New Zealand

Insurance Market Update

2021

Welcome to our Insurance Market Update for New Zealand in 2021. We will explore general and financial lines as well as a focus on our specialty areas. The global pandemic continues to influence all our markets and we hope to bring some clarity and information to you in this update about the months ahead.

New Zealand

Insurance Market Update 2021

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Welcome

2021 Insurance Market Update

It has been another challenging year in the New Zealand insurance market where change appears to be the only constant.

The impacts of COVID-19 – many of which emanate from beyond our borders – have had flow on effects for the NZ based Insurers who are grappling with changing conditions around reinsurance renewals, operating ratios, investment returns, and incurred and reserve costs.

The Insurance Council, in its 2020 results to September, showed overall a 4% deterioration of loss ratio over the previous year but this is still superior to those from 2016-2019.[1]

New Zealand insurers remain very focused on policy wordings and communicable disease and cyber exclusions are being introduced across the board. While adequate capacity remains for most risks across property, there are two specific areas going against the grain; earthquake risks in Wellington and the ongoing issues around the use of polystyrene panels.

Premiums in the motor insurance market continue to be driven by loss histories and we are seeing greater uptake of analytics to determine trends. Having said that, we anticipate more stable pricing in the next 12 months. In terms of general liability, capacity should remain plentiful; rate increases predicted in 2020 (following treaty reinsurance renewals) have been slow to flow down to the New Zealand market in certain sectors, however insurers are continuing to push for these. The Directors' and Officers' Liability market continues to undergo a period of correction with reducing capacity and more stringent underwriting, while the cyber landscape continues to deteriorate with a significant increase in the frequency and severity of ransomware attacks over the past 12 months.

The WTW team prides itself on staying close to clients and market dynamics should not come as a surprise to them. Having said that, at every possible juncture, we reinforce the need for organisations to develop a long-term strategy towards managing and mitigating risk. Insurance is the ultimate risk-management tool but achieving the best from any program is the result of a long-term partnership, rather than a cost-driven, short-term transactional approach. Insurers are showing increased focus on their own profitability and expect the best information and submissions before they will reward organisations with optimal premium pricing and terms and conditions for their risks.

> **"This is not a cost. It is an investment in their own companies, and the optimal way WTW can present their risk to the market to attract the best-possible placement terms. This approach will stand our clients in good stead for not only whatever the pandemic may throw at us next, but for all economic conditions into the future.**

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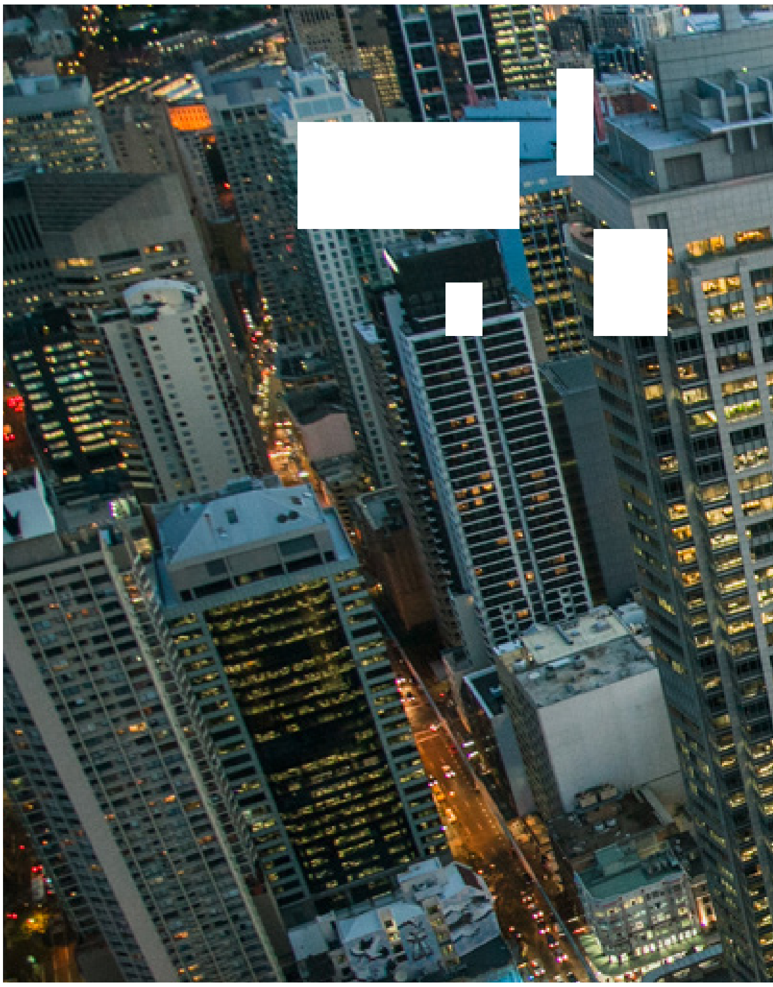
[1] https://www.icnz.org.nz/media-resources/market-data

The direct market – general lines

Property

We are working in one of the most dynamic periods the insurance market has seen for many years. The challenging conditions characterising the market remain ongoing, and our approach to 2021 renewals requires the same high level of preparation and strategy.



This is not a typical market cycle where we see short term significant premium increases followed by intense competition that drives equally significant premium reductions. Local and global events over recent years have pushed the market into a sustained period of difficult trading conditions.

2020 presented challenges that no one could have predicted and the social and economic impacts of COVID-19 continue to unfold.

The financial impact of the pandemic to the insurance industry is not expected to crystallise until well into the third quarter of this year. This has further strengthened insurers' resolve to maintain upward pressure on premium rates, seeking to hold onto their strong position for as long as possible in this seller's market.

The upshot is that rate increases will continue throughout 2021 where capacity remains tight and where clients have suffered losses.

It is, however, not all doom and gloom. We are starting to see normal market dynamics play out where premiums on attractive risks are reaching a level which is more widely seen as sustainable. This scenario is being played out differently across the globe, with some international markets continuing to push for further premium increases across the board, no doubt due in part to the pressures they are seeing in different territories and the losses being felt in various parts of the world. At the same time, insurers who have weathered the storms and now have their books in order are ready to seek profitable growth opportunities. We are also seeing some new capacity coming to the market, attracted by the premium rates now on offer, but we expect them to be prudent in the deployment of their capital, at least in the short term.

In New Zealand we are seeing a plateauing in premium rates with a roll over not uncommon for well-managed risks in attractive industries and locations. As is the case globally, New Zealand insurers are extremely focused on policy wordings with the introduction of communicable disease and cyber exclusions across the board and scrutiny of sub limits and non-damage business interruption coverage.

It is certainly a case of each risk being underwritten on its merits.

As we move further into 2021, there is likely to be a continuation of the fundamental characteristics prevalent in this stage of the market cycle:

Capacity remains available – at a price

Global insurance capacity for all but the most challenged risk locations and industries remains generally stable and the available capacity continues to be judiciously deployed. Insurers are focused on their exposure to individual risks and closely managing their aggregate exposure to higher risk locations, which can create pricing pressure and require restructuring of insurance programs.

Insurance market remains financially strong

The insurance market continues to be well capitalised, due in part to the ongoing low interest rate environment globally, and in strong financial health.

Disciplined underwriting

Underwriting will continue to be disciplined and rigorous, with a focus on core coverage terms and conditions. Insurers are showing some willingness to negotiate on premium rates, however less willing to negotiate on breadth of cover.

Due to the drive for underwriting discipline and profitability, there is greater central control over decision making for the risk selection process and deployment of capital.

The Outlook

- Pockets of distress will remain as insurers continue to manage their exposure to certain locations such as earthquake risks in Wellington and industries such as the food sector with ongoing issues concerning the use of polystyrene panels, both of which will continue to be challenged in securing favourable terms.
- With insurers underwriting each risk on their merits there is real opportunity for risk differentiation. Insureds who can demonstrate being proactive in minimising their risk through first class risk management practices will secure the most competitive pricing, terms and conditions from the market. Those who have chosen to develop a long-term risk management philosophy and built relationships with insurers will also be in a stronger negotiating position.
- The best results in this market will be achieved through:
  - being proactive
  - starting the process early
  - having a clear strategy leading into renewal negotiations
  - clearly articulating your risk management procedure and improvements made in mitigating risk exposures.
- Be clear with the market as to what you want, know where you are willing to trade off for coverage and stick to the plan.

Motor

Overall loss ratios for Insurers slightly improved in 2020 over the previous year off the back of reduced overall utilisation due to the impact of COVID-19. However, the improved underwriting result was tempered by reduced investment income.

Loss histories continue to be a major driver in determining premiums with a continuing trend towards utilisation of analytics to determine trends and improved data from in-vehicle GPS technology. These analytics are helping fleet managers give stronger consideration towards self-insurance options in addition to the historical claims-driven structures. Analytics also provide valuable data to identify trends to help reduce avoidable losses and assist with Insurer negotiations where new driver management strategies are introduced.

Repair times continue to present challenges with increased technology in vehicles slowing down and increasing the cost of repairs. The utilisation of third-party claims operations can provide benefits for businesses in respect of improved repair times and access to a wider range of courtesy vehicles.

Your Account Manager will discuss which of these options may benefit your fleet as part of your normal renewal cycle.

The Outlook

We expect insurers to continue to focus on both portfolio and individual fleet profitability and businesses that proactively approach fleet and accident management will achieve more favourable results.

While direct lodgement of claims with insurers and increasing use of digital assessments are speeding up the claims approval process, longer repair times due to limited capacity within the repair industry and more advanced vehicle technology will continue to weigh heavily. Some of these delays can be mitigated with the help of third-party claims operations.

The next 12 months will continue to see larger fleet operators consider alternative structures with higher deductibles.

Marine

The New Zealand marine market saw premium volumes drop from $149 million to $140 million in the last 12 months, along with a slightly improved loss ratio. We expect the reduction was driven by COVID-19 and anticipate increased volumes in 2021. This is notwithstanding the challenges surrounding supply and delivery into NZ, along with Insurers continuing to be impacted by low investment returns.

We have seen increased appetite in the New Zealand market as newer entrants attempt to seek market share from the traditional leaders. However, there continues to be some challenges around capacity for stock throughput particularly in respect of those risks with polystyrene panelling. The Hull and Liability markets both seem to be looking for small increases on renewal business yet offering flat to slightly lower pricing for new business.

The Outlook

In the local market we anticipate relative stability for the balance of the year with flat to modest increases. Insurers are trying to work with businesses managing to either re-establish themselves post COVID-19 or deal with increasing demand as consumers reinvest money previously spent on overseas travel, on consumer goods and home improvement. Competitive tensions will remain, with increasing appetite for Marine business from newer entrants to the NZ market.

Globally in the cargo market, fluctuation around pricing is starting to subside, although conditions remain hard and market capacity continues to shrink with an increase in quota share placements becoming more prevalent.

In hull, 2020 was one of the hardest marine markets in more than 20 years, and there are no indications that this will improve in 2021. In the Marine Liability (Protection & Indemnity) market we expect to see modest increases (5-10%) as capacity continues to be challenged, along with the introduction of new exclusions not unlike the cyber exclusions we have seen on the last few years.

Many global marine underwriters continue to work remotely – the inability to discuss risks face-to-face and having time to more closely scrutinise submissions has resulted in underwriters becoming more demanding in terms of cover and pricing.

As always, we will look to leverage local and international markets to find the best solutions for our clients.

General Liability

Rate increases predicted in 2020 (following treaty reinsurance renewals) have been slow to flow down to the New Zealand market in certain sectors, however insurers are continuing to push for these.

For the more "vanilla" risks, that have no bodily injury or product liability exposure, a clean claims record and no change in risk profile, rate increases of between 5-10% are being sought in a bid to counter "turnover creep". This is where turnover has increased steadily over the past few years, with no corresponding increase in premium, resulting in reduced premium rates. Insurers are also pushing for an increase in minimum policy deductibles.

Where additional risk factors apply such as exposure to overseas territories and jurisdictions, bodily injury and product liability claims, insurers continue to underwrite selectively and are also reducing capacity on the larger accounts.

Losses in the US and Australian markets continue to influence pricing and capacity, as claims activity and resultant costs incurred by insurers have been steadily rising over the past five years.

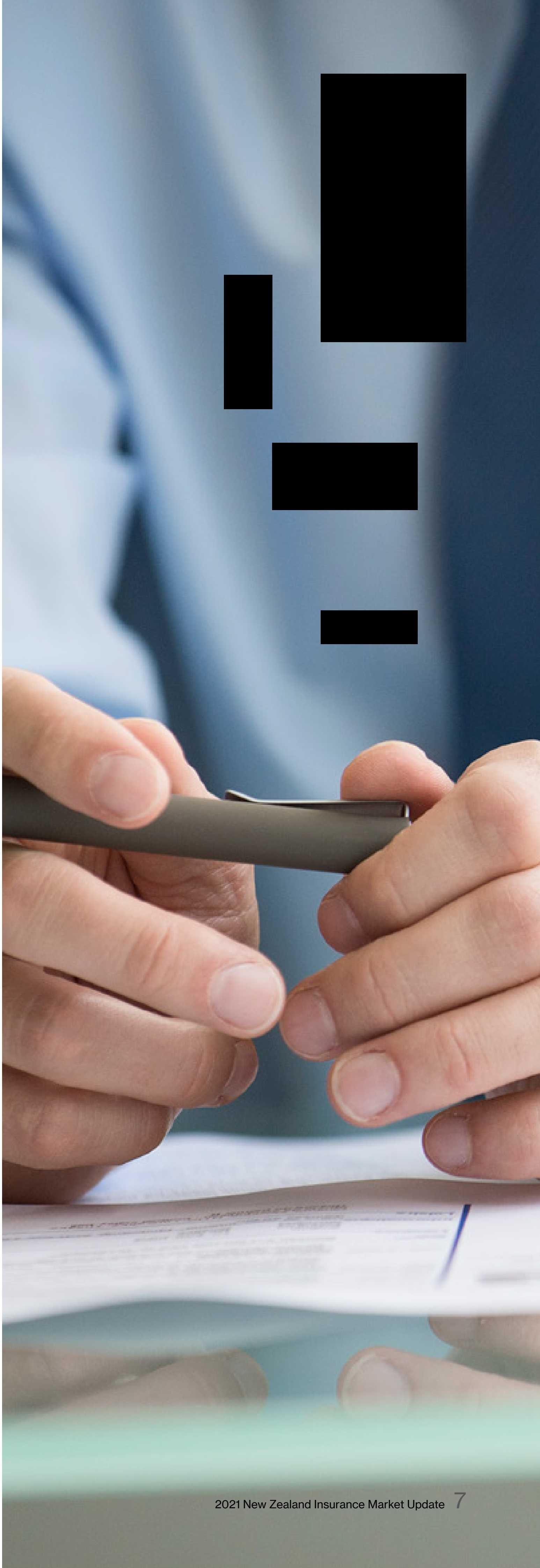
Robust risk management and the ability to clearly demonstrate the effectiveness of this to insurers is still key. Now more than ever, a longstanding relationship with an insurer can also be of huge benefit to an insured.

The Outlook

Locally, capacity should remain plentiful, however insurers will continue to push for rate increases and look to decrease their participation on larger and more complex programs.

Some insurers may also look to increase minimum deductibles and restrict coverage in certain areas. Defective workmanship cover is also likely to come under greater scrutiny as claims activity continues to increase.

Globally, it is predicted that the market will continue to see increasing claims activity incurring greater costs and corresponding price increases.



The direct market – financial lines

Directors' and Officers' Liability

The D&O insurance market has been undergoing a prolonged period of correction, with insurers:

- Limiting their capacity on any one risk
- Substantially increasing company retentions
- Increasing premiums
- Withdrawing support completely for existing clients in unfavourably perceived industries (such as travel, hospitality and retail) and/or jurisdictions
- Displaying limited appetite for new business risks, especially on a primary layer basis
- Seeking more detailed information, often by way of supplementary questionnaires focussing on the financial impact of the COVID-19 pandemic on the company business, including directors' and management's responses thereto and the effect on employees and customers or clients.

The drivers behind the correction have been well documented. They include the size and number of securities class action claims fuelled by litigation funders in Australia, as well as the reduction in capacity available in the London market; Lloyd's has increasingly required its syndicates to demonstrate their solvency and ability to operate profitably.

Throughout 2020 and in early 2021 the ongoing social and economic impact of COVID-19 served to increase uncertainty, which in turn cemented insurers' positions, causing them to increase premiums and reduce capacity further.

Insurers are currently demonstrating an increasing concern about issues such as:

- the number of employment practices liability claims (due to companies downsizing and restructuring)
- cyber resilience, with concerns about the increasing number of employees working from home
- the emergence of Environmental, Social and Governance (ESG) and related reputational risks.

In Australia, securities class actions, and class actions in general, are the focus of regulatory attention and the regulation of litigation funders is increasing. An announcement in February 2021 that the Australian Government will make the relaxation of rules around continuous disclosure permanent is important, as companies and directors will now only be liable for breaches if "knowledge, recklessness or negligence" can be proved. The first successful defence of a securities class action occurred in the Federal Court in 2020 (Crowley v Worley Ltd), which may encourage more companies to defend, rather than settle claims. All these factors will have positive longer-term implications for the D&O market.

The introduction of new markets and increased capacity in London will help ameliorate opportunistic pricing and create competition especially on excess layers.

The Outlook

We are forecasting that premium rates will continue to increase but less dramatically than they have in the past few years. Clients which have a dual listing in Australia and/or require Side C cover will still be scrutinised carefully with insurers closely reviewing financials, and the business response to COVID-19 and exclusions across some areas of cover may be applied. As premiums increase, clients are reviewing the purchase of Side C cover.

Side AB only cover will also see premium increases as insurers target optimal rates, but again in a more restrained manner, with the focus on corrective underwriting and endorsements relating to insolvency, shareholder support, cyber and employment practices liability.

In order to manage the premium increases, it remains as important as ever to start the renewal process early and engage with your brokers to differentiate your risk from others and remove negative assumptions regarding your business. We recommend larger insureds look at more creative options around retaining risk via bigger retentions, reviewing limits or coinsurance in order to drive a more favourable renewal outcome.

Cyber Liability

The cyber landscape continues to deteriorate with a significant increase in the frequency and severity of ransomware attacks over the past 12 months with some of the more notable breaches including Accellion, SolarWinds and, most recently, the Colonial Pipeline attack. These claims trends are expected to continue for the foreseeable future as the use of cryptocurrency and expanding networks of criminal groups outmanoeuvre the development of protective measures.

The human element continues to be the leading contributor of cyber loss claims reported. Organisations need to maintain a constant review of their cyber risk management and mitigation strategies (including supply chains) and align them to the organisation's unique and individual risks. Pre-breach consultation services, including base line assessments and monitoring, is just one way organisations can become more cyber resilient.

Global regulation is driving wholesale changes in the market around privacy and the collection of data and we are seeing more governments introduce sanctions around the payment of ransoms from cyberattacks to try and stem the flow of money heading offshore into criminal hands.

Recently, New Zealand has passed and incepted the Privacy Act 2020 which replaced the outdated Privacy Act 1993. The new Act requires greater control by insureds to manage personal data and provides guidelines on how data should be handled, stored, accessed, and disposed of in a secure way. Failure to adhere to the Act could result in fines and penalties as well as damages to brand recognition and negative PR.

The cyber insurance market continues to harden. With claims on the increase, insurers are increasing rates, tightening capacity and restricting/removing cover to organisations that fail to demonstrate strong cyber risk controls, culture and governance. Heavily exposed industries bearing the brunt of these rate increases include healthcare, higher education, public entities, manufacturing, financial institutions, construction, and large media and technology companies. Cyber underwriters are also working more closely with their colleagues in other lines to address the issue of silent cyber coverage and concerns over aggregation.

The Outlook

Given the dramatic increase in cyber incidents, both in frequency and severity across all industries over the past year, organisations need to be proactive in assessing their cyber resilience and be able to demonstrate this both to their shareholders and insurers. Limits should be carefully reviewed in light of the recently published ransomware attacks and the consequent business interruption and associated costs of restoring systems and infrastructure.

Professional Indemnity

The market compression of prior years that saw an overall increase in rates, a withdrawal of capacity and in some cases a market exit from writing certain areas of business has eased with most renewals seeing rates maintained or slightly increased.

In the areas of construction and financial planning, rates are continuing to rise. Construction industry losses have been significant, and the financial planning industry has been impacted by recent changes to legislation and a very tight market, leading to insurers remediating their portfolio.

While insurer capacity is still healthy, we are seeing more use of coinsurance on large placements as insurers look to “right size” their overall capacity on any one particular client.

Insurers are however scrutinising new business more closely, with clients claims records going back 10 years (instead of the more usual five to six) being required.

Minimal impact from COVID-19 has been felt. Losses relating to PI were almost non-existent and medical malpractice claims are generally covered by the government-run Accident Compensation scheme.

Silent cyber exclusions are starting to enter the market, reflecting insurers’ requirements to cover PI risks only and not cyber risks which, by virtue of wide operative clauses, can bring the unintended consequence of a cyber claim being covered under a PI policy.

The Outlook

Apart from the distressed sectors mentioned here, the outlook is generally stable for clients with a good claims history. Linear increases in premium as they relate to any increase in fees/turnover is still likely to occur, however risks that have had claims are receiving increases with little appetite shown by competing insurers if a remarketing exercise is undertaken.

Our specialities

Agriculture & Dairy

The global demand for New Zealand agricultural products, particularly dairy and pip fruit, has never been greater. However, COVID-19 challenges continue with the food industry. There have been delayed export and import freight shipments due to congestion at Auckland and Tauranga ports, reduced sailing schedules to New Zealand, immigrant employment restrictions, a port experiencing IT issues and union strikes also contributing to already congested system.

Property insurance markets remain active on accounts where businesses show a strong risk management culture, with less available capacity and interest for businesses not investing in better managing their internal risks.

Property insurance risks

The major property risks associated with the dairy, food and agricultural industries are similar to many other manufacturing risks such as fire and natural catastrophic losses that can be devastating to a business. Notably, the widespread use and existence of Expanded Polystyrene Panel (EPS) or similar panel products in building and internal linings continue to be viewed as very high fire risks by insurers and higher premium rates and terms are reflected in the terms provided. It is critical to manage and mitigate potential ignition sources for panel-related building product and any other combustible materials, so general regular planned regular maintenance is extremely important. The installation and or upgrading and maintenance of complaint fire sprinkler systems, thermographic imaging, hot work permits and sound maintenance practices assist in preventing loss. Avoiding improving your risk profile in any business will mean increased terms or insurance protection being unavailable.

While capacity, premiums and deductibles have been impacted by past and recent losses in Australia and New Zealand, in seeking insurance protection the critical factor remains being able to demonstrate first-class risk management, fire protection and maintenance practices, disaster/crisis recovery strategies and the strength of business continuity plans.

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Commitment is required by clients to manage external and internal high-risk sites by improved risk management processes and investment in additional fire protection, namely, fire sprinkler protection and, where possible and practical, the use of alternative panel products that are less combustible.

We have seen some recent signs of local market rates easing as a result of the last two years of significant rate increases and insurer review of available capacity. International markets have shown more interest of late, but we continue to see insurers being more selective on the risks they will write.

Working in partnership with your insurer is important so a common goal of a mutually beneficial relationship is achieved.

The Outlook

New capacity is scarce but not impossible to achieve with a better risk managed accounts. A handful of New Zealand based insurers continue to support the food sector, though every year seems to bring on a new challenge with insurers underwriting risk more carefully and deploying their capital appropriately.

Alternative Risk Transfer & Captives

The Alternative Risk Transfer (ART) market is a steady force throughout the traditional insurance market cycle. During challenging market conditions such as we are currently navigating is where ART solutions often deliver the most value and receive the most attention from risk managers.

Turmoil continues to spread across many lines of insurance as insurers struggle to address high combined ratios, low interest rates and the economic upheaval brought on by the COVID-19 pandemic. Traditional insurers are seeking to manage their aggregate exposures, re-underwrite policy coverage and re-price risk, all of which creates inflexibility and hampers the delivery of what many insurance buyers need.

More often, insurance buyers are looking to their insurance partners to create solutions which deliver pricing, capacity and coverage that adapt and flex with their everchanging risk profile. The ART marketplace offers those buyers alternative risk transfer and financing solutions that are tailored to each situation, delivering value that the traditional insurance market is unable or unwilling to offer.

We work with companies across New Zealand, Australia and the Pacific, bringing clarity to their risk management philosophy, their risk appetite and their risk financing strategies, all of which supports them achieving their business goals and reducing their total cost of risk. We achieve this through analysis of each company's need, striking the optimal balance between risk transfer and retention and creating bespoke products and solutions.

This process reduces insurance premium volatility and enables the prefunding of a broader range of insurable and uninsurable risks. Our clients have enjoyed significant financial benefits from the formation of alternative risk transfer vehicles such as captive insurance companies. These clients have saved between 30-50% of their total cost of risk over a five-year period, enabling them to create a competitive cost advantage over their business rivals and enhance their shareholder returns.

The Outlook

The current economic environment is a catalyst for increased interest in ART through 2021 and beyond as many insurance buyers seek to find their 'new normal' in a post COVID-19 world. As companies seek to recover losses incurred through shutdowns or limited trading a greater emphasis will be placed on bespoke solutions that deliver where the traditional insurance market and product offerings cannot or will not.

We are seeing significantly increased interest in ART solutions which support insurance buyers' strategic direction and enhance earnings for their shareholders. With the ever-increasing focus on captives, the insurance market will respond favourably to those clients taking a more active involvement in their risk management.

Construction

The first half of 2021 has been a mirror image of H2 2020, with the same trends in the New Zealand insurance market continuing to exacerbate.

Insurers have maintained their focus on underwriting profitability, resulting in continued application of increases in rates and deductibles, reductions in capacity deployed and restrictions in the levels of cover they are willing to provide. We have had insurers reduce their underwriting appetites, and earlier this year another global insurer exited the New Zealand construction scene, further reducing competition at local level.

To position clients more favourably, we recommend building closer relationships with your insurers, hosting risk presentation and project site surveys as appropriate, coupled with providing quality underwriting information to better differentiate your risk profile. Clients should be prepared to allocate more time and resources to either insurance renewals or project placements.

The Outlook

With the changes in market conditions, insurers are no longer hungry for business, in turn becoming more particular with the risks they are willing to insure. At times, the attitude is very much a "take it or leave it" approach.

Challenges in the construction sector can be met by early strategic planning, and by heightened focus on the quality of information being supplied to an increasingly discerning underwriting community.

In addition, it is imperative to evaluate the insurance placement strategy to ensure overall project success and to consider alternative risk transfer techniques, including parametric solutions for addressing project risks stemming from extreme events.

Creativity and innovation will be essential to building leading edge approaches to risk management.

Contract Works – Material Damage

While we are still experiencing hardening pressure, most local insurers have adjusted their premium rating on new and renewing risks. Previously available coverage enhancements such as Guarantee Maintenance and Design Exclusion (DE5 or LEG3) are either no longer available or are only offered with increased rating and deductibles.

Annual programs with repeat loss history and exposure to extreme natural events continue to face changes to coverage and insurer capacity availability – in some instances, insurers are imposing separate Major Perils deductibles.

Large infrastructure and major projects still have a supply of capacity available, however rating and deductibles are higher than 12 months ago, and policy terms and conditions are narrower. Insurers are underwriting with greater scrutiny given to Contractor performance on previous projects.

COVID-19 has had an impact with insurers now insisting on Communicable Disease exclusions. Insurers are watching the outcome of the various Business Interruption court cases currently underway in the UK and Australia. While these cases are more related to property covers, the outcome has the potential to flow through to the Contract Works market, particularly around Prevention of Access type extensions in Delay in Start Up policies.

The Outlook

The theme has not changed too significantly since 2020 and we expect this to continue for the remainder of 2021. Organisations must continue to work closely with their brokers on a short to medium-term plan, ensuring early engagement with insurer partners.

Construction Liability

Construction liability pricing on annual policies for programs with a favourable claims history has been positive, however insurer selection and competition remains for quality business from local markets.

The Outlook

Clients with a deteriorating performance on claims can expect remediation via either increases in premiums or deductibles. Clients who are willing to accept higher deductibles will continue to receive competitive pricing from the market.

Design and Construct Professional Indemnity

The Design and Construct Professional Indemnity (D&C PI) has continued to shift with dramatic corrections over the last 24 months, all driven by claims developments both locally and globally. Rating and deductibles are continuing to increase at a significant pace.

Insurers are tightening up areas of cover, including nonconforming building products, leaky buildings, loss mitigation and rectification costs as well as express fitness for purpose. Aluminium composite panels continue to be an issue for insurers as they impose exclusions and conditions to address the increasing level of claims experienced overseas.

The Project Specific PI market continues to be a heavily scrutinised class of insurance with local and overseas insurers re-thinking their approach to participating on large infrastructure projects for multi-year periods – particularly those delivered under a project alliance structure. This has significantly reduced the available capacity and coverage available for these projects. Long lead in time is required working with all project sponsors and both the local and international markets to ensure a robust project PI program is built.

The Outlook

The market capacity available for Project Specific PI placements has reduced significantly. This makes achieving the contractually required limits increasingly challenging, with additional insurers required and resulting in a consequential increase in pricing.

Health & Benefits

Solving new health and benefit initiatives

The Life Insurer market in New Zealand has been very much inwardly focused over the past year, pivoting to the demands of COVID-19 as well as built changes in New Zealand Financial Services legislation.

From the outside looking in, the impact of Covid-19 on a New Zealand Life Insurer may appear minimal, however local insurers have clearly been forced to grapple with the views of their offshore reinsurers. The reinsurers have been operating in a far different environment with more pressure on their businesses from offshore. A key concern noted in our discussion locally and globally with the market has been the potential for future claiming patterns, in particular around the unknown quantum of mental health and stress-related claims into the future.

The Outlook

We anticipate a tightening of terms available, in particular for longer term Income Protection Insurance claims. We may also see some contraction in insurer appetite for the availability of voluntary or employee-paid benefits, which have traditionally been available.

Wellbeing

With a direct connection between employee wellbeing and business success, it has moved from the periphery to the centre of most business owner and HR Director discussions.

In response to the COVID-19 pandemic, our clients and own teams have shown extraordinary resilience.

While from a statistical perspective, New Zealand has been relatively immune to COVID-19, the wider regional and global research by Willis Towers Watson presents a starker reality. According to Willis Towers Watson's 2020 Global Benefits Attitudes Survey, 29% of employees feel their mental health has worsened as a result of the pandemic and 36% of employees have experienced anxiety and/or depression within the last year. Nearly two-in-three (65%) of employees under 25 report suffering from anxiety or depression over the past two years.

New Zealand's insurance market has, as we would expect, also noted the trend and demand in this area – and we are therefore seeing increased availability in particular of App-based technology to assist with meeting some of the needs of insured members.

Our view is very much that Wellbeing is not an isolated program or initiative. Wellbeing is purpose-driven and woven into the fabric of an organisation's values and the employee experience. It is inextricably linked to a myriad of policies, programs and benefit offerings as well as to desired culture, productivity improvement, longer-term organisational talent retention and sustainability of business results.

Four key dimensions of wellbeing

Integrated wellbeing incorporates four key dimensions:

- ***Physical wellbeing:*** To thrive physically means understanding and managing one's health, taking appropriate preventive measures, improving health status where needed, managing chronic conditions, navigating and recovering from an acute illness or unexpected injury and successfully returning to peak functionality at home and at work.
- ***Emotional wellbeing:*** Being emotionally balanced means being self-aware, maintaining good mental health, being resilient by managing stress, coping with positive and negative emotional triggers, dealing with life crises and maintaining stability through illness or injury.
- ***Financial wellbeing:*** Achieving the state of being financially secure means having the ability to manage budgetary commitments, meet financial goals, protect against risks, save for contingencies or future needs like college or retirement and cope with financial shocks.
- ***Social wellbeing:*** Social wellbeing is about being connected by understanding how to interact well with others by accepting diversity, being inclusive, knowing how to support and collaborate with others, being able to successfully resolve conflicts and adapting to change. Being connected applies across one's family and friends, one's workplace and the larger community.

Each dimension is unique and intertwined with the others. Integrated wellbeing begins with individuals and, when achieved, extends throughout their organisations, families and the larger community.

As a result, the ideal state of wellbeing – physically thriving, emotionally balanced, financially secure and socially connected – places the employee at the centre and is truly integrated across all four dimensions.

Irrigation

The irrigation sector remains topical among political and ecological groups, commentators and advocates. Quantities of water usage, resulting environmental effects, the highly-publicised issue of river pollution and the ongoing climate change debate, are common themes drawing irrigation schemes into wider-ranging conversations.

The political agenda contains some weighty matters, headed by changes to the Resource Management Act, water apportionment including Iwi rights and interests, nutrient allocation and possibly the most significant action stemming from the Essential Freshwater Reforms.

We have remarked on prior occasions of capacity generally remaining stable, with pricing models dictated largely by natural catastrophe ratings.

In 2020 we commented "...we do not anticipate this to change over the next 12 to 18 months at least". From risk and insurance perspectives, the myriad of issues flowing around of the irrigation sector are in stark contrast to the steady and still fairly benign nature of the insurance market. We contend that the industry is in for more of the same, probably into 2023.

Upward premium rate movement of medium single-digit percentage points is our widely envisaged norm, predicated by an absence of significant natural events. There may be outlying exceptions to this broad expectation, with example scenarios being cases of an irrigation scheme facing a significant uplift in replacement values or experiencing isolated losses.

> **"From risk and insurance perspectives, the myriad of issues flowing around of the irrigation sector are in stark contrast to the steady and still fairly benign nature of the insurance market.**

With very few notable highlights within the local insurance market arena, it's worth looking a little more closely at the existing state of affairs, particularly the how, and the why.

New Zealand is, in many respects, a challenging territory for insurance underwriters and especially so for infrastructure programs. As has been the case in recent years, market appetite to expand beyond their respective existing portfolio of insured risks remains limited.

Looking back, there have been significant premium corrections in the aftermath of earthquakes around the turn of the last decade. That, in itself, is old news but the cause and effect of today's premium pricing stems from a lengthy pre-earthquake period when local costs were massively out of step with other developed nations.

"Hard-market" insurance conditions of the past were characteristically a short, sharp shock, lasting usually no more than two or three years and punctuating prolonged periods (up to 20 years) of a "soft market". So why has this hard market maintained its traction? Insurance buyers have more easily understood why rates increased when major events such as earthquakes in Christchurch or Kaikoura occur.

Progressively it is now the result of aggregated losses from an increasingly larger number of smaller events that stretch capacity and create premium pressures. Locally, we are experiencing floods of greater frequency and increasing severity and other damaging events such as costly bushfires. Globally, severe natural catastrophes cause ripple effects that reach Aotearoa and impact insurance capacity and pricing.

Infrastructure risks bear these market strains, even if the loss examples given here are not a direct correlation to the risk profile of an irrigation scheme. As has now been the case for the last two to three years, insurance capacity remains available at a price. A major factor in availability and how this plays out is the reinsurance market – not least due to the limited number of reinsurers that are active in our region compared with most global markets.

Compounding the selective readiness of capacity is the financial landscape. Prevailing low interest rates create additional premium pressures due to the lack of investment returns insurers and reinsurers are able to achieve, thereby limiting their alternative avenues for profitability.

The Outlook

Fresh market challengers are, in our view, unlikely in the short-term. Increased competition requires new entrants to be wholly convinced of creating an enduring and profitable play for market-share.

The existing small cluster of active insurers have all gathered a lengthy period of experience with irrigation risks. As mentioned earlier, indications are these local insurers will demonstrate restraint in the pursuit of additional clients and instead remain focused upon maintaining capacity to their existing portfolios of irrigation risks.

London markets are not expected to emerge as a challenge, which would necessitate a markedly improved pricing point to create a serious level of competitive tension.

Liability markets remain relatively steady and premium variations only slight. We foresee minimal fluctuations in cost or coverage availability

The narrative for most irrigation clients continues to be preserving current capital and investing in positive and comprehensive profile promotion to ensure that current markets stick.

Iwi

Willis Towers Watson has developed a strong relationship with Tangata whenua.

We continue to grow our marae insurance schemes that provide insurance solutions to meet the cultural needs of marae, specifically around basis of settlement for Taonga, cultural artwork and risk management solutions. Iwi have been recently investing heavily in improving their risk profiles from a physical perspective.

The Outlook

Our involvement in the maori sector is significant in addressing the required insurance needs. Our focus on marae has been very successful in leveraging the insurance purchasing power for iwi resulting in significant cost benefits.

We have seen a changing perspective in providing insurance solutions to marae from many insurance markets. Marae are an important part of the Tangata whenua community and we continue to see significant investment from marae in improving their sites, upgrading facilities with modern buildings and improved fire protection systems.

> **The perceptions of marae risks, which are an important base for iwi, have changed where it has been acknowledged that a collective approach to insuring is beneficial for both clients and insurers.**

We continue to grow our presence in this sector providing sound and reasonable solutions to iwi. Willis Towers Watson's iwi practice continues to assist iwi to achieve their collective goals, with insurers keen to align themselves with Tangata whenua.

Pacific Islands

COVID-19 has had and continues to affect the Pacific Islands with borders being closed for over a year and the majority still closed. This has had a significant effect on their economies especially the ones that relay mainly on tourism.

Insurance buyers in the Pacific Islands have largely continued to feel the effects of ongoing underwriting market strains and pressures. With tightened economic conditions across almost all classes of risk and occupations, companies need to take even greater care in risk mitigation and their insurance program.

Continuing the trend set over the previous three years, rates continue to climb as the limited number of active market participants remediate their underwriting portfolios, especially with regard to natural catastrophe exposure.

The 2021 cyclone season officially closed at the end of April and the scale of losses were by no means comparable to the severe events of recent history. The strongest tropical cyclone in the South Pacific since 2016 arrived in the form of Severe Tropical Cyclone Yasa in December 2020. This event was noted as the fourth most intense tropical cyclone on record in the basin and it was the second successive cyclone season in which a Category 5 severe tropical cyclone event has been recorded, following Harold in 2020.

The severity and constancy of these weather systems continues to restrain underwriters who cannot achieve sustainable returns upon their expended capital. While simple economics tells us that competition is the driving force of premium pricing, the insurance market relies on an understanding of risk, quality information and solid relationships – but most of all the availability of sustainable and profitable capacity.

For Pacific Islands risks, the fundamentals of insurance purchasing have shifted and – in all probability – with some permanence. It is clearly understood the crux of the situation is the preparedness for any future severe natural events and this will be the ongoing driver of premium costs while returns on capital remain poor. It therefore burdens clients if the purchase of insurance and risk management advice is not a key strategic decision, and a business cannot make fully informed choices about its future.

In the prevailing hard market conditions opportunities are limited. Companies face potentially greater cost increases or limitations in cover, or a combination of both in the absence of clear and effective risk control measures.

Insurance markets are cyclical, and premiums are influenced by a range of factors, such as loss history, natural disasters (both locally and globally), interest rates, and the cost of capital, among others.

Ultimately, for businesses in the Pacific to get the best results out of the insurance market, it is critical to ensure insurers are presented with the information they want (not the minimum they need) when negotiating coverage and premium terms. The more information clients are able to share, the clearer the insurance market will understand your business and specific risk factors.

When uncertainty is eliminated, we can ensure clients receive the right cover for their situation and advise on risk mitigation strategies to improve leverage and desirability within the insurance market.

It is increasingly crucial for businesses in the Pacific Islands to be tactically minded and 'risk led'. These astute enterprises will hold a longer-term view, developing a flexible framework and capacity to optimise retention, control and transfer of risk.

This is an approach that will aid prosperous, resilient and sustainable organisations, where risk control underpins commercial and operational objectives, as well as return on investment. It's a departure from the outdated 'market-led' position – essentially where businesses fail to alter their approach each year, this will invariably result in pricing and scope of coverage outcomes dictated by whatever stage of the market cycle is in effect at that point in time.

Organisations which have adopted the now mandatory forward-looking mind-set will have already firmly grasped that having the correct insurance and risk management strategies in place has a positive impact on the delivery of its short, medium and long-term ambitions.

The Outlook

A heavy reliance upon the London insurance market remains. There is no change anticipated, in the next 18-24 months in New Zealand and Australian markets will continue to be constrained in their ability to offer any capacity for Pacific Islands risks.

Alternative markets in Asia are able to offer support, but this is on a very selective basis and will not alleviate the current situation by creating the necessary competitive pressure which could meaningfully shift the pricing scale and extent of coverage made available.

The outlook remains fragile. The key will be to retain leader markets and take benefit from continuity of coverage, wherever possible.

Power & Renewable Energy

Property

We reported in 2020 that it would take more than 12 months of a 'hardened' market for conditions to settle, and this has proved to be the case. The historically poor loss record in the sector globally remains a key constraint for insurers, and therefore for insurance buyers.

There is on-going pressure from several sources which have the effect of continued capacity constraints and constant scrutiny of insurers' power portfolios. These include:

- Poor loss record and consequent unprofitability
- Unprofitability of related sectors (e.g. renewables and downstream energy)
- COVID-19 challenges
- Technology challenges
- Reduced capacity for Coal and Hydro
- Increased operating costs
- Management pressures and Lloyd's Performance Management Directive (PMD).

Contributing factors to the poor loss record include:

- Natural Catastrophe losses, including storm, flood, earthquake and wildfires
- Aging industry infrastructure
- Maintenance "efficiencies" manifesting themselves
- Aging workforce not being replaced with equal quality/ experience
- Experienced workforce spread more thinly across growing asset base.

The PMD and internal management pressure means underwriters continue to be selective in their risk appetites. Global capacity for the energy sector has continued to reduce with insurers not offering full capacity and line sizes being trimmed. We are seeing very few over-signed placements, with more challenging risks facing capacity gaps which is, in turn, driving greater premium increases.

In addition, the reinsurance market is "hard", reducing insurers' ability to lay off less attractive risks, further driving premium increases. Chinese capacity remains limited unless there is a direct association with Chinese interests.

Coverage issues

Policy coverage continues to be scrutinised closely. 2020 saw cyber coverage within property programs either excluded from policy wordings or provided on an affirmative basis. We also saw the introduction of Communicable Disease exclusions, directly as a result of COVID-19. To date in 2021 we are seeing:

- Following on from the pandemic, the non-damage Business Interruption element in some cover extensions such as Denial of Access or Public Authority is explicitly excluded
- Increasing deductibles
- Requirement for greater detail to maintain sub-limits
- Increased transparency for Business Interruption exposure
- Insureds that have sustained losses having coverage restrictions applied and higher deductibles imposed.

A challenging environment

- While Power business continues to be within most insurers' general underwriting appetite, there are challenges. As capacity reduces, fresh competition is hard to find. Underwriters remain cautious, being well aware of the scrutiny from their management, from the Lloyd's PMD, and from their peers. Panel insurers are not challenging lead insurer terms and new insurers require details of the previous year's pricing before offering terms. In addition, new capacity is often opportunistic, knowing that placements are harder to complete which often leads to an element of price-gouging.
- Insureds are having to accept premium increases unless they are prepared to make substantial changes to coverage requirements. And even then, Insureds willing to take more risk often remain disappointed by the market response. Insurers are seeking to increase premium income and are not offering viable trade-offs between reduced risk and premium credit.
- Willis Towers Watson has synchronised the activities of our Power Broking hubs globally in the search for the most competitive pricing and market access points. While this provides wider market access and more options, in the current market it has not alleviated the premium rate increases significantly. We are also seeing a strong

move to more centralised underwriting among major international insurers - markets in, say, Singapore will refer risks back to their London underwriters.

- Market increases are ranging between:
  - London: +20% starting point for clean business
  - Singapore: +25% starting point for clean business
  - Dubai: +17.5% although less for more “favoured” accounts.

The Outlook

- The Market remains hard, with some evidence of slightly lower increases, however most insurers’ staring point will be +20%.
- Centralisation of underwriting is reducing market access points
- Detailed underwriting information, well-developed marketing strategies and greater flexibility in terms of limits, deductibles and certain covers remain key to renewal success.

Our key message is to plan ahead:

- Engage experienced WTW risk engineers early to survey your site and provide comprehensive risk engineering surveys and support
- Understand your risks and coverage requirements to enable the most cost-effective programme to be designed (don’t pay for what you don’t need…)
- Have a clear marketing strategy including careful market management and early engagement with key insurers
- Work with WTW to develop the best possible presentation of underwriting data to the insurance market
- Start placement early and allow WTW the time to assemble the optimum risk transfer solution available for you
- It is important for power sector companies and their brokers to engage with insurers as early as possible and provide risk management protocols and up to date underwriting information such as survey reports and detailed Business Interruption breakdowns.

In these challenging conditions, organisations should think very carefully about which market relationships they value as we think a relentless focus on price above any other factor may run the risk of backfiring – especially if a loss is incurred.

General Liability

Power organisations seeking cover in the General Liability market also continue to face challenges. Deteriorating underwriting results and the rising social inflation costs driving larger liability losses has resulted in continuing reductions in actual available market capacity, as opposed to theoretical capacity. The Lloyd's energy casualty insurance loss ratio for 2020 is currently sitting at 110.3%

The energy insurance market (including power) is increasingly segmented, devolving into four key segments:

- Core Existing Markets: we are seeing measured and, in relative terms, fair market increases
- Volatile Existing Markets: these tend to be unpredictable and may totally re-rate pricing
- New Markets: minimum rates often higher
- Opportunistic Markets: looking for the highest price they can achieve.

Underwriters have taken a definitive position on cyber coverage; it is either excluded from policy wordings or provided on an affirmative basis. In addition, underwriters have introduced Communicable Disease exclusions, ranging from blanket exclusions for all forms of communicable diseases to some insurers preferring to abstain from applying any exclusionary language altogether.

> **Pricing and policy conditions hardened considerably throughout 2020, and this trend is continuing through 2021. Market capacity is significantly reduced, and we have seen a number of accounts renewed with reduced limits.**

An inconsistent and segmented market has resulted in a large range in renewal pricing outcomes. New or replacement capacity is significantly more expensive. A key driver for insurers is "Rate Adequacy", which to date in 2021 has meant:

- Price increases across all layers
- More "measured" increases for primary policies
- Larger increase on excess layers, due in the main to minimum rate issues
- Latest average Q2 2021 increases ranging from +30% to + 40%
- Some excess layers are renewing in excess of +100%.

Notwithstanding a theoretical capacity available for power risks of US$3 billion, the more realistic available capacity is closer to US$1.2 billion. Power organisations should be prepared for continued upward pressure on rates and for insurers to take a much firmer stance on risks that do not fall within their underwriting appetite.

As we reported in 2020, larger programs are likely to face a significant challenge when it comes to maintaining existing limits as the pressure of market contraction and reduced capacity deployment takes effect.

Trade Credit

Trade credit insurance supports self-liquidating business-to-business trade across both domestic and export categories.

Apart from providing indemnification for a bad debt, policies are often used to identify new markets and ensure customers are safe in the knowledge the Insurer will support this increased trade. Financiers often look to enhance their security by taking a lien over policies issued, in turn providing support for additional funding options or reduced interest rates.

Since the beginning of 2021 we have seen a change to the trade credit insurance market. Anticipated levels of delayed payments and payment defaults have not eventuated to the levels predicted by insurers. This is a massive contrast to the same time last year where there was much concern among insurers unsure of how the economy would perform. Through the actions taken by insurers we saw a comprehensive review undertaken of their risks while, at the same time, premium rates increased to reflect the changing economic environment. Policy structures were also amended resulting in a change to the degree of risk shared.

Insurers are now considering new business opportunities, their appetite for increased credit risk support has improved and policy structures are more negotiable.

Trade credit insurance has always played a vital role in protecting the supply chain, however insurers are now insisting on improved visibility of customers' financial information before committing to their ongoing support. New Zealand businesses are not used to sharing this information, but it is a common practice across most advanced economies. Business here will need to accept and adapt to these new requirements, which will create challenges for some industry sectors that are undercapitalised or have performed poorly.

Both the building and construction and retail sectors continue to be difficult for the trade credit market with some high-profile insolvencies. Insurers will continue to participate in a cautious manner in these sectors.

The Outlook

After years of declining premium prices, we have seen a correction to reflect the increase in global risk. Insurers remain selective around the business they consider; the credit risks they are being asked to assume and the policy structures offered. That said, insurers are focused on looking after their existing clients and, as the economy improves, they will welcome more new business.

Want more information?

To get in touch with our brokers and consultants visit our website for contact details of our office locations.

About Willis Towers Watson

Willis Towers Watson (NASDAQ: WLTW) is a leading global advisory, broking and solutions company that helps clients around the world turn risk into a path for growth. With roots dating to 1828, Willis Towers Watson has 45,000 employees serving more than 140 countries and markets. We design and deliver solutions that manage risk, optimise benefits, cultivate talent, and expand the power of capital to protect and strengthen institutions and individuals. Our unique perspective allows us to see the critical intersections between talent, assets and ideas – the dynamic formula that drives business performance. Together, we unlock potential. Learn more at willistowerswatson.com.

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