VIEWPOINT

Co-operation is essential to contain US construction claims costs

Better communication between adjusters, quantity surveyors and other professionals who oversee the construction process could stem the rise in claims adjusting costs

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As a result of the Covid-19 pandemic, the US insurance construction sector is facing unprecedented challenges driven by the increase in material costs and ongoing supply shortages, shipping delays and longer restoration periods, which have all trickled down to affect the claims environment.

In terms of transportation, a lack of trucks and ocean transport capacity for items used in production has led to delays for customers and widespread interference at manufacturing facilities.

According to a recent report from global claims management company Sedgwick, material and supply costs that historically have made up a relatively low percentage of the total fee of a project have been becoming a real issue. As prices and reliable supply for both have been affected, a new variable of volatility has been introduced that will continue to affect construction material costs into the future.

The proportion of costs against materials is a crucial element that is ever changing; however, labour-associated expenses are affecting projects significantly more than material outgoings.

The make-up of cost per claim differs by carrier and type of claim, but there are some generalities that can be applied across the industry. For instance, roof claims are the most common types of losses for private residences, followed by water and fire damage. Each type of loss has different costs associated with its equipment, labour and materials. For example, roof repairs involve heavy material use.

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Lumber costs

The report identifies lumber expenses as an area of concern. It details the costs of two categories of wood materials, namely dimensional lumber and sheet goods. The price of the former, also known as softwood, has been affected by supply shortages related to disruption from the largest suppliers – countries such as Canada (which makes up 85% of all US lumber imports), Germany, Sweden, Austria and Brazil.

In the past 12 months, for example, board foot (BF) has seen a 350% price increase across all grades and qualities of wood.

Hardwoods, such as red oak, are commonly used to make furniture and cabinetry and are the best woods, despite making up a fraction of the total market.

Records indicate a 42% price increase in a 1.5" x 1.5" x 3' piece of red oak from June 2020. The reason for price differentiations between hardwoods and those on the

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commodities exchange is related to its rate of use in an average home.

On the one hand, hardwood may comprise a very small part of a home for the average US residence, such as a cabinet face, whereas softwoods will comprise thousands of feet of boards for the construction for the same home. As a result, how much a customer will be affected by rises in either softwood or hardwood prices depends on the type of wood needed to make repairs to their residence or build a new one.

350%
Board foot price increase across all grades and qualities of wood over past year

Therefore, a reported doubling of lumber prices does not necessarily mean a doubling of the cost of the reinstatement.

Following the drop of the US dollar by 11.2% in comparison to the Chinese yuan in the past year, US wholesalers must pay a weaker dollar at each stage of the transaction, which occurs in or is controlled by China. Long transits also add to uncertainty, as sellers of the finished sheet goods must charge what they believe to be the price of the materials once at its destination. This itself contributes to a 33% rise in sheet goods costs.

Labour in the US has been affected by a variety of factors including the pandemic and multiple hurricanes. Since the start of the pandemic, wages in the construction industry have increased by 1.2% for skilled trades. This increase fails, however, to capture the real issue, which is a general shortage of labour at the middle and lower ends of the market.

It is this shortage that creates an increasingly challenging market for restoration companies, which either have to opt for lower worker qualification levels or a lower operational margin when accepting insurance claims work under traditional pricing.

Transportation and labour

More broadly, the overall insurance construction process has been disrupted by transportation costs and delays, rising numbers of claims adjustment costs, and increased periods of restoration. Transport costs are likely to remain high for the foreseeable future, international logistic providers have indicated, with international shipping costs expected to carry on rising, resulting in a 300% to 500% year-on-year increase. There are some indications of a stabilising lumber market by the end of the summer, but shipping and labour will continue to be drivers of increased cost.

Over the course of the past year, delays in the period of restoration have increased and it is anticipated this will continue. Current delays are resulting in projects taking three times longer to finish, starkly contrasting with the pre-pandemic era, which saw dozens of trades and hundreds of material suppliers working together to ensure efficiency in the construction industry.

Some mitigating factors against this issue could arise, if a significant improvement in logistical availability of materials is achieved or there is a large arrival of skilled workers. Both factors need to come about to prevent, in the best-case scenario, a doubling in restoration period times.

The property claims sector is becoming more complicated. In the past, it was common for all parties to agree to labour rates offered by the contractor for a project with the necessary materials well established and easily quantifiable.

Indeed, the construction process was smooth and well-established, made possible through effective communication between adjusters, quantity surveyors and other professionals who oversaw different aspects of the project.

Nonetheless, 2021 has witnessed an increasing debate between stakeholders about all components relating to the cost, making it more difficult to come to an agreement.

Delays in obtaining materials are also causing disruptions, leading to adjustment teams getting involved in discussions of further business interruption costs. Today, a claim that would have been completed within three months in 2019 is now taking almost four times longer.

From a cost point of view, particularly on lumber market prices, record highs will normalise and stabilise in the 20% to 30% (year on year) range by late Q3. Material pricing generally depends where the material is sourced and how long it takes for the material to get to store shelves. The longer the process, which may involve materials being shipped overseas and back again, the more likely it will be that costs increase as a result of incremental wage pressure and the cost of travel will be observed.

There is light at the end of the tunnel, however. The majority of materials used for restoration projects is less impacted and if they are affected, the percentage of a total claim the materials represent is relatively small.

This dynamic means, as supply chains stabilise and material prices normalise the biggest remaining driver of cost, will be increased labour, the quantification of which is part of a normal claims process.■

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Transport costs in US construction are likely to remain high for the forseeable future