

CONSTRUCTION INDUSTRY

CONSTRUCTION INDUSTRY TRENDS TO WATCH - 2023

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Market Outlook – Construction

Key Market Trends

Pricing and Labor Challenges Continue

- Skilled labor and cost volatility continue to plague construction contractors of all sectors in all markets. Supply chain disruptions are further exacerbating the issue. The infrastructure legislation may put additional pressure on labor and materials challenges for construction firms in 2023 if supply chains have not recovered

Inflation

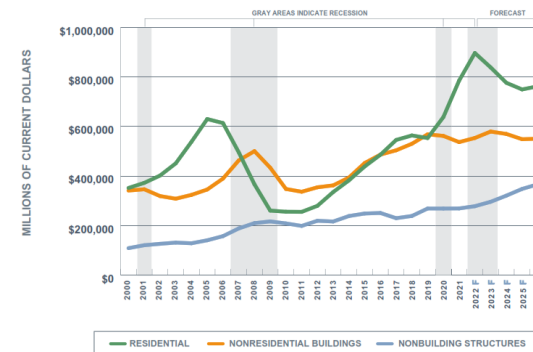
- Moody's Analytics reported in June that inflation rose to 8.6% on an annual basis but noted there were indicators that "global supply-side inflation pressure is peaking in some areas." The Bureau of Labor Statistics says inflation dipped to 8.5% in July after peaking at 9.1% in June.

Construction Confidence

- According to FMI's latest market outlook, the latest Nonresidential Construction Index (NRCI) suggests difficulties heading into the third quarter of 2022, at 45.2, down from 53.8 in the quarter prior. Sentiment this quarter was particularly weakened considering a slowdown in the overall economy. The index has fallen below the growth threshold of 50 for the first time since the 2020 pandemic recession and reflects declining engineering and construction opportunities ahead.

Architectural Billing Index (ABI)

Total Construction Put in Place Estimated for the U.S.



YoY % Change in Select Producer Price Index

Producer Price Index, August 2022

| | 1-Month % Change | 12-Month % Change | % Change Since Feb 2020 |
|---|------------------|-------------------|-------------------------|
| Inputs to Construction | -1.4% | 16.7% | 40.5% |
| Inputs to Nonresidential Construction | -1.4% | 16.3% | 40.8% |
| Plumbing Fixtures and Fittings | 0.4% | 10.9% | 15.7% |
| Fabricated Structural Metal Products | 0.0% | 17.7% | 54.8% |
| Iron and Steel | -5.1% | -5.7% | 78.2% |
| Steel Mill Products | -5.7% | -4.6% | 103.1% |
| Nonferrous Wire and Cable | 0.1% | 6.1% | 43.3% |
| Softwood Lumber | -3.1% | 14.8% | 43.3% |
| Concrete Products | 1.5% | 14.3% | 22.4% |
| Prepared Asphalt, Tar Roofing & Siding Products | 0.2% | 15.2% | 35.1% |
| Crude Petroleum | -5.3% | 38.8% | 89.6% |
| Natural Gas | 35.3% | 118.0% | 457.9% |
| Unprocessed Energy Materials | 13.5% | 75.0% | 185.2% |

Specialty Contractor Public Company Backlog Comparison

Construction Backlog Indicator

| | Aug. 2022 | July 2022 | Aug. 2021 | 1-Month Net Change | 12-Month Net Change |
|----------------------------|------------|------------|------------|--------------------|---------------------|
| Total | 8.7 | 8.7 | 7.7 | 0.0 | 1.0 |
| Industry | | | | | |
| Commercial & Institutional | 9.1 | 8.9 | 7.8 | 0.2 | 1.3 |
| Heavy Industrial | 7.4 | 6.6 | 5.4 | 0.8 | 2.0 |
| Infrastructure | 8.2 | 9.3 | 7.7 | -1.1 | 0.5 |
| Region | | | | | |
| Middle States | 7.2 | 7.5 | 7.4 | -0.3 | -0.2 |
| Northeast | 8.0 | 8.6 | 7.4 | -0.6 | 0.6 |
| South | 10.9 | 11.6 | 8.9 | -0.7 | 2.0 |
| West | 9.1 | 6.9 | 7.4 | 2.2 | 1.7 |
| Company Size | | | | | |
| <\$30 Million | 7.8 | 7.4 | 7.4 | 0.4 | 0.4 |
| \$30-\$50 Million | 10.0 | 10.8 | 7.5 | -0.8 | 2.5 |
| \$50-\$100 Million | 13.1 | 12.9 | 10.9 | 0.2 | 2.2 |
| >\$100 Million | 13.9 | 13.2 | 10.4 | 0.7 | 3.5 |

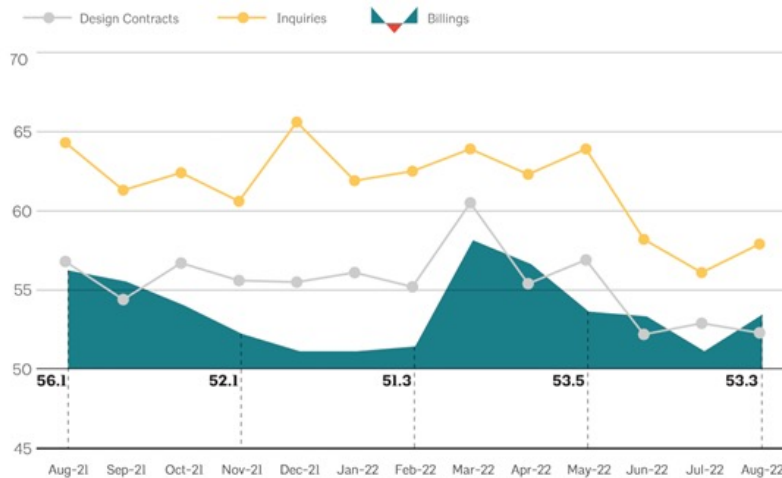
© Associated Builders and Contractors, Construction Backlog Indicator

Market Outlook – Construction

National

Billings continue to rise at architecture firms in August

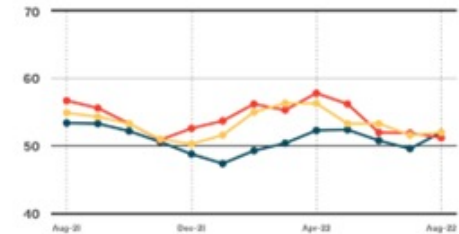
Graphs represent data from August 2021–August 2022.



Sector

Firms of all specializations still experiencing billings growth

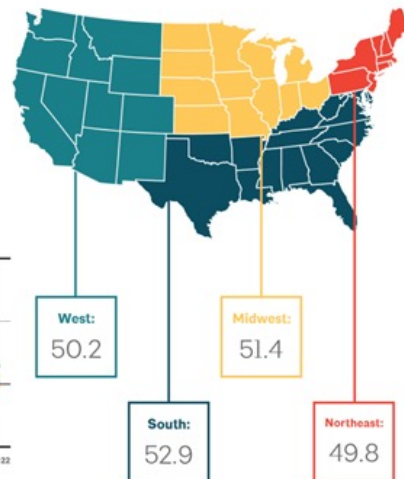
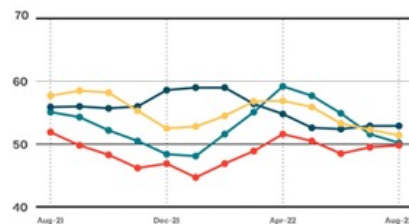
Graphs represent data from August 2021–August 2022 across the three sectors. 50 represents the diffusion center. A score of 50 equals no change from the previous month. Above 50 shows increase; Below 50 shows decrease. 3-month moving average.



Regional

Business conditions continue to improve in all regions of the country except the Northeast

Graphs represent data from August 2021–August 2022 across the four regions. 50 represents the diffusion center. A score of 50 equals no change from the previous month. Above 50 shows increase; Below 50 shows decrease. 3-month moving average.

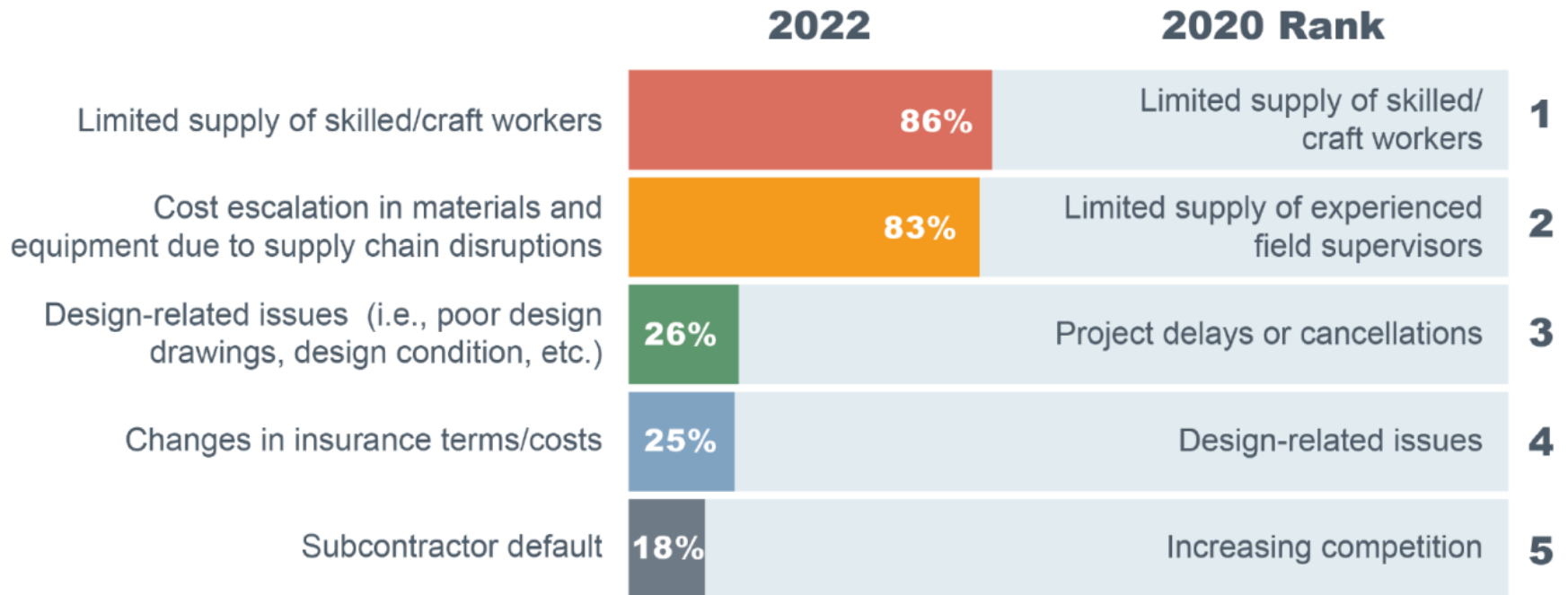


Key Takeaways:

- Overall, business conditions remained generally strong. The ABI score for the month is up from 51.0 in July to 53.3 in August 2022
- Billings continue to rise in the West, but fewer firms reported growth in August than in past. ABI slightly over 50

Top Construction Risk Management Risks

Top Risks Today



Top Risks Today

What is causing the most disruption on current projects?



89%
of respondents
experienced
project delays

Overall Insurance Market Trends for 2023

Trends:

- Lack of **skilled** labor
 - Has been #1 risk issue for contractors for more than five years and counting
- More **complex** contracting structures
 - Design-Build is no longer seen as an Alternative Delivery Method
 - Owners are allocating more risk to General Contractors which in turn pushing down additional risk to subtrades
 - Vertical integration and/or taking design in-house
- Supply chain **disruption**
- Material cost volatility
- Inflation and interest rates and impact on budgets
- Project delays
- Subcontractor **financial** health and wellness
- Increase in **frequency of severity of claims**
- Notable challenges:
 - Communicable disease exclusions
 - Large auto fleet exposures/street and road
 - Wildfire exposed risks
 - Umbrella/Excess liability
- **Cyber** risks increasing and availability of insurance

Adapting to a Volatile World

Top risk management tools used today

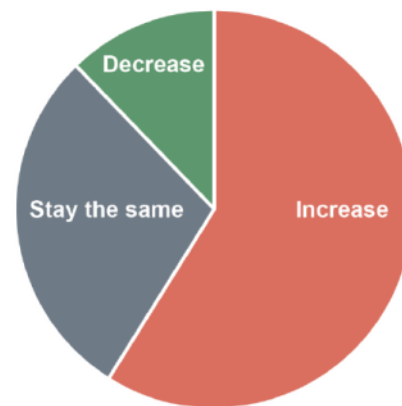


Juggling Project Risks

Top risk factors organizations consider when **determining to pursue** a project opportunity



The **average project size** compared to a year ago (\$ revenue volume)



Primary Casualty Market Observations Going into 2023

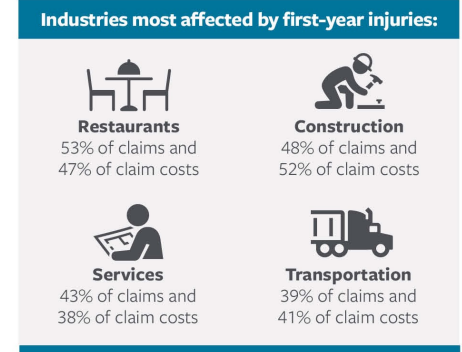
Observations:

- Abundant Carrier Capacity, but stricter underwriting guidelines on how that capacity is deployed
 - New InsureTech offerings available for adoption of tech platforms to gather data and greater project risk management
 - Exception is New York Construction which remains challenging and getting even more challenging
- Worker's Compensation was one bright spot for primary casualty, but losses are beginning to trend upward
- Auto Liability continues upward trend on losses
 - Increased use of Telematics
 - Cost to repair cars has increased
- Project Extensions
 - Reinsurance pressures causing large pricing increases
 - Extension challenges after a loss occurs
- Increase in captive (Both Single Parent and Group) interest or adoption

Potential Solutions:

- Early and often: Continuous open dialogues with markets (akin to surety and banking relationships) to go through operations on a more intentional and regular basis
- Develop longer term relationships with carriers – this is not a shopper's market
- Data Driven Submissions: It's no longer only about exposures!
- Alternative program structures and ideas
 - Start with Umbrella Liability/Excess Liability and work backwards to underlying requirements

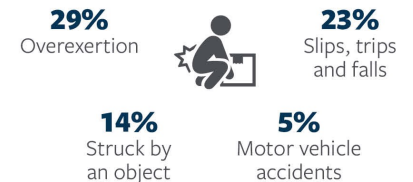
The Skilled Labor Shortage and Impact on Construction



Findings Across All Employees and Industries

The injuries analyzed kept workers across all industries out of work for **more than 17 million days**.

The most common causes of all injuries were:



The industries with the highest average of missed workdays were **construction (98)**, **transportation (88)** and **services (69)**.

Key Takeaways:

- Top 5 causes of injuries are costing the industry 11.3B a year.
- 48% of claims and 52% of claim costs involve construction workers employed for less than one-year
- Construction industry has average of 98 missed workdays per year

The Supply Chain and Impact on Construction



Note: The Risk Matrix is produced by the Risk and Insurance® editorial team. Liberty Mutual Insurance is the presenting sponsor and has no responsibility for the content.

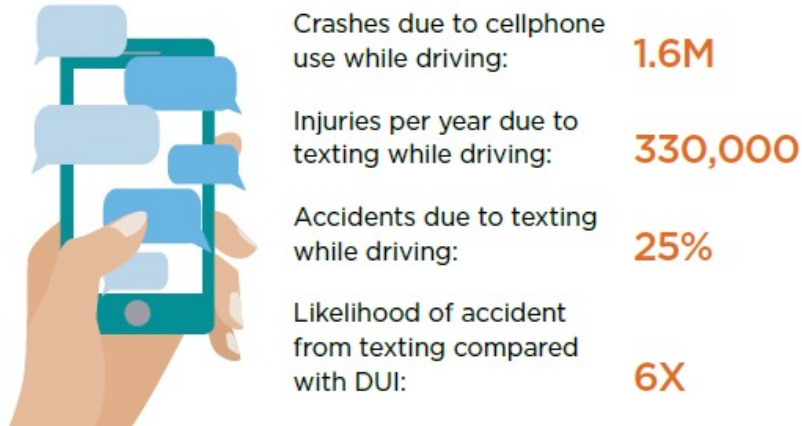
Factors Impacting Auto Liability

Risky behaviors. Drivers can be distracted by anything, but here are the main culprits and results.²

How much do risky behaviors increase the likelihood of crashes?



More facts on cellphone use while driving.



High-tech distractions. Safety technology is helpful, but can be very distracting without specific training.

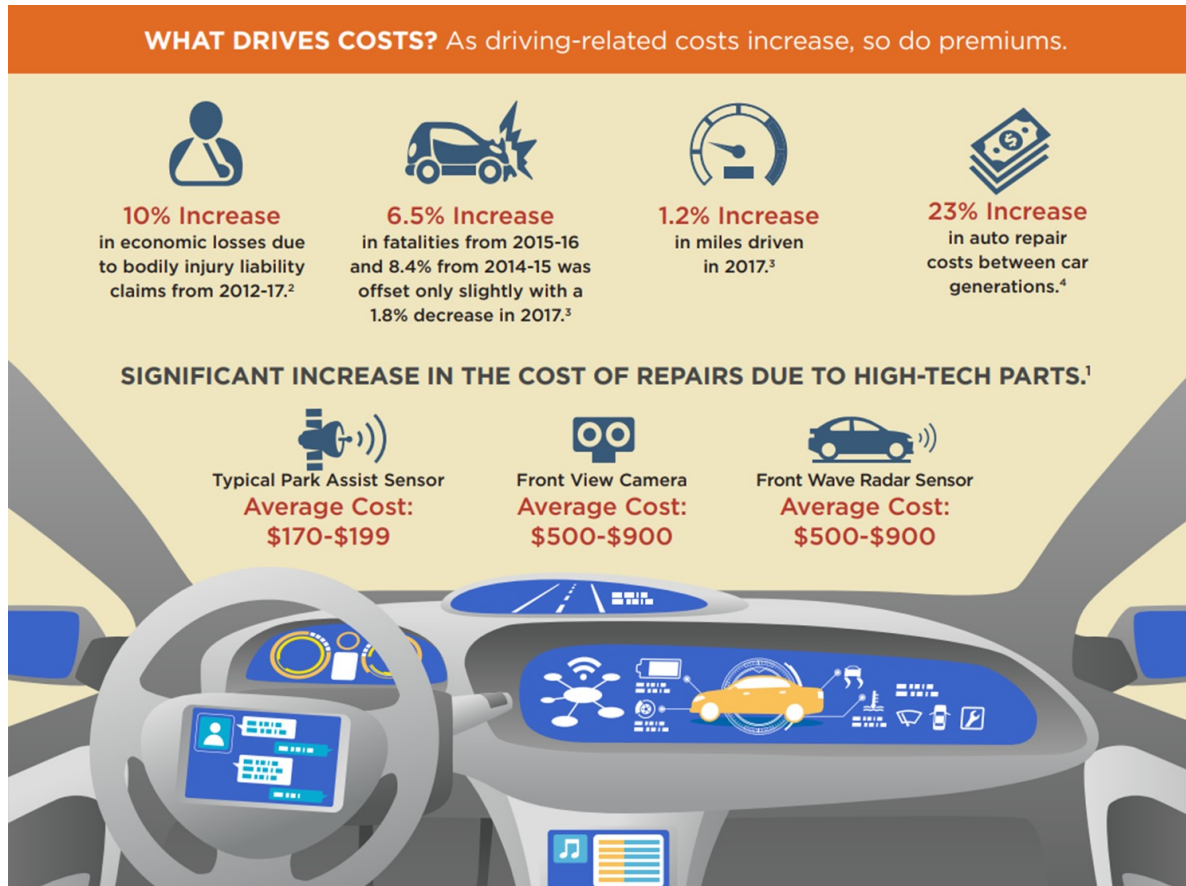


"... there is a tremendous need to improve customer understanding of these critical safety features."

– Daniel McGehee, University of Iowa Public Policy Center

*Source: Hartford Construction

Factors Impacting Auto Liability



*Source: Hartford Construction

Multitasking is hazardous to your health.

When you try to do two things at once, your brain is forced to shift focus.

See how the likelihood of a car accident increases while performing these common activities.

TEXTING
23X¹

Turn your phone off when you get into the car to avoid temptation.

REACHING
9X²

Find a safe place to pull over and pick up a dropped item or something behind you.

READING
4X²

Choose a voice activated GPS to avoid taking your eyes off the road.

GROOMING
3X²

First arrive safely, then check your hair or makeup.

EATING
2X³

Eat *before* you get into the car so you can focus on the road.

¹ Driver Distraction in Commercial Vehicle Operations, FMCSA, 2009
² <http://www.nhtsa.gov/About/NHTSA/Press+Releases/2006/100-Car+Naturalistic+Driving+Study>
³ Ergonomics in Design: The Quarterly of Human Factors Applications, October 2011



*Source: Travelers Construction | 13

State of the Umbrella/Excess Liability Market

Trends:

- Reductions in Coverage – See primary casualty slide
- Reductions in capacity (i.e., from \$25M to \$15M or \$15M to \$10M, etc.)
- Increased underlying limit requirements Auto/GL limits
- Pricing stabilization after overcorrection of last 18 months. There is still pricing pressure resulting from underlying results

Observations:

- Reduced underwriting authority
- Underwriting criteria is more stringent and in depth than before. It's no longer about providing underlying quotation and hope for the best. Hope is not a strategy!
- Extensions for project placements challenged
- Continued negative impact of Auto exposure

Potential Solutions:

- Develop relationships and a reputation with carriers to drive positive results – OFF CYCLE
- Submission Quality is paramount – It is all about **Data!** No longer exposure base only,
- Initiate early renewal cycles and proactive project specific efforts; renewal efforts should be year-round.
- Broader risk management strategies matter (subcontractor prequalification include safety and financial health and wellness, QA/QC embedded process, project controls)

State of the Builder's Risk Market

Trends:

- Shrinking u/w appetites for: frame construction, solar, civil/underground, tunnels, and bridges
- CAT peril sub-limits are getting squeezed while deductibles are increasing
- Reinsurance costs are driving implied average rate indices higher
- Infectious disease exclusions imposed by almost every Builder's Risk market on renewals or new placement
- CLT/Mass Timber – evolving, mixed u/w appetite
- Supply chain disruption and material cost volatility impacting the accurateness of project budgets and project schedules.

Observations:

- Specialty MGUs, and/or E&S markets are the only avenues for much of the “challenged” segments.
- Treaty reinsurance directly impacting u/w appetite
- Extensions on projects becoming more challenging with increased deductibles, rates and/or requirements (fire mitigation plans, water sensors, increased watchman patrol, etc.)

Potential Solutions:

- Engage underwriter(s) early; helping them understand the design and contractor means & methods, controls and monitoring is critical in achieving competitive capacity
- Consider investment in technology to assist with project site safety/water and fire mitigation of risk
- Explore alternatives for higher risk (frame) projects including quota share solution
- Wrap Around/Difference in Conditions (DIC) coverage for inadequate insurance purchased

State of the Contractor's Pollution and Professional Market

Trends:

- Product Stability
- A&E Market showing signs of hardening
- High Risk Exposures like frame and residential under more scrutiny
- Project professional market still limited
- Communicable disease exclusions being endorsed on renewals and new placements
- Reduced Capacity Deployment

Observations:

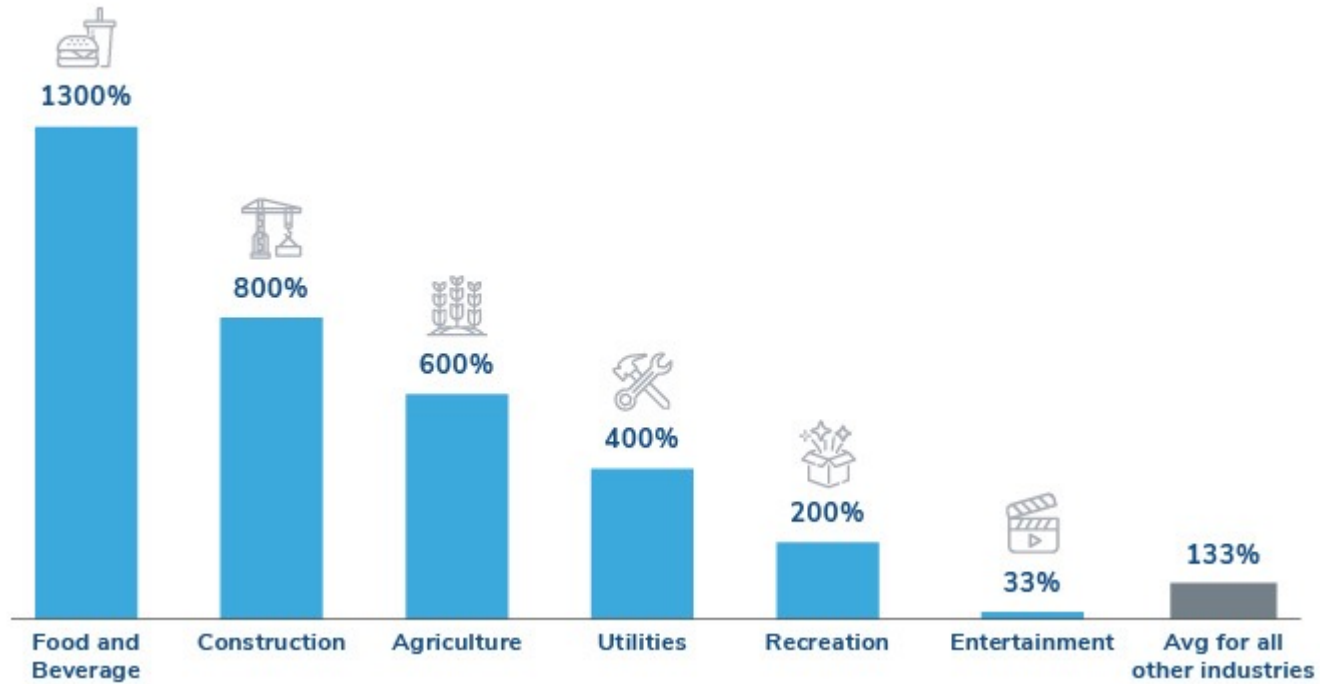
- Rate, Retention & Limit Stable
- Design Build Impact; Underwriters looking for more information on scope of work
- Residential, Wood Frame Sublimit Available

Potential Solutions:

- Engage underwriter(s) early; helping them understand the design and contractor means & methods, scope of work and controls in place.
- Seek alternative program structures to maximize capacity and coverage while achieving the most efficient cost structure (moving away from large layers potentially)

Cyber: Everyone is Impacted

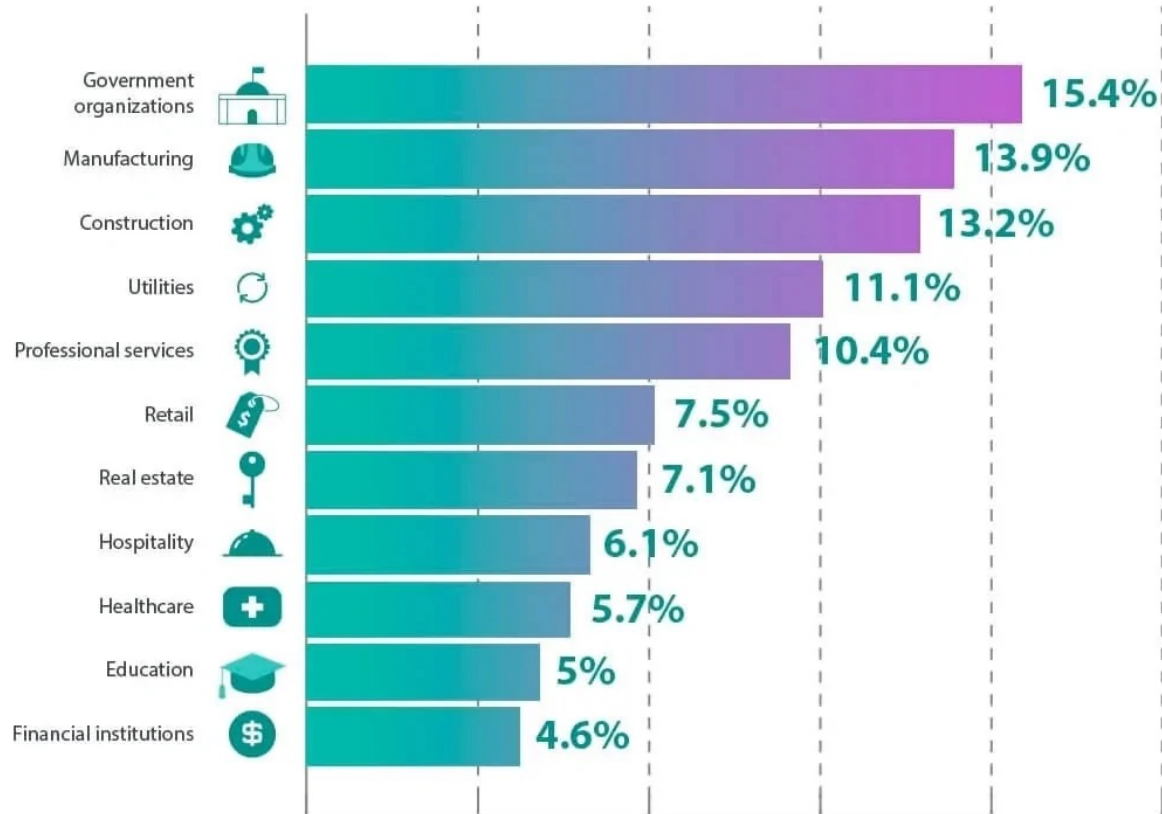
PERCENTAGE GROWTH IN 2020 DATA BREACHES COMPARED TO 2019



*Source: <https://www.kroll.com/en/insights/publications/cyber/data-breach-outlook-2021>

YoY Comparisons...Which Industries are Most at Risk?

INDUSTRIES IN NORTH AMERICA REPORTING RANSOM ATTACKS IN THE LAST YEAR



Percentage of all reported incidents caused by ransomware



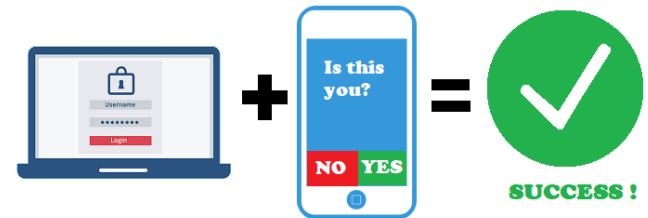
State of the Cyber Market

Trends:

- Technology and connected projects increasing to address labor shortage woes
 - Manage the fluidity of a workforce moving between work sites relying on laptops, tablets and smartphones (BYOD)
- Supply chain attacks on the rise
- Sharing sensitive data across multiple sites includes plans, blueprints, costs estimates, bids and employee records
 - Shift to remote work has left employees and employers more vulnerable to Cybercrime
- Business interruption is largest fear by employers
- Owners asking for more details on contractor and subcontractor cyber insurance and privacy procedures

Observations:

- Increased excess rates
- Aggregation Exposures (supply chain, specifically)
- Premium and SIR changes
- Additional underwriting requirements
 - Cyber hygiene really does matter!
 - You may be OK, but what about your subcontractors?



Potential Solutions:

- Cyber risk should be part of your overall enterprise risk management approach – not only an “IT Issue”
- Engage with cyber specific vendors on the front-end. Sourcing vendors after a loss
- Build a solution based on three core building blocks: Liability costs, Compliance/corrective costs, and Direct costs

Other Market Observations

- Environmental Social Governance (ESG)
- Employment Practice Liability and Other Executive Risks post the **#MeToo** movement
- Mental Health and Suicide among Contractors
- Commercial Contractors Expanding into Residential
- New Product Developments
 - Parametric and Pandemic Insurance Solutions
 - Project Loss Insurance as an alternative to Subcontractor Default Insurance (SDI)

The background of the slide is a blurred image of a construction site. In the foreground, a hand holds a tablet computer. Overlaid on the image are several white icons: a gear at the top, a globe with a person icon in the middle, a document with a checklist on the left, and a person working on a structure at the bottom. The text 'Q&A' is positioned in the upper right area of the slide.

Q&A

Thank you!