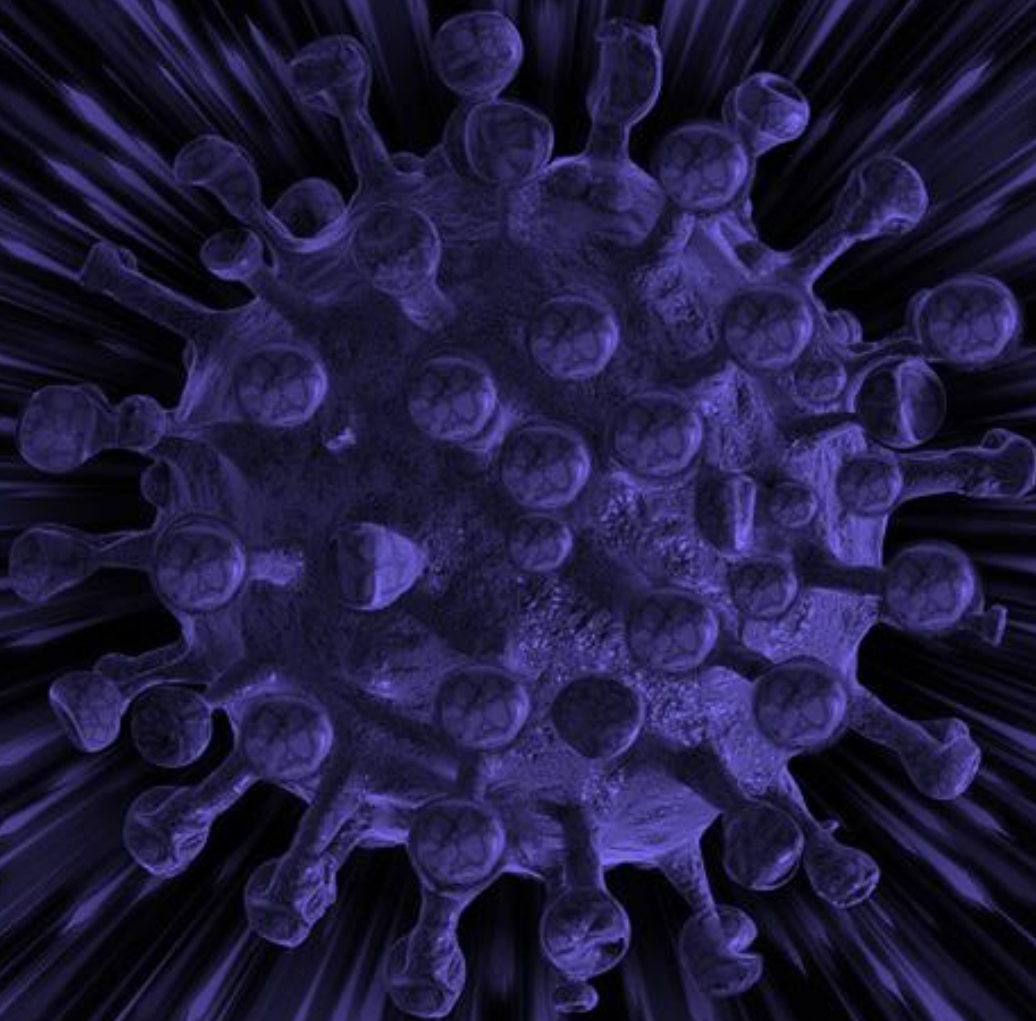


COVID-19 Newsletter

Edition 7

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Beach

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General Outlook

After the worst quarter in history, the S&P 500 had one of its best months on record in April. Though it remains well shy of pre-pandemic levels, this offers a flicker of hope and perhaps even a hint of market resilience. Caution is advised by a great many commentators who warn of a secondary dip in the market, with some stressing the view that market activity is tracking to that of the dot com crash¹. Warren Buffet's bolstered cash holdings at Berkshire Hathaway will go some way to reinforcing this belief.

One way to avoid share price uncertainty is to announce that your own is "too high", an interesting strategy deployed on twitter this week by Elon Musk, one can be pretty certain of what that did to Tesla stock value. If the health of Wall Street is wobbly, Main Street is distinctly unwell. Demand downturn is ubiquitous in both occurrence and impact – immeasurable in duration. The immediate task for industry participants to quantify how much they will have to (or should have to) pay out in claims, has been tough. The other side of the equation – the impact reduced activity and demand will have on premium levels – is far less of an exact science.

A primary factor in considering the potential impact on premium income levels will be the duration of movement / travel restriction. Central to curtailing this period will be the development of treatments and vaccines. Finding an effective one would save lives and expedite the rebooting of economies. Though underreported, clinical trials have been a key area within which insurance has been able to proactively support the fight against Coronavirus. Given the urgency, underwriting teams have been working to a tightened schedule to formalise capacity and to get trials off the ground. The flu drug Avigan is undergoing trials in China, Japan and the United States, after Japan started distributing the drug for free, to 38 different countries. Clinical trial insurance specialists mobilised swiftly to cover the process and the drug has been called "clearly effective" by Chinese medical authorities.

Considerations of force majeure rulings caught our eye this week, following a webinar hosted by the International Underwriting Association. The potential for force majeure rulings has been voiced across a number of lines of business (the case of Healthcare was approached in previous editions of this publication), however caution was raised surrounding overreliance. Cases will be viewed on their own characteristics, there will not be a general all-encompassing classification of the outbreak as one to which force majeure applies in its entirety. Further, an interesting debate was raised around the temporal aspect of force majeure, as to whether this is a single event or whether there could be separate events by line of business, industry, territory or otherwise. Finally, some sensitive discussion was raised around declaring 'business as usual', a statement many businesses would love to make, but one that could be considered to be at odds with claims of force majeure.

¹ Source: https://www.marketwatch.com/story/this-year-is-lining-up-exactly-like-the-2000-dot-com-bubble-crash-stocks-will-drop-40-from-here-former-goldman-manager-says-2020-05-04?mod=MW_article_top_stories

During the lockdown and the new working from home experience, there has been a huge uptick in the number of cyber attacks. This week we include a piece in our newsletter discussing developments in the cyber space, produced by the Beach cyber leader, Tom Quy. As insurers begin to announce their Q1 results, we have taken a few choice examples to take a look at. Finally, we consider some of the new announcements coming from no.1 Lime Street, displaying the market's continued commitment to progression.

Cyber resilience in the times of COVID-19

By Tom Quy, Senior Vice President, Cyber at Beach

COVID-19 has and is still having a huge effect on the world we live and work in. Lockdowns and social distancing remain in effect across most of the world, with a large percentage of people having to work from home. For the majority of companies, this is the first time that most, if not all, of their employees are having to work remotely and it's a scenario that many businesses were not prepared for, whether from an operational, cultural or security perspective. So, we are in uncharted waters. Yet unfortunately, even in this difficult situation, cyber criminals are still at work and are taking advantage of people's vulnerability, fears and uncertainty during this time.

Cyber resilience is not a new phenomenon but it's a topic that has been in the news a lot more as there has been an increase in COVID-19 related fraud and cyber-attacks. In the UK, The City of London police reported a 400% increase in COVID-19 related fraud within a month, with the majority of cases related to online shopping scams. Examples included people ordering hand sanitizer, protective face masks and other similar products, which then never arrived. Since February 2020 Action Fraud, the UK's fraud reporting centre, has recorded total losses of nearly £970,000 related to COVID-19 fraud. There are also fake emails purporting to be from the UK tax authorities offering tax-refunds which, at a time when people are suffering the financial impact of COVID-19, plays considerably on people's vulnerabilities.

Workplace changes and the evolution of cyber exposures

This move to remote working has meant a number of companies are relying on video conferencing software like Zoom and Blue Jeans to hold meetings and communicate with employees. Yet data from [BrandShield](#) has found that 3300 new phishing domains have been registered with the word "zoom" included, and of these, 67% were created in March – the height of the lockdown across European and US companies.

There has also been a marked increase in coronavirus-themed phishing emails, (and phishing emails are the most common form of social engineering). Criminals are purporting to be delivering information, assistance or instruction related to COVID-19, such as impersonating the World Health Organisation (WHO) or the US Centre for Disease Control and Prevention (CDC), sending emails claiming to provide the reader with a list of active infections in their area if they just click the link provided, or emails offering victims a list of safety measures, which they have to download. Once the victim clicks on the link or downloads the document, they have given the attacker access their system; the attacker can create backdoors (methods to allow access bypassing the normal security), monitor emails and other network traffic, or download malware onto the system.

Companies are also having to adapt and fix security issues resulting from the workforce operating remotely rather than in an office, on a central server and through authorized systems etc. In the initial phase of the lockdown, there were issues of employees having to work from their own devices, placing data outside of the firm's defences and control and potentially compromising security measures. Firms are also still restricted by their employees' internet connections; any insecure connections or Wi-Fi networks that are not password protected can create entrance opportunities for hackers.

Working via remote access leaves a company's systems more vulnerable than when they are controlled centrally, particularly when facing malware offensives. Companies do not have the same visibility into how people are using professional devices, and neither can they secure their employee's personal devices. There is also the risk of denial of service where the system is overloaded and crashes, due to the increased volume of remote workers. This wouldn't even necessarily be caused by external malicious involvement, but rather the system might crash of its own accord.

How should corporations respond to this?

So, what can and should companies be doing? Firstly, they have a responsibility to educate and guide their employees to identify and mitigate against these cyber threats. Human error is the most common cause of failure in a company's cyber security, so education is vital. Companies should also encourage employees to voice any concerns and know how to report suspicious emails. In addition:

- Companies should be discouraging employee use of personal devices for work unless absolutely necessary and as a last resort. Employees should be using verified company laptops and any other electronic devices, and companies should be deploying multiple methods to reduce the relative risk such as encryption, endpoint monitoring, virtual private network connections and data loss protection tools.
- Multi-factor authentication is also a key defence mechanism, and something companies should be implementing if they don't already. The process follows the 'something you know, something you have' process, so for example something you know like a password and then a text message sent to something only you have, like your mobile phone. This means that even if a hacker manages to obtain a password they are prevented from getting any further into the system, as they do not possess the 'something you have' part of the process.

Given the increased threat, we expect to see an uptick in cyber claims, so it is vital that firms have the right insurance programmes in place to help manage and mitigate these risks. Insurance is there to support businesses – it is a key part of a businesses' resilience programme. Cyber risks can be insured, solutions do exist, and they cover a broad range of cyber consequences.

There is currently no certainty around when lockdown measures will end and when people will return to offices, so it's vital that businesses prioritise strengthening their cyber security measures and IT resilience. Businesses have a duty of care to educate employees on the dangers and risks present, particularly around scams and phishing attempts relating to COVID-19. Education is key, as is ensuring a culture of openness where employees can raise concerns and log any potential cyber threats they receive. Additionally, IT and risk departments need to focus on strengthening digital defences, such as multi-factor authentication and using virtual private networks to mitigate the risks and help protect the business. Finally, businesses need to ensure that their insurance policy provides adequate cover for these circumstances and will help the business manage and mitigate the threats they face.

Q&A with Tom Quay

The cyber market was starting to see rate ahead of the crisis, do you expect underwriter discipline and the impacts of COVID-19 to keep this movement going?

We are seeing insurers reduce their line size, especially where they may have lines out on multiple platforms (Lloyd's/US/Bermuda etc.), plus a general hardening of rates across especially excess layers. We expect this to continue as the COVID losses, not just in cyber, but more so elsewhere restrict capacity. The performance of middle market cyber accounts has not been great, with a lot more pressure on rates in this space.

Some companies still see cyber as a discretionary purchase. With revenues falling across the board, is there the potential for insureds dropping the purchase? Or do you actually anticipate demand to grow as per the recent McKinsey report?

We don't expect to see many insureds dropping the purchase altogether, but we could see a reduction in total limits on some of the larger programmes. Especially where insureds have seen their revenues and more importantly their business models drastically changed. We were starting to see an increase in Cyber-Property Damage coverage being purchased in the Oil & Gas, Marine and Manufacturing sectors, and we could see the current situation slowing the development in this space somewhat. It's worth noting that for most businesses, a dip in revenue will not materially reduce their exposure and in fact the increase in remote working and a surge in attacks could create a greater risk. Here, underwriters may struggle at renewal with wanting more rate, due to market conditions and exposure, but having to sell this to an insured with less revenue than the year prior.

It sounds as though these enhancements to exposure will be more of an attritional issue than one of volatility, or could it be both?

I think you will see a spike in social engineering crime, which could be seen as more attritional, but the increased attack surface that WFH brings could lead to some significant areas of volatility. A huge increase in ransomware attacks is being seen and this could bring both attritional and severe losses.

Do you anticipate that COVID-19 and the rise of home working will impact cyber policies' necessary coverages?

Not especially. If you have a well drafted, up to date policy wording.

Any jurisdictional differences of note? (e.g. anticipated rise in non-US and SME demand)

I think the general trend for an increase in cyber in non-US regions will continue. SME demand will also continue to tick up.

Tom is an experienced cyber insurance specialist focused on placing cyber programmes for insureds located globally on both an individual large risk basis and for SME's via facilities. Prior to joining Beach, Tom headed up the Miller Insurance Services cyber team. He has over ten years of experience working within the cyber market and was recently named 'Most Skilled Cyber Broker of the Year' by the Insurance Insider.

If you would like to find out more about the Beach cyber offerings, please contact one of our team members listed at the end of this newsletter.

Q1 2020 Earnings Releases

The below table summarises the performance of various companies in the 3 months up to 31 March 2020 compared to the same period in 2019.

All figures below are presented in millions of USD unless stated otherwise.

	Net Premiums Earned			Underwriting Profit/Loss			Estimated Covid-19 Losses			Combined Ratio			Net Investment Income			Income attributable to shareholders			Earnings Per Share		
	2020	2019	% +/-	2020	2019	% +/-	2020	2019	% +/-	2020	2019	% +/-	2020	2019	% +/-	2020	2019	% +/-	2020	2019	% +/-
AIG	6,079	6,713	-9.4%	(87)	179	-148.6%	272	-	n/a	101.5%	97.4%	4.1%	2,508	3,879	-35.3%	1,742	654	166.4%	2.0	0.8	164.0%
Arch	1,744	1,369	27.4%	154	260	-40.8%	87	-	n/a	91.5%	81.7%	9.8%	145	157	-7.6%	134	438	-69.5%	0.3	1.1	-70.1%
Axis	1,089	1,134	-4.0%	(197)	78	-352.9%	325	-	n/a	119.8%	96.9%	22.9%	93	107	-13.2%	(185)	98	-288.8%	(2.2)	1.2	-289.7%
Chubb	7,794	7,137	9.2%	824	669	23.2%	13	-	n/a	89.1%	89.2%	-0.1%	861	836	3.0%	252	1,040	-75.8%	0.6	2.3	-75.6%
Fairfax	3,388	3,522	-3.8%	103	88	16.6%	84	-	n/a	96.8%	97.0%	-0.2%	(1,621)	998	-262.4%	(1,389)	815	-270.4%	(47.4)	27.0	-275.6%
Hannover Re *	5,090	4,610	10.4%	(45)	75	-159.7%	220	-	n/a	99.8%	95.7%	4.1%	471	399	18.1%	300,887	293,653	2.5%	2.5	2.4	2.5%
Markel	1,330	1,203	10.6%	(240)	61	-493.4%	325	-	n/a	118.0%	95.0%	23.0%	88	104	-15.4%	(1,353)	732	-284.8%	(100.6)	42.8	-335.3%
Munich Re *	12,646	11,632	8.7%	221	633	-65.1%	800	-	n/a	106.0%	97.3%	8.7%	1,920	1,757	9.3%	222	632	-64.9%	1.6	4.4	-63.9%
Renaissance Re	913	550	66.0%	64	154	-58.4%	104	-	n/a	93.0%	72.0%	21.0%	99	82	20.7%	(82)	273	-130.0%	(1.9)	6.4	-129.4%
Swiss Re	9,586	8,933	7.3%	(225)	429	-152.4%	223	-	n/a	110.8%	110.3%	0.5%	n/a	n/a	n/a	27,979	29,251	-4.3%	n/a	n/a	n/a
The Hartford	4,391	3,940	11.4%	220	217	1.4%	50	-	n/a	94.9%	92.7%	2.2%	459	470	-2.3%	268	625	-57.1%	0.7	1.7	-56.7%
Travelers	7,229	6,855	5.5%	288	395	-27.1%	86	-	n/a	95.5%	93.7%	1.8%	611	582	5.0%	600	796	-24.6%	2.3	3.0	-22.1%
W.R. Berkley	1,691	1,592	6.2%	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	174	158	10.1%	(4)	180	-102.2%	(0.0)	0.9	-102.1%

Notes:

Those companies with an asterisk (*) next to their name are reporting in millions of EUR.

The earnings per share figures are not in millions.

W.R. Berkley's combined ratio is that of their Commercial Lines division.

April Earnings Season – Looking Below the Surface

With the first earnings season of 2020 now in full swing, the costs that the coronavirus has truly had on the economy's publicly traded constituents are becoming clear. Many companies sought to manage expectations well in advance by issuing press releases stating that any prior guidance should be disregarded, however early warning signs don't make the outcome any prettier.

Berkshire Hathaway with Warren Buffett at the helm, were one of the big entities to hit the headlines this week with the announcement that they had suffered a net loss just shy of \$50bn for the first quarter. This would be enough to cripple most companies a dozen times over, but according to Mr Buffett, judging Berkshire on its net loss alone is "meaningless". This view can be proven true for a number of reasons:

- Berkshire's operating profit rose 6% relative to 2019², which Mr Buffett believes is a truer measure of performance;
- Cash rose to \$137bn, a sum not to be ignored;
- \$49bn of the \$55bn in investment losses suffered are due to accounting rules that, when reporting unrealized stock losses and gains, cause large swings in earnings. This contradicts many who are quick to judge and cite that the loss is attributable to the fastest bear market ever experienced, at the start of March.

Warren Buffett also announced at the annual shareholders meeting that he had taken the decision to sell his stake in all airline companies, even though this came at a large cost to the business. Much like the airlines, Berkshire's share price is still nowhere near reaching the heights it revelled in prior to the crisis.

Covid-19 Induced Underwriting Losses

At first glance, AIG's first quarter results paint a different picture to that that might have been expected, with the underlying message that "AIG was in a strong financial position before this crisis began and remains in a strong financial position today"³. They reported a 166% higher income attributable to shareholders for the 3 months ended 31 March 2020 than that of the first 3 months of 2019. This taken alone however, is potentially misleading given that they saw \$3.5 billion of pre-tax net realized capital gains thanks to the mark-to-market accounting principles.

Upon deeper inspection, the effects of Covid-19 are clearly visible – AIG would have achieved an underwriting profit had it not been for the impact of \$272m in estimated Covid losses, resulting in an underwriting loss of \$87m. According to AIG's President and COO Peter Zaffino, they "looked at everything where there was a potential [loss] and evaluated whether there would be reason to put up a reserve. If [there] was, it was done. So we have posted the reserves that we believe are appropriate, albeit conservative, for that."

² Source: <https://berkshirehathaway.com/qtrly/links1stqtr20.html>

³ Source: https://www.aig.com/content/dam/aig/america-canada/us/documents/investor-relations/2020/aig_reports_1q_2020_results.pdf

Much like AIG, Axis' underwriting result suffered at the hands of Covid-19. Due to estimated Covid-19 losses equal to \$325m, Axis first quarter yielded a \$197m underwriting loss. Off the back of this announcement, AM Best has downgraded their financial strength rating from A+ to A, citing their operating performance as the cause⁴. This is something that many are speculating will become more frequent over the coming weeks.

Escaping Q1 largely unscathed?

Unlike the aforementioned companies, Arch and Chubb are amongst those that still earned an underwriting profit in the first quarter. Both companies' Covid-19 loss estimates as shown on the prior table are much less significant, but Chubb noted that although there was no significant impact in Q1, they are anticipating a more meaningful impact in the following quarters due to both an increase in claims and recessionary economic conditions⁵.

AXA, in a similar boat to Chubb, also spoke to the fact that Covid's impact in Q1 was not as detrimental as might be expected. AXA published their Q1 performance following the close of the markets on Tuesday and investors responded positively to their results, with the stock price trading marginally higher at market open Wednesday. Their full Q1 financial update is not due to be released until later this month, but early signs from their press release this week indicate that the impacts of Covid are still yet to be of significant detriment to their business. Thomas Buberl, CEO of AXA, stated that despite there being limited claims activity in March, the impact of the coronavirus will have a material impact on their 2020 earnings⁶. This is certainly a space to watch out for.

Looking to the other side of the pond, Mapfre hosted a webcast⁷ to inform stakeholders of their Q1 performance in advance of their full financial release. Unlike many other insurance companies, they did not spend too much time dwelling on the impacts of Covid-19, merely stating that they have sufficient liquidity and that they are constantly monitoring the impact on their balance sheet. Instead, they made sure to note the impact of NatCat events that have not gained the attention they necessarily warrant, in particular the earthquake in Puerto Rico and storm Gloria in the Northeast of Spain. Given that they chose to highlight this as opposed to Covid's impact, may suggest that the pandemic has not been too much of a hindrance on Q1 performance. Overall, the messages delivered by Mapfre are likely to be highly reassuring to their many stakeholders.

Finally, returning to the wisdom that Warren Buffett imparted upon us in the Berkshire Hathaway AGM this week: "In 2008 and '09, our economic train went off the tracks. This time, we just pulled the train off the tracks and put it on a siding." This should provide solace to all of us.

⁴ Source: <https://news.ambest.com/newscontent.aspx?refnum=225026>

⁵ Source: https://s1.q4cdn.com/677769242/files/doc_financials/2020/q1/1st-Quarter-2020-Earnings-Press-Release.pdf

⁶ Source: <https://www.axa.com/en/newsroom/events/20200505-q1-activity-indicators>

⁷ Source: <https://www.mapfre.com/en/financial-information/>

Lloyd's of London – Getting Back in the Room

For an industry that is considered to be somewhat archaic when it comes to technology, a great many of the friends of Beach have considered their move to “WFH” to have been fairly seamless and even rather agreeable. Plans are now being made to return to the office and for the underwriting room to be reopened at Lloyd's of London at some stage in the summer, after a closure not seen for some 330 years. A detailed plan is being drawn up as to how this will be possible whilst taking heed of the governmental advice. Brokers sat in gangways? No lifts? Face masks? Life will certainly not be back to normal.

Syndicate in a Box (SIAB)

Lloyd's recently unveiled their latest innovation, an attempt in providing eased underwriting access to new potential participants. Likely a long-term plan coming to fruition, it has exceptional timing as it provides a monumental step towards remote underwriting. With the closure of the trading floor and the move to remote working, Coronavirus has raised discussion surrounding whether there still needs to be a physical trading floor. With no physical footprint in Lloyd's, Syndicate in a box is a new, more capital efficient way of entering the market; designed with some added constraints to in return allow a more streamlined entry with added Lloyd's integration.

Consisting of a 3 year life-cycle, syndicates in a box are allowed to enter with removal of the 20% new entrant capital uplift, use of the Lloyd's benchmark model for all 3 years, (removing need for an internal model), the option to defer central fund contributions from years 1-3 to years 4-6, and flexibility in line size dispensations. Along with other benefits, this comes at the cost of added restrictions on business to be underwritten, agreed exit plans to facilitate fast failure as well as fast success, and connection requirements of relevant platforms. (Amongst other restrictions and benefits).

The idea is for new innovative syndicates to use this as an easier route into the Lloyd's market, with the intention that after the 3-year cycle, syndicates will graduate to a 'full' syndicate, with the option to reapply as a syndicate in a box. Clearly, there is question as to whether this is the first step in the direction of mainstream remote trading. With the current work from home situation showing success, and the prospect of reduced operating costs from virtual trading, what would stop the call for syndicate in a box to be extended to larger companies without the added restrictions in place for new syndicates.

Carbon Underwriting have received in-principle approval from Lloyd's to launch the first SIAB (Syndicate 4747). The syndicate will be agnostic in terms of class, focusing on coverholder partnerships in the international space. As with most things new at present, the start-up has a 'technological edge', through the deployment of their platform Graphene which is an informative underwriting data provision tool. The syndicate will have a stamp capacity of £15m. As outlined above, the syndicate will have no presence in the Lloyd's building.

Further Initiatives

- Streamlined planning – syndicates that satisfy the key performance indicators at Lloyd's will be given the same "light touch" treatment as top performing entities.
- Fast tracked capital – pre-approval programme to achieve confidence in models ahead of submission. Subject to no material change in the model, this will reduce the amount of review required across the capital planning group process.
- New Syndicates
 - o AIG 2019 – AIG hope for this to be the largest ever to be launched through Lloyd's, exclusively reinsuring risks from AIG's Private Client Group.
 - o Brit follow only – Brit received approval in principle to start writing follow line business from the 1st of January 2012. Interestingly, their original intention was to pursue a SIAB solution as outlined above.

Fast tracking, streamlining, fresh syndicates – Lloyd's clearly sees an opportunity to keep driving their commitment to modernisation and change.

As always, if you have any questions about any of the content in this newsletter or you might have any enquires regarding the suite of services offered by the Beach team, please do not hesitate to contact any member of the team on the contacts page below. Stay safe.

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