

HUB 2023

# Outlook.

# Private Equity



**Leaving no stone unturned  
in seeking higher profits.**



Risk & Insurance | Employee Benefits | Retirement & Private Wealth

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Setting the Scene

# Focusing on management — and risk management

Private equity will put more focus on long-term management of portfolio companies. With difficult credit markets and heightened competition, the emphasis is on greater professionalism and best-in-class management. Private equity is investing in its businesses and the people who run them.

**\$1.7T**

Global private equity deal value for the 18 months ending in June 2022.<sup>1</sup>

1. Bain & Company, "[Shifting Gears: Private Equity Report Midyear 2022](#)," July 18, 2022.

## What to Expect in 2023

PE firms and their holdings will face higher costs in 2023 for raw materials, staff and insurance premiums. Rising interest rates will hamper firms' ability to purchase companies on the front end and pressure exit prices on the back end. As a result, PE firms will focus on improving their portfolio companies' management to generate superior returns and keep their funding pipelines open.



# A greater focus on portfolio companies' bottom lines.

Several factors will weigh down PE profits in 2023: tighter credit, higher insurance premiums, surging interest rates, rising raw materials costs and the labor shortage.

With credit tight, primary market deals may decline in 2023. However, the secondary market grew exponentially in recent years. Assets under management quadrupled over the past decade and the compound annual growth rate has risen 20.2% since 2000, far surpassing that of the overall private equity market (12.9%) over the same period.<sup>2</sup>

Because higher interest rates could hamper deal-making, PE firms will generate more profit from their portfolio companies by managing costs and maximizing efficiencies. In the long run, investments in



people and processes will pay off through improved valuations and attractiveness to prospective buyers when it's time to sell.

PE firms will need to pay more attention to insurance costs, risk exposures and coverage. Insurance rates rose across the board in 2022 and are expected to rise in 2023, especially for certain lines, including catastrophe, general liability, umbrella and property.

We see opportunities to boost margins through leveraged insurance purchasing programs among portfolio companies, which not only can cut costs but can reduce losses and claims.

2. CAIS Group, "[The Evolution of the Private Equity Secondary Market](#)," September 7, 2022.



# “Benefits strategy” will become a reality for PE firms.

In 2023, private equity executives will examine an area they’ve haven’t emphasized in the past: benefits strategies at their portfolio companies. To meet growth targets, private equity executives need to invest in HR systems, processes and technology at the companies they acquire.<sup>3</sup>

For private equity firms and their portfolio companies that are experiencing worker shortages, professionalizing HR operations and rethinking benefits can increase profits and simply help companies stay fully staffed.

The biggest challenge for PE portfolios is the variety of industries, each with different benefits needs. Offering childcare and eldercare benefits are highly desired in healthcare and hospitality, but less so in construction and transportation.

A personalized benefits strategy can address this dilemma. By using data analytics and on-the-ground HR expertise at individual operations, companies can tailor benefits to meet individual employee needs without increasing their benefits spend. Personalized benefits result in positive employee experiences, which engenders loyalty and increases engagement



3. Hunt Scanlon Media, “[The Evolving Role of HR in Private Equity](#),” March 23, 2022.



## Staying viable will mean more than obtaining R&W coverage.

The cost and availability of representations and warranties (R&W) insurance remains a major hurdle in keeping PE firms viable. But PE firms will face ongoing threats to their resiliency, such as rising interest rates, weather-related catastrophes and cybercrime.

In addition, supply-chain disruptions and staff shortages also will challenge PE executives and their portfolio companies.

Insurable events, like catastrophes, have become more frequent and damaging. Global losses from catastrophes totaled \$105 billion in 2021, with estimated insured losses reaching \$35 billion in the first half of 2022.<sup>4</sup> That doesn't include losses from hurricane season, including Hurricane Ian, which alone could total \$65 billion in damages.<sup>5</sup>

**\$105B**

global catastrophe losses in 2021

**\$65B**

estimated damages from Hurricane Ian in September 2022

Cyber insurance has been particularly fraught, with premium expected to increase as much as 40% in 2023, following similar hikes the last two years. Carriers will expect portfolio companies to conduct security audits, have two-factor verification, endpoint detection and response, and continuing cybersecurity training before being considered for cyber coverage.

Forward-thinking managers will leverage advanced data analytics to improve their risk management, ascertain acquisition viability and decide the correct amount of insurance coverages for portfolio companies.

4. Swiss Re Institute, "[Floods and storms drive global insured catastrophe losses of USD 38 billion in first half of 2022](#)," [Swiss Re Institute estimates](#)," August 2, 2022.
5. ABC News, "[Hurricane Ian could cause \\$65 billion in damage](#)," September 30, 2022.



## Non-traditional strategies will be rewarded over time.

If PE firms need to hold portfolio companies for longer periods than in the past, they must use that time to implement best-in-class management practices to build value.

With the challenges of securing investor funding, middle-market PE firms, in particular, will feel pressure to generate top-quartile profitability in order to raise sufficient capital in the future.

As a result, PE executives will strive to improve management, closely examine everything from accounting to technology operations and focus on securing top talent for long-term retention.

For many PE firms, this will represent a return to basics. While private equity firms have focused on short-term results to make portfolio companies attractive to sale — often through major cost-cutting measures — trying to “professionalize” operations points to the need for PE firms to play a greater role in managing their assets.

*Firms that professionalize operations will be rewarded with higher margins.*

To counter the increased rates and threats to long-term viability, private equity managers are embracing risk management strategies that can ease the insurance burden at their portfolio companies. They're examining all opportunities to maximize returns, and part of that will entail a management emphasis on taking a far more sophisticated approach to insurance.

For instance, we've seen forward-looking PE firms find creative ways to manage product liability exposure and cut costs. Other PE firms have explored benefits captives to maximize cost savings and improve benefits overall.



# Make a plan

HUB private equity specialists will work with you to develop a tailored strategy that will protect the bottom line, support your workforce and build resiliency for 2023. Here are some initial considerations:



## **Don't shy away from risk.**

As interest rates climb and deal volume falls, private equity firms need to be more mindful of their bottom line. Taking a higher deductible on any number of coverages can reduce premiums and improve experience rating. Ask your HUB broker about captive solutions, self-insurance and risk retention groups.



## **A (good) loss trend is your friend.**

Understand the root cause of large losses and explain to carriers your plan for preventing future losses. Develop a strategy with HUB to determine the best time and frequency to review alternative markets.



## **It's all about your people.**

As private equity pivots toward portfolio company retention, firms will place a greater emphasis on people management at their portfolio companies. They'll need to support employees' health, safety and wellbeing. Give them the ability to personalize their benefits without increasing costs. [HUB's QEX approach](#) will give you a competitive advantage.



## **Be transparent with your broker.**

With multiple businesses to manage, you'll have multiple risk issues. Let your broker know what changes you've made so there are no surprises at renewal. Review exposures and insurance needs at least 90 days prior to policy renewal, so your broker can identify the best options.



# Be Prepared

HUB International analyzes proprietary national survey data and interviews commercial insurance brokers and risk services consultants to create an annual rate outlook for financial institutions and private equity firms.

We expect rate increases for nearly all coverages in private equity, as carriers are experiencing high losses and expenses.

On the next page is HUB's 2023 rate outlook for several insurance coverages for financial institutions and private equity. This will help you discuss business' exposure with your insurance broker in advance of your next renewal.



# Financial Institutions and Private Equity Industry Rate Outlook – U.S.

Coverage	2023 Private Equity Rate Outlook	Insights
<b>Management Liability</b>	<b>For Portfolio Companies:</b> ↑ 5% to 10% Directors & Officers (varies by industry)	The D&O market specific to private equity portfolio companies will improve after several years of difficult market conditions. There is more competition and carriers have reduced the number of their restrictive classes, with better pricing for best-in-class risks. However, pricing for healthcare, education, energy, cryptocurrency and cannabis operations will remain difficult.
	↑ Flat to 10% Fiduciary Liability	
	↑ Flat to 10% Crime	Reflecting an uptick in claims for FMLA, biometric and privacy laws, and pay equity, the price of Employment Practices Liability (EPL) insurance will rise.
	↑ 5% to 20% or higher Employment Practices Liability	
<b>General Partner Liability</b>	↑ 5% to 10%	<p>The GPL market has experienced more than three years of steady rate increases. However, the 2023 outlook see stabilization, with rates rising 10% or less.</p> <p>Rates are expected to increase for private equity portfolio companies. The market is still determining how to price for minority growth equity, which is expected to drive rate increases as well.</p> <p>More favorable pricing exists for best-in-class risks. Underwriting considerations include the number of funds and assets under management; investment strategy; management pedigree; portfolio company board exposure; and investor base or investment structure.</p> <p>Large clients with larger strategies might see rate increases of 15% and above in 2023 and 2024.</p>
<b>Representation &amp; Warranty</b>	↓ 10% to 20%	After record deal volume in 2021, private equity acquisitions declined three consecutive quarters in 2022. However, many insurers increased capacity based on 2021, resulting in lower rates for R&W insurance. Interest rate hikes and inflation will continue to depress deal volume, lowering rates further.
<b>Cyber Liability</b>	↑ 20% to 40% or higher	Rates are easing for operations that have not had significant exposure changes or claims, and have proper cybersecurity controls. Operations lacking multi-factor authentication (MFA), endpoint detection and response (EDR), and offline backups will have difficult renewals.
<b>Workers' Compensation</b>	↑ Flat to 5%	Rates are relatively stable. However, it's important to adopt best practices for onboarding and training to keep accidents at bay, especially when it comes to less experienced staff. Rates remain relatively stable.

**NOTE:** *Rate* is typically defined as the amount of money necessary to cover losses, expenses, and provide an insurance company with a profit for a unit of exposure. *Exposure* refers to a business' or individual's susceptibility to various risks encountered daily. Carriers evaluate the level of risk an insured faces in calculating insurance premiums.

## HUB Private Equity

When you partner with us, you're at the center of a vast network of experts who will help you reach your goals. For more information on how to manage your insurance costs, reduce your risk and take care of your employees, talk to a HUB private equity insurance specialist.

**\$721M**

in commercial insurance  
premium brokered by HUB

**7,763**

private equity clients

**24,357**

insurance policies  
managed

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