When attempting to sum up the industry’s business environment during the pandemic, the word ‘extreme’ comes to mind

By Glenn McGillivray, Managing Director, Institute for Catastrophic Loss Reduction
he year in review, it seems, was largely about extremes. Extreme weather. Extreme volatility in investment markets. Extreme variations in company results.

And an extreme virus.

In its 2020 annual report, the Property and Casualty Insurance Compensation Corporation (PACICC) observes: “The combined impact of the first quarter oil shock, wild swings in investment markets throughout the year, COVID-19 claim payments, and substantial rebates of premiums in auto markets meant it was a particularly challenging year for the industry.”

Perhaps “challenging” is an understatement.

Industry results

In the Q4-2020 MSA Quarterly Outlook Report, MSA Research president and CEO Joel Baker, commenting on the industry’s financial results, said “all boats were lifted” for insurers in 2020. Taken by itself, this line blurs the fact that some lines of business, industry segments, and individual companies quite dramatically outpaced others.

In very general terms, Baker summarizes things as so: “A solid year for the industry. Best for personal/multi-line carriers, less so for commercial carriers and reinsurers.”

Perhaps saying “considerably less so for reinsurers” would be more accurate.

As a whole, the industry saw decent results and stronger capitalization owing in large measure to a hard market that has seen fairly significant rate increases in several lines. Indeed, the Canadian property and casualty sector wrote a record $71 billion of direct premiums written (DPW) over the course of the year, up close to 10% over 2019.

This very strong top-line showing outpaced claims inflation as a whole, leading to an improved industry combined operating ratio (COR). “On a net earned basis, premiums were up almost 14% while claims incurred climbed 8%,” according to MSA. “This resulted in a 3-point improvement in the industry combined ratio to 94.6.”

The improved industry combined ratio was aided somewhat by a lower expense ratio “due to the overall volume growth relative to fixed overhead costs,” MSA says.

One might wonder about the impact COVID had on industry expenses. “Though COVID has had some negative impact on insurer earnings in 2020, it has also led to lower claims costs (particularly on the auto side) and administrative expenses,” PACICC says.

It should be noted, however, that general expenses were down only slightly from the year prior, coming in at $4.86 billion for 2020 ($4.44 billion in 2019, according to MSA).
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Along with the decent COR, the industry return on equity (ROE) came in at a more-than-acceptable 11.03% with net income of just over $6 billion (up from $3.89 in 2019).

Personal lines/Multi-lines
Though 2021 was yet another active one for insured disaster losses (more below), premium growth managed to stay ahead of catastrophe and other claims. According to MSA data, DPW in the segment were up 7.2% over the previous year, while net premiums written (NPW) were up a significant 12.2%.

Despite 2020 ending as the fourth-costliest year on record for Cat losses, claims were up only 4.7%, tempered to some degree by a decrease in auto claims due to pandemic-related lockdowns. This resulted in a COR of 95.8% (compared to 100.7% in 2019), yielding an exceptional ROE of 13.7%.

Still, this comes with a proviso from Joel Baker to “enjoy it while it lasts.”

Commercial lines
“Commercial insurers exhibited very strong top-line growth of 18% as a result of firming rates,” MSA says. “Despite this, claims were up more than 17%.”

While DPW were up 18%, NPW were up 16%. The “saving grace,” according to Baker, was a one-point decline in the expense ratio “enabling the sector to tread water and remain at 98.6.” While the personal lines side enjoyed a very healthy double-digit ROE, pure-play commercial writers saw a return languishing at 6.2%. After inflation, not much meat was left on the bone.

Much of the problem appears to be on the liability side of the business. According to PACICC, insurers that offered commercial liability coverages didn’t have a good year. “Insurers report on 10 different types of liability insurance. In nine of the 10 categories, results were worse in 2020 compared to 2019.”

Reinsurance
Reinsurers saw growth of 21.8% driven by the hard market, Baker reports. However, “astoundingly, this was overshadowed by a 43.3% jump in claims — driven largely by Cats.”

The jump in claims, Baker adds, contributed to an underwriting loss of $88 million and a COR of 103.7% against 92.6% the year prior.

The sector clearly underperformed the rest of the market.

The COVID paradox
SARS-CoV-2 has been a bit of a mixed bag for Canadian insurers. On the one hand, COVID-19 led to lower claims in some segments (particularly on the auto side) and may have had (minor) beneficial impacts on overhead expenses for some companies.

On the other hand, the virus has cost certain segments dearly, having contributed to poor results for commercial carriers (particularly on the liability side), precipitated premium refunds for auto, and contributed at least somewhat to a very poor year for reinsurers.

Then, there are the lawsuits.

In Canada (and globally), the virus raised the issue of whether COVID-related business closures fall under an enterprise’s business interruption policy. With very few exceptions, the industry maintains that they don’t — for good reason.

A very recent analysis of the issue indicates that court decisions in the U.S. have been mixed, with rulings contingent on two main factors: Whether a policy has a virus exclusion (where wordings include an exclusion insurers have generally been winning); and whether a given case is heard in a federal or a state court (federal court cases are trending in favour of insurers while state court cases are largely being decided for plaintiffs).

Internationally, several court decisions have come down in favour of insurers. Yet, the global industry continues to wait with bated breath for final resolution of the question.

Alister Campbell, president and CEO of PACICC, recently predicted that courts in Canada should rule in favour of the industry. BI policies are customized to individual businesses, and the courts will examine the facts of each specific case, but there is little evidence to suggest the industry’s pandemic exclusions wouldn’t hold up in court.

“I think the wordings in Canada are clear enough, and so I think it is reasonable to assume that over time the courts will rule correctly that policy intent was clearly articulated,” Campbell said during the recent CIP Society Symposium 2021 virtual conference.

Still, this is going to take time.

NatCats in 2020
Last year was yet another active one in terms of insured disaster losses.

Nine disasters (i.e. events of $25 million in claims or higher) were declared by CatIQ in 2020. These triggered more than 106,500 claims for Canadian insurers, totalling more than $2.3 billion.

Of the nine, two in particular are worthy of note: The spring flooding in Fort McMurray and the June hailstorm in Calgary. The late April flood, while “just” a typical Canadian ice-jam-triggered event, caused $562 million in insured losses. The June 13 hailstorm resulted in insured
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damaged of more than $1.3 billion, making it the costliest hailstorm in Canadian insurance history.
Since CatIQ began tracking Canadian Cat losses, hail has generated almost 900,000 insurance claims totalling more than $8.2 billion (2008 to 2020). More than 612,000 of these claims have occurred in Alberta, costing insurers more than $6 billion.
In all, 2020 went down as the fourth-costliest year on record for insured damage from severe weather, behind 2016, 2013, and 2018. CatIQ data indicate that more than 1.5-million Cat claims have been filed in Canada (2008 to 2020 inclusive) totalling more than $21 billion. This is a big number to be sure.

Disparity
The industry as a whole enjoyed an ROE of 11.03% in 2020. However, not all companies can revel in this aggregate result. PACICC conducted a telling ranking of insurers by 2020 ROE. The results, which can be found in PACICC’s Solvency Matters Apr. 1 newsletter, found that the top 46 companies (a quarter of the sample) reported an average ROE of 23.5%. The next tier of 47 companies reported an average ROE of less than half that, at 11%. The third tier of 47 companies reported an average ROE of 5.4%. The fourth tier of 47 companies reported an average ROE of negative 4.0%.

Underwriting performance was the main difference between the financial performance of insurers, according to PACICC. “The average combined ratio of the top performers was 80.2%. The next tier of profitable insurers reported a combined ratio of 89.3%. The third tier of profitable insurers reported an average combined ratio of 94.5%.”

This means approximately 75% of P&C insurers reported profitable underwriting results in 2020, as PACICC notes. It also means about 25% of Canada’s P&C insurers did not underwrite insurance risks profitably in 2020. The average combined ratio of this group was 158.0%.

Let than sink in: From 80.2% to 158%. A year of extremes, indeed. 

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