Economic Architecture Podcast - Episode 9 Transcript

The following transcript has been edited for clarity.

Stuart Yasgur: We're talking about insurance today. If I think back, if I hosted a conversation about insurance 10 years ago, I'm not sure that room would've been full, but now…

Carolyn Kousky: I've been thinking about insurance going back to 2005 with Hurricane Katrina. And in the years after that, I spent a lot of time working on flood insurance, and a lot of times I got blank stares about why it was so blank.

Stuart Yasgur: So, we may have been in the room together.

Carolyn Kousky: Yes, exactly.

Stuart Yasgur: But today, if we have a conversation about insurance today, that room is full. Can you help us understand what that big difference is that's moving in the background?

Stuart Yasgur: I'm Stuart Yasgur, and this is Economic Architecture, the Podcast.

Lately it feels like the topic of insurance has come up more and more, and it's coming up at dinner tables across the country. We live in a time where we're experiencing more extreme weather events that are happening more frequently and with greater intensity. One of the natural consequences of this is that it's increasing the risk that we face in our homes, and that increased risk is driving up the cost of insurance.

Stuart Yasgur: You know, for a lot of folks, when they get to the end of the month, they're thinking, can I even make these payments? That's not just a sense we have. It's actually reflected in the data. In 2024, U.S.

homeowners' insurance rates rose by 10.4% on average, and that was on top of a 12.7% increase the year before.

Stuart Yasgur: The costs are really increasing, and that's putting real pressure on homeowners, many of whom are already cost burdened. And we're also seeing a large number of people who are not getting access to insurance, even if they want it. According to the U.S. Treasury, there are about 620,000 non-renewals per year.

Stuart Yasgur: Nationwide and non-renewal rates are even higher in areas that are prone to extreme weather. So, for example, about 2% of homeowner policies in California received a notice that said that their homeowner's insurance wouldn't be renewed. And in some counties, places where the risk is higher, those numbers are even higher.

Stuart Yasgur: So, for example in Lake County, there was nearly an 8% non-renewal rate. If you put that all together, it's an enormous number of households who are not getting the insurance that they need at a price that they can afford.

Carolyn Kousky: And unfortunately, we often see that some of this hits hardest in the aftermath of a disaster where people go to rebuild and realize they actually didn't have all the coverage they thought they did.

Stuart Yasgur: Carolyn Kousky is acting Chief Economist at the Environmental Defense Fund and the founder of Insurance for Good. Her work explores multiple aspects of climate risk management and policy approaches for increasing resilience. Talking about insurance is really an invitation to a larger conversation. In many instances, when insurance costs are too high or there isn't enough coverage, that's a reflection of the fact that the risk is high, maybe even higher than we thought it was. And we need to face those risks head-on and decide what we're going to do about them.

Carolyn Kousky: Insurance was often thought of as just this private market product. And actually, it's this really critical part of our social safety net. So, is insurance a market product or is it a benefit that we think all households and communities deserve? And our answer to that question has a lot of implications for what types of policy interventions we think should be undertaken in these markets.

Carolyn Kousky: I think it's really happened over the last maybe five years or maybe since the pandemic about? In that time period, a whole bunch of factors came together to really drive up the price of insurance actually around the country. So not just in hotspots where we expected there to be challenges with insurance like Southern Florida, for example.

Carolyn Kousky: And you couple that with the growing risk of extreme events as our planet warms and you've had this kind of perfect storm of impacts. So, we saw coming out of the pandemic supply chain disruptions, labor market disruptions, that prior period of high inflation, all of that made insurance cost more everywhere.

Because when it costs more to rebuild a home, then insurers have to pay more claims, which means they have to charge more premiums to cover those costs.

Carolyn Kousky: So that has, I think, made it more of a national issue than it used to be. And then of course, we've seen the really biggest impacts in the places of highest climate risk. And in response to that, insurers have been unwilling to take on risk, pulling back. And so that's really reduced coverage. And when you have that in the, um, presence of growing disasters, you also realize how critical insurance is.

Carolyn Kousky: Because when you don't have it, people really struggle with recovery and communities struggle with recovery. So, it's like the double challenge of it becoming much more expensive and harder to get at the moment we really need it more.

Stuart Yasgur: Absolutely. Yeah. And I think a lot of people are feeling it, but for some people it's having an impact on can they make their payments at the end of the month?

Stuart Yasgur: And for other people, as you point out, when they need to turn to insurance, are they going to have the insurance that they really need to recover from some of these events?

Carolyn Kousky: Yeah, exactly. And unfortunately, we often see that some of this hits hardest in the aftermath of a disaster where people go to rebuild and realize they actually didn't have all the coverage they thought they did.

Carolyn Kousky: So, we see for example, like after the LA fires, after lots of fires actually, that people tend to be underinsured, which is they didn't buy enough coverage. After other types of disasters, we've seen that it's not surprising, but consumers don't read the fine print of their policies, and one way that insurers have been dealing with some of the growing costs and risks, it looks like, anecdotally, is putting restrictions on coverage.

Carolyn Kousky: So, you might think you've insured your home to its full value, but there are these hidden sub-limits. Well, if it's hail on your roof, you only get this much. If it's burst pipes, you only get this much, and often not enough to actually fully cover those damages.

And finding out that you don't have the funds you need to rebuild at the time of a disaster is a really terrible time to realize you don't have the financial protection in place.

Carolyn Kousky: And then we're seeing in places like California that it's becoming more of an existential issue. Can I get covered at all? And of course, there's always the state-backed programs, but those tend to be worse coverage and more expensive. And so just fundamental insurability, I think has become a question in a way that it didn't used to be previously.

Stuart Yasgur: Yeah, and I think even just as you're talking about it, the complications that are involved with figuring out your insurance and what your coverage is and what you're paying for and what you might get and what kind of circumstance, it's so difficult for kind of an individual homeowner.

Carolyn Kousky: Yeah. And I've seen several proposals that suggest that to kind of help consumers with that we really should have baseline coverage standards. So that your standard homeowner's policy, because homeowner's policies are actually really different from each other, and I'm not sure consumers know that.

Carolyn Kousky: And if you just shop on price. You might not realize you're also shopping on what, what's covered and the extent of coverage that you have as well. So, if we could kind of make sure everyone has a baseline level of coverage to help them. I'll give you an example.

In California, they have a state law that if you have sort of full replacement homeowner's coverage, sort of good standard homeowner's coverage. It has to come with it. Ten percent code upgrade coverage, which sounds maybe in the weeds, but has proven really important in the aftermath of these fires. Because if building codes have increased. And in very important ways, like some of the fire codes might have increased since your home was originally built, and we need those codes to make sure that homes are safer, and that people are safe.

Carolyn Kousky: It pays you extra money to comply with those codes. So, it's a really important extra source of money for investing in resilience or any other upgrades for health and safety that have been undertaken. But you might not choose to add that in if it wasn't just bundled for you.

Stuart Yasgur: That's really interesting. And as you pointed out, the other major thing is that we have a bunch of people who can no longer afford homeowners' insurance. You're either getting subpar insurance, and I saw recent numbers that suggest there are 11 million households across the country who are now uninsured, and people are not getting renewed.

Stuart Yasgur: This seems like an entirely new phenomenon that's starting to happen here.

Carolyn Kousky: Yeah. We are seeing increases in people choosing to go without insurance. Now, lenders usually won't allow that. So, this is concentrated among people who can do that, which means they don't have a mortgage anymore, so they've paid off their home or they're not subject to a lender's restriction.

Carolyn Kousky: And that can feel like a good decision in the short term because it reduces your monthly expenses. But of course, as we were just talking about, it makes it really hard for recovery and we come up against this constant challenge in insurance, which is that the people who really need it the most, because they don't have other sources of dollars for recovery, they might not have large amounts of liquid savings.

Carolyn Kousky: They might be locked out of access to credit. Those households really need that protection more, more, and yet are often the ones who can't afford it and so don't have that coverage at all. And it explains too, a lot of research findings that post-disaster, we see increases in income inequality and it's often driven by who has insurance and who does not.

Stuart Yasgur: Especially at this moment now where we need to rely on it to play a larger and larger role in our lives as these events are happening more frequently and in more severe ways. We're starting to see all these challenges related to insurance. You're bringing together a place where people are starting to think differently about insurance and how it works.

Stuart Yasgur: Can you kind of share a little bit about what you're doing there?

Carolyn Kousky: In the last year, I founded Insurance for Good. We're a new non-profit that's focused on helping communities and the public sector with insurance and risk transfer solutions that can support their broader social and environmental goals.

Carolyn Kousky: And what we've seen is that those challenges can take a number of different forms. We've been talking about affordability challenges. That's certainly one. There are often times where the products on offer in our insurance market don't meet the particular needs that groups have. A really nice example of this is renters, which often, post-disaster, their biggest expense is an increase in rental costs because after a big disaster, housing supply goes down and demand goes up and rents often go up quite a bit and you can't buy insurance protection against that right now.

So, we also see these types of losses like that, that aren't well covered, other types of populations that aren't well covered. So, we're trying to help improve that safety net. We're also trying though, to better link the insurance with the needed risk reduction in resilience investments, because at the base of it, we can't create new financial structures to, to navigate our way out of the current challenges, right?

We have to actually invest in lowering the risk and then everything becomes more insurable. So, some of that means thinking about things that have nothing to do in with insurance, like our building codes, right? And our land use decisions and our zoning decisions. But I do think there are also intersections where insurance can really help and create a tighter link to drive those things together.

We've also been thinking about how insurance is widespread across the economy. It enables a lot of economic activity, which also means it's a lever into lots of sectors to get better environmental outcomes, better climate outcomes. So, there's a lot of ways insurance can end up being a force for good.

Stuart Yasgur: That's fascinating. And is there a concrete example there of how it might prompt us to think differently?

Carolyn Kousky: I think one example goes back decades, which is our flood insurance program. And over 50 years ago, the private sector really withdrew from offering flood coverage for some reasons that still exist today, others that don't. Only the riskiest people buy insurance and that doesn't make a great risk pool. That's still the case.

But also 50 years ago, we did not have the modeling data, technology tools to understand the risk in the way we can now. So that's actually different. But in response to that there was a kind of general policy conversation that people shouldn't be relying on ex-post disaster aid for these events, and that insurance really should be the vehicle for recovery. And if the private sector wasn't going to offer it, then the government was going to step in and create an insurance program.

Carolyn Kousky: So, are we creating these insurance programs? And then that raises a whole host of follow-on questions, right? Who's eligible? How much are we charging? Are we subsidizing? Are we cross-subsidizing? Like where does the taxpayer fit in to covering these losses versus the people who are at risk? How do we integrate it into our risk reduction and our mapping efforts and all these things?

Carolyn Kousky: It gets complicated, but there's actually a very long history now of these types of programs. The flood program, as we just said, is like over 50 years old now, but if you look around the world, there's really no private disaster insurance market that's fully functioning with a high degree of take-up rate that doesn't have the government inserted in some capacity, because disasters are just fundamentally difficult for the private market.

Stuart Yasgur: That's fascinating. So, you think that there's a structural reason why the government needs to play this kind of backstopping role?

Carolyn Kousky: If you want insurance to not be wildly expensive? Yes. So that comes back to these questions. And so, if you think about everybody putting money into a pot and something bad happens to them, they take the money cover their loss, so lots of things.

Auto insurance is pretty much like that. Health insurance can be like that. Like not everyone gets in a car accident at the same time every year it's someone else. But losses year to year are pretty stable and so you can largely, not totally, but largely fund this year's losses out of this year's premium revenue and disasters, of course, are just not like that when a big disaster happens.

Carolyn Kousky: Everybody gets hit at the same time and really badly, right? And so, losses are not stable year to year. You have these huge spikes. And so, to offer insurance coverage without the company going insolvent, they have to have access to a lot of capital. So that's why we have global reinsurance markets that pool the risk globally.

Carolyn Kousky: That's why we have an insurance-linked securities market to transfer some of that risk into the capital markets. And all of that allows for disasters to be insured at much higher cost, because that kind of risk transfer is not free. And so, you often get it the situation where the cost for the private sector to cover a disaster risk is just above what people are willing or able to pay.

Carolyn Kousky: And that's when you have a market breakdown, and that's when we see governments step in.

Stuart Yasgur: Interesting. And then I'd love to go back to something you said before, which is the connection between insurance and resilience. So, insurance is something we take out to deal with the consequences of risk. We are certainly seeing more extreme weather events.

Stuart Yasgur: They're coming more frequently; they're becoming more significant in the occurrences that are happening. But whether or not that translates into risks that affect people, that affect our lives, our communities, our property, it's somewhat an effect of the choices we make. And if we can lower that risk, there's the argument that potentially we can save on insurance, but how do we make that connection between the choices we make to create more resilient communities and our ability to lower the cost of ensuring our risk and using some of that savings to help pay for creating some of the resilience?

Carolyn Kousky: I think that's the outcome everyone would like to get to where your investments in loss reduction create this savings and you can somehow pull that savings forward as a cashflow to pay for the needed investments in risk reduction. I think there's some challenges to getting there, although it's maybe not out of reach.

Carolyn Kousky: So, let's maybe look at a few examples. So, some types of investments. Like fortifying your home. Putting on a fortified roof or other hurricane upgrades are incredibly cost-effective. They immediately lower your losses for the individual property, and there's really great evidence, and we've already seen it start to be translated into insurance markets.

Carolyn Kousky: Now, insurance won't necessarily do this on their own, but regulators in almost every Southeast State have required premium reductions for home fortification, and so you can now get pretty sizable reductions in your premium when you undertake these measures and enough to pay back over some period of time.

Carolyn Kousky: Now, we haven't seen programs that create the financing to do that, but if you make the investment as a homeowner, you can know that you'll recoup your costs and of course you really recoup them and avoided losses. One of the challenges with wildfire is that. Your risk doesn't just depend on your decisions and your house.

Carolyn Kousky: It depends on your neighbors and what your community does and how the natural lands around your community are managed. So, it's really a collective risk and a lot of the investments are just never going to be paid for by the change in the premiums. But when you look at those investments, the avoided losses broadly to the community, as well as all the co-benefits of these investments.

Carolyn Kousky: Obviously make a lot of economic sense. There's been a lot of studies on these, and so it's how do we find the funding and financing to do these types of risk reduction measures that we know are beneficial for the community overall, but are not going to really be paid for by one individual premium, or even if you could collectively think of an institutional way to pull them across the thousands of properties that would be protected.

Carolyn Kousky: So, some of those are a bit more challenging. Another challenge to all of this is that risk is going up. That means prices are going up. And so, when we invest in loss reduction, sometimes all we're doing is. Not making it go up as much. And if we're not making it go up as much, we're not seeing price savings off today's dollars.

Carolyn Kousky: We're just seeing that prices aren't going to grow as rapidly as they would have otherwise. And there's probably a lot of behavioral reasons for that, but people don't really appreciate that as a benefit if you say, we're not going to give you a savings, but you can be really glad that your premium's not going to go up by 10 times would it? So that's a harder sell.

Stuart Yasgur: Right. Absolutely. Yeah. It's hard for people to imagine. Or to believe and have credibility in how high those prices would've been and what they're actually saving.

Carolyn Kousky: Yeah. Yes. And no one wants to tell that or make that public. So, no insurance company is going to be like, oh, actually by the way, we're putting you on this price trajectory where you can expect your premium to be going up by X percent every year.

Carolyn Kousky: And so, I think it's often a challenge because homeowners don't understand that they're in this environment of growing risk and that we are really seeing extreme event risk go up year after year and events that are far outside the historical record. And that's the environment that we're now trying to ensure and build for. But it's very difficult for us to have mental models of how much risk is growing.

Stuart Yasgur: So, you're in conversations all the time about how we might think differently about insurance. Are there some of these kinds of new evolving models that you're seeing that you think are particularly innovative or worth consideration?

Carolyn Kousky: Yeah. We're looking at a couple different things. We're working with the city of Philadelphia and some neighborhood organizations right now on whether a parametric, a microinsurance product around flooding, might be a good fit for this community. We're looking at a community that has pretty substantial flood risk, but it tends to all be shallow flood risk.

Carolyn Kousky: And this makes our federal program not the best fit for it because in our federal program, you have to ensure to almost the whole value of your home, If you want to get what's called replacement cost coverage, which means we give you the full value you need to replace an item that was damaged.

Carolyn Kousky: Otherwise, you get actual cash value coverage, and that means that if you have 20-year-old cabinets, we're going to give you the depreciated value of 20-year-old cabinets that got flooded. But you can't go out and buy 20-year-old cabinets. So that really just means you do not have close to enough money you need to actually repair.

Carolyn Kousky: We also see that in this neighborhood. There's a lot of non-property losses, which aren't well covered by our current market. So, things like evacuation expenses or higher commuting costs, because the roads were flooded, needing to clean out the debris, these types of things. Some of the stakeholders that we're working with think that a much better and higher value product for this community would be: the flood happens, you get 10K, 20K automatically in your bank account right away for whatever your economic needs are.

And that's also really appealing to residents because it can often be really contentious to negotiate with your insurer and feel like you got a fair payout and can take a really long time. So even if you don't get quite as much, but you get it quickly with no transactional cost of like meeting and fighting and phone calls, that can be really beneficial.

Carolyn Kousky: I will say though, they're not a replacement for homeowners' coverage, right? If you're somewhere where your whole home could burn down or be knocked away in storm surge, you need full and complete coverage. So, it's not for everywhere.

Stuart Yasgur: That's really interesting. So, in the absence of the federal government playing this role, we need to think about how do we help take care of our own risk and also the risk of our neighbors and our community members.

Carolyn Kousky: Exactly.

Stuart Yasgur: Yeah. That's really interesting. Is there somebody specific that you think is stepping forward in that way?

Carolyn Kousky: Always the challenge that we talked about at the beginning of this conversation is who's going to pay for it? And especially this one we were just talking about with; there are lots of ways that the insurance sector could come in.

Carolyn Kousky: As a substitute for a loss of federal dollars, but it's not free anymore. The reason communities like to rely on FEMA and HUD dollars is they don't have to pay for them. And so, insurance, it's not free money. It's a financing tool, and you use it because you'd rather pay a little bit in the good years to protect yourself from that huge disaster cost.

Carolyn Kousky: And so that's, yeah, this affordability issue isn't going to go away. I think we need to change our frame of mind to think about insurance as part of. A more holistic approach to risk management. And as risks grow, we really need to be thinking comprehensively about how do we reduce the ones that we can cost effectively?

Carolyn Kousky: Where does the risk transfer come in? Where does the risk education come in so that everyone understands the risks, they're facing? Risks are essentially invisible, right? You don't see your risk level anywhere, so most people really aren't aware of the risks that they face until something bad happens, but you've then missed the moment to prepare and mitigate and right. So, yeah, so there's lots of hurdles.

Stuart Yasgur: Yeah, I think that that's a really good point. And in some ways, and to something we've mentioned earlier, which is insurance is where this stuff sometimes becomes visible for people, and so we have a lot of conversations about insurance at this moment, but it's also a much broader conversation about all kinds of planning decisions we are making. We could be making, what actions we could be taking.

Carolyn Kousky: And I think sometimes our policy conversations are getting caught up on insurance solutions for insurance problems, which makes a lot of sense. But conversations like, should the federal government be ensuring all types of payrolls and all of those are really important conversations that we're a part of.

Carolyn Kousky: And I don't mean to minimize the importance of figuring out the federal and state roles. I think it's absolutely essential. But that's not going to solve the problem. We can't have new insurance structures to get our way out of rising climate risk. What's going to solve the problem is actually facing that risk head-on, and insurance really should be seen as the signal that the risk has gotten too high.

Carolyn Kousky: So high prices, we tend to say insurance problem. We need to change the market. We need to change regulations; we need to change the structure. Instead of saying, wow, that means risk is higher than we thought. What do we do to lower our risk? And for some reason, those conversations are much harder to have, and I think it's because they fundamentally require more difficult type changes.

Carolyn Kousky: We need to think about the way we build where we put capital, but that's going to be our long-term solution.

Stuart Yasgur: That's great. And then in light of that, what do people do? You're an individual listening to this thinking maybe for the first time or thinking in a new way about the risks that you're, that are around you, and what kind of steps do you take?

Stuart Yasgur: How do you start thinking about this differently?

Carolyn Kousky: The first is to try to educate yourself about the risks that you face, where you live, and that should be easier than it is. There are states that are making some steps to doing that. Things like disclosure laws when you buy and sell property, so you can better understand different communities and places are creating better maps for their populations.

Carolyn Kousky: There's not the one-stop shop right now to understand that. Um, for example, if you're in New York City, they've created an inland flood map around stormwater flooding, since that's a growing risk. So, you have to track down some sources of information and then think about what that means in terms of what your potential losses might be and what you can do in order to lower those.

Carolyn Kousky: So, for, as we were talking about for some perils, there's some really cost-effective and simple upgrades to your home that can really provide a lot of protection for others, it's a lot harder if you're at risk of high flooding. You can elevate your home. That's really expensive. You could do some things if you were facing shallow flooding to pick flooring and stuff that's more flood resilient, but that's just a harder peril that frankly probably needs to be addressed through location, choice, and community level investments and things like green infrastructure and levies, and other types of things.

Carolyn Kousky: I think dealing with the risk of where you live is something that really needs to happen at the time you decide to live somewhere.

Carolyn Kousky: And so, using that window of when you're buying a home is really a good time to be thinking about how much is the insurance going to cost? How safe is this home? Have there been upgrades? And to ask all of those questions. And I think understanding that risk and how it's changing is very much what economists would call a public good.

Carolyn Kousky: It's something that helps everybody and everybody benefits from it. And just because I'm benefiting doesn't mean you're not going to benefit. And public goods tend to be underprovided by the market. It's why we see governments provide things like national defense and education, right? This kind of classic economic theory, but I think it applies to climate risk information as well.

Carolyn Kousky: And so, I do think that there is a powerful policy argument for having federal, state, and local governments providing more of this information and making it easily accessible for everyone. And that's why also to bring it back to the present moment, I'm really troubled by the fact that a lot of the federal climate risk information has now been removed, and that's going to make it harder to make the good decisions we need to make that will keep ourselves safer and lower losses into the future.

Stuart Yasgur: Yeah, and on that note, I want to say thank you, Carolyn. This is a great conversation.

Carolyn Kousky: Thanks for having me on. It was great to chat with you.

Stuart Yasgur: One of the threads that I would want to pull out of this conversation is really a design question. In some instances, the rising insurance costs are really a signal about the growing level of risk that homeowners face. Given the increasing frequency and intensity of extreme weather events and the rising cost of insurance is a call to action that we need to address those risks in a way that we haven't yet.

Stuart Yasgur: In some cases, there are effective steps we can take to lower the risk we face in our homes. For example, think about the standard for fortified homes that Carolyn mentioned. We've seen evidence that when homes are built to the fortified standard, it lowers the risk of damage from storms and hurricanes, and that lower risk is reflected in the lower insurance costs for fortified homes.

Stuart Yasgur: It's a great example of how we can lower insurance costs by lowering the risks. So, the question is how do we pay to fortify homes? There are some people for whom this isn't an issue. They have the means to make the investment and it's worth it to have a home that's more resilient. There are also some very interesting government programs that have successfully helped create thousands of fortified homes, and we're going to get into that in one of the later episodes.

Stuart Yasgur: And there's still other examples where the fortified standards is built right in from the outset in new home construction. And while these examples have been very successful, the number of fortified homes that they've been able to create still pales in comparison to the scale of the problem, especially when we think of the sheer number of homes that would benefit from meeting the fortified standard.

Stuart Yasgur: So, this really raises the design question. Is there a way we can restructure our markets to address the problem? Can we use the savings from our insurance costs and use that to help us pay and make our homes more resilient? That's a question we are interested in looking at in the economic architecture design studio, where we think through how to design structural innovations.

Stuart Yasgur: We are interested in this question because we think a successful answer to it would lower the risk and would lower the insurance costs. And by doing that, it would enable us to use market forces to really scale the number of fortified homes there are, and that would help us create more resilient communities.

Stuart Yasgur: I'm Stuart Yasgur, and this is Economic Architecture, the podcast. If you're an organization or individual working on issues like these, please get in touch with us at info@economicarchitectureproject.org.

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