wording, and Communicable Disease/Pandemic exclusions in some cases).
- However, the second and third quarters of 2021 may be a bit fractured for certain accounts that over-corrected last year in price, deductible or both.

Workers' Compensation

In a rapidly changing insurance market where rate increases are ubiquitous and capacity is shrinking, Workers' Compensation continues to be the most competitive casualty line of business, but rates are inching upward.

- Most carriers continue to use Workers' Compensation as a competitive tool, pairing it with General Liability and Auto in their primary casualty quotes for multi-line deals.
- Carriers continue to work through pandemic impacts, including compensability of claims related to COVID-19, telecommuting/changes in the workforce, and classification changes as employee roles change.

[1] CIAB Commercial Property/Casualty Market Report Q2 2021

Cyber

The beleaguered cyber insurance market continues to worsen at an accelerating rate. Many leading carriers have exceeded their 2021 underwriting budgets, allowing them to be even more selective in committing capacity. As capacity contracts, rates continue to rise.

Picking Up Speed

Since the cyber insurance market is proving to be a large Cat market with substantial aggregation potential, it may take at least three years for the market to stabilize. The problematic threat landscape, combined with systemic risk, means that losses are overwhelming a relatively small premium pool. Complex and widespread attacks – SolarWinds, Accellion, MS Exchange, and Accenture, for example – are difficult to shoulder. Cyber underwriters have grown intolerant of poor cyber hygiene.

Most cyber insurers have reduced their line size to half of the expiring limit on the tower, and many reserve full limits for clients with a proven track record of cyber security excellence. According to Fitch, in 2020 the direct loss ratio for the standalone cyber market was 73%, up from the 42%-47% average loss ratio in prior years. Carriers have experienced no breathing room on their loss ratios into 2021, so even with hefty premium increases, their near-term forecasts look dire.

Threat Actors Advance Skills

Ransomware attacks continue, seemingly with no end in sight. Gen. Paul Nakasone, who jointly leads the National Security Agency and the U.S. Cyber Command, was asked at the Mandiant Cyber Defense Summit in early October to predict whether or not companies will still be mired with the ongoing threat of ransomware in five years. His simple reply was swift and affirmative: "Every single day."

According to CrowdStrike's 2021 Annual Threat Hunting Report, over 65,000 intrusions were detected by their Overwatch tool, while intrusion campaigns increased by 60% year over year. Nearly 70% of reported attacks were not malware, which means threat actors are using stealthy tradecraft to evade autonomous detection. To make matters worse, the length of time adversaries take to move laterally across the network once they've compromised an access point is now just 90 minutes, down from nine hours last year. In some cases, this "breakout time" took a mere 30 minutes.

Invest, Prevent, and Prepare

Cyber insurance does not forgo the need for cyber security. In fact, the opposite is true. In order to qualify for cyber insurance, companies must have a fairly robust cyber security program in place. Multifactor authentication (MFA) for remote and privileged access is mandatory. Some underwriters consider inadequate remote desktop management protocols, overutilization of service accounts, and lack of protections around domain administration credentials to be reckless and disqualifying for insurance coverage.

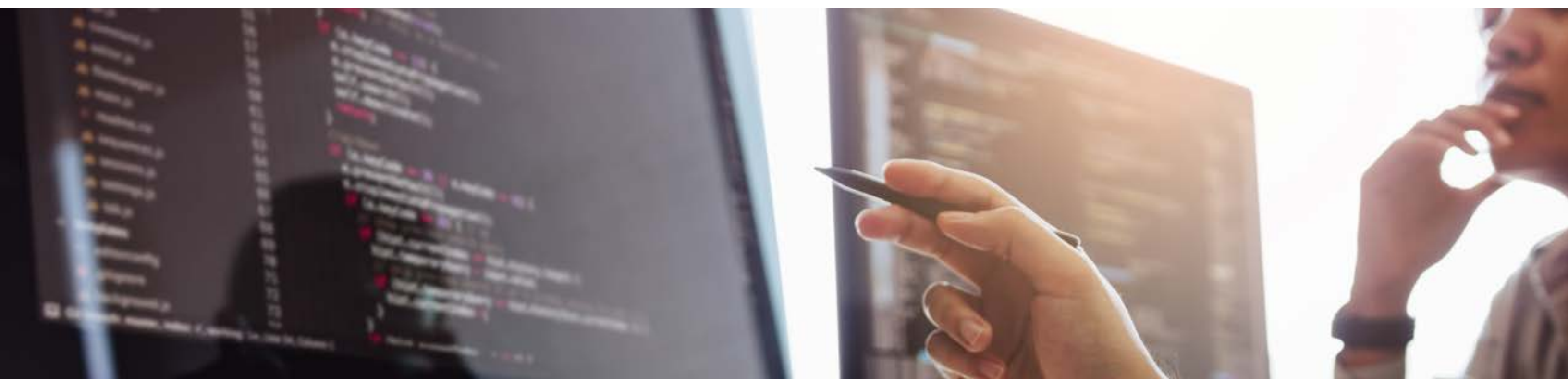
Underwriters may consider other stopgap mitigating risk controls, but patience has grown thin for companies that promised to make these upgrades last year and never did so.

To qualify for coverage, risk managers need to convey to their Information Technology and Operation Technology leadership the following minimum expectations from cyber underwriters:

- MFA in place for remote access to email accounts and to the network, in desktop/laptop logins, and for all privileged accounts and critical applications.
- Formal written and updated Disaster Recovery Plan and Business Continuity Plan – both plans must be tested annually.
- Limited reliance on service accounts and proper configuration and controls for domain admin accounts.
- Formal backup restoration program, including on-premises and off-premises environments and tested for viability.
- Periodic internal and external penetration testing.
- Rigorous patch management.
- Vendor cyber risk assessments and ongoing supply chain governance.
- Persistent employee and contractor phishing awareness training.
- Compliance with applicable state and federal regulatory laws and standards.
- Diligent retirement of aged technology resources and legacy data.

In specific circumstances, some underwriters will agree to write the program on the condition that these minimum standards will be met at targeted timeframes during the policy year. Sub-limits may apply during this "curing period." Higher self-insured retentions and longer business interruption waiting periods also may apply to the first-party insuring agreements. However, many underwriters are quite content to roll off cyber program towers, especially if there is insufficient premium at the attachment point and if the policyholder has failed to deploy these minimum standards.

Because of rising pressure to harden network and data resources, we expect the global cyber security products market will grow from $150 billion last year to $156 billion for 2021 at a compound annual growth rate (CAGR) of 4.4%. Experts predict it will reach $240.5 billion in 2025 at a CAGR of 11%. The total security tools market will expand to at least $208 billion by 2023.



Government Intervention

Because of the boundaryless nature of cyber risk, the U.S. government is limited in what it can do to protect against international threats, especially since 87% of the nation's infrastructure is privately owned. So it's incumbent upon organizations to deploy every affordable resource and plan for every contingency in order to maintain the highest level of cyber security. That said, there are a number of federal government programs designed to prioritize initiatives and empower the private sector in the war against cybercrime. Notable measures include:

Cyber Regulatory Oversight – In June 2021, the U.S. Securities and Exchange Commission (SEC) announced it would be focusing on cybersecurity disclosures made by public companies, following a series of executive orders from the Biden administration. In doing so, the SEC signaled it would take an increasingly active role in a "whole-of-government" response to cybersecurity threats. A proposal for final rule-making on cyber security disclosures and updates to the SEC's 2018 Guidance was expected to be issued in October. In August, the SEC sanctioned three firms in the investment advisor and broker-dealer industry, charging deficient cyber security procedures and making clear its expectations for proper protection of confidential consumer information.

Cyber Solarium Commission – Established in 2019 to develop consensus on the strategy to defend the U.S. in cyberspace, the commission has released a series of instructive white papers on key topics, including "CyberSecurity Lessons from the Pandemic," "Growing a Stronger Federal Cyber Workforce," and "Building a Trusted ICT Supply Chain."

Updated OFAC Guidance – The Office of Foreign Assets Control updated its October 2020 ransomware guidance to introduce "significant mitigating factors" in the agency's enforcement determinations to account for proactive measures that a victim company may have taken to reduce risk, such as incident response planning, maintaining offline backups, and employing authentication protocols. Companies that do not adopt cybersecurity measures, report incidents to law enforcement, and/or fail to conduct due diligence before paying ransom to a sanctioned entity will be more likely to incur public enforcement actions, including civil monetary penalties.

Also, as part of its announced "robust actions against ransomware," the U.S. Treasury Department added the virtual currency exchange, SUEX, to its Specially Designated National (SDN) list, citing that over 40% of known SUEX transactions stemmed from illicit activities. SUEX is registered in the Czech Republic but operates from Russia. This action was an important step in the federal government's ongoing effort to suppress money laundering via cryptocurrency.

Concurrently, U.S. Deputy Attorney General Lisa Monaco recently announced a new Justice Department initiative to utilize the False Claims Act (FCA) to go after contractors and grant recipients for cybersecurity-related fraud by failing to secure their networks and notify following cyber breaches adequately.

> "We are going to go after that behavior and extract very hefty fines," Monaco said. "This is a tool we have to ensure that taxpayer dollars are used appropriately and to guard the public trust and that is what we are going to do with respect to this civil fraud initiative."

Ransomware is Here to Stay

In our view, laws that would make it illegal to pay ransoms will not deter determined criminals. Unindexed and untraceable cryptocurrency makes it exceptionally difficult, if not impossible, to track payers and payees, due to the widespread use of tumblers. It's hard to believe that underground criminals would be swayed by such laws.

It's also worth noting that the rationale behind paying threat actors is often tied to public safety and/or the demands of consumers and communities that depend upon the rapid resumption of critical services and availability of critical products (e.g., Colonial Pipeline, JBS Foods). Companies may have no other choice than to pay the ransom because the alternative may be far worse to their customers or the public at large, especially when the health and safety and potential for massive property damage are part of the calculus.

Interdependency

The recent major outage at Facebook demonstrates our society's increased dependence on automated technology. We have moved on from a time when we could revert back to manual processes to conduct business. The Facebook event also showed that configuration issues, such as a routine Border Gateway Protocol update gone wrong, play a very large part in the reliable functioning of networks. Adding further insult to injury was the sobering reality that even sound controls can backfire. As they urgently tried to fix the problem, Facebook employees could not get physical access to their data centers because the security credentials embedded in their ID badges were managed by technology controls that were offline due to the outage.

Adopt a Security Culture

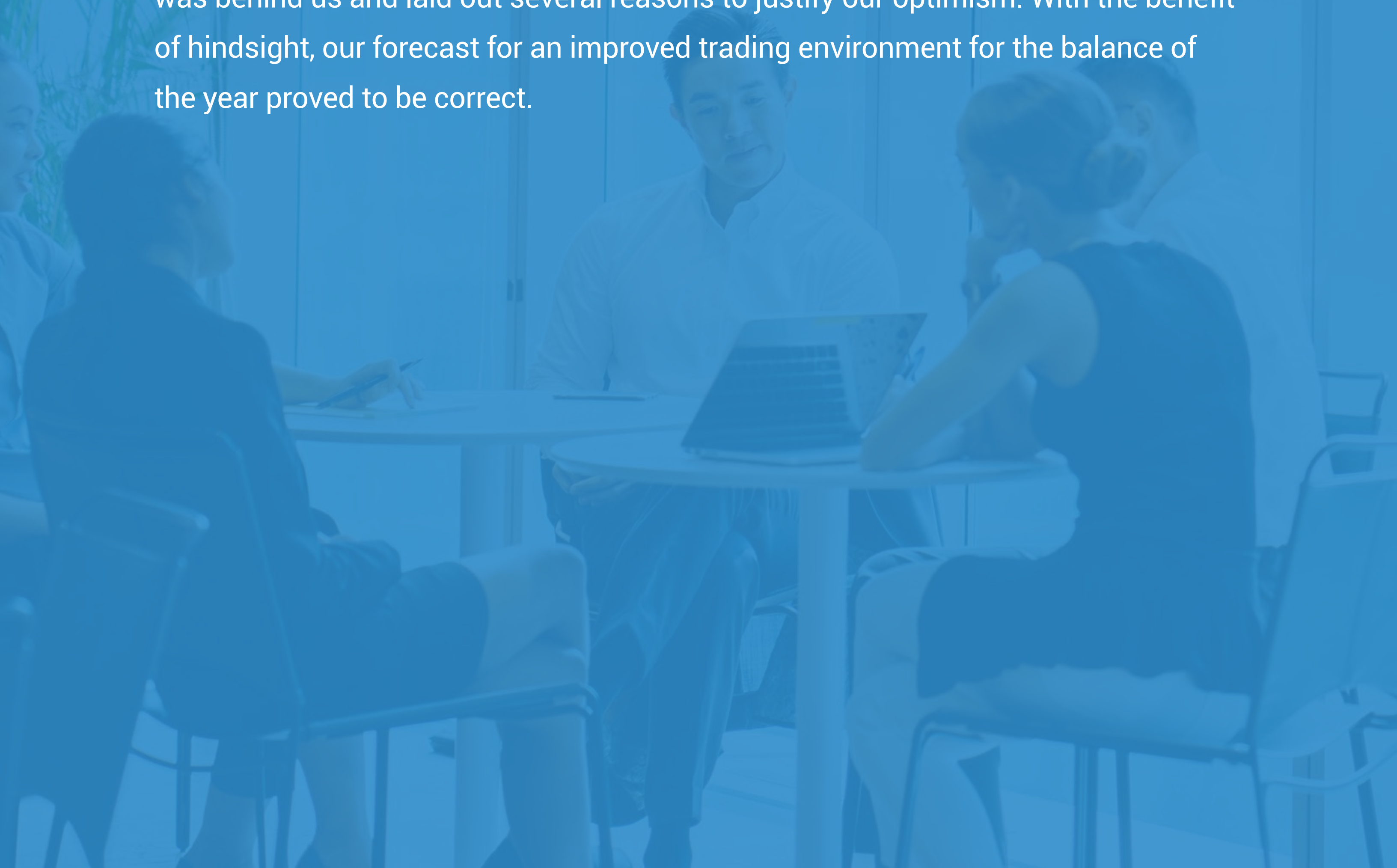
All efforts, from cyber underwriting to federal enforcement, illustrate the fact that organizations must fully commit to making cyber security a core component of everything they do. From product design and operation oversight to software provenance and vendor management, cyber security must be front of mind. Three questions were posed to Chris Krebs, former head of the U.S. Cybersecurity and Infrastructure Security Agency (CISA), at the recent InsureTech Connect conference: "Why is it so bad out there? What is the government doing? What should I be doing?"

Krebs acknowledged that the situation had indeed worsened and that it is likely not going to improve anytime soon. He emphasized the fact that everything is becoming more digitized and that threat actors are keenly aware of that. He implored companies to make it much more difficult for threat actors to be successful.

Krebs also offered these words of caution: "If the leaders aren't committed to enabling a better secure culture or outcome, then you're dead in the water. You might turn another good quarter, have a good fiscal year, but it's going to catch up to you." He reminded all organizations that they must demonstrate they're worthy of an insurance policy with proof that they've "adopted the right measures and done the right things."

Executive Lines

In our Spring 2021 *Market Update*, we speculated that the worst of the hard market was behind us and laid out several reasons to justify our optimism. With the benefit of hindsight, our forecast for an improved trading environment for the balance of the year proved to be correct.



The Hopeful Start of A More 'Buyer-Friendly' Market Cycle

While premium levels certainly remain elevated for the vast majority of clients compared with recent historical norms (i.e., prior to the market correction which began in earnest in late 2018), we have seen a marked and consistent tapering of premium increases this year. And now, many clients with renewals in the fourth quarter are experiencing flat or close to flat pricing, and in some circumstances, even modest premium reductions compared with their 2020 renewals.

Additional Market Observations

Impact of New Market Capacity – Just like any other market, Directors and Officers (D&O) insurance is driven by basic supply and demand. Over the past 18 months, there has been a significant influx of new capital entering the public company D&O space, either through new insurers (to the product line) or through MGA/MGU vehicles. While this new capacity has thus far not been materially impactful in terms of overall market participation, there is no question the newer market entrants will continue to create competition with legacy carriers. This will lead to client leverage and better pricing outcomes, especially on excess layer placements. We expect this capital to really get to work in 2022.

Increased D&O Insurer Appetite for New Business – Recognizing that the current market still offers attractive pricing, some leading D&O insurers have clearly recalibrated their approach toward new business opportunities in a concerted effort to gain greater market share. Clients with excellent financial and operational performance, strong balance sheets, and superior corporate governance standards are attracting considerably more interest from D&O insurers than they did last year.

For the most part, primary layer placements continue to renew with incumbent carriers. But we are seeing some movement on excess layers as D&O insurers that have competed for primary opportunities are getting rewarded with excess layer participation.

Focus on Client-Specific Underwriting – In 2020, we saw a considerable amount of "portfolio underwriting" where the perceived risk characteristics of an individual client company garnered little attention. As a rising tide lifts all boats, clients were subject to broadly consistent premium rate and retention increases based on their industry sector and market capitalizations. Today, we think the market is underwriting clients much more objectively. Some client programs are perceived as still being underpriced, whereas others might be viewed as being priced above market. Either way, D&O insurers are paying more attention to the specific client risk as opposed to taking a "peanut butter" (spreading) approach across their book of business.

Underwriter Merry-Go-Round – There has been an unprecedented level of personnel movement in the D&O market, with underwriters and management teams coming and going between different insurers and facilities. Industrywide, there is a scarcity of underwriting talent and some D&O insurers also seem to be challenged in terms of their professional staffing. This demand for talent is driving up operational costs for insurers, which conceivably could have an inflationary effect on the future pricing of their product. A more likely scenario, however, is that these cost pressures will push D&O insurers to grow and compete more aggressively for business.

Initial Public Offerings (IPOs) and Special Purpose Acquisition Corporations (SPACs) –The D&O market remains incredibly challenging for companies filing for an IPO, including SPACs, or for companies still within a three-year window of their IPO. D&O insurers continue to be very cautious with risk selection and capacity deployment, even though the substantial premium rates and retentions on offer are seemingly very much in their favor.

The explosive recent growth in IPO and SPAC formations has led to an increase in the number of U.S. publicly traded companies, but the jury is still out on whether this business will ultimately be profitable for D&O insurers. Year to date, there have been over 20 SPAC-related securities class actions filed. And since there are currently 485 active SPACs seeking their merger targets, we would expect SPAC-related securities litigation to escalate considerably in 2022.

Securities Class Action (SCA) filings Continue to Decline – Notwithstanding the cautionary comments on anticipated SPAC-related claims, the general trend of SCA filings is promising. According to litigation data from Stanford Securities Class Action Clearinghouse, 162 companies have been named as defendants in federal SCA actions year to date as of October 2021. This compares with 321 cases in 2020 and an average of over 400 companies facing lawsuits in federal securities fraud cases each year from 2017 to 2019.[1]

Some of this lower filing volume in federal courts can be attributed to a change in plaintiff attorney strategy on "merger objection" cases, but nevertheless the trend is encouraging. According to Cornerstone Research in their 2021 Midyear Assessment report on securities litigation, the likelihood or susceptibility of a U.S. domiciled company being named as a defendant in an SCA decreased to 4.2%, the lowest rate since 2014.

Coverage Quality Remains Strong – Despite the challenges of the past several years, it is worth noting that D&O insurers have not made significant efforts to scale back meaningful coverage terms and conditions, and they continue to provide clients with high quality coverage solutions.

As we look forward to 2022, we believe we're now hopefully at the start of a more "buyer-friendly" market cycle. We predict that competition in the market will generally lead to more successful renewals. But with an enhanced focus on client-specific underwriting by D&O insurers, clients should expect to see some variance in renewal outcomes.

[1] https://securities.stanford.edu/charts.html

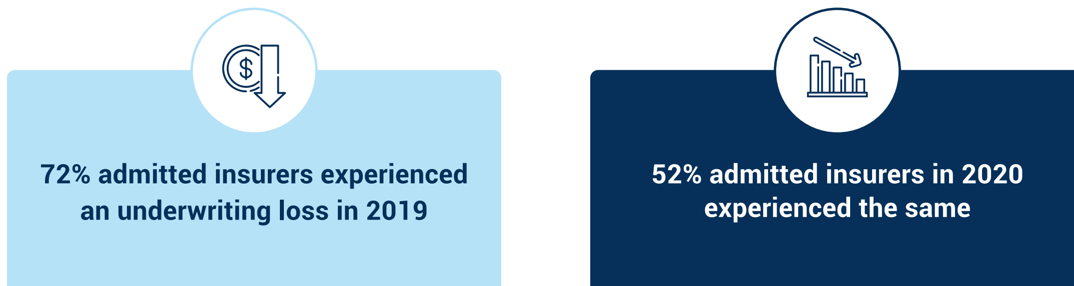
Aviation

The aviation insurance marketplace has been stabilizing in the wake of a three-year period of hard market conditions that increased premium volume. While incumbent markets are still driving for rating increases, the level of increase has moderated significantly. We've also seen a slow, but steady increase in capital deployment, providing a pressure relief valve for the industry. All of this means the outlook is beginning to look more and more favorable for insurance buyers. Nevertheless, we continue to closely monitor an industry that, overall, is still in a precarious position.

Current State of the Aviation Insurance Market

Actuarial firm Milliman released its "United States General Aviation (USGA) – Admitted Market" report in July 2021 summarizing the 2020 statutory financial results for the market. The report provides useful insight into insurer performance from 2016 through 2020, quantifying the industry's underwriting losses, among other insights. "USGA premium increased significantly over the last two years, specifically a 33% increase in written premiums from 2018 to 2020," the report said.

While we saw a $52 million loss in overall admitted markets in 2020, this was significantly lower than the $285 million underwriting loss in 2019.



While this could be attributed to underwriting selection, it is also proof that the rating increases in the past few years have started to improve the health of the marketplace.

The Milliman report also acknowledges that, "the 33% increase in premium may understate the scale of increase, as some large USGA accounts that went to the subscription market may have been written in part by European insurers or via surplus lines capacity."

We believe Milliman's 33% overall increase is understated. In the prolonged soft market, most U.S. domestic brokers walked away from London and surplus lines insurers, since there was no need to go outside the admitted market. McGriff took a different approach and worked to continue to foster relationships with the overseas marketplace. Nonetheless, there has been continued growth in the level of London and surplus lines market participation on accounts. Looking at our own portfolio, average London market participation on vertical placements was around 10%-15% prior to 2018. Today, depending on the account profile, we see an average of 20%-25% overseas participation on placements. Overseas markets continue to adjust their risk appetite and we are seeing increased interest on a regular basis.

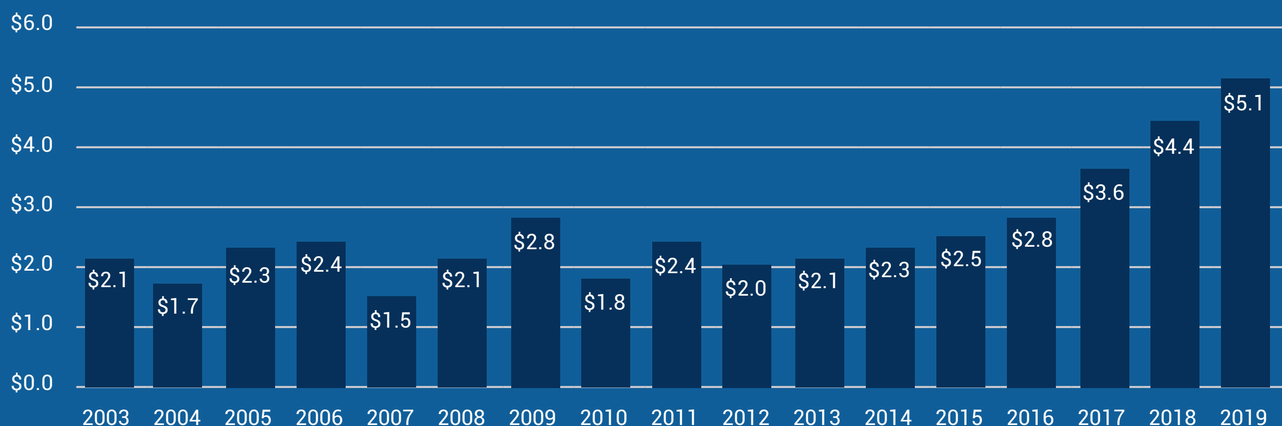
Back to the U.S. market, we have recently seen a group of more than ten people leave QBE Aerospace for Applied Underwriters with an eye toward writing a broad portfolio of aviation and aerospace risks. They also will be entering into the aviation Workers' Compensation market.

Claims Experience, Social Inflation and Legal System

Our optimism about the aviation insurance market remains tempered by continued claims activity. In July 2021, a hailstorm moved through Roswell, NM and damaged hundreds of aircraft that had been parked by airlines due to the pandemic. Market intelligence suggests this will mean $100 million (or higher) claim to insurers, a very substantial non-operational loss.

Additionally, despite much lower flight activity in 2020 due to the pandemic, "the number of people killed in large commercial airplane crashes rose in 2020 to 299 worldwide, even as the number of crashes fell by more than 50%."[1] Liability concerns resulting from aviation accidents continue to be a problem as social inflation is still at the forefront of insurers' minds.

While we haven't seen many large liability awards related to aviation accidents of late, we worry that unexpected liability awards could arise in the future as the stalled court system (due to the pandemic) resumes normal activity. Even without nuclear verdicts, the Milliman report shows that the median value of awards in the U.S. from a single-fatality accident has increased from $2.5 million in 2015 to $5.1 million in 2019.



Source: Milliman Report

Reinsurance Market

The aviation insurance marketplace is unique compared with most other lines of insurance because of the high hull and liability limits that are written on a primary basis. Most other lines of insurance rely on layering policies to achieve a higher liability limit. A primary policy for a corporate jet on the other hand often will include a liability limit of at least $300 million. Insurers are able to write these programs because the reinsurance market creates the necessary spread of risk.

The cost of reinsurance, a vital component of the aviation insurance marketplace, has a significant impact on the premiums paid by operators. And while the reinsurance market has continued to push rating increases and returns have improved, we have seen numerous natural disasters this year and many reinsurers reporting large losses in the third quarter. Combined with inflation trends such as social inflation and climate change, these losses suggest that further reinsurance rate hardening is necessary as reinsurers continue to seek returns above their cost of capital. Therefore we would expect reinsurers to push for increases on their January 1, 2022 renewals.

[1] https://www.insurancejournal.com/news/international/2021/01/04/595850.htm

Construction

The construction market continues to tighten across multiple lines of coverage, albeit at a slower rate (with the exception of cyber and executive risk). That adds up to continuing rate increases and restricted policy terms. These increases and terms have created the first hard market in the past 20 years, causing many contractors to scramble to maintain some level of consistency in risk management costs. However, we believe we have arrived at a potential new norm of pricing levels, driven by rising inflation, increased claim costs, etc.

Market Rate Changes

Primary Casualty	
General Liability	5-15%
WC	0 – 3%
AL	10-20% (Continues to be biggest primary casualty loser)

Professional / Pollution	
Professional & CPPI	0 - +5%
Pollution	0 - -5%

Umbrella / Excess	
Lead Excess / Umbrella	15-25% (Continue to rise, but at slower pace)
Excess Layers	5-10%

Property
10-15%

Builders Risk
10-15%

Q1 – Q3 of 2021 Summary and Looking Ahead

With the changing market conditions, contractors must approach their renewals with care. Here is a summary of key considerations:

- Since the auto liability line continues to be the main loss driver of the primary lines of business, push for investments in the telematics space to differentiate yourself from other contractors (applies to both primary and excess carriers)
- Excess carriers continue to push for higher attachment points, so getting primary limits as high as possible is critical
- Due to pricing levels, new capacity has opened up in both the domestic and international (London and Bermuda) channels
- Wildfire-exposed risks continue to be among the most challenging placements. Contractors with true wildfire exposure will pay 30% rate on line as a starting point and higher for certain utilities you're working for
- Captives continue to be a hot topic (more on this below)
- Cyber liability is the most volatile renewal, with carriers continuing to deploy their capacity on accounts with best-in-class security, i.e., Multi-Factor Authentication (MFA)
- Professional/Pollution remains competitive, yet carriers willing to cover design/build exposures are commanding more premium to cover the risk

General Liability

Primary capacity for the overall general liability market remains strong, with carriers eager to write new accounts. Although capacity is favorable, we are seeing rates begin to climb in the 5%-15% range, in view of industry loss experience, particularly for certain sectors such as street/road contractors.

Risks that have had mediocre loss performance can expect to see increases of nearly 20%. On the other hand, contractors with good loss performance can expect flat to 5% increases since primary carriers are looking to retain high-performing accounts. Contractors with exposures on the more difficult end of the spectrum include those based in New York, residential/condo, and wildfire-prone. These contractors should expect to see the highest rate increases as well as deductible/SIR pressure.

Automobile Liability

As many underwriters watch their portfolios inch closer to a 100% (or higher) loss ratio, automobile liability continues to be a problem line. The reasons, which have not changed in the past three to five years, include: large losses, more litigation instead of pre-trial settlements, inflation, and distracted drivers (often by digital devices). Most underwriters are seeking increases of 10%-20% depending on loss experience, location, and fleet composition.

Workers' Compensation

The most stable of the primary casualty lines is Workers' Compensation (WC), with pricing increases averaging under 5% for a high-performing account. Most state manual rates are stable or declining. COVID-19 has had a minimal impact on WC losses in most states with California being the exception. That said, we will be closely monitoring any new activity from state lawmakers related to WC treatment of COVID-19 exposures for construction, as well as any new COVID variants. While the current rate environment is favorable, we will need to evaluate the impact of the pandemic on overall loss experience.

Long-term, WC is a sector of the construction insurance industry most likely to benefit from major advances in technology. That would include a corresponding favorable impact on loss experience, expenses, and rates. This comes as a result of technology advances on job site safety, employee medical treatment, and employment pre-screening.

Umbrella/Excess

Continuing to be a volatile line of construction insurance, 2021 will mark the third year of significant increases in umbrella/excess in order to offset loss experience as well as unprecedented underpricing and rising claim costs. Excess/Umbrella carriers continue to receive rate increases from their reinsurers along with reduced capacity, which translates to higher pricing for insureds with less limit. On lead excess placements, insureds should expect increases of 15%-25% – with some much higher depending on sector and experience. Carriers continue to mandate higher attachment points on the underlying policies.

We see no near-term improvement overall, which reinforces the need for a good partner with the ability to support a significant lead. Carriers are closely watching the terms they will agree to follow or provide aggregates, excess of wrap-up, and wildfire, to name a few.

For those contractors with substantial excess towers, you can still match, or nearly match, your limits from last year. But it will require a well-defined plan to scan the domestic (direct and wholesale) markets, along with markets in London/Bermuda.

Markets still willing to write on a lead excess/umbrella basis are increasingly very selective regarding capacity deployment, so we can't overemphasize the importance of working closely with your broker on how to make your submission stand out.

Builder's Risk/Property Insurance

The overall market experience for Builder's Risk/Property Insurance has been mixed, very much dependent on the underwriter and line of business. Throughout the property and contractors equipment marketplace, we are generally seeing some firming in this area, with rate increases of 5%-10%. The main driver has been reinsurer rate increases flowing down to the carriers writing the business.

The Builder's Risk market is segregated based on type of construction, location of project (CAT, coastal, etc.), and size. For projects comprised of fire-resistive commercial and industrial construction, the market remains very competitive leading to flat rates in this space. Domestic carriers continue to put out lead terms, with quite significant lines of capacity, as well as overseas markets providing capacity.

The habitational market, especially wood-frame risks, has been extremely hard for the last few years, with no signs of relief this year. Annual rates are averaging $0.50-$0.60 per $100 of project value. The main loss driver for all builder's risk carriers continues to be water damage, leading to higher deductibles.

Professional and Pollution Liability

Probably the two most favorable lines of coverage for contractors in 2021 (as they were in 2020) are Professional and Pollution Liability. With a favorable overall loss experience and ample support from underwriters, the market is robust, even with the entrance of new markets. The exception would be for contractors with large design/build projects, where the loss experience for the last few years has been poor overall due to significant large losses. As a result, we are seeing higher rates with additional scrutiny of design/build partners and project parameters for large projects. For professional and CPPI, we're forecasting rate increases in the flat to +5% range. For pollution, depending on loss experience, contractors with favorable results should anticipate flat rate renewals and even decreases in some situations.

Surety

The contract surety market remains stable and profitable largely due to the construction industry's "essential" status during the pandemic. However, underwriting scrutiny does prevail as underwriters continue to focus on backlog when considering future work due to the lack of skilled labor in the workforce. Labor was an issue prior to the pandemic and continues to be an emphasis, particularly as vaccine mandates and their legality have come to the forefront. These labor issues coupled with supply chain issues also have underwriters focused on project completion times along with other damages contractors could face. Contractors should focus on contract terms that allow for price escalations and adequate time to complete projects. Access to liquidity and debt structure continue to be important in underwriting, as the surety markets want to be confident that the balance sheet can absorb any problems.

Commercial surety results also remain strong. At the outset of the pandemic it seemed certain there would be significant losses stemming from the number of financial guarantee obligations in the travel, hospitality, retail, and energy sectors. However the surety markets so far have seen very few losses. We can attribute that to collateral requirements or the resiliency of these companies related to debt service relief, overhead adjustments (including workforce-related), access to capital, or a combination of all three.

Although overall writings have decreased over the last two years, there has been growth in the renewable energy space helping to fill the gap left by the other sectors. Similar to contract surety cash flow, underwriters are primarily focused on access to capital and debt structure.

Recommendations for Managing Better Underwriting Outcomes

Start the Renewal Process Early

COVID-19 has slowed everything down. It seems to take twice as long to get a burger at a fast-food restaurant, and the experience feels the same when it comes to insurance renewals. Plan ahead and start the renewal process up to four months before policies expire. Securing terms early from the incumbent market has proven successful as well.

Give Detailed Submissions

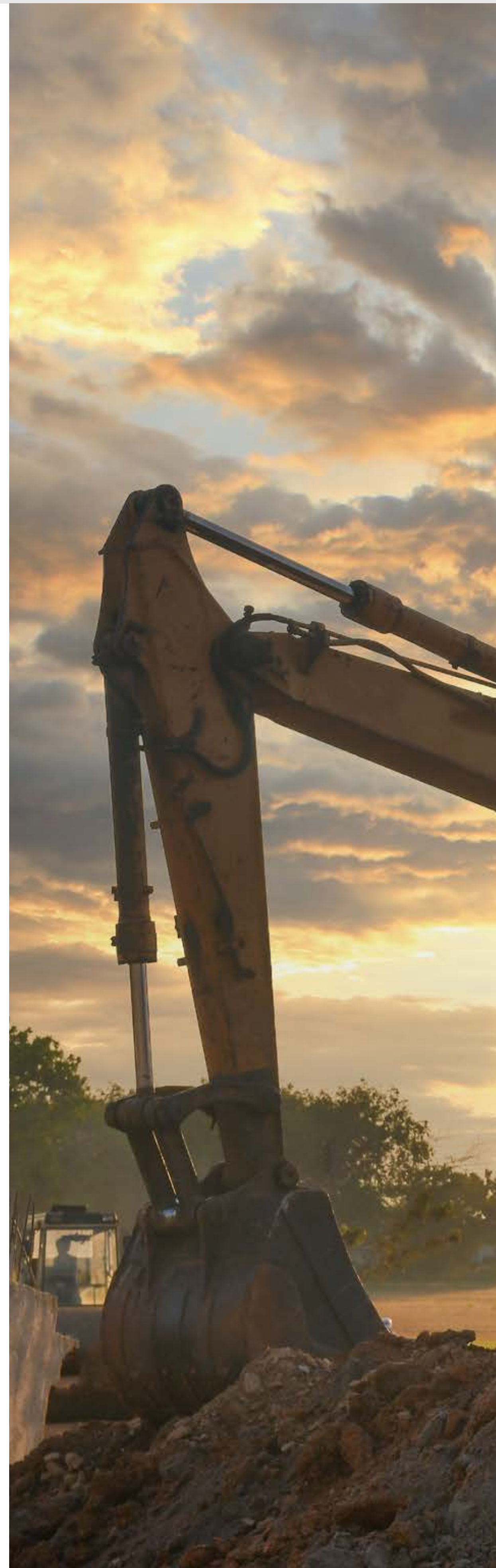
The underwriter's job is to price uncertainty, so the more quality information they have on your exposures, the more competitive the price will be. It is important in this environment to make sure the submission stands out from the others on the underwriter's desk. Be as granular as possible with information, from claims to project management.

Analyze Various Deductible Levels

Study your past claim history and create a loss stratification (this can be tasked to the broker). They will analyze what would have been paid out of pocket, and what would have been transferred to the carrier based on varying deductible levels. This will help select the best deductible option, as well as letters of credit demands from the underwriting community. Keep in mind that trading dollars with an insurance company rarely lowers your cost of risk.

Seek Your Primary Underwriter's Help on the Excess

This will significantly help manage your excess insurance cost. An underwriter receiving more premium from multiple casualty lines can be incentivized to reduce the lead umbrella/excess price. In the current environment, they view this as one way to remain competitive against other insurers. This isn't always possible or effective due to type of operations, underwriting appetites and venues for payroll; however it should be an option to explore as you test the market.



Review Contractual Risk Transfer Protocols

It is in the best interest of the contractor to manage the allocation of risk through contractual risk transfer, both upstream and downstream. Develop internal audit processes to manage this risk, and share them with underwriters. Contractors who manage this well typically get more competitive responses from the insurance market.

Safety Management First

The best way to reduce insurance cost is to reduce claims. The goal is to have several underwriters competing to underwrite the operations. One of the most important contributors to a contractor's safety management program is the engagement of senior management. Without that, nothing else works. Additionally, ideas to consider for fleet safety include geofencing, telematics, driver selection, education, and training.

Explore Different Risk Financing Mechanisms

Several risk financing tools may benefit a construction firm depending on a company's appetite for assumption of risk. Single-parent captives, group captives and segregated cells are available for consideration. Each of these financing tools has advantages and disadvantages, particularly when sharing risk with other contractors.

Don't Burn Bridges With the Underwriting Community

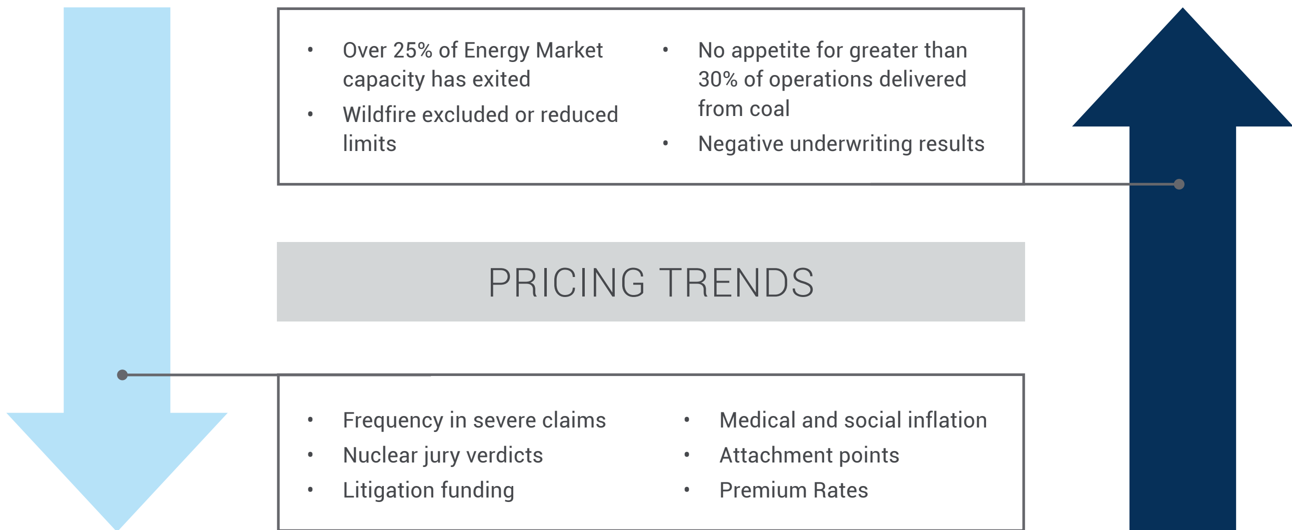
Relationships matter in the construction industry as well as the insurance industry. While marketing the program every year may feel like the logical thing to do, it often leads to only short-term gains that come with long-term consequences. And since turnover also affects the marketing process, be sure to cultivate multiple relationships with underwriters.

Energy & Utilities

Social inflation remains the hottest topic in the liability space as markets reckon with a higher frequency of severe losses.

Liability

According to a 2021 Chubb Bermuda report[1], loss costs have increased by 50% over the past decade. Due to poor results, nearly $100 million in capacity has left the excess casualty market for power and utilities since January 2020. Until we see significant new capacity, insurance buyers are likely to continue to face pricing pressure.



Since most power markets no longer offer California wildfire coverage, attention has now shifted to surrounding states. Insureds in western states should share fire mitigation and vegetation management efforts with their liability insurers in order to avoid sub-limits and exclusions for wildfire.

Have we seen the necessary market corrections that would allow for stability in 2022? We believe we are nearing stability but expectations for 2022 will come into sharper focus when treaty reinsurance renewals are complete and business plans have been submitted in the fourth quarter.

In order to keep up with rising severity, AEGIS announced at their recent virtual policyholders conference that they will be targeting an average rate increase of 10% across their book for clean accounts in 2022. After averaging close to 20% on rate for their book to date in 2021 this is welcome news. AEGIS also announced the introduction of a new policy form effective Jan. 1, 2022 that will incorporate a new cyber exclusion, with a limited BI/PD (contingent bodily injury and property damage) giveback, and a Protected Information exclusion. More information on the form changes will be provided to our AEGIS members directly.

EIM will provide guidance on their 2022 plans after their reinsurance renewal. We are hopeful that their 2021 demands (20%-25%) will be tempered, and that no further wildfire or coverage restrictions will be introduced.

Cedar Hamilton (NEIL) is up and running and looking to support members as a capacity provider. Wildfire is being reviewed on all accounts and Cedar Hamilton typically will not provide more than $25 million for any new excess liability accounts.

We think that London and Bermuda markets will be targeting rate growth between 5% and 15% on their renewal book, a marked improvement from 2021. This has been influenced by the introduction of new capacity and several years of increased rates. We will see differentiation here based on exposure type, e.g., thermal coal, wildfire exposed risks, High Consequence Area gas pipelines, etc.

The primary General Liability market has experienced tightening, although not as severe as the Umbrella/Excess market. While severity is driving rate for this coverage segment, the increases are predicated more on class of business and claim frequency concerns. Severity is typically capped due to total limits of $1 million to $2 million per occurrence and in the aggregate. Accounts without loss severity or frequency issues can typically expect increases ranging from 7.5% to 15%. Clients with perceived higher hazard products, premises exposure, or accounts with poor loss experience can expect higher rate increases and higher retentions. In these cases, alternative program structures (deductibles/retentions/captives/fronts) should be explored.

Property

A handful of shock losses in the power generation space have stood out in the property market so far this year. Three to four losses alone (domestic and abroad) are estimated to represent a value equal to 20%-25% of the global power premium spend of $2 billion to $2.5 billion. Rate increases had begun to temper to the high single digits before these losses materialized. However, the average rate increase for the third quarter of 2021 is in the mid- to high-teens.

Market capacity overall remains stable heading into the end of the year, though markets continue to tighten their Environmental, Social and Governance (ESG) policies. Key areas of focus for the remainder of 2021 and heading into 2022 include:

- Coal generation: As part of the “Unfriend Coal” movement, there is little appetite for operations that derive 30% or more of revenue from coal.
- Technology concerns related to LMS100, 7FA, and LM6000, among others.
- New and emerging technologies: GE 9FB, HA Stage 1 bucket, battery storage, fuel cells.
- Cyber: London and most U.S. insurers (other than AEGIS US) are providing limited resultant damage coverage for the perils of fire, explosion and machinery breakdown –this may come with additional AP to maintain.
- Pandemic-related challenges in the supply chain, such as obtaining spare parts and performing routine maintenance/inspections.
- Communicable Disease and COVID-19 exclusions
- CAT-exposed risks
- Wind and solar

We have seen an influx of capacity for renewables on the backs of insurance carrier ESG initiatives. The capacity has pushed average rate increases down below 20% after a couple of cycles of dramatic pricing corrections. While the shift is a welcome change from insurance buyers, some in the renewable underwriting community believe it is happening too soon. These underwriters also contend that the market has not reached a point of sustainability for the increasing reliance on renewable energy.

Severe convective storm losses continue to be a key issue for renewable insurers. Lightning strikes for certain wind turbine original equipment manufacturers (OEMs) have been particularly challenging from a frequency standpoint. Additionally, high-profile (Battery Energy Storage System (BESS) losses are challenging a market that is still in the early stages of developing underwriting guidelines for this emerging class of business.

It is best to engage insurers early in the BESS development process if possible since the market may have insight on both project design and OEM providers. We have seen the reemergence of No/Low Claims Bonuses and/or Long-Term Agreements in 2021, signaling some stability in the pricing models.

As always, financier/financier consultants have a significant impact of renewables insurance. We have recently seen emphasis begin to shift away from Full Replacement Cost natural catastrophe (Nat Cat) limits in favor of Nat Cat retentions.

As project values continue to increase, the percentage of total insurance value (TIV) language that the financier world has become accustomed to is keeping pace, resulting in significant risk retention on behalf of the project (often mirroring the project revenue itself.) New capacity in the traditional risk transfer space and deductible buy-down solutions will continue to serve as relief valves for the increasing deductible pressure.

[1]https://www.chubb.com/bm-en/chubb-bermuda-benchmark-report.html

Public Entity

Although public entities continue to see overall rate increases through most lines of insurance, we are seeing the market adjust and flatten to some extent. Carriers continue to limit capacity while tightening underwriting guidelines and policy terms and conditions.

We are also seeing more public entities agreeing to higher retentions and/or deductibles to meet budget constraints. As always, we are optimistic that the insurance market is peaking and that we will see rates stabilize by early spring next year.

Property rates, particularly in areas prone to wind and hail, have continued to rise with no immediate relief expected. Traditional events, such as hurricanes and hail, had their typical impact, while other less predictable black swan events, such as the February deep freeze in Texas, made matters worse. Public entities with poor loss experience or elevated exposure, such as coastal marine, continue to see higher rate increases. One emerging trend is policy language dealing with extreme temperature changes. Insurers want to make sure that, as much as possible, climate change is a factor in catastrophic CAT modeling.

Casualty rates continue to rise, as coverages are affected by events such as social movements, civil unrest and high-profile court cases.

Workers' Compensation rates are on the rise due to presumption laws for first responders. One emerging issue is centered on the question of COVID-19 vaccine mandates and how they could impact Workers' Compensation rates, or create a liability exposure.

Cyber coverage renewals are still on the rise due to the increased frequency and severity of data breaches. While $1 million in cyber coverage was considered to be generally sufficient not that long ago, entities are now requesting at least $3 million as a starting point.

Multifactor authentication (MFA) is now a must for entities seeking cyber coverage. Insurers also want proof that entities are conducting cyber training for their employees and have an incident response plan in place. Insurers are limiting capacity and reducing limits. Attacks on public entities, including a water treatment facility in Oldsmar, FL and the Metropolitan Water District of Southern California, show that public entities continue to be a major target for cyber criminals.

Public Officials and Employment Practices coverages are also seeing rate increases and a tightening of policy terms and conditions.

Underwriters are more likely to keep rate increases manageable for entities that are engaged and proactive with their risk management programs including:

- Collecting and providing detailed COPE data
- Maintaining loss control programs
- MFA processes for computer logins
- Disaster response plans
- Business continuity plans
- Social media response plans

Lower limits and higher deductibles/retentions are becoming increasingly common as public entities struggle to keep premium increases within their budgets. We are also seeing more interest in creative and strategic risk financing methods, such as parametric and aggregate stop-loss programs.

While entities that are part of risk pools have been somewhat insulated from large market fluctuations in the past, now even these entities are seeing an impact. Members in several of these pools have experienced significant losses and reinsurance issues.

Factors driving the hard market include CAT losses, inconsistent underwriter profits, mixed investment returns, market uncertainty, and the higher cost of reinsurance.

Additional Factors Include:

Natural Disasters

- The 2021 hurricane season ends November 30. At the time of publication, we have seen 14 named storms, with six of those developing as hurricanes (three were major hurricanes)
- Wildfires have increased in scope and size
- Tornadoes in the Southeast
- Extreme/severe weather (Winter storm Uri, Feb. 13-17)

Economic Climate

- Low interest rate on investment income
- Business interruption caused by the pandemic
- Supply chain risk
- Medical cost inflation
- Litigation
- Nuclear verdicts against insureds
- More class-action lawsuits

Umbrella Effect

- The increasing frequency and severity in Property, General Liability, and Auto claims is driving excess carriers to reduce capacity, restrict terms and conditions, and implement stricter underwriting guidelines
- Geographical locations are impacting excess rates
- Rising costs with reinsurance carriers

Legislation and Other Factors

- Presumption laws – pandemic and cancer
- Social justice movements, cancel culture, and civil unrest
- Black swan events (pandemic, power grid failure, ash cloud, supply chain disruptions)
- Discussions related to qualified immunity reform for police officers
- Increase in frequency and severity of cyber attacks (T-Mobile, Colonial Pipeline, SolarWinds, UTEP, Microsoft)

Real Estate & Hospitality

Overall, the Real Estate, Hospitality and Gaming industries are still recovering from the constraints of the property market over the last two years. Capacity has stabilized to some degree, but underwriters remain cautious when deploying it. This is not surprising given the increased frequency and severity of natural catastrophe losses since 2020 and the increased cost to rebuild, affecting all asset classes. These losses stem from Winter Storm Uri, around 21 additional severe weather-related events and the extreme heat, drought and wildfires in the Northwestern U.S. La Niña could also negatively impact winter weather across the U.S. in the coming months. Speaking of extreme weather, the National Flood Insurance Program ("NFIP") implemented a new rating methodology which will have a positive impact for a significant portion of buyers. The new rating will align more closely to the true exposure - coastal / beach front properties will most likely see a substantial increase while a majority of other lower hazard areas may experience a decrease.

Key Updates by Industry Segment

General Overview

Non-CAT: +7.5% to +10%
CAT/Poor Losses: +20% or higher

Hospitality & Gaming

Non-CAT: +7.5% to +15%
CAT/Poor Losses: +20% or more

Habitational/Multifamily

Non-CAT: +7% to +12%
CAT (with favorable loss experience): +12%-+20%
CAT/Poor Losses: +20% or more

Industrial

Non-CAT: +7.5% to +10% or more
CAT: +10% or more
High Hazard Risks: +15% to +20%

Retail

Non-CAT: +5% to +7%
CAT: +7% or more

Commercial Office

Non-CAT, Class A Office Portfolios: +7% to +10%
CAT, Poor Losses or Vacancy: +10% or more

Property

Given the challenges of the property market, clients may be surprised with the outcome of their program structure. Multiple insurance carriers may be needed for larger valued locations. Creative solutions, such as increased deductibles, quota-share arrangements or reduced excess coverage limits, may be needed to achieve the best possible results. Additionally, to ensure appropriate coverage limits/validate reported values, we recommend that clients obtain updated property valuations and replacement cost appraisals, to avoid over or under insuring. And, finally, despite a growing amount of case law favoring insurers, the market still lacks certainty related to COVID-19 business interruption claims.

Hospitality & Gaming

The good news is, the hospitality and gaming industry segment is rebounding after periods of vacancy and decreased occupancy. The bad news is the industry has not been immune to catastrophe losses and social inflation trends. Many hospitality and gaming clients are feeling the lasting impacts of recent water, mold and or fire-related losses, whether vacancy-related or not, sometimes to the tune of double-digit rate increases. To combat these obstacles and keep premiums manageable, hotel clients are opting for higher all other perils and water deductibles, some as high as $100K. Higher wind and hail deductibles are growing more common as well. This asset class has also proven a bit challenging, as many carriers are no longer taking on hospitality and gaming exposures due to the pandemic or are only doing so in a highly restrictive capacity. Additionally, some carriers have been less willing to add clients' mid-term additions to an existing program. Our goal is to learn as much about an incumbent carrier's appetite to determine, as far in advance as possible, whether an account needs to be matched with a better carrier-client fit.

Habitational/Multifamily

While other commercial property segments like retail, hospitality and gaming recover from the pandemic's economic impact, demand for multifamily housing has increased during the COVID-19 pandemic, and is forecasted to continue. But the habitational and multifamily industry segment has also seen increases in property insurance premium costs. Some clients have been surprised by double-digit percentage premium increases in Q3 2021, combined with carriers requiring insureds to take on more of the loss-related, financial exposure via larger deductibles.

Implications from the Surfside/Champlain Towers tragedy in Miami, Florida are having an impact on the Florida condominium market. Some markets are limiting capacity and/or instituting restrictions on coastal Florida buildings that are greater than 20-25 years in age, especially in the South Florida area. Most Florida condominium markets have begun to require a 40-year recertification for the South Florida condominium accounts. Florida clients are also seeing carriers shift from a Hurricane Calendar Year deductible to a Named Windstorm deductible and declining to provide coverage to properties with exterior insulation finish systems (EIFS) cladding/construction. Due to these challenges, Florida clients should be in the market early.

Multifamily clients are seeing a strong demand for single family rentals ("SFR"), and this asset class is attractive to owners given the potential for reduced property and tenant management. Some clients without large SFR portfolios, though, are experiencing a limited marketplace but new carriers are continuing to flowing into this space. While carriers may consider SFR exposure to have a lower attritional loss ratio (e.g. pipe burst affects one unit vs. multiple units) underwriters are still paying close attention to overall valuation and roof replacement costs.

Industrial

The industrial section has also fared well, economically, in the face of the pandemic. For the most part, in-person engineering inspections proceeded this year, allowing clients access to a broader marketplace, including more technical carriers. Supply chain issues have led to many clients to consider whether contingent time element coverage comes into play. Carriers are paying close attention to engineering recommendations, so clients in this space should ensure sufficient capital expenditures are set aside to make themselves as attractive as possible to underwriters. We also suggest getting engineering inspections completed as far in advance of renewal as possible, that clients correct easy to address and high priority items as soon as possible and that clients try to provide detail to underwriters to help show why overall market conditions shouldn't affect their particular risk. Clients who take these steps and who have complied with loss control and engineering recommendations are seeing better results in their renewals.

Retail

The retail segment was hit hard by the pandemic with many businesses losing customers. With some tenants backing out of leases, underwriters were concerned that vacancies might lead to unnoticed pipe bursts or other maintenance related issues. Landlords and tenants who are up and running again will want to ensure they have a proper building valuation (for tenants, this will be with a triple net lease) and that business interruption values have been updated and are evidenced by a business interruption worksheet as backup.

Commercial Office

Large commercial office space, especially Class A office portfolios, remain an attractive asset to underwriters due to lower incurred losses and stable rent collection rates. Insureds with loss or vacancy-heavy portfolios are seeing higher premium rate increases, deductibles and underwriter scrutiny. Owners/landlords should ensure they have sufficient business interruption/rental income values reported for proper coverage in the event a tenant is unable to occupy.

Casualty

2021: Q1-Q3

Type of Account	General Liability	Auto	WC	Umbrella/Excess Liability Rate
General	5% to 10%	5% to +10%	Flat to 5%	Middle Market: 10%-25% Risk Management: 20%-50%+
Bad loss experience/non-renewing incumbent	10%-25%	25%-40%	5%-10%	Middle Market: 25%-100%+ Risk Management: 25%-100%+

The real estate industry as a whole has seen steady casualty rate increases throughout the first half of this year, although not as steep as 2020. We expect the casualty market will remain firm for certain classes of real estate and hospitality. Capacity will continue to tighten, especially for umbrella/excess liability, throughout the remainder of 2021.

Losses continue to plague the industry, especially in the habitational and hospitality sectors. Lawsuits, nuclear verdicts and large settlements all show no signs of slowing, pressuring underwriters as they seek to increase profitability. In some sectors of the real estate market, carriers have maintained a limited underwriting appetite, reduced their capacity, and/or placed more restrictive coverage terms within their policies while increasing rates.

Higher casualty rate levels over the last couple of years have led to an influx of new carriers entering the real estate and hospitality sectors. While appetite remains limited overall, we believe this new capacity has slowed some of the severe volatility we have seen over the past two years, particularly for the umbrella/excess market, where 50%-100% increases were not uncommon.

We continue to see umbrella/excess carriers reduce their participation on the lead layer. Where an individual carrier would offer a $25 million lead umbrella limit in the recent past, they now will offer only $5 million, or possibly $10 million for the right risk. For all casualty lines of coverage, umbrella/excess pricing continues to be the most volatile for real estate and hospitality risks. As Programs/MGUs continue to restructure, low pricing continues to catch up with market pricing.

Habitational and hospitality risks are seeing the highest overall increases in the real estate sector. For insureds with good to average loss, these groups are experiencing the following rate increases on average:

- General Liability – 5%-10%
- Automobile – 5%-15%
- Workers' Compensation – Flat to 5%
- Umbrella/Excess – 10%-25%

Industrial and commercial office risks, while experiencing slight casualty rate increases on average, are not experiencing the type of rate volatility as the hospitality and habitational sector.

Coverage Challenges

In response to COVID-19, communicable disease exclusions are being placed on most casualty programs. COVID-19-related losses continue to wane, and the long-term financial impact related to these claims remains unknown for insurers. Some specialty "pandemic products" designed to provide coverage for losses related to any future pandemic (unrelated to COVID-19) have entered the marketplace.

Assault and Battery (A&B) coverage has been one of the largest challenges facing the real estate and hospitality sector over the past two years, due to concerns related to social unrest and increased claims. This is especially true for habitational and hotel risks, where insureds are facing lawsuits involving an incident on their premises, whether or not the insured was involved. A&B exclusions are becoming the norm for many carriers providing coverage for these risks, given the high cost (including "defense-only" coverage).

While General Liability (GL), Automobile and Umbrella coverage lines continue to see rate increases, Workers' Compensation (WC) insurance rates remain stable for the real estate industry, though we are beginning to see a negative impact on rates resulting from high severity issues.

Overall, underwriters continue to remain aggressive on WC pricing for insureds with good to average loss experience. For carriers that write primary casualty lines (GL, Auto, WC), many underwriters are writing WC coverage before they agree to offer a "competitive" quote for GL and Commercial Auto lines of coverage.

The overall casualty outlook for the real estate and hospitality sector as we continue in the fourth quarter is cautiously optimistic. As rates across all casualty lines continue a downward trend from the past two years, insureds should continue to provide detailed submissions and utilize analytics tools, when possible, to help differentiate risk profiles and exposures.

Businesses in this sector must evaluate their risk management and insurance programs, and engage with their loss control and claims experts (broker and carrier) to develop a safety strategy. And always communicate early and often throughout the renewal cycle to achieve the most favorable results.

Although we have seen some level of stabilization in the insurance market in the first half of 2021, several headwinds persist as we look to 2022. Among those challenges are the continued deterioration of the legal climate, labor and product shortages causing strain on the supply chain, and a very active weather season leading to significant insured losses. COVID-19 also continues to have a significant impact on the transportation industry, creating growth opportunities for those serving e-commerce channels and major challenges for other sectors.

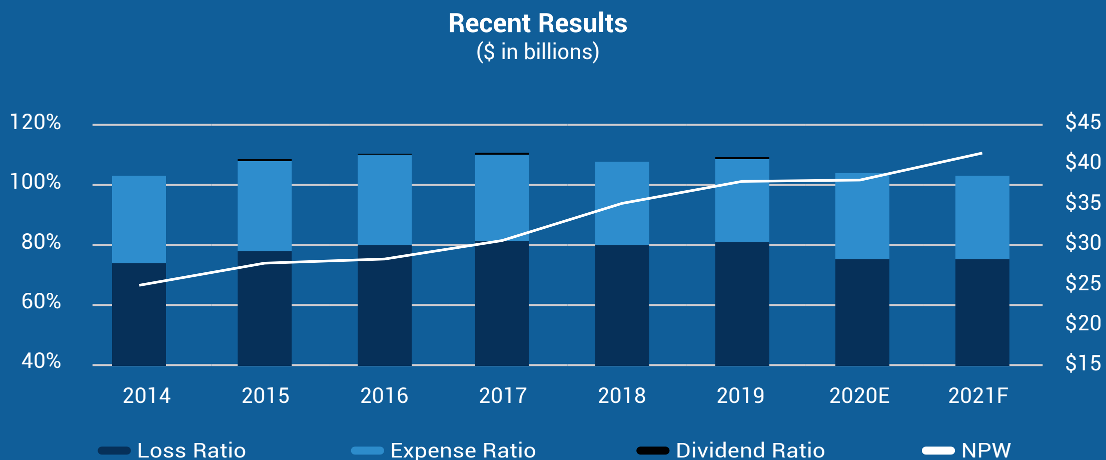
State of the Commercial Transportation Insurance Market

Following an optimistic spring when recovery seemed nearer than ever, the Delta variant has created uncertainty in recent months that will likely persist into 2022. Recent economic data indicates a slight pullback, with continued signs of a slowdown expected for the remainder 2021, primarily due to supply chain disruptions and the ongoing pandemic. The Fed is currently projecting an unemployment rate of 3.6% to 4% in 2022. That would be an improvement over 2021, but still above the 3% unemployment rate before the pandemic.

In light of the COVID-19 vaccine rollout and increased travel as the general population continues to resume pre-pandemic activity, we have seen road congestion – and accidents – continue to pick up, now resembling what we were seeing prior to the pandemic.

The insurance industry sector has been unprofitable for the past 11 years, despite significant year-over-year increases in the rating structure. To date, 2021 forecasts look similar to the expectations for 2020. However, since the industry has struggled to accurately reserve growth in loss severity, more time will be needed to better understand profitability for 2021.

Recent Results
($ in billions)



Prepared by Conning, Inc. as published in Conning's Property-Casualty Forecast & analysis by Line of Insurance, first -quarter 2021 edition Historical data source: ©2021 S&P Global Market Intelligence

Primary Automobile Liability

Commercial automobile liability underwriters continue to price their underwriting models to account for trend over the next year, from +5%-10% depending on the insurer. Trend is defined as the expected increase in claims costs year-over-year, which is primarily driven by an increase in medical expenses and continued deterioration of the legal climate. The Council of Insurance Agents & Brokers (CIAB) second quarter Commercial Property Casualty Index reported commercial auto rates up 6.8%, an improvement over the 9%-11% range from the previous four quarters.

Underwriters continue to place a major emphasis on safety technology, including camera- and telematics-based behavior coaching. Motor carriers that have yet to make these investments are seeing rate increases at exponential levels compared with their peers.

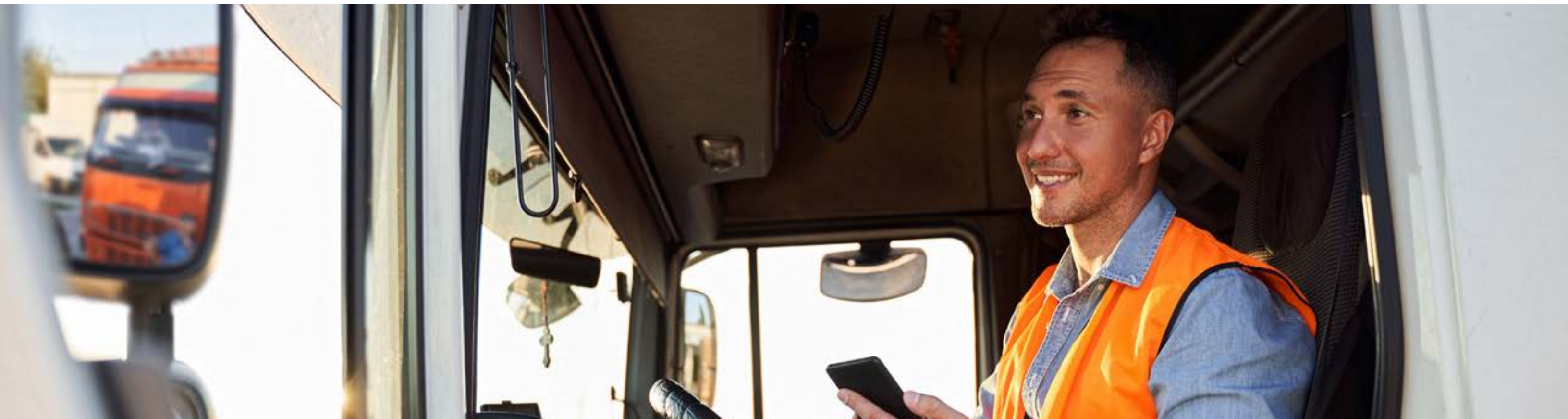
We anticipate rate increases of 5%-12% on average for the rest of the year. Insureds with challenging loss experience will likely see significantly higher rate increases while those with favorable loss experience will be closer to the average range. In addition to rate increases, underwriters are also pushing less profitable clients to alternative structures where they will have to take on more risk.

Excess Liability

Excess liability costs have continued to be a major issue for larger insureds considered to be targeted defendants. We have seen price softening for smaller and middle market insureds compared with what we were seeing over the first half of this year. Judicial areas of concern continue to include Louisiana, Florida, New Jersey, New York, Texas, Georgia and California.

As we predicted in in our spring market update, we have seen some new capacity enter the market. Carriers in London and Bermuda are deploying capacity above $10 million through creative alternatives to the traditional lead umbrella layer. Chubb remains the most common provider of $10 million in per occurrence capacity at the $10 million attachment point. However there are now more domestic insurers expressing interest in participating in this layer, given increase in rate per million over the past 18 months.

While excess liability pricing has continued to face pressure, rate increases are much lower than what we saw over the prior 12 months, varying by layer of risk. For risks with favorable loss performance, rate increases in the auto buffer layer (defined as the first excess placement attaching above the primary and before the umbrella) have been in the 10%-15% range. The remaining excess layer results, including the umbrella, have been as follows: umbrella and lead excess layers ($10 million-$30 million) have been generally contained at 15%; the next layer ($30 million-$50 million) at 10%; and above $50 million, flat to 5%.



Major Driving Factors

Nuclear Verdicts

In our spring Market Update, we covered what was, at the time, the largest truck accident verdict in history, at $411 million. A new record was set on August 20, when a Nassau County, FL jury issued a total of $1 billion in monetary damages against two motor carriers, AJD Business Services and Kahkashan Carrier, who were declared negligent for their role in a pair of 2017 crashes on the same night.

Both carriers no longer maintain active DOT authorities. AJD Business Services was absent during the proceedings and shouldered the bulk of the award, $900 million in punitive damages. While the majority of this jury award is unlikely to be collected, the impact on the industry will be considerable. We wonder if the plaintiff bar will use this case to argue that astronomical jury awards are acceptable.

The Stalled Court System and Litigation Financing

Insurers are keeping a close watch on the stalled court system, which is moving very slowly due to COVID-19. Virtual court cases are taking much longer than usual to litigate, creating a backlog of cases that will only begin to clear when courts are fully opened.

With courts moving slowly, litigation financing is becoming even more prominent. Litigation finance companies and law firms are investing in claims by paying claimants money up front in exchange for an interest in the ultimate outcome of their claim. This creates an environment in which a claimant is more secure financially and incentivized to leave open their claim. It also prolongs a claimant's need to settle.

The slowing court system and litigation financing creates uncertainty for insurers. Insurers and actuaries are valuing claims as best they can, but without an accurate pulse on the judicial system due to the stall, insurers are more likely now to miss the mark on claim values. Once the court systems fully reopen, if claims are settled or litigated at values higher than what has been reserved, insurers could face an unexpected adverse development. This is an issue that the insurance industry may face in the future. For now, insurers are watching the court systems, their reserves, and their premium rates to try to avoid this predicament.

Social Inflation

A growing issue in the insurance industry for years, social inflation has become more pronounced in the trucking industry in particular over the past 36 months. It's defined as an increase in claims costs due to factors such as more litigation, a broader definition of liability, plaintiff-friendly legal decisions, and larger jury awards. And we have also seen a growing disconnect between a claimant's actual financial loss and the compensatory awards coming from those juries.

While the headline-worthy nuclear verdicts capture the public's attention, it is the circumstances we mention above that have driven all claims outcomes up exponentially. Designed to compensate a victim for their losses, compensatory damages in our view too often punish the at-fault party with awards far higher than that.

Driver Shortage

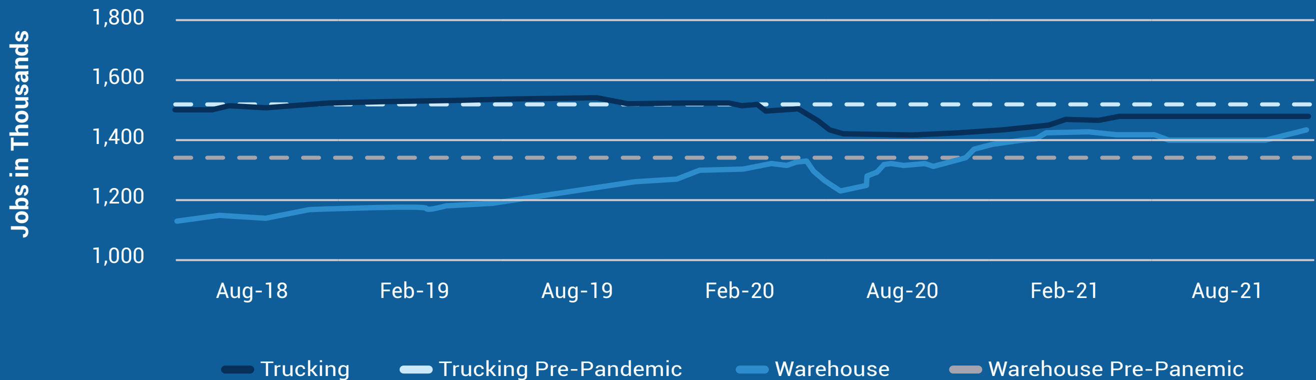
In our spring update we referenced an October 27, 2020 American Trucking Association (ATA) survey reporting the driver shortage as the primary concern of truckers in 2020. Not much has changed in the fall of 2021.

While the Federal Motor Carrier Safety Administration (FMCSA) reported that more than 45,000 drivers lost their jobs due to the implementation of the Drug & Alcohol Clearinghouse, many more have elected to retire or seek alternative forms of employment since the start of the pandemic.

Data from the U.S. Bureau of Labor Statistics show that trucking industry jobs are down 6.6% from prior to the pandemic. While those jobs are steadily coming back, the industry is also now facing a threat from the warehouse side of the business, which is attracting younger workers.

One negative effect of the driver shortage is that some trucking companies have become more lenient in their hires in order to keep up with customer demand, leading to a more dangerous workforce and eroding their safety culture.

Transportation Sector Employment Data*



*Data provided by the U.S. Bureau of Labor Statistics

Texas House Bill 19 (Tort Reform)

While the factors above all have negative impacts on claims outcomes, we have seen some positive movement in the past six months at the state level. Texas House Bill 19 (HB 19), which was signed by Gov. Abbott on June 16 and went into effect September 1, is a bill covering Class 8 trucks, delivery vehicles and rideshare passenger cars. Under HB 19, when a commercial vehicle owner or operator is sued after an accident, the driver would have to be proven liable in court before a case could be brought against their employer. The law also clears the way for other trial procedures, including a provision that will clear the way for more photo and video evidence, which previously was not always permitted in trials. While this is only a start, it's a positive outcome of the industry working together under the leadership of the ATA to support state trucking associations to enact change.

Workers' Compensation

Despite a 10% decline in premium volume related to the economic fallout from the pandemic, industry results remained strong. 2020 was the third consecutive year in which the industry has posted a combined ratio (CR) higher than 90%, according to Fitch Ratings, the measure of insurance company claims and operating expenses. 2021 is expected to remain a profitable year for the industry with combined ratios in the low 90% range.

According to the National Council on Compensation Insurance (NCCI), it received 45,000 COVID-related claims in 2020, representing incurred values of roughly $260 million (projected to grow to over $500 million). NCCI data on claims frequency of COVID-related claims – eight claims per 10,000 workers – is significantly below the 250 non-COVID related claims per 10,000 workers.

While the NCCI includes data from only 34 states, this shows the low loss frequency of COVID-related claims and how the insurance industry has been able to weather the pandemic and remain profitable. In addition, the severity of COVID-related claims has been minimal, with the NCCI reporting 88% of claims below $10,000. Uncertainty continues regarding long-term health implications from "long COVID" (post-infection symptoms that have lasted for a month or more) as well as more severe COVID-19 cases, including the potential for major organ damage and other chronic conditions that would ultimately increase Workers' Compensation costs.

The longer-term outlook of the workers' compensation market continues to remain a concern due to the long-tail nature of workers' compensation claims against several years of industrywide rate decreases and flat rate environments. Still, we see the renewal rates in the range of flat to +5% for the remainder of 2021 and into 2022.

Property

The property insurance market has continued to be a challenge as the industry works toward maintaining underwriting profitability. 2021 has seen significant catastrophic loss activity from winter storm Uri in Texas and the Southeast; numerous wildfires in the West; and the ongoing hurricane season, which is predicted to have 21 named storms, a 30% increase over last year.

In addition to the catastrophic loss activity, COVID-19 and the impact on the supply chain has increased the cost of construction from both a building materials and labor perspective. It is critical that property owners pay particular attention to their insured values from both a reconstruction and business interruption perspective because those expenses have risen dramatically. The length of construction time is much longer now also.

While the industry faced headwinds in the first half of 2021, we are seeing some stabilization with respect to rate increases. According to the CIAB second quarter Commercial Property Casualty Index, property insurance rates are up 9.9% on average, which is an improvement from the previous four quarters with average ranges from 12% to 14.2%.

Looking forward we anticipate rate increases in the 5%-15% range for clients with favorable loss history, best-in-class risk management, and established carrier relationships. Insureds with a poor loss history or viewed as high-risk could experience a rate increase of at least 25%, combined with increased deductibles and tighter policy terms and conditions.

Environmental

The U.S. environmental insurance marketplace through the third quarter of 2021 remains strong and stable with about $2 billion to $3 billion in annual premiums. Despite the pandemic, the marketplace continues to grow. Overall capacity is estimated at $700 million-$800 million depending on industry sector risk profile and who you ask.

Pollution insurance policies, which followed the Commercial General Liability (CGL) pollution exclusions of the 1970s, have evolved into a variety of different products. Two primary policy types are most frequently purchased: Environmental Site Liability (ESL), also known as Pollution Legal Liability, and Contractor's Pollution Liability (CPL), often combined with Professional Liability.

Other important coverages include Underground Storage Tank, Lender Liability, Closure Liability and combinations thereof. Environmental casualty products are also popular and used to fill gaps in traditional property and casualty coverage. These often heavily manuscripted policies provide very comprehensive, legally vetted, and proven environmental coverage, which has been invaluable to insureds for more than 40 years.

Even still, carriers continue to look for ways to modify or create new products to address changing needs stemming from regulatory requirements and public demand. Climate change, clean water and air, extreme weather events, biodiversity threats, and natural disasters remain major drivers of global pollution risk.

Current Market Climate

Environmental insurance products are offered today by many insurance carriers, each with different risk appetites, products, capacity, qualifications and financial strengths. In a very competitive marketplace, customized products are not uncommon.

As noted in our spring Market Update, Zurich discontinued their site liability product line, citing profitability issues. Very qualified markets have been filling the gaps with few outward impacts other than inconvenience.

Key observations of the current marketplace:

- Regulatory enforcement is increasing under the Biden administration, resulting in an increase in violations, fines, penalties, and claims (adding to an existing steady increase in environmental claims of about 15% per year).
- Social media and environmental activism is increasing awareness of pollution risks and leading to additional lawsuits.
- Pollution incidents are more frequent and more severe, often as a result of catastrophic events, natural hazards (e.g., flooding/water intrusion causing mold), infrastructure and pipeline releases, and new or poorly understood contaminant impacts.
- Carriers are very selective regarding the risk they will insure. For example, meaningful coverage for historic and operational coal mining or energy production is available from only two or three carriers. The same is true for upstream and mid-stream oil and gas pipeline operations.
- More and more carriers are protecting themselves from complex risks by layering – offering lower primary policy limits requiring multiple excess layers through other markets to achieve higher overall limits.
- We've seen some hardening of the market depending upon product type, generally in the 6% range. However, the hardening is also reflected by shortening policy terms and broadening exclusions or restrictions, rather than increasing premium.

COVID-19 Impact

Since carriers have not yet provided updates, we know little about COVID-19-related pollution policy claims (including number, status and settlements). Virtually all carriers now exclude COVID-19 outright, or by broad exclusions for communicable diseases, viruses or both. Some carriers, while broadly excluding communicable diseases, may provide coverage for decontamination costs.

Products

The two primary environmental policy types, ESL and CPL policies are summarized below.

1. ESLs are claims-made policies that generally cover the environmental liabilities of an insured's active business operations and those stemming from historic operations. An ESL policy (proprietary versions are offered by over 20 carriers) covers most types of regulated pollution releases or incidents. The ESL is location-specific and intended to cover liability for pollution at, on, under and migrating from an insured's real property. Coverage is often extended to a portfolio of sites, both domestic and international. Highlights of the ESL product include:

- The best ESL policies are usually heavily manuscripted by endorsement to obtain broader coverages and fewer exclusions.
- While generally similar in intent, differences in policy wording, terms, conditions and definitions vary from carrier to carrier.
- An ESL policy can cover liability to first- and third-parties for bodily injury and property damage, remediation (cleanup) costs and associated legal defense expenses. In the current political climate, the very important Natural Resources Damages coverage is available through an ESL policy. Available for both on-site and off-site exposures, these coverages can be offered for new (occurring *after* policy inception) and historic (occurring *before* policy inception) pollution conditions.
- Several enhancement coverages are available, including Non-criminal Fines and Penalties; Contingent Business Interruption; Illicit Abandonment; Property Diminution in Value; Underground Storage Tanks / Aboveground Storage Tanks; Mold and Fungi; Asbestos Containing Materials and Lead-Based Paint; First- and Third-party Transportation; and liability for wastes delivered to properly permitted, non-owned treatment, storage and disposal facilities.
- A standalone ESL policy covering risk associated with pre-existing conditions may be available for up to 10 years, although that is rare. Active operations coverage is usually limited to three to five years. Limits can be up to $50 million (higher limits are available by purchasing excess policies). Deductibles or self-insured retentions can be negotiated and limits (and terms and conditions) are not shared with other coverage lines, unless desired.
- Significant information regarding environmental conditions at the location(s) to be covered is usually necessary for the intense underwriting required for a comprehensive policy.
- These policies cover both gradual and sudden, accidental releases. Some CGL, Energy, Property, Auto, and other product lines will offer sudden and accidental coverage for pollution, but these are often sub-limited with coverage restrictions. Sudden and accidental coverage can augment the ESL, but is not an adequate substitute since many pollution incidents are complex in nature and gradual in occurrence.
- ESL policies can also provide substantial excess coverage above pollution indemnifications.

2

CPL is a very popular insurance product offered by over 40 insurers. It is designed to protect against third-party claims for damages caused by “pollution conditions” arising from an insured’s covered contracting operations, by or on behalf of the insured. The CPL marketplace is growing rapidly to keep pace with construction sector growth. A CPL policy in fact is now often required by contract. While there are fundamental differences between the CPL and ESL products, coverage and definitions are often similar.

- These policies are available as claims-made (less expensive) or occurrence-based forms. Occurrence-based is recommended since completed operations coverage is generally unnecessary (a claim can be made for an incident that occurred during the policy period after the policy expires), assuming the CPL policy term is long enough to capture possible latent defect exposures.
- The coverage can be provided on a project-specific or blanket basis for the insured’s overall operations.
- CPL coverage is a vital component of the insurance program for any contractor involved in construction or excavation activities.
- Limited coverage can be extended to the insured’s owned and leased properties for their covered operations.
- Transportation, Non-Owned Disposal Sites, Non-criminal Fines and Penalties, and Emergency Response are significant coverage offerings.
- Since consulting, contracting, design and field work performed by architects, design firms, engineers, environmental consultants and contractors can result in significant claims, CPLs are often paired with Professional Liability coverage.
- CPL coverage can respond to pollution conditions created by both current and completed operations. Long-term completed operations coverage (tail) can be added to the claims-made policy.
- Coverage limits are generally in the $5 million-$10 million range, although limits of $100 million and higher are not unusual for larger projects and may require excess layers offered by other carriers.
- A CPL can be structured within or outside of an owner-controlled insurance program or contractor-controlled insurance program. These programs provide coverage for subcontractors working under written contract on the insured’s project(s).
- As with the ESL, while generally similar in intent, differences in policy wording, terms, conditions and definitions vary from carrier to carrier.

Market Trends

We are seeing a number of marketplace trends or concerns, including:

- The World Economic Forum noted that the top five global risks are environment–related and contributing to catastrophic losses:
  - Extreme weather events
  - Climate change
  - Human-made environmental disasters
  - Biodiversity loss
  - Natural disasters
- As Zurich ESL policies expire, they will need to be replaced by policies from other qualified carriers. This can be a good opportunity to competitively solicit quotes from the several available qualified markets to improve or expand coverage. It's very important to involve other qualified carriers early in the renewal cycle to allow adequate time to underwrite potentially complex risks.
- Major claims are arising from per- and polyfluoroalkyl and perfluorooctane sulfonates (PFOS), used as stain and fire repellants. According to the U.S. Environmental Protection Agency, they can harm both humans and the environment.
- Glyphosate (Roundup) continues to be a concern, with several large class lawsuits pending or active.
- Asbestos in talc
- Claims are arising from 1,4-dioxane (a stabilizer in some chlorinated solvents) and ethylene oxide (a flammable gas used for sterilization, often in hospitals) primarily from air quality impacts.
- Microplastics and pharmaceuticals are garnering significant attention because of environmental impacts to marine and freshwater ecosystems and drinking water. It is unclear how the carriers will address these materials.
- Flame retardants, bisphenol A and phthalates.
- Because of real estate vacancies related to COVID-19, legionella and mold claims are rising significantly. Mold claims already have had a major impact on several markets.
- Brine water from oil and gas drilling and water treatment.
- Litigation is resulting from misrepresentation of policies with language more often related to exclusions than coverage.
- Transactional liability transfer program deals, particularly for energy companies divesting coal combustion residuals, are becoming more common.

Employee Benefits

The COVID-19 pandemic is still the overarching theme this fall for employee benefits costs and utilization patterns. We saw cost trends for healthcare start to tick upward in March, surpassing expected trend for the first time since early 2020. Cost and utilization for many services, including lab testing, behavioral health, and pulmonary-related services, has rebounded to pre-COVID levels. The increase in health spending in 2021 is due to the continuation of COVID-specific claims and the resumption of surgeries and inpatient claims that were put off in 2020 due to the pandemic.

The persistence of COVID-19 infection rates due to mutations such as the Delta variant, has made COVID-19 the top claim diagnosis based on total spend in 2021. What happens next with this trend will largely depend on two factors:

- New disruptive variants in the U.S.
- Vaccination rates among U.S. workers

54% **More than half of U.S. employers already have a COVID-19 vaccine mandate or are strongly considering one, according to a McGriff survey taken in September.**

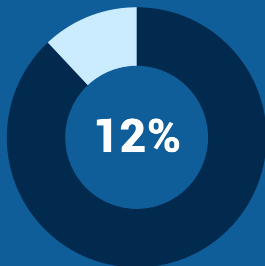
Ahead of President Biden's plan requiring about two-thirds of all American workers to get fully vaccinated or tested weekly, the McGriff survey shows that more employers were already leaning in that direction. In a previous survey in January, only 3% of employers said they were planning on a vaccine mandate.

The inaugural "Instant Insights" COVID-19 vaccine mandate survey revealed that 11% of the 315 employers surveyed had already implemented, or were in the process of implementing, a vaccine mandate.

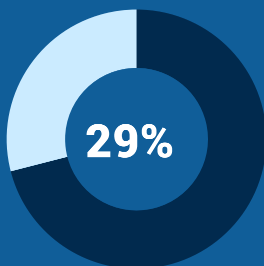
Companies still considering a mandate at the time of the Sept. 1 survey said that a significant increase in COVID-19 medical claims costs among non-vaccinated employees would be the most likely reason to move forward with a mandate (36%). Thirty-five percent of employers said an increase in local COVID-19 infection rates and hospitalizations would be their No. 1 decision-making factor. And 31% of respondents said an outbreak in the workplace would be the top consideration in making their decision.

The survey also found that at least 45% of companies are providing additional paid leave due to COVID-19 quarantines beyond normal paid time off. Many are beginning to make the paid leave contingent upon vaccination status – with 9% already doing so and 29% considering it.

Other key findings from the survey include:



of employers are either already providing an incentive to vaccinated employees or are planning to do so while 19% were weighing that option



of employers said they would not consider a vaccine mandate or surcharge/incentive policy under any circumstances. The most common reason cited was that the mandate did not align with company culture or beliefs (43%)

It remains to be seen how Biden's Emergency Temporary Standard regarding mandates and testing will be implemented, but there's no question it will have an effect on overall healthcare spending in 2022.

As we look forward to the end of 2021 and beginning of 2022, expect a few of these pandemic trends to stick around. One of those is the increase in the use of telemedicine. While telehealth utilization has tempered since the sharp increases we saw beginning in March 2020, the days of telehealth being an afterthought are behind us. The usage rate in 2021 hovered around 20-25 times pre-pandemic levels.

But so far, employers have been less sure what to do about it, with only 25% saying they've either already increased, or planning to increase, their emotional health or well-being programs this year.

Naturally, employers across the country are looking for ways to combat the emotional effects of the pandemic, such as burnout and a feeling of increased loneliness and isolation among their remote workforce. The focus for many employers will be developing offerings to address these mental health issues and making sure their employees know about them. The survey found that a majority of employers (64%) already have an Employee Assistance Program (EAP), but those who do not were not planning to add one.

The survey also showed that digital health coaching for mental health is gaining traction with larger employers – with 40% either already providing or planning to add it in 2021. Free access to well-being mobile apps is also gaining popularity, with 33% of large employers already offering them or planning to start before the end of the year.

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