Property/Casualty Insurance Results: First-Quarter 2019

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Private U.S. property/casualty insurers' net income after taxes rose to $17.9 billion in first-quarter 2019 from $17.1 billion in first-quarter 2018. Insurers' overall profitability as measured by their annualized rate of return on average policyholders' surplus rose to 9.4 percent from 9.1 percent a year earlier, according to ISO, a Verisk (Nasdaq:VRSK) business, and the American Property Casualty Insurance Association (APCIA).[1]

Insurers' combined ratio[2] deteriorated to 95.6 percent for first-quarter 2019 from 94.6 percent for first-quarter 2018, while net underwriting gains[3] increased to $5.3 billion from $4.1 billion a year earlier. Net written premium dropped 1.2 percent in first-quarter 2019 from the unusually high value for first-quarter 2018.

Insurers' net investment income in first-quarter 2019 increased to $13.2 billion from $11.8 billion in first-quarter 2018, while insurers' realized capital gains fell to $1.6 billion from $3.6 billion, resulting in $14.7 billion in net investment gains[4] for first-quarter 2019, a $0.6 billion decrease from $15.3 billion for first-quarter 2018.

> Similar to first-quarter 2018, the industry reported underwriting gains and a combined ratio close to 95 percent.

Insurers' annualized rate of return on average surplus increased from 9.1 percent in first-quarter 2018 to 9.4 percent in first-quarter 2019—the best first-quarter result since 10.8 percent in 2015, and 1.8 percentage points above the 7.6 percent average annualized quarterly rate of return for 1989 to 2018.

The industry's surplus[5] as of March 31, 2019, was $779.5 billion, up $37.4 billion from $742.2 billion as of December 31, 2018.

Underwriting Results

In the first quarter of 2019, earned premiums grew 4.6 percent to $149.6 billion, while LLAE rose 5.9 percent to $101.8 billion, other underwriting expenses fell 0.4 percent to $41.8 billion, and policyholders' dividends remained essentially unchanged at $0.8 billion. As a result, the industry reported a $5.3 billion net underwriting gain, a 27.0 percent increase from the $4.1 billion for first-quarter 2018.

Net written premiums fell $1.8 billion to $154.8 billion in first-quarter 2019 from $156.6 billion in first-quarter 2018, a 1.2 percent decline after a 15.7 percent increase in first-quarter 2018. Written premium had not decreased since the series of declines associated with the Great Recession, and the last of those declines was in first-quarter 2010. Net earned premium growth slowed to 4.6 percent in first-quarter 2019 from 9.4 percent in first-quarter 2018.

The main reason for the reported decline in net written premiums is the unusually high comparison base. In 2018, many insurers chose to significantly reduce the portion of premiums ceded to their non-U.S. affiliates, with the reinsurance changes typically effective January 1, 2018. As a result, first-quarter 2018 premium growth was a compound effect of several developments, with the main drivers being organic growth in underlying direct

1. This study defines the U.S. property/casualty insurance industry as all private property/casualty insurers domiciled in the United States, including excess and surplus insurers and domestic insurers owned by foreign parents but excluding state funds for workers' compensation and other residual market carriers. The figures are consolidated estimates based on reports accounting for at least 96 percent of all business written by U.S. property/casualty insurers. All figures are net of reinsurance unless otherwise noted and occasionally may not balance due to rounding.
2. Combined ratio, defined as the sum of loss ratio, expense ratio, and dividend ratio, is a key measure of losses and other underwriting expenses per dollar of premium. The loss ratio is the ratio of losses and loss adjustment expenses (LLAE) to earned premiums; the expense ratio is the ratio of other underwriting expenses to written premiums; and the dividend ratio is the ratio of policyholders' dividends to earned premiums.
3. Underwriting gains (or losses) equal earned premiums minus LLAE, other underwriting expenses, and dividends to policyholders.
4. Net investment gains equal the sum of net investment income and realized capital gains (or losses) on investments.
5. Policyholders' surplus is insurers' net worth measured according to Statutory Accounting Principles.

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written premiums, multiple insurers ceding less premiums to their non-U.S. affiliates in 2018, and in some cases, one-time increases in written premiums associated with the returns of previously ceded unearned premium reserves. Notably, the 2018 increases in earned premiums were less pronounced than the increases in written premiums, mostly due to the absence of one-time increases and partially due to the time it takes for increased written premiums to be earned.

With 2018 values unusually high, it is worth comparing 2019 premiums with the values for 2017. Average annual growth over the two-year period from first-quarter 2017 to first-quarter 2019 was 6.9 percent for net written premium and 7.0 percent for earned premium.

To assess the underlying direct premium growth, ISO had compiled premiums for a large cohort of insurers whose first-quarter data was available for 2017, 2018, and 2019, which represents more than 95 percent of the total net written premiums for the industry. Aggregated net written premiums for these insurers grew 15.2 percent in first-quarter 2018 and then dropped 1.3 percent in first-quarter 2019, while direct written premiums grew approximately 6.2 percent in first-quarter 2018 and then grew 4.3 percent in first-quarter 2019. The changes in direct written premiums are consistent with continued growth in the economy and relative stability in insurance markets.

The 5.9 percent increase in LLAE in first-quarter 2019 outpaces earned premium growth and compares with the 3.0 percent increase a year earlier. Private U.S. insurers' net LLAE from catastrophes in first-quarter 2019 declined to $4.8 billion for first-quarter 2019 from $5.0 billion a year earlier. Net LLAE for losses other than catastrophes rose $5.8 billion, or 6.4 percent, to $97.0 billion in first-quarter 2019 from $91.2 billion in first-quarter 2018.

Private U.S. insurers' net LLAE includes both their domestic and foreign catastrophic losses.[6] However, U.S. insurers' $4.8 billion in net LLAE from catastrophes in first-quarter 2019 is primarily attributable to catastrophes that struck the United States. Though estimating U.S. insurers' LLAE from catastrophes elsewhere around the globe is difficult, the available information suggests that U.S. insurers' net LLAE arising from such events was not large in either 2019 or 2018.

Net written premium declined compared with unusually high first-quarter 2018 levels, but direct written premiums continued to grow.

Reflecting the differences between premium growth and growth in LLAE and other costs of providing insurance, the combined ratio deteriorated by 1.0 percentage point to 95.6 percent in first-quarter 2019 from 94.6 percent in first-quarter 2018.

Underwriting results benefited from $4.5 billion in favorable development of LLAE reserves in first-quarter 2019, based on new information and updated estimates for the ultimate cost of claims from prior accident years. The $4.5 billion of favorable reserve development in first-quarter 2019 compares with $7.4 billion of favorable development in first-quarter 2018. Favorable development reduced the combined ratio by 3.0 percentage points in first-quarter 2019 and by 5.2 percentage points in first-quarter 2018.

Excluding development of LLAE reserves, net LLAE grew $2.7 billion, or 2.6 percent, to $106.3 billion in first-quarter 2019 from $103.6 billion in first-quarter 2018. Excluding both the LLAE from catastrophes and the development of LLAE reserves, net LLAE grew $2.8 billion, or 2.8 percent, to $101.9 billion in first-quarter 2019 from $99.1 billion a year earlier. The combined ratio deteriorated 1.0 percentage point in first-quarter 2019, but if catastrophe LLAE and LLAE reserve development in first-quarter 2019 had been at the same level as in first-quarter 2018, the combined ratio would have improved 1.0 percentage point.

The $5.3 billion in net underwriting gains in first-quarter 2019 amounted to 3.5 percent of the $149.6 billion in net premiums earned during the period. The $4.1 billion in net gains on underwriting in first-quarter 2018 amounted to 2.9 percent of the $143.1 billion in net premiums earned during that period.

While overall net written premium declined 1.2 percent in first-quarter 2019 after jumping 15.7 percent a year earlier, the dynamics varied significantly across industry segments.

Net written premium growth for insurers writing mostly personal lines slowed to 4.5 percent in first-quarter 2019 from 8.7 percent a year earlier. Excluding mortgage and financial guaranty insurers, net written premium for insurers writing predominantly commercial lines dropped 9.2 percent in first-quarter 2019 after jumping 32.0 percent in first-quarter 2018. The bulk of the changes in reinsurance utilization was concentrated in this segment. Premium growth for insurers writing more balanced books of business slowed to 2.5 percent in first-quarter 2019 from 4.9 percent in first-quarter 2018. Estimated direct premium growth was approximately 4.4 percent for insurers writing predominately personal lines, approximately 3.9 percent for insurers with balanced books of business, and approximately 4.7 percent for insurers writing mostly commercial lines, excluding mortgage and financial guaranty insurers. Direct premium growth was estimated using a consistent set of insurers representing about 95 percent of commercial insurers and close to 100 percent of remaining segments.

Excluding mortgage and financial guaranty insurers, commercial lines insurers' combined ratio deteriorated 2.7 percentage points to 96.6 percent in first-quarter 2019. Personal lines insurers' combined ratio deteriorated 0.6 percentage points to 94.8 percent, while balanced insurers' combined ratio improved 1.3 percentage points to 96.7 percent.

6. Net LLAE from catastrophes also includes revisions to LLAE from catastrophes that occurred during prior periods but excludes LLAE covered by the National Flood Insurance Program, residual market insurers, and foreign insurers and reinsurers.

Investment Results

Insurers' net investment income—primarily dividends from stocks and interest on bonds—was $13.2 billion in first quarter 2019, up 11.7 percent from $11.8 billion in first-quarter 2018. Insurers' realized capital gains on investments decreased to $1.6 billion in first-quarter 2019 from $3.6 billion a year earlier. Combining net investment income and realized capital gains, overall net investment gains declined 4.1 percent to $14.7 billion in first-quarter 2019 from $15.3 billion a year earlier.

Insurers' net investment income grew 11.7 percent to $13.2 billion, while average cash and invested assets for first-quarter 2019 grew 2.3 percent compared with first-quarter 2018. The annualized yield on insurers' investments in first-quarter 2019 increased to 3.1 percent from 2.9 percent for first-quarter 2018. Both yields were significantly below the 3.4 percent average annualized quarterly yield for the last ten years. From 1960 to 2018, insurers' annual investment yield averaged 5.0 percent but ranged from as low as 2.8 percent in 1961 to as high as 8.2 percent in 1984 and 1985. In recent years, investment yields have trended downward, and annual yields have not exceeded 4.0 percent since 4.2 percent for 2008. On a full-year basis, insurers' annual investment yield steadily declined from 4.6 percent for 2005 to 3.2 percent for both 2014 and 2015 and to 3.1 percent in 2017. In 2018, investment yield rose to 3.4 percent, but the bulk of the increase was due to one-time money transfers from noninsurance entities, rather than from sustainable increases in investment profitability.

Combining the $1.6 billion in realized capital gains in first-quarter 2019 with the $25.6 billion in unrealized capital gains[7] during the same period, insurers posted $27.1 billion in overall capital gains for first-quarter 2019, a $35.6 billion improvement from first-quarter 2018. Over the past 30 years, insurers' total capital gains have averaged $3.1 billion per quarter but have ranged from as high as $45.8 billion in fourth-quarter 2017 to as low as negative $44.9 billion in fourth-quarter 2018.

Unrealized capital gains in first-quarter 2019 drove the largest-ever quarterly surplus growth for the industry.

Pretax Operating Income

Pretax operating income[8] increased to $19.0 billion for first-quarter 2019 from $16.1 billion for first-quarter 2018. The $2.9 billion increase in operating income was the combined result of the $1.1 billion increase in net gains on underwriting, the $1.4 billion increase in net investment income, and the $0.4 billion increase in total other income.

Net Income after Taxes

Combining operating income, realized capital gains (losses), and federal and foreign income taxes, the insurance industry's net income after taxes rose $0.8 billion to $17.9 billion for first-quarter 2019 from the $17.1 billion for first-quarter 2018. First-quarter 2019 net income after taxes is well above the $11.3 billion average quarterly income for the last ten years and is the highest quarterly income since $18.2 billion for first-quarter 2015.

Policyholders' Surplus

Policyholders' surplus increased $37.4 billion to $779.5 billion as of March 31, 2019, from $742.2 billion as of December 31, 2018. Additions to surplus in first-quarter 2019 included $17.9 billion in net income after taxes and $25.6 billion in unrealized capital gains on investments (not included in net income). The deductions from surplus consisted of $0.3 billion in net capital outflow, $5.4 billion in dividends to shareholders, and $0.3 billion in miscellaneous net charges against surplus.

The $37.4 billion increase in surplus for first-quarter 2019 is the greatest nominal quarterly growth in surplus on record. It followed immediately after the record $39.3 billion drop in surplus in fourth-quarter 2018. Both events were driven by a significant downturn in the stock market at the end of 2018 and the subsequent recovery in first-quarter 2019. With insurers' investments in publicly traded common stocks mostly valued according to their market price, stock markets' ups and downs usually generate unrealized capital gains and losses for the industry, respectively. The $25.6 billion in unrealized capital gains in first-quarter 2019 offset most of the record $46.0 billion in unrealized capital losses in fourth-quarter 2018.

Insurers' $25.6 billion in unrealized capital gains in first-quarter 2019 represent a $37.6 billion swing from $12.1 billion in unrealized capital losses a year earlier. The net $0.3 billion of capital outflow in first-quarter 2019 compares with $2.4 billion of inflow a year earlier. Dividends to shareholders dropped to $5.4 billion in first-quarter 2019 from $10.1 billion in first-quarter 2018. The net result of aggregated miscellaneous credits to surplus and charges against surplus was a $0.3 billion charge in both first-quarter 2019 and in first-quarter 2018.

Using 12-month trailing premiums, the premium-to-surplus ratio rose to 0.78 as of March 31, 2019, from 0.77 as of March 31, 2018. In contrast, the ratio of loss and loss adjustment expense reserves to surplus declined to 0.81 as of March 31, 2019 from 0.82 a year earlier. These ratios remain low compared with their historical levels, due to surplus generally growing more rapidly than premiums or reserves. For example, over the 20 years ending 2018, the average premium-to-surplus ratio was 0.89 and the LLAE-reserves-to-surplus ratio was 1.05.

The key operating results for the industry are summarized in the table on page 4.

7. Unrealized capital gains or losses contribute directly to surplus change, but they do not affect net income.
8. Pretax operating income is the sum of net gains or losses on underwriting, net investment income, and miscellaneous other income.

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Operating Results for 2019 and 2018 ($ Millions)

First Quarter	2019	2018
Net Written Premiums	$154,776	$156,608
Percent Change (%)	–1.2	15.7
Net Earned Premiums	149,648	143,099
Percent Change (%)	4.6	9.4
Incurred Losses & Loss Adjustment Expenses	101,821	96,187
Percent Change (%)	5.9	3.0
Statutory Underwriting Gains (Losses)	6,040	4,960
Policyholders' Dividends	780	818
Net Underwriting Gains (Losses)	5,259	4,142
Pretax Operating Income	18,994	16,118
Net Investment Income Earned	13,158	11,780
Net Realized Capital Gains (Losses)	1,560	3,559
Net Investment Gains	14,718	15,339
Net Income (Loss) after Taxes	17,867	17,093
Percent Change (%)	4.5	114.6
Surplus (Consolidated)	779,520	747,780
Loss & Loss Adjustment Expense Reserves	633,322	611,554
Combined Ratio, Post-Dividends (%)	95.6	94.6

First-Quarter 2019: BY THE NUMBERS

$779.5 billion
Industry surplus, up from $742.2 billion at year-end 2018

$17.9 billion
Net income after taxes, a $0.8 billion increase from $17.1 billion in first-quarter 2018

$154.8 billion
Net written premium, after the record $156.6 billion in first-quarter 2018 and $135.4 billion in first-quarter 2017

95.6%
Combined ratio, after 94.6% in first-quarter 2018

$5.3 billion
Net underwriting gain, after a $4.1 billion gain in first-quarter 2018

3.1%
Annualized quarterly investment yield, after 2.9% in first-quarter 2018

$27.1 billion
Total capital gains, after $8.5 billion of total capital losses in first-quarter 2018

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