2023 US CASUALTY MARKET OUTLOOK

Insights on the current and future state of the US casualty insurance market

RPS RISK PLACEMENT SERVICES

WHAT GOES UP…BECOMES THE NEW NORMAL

If there is one word to describe the casualty market over the last few years, it is growth. After all, nearly 30 new, well-capitalized insurers have come on the scene since 2020, bringing fresh capacity to the marketplace and helping stabilize the rate environment in desirable classes of business like commercial construction and manufacturing.

"From a high level, the casualty marketplace today is starting to level off in pockets and become a little bit more consistent with rate increases," explains Adam Mazan, area president, Southern California, at Risk Placement Services (RPS). "Year over year, you still have some challenging classes – namely habitational, public entity, and education continue to be a challenge due to the lack of capacity in those spaces – but once you get in excess of about $10 million in an attachment point, there are many new carriers that are going after that business."

As a result, he says, the market for some coverages has become very competitive. From a rate increase standpoint, many carriers are trying to get between eight and 12 points of increase this year, knowing that their loss costs are probably going up about 9% on average, but the reality is more nuanced. Most carriers are getting around 10% of rate increase with the first $5 million to $10 million of coverage, but in excess of $10 million the rate increases have been relatively small, from flat to 5%.

"As a broker, it's important for us to seek out new capacity, but frankly we know that some of these new entrants won't survive," says Bill Wilkinson, president, RPS National Casualty Brokerage. I've never seen this much capacity flood into the market in my 33-year career, and I don't think it will ever happen again."

That isn't to say that growth in the overall property and casualty (P&C) market is slowing down. According to McKinsey, annual premium growth rate for commercial P&C lines has remained between 6% and 8% since 2018, and that trend is expected to continue. Rates in casualty continue to increase on multifamily residential projects, especially affordable housing policies, as well as wildfire, land clearing and law enforcement legal liability coverages, all of which are difficult to place in the current environment. And the marketplace is shrinking for anything involving younger children, such as water parks, trampoline facilities, indoor kart tracks and other similar businesses.

"Fresh capacity in desirable classes of business is always good news," says Wilkinson, "but it isn't universal across all businesses."

The challenge is in balancing who gets business in this new landscape, how long they last and what all this dry powder on the market means for strong, long-standing carrier partnerships that cannot match today's lower rates. After all, the industry as a whole lost almost $27 billion in 2022 and the average carrier's combined loss ratio last year was 103%. New capital coming into the market is generally welcome, but participants need to be careful with whom they're working and how stable they are in the case of increased claims. No one wants to be left holding the bag if things turn south.

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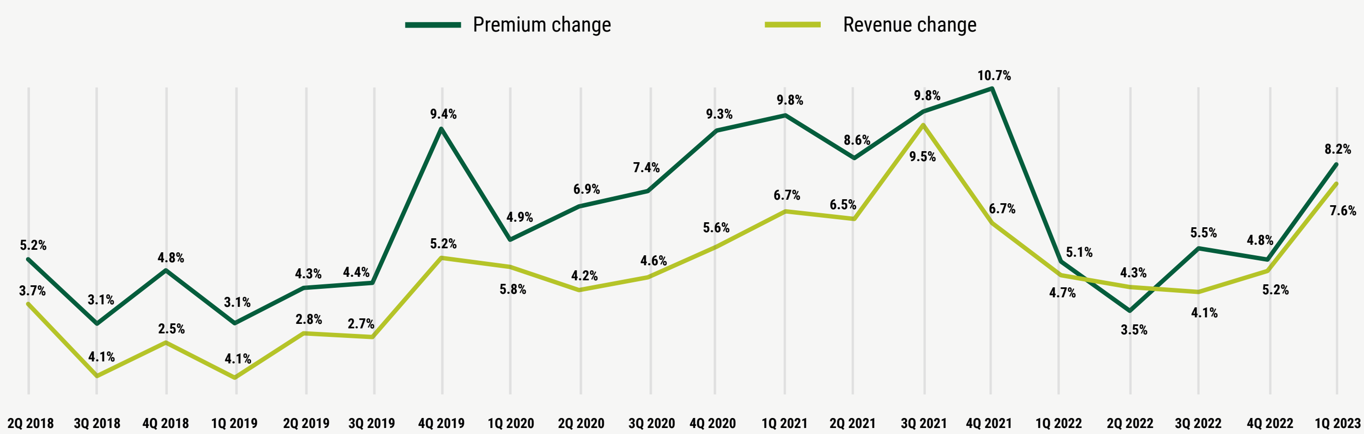
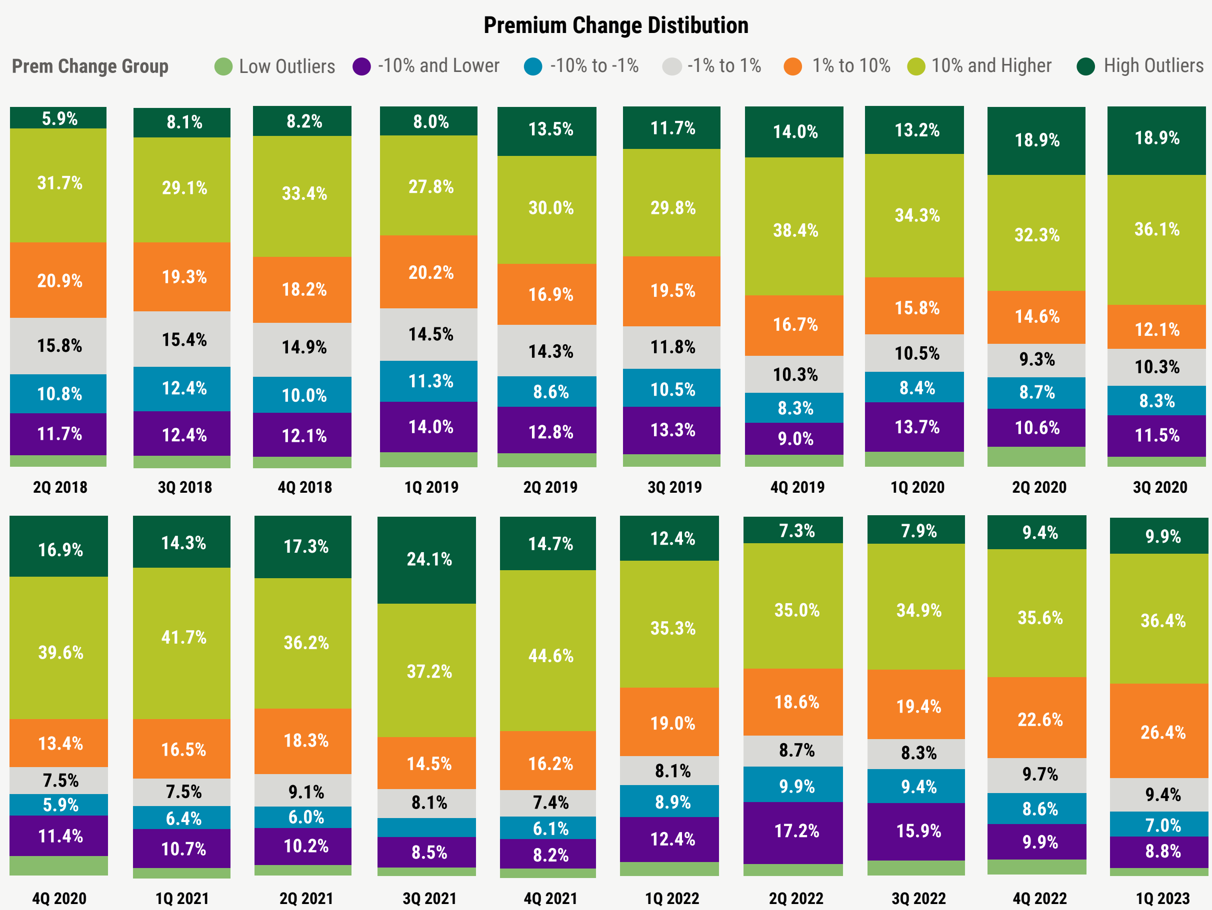
"We recently saw three new transportation partners focused on excess trucking businesses with 250 units or less, and they were undercutting the market by 10% to 30% in some cases," Wilkinson adds. "Then we had three new wrap-up project markets pop up in construction that we're doing the same thing."

INFLATION IN THE SPOTLIGHT

After peaking at 9.1% in June 2022 following more than two years of pandemic-induced growth, global inflation has trended down slowly for the last few quarters. The Bureau of Labor Statistics reported that the consumer price index had settled down to 5% on an annual basis as of March 2023, down a full percentage point from the month prior, though still above the long-term average of 3.2%. This is starting to show up on the personal balance sheets of everyday Americans, as energy and food prices have begun to drop again as day-to-day life becomes more affordable.

AVERAGE PREMIUM AND REVENUE CHANGE TREND





Source: RPS proprietary data (as of March 2023)

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Still, inflation remains a concern across the entire P&C value chain. Naturally, rising costs will have a direct impact on insurers through increased claims costs and other expenses. In late 2022, McKinsey estimated that inflationary forces in 2021 added roughly $30 billion in loss costs to insurers' bottom lines, well above the long-term average.

"Price increases have been exceptionally high for the goods and services that drive personal insurance claims," the firm wrote. "For example, prices for motor vehicle parts and equipment rose 22.8% between June 2021 and June 2022, while the cost of used cars and trucks rose 14%. Supply chain disruptions and other causes of inflation in the automotive industry led to an estimated $9 billion in loss costs for auto physical damage in 2021. Loss costs for lines with long settlement periods, such as workers' compensation, went up by an incremental $4 billion, and high prices for core commodities drove up loss costs in multiperil insurance lines, both personal and commercial, by an incremental $8 billion and $2 billion respectively."

For casualty as of 2023, inflation is causing widespread disruption, from cuts on the binding side by carrier partners to new approaches to sales payroll for wholesalers. As exposures increase, typically premiums do as well at renewal time. That can lead to increased, commissions for salespeople that further erode margins.

Says Mazan: "Inflation's having an impact on medical bills, it's having an impact on auto repairs, it's having an impact on rebuilding from a construction standpoint. That's all driving increasing loss costs, which continue to put upward rate pressure on the excess carriers."

In this environment, market participants need to get creative and find alternative ways to look at exposures for their customers. For example, consider a concrete manufacturing and erection firm that posted $300 million in sales in 2022 that might be projecting $450 million topline in 2023. But that increase doesn't necessarily mean they are producing any more quantity of product than they had in the past. It just costs more now.

"On one of my accounts recently I changed the exposure from sales and payroll to gross tonnage produced year over year," Wilkinson explains. "That was to give the underwriters a better idea of what is going on in the business. Yes, sales are up, but it's due to the rising cost of product and everything else involved. The insured should not be penalized because their exposures are truly not up that much year over year."

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The challenge in an inflationary environment is that rising costs impact every corner of the economy, from construction to manufacturing to services, housing and more. Brokers would do well to consider alternative ways to rate new policies and renewals, getting specific in their exposures to truly reflect what's actually happening in the client's marketplace.

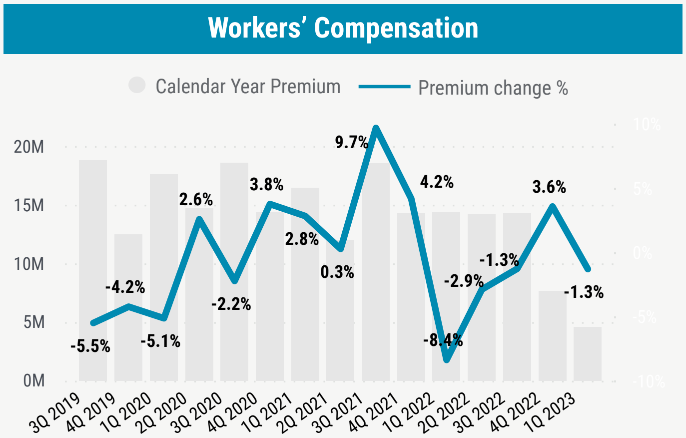
"Many carriers are pushing up rates on general liability to keep up with inflation, which from a broker's standpoint can be really tough," Mazan says. "If you're basing your rate on a sales figure or an inflationary impacted exposure base, and then you increase the rate because of inflation, you're kind of taking a hit twice."

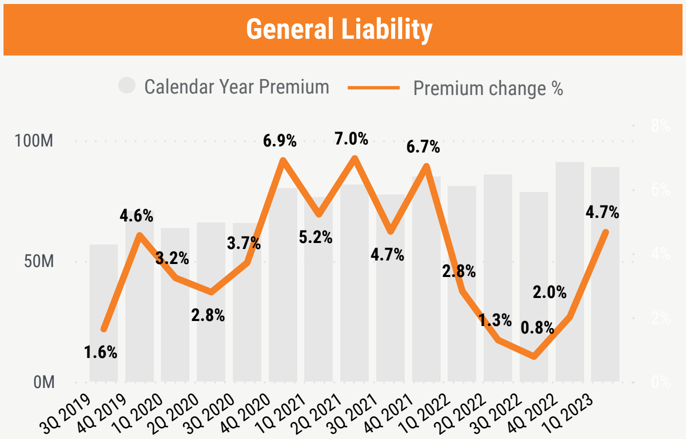
SHIFTING CAPACITY, CHANGING RATES

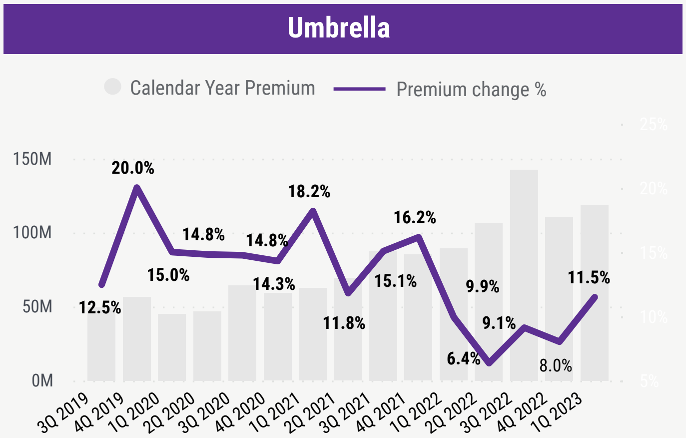
The casualty market has come a long way since 2019, when carriers were commonly putting up in excess of $25 million in capacity at rates as low as $750 per million. Today very few carriers will offer a full $25 million of capacity with most preferring to offer $5 million or $10 million at a time. Pricing is up three to four times over what it was just a few years ago, and terms have become more restrictive.

"Three to four years ago, we were able to build up $100 million in capacity with just three or four markets," Wilkinson says. "Now you need eight or 10 markets to build up $100 million. There's hardly anybody putting out $25 million anymore, and there is a lot of quota sharing going on, which historically we would never even do."

RENEWAL PREMIUM AND PREMIUM TRENDS: TOP LINES







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The good news, explains Mazan, is that brokers are now seeing better limit profiles: “You’re able to come in and actually write business with only $5 million to $10 million in capacity, and you’re getting a much stronger rate than what people had been getting. So from a capital standpoint, it’s no surprise that a lot of new carriers have been entering the market. It just made sense for a lot of people to invest in what has been, according to Lloyd’s, the strongest rate and term environment of the last 30 years.”

So far in 2023, this has translated into some overlap in the market for premium pricing, where a number of legacy accounts have ended up as pricing outliers relative to where the rest of the marketplace is right now. Those accounts are generally coming into line during renewals, but can be a challenge in the short term, in particular those who are facing non-renewal or with carriers that are cutting capacity. At RPS, we’ve seen incumbent carriers at a disadvantage when working in excess of $10 million in 2023 because of the amount of competition and the growth goals that a lot of these new carriers have. That’s a change from the past few years, when incumbents had a distinct advantage over the smaller carriers trying to get onto an account for the first time.

All of this has introduced new volatility into a casualty market that is typically more stable and predictable.

“Going back to 2019, you could send me an account, and I could probably price a $100 million excess placement and be within single-digit percentage points of what the actual carrier pricing would be,” says Mazan. “But now, because there are so many different factors coming into play, we don’t really know how much capacity a carrier may or may not give us. The relativities are constantly changing, and it makes it a lot more challenging to predict what pricing is going to be. While the casualty marketplace is gaining consistency, it’s still a little bit unpredictable in terms of how to gauge what to expect when you’re working on a new deal.”

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INCREASING RISKS IN THE COURT OF PUBLIC OPINION

In 2017, a driver for a commercial trucking company was involved in an accident, flipping his semitruck, and bringing traffic on an interstate highway to a standstill. In a resulting backup, an 18-year-old driver for another commercial trucker, collided with the stopped traffic killing him instantly. The driver of the flipped semi was later found to have been on his cellphone at the time of the original accident, driving in excess of his legal hours limit, and was behind the wheel without a current commercial driver's license.

Four years later, a jury awarded the parents of the deceased a record $1 billion verdict in a wrongful death case, more than double the most expensive verdict involving a trucking company at that point, and the latest in what are known as nuclear verdicts, or any verdict valued in excess of $10 million.

These cases impact not only trucking companies, though that industry has traditionally been overrepresented, but also can touch nearly every industry covered by commercial insurance, including manufacturing, habitational, commercial construction and more. Anything where there is potential for casualty coverage or injury is being impacted by this trend toward large, financially destabilizing decisions.

These types of verdicts have been on the rise for more than a decade. According to a March 2023 report from Marathon Strategies, the median verdict greater than $10 million against corporate defendants is up 55% since 2010. The COVID-19 pandemic shutdowns in 2020 slowed this trend, but it has only accelerated since then. Total corporate nuclear verdicts spiked sharply from $4.9 billion in 2020 to over $18.9 billion in 2022. The mean verdict also nearly doubled in that time to $41.1 million.

Nuclear verdicts threaten not only corporate operations in a wide range of fields, but also their insurance premiums and the insurers behind those policies. After all, insuring a company against potential losses in the normal course of business is one thing. Insuring it against legal decisions that effectively have no ceiling on their value is a different matter entirely.

"These juries are more focused today on injuries and damages and not on liability," says Wilkinson. "It used to be that, in the case of a claim, you would evaluate liability, look at what the insured did wrong versus what the claimant did wrong, and portion fault in a way that determines a reasonable settlement. With these verdicts that just isn't happening."

According to Chubb Bermuda's 2022 Liability Limit Benchmark & Large Loss Profile report, three industries—manufacturing, oil and gas, and utilities—each saw verdicts or settlements worth $1billion-plus in the last year, while four others—chemical, life sciences, real estate and hospitality, and transportation—each had verdicts of up to $800 million. Consumer products, healthcare and construction all saw decisions between $110 million and $384 million in 2022.

This trend toward larger verdicts against corporations has, not surprisingly, attracted interest from third-party investors who are willing to help fund litigation in exchange for a portion of the plaintiff's recoveries. Arrangements of this type reached $17 billion in 2021 according to Chubb, and show no signs of slowing down.

The prevalence of nuclear verdicts varies from state to state and jurisdiction to jurisdiction, with Georgia replacing California at the top as of 2023, according to the American Tort Reform Foundation's (ATRF) most recent Judicial Hellholes report, in large part due to a recent $1.7 billion verdict in the state. But Georgia has been growing into this position for some time. From 2010 to 2019, the state saw 53 nuclear verdicts in personal injury and wrongful death cases, totaling more than $3 billion. Per the ATRF report: "The recent dramatic rise in nuclear verdicts can be attributed to several factors, including the state's allowance of 'anchoring' tactics by plaintiffs' lawyers. Anchoring is a tactic that lawyers use in order to place an extremely high amount into jurors' minds to start as a base dollar amount for a pain and suffering award. While some states have laws that prevent or limit this tactic's use in a courtroom, Georgia is one of a few that has a specific state statute allowing the practice."

According to ATRF, the top five jurisdictions for nuclear verdicts are rounded out by the Pennsylvania Supreme Court; California; New York; and Cook County, Illinois, which accounts for Chicago. And some surprising new localities are beginning to emerge. For instance, Texas was home to 10 of the top 20 nuclear verdicts in 2022 despite its reputation for less judicial activism.

With regulatory relief still to come, brokers and their clients are being forced to take steps to minimize their exposures to nuclear verdicts using any means possible. Plus, although the $1 billion verdicts grab the headlines, a steady drumbeat of smaller but still significant verdicts is having a direct impact on the casualty market.

"I had one of my insureds do a mock trial about six months ago," says Wilkinson, "and instead of having one jury pool try the case, they decided to have two jury pools. These two jury pools went into separate rooms, and jury A came back with a verdict of $5 million while jury B decided it should be $100 million. The client spent a lot of money for a mock trial and I'm not even sure where they got the answer they wanted. There's just so much uncertainty."

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TECHNOLOGY MAKING A DIFFERENCE

As recently as the 1970s, the UK had roughly 60 CCTV security cameras in use across the country. Today, that number is well over 6 million. It's the same in the US, where more than 10 million cameras were installed nationwide as of 2020, according to IHS Markit. That number has only continued to climb with the increased usage of dashcams in cars, doorbell cameras in homes and overlapping security cameras at many businesses, often equipped with facial recognition technology.

This new reality is also changing the game for insurers.

Today the majority of large commercial trucking companies have forward-facing cameras installed on their rigs, to monitor driver compliance and provide evidence in the case of an accident. More than a few insureds have been exonerated in many casualty claims as a result of that video evidence. The same can be said for slip-and-fall cases, apartment claims, personal injury, and a wide range of other claims.

The trouble is, even with the growth of camera installations, not every place that's covered has a camera. This is particularly the case with smaller clients that aren't able to fund a full video security system. After all, a $1 billion trucking company with 2,000 units in the field is likely better able to install cameras in each of its tractor trailers than a small family business with just a few trucks might be.

"Technology is key, especially for truck risks," Wilkinson says. "Now we have everything from driver-facing cameras to forward-facing cameras, lane departure detection devices and more going into these trucks. Even technology that can detect what's going on with the driver's eyes and whether they're paying attention or not."

COVERAGE FOCUS

As is typically the case, while some parts of the casualty market are facing more difficult conditions, other areas are seeing more positive performance. As of 2023, the bright spots are focused on products, manufacturing and commercial construction, all of which are seeing a lot of interest from clients as well as plenty of capacity to write contracts. This comes as no surprise, as all three are typically high severity but low frequency in terms of claims. There simply won't be a large number of claims for those lines.

Even wildfire, which has been tough for the last several years due to increasing fire instances in the Western US, is getting a little easier to place due to increased capacity, as rates have increased.

That said, nothing is truly "easy" these days. Every market has its nuances and challenges, and casualty is no exception. Those brokers who are able to specialize in one or more industries will be best positioned to spot emerging opportunities and bring real value to their clients in these changing times.

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ENERGY

The energy market is unique in insurance due to the fact that it is based on commodity prices—the price of oil, natural gas, etc.—that fluctuates just as the insurance markets do. Sometimes those trends move in conjunction with each other and sometimes they are opposed, but right now we're seeing rapid growth in both sectors, explains Grant Bryant, senior vice president, Energy and Environmental at RPS.

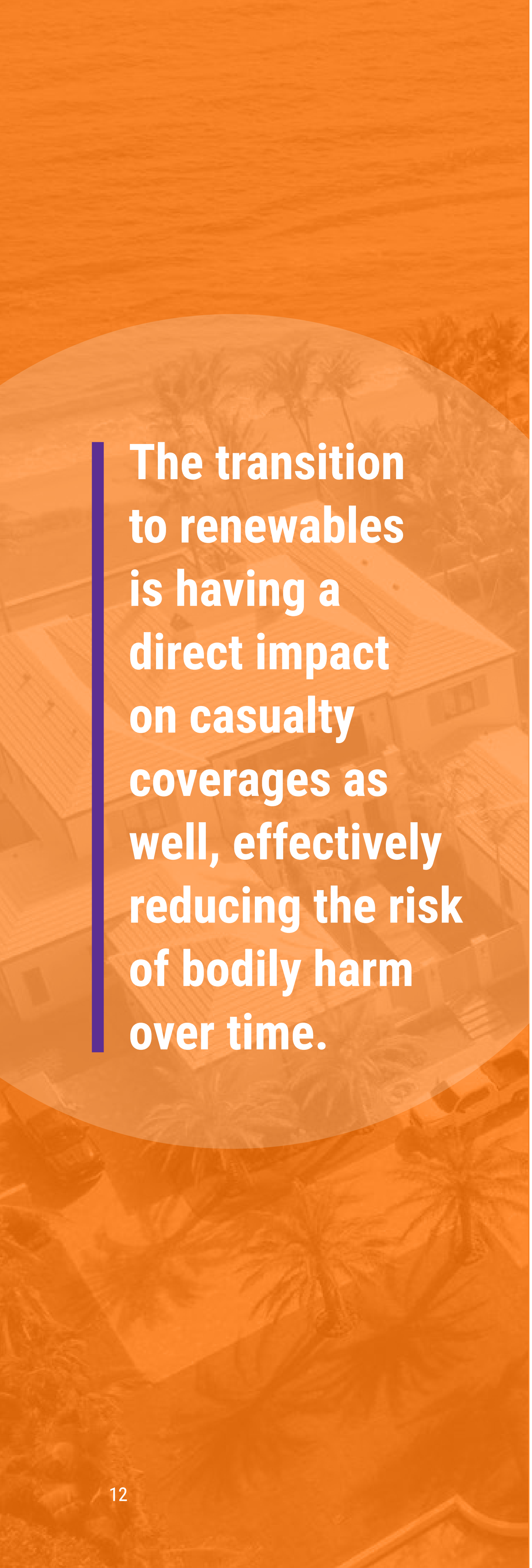
"There is more capacity out there than we've seen in the oil and gas space in years," he says. "And to go along with that capacity are the new insurance requirements of our clients."

Clients in oil and gas are facing demands to carry higher limits on their coverages. In the past an upstream (that extracts oil or natural gas from the ground) or midstream (that transports those products to their downstream destination) company might have been able to get a $5 million excess policy that covers their primary liabilities, now it is more common to see at least $10 million umbrella requirements across the board. As a result, demand for casualty and other coverages is high across the energy industry in 2023.

In energy, there are always ebbs and flows as we look to get what we need to power the United States." Bryant explains. "Natural gas and oil look to be a part of that for the foreseeable future, even though we're seeing a big push to electrify everything and move to renewable smart grids. As I see it, everybody just wants to have a little bit more protection for their assets."

As part of this broader transition to renewables, new regulations are emerging, especially on the environmental side, to dictate what energy companies need from an insurance standpoint. This has so far included things such as operator's extra expense coverage, which applies to those companies working to install new renewable infrastructure in place of old abandoned oil and gas wells. These are facilities that might have been abandoned decades ago, so the process to make them viable again is being heavily regulated by local and state governments, adding to new costs for clients.

Casualty claims exposure in energy is most commonly related to accidents that occur on oil and gas sites. Whenever a landowner leases part of their land to an energy company to generate oil and gas production on it, the company has a responsibility to ensure that the site is a safe place to work for their employees and subcontractors. That often results in contractual agreements between both parties in the form of a master service agreement, which puts the indemnifications on each party.



> **The transition to renewables is having a direct impact on casualty coverages as well, effectively reducing the risk of bodily harm over time.**

When considering midstream companies, most incidents involve pipeline trucking, though environmental exposures related to leaks and other incidents are on the rise, Bryant says. These accidents can be as simple as leaving a tank open or not properly doing a lockout at a worksite that results in an injury.

“A lot of the policies that we’re placing are on a combined form,” he explains, “with the general liability for pollution and professional coverage all wrapped up in a single package.”

The transition to renewables is having a direct impact on casualty coverages as well, effectively reducing the risk of bodily harm over time. As Bryant explains it, a renewable energy site is fairly similar to a traditional oil and gas site throughout the construction process, with all the same risks. But, once brought online, renewable sites are fairly hands-off and don’t require much operational attention or maintenance, unlike oil and gas. There is no pumping equipment, no meters to check, no materials that need tending by on-site staff. As a result, these installations post more of a property risk than casualty.

“A lot of this renewable work is also being government funded, with a lot of it even being foreign owned,” Bryant explains. “So we’re just not seeing a lot of opportunity in the renewable space. From an overall casualty standpoint it doesn’t pose as much of a risk because there’s not as many contractors on site once it’s completed.”

HABITATIONAL

While the deadly Surfside building collapse in Florida in 2021 drew national attention to the state’s aging housing stock, the slow pullback in condominium insurers in the wake of that incident might be the biggest indication of what has been happening in habitational coverage over the last few years. According to the Insurance Information Institute, condo associations in Florida are seeing premium increases ranging from 30% to 50% at renewal, with some reports of more than 100% increases.

But it’s not just Florida, and it’s not just condos.

The rise in everything from assault and battery claims to habitability claims to human trafficking claims and more means the habitational sector continues to be a challenge for insurers, and it is getting worse.

"From a habitability standpoint, we're starting to see claims in new places," Mazan says. While habitational claims were traditionally more common in California, now insurers are starting to see claims in Texas, Georgia and Florida. Georgia in particular has become a challenge due to assault and battery claims in recent years.

"You're seeing more issues pop up across the entire habitational line of business versus what it was years ago when it was predominantly slip-and-fall exposure," he says. "Now, not only are the costs of slip-and-fall claims increasing, but you have violent crimes, human trafficking, and then habitability all thrown in there too, which is making the market more challenging than it had been in the past.

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This is playing out in rates and coverages as well. As recently as 2020, the rate per door for many habitational policies averaged between $40 and $50. Today it is closer to $100 a door. So not only do clients in habitational have broader exposures from all the units they have under their policies, they are also facing higher rates per unit, and those rates often come with more restrictive terms than what was being offered just a few years ago.

It's getting tighter and tighter, explains Wilkinson: "I worked on one habitational renewal recently where there were only five general liability markets willing to entertain it. Two of them had been on it in the past and didn't want any part of it, so I was basically down to three markets. The carrier that's on it now that we renewed with is looking to get out next year, which will leave us with one or two. There's nothing available in the London marketplace, so many of us are still trying to find solutions for this type of business."

LOSS CHALLENGED AREAS

Broadly speaking, casualty is facing headwinds in a number of markets. For instance, law enforcement continues to be a challenge, with carriers increasing attachment points, reducing limits on offer for law enforcement or even excluding it altogether. The same can be said for markets like active shooter and sexual abuse and molestation, all of which are seeing increasing claims and rising claims costs.

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Explains Mazan: "That exposure used to be isolated to the education space, but it's now transcended across any account that has youth exposure in it." That can include zoos, charitable organizations, municipalities, fitness facilities, recreational facilities and more.

Other challenging segments in casualty are more niche, such as agriculture. Growers of leafy greens, for example, are facing a limited marketplace for coverage for farmers, processors, shippers and distributors. "It's not quite as bad as those accounts with abuse exposure," says Mazan, "but it can be difficult due to the limited number of carriers willing to participate in this space."

In addition, ongoing increases in nuclear verdicts has led to new risks for any businesses with foot traffic, like hospitality or bars and nightclubs. It's currently very difficult to place these policies, because carriers are trying to sublimit things like liquor and assault and battery coverage. And that trend appears to be sticking around. Wilkinson says that he has tried to sell deals without a sublimit, but in many cases you have no choice but to go with the carriers not providing as much coverage as you'd like.

WHAT'S NEXT FOR CASUALTY?

As much as things change, the basics of the casualty business tend to stay the same. Generalist agents can do well, but thinking more like a specialist can pay dividends in mixed markets like what we're seeing today.

Wilkinson suggests thinking about practice growth in terms of buckets of business, lumping potential clients together based on classes of business and targeting just those with the best opportunities. Right now, that means he's focused on manufacturing, construction, habitational, hospitality and excess trucking. From there, it's all about being strategic with outreach, he says.

"In construction, for example, I'll say here's the top 10 cities with the largest number of cranes. Go get 'em. Or here are the largest ports of entry that deal with the most imported products. We're trying to be a little bit more strategic and have had good success doing that."

The key is to bring a specialist mindset to a range of different markets. It's difficult to be a true generalist these days, in part because of how many markets are available and how many relationships agents need to foster across all those markets, but the lessons of the specialist still apply. That's why more regional agencies as well as the larger independents are becoming more niche-driven and focused across their producer teams. They're better able to compete with the larger players that way. Small independent agencies serving up to $1 million accounts continue to be generalists, though that approach will increasingly hamstring them in an evolving and segmenting marketplace.

"If you look at the industry as a whole, there are still a lot of generalists out there," says Mazan. "Their success depends on the type of business they're going after and how deep they can go. But when you get into very specialized segments like education, you need to be very specialized yourself. The brokers targeting that business typically have a large portfolio of that business."

The casualty market has undergone some wide-ranging changes over the last several years, and if we've learned anything since the COVID-19 pandemic it's that not everything returns to "normal" over time. In casualty, the new normal for agents is more specialized, more targeted and better attuned to the overall trends shaping the market. Not all segments will do well at the same time, but as capacity has grown across the board, new opportunities have opened up for agents who know their markets well and are best positioned to work with them.

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