State of the Property Market: 1st Quarter Update 2020.

It seems like an indescribable amount of time has gone by since our last quarterly update. As we all know, the world is a very different place today than it was three months ago and if you are like me then you are probably still trying to figure out how we got here and are optimistically counting the days until we can go back to the way things were done before the COVID-19 pandemic took its full effect on the globe. This virus has impacted everyone around the world and our thoughts are certainly with those who have been infected or who have passed away as a result of this horrific pandemic

It seems we are getting inundated with market feedback on a daily basis so much of what I can tell you is probably information you already know, but there are a few key takeaways that will drive the market for the foreseeable future. It is the expectation of many carriers and insurance professionals that as a result of this pandemic, the firm market is here to stay. Hopefully the summation below provides you with a little insight that will be beneficial to you for the rest of 2020.

1. Rate Change - When 2020 began, carriers had both the need and expectation that rates still were not where they needed to be in order to maintain long term profitability. The firm market cycle really accelerated in May and June of 2019, so markets started the year pushing increases in the 10% to 25% range.

The initial outlook was that rate increases would slow down as we got further into Q2 of 2020. Now, everything has changed and business are losing money, properties sit vacant, construction projects are stalled, and carriers are seeing claims filed daily by almost every one of their customers for BI losses related to COVID-19.

Furthermore, legislation is being considered at both a national and state level to potentially put pressure on carriers to pay for lost revenue due to communicable diseases. I can assure you, carriers did not model or price risk for BI losses due to communicable diseases—they are property carriers and they price risk for fire, flood, wind, and earthquake.

The same uncertainty that is bad for the global economy and the stock market is also bad for insurance carriers, and it is more difficult than ever to balance the need for rate and profitable business while their customers are financially constrained. The more difficult reality is that carriers have lost money for several years in a row while the global economy boomed, and they are not in a position to lose money again purely as a result of a global pandemic.

If they do not make an underwriting profit in 2020, it is quite possible that many carriers may not be able to continue to be there for the customers. As such, clients need to be prepared for further increases as best they can. I suspect many clients will increase retentions and buy less limits since those are the two primary tools they have to ease premium increases.

2. Capacity – There is still not a shortage of capacity in the market but with major changes being made by AIG, FM, and many of the large line excess capacity carriers we will continue to see some customers have rate adjustments that are outside of the market.

Many of the accounts that will be renewed throughout the year that are in the large account space with total insured values in excess of $500M will see capacity shortages in their excess layers, and in some cases need to replace blocks of capacity in excess layers to a tune of $100M or more.

Carriers are also acting more cautiously in excess positions as a result of industry events where claims crept into layers that were previously felt to be "out of the exposure" or "PML". Replacement cost valuations, building ordinance triggers, non-damage business interruption, post claim remediation costs, etc. are all items that are causing excess markets to charge more, trim line size, and tread lightly. In many cases, accounts are seeing stable rate change in the primary and first excess position but as you get into the higher layers, rate swings are far more drastic and sometimes in excess of 100% year over year.

3. Asset Class Impact in 2020 – It is no secret that multi-family continues to be the most challenging asset class. As a market segment, it has been a loss leader for the better part of a decade and despite higher deductibles, rates, and more restrictive terms, many carriers are still running for the hills.

In the large account space, only a handful of carriers will consider primary in a meaningful way and most of the players in the space will only deploy small quota share lines, so getting a primary layer together usually takes three to five markets for a primary $5M or $10M layer. These customers will continue to see markets push rate and standard carriers are likely to pull back.

Towards the tail end of 2019, we saw a lot of the large shared limit programs that exist in this space either pull back or disappear, and that ones that are around saw significant rate lift which is putting their rates closer to open market prices. There continues to be no sign of increased competition in this space and I suspect that will not change through the bulk of 2020.

The hospitality sector is starting to feel similar pain as markets pull back capacity due to uncertainty around the accuracy of modeled CAT events, BI claims, and increased risk due to forced COVID-19 hotel closures. On top of that, what once was a hotel could now potentially be a temporary government hospital, which, depending on where you sit, may not be an exposure you want to take on.

As I write this, the list of carriers who have mentioned they will be pulling back from the hospitality space and no longer targeting new business in this area is growing. Early reports of increased hurricane activity by way of 2020 scientific projections are adding concern to what the correct underwriting rate should be deal by deal and how volatile this space can be depending on how the weather blows.

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We are highlighting hospitality and multi-family because thus far, these two industry segments continue to be impacted the hardest by market conditions but in the current environment, there is not one asset class that is immune to market conditions and I recommend that all asset classes be prepared for increases at varying levels. Those insureds who have good claims experience and have cultivated long term carrier partnerships will fare the best and may even see increases in the single-digit range.

4. Treaty Reinsurance and Rating Agencies – When all is said and done, sitting atop of the insurance capacity pyramid are the reinsurers (both treaty and retrocessional markets). The retrocessional market has had several challenges that are carrying over from 2018 and 2019, making it difficult for reinsurance providers to get the kind of protection they are accustomed to.

As a result, treaty reinsurers are having to be more restrictive in their offerings. Several major P&C carriers are in the process of wrapping up their April 1st treaty renewals as we speak. Outside of the increases most reinsurers are pushing, they are also making sure they have assurances that communicable disease coverages are excluded in their entirety. Should BI claims from COVID-19 have an impact on the direct writers, they would likely be taking these claim payments net which will have an impact on their financial health.

Just today (April 2nd), Lloyds financial rating was downgraded due to COVID-19 concerns and there will be a bit of a domino effect with the rating agencies who seem eager to add to the panic that they create with their downgrades. The cautionary downgrades may be warranted because it is way too soon to fully understand the balance sheet impact COVID-19 will have on major insurance carriers. That said, the early downgrades are a sign of things to come and will have an impact with lenders who need to approve the capacity and deductibles clients have on their programs.

In closing, it is a firm market and relationships count more than ever today. All of the feedback I have provided in this update is not meant to add to the hysteria, but I do firmly believe that the best advice comes from a place of honesty. While it may not be what you want to hear, it will help you manage the future with a much clearer picture in mind.