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► *Property: No longer the risk you can depend on* Societal, environmental and political trends are driving fundamental changes in property risk, an area famed for its predictability. Cécile Fresneau looks at what's changing, and the impact these developments may have

Property Focus



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Property is one of the best-understood and predictable lines of insurance – insurers have been writing fire insurance policies for over 300 years. Yet, property risks are becoming less predictable, reflecting wider societal, political, and environmental changes.

According to QBE’s Unpredictability Index, the world is a less predictable place for businesses. The past two decades, and the last ten years in particular, have been especially unpredictable, largely driven by deterioration in political stability since the millennium, the economic and political fallout from the 2008 financial crisis, a series of technological developments, and now Brexit.

Big picture

This unpredictability has profound implications for property risks. Despite an impression of permanence, factories, offices and public buildings are surprisingly vulnerable to change. Increasingly, fast changing social, political, economic and environmental factors will alter where and what we build, and how we use buildings.

Advancements in technology and machine learning are not only changing the ways businesses operate but are also driving a shift in work culture. Different working patterns and agile workforces are increasingly being enabled by improvements in communication.

The ‘globalisation’ of property will also have implications for physical and political risks. Most of the world’s fastest growing cities are in Africa and Asia. More development in areas prone to natural catastrophes are changing the impact of weather and catastrophic events in terms of physical damage, on a scale not previously seen. The cost of natural disasters has been steadily climbing



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– extreme weather in 2017 and 2018 cost a total of US\$487bn, according to data from Swiss Re.

Conversely, unpredictability in the political arena is also having a knock-on effect on real estate development as uncertainty drives cautious investors to adopt a ‘wait and see’ attitude

before committing to new projects. Equally, property occupancy rates are also feeling the brunt of economic and political factors as more premises are unoccupied or remain unoccupied for longer – creating a wholly different risk profile to those properties that are in use.



Green exposures

Environmental factors are an important driver for property risks. The need to reduce emissions and reduce energy consumption, for example, will lead to innovative building design and materials, which may have different risk characteristics. There is already a trend for industrial, commercial and retail properties to incorporate the use of green energy (including heat recovery and solar farms) while also reducing their water consumption and reliance on single use items, but these can bring enhanced or different inception or damage risks.

Potentially, higher environmental standards or green expectations could shorten the lives of buildings, making them obsolete or uneconomical. An increasing proportion of new builds are green, according to the 'World Green Buildings Trends' report.

Almost half of respondents to the survey said most new buildings constructed will be green by 2021, compared with 27 per cent in 2018, according to the report.

Keeping pace

The speed and complexity of change today is a particular challenge for property owners and occupiers. Buildings are typically designed and built with a specific purpose in mind, but they often last a lifetime, or longer, changing use many times over. Equipment and machinery can also quickly become out of date with technology advancements or changes in environmental laws or expectations.

New business models, technology and changing environmental standards are expected to affect demand for certain types of commercial real estate. According to

PwC, rapid changes in the application of digital technology will continue to reduce demand for retail and office space, but increase demand for new types of warehousing, close to the customer. For example, internet shopping has resulted in the decline of high street shopping and the creation of huge automated logistics centres. Older or underutilised buildings may need to be refurbished to bring them up to standard, extend their lives or for change of use – for example, many industrial sites in recent years have been redeveloped into residential, retail and office spaces. However, combustible materials, hot working and electrical installations during refurbishment result in a higher risk of fire.

The pace of change also comes into play post loss. Increasingly, companies that have suffered a loss want flexibility when rebuilding



a facility or replacing plant and equipment to consider advances in technology or environmental options.

Buildings for robots

Technology is having a big influence on how and where we work. With advances in communications, people are spending less time in factories and offices, and more time working on-the-go or from home. Over half of the labour force in the UK and US will work remotely within the next few years (according to the UK's Office of National Statistics and Freelancing in America report).

Automation is another factor affecting building use with robotics increasingly replacing human workers in factories and offices. According

to the International Federation for Robotics - the number of robots has increased by 114 per cent over the past five years, and is expected to double again by 2021. Several companies now operate so-called 'lights-out' factories- which are fully automated. Robots outnumber humans 14-1 at Philips electric razor manufacturing facility in the Netherlands while just four people oversee robots at Fanuc's Japanese robotics plant in Oshino.

Automation and robotics will reshape property exposures. For example, an increased reliance on technology places more emphasis on machinery breakdown risks and business interruption. Plant and equipment are more complex and

higher value than in the past, and specialised machinery can take much longer to repair or replace.

Increased electronics and machinery are also a challenge for fire risk and firefighting. Electronics and machinery tend to generate heat and run the risk of electrical fires, while the design of automated factories and logistics centres is centred around efficiency, rather than human intervention. Access may be inhibited during a crisis while the absence of employees can also affect the severity of loss – fewer people mean a reliance on fire detection systems, while fire fighters may be more inclined to tackle a blaze from the outside of the building where lives are not at risk.

There are also the hard to predict,



unintended consequences of using new technology in a factory or warehouse setting. Whereas a human will down tools in the case of a fire, the same may not be true for robots which may indeed hasten the spread of a fire if they continue to operate during a blaze. The fire at a state-of-the-art logistics centre in the UK earlier this year is a case in point. Despite improvements in risk management and safety regulation over the years, insurers have experienced an increase in commercial fire claims. While there is no single cause for this, machinery/electronics and refurbishment of buildings has played a part in several large claims. The adoption of state-of-the-art technology has also figured

in this. Different things can go wrong in commercial properties now and the impact of incidents can be more pronounced. Scenario planning needs to evolve at the same pace as technology and risk managers need to be able to think quite laterally when putting together their ‘what-if’ scenarios.

What’s next?

As buildings and factories become ‘smart’, the unpredictability of risks facing the property sector is likely to multiply. Alongside a deviation in building usage, an increase in automation and a shift in attitudes towards more eco-friendly solutions the nature of property exposures is changing. So too are the risk

mitigation practices business can put in place. The insurance industry has excelled at protecting against property risk for over three centuries but now, more than ever, the importance of risk management comes to the fore. While risk transfer mechanisms will continue to provide a security blanket for companies, in the face of rising unpredictability, it is the combination of insurance and risk engineering that will see businesses through the vagaries of an ever-shifting landscape.



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