Future Shock: What’s Ahead for the US Economy and the Insurance Industry

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Insurance Information Institute
THE ECONOMY

How Will “Trumponomics” Impact the Insurance Industry and the Overall Economy?
Trumponomics: The Essential Elements

- 5 Elements
  - Healthcare
  - Fair Trade
  - Deregulation
  - Tax Reform
  - Infrastructure Investment
  - Immigration Reform/Enforcement

- Most of these have direct impacts for insurers
Awakening America’s “Animal Spirits”

Economic Policy and the Insurance Industry

The Strength of the Economy Will Greatly Influence Insurer Exposure Base Across Most
US Real GDP Growth*

The Q4:2008 decline was the steepest since the Q1:1982 drop of 6.8%

Recession began in Dec, 2007

2017/18 GDP forecasts were revised upwards by ~0.2% following Trump election. Tax reform could add 0.1% - 0.2% to real GDP growth in 2018

Demand for Insurance Should Increase in 2017-18 as GDP Growth Continues at a Steady, Albeit Moderate Pace and Gradually Benefits the Economy Broadly

* Estimates/Forecasts from Blue Chip Economic Indicators.
Source: US Department of Commerce, Blue Economic Indicators 10/17; Insurance Information Institute.
The Economy Drives P/C Insurance


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.

Average 2007–2016
U.S.: 2.1%
SC: 2.7%

Source: NAIC data, sourced from S&P Global Market Intelligence, Insurance Information Institute.
Animal Spirits: Unleashed from the Oval Office?

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Great optimism in America – and the results will be even better!

Optimism Among U.S. CEOs Shows Biggest Increase...
Optimism among chief executive officers of some of the largest U.S. companies jumped in the first quarter by the most since the economy was emerging from the last ...
bloomberg.com

Donald J. Trump • @realDonaldTrump • 6h
JOBS, JOBS, JOBS!

Source: https://twitter.com/realDonaldTrump

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 business investment.

Source: The Conference Board; Wells Fargo Research.

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Source: The Conference Board; Wells Fargo Research.
The NFIB’s Index of Small Business Optimism remains near recent highs, but slipped in June as hopes for significant regulatory and tax reform fade.

Outlook: Small businesses are much more optimistic about the future.

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

New auto/light truck sales fell to the lowest level since the late 1960s. Forecast for 2014-15 is still below 1999-2007 average of 17 million units, but a robust recovery is well underway.

Job growth and improved credit market conditions boosted auto sales to near record levels in recent years.

Sales have returned to pre-crisis levels.

Truck, SUV purchases remain strong but have slumped a bit.

Manufacturing: ISM New Orders Index
Jan. 1990 – Oct. 2017 (>50 implies expansion)

Manufacturing activity remains near its cyclical high

Source: Institute for Supply Management (ISM); Wells Fargo Securities.
New Private Housing Starts, 1990-2023F

(Millions of Units)

New home starts plunged 72% from 2005-2009; A net annual decline of 1.49 million units, lowest since records began in 1959.

Job growth, low inventories of existing homes, still-low mortgage rates and demographics should continue to stimulate new home construction for several more years.

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

Private (but not public) construction spending remains relatively strong. Public construction spending could benefit from a boost in infrastructure investment.
New Home Sales: By Region  
Jan. 1989 – July 2017 (thousands, annual rate)

Source: US Dept. of Commerce; Wells Fargo Securities.
US Unemployment Rate Forecast

2007:Q1 to 2018:Q4F*

- Rising unemployment eroded payrolls and WC’s exposure base.
- Unemployment peaked at 10% in late 2009.

- Unemployment forecasts have been revised modestly downwards. Optimistic scenarios put the unemployment as low as 4.2% by Q4 2017 and 3.8% by Q4 2018.

* = actual;         = forecasts

Sources: US Bureau of Labor Statistics; Blue Chip Economic Indicators (10/17 edition); Insurance Information Institute.

The number of “discouraged workers” continues to fall, from nearly 18% in 2010 to 7.9% in Oct. 2017.


More workers now believe jobs are plentiful than scarce

Source: The Conference Board; Wells Fargo Research.
Hourly earnings fell in October, but should soon begin to respond to tightening labor market conditions.
**Annual Inflation Rates, (CPI-U, %), 1990–2018F**

<table>
<thead>
<tr>
<th>Year</th>
<th>Inflation Rates (%)</th>
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<tbody>
<tr>
<td>90</td>
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</tr>
<tr>
<td>91</td>
<td>5.1</td>
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<td>1.9</td>
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<td>18F</td>
<td>2.1</td>
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Inflation peaked at 5.6% in August 2008 on high energy and commodity crisis. The recession and the collapse of the commodity bubble reduced inflationary pressures in 2009/10.

Inflationary expectations are up on expectations of stronger economic growth, deficit spending.

Slack in the U.S. economy and falling energy prices suggests that inflationary pressures should remain subdued for an extended period of times.

Sources: US Bureau of Labor Statistics; Blue Chip Economic Indicators, 10/17 (forecasts).
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?


Yields on 10-Year U.S. Treasury Notes have been essentially below 5% for more than a decade.

Late 2016 “Trump Bump” in the aftermath of the 2016 election—shrank in 2017

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 August 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.

Sources: NAIC data, sourced from S&P Global Market Intelligence; Insurance Information Institute.
P/C Insurer Investment Yields: Lowest in Half a Century

Average yields in 2016 dropped to 3.1%, their lowest level since the mid-1960s.
Insurers Are Major Investors, 2016*

Total invested assets: $6.1 trillion*

22% of corporate bonds outstanding
15% of municipal bonds outstanding

*Includes affiliated and unaffiliated investments. All segments of the insurance industry.
Sources: NAIC (the Center for Insurance Policy and Research, August 24, 2017) via SNL Financial; I.I.I.
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.

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

*2017 estimate based on annualized $23.4B actual figure for 1st Half 2017.
A full normalization of interest rates is unlikely until the early/mid-2020s, more than a decade after the onset of the financial crisis.
Insured Catastrophe Losses

2017 Will Become One of the Costliest Years Ever for US Insurers

*Hurricanes Harvey and Irma Exact a Big Toll*

2017 is likely to become the second most costly year ever for insured CAT losses, behind only 2005. Maria losses in PR could push this figure beyond $75B.

*Includes PCS H1 insured losses of $17.7B, estimated Hurricane Harvey and Irma insured losses of $20B and $18B, respectively. Stated in 2017 dollars. Excludes NFIP losses.

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/ISO; Insurance Information Institute.
Inflation Adjusted U.S. Catastrophe Losses by Cause of Loss, 1997–2016

1. Catastrophes are defined as events causing direct insured losses to property of $25 million or more in 2016 dollars.
2. Excludes snow.
3. Does not include NFIP flood losses
4. Includes wildland fires
5. Includes civil disorders, water damage, utility disruptions and non-property losses such as those covered by workers compensation.

Source: ISO’s Property Claim Services Unit.
Top 18 Most Costly Disasters in U.S. History—Katrina Still Ranks #1

(Insured Losses, 2017 Dollars, $ Billions)*

Harvey, Irma and Maria combined caused an estimated $60B+ in privately insured losses in the US

15 of the 18 Most Expensive Insurance Events in US History Have Occurred Since 2004—3 of those in 2017

*Adjusted to June 2017 values.
Sources: PCS, RMS, Karen Clark & Co; USC Center for Risk and Uncertainty Management adjustments to 2017 dollars using the CPI.
NFIP Policies in Force, 1979 – 2017*

Before Harvey and Irma, the NFIP was already $24.9B in debt. Harvey NFIP claims are expected total $7-$10B with Irma adding to this total. NFIP will need to borrow, likely pushing its debt load well above $35B

(Policies in Force)

NFIP policies-in-force are down by nearly 750,000—or 13.2%—from 5.70 million in 2009 to 4.95 million as of mid-2017

*As of June 30, 2017
Sources: NFIP/FEMA accessed 9/18/17 at: [https://www.fema.gov/total-policies-force-calendar-year](https://www.fema.gov/total-policies-force-calendar-year); USC Risk and Uncertainty Management Center.
Few Houston-area residents had flood insurance.

Penetration rates are relatively high in coastal SC.

FL residents were much better prepared.
Health Insurance Markets

Decades-Old Problem in Search of an Economically and Politically Viable Solution

Adverse Selection Death Spiral?
Health care expenditures as a share of GDP rose from 5.8% in 1965 to 18.0% in 2013 and are expected to reach 19.9% of GDP by 2022. Since 2009, health expenditures as a % of GDP have flattened out at about 18%--the question is why and will it last?

### Example of Health Insurance Exchange Monthly Premiums in SC from HealthCare.gov

#### 25-Year Old Single Adult, No Tobacco Use

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**Average Silver Plan monthly premium in 2018 for 25-yr. old single adult will rise by 33.7%, to $446.15 from $333.67.**

#### 60-Year Old Single Adult, No Tobacco Use

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<td>$835.49</td>
<td>$879.57</td>
<td>$856.29</td>
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**Silver Plan for a 60-yr. old single adult will rise by 33.7%, to $1,206.03 from $901.97.**

*NOTE: All plans are offered through BC/BS of SC, the only exchange insurer in SC. Source: SC DOI: [http://doi.sc.gov/DocumentCenter/View/10319](http://doi.sc.gov/DocumentCenter/View/10319) accessed 9/26/17.*
Number of ACA Exchange Insurers by County for 2018

- 63 counties projected to have 0 carriers (2.01%)
- 1,472 counties projected to have 1 carrier (46.86%)
- 70,356 Exchange participants projected without coverage (0.78%)
- 2,643,431 Exchange participants projected without choices (28.73%)

Claim Trends in SC Private Passenger Auto Insurance

Rising Frequencies and Severities in Many Coverages

Will that Pattern Be Sustained?
SC Coverage: Collision Severity Is Sharply Higher in Recent Years*

Improving Economy, Distracted Driving, DUI Are Just a Few of the Numerous Factors Pushing Collision Claim Severity Higher

*2017 data are for the 4 quarters ending March 31, 2017.
Source: ISO/PCI Fast Track data; Insurance Information Institute
**SC Coverage: BI Severity & Frequency Trends Are Both Higher in Recent Years**

**Annual Change, 2013 through 2017**

<table>
<thead>
<tr>
<th>Year</th>
<th>Severity</th>
<th>Frequency</th>
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</thead>
<tbody>
<tr>
<td>2013</td>
<td>3.9%</td>
<td>0.9%</td>
</tr>
<tr>
<td>2014</td>
<td>2.5%</td>
<td>-1.8%</td>
</tr>
<tr>
<td>2015</td>
<td>8.3%</td>
<td>3.6%</td>
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<tr>
<td>2016</td>
<td>2.9%</td>
<td>6.9%</td>
</tr>
<tr>
<td>2017*</td>
<td>5.1%</td>
<td>7.7%</td>
</tr>
</tbody>
</table>

*Improving Economy, Distracted Driving, DUI Are Just a Few of the Numerous Factors Pushing Bodily Injury Claim Frequency and Severity Higher*

*2017 data are for the 4 quarters ending March 31, 2017.
Source: ISO/PCI Fast Track data; Insurance Information Institute
USC’s Inaugural RMI Newsletter
(http://us16.campaign-archive1.com/?u=de4d9fc579ae40ab21b8a5d36&id=28137b2148)

RISK and Uncertainty Management Center
Darla Moore School of Business | University of South Carolina

August 25, 2017

Introducing the RMI Newsletter
Darla Moore School of Business, University of South Carolina

A quarterly glimpse of recent happenings for the Risk and Uncertainty Management Center, Gamma Iota Sigma members, Risk Management and Insurance (RMI) Majors, Minors, and Alumni.

RMI-DAY | Oct 25
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Gamma Iota Sigma

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Contact us to learn more about the Risk and Uncertainty Management Center and get your business involved!

Benefits include access to the latest research in risk management and opportunities to engage with and hire top talent in risk management and insurance.

THE WALL STREET JOURNAL.

Check out the June 25th article from the front page of the Wall Street Journal featuring RMI professor, Robert Hartwig.

Insurance Is a Fun Career! Just Consider the Zombies and Bacon

Insurers use extreme measures to lure new hires, from ghoulish videos to free beer. Allstate’s ‘happiness guru’

Since joining the USC faculty last year, RMI Professor Robert Hartwig has been interviewed by local, state and national media more than 100 times on a wide variety of issues, earning the Moore School and USC mentions in publications, on television and radio across the country. Recent
Thank you for your time and your attention!

Twitter: twitter.com/bob_hartwig

For a copy of this presentation, email me at robert.hartwig@moore.sc.edu