February 23, 2023

Market Segment Outlook: US Title Insurance

Our outlook is moving to Negative, owing to the significant decline in home sales and refinancing activity, as well as other factors

AM Best is revising the outlook for the title insurance segment to Negative from Stable, owing to the following key drivers:

- Significant decline in home sales and refinancing activity
- Continued economic slowdown
- Expected rise in unemployment
- Continued monetary tightening and high prevailing mortgage interest rates
- Potential recessionary pressures

These factors have been prompted by the recent rise in the Federal Reserve's key lending rate, which has increased mortgage rates to levels not seen in two decades. These same challenges also apply to commercial real estate transactions. The drop in both residential and commercial transactions is very likely to dampen revenue prospects for all US title insures over the next 12 to 24 months.

Based on the most recent data (collected through third quarter 2022), title premiums were down 7.5%, which confirms that home loans originations and refinancing have dwindled. Most of the contraction occurred in the third quarter, with further deceleration expected in the fourth quarter due to the timing of the Fed's rate hikes, which occurred in the latter part of the year, and their impact on transaction activity. As interest rates remain more than twice the mortgage interest rate reported in 2021, home sales have declined steadily, and home refinancing is almost non-existent. Through third-quarter 2022, home sales declined 18%, with expectations for a continued decline throughout 2023.

Operating Profitability Remains Solid

Mortgage interest rates rose throughout 2022 and are now at a level not seen in nearly two decades. As a result, home sales fell more than 17%, and refinancing activity was significantly lower than the record-breaking transactions reported over the past two years. The real estate market is going through a soft patch, but title insurers are expected to weather the storm even as market headwinds drive down new business opportunities and curtail growth. This is not to say that title insurers are immune to adversity but are instead viewed as prudent cycle managers, as observed in 2008.

Direct written premium is expected to fall significantly in 2023, but net underwriting and net operating results should remain positive. Despite the headwinds and their expected impact on revenues over the next 12 to 24 months, the loss and loss adjustment expense ratios for title insurers should remain at their historically low levels. In recent years, the increase in commercial real estate transactions often helped offset some of the decline in residential transactions (both mortgage originations and refinancing). However, commercial transactions are likely to dry up in 2023 as well. Revenue from commercial transactions, given the values of the properties insured, is typically higher than from residential transactions. These transactions typically account for 5% to 10% of the market.

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Housing affordability is another concern and is likely to be a barrier for new homebuyers, as high interest rates and elevated home values will likely keep them out of the market over the next 12 to 24 months. This was already happening in later half of 2022 with 30-year mortgage rates hovering at 7%, compared with the average interest rate of 2.6% in 2021. Furthermore, homebuyers will be reluctant to leverage all of their purchasing power in light of a potential recession and a resulting rise in unemployment.

There does not seem to be any indication that the housing market will suffer through another crisis resembling the crash in 2008, given that underwriting guidelines are much tighter. Housing inventory is beginning to grow but is likely to remain tight for some time, even though purchasing activity will continue to slow and homes will stay on the market longer. Home prices are expected to remain high for at least the short term compared with pre-pandemic levels, which helps alleviate foreclosure concerns. Home equity remains favorable.

Segment Benefiting from Accelerated Innovation

The title industry has benefited from innovative technology and a shift toward a digital ecosystem (which other industries took longer to adopt). The industry was already heading in that direction, but the pandemic accelerated the pace of change. For most industries, being able to adapt to changes in buying behavior is essential, and this is particularly true for the title industry, whose customers are extremely comfortable conducting transactions in a digital economy. Title insurers have embraced technology and realized greater efficiency through the broader use of technology, but much of the imbedded cost remains at the agency level. Title insurance companies will continue to seize innovative opportunities to grow, including partnerships and acquisitions of complementary tech companies, potentially allowing regional and local title insurers to increase their market share in more favorable operating environments.

Home Purchases Expected to Decline; Refinancing Remains Low

Over the next year, AM Best expects to see a continued downturn in home purchases while mortgage interest rates remain high compared with 2019-2021. Refinancing transactions are also expected to continue to decline in 2023. Commercial transactions, which have picked up and offset some of the drop in refinancing transactions, are also expected to slow in 2023.

Title insurers do not expect the same rate of record-breaking profits of the past couple of years; however, most realize this is just a soft patch in a cyclical market that they will need to manage as they've done before.

GUIDE TO BEST'S MARKET SEGMENT OUTLOOKS

Our market segment outlooks examine the impact of current trends on companies operating in particular segments of the insurance industry over the next 12 months. Typical factors we would consider include current and forecast economic conditions; the regulatory environment and potential changes; emerging product developments; and competitive issues that could impact the success of these companies.

A Best's Market Segment Outlook can be Positive, Negative, or Stable.

Best's Market Segment Outlook	
Positive	A Positive market segment outlook indicates that AM Best expects market trends to have a positive influence on companies operating in the market over the next 12 months. However, a Positive outlook for a particular market segment does not mean that the outlook for all the companies operating in that market segment will be Positive.
Negative	A Negative market segment outlook indicates that AM Best expects market trends to have a negative influence on companies operating in the market over the next 12 months. However, a Negative outlook for a particular market segment does not mean that the outlook for all the companies operating in that market segment will be Negative.
Stable	A Stable market segment outlook indicates that AM Best expects market trends to have a neutral influence on companies operating in that market segment over the next 12 months.

We update our market segment outlooks annually but may revisit them at any time during the year if regulatory, financial, or market conditions warrant.

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BEST'S MARKET SEGMENT REPORT

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