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Business Insurance Market Conditions and Risk Dynamics

H2 2023 Australia

Gallagher

Insurance | Risk Management | Consulting

This report provides an update on current insurance market conditions and the primary risks your business may encounter.

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2023: Risk and Market Dynamics Shaping the Closing Half of the Year

A trend of uncertainty with upside continues

While there is an emerging upside in the current market, premium increases and extended timelines to resolve more complex claims continue, and this trend is expected to continue into the opening half of 2024, and potentially longer. There are a number of steps that can be taken when reviewing your insurance arrangements to make changes to the way your business continues to manage its risk exposure appropriately, while continuing to move forward with your future plans.

It's all about relationships

Your insurance broker is a trusted partner working with you to build a commercial relationship with insurers. With change and periods of disruption, taking a refreshed approach to risk management supported with a strategic placement solution, your broker can help you to achieve better outcomes from insurance renewal discussions.

No one can tell the story of your business better than you. Regular communications with insurers and their underwriting team deepen their understanding of your business and brings them closer to your future ambitions and to where risk management recommendations can help.

At Gallagher, we pride ourselves on our in-house expertise and the strength of our global relationships. We look forward to continuing to help with innovative and tailored insurance and risk management solutions.

02 EXECUTIVE SUMMARY

Welcome to the H2 2023 edition of Business Insurance Market Conditions and Risk Dynamics, providing an overview of the insurance market dynamics and in-depth perspectives on the key risks faced by Australian businesses.

While the business insurance market remains challenging in specific areas, signs of annual premium increases steadying for certain types of risk and with broader coverage options becoming available give cause for a degree of optimism. Responding to insurer recommendations and implementing risk management processes continues to be viewed positively by insurers for renewals and helpful in achieving better outcomes.

For industries with higher exposure to risk, including waste recycling, hazardous materials and commercial properties located in areas more prone to flooding and bushfires, the insurance market remains tight and insurers are selectively underwriting risks that fit their appetite.

Upward pressure on premium prices continues due to a variety of factors, and the hard market cycle remains, albeit with some easing. Inflationary and interest rate movements continue to dampen growth plans across Australian industries and sectors. Supply chain bottlenecks are now starting to ease, although suppliers remain challenged by restricted access to labour and specialist skills in some spaces. El Niño and the continuing round of extreme weather events add to the dynamic of rising reinsurance costs and a tighter property insurance market.

Current position – September 2023

A flow of premium investment into the Australian insurance market has been influenced by underwriters and insurers becoming more comfortable with businesses that are able to demonstrate improved risk management practices and provide comprehensive insights into their business.

A two-speed market continues to be characterised by a challenging property underwriting environment and, in contrast, general improvements for cyber insurance where premium increases have started to level off as more capacity becomes available. Ongoing rate and market adjustments impacted by inflationary pressures will continue to define how the market travels longer term.

Market and risk dynamics at this time include:

- Uncertainty and cautious optimism as inflation, capital market volatility and skilled labour shortages dampen otherwise improving market conditions.
- Increased competition amongst insurers to provide insurance for businesses that demonstrate robust risk management, with those businesses more likely to achieve the best possible outcome on premium price and product coverage.
- A challenging claims environment marked by slower decision-making and referrals to third-party claims specialists to settle complex claims.
- ESG activism on the rise, with Australian regulators placing closer scrutiny on green credentials and a number of legal cases already underway following Australian Securities & Investments Commission (ASIC) notifications and the potential of heavy fines where greenwashing is claimed to have occurred.
- An increasingly mature cyber risk market, reflecting data and technology risks being generally better understood, attracting more insurers and premium into the Australian insurance market.

Expectations for the next 6–12 months

Current trends are likely to continue in the months ahead, alongside early signals of market improvement for selected risks as insurers provide capacity opening up more premium. In addition, other trends that may emerge or continue include:

- Inflation and interest rates falling from mid-2024 and into 2025.
- Property continues to be a challenging risk in Australia with tighter underwriting criteria and deeper scrutiny of occupancy, with particular focus on the way the business premises is used and neighbouring properties involved with higher risk occupations (e.g. flammable materials, waste recycling) and ensuring valuations are aligned with the current market and factoring in inflationary impact on building material and construction costs.
- Underinsurance concerns will continue, motivating a closer partnership between business owners and insurance brokers to ensure premiums and the scope of coverage values remain up to speed with the market.
- Aside from ongoing signs of insurance market improvement, premium increases are anticipated – although at lower growth rates than in 2022, and with any declines remaining above pre-pandemic levels.

Critical factors affecting the current pricing and availability of insurance cover

Up-to-date valuations, claims history and risk engineering reports will help to secure the best possible terms.

Implementing risk recommendations will generally be viewed as a big positive by underwriters in the current market.

Cover restrictions and reduced limits for more challenging risks – natural catastrophe, professional indemnity and cyber.

Property occupancy, including that of surrounding properties, will affect pricing and capacity.

Risk dynamics at a glance

CYBER

- As the cyber insurance market continues to open up in Australia, new insurers are entering the market.
- Tighter focus on assessing IT and cybersecurity management, including action to resolve data and supply chain vulnerabilities.
- Artificial intelligence (AI) and a new wave of digital technology innovations are opening up new routes to cyberattack, with attacks becoming increasingly sophisticated and challenging.

CLAIMS

- Underwriters are displaying significant risk aversion, increasingly looking for third-party legal and specialist risk advice to determine the outcome of more challenging claims.
- Upward material and labour cost movements, as well as supply chain bottlenecks, continue to cause timing delays for essential repairs and replacement of machinery and equipment.
- Risk analysis and evaluation using data continues to be explored as a way to reduce rising claims costs.

PROFESSIONAL AND FINANCIAL LIABILITY

- A renewed sense of confidence marked by greater premium stability following the introduction of new local insurers and competition from the London market.
- Insurers willing to consider coverage enhancements, including some that were removed in the hard market.
- Regulatory risks continue to pose challenges for companies and their directors, particularly in the ESG space.

WORKPLACE RISK

- Increased workers' compensation claim amounts and durations are hiking pressure on employers.
- Parliamentary moves continue to tighten eligibility rules for claims; but employers' regulatory obligations to identify mental health risks remain.

D&O

- Renewed market optimism with stabilisation of premium rates.
- Insurer competition is ramping up for well-managed accounts, including the introduction of new global insurers into the local market.
- Consideration is being given to the purchase of coverages such as Side C that were unavailable or uncompetitive in the past few years.

PROPERTY

- Up-to-date surveys and valuations have heightened importance, with some insurers limiting cover via coinsurance clauses, deductibles or indemnities.
- Increased scrutiny on the occupancy of neighbouring property by insurers is leading to an increased number of declines where the use is outside commercial appetite.

KEY TRENDS:

- Competition amongst insurers for quality risks is increasing, and new capacity is entering the market both locally and overseas.
- Businesses have greater control over how they structure risk, including the use of alternative risk transfer solutions.
- Uncertainty remains despite good trading conditions amid the volatility of wider pressures such as inflation and labour shortages.

A More Positive Outlook for Buyers as Capacity Returns and Insurer Competition Increases

Insurance premiums are showing signs of steadying across most commercial lines as insurer capacity continues to increase both in Australia and international markets. The focus is shifting from price to cover, with businesses becoming more involved in their renewal process.

Capacity/Market:

Gradual increase in options and control for businesses

The first half of 2023 saw an increase in confidence in the insurance market following several years of significant premium rises and challenging market conditions. It's clear there is a direct relationship between improving risk management profiles and the increase in underwriter appetite.

Capacity in the Australian market for businesses with quality risks is returning following a trend of declines since 2020 where insurers exited certain markets to avoid high losses. This is leading to increased competition and a shift in the market dynamic, particularly from London and Singapore markets which now present a new opportunity, and in some cases offer better pricing, especially on hard-to-place risks.

Overall, there is increased stability and more competition, with premiums in most commercial lines beginning to show signs of levelling out. It is no longer the norm for insurers to dictate their terms – with more options available, there is renewed control over risk placement.

Global pressures continue to impact the insurance market

Alongside a more positive outlook comes a degree of caution as global pressures such as inflation, interest rate hikes, ongoing supply chain bottlenecks and labour shortages continue to influence markets.

The property insurance market globally continues to be challenging, including in Australia, partly driven by natural catastrophe and extreme weather events and also due to ongoing inflationary pressures that continue to lift material, labour and construction costs. Insurer appetite remains restricted, with higher deductibles, reduced terms and a narrower scope of coverage being offered.

This has added to the challenge for insurance advisers and risk managers who are being asked to communicate why premiums have risen considerably in recent years and to manage a sense of 'rate fatigue' for businesses facing year-on-year premium increases. This has prompted a revised outlook on insurance program design to determine the most suitable options for businesses – this could involve rethinking capacity or considering alternative risk transfer structures such as captives or parametric insurance.

There has also been an increase in using insurance-linked securities (ILS) and captives within their programs to stabilise costs. With the option to rent cell captives, this can provide an opportunity to review the current placement strategy.

Risk spotlight: A focus on cover, not just price

With heightened focus on renewal strategy, there is more awareness of the need to better demonstrate risk management, as well as ensuring claims history is well documented. This is especially important in harder market conditions.

As the market becomes more competitive, insurance considerations are moving away from price and becoming more focused on cover. This will prove particularly important for more challenging risks such as natural catastrophes, professional indemnity and cyber. This is where broker expertise can make the difference, and a more strategic focus on placement will be integral to renewal discussions.

The anticipated deadline approaches for climate-related financial risk reporting to become mandatory, and with it attention needs to turn to climate targets and how to accurately present them to avoid the risk of facing greenwashing claims and potential fines. As such, insurers are starting to ask for demonstrable commitment to ESG as part of their insurance submissions. Now is the time to prepare for this impending regulatory requirement.

RISK STRATEGY IS AS IMPORTANT AS PRODUCT COVERAGE

It's critical to understand the coverage being presented by the insurer and begin the renewal process between three to six months in advance, answering all the prior year's recommendations.

Demonstrating robust risk management strategies is more likely to achieve a better outcome on premium price and product coverage due to higher insurer competition for quality risks. Structuring an insurance program to achieve the best possible outcome and being able to explain why any changes have been made, to either reduce the scope of the insurance and/or reduce the cost of insurance to the business, is of heightened importance at this time given the more challenging economic climate and trading environment.

KEY TRENDS:

- Underwriters are increasingly deferring decision making on more challenging claims, and seeking advice from specialist, third-party claims assessors.
- Businesses need to take extra care to ensure assets are correctly valued to avoid claims settlement issues.
- A more sophisticated application of data is helping to minimise business disruption when a claim is undergoing review, improving resolution timelines and as a claims prevention tool.
- ASIC clamping down on ESG corporate statements with regulatory requirements has led to fines and broader repercussions amidst claims of greenwashing, and D&O claims may occur.

Supply Shortages and Significant Weather Events Drive Up Claims Inflation Rate Leading to Underwriter Risk Aversion

The current insurance market is experiencing one of the most challenging periods ever with significant claims events on the rise. A risk-averse approach from underwriters necessitates greater risk management vigilance by businesses.

Capacity/Market:

Risk aversion and rigid decision making

The Australian claims market is witnessing unprecedented challenges with major claims events and supply shortages extending claims resolution timeframes. There are a number of reasons for this ranging from the longer term impact of the COVID-19 pandemic creating heightened uncertainty regarding the scope of business interruption coverage through to higher claims cost and the harder market cycle.

Insurers are seeking external legal opinions for claims that were previously decided internally as greater scrutiny is being applied to claims assessments. This raises challenges where decision makers and legal teams located outside of Australia may struggle to grasp the nuances of the local market, leading to rigid decision making.

With lengthened claims resolution periods, monitoring and managing indemnity periods is vital for ensuring business continuity during unplanned downtime or disruptions. Understanding how to assess the necessary indemnity period for insurance coverage is crucial, especially for events involving building repairs, maintenance, or reconstruction. In those situations, business interruption insurance needs to reflect the extended periods of coverage required for non-functioning operations due to maintenance or supply delays.

Risk spotlight:
Finding the value in data

There are now moves to leverage extensive data to reduce future business disruption and downtime impacts, particularly in the transport and property sectors. The aim is to reduce the volume of claims and the severity of losses relating to standard business claims outside of extreme weather and catastrophe type events. Telematics is gaining popularity in the transport sector to build a better understanding of patterns and risk exposures for businesses. Data capture points on new claims are collated and analysed, which will help firms to consider how claims can be reduced.

Risk engineering to improve hazard identification and risk evaluation is also being explored as a scientific method to help with loss mitigation. Although this has primarily been an area that large corporations have embraced, the mid-market sector can benefit from applying risk engineering methods to improve risk assessments, particularly in flood or natural-disaster-prone areas.

New risks as floods become fires

The transition from La Niña to El Niño signals a positive change for the Australian market, with the former often leading to floods, rainfall, and extensive storms, causing havoc particularly to infrastructure built on flood plains. However, the drier El Niño brings its own challenges from dry weather and higher bushfire risk.

Steps to ensure greater claim success:

- Follow risk recommendations from your broker and the insurer.
- Get a claims expert involved in renewal considerations.
- Maintain correct valuations to avoid underinsurance and under-declaring of property and asset values.
- Be vigilant regarding indemnity periods.

INSIGHT INTO THE CLAIMS MARKET IN SPECIFIC SECTORS

Transport: Over the past six months, the transportation and logistics sector has seen an 8% increase in repair costs, and total loss settlements have sustained a significant 17% rise. Supply and demand challenges to resolve claims (such as parts and repairs) present a major issue. Due to the lack of parts availability, insurers are displaying a preference for settling claims as total losses rather than repairs, particularly in the commercial vehicle sector.

Moreover, amid inflationary and market pressures, be mindful to avoid under-declaring units and asset values.

Construction: Due to a backdrop of year-on-year construction material pricing increases and with the supply of skilled labour being restricted, and with higher wage expectations, project costs have significantly increased. This has resulted in higher claims pay-outs.

05 PROFESSIONAL & FINANCIAL RISKS – D&O

KEY TRENDS:

- **Premium rates have stabilised and in many cases reduced, although not to the lower levels seen five years ago.**
- **Competition is increasing amongst insurers, with a mixture of incumbents and new entrants vying for territory.**
- **Premium volume has not grown as expected, partly due to businesses reducing their limits, increasing their retentions or removing coverage.**
- **Regulatory risks continue to pose challenges for directors, particularly in ESG and greenwashing.**

Negotiable Premiums Provide a More Favourable Market for Companies Seeking D&O

A rebalancing of market dynamics brings a renewed sense of confidence for directors and officers' insurance. Premiums remain negotiable amid increasing competition and innovation in the professional & financial lines market.

Capacity/Market: Confidence increasing

The D&O market shows renewed positivity after a prolonged three to five year trend of premium price increases and tighter underwriting. As insurance incumbents and new players vie for space, increased capacity and competitive conditions characterise the market.

Premiums have stabilised at levels relative to risk

D&O discussions now centre on adequacy, given ongoing market changes and insurer shifts. Some insurers may offer reductions in premium amid limited premium volume caused by companies reducing limits or increasing retentions or coverage, due to pressures from prior years.

Looking ahead to the next six–12 months, it may be premature to predict further softening in the market, and the generally held view is that companies and insurers will test the adequacy of premiums relative to risk.

The conversation has shifted from whether the D&O premium is going to increase or decrease and now focuses on whether the premium adequately covers the scope of the risk(s). This is due to the many changes the market has been seeing: insurers changing positions on programs, new entrants into the D&O market, and supply and demand challenges. Some insurers feel justified in reducing their premiums or meeting a level they were previously unable to serve.

Captives offer a potential short term solution for harder to place D&O risks

Interest in alternative risk transfer platforms is rising in the current market, driven primarily by the desire for increased control over risk pricing and structuring of certain risks. In harder markets a short-term cell captive rental has offered respite during an insurance crisis to essentially ride out a period of time when the market has a reduced appetite to underwrite a specific risk. This option was favoured over traditional captive approaches that generally involve a longer time period to set up and are geared towards structuring risks with a longer term perspective. As market conditions have settled, captives are being considered to manage the cost of funding very significant self insured retentions or risks that are either not transferred to insurers or not accepted by insurers. Companies can take advantage of favourable market conditions to establish a captive on their own terms, and with the benefit of optionality.

Risk spotlight:
A sharper focus on regulatory risks

Regulatory risks will continue to present challenges for companies purchasing D&O insurance. Key concerns for directors in the professional and financial risk space include cyber resilience, anti-money-laundering compliance, ESG and greenwashing. Disclosure is the common thread running through, and insurers are looking for evidence of compliance with greater scrutiny.

A crackdown on greenwashing has seen regulators impose financial penalties, including high-profile cases that saw fines against ASX-listed Tlou Energy in October 2022 for carbon footprint statements concerning electricity and gas projects found to be ‘factually incorrect’, and investment management company Vanguard Australia in December 2022 for overstating the extent of investment screening for preventing tobacco company investments.

While the fines were paid in compliance with infringement notices that did not constitute an admission of guilt or liability, these actions are a clear statement of intent by the regulator to put directors on notice. The first court proceedings alleging greenwashing were launched against Mercer Superannuation in February 2023 concerning the accuracy of sustainability-related claims.

Climate-related financial risk reporting looks set to become mandatory in Australia in 2024, emphasising the greater need for directors to examine their climate risk exposures.

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DO YOUR D&O DUE DILIGENCE

Despite evidence of improving D&O market conditions, preparing for renewal and engaging with the insurer will be key to achieving the best possible outcome at renewal.

Consider more than just an insurer’s security ratings. It’s important to assess the track record in the specific product line, claims handling expertise, prudential regulation, and overall reliability.

Education and Risk Awareness Take Centre Stage as IT Security and Breach Response Resilience are Prioritised

Rate stabilisation and increased capacity are redefining competition in cyber, with the increasingly mature market recognising businesses that follow best cyber security practices.

Capacity/Market:

Increasingly mature market shifts towards stabilisation

During H1-2023, the cyber insurance sector has experienced a notable shift characterised by stabilisation and, in some cases, reduction of premium rates where robust cyber risk management is being practised and can be demonstrated. Insurers have expanded their capacity, which has been vital for retaining business against intensified competition and a more mature cyber market.

Government regulation is now sharply focused on Australia's cyber security risks and need for comprehensive risk mitigation controls, emphasising cyber awareness education, deeper understanding of risks and insurance implications. Businesses and operators in any space are required to embrace cyber compliance and active vigilance against known threats in real time.

There is no longer a push for alternative cyber placement strategies, this shift is primarily due to insurers offering improved premiums and a commitment to long-term partnerships. The evolving cyber insurance landscape prioritises business protection where enhanced IT security and resilience frameworks are actively in place.

This contributes to avoiding cyber policy restrictions and provides stronger protection for businesses generally.

KEY TRENDS:

- **The market is now increasingly mature, attracting more insurers to participate in new and emerging opportunities.**
- **It's essential to demonstrate cyberattack preparedness, including response protocols and proactive defence and recovery tactics.**
- **Previously looking at the cyber security of the business perimeter, insurer focus now extends to identity access management, privileged access management and supply chain vulnerabilities of business infrastructure, including how third party vendor risks are managed.**
- **The implementation of the Australian Cyber Security Strategy demonstrates the government's commitment to rolling out world-class cyber best practices; government stakeholder management is now a key concern, especially where a breach has 'national significance'.**
- **Company boards are now alert to cyber risk, and a cyber-specific risk management framework is high on the agenda, particularly given the evolving regulatory environment.**

Risk spotlight:
Organisations now regard ransomware as inevitable

Healthcare, manufacturing, and financial services have continued to be the primary targets for cyberattacks, with hackers focusing on highly data sensitive sectors and attempting to disrupt essential services. There have also been a number of attacks targeting government agencies. The primary attack vector across both private and public sectors continues to be human-phishing emails, which are responsible for around 97% of attacks.

In the opening half of 2022 there was an expansion in the number of sectors required to adhere to the *Security of Critical Infrastructure Act 2018* from four to eleven. Top executives now face increased pressure to establish strategies and risk management practices to gain the regulator's confidence.

Ransomware continues to be the most prevalent cyber threat to organisations globally. It's now considered a very real likelihood that a business will be a target of an attack, and insurers want evidence of detailed response protocols, proactive defence, and recovery tactics. The question boils down to: "How prepared are you?"

Carriers view businesses with superior cyber supply chain diligence positively

Businesses implementing robust cybersecurity measures are more likely to have a range of insurance options and improved terms on the table for consideration. Cybersecurity needs to factor in supply chain related risks, acknowledging the interconnected technology platforms, invoicing and purchase ledger through to order placement and logistics, that have points of vulnerability and heightened exposure to system hacking and data theft.

Insurers now extend their focus beyond company perimeters, ensuring supply chain partners maintain matching security standards. Audits and strict protocols ensure vendor alignment with business maturity levels.

Cyber risk programs are now an expectation

Following a surge in phishing attacks, businesses are increasingly investing in more sophisticated cybersecurity tools and risk awareness and education programs are becoming standard practice across multiple industries.

AUSTRALIAN GOVERNMENT PREPARES FOR THE FUTURE

AI developments have enabled more sophisticated communication through business email compromise, making scam detection more challenging.

Meanwhile, the threat of cloud outages carries substantial financial and reputational risks. Whilst many delegate security to third-party providers, it has become clear that there is a need to continuously educate on evolving security controls. Australia's Minister of Cyber Security is ramping up the implementation of the Australian Cyber Security Strategy to help achieve the government's vision of making Australia the most cyber secure nation in the world by 2030, backed by appropriate levels of public investment. All associations, regulators and businesses are urged to align so that Australia is best positioned to respond to the opportunities and threats of the digital age.

To comply with cyber strengthening, penalties for repeated and serious data breaches have significantly increased. Government, insurers, and the community demand robust data retention and destruction policies to mitigate data breach impact, whether accidental or malicious.

KEY TRENDS:

- Renewal premiums remain high as inflationary pressures continue to impact the sector.
- A greater number of property risks are being declined than previously, with increased rates applied.
- A rising volume of natural catastrophe and extreme weather related claims have led to market pricing adjustments and reduced capacity.
- Business interruption indemnity periods should be reviewed for rebuilding or property reinstatement to ensure that the stated time period factors in ongoing supply chain delays and elevated construction, material and labour costs.

Increased Rates and Variable Capacity Are Becoming the New Norm

The commercial property insurance market remains challenging, with rate increases at renewal broadly expected and increased scrutiny from underwriters becoming the norm.

Capacity/Market: Challenging landscape

The property market continues to feel the impact of high inflation, following year-on-year premium increases since 2020, due to a more challenging risk placement climate.

It's important to be mindful that renewal rate increases are in the region of 10% for commercial property owners with a well-managed account and no claims losses, and up to 20% if there are claims involved. This trend will likely continue in the next 12 months, but ultimately the market may stabilise to a new rate norm.

Natural catastrophe losses, El Niño and extreme weather events remain front of mind and will continue to impact market pricing and capacity constraints for the foreseeable future.

Given the currently challenging market conditions it is essential to review and update building sums insured reinstatement values and ensure adequate business interruption indemnity periods, as inflationary pressures and construction supply chain issues continue to bite.

Self-insurance – considering captive and mutual to transfer risk

Rising property premiums are prompting interest in self-insurance or risk transfer alternatives like captives and mutuals (an insurance company owned by the policy holders). A business may choose to insure the majority of a property through traditional cover and use an alternative risk transfer option for the remaining cover, to reduce pricing.

A mutual can be used to cover risks that cannot be placed in the traditional insurance market. However, caution needs to be exercised when exploring other options as while the business may benefit from reduced premiums this may be at the cost of policy coverage.

Deductibles, or excesses, are another way to reduce premiums. The AUD500 or AUD1,000 amounts are now outdated, with many companies now electing higher levels, moving into AUD5,000 or AUD10,000 excesses as a minimum.

Capacity remains tight across the board

A trend of upward premium movement is being experienced in metro and regional locations. Increases may vary, with deductibles and excesses being tailored to a specific property, or the underwriter may insert a provision in the policy wording to provide terms for an extreme weather event, for example.

The overriding challenge, however, is currently in sourcing suitable levels of commercial property insurance cover and insurers accepting the risk, as a growing number of declines are being seen at this time. One workaround to this issue is the use of multi-insurer panels to structure property risk and achieve the desired limits and levels of cover.

Meanwhile, international markets retain a critical role to offset current capacity challenges in the Australian market.

Risk spotlight: Building occupation, use and location

Heightened interest in commercial premises occupancy and its nature of use determines the scope of the risks to be assessed. These include more challenging risks such as waste storage and recycling, along with plastics or other combustible materials.

Insurers would historically take on 100% of the risk, however, now this is more like 70%, leaving the business to secure the remaining 30% – either through self-funding or by means of alternative risk transfer. For commercial properties/business premises, additional time should be factored in to source alternative markets to place the remaining risk.

For construction projects (renovations/additions or new builds), insurers are placing increased scrutiny on materials including the presence of asbestos in any demolition and in construction, making sure materials have weather resilience qualities, particularly where there is new urban sprawl and bushfire risks are a growing concern.

There has been a number of cases recently where renewal terms factor in the neighbouring properties and/or the land space surrounding the insured property due to bushfire or grassfire risk. As the drier season approaches and there is more fuel available following high rainfall, this risk will inevitably be heightened.

INSURANCE RECOMMENDATIONS

- **Review property reinstatement costs in advance of renewal to ensure accurate sums for insured values, and engage with a risk engineer to conduct a property survey.**
- **Business interruption indemnity periods need to provide adequate protection in the current climate of supply chain pressures and elevated building costs.**
- **Seek advice from a broker before changing your risk placement to achieve short-term cost savings, which could lead to issues further down the line.**
- **Take a proactive approach to risk prevention and mitigation; implementing a strong risk management culture can help minimise claims and improve renewal outcomes.**

Regulators Consider Tightening Measures as the Trend Towards Long-term Claims Rises Among Workers

The increase in volume and length of workers' claims across Australia has significantly raised premium costs. Meanwhile, there is a focus on establishing workplace environments that improve workers' mental well-being and physical health as employee retention becomes key amid persistent recruitment struggles.

Capacity/Market:

Frustrated employers burdened by increased premium rates

During H1-2023, Australia has sustained a significant increase in premium rates for workers' compensation. The state of Victoria has recorded an unprecedented 46% rise in just one year. This surge is largely attributed to the workers' compensation schemes operating at a deficit across several years, prompting the need to recover costs. This trend is particularly pronounced in states where premiums are government regulated and non-negotiable, such as Victoria and New South Wales.

Current reviews of workers' compensation schemes may prompt certain states to tighten the criteria for claim eligibility. For example, in the Victorian Parliament there is a debate on removing burnout and workload as acceptable grounds for compensable mental health claims. If these changes are approved, they will be welcomed by employers burdened with increasing premiums.

Even if state parliaments pass new regulations to manage and limit workers' compensation claims, these will not absolve employers of their duty to identify and manage mental health risks within the workplace – a fundamental obligation.

Another concern is the trend of long term claims and stagnant return to work rates, particularly in relation to surging mental health related claims. This shift is further exacerbated by a significant rise in the engagement of personal injury lawyers representing plaintiffs in these cases.

However, there is also substantial evidence to show that when an employee is engaged in suitable, meaningful employment, it is good for both their mental and physical health (Health Benefits of Good Work®). Getting employees back to work needs to be encouraged.

KEY TRENDS:

- **Substantial premium increases due to prolonged COVID-19 effects and a surge in claims and durations.**
- **Significant rise in workplace issues resulting in legal representation and common law claims.**
- **Emergence of new laws that legally prohibit insurance provisions in the case of employer health and safety fines.**
- **Regulators are bringing in additional specialist psychosocial safety inspectors to investigate workplace risk.**

Risk spotlight:
Post-pandemic realities in the workplace

During and in the aftermath of the pandemic, the office landscape has undergone a significant shift in team structures and job roles, prompting individuals to shoulder unfamiliar tasks, often with extreme stress factors and few breaks in the work cycle. This has led to 'the great burnout' where many workers, particularly those in management and supervisory positions, are exhibiting exhaustion and decreased emotional resilience.

With workplace flexibility now commonplace, there is a loss of skill sets, social interaction and cognitive abilities. This is particularly prevalent in the younger generation. Working from flexible workspaces, those new to the workplace lose opportunities to observe and learn from senior members' interactions.

Recruitment, retention and good employer practices

Ongoing challenges in recruiting experienced workers have exacerbated the burnout problem. Employers are now exploring how to retain and empower their existing workforce while establishing a safe workplace that fosters growth.

Employers are recommended to focus on factors which are under their control, such as limiting workplace injuries and implementing strategies to reduce fatigue or address safety through intervention procedures, reducing staff turnover.

Redefining work environments and navigating regulations

Prevention is key with employee mental health. Employers must look towards establishing practices to enable early intervention and support through the fostering of a culture that addresses individual concerns. Employee assistance programs (EAPs) have become commonplace and well-used in recent years, providing support while preserving privacy. However, this also leaves employers in the dark on the issues their employees are dealing with, and may lead them to overlook necessary actions for getting in early and aiding recovery.

With new psychosocial regulations in force, there is employer concern regarding their lack of familiarity with obligations and required risk assessments. The initial implementation period has focused on education and now we are also seeing regulators move towards use of dedicated, specially trained psychosocial risk inspectors.

Predicting future incidents with data

With risk avoidance being key, the implementation of AI and machine learning in data capture to recognise worker safety concern patterns is exciting. Although in its infancy, the technology makes it possible to study previous incidents and events leading up to them and search for similarities, which can in future facilitate risk prevention and mitigation.

"The current state of workers' compensation costs has had a significant impact on employers nationally, and will continue to do so as a mandatory compliance-based insurance. However, it is not all doom and gloom, with some of our clients realising significant savings through our assistance on insurance program design or prevention strategies."

Paul Marsh, Joint Head of Workplace Risks

09 INDUSTRY FOCUS: MARINE & CARGO

KEY TRENDS:

- **Rates stabilise as insurers display a higher risk appetite.**
- **Enhanced regulatory scrutiny on ESG practices over the next 12 months.**
- **Rising sophistication of cyberattacks drive specialised cyber insurance demand.**
- **Geopolitical and natural catastrophe concerns are driving increased risk management awareness in businesses.**
- **Rapid digitisation and adoption of AI-driven automated tools are revolutionising efficiency in the industry.**

Regulatory Scrutiny of Business ESG Credentials to Increase

Regulators are steering substantial ESG compliance requirements; rates flatten following previous increases and insurers display a higher risk appetite. Worryingly, we are seeing greater levels of cyberattack sophistication.

Capacity/Market:

Rates flatten

There was a flattening of rates during the first half of 2022 in the marine and cargo sectors, a shift from the rising rates of previous years. For H2 2023, for businesses in the marine space, insurers are offering a more accommodating risk appetite within limits, although there has been no softening yet.

The marine market is showing renewed activity, with opportunities for growth, particularly in Australia, and we anticipate this trend to continue for the next six months.

An emerging trend of underinsurance being observed in other commercial sectors is not being seen in marine and cargo. This is primarily due to a post-pandemic shift in this sector. In the COVID-19 aftermath, there was an application and condition process, with valuation reports required for all vessels. Where ships had been left idle for a period of time, insurers would only move the status of vessels from non-operational to operational on the basis that a qualified surveyor determined that the stipulated standards were met.

This contributed to more sophisticated insurance and risk knowledge in the marine sector, as companies look to de-risk through added capital expenditure in their operations and risk mitigation to secure better terms from the insurance market.

Risk spotlight: Environmental concerns in the electric vehicle space

In the Australian electric vehicle (EV) market, the fire risk of lithium batteries remains a key concern for regulators, particularly during transportation. The impact on passenger vessels from EV fire hazard concerns is also being researched.

With the shift towards environmental-related practices motivating greater supply of these vehicles, and with the technology still developing at pace, there is a potential to see claims costs increase in this area. However, as with extreme weather and natural catastrophes, the current impact on claims remains low frequency but high severity.

New environmental regulations impact business profitability

New regulations such as the Energy Efficiency Existing Ship Index and the Carbon Intensity Indicator are placing pressure on profitability due to costs to conform. The current market conditions are leading companies to strongly focus on ESG vessel compliance, with underwriters carefully assessing risks before accepting them within the scope of the insurance cover. With increased scrutiny ensuring that operators are complying, it is vital operators don't cut corners to balance squeezed profit margins.

There is a regulatory push to achieve net zero emissions in the transport industry by 2050. The current technology, especially for freight transportation, is not yet ready. However, there are great strides being made with electric trucks in the USA, albeit in conceptual stages.

Sophisticated cyberattacks on the rise

The past six months have seen cyberattacks rise. While phishing remains a significant threat, cyber claims filed show an increased level of sophistication in the cyberattack methods employed. A new form of cyberattack in the marine sector involves hackers infiltrating a company's system for a long period of time to collect huge datasets before a ransom demand is made. The new threat wave has increased demand for cyber insurance from being a policy extension to a high-priority specialisation.

Positively, the addition of blockchain technology is promising to deliver rapid and favourable changes in shipping, via enhancing security of information sharing and document management.

On the AI front, high efficiency has resulted from the implementation of automated tools for warehouse management. Although these AI advancements raise concerns about job displacements, they are highly effective in improving the speed of business operations.

Geopolitical uncertainty creates caution

The situation in Ukraine and the Black Sea confrontation has impacted the current market conditions, leading to heightened concerns among insurers. Although Australia has a sense of relative geographical protection, the developments in Taiwan are also raising concern.

Insurers in the marine sector are exercising caution concerning war risk cover, and there are increased costs in this area. Claims related to assets in Ukraine have been closely monitored, with some assets still being sold at discounted rates to opportunistic buyers, but with a longer term view of retrieving certain holdings post-war.

10 INDUSTRY FOCUS: ENERGY & RENEWABLES

KEY TRENDS:

- Competition is increasing in the renewable energy insurance market with the arrival of new entrants offering more insurance choice.
- Pricing remains stable, particularly for those with a good claims history and a strong renewal strategy.
- Commodity prices and supply chain challenges continue to be felt across the sector, raising business interruption risk.
- Traditional energy providers are facing increased scrutiny from regulators in terms of ESG reporting, leading these companies to offer alternate future means of energy production.

Energy & Renewables: Insurer Appetite is Growing in a Period of Transition

Increased insurer competition creates improved insurance conditions, as underwriting capacity expands and premiums remain largely stable.

Capacity/Market: Increasing renewables focus

In a challenging geopolitical landscape and with climate change hot on global agendas, the energy sector's focus is increasingly on the renewables space. Insurance markets are either pulling out of the upstream oil and gas sector completely or refocusing underwriting teams on technical training for writing renewable energy risks.

From a pricing perspective, the market remains relatively flat, and we expect to see renewal pricing in the region of 0%–10% uptick.

Beyond wind and solar power

The renewables space has grown significantly in the past two to three years, no longer simply focusing on wind and solar power but moving into areas such as battery energy storage systems and floating technologies. This presents a big opportunity for Australia, with a large flow of capital from international companies investing in this space.

In the next two years, we anticipate growing insurance competition for renewables, building on existing underwriting capacity. More market leaders will emerge, driving competition and price; and there are already notable new entrants.

The domestic insurance market is keen on renewable business; however, for larger renewable developments a combination of domestic and international market placement is expected.

Parametric insurance and alternative risk transfer

Parametric solutions have become increasingly common in the renewables insurance space, particularly for higher risk exposures such as natural catastrophes. Alternative risk management transfer methods are being more readily considered, and future use of captives is possible as the renewables sector evolves in terms of scope and scale.

Traditional oil and gas companies still have an important role to play in meeting Australia's energy demands. This will include building the supporting infrastructure for the use and distribution of the renewable energy produced, which will also require alternative forms of risk transfer as part of the insurance approach.

Risk spotlight: Evolving risks present challenges

Technical challenges and new risks continue to evolve. In engineering terms, for example, wind turbines have shifted from generating around 2–3 megawatts (MW) of power, to now 15–18MW for offshore wind projects Such advancements are likely to bring revised underwriting considerations, particularly if the technology used is at the prototype stage versus a proven technology.

In addition to physical risks, underwriters will look at how the contractual, legal and regulatory risks are managed – particularly for the upscaling of wind and solar energy technologies, as well as technologies still under development.

In terms of extreme weather risks, solar farms in northern Australia have experienced problems particularly from wind, hail and flood, while wind farms suffer lightning strikes. As a result, the need for risk mitigation measures, such as site selection, appropriate construction materials and engineering design is increasing.

Given the increasingly unpredictable global weather patterns and prevalence of natural catastrophes, underwriters will scrutinise any new renewables projects that are deployed in higher risk locations.

Macroeconomic headwinds are ongoing

Commodity prices and supply chain issues continue to affect the energy sector as materials and parts are in short supply, with longer lead times elevating the risk of extended business interruption.

As investment within the renewables sector increases, this may create challenges within supply chains for renewable projects by protracting replacement times for warranty claims and insurance losses. In order to mitigate the risk, it may be prudent for replacement times to be negotiated within supply contracts to provide certainty in the event an issue arises.

In addition, for new renewables projects, costs sourced at the current time are likely to be inflated for insurance purposes, given that there may be a two-to-three year period between sourcing the cost and the risk being insured. When a new project eventually moves into the operational phase, the original construction values must be reviewed.

ESG under the spotlight

ESG momentum is on the rise and traditional energy sector operators are taking deliberate steps towards transitioning into renewable and alternate energy production and storage. Companies are naturally going to be scrutinised for their ESG approach, despite many having subsidiaries that are purely focused on the environmental element. These companies must be diligent in their ESG reporting to avoid greenwashing fines and notifications from ASIC.

INSURANCE RECOMMENDATIONS

- **Review your insured values and maintain up-to-date valuations for property, plant and other assets in line with market valuation, factoring in inflation and pricing.**
- **Clarify where renewable plant and machinery/equipment are prototypes or proven technologies. This is factored into risk pricing by underwriters.**
- **Understand your contractual obligations, including power generation agreements and regulatory compliance. This is integral to the scope of insurance.**
- **Take time to fully understand your risk profile (physical, financial, contractual and regulatory risks) when preparing for renewal, working closely with your risk management partner.**

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Insurance Market Cycle

Prices rise and insurers' reduce coverage. Loss events, dipping underwriter profits and capital retreat signal to the insurance market that prices have risen in order for insurance businesses to remain profitable.

Premium prices and insurer profits start to react to negative pressure. As claims losses rise, the market starts to tighten.

Premiums are higher and cover is more difficult to find. Underwriters may step away from certain markets as they look to rebalance the profitability of their books.

Prices begin to drop, cover becomes more accessible in the absence of major losses or with more capital entering markets, underwriters are more willing to place business.

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As a guide to working on effective risk outcomes for business these key steps remain a focus.

1. Building strong relationships ahead of renewal

Your relationship with your insurance broker and their relationship with providers in the insurance market are of critical importance. It's imperative that your broker understands your organisation and knows the individual risk exposures associated with your business. This enables them to design a fit for purpose insurance and risk program, ensuring you get value for money with the correct coverage in place.

2. Starting renewal preparations early

The more time your broker and you and your business team have to work on the renewal of your insurance program, the more likely you will gain an effective result in this challenging insurance market. That demands putting in the time to gather the relevant and comprehensive information so that it can be presented to potential insurers well before the renewal date. Building in a longer lead time enables your broker to properly market your insurance program to and negotiate with potential insurers, presenting your business in the best possible light.

3. Provide detailed information that represents your risk profile in positive terms

Be prepared to document and detail your risk management protocols. In the current market conditions insurers will require more underwriting information. Collect and collate accurate, up-to-date building valuations and risk surveys. Insurers will also want to see your business's risk control processes, supply chain management and your risk management program. Work with your broker so that they can present your insurance needs to potential insurers in a tangible manner that will resonate and be attractive.

4. Being open to flexible, innovative ways of structuring your insurance program

The insurance market isn't static but in fact highly responsive to claims impacts and events that alter the perspective on risk. Be open to working with your broker around changes to pricing, deductibles and coverage. Your insurance broker may be able to offer creative solutions for high risk businesses where the insurance market may be unwilling to deploy their capital. If you're willing to take more risk on your balance sheet, let your broker know.

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