P/C Insurance Overview & Outlook for 2023 and Beyond
Insurance at the Economic Crossroads

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P/C Insurance Overview & Outlook: Outline

- Economic Overview & Outlook—Impacts for P/C Insurers
  - Growth, Employment, Inflation, Recession…
- Bank Debacles: Are there Any Impacts for P/C Insurers?
- Inflation: Where it Is Headed & What It Means for P/C Insurers
  - Impacts on claim severities and loss ratios
  - Long-term inflation considerations
- P/C Financial Overview & Outlook in the Post-COVID, High-Inflation Era
  - Premium Growth
  - Underwriting Performance
  - CAT Loss Update
  - Investment Market Issues: Volatility Rules and the Hawkish Fed
- Summary and Q&A

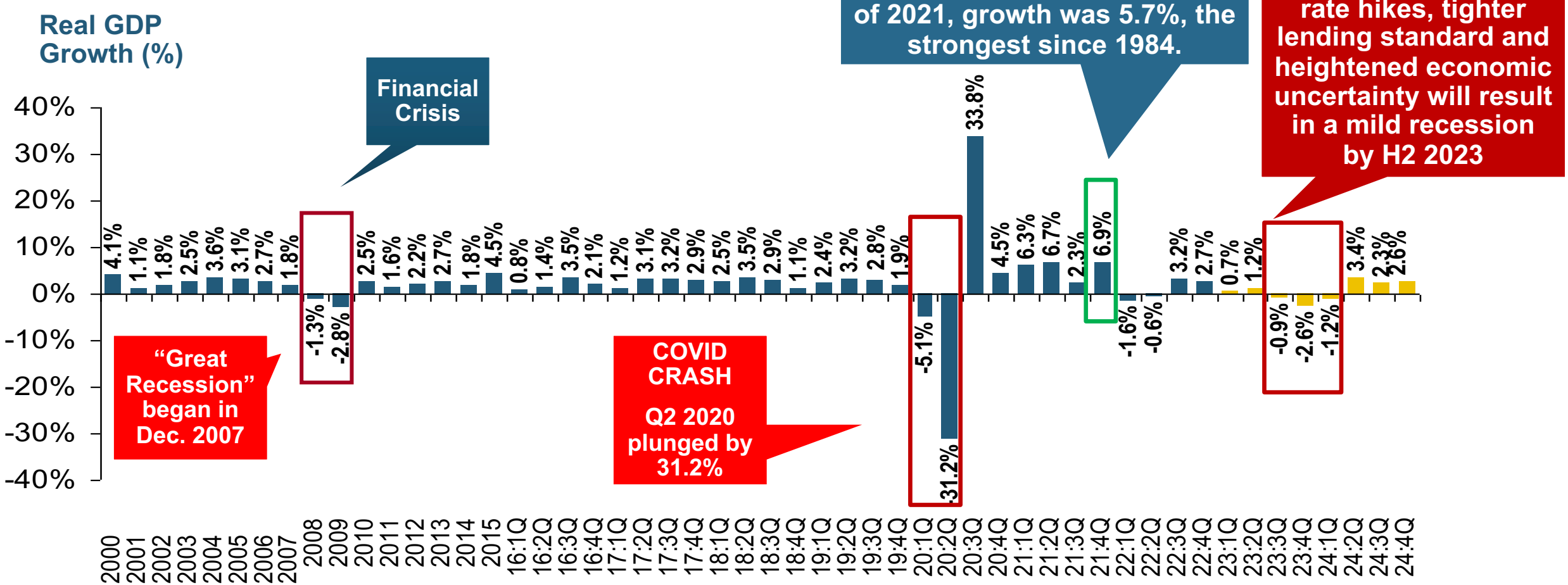
Economic Overview
Economic Optimism Plummeted in 2022
Inflation is Breeding Ground for Pessimism

Inflation, Geopolitical Conflicts and Rising Interest Rates and Weighing Heavily on Business and Consumer Sentiment

Can the Fed "Thread the Needle" and Achieve a "Soft Landing"?

3

US Real GDP Growth*

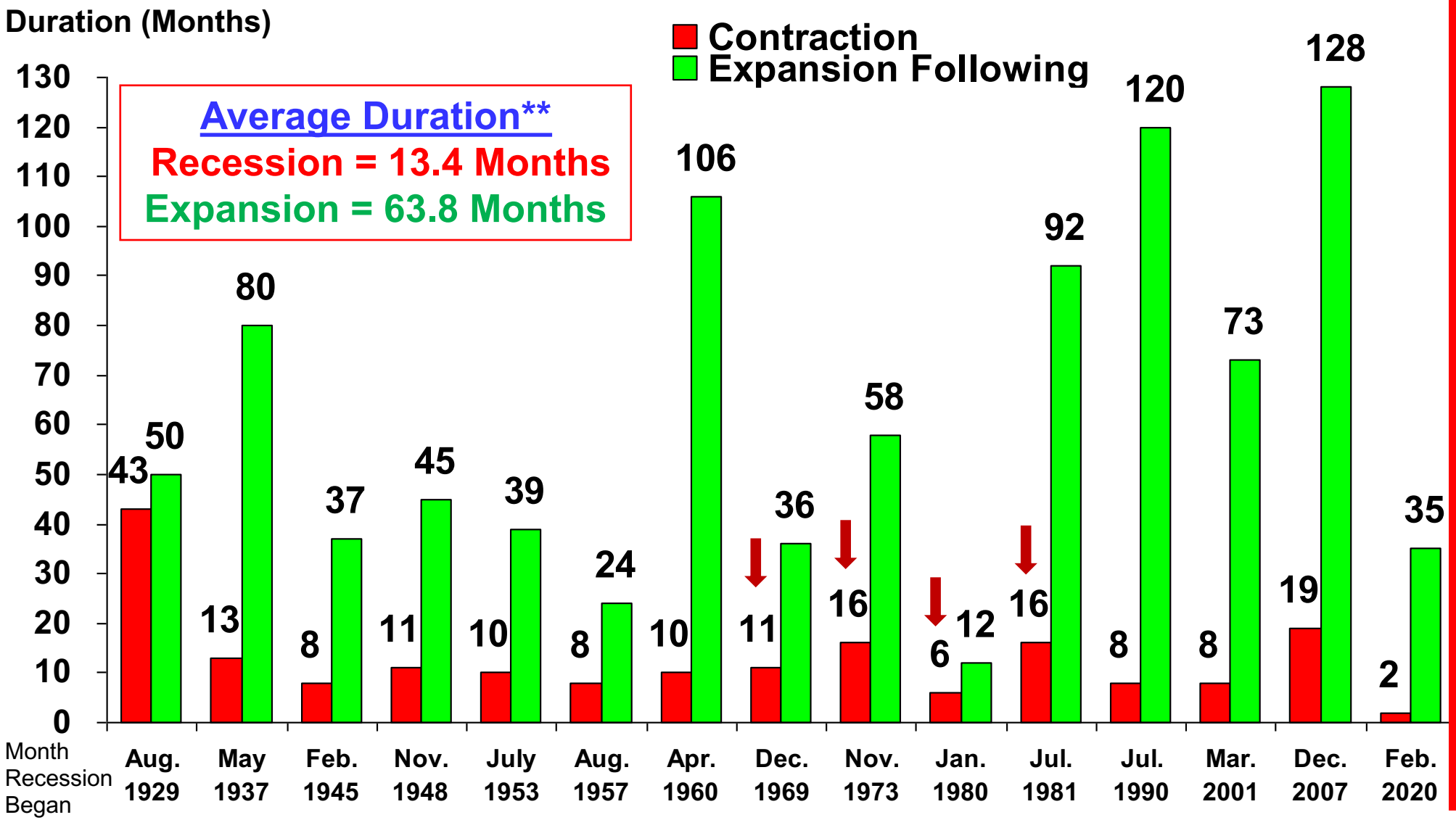


Demand for Insurance Increased Materially in 2021/22 During Recovery from the Pandemic—Particularly in Economically Sensitive Commercial Lines Such as WC. Premium growth will likely slow in 2023 as Economy Slows.

* Estimates/Forecasts from Wells Fargo Securities.

Source: US Department of Commerce, Wells Fargo Securities (3/23); Center for Risk and Uncertainty Management, University of South Carolina.

Length of US Business Cycles, 1929-Present*

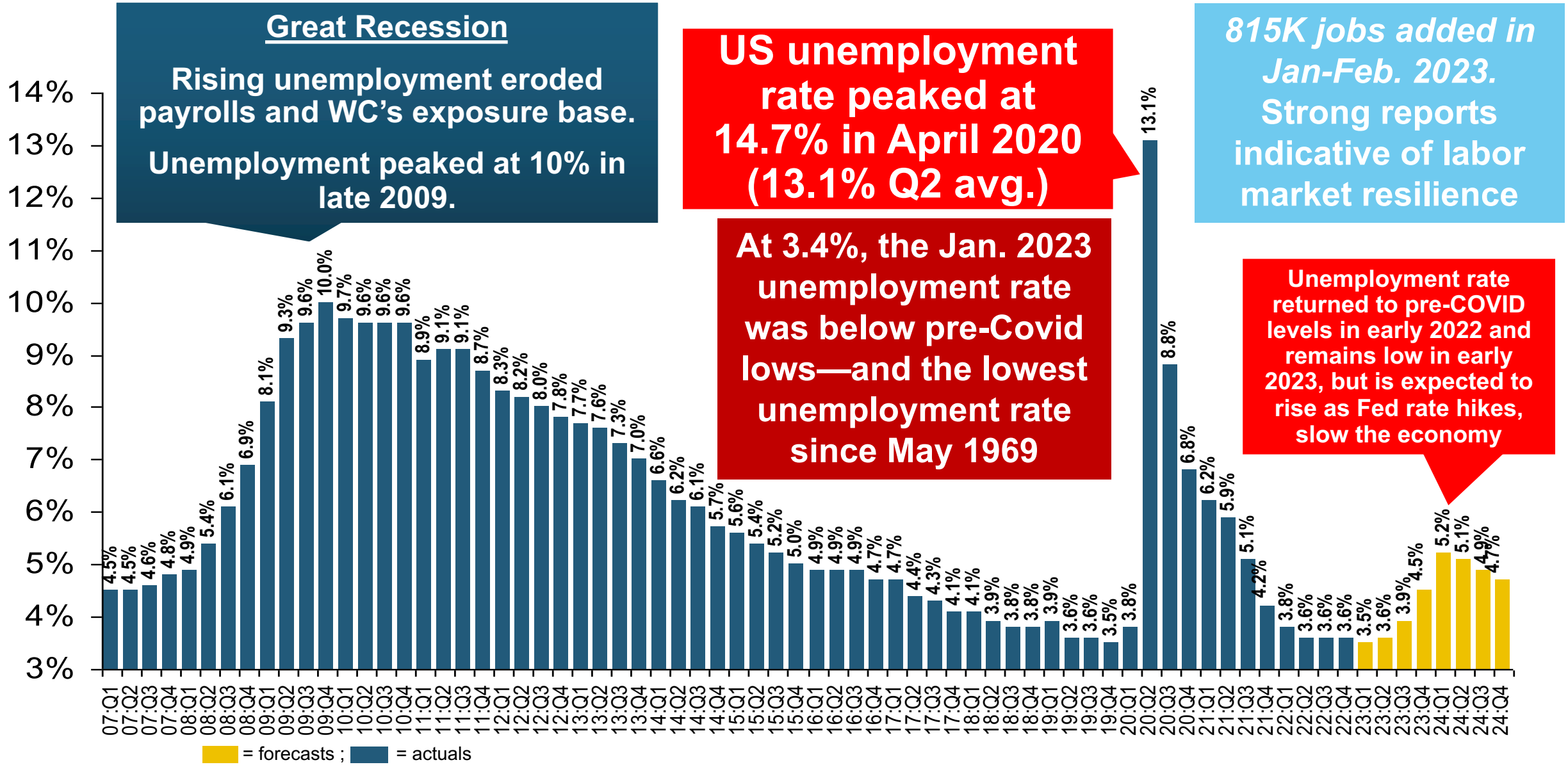


- The Covid recession lasted just 2 months, ending in April 2020, the shortest on record
- Covid abruptly ended the longest economic expansion in US history, which spanned nearly 11 years
- *From 1970 – 1982, the economy was in recession for 48 months through 4 recessions (vs. just 2 months over the past 14 years)*

*Through April 2023. **Excluding Covid-19 recession.

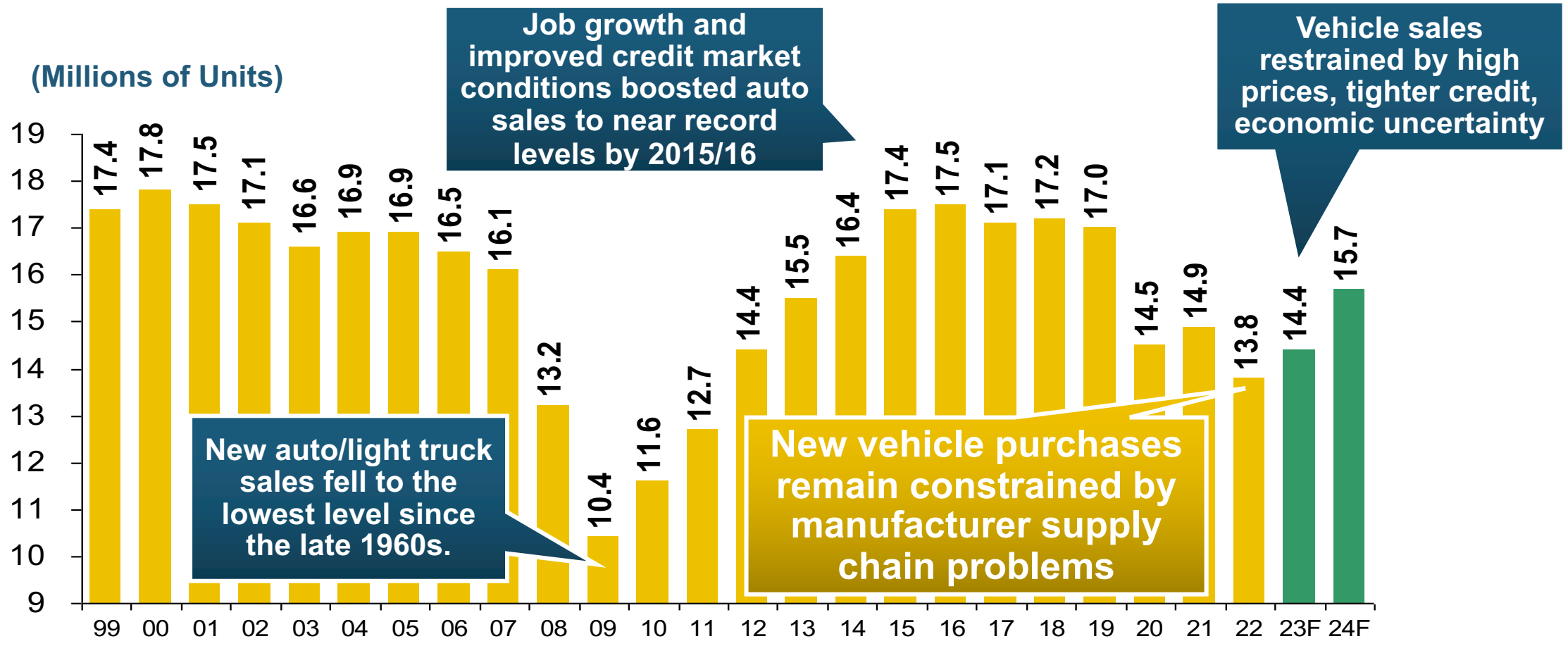
Sources: National Bureau of Economic Research; Risk and Uncertainty Management Center, University of South Carolina.

US Unemployment Rate Forecast: 2007:Q1–2024:Q4



Sources: US Bureau of Labor Statistics; Wells Fargo Securities (3/23 edition); Risk and Uncertainty Management Center, University of South Carolina.

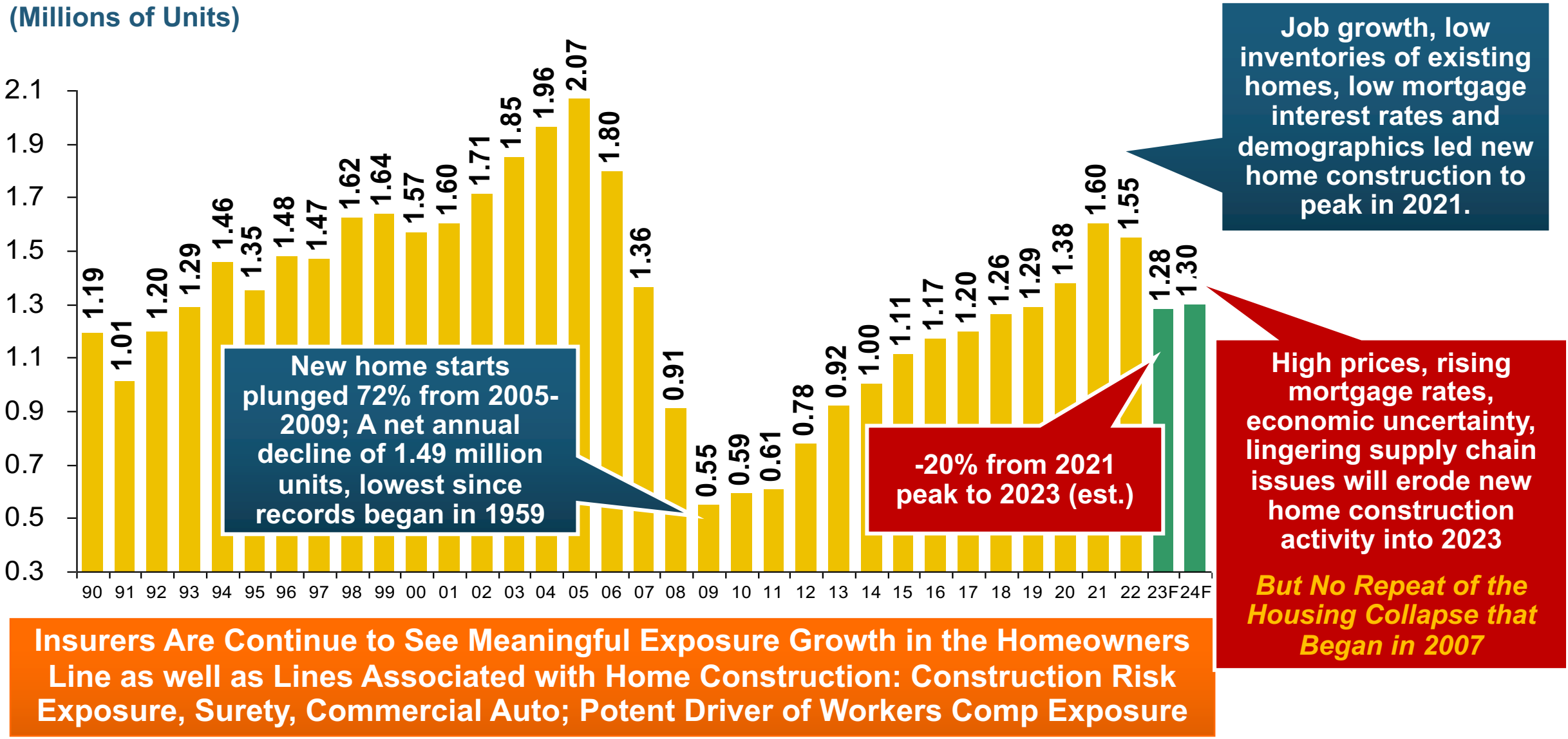
Auto/Light Truck Sales, 1999-2024F



Yearly car/light truck sales remain below pre-COVID levels. Auto manufacturer supply chain issues are expected to linger into early 2023, with tighter credit weighing on sales as well. PP Auto premium might grow by 4%-5%.

Source: U.S. Department of Commerce; Wells Fargo Securities (3/23 for 2022-24F); Univ. of South Carolina, Center for Risk and Uncertainty Management..

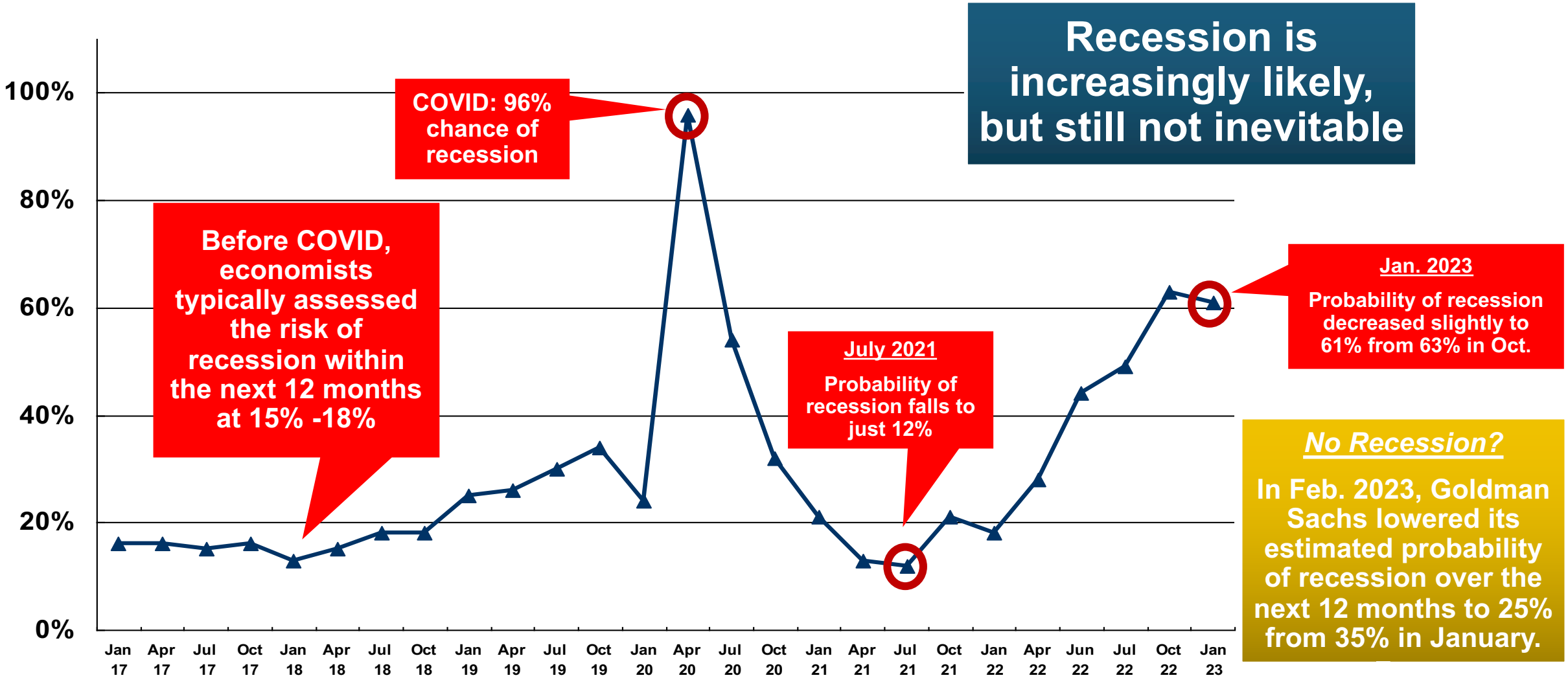
New Private Housing Starts, 1990-2024F



Insurers Are Continue to See Meaningful Exposure Growth in the Homeowners Line as well as Lines Associated with Home Construction: Construction Risk Exposure, Surety, Commercial Auto; Potent Driver of Workers Comp Exposure

Source: U.S. Department of Commerce; Wells Fargo Securities (3/23 for 2022-24); Univ. of South Carolina, Center for Risk and Uncertainty Management..

Probability the U.S. Is in a Recession Within Next 12 Months: Jan. 2017 – Jan. 2023*

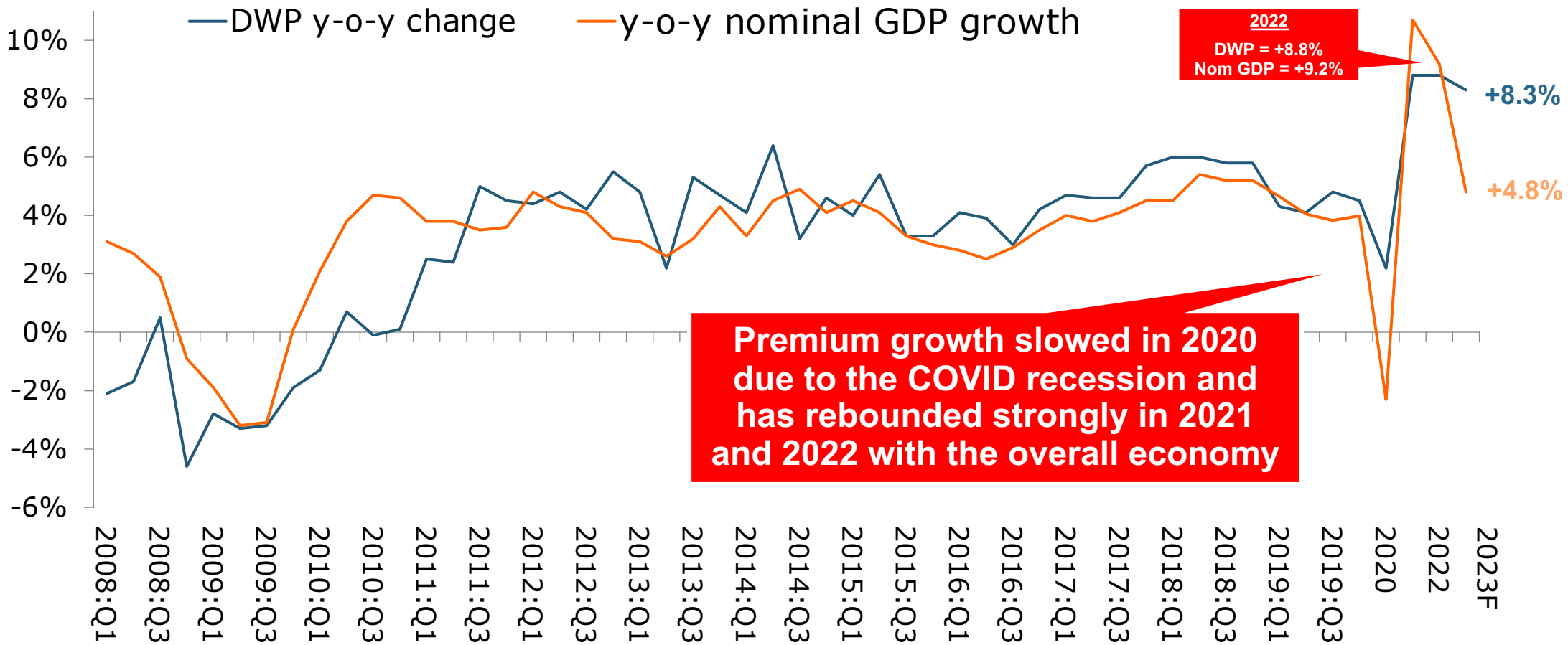


*Jan. 2023 survey included the responses of 71 economists.

Source: Wall Street Journal surveys of economists: https://www.wsj.com/articles/despite-easing-price-pressures-economists-in-wsj-survey-still-see-recession-this-year-11673723571; Risk and Uncertainty Management Center, University of South Carolina.

The Economy Drives P/C Insurance Industry Premiums: 2006:Q1–2023F*

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



Premium growth slowed in 2020 due to the COVID recession and has rebounded strongly in 2021 and 2022 with the overall economy

Direct written premiums track nominal GDP fairly tightly over time, suggesting the P/C insurance industry's growth prospects inextricably linked to economic performance.

*2020-23F figures are annual.

Sources: SNL Financial; U.S. Commerce Dept., Bureau of Economic Analysis; ISO; I.I.I.; Risk and Uncertainty Management Center, University of South Carolina.

Financial Institution Instability

Crisis, Confusion or Contained?

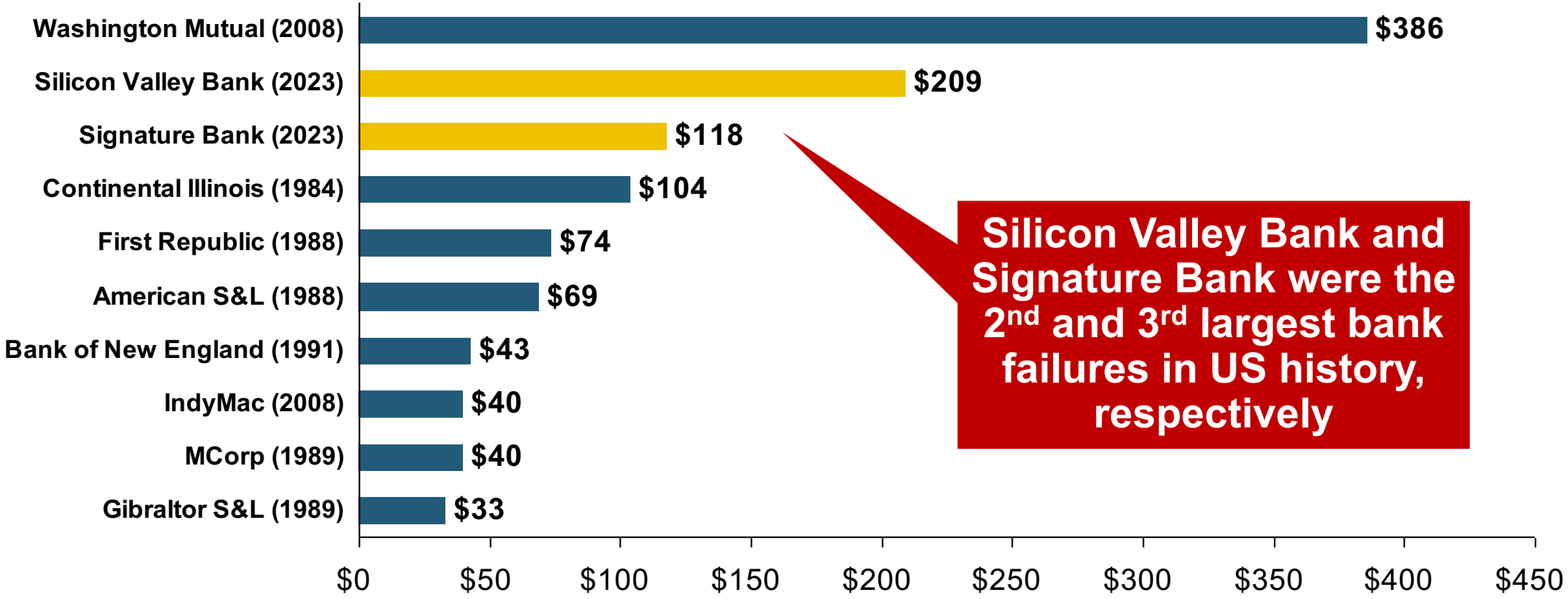
Are Today's Problems Isolated to Banks or Could they Spread to Insurers?

Critical Differences Between Insurers and Banks

Financial System Distress: What's Happened and Why?

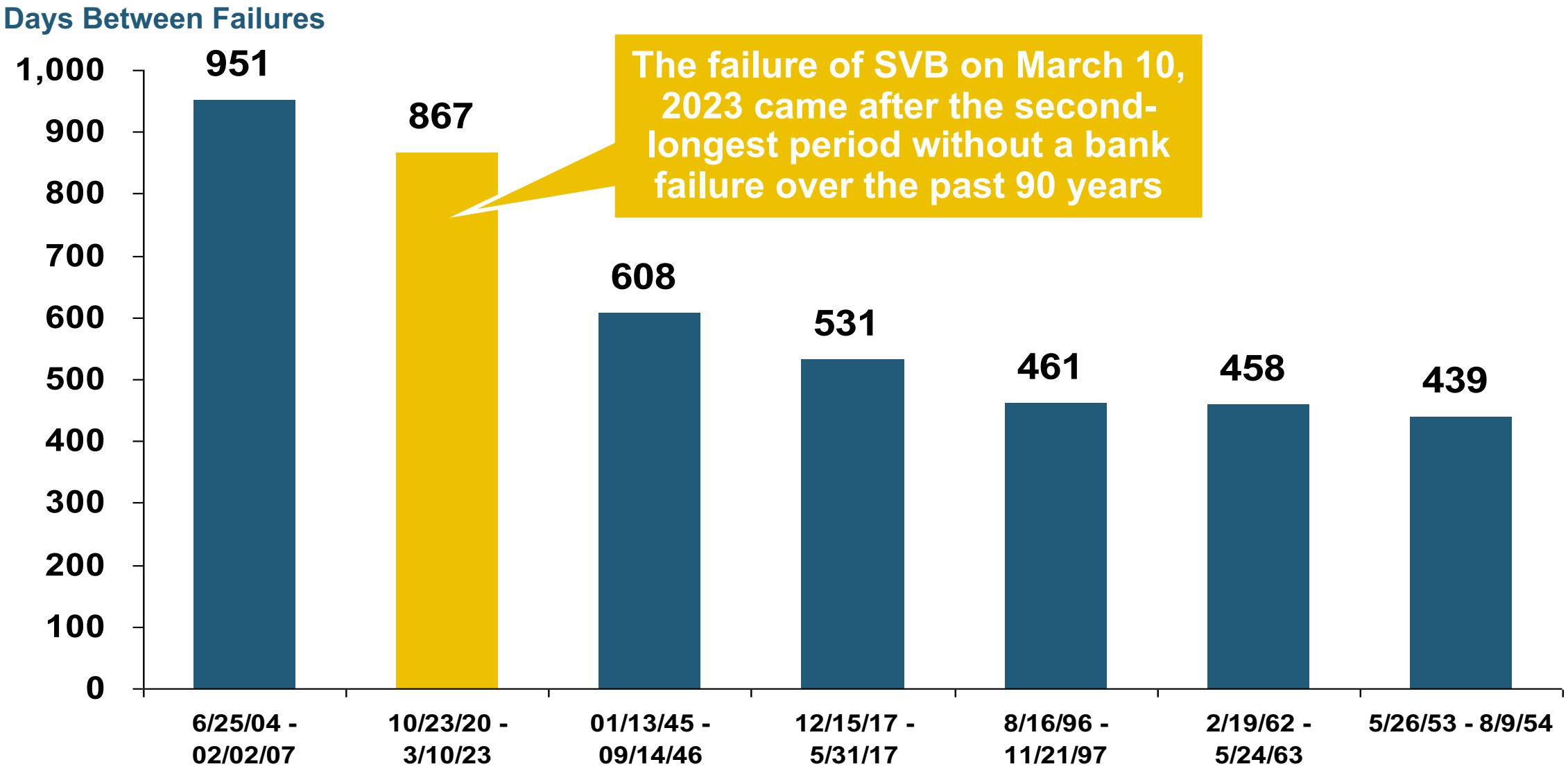
- **Silicon Valley Bank Failed on March 10th — 2nd Largest Failure in US History**
  - Signature Bank failed on March 12th — 3rd largest U.S. failure ever
  - Credit Suisse taken over by UBS on March 19th — raising global concerns
- **What Happened: Focus on Regional Banks at Perceived Risk of Deposit Flight**
  - 85% of SVB deposits above FDIC limit of $250K
  - "Run on Bank" occurred because market value of SVB assets insufficient to honor withdrawals—hence a major liquidity problem
  - Assets were insufficient to cover withdrawals because market value of assets had dropped sharply as Fed increased interest rates sharply
  - SVB depositors were undiversified—predominantly tech start-ups—who were burning through cash rapidly as funding became scarcer in 2022
  - Signature failed for similar reasons, in part due to its exposure to the crypto sector
- **Are Insurers at Risk Too?**
  - Fundamental differences between structure of insurers and banks make this highly unlikely

Top 10 Bank Failures in U.S. History
*(Based on Assets at Time of Failure, $Billions)**



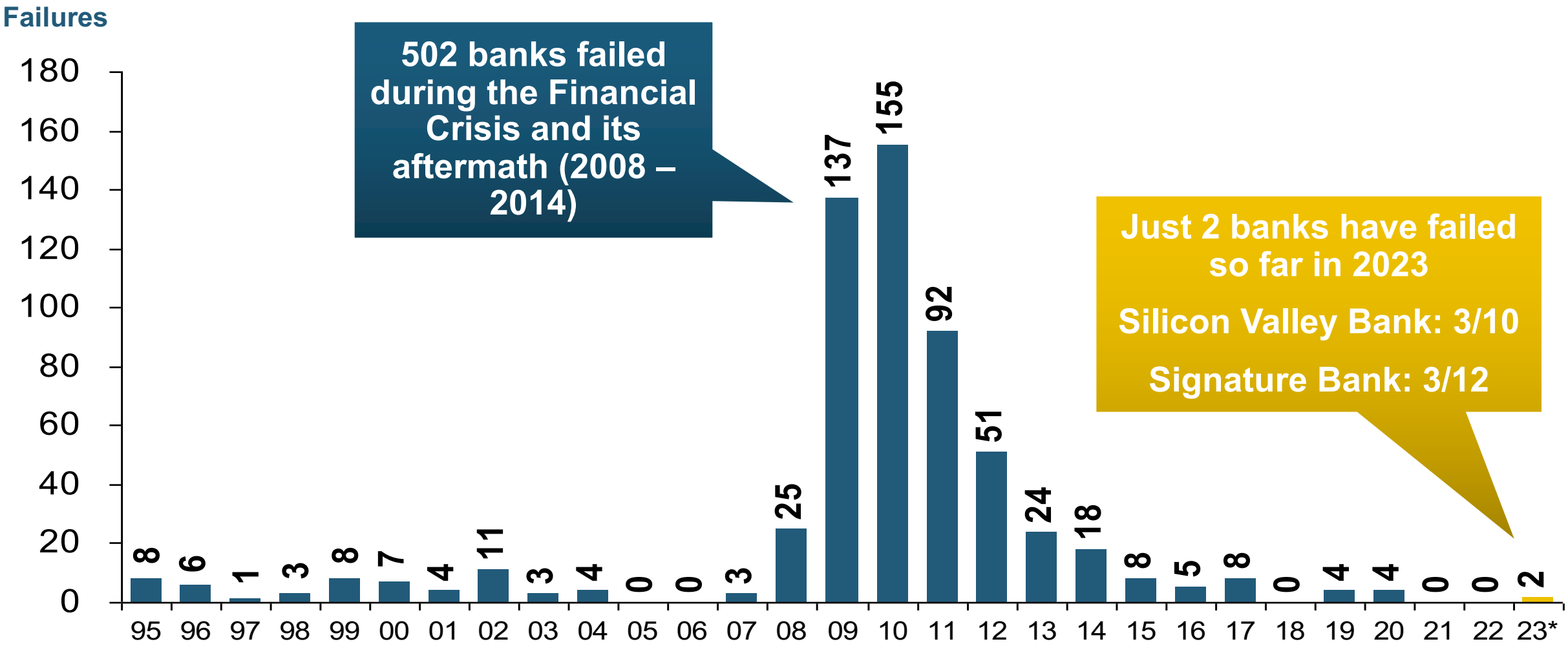
*Figures are inflation-adjusted to 2021 dollars, except Silicon Valley and Signature Bank which are as reported at year-end 2022.
Source: FDIC; USC Risk and Uncertainty Management Center.

Longest Period Between Bank Failures Since 1933*



Sources: FDIC from Bankrate.com accessed at: https://www.bankrate.com/banking/list-of-failed-banks/;
Risk and Uncertainty Management Center, University of South Carolina.

Number of Bank Failures, 1995-2023*



*Through March 28, 2023

Source: FDIC accessed at: https://banks.data.fdic.gov/explore/failures; Univ. of South Carolina, Center for Risk and Uncertainty Management..

Insurance Industry Will Remain Stable Despite Bank Instability

Bottom Line:

- Can't have a "run" on an insurer—liabilities are satisfied by triggering events (e.g., property or auto claim), not on a "demand" basis (e.g., deposits)
- Insurers invest and manage assets very conservatively, focusing on quality and liquidity
- Insurance markets – unlike banking – are operating ***normally***
- The basic function of insurance – the orderly transfer of risk from client to insurer – ***continues uninterrupted***
- This means that insurers continue to:
  - Pay claims (whereas banks need bailouts)
    - ***The promise is being fulfilled***
  - Renew existing policies *(banks are tightening—reducing and eliminating lines of credit*
  - Write new policies *(banks are turning away people and businesses who want or need to borrow)*
  - Compete intensively *(banks are consolidating, reducing consumer choice)*

Source: Risk and Uncertainty Management Center, University of South Carolina.

The U.S. Inflation Threat

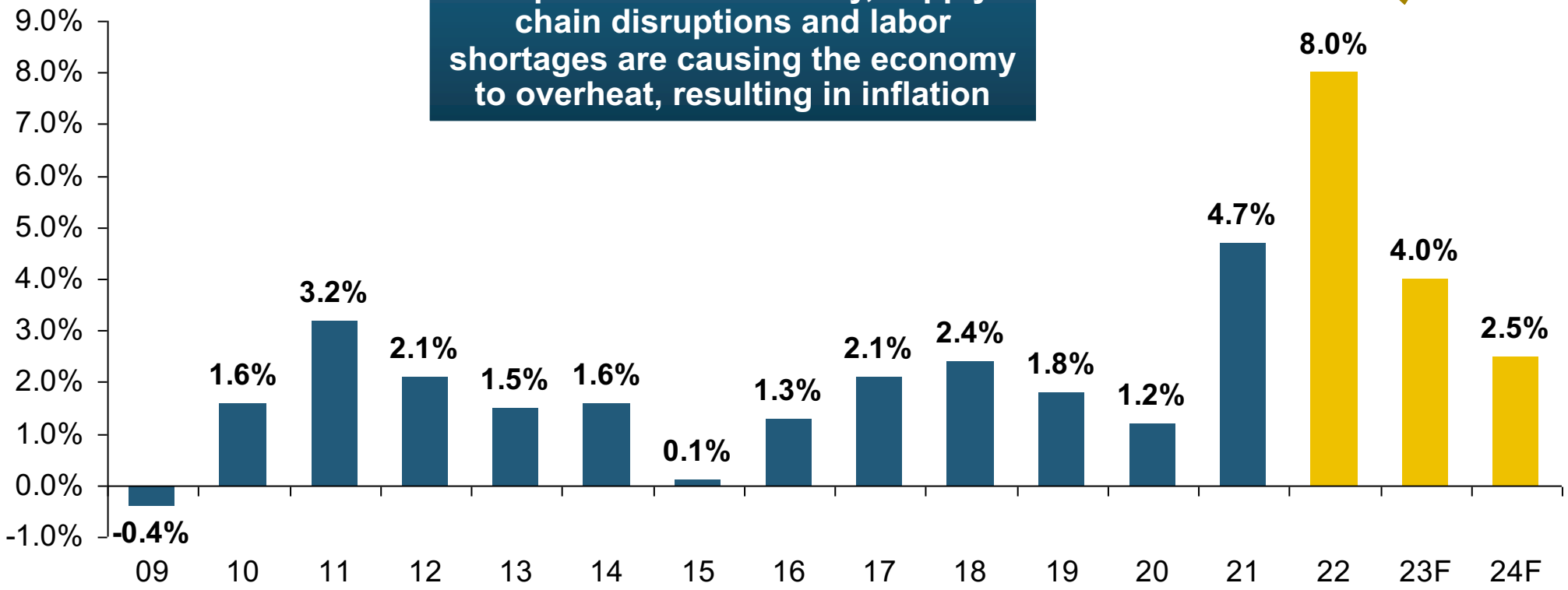
Inflation is the #1 Concern of U.S. Consumers and Corporations…

It's Also a Major Concern of Insurers

U.S. Inflation Rate: 2009-2024F*

Inflation accelerated sharply in 2021 before peaking at 9.1% in June 2022. Inflation should moderate through 2023/24; Forecast is highly dependent of trajectory of energy prices and Fed rate hikes.

There's a great deal of concern that trillions of dollars of stimulus plus the post-COVID recovery, supply chain disruptions and labor shortages are causing the economy to overheat, resulting in inflation



Insurer Concerns About Inflation

Rate Inadequacy

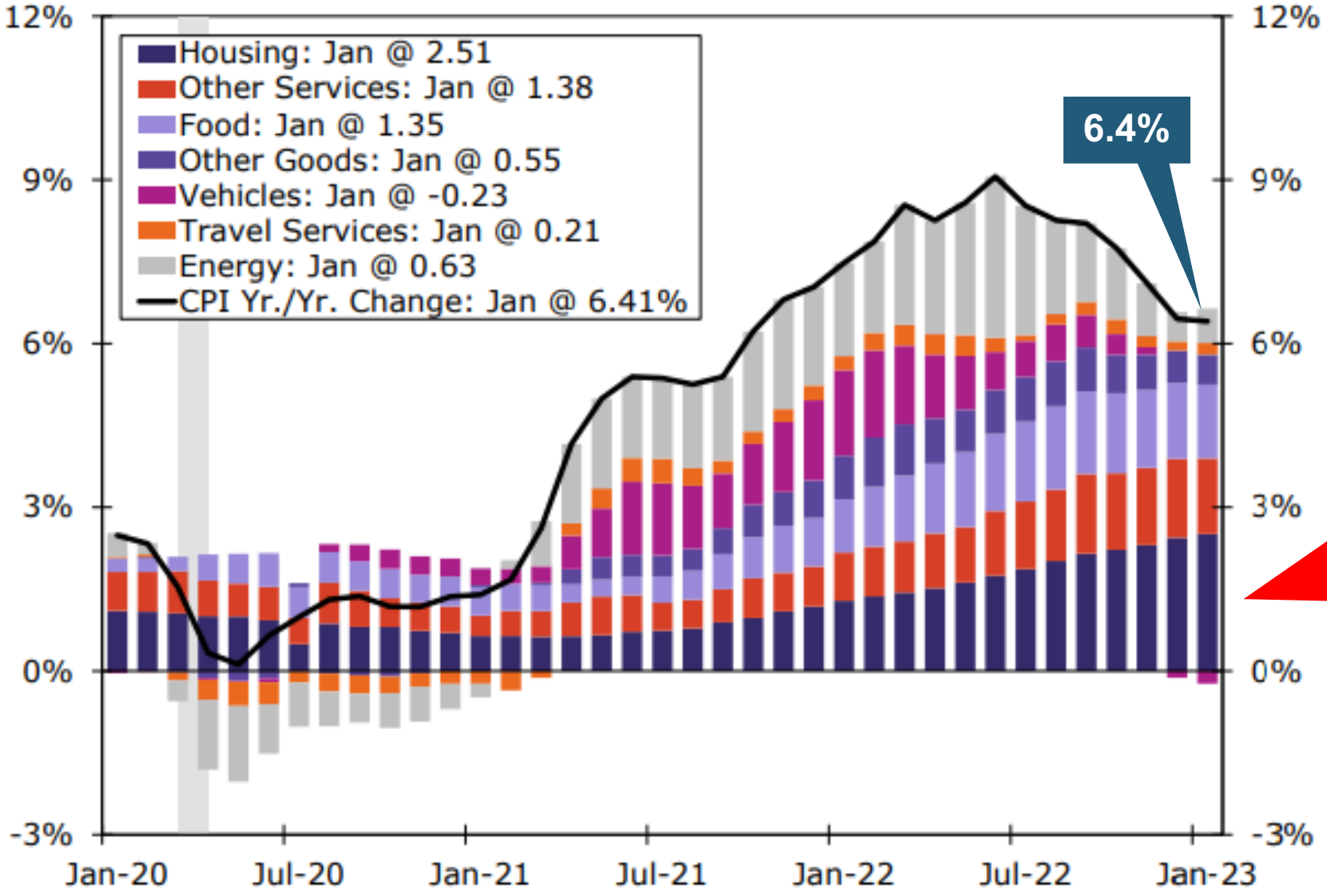
Reserve Inadequacy

Insurance-to-Value

*Annual change in Consumer Price Index for All Urban Consumers (CPI-U).

Source: U.S. Bureau of Labor Statistics; Wells Fargo Securities (3/23); USC Center for Risk and Uncertainty Management.

Contribution to CPI by Category: January 2023

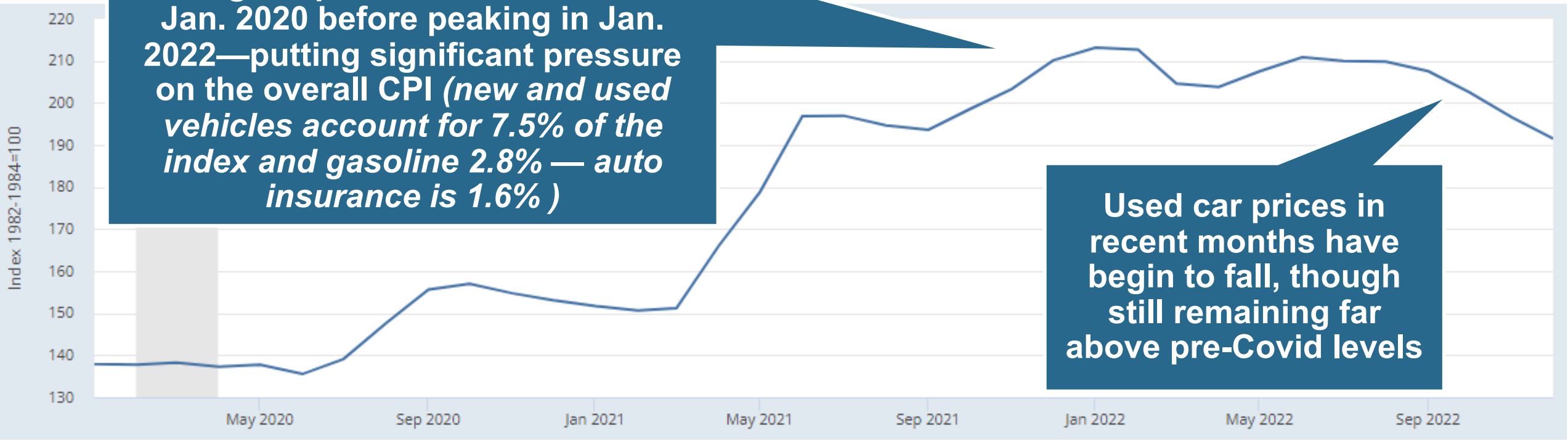


Prices were up 6.4% in Jan. 2023 vs. a year ago, down from the June 2022 peak of 9.1%. Even as energy prices recede fom their 2022 peak, increases in Housing, Food, and Other Services are the major obstacles to tempering inflation

Source: U.S. Department of Commerce and Wells Fargo Economics.

Price Index Changes for Used Cars & Trucks, Jan. 2020 – Dec. 2022

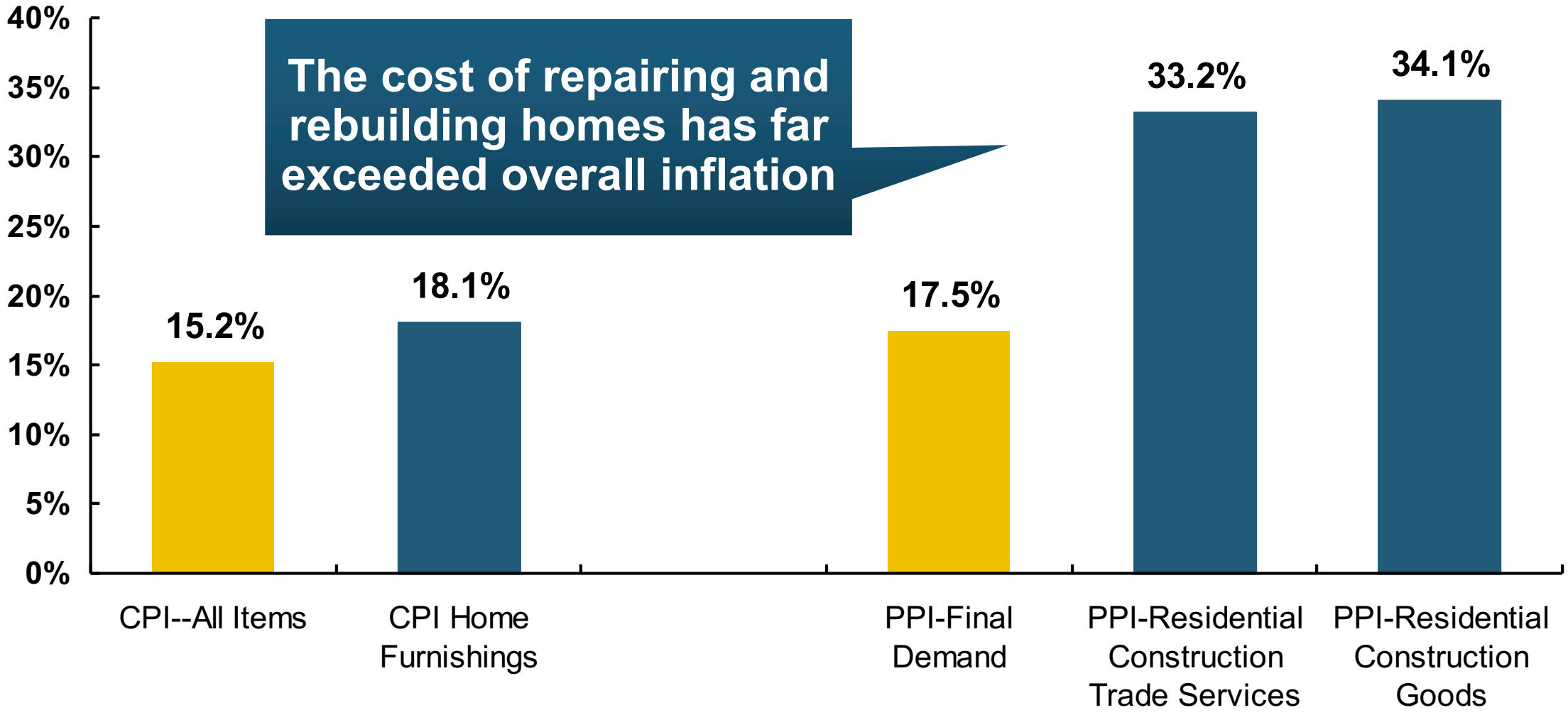
New and Used Vehicle prices surged during the pandemic, +52.3% from Jan. 2020 before peaking in Jan. 2022—putting significant pressure on the overall CPI *(new and used vehicles account for 7.5% of the index and gasoline 2.8% — auto insurance is 1.6%)*



Used car prices in recent months have begin to fall, though still remaining far above pre-Covid levels

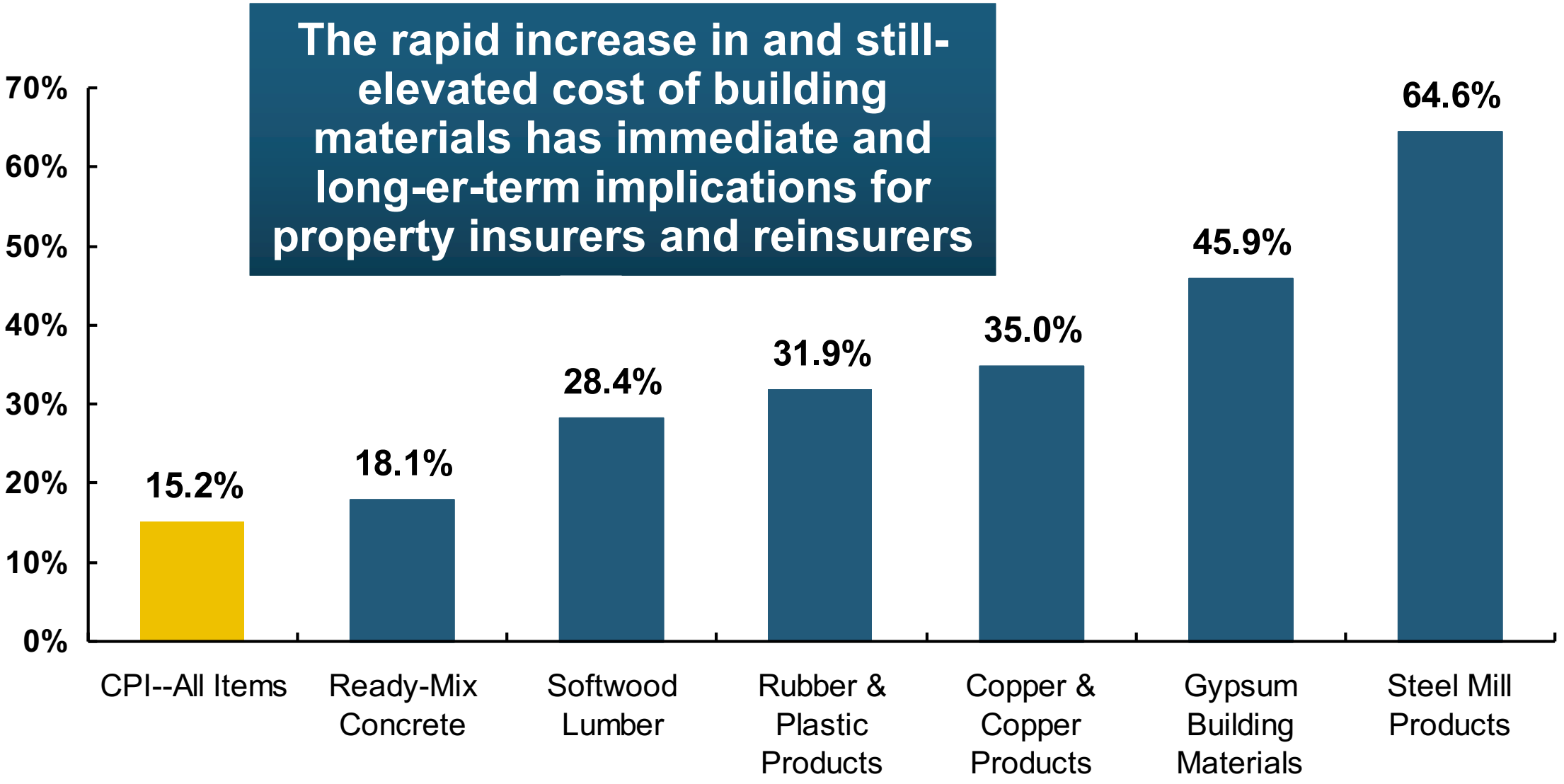
Sources: US Bureau of Labor Statistics; Risk and Uncertainty Management Center, University of South Carolina.

Change in Cost Indicators for Home Insurance (U.S.), Jan. 2020 – Dec. 2022



Source: U.S. Bureau of Labor Statistics.

Change in Cost Indicators for Home Insurance (U.S.), Jan. 2020 – Dec. 2022

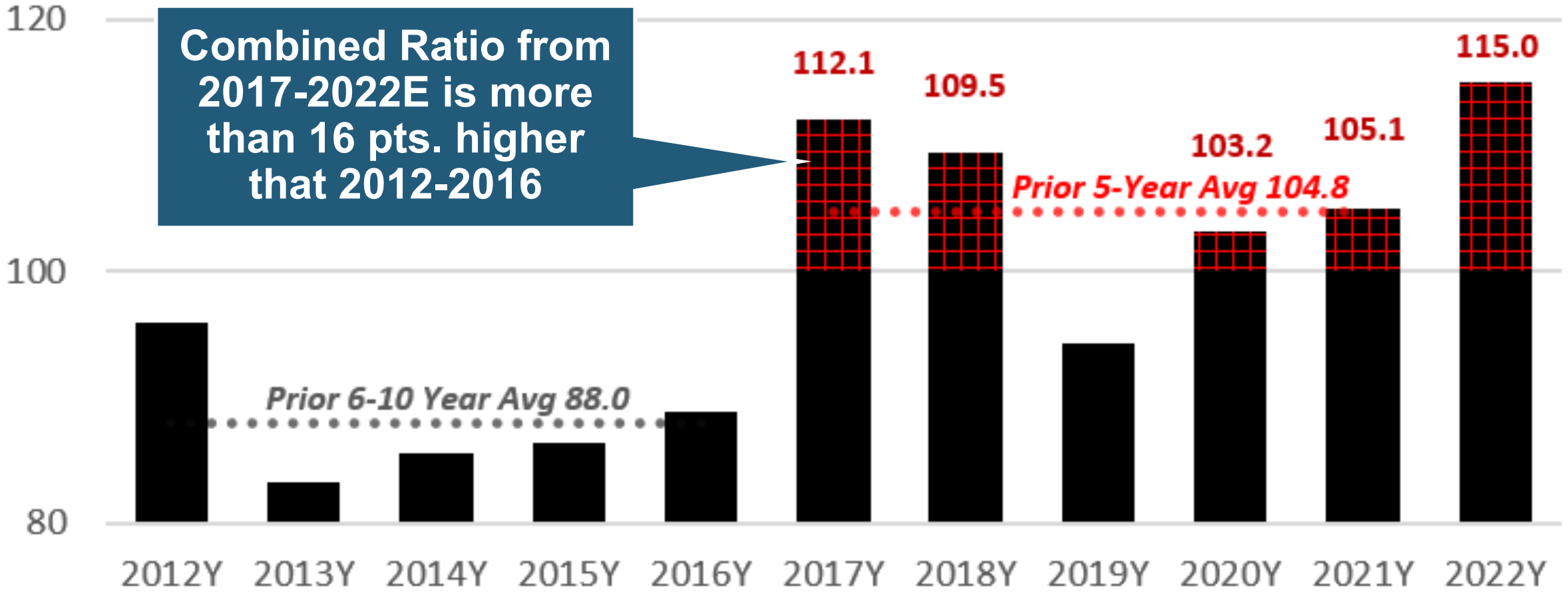


Source: U.S. Bureau of Labor Statistics.

Producer Price Index: Lumber and Wood Products, Jan. 2020 – Dec. 2022

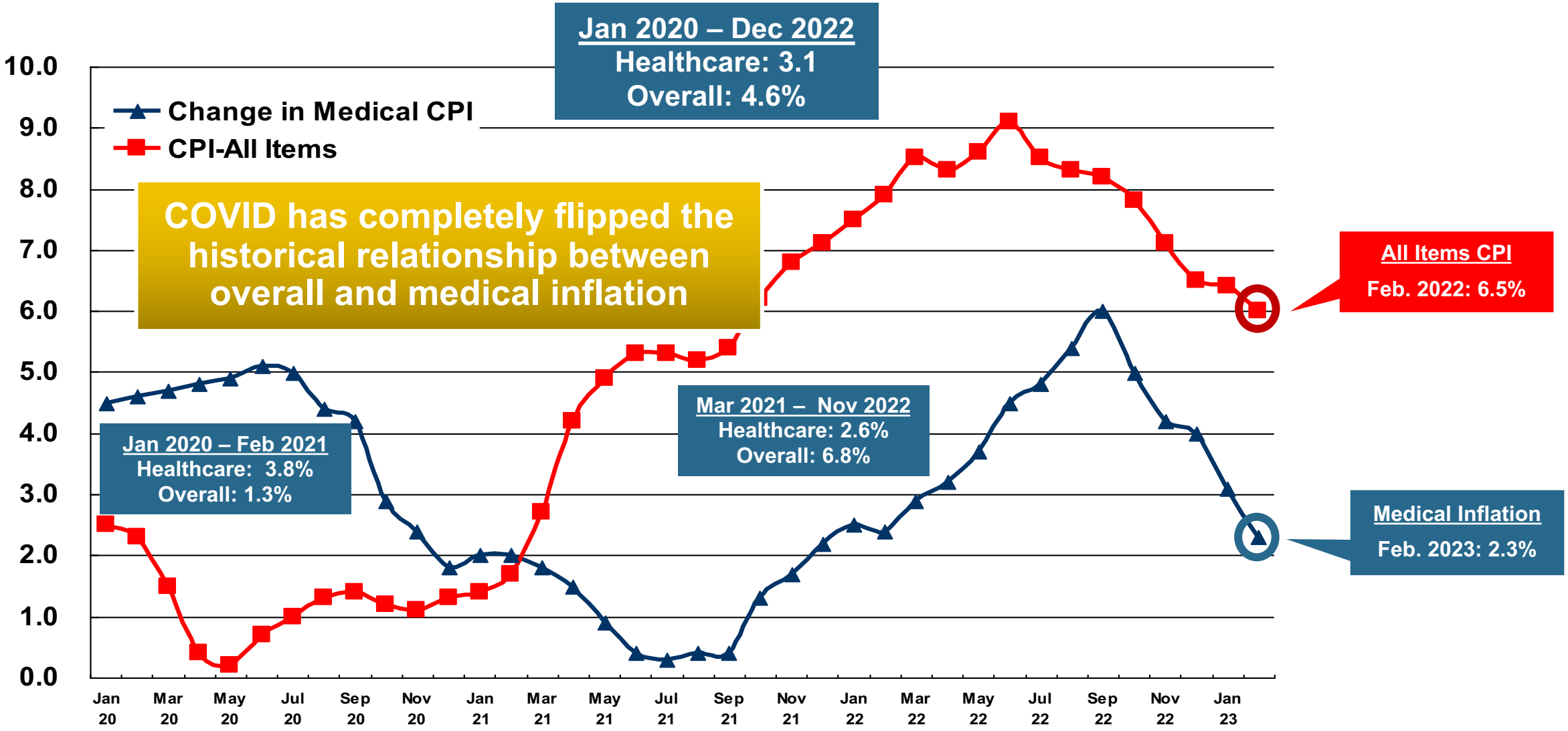
Sources: US Bureau of Labor Statistics; Risk and Uncertainty Management Center, University of South Carolina.

Homeowners Combined Ratio, 2012-2022E: Shows the Combined Effects of Record CATs and Inflation



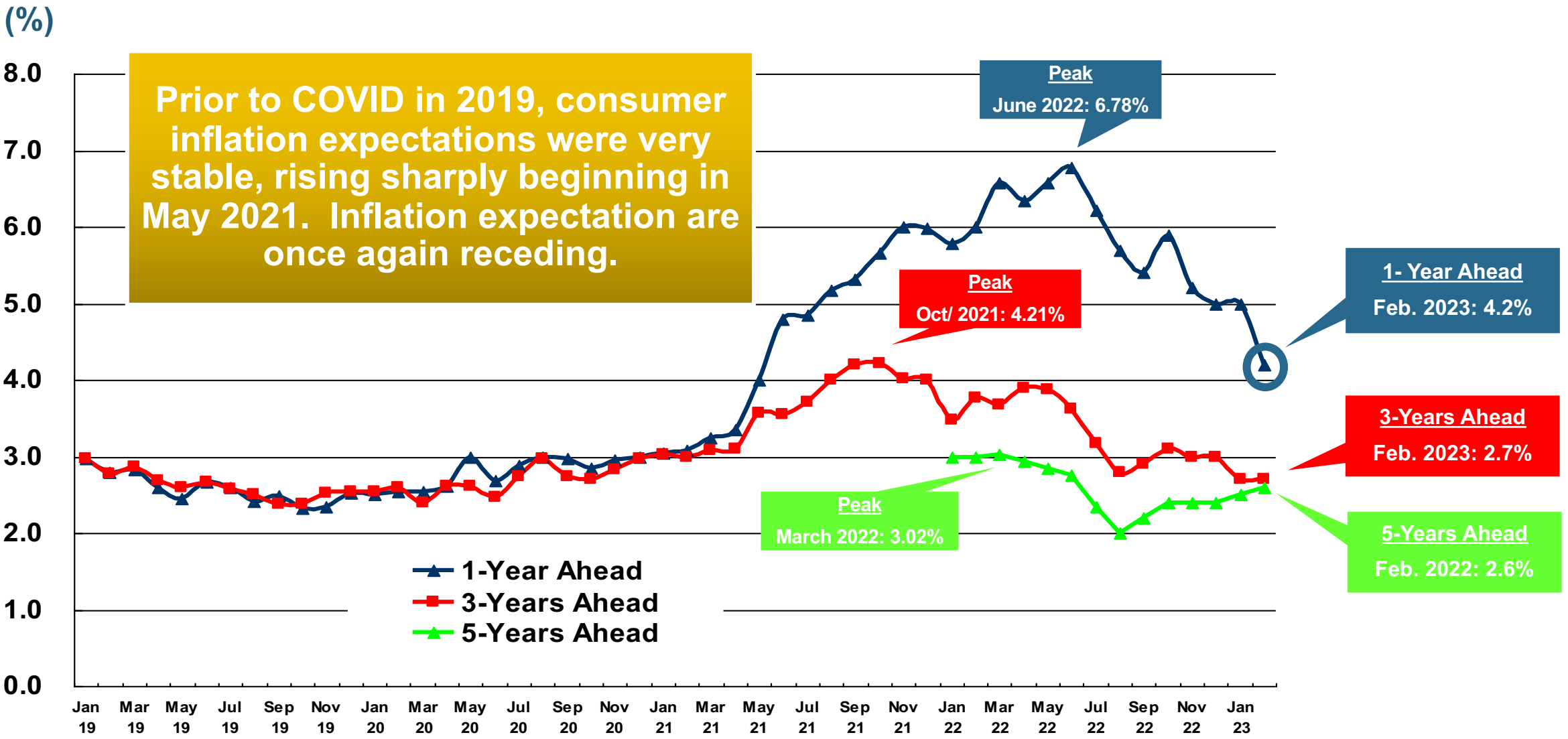
Source: APCIA using S&P Global Markets Intelligence; 2022 estimate is from Triple-I and Milliman (Nov. 2022).

Medical Cost Inflation vs. Overall CPI During COVID, Jan. 2020 – Feb. 2023 *(Percent Change from Year Ago)*



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

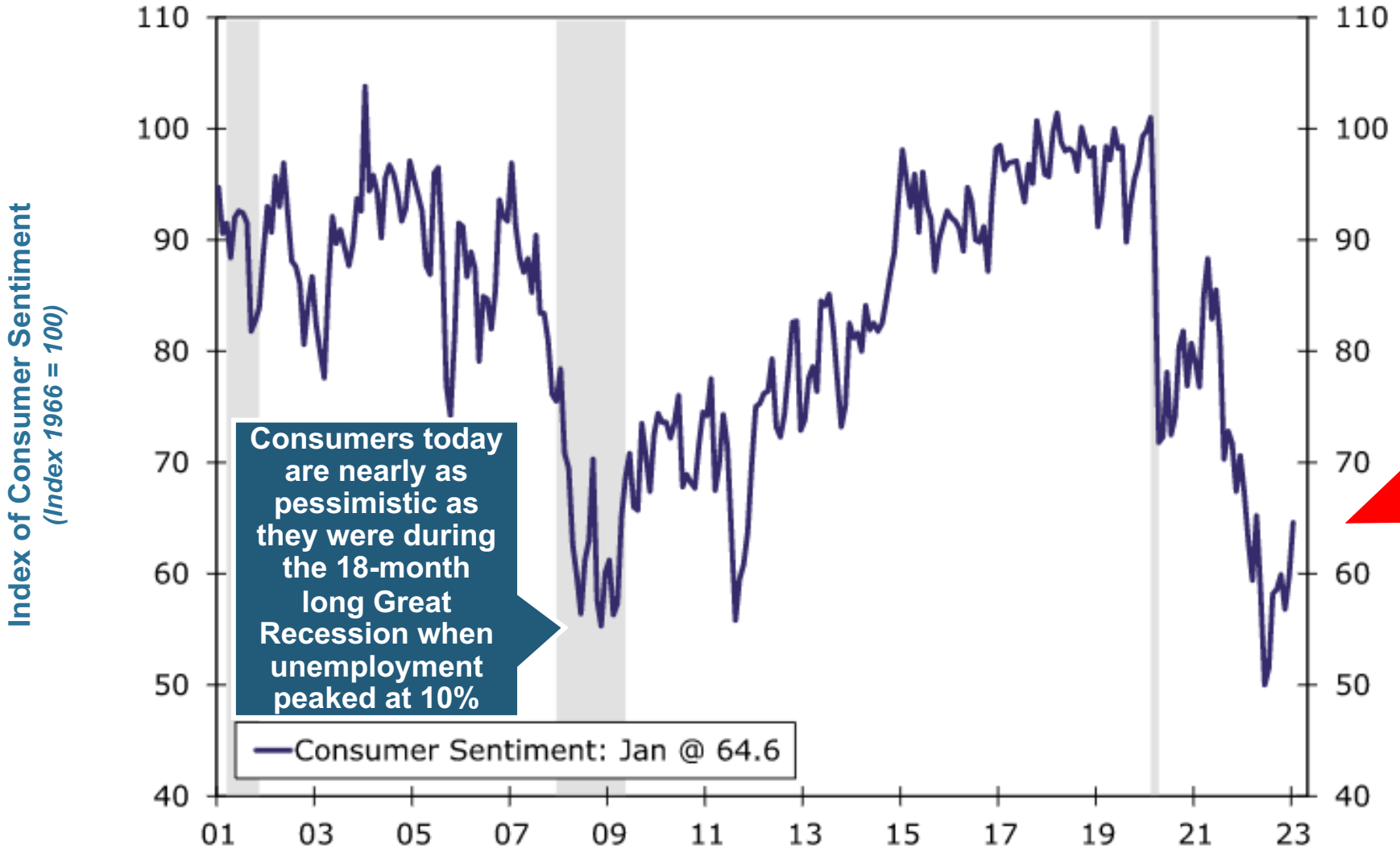
Consumer Inflation Expectations: 1, 3 and 5 Years Ahead*



*Survey data for 5-year ahead series begin in January 2022.

Sources: Federal Reserve Bank of New York, accessed at: https://www.newyorkfed.org/microeconomics/sce#/inflexp-1; Risk and Uncertainty Management Center, University of South Carolina.

Consumer Sentiment: Close to the Lowest Ever in 2022 Despite Strong Jobs Markets—But Now Rebounding



Despite unemployment rates that are among the lowest in 50+ years and the "end" of the COVID pandemic, consumers are *GRUMPY*—sentiments improved in late 2022/early 2023

Source: University of Michigan and Wells Fargo Economics.

Annual Change in Average Hourly Wage, 2007–2022*

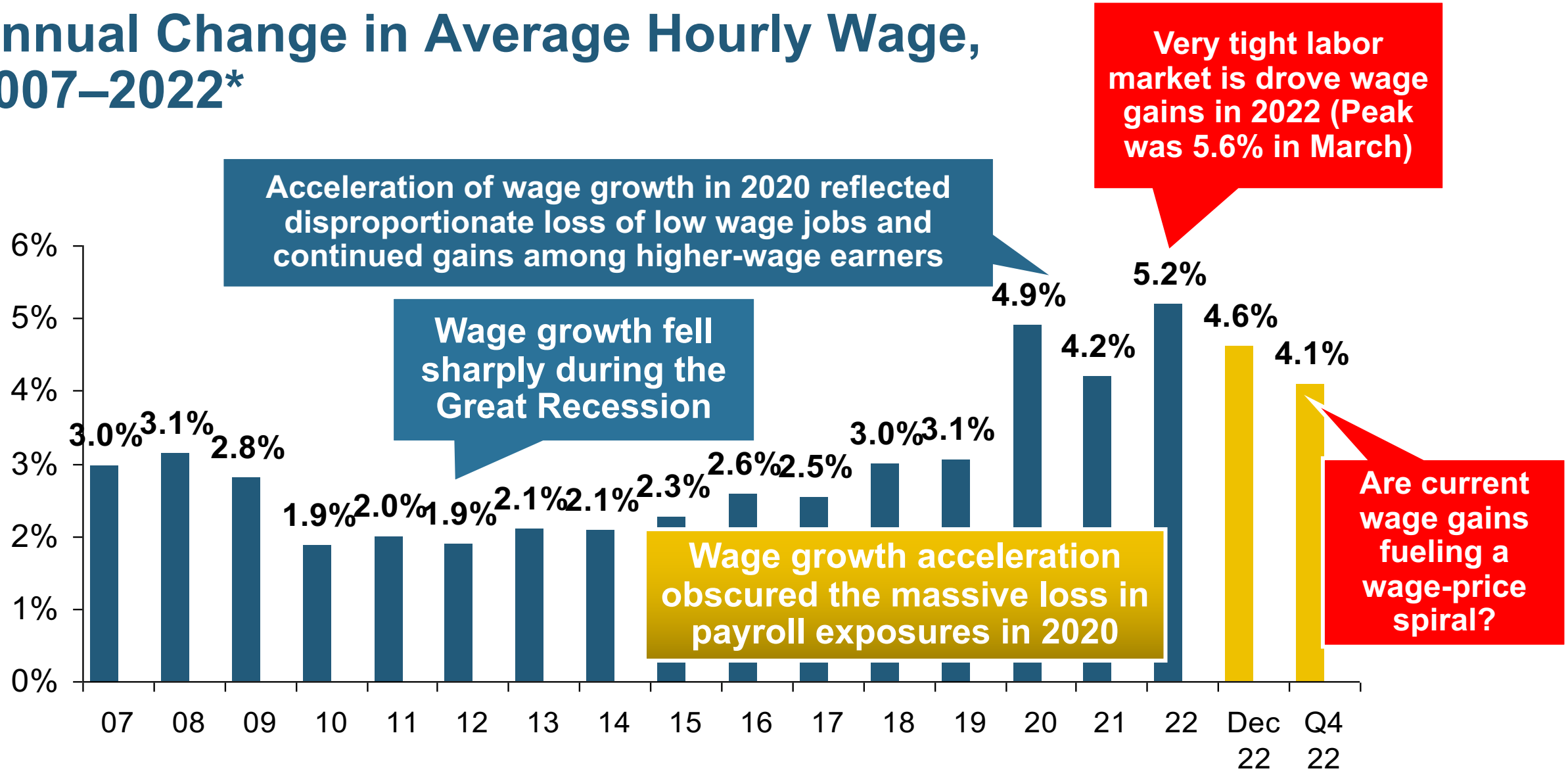
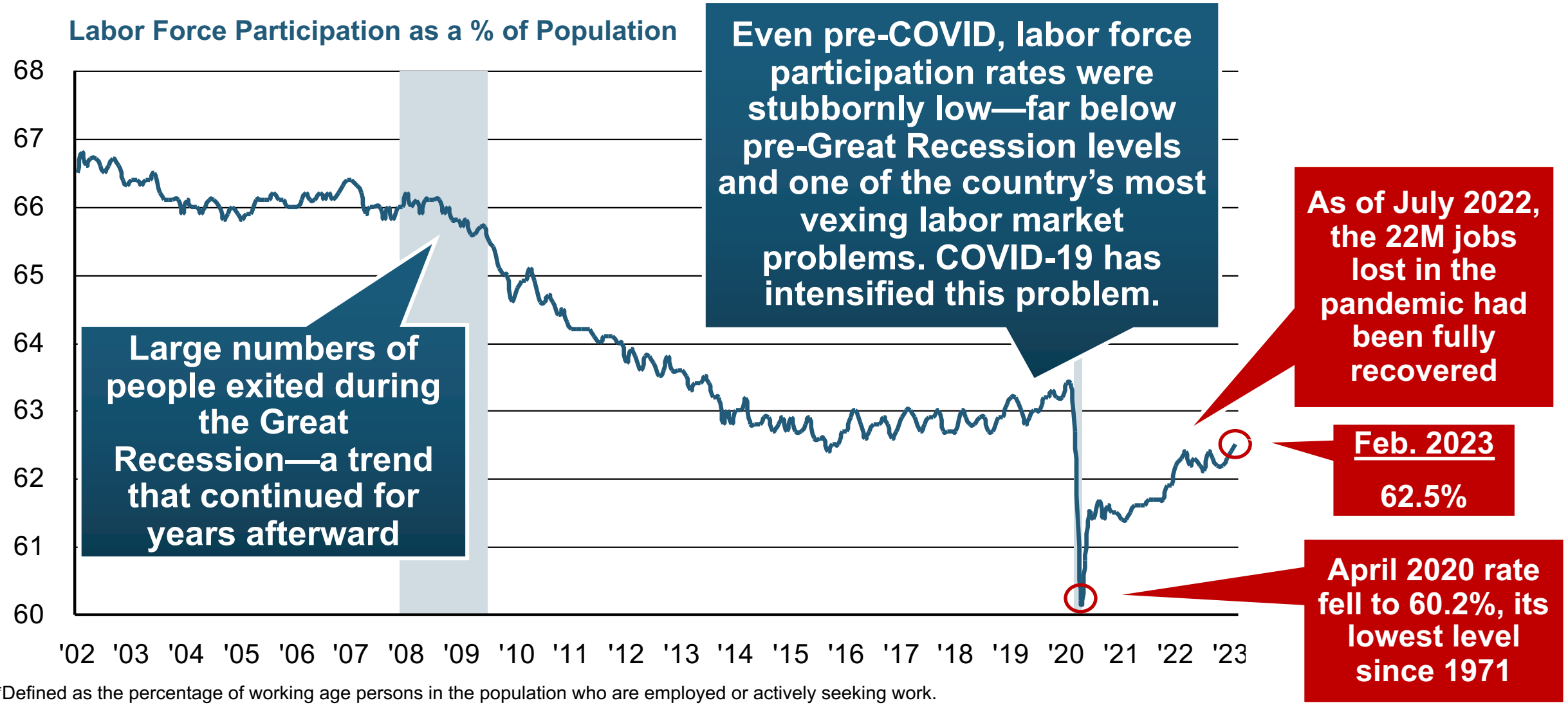


*Figure is year-over-year change from Dec. 2021 to Dec. 2022.

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.

Labor Force Participation Rate, Jan. 2002–Feb. 2023*



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

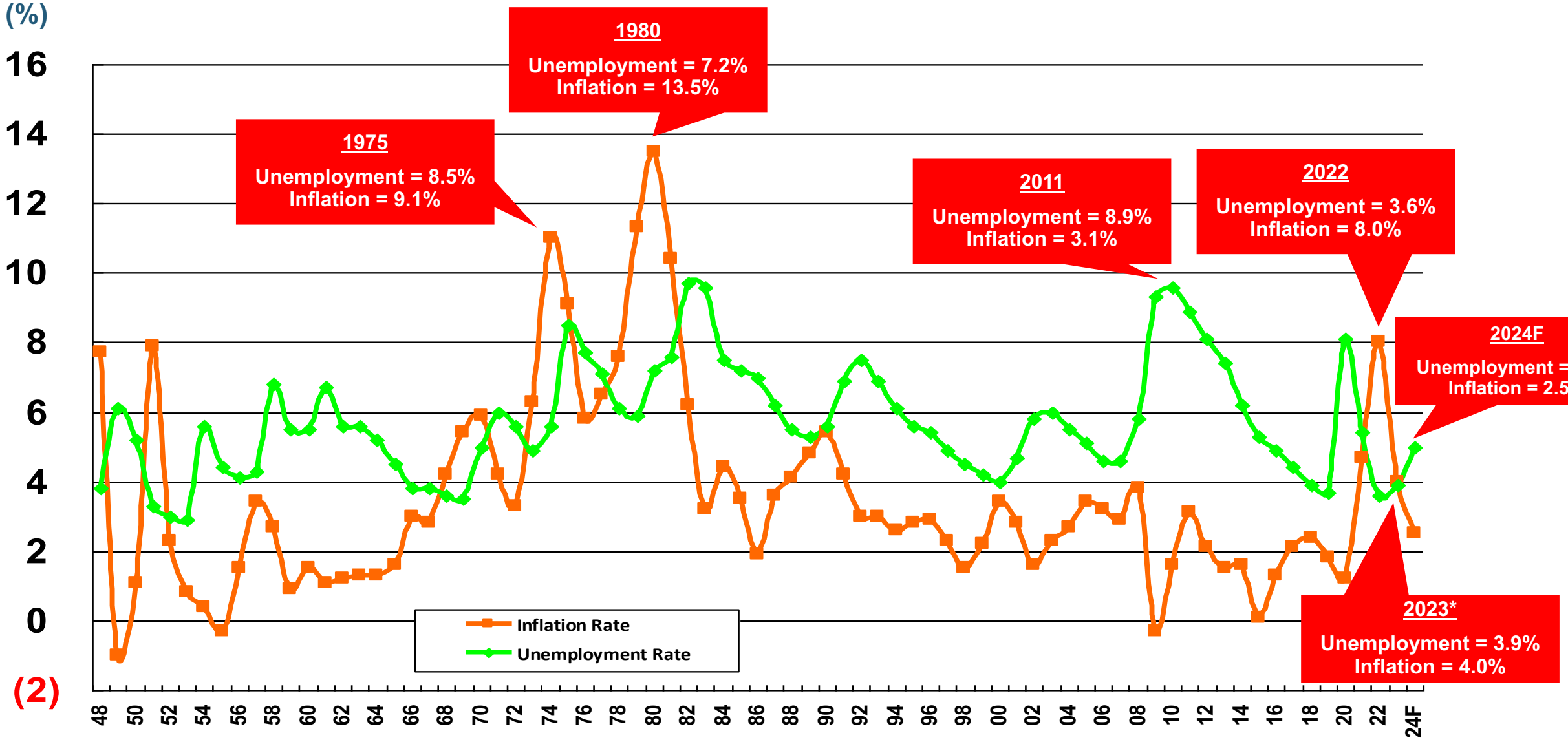
Note: Recessions indicated by gray shaded columns.

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.

Are Things As Bad as Many Believe Them to Be?

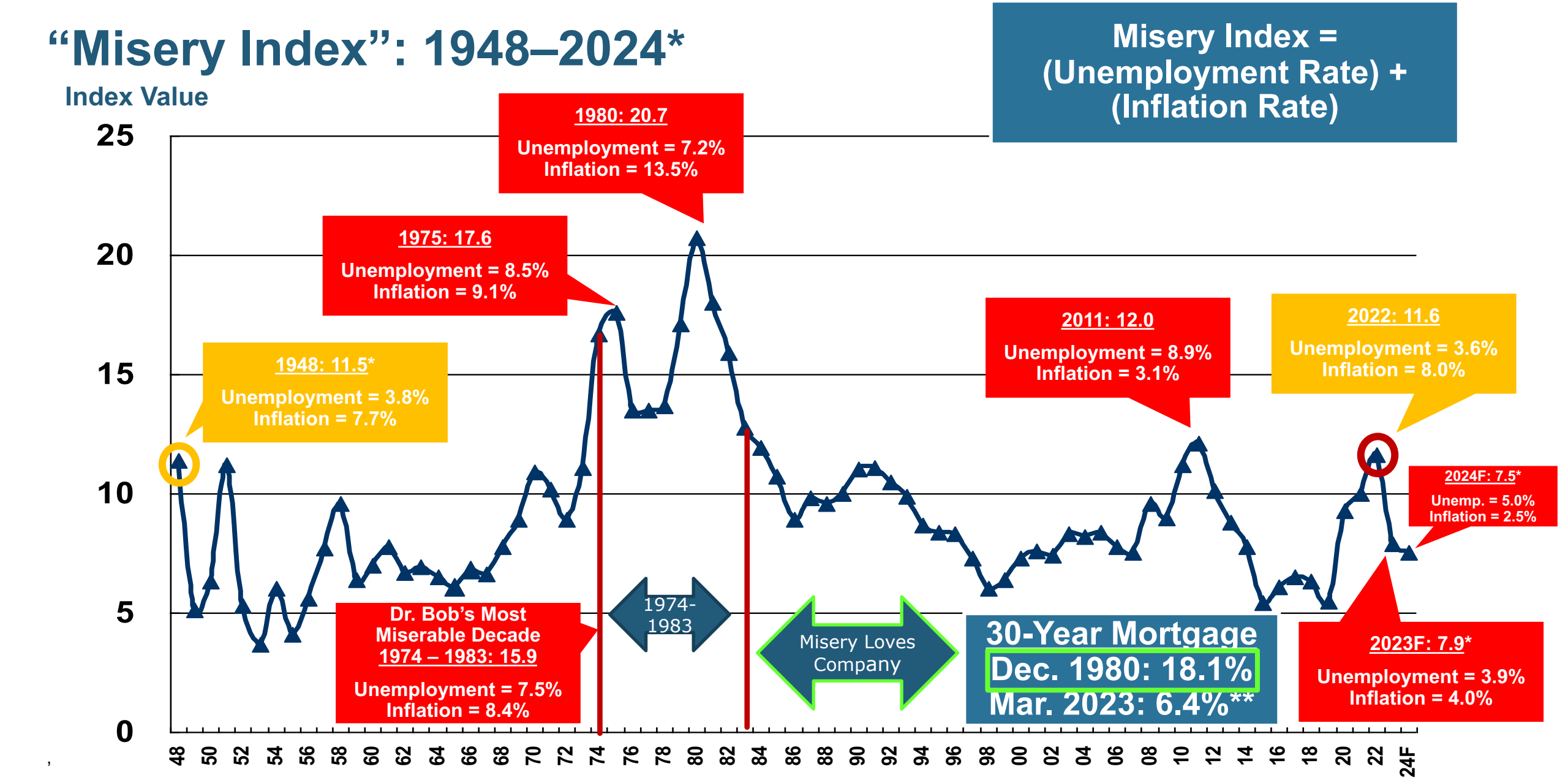
A Quick Review of Economic History Is Helpful

Inflation and Unemployment Rate, 1948–2024F*



*2023-24 forecast of unemployment and inflation rates based on Wells Fargo Securities forecasts (3/23).
Source: U.S. Bureau of Labor Statistics; Center for Risk and Uncertainty Management, University of South Carolina.

“Misery Index”: 1948–2024*



*Estimated based on Wells Fargo Securities forecasts (3/23).
**As of 3/28/23 based on Freddie Mac data.
Source: U.S. Bureau of Labor Statistics; Center for Risk and Uncertainty Management, University of South Carolina.

P/C Insurance Industry Financial Overview & Outlook:

Challenges Amid Rising Inflation and Higher Interest Rates

The Current Economic Environment Presents Many Challenges for P/C Insurers

Industry Remains Strong

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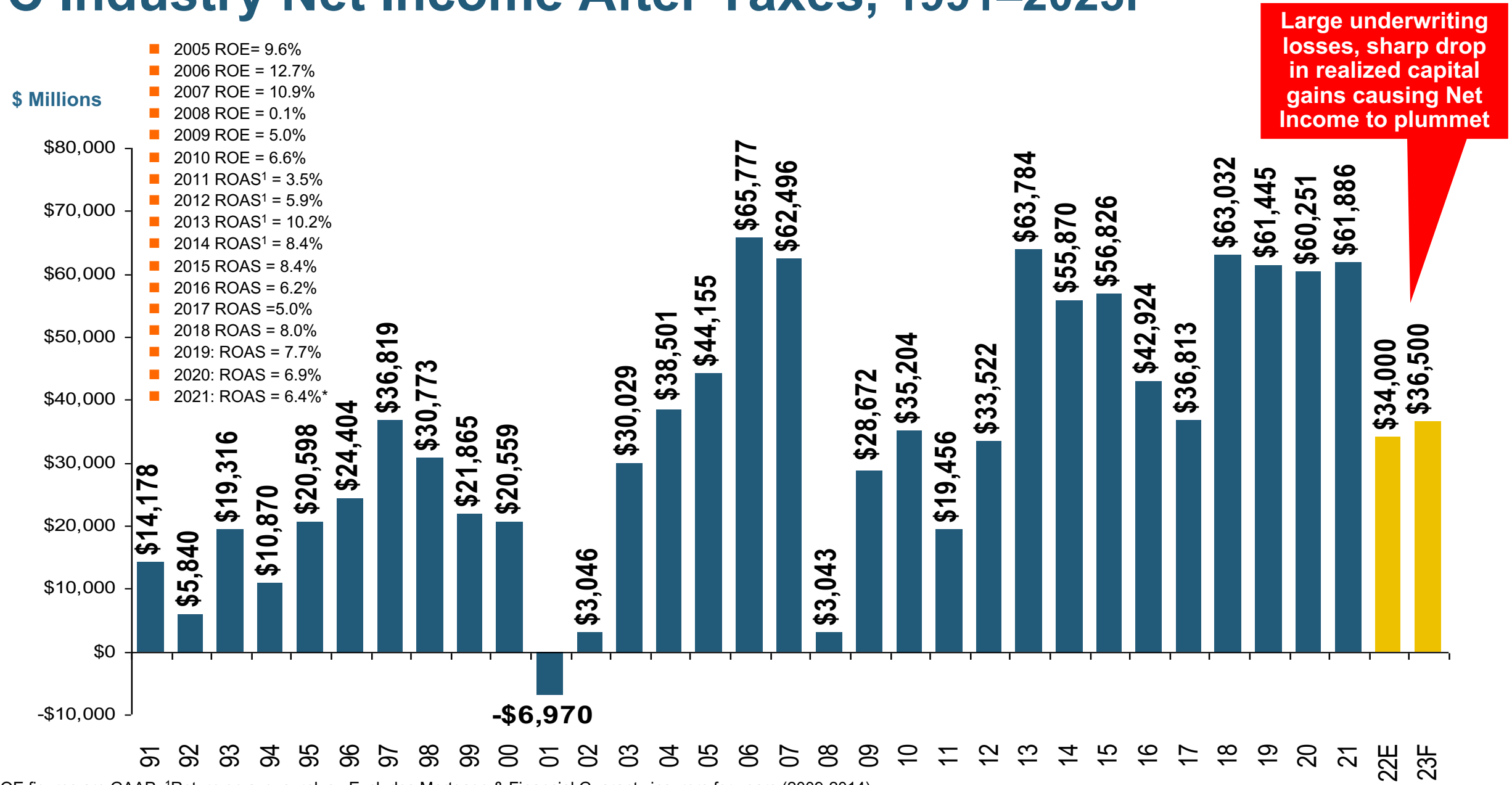
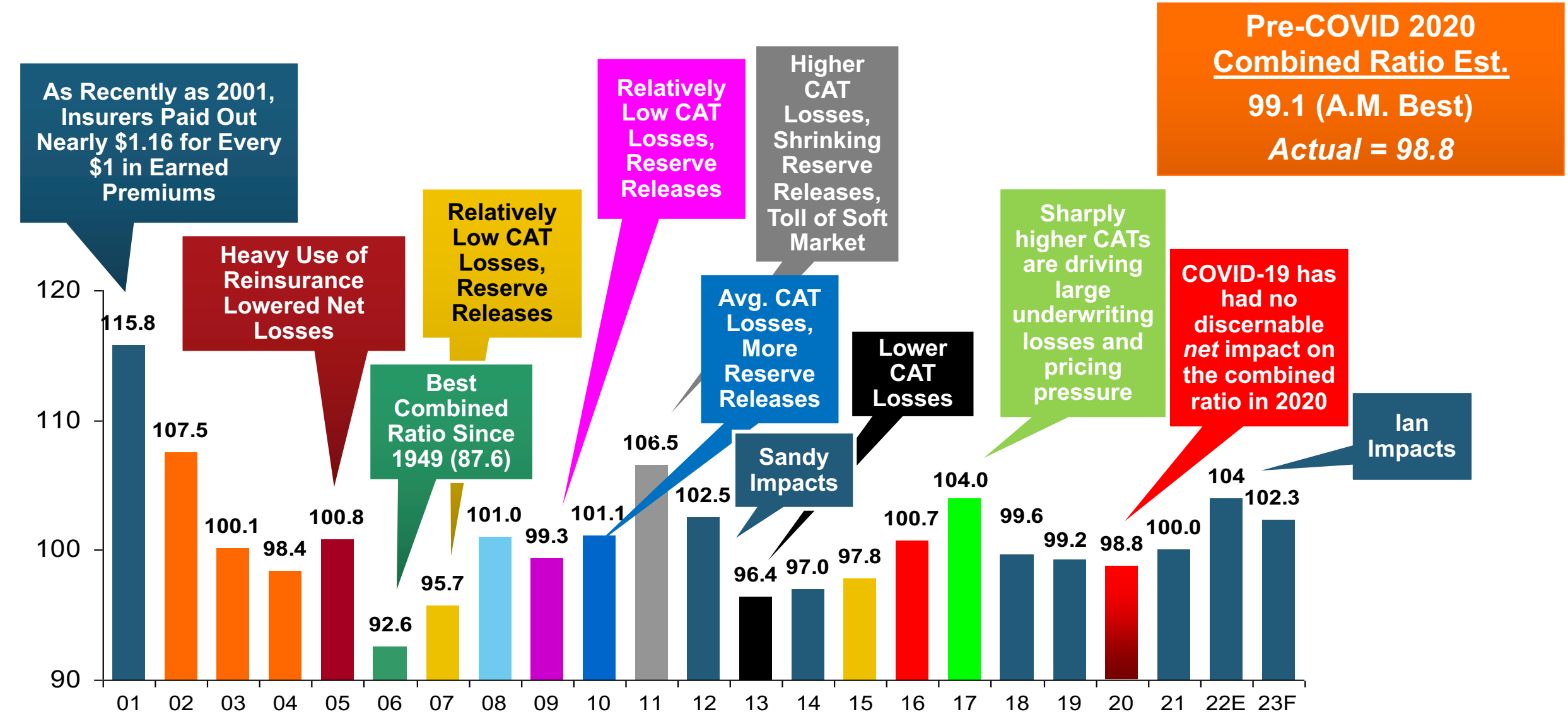
P/C Industry Net Income After Taxes, 1991–2023F



*ROE figures are GAAP; [1]Return on avg. surplus. Excludes Mortgage & Financial Guaranty insurers for years (2009-2014).

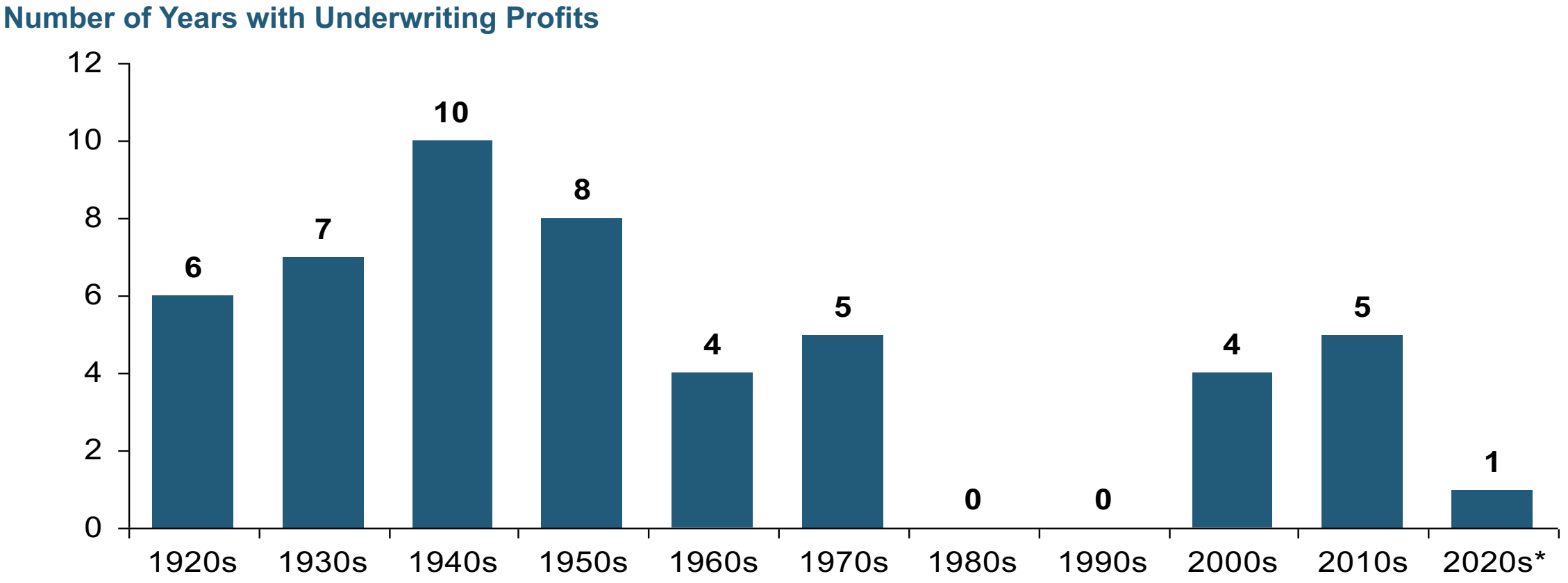
Sources: A.M. Best, ISO, APCIA.

P/C Insurance Industry Combined Ratio, 2001–2023F*



*Excludes Mortgage & Financial Guaranty insurers 2008–2014.
Sources: A.M. Best, ISO (2014-2024F).

Number of Years with Underwriting Profits by Decade, 1920s–2020s



Underwriting Profits Were Common Before the 1980s (40 of the 60 Years Before 1980 Had Combined Ratios Below 100) –But Then They Vanished. Not a Single Underwriting Profit Was Recorded in the 25 Years from 1979 Through 2003

* 2020 through 2022

Note: Data for 1920–1934 based on stock companies only.

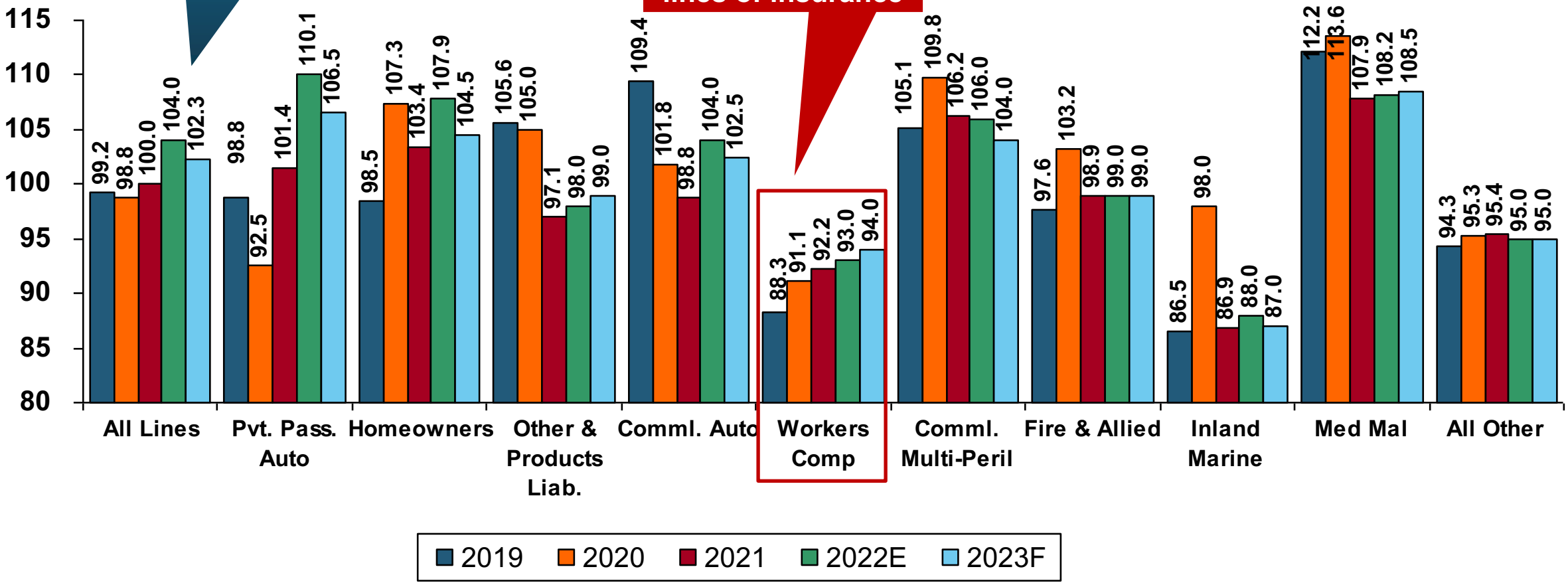
Sources: Insurance Information Institute research from A.M. Best Data.

Combined Ratios by Line: 2019 – 2023F

High CAT losses and inflation are pushing up combined ratios

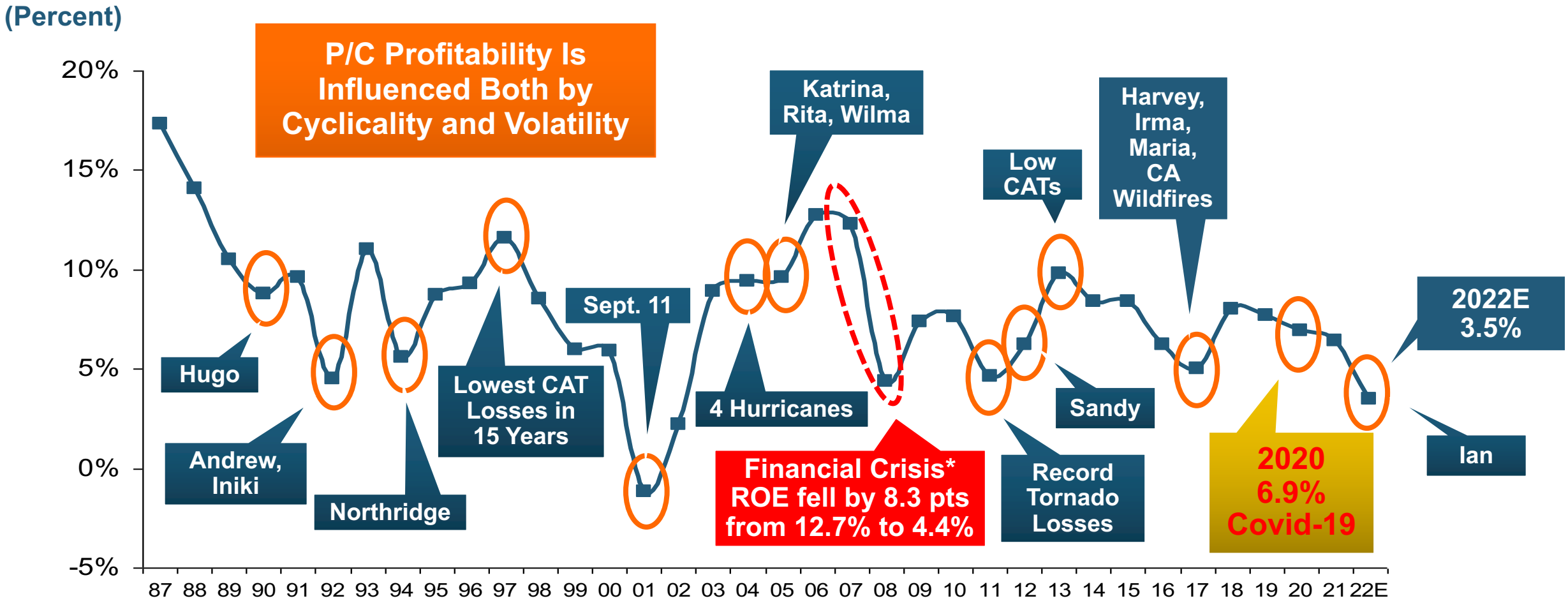
WC is among the best performing lines of insurance

Inflation will continue to pressure the combined ratio in 2023



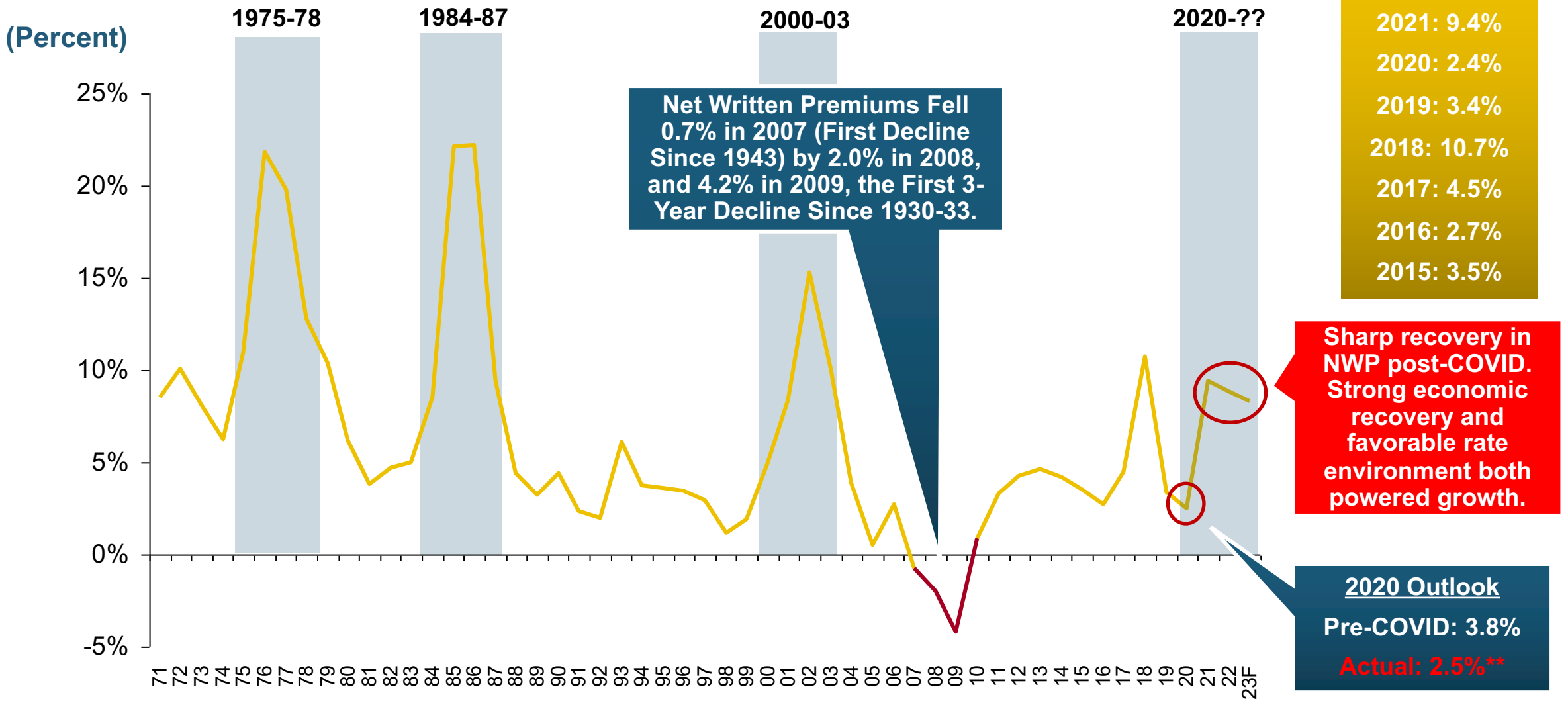
Source: A.M. Best *Review & Preview* (2023 forecasts as of Mar. 2023); Univ. of South Carolina, Risk and Uncertainty Management Center.

ROE: Property/Casualty Insurance by Major Event, 1987–2022E*



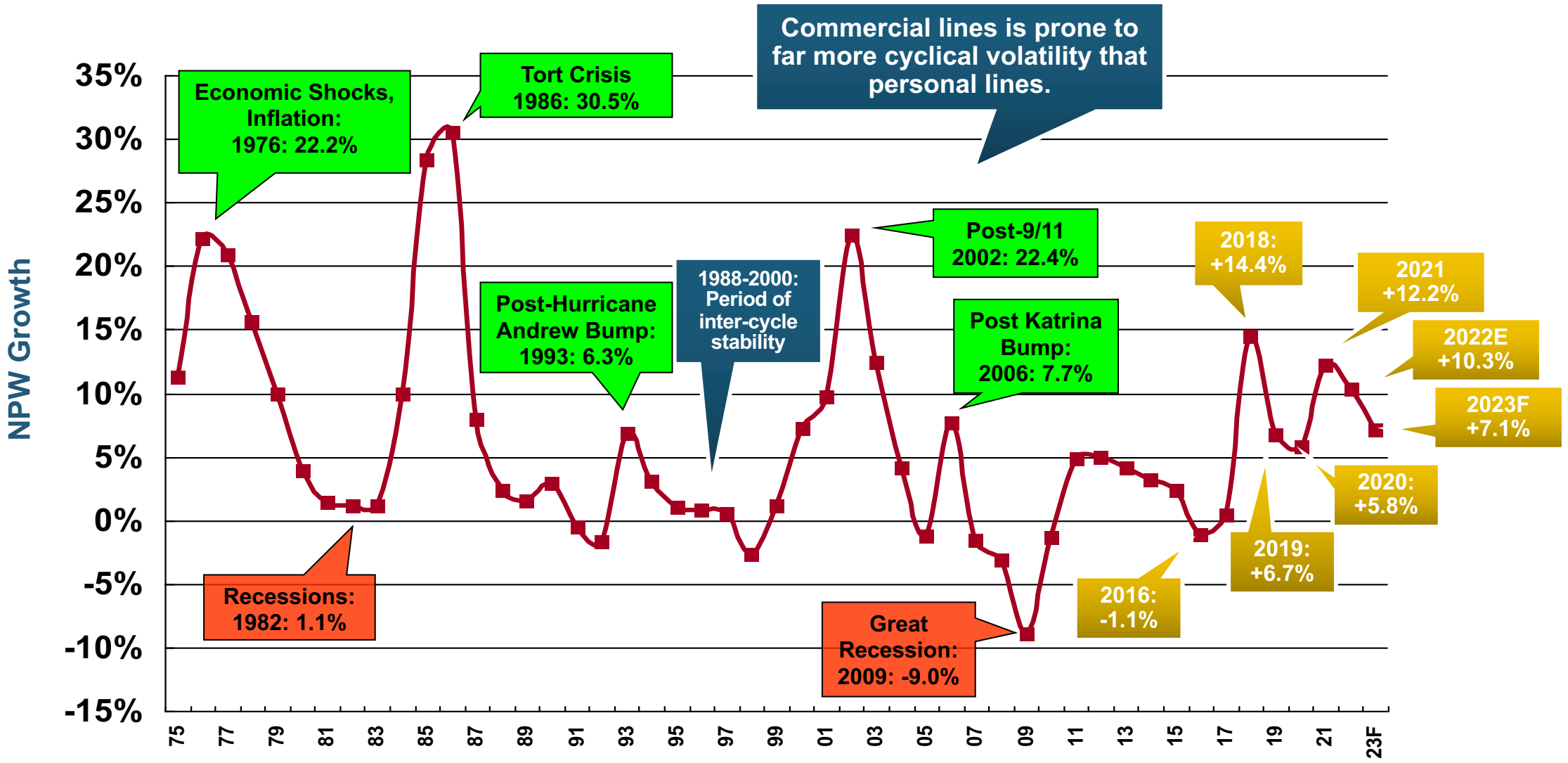
*Excludes Mortgage & Financial Guarantee in 2008 – 2014.
Sources: A.M. Best, ISO, *Fortune,* APCIA; USC RUM Center.

Net Written Premium Growth (All P/C Lines): Annual Change, 1971–2023F



NOTE: Shaded areas denote “hard market” periods.
Sources: A.M. Best (1971-2013, 2022E – 2023F), ISO (2014-21); Risk & Uncertainty Management Center, Univ. of South Carolina

Commercial Lines NPW Premium Growth: 1975 – 2023F



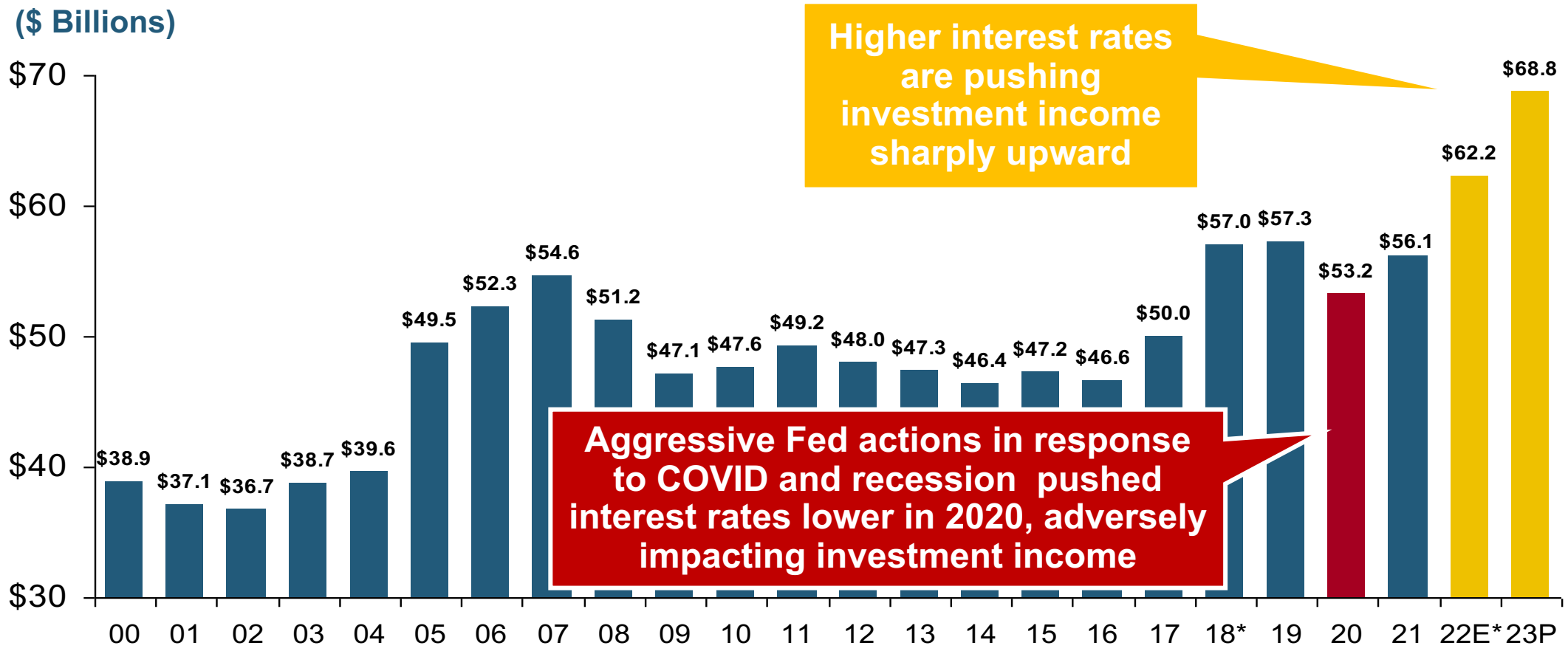
Note: Data include state funds beginning in 1998.
Source: A.M. Best; ISO; APCIA; Univ. of South Carolina Center for Risk and Uncertainty Management Center.

Investments

Investment Performance Is a Key Driver of Insurer Profitability

Dove to Hawk: How Will an Aggressive Fed Impact Insurer Portfolios?

Property/Casualty Insurance Industry Investment Income: 2000–2023P

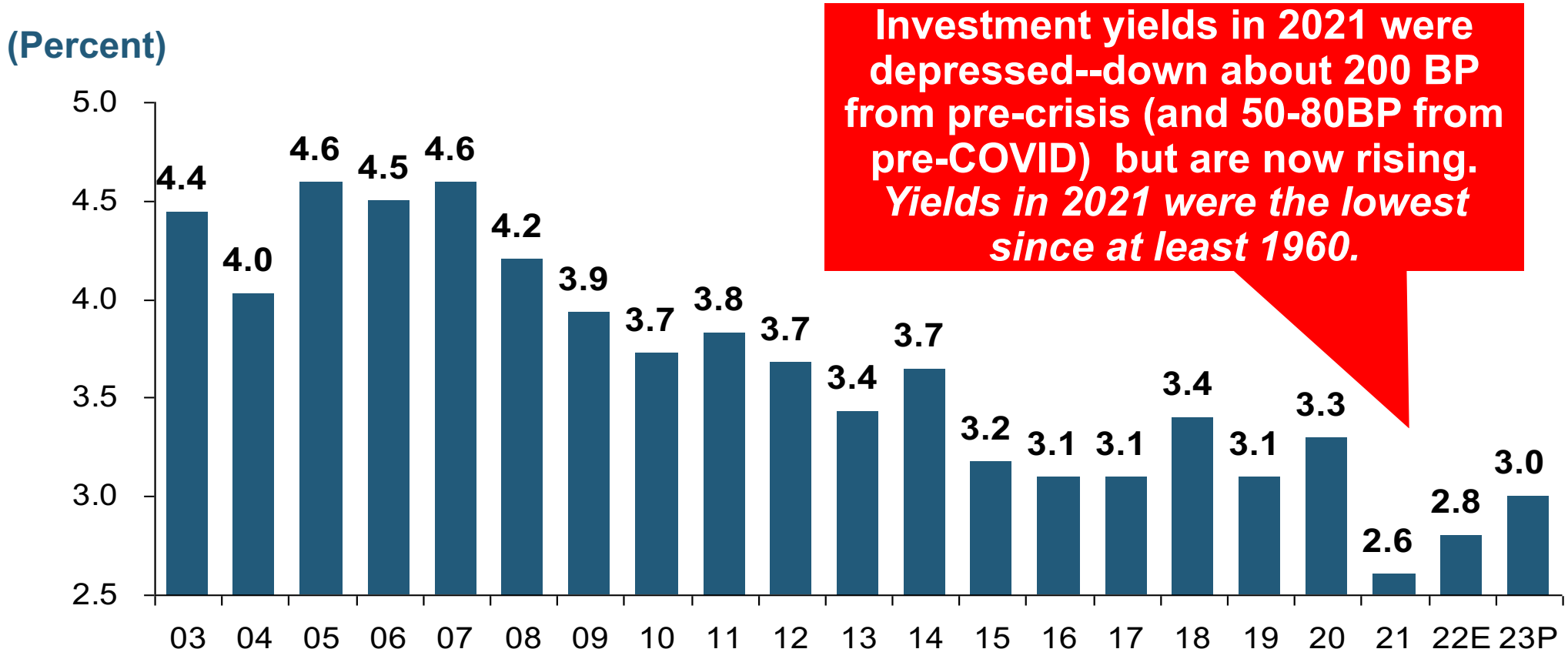


Due to persistently low interest rates, investment income remained below pre-crisis levels for a decade. Lower interest rates during COVID drove investment income down once again. Fed rate hikes in 2022-23 are reversing this trend.

*2022 figure excludes $10.8B intercompany distribution at a large reinsurer. 2018-19 figures are distorted by provisions of the TCJA of 2017. Increase reflects such items as dividends from foreign subsidiaries.

[1] Investment gains consist primarily of interest and stock dividends. Sources: A.M. Best Review & Preview (March 2023); ISO; University of South Carolina, Center for Risk and Uncertainty Management.

Net Investment Yield on Property/Casualty Insurance Invested Assets, 2007–2023P



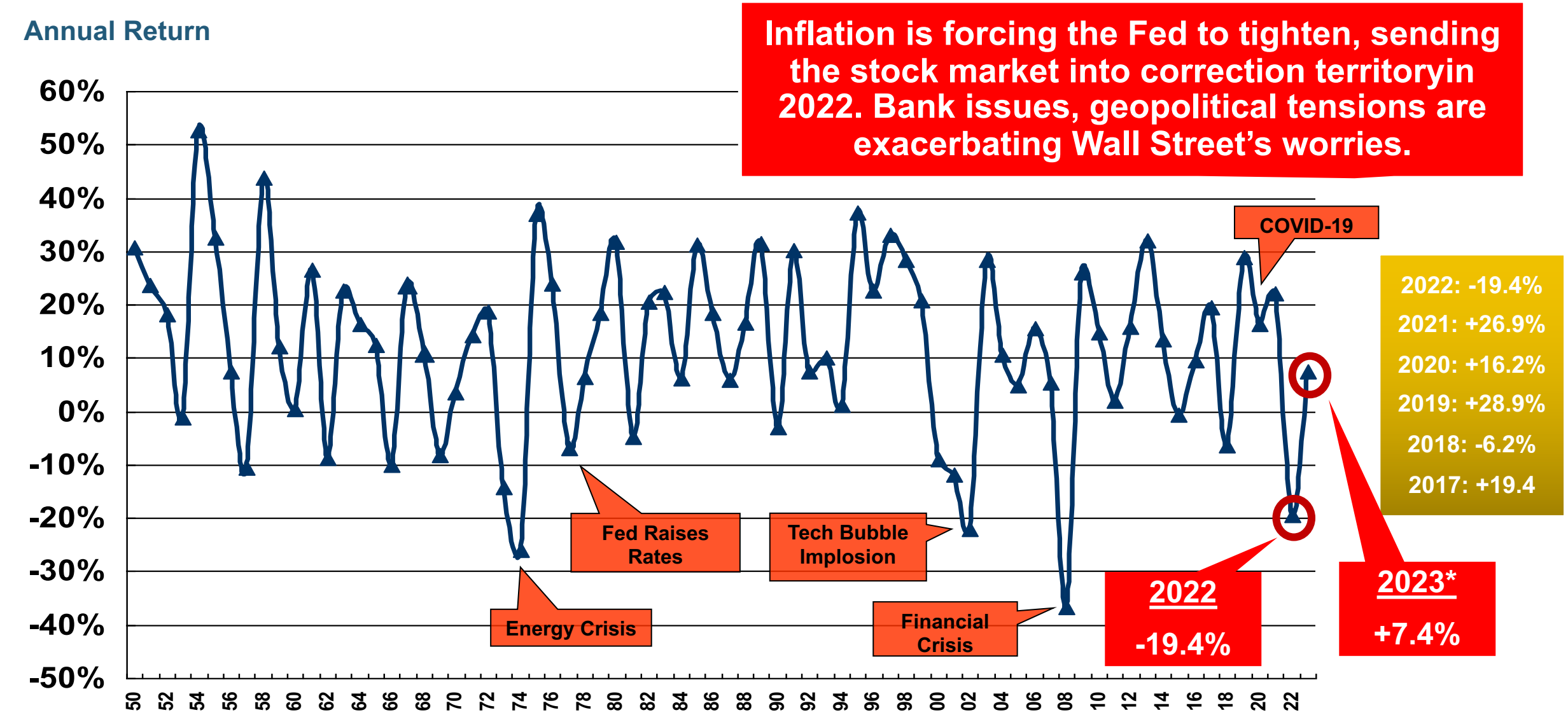
Investment yields in 2021 were depressed--down about 200 BP from pre-crisis (and 50-80BP from pre-COVID) but are now rising. *Yields in 2021 were the lowest since at least 1960.*

The yield on invested assets remains depressed relative to pre-financial crisis and pre-COVID yields. Fed rate hikes in 2022-23 are lifting yields and investment income.

Average: 1960-2019 = 4.9%
Low: 2.8% (1961)
High: 8.2% (1984/85)

Sources: NAIC data, sourced from S&P Global Market Intelligence; 2017-19 figures are from ISO. 2020-21 data from the APCIA. 2022^{E}-23P from A.M. Best Review & Preview (March 2023). Risk and Uncertainty Management Center, Univ. of South Carolina.

S&P 500 Index Returns, 1950–2023*



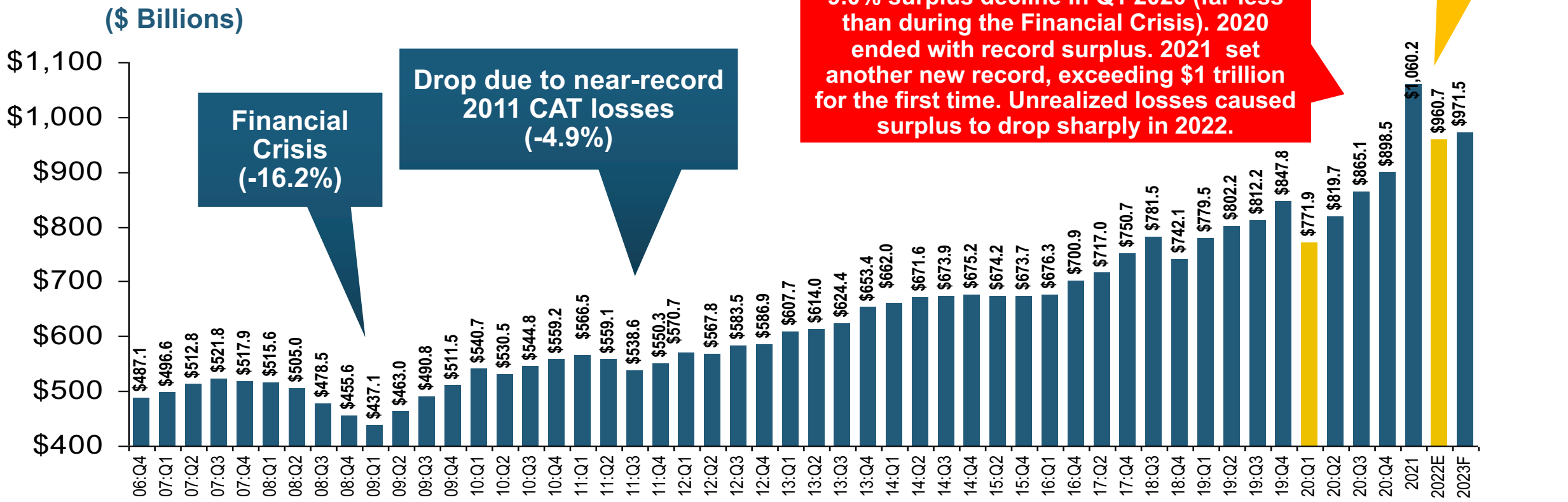
*Through Apr. 3, 2023.
Source: NYU Stern School of Business: http://pages.stern.nyu.edu/~adamodar/New_Home_Page/datafile/histretSP.html;
Center for Risk and Uncertainty Management, University of South Carolina.

Capital and Capacity

P/C Insurance: Over or Under Capitalized?

Is the Industry Creating Economic Value?

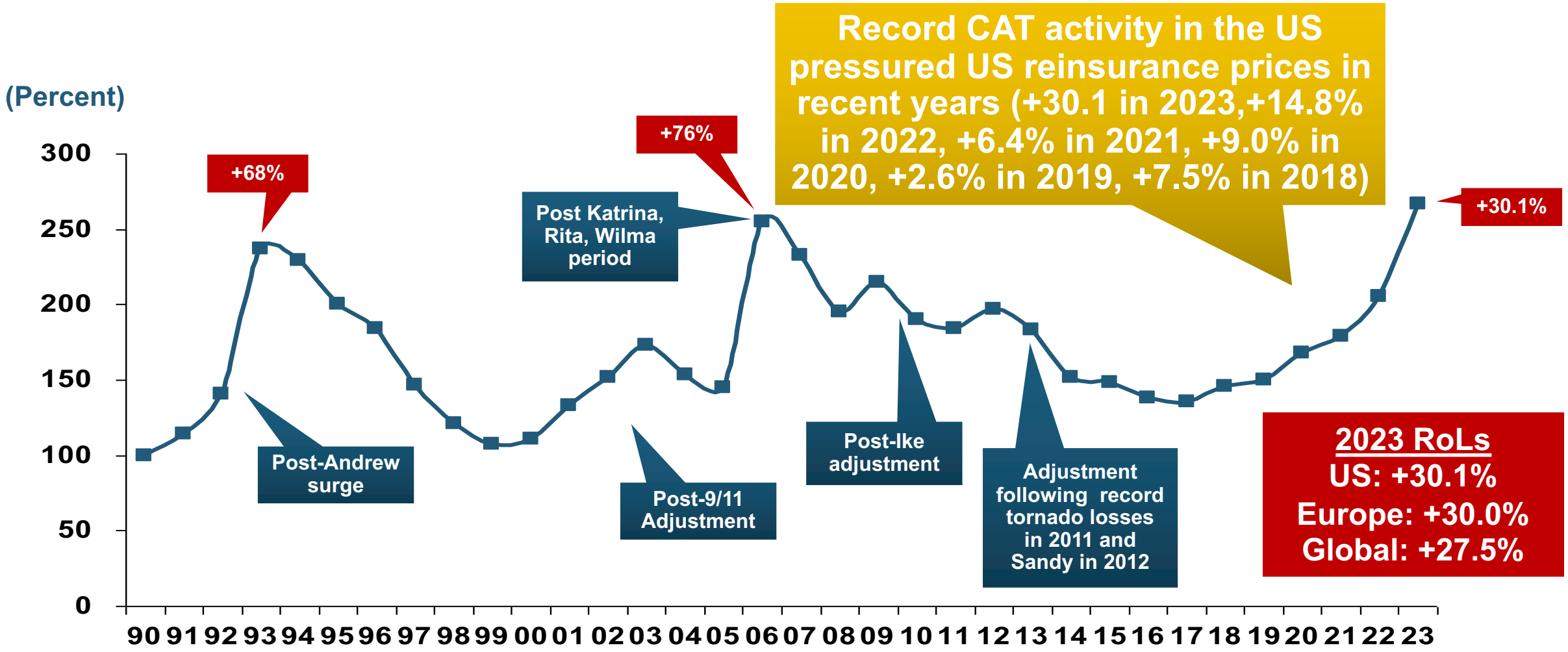
Policyholder Surplus (Capacity), 2006:Q4 – 2023F



Policyholder Surplus is the industry's financial cushion against large insured events, periods of economic stress and financial market volatility. It is also a source of capital to underwrite new risks.

Sources: ISO, A.M .Best, NAIC. Risk and Uncertainty Management Center, University of South Carolina.

US Property Catastrophe Rate-on-Line Index: 1990 – 2023*



US Property-CAT Reinsurance Pricing Is Sensitive to CAT Activity and Ultimately Impacts Primary Insurance Pricing, Terms and Conditions.

*As of January 1 each year.

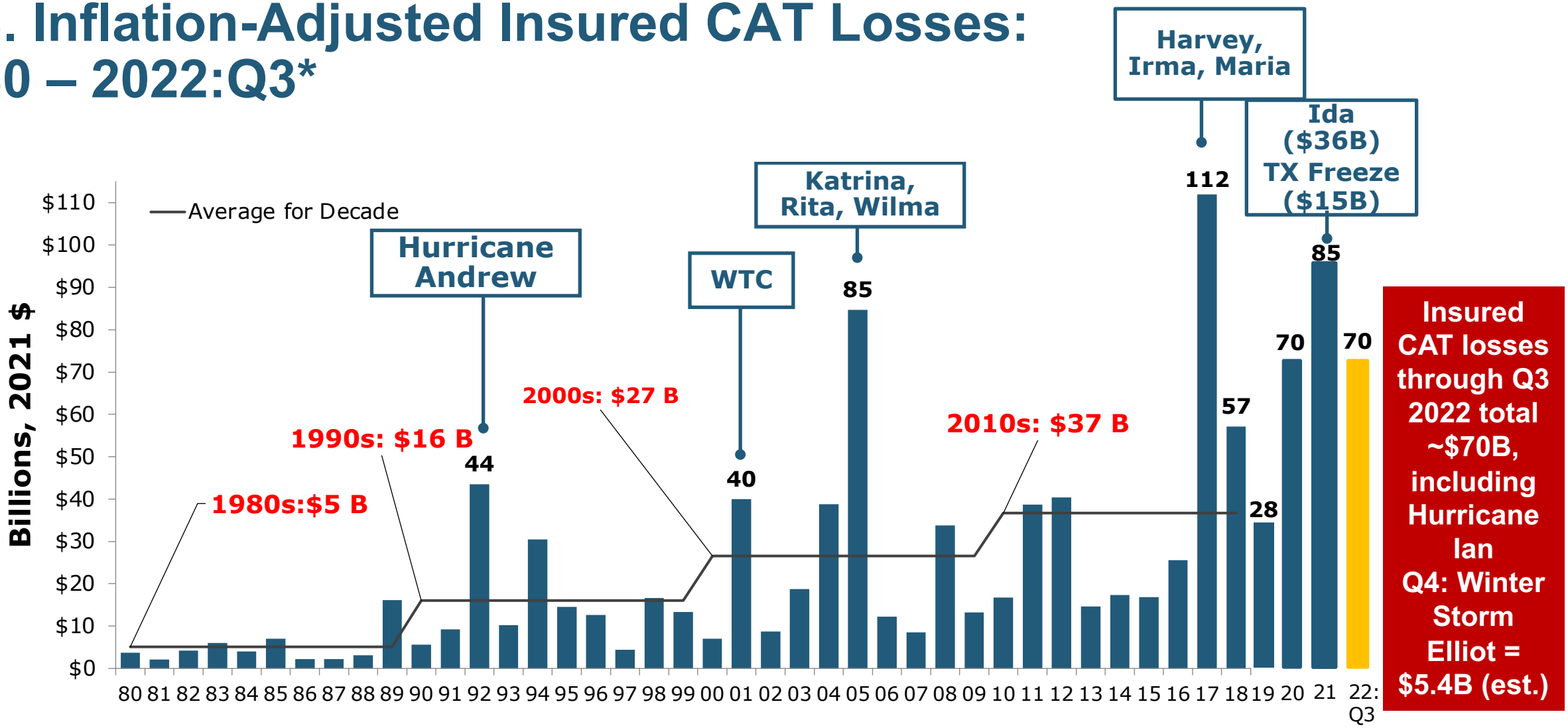
Source: Guy Carpenter; Artemis.bm accessed at: http://www.artemis.bm/us-property-cat-rate-on-line-index

Catastrophe Loss Trends

The Rise in CAT Losses Shows No Signs of Easing

The 2020s Are Off to an Ominous Beginning

U.S. Inflation-Adjusted Insured CAT Losses: 1980 – 2022:Q3*



Insured CAT losses through Q3 2022 total ~$70B, including Hurricane Ian
Q4: Winter Storm Elliot = $5.4B (est.)

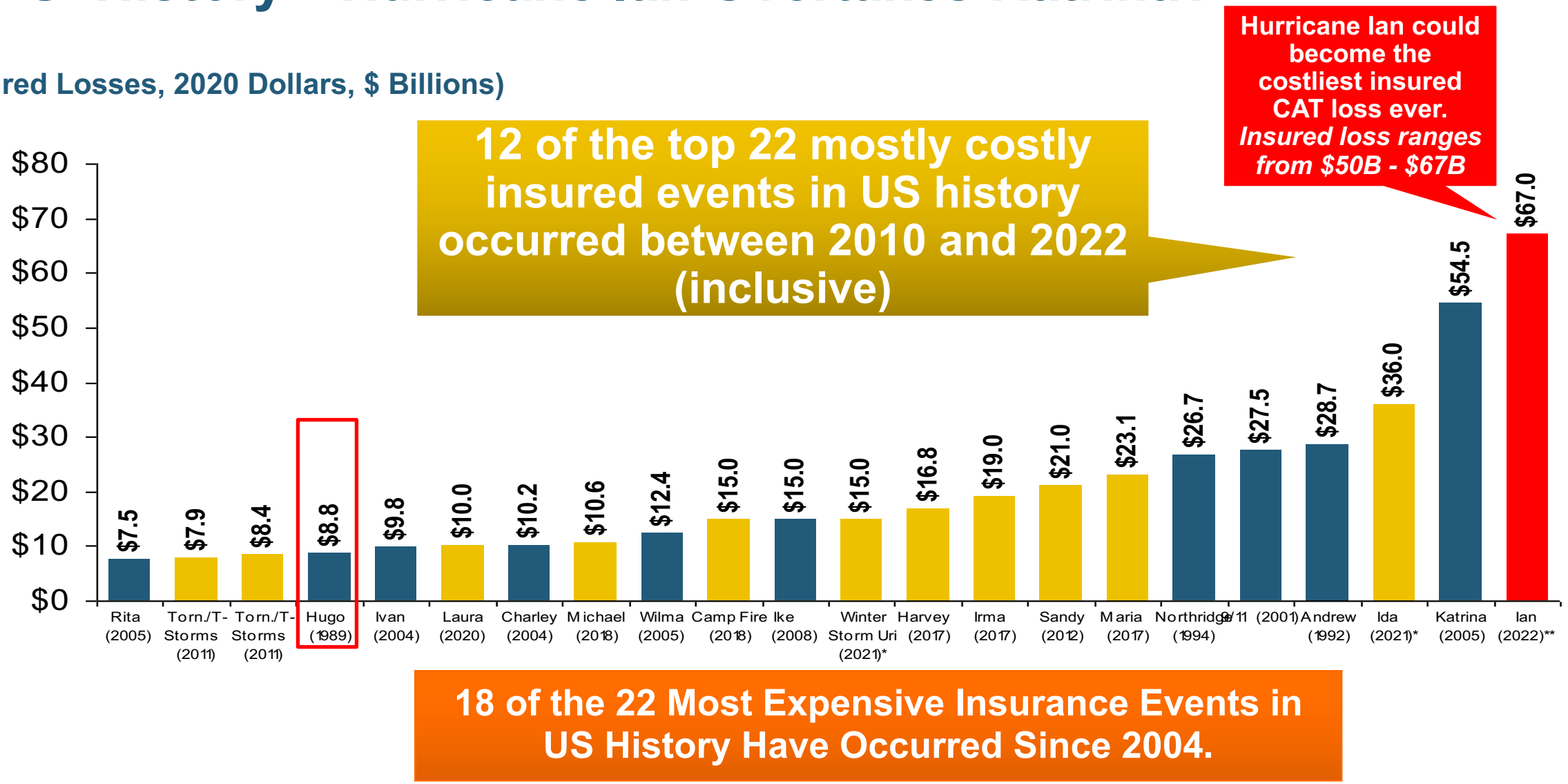
Average Insured Loss per Year*
1980-2021: $23.8 Billion
2012-2021: $44.1 Billion

The 2020s are off to an ominous start with $76B in average annual insured losses (2020-21)

*Stated in 2021 dollars except 2022:Q3 (2022 dollars).
Sources: Property Claims Service, a Verisk Analytics business (1980-2019); 2020-21 figures from Munich Re; 2023 YTD data from Aon; Insurance Information Institute; University of South Carolina, Risk & Uncertainty Management Center.

Top 22 Most Costly Disasters in U.S. History—Hurricane Ian Overtakes Katrina?

(Insured Losses, 2020 Dollars, $ Billions)



*2021 dollars; **2022 dollars (RMS private insurer estimate as of 10/10/22).

Sources: PCS, RMS, Aon, Karen Clark & Co; USC Center for Risk and Uncertainty Management adjustments to 2020 dollars using the CPI.

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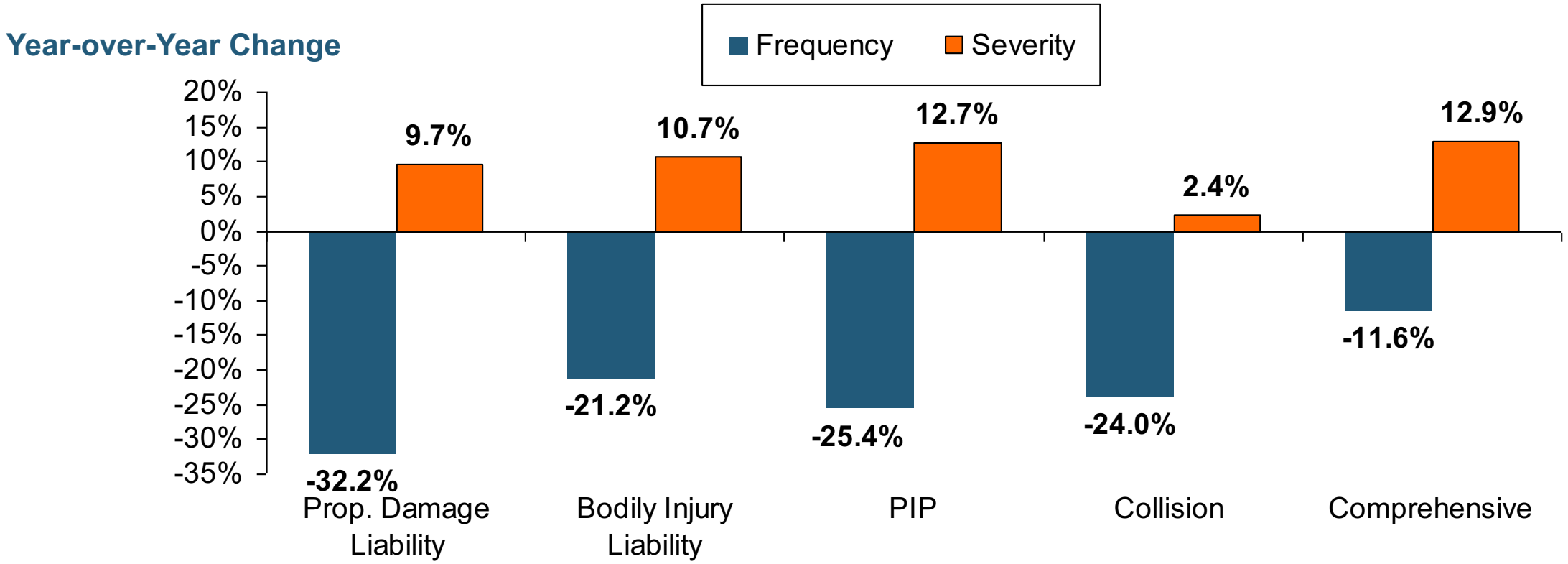
Private Passenger Auto Frequency & Severity Trends

Frequency, Severity and Loss Ratio Trends Are Adverse

Inflation is a Major Driver

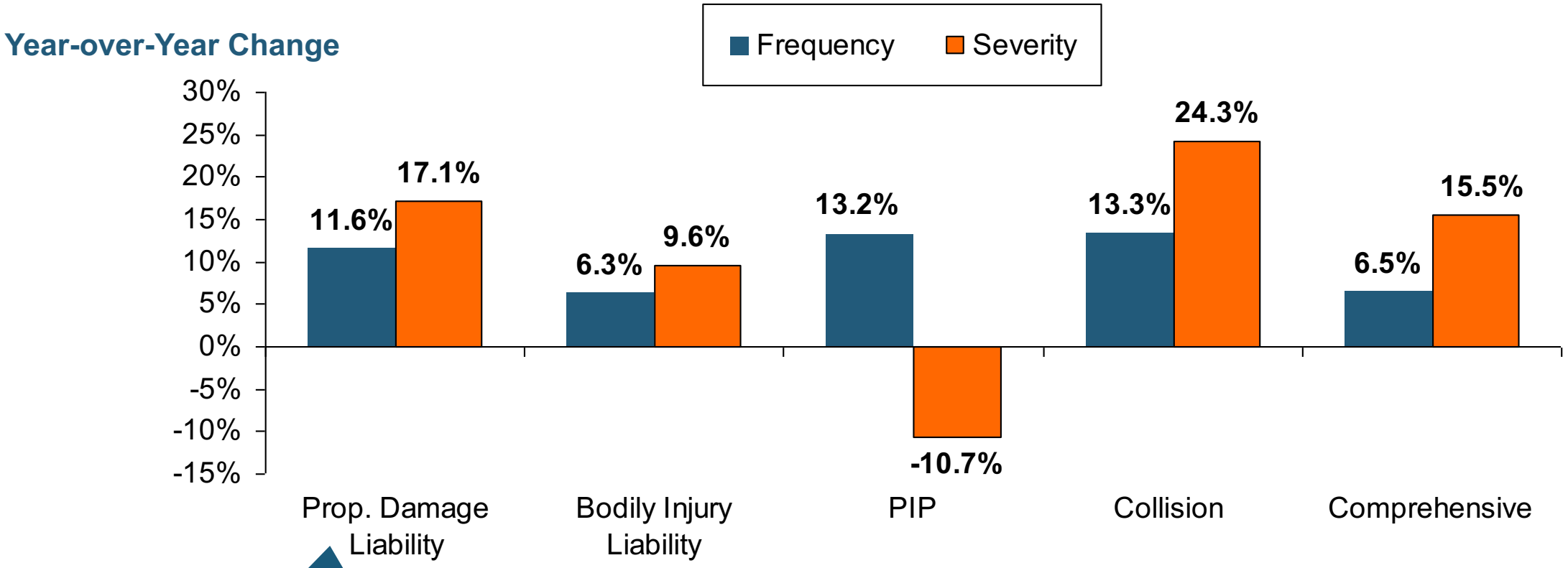
At the Peak of the Pandemic, Frequencies Across All Coverages Plummeted and But Severities Rose: 4 Qtrs. Ending Q1 2021



The COVID-19 Pandemic Introduced Unparalleled Volatility in the Personal Auto Line

Source: ISO/PCI *Fast Track* data for 4 quarters ending in Q1 2021; Risk and Uncertainty Management Center, Univ. of South Carolina.

Personal Auto Claim Frequency Declines Have Ended and Are in Full Reversal, Severity Rise Continues: 4 Qtrs. Ending Q3 2022



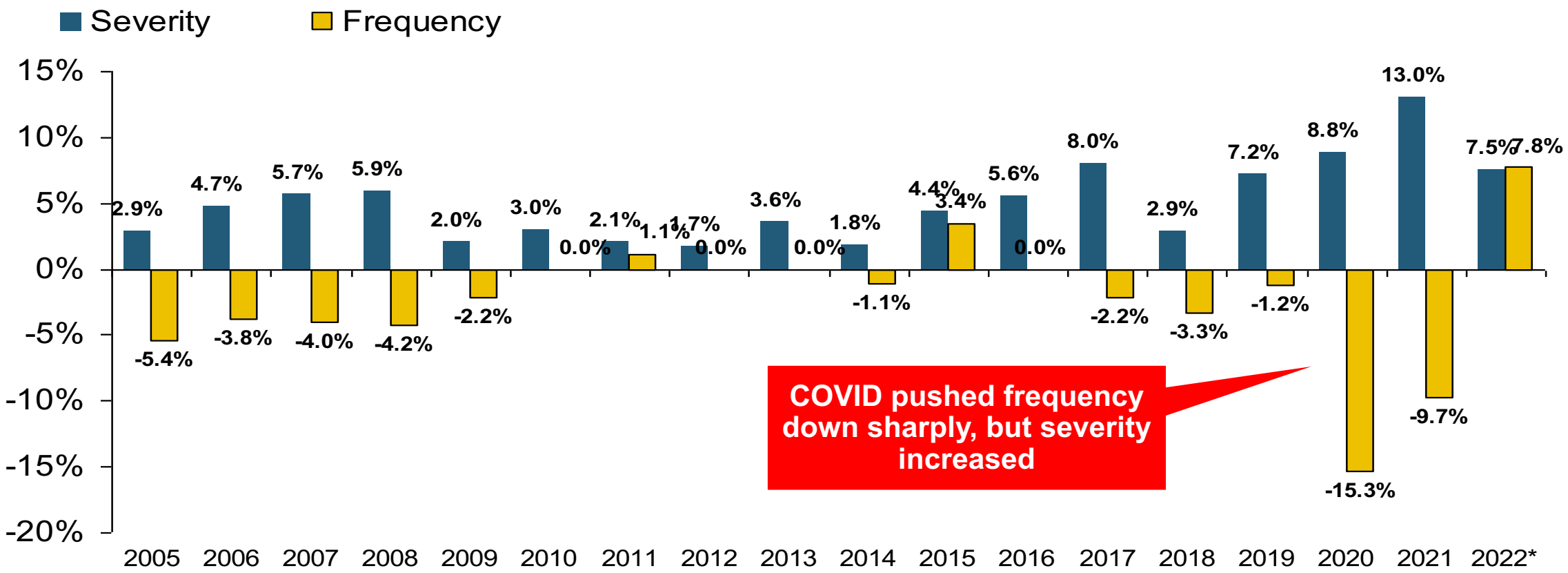
Recall: PD Liability claims were down 32.2% for the 4 qtrs. ending Q1 2021

Auto Claim Frequencies Fell Sharply During the Pandemic, though Claim Severities Rose Materially

Source: ISO/PCI *Fast Track* data for Q3 2022; Risk and Uncertainty Management Center, Univ. of South Carolina.

Bodily Injury: Severity Trend Is Up, Frequency Plunge Due to COVID Has Ended and Is Reversing

Annual Change, 2005 through 2022*



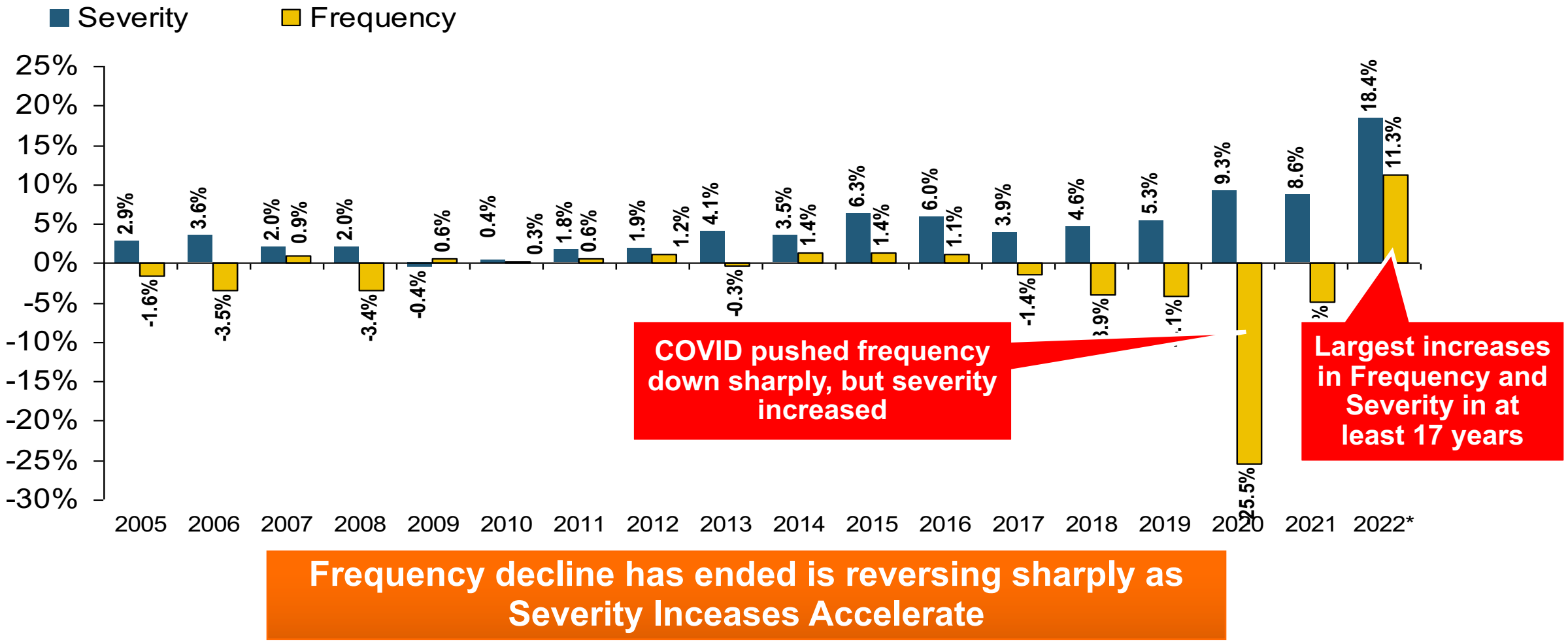
Frequency decline has ended and Severity Increases Continue

*2022 figure is for the 4 quarters ending 2022:Q3.

Source: ISO/PCI *Fast Track* data; Center for Risk and Uncertainty Management, Univ. of South Carolina.

Property Damage Liability: Severity Trend Is Up, Frequency Plunge in 2020 Due to COVID Has Ended and Is Reversing

Annual Change, 2005 through 2022*



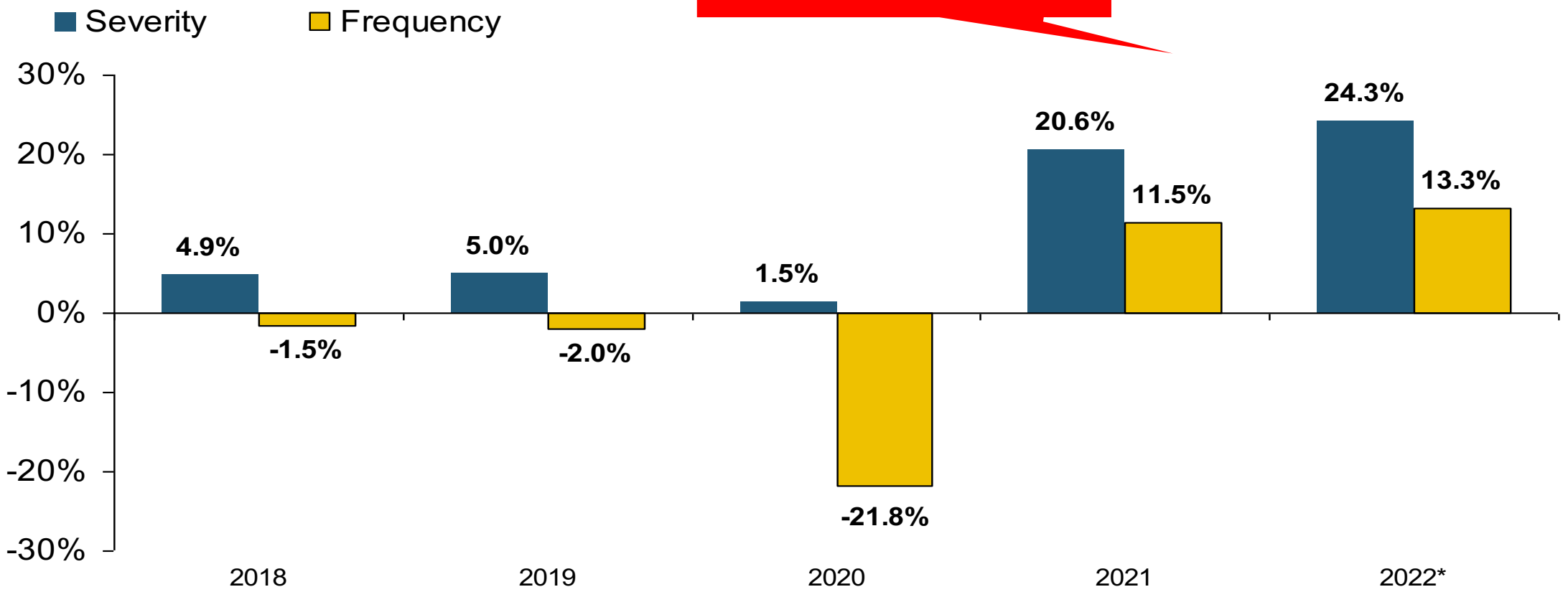
Frequency decline has ended is reversing sharply as Severity Inceases Accelerate

*2022 figure is for the 4 quarters ending 2022:Q3.

Source: ISO/PCI *Fast Track* data; Center for Risk and Uncertainty Management, Univ. of South Carolina.

Collision Coverage: Post-Pandemic Surge in Both Frequency and Severity

Annual Change, 2018 through 2022*

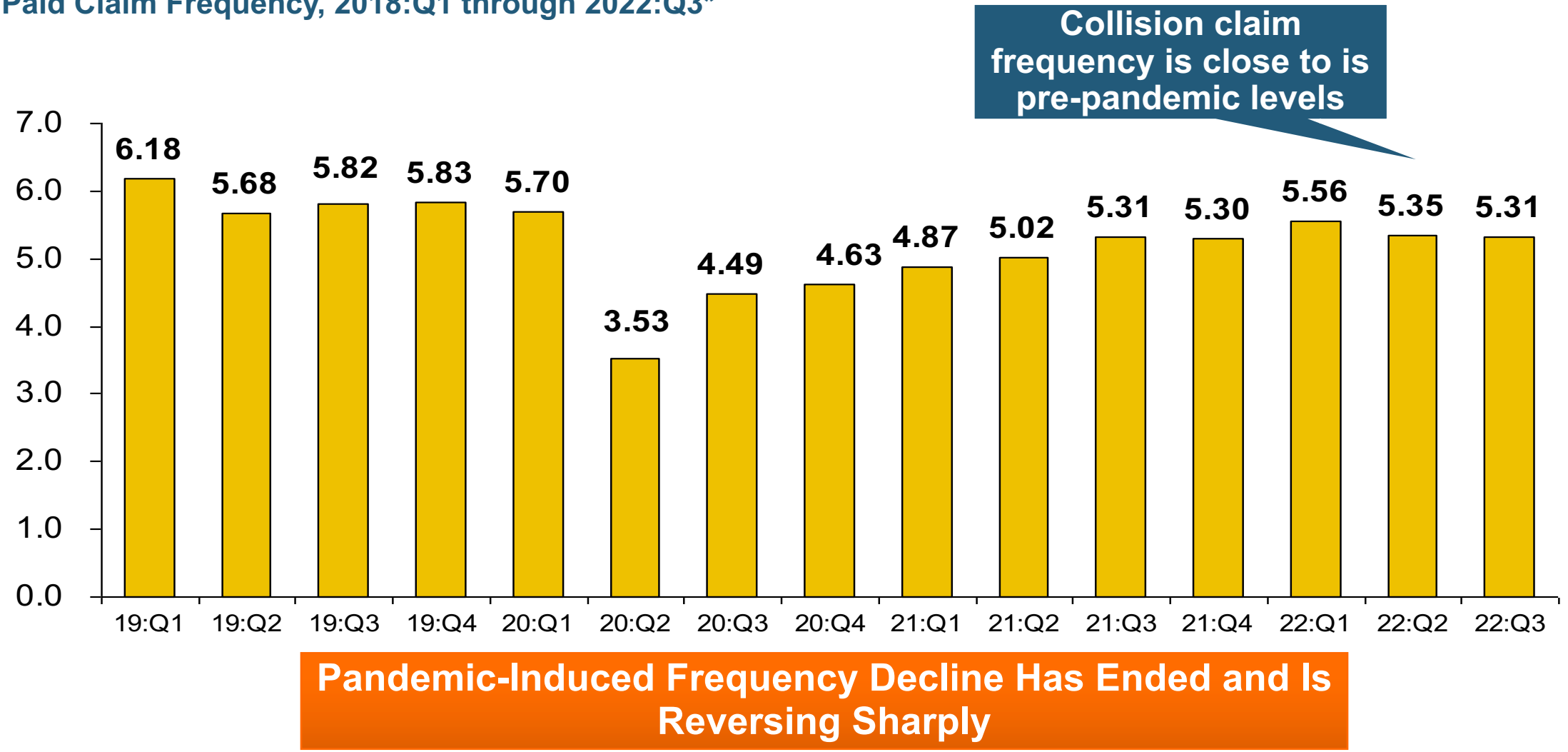


Pandemic-Induced Frequency Decline Has Ended and Is Reversing Sharply

*2022 figure is for the 4 quarters ending 2022:Q2.
Source: ISO/PCI *Fast Track* data; Center for Risk and Uncertainty Management, Univ. of South Carolina.

Collision Claim Frequency Trend: Returning to Pre-Pandemic Levels?

Paid Claim Frequency, 2018:Q1 through 2022:Q3*



Pandemic-Induced Frequency Decline Has Ended and Is Reversing Sharply

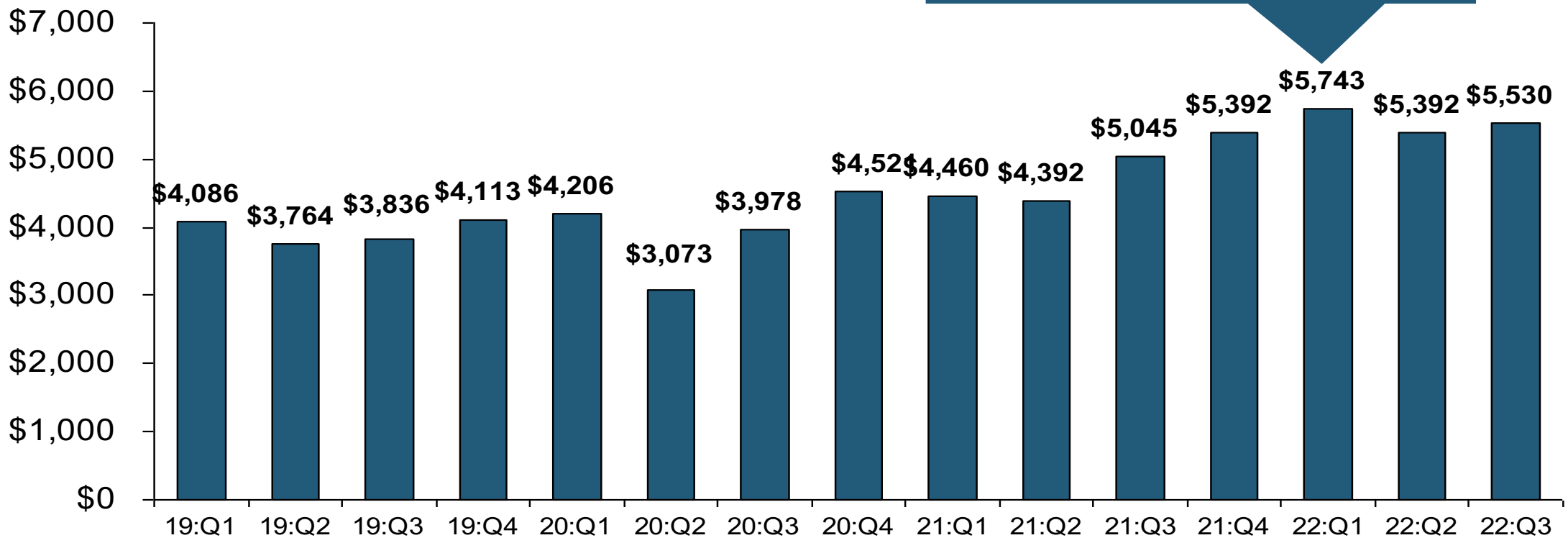
*Number of claims per 100 earned car years.

Source: ISO/PCI *Fast Track* data; Center for Risk and Uncertainty Management, Univ. of South Carolina.

Collision Claim Severity: Rising to New Record Highs

Average Loss, 2018:Q1 through 2022:Q3

Collision claim severity reached a record high in 2022:Q1, up 36.5% from 2020:Q1



Severities Are Up Sharply—Inflation Is a Major Factor

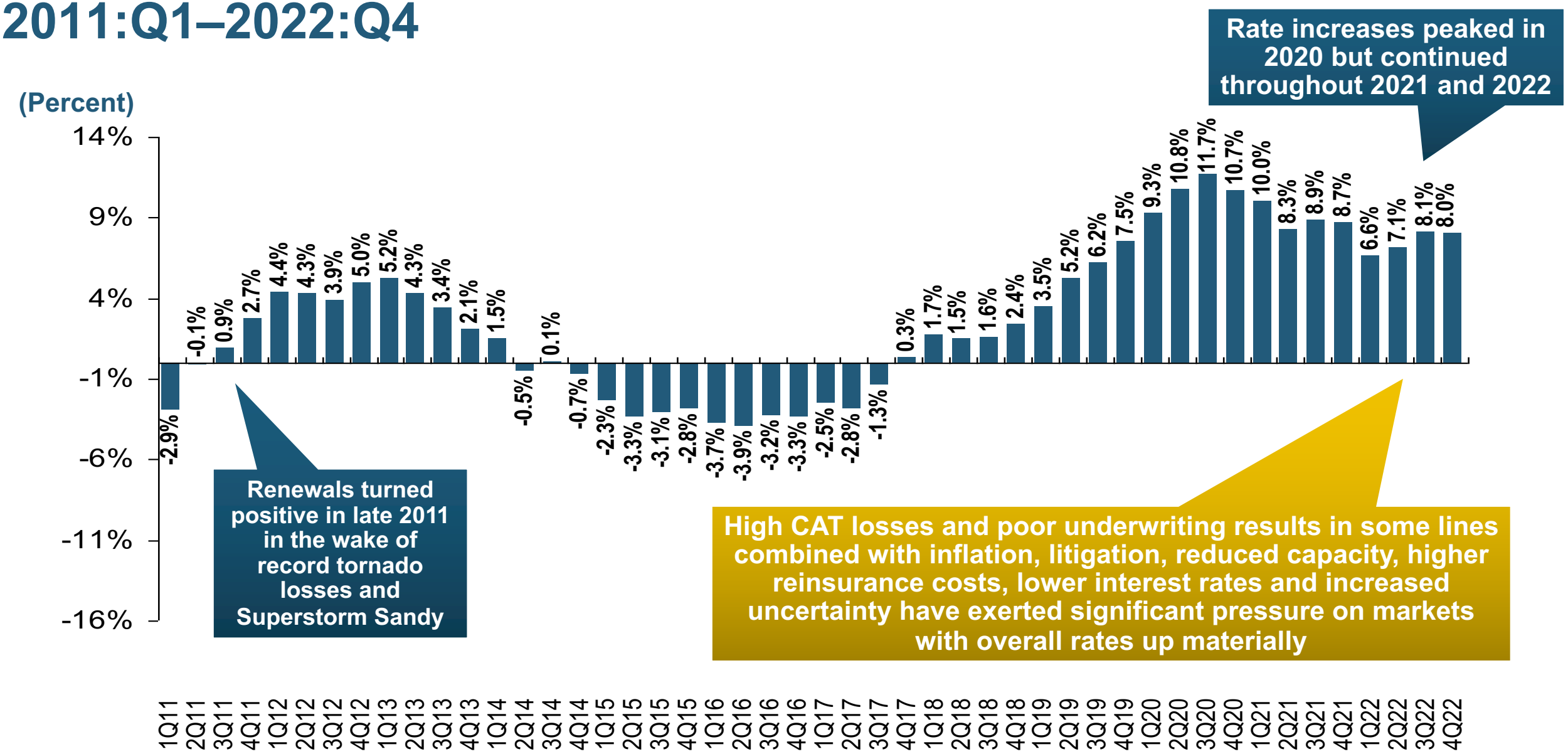
Source: ISO/PCI *Fast Track* data; Center for Risk and Uncertainty Management, Univ. of South Carolina.

Commercial Lines & Pricing Cyclicality

Economic and Tort Environment Create Pricing Pressure

80

CIAB: Average Commercial Rate Change, All Lines, 2011:Q1–2022:Q4

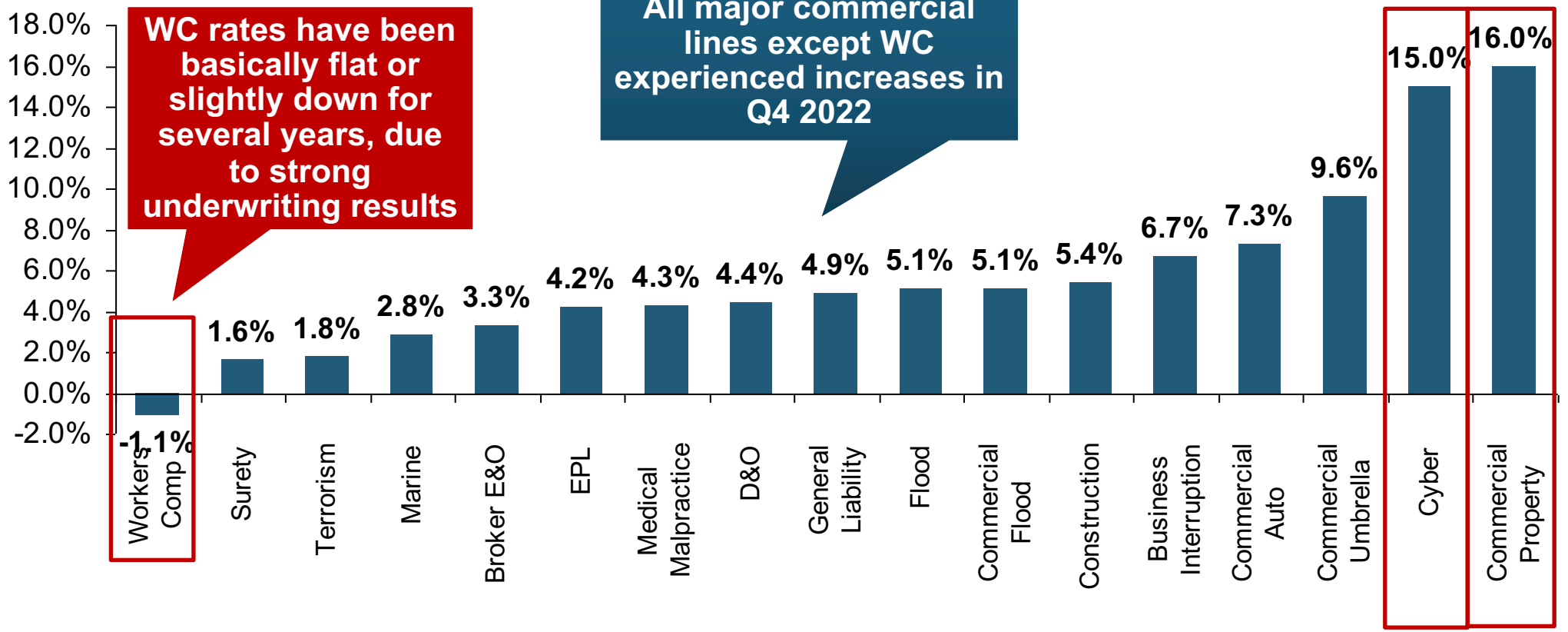


Note: CIAB data cited here are based on a survey. Rate changes earned by individual insurers can and do vary, potentially substantially.
Source: Council of Insurance Agents & Brokers; Center for Risk and Uncertainty Management, Univ. of South Carolina.

Change in Commercial Rate Renewals, by Line: 2022:Q4

Commercial property is up sharply as CAT losses and inflation continue to take their toll, overtaking Cyber, which is up in response to major breaches in recent years.

(Percent Change)



Note: CIAB data cited here are based on a survey. Rate changes earned by individual insurers can and do vary, potentially substantially.

Source: Council of Insurance Agents and Brokers; USC Center for Risk and Uncertainty Management.

SUMMARY

- The P/C Insurance Industry Remains Strong, Stable, Sound and Secure
- A Shallow Recession is Increasingly Likely Beginning in Q3 or Q4 2023
- Asset Price Volatility Will Persist as Inflation Uncertainty
- Banking Sector Problems Will Have Few Direct Impacts on P/C Insurers
- Higher Interest Rates Provide a Modest Tailwind for Investment Income
- Inflationary Pressures Will Persist in 2023, But Will Subside (Peak Reached in June 2022)
- Loss Cost Challenges Remain but Should Ease in 2023—Inflation, Supply Chain
- Legal System Abuse Issues Remain a Long-Term Challenge
- Immediate P/C Concerns: Capacity, CATs, Inflation→Rate/Reserve Adequacy, ITV

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