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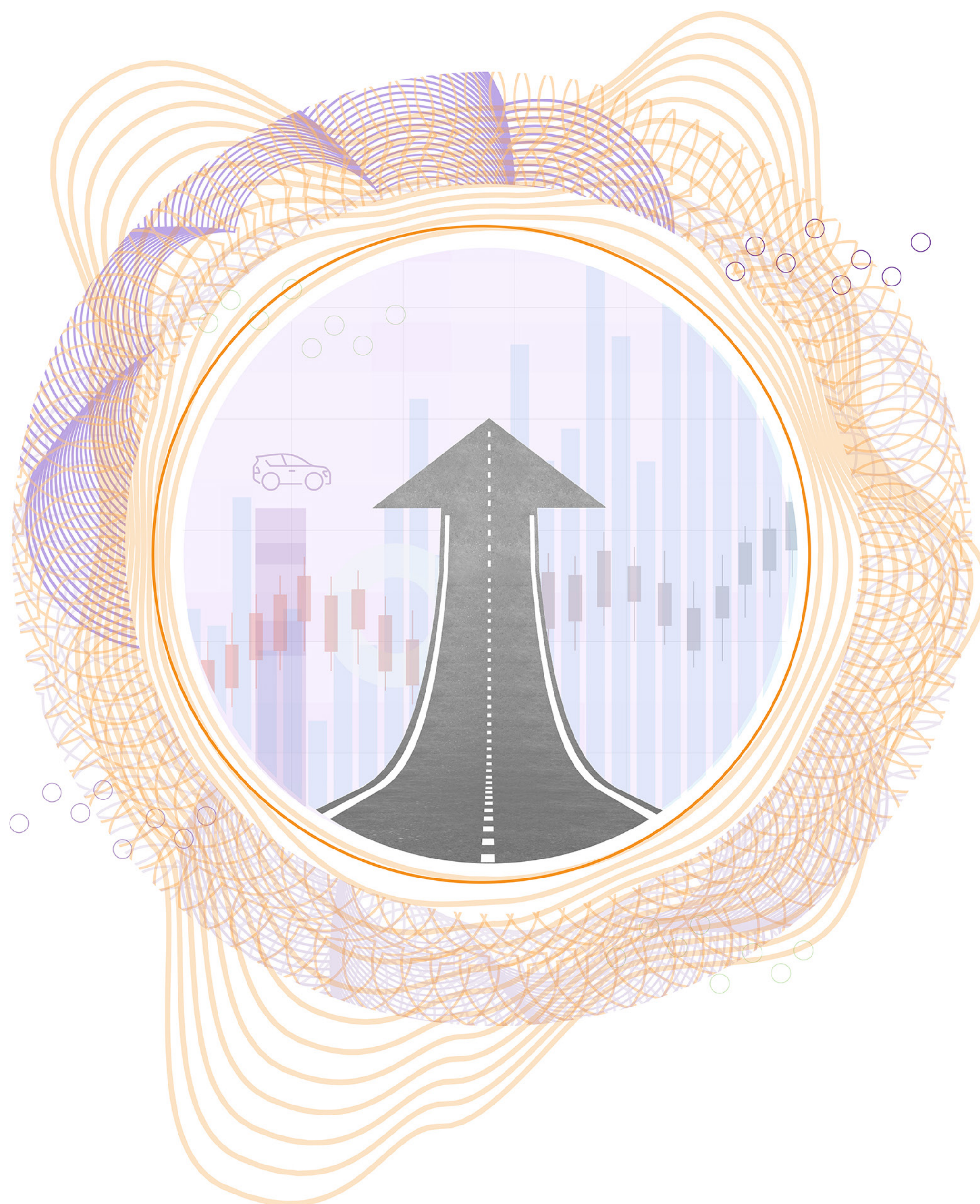

Roller-coaster auto trends post-COVID and the path ahead

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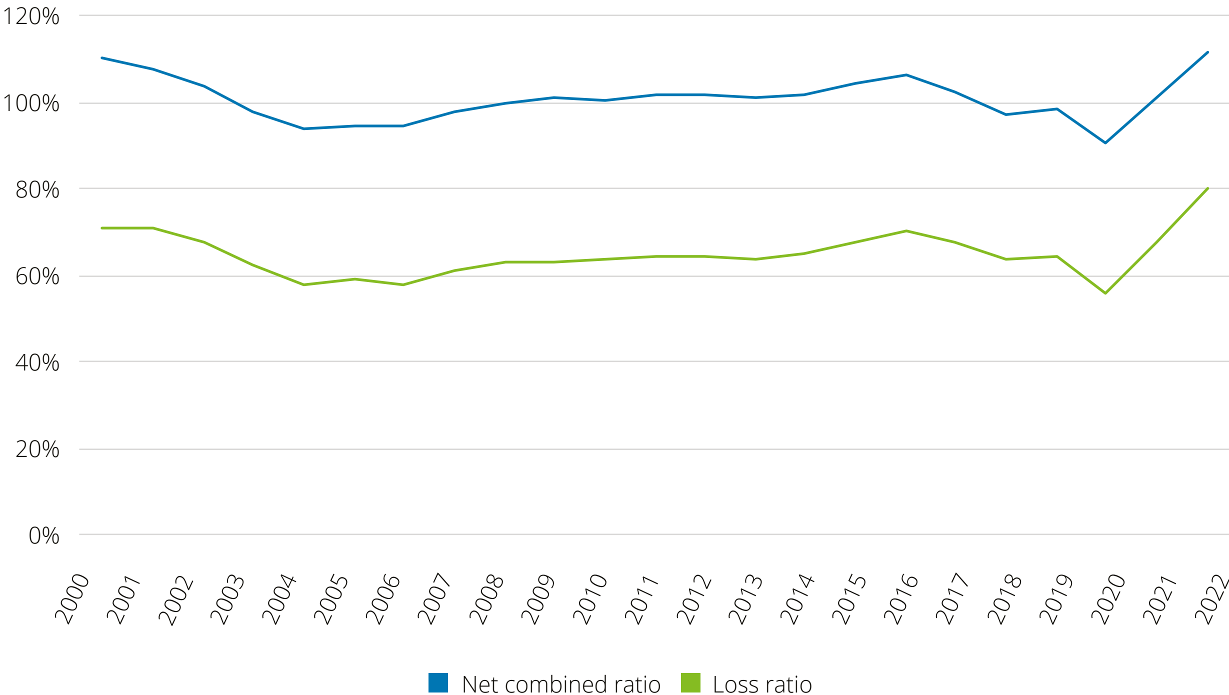
Introduction

The COVID-19 pandemic triggered a period of unprecedented uncertainty and volatility across the insurance industry. Within the property and casualty space, personal auto lines were among the most impacted, and the industry is still struggling to catch up to the rapidly growing need for rate as of Q3 2023. The 56% industry loss ratio that personal auto insurers enjoyed in 2020 gave way to a historically high 80% industry loss ratio in 2022, and the whiplash has left many insurers second-guessing their assumptions and racing to take rate. If the situation wasn't challenging enough, 2024 industry outlooks have turned increasingly pessimistic, indicating that relief to the tumultuous market conditions may still be out of reach.

Figure 1. Auto private industry recorded ratios

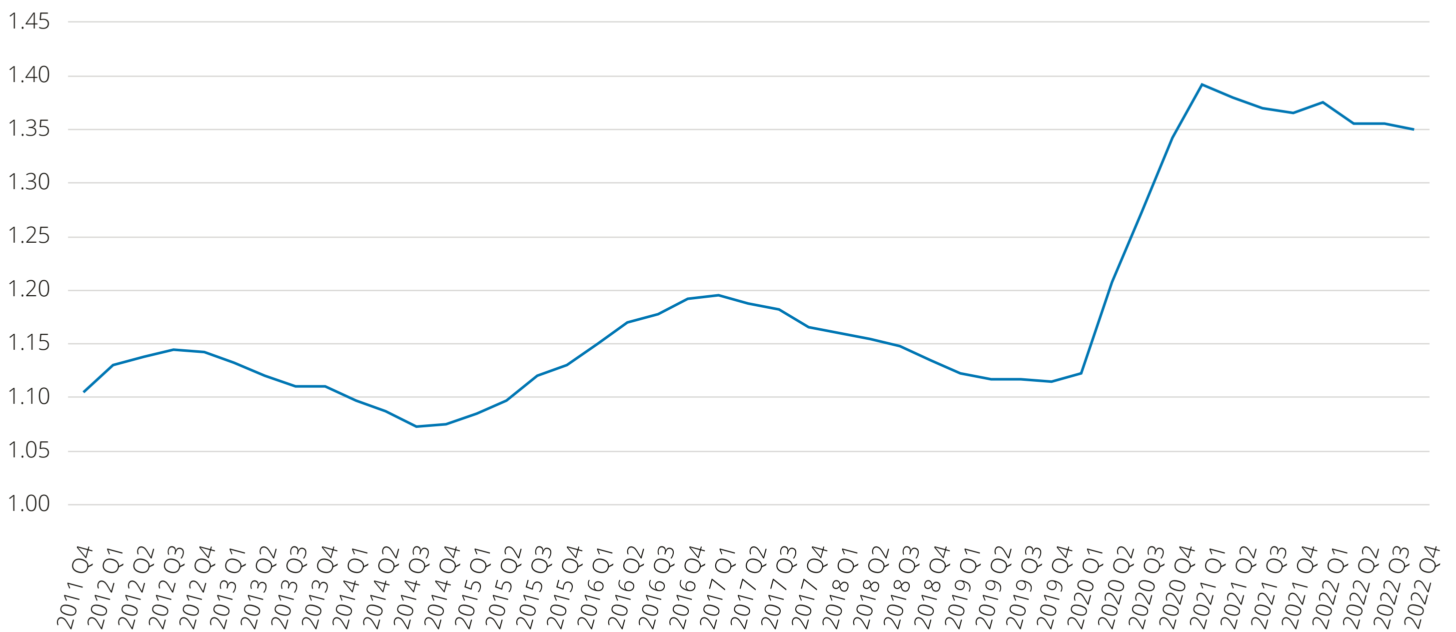


The road less traveled

The outbreak of the COVID-19 pandemic in early 2020 led to a sudden and significant decrease in the amount of time drivers were spending on the road. US vehicle miles in April 2020 fell 39% compared to the prior year. The reduction in exposure was so dramatic that nearly every personal auto insurer issued premium refunds to their policyholders amounting to more than $13 billion across the industry. Drivers have gradually made their way back to the road, and as of 2023, driving habits are in line with pre-pandemic norms, with 263.6 billion vehicle miles being logged in November 2023 compared to 260.3 billion in November 2019.

Unfortunately, less crowded roads through the pandemic years did not translate to a safer experience behind the wheel. Telematic data suggests that beginning in mid-2020 there was an alarming increase in how often drivers were traveling at speeds well above speed limits. Perhaps more concerning: Drivers have not let off the pedal as the pandemic era has subsided. Data shows that the rate of major speeding (driving 26 mph or more above the speed limit) has remained consistently high since mid-2020. These dangerous new driving habits have had a deadly effect on roadway fatality rates—data shows that 2022 logged 22% more fatalities per vehicle mile traveled than 2019. The impact of these changes in driving behavior is reflected in the mix of claims that insurers are receiving as higher-speed collisions increase the likelihood of bodily injury. Bodily injury (BI) claims as a percentage of total claim counts jumped from 26% in 2019 to 30% in early 2021. As of late 2022, the BI claims-mix percentage remained high compared to pre-pandemic norms at 27%—and is likely to remain elevated as long as aggressive driving behavior persists.

Figure 2. Quarterly weighted-average fatality rate per 100 million vehicle miles traveled (VMT)



The severity crisis

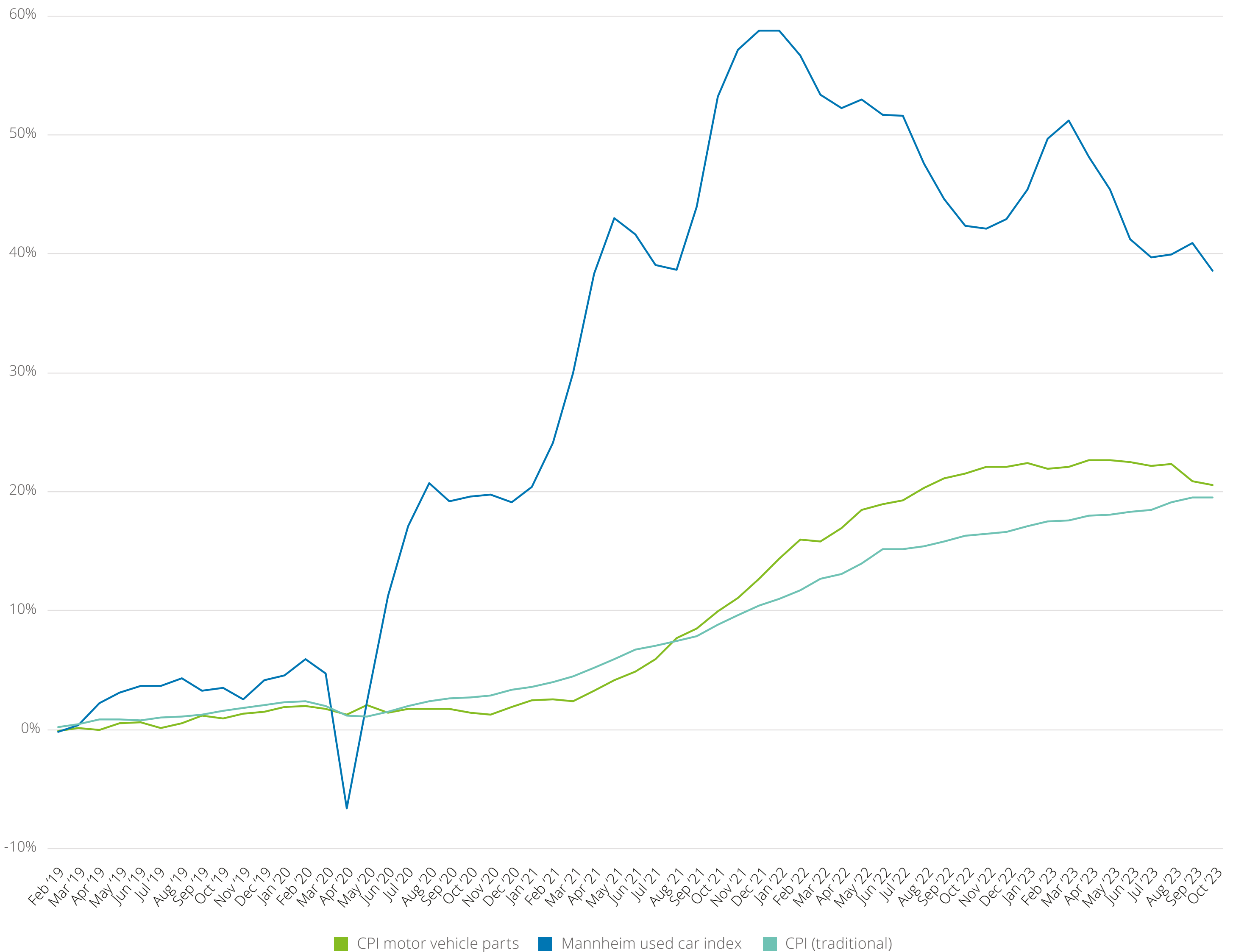
In the wake of the worldwide pandemic, a swelling money supply and supply chain struggles led to inflation surging at levels that had not been witnessed since the early 1980s. The Consumer Price Index (CPI)—the generally accepted measure of inflation—peaked at nearly 9% in June 2022 after hovering barely above 0% in April 2020. From December 2019 to December 2023, the industry saw the cost of motor vehicle maintenance and repair grow 31%, contributing to property damage and collision severity trend estimates reaching astonishingly high figures—as high as 20% in 2022. Inflation isn't the only culprit here, however; the increasing technical complexity of automobiles has led to carmakers requiring stricter adherence to original manufacturer guidelines for replacement parts and mandating that vehicle systems be scanned for faults after every repair. These tighter specifications have restricted the use of cost-efficient aftermarket parts during repairs and are forcing insurers to pay higher costs for original equipment manufacturer's replacement parts, further driving up severities.

To compound the troubles with property damage and collision severities, the cost of used vehicles has inflated at an even greater rate than auto body work since the start of the pandemic. The Manheim Used Vehicle Value Index estimates that as of January 2024, the cost of a used vehicle is 30.6% higher than in January 2020, despite a 10% drop since January 2023. Additionally, Manheim's latest revision to its forecast projects a 0.5% year-over-year increase in used vehicle values as of December 2024, suggesting that the pain of high prices for used vehicles may be long felt and that prices will not be returning to their prior levels anytime soon.

Bodily injury severities have also been problematic for insurers with the industry trend coalescing around the 10% mark in 2022. Inflation is again part of the story, but an increase in litigation rates is also playing a role, according to industry leader comments in recent filings. Analysis of industrywide liability claim closure rates reveals a slowdown in claim closures for calendar year 2022, suggesting that more attorney representation is holding claims open longer and driving severities higher. This uptick in litigiousness may be short-lived, however, as tort reform has become a hot-button issue in state legislatures. The industry has been closely monitoring the impact of Florida's House Bill 837, a tort reform act aiming to temper growing damage awards and increasing insurance costs, which took effect in July 2023.

The most notable changes driven by the law include repealing one-way attorney fees, adjusting the "bad faith" framework to benefit insurers, reducing the statutes of limitations for general negligence cases, and providing a framework to assist juries in awarding medical damages. These changes are set to affect new policies and claims after the effective date, which initial observation suggests has prompted an increase in early-year claims filings before the reform took place. While it is still too early to determine the full extent of the bill's effects, it is possible that it may result in heightened litigious activity in neighboring states as claimants aim to obtain more favorable verdicts before the passage of similar legislation.

Figure 3. Cumulative monthly percentage change in price



The path ahead

As severities soared following the pandemic, the industry was caught on its heels. The largest personal auto insurers took only 1.7% in rate increases on average in 2021, which, in hindsight, is well below the 5% bodily injury and 8% property damage pure premium trends measured by Fast Track. In 2022, the industry scrambled to catch up to runaway severity trends and increased rates an average of 9.5% but still fell far short of their overall rate need, resulting in a devastating 112% industry combined ratio in 2022.

If there was any optimism for a quick return to profitability in 2023, it was dashed as 2023 came to an end. Large insurers are reporting a need for additional rate in the double digits, and results reveal an industry average combined ratio for the 2023 calendar year exceeding 100%. Though broader economic inflation appears to be relenting—the December 2023 CPI measured at 3.4% in comparison to the 12 months prior—severity trends have so far remained stubborn. Frequencies have stabilized, but uncertainty remains around what direction litigation rates and claims-mix will take going forward.

The path ahead will likely be challenging for insurers but also presents a rare opportunity within the industry. The fierce rate disruption that is being felt by policyholders, combined with an economy turning more recessionary, is likely to drive an equally fierce reaction in the way of policy shopping. Those carriers who are able to deftly navigate these difficult circumstances may find themselves well positioned in the market for years to come.

Whether you are struggling with the economic turbulence or looking to modernize your department, Deloitte's specialists are ready to help. With extensive experience in all facets of the industry, our specialists have the skills and tools to help deliver results. Reach out to us to start the conversation today.

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