Property Market Update

SUMMER 2022

Gallagher

Insurance | Risk Management | Consulting

How did we get here?

A REVIEW OF BILLION-DOLLAR NATURAL DISASTERS OCCURING IN THE PAST 5 YEARS.

As natural catastrophes continued to increase in frequency and severity, the COVID-19 pandemic engulfed the globe. Economic stimulus measures were quickly put in place, creating a near-zero interest rate environment As a result, carriers lost a stream of revenue in the form of interest-bearing investment vehicles. As carriers absorbed large losses, they were forced to play defense by both slashing the limit capacity they offer and charging higher premiums.

2017

- U.S. experienced 16 separate billion-dollar natural disasters, totaling $306 billion
- Tied for 3rd highest number of disasters, totaling $1 billion or more
- 3 tropical cyclones, 8 severe convective storms, 2 inland floods, 1 crop freeze, 1 drought and 1 wildfire

2018

- U.S. experienced 14 separate billion-dollar natural disasters, totaling $91 billion
- Tied for 4th highest number of disasters, totaling $1 billion or more
- 2 tropical cyclones, 8 severe convective storms, 2 winter storms and 2 wildfires

2019

- U.S. experienced 14 separate billion-dollar natural disasters, totaling $45 billion
- Tied for 4th highest number of disasters, totaling $1 billion or more
- 3 major inland floods, 8 severe convective storms, 2 tropical cyclones, and 1 wildfire

2020

- U.S. experienced 22 separate billion-dollar natural disasters, totaling $95 billion
- Highest total number of disasters, totaling $1 billion or more
- 7 tropical cyclones, 13 severe convective storms, 1 drought, and 1 wildfire

2021

- U.S. experienced 20 separate billion-dollar natural disasters, totaling $145 billion
- 2nd highest number of disasters, totaling $1 billion or more
- 1 winter storm, 1 wildfire, 1 drought, 2 floods, 3 tornado, 4 tropical cyclones and 8 severe weather events

2022: Present day

HOW DOES THE PAST FRAME THE PROPERTY INSURANCE LANDSCAPE FOR INSUREDS TODAY?

SCRUTINY OF SUBMITTED REPLACEMENT COST VALUATIONS

- Actual cash value endorsements
- Occurrence limit of liability
- Margin clauses
- Increased rate/premium

RISING/CHANGING DEDUCTIBLE STRUCTURE

- Percentage wind/hail deductibles
- Water damage deductibles $100,000+

LESS CAPACITY

- Large losses hit reinsurance carriers
- Increased cost for reinsurers is passed on to primary insurers and insureds

SUBMISSION COMPETITION

- Commercial insurers receive as many as 100 million submissions per year
- Underwriters require more data to work on submissions

ZERO TOLERANCE

- Carriers are showing zero tolerance for incomplete engineering recommendations
- Additional characteristics such as inspections, property condition assessments, and favorable carrier engineering reports are more important than ever

What does it all mean?

CHANGING RISK MANAGEMENT PRACTICES FOR INSUREDS AS DEFINED BY THE FACTS.

In response to such notable catastrophic events, carriers made frictional changes to underwriting practices, which insureds felt. While the market has indicated some signs of stabilization, insureds should heed the following to navigate the current property market successfully.

Carefully Review Replacement Cost Valuations

- Carriers have been burned by losses resulting from insureds who underreport values. This loss negatively impacts the market for all insureds. The latest example is an Indiana warehouse fire so large it could be seen from space. In the wake of the loss, some estimate that the building was undervalued by as much as $75 million.
- Carriers will no longer accept blanket 2%–3% increases on submitted statements of values. This change rings especially true as the May CPI shows inflation running at a 40-year high of 8.3%, significantly contributing to increased construction costs.
- Insureds who provide updated replacement cost valuations and show the methodology by which they were obtained will receive better renewal results than those who roll over old values.

Bifurcation of Riskier Assets From Clean Portfolios

- Insurers are taking note of the increased risk of loss due to so-called "secondary perils" such as hail, flood, tornado, and wildfire. Their increased focus has seen heightened water damage deductibles of $100,000+ and percentage wind/hail deductibles.
- Swiss Re reports that in 2021 the world saw a total $119 billion of insured catastrophe losses. Of the $119 billion, $8 billion were man-made catastrophes and $111 billion were due to natural catastrophes. 73% of the natural catastrophe losses totaling $81 billion were due to "secondary perils."
- Riskier assets contribute to the rate applied to a portfolio of assets. In some cases, it might be advantageous to break those assets into a separate program.

Submission Competition: Build an Attractive Submission

- PropertyCasualty360 reported that commercial insurers receive roughly 100 million submissions each year, as such underwriters are extremely selective as to which risks they are willing to work on.
- Insured can make their submissions more attractive by including:
  - » Cover letter summarizing the risk and opportunity
  - » Business continuity planning and supply chain details
  - » Property risk engineering summary, inspections, and property condition reports
  - » In-depth loss history, complete with description of loss, and what has been done to mitigate recurrence
  - » Detailed description of operations, products if applicable, and revenue attributable to each

An eye to the future

WHAT DO EXPERTS PREDICT AND WHAT IMPACT WILL IT HAVE FOR INSUREDS?

The predicted season continues getting longer for perils such as named storm, wildfire and severe convective storms. In addition to an expanded peak season, the geographies most prone to these types of loss are also expanding or shifting. Insureds should consult with their broker's property risk engineering units to adequately prepare for loss and mitigate circumstances that could give rise to a loss. Additionally, carriers often have in-house resources that can be engaged to improve an insured's risk profile.

WILDFIRE AND DROUGHT

- The University of California, Irvine stated that the annual burn season has lengthened, and the peak months have moved earlier in the season.
- The National Interagency Fire Center reports that year-to-date the U.S. is roughly 70% above the 10-year average of acres burned.

TORNADO/SEVERE CONVECTIVE STORM

- A Northern Illinois University study found that:
  - Severe convective storms accompanied by hail result in an average of $5.4 billion in damages each year in the U.S.
  - Tornado frequency is shifting its primary geography to the Midwest and Southeast, and away from the Central and Southern Great Plains.

HURRICANE

- The National Hurricane Center is considering moving up the official start of hurricane season by 2 weeks to May 15 due to seven years of "early-season or even preseason tropical development."
- NOAA predicts 21 named storms, six of which could become major hurricanes.

When considering the macro environment of the property insurance industry, Zachary Diamond, area vice president for Gallagher's Property practice in New York City, has observed that clients by and large continue to see increases and tightening coverage. The primary focus for underwriters from a macro perspective will continue to be the intense scrutiny of submitted replacement cost valuations.

Conversely, when we shift our focus to individual clients, underwriters are not applying blanket increases. Those who distinguish themselves from the group with data rich submissions to support their valuations are experiencing superior outcomes.

Carriers have created what Diamond refers to as a "micro-climate," meaning that pockets of favorable renewals terms exist for specific carriers who have begun to stabilize their book of business and realize profits once again. Those carriers that have been unsuccessful in securing meaningful rate increases and staving off continued large losses will continue to raise rates, premiums, and tighten terms and conditions.

Of particular concern is the potential for an active hurricane season. The National Oceanic and Atmospheric Administration (NOAA) once again has predicted an overactive Atlantic hurricane season. NOAA predicts up to 21 named storms, up to six of which could become major hurricanes. As the potential for major catastrophic natural disasters looms, Gallagher will continue to monitor the capacity carriers offer and the associated pricing.

The **CORE**360® Difference

CORE360 is our unique comprehensive approach of evaluating our clients' risk management program that leverages our analytical tools and diverse resources for customized, maximum impact on six cost drivers of their total cost of risk.

We consult with you to understand all of your actual and potential costs, and the strategic options to reallocate these costs with smart, actionable insights. This will empower you to know, control and minimize your total cost of risk, and improve your profitability.

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