Reinsurance Capacity

The Impact of Catastrophic Events on Insurance

When a catastrophic event occurs, such as the severe storms striking the Midwest during the first half of 2020, devastating fires in the Western United States, and COVID-19, losses are partially insured by another level of insurance called re-insurance. Prior to COVID-19, years of catastrophic events heightened the need for reinsurers to address their capacity and tighten their underwriting guidelines. The current hard market was caused in part by natural or severe catastrophes, making the hard market dynamics better understood through the dynamics of the reinsurance marketplace.

Understanding Reinsurance At-a-glance

Primary insurance carriers look to transfer or offset a percentage of their risk to reinsurers. By transferring some of the financial consequences, primary insurers gain several benefits, including some financial protection from potentially-catastrophic events. Depending on the conditions agreed upon between the primary and reinsurer, a reinsurer will either absorb losses incurred over a certain threshold or will share a portion of the financial consequences with the primary insurance carrier.

The primary insurer pays a premium to the reinsurer for the protection. This relationship is why when reinsurance rates increase, insurance carriers raise their premium rates. At 2020 June-July renewals, reinsurance pricing was up between 5-35%.

Munich Re, an international reinsurer, noted that over the first half of 2020, natural catastrophes resulted in estimated losses of $68 billion, with $27 billion absorbed by reinsurance. Over the past ten consecutive years of catastrophic losses, premium rate changes have remained stagnant or diminished, and not adequately adjusting for the losses. Causing reinsurers in the present market to increase their attachment points in an effort to adjust for the severity of losses. COVID-19 losses are forecasted to reach $107 billion in covered losses. Which means the recovery period for their capacity will require a more dramatic correction timeline before we start seeing a change in appetites or pause to premium increases.

Prior to the pandemic, reinsurers were working to stabilize performance and address capacity and will continue to do so as the severity of COVID-19 is realized—directly impacting the cost to transfer risk for primary carriers and the end consumer. The cost of doing business has increased dramatically for many insurance carriers and those increased costs are being passed along to insureds in the form of higher premiums, lower limits and tighter terms.

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UNDERLYING CONDITIONS OF THE HARD MARKET

NATURAL CATASTROPHES

- Tornado outbreaks and severe thunderstorms throughout the South and Midwest
- Tropical Storms, for example Imelda and Dorian
- Catastrophic wildfires in Australia, California, Washington, Montana and Alaska

THE ADDITIONAL PRESSURE FROM COVID-19

- Cancellation of major events
- Business Interruption
- Civil Unrest
- Cyber Attacks
- Director and Officer Error
- Employee Safety

Natural Catastrophes in the first half of 2020

	First Half of 2020	First Half of 2019 *(Losses in original values)*	10-year Average of First Half 2010-2019 *(Losses adjusted to inflation on local CPI)*	30-year Average of First Half 1990-2019 *(Losses adjusted to inflation on local CPI)*
Number of Events	530	420	360	270
Overall Losses *(in U.S. $Billion)*	$68	$69	$97	$74
Insured losses *(in U.S. $Billion)*	$27	$20	$32	$20
Fatalities (approx.)	2,900	4,606	24,405	27,270

July 2020 Munich Re NatCatSERVICE

INDUSTRY PERSPECTIVE TAKEAWAY

Reinsurance capacity is strained due to consecutive years of multi-billion dollar natural catastrophe losses. The upcoming hurricane and storm cycle compounded with COVID-19 will continue to impact primary carriers and reinsurers. Relief will partially depend on the severity of catastrophic losses over subsequent storm cycle and COVID-19 losses.

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