COVID-19 WINDFALL PROFITS ESTIMATED AT $100B FOR CAR INSURERS

Millions of vehicles are now parked in garages and driveways as people shelter in place, or worst yet, suffer crushing job loss. That means hundreds of thousands of fewer accidents and billions of dollars in claim dollars that won't be paid. Big-name insurance carriers will be the chief beneficiaries in this scenario, leaving consumers fighting for relief.

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Industry Backgrounder

Executive Summary

The coronavirus and the associated shutdown of the U.S. economy will dramatically reduce car insurance accidents. The impact began in mid-March with the "15-days to slow the spread" initiative and will continue until U.S. drivers are driving as much as they were in early March.

The impact of social distancing will soon become very apparent in auto accident statistics. Our projections are that the paid losses in 2020 could be as much as $100 billion less than in 2019. If this savings is passed through to customers, this $250 billion industry would shrink by $150 billion.

For consumers, this means there's significant opportunity to save money. This can easily be done by adjusting insurance coverage to account for new driving patterns. On average, consumers could save approximately $560 per vehicle. For those out of work or working from home, the amount could be even larger.

The impact on carriers will be two-fold. ValChoice expects that many carriers are hoping to see a substantial increase in profits due to reduced claim payouts. Other carriers will use this as an opportunity to gain goodwill through lower prices.

No matter how the auto insurance industry reacts, the outcome that's almost certain is that some companies will fail. In the long-term, less competition is bad for consumers.

The Analysis

Auto accident frequency is heavily influenced by traffic patterns. The strong majority of accidents occur during times of heavy flow and congestion. See chart 1.

Since mid-March 2020, tens of millions of people have either been added to the unemployment rolls or are working from home. Furthermore, virtually no one is going to social engagements, sporting events, or other optional activities that contribute significantly to traffic volume.

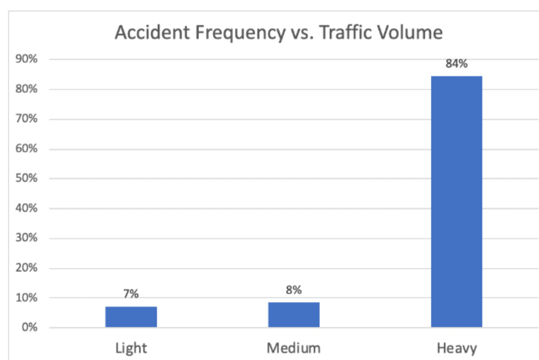

Chart 1 shows a relationship between accident frequency and traffic volume.

Assumptions Behind the Analysis

Key questions to be addressed in the assumptions include how quickly a recovery will begin, when the economy has fully recovered and after recovery will traffic levels be similar to traffic levels prior to COVID-19?

With regards to the rate of the economic recovery, a V-shaped recovery was assumed with full recovery by January 2021. However, with regards to traffic levels, a full recovery will not result in the same high level of driving as existed prior to the virus.

A full recovery with lower levels of traffic is best described by the colloquialism the “new normal.” The new normal is that workers and companies previously reluctant to embrace broadly available, and nearly free, technology that enabled working remotely. However, working remotely is no longer an option. It’s mandatory. Many may find this new normal preferable. If so, traffic volume increases will be less related to economic growth. Instead, more slowly moving factors such as population growth and housing density will become increasingly important in projecting traffic volume.

These assumptions led us to a model generally defined as follows:

- Light traffic through June 2020
- Medium traffic through August 2020
- Gradually ramping to traffic representing ~90 of normal by January 2021

Change in Insurance Industry Losses

Applying accident rates based on traffic flow enables projecting changes in the auto insurance loss ratio (the amount of money paid per dollar received in premiums collected) and the associated dollar value of the losses.

See chart 2 for a visual representation of the rapid decline and gradual growth back toward normal of insured losses due to COVID-19.

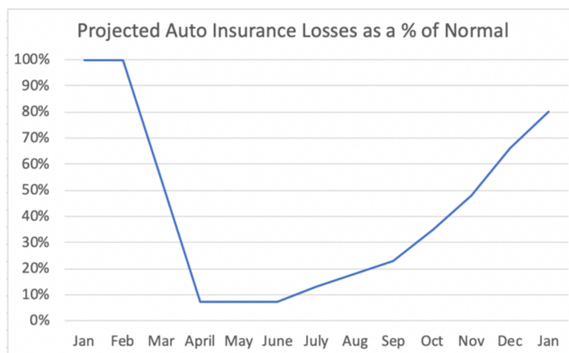

Chart 2 shows the rapid decline followed by the forecasted increase in auto insurance losses based on a reduced accident frequency.

What This Means for Consumers

More than ten million workers lost their jobs in the first two weeks of the 15-days to “slow-the-spread” initiative. Now that initiative is extended for 30 more days. Most likely, tens of millions more will be out of work during this time.

Additionally, tens of millions more workers are working from home. For most, this will be for a period of time lasting much longer than the “slow-the-spread” initiatives. The good news for consumers is that everyone who has changed their driving routine is entitled to a reduction in their car insurance price.

How much savings is possible?

The savings for individual consumers will vary depending on how much their situation has changed. Below are a couple common scenarios. While the amounts vary somewhat from individual to individual and carrier to carrier, the figures below are a well-informed estimates based on ValChoice having analyzed thousands upon thousands of insurance company rate filings across all 50 states. Any consumer can run their own estimates using the ValChoice car insurance calculator.

Scenario 1: Commuter driving more than 15 miles per each way to work. Their current insurance coverage is 50/100 liability with collision and comprehensive. This person is no longer commuting and estimates their new mileage is less than 3K per year. They need to make the following changes to their insurance coverage:

- Driving "for pleasure" rather than commuting
- Reduce the annual mileage to 3K*.

Savings = approximately 20%
Note: not all insurers use driver reported mileage for rating.

Modified scenario 1: Same driver as scenario above, plus the more aggressive modification listed below:

- If the vehicle is owned, canceling collision and comprehensive insurance is an option, maintaining the same level of liability coverage as prior to the coronavirus.

Savings = as much as 65%

Scenario 2: A family with two cars and a teenage driver. Both cars drivers commute more than 15 miles to work. Their current insurance coverage is 100/300 liability with collision and comprehensive. Now neither of these drivers are commuting. To maximize the discount, they need to make the following changes to their insurance coverage:

- Driving "for pleasure" rather than commuting, for both cars
- Reduce the annual mileage to the minimum level, for both cars*
- Make sure the drivers whom are most expensive to insure are assigned to the least expensive car to insure

Savings = as much as 35%
*Note: not all insurers use driver reported mileage for rating.

Scenario 2 modified: Same drivers as scenario 2 with the more aggressive modifications listed below:

- Cancel collision and comprehensive insurance and maintain liability If there's no loan or lease, the collision and comprehensive insurance is not required. In order to driver the vehicle, maintain liability insurance. The other vehicle can be parked. When parked, liability insurance can be canceled. Keep collision and comprehensive if there is a loan or lease, or you cannot afford to pay for repairs.

Savings = as much as 80%

How will insurers respond?

On April 6, 2020 some insurers began to voluntarily pass through limited savings. This is excellent and deserving of recognition. However, the savings passed through are significantly less than what the ValChoice models estimate the actual cost savings to be.

Separately, a few insurance companies were contacted by consumers to test responses on our behalf. Here are three examples:

Consumer #1: I would like to change my driving from commuting to recreational use.
Agent: We don't base premiums on mileage estimates anymore. We collect data from car service centers because when you get your oil changed, they record the mileage.

This was a deceptive misdirection. ValChoice knows this company does use mileage estimates. Also, the response did not answer the question about changing the use of the vehicle. Instead, the response redirected the conversation to an irrelevant, dishonest discussion about mileage.

Consumer #2: I would like to reduce my car insurance due not driving because of the shelter-in-place due to the coronavirus.
Agent: "I haven't heard of anything like that. If such a change is possible, the insurance company will notify you directly."
Consumer #2: Okay, can I change the use of my vehicle to "for pleasure?"
Agent: After looking into the policy, "yes." Roughly 10% savings.

Consumer #3: Contacted agent for carrier. No response at.

Consumers wonder, "who will help me?"

Some insurance companies working to help consumers is laudable. ValChoice anticipates that following the early announcements of passing through savings, more insurers will follow. However, not all companies will respond similarly. For many consumers, how your insurance company, or agent, responds depends on their corporate structure. The following are two key considerations:

Companies with shareholders have limited flexibility due to shareholder expectations on both revenue levels and profitability. To some degree, tradeoffs in these two metrics are possible without disillusioning investors. However, large drops in revenue, or profits, are alarming to investors and will cause concerns about future growth prospects. This is a scenario management teams do not wish to face.

Companies without shareholders have more flexibility because they do not need to reset the expectations of investors. However, that alone does not mean these companies will be accommodating. Instead, this depends on their financial position and willingness/ability to invest in growth.

The best way for consumers to think about this may be how to interpret a company's response when requesting a lower price. Here's a guide for consumers on how to interpret the agent's response, based on the sales channel used by the company:

- **Direct to consumer** – examples include: GEICO, USAA, Amica, Esurance, Progressive Direct. Whatever the person you contact tells you is a direct communication from the company. The person you are communicating with has no additional options for helping you, other than what they tell you.
- **Companies with captive agents** – examples include: State Farm, Allstate, Liberty Mutual. You likely have somewhat of a relationship with your agent, so you can expect personal sympathy. However, similar to the direct to consumers companies, they only have as much flexibility as the company offers them.
- **Companies with independent agents** – examples include: Many insurance companies use agents that represent multiple companies. These agents have maximum flexibility. Insurance companies will instruct them on what they're willing to agree to in terms of changes. However, if that does not fit your needs, these agents should be able to switch you to a company that will better accommodate your needs.

Should consumers move their business to another company?

There are benefits for consumers to by moving to another company. By law, insurance companies must refund the portion of an insurance policy that was not used at the time of cancellation. This gives consumers the opportunity to get a refund at their previous higher rate, then buy new insurance at a lower rate. The net effect of this is cash in the consumers pocket, at a time when cash is badly needed by many.

Summary

A disruption of this magnitude has never been experienced by the auto insurance industry. While this is welcome news for consumers in the short term, the longer term may be different. If companies fail, leading to accelerated consolidation, that means less competition. Less competition is always bad for consumers.

From a consumer perspective, keep the following point in mind. If your lifestyle has changed, changing your insurance coverage is a legitimate request. If your insurance company will not accommodate your request, that's a bad indicator about their willingness to support you in your time of need.

The good news is that consumers have the final say. If a company will not accommodate a consumer's request, the consumer can change to another company.