CREDIT SUISSE

Event Report

CSA Insurance Linked Strategies
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COVID-19 Update – October 2020

We would like to update you on the status of the ongoing novel coronavirus (COVID-19) outbreak as well as the impact that COVID-19 has had on the portfolios we manage.

Since our last event report, the pandemic spread has become progressively under control across most developed countries during the third quarter. Over the recent weeks however, potentially related to the reduction of governmental restrictions and the colder weather on the norther hemisphere, a steep acceleration is observed in Europe and parts of North America. Within the European Region, some countries are experiencing a second wave of the pandemic spread that is exceeding previous peaks in terms of new cases. In other regions like Latin America, new cases have gradually declined from peaks observed in August. A certain stabilization can be observed in most Asian countries.

Business Interruption (BI) litigation and legislation cases
As we have reported in previous investor communications, the COVID-19 pandemic spread has had a severe impact on the global economy and in parts on the (re)insurance industry. Following the closures of businesses resulting from the pandemic spread, uncertainty surfaced around the coverage of foregone revenues caused by these business interruptions under standard commercial property insurance policies.

Across various developed countries, notably in the US and Europe, policyholders have challenged the denial of coverage of losses from business interruption by bringing their cases to court via lawsuits. So far, the outcomes of these litigation cases vary per country. Most cases in the US have produced favorable outcomes for insurance carriers whilst in Europe, most of the outcomes have been in favor of policyholders.
In addition, in the US, lawmakers in 10 US states have introduced legislation attempting to force insurers to be held liable for COVID-19 related government imposed business interruption losses under existing policies retroactively. This is despite standard policy terms requiring direct physical loss to the covered property to trigger an insurance loss.

Business Interruption Litigation cases
In the US, coverage of BI caused by a pandemic had never been tested in court. Although not all commercial property insurance contracts include specific pandemic exclusions, generally physical damage to the insured property is a required trigger for coverage. To date, litigation outcomes have been mostly in favor of insurance companies. In around 9 out of 10 cases nationwide, COVID-19 was not considered a direct physical loss.

In the UK, the Financial Conduct Authority (FCA) announced on 1 May that it would seek a court declaration in order to assist with the potential and ongoing disputes over BI insurance claims in the context of the disruption from COVID-19.
The FCA proposed to put the example policy wordings to the UK High Court on an agreed basis with eight participating insurers as defendants. A final draft judgment prepared for the parties came out on 15 September. The UK High Court ruled largely in favor of insurance policyholders admitting that coverage should largely apply in many cases. Clauses and terms under consideration are relevant to some 370'000 UK policyholders. Total payout from the industry could be as much as GBP 4 billion.

In Germany, following a surge of lawsuits against insurers, a Munich court ruled that the insurance chamber must pay the COVID-19 related business interruption. Hundreds of similar lawsuits against various insurance companies are pending in courts in Germany.

In France, a Paris court ruled that AXA should pay a restaurant owner two months of revenue losses. AXA decided to meet the bulk of business interruption claims from some restaurants in France after losing this court case.

In general, litigation cases across the US and Europe are progressing. Nevertheless, uncertainty around the overall outcome of losses across the industry remains substantial, given the growing number of pending litigation cases.

Business Interruption Legislation in US
In most states, legislation proposals are stalling and the expectation is that it is unlikely that these proposals will be enacted. In California, the legislation proposal has been withdrawn. However, if any of these legislation proposals is adopted, it will have far-reaching consequences. Consequently, a medium level of uncertainty remains until these bills are all withdrawn.

In California, a bill was introduced which included "rebuttable presumptions" of COVID-19 being present and causing damage to the insured business's property. This bill is considered unique, as insurance coverage would be made available resulting from COVID-19 being the direct cause of the insured's business interruption without the required physical damage to the insured property. Although the bill initially passed the California State Assembly, it failed to pass the Senate's Insurance Committee with insufficient support, after which the bill was withdrawn. However, the bill could be reintroduced early next year with amendments.

Non-Life Insurance Market COVID-19 Impact Categories
As the COVID-19 pandemic is still ongoing, there is a high uncertainty about the general COVID-19 impact on the (re-)insurance market as a whole and it is difficult to accurately determine the ultimate insured losses caused by COVID-19 and the magnitude of insurance and reinsurance claims.
We have grouped the (potential) impact from COVID-19 on the non-life insurance market into five broad categories:
1. Direct and specific pandemic insurance exposures (such as pandemic cat bonds and other forms of pandemic insurance)
2. Second degree pandemic exposure in **specialty lines** of business such as event cancelation, trade credit, mortgage insurance, workers compensation, Directors & Officers liability and travel insurance
3. Traditional property policies with **ongoing litigation**

4. Traditional property policies subject to **potential change of law** with retroactive effect, where business interruption claims would be covered even if not considered within contractual rights
5. Traditional property policies with **affirmative pandemic cover**, where pandemic risk is included

Uncertainty Scoring
With the aim to continue providing you with regular updates on the latest developments, we are introducing a relative "uncertainty–scoring" in the table attached. This scoring enables us to track how the relative valuation uncertainty is evolving across all the five categories mentioned above and provide respective reference in our future COVID-19 event reports.

Timing and Outlook
As court ruling across various jurisdictions are progressing, we expect to see further developments around the uncertainty of impact of ongoing litigation (category 3) during the fourth quarter. These developments would bring clarity and dissipate some of the existing valuation uncertainties. Regarding impact from change in legislation (category 4), we observe ongoing uncertainty as most proposed bills have stalled and with pending uncertainty of new bills being proposed. We will continue to actively monitor the status of these cases.

What has been described above is mostly in relation to the direct insurance market. The challenges and questions of the insurers being able to recover from reinsurers and reinsurers from reinsurers (retrocession market) has not yet entered a critical phase yet. We expect that on both levels there will be different legal and contractual challenges and hence uncertainties in relation to potential claims and payouts. We expect those legal questions to be addressed market wide in 2021. Currently we take the approach that potential claims on reinsurance contracts and retrocession contracts are reserved, which does not mean that there will be claims paid ultimately.

The COVID-19 pandemic as well as the related potential impacts are still developing and are subject to unexpected changes.

In the month of September, we have seen performance impacts from COVID-19 because of the UK court ruling and the prudent approach to reserve for this. At the time of writing, the impact of this negative reserve development on the Fund for September is -0.26%.

We will continue to monitor the situation of this event and will keep you updated on significant developments. In the meantime, please do not hesitate to contact us if you have any questions.

Kind regards,
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