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Social Inflation Meets Economic Inflation

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Agenda

- Economic Inflation vs. Social Inflation
- Observed Impacts
- Challenges for Reserving
- Potential Solutions & Methods
- Summary

Economic Inflation vs. Social Inflation



Jury awards have increased ~17x

Source: Image generated/edited using ChatGPT (OpenAI)

Social Inflation



NAIC: the increase of insurance claims' payouts and loss ratios due to non-economic factors resulting from the high costs of liability litigation.



AM Best: rising cost of insurance claims that exceeds general economic inflation, driven by societal and legal trends, such as higher jury awards, increased litigation, and expanded definitions of liability.

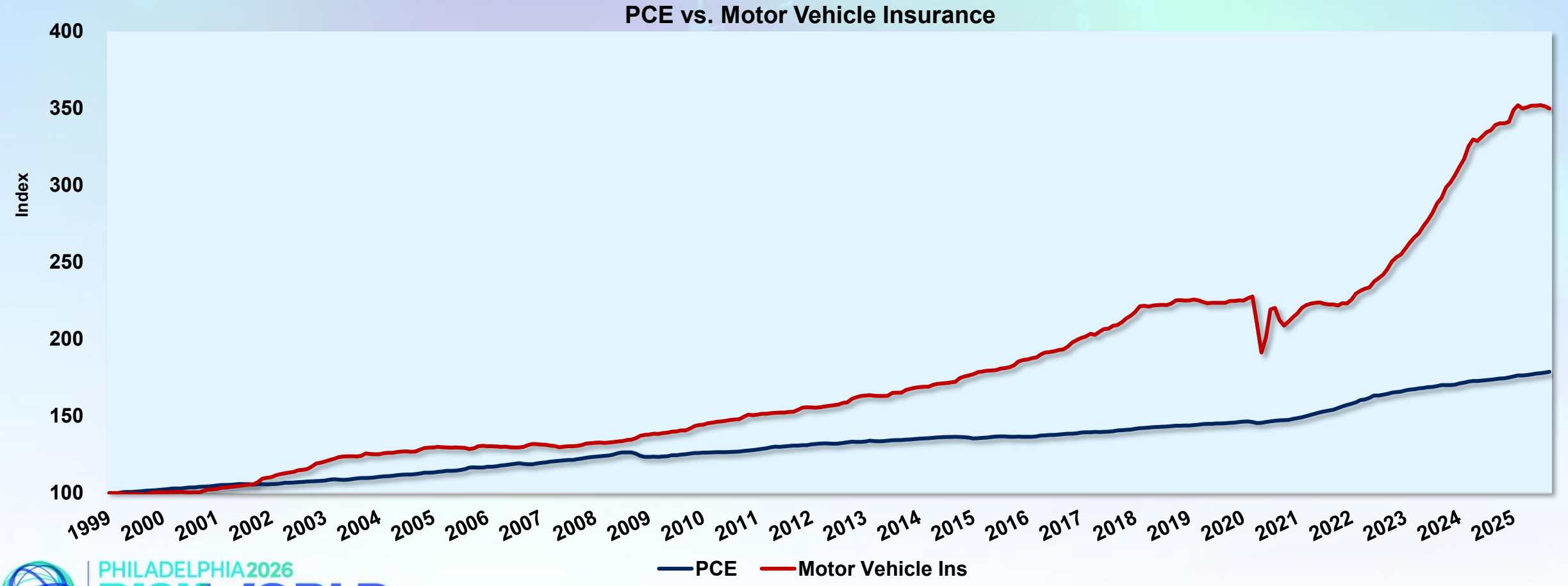
Different Emphasis for Each Stakeholder

Stakeholder	Emphasis
Insurers & Reinsurers	Claims severity and reserve pressure
AM Best	Capital adequacy and underwriting risk
Actuaries	Modeling uncertainty and trend deviation
Legal Reform Groups	Plaintiff bar tactics and tort expansion
Regulators	Market stability and availability/affordability

Common Themes

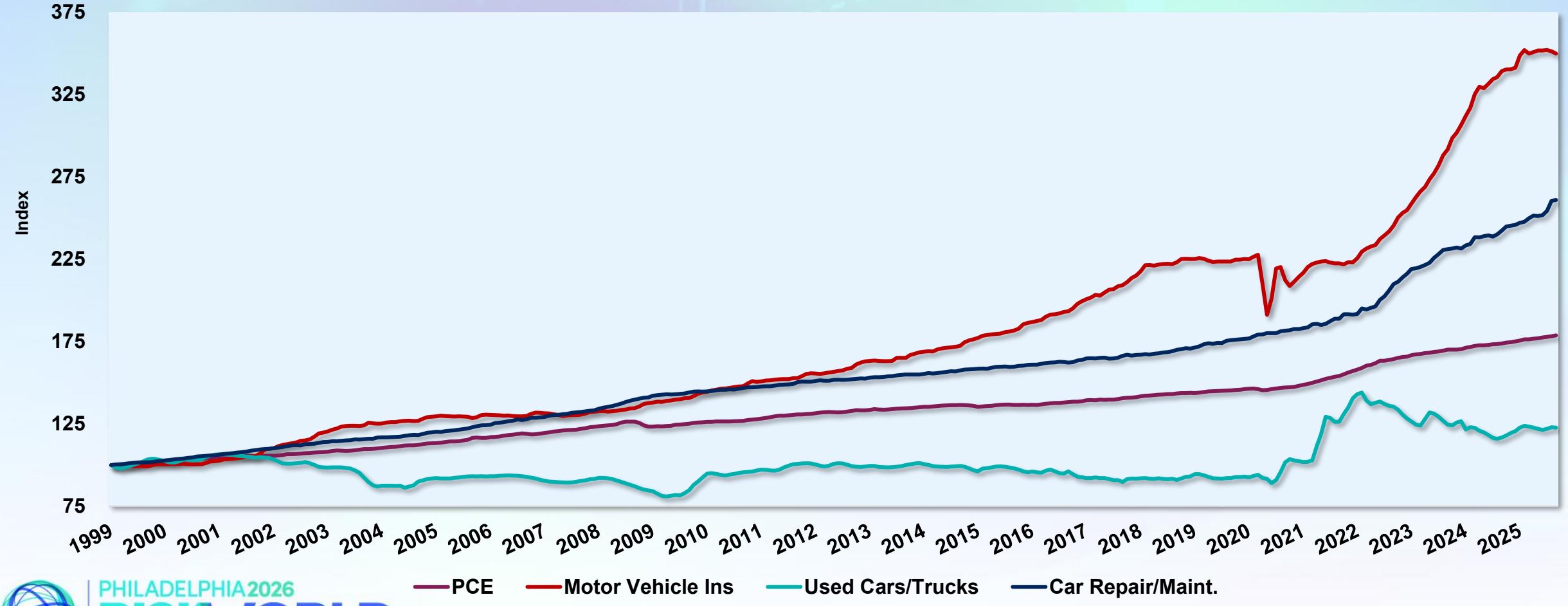
Nuclear verdicts	Third-party litigation funding (TPLF)	Attorney advertising growth	Expanded liability doctrines
Reptile theory litigation tactics	Broader interpretations of coverage	Societal distrust of corporations	Claims severity outpacing economic inflation

Insurance Inflation Significantly Outpaces Broader Consumer Prices

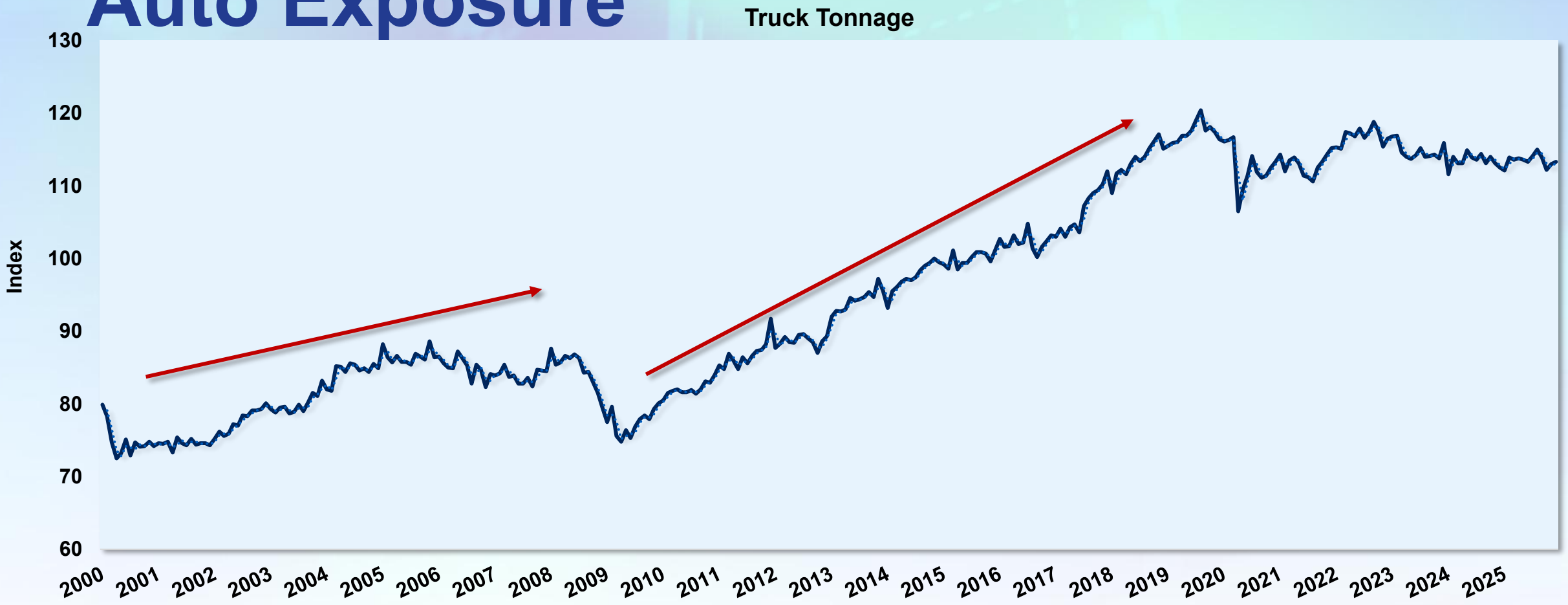


Note: PCE Index and Motor Vehicle Insurance Indexed to 100 in 1999

Severity Shock and the Rate Catch-Up Cycle



Freight Activity Drives Commercial Auto Exposure

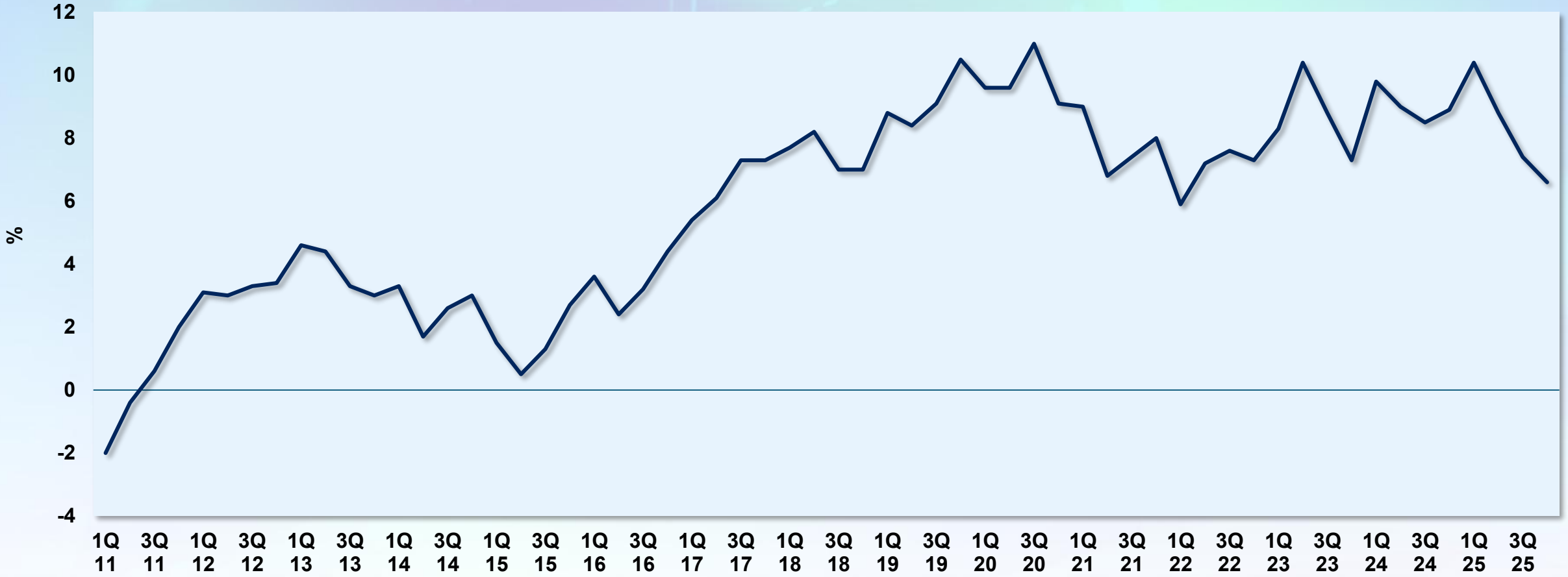


Source: FRED

Commercial Auto Results Reflect the Exposure Cycle



Commercial Auto Pricing: Too Late to Respond to Loss Deterioration



Observed Impacts

Swiss Re Social Inflation Index[5]

- Measures the increased severity of insurance claims beyond that which can be explained by economic drivers
- US liability
  - Above 0% beginning in 2014
  - 5.4% annually for 2017-2022
  - Rising to 7% in 2023
  - Driven by large single-claimant events, non-economic damages, centered around personal injury verdicts
- Other Countries
  - Australia and Canada: rose 7 points in 2022
  - United Kingdom: rose 10 points in 2022
  - Minimal in Germany and Japan

They believe social inflation will continue into the future in the US with no signs of letting up despite declining economic inflation.

Observed Impacts – Commercial Auto Liability

Inflation				
	Change in Reserve Deficiency (undiscounted Basis)			
	Based on CY Inflation Increase of:			
	1.0%	3.0%	5.0%	7.0%
All 2 Year Lines Combined	1.6	4.9	8.4	12.1
Homeowners/Farmowners	1.6	5.0	8.4	12.1
Private Passenger Auto Liability	2.1	6.4	11.0	15.8
Commercial Auto Liability	2.6	8.1	13.8	20.0
Reins Assumed - XS - Property	2.7	8.6	15.0	22.0
Medical Prof Liab (CM)	2.9	9.1	15.9	23.2
Commercial Multiple Peril	3.2	10.0	17.5	25.6
Medical Prof Liab (Occ)	3.6	11.4	20.1	29.7
Other Liability (CM)	3.8	12.1	21.2	31.4
Products Liability (Occ)	4.4	14.0	24.7	36.8
Other Liability (Occ)	5.0	16.1	28.8	43.3
Reins Assumed - XS - Liability	5.4	17.5	31.2	46.9
Workers' Compensation	5.5	17.7	31.8	48.1
Total	3.7	11.8	21.0	31.2

4.1%

11.2%

Inflation					
	Effect on PHS				
Reserves To Surplus	Based on CY Inflation Increase of:				
	1.0%	3.0%	5.0%	7.0%	
0.3	0.5	1.6	2.8	4.0	
0.3	0.5	1.6	2.7	3.8	
0.4	0.8	2.6	4.4	6.3	
1.1	3.0	9.2	15.7	22.7	12.7%
0.3	0.8	2.6	4.5	6.6	
0.9	2.5	7.8	13.6	19.9	
1.1	3.5	11.0	19.2	28.2	
1.0	3.6	11.4	20.1	29.7	
1.4	5.3	16.7	29.4	43.5	
1.4	6.1	19.4	34.3	51.0	
1.4	7.0	22.3	39.9	60.0	
1.5	8.2	26.2	46.8	70.3	
1.1	6.2	20.0	36.0	54.5	
0.7	2.8	8.8	15.6	23.2	

4.1%

Observed Impacts

Auto Liability – Frequency

Number of motor vehicle tort civil lawsuits [4, 5]

Federal courts – Average annual increase 4.9% compound annual growth rate 2014-2023	State courts – Average annual increase 2.8% compound annual growth rate 2014-2023

- Increasing frequency by itself does not mean social inflation
- Question is: are lawsuits being filed now that would not have been filed in the past?
  - If yes, then social inflation

Observed Impacts – Commercial Auto Liability

Commercial Auto Liability								
AY	NEP (000)	ULT LR	UW Exp Ratio	Combined Ratio	UW Profit / (Loss) Ratio	Excess(4) Inflation Ratio	Revised Combined Ratio	Revised UW Profit / (Loss) Ratio
2016	20,782	85.8	29.5	115.3	-15.3	14.7	100.6	-0.6
2017	21,811	85.8	28.7	114.5	-14.5	15.4	99.1	0.9
2018	25,268	86.5	28.2	114.7	-14.7	18.6	96.1	3.9
2019	28,013	87.9	27.5	115.4	-15.4	20.0	95.4	4.6
2020	28,889	72.4	28.0	100.4	-0.4	16.1	84.3	15.7
2021	32,968	79.7	26.1	105.8	-5.8	17.6	88.2	11.8
2022	37,375	84.9	25.5	110.4	-10.4	18.3	92.0	8.0
2023	40,509	85.9	26.3	112.2	-12.2	17.7	94.6	5.4
2024	44,881	81.4	25.4	106.8	-6.8	17.8	89.0	11.0

Observed Impacts

Personal Auto Liability
$61B AYs between 2013 and 2022 [3] Net, severity impact only

- CY 2013-2017 paid emergence 2.2% higher than expected, CY 2018-2022 6.1% higher, per yr
- CY 2013-2022 case incurred emergence 8.4% higher than expected, per yr
- 2013-2019 largely social inflation, 2020-2022 economic and social
- Slow down of claims settlement patterns during COVID, subsequent speed up
- Approx $7B per year for AY2018-2020, $12.5B for 2021-2022 (4.5%, 4.8%, 5.3%, 8.4%, 8.3% of NEP)
- Total (social + economic) “above average” inflation was 0.6% yr above avg

Personal Auto Liability
$92B to $102B AYs 2015 thru 2024 [4] Net, severity impact only

- Approx $15.5B per year for AY2022-2024, (9.2%, 9.0%, 9.2% of NEP using $92B)
- “Above average” annual inflation = 0.7% using case incurred, 0.8% using paid
- Bodily Injury claim frequency increasing

Observed Impacts – Personal Auto Liability

Inflation				
	Change in Reserve Deficiency (undiscounted Basis)			
	Based on CY Inflation Increase of:			
	1.0%	3.0%	5.0%	7.0%
All 2 Year Lines Combined	1.6	4.9	8.4	12.1
Homeowners/Farmowners	1.6	5.0	8.4	12.1
Private Passenger Auto Liability	2.1	6.4	11.0	15.8
Commercial Auto Liability	2.6	8.1	13.8	20.0
Reins Assumed - XS - Property	2.7	8.6	15.0	22.0
Medical Prof Liab (CM)	2.9	9.1	15.9	23.2
Commercial Multiple Peril	3.2	10.0	17.5	25.6
Medical Prof Liab (Occ)	3.6	11.4	20.1	29.7
Other Liability (CM)	3.8	12.1	21.2	31.4
Products Liability (Occ)	4.4	14.0	24.7	36.8
Other Liability (Occ)	5.0	16.1	28.8	43.3
Reins Assumed - XS - Liability	5.4	17.5	31.2	46.9
Workers' Compensation	5.5	17.7	31.8	48.1
Total	3.7	11.8	21.0	31.2

1.2%

2.6%

Inflation				
	Effect on PHS			
Reserves To Surplus	Based on CY Inflation Increase of:			
	1.0%	3.0%	5.0%	7.0%
0.3	0.5	1.6	2.8	4.0
0.3	0.5	1.6	2.7	3.8
0.4	0.8	2.6	4.4	6.3
1.1	3.0	9.2	15.7	22.7
0.3	0.8	2.6	4.5	6.6
0.9	2.5	7.8	13.6	19.9
1.1	3.5	11.0	19.2	28.2
1.0	3.6	11.4	20.1	29.7
1.4	5.3	16.7	29.4	43.5
1.4	6.1	19.4	34.3	51.0
1.4	7.0	22.3	39.9	60.0
1.5	8.2	26.2	46.8	70.3
1.1	6.2	20.0	36.0	54.5
0.7	2.8	8.8	15.6	23.2

1.2%

1.1%

Observed Impacts – Personal Auto Liability

Personal Auto Liability								
AY	NEP (000)	ULT LR	UW Exp Ratio	Combined Ratio	UW Profit / (Loss) Ratio	Excess (4) Inflation Ratio	Revised Combined Ratio	Revised UW Profit / (Loss) Ratio
2016	120,914	84.3	23.7	108.0	-8.0	3.7	104.3	-4.3
2017	130,143	80.1	23.1	103.2	-3.2	4.1	99.0	1.0
2018	140,877	77.3	23.3	100.6	-0.6	4.8	95.8	4.2
2019	145,600	78.5	23.3	101.8	-1.8	4.8	97.0	3.0
2020	144,036	66.1	26.1	92.2	7.8	4.5	87.7	12.3
2021	146,784	80.0	23.7	103.7	-3.7	8.2	95.5	4.5
2022	151,992	86.5	22.0	108.5	-8.5	9.2	99.3	0.7
2023	167,471	85.6	19.9	105.5	-5.5	9.0	96.5	3.5
2024	188,786	80.8	20.8	101.6	-1.6	9.2	92.4	7.6

Observed Impacts

Medical Professional Liability Claims Made Physicians –
$2.4B to $3.5B for AYs 2012 thru 2021[7] Net, severity impact only

- CY 2012-2019 paid emergence 2.9% higher than expected, CY 2020-2021 favorable due to COVID
- Approx $500k per year for AY 2015-2021 (avg 11.2% of NEP) Social Inflation
- Pace of claim settlements >$1m accelerated – significant driver of social inflation

Medical Professional Liability Claims Made Physicians –
$4.0B for AYs 2015 thru 2024[8] Net, severity impact only

- CY 2015-2024 paid emergence 4.3% higher than expected, CY 2020-2021 favorable due to COVID
- Approx $400k per year for AY2015-2024(avg 8.5% of NEP) Total (Economic + Social) "Above Average" inflation
- Claim settlements >$1m went from 7% of total in 2006 to 12% of total in 2023 – significant driver of social inflation

Observed Impacts – Medical Professional Liability Claims Made

Inflation				
	Change in Reserve Deficiency (undiscounted Basis)			
	Based on CY Inflation Increase of:			
	1.0%	3.0%	5.0%	7.0%
All 2 Year Lines Combined	1.6	4.9	8.4	12.1
Homeowners/Farmowners	1.6	5.0	8.4	12.1
Private Passenger Auto Liability	2.1	6.4	11.0	15.8
Commercial Auto Liability	2.6	8.1	13.8	20.0
Reins Assumed - XS - Property	2.7	8.6	15.0	22.0
Medical Prof Liab (CM)	2.9	9.1	15.9	23.2
Commercial Multiple Peril	3.2	10.0	17.5	25.6
Medical Prof Liab (Occ)	3.6	11.4	20.1	29.7
Other Liability (CM)	3.8	12.1	21.2	31.4
Products Liability (Occ)	4.4	14.0	24.7	36.8
Other Liability (Occ)	5.0	16.1	28.8	43.3
Reins Assumed - XS - Liability	5.4	17.5	31.2	46.9
Workers' Compensation	5.5	17.7	31.8	48.1
Total	3.7	11.8	21.0	31.2

4.3%

13.6%

Inflation					
Reserves To Surplus	Effect on PHS				
	Based on CY Inflation Increase of:				
	1.0%	3.0%	5.0%	7.0%	
0.3	0.5	1.6	2.8	4.0	4.3%
0.3	0.5	1.6	2.7	3.8	
0.4	0.8	2.6	4.4	6.3	
1.1	3.0	9.2	15.7	22.7	
0.3	0.8	2.6	4.5	6.6	
0.9	2.5	7.8	13.6	19.9	11.6%
1.1	3.5	11.0	19.2	28.2	
1.0	3.6	11.4	20.1	29.7	
1.4	5.3	16.7	29.4	43.5	
1.4	6.1	19.4	34.3	51.0	
1.4	7.0	22.3	39.9	60.0	
1.5	8.2	26.2	46.8	70.3	
1.1	6.2	20.0	36.0	54.5	
0.7	2.8	8.8	15.6	23.2	

Observed Impacts – Medical Professional Liability Claims Made

AY	NEP (000)	ULT LR	UW Exp Ratio	Combined Ratio	UW Profit / (Loss) Ratio	Excess [4] Inflation Ratio	Revised Combined Ratio	Revised UW Profit / (Loss) Ratio
2015	5,869	81.5	32.7	114.2	-14.2	9.7	104.5	-4.5
2016	5,926	88.0	28.9	116.9	-16.9	11.4	105.5	-5.5
2017	5,850	90.8	28.4	119.2	-19.2	12.5	106.7	-6.7
2018	6,175	97.7	28.8	126.5	-26.5	13.5	113.0	-13.0
2019	6,332	94.8	27.8	122.6	-22.6	3.1	119.5	-19.5
2020	6,597	87.5	27.9	115.4	-15.4	9.6	105.8	-5.8
2021	7,447	76.5	26.1	102.6	-2.6	7.8	94.8	5.2
2022	7,957	73.5	25.3	98.8	1.2	8.8	90.0	10.0
2023	8,324	80.0	26.4	106.4	-6.4	0.4	106.0	-6.0
2024	8,956	81.0	26.5	107.5	-7.5	8.3	99.1	0.9

Observed Impacts – Other Liability Occurrence

Inflation				
	Change in Reserve Deficiency (undiscounted Basis)			
	Based on CY Inflation Increase of:			
	1.0%	3.0%	5.0%	7.0%
All 2 Year Lines Combined	1.6	4.9	8.4	12.1
Homeowners/Farmowners	1.6	5.0	8.4	12.1
Private Passenger Auto Liability	2.1	6.4	11.0	15.8
Commercial Auto Liability	2.6	8.1	13.8	20.0
Reins Assumed - XS - Property	2.7	8.6	15.0	22.0
Medical Prof Liab (CM)	2.9	9.1	15.9	23.2
Commercial Multiple Peril	3.2	10.0	17.5	25.6
Medical Prof Liab (Occ)	3.6	11.4	20.1	29.7
Other Liability (CM)	3.8	12.1	21.2	31.4
Products Liability (Occ)	4.4	14.0	24.7	36.8
Other Liability (Occ)	5.0	16.1	28.8	43.3
Reins Assumed - XS - Liability	5.4	17.5	31.2	46.9
Workers' Compensation	5.5	17.7	31.8	48.1
Total	3.7	11.8	21.0	31.2

2.0%

10.4%

Inflation				
Reserves To Surplus	Effect on PHS			
	Based on CY Inflation Increase of:			
	1.0%	3.0%	5.0%	7.0%
0.3	0.5	1.6	2.8	4.0
0.3	0.5	1.6	2.7	3.8
0.4	0.8	2.6	4.4	6.3
1.1	3.0	9.2	15.7	22.7
0.3	0.8	2.6	4.5	6.6
0.9	2.5	7.8	13.6	19.9
1.1	3.5	11.0	19.2	28.2
1.0	3.6	11.4	20.1	29.7
1.4	5.3	16.7	29.4	43.5
1.4	6.1	19.4	34.3	51.0
1.4	7.0	22.3	39.9	60.0
1.5	8.2	26.2	46.8	70.3
1.1	6.2	20.0	36.0	54.5
0.7	2.8	8.8	15.6	23.2

2.0%

14.4%

Challenges for Reserving

- Potential Third-Party Litigation Funding Costs (Ernst & Young [16])(CAL + OL Occ + MPL)
  - Direct Costs
    - Returns on assets under management (AUM)
    - $2B to $5B per year for the next 5 years
  - Indirect Costs
    - Increased legal fees
    - Increased awards
    - $2B to $5B per year for the next 5 years
  - Total Cost
    - $4B to $10B per year for the next 5 years
    - Average cost $6B per year
    - Between 4.0 and 5.5 points of loss ratio per year (on $120B NEP in 2024)

They believe TPLF is the most significant and measurable driver of social inflation.

Challenges for Reserving

Economic inflation increases claim severity, now more volatile, so harder to predict

Social inflation further increases claim severity

TPLF further increases social inflation

Inflation is a calendar year effect, so impact on multiple accident years

Challenges for Reserving

- LDF method understates ultimate losses when inflation is greater than expected
- Longer time to settlement slows loss development and LDF method understates ultimates
- Greater willingness to pursue claims increases frequency
- Covid-19 distortions

Potential Solutions and Methods

- Loss Development Methods
  - Adjustments for changes in closing rates
  - Adjustments for changes in average case reserves
- Frequency/Severity Methods
  - Advantage: reflects frequency and severity change
  - Disadvantage: wrong trend assumption
  - Using long-term trends may understate current trends
- Insurer responses
  - Claims handling/UW actions/lawsuits
- Be aware of Judicial Hellholes[14]
- Legislative
  - Caps on non-economic damages
  - TPLF disclosures, caps on funder returns, restrictions on funder input to legal counsel decisions, and settlement timelines[15]

Social Inflation Impacts from Studies

	Year(s)	$ Impact	Annual Severity Trend Impact	Combined Ratio Impact
Comm Auto Liability[4]	2015-2024	52B - 71B	2.2% - 3.1%	18 points*
Personal Auto Liability[4]	2015-2024	92B - 102B	0.7% - 0.8%	9 points*
Other Liability Occ[4]	2015-2024	83B - 103B	2.7% - 3.7%	9 points*
MPL Physicians[8]	2015-2024	4B	--	8.5 points**
US Liability[5]	2017-2022	--	5.4%	--
	2023	--	7.0%	--
Total		231B - 280B		

*Combined Ratio impact is avg for latest 3 AYs, using low end of range
** Combined Ratio impact is avg for all 10 AYs, higher in earlier years

Summary

Liability severity trends impacted by changing economic inflation and social inflation

Can be estimated

Social Inflation is material and expected to continue

- Ranging from $231B to $280B cumulative as of 2024
- Impact varies by line, by year, and by location

Need to reflect in pricing and reserving

Don’t give up

- Can adjust procedures / locations / limits / etc.

Look for help and educate

- Legislatures
- Insureds
- Public

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