Today’s Uncertain Economy: Implications for P/C Insurance

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The Strength of the Economy Will Influence the Insurance Environment

Premium Rates, Claims, and Investment Income Will Be Affected
The Economy Drives P/C Insurance Industry Premiums:

Except for the three “hard markets” in this 47-year period, Net Written Premiums track Nominal GDP—not year by year but fairly well.

But How Strong Is the Economy, Really?
Since the Great Recession ended, the economy (as measured by real GDP) grew faster than 3% (at an annual rate) in a calendar quarter only 10 times in 35 quarters. Only twice in the last 14.

**Percent change from previous quarter, seasonally-adjusted at an annual rate**

Sources: U.S. Department of Commerce; Insurance Information Institute.
The manufacturing sector expanded in 67 of the 70 months from January 2010 through October 2015. It contracted in November 2015 through February 2016 and again in August 2016 but is expanding again.

Sources: Institute for Supply Management; Insurance Information Institute.
The non-manufacturing sector expanded in every month after January 2010. The pace of expansion roared ahead in 2014-15, slowed a bit in 2016, but is now as strong as it has been since the end of the Great Recession.

Tough times ahead? Forecasts expect U.S. growth to slow markedly by 2020, then rebound mildly into 2022.
State-by-State Leading Indicators through September 2018

Sources: Federal Reserve Bank of Philadelphia at www.philadelphiafed.org/index.cfm, released May 3, 2018; Next release is June 5, 2018; Insurance Information Institute.
### Strongest Growth

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### Weakest States in Top Growth Category

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<td>MN</td>
<td>1.64</td>
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Sources: Federal Reserve Bank of Philadelphia at [www.philadelphiafed.org/index.cfm](http://www.philadelphiafed.org/index.cfm), released May 3, 2018; Next release is June 5, 2018; Insurance Information Institute.
Length of US Business Cycles, 1960–Present*

The length of the expansions greatly exceeds the length of contractions (recessions).

*Through May 2018; June 2009 was the “official” end of recession.
Sources: National Bureau of Economic Research; Insurance Information Institute.
Labor Market Trends

Continuing Job Gains in the Private Sector Offset Flat Public Sector Employment
In February 2018, the workforce grew by 806,000. This big a jump is rare. The last time the workforce grew by over 800,000 was January 2003 (up 871,000).

Prosperity can appear to be trouble: The unemployment rate can increase if the civilian work force grows faster than the number newly employed.

If you are unemployed but haven’t looked for work in the past four weeks, you aren’t counted in the labor force. So it ebbs and grows according to perceived job opportunities.

Notes: Recession indicated by gray shaded column. Data are seasonally adjusted. Sources: Bureau of Labor Statistics; National Bureau of Economic Research (recession dates).
After a strong 2014-15, the pace of job growth has slowed somewhat.

*Seasonally adjusted
Sources: US Bureau of Labor Statistics; Insurance Information Institute
The Great Recession shifted employment from full-time to part-time. Full-time employment is finally above its pre-recession peak, but part-time hasn’t receded.

Opposite Trends for Components of Part-time Employment, 2003-2018

Both lines are now moving in good directions. People who work part-time “for economic reasons” would prefer full-time work. People who work part-time “for non-economic reasons” want (or need) part-time work.

Data are seasonally adjusted. Red-outlined box shows the Great Recession.
Sources: [https://fred.stlouisfed.org/series/LNS12032197](https://fred.stlouisfed.org/series/LNS12032197) and [https://fred.stlouisfed.org/series/LNS12032200](https://fred.stlouisfed.org/series/LNS12032200)
Unemployment and Underemployment Rates: Back to Normal?

January 2000 through April 2018
Seasonally Adjusted (%)

"Headline" Unemployment Rate U-3

Unemployment + Underemployment Rate U-6

For U-6, 7.5% to 9.5% is "normal."

U-6 went from 8.0% in March 2007 to 17.5% in October 2009

U-6 was 7.8% in Apr. 2018.

"Headline" unemployment was 3.9% in Apr. 2018. 4.0% to 5.5% is "normal."

Based on the latest readings, it appears that the job market is now back to "normal"

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).

A “discouraged worker” in a month did not actively look for work in the prior month for reasons such as
--thinks no work available,
--could not find work,
--lacks schooling or training,
--thinks employer thinks too young or old, and other types of discrimination.

Latest reading: 408,000 in Apr. 2018.
Nonfarm Payroll (Wages and Salaries): Quarterly, 2005:Q1–2018:Q1

Latest (2018:Q1) was $8.60 trillion, a new peak—$2.37T above 2009 trough

Prior peak was 2008:Q3 at $6.54 trillion

Recent trough (2009:Q1) was $6.23 trillion, down 5.3% from prior peak

Y-o-Y Growth rates
- 2011:Q1 over 2010:Q1: 5.5%
- 2012:Q1 over 2011:Q1: 3.9%
- 2013:Q1 over 2012:Q1: 2.3%
- 2014:Q1 over 2013:Q1: 5.2%
- 2015:Q1 over 2014:Q1: 4.9%
- 2016:Q1 over 2015:Q1: 3.2%
- 2017:Q1 over 2016:Q1: 3.4%
- 2018:Q1 over 2017:Q1: 4.5%

Note: Recession indicated by gray shaded column. Data are seasonally adjusted annual rates.
Sources: [http://research.stlouisfed.org/fred2/series/WASCUR](http://research.stlouisfed.org/fred2/series/WASCUR); National Bureau of Economic Research (recession dates); Insurance Information Institute.
Manufacturing Employment, 2010:Q1—2018:Q1

(Thousands)

Y-o-Y Growth rates
- 2011:Q1 over 2010:Q1: 1.9%
- 2012:Q1 over 2011:Q1: 1.9%
- 2013:Q1 over 2012:Q1: 0.8%
- 2014:Q1 over 2013:Q1: 1.0%
- 2015:Q1 over 2014:Q1: 1.6%
- 2016:Q1 over 2015:Q1: 0.3%
- 2017:Q1 over 2016:Q1: 0.4%
- 2018:Q1 over 2017:Q1: 1.9%

Construction and manufacturing employment constitute 1/3 of all workers comp payroll exposure.

Seasonally adjusted
Construction Employment, 2010:Q1—2018:Q1

(Thousands)

Y-o-Y Growth rates
2011:Q1 over 2010:Q1: -1.1%
2012:Q1 over 2011:Q1: 2.7%
2013:Q1 over 2012:Q1: 3.1%
2014:Q1 over 2013:Q1: 4.1%
2015:Q1 over 2014:Q1: 4.9%
2016:Q1 over 2015:Q1: 5.5%
2017:Q1 over 2016:Q1: 3.5%
2018:Q1 over 2017:Q1: 3.4%

Construction and manufacturing employment constitute 1/3 of all workers comp payroll exposure.

Seasonally adjusted
Coal Mining Employment, 2010:Q1—2018:Q1

(Thousands)

Y-o-Y Growth rates
2011:Q1 over 2010:Q1: 6.7%
2012:Q1 over 2011:Q1: 5.3%
2013:Q1 over 2012:Q1: -10.5%
2014:Q1 over 2013:Q1: -7.4%
2015:Q1 over 2014:Q1: -7.6%
2016:Q1 over 2015:Q1: -23.5%
2017:Q1 over 2016:Q1: -1.7%
2018:Q1 over 2017:Q1: 2.1%

Seasonally adjusted

Construction and manufacturing employment constitute 1/3 of all workers comp payroll exposure.
P/C Insurance Industry: 
Financial Update

2017 Was a Tough Year

Shaded areas denote “hard market” periods

Net Written Premiums rose 4.6% in 2017, the best one-year gain since 2003.
Commercial Lines is Prone to Much More Cyclical Volatility Than Personal Lines.

Note: Data include state funds beginning in 1998.
Sources: A.M. Best; Insurance Information Institute.
Underwriting Performance
Business Nonresidential Fixed Investment Tracks Commercial Property Premium Growth

Econometric forecasts of business fixed investment anticipate growth of 4.5%–7.0% in 2018 and at 2.5%–6.5% in 2019.

Investment in structures, equipment, and software is expected to grow at least partly due to the provisions of the Tax Cuts and Jobs Act.

*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.
Net Underwriting Gains & Losses, Annually, 2007-2017

2013/14/15 were welcome respites from 2008/11/12, which were among the costliest years for insured disaster losses in U.S. history. The longer-term trend is for more – not fewer – costly events.

Sources: SNL Financial; Insurance Information Institute.
P/C Insurance Industry Combined Ratio, 2001-2017*

Sources: A.M. Best; ISO, a Verisk Analytics company; I.I.I.
U.S. Insured Catastrophe Losses, 1989-2017

Insured CAT losses surpassed $30 billion in 7 of the last 17 years (only once in the prior 12 years).

In the ten years since 2001 when CAT losses were below $30 billion, the yearly average was $13.8 billion.

Note: 2001 figure includes $20.3B for 9/11 losses reported through 12/31/01 ($25.9B 2011 dollars). Includes only business and personal property claims, business interruption and auto claims. Non-prop/BI losses = $12.2B ($15.6B in 2011 dollars).

Sources: Property Claims Service, a Verisk Analytics business; Insurance Information Institute.
The average number of storms in the last 5 years is less than half of the number in 2000-2005. Is this the “new normal”?

Sources: [http://www.spc.ncep.noaa.gov/climo/online/monthly/2017_annual_summary.html](http://www.spc.ncep.noaa.gov/climo/online/monthly/2017_annual_summary.html) and earlier years; Insurance Information Institute.
Number of Large Hail Storms, Top 25 States, 2017

In 2017, five states averaged over one large hail storm per day.

Together, these five accounted for 42% of all hail storms nationwide.

CAT claims are significant in some calendar quarters and less so in others. They are 8-10% of total claims every Q2, but in Q1 usually only 4-5%.

Sources [http://www.spc.ncep.noaa.gov/climo/online/monthly/2017_annual_summary.html](http://www.spc.ncep.noaa.gov/climo/online/monthly/2017_annual_summary.html); Insurance Information Institute.
Number of Large Hail Storms, 2017, Varied Widely by State and Region

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Number of Large Hail Storms, 2017, Varies Widely by State and Region

Southwest

Great Plains

Mountain

Far West

Source: NAIC
To rent or to buy?

Since 2004 the number of renter-occupied housing units has grown by about 10.5 million units (+34%), but there has been no growth in the number of owner-occupied housing units in 12 years. Did this streak end in 2017?

Sources: U.S. Census Bureau at [http://www.census.gov/housing/hvs/data/histtabs.html](http://www.census.gov/housing/hvs/data/histtabs.html), Table 8; Insurance Information Institute.
Investments

Investment Performance is a Key Driver of Profitability

Depressed Yields Will Necessarily Influence Underwriting & Pricing

Yields on 10-Year US Treasury Notes have been below 3% for over 5 years: 10-year bonds bought in 2008 at 4% will be reinvested at 2.9% for 10 more years.

Since nearly 50% of P/C bond/cash investments are in 5-year or longer maturities, most P/C insurer portfolios will have low-yielding bonds for years to come.

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

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

Sources: Blue Chip Economic Indicators (5/18); Insurance Information Institute
P/C Carrier Yields Have Been Falling for Over a Decade, Reflecting the Long Downtrend in Prevailing Interest Rates.

Even as Prevailing Rates Rise in the Next Few Years, Portfolio Yields Are Unlikely to Rise Quickly, Since Low Yields of Recent Years Are “Baked In” to Future Returns.

Sources: NAIC data, sourced from S&P Global Market Intelligence; Insurance Information Institute.
Sources of investment gains

Net investment income has been steady, but realized capital gains/losses have been somewhat variable.

Sources: NAIC data, sourced from S&P Global Market Intelligence; Insurance Information Institute.
Profits and Capacity
P/C industry net income after taxes*

Billions, 2017 dollars

$57.4  $19.1  $32.2  $9.0  $32.1  $53.8  $40.6  $46.9  $33.9  $23.6

In the first three quarters of the year, net income varied. 2017 was the fourth lowest profit in the last 11 years.

*Through third quarter. Adjusted for inflation using the BLS CPI calculator, to 2017 dollars.
Sources: NAIC data, sourced from S&P Global Market Intelligence; Insurance Information Institute.
Key sources of P/C insurer profits

Net investment gains
- Underwriting gains/losses

Data are before taxes and exclude extraordinary items.
Sources: NAIC data, sourced from S&P Global Market Intelligence; Insurance Information Institute.
Profitability Peaks & Troughs in the P/C Insurance Industry, 1975-2017

If historical patterns hold, next ROE peak could be in 2018.

*Profitability = P/C insurer ROEs. 2011-17 figures are estimates based on ROAS data.
Note: Data for 2008-2014 exclude mortgage and financial guaranty insurers.
Sources: Insurance Information Institute; Natl. Assoc. of Insurance Comm.; ISO, a Verisk Analytics company; A.M. Best, Conning.
Policyholder Surplus, Year-end, 2006–2017

The industry now has $1 of surplus for every $0.73 of NPW, the strongest claims-paying status in its history.

The P/C insurance industry entered 2018 in very strong financial condition.

Surplus as of 12/31/17 stood at $752.5B

Surplus grew by 7.4% over 12/31/2016

Sources: ISO, A.M. Best.
Thank you