



Property funds prepare for insurance renewal shocks: what funds need to know

Unlisted property funds face an increasingly difficult insurance landscape as the COVID-19 recession creates a 'perfect storm' in the insurance industry, with premiums to rise further, a tightening in terms, and capacity constraints all set to test property funds.

Speaking to the Property Funds Association, Scott Curley, Director Professional Credit and Financial Risks for [GSA Insurance Brokers](#), said property funds which have not renewed their insurance during 2020 could be in for a shock. "It was a tough renewal period last year, but insurance renewals are even tougher this year due to COVID-19.

"I've been working in the insurance industry for 27 years and this is the toughest I have seen it. Unlisted property funds will need to work harder to avoid the worst of these shocks, and will benefit by working closely with risk and insurance advisors."

A key issue for commercial property assets is getting insurers to write coverage for anything below A-grade assets. But Mr Curley said even A-grade properties are facing higher premiums, limited capacity, and tighter terms.

The tightening reflects the fact many of the world's largest insurers have experienced COVID-related losses: [Chubb recently estimated COVID-19 related losses](#) of \$1.37bn in its second quarter 2020 results, representing the bulk of its \$1.81bn of pre-tax global net catastrophe losses during the period.

It has been widely reported that global insurance prices rose 19% in the second quarter 2020, marking 11 consecutive quarters of price hikes, with Australia among the most impacted markets.

Mr Curley said the environment was leading to more restrictive terms and tightening of insurance policies in an attempt to offset the rise in premiums.

Capacity has shrunk as COVID-19 impacts all corners of the globe. "We would normally see an influx of capacity coming from London, but this time we are seeing London pull back – it's the perfect storm in many ways."

He said the insurers are not under any pressure to write new business. "We may struggle to get insurers to look at commercial assets which are old, have asbestos, are made of timber, have cladding issues or are located in a regional area."





Property funds face insurance challenges in two most important areas: firstly, when insuring physical property assets, such as buildings; and secondly, when insuring the funds management business, including professional indemnity for investors.

Steadfast's most recent Infinity Report shows property insurance prices in Australia already rose 12.5% by early in the COVID-19 pandemic, and are expected to rise approximately 5-10% again. There were bigger increases along financial lines, with insurance prices rising 25% and expected to climb another 15%. Steadfast's estimates could be considered conservative given other sources are reporting even higher increases.

Mr Curley said funds with higher risk exposures can expect major premium increases come renewal time. "Any assets which have perceived significant or high risk occupancies, perceived poor construction issues, or an adverse claims history are receiving significant increases."

At the same time, capacity is being restricted. Traditionally, a major asset such as an office building would spread insurance coverage across four or five insurers. But with insurers now reducing capacity, funds and asset owners may need more than 10 insurers, and possibly up to 20 insurers to cover the same asset values as previously, according to Mr Curley.

What insurance companies are looking for during COVID-19

All property funds can expect tougher renewals during COVID-19, but Mr Curley said there are several ways funds can help themselves.

Asset quality may seem obvious, but is a key starting point: An A-grade office building will always be better placed than a C or D grade building in insurance negotiations. "Buying good buildings comes into it, but so does working with risk advisors.

"Funds need to work with insurers closely regarding risk management of the asset. Some funds might need to consider spending on the asset to reduce or even entice insurers to in the current climate."

Insurers need evidence the asset has a track record in good management. "Good defensibility material helps the risk assessor. They like to see record keeping which shows a strong track record on issues around risk management, maintenance, health and safety and so on."

Insurance costs regarding the funds management business largely rest on how the manager structures the property funds. "An obvious thing insurers look for is the amount of leverage in a fund as well as the underlying assets.





“But there are a host of other issues funds management businesses need to consider, including financial requirements and the performance of the business. Managers who are transparent and able to demonstrate their performance will be better placed.

“Responsible entities need to show how it meets minimum financial requirements over 12 months, including its cash flow, its NTA requirements, and its liquidity, which all comes into it.

“We can’t deny there will be pain for property funds come renewal time. But with some preparation, transparency, and a willingness to work closely with risk assessors, funds may avoid the worst of it”, Mr Curley concluded.

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