SPECTRUM
Asset Management

ESG, Catastrophes and Other P&C Themes

September 25, 2019

Hurricane Dorian made landfall as a Category 5 in the Bahamas, becoming one of the strongest storms which resulted in loss of life and physical devastation. Dorian generated less U.S. destruction than initially feared, and insured losses in the Bahamas should be well below total damages given gaps in coverage. Moreover, tropical storm Imelda has deluged the Houston area, still reeling from the effects of Hurricane Harvey in 2017. In addition, in Japan Typhoon Faxai has led to fatalities and large insured losses, compounding those from Typhoon Jebi in 2018. Several storm systems are ongoing as we are in the most active part of wind season.

If past is prologue, two of the largest catastrophe (CAT) years on record in 2017-18 could signal increasing frequency and severity of CAT activity. In fact, according to an article in the Economist, *"Annual insured losses from catastrophic events have grown 20 times, adjusted for inflation, since the 1970s, to an average of $65 billion this decade."* This may be explained by such factors as coastal population density, and climate change, an important issue addressed by insurers and other major corporations under their environmental, social and governance (ESG) policies.

Despite higher absolute loss figures, relative insured losses (as % of premiums) have been stable over the longer term, while underinsurance in many regions presents an opportunity to expand. Pricing dynamics for P&C companies are generally improving which, coupled with technology and expense initiatives, could boost earnings and provide additional cushion against elevated claims activity. Insurance capitalization continues to be robust.

Reductions in what and how much P&C insurers will cover, and the withdrawal of several alternative reinsurance capital providers, has led to rising premium rates in many business lines. Companies are reassessing rising costs of risk, declining investment income (due to low interest rates) and growing liabilities — partly due to a more generous tort environment and active attorney involvement. Some questions include:

- *Are wildfires and hurricane damages on the rise due to climate change?*
- *Will litigation against manufacturers of e.g., glyphosate, talc and opioids lead to financial burdens?*
- *Will states extend statutes of limitation, exposing insurers to previously time-barred claims?*
- *Are cyber-attacks a growing threat, and are they covered under existing policies?*

Due to evidence of rising liabilities, insurers are strengthening some reserves and pushing price hikes across many lines of business to support earnings.

Those affected by recent natural disasters are in our thoughts. **We remind our investors that insurers are in the risk business, and well capitalized to absorb large CAT events. Furthermore, our P&C exposed names maintain good track records, prudent risk management and disciplined underwriting practices.**

Please see industry data on the next page.

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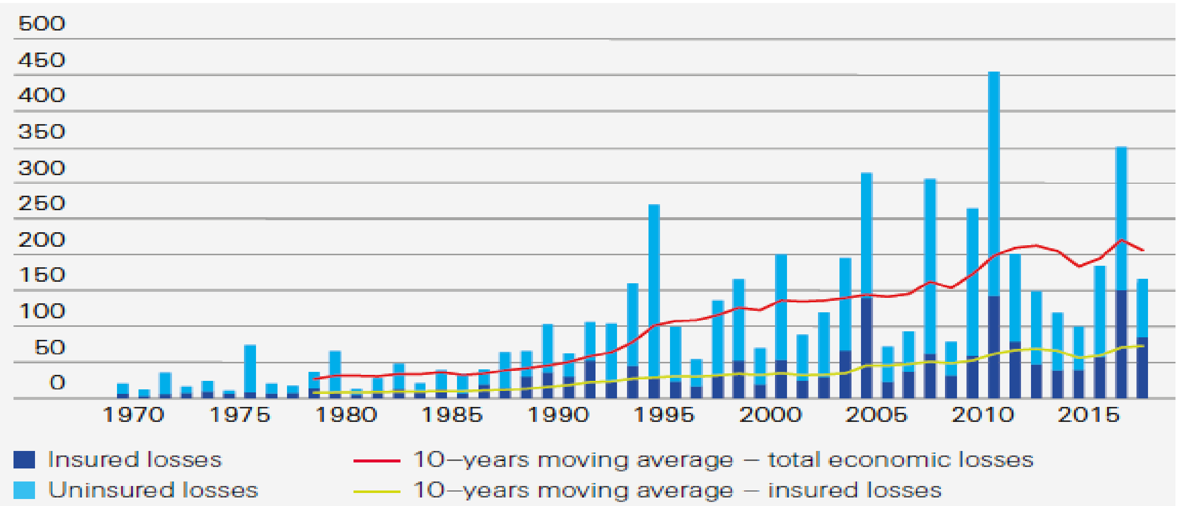
In 2017, Hurricane Irma struck Florida and caused insured losses of over $20 billion, contributing to the largest insured CAT loss year on record, which also included Hurricanes Harvey and Maria, and major California wildfires. Another active CAT year occurred in 2018 with large losses from Hurricanes Florence and Michael, Typhoons Jebi and Trami, and more California wildfires.

Figure 1. Annual and 10-year moving average of insured and uninsured catastrophe losses



Economic losses = insured + uninsured losses
Source: Swiss Re Institute