The Economics of Workers Compensation

National Council on Compensation Insurance
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Darla Moore School of Business

Outline: The Economics of Workers Comp

- **The U.S. Economy: Animal Spirits Awakened?**
- **Labor Markets: A Deep Dive**
  - Adverse and favorable developments impacting WC
- **Financial Markets: A Decade After the Crisis Began**
  - Interest rate trends: On the rise
  - Financial markets: The return of volatility
  - Why this matters to WC
- **Tax Cuts and Jobs Act of 2017**
  - What the Act means for insurers and WC
- **Trade Policy**
  - Why trade wars and workers comp don’t mix
- **Infrastructure Initiatives**
  - Good news for workers comp?

THE ECONOMY

The Strength of the Economy Will Greatly Influence Growth in Insurers' Exposure Base Across Most Lines—Especially Workers Com

How Is "Trumponomics" Impacting the Industry?

3

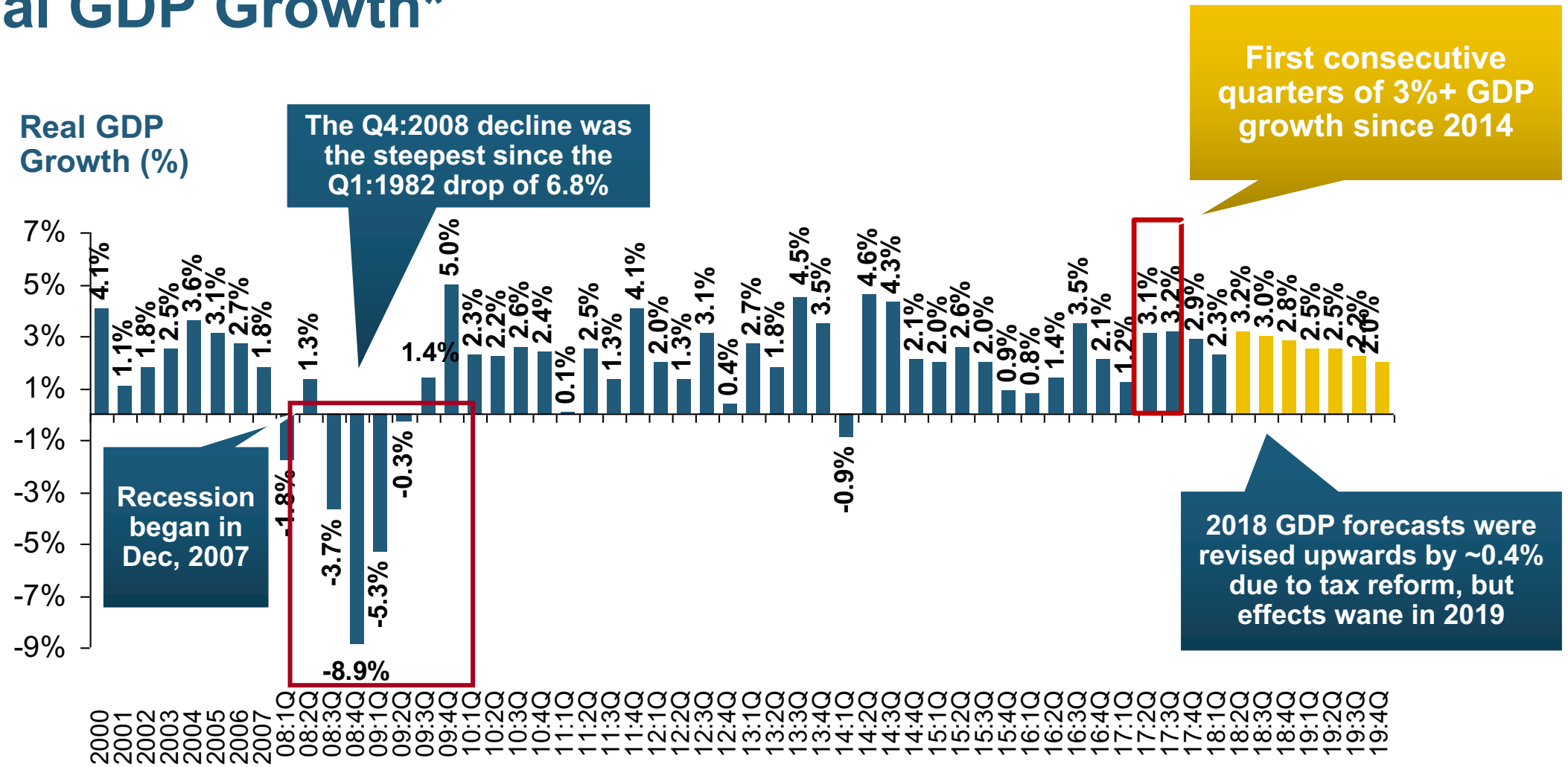
Awakening America's "Animal Spirits"

Economic Policy and the Insurance Industry

Consumer and Business Confidence Are Key

4

US Real GDP Growth*



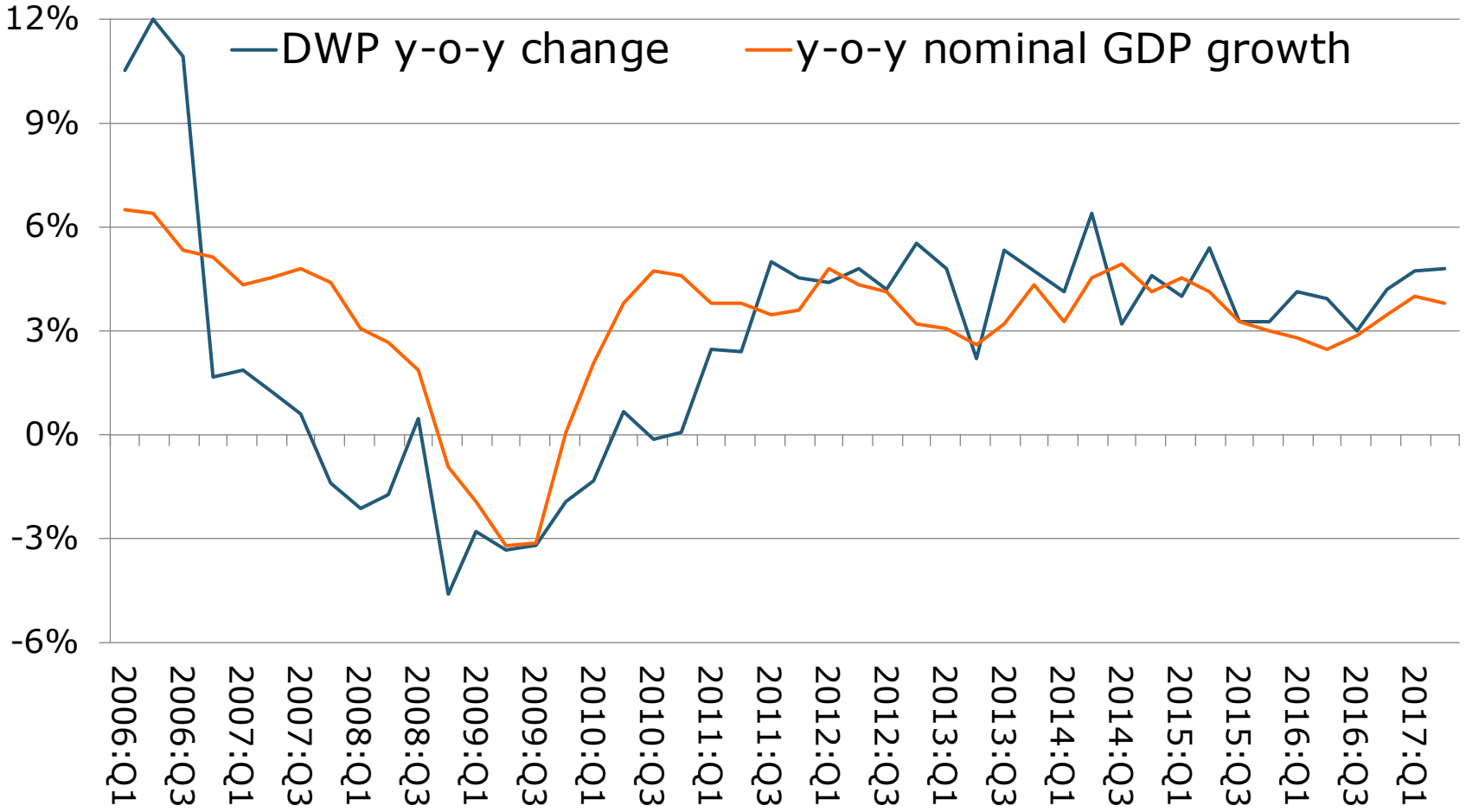
Demand for Insurance Should Increase in 2018-19 as GDP Growth Continues at a Steady and Perhaps Accelerating Pace and Gradually Benefits the Economy Broadly

* Estimates/Forecasts from Blue Chip Economic Indicators.

Source: US Department of Commerce, Blue Economic Indicators 5/18; Center for Risk and Uncertainty Management, Univ. of South Carolina.

The Economy Drives P/C Insurance Industry Premiums: 2006:Q1 – 2017:Q2

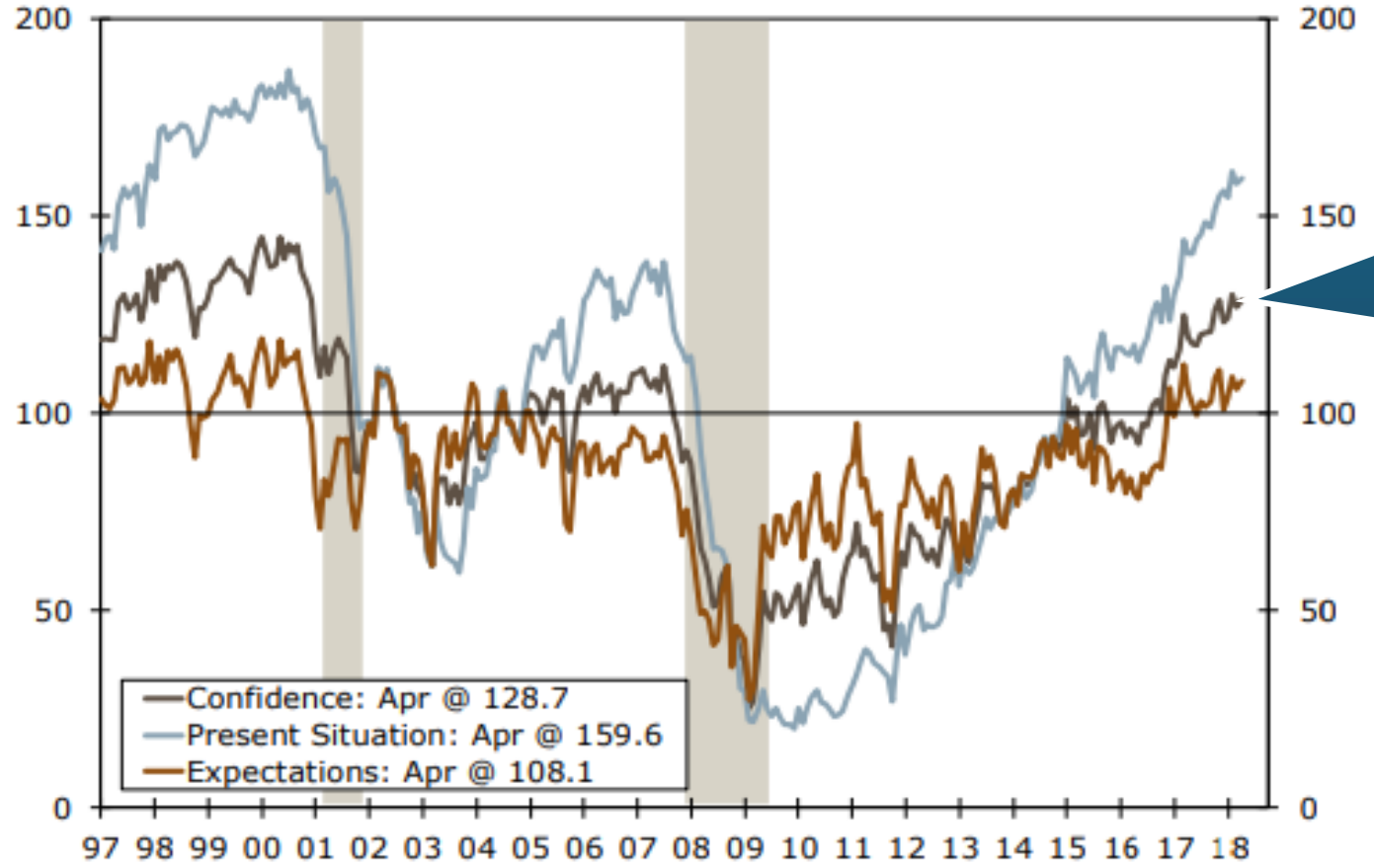
Direct Premium Growth (All P/C Lines) vs. Nominal GDP: Quarterly Y-o-Y Pct. Change



Direct Written Premiums track Nominal GDP—not quarter by quarter but overall fairly well.

Sources: SNL Financial; U.S. Commerce Dept., Bureau of Economic Analysis; I.I.I.

Consumer Confidence Index: Jan. 1987 – Apr. 2018

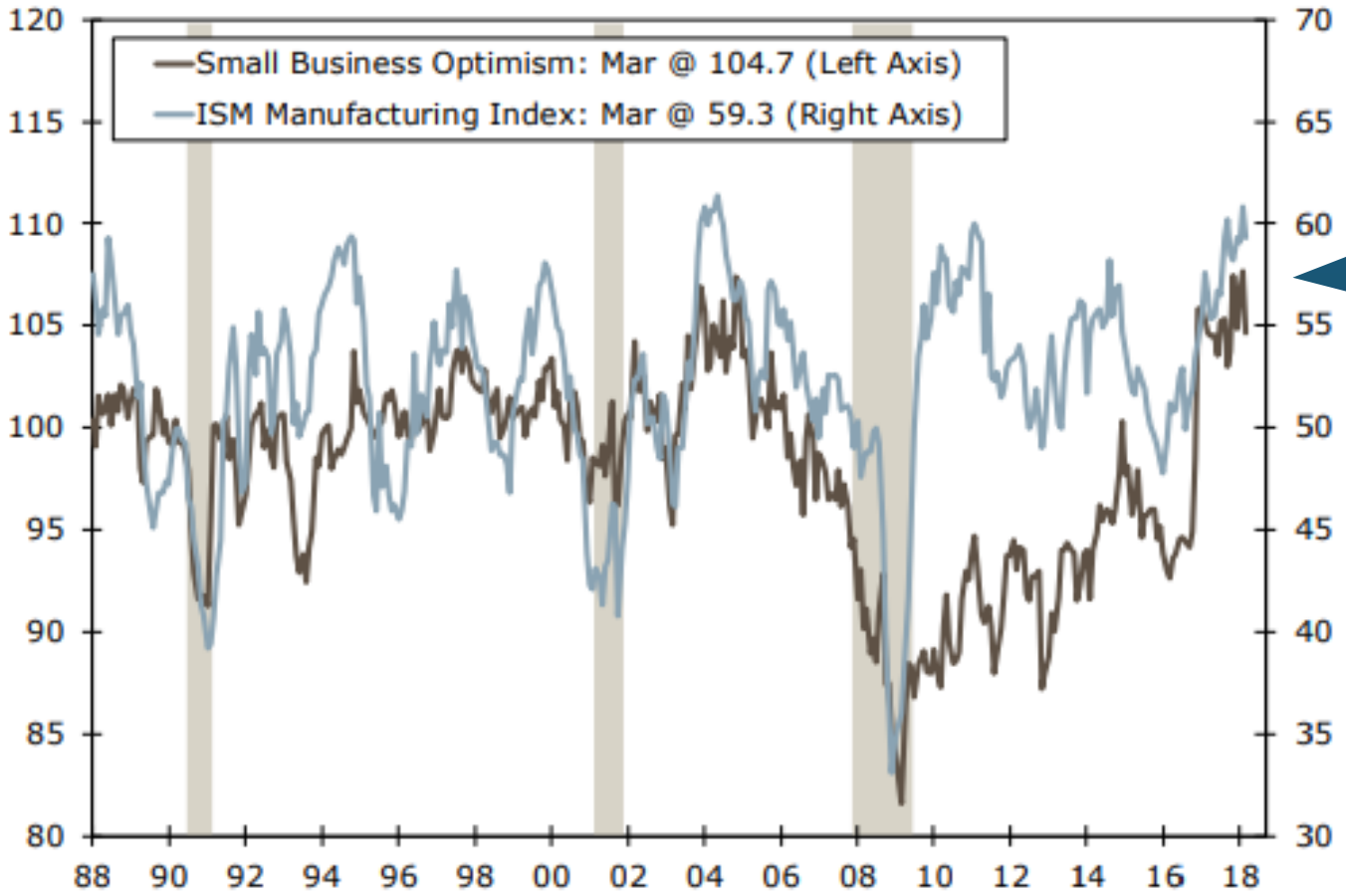


The Conference Board's Consumer Confidence Index stood at 128.7 in April, close to its post-recession high

Outlook: Consumers are optimistic about the future, which is consistent with expectations for stronger economic growth (consumers account for nearly 70% of all spending in the economy). Should positively influence growth of insurable exposures.

Source: The Conference Board; Wells Fargo Research.

NFIB Small Business Optimism Index: Jan. 1988 – March 2018



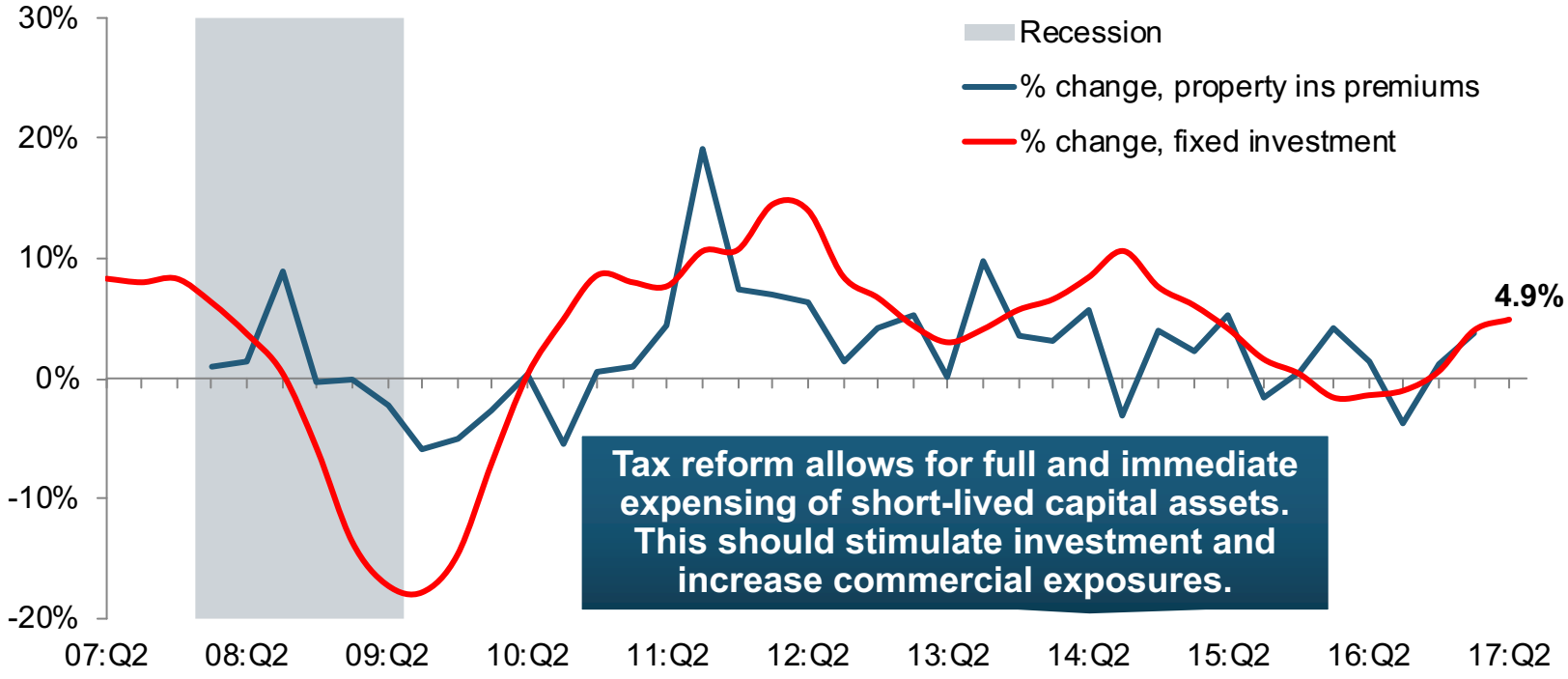
The NFIB's Index of Small Business Optimism remains close to its cyclical high. Tax reform, reduced regulations and strong sales will drive investment, hiring and exposures

Outlook: Small businesses are much more optimistic about the future

Source: National Federal of Independent Business; Wells Fargo Research.

Business Investment Is a Potent Driver of Property Insurance Premium Growth*

% change from same quarter, prior year



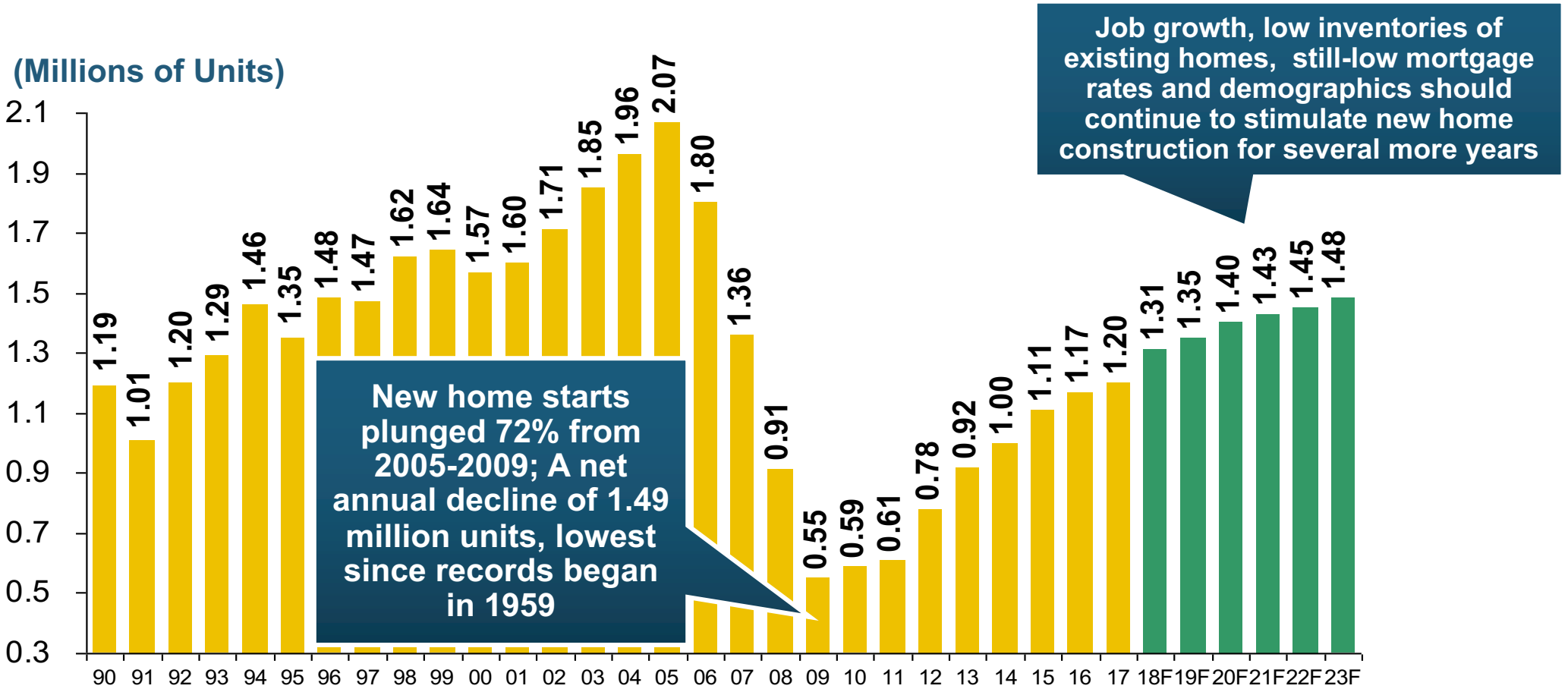
- **Business fixed investment is forecast to grow at 5%–6% in 2017:2H and at 4.5%–5.5% in 2018.**
- **Investment in equipment and software is expected to grow but investment in structures is expected to shrink.**

*Commercial property direct premiums written (fire, allied lines, CMP, inland marine, burglary and theft); business fixed investment (structures, equipment, and software).

Note: Recession indicated by gray shaded column. Data are seasonally adjusted annual rates.

Sources: https://fred.stlouisfed.org/series/PNFI#0; National Bureau of Economic Research (recession dates); Insurance Information Institute.

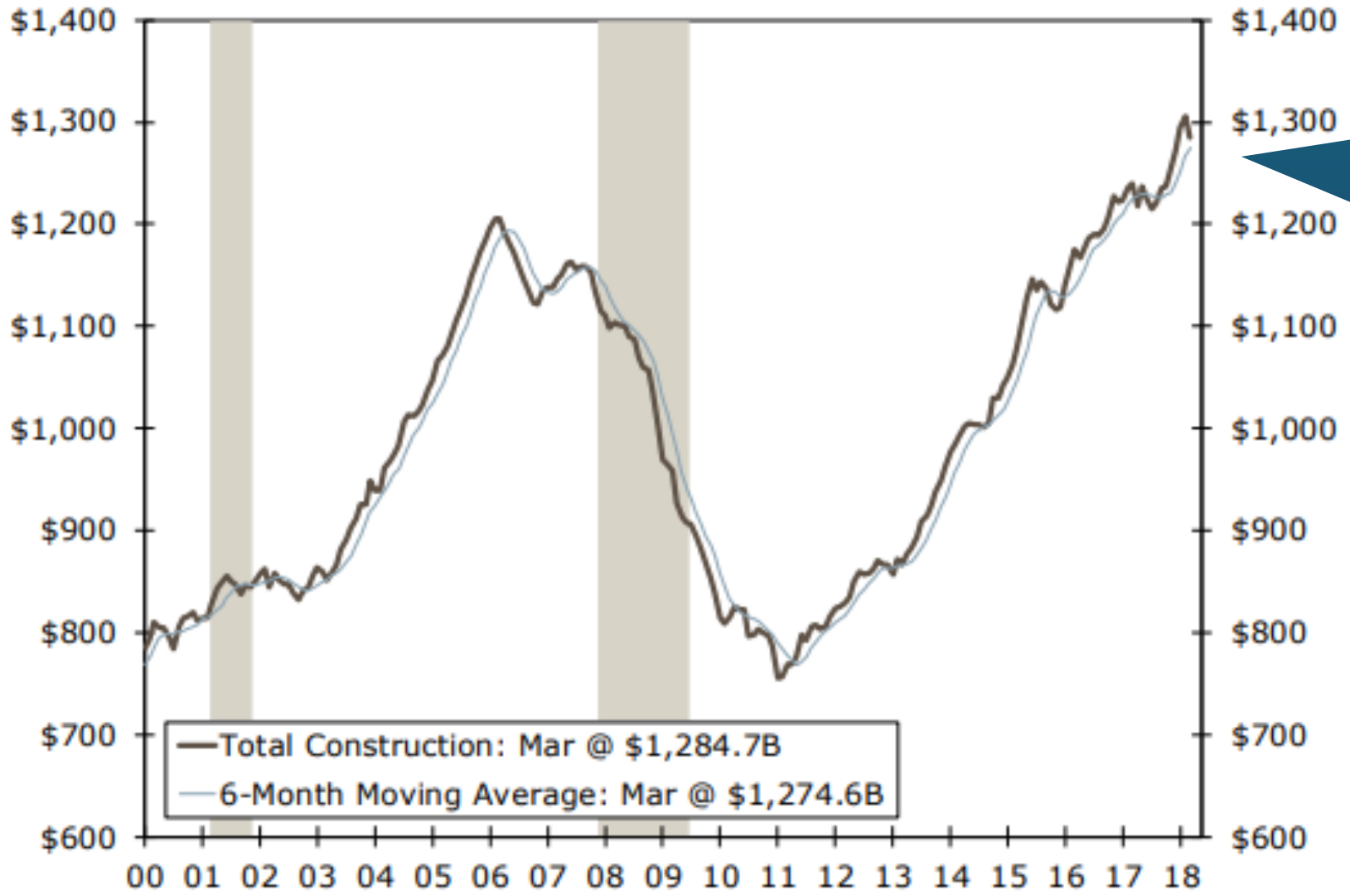
New Private Housing Starts, 1990-2023F



Insurers Are Continue to See Meaningful Exposure Growth in the Wake of the "Great Recession" Associated with Home Construction: Construction Risk Exposure, Surety, Commercial Auto; Potent Driver of Workers Comp Exposure

Source: U.S. Department of Commerce; Blue Chip Economic Indicators (5/18 for 2018-19; 10/17 for 2019-23F; Insurance Information Institute.

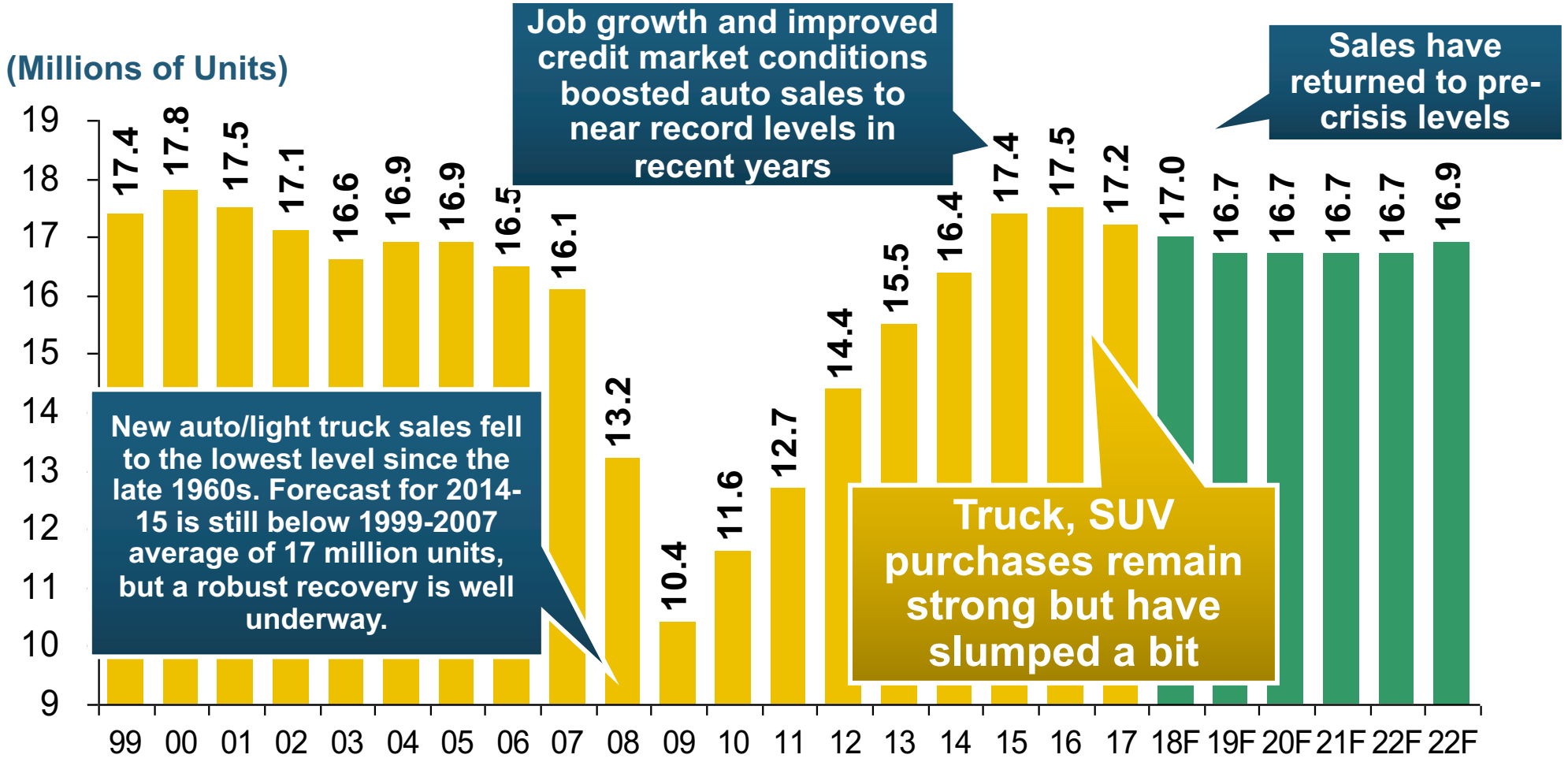
Construction Spending: Jan. 2000 – Mar. 2018 ($ Bill)



Private (but not public) construction spending remains relatively strong. Public construction spending could benefit from a boost in infrastructure investment

Source: US Dept. of Commerce; Wells Fargo Securities.

Auto/Light Truck Sales, 1999-2023F



Yearly car/light truck sales are slowing slightly, as demand tapers following the recovery from the recession. PP Auto premium might grow by 3.5% - 5%.

Source: U.S. Department of Commerce; Blue Chip Economic Indicators (5/18 for 2018-19; 10/17 for 2019-23F; Insurance Information Institute.

Labor Markets Trends:
Strengthening Continues in 2018

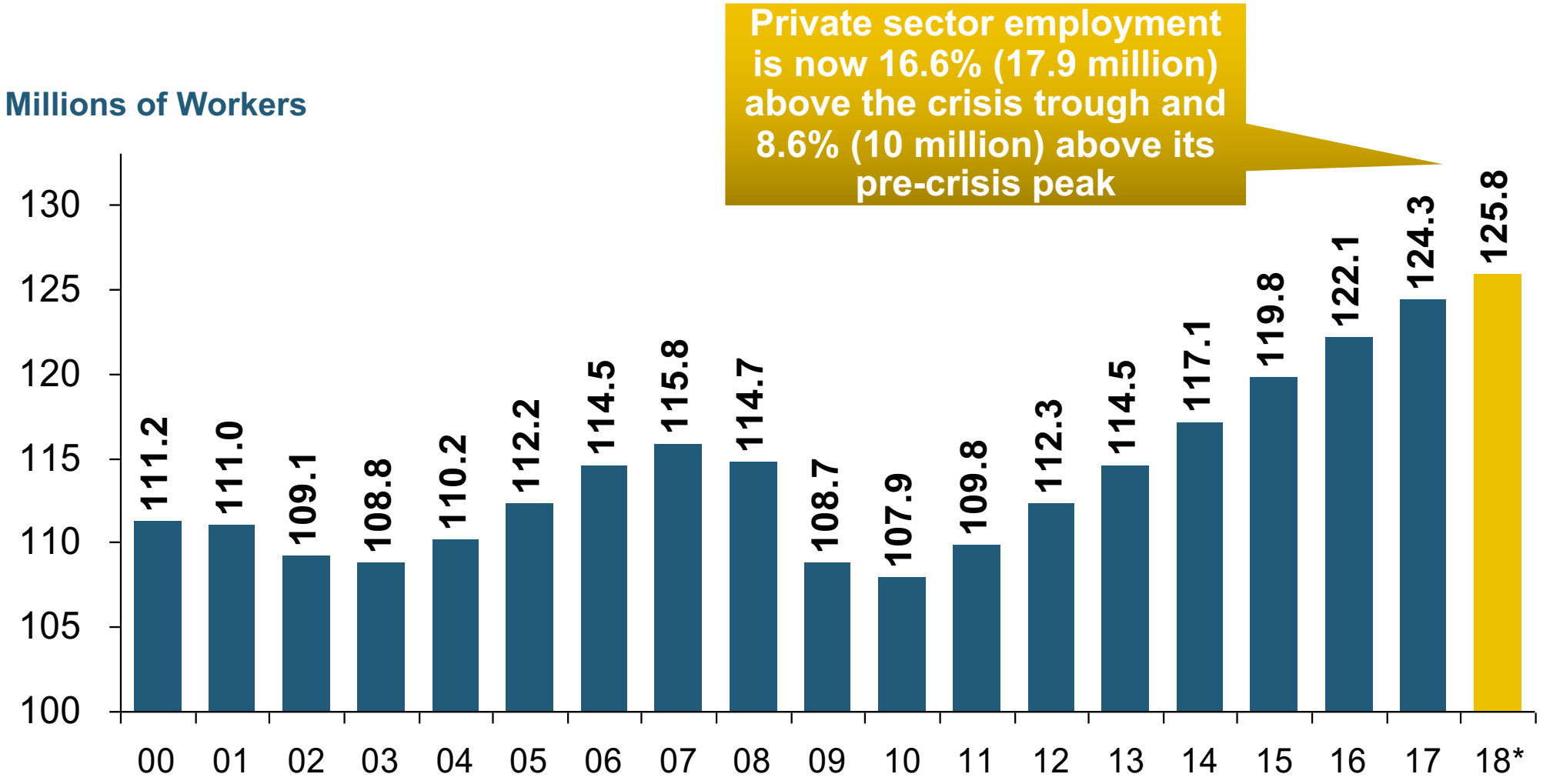
Strong Job Gains Continue

Unemployment Is at an 18-Year Low

Payrolls Expand to Record Highs

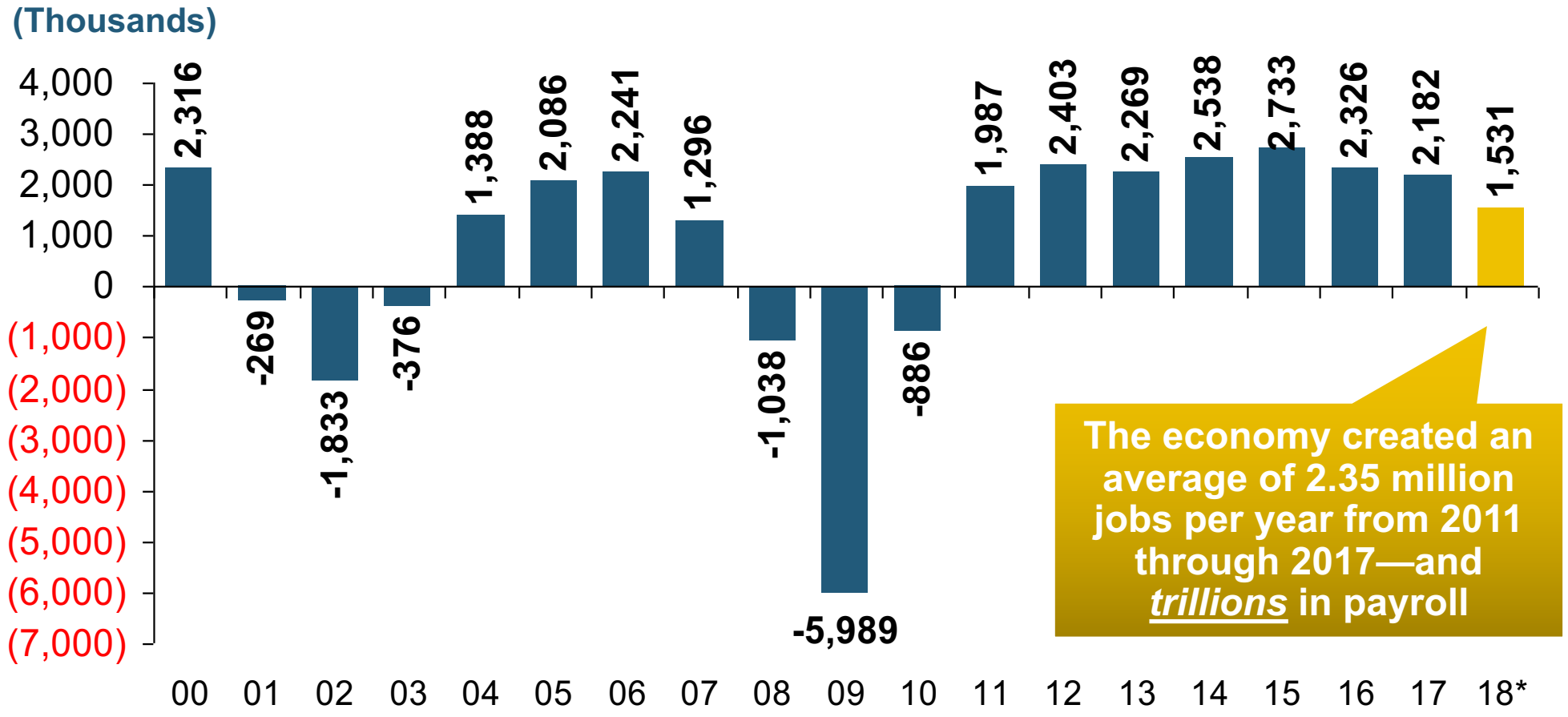
13

Private Sector Employment, 2000-2018*



*Annual averages of monthly data. 2018 figure is annualized based on data through April.
Sources: US Bureau of Labor Statistics; Risk and Uncertainty Management Center, Univ. of South Carolina.

Annual Change in Private Sector Employment, 2000-2018*



*Annual averages of monthly data. 2018 figure is annualized based in data through April.

Sources: US Bureau of Labor Statistics; Risk and Uncertainty Management Center, Univ. of South Carolina.

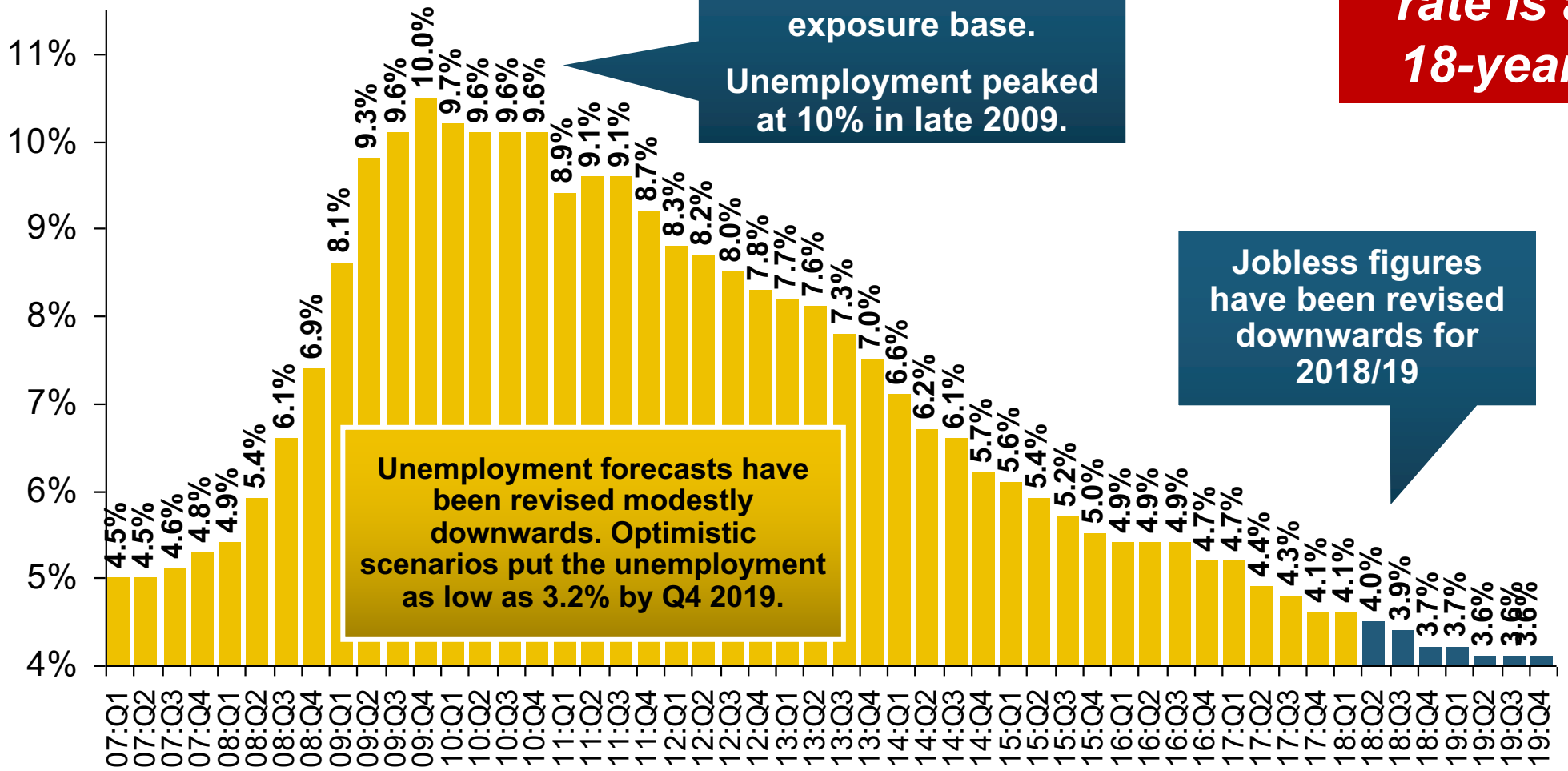
US Unemployment Rate Forecast

2007:Q1 to 2019:Q4F*

Rising unemployment eroded payrolls and WC's exposure base.

Unemployment peaked at 10% in late 2009.

At 3.9%, the unemployment rate is at an 18-year low



Unemployment forecasts have been revised modestly downwards. Optimistic scenarios put the unemployment as low as 3.2% by Q4 2019.

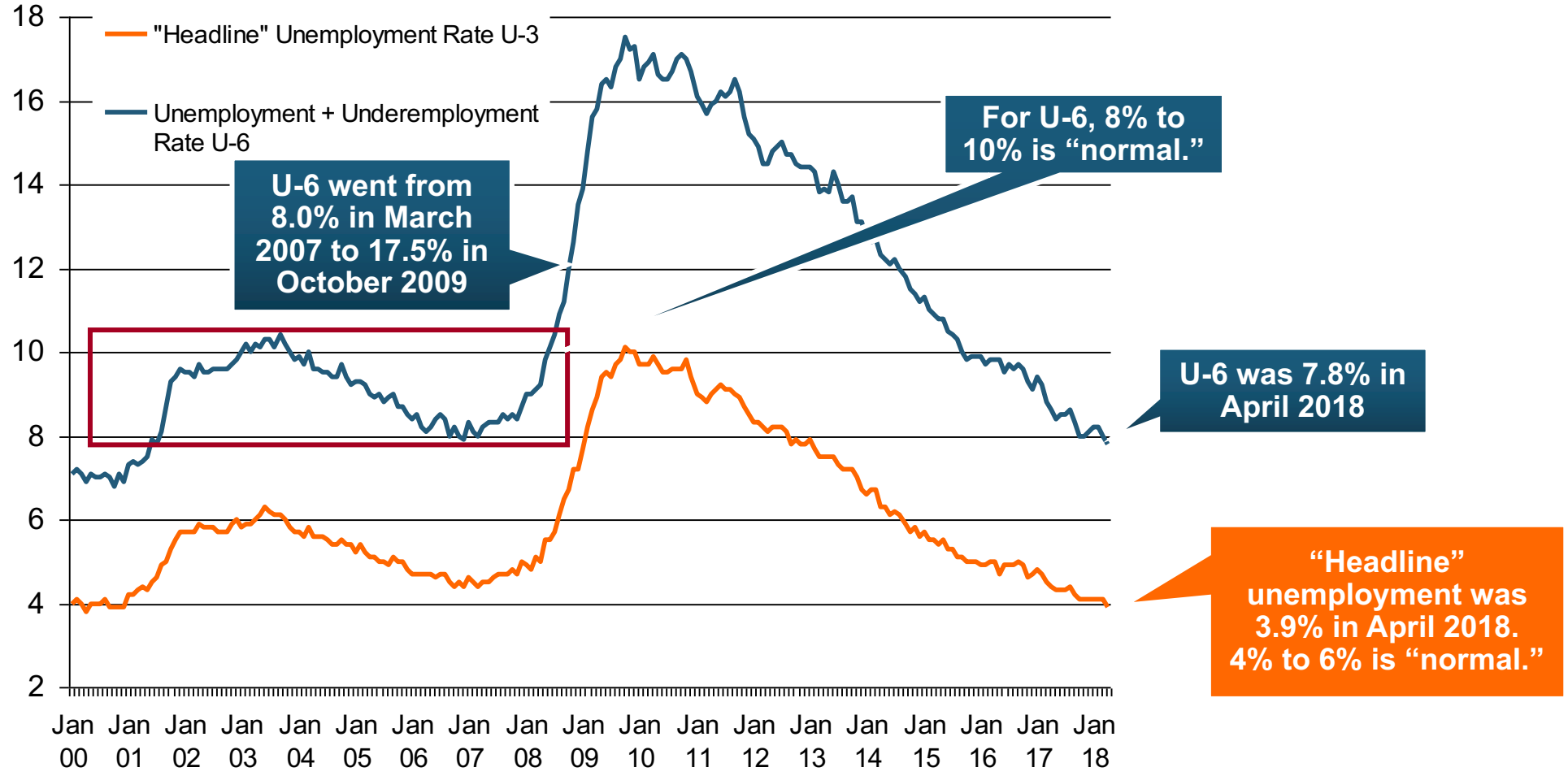
Jobless figures have been revised downwards for 2018/19

* = actual; = forecasts

Sources: US Bureau of Labor Statistics; Blue Chip Economic Indicators (5/18 edition); Risk and Uncertainty Management Center, University of South Carolina.

Unemployment and Underemployment Rates: Still Falling

January 2000 through April 2018, Seasonally Adjusted (%)

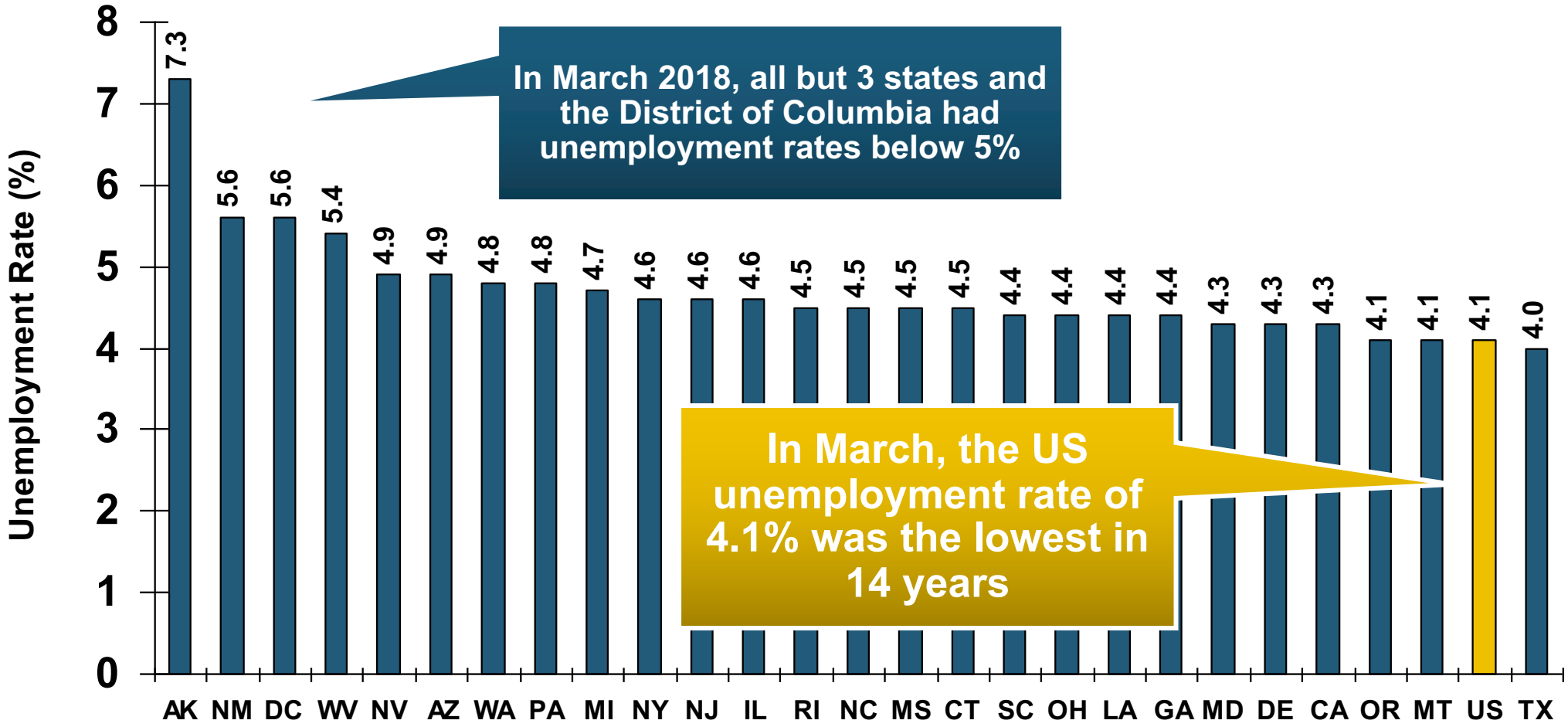


High unemployment and underemployment constrained overall economic growth for years, but the job market is operating near full employment.

Source: US Bureau of Labor Statistics; Center for Risk and Uncertainty Management, Univ. of South Carolina.

17

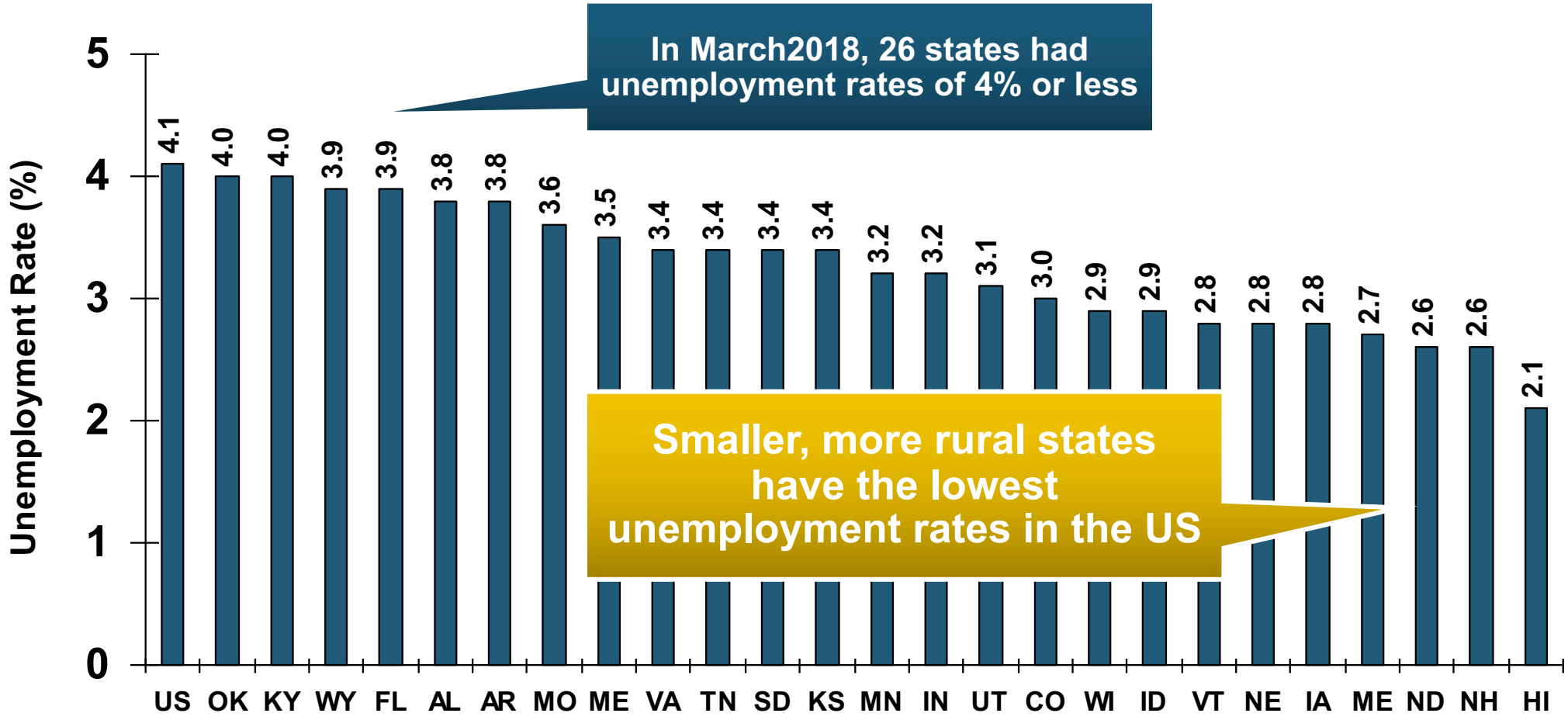
Unemployment Rates by State, March 2018: Highest 25 States*



*Provisional figures for March 2018, seasonally adjusted.

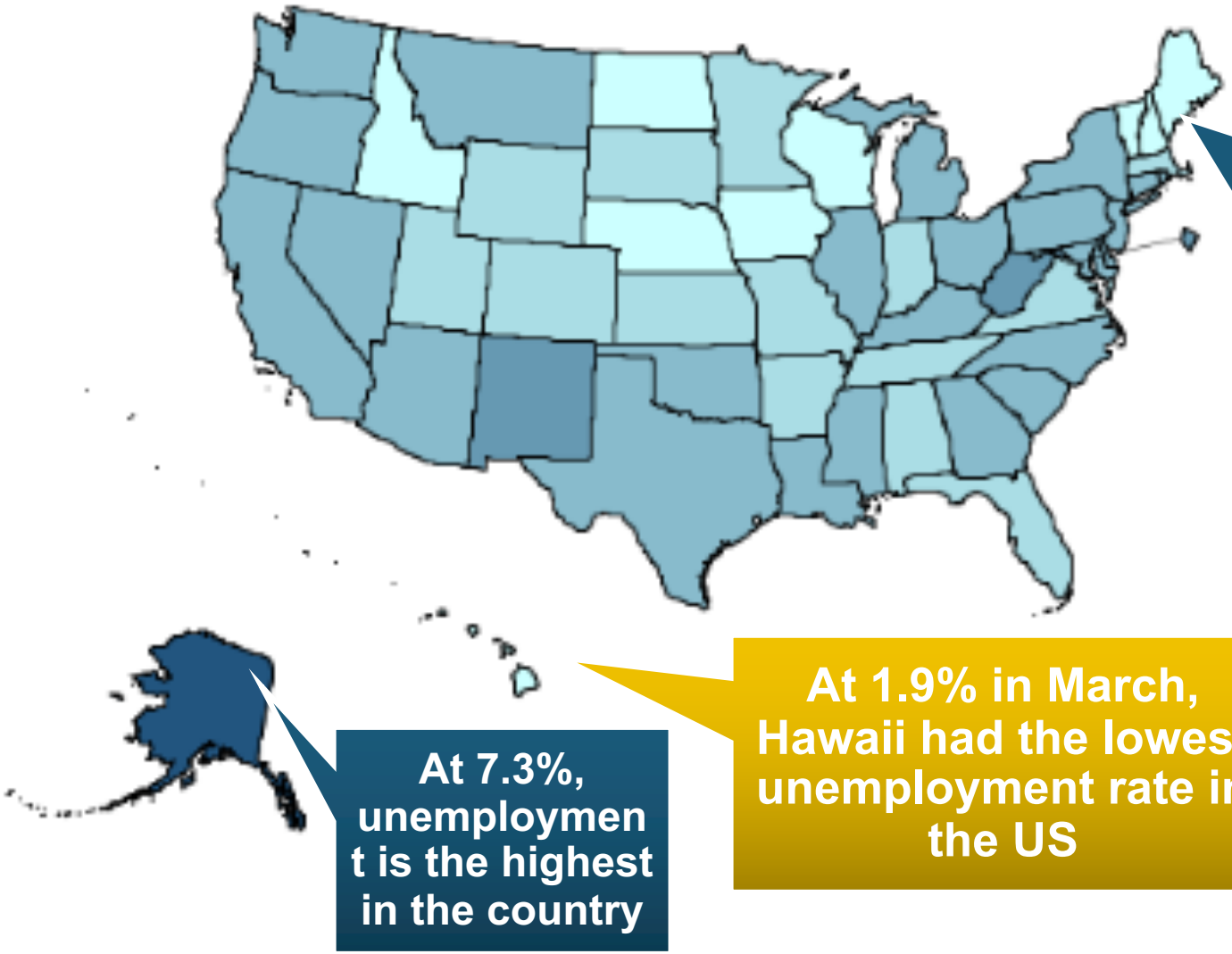
Sources: US Bureau of Labor Statistics; Insurance Information Institute.

Unemployment Rates by State, March 2018: Lowest 25 States*



*Provisional figures for March 2018, seasonally adjusted.
Sources: US Bureau of Labor Statistics; Insurance Information Institute.

Unemployment Rate by State: March 2018



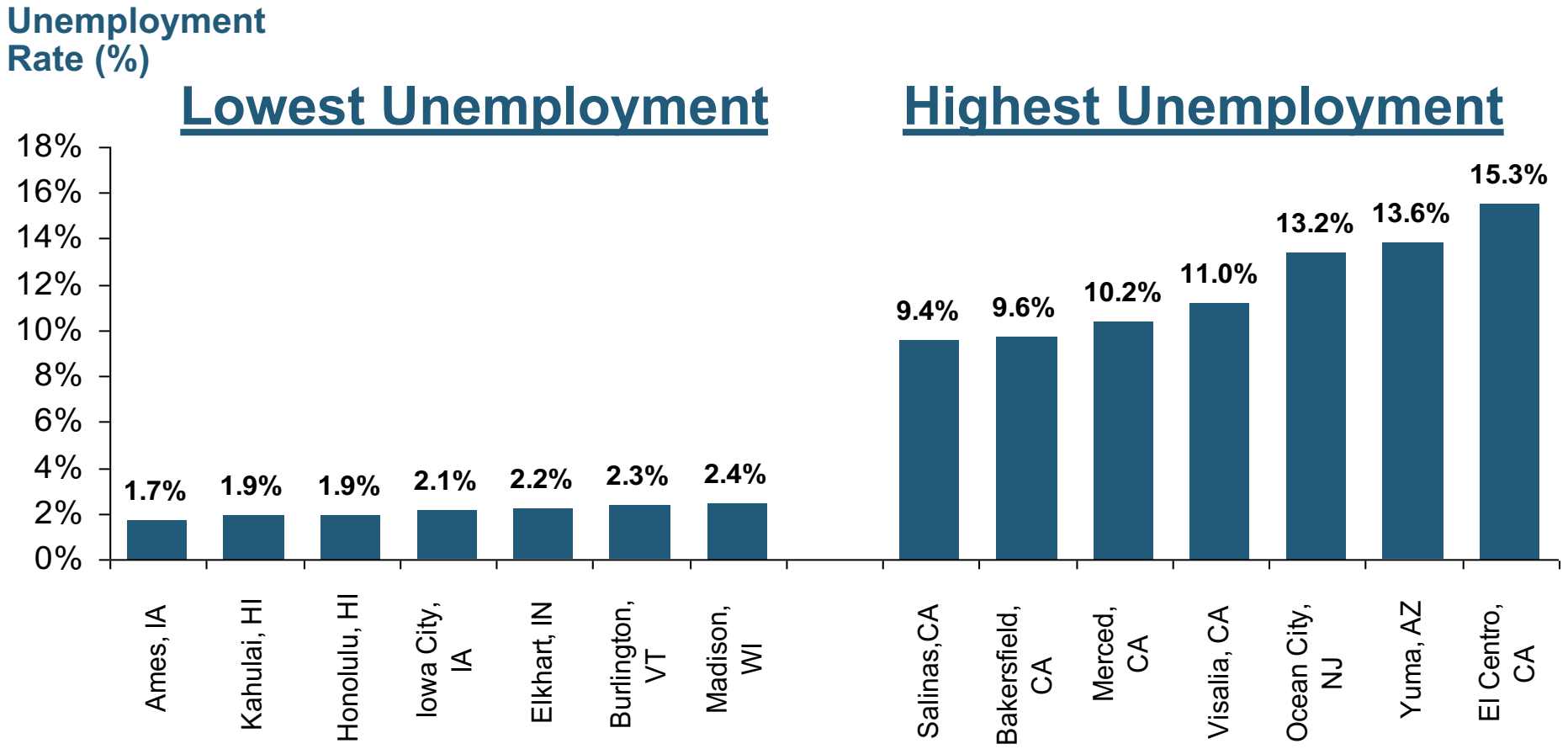
Lowest unemployment rates are found in northern New England, upper Midwest and northern plains—and Hawaii!

At 1.9% in March, Hawaii had the lowest unemployment rate in the US

At 7.3%, unemployment is the highest in the country

Source: US Bureau of Labor Statistics; Center for Risk and Uncertainty Management, University of South Carolina.

Extremes in Metro Area Unemployment Rates: March 2018



Gradual improvements in the US labor market over the past 9 years have created millions of jobs, but pockets of despair remain

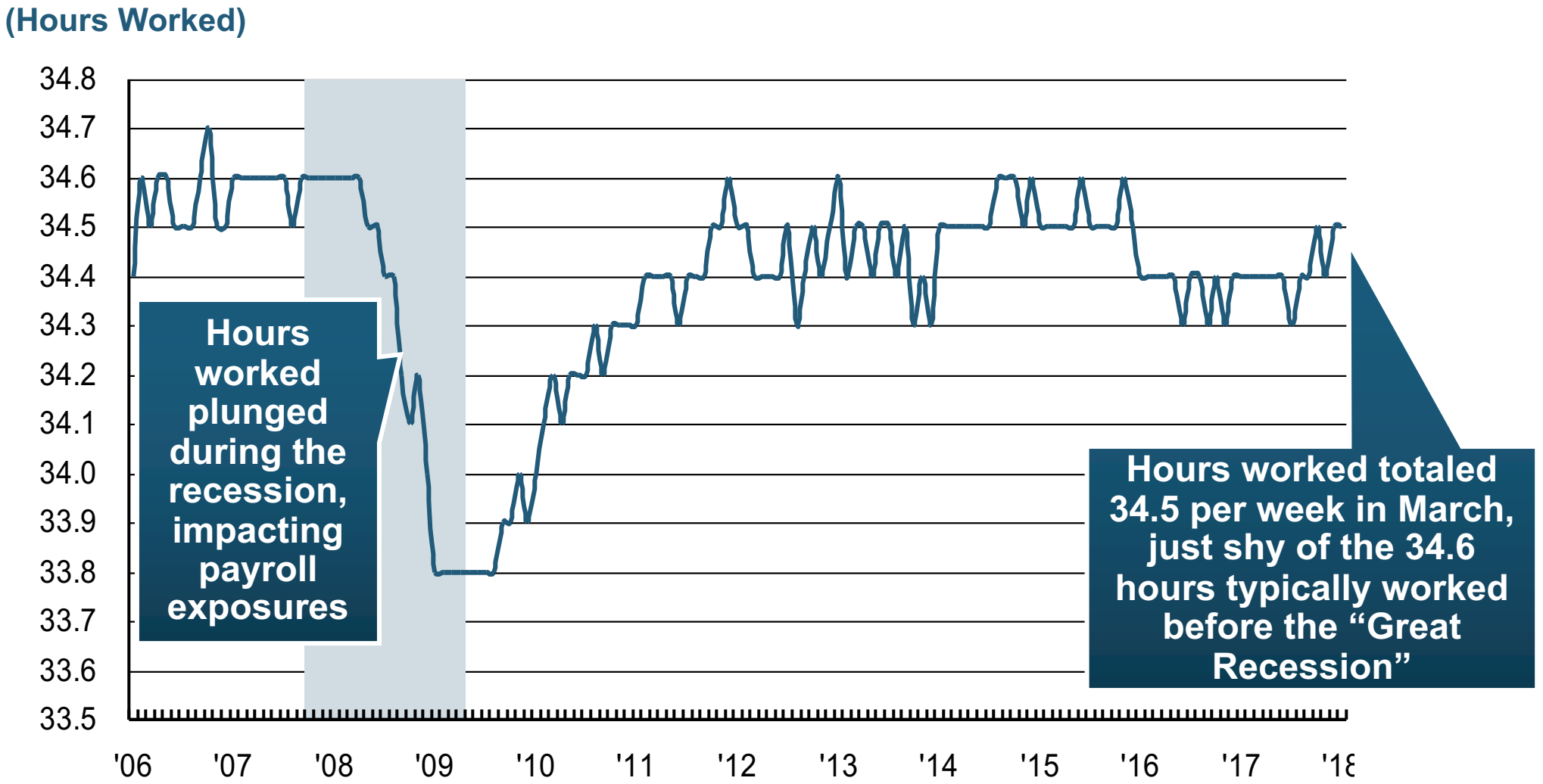
Source: US Bureau of Labor Statistics; Center for Risk and Uncertainty Management, University of South Carolina.

POSITIVE LABOR MARKET DEVELOPMENTS

Key Factors Driving Workers Compensation Exposure

22

Average Weekly Hours of All Private Workers, March 2006—March 2018*

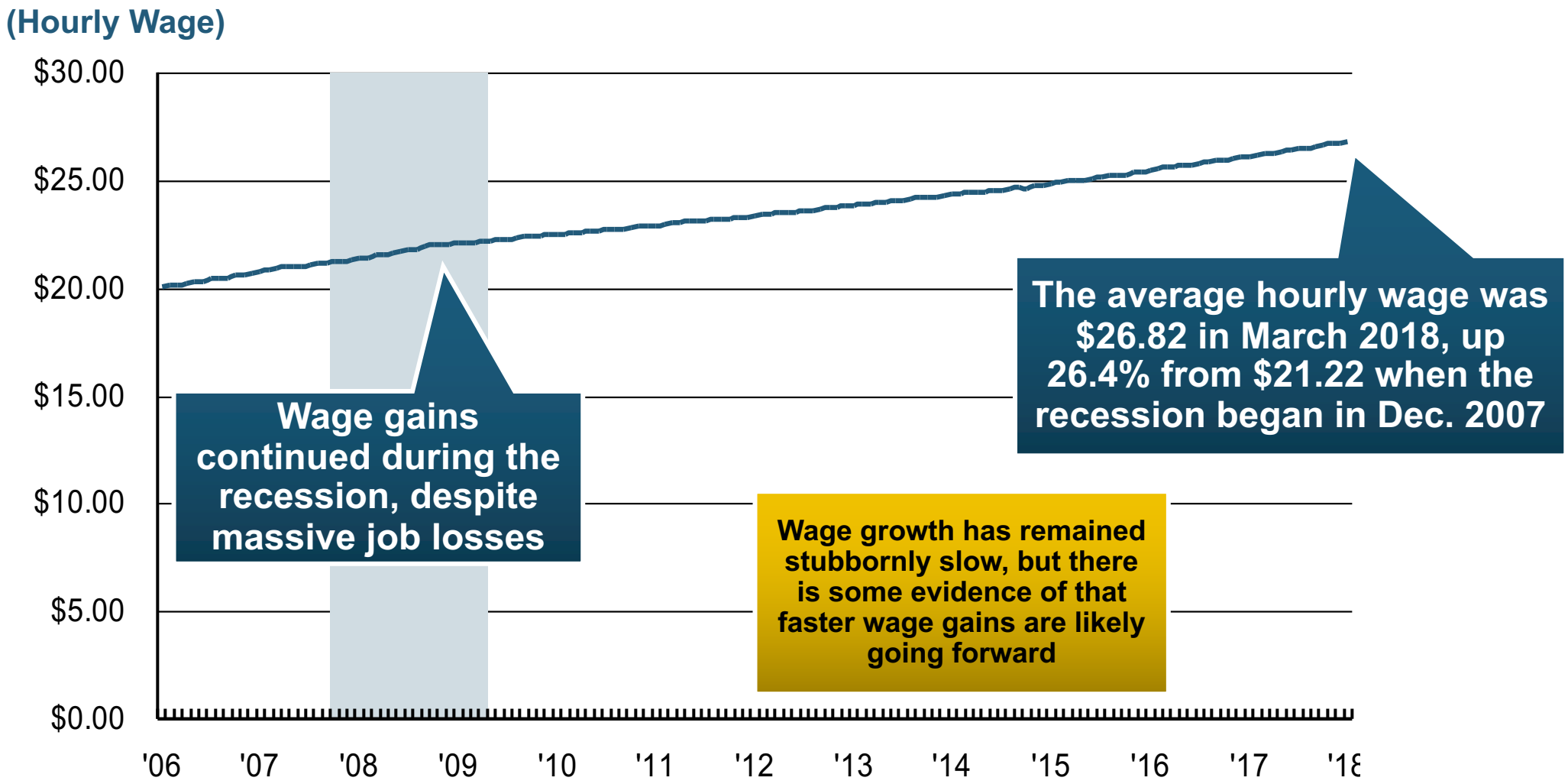


*Seasonally adjusted

Note: Recessions indicated by gray shaded columns.

Sources: US Bureau of Labor Statistics at http://www.bls.gov/data/#employment; National Bureau of Economic Research (recession dates); Center for Risk and Uncertainty Management, University of South Carolina.

Average Hourly Wage of All Private Workers, March 2006—March 2018*

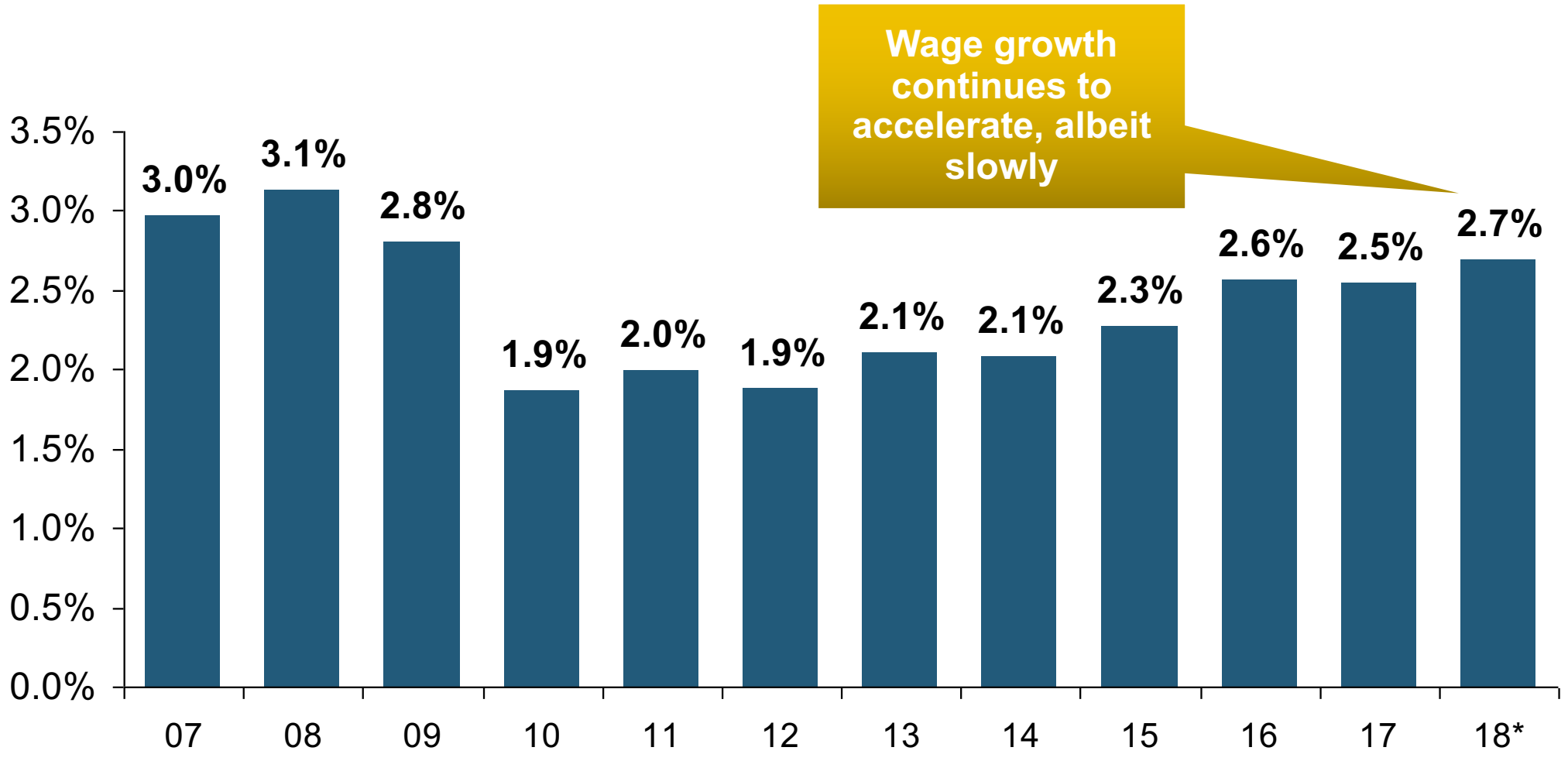


*Seasonally adjusted

Note: Recessions indicated by gray shaded columns.

Sources: US Bureau of Labor Statistics at http://www.bls.gov/data/#employment; National Bureau of Economic Research (recession dates); Insurance Information Institute.

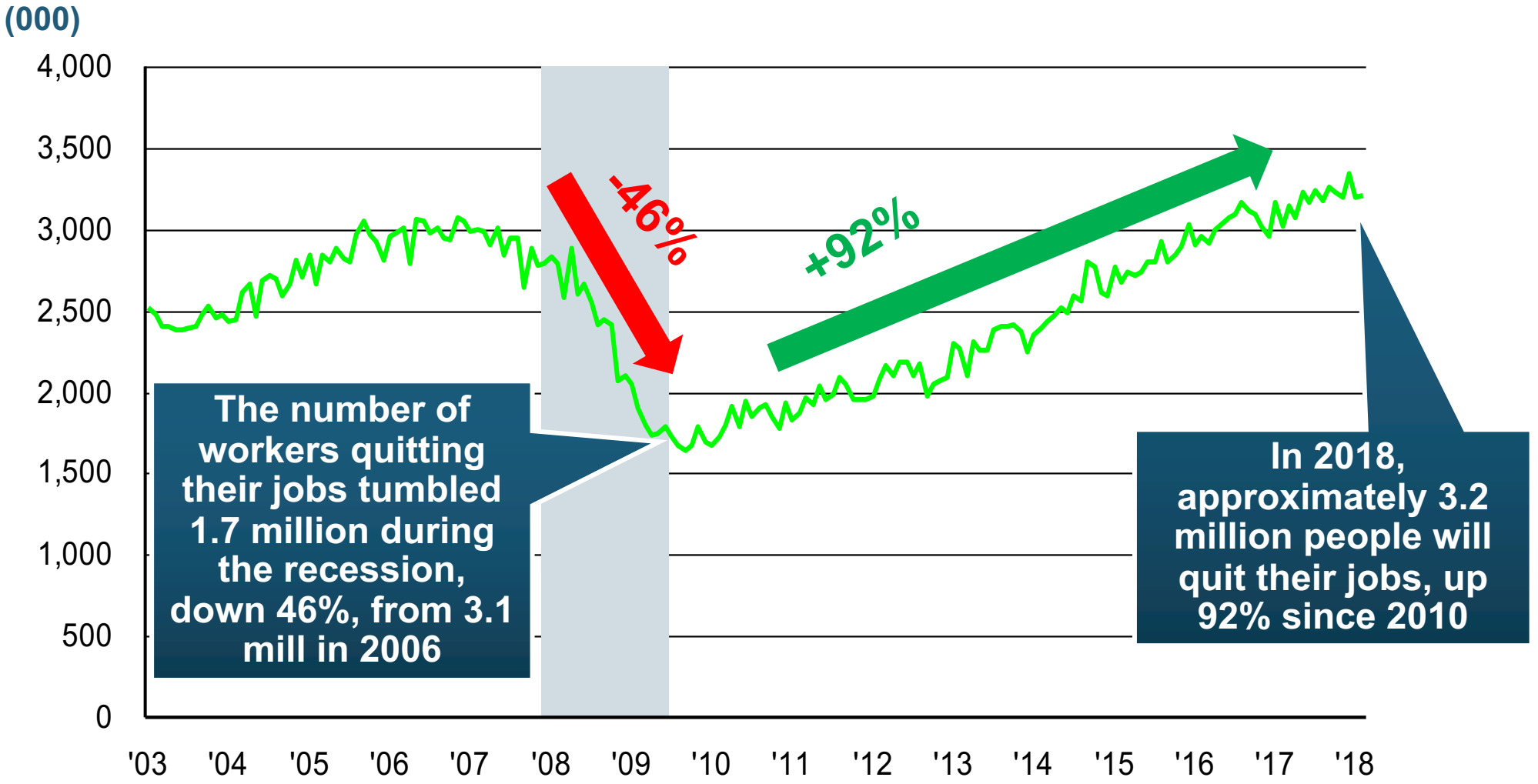
Annual Change in Average Hourly Wage, 2007–2018*



*Annual figures calculated from monthly seasonally adjusted data. 2018 data through February.

Sources: US Bureau of Labor Statistics at http://www.bls.gov/data/#employment; National Bureau of Economic Research (recession dates); Risk and Uncertainty Management Center, Univ. of South Carolina.

Take This Job And…
Number of Quits, Jan. 2003—Feb. 2018*

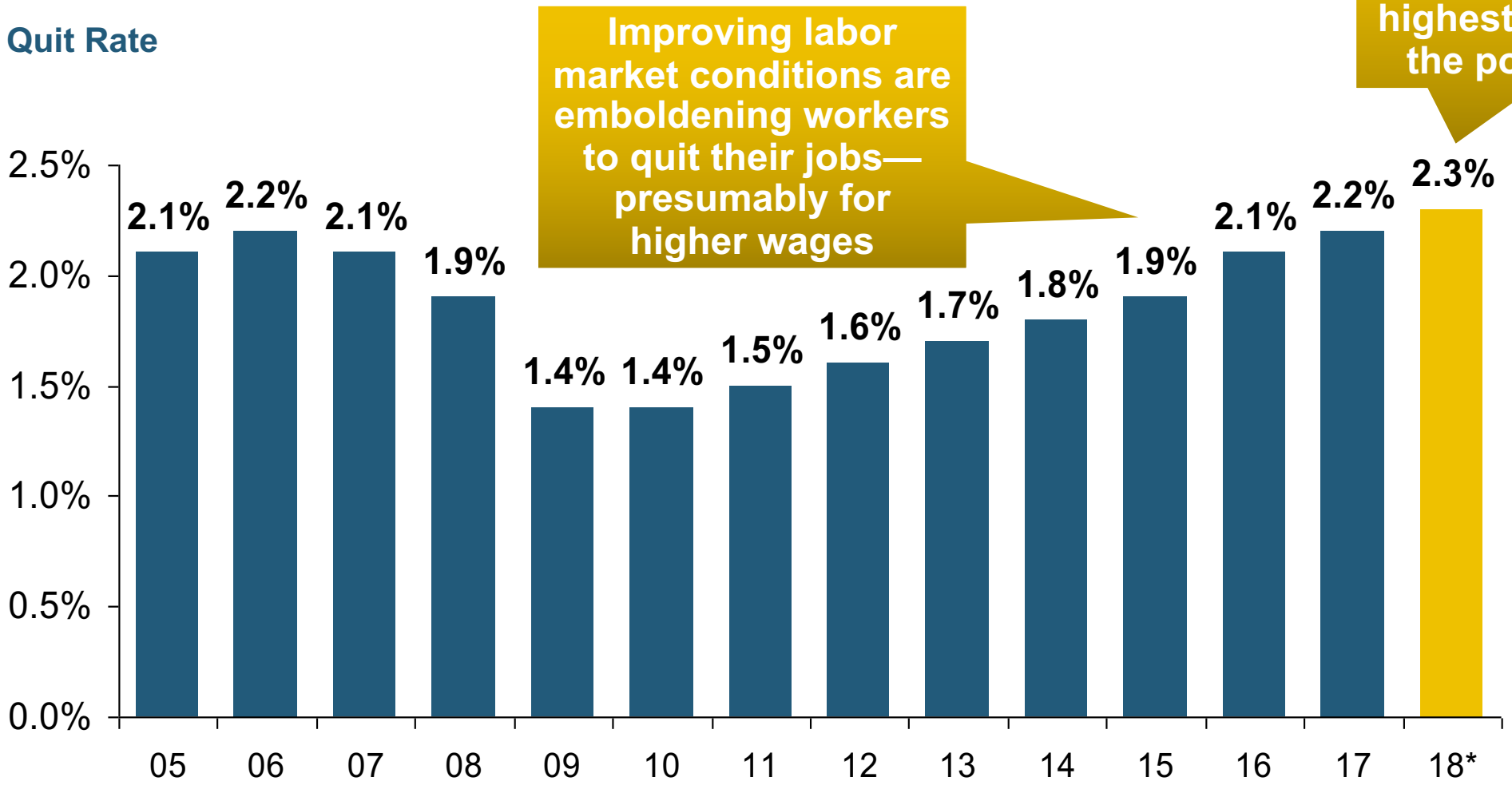


*Seasonally adjusted

Note: Recessions indicated by gray shaded columns.

Sources: US Bureau of Labor Statistics JOLTS survey: at http://www.bls.gov/jlt/; National Bureau of Economic Research (recession dates); Center for Risk and Uncertainty Management, University of South Carolina.

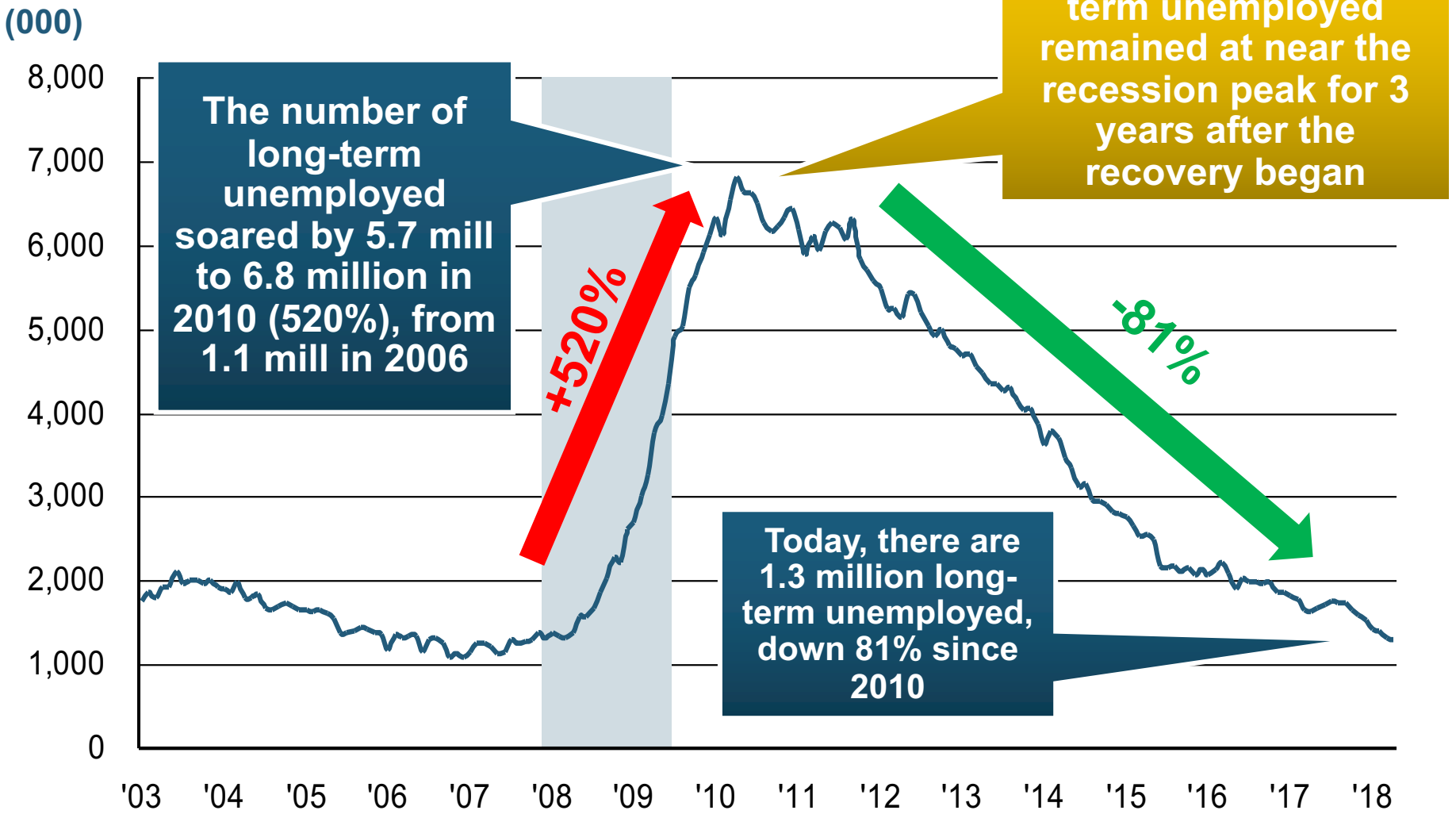
Take This Job And…Quit It!
Quit Rate, 2005–2018*



*Annual figures calculated from month seasonally adjusted data. 2018 figure through March.

Sources: US Bureau of Labor Statistics JOLTS Survey at https://www.bls.gov/jlt/ ; Risk and Uncertainty Management Center, Univ. of South Carolina.

Long-Term Unemployed (27+ Weeks), Jan. 2003—Apr. 2018*

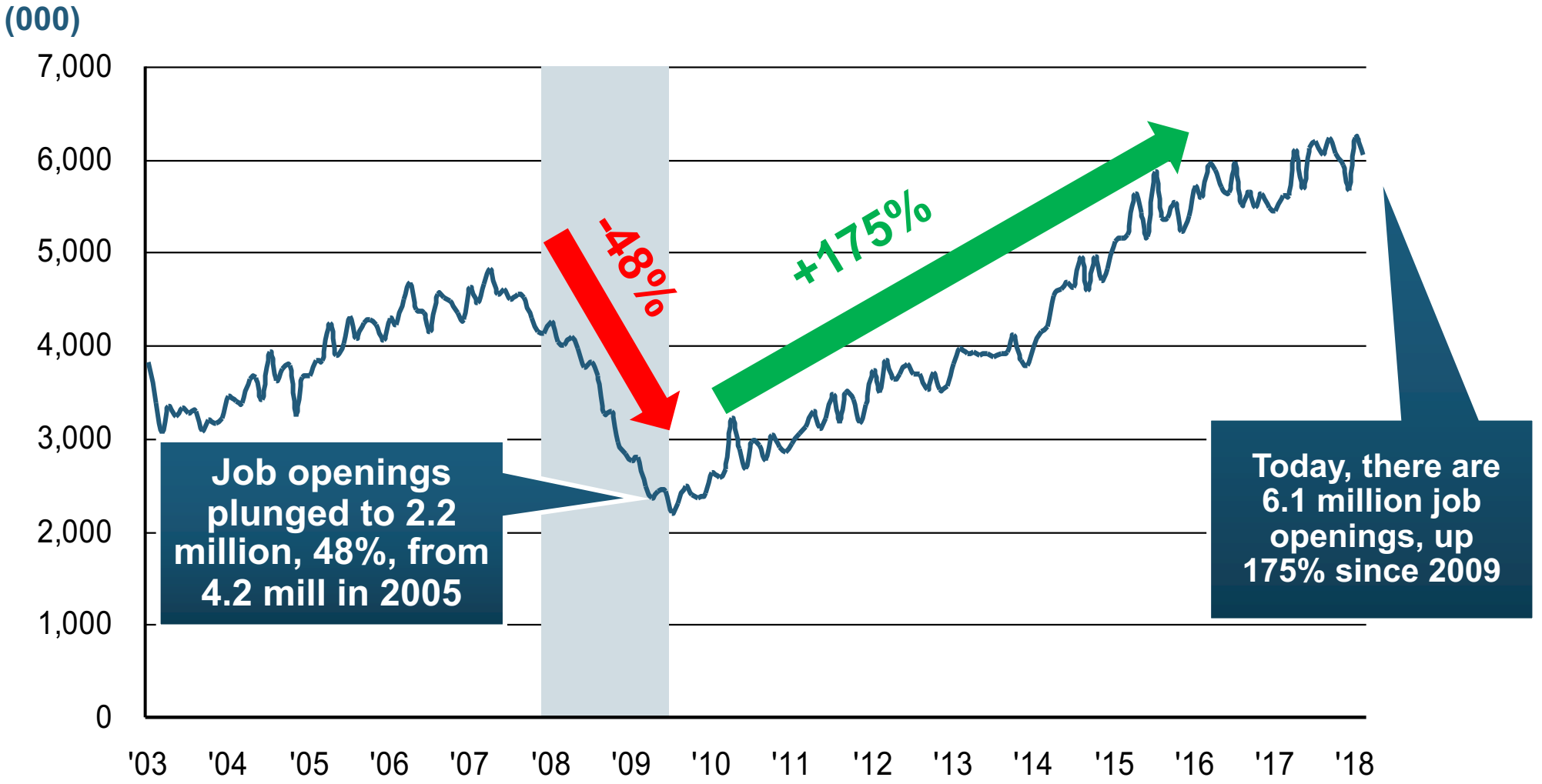


*Seasonally adjusted

Note: Recessions indicated by gray shaded columns.

Sources: US Bureau of Labor Statistics at http://www.bls.gov/; National Bureau of Economic Research (recession dates); Center for Risk and Uncertainty Management, University of South Carolina.

Help Wanted! Number of Job Openings, Jan. 2003—Feb. 2018*

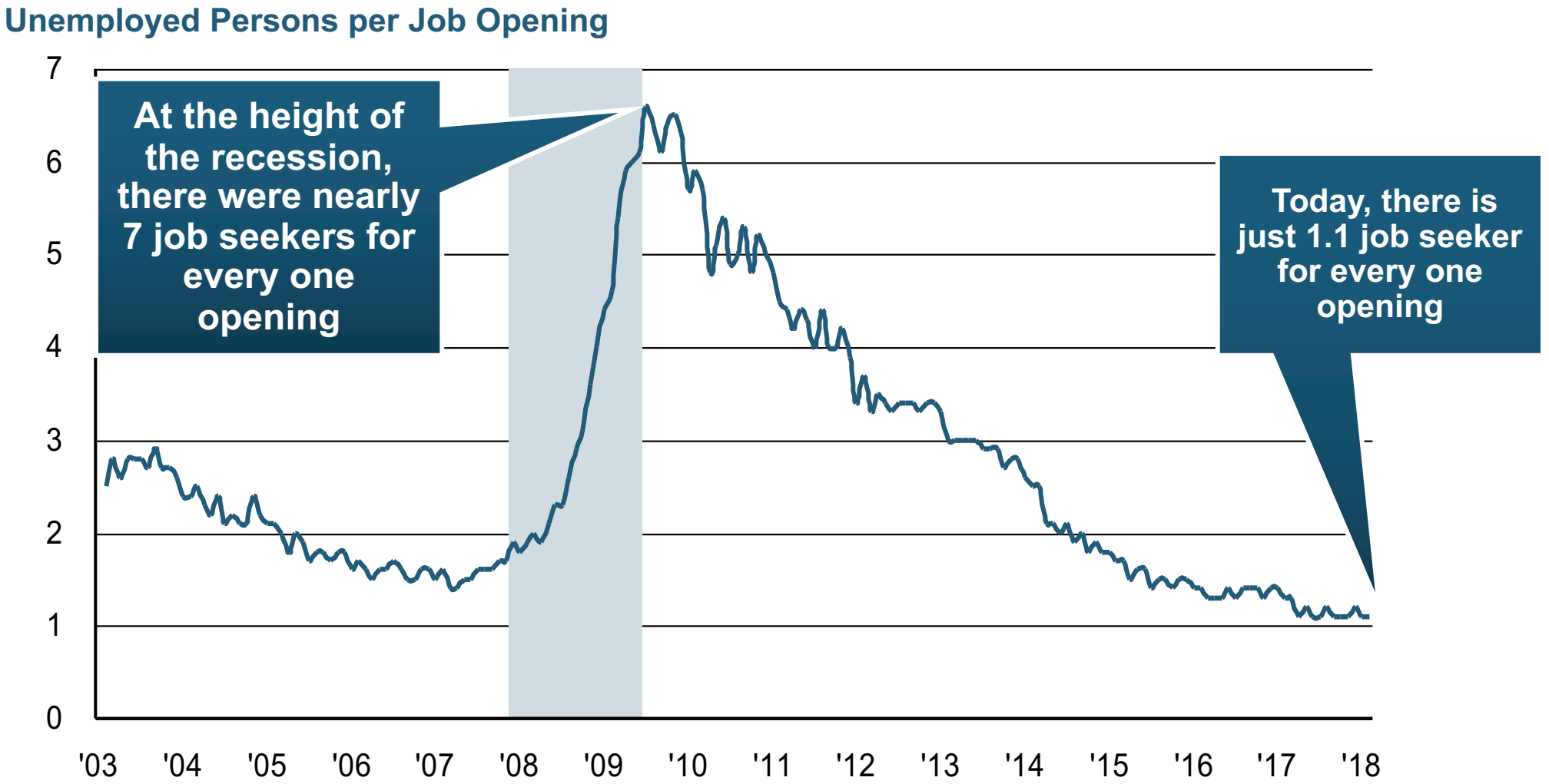


*Seasonally adjusted

Note: Recessions indicated by gray shaded columns.

Sources: US Bureau of Labor Statistics JOLTS survey: at http://www.bls.gov/jlt/; National Bureau of Economic Research (recession dates); Center for Risk and Uncertainty Management, University of South Carolina.

Number of Unemployed Persons per Job Opening, Feb. 2003—Feb. 2018*

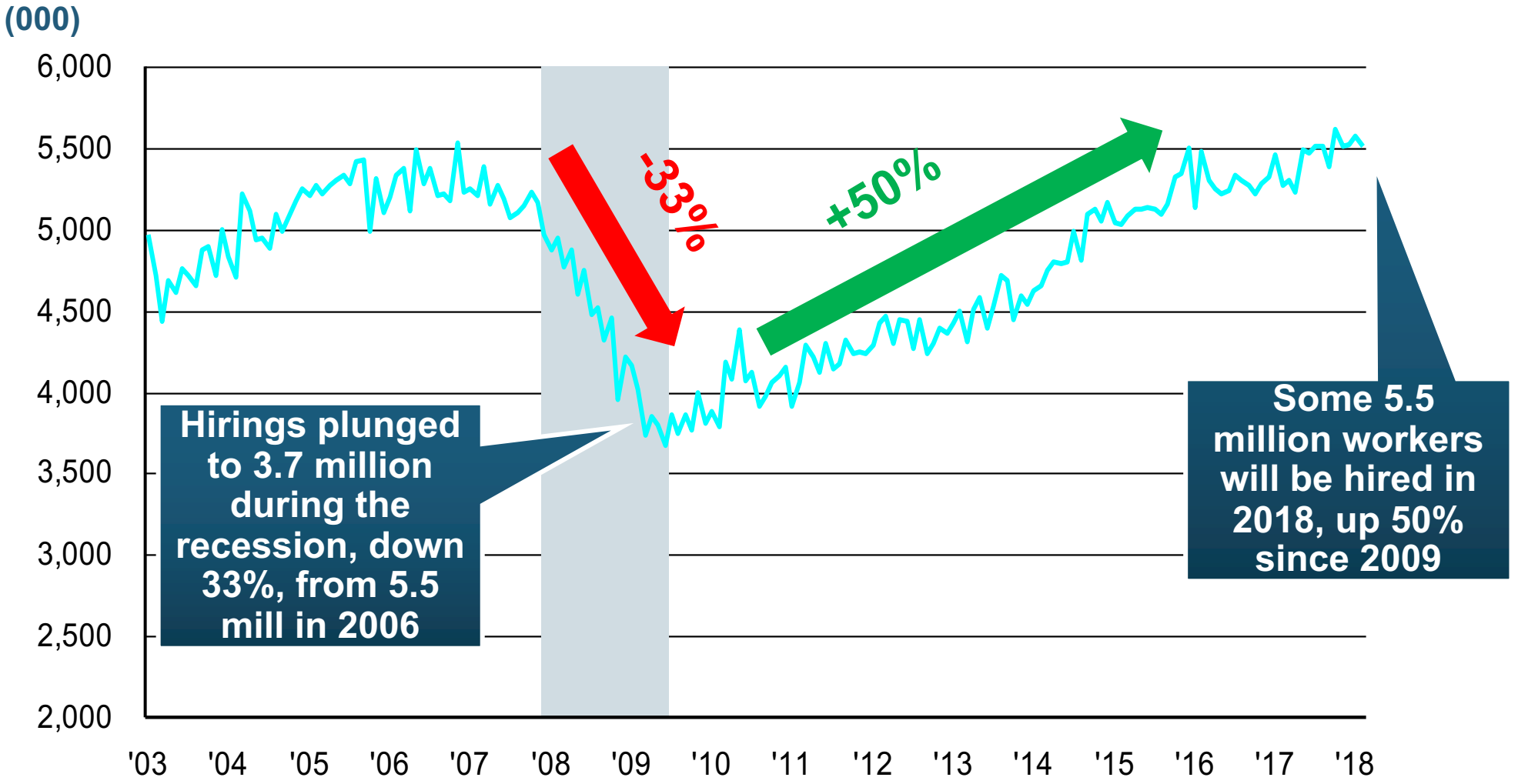


*Seasonally adjusted

Note: Recessions indicated by gray shaded columns.

Sources: US Bureau of Labor Statistics JOLTS survey: at http://www.bls.gov/jlt/; National Bureau of Economic Research (recession dates); Center for Risk and Uncertainty Management, University of South Carolina.

You're Hired!
Number of Hires, Jan. 2003—Feb. 2018*

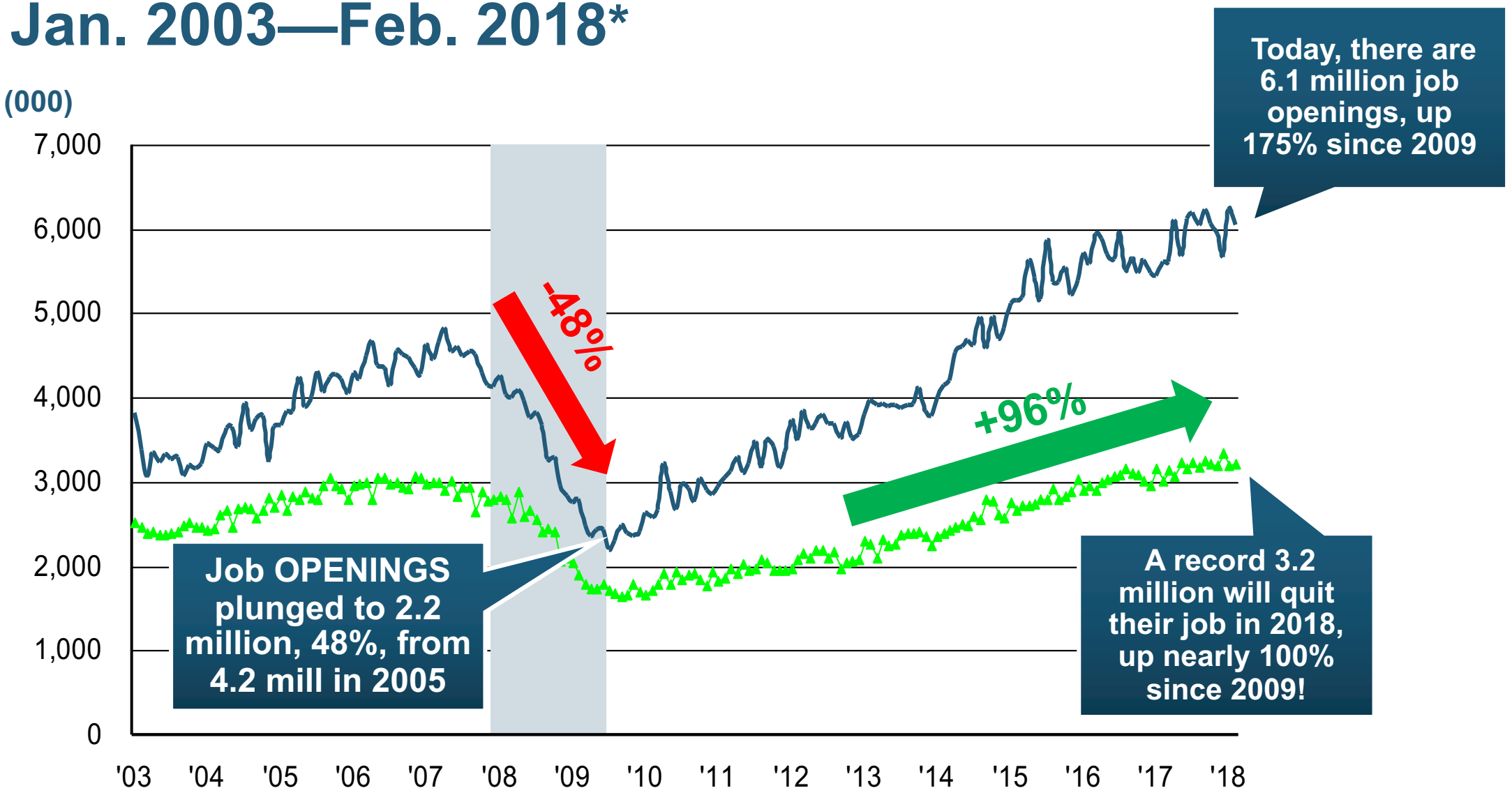


*Seasonally adjusted

Note: Recessions indicated by gray shaded columns.

Sources: US Bureau of Labor Statistics JOLTS survey: at http://www.bls.gov/jlt/; National Bureau of Economic Research (recession dates); Center for Risk and Uncertainty Management, University of South Carolina.

Number of Job Openings vs. Quits, Jan. 2003—Feb. 2018*

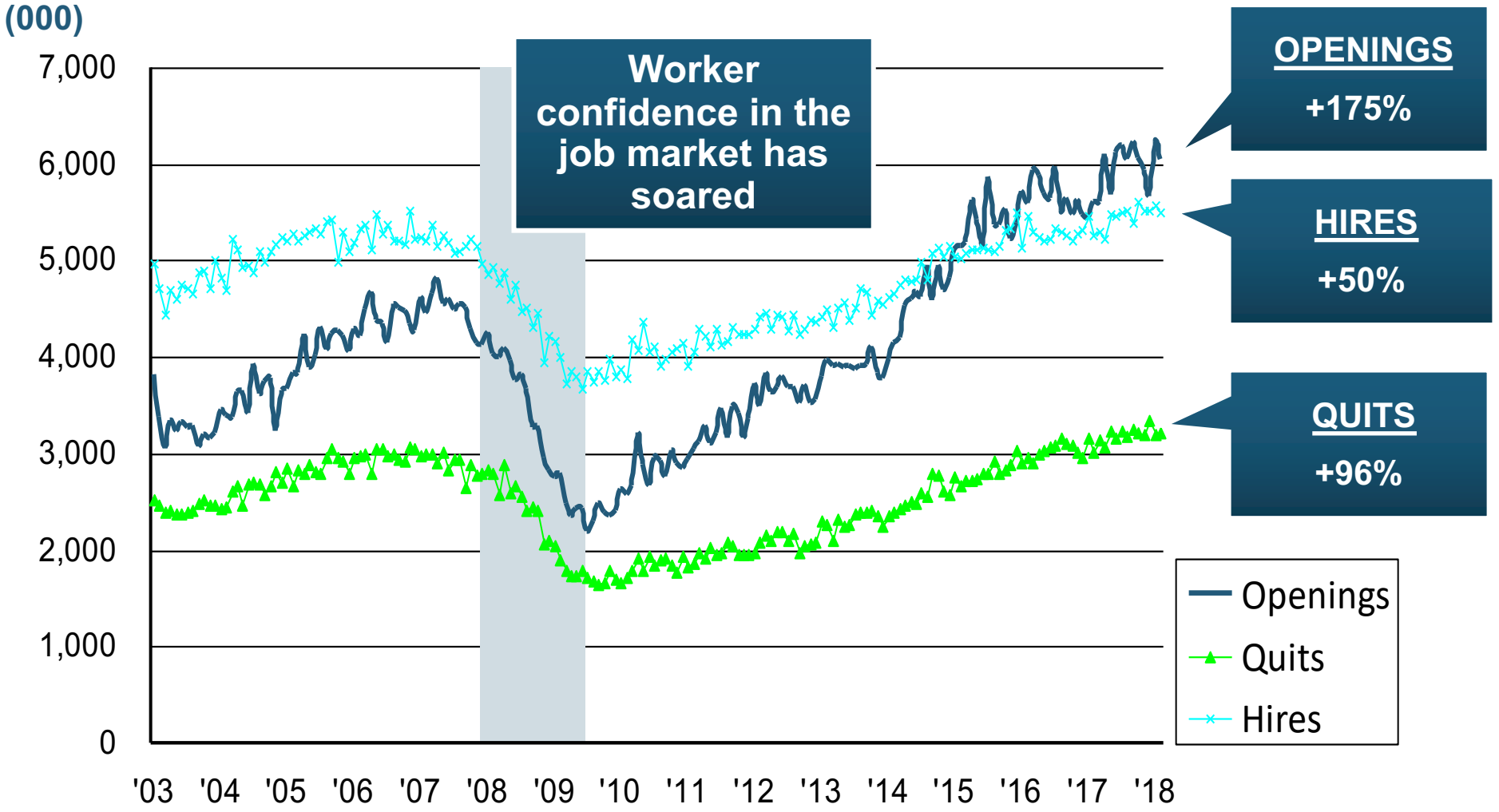


*Seasonally adjusted

Note: Recessions indicated by gray shaded columns.

Sources: US Bureau of Labor Statistics JOLTS survey: at http://www.bls.gov/jlt/; National Bureau of Economic Research (recession dates); Insurance Information Institute.

Number of Job Openings, Hires and Quits, Jan. 2003—Feb. 2018*



*Seasonally adjusted

Note: Recessions indicated by gray shaded columns.

Sources: US Bureau of Labor Statistics JOLTS survey: at http://www.bls.gov/jlt/; National Bureau of Economic Research (recession dates); Center for Risk and Uncertainty Management, University of South Carolina.

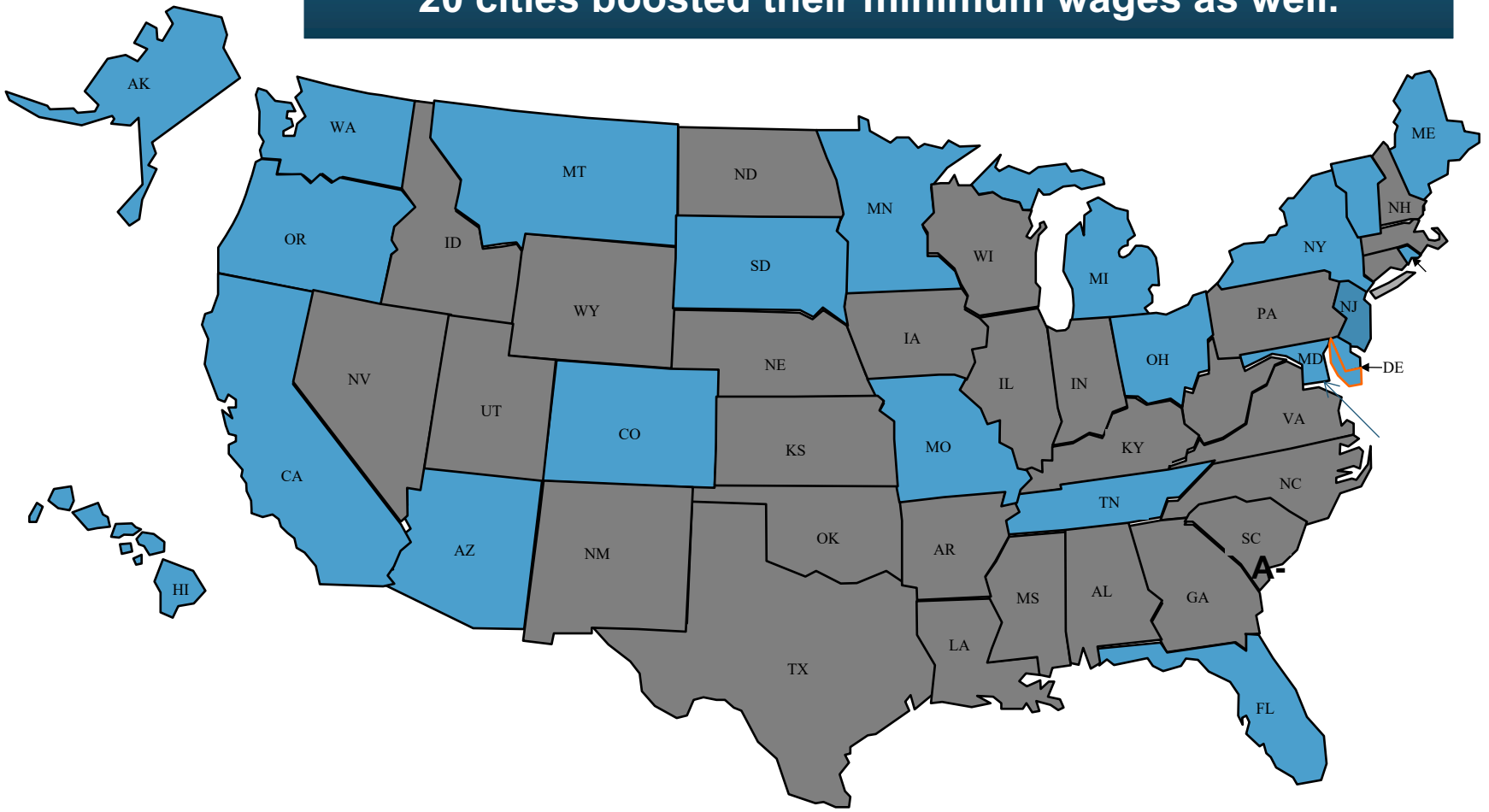
DOES THE MINIMUM WAGE MATTER FOR WORKERS COMPENSATION?

Yes, and Increasingly So!

34

States Increasing Their Minimum Wage in 2018: Fuels WC Exposure

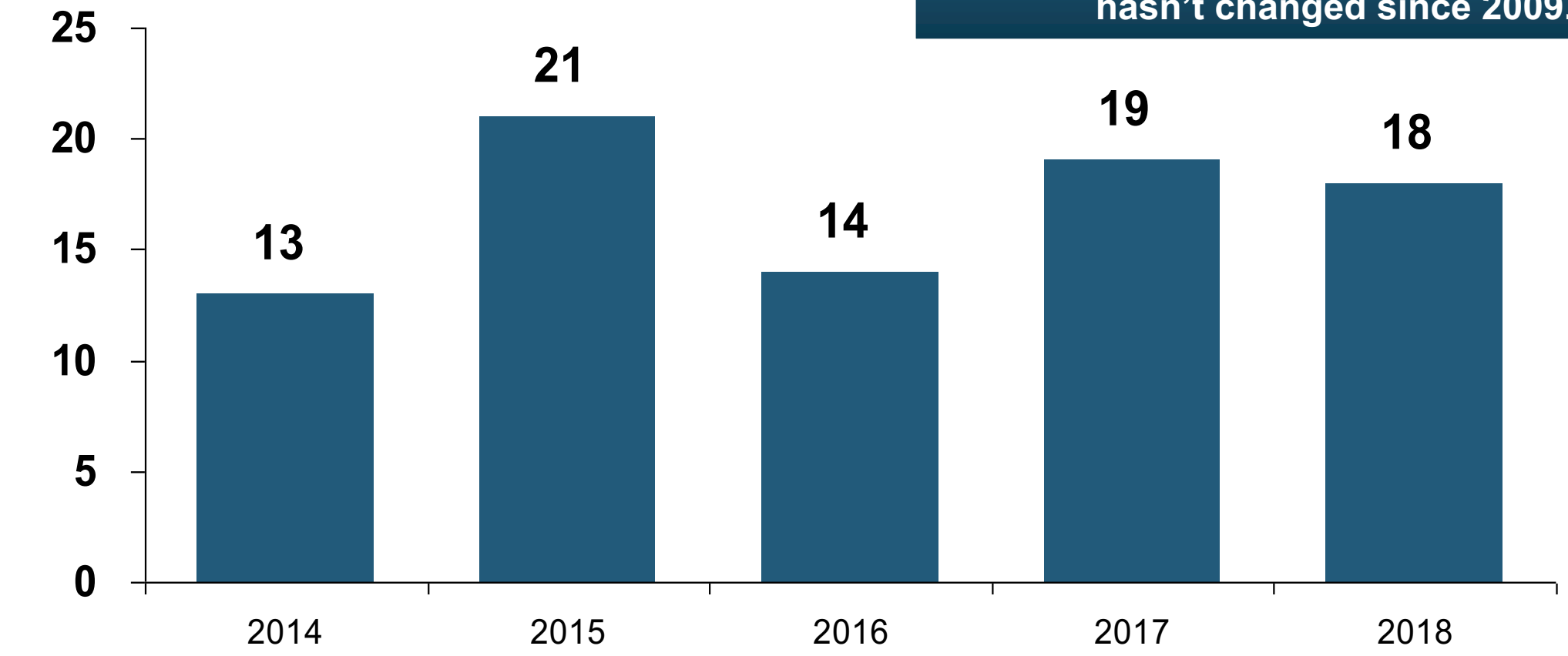
18 states increased their minimum wage in 2018, adding $5 billion in wages to 4.5 million workers. Approximately 20 cities boosted their minimum wages as well.



Source: Economic Policy Institute, *Economic Snapshot*, Dec. 21, 2017.

Number of States Increasing their Minimum Wage, 2014 – 2018

Minimum wage increases by states, cities and counties have added tens of billions of dollars to the WC exposure base in recent years. The federal minimum wage of $7.25 hasn't changed since 2009.



Sources: Economic Policy Institute, BusinessInsider.com, USA Today; Risk and Uncertainty Management Center, Univ. of South Carolina.

The Minimum Wage and Workers Comp

- In 2017, 80.4 million workers age 16+ were paid on an hourly basis, representing 58.3% of all wage and salary workers (BLS)
- Of those paid by the hour, 542,000 earned the prevailing federal minimum wage of $7.25 (down from 701,000 in 2016) and 1.8 million made less than the federal minimum (up from 1.5 million in 2016)
- These workers account for 2.3% of the labor force, down from 2.7% in 2016 and 3.3% in 2015
- This suggests that large numbers of workers are benefiting from minimum wage increases
- Tens of billions of new WC payroll exposure added

ADVERSE LONG-TERM LABOR MARKET DEVELOPMENTS

Key Factors Harming Workers Compensation Exposure and the Overall Economy

38

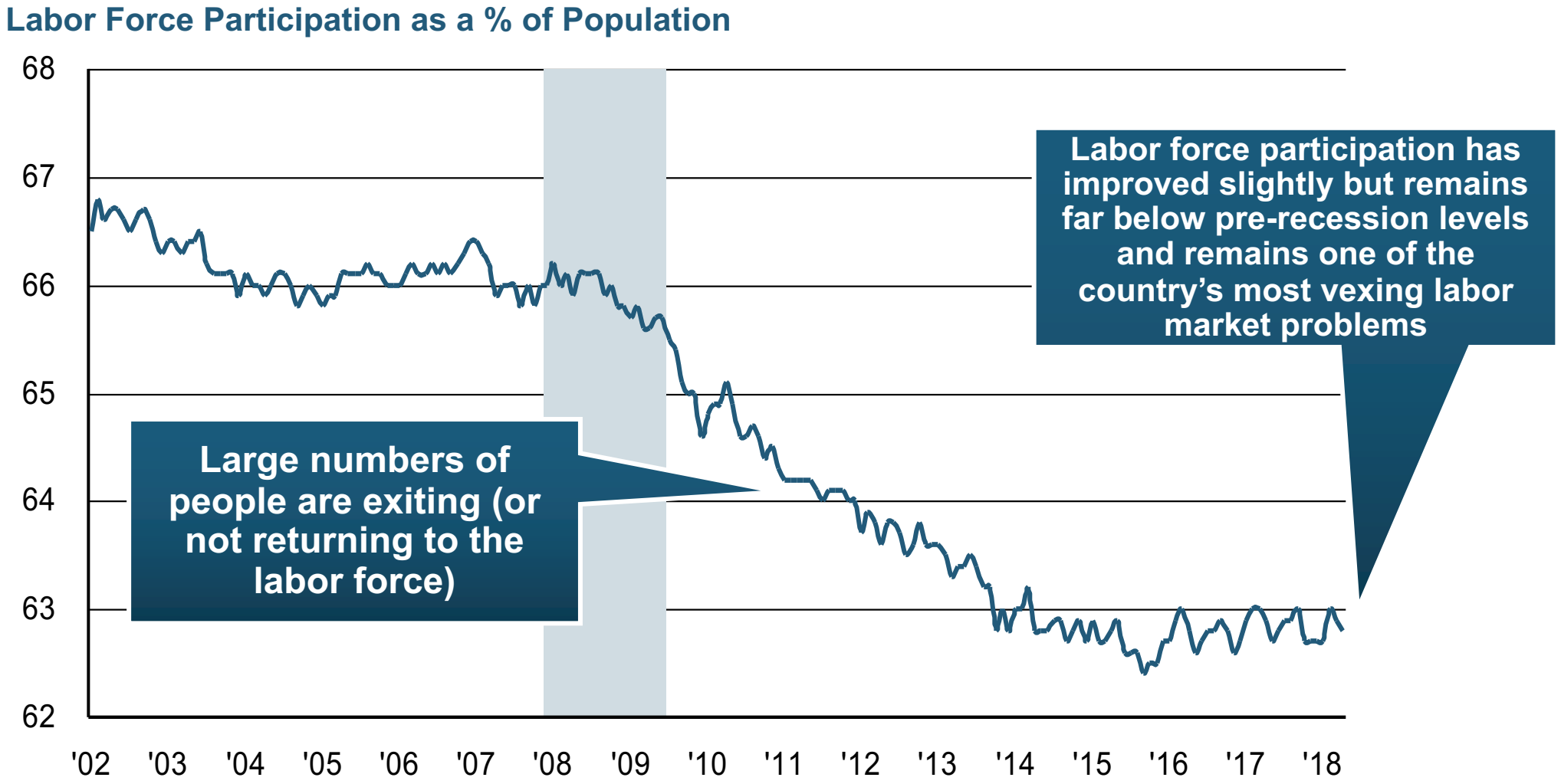
Number of "Discouraged Workers," Jan. 2002—April 2018

In recent good times, the number of discouraged workers ranged from 200,000-400,000 (1995-2000) or from 300,000-500,000 (2002-2007).

Notes: Recessions indicated by gray shaded columns. Data are seasonally adjusted.

Sources: Bureau of Labor Statistics http://www.bls.gov/news.release/empsit.a.htm ; NBER (recession dates); Center for Risk and Uncertainty Management, University of South Carolina.

Labor Force Participation Rate, Jan. 2002—April 2018*

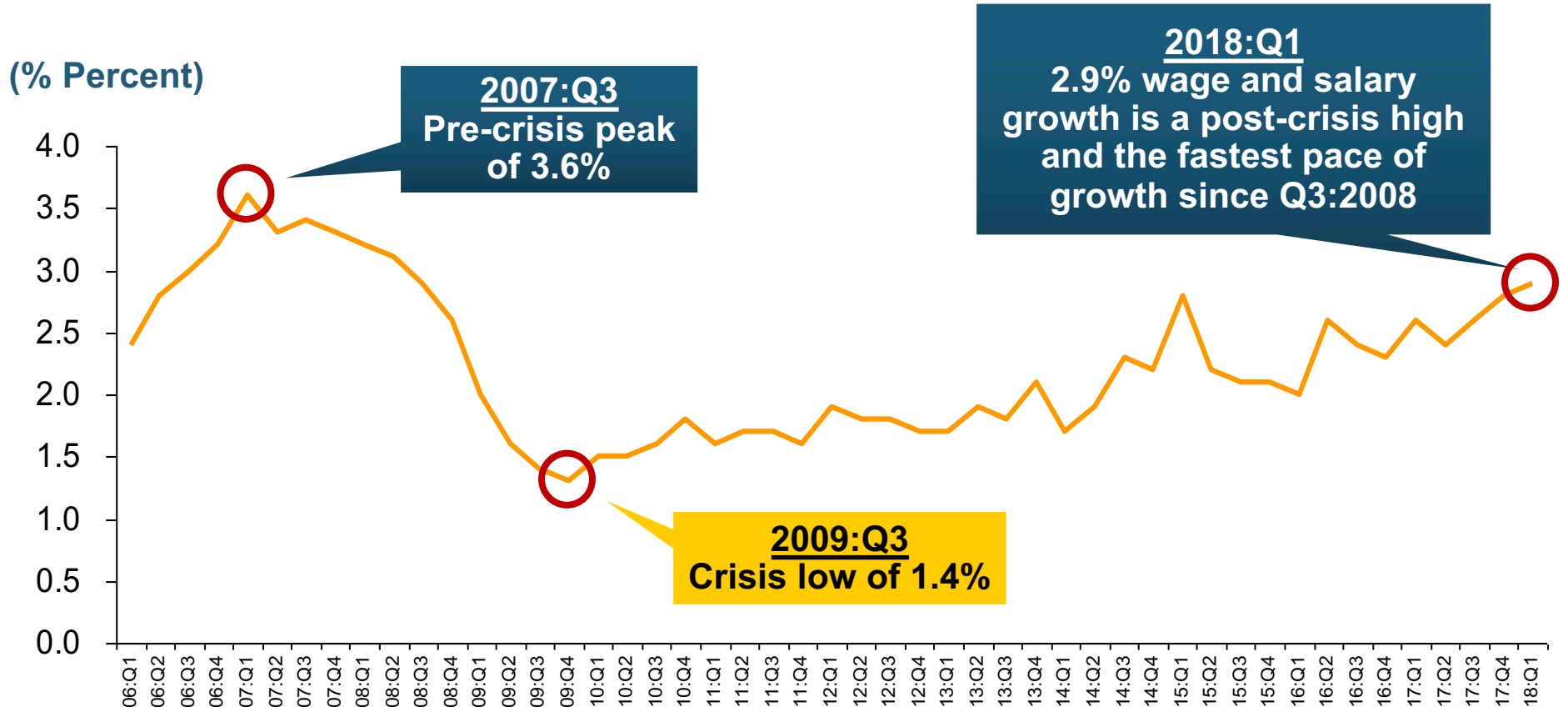


*Defined as the percentage of working age persons in the population who are employed or actively seeking work.

Note: Recessions indicated by gray shaded columns.

Sources: US Bureau of Labor Statistics at http://www.bls.gov/data/; National Bureau of Economic Research (recession dates); Center for Risk and Uncertainty Management, University of South Carolina.

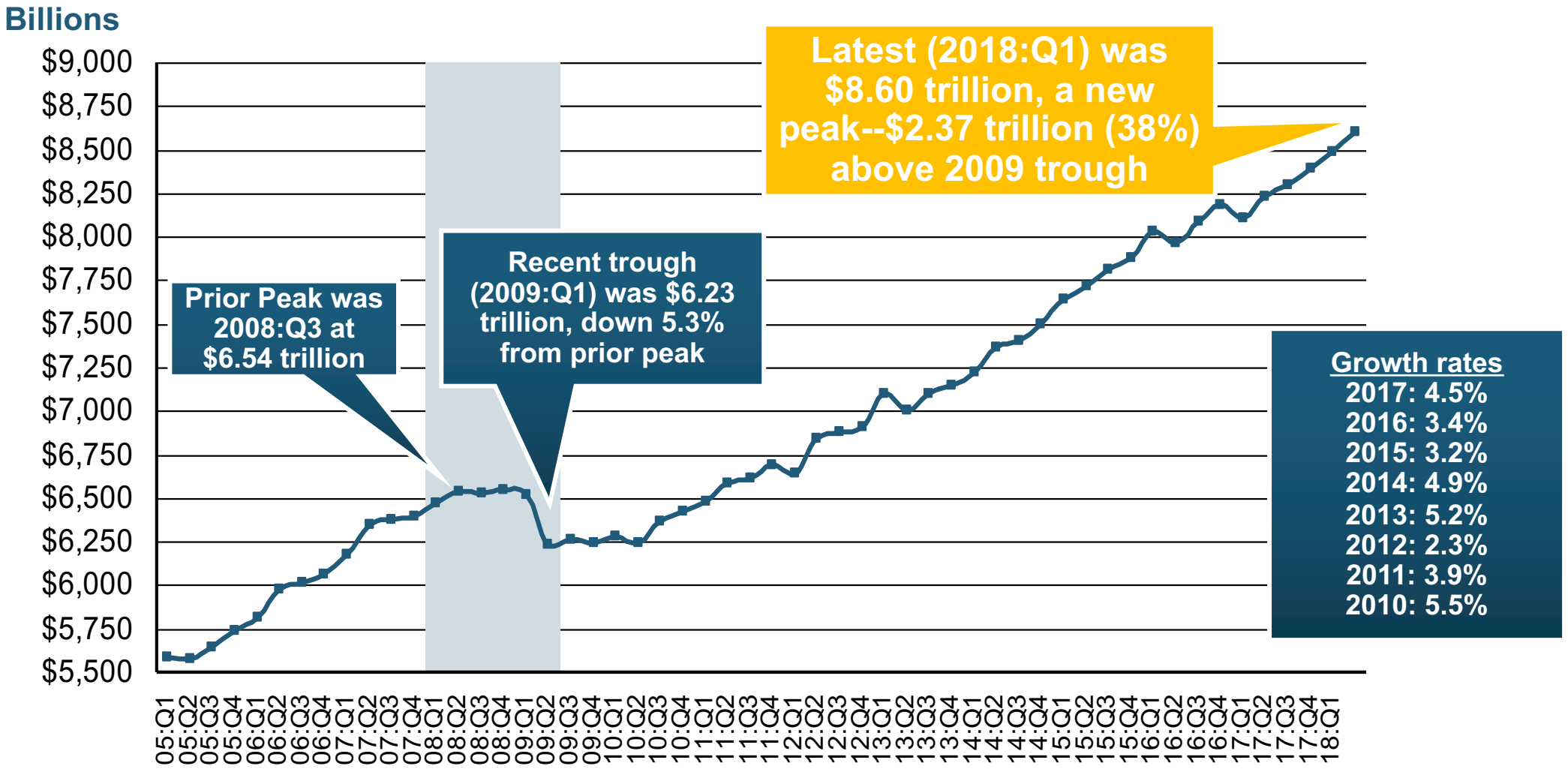
Wage and Salary Growth for Private Sector Workers, 2006:Q1–2018:Q1*



The recovery in wage and salary growth is nearly 9 years old—and remains incomplete. This is a major factor holding back payroll exposure and premium growth in WC.

*Seasonally adjusted.
Sources: US Bureau of Labor Statistic.

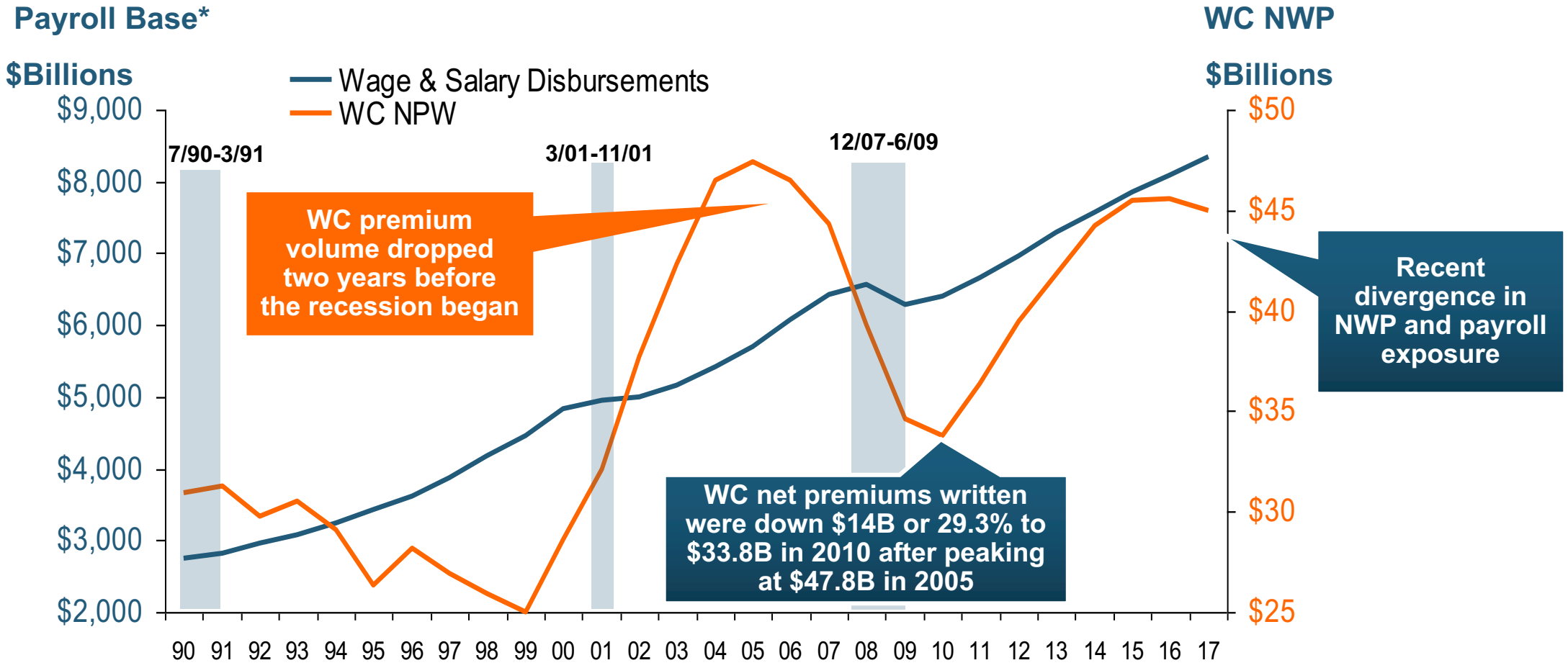
Nonfarm Payroll (Wages and Salaries): Quarterly, 2005–2018:Q1



Note: Recession indicated by gray shaded column. Data are seasonally adjusted annual rates.
Sources: http://research.stlouisfed.org/fred2/series/WASCUR; National Bureau of Economic Research (recession dates).

42

Payroll vs. Workers Comp Net Written Premiums, 1990-2017



Continued payroll growth will benefit WC exposure growth, but falling rates will adversely impact growth in Net Written Premiums

*Private employment; Shaded areas indicate recessions. WC premiums are from NCCI through 2017.
Sources: NBER (recessions); Federal Reserve Bank of St. Louis at http://research.stlouisfed.org/fred2/series/WASCUR.

Impacts of Tax Reform on the P/C Insurance Industry

The Tax Cuts and Jobs Act of 2017

Lower Corporate Tax Rate Benefits All Insurer, but Not Equally

44

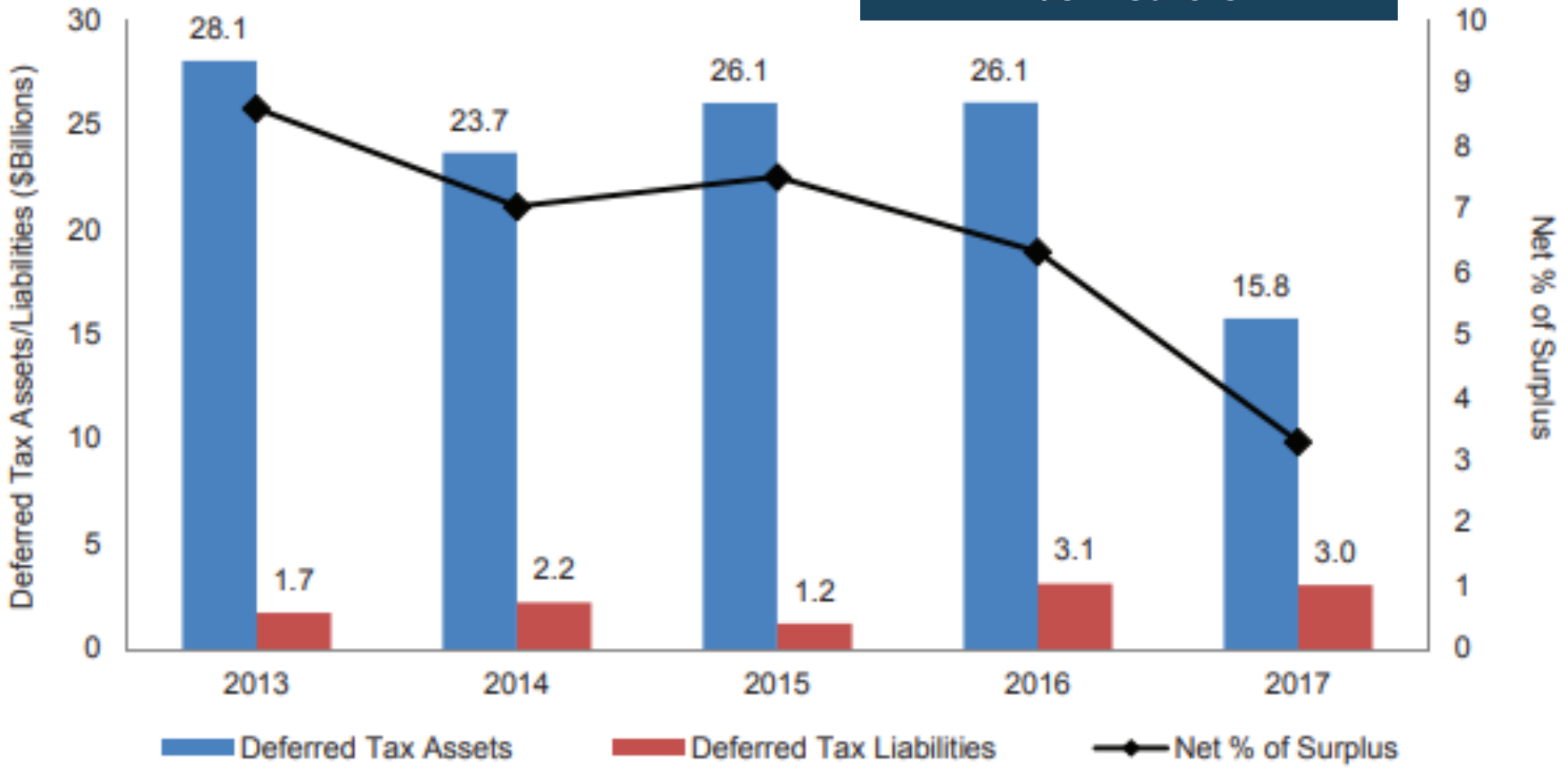
Tax Reform Implications for P/C Insurers and Reinsurers

- **Reduction of Corporate Tax Rate from 35% to 21%...**

- **All Insurers Benefit…But Not Equally**
  - Companies generating most of their profits from underwriting income previously taxed at 35% benefit the most
  - Write-downs of Deferred Tax Assets hurt some insurers
  - Companies generating proportionately more of their Net Investment Income from (taxable) Corporate Bonds benefit more than companies with heavier muni holdings
    - In P/C industry, insurers with underwriting losses tend to hold proportionately more in corporates
  - **Base Erosion and Anti-Abuse Tax (BEAT): Leveling the Playing Field**
    - Domestic (re)insurers previously taxed at 35% will benefit relative to (re)insurers domiciled in Bermuda, etc.
    - Diminished advantage for foreign-owned insurers that cede premium offshore

Impact of Tax Cuts and Jobs Act on US P/C Publicly-Traded Insurers: Deferred Tax Assets and Liabilities

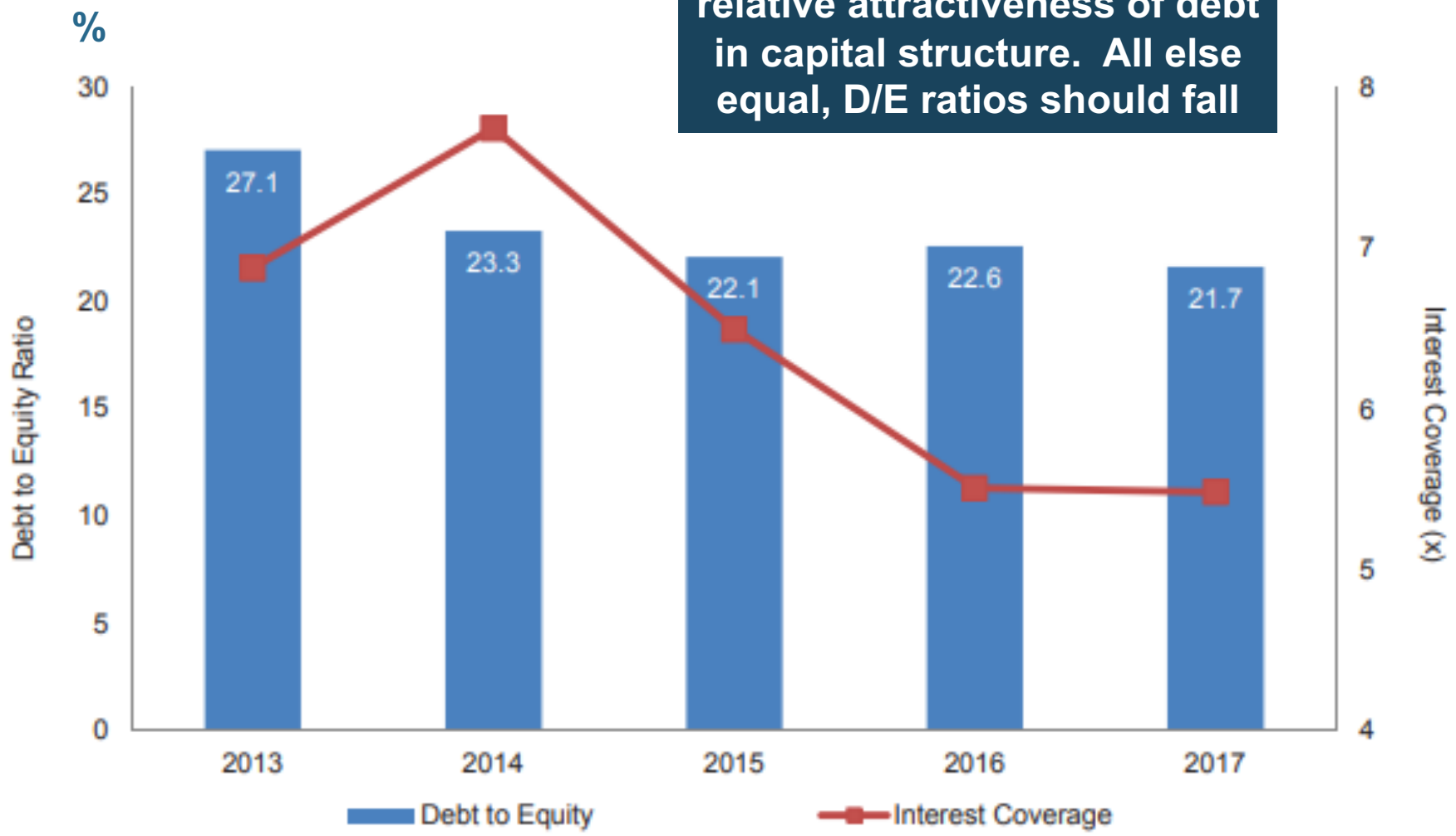
The reduction in corporate tax rates under the TCJA of 2017 reduced the value of DTAs by 39.5% for public P/C insurers



Source: A.M. Best, *Financial Review*, April 13, 2018.

US P/C Publicly-Traded Insurers: Debt Servicing Ability

TCJA of 2017 reduced relative attractiveness of debt in capital structure. All else equal, D/E ratios should fall

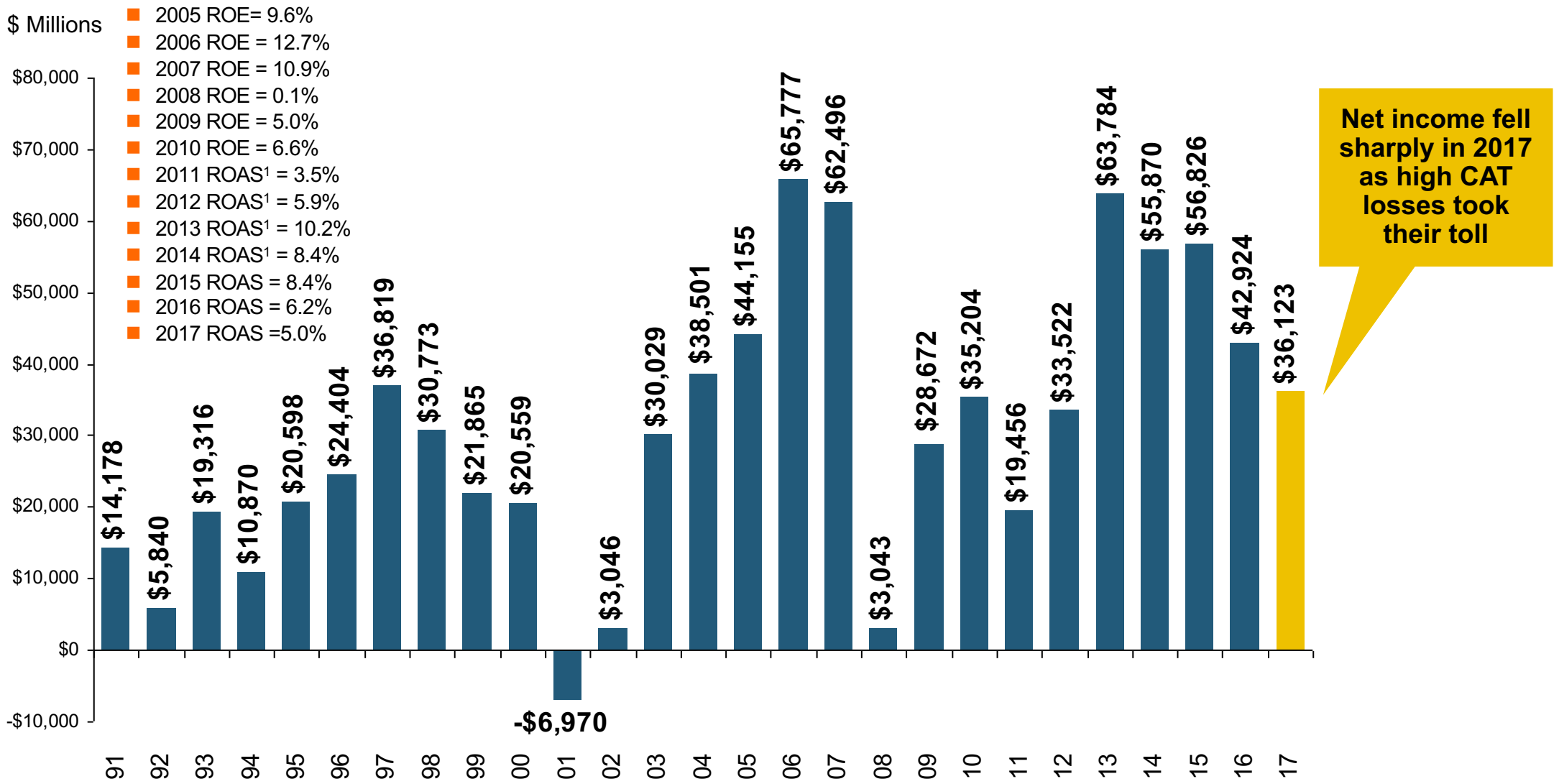


Source: A.M. Best, *Financial Review*, April 13, 2018.

Summary of Structural Changes to the Industry as the Result of Tax Reform

- **All Else Equal, Reduction in Corporate Tax Rate from 35% to 21% Should Enhance Profitability**
  - Public Companies: More share buybacks, higher dividends
  - DTA write-downs are a one-time hit
- **Decreases Attractiveness of Holding Muni Debt**
  - Expect muni share of bond portfolio to shrink modestly
- **Decreases Attractiveness of Issuing Debt**
  - Expect D/E ratios in insurer capital structures to fall; M&A excepted
- **Expect Diminished Cessions to Offshore Reinsurance Affiliates Due to Base Erosion and Anti-Abuse Tax (BEAT)**

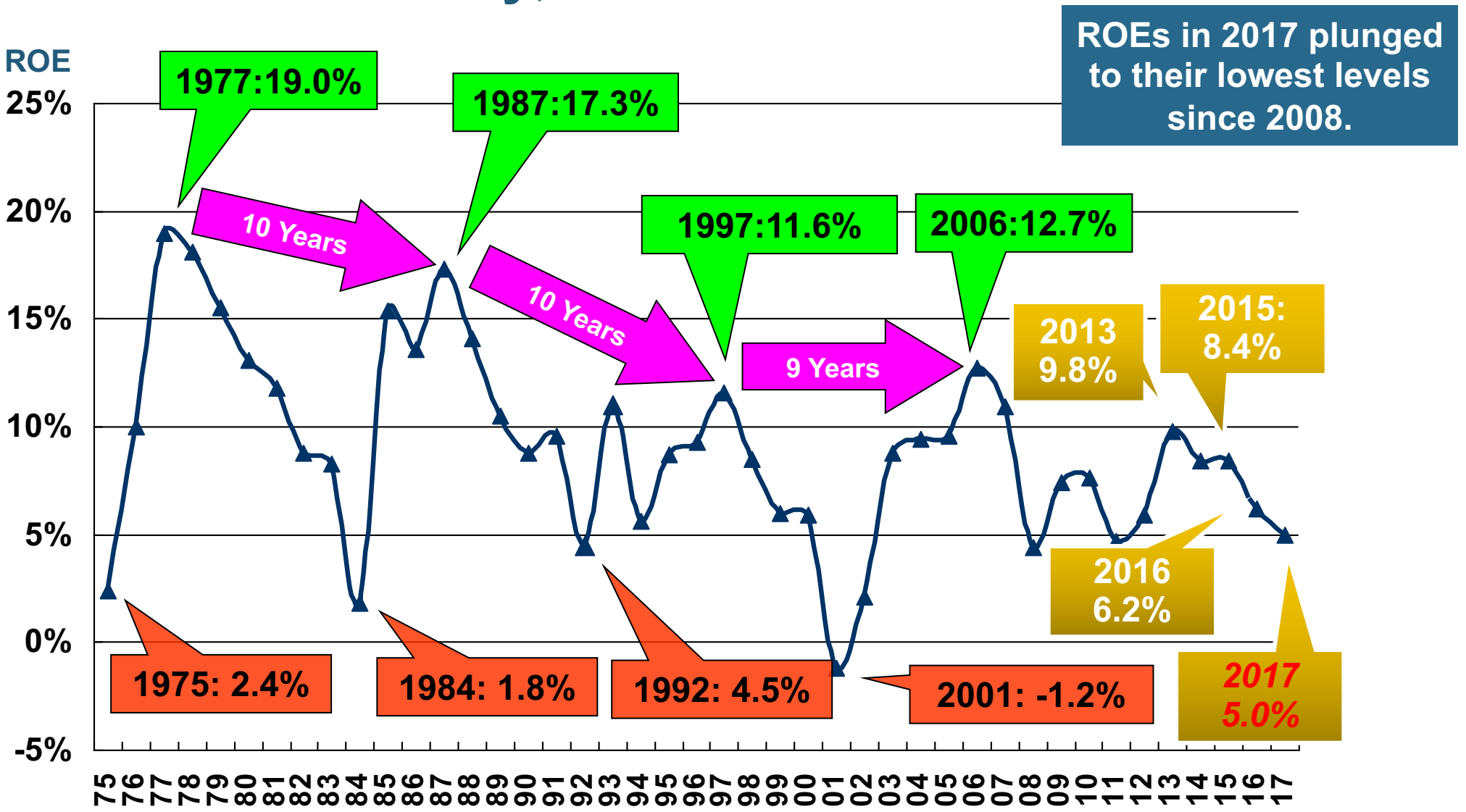
P/C Industry Net Income After Taxes 1991–2017



•ROE figures are GAAP; [1]Return on avg. surplus. Excluding Mortgage & Financial Guaranty insurers yields a 8.2% ROAS in 2014, 9.8% ROAS in 2013, 6.2% ROAS in 2012, 4.7% ROAS for 2011, 7.6% for 2010 and 7.4% for 2009;

Sources: A.M. Best, ISO.

Profitability Peaks & Troughs in the P/C Insurance Industry, 1975 – 2017



Profitability = P/C insurer ROEs. 2011-16 figures are estimates based on ROAS data. Note: Data for 2008-2014 exclude mortgage and financial guaranty insurers.
Source: NAIC, ISO, A.M. Best, USC RUM Center.

INVESTMENTS: THE NEW REALITY

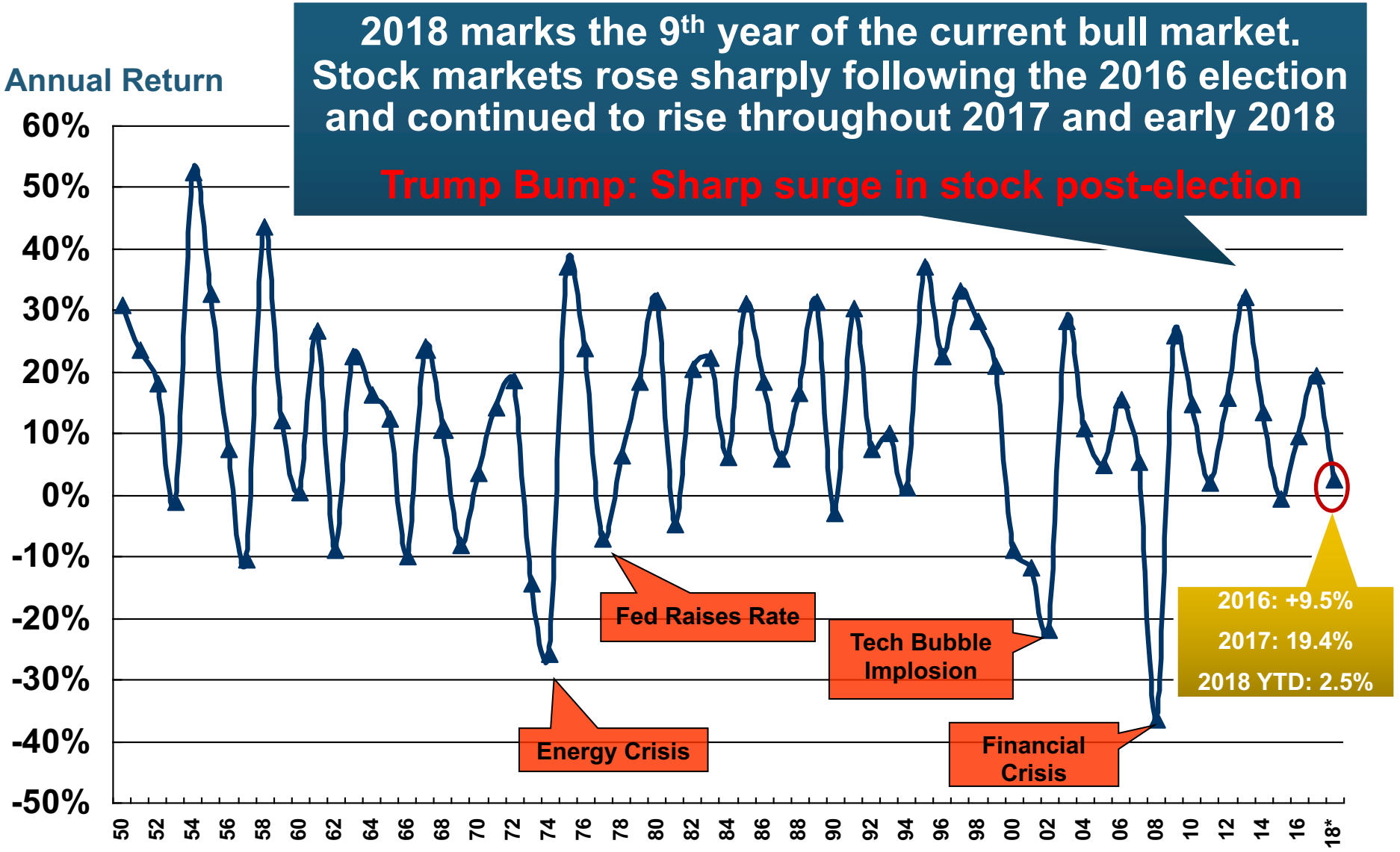
Investment Performance is a Key Driver of Insurer Profitability

The "Trump Bump" Has Lifted Stock Markets and Interest Rates

Will the Gains Help Insurers?

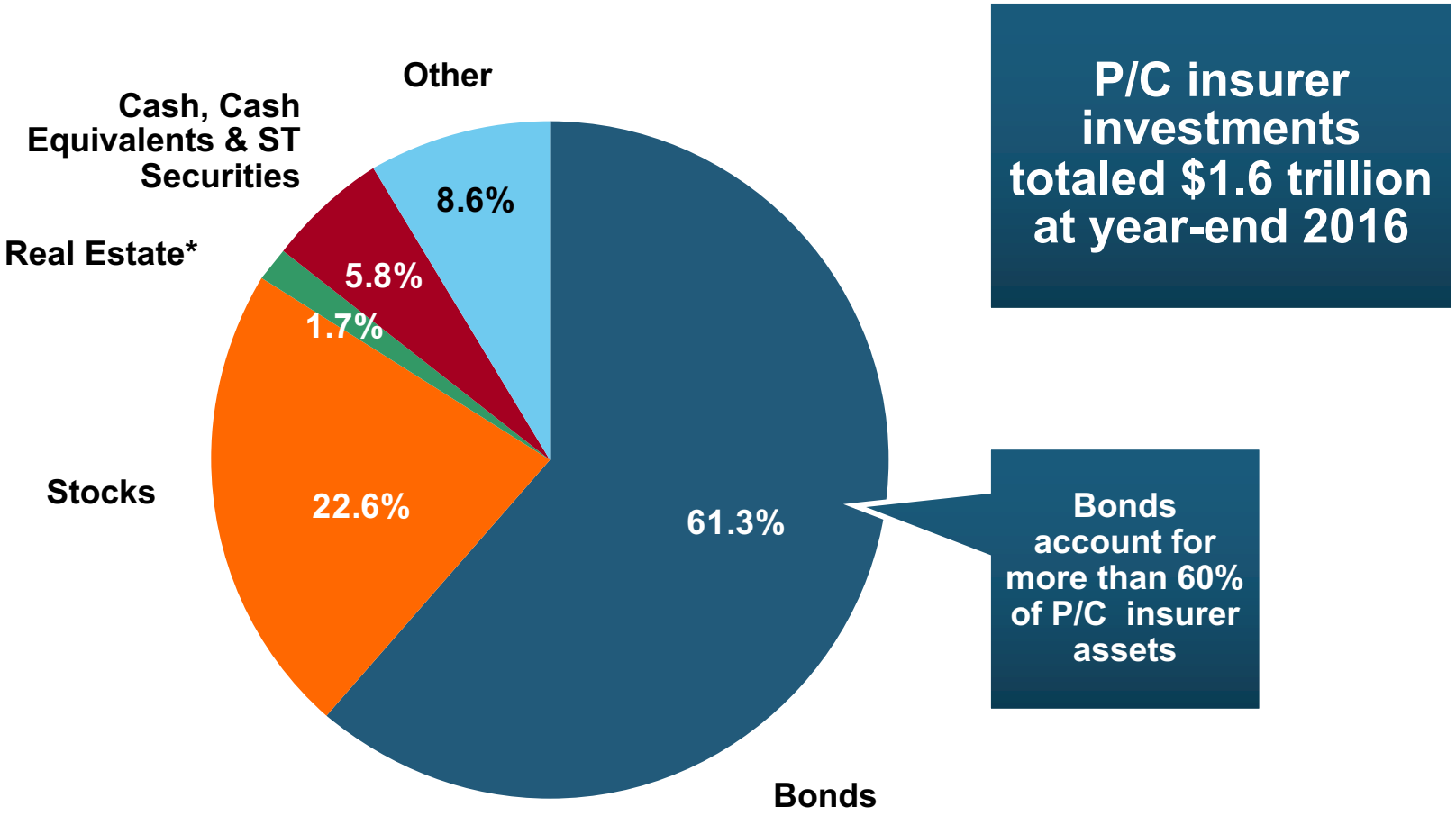
51

S&P 500 Index Returns, 1950 – 2018*



*Through May 11, 2018.
Source: NYU Stern School of Business: http://pages.stern.nyu.edu/~adamodar/New_Home_Page/datafile/histretSP.html.

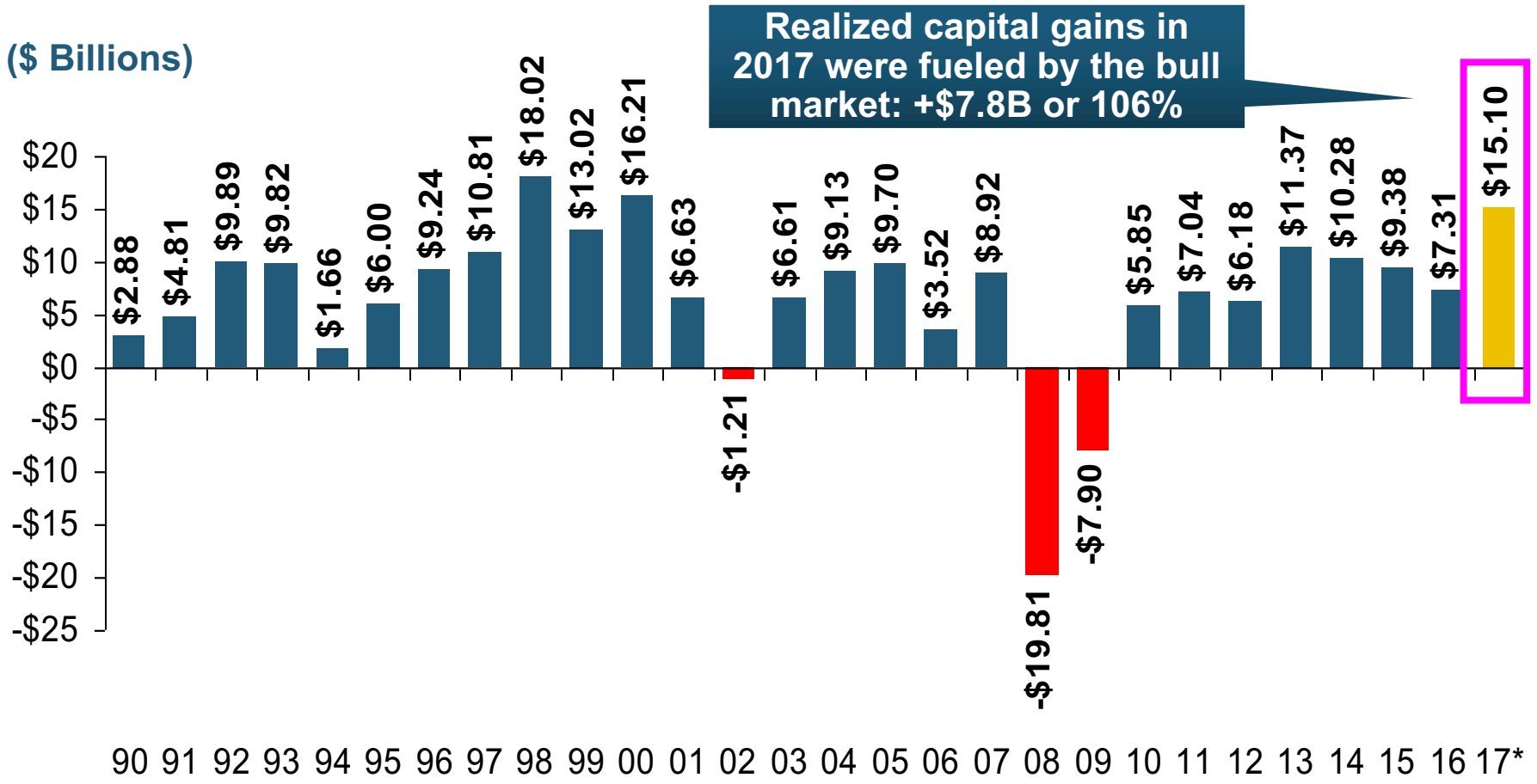
P/C Insurers Investments by Type, 2016



*General account assets.

Source: NAIC data sourced from S&P Global Market Intelligence; *2018 Insurance Fact Book*, Insurance Information Institute.

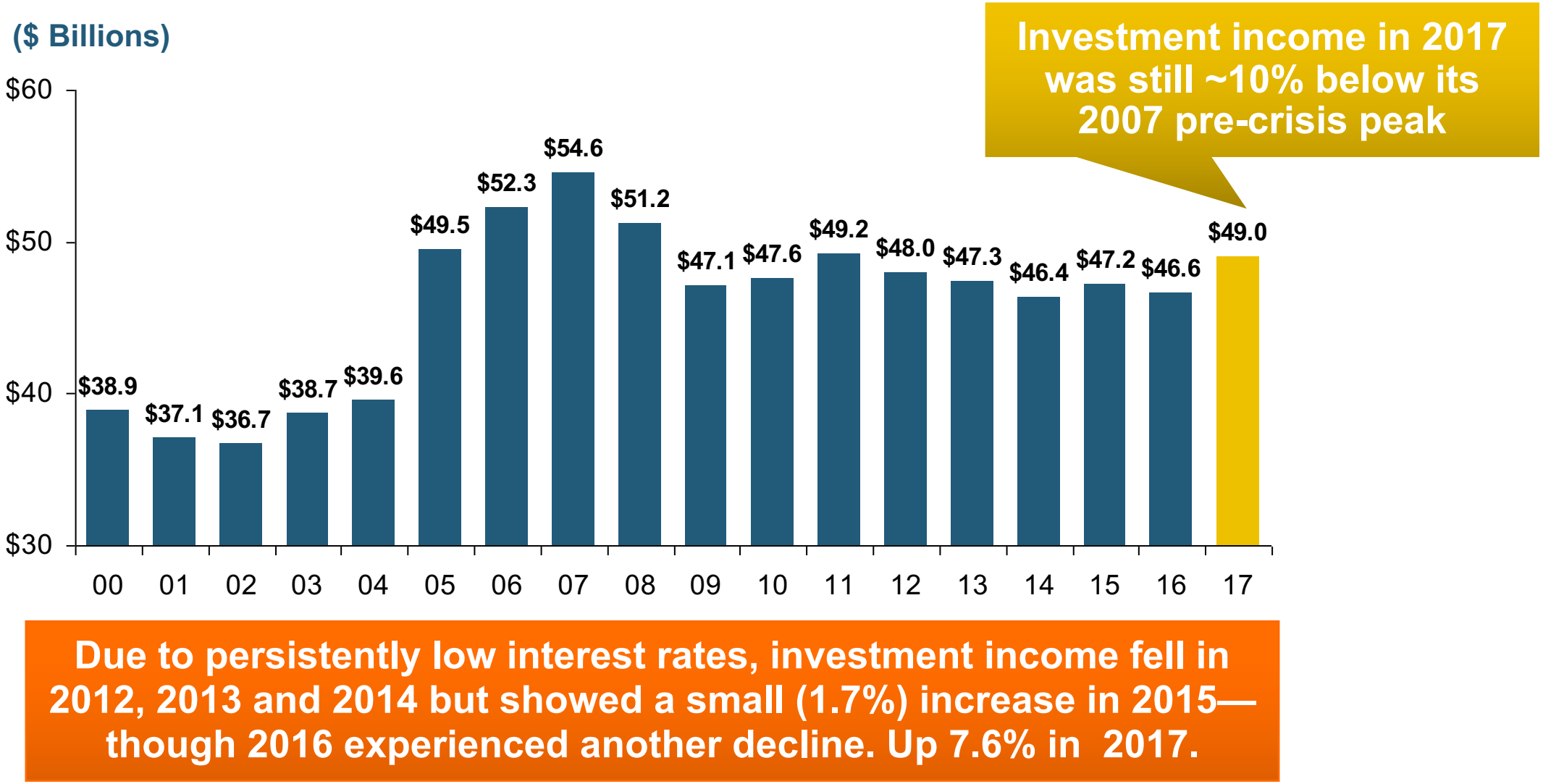
P/C Insurer Net Realized Capital Gains/Losses, 1990-2017:Q4



Insurers posted net realized capital gains in 2010 - 2017 following two years of realized losses during the financial crisis. The bull market of 2017 helped push gains to more than twice their 2016 level.

*Figure is through Q4:2017
Sources: A.M. Best, ISO; Insurance Information Institute.

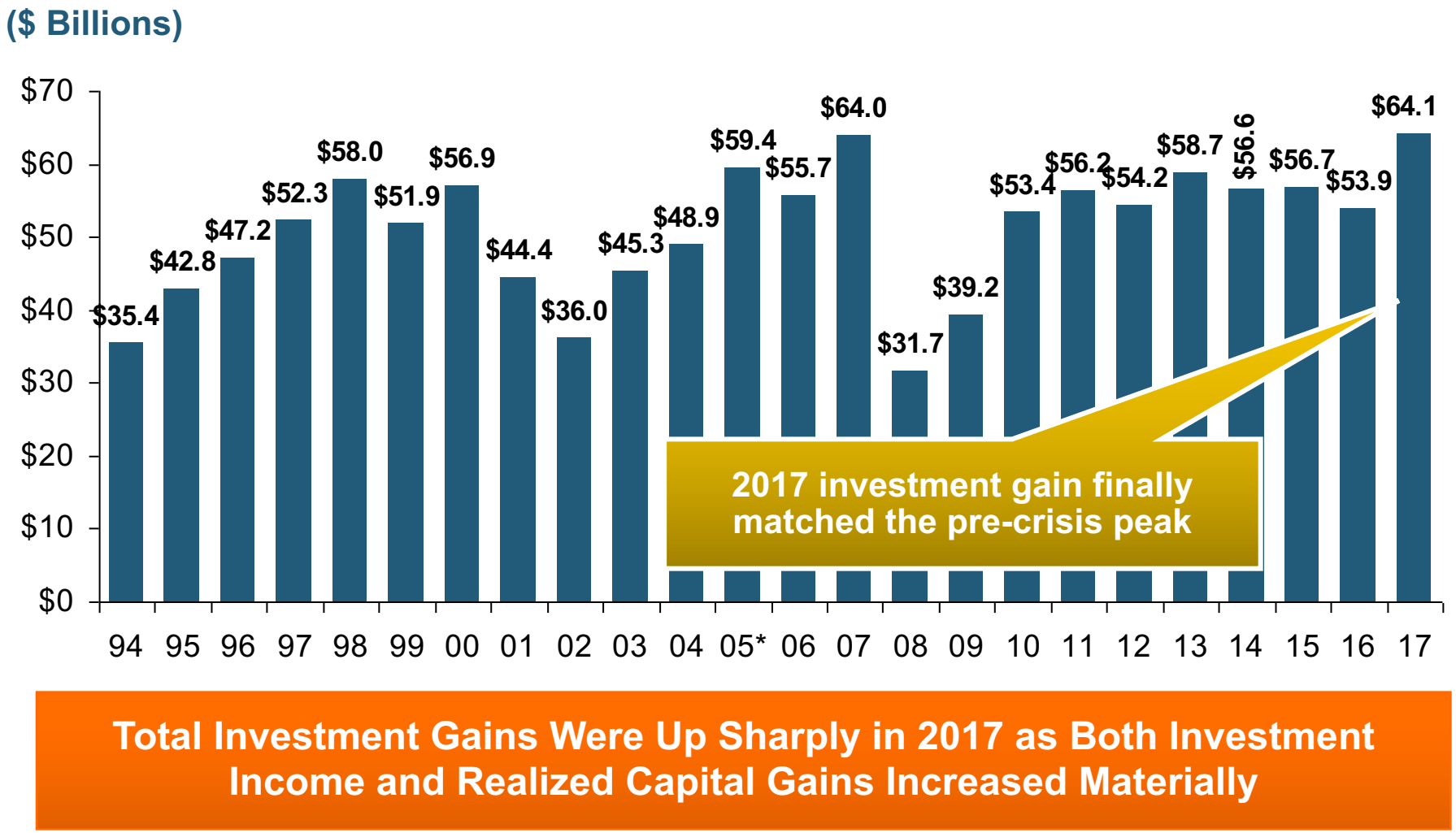
Property/Casualty Insurance Industry Investment Income, 2000–2017



Due to persistently low interest rates, investment income fell in 2012, 2013 and 2014 but showed a small (1.7%) increase in 2015—though 2016 experienced another decline. Up 7.6% in 2017.

[1] Investment gains consist primarily of interest and stock dividends. Sources: ISO; Insurance Information Institute.

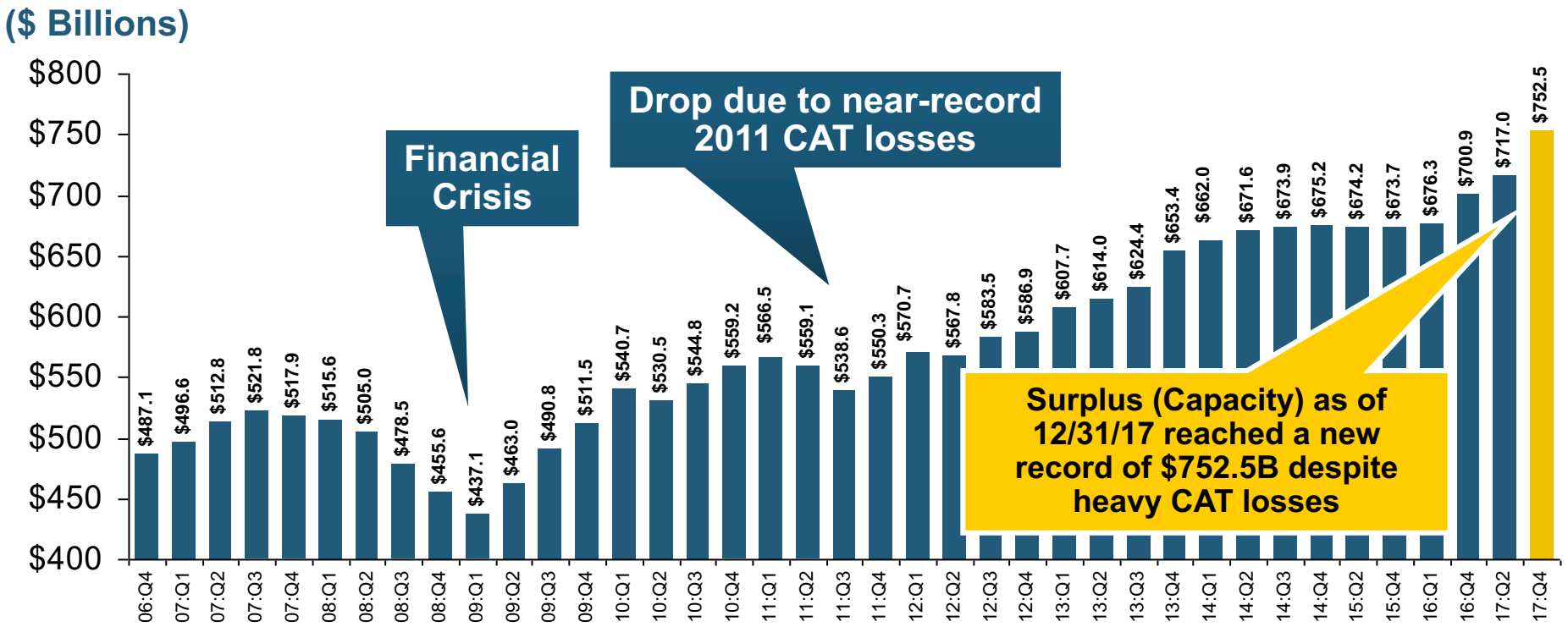
Property/Casualty Insurance Industry Investment Gain: 1994–2017[1]



Total Investment Gains Were Up Sharply in 2017 as Both Investment Income and Realized Capital Gains Increased Materially

[1] Investment gains consist primarily of interest, stock dividends and realized capital gains and losses.
*2005 figure includes special one-time dividend of $3.2B.
Sources: ISO, SNL; Insurance Information Institute.

Policyholder Surplus, 2006:Q4–2017:Q4

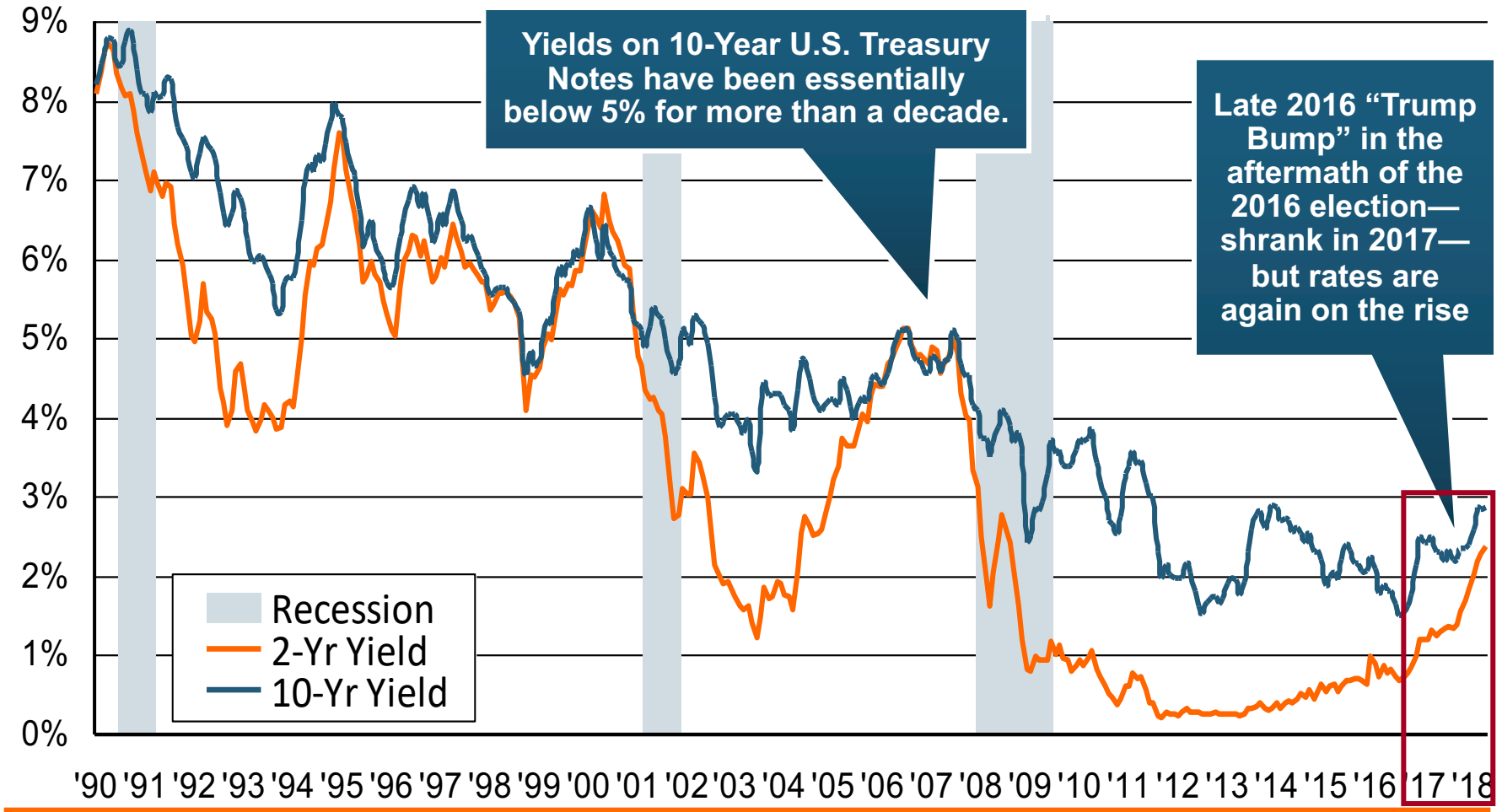


2010:Q1 data includes $22.5B of paid-in capital from a holding company parent for one insurer's investment in a non-insurance business .

Capacity/Capital "shocks" typically do not on their own drive a sustained firming of the pricing environment

Sources: ISO, A.M .Best; 2018 estimate from the Center for Risk and Uncertainty Management, University of South Carolina.

U.S. Treasury Security Yields: A Long Downward Trend, 1990–2018*



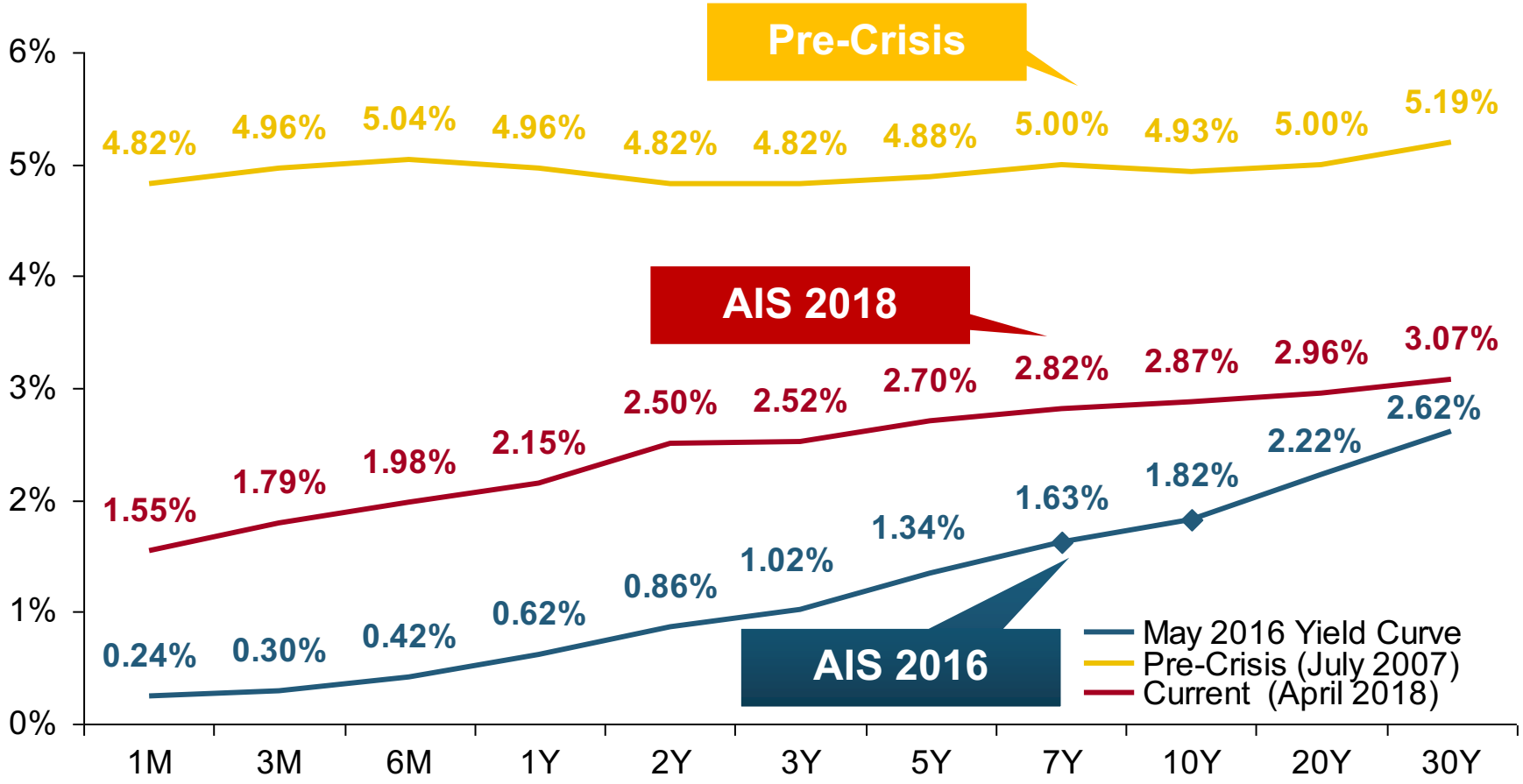
Since roughly 80% of P/C bond/cash investments are in 10-year or shorter durations, most P/C insurer portfolios will have low-yielding bonds for years to come.

*Monthly, constant maturity, nominal rates, through Apr. 2018.

Sources: Federal Reserve Bank at http://www.federalreserve.gov/releases/h15/data.htm. National Bureau of Economic Research (recession dates); Insurance Information Institute.

58

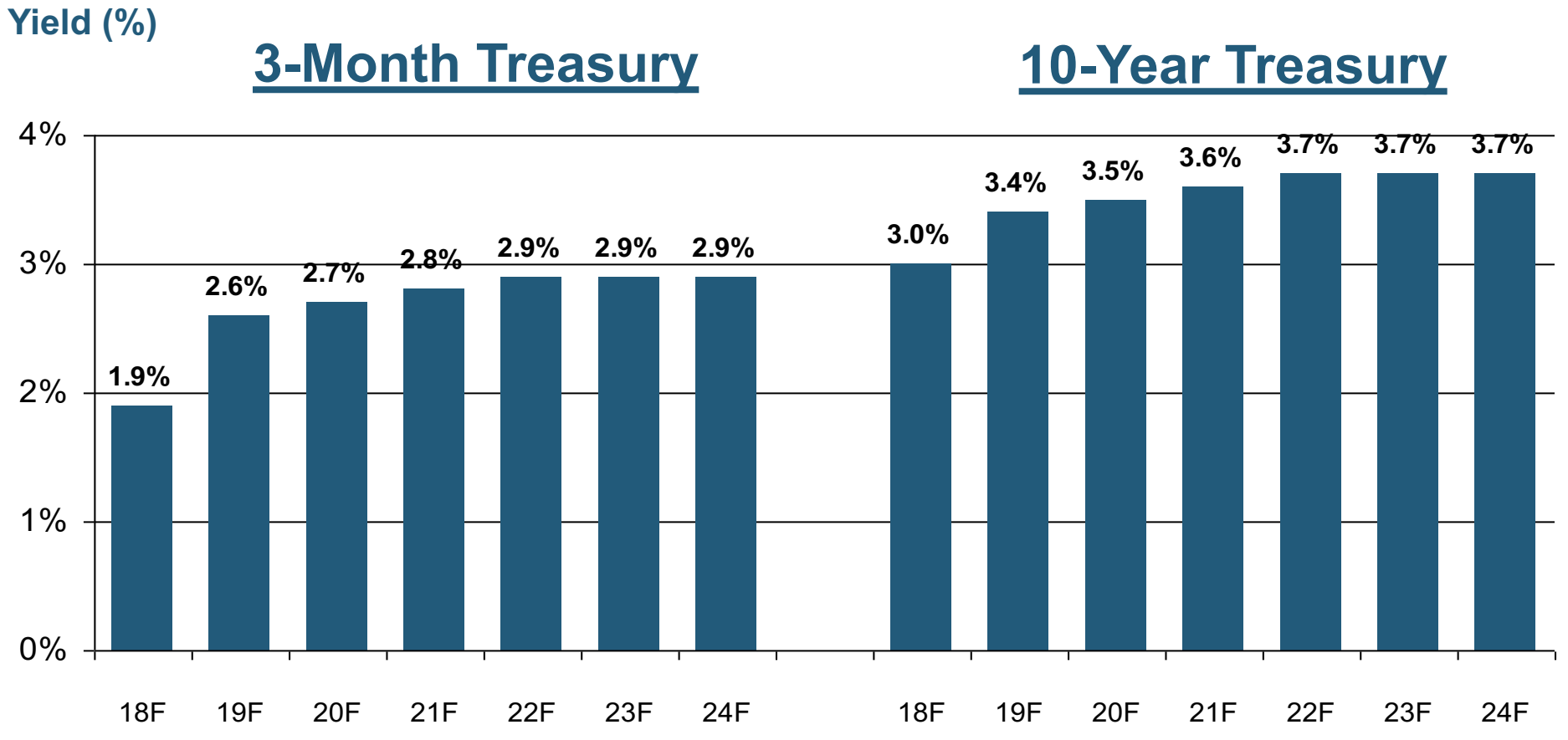
Treasury Yield Curves:
Pre-Crisis (July 2007) vs. April 2016 and 2018



The Fed Began to Raise Rates in Dec. 2015 but Rates Remain Far Below Pre-Crisis Levels

Source: Federal Reserve Board of Governors: http://www.federalreserve.gov/releases/h15/data.htm; Univ. of South Carolina..

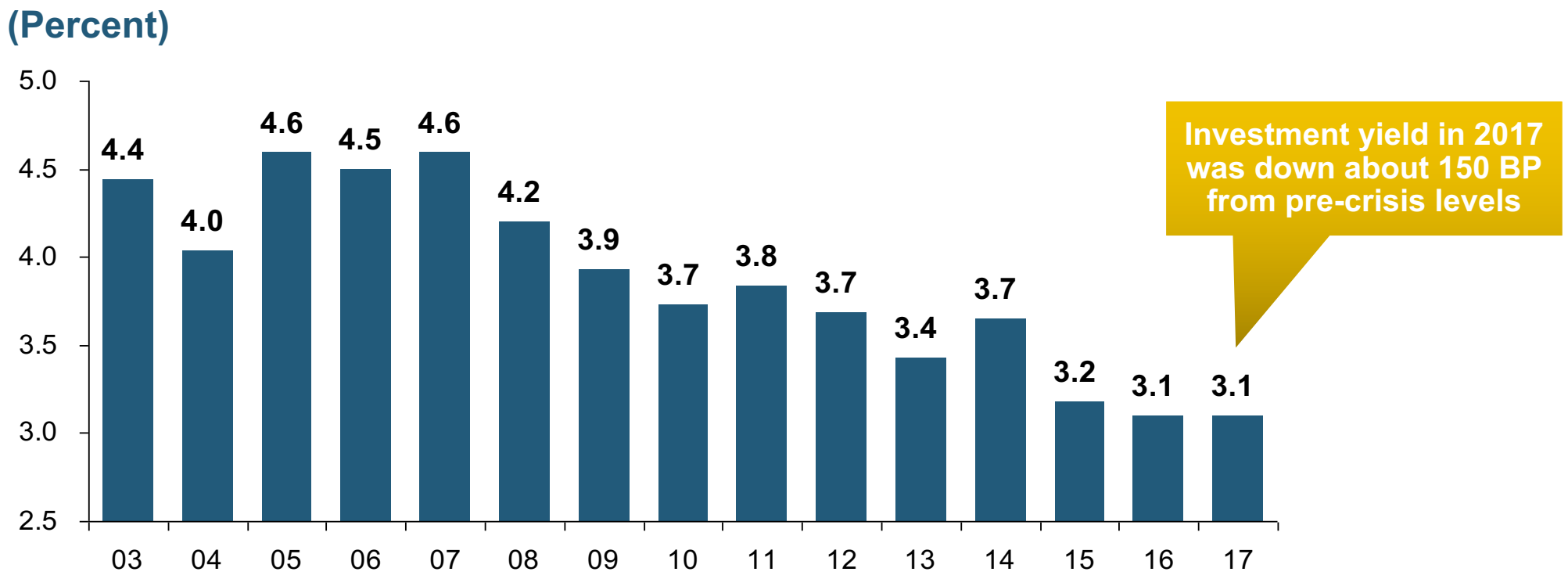
Interest Rate Forecasts: 2018 – 2024



A full normalization of interest rates is unlikely until the early 2020s, approximately 15 years after the onset of the financial crisis.

Sources: Blue Chip Economic Indicators (5/18 for 2018 and 2019; for 2018-2024 3/18 issue); Univ. of South Carolina.

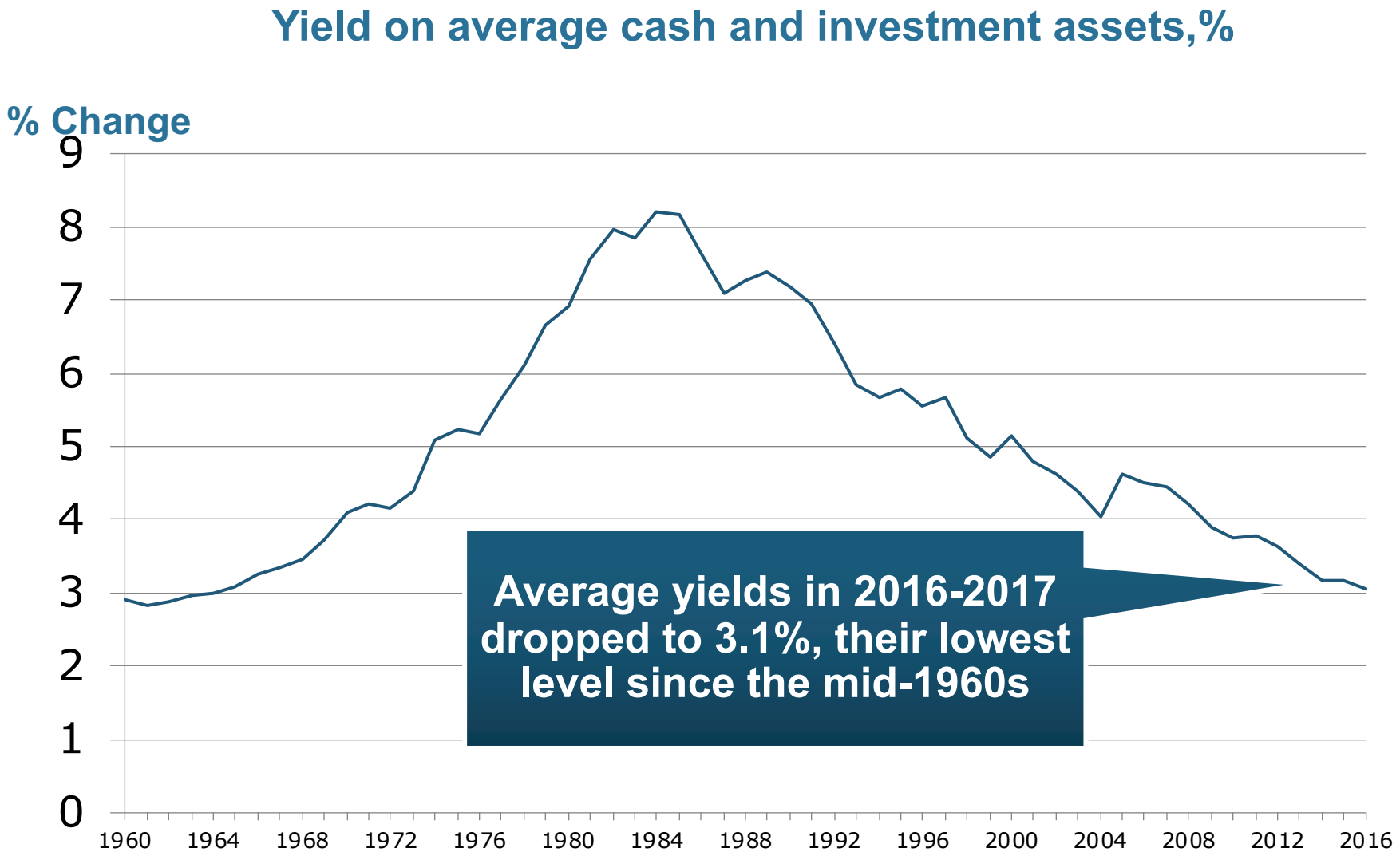
Net Investment Yield on Property/ Casualty Insurance Invested Assets, 2007–2017*



The yield on invested assets remains low relative to pre-crisis yields. Fed rate increases beginning in late 2015 have pushed up some yields, albeit quite modestly. Shrinking of Fed's balance sheet should help too in 2018 and beyond.

Sources: NAIC data, sourced from S&P Global Market Intelligence; 2017 figure is from ISO.

P/C Insurer Investment Yields: Lowest in Half a Century

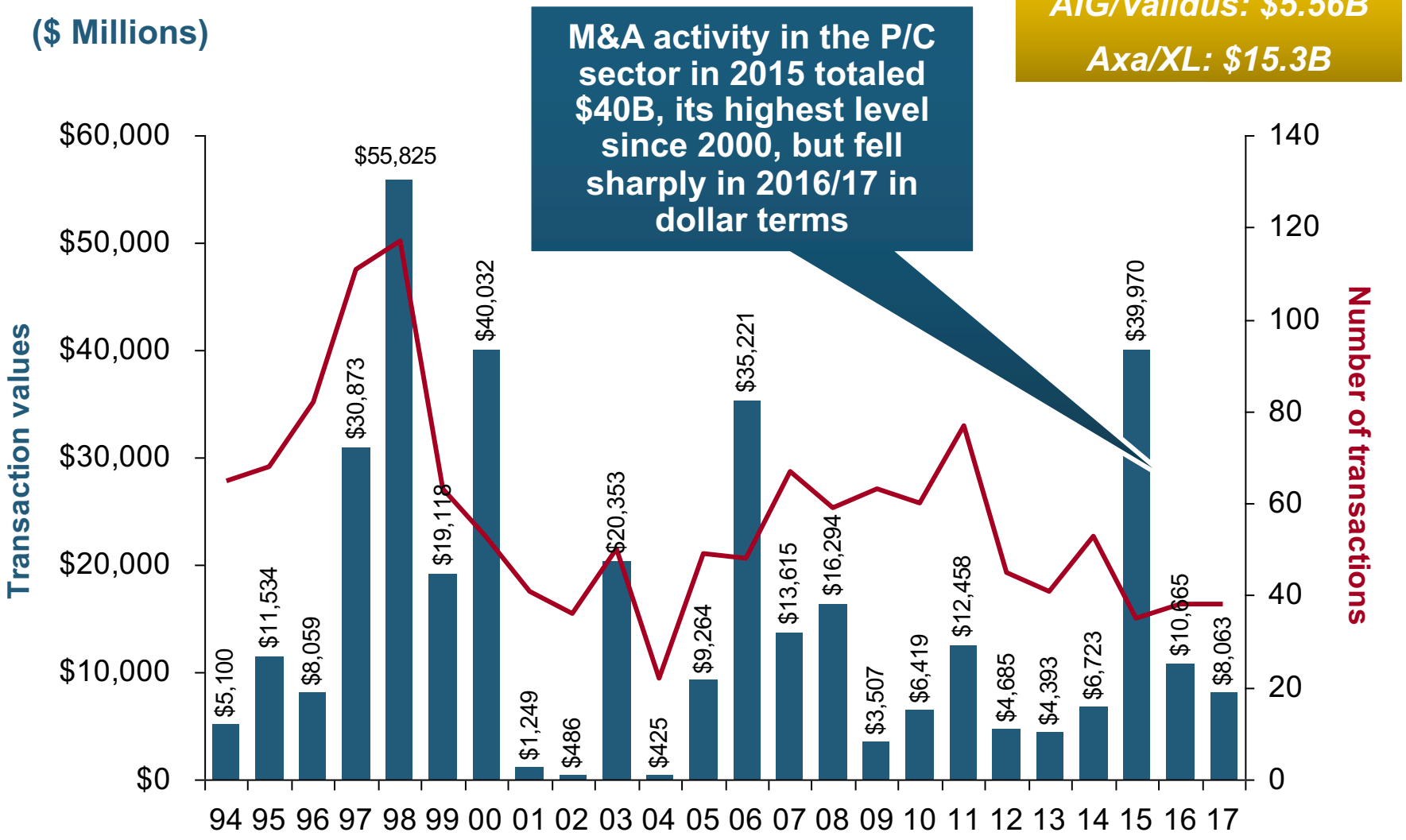


M&A Trends

Accumulation of Capital, Modest Growth Could Fuel M&A Activity

U.S. INSURANCE MERGERS AND ACQUISITIONS, P/C SECTOR, 1994-2017 (1)

Major 2018 Deal:
AIG/Validus: $5.56B
Axa/XL: $15.3B



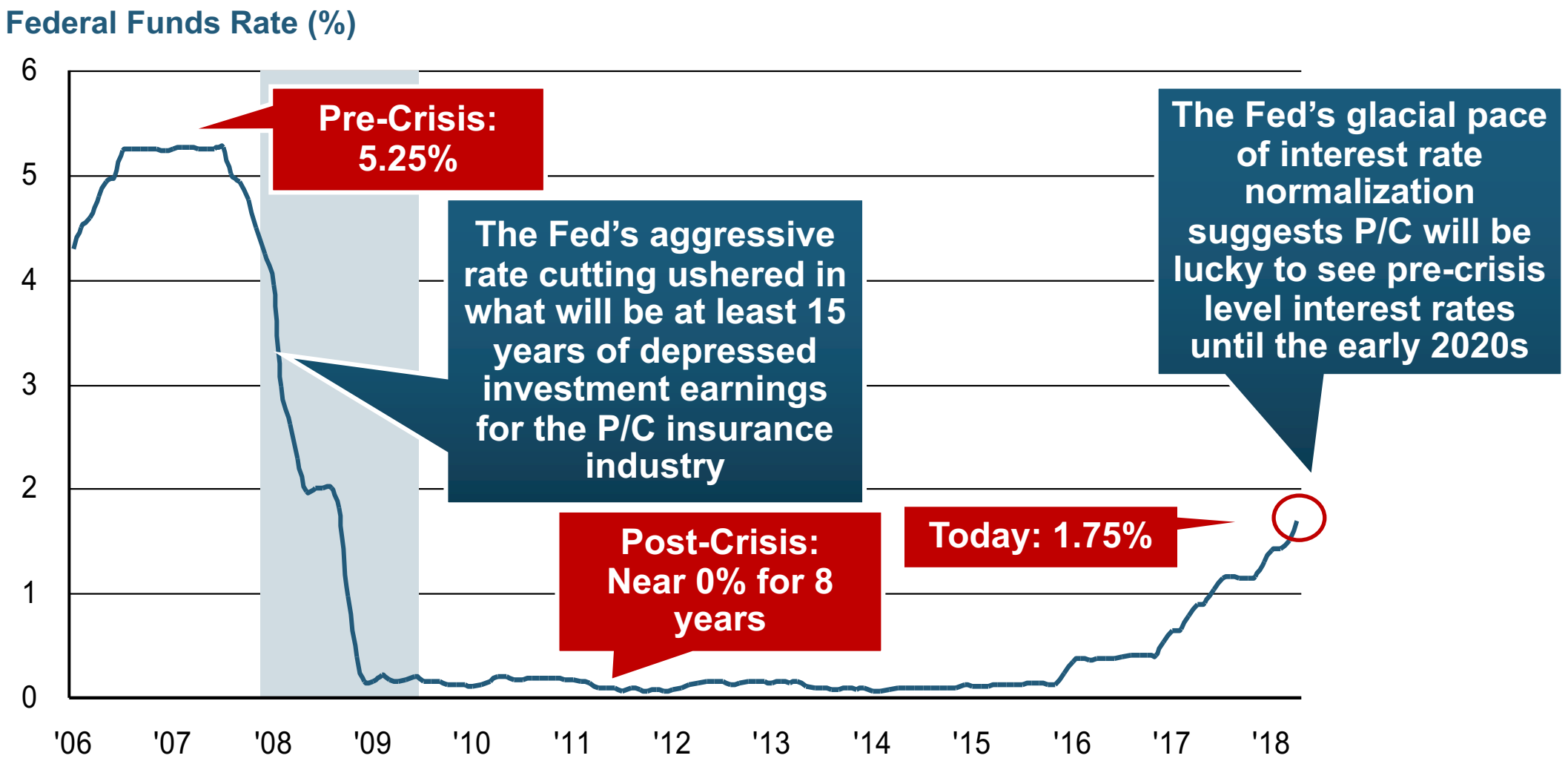
(1) Includes transactions where a U.S. company was the acquirer and/or the target.

Source: Conning proprietary database.

Interest Rate and Inflation Trends

Federal Reserve Policy, Economic Strength and Deficits Will Drive Interest Rates and Inflation

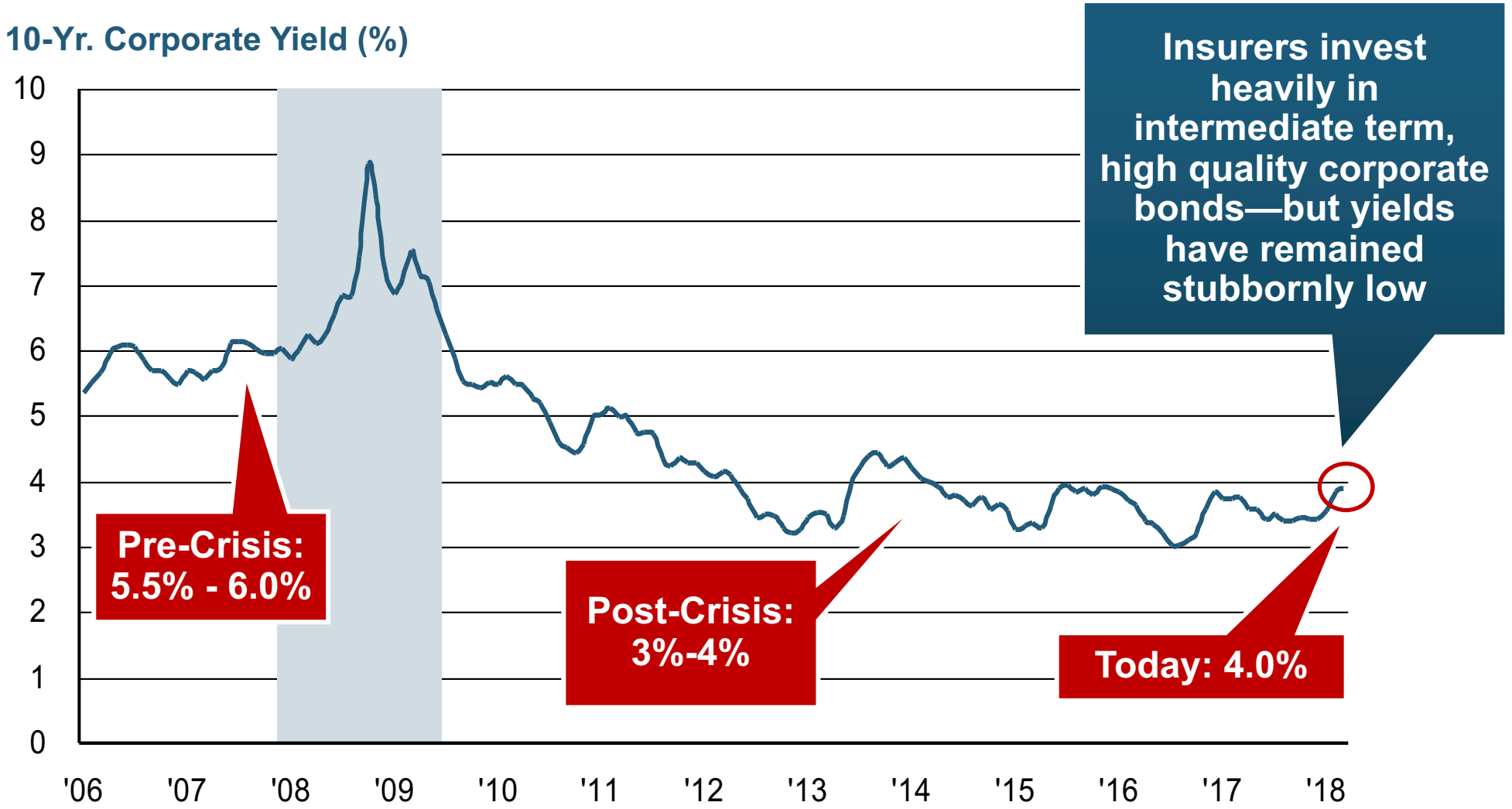
Federal Funds Rate: Jan. 2006 – Apr. 2018



Note: Recessions indicated by gray shaded columns.

Source: Board of Governors, Federal Reserve; National Bureau of Economic Research (recession dates); Center for Risk and Uncertainty Management, University of South Carolina.

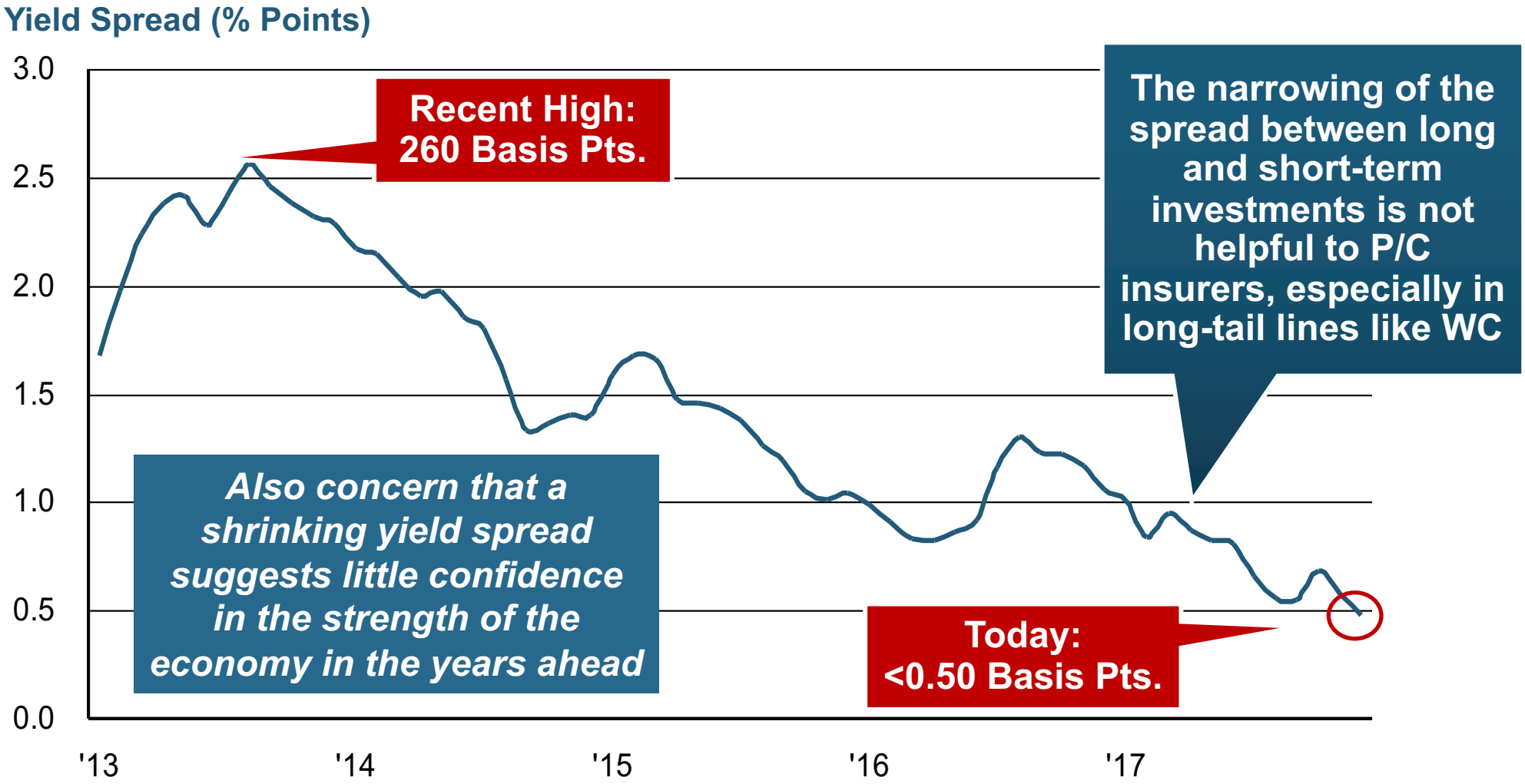
High Quality 10-Yr. Corporate Bond Yields: Jan. 2006 – Mar. 2018



Note: Recessions indicated by gray shaded columns.

Source: Board of Governors, Federal Reserve; National Bureau of Economic Research (recession dates); Center for Risk and Uncertainty Management, University of South Carolina.

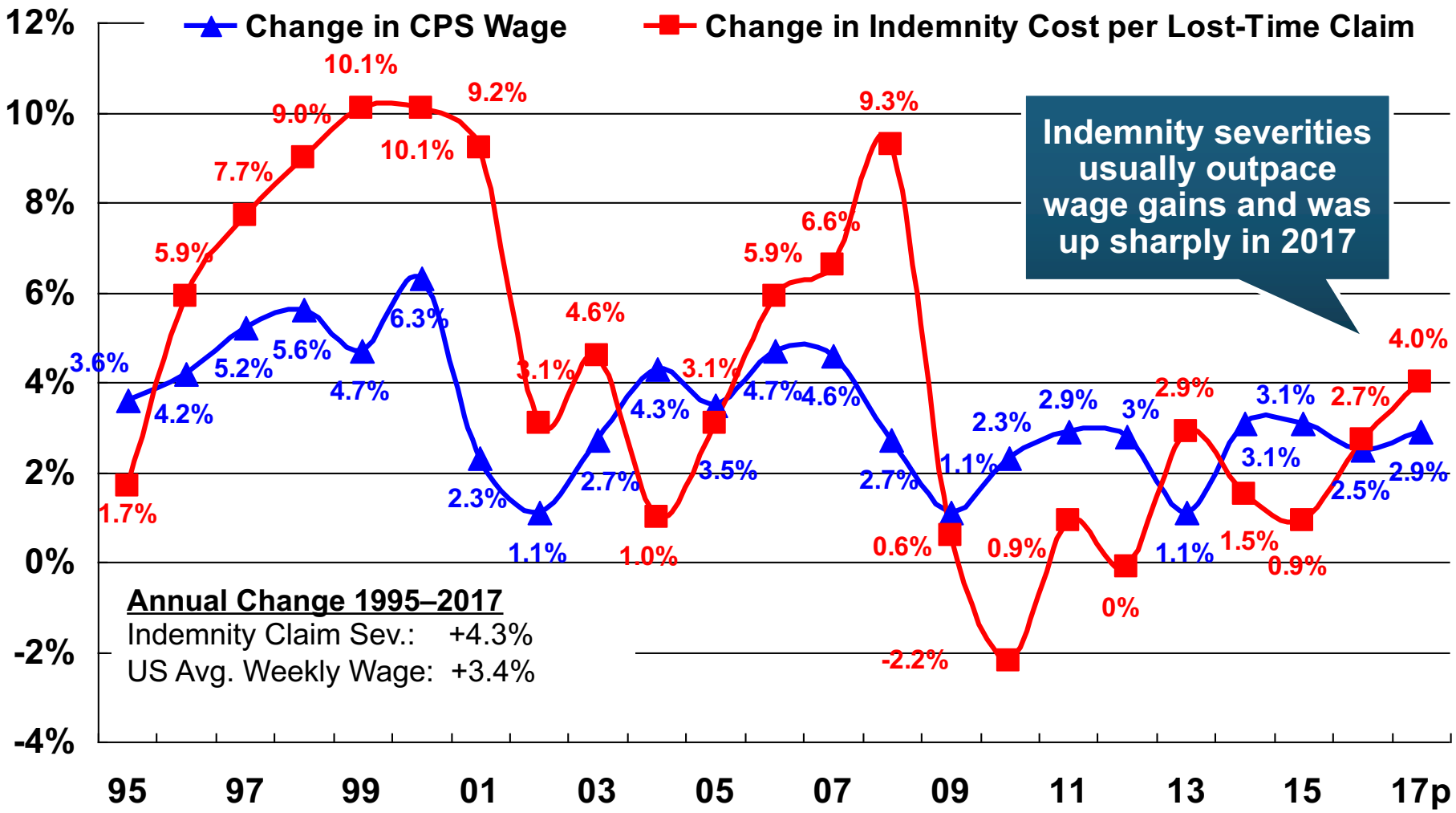
Yield Spread Between 10- and 2-Yr. Treasury, May 2013 – April 2018



Note: Recessions indicated by gray shaded columns.

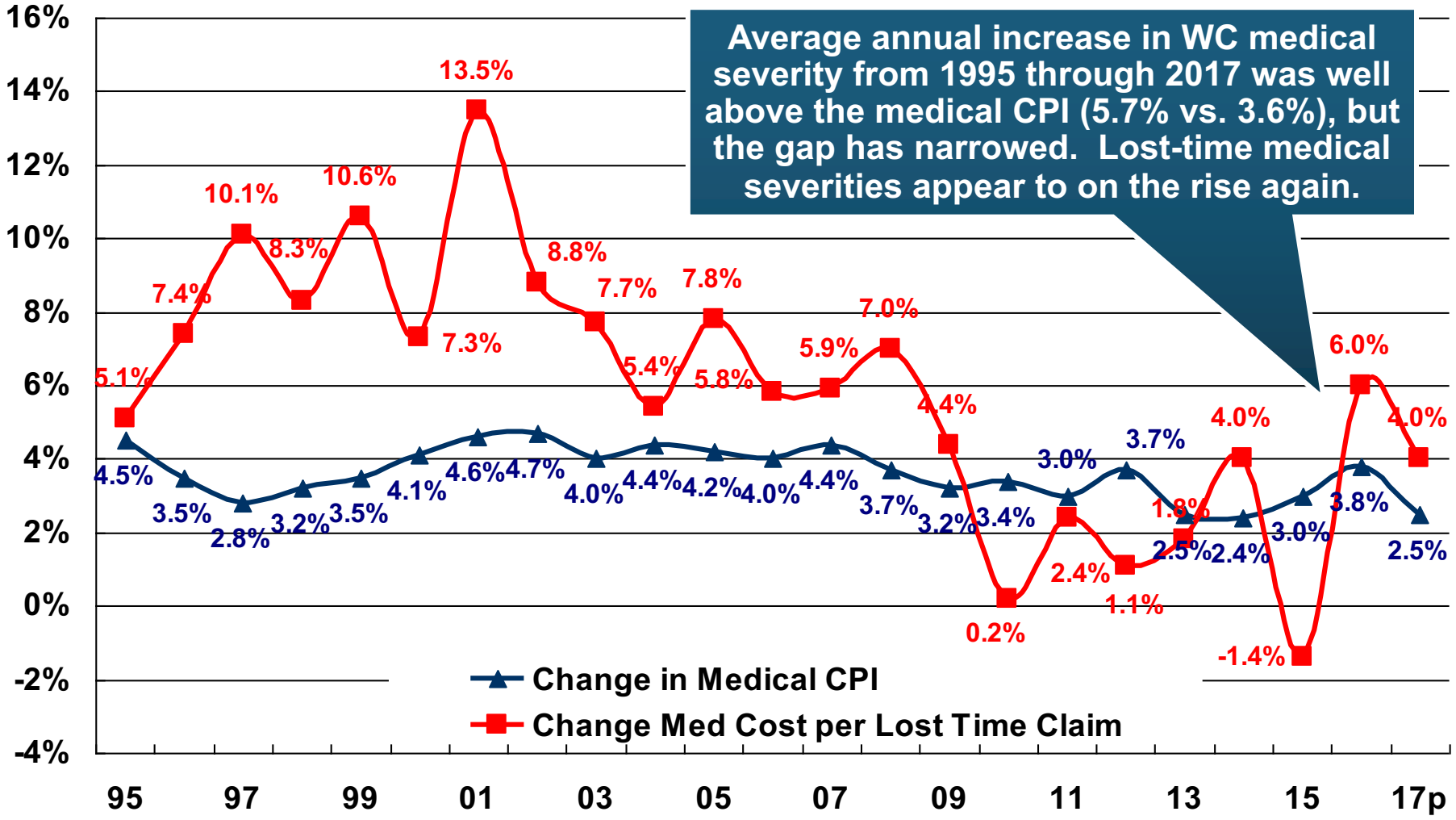
Source: Federal Reserve Bank of St. Louis. FRED Economic Data; Center for Risk and Uncertainty Management, University of South Carolina.

WC Indemnity Severity vs. Wage Inflation, 1995 -2017p



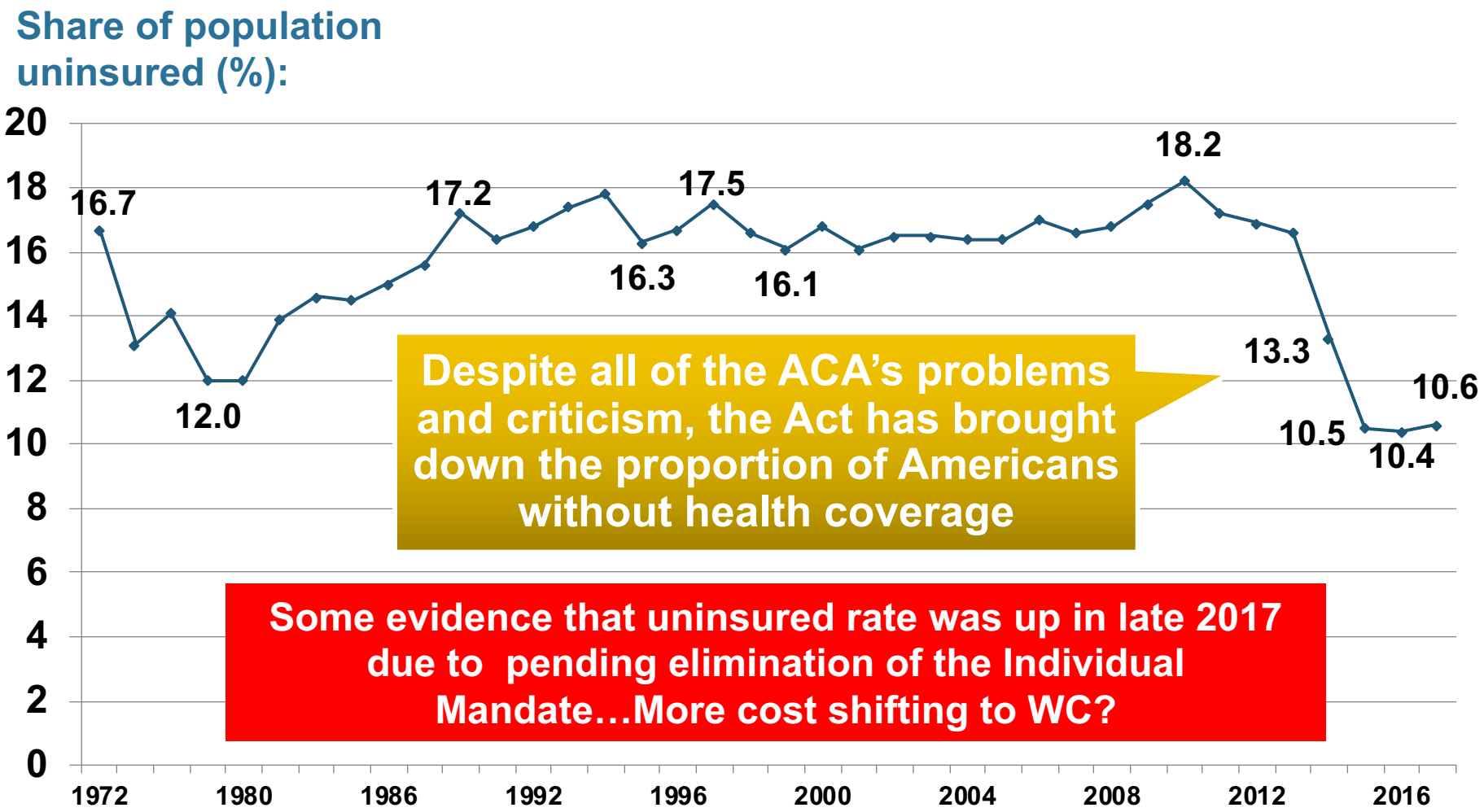
2017p: Preliminary based on data valued as of 12/31/2017;, Developed to ultimate. Based on the states where NCCI provides ratemaking services. Excludes the effects of deductible policies. CPS = Current Population Survey.
Source: NCCI; University of South Carolina, Center for Risk and Uncertainty Management.

WC Medical Severity Generally Outpaces the Medical CPI Rate, 1995 – 2017p



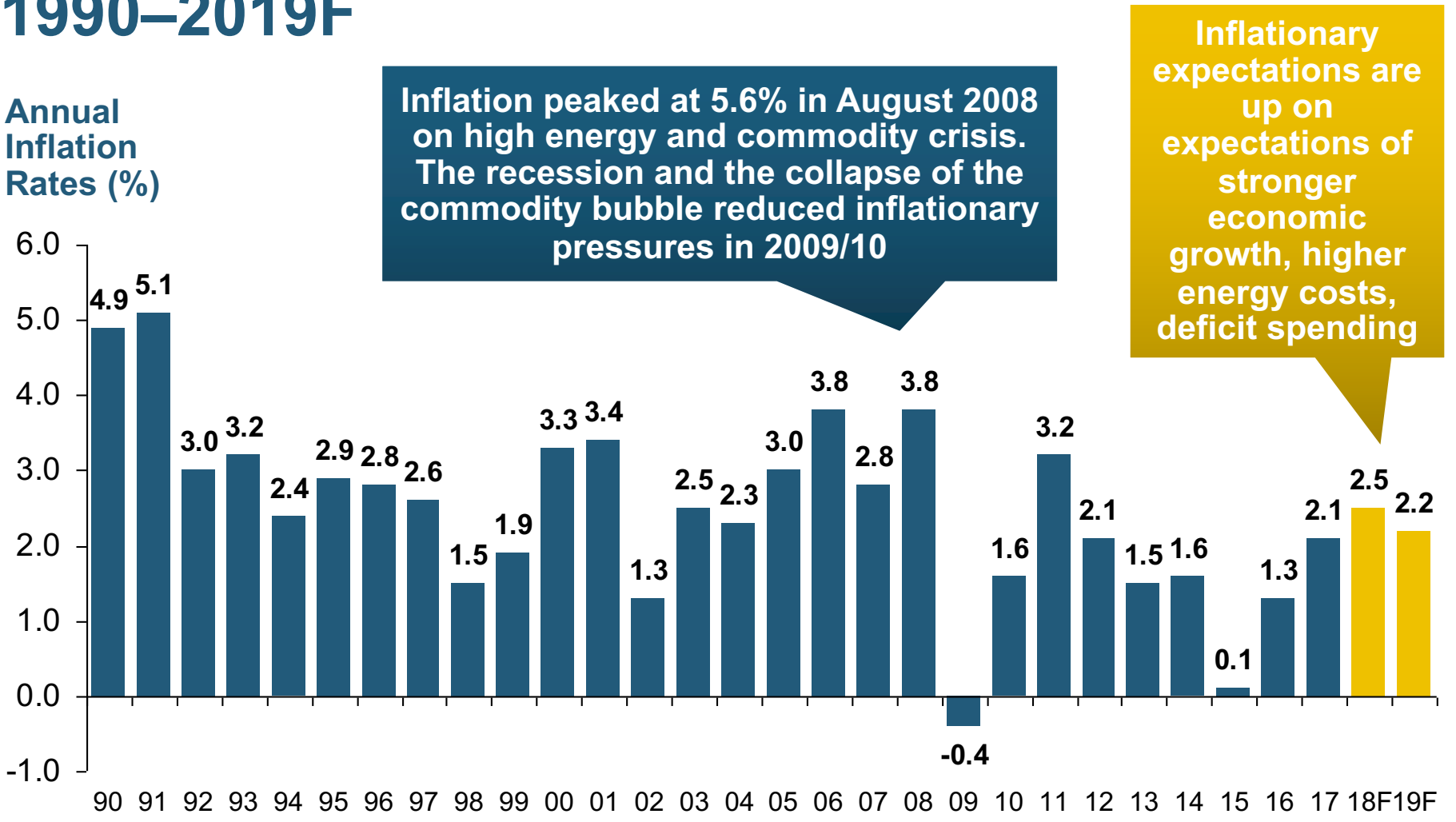
Sources: Med CPI from US Bureau of Labor Statistics, WC med severity from NCCI based on NCCI states.

Health Insurance: Uninsured Rate Among the Nonelderly Population, 1972 – 2017:Q3



Source: CDC/NCHS, National Health Interview Survey, reported in: https://www.cdc.gov/nchs/data/nhis/earlyrelease/insur201802.pdf

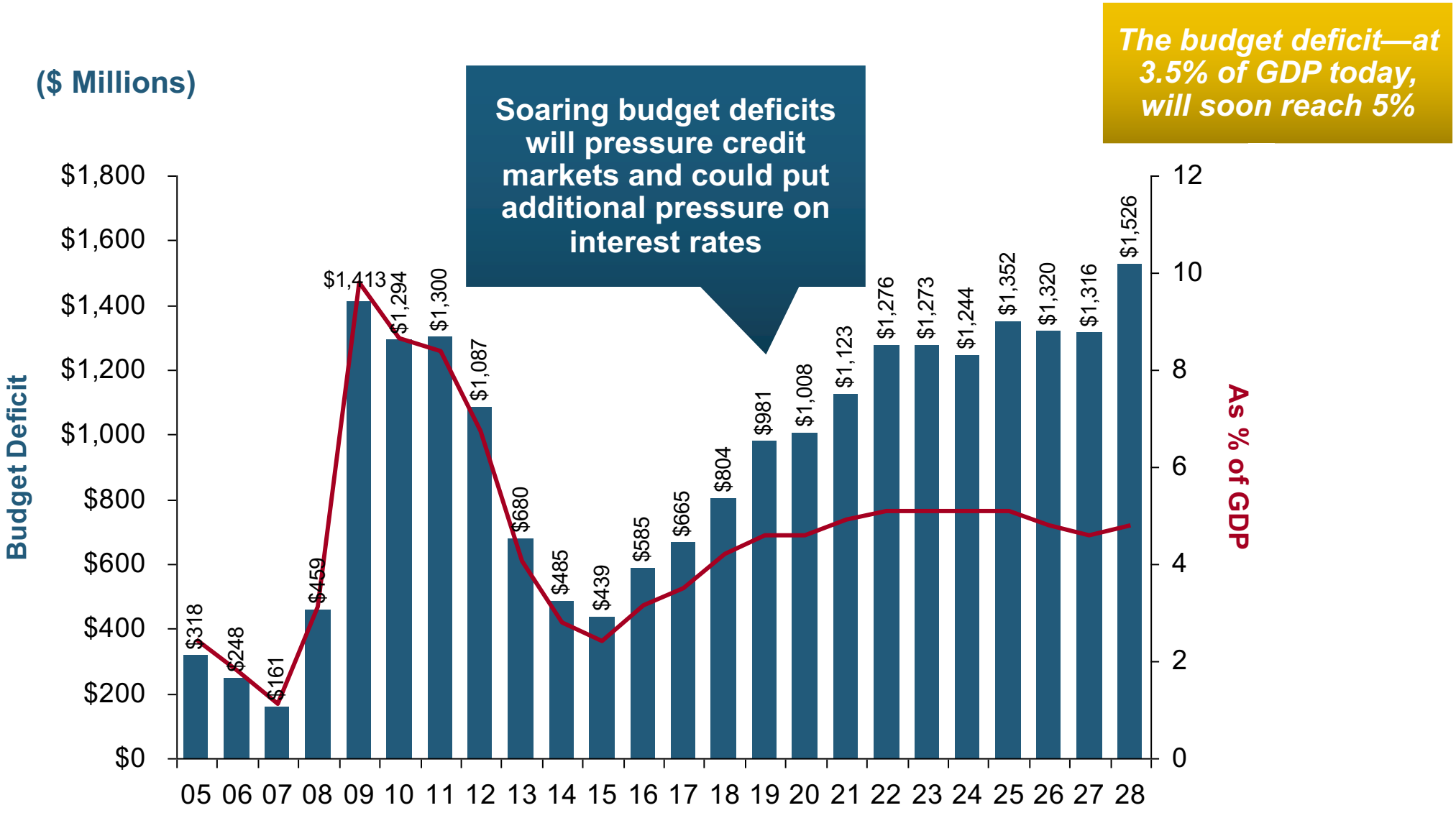
Annual Inflation Rates, (CPI-U, %), 1990–2019F



Less slack in the U.S. economy, rising energy prices and looming budget deficits suggest additional inflationary

Sources: US Bureau of Labor Statistics; Blue Chip Economic Indicators, 5/18 (forecasts).

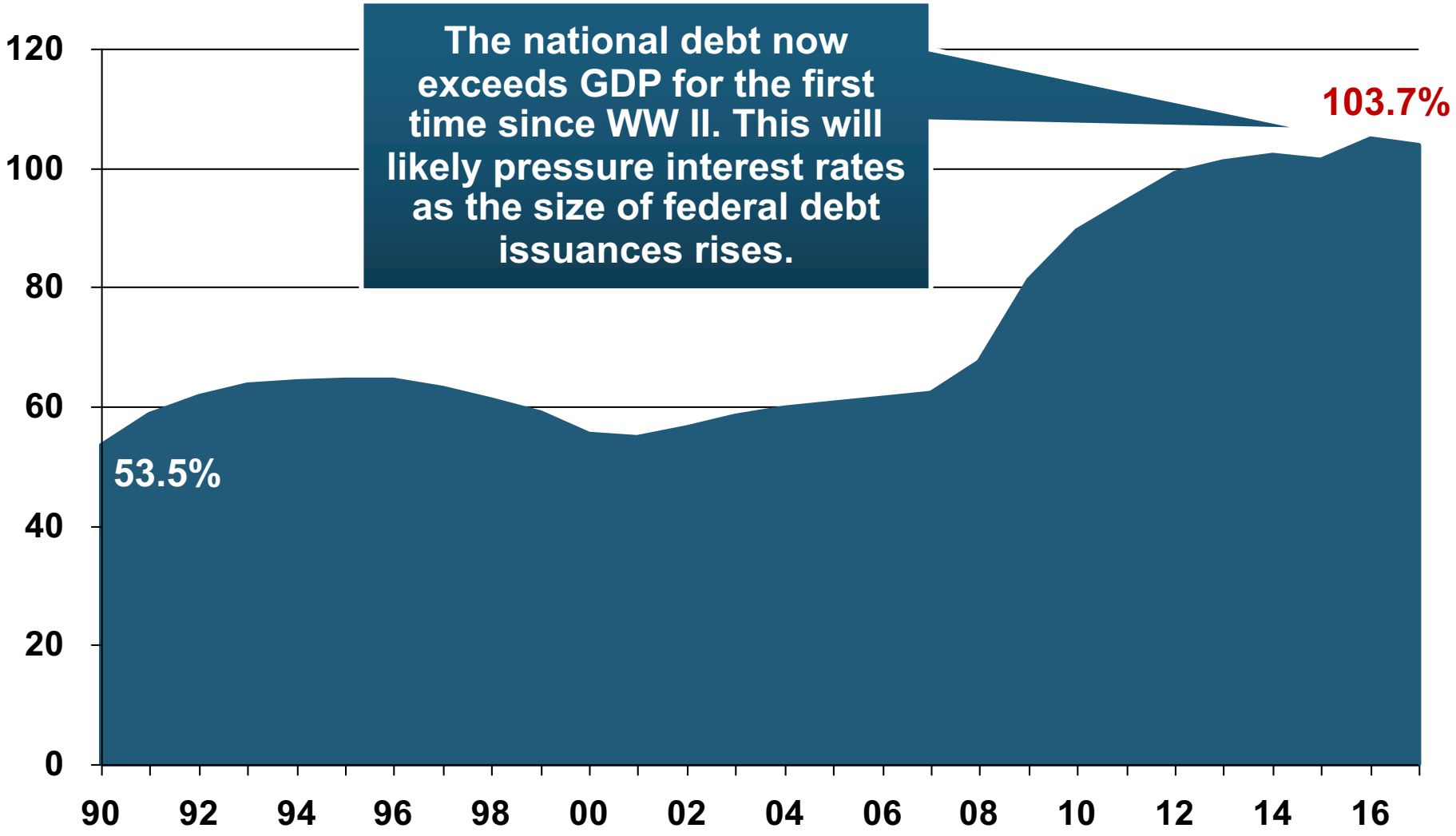
U.S. Budget Deficit in Dollars and as a Share of GDP: 2005-2028F



(1) Includes transactions where a U.S. company was the acquirer and/or the target.

Source: Conning proprietary database.

US National Debt as a Share of GDP: 1995 - 2017



Source: Congressional Budget Office.

Infrastructure Initiatives

WC Insurance Will Be a Primary Beneficiary of Any Major Infrastructure Initiatives

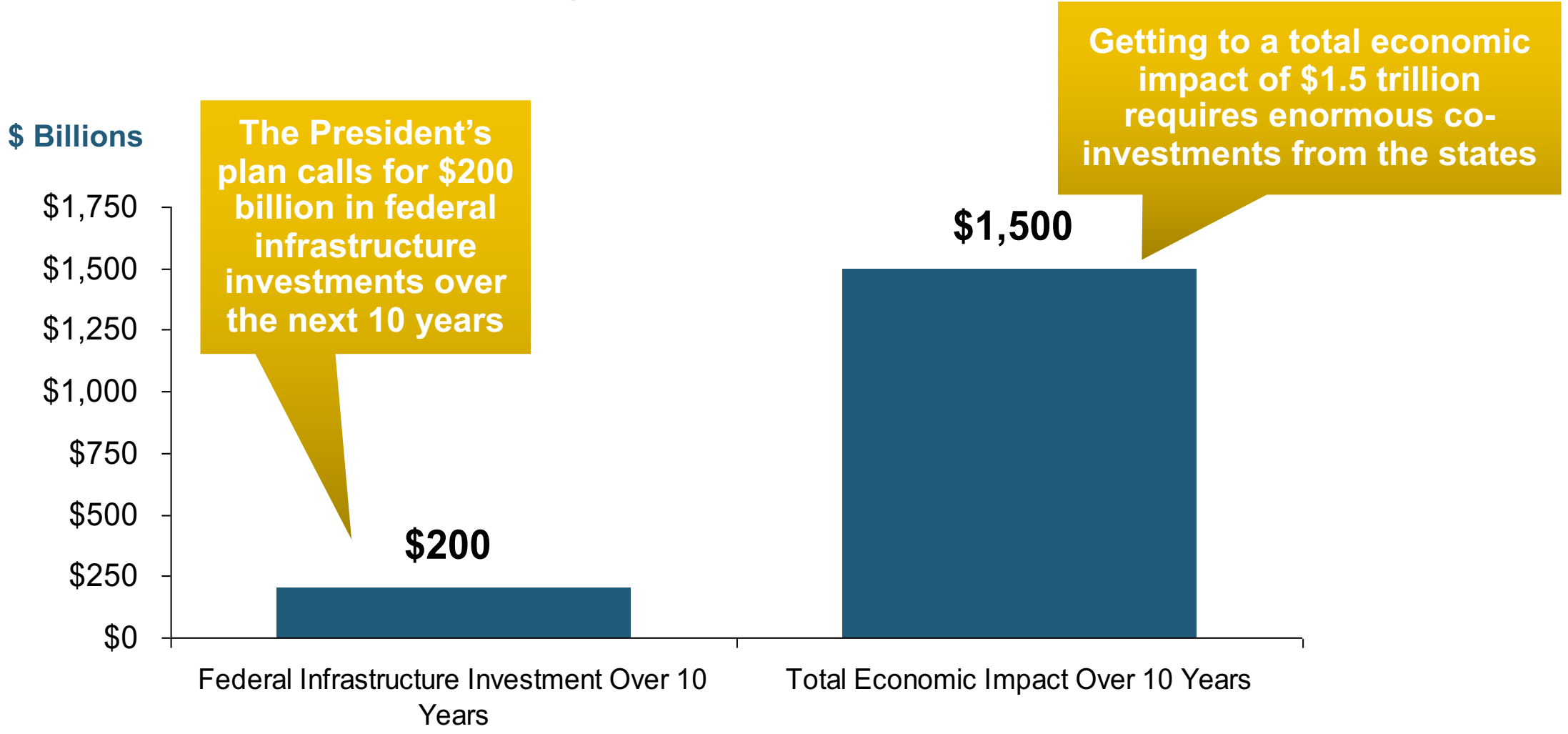
76

Infrastructure Spending: Benefits for WC Insurers?

Infrastructure Spending

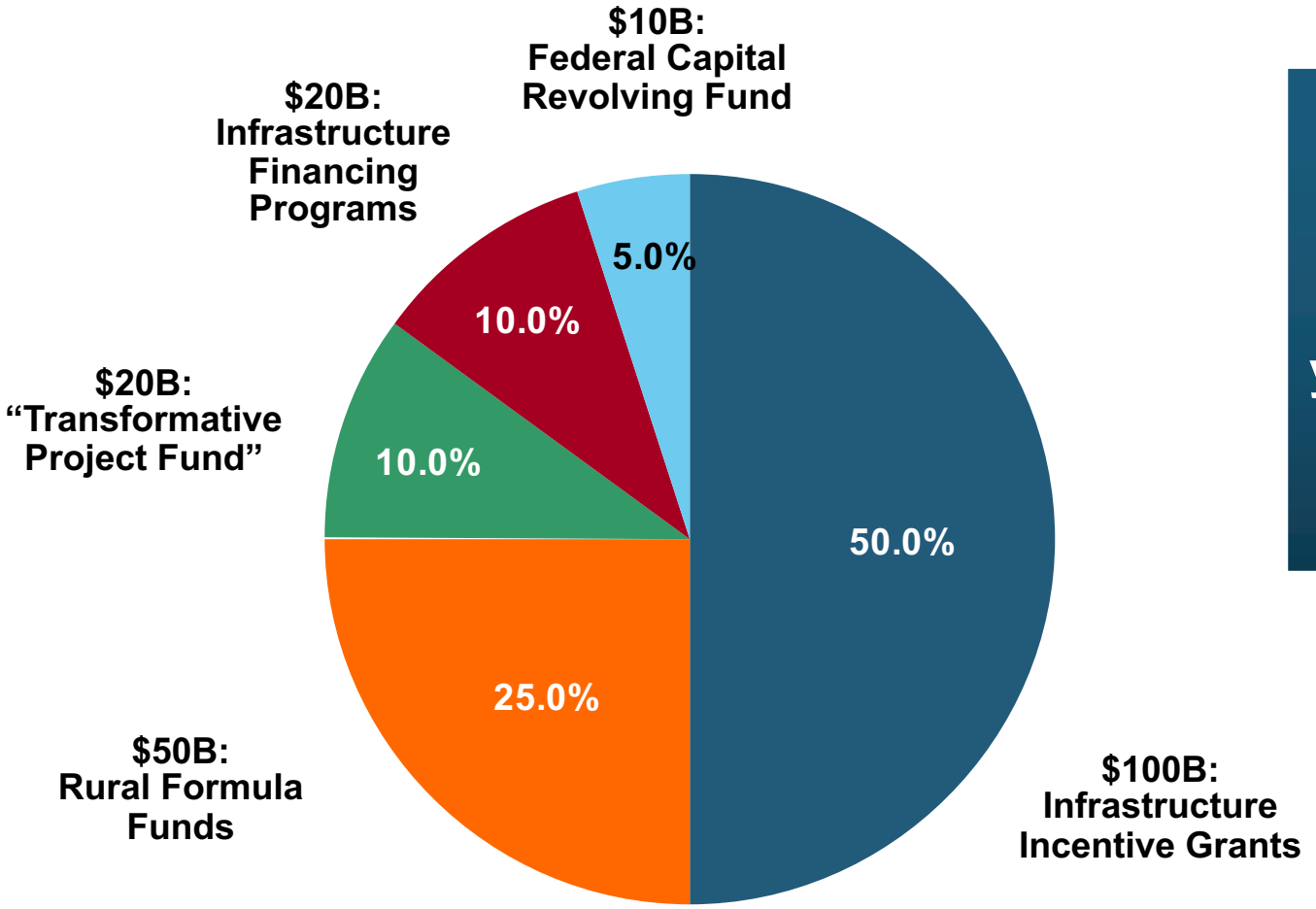
- Insurance industry could benefit from stepped-up infrastructure spending as promised by Trump
- But 2017 Tax Cuts and Jobs Act means little fiscal room for infrastructure initiatives
- Privatization of government infrastructure could provide growth opportunity for commercial insurers
- If infrastructure spending materializes, will benefit all major commercial lines:
  - WC
  - Commercial Property & Liab.
  - Surety
  - Commercial Auto

The White House Infrastructure Initiative: President Trump's Plan by the Numbers



Sources: The White House, *2018 Budget: Infrastructure Initiate accessed at:* https://www.whitehouse.gov/sites/whitehouse.gov/files/omb/budget/fy2018/fact_sheets/2018%20Budget%20Fact%20Sheet_Infrastructure%20Initiative.pdf ; Risk and Uncertainty Management Center, Univ. of South Carolina.

Composition of Infrastructure Spending Under President Trump's Plan (April 2018)



The Trump Administration proposes to make $200 billion in infrastructure investments over 10 years, producing a total economic benefit of $1.5 trillion over the next decade

Sources: The White House, *2018 Budget: Infrastructure Initiate accessed at:* https://www.whitehouse.gov/sites/whitehouse.gov/files/omb/budget/fy2018/fact_sheets/2018%20Budget%20Fact%20Sheet_Infrastructure%20Initiative.pdf ; Risk and Uncertainty Management Center, Univ. of South Carolina.

Types of Infrastructure Targeted

- **Infrastructure Spending: Eligible Types of Spending**
  - Surface transportation (roads, bridges, etc.)
  - Airports, Rail, Ports and Waterways
  - Water resources (hydro power, drinking water, waste)
  - Brownfield remediation/Superfund sites
  - Broadband
  - Worker education and training
- **Major Challenge: Funding at Federal & State Levels**
  - Deficit consequences of Tax Cuts and Jobs Act limit appetite for additional federal spending
  - States need to participate financially but finances are tight

US Trade Policy

How Will the WC Insurance Industry Be Impacted by Trade Disputes?

81

Trade Actions and Workers Compensation

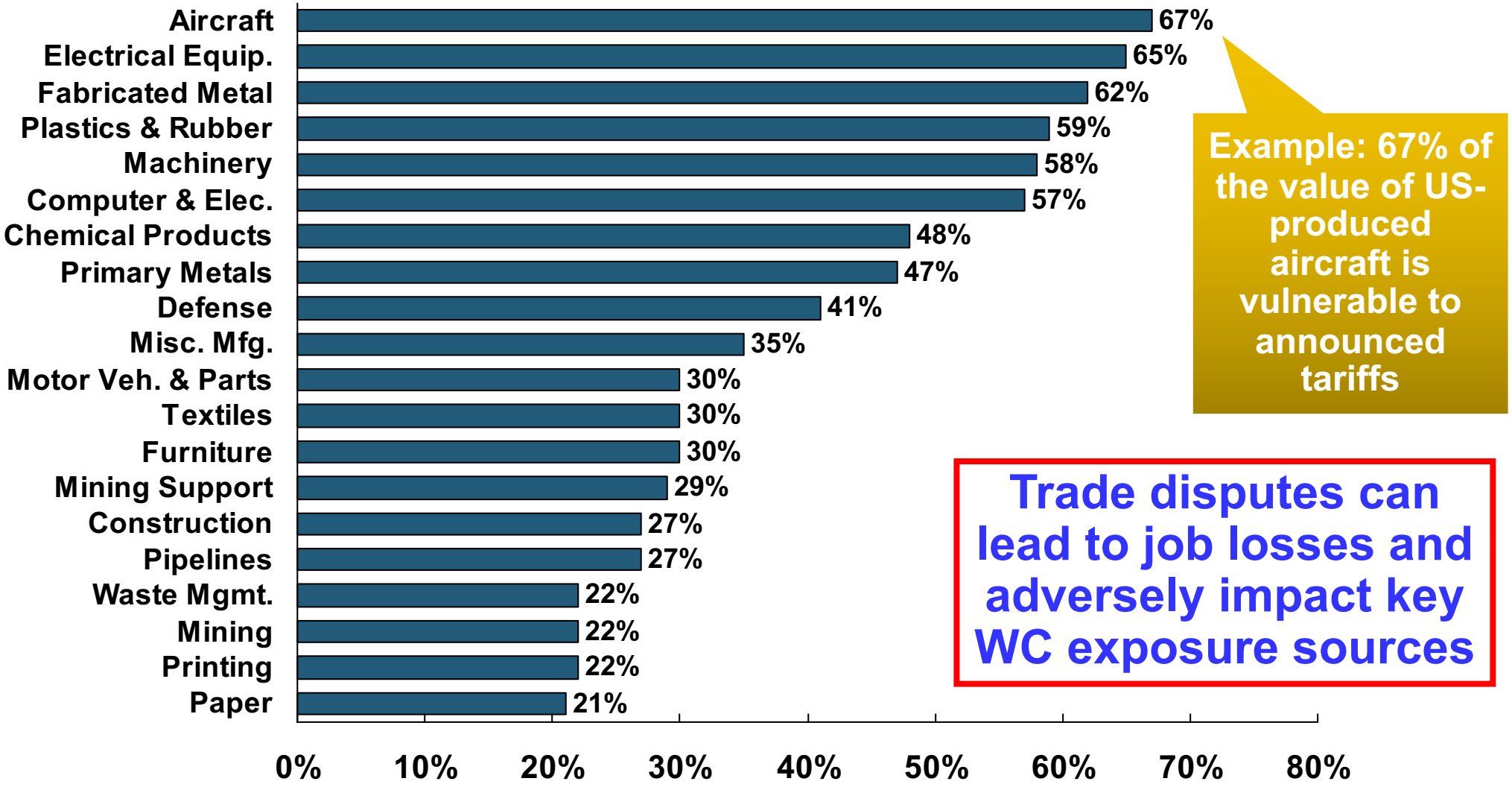
Major Trade Actions Announced so Far

- April 3: $50B in tariffs announced on some 1,300 products produced in China
- March 8: Steel and Aluminum
  - 25% tariff on foreign steel
  - 10% tariff on imported aluminum
- NAFTA renegotiation; TPP pull-out

Potential Impacts: Job and Income Losses Could Be Severe if Targeted Countries Retaliate

- Hundreds of thousands of jobs would be lost across many industries
- WC premium shrinkage would be measured in the billions as hundreds of billions in wages and salaries would be at risk

Dollar Share of Inputs Potentially Impacted by Tariffs on Chinese Goods



Example: 67% of the value of US-produced aircraft is vulnerable to announced tariffs

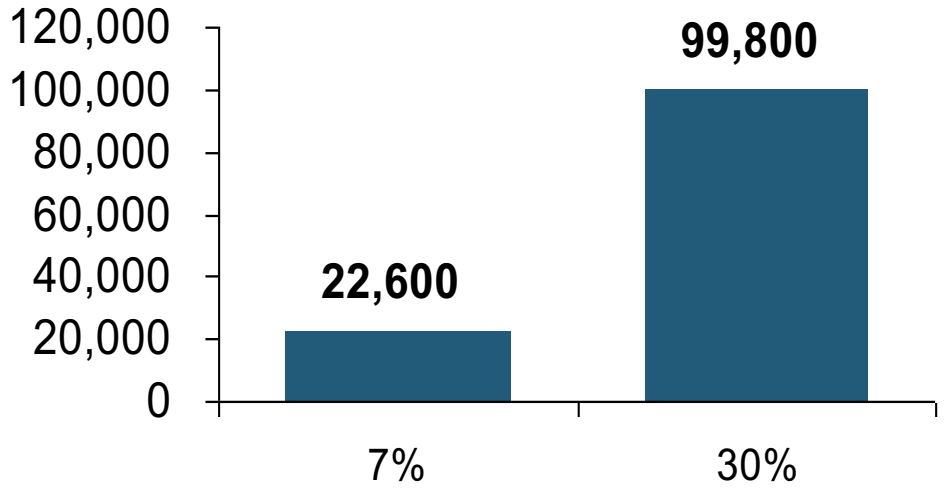
Trade disputes can lead to job losses and adversely impact key WC exposure sources

*Trump administration based on 2017 only and figures is an estimate based on the first three quarters of the year.
**Truman administration ROE of 6.97% based on 3 years only, 1950-52;.
Source: Wells Fargo Securities, *Could Tariffs Gum Up Industry Supply Chains?,* April 12, 2018.

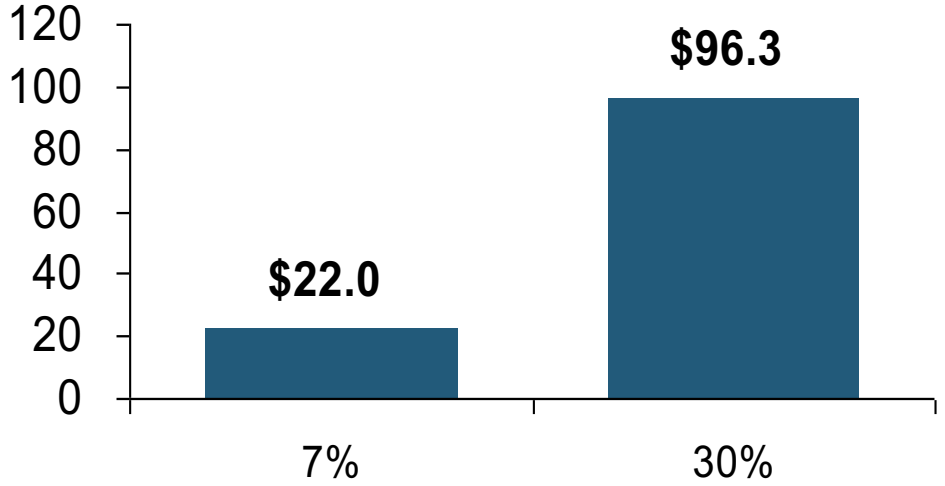
Impacts on Employment and Income from Aluminum Tariffs: 7% and 30% Tariff Scenarios

There is no question that tariffs in the aluminum and steel industry will kill jobs in industries that use these inputs, harming workers comp payroll exposures. The damage will be far worse when foreign countries introduce retaliatory tariffs of their own.

Average Annual Job Losses



Cumulative Personal Income (Wage/Salary) Loss ($ Billions)



Sources: NERA, *Impacts of Potential Aluminum Tariffs on the U.S. Economy,* June 2017.

Summary

The Ever-Changing Economics of Workers Compensation

85

Summary: The Economics of Workers Comp

- **Economy:** The strong economy is the primary driving force behind the majority of commercial exposure growth, including for WC insurers
- **Labor Markets:** Strongest they have been in 18 years
  - Expect employment growth to slow since the economy is at full employment
  - Modest wage pressures should build
- **Investment Earnings:** Gradual improvement as interest rates rise
- **Tax Reform:** New positive for most insurers
- **Trade Disputes:** Unambiguous negative
- **Infrastructure:** Little significant impact

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