Property/Casualty Insurance Results: First-Half 2019

By Neil Spector, President, ISO, and Robert Gordon, Senior Vice President, Policy, Research and International, APCIA

Private U.S. property/casualty insurers' net income after taxes fell to $32.8 billion in first-half 2019 from $34.0 billion in first-half 2018. Insurers' overall profitability as measured by their annualized rate of return on average policyholders' surplus decreased to 8.5% from 9.0% 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 97.3% for first-half 2019 from 96.2% for first-half 2018, as their net underwriting gains[3] declined to $5.4 billion in first-half 2019 from $6.0 billion a year earlier. Net written premium growth slowed to 1.0% for first-half 2019 from 13.2% for first-half 2018.

Insurers' net investment income increased to $26.9 billion in first-half 2019 from $26.8 billion a year earlier, while realized capital gains decreased to $4.3 billion from $5.4 billion, resulting in $31.2 billion in net investment gains[4] for first-half 2019, down $1.0 billion from $32.2 billion for first-half 2018.

First-half 2019 delivered solid underwriting gains and brought the industry surplus to a new record.

The industry's surplus[5] grew in both the first and second quarters, reaching a new all-time-high value of $802.2 billion as of June 30, 2019, after $742.1 billion as of December 31, 2018, and $779.6 billion as of March 31, 2019.

The surplus growth combined with the decrease in net income after taxes lowered insurers' annualized rate of return on average surplus to 8.5%—down from the 9.0% for first-half 2018 but 0.3 percentage points above the average annualized first-half rate of return for 1989–2018.

Underwriting Results

In the first half of 2019, earned premiums grew 3.8% to $304.0 billion, while loss and loss adjustment expenses (LLAE) rose 5.7% to $212.6 billion, other underwriting expenses grew 0.7% to $85.0 billion, and policyholders' dividends remained essentially unchanged from the prior year at $1.1 billion. As a result, the industry reported a $5.4 billion net underwriting gain, a decrease from the $6.0 billion net underwriting gain for first-half 2018. The $5.4 billion underwriting gain for 2019 comprises a $5.2 billion gain for the first quarter and a $0.1 billion gain for the second quarter, while the $6.0 billion underwriting gain for first-half 2018 comprises a $4.1 billion gain for the first quarter and a $1.9 billion gain for the second quarter. The first-half underwriting gains are often concentrated in the first quarter—that was the case for 24 of the last 30 years.

Net written premiums rose $3.1 billion to $315.1 billion in first-half 2019 from $312.0 billion in first-half 2018, and net written premium growth slowed to 1.0% from 13.2% for first-half 2018. Net earned premium growth also slowed, to 3.8% in first-half 2019 from 10.1% for first-half 2018.

The unusually low written premium growth for first-half 2019 is mainly due to the unusually high comparison base. In 2018, many insurers

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% 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.

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-half 2018 premium growth was a compound effect of several developments, with the main drivers being organic growth in underlying direct 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's worth comparing 2019 premiums with the values for 2017. Average annual growth over the two-year period from first-half 2017 to first-half 2019 was 6.9% both for net written premium and for earned premium, and that significantly exceeds the rates observed in the preceding years. During the 14 years from 2004 until 2017, the net written premium growth rate never exceeded 5.0% and averaged 2.2%.

To assess the underlying direct premium growth, ISO compiled premiums for a large cohort of insurers whose first-half data was available for 2017, 2018, and 2019, which represents more than 95% of total net written premium for the industry. Aggregated net written premium for these insurers grew 13.2% in first-half 2018 and then grew only 0.9% in first-half 2019, while direct written premium grew approximately 6.0% in first-half 2018 and then grew 4.4% in first-half 2019. The changes in direct written premiums are consistent with continued growth in the economy and relative stability in insurance markets.

The 5.7% increase in LLAE in first-half 2019 outpaces earned premium growth and compares with the 3.5% increase a year earlier. Private U.S. insurers' net LLAE from catastrophes declined $1.0 billion to $13.7 billion for first-half 2019 from $14.7 billion a year earlier.[6]

Net LLAE for losses other than catastrophes rose $12.3 billion, or 6.6%, to $198.8 billion in first-half 2019 from $186.5 billion in first-half 2018.

Private U.S. insurers' net LLAE includes both their domestic and foreign catastrophic losses. However, U.S. insurers' $13.7 billion in net LLAE from catastrophes in first-half 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 the first half of 2019 or the first half of 2018.

Net written premium growth looks small when measured against the unusually high first-half 2018 level, but the two-year average growth rate is the strongest in years.

Reflecting the differences between premium growth and the growth in LLAE and other costs of providing insurance, the combined ratio deteriorated by 1.1 percentage points to 97.3% in first-half 2019 from 96.2% in first-half 2018.

Underwriting results benefited from $5.7 billion in favorable development of LLAE reserves in first-half 2019, based on new information and updated estimates for the ultimate cost of claims from prior accident years, including catastrophe losses. The $5.7 billion of favorable reserve development in first-half 2019 compares with $9.6 billion of favorable development in first-half 2018. Favorable development reduced the combined ratio by 1.9 percentage points in first-half 2019 and by 3.3 percentage points in first-half 2018.

Excluding development of LLAE reserves, net LLAE grew $7.5 billion, or 3.6%, to $218.3 billion in first-half 2019 from $210.8 billion in first-half 2018. Excluding catastrophes and the development of LLAE reserves, net LLAE grew $7.9 billion, or 4.0%, to $205.1 billion in first-half 2019 from $197.3 billion a year earlier. The combined ratio deteriorated 1.1 percentage points in first-half 2019; but if catastrophe LLAE and LLAE reserve development in first-half 2019 had been at the same level as in first-half 2018, the combined ratio would have remained unchanged.

The $5.4 billion net gain on underwriting in first-half 2019 amounted to 1.8% of the $304.0 billion in net premiums earned during the period. The $6.0 billion net gain on underwriting in first-half 2018 amounted to 2.1% of the $292.7 billion in net premiums earned during that period.

While overall net written premium growth in first-half 2019 dropped to 1.0% from 13.2% a year earlier and the combined ratio deteriorated to 97.3% from 96.2%, the dynamics varied across industry segments.

Net written premium growth for insurers writing mostly personal lines slowed to 4.0% in first-half 2019 from 7.6% a year earlier. Excluding mortgage and financial guaranty insurers, net written premium growth for insurers writing predominantly commercial lines dropped 3.2% in first-half 2019 after jumping 25.6% in first-half 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 from 5.7% in first-half 2018 to 2.4% in first-half 2019. Estimated direct premium growth was approximately 3.8% for insurers writing predominately personal lines, approximately 5.3% for insurers with balanced books of business, and approximately 5.4% for insurers writing mostly commercial lines, excluding mortgage and financial guaranty insurers. Direct premium growth was estimated using a consistent set of insurers representing more than 95% of commercial insurers and close to 100% of remaining segments.

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.

Underwriting profitability as measured by the combined ratio deteriorated across all segments. Excluding mortgage and financial guaranty insurers, commercial lines insurers' combined ratio increased 1.1 percentage points to 96.2% in first-half 2019. Personal lines insurers' combined ratio rose 1.3 percentage points to 97.2%, while balanced insurers' combined ratio deteriorated 0.6 percentage points to 100.3% in first-half 2019 from 99.7% in first-half 2018.

Investment Results

Insurers' net investment income—primarily dividends from stocks and interest on bonds—increased to $26.9 billion in first-half 2019 from $26.8 billion in first-half 2018. Insurers' realized capital gains on investments declined to $4.3 billion in first-half 2019 from $5.4 billion a year earlier. Combining net investment income and realized capital gains, overall net investment gains decreased 3.1% to $31.2 billion in first-half 2019 from $32.2 billion a year earlier.

Insurers' net investment income increased 0.3%, while average cash and invested assets for first-half 2019 grew 2.6% compared with first-half 2018. This brought the annualized yield on insurers' investments in first-half 2019 to 3.2%, essentially unchanged from a year earlier, and below the 3.4% average annualized quarterly yield for the last ten years. From 1960 to 2018, insurers' annual investment yield averaged 5.0% but ranged from as low as 2.8% in 1961 to as high as 8.2% in 1984 and 1985. In recent years, investment yields have trended downward, and annual yields have not exceeded 4.0% since 4.2% for 2008. On a full-year basis, insurers' annual investment yield steadily declined from 4.6% for 2005 to 3.2% for both 2014 and 2015 and to 3.1% in 2017. In 2018, investment yield rose to 3.4%, but the bulk of the increase was due to one-time money transfers from subsidiaries outside the U.S. property/casualty universe, rather than from sustainable increases in investment profitability.

Combining the $4.3 billion in realized capital gains in first-half 2019 with the $41.6 billion in unrealized capital gains[7] during the same period, insurers posted $45.9 billion in overall capital gains for first-half 2019—a $48.5 billion improvement from first-half 2018. Over the past 30 years, insurers' total capital gains have averaged $3.3 billion per quarter but have ranged from as high as $45.7 billion in fourth-quarter 2017 to as low as negative $44.6 billion in fourth-quarter 2018.

> Insurers reported record first-half capital gains as stock markets recovered from the year-end 2018 decline.

Pretax Operating Income

Pretax operating income[8] decreased $0.5 billion to $33.1 billion for first-half 2019 from $33.6 billion for first-half 2018. The decrease in operating income was the net result of the $0.6 billion decline in net gains on underwriting, the $0.1 billion increase in miscellaneous other income, and the $0.1 billion increase in net investment 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 fell $1.2 billion to $32.8 billion for first-half 2019 from $34.0 billion for first-half 2018. First-half 2019 net income after taxes is considerably above the $22.5 billion average first-half income for the last ten years.

Policyholders' Surplus

Policyholders' surplus surged by $60.1 billion to a new record-high $802.2 billion as of June 30, 2019, from $742.1 billion as of December 31, 2018. Additions to surplus in first-half 2019 included $32.8 billion in net income after taxes and $41.6 billion in unrealized capital gains on investments (not included in net income). Deductions from surplus consisted of $12.3 billion in dividends to shareholders, $0.5 billion in net capital outflow, and $1.5 billion in miscellaneous charges against surplus.

The $60.1 billion increase in surplus for first-half 2019 followed immediately after the $39.5 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 2019. With insurers' investments in publicly traded common stocks mostly valued according to their market price, stock market ups and downs usually generate unrealized capital gains and losses for the industry, respectively. The $41.6 billion in unrealized capital gains in first-half 2019 offset most of the $45.7 billion in unrealized capital losses in fourth-quarter 2018.

Insurers had $41.6 billion in unrealized capital gains in first-half 2019, a $49.6 billion swing from $8.0 billion in unrealized capital losses a year earlier. The net $0.5 billion of capital outflow in first-half 2019 compares with $3.3 billion of capital inflow a year earlier. Dividends to shareholders fell to $12.3 billion in first-half 2019 from $17.4 billion in first-half 2018. Miscellaneous charges against surplus rose to $1.5 billion in first-half 2019 from $1.3 billion in first-half 2018.

Using 12-month trailing premiums, the premium-to-surplus ratio remained at 0.77 both as of June 30, 2019, and as of June 30, 2018. The ratio of loss and loss adjustment expense reserves to surplus declined to 0.80 as of June 30, 2019, from 0.81 a year earlier. These ratios remain low compared with their historical levels because surplus grew 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.

Second-Quarter Results

The property/casualty insurance industry's consolidated net income after taxes fell to $14.9 billion in second-quarter 2019 from $16.9 billion in second-quarter 2018. Property/casualty insurers' annualized rate of return on average surplus fell to 7.5% in second-quarter 2019 from 9.0% a year earlier.

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.

The $14.9 billion in net income after taxes for the insurance industry in second-quarter 2019 was the net result of $14.2 billion in pretax operating income, $2.7 billion in realized capital gains on investments, and $2.0 billion in federal and foreign income taxes.

The industry's $14.2 billion in pretax operating income for second-quarter 2019 was down $3.3 billion from $17.5 billion for second-quarter 2018. The industry's second-quarter 2019 pretax operating income was the sum of $0.1 billion in net underwriting gains, $13.7 billion in net investment income, and $0.3 billion in miscellaneous other income.

Net underwriting gains deteriorated to just $0.1 billion for second-quarter 2019 from $1.9 billion for second-quarter 2018.

Net LLAE from catastrophes included in private U.S. insurers' financial results in second-quarter 2019 declined to $9.0 billion from $9.7 billion in second-quarter 2018. The contribution of catastrophe LLAE to the second-quarter combined ratio decreased to 5.8 percentage points in 2019 from 6.5 percentage points in 2018.

Second-quarter results worsened compared with 2018, but the industry surplus continued to grow.

Second-quarter 2019 net gains on underwriting amounted to 0.1% of the $154.4 billion in premiums earned during the period, whereas in second-quarter 2018 net gains on underwriting amounted to 1.3% of the $149.7 billion in premiums earned during the period. The industry's combined ratio deteriorated to 98.9% in second-quarter 2019 from 97.7% in second-quarter 2018. Over the last 30 years, the second-quarter combined ratio averaged 103.7% but reached as high as 117.5% in 2011 and as low as 92.8% in 2006.

Net written premiums rose $4.9 billion, or 3.1%, to $160.4 billion in second-quarter 2019 from $155.5 billion in second-quarter 2018. The overall trend has been for quarterly written premiums to rise, and indeed there have been increases in 36 of the past 37 quarters. The most recent decline occurred in first-quarter 2019 and was due to an unusually high comparison base in the prior year triggered by changes in reinsurance utilization.

Net earned premiums grew 3.1% to $154.4 billion in second-quarter 2019 from $149.7 billion in second-quarter 2018. LLAE grew 5.4% to $110.7 billion in second-quarter 2019 from $105.0 billion in second-quarter 2018. Noncatastrophe LLAE rose 6.8% to $101.8 billion from $95.3 billion in second-quarter 2018.

Net investment income for the industry declined to $13.7 billion in second-quarter 2019 from $15.0 billion in second-quarter 2018. The elevated levels of investment income in second-quarter 2018 are attributable to the variations in magnitude and timing of dividends from subsidiaries outside the U.S. property/casualty insurance universe. Miscellaneous other income dropped to $0.3 billion in second-quarter 2019 from $0.6 billion in second-quarter 2018.

Realized capital gains on investments increased to $2.7 billion in second-quarter 2019 from $1.8 billion in second-quarter 2018. Combining net investment income and realized capital gains, net investment gains fell $0.4 billion, or 2.6%, to $16.4 billion in second-quarter 2019 from $16.9 billion a year earlier.

Insurers posted $16.0 billion in unrealized capital gains on investments in second-quarter 2019, a $12.0 billion increase from $4.0 billion a year earlier. Combining realized and unrealized amounts, the insurance industry posted $18.7 billion in overall capital gains in second-quarter 2019—a $12.8 billion increase from the $5.9 billion in overall capital gains on investments in second-quarter 2018.

The key operating results for the industry are summarized in the table on page 5.

Neil Spector is president of ISO, helping property/casualty insurers manage and improve underwriting and rating performance throughout the policy life cycle. In the United States, Europe, and around the world, Mr. Spector is responsible for the personal and commercial lines underwriting and rating organization, including product management, strategy, sales, and operations, as well as application development, business development, government relations, and finance.

Robert Gordon is senior vice president for policy, research and international, APCIA. He is responsible for working with APCIA members to develop and frame public policy positions on the opportunities and challenges facing the property/casualty insurance industry at the state, federal, and international levels. Mr. Gordon also coordinates policy support for APCIA's extensive state and federal advocacy efforts, media outreach, and information products.

Operating Results for 2019 and 2018 ($ Millions)

First Half	2019	2018
Net Written Premiums	$315,068	$311,982
Percent Change (%)	1.0	13.2
Net Earned Premiums	304,006	292,741
Percent Change (%)	3.8	10.1
Incurred Losses & Loss Adjustment Expenses	212,554	201,162
Percent Change (%)	5.7	3.5
Statutory Underwriting Gains (Losses)	6,447	7,139
Policyholders' Dividends	1,086	1,128
Net Underwriting Gains (Losses)	5,362	6,011
Pretax Operating Income	33,147	33,597
Net Investment Income Earned	26,890	26,806
Net Realized Capital Gains (Losses)	4,304	5,388
Net Investment Gains	31,194	32,194
Net Income (Loss) after Taxes	32,787	33,973
Percent Change (%)	-3.5	119.3
Surplus (Consolidated)	802,192	761,198
Loss & Loss Adjustment Expense Reserves	642,096	618,971
Combined Ratio, Post-Dividends (%)	97.3	96.2

Second Quarter	2019	2018
Net Written Premiums	$160,349	$155,477
Percent Change (%)	3.1	10.9
Net Earned Premiums	154,413	149,743
Percent Change (%)	3.1	10.9
Incurred Losses & Loss Adjustment Expenses	110,729	105,032
Percent Change (%)	5.4	4.0
Statutory Underwriting Gains (Losses)	449	2,197
Policyholders' Dividends	310	312
Net Underwriting Gains (Losses)	139	1,885
Pretax Operating Income	14,192	17,493
Net Investment Income Earned	13,736	15,035
Net Realized Capital Gains (Losses)	2,708	1,847
Net Investment Gains	16,444	16,882
Net Income (Loss) after Taxes	14,923	16,921
Percent Change (%)	-11.8	124.8
Surplus (Consolidated)	802,192	761,198
Loss & Loss Adjustment Expense Reserves	642,096	618,971
Combined Ratio, Post-Dividends (%)	98.9	97.7

First-Half 2019: BY THE NUMBERS

$802.2 billion

Industry surplus, up from $779.6 billion on March 31, 2019, and from $742.1 billion at year-end 2018

$32.8 billion

Net income after taxes, down from $34.0 billion in first-half 2018

$315.1 billion

Net written premium, after $312.0 billion in first-half 2018 and $275.6 billion in first-half 2017

97.3%

Combined ratio, after 96.2% for first-half 2018

$5.4 billion

Net underwriting gain, after $6.0 billion underwriting gain in first-half 2018

3.2%

Annualized investment yield, essentially unchanged from a year earlier

$45.9 billion

Total capital gains, compared with $2.6 billion of total capital losses in first-half 2018

ISO
A Verisk Business
ISO
545 Washington Boulevard
Jersey City, NJ 07310-1686
1-800-888-4476 • www.iso.com

APCIA
8700 West Bryn Mawr Avenue, Suite 1200S
Chicago, IL 60631-3512
847-297-7800 • www.pciaa.net

American Property Casualty Insurance Association℠
INSURING AMERICA apci.org

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