MARKETS IN FOCUS

REAL ESTATE

Insurance Pricing &
Market Update

Q3 2022

Introduction

Given the recent change in demand forces impacting urban/suburban real estate, **Mixed Use** projects have become popular once again due to their ability to improve tenant experience through walkability between housing, workplaces and other amenities.[1]

+ Although the first eruption for mixed-use development began in the mid-2000s and simmered shortly after, it appears that the trend is back and here to stay as many cities struggle with housing demand and the younger generations' desire for neighborhood walkability.

Industrial Properties are expanding their reach to a single facility for multiple business purposes, such as a shipment center also containing offices or a showroom.[2] While e-commerce and demand for quick last-mile deliveries continues to grow, so will industrial properties designed to service these needs.

+ Digitalization, demographics and deglobalization will boost industrial market growth in 2022 and beyond.[3]
  - The demand for industrial real estate will be necessary to support forecasted double-digit annual growth in e-commerce sales.[4]
  - The retail and e-commerce waves are here to stay and will continue driving the growth of the industrial real estate market.
+ Industrial property inventory modernization is still in an early stage as more than 70% of U.S. industrial space was built before 2000 and a full third of the inventory is now over 50 years old.[5]
+ The current industrial construction pipeline is approximately 500 million sq. ft., all set to deliver by 2023, signaling a potential future supply gap if speculative construction starts remain paused through 2022 due to prolonged disruption.[6]
+ In the second quarter of 2022, sales prices reached $138 per square foot (sq. ft.), up 31.3% YoY.[7]

Multifamily Housing demand remains strong due to rising prices and rising mortgage rates in the single-family housing market.[8]

+ Average asking and effective rents posted near-record highs in the first quarter of 2022 with a 5.4% effective rent growth rate.[9]
    - The effective rent growth record is still 8.1%, set in the third quarter of 2021, which was three times more than the prior record of 2.4% set in the third quarter of 2001.[10]
+ CBRE forecasts multifamily occupancy levels to remain above 95% for the foreseeable future and nearly 7% growth in net effective rents next year.[11]
+ Construction will remain elevated in the near term with another 300,000-plus units expected to be completed in 2022.[12]
    - Deliveries averaged 206,000 units annually since 2010 and 171,000 since 1994.[13]

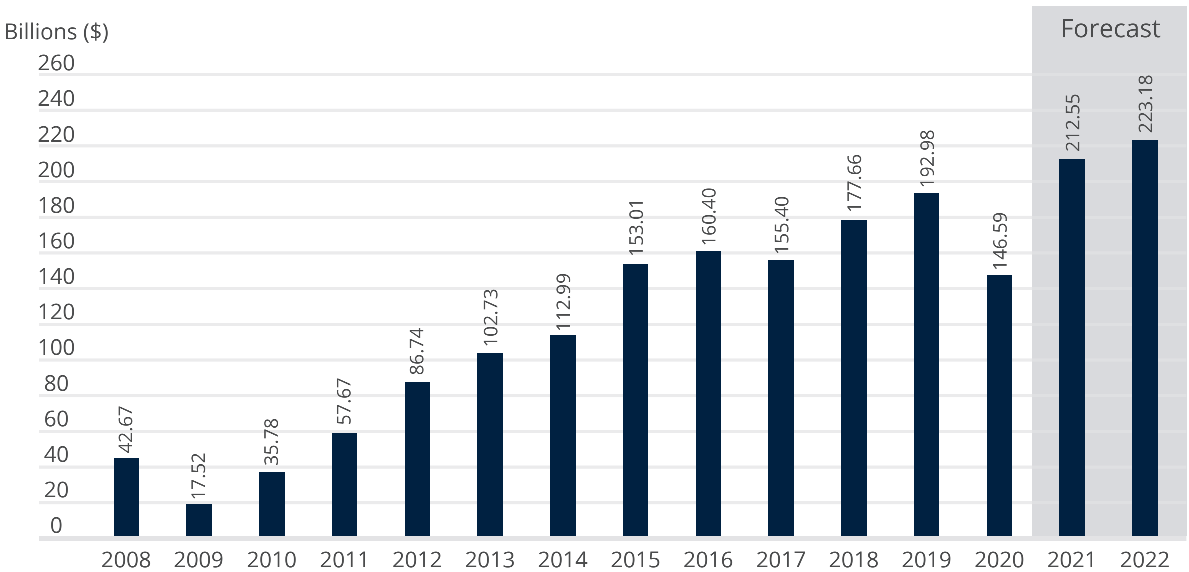
Top 10 Metropolitan Areas for Construction & Multifamily Starts

CITY	% CHANGE	TOTAL VALUE
New York City Area	Up 20%	$15.3 billion
Dallas	Up 72%	$8.1 billion
Washington D.C. Area	Up 35%	$5.5 billion
Miami	Up 35%	$5.5 billion
Austin	Up 70%	$4.3 billion
Phoenix	Up 53%	$4.2 billion
Atlanta	Up 68%	$4.2 billion
Seattle	Down 10%	$3.5 billion
Los Angeles	Down 14%	$3.4 billion
Philadelphia	Down 3%	$3.2 billion

Source: contructiondive.com

+ Downtown multifamily properties are filling back up and occupancy rates are nearing pre-pandemic levels.
    - A few factors contributing to this are fewer restrictions on urban amenities, higher vaccination rates, a growing willingness to use public transit, the reopening of college campuses and more workers returning to the office.[14]

Multifamily Investment to Set New Records in 2021 and 2022



Source: CBRE Research, Real Capital Analytics, Q3 2021

2H Outlook

PROPERTY

The market continues to bifurcate between CAT exposed risk and non-CAT exposed risk.

Facultative reinsurance and 7/1 treaty reinsurance rates are on the rise for heavily CAT-exposed properties, which is expected to impact primary rates moving forward.

Due to multiple years of strenuous hurricane losses, 2022 is anticipated to have 20 named storms throughout the year[15] and could create some reinsurance difficulties for carriers.[16] Coastal properties will continue to be a challenge from pricing and capacity standpoints. Hurricane Ian, which struck Florida and the Carolinas in late September is projected to have caused $63 billion of insured losses alone.

+ This is particularly true for the residential property market.

Properties that sit within wildfire-exposed areas are also receiving extra scrutiny in western states, but larger wildfire losses have mainly been associated with residential and hospitality-focused properties.

+ Many carriers are withdrawing from this risk class, forcing more volume to the Excess and Surplus markets.
+ In some situations, capacity might not be available for full total insurable value limits.

Supply chain and inflationary worries have resulted in a rise in demand for Business Interruption coverage (BI), which has caused an increase in pricing and additional scrutiny from underwriters.

+ Properties with more complex risks should be prepared to provide supply chain maps, forensic accounting reports and engineering analysis to get underwriters more comfortable with writing their risks.

Property valuations and business interruptions will continue to be a challenge for underwriters due to recent deltas in property values and total claim costs.

+ Third-party valuations have become the norm for quotes.

Excessive losses and the resulting elevated reinsurance costs have forced many insurers in the **habitational property** market to be far more cautious about underwriting risk, reduce capacity or even shutter operations completely.[17]

+ The $22 billion habitational property market – 7% of the $314 billion commercial lines market – is too large to ignore, but underwriters are exercising extreme caution and implementing AI technology to help in their rating processes.

- Gulf Coast and Florida risks have seen a significant decline in the reinsurance appetite, resulting in rate hikes at the carrier level and forcing some markets (such as Strata[18]) to be forced into restructuring.
- After being hit with insured losses of more than $112 billion from natural catastrophes in 2021, the industry is facing unnerving payouts in 2022.[19]
  - According to Business Insurance, habitational properties are exposed to the worst of these risks because of lighter materials used in construction.[20]
- In many cases the Excess and Surplus market is the only resort for primary layers for tougher classes of business.

Similar to other markets, **Builder's Risk** policies are experiencing increases in pricing and retention not only due to significant losses from natural disasters but also an increased volume of smaller claims, supply chain issues, cost of materials and labor shortages.

- Some of the most challenging projects to place are large wood frame, modular construction and renovation projects.
- Rate/exposure increases are becoming more common given the current price for building materials. Project delays are not uncommon due to supply chain bottlenecks and labor shortages, causing many insureds to seek extensions, which can be problematic for carriers since extension premiums are not easily calculated in pricing models for this line of business.

GENERAL PRICING ESTIMATES

Non-CAT exposed property with favorable loss history	Flat to single digit increases
CAT exposed property with favorable loss history	Flat to 10% increases
Property with unfavorable loss history and/or a lack of demonstrated commitment to risk improvement (unresolved recs, pattern of same issues, etc.)	10%+ increases for non-CAT 25%+ increases for CAT exposed accounts and higher depending on frequency/severity of losses and when there are limited markets for a risk due to occupancy/class of business or concerns related to loss control

CASUALTY

The casualty industry experienced 24 months of significant rate increases and capacity reductions but has moderated in recent months.

+ The casualty market is in good standing, with primary general liability rates continuing to plateau in areas with favorable loss histories.
+ Carriers are typically looking for more history of loss information, more details related to past losses and any subsequent changes made to prevent future losses.
+ As the back-logged court systems catch up to the pace of pre-pandemic operations, carriers are keeping a close eye on loss trends across the country. Carriers are planning for large settlements and judgments from sympathetic juries, compounded more than ever with the pressure from social inflation.[21]

Umbrella/Excess – Capacity remains adequate for the excess coverage but lead umbrella underwriter offerings are being required to reduce offered limits from traditional $25M layers to $15M with some offering limits as small as $5M. Essentially, a stacking of insurance carrier tiers are generally required to achieve desired limits.

Auto – Social inflation, nuclear verdicts and carrier combined ratios greater than 100.0 have resulted in challenges for those who have large vehicle fleets. The demand for fleet monitoring technology is on the rise, and many auto carriers are investing in telematics implementation in hopes of improving loss ratios.[22]

Workers' Compensation continues to be a profitable line of coverage for carriers and pricing is fair for insurance purchasers with capacity remaining stable. Loss history and Modification Factors is a large determinant for pricing, but carrier competition over accounts with adequate to strong loss history continues to help pricing.

GENERAL PRICING ESTIMATES

General Liability	Up 5% - 15%
Workers' Compensation	Flat to Up 5%
Auto	Up 10% to 25% Up 30% if large fleet and/or poor loss history
Umbrella & Excess Liability – Middle Market	Up 10% to 25%+
Umbrella & Excess Liability – Risk Management and other Complex/Hazardous Exposures	Up 25% to 150%

It should also be noted that tail claims continue to impact pricing and terms and conditions, especially in the Section 8 space.

+ It is not uncommon to see exclusions for firearm related losses or sub-limits for assault and battery claims.

EXECUTIVE RISK

D&O & Cyber markets are seeing their own set of **unique challenges**.

D&O – After a very hard market in 2020 and much of 2021, rates stabilized in early 2022 and there now appears to be small downward pressure on rates for the remainder of 2022.

+ Generally speaking, multiple years of substantial rate increases have lowered the insurers' loss ratios, returning them to profitability.
+ Because of the attractive rates in the D&O space from the insurers' point of view, additional insurance capital has entered the market over the last 6–12 months.
+ At the same time, there has been a large decrease in the number of traditional IPO's, SPAC IPO's and De-SPAC transactions. With these areas no longer demanding insurance capital, the insurers are competing more aggressively for traditional and mature companies. This, in addition to the reasons mentioned above, has shifted the supply/demand dynamic and created a more favorable market for policyholders over the last few months.
+ Despite the comments above, there are certain sectors that continue to be in a "hard" market, such as SPAC's and De-SPAC's.

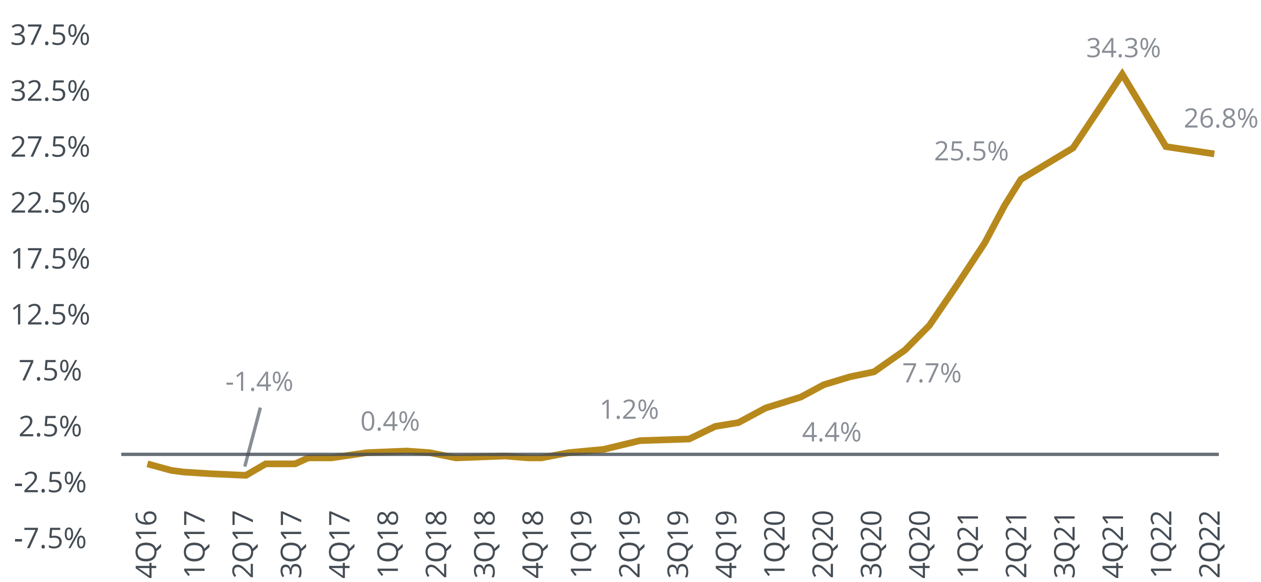
Cyber – The Cyber insurance market is best categorized as "transitioning out of a hard market".

+ Loss activity has decreased in the aggregate
+ According to Moody's Investor Service, the sector's loss ratio improved to 62% in 2021 from 65% in 2020[23]
+ Frequency has decreased but severity remains an issue

Average and Median Ransom Payments in Q1 2022

+ Average Ransom Payment: $211,529 (-34% from Q4 2021)[24]
+ Median Ransom Payment: $73,906 (-37% from Q4 2021)[25]
+ We continue to see a change in tactics amongst attackers. Due to improvements in data backups, the attackers are avoiding the encryption step altogether but are instead focusing exclusively on stealing data and demanding payment to prevent disclosure of that data.
+ Carriers are still focused on "must have" controls and increasingly reliant on external scanning technology in risk assessment
+ Pricing increases are still the norm
+ According to the CIAB, the average premium increase in Q2 was around 27%
    – We caveat that this is an average, and certain industry groups continue to see substantially higher increases

Premium Change for Cyber, Q4 2016 - Q2 2022



Source: https://www.ciab.com/wp-content/uploads/dlm_uploads/2022/05/Q1-2022-PC_FINAL.pdf

Major Claims in the Sector

LIABILITY CLAIM

During April 11, 2022, a plumbing worker working at an apartment complex was electrocuted. He and two colleagues were moving a flagpole.[26] When the flagpole made contact with a live wire, he was killed.[27] The jurors found the apartment management company was negligent and awarded the plaintiff's $15.6M, including $10.5M for the deceased family's past and future mental anguish, along with loss of companionship.[28]

PREMISES LIABILITY

On August 6, 2021, a plaintiff was headed to the rooftop of a mall, checking lights as part of his work, when his clothing snagged on the hatch door.[29] As his belt got caught on the door's locking mechanism, it became unlocked.[30] The door slammed onto the plaintiff instead of slowly closing, due to a missing part, causing injuries to his lower back, right shoulder and neck.[31] Jurors awarded $12.6M, which included $9.8M for past and future noneconomic loss.[32]

Guidance

BEGIN THE RENEWAL PROCESS EARLY

In regard to the **General Liability**, **Cyber**, **Excess/Umbrella** and **Property** markets, they are all constrained and more challenging to navigate in the disciplined market. Since prices are increasing across all lines of business for real estate companies, brokers are being overwhelmed with submissions from their insureds who want to minimize these additional costs.

PARTNER WITH INDUSTRY EXPERTS

It is of high importance to work with your broker's real estate experts who truly understand the business and the market for placing these complex risks. Working side-by-side with a team who can represent your risks at the highest level, and partner with your operations, is more important than ever during this disciplined market we are currently experiencing.

HIGHLIGHT CYBER SECURITY & PROACTIVE RISK MANAGEMENT

Recently, the market has seen the frequency and severity of cyber claims continue to rise, resulting in more underwriter scrutiny of companies' cybersecurity hygiene. The significance of **highlighting any additions in cybersecurity staffing or updated system protocols cannot be overstated**.

ENGAGING LOSS CONTROL TEAMS

Consistent communication with your brokers' loss control team is a top priority, especially when a claim arises. Engaging your loss control team in the event of a claim can help minimize the impacts to your business financially and operationally. IMA and partners will work with you to understand your financial goals and operational challenges so we can identify, develop and deliver Risk Control Solutions that strategically align with your objectives.

CONTRACT REVIEW

Our **Contract Review** teams add value to our clients' overall risk management program by ensuring the indemnity language is market standard and doesn't expose our clients to unforeseen losses that may not be insurable. Additionally, making sure Waiver of Subrogation language is correctly written in lease agreements is crucial to not seeing any losses compounded. Your account team can have this language reviewed for optimal results before a claim occurs.

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