BEST'S MARKET SEGMENT REPORT

February 17, 2021

Market Segment Outlook: US Title Insurance

Our outlook is going to Stable from Negative, owing to the segment's exceptional performance in 2020

The title insurance industry performed exceptionally well in 2020 and was the most profitable segment in the property/casualty industry, despite the pandemic and all of its inherent challenges. AM Best expects this trend will continue during the next 12 months albeit at perhaps a slower pace and is therefore revising its outlook for the US title segment to Stable from Negative. The industry proved to be far more resilient than anticipated in the wake of the sudden economic slowdown and lockdowns brought about by the COVID-19 pandemic.

The outlook for the title segment had been revised to Negative from Stable on April 7, 2020, prompted by the sudden and substantial economic slowdown in the US as a result of the pandemic. The change to Negative was also due to questions about whether the US economy would be thrown into an extended recession owing to lockdown measures, business closures, tighter labor markets, and rising unemployment levels.

The change to Stable takes into account the Federal Reserve's decision in 2020 to cut the federal funds rate by 150 basis points, effectively bringing the rate to zero, as well as its decision to purchase assets in the open markets, including mortgage-backed securities. These two decisions lowered interest rates and brought the 30-year fixed mortgage rates down to near historical lows, which should continue to fuel real estate sales and refinancing activity in the real estate markets—and further the business activities of title insurers.

Low interest rates accelerated the level of refinancing activity through the first quarter of 2020. However, with the start of the pandemic, there was much uncertainty and skepticism as to whether this pace would continue. With the pandemic under way, AM Best believed that the economic slowdown and its impact on small business, housing, lending, and consumer confidence would temper refinancing activity through the remainder of the year. These same economic constraints, along with a presumed change in people's behavior, were expected to negatively affect both commercial and residential real estate transactions and dampen revenue prospects for US title insurers. However, just the opposite occurred, as refinancing and home buying surged in the latter half of 2020.

With 30-year mortgages at or below 3% for the first time, new and existing homebuyers were flooding the markets, looking to take advantage of historically low mortgage rates. This was evidenced by record refinancing activity during the year and 2020 being one of the most active years in home sales in recent memory.

In March and April 2020, the impact of the COVID-19 pandemic was felt by all companies in the P/C insurance industry, due to temporary investment impairment, business closures, requirements for social distancing and other restrictive ordinances required by federal and state regulations. However, for the title insurers, advancements in digitization and technology, including online notorizations, played key roles in keeping the deal flow and business pipeline moving. The ability to interface with lenders and agents proved to be crucial in allowing title insurers to keep pace with the record number of closings during the year, all while following the COVID-19 guidelines.

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AM 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. Best's ratings take into account the manner in which companies manage these factors and trends.

A Best's Market Segment Outlook, like a Best's Credit Rating Outlook for a company, can be Positive, Negative, or Stable.

- 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.
- 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.
- 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.

With the Biden administration's initiatives set to address the economy and the pandemic in an organized manner, there is hope that the unemployment rate will fall further and that the US economy will return to a more solid footing. The availability of a number of COVID-19 vaccines and the administration's goal to vaccinate more than 100 million individuals through the first half of 2021 fosters hope of a return to normalcy.

Because of these factors, we expect the residential real estate market to remain strong in 2021. Default levels should not be elevated, as in the housing crisis of 2007-2009, given that homeowners today have more equity in their homes. Nor are foreclosures expected to cause major disruptions, owing to enhanced provisions contained in the various stimulus packages passed by or proposed by Congress.

AM Best also expects US monetary policy to remain accommodative through 2021 and beyond, resulting in a prolonged low interest rate environment. Low rates will support home purchases and refinancing, although the number of refinancings will likely be down from the historical levels of 2020. Sales of single-family homes will likely continue to rise through year-end 2022, while refinancing is expected to revert to "normal" levels. Given the lack of supply, we expect new construction of single-family homes to rise and to continue do so through year-end 2022, driven primarily by relocations and millennials entering the housing market. New construction of multifamily residential homes is likely to average a third of new single-family construction, while the commercial market and construction may remain tepid compared with residential market.

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