The Conning Commentary

Strategic Issues for Insurance Industry Executives

JUNE 2020

VOLUME 30, NO. #6

Earnings roundup, first quarter 2020

Property-casualty: Jekyll and Hyde

For property-casualty insurers, January and February were characterized by favorable economic growth, hardening commercial lines pricing, and strong growth in invested assets. March went in the opposite direction with an economic collapse, premium rebates, and turmoil in the bond and equity markets. This can be seen in the stock price graph below, indicating the market reaction to the impact COVID has had on property-casualty insurers.

In our review of the investor calls regarding first-quarter results, we noted several important themes:

- diversity in loss estimates arising from COVID-19
- expectations for continued firming in commercial lines pricing
- concern about business interruption exposure
- challenges to InsurTech
- adverse COVID-related effects on the investment portfolio
- broker preparations for the financial impact

COVID loss estimates

The WHO declared the COVID-19 outbreak a pandemic on March 11, less than three weeks before companies had to finalize their first-quarter 2020 financial results. Not surprisingly, there was a considerable range of COVID-related loss estimates depending on the business model of the company (insurance vs. reinsurance, personal vs. commercial, etc.). As these were initial loss provisions, we expect additional provisions in subsequent quarters and likely meaningful adjustments to these estimates.

Lloyd's announced that, for underwriting year 2020, it expects to pay between $3 billion and $4.3 billion in COVID-related claims. (These amounts could be higher if lockdowns stay in place through the second quarter.) Other companies that announced large expected loss payouts from COVID in 2020 include Munich ($865 million), Zurich ($750 million for the year), and Swiss Re ($476 million). Most of the claims are related to event cancellations/postponement, business interruption, and other policies that did not have pandemic exclusions. Munich and Swiss Re both had significant exposure to cancellation of the Tokyo Olympics ($500 million and $250 million, respectively), so the postponement of the Games to 2021 should have mitigated the losses for these companies.

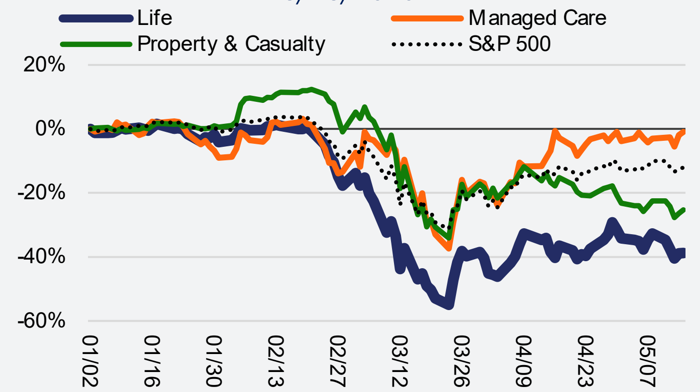
Several reinsurers posted large COVID-related losses for the first quarter of 2020. Hannover Re and Berkshire Hathaway announced losses of $245 million and $230 million, respectively, for COVID claims. AXIS, Everest Re, TransRe, and RenaissanceRe each posted pandemic-related losses of at least $100 million for the first quarter. The impact of these losses on the first-quarter combined ratios for the companies ranged from mid-single digits to more than 20 points.

Insurance companies with large COVID losses in the first quarter were Markel ($325 million, or 24 points on the combined ratio, for U.K. business interruption and worldwide event cancellation coverage) and AIG ($272 million, or 4.5 points, for travel, trade credit, and workers' compensation). Other companies that reported COVID-related losses or charges include Travelers ($86 million), W.R. Berkley ($67 million), Hartford ($50 million), and Argo ($26 million). For the latter group of companies, the impact of COVID losses on the combined ratios was de minimis.

Pricing expectations

Prior to the onset of the COVID-19 crisis, all commercial lines, with the exception of workers' compensation, were seeing renewal rate increases. Commercial property, D&O, and com-

Conning Insurer Stock Indices, 1/2/2020 through 5/15/2020



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mercial auto rates saw the strongest increases to combat loss trends and adverse loss development on prior accident years. Personal lines rate trends were more subdued. When the effects of the crisis on the economy began to emerge in the second half of March, there was heightened discussion in the industry about whether the crisis would stoke further rate-firming or arrest it. As the crisis deepened in April and May, the prevailing view was that commercial lines would continue to harden and personal lines would remain flattish to soft. Below we present comments from leading property-casualty insurers from their first-quarter earnings calls regarding rate-related trends through April.

Chubb reported 10.5% rate increases on North American commercial business, including major accounts, specialty, middle market, and small commercial. Middle market pricing was up by 5% to 6.5%. Travelers also reported commercial rate increases, with reported rates increasing by 6.2%, up more than one point from the fourth quarter of 2019 and more than 4 points from the first quarter of 2019, notwithstanding workers' compensation rate reductions. Travelers reported positive rates at about three-fourths of its middle market accounts. In its Select business segment, renewal rates were up by 1.6%, whereas in middle market renewal rates were up 6.6%.

The Hartford referenced "rigorous execution on renewal pricing and rate increases" with the integration of Navigators, compared to the second half of 2019. For the wholesale business, it reported up to 21% rate increases in the first quarter. CNA reported rate increases of 8% in the first quarter, up one point from the fourth quarter of 2019. Its specialty business had 9% rate increases, as well as tightening of terms and conditions. Liberty Mutual reported standard commercial lines rates, excluding workers' compensation, up 7.4%. Its middle market segment saw rates up 9.4%, excluding workers' compensation.

W.R. Berkley reported that rate increases began accelerating in March. Hanover reported core commercial rates up 4.6% and continued rate increases in specialty.

ProAssurance, a medical professional liability insurance specialist, reported renewal rate increases of 11% across its specialty segment, including 13% for physicians and 20% for health care facilities. It also reported strengthening rate adequacy in E&S lines for health care facilities business through improved terms and conditions.

The renewal rate environment in personal lines was milder than the firming trend in commercial lines. Prior to the outbreak of COVID, personal auto rates were flat to up low single digits. Homeowners rates were increasing on the order of 5%. The rate picture for personal auto changed in the wake of drastically reduced miles driven as the result of COVID-induced shelter from home initiatives. As reported in the May issue of *The Conning Commentary*, personal auto insurers are giving rebates of varying amounts to reflect the reduction in driving. These rebates effectively constitute rate reductions. The extent of the reductions will depend on the duration of the crisis and the timing of workers resuming commuting and pleasure-related driving.

Business interruption

As one of the key uncertainties relating to COVID-19 effects, business interruption coverage/exposure was a frequent topic on the first-quarter earnings calls. It was addressed by most commercial insurers and was also the subject of a number of analyst questions.

Both Chubb and Argo affirmed that they had written policies that included coverage for pandemic. For most insurers, that coverage was the exception and not the rule. Argo and others noted that most of that coverage was provided in international markets and carried sublimits.

With an opportunity to speak to a broad audience, insurers voiced the common refrain that broad attempts to expand coverage for business interruption by government action would have a devastating impact on individual companies and on the industry at large.

In the May 2020 edition of the *Commentary*, Conning estimated that a conservative assessment of the impact from any imposed retroactive BI coverage via regulatory or legislative demand at $138 billion per month—equivalent to 16% of industry surplus. A.M Best estimates that $633 billion of insurer surplus could be exposed to business interruption losses.

As noted by The Hartford, "[a]ny effort to retroactively rewrite these contracts, presume coverage or remove exclusions would threaten the very foundation of the insurance industry, the sanctity of contracts under our constitution and the principles of a free market economy. Doing so would threaten the ability of carriers to pay losses rising out of everyday-covered perils our customers will inevitably face in the months and years ahead."

Chubb was also clear about the threat posed by retroactively changing contract terms and conditions ("torturing the language on standard industry forms and try to prove something exists that actually doesn't exist") would be unconstitutional and a blow to our constitutional democracy. "... [P]reservation of that and the certainty of that in such uncertain times is paramount."

When discussing contractual protections in place guarding against large-scale COVID-based business interruption exposure, most insurers refer first to the requirement that property policies require direct physical damage to the property from a covered peril for coverage to attach.

Cincinnati Financial noted that it will rely exclusively on the underlying contract language in assessing COVID-driven BI claims, noting a pandemic/virus exclusion is unnecessary: "... because the virus does not produce direct physical damage or loss to property no coverage exists for this peril, rendering an exclusion unnecessary. For this reason most of our standard market, commercial property policies in states where we actively write business do not contain a specific exclusion for COVID-19 ..."

Most insurers, however, were also quick to point out the presence and the importance of the pandemic exclusion that is in place for the majority of business interruption-related contracts. CNA was clear in stating that, "… our property policies, whether issued in the U.S. or international, all have exclusions barring coverage for viruses. There are a very few policies where coverage may exist on small participations in our Lloyd's operation, but the total limit exposed is de minimis. So with respect to business interruption, our property policy exclusionary language does not provide coverage for COVID-19, and as such, we never collected premiums for it."

Challenges to InsurTech

InsurTech was mentioned less in the earnings results for first-quarter than in the past. The primary InsurTech news of the quarter was AIG was placing Blackboard, its internal InsurTech startup, in runoff, recognizing a pretax loss of $210 million. Blackboard was acquired by AIG in 2017 and had projected income of $50 million in 2020. While AIG put the business directly into runoff, it appears there may be a last-ditch effort by Blackboard management to secure outside financing and keep the firm alive.

Some of the prominent InsurTech startups, specifically those that write their own policies, announced some struggles due to the COVID-19 pandemic. Oscar Health announced it was laying off 5% of staff in April. Bold Penguin laid off about 25% of staff as the small business InsurTech saw a decrease in quotes due to pandemic-related closures. Similarly, Slice Labs announced a roughly 40% reduction in workforce. Finally, Metromile, a pay-as-you-drive auto insurer, announced significant layoffs as part of getting to a two-year runway of capital. While the Metromile business model may prove attractive during a period of reduced driving like what presently exists, lower driving has meant less premium incoming and further need to stretch capital.

Insurers did praise past investments in technology as being immensely useful during the COVID-19 pandemic. Travelers spoke to a 4.5× increase in virtual risk assessments due to third-party data remote-enabled technology. Regarding future investments in technology, there may be some near-term expense management and greater oversight on spending. However, insurers indicated that future investments will still be made, in technology, analytics, and talent, as the industry progresses through the pandemic. As the economy recovers from the pandemic, customers will return to InsurTech firms and technological investment will continue to be made by insurers. In the meantime, a focus on expense management will begin to alter the makeup of the InsurTech ecosystem.

Adverse COVID-related impacts on investment portfolios

More time on the conference calls centered around impacts on the liability side of the balance sheet from increased claim activity, but the negative effect on investment portfolios was highlighted as well. Insurers noted the negative effect of and from widening credit spreads in investment-grade and high-yield bond portfolios.

The principal source of 2020 investment losses was attributable to the decrease in the fair value of the equity portfolio during the period as COVID-19 caused unprecedented volatility in the capital markets.

Also, insurers noted actions to increase liquidity to offset the expected decrease in premium receipts due to COVID-19, including the effect of the billing relief provided to policyholders.

Brokers prepare for impact

COVID-19 was heavily discussed in brokers' first-quarter earnings calls as well, with most saying that unfavorable results are coming—but they do not know how unfavorable. With economic uncertainty and a weakened revenue outlook, brokers have been getting ahead of the curve by cutting expenses. Aon vowed not to lay off workers during the pandemic, but did take serious cost-cutting measures by cutting salaries. The majority of the firm's employees saw reductions of up to 20% to their salaries; however, executive salaries were reduced 50%. The firm also noted that 30% of its employees will see no reductions. Other expense-cutting actions from Aon include managing vendor spending and pausing share buybacks, mergers and acquisitions, and discretionary spending.

Other brokers noted Aon's measures as drastic, although the majority noted some form of expense-cutting. Arthur J. Gallagher adjusted its expense basis down $50 to $75 million a quarter by eliminating discretionary spending, reducing travel and entertainment expenses, limiting temporary work, increasing use of its center for excellence, and hiring and wage freezes. AJG did note plans to furlough its workforce in areas where business has declined significantly; however, it expected this to affect less than 4% of its global workforce. Willis Towers Watson noted it would not be following Aon's footsteps of salary cutting despite its pending merger. Instead Willis implemented hiring and traveling freezes in addition to reductions to its variable cost structure for discretionary spending and capital expenditures.

Marsh pledged it would not make job cuts related to the pandemic and suggested it would not reduce pay to cut expenses. Instead Marsh has made efforts to cut expenses by halting nonessential expenses and reducing capital expenditures. The broker did note that reductions to the firm's bonus pool may be required in order to protect earnings.

While expense reductions were implemented for the majority of the brokers in the first quarter of 2020, most have not seen the true impact of this pandemic yet. Arthur J. Gallagher noted revenue growth saw 3% of unfavorable change in revenue growth due to COVID in its first quarter. Even so, through April, new business remained strong and retention was up for this broker. CEO J. Patrick Gallagher stated the firm is heading into uncharted territory and expects property-casualty exposure units to decrease.

Brown & Brown anticipates the third quarter of 2020 to see the largest impact on performance due to COVID. It expects negative organic growth in the second quarter due to the high unemployment rate. Looking forward, Brown & Brown expects new business to slow, but anticipates retention will increase. John Haley, Willis Towers Watson CEO, noted the pandemic did not have an impact on its first-quarter results, although expects the negative economic impact to hit revenue and results for the remainder of 2020. Marsh also noted strong performance in the first quarter despite the pandemic, but expects a modest decline in its underlying revenue for the full year.

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Life-annuity: preparing for recovery

The first-quarter 2020 earnings calls of life-annuity insurers presented a picture of an industry preparing for recovery. COVID-19 and the economic turmoil it caused occurred toward the end of the first quarter. As a result, overall results for the quarter were mildly positive. However, that turmoil did have an impact, and life-annuity insurers responded in several key areas. As 2020 develops, we see life-annuity insurers preparing for recovery. That recovery is predicated, in part, on the relatively strong capital position of the industry and the adjustments made during the prior crisis.

The graph on page 1 shows life insurer stock performance for 2020.

The calm before the storm

The economic turmoil created by COVID-19 began in earnest in mid-March 2020. While that turmoil has been significant, its timing had less impact than if it had occurred closer to the beginning of 2020.

Reviewing the first-quarter 2020 earnings releases and calls of those insurers found that their aggregate GAAP net income rose 106%, from $5.0 billion in the first quarter of 2019 to $10.3 billion. That growth was driven by Brighthouse Financial and MetLife, which reported a combined net income of $9.4 billion for the first quarter of 2020, driven primarily by net derivative mark-to-market gains on the hedging programs used to manage variable annuity risk. As a result of significantly lower equity markets and lower interest rates, the value of those hedges increased. However, under GAAP accounting, the corresponding liabilities are not reflected at fair value, and thus are less sensitive to market movements.

That said, a total of nine companies did report positive financial results for the quarter. However, aside from Brighthouse Financial and MetLife, only American Equity Life and Ameriprise reported an increase in net income over the first quarter of 2019.

In terms of policy premiums, eleven of the companies reported higher policy premiums in 2020 than for 2019. Overall, the 17 companies we analyzed reported a 3% increase in policy premium.

Net investment income was lower, in aggregate, by 13%. That decrease was driven by Athene and Great-West. Both companies reported net investment losses for 2020. Athene's loss was driven by mark-to-market losses on its derivatives, while Great-West experienced losses on its non-U.S. investment portfolios. Excluding those two companies, the remaining 15 insurers had a 9% increase in net investment income in the first quarter of 2020 compared to the first quarter of 2019.

Insurer capital positions were also strong as the economic turmoil began. That said, some companies reported lower RBC ratios for the first quarter compared to year-end 2019. CNO Financial's RBC ratio was 406% at the end of the first quarter, a slight decrease from 408% at the end of 2019. FBL's RBC ratio was 525% at the end of the first quarter, lower than the year-end, but expected by management because of the dividends to shareholders. American Equity Life's RBC ratio for the first quarter increased 5 percentage points from year-end 2019 to end at 377%. Companies also reported significant capital and lines of credit. Principal, for example, reported it held $3 billion in cash and liquid assets as well as $1.7 billion of excess capital and access to contingent capital facilities. Athene had $2.7 billion of excess equity capital, $7.5 billion of deployable capital, and $900 million of preferred equity capacity.

Weathering the storm

As COVID-19's economic turmoil took hold, insurers began to adjust operations and investments. While there was a negative impact on assets, hedging programs worked as designed. In addition to hedging, insurers also discussed their results of modeling the mortality impact on their business. Insurers deployed digital distribution solutions as well as adjusted underwriting.

During earnings calls, management teams discussed their exposure sectors under pressure from COVID-19. Ameriprise, for example, was not exposed to airlines and specialty retail. Brighthouse provided detail on its exposure to energy, retail, leisure, metals, autos, and airlines. One sector that drew attention was CML (commercial mortgage loans). CNO reported it had approximately 6.7% in CML, which was underweight compared to peers. It had an additional 9% in RMBS (residential mortgage-backed securities).

Insurers with significant annuity blocks also described how effective their hedging programs were in managing annuity risks. Prudential, for example, described that, during the first quarter, its variable annuity hedging performed extremely well with a 99% effective rate that offset increased VA liability. Ameriprise reported its hedging program also had a 99% effective rate. Lincoln National reported that its hedging program covered over 95% of the changes in the hedge target during what was the most volatile quarter it had ever seen.

Globe Life is estimating 2,500-3,000 deaths with a $25 million impact. Brighthouse estimated an adjusted earnings impact of approximately $70 million after-tax for every 100,000 COVID-19-related deaths in the U.S. Primerica estimated $5 million in COVID-related claims, net of reinsurance. Lincoln National did not see many COVID-19 mortality claims in the first quarter, but expects an increase in the second quarter.

In terms of operational adjustments, all insurers were on a work-from-home basis for their staff. For some of the insurers, digital distribution was already a significant part of their business. Primerica, for example, reported that 95% of business transactions were electronic before COVID-19. Prudential introduced a fast track automated underwriting process for COVID-19-related claims, new mobile apps, and chatbots, and expanded the use of electronic signatures across its businesses.

Not all distributor support was technological. In early April, American Equity announced prepayment of $30 million in deferred commissions to over 2,700 of its producers to help them manage their small business costs. CNO introduced financial support programs for exclusive agents with business disrupted and livelihood affected.

Another key adaptation involved changes in underwriting. Primerica, for example, switched its paramedical visits from at-home collection to at clinics. It also promoted its accelerated underwriting TermNow product with up to $300K face amount. The result was an increase from it being 65% of U.S. sales volume to 75% of volume.

Preparing for the rest of 2020

During their earnings calls, management teams explained their initiatives and outlook for the remainder of 2020. Many stated that the negative asset impacts are “temporary” and will improve as the year progressed. Capital management and liquidity would remain a key focus, with some insurers taking the opportunity to raise capital. Part of the capital management strategies will include selective deployment of capital for M&A transactions.

As the economy stabilizes and recovers, insurer assets should also recover. Athene’s management, for example, believes that its first-quarter asset decreases were temporary and expects its alternative net investment earned rate may be close to breakeven for the full year of 2020. While looking for a recovery, many insurers discussed the results of stress tests on their investment portfolio. Those results indicated that their capital position was strong enough to withstand the stress from a severe-case scenario.

Another key capital management tactic by many insurers paused share buybacks. Globe Life paused its buyback program and may start up again in the third quarter. Brighthouse suspended repurchases. MetLife paused its buyback program. Principal paused its share repurchases in early March as the pandemic emerged.

Along with pausing share buybacks, M&A activity is likely to slow in 2020. That said, companies such as Prudential will continue to dispose of noncore businesses. At the same time, insurers with strong excess capital levels, Athene most noticeably, announced they will be selectively looking for acquisition opportunities.

Some insurers are taking advantage of current market conditions to issue debt. Between March 1 and May 28, six insurers issued $5.9 billion of debt. Those companies are identified in the accompanying table. In addition to issuing debt, insurers with access to FHLB stated their intention to further access that for spread investments. For example, Midland National Life executed $800 million in borrowings from the Federal Home Loan Bank of Des Moines in March to provide a source of additional liquidity should COVID-19 continue to disrupt financial markets.

A reason for cautious optimism

While the economic turmoil from COVID-19 has disrupted life-annuity insurer operations and financial results, the earnings calls contain reasons for cautious optimism about the industry’s future performance. First, capital was and appears to remain strong. Yes, there will be a hit to RBC as there was in 2009 due to asset downgrades. However, provided the economy stabilizes, insurers appear to believe the hit will be manageable as the risk management lessons learned after the last economic crisis are applied. Adjusting to a work-from-home environment has spurred the roll-out of more digital technology. This should help the industry reach younger consumers who may prefer to interact with their product and service providers that way. Even as the industry adapts to a post-COVID environment, one remaining issue remains: the continued low interest rate environment. Insurers need to balance investment risk against investment return. This may prove increasingly difficult over the short and perhaps medium term.

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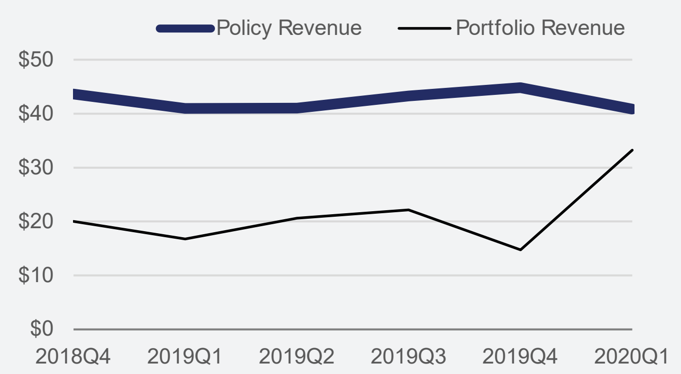
Life Insurer Debt Issuance, 3/1/2020 to 5/28/2020
$ in millions

Insurer	Amount
Prudential Financial	$2,000
Aflac	1,057
MetLife	1,000
Lincoln National	800
Brighthouse Financial	615
Unum Group	500
Total	**$5,972**



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Health insurers: unscathed

With first-quarter earnings now reported, health insurers saw results that were relatively unscathed by COVID-19 due to the timing of events caused by the virus. Nationally, most shutdowns began in mid-March. However, based on April data, insurers have begun to see larger impacts of COVID. This pandemic has forced these public insurers to reassess their earnings guidelines, cost impacts, membership, telehealth, as well as what the future could hold.

Year-to-date through May 15, Conning's managed care stock index is down only 1.0%, compared to the -12.1% of the S&P 500 during this same period. This stock performance is driven primarily by three companies. The top-performing companies are Molina Healthcare (up 36.0% year-to-date through May 15), Centene (up 11.0%), and Humana (up 9.6%). These companies have a larger share of individual or Medicaid premiums as a percentage of their total business and have seen their stocks perform better than those with larger group comprehensive blocks of businesses.

Updated earnings guidelines

Because of the current environment, health insurers addressed their 2020 full-year earnings estimates. Based on a multitude of factors, health insurers have either maintained their 2020 earnings guidance, improved guidance, or withdrawn certain guidance levels. Factors such as unemployment, line-of-business memberships, lowered investment income, as well as COVID-19 costs, have caused companies to update or remove forecasts. Centene raised its 2020 total revenue guidelines from a range of $104.8 to $105.6 billion to $110.0 to $112.4 billion. This increase is due in part to the current economic environment, as the company forecasts an increase in membership. "We have seen early evidence of membership growth in April driven primarily by states suspending eligibility redeterminations and special enrollment periods for Marketplace businesses in some states." Despite the increase in revenue growth, other factors such as COVID-19 costs and lower investment income has kept the company's adjusted EPS (earnings per share) at the same level between $4.56 and $4.76.

Membership changes

An insurer's main lines of business will play a large factor in membership growth over the next few months. With more than 36 million people filing for unemployment in the past eight weeks and an unemployment rate of 14.7% in April, a shift from commercial employer plans to Medicaid and the individual marketplace has started. Insurers are forecasting increases in their Medicaid and individual marketplace membership. Centene Chairman, President, and CEO Michael Neidorff noted during his prepared remarks: "We expect economic impact and resulting unemployment to drive increases to members. These increases will be partially reversed as and when the economy reaches the recovery stage." With these increases in membership comes an increase in revenue. Later in the call, Executive VP and CFO Jeffrey Schwaneke stated: "Second, as a result of the higher unemployment rate in the U.S., the suspension of eligibility redeterminations and our product mix, we are increasing our total revenue guidance by an additional $4 billion at the midpoint, bringing our total guidance increase to $6 billion at the midpoint … We have seen early evidence of membership growth in April driven primarily by states suspending eligibility redeterminations and special enrollment periods for Marketplace businesses in some states. However, we are also conscious that some of these trends may lessen significantly as economic conditions improve."

While Medicaid and individual marketplace enrollment are forecast to increase, due to layoffs and furloughs, group membership is expected to decline. In Humana's first-quarter call, CFO Brian Kane noted: "Through March, we are on track to achieve membership targets, but now anticipate COVID-19 headwinds will be challenging for this segment, including potential small group health plan terminations and large group workforce reductions, primarily driven by the duration of the social distancing restrictions across the nation and the speed of recovery and reentry … We are closely watching how unemployment trends develop, differentiating between layoffs and furloughs, as furloughs enabled by the federal payroll protection program resulted [in] employees generally continuing to receive health coverage through their employer."

Because of the current economic effects of COVID, insurers are working with employers in providing them assistance during these hard times. Companies such as Humana are providing extended grace periods for premiums for those companies facing financial hardships, waiving certain active work requirements to help maintain coverage, as well as working with small businesses in navigating the CARES Act and Paycheck Protection Program.

COVID-19 cost impacts

At this point, the total cost estimates for COVID-19 are unknown. At this point, it is hard to pinpoint how long and how much the virus will cost insurers. It is also hard to estimate hospitalization costs, as they have ranged wildly on a case-by-case basis. In Molina's earnings call, the company noted that, through April 27, 950 members were hospitalized for COVID-19 and, based on the early data, "there is no statistically credible cost per episode yet." Joseph Zubretsky, Molina President & CEO, noted: "We have 5-day stays, and we have 1-month stays. We have people in the ICU on ventilators and people that go in and go out. Cost[s] range from $10,000 per episode to $100,000 per episode … With only 1,000 data points … it's hard to draw any statistical conclusions."

Other unknown costs include the reduction in elective procedures. As levels of COVID remain high and the public is unwilling or unable to go in for elective procedures, health insurers will see a large reduction in elective procedure payments. John Gallina, Executive VP & CFO at Anthem, stated during the company's conference call that "we estimate that approximately 30% to 40% of our annual medical expense is related to deferrable elective procedures. As a result of deferrals, we currently expect the second quarter MLR to be well below historical levels but expect an elevated MLR in the second half of the year as elective procedures return." Depending on whether elective procedure deferrals continue through the second half of the year, this could also affect insurers in marketplaces and MLR (medical loss ratio) rebates. When asked about the potential for MLR rebates, Mr. Gallina noted: "in our individual line of business, we have earned above target margins in both 2018 and 2019, and we expected a normalization of that to occur—of our margins to occur here in 2020. So obviously, regardless of the length or the recovery of the COVID situation, I think individuals are going to have MLR rebates under any circumstance."

Telemedicine

Social distancing has affected how individuals see doctors. While in-person visits to doctors have decreased drastically, the use of telemedicine has replaced some routine doctor visits. In his prepared remarks, Larry Merlo, President & CEO of CVS. noted that "Utilization of telemedicine for virtual visits through MinuteClinic is up about 600% compared to Q1 '19 ... Aetna is seeing about 60,000 telehealth engagements on a daily basis."

Cigna has also seen an increased use of telehealth. President and CEO David Cordani stated: "So with telehealth, [it wasn't] that long ago that I think we as a society would be viewing telehealth as a small slice of triage intervention. And the COVID-19 epidemic is reinforcing to us, it could be a larger portion of an overall integrated or coordinated health care offering. And we see that as a big part of both today and the future." When asked about the future of growing telehealth by partnering or bringing capacity in-house, Mr. Cordani noted "we've co-developed telehealth capability with some of our more advanced value-based health care partners in certain markets ... Bigger picture, expect to see us be oriented around, at a minimum, the IP or intellectual property. The data, the data management, the data algorithms, the predictive capability to deliver the personalization and the clinical quality, we're going to be more oriented around that and then open architect it to own some and then partner with some in very different ways to be able to bring it to marketplace to offer the respective choice."

Increase in liquidity

As COVID ramped up in the United States, health insurers increased their liquidity by borrowing or issuing debt and commercial paper to increase their cash position. CVS issued $4 billion in bonds in March and has access to over $5 billion in cash and short-term investments, as well as $6 billion available by issuing commercial paper. Humana increased its liquidity in March with the "issuance of $1.1 billion in senior notes and a $1 billion draw under our 1-year term loan bank commitment we have in place."

What does the future hold?

With many unknowns, it is difficult for health insurers to develop pricing for 2021. Dirk McMahon, CEO of UnitedHealthcare, comment on the company's 2021 pricing. "We're closely monitoring the emerging COVID-19 information, including things like the claim experience from our members who have been diagnosed with the disease as well as other procedures. We're going to continue our commitment to pricing to our forward-looking costs, including estimates of things like significantly increased testing costs as well as, hopefully, the cost of the vaccine. Our view of the 2021 cost will continue to evolve as we learn more about the virus."

Summary

With so many unknowns still up in the air regarding the virus, it is hard to predict where we will be in one week, one month, or one year from now. However, as we continue through this pandemic, health insurers are processing and analyzing more information regarding COVID-19 every day. While other external factors such as the 2020 election and regulatory factors will still play a factor in the industry, COVID continues to be the dominant factor in the industry.

Daniel Erickson

Conning's New and Upcoming Releases

ANNUAL—2020 Managing General Agent & Program Market

The managing general agent (MGA) market accounts for a growing share of both commercial and personal lines premium spread over an increasingly large number of insurers. This sector continues to be at the forefront of product, technology, and business model innovation. The MGA structure is typically the business model that InsurTechs choose, and fronting arrangements with insurers are expanding. Using industry-filed data from insurers, as well as Conning's proprietary survey results, this study will analyze the overall industry, the largest MGAs and insurer partners in this market. Conning will also look at the changing role of MGAs, their influence in today's insurance market, and what is next in the evolution of the MGA model. **Coming soon**

ANNUAL—Property-Casualty Loss Reserves

Conning analyzes Schedule P statutory data and presents its loss reserve findings for individual lines of business, both for the industry and for small, midsized, and large groups of companies. Our prior-year analysis indicated that the industry's loss reserve position was redundant. However, favorable loss reserve development in 2019 was less than half of the amount recorded in 2018. In this update, Conning will reassess the industry's reserve position at year-end 2019, compare it to prior years, and examine the implications of its relative strength—or weakness. The study includes historical loss development data, accident-year results, and analysis of trends based on key segments and company actions. **Coming soon**

Surviving the Financial Crisis for the Life-Annuity Industry

This Focus Series will examine prior and current responses to financial crises by the life-annuity industry, along various dimensions of risk as well as regulatory responses. Challenges such as management preparedness, policy setting, and the impact of regulation will be reviewed, along with an assessment of mortality, credit, interest rate, and equity risks. **Coming soon**

ACA—Ten Years Out

In March 2010, the Patient Protection and Affordable Care Act, more commonly known as the ACA, was signed into law by then-President Barack Obama. Over the past decade, the bill has been implemented, but has also faced numerous changes, challenges, and lawsuits. Conning's Focus Series publication explores major aspects of the bill, its effect on health insurance and the insurance industry, as well as what the next ten years could hold based on current lawsuits and elections. **Coming soon**

Homeowners—Impact of IoT

Sensors in the home (smart-home technology) are becoming a more common feature and create a number of opportunities for personal property insurers to gather data. More importantly, the information that is increasingly available has the potential to change the value proposition for insurers from post-loss indemnity payers to active risk managers focused on prevention and mitigation. **Coming soon**

Old Lloyd's, New Lloyd's

Lloyd's has responded to pressures to address longstanding expense, performance, and service issues with an ambitious plan launched in 2019. The Future at Lloyd's plan proposed a bold, comprehensive overhaul of Lloyd's business processes to slash expenses, attract new capital providers, and enhance customer service. Conning's study explores prospects for the plan's success. The study presents important implications for brokers as well as insurers competing with Lloyd's at both ends of the market—complex risks as well as binding authority business. **Released May 2020**

Medical Professional Liability Insurance—Years of Plenty, Years of Famine

This Strategic Study will explore the changing dynamics within the medical professional liability line of business, including the impact of hospital consolidations, a shrinking physician exposure base, along with financial performance of the line and other factors that will influence strategic decision-making for MPL insurers and groups that service this line of business. **Released May 2020**

ANNUAL—Mergers & Acquisitions

Conning's annual insurance M&A study examines both insurer, distributor, and service company mergers & acquisitions. This year, Conning will publish separate reports for the P&C and life/health sectors. These studies include in-depth analysis of emerging or expected trends in M&A activity, along with the motivations behind key individual transactions. Insights will benefit market participants and investors alike. This global insurance M&A analysis provides a listing of transactions announced in 2019 and in early 2020. **Released April 2020**

Life-Annuity Liabilities—Growing Interest in a New Asset Class

The life-annuity industry has seen the emergence of a new type of insurer and reinsurer focused on acquiring and managing liabilities. Companies outside the industry, such as asset managers and private equity funds, have formed new platforms, with some insurers beginning to partner as well. The study examines the business model development, financial performance, the role of reinsurers, and growth potential. **Released March 2020**

Surplus Lines Insurance—A Booming U.S. Market

The surplus lines market is booming in the United States. This study includes analysis of the U.S. E&S market and conditions shaping its performance. It examines the drivers of the growing E&S U.S. market, including distribution, technology, and M&A, along with a review of E&S insurer peer group comparisons, and assessments of the different strategies employed by E&S writers. Additionally, the strategic study provides for a primer on the E&S market, E&S premium by state, and Conning's Surplus Lines index. **Released January 2020**

CONNING®
©2020 by Conning, Inc.
ISSN 1067-7364
THE CONNING COMMENTARY
is published monthly by
Conning
One Financial Plaza
Hartford, CT 06103
Phone: (860) 299-2000
Subscription rate: $295 per year. Reprints available.
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