Compensation
Advisory Partners

Industry Report // 2019-2020

Insurance

This report examines 2019 compensation and financial performance across two segments of the insurance industry, including seventeen of the largest Property & Casualty (P&C) and Life & Health (L/H) Insurance companies. 2019 median revenue of these companies was approximately $22B. CAP focused on 2019 financial performance, CEO pay trends and current industry dynamics, including the impact of the COVID-19 pandemic.

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Key Takeaways

2019 Pay and Performance. Bonus payouts for insurance company CEOs continued to be above target and commensurate with good financial results and strong total shareholder return in 2019.

Current Environment. 2020 started strong before the COVID-19 pandemic significantly impacted economies with stay at home orders and travel bans. Insurance companies were generally less impacted than other companies that had to take more extreme actions to stabilize business.

Looking Ahead. The COVID-19 pandemic is expected to result in changes in lifestyles and consumer behaviors. We do not believe this will lead to major overhauls in executive compensation programs among insurers. Most companies will make minor changes to their programs, and the primary focus will be on diminishing the impact of future uncertainties on compensation outcomes.

2019 Performance: Another Good Year

The insurance industry saw growth results generally similar to 2018. Companies in our study experienced 5% median revenue growth, coupled with 6% operating income growth in 2019. Median TSR was strong (+25%), a noticeable improvement from 2018; however, the sample did lag the median TSR of the S&P 500 companies of 30%.

The P&C industry generally experienced a better year than the L/H companies in our sample. Catastrophe (CAT) losses were down again in 2019, helping drive better performance. Operating income increased for all the P&C companies in the sample, with a median increase of 23% compared to 18% in 2018. CAT loss volatility continues to impact performance results for each company.

L/H company performance in terms of growth was consistent with the prior year, with a median revenue increase of 3.5% and operating income growth at 1.2%. Contrary to expectations for 2019, the industry experienced two interest rate decreases during the year, which depressed sales of certain products. Despite flat performance, TSR results were strong at +20% at median.

P&C Financial Performance

- Median revenue growth of 7.9% in 2019 was similar to 2018 median growth of 5.5%.
- Operating Income increased by 23% at median, higher growth compared to 2018.
- Similar to prior years, CAT losses had mixed impact on individual company results; CAT losses were down for all companies, nearly 40% at median.
- Median Operating ROE of 11.2% increased 0.9% compared to last year.
- Net Investment Income increased 11.2% at median, compared to 2018 growth of 4.5%.

L/H Financial Performance

- Revenue increased by 3.5% at median, similar to 2018.
- Operating income was flat compared to last year (+1.2%), a decline from 2018 growth at 18%.
- Median Operating ROE of 12.8% declined slightly from prior year.

	Median Revenue Growth	Median Op. Income Growth	Median Op. ROE Improvement	Median TSR
Property & Casualty	7.9%	23.4%	0.9%	29.4%
Life & Health	3.5%	1.2%	-0.5%	20.1%
All Insurance	5.1%	6.0%	0.3%	25.1%

2019 CEO Pay For Performance: Bonuses Pay Out Above Target

CEO Bonuses	Median Annual Incentive Payouts (% of Target)			Median Annual Incentive Payouts (% of Salary)		
	2019	2018	2017	2019	2018	2017
P&C (n=8)	132%	135%	142%	393%	409%	396%
Life and Health (n=9)	112%	125%	138%	278%	281%	300%
Total Sample (n=17)	**117%**	**125%**	**138%**	**370%**	**283%**	**318%**

Executive bonus payments in the insurance industry were above target again in 2019, although to a lesser degree than 2018.

Property & Casualty: 2019 was another strong year for the P&C industry. All eight companies experienced positive operating income growth. Performance results for P&C companies resulted in CEO bonuses as percent of target for 2019 that were consistent with prior years. On a dollar value basis, bonus payouts increased by 5% year over year (driven by small increases in salaries and target bonus opportunities).

Life & Health: Modest revenue growth and flat operating income growth for 2019 resulted in reduced bonus payouts for 2019. While payouts are still above target, they were closer to target than in prior years, reflecting financial results.

2020 Developments and Expectations for 2021

This year, the COVID-19 pandemic has led to significant volatility in financial markets, hampered growth for many companies, and transformed social behaviors. This section assesses the impact to-date and future expectations for insurance industry executive compensation and performance.

S&P 500 Performance (through 5/31/2020). Year-to-date, the S&P 500 index has been volatile. Performance was strong before the COVID-19 pandemic disrupted the economy and financial markets. At its highest point on February 19, the index was up 4.8%. Just a little over a month later, on March 23, the index loss was 30.7% for the year. While certain industries were impacted more than others, all industries were down for the year. As the CARES (Coronavirus Aid, Relief, and Economic Security) Act agreement got closer to being passed, markets started rebounding late March. The act will ultimately inject over $2 trillion into the US economy. Despite record unemployment claims, the S&P 500 index recouped most of the losses by the end of May.

S&P 500 Insurance Sector TSR. Insurance companies in the S&P 500 index tracked the index at both the height of the market in February, and the bottom of the market on March 23. As the market began recouping losses, insurers recovered to a lesser degree than other industries. We believe this has been driven by investor sentiment on profitability expectations for insurers due to lower interest rates, increased short-term disability and mortality rates, and uncertainty around potential lawsuits related to business interruption.

	2/19/2020 S&P 500 High	3/23/2020 S&P 500 Low	5/31/2020
S&P 500 Index	4.8%	-30.7%	-5.8%
Insurance Industry Group Median	4.9%	-38.2%	-26.9%
Insurance Industry Rank vs. Other Industry Groups	6 of 24	13 of 24	19 of 24

COVID-19 Impact on Compensation. As it became apparent that the COVID-19 pandemic would have a more lasting impact on businesses, companies took significant actions to preserve liquidity and conserve costs. More than 200 companies in the S&P 500 have taken temporary compensation or human capital actions. The most prevalent action has been salary reductions for executives, with over 100 companies announcing such actions. The most impacted industries have been retail, consumer services and automotive.

The insurance industry has not been impacted as much as other industries that may have lost significant sources of revenue. As a result, we have seen very few insurance companies reduce compensation or significantly reduce the workforce on a temporary or permanent basis. Instead, many insurers, particularly P&C companies, have announced favorable actions directed at customers, including rebates on certain policies, suspension of policy cancellations for non-payment, and fee waivers for late payments, to help customers through the crisis and retain customer loyalty. Some companies also committed to no layoffs and expanded employee benefits, such as additional paid leave and travel reimbursements for essential employees.

Developments in the Insurance Industry. The impact of the COVID-19 pandemic has been far reaching, and it is unclear what the long-lasting behavior changes will be on daily lives, work habits, and consumer preferences. For insurance companies it will be important to correctly plan for such changes in order to respond with new products, adjust pricing of current products and maintain appropriate digital platforms, among other things.

For the P&C industry, one area of change will likely include revisions to workers compensation insurance and how it applies to the increasing number of telecommuters. Further, P&C insurers have already been impacted by pricing on auto insurance. Incident rates have currently declined as Americans stopped commuting to work and reduced leisure travel. It is not clear if this behavior will continue, or if we will see a surge in driving when COVID-19 is perceived to be more controlled. Enterprise cybersecurity is also becoming more important with millions working from home and creating needs in cyber liability insurance products. In Life and Health insurance companies, the extremely low interest rate environment has forced some insurers to make changes to product offerings, reprice products, turn away certain customers, and increase premiums. The fast pace of change in products is driven in part by increased demand in response to the COVID-19 pandemic. Some life insurers reported over a 20-30% jump in sales in the months of March or April, yet life insurers are also expecting increased claims (e.g., short-term disability and mortality claims) in the remainder of the year, which will put pressure on profitability.

Uncertainty in the industry is also coming from a potential issue around business interruption policies. Many property policies-in-force specifically exclude viruses. For those that do not, interpretation exists around the requirement for physical damage. There is increasing pressure suggesting that insurers may be expected to cover some of the loss from the pandemic, and pressure to retroactively change policies to cover such losses.

Lawsuits have followed, with preliminary arguments favoring both sides of the issue. If insurers are ultimately required to change outstanding contracts, the financial impact on the industry could be significant.

2020 Performance Expectations. In light of the expected changes among P&C and Life Insurance companies, we expect financial performance in 2020 to be lower and impact compensation accordingly. Companies will likely pay below target incentives (with just a few falling below threshold and paying no incentives to executives and a few paying above target), yet performance and bonus payouts will vary significantly depending on the line of business.

We believe companies will adjust performance results for COVID-19 to varying degrees. Some will adjust for direct costs of COVID-19 if quantifiable. For example, if companies helped employees with costs of establishing home offices, those costs are easily identifiable and reasonable to exclude as unplanned costs. Some companies will take a more holistic assessment and consider not only financial performance but also how well the company and senior leadership responded in the crisis. It is fairly certain that Compensation Committees will use more discretion (if allowed under the plan) when determining current year bonuses. For long-term incentives, we do not expect many changes to performance goals on outstanding awards, yet some COVID-19 related adjustments to performance will likely be applied when performance periods are completed.

Implications on 2021 Executive Compensation. The COVID-19 pandemic will result in companies in most industries evaluating their incentive compensation plans to determine if any potential design changes should be made on a go forward basis, to ensure that the incentive plans continue to be relevant and motivational during the economic downturn and period of uncertainty. Some of the incentive design changes companies may consider, include:

Annual Incentive Plans	Long-term Incentive Plans
Use of wider performance scales around target goals, which may lead to less volatility in payouts	Increased use of time-based restricted stock/units, given its certainty and retentive aspect
Increased weighting on (or introduce) individual, strategic or ESG performance components	Adopting relative performance measures (primarily TSR) or increasing the weight of relative measures
Greater degree of (informed) discretion used in approving final payouts	Potentially shorter performance periods for performance based LTI to de-risk the overall incentive program. In periods of uncertainty, a longer performance period exposes participants to greater risk of awards not being earned and makes goal setting more challenging.

We do not expect insurance companies to make sweeping changes to their incentive programs due to the COVID-19 pandemic, yet companies will likely make some changes depending on the expected length and severity of the economic downturn. We anticipate that shareholders will look for parity in treatment between the broader population and executives. While shareholders may be understanding of the significant business impact related to COVID-19, we are confident they will still look for strong business rationale behind pay program decisions, even if original performance objectives have been reconstituted. As companies forge ahead through the challenges presented this year, we also believe it is a very opportunistic time to reassess programs and potentially redefine performance expectations and accountability at both the corporate and individual executive level.

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Insurance Sample for Pay for Performance Analysis:

P&C Companies

Allstate Corporation
American International Group, Inc.
Assurant, Inc.
Chubb Limited
CNA Financial Corporation
Hartford Financial Services Group
Progressive Corp.
Travelers Companies, Inc.

Life & Health Companies

Aflac Incorporated
Genworth Financial, Inc.
Globe Life
Lincoln National Corporation
Manulife Financial Corporation
MetLife, Inc.
Principal Financial Group Inc.
Prudential Financial, Inc.
Unum Group