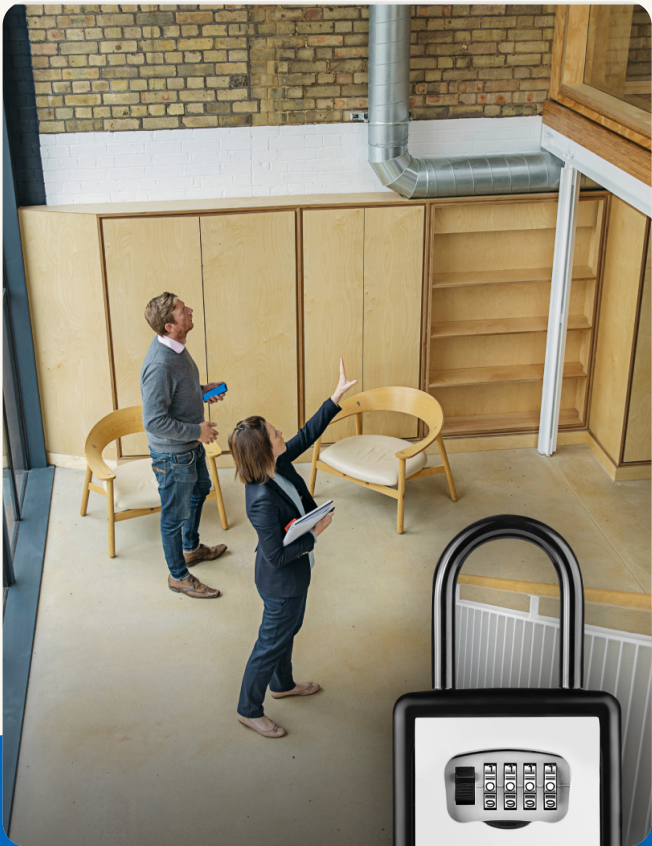


HUB 2023

Outlook.

Real Estate



Seeking stability in a market going sideways.



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Resiliency
Climate change

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Setting the Scene

Risk and costs will increase.

Higher interest rates and inflation will affect the cost of borrowing, construction, maintenance and insurance. At the same time, costlier natural disasters — Hurricane Ian being a harbinger — and remote work becoming permanent will transform how investors value their real estate holdings.

18.4%

The vacancy rate for office buildings in mid-2022.

Moody's Analytics, "[2022 Midyear Outlook: Multifamily and industrial flourish, office and retail muddle through](#)", August 2, 2022.

What to Expect in 2023

Inflation reached a 40-year high in 2022, driving up interest rates, which will remain high and possibly increase in 2023.¹ Rising construction costs, as well as more frequent and extensive property claims, will exacerbate market challenges and weaken profits. Real estate owners and operators who understand their risks and embrace creative market solutions will have better coverage options at lower costs.

1. Bloomberg, "[US Inflation Quickens to 40-Year High, Pressuring Fed and Biden](#)," June 10, 2022.



Real estate will see lower profits, with interest.

Several years of high rebuilding costs and outdated or inaccurate property valuations, rising crime, chronic inflation and high interest rates will continue to hurt real estate profits.

Climbing interest rates have made loans and refinancing more expensive; rates are likely to stay high and increase in 2023.² Real estate owners and managers will need to plan for further rate hikes and continued high inflation, which will make it more difficult for their commercial and residential lessors to make rent.

The shift to remote work will continue to pressure commercial real estate profits. The national vacancy rate for office buildings rose steadily throughout the first half of 2022,³ standing at 18.4% in the third quarter of 2022. Pension funds have pulled back on office building investments, with

Pension funds have reduced their holding in



private real estate holdings in offices falling 11% in 2021 compared with the three years prior. Holdings in the retail space fell 7% over the same period.⁴

These factors will make an already onerous insurance market even more difficult in 2023, with carriers pulling back on capacity and significantly increasing insurance rates, further squeezing profits.

2. Wall Street Journal, "[Fed Raises Interest Rates by 0.75 Percentage Point for Third Straight Meeting.](#)" September 21, 2022.
3. Moody's Analytics, "[2022 Midyear Outlook: Multifamily and industrial flourish, office and retail muddle through.](#)" August 2, 2022.
4. Wall Street Journal, "[Pension Funds Are Selling Their Office Buildings.](#)" August 25, 2022.



Shrinking workforce, shrinking revenue.

Real estate companies are struggling to find capable employees. In today's era of remote work, half of commercial real estate companies say geographic challenges have become the top issue in hiring.⁵

The labor shortage also is affecting real estate indirectly. Construction companies are facing delays because they can't find enough workers. Most real estate operations hire vendors to handle maintenance, security and cleaning services, but they're having trouble with staffing as well.

Those vendors and construction companies are raising wages to attract and retain workers, with costs likely to be passed on to real estate owners and operators.

Just as troubling: The labor shortage is affecting renters' ability to hire workers. In 2020, lessors were going out of business or not paying rent, but today they can't get enough workers to stay viable or expand, resulting in less rental income for owners.⁶

Although real estate owners and operators can do little for the overall labor shortage, they can improve their own recruiting and retention through personalized benefits based on data analytics. Ultimately, this will create [quality employee experiences \(QEX\)](#) that improve employee engagement and engenders workforce loyalty.



5. Northspire, "[Commercial Real Estate's Most Critical Issue: A Labor Shortage](#)," September 1, 2022.
6. CRE, "[Labor Shortage Strain: Where Have All the Workers Gone?](#)" August 17, 2022.



Real estate owners will face stubborn challenges to resilience.

In addition to threats from financial and economic conditions, real estate owners and operators will face a difficult insurance market.

Commercial property-casualty insurance is projected to increase as much as 20% in most geographies. The rise will be due to carriers' increased scrutiny of insurance-to-value, rising construction costs and supply chain disruptions. Expect coverage for habitational and multi-family properties to rise about the same amount.

There are bright spots for top properties with lower risk profiles. For instance, underwriters are still offering coverage for fire-resistant Class A high-rise office buildings. Best-in-class property risks will find good coverage at a good rate.

Claims litigation also threatens real estate owners as the number of so-called nuclear verdicts (awards of \$10 million or more) will increase.⁷ These lawsuits, such as one that awarded \$43 million because of a crime that happened in the parking lot of



a drugstore,⁸ may drive carriers away from insuring sectors such as older multi-family properties or properties in high-crime areas.

When coverage is available, it will be significantly less than what is needed to adequately protect the property owner, or board of directors, in the event of a lawsuit.

Carriers are more likely to offer coverage for properties where the owners or operators are actively trying to prevent damage or liability claims. Underwriters will target best-in-class properties and will require current building valuations before even considering risks.

In order to get preferable rates, real estate owners and operators will need to have detailed data on renovations and maintenance, such as new roofing or plumbing. Otherwise, insurers will assume that buildings have no renovations and will price insurance accordingly.

7. Travelers Institute, [The Exponential Rise of Nuclear Verdicts](#), June 29, 2022.

8. Insurance Journal, ["Insurers for High Crime Areas on Notice after Georgia Court Affirms \\$43M Verdict,"](#) November 12, 2021.



Weather disasters will affect commercial real estate insurance.

Catastrophes will weigh heavily on insurers' minds, with global catastrophe losses in 2021 totaling \$105 billion and estimated insured losses reaching \$35 billion in the first half of 2022 alone. And that does not account for Hurricane Ian, which slammed into Florida's southwest coast in September 2022 and caused an estimated \$42 billion to \$57 billion of damage from wind, storm surges and inland flooding.

Coverage for catastrophic perils will rise 20% to 50% in low-hazard areas, while in high-hazard areas, rates could triple. Investing in stronger building materials that can withstand geographical hazards and ensuring properties are consistently and properly maintained will be crucial to reduce risks.

If a property does suffer a loss, underwriters are more likely to consider coverage if they have been rebuilt with proven construction materials to mitigate against future losses.

Parametric insurance also may be available in areas where property insurance capacity is scarce. Parametric policies pay out a set amount based on the magnitude of the event, even if there is no loss for the insured.



9. [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.](#)
10. [Business Insurance, "Hurricane Ian: Loss Tally Continues," October 4, 2022.](#)



Make a plan

HUB real estate 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:



Lean into risk.

Higher interest rates and increasing catastrophes have driven up risk for real estate owners and investors. A higher deductible reduces premiums and improves experience rating. Ask your HUB broker about what kind of deductible meets your risk profile and budget.



Make safety a tenet of the organization.

Nuclear verdicts against real estate companies are exploding. Make safety a tenet of the organization, with extra training and risk management practices for all properties. A little prevention can save you millions.



Analyze loss trends.

Understand the root causes of large losses and explain to carriers what you're doing to prevent future claims. Develop a strategy with HUB to determine the best time and frequency to review alternative markets.



Improve materials and construction.

Whether it's rebuilding or new construction, it's important to use materials and construction techniques that will minimize losses later on. Think hail resistant roofing and siding, fire-resistant building materials and automatic plumbing shut off controls. It will go a long way in lowering claims and premiums.



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 the Real Estate industry.

We expect rate increases for nearly all lines of coverage in Real Estate, as a result of carriers trying to account for high losses.

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



Real Estate Industry Rate Outlook – U.S.

Coverage	2023 Real Estate YOY Rate Guidance	Insights
Commercial Property	↑ 10% to 20%	<p>Increased underwriting scrutiny on insurance to value (ITV) and expected losses from Hurricane Ian are driving higher premiums for properties in areas with limited catastrophe exposure. Properties that are well maintained and have sound business continuity planning are getting first consideration. Risks requiring reinsurance will get the biggest rate increases.</p> <p>In areas subject to catastrophes, standard markets will provide terms for best-in-class properties with superior construction only.</p>
Habitational & Multifamily Property	↑ 20% to 50%	<p>Following years of hefty rate increases, expect modest increases for properties that are in geographies not typically exposed to catastrophes. Carriers lost additional capacity through treaty renewals for the fourth quarter of 2022 for policy year 2023, which will further pressure premiums and result in less coverage.</p>
Catastrophic Perils	<p>↑ 20% to 50% (low hazard zones/tiers)</p> <p>↑ 75% to 200% (high hazards zones/tiers)</p>	<p>Capacity is limited, particularly in high-hazard areas exposed to convective storms, floods, earthquakes and wildfires. Expect higher deductibles and retentions, coupled with reduced limits. Standard markets will only provide terms for best-in-class properties with superior construction; many insureds will have to rely on the non-standard E&S market or parametric coverage.</p>
General Liability	↑ 5%	<p>Due to increased litigation and nuclear verdicts, insureds are often purchasing a buffer layer to offset reduced capacity on the excess tower.</p>
Workers' Compensation	↔ Flat	<p>Heightened competition will lead to rates remaining flat in 2023.</p>
Umbrella / Excess Liability	↑ 20% or higher	<p>Premiums have risen over the last several years, largely due to increased litigation and nuclear verdicts. While rate increases will continue in 2023, additional market entrants should eventually help stabilize rates.</p>
Directors & Officers	↑ Flat to 5%	<p>D&O rates will be relatively flat for real estate-focused investors and publicly traded REITs. However, privately held REITs will see slight rate increases due to underwriting concerns over liquidity and valuations.</p>
Cyber Liability	↑ 20% to 40% or higher	<p>Rates are easing for real estate 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.</p>

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 Real Estate

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 real estate insurance specialist.

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