Challenging Headwinds in the Excess Casualty Market

Introduction

The U.S. Excess Liability insurance market began showing signs of greater underwriting discipline in Q1 2019 and transitioned into a firming market in Q2 2019. The quantum of capacity restrictions and pricing increases has accelerated significantly in the last sixty days, leaving many risk managers with mid-year renewal programs experiencing significant challenges with program structure, available capacity and pricing. For several years, insurers have warned of the need for rate improvement without success. In the first two quarters of 2019, insurers have moved the market, impacted by the following factors:

- Years of declining premium rates against exposures (nine of the past twelve years have seen average premium rate declines)
- Increased frequency of severity outpacing any meaningful movement in rates
- Large loss events yielding nuclear jury verdicts and pushing up the value of negotiated settlements
- U.S. medical cost inflation and advancements to improve quality of life for the injured
- Growth of industry catastrophic exposure including wildfires, opioid epidemic, gas explosions, mass shootings and terrorism, traumatic brain injury
- Continuous improvement in science and technology to identify losses and their causes as well as increased publicity including social media and product recall announcements
- 'Social Justice' sentiment among certain groups of people, including anti-corporate philosophy leading to desensitized view of enormous jury awards. "Reptile Strategy" implementation in litigation has further exacerbated this trend
- Erosion of the concept of fault
- Lack of reinsurance capacity in the primary buffer layers, especially for auto risks
- Increased focus on non-owned vehicles and the impact on auto attachment points
- The advent of third party litigation finance to support plaintiff action

While insurers have always maintained that they underwrite each client individually, of late the marketplace is driving up rate in a very coordinated pattern. Many insurers are focused on rate adequacy across their book to address overall profitability goals which is difficult when coupled with client specific experience or loss mitigation efforts. To address this, Aon works diligently with our clients to differentiate their unique risk and help insurers to quantify the value of client investments in safety, product efficacy, and overall risk avoidance techniques. In addition, evidence still prevails that long-term, high-quality relationships with the insurers benefit clients in both renewal and claims outcomes. We have see the benefits of this approach pay off for our clients.

The pressures of the factors together with capacity restrictions and reductions in the Excess Casualty market are creating significant challenges for many of our clients.

We're here to empower results

If you have any questions about your specific coverage or are interested in obtaining coverage, please contact your Aon broker. For general inquiries about Excess Casualty, contact:

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The "Here and Now" of Capacity and Pricing

Capacity

As mentioned, we have seen a continuing constriction of available capacity for Umbrella and Excess Liability placements. Since mid-year 2018, more than $250 million of capacity has disappeared from the marketplace. This reduction has affected the markets in the U.S., Bermuda and particularly in London. These reductions in capacity manifest in many ways:

- Insurers who have ceased writing Excess Liability completely
- Insurers who have reduced available capacity across the board
- Insurers who have reduced available capacity for certain classes of business
- Insurers who are managing deployed capacity by size of Insureds
- Insurers who are aggregating capacity across their geographical platforms
- Insurers who are deploying less than their full capacity and or positioning their capacity at different positions in the tower

All of these changes have caused considerable disruption in the market. There are insurers who theoretically have not reduced their capacity, but in reality are deploying less. This is evident for lead Umbrella placements. Many carriers who write in the lead Umbrella space are reducing limits deployed. The $50 million lead layers that were available in the past are for the most part gone, and $25 million layers have been reduced in many instances to $10 to $15 million for larger clients.

This current pressure on capacity is rivaled only by the pressure for increased rate. The combination of the two has resulted in a significant shift in the profile of the lead Umbrella placement, as well as continued pressure on pricing throughout the remainder of the tower.

In addition to the lead Umbrella, available capacity has been reduced and/or is being managed in the excess layers. Capacity is being affected by class of business, coverage provided and overall aggregate exposure of the insurer. Excess layers are not immune to many of the realities outlined above for changes in underwriting appetites and deployment of capacity that we are witnessing across a wide array of insurers both domestic and global. All of these factors are multiplied considerably for accounts which have experienced recent loss activity. In addition, accounts that buy significant towers of insurance (more than $500 million in total limits) are experiencing difficulty in generating enough competition to help defray significant pricing increases. If the client is considered to be 'challenged', some are finding it difficult to duplicate the limit previously purchased at any cost.

Pricing

For the second quarter of 2019, more than 70% of our clients have experienced rate increases, even those with declining exposures. In 2018 and prior periods, clients with exposure change (growth or decline) were more likely to see declining premium rates. The magnitude of pricing and rate increases has accelerated significantly in Q2 2019, and the trend is continuing into Q3 2019.

About Aon's U.S. National Casualty Practice

Aon's U.S. National Casualty Practice is the premier team of casualty broking professionals, with extensive experience in representing buyers of large and complex insurance and risk financing products including primary casualty & collateral, umbrella & excess, loss portfolio and structured transactions, excess workers' compensation and non-subscription, complex claims advisory, and data and analytics with partner resources across Aon's industry practice groups, Aon Global Risk Consulting, and Aon Global Client Network. Casualty's global platform assists clients in addressing their casualty exposures across their worldwide operations. Aon's casualty team places more than $4.7 billion in annual premiums from the U.S. and uses its unmatched data to help empower its clients' diverse business goals and results.

Average tower rate and/or premium increases for many large clients without loss experience in the umbrella/excess tower has now reached double digits. For those clients that have experienced losses or are in a class of business considered ‘challenged’, the increases may be materially higher. We have seen increases as high as 200% to 300% for classes considered to be severely stressed (including Trucking), and have seen everything in between. We have experienced increasing volatility in the Excess Liability market throughout 2018 and now into the first half of 2019. We don’t anticipate this trend slowing in the near term as the market is seeking to find a ‘new normal’. Indeed, it is clear that the marketplace is focused on premium growth more so than rates. Evidence of these trends within Aon’s excess casualty business include:

- Average umbrella/excess rate change is at the highest level we have seen in the last 10+ years
- 70% of umbrella/excess accounts experienced a rate increase in Q2 2019, double the number of accounts with rate increase in the same quarter last year
- Average July 1 premium increases for total umbrella/excess towers has reached double digits
- For third quarter renewals to date, over 30% of clients experienced a structural change to their program (i.e. lead limit reduction, attachment point change)

Coverage

The most significant change we have seen is the elevated pressure by insurers on increased attachment points for lead Umbrella layers. This is particularly true with respect to Automobile Liability attachment. Despite the increase in attachment, the push for rate shows little leniency for the change in attachment points.

The breadth of coverage we have seen in Excess Liability programs has stabilized with very little broadening of terms and conditions taking place. Coverage for certain classes of risk continues to be restricted or is diminishing. Insurers continue to explore coverage specific restrictions or evaluations for certain products, or risk classes including:

- Wildfire
- Implantable Medical Devices, pharmaceuticals and medical product distribution
- Opioids
- Traumatic Brain Injury
- Certain transportation risks, including those accounts with a contingent exposure
- Cannabis related exposures
- Electronic Data Events
- Certain types of chemical compounds such as glyphosate, diacetyl, etc.

Conclusion

In summary, many clients are experiencing a ‘perfect storm’: reduction in available capacity, increased pricing, and potential reduction in coverage afforded, both in terms of policy language and forced higher attachment points.

To help create competitive options for clients and to strengthen the industry, Aon has invested in building new market capabilities and resources. These include but are not limited to the Aon Client Treaty (ACT), which expands capacity for most annual and multi-year contracts within the London market, Lloyd’s Lead Aon Excess Facility (Aon LLEAF), a proprietary facility for lead layer Umbrella and excess liability placements, and Aon Overwatch, a newly created, London-based dedicated facility to help protect our clients from the effects of events of malicious violence, including Active Shooter events. Further, we have made significant investments in data and analytics. These investments deliver highly valued loss and program design analytics which ensure our clients not only have unique insight into their risk profile, but also assist in making the most informed risk decisions.

About Aon

Aon plc (NYSE:AON) is a leading global professional services firm providing a broad range of risk, retirement and health solutions. Our 50,000 colleagues in 120 countries empower results for clients by using proprietary data and analytics to deliver insights that reduce volatility and improve performance.

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