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# State of the Canadian Commercial Property & Casualty Insurance Market

**Pressures Facing the Canadian Commercial Insurance Market in 2020**

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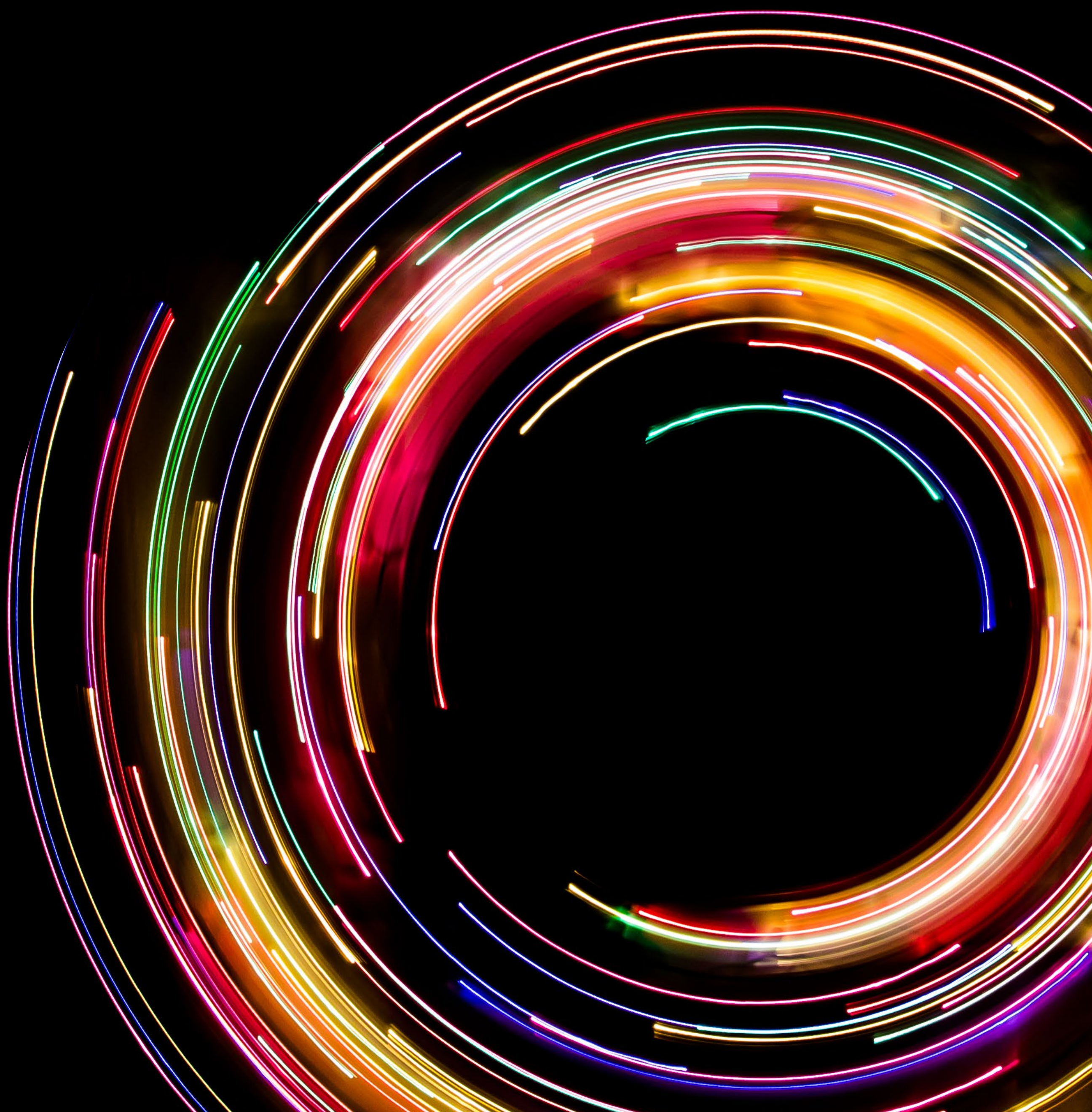

# Executive summary

The core objective of commercial insurance is to financially protect businesses and non-profit enterprises against the insurable risks that they face. Currently, the Canadian commercial insurance market is facing a period of significant change. Several sizable external pressures are negatively impacting insurers, intermediaries, and their clients and creating tension in the commercial insurance market.

The Canadian commercial insurance market became a "hard market" in 2019, which means the market entered a period of higher rates and reduced underwriting capacity for certain lines of business and/or geographies (e.g., commercial property). Years of insufficient underwriting profitability, driven by rising claims costs, and low returns on investment led to an overall decline in net income between 2015 and 2019 for property and casualty (P&C) insurers. The environmental and macroeconomic events of 2020 have exacerbated these market dynamics, driven by three immediate pressures:

**Immediate pressures**

**Rise in extreme weather events**

Canada is experiencing an increase in the severity and frequency of extreme weather events, which have led to a significant rise in catastrophic losses. Over the last five years, the costs to cover losses from floods, wildfires, and storms have increased, with the highest natural catastrophe loss for a single year occurring in 2016, at the cost of $5.1 billion.

Insurers, intermediaries, and clients are feeling the impact of these catastrophic events. Insurers face growing volatility in the risks they cover due to the unpredictability of extreme weather, alongside rising claims losses. Intermediaries struggle to place coverage for their clients. Businesses face growing costs associated with extreme weather damage, including property damage, liability costs, and potential incremental costs of doing business (e.g., investments into staff safety).

The frequency and severity of extreme weather events are projected to continue to rise, creating sizable pressure on the commercial insurance market.

**COVID-19 pandemic**

COVID-19 has created a global health crisis, with a broad range of impacts, including financial strain on Canadian businesses and the global economy, and changes to the risk exposures that insurers and businesses face.

The impact of COVID-19 will be disproportionately felt by certain industries (e.g., Arts and Entertainment, Accommodation and Food Services) and small businesses. Insurers will face greater financial challenges as their clients' risk profiles change, and premium volumes decline due to business closures.

COVID-19 has compounded pre-existing hardening market conditions, worsening the tensions between insurers, intermediaries, and clients.

**Macroeconomic conditions**

Insurers have faced multiple years of low investment returns, driven by declining bond yields. This pressure has been enhanced in 2020, as COVID-19 led to unprecedented economic uncertainty and drove Canada into the deepest recession in its history.

Economists project that Canada will experience a 5.8% decline in GDP in 2020. Insurers will receive fewer premiums, as a growing number of clients cease operations during this economic decline. While growth is projected for 2021, it comes in a period of record low interest rates (e.g., 0.4% for a five-year government bond), placing further pressure on insurers to improve underwriting profitability to counter the declines in investment performance.

Global macroeconomic conditions remain uncertain and global investors are therefore hesitant to provide capital. Insurers may accept less risk and reduce their underwriting capacity to ensure sufficient financial strength to service future claims.

### Industry financial performance

By the end of Q2 2020 (YTD), the P&C insurance industry's financial performance remained strained. The industry experienced a sizable underwriting loss (-$564 million), alongside a 28.6% decline in investment income. While net income increased by $138 million compared with 2019 YTD, this was driven by a sizable increase in "other revenue" of $668 million, which rose largely as a result of accounting adjustments (e.g., reclassification of financial instruments, gains on fluctuations in foreign exchange rates). The increase in net income is not an improvement in the underlying drivers of insurers' performance, as evidenced by the underwriting loss and decline in investment income.

This financial pressure is felt even more by commercial insurers who experienced significant claims losses over this period. The commercial insurance net loss ratio (i.e., net claims incurred as a percentage of net premiums earned) grew by 11.5%, highlighting the financial challenges felt by commercial insurers and their clients.

### Preparing for the future

Insurers, intermediaries, and clients must prepare themselves for a continuation of current hard market conditions. A full Canadian economic recovery is forecast for 2022 at the earliest. After this point, the economic impacts on the insurance market will be reduced, which is likely to result in a rise in underwriting capacity and lower annual increases in clients' insurance rates.

However, action is still required in the short-term. Canada's insurers and intermediaries need to find creative solutions to ensure that Canadian businesses can access the insurance they need.

*__Prepared in collaboration with Insurance Bureau of Canada.__*