Energy, Power, and Renewables Insurance Market Update

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UPSTREAM

As we enter the second half of 2024, the upstream insurance market continues to soften, with most subsectors of upstream energy now seeing improving terms on their property insurance renewals. At the beginning of 2024, we predicted we would see the market tipping in the buyer's favor, and this has proven to be the case. There was a sense as we closed out the 2023 year that we would see a renewed appetite for underwriters looking to increase their market share and deploy capacity in the upstream class, and this has proven to be true. The theoretical market capacity is now touching $10 billion, which is at an all-time high, and the amount of true "capacity risks" is now limited to a handful of buyers. There are pockets of the upstream market that continue to be a challenge; however, most of the well-known and popular risks that have renewed in the first half of 2024 would have experienced improving conditions. Single-digit rate decreases for offshore exposures have become the norm, with examples of significant reductions being made available to those accounts willing to compete for their leadership. The onshore section of the market has held a rating of "flat," but as we head into the second half of this year, we also see this softening. The lack of loss activity and continued excess capacity are creating a buyers' market for the rest of the year.

Actuarial observations of the upstream loss record and major loss frequency suggest that, in the past ten years, the industry has become safer due to a renewed emphasis on safety and the additional worries that oil and gas companies have about the reputational risk of an incident that would make their operations public. The true cost of a fire on a platform or an oil spill is not about insurance but about the companies being able to continue to operate or raise finance going forward. The industry has never been more focused on safety and any reputational damage that a loss could cause to the integrity and reputation of the industry, and this has in turn meant that upstream underwriters continue to try to deploy capacity into the sector, which continues to apply pressure on rating.

ESG continues to be a concern for investors and insurers, but we haven't seen a withdrawal of capacity owing to ESG pressures. The market has become much better at talking about ESG and the insurer's role in transition, emerging markets, and technology, among other things. Greenfield exploration will need to have an excellent story on ESG, especially with European insurers, who have a heavier focus on ESG. Unlike their US, Canadian, and Asian counterparts, who place a greater emphasis on energy security and the importance of oil and gas in geopolitics.

Commodity prices have remained stable for the last 18 months, at a price where the market clients are profitable but where capital discipline remains. This is good for insurers as Capex will go to safety; however, we do not see companies rushing to produce through the drill bit, which is a dynamic that can be seen in very high commodity price environments. In addition to commodity prices, the relative cost of risk transfer to insurers' balance sheets has cooled, and inflationary pressure is receding.

Government policies and economic conditions remain unpredictable, but in the current environment, the client base for the upstream market is proceeding with caution but is profitable; this creates an attractive market for insurers as they know that safety capex budgets will be healthy and any capex going back into the drill bit will be well planned and executed.

High oil price environments have historically resulted in more loss activity as clients have rushed to bring production online, but what we are seeing now is oil and gas, sector leadership commitment to safety and performance, hazard identification, risk management, and reporting occurrences of near misses to prevent future incidents.

Due to all of the aforementioned reasons, the market is still active and steady from the standpoint of the customer and the insurer, but most purchasers are experiencing overcapacity, which presents difficulties for brokers and underwriters. For the remainder of 2024, we believe that will remain the case, barring a significant loss event in the upstream sector. As we are in the midst of a hurricane season that is predicted to be active in the Gulf of Mexico, it is always challenging to advise clients on what market conditions to expect for the remainder of the year. However, all insurers have budgets to fill and their fixed costs remain the same, and as rates start to cool and they look to replace missing revenue with a similar number of buyers, it could create a snowball effect in that leaders will have to offer bigger reductions to maintain their position. Well-regarded accounts should expect to see meaningful rate reductions for the remainder of 2024, with all bar a handful of risks seeing capacity far exceed the limits being purchased.

MIDSTREAM

In 2023, midstream (re)insurers faced challenging market conditions due to some significant and isolated incidents in the USA and Middle East, as well as some severe wildfires in Alberta, Canada. Regarding the wildfires, while few oil and gas companies experienced any actual physical damage, the (re)insurance market suffered a high number of business interruption (BI) claims. As such, we have seen a tightening of policy terms and conditions, namely around additional coverages such as interruptions from denial of access and civil and military authorities.

Determining the final quantum of these wildfire claims took some time due to the involvement of forensic accountants and the additional work required by loss adjustors given the fact that they were financial losses rather than physical damage (PD). As a result, we continued to see consistent rate increases from the back end of 2023 into the first quarter of 2024. During the second quarter of 2024, however, the total claim amounts for these wildfires became much clearer, and reinsurers observed steady decreases in their overall net reserves, which contributed to a moderation of increases.

Other key factors having a positive impact on the midstream market are:

1. The improved outlook for the global economy, namely the tailing off of inflation (in sharply rising inflation environments, (re)insurers become very concerned about valuations given the increased likelihood of claims costing considerably more than originally anticipated), and largely restored supply chains.
2. The stabilization in commodity prices has meant that the spikes in BI values witnessed in 2022 and 2023, have subsequently retreated and allowed for more balanced PD and BI programs.
3. An uptick in available Domestic and London capacity.

Expanding on point three, we have seen a softening rate environment in the offshore space coincide with the noted increase in available capacity and have even seen some more traditional “upstream” (re)insurers decide to branch into the midstream space, primarily to increase their GWP’s in line with their stringent 2024 income targets.

For the midstream sector, halfway through 2024, this means continued downward pressure on the rating environment, which has already moved average program rate increases into the early single-digit region. Even considering this positive pressure, (re)insurers continue to witness total annual claims outweighing the global premium pool, and therefore, the midstream sector remains harder than the traditional upstream market.

DOWNSTREAM

As anticipated, the market is softer in terms of ratings as we move into the second half of 2024. The previous several years have seen a massive influx of premium income into the market, which has had a multiplier impact on premium income due to rising base rates, inflationary pressure on the physical assets of the insured, strong profit margins, and supply chain delays driving greater BI indemnities. Insurers have benefited from a sizable increase in premium income, which has a beneficial net effect against any losses.

Of course, the level of softening is as ever dependent on numerous factors, including the usual considerations of premium volume, loss record, risks deemed to be well-engineered, and the amount of critical Nat Cat exposure, i.e., risk location.

One of the key factors behind this momentum shift is that 2023 was a relatively benign loss year for downstream insurers, with a return to profitability for most. Last year's profits, in addition to a positive Reinsurance Treaty Renewal Season, have indeed led to an increase in capacity, both from existing insurers and with the introduction of new markets/MGAs into this class of business. This has led to a scramble for signings and, in some cases, even participation in high-profile risks.

Areas that require continued monitoring are ESG, business interruption, valuations, and more recently, wildfires (not necessarily in that order):

- **ESG:** There continues to be no market consensus on this issue. As has been widely reported, some of the major European insurers have tended to be the ones taking the toughest stance, and it will be important to keep a close eye on how their positions could affect future market capacity, particularly in certain sub-sectors of the downstream book.
- **Business interruption:** This coverage continues to be under the spotlight across the market, and with the release of the new LMA 5515A Clause (which includes a Partial Loss Adjustment Factor), this is deemed a way for insurers to further reduce the uncertainty of any potential claim amounts. From a client's perspective, the best way to push back on this is to provide ever more detailed and regularly adjusted breakdowns of their business interruption values.
- **Valuations:** Insurers continue to expect clients to have undertaken recent revaluation exercises to ensure their asset base is correctly valued in what, post-COVID-19,, has been a highly inflationary environment across the globe (although this is starting to slow down). Many clients we have seen have employed major valuation companies to assist with this exercise, and when this occurs, it is well received by the market. Where no recent valuation exercise has been undertaken and insurers deem there to potentially be underinsurance, then the market will look to impose either an average or a rating load to compensate.
- **Wildfires:** This is becoming more topical in certain areas of the world, with insurers requiring to be updated on vegetation management and firefighting capabilities.

For the second half of 2024, we are shifting to a market that is in many clients' favor, but with a lively start to what was already expected to be an above-average named windstorm season, all eyes will be on how insurers react if there is a major loss.

POWER

The Power Generation market is shadowed by several geo-political stressors, foremost being turmoil from the Russian-Ukraine conflict, and the subsequent global rise in inflation, which continues to raise questions around energy security. More recently, the Israel/Gaza conflict (and the areas of conflict all around the region) has reiterated that supply chain issues and energy security are still very prevalent and capable of causing significant stress to the Power Generation insurance market. These pressures loom even before we consider the various sizeable losses in the market and the poor year that North American insureds had in 2023.

There have been several recent high-profile moves in the market to new organizations (departures from Travelers in London and Tokio Marine Kiln HCC have formed a new Power Generation team) and various new MGAs popping up in both London and international markets. Nevertheless, there has not been the significant injection of capacity that buyers need to meaningfully suppress the current rating environment. While these changes haven't quite yet pushed the balance of capacity into an environment beneficial for insureds, it could be a positive sign of things to come.

There are signs of change ahead and hopefully a better buying environment, with some positive signs emerging. A handful of London property markets participate on Power Generation accounts, largely supporting the non-proportional structures in our placements, and they are in a rapid and significant softening phase, which has helped drive competition.

This market saw rapid increases in prices after the 1/1/23 treaty renewals (in particular for Nat Cat capacity), even during a large softening phase. This is great news for our clients who have support from these markets and should help with the overall pricing.

In the years following the start of the pandemic, there has been a real focus on insurers insisting on the accurate reporting of values. In response to this, insureds have increased their efforts toward accurately appraising their assets; markets have seen this, and it has led to a slight softening of expectations from insurers. This is certainly the case where insurers have previously had to price in an ambiguity factor for values that were not up-to-date.

Global capacity for this risk class is still very abundant, with no major exits from the power market in recent months. What's even better for buyers is that, as more MGAs appear, and more Lloyd's property syndicates consider writing power and wider energy business to supplement premium losses on their Direct and Facultative books, there will be increased competition that helps to drive down pricing.

Although there have not been any major withdrawals within the last six months, coal capacity is still significantly less than what is available in the wider market, with virtually all the large European reinsurers now not supporting new business.

CASUALTY

International casualty

Facing a pessimistic run-up to the reinsurance renewals on January 1, with many treaty reinsurers expressing concerns about the market, most reinsurance buyers ended up with "as before" type renewals, correlating with direct buyers seeing flat renewals. Insureds that are willing to change their panel of insurers are oftentimes seeing moderate decreases given that there remains an abundance of capacity for "most" buyers in the international energy liability space.

There is still a lot of caution from insurers where international liability risks have any US exposures, and we expect this element of accounts to continue to be a difficult write-off for those markets that favor non-US risks.

It also ought to be mentioned that insureds have paid increases in premiums over multiple renewal cycles, so there is hope that we are at, or very close to, rate adequacy, and this has filtered through to underwriting results.

US energy liability

Loss deterioration from previous years remains a prominent issue, with losses from 2019–2021 showing significant worsening. Certain insurers, both in London and domestically, are reassessing their risk appetite and seeking to reduce their exposure at specific attachment points and within certain sub-classes.

We are observing a trend of large domestic US insurers reducing their limits on lead umbrellas and prioritizing pricing on primary lines such as auto liability, general liability, and workers' compensation. $5 million lead umbrella limits are becoming far more common, whereas in recent years we have seen $10 million.

General liability rates are experiencing increases ranging from +2.5% to +7.5%, whereas umbrella rates are experiencing +5% to +10% increases.

While there is still ample capacity available in the excess liability market in London, claims inflation remains the primary factor impacting loss records, as the increasing frequency and severity of litigated claims continue to place significant pressure on excess liability carriers. As settlements grow and nuclear verdicts become more common in trials, carriers across all segments are closely examining the limits and premiums associated with their excess products to ensure sustainability.

Companies with larger fleets or losses are facing capacity challenges due to severely litigated auto liability and bodily injury claims, which continue to erode profitability for London insurers.

The upstream space has stabilized since Markel withdrew from JH Blades a couple of years ago. JH Blades has a new facility, but it appears to be less powerful than it was when the authority sat in-house.

While the market is not devoid of losses, it is in a stable place, and the reinsurance renewals at both 1/6 and 1/7 were relatively uneventful. There is a feeling that reinsurance renewal next year will be driven by the 2024 Nat Cat season, where most capacity providers are either profitable or trading at a loss.

RENEWABLES

The first half of 2024 has seen a continuation of natural perils impacting the insurance market, giving rise to the frequency and magnitude of solar claims. Some of the assets affected have been in unmodelled locations due to the data software not yet having full accuracy for all perils geographically. From January 2025, there will be multiple data software upgrade products that will become available to improve the visibility of all Nat Cat exposures.

The onshore wind market is seeing a rise in Chinese Original Equipment Manufacturers (OEMs) being installed in certain territories by offering an attractive cost reduction compared to their European-origin OEM competition. This is likely to drive the need, by client and insurer, for an extended monitoring period to foresee the success of these turbines and their warranties. Ultimately, this is a positive for the renewable energy industry globally as it pushes forward to reach installed gigawatt (GW) targets.

The offshore wind market remains attractive to new insurers coming in to increase market share globally. Standardization can be seen in the sector, which should lead to clearer claims outcomes and shorter development windows, a necessity to meet GW targets set for 2030 by many countries that already have a considerable GW number of installed assets.

The BESS market is stable as site layouts have become more uniform in guidelines for spacing and equipment separation. This enables insurers to quantify Probable Maximum Loss (PML) values more accurately, which supports rating and deductible stability.

Overall, the downward premium rating turn of the market has begun to take place for clean or well-running accounts where competition amongst insurers for market share is taking place. Further improvements to existing technology protections and performance will continue this trend as new and existing insurer capacity increases.

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