



**INSURANCE
INFORMATION
INSTITUTE**

Today's Uncertain Economy: Implications for Public Entities and P/C Insurance

Genesis 2019 Client Forum

Chicago, IL

April 18, 2019

**Steven N. Weisbart, Ph.D., CLU, Senior Vice President & Chief Economist
Insurance Information Institute ♦ 110 William Street ♦ New York, NY 10038**

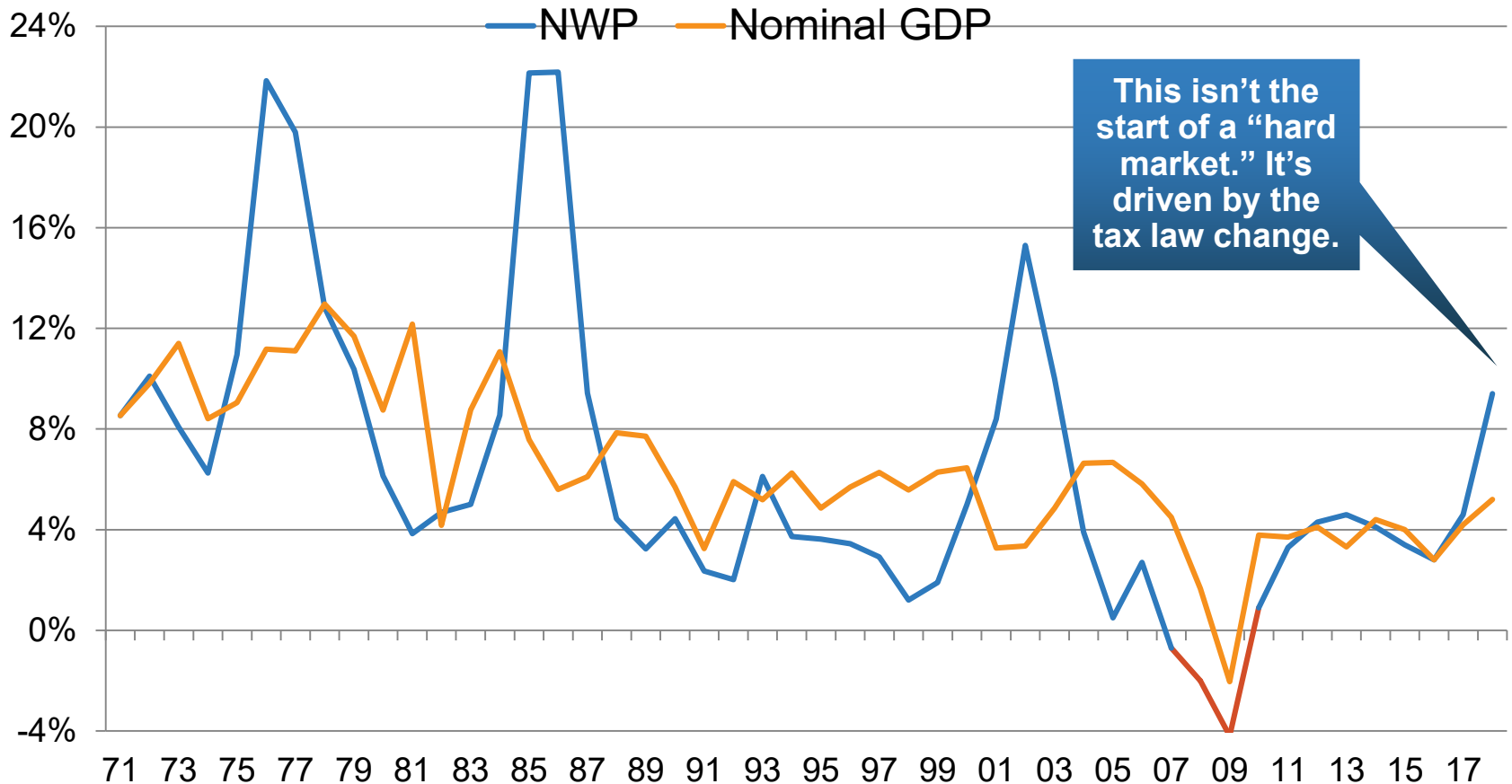
The Strength of the Economy Will Influence the Insurance Environment

Premium Rates, Claims,
and Investment Income Will Be Affected



The Economy Drives P/C Insurance Industry Premiums:

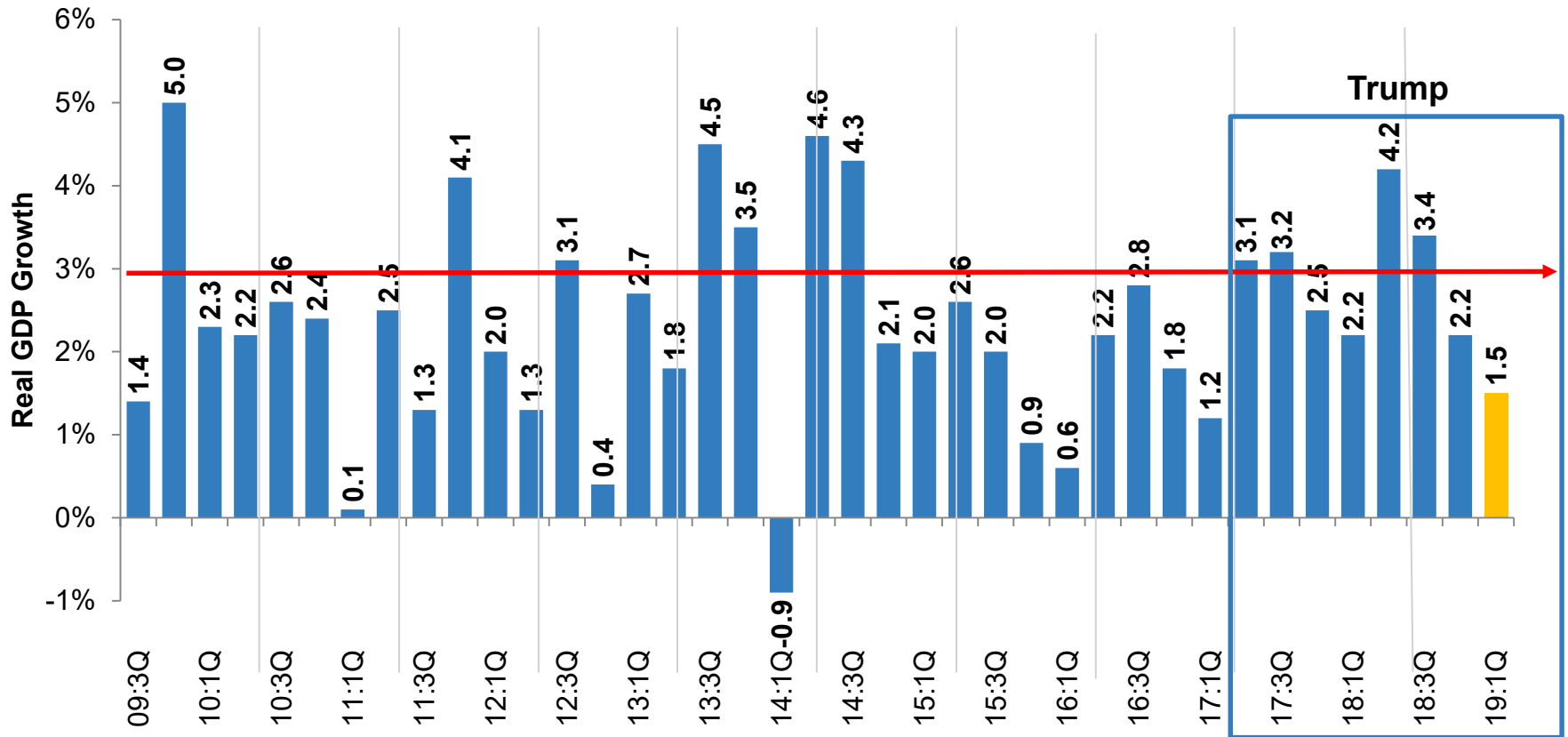
Net Premium Growth (All P/C Lines) vs. Nominal GDP: Annual Change, 1971-2018



Except for the three “hard markets” in this 45-year period, Net Written Premiums track Nominal GDP—not year by year but fairly well.



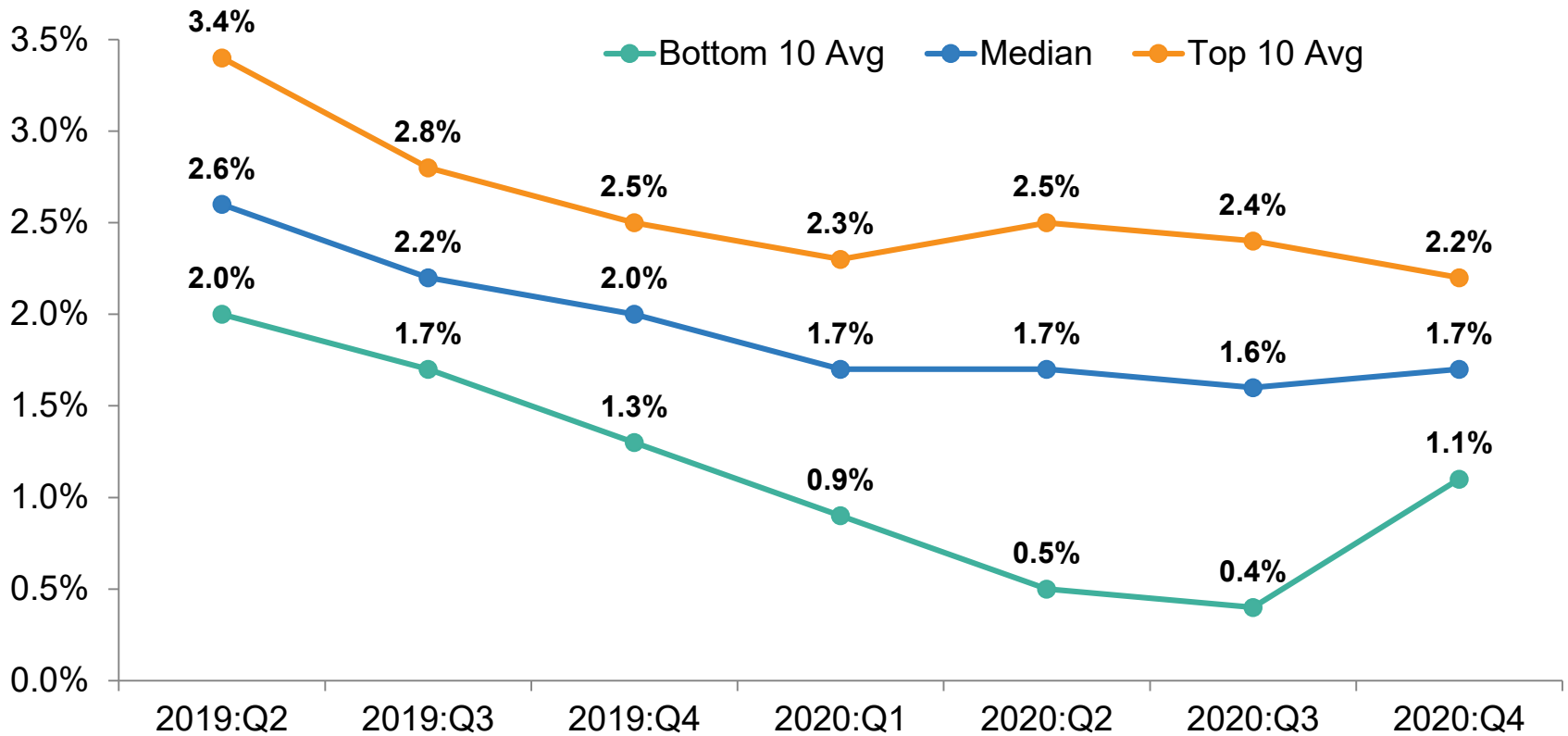
U.S. Post-Recession Real GDP Growth,* Quarterly (Seasonally-Adjusted at an Annual Rate)



Since the Great Recession ended, the economy (as measured by real GDP) rarely grew faster than 3% (at an annual rate) in a calendar quarter. Only 4 times in the 8 quarters since the Trump presidency began.



Yearly U.S. Real GDP Growth: Range of Forecasts, 2019-2020

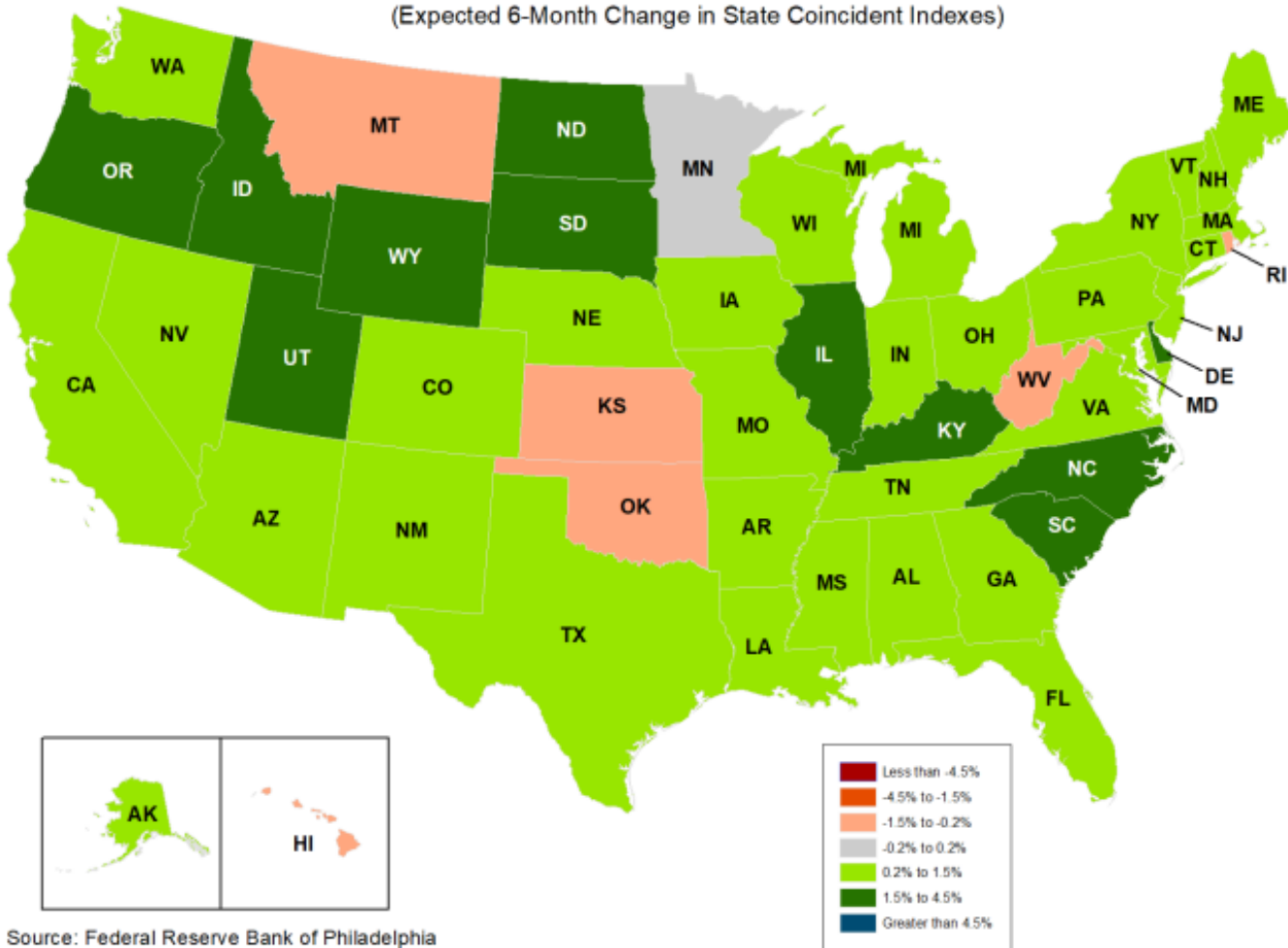


**Tough times ahead?
Forecasts expect U.S. growth to slow markedly by 2020.**



State-by-State Leading Indicators through January 2019

January 2019 State Leading Indexes
(Expected 6-Month Change in State Coincident Indexes)



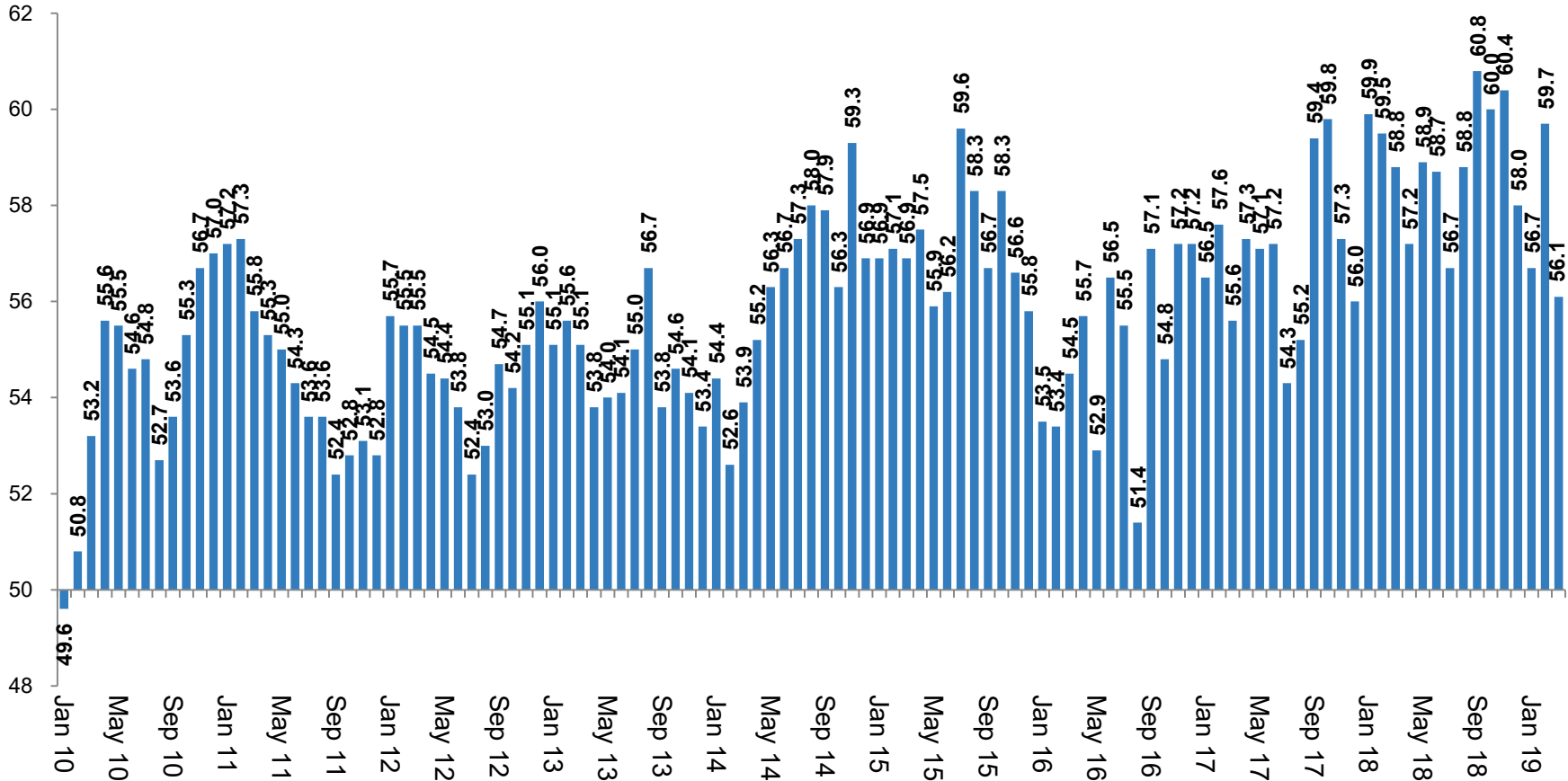
Near-term growth forecasts vary widely by state.
Strongest growth = blue (over 4.5%);
dark green (1.5%-4.5%);
then light green;
then gray;
weakest = pink

Source: Federal Reserve Bank of Philadelphia



Sources: Federal Reserve Bank of Philadelphia at www.philadelphiafed.org/index.cfm, released April 4, 2019; Next release is April 12, 2019; Insurance Information Institute.

ISM Non-Manufacturing Index (Values > 50 Indicate Expansion), January 2010-March 2019



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 again strong.



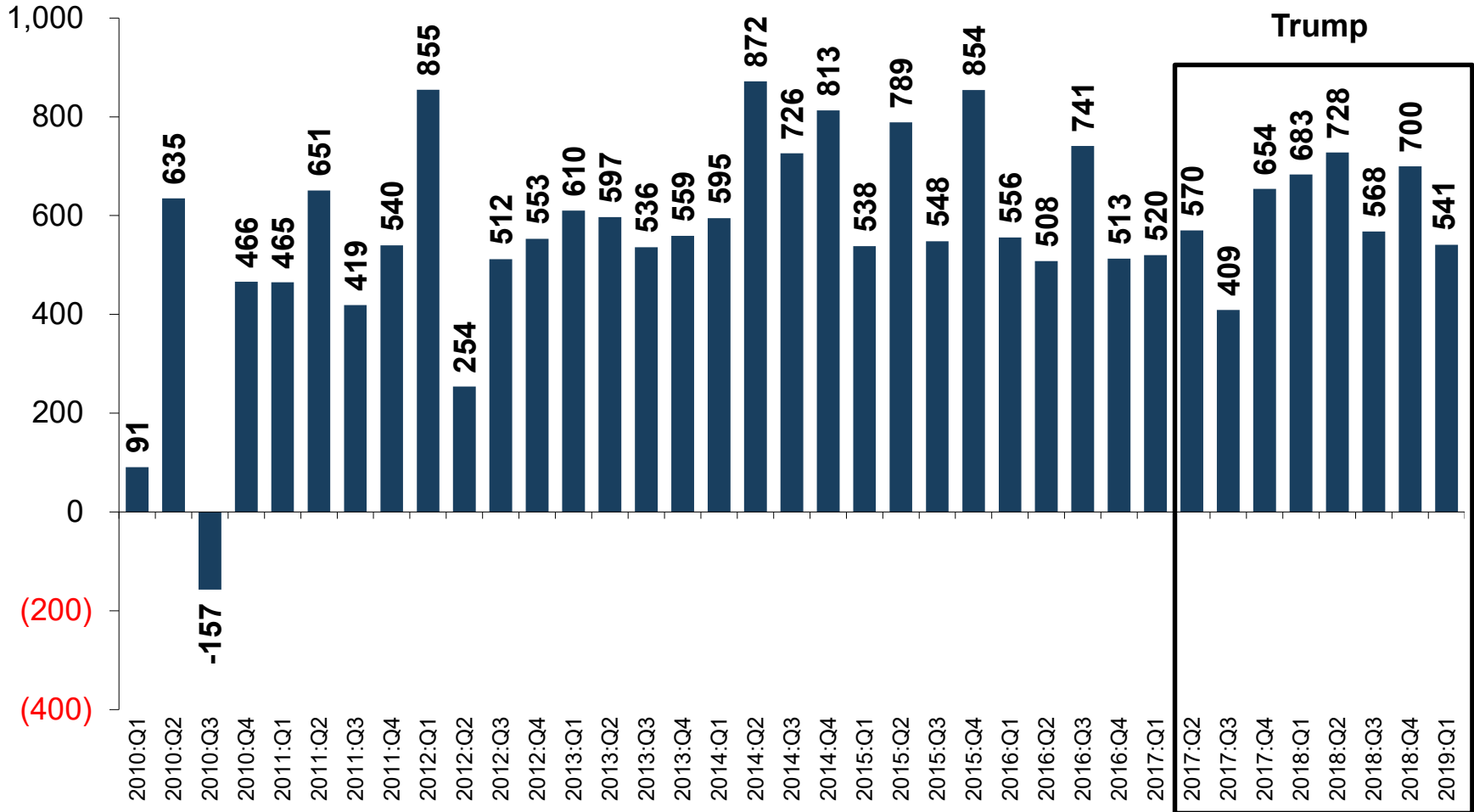
Labor Market Trends

Continuing Job Gains Lure Some
“on the Sidelines” to Enter the Labor Force



Nonfarm Employment, Quarterly Change, 2010 – 2019*

Thousands



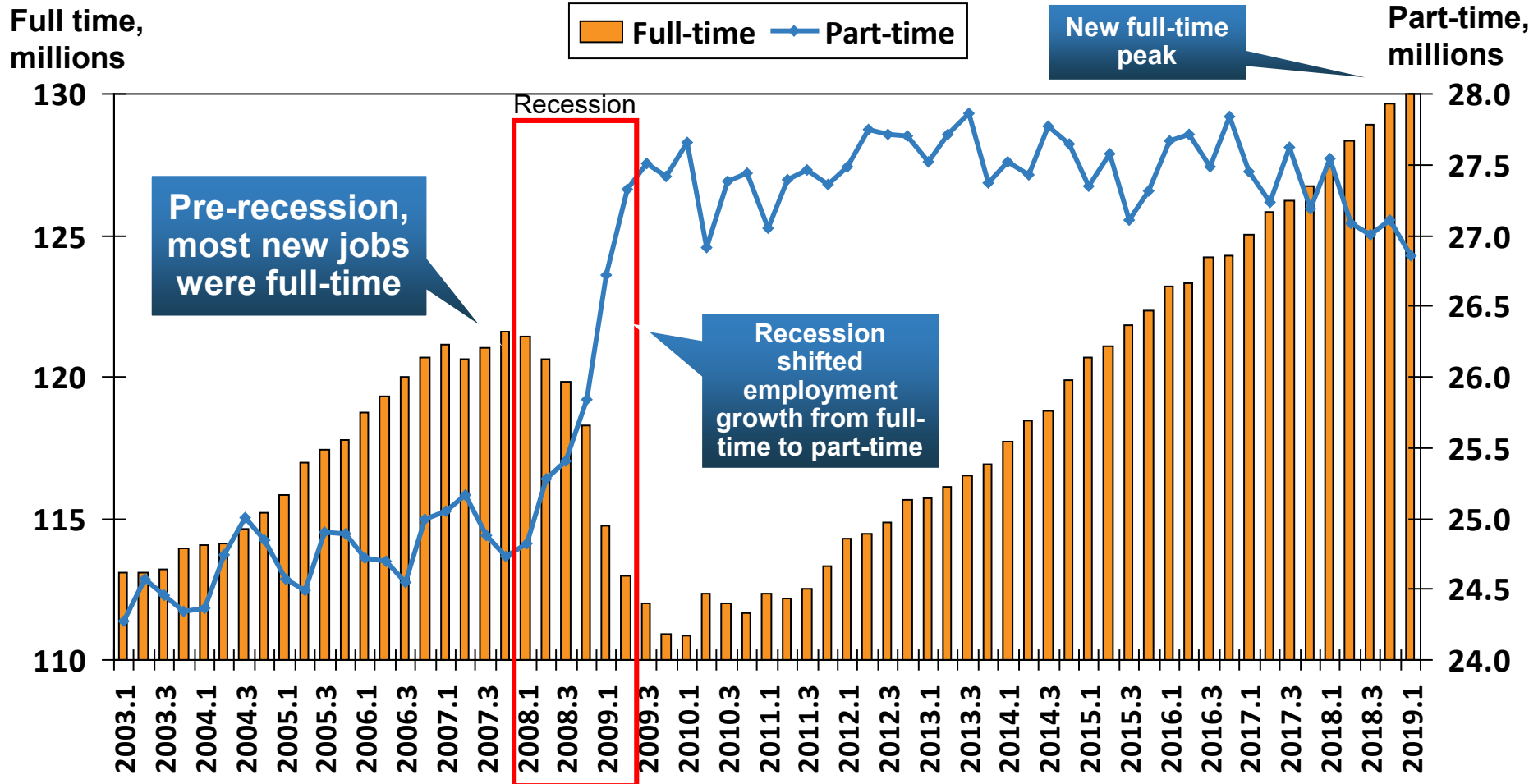
Trump

After a strong 2014-15, the pace of job growth has slowed slightly.



*Seasonally adjusted, growth as of end of each quarter
Sources: US Bureau of Labor Statistics; Insurance Information Institute

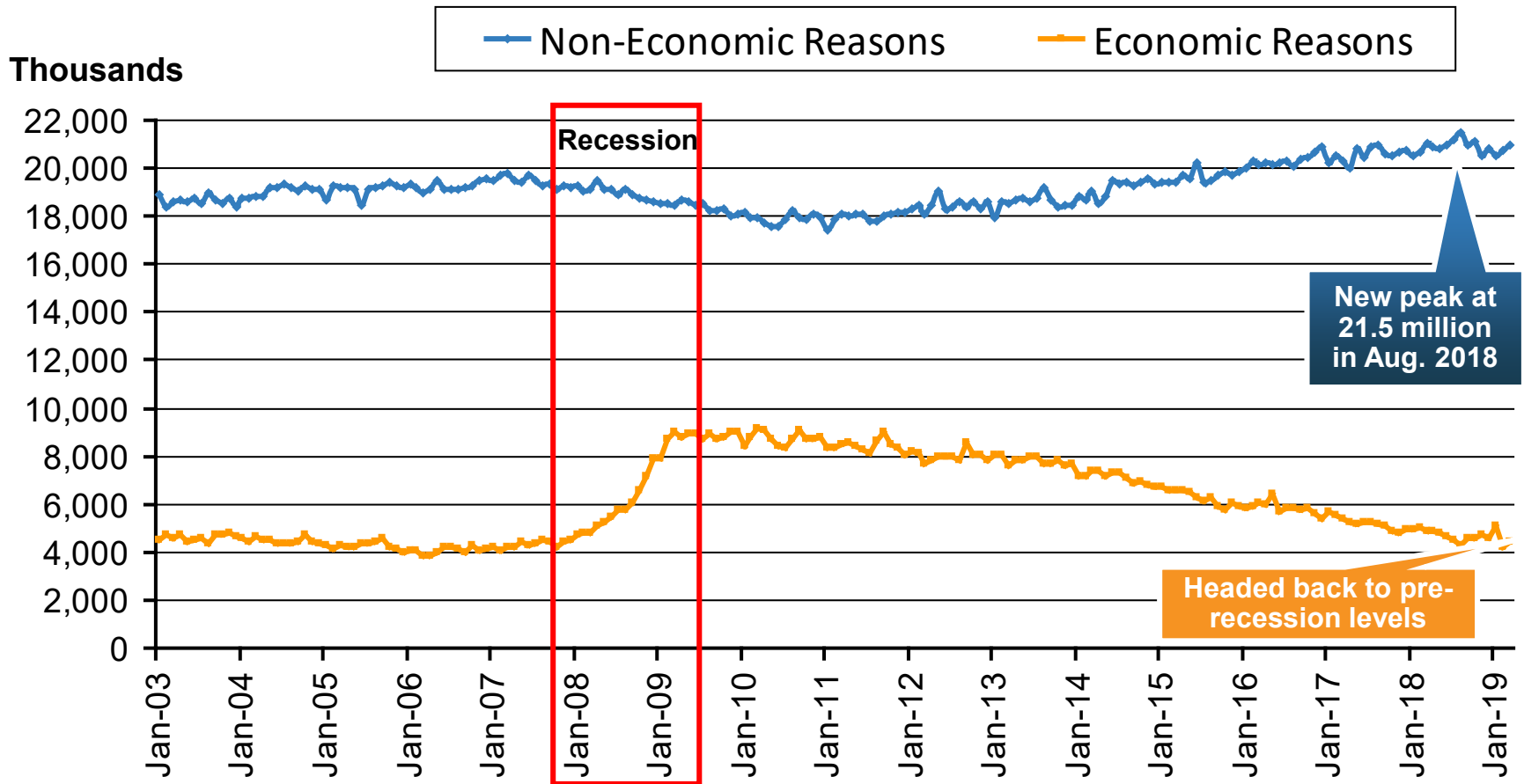
Full-time vs. Part-time Employment, Quarterly, 2003-2019



The Great Recession shifted employment from full-time to part-time. Full-time employment is now well above its pre-recession peak, but part-time has barely receded.



Opposite Trends for Components of Part-time Employment, 2003-2019



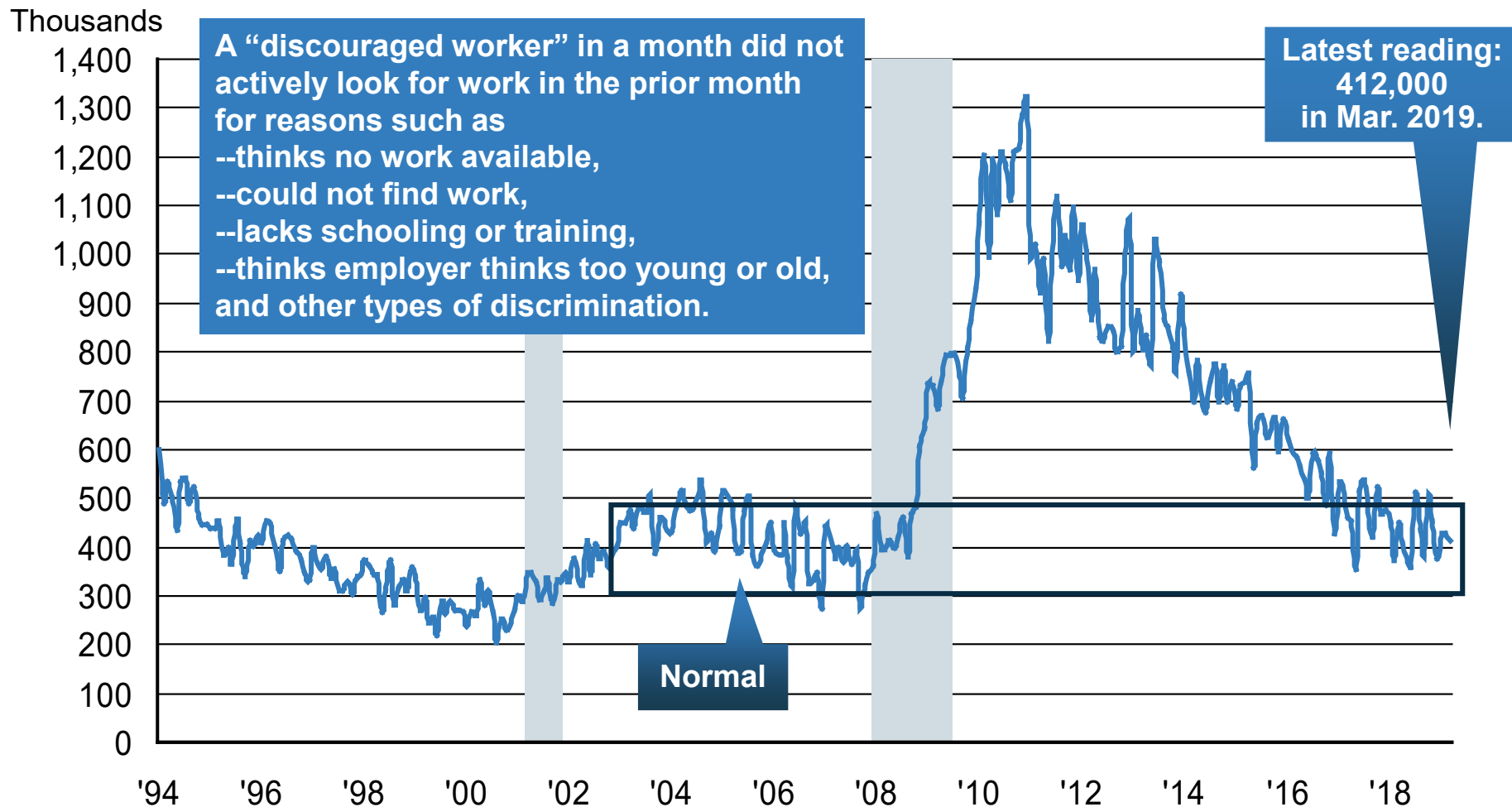
Both lines are now moving in good directions. People who work part-time “for economic reasons” would prefer full-time work. People who work part-time “for non-economic reasons” want (or need) part-time work.



Data are seasonally adjusted. Red-outlined box shows the Great Recession.

Sources: <https://fred.stlouisfed.org/series/LNS12032197> and <https://fred.stlouisfed.org/series/LNS12032200>

Number of “Discouraged Workers”: Back to a “Normal” Range Jan. 1994 – Mar. 2019



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).

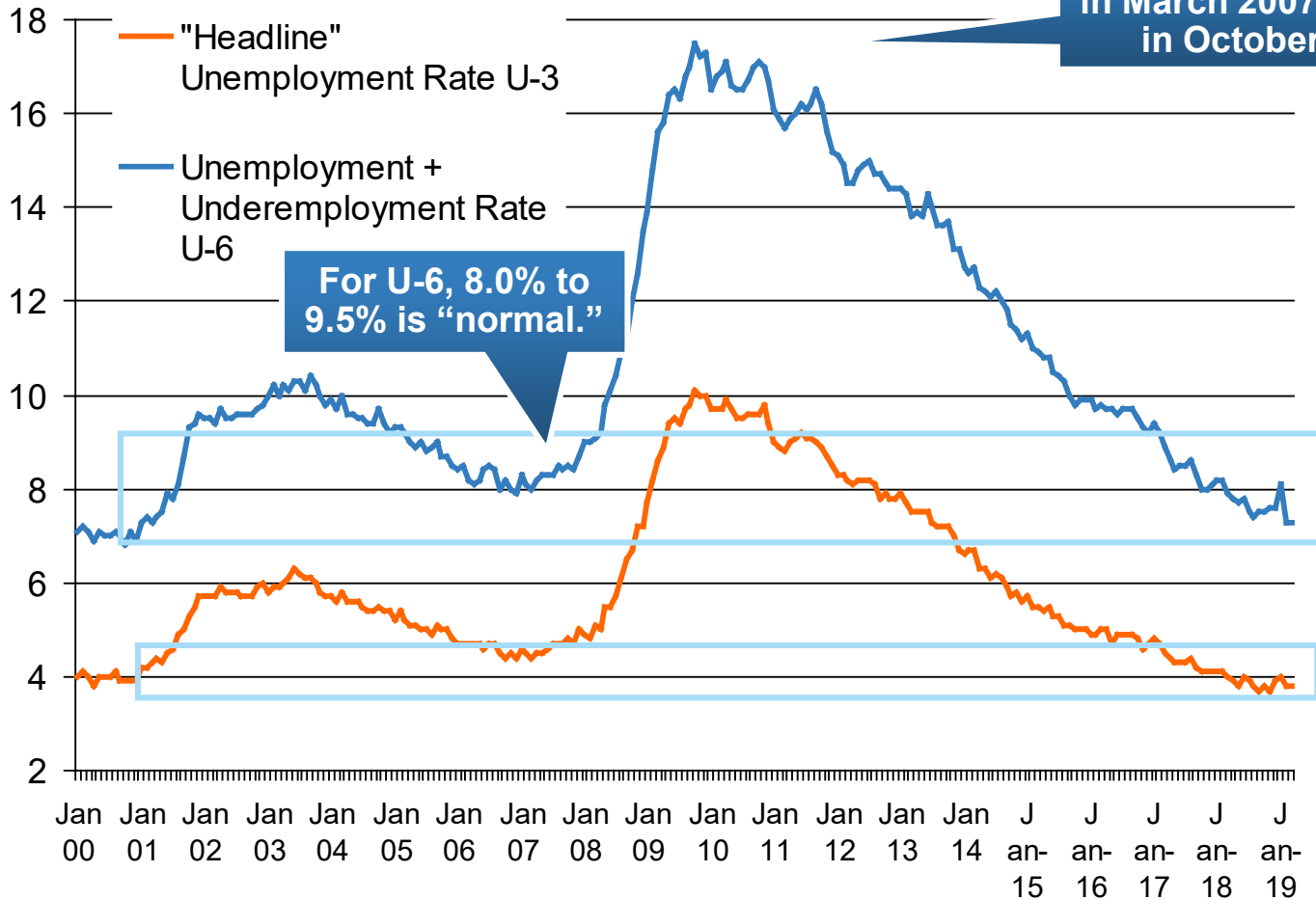


Notes: Recessions indicated by gray shaded columns. Data are seasonally adjusted.

Sources: Bureau of Labor Statistics; National Bureau of Economic Research (recession dates).

Unemployment and Underemployment Rates: Back to Normal?

January 2000 through March 2019
Seasonally Adjusted (%)



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

For U-6, 8.0% to 9.5% is "normal."

U-6 was 7.3% in Mar. 2019.

"Headline" unemployment was 4.1% in Mar. 2018. 4.5% to 5.5% is "normal."

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

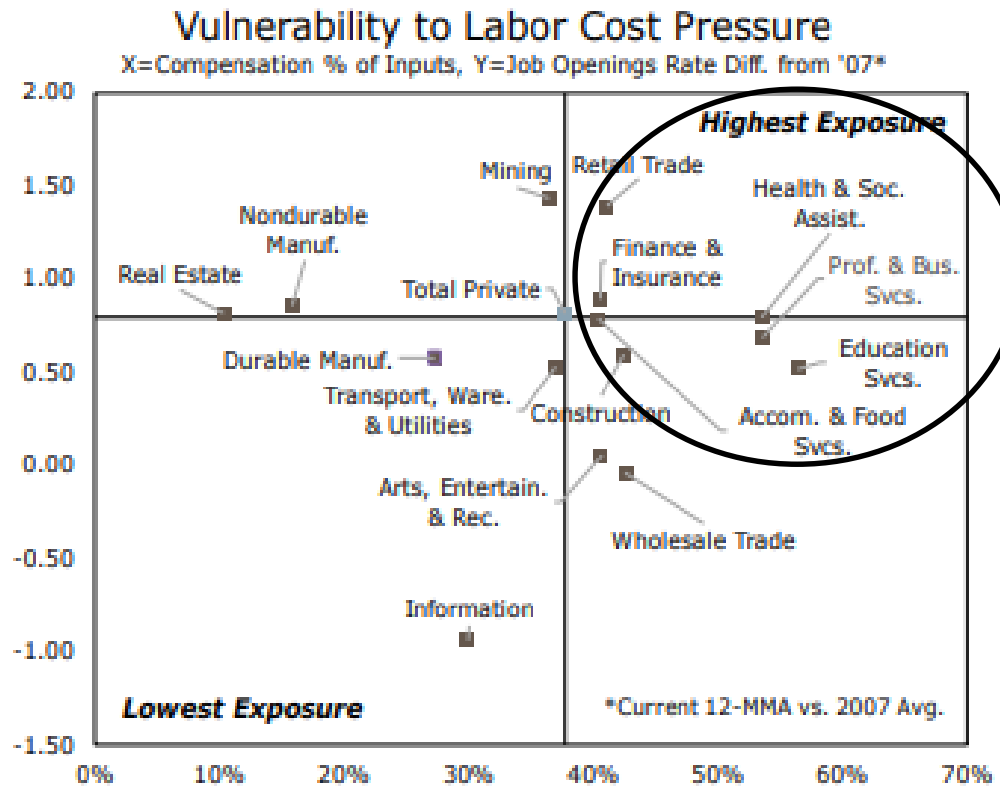


Sources: US Bureau of Labor Statistics; Insurance Information Institute.

Which Private-Sector Industries Are Most Vulnerable to Pressures to Raise Pay?

Y axis: Job Openings Rate in 2017 vs 2007

X axis: Total Compensation as a % of Total Inputs



Most Vulnerable:
Industries with

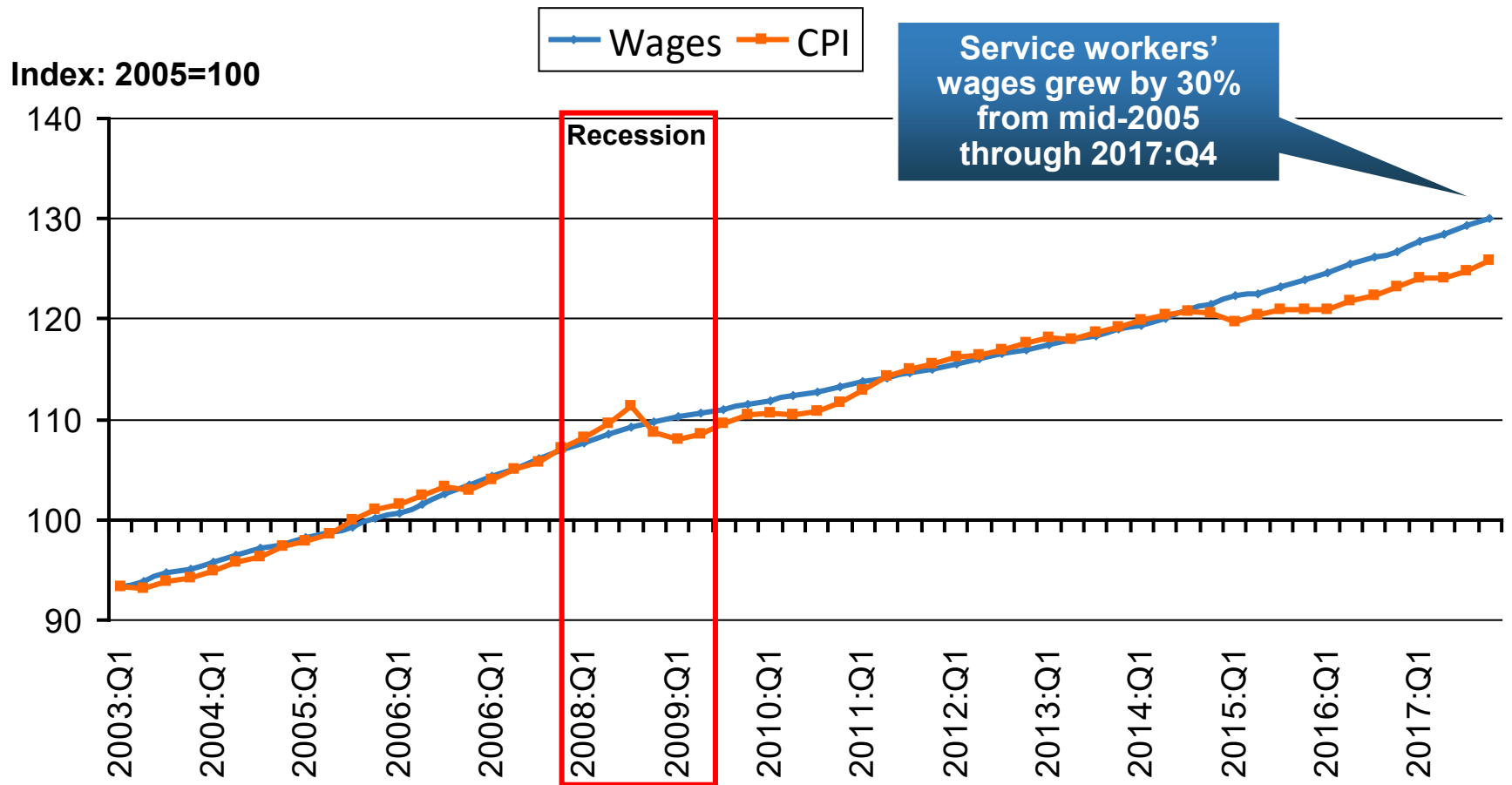
high compensation as a percent of inputs and also

a high percent of job openings vs. previous job-openings peak.

Source: U.S. Department of Labor, U.S. Department of Commerce and Wells Fargo Securities



Service Workers: Wage Growth, Quarterly, 2003-2017

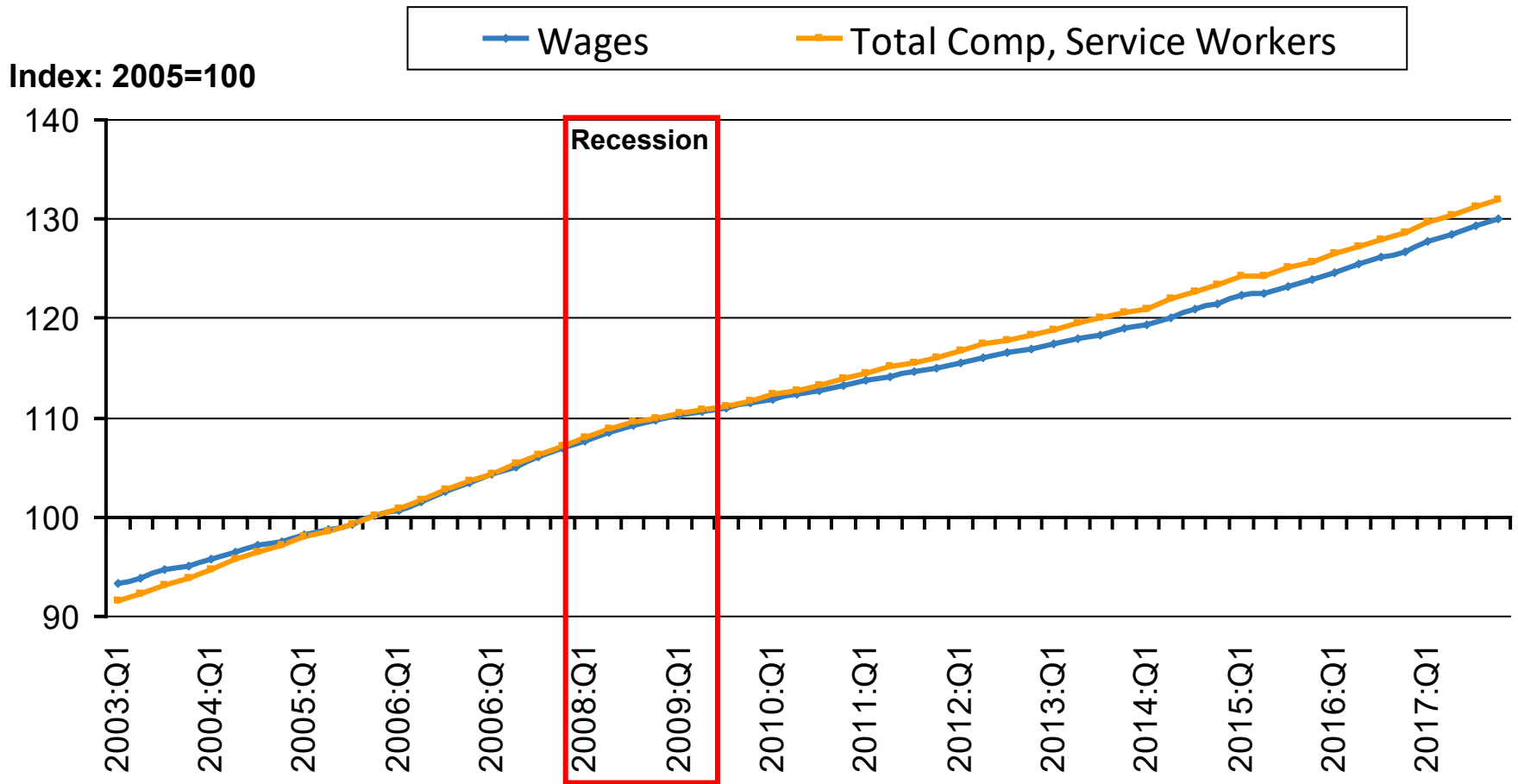


Wages only kept up with, but did not exceed, inflation from 2003 through 2014. Since then, a small gain in purchasing power.



Data are seasonally adjusted. Red-outlined box shows the Great Recession.
Sources: U.S. Bureau of Labor Statistics; Insurance Information Institute.

Service Workers: Wages and Total Compensation, Quarterly, 2003-2017



Virtually no difference in growth rates of wages and total compensation for service workers over the last 15 years.

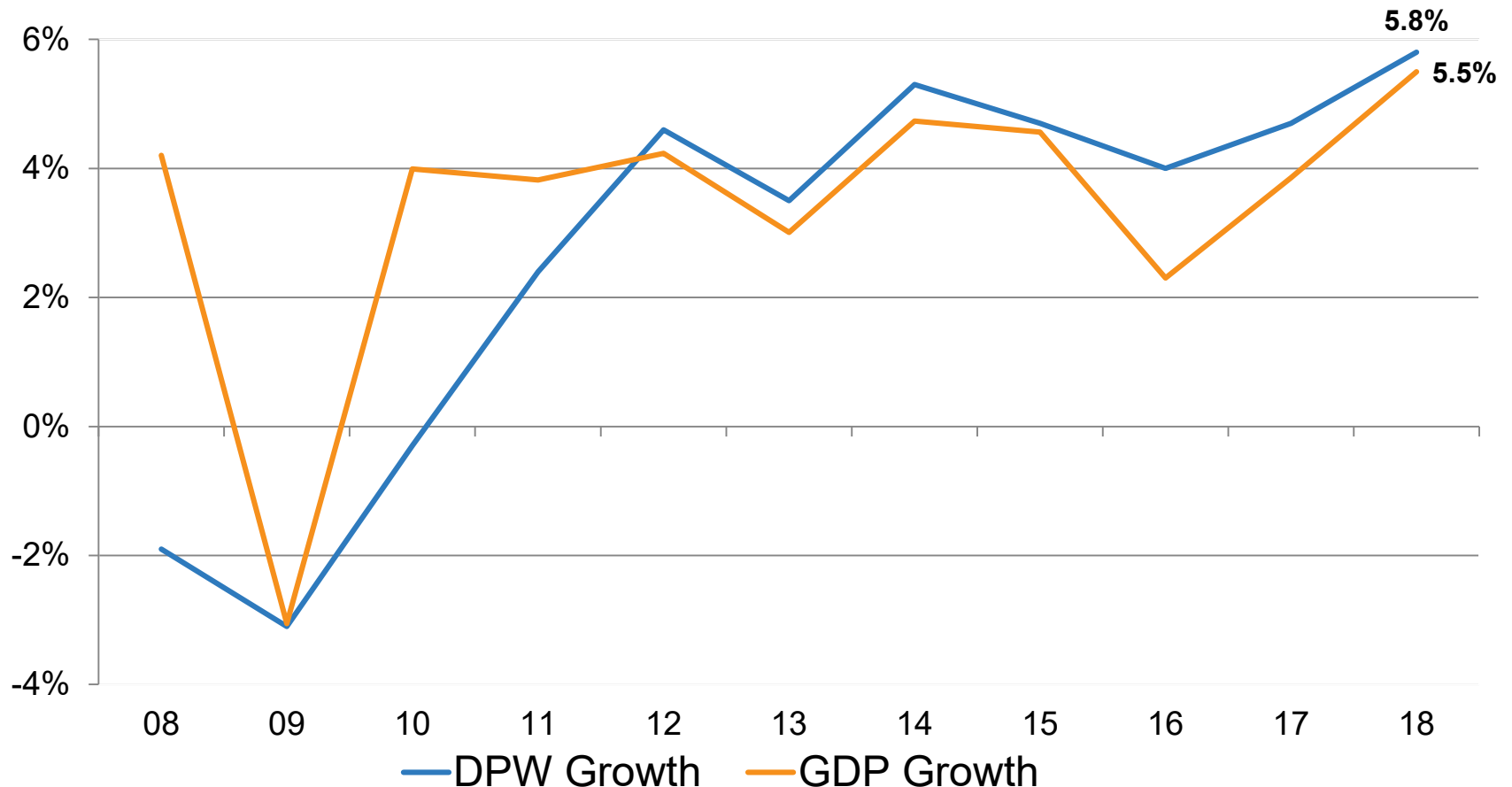


Data are seasonally adjusted. Red-outlined box shows the Great Recession.
Sources: U.S. Bureau of Labor Statistics; Insurance Information Institute.



Insurance Industry Economic Trends

Direct Premium Growth, Annual Change



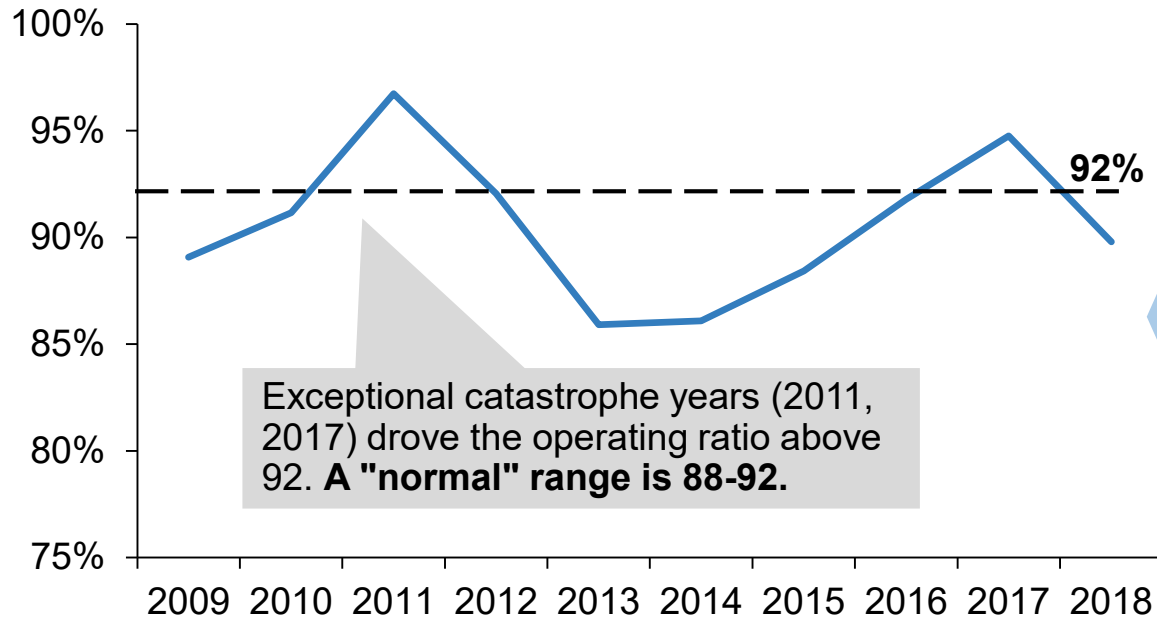
▼ **Direct Premiums Continue to Track Economic Growth**



All data through second quarter.

SOURCES: NAIC data sourced through S&P Global Intelligence, Bureau of Economic Affairs, Insurance Information Institute.

P/C Industry Operating Ratio, 2009 - 2018



- Operating ratio = combined ratio (losses plus expenses as a percent of earned premiums) minus net investment income as a percent of earned premiums.
- Operating ratio includes all insurance and investment operations except taxes and capital gains and losses.
- The lower the ratio, the better.

Other P/C Industry Metrics

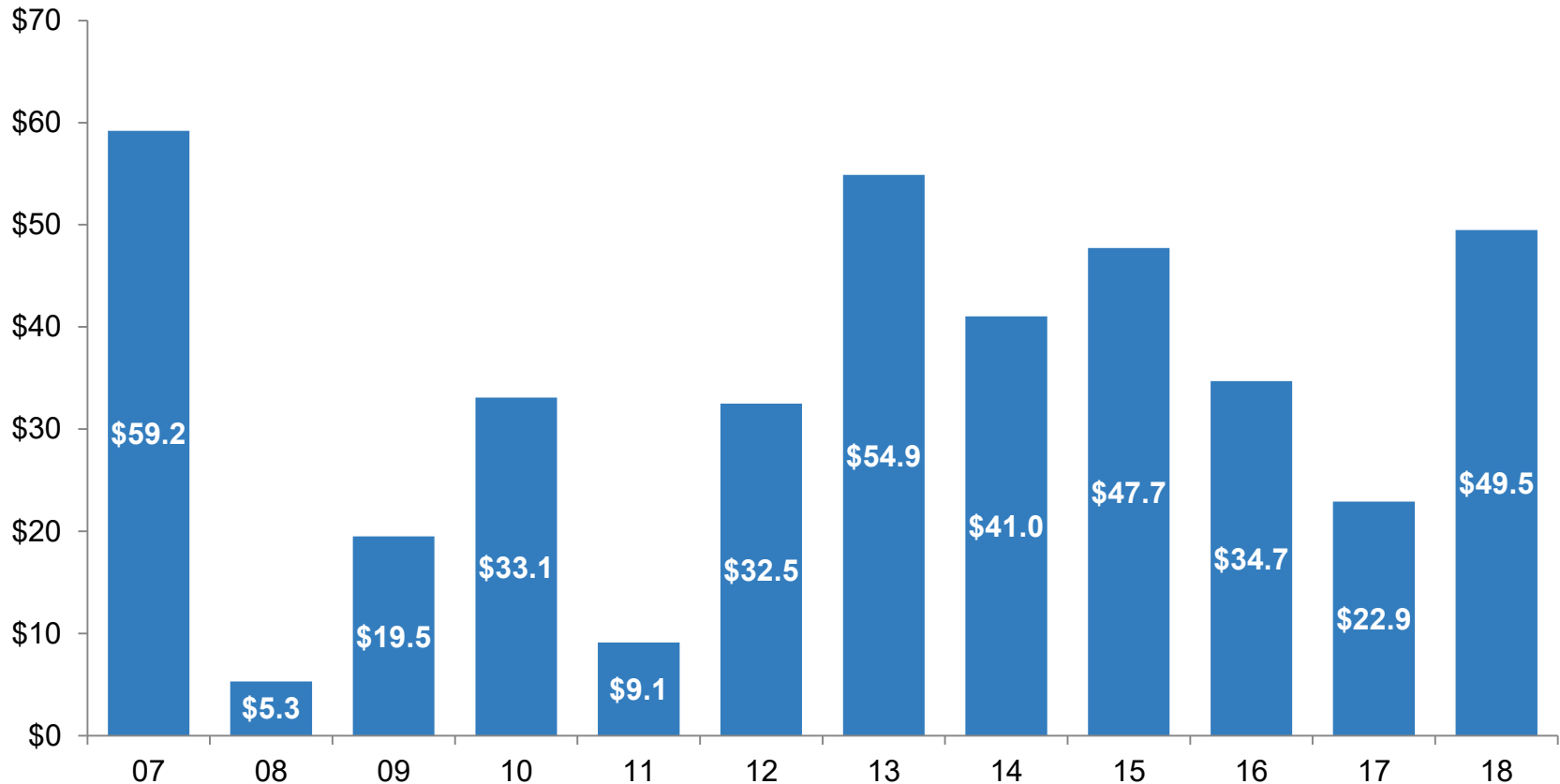
Insurance Industry Indicators	2017	2018	Analysis
Direct Premiums Written	4.75%	4.87%	Generally follows nominal (not inflation-adjusted) GDP growth
Combined Ratio	103.9	99.3	Lower is better; the industry profited from insurance operations in 2018
Net Yield on Invested Assets	3.03%	3.35%	Interest rates are forecast to decline in 2019 and 2020



Sources: AM Best; S&P Global; Insurance Information Institute

P/C industry net income after taxes

Billions, 2018 dollars

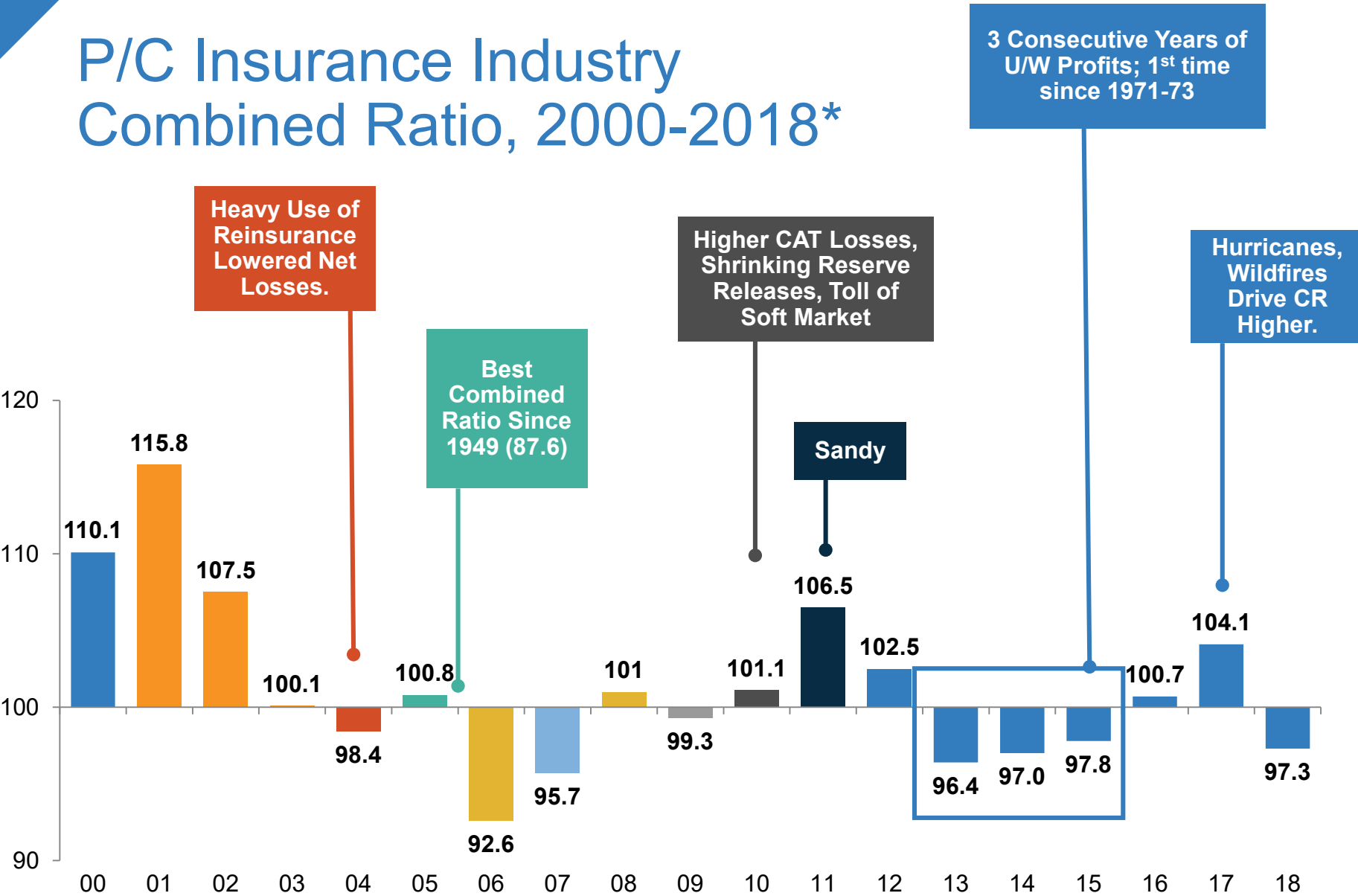


▼ Catastrophes Drove Earnings Down in 2017, Continuing a Four-Year Slide in Inflation-Adjusted Profits.



Through third quarter. Adjusted for inflation using the BLS CPI calculator, to 2018 dollars.
Sources: NAIC data, sourced from S&P Global Market Intelligence; Insurance Information Institute.

P/C Insurance Industry Combined Ratio, 2000-2018*

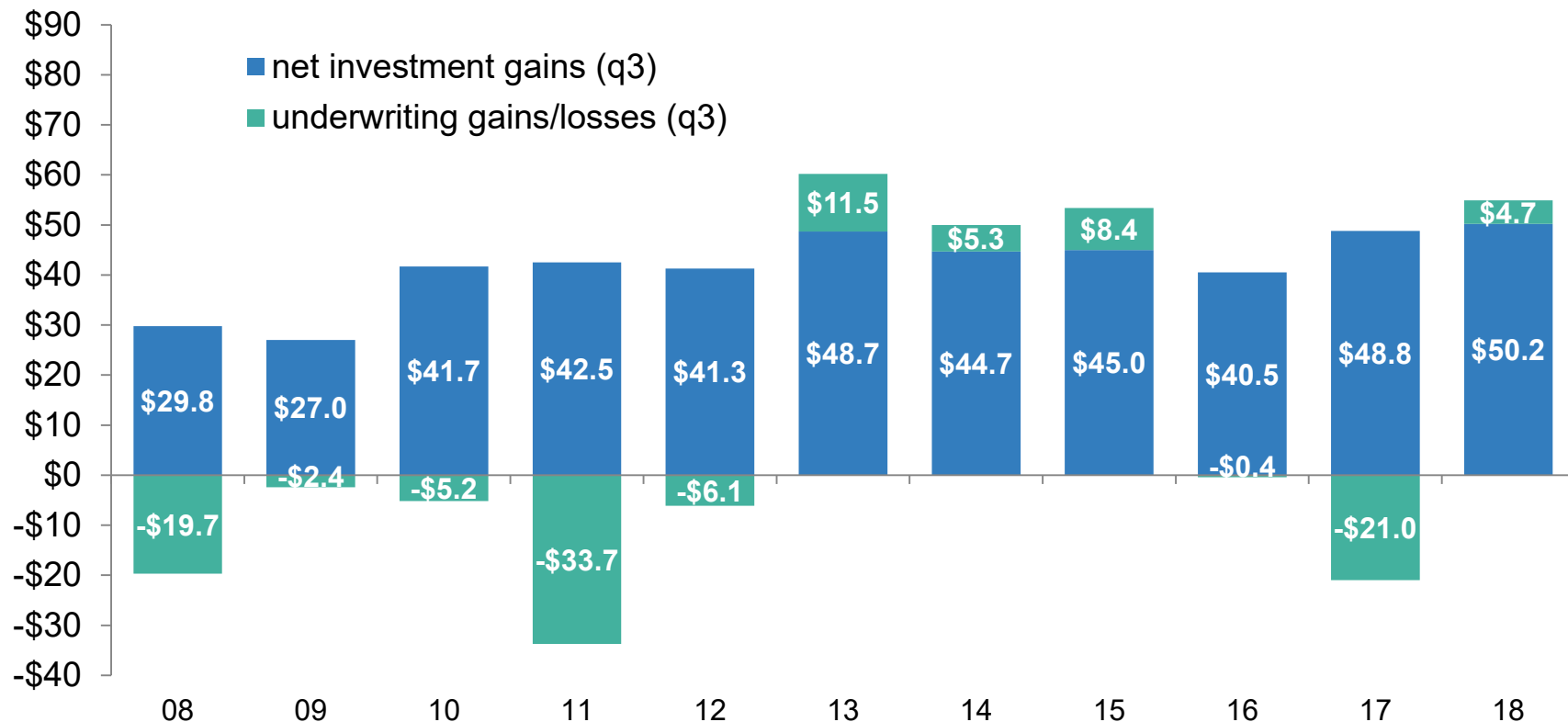


*Excludes Mortgage & Financial Guaranty insurers 2008-2014.
 Including M&FG, 2008=105.1, 2009=100.7, 2010=102.4, 2011=108.1; 2012:=103.2; 2013: = 96.1; 2014: = 97.0.
 Sources: A.M. Best; ISO, a Verisk Analytics company; I.I.I. estimate for 2018.



Key sources of P/C insurer profits

\$ Billions

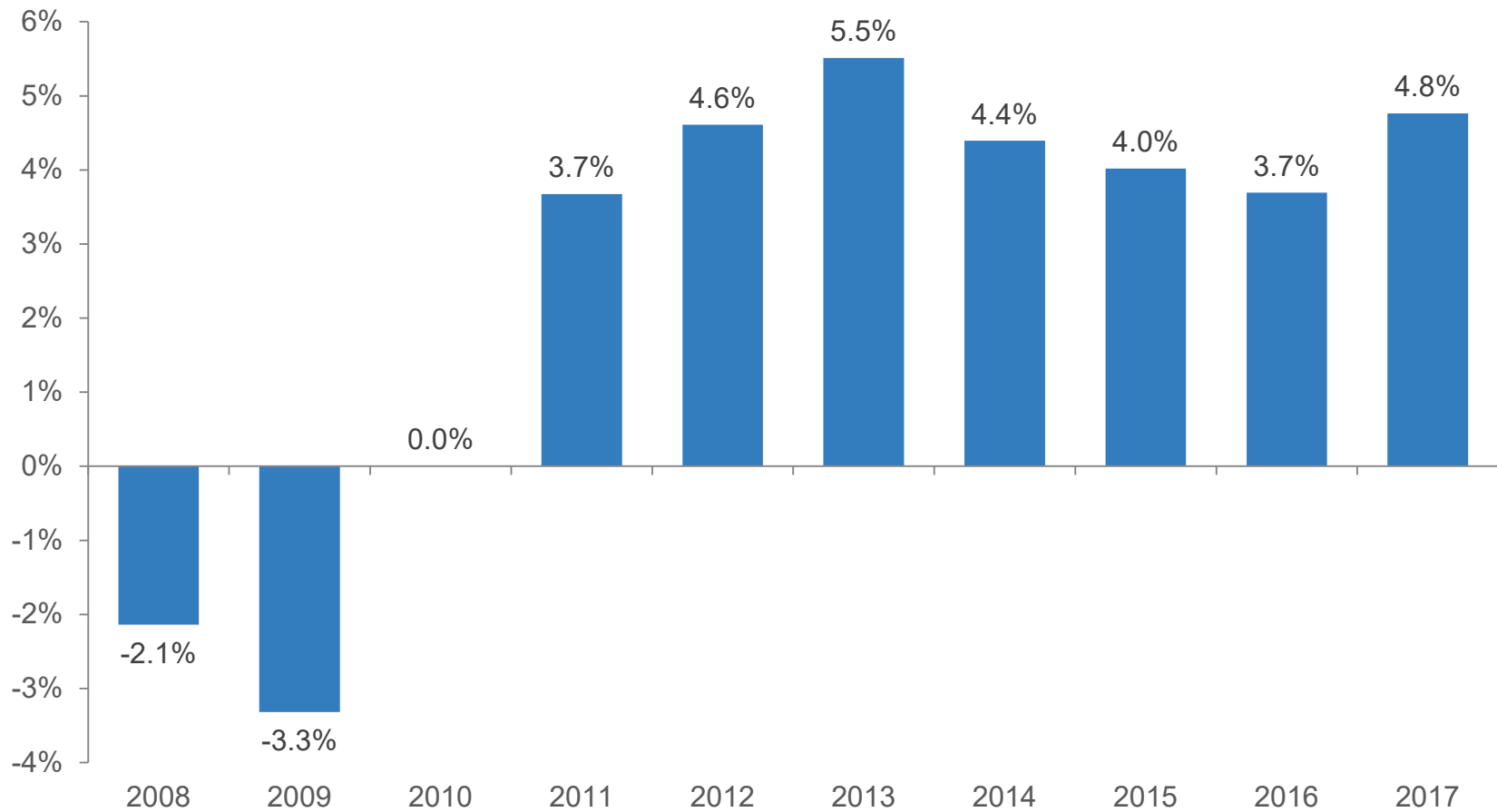


Data are before taxes and exclude extraordinary items.

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

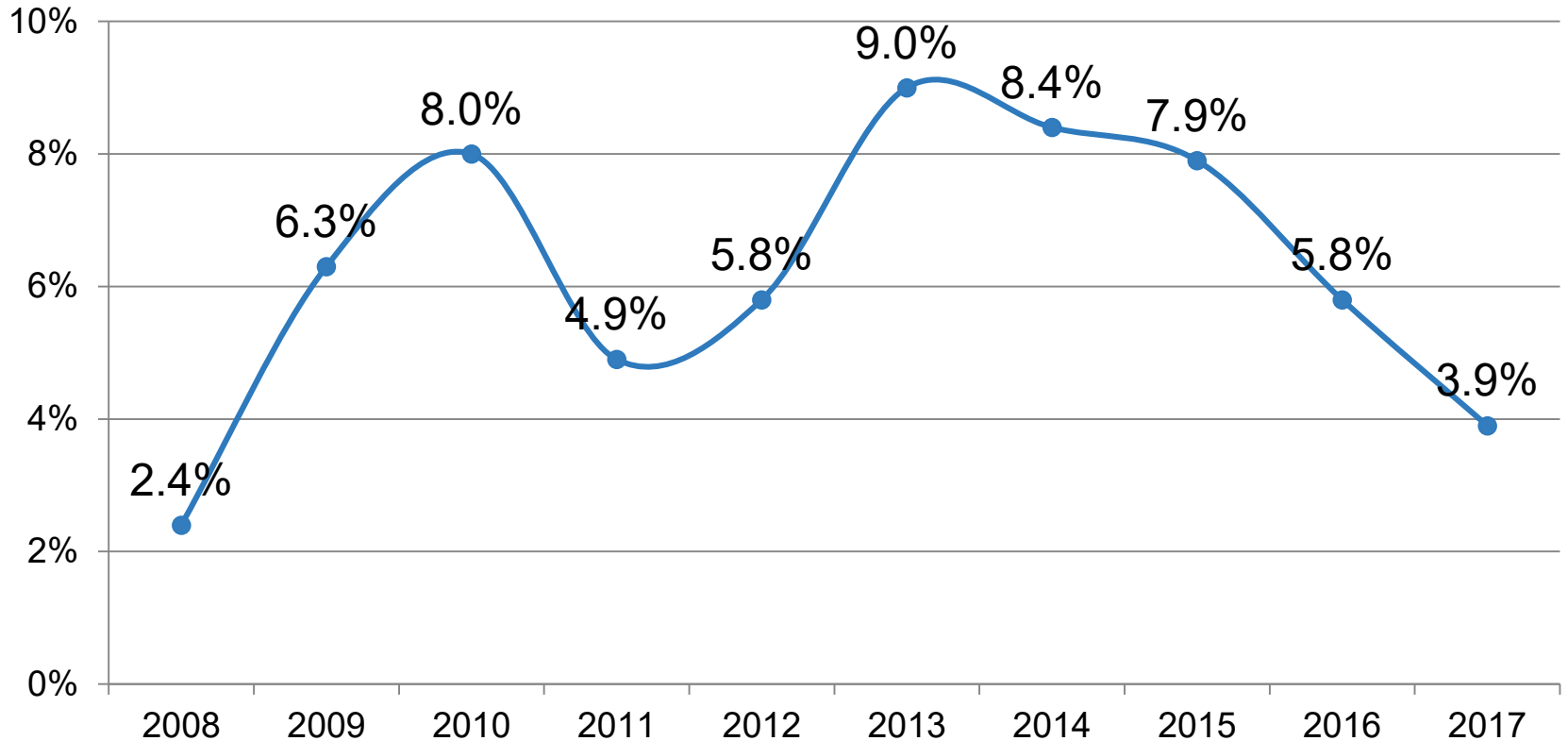


All Lines DWP Growth, U.S.



Source: NAIC data, sourced from S&P Global Market Intelligence, Insurance Information Institute.

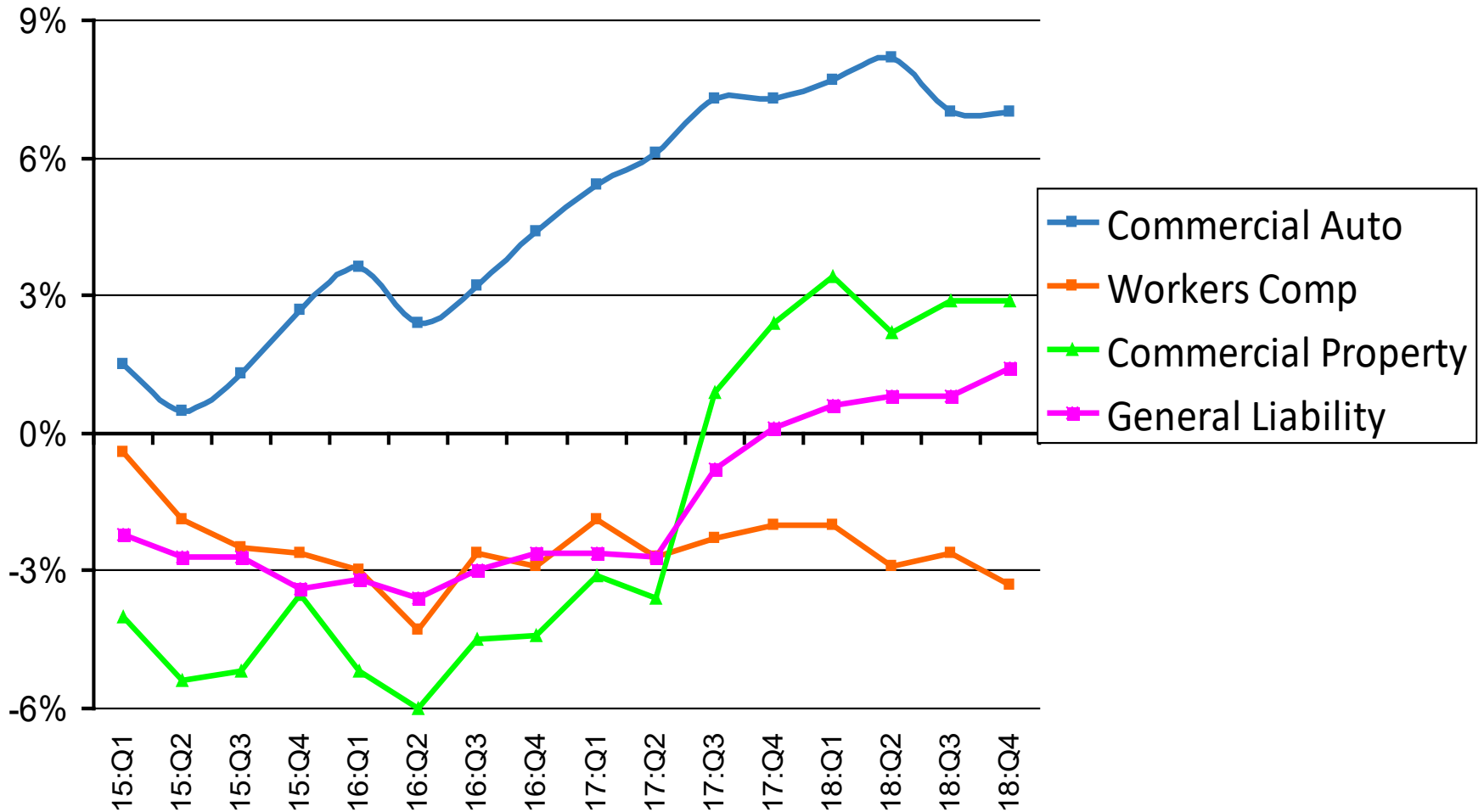
Return on Net Worth, All Lines, U.S.



Source: NAIC.

Commercial lines trends

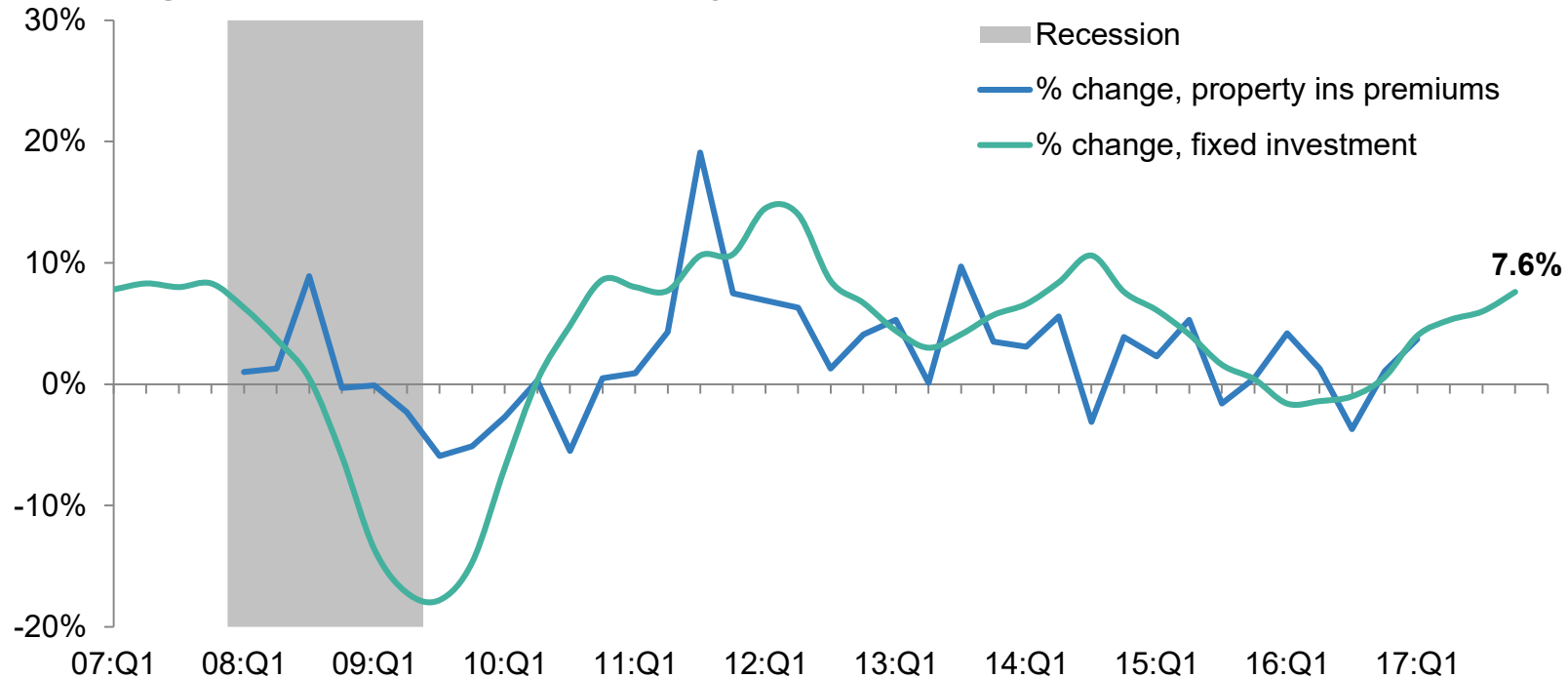
Rate Changes for 4 Major Lines of Business, Quarterly, 2015:Q1–2018:Q4



Sources: <https://www.ciab.com/download/13476/>; Insurance Information Institute.

Business investments predict premium growth

% change from same quarter, prior year



▼ **Econometric forecasts of business fixed investment anticipate growth of 4.5%–6.5% 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.**

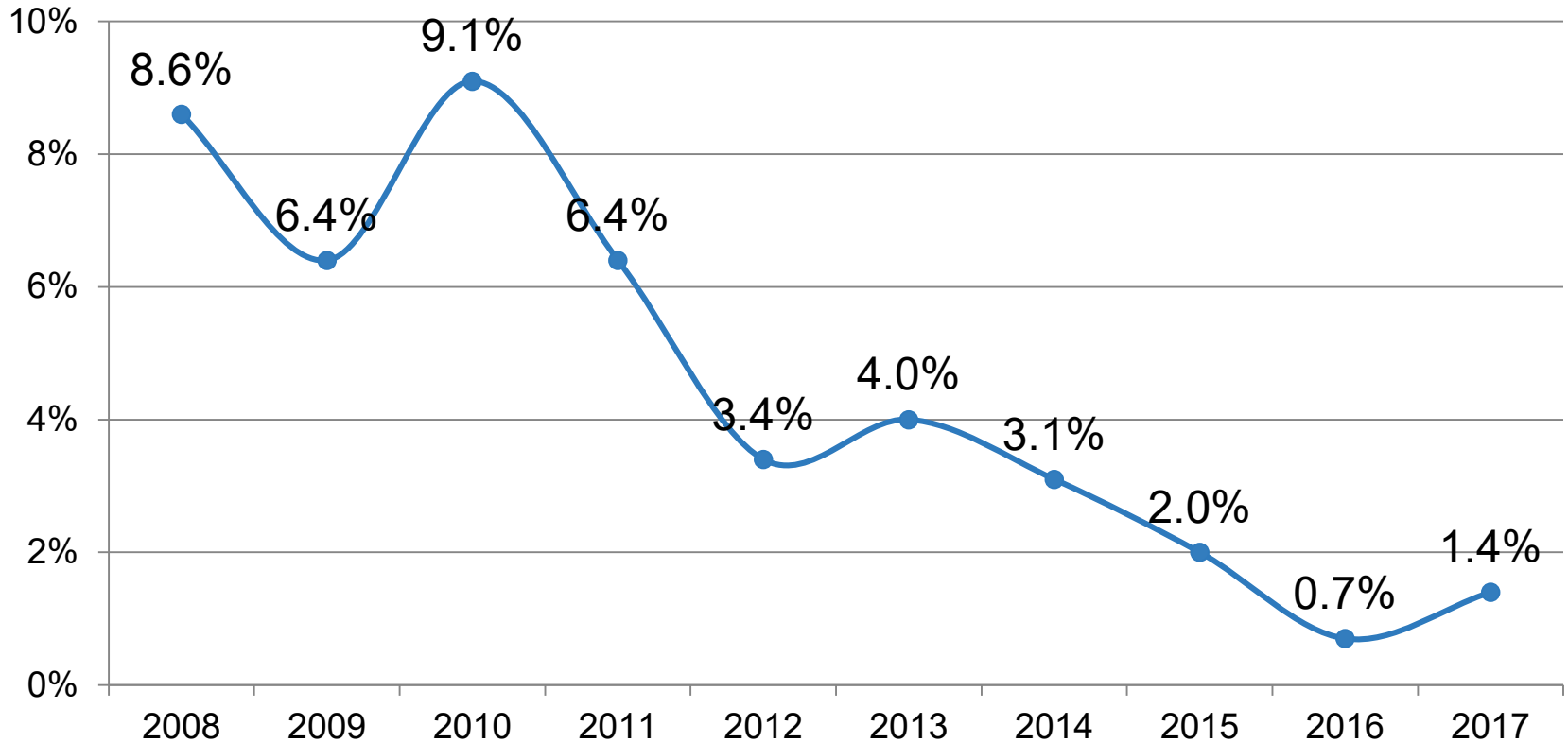
*Commercial property direct premiums written (fire, allied lines, CMP, inland marine, burglary and theft); business fixed investment (structures, equipment, and software).

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.

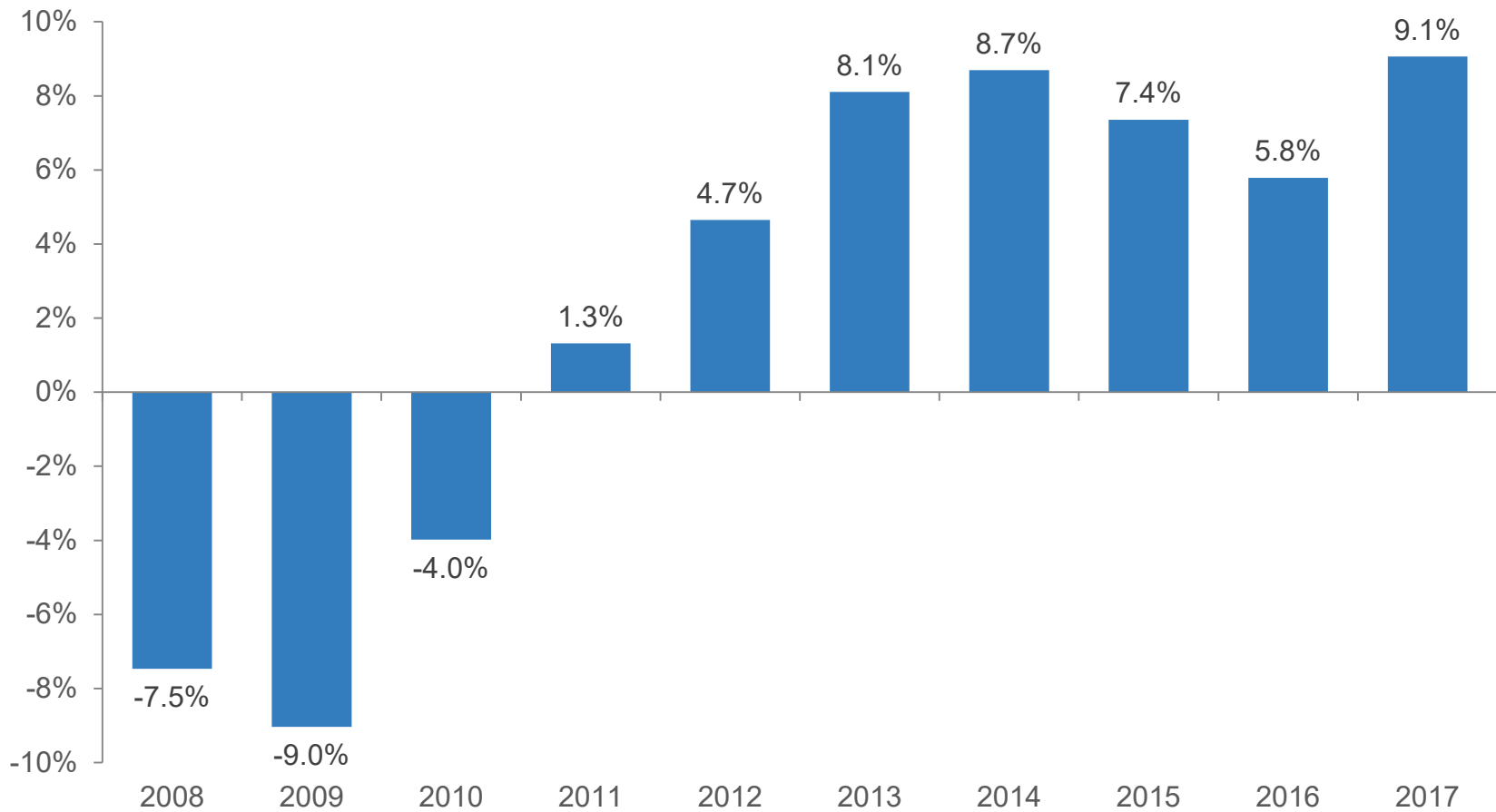


RNW Commercial Auto, U.S.



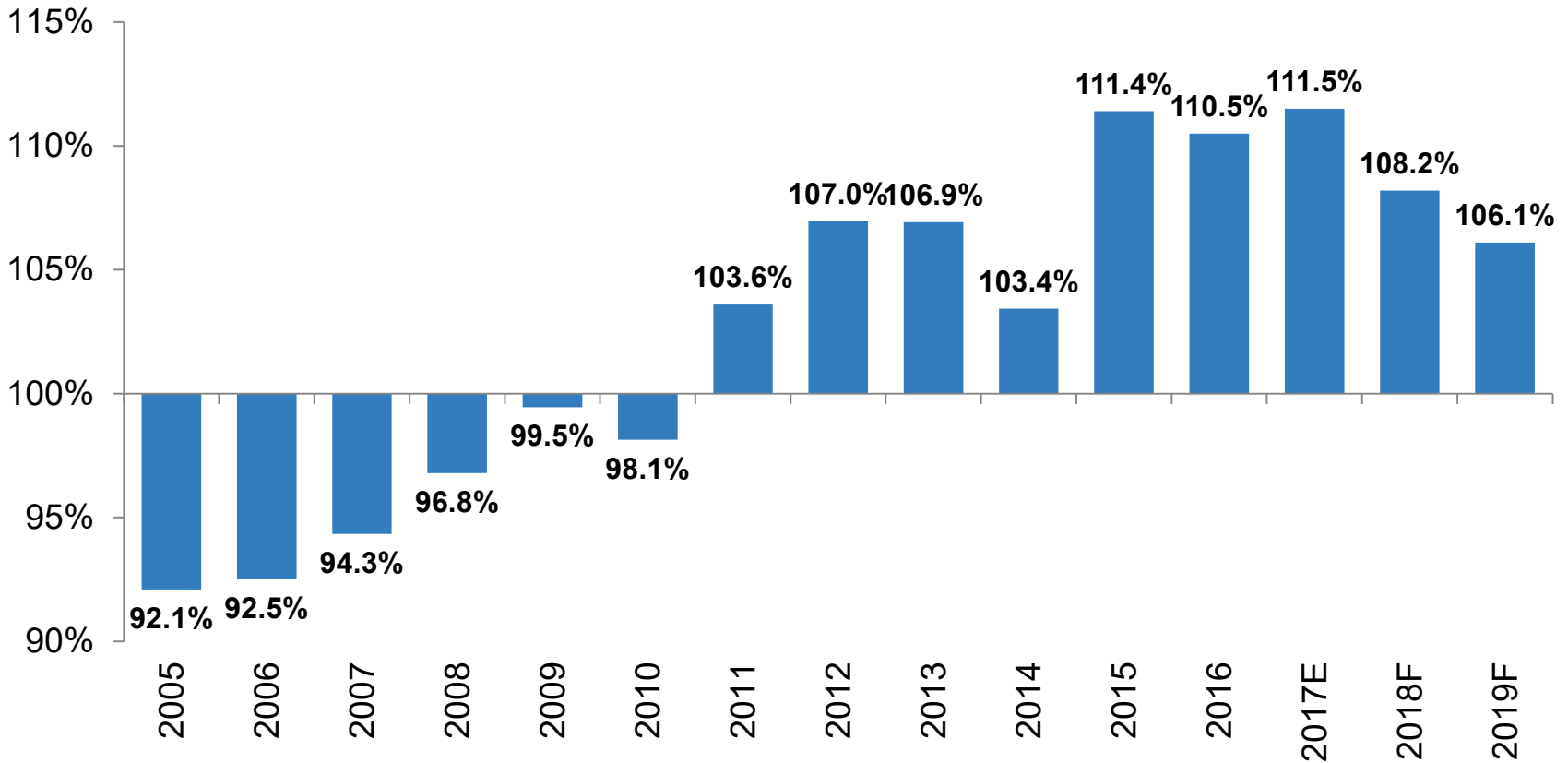
Source: NAIC.

Commercial Auto DWP Growth, U.S.



Source: NAIC data, sourced from S&P Global Market Intelligence, Insurance Information Institute.

Commercial Auto Net Combined Ratio, 2005-2019F



Just like Private Passenger Auto, Net Combined Ratios Have Been Rising Virtually Every Year for a Decade.

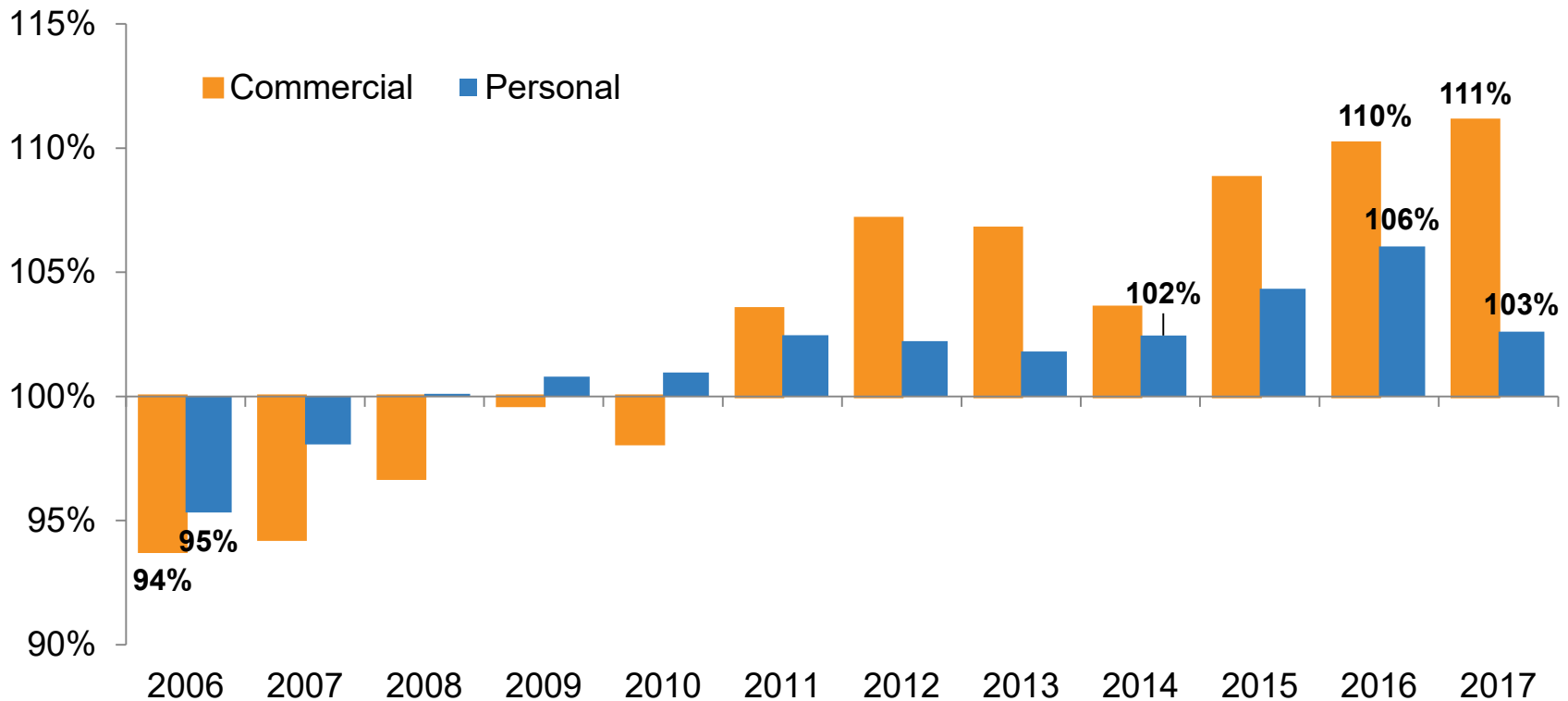


Source: National Association of Insurance Commissioners data, sourced from S&P Global Market Intelligence; Insurance Information Institute.

Auto Coverages

The Tide Has Turned.
But It Is Not Low Tide.

Auto Net Combined Ratio



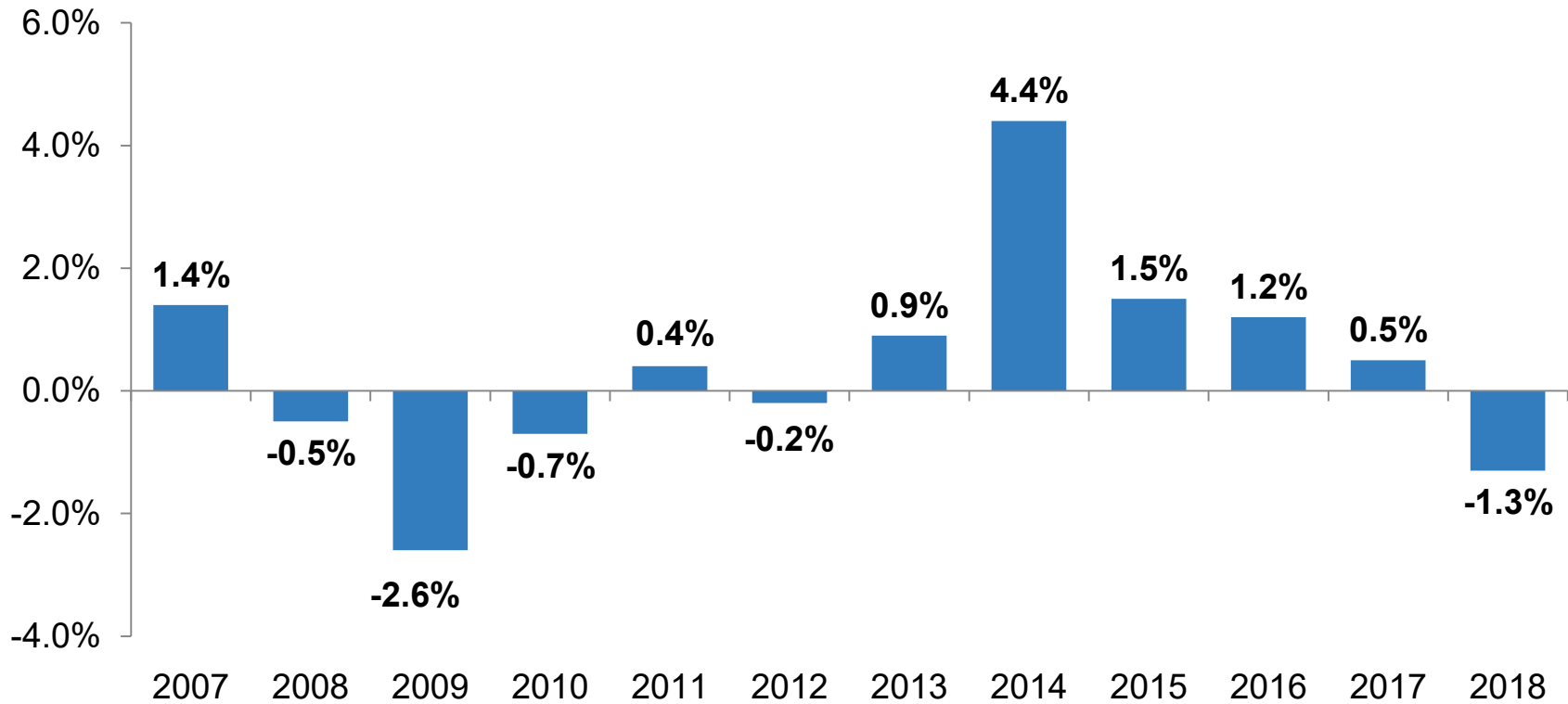
Rate Actions Helped Personal Auto Results. Not So for Commercial Auto.



Source: National Association of Insurance Commissioners data, sourced from S&P Global Market Intelligence; Insurance Information Institute.

Collision Claims Frequency

Annual % Change



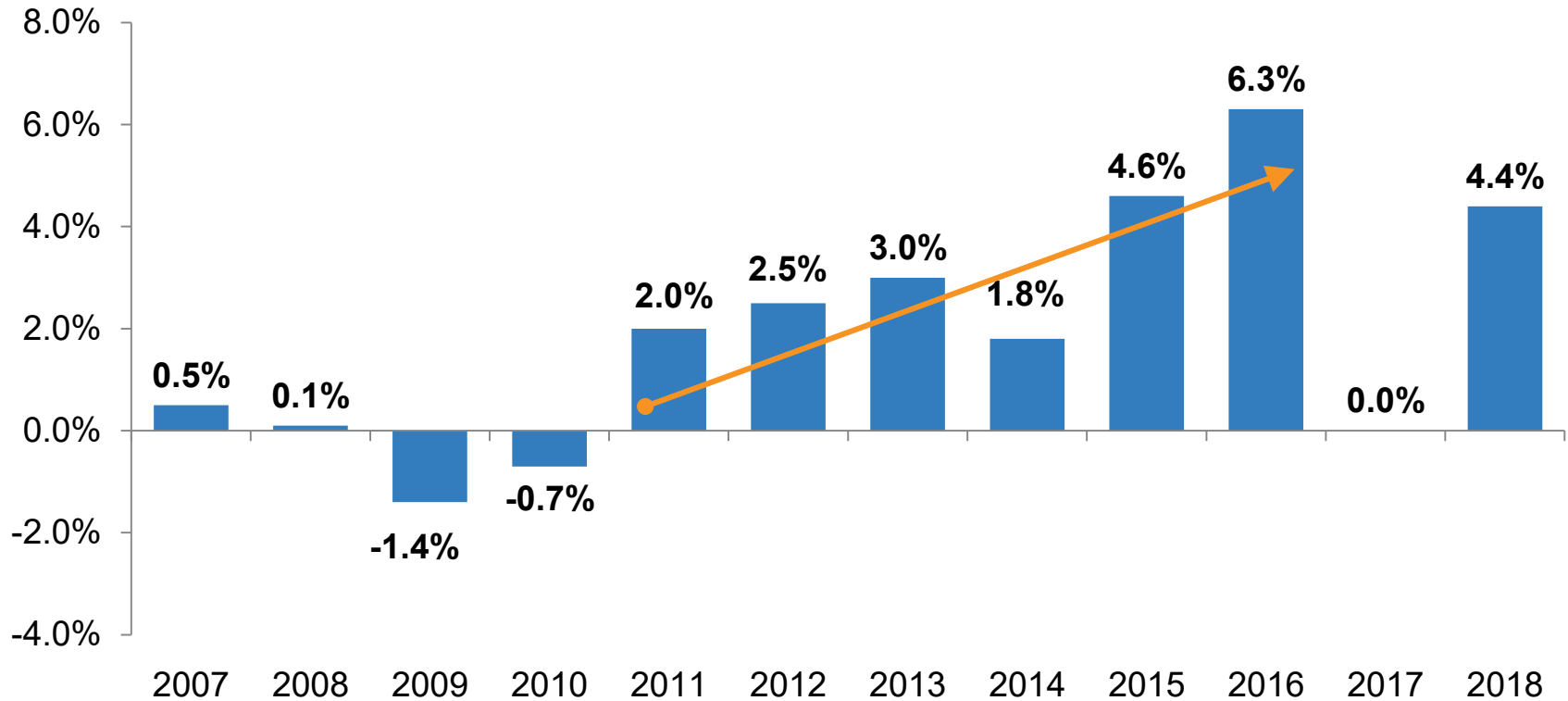
Claim Frequency Has Been Flat Since 2014. But It Normally Falls.



*Four Quarters Ending in September.
Source: Fast Track Monitoring System.

Collision Claims: Severity Trending Higher

Annual % Change



The Size of Claims Keeps Growing.



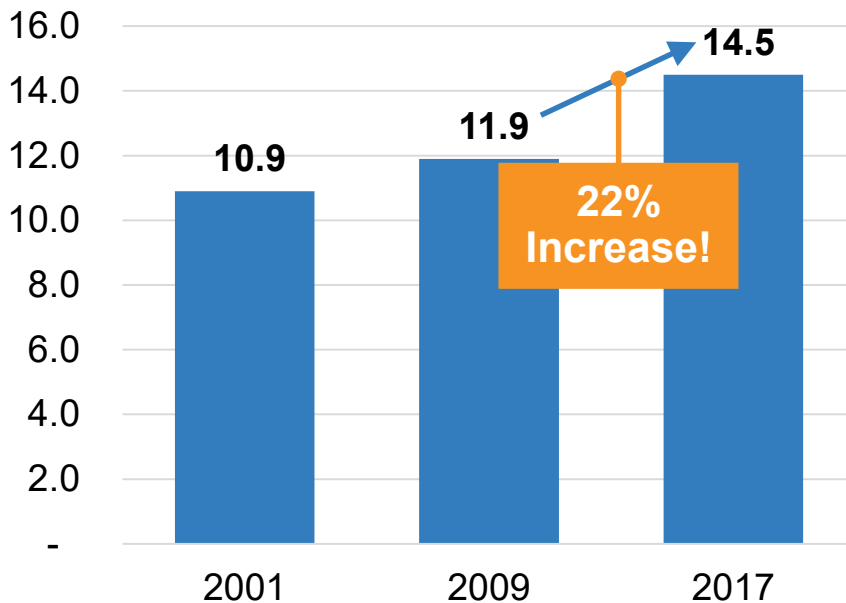
*Four Quarters Ending in September.
Source: Fast Track Monitoring System

Auto Repair: Complexity Grows

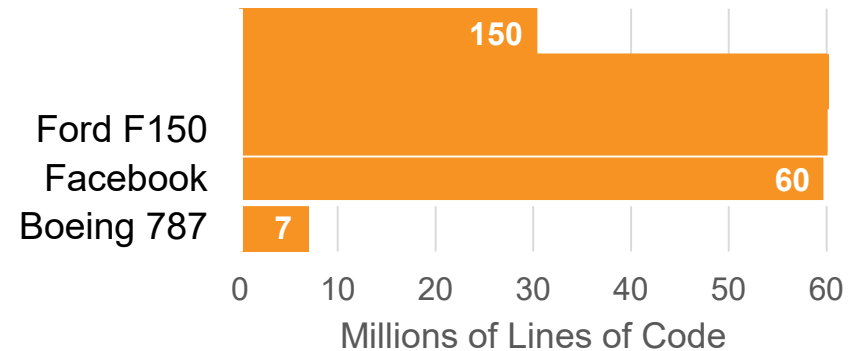
More Cool Stuff to Fix

More Parts, More Labor: Higher Costs

Parts/Collision Claim on Current Year Car



Electronics Add to Cost, Complexity



- ▶ Electronics: 40-50% of cost of vehicle
 - ◆ Pre-repair scan: \$63
 - ◆ Post-repair scan: \$93
 - ◆ Calibration labor: sublet at \$150
 - ◆ OEM: 98% of camera/sensors



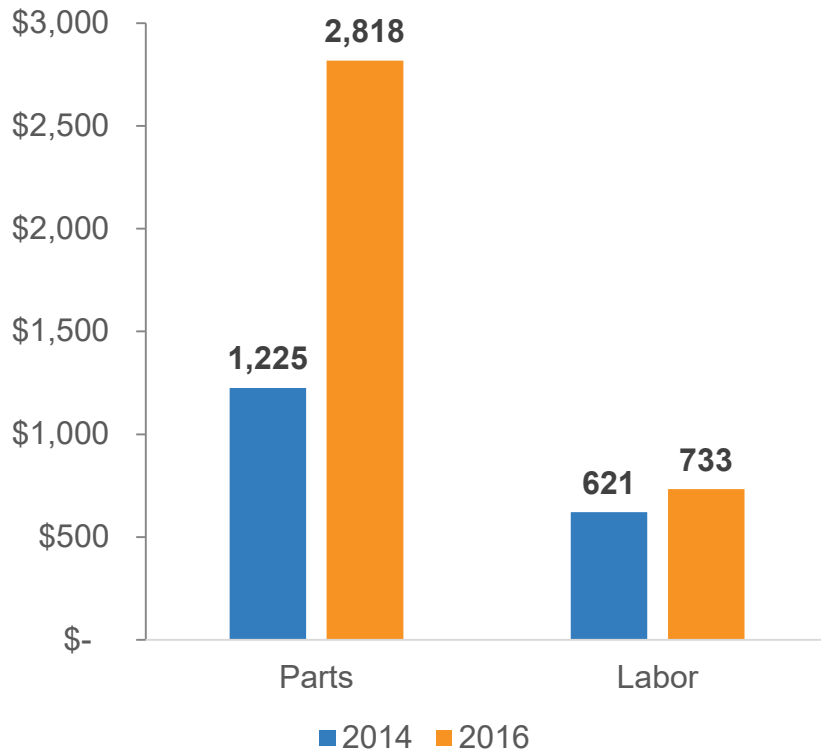
* Property Damage Only.

SOURCES: CCC Information Services; Ford Motor Co.;

Fixing a Bumper

... On an Entry-Level Luxury Car (~\$35K)

2014 Cost vs. 2016 Cost



What Has Changed?

	2014	2016
Grille: Distance Sensor	\$0	\$2,818
Headlamp Assembly	394	918
Mechanical Labor	0	108

Fewer Accidents, Higher Costs

- ▲ Parts: 130% Higher
- ▲ Labor: 18% Higher
- ▲ Total cost: \$1,705 higher

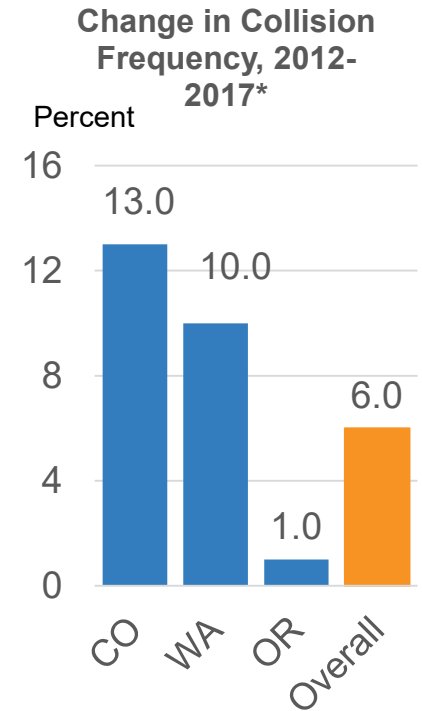
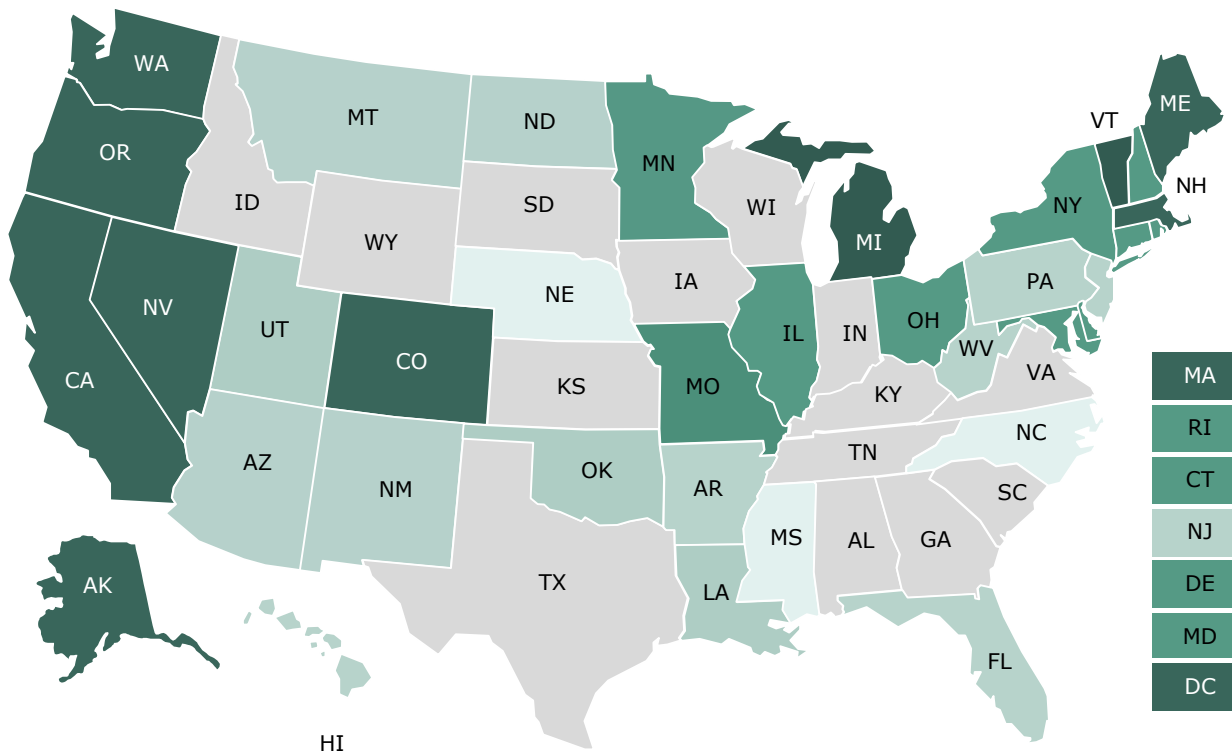


2016 vehicle has LED headlights and adaptive cruise control.
SOURCE: Liberty Mutual Insurance.

Weed Spreads Like Wildfire. Insurers Caught in the Middle

Current marijuana laws by state

■ Fully legal
 ■ Medical use legal and recreational use decriminalized
 ■ Medical use legal
 ■ Recreational use decriminalized
 ■ Fully illegal



* Vs. Neighboring States.

Sources: – Map - National Journal; Ballotpedia, 2019

Collision Frequency – IIHS, LEGAL POT: Crashes are up in states with retail sales, October 18, 2018



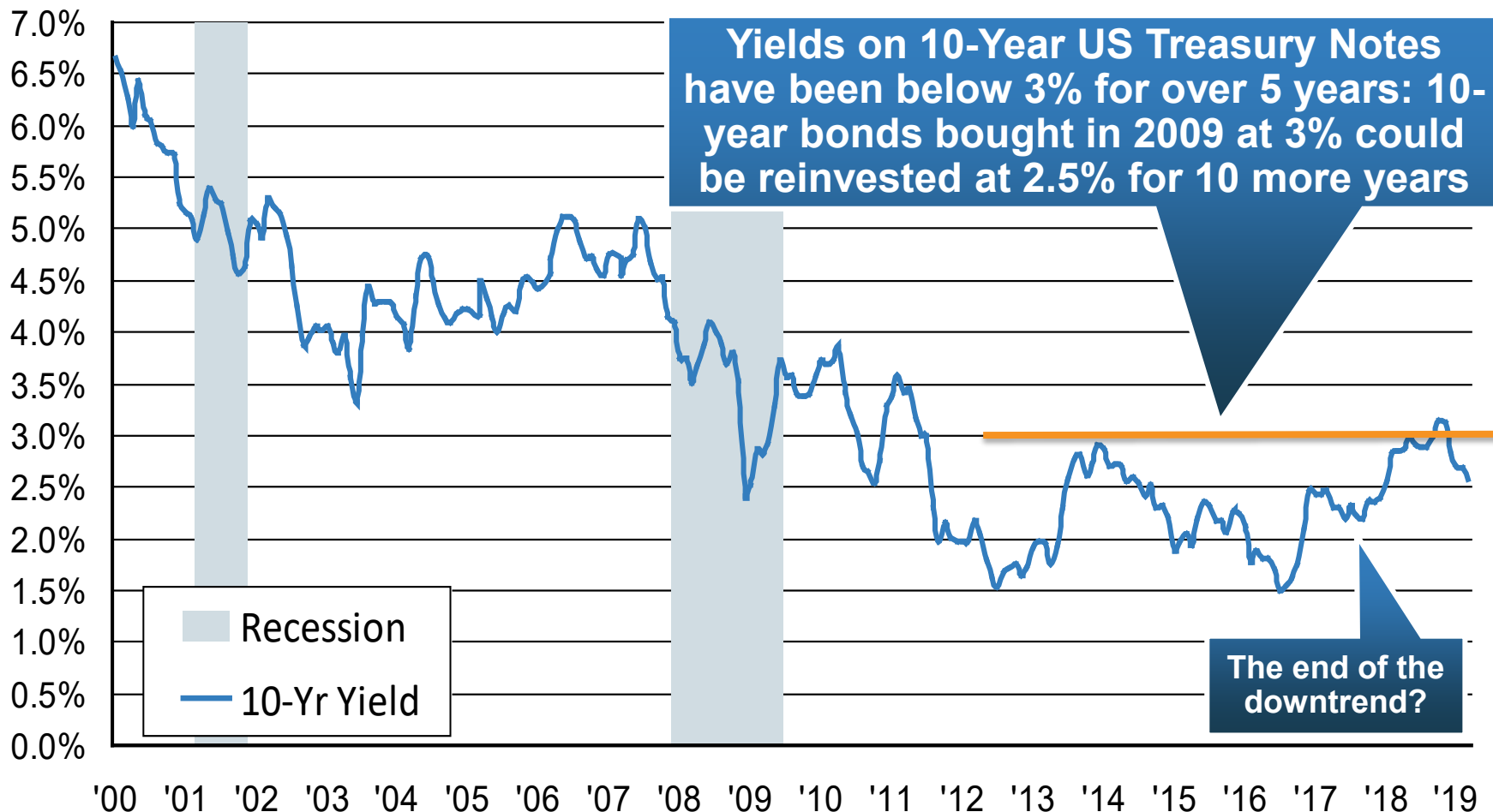
The Investment Story: Low Interest Rates, Past and Future

**Investment Performance is
a Key Driver of Profitability**

*Depressed Yields Will Necessarily
Influence Underwriting & Pricing*



US Treasury Note 10-Year Yields: A Long Downward Trend, 2000–2019*



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.

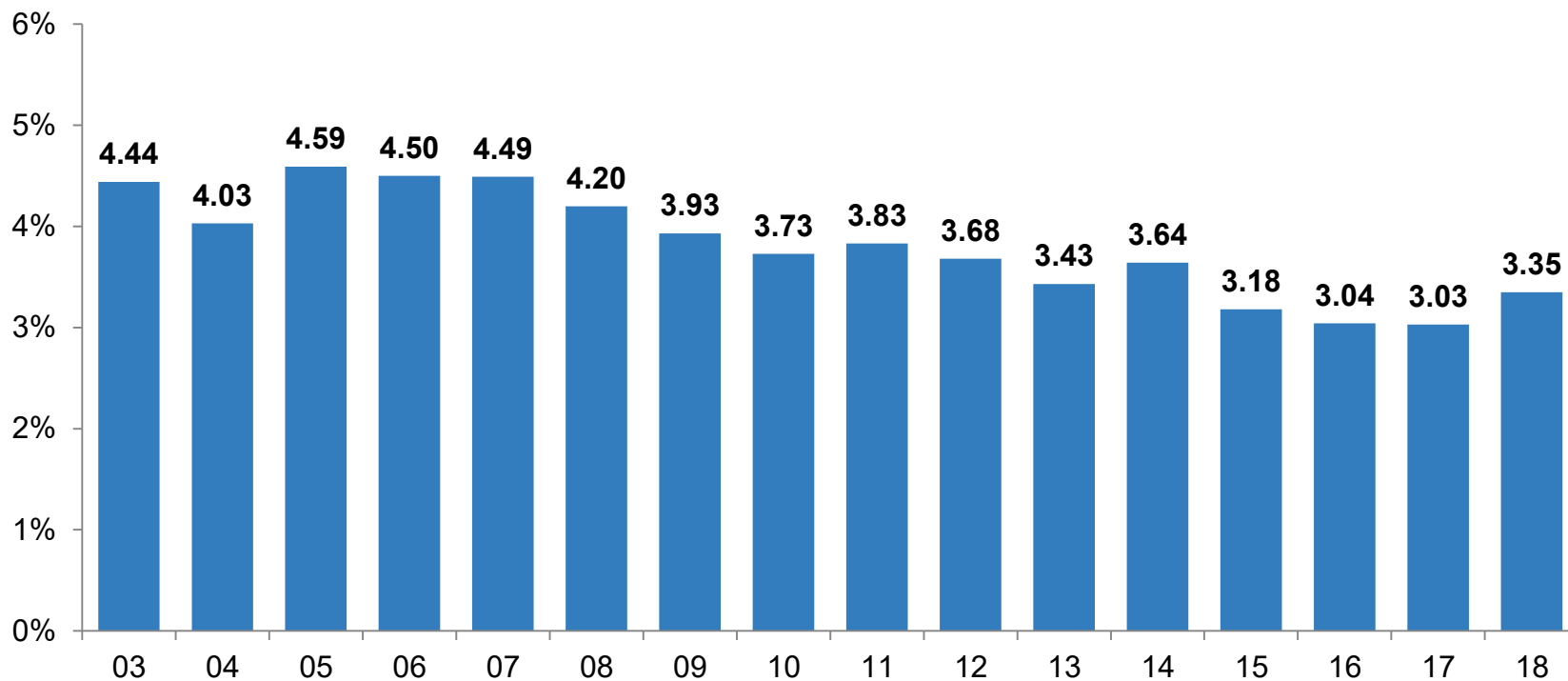
*Monthly, constant maturity, nominal rates, through March 2019.



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

P/C Insurer Portfolio Yields, 2002-2016

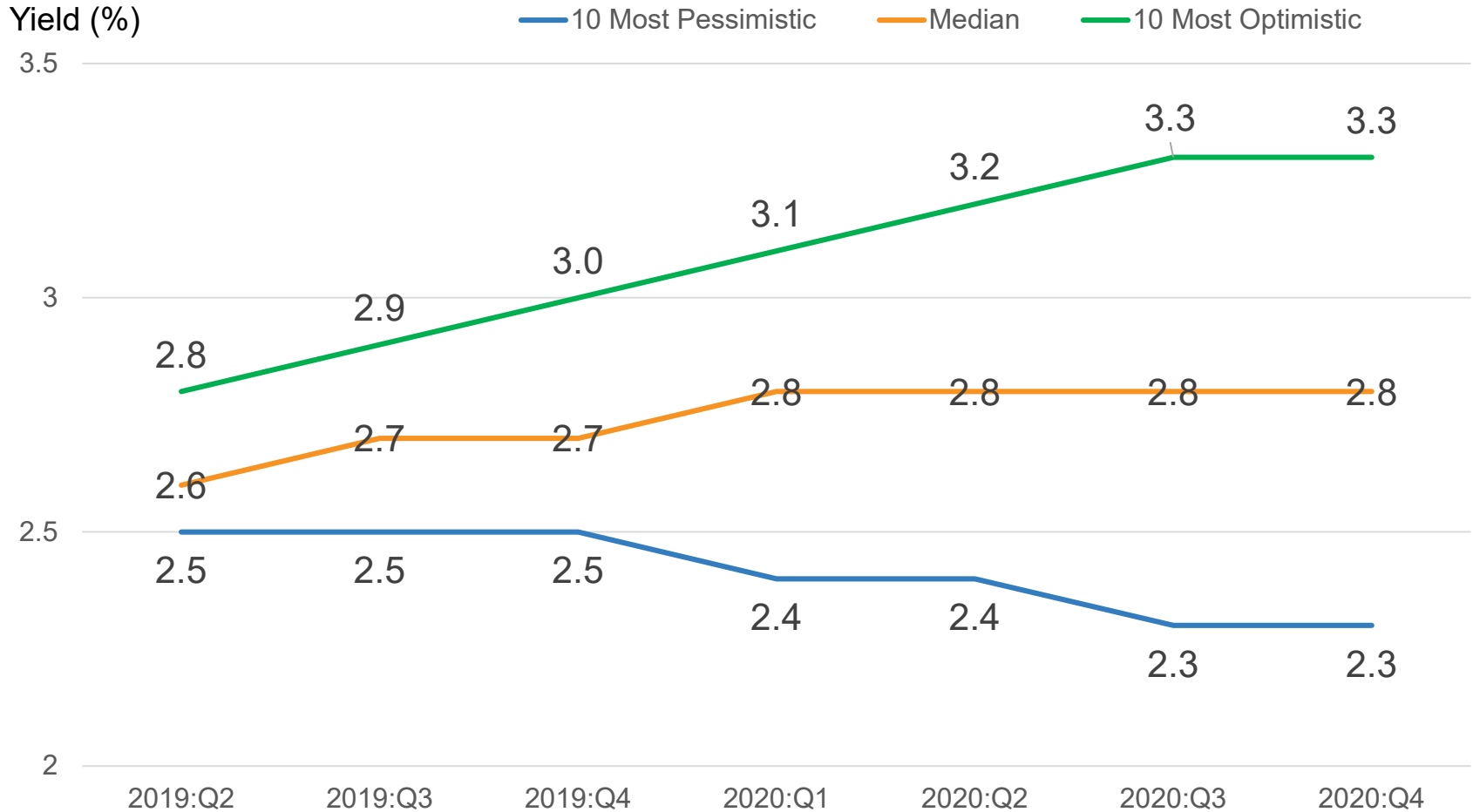
P/C Carrier Yields Have Been Falling for Over a Decade, Reflecting the Long Downtrend in Prevailing Interest Rates.



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.



April 2019: Quarterly Yield Forecasts for 10-Year US Treasury Bonds in 2019-20



The forecasts in the Blue Chip survey don't even see a common direction for the yield of 10-year T-bonds in 2019-20.



Questions?

Insurance Information Institute

www.iii.org

*Thank you for your time
and your attention!*

