COMMERCIAL LINES INSURANCE MARKET UPDATE – FIRST QUARTER 2022

Executive Summary

Market stabilization is the theme as we closed the first quarter of 2022. We monitored the first quarter earnings releases of commercial insurers carefully to detect trends. All the top commercial lines insurers reported rate deceleration, which many described as rate moderation. What this means is that the insurers are still reporting single-digit rate increases across their commercial lines business, but the level of the rate increase is either unchanged from the last quarter or slightly lower.

The big macroeconomic event in the first quarter was Russia's invasion of the Ukraine. Since many commercial lines policies include war exclusions, most insurers reported minimal losses and minimal expected ongoing impact. At the onset of the invasion, Swiss Re, one of the industry's top reinsurers estimated industry losses arising from the invasion to be in the $10 billion–$20 billion range. Swiss Re recently updated this guidance to report that it believes industry losses will be at the lower end of this range.

Digging deeper into the specific segments of the commercial lines markets, both the Property and Casualty segments are reporting moderating rate increases. In the property segment, insurers are reporting that rates are keeping pace with loss costs. This is an important area we will be watching as inflation continues to impact the economy. If loss costs rise rapidly, insurers will likely look to increase rates again. For now, insurers are remaining vigilant around appropriate property valuations.

On the Casualty side, Workers' Compensation remains a profitable line of business, so insurers are keeping rates flat and, in some cases, offering competitive quotes on other casualty segments to win the workers' compensation line of business. As with property, insurers are watching loss cost trends particularly in segments like auto which will be impacted by inflation.

For Directors & Officers (D&O) liability, our characterization of the overall environment is flat. We started to notice decelerating rate increases in late 2021 and this trend continues to the point where some clients are seeing decreasing premiums and retentions. As of the end of the first quarter, premium and retention decreases mostly occurred for companies that have been traded publicly for some time with a history of strong earnings. We do expect this trend to continue and the number of new entrants to the D&O market ramp up their staffing and quote more business.

Finally, Cyber continues to be the outlier to the positive trends we've seen in the other areas of the commercial market. Premiums continue to rise as insurers cut policy limits and restrict coverage. Given the continued problems with ransomware losses and concerns over increased threats arising from the Russian-Ukrainian War, we don't expect relief in this market any time soon. Clients should continue to focus on having up-to-date cybersecurity measures in place. Good security controls will not necessarily reduce premiums, but they can mitigate the level of premium increases.

D&O: Market Update

OUR POV

Public D&O rates continued to rise in 2021, but the market has transitioned and some clients are achieving decreases in rates and/or retentions.

MARKET TRENDS

- Market leading carriers continue to seek premium increases, but there has been a deceleration in the rate of increase; upward adjustments are generally still larger on excess layers.
- The economic uncertainty created by COVID-19 is resulting in more D&O litigation due to factors like misleading statements about the outbreak, deceptive claims regarding potential vaccines and treatments, and privacy concerns.
- The March 2020 *Sciabacucchi* ruling on federal choice of forum in the Delaware Supreme Court has led to numerous state court Section 11 suit dismissals, and eventually more stable IPO pricing. The public markets cooled significantly in Q1—the number of SPAC IPO and de-SPAC listings dropped to the lowest levels since 2016.

CONTEXT FOR CURRENT TRENDS

- Securities class action severity remains high. There were 101 settlements totaling $3.2B in 2021, the largest total annual settlement amount in the last decade.
- The likelihood of a public company being sued reached a record high of 5% in 2019 when 268 lawsuits were filed but declined in both 2020 and 2021. The total number of suits dropped to 210 in 2020 and 182 in 2021, a 13% year-over-year drop. 45 cases were filed in Q1 2022, on par with activity through the first quarter of 2021.
- Litigation is being driven by new and increased exposures including cyber (data breach), #MeToo, privacy oversight (GDPR), climate change, and COVID-19.
- Derivative actions are on the rise with notable settlements (Renren, Boeing, First Energy, American Realty, Wells Fargo...) tapping “A Side-only” insurance.

3.3%
Likelihood of Being Sued (decline for 2nd year in a row after 2019 all-time high)

488
Number of open SCA cases pending

$11M
2021 Median Cash Settlement (10-year average $8.5M)

$32M
2021 Average Settlement (10-year average $29.6M)

1

Property: Market Update

OUR POV

Rate increases will continue to moderate throughout 2022 as carriers strengthen their balance sheets and rate levels begin to keep pace with loss costs. Adequate valuation and risk improvement are the biggest factors in generating competition and achieving a favorable renewal outcome.

MARKET TRENDS

- Rate increases continue to moderate for insureds that demonstrate improvements.
- Capacity remains restricted for challenging occupancies.
- Carriers continue to work towards profitability in their property portfolios.
- Focus and scrutiny of credible and reliable valuations persists and is a key factor in the renewal process.
- Secondary perils such as winter storms, wildfires, hail, flood, and tornadoes contributed to an accumulation of losses in 2021.

CONTEXT FOR CURRENT TRENDS

- Insureds that distinguish themselves with comprehensive and robust underwriting information and demonstrated risk improvement position themselves for the most favorable outcomes.
- Carriers continue to apply a differentiated approach to risks, with challenged occupancies (forest products, metals, and food and beverage) continuing to see double-digit rate increases.
- Concerns with valuations persist due to supply chain issues, labor and material costs / shortages, and longer duration business interruption, which contribute to an increase in cost of claims.
- Absent trending and appropriate valuation, carriers push for margin clauses and occurrence limit of liability endorsements, restricting claims recovery.
- Secondary (non-modelled perils) are an increasing component of loss costs that remain a focal point, with a push towards rating for these exposures accordingly and exerting pressure to increase deductibles.

0%–5%
Non-CAT accounts with favorable loss history

2.5%–7.5%
CAT accounts with favorable loss history

15%+
Non-CAT accounts with unfavorable loss history

30%+
CAT accounts with unfavorable loss history

Cargo and Stock Throughput: Market Update

OUR POV

Markets are capitalizing on growth opportunities and looking to make the most of the current climate. Global supply chain instability is leading markets to review participation structure on accounts.

MARKET TRENDS

- Carriers are looking for a balance between rate and risk, the result being single-digit increases. We are seeing flat renewals on larger pieces of business with good loss records.
- The war in Ukraine has seen Marine markets issue Notice of Cancellation on all accounts with potential exposure in and around the waters of Russia, Ukraine, and Belarus in respect of war perils.
- Requirements for detailed COPE or surveys on locations over $1,000,000 as markets look to protect themselves against large stock losses
- Carriers are reviewing line sizes deployed and participation in large programs in light of fire losses to ensure their exposure is managed.

CONTEXT FOR CURRENT TRENDS

- Global supply chain challenges have led to significant values accumulating in ports, and insureds consolidating goods on single vessels. With global commodity prices, the value of goods onboard vessels has risen markedly.
- China's recent COVID-19-related lockdowns and manufacturing facility closures alongside the Ukraine war will only extend the period of instability for global supply chains.
- Cargo & Stock Throughput policies require physical loss or damage. Many of the supply chain delay costs faced by insureds are not covered unless resulting from a physical loss or damage event.
- New capacity and growth targets still hold true, with markets maintaining underwriting discipline, insofar as coverage, but far more malleable on price for clients that demonstrate continued risk improvement and favorable loss history.
- Large warehouse fire losses such as with Walmart in Indiana reinforce requirements for detailed COPE and fire protections, with an increased need for surveys to be undertaken on larger risks.
- Despite lines size cutbacks over the last few years, the London market maintains the ability to write large primary stretches even on CAT-exposed risks.

Flat–7.5%

Accounts with favorable loss history and a focus on risk management

10%–20%

Accounts with unfavorable loss history or those that do not meet rate adequacy for underwriters

Casualty: Market Update

OUR POV

A stabilization of the casualty market is underway. WC remains profitable for insurers, who are generally willing to accept flat rates. GL and Auto rate increases are slowing. Lead Umbrellas are challenging due to ongoing increased large claim activity, while high excess is competitive.

MARKET TRENDS

- Primary casualty insurers continue to seek rate increases on GL/Auto overall for the 17th consecutive quarter in order to keep up with loss trends.
- Workers' compensation is the most competitive and profitable line of coverage, but with medical inflation driving increases in the average cost of an indemnity claim, the market's combined ratio is trending up.
- With aggressive corrections to rates, limit deployment and attachment points over the last two years, the high excess market has stabilized while lead Umbrella insurers continue to achieve significant rate increases due to increasing large claim activity and limited competition.

CONTEXT FOR CURRENT TRENDS

- Nuclear verdicts continue to create headlines. Social inflation and litigation financing has also increased pressure on settlements with defense attorneys looking to avoid unpredictable jury verdicts.
- Organizations with large auto fleets, high-hazard products, or significant premises exposures are facing the greatest pain in their Umbrella renewals. Using self-insurance or buffer layers to increase attachments can help mitigate premium increases but limited umbrella insurer capacity remains a challenge.
- Carriers continue to refine coverage terms and conditions. Insurers seek to apply new exclusions or sublimits on communicable disease, abuse & molestation, assault, PFAS, and Russia/Ukraine/Belarus.

By-Line 4th Quarter 2021 Rate Changes Ranged From under 1% to +15%

	Auto	WC	GL	Umbrella
Q4 2021	8.00%	0.30%	6.40%	15.00%
Q3 2021	7.40%	-0.30%	6.30%	16.90%
Q2 2021	6.80%	0.30%	6.00%	17.40%
Q1 2021	9.00%	1.00%	6.20%	19.70%
Q4 2020	9.10%	0.40%	7.30%	21.30%

Source: CIAB Q4 2021 Rate Survey

Cyber: Market Update

OUR POV

If 2021 was the year of rate increases, 2022 will be the year of coverage restrictions—and more rate increases.

MARKET TRENDS

- Coverage restrictions coming to cyber market include:
  - Dependent business interruption and system failure
  - Failure to timely patch vulnerabilities exclusion
  - Non-breach privacy (GDPR, CCPA, BIPA)
  - Media liability
- Rates are increasing across the board—strong relationships with incumbent insurers help limit impact.
- Excess rate increases are accelerating fast, often 85%-95% of underlying pricing.
- Underwriters more reliant on 3rd-party scanning tools for information gathering.

CONTEXT FOR CURRENT TRENDS

- Many clients looking at parametric insurance for cloud outages to replace lost dependent business interruption coverage.
- The conflict in Ukraine has raised the prospect of the war exclusion applying to cyber losses. However, the increase in cyber attacks in Ukraine have not resulted in major insurance losses to date.
- Technology supply chain attacks like the SolarWinds hack and zero-day vulnerability exploits like Log4j are driving significant carrier concern around risk aggregation and patching procedures.

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