

## 2. A pathway to recovery





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Covering customers' most material risks in the short term

As governments begin to ease restrictions on businesses and individuals, albeit to differing timetables, companies are taking tentative steps to begin operating again.

The return to work is fraught with complexity. Companies need to keep their employees and customers safe, both from the current virus and from any potential further waves. At the same time, they are facing restricted working conditions, falling demand and changing customer behaviours.

This is changing the type of risk protection they are looking for over the short, medium and long-term.

In the short-term, Lloyd's research found that customers are most concerned about:

- Ensuring business resilience to a second wave of the pandemic
- Safeguarding employees as they return to work
- Providing a safe environment for customers as businesses reopen
- Clarity of insurance cover

The insurance industry and governments both have important roles to play in facilitating this economic reboot. The industry can offer insight into the nature of the risks to which their customers are exposed, advising them on the steps they can take to mitigate them, and by designing new risk transfer solutions that protect business recovery and ongoing operations in a post lockdown risk landscape.

Governments can provide clear guidelines on how to reduce the spread of COVID-19 and in some areas, work with the insurance industry to provide the security needed in the short term, ahead of a longer term solution (see Chapter Four for potential longer term solutions: *Recover Re* and *Black Swan Re*).

### Using existing insurance products to help the return to work

Many businesses are concerned about providing a safe environment for their employees and customers, while remaining commercially viable during what could be a long recovery phase.

Supermarkets have already put in place protection for customers and employees by restricting the number of individuals in stores, using personal protective equipment (PPE) and adding physical barriers. However, smaller stores may lack the physical space to ensure the safety of their customers. This will impact consumer confidence, businesses' risk exposure and ultimately their commercial viability – compounding the pressure on many smaller retailers who were facing challenges even before the current crisis.

Most businesses should be able to obtain the core commercial insurances that protect their employees and customers (e.g. public liability, employers' liability/ workers' compensation, professional indemnity) as they restart operations, provided they can demonstrate (e.g. through an audit process) that they are following government guidelines on social distancing and PPE usage.

Where government guidelines do not exist, or where there is evidence the guidelines are not being followed, providing cover could be more challenging. In some instances, clarification may be required to make existing cover relevant. This could be as simple as confirming the scope of existing cover, being clear about the conditions for the cover to be valid or by offering additional explicit cover.

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### Developing new solutions to support business recovery

Lloyd's research also shows that businesses are concerned about their exposure to a second wave of the pandemic. Many industry segments have suffered significantly since the onset of the COVID-19 pandemic, and their recovery will be challenging and heavily dependent on cashflow.

Any subsequent waves of COVID-19 would exacerbate this situation and could lead to more insolvencies, especially if governments begin to reduce the financial support they have provided to date. For example, trying to resume operations amid a second wave will be particularly difficult for airlines operating within Europe who already face large liabilities as a result of the EC261 regulation, which allows customers to claim compensation for delayed and cancelled flights.

Most businesses operated without cover for non-damage business interruption for communicable disease prior to COVID-19, but the demand for cover that includes protection against a second wave of the pandemic will now be significant. Indeed, research<sup>3</sup> shows that 44% of UK SMEs expect their insurers to change their policy terms around COVID-19 and cover it in the future.

In some countries, the threat of a second wave could make new COVID-19 business interruption cover unaffordable for customers (many of whom are already struggling from the effects of the current lockdown), or loss-making for insurers (many of whom are already heavily exposed to COVID-19 losses).

This is also true in certain sectors where the risk of transmission of COVID-19 is particularly high (e.g. liability cover in care homes and parts of the hospitality sector that provide accommodation or support to health workers), or where the impact of another lockdown would be particularly costly (e.g. event cancellation or film and TV production).

To overcome these short-term challenges and ensure customers are protected, there are three potential solutions:

- 1. The provision of a short-term government backstop ahead of a longer-term solution.** This model is already being deployed in some countries for industries such as film and TV production, and for trade credit insurance. Trade credit insurance relies on the credit risk of the recipient, which becomes a more material risk in a recession. This can lead to insurers withdrawing cover, which restricts trade and slows economic recovery. To prevent this, governments in some countries have stepped in to provide a backstop, taking on some of the risk.
- 2. Pooling insurance capital to provide some of the capacity required to cover a second wave of COVID-19.** This has the benefit of offering certainty of pay-out to customers in the event of a resurgence of the virus. The risk to insurers (and therefore the cost to customers) could be significant, but insurers could diversify this by offering the product across different industries or countries or even within a single country, where future lockdowns are applied only at a local level. Insurers could also manage their exposure by writing to a limit or targeting specific customer segments or industries, such as SMEs. If enough insurers participated in such pools or consortia, key sectors of the economy could be protected commercially. The Lloyd's market is planning to develop a new product along these lines (see *ReStart* below).
- 3. Offering longer-term commercial policies** so that insurers have a chance to recoup the claims made in the early part of the policy term over a longer period. However, government support may still be required given the high credit risk of such longer-term policies. Lloyd's has developed a framework that could be used to develop a government-backed insurance vehicle - *Recover Re* - that could do this (see Chapter Four for details).

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### **ReStart: a potential non-damage business interruption solution from the Lloyd's market**

Many industry segments - and SMEs in particular - have suffered significantly since the onset of the COVID-19 pandemic. Forced closures as a result of lockdown conditions have restricted the ability of SMEs to operate. The smaller nature of these businesses means that recovery will be challenging and heavily dependent on cashflow. A second wave of COVID-19 could exacerbate this situation and push businesses into insolvency.

**ReStart** is a potential new insurance solution the Lloyd's market is developing that could help. It would offer business coverage for future waves of COVID-19 by pooling capacity from several Lloyd's market participants. It would initially be aimed at smaller businesses, potentially expanding across a broader range of SMEs and mid-market over time. It will still be subject to the usual Lloyds performance management requirements and competition law considerations.

Benefits could include:

- Resilience for a key sector of the economy and support for the recovery from COVID-19
- Certainty of business interruption coverage for a second wave of COVID-19 to customers where few alternatives are available
- Contributes directly to customers and their recovery from COVID-19, helping strengthen customer relationships over time
- Potential application outside the Lloyd's market e.g. through involvement of wider London market and global reinsurers
- Manages affordability and insurers' exposure through risk pooling, variable limits and industry or geographical diversification
- *ReStart* could also provide a complementary offering to *Recover Re* (see Chapter 4 for details)

### **Accelerating the reopening of society by insuring the COVID-19 exit strategy**

There is broad consensus that life can only return to normality after a vaccine is developed, distributed and administered around the world.

The insurance industry has a major role to play in insuring the many risks associated with this medical response. For example, there are already multiple trials underway to test existing medicines' impact on COVID-19 in terms of treatment and prevention, all of which require insurance, and some of which are being insured through the Lloyd's market. As a new vaccine is developed further, larger scale medical trials will be required around the world, which will carry significant risk and will also require insurance. Insurers need to be prepared to write these risks at short notice at a significant scale.

Once a vaccine is approved and manufactured at scale, it will need to be transported safely and, potentially, at the right temperature around the world. Donors of vaccines to emerging markets often require the shipments be insured by local governments where possible; where cover is not available, recipients of the vaccines are not protected from losses. The Lloyd's market is working with several parties to develop ways to address this gap by providing effective cover for local vaccine distribution supply chains.