Market Insights - June 2020

SUMMARY

As the COVID-19 pandemic continues to unfold and impact many in the ways they live and do business, the insurance industry will have to adapt and keep navigating through a variety of unexpected challenges in 2020.

In 2019 we had a year of great transformation in the real estate insurance market. Rising global claims from weather related catastrophic events, which keep becoming more frequent and severe, continued to impact portfolios.

The hard market environment saw insurance companies increase rates and deductibles while at the same time restricted their involvement in the residential sector. These conditions have continued into 2020 with the impact being felt by nearly all strata and condo corporations.

2020 MARKET OUTLOOK

While the future of the insurance market is very difficult to predict, there are a few key indicators that can help us understand how long the hard insurance market will last and what the post-COVID-19 recovery could look like.

Insurer Performance

While the increased rates and deductibles will have a positive impact on the industry in the future, this will take time to be realized in the insurers' results. Until these increases are fully earned, the historic poor performance and high claims costs of the multi-family residential segment will remain.

Low Interest Rates

A difficult investment environment has resulted in lower investment income, which usually makes up for any deficiencies in premium pricing for insurance companies. This compounds the need to increase rates.

COVID-19 Effects on Residential Strata/Condo Insurance

In general terms, the insurable loss from the marketplace is still being realized. For the strata and condo clients, there is typically no property coverage for communicable disease.

COVID-19 AND INSURANCE

Property Changes

The intention of the typical property policy for strata and condo corporations has always been to exclude financial losses, if not the result of a covered property damage event. With the introduction of COVID-19, this has come to the forefront. To ensure absolute clarity, insurers all quickly introduced absolute exclusions to ensure that any losses related to the virus were clearly excluded. While the wording has become more clear, and absolute in nature, the coverage outcome remained the same as the initial intent.

From the onset of COVID-19 we have received, and, continue to receive, questions relating to rental losses due to tenants inability to afford rent due to financial hardship. Unfortunately, this continues to be an uncovered loss under the Strata and Condo Protect programs. Owners should be directed to their personal insurer to determine if they have coverage directly.

D&O and CGL

Currently, there is no exclusion specifically for Covid-19 related claims under the CGL and D&O policies. However, it is important to note that coverage is dependent on the allegations made on the notice of claim. As insurers wrestle to understand the impact of COVID-19, be prepared for exclusions to be implemented upon renewal of policies. All actions brought forward as a result of communicable disease or virus, will be excluded.

As is the current process for all legal matters, each claim will be reviewed independently and coverage determined based on its own merits. As soon as any notice of claim/dispute or demand letter is received, please forward to our claims department for immediate review at: realestateclaims@bflcanada.ca

MARKET IMPACT ON REAL ESTATE

Strict Underwriting

Poor global and local industry performance has led many insurers to stop insuring the strata and condo class of business altogether, or greatly restrict their involvement in this class of business.

Rising Premiums

We observed premiums quickly accelerate throughout the year increasing to anywhere between 50-400% in very extreme cases.

Deductibles Increases

Owners also felt the impact of increased deductibles with some reaching up to $500,000. In some extreme cases stratas or condos were left being unable to secure insurance coverage at all.

Late Quotes

The reduction in capacity limits the options available in the marketplace which means that it is harder to find full placement so quotes are renewed at the last minute.

PROGRAM PLACEMENT CHANGES

This withdrawal in capacity from traditional insurers in the segment has in many cases forced a change in how a typical placement is performed.

Brokers now need to rely on insurance companies that traditionally have not participated in this class. This, in many cases, has meant that insurance policies needed to be restructured from the traditional participation to primary and excess placements in order to offer full limit coverage. In some extreme cases loss limit policies have been the only option.

Traditional Quota Share Structure	Primary/Excess Structure	Loss Limit Structure
Insurer 5 25%	**Excess Insurer 2**	**No Coverage**
Insurer 4 15%	**Excess Insurer 1**	Primary Insurer 4
Insurer 3 15%	Primary Insurer 3	Primary Insurer 3
Insurer 2 15%	Primary Insurer 2	Primary Insurer 2
Insurer 1 30%	Primary Insurer 1	Primary Insurer 1
Result: 100% Full Replacement Coverage	Result: 100% Full Replacement Coverage	Result: <100% Replacement Coverage

HIGHER RISK PROPERTIES

Most properties have seen or will see the impact of the hard market conditions but in particular four property types have experienced acute challenges:

High Earthquake Zone

Insurance companies use sophisticated computer models that determine risk. These models estimate the building damage in any one area.

Wood Frame Buildings

Wood frame buildings have historically seen large claims payouts due to fire loss, coupled with water damage that affects all types of buildings in the sector.

Larger Valued Properties

Larger properties require more insurance companies to share the risk and so brokers have to look further afield for support and that support often comes at a cost.

Properties with Poor Loss Record

Properties that have experienced loss in the past are less desirable to insurers.

BFL CANADA

Market Data

BFL CANADA

Summary of key industry shifts in the real estate market over the past few months. Data on the impact of COVID-19 pandemic on the insurance industry is still being collected and it is expected to significantly affect every industry across the globe.

LESS SUPPLY, MORE DEMAND

The insurance market saw a reduction in available insurers with an increased demand.

30% +
Supply Reduction

Supply reduction due to:

— Poor insurer performance;
— 30-40% reduction in insurer residential capacity

Demand increase due to:

— Increased replacement values approx. 3-9% More buildings being built;
— Larger buildings being built;
— Higher value buildings being built.

CLAIMS ON THE RISE

2010-2019: The Globe's Costliest Decade

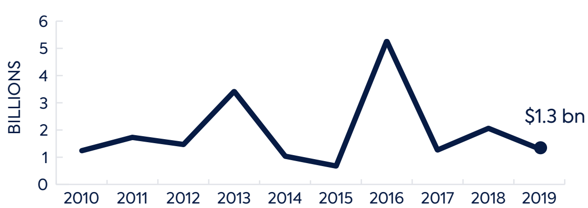
Insurers have seen record-breaking losses from earthquakes, tsunamis, tropical cyclones, severe convective storms, inland flooding, wildfires, droughts, extreme heat and extreme cold adding up to payouts totalling approximately $845bn USD.

2019 Global Snapshot

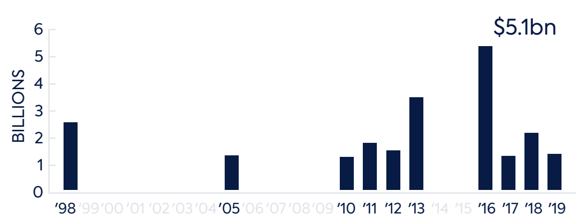
— $71 billion insured losses (USD) + 6% above avg.;
— 12 billion dollar insured loss events;
— 409 natural disaster events;
— Flood, Tropical Cyclone, Severe Weather were the costliest perils.

CANADA AT AT GLANCE

Losses in Canada - Last 10 Years



Top 10 Highest Loss Years on Record



Unpredictable Severe Weather

In 2019 multiple severe weather events contributed to approximately CAD $1.3 bn in losses, the 7th highest year on record.

Data Sources: Insurance Bureau of Canada www.ibc.ca
AON Weather, Climate & Catastrophe Insight 2019 Annual Report