State of the Insurance Industry

AVANT Insurance Brokers Ltd.

2020 Insurance Company Financials are showing improvements in loss ratios and overall profitable results, pleading the question of how long the hard market will last.

March 26, 2021

2020 was a year we will never forget, it was hard for all of us. Within the insurance industry, 2020 was literally "hard" while we faced, and continue to face, a hard market. This type of market sees insurers reducing their capacity (amount of risk in dollar values that they are willing to accept), increasing their rates (not just specifically in poor performing segments), and being more selective in the types of risks they are willing to insure. Insurance rates fluctuate much like a bank's interest rates, and it was argued in early 2020 that we weren't in a hard market yet. While several segments (hospitality and residential realty for example) had been seeing increases for years as they performed poorly, competition was still fierce for other classes of business. The ebb and flow of insurance rates are based on insurance company results. As the insurance marketplace gets softer, capacity increases, sometimes as a result of new insurance companies introducing themselves to our profitable Canadian Insurance market.

As a result, rates are driven down by eager companies who are more flexible on their appetites to meet production goals. Over time, unprofitable trends emerge in segments and insurers must increase rates. Their responsibility being in the ability to pay claims and make good on every promise made via an insurance policy. The last hard market for commercial insurance was in 2002 so we have been in a soft market and had insurers competing and driving down rates for almost 20 years. Surely a soft market had to end at some point, and the COVID-19 pandemic ensured the hard market's introduction with unique elements.

"The pandemic created a perfect storm as it relates to the current hard market"

The pandemic brought a lot of uncertainty to the insurance market and the financial crisis that was expected as a result. The lockdown meant commercial businesses were closed and vacant buildings are more prone to losses when no one is there to see and hear things going on. In poor economic conditions, traditionally crime rates rise. And for the policies that were sold, could people pay their bills? Luckily, the state of emergency came with implications for insurers meaning that they had to give payment flexibility and there was essentially a "hold covered" protocol in place that even required them to hold coverage for a certain time period after a policy's expiry if alternate coverage could not be placed. We are still in a state of emergency that insurers are still adhering to.

These uncertainties plummeted us into an unarguable hard market. Despite the state of emergency protocols, it has not stopped insurers from infringing stricter underwriting guidelines and imposing unexplainable rate increases. New business that was once eagerly written by insurers is being declined, in some cases directly because of the pandemic and in other cases, citing changes to appetite although the underlying tone IS the pandemic. Insurers and brokers alike, some better than others, scrambled to continue operations with employees at home – some while still trying to work with paper files.This also presented a difficulty within the hard market as it meant a substantial amount of back log and service issues making the insurers more inclined to just “say no” and move on to the next. It was in essence a perfect storm, and while they may deny it, the “hard” truth is, some insurance companies used the pandemic to their advantage to clean up the unprofitable business that a 20 year soft market built.

The accountability and proof in the pudding however is in the insurers results. Published by the Office of the Superintendent of Financial Institutions (OSFI) who regulates Canada’s insurers, it shows some expected trends but overall a profitable fourth quarter. In Q4 of 2020, the insurers posted an underwriting profit of almost $2 billion, this a considerable increase from 2019 Q4 which was closer to $500 million. While that was their profit, their overall net written premium increased by 13%. In the most general and overall way, the hard market has increased premiums by that percentage. The increase in profits is a result of the increased top line income along with some good and bad results to loss ratios. Personal lines and automobile Insurance carriers benefited in 2020 Q4 from people being at home so losses reduced; however, people working from home caused a drastic increase in Cyber liability claims resulting in a substantially increased loss ratio in that segment.

Overall the property insurer’s loss ratios decreased approximately 10%, even commercial property loss ratios have shown a downward trend. Commercial general liability loss ratios have decreased slightly overall, however, along with an increased loss ratio for Cyber Liability, For Profit Directors and Officer's Liability loss ratios also increased as many boards saw lawsuits for mismanaging their business through COVID pandemic.

While these results seem positive on the surface, we predict minimal changes to how Insurance Companies adjust their strategy in 2021. In the coming months as Insurance Companies review and analyze their own personal results, their strategies will include much of the same uncertainties as the year prior. The very predominant issues we face today is that the indicators that generally allow us to see the hard market coming, didn’t occur with this hard market; or at least not completely. While loss ratios were trending in that direction, they weren’t there yet and the pandemic accelerated the process. In reviewing positive company results, the most literal observation is that these results could accelerate us out of the hard market. History tells us that most hard markets last for 2-3 years. The long tail effects of the pandemic remain to be seen but it’s definitely the “chicken before the egg” analogy. Since the insurance industry and the economy are interdependent (the insurance industry providing jobs and taxes on premiums and providing security such as mortgages that are insured, all allow the economy to flourish and in return, in a healthy economy insurers benefit as there are more homes and businesses to insure) if the insurance industry refuses to reduce their stringent hard market underwriting guidelines such as requiring a business be in business for more than 3 years, or refusing to insure buildings built before the 1950’s therefore not allowing someone to get a mortgage, our economy will suffer far longer than it has to.

A year into the hard market, the results show positive developments and allows for the potential of insurance companies to begin to loosen their restrictions. As we all begin to rebuild, reintroduce and regain after this pandemic, we will continue to advocate for the good of the economy by supporting our industry and encouraging it to fulfil this important societal financial need.