



# A Valentine for the P/C Insurance Industry: *Why I ♥ this Business & Why You Should Too*

**Association of Professional Insurance Women  
New York, NY  
February 14, 2013**

Robert P. Hartwig, Ph.D., CPCU, President & Economist  
Insurance Information Institute ♦ 110 William Street ♦ New York, NY 10038

Tel: 212.346.5520 ♦ Cell: 917.453.1885 ♦ bobh@iii.org ♦ www.iii.org

## ■ Economic Outlook

- ◆ Exposure and premium growth depend critically on growth trajectory for the economy

## ■ Catastrophe Loss Overview

- ◆ Hurricane Sandy guarantees that 2012 will become the 2<sup>nd</sup> or 3<sup>rd</sup> costliest year in US history in terms of insured losses
- ◆ Interior US losses loom ever larger

## ■ P/C Industry Performance: Overview & Outlook

- ◆ Underwriting
- ◆ Pricing
- ◆ Growth
- ◆ Capacity
- ◆ Investments

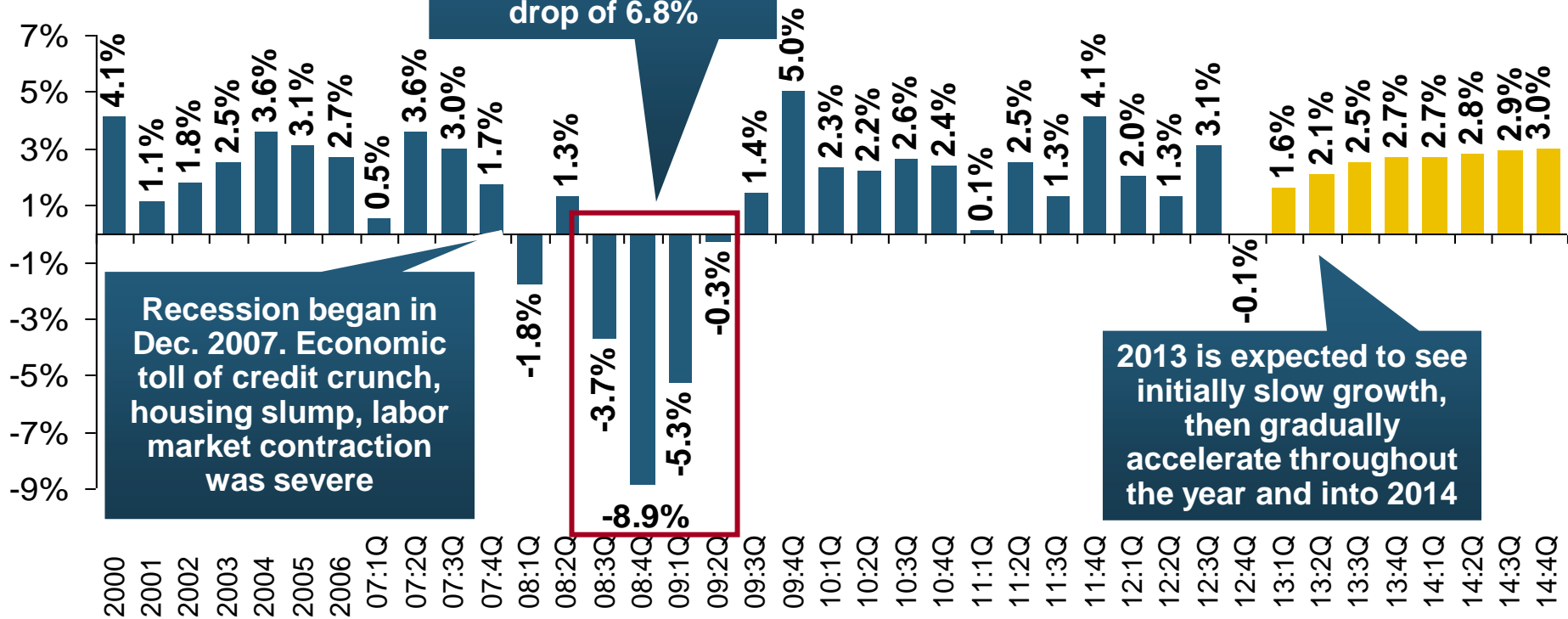


# The Strength of the Economy Will Influence P/C Insurer Growth Opportunities

**Growth Will Expand Insurer Exposure  
Base Across Most Lines**

# US Real GDP Growth\*

## Real GDP Growth (%)



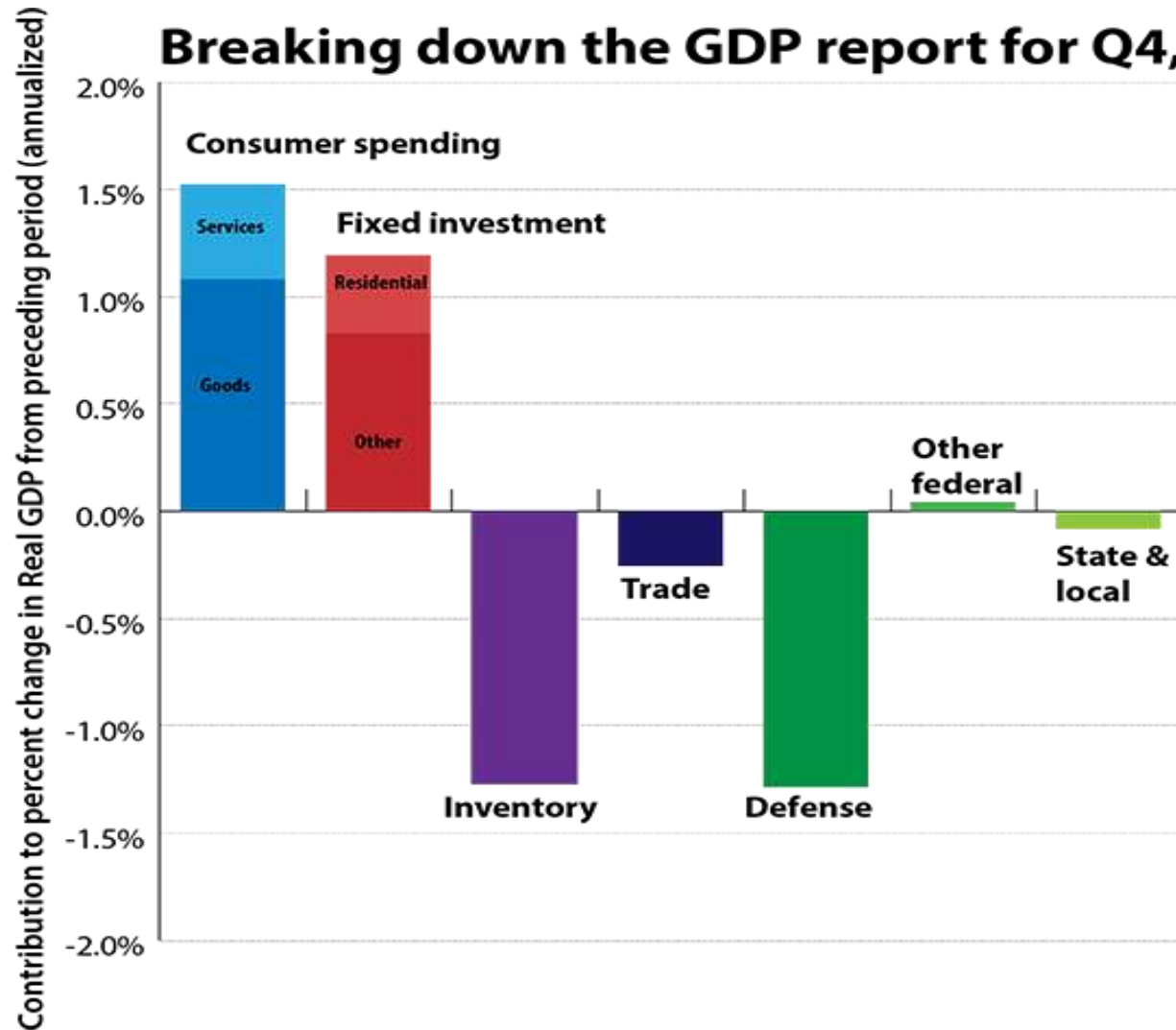
**Demand for Insurance Continues To Be Impacted by Sluggish Economic Conditions, but the Benefits of Even Slow Growth Will Compound and Gradually Benefit the Economy Broadly**

\* Estimates/Forecasts from Blue Chip Economic Indicators.

Source: US Department of Commerce, Blue Economic Indicators 1/13; Insurance Information Institute.

# 2012:Q4 GDP Number Was Not as Bad as the Headline Suggests

## Breaking down the GDP report for Q4, 2012



- GDP declined by 0.1% in Q4
- The shrinkage in the economy was driven mostly by a decline in defense spending and a decumulation of inventory
- State and local govt. are dragging on the economy as well
- The private economy actually expanded by 1.2%

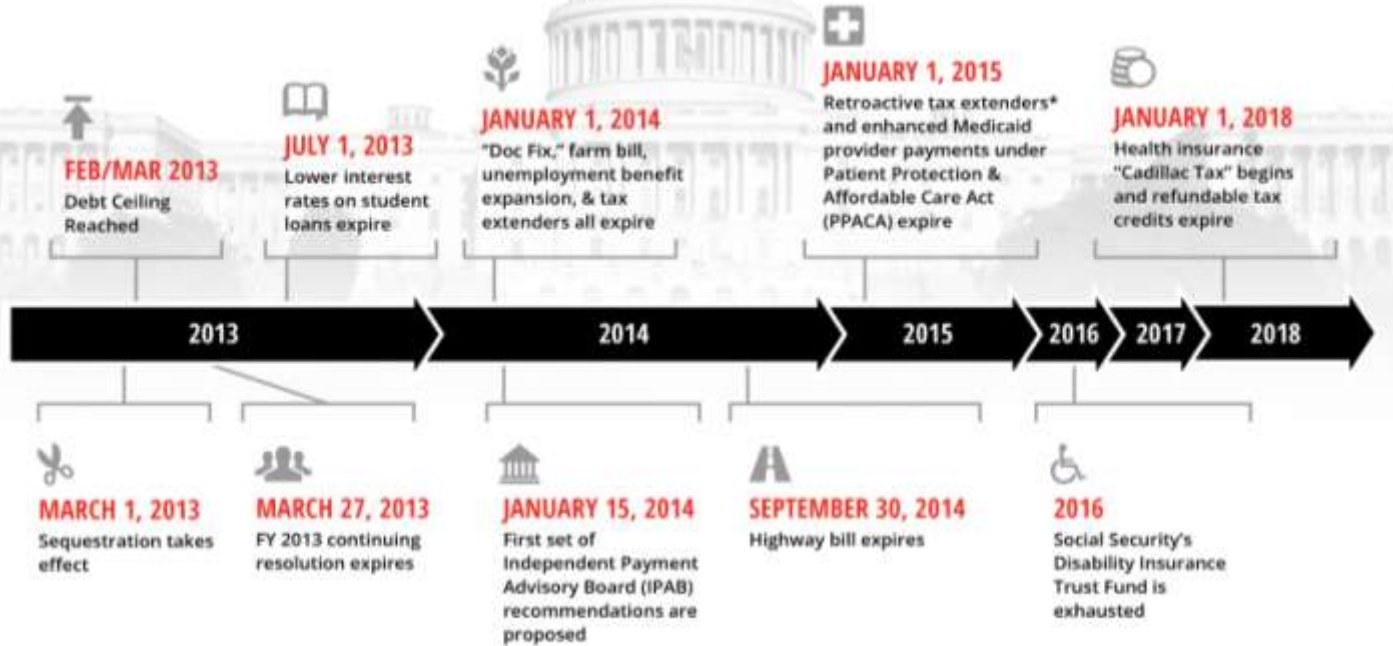
# The Fiscal Cliff Was Just the Beginning: Budget Battles for Years to Come?

*Poll: 94% of P/C insurance executives think looming budget battles In Washington will hurt the economy.\**

- The “Fiscal Cliff” was just the beginning
- There are 10+ “Fiscal Speed Bumps” over the next 5 years, setting up a potentially extended period of fiscal uncertainty
- Creates long-term uncertainty around federal spending, tax policy, entitlements

## Impending “Fiscal Speed Bumps”

2013–2018

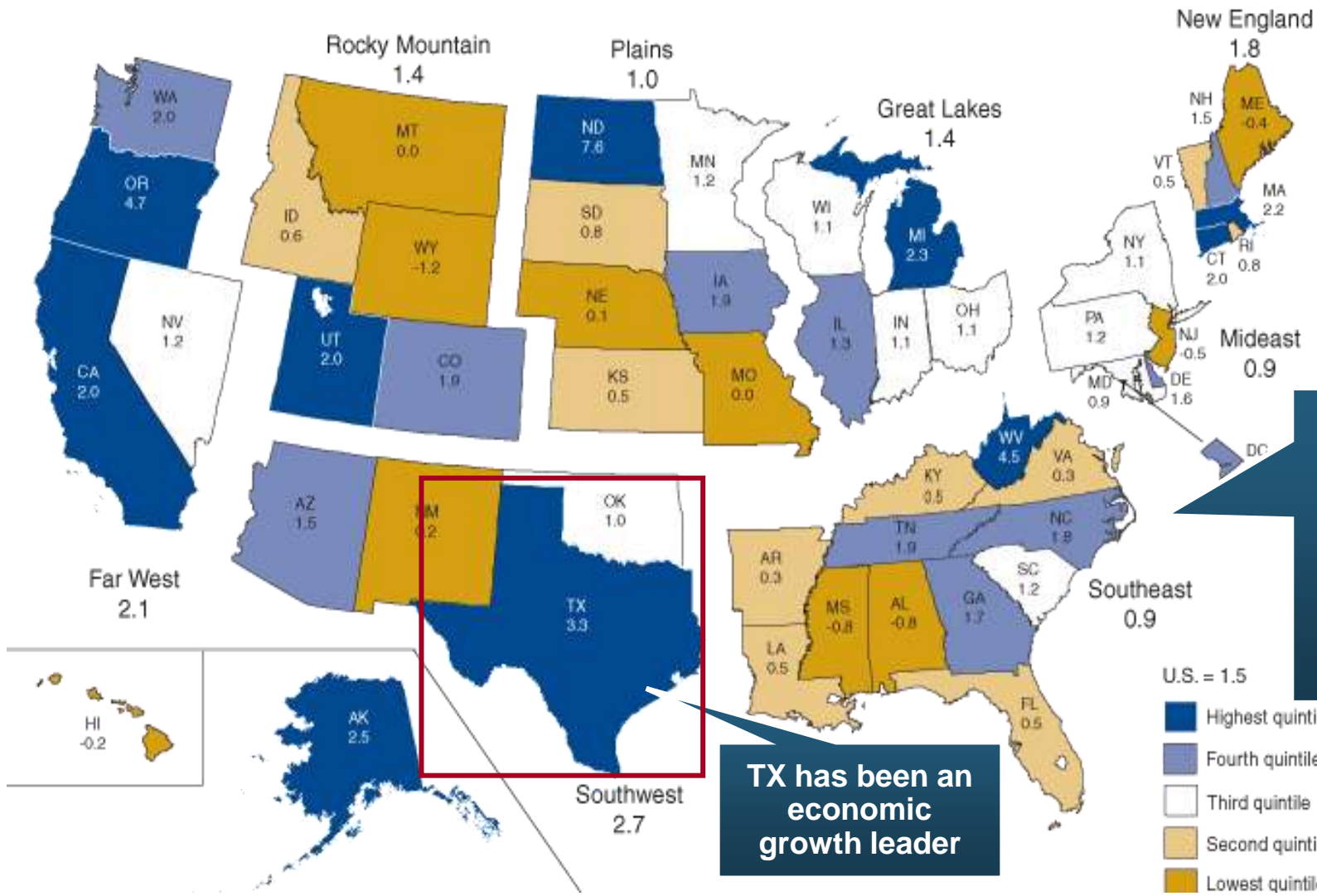


\*The tax extenders officially expire at the end of 2013, but can be restored retroactively up until this point.

\*P/C Insurance Joint Industry Forum press release ([www.iii.org/press\\_releases](http://www.iii.org/press_releases)), January 15, 2013.

Source: Fix the Debt Coalition, January 18, 2013; Insurance Information Institute

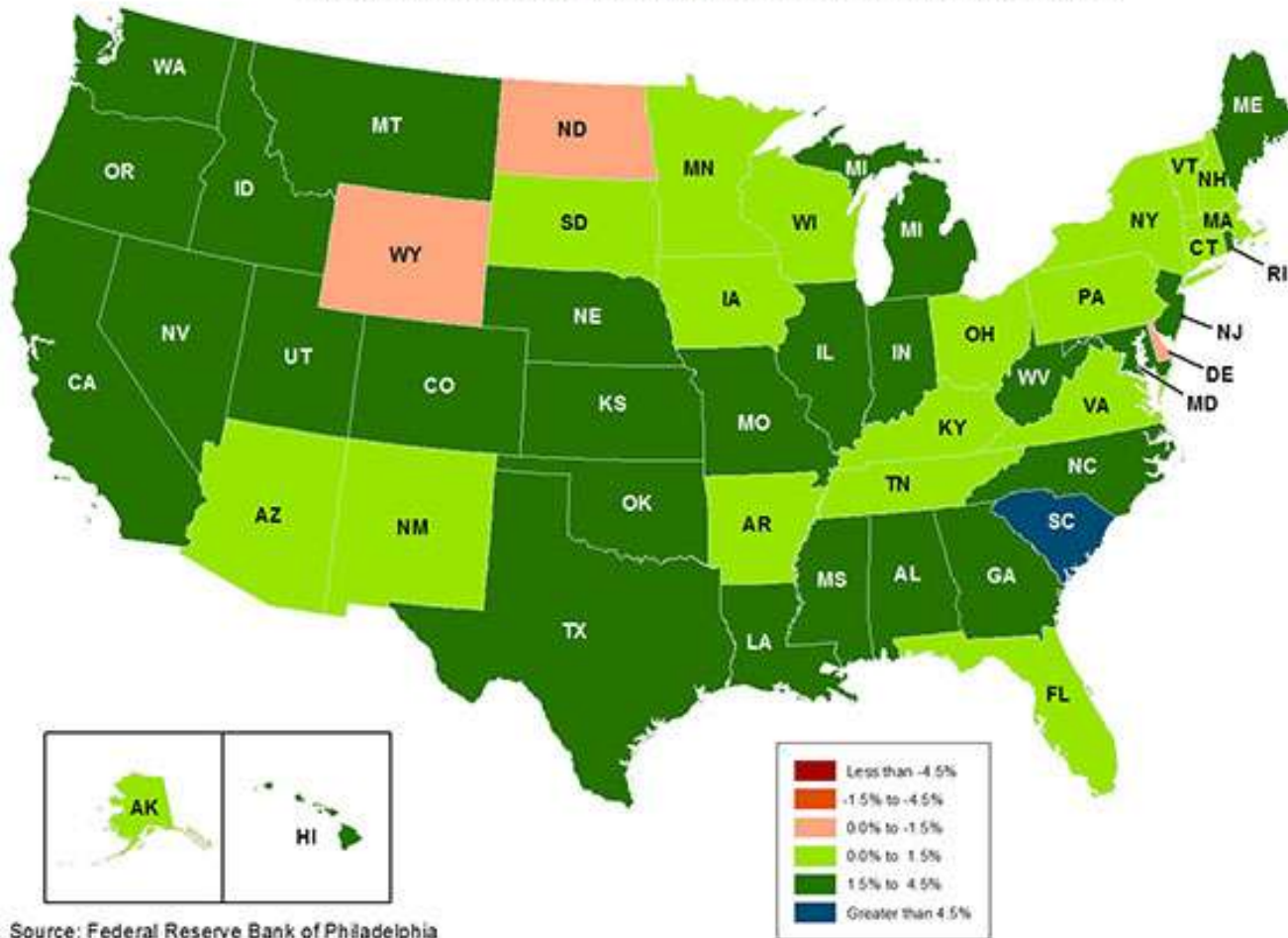
# Percent Change in Real GDP by State, 2011





# State-by-State Leading Indicators through 2013:Q1

October 2012 State Leading Indexes: 6-Month Forecast



## Near-term growth forecasts vary widely by state

### 5 Fastest Growing States

South Carolina	6.97%
Michigan	4.32%
West Virginia	3.59%
Idaho	3.14%
Georgia	3.04%

### 5 Slowest Growing States

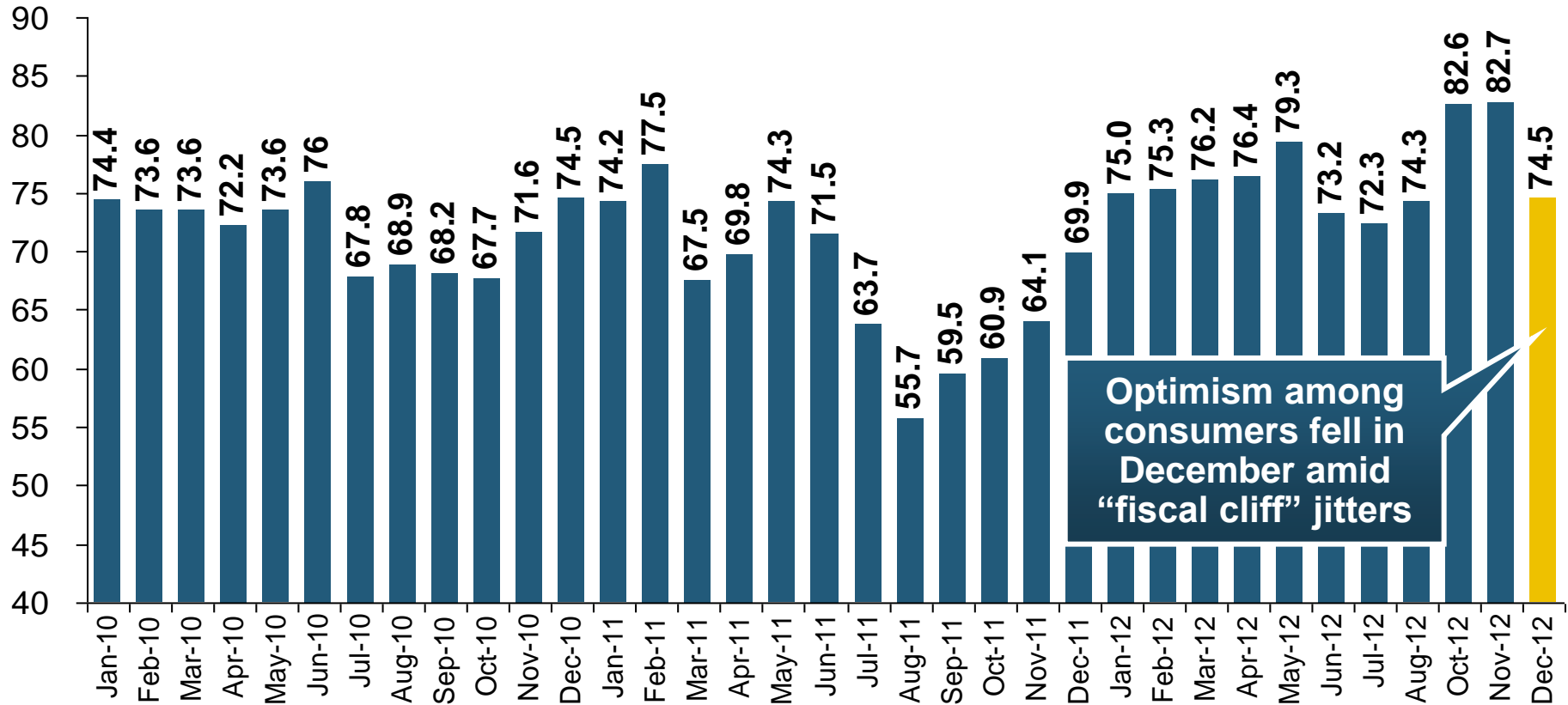
Wyoming	-1.09%
Delaware	-0.24%
North Dakota	-0.19%
Vermont	0.09%
Minnesota	0.18%

Source: Federal Reserve Bank of Philadelphia



# Consumer Sentiment Survey (1966 = 100)

## January 2010 through December 2012

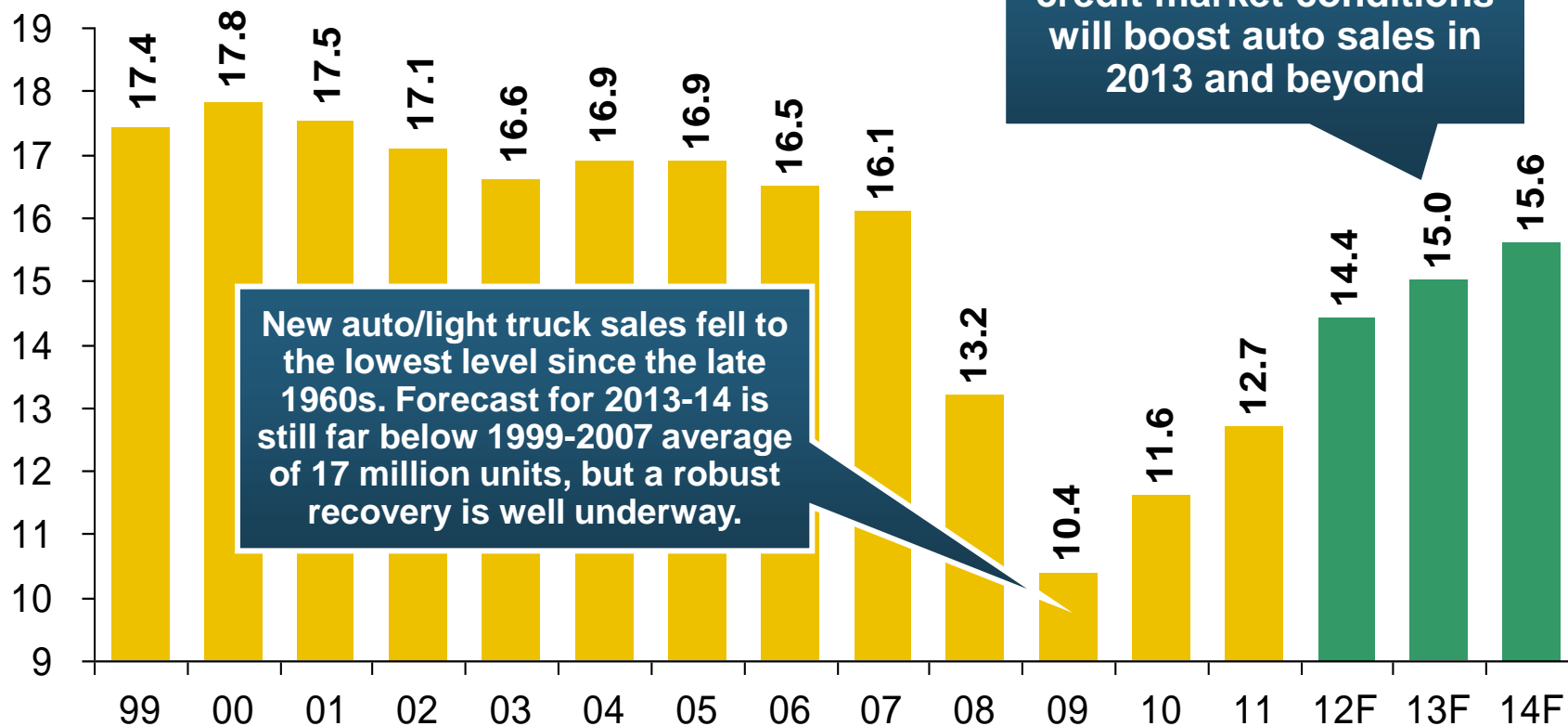


Optimism among consumers fell in December amid "fiscal cliff" jitters

**Consumer confidence has been low for years amid high unemployment, falling home prices and other factors adversely impact consumers, but improved substantially in late 2011 and in 2012**

# Auto/Light Truck Sales, 1999-2014F

(Millions of Units)

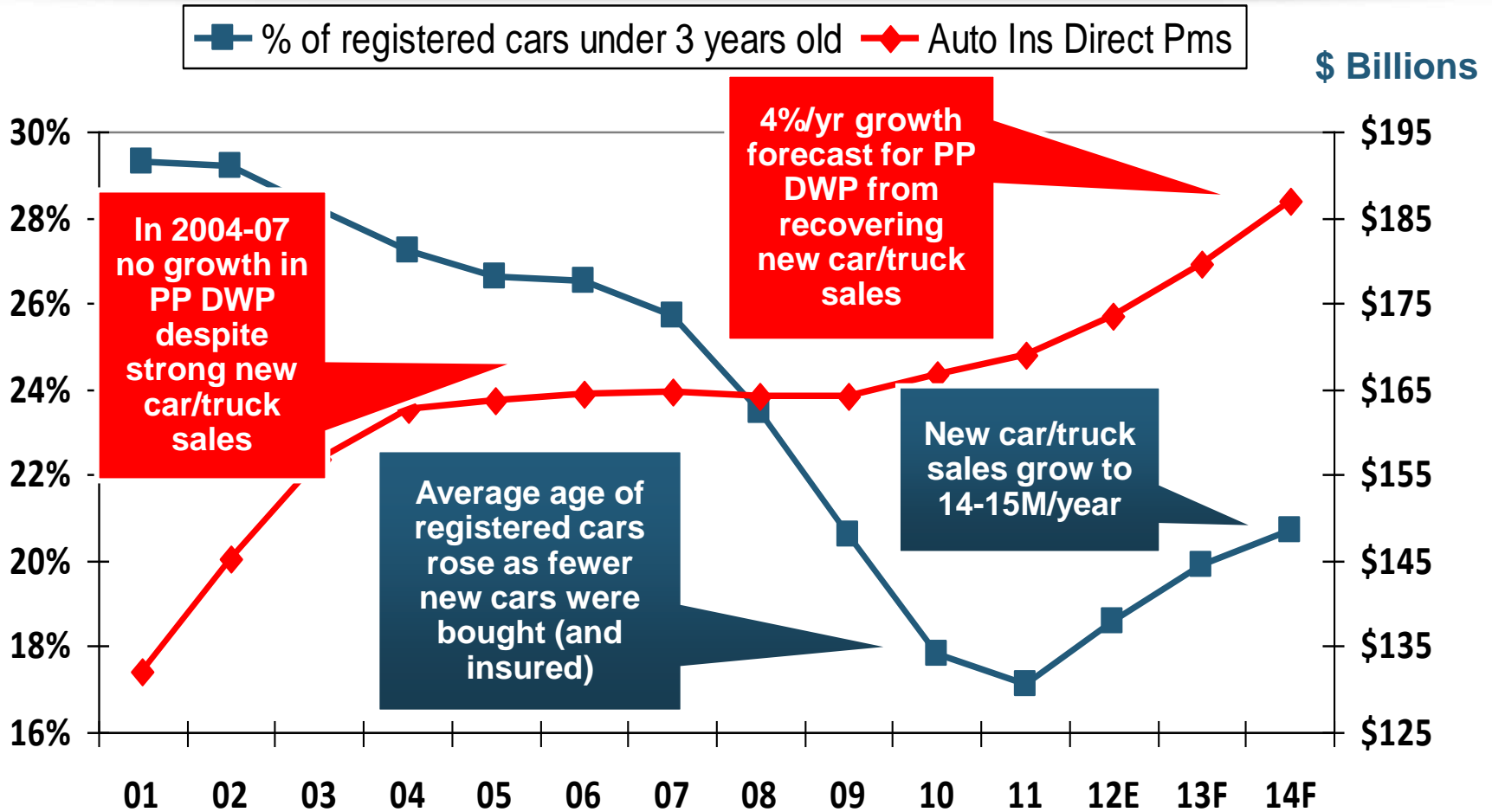


Job growth and improved credit market conditions will boost auto sales in 2013 and beyond

New auto/light truck sales fell to the lowest level since the late 1960s. Forecast for 2013-14 is still far below 1999-2007 average of 17 million units, but a robust recovery is well underway.

**Car/Light Truck Sales Will Continue to Recover from the 2009 Low Point, Bolstering the Auto Insurer Growth and the Manufacturing Sector.**

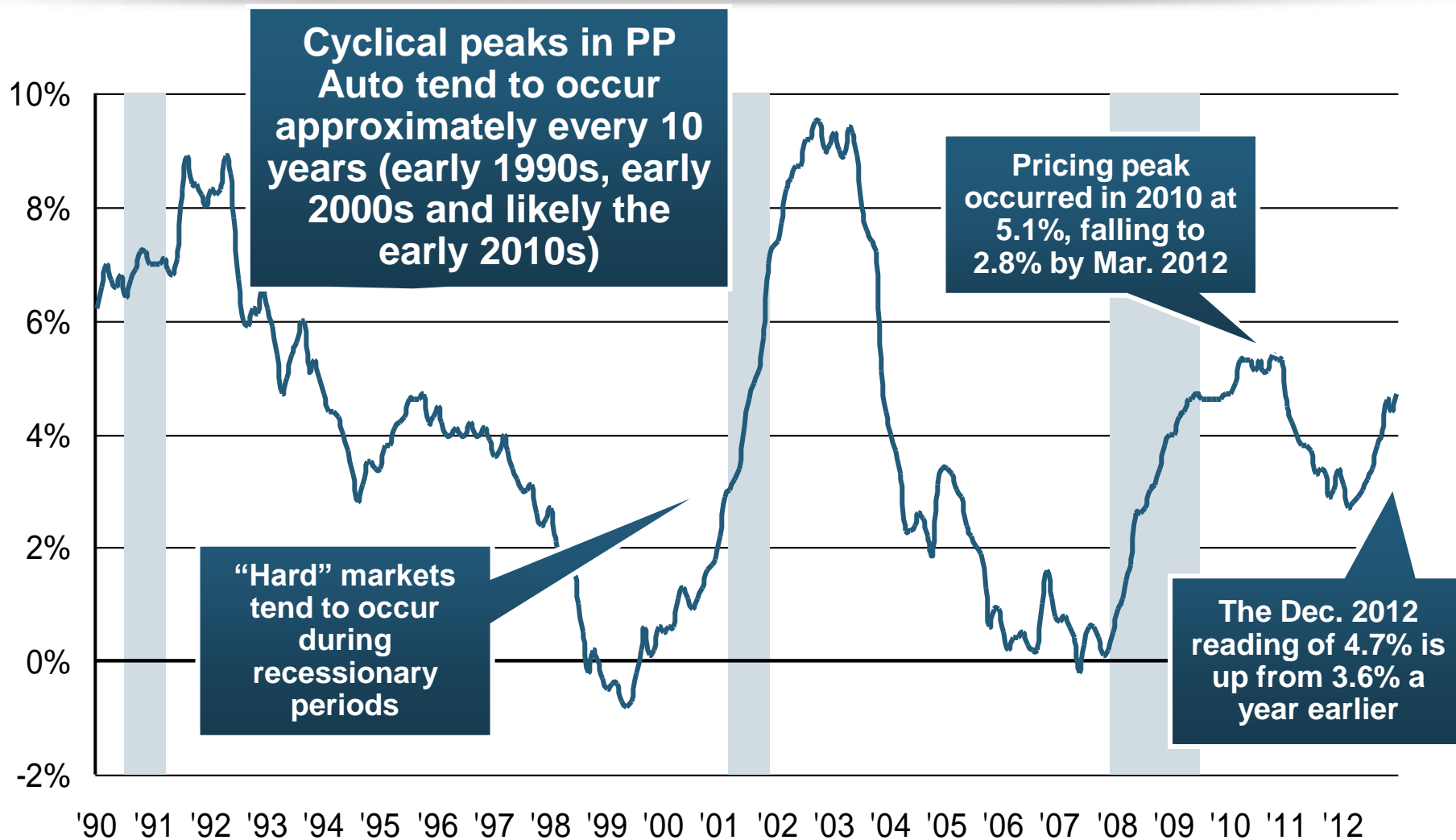
# Personal Auto Insurance Direct Written Premiums vs. Recently-Registered Cars



**PP DWP, flat from 2004-2009, is rising again. Conning forecasts growth at 3.5% in 2013 and 4.0% in 2014.**

Sources: AIPSO Facts (various issues); SNL Financial; Conning Research & Consulting, *Property-Casualty Forecast and Analysis*, First Quarter 2012; Insurance Information Institute.

# Monthly Change\* in Auto Insurance Prices, 1991–2012\*



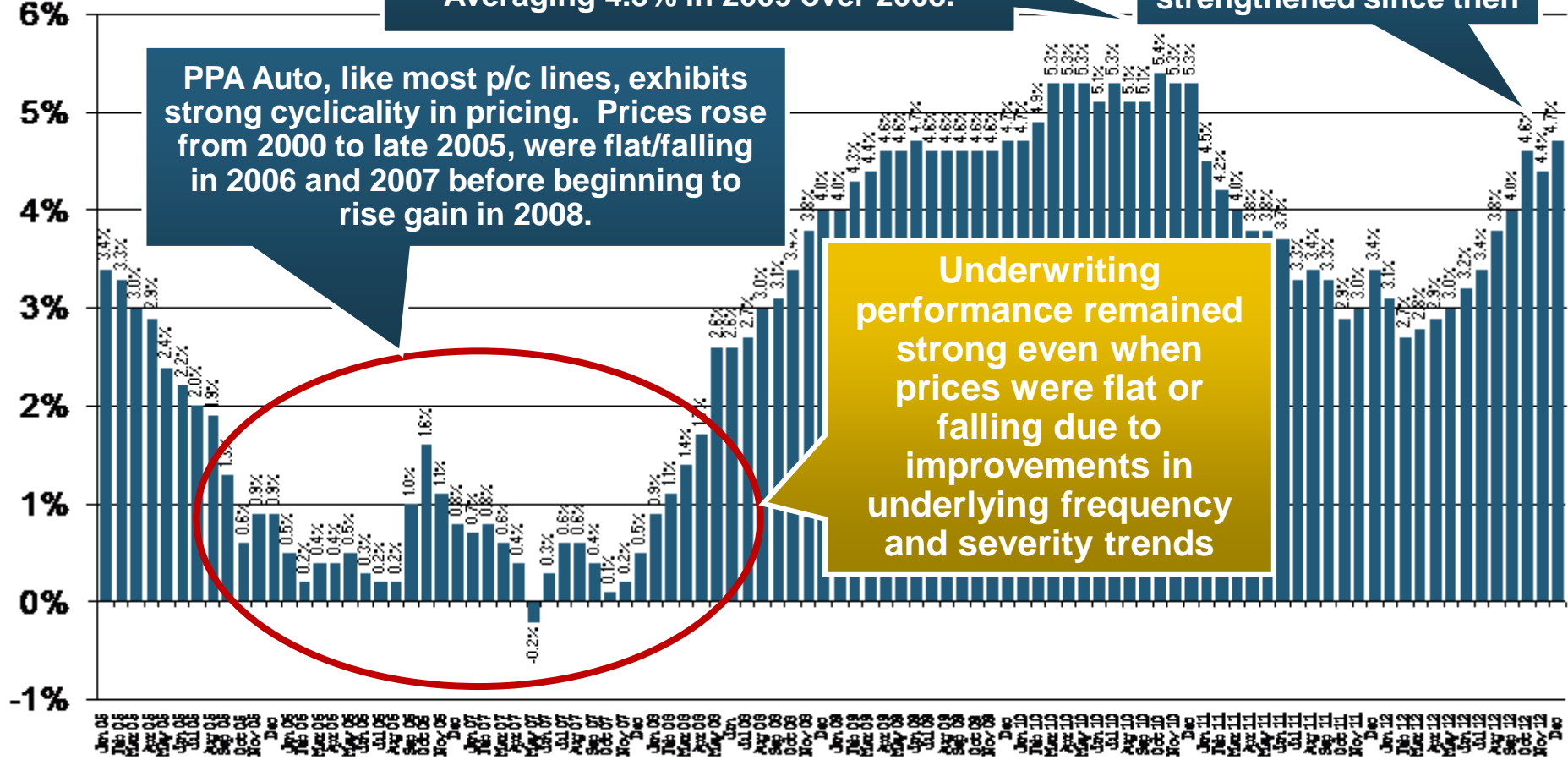
\*Percentage change from same month in prior year; through Dec. 2012; seasonally adjusted

Note: Recessions indicated by gray shaded columns.

Sources: US Bureau of Labor Statistics; National Bureau of Economic Research (recession dates); Insurance Information Institutes.

# Monthly Change\* in Auto Insurance Prices, January 2005 - December 2012

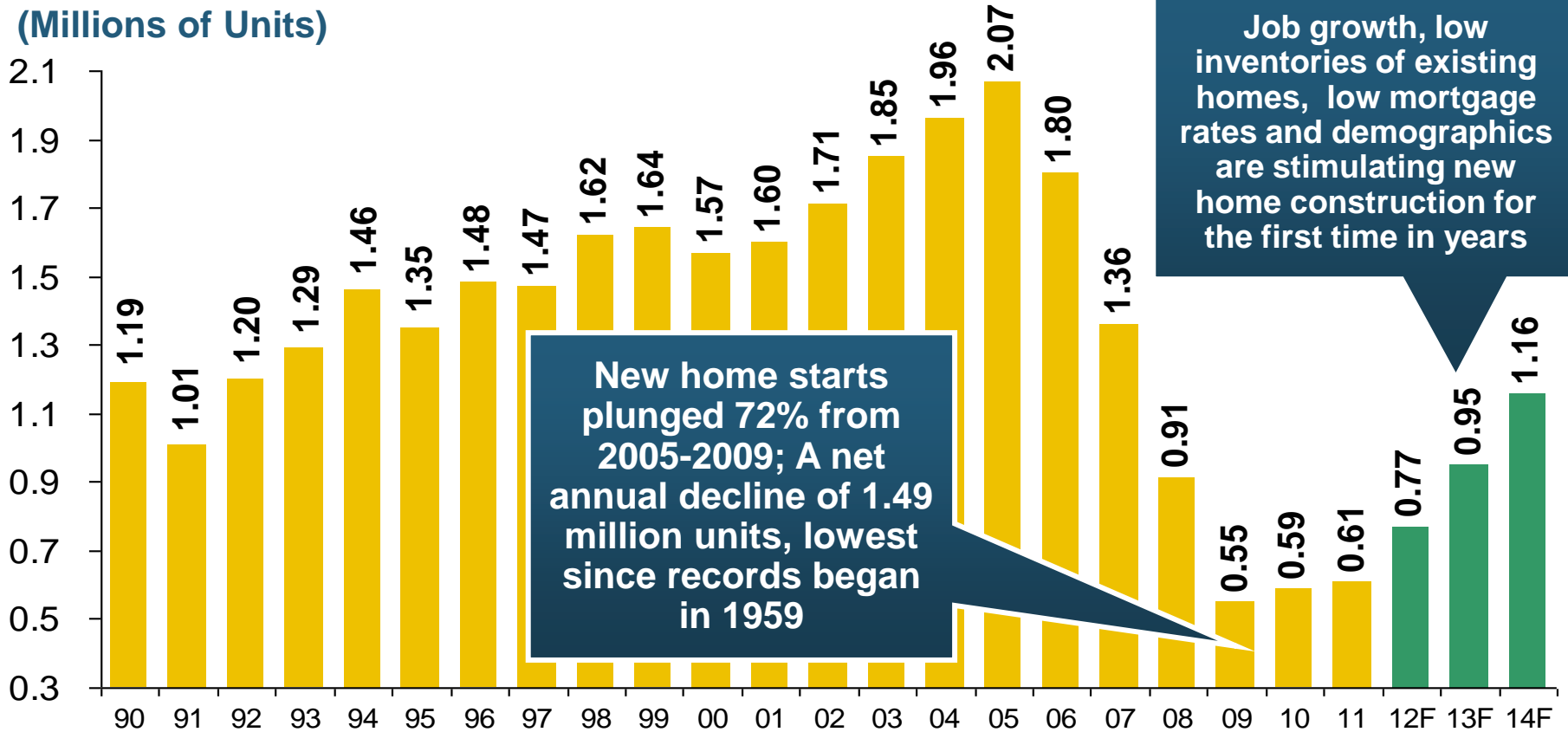
(Percent Change from same month, prior year)



\*Percentage change from same month in prior year, seasonally adjusted.  
Sources: US Bureau of Labor Statistics; Insurance Information Institute

# New Private Housing Starts, 1990-2014F

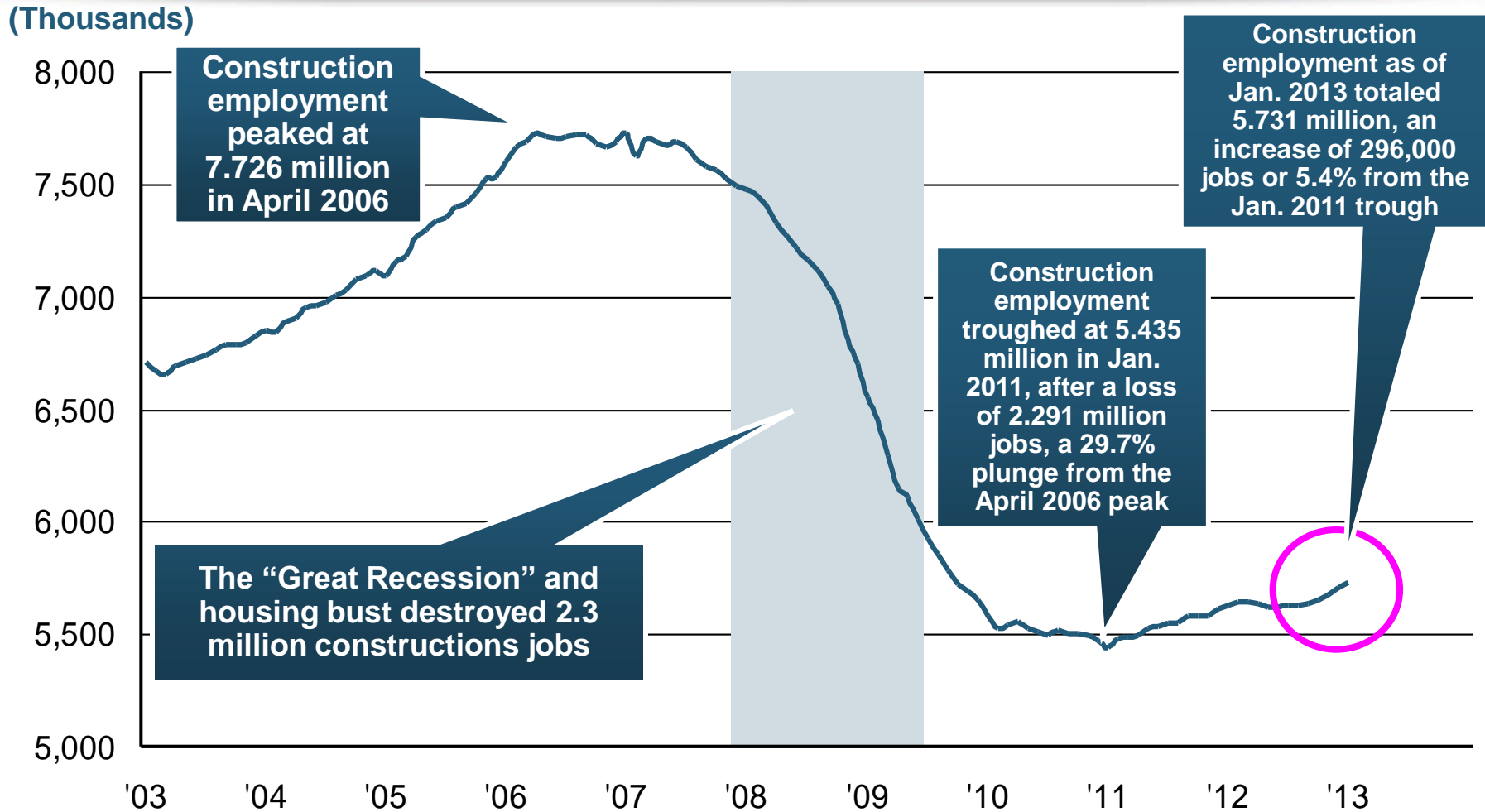
(Millions of Units)



**Homeowners Insurers Are Starting to See Meaningful Exposure Growth for the First Time Since 2005. Commercial Insurers with Construction Risk Exposure, Surety Also Benefit**



# Construction Employment, Jan. 2003–Jan. 2013



**The Construction Sector Could Be a Growth Leader in 2013 and 2014 as the Housing Market and Private Investment Recover. Commercial Insurers Will Benefit.**

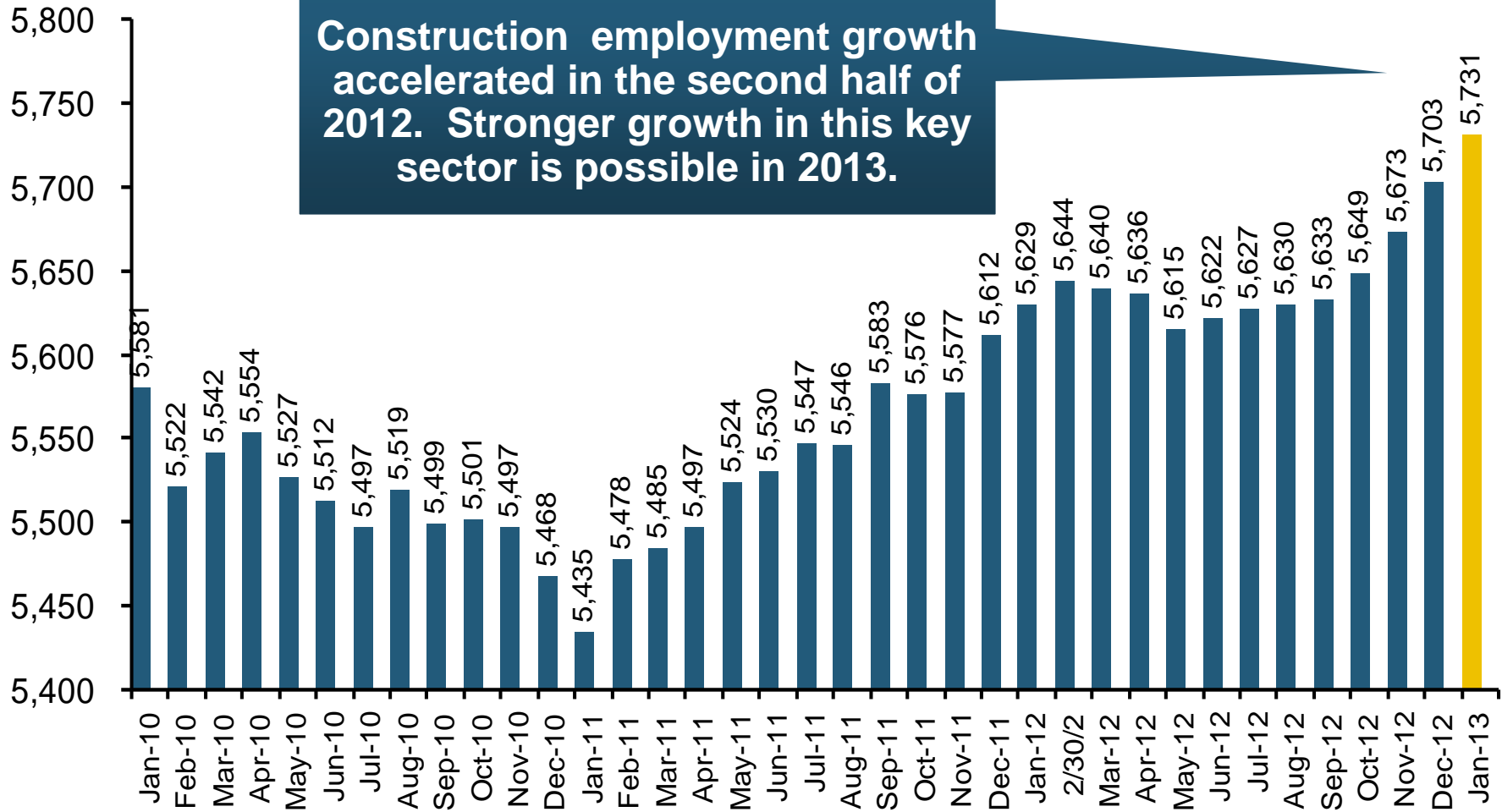
Note: Recession indicated by gray shaded column.

Sources: U.S. Bureau of Labor Statistics; Insurance Information Institute.

# Construction Employment, Jan. 2010—January 2013\*

(Thousands)

Construction employment growth accelerated in the second half of 2012. Stronger growth in this key sector is possible in 2013.



\*Seasonally adjusted

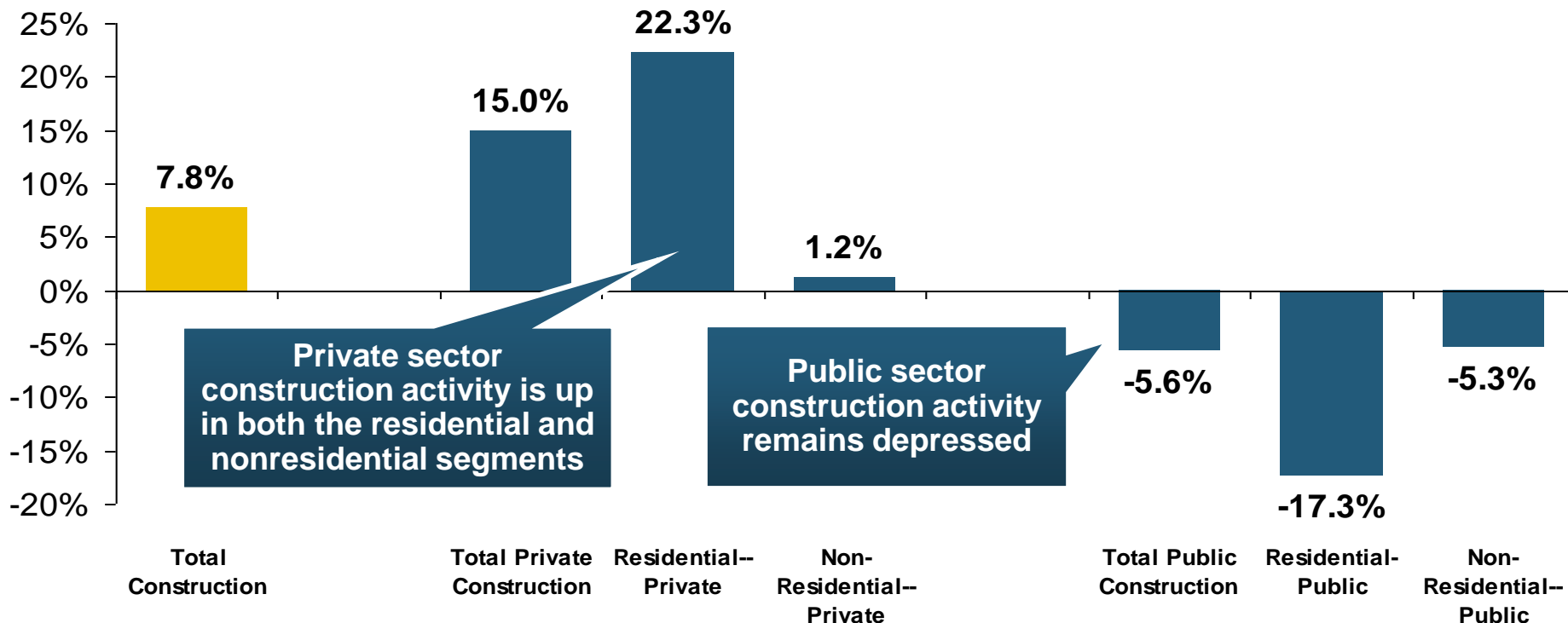
Sources: US Bureau of Labor Statistics at <http://data.bls.gov>; Insurance Information Institute.

# Value of Construction Put in Place, December 2012 vs. December 2011\*

Growth (%)

**Private: +15.0%**

**Public: -5.6%**



**Overall Construction Activity is Up, But Growth Is Entirely in the Private Sector as State/Local Government Budget Woes Continue**

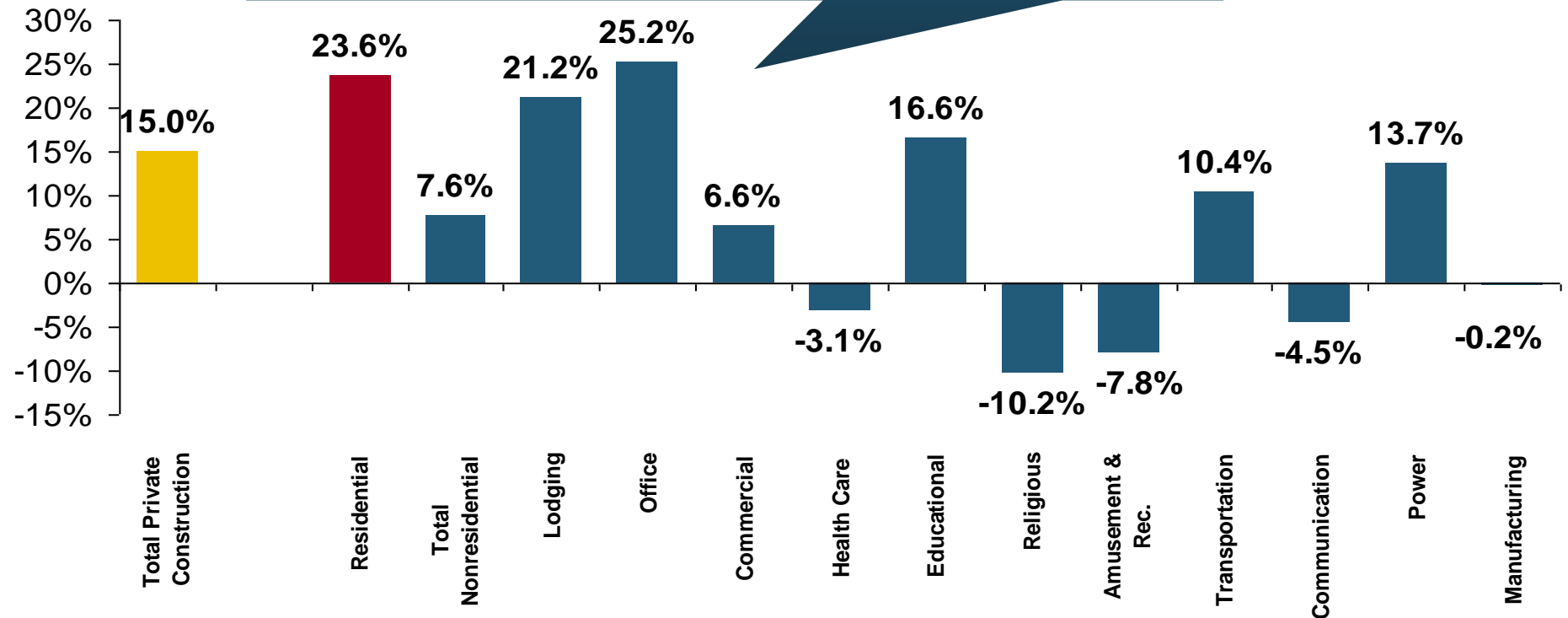
\*seasonally adjusted

Source: U.S. Census Bureau, <http://www.census.gov/construction/c30/c30index.html> ; Insurance Information Institute.

# Value of Private Construction Put in Place, by Segment, Dec. 2012 vs. Dec. 2011\*

Growth (%)

Led by the Residential Construction, Lodging, Office, Transportation and Power industries, Private sector construction activity is up across many segments after plunging during the “Great Recession”

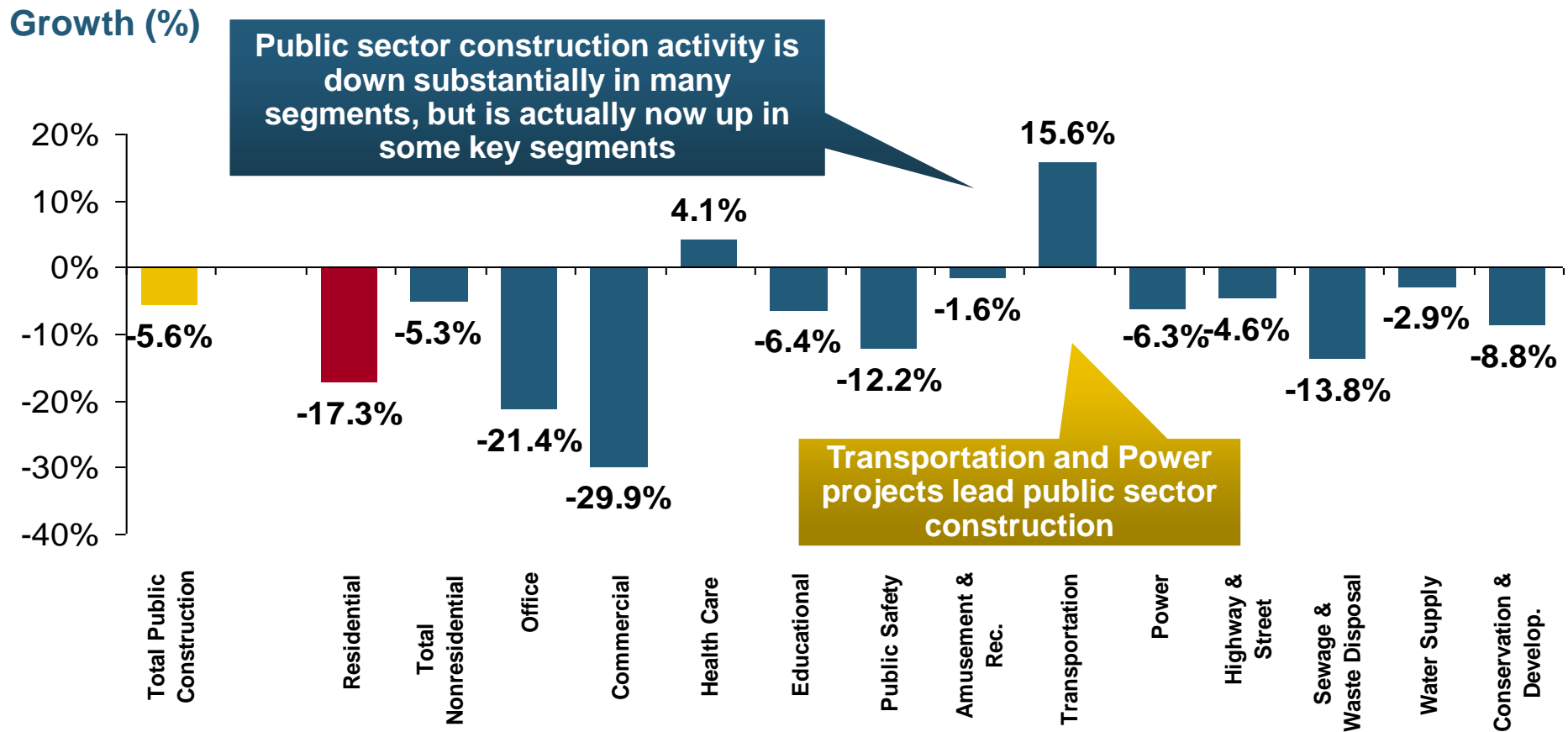


Private Construction Activity is Up in Most Segments, Including the Key Residential Construction Sector

\*seasonally adjusted

Source: U.S. Census Bureau, <http://www.census.gov/construction/c30/c30index.html> ; Insurance Information Institute.

# Value of Public Construction Put in Place, by Segment, Dec. 2012 vs. Dec. 2011\*



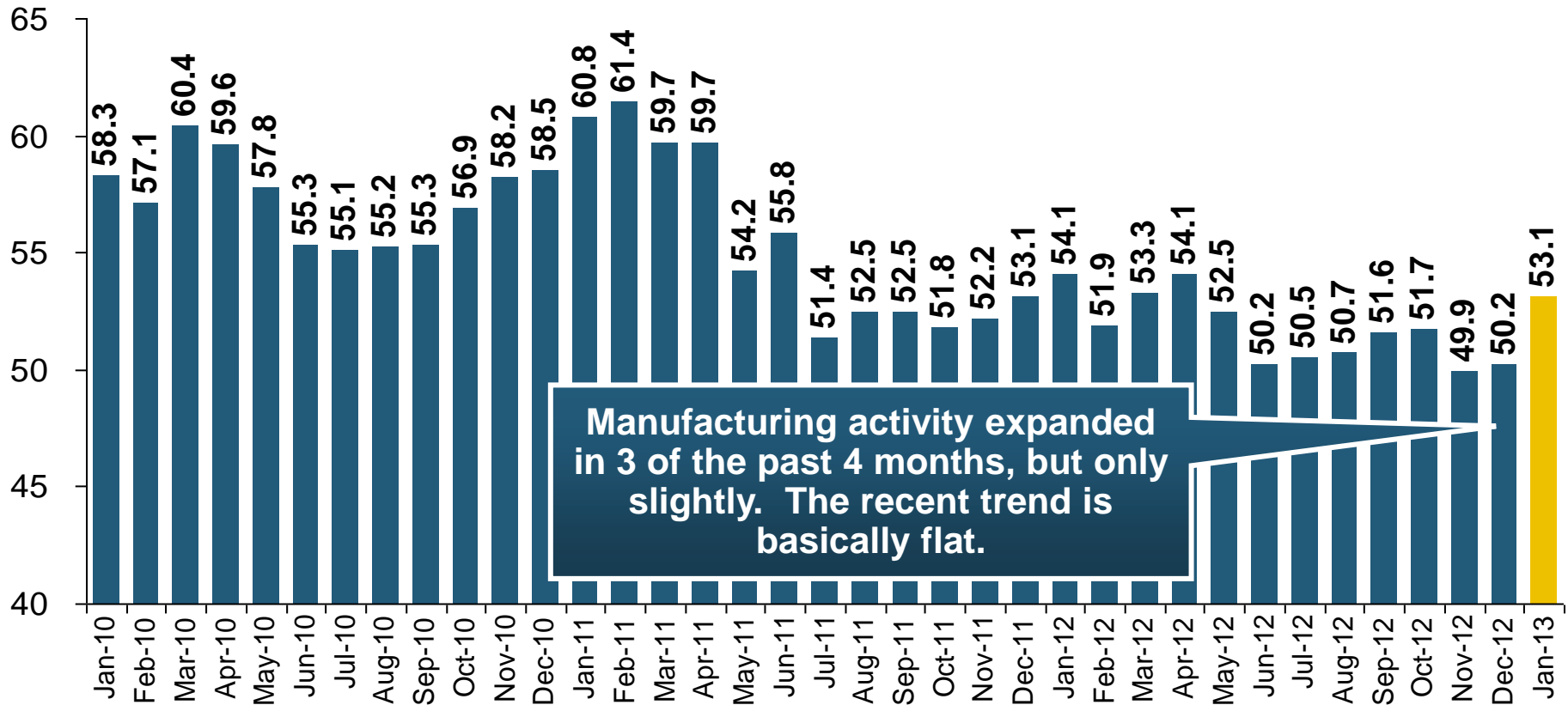
**Public Construction Activity is Down in Many Segments as State and Local Budgets Remain Under Stress; Improvement Possible in 2013.**

\*seasonally adjusted

Source: U.S. Census Bureau, <http://www.census.gov/construction/c30/c30index.html> ; Insurance Information Institute.

# ISM Manufacturing Index (Values > 50 Indicate Expansion)

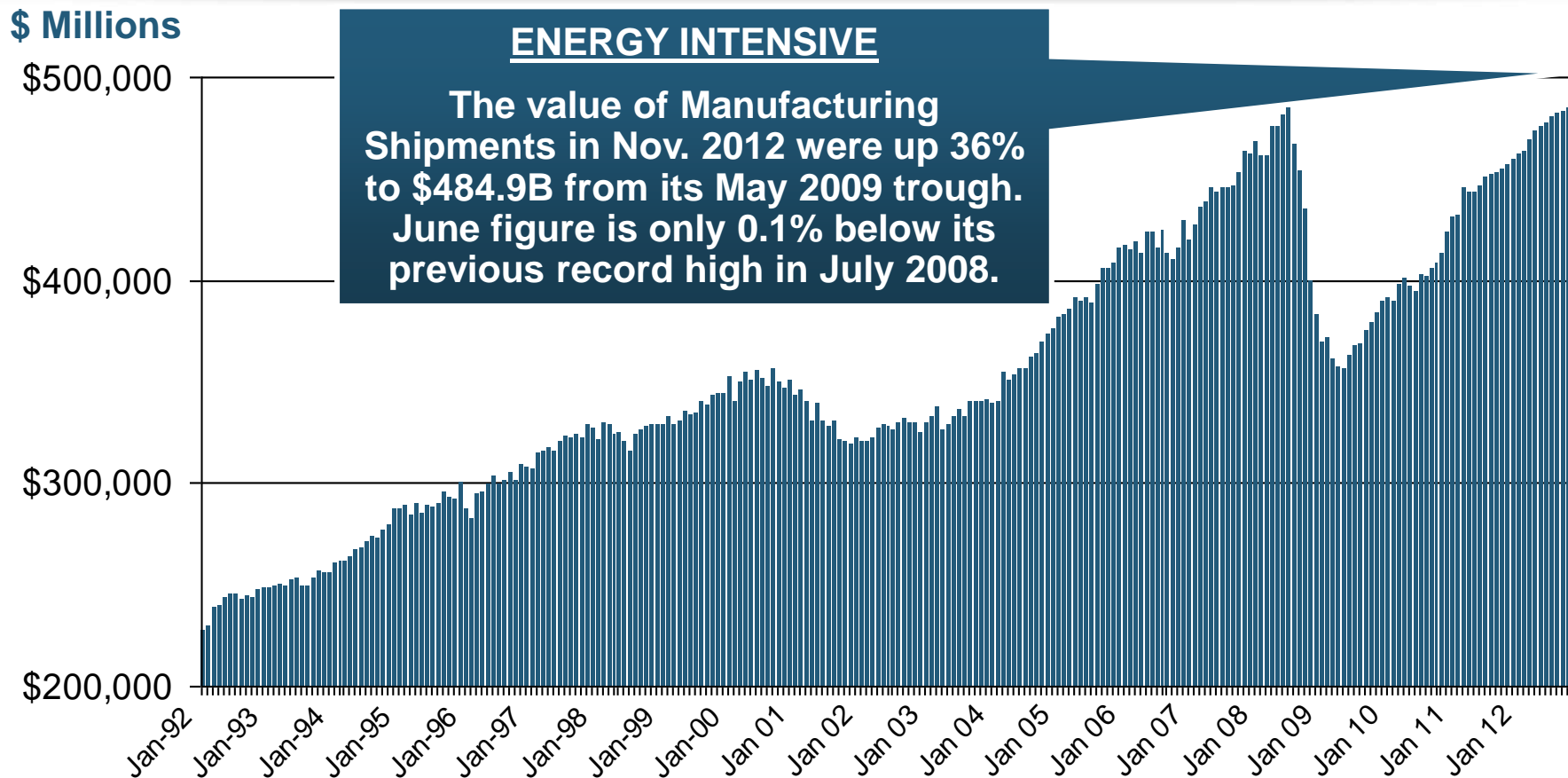
January 2010 through January 2013



The manufacturing sector expanded for 33 of the 37 months from Jan. 2010 through Jan. 2013. The question is whether this will continue.



# Dollar Value\* of Manufacturers' Shipments Monthly, Jan. 1992—Dec. 2012



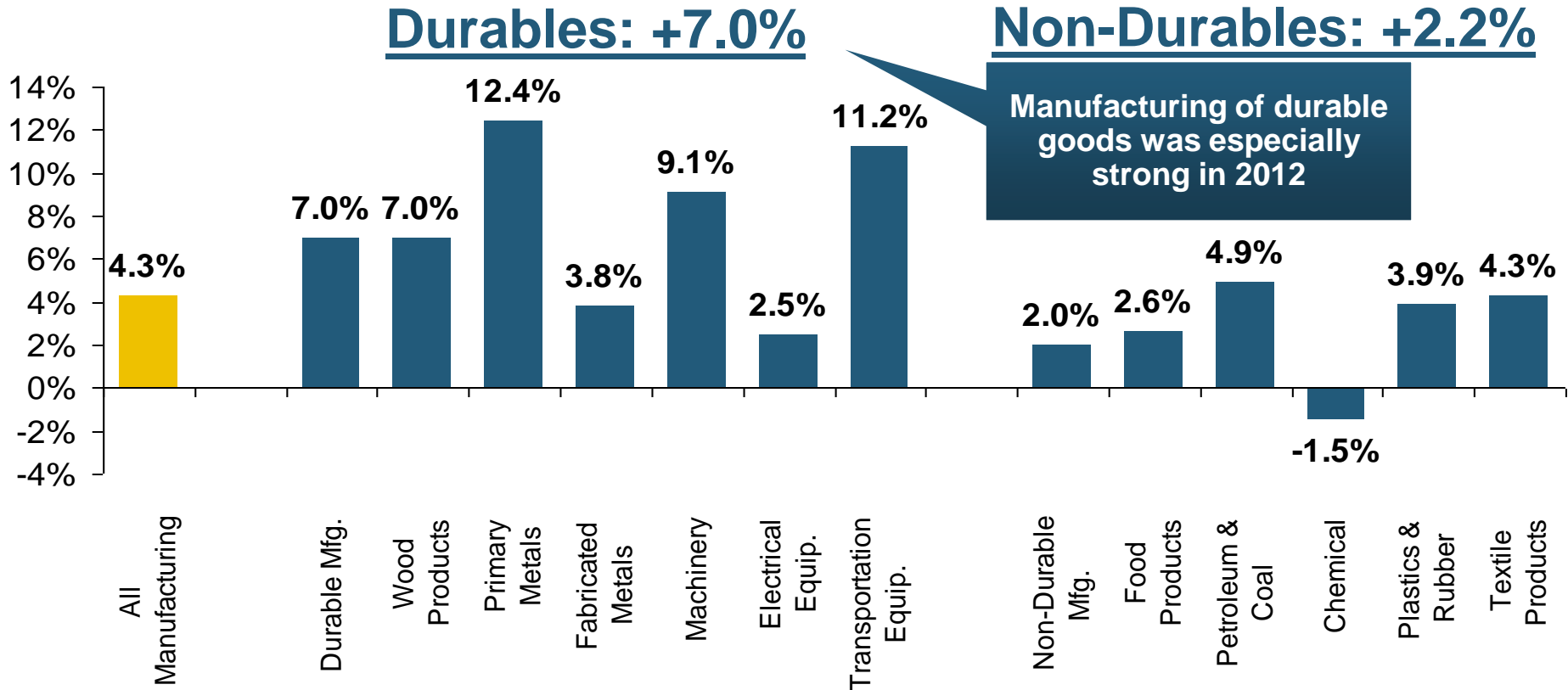
Monthly shipments are nearly back to peak (in July 2008, 8 months into the recession). Trough in May 2009. Growth from trough to Dec. 2012 was 36%. Manufacturing is an energy intensive activity and growth leads to gains in many commercial exposures: WC, Commercial Auto, Marine, Property and Various Liability Coverages

\*seasonally adjusted

Source: U.S. Census Bureau, *Full Report on Manufacturers' Shipments, Inventories, and Orders*, <http://www.census.gov/manufacturing/m3/>

# Manufacturing Growth for Selected Sectors, 2012 vs. 2011\*

Growth (%)



**Manufacturing Is Expanding Across a Wide Range of Sectors that Will Contribute to Growth in Insurable Exposures Including: WC, Commercial Property, Commercial Auto and Many Liability Coverages**

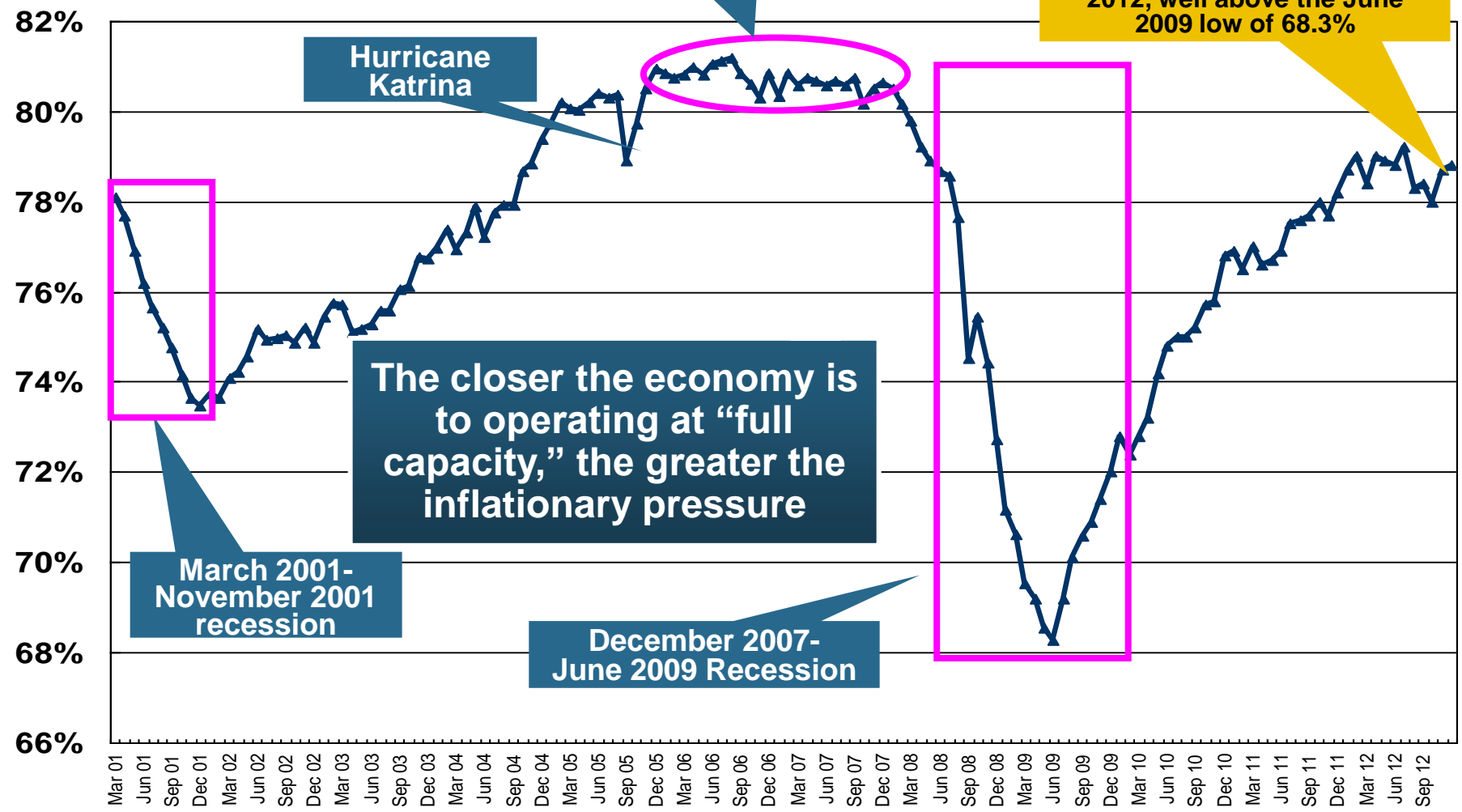
\*Seasonally adjusted; Date are YTD comparing data through December 2012 to the same period in 2011.

Source: U.S. Census Bureau, *Full Report on Manufacturers' Shipments, Inventories, and Orders*, <http://www.census.gov/manufacturing/m3/>

# Recovery in Capacity Utilization is a Positive Sign for Commercial Exposures

March 2001 through December 2012

Percent of Industrial Capacity

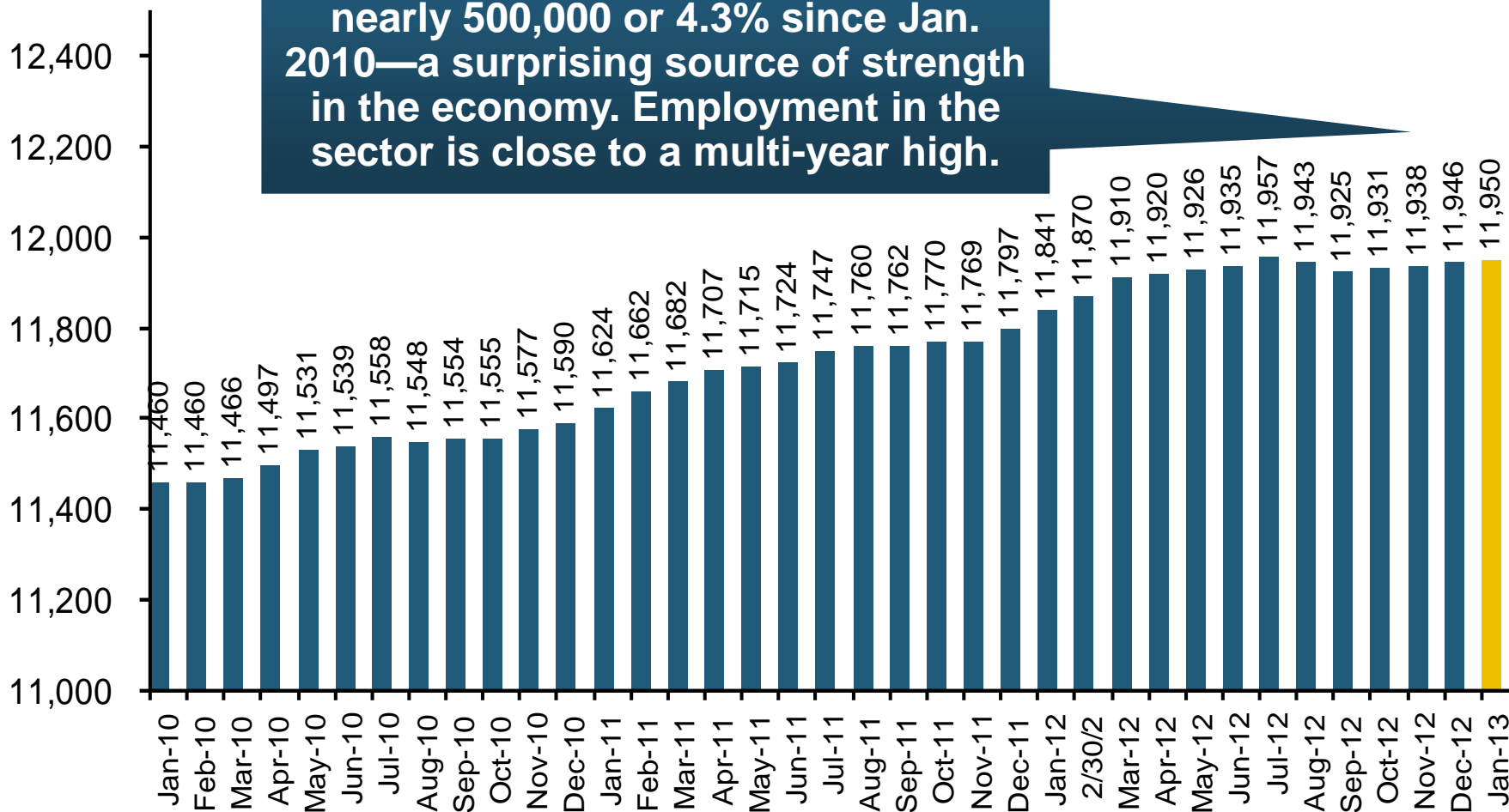


Source: Federal Reserve Board statistical releases at <http://www.federalreserve.gov/releases/q17/Current/default.htm>.

# Manufacturing Employment, Jan. 2010—January 2013\*

(Thousands)

Manufacturing employment is up by nearly 500,000 or 4.3% since Jan. 2010—a surprising source of strength in the economy. Employment in the sector is close to a multi-year high.

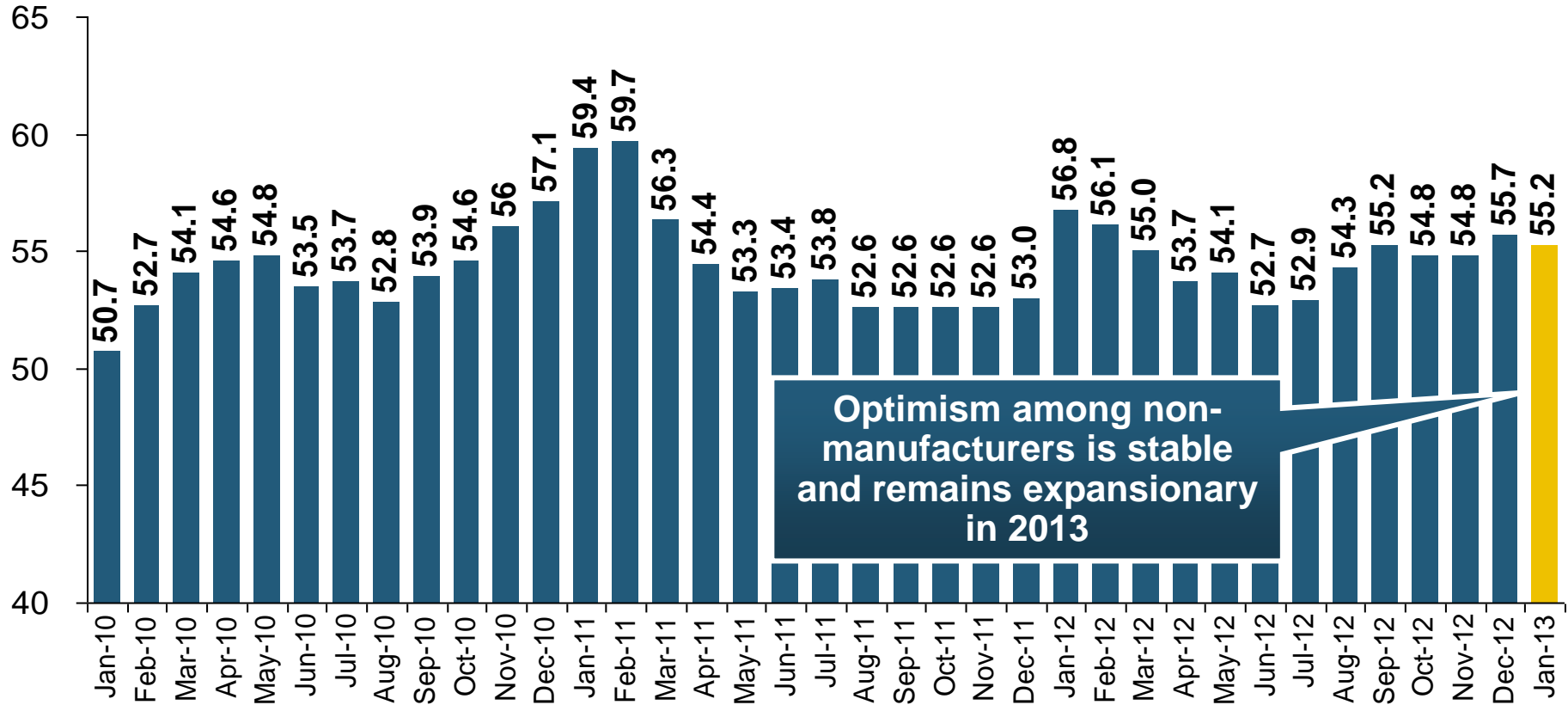


\*Seasonally adjusted

Sources: US Bureau of Labor Statistics at <http://data.bls.gov>; Insurance Information Institute.

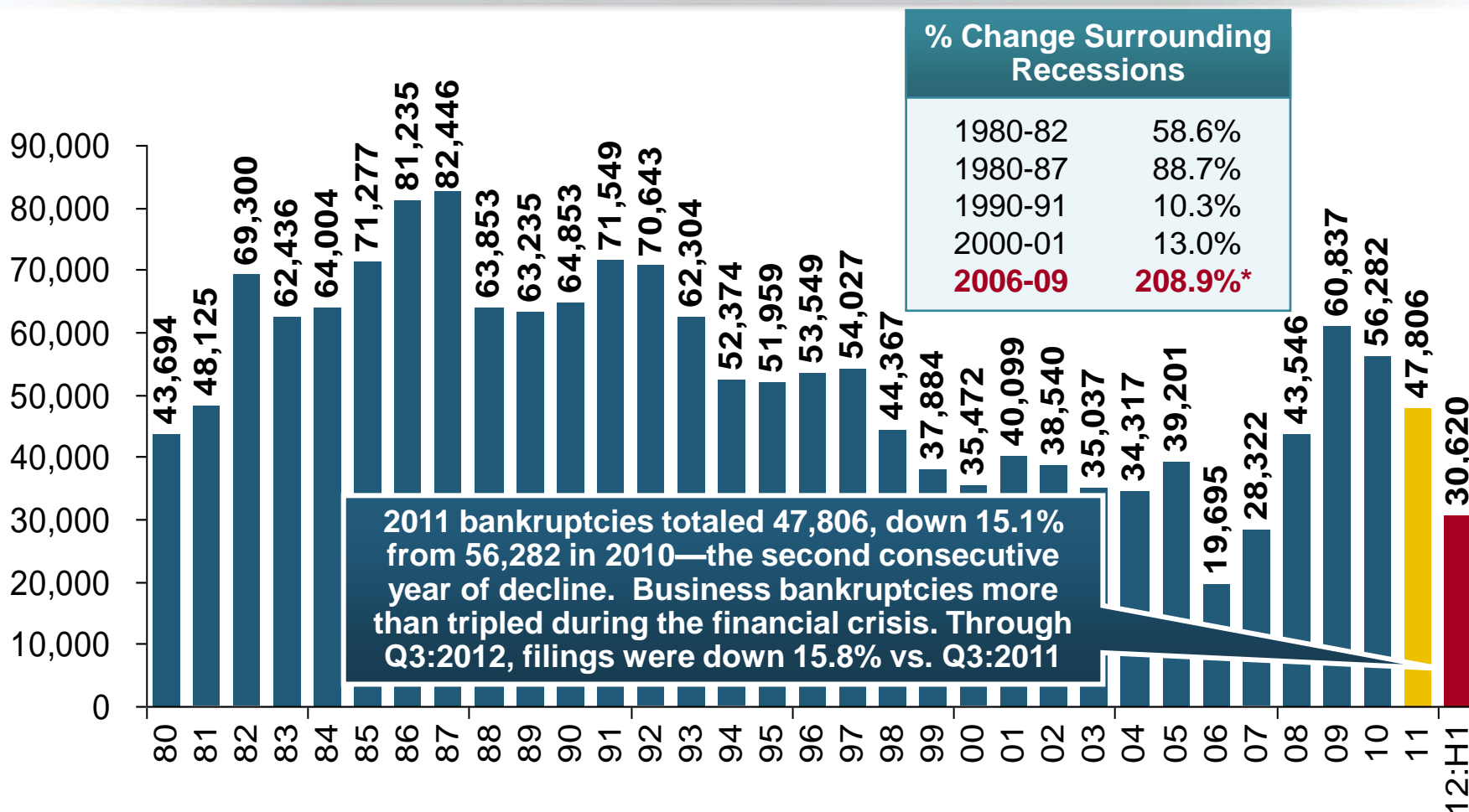
# ISM Non-Manufacturing Index (Values > 50 Indicate Expansion)

January 2010 through January 2013



**Non-manufacturing industries have been expanding and adding jobs. The question is whether this will continue.**

# Business Bankruptcy Filings, 1980-2012:Q3

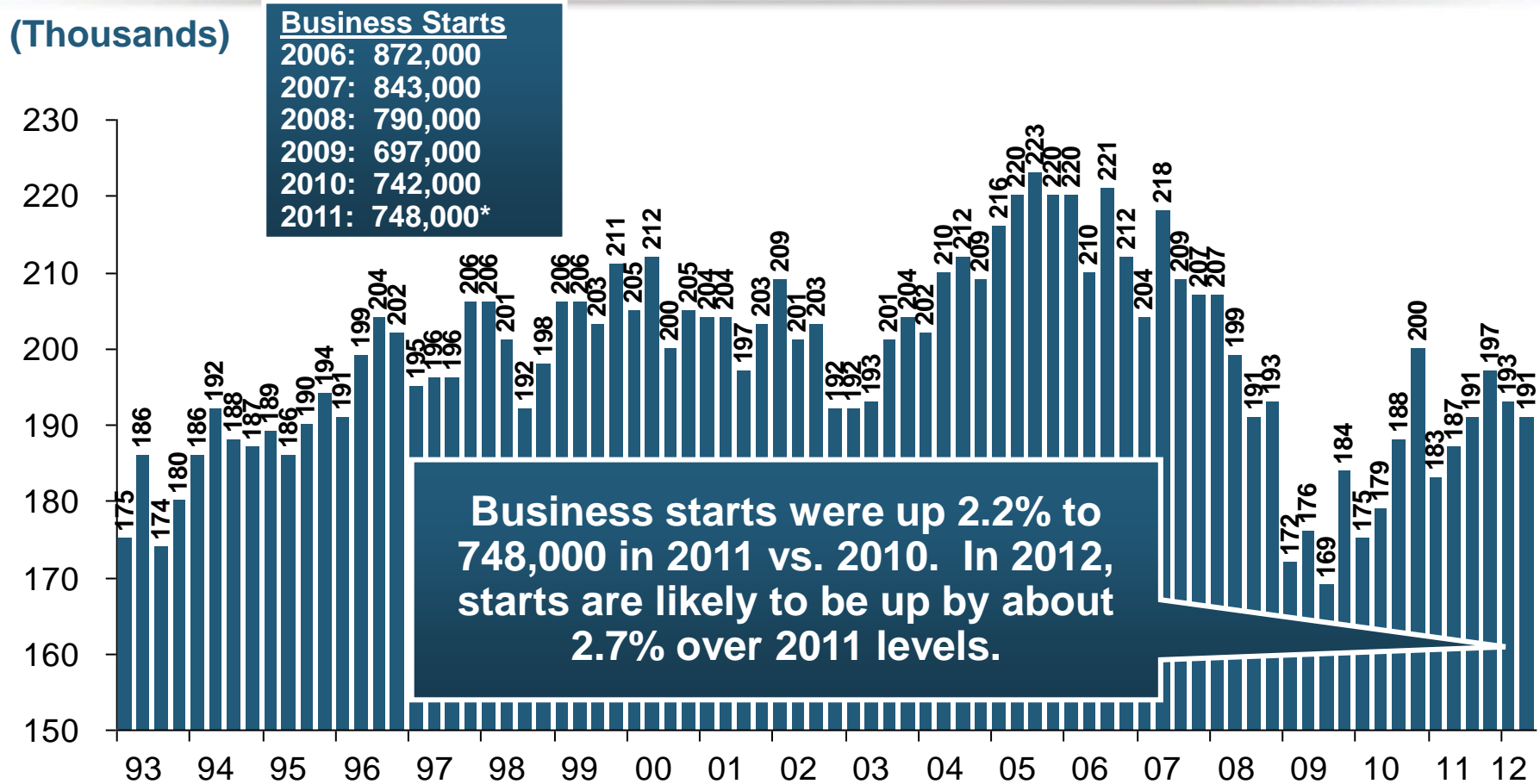


**Significant Exposure Implications for All Commercial Lines as Business Bankruptcies Begin to Decline**

Sources: American Bankruptcy Institute at <http://www.abiworld.org/AM/AMTemplate.cfm?Section=Home&TEMPLATE=/CM/ContentDisplay.cfm&CONTENTID=61633>; Insurance Information Institute



# Private Sector Business Starts, 1993:Q2 – 2012:Q2\*



**Business Starts Were Down Nearly 20% in the Recession, Holding Back Most Types of Commercial Insurance Exposure, But Are Recovering Slowly**

\* Data through Jun. 30, 2012 are the latest available as of Feb. 6, 2013; Seasonally adjusted.

Source: Bureau of Labor Statistics, <http://www.bls.gov/news.release/cewbd.t08.htm>.

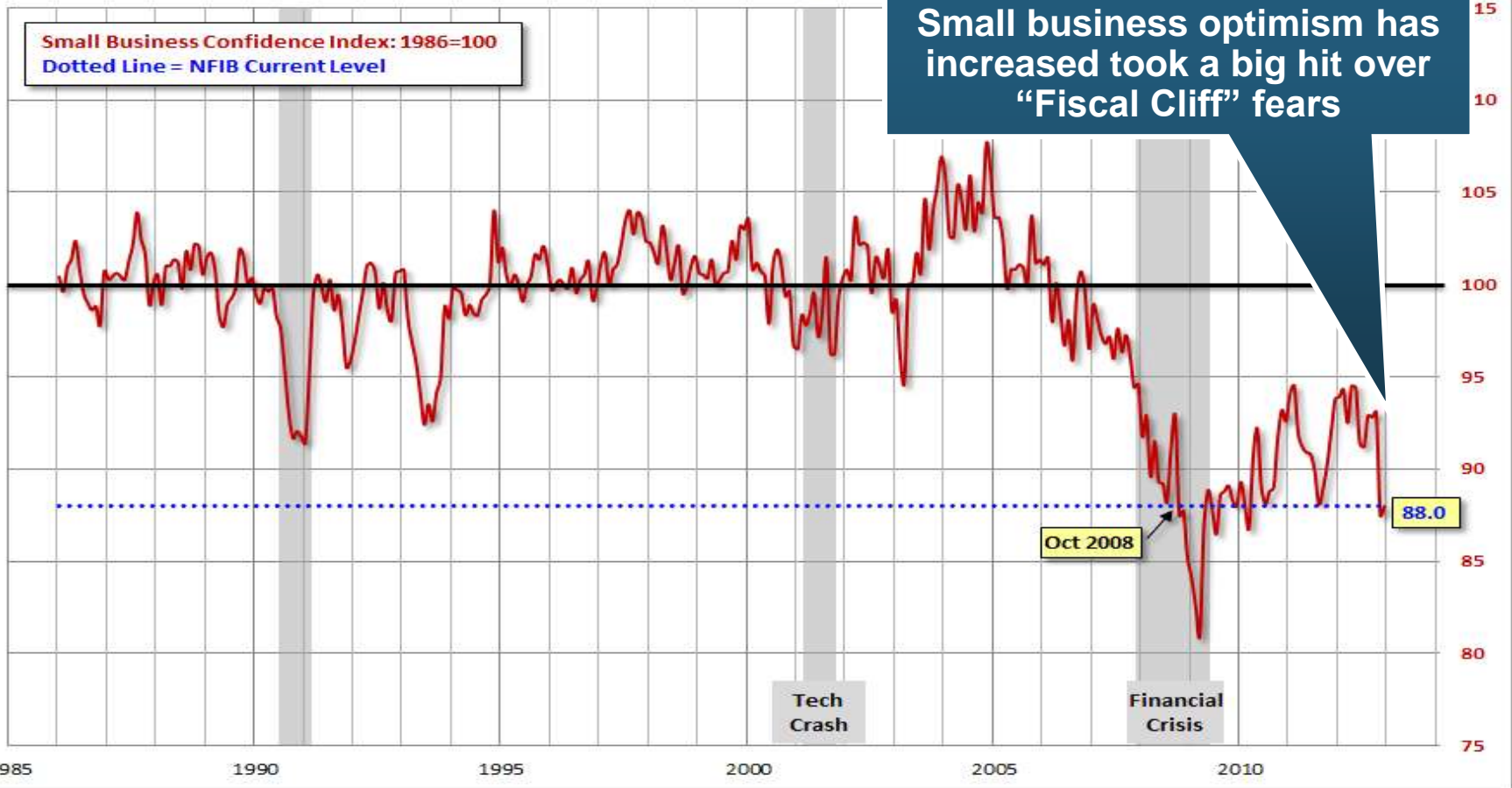
# NFIB Small Business Optimism Index

January 1985 through December 2012

Data through  
December 2012

NFIB Small Business Optimism Index  
with Recessions Highlighted

dshort.com  
January 2013



# 12 Industries for the Next 10 Years: Insurance Solutions Needed

Health Care

Health Sciences

Energy (Traditional)

Alternative Energy

Petrochemical

Agriculture

Natural Resources


Technology (incl. Biotechnology)

Light Manufacturing

Inourced Manufacturing

Export-Oriented Industries

Shipping (Rail, Marine, Trucking)



Many industries are poised for growth, though insurers' ability to capitalize on these industries varies widely

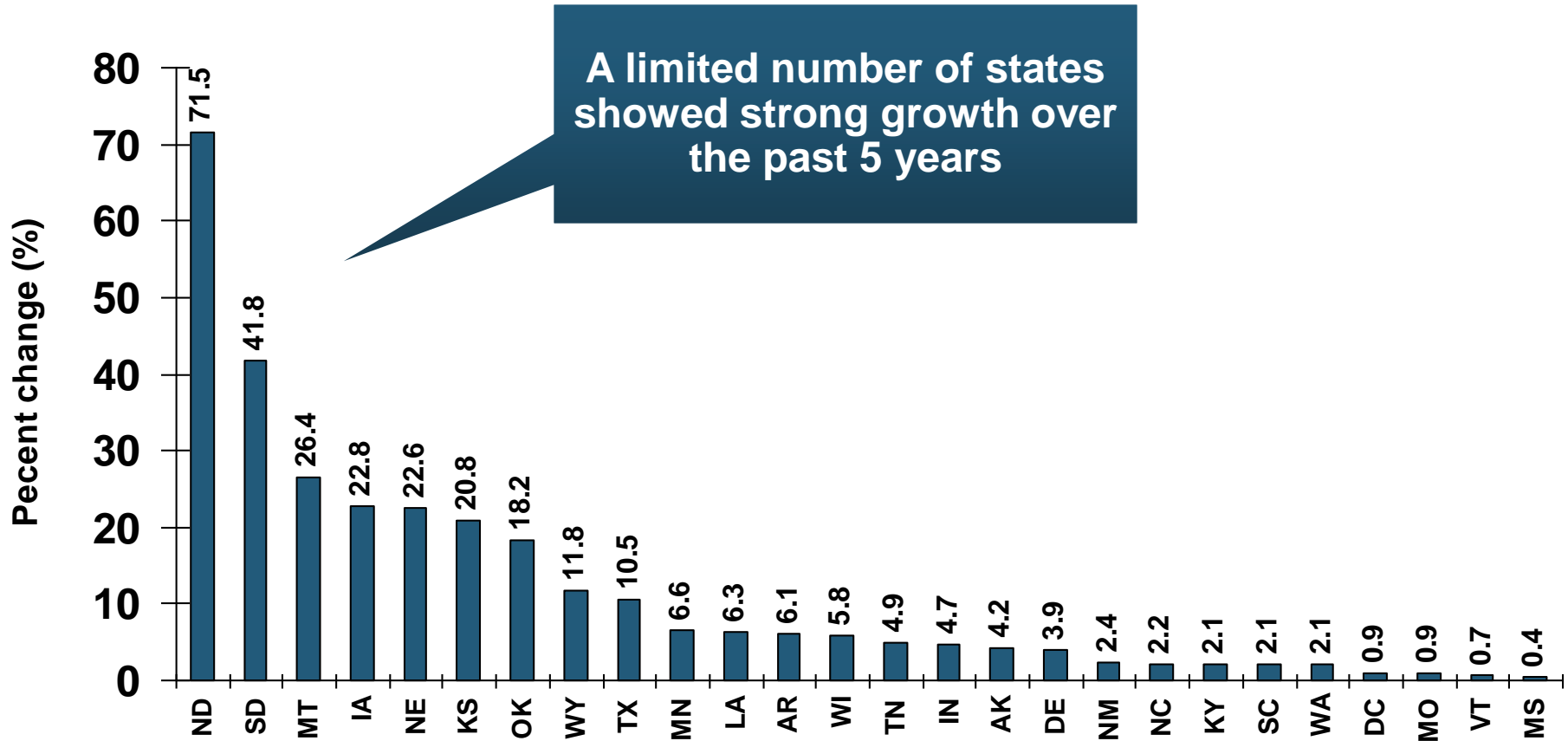


# Growth Analysis by State and Business Segment

**Premium Growth Rates Vary Tremendously by State**

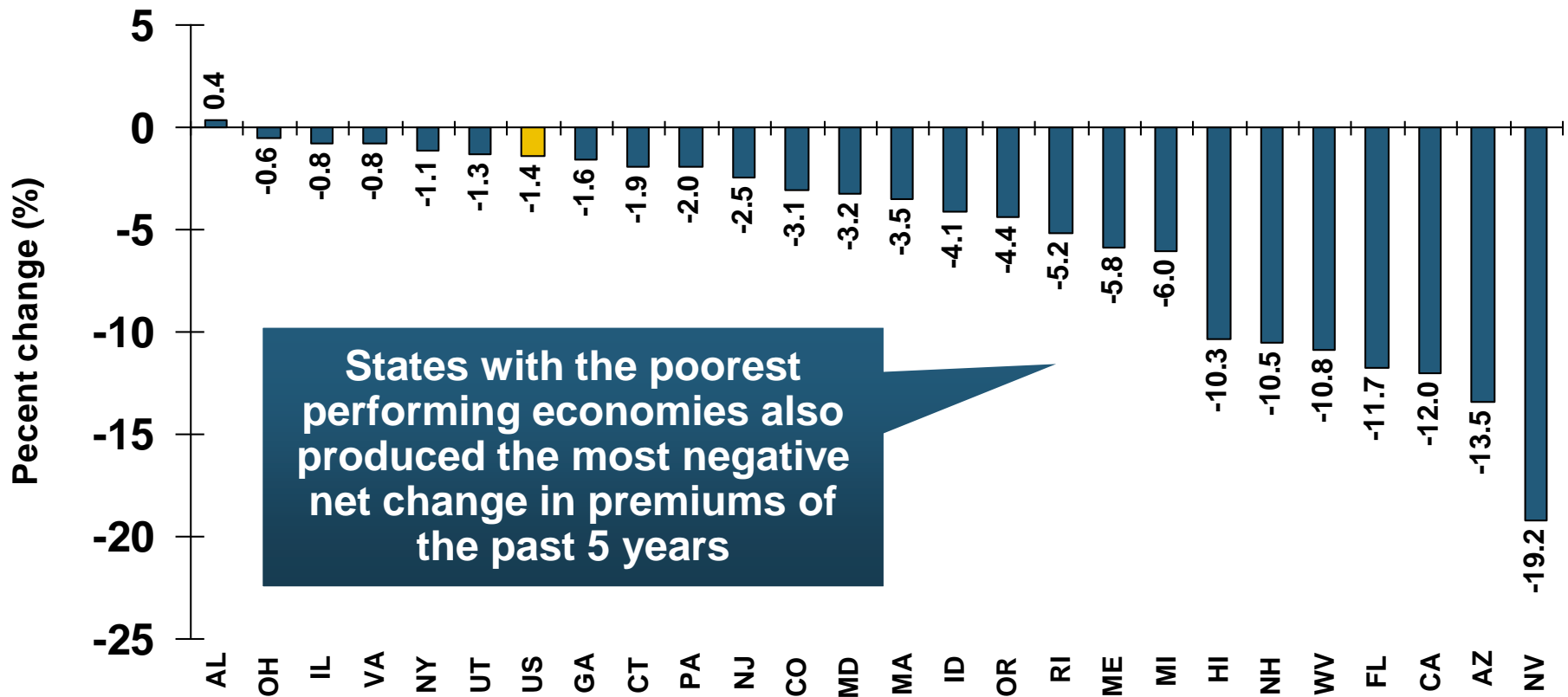
# Direct Premiums Written: Total P/C Percent Change by State, 2006-2011\*

## Top 25 States



# Direct Premiums Written: Total P/C Percent Change by State, 2006-2011\*

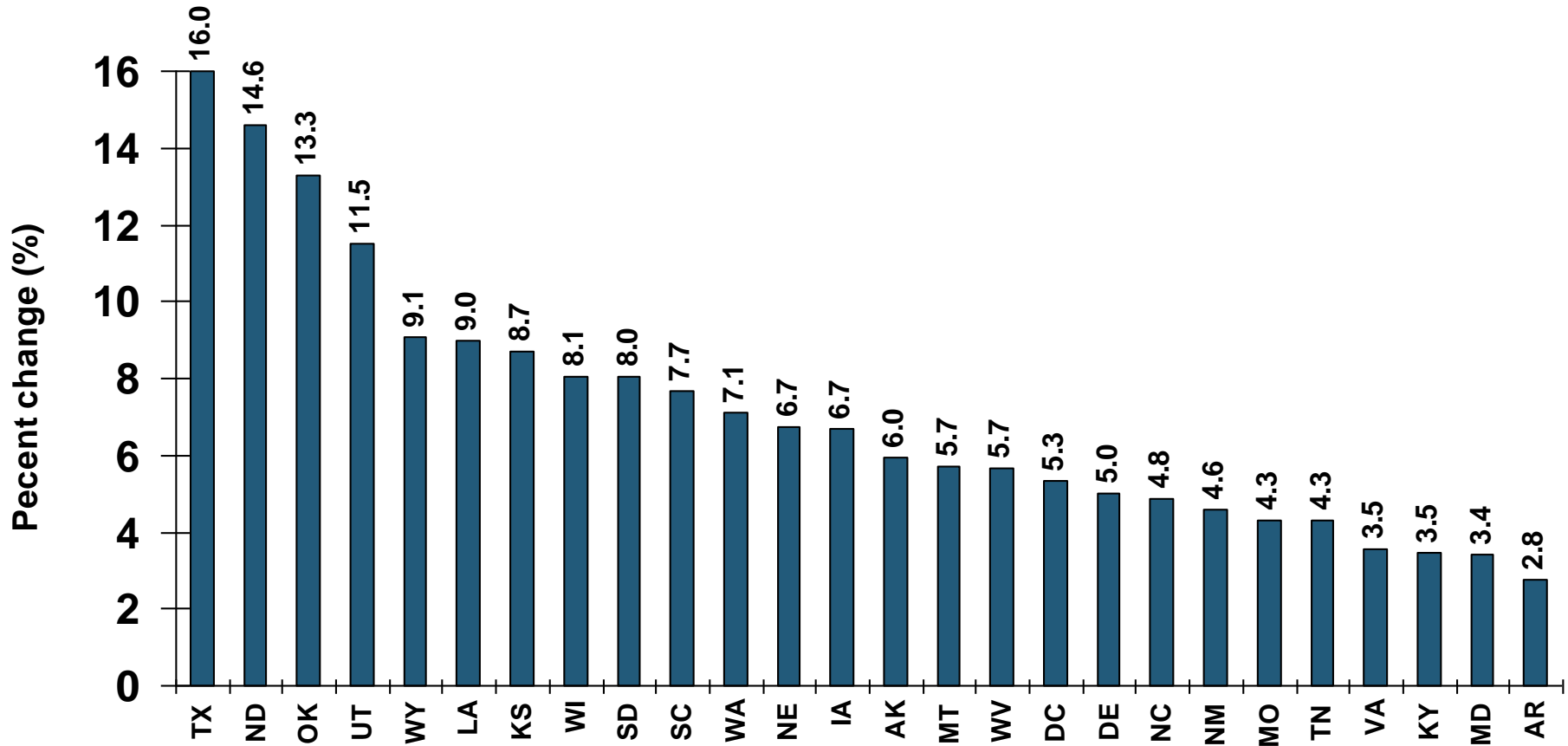
## Bottom 25 States





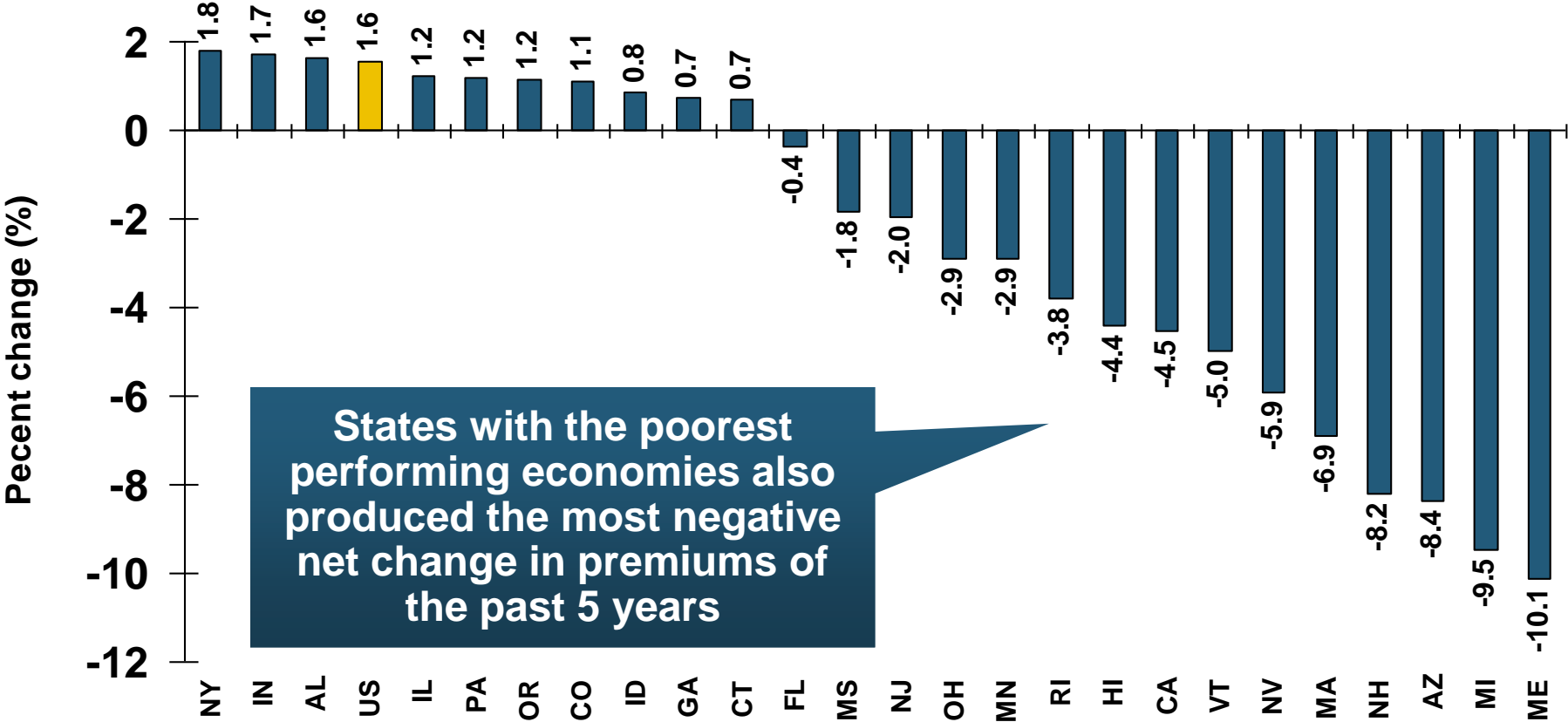
# Direct Premiums Written: PP Auto Percent Change by State, 2006-2011\*

## Top 25 States



# Direct Premiums Written: PP Auto Percent Change by State, 2006-2011\*

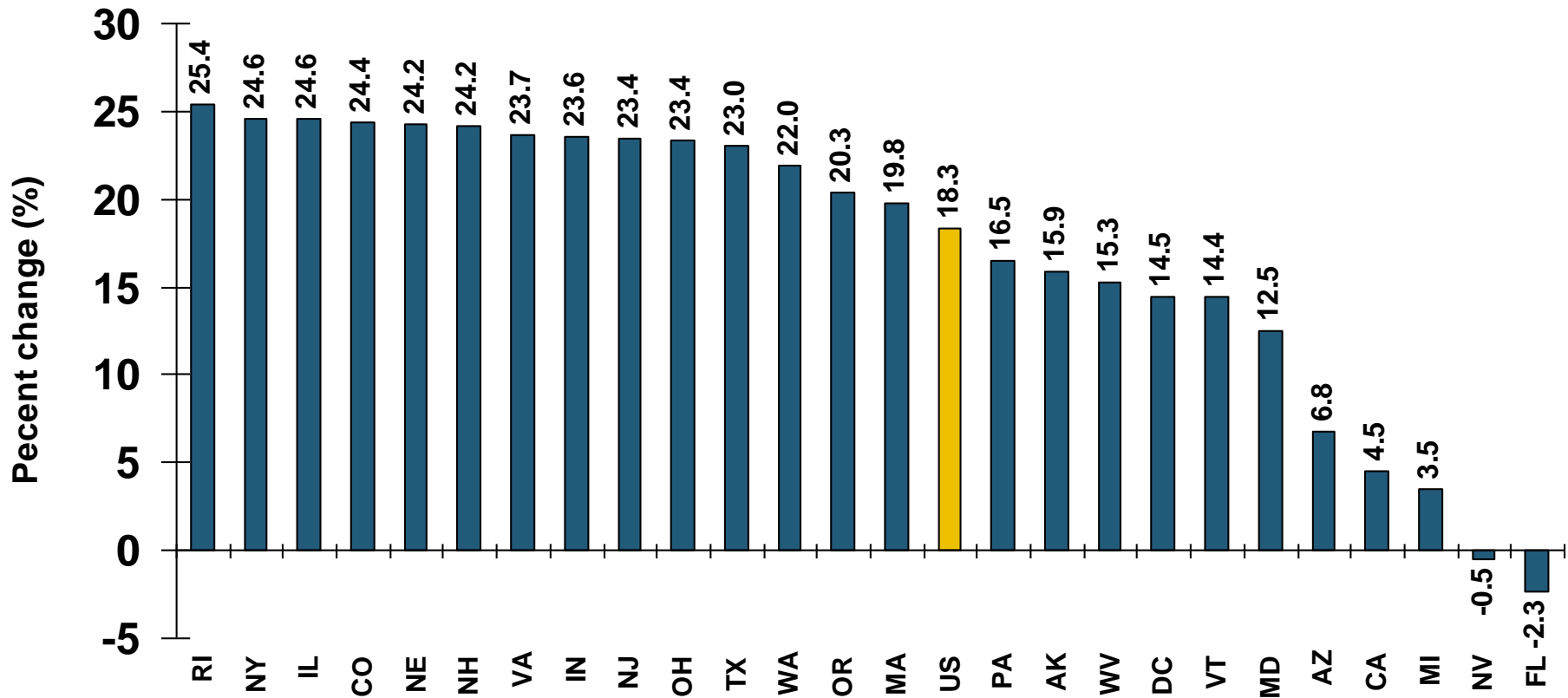
## Bottom 25 States



Sources: SNL Financial LC.; Insurance Information Institute.

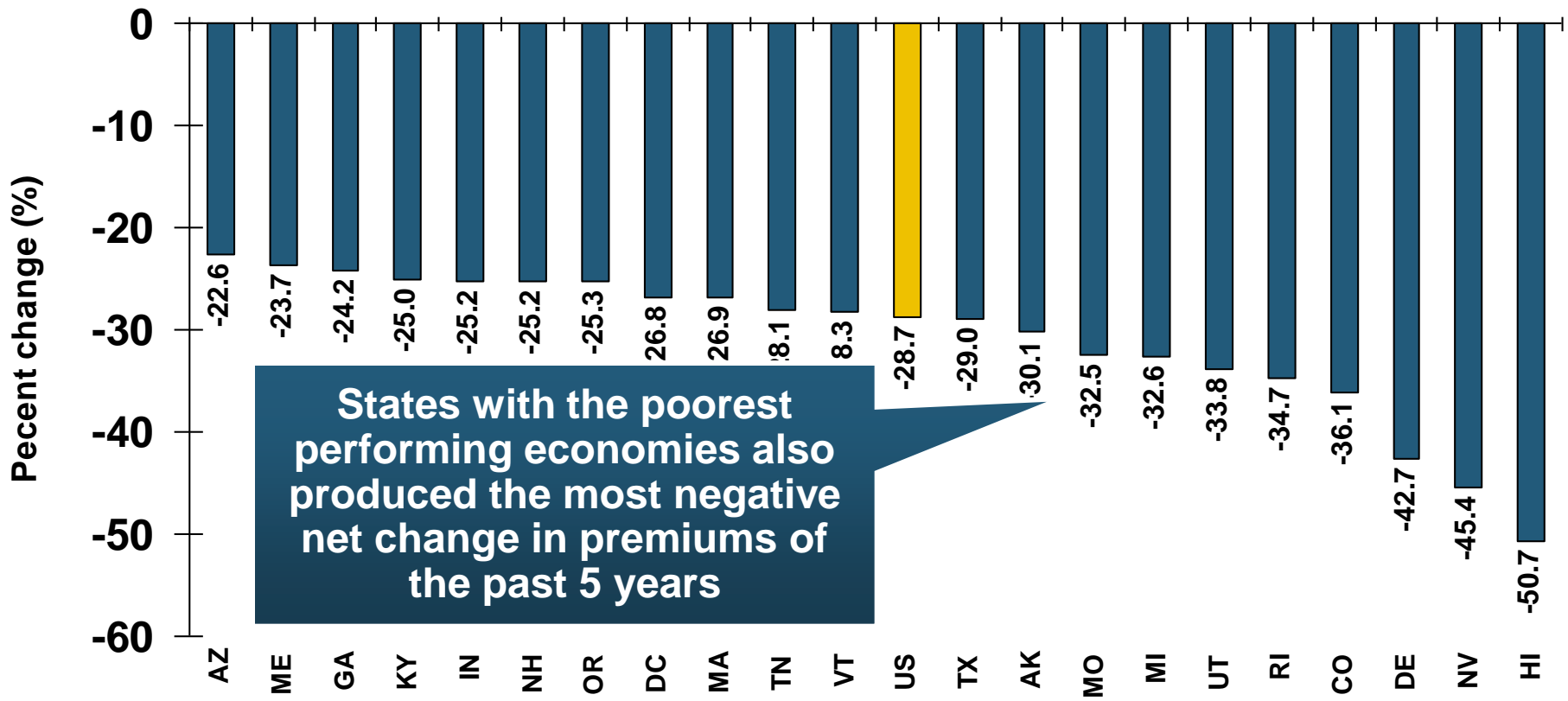
# Direct Premiums Written: Homeowners Percent Change by State, 2006-2011\*

## Top 25 States



# Direct Premiums Written: Homeowners Percent Change by State, 2006-2011\*

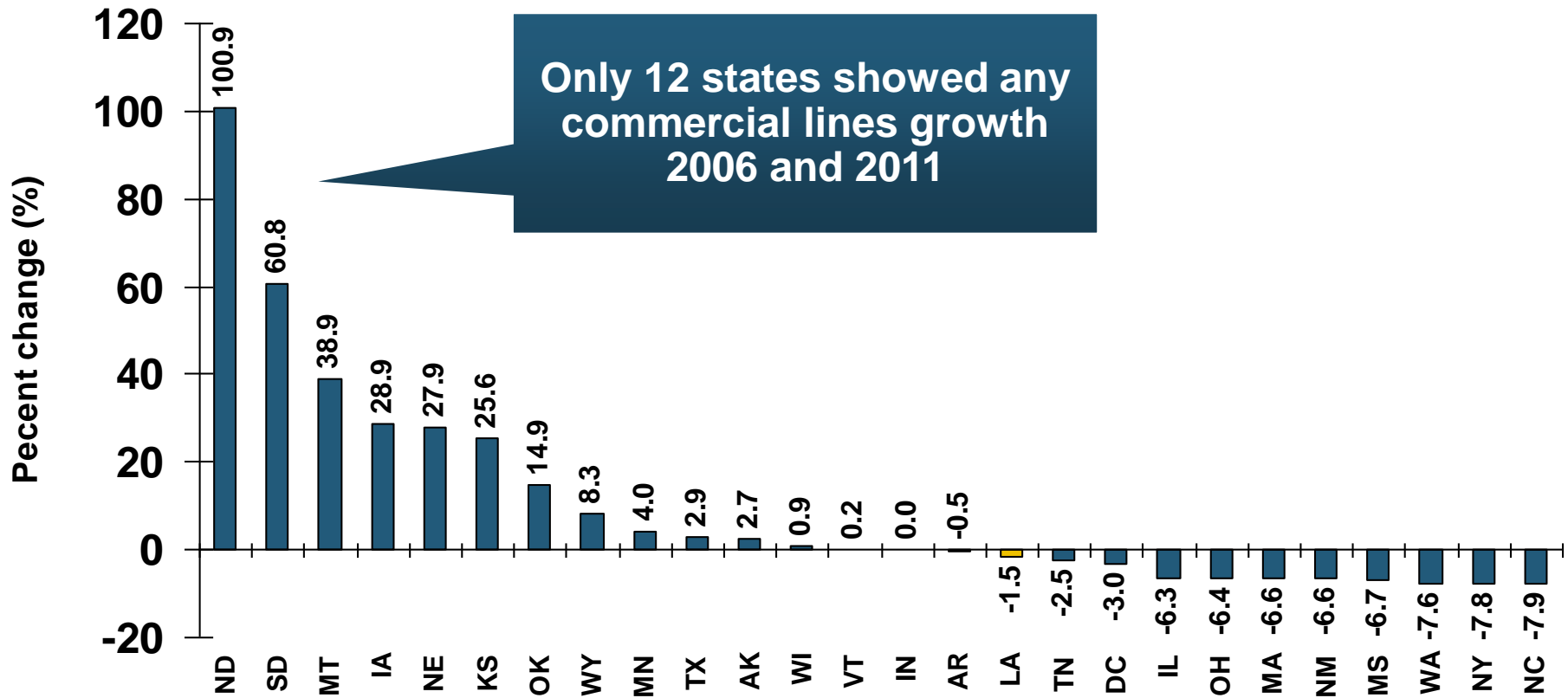
## Bottom 25 States



Sources: SNL Financial LC.; Insurance Information Institute.

# Direct Premiums Written: Comm. Lines Percent Change by State, 2006-2011\*

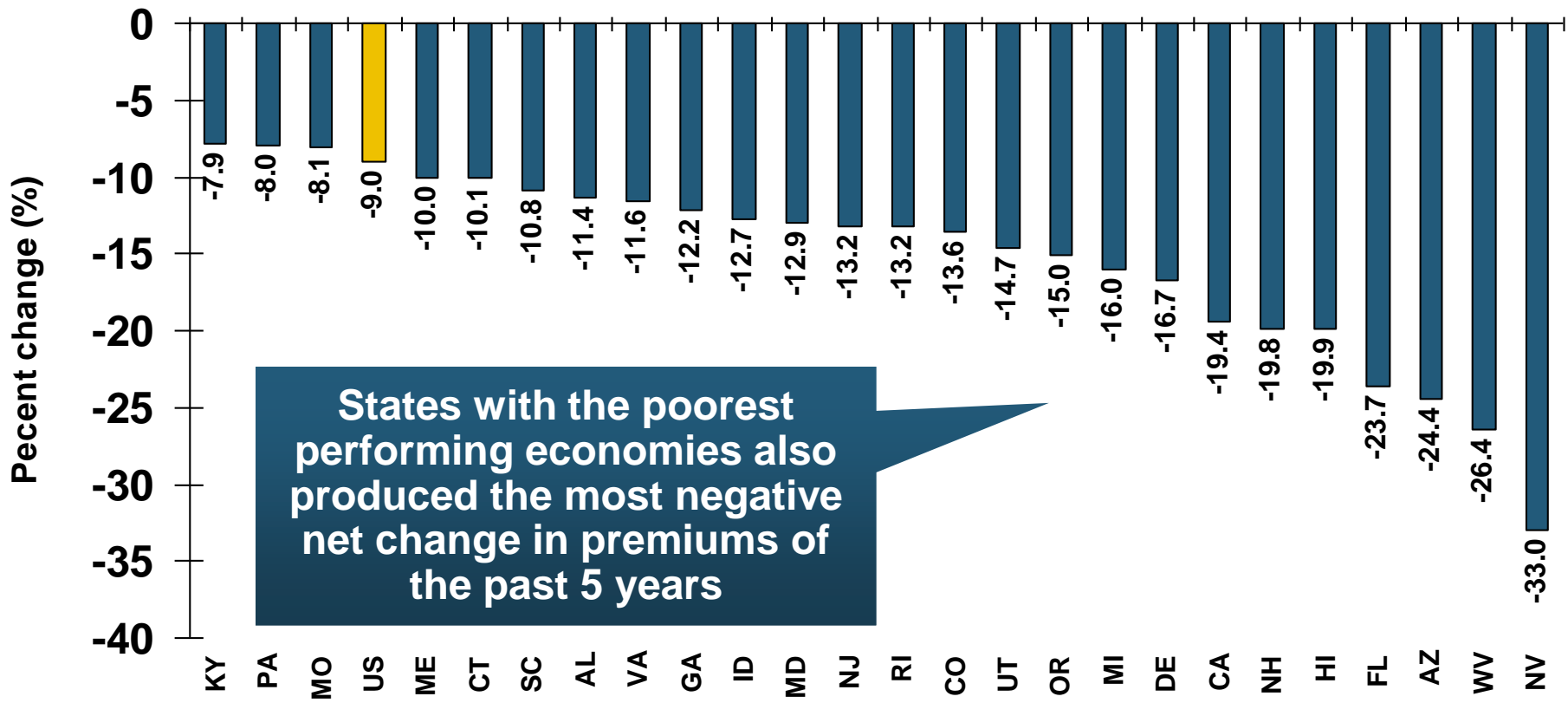
## Top 25 States



Sources: SNL Financial LC.; Insurance Information Institute.

# Direct Premiums Written: Comm. Lines Percent Change by State, 2006-2011\*

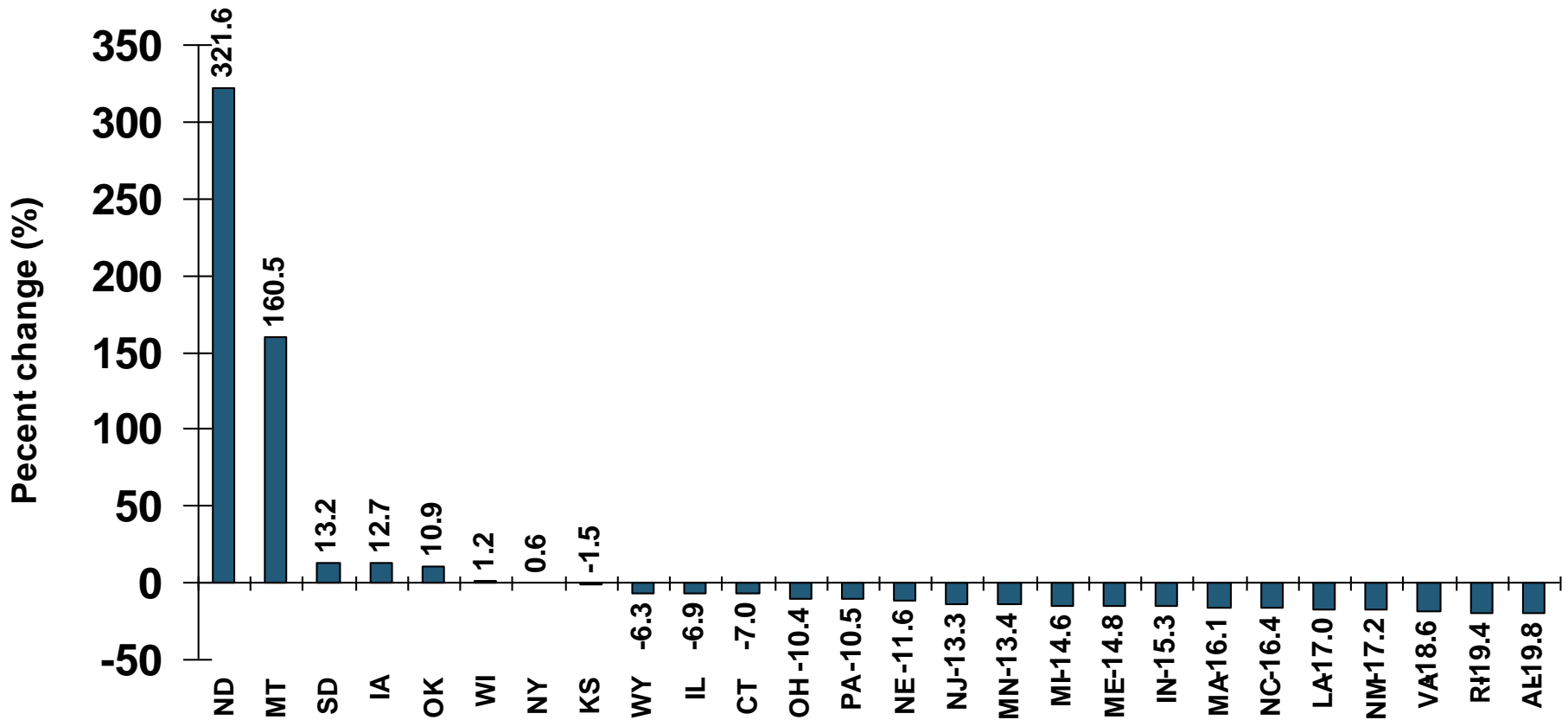
## Bottom 25 States



Sources: SNL Financial LC.; Insurance Information Institute.

# Direct Premiums Written: Workers' Comp Percent Change by State, 2006-2011\*

## Top 25 States

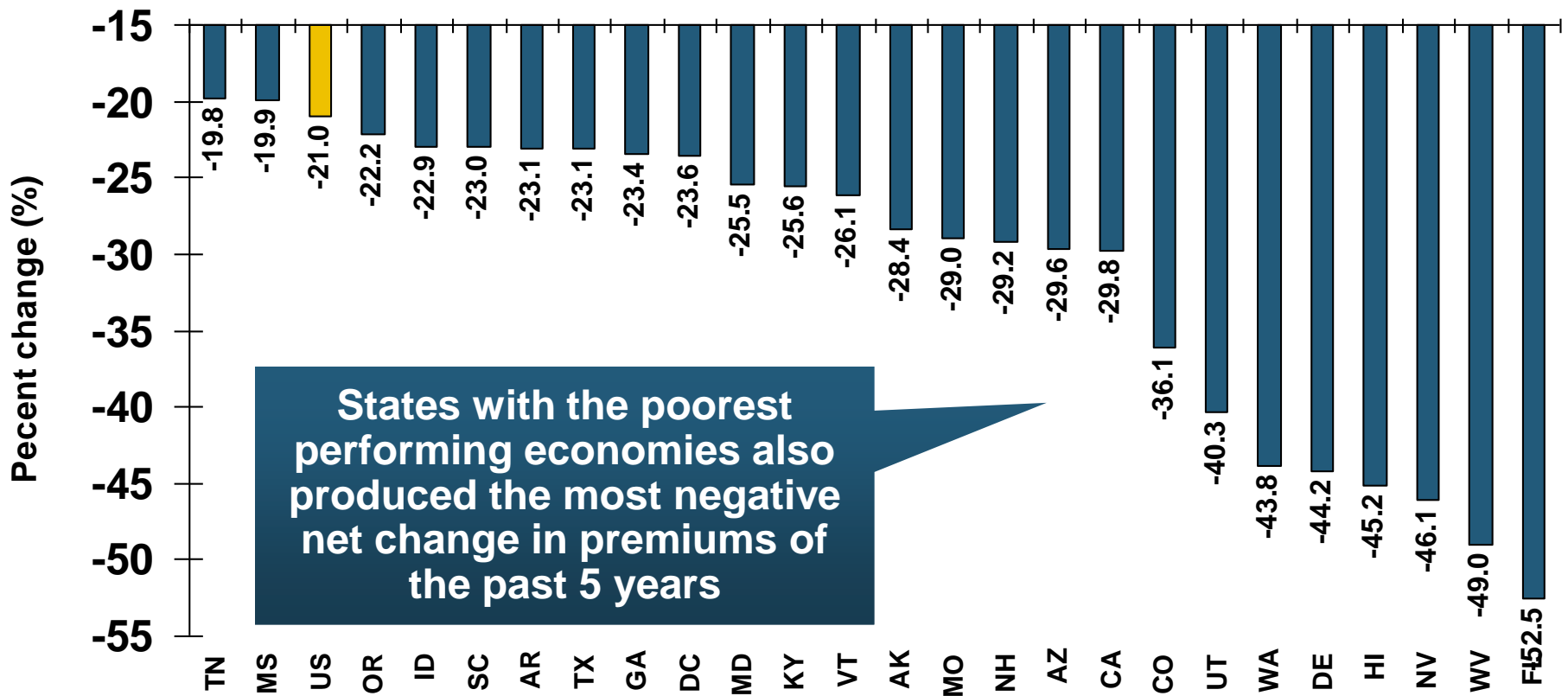


\*Excludes monopolistic fund states: ND, OH, WA, WY as well as WV, which transitioned to a competitive structure during this period.

Sources: SNL Financial LC.; Insurance Information Institute.

# Direct Premiums Written: Worker's Comp Percent Change by State, 2006-2011\*

## Bottom 25 States



\*Excludes monopolistic fund states: ND, OH, WA, WY as well as WV, which transitioned to a competitive structure during this period.

Sources: SNL Financial LC.; Insurance Information Institute.

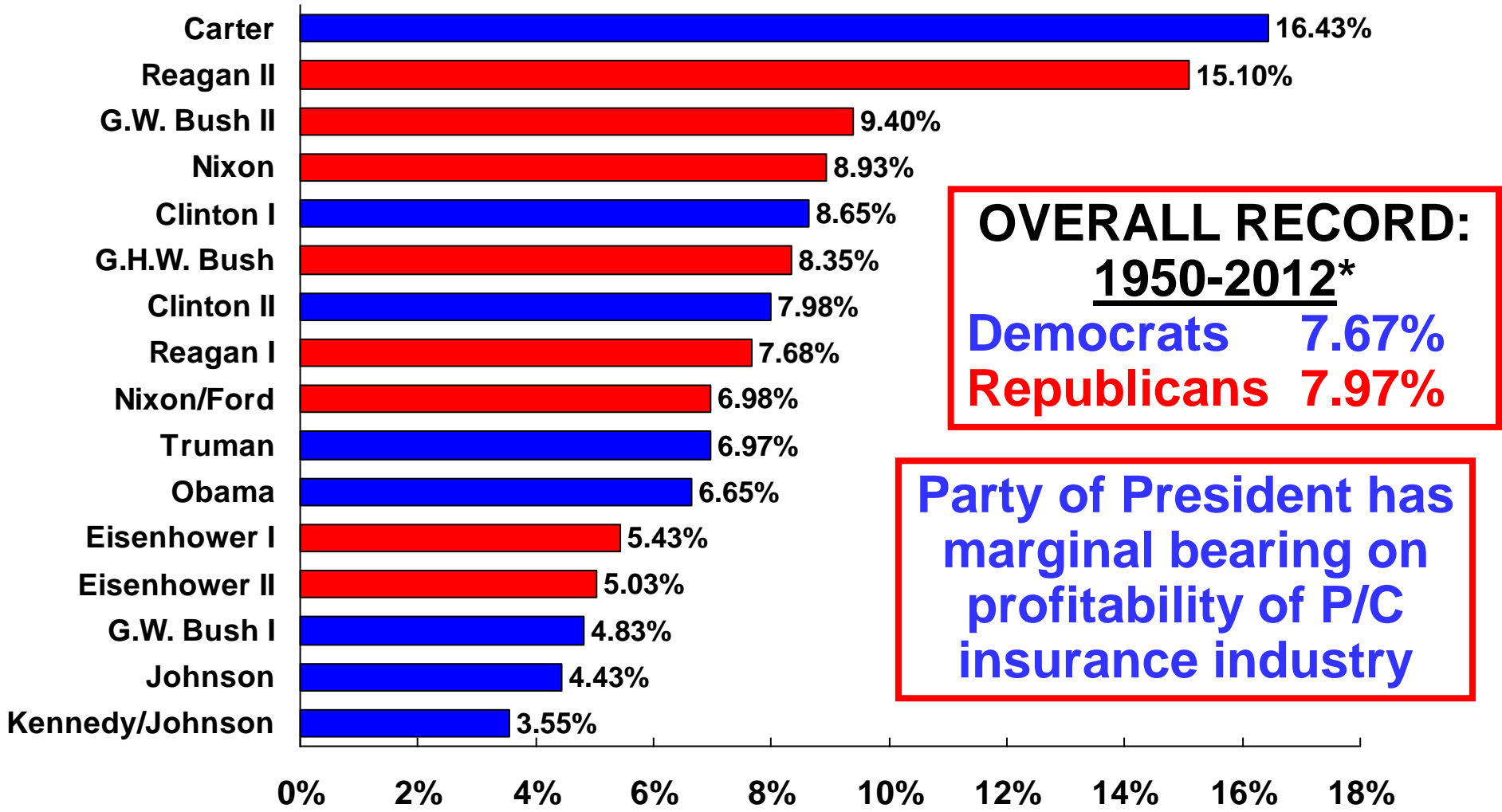




# Presidential Politics & the P/C Insurance Industry

## How Is Profitability Affected by the President's Political Party?

# P/C Insurance Industry ROE by Presidential Administration, 1950- 2012\*

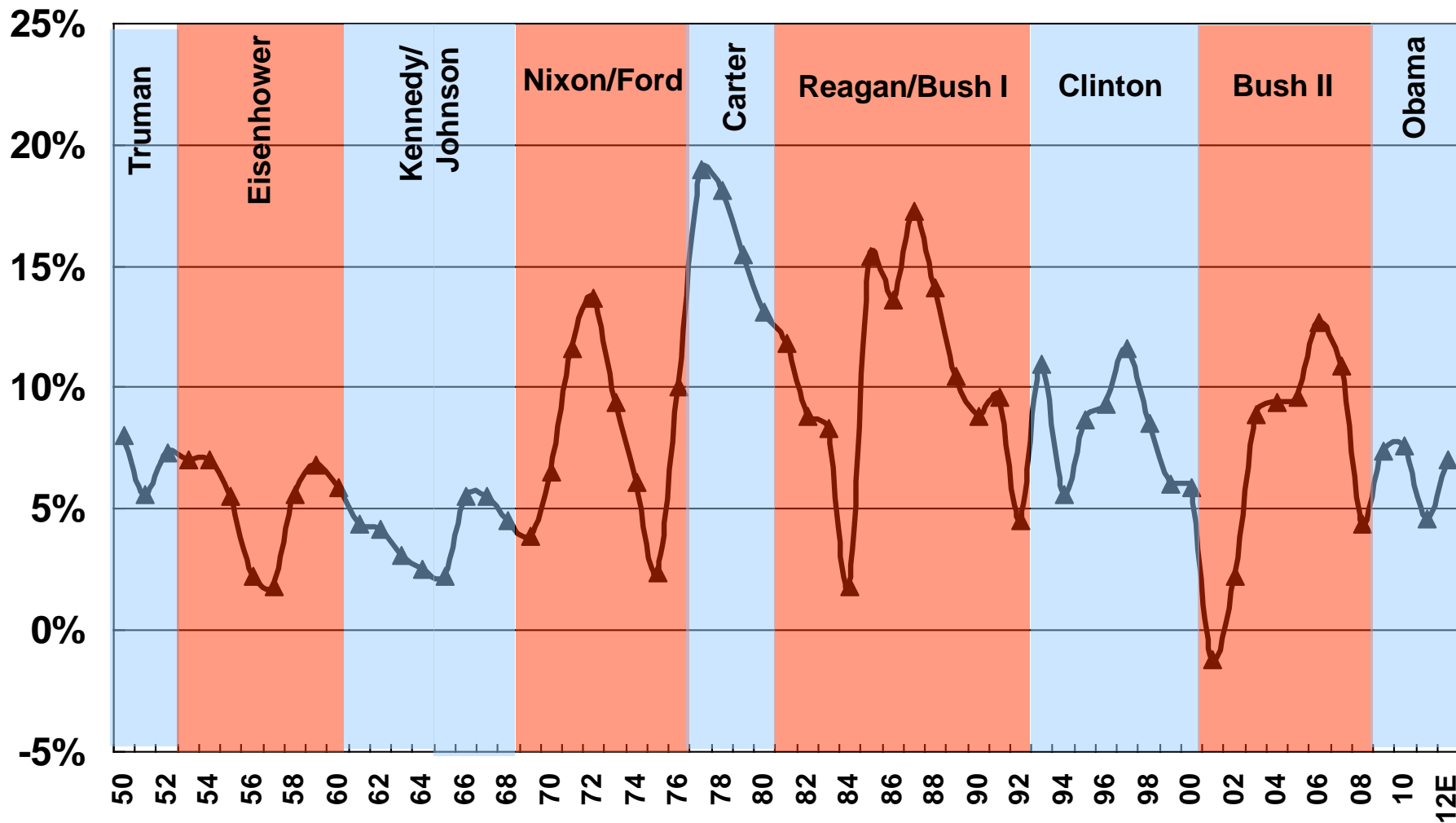


\*Truman administration ROE of 6.97% based on 3 years only, 1950-52; ROEs for the years 2008 forward exclude mortgage and financial guaranty segments. Estimated ROE for 2012 = 7.0%.

# P/C insurance Industry ROE by Presidential Party Affiliation, 1950- 2012\*

**BLUE** = Democratic President

**RED** = Republican President



\*ROEs for the years 2008 forward exclude mortgage and financial guaranty segments; Estimated 2012 ROE = 7.0%

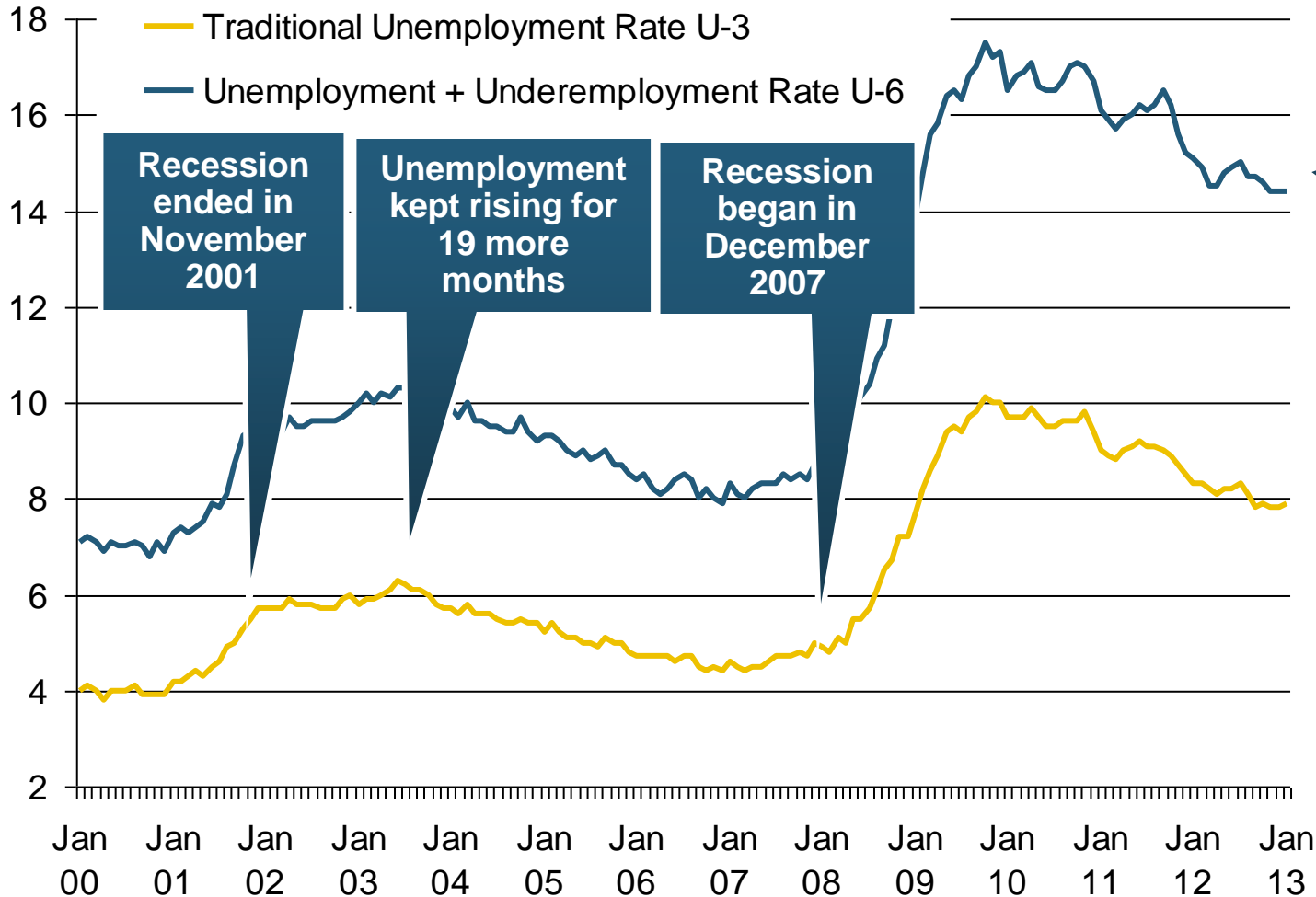
Source: Insurance Information Institute

# Labor Market Trends

**Massive Job Losses Sapped the Economy and Commercial/Personal Lines Exposure, But Trend is Improving**

# Unemployment and Underemployment Rates: Stubbornly High in 2012, But Falling

January 2000 through Jan. 2013, Seasonally Adjusted (%)



**U-6 went from 8.0% in March 2007 to 17.5% in October 2009; Stood at 14.4% in Jan. 2013**

**Unemployment stood at 7.9% in Jan. 2013—lowest in 4 years.**

**Unemployment peaked at 10.1% in October 2009, highest monthly rate since 1983.**

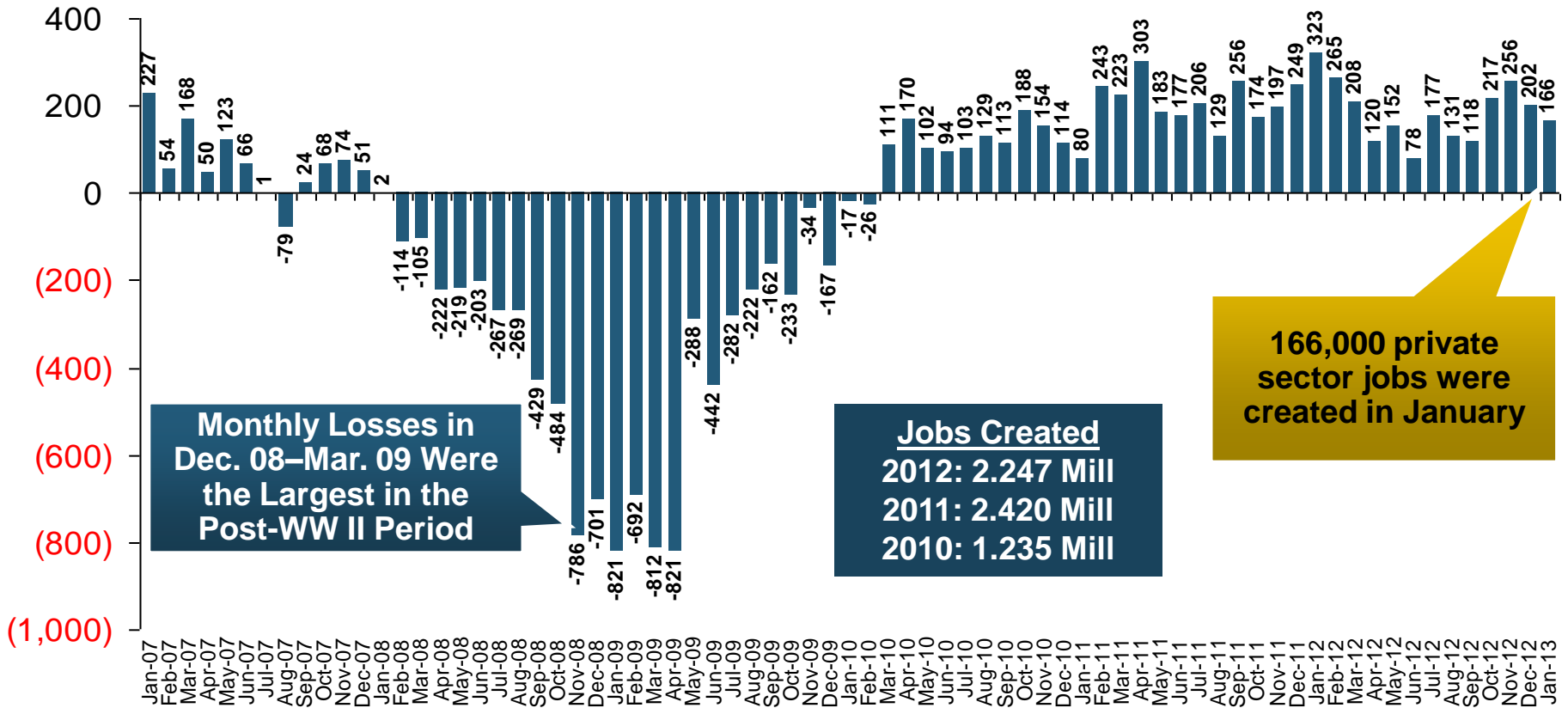
**Peak rate in the last 30 years: 10.8% in November - December 1982**

**Stubbornly high unemployment and underemployment constrain overall economic growth, but the job market is now clearly improving**

Source: US Bureau of Labor Statistics; Insurance Information Institute.

# Monthly Change in Private Employment

January 2008 through Jan. 2013 (Thousands)



Monthly Losses in Dec. 08–Mar. 09 Were the Largest in the Post-WW II Period

**Jobs Created**  
 2012: 2.247 Mill  
 2011: 2.420 Mill  
 2010: 1.235 Mill

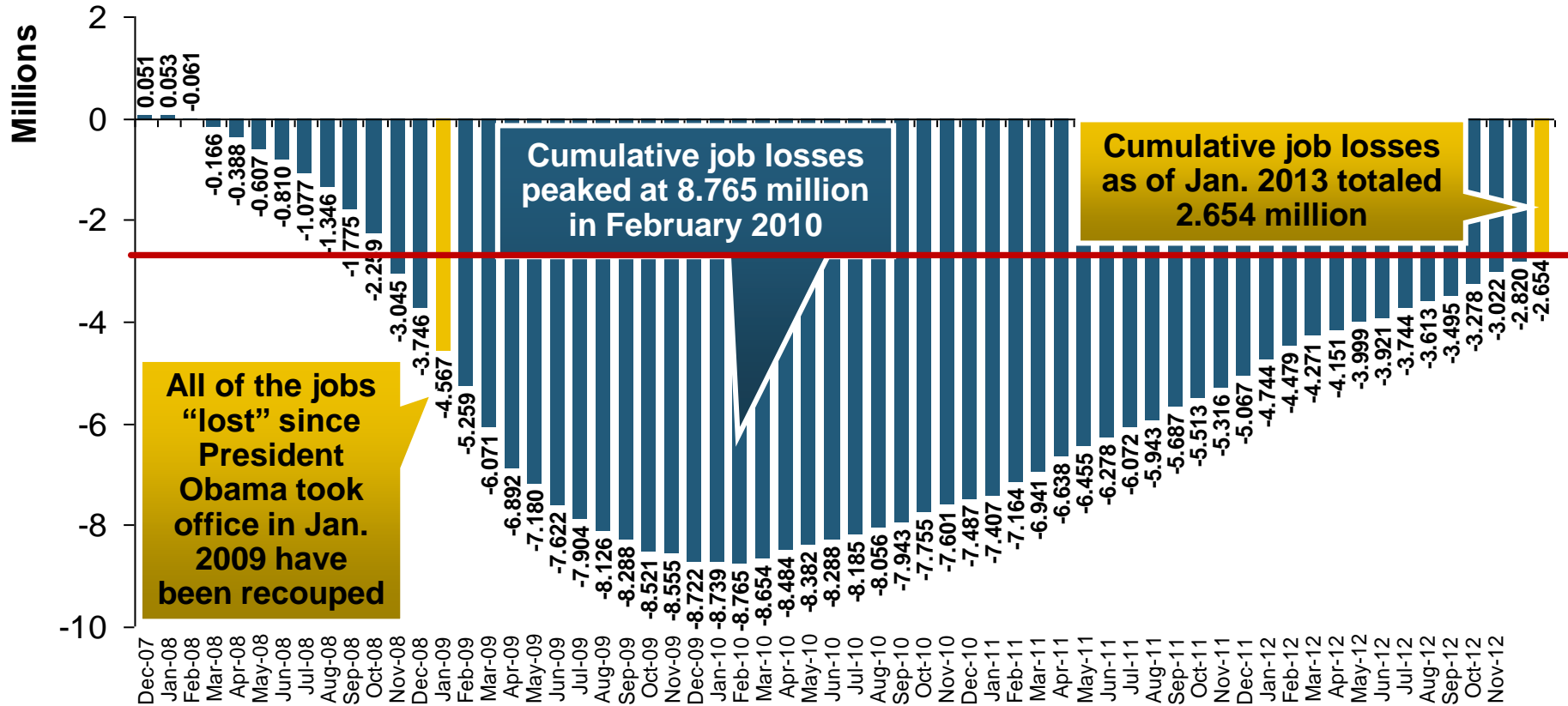
166,000 private sector jobs were created in January

Private Employers Added 6.07million Jobs Since Jan. 2010 After Having Shed 4.98 Million Jobs in 2009 and 3.80 Million in 2008 (State and Local Governments Have Shed Hundreds of Thousands of Jobs)

Source: US Bureau of Labor Statistics: <http://www.bls.gov/ces/home.htm>; Insurance Information Institute

# Cumulative Change in Private Employment: Dec. 2007—Jan. 2013

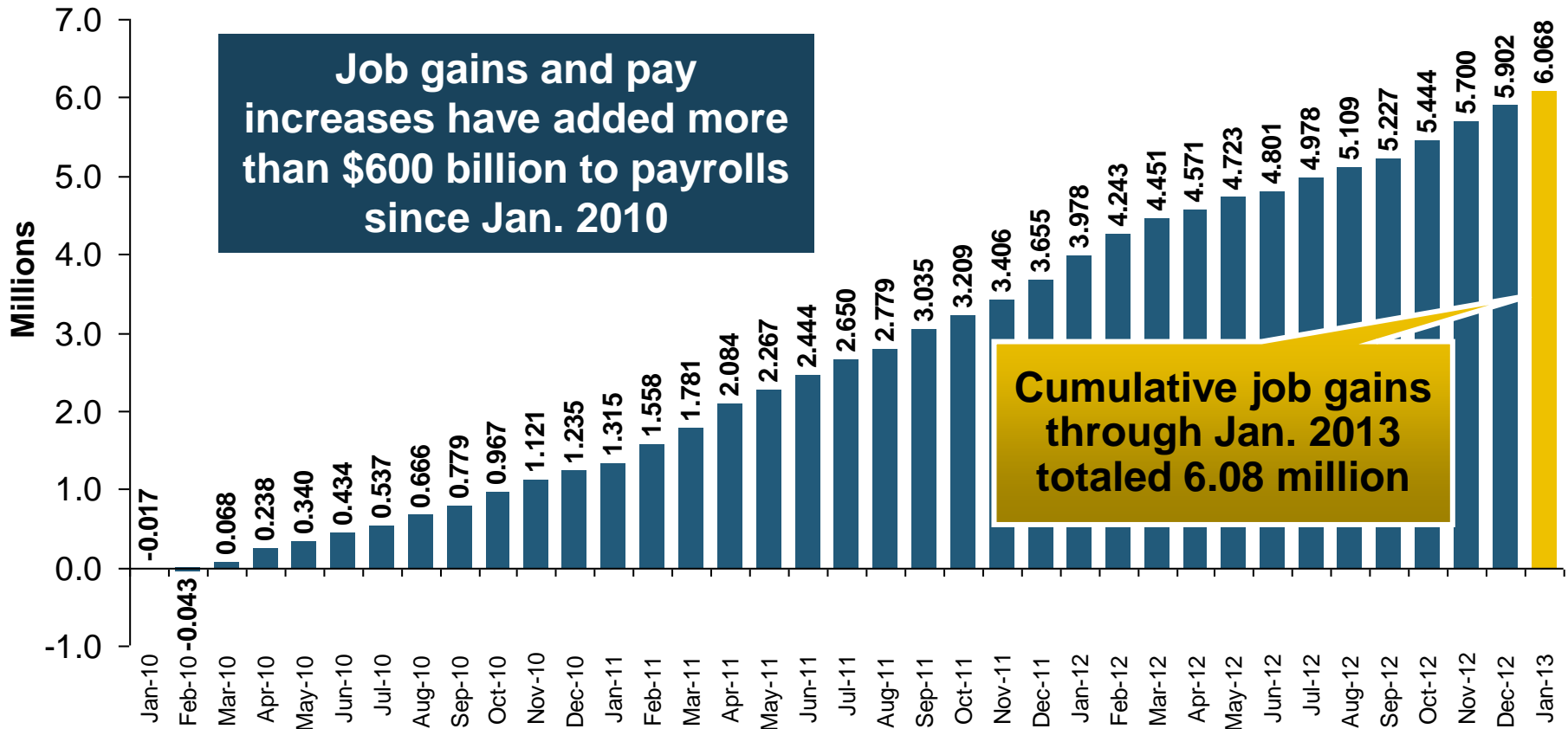
December 2007 through January 2013 (Millions)



**Private Employers Added 6.07million Jobs Since Jan. 2010 After Having Shed 4.98 Million Jobs in 2009 and 3.80 Million in 2008 (State and Local Governments Have Shed Hundreds of Thousands of Jobs)**

# Cumulative Change in Private Sector Employment: Jan. 2010—Jan. 2013

January 2010 through January 2013\* (Millions)

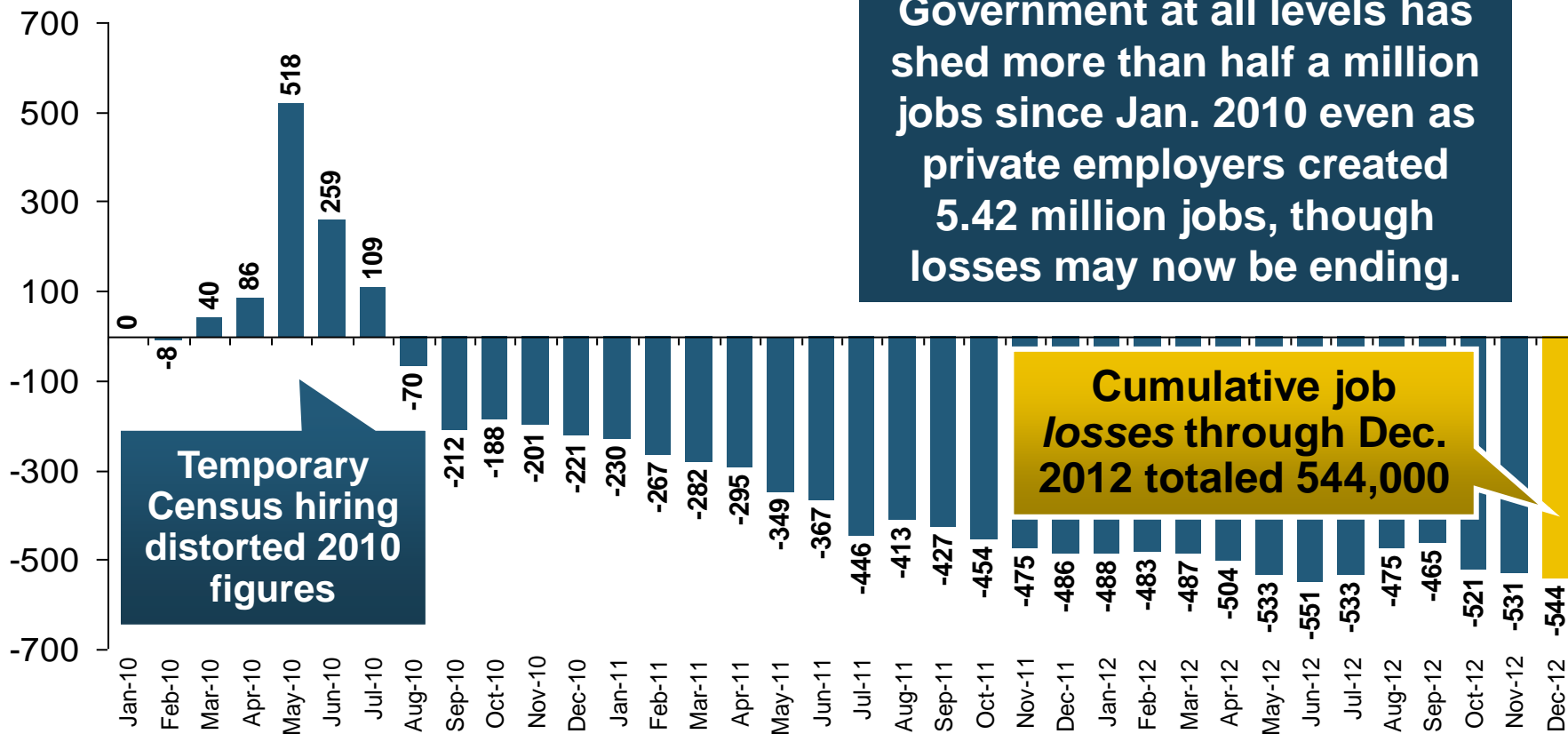


**Private Employers Added 6.07 million Jobs Since Jan. 2010 After Having Shed 4.98 Million Jobs in 2009 and 3.80 Million in 2008 (State and Local Governments Have Shed Hundreds of Thousands of Jobs)**



# Cumulative Change in Government Employment: Jan. 2010—Dec. 2012

January 2010 through Dec. 2012\* (Millions)



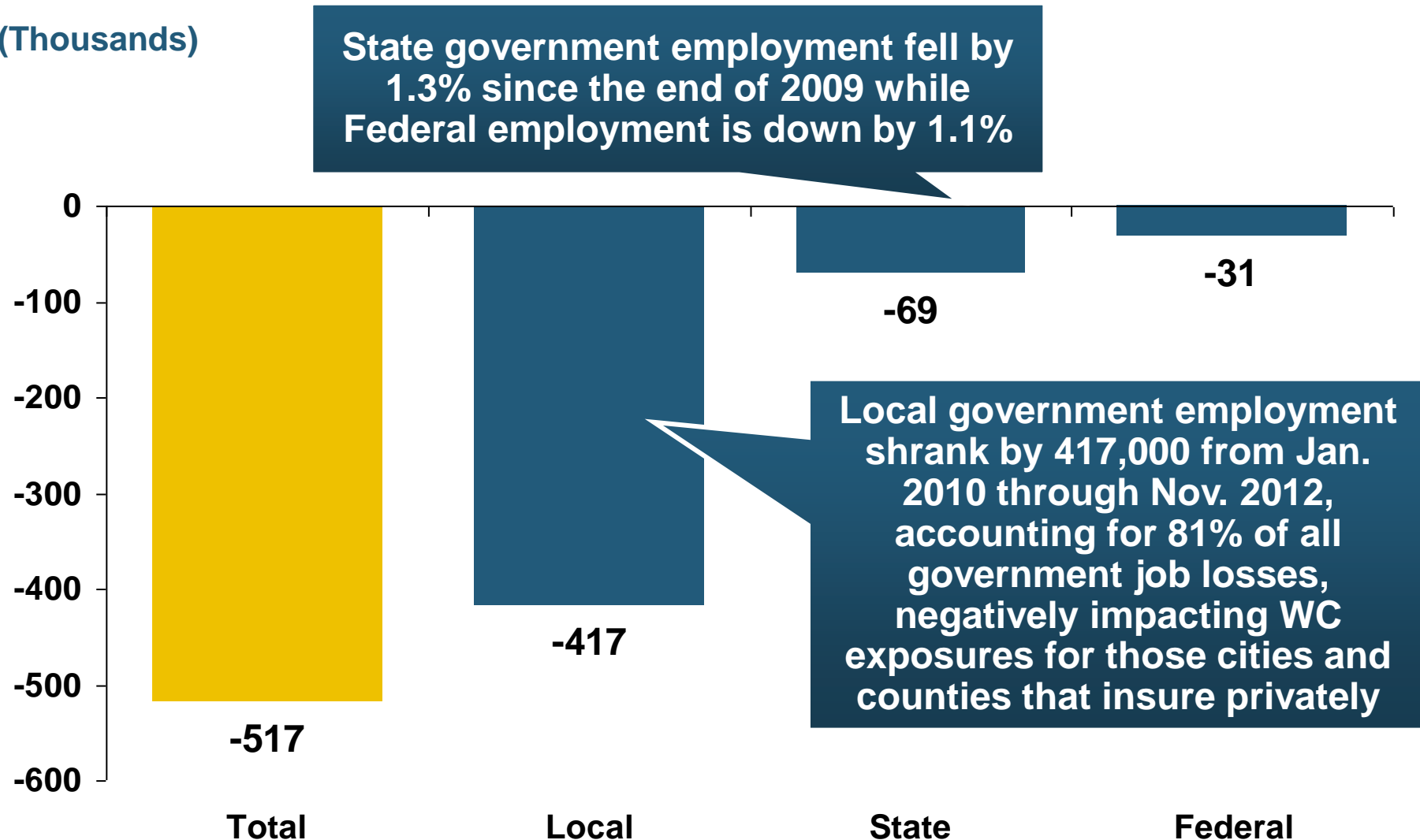
Government at all levels has shed more than half a million jobs since Jan. 2010 even as private employers created 5.42 million jobs, though losses may now be ending.

Cumulative job losses through Dec. 2012 totaled 544,000

**Governments at All Levels are Under Severe Fiscal Strain As Tax Receipts Plunged and Pension Obligations Soared During the Financial Crisis, Causing Them to Reduce Staff**

# Net Change in Government Employment: Jan. 2010—Nov. 2012\*

(Thousands)



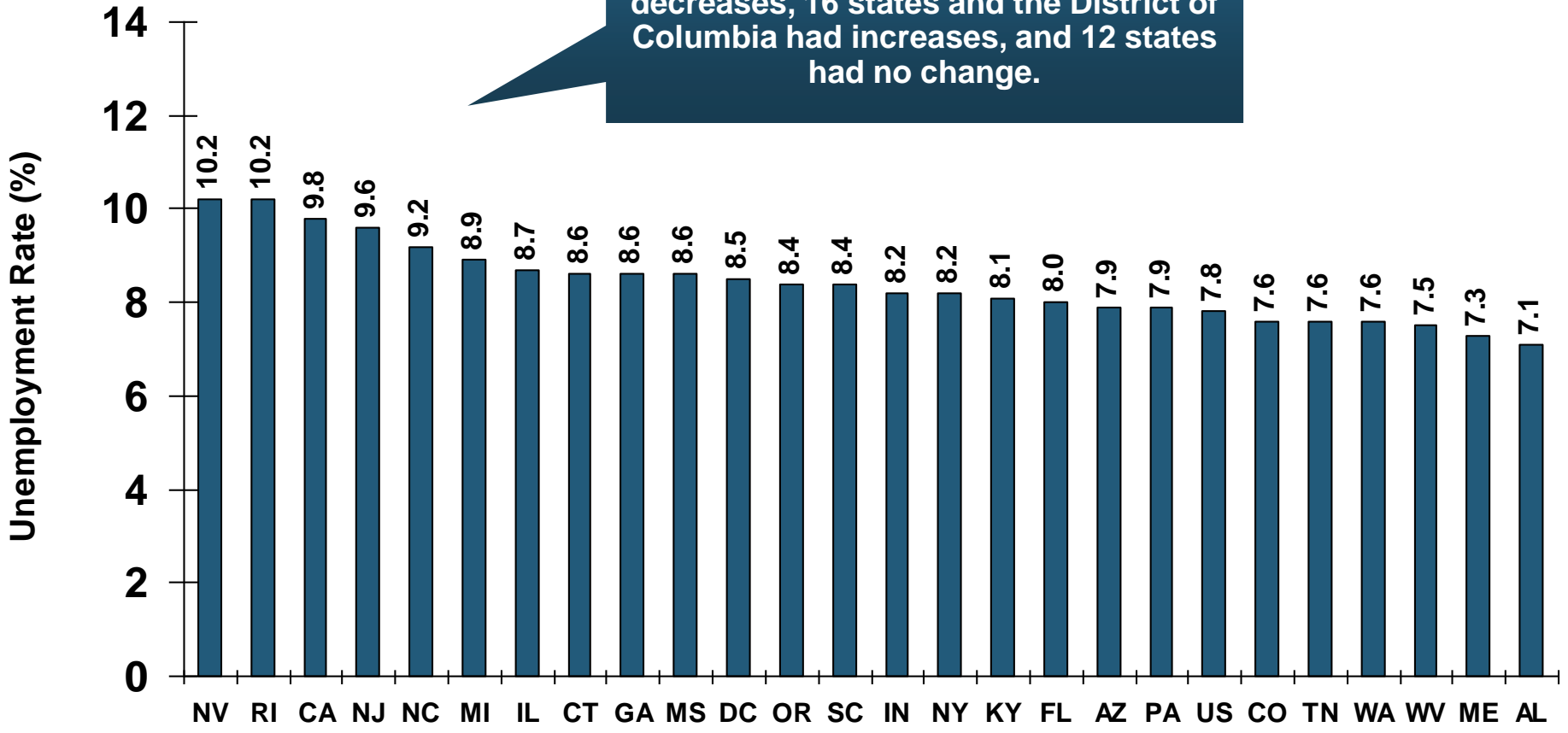
\*Cumulative change from prior month; Base employment date is Dec. 2009.

Source: US Bureau of Labor Statistics <http://www.bls.gov/data/#employment>; Insurance Information Institute

# Unemployment Rates by State, December 2012: Highest 25 States\*



In December, 22 states reported over-the-month unemployment rate decreases, 16 states and the District of Columbia had increases, and 12 states had no change.



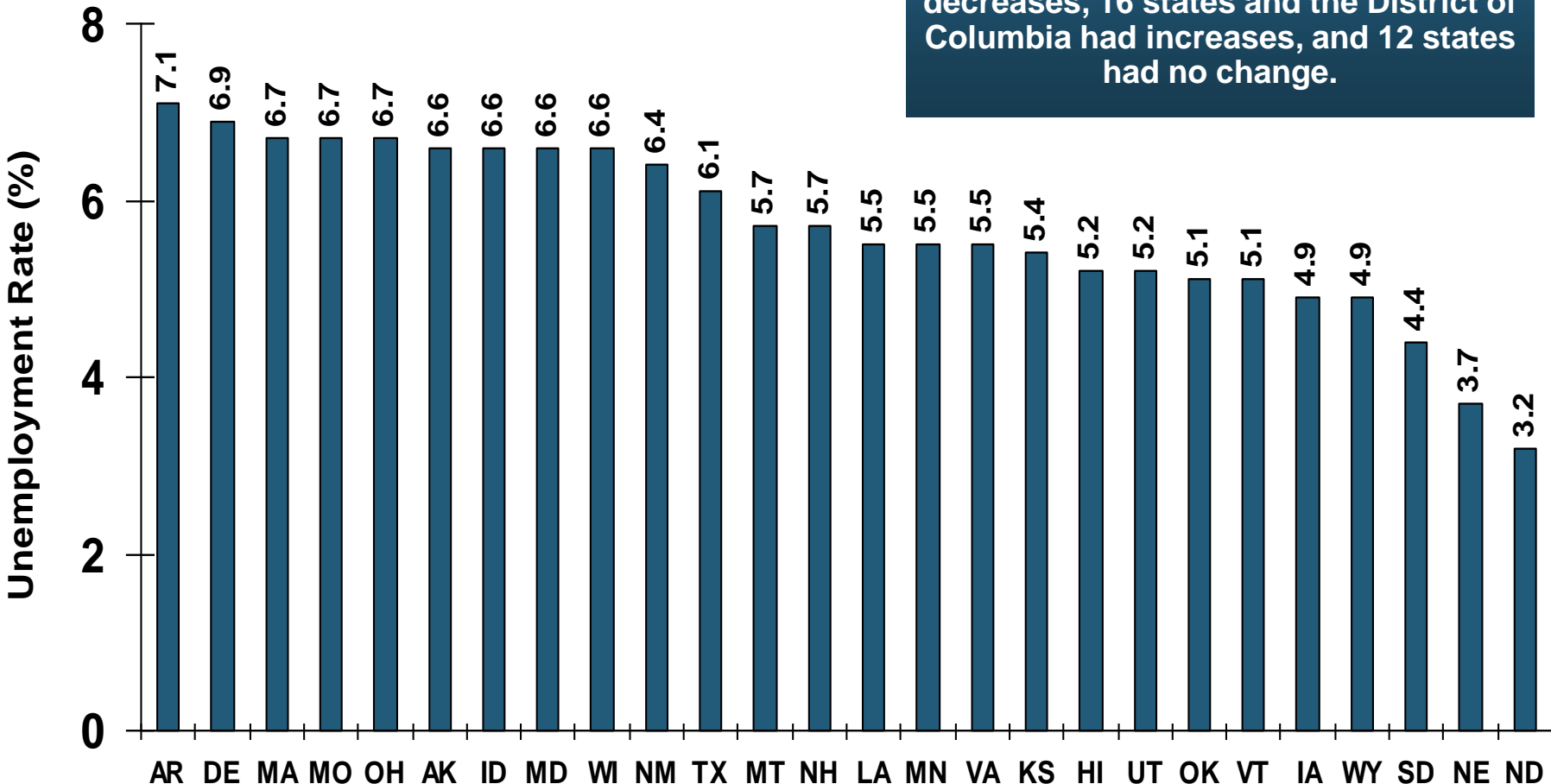
\*Provisional figures for December 2012, seasonally adjusted.

Sources: US Bureau of Labor Statistics; Insurance Information Institute.

# Unemployment Rates by State, December 2012: Lowest 25 States\*



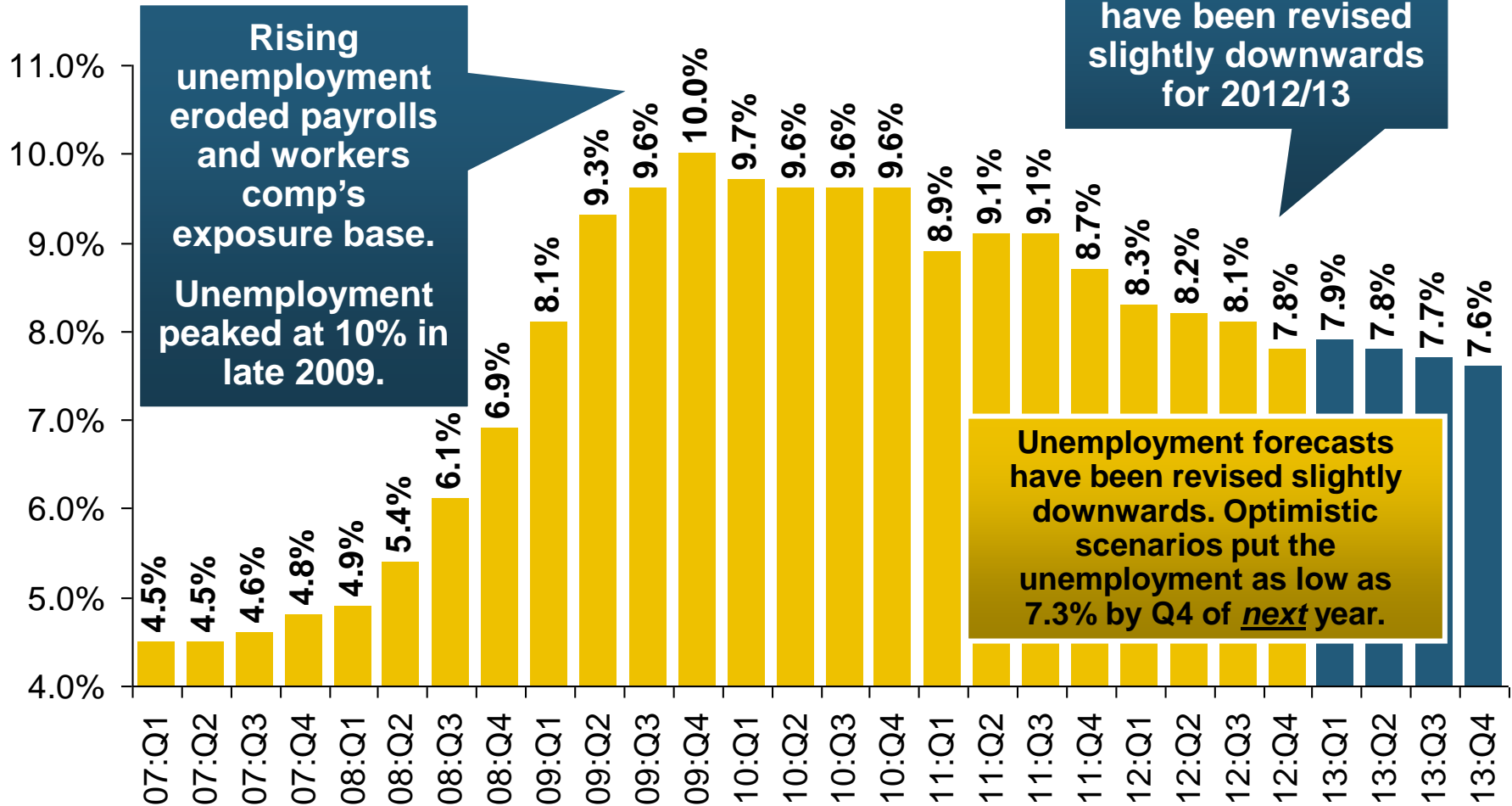
In December, 22 states reported over-the-month unemployment rate decreases, 16 states and the District of Columbia had increases, and 12 states had no change.



\*Provisional figures for December 2012, seasonally adjusted.  
Sources: US Bureau of Labor Statistics; Insurance Information Institute.

# US Unemployment Rate Forecast

2007:Q1 to 2013:Q4F\*

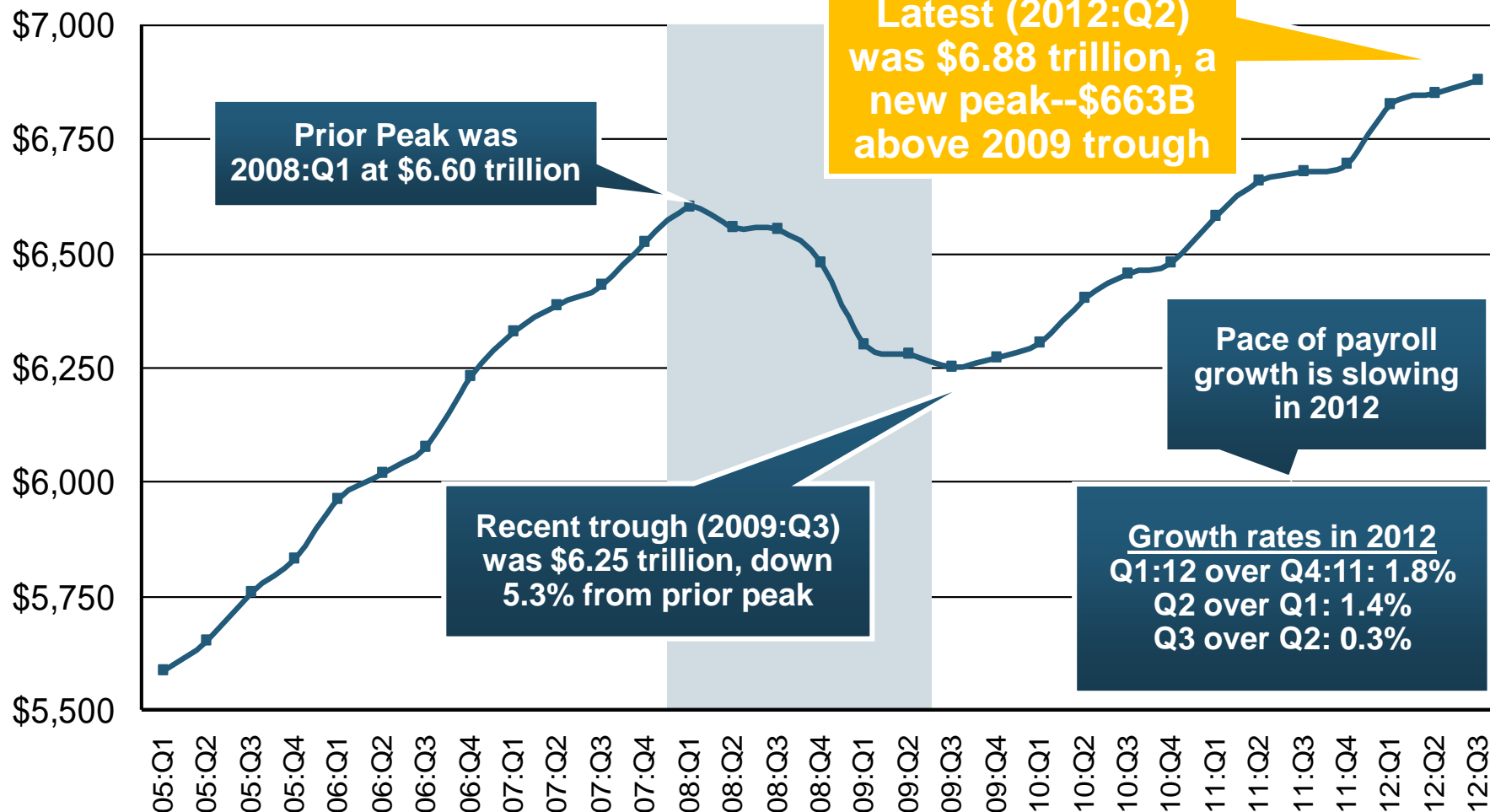


\* ■ = actual; ■ = forecasts

Sources: US Bureau of Labor Statistics; Blue Chip Economic Indicators (12/12 edition); Insurance Information Institute.

# Nonfarm Payroll (Wages and Salaries): Quarterly, 2005–2012:Q3

Billions



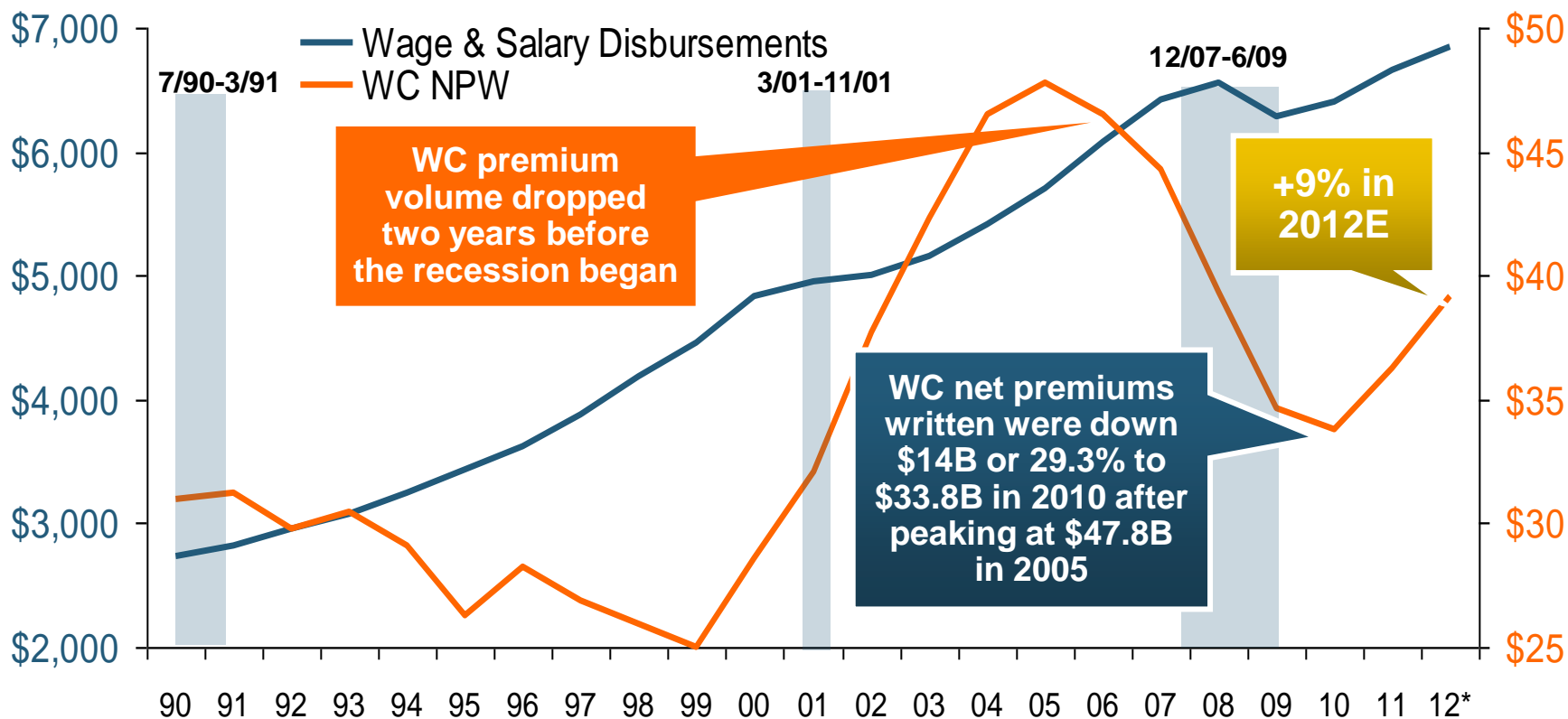
Note: Recession indicated by gray shaded column. Data are seasonally adjusted annual rates.

Sources: <http://research.stlouisfed.org/fred2/series/WASCUR>; National Bureau of Economic Research (recession dates); Insurance Information Institute.

# Payroll vs. Workers Comp Net Written Premiums, 1990-2012E

Payroll Base\*  
\$Billions

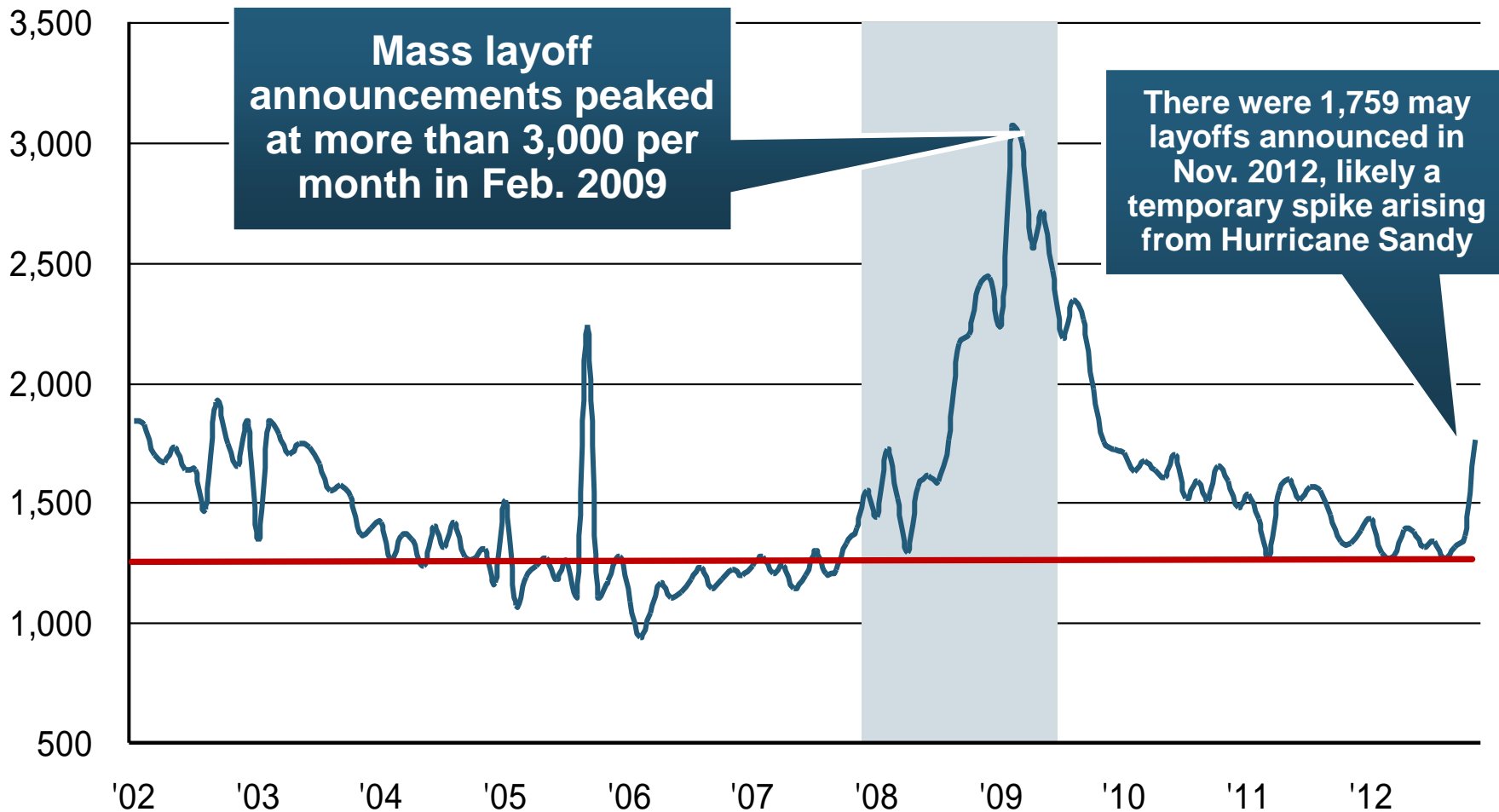
WC NWP  
\$Billions



**Continued Payroll Growth and Rate Increases Suggest WC NWP Will Grow Again in 2012; +7.9% Growth in 2011 Was the First Gain Since 2005**

\*Private employment; Shaded areas indicate recessions. Payroll and WC premiums for 2012 is I.I.I. estimate based YTD 2012 actuals. Sources: NBER (recessions); Federal Reserve Bank of St. Louis at <http://research.stlouisfed.org/fred2/series/WASCUR> ; NCCI; I.I.I.

# Mass Layoff Announcements, Jan. 2002—November 2012\*



\*Seasonally adjusted.

Note: Recessions indicated by gray shaded columns.

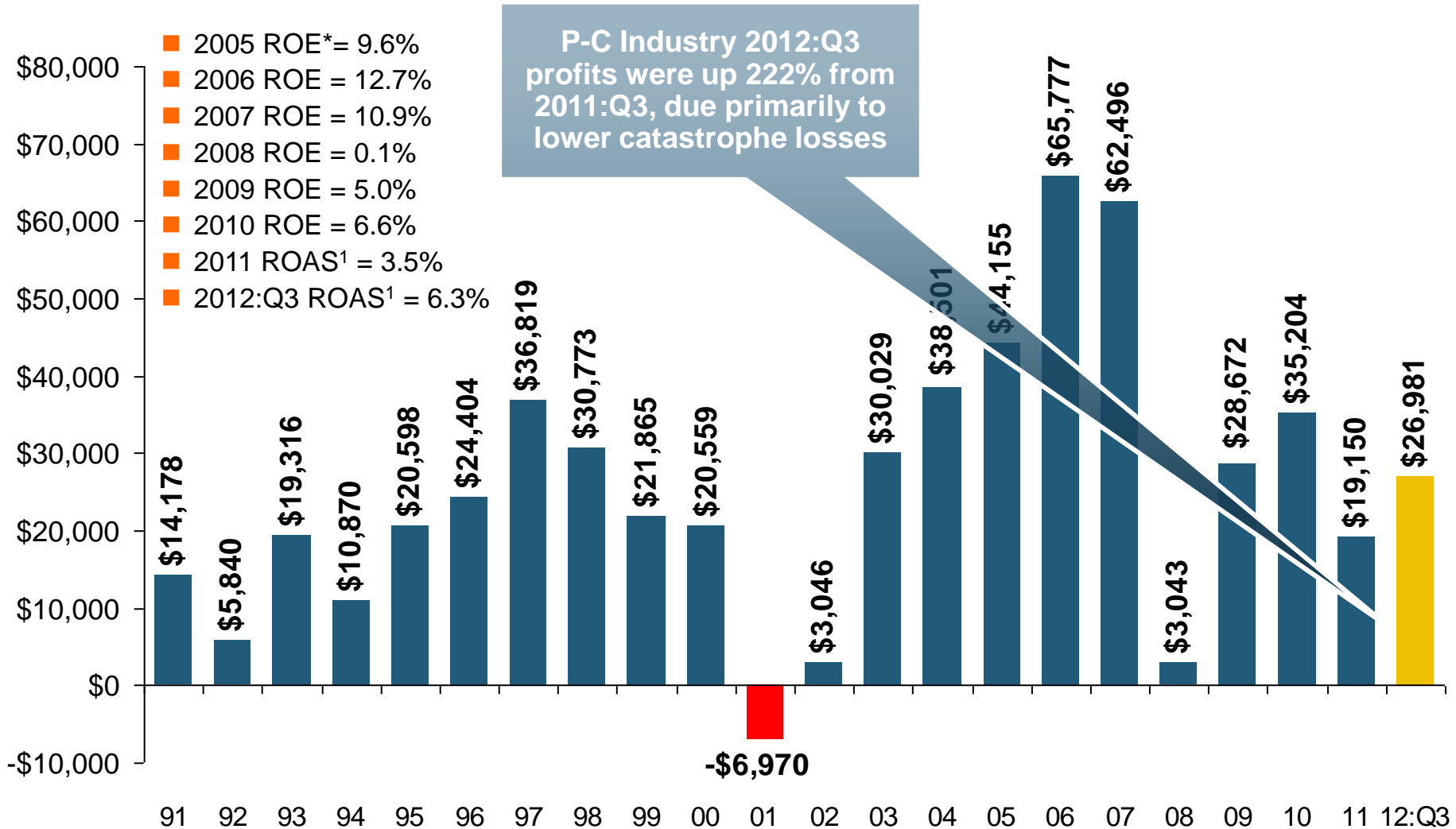
Sources: US Bureau of Labor Statistics at <http://www.bls.gov/mls/>; National Bureau of Economic Research (recession dates); Insurance Information Institute.



# **P/C Insurance Industry Financial Overview**

**Profit Recovery in 2012 After  
High CAT Losses; Ultimate  
Impact of Sandy Still Unclear**

# P/C Net Income After Taxes 1991–2012:Q3 (\$ Millions)



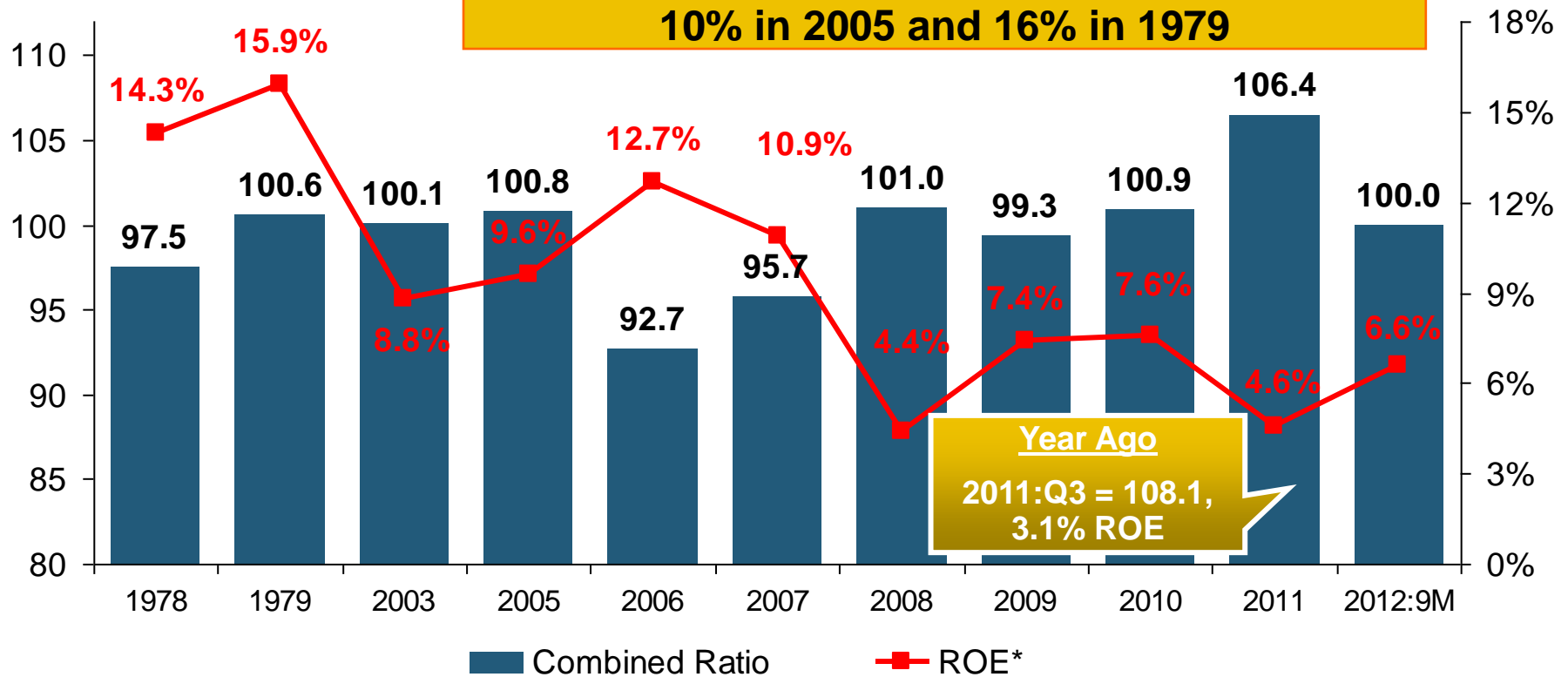
\* ROE figures are GAAP; <sup>1</sup>Return on avg. surplus. Excluding Mortgage & Financial Guaranty insurers yields a 6.6% ROAS through 2012:Q3, 4.6% ROAS for 2011, 7.6% for 2010 and 7.4% for 2009.

Sources: A.M. Best, ISO, Insurance Information Institute

# A 100 Combined Ratio Isn't What It Once Was: Investment Impact on ROEs

## Combined Ratio / ROE

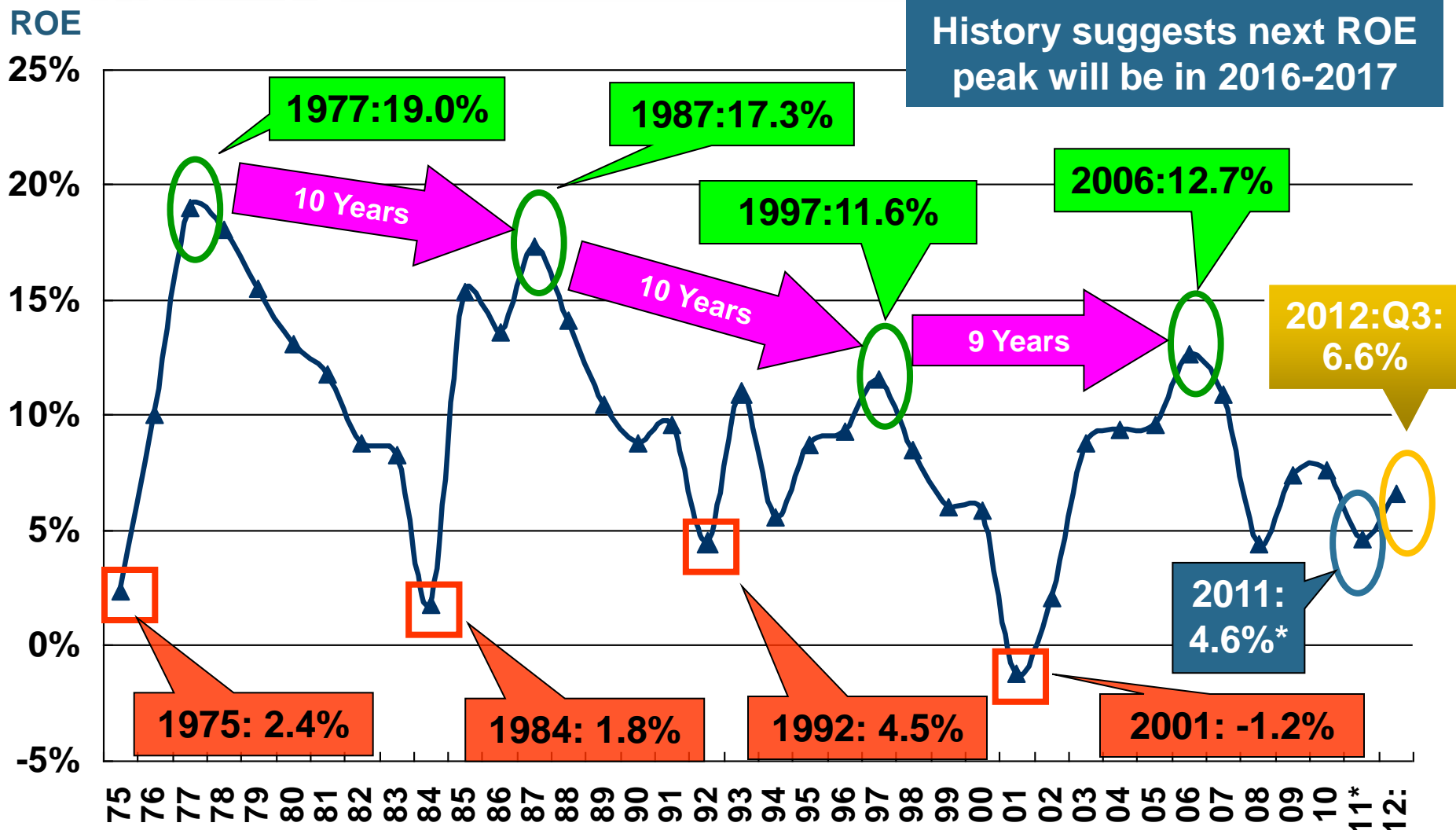
A combined ratio of about 100 generates an ROE of ~6.6% in 2012, ~7.5% ROE in 2009/10, 10% in 2005 and 16% in 1979



**Combined Ratios Must Be Lower in Today's Depressed Investment Environment to Generate Risk Appropriate ROEs**

\* 2008 -2012 figures are return on average surplus and exclude mortgage and financial guaranty insurers. 2012:Q3 combined ratio including M&FG insurers is 100.9, ROAS = 6.3%; 2011 combined ratio including M&FG insurers is 108.2, ROAS = 3.5%. Source: Insurance Information Institute from A.M. Best and ISO data.

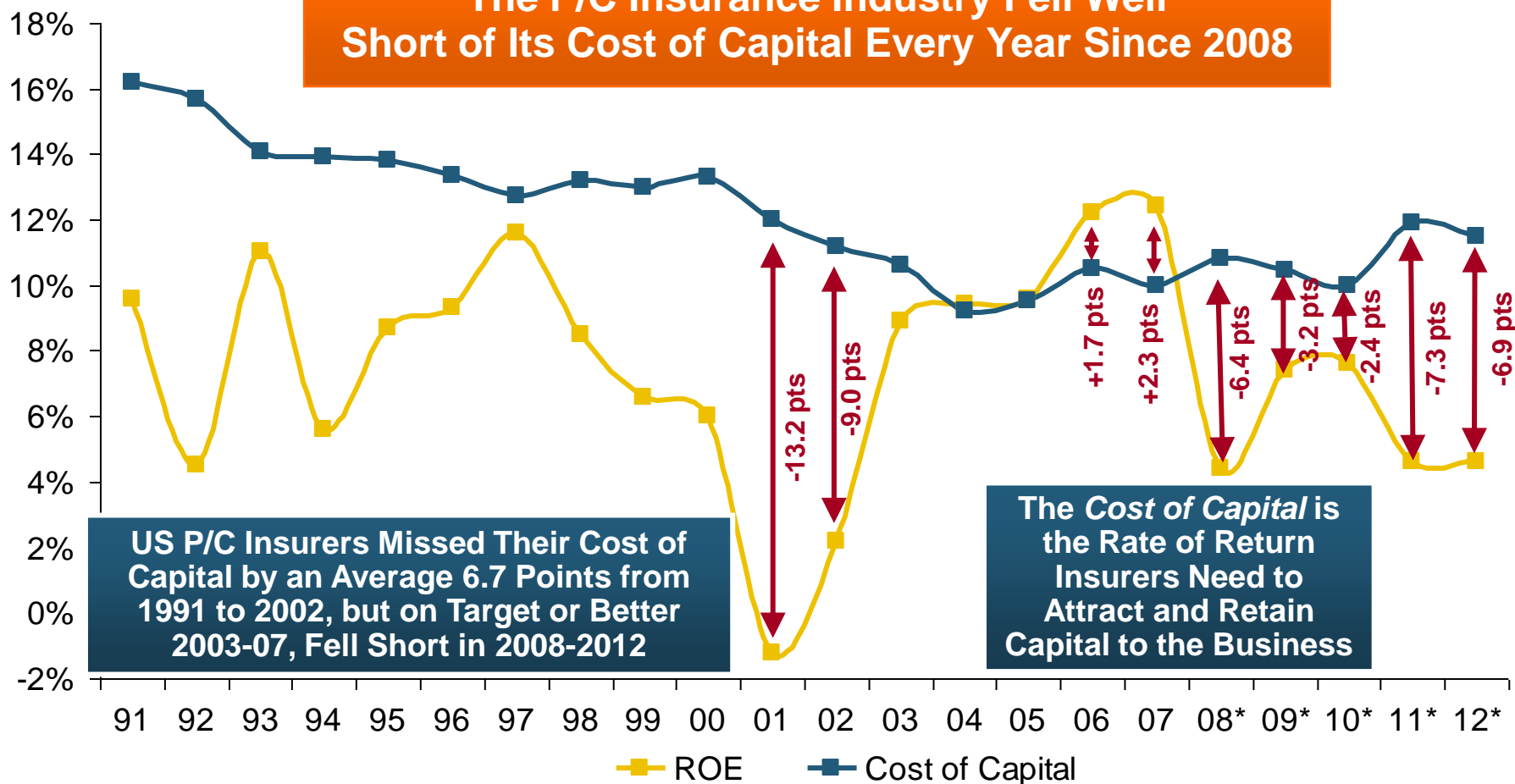
# Profitability Peaks & Troughs in the P/C Insurance Industry, 1975 – 2012:Q3\*



\*Profitability = P/C insurer ROEs. 2011 figure is an estimate based on ROAS data. Note: Data for 2008-2012 exclude mortgage and financial guaranty insurers. 2012:Q3 ROAS = 6.2% including M&FG.

# ROE vs. Equity Cost of Capital: U.S. P/C Insurance:1991-2012\*

(Percent)



\* Return on average surplus in 2008-2012 excluding mortgage and financial guaranty insurers. 2012 figures are III estimates.  
Source: The Geneva Association, Insurance Information Institute

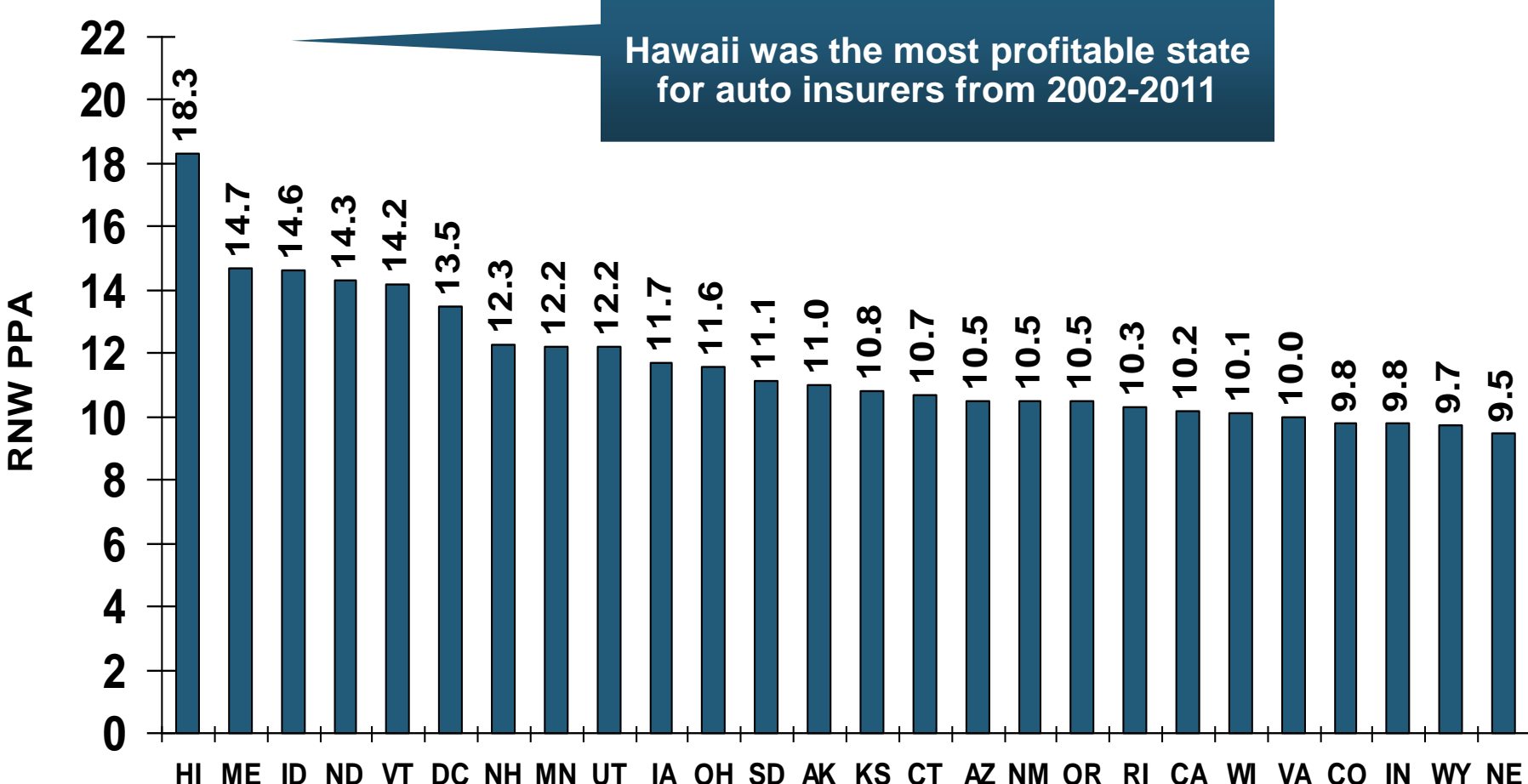
# **Personal Lines Profitability Analysis**

**Significant Variability Over  
Time and Across States**

# Return on Net Worth: Pvt. Passenger Auto, 10-Year Average (2002-2011\*)

## Top 25 States

(Percent)



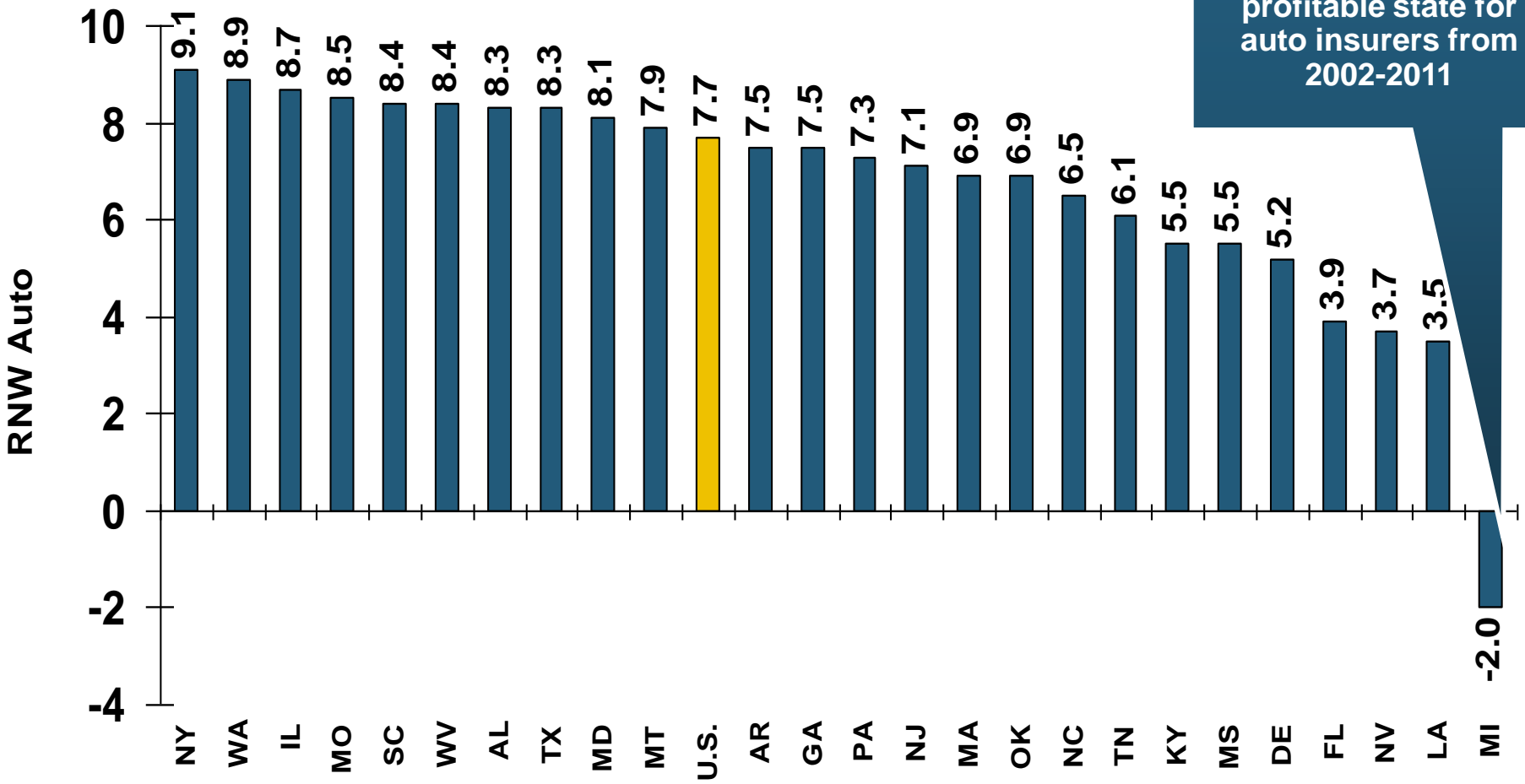
\*Latest available.

Sources: NAIC.

# Return on Net Worth: Pvt. Passenger Auto, 10-Year Average (2002-2011\*)

(Percent)

## Bottom 25 States



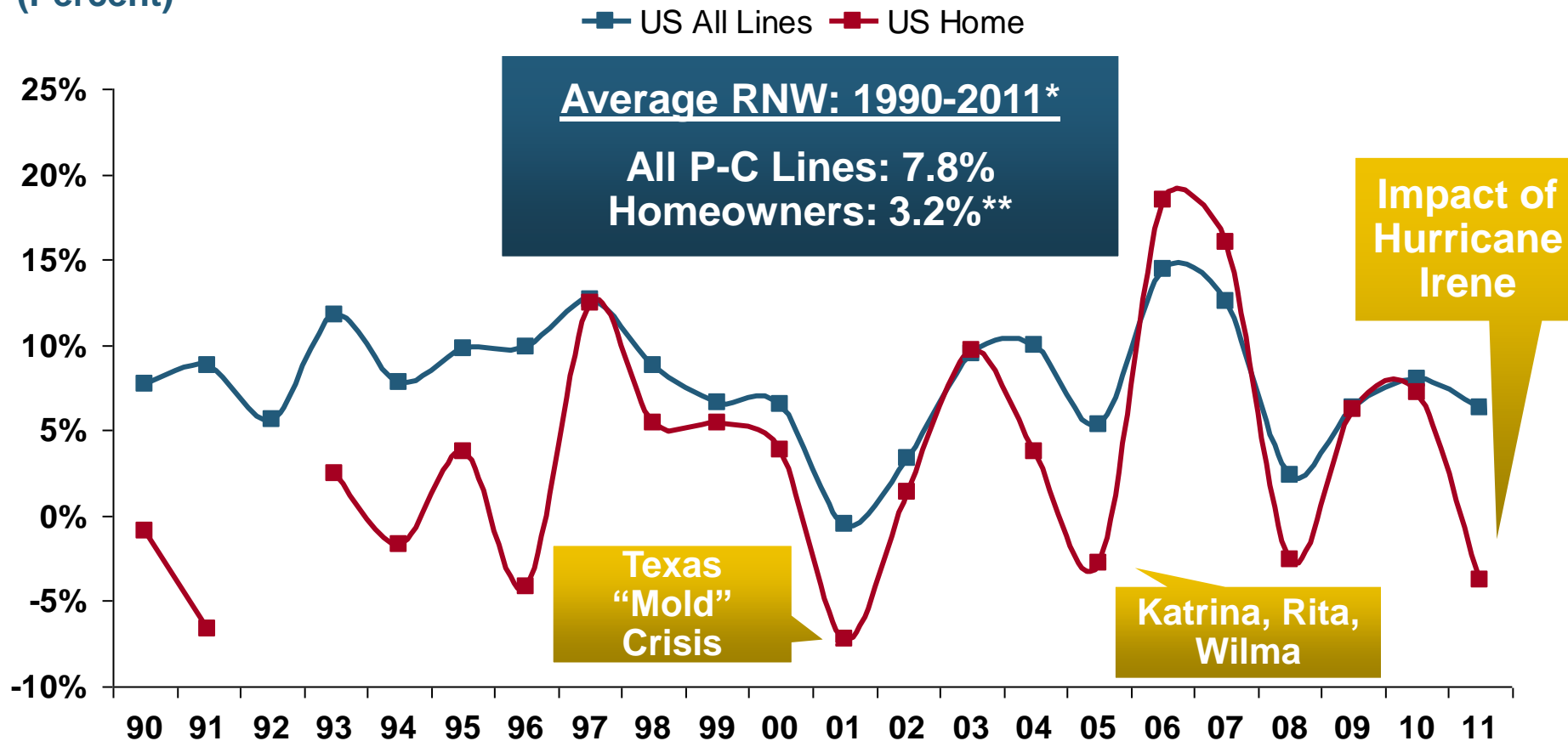
Michigan was the least profitable state for auto insurers from 2002-2011

\*Latest available. Sources: NAIC



# Return on Net Worth: All P-C Lines vs. Homeowners, 1990-2011\*

(Percent)



**Homeowners Insurance Is Considerably More Volatile than the Market Overall Due to Coastal Exposure and Interior Wind/Hail Events**

\*Latest available.

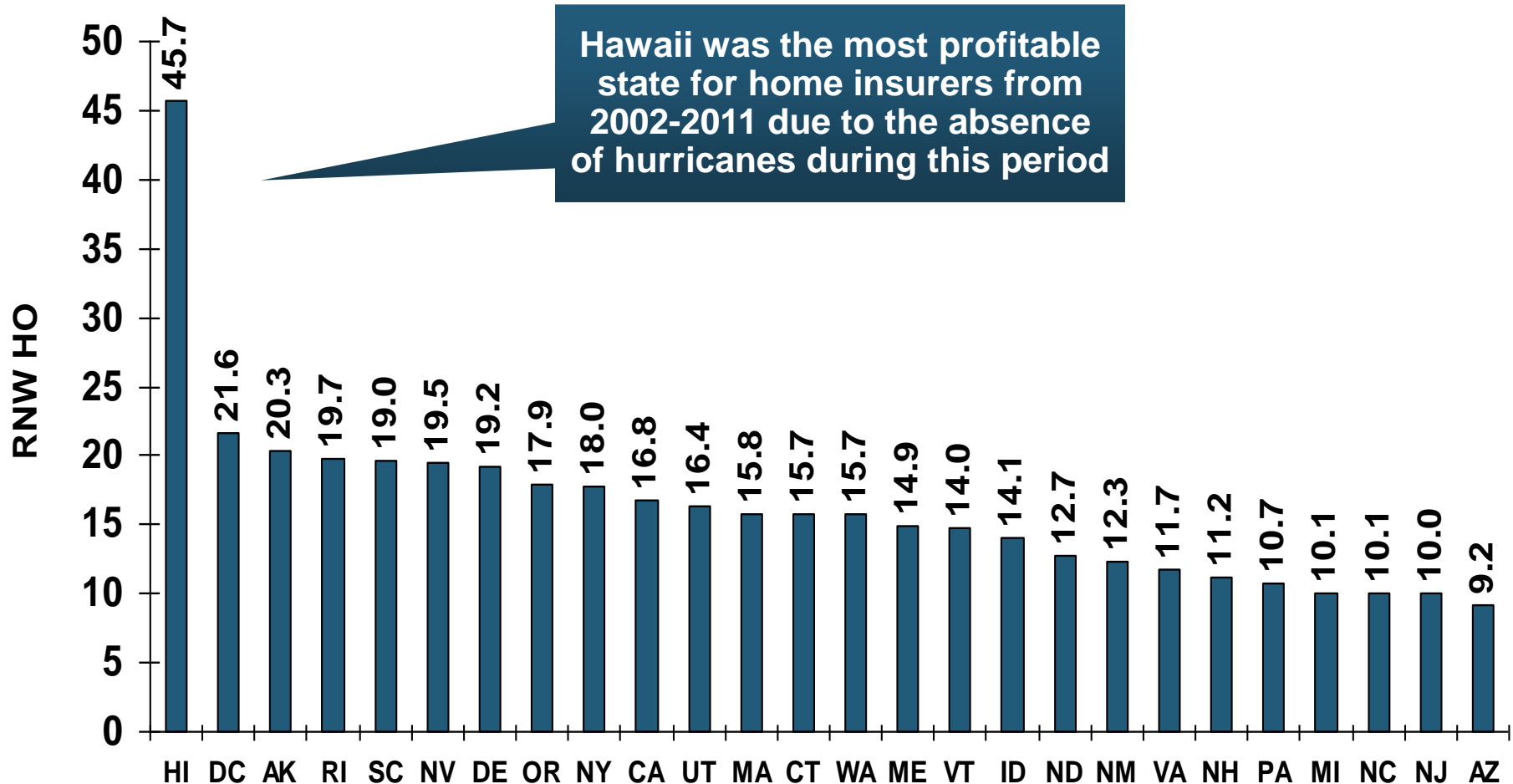
\*\*Excluding Hurricane Andrew (1992); Including 1992 produces an average homeowners RNW of 0.5%.

Sources: NAIC; Insurance Information Institute.

# Return on Net Worth: Homeowners Insurance, 10-Year Average (2002-2011\*)

## Top 25 States

(Percent)



Hawaii was the most profitable state for home insurers from 2002-2011 due to the absence of hurricanes during this period

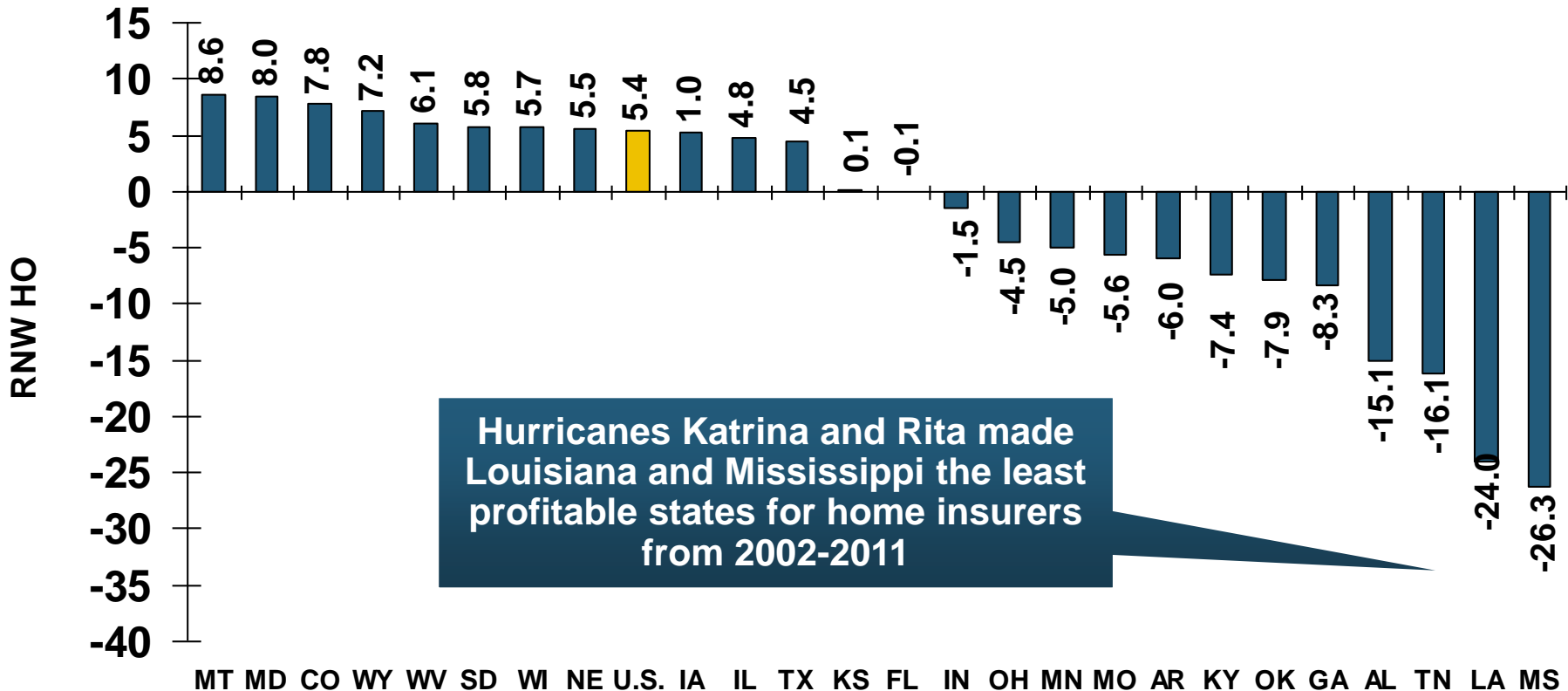
\*Latest available.

Sources: NAIC.

# Return on Net Worth: Homeowners Insurance, 10-Year Average (2002-2011\*)

## Bottom 25 States

(Percent)



\*Latest available.  
Sources: NAIC



# Hurricane Sandy Summary

**Sandy Will Become One of the  
Most Expensive Events in  
Insurance History**

# Why We Aren't at Bridgewaters Today: Scenes from the South Street Seaport



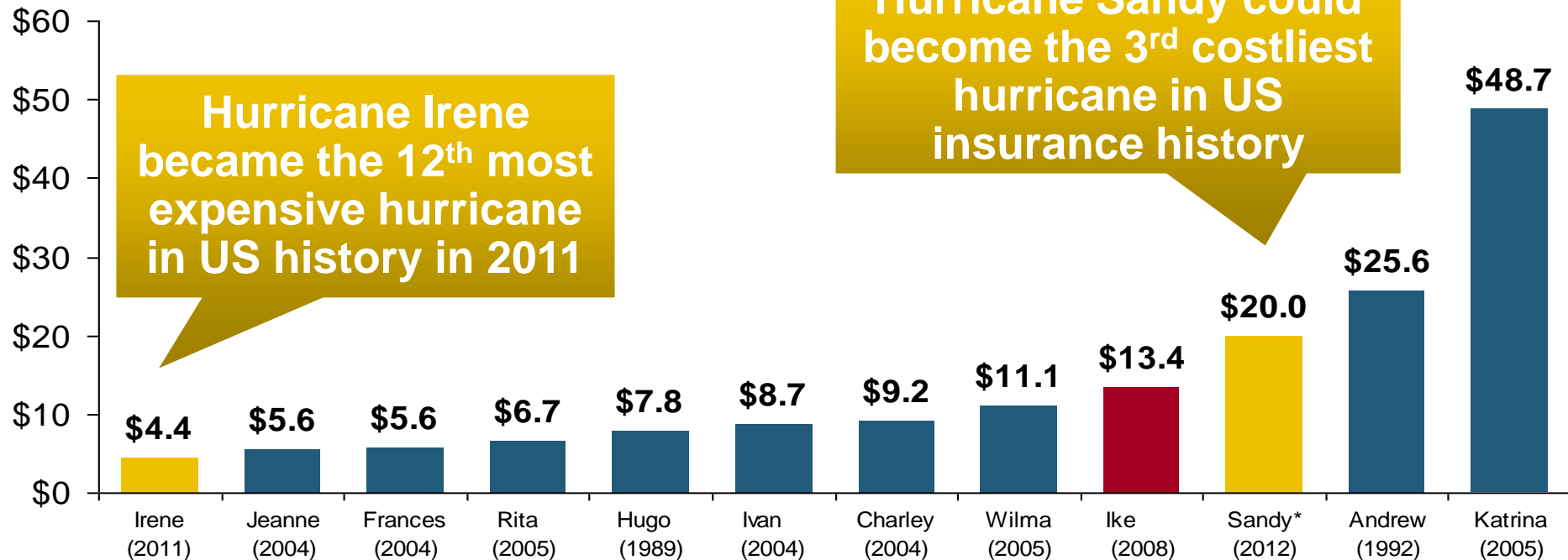
## ■ Catastrophe Communications: US & Global

- **U.S. Focus:** ~\$37-\$42B = 2<sup>nd</sup> Most Costliest Year Ever for Insured Catastrophe Loss (Behind 2005)
  - Economic Losses = \$101B
  - Crop = Additional ~\$16B (\$7B-\$8B privately insured)
  - NFIP Flood = Additional \$9B+
  - Flood losses/NFIP/FEMA has been the #1 communications “issue” in the wake of Sandy
- **Global Focus:** \$65B in Insured Losses → Well Below \$105B in 2011 but Above 10-Yr. Avg. of \$50B
  - Cats abroad did not drive media cycle in 2012, save ongoing Fukushima issues; Climate change
- **Market Consequences:** Primary & Reinsurance
  - Impacts on price, availability

# Top 12 Most Costly Hurricanes in U.S. History

(Insured Losses, 2012 Dollars, \$ Billions)

**10 of the 12 most costly hurricanes in insurance history occurred over the past 9 years (2004—2012)**

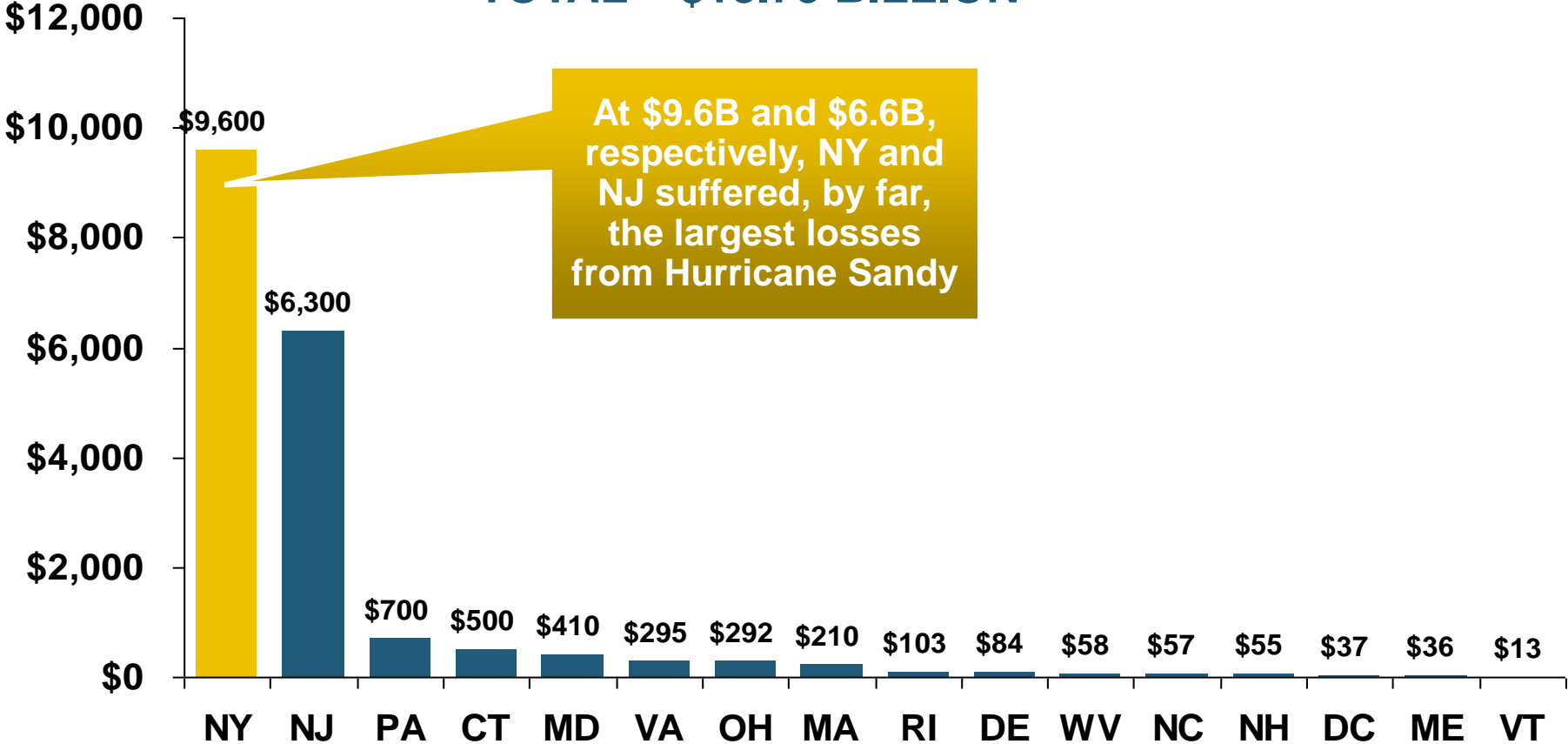


\*Estimate as of 12/09/12 based on estimates of catastrophe modeling firms and reported losses as of 1/12/13. Estimates range up to \$25B.  
Sources: PCS; Insurance Information Institute inflation adjustments to 2012 dollars using the CPI.

# Hurricane Sandy: Claim Payments to Policyholders, by State

(\$ Thousands)

**TOTAL = \$18.75 BILLION**



At \$9.6B and \$6.6B, respectively, NY and NJ suffered, by far, the largest losses from Hurricane Sandy

**Insurers Will Pay at Least \$18.75 Billion to 1.52 Million Policyholders Across 15 States and DC in the Wake of Hurricane Sandy**

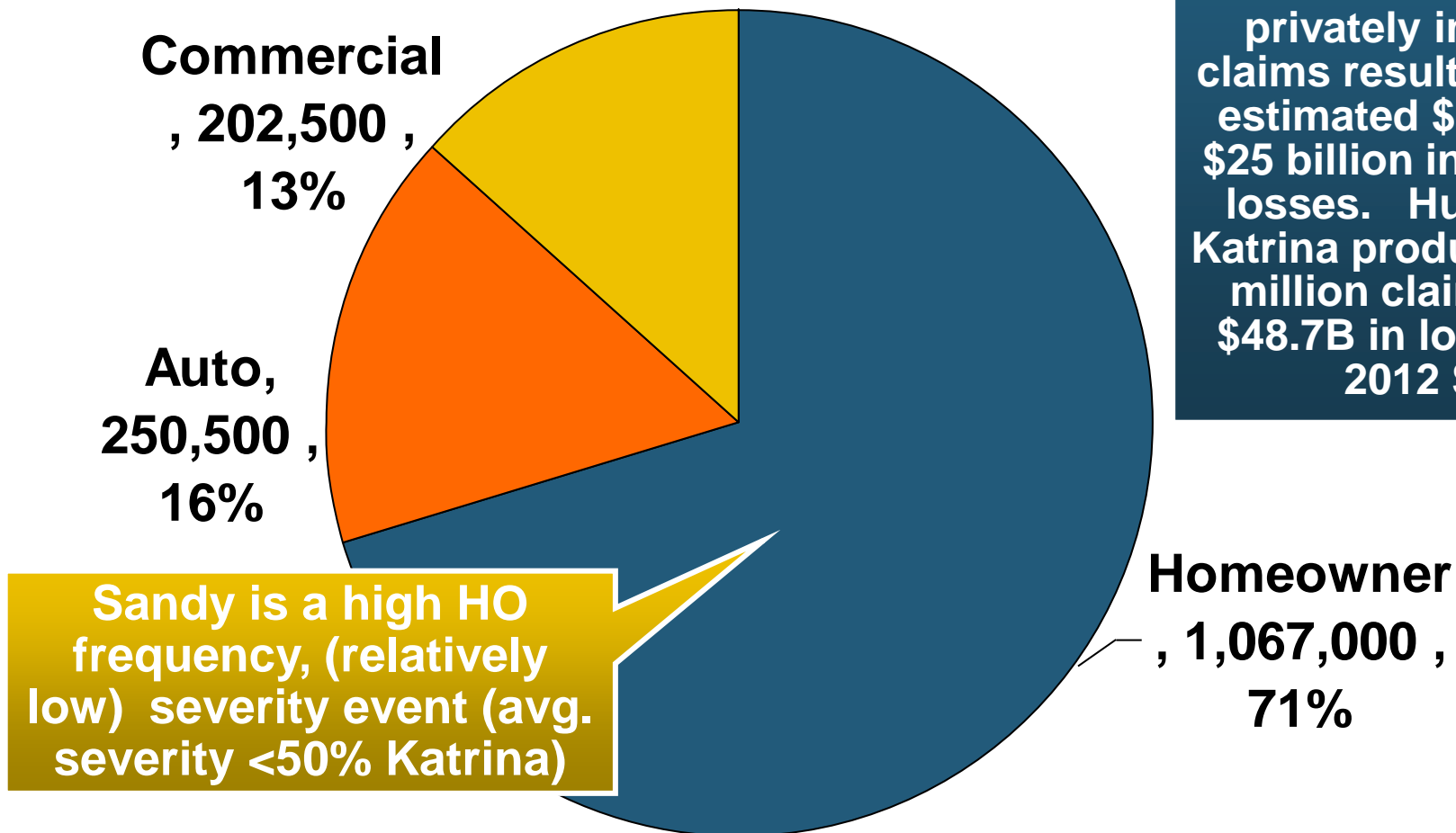
Sources: Catastrophe loss data is for Catastrophe Serial No. 90 (Oct. 28 – 31, 2012) from PCS as of Jan. 18, 2013; Insurance Information Institute .



# Hurricane Sandy: Number of Claims by Type\*

**Total Claims = 1.52 Million\***

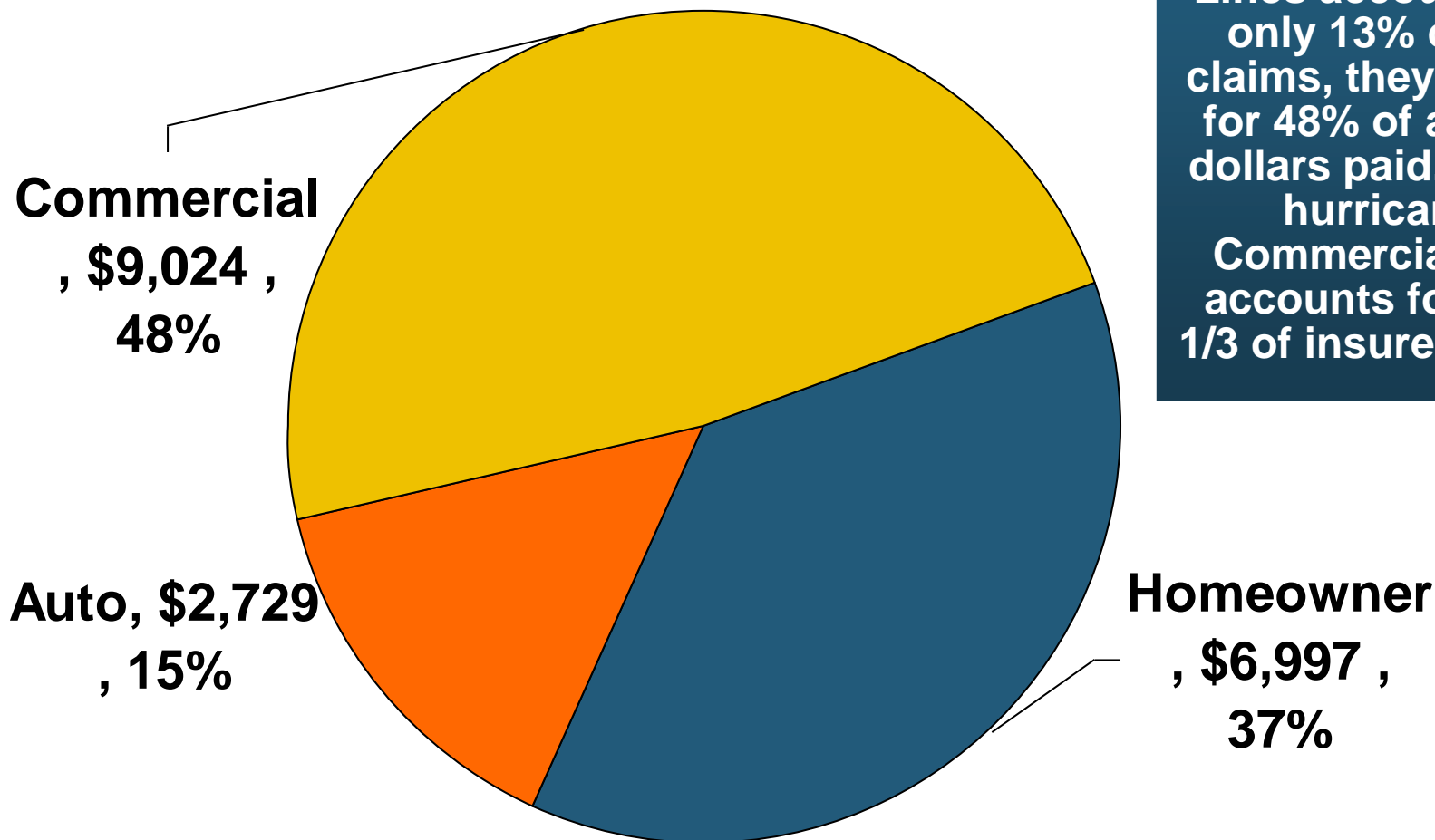
Hurricane Sandy resulted in an estimated 1.52 million privately insured claims resulting in an estimated \$18.75 to \$25 billion in insured losses. Hurricane Katrina produced 1.74 million claims and \$48.7B in losses (in 2012 \$)



\*PCS claim count estimate s as of 1/18/13. Loss estimate represents PCS total (\$18.75B) and upper end of range estimates by risk modelers RMS, Eqecat and AIR. All figures exclude losses paid by the NFIP.  
Source: PCS; AIR, Eqecat, AIR Worldwide; Insurance Information Institute.

# Hurricane Sandy: Insured Loss by Claim Type\* (\$ Millions)

**Total Claim Value = \$18.75 Billion\***

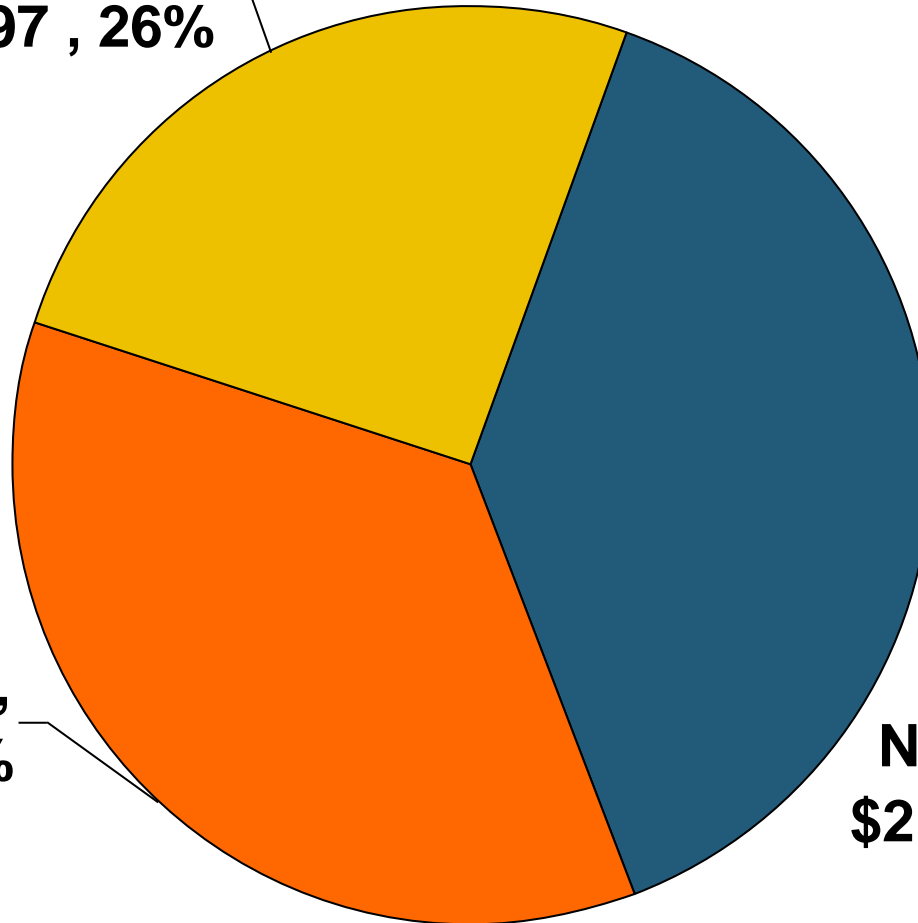


Although Commercial Lines accounted for only 13% of total claims, they account for 48% of all claim dollars paid. In most hurricanes, Commercial Lines accounts for about 1/3 of insured losses.

\*PCS insured loss estimates as of 1/18/13. Catastrophe modeler estimates range up to \$25 billion. All figures exclude losses paid by the NFIP. Source: PCS; Insurance Information Institute.

# Hurricane Sandy: Value of Homeowners Claims Paid, by State\* (\$ Millions)

**All Other,  
\$1,797 , 26%**



**New Jersey,  
\$2,500 , 36%**

**New York,  
\$2,700 , 38%**

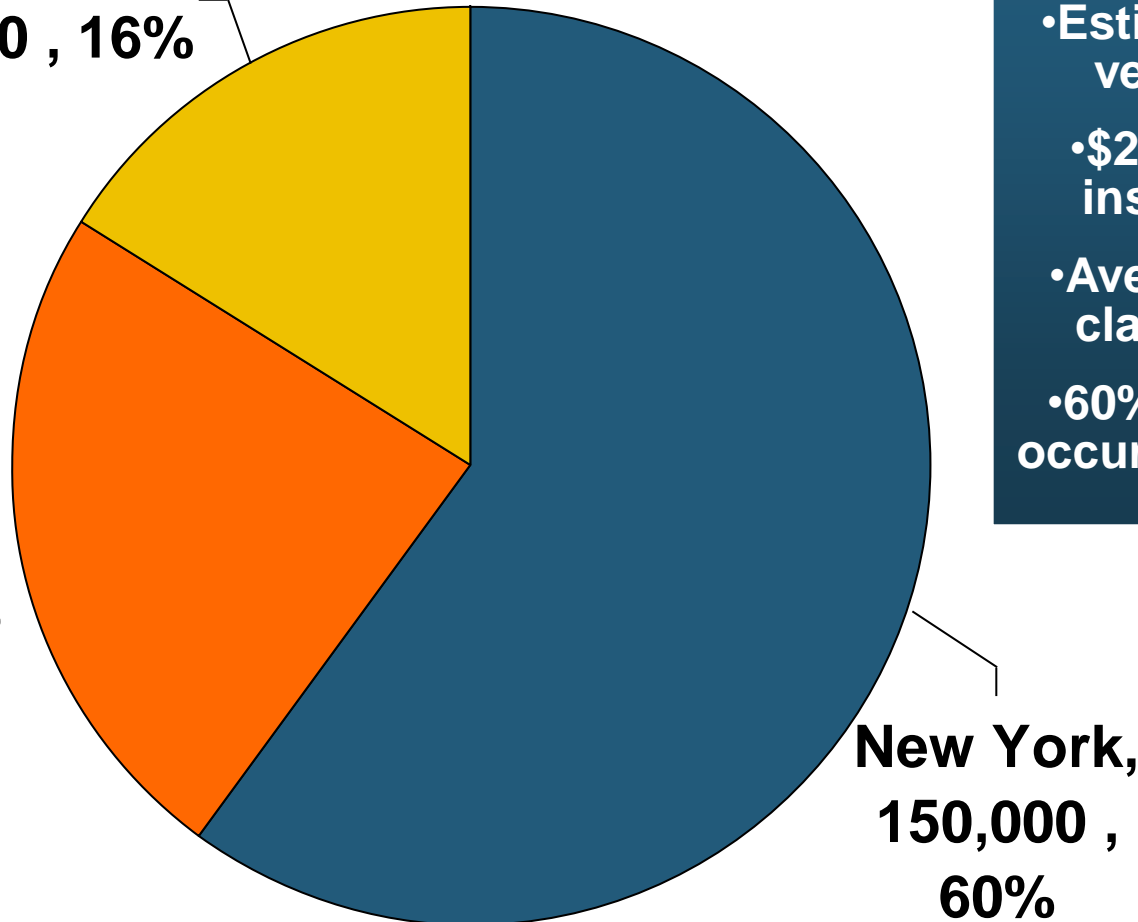
## Hurricane Sandy

- Estimated 1,067,000 homeowners claims\*\*
- \$7.0 billion in insured losses.
- Average loss per claim is \$6,558
- Claims in NJ estimated at \$2.5 billion (36%) and \$2.7 billion in NY (38%)

# Hurricane Sandy: Number of Auto Claims by State\*

All Other,  
40,500 , 16%

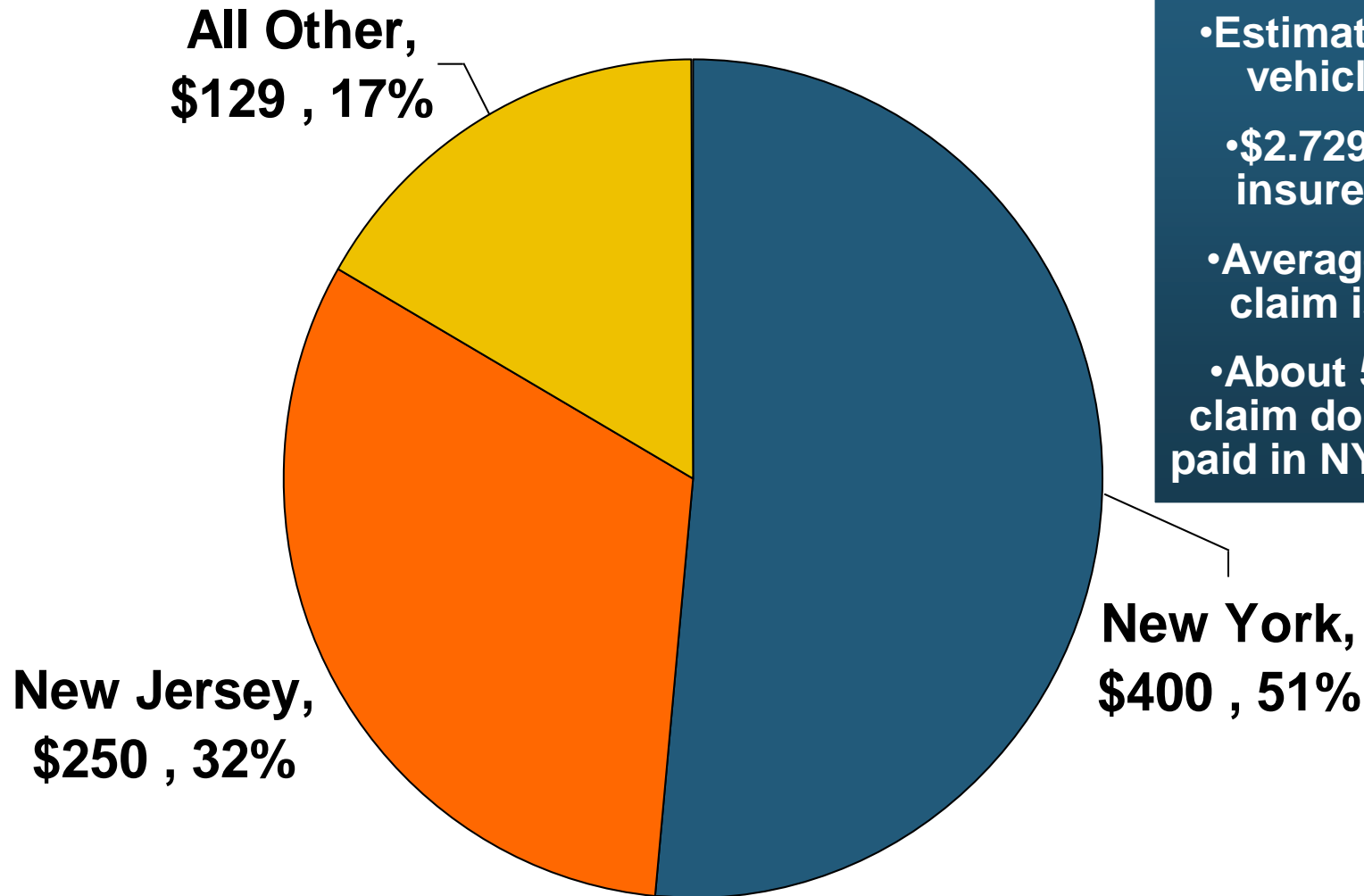
New Jersey,  
60,000 , 24%



## Hurricane Sandy

- Estimated 250,500 vehicle claims
- \$2.729 billion in insured losses.
- Average loss per claim is \$10,894
- 60% of the claims occurred in NY state.

# Hurricane Sandy: Value of Auto Claims Paid, by State\* (\$ Millions)

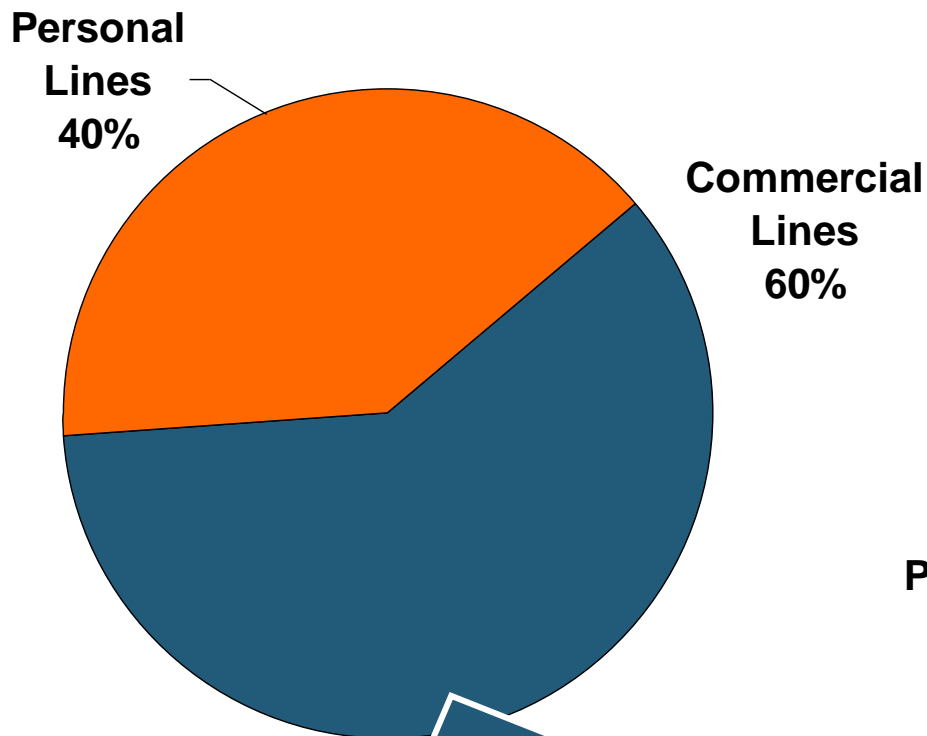


## Hurricane Sandy

- Estimated 250,500 vehicle claims
- \$2.729 billion in insured losses.
- Average loss per claim is \$10,894
- About 50% of the claim dollars will be paid in NY, 32% in NJ.

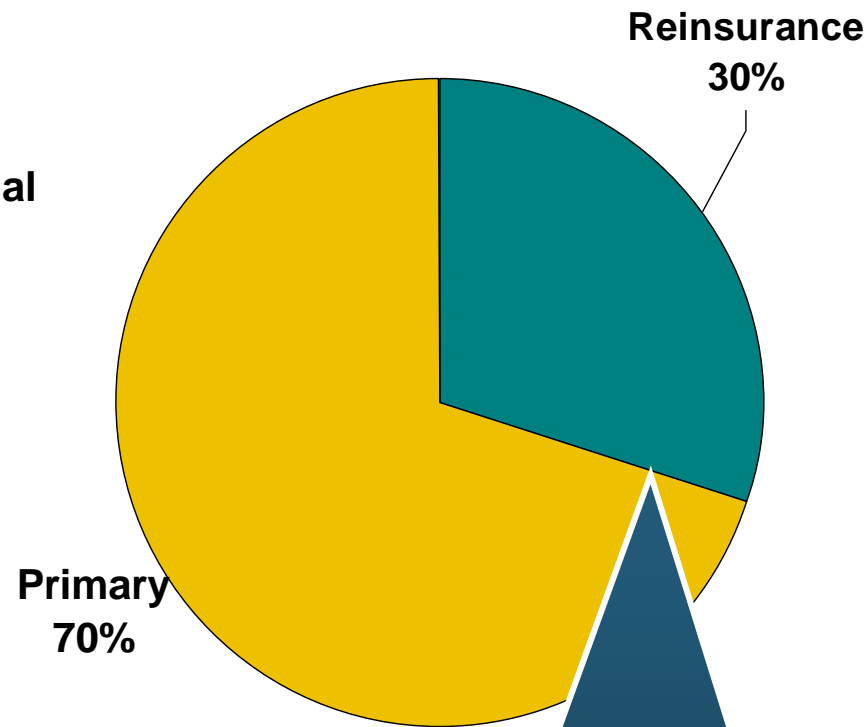
# Hurricane Sandy: Loss Distribution by Commercial/Personal Lines and Reinsurance vs. Primary Insurer

## Personal vs. Commercial Lines\*



**~60-65% of Sandy losses appear to be commercial lines, and 35-40% personal, the opposite of the norm for hurricane losses**

## Primary vs. Reinsurer Share\*\*

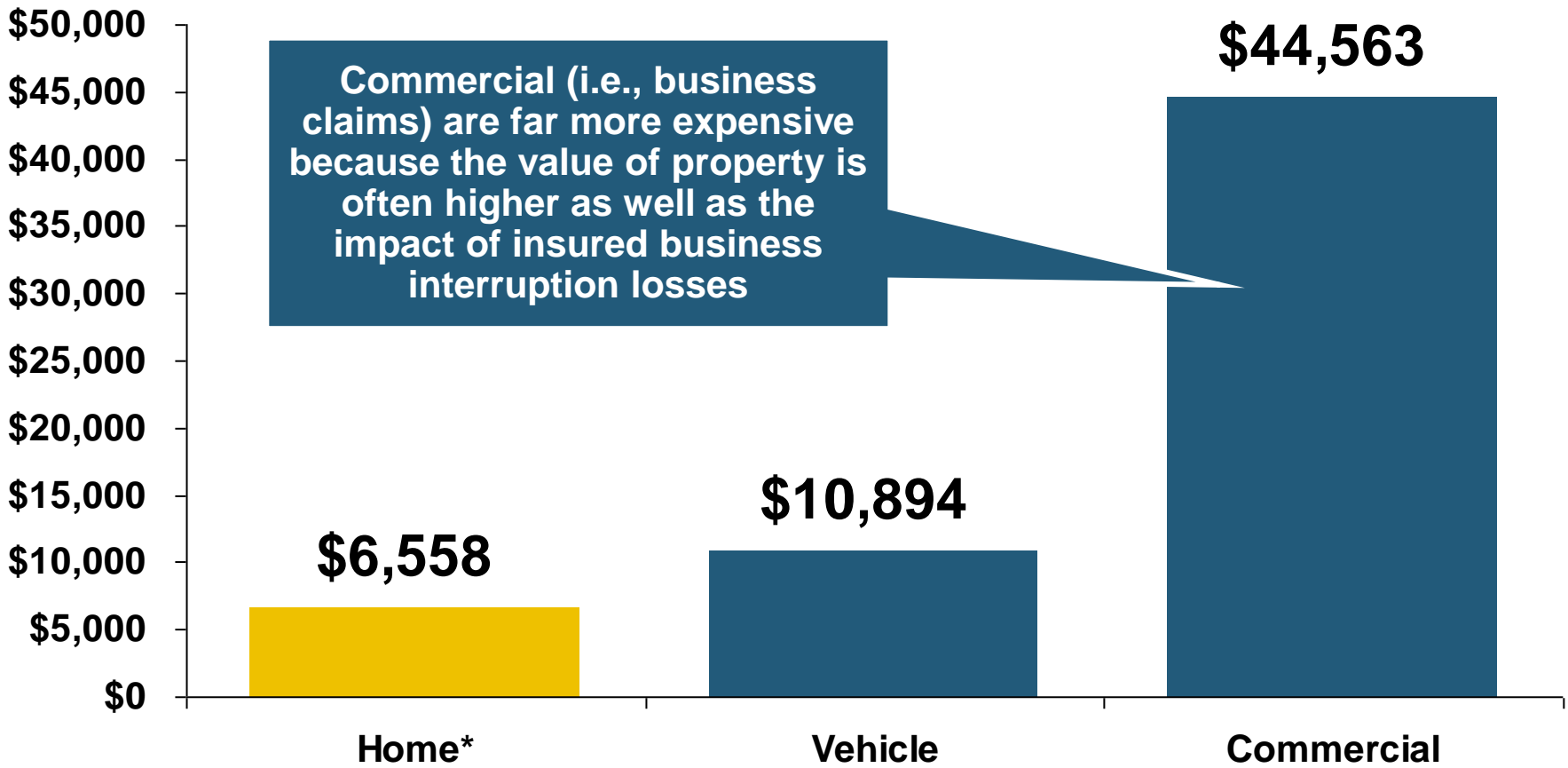


**Reinsurers' share of Sandy losses appears to be in the 30% range, though this is highly preliminary**

\*Fitch Ratings assigns a range of 60-65% commercial and 35-40% personal lines., *Hurricane Sandy Update*, January 8, 2013.

\*\*Source: Insurance Information Institute rough estimate based on company reports as of January 13, 2013. Actual number will vary.

# Hurricane Sandy: Average Claim Payment by Type of Claim



Commercial (i.e., business claims) are far more expensive because the value of property is often higher as well as the impact of insured business interruption losses

**Commercial (Business) Claims Were Nearly Seven Times More Expensive than Homeowners Claims; Vehicle Claims Were Unusually Expensive Due to Extensive Flooding**

\*Includes rental and condo policies.

Sources: Catastrophe loss data is for Catastrophe Serial No. 90 (Oct. 28 – 31, 2012) from PCS as of Jan. 18, 2013; Insurance Information Institute .



# U.S. Insured Catastrophe Loss Update

**2012 Catastrophe Losses Were Close to  
“Average” Until Sandy Hit  
*2011 Was the 5<sup>th</sup> Most Expensive  
Year on Record***



# Natural Disaster Losses in the United States: 2012

As of January 1, 2013	Number of Events	Fatalities	Estimated Overall Losses (US \$m)	Estimated Insured Losses (US \$m)
<b>Tropical Cyclone</b>	4	143	52,240	<b>26,360</b>
<b>Severe Thunderstorm</b>	115	118	27,688	<b>14,914</b>
<b>Drought</b>	2	0	20,000	<b>16,000<sup>†</sup></b>
<b>Wildfire</b>	38	13	1,112	<b>595</b>
<b>Winter Storm</b>	2	7	81	<b>38</b>
<b>Flood</b>	19	3	13	<b>0<sup>††</sup></b>
<b>TOTALS</b>	<b>184</b>	<b>284</b>	<b>\$101,134</b>	<b>\$57,907</b>

Source: MR NatCatSERVICE

† - Includes Federal Crop Insurance Losses. †† - Excludes federal flood.

# Significant Natural Catastrophes, 2012

(Events with \$1 billion economic loss and/or 50 fatalities)



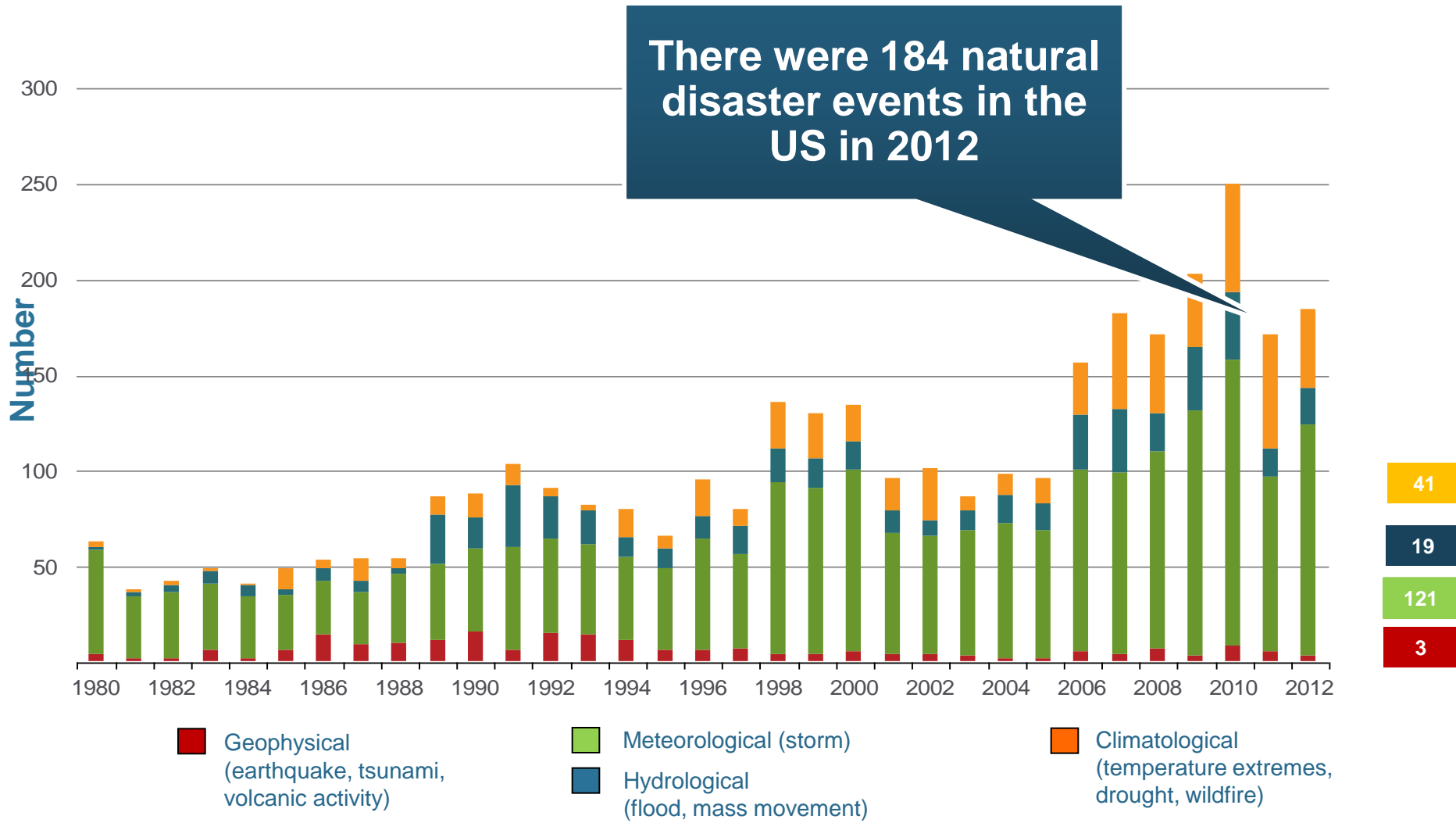
Date	Event	Estimated Economic Losses (US \$m)	Estimated Insured Losses (US \$m)
June – Sept 2012	Central US Drought	20,000	16,000 <sup>†</sup>
March 2 - 3	Thunderstorms	5,000	2,500
April 2 – 4	Thunderstorms	1,550	775
April 13- 15	Thunderstorms	1,800	910
April 28 – 29	Thunderstorms	4,500	2,500
May 25 – 30	Thunderstorms	3,400	1,700
June 6 – 7	Thunderstorms	1,400	1,000
June 11 – 13	Thunderstorms	1,900	950
June 28 – July 2	Thunderstorms	4,000	2,000
August 26 - 30	Hurricane Isaac	2,000	1,220
October 28 - 30	Hurricane Sandy	50,000	25,000 <sup>††</sup>

Source: MR NatCatSERVICE

<sup>†</sup> - Includes Federal Crop Insurance Losses.; <sup>††</sup> - Excludes NFIP losses.

# Natural Disasters in the United States, 1980 – 2012

Number of Events (Annual Totals 1980 – 2012)



# Losses Due to Natural Disasters in the US, 1980–2012 (Overall & Insured Losses)

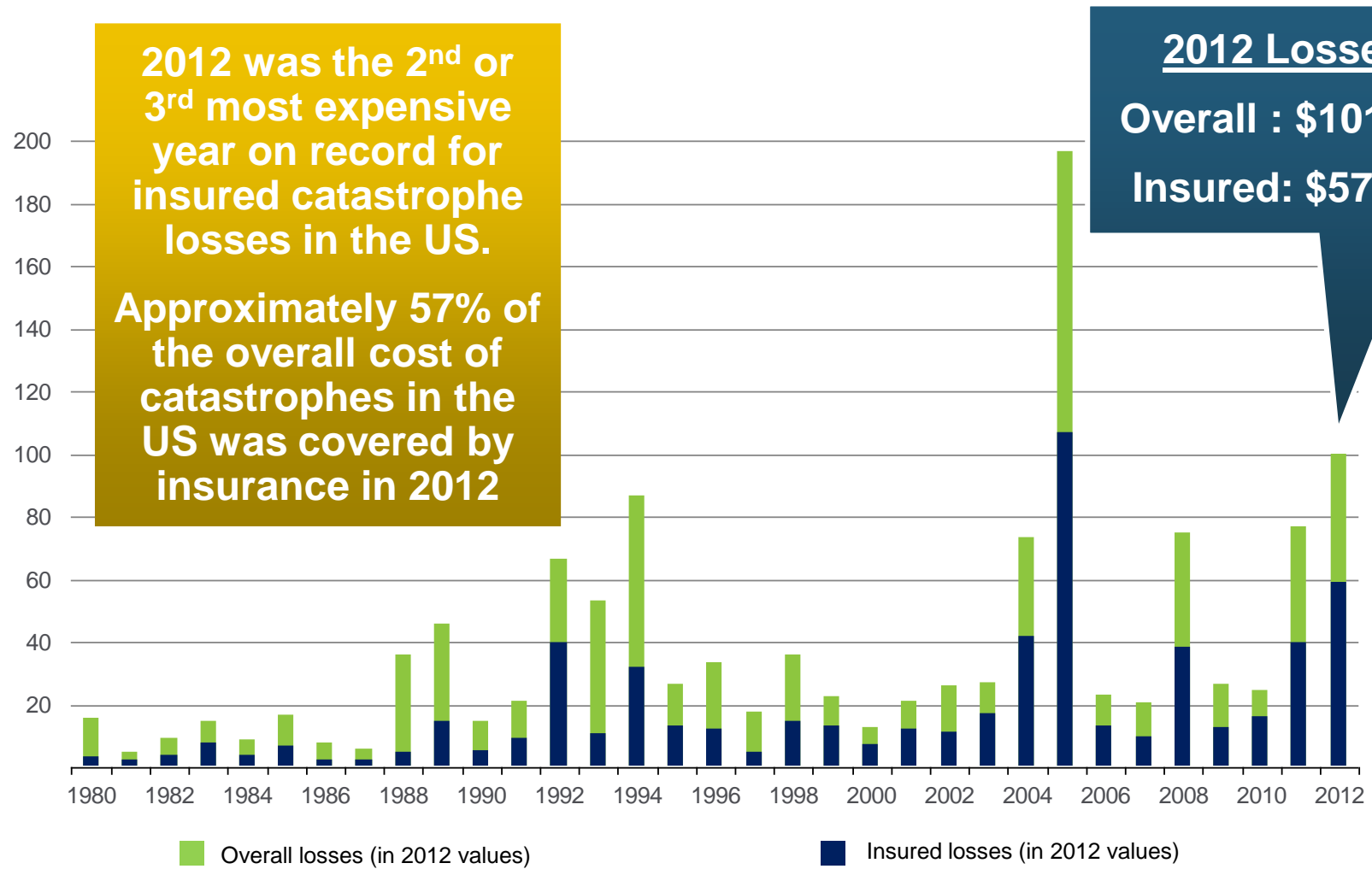
## (Overall and Insured Losses)

(2012 Dollars, \$ Billions)

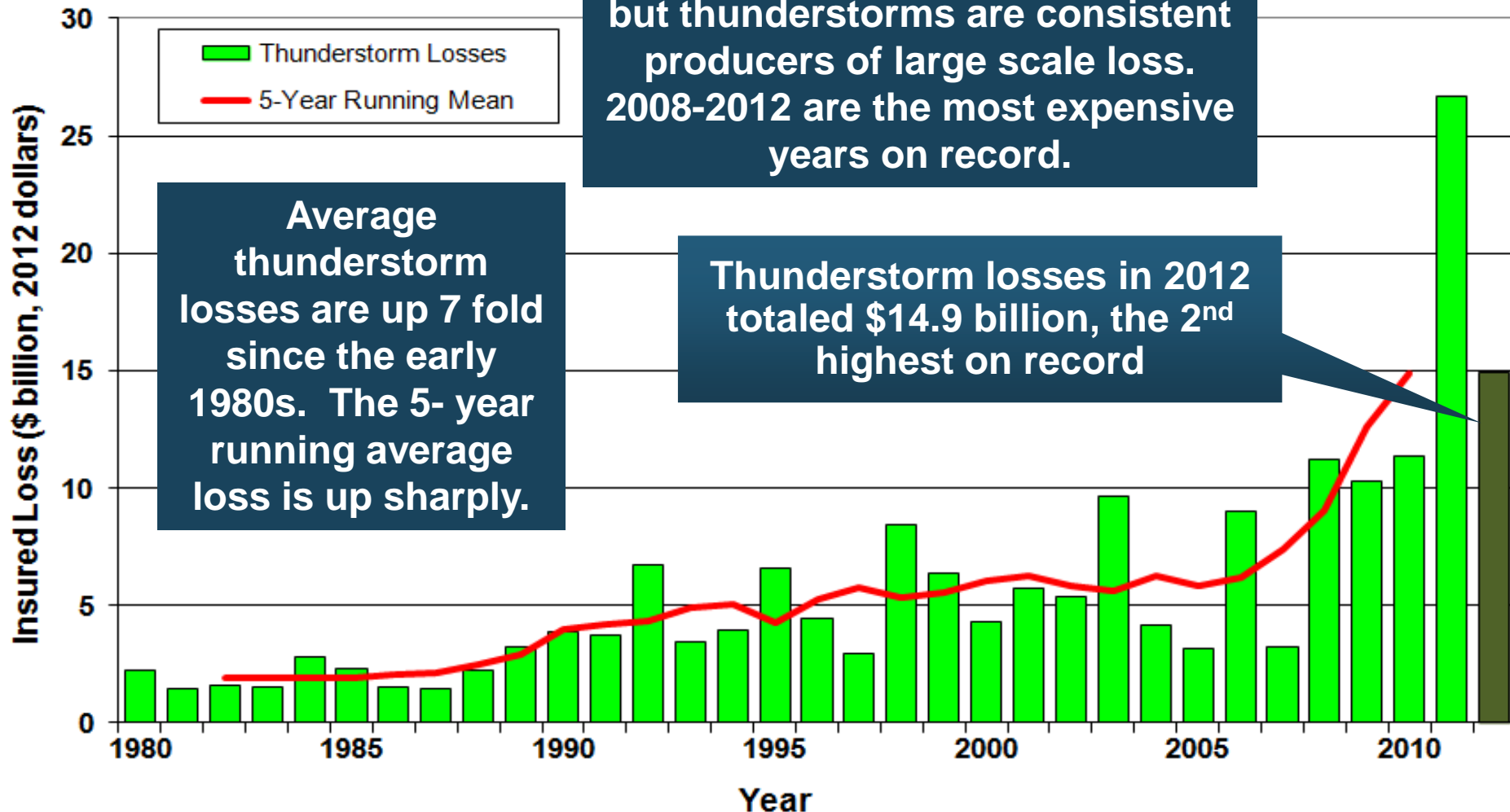
**2012 was the 2<sup>nd</sup> or 3<sup>rd</sup> most expensive year on record for insured catastrophe losses in the US.**

**Approximately 57% of the overall cost of catastrophes in the US was covered by insurance in 2012**

**2012 Losses**  
**Overall : \$101.1B**  
**Insured: \$57.9B**



# U.S. Thunderstorm Loss Trends, 1980 – 2012



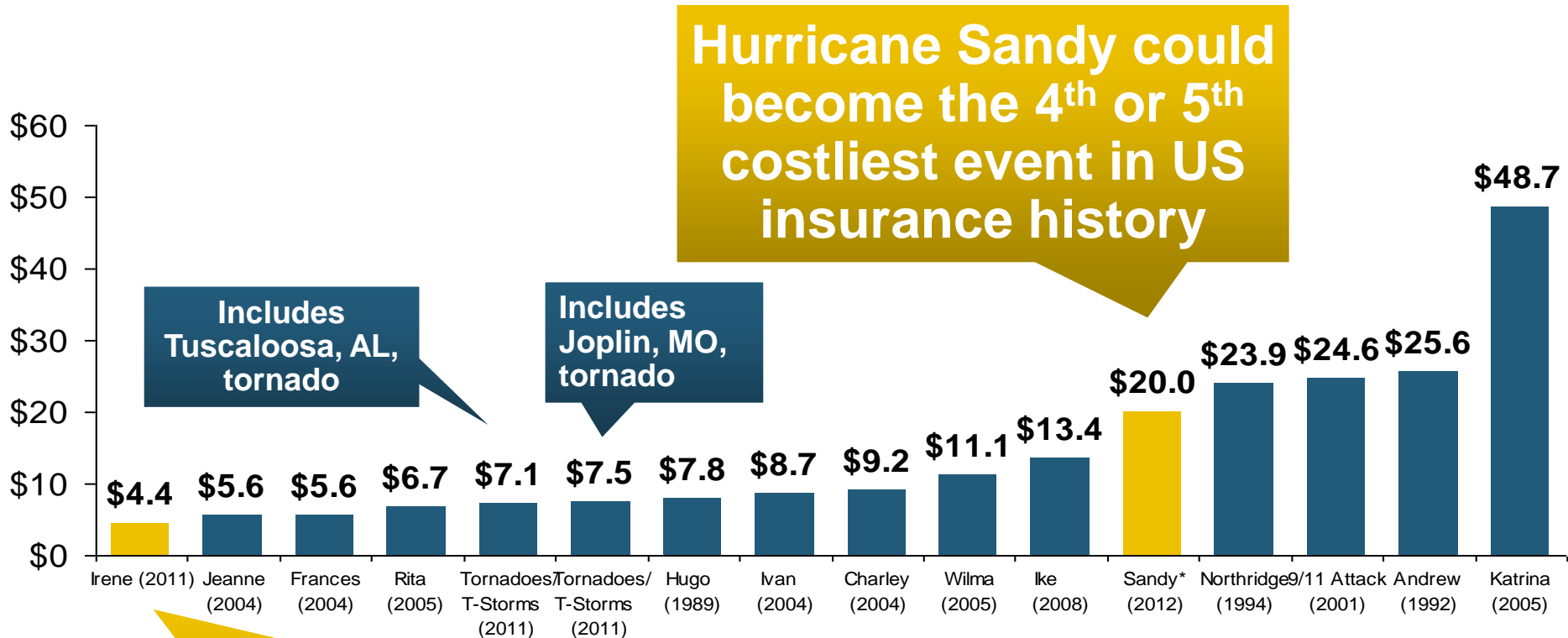
Hurricanes get all the headlines, but thunderstorms are consistent producers of large scale loss. 2008-2012 are the most expensive years on record.

Average thunderstorm losses are up 7 fold since the early 1980s. The 5- year running average loss is up sharply.

Thunderstorm losses in 2012 totaled \$14.9 billion, the 2<sup>nd</sup> highest on record

# Top 16 Most Costly Disasters in U.S. History

(Insured Losses, 2012 Dollars, \$ Billions)



Hurricane Sandy could become the 4<sup>th</sup> or 5<sup>th</sup> costliest event in US insurance history

Includes Tuscaloosa, AL, tornado

Includes Joplin, MO, tornado

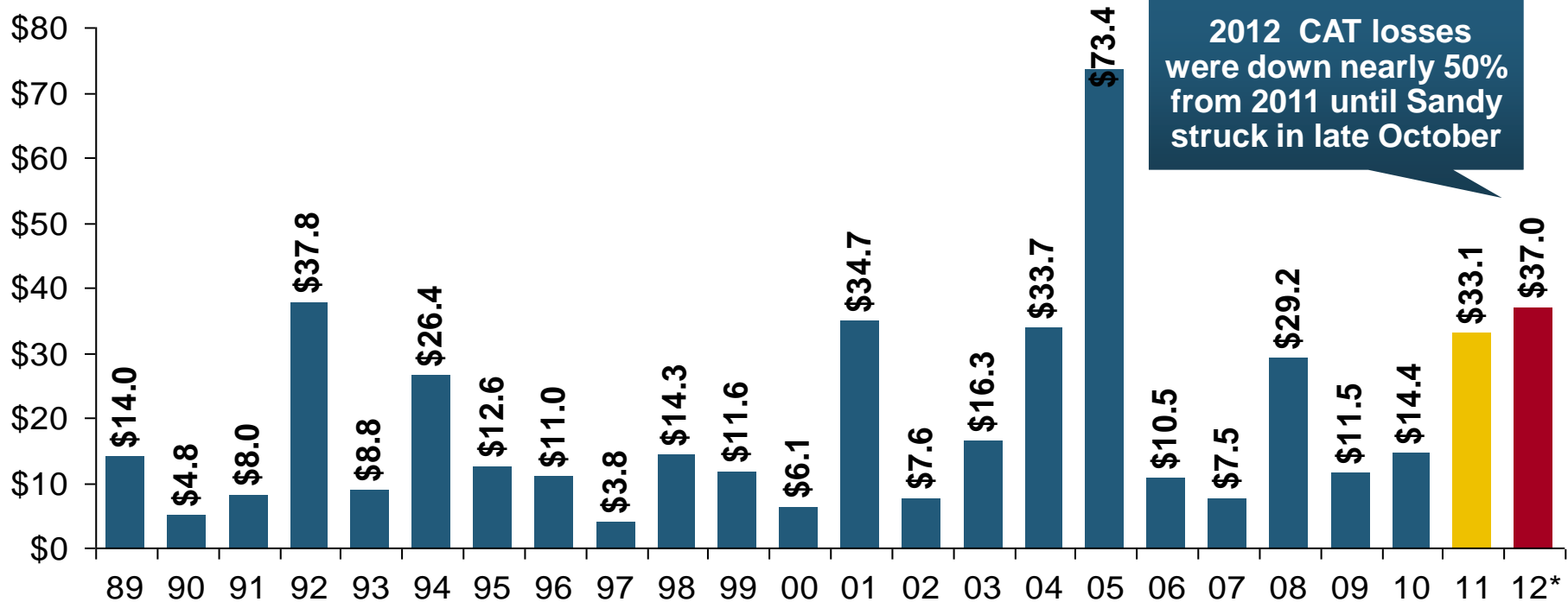
Hurricane Irene became the 12<sup>th</sup> most expensive hurricane in US history in 2011

12 of the 16 Most Expensive Events in US History Have Occurred Over the Past Decade

\*Estimate as of 12/09/12 based on estimates of catastrophe modeling firms and reported losses as of 1/12/13. Estimates range up to \$25B. Sources: PCS; Insurance Information Institute inflation adjustments to 2012 dollars using the CPI.

# US Insured Catastrophe Losses

(\$ Billions, 2012 Dollars)



**US CAT Losses in 2012 Will Likely Become the 2<sup>nd</sup> or 3<sup>rd</sup> Highest in US History on An Inflation-Adjusted Basis (Pvt Insured). 2011 Losses Were the 5<sup>th</sup> Highest**

**Record Tornado Losses Caused 2011 CAT Losses to Surge**

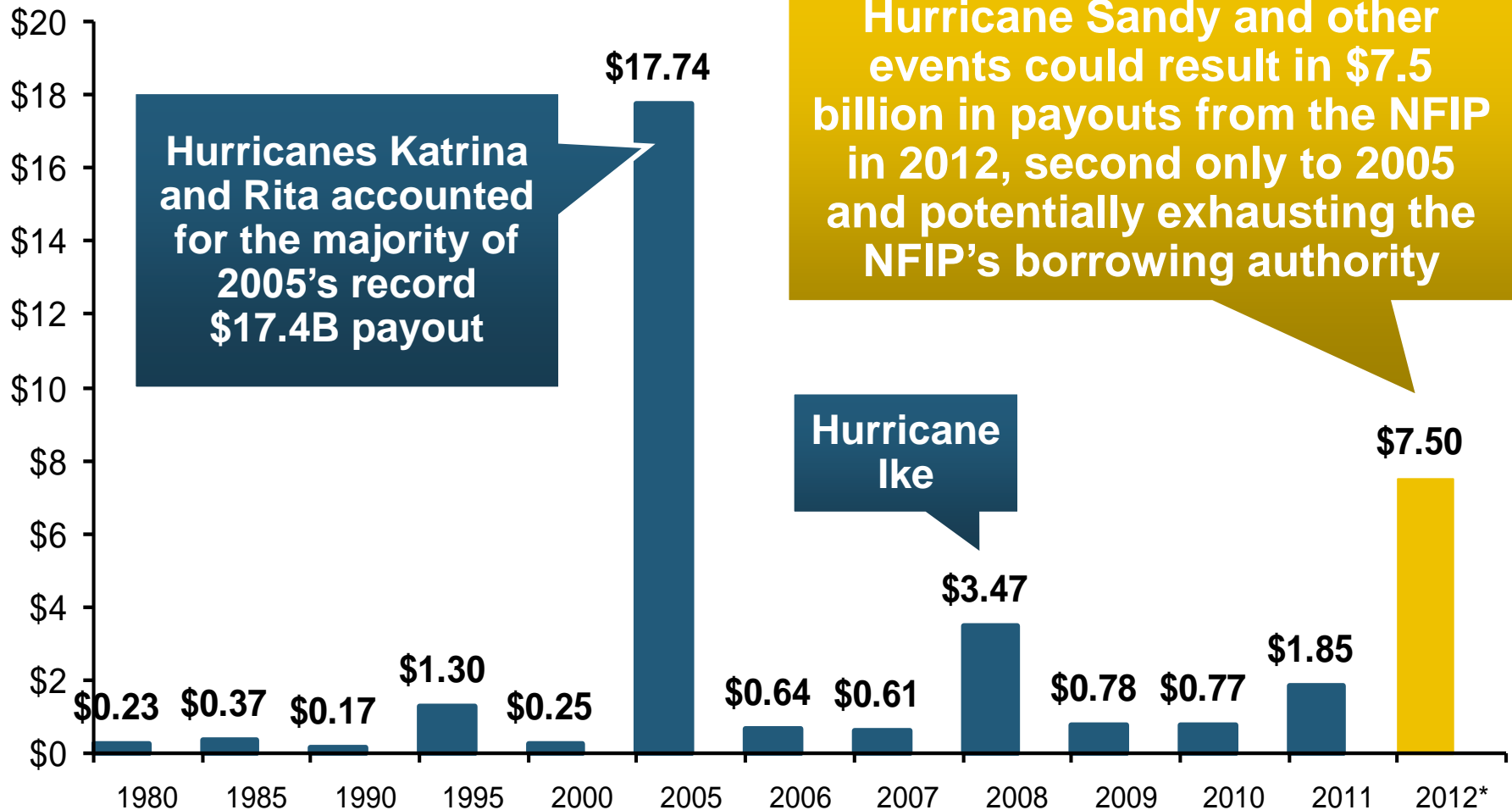
\*As of 1/2/13. Includes \$20B gross loss estimate for Hurricane Sandy.

Note: 2001 figure includes \$20.3B for 9/11 losses reported through 12/31/01 (\$25.9B 2011 dollars). Includes only business and personal property claims, business interruption and auto claims. Non-prop/BI losses = \$12.2B (\$15.6B in 2011 dollars.)

Sources: Property Claims Service/ISO; Insurance Information Institute.

# Flood Loss Paid by the National Flood Insurance Program, 1980-2012E

Billions (Original Values)

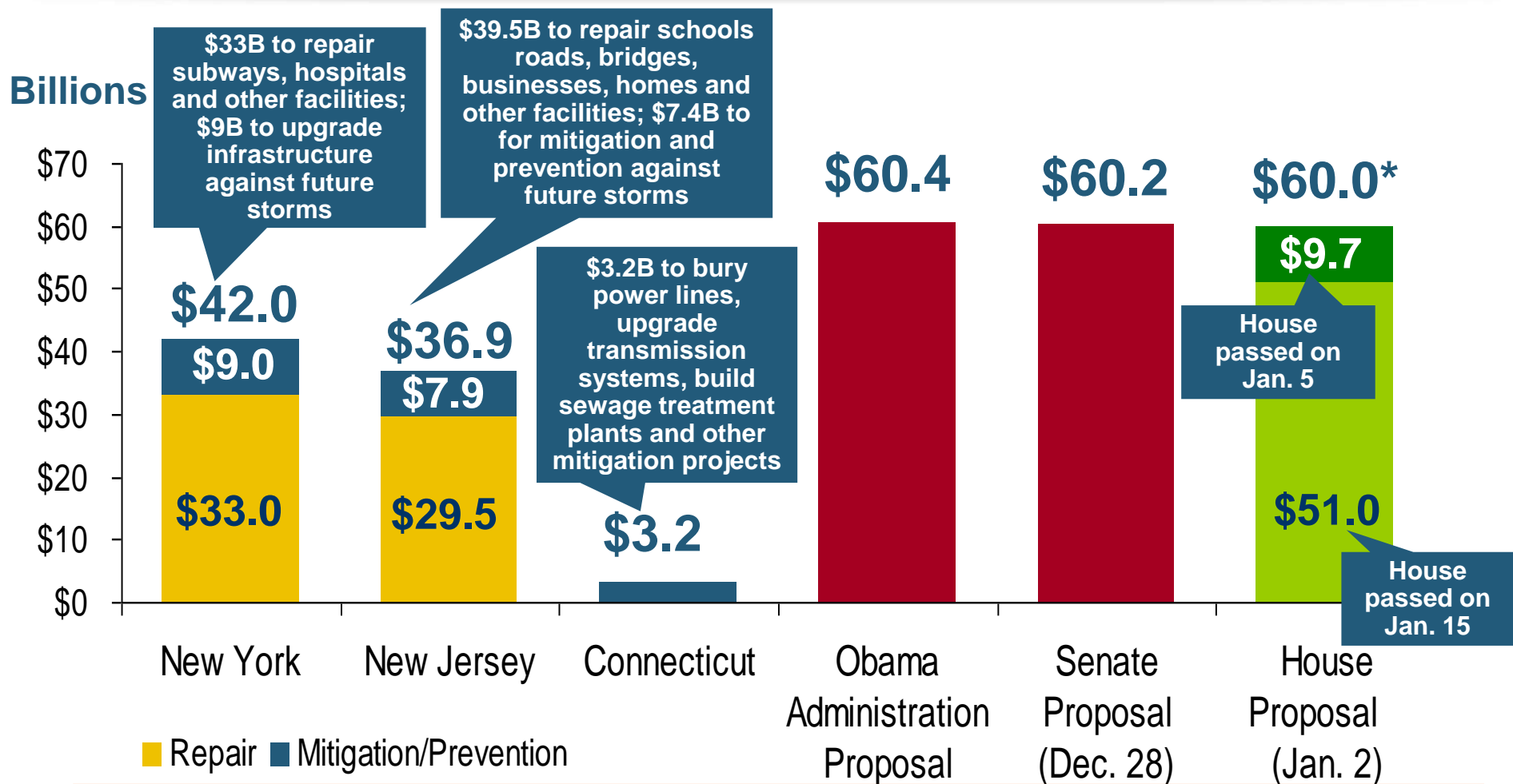


\*Estimate as of 11/25/12.

Sources: Department of Homeland Security, Federal Emergency Management Agency, NFIP; Insurance Information Institute.



# Federal Aid Requests for States With Greatest Sandy Impact & Federal Aid Proposals (as of 1/6/13)



**States Requested Enormous Sums in Sandy Aid in the Middle of the "Fiscal Cliff" Debate, Causing Delays**

\*As of Jan. 2, 2013.

Source: *New York Times*, Dec. 6, 2012; Insurance Information Institute research.

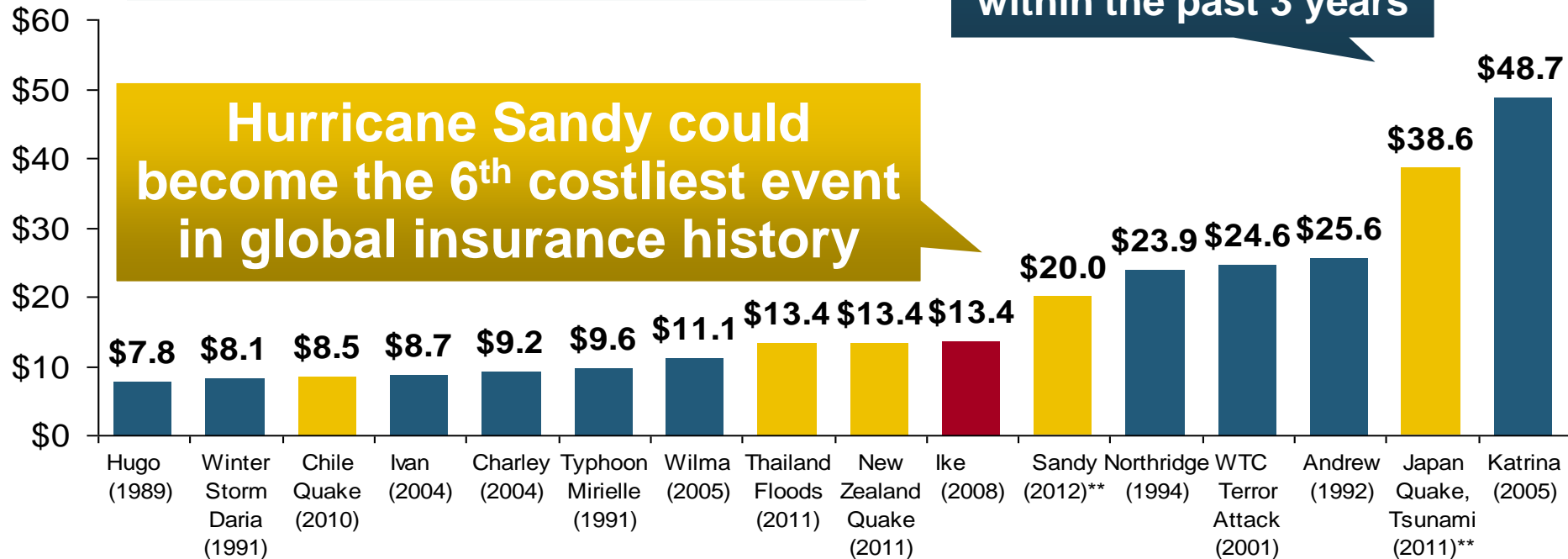
# Top 16 Most Costly World Insurance Losses, 1970-2012\*

(Insured Losses, 2012 Dollars, \$ Billions)

**2012 insured CAT Losses totaled \$60B; Economic losses totaled \$140B, according to Swiss Re**

**5 of the top 14 most expensive catastrophes in world history have occurred within the past 3 years**

**Hurricane Sandy could become the 6<sup>th</sup> costliest event in global insurance history**

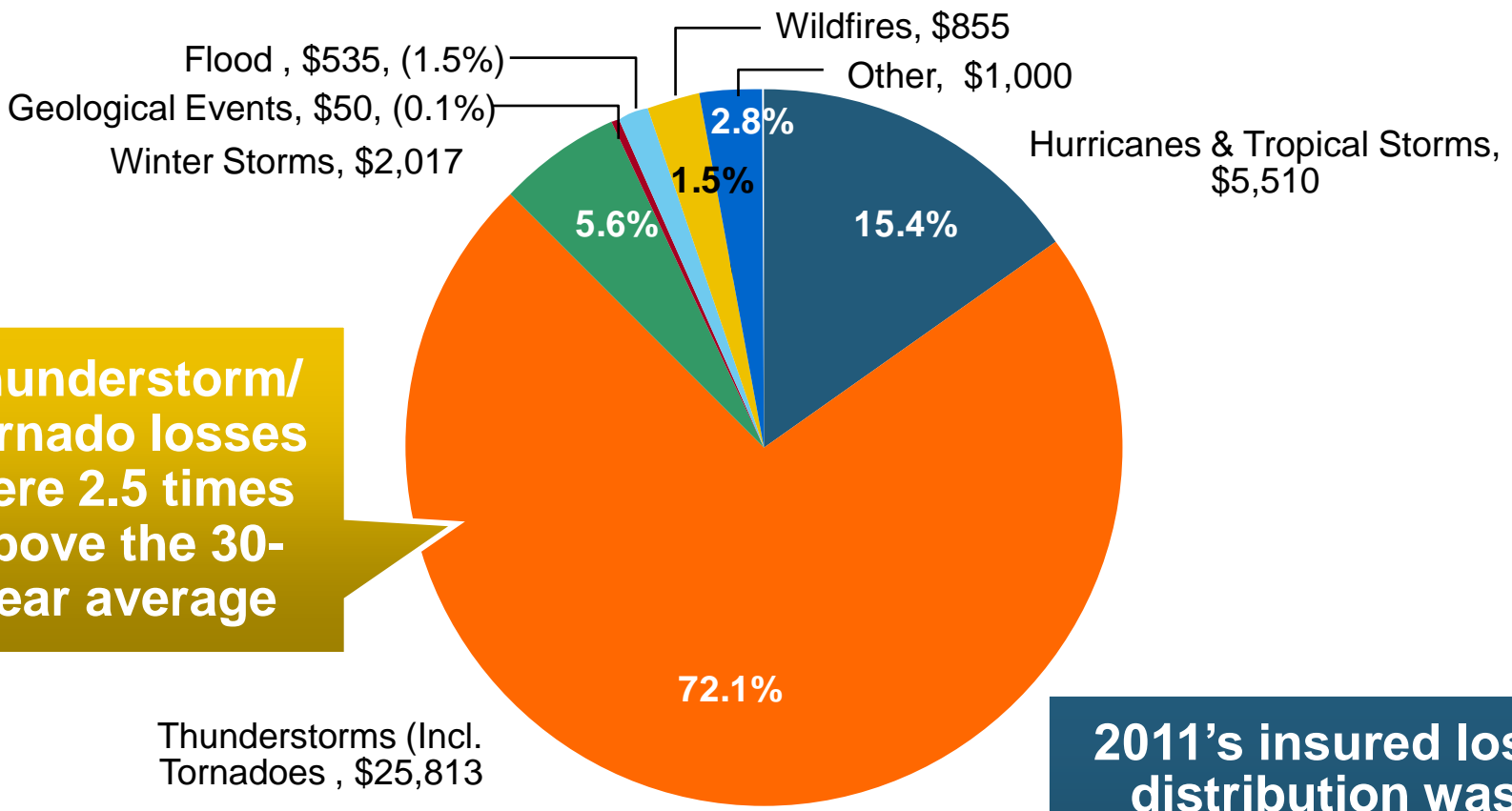


\*Figures do not include federally insured flood losses.

\*\*Estimate based on PCS value of \$18.75B as of 1/18/13 and assumption of upward development based on catastrophe modeler estimates ranging as high as \$25B.

Sources: Swiss Re *sigma* 1/2011; Munich Re; Insurance Information Institute research.

# U.S. Insured Catastrophe Losses by Cause of Loss, 2011 (\$ Millions)

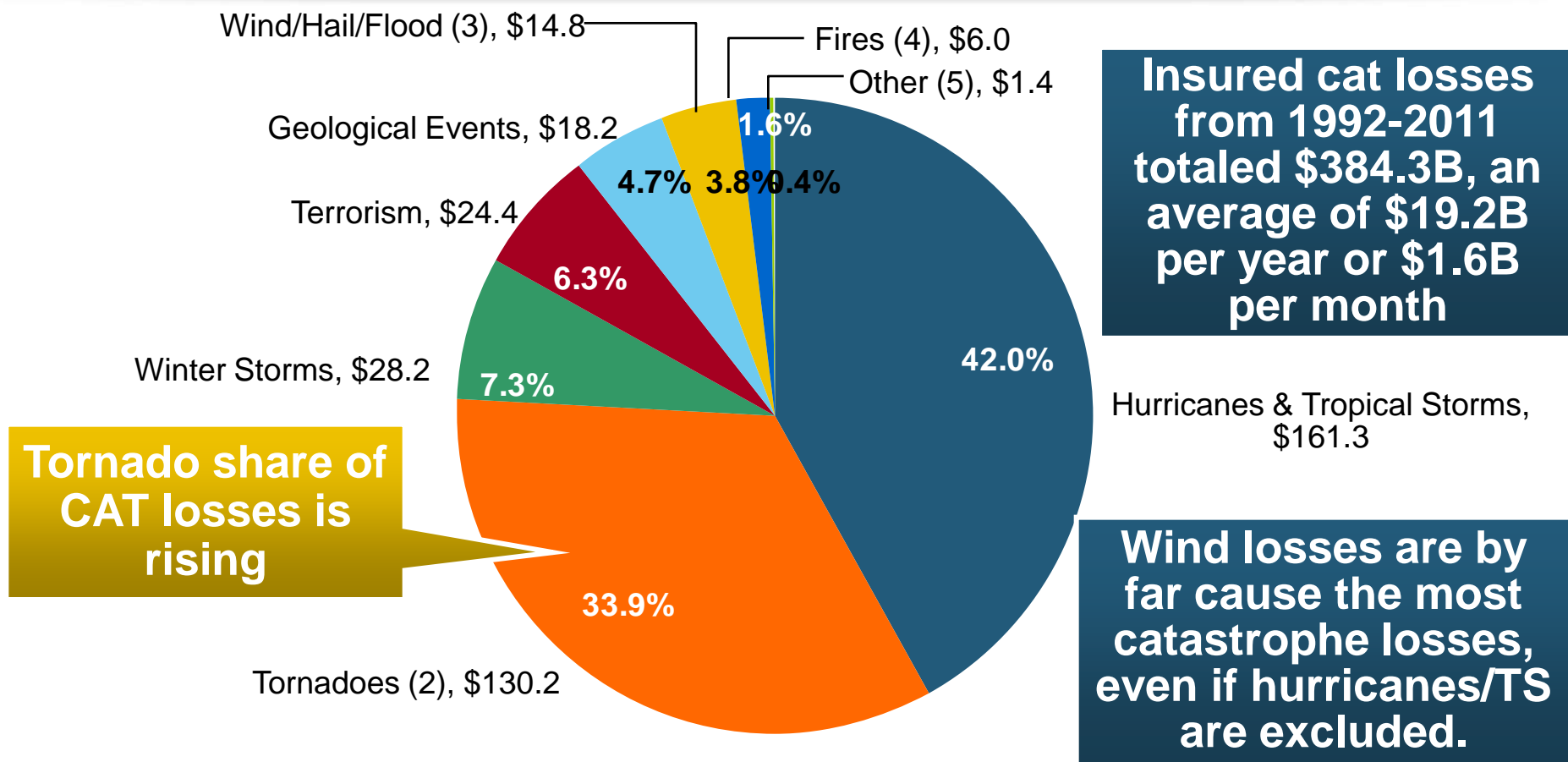


**Thunderstorm/  
Tornado losses  
were 2.5 times  
above the 30-  
year average**

**2011's insured loss  
distribution was  
unusual with tornado  
and thunderstorm  
accounting for the  
vast majority of loss**

Source: ISO's Property Claim Services Unit, Munich Re; Insurance Information Institute.

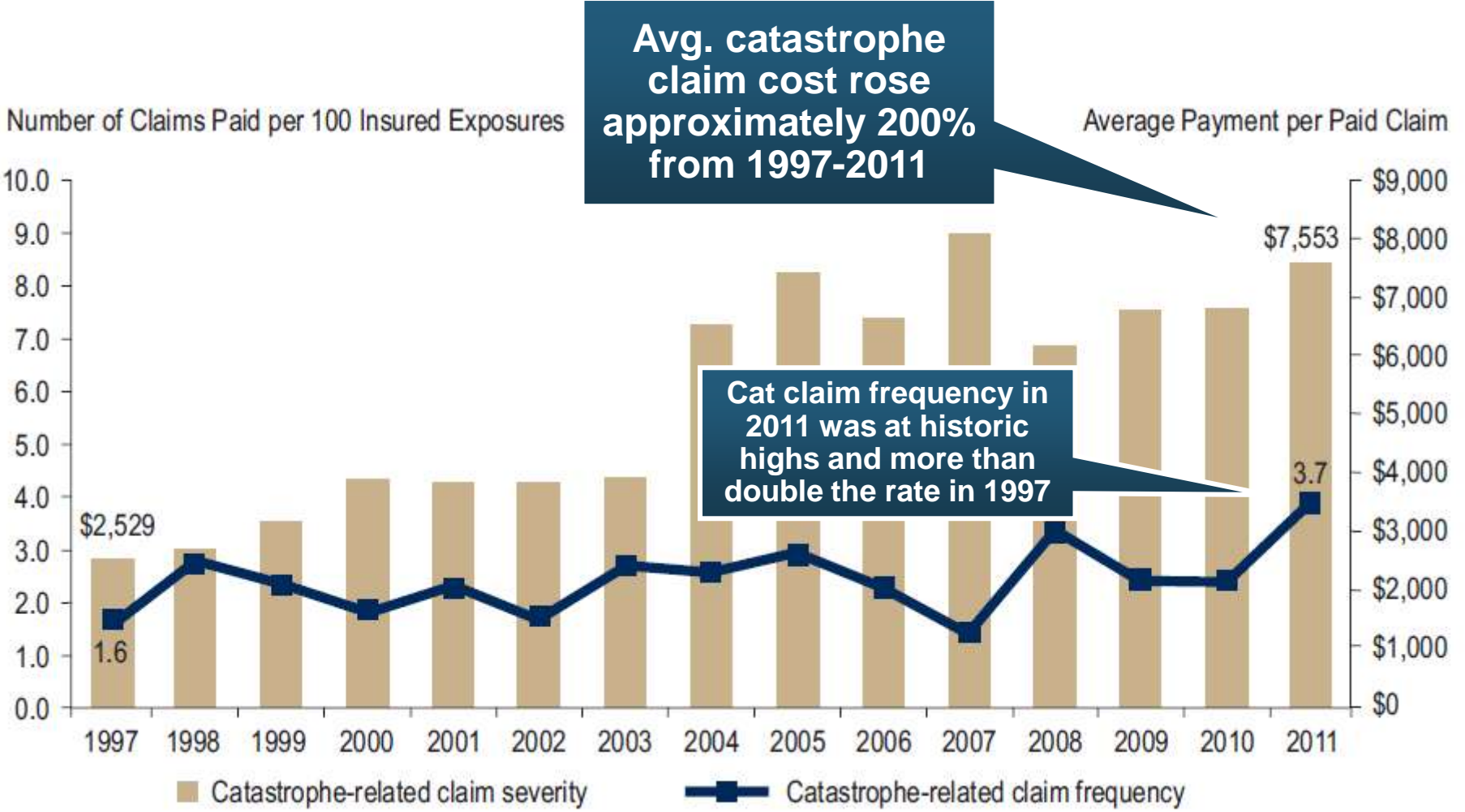
# Inflation Adjusted U.S. Catastrophe Losses by Cause of Loss, 1990–2011<sup>1</sup>



1. Catastrophes are defined as events causing direct insured losses to property of \$25 million or more in 2009 dollars.
2. Excludes snow.
3. Does not include NFIP flood losses
4. Includes wildland fires
5. Includes civil disorders, water damage, utility disruptions and non-property losses such as those covered by workers compensation.

Source: ISO's Property Claim Services Unit.

# Homeowners Insurance Catastrophe-Related Claim Frequency and Severity, 1997—2012\*



\*All policy forms combined, countrywide.

Source: Insurance Research Council, *Trends in Homeowners Insurance Claims*, Sept. 2012 from ISO Fast Track data.

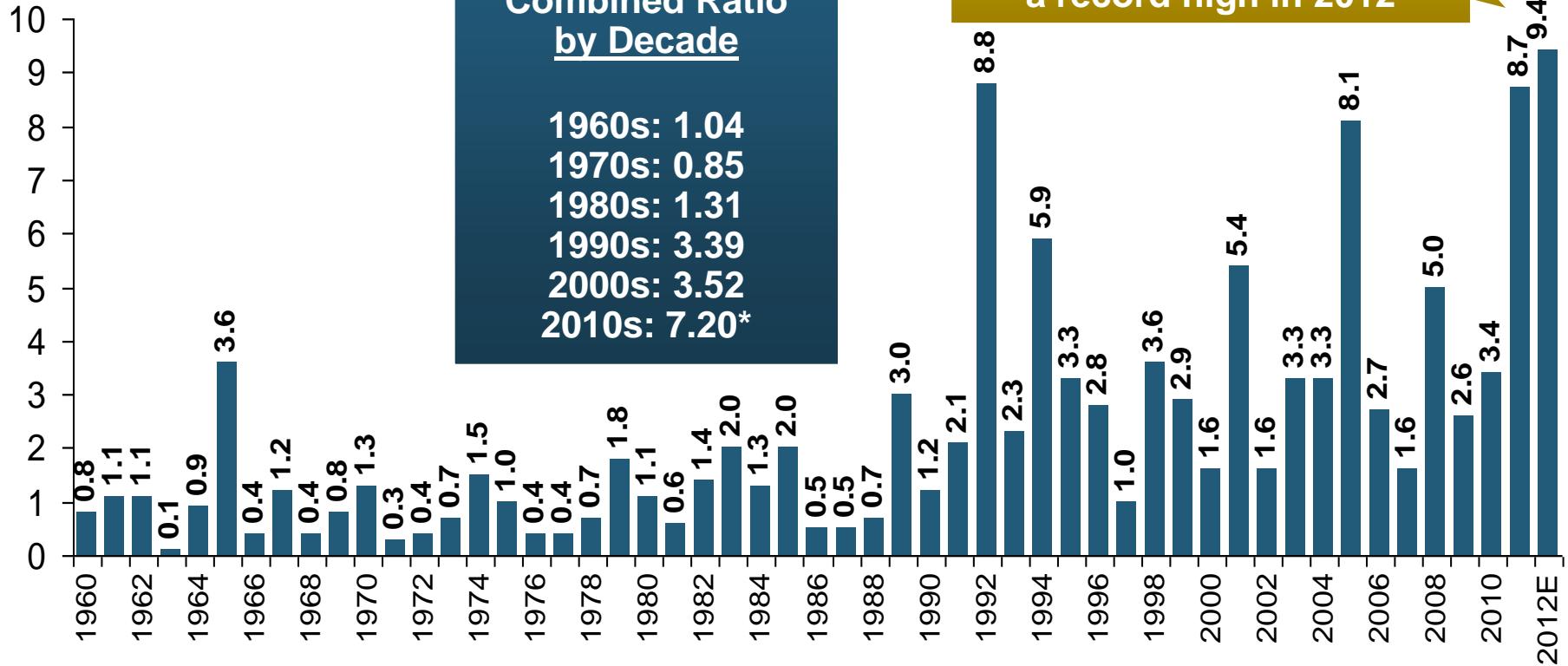
# Combined Ratio Points Associated with Catastrophe Losses: 1960 – 2012\*

## Combined Ratio Points

**Avg. CAT Loss Component of the Combined Ratio by Decade**

1960s: 1.04  
 1970s: 0.85  
 1980s: 1.31  
 1990s: 3.39  
 2000s: 3.52  
 2010s: 7.20\*

Catastrophe losses as a share of all losses reached a record high in 2012



**The Catastrophe Loss Component of Private Insurer Losses Has Increased Sharply in Recent Decades**

Notes: Private carrier losses only. Excludes loss adjustment expenses and reinsurance reinstatement premiums. Figures are adjusted for losses ultimately paid by foreign insurers and reinsurers.

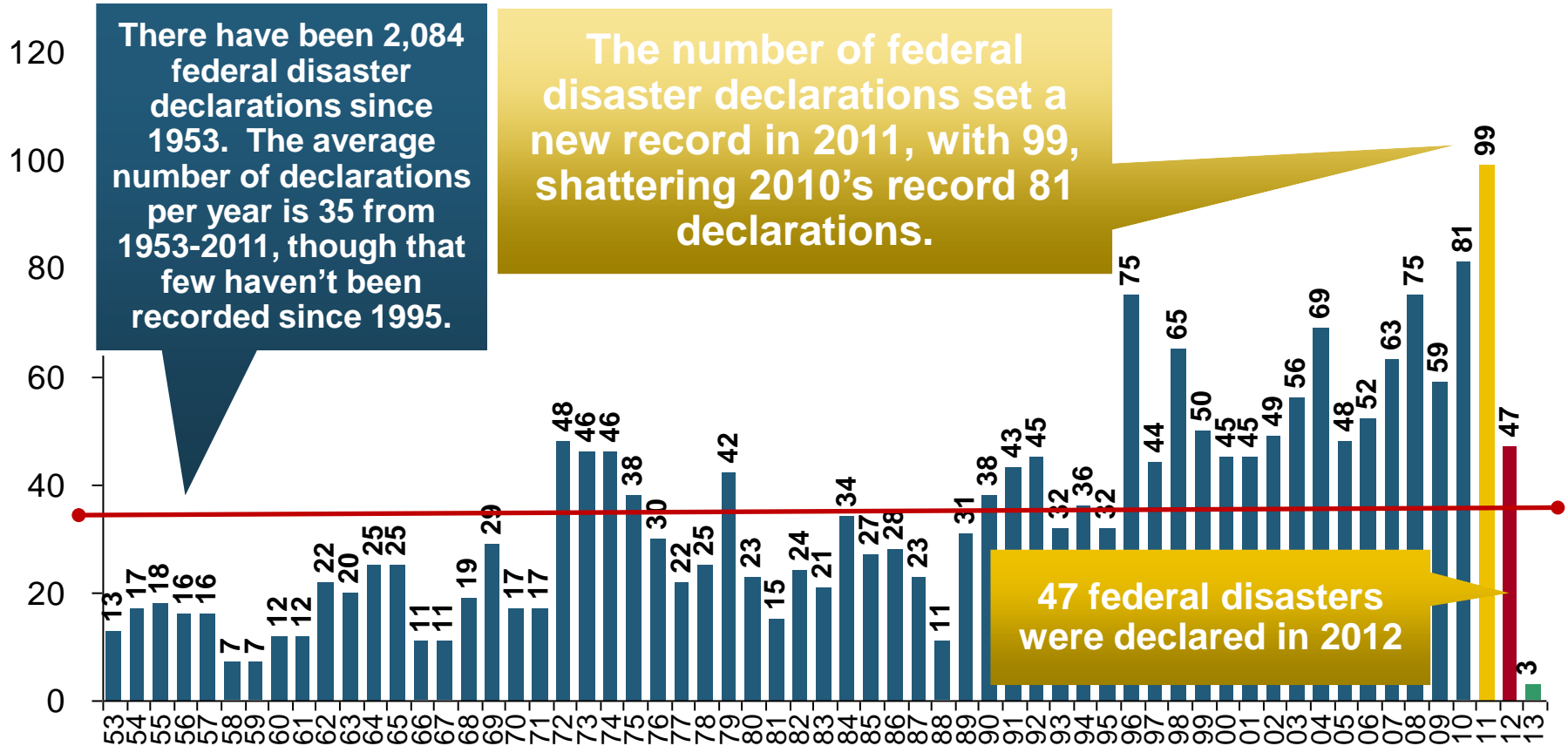
Source: ISO (1960-2011); A.M. Best (2012E) Insurance Information Institute.



# Federal Disaster Declarations Patterns: 1953-2012

**Despite 11 Sandy Declarations,  
Fewer Disasters Were Declared in  
2012 than the Record Number of  
Declarations in 2010 and 2011**

# Number of Federal Disaster Declarations, 1953-2013\*



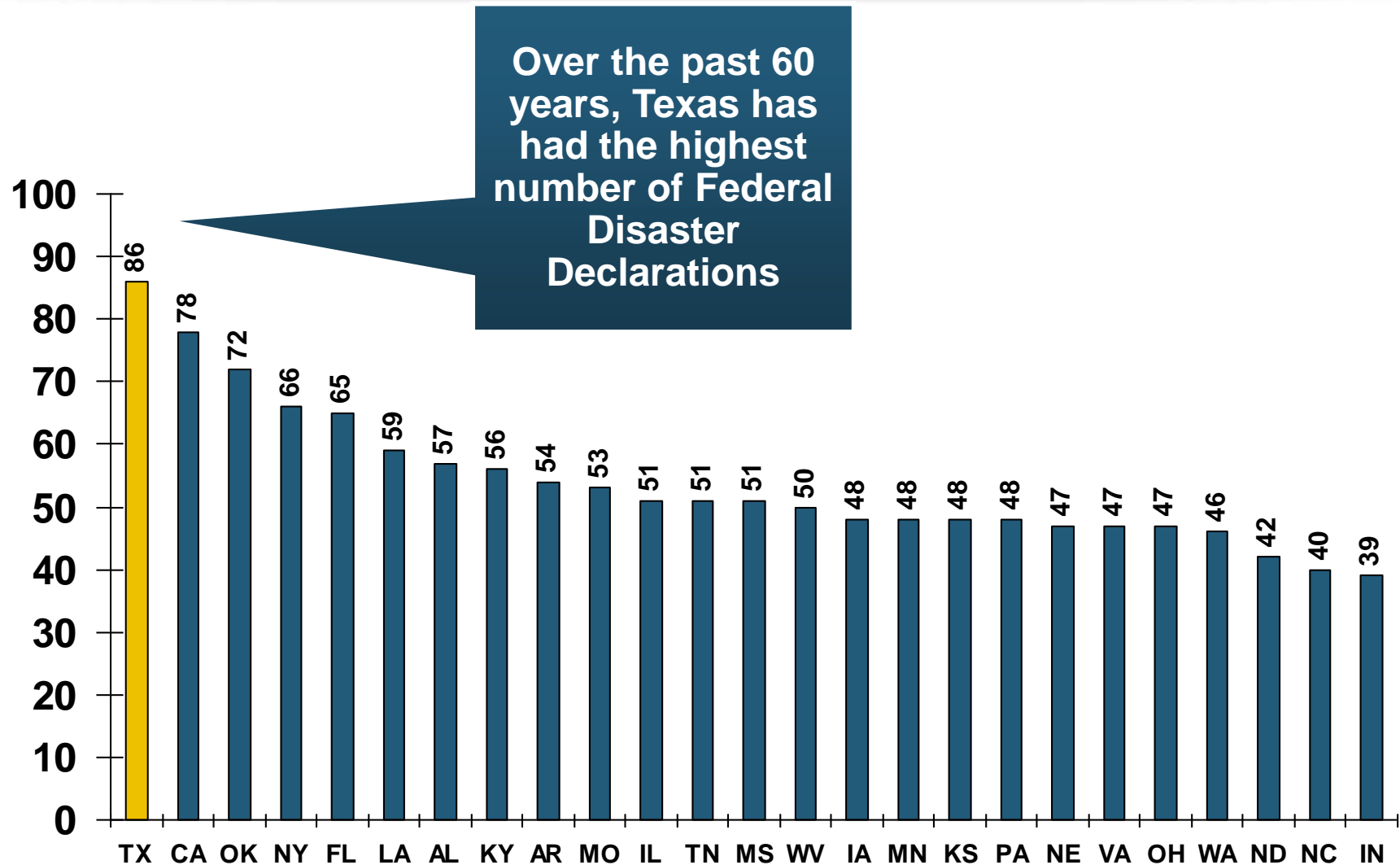
**The Number of Federal Disaster Declarations Is Rising and Set New Records in 2010 and 2011. Hurricane Sandy Produced 13 Declarations in 2012/13.**

\*Through Jan. 31, 2013.

Source: Federal Emergency Management Administration; <http://www.fema.gov/disasters>; Insurance Information Institute.



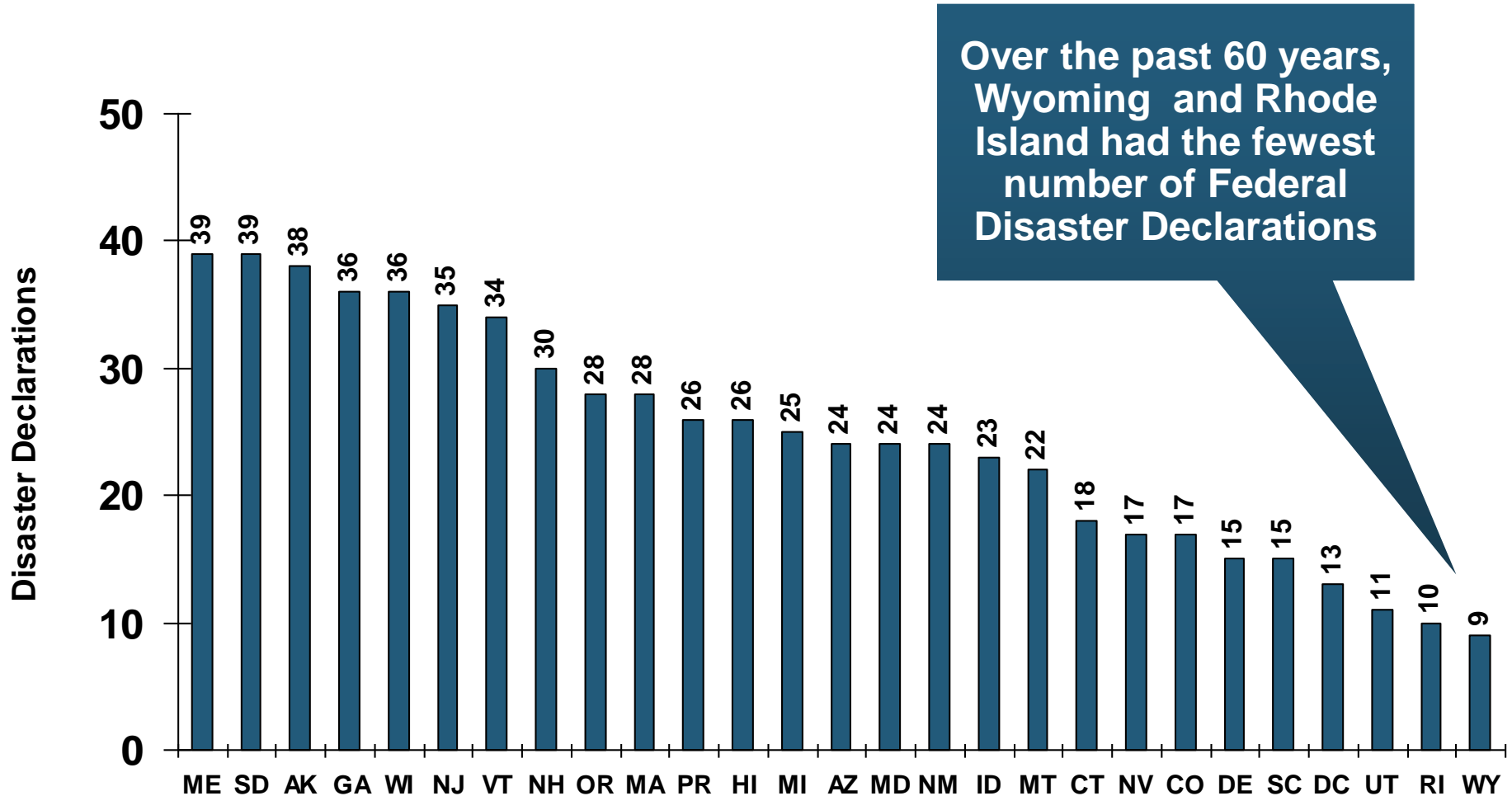
# Federal Disasters Declarations by State, 1953 – 2013: Highest 25 States\*



\*Through Jan. 31, 2012. Includes Puerto Rico and the District of Columbia.

Source: FEMA: [http://www.fema.gov/news/disaster\\_totals\\_annual.fema](http://www.fema.gov/news/disaster_totals_annual.fema); Insurance Information Institute.

# Federal Disasters Declarations by State, 1953 – 2012: Lowest 25 States\*



\*Through Jan. 31, 2013. Includes Puerto Rico and the District of Columbia.

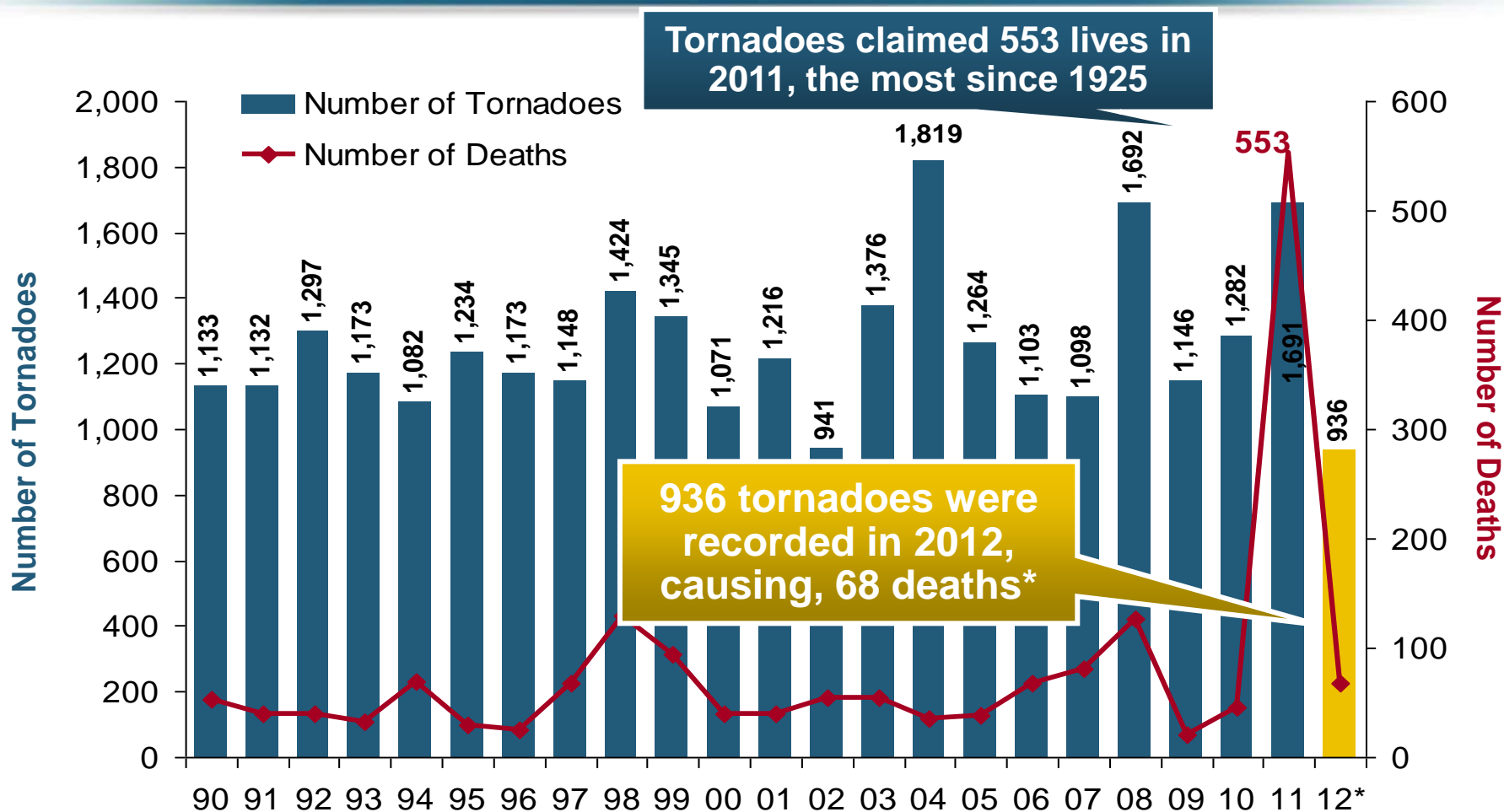
Source: FEMA: [http://www.fema.gov/news/disaster\\_totals\\_annual.fema](http://www.fema.gov/news/disaster_totals_annual.fema); Insurance Information Institute.



## **2012 TORNADO & SEVERE STORM SUMMARY**

**2012 Got Off to a Worrisome Start,  
But Is No Repeat of 2011**

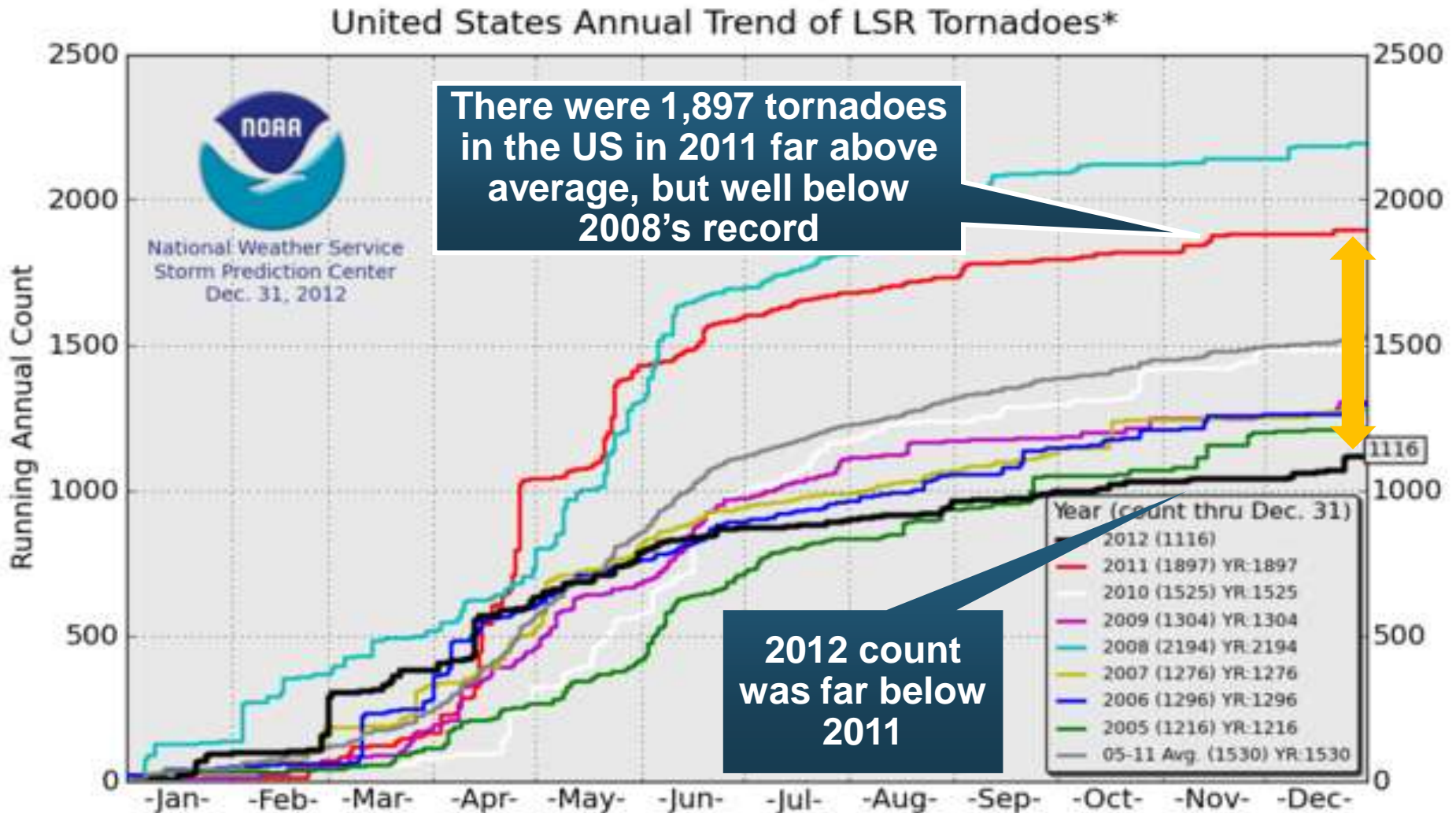
# Number of Tornadoes and Related Deaths, 1990 – 2012\*



**2012 Tornado Losses Got Off to an Ominous Beginning, but Slowed. Yet Despite Fewer Tornadoes, Overall Insured Losses from Thunderstorms Totaled \$14.9B, the 2<sup>nd</sup> Highest on Record.**

\*Through Dec. 31, 2012.

# U.S. Tornado Count, 2005-2012\*

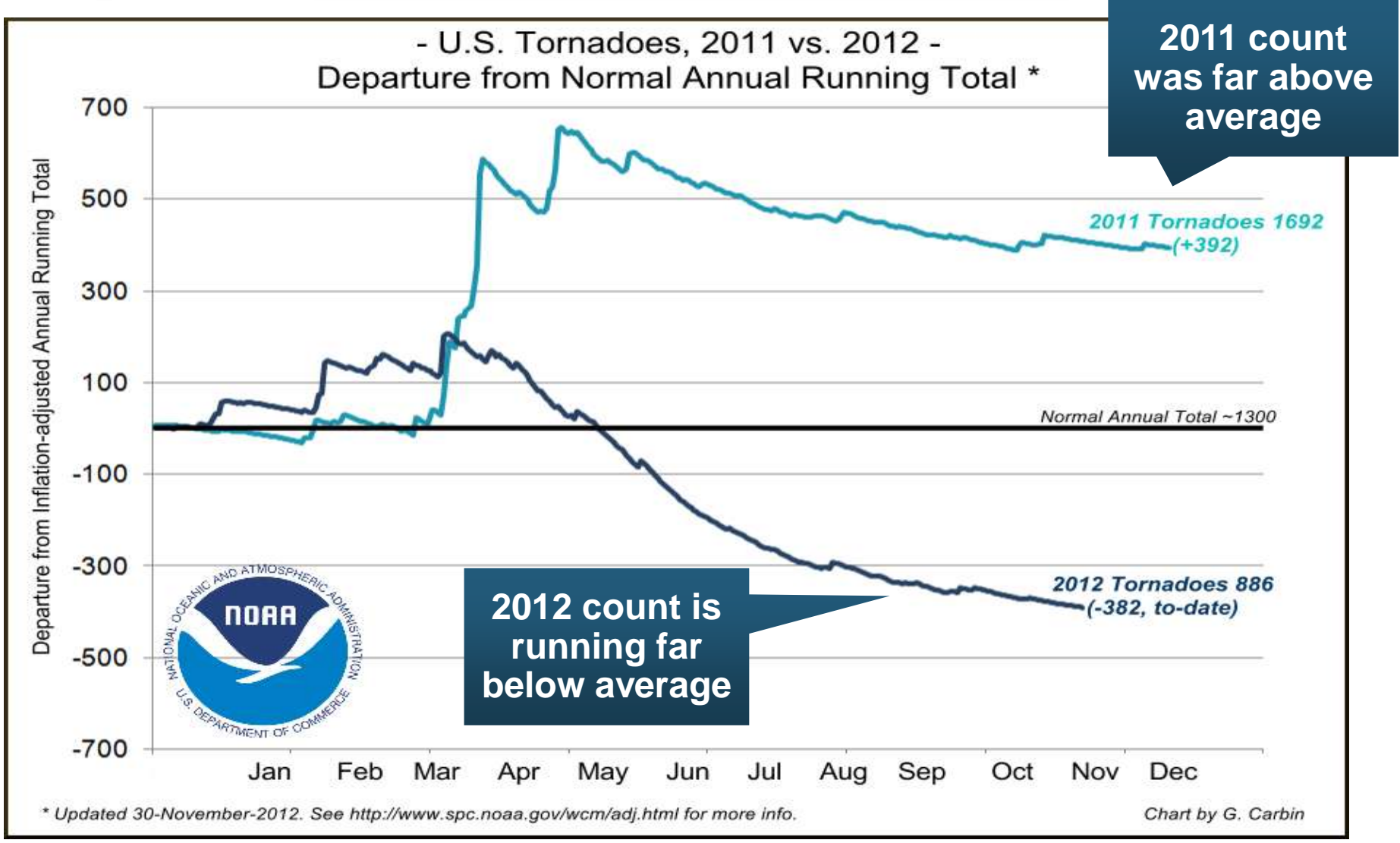


\*Preliminary tornadoes from NWS Local Storm Reports (LSRs)  
Annual average is based on preliminary LSRs, 2005-2011

\*Through Dec. 31, 2012.

Source: <http://www.spc.noaa.gov/wcm/>

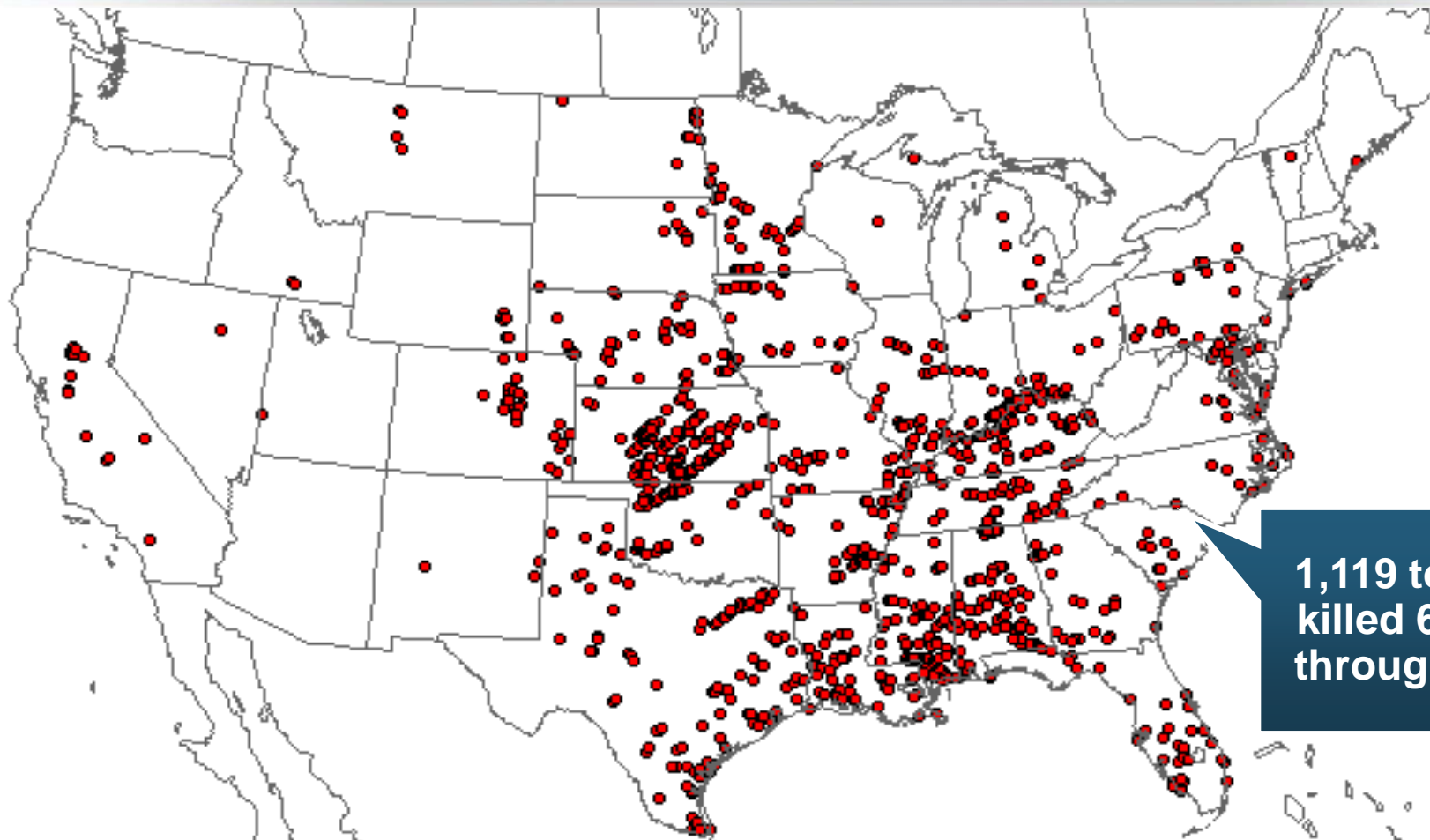
# U.S. Tornado Count, Departure from Inflation-Adjusted Running Total, 2011 vs. 2012\*



\*Through Nov. 30, 2012.

Source: <http://www.spc.noaa.gov/wcm/>

# Location of Tornadoes in the US, 2012\*



**1,119 tornadoes  
killed 68 people  
through Dec. 31**



**PRELIMINARY SEVERE WEATHER  
REPORT DATABASE (ROUGH LOG)**

NOAA/Storm Prediction Center Norman, Oklahoma

**Tornado Reports  
January 01, 2012 - December 31, 2012**

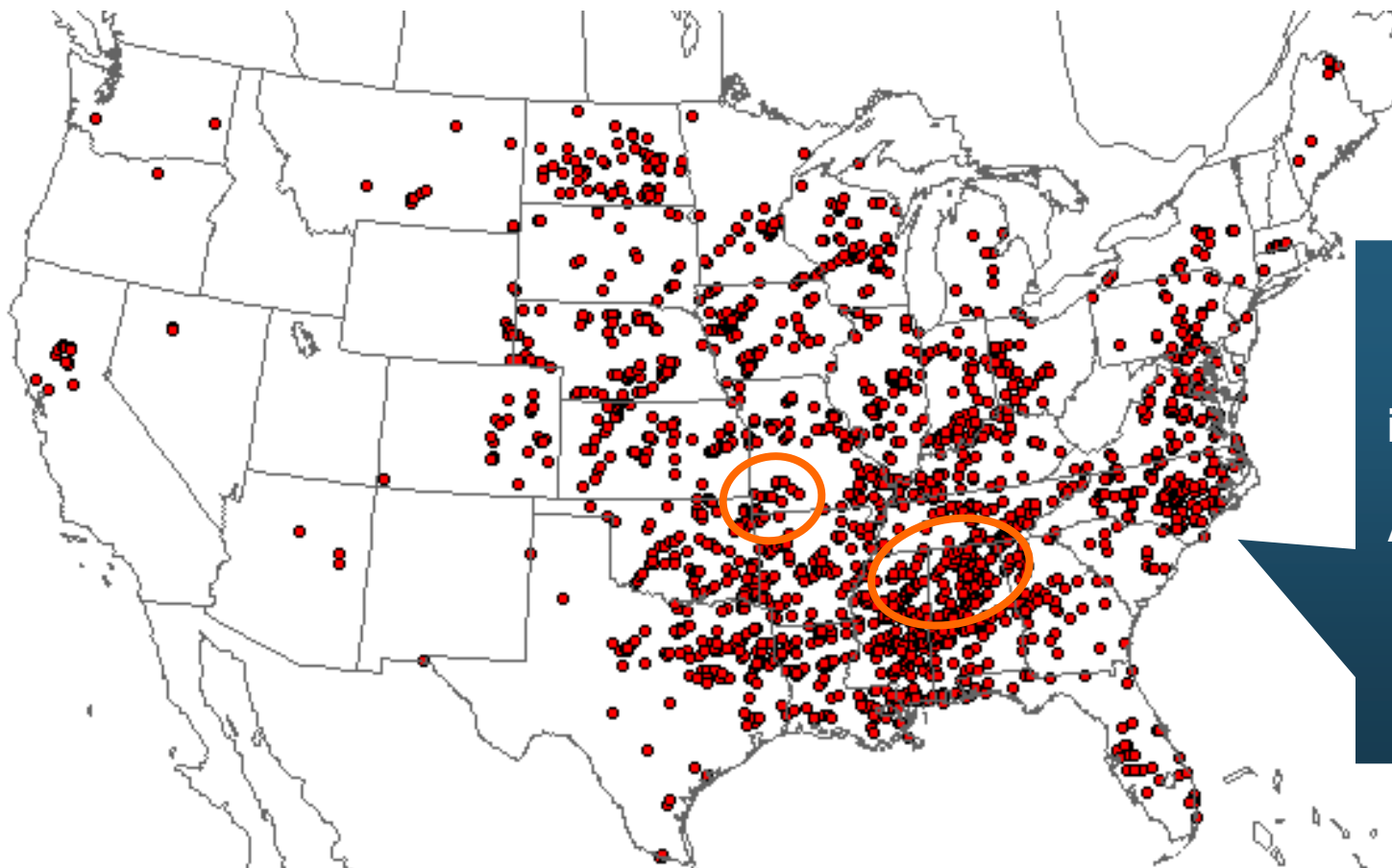
Updated: Sunday January 06, 2013 02:10 CT

\*Through Dec. 31, 2012.

Source: NOAA Storm Prediction Center; [http://www.spc.noaa.gov/climo/online/monthly/2012\\_annual\\_summary.html#](http://www.spc.noaa.gov/climo/online/monthly/2012_annual_summary.html#)



# Location of Tornadoes in the US, 2011



1,894 tornadoes killed 553 people in 2011, including at least 340 on April 26 mostly in the Tuscaloosa area, and 130 in Joplin on May 22



PRELIMINARY SEVERE WEATHER  
REPORT DATABASE (ROUGH LOG)

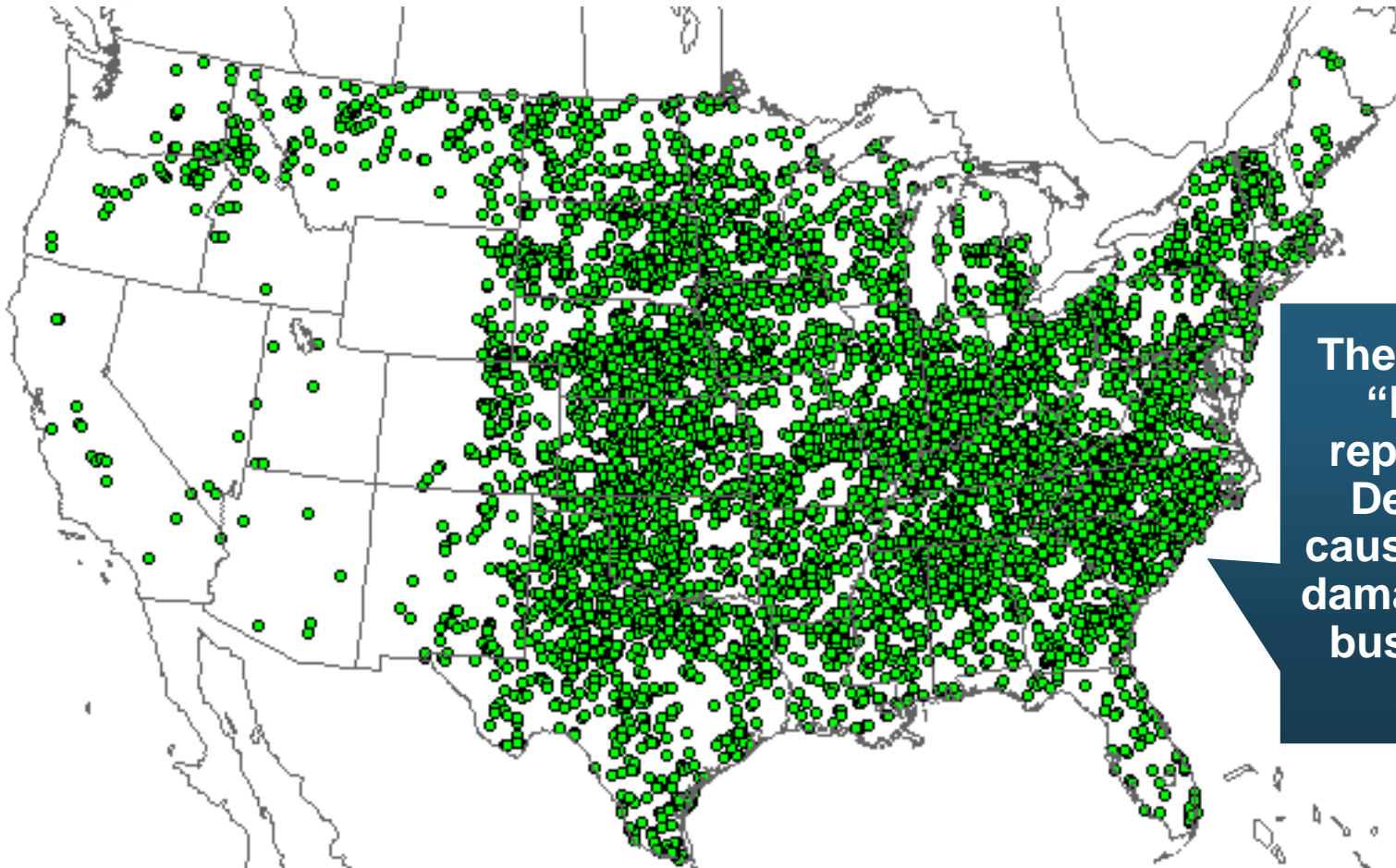
NOAA/Storm Prediction Center Norman, Oklahoma

Tornado Reports  
January 01, 2011 - December 27, 2011

Updated: Tuesday December 27, 2011 16:35 CT



# Location of Large Hail Reports in the US, 2012\*



There were 7,033  
“Large Hail”  
reports through  
Dec. 31, 2012,  
causing extensive  
damage to homes,  
businesses and  
vehicles



PRELIMINARY SEVERE WEATHER  
REPORT DATABASE (ROUGH LOG)

NOAA/Storm Prediction Center Norman, Oklahoma

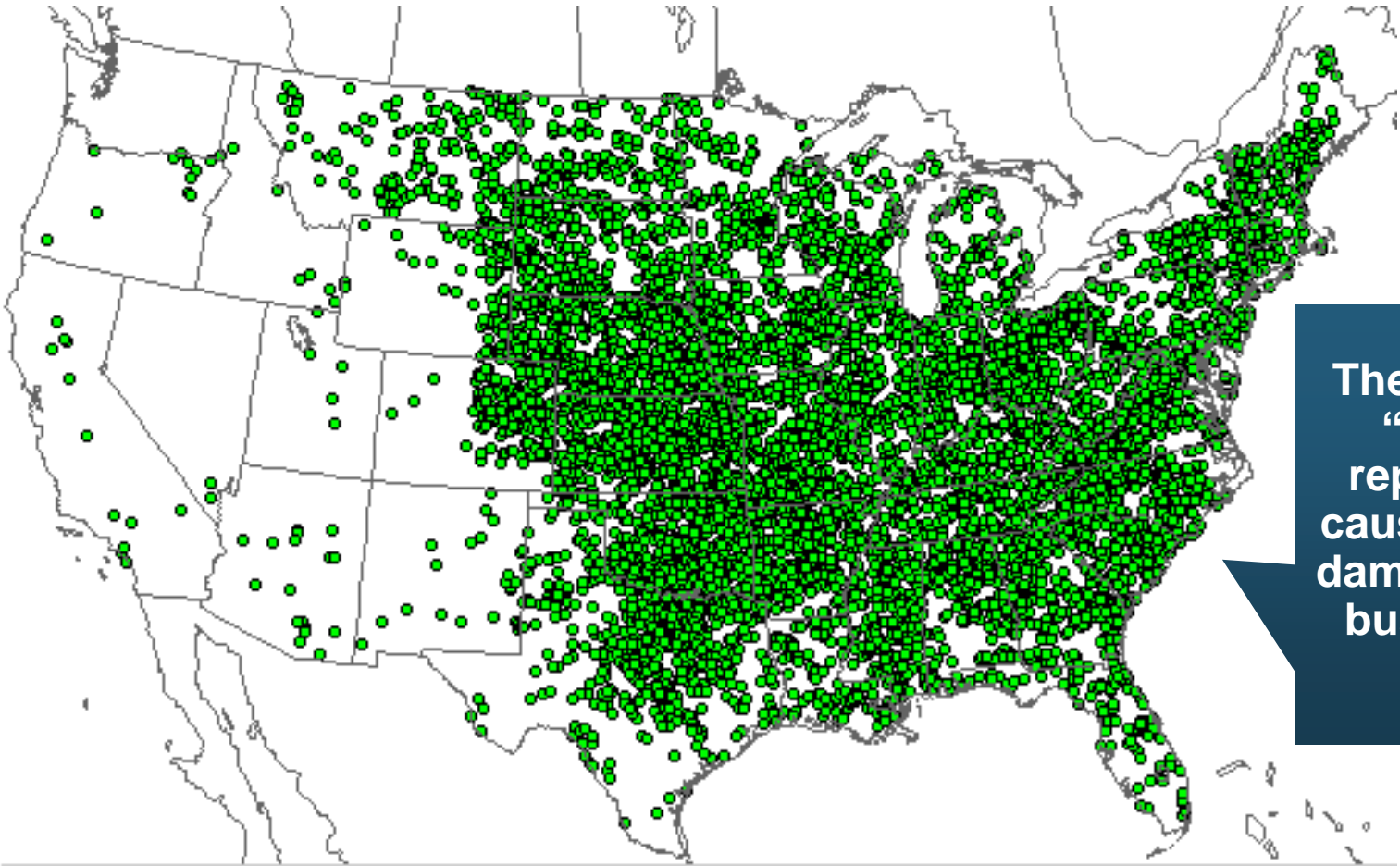
Hail Reports  
January 01, 2012 - December 31, 2012

Updated: Sunday January 06, 2013 02:10 CT

\*Through Dec. 31, 2012.

Source: NOAA Storm Prediction Center; [http://www.spc.noaa.gov/climo/online/monthly/2012\\_annual\\_summary.html#](http://www.spc.noaa.gov/climo/online/monthly/2012_annual_summary.html#)

# Location of Large Hail Reports in the US, 2011



There were 9,417 “Large Hail” reports in 2011, causing extensive damage to homes, businesses and vehicles



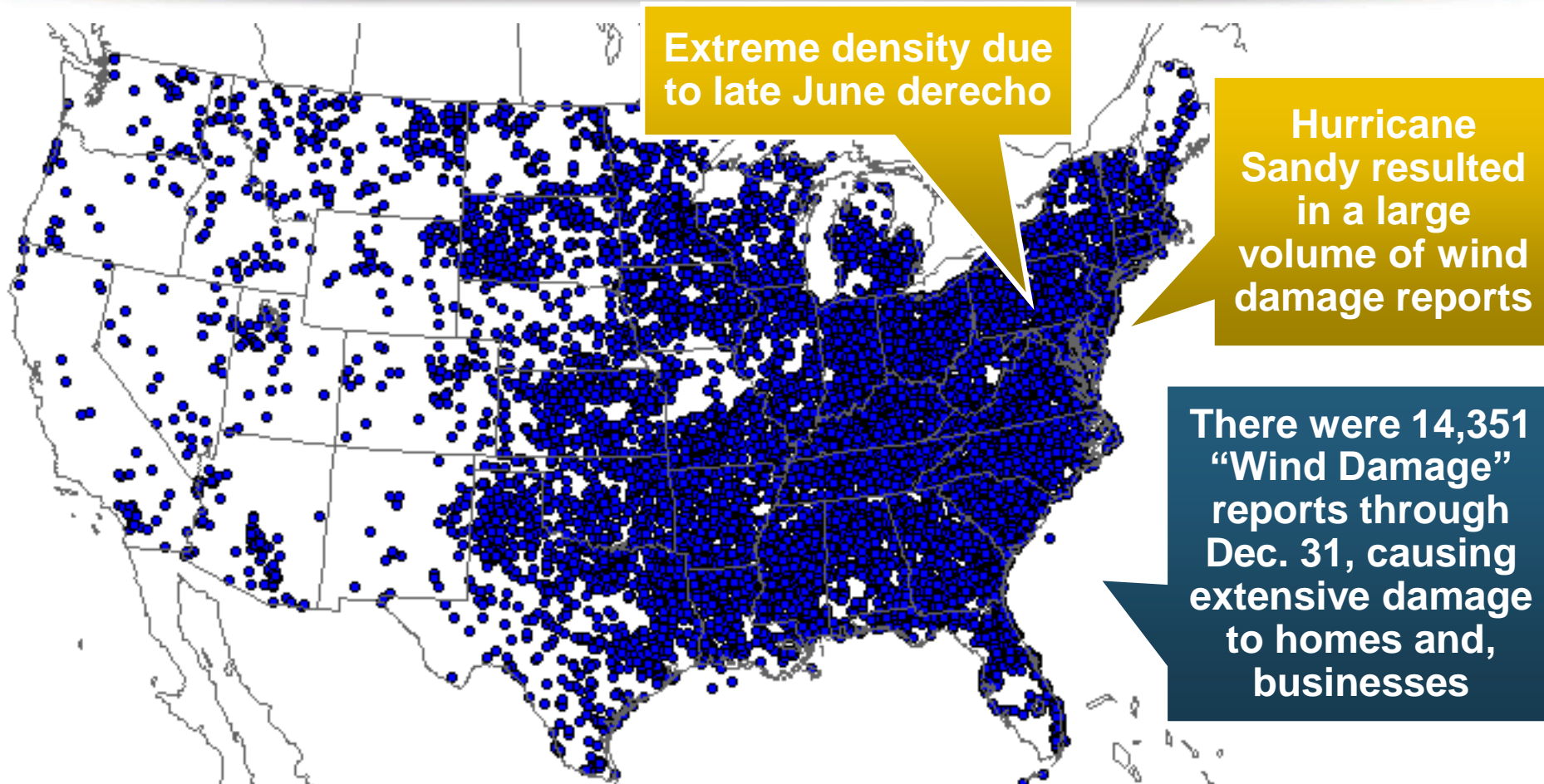
PRELIMINARY SEVERE WEATHER  
REPORT DATABASE (ROUGH LOG)

NOAA/Storm Prediction Center Norman, Oklahoma

Hail Reports  
January 01, 2011 - December 27, 2011

Updated: Tuesday December 27, 2011 16:35 CT

# Location of Wind Damage Reports in the US, 2012\*



PRELIMINARY SEVERE WEATHER  
REPORT DATABASE (ROUGH LOG)

NOAA/Storm Prediction Center Norman, Oklahoma

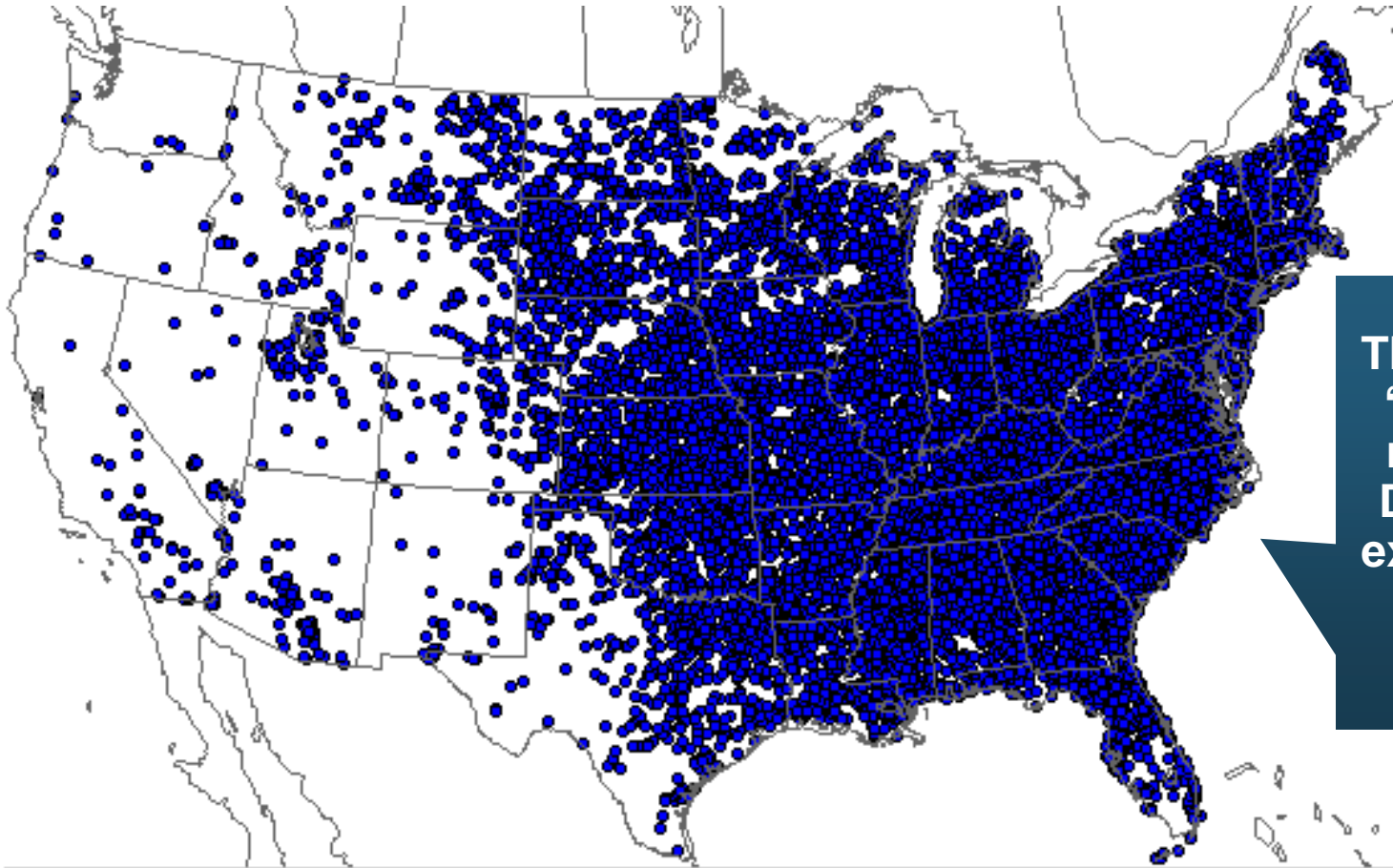
Wind Reports  
January 01, 2012 - December 31, 2012

Updated: Sunday January 06, 2013 02:10 CT

\*Through Dec. 31, 2012.

Source: NOAA Storm Prediction Center; [http://www.spc.noaa.gov/climo/online/monthly/2012\\_annual\\_summary.html#](http://www.spc.noaa.gov/climo/online/monthly/2012_annual_summary.html#)

# Location of Wind Damage Reports in the US, 2011



There were 18,685  
“Wind Damage”  
reports through  
Dec. 27, causing  
extensive damage  
to homes and,  
businesses



PRELIMINARY SEVERE WEATHER  
REPORT DATABASE (ROUGH LOG)

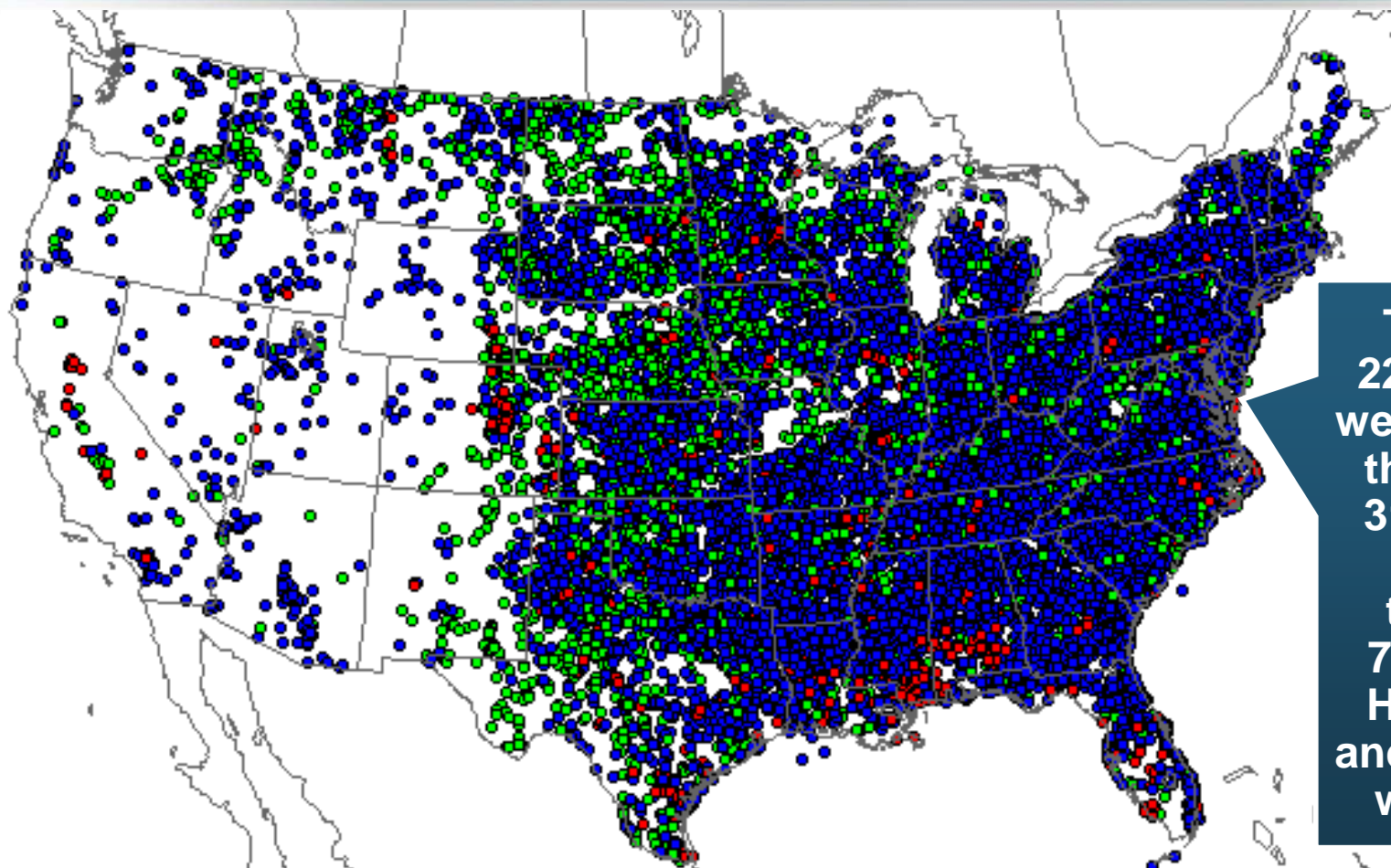
NOAA/Storm Prediction Center Norman, Oklahoma

Wind Reports  
January 01, 2011 - December 27, 2011

Updated: Tuesday December 27, 2011 16:35 CT



# Severe Weather Reports, 2012\*



There were  
22,503 severe  
weather reports  
through Dec.  
31; including  
1,119  
tornadoes;  
7,033 “Large  
Hail” reports  
and 14,351 high  
wind events



PRELIMINARY SEVERE WEATHER  
REPORT DATABASE (ROUGH LOG)

NOAA/Storm Prediction Center Norman, Oklahoma

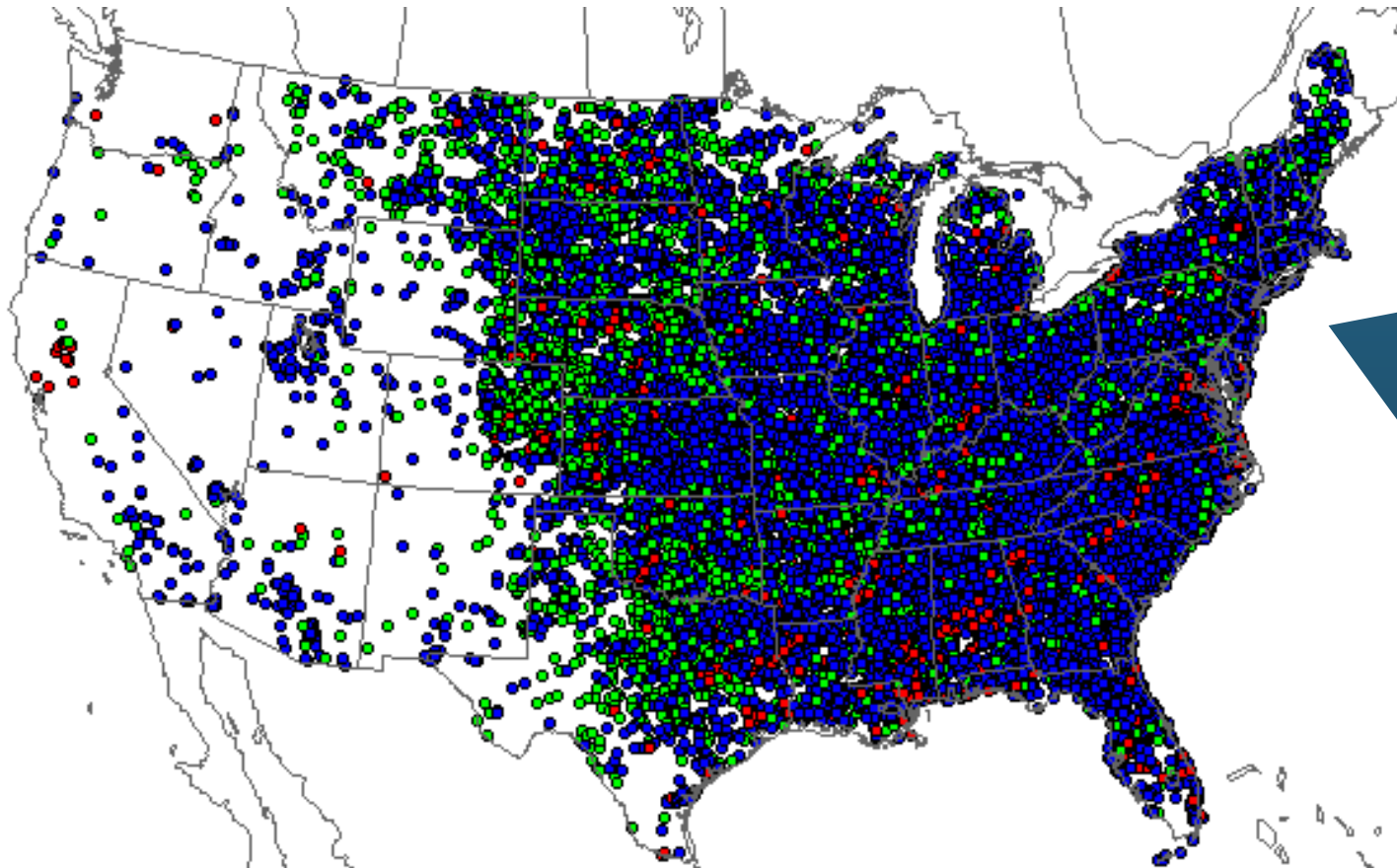
Severe Weather Reports  
January 01, 2012 - December 31, 2012

Updated: Sunday January 06, 2013 02:10 CT

\*Through Dec. 31, 2012.

Source: NOAA Storm Prediction Center; [http://www.spc.noaa.gov/climo/online/monthly/2012\\_annual\\_summary.html#](http://www.spc.noaa.gov/climo/online/monthly/2012_annual_summary.html#)

# Severe Weather Reports, 2011



There were 29,996 severe weather reports in 2011; including 1,894 tornadoes; 9,417 “Large Hail” reports and 18,685 high wind events



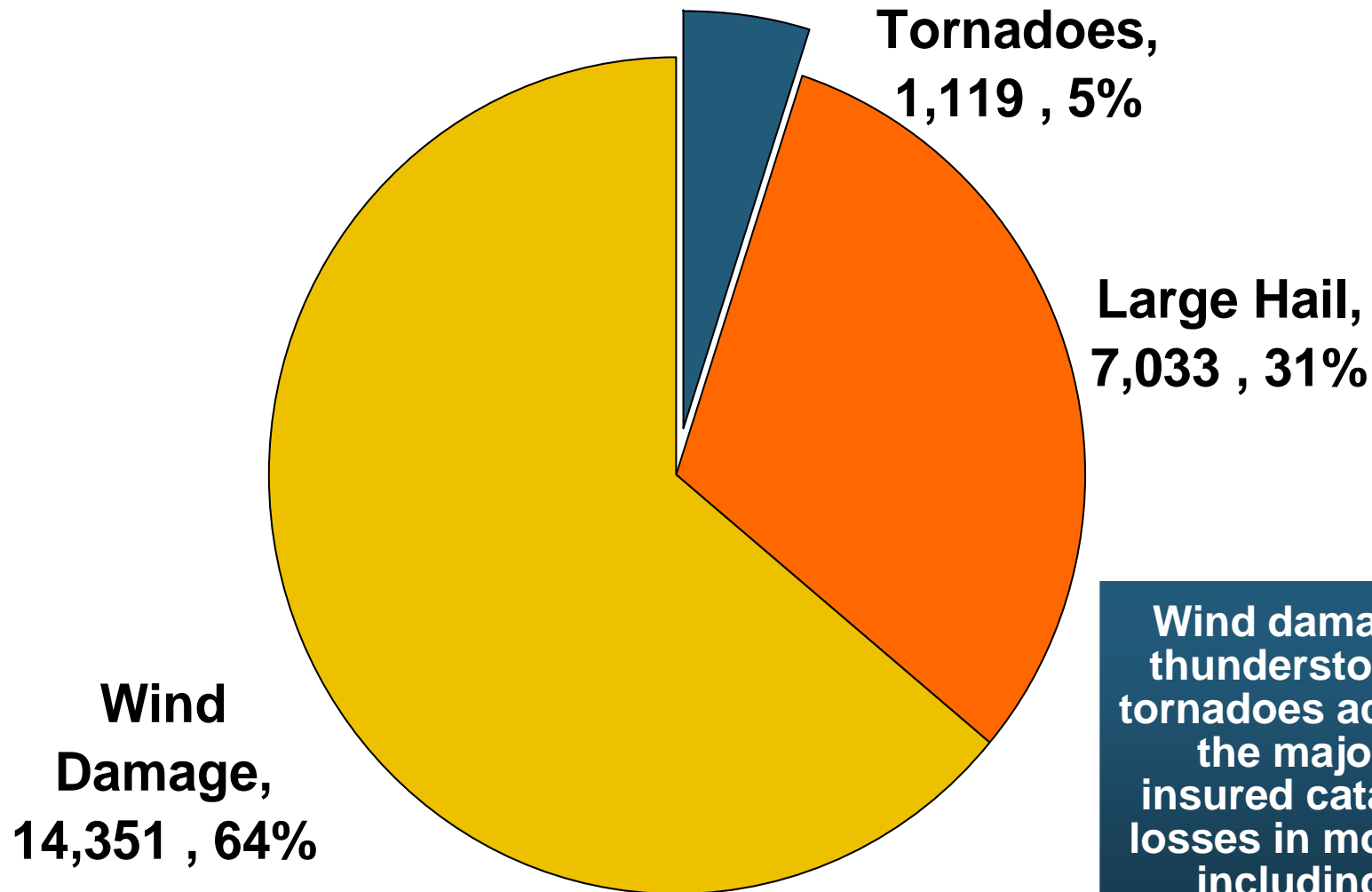
PRELIMINARY SEVERE WEATHER  
REPORT DATABASE (ROUGH LOG)

NOAA/Storm Prediction Center Norman, Oklahoma

Severe Weather Reports  
January 01, 2011 - December 27, 2011

Updated: Tuesday December 27, 2011 16:35 CT

# Number of Severe Weather Reports in US, by Type, 2012



Wind damage from thunderstorms and tornadoes account for the majority of insured catastrophe losses in most years, including 2012

# **The BIG Question: Where Is the Market Heading?**

**Catastrophes and Other Factors Are  
Pressuring Insurance Markets**

***New Factor: Record Low Interest  
Rates Are Contributing to  
Underwriting and Pricing Pressures***



# Historical Criteria for a “Market Turn”: Low Interest Rates Add New Pressure

Criteria	Status	Comments
<b>Sustained Period of Large Underwriting Losses</b>	<i>Large CAT Losses in 2011/12 Pushed Up Combined</i>	<ul style="list-style-type: none"> <li>•CAT Losses contributing to higher underwriting losses</li> <li>•Apart from CAT losses, overall p/c underwriting losses remain modest</li> <li>•Combined ratios (ex-CATs) still in low 100s (vs. 110+ at onset of last hard market); CR= 101.1 in H1:2012 (ex-M&amp;FG)</li> <li>•Prior-year reserve releases continue to reduce u/w losses, boost ROEs, though more modestly</li> </ul>
<b>Material Decline in Surplus/ Capacity</b>	<i>Small Decline Due to 2011 Cats; Could drop in 2012</i>	<ul style="list-style-type: none"> <li>•Fell 1.6% in 2011 due to CATs</li> <li>•Surplus reached record as of 9/30/12 record \$583.5B</li> <li>•Likely drop as of 12/31/12 due to Sandy impact</li> <li>•Modest growth in demand for insurance should begin to absorb some capacity</li> </ul>
<b>Tight Reinsurance Market</b>	<i>Somewhat in Place</i>	<ul style="list-style-type: none"> <li>•Ample capacity</li> <li>•Market is generally flat except up for cat-impacted accounts</li> <li>•Lower prices in Europe</li> </ul>
<b>Renewed Underwriting &amp; Pricing Discipline</b>	<i>Firming Broad, Sustained, esp. in Property, WC</i>	<ul style="list-style-type: none"> <li>•Commercial lines pricing is consistently and uniformly across all major lines, esp. Property &amp; WC;</li> <li>•Markets remain competitive in most segments</li> </ul>

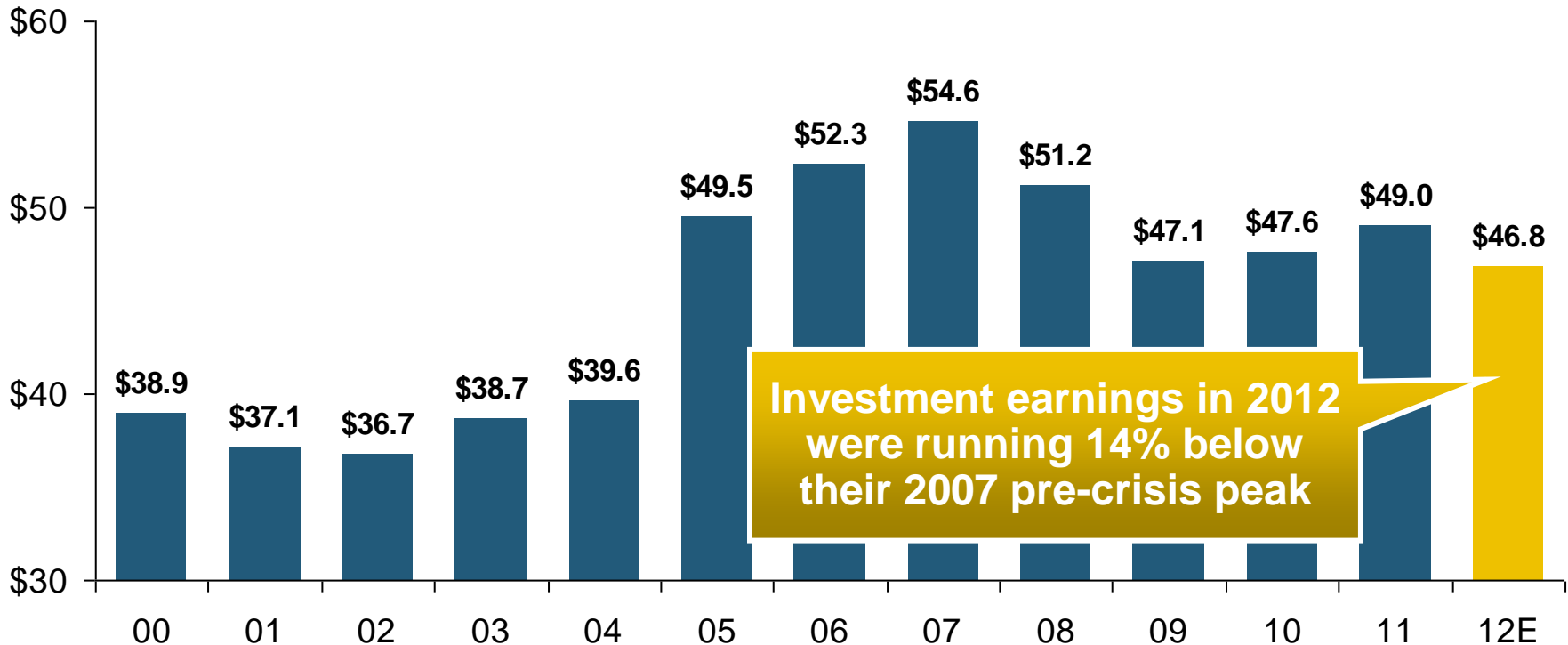
# **INVESTMENTS: THE NEW REALITY**

**Investment Performance is a Key  
Driver of Profitability**

***Depressed Yields Will Necessarily  
Influence Underwriting & Pricing***

# Property/Casualty Insurance Industry Investment Income: 2000–2012E<sup>1</sup>

(\$ Billions)

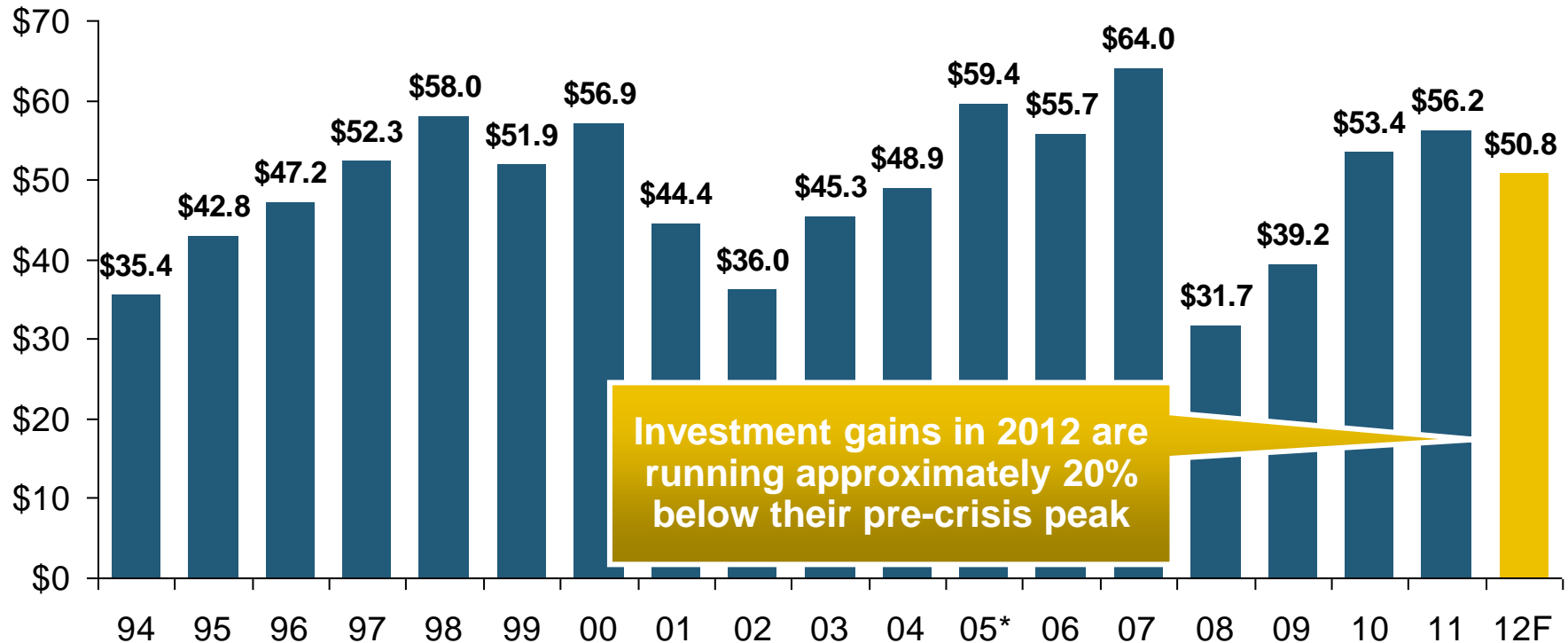


**Investment Income Fell in 2012 Due to Persistently Low Interest Rates, Putting Additional Pressure on (Re) Insurance Pricing**

<sup>1</sup> Investment gains consist primarily of interest and stock dividends.  
\*2012F is based on annualized 9M:2012 actual figure of \$35.131B.  
Sources: ISO; Insurance Information Institute.

# Property/Casualty Insurance Industry Investment Gain: 1994–2012F<sup>1</sup>

(\$ Billions)



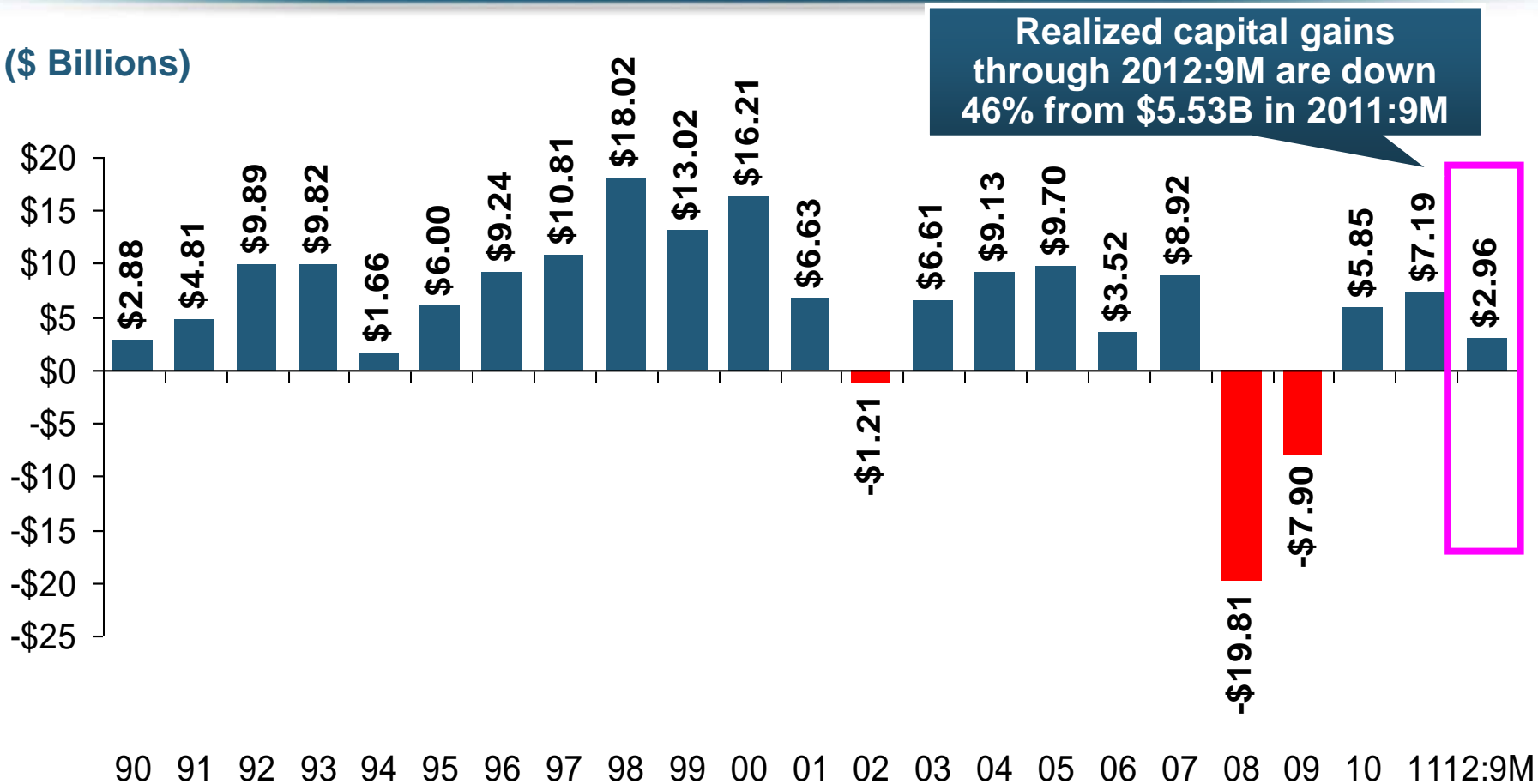
**Investment Gains Are Slipping in 2012 as Low Interest Rates Reduce Investment Income and Lower Realized Investment Gains; The Financial Crisis Caused Investment Gains to Fall by 50% in 2008**

<sup>1</sup> Investment gains consist primarily of interest, stock dividends and realized capital gains and losses.

\* 2005 figure includes special one-time dividend of \$3.2B; 2012F figure is III estimate based on annualized actual 9M:2012 result of \$38.089B.  
Sources: ISO; Insurance Information Institute.

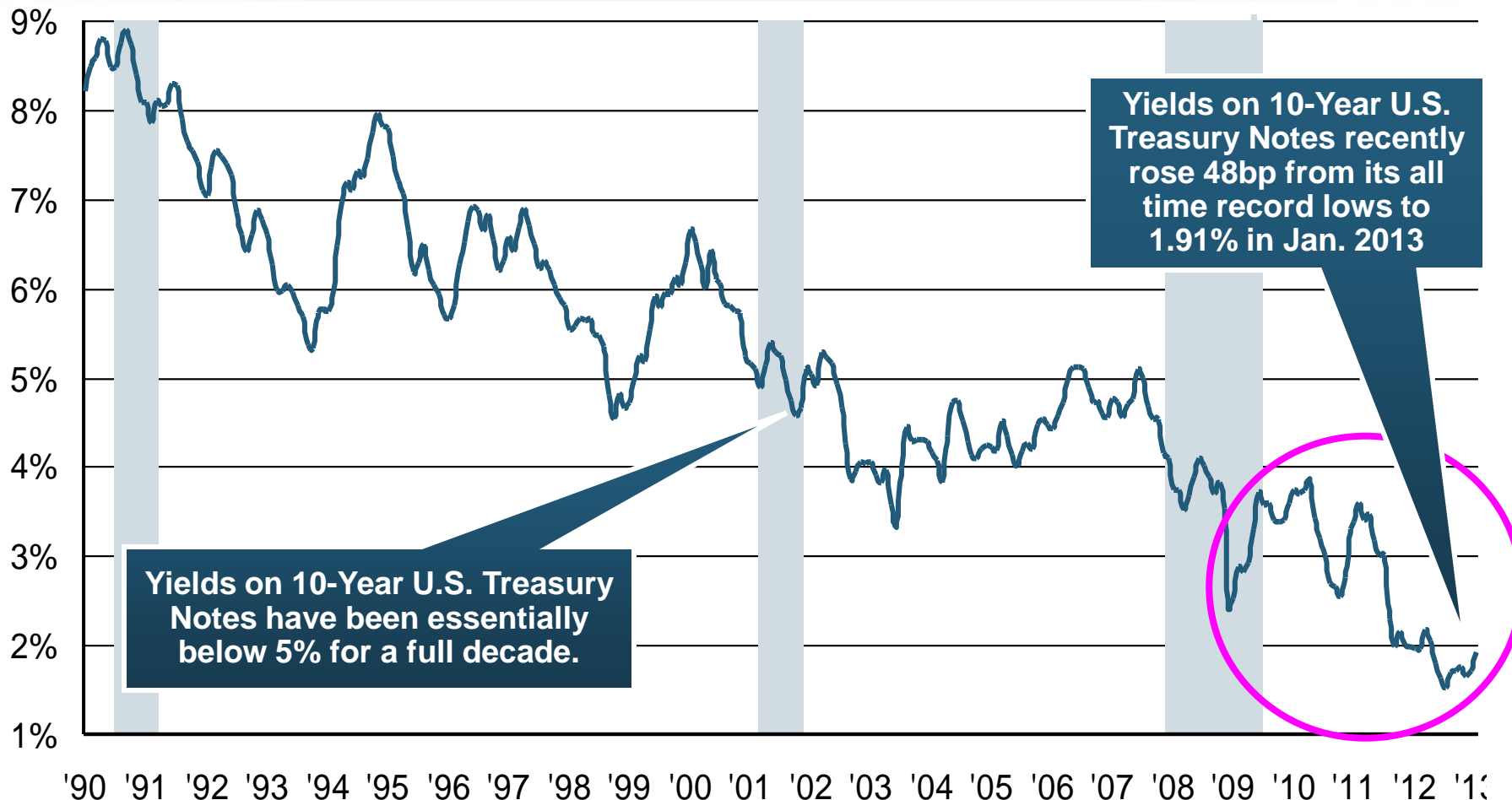
# P/C Insurer Net Realized Capital Gains/Losses, 1990-2012:Q3

(\$ Billions)



**Insurers Posted Net Realized Capital Gains in 2010, 2011 and 2012 Following Two Years of Realized Losses During the Financial Crisis. Realized Capital Losses Were the Primary Cause of 2008/2009's Large Drop in Profits and ROE**

# U.S. 10-Year Treasury Note Yields: A Long Downward Trend, 1990–2013\*



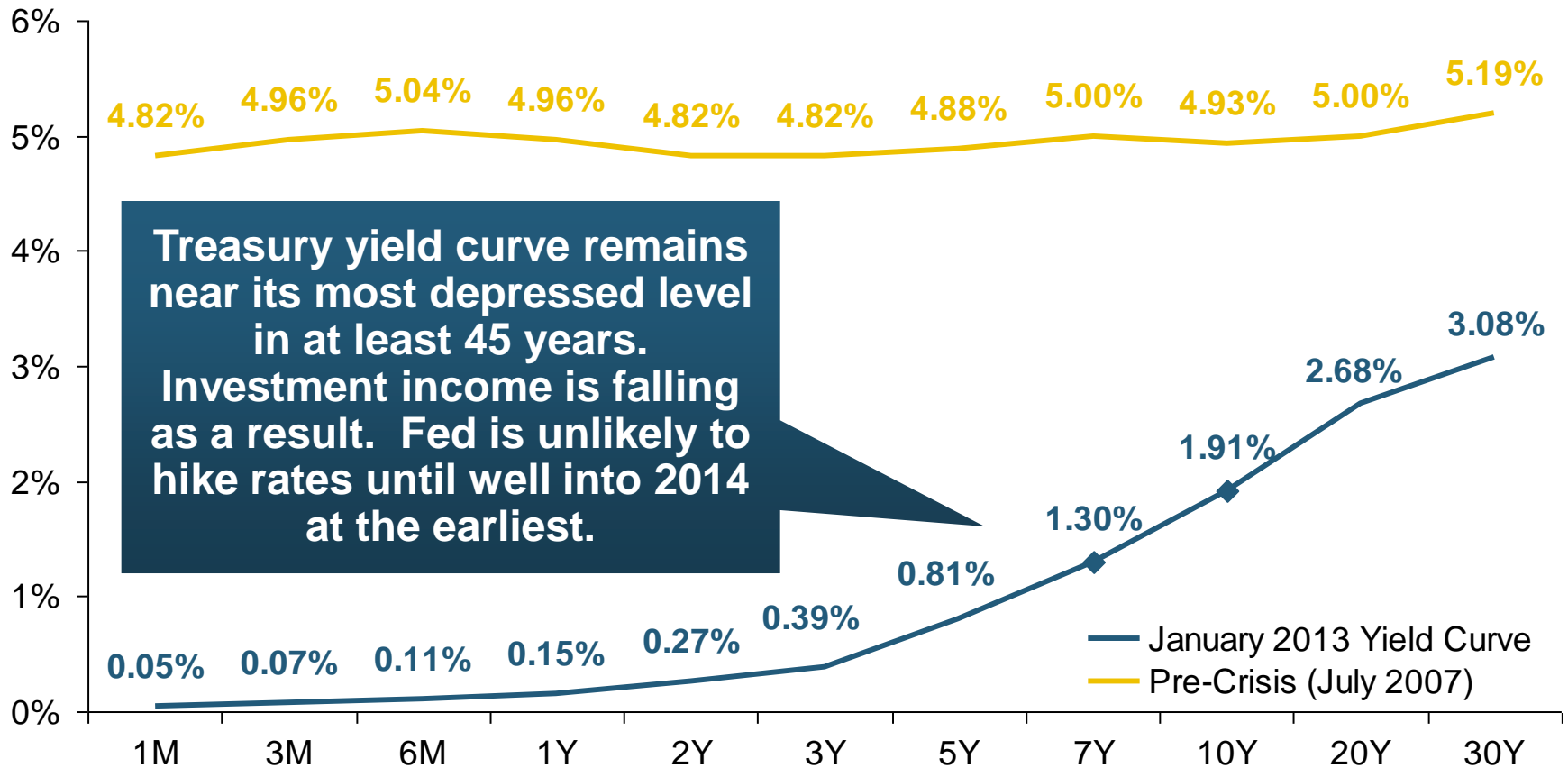
**Since roughly 80% of P/C bond/cash investments are in 10-year or shorter durations, most P/C insurer portfolios will have low-yielding bonds for years to come.**

\*Monthly, through Jan. 2013.

Note: Recessions indicated by gray shaded columns.

Sources: Federal Reserve Bank at <http://www.federalreserve.gov/releases/h15/data.htm>.  
National Bureau of Economic Research (recession dates); Insurance Information Institutes.

# Treasury Yield Curves: Pre-Crisis (July 2007) vs. Jan. 2013

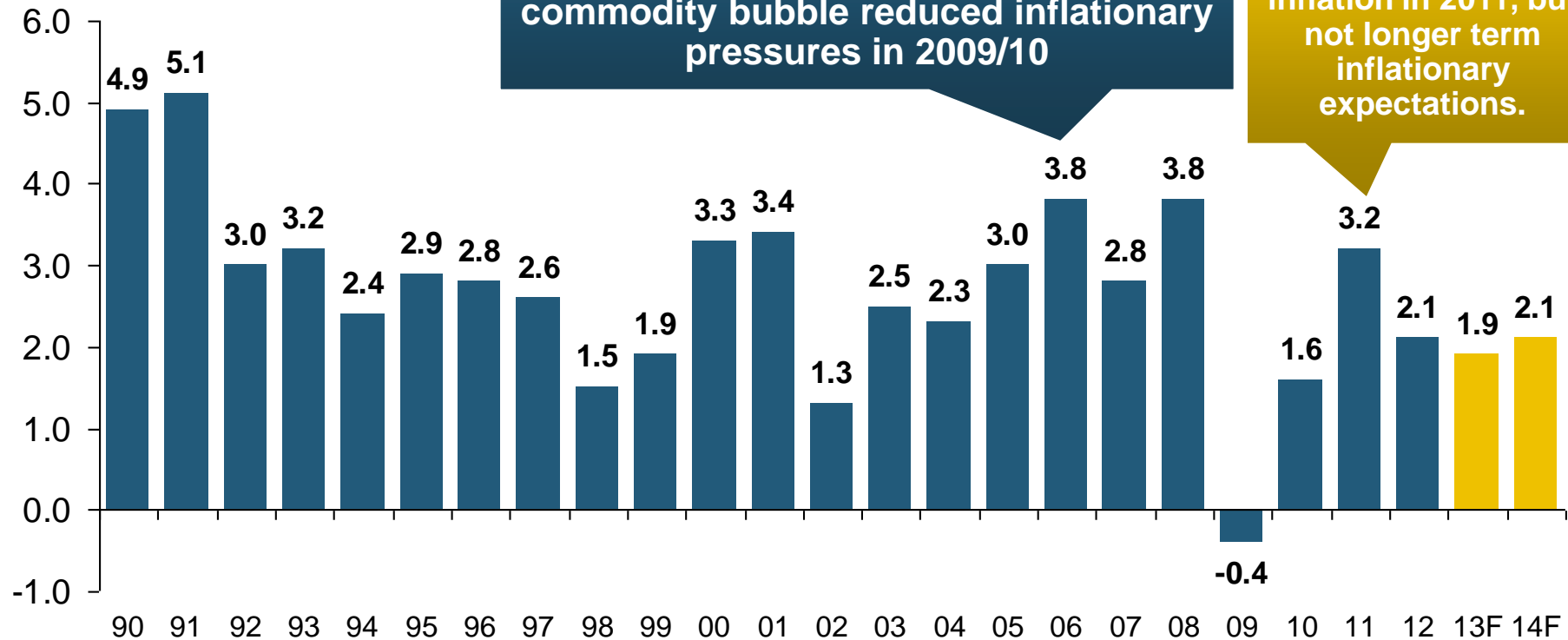


Treasury yield curve remains near its most depressed level in at least 45 years. Investment income is falling as a result. Fed is unlikely to hike rates until well into 2014 at the earliest.

The Fed Is Actively Signaling that it Is Determined to Keep Rates Low Until Unemployment Drops Below 6.5% or Until Inflation Expectations Exceed 2.5%; Low Rates Add to Pricing Pressure for Insurers.

# Annual Inflation Rates, (CPI-U, %), 1990–2014F

Annual Inflation Rates (%)



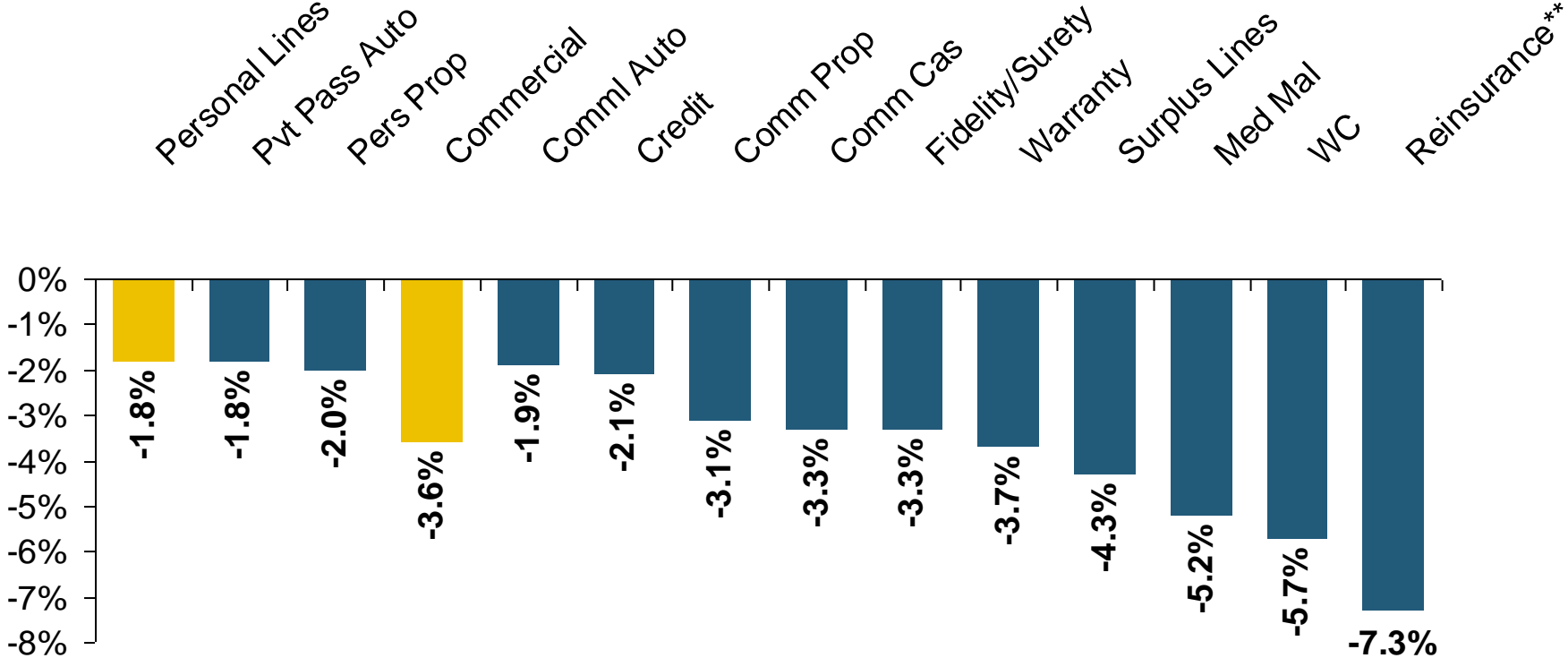
Inflation peaked at 5.6% in August 2008 on high energy and commodity crisis. The recession and the collapse of the commodity bubble reduced inflationary pressures in 2009/10

Higher energy, commodity and food prices pushed up inflation in 2011, but not longer term inflationary expectations.

The slack in the U.S. economy suggests that inflationary pressures should remain subdued for an extended period of times. Energy, health care and commodity prices, plus U.S. debt burden, remain longer-run concerns



# Reduction in Combined Ratio Necessary to Offset 1% Decline in Investment Yield to Maintain Constant ROE, by Line\*



**Lower Investment Earnings Place a Greater Burden on Underwriting and Pricing Discipline**

\*Based on 2008 Invested Assets and Earned Premiums

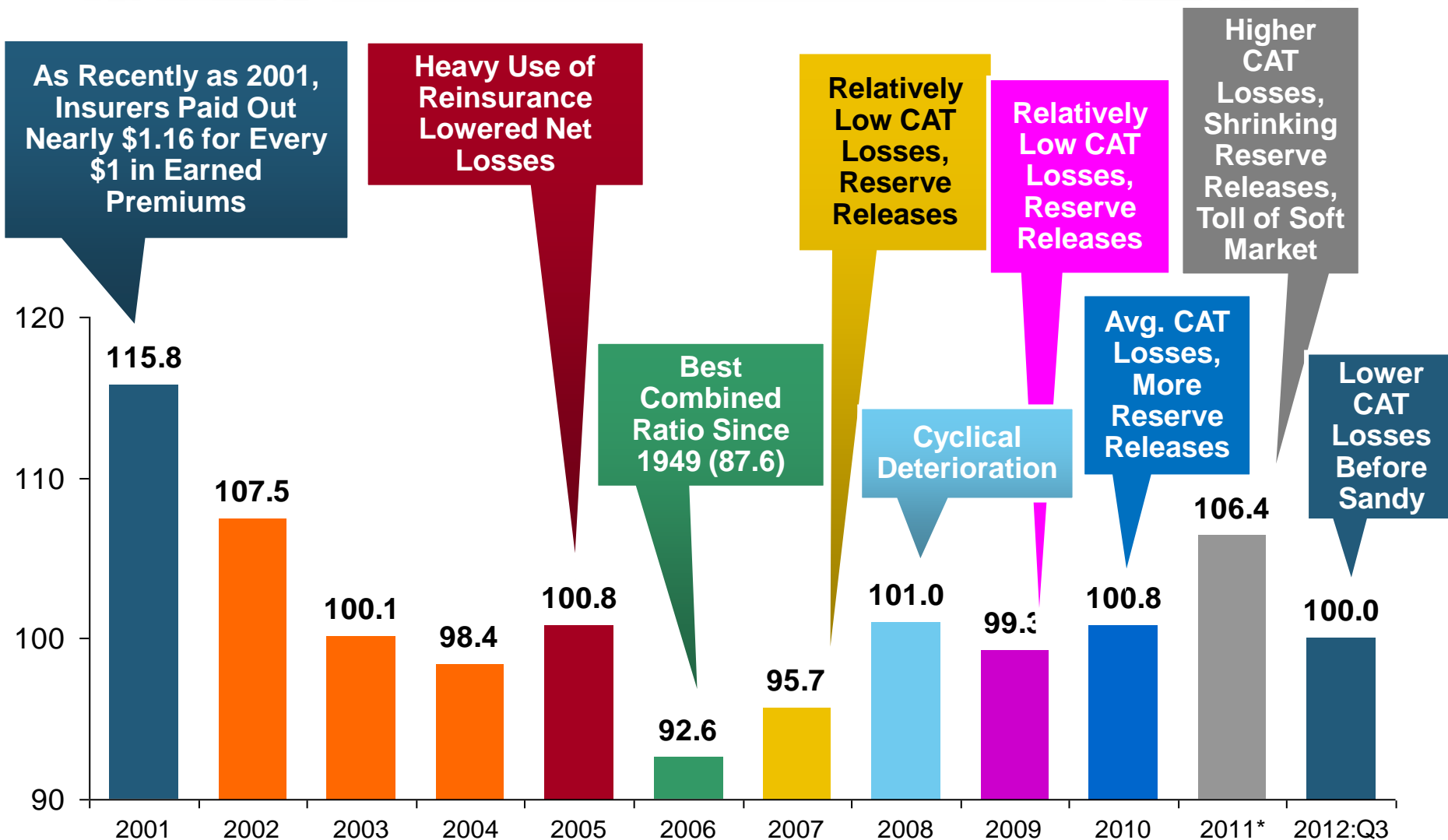
\*\*US domestic reinsurance only

Source: A.M. Best; Insurance Information Institute.

# 1. UNDERWRITING

**Underwriting Losses in 2011  
and 2012 Are Elevated by High  
Catastrophe Losses**

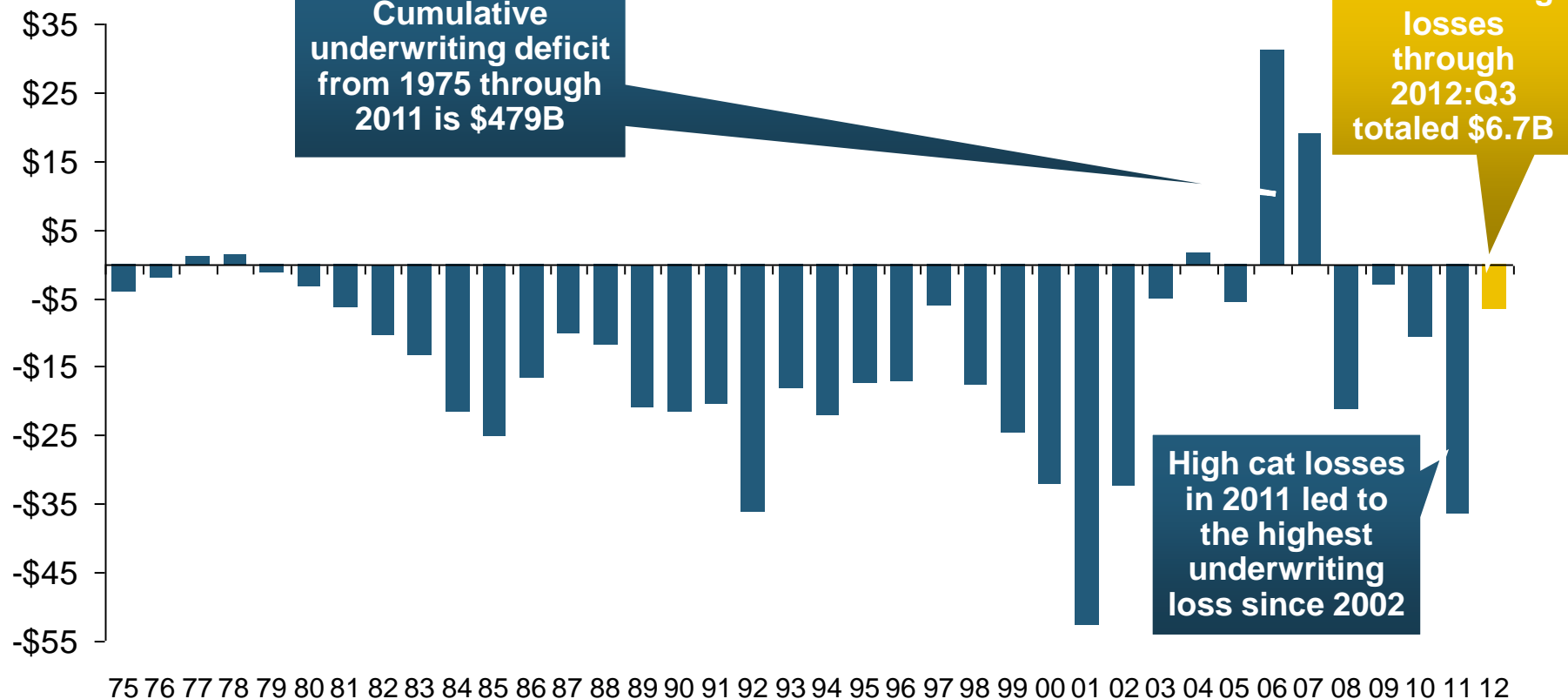
# P/C Insurance Industry Combined Ratio, 2001–2012:Q3\*



\* Excludes Mortgage & Financial Guaranty insurers 2008--2012. Including M&FG, 2008=105.1, 2009=100.7, 2010=102.4, 2011=108.2; 2012:Q3=100.0.  
Sources: A.M. Best, ISO.

# Underwriting Gain (Loss) 1975–2012:Q3\*

(\$ Billions)



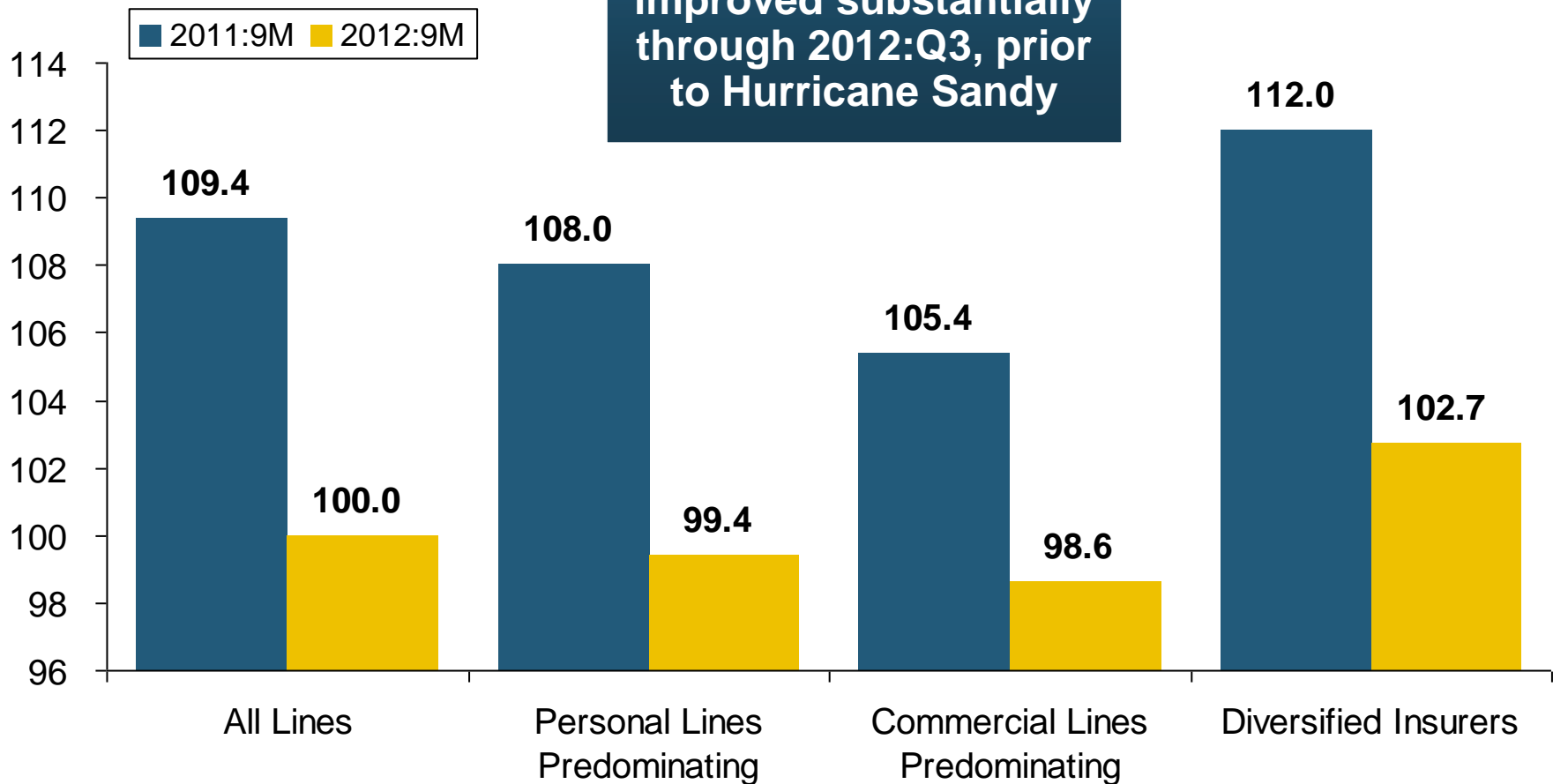
**Large Underwriting Losses Are *NOT* Sustainable  
in Current Investment Environment**

\* Includes mortgage and financial guaranty insurers in all years.  
Sources: A.M. Best, ISO; Insurance Information Institute.

# Combined Ratios by Predominant Business Segment, 2012:9 Mos. vs. 2011:9 Mos.\*

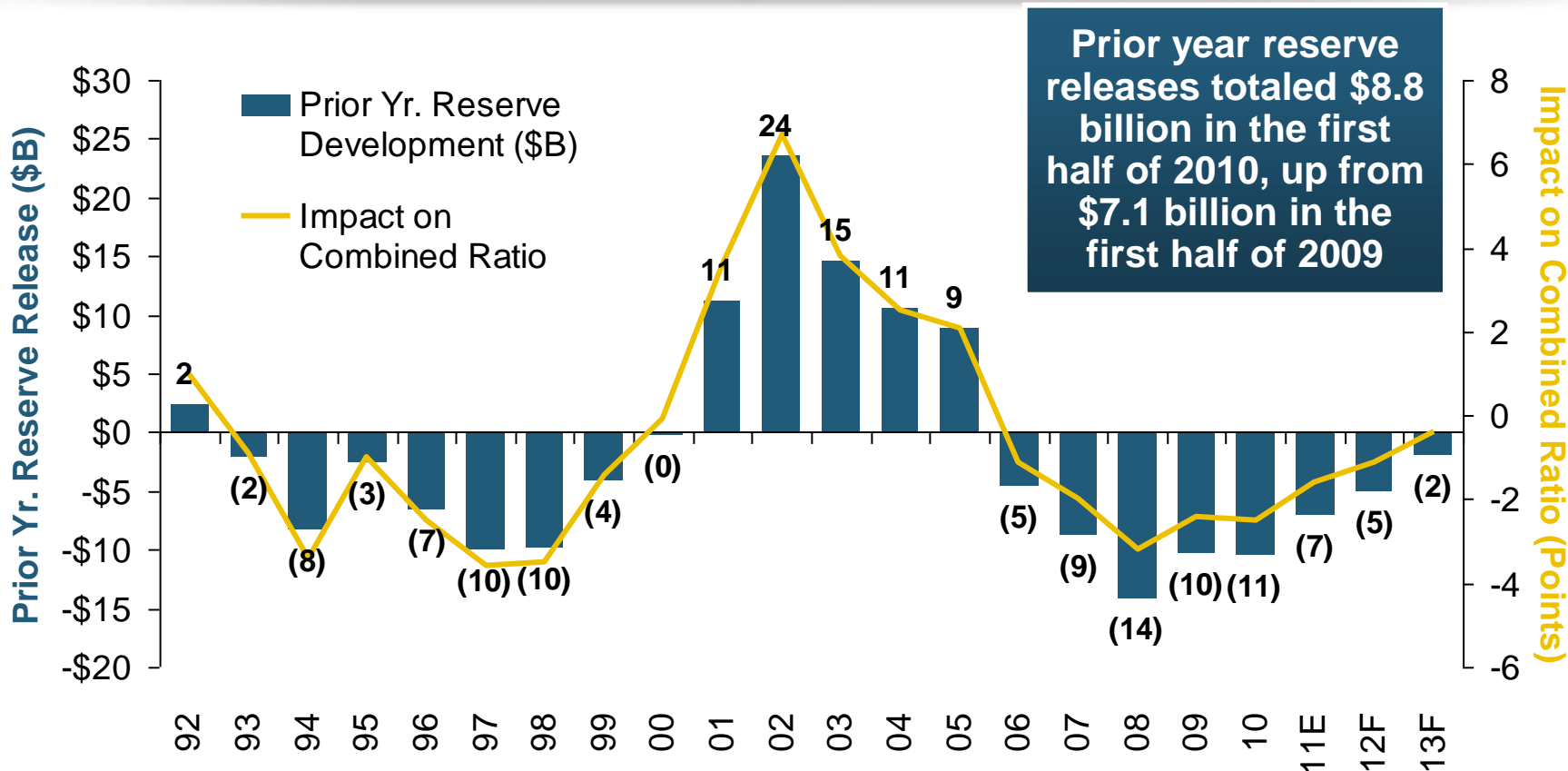
(Percent)

The combined ratios for both personal and commercial lines improved substantially through 2012:Q3, prior to Hurricane Sandy



\*Excludes mortgage and financial guaranty insurers.

# P/C Reserve Development, 1992–2013F



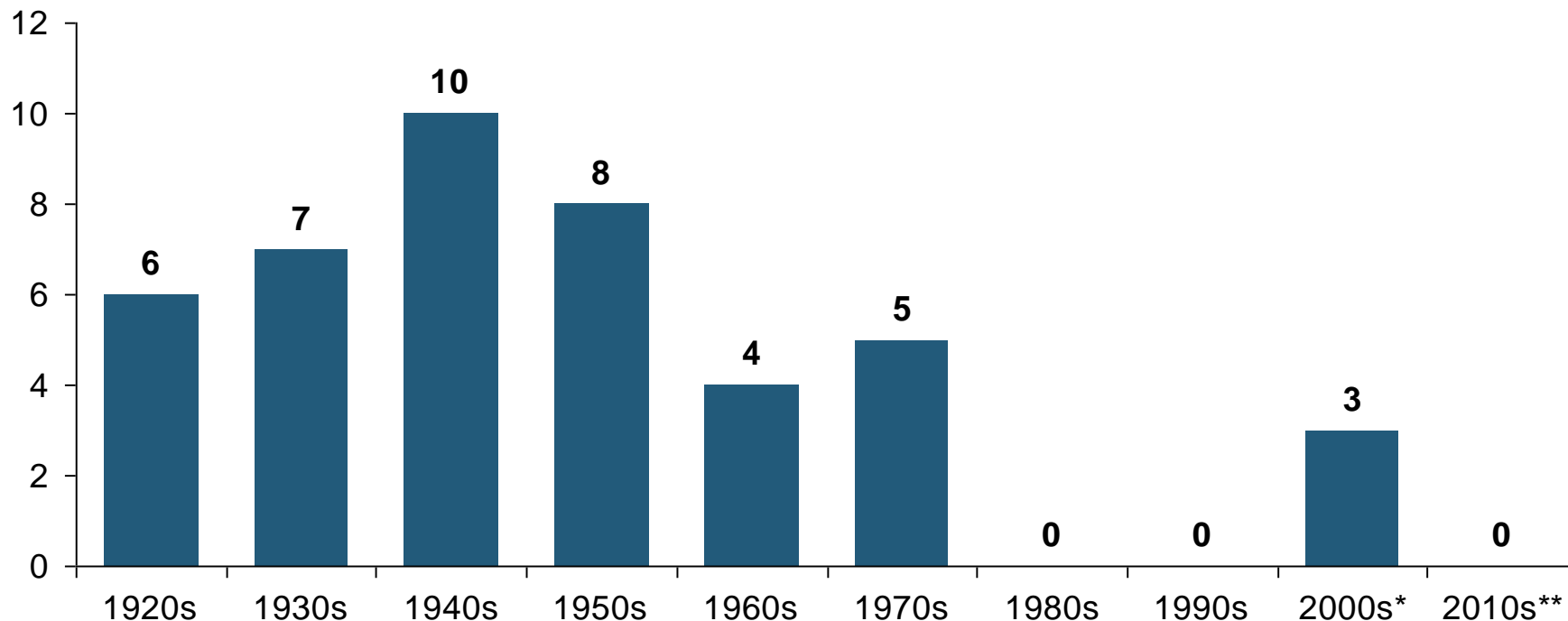
**Reserve Releases Remained Strong in 2010 But Tapered Off in 2011. Releases Are Expected to Further Diminish in 2012 and 2103**

Note: 2005 reserve development excludes a \$6 billion loss portfolio transfer between American Re and Munich Re. Including this transaction, total prior year adverse development in 2005 was \$7 billion. The data from 2000 and subsequent years excludes development from financial guaranty and mortgage insurance.

Sources: Barclays Capital; A.M. Best.

# Number of Years with Underwriting Profits by Decade, 1920s–2010s

## Number of Years with Underwriting Profits



**Underwriting Profits Were Common Before the 1980s (40 of the 60 Years Before 1980 Had Combined Ratios Below 100) – But Then They Vanished. Not a Single Underwriting Profit Was Recorded in the 25 Years from 1979 Through 2003**

\* 2009 combined ratio excl. mort. and finl. guaranty insurers was 99.3, which would bring the 2000s total to 4 years with an u/w profit.

\*\*Data for the 2010s includes 2010 and 2011.

Note: Data for 1920–1934 based on stock companies only.

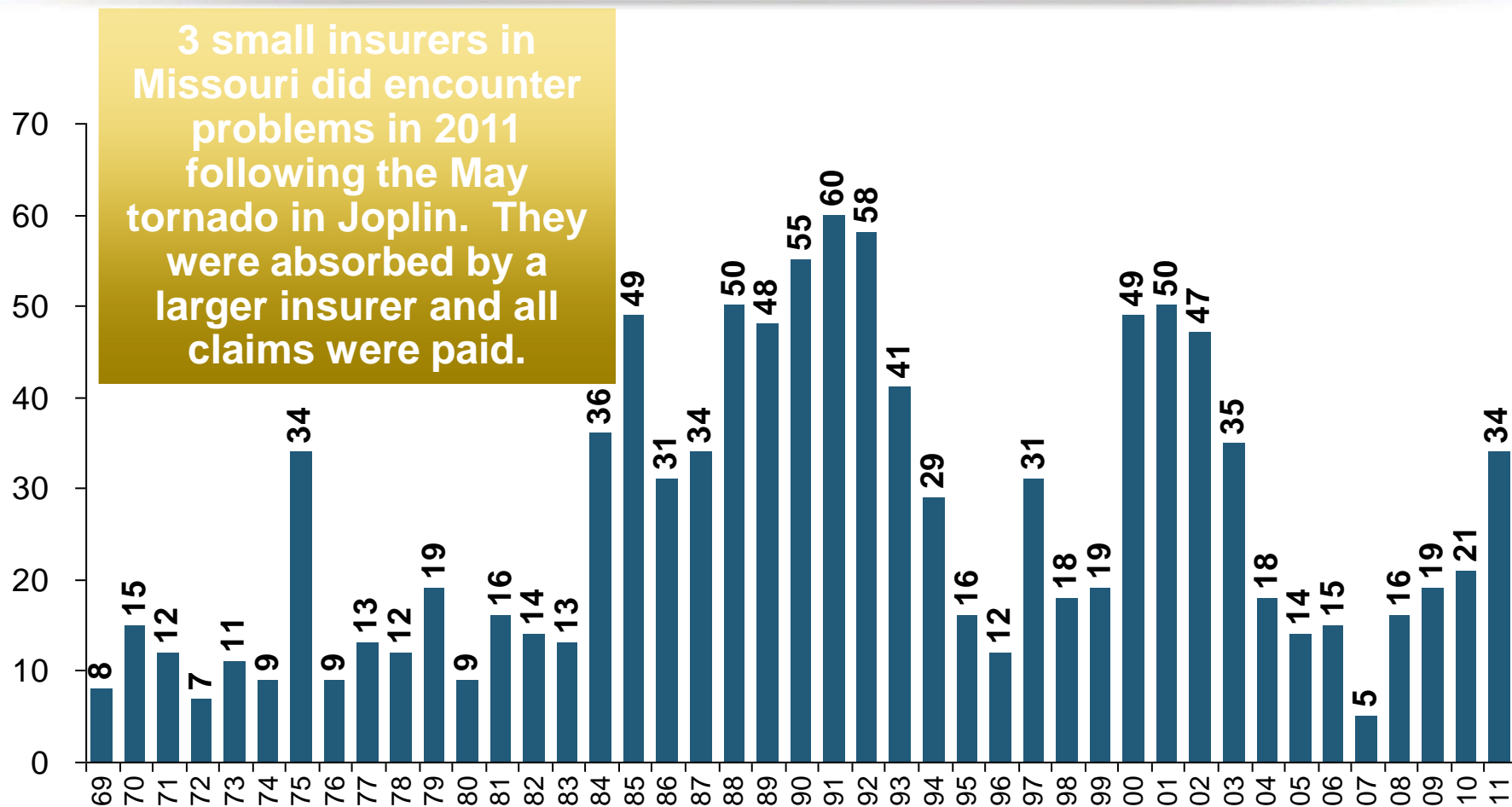
Sources: Insurance Information Institute research from A.M. Best Data.

# **Financial Strength & Underwriting**

**Cyclical Pattern is P-C Impairment  
History is Directly Tied to  
Underwriting, Reserving & Pricing**

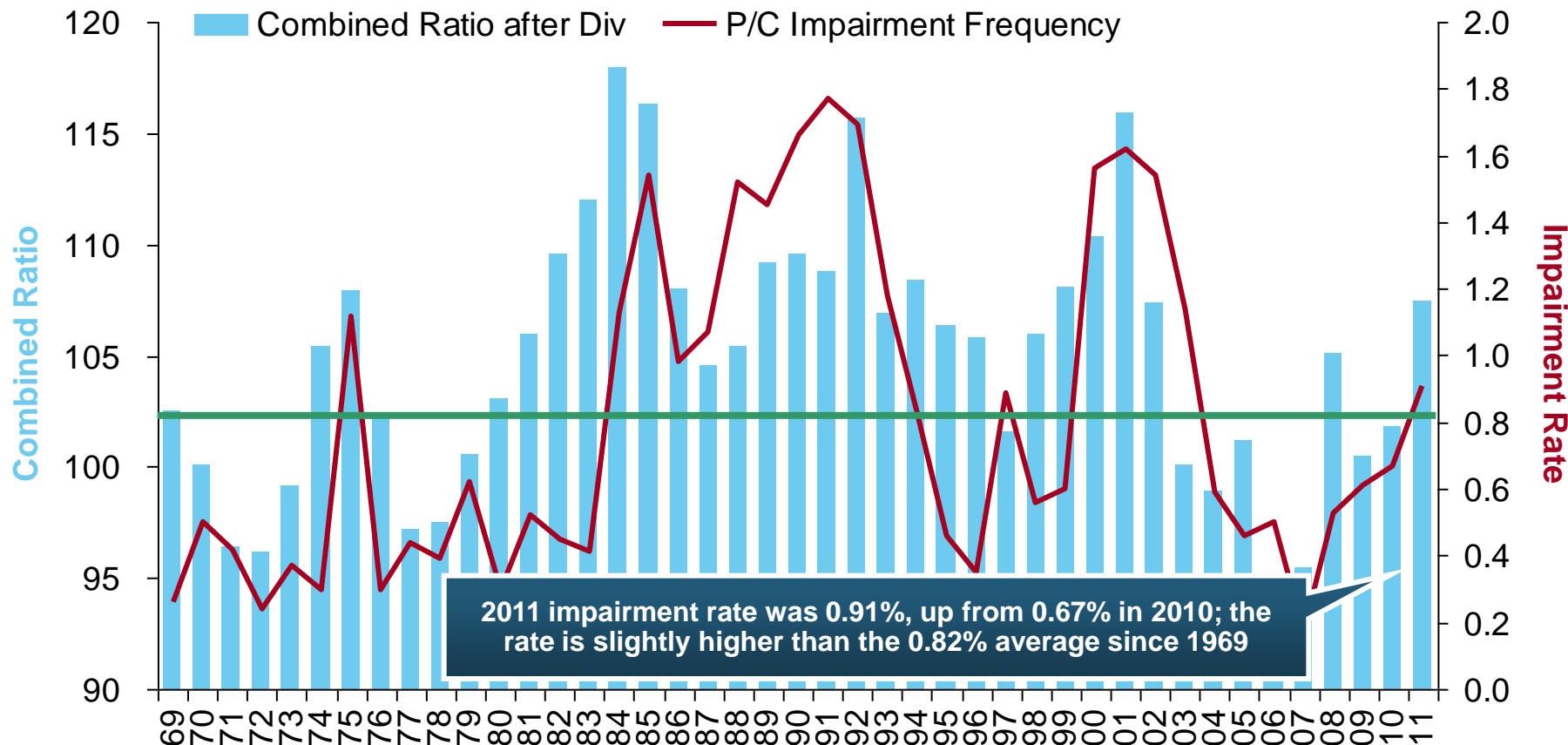


# P/C Insurer Impairments, 1969–2011



**The Number of Impairments Varies Significantly Over the P/C Insurance Cycle, With Peaks Occurring Well into Hard Markets**

# P/C Insurer Impairment Frequency vs. Combined Ratio, 1969-2011

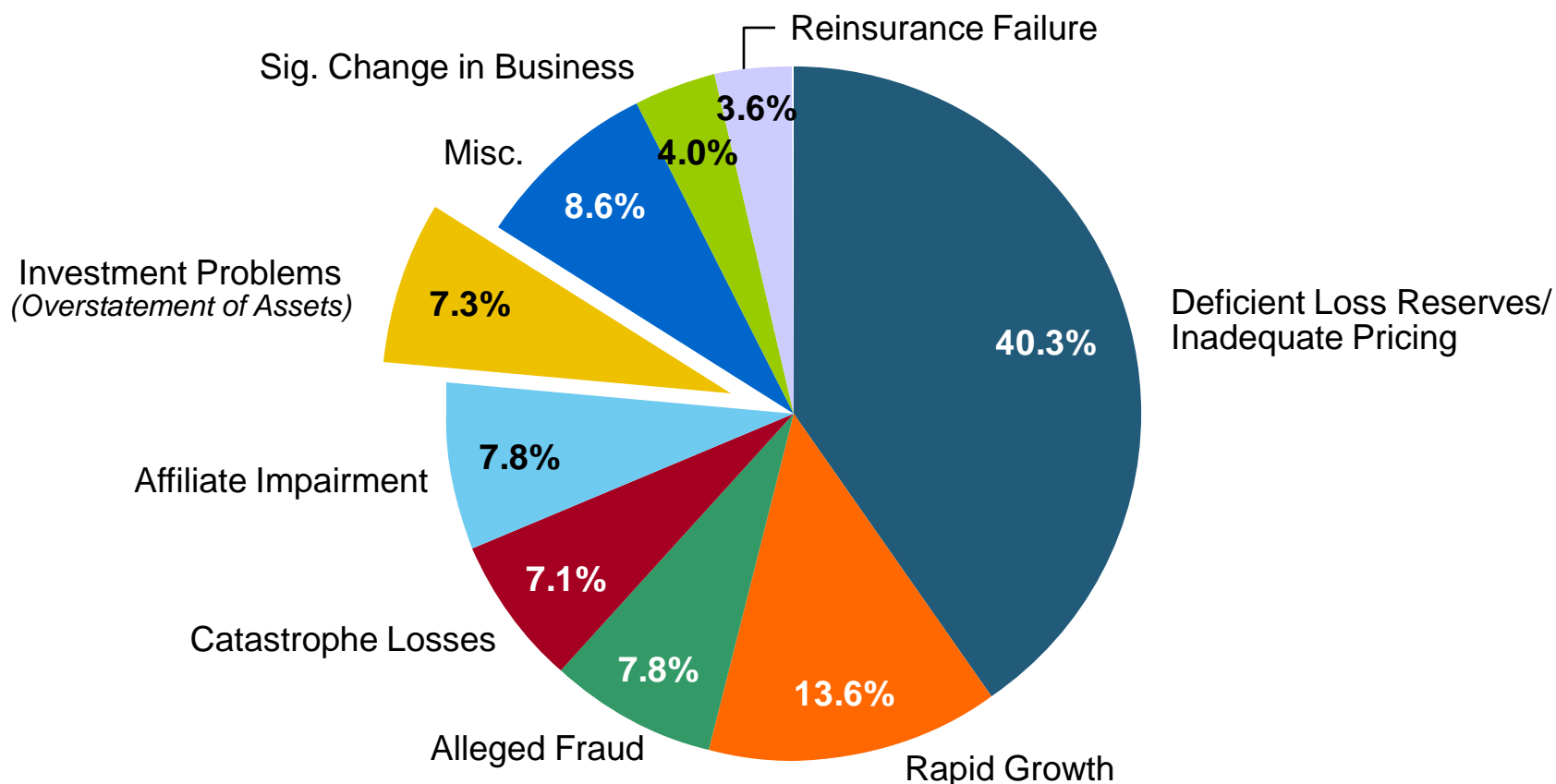


2011 impairment rate was 0.91%, up from 0.67% in 2010; the rate is slightly higher than the 0.82% average since 1969

**Impairment Rates Are Highly Correlated With Underwriting Performance and Reached Record Lows in 2007; Recent Increase Was Associated Primarily With Mortgage and Financial Guaranty Insurers and Not Representative of the Industry Overall**

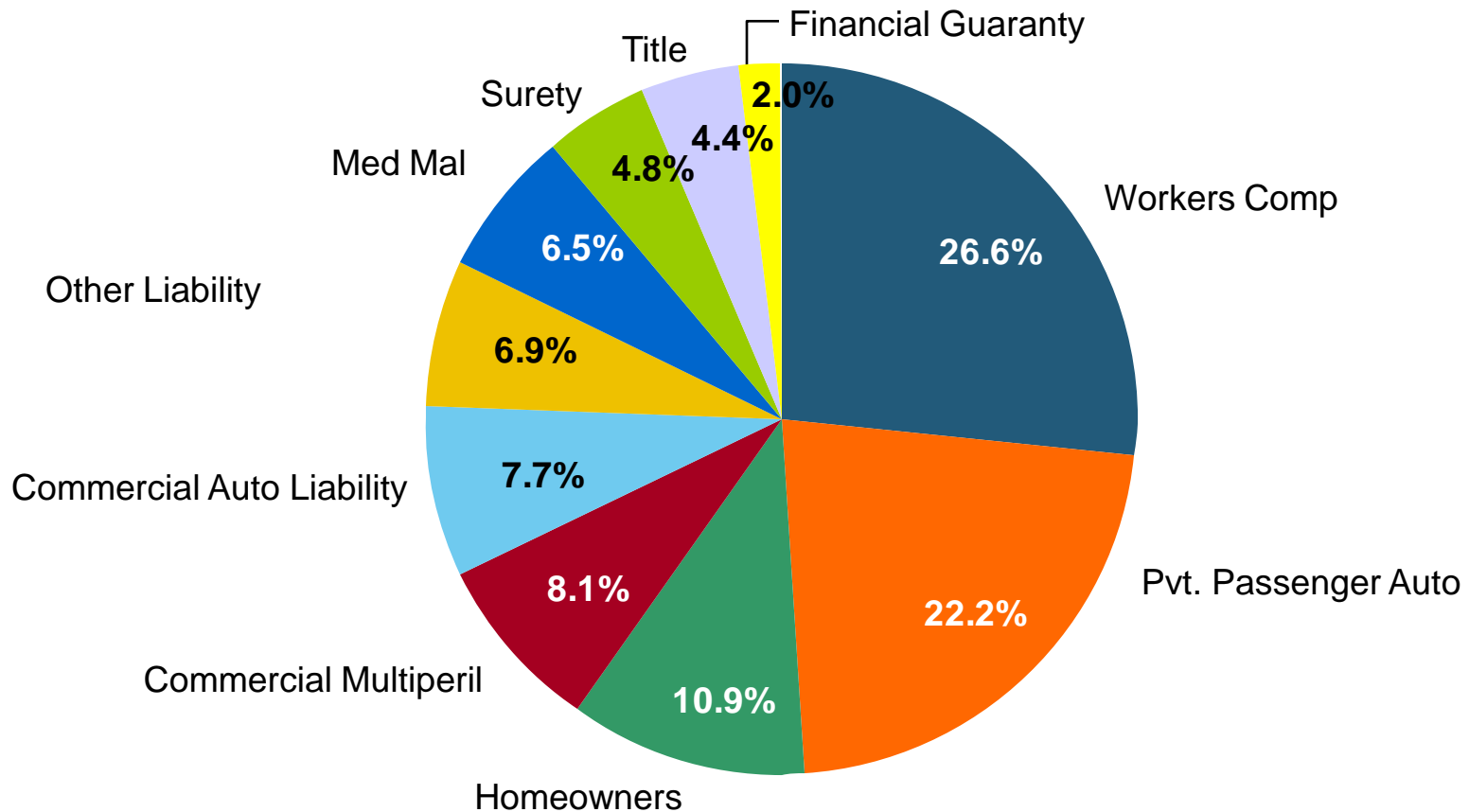
# Reasons for US P/C Insurer Impairments, 1969–2010

Historically, Deficient Loss Reserves and Inadequate Pricing Are By Far the Leading Cause of P-C Insurer Impairments. Investment and Catastrophe Losses Play a Much Smaller Role



# Top 10 Lines of Business for US P/C Impaired Insurers, 2000–2010

Workers Comp and Pvt. Passenger Auto Account for Nearly Half of the Premium Volume of Impaired Insurers Over the Past Decade



# Number of Recessions Endured by P/C Insurers, by Number of Years in Operation

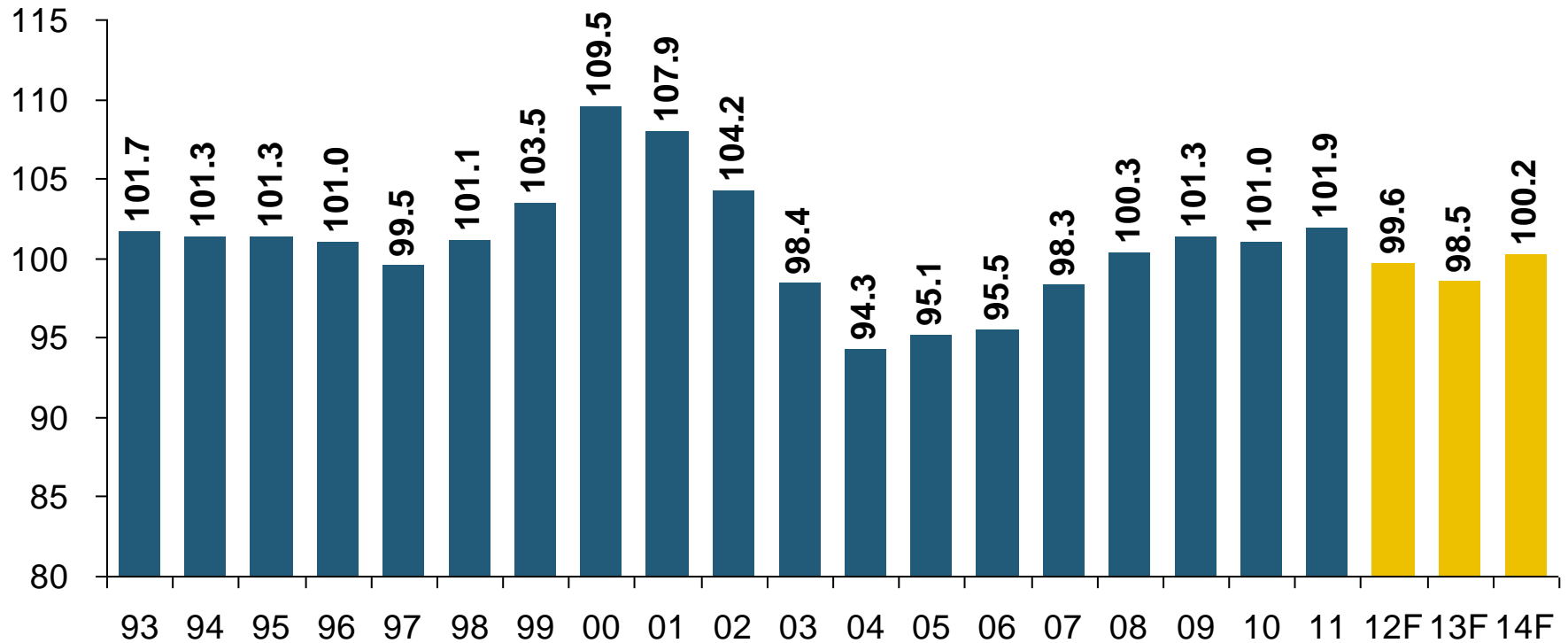
## Number of Recessions Since 1860



**Many US Insurers Are Close to a Century Old or Older**

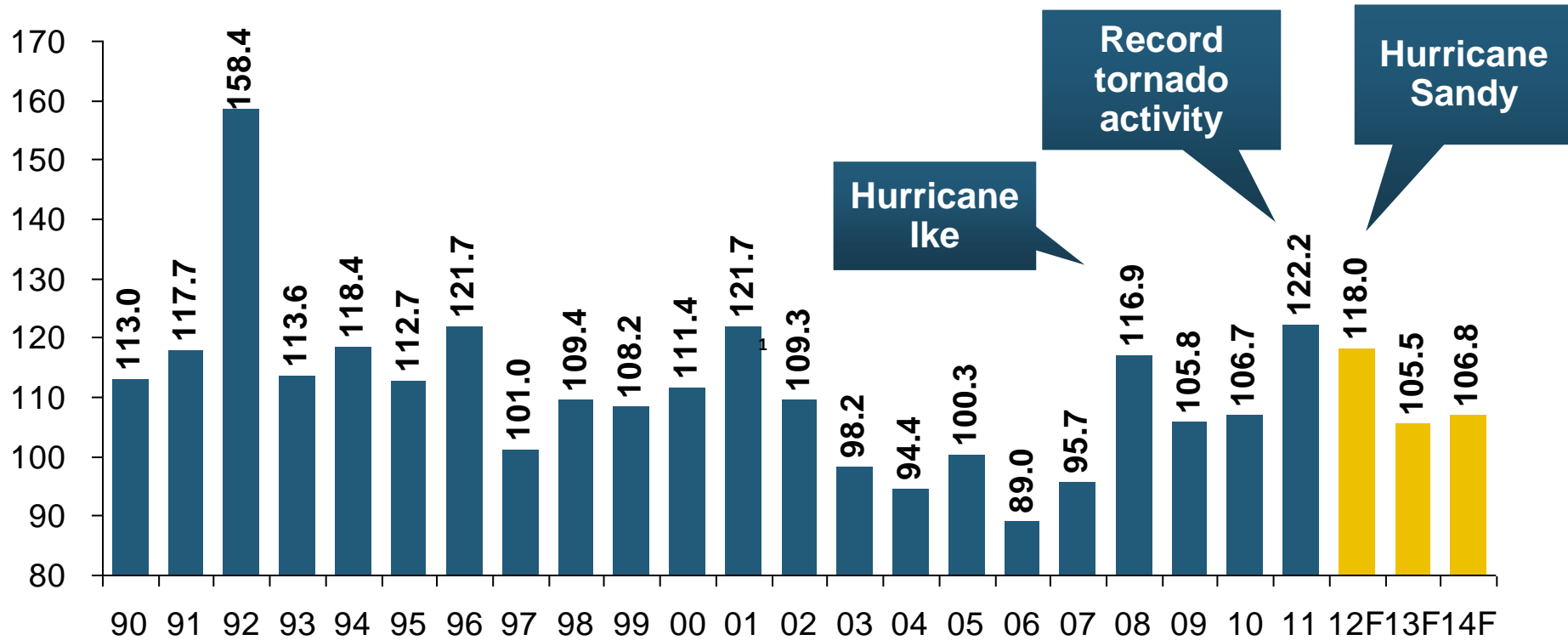
# Performance by Segment

# Private Passenger Auto Combined Ratio: 1993–2014F



**Private Passenger Auto Accounts for 34% of Industry Premiums and Remains the Profit Juggernaut of the P/C Insurance Industry**

# Homeowners Insurance Combined Ratio: 1990–2014F

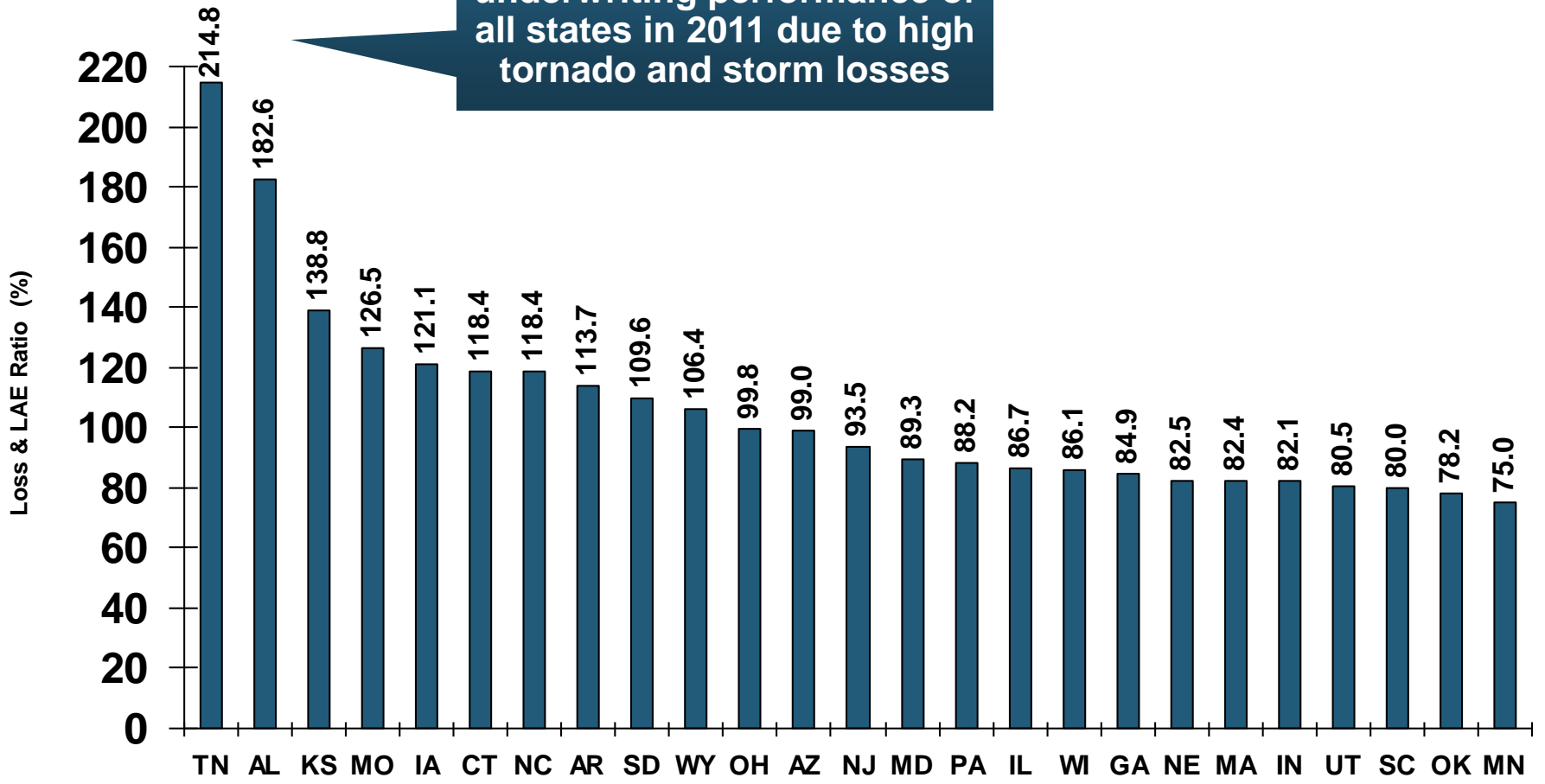


**Homeowners Performance Deteriorated in 2011/12 Due to Large Cat Losses. Extreme Regional Variation Can Be Expected Due to Local Catastrophe Loss Activity**



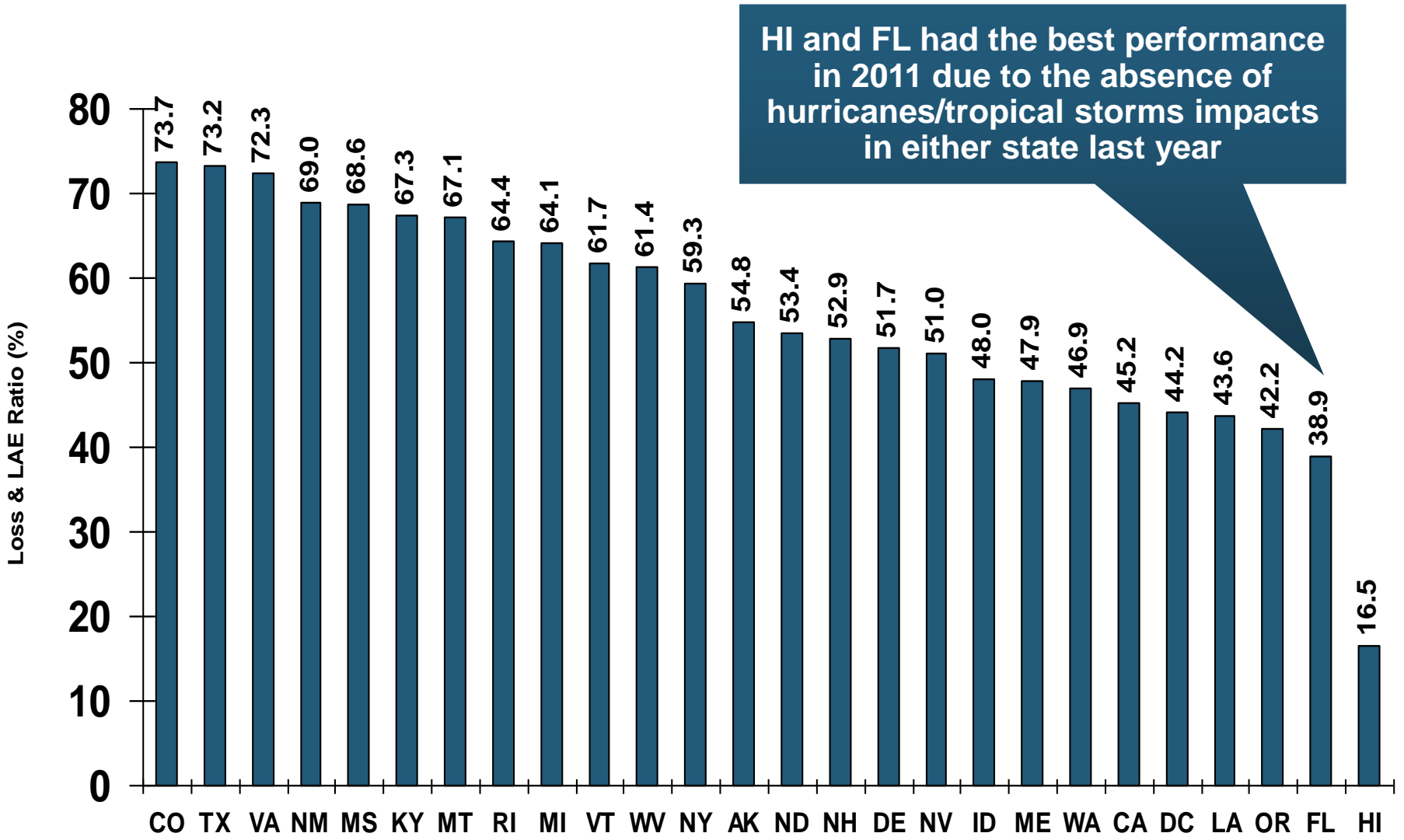
# Homeowners Multi-Peril Loss & LAE Ratio, 2011: Highest 25 States

TN and AL had the worst underwriting performance of all states in 2011 due to high tornado and storm losses



Sources: SNL Financial; Insurance Information Institute.

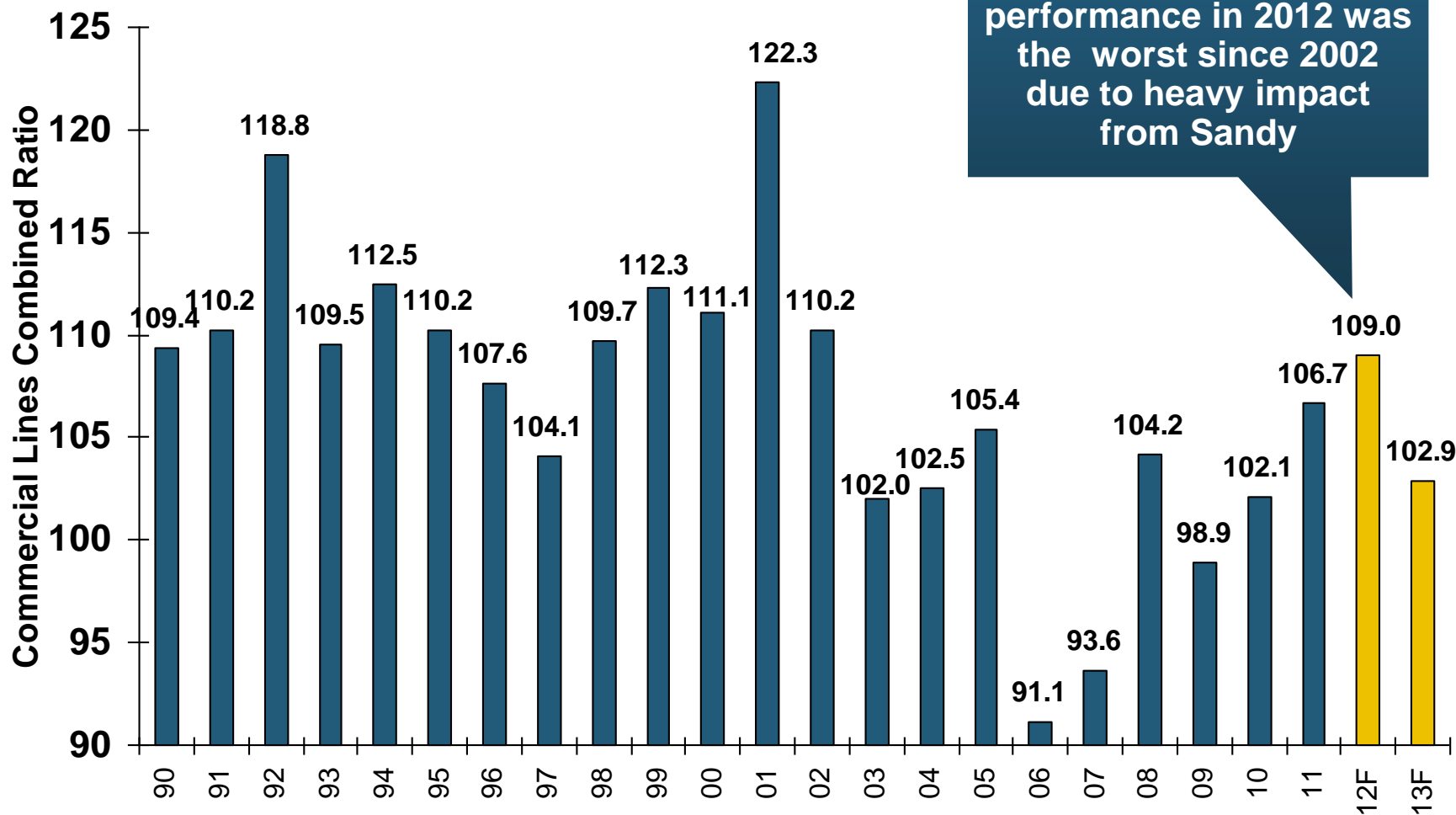
# Homeowners Multi-Peril Loss & LAE Ratio, 2011: Lowest 25 States



HI and FL had the best performance in 2011 due to the absence of hurricanes/tropical storms impacts in either state last year

Sources: SNL Financial; Insurance Information Institute.

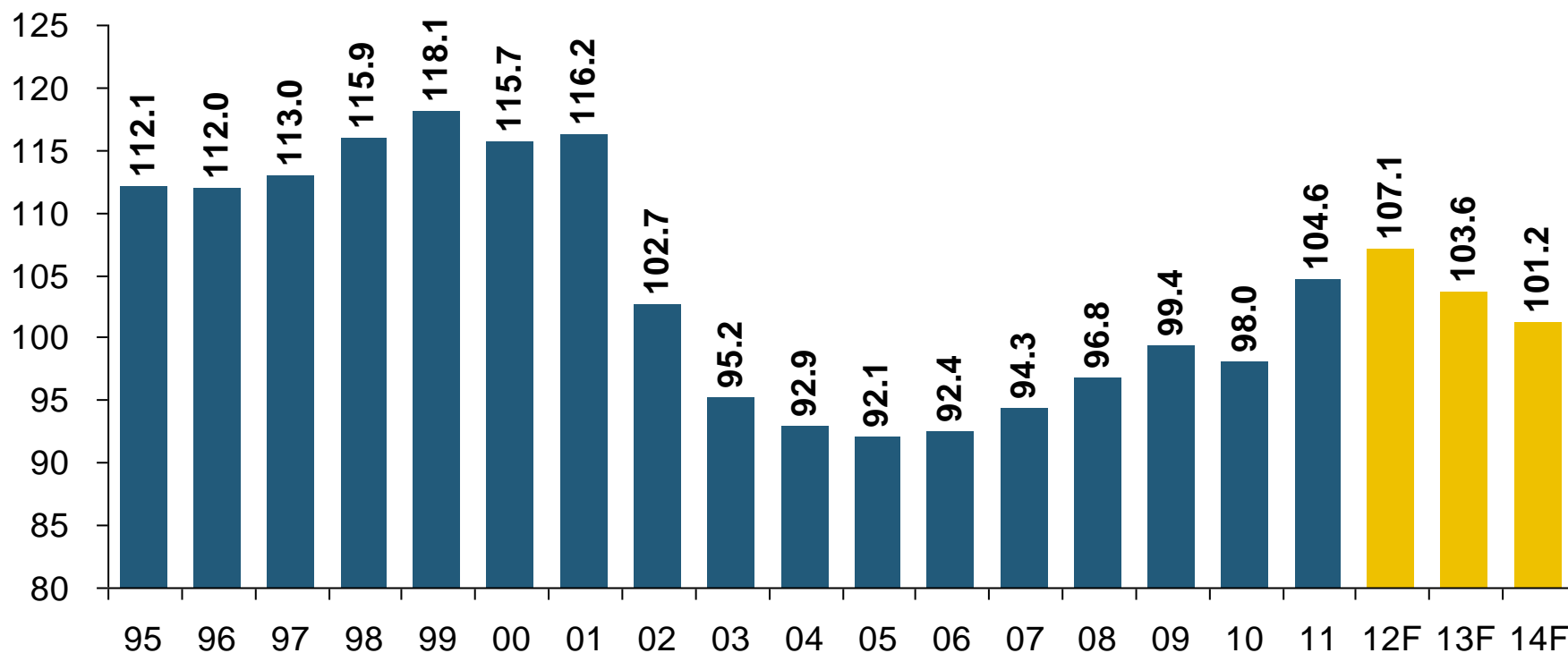
# Commercial Lines Combined Ratio, 1990-2013F\*



\*2007-2013F figures exclude mortgage and financial guaranty segments.

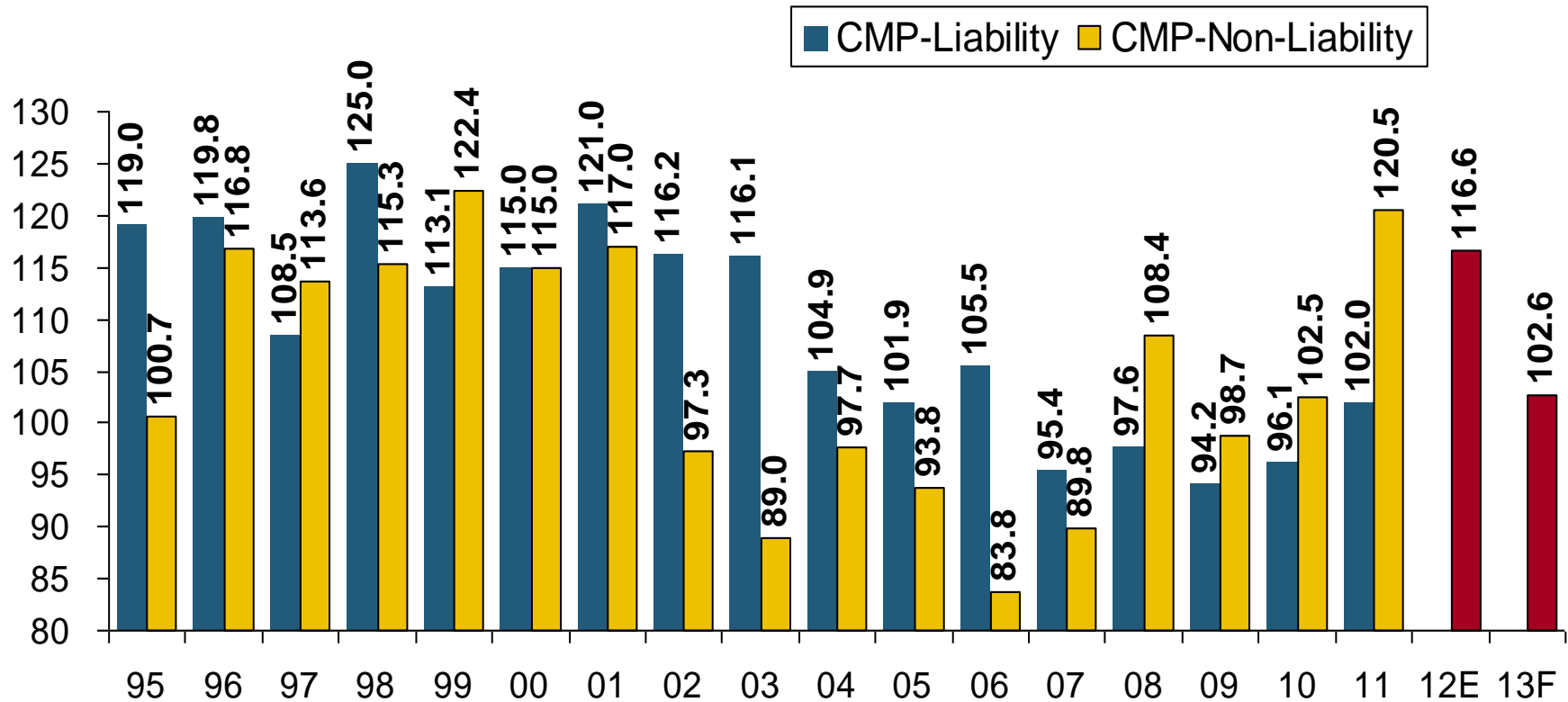
Source: A.M. Best; Insurance Information Institute

# Commercial Auto Combined Ratio: 1993–2014F



**Commercial Auto is Expected to Improve as Rate Gains Outpace Any Adverse Frequency and Severity Trends**

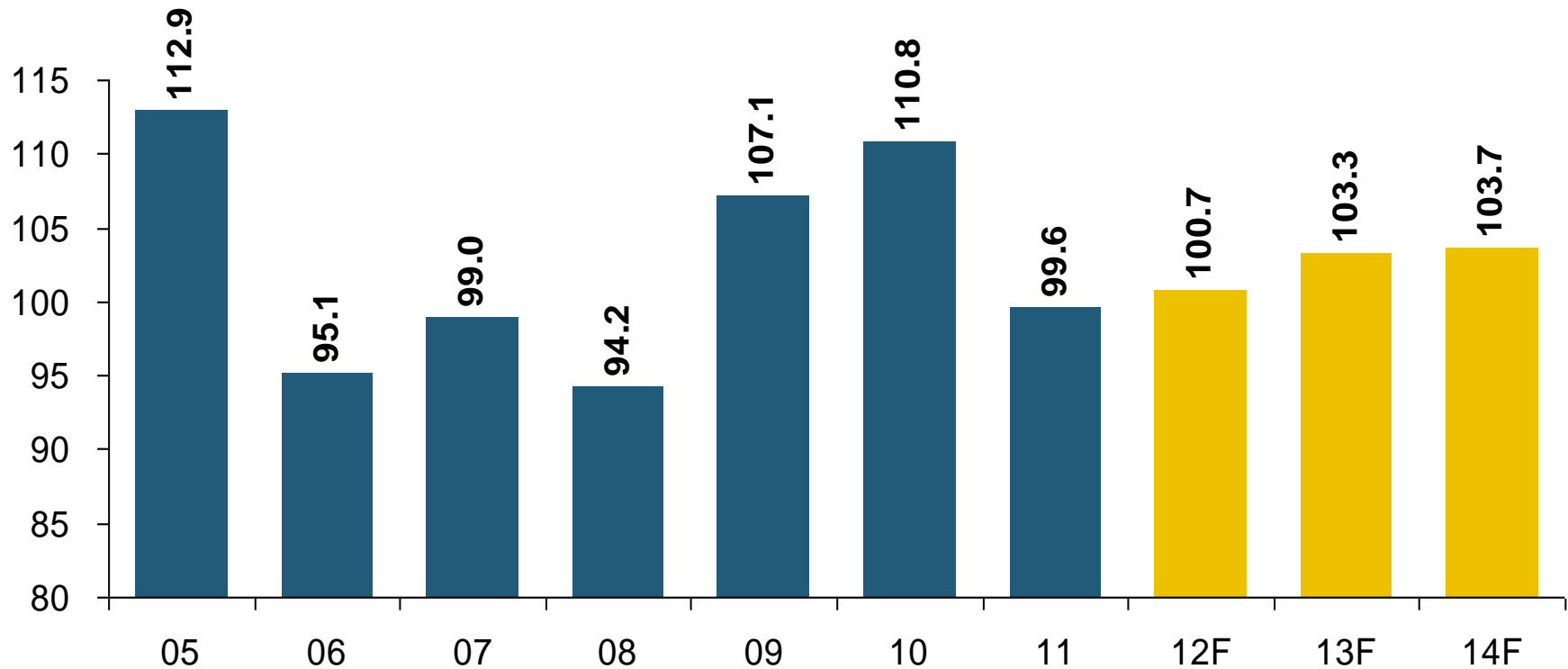
# Commercial Multi-Peril Combined Ratio: 1995–2013F



**Commercial Multi-Peril Underwriting Performance is Expected to Improve in 2013 Assuming Normal Catastrophe Loss Activity**

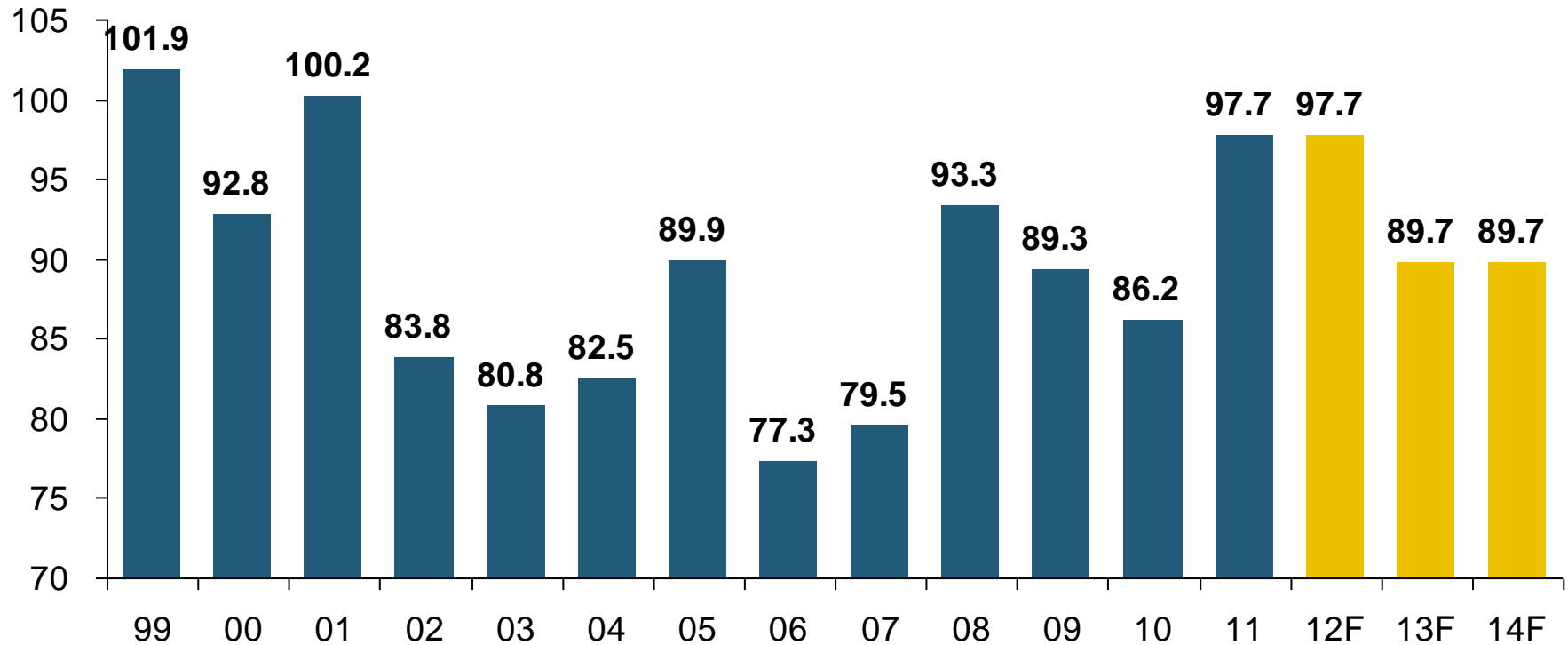
\*2012-2013 figures are A.M. Best estimate/forecast for the combined liability and non-liability components.  
Sources: A.M. Best; Insurance Information Institute.

# General Liability Combined Ratio: 2005–2014F



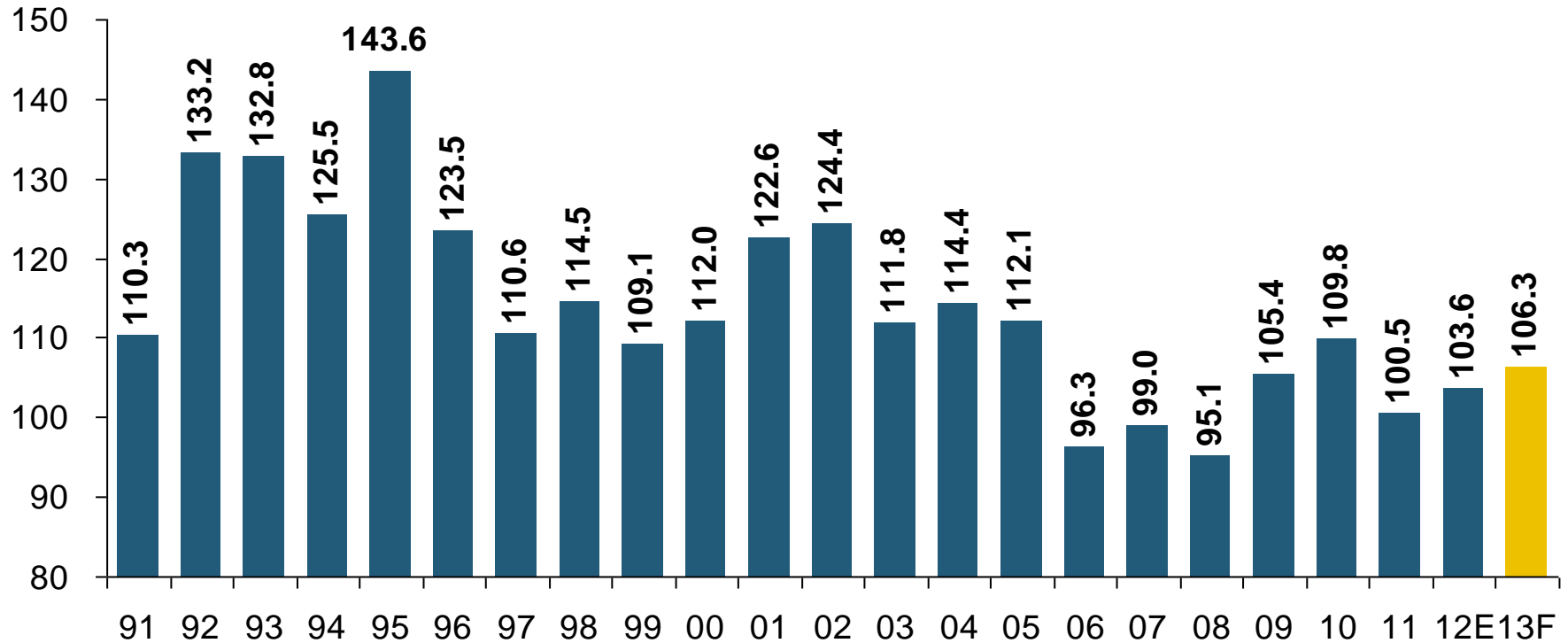
**Commercial General Liability Underwriting  
Performance Has Been Volatile in Recent Years**

# Inland Marine Combined Ratio: 1999–2014F



**Inland Marine is Expected to Remain Among the Most Profitable of All Lines**

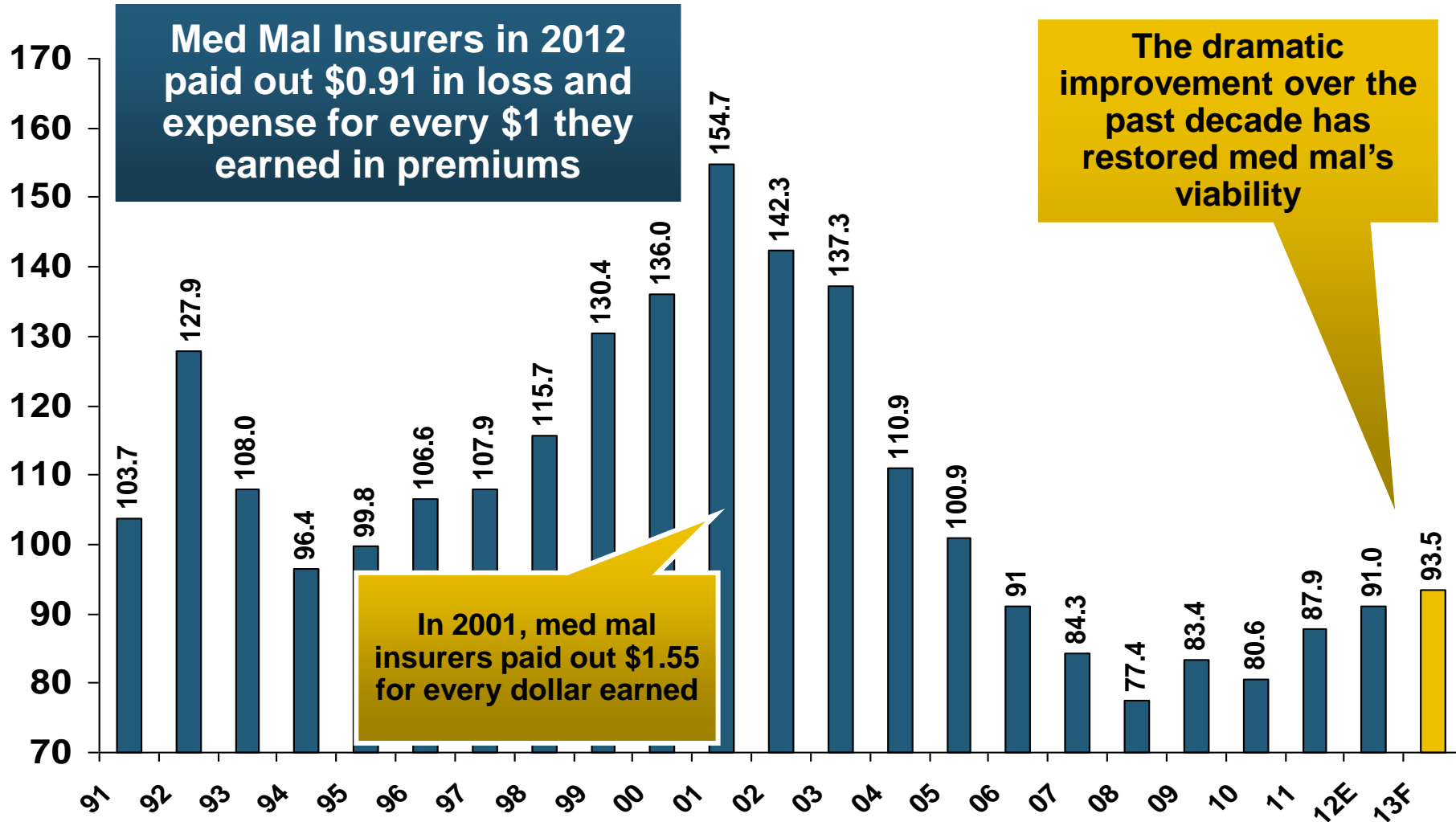
# Other & Products Liability Combined Ratio: 1991–2013F



**Liability Lines Have Performed Better in the Post-Tort Reform Era (~2005), but There Has Been Some Deterioration in Recent Years**



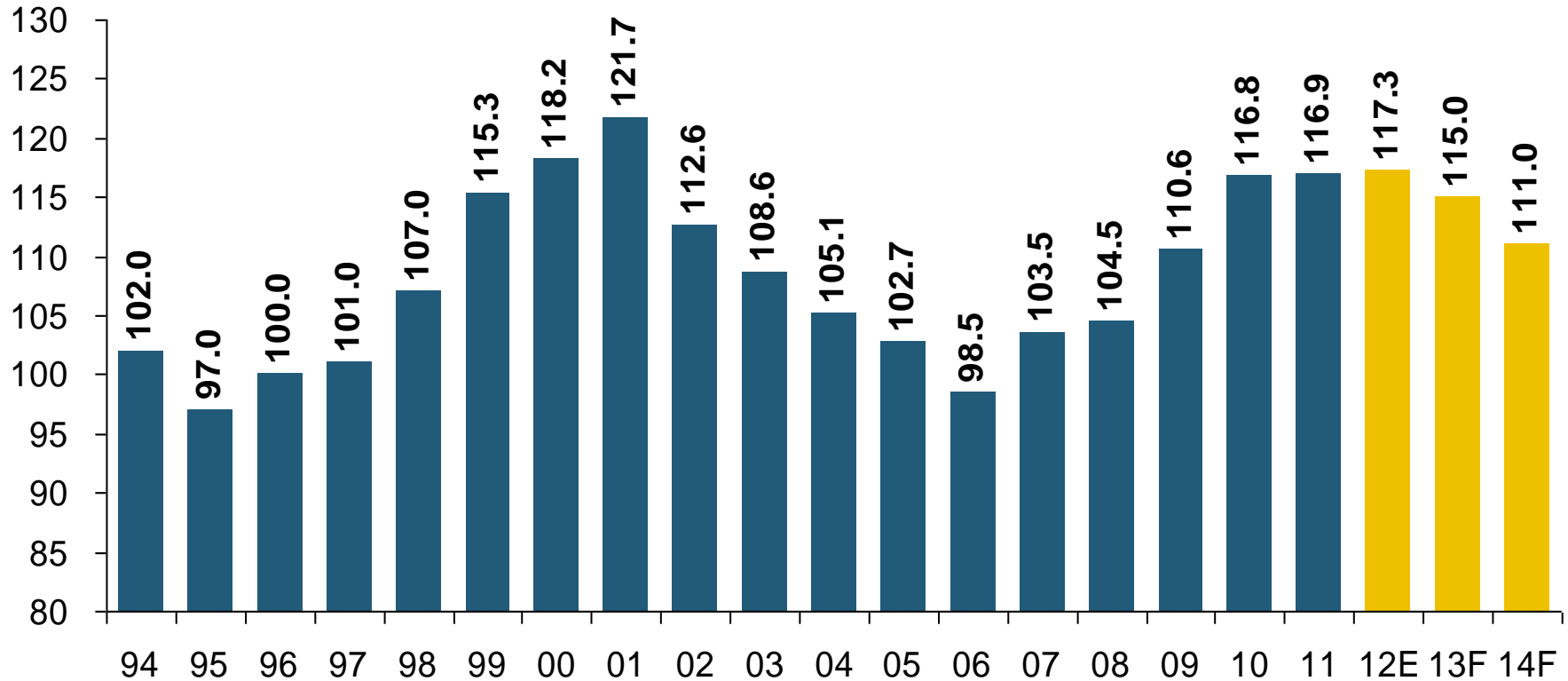
# Medical Malpractice Combined Ratio vs. All Lines Combined Ratio, 1991-2013F



# **Workers Compensation Operating Environment**

**The Weak Economy and Soft Market Have  
Made the Workers Comp Operating  
Increasingly Challenging**

# Workers Compensation Combined Ratio: 1994–2014F



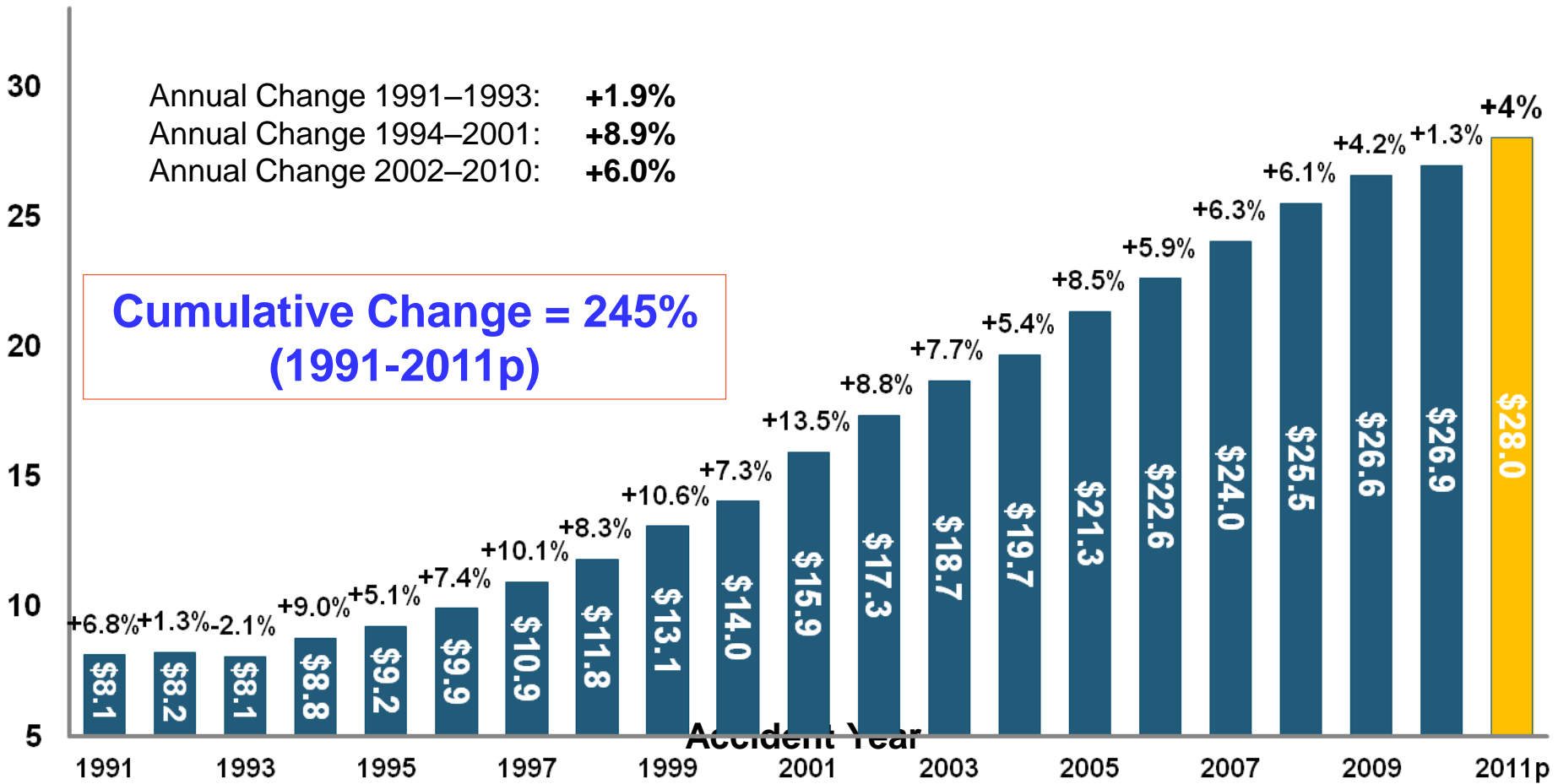
**Workers Comp Results Should Begin to Improve in 2013. Underwriting Results Deteriorated Markedly from 2007-2012 and Were the Worst They Had Been in a Decade.**

# Workers Compensation Medical Severity Moderate Increase in 2011



## Average Medical Cost per Lost-Time Claim

Medical Claim Cost (\$000s)



**Cumulative Change = 245%  
(1991-2011p)**

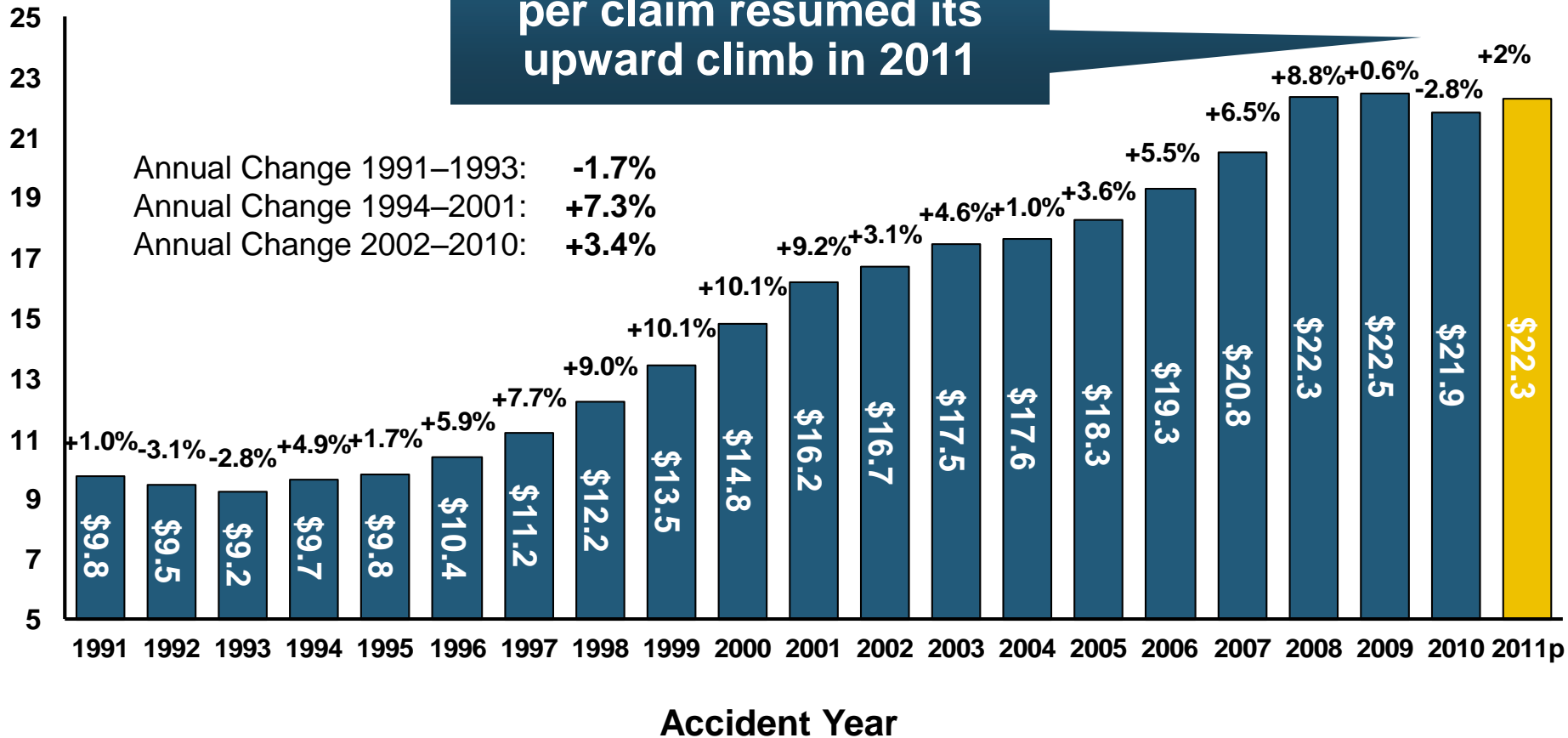
2011p: Preliminary based on data valued as of 12/31/2011  
 1991-2010: Based on data through 12/31/2010, developed to ultimate  
 Based on the states where NCCI provides ratemaking services; Excludes high deductible policies

# Workers Comp Indemnity Claim Costs: Modest Increase in 2011

## Average Indemnity Cost per Lost-Time Claim

Indemnity Claim Cost (\$ 000s)

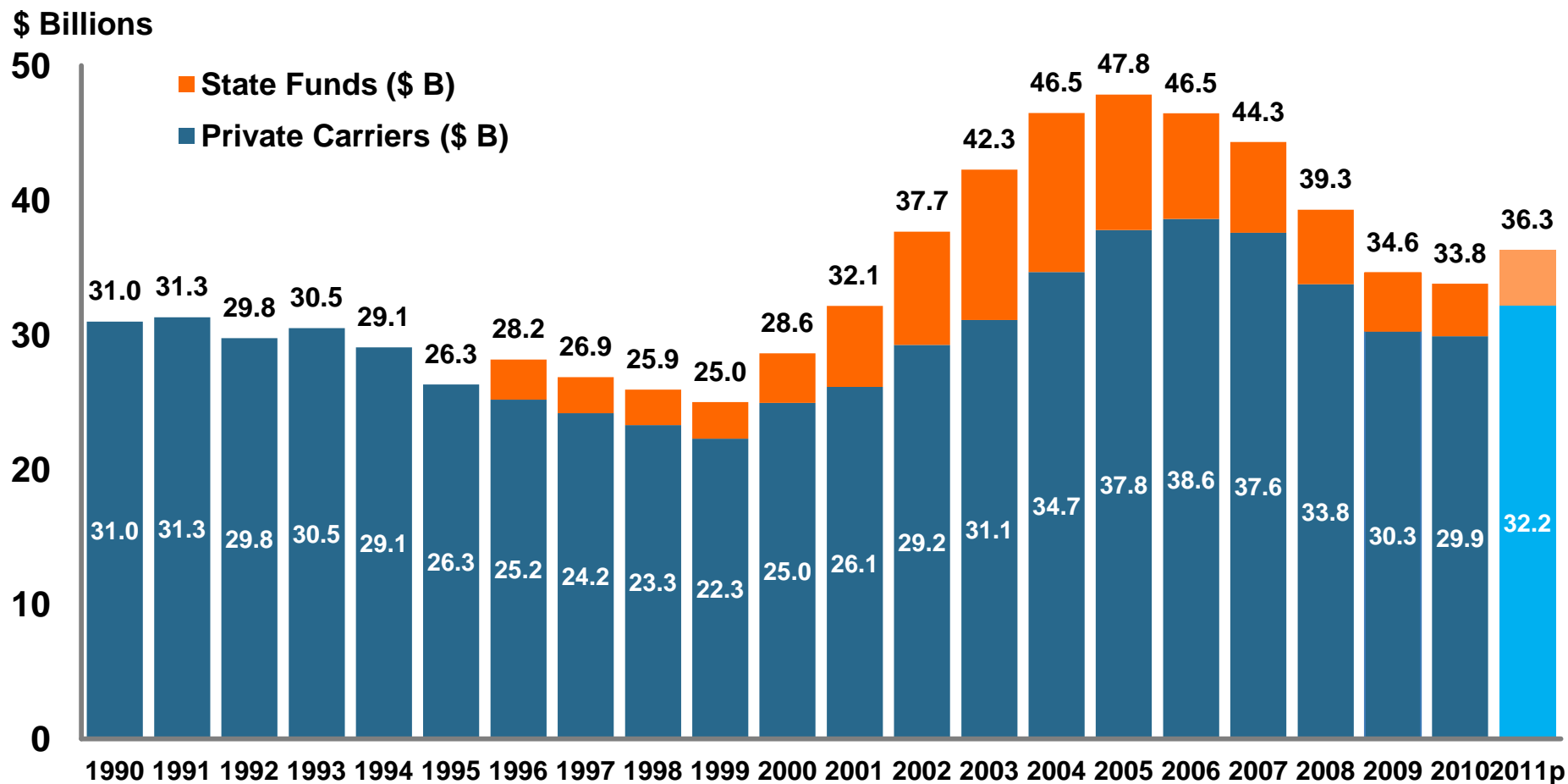
Average indemnity costs per claim resumed its upward climb in 2011



2010p: Preliminary based on data valued as of 12/31/2011  
 1991–2010: Based on data through 12/31/2010, developed to ultimate  
 Based on the states where NCCI provides ratemaking services  
 Excludes high deductible policies

# Workers Compensation Premium: First Increase in Years

## Net Written Premium



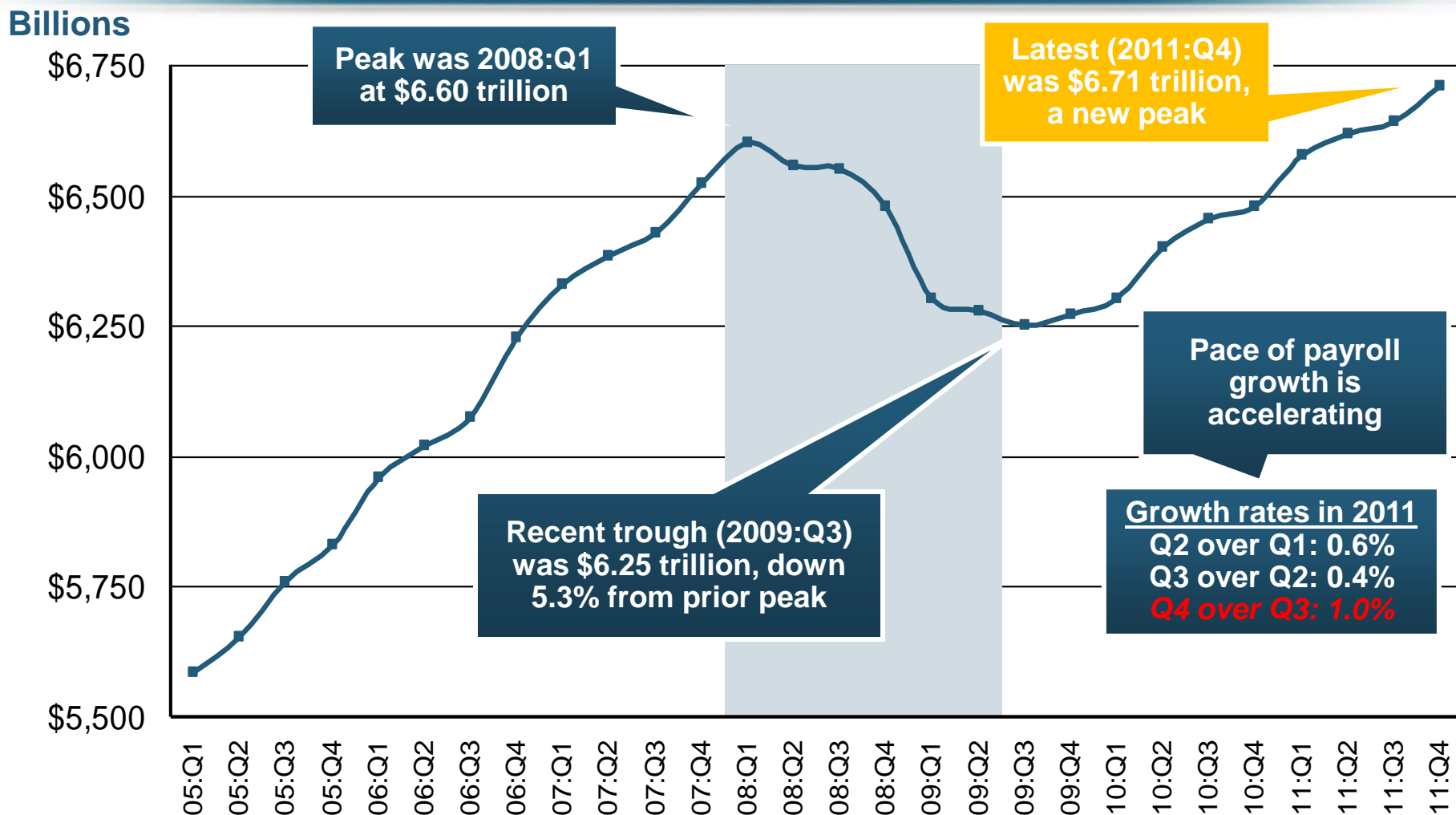
p Preliminary

Source: 1990–2010 Private Carriers, *Best's Aggregates & Averages*; 2011p, NCCI

1996–2011p State Funds: AZ, CA, CO, HI, ID, KY, LA, MD, MO, MT, NM, OK, OR, RI, TX, UT Annual Statements

State Funds available for 1996 and subsequent

# Nonfarm Payroll (Wages and Salaries): Quarterly, 2005–2011:Q4



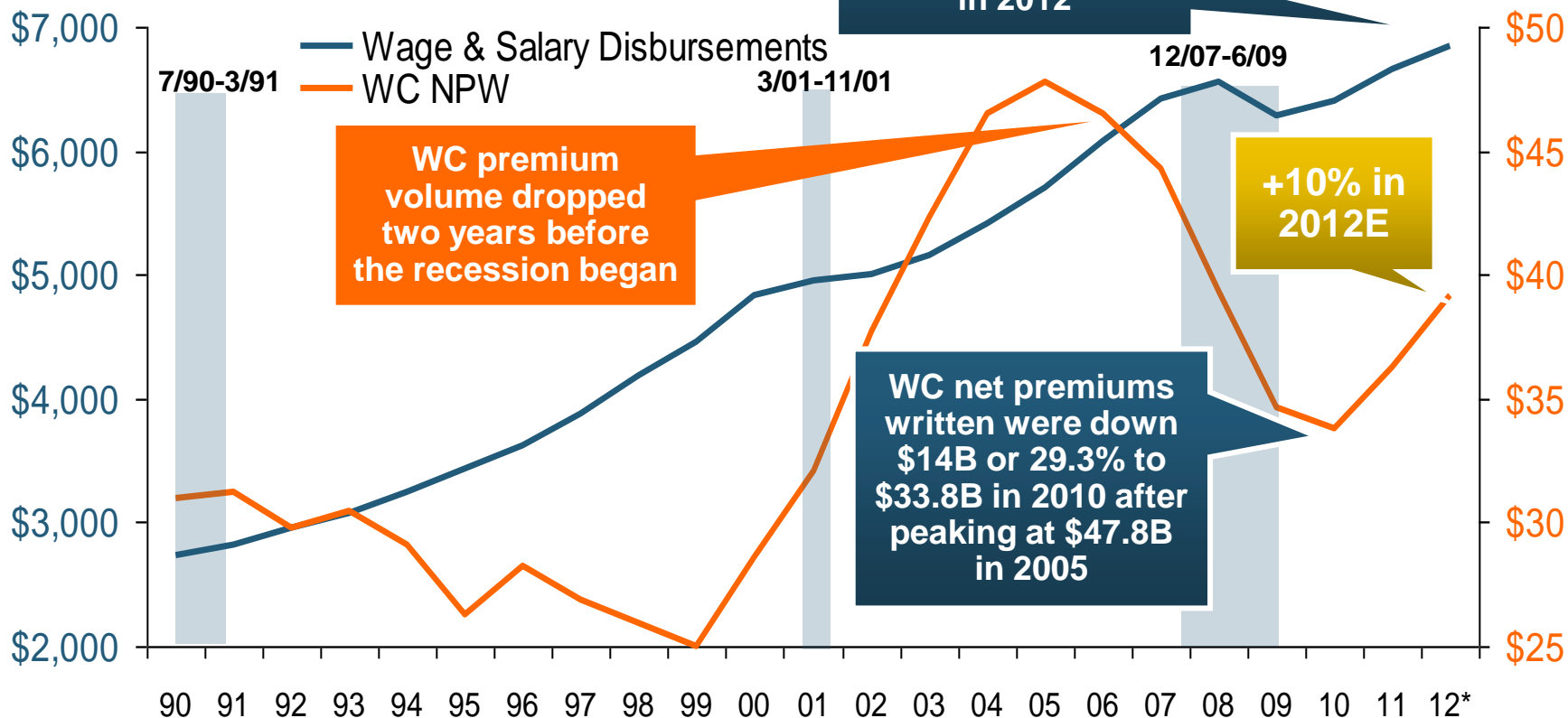
Note: Recession indicated by gray shaded column. Data are seasonally adjusted annual rates.

Sources: <http://research.stlouisfed.org/fred2/series/WASCUR>; National Bureau of Economic Research (recession dates); Insurance Information Institute.

# Payroll vs. Workers Comp Net Written Premiums, 1990-2012E

Payroll Base\*  
\$Billions

WC NWP  
\$Billions



**Continued Payroll Growth and Rate Increases Suggest WC NWP Will Grow Again in 2012; +7.9% Growth in 2011 Was the First Gain Since 2005**

\*Shaded areas indicate recessions.

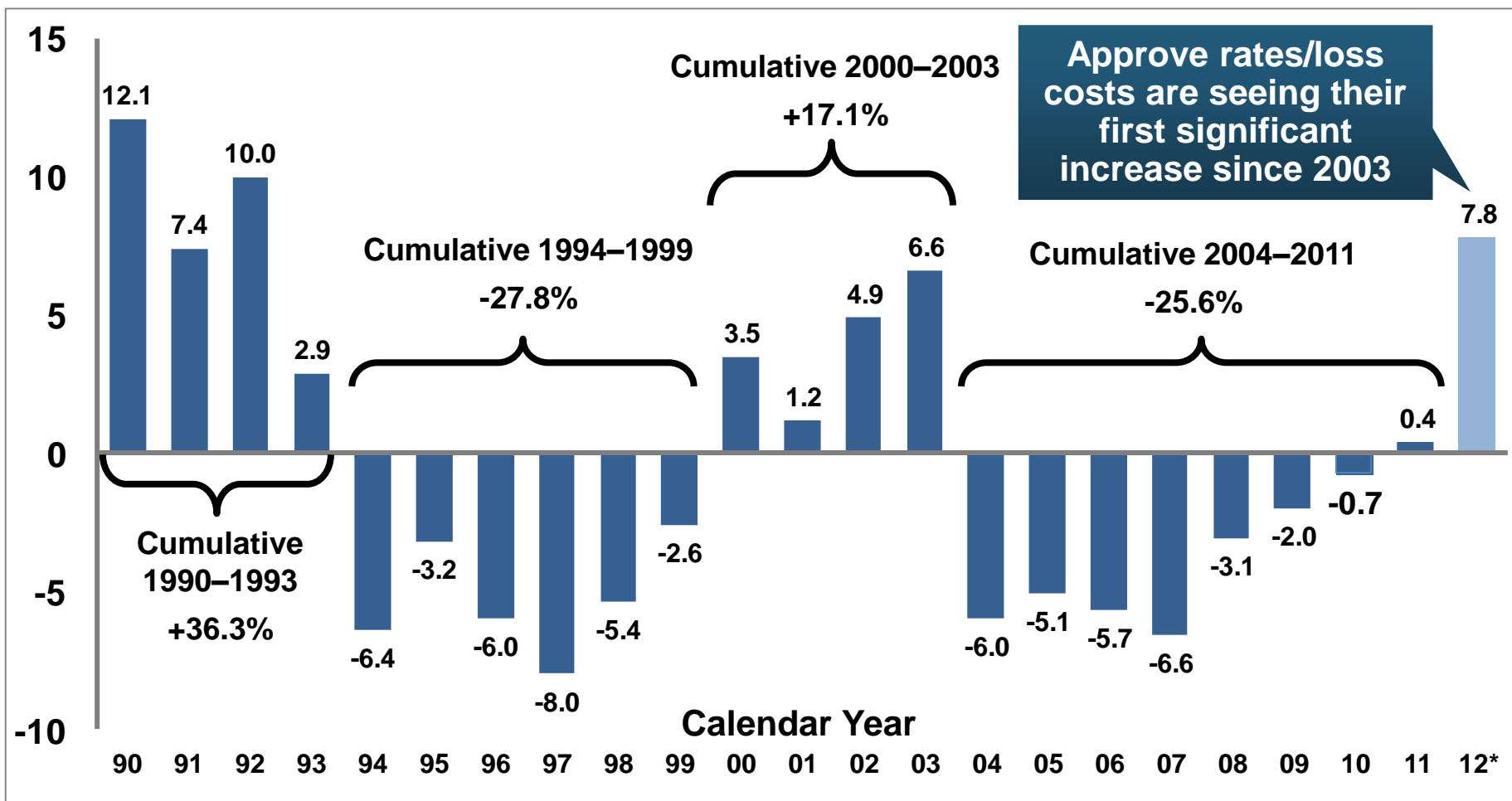
Sources: NBER (recessions); Federal Reserve Bank of St. Louis at <http://research.stlouisfed.org/fred2/series/WASCUR> ; NCCI; I.I.I.



# Average Approved Bureau Rates/Loss Costs

## History of Average WC Bureau Rate/Loss Cost Level Changes

Percent



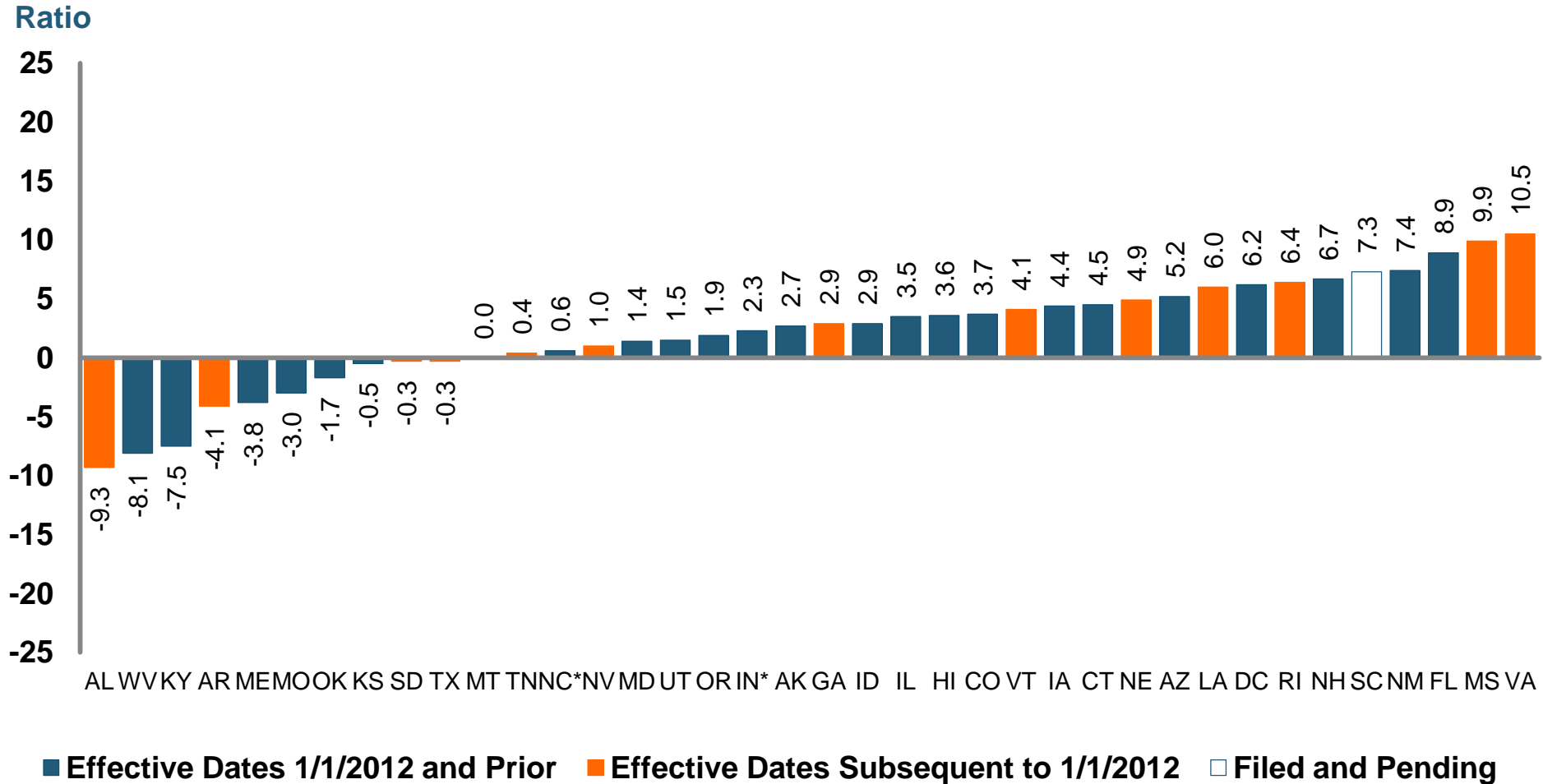
\*States approved through 7/31/12.

Note: Countrywide approved changes in advisory rates, loss costs and assigned risk rates as filed by applicable rating organization.

Source: NCCI.

# Current NCCI Voluntary Market Filed Rate/Loss Cost Changes

(Excludes Law-Only Filings)

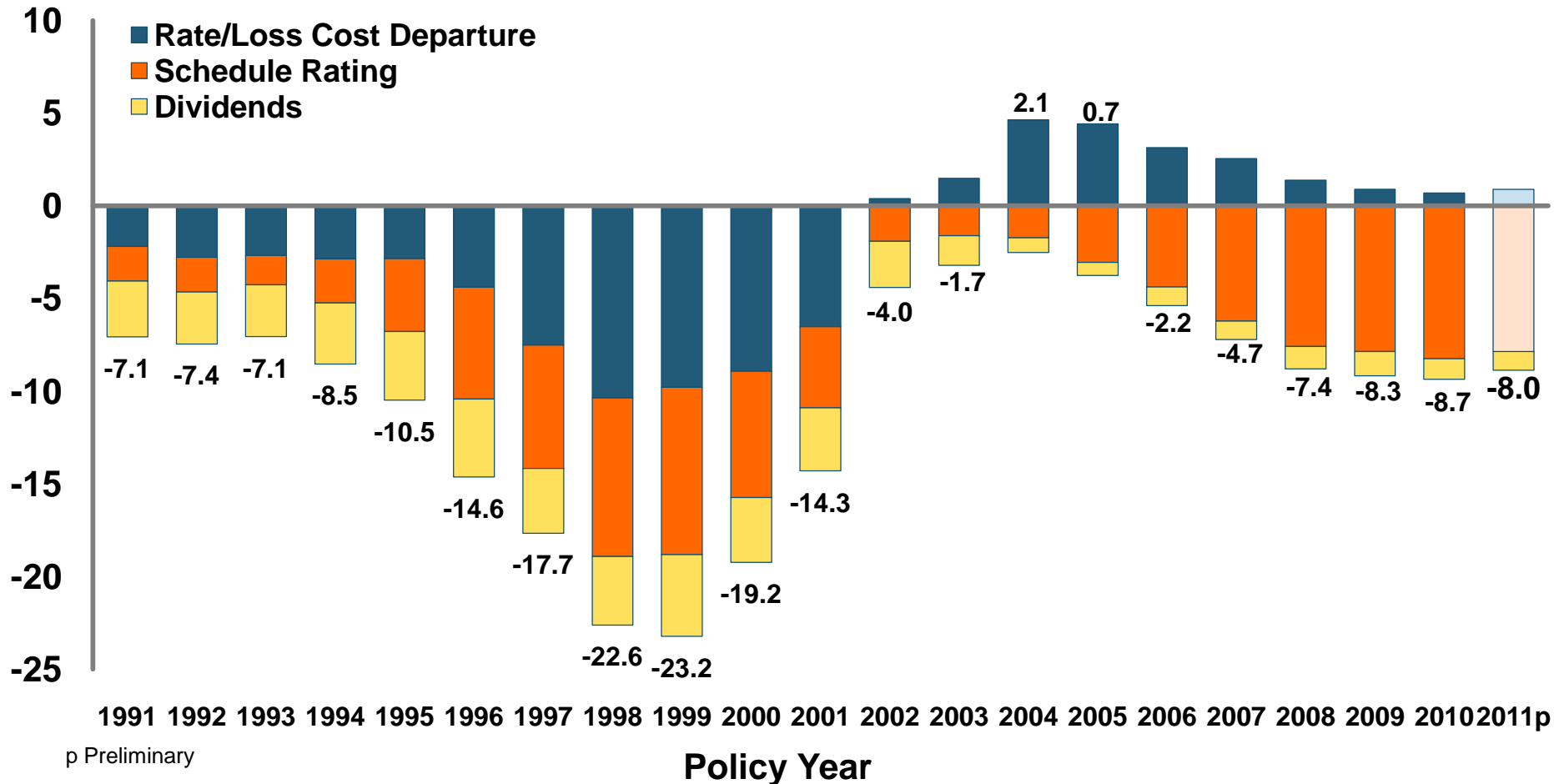


\*IN and NC filed in cooperation with state rating bureau  
Source: NCCI

# Impact of Discounting on Workers Compensation Premium

## NCCI States—Private Carriers

Percent



p Preliminary

Dividend ratios are based on calendar year statistics

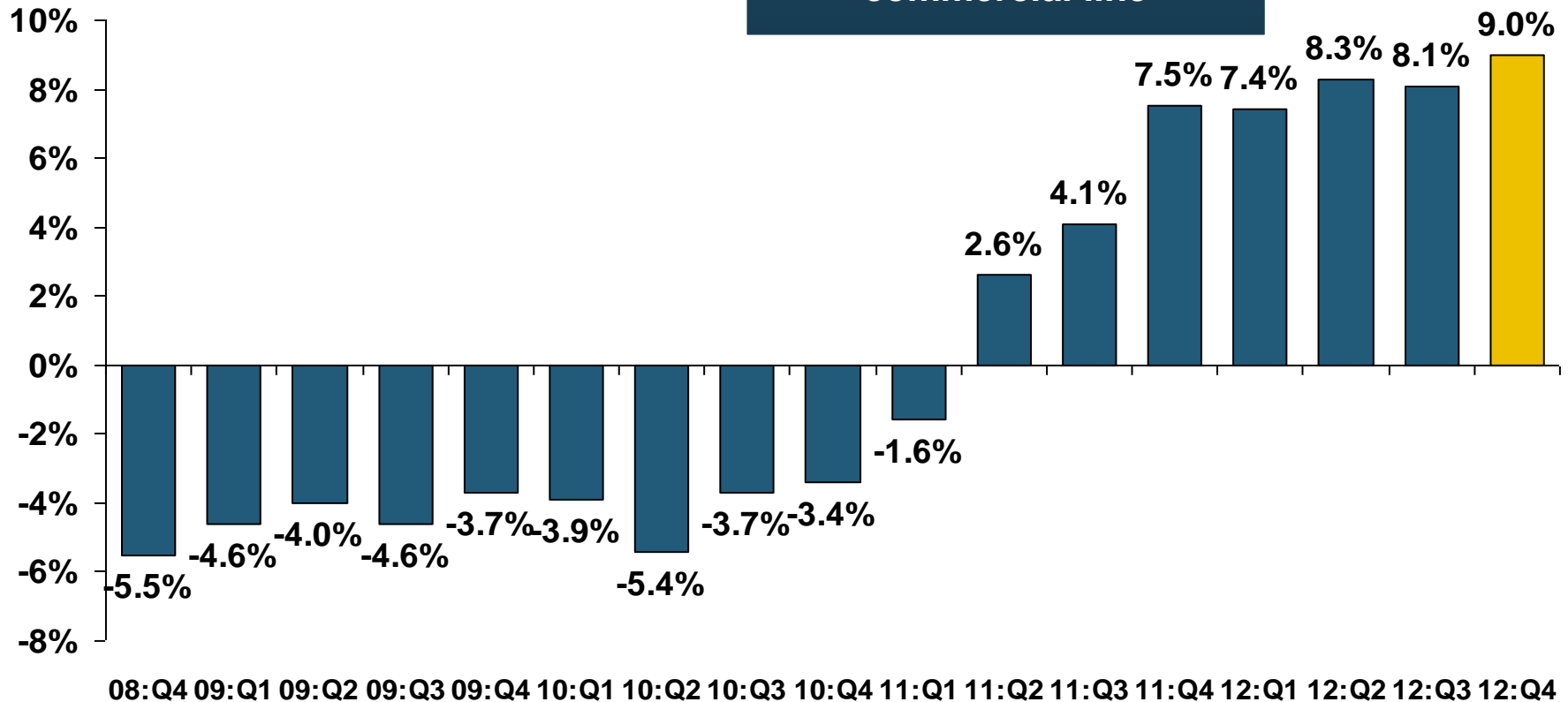
NCCI benchmark level does not include an underwriting contingency provision

Based on data through 12/31/2011 for the states where NCCI provides ratemaking services

Source: NCCI.

# Workers Comp Rate Changes, 2008:Q4 – 2012:Q4

(Percent Change)



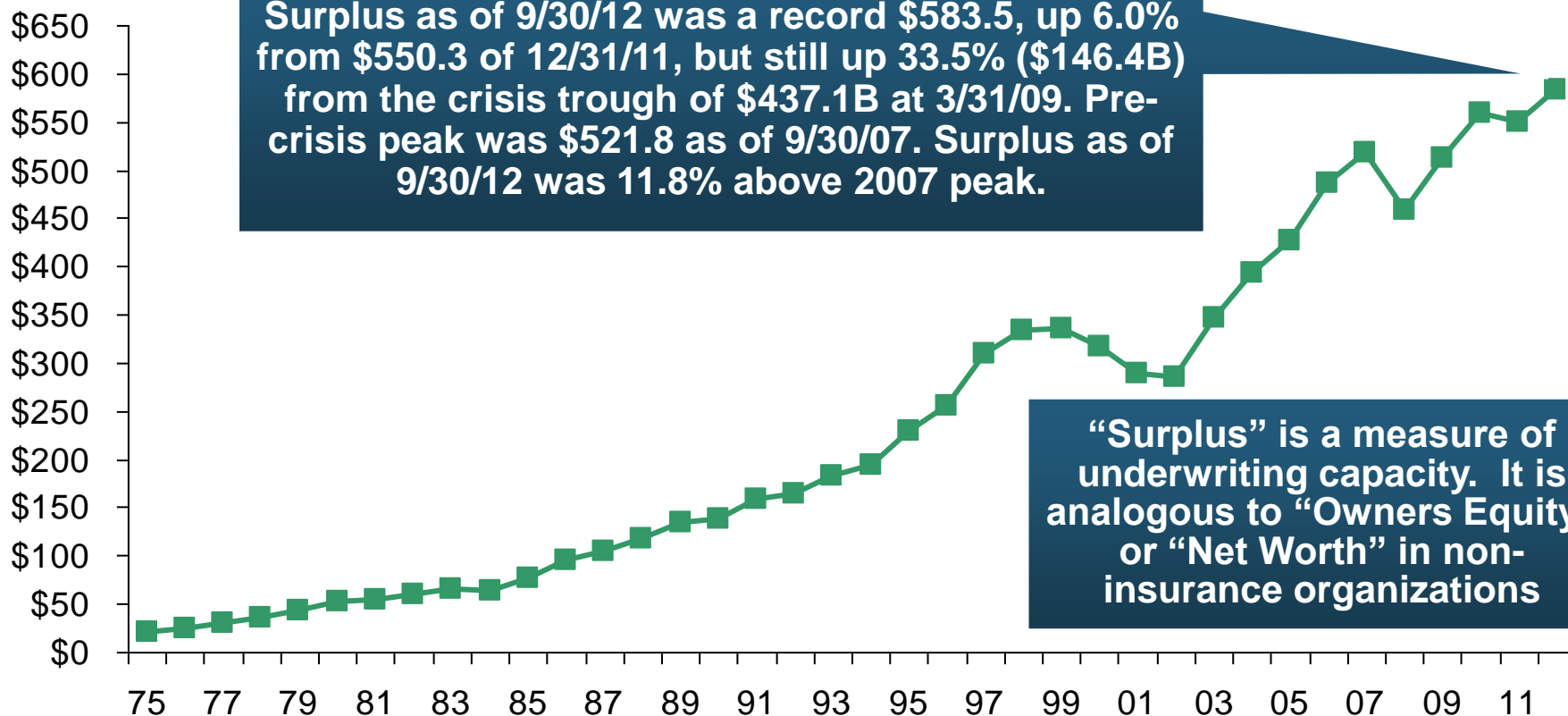
Note: CIAB data cited here are based on a survey. Rate changes earned by individual insurers can and do vary, potentially substantially.  
 Source: Council of Insurance Agents and Brokers; Information Institute.

## **2. SURPLUS/CAPITAL/CAPACITY**

**How Will Large Catastrophe Losses  
Impact Capacity?**

# US Policyholder Surplus: 1975–2012\*

(\$ Billions)



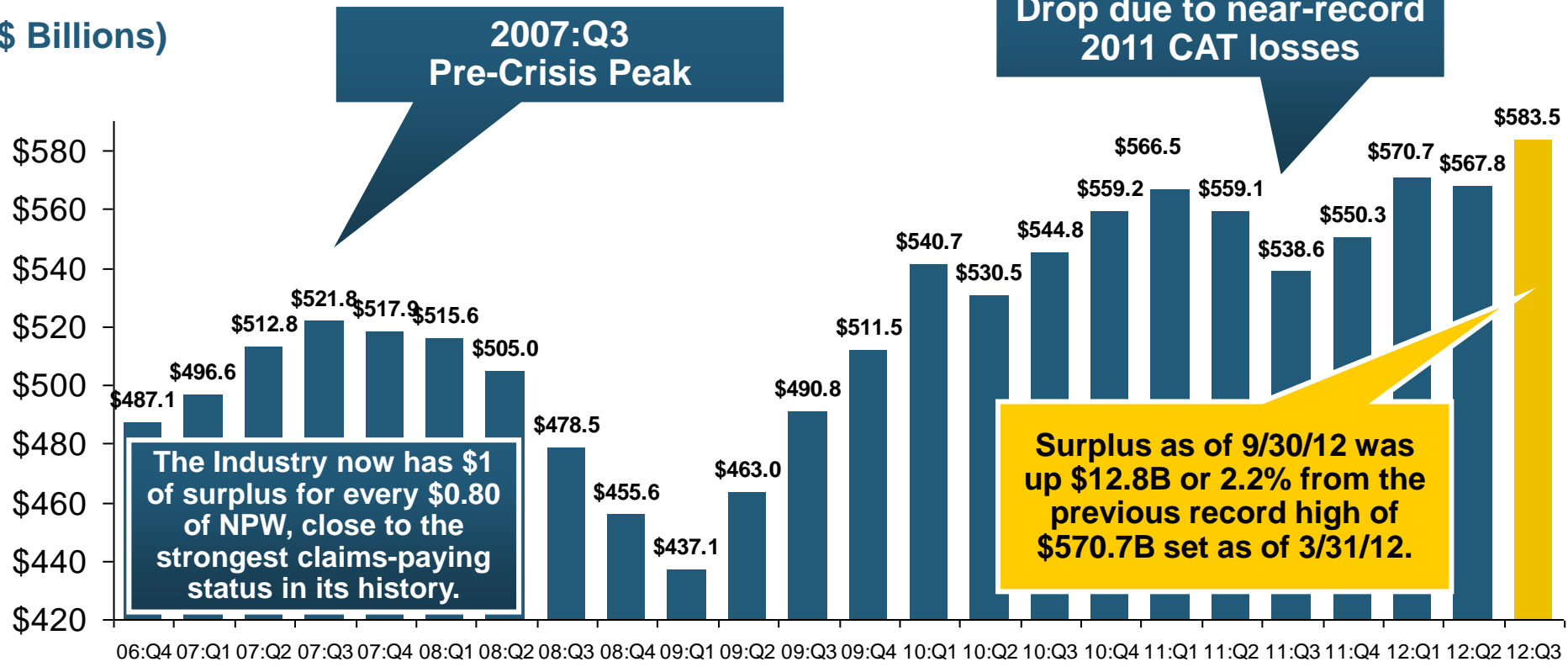
**The Premium-to-Surplus Ratio Stood at \$0.80:\$1 as of 9/30/12, A Near Record Low (at Least in Recent History)\***

\* As of 9/30/12.

Source: A.M. Best, ISO, Insurance Information Institute.

# Policyholder Surplus, 2006:Q4–2012:Q3

(\$ Billions)



The Industry now has \$1 of surplus for every \$0.80 of NPW, close to the strongest claims-paying status in its history.

Surplus as of 9/30/12 was up \$12.8B or 2.2% from the previous record high of \$570.7B set as of 3/31/12.

\*Includes \$22.5B of paid-in capital from a holding company parent for one insurer's investment in a non-insurance business in early 2010.

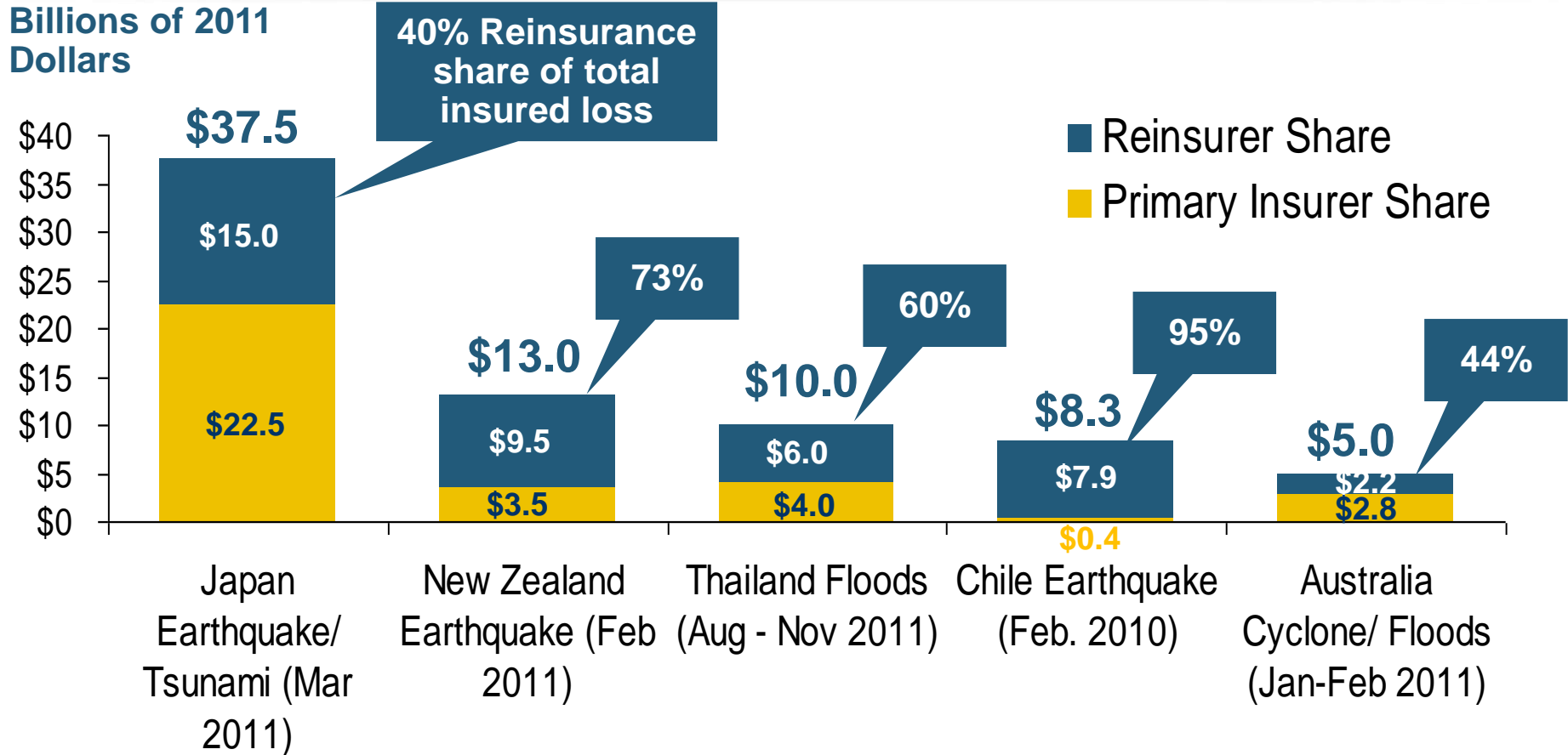
**The P/C Insurance Industry Both Entered and Emerged from the 2012 Hurricane Season Very Strong Financially. There is No Insurance Industry "Fiscal Cliff"**

## **3. REINSURANCE MARKET CONDITIONS**

**Record Global  
Catastrophes Activity is  
Pressuring Pricing**



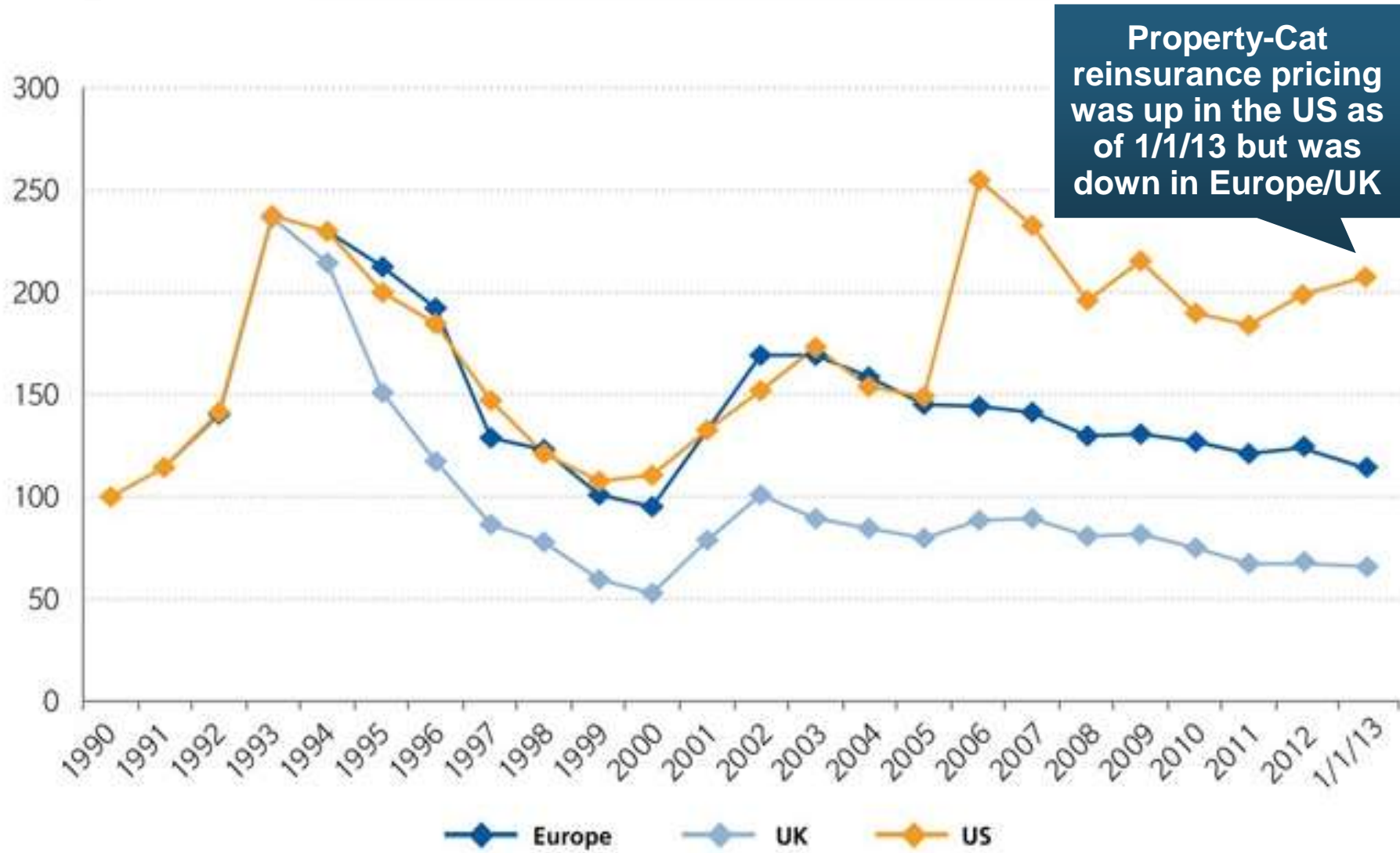
# Reinsurer Share of Recent Significant Market Losses



**Reinsurers Paid a High Proportion of Insured Losses Arising from Major Catastrophic Events Around the World in Recent Years**

Source: Insurance Information Institute from reinsurance share percentages provided in RAA, ABIR and CEA press release, Jan. 13, 2011.

# Regional Property Catastrophe Rate on Line Index, 1990—2013 (as of January 1)



Sources: Guy Carpenter; Insurance Information Institute.

## **4. RENEWED PRICING DISCIPLINE**

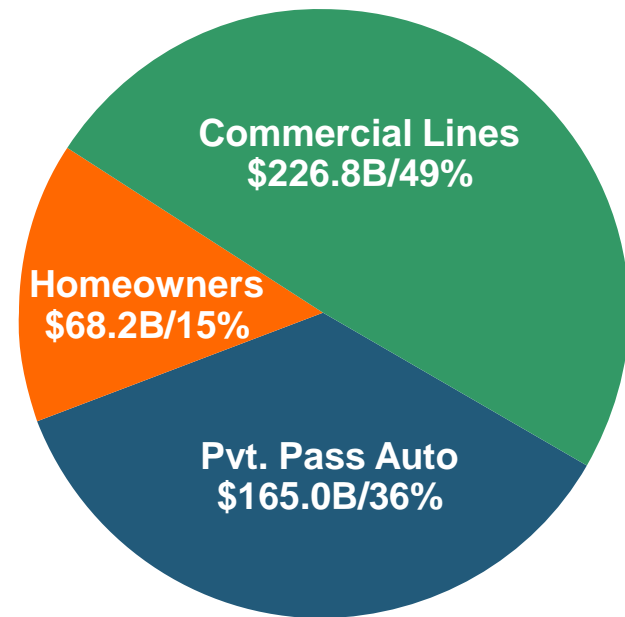
**Evidence of a Broad and  
Sustained Shift in Pricing**

# Distribution of Direct Premiums Written by Segment/Line, 2010

## Distribution Facts

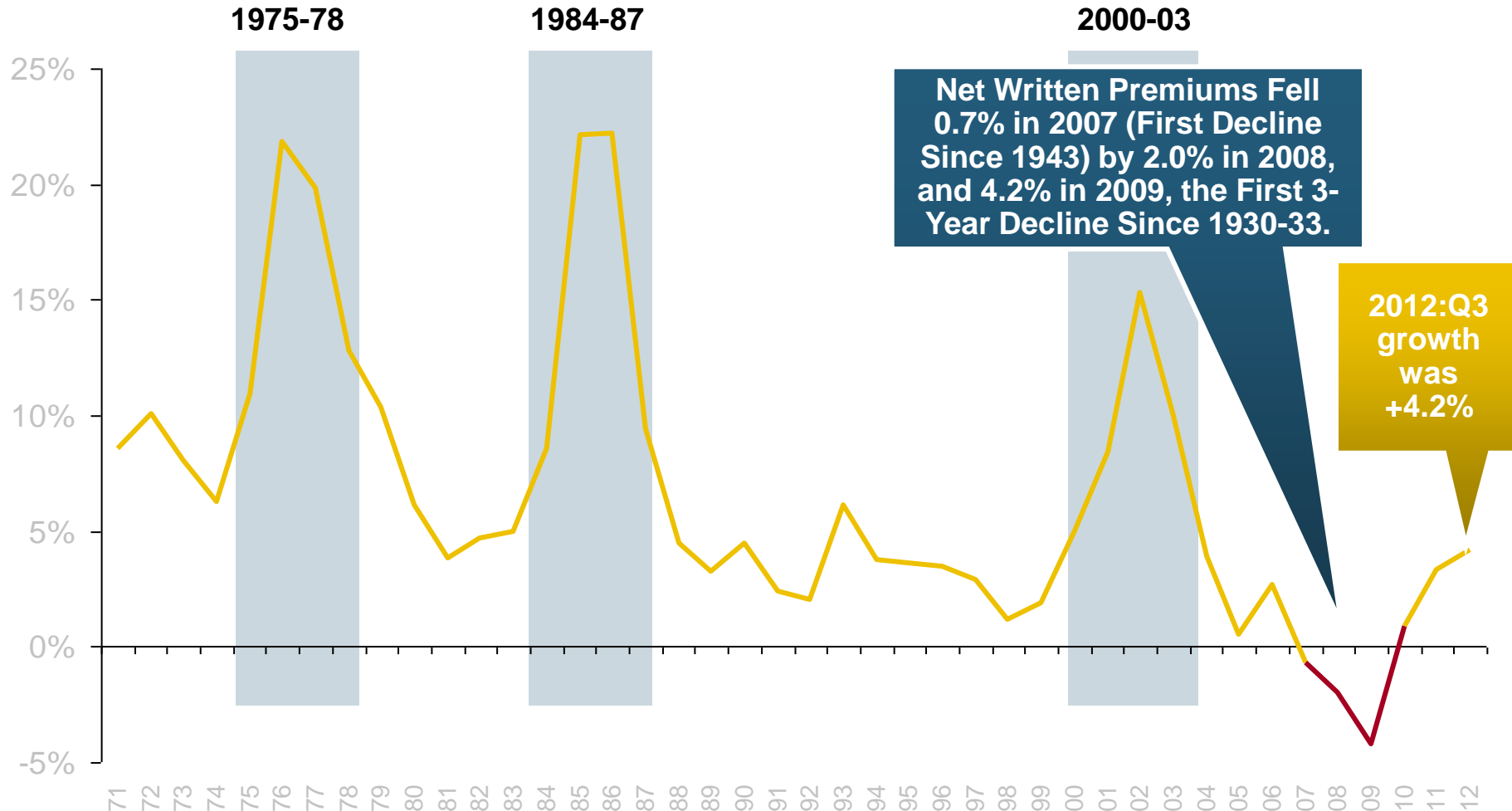
- Personal/Commercial lines split has been about 50/50 for many years; Personal Lines overtook Commercial Lines in 2010
- Pvt. Passenger Auto is by far the largest line of insurance and is currently the most important source of industry profits
- Billions of additional dollars in homeowners insurance premiums are written by state-run residual market plans

2010



# Net Premium Growth: Annual Change, 1971—2012:Q3

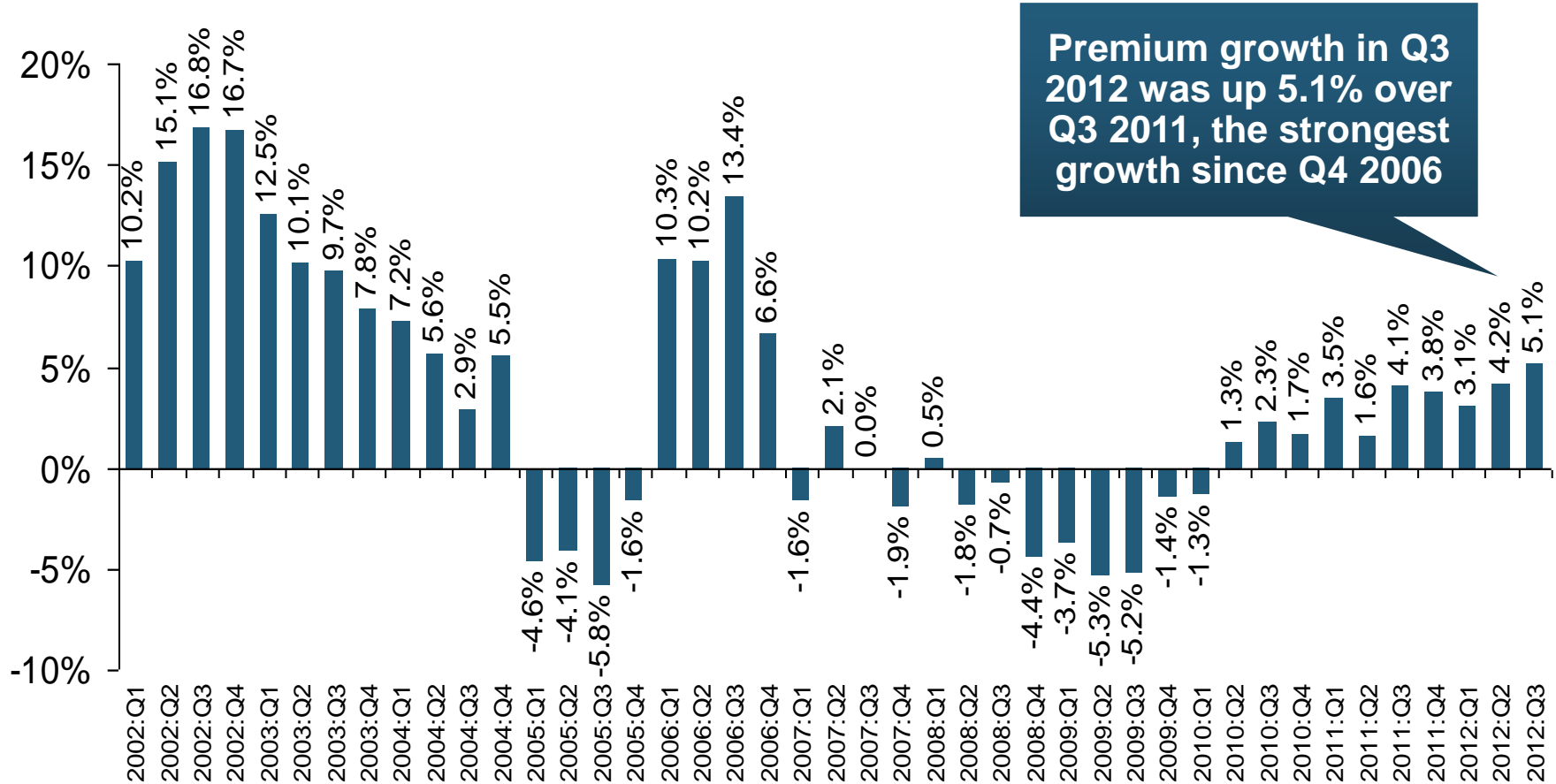
(Percent)



Shaded areas denote “hard market” periods

Sources: A.M. Best (historical and forecast), ISO, Insurance Information Institute.

# P/C Net Premiums Written: % Change, Quarter vs. Year-Prior Quarter

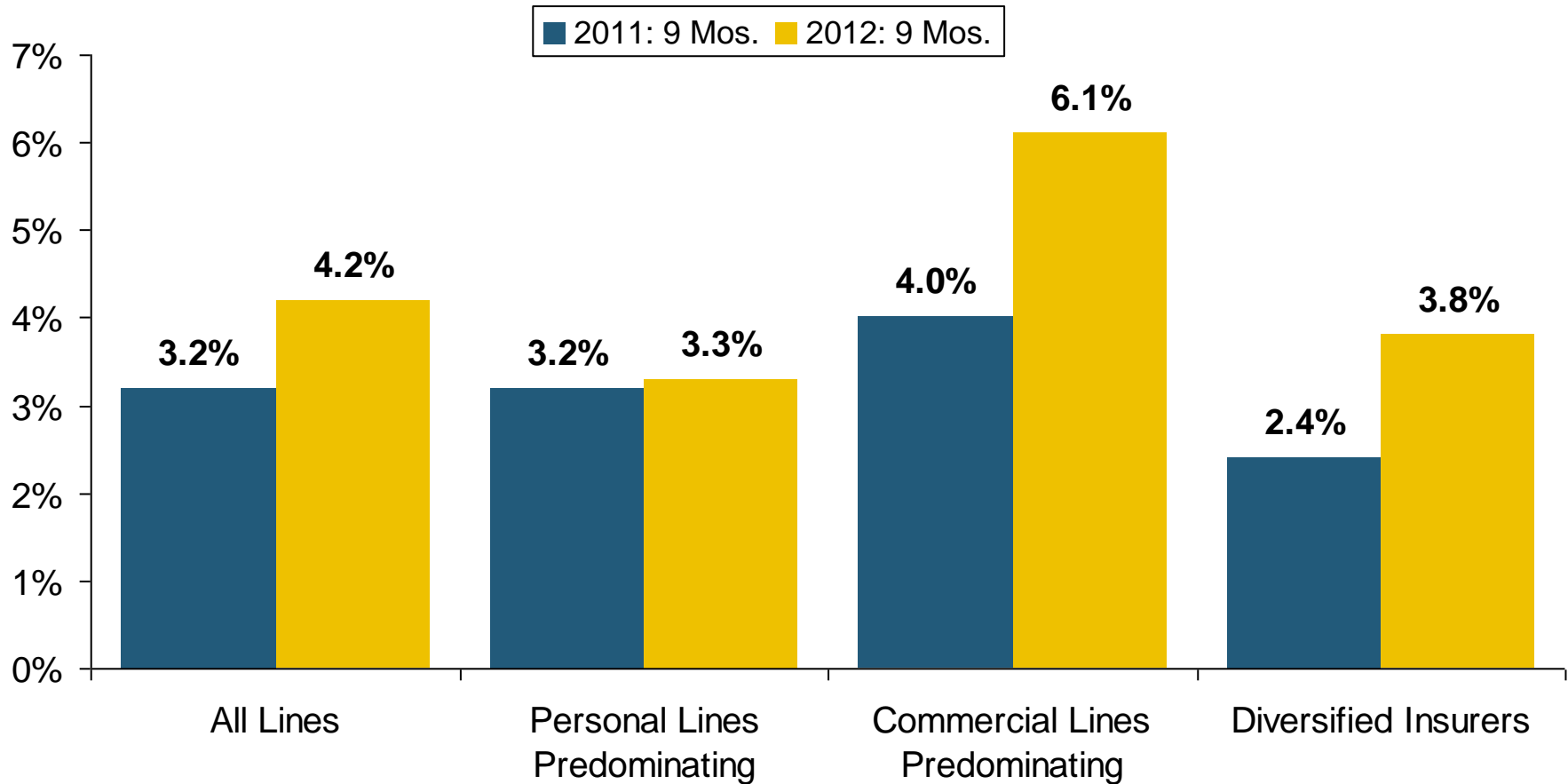


Premium growth in Q3 2012 was up 5.1% over Q3 2011, the strongest growth since Q4 2006

**Sustained Growth in Written Premiums (vs. the same quarter, prior year) Will Continue into 2013**

# Growth in Net Written Premium by Segment, 2012:9 Mos. vs. 2011:9 Mos.\*

(Percent)

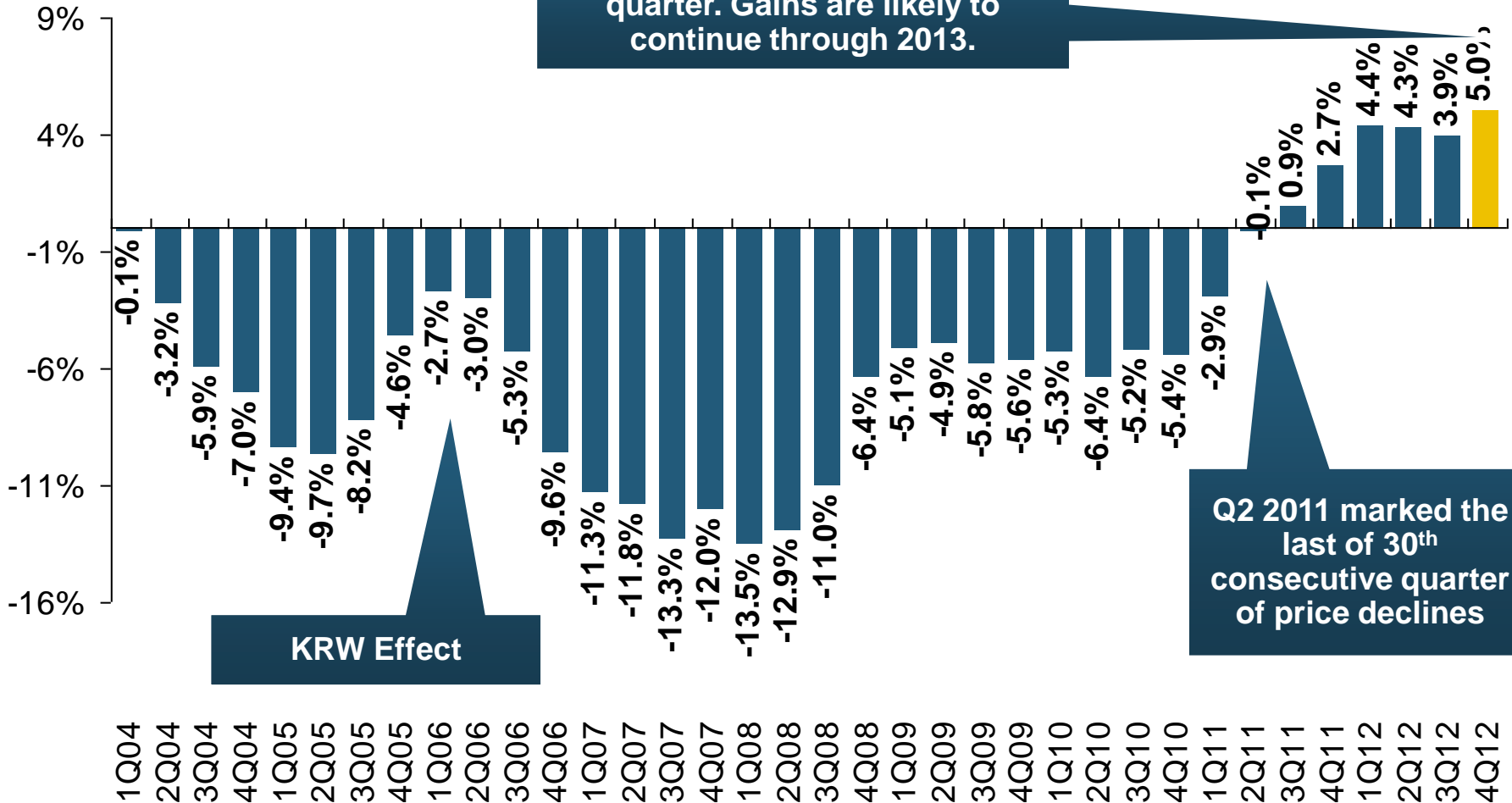


\*Excludes mortgage and financial guaranty insurers.

Source: ISO/PCI; Insurance Information Institute

# Average Commercial Rate Change, All Lines, (1Q:2004–4Q:2012)

(Percent)



Pricing as of Q4:2012 was positive for the 6<sup>th</sup> consecutive quarter. Gains are likely to continue through 2013.

KRW Effect

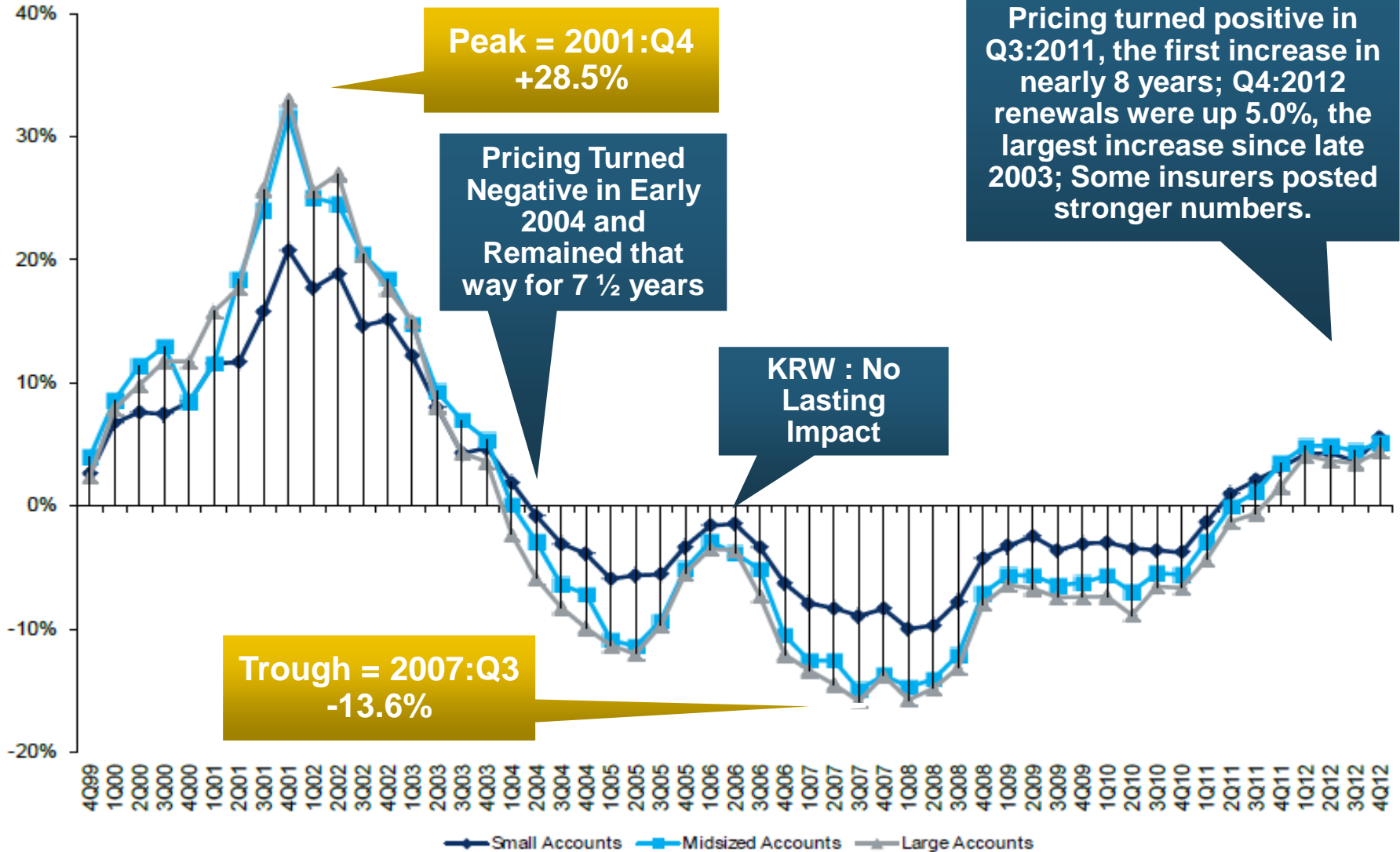
Q2 2011 marked the last of 30<sup>th</sup> consecutive quarter of price declines

Note: CIAB data cited here are based on a survey. Rate changes earned by individual insurers can and do vary, potentially substantially.  
 Source: Council of Insurance Agents & Brokers; Insurance Information Institute



# Change in Commercial Rate Renewals, by Account Size: 1999:Q4 to 2012:Q4

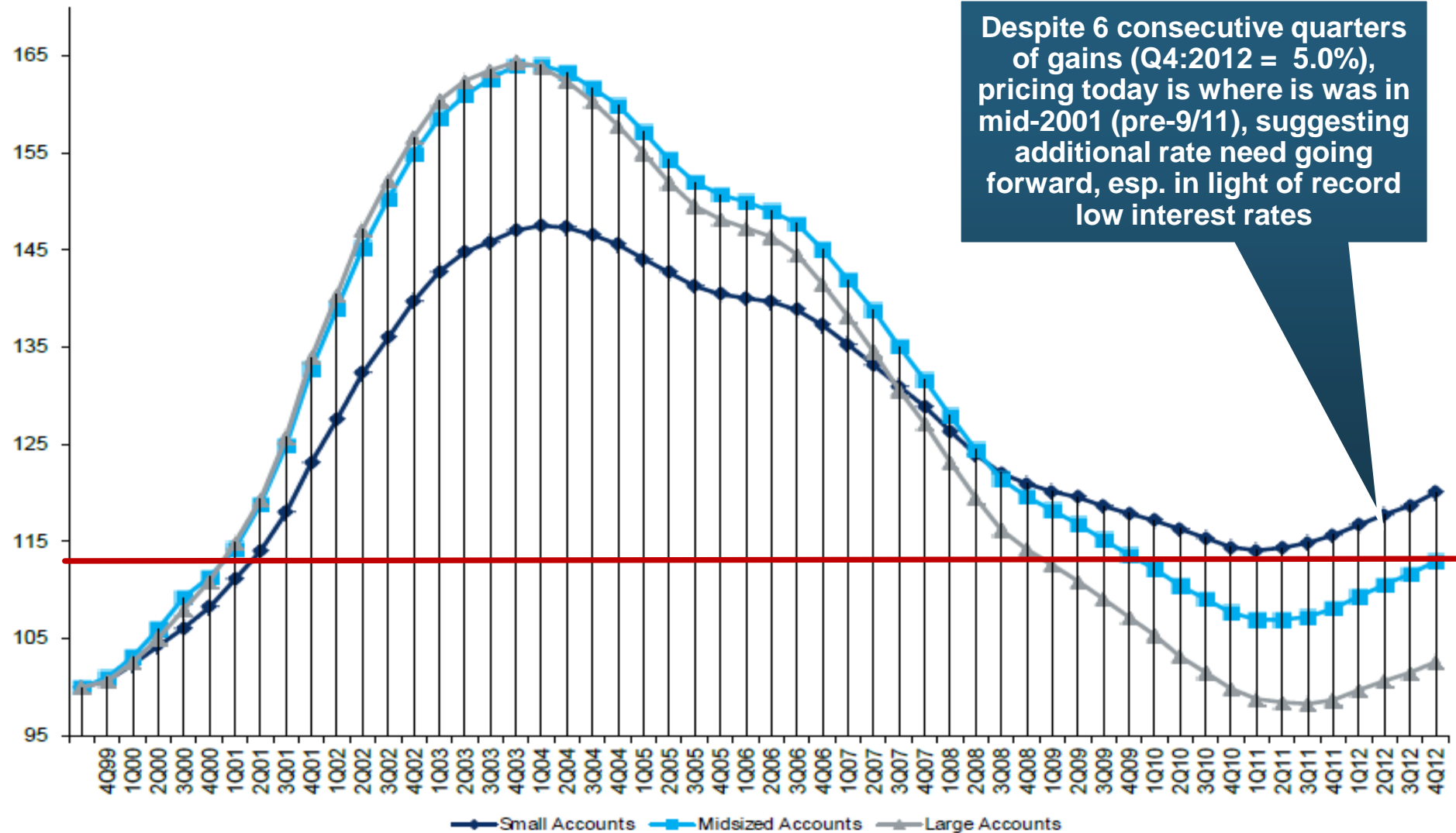
Percentage Change (%)



Note: CIAB data cited here are based on a survey. Rate changes earned by individual insurers can and do vary, potentially substantially.  
 Source: Council of Insurance Agents and Brokers; Barclay's Capital; Insurance Information Institute.

# Cumulative Qtrly. Commercial Rate Changes, by Account Size: 1999:Q4 to 2012:Q4

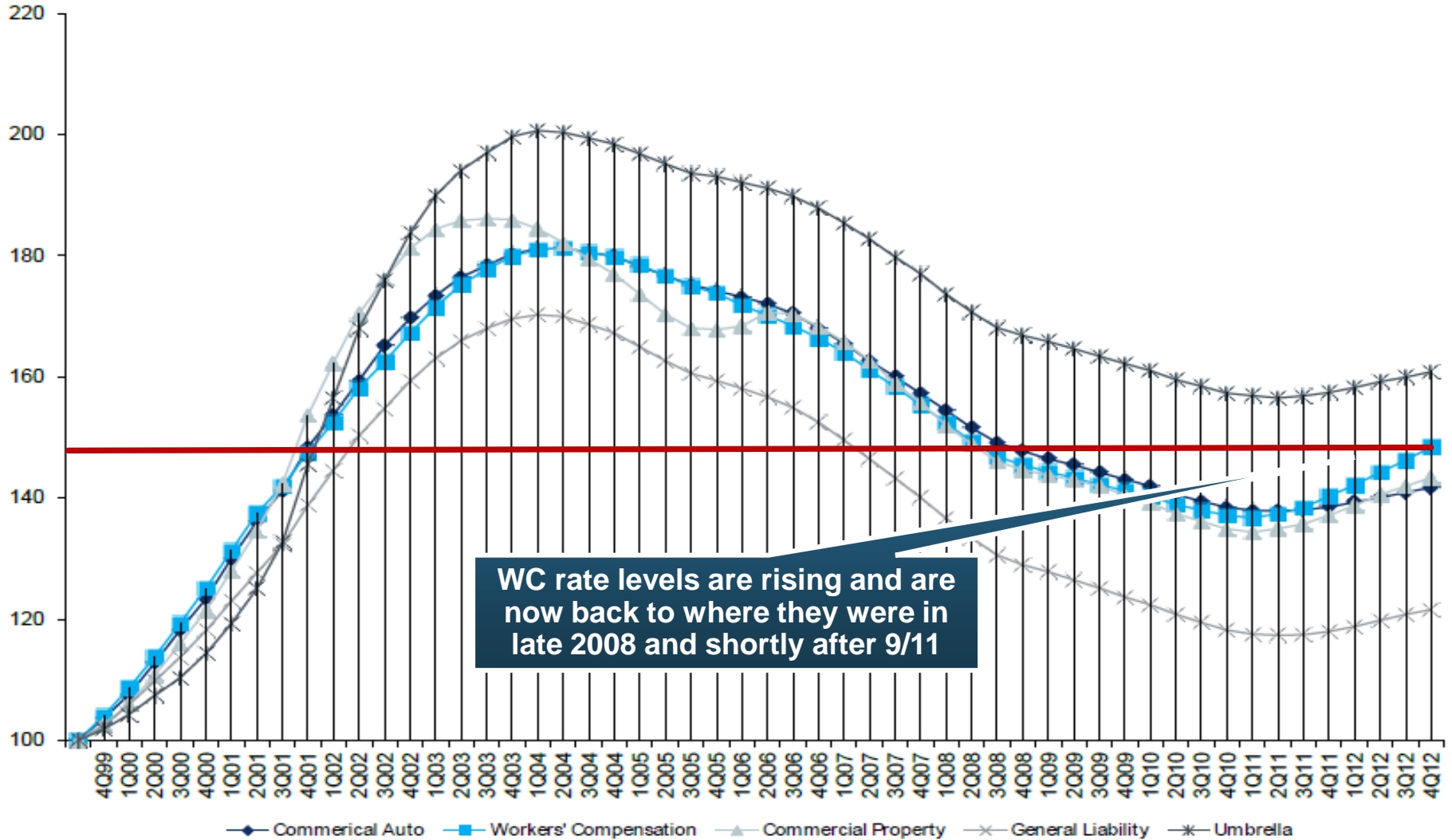
1999:Q4 = 100



Note: CIAB data cited here are based on a survey. Rate changes earned by individual insurers can and do vary, potentially substantially. Source: Council of Insurance Agents and Brokers; Barclay's Capital; Insurance Information Institute.

# Cumulative Qtrly. Commercial Rate Changes, by Line: 1999:Q4 to 2012:Q4

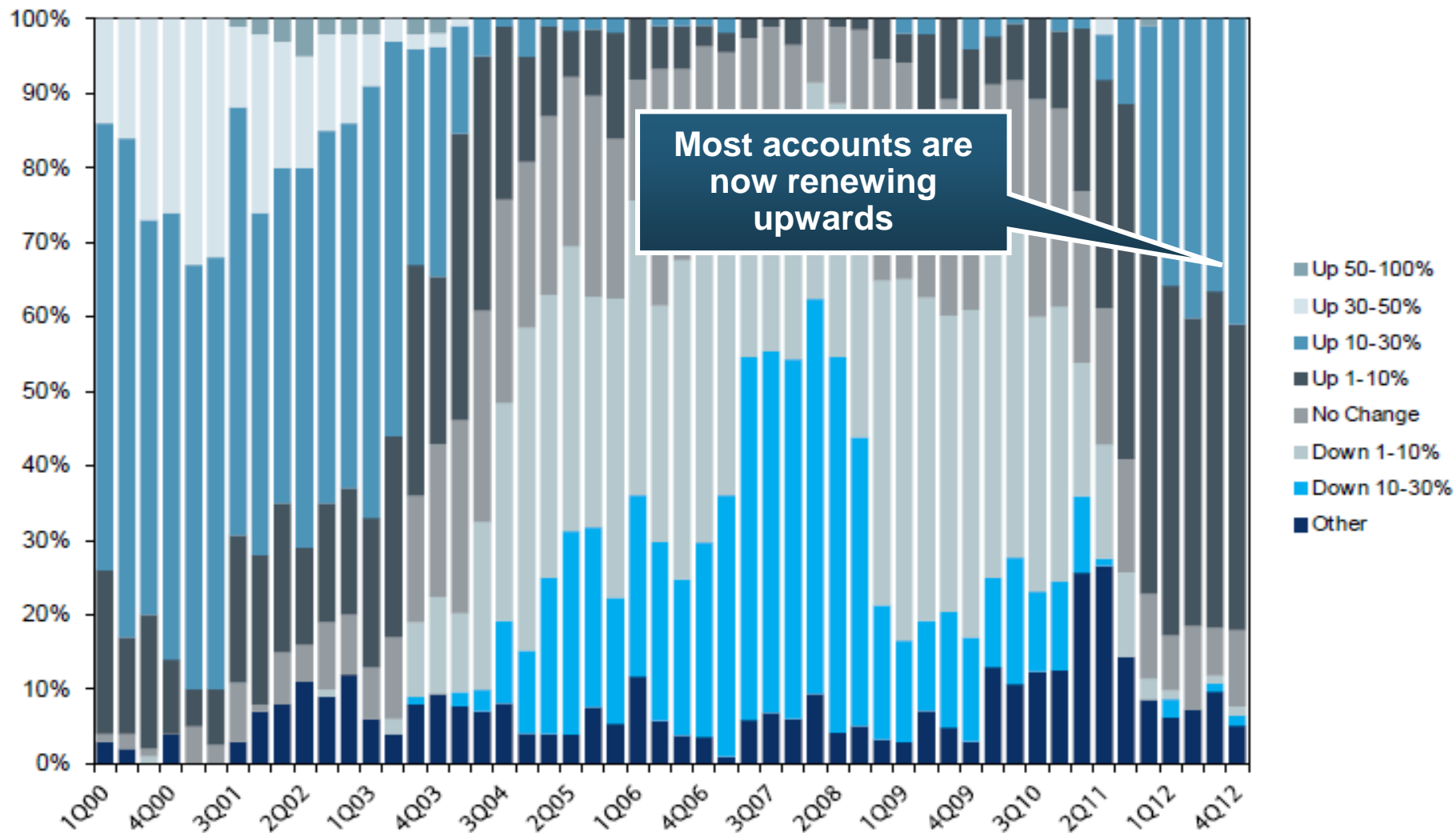
1999:Q4 = 100



Note: CIAB data cited here are based on a survey. Rate changes earned by individual insurers can and do vary, potentially substantially.  
 Source: Council of Insurance Agents and Brokers; Barclay's Capital; Insurance Information Institute.

# Workers Comp. Quarterly Rate Changes, by Line: 2000:Q1 to 2012:Q4

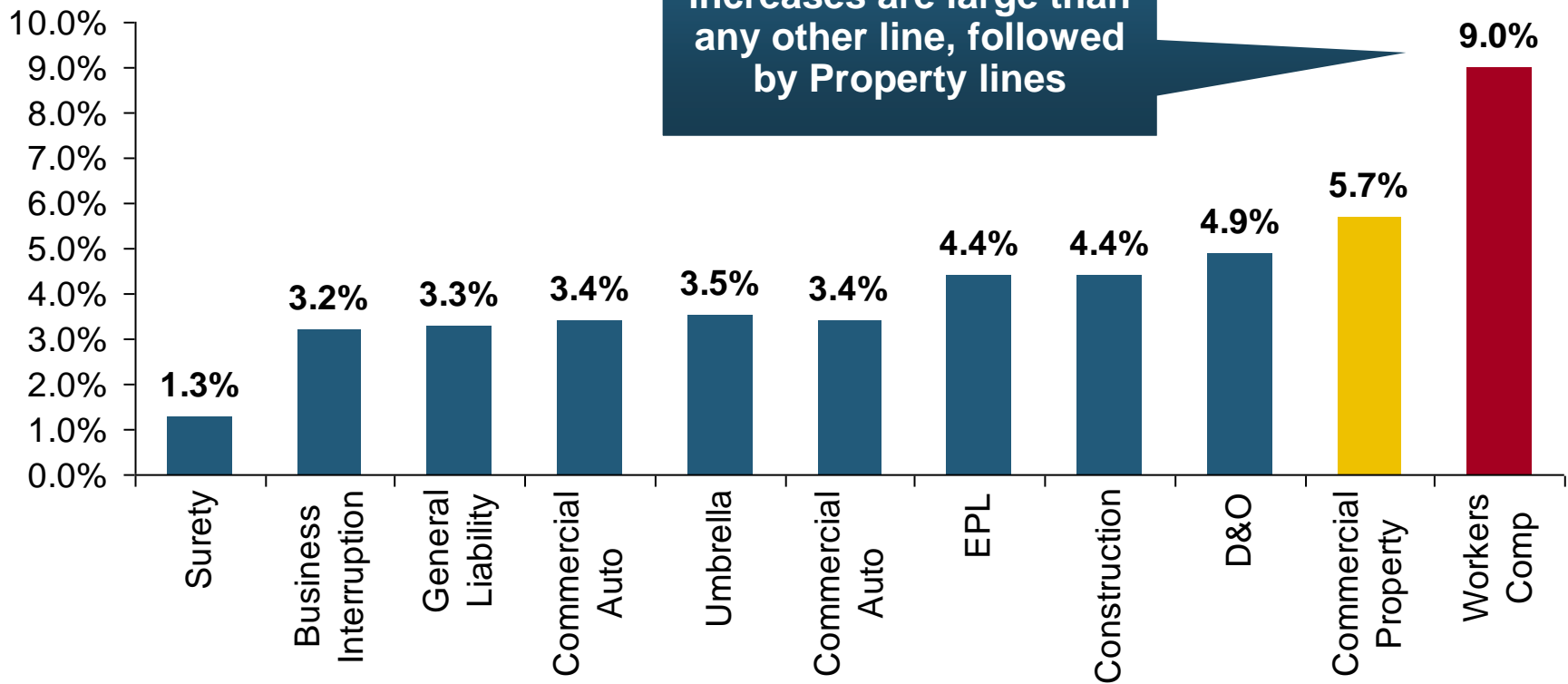
1999:Q4 = 100



Note: CIAB data cited here are based on a survey. Rate changes earned by individual insurers can and do vary, potentially substantially.  
 Source: Council of Insurance Agents and Brokers; Barclay's Capital; Insurance Information Institute.

# Change in Commercial Rate Renewals, by Line: 2012:Q4

## Percentage Change (%)

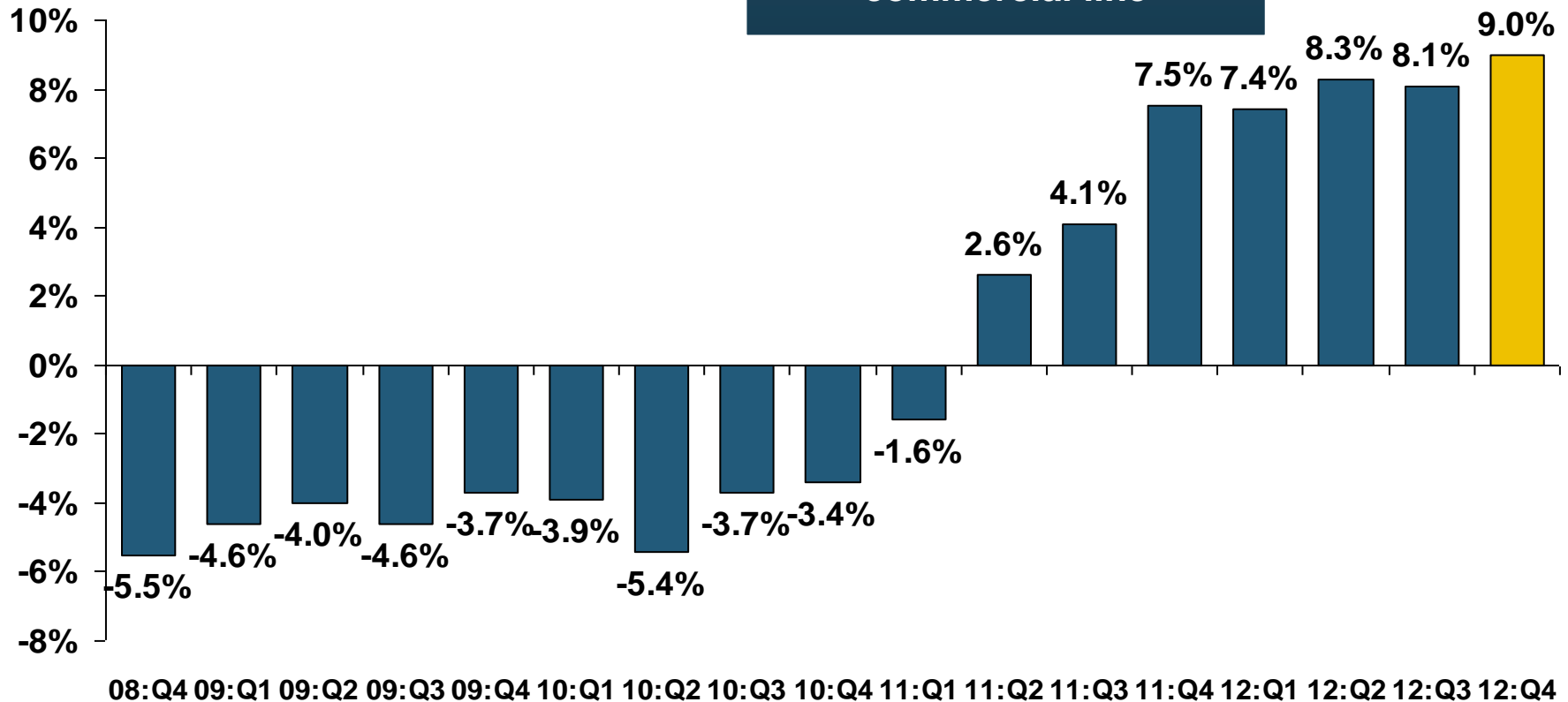


**Major Commercial Lines Renewed Uniformly Upward in Q4:2012 for the Sixth Consecutive Quarter; Property Lines & Workers Comp Leading the Way; Cat Losses and Low Interest Rates Provide Momentum Going Forward**

Note: CIAB data cited here are based on a survey. Rate changes earned by individual insurers can and do vary, potentially substantially.  
Source: Council of Insurance Agents and Brokers; Insurance Information Institute.

# Workers Comp Rate Changes, 2008:Q4 – 2012:Q4

(Percent Change)



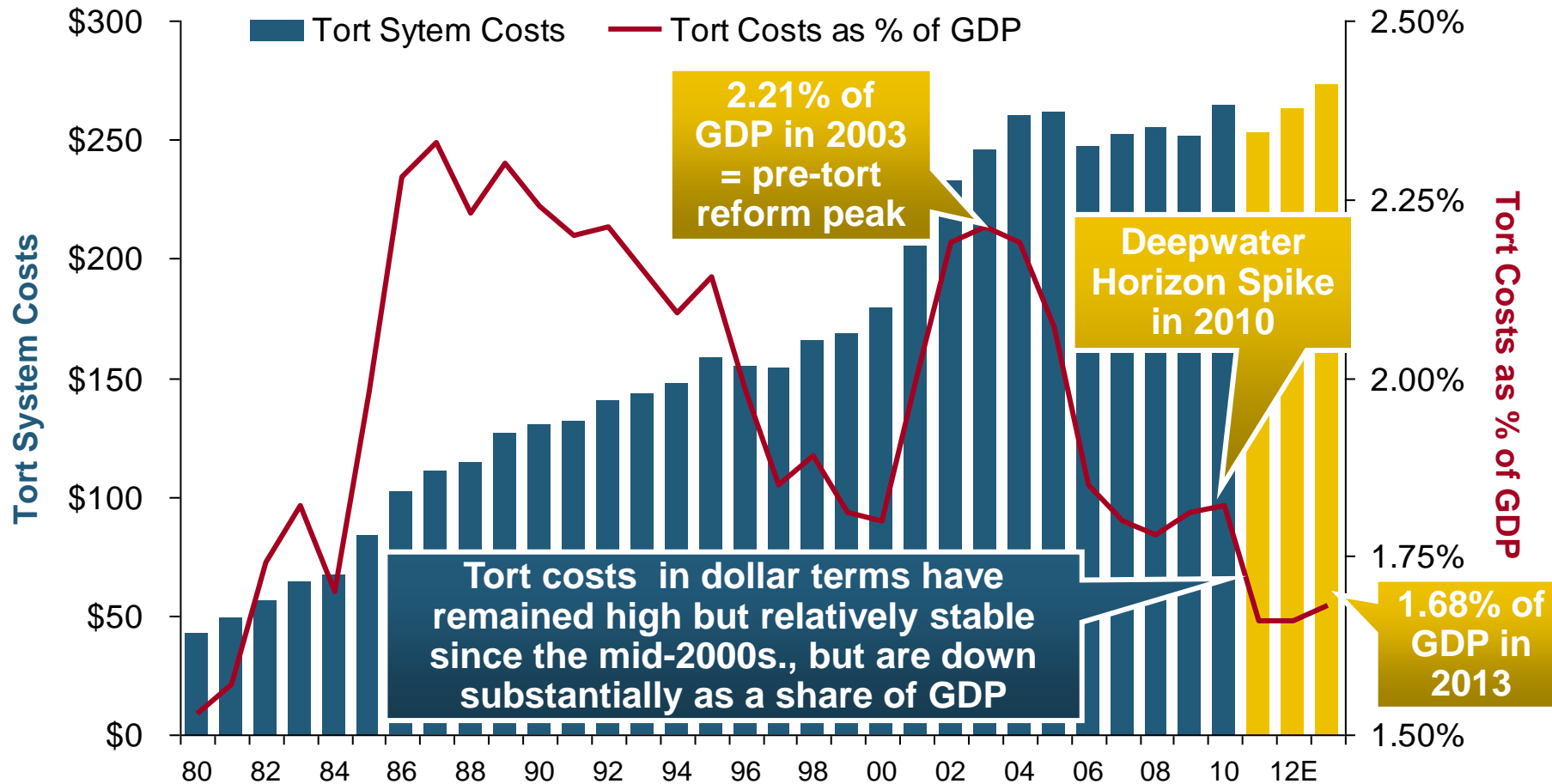
Note: CIAB data cited here are based on a survey. Rate changes earned by individual insurers can and do vary, potentially substantially.  
 Source: Council of Insurance Agents and Brokers; Information Institute.

# Shifting Legal Liability & Tort Environment

## Is the Tort Pendulum Swinging Against Insurers?

# Over the Last Three Decades, Total Tort Costs as a % of GDP Appear Somewhat Cyclical, 1980-2013E

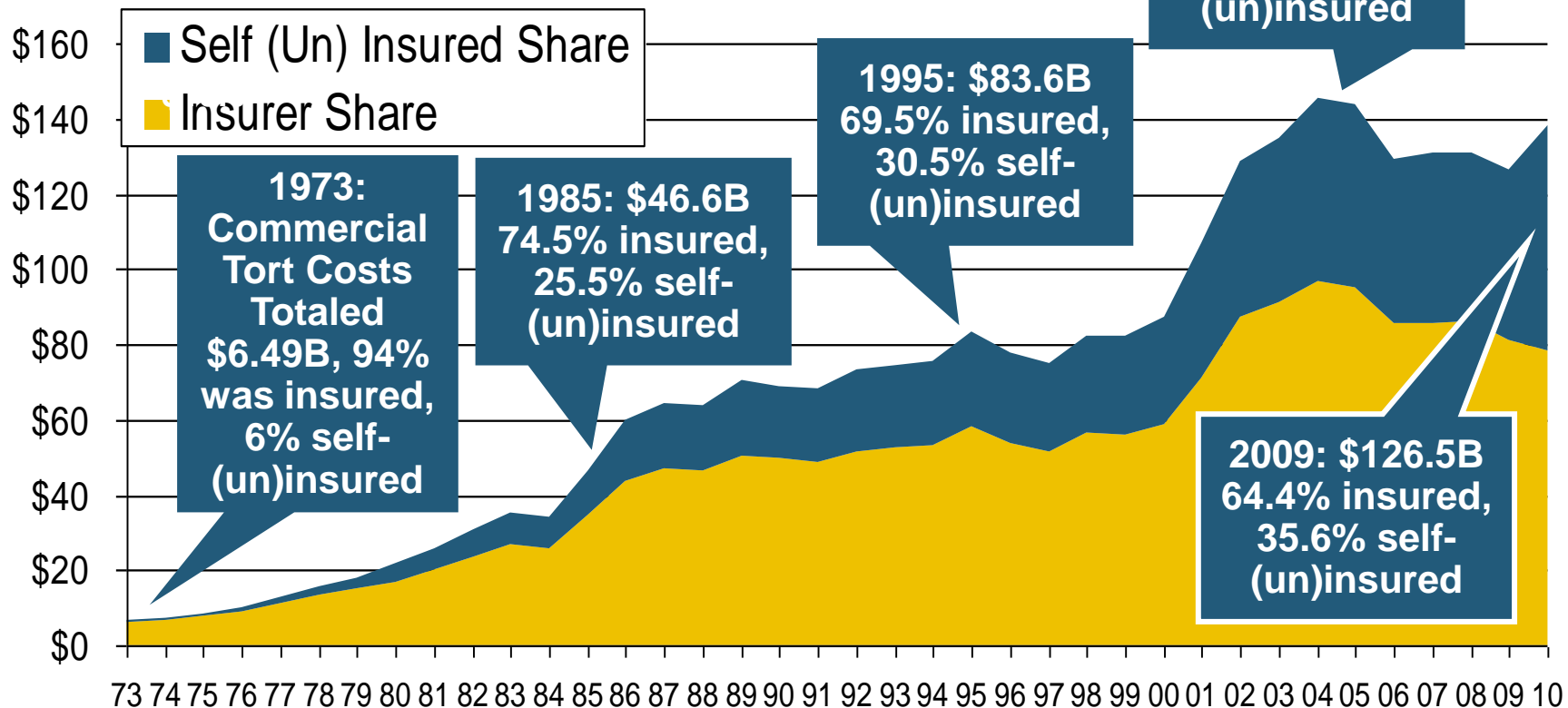
(\$ Billions)





# Commercial Lines Tort Costs: Insured vs. Self-(Un)Insured Shares, 1973-2010

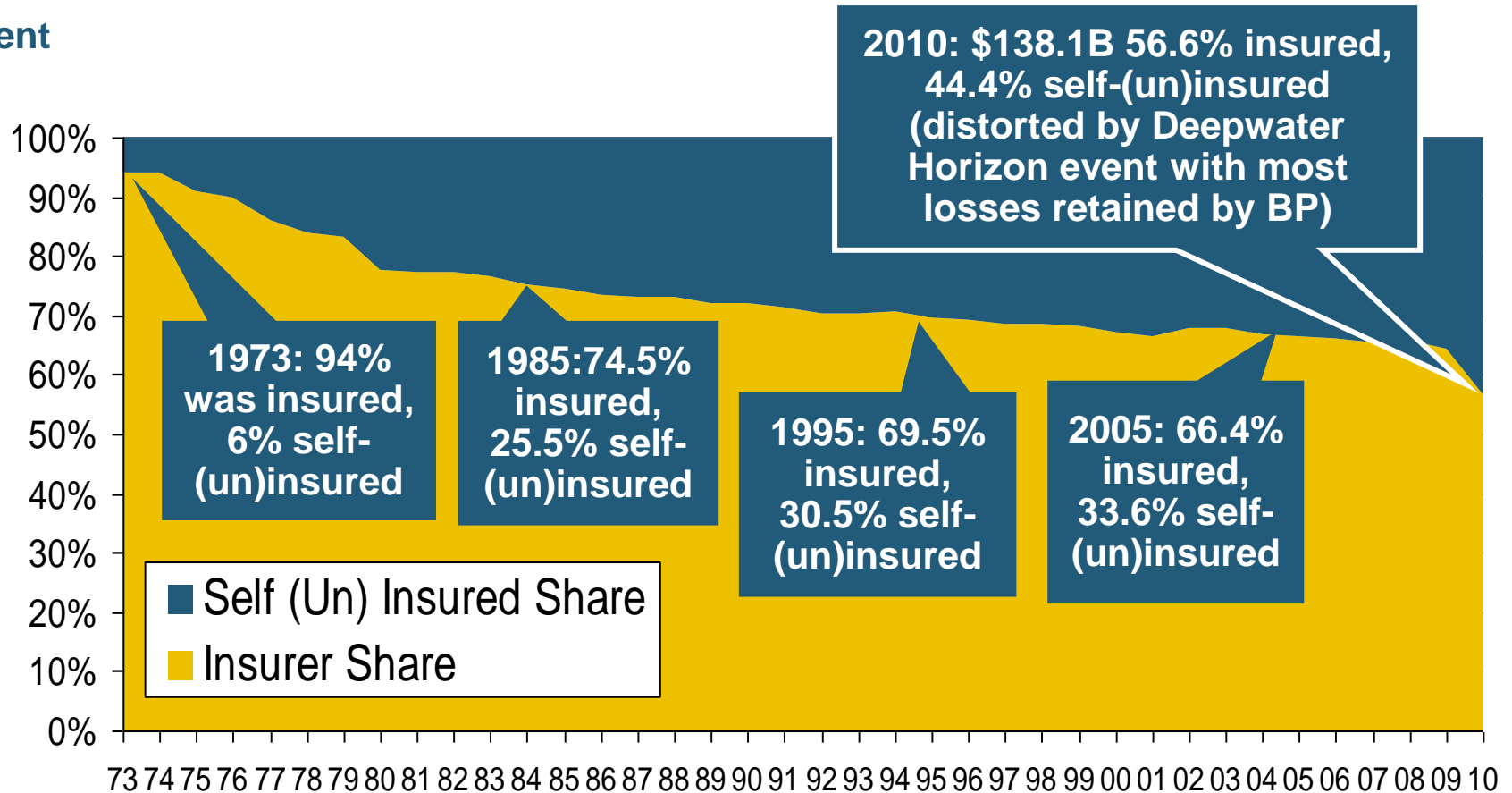
Billions of Dollars



**Tort Costs and the Share Retained by Risks Both Grew Rapidly from the mid-1970s to mid-2000s, When Tort Costs Began to Fall But Self-Insurance Shares Continued to Rise**

# Commercial Lines Tort Costs: Insured vs. Self-(Un)Insured Shares, 1973-2010

Percent



**The Share of Tort Costs Retained by Risks Has Been Steadily Increasing for Nearly 40 Years. This Trend Contributes Has Left Insurers With Less Control Over Pricing.**

# Business Leaders Ranking of Liability Systems in 2012

## Best States

1. Delaware
2. Nebraska
3. Wyoming
4. Minnesota
5. Kansas
6. Idaho
7. Virginia
8. North Dakota
9. Utah

### New in 2012

- Wyoming
- Minnesota
- Kansas
- Idaho

### Drop-offs

- Indiana
- Colorado
- Massachusetts
- South Dakota

## Worst States

41. Florida
42. Oklahoma
43. Alabama
44. New Mexico
45. Montana
46. Illinois
47. California
48. Mississippi
49. Louisiana
50. West Virginia

### Newly Notorious

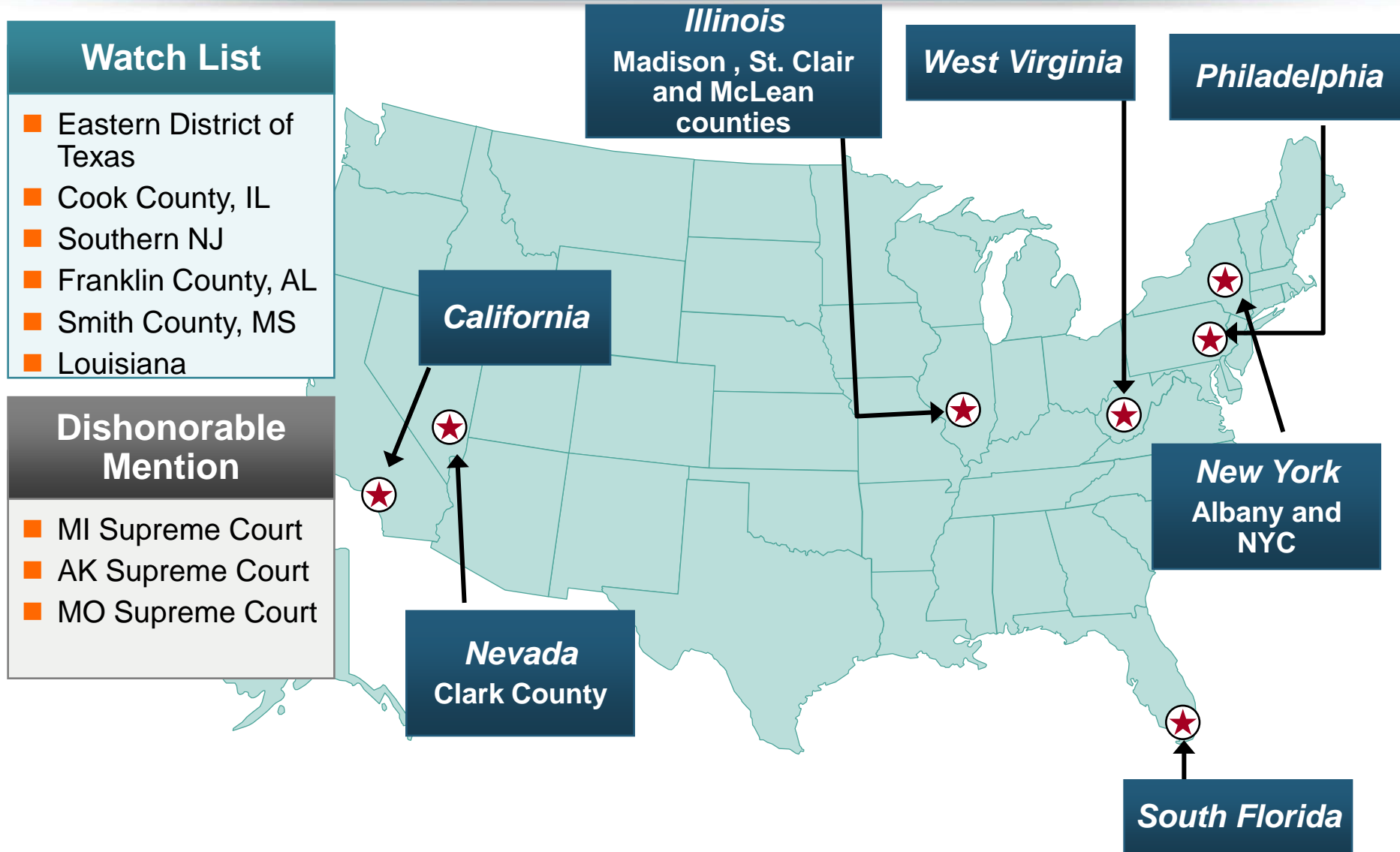
- Oklahoma

### Rising Above

- Arkansas

**10. Iowa**

# The Nation's Judicial Hellholes: 2011



## Insurance Information Institute Online:

**[www.iii.org](http://www.iii.org)**

*Thank you for your time  
and your attention!*

*Twitter: [twitter.com/bob\\_hartwig](https://twitter.com/bob_hartwig)*

*Download at: [www.iii.org/presentations](http://www.iii.org/presentations)*