**JDA Real Estate Development Webinar**

**Focus on the Impact of Climate Change and the Changing Role of Insurance**

**Talking Points**

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The focus of my comments is the negative impact of climate change on the cost and availability of insurance coverage for governments, businesses and households. The role of insurance in real estate development is very clear to us all, however, it may be useful to consider some of the possible changes in the insurance market that could have a profound impact on the real estate market in the near future.

**Extreme Weather Events**

Jamaican insurance companies rely heavily on reinsurance companies in North America and Europe to backstop the policies that they write here in Jamaica. In some cases 80% of the risk is transferred to the reinsurance companies. The importance of this is that the foreign reinsurance companies largely determine the rates that we pay locally.

The problem is that extreme weather events in other countries. Jamaica has been relatively fortunate over the last decade to have dodged major hurricane damage to its infrastructure and agricultural sector). However, neighbouring countries like Dominica and The Bahamas have suffered massive damage that, in the case of Dominica reached 150% of its GDP. That is one and a half times the total output of the whole economy for a whole year.

Consequently, the insurance payouts in the Caribbean Yes, have been massive and the insurance companies have taken relatively high losses on their Caribbean portfolios. The upshot is that although there were not abnormal payouts in Jamaica the vulnerability of the region to extreme weather events caused the reinsurance companies to either stop offering any coverage whatsoever or to hike up the price of coverage.

**Insurance is essential for Development Projects**

The increasing cost of insurance and the rising difficulty in getting coverage has dire consequences for real estate development.

Unless the developer has such deep pockets that he or she is able to finance the project out of savings

But even if it can be built without insurance most of the purchasers of the units will have to rely on insurance politics to obtain the financing they need to pay for the units. As we all know, the banks require insurance coverage of the asset they are financing.

At some point the cost of insurance will start to affect the decision to launch a development project. In places like The Bahamas, that point has already arrived.

**Potential Mitigation: Evolve beyond regional or country risk ratings**

The current methodology used by insurance companies is to assess risk regionally and not based on actual data from a single Caribbean country or from an individual business or house.

The implication is that regardless of investments in stronger roofs, better drainage systems, back up power systems, reserve water storage, and removing avalanche risk, the actual cost of insurance will remain the same. This reality has started a trend of self insurance where governments, businesses and households are opting to not insure the full value of their assets. Entire sections of structures are left uninsured or owners opt for high deductible amounts so that only catastrophic losses are covered.

The implications for households, small businesses and governments are clear. The risk of climate change is not being transferred to insurance companies, it is being absorbed by local entities. This poses fiscal risk to governments, solvency risk to companies and financial risk to households.

There may be scope to partially reverse this trend by getting insurance companies to link the cost of policies to an assessment of the risk posed by an individual structure. This would create an incentive to invest in more resilient structures since there would be a payoff in terms of lower insurance premiums.

The challenge is that the Caribbean has not kept pace with North America in the creation of a market for affordable, bespoke adaptation solutions. Engineering design companies have not copied their counterparts in the US, who have created whole departments dedicated to providing climate adaptation solutions. Our engineering design firms and EPC contractors have preferred to import specialised technical know how when it is demanded. They have not seen this as a growth segment of the industry. It is possible that as the demand for climate adaptation solutions grows there will be an evolution of the design outfits and EPC in this direction. The firms that anticipate this new trend and act could reap first mover benefits.

**Lessons from Florida**

Here’s a quote from “**Florida's Looming Storm: Climate Change and An Unstable Insurance Market” by Leslie Eaves. 2024,** that demonstrates the similarities that exist between us; and which may offer the Caribbean a glimpse into our future when it comes to insurance coverage of our infrastructure, our businesses and our homes.

*“As climate change intensifies hurricanes in Florida and elsewhere, the property insurance system has come under pressure, with some carriers abandoning affected states, and others raising premiums to prohibitive levels for many homeowners.*

*The damage inflicted by Hurricane Idalia at the end of August is the most recent reminder of the devastating human and property losses associated with the extreme weather events that are being fueled by climate change.  In the state of Florida, the insurance sector has felt the effects of uncertainty and difficulty in calculating the risks that could occur from environmental disasters.   Florida’s insurance crisis is characterized by growing insurance agency insolvencies, policy non-renewals of and unsustainable reliance on taxpayer subsidies. After the record-breaking damages that occurred during Hurricane Ian almost exactly a year ago in 2022, some insurance carriers have become reluctant to price coastal properties, while other carriers have gone completely insolvent. Citizens Property Insurance Corporation, formerly the insurer of last resort in Florida, is increasingly becoming the only carrier that will price Florida home and property owner policies.”*

As we know, the actuarial experts at insurance companies base their estimation of risk on historical data. However, climate change is making historical data unreliable as a way to predict the likelihood of outcomes going forward. They are keenly aware of this and therefore have introduced “fudge factors” in their estimations to anticipate increasingly frequent and severe extreme weather events and therefore to price premiums. An underestimation of the risk could result in insolvency for the insurance company, therefore they are aggressive in pricing their anticipation of rising risks.

Florida’s Department of Financial Services reports that more than 14 insurance companies in the state were in receivership due to the hurricane-triggered payouts in 2022. The response of the surviving companies was to increase the price of premiums and to simply refuse to offer to renew coverage. This is an existential moment for insurance companies.

Even Florida has realised that efforts to transfer risk to the government as a way to ensure continued insurance coverage will not work. The risks are too high for the state government to absorb (the Caribbean governments certainly do not have the fiscal space to absorb that high and growing risk). The only sustainable solution is climate adaptation and Florida has not been slow in developing that capacity. They toughened building codes which instantly created a booming market for retrofitting private infrastructure to make it compliant with the new exigencies.

The Caribbean would be wise to look at the lessons learnt by its hyper-rich neighbour to the north. They ended up with a focus on climate adaptation. We would be well served to fast forward to that conclusion.