ANNUAL REPORT

2023 commercial auto liability statutory financial results

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30 April 2024

We are pleased to summarize key year-end 2023 financial results for U.S. commercial auto liability writers based on data available from S&P Global Market Intelligence. Milliman's composite of commercial auto liability writers includes 40 companies or groups of companies, each with 2023 commercial auto liability direct written premium of more than $250 million. This selected composite represents nearly 80% of the total commercial auto liability direct written premium volume for the industry in 2023. The metrics we reviewed show a slowing top-line revenue growth in direct written premium as several carriers have begun to reduce exposure, increasing adverse one-year reserve development, and upward pressure on the calendar year loss and defense and cost containment expense (DCCE) ratios.

Historically, commercial auto liability results have been problematic, as indicated by the consistent loss ratio deterioration within most accident years. This has been fueled in recent years by a continued marketing presence of the plaintiffs' bar concerning bodily injury claims stemming from large trucking events, social inflation driving settlement decisions, supply chain issues, and increasing third-party litigation funding, among other factors. All of these issues have had a significant impact on loss trend rates. As a result, one of the major issues facing the commercial auto liability industry is the answer to the question "What is the correct annual loss trend rate?"

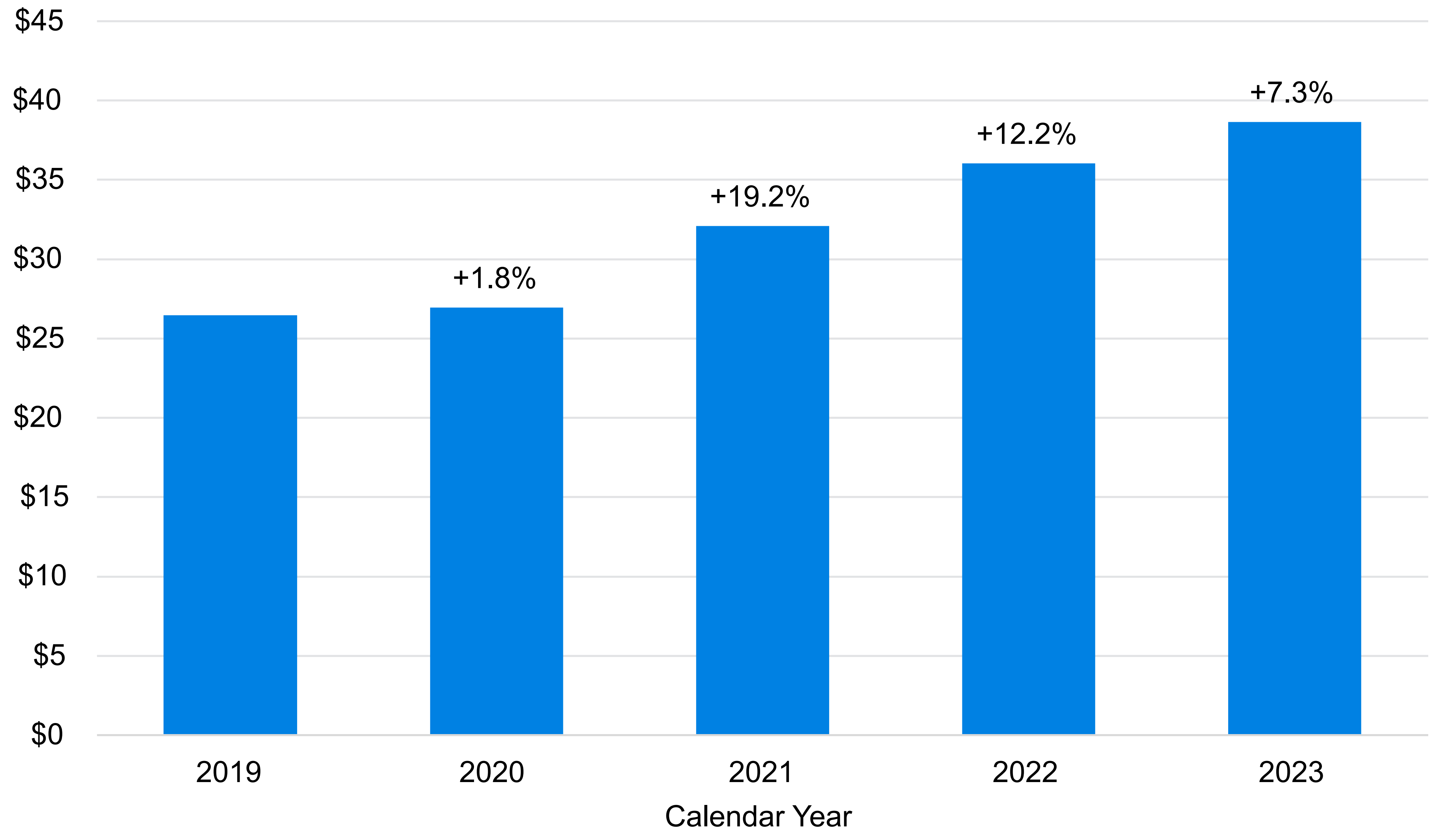
The industry has looked to remedy the situation by taking rate increases in recent years, but the overall increase in premium has not kept up with loss costs. After a brief reprieve in 2020 and 2021, primarily due to pandemic-related frequency decreases, the commercial auto industry appears as though it has returned to more of the same in 2022 and 2023. As a result, during 2023 several large insurers began to take drastic action by significantly reducing exposures or exiting certain markets altogether, in an attempt to boost profitability. The industry will certainly be keeping a close eye on how these decisions will impact the commercial auto liability landscape in 2024 and beyond.

It should be noted that the data for this composite of insurers has been aggregated to reflect any historical acquisitions, such that the historical data is on a basis similar to the current data.

Direct written premium (DWP) growth slows

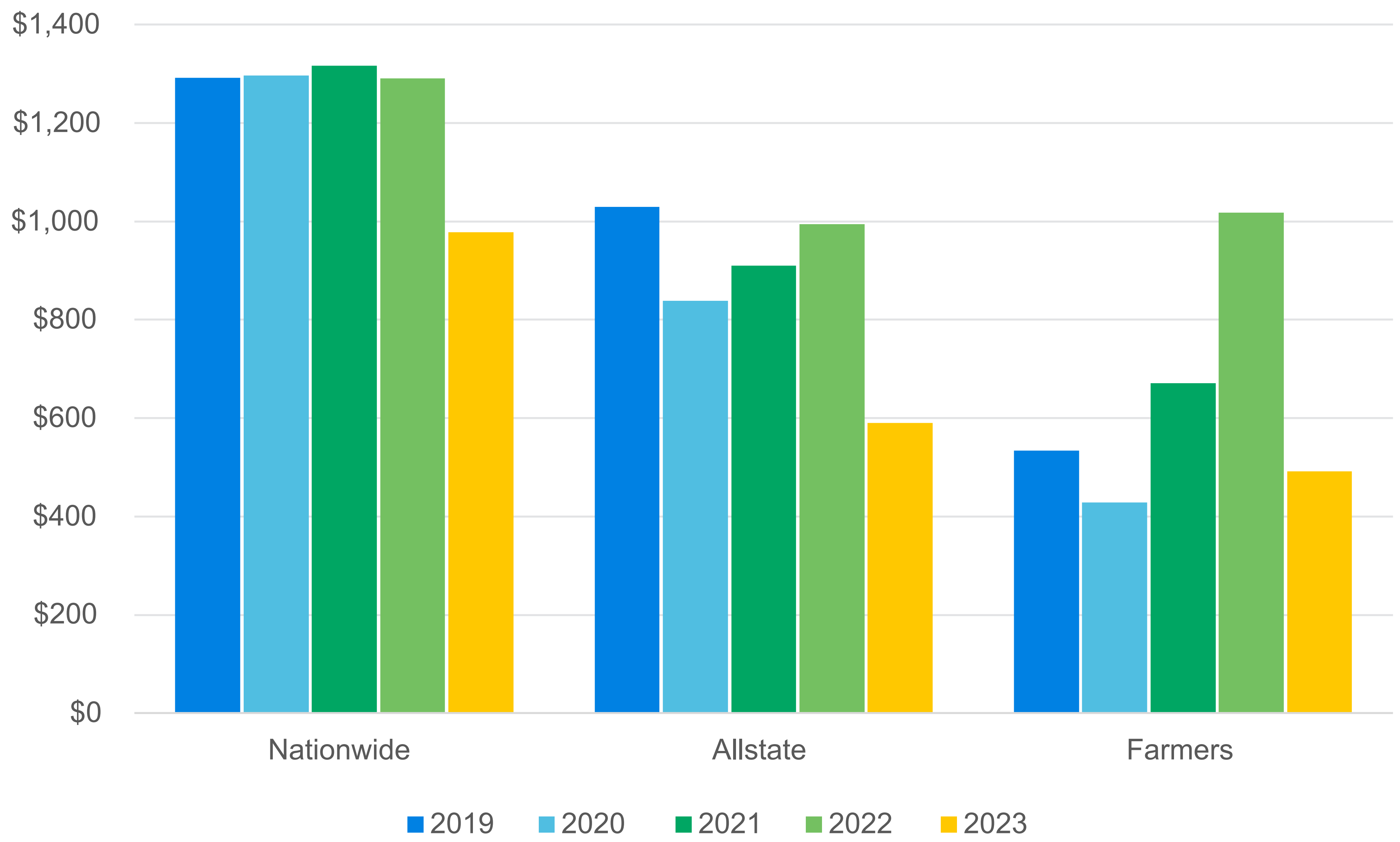
Commercial auto liability DWP for this composite increased to just over $38 billion in 2023, an increase of 7.3% compared to 2022. After two consecutive years of double-digit DWP growth experienced by this composite in 2021 and 2022, the 2023 DWP increase of 7.3% may have signaled a change. In 2023, for the first time in the last three years, the change in DWP for commercial auto liability did not outpace the change in DWP for all lines of business. Rate increases remained prevalent during 2023, but certain carriers appear to be reducing exposure as rate increases have not been able to keep pace with severity trends. Figure 1 displays the total commercial auto liability DWP for this composite, along with the percentage change from the prior year.

Figure 1: Top 40 commercial auto liability writers – direct written commercial auto liability premium ($ billions)



Three carriers within this composite (Nationwide, Allstate, and Farmers) experienced DWP decreases of approximately 25% or more, which aligns with recent press releases from these companies discussing strategies to withdraw their commercial auto business from several states, in what has historically been a difficult and unprofitable segment. It remains to be seen whether additional carriers follow suit in 2024 and beyond, or whether they will attempt to improve the underwriting results with further rate increases and re-underwriting. Figure 2 displays the total commercial auto liability premium for these three carriers over the last five years.

Figure 2: Nationwide, Allstate, and Farmers – direct written commercial auto liability premium ($ millions)

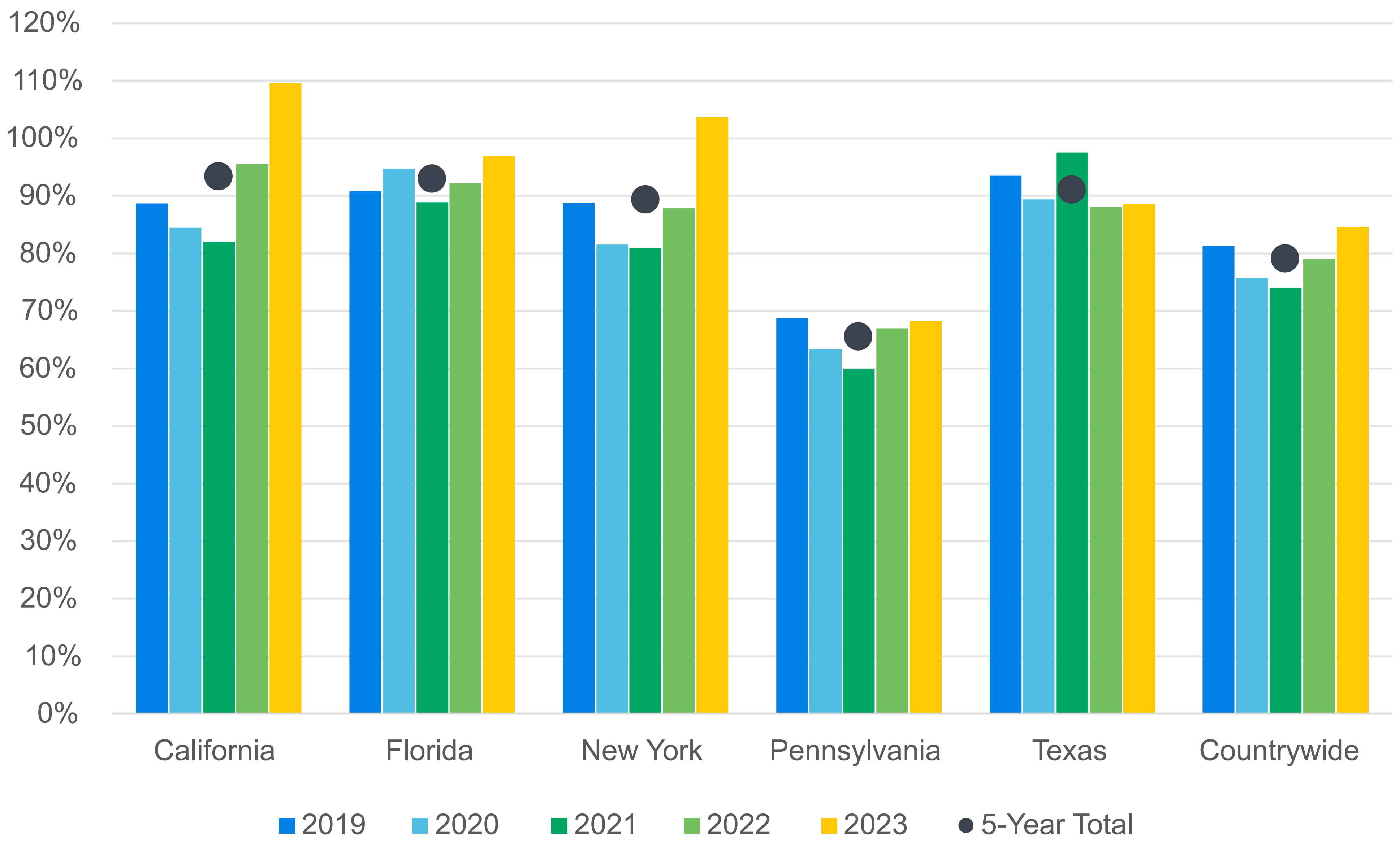


Upward pressure on loss ratios continues

Commercial auto liability remains a particularly difficult segment for many insurers, as loss ratios remain well above other lines of business. Social inflation continues to put upward pressure on severity and driver shortages have led to more inexperienced operators on the road. As a result, the 2023 countrywide commercial auto liability calendar year loss and DCCE ratio (CYLR) continued its upward trek from the pandemic-impacted low frequency years of 2020 and 2021.

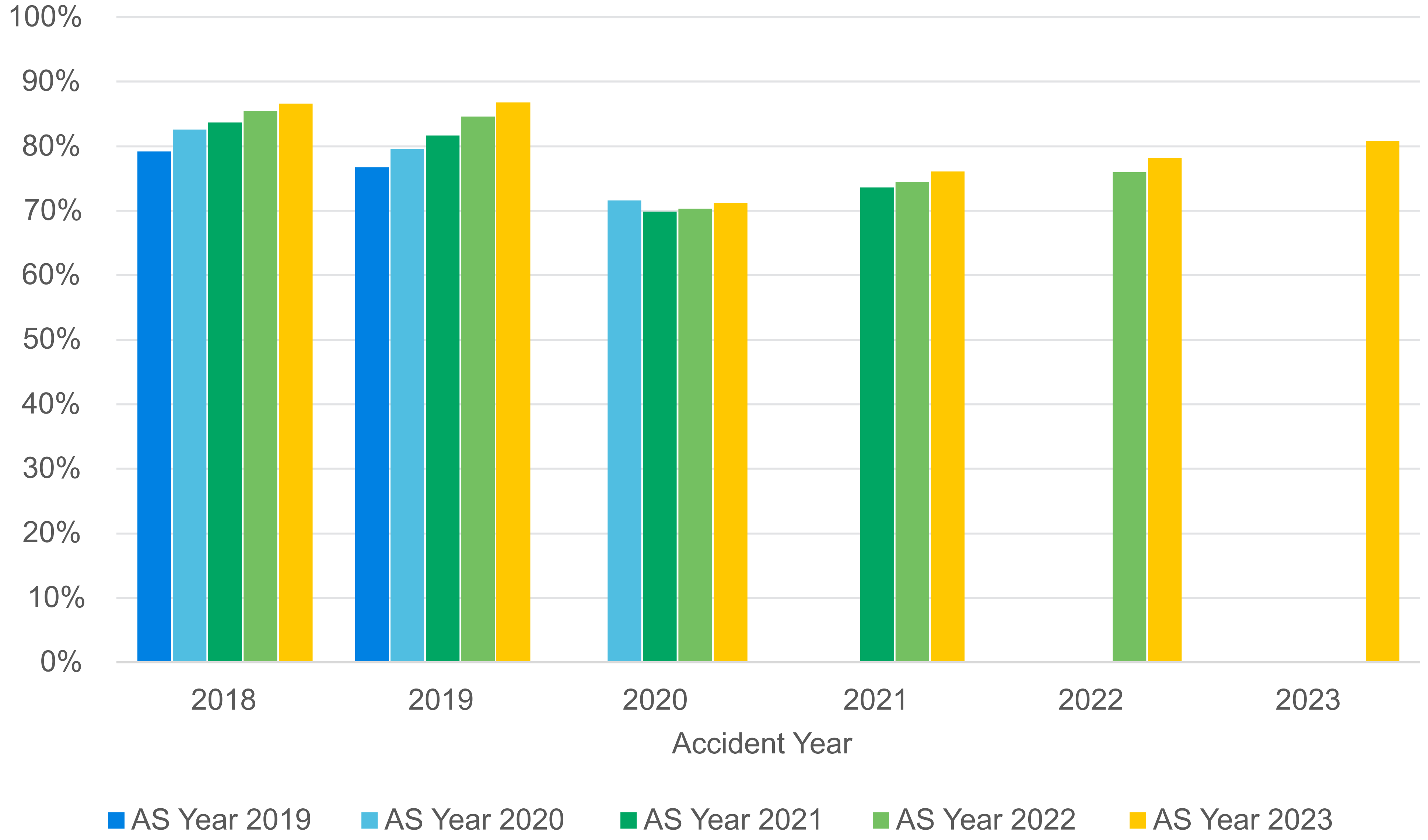
Figure 3 shows commercial auto liability CYLRs for each of the last five years on a countrywide basis and for several of the largest states. The countrywide 2023 CYLR for the commercial auto liability industry increased 600 basis points to 84.5%, the highest in the last five years. The median 2023 CYLR increased to 80%, with half of the composite between a 70% and 90% CYLR for 2023. This can likely be attributed to rising severities across much of the industry, as well as the return to pre-pandemic frequencies and increases in prior year reserves. Two states that experienced some of the most significant deterioration in the CYLR were California and New York, both of which saw the CYLR spike above 100% in 2023, while several other states experienced mid-to-high single digit increases in the CYLR, including Florida, Illinois, New Jersey, North Carolina, and Ohio.

Figure 3: Commercial auto liability total industry – calendar year direct loss and DCCE ratio



Due to the factors mentioned previously (i.e., social inflation, third-party litigation funding, etc.) commercial auto liability accident year net loss and loss adjustment expense (LAE) ratios have continued to develop adversely for each accident year back to 2016. For example, the accident year 2019 loss ratio, which was initially reported at 76.8%, has deteriorated to 86.8% as of year-end 2023. The initial accident year loss ratio increased in both 2022 and 2023, after the pandemic-related frequency declines favorably impacted the initial accident year 2020 and 2021 loss ratios. The accident year loss ratio for 2023 has initially been estimated at 81%, which is the highest in at least five years. The median accident year loss ratio for 2023 is 79%, with the middle 50% of carriers in this composite between 73% and 87%. However, it remains to be seen whether the higher initial accident year loss ratio in 2023 will result in less adverse development in future years, compared to what the industry has experienced in prior accident years. Figure 4 displays the development of the net ultimate loss and LAE ratio for 2018 and subsequent, but similar trends can also be observed in 2016 and 2017.

Figure 4: Top 40 commercial auto liability writers – accident year net ultimate loss and LAE ratio by annual statement year

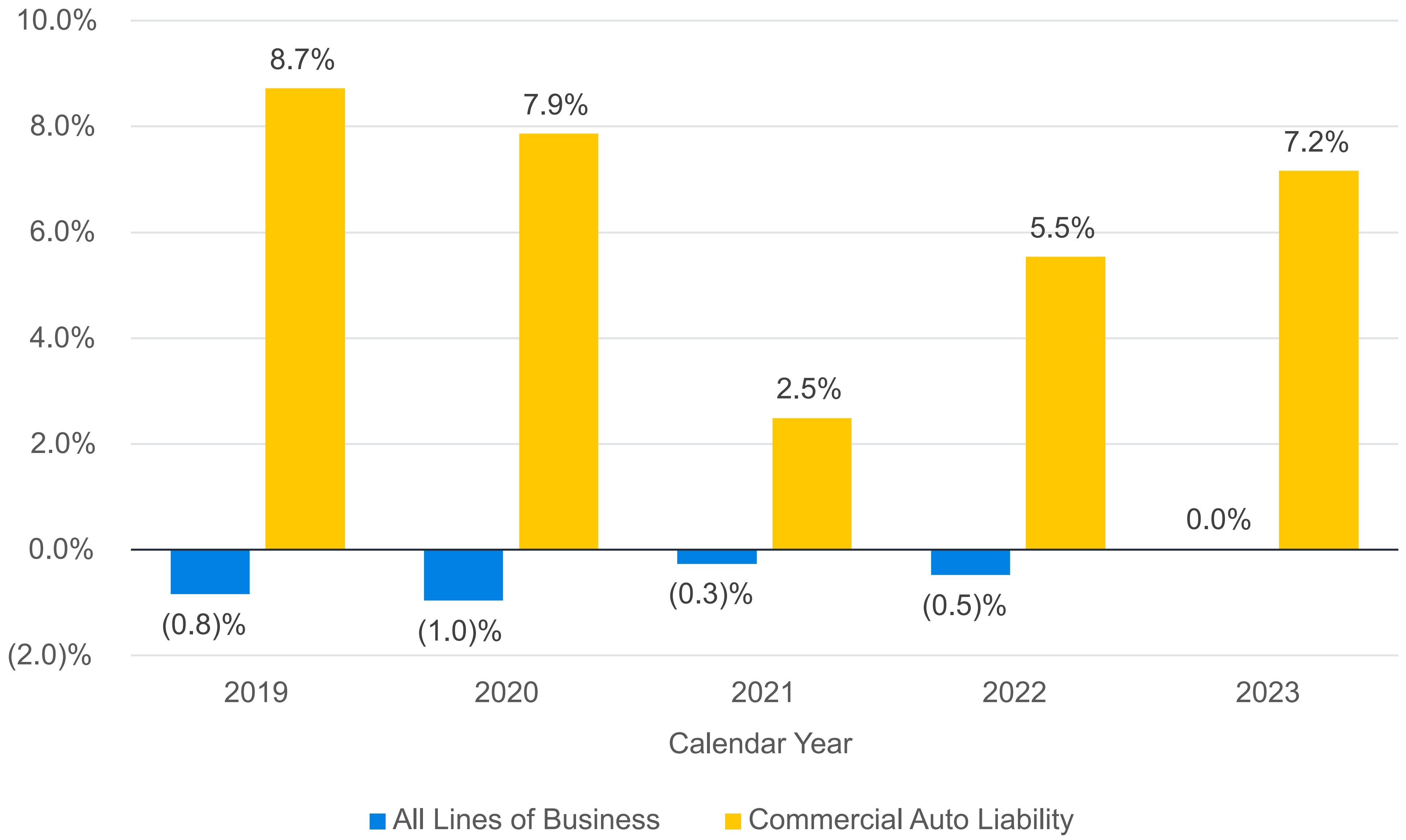


Prior-year reserve development remains adverse

This composite's ratio of one-year reserve development to net earned premium for all lines of business has been flat or slightly favorable for each of the last five years. However, the ratio of one-year reserve development to net earned premium for commercial auto liability continues to be adverse (see Figure 5). This composite saw an adverse one-year reserve development of 7.2% of net earned premium in 2023.

When pricing policies, insurers rely to some extent on experience from prior accident years, adjusted for loss development, loss and exposure trends, and historical rate changes. Given the adverse reserve development, to the extent companies used understated estimates of historical accident years to price policies in the more recent years, the resulting indicated rates would be inadequate.

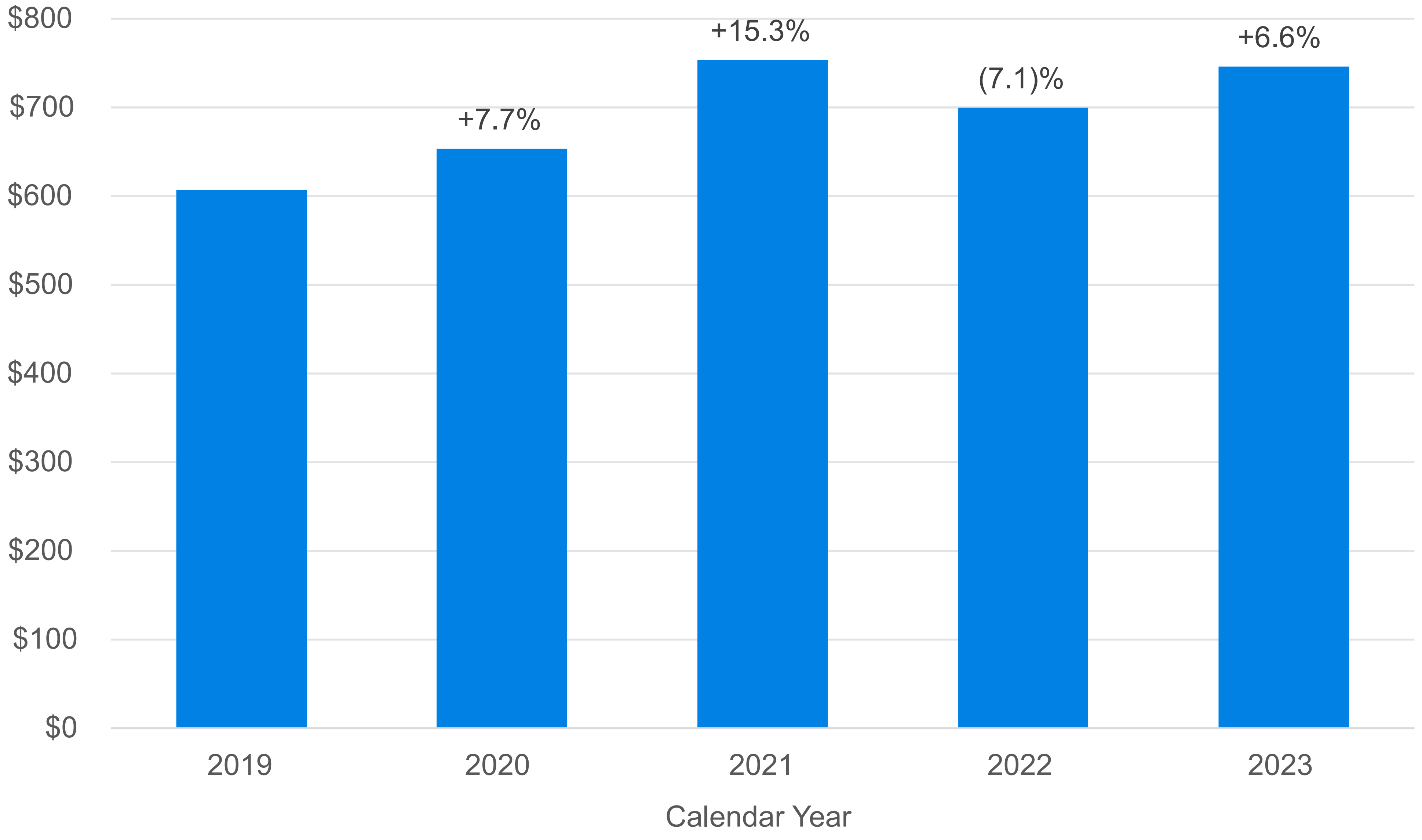
Figure 5: Top 40 commercial auto liability writers – one-year reserve development



Policyholders' surplus (PHS) recovers after 2022 dip

PHS for this composite increased by 6.6% in 2023, after a 7.1% decrease in 2022. The decrease in PHS during 2022 was primarily impacted by macroeconomic factors, such as rising inflation, that led to prominent levels of unrealized capital losses for the entire industry and increased underwriting losses from catastrophes such as Hurricane Ian. While commercial auto liability underwriting results did not improve in 2023, both realized and unrealized capital gains increased due to the rising financial markets, which helped PHS increase across virtually the entire insurance sector. Many of the companies included in this composite write multiple lines of business, therefore it should not be inferred that the change in PHS for this composite is a direct result of commercial auto liability experience. Figure 6 displays the total PHS for this composite, along with the percentage change from the prior year.

Figure 6: Top 40 commercial auto liability writers – policyholders' surplus ($ billions)



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