



# GLOBAL ENERGY INSURANCE MARKET UPDATE

August 2021



**Gallagher**

Insurance | Risk Management | Consulting

# INTRODUCTION

- COVID-19 continues to present challenges, particularly for risks where on-site engineering is required—insurers and insureds are adapting well to the use of remote technology, although it is far from ideal.
- Some energy sectors are seeing continuing capacity withdrawal on environmental concerns as a result of pressure on insurers from environmental, social and governance (ESG) lobbyists, in particular oil sands, coal-fired power generation and some offshore drilling activity (e.g., Arctic region).
- Oil prices have returned to pre-pandemic levels, but rig counts overall are still at around 50% of the levels in early 2020 (although to some extent this reflects a displacement of older equipment).
- In the upstream market so far in 2021, on average we have seen single-digit rises in the range of 2.5%–10%. Underwriters are continuing to scrutinise specific sections like loss of production income (LOPI) and control of well. The higher rate increases have been seen mostly on smaller accounts or niche areas such as onshore contractors.
- 2020 saw the downstream market make a profit for the first time in a number of years. The rate rises seen over the past 18–24 months are beginning to plateau. Those insureds with good risk engineering and a good loss record are now looking at 10%–15% rate rises compared to the 20%–30% in early 2021. Total capacity appears to be fairly stable at approximately USD 4 billion.
- The power market has continued in 2021 where it left off in 2020; rates are still rising, albeit perhaps a little slower than at the start of the year. We may be reaching a point where we are seeing real competitive tension between underwriters, partly down to pockets of new capacity and demanding growth targets. ESG continues to be a significant factor in the reduction of capacity for coal-powered generation assets with the Lloyd's directive to stop writing new coal-fired power plants from 2022.
- 2020 was a challenging year in the energy casualty sector, with key capacity withdrawing altogether or significantly reducing appetite. There is some positive news for 2021, as we are seeing rates stabilise.
- The renewable energy market has started the year with greater stability than 12 months ago. Rate increases at the start of 2021 are typically in the range of 10%–25%. We have seen some new capacity in the offshore wind sector as insurers look to increase their exposure to the green energy sector.
- In these tougher market conditions, the mutual OIL continues to add new members and is now up to 62. OIL's financial results have outperformed the commercial market over the last 10 years, and long-standing members are receiving annual dividends (to the value of about 50% of premiums 2014–2021). OIL are undertaking a strategic review which could result in an increased limit (from \$400 million), and a more tailored product for the new and expanding renewables sector.

# UPSTREAM

- In the first half of 2021, we have seen rate rises between 2% and 10% on average for upstream business, however this is dependent on loss record and profile. It is often more complicated than a blanket rate rise across an account; rather sections such as LOPI and control of well are being peeled back and scrutinised, and will be the reason for overall policy rises. The upper end of these rate changes (10%) have been seen mostly on business with smaller premium levels (sub USD 1 million) and in certain niche areas of the upstream book of business, such as onshore contractors and saltwater disposal.
- Notwithstanding the above, there still seems to be excess capacity for many upstream accounts, especially for business that is larger in scale and with attractive loss records. Whilst rate momentum has continued into Q2 2021, we are seeing this slow to low single-digit rate increases. Where market competition can be established and placements are able to be remarketed, we are seeing the first examples of reductions.
- Rates have increased on construction business by around 10%–15% along with deductibles, and large projects continue to be challenging, with limited appetite to offer subsea elements. There have been a number of pipeline/subsea losses around the globe which has seen some more underwriters stop writing this class of business within the construction all risk (CAR) portfolio. Very good underwriting information around the contractor is needed to place subsea risks currently.
- Across the upstream sector, there seems to be a minimum premium issue within the market; more often underwriters are imposing minimum premium limits on small business or introducing artificial rate rises. Mostly we are seeing this up to \$50,000, however there is possibility as the year develops that this could be anything up to \$100,000, something to watch for as we go through the year.
- The ESG movement within Lloyd's is growing and poses a potential problem for underwriters, as this could isolate risk appetite.

## ▶ U.S. Market Summary

Bankruptcies hit the highest levels since 2016.

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## ▶ Canada Market Summary

The upstream market remains a challenge following recent hardening market trends.

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## ▶ Australia Market Summary

Dependence on Singapore and London markets remains constant.



## U.S. UPSTREAM

According to Reuters, bankruptcies in Q1 2021 by North American exploration and production (E&P) companies hit their highest levels since Q1 2016. This was a direct result of companies having difficulty recovering from the 2020 crash in commodity prices. As 2020 closed out, the U.S. rig count was approximately 320, which was over 59% fewer than the same time in 2019. As of April 16, 2021, the count has slowly but steadily increased from year-end 2020 to 439, representing a less significant drop from the same time a year ago.

The natural attrition of exposure coupled with the poor historical performance in the sector is leading to enhanced competition for financially stable companies.

## CANADA UPSTREAM

The upstream sector remains a challenge, following hardening market trends in recent years. Until recently, capacity in the upstream market for operators extra expense (OEE) in Canada was essentially nonexistent, but we have seen two new entrants in this space offering some alternatives to the London market for this product. Primary liability capacity has dwindled to only a handful of insurers, as the frequency and severity of pipeline losses in recent years has forced others out of the market. In contrast, capacity and appetite for upstream property has remained strong in Canada, with new players coming into the space in 2019 and 2020, but for the time being, rating out of London remains more competitive.

Recent changes to federal legislation now require companies with federally regulated pipelines to carry extraordinarily high liability limits making these placements difficult and very expensive, often requiring most or all of the available capacity in Canada and London to complete them.

A number of economic and geopolitical factors have made access to investment capital more difficult for companies focused on upstream operations in Canada. This has resulted in a number of mergers and acquisitions within the space, and has reduced the overall available market share for competing brokers.

## AUSTRALIA UPSTREAM

The upstream market in Australia has always remained limited. Whilst there are companies who offer their stamps out of Australia for internal purposes, there are truly only a few insurers offering upstream property and OEE capacity in Australia.

The Australian upstream sector therefore continues to rely on the Singapore and London markets, both of which have been significantly impacted by internationally mandated travel restrictions.

Fortunately, Gallagher's Energy team maintains a strong, long-lasting relationship with both the London and Singapore markets, which allows us to maintain excellent levels of client service for our clients throughout 2021 and beyond.

Despite very few losses, the casualty upstream market has seen significant change. We have moved from an Australian market which could offer up to USD 350 million in capacity to one which now at best offers USD 210 million.

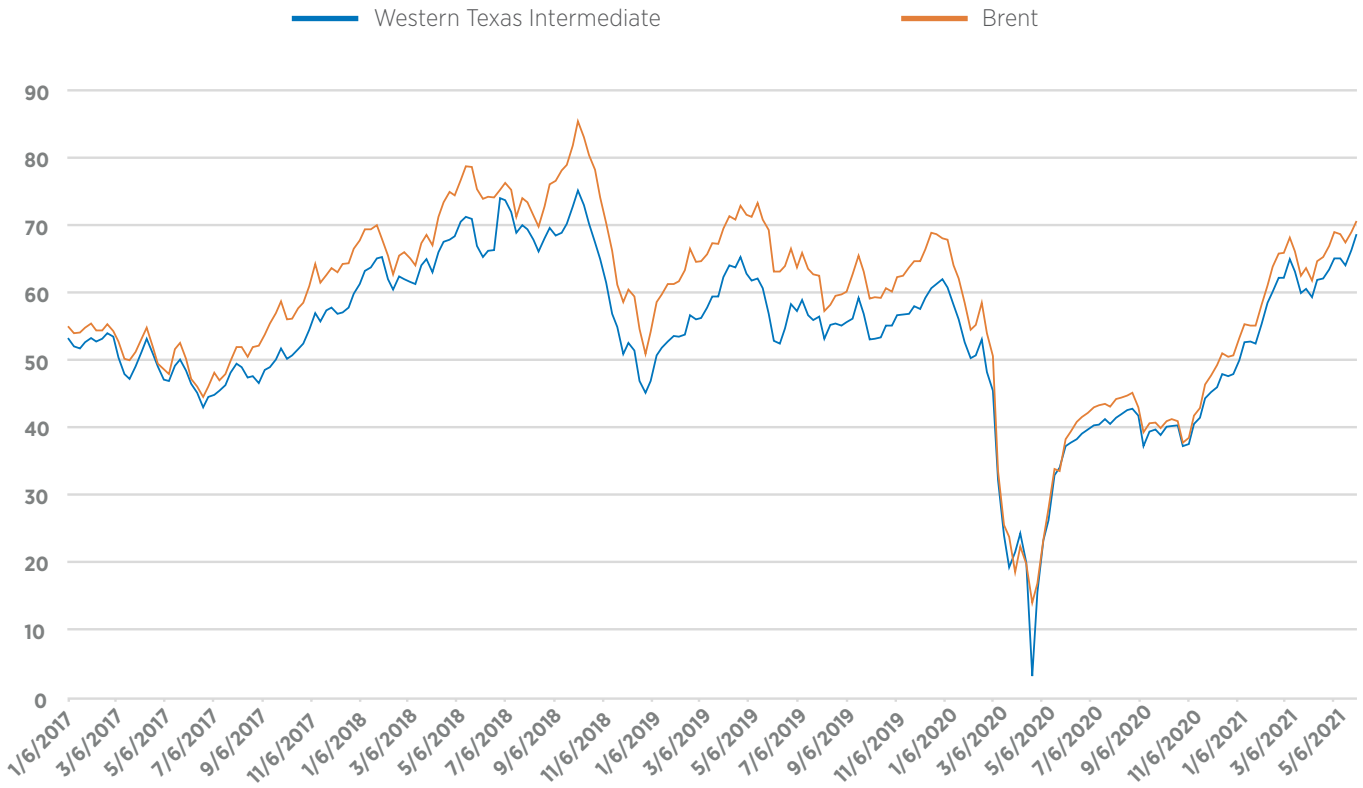
The only insurer we have lost locally is Zurich, who has moved all underwriting back to London. As a result, we are seeing a reduction in capacity being offered by the likes of AIG, Munich Re, Chubb and Berkshire Hathaway.

Insurers are also seeking to review ratings, with some now insisting on rate increases in the multiples to what they had previously been offering.

This combination of reduction in capacity, limited primary insurers and rating increases results in the need for brokers to strategically and methodically approach insurers to receive favourable terms.

# OIL PRICE TREND 5 YEARS TO JUNE 2021

## Oil Prices—Weekly

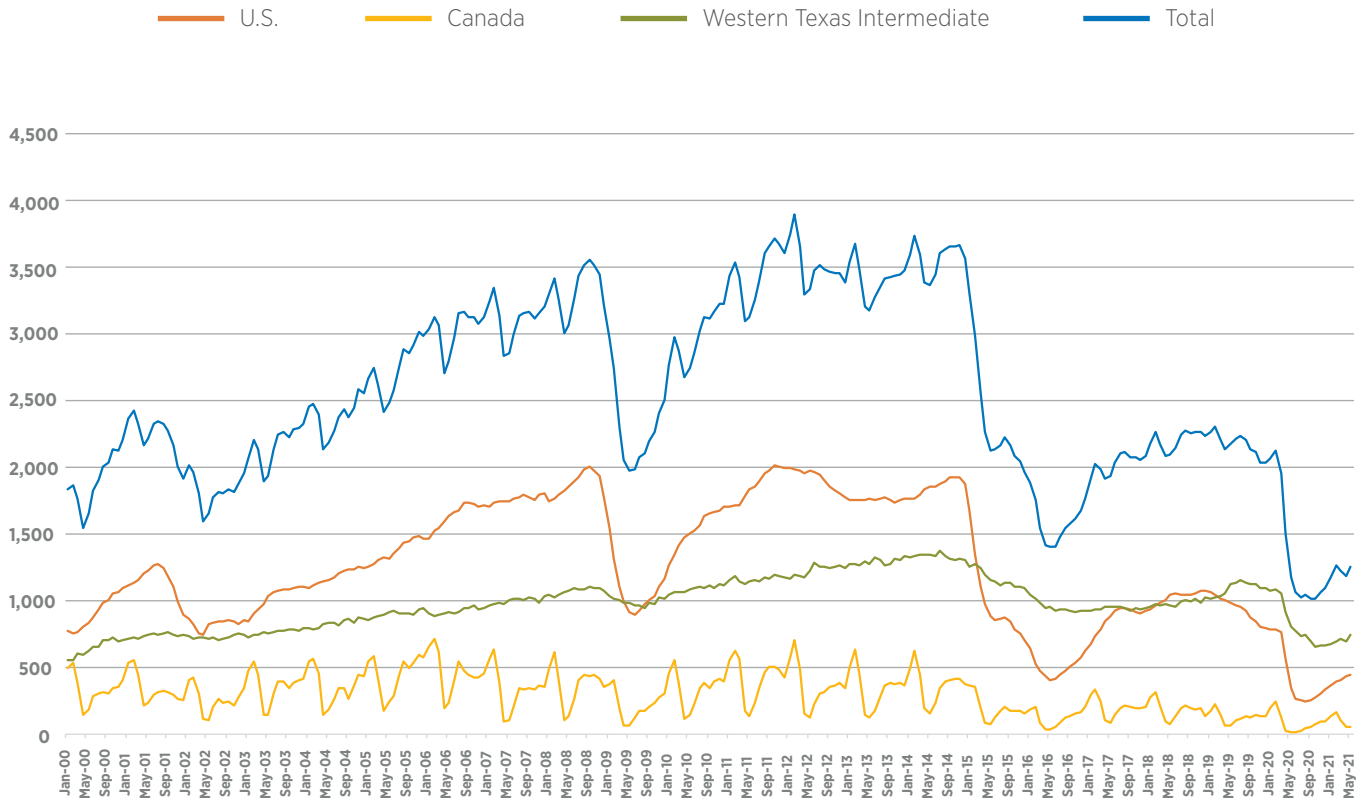


Benchmark oil prices currently \$60 per barrel

Source: <https://fred.stlouisfed.org/tags/series?t=oil>

# MONTHLY RIG COUNTS (TO MAY 2021)

Monthly Rig Counts (Land and Offshore, All Assets)



Total global rig count 1,100 (down 950 in 2020)

Source: <https://rigcount.bakerhughes.com/intl-rig-count>

# MIDSTREAM

- At the half-year mark, the market remains in its hardening phase with rate rises in the midstream sector, however, as predicted in our last brief, the market stance is softening and clients with clean business can now expect to be quoted circa +10%. The London downstream and domestic markets continue to harden at a faster pace, so the Alesco Midstream Facility remains competitive by contrast.
- The midstream sector continues to see the imposition of minimum premiums, though the demand by the market seems to have stabilised at between USD 50,000 and USD 75,000 for this sector of the business, and at the time of writing there aren't any signs of a further hardening of this stance.
- The unusually cold weather in the early part of the year so far hasn't translated into a large number of claims in the midstream space, so the most prevalent losses still remain gas plant fires and compressor issues, with resultant BI the major cause of loss to the market.
- The downstream market, where midstream has traditionally been purchased, continues to harden at a significant rate following poor book performance in that sector, and the pricing delta between the upstream and downstream markets continues to widen despite the year-on-year rises.
- Capacity remains static at the half-year point, with signs of some new entrants to the market potentially to come later in the year.
- High-profile midstream loss in the cyber sector in North America is likely to cause clients to rethink their cyber risk transfer, and the Alesco midstream team is actively engaging with the market to bring a satisfactory product to the table for the cover clients.

## ▶ U.S. Market Summary

Bankruptcies hit the highest levels since 2016.

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## ▶ Canada Market Summary

Alesco Midstream Facility continues to provide valuable capacity to Canadian midstream companies.

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## ▶ Australia Market Summary

The diversification of some majors is seeing opportunity for mid-tier companies to acquire more mature assets.



# DOWNSTREAM

- As we move towards the end of Q2 2021, the rate rises which the downstream market has undergone over the last 18–24 months are beginning to plateau, and we believe we may be close to reaching the crest of the hard market cycle.
- Whilst we are still not at the stage of seeing rate reductions, for those insureds with good loss records and that can provide quality engineering for their risk, we are now looking at +10%–15% rate rises as opposed to rises upwards of +20%–30%, which had been witnessed earlier in the year.
- Whilst underwriter discipline has largely remained intact, we are starting to see a move away from reduced capacity deployment. Nevertheless, since we have not seen a large influx of new capacity, there has not been a marked change in the supply vs. demand balance. That's not to say there have been no new players entering the marketplace, and the emergence of Guideone amongst others is a welcome addition.
- Despite this, we estimate capacity to remain fairly constant at approximately USD 4 billion, but with the insureds with a policy limit beyond USD 1.5 billion are faced with a challenge to complete a placement at a cost which is not considered to be too prohibitive. For risks in CAT-exposed areas, the access to competitively priced capacity is even more challenging.
- The pressure clients are experiencing on pricing and the withdrawal of capacity and, in some cases, reduced capacity deployment has led to more programmes reintroducing a layered structure (when they have been placed wholly quota share for many years). This approach, which has had a legacy of typically being done out of necessity due to lack of commercial QS capacity, can often bring additional capacity and competition where and when it is needed.

## ▶ U.S. Market Summary

Reported losses in 2021 continue to put upward pressure on rates.

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## ▶ Canada Market Summary

ESG dynamic emerging in oil sands marketplace.

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## ▶ Australia Market Summary

Fire and windstorms are leading the major losses in the sector.





## CANADA DOWNSTREAM

The downstream market in Canada remains intact, and largely mirrors what has been happening in the London and international markets. Terms and conditions are hard and capacity is being restricted. This year continues to see increased rating, but somewhat muted when compared to 2020. As licensed capacity reduces, clients are relying more heavily on unlicensed capacity, which does have potential tax implications. Nontraditional risk transfer through mutual insurers and captives is being explored by many in the marketplace.

A unique dynamic in the Canadian marketplace is oil sands exposures. Certain insurers (Munich Re, Swiss Re, Zurich, etc.) who were cornerstone markets for commercial market placements are withdrawing their capacity, forcing clients to look for capacity replacement and often new leaders. More markets are following suit, including Lloyd's. Capacity shortages are leading to program limits being reduced. Oil sands operators are spending considerable time and energy educating insurers on the industry's extensive ESG initiatives. Additionally, there is a feeling of frustration amongst Canadian oil sands clients that their ESG initiatives are not being measured objectively against other jurisdictions in the world.

## AUSTRALIA DOWNSTREAM

The downstream sector has also seen the market in Australia harden to the point where risks are either now being shown to London for lead alternatives or need to be completed in the international insurance market. Specific factors such as fire and windstorms are leading the major losses. We are also seeing a desired removal from prototypical technology as a result of an increase in frequency of these natural disasters across the country.

Additionally, more nontraditional markets, including mutuals who are able to offer significant capacity, are being considered as alternative routes of placement within Australia.

# POWER AND UTILITIES

- COVID-19 still remains a challenge. At the current time, the provision of up-to-date risk engineering information is a prerequisite for underwriters. With travel restrictions remaining largely in place, this continues to be an issue. Desktop reports combined with more direct interface between client and underwriter has proved to be helpful in many circumstances, however in certain geographical areas, this is proving to be challenging. As a market, we continue to navigate our way through this situation but watch with interest for any relaxation in travel restrictions going into Q3/Q4.
- Markets are continuing to underwrite with caution. Rates are still rising albeit perhaps a little slower, and the market is also showing a slightly greater appetite for clean/good quality business. General terms and conditions may now have seen a cycle of adjustment, so in many cases no major changes are being seen in this respect for clean business. There is still a high level of underwriting discipline, but hopefully we are getting to a point where there may be the possibility of introducing some competitive tension between markets. This may be further encouraged by the recent emergence of pockets of new capacity and increased growth targets in certain areas. We are still encouraging our clients to have an early engagement with underwriters and provide as much comprehensive/updated risk information as possible.
- The focus on coal remains an ongoing situation and one we continue to monitor closely. This is a high-profile issue, particularly with the Lloyd's directive to stop writing schedules including coal-fired power plants from 2022. This is a stance not just exclusive to Lloyd's, with the reduction in available capacity impacting both pricing and limits purchased. A recent high-profile loss at a coal-fired plant in Australia is only serving to bring this into further focus.

## ▶ U.S. Market Summary

After two years of significant rate increases, the level of rate increases in 2021 has shown signs of moderating.

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## ▶ Canada Market Summary

Consistent loss making has led to a number of insurers exiting this class of business.

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## ▶ Australia Market Summary

Whilst domestic capacity remains, current market conditions require a more strategic approach and longer lead times to renewal.



## U.S. POWER AND UTILITIES

### Property

The historical loss history within these subsegments of energy has been poor over the last several years. For that reason, underwriters are seeking an increase of 20% to 25% or more in rate for accounts not exposed to natural catastrophe risks and without adverse loss experience. For accounts with adverse loss history or those in high-hazard natural catastrophe zones, rate increases can be 25% to 50% or more.

### General Liability and Umbrella/Excess Liability

While liability insurance rates are firming within the energy sector, primary general liability rates are increasing at a slower rate than umbrella/excess liability coverage. In many instances, year-over-year rate changes for general liability remain in the middle to upper single digits. In contrast, umbrella/excess liability rates are increasing by 15% to 25% or more. The increase in umbrella/excess rates is driven in part by carriers restricting their capacity and reducing their renewal limits on any given account. As a result, markets are taking advantage of opportunistic pricing, as it is taking more insurance carriers and more premium to replace the lost capacity.



## CANADA POWER AND UTILITIES

Consistent loss making has led to a number of insurers exiting this class of business. Resultant reductions in capacity deployed on any one risk coupled with the uncertainty surrounding the pandemic has increased fragility and made the market more challenging than we've seen in many years. On the property side, insurers are pushing premium increases in the 20% to 30% range for clean accounts. They are also increasing deductibles and/or reducing coverage, as they look to return to profitability.

With respect to liability, a number of markets have reduced or withdrawn wildfire capacity, regardless of attachment, meaning existing limits can be difficult to replicate with premiums for the exposure up substantially. Well over \$200 million capacity has been withdrawn, and the capacity that remains is much more costly with much higher minimum premiums per million. Many insureds are either forced or voluntarily deciding to reduce limits as a result. Large blocks of capacity that were once the cornerstone of towers have all but vanished. Those markets that were once deploying \$25 million-plus are typically now offering only \$5 million to \$10 million, meaning it could take 20–30 markets to complete large limit towers, making it very difficult to create competition.

To help keep prices in check, differential pricing between insurers on the same layers has become common—and the differentials are in many multiples from lowest to highest price in some instances. The use of unlicensed/non-admitted insurers (and the associated tax consequences) has also increased in order to try complete placements.

In certain jurisdictions like California, wildfire coverage has become all but uninsurable. We have seen instances where large utilities with losses (PG&E, SoCal Edison) are faced with paying nearly dollar for dollar (premium for limit), retaining large deductibles (\$50 million-plus) and/or having to coinsure material portions of their tower (~10%).

The situation is unlikely to get better in the near term, as additional markets are signaling that they will not be able to renew programs or will have to offer reduced capacity with the placements that come up in 2022.

## AUSTRALIA POWER AND UTILITIES

The power and utilities sector in Australia has been impacted in recent years by various natural disasters, including bushfire, windstorm and flooding. As a result, the market has shown a view to hardening, offering more restricted cover and an increase in rating.

Market approach needs to be more strategic as a sector, which could once be accommodated in the domestic insurance market, and now needs to be accommodated in the international insurance market for both lead and/or supporting capacity.



# RENEWABLES

- The renewable energy market remains stabilised compared to the 2020 market correction.
- Renewals are seeing some 10% to 25% increases in rates and levelling of deductibles.
- There's a greater emphasis on equipment warranty status, technology manufacture and O&M scope than previous years as insurers become more familiar with their book performances.
- The increase in insurers' available capacity in terms of number of insurers in renewable energy has offset/compensated for the change in approach from some leads dropping from 100% to 50% lead lines.

## ► U.S. Market Summary

Rate increases of 10%-20% or more are commonplace in the current market.

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## ► Canada Market Summary

Insurer hot buttons revolve around natural catastrophes, extreme weather, remote locations, changing climate, warranty provisions and longevity of contractors/manufacturers, quality of product/workmanship with the rapid expansion of renewables, and emergence/growth of associated contractors and manufacturers.

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## ► Australia Market Summary

As the industry progresses to more sustainable technology, so will the market continue to evolve. With a strong focus on ESG, the Australian renewable market is continuing to expand with investment in a number of new projects.





## U.S. RENEWABLES

### Property

In addition to rate increases, markets are reducing their capacity on individual programs, and many insurers are no longer willing to write 100% of a single asset or program. This has an overall impact on pricing volatility within placements. The market is also imposing sublimits and higher deductibles for nontraditional natural catastrophe perils including hail, tornado and convective storms.

### General Liability and Umbrella/Excess Liability

The casualty marketplace for renewable energy risks generally remains quite competitive relative to other lines of coverage throughout the energy sector. Rate increases in the low single digits are achievable for accounts with favorable loss experience. Within the sector, utility scale ground mount solar installations will often achieve more favorable rates as compared to residential rooftop or commercial and industrial rooftop installations.

## CANADA RENEWABLES

Insurers have experienced adverse underwriting results for five of the last six years, driven by both catastrophe and attritional losses. As expected, this has resulted in capacity restrictions in the market with tightening coverage conditions. Catastrophe sublimits have been introduced for hail and convective storms, as have series loss clauses and micro-cracking exclusions on solar capacity. There has also been material increases in deductibles and waiting periods on all asset classes, particularly aging assets. Insurer hot buttons revolve around natural catastrophes, extreme weather, remote locations, changing climate, warranty provisions and longevity of contractors/manufacturers, quality of product/workmanship with the rapid expansion of renewables, and emergence/growth of associated contractors and manufacturers. In the current state of the market, results should be focused on preserving coverage and capacity, and less on price advantages.



## AUSTRALIA RENEWABLES

The past few years has seen a significant expansion within the renewables sector, which is not increasingly being backed by major E&P companies diversifying towards decarbonisation and support from the Australian government. Whilst we continue to see new projects being developed in the more traditional forms of renewable energy, such as solar and wind, across the country we are also seeing investment from governments and major E&P companies into newer technology including hydrogen and carbon capture, both of which were largely discussed during the recent APPEA conference.

The domestic property markets are well placed for both project and operational insurances for the renewable sector, however what is being seen is that pricing differentiator between the domestic and international markets is limited. Further, the domestic market presents a gap in project values between those in the AUD 10 million and AUD 20 million range, with some insurers suggesting it is too large and others stating they are too small to fit into their underwriting guidelines.

The domestic casualty market however remains robust towards renewables.



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