



Catastrophes, Uncertainty and Insurance:

Overview & Outlook for 2012 & Beyond

M200 Meeting

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- **Review of Recent Events**
 - ◆ What in the World is Going On?
- **Summary of P/C Financial Performance**
- **Catastrophe Loss Developments & Trends**
 - ◆ Global
 - ◆ US
- **Will the Market Turn? Four Necessary Criteria:**
 - ◆ Underwriting Loss Trends
 - ◆ Capital/Capacity
 - ◆ Reinsurance Markets
 - ◆ Pricing Discipline
- **Other Contributing Factors to the Underwriting Cycle**
 - ◆ Investment Environment
 - ◆ Tort/Casualty Environment
 - ◆ Inflation
 - ◆ Economic Environment

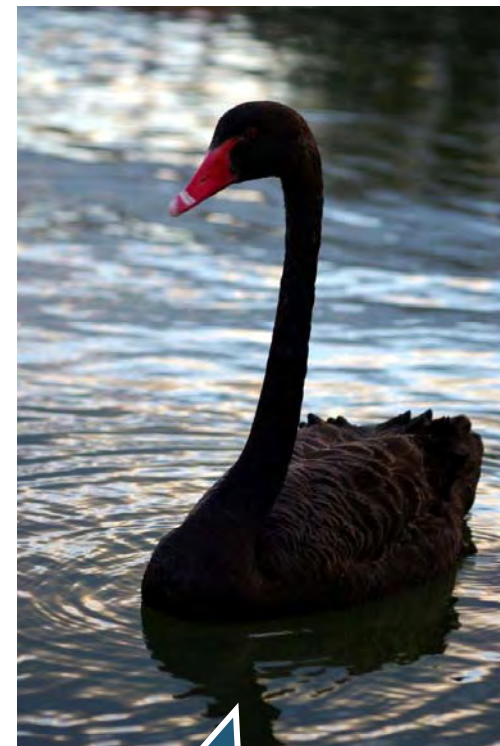
What in the World Is Going On?

**Is the World Becoming a
Riskier Place?**

***What Are the Implications for
Insurance and Risk Management?***

Uncertainty, Risk and Fear Abound

- **Global Economic Slowdown**
- **US Debt and Budget Crisis and S&P Downgrade**
- **Echoes of the Financial Crisis**
- **Housing Crisis**
- **Persistently High Unemployment**
- **European Sovereign Debt, Bank & Currency Crises**
- **Japan, New Zealand, Turkey, Haiti, Chile Earthquakes**
- **Nuclear Fears**
- **Record Tornado, Flooding in the US, Wildfires**
- **Cyber Attacks**
- **Manmade Disasters (e.g., Deepwater Horizon)**
- **Resurgent Terrorism Risk (e.g., Bin Laden Killing)**
- **Political Upheaval in the Middle East**
- **Inflation/Deflation**
- **Runaway Energy & Commodity Prices**
- **Era of Fiscal Austerity**
- **Reshuffling the Global Economic Deck**
- **China Becomes #2 Economy in the World**



Are “Black Swans”
everywhere or
does it just seem
that way?

Impacts on P/C Insurers of S&P's Downgrade of US Sovereign Debt

- **S&P Downgrade of US Debt Will Have Little Practical Impact**
 - ◆ Solvency, liquidity, claims paying capacity all unaffected
 - ◆ US sovereign debt accounts for 6% (\$80B out of \$1.3 trillion) in invested assets
- **Investors Will Continue to View US Treasury Securities as the Safest Investment in the World**
 - ◆ Other bond raters (Moody's, Fitch) affirmed top credit ratings for US
 - ◆ US bond yields *fell* in the days after S&P issued its initial warning
 - ◆ Evidence suggests that investors' asset of choice during "flight to safety" remains US debt
- **Risk Charge/Weights for US Debt Held by Finl. Firms Won't Change**
 - ◆ Federal bank regulators have already stated risk weights won't change
 - ◆ Extremely unlikely state insurance regulators would do anything different
 - ◆ NAIC (Aug. 7) "*There is no impact on insurer investments in U.S. government and government-related securities from the actions recently taken by the rating agencies. Risk-based capital and asset valuation reserves are unaffected.*"
- **Interest Rates on US Debt Unlikely to Rise Due to Downgrade**
 - ◆ Insurers should see little or no need to mark down value of bonds
- **Market for US Debt Will Remain Largest & Most Liquid in the World**
 - ◆ Downgrade poses no liquidity or solvency issues

What is Going On in the US and Global Financial Markets?

- **S&P Downgrade Poured Gasoline on a Fire that Was Already Burning**
 - ◆ Downgrade didn't tell us anything we didn't already know about US finances
- 1. **Realization that US Economy is Slowing**
 - ◆ Q1 GDP growth revised downward to 0.4%; Q2 growth was just 1.0%
 - ◆ Job growth has been anemic for several months and unemployment remains high at 9.1% in August
 - ◆ Stock market sell-off was driven by fear and technical factors (e.g., margin calls, hedge fund mass selling)
- 2. **Need for a More Comprehensive Solution to Europe's Debt Problems**
 - ◆ Solution developed for Greece, Italy, Spain, Ireland may be too small
 - ◆ Difficulties in managing multinational institutions and economic policies
 - ◆ ECB and individual member EU countries not all on same page
 - ◆ Solution: Unified strategy similar to TARP; Monetary easing
- 3. **View that Washington is Dysfunctional and "Rudderless"**
 - ◆ Lack of coherent, consistent medium and long term plan to deal with basic structural issues in the US economy (debt, taxes, employment, regulation, etc.)
- 4. **Economic Slowdown in Emerging Markets**
 - ◆ China, other economies less able to stimulate global economy than in 2008

Déjà Vu? Lehman II?

Is This 2008 All Over Again?

Why Today is Not 2008 All Over Again

- The Situation Today is Very, Very Different from 2008
- Credit Markets Are Not Seizing; Some Contraction in Europe
- Bank Balance Sheets Are in Much Stronger Shape
 - ◆ Capital up, charge offs falling
- We Will Not Experience the Collapses/Near Collapses Like in 2008
 - ◆ No repeat of Lehman, AIG, Washington Mutual, Wachovia...
- Some Additional Regulatory Controls Are Now Place

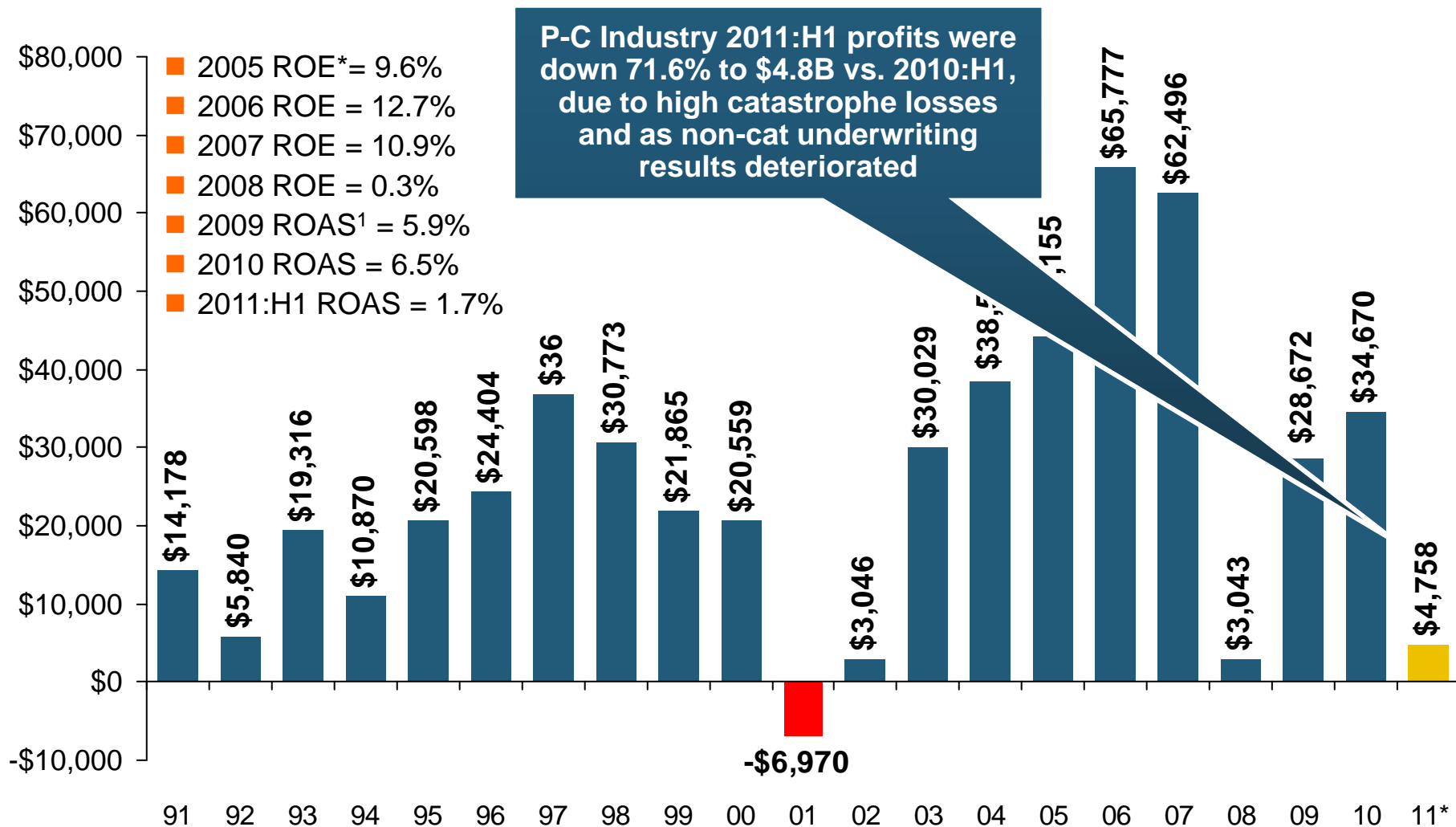
What Would Be Helpful Now?

- Solution to European Bank/Sovereign Debt Problem,
- Long-Term Fiscal and Monetary Policy Direction
- Fed on Aug. 9 stated rates would remain low “*at least through mid-2013*”
 - ◆ This is not only a signal that borrowing costs will remain low over an extended period of time and that inflation will remain muted; Also tells investors that they’ll need to take on risk in order to earn returns in the market. Should be bullish for stocks.
 - ◆ Congress and the Administration need to remove regulatory and tax uncertainty ASAP and drive a pro-growth agenda

P/C Insurance Industry Financial Overview

**Profit Recovery Will Be Set
Back by High CATs, Low
Interest Rates, Diminishing
Reserve Releases**

P/C Net Income After Taxes 1991–2011:H1 (\$ Millions)



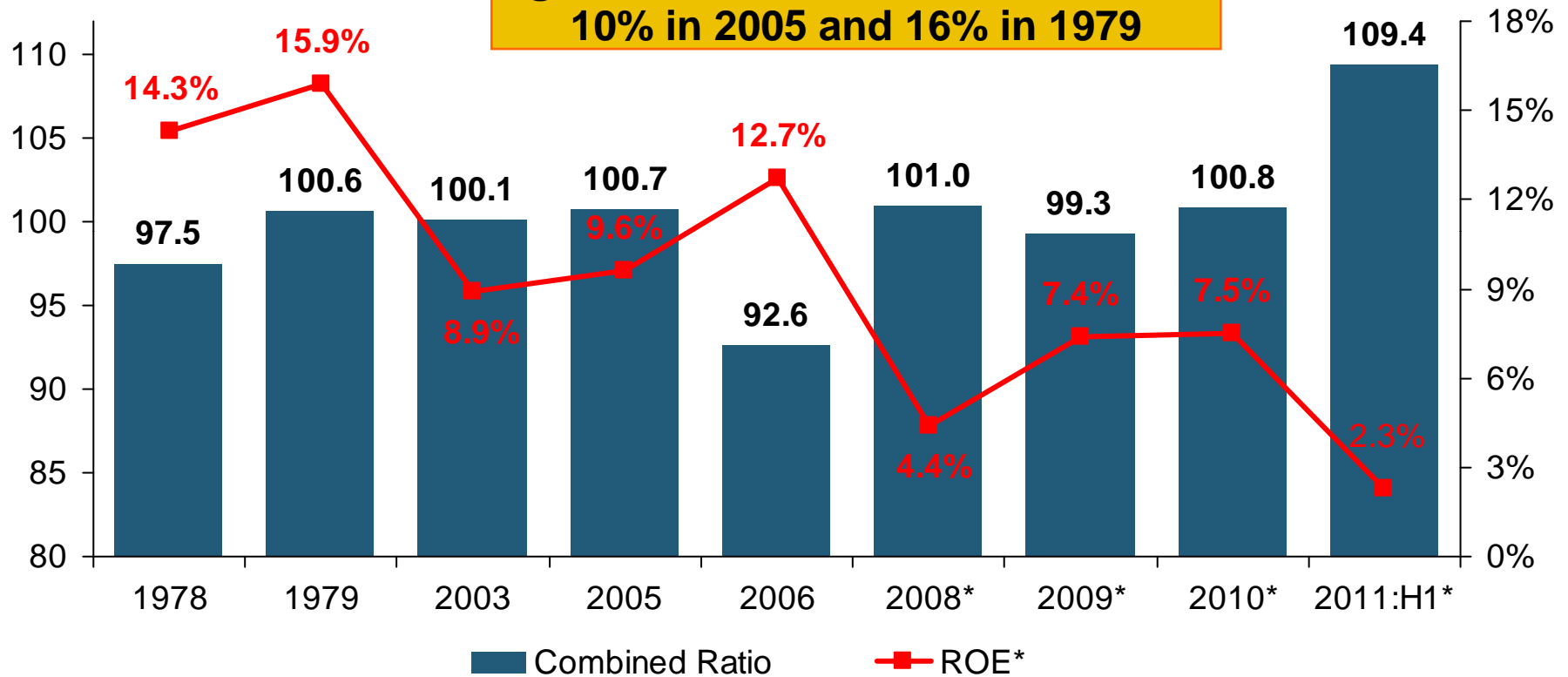
* ROE figures are GAAP; ¹Return on avg. surplus. Excluding Mortgage & Financial Guaranty insurers yields a 2.3% ROAS for 2011:H1, 7.5% for 2010 and 7.4% for 2009.

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 generated ~7.5% ROE in 2009/10, 10% in 2005 and 16% in 1979

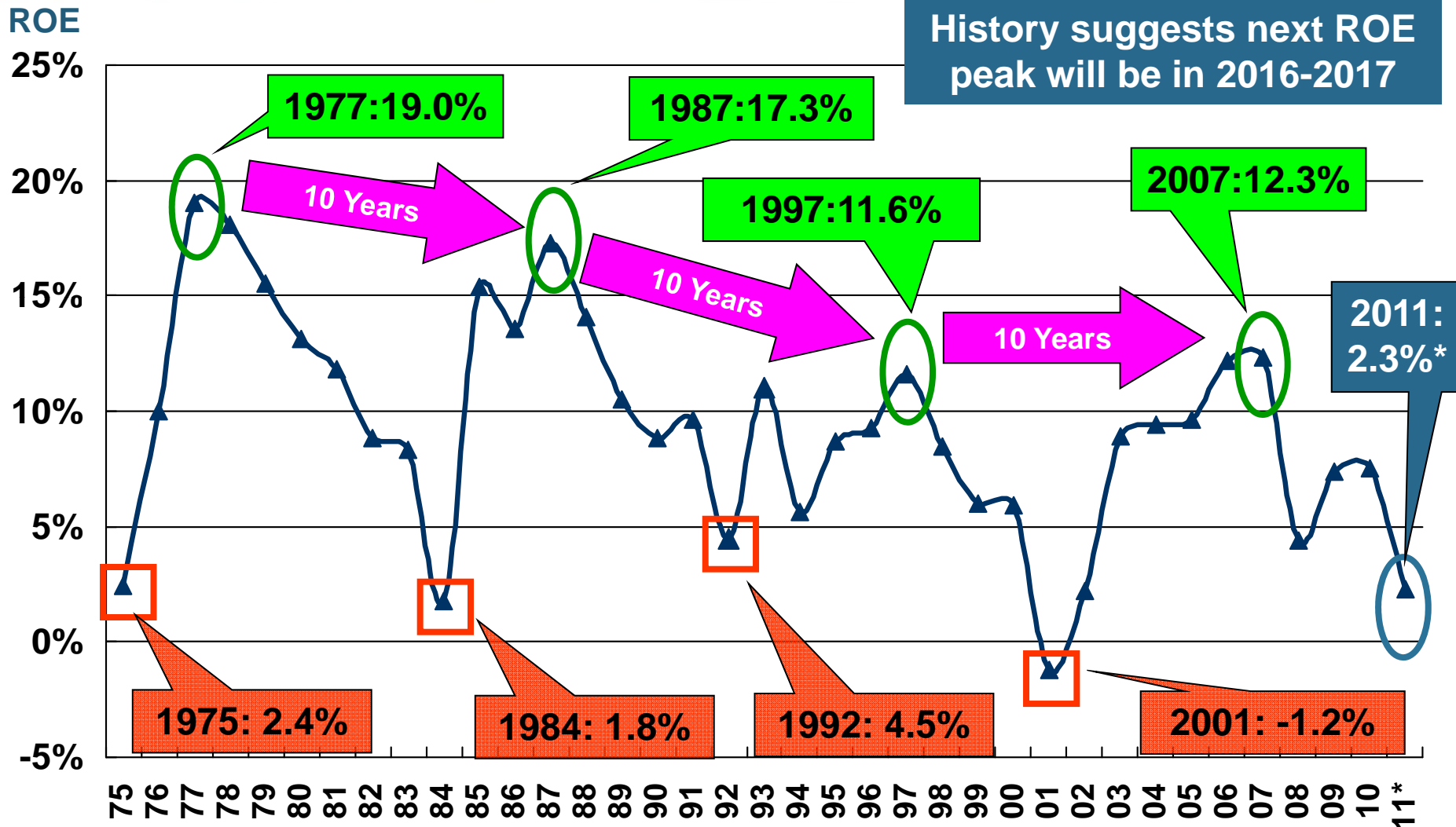


Combined Ratios Must Be Lower in Today's Depressed Investment Environment to Generate Risk Appropriate ROEs

* 2009 and 2010 figures are return on average statutory surplus. 2008 -2011 figures exclude mortgage and financial guaranty insurers. 2011H1 combined ratio including M&FG insurers is 110.5 , ROAS = 2.3%.

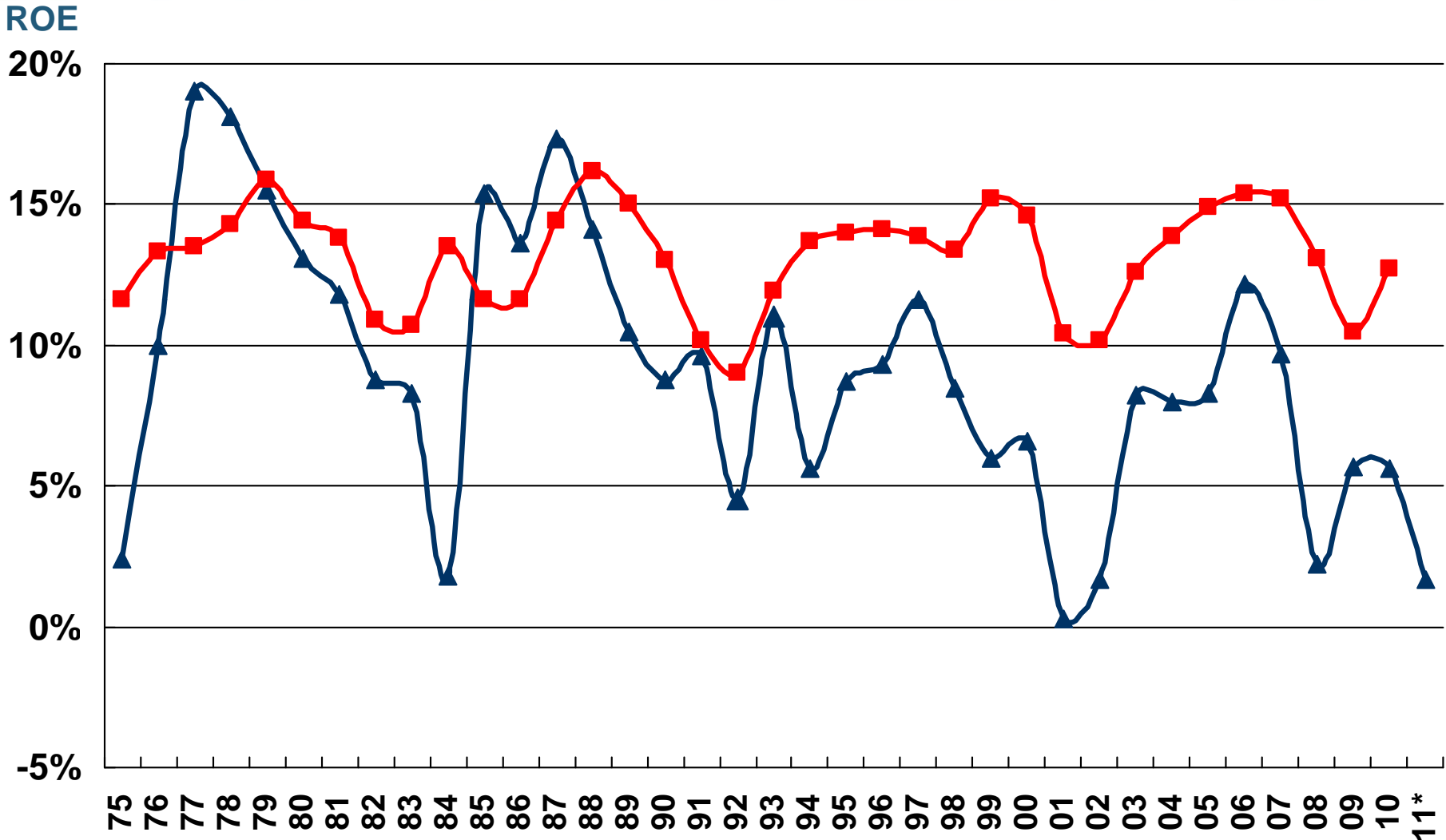
Source: Insurance Information Institute from A.M. Best and ISO data.

Profitability Peaks & Troughs in the P/C Insurance Industry, 1975 – 2011*



*Profitability = P/C insurer ROEs are I.I.I. estimates. 2011 figure is an estimate based on annualized ROAS for H1 data.
 Note: Data for 2008-2011 exclude mortgage and financial guaranty insurers. For 2011:H1 ROAS = 1.7% including M&FG.
 Source: Insurance Information Institute; NAIC, ISO, A.M. Best.

P/C Insurance Industry ROE vs. Fortune 500, 1975 – 2011*



For 2011:H1 ROAS.
 Source: Insurance Information Institute; NAIC, ISO.



Catastrophe Loss Developments and Trends

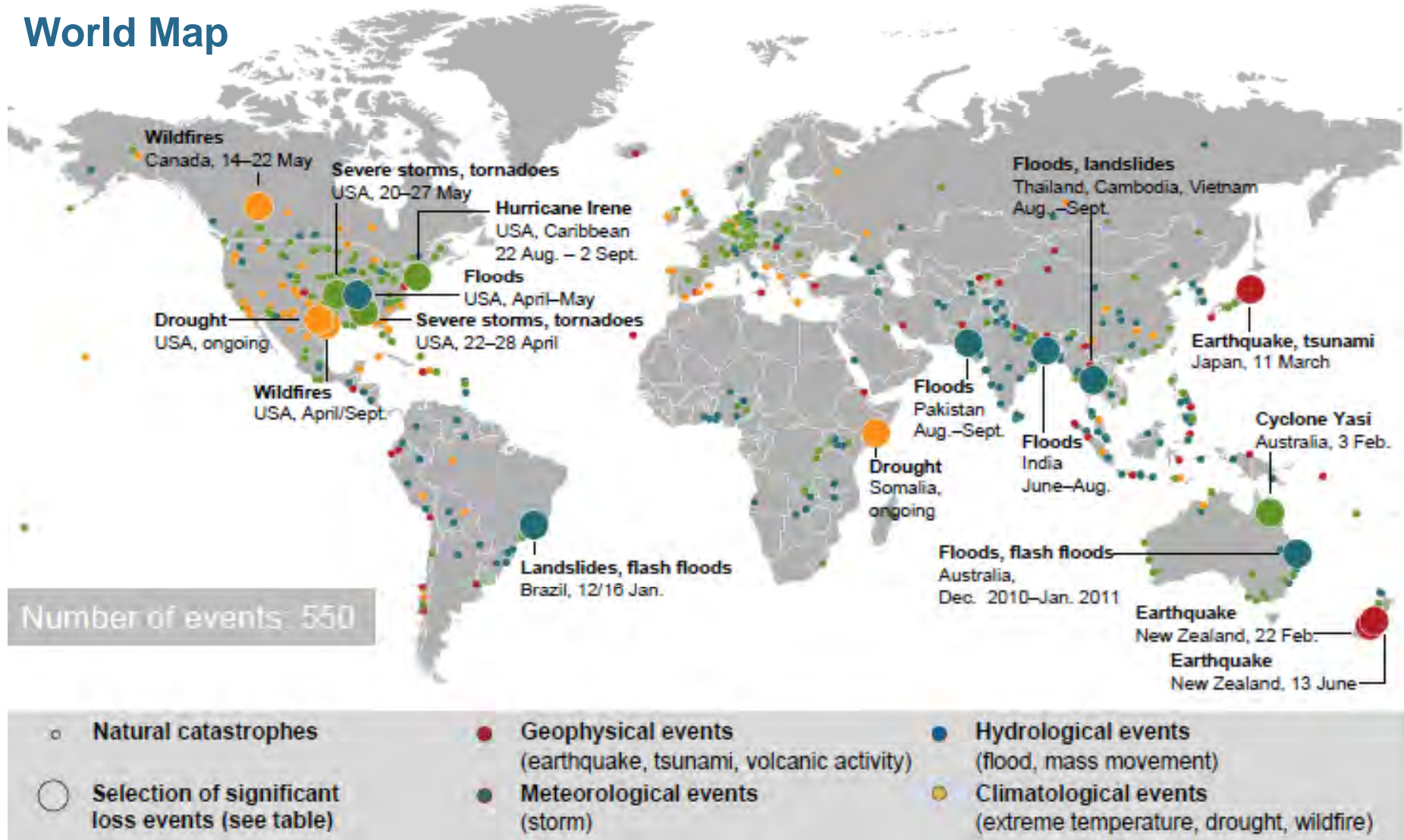
**2011 and 2010 Are Rewriting
Catastrophe Loss and
Insurance History**

Global Catastrophe Loss Summary: First Half 2011

- **2011 Is Already (as of June 30) the *Highest* Loss Year on Record Globally**
 - ◆ Extraordinary accumulation of severe natural catastrophe: Earthquakes, tsunami, floods and tornadoes are the primary causes of loss
- **\$260 Billion in *Economic* Losses Globally**
 - ◆ New record for the first six months, exceeding the previous record of \$220B in 2005
 - ◆ Economy is more resilient than most pundits presume
- **\$55 Billion in *Insured* Losses Globally**
 - ◆ More than double the first half 2010 amount
 - ◆ Over 4 times the 10-year average
- **\$27 Billion in *Economic* Losses in the US**
 - ◆ Represents a 129% increase over the \$11.8 billion amount through the first half of 2010
- **\$17.3 Billion in *Insured* Losses in the US Arising from 100 CAT Events**
 - ◆ Represents a 162% increase over the \$6.6 billion amount through the first half of 2010

Natural Loss Events, January – September 2011

World Map



Worldwide Natural Disasters 2011

Significant Natural Disasters (January – September only)

Period	Loss event	Affected area	Overall losses*	Insured losses*	Fatalities*
			US\$m, original values		
Dec 2010–Jan 2011	Floods, flash floods	Australia (Queensland)	7,300	2,550	29
12/16 Jan.	Landslides, flash floods	Brazil (State of Rio de Janeiro)	**	**	1,350
3 Feb.	Cyclone Yasi	Australia (Queensland)	2,000	1,000	1
22 Feb.	Earthquake	New Zealand (Christchurch)	25,000	13,000	181
11 March	Earthquake, tsunami	Japan (esp. northeastern Honshu)	210,000	~30,000	15,800 (3,800 missing)
22–28 April	Severe storms, tornadoes	USA (esp. AL, Tuscaloosa)	12,000	7,300	350
April–May	Floods	USA (esp. Ohio River, Mississippi River, Missouri River)	2,600	**	9
April/Sept.	Wildfires	USA (TX)	1,500	680	4
14–22 May	Wildfires	Canada (Alberta, Slave Lake)	>1,500	720	1
20–27 May	Severe storms, tornadoes	USA (esp. MO, Joplin)	9,000	5,900	176
13 June	Earthquake	New Zealand (Christchurch)	**	**	1
Aug.–Sept.	Floods, landslides	Thailand, Cambodia, Vietnam	**	**	370
Aug.–Sept.	Floods	Pakistan	**	**	445
22 Aug.–2 Sept.	Hurricane Irene	USA, Caribbean	15,000	7,000	54

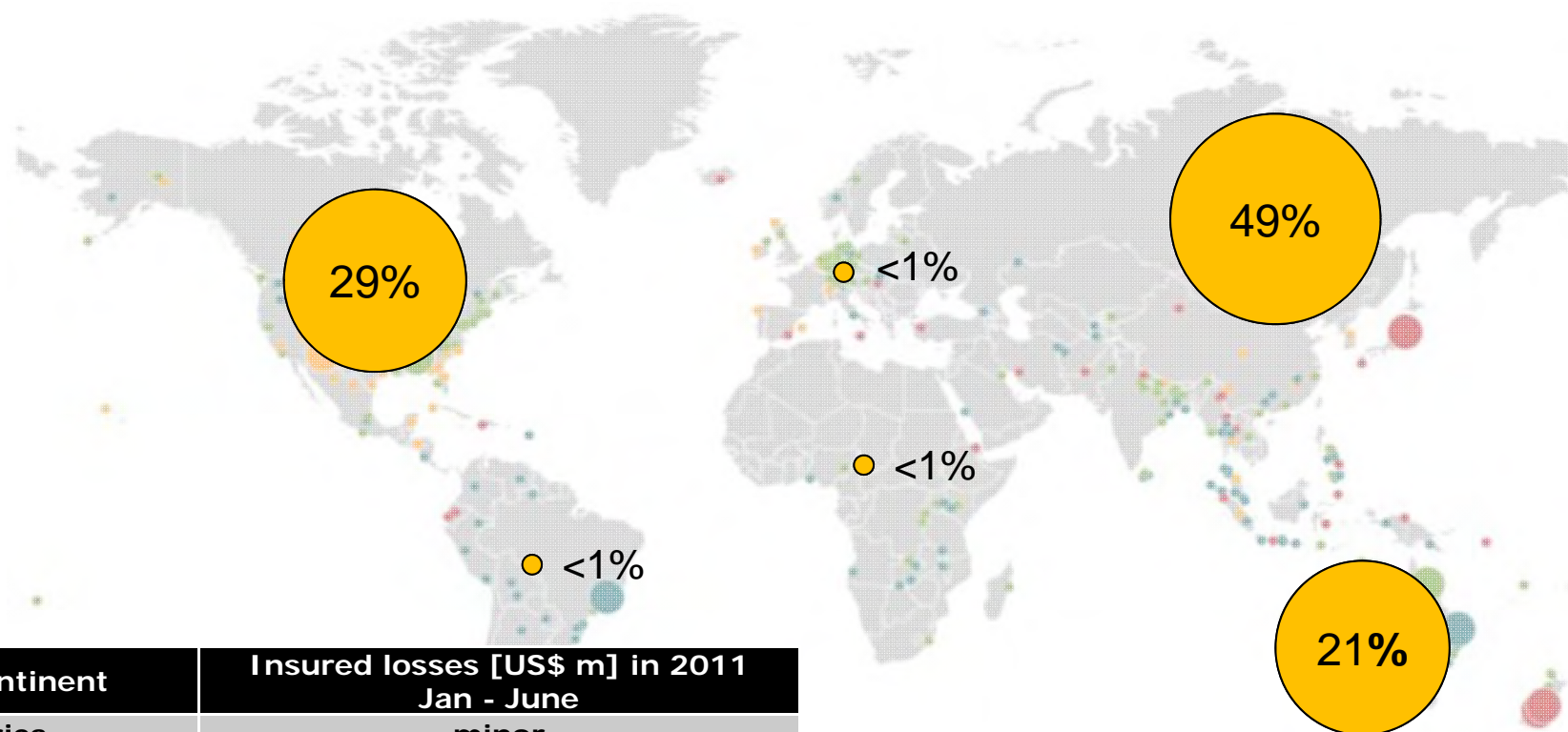
*As at October 2011

**Loss assessment still in progress

Worldwide Natural Disasters 2011

% Distribution of Insured Losses Per Continent (January – June only)

Insured losses 2011 (January – June only): US\$ 60bn

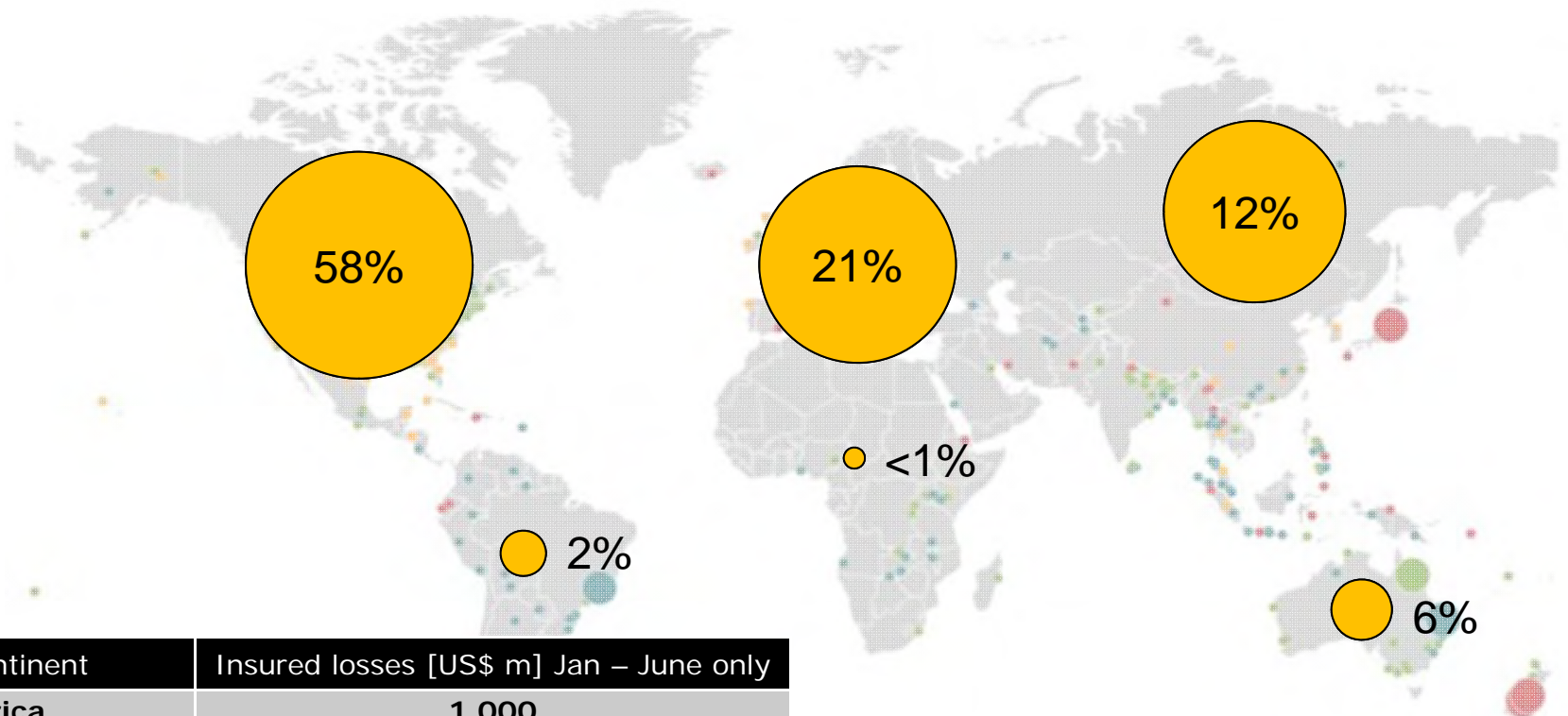


Continent	Insured losses [US\$ m] in 2011 Jan - June
Africa	minor
America	17,800
Asia	30,080
Australia/Oceania	12,900
Europe	100

Worldwide Natural Disasters, 1980-2011

% Distribution of Insured Losses Per Continent (January – June only)

Insured losses 1980 - 2011 (January – June only): US\$ 389bn



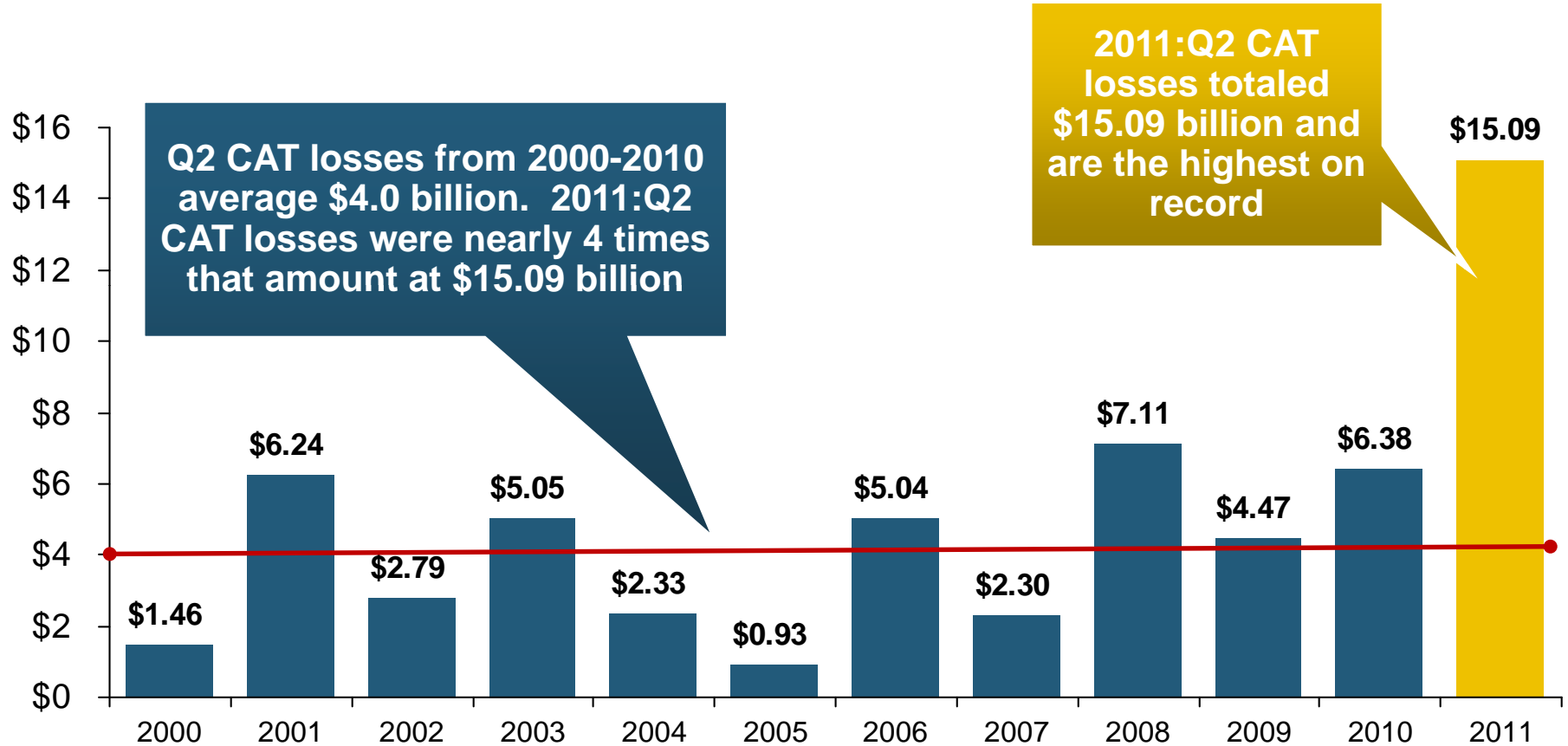
Continent	Insured losses [US\$ m] Jan – June only
Africa	1,000
America	237,200
Asia	45,100
Australia/Oceania	25,100
Europe	80,900

Insured Loss Estimates for Selected Major Catastrophes in 2011

	Japan Earthquake	April Tornadoes	May (Joplin) Tornadoes
Eqecat	\$22 to \$39 billion	\$5 billion to \$7 billion	\$1 billion to \$3 billion
RMS	\$21 to 34 billion	\$3.5 to \$6 billion	\$2 to \$6 billion
AIR	\$20 billion to \$30 billion	\$5 billion to \$7 billion	\$2 to \$6 billion

US Second Quarter Insured Catastrophe Losses, 2000–2011

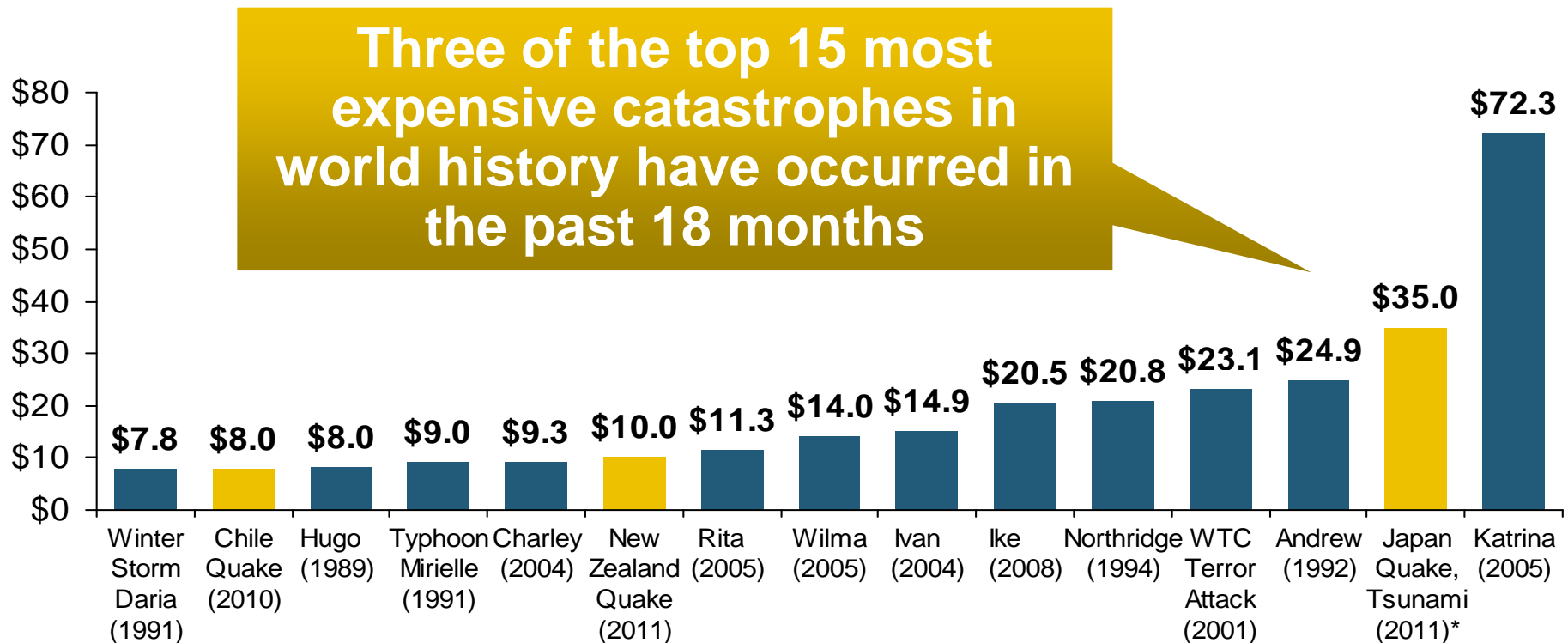
\$ Billions



Record Q2 (and First Half) CAT Losses Will Adversely Impact Insurer Results in 2011

Top 15 Most Costly World Insurance Losses, 1970-2011*

(Insured Losses, 2010 Dollars, \$ Billions)



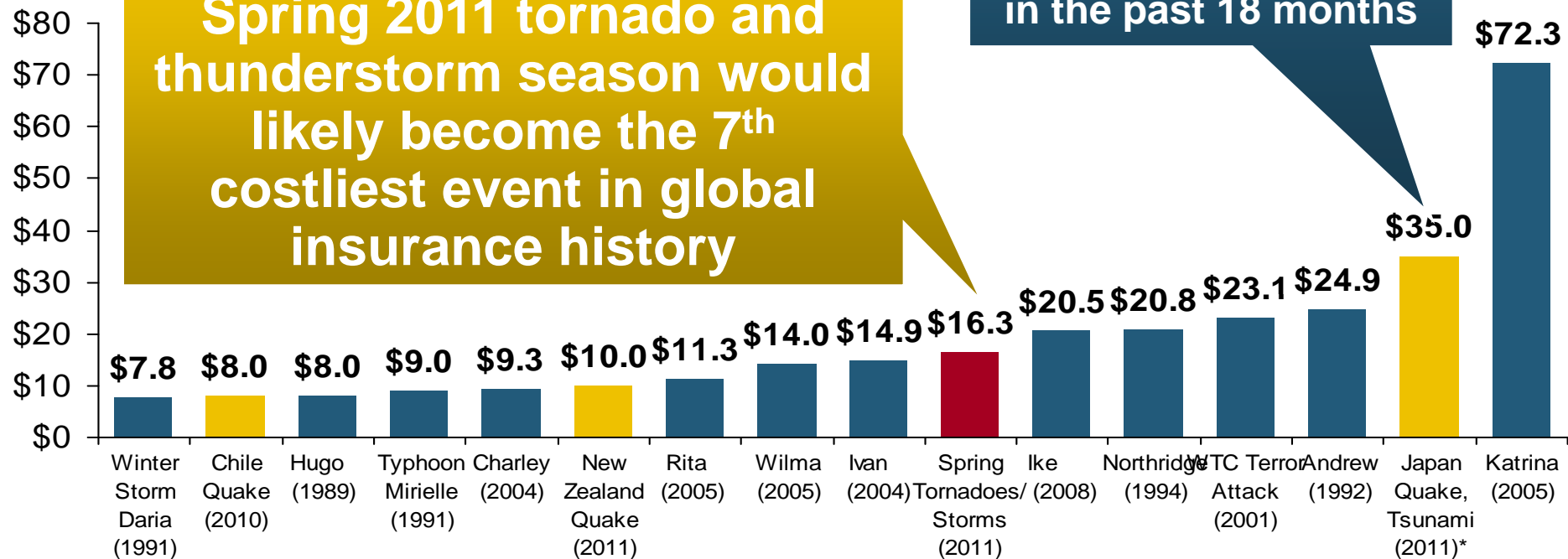
*Through June 20, 2011. 2011 disaster figures are estimates; Figures include federally insured flood losses, where applicable.
Sources: Swiss Re *sigma* 1/2011; AIR Worldwide, RMS, Eqecat; Insurance Information Institute.

Top 16 Most Costly World Insurance Losses, 1970-2011*

(Insured Losses, 2010 Dollars, \$ Billions)

Taken as a single event, the Spring 2011 tornado and thunderstorm season would likely become the 7th costliest event in global insurance history

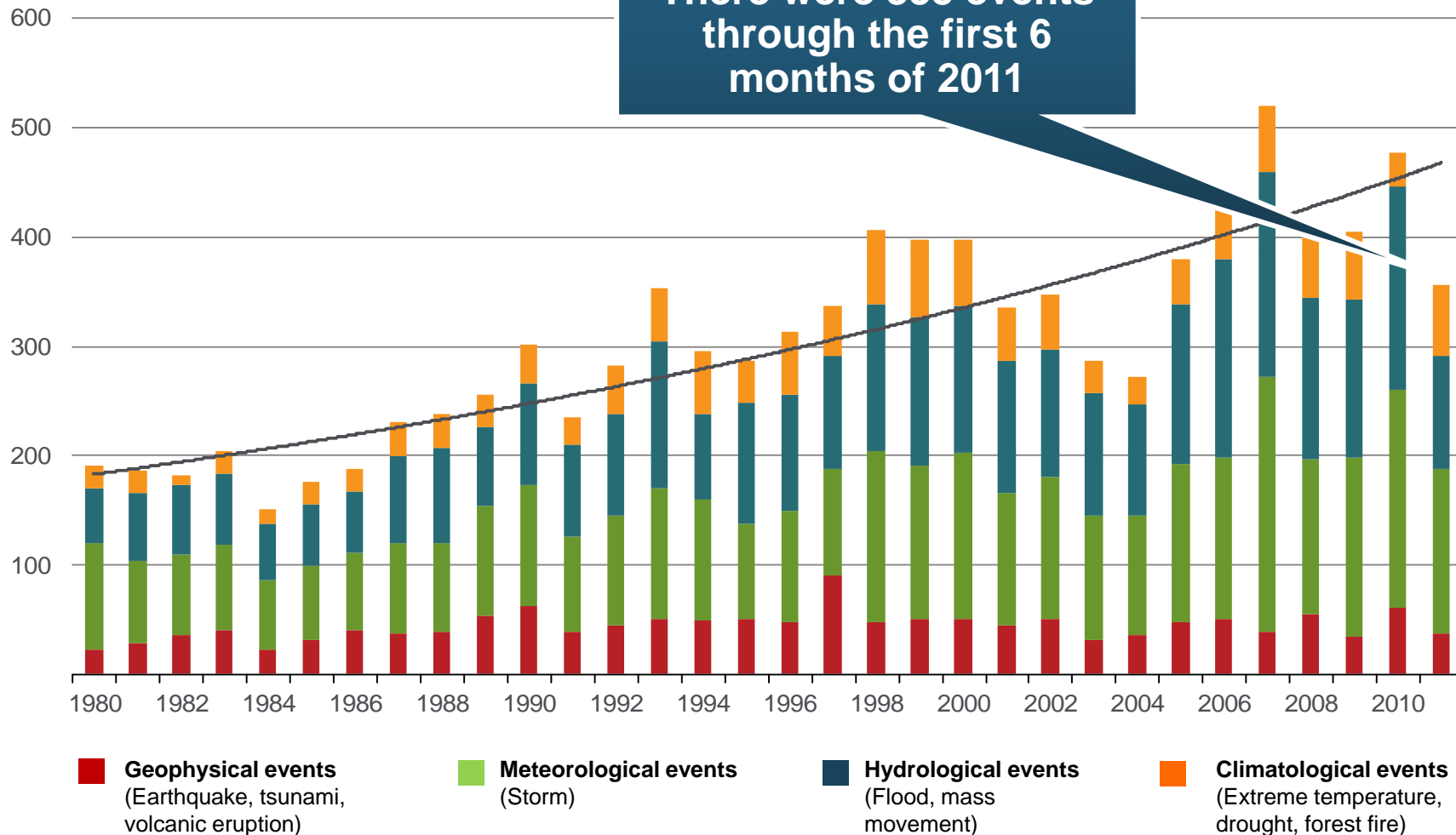
3 of the top 15 most expensive catastrophes in world history have occurred in the past 18 months



*Through June 20, 2011. 2011 disaster figures are estimates; Figures include federally insured flood losses, where applicable. Sources: Swiss Re *sigma* 1/2011; AIR Worldwide, RMS, Eqecat; Insurance Information Institute.

Worldwide Natural Disasters, 1980 – 2011*

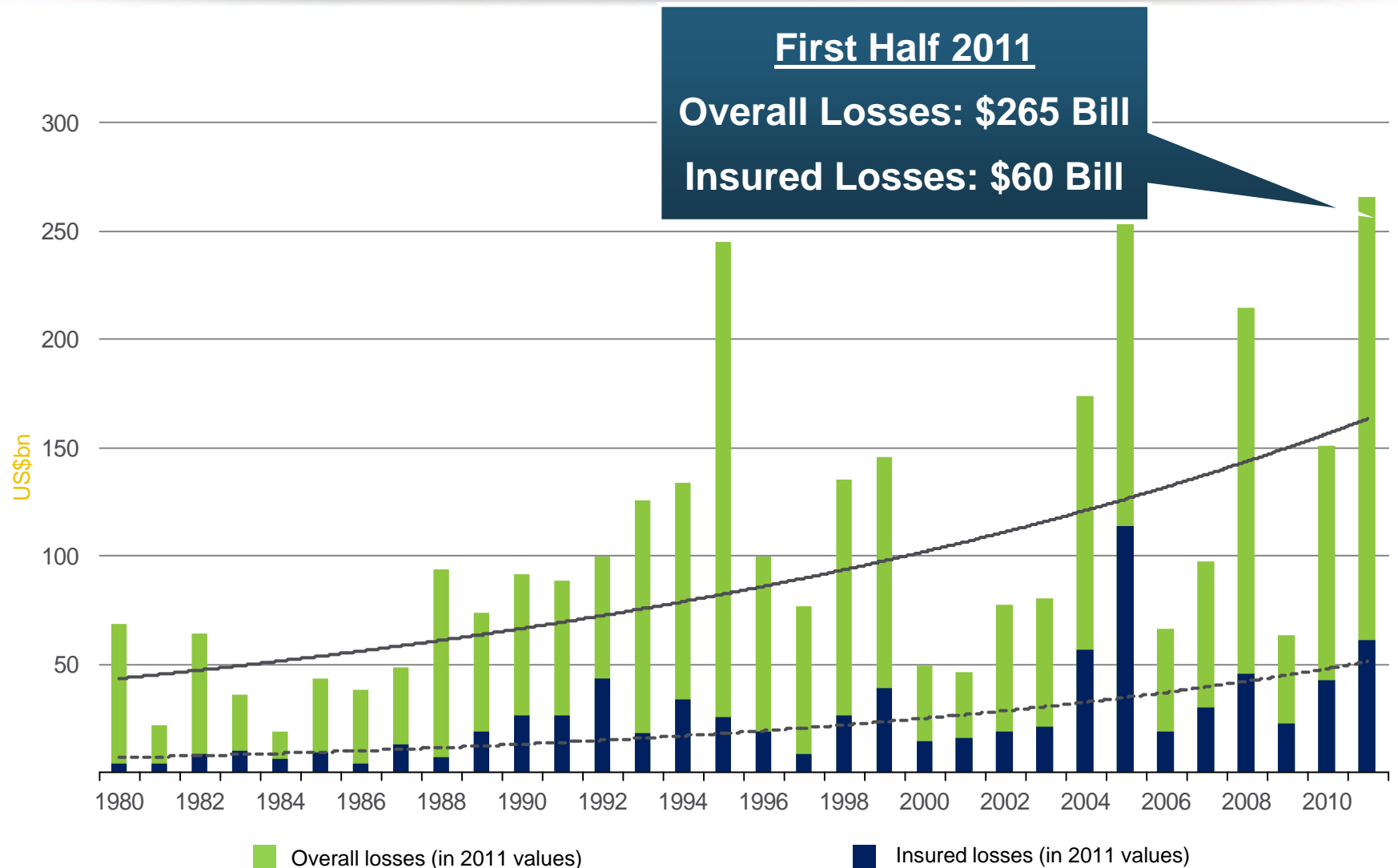
Number of Events



*2011 figure is through June 30.

Source: MR NatCatSERVICE

Worldwide Natural Disasters 1980–2011, Overall and Insured Losses*



*2011 figure is through June 30.

Source: MR NatCatSERVICE

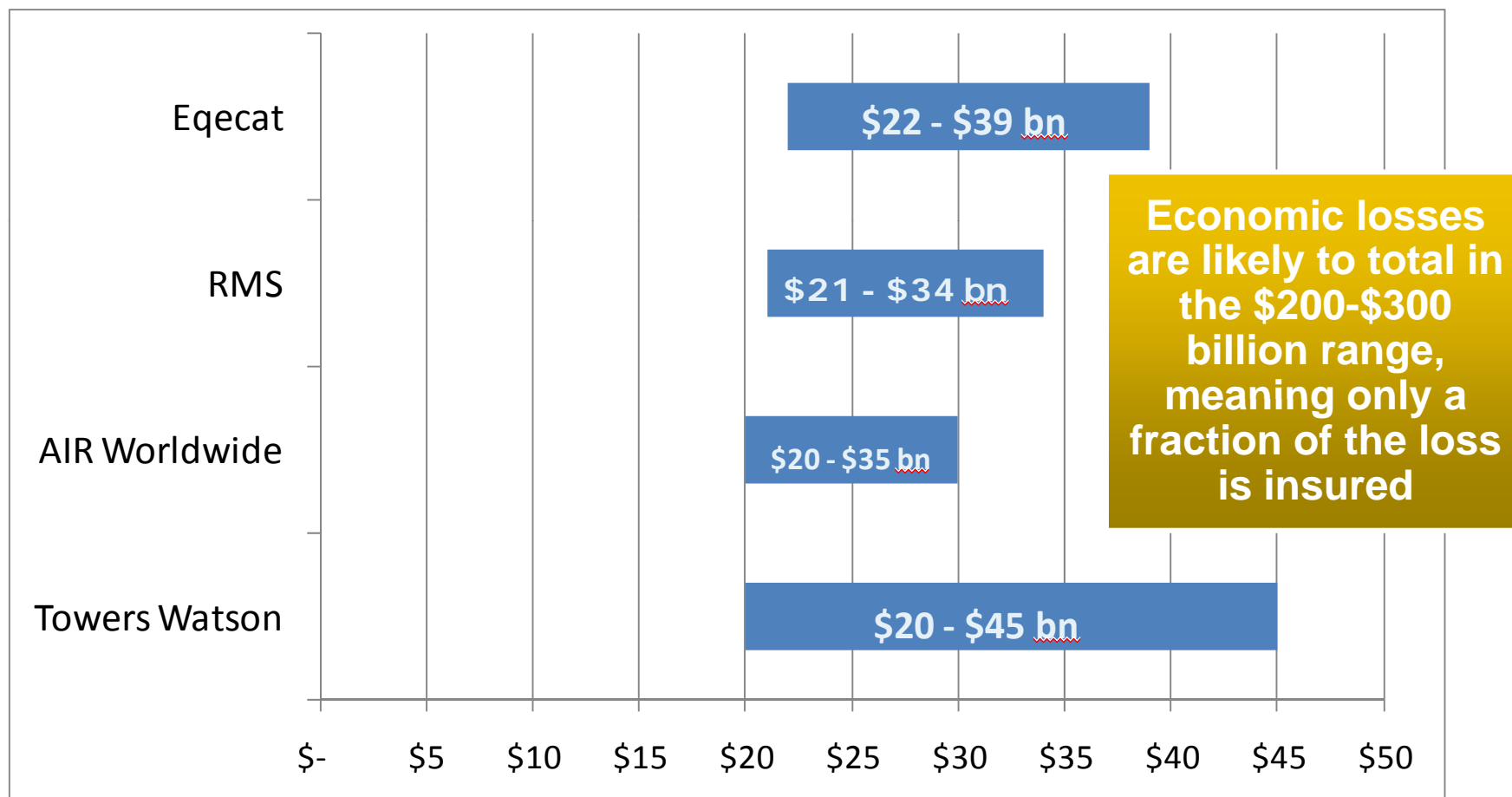


JAPAN EARTHQUAKE/TSUNAMI & NUCLEAR DISASTER

**March 11 Quake/Tsunami Is Just the Most Recent of
Several Large Global Catastrophe Losses**

Insured Japan Earthquake Loss Estimates*

(Insured Losses, \$ Billions)

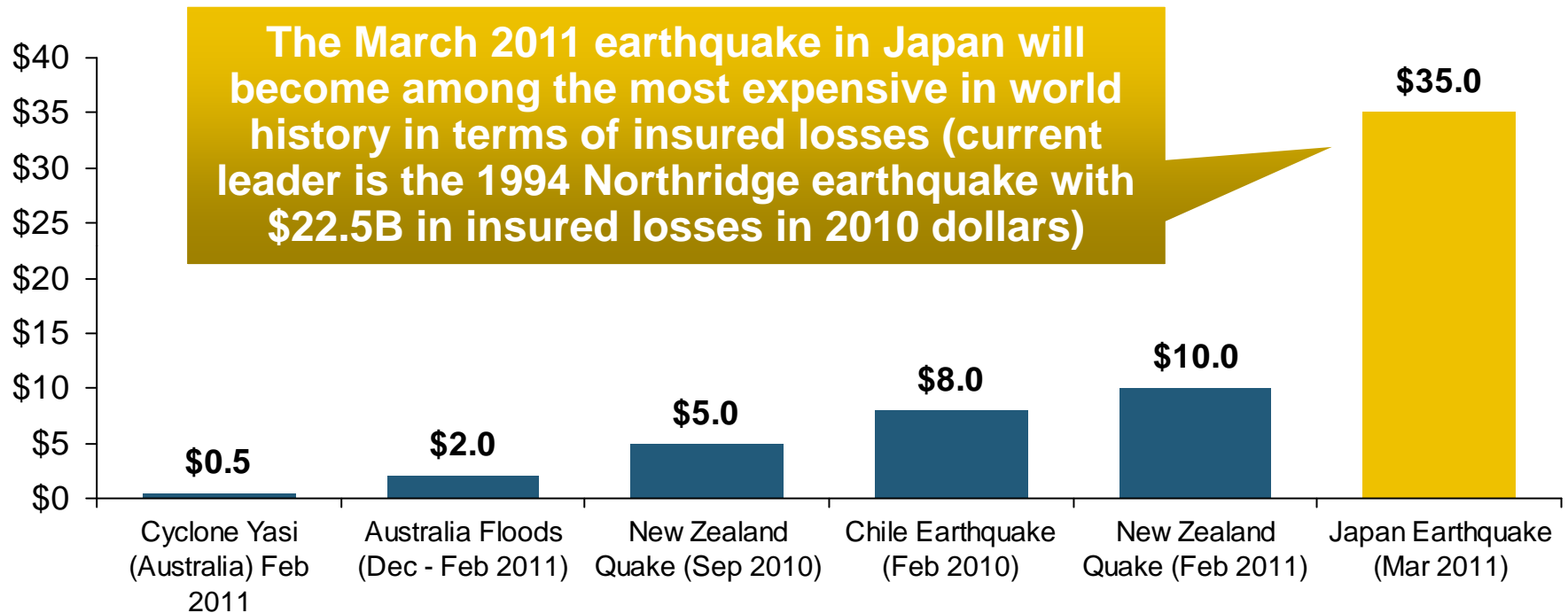


*As of June 17, 2011. Towers Watson estimate includes \$3.0 (low) to \$4.9 billion (high) in life insurance losses. RMS estimate includes insured life/health losses of \$3 to \$8 billion.

Sources: AIR Worldwide, Eqecat, RMS, Towers Perrin; Insurance Information Institute.

Recent Major Non-US Catastrophe Losses

(Insured Losses, \$US Billions)



Insured Losses from Recent Major Catastrophe Events Exceed \$60 Billion, an Estimated \$53 Billion of that from Earthquakes

Nonlife (P/C) Insurance Market Impacts of Japan Earthquake

- **No Direct Impact for US Domestic Primary Insurers**
- ***BUT: \$2 - \$5 Billion in Assumed Loss from Foreign Catastrophes Will Wind Up on the Books of US Insurers, Most with No Direct Exposure to Japan/Australia/NZ***
 - ◆ US reinsurers
 - ◆ Retrocessional market
 - ◆ Blanket property insurance covers
- **Primary Insurance: Domestic Japanese Insurers Take Big Losses**
- **Few US/Foreign Insurers Had Direct Exposure to Japanese P/C Market**
 - ◆ Low single-digit market share for a small number of companies
- **Significant Absorption of Loss by Japanese Government**
 - ◆ Residential earthquake damage
 - ◆ Nuclear-related property and liability damage
- **Significant Impacts for Global Reinsurers**
 - ◆ Property-Catastrophe covers on Commercial Lines
 - ◆ Business Interruption/Contingent Business Interruption
- **Supply Chain Disruption Concern (Now Waning)**
- **Currently an Earnings Event for Global Reinsurers**
 - ◆ Not a capital event: Global reinsurance markets entered 2011 with record capital
- **Cost of Property/Cat Reinsurance Rising in Japan, New Zealand, Australia**
 - ◆ Up for all; Magnitude of increase is sensitive to size of loss
- **Impact on Cost of US Property-Cat Reinsurance is Possible/Likely**
 - ◆ Market remains well capitalized and competitive

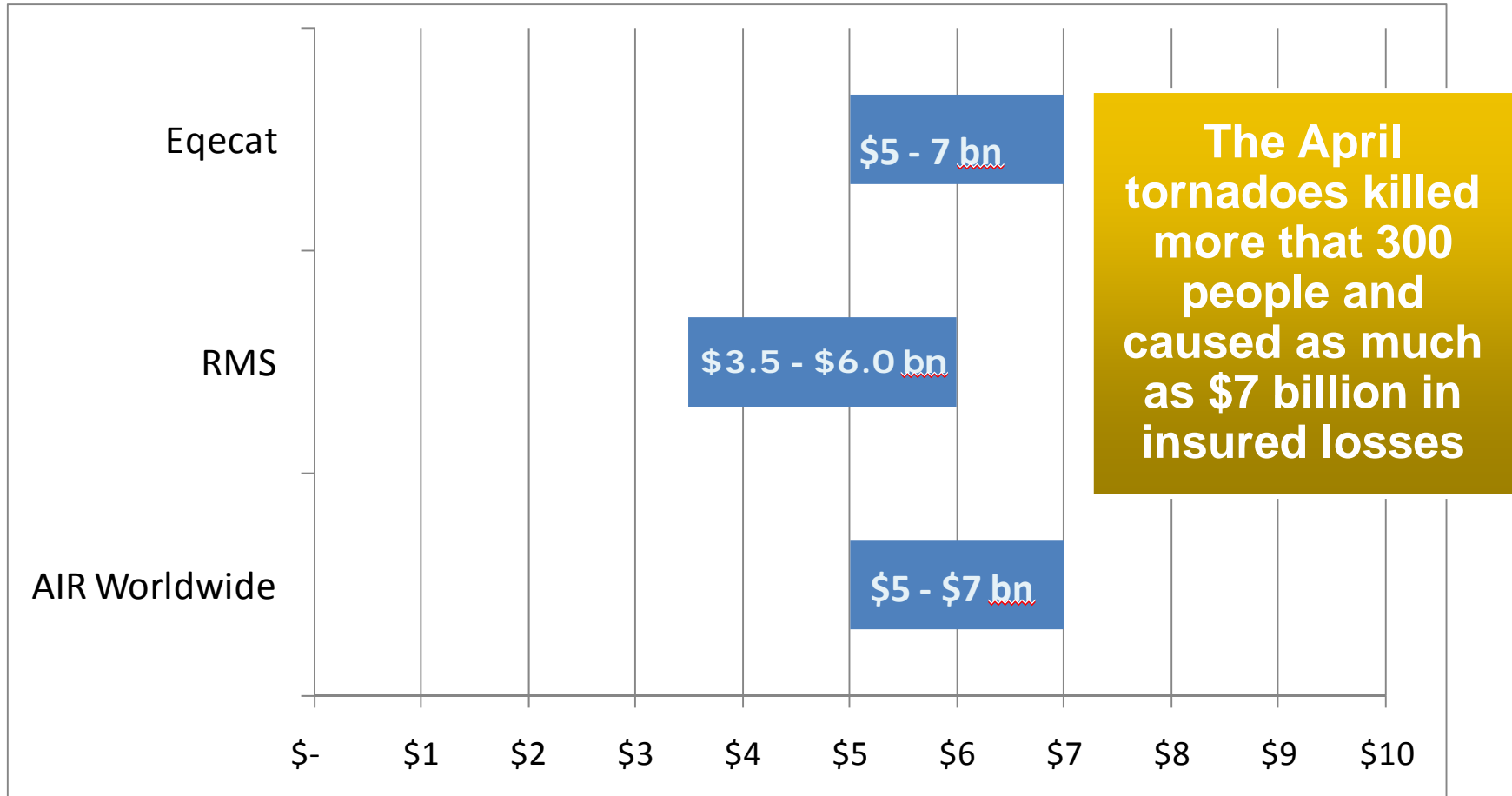


SPRING 2011 TORNADO OUTBREAK

2011 Will Be Among the Most Deadly and Expensive for Tornadoes In History

Insured Loss Estimates from April 2011 Tornadoes*

(Insured Losses, \$ Billions)

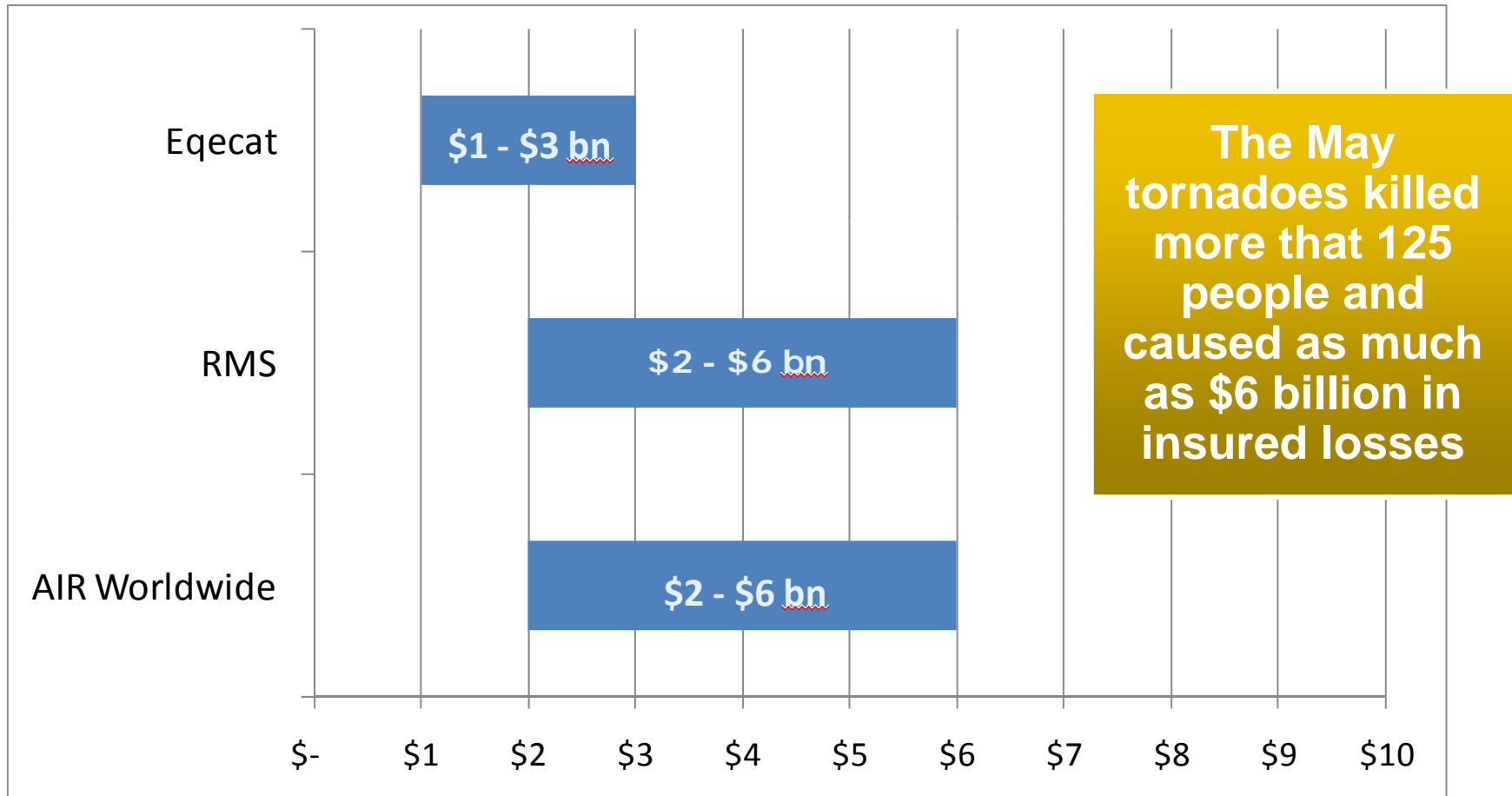


*As of June 17, 2011.

Sources: AIR Worldwide, Eqecat, RMS; Insurance Information Institute research.

Insured Loss Estimates from May 2011 (Joplin) Tornadoes*

(Insured Losses, \$ Billions)



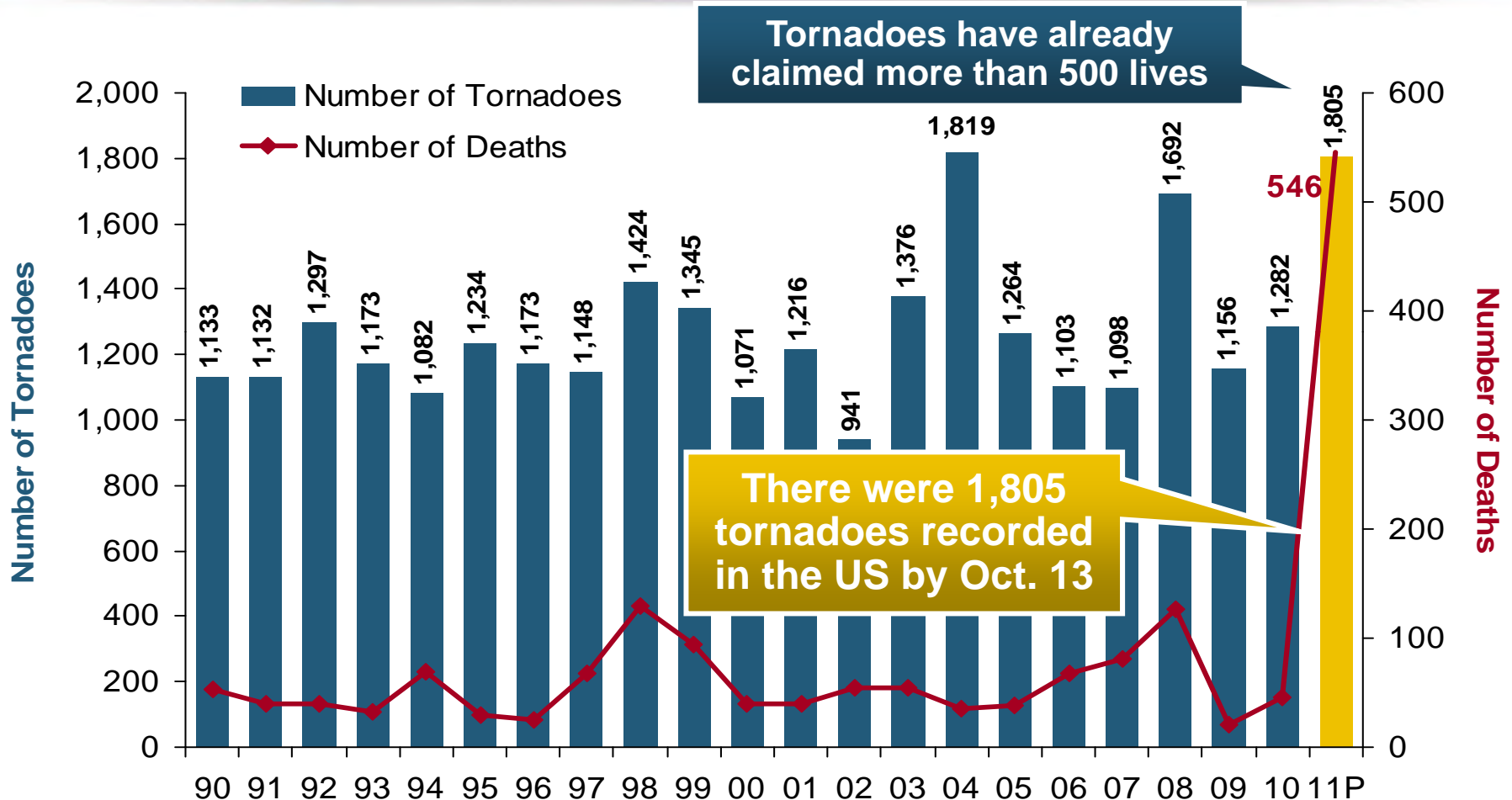
*As of June 17, 2011.

Sources: AIR Worldwide, Eqecat, RMS; Insurance Information Institute research.

Summary of Recent Tornado Activity

- **There Have Been 1,585 Tornadoes Through June 30 in the US**
- **537 People Have Been Killed**
- **The April 27 Tornado Outbreak Killed at Least 342 People**
 - ◆ Now the 2nd deadliest outbreak in US history (747 killed in march 1925 event)
 - ◆ States impacted: AR, TN, LA, MS, GA and especially AL
 - ◆ *Insured Losses Estimated at \$3.5B to \$7B*
- **Economic Losses Likely in the \$7 Bill to \$14 Bill Range**
- **The May 22 Tornado in Joplin, MO, Killed at Least 130 People**
 - ◆ Largest number of deaths from a single tornado
 - ◆ *Insured Losses Estimated at \$1B to \$6B*
- **P/C Insurance Industry is Very Strong and Will Encounter No Difficulties in Paying these Claims**

Number of Tornadoes and Related Deaths, 1990 – 2011*



Insurers Expect to Pay at Least \$2 Billion Each for the April 2011 Tornadoes in Alabama and a Similar Amount for the May Storms in Joplin

*2011 is preliminary data through October 13.

Source: U.S. Department of Commerce, Storm Prediction Center, National Weather Service.

Insurers Making a Difference in Impacted Communities



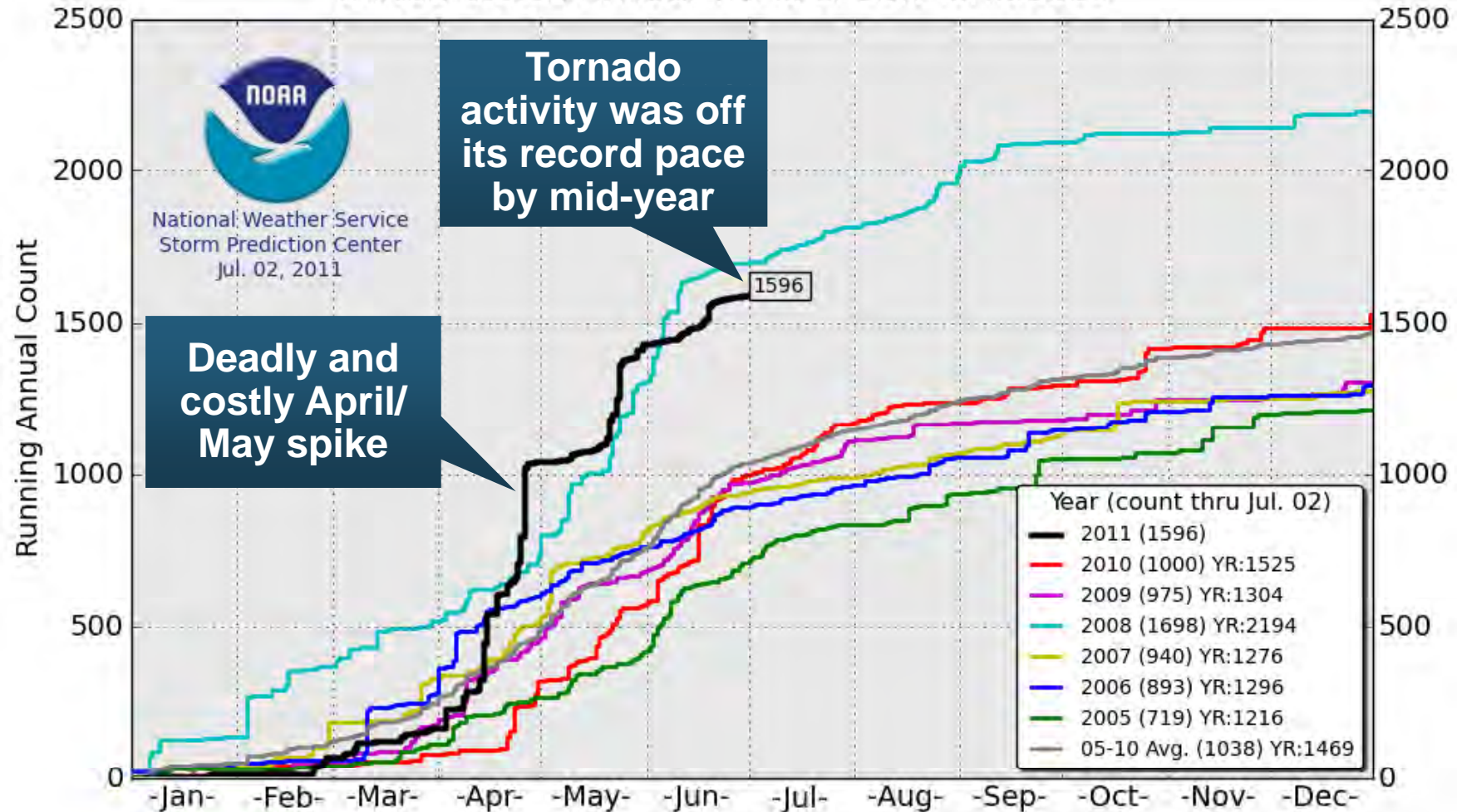
Destroyed home in Tuscaloosa. Insurers will pay some 165,000 claims totaling \$2 billion in the Tuscaloosa/Birmingham areas alone.

Presentation of a check to Tuscaloosa Mayor Walt Maddox to the Tuscaloosa Storm Recovery Fund



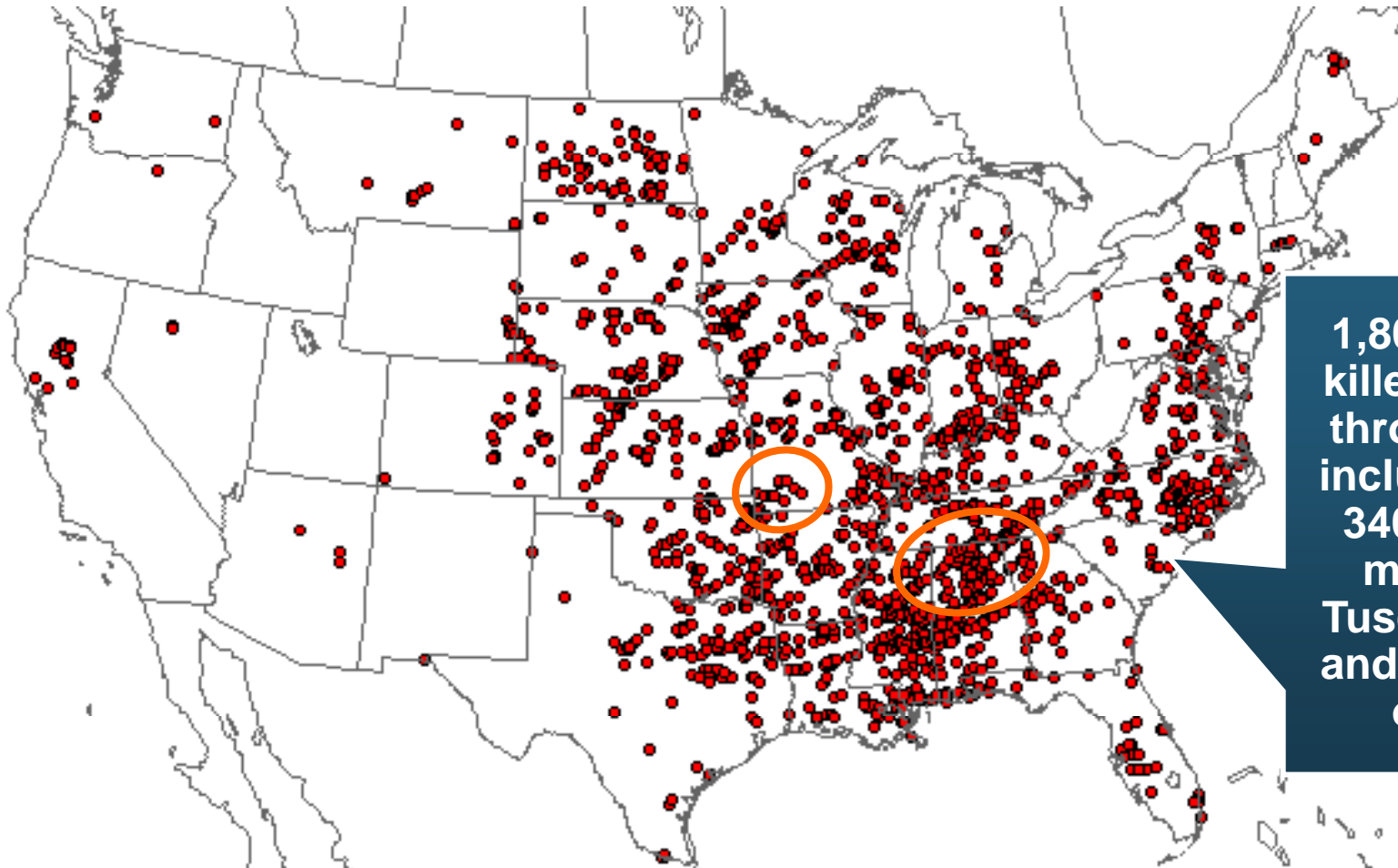
U.S. Tornado Count, 2005-2011*

United States Annual Trend of LSR Tornadoes*



*Preliminary tornadoes from NWS Local Storm Reports (LSRs)
Annual average is based on preliminary LSRs, 2005-2010

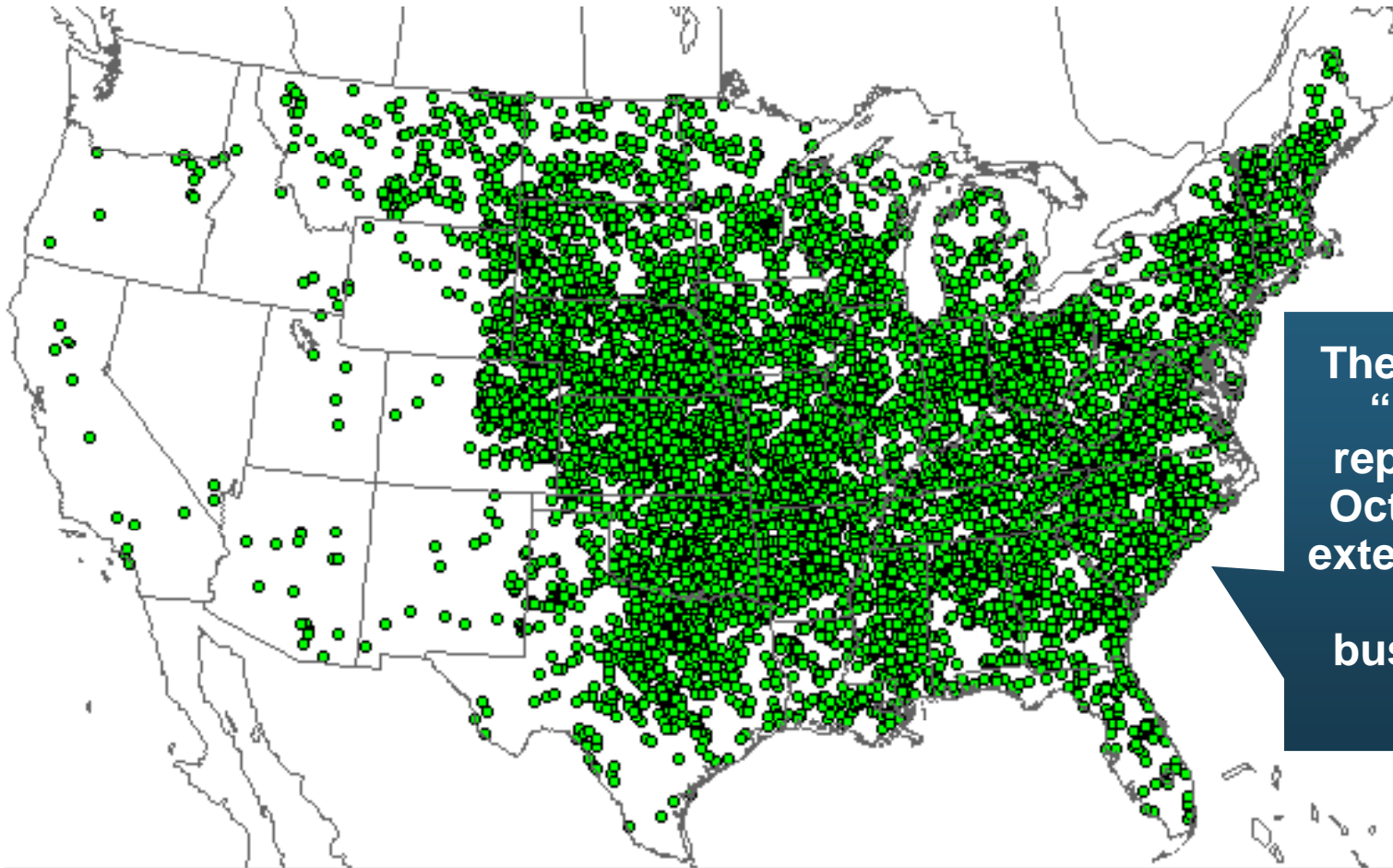
Location of Tornadoes in the US, January 1—October 13, 2011



1,805 tornadoes killed 546 people through Oct. 13, 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)** **Tornado Reports**
NOAA/Storm Prediction Center Norman, Oklahoma **January 01, 2011 - October 13, 2011**
Updated: Thursday October 13, 2011 12:59 CT

Location of Large Hail Reports in the US, January 1—October 13, 2011



There were 9,287
“Large Hail”
reports through
Oct. 13, causing
extensive damage
to homes,
businesses and
vehicles



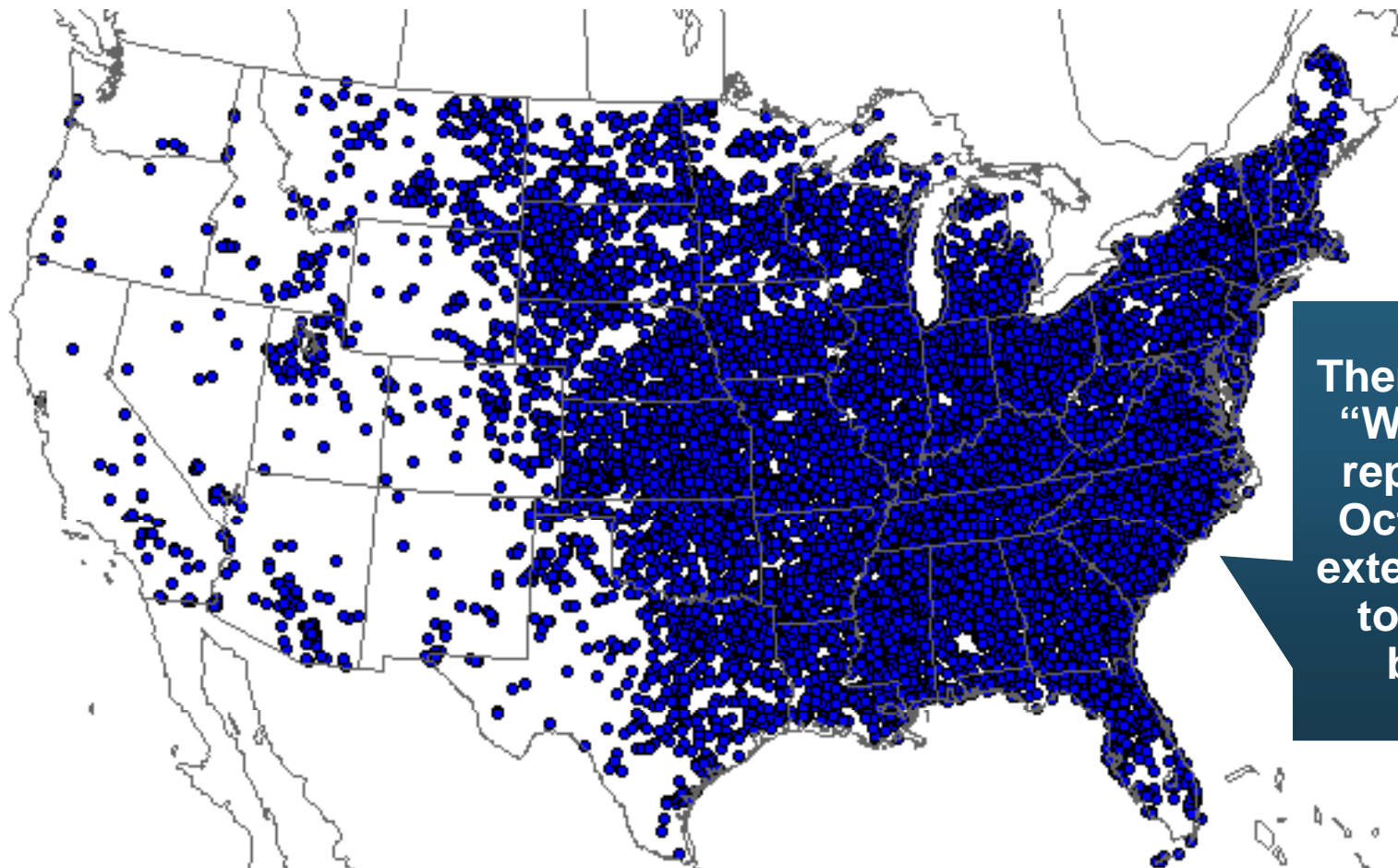
PRELIMINARY SEVERE WEATHER
REPORT DATABASE (ROUGH LOG)

NOAA/Storm Prediction Center Norman, Oklahoma

Hail Reports
January 01, 2011 - October 13, 2011

Updated: Thursday October 13, 2011 12:59 CT

Location of Wind Damage Reports in the US, January 1—Oct. 13, 2011



There were 18,293
“Wind Damage”
reports through
Oct. 13, causing
extensive damage
to homes and,
businesses



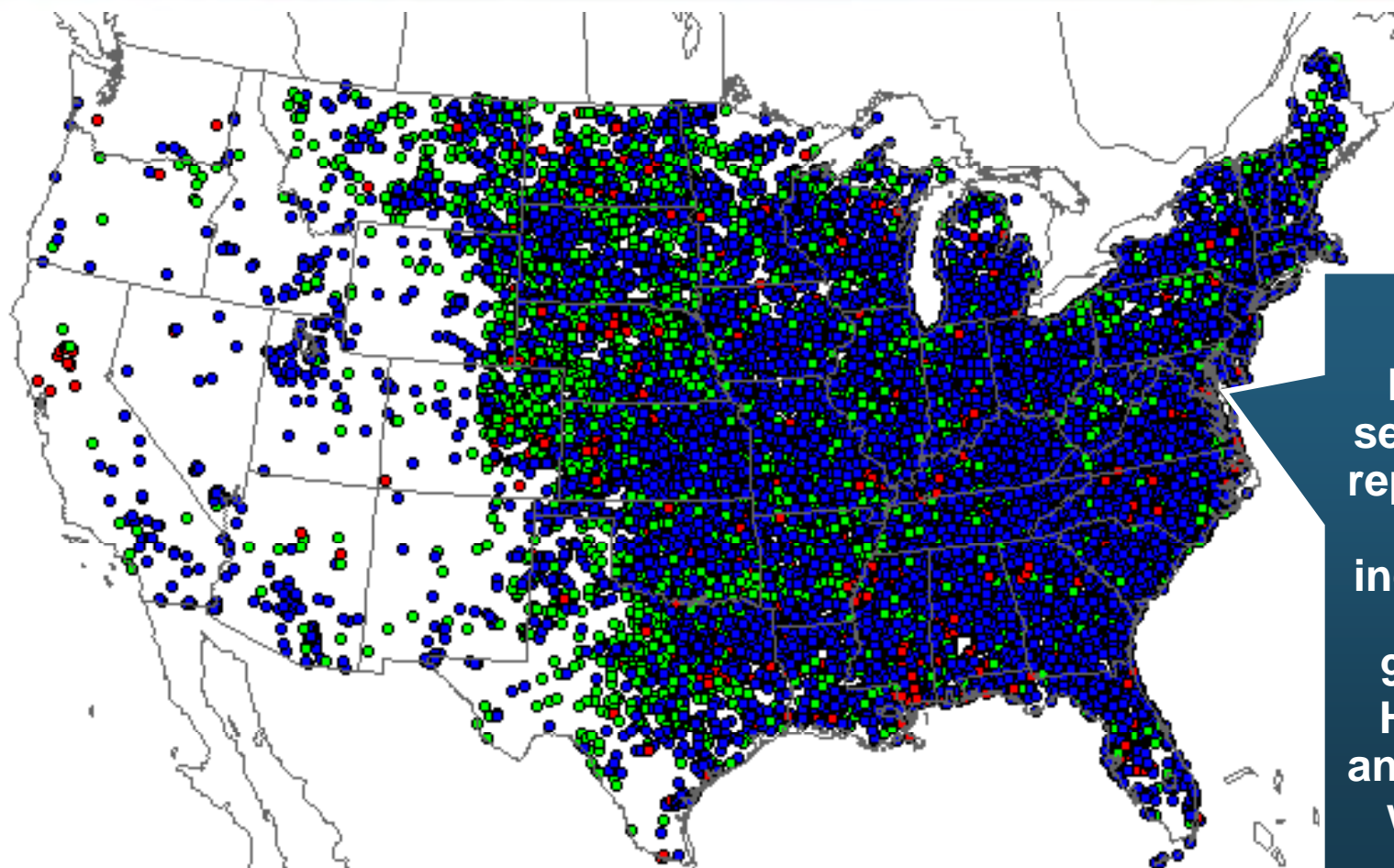
PRELIMINARY SEVERE WEATHER
REPORT DATABASE (ROUGH LOG)

NOAA/Storm Prediction Center Norman, Oklahoma

Wind Reports
January 01, 2011 - October 13, 2011

Updated: Thursday October 13, 2011 12:59 CT

Severe Weather Reports, January 1—October 13, 2011



There have been 29,385 severe weather reports through Oct. 13; including 1,805 tornadoes; 9,287 “Large Hail” reports and 18,293 high wind events



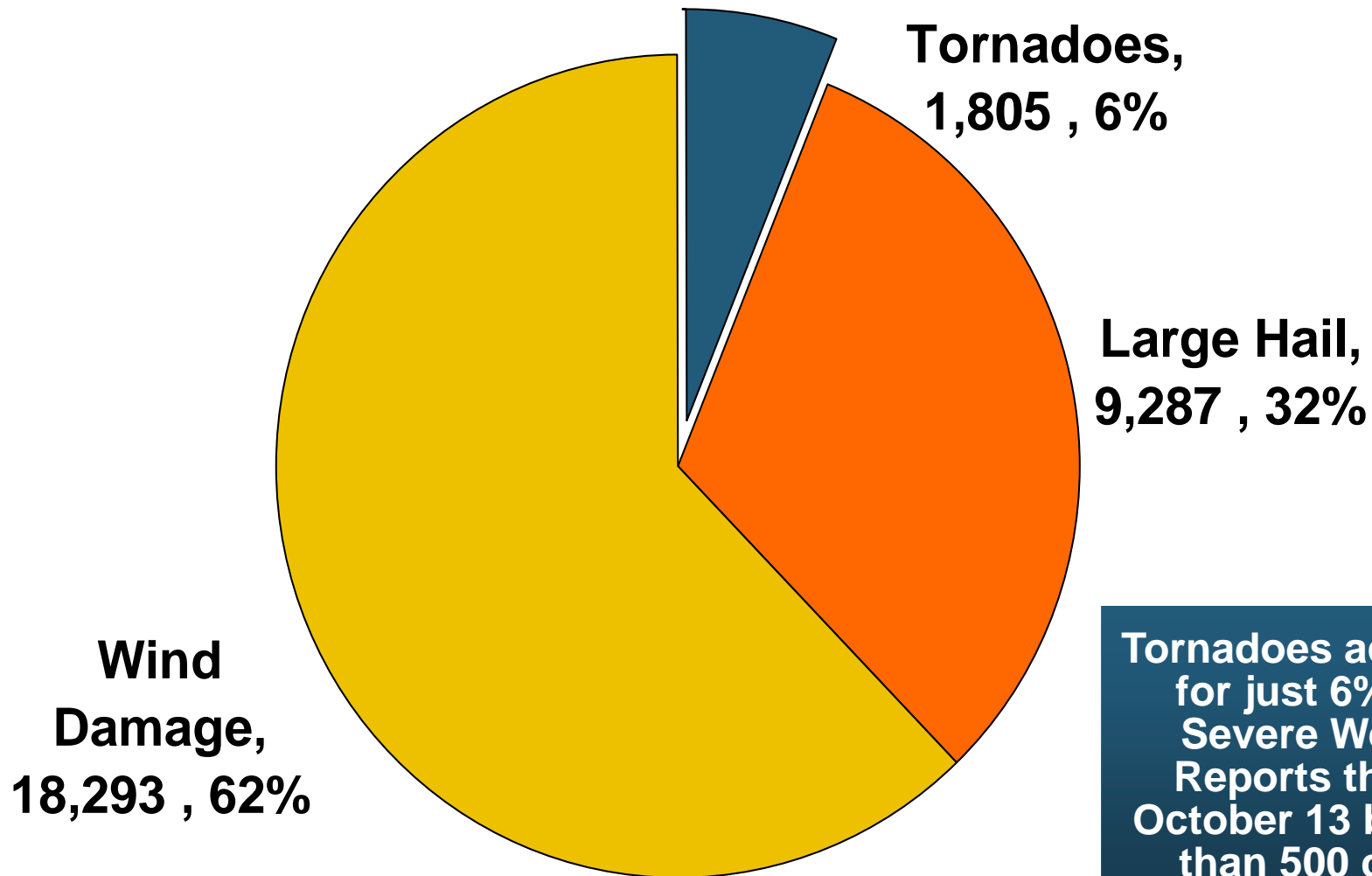
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NOAA/Storm Prediction Center Norman, Oklahoma

Severe Weather Reports
January 01, 2011 - October 13, 2011

Updated: Thursday October 13, 2011 12:59 CT

Number of Severe Weather Reports in US, by Type: January 1—October 13, 2011



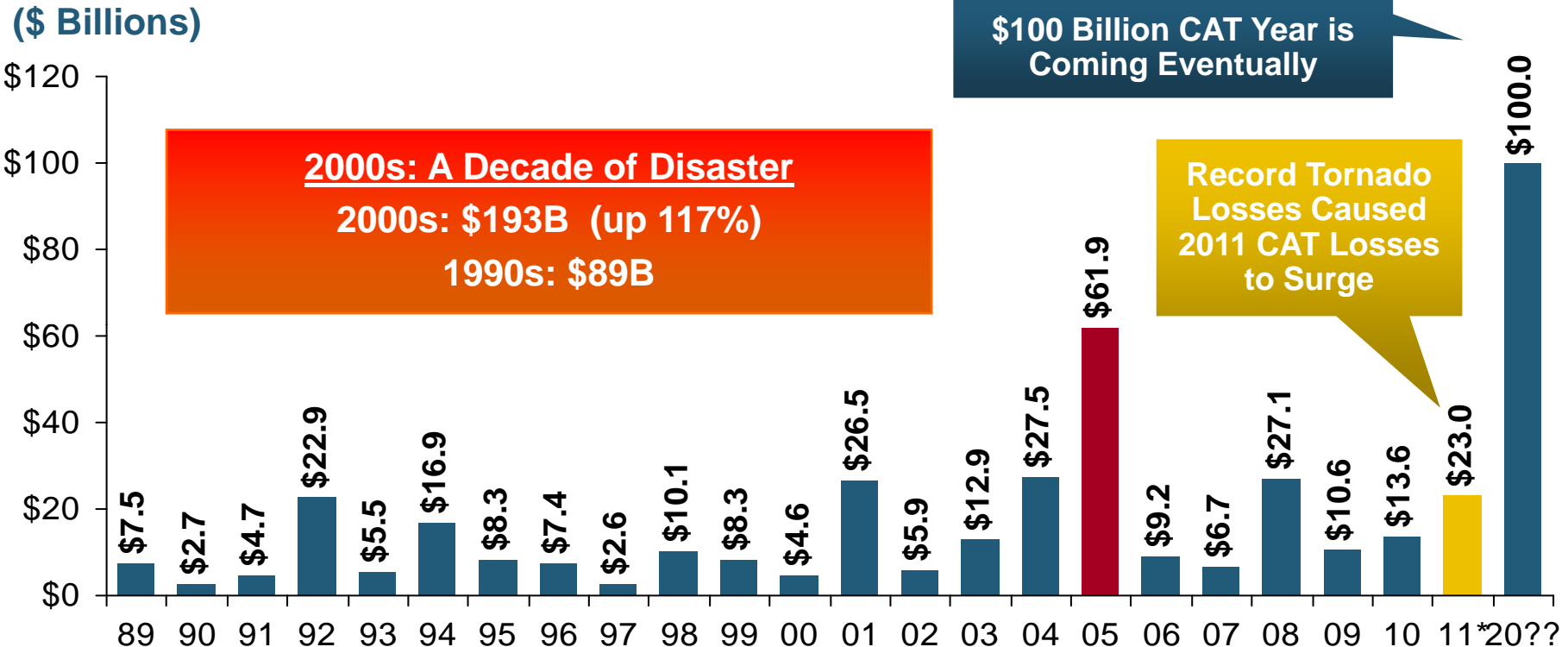
Tornadoes accounted for just 6% of all Severe Weather Reports through October 13 but more than 500 deaths



US CATASTROPHE INSURED LOSS UPDATE

**First Half 2011 CAT Losses Already Exceed All of
2010 and Could Become One of the Most
Expensive Years on Record**

US Insured Catastrophe Losses



First Half 2011 US CAT Losses Already Exceed Losses from All of 2010. Even Modest Hurricane Losses Will Make 2011 Among the Most Expensive Ever for CATs

*Estimate through Sept. 30, 2011.

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

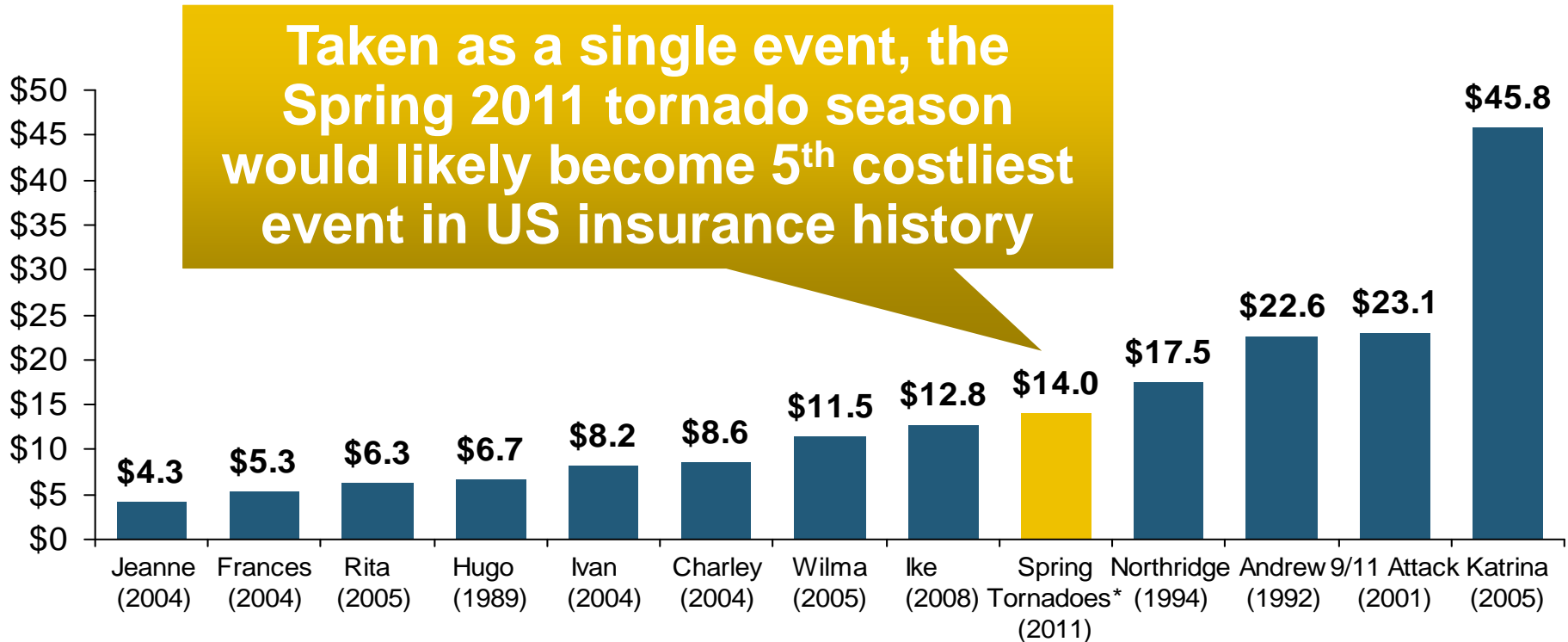
Sources: Property Claims Service/ISO; Insurance Information Institute.

Natural Disaster Losses in the United States: First 6 Months 2011

As of July 6, 2011	Number of Events	Fatalities	Estimated Overall Losses (US \$m)	Estimated Insured Losses (US \$m)
Severe Thunderstorm	43	593	23,573	16,350
Winter Storm	8	15	1,900	1,425
Flood	8	15	2,100	in progress
Earthquake	2	1	105	in progress
Tropical Cyclone	0	0	0	0
Wildfire	37	7	125	50

Top 12 (13?) Most Costly Disasters in U.S. History

(Insured Losses, 2010 Dollars, \$ Billions)



*Losses will actually be broken down into several "events" as determined by PCS.

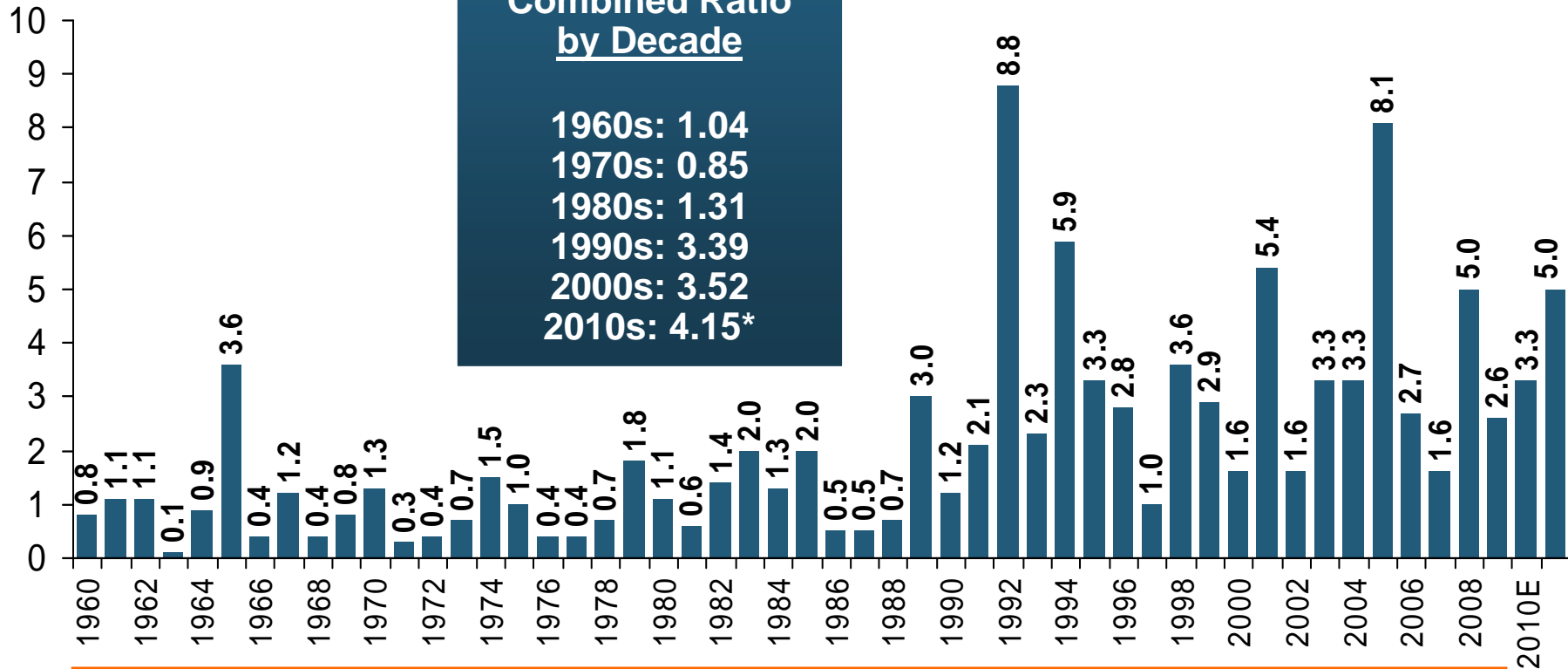
Sources: PCS; Insurance Information Institute inflation adjustments.

Combined Ratio Points Associated with Catastrophe Losses: 1960 – 2011:H1*

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: 4.15*



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

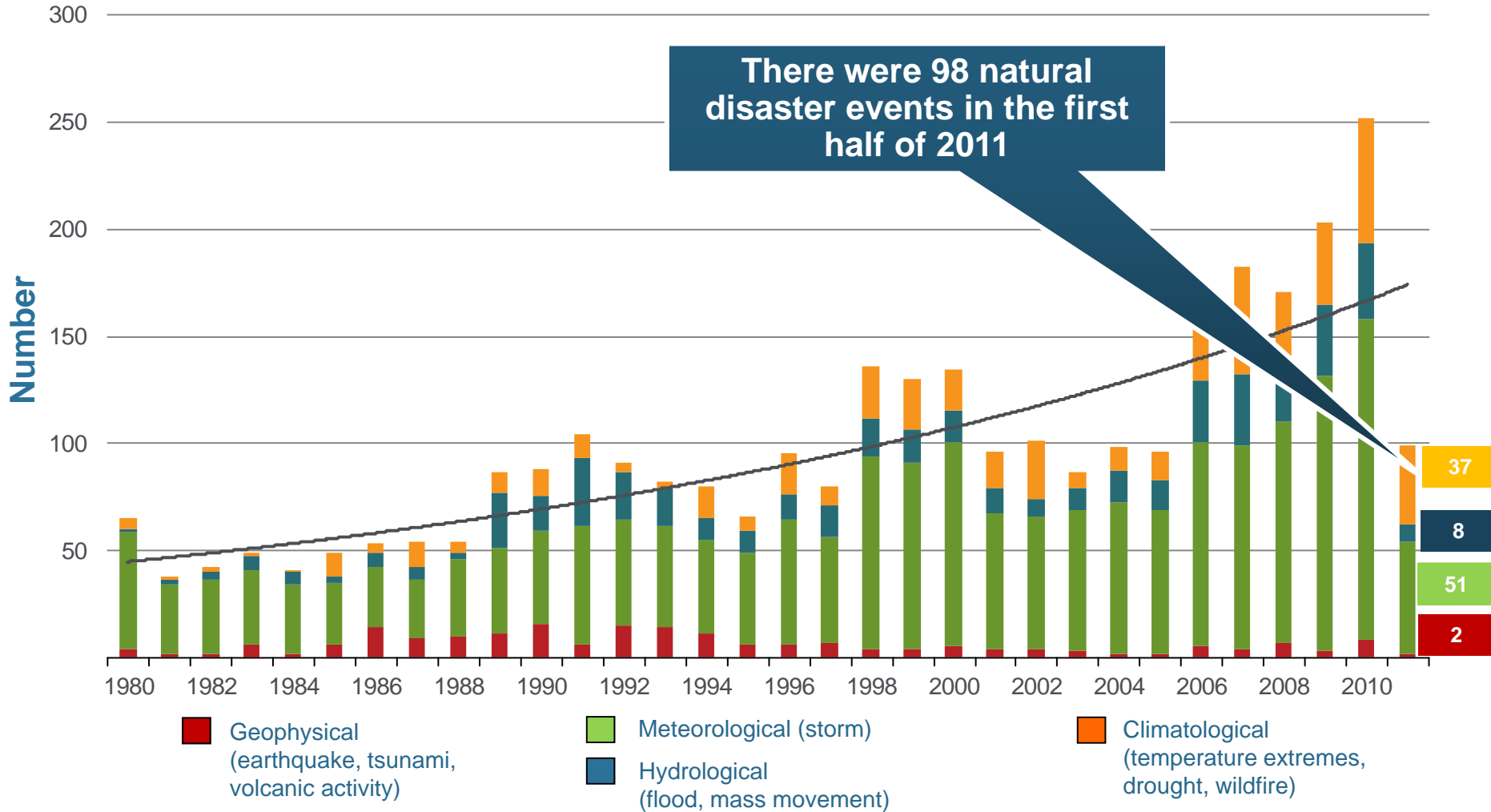
*Insurance Information Institute estimates for 2010 and 2011:H1

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; Insurance Information Institute.

Natural Disasters in the United States, 1980 – 2011*

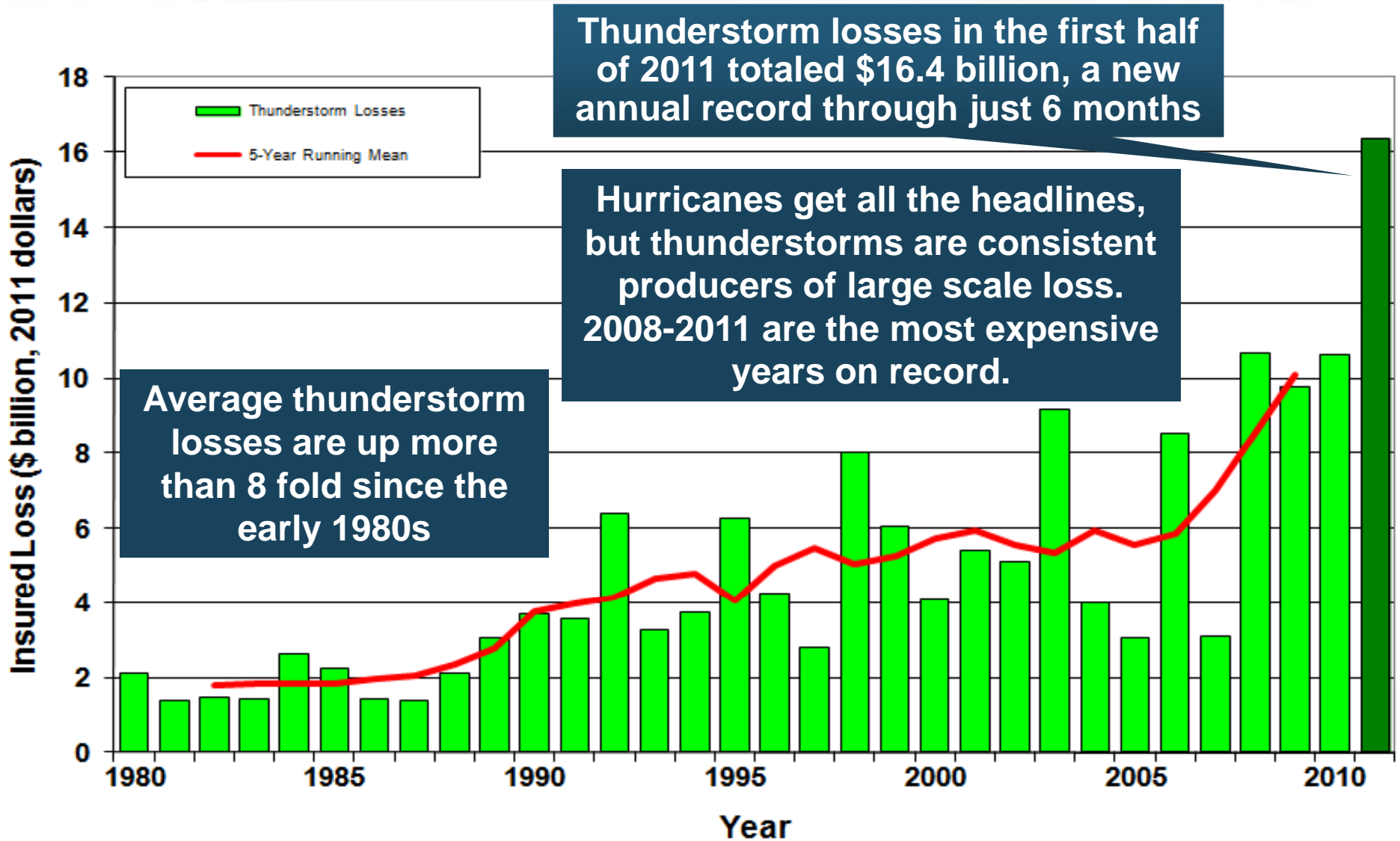
Number of Events (Annual Totals 1980 – 2010 and First Half 2011)



*Through June 30.

Source: MR NatCatSERVICE

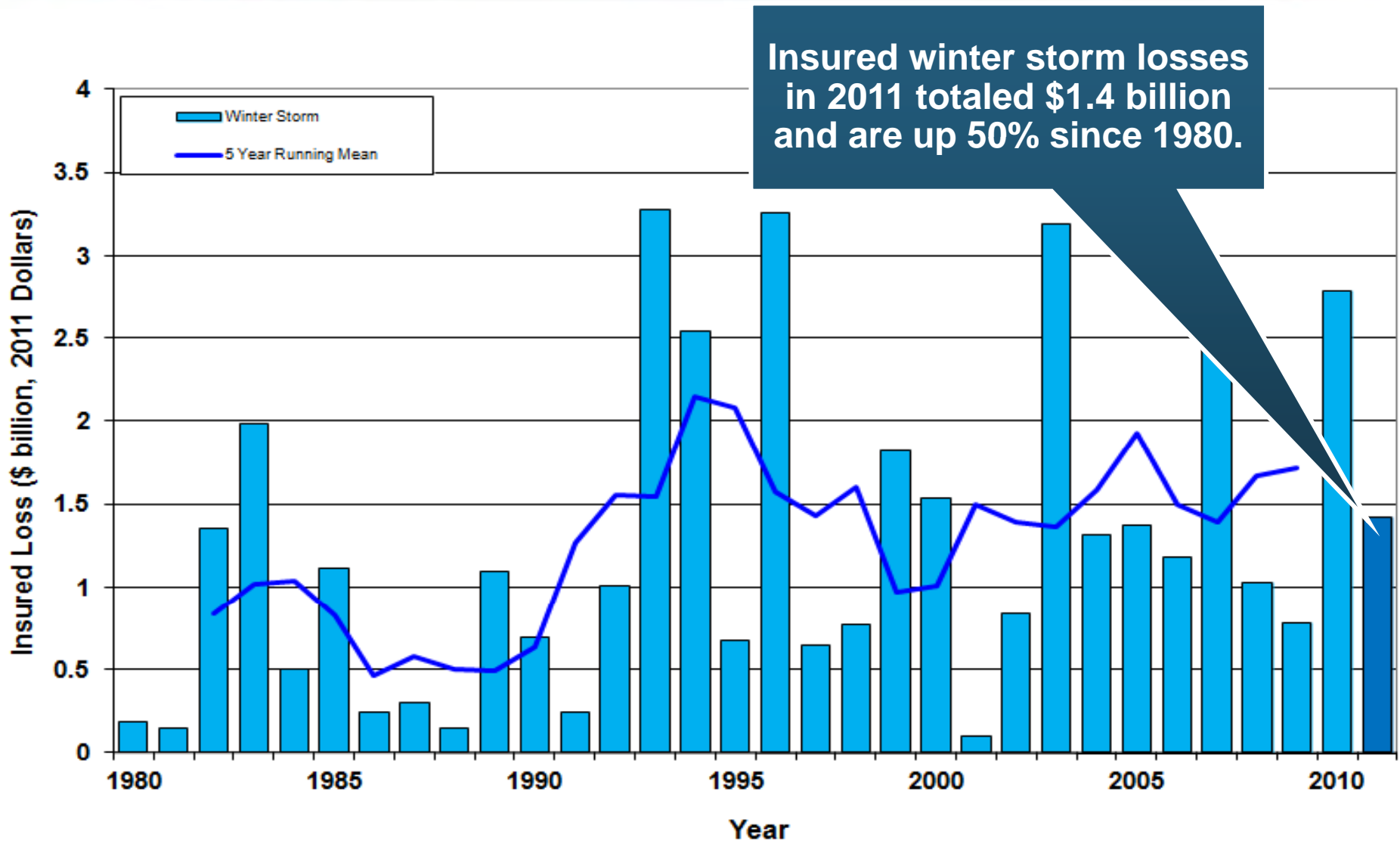
U.S. Thunderstorm Loss Trends, 1980 – 2011*



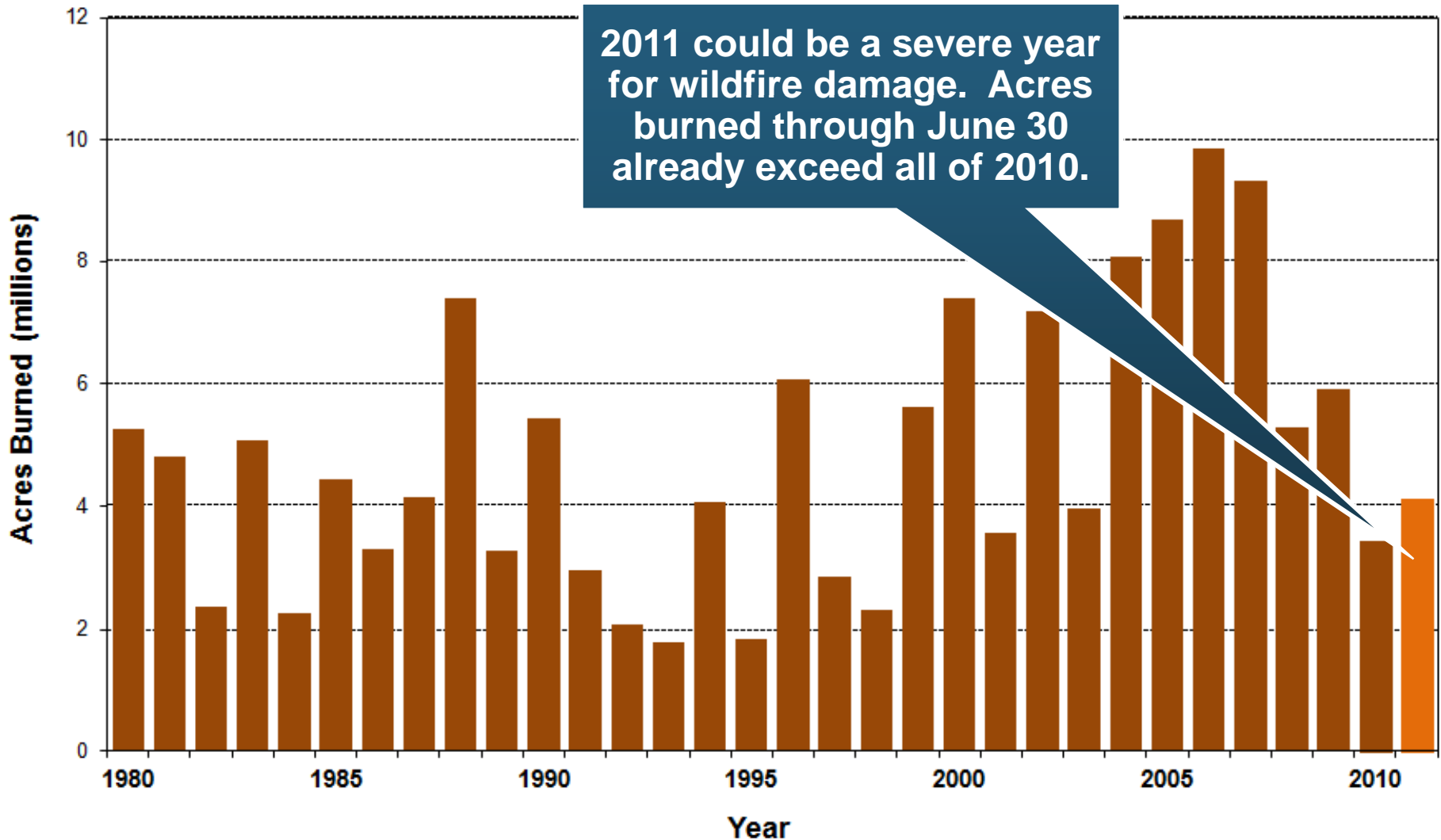
*Through June 30, 2011.

Source: Property Claims Service, MR NatCatSERVICE

U.S. Winter Storm Loss Trends, 1980 – 2010 (Annual Totals) vs. First Half 2011



U.S. Acreage Burned by Wildfires, 1980 – 2010 (Annual Totals) vs. First Half 2011



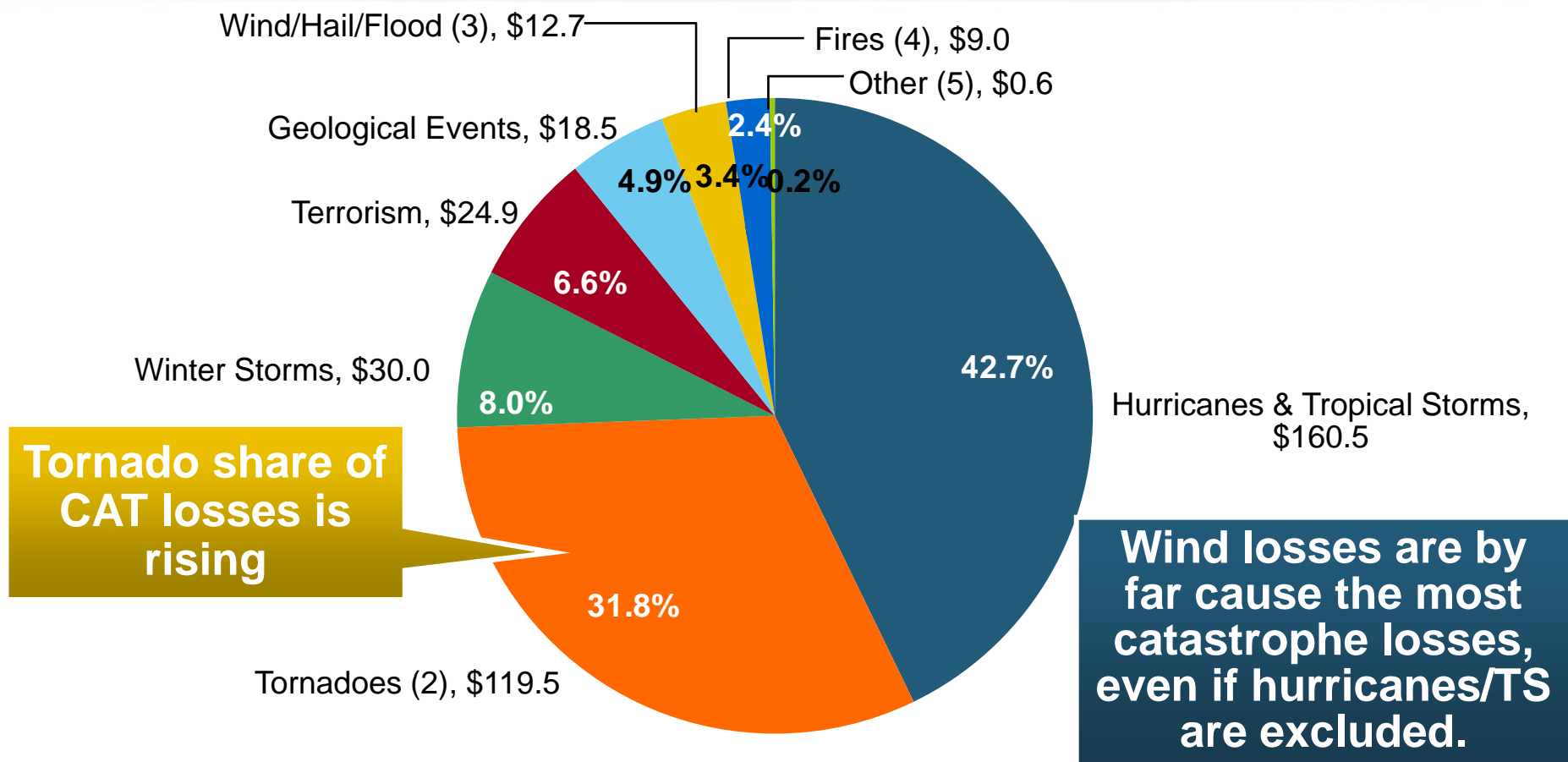
Notable Wildfires in 2011

April – June

- ***Texas: Millions of acres burned in west and central Texas. Over 500 homes and businesses destroyed, \$250 million insured loss.***
- Arizona and New Mexico: “Wallow” fire largest in AZ history at 538,000 acres, Las Conchas fire near Los Alamos, 30 buildings destroyed.



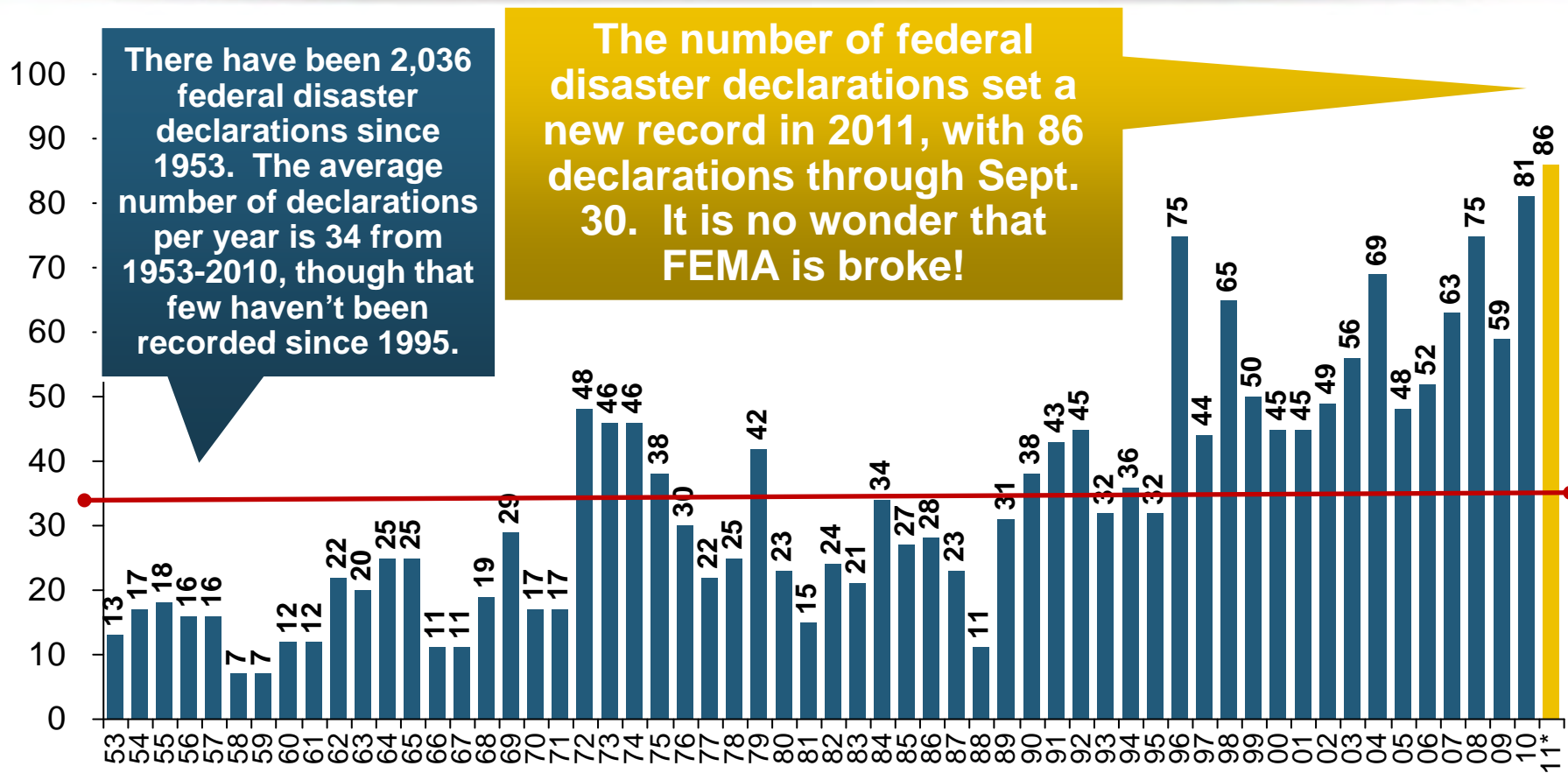
Inflation Adjusted U.S. Catastrophe Losses by Cause of Loss, 1990–2011:H1¹



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.

Number of Federal Disaster Declarations, 1953-2011*

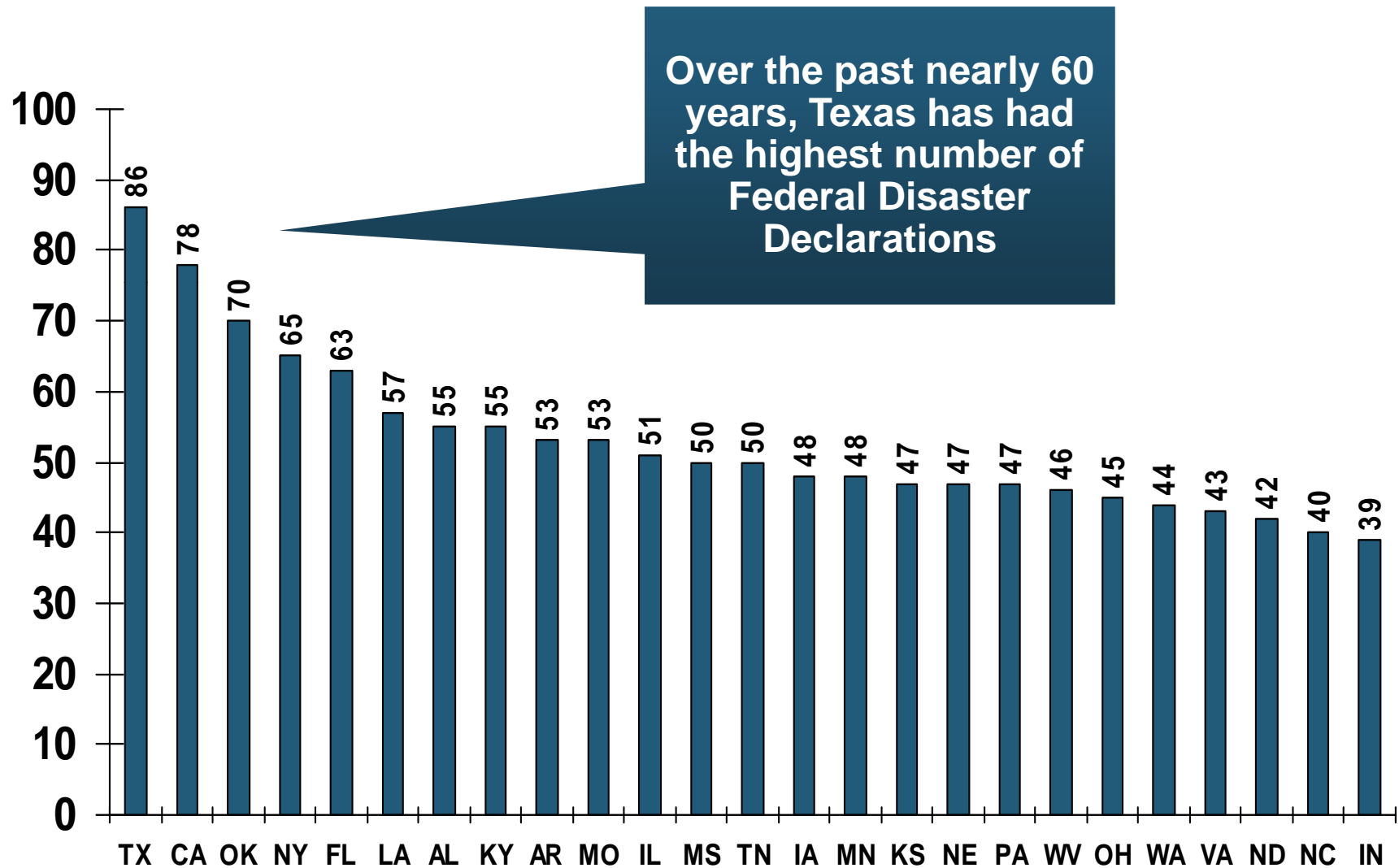


The Number of Federal Disaster Declarations Is Rising and Set a New Record in 2011

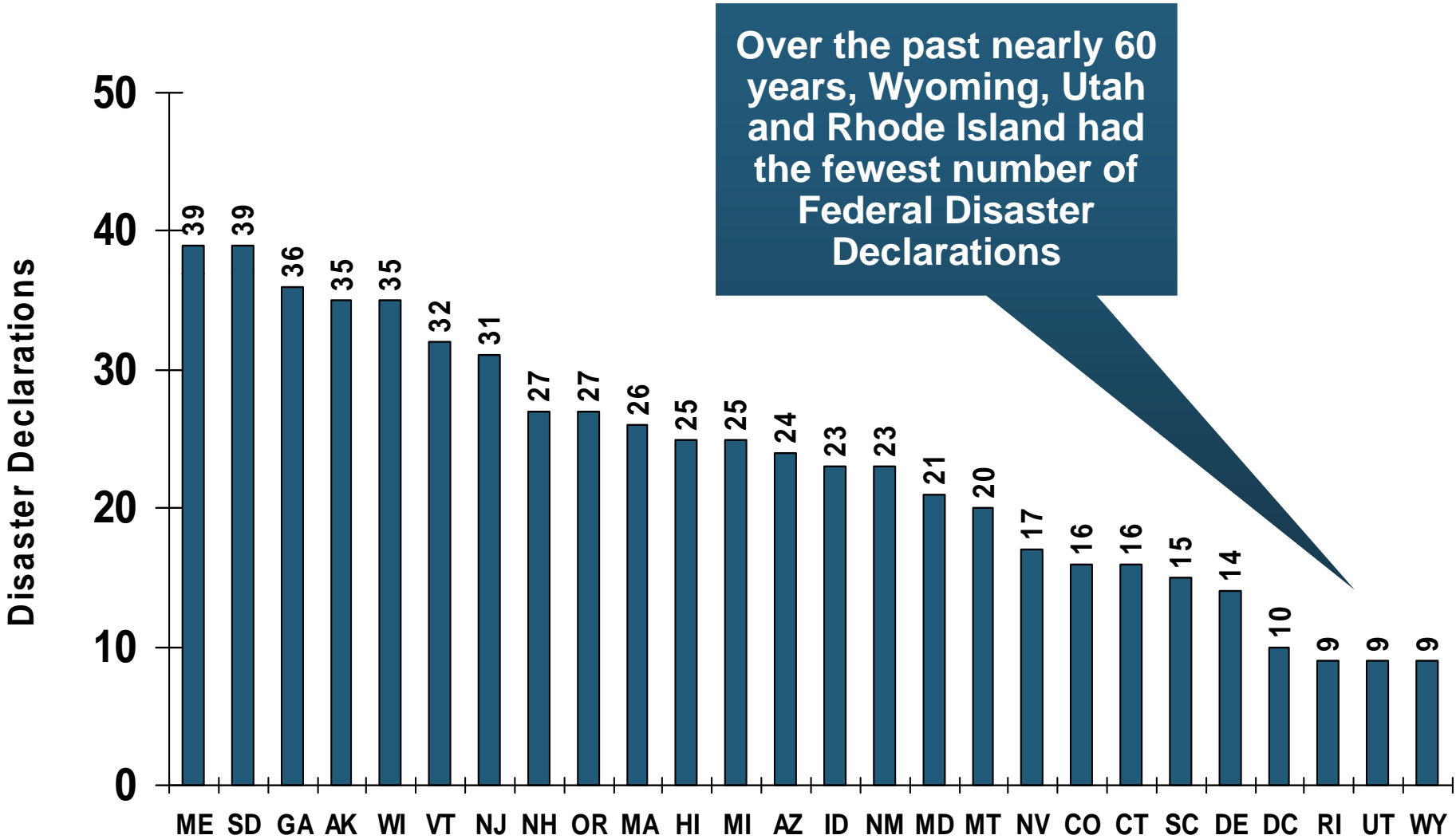
*Through September 30, 2011.

Source: Federal Emergency Management Administration: http://www.fema.gov/news/disaster_totals_annual.fema ; Insurance Information Institute.

Federal Disasters Declarations by State, 1953 – Sept. 30, 2011: Highest 25 States



Federal Disasters Declarations by State, 1953 – Sept. 30, 2011*: Lowest 25 States



Source: FEMA: http://www.fema.gov/news/disaster_totals_annual.fema; Insurance Information Institute.



Major Lesson of 2011 Global Catastrophes: Vulnerability of Supply Chains

**Catastrophe Can Produce
Costly Disruptions, but
Solutions Are Available**

Risk Management Techniques for Managing Supply Chain Disruptions

■ Identification of Risk

- ◆ Conduct thorough supply chain mapping exercise
- ◆ Look at processes as they come together to create final products
- ◆ Look in reverse: starting with where profits are generated and work backwards to identify greatest financial threats

■ Avoidance

- ◆ ***Remove the threat of exposure to the supply chain***

■ Mitigation

- ◆ Reduce the threat associated with exposures

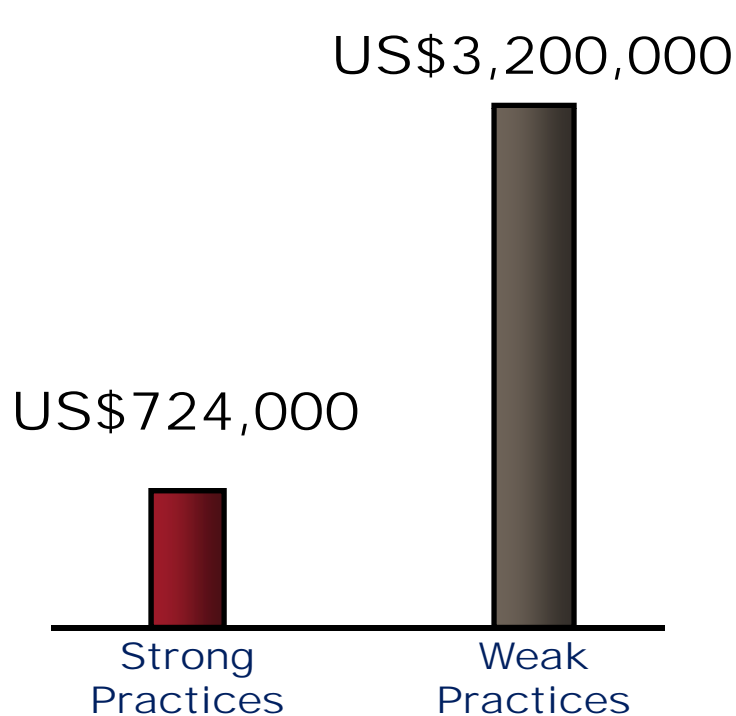
■ Manage

- ◆ Includes transfer of risk through insurance

If Fail to Manage the Risk, the Consequences Can Be Dire...

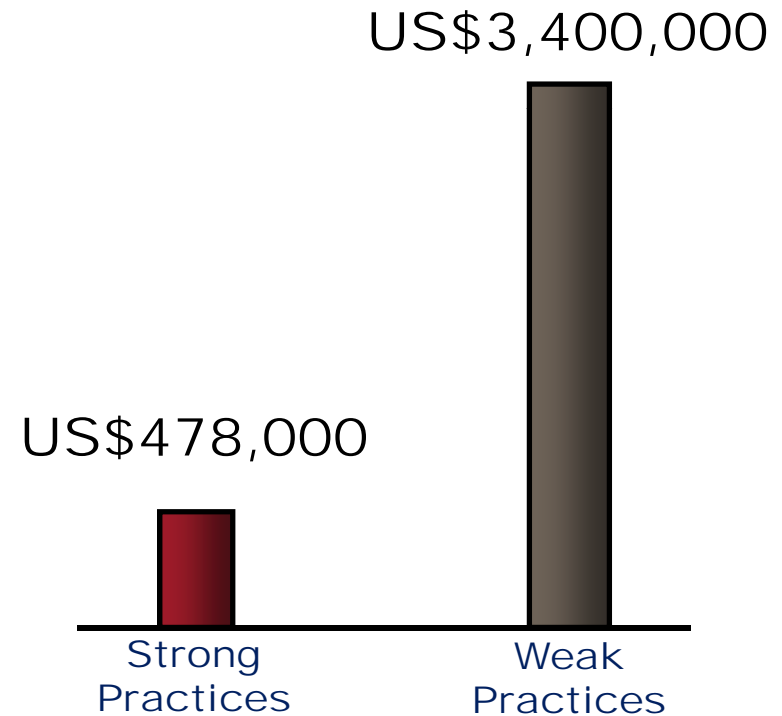
Fire

Physical Risk Management
Practices versus Ave. Loss
Severity (2005-08)



Natural Catastrophes

Physical Risk Management Practices
versus Average Loss Severity (2005-08)



- Avoid or mitigate the supply chain exposures
- Manage the financial impact
- Seize the opportunity

Avoid or Mitigate the Interruption

- Thoroughly understand your supply chain at every tier – loss control and business impact analysis
- Map the manufacturing process
- Identify weaknesses
- Harden facilities, owned or otherwise
- Duplicate if necessary
- Overlay with financial mapping
- Define acceptable risk

- **Requires top level commitment**
- **Must engage multiple disciplines**
 - ◆ Governance
 - ◆ Risk tolerance
 - ◆ Finance and balance sheet considerations
 - ◆ Manufacturing
 - ◆ Logistics
 - ◆ Sales and Marketing
 - ◆ Human Resources
 - ◆ Risk Management
 - ◆ And More!

- *Part* of the solution
- Insurance product is evolving
- Traditionally, physical damage, business interruption, CTE
- Business Interruption, two flavors
 - ◆ Gross earnings
 - ◆ Gross profits
- CTE – Typically direct and/or named, first tier

- Solutions continue to be created
 - ◆ Broad master global insurance policy (DIC & DIL)
 - ◆ First party property coverage
 - ◆ Time element select/extended period of liability
 - ◆ Contingent time element
 - ◆ Contingent time element extended

- Solutions continue to be created (*cont.*)
 - ◆ Service interruption
 - ◆ On premises services
 - ◆ Civil or military authority (typically 30 days/5 miles)
 - ◆ Ingress/egress
 - ◆ Computer systems physical/non physical damage



The BIG Question: When Will the Market Turn?

Are Catastrophes and Other Factors Pressuring Insurance Markets?

Criteria Necessary for a “Market Turn”: All Four Criteria Must Be Met

Criteria	Status	Comments
Sustained Period of Large Underwriting Losses	<i>Early Stage, Inevitable</i>	<ul style="list-style-type: none"> • Apart from Q2:2011, overall p/c underwriting losses remain modest • Combined ratios (ex-Q2 CATs) still in low 100s (vs. 110+ at onset of last hard market) • Prior-year reserve releases continue reduce u/w losses, boost ROEs
Material Decline in Surplus/ Capacity	<i>Entered 2011 At Record High; Since Fallen</i>	<ul style="list-style-type: none"> • Surplus hit a record \$565B as of 3/31/11 • Fell by 1% in Q2 2011 • Little excess capacity remains in reinsurance markets • Weak growth in demand for insurance is insufficient to absorb much excess capacity
Tight Reinsurance Market	<i>Somewhat in Place</i>	<ul style="list-style-type: none"> • Much of the global “excess capacity” was eroded by cats • Higher prices in Asia/Pacific • Modestly higher pricing for US risks
Renewed Underwriting & Pricing Discipline	<i>Some Firming in Property, WC</i>	<ul style="list-style-type: none"> • Commercial lines pricing trends turning from negative to flat or up in some lines (property, WC) • Competition remains intense as many seek to maintain market share

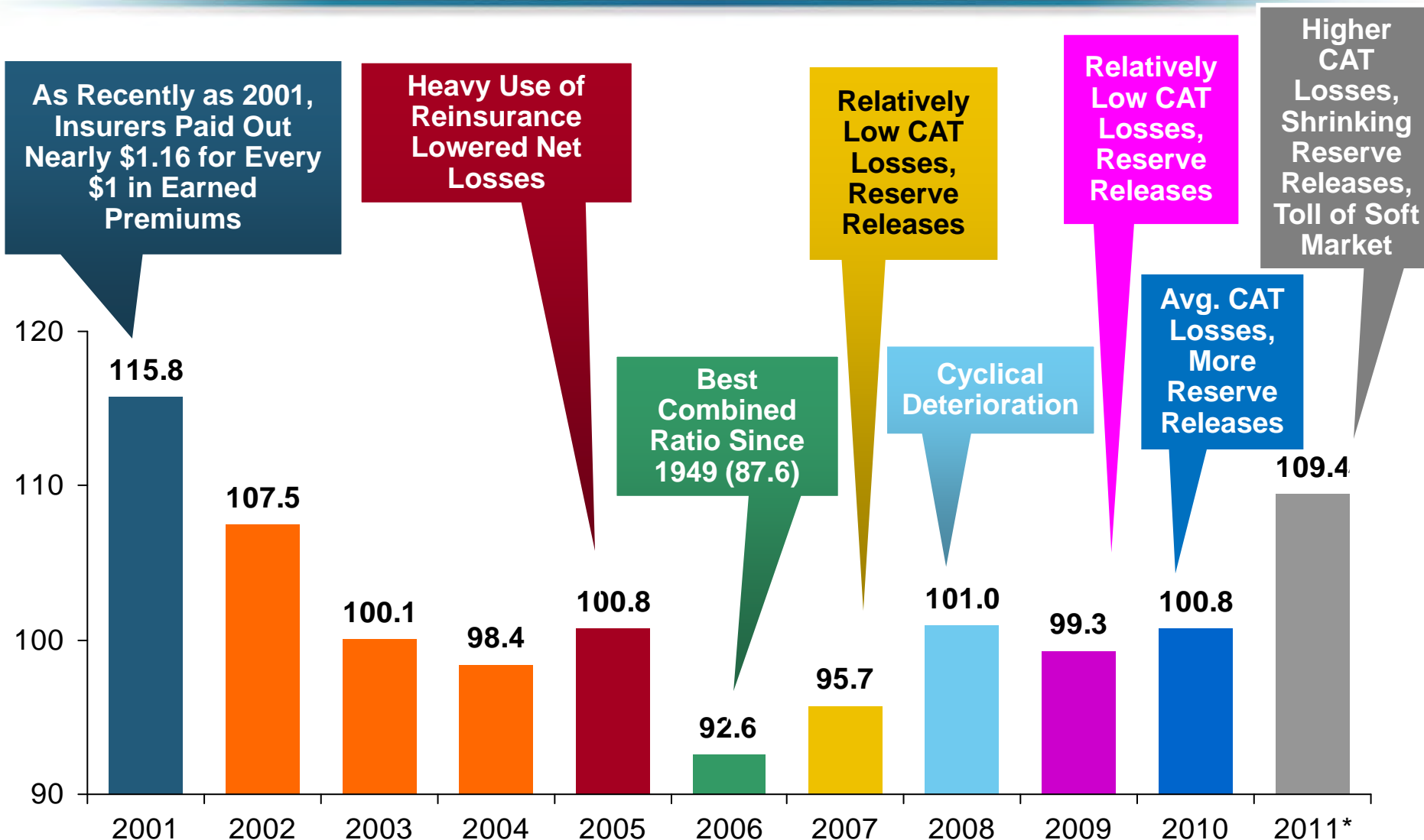
Do the Property Catastrophe Events of 2011 Impact Casualty Markets?

- **Unlikely that Record 2011 Property CAT Loss Will Impact Casualty Markets in Any Material Way**
- **Global P/C & Reinsurance Industries Entered 2011 w/ Record Capital**
 - ◆ Events so far in 2011 are earnings events, rather than capital events
- **Natural Catastrophe and Casualty Risks Are Largely Uncorrelated**
 - ◆ Risks are different
 - ◆ Geographically, mostly distinct primary carriers: Japan-Australia-NZ-US
 - ◆ Casualty markets generally don't influence property markets
- **Property and Casualty Risks Are Largely Siloed**
- **Record Property Losses in 2004/2005 Did Not Impact Casualty Mkts.**
- **Casualty Markets Have Their Own Issues**
 - ◆ Tort environment
 - ◆ Inflation
 - ◆ Public policy

1. UNDERWRITING

**Have Underwriting Losses
Been Large Enough for Long
Enough to Turn the Market?**

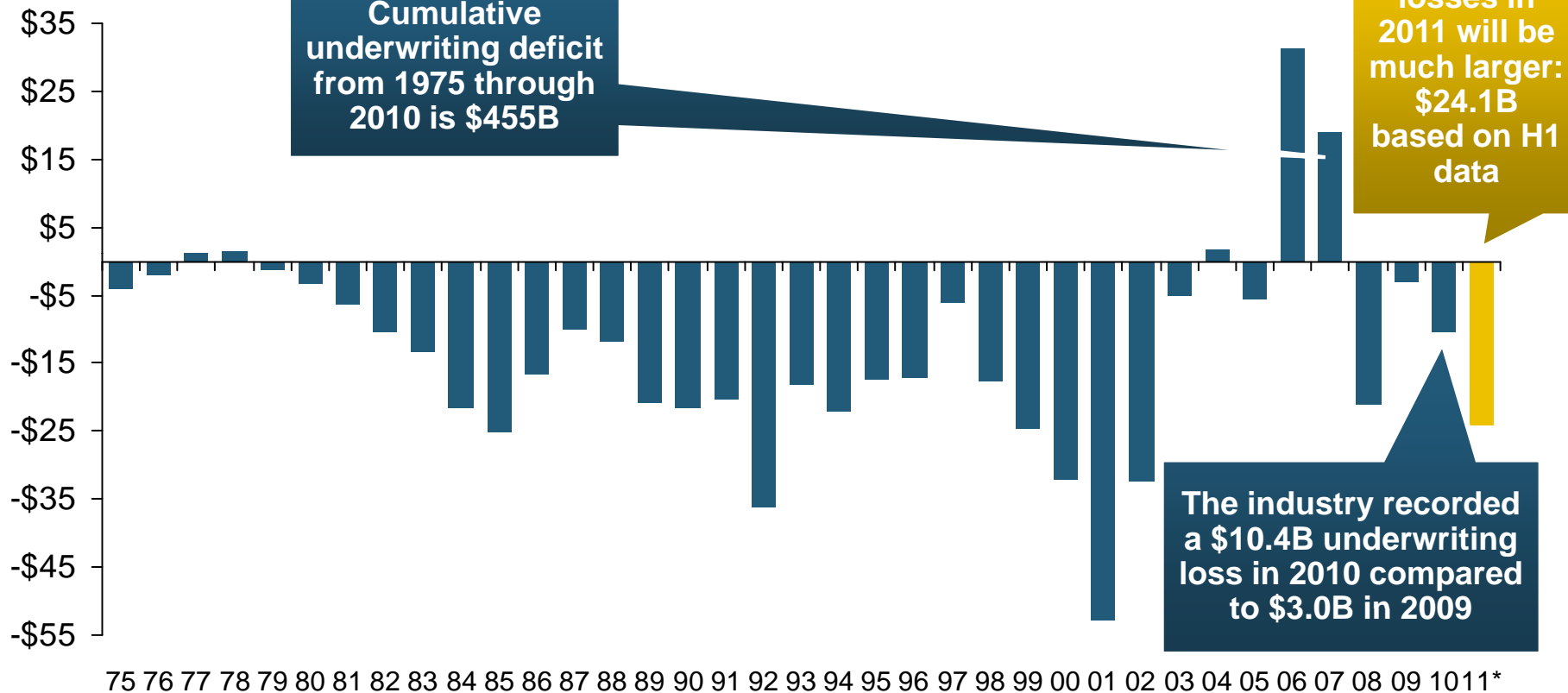
P/C Insurance Industry Combined Ratio, 2001–2011:H1*



* Excludes Mortgage & Financial Guaranty insurers 2008--2011. Including M&FG, 2008=105.1, 2009=100.7, 2010=102.4, 2011=110.5
Sources: A.M. Best, ISO.; III Estimated for 2011:H1 (Q1 actual ex-M&FG was 102.2).

Underwriting Gain (Loss) 1975–2011*

(\$ Billions)



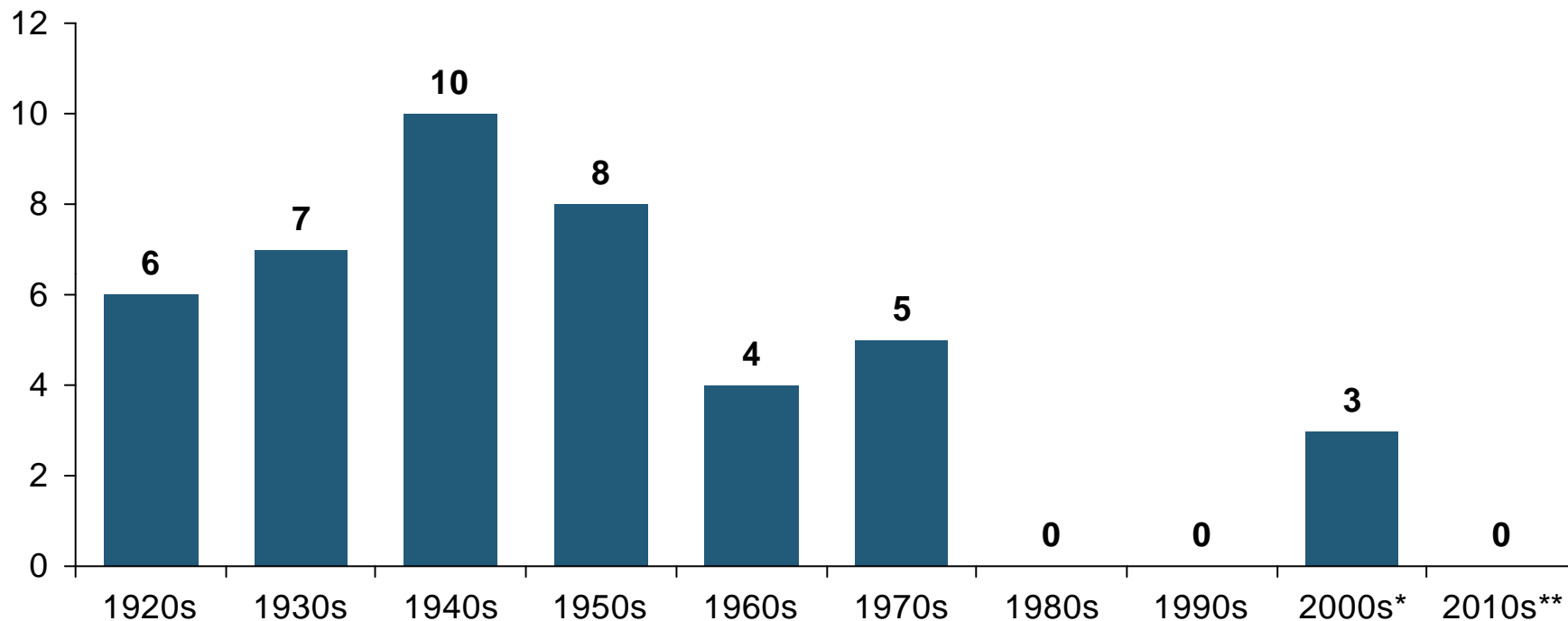
**Large Underwriting Losses Are *NOT* Sustainable
in Current Investment Environment**

* Includes mortgage and financial guaranty insurers in all years. 2011 figure is actual H1 underwriting losses of \$24.098 billion.

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

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

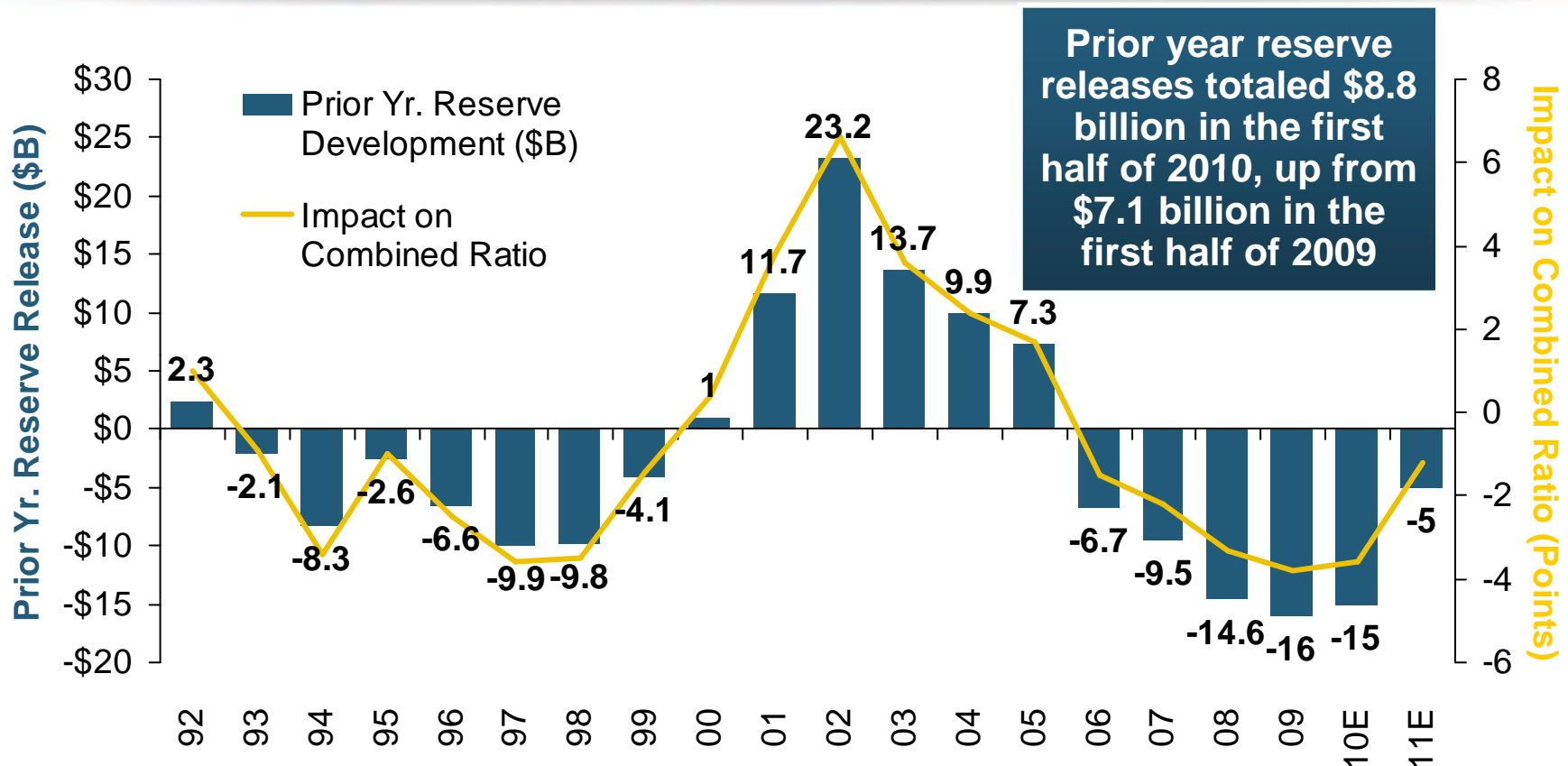
total to 4 years with an underwriting profit.

**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.

P/C Reserve Development, 1992–2011E



Prior year reserve releases totaled \$8.8 billion in the first half of 2010, up from \$7.1 billion in the first half of 2009

Reserve Releases Are Remained Strong in 2010 But Should Begin to Taper Off in 2011

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.

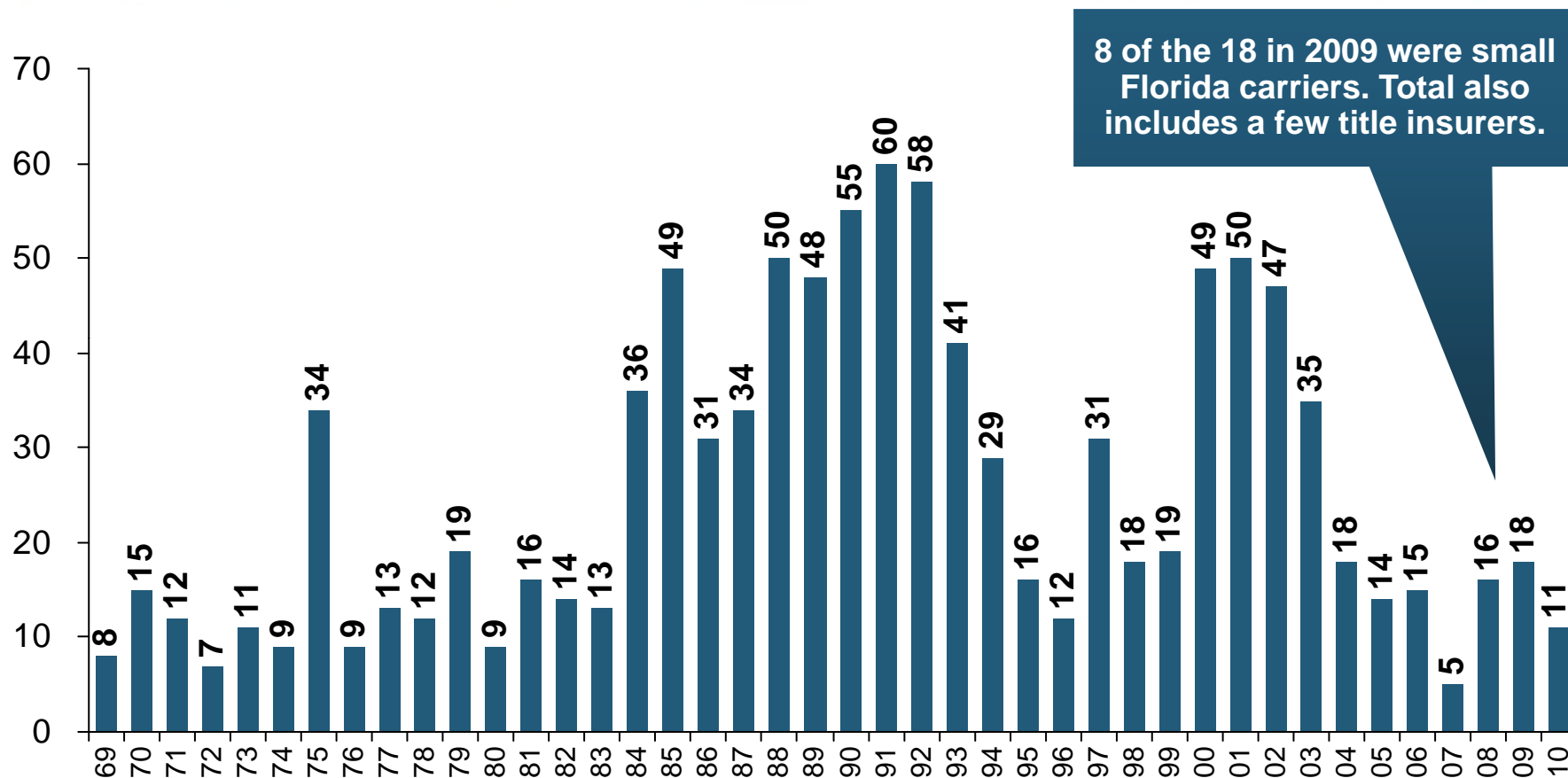
Sources: Barclay's Capital; A.M. Best.



Financial Strength & Underwriting

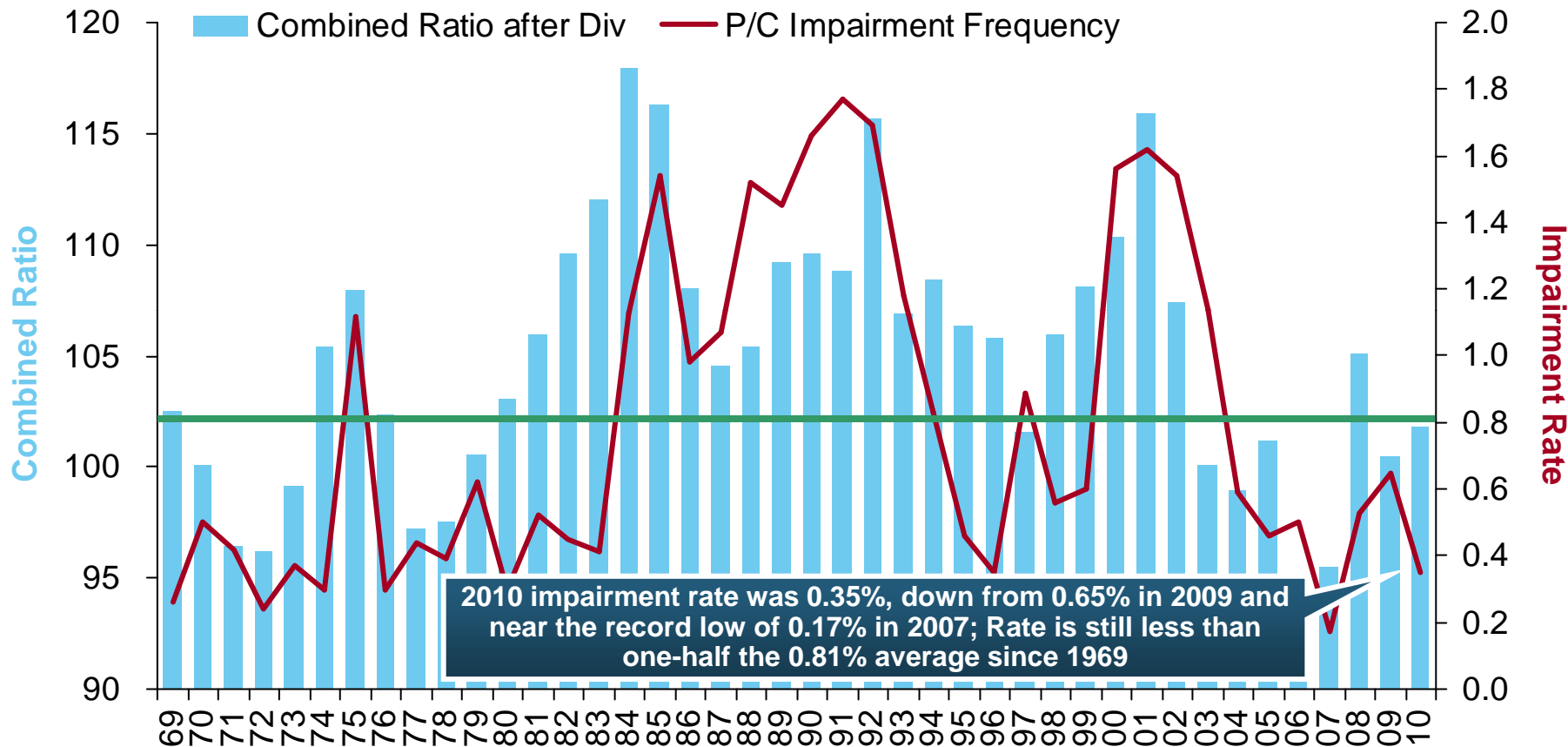
**Cyclical Pattern is P-C Impairment
History is Directly Tied to
Underwriting, Reserving & Pricing**

P/C Insurer Impairments, 1969–2010



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

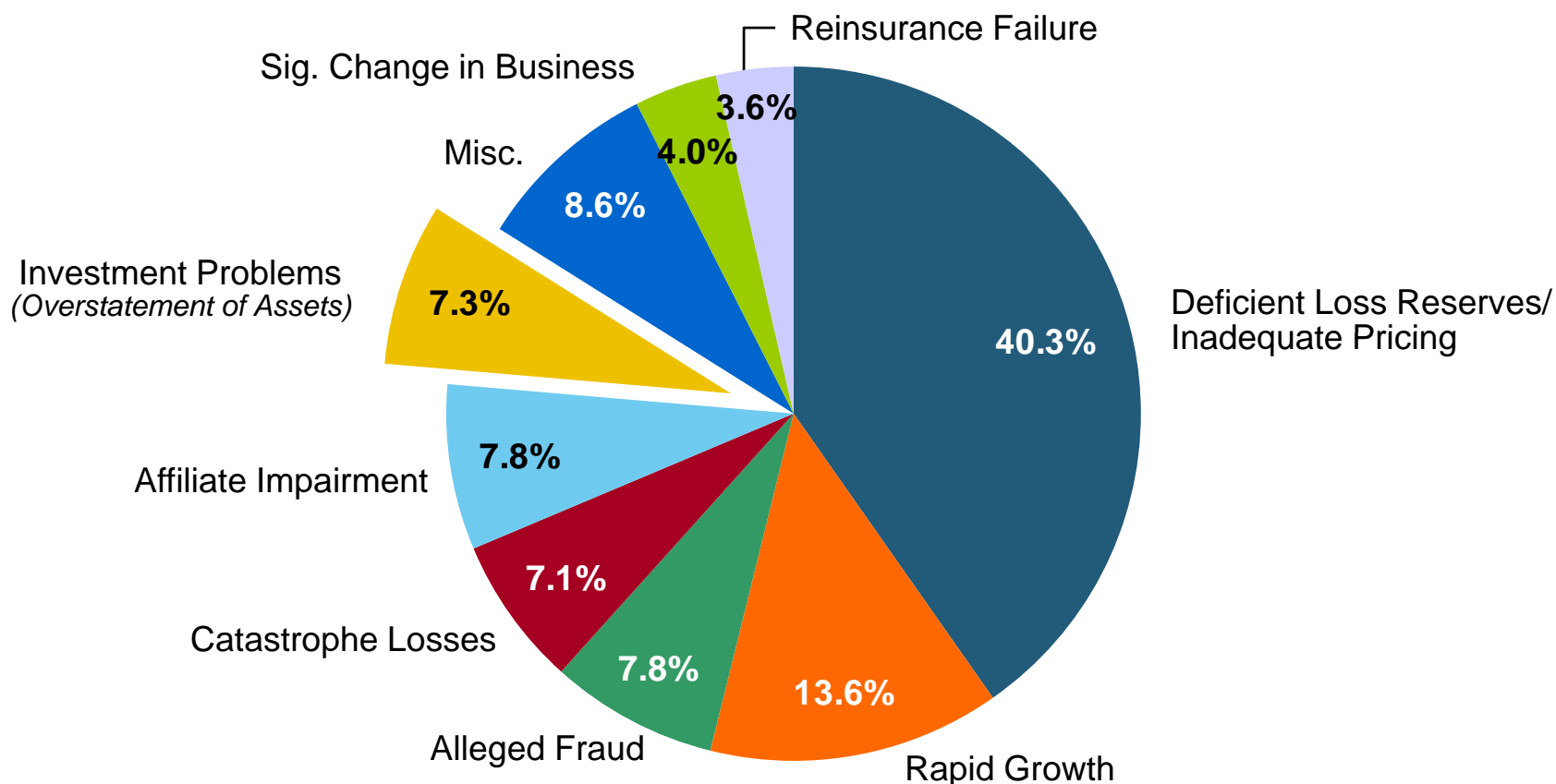
P/C Insurer Impairment Frequency vs. Combined Ratio, 1969-2010



Impairment Rates Are Highly Correlated With Underwriting Performance and Reached Record Lows in 2007

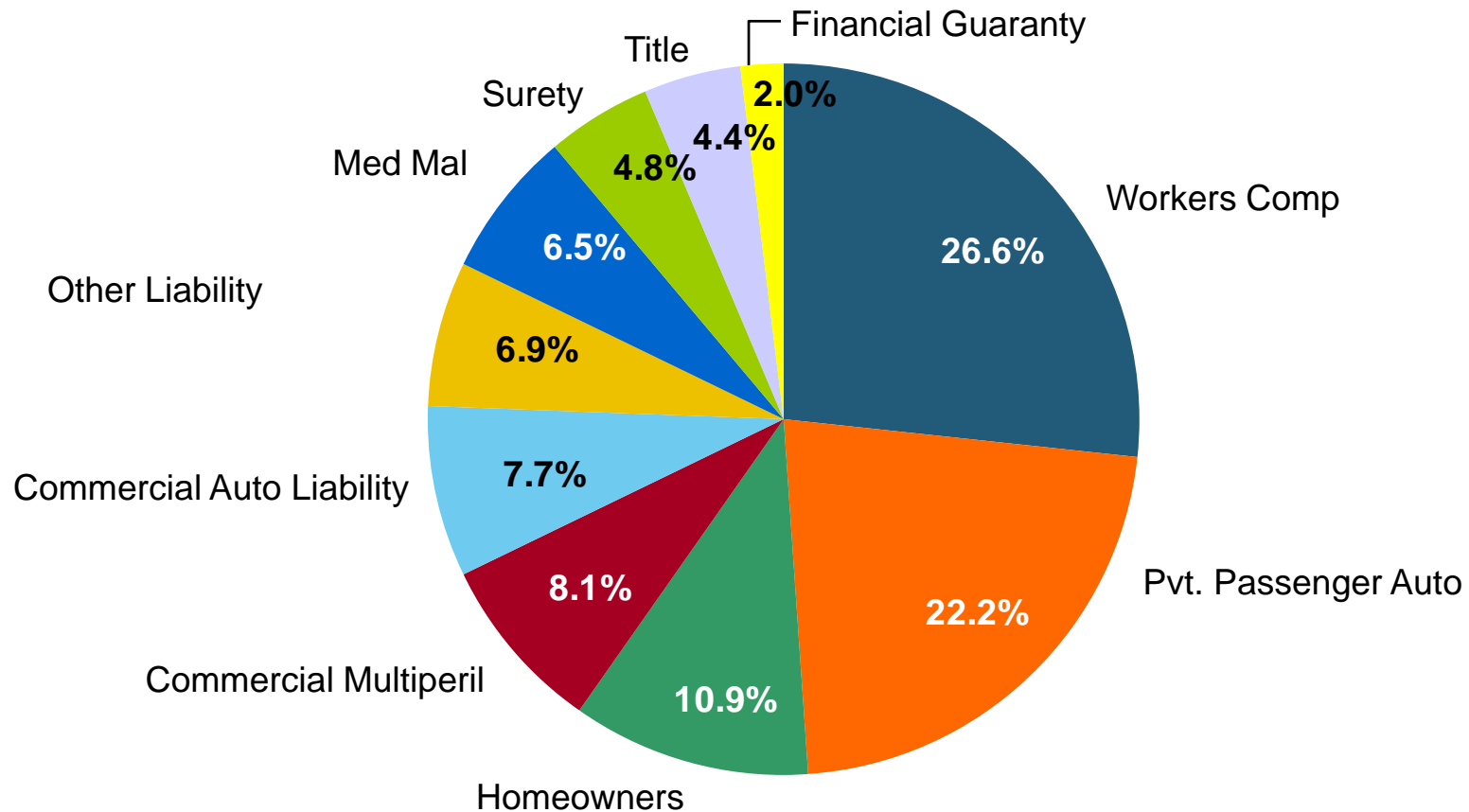
Reasons for US P/C Insurer Impairments, 1969–2010

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



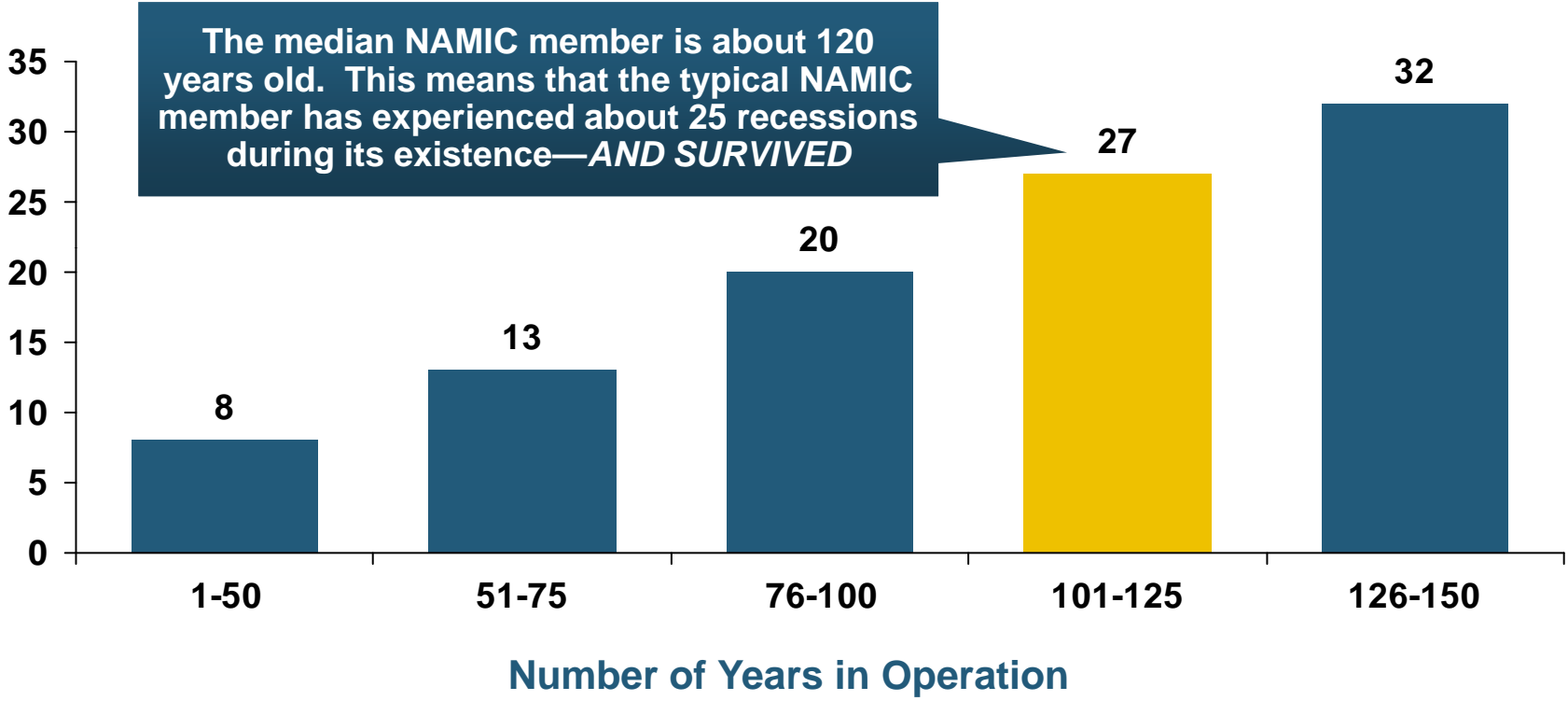
Top 10 Lines of Business for US P/C Impaired Insurers, 2000–2010

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



Mutual Insurers, Which Account for the Majority of Centenarian Insurers, Are True Survivors

Sources: Insurance Information Institute research from National Bureau of Economic Research data.



Performance by Segment: Commercial Lines & Reinsurance

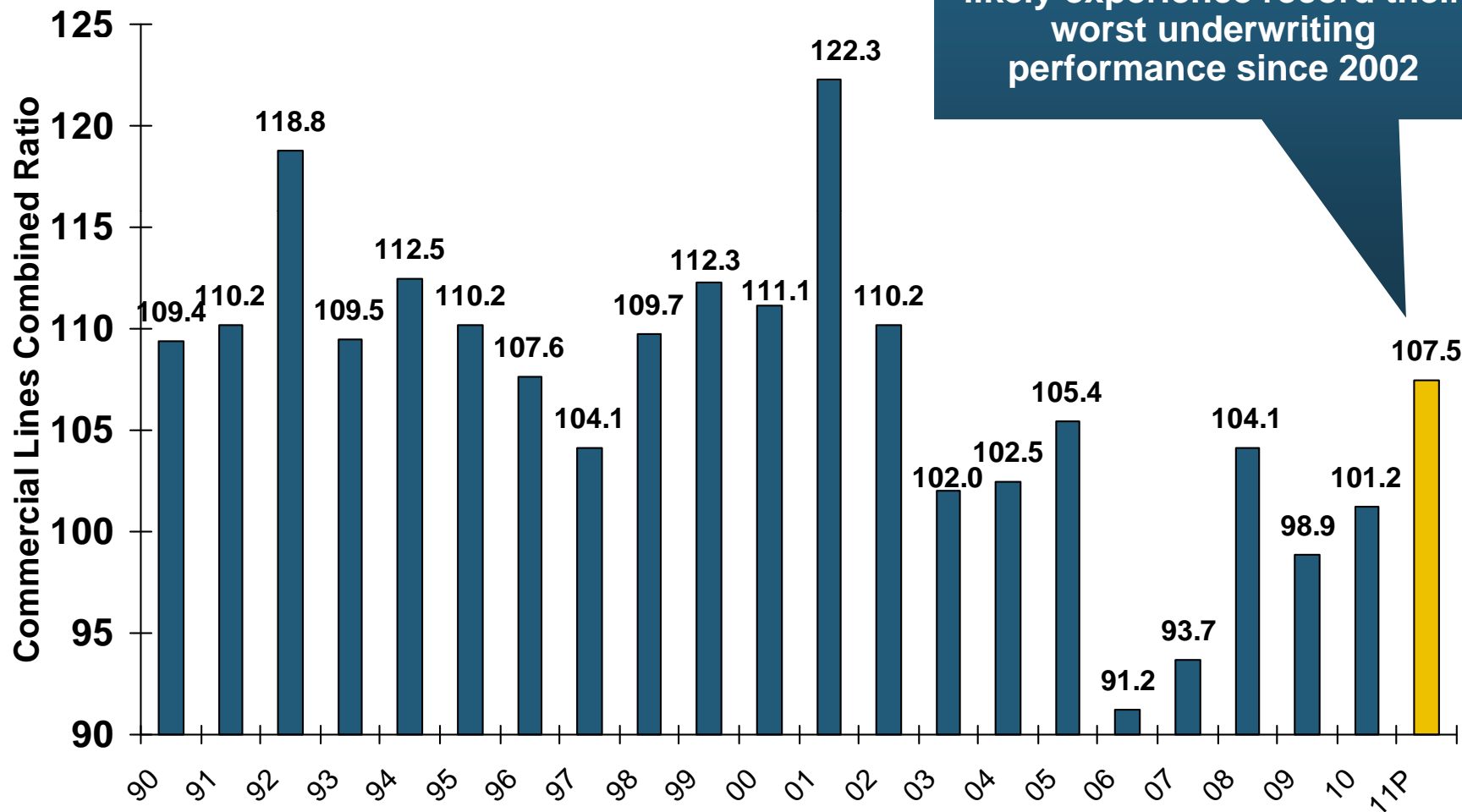
P/C Underwriting Results: 2008-2010P



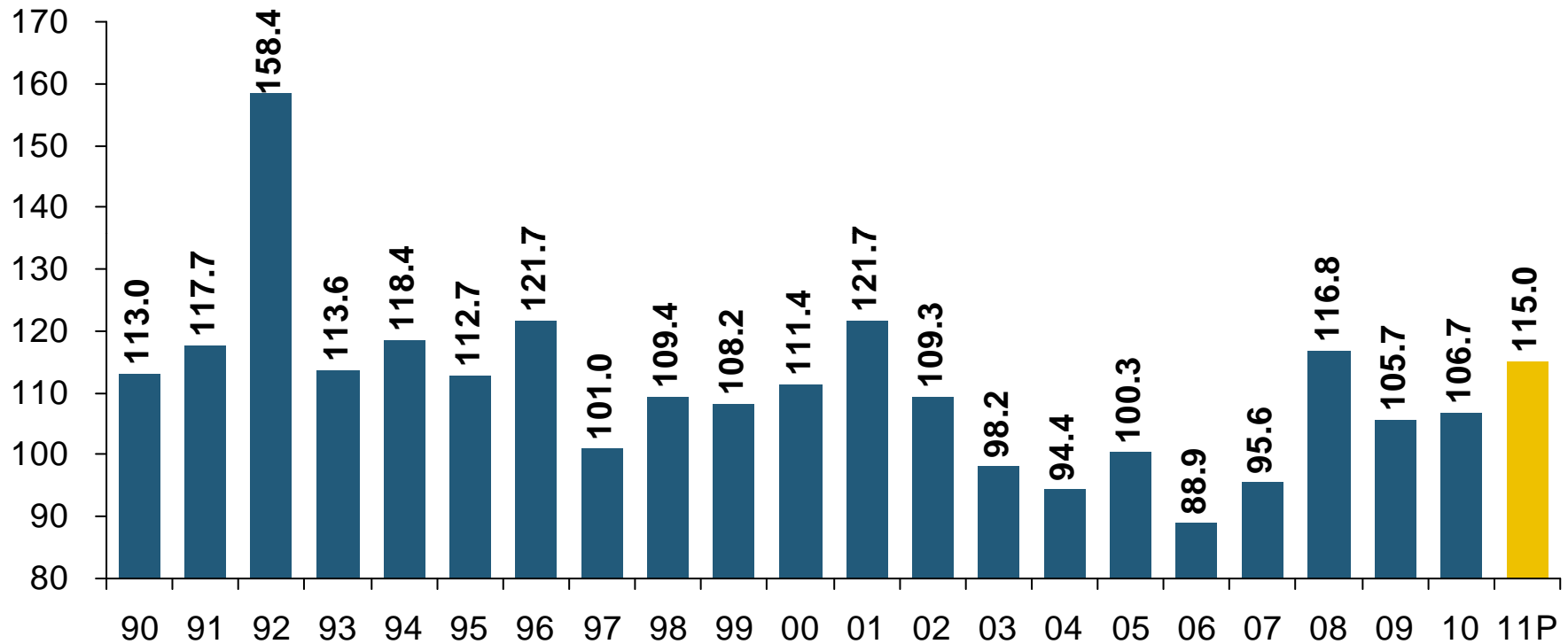
Line of Business	2008	2009	2010P
Personal Auto	100.3	101.3	101
Homeowners	117.0	105.6	107
Other Liability (incl. Prod Liab)	95	105	110
Workers Compensation	101	110.5	115
Commercial Multi Peril	104	97	101
Commercial Auto	96.8	99.5	98
Fire & Allied Lines (incl. EQ)	99	80	83
All Other Lines	113	96	101
Total P/C Industry	104	101	102

Source: All lines except WC for 2008-09, A.M. Best; Worker Comp., NCCI; 2010P data, ISO. Private carriers only.

Commercial Lines Combined Ratio, 1990-2011P

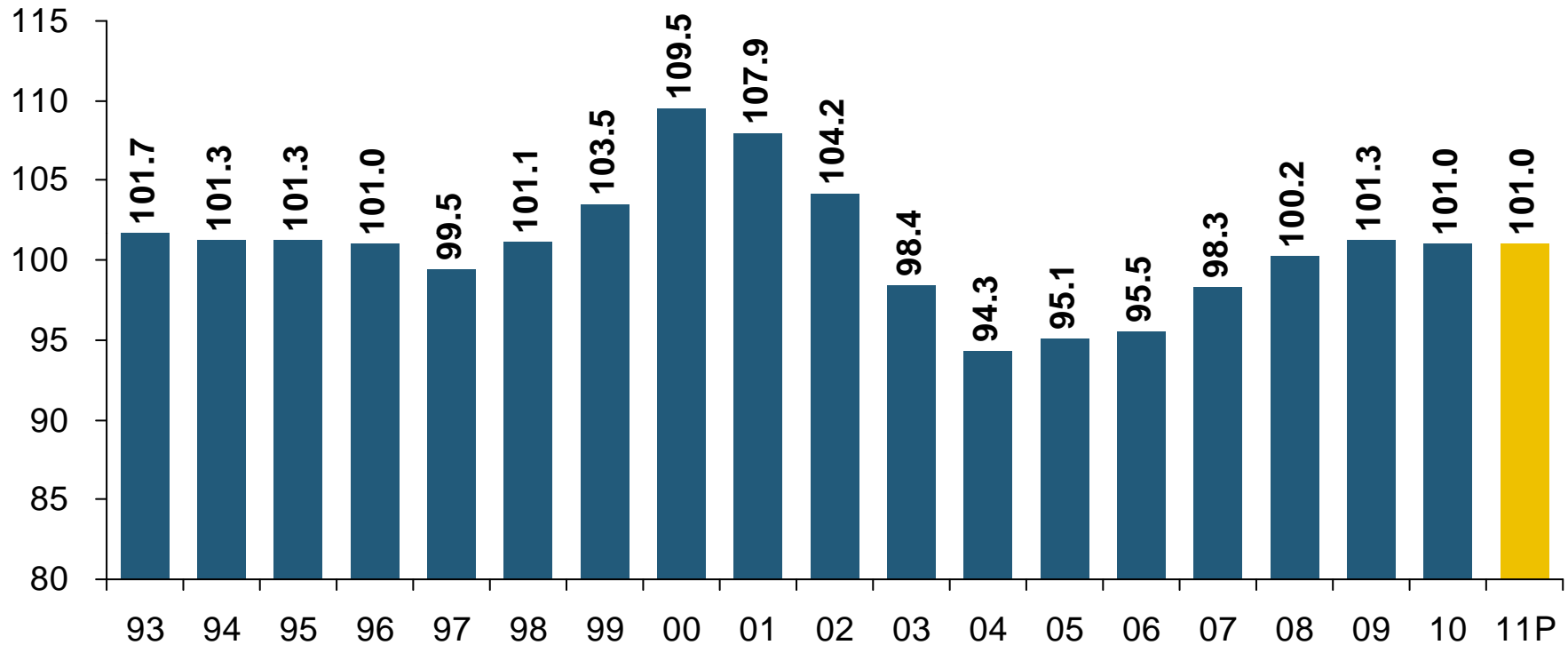


Homeowners Insurance Combined Ratio: 1990–2011P



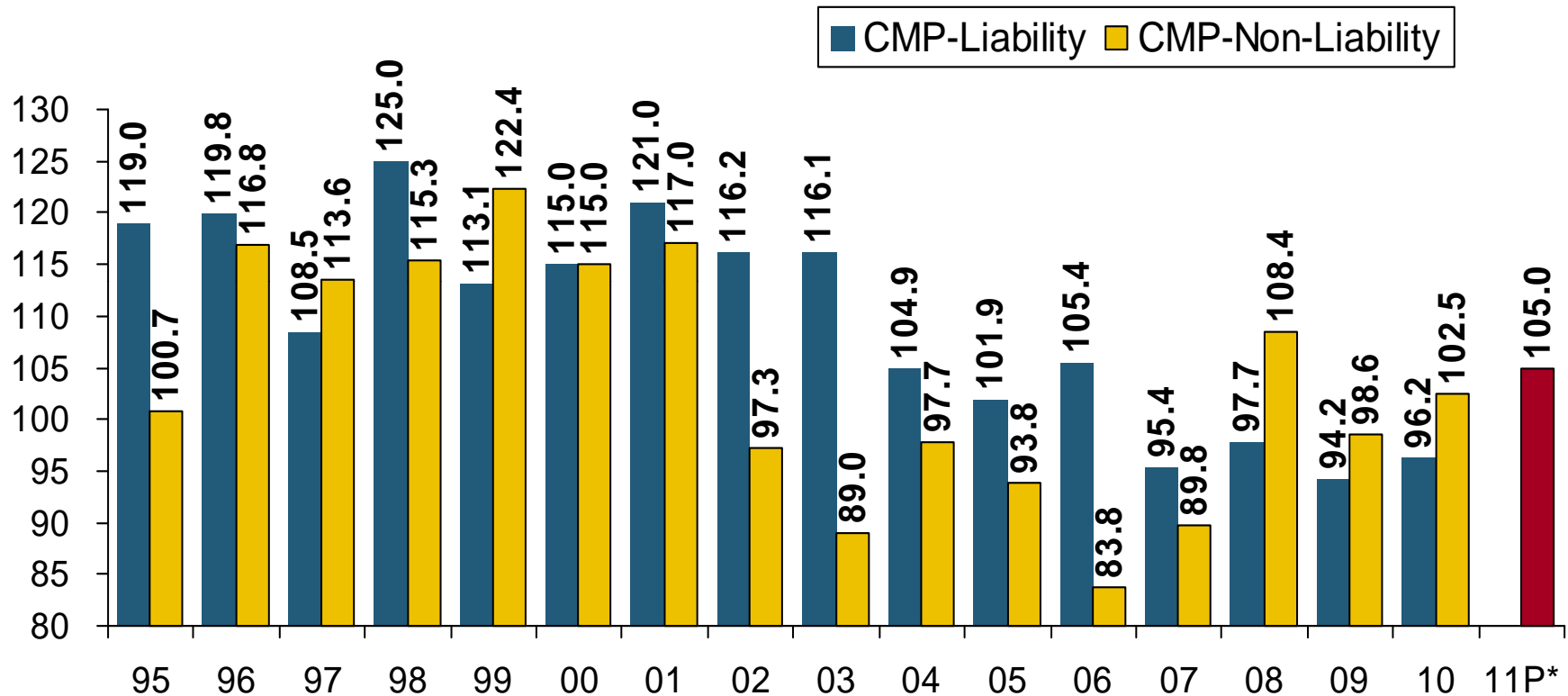
Homeowners Line Could Deteriorate in 2011 Due to Large Cat Losses. Extreme Regional Variation Can Be Expected Due to Local Catastrophe Loss Activity

Private Passenger Auto Combined Ratio: 1993–2011P



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

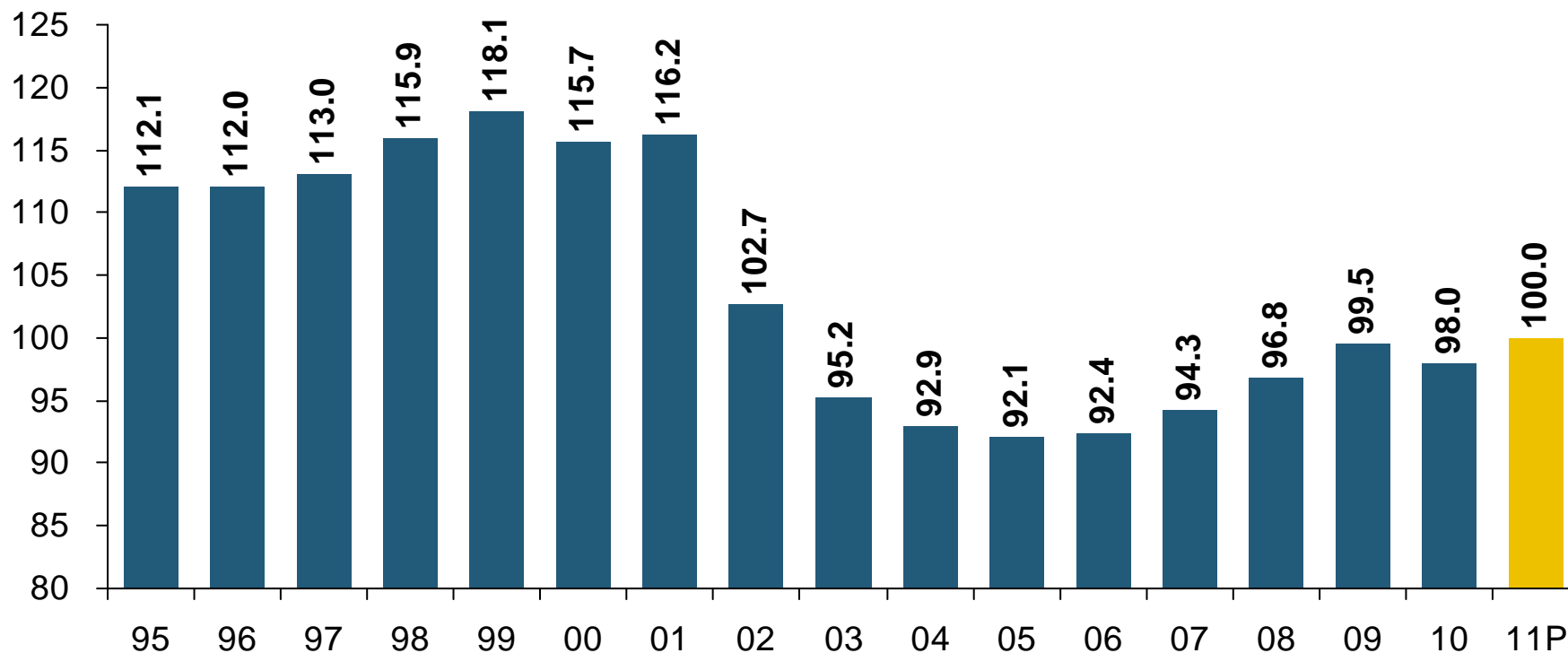
Commercial Multi-Peril Combined Ratio: 1995–2011P



Commercial Multi-Peril Underwriting Performance is Expected to Deteriorate Modestly

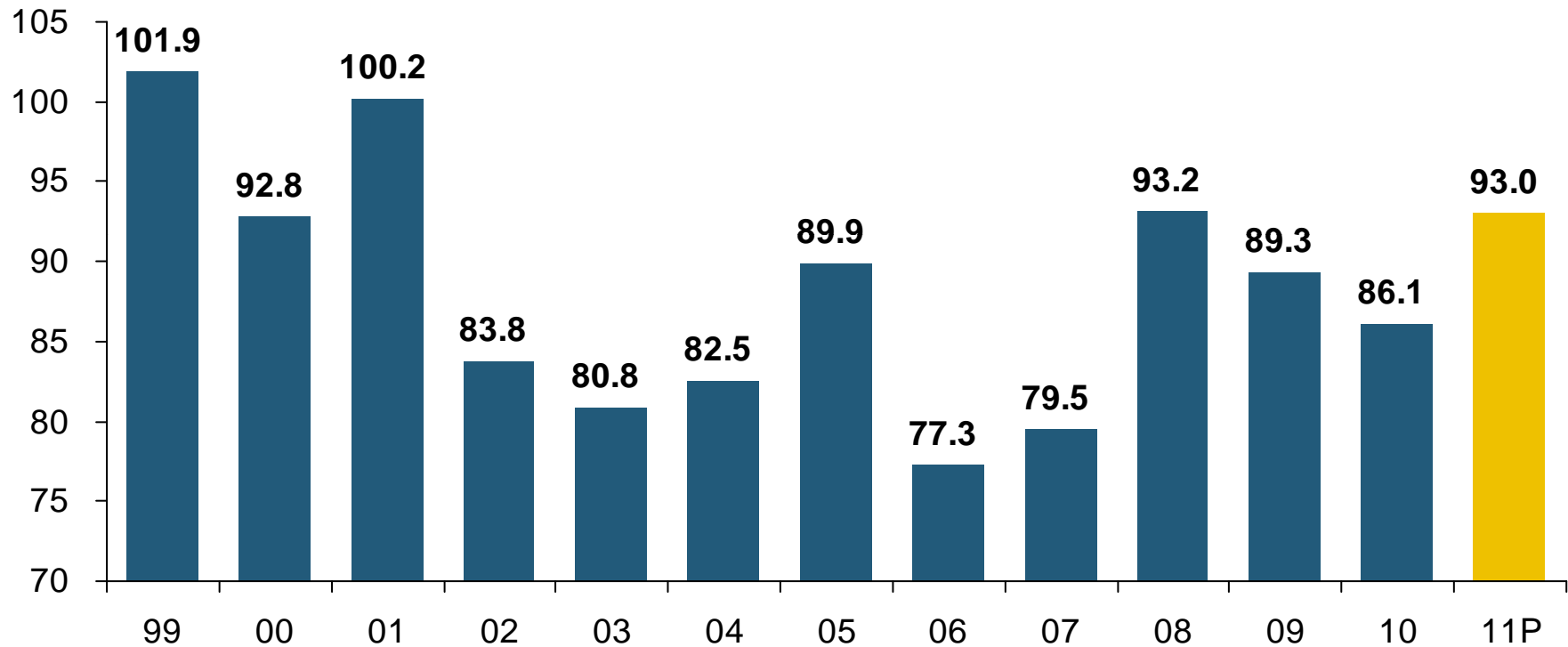
*2011P figure is III estimate for the combined liability and non-liability components.
Sources: A.M. Best; Insurance Information Institute.

Commercial Auto Combined Ratio: 1993–2011P



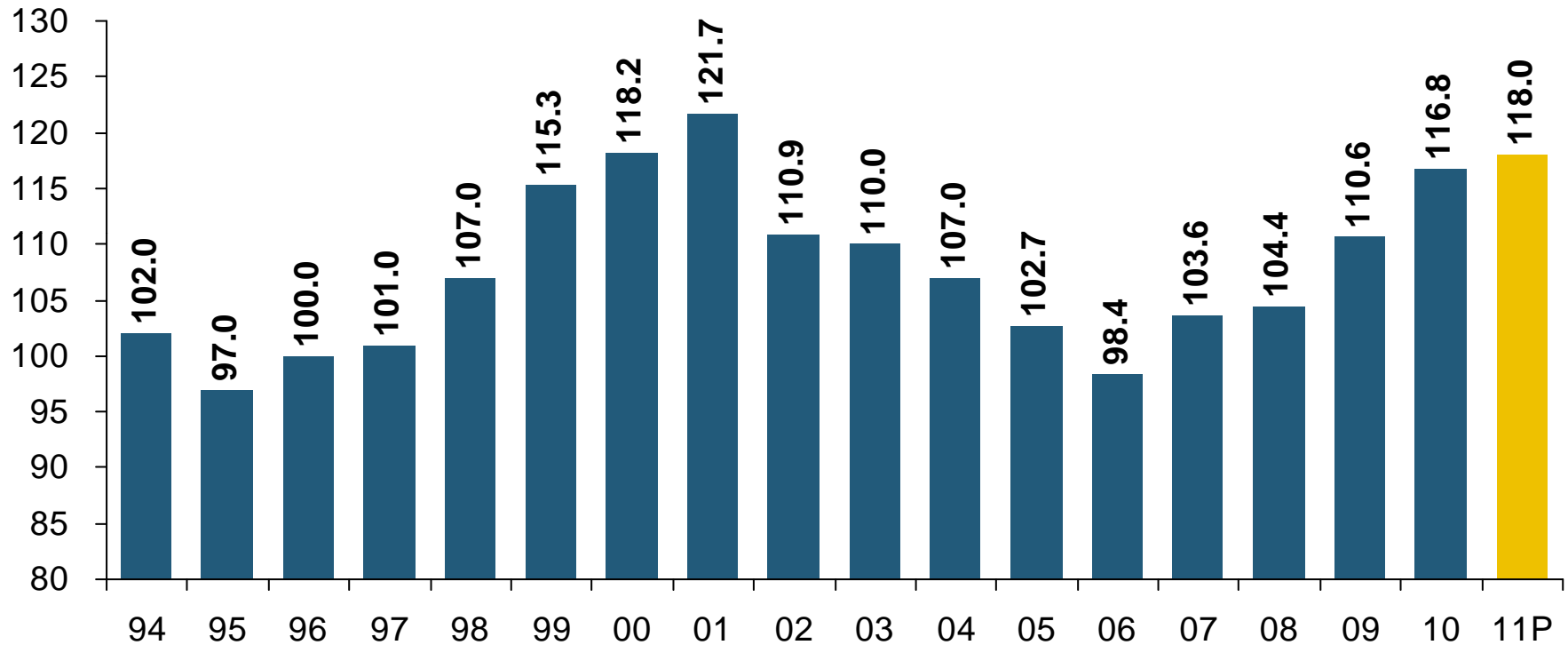
**Commercial Auto Underwriting Performance is
Expected to Deteriorate Modestly**

Inland Marine Combined Ratio: 1999–2011P



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

Workers Compensation Combined Ratio: 1994–2011P



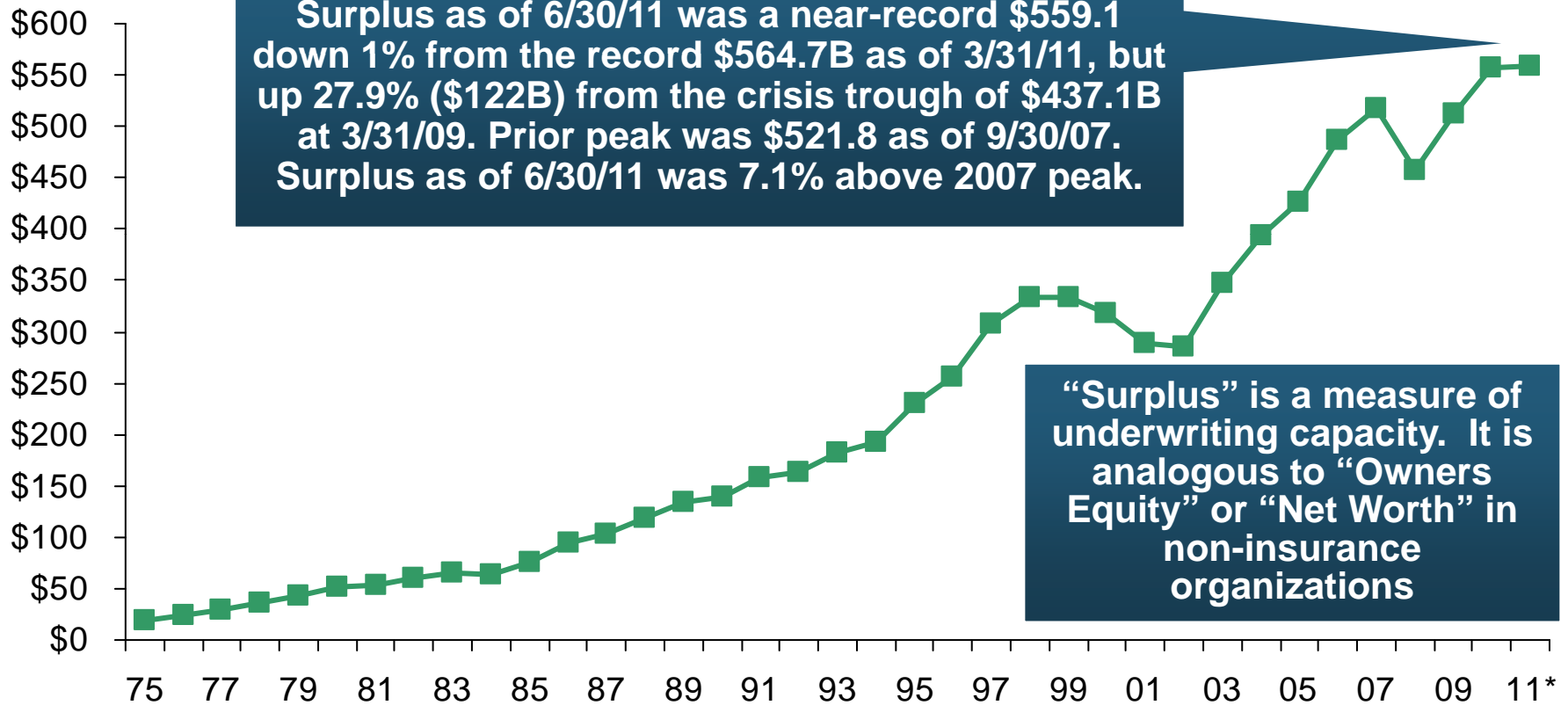
Workers Comp Underwriting Results Are Deteriorating Markedly and the Worst They Have Been in a Decade

2. SURPLUS/CAPITAL/CAPACITY

Have Large Global Losses Reduced Capacity in the Industry, Setting the Stage for a Market Turn?

US Policyholder Surplus: 1975–2011*

(\$ Billions)

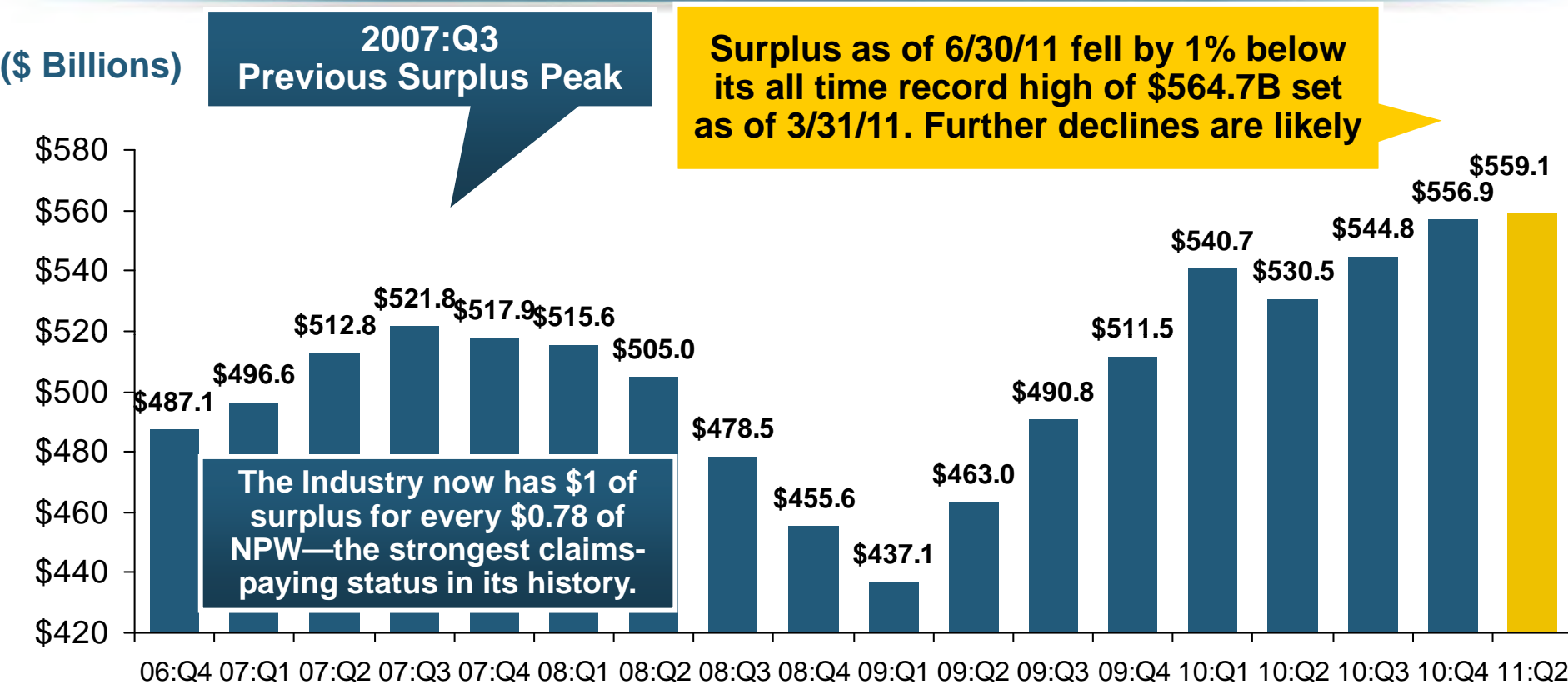


The Premium-to-Surplus Ratio Stood at \$0.78:\$1 as of 6/30/11, A Near Record Low (at Least in Recent History)**

* As of 6/30/11.

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

Policyholder Surplus, 2006:Q4–2011:Q2



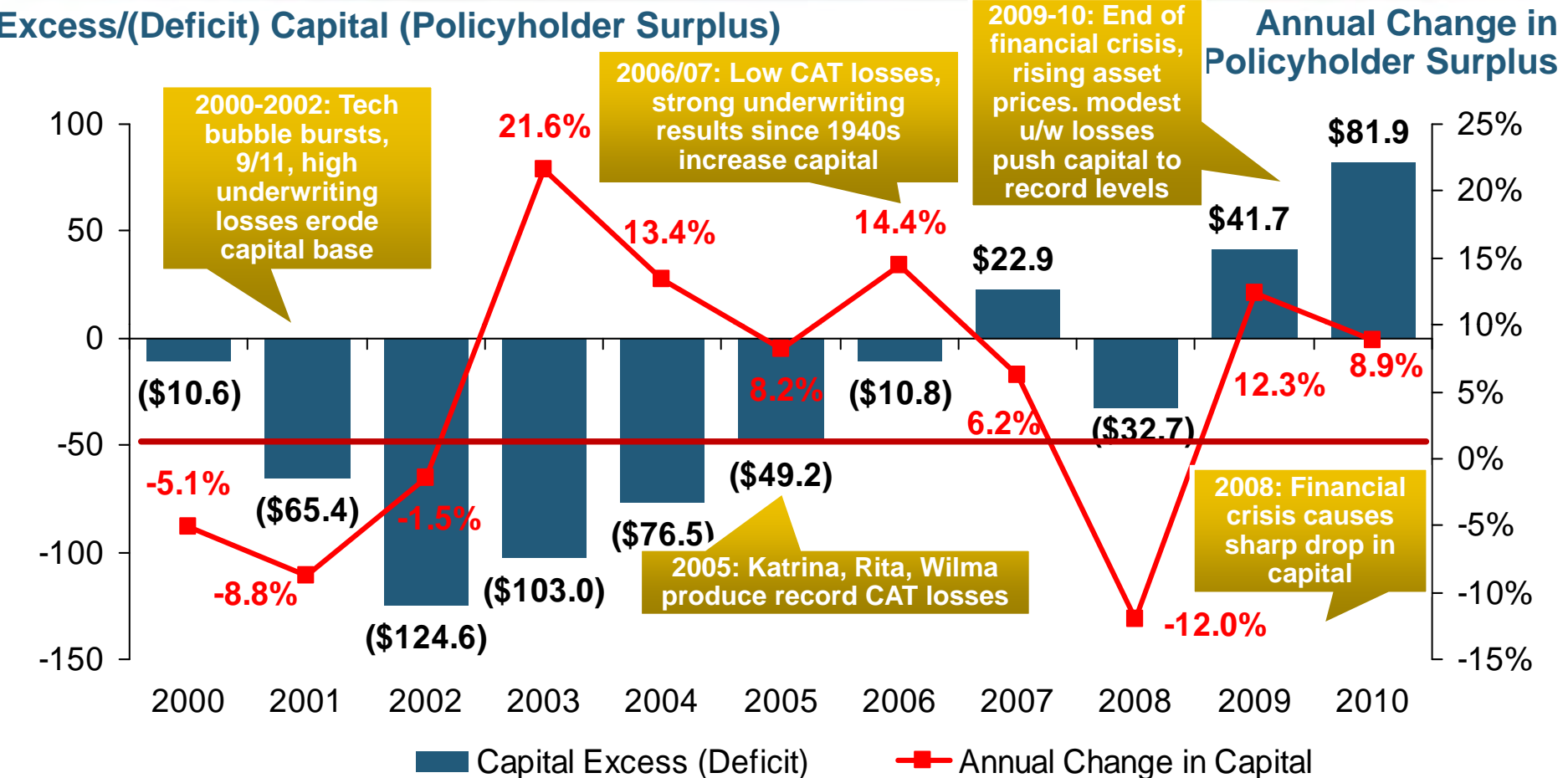
Quarterly Surplus Changes Since 2007:Q3 Peak

09:Q1: -\$84.7B (-16.2%)	10:Q2: +\$8.7B (+1.7%)
09:Q2: -\$58.8B (-11.2%)	10:Q3: +\$23.0B (+4.4%)
09:Q3: -\$31.0B (-5.9%)	10:Q4: +\$35.1B (+6.7%)
09:Q4: -\$10.3B (-2.0%)	11:Q1: +\$42.9B (+8.2%)
10:Q1: +\$18.9B (+3.6%)	11:Q2: +\$37.3B (+7.1%)

*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.

Sources: ISO, A.M. Best.

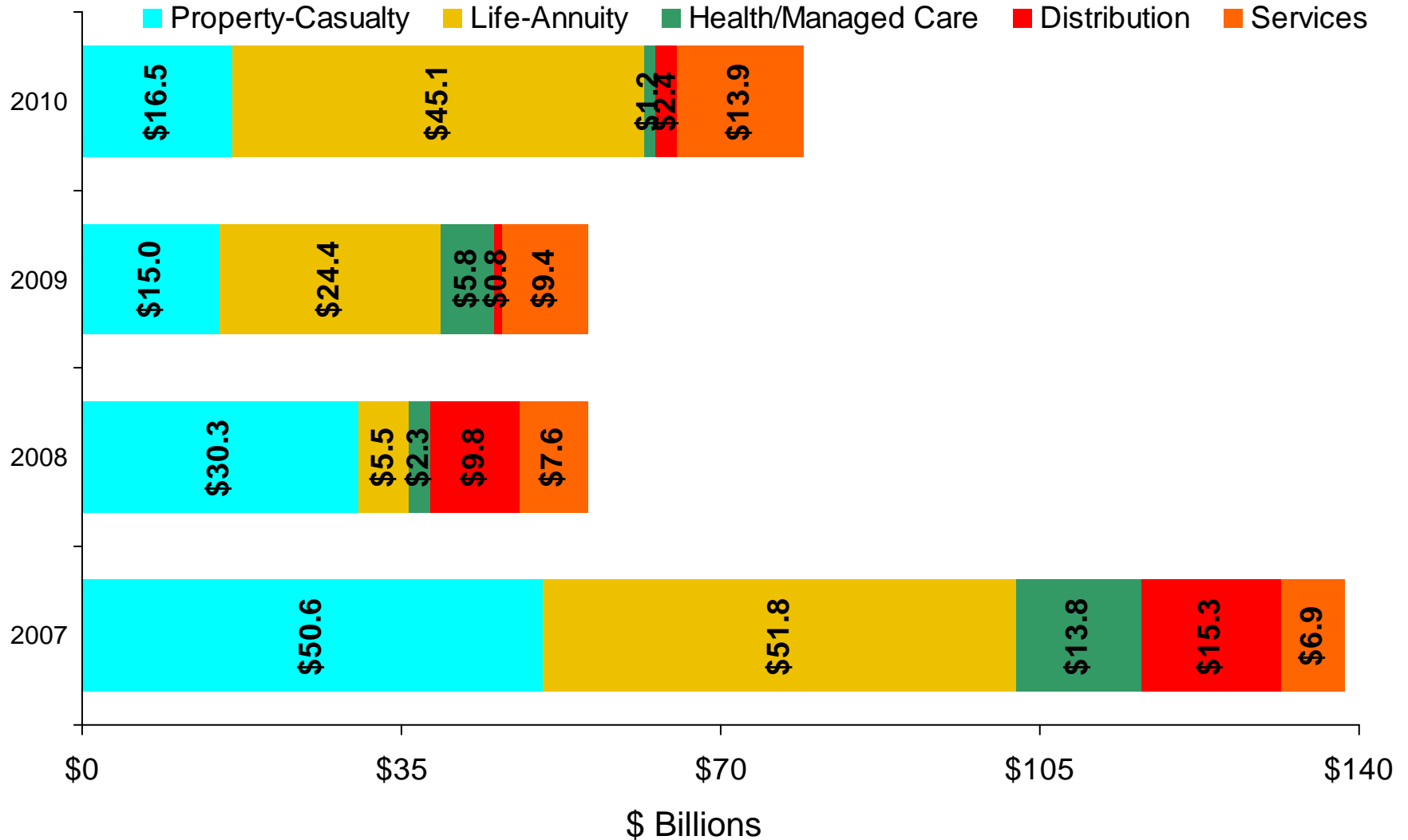
Implied Excess (Deficit) Capital Assuming Premium/Surplus Ratio = 0.9:1



Record Policyholder Surplus (Capital) Has Resulted Significant Excess Capital in the P/C Insurance Sector As of Year End 2010. Deteriorating Underwriting Losses, Higher CAT Activity, More Modest Market Returns Will Likely Shrink Excess Capital in 2011.

Note: The assumption of a 0.9:1 P/S ratio is derived from a Feb. 2011 announcement by Advisen, Ltd., that the US P/C insurance industry has \$74 billion in excess capital. The implied P/S ratio (calculated by III) is 0.88:1, which was rounded to 0.9:1.
 Source: Insurance Information Institute calculations from A.M. Best and ISO data. * Net Premiums Written

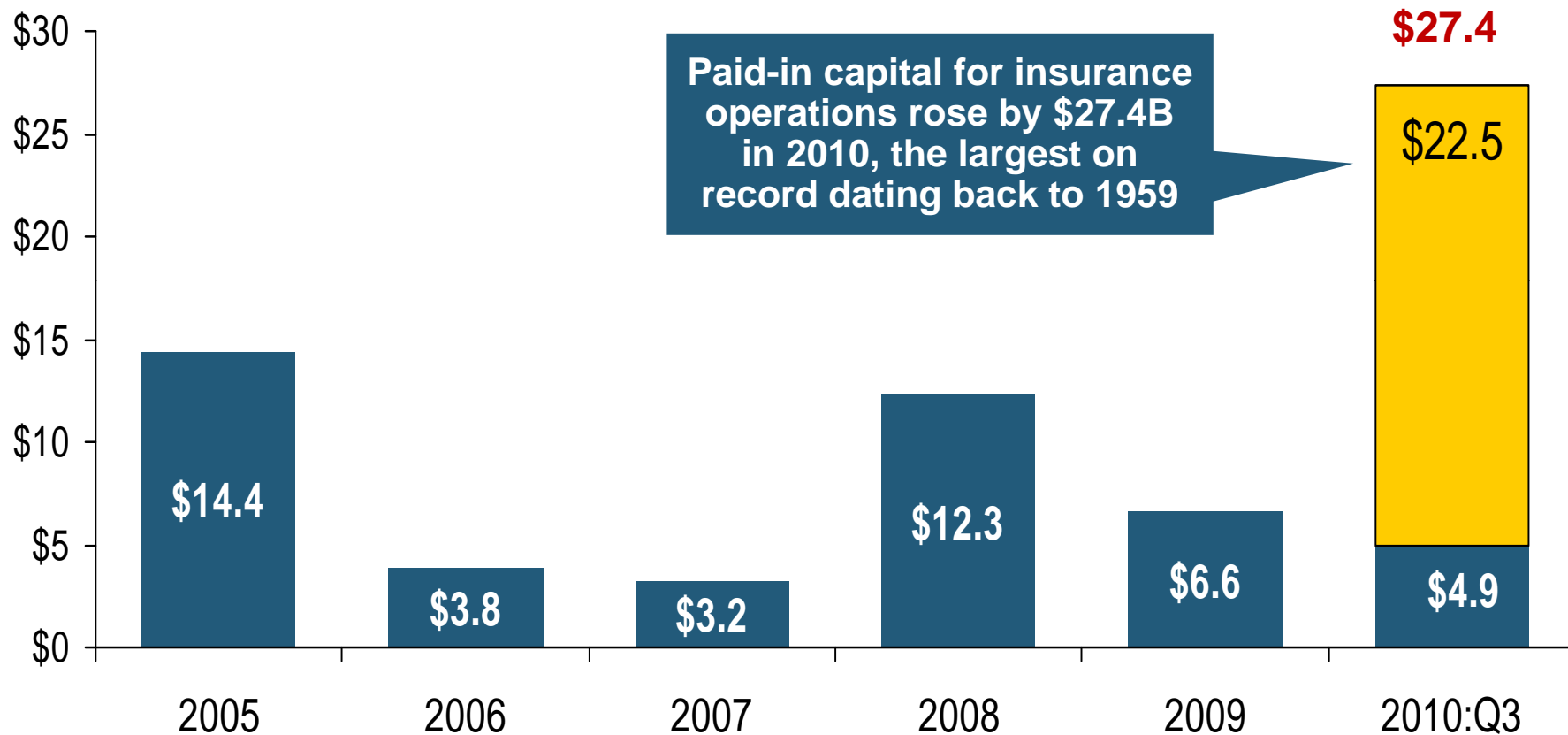
M&A Activity Globally Among P/C Insurers Remains Subdued: Little Capacity Leaving



Sources: Conning Research; Insurance Information Institute.

Paid-in Capital, 2005–2010

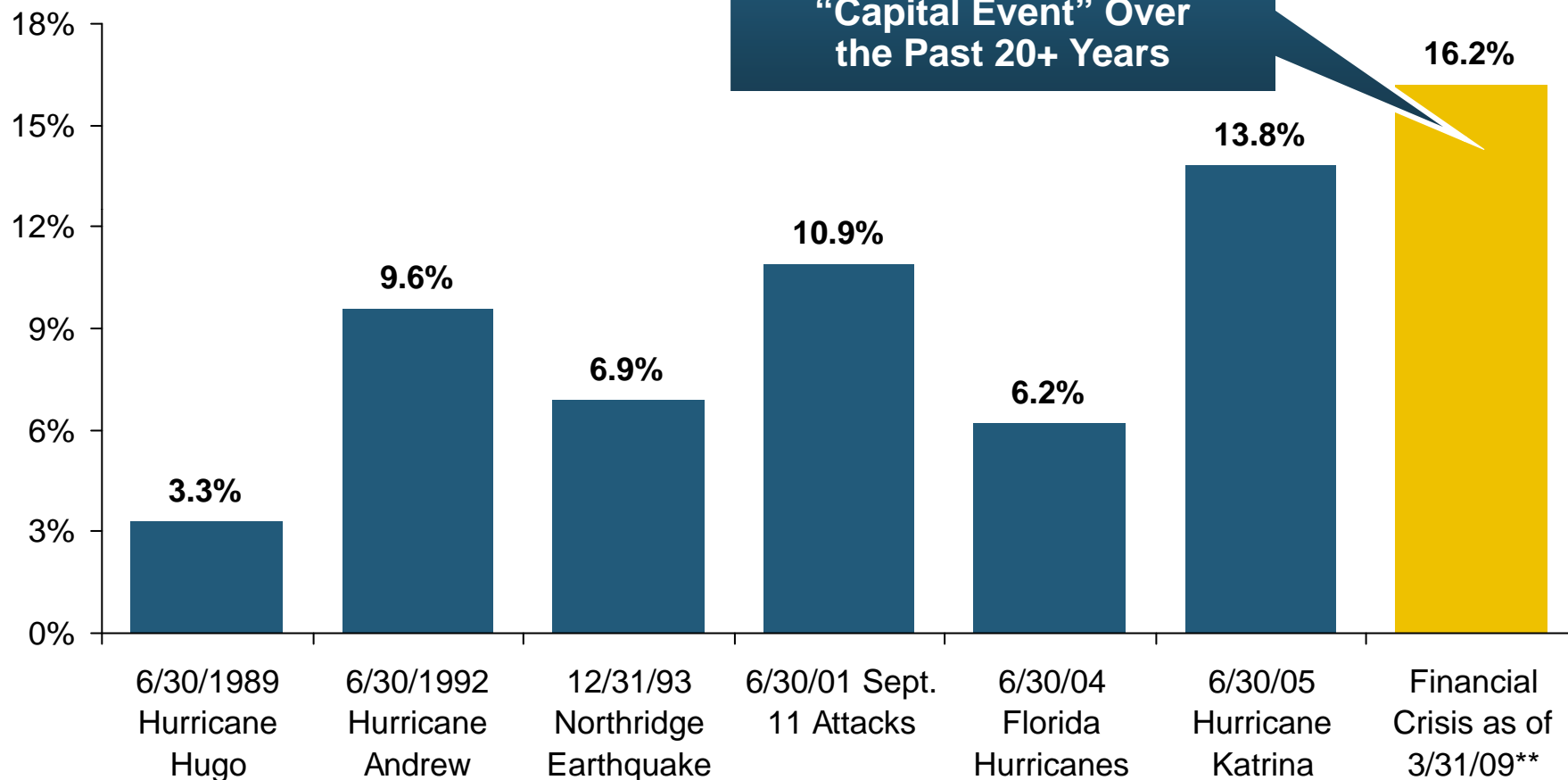
(\$ Billions)



In 2010 One Insurer's Paid-in Capital Rose by \$22.5B as Part of an Investment in a Non-insurance Business

Ratio of Insured Loss to Surplus for Largest Capital Events Since 1989*

(Percent)



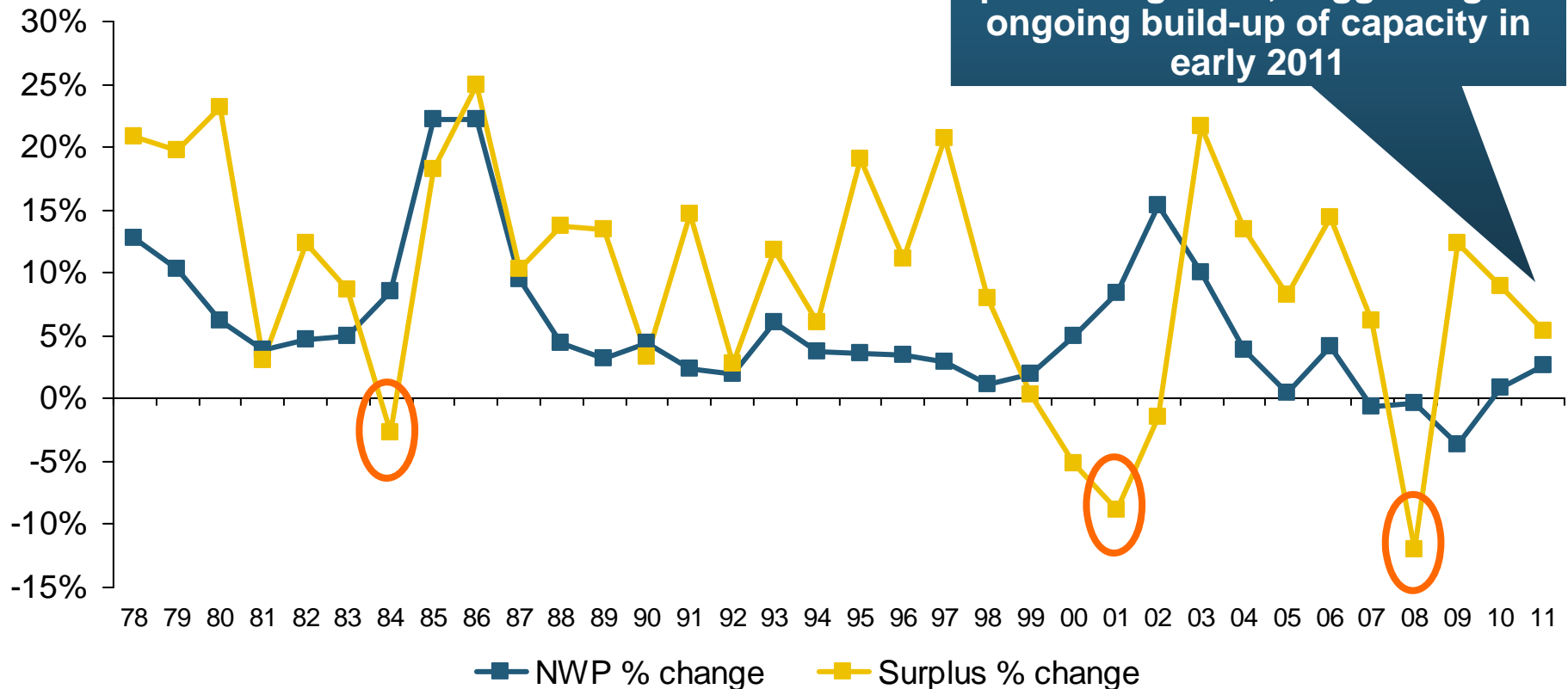
* Ratio is for end-of-quarter surplus immediately prior to event. Date shown is end of quarter prior to event

** Date of maximum capital erosion; As of 9/30/09 (latest available) ratio = 5.9%

Source: PCS; Insurance Information Institute

Historically, Hard Markets Follow When Surplus “Growth” is Negative*

(Percent)



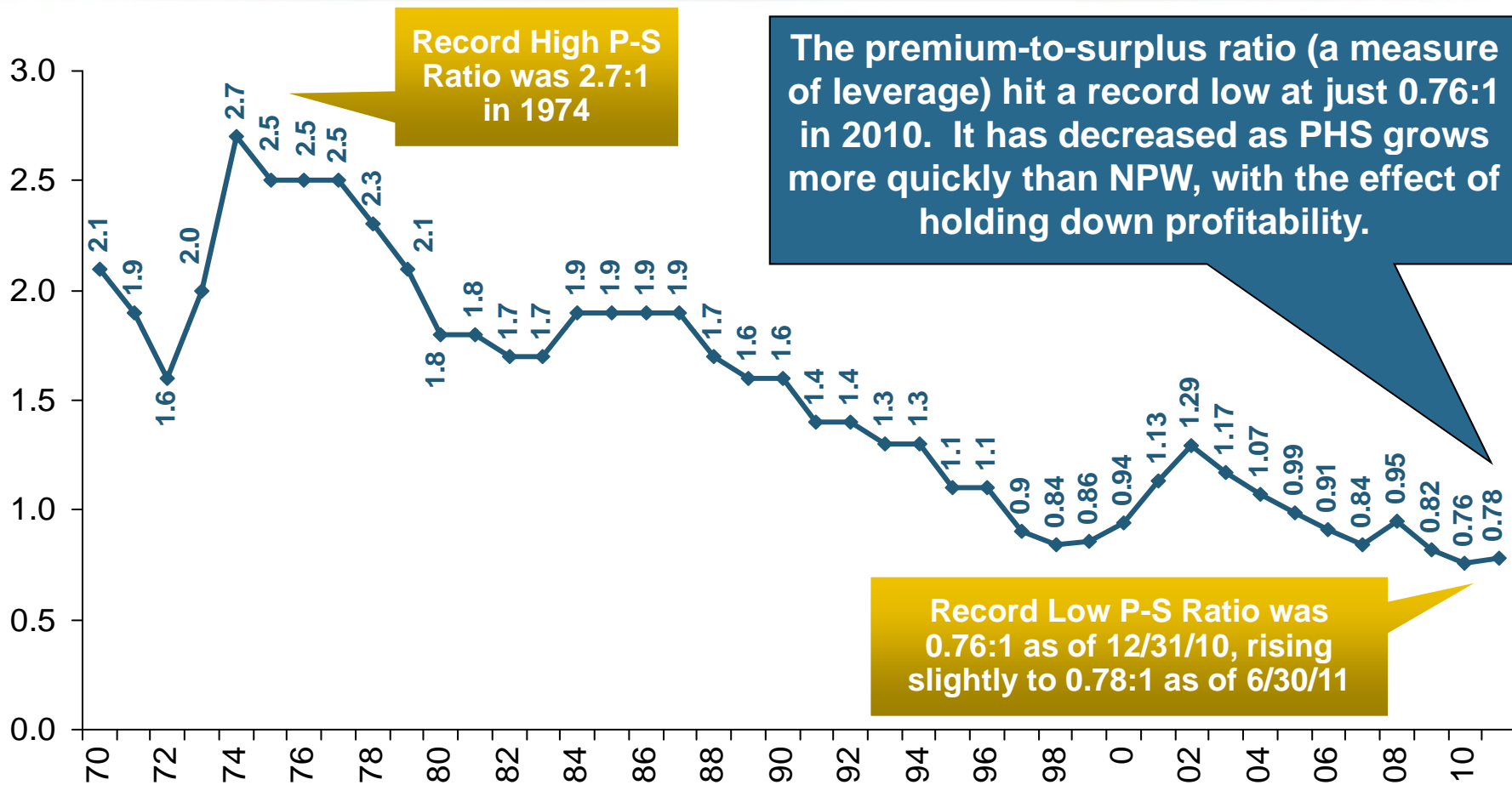
Surplus growth still exceeds premium growth, suggesting an ongoing build-up of capacity in early 2011

Sharp Decline in Capacity is a Necessary but Not Sufficient Condition for a True Hard Market

* 2011 NWP and Surplus figures are % changes as of H1:11 vs. H1:10.

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

Ratio of Net Premiums Written to Policyholder Surplus, 1970-2011*



Record High P-S Ratio was 2.7:1 in 1974

The premium-to-surplus ratio (a measure of leverage) hit a record low at just 0.76:1 in 2010. It has decreased as PHS grows more quickly than NPW, with the effect of holding down profitability.

Record Low P-S Ratio was 0.76:1 as of 12/31/10, rising slightly to 0.78:1 as of 6/30/11

The Premium-to-Surplus Ratio in 2011:H1 Implies that P/C Insurers Held \$1 in Surplus Against Each \$0.78 Written in Premiums. In 1974, Each \$1 of Surplus Backed \$2.70 in Premium.

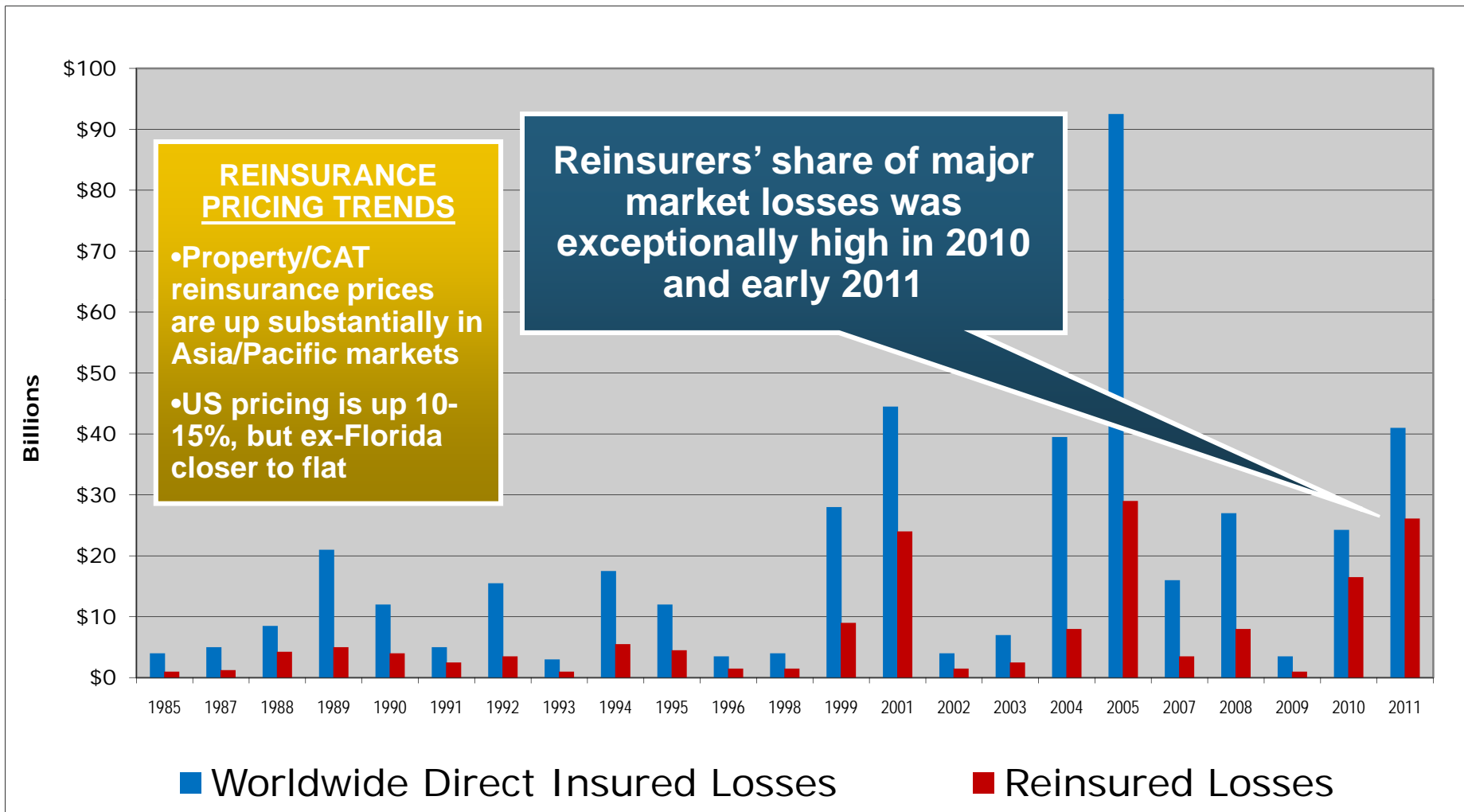
*2011 data are as of 6/30/11.

Sources: Insurance Information Institute calculations from A.M. Best data.

3. REINSURANCE MARKET CONDITIONS

**Record Global
Catastrophes Activity is
Pressuring Pricing**

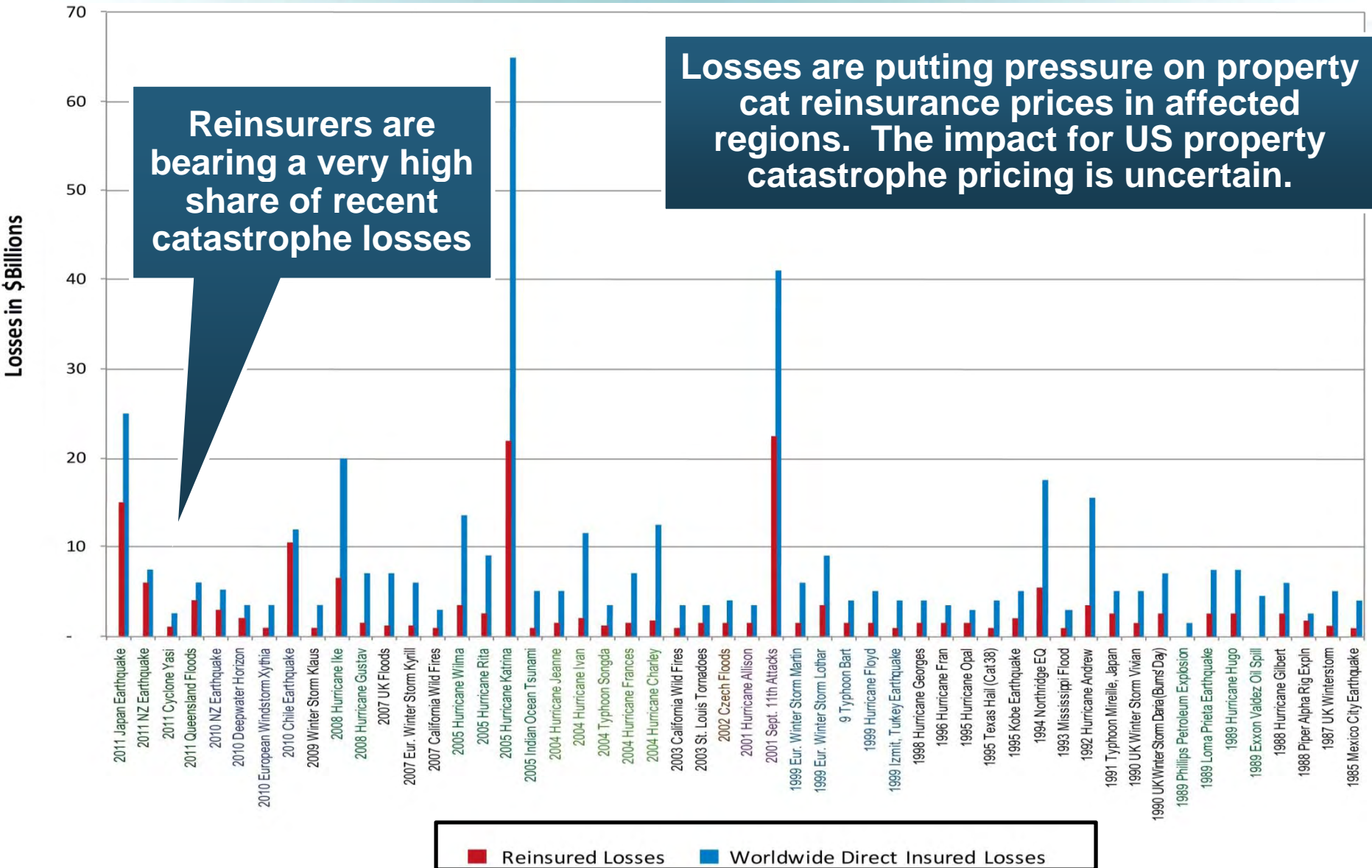
Significant Market Losses, 1985-2011*



Source: Holborn; RAA.

* 2011 events are as of March 31 and are preliminary and may change as loss estimates are refined further.

Significant Market Losses by Event, 1985-2011*



Source: Holborn, RAA. *2011 events as of March 31 are preliminary and may change as loss estimates are refined further.

Global Property Catastrophe Rate on Line Index, 1990-2011 YTD (6/1/11)

A modest increase in global property catastrophe reinsurance pricing was evident in June 1 renewals in the wake of record global catastrophe losses. Larger increase could occur for the Jan.1, 2012 renewals

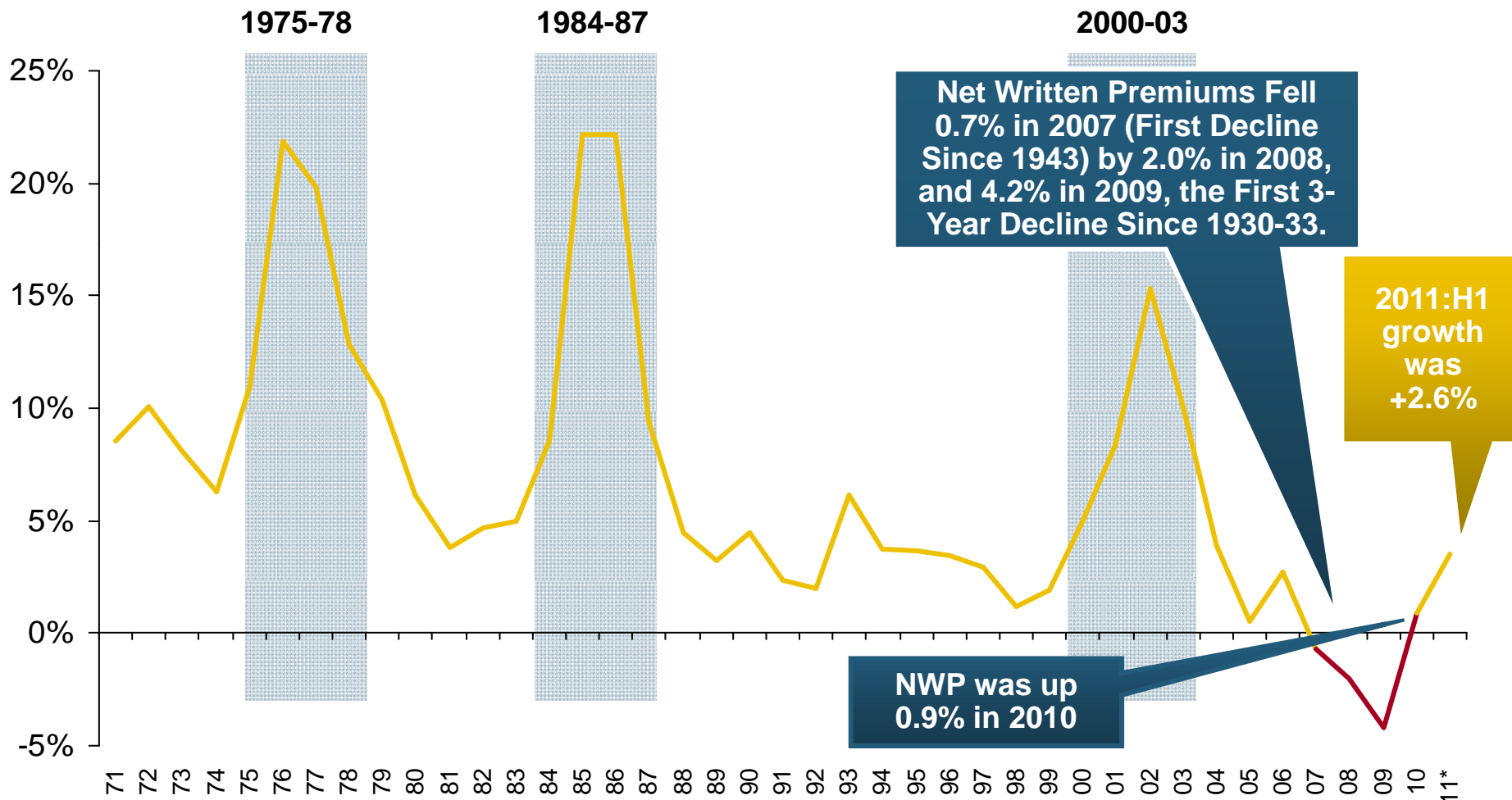


4. RENEWED PRICING DISCIPLINE

**Is There Evidence of a Broad
and Sustained Shift in Pricing?**

Soft Market Persisted in 2010 but Growth Returned: More in 2011?

(Percent)

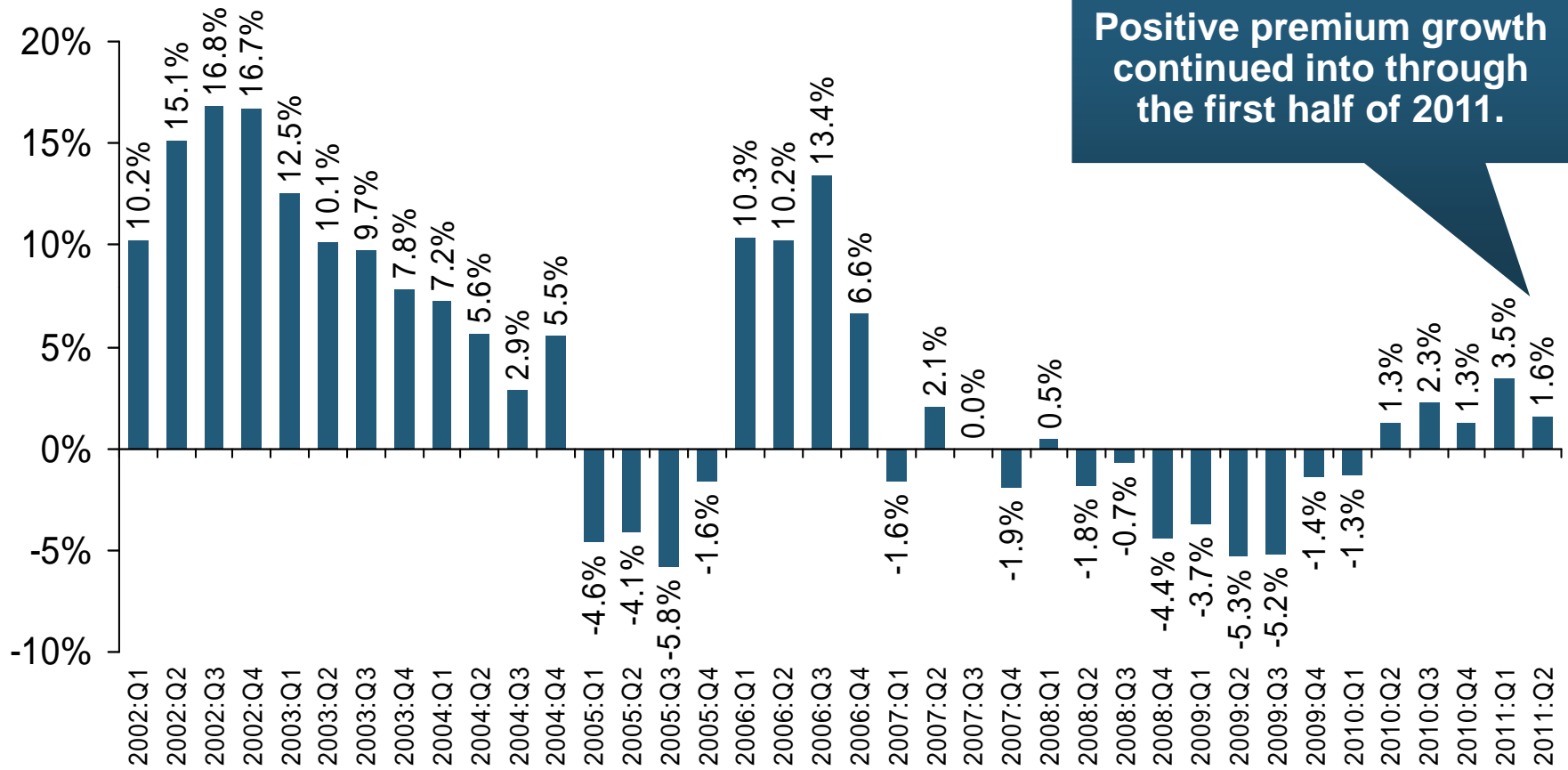


*2011 figure is for H1 vs. 2010:H1.

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



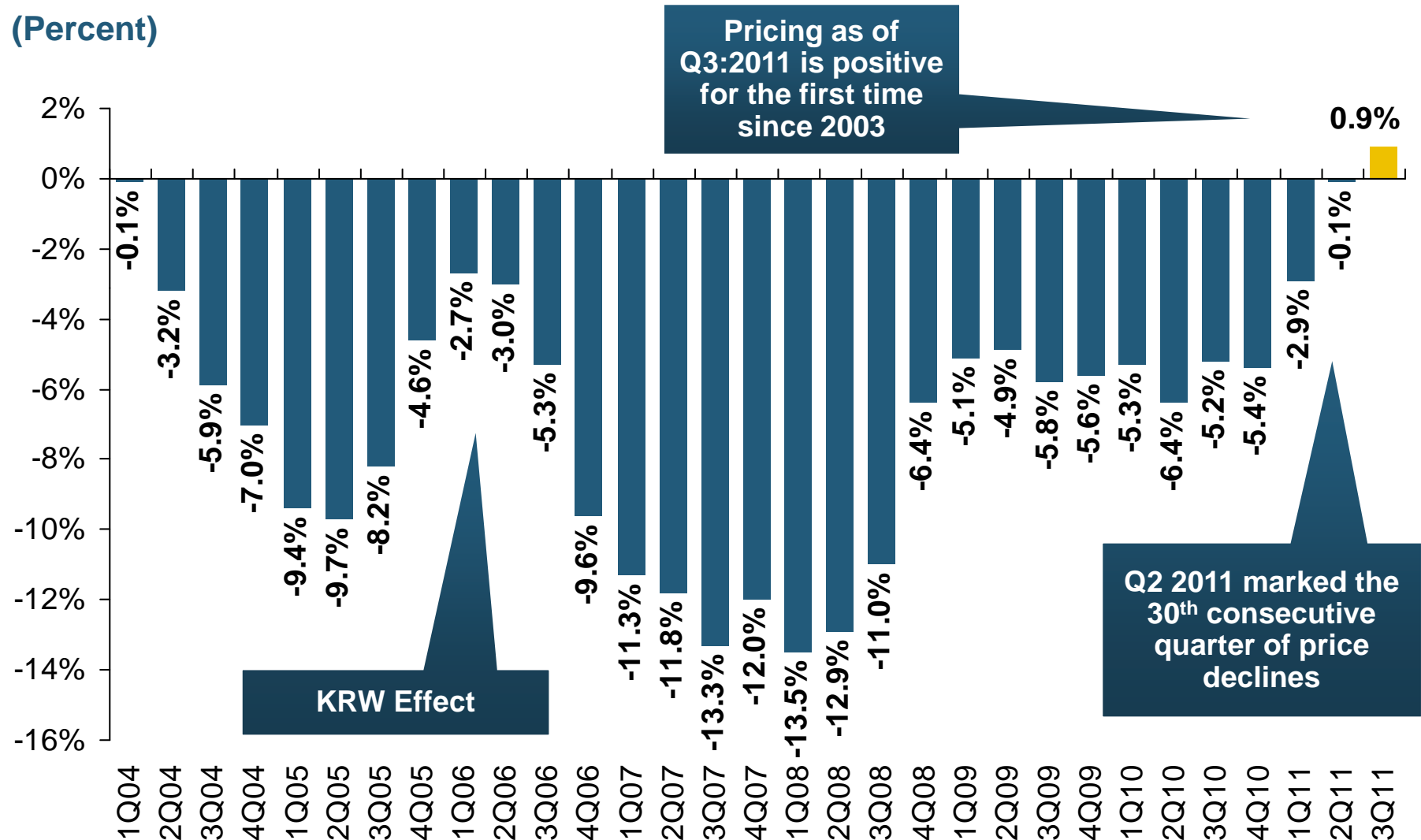
Positive premium growth continued into through the first half of 2011.

Pricing and more stable exposure environment are contributing to consistent positive growth in recent quarters (vs. the same quarter, prior year)

Sources: ISO, Insurance Information Institute.

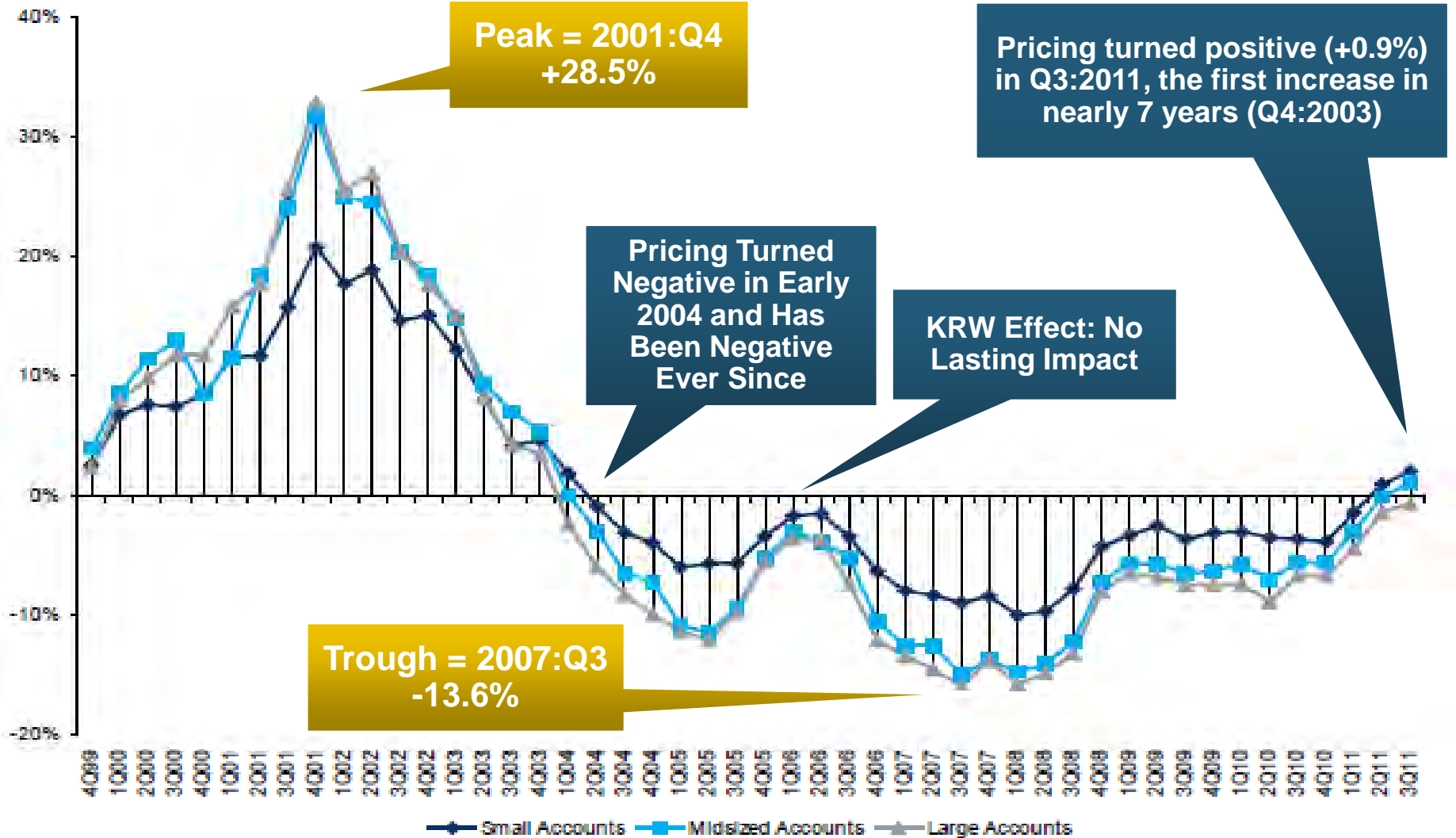
Average Commercial Rate Change, All Lines, (1Q:2004–3Q:2011)

(Percent)



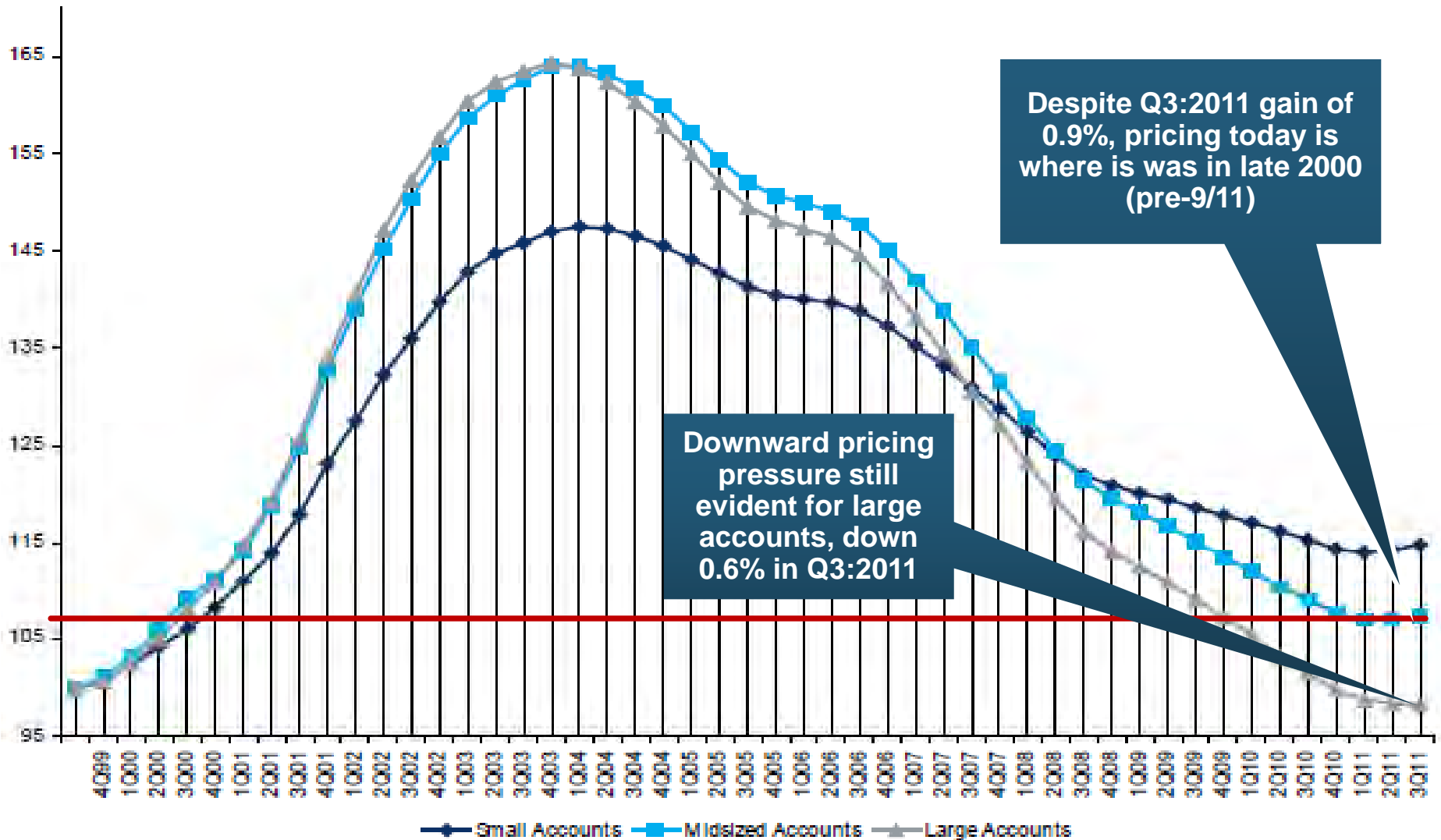
Change in Commercial Rate Renewals, by Account Size: 1999:Q4 to 2011:Q3

Percentage Change (%)



Cumulative Qtrly. Commercial Rate Changes, by Account Size: 1999:Q4 to 2011:Q3

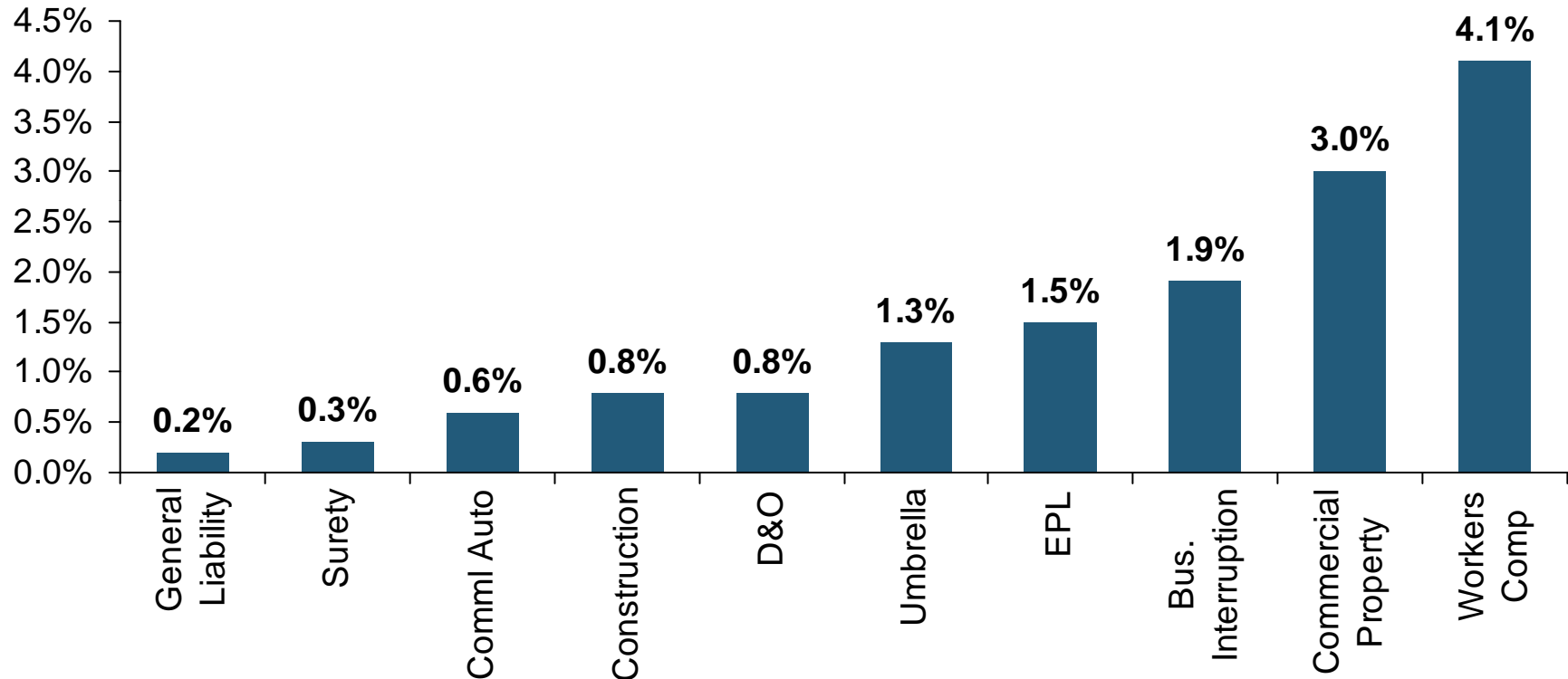
1999:Q4 = 100



Source: Council of Insurance Agents and Brokers; Insurance Information Institute.

Change in Commercial Rate Renewals, by Line: 2011:Q3

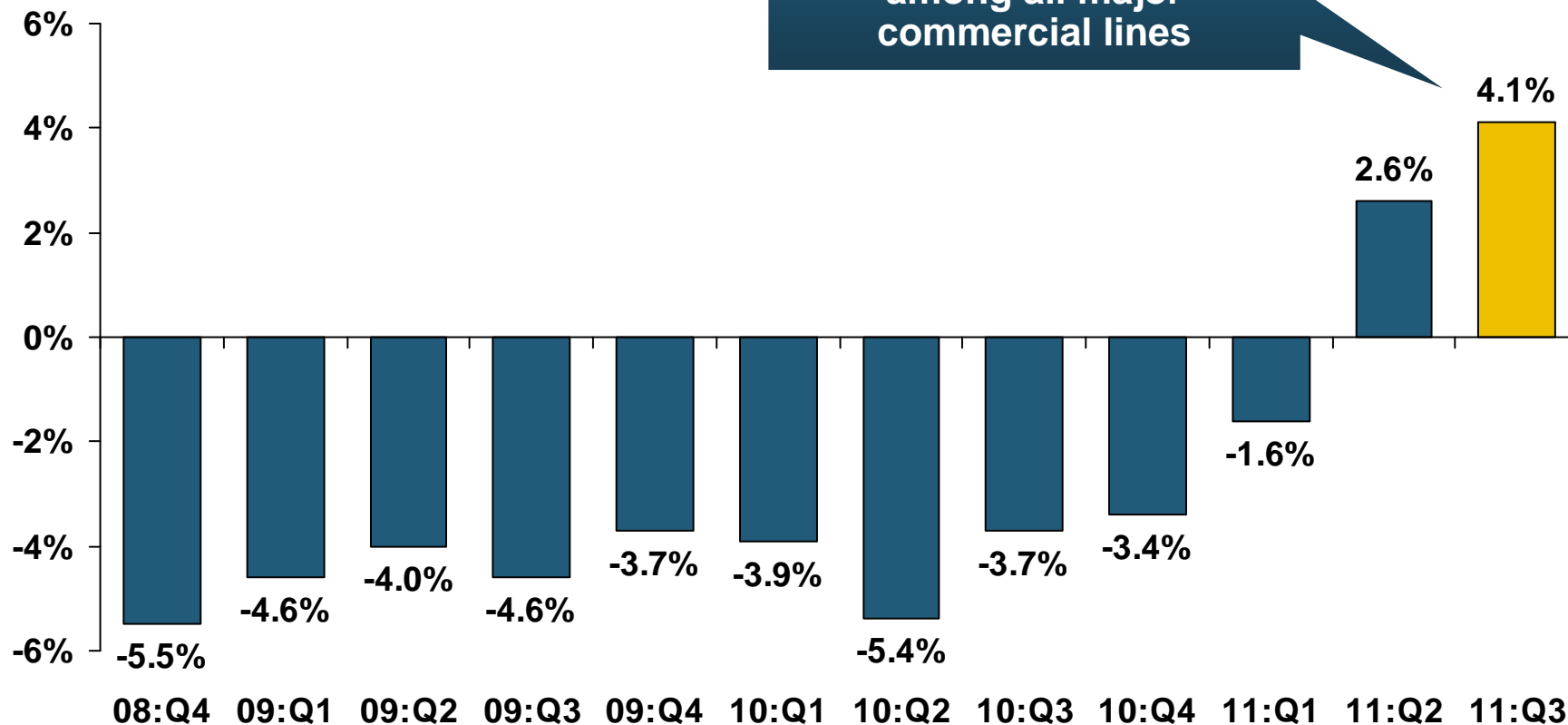
Percentage Change (%)



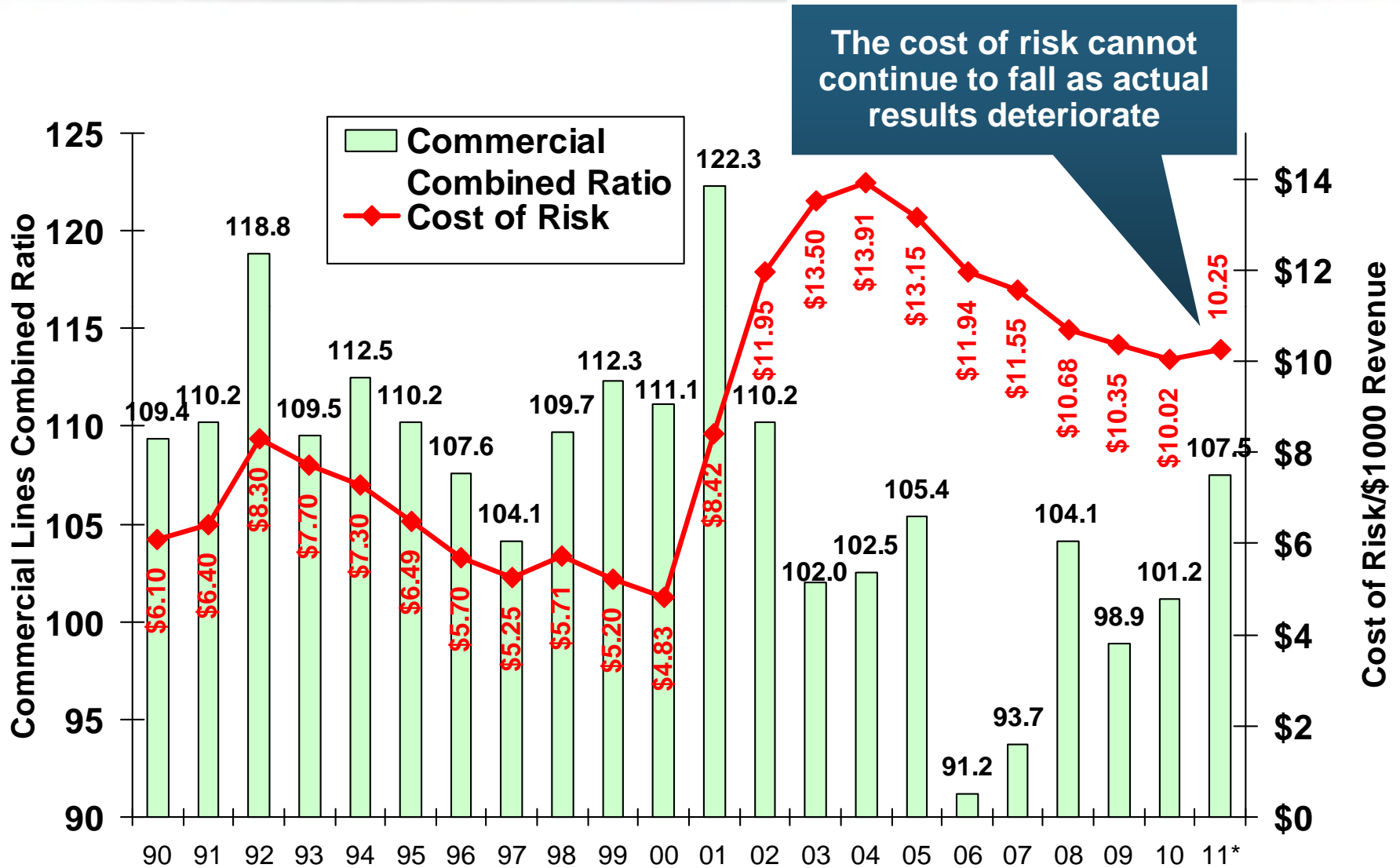
Major Commercial Lines Renewed Uniformly Upward in Q3:2011 for the First Time Since 2003, With Workers Up More than Any Other Line

Workers Comp Rate Changes, 2008:Q4 – 2011:Q3

(Percent
Change)



Cost of Risk vs. Commercial Lines Combined Ratio



*Insurance Information Institute estimates for 2011.

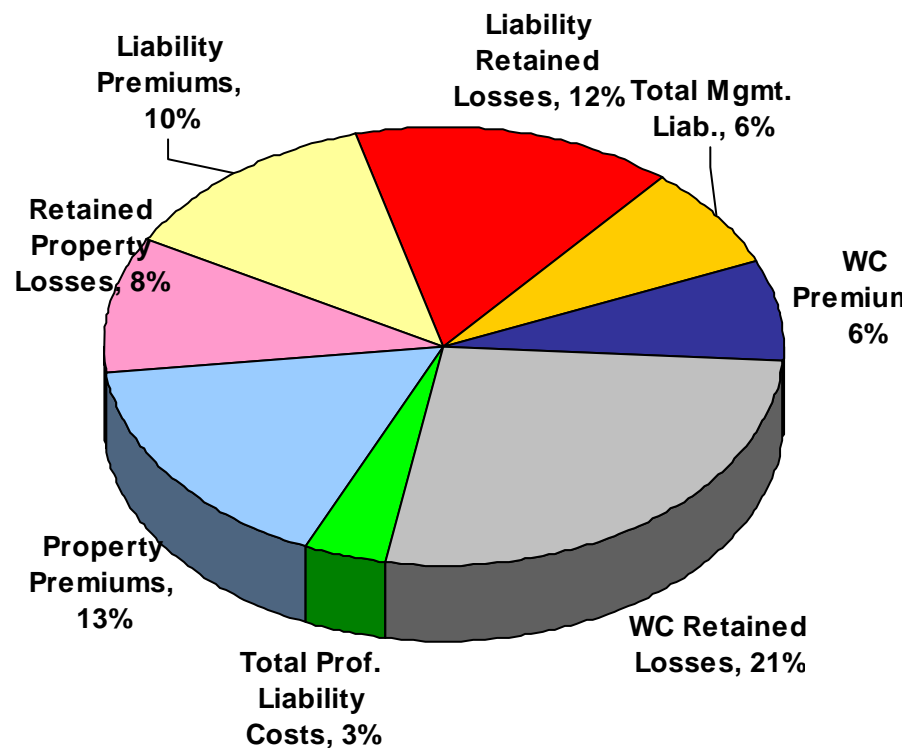
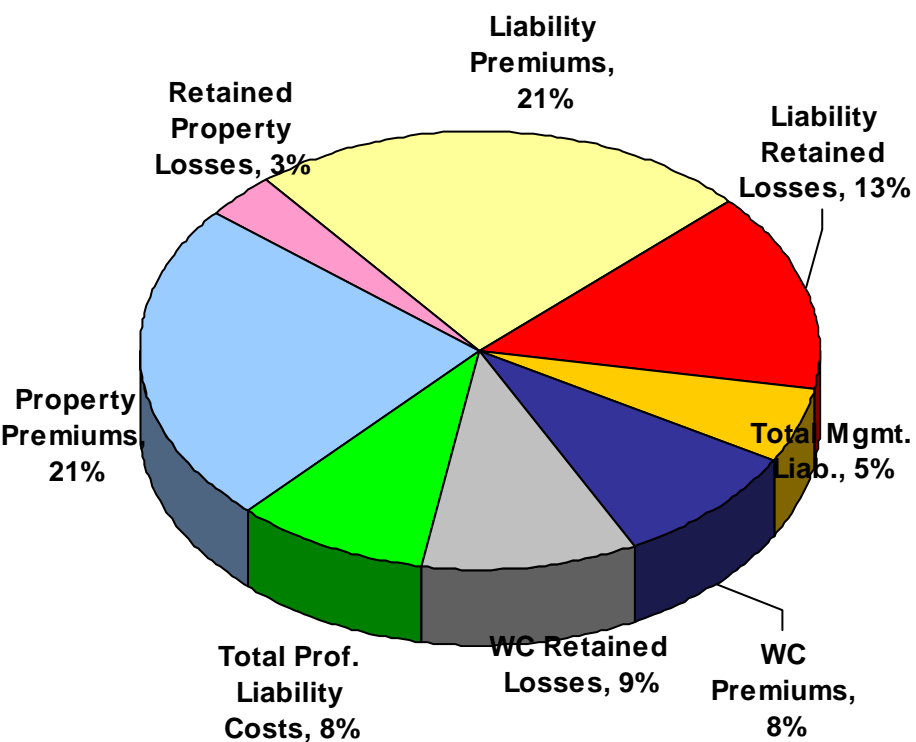
Source: 2011 RIMS Benchmark Survey; A.M. Best; Insurance Information Institute

How the Risk Dollar is Spent (2011)

Total liability costs account for 35% - 40% of the risk dollar

Firms w/Revenues < \$1 Billion

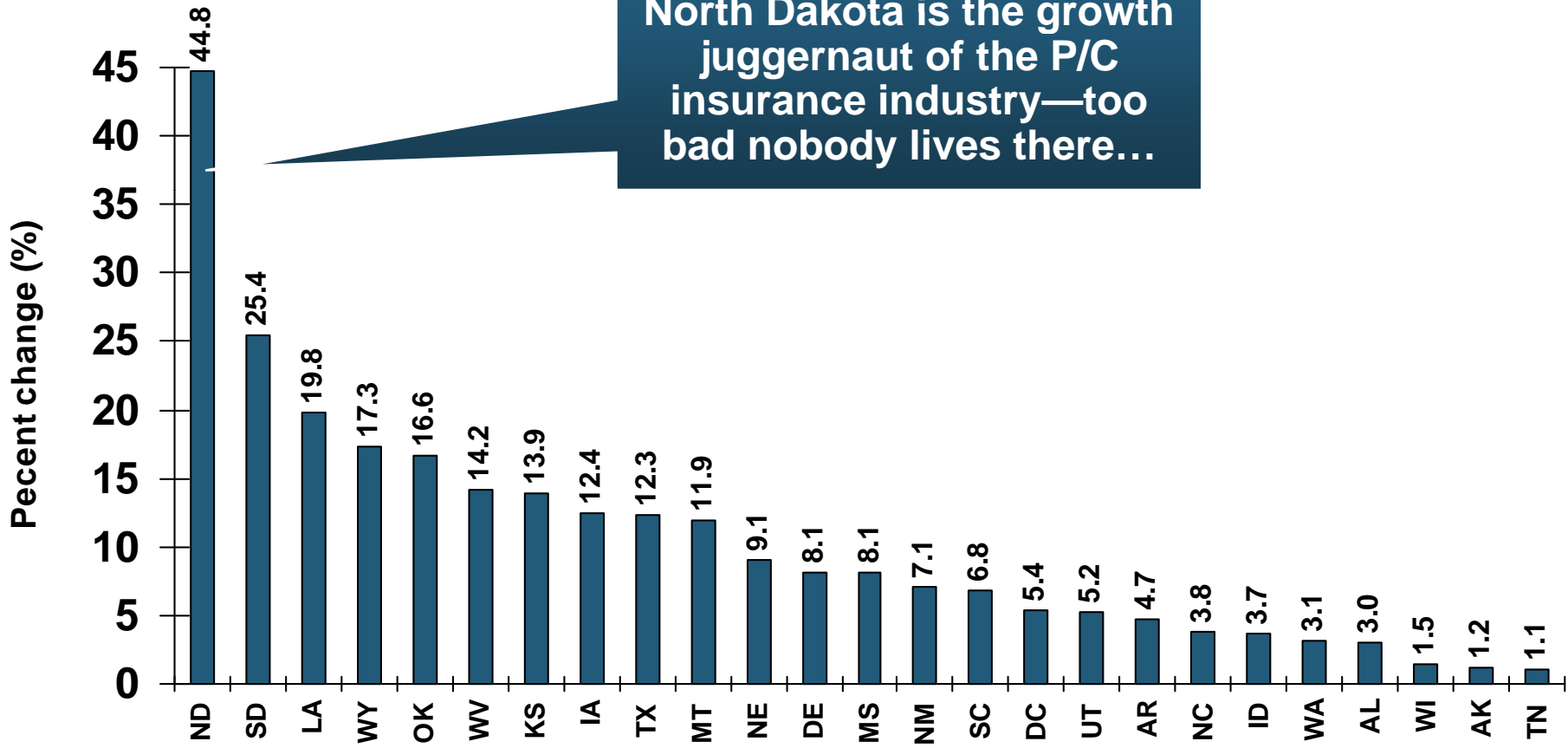
Firms w/Revenues > \$1 Billion



Direct Premiums Written: All P/C Lines Percent Change by State, 2005-2010

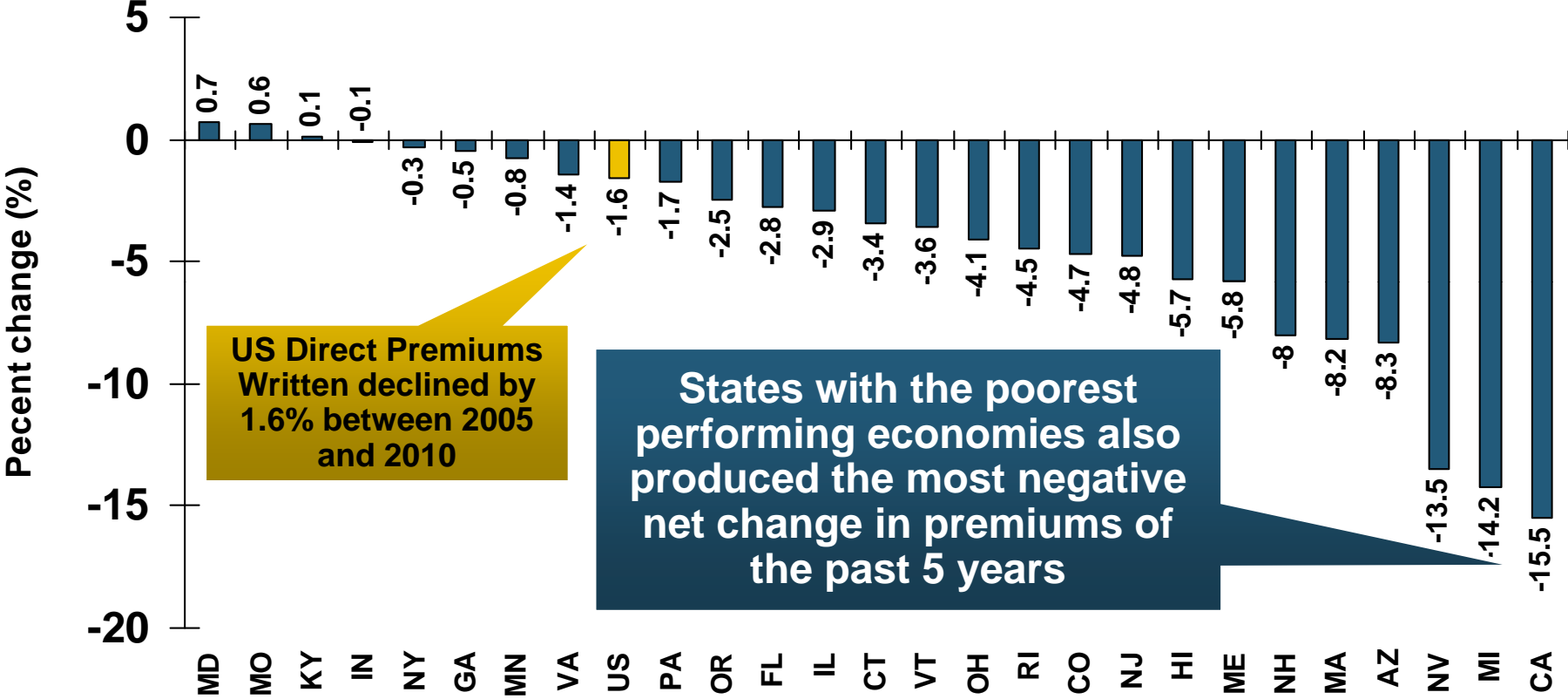
Top 25 States

North Dakota is the growth juggernaut of the P/C insurance industry—too bad nobody lives there...



Direct Premiums Written: All P/C Lines Percent Change by State, 2005-2010

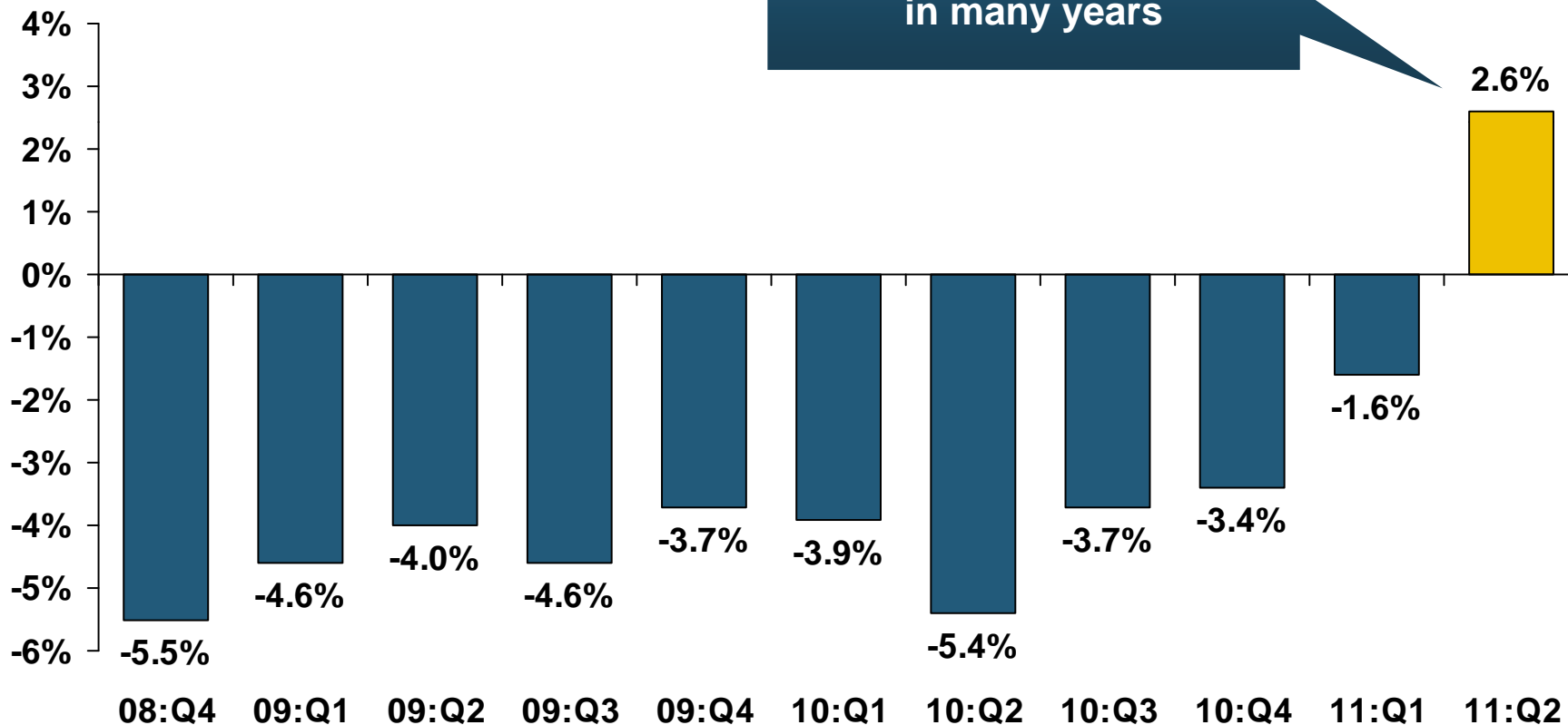
Bottom 25 States



Sources: SNL Financial LC; Insurance Information Institute.

Workers Comp Rate Changes, 2008:Q4 – 2011:Q2

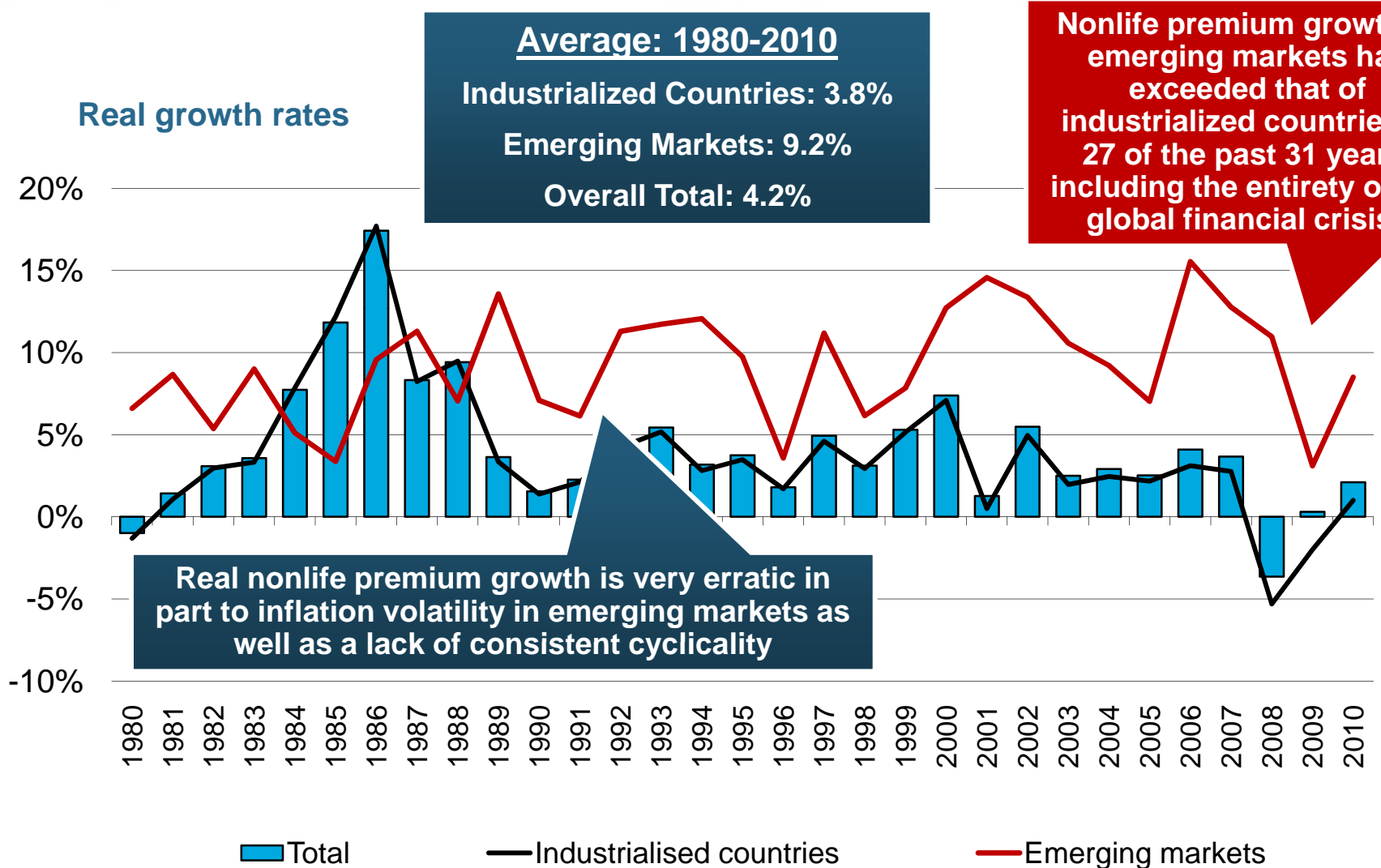
(Percent
Change)



The Unfortunate Nexus: Opportunity, Risk & Instability

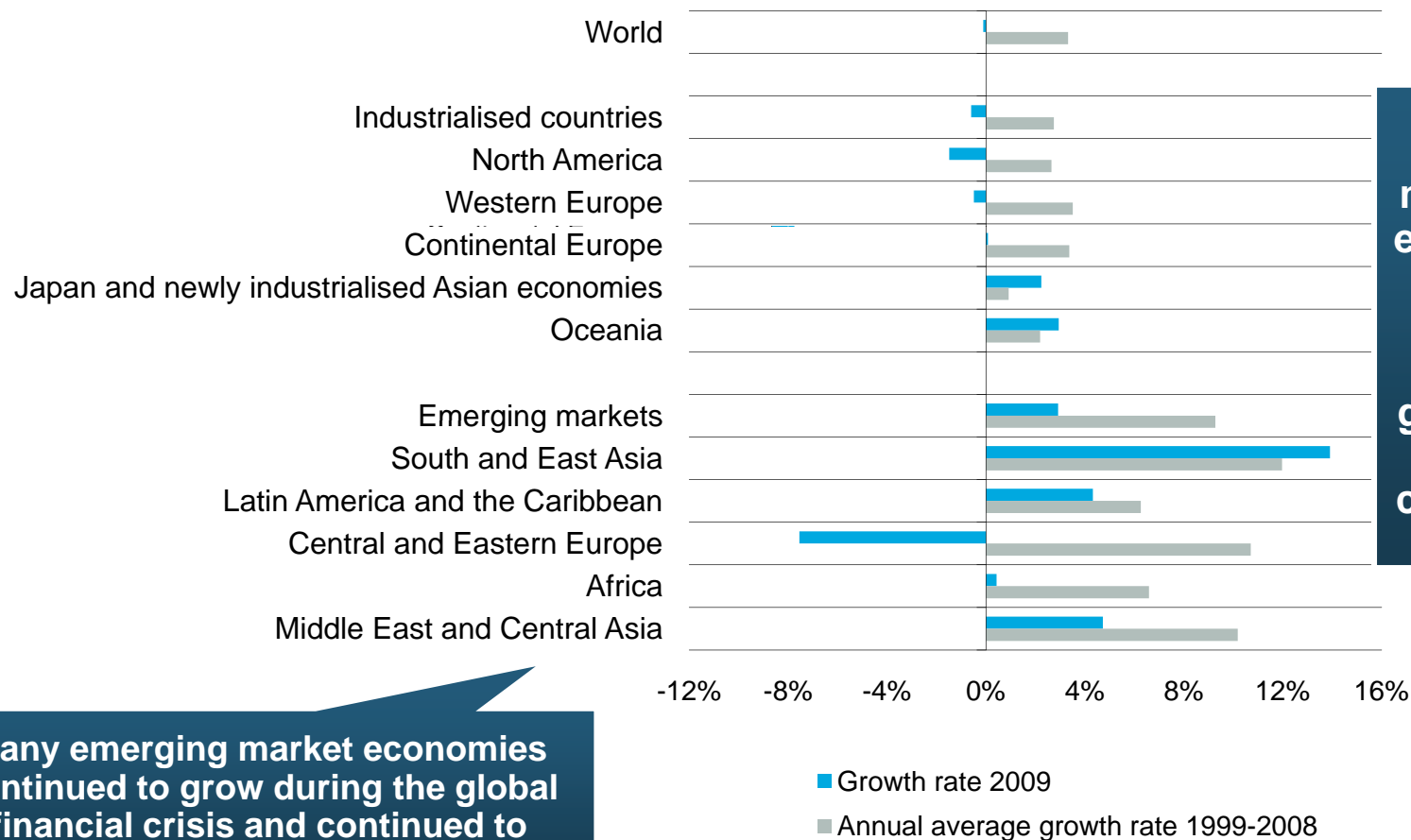
**Most of the Global Economy's Future
Gains Will be Fraught with Much
Greater Risk and Uncertainty than in
the Past**

Global Real (Inflation Adjusted) Nonlife Premium Growth: 1980-2010



Nonlife Real Premium Growth Rates by Region: 2000-2009 and 2010

Real Premium Growth Rates



Every emerging market region except Central and Eastern Europe experienced growth during the financial crisis and into 2010

Many emerging market economies continued to grow during the global financial crisis and continued to benefit from foreign direct investment

Distribution of Nonlife Premium: Industrialized vs. Emerging Markets, 2009

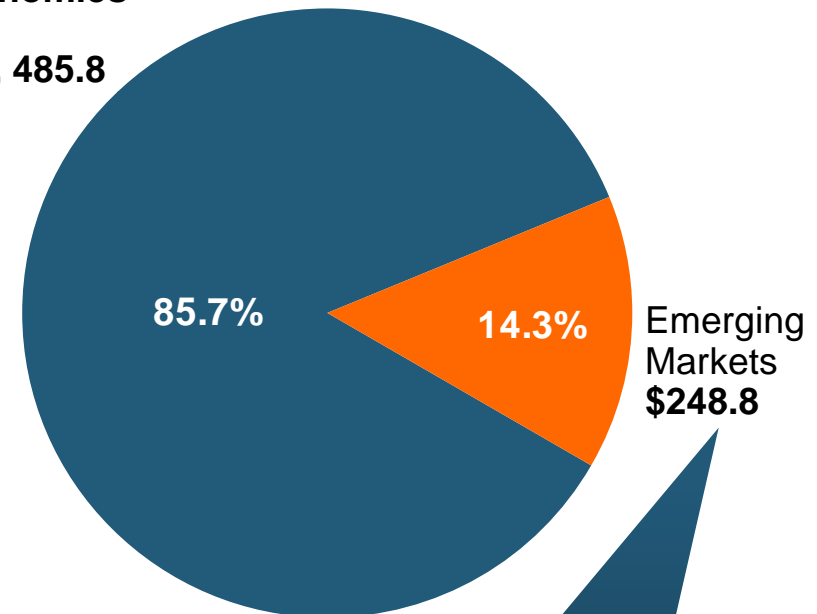
Premium Growth Facts

- Although premium growth throughout the industrialized world was negative in 2009, its share of global nonlife premiums remained very high at nearly 86%--accounting for nearly \$1.5 trillion in premiums.
- The financial crisis and sluggish recovery in the major insurance markets will accelerate the expansion of the emerging market sector

2009, \$Billions

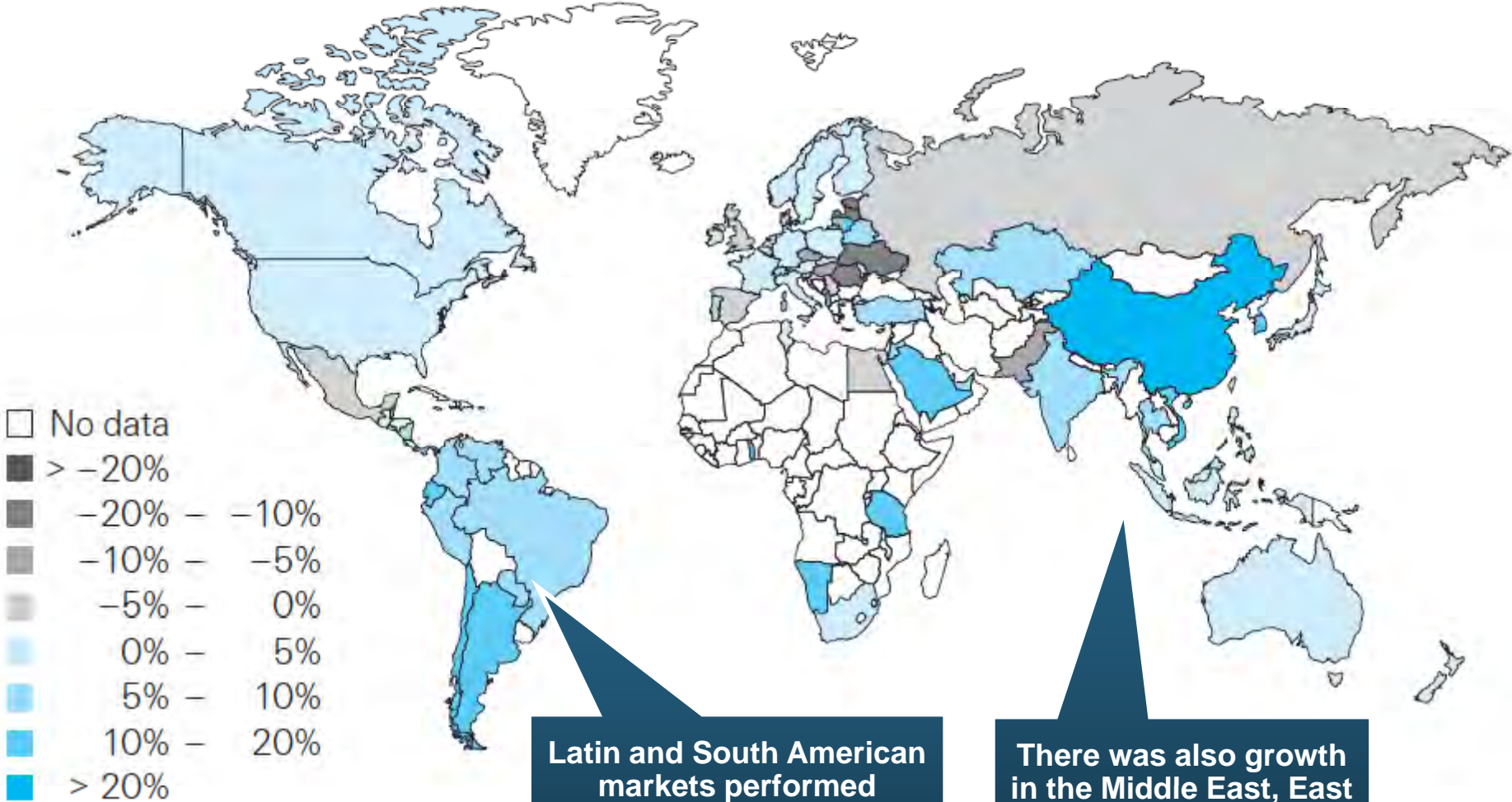
Industrialized
Economies

\$1, 485.8



Developing markets now account for 47% of global GDP but just 14% of nonlife premiums

Nonlife Real Premium Growth in 2010



Latin and South American markets performed relatively well during and after the global financial crisis in terms of growth

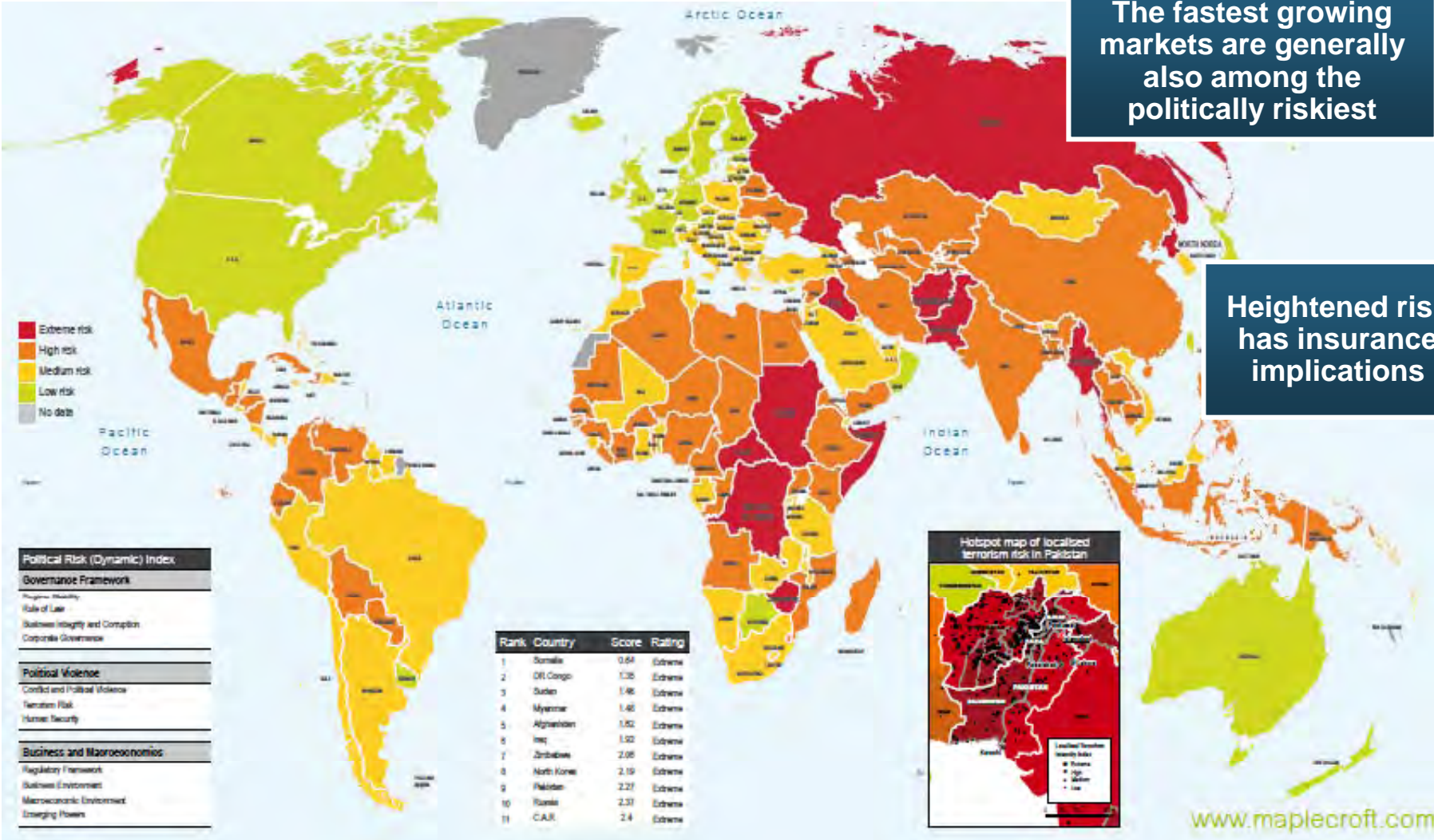
There was also growth in the Middle East, East and South Asia as well as Australia and New Zealand

Source: Swiss Re, *sigma*, No. 2/2011.

Political Risk in 2010: Greatest Business Opportunities Are Often in Risky Nations

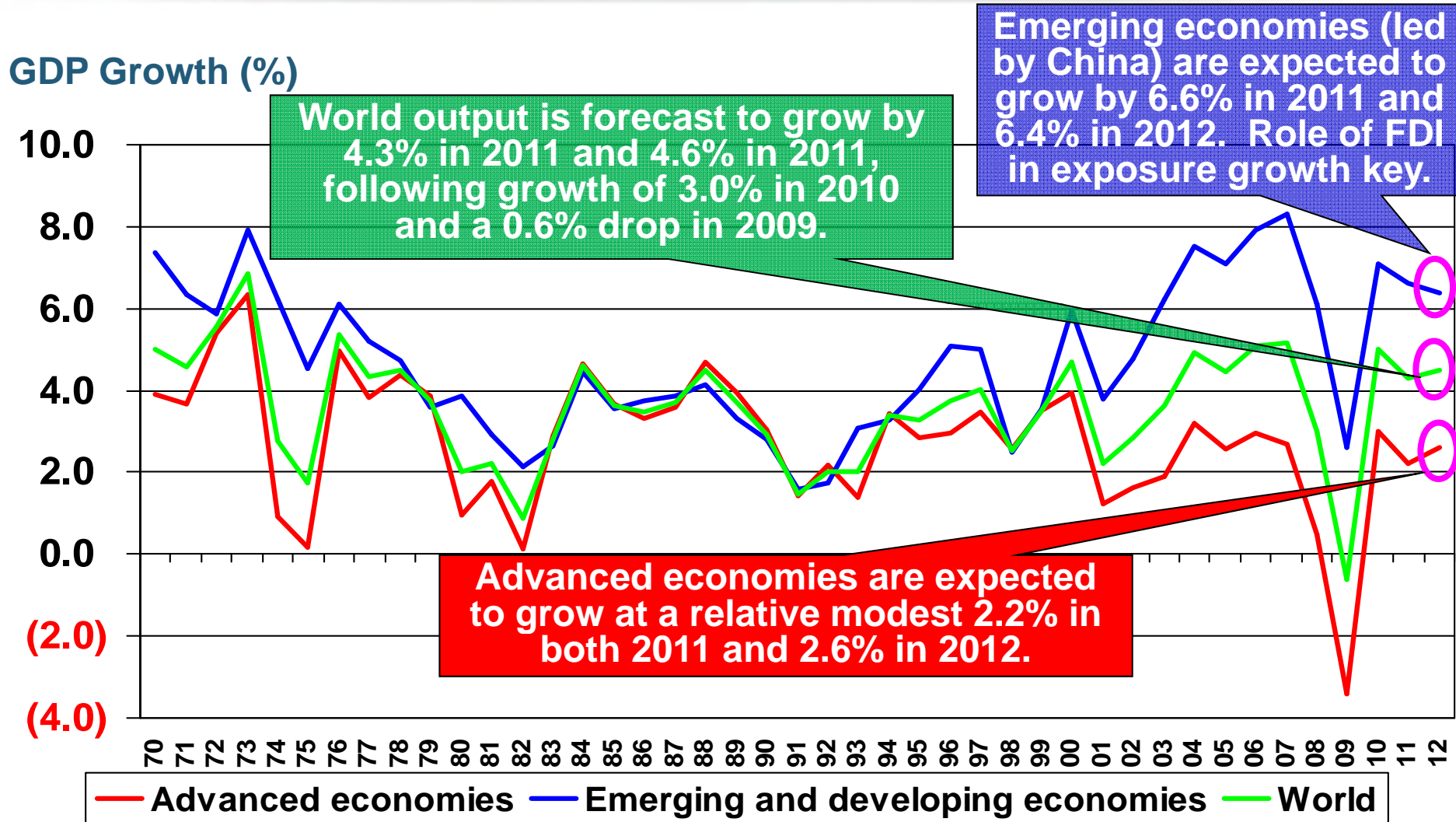
The fastest growing markets are generally also among the politically riskiest

Heightened risk has insurance implications



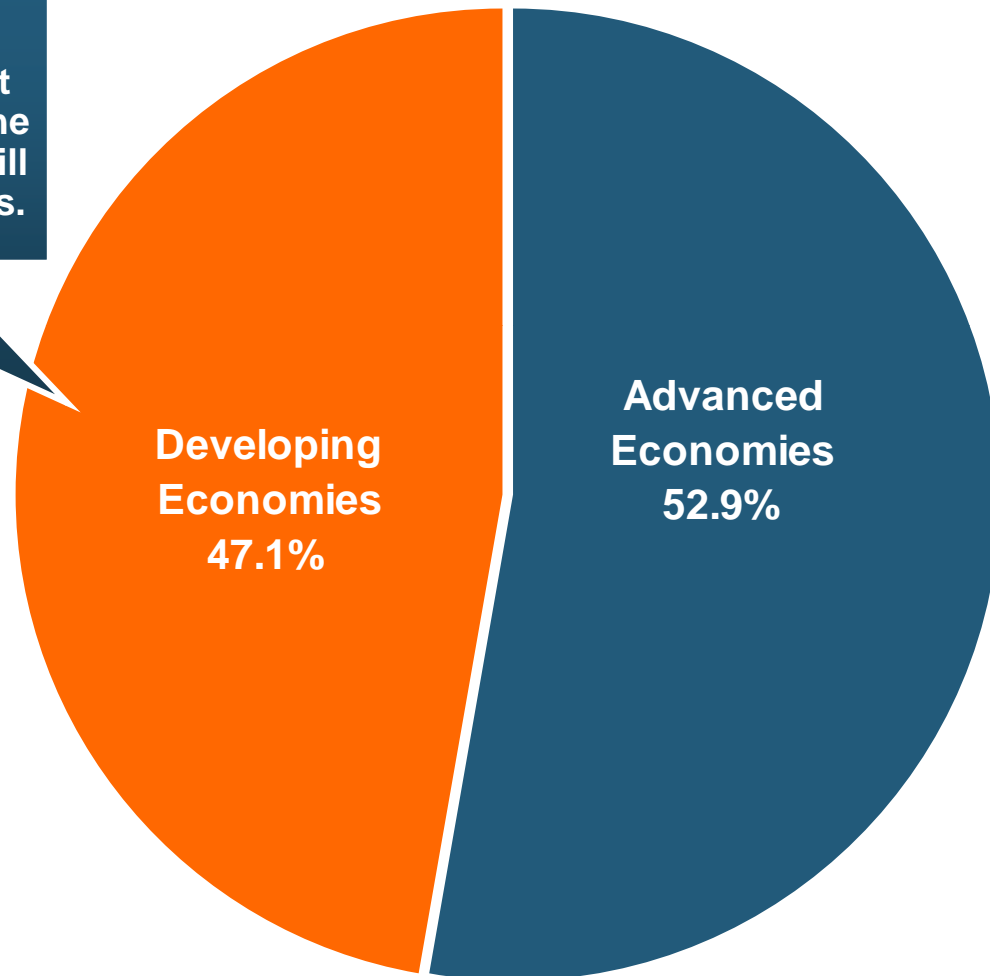
Source: Maplecroft

GDP Growth: Advanced & Emerging Economies vs. World, 1970-2012F

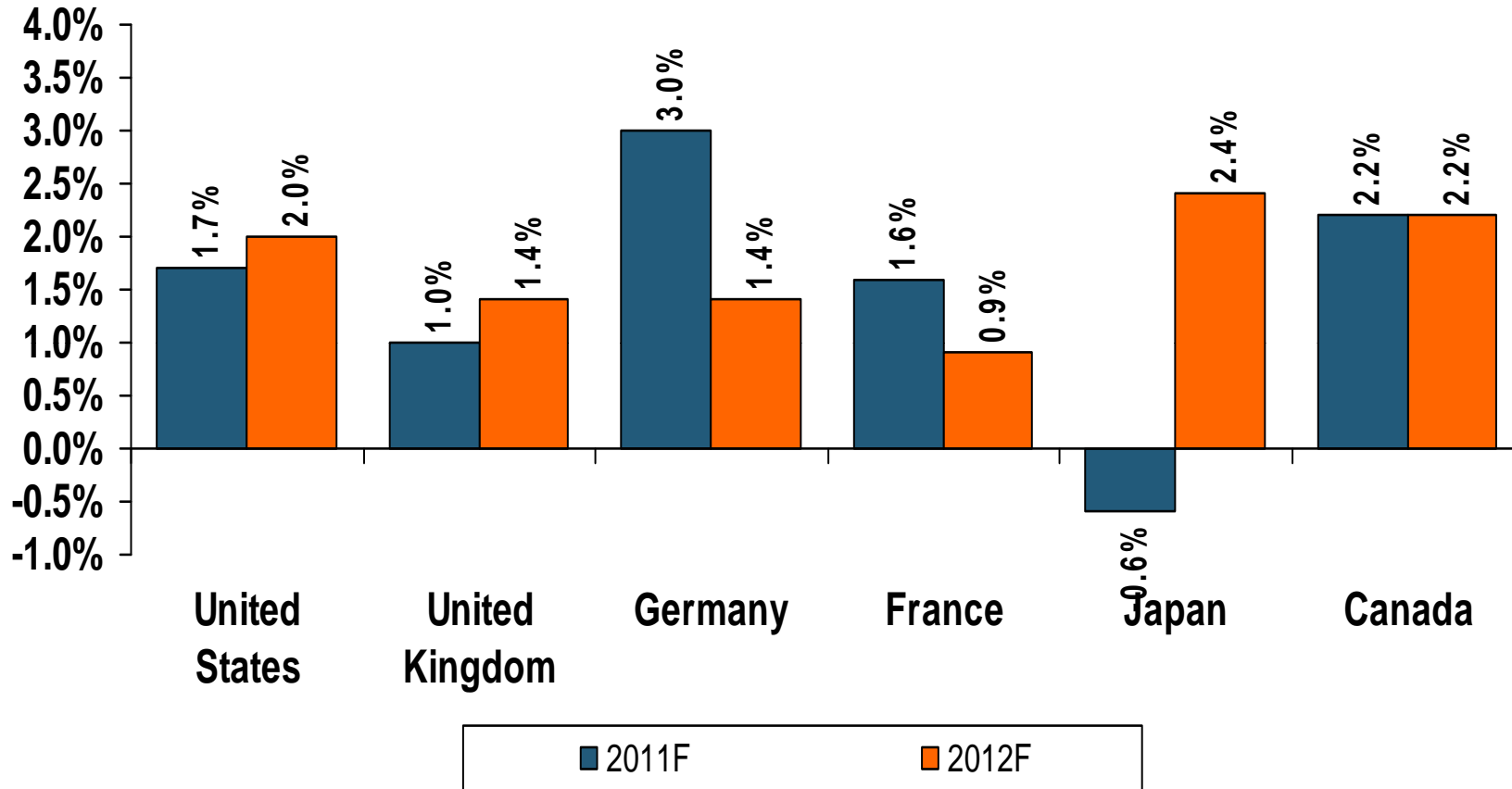


Relative Shares of Global Output, Advanced vs. Developing Economies, 2009

The gap is closing quickly. China became the world's second largest economy in 2010 and before long the developing world's share of GDP will exceed that of advanced economies.

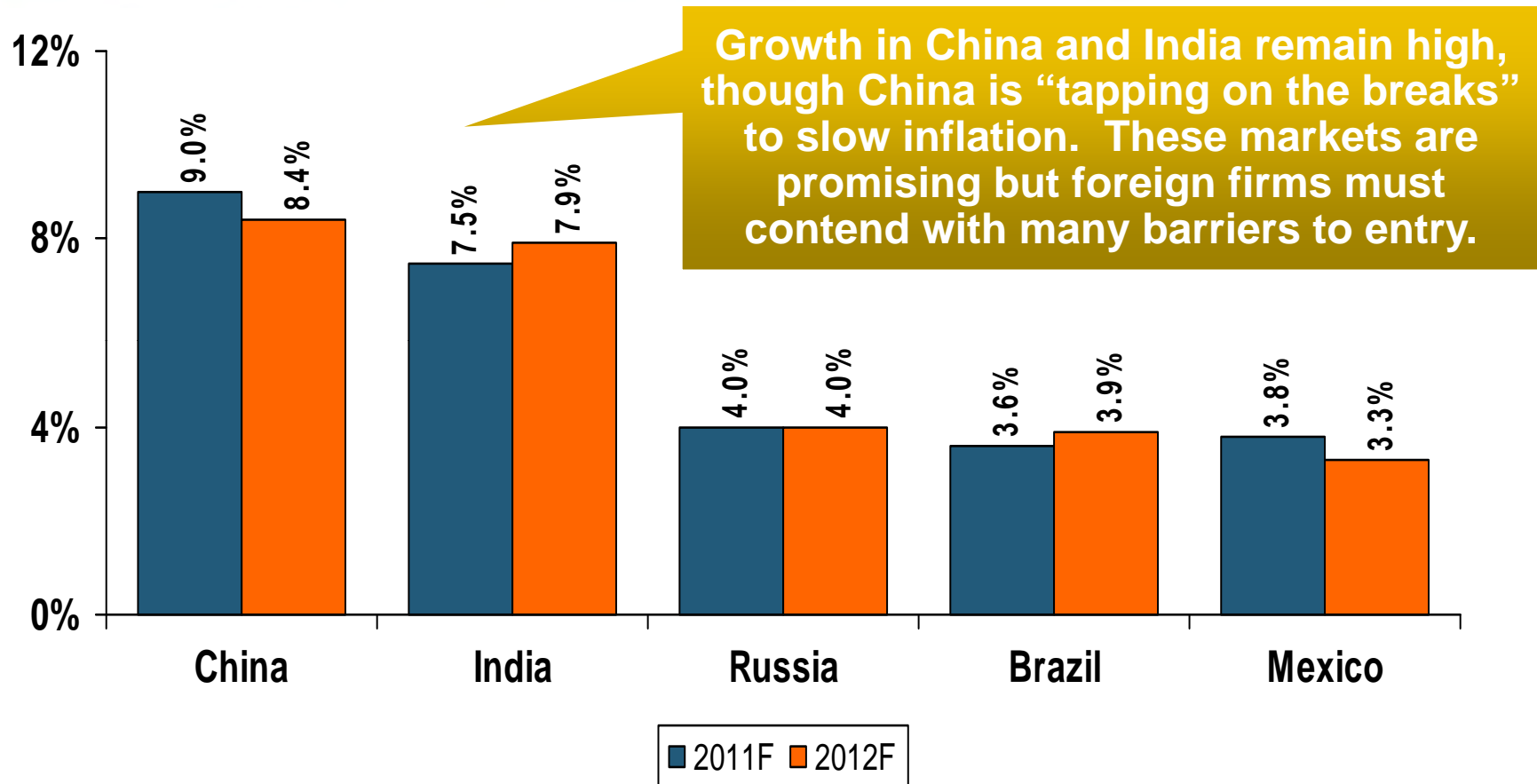


Real GDP Growth Forecasts for Advanced Economies: 2011 - 2012



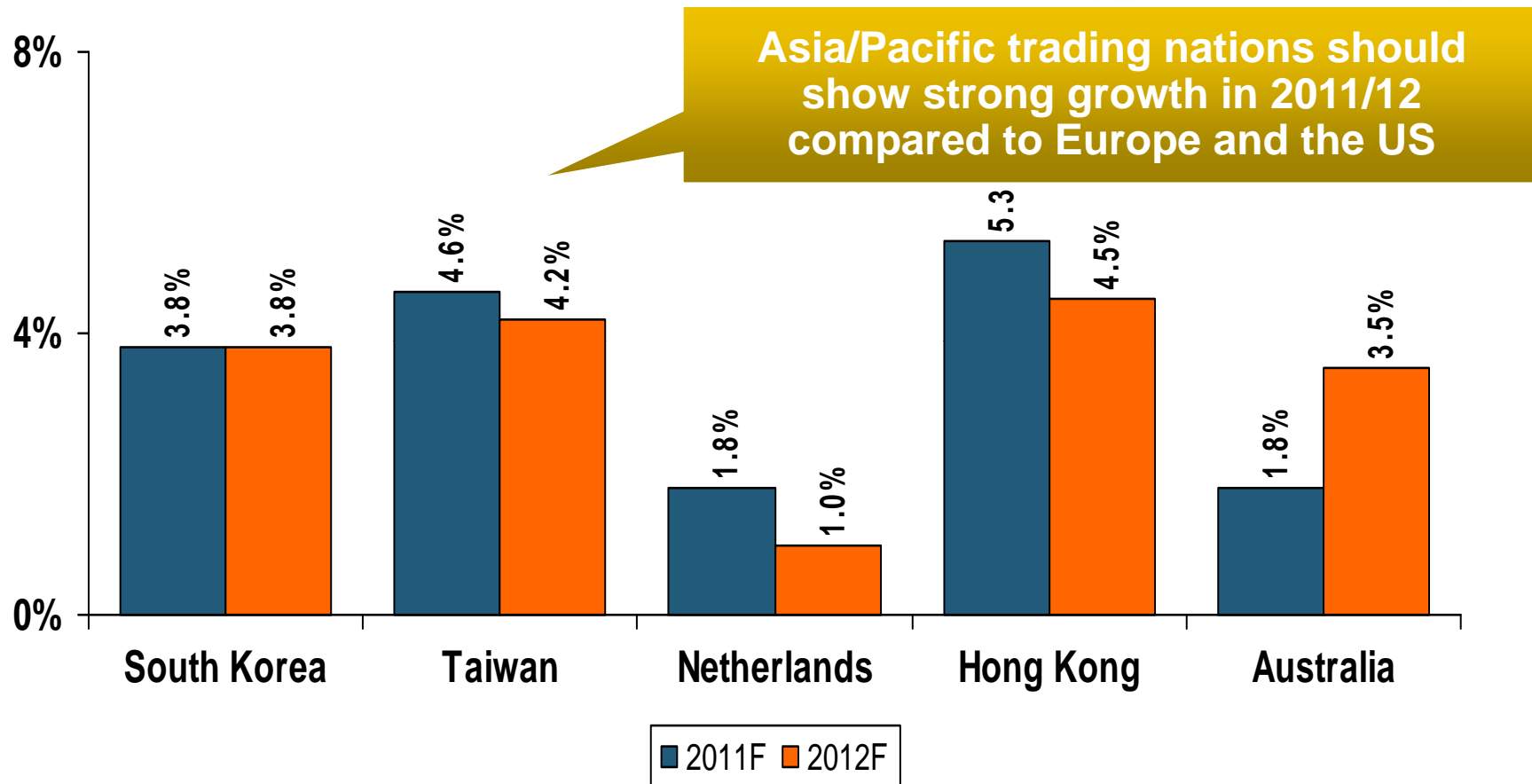
Growth projections could slow for 2011 and 2012 have been revised downward as austerity measures take effect and concerns related to sovereign debt worsen

Real GDP Growth Forecasts for Key Developing Economies: 2011 - 2012



Growth in emerging and developing economies will greatly outpace advanced country growth in 2011/12. This will accelerate the growth of insurance exposures in emerging markets relative to the U.S., W. Europe and Japan.

Real GDP Growth Forecasts for Other Key Trading Economies: 2011 - 2012



Growth in industrialized Asian economies will greatly outpace much of the rest of the world in 2011/12. This will accelerate the growth of insurance exposures in emerging markets relative to the U.S., W. Europe and Japan.

Other Cycle-Influencing Factors

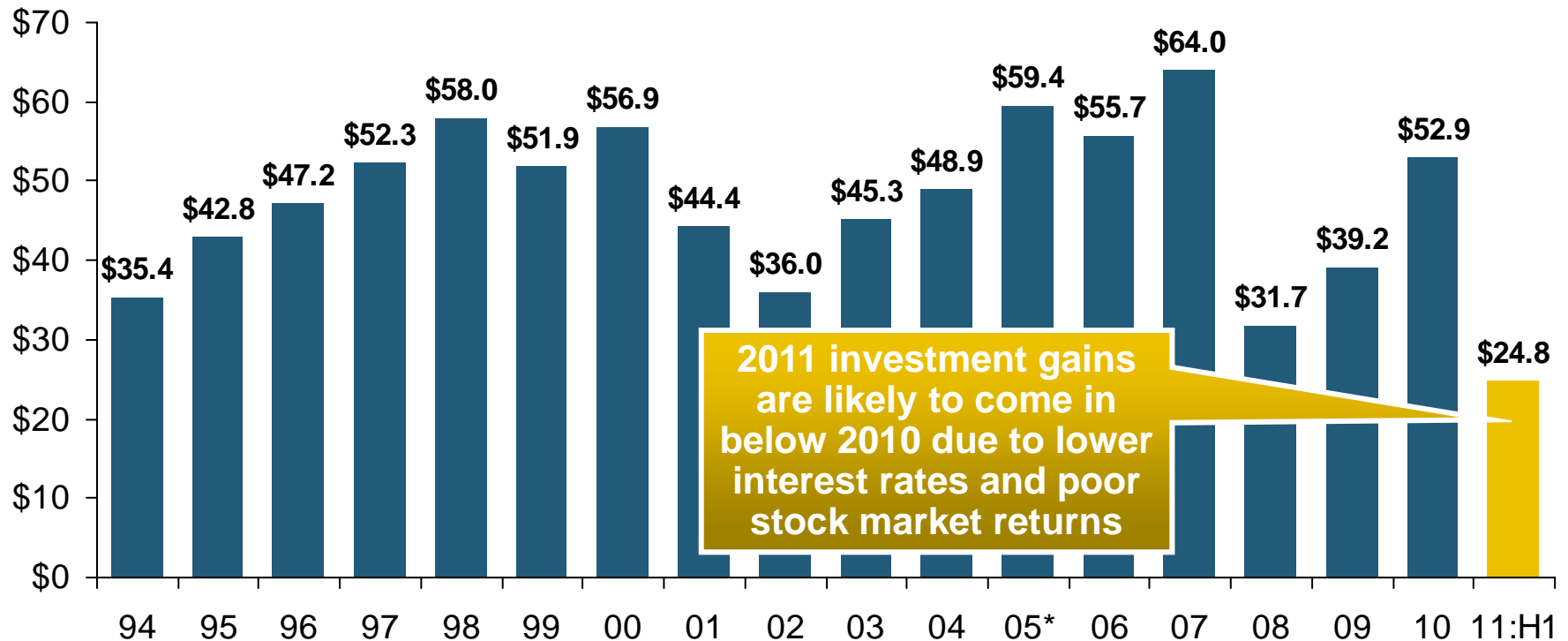
**Could Other Factors Act as
a Catalyst to Turn the
Market?**

INVESTMENTS: THE NEW REALITY

**Investment Performance is a
Key Driver of Profitability
*Does It Influence
Underwriting or Cyclicalities?***

Property/Casualty Insurance Industry Investment Gain: 1994–2011:H1¹

(\$ Billions)



2011 investment gains are likely to come in below 2010 due to lower interest rates and poor stock market returns

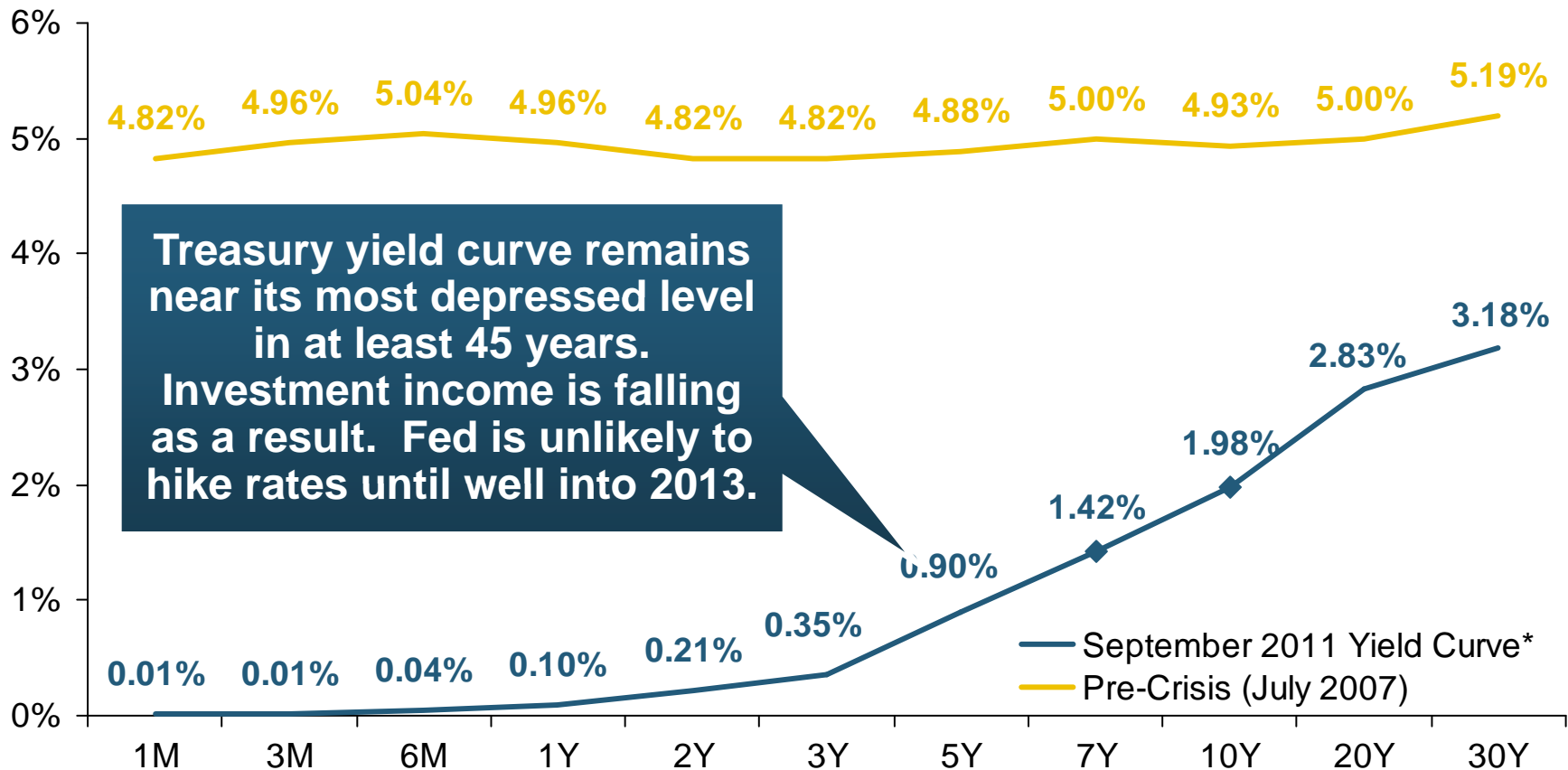
Investment Gains Recovered Significantly in 2010 Due to Realized Investment Gains; The Financial Crisis Caused Investment Gains to Fall by 50% in 2008

¹ Investment gains consist primarily of interest, stock dividends and realized capital gains and losses.

* 2005 figure includes special one-time dividend of \$3.2B.

Sources: ISO; Insurance Information Institute.

Treasury Yield Curves: Pre-Crisis (July 2007) vs. Sept. 2011*



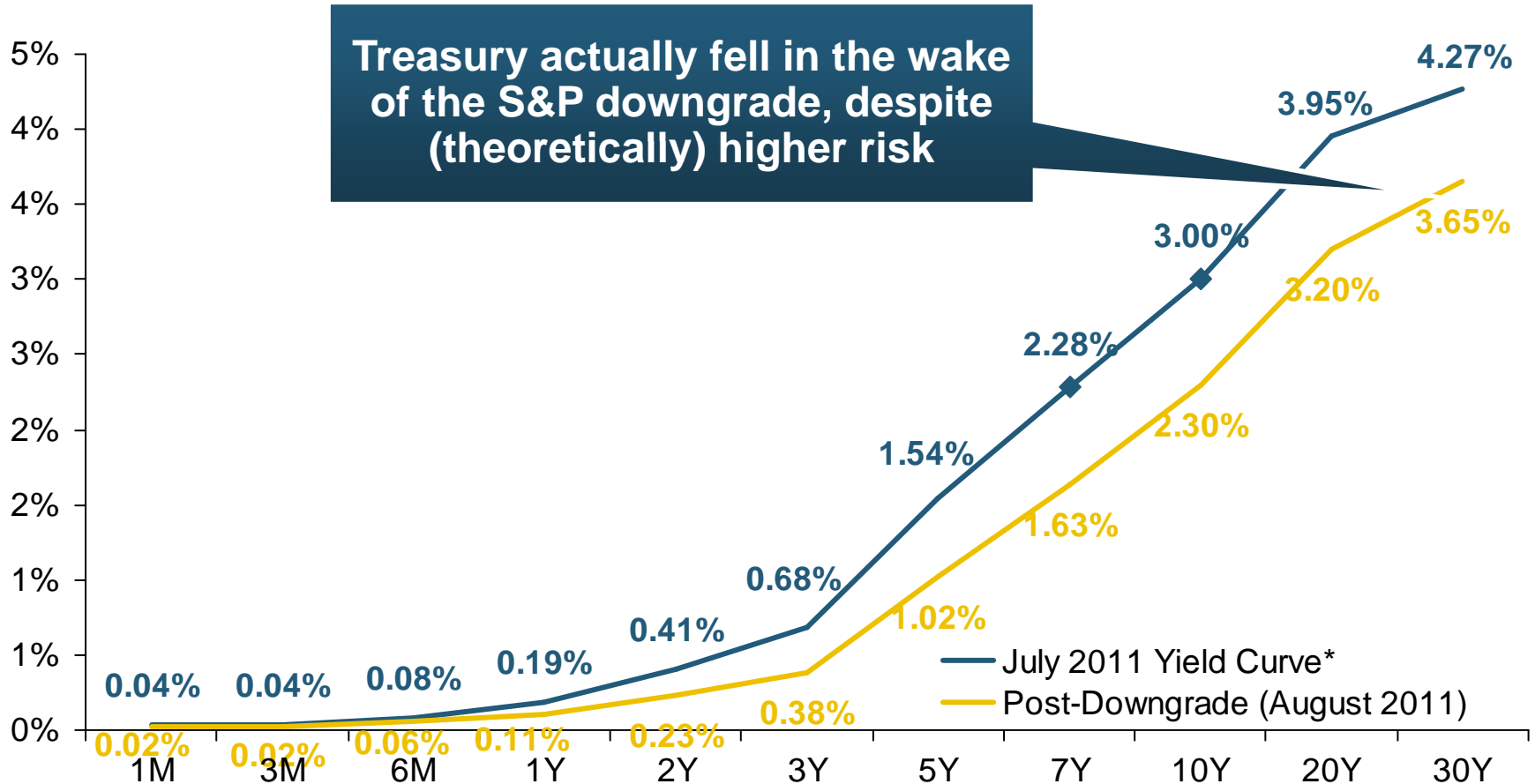
Treasury yield curve remains near its most depressed level in at least 45 years. Investment income is falling as a result. Fed is unlikely to hike rates until well into 2013.

The End of the Fed's Quantitative Easing Is Unlikely to Push Interest Rates Up Substantially Given Ongoing Economic Weakness

*Average of daily rates.

Sources: Board of Governors of the United States Federal Reserve Bank; Insurance Information Institute.

Treasury Yield Curves Before and After S&P Downgrade

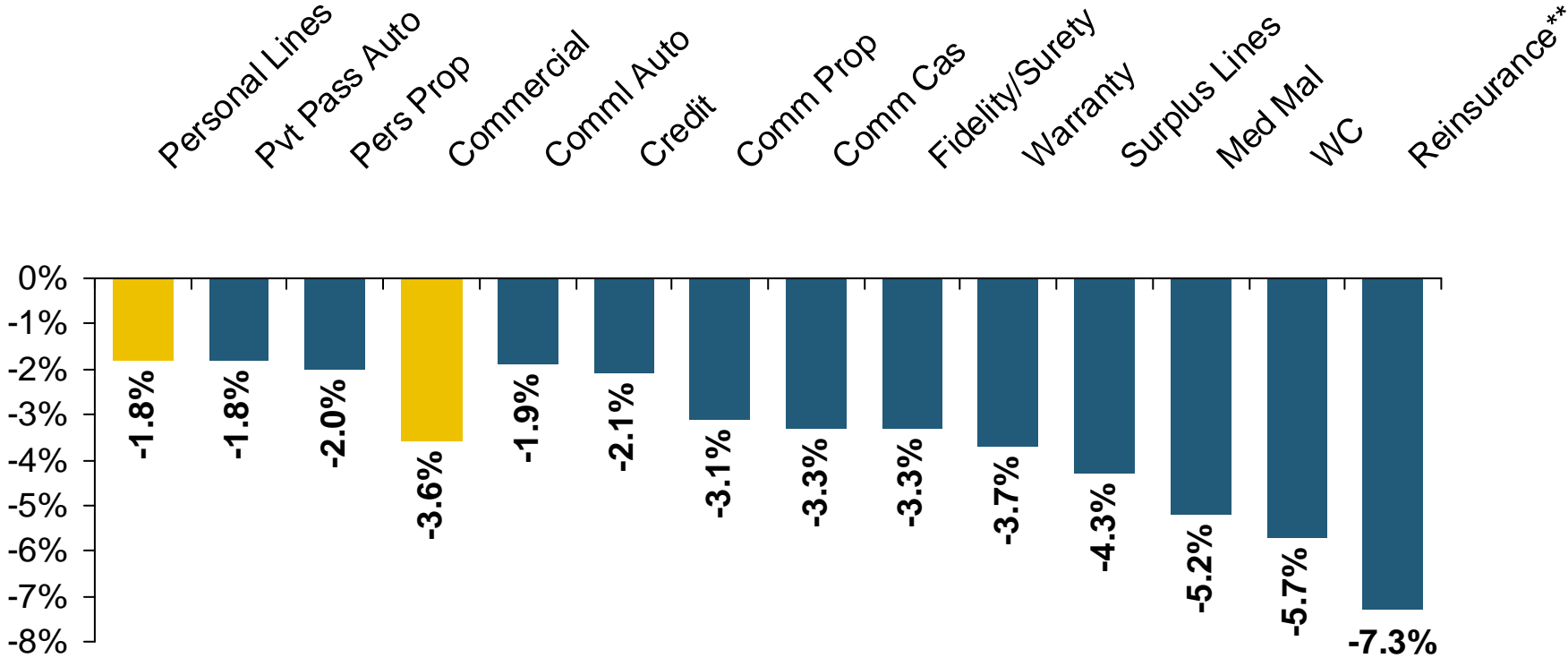


S&P's Downgrade on August 5th Did Not Increase the Borrowing Costs of the US Government. In Fact, Treasury Yields Fell Afterwards

*Average of daily rates.

Sources: Board of Governors of the United States Federal Reserve Bank; Insurance Information Institute.

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

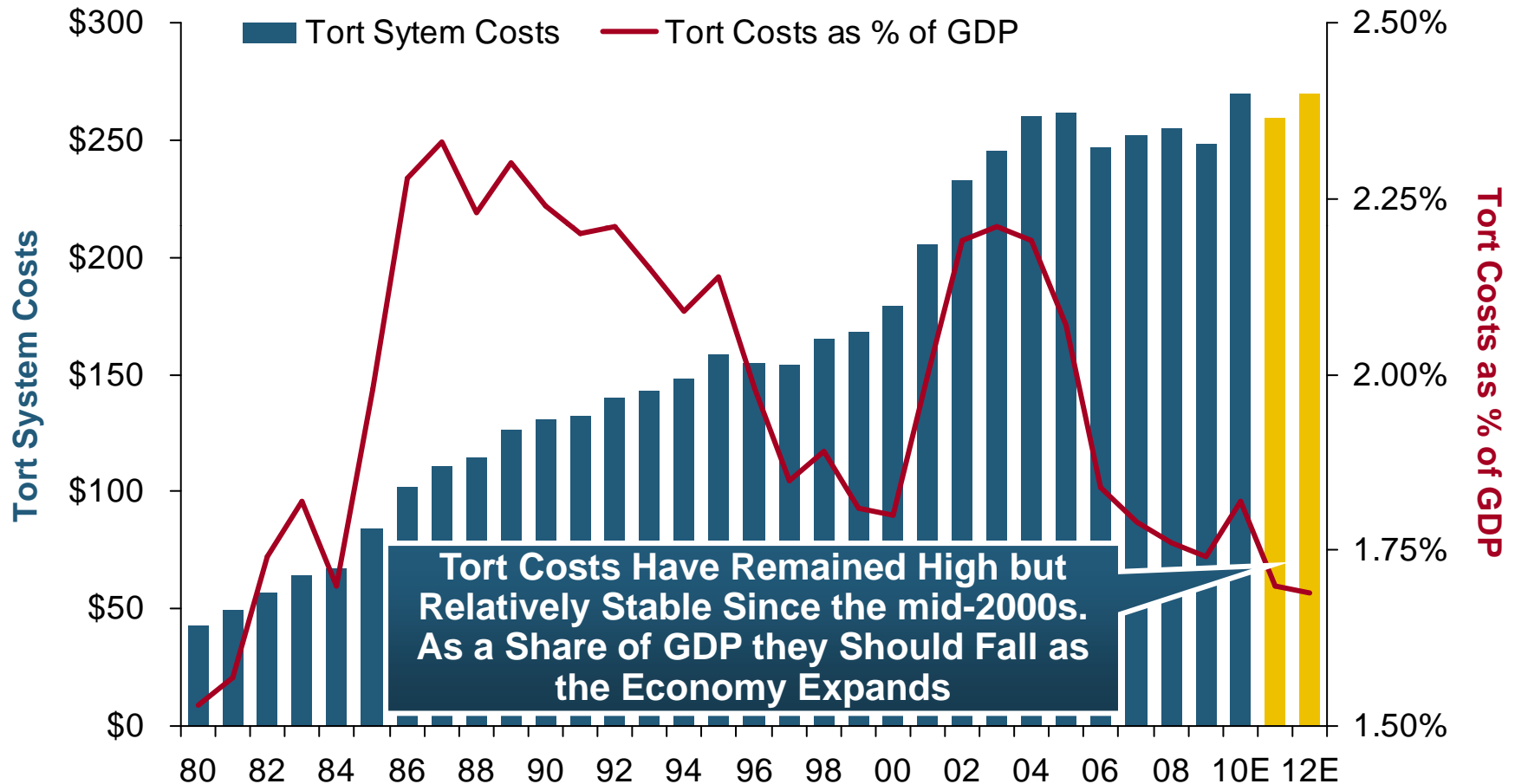
Source: A.M. Best; Insurance Information Institute.

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

(\$ Billions)



Business Leaders Ranking of Liability Systems in 2010

Best States

1. Delaware
2. North Dakota
3. Nebraska
4. Indiana
5. Iowa
6. Virginia
7. Utah
8. Colorado
9. Massachusetts
10. South Dakota

New in 2010

- North Dakota
- Massachusetts
- South Dakota

Drop-offs

- Maine
- Vermont
- Kansas

Midwest/West has mix of good and bad states.

Worst States

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

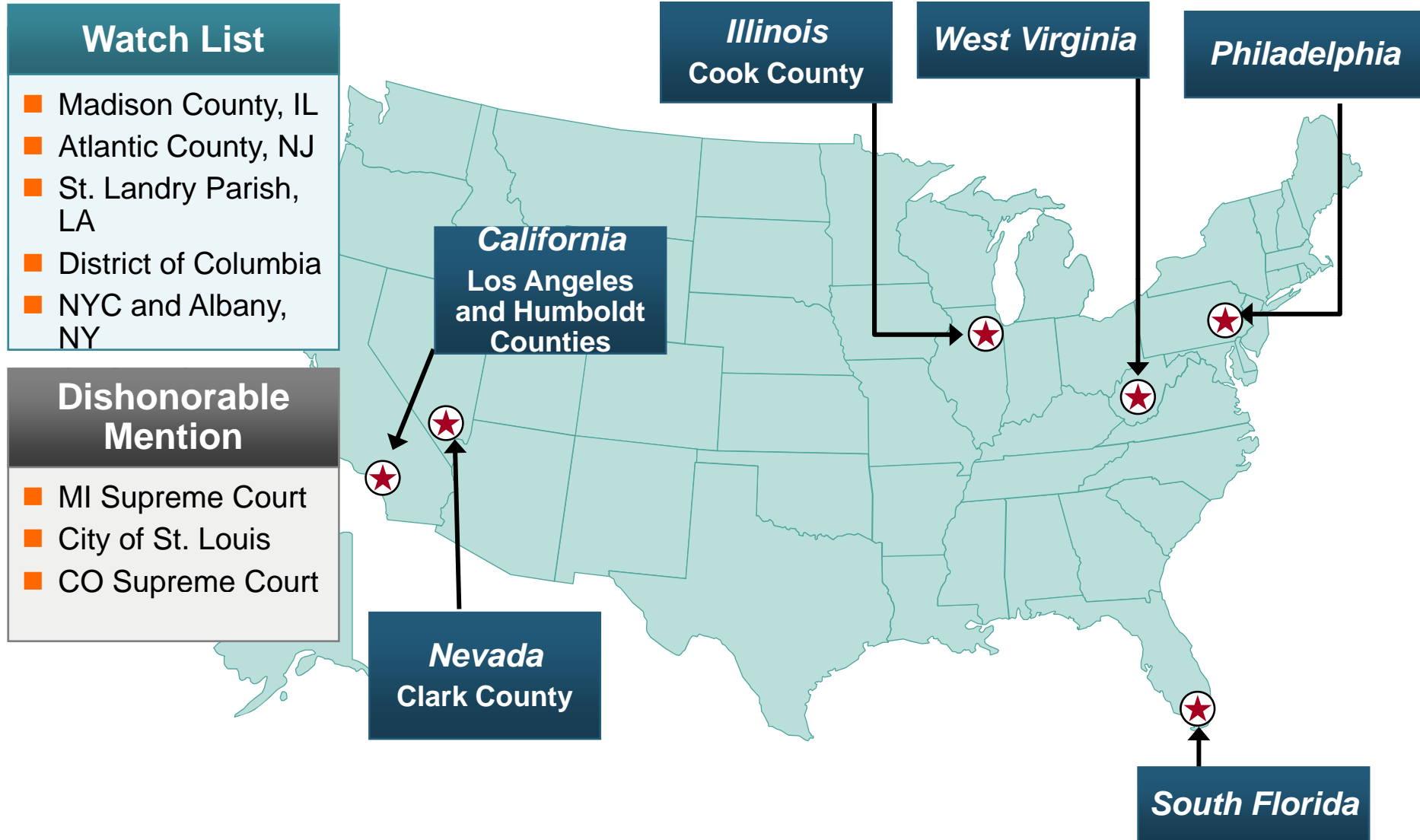
Newly Notorious

- New Mexico
- Montana
- Arkansas

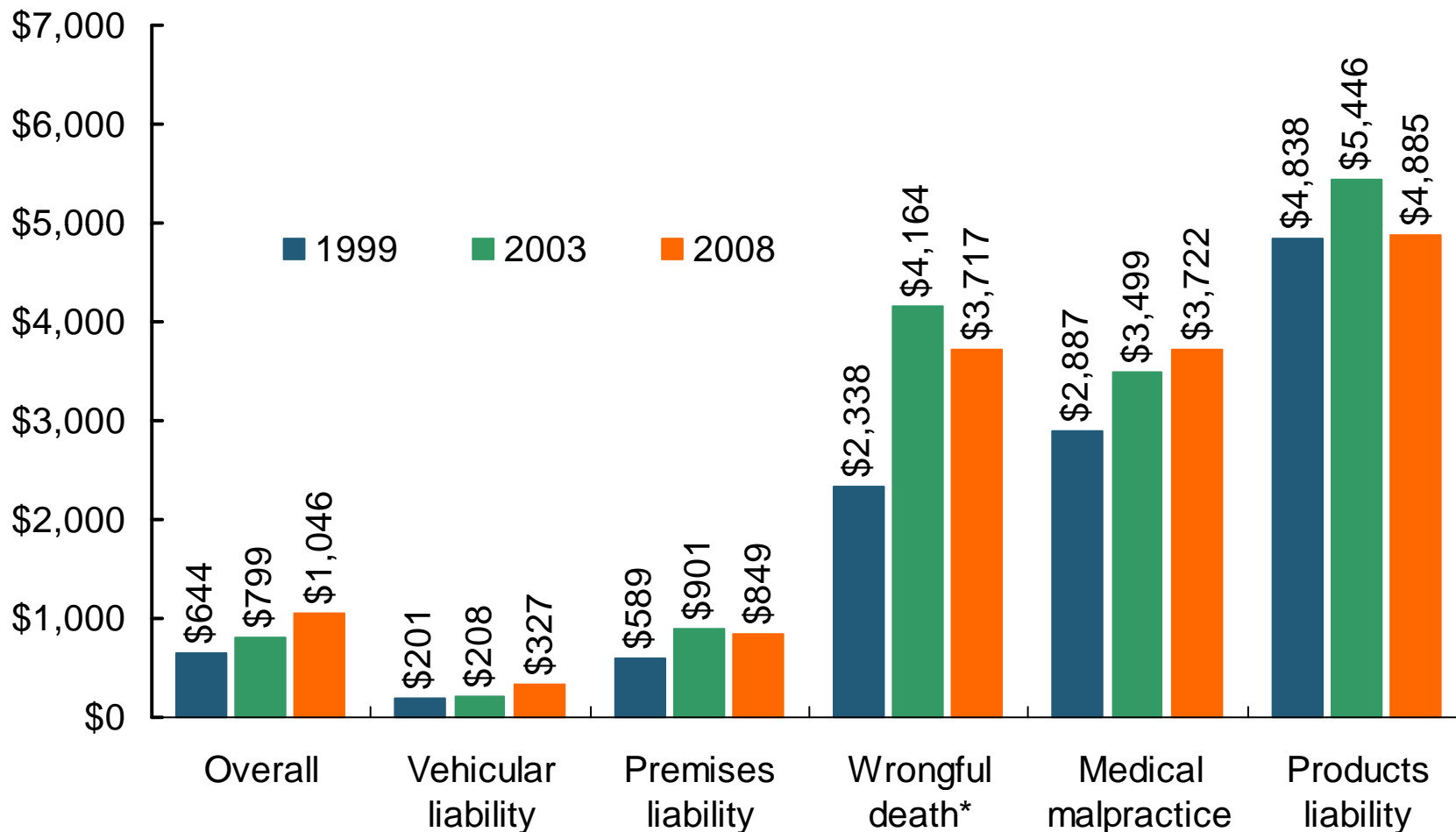
Rising Above

- **Texas**
- South Carolina
- Hawaii

The Nation's Judicial Hellholes: 2010



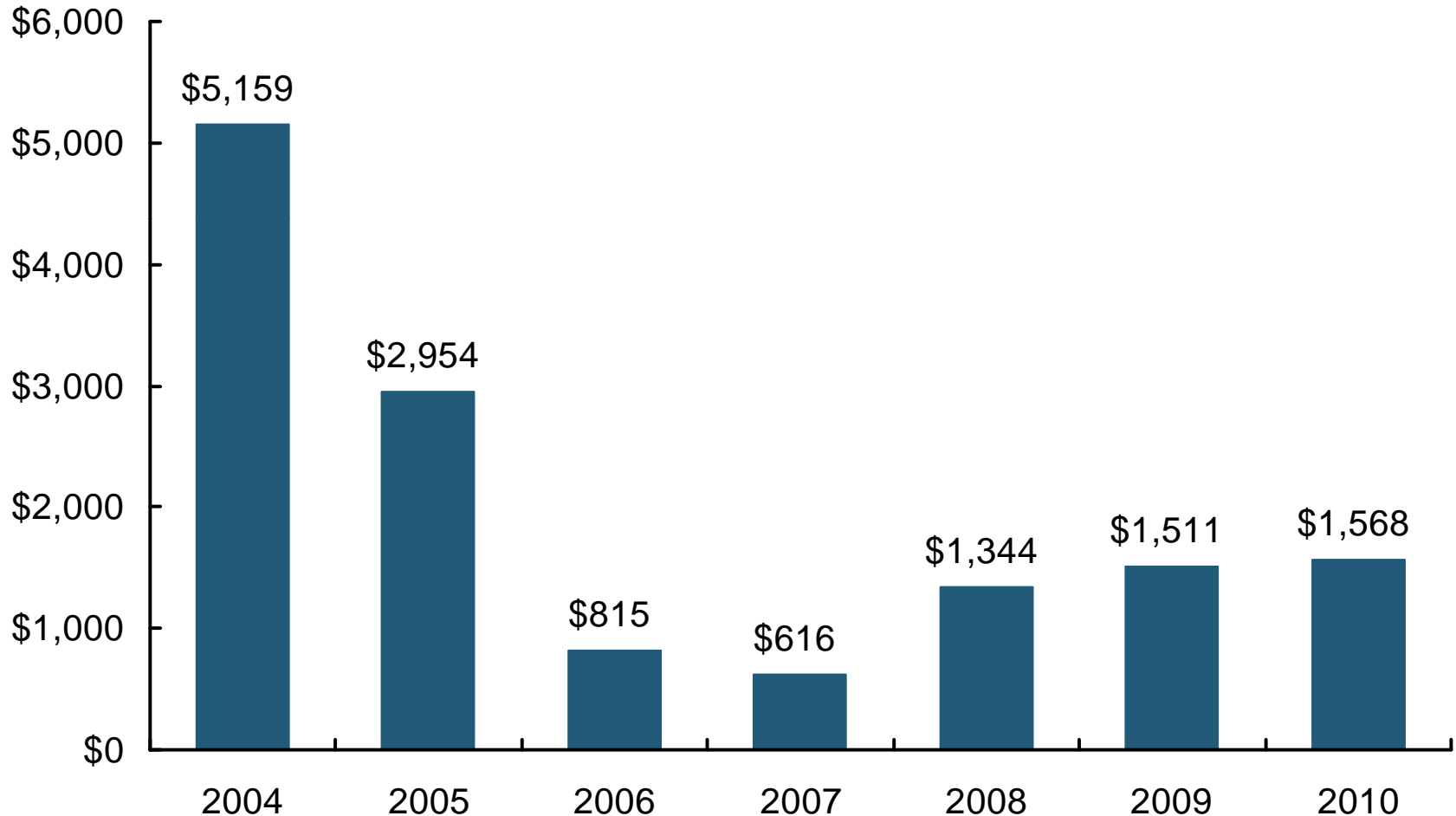
Avg. Jury Awards 1999 vs. 2003 and 2008



*Award trends in wrongful deaths of adult males.

Source: Jury Verdict Research; Insurance Information Institute.

Sum of Top 10 Jury Awards 2004-2010

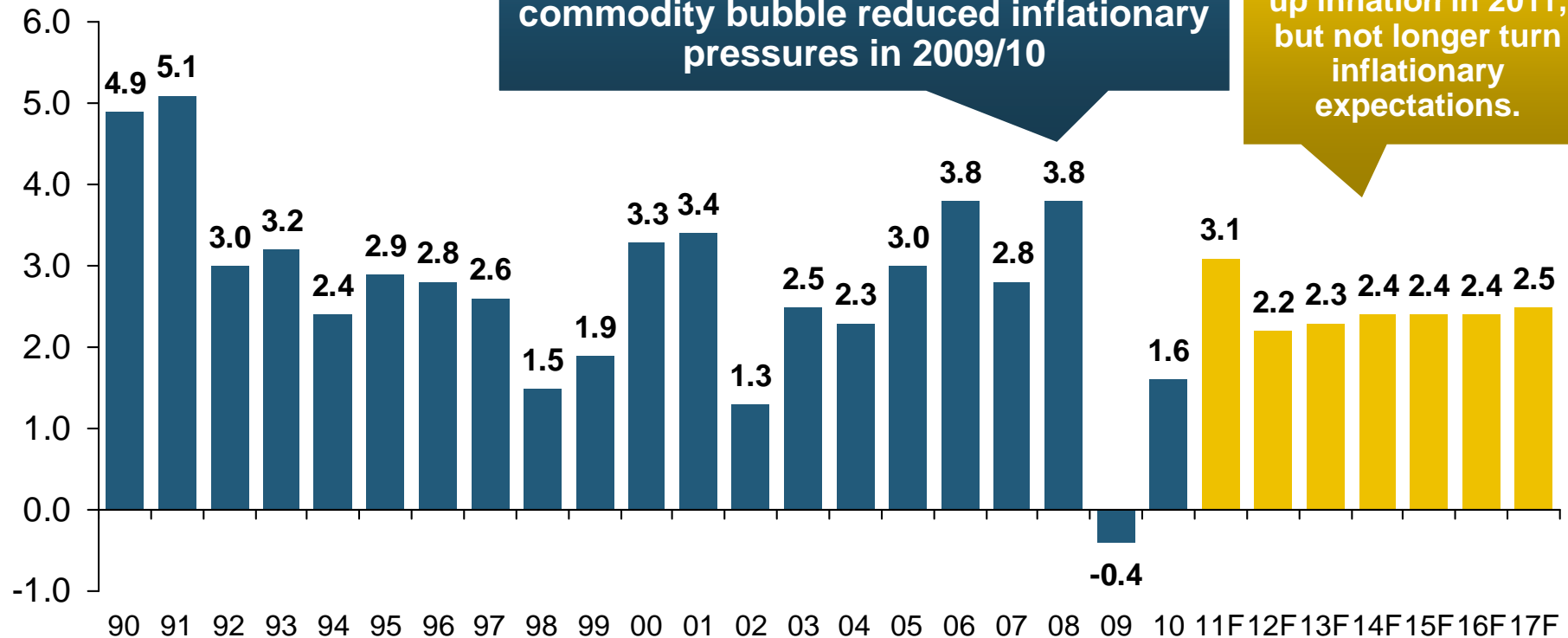


Inflation

**Is it a Threat to Claim Cost
Severities**

Annual Inflation Rates, (CPI-U, %), 1990–2017F

Annual Inflation Rates (%)



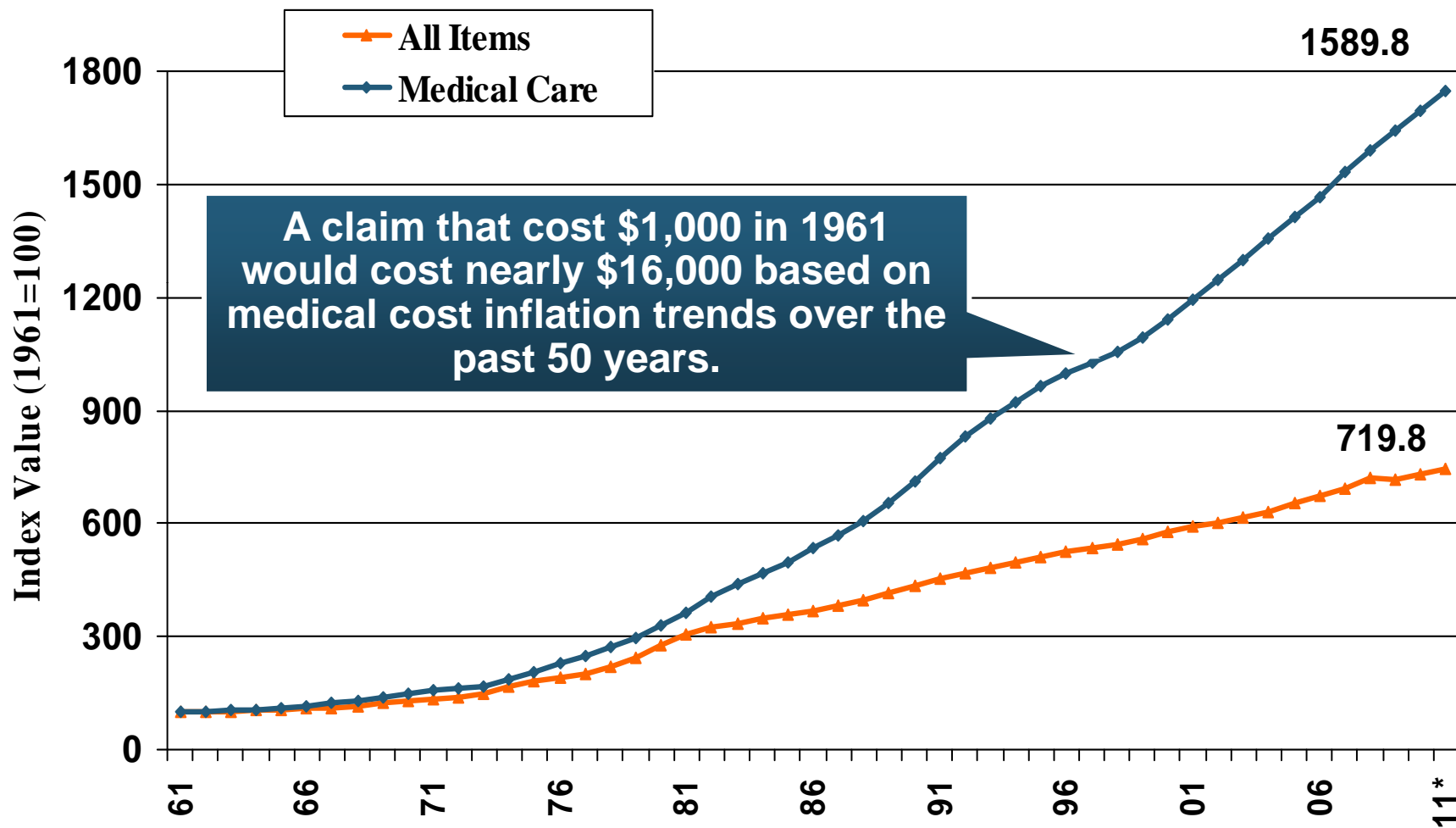
Inflation peaked at 5.6% in August 2008 on high energy and commodity crisis. The recession and the collapse of the commodity bubble reduced inflationary pressures in 2009/10

Higher energy, commodity and food prices are pushing up inflation in 2011, but not longer turn inflationary expectations.

The slack in the U.S. economy suggests that inflation should not heat up before 2012, but other forces (commodity prices, inflation in countries from which we import, etc.), plus U.S. debt burden, remain longer-run concerns

Sources: US Bureau of Labor Statistics; Blue Chip Economic Indicators, 10/11 (forecasts).

Medical Cost Inflation Has Outpaced Overall Inflation Over 50 Years



*Based on change from Feb. 2011 to Feb. 2010 (latest available)
Source: Department of Labor (Bureau of Labor Statistics)

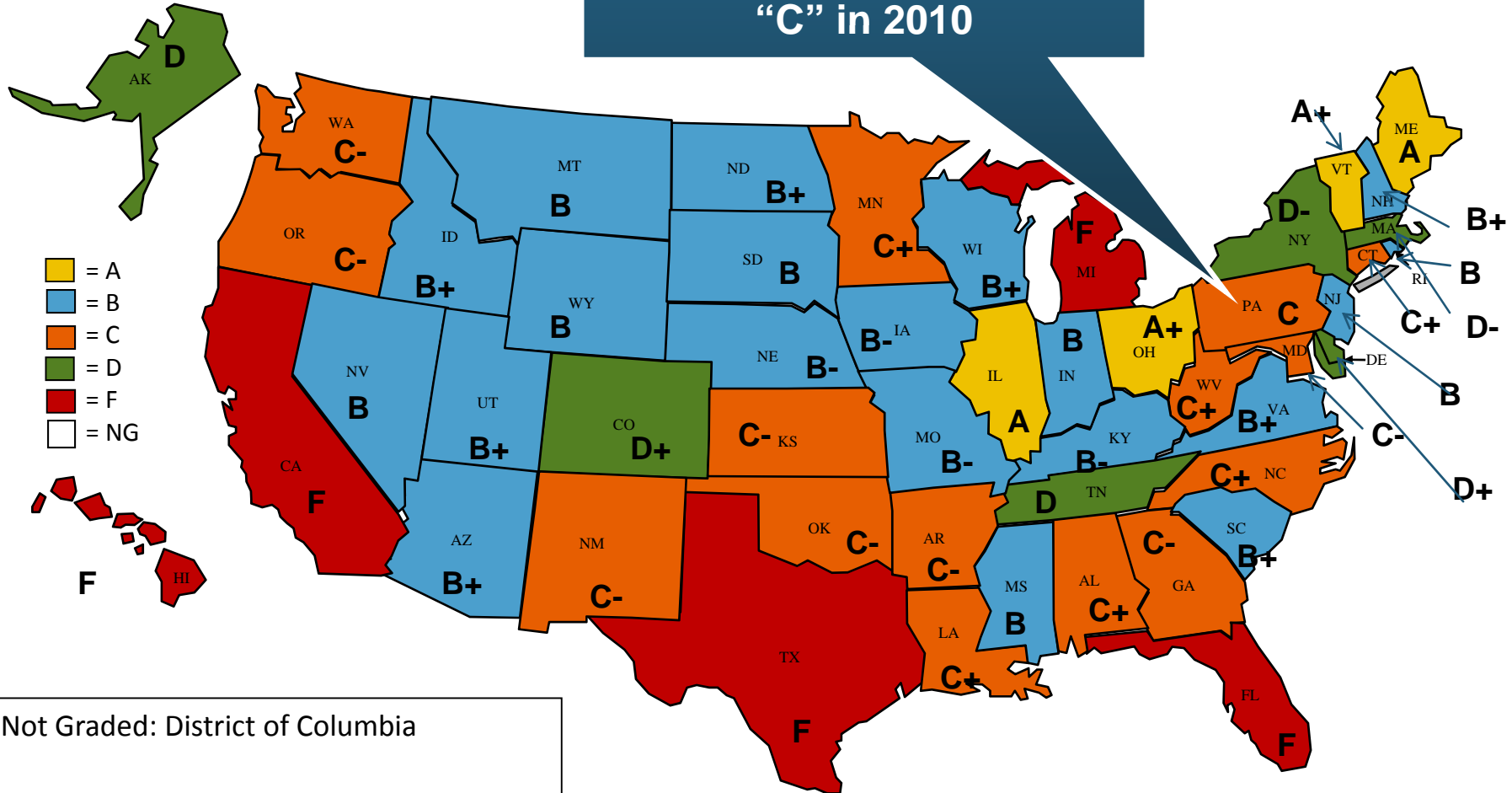


Regulatory Environment & Financial Services Reform

**Insurers Not as Impacted as
Banks, But Dodd-Frank
Implementation Has Been a
Concern for Insurers**

2010 Property and Casualty Insurance Regulatory Report Card

Pennsylvania's regulatory environment got a grade of "C" in 2010



Not Graded: District of Columbia

Dodd-Frank & Insurance One Year: *Status Report*

Expectations vs. Reality



Dodd-Frank Implementation

Status Report for Insurers: Slow Start

The Dodd-Frank Wall Street Reform and Consumer Protection Act

- **Financial Stability Oversight Council—*Slow to Consider Insurer Concerns***
 - FSOC deliberates largely behind closed doors
 - Criteria and process for designation of Systemically Important Financial Institutions (SIFIs) were not announced until October 12, 2011
 - ***Possible that small number of US insurers will be designated as SIFIs***
 - Operated/deliberated until late September 2011 without a voting member representing the insurance industry
 - ***Roy Woodall, approved by Senate in Sept. 27, 2011, is the sole voting representative for the entire p/c and life insurance industry (was Kentucky Ins. Comm. 1966-1967; Worked in other insurance trade posts, Treasury)***
 - Two non-voting FSOC members represent insurance interests:
 - ***FIO Director Michael McGraith (started June 1, 2011)***
 - ***Missouri Insurance Director John Huff (started in Sept. 2010)***
 - ***Not allowed to brief fellow regulators on FSOC discussions***

Dodd-Frank Implementation: *SYSTEMIC RISK CRITERIA*

The Dodd-Frank Act and Systemic Importance

- All Banks with Assets > \$50B Considered Systemically Important
- Non-Bank Financial Groups with Global Consolidated Assets > \$50B Will Be Examined for Systemic Riskiness, But Not Automatically Labeled as a Systemically Important Financial Institution (SIFI)
 - Foreign firms with assets in the US exceeding \$50 billion will also fall under review
- If Firm Exceeds the \$50B Threshold, a 3-Stage Test Applies
- **STAGE 1:** Non-Banks Financial Groups with \$50B+ Assets Will Be Evaluated on Five “Uniform Quantitative Thresholds,” at Least One of Which Will Have to Be Met to Trigger a Further (Stage 2) Review Potentially Leading to a SIFI Designation
 - **Leverage:** Would have to be leveraged more than 15:1 (insurers unlikely to trigger)
 - **ST Debt-to-Assets:** Would have to a ratio of ST debt (less than 12 months to maturity) to consolidate assets exceeding 10%
 - **Debt:** Have total debt exceeding \$20 billion (i.e., loans borrowed and bond issues)
 - **Derivative Liabilities:** Have derivative liabilities exceeding \$3.5 billion
 - **Credit Default Swaps:** Have more than \$30 billion CDS outstanding for which the nonbank financial firm is the reference entity (i.e., CDS written against firm’s failure)
- **Thresholds Considered to Be Guideposts**
 - Not all companies that breach a barrier will be deemed systemically important
 - Regulators retain right to include firms that do meet any of the criteria

Dodd-Frank Implementation: *SYSTEMIC RISK CRITERIA (continued)*

The Dodd-Frank Act and Systemic Importance

- **STAGE 2: Analysis of Firms Triggering Uniform Quantitative Thresholds**
 - Firms triggering one or more of the quantitative thresholds in Stage 1 will be analyzed using publicly available information in order to conduct a more thorough review
 - No data call will be required at this stage
 - Firms viewed as potentially systemically important (candidate SIFIs) will subject to a Stage 3 analysis
- **STAGE 3: Analysis of Candidate Systemically Important Financial Institutions**
 - Firms deemed in Stage 2 to be potentially systemically important will be subjected to more detailed analysis including data not available during the Stage 2 analysis
 - Stage 3 firms will be notified by the FSOC that they are under consideration and will have the opportunity to contest their consideration
- **SIFI DESIGNATION PROCEDURE: 2-Stage Voting Procedure by FSOC is Required Before a Final SIFI Designation is Made**
 - At the conclusion of the Stage 3, FSOC has the authority to propose a firm be designated as a SIFI
 - Requires 2/3 majority vote of FSOC members, including affirmation of the Chair (Treasury Secretary)
 - Potential SIFI firm will be given written explanation for the determination
 - Firm can request a hearing to contest the determination
 - Final determination requires another 2/3 majority of FSOC members and affirmation of the Chair

Dodd-Frank Implementation: *FSOC MEMBERS*

The Dodd-Frank Act and Systemic Importance

Members of the Financial Stability Oversight Council

➤ There are 10 voting members of the FSCO

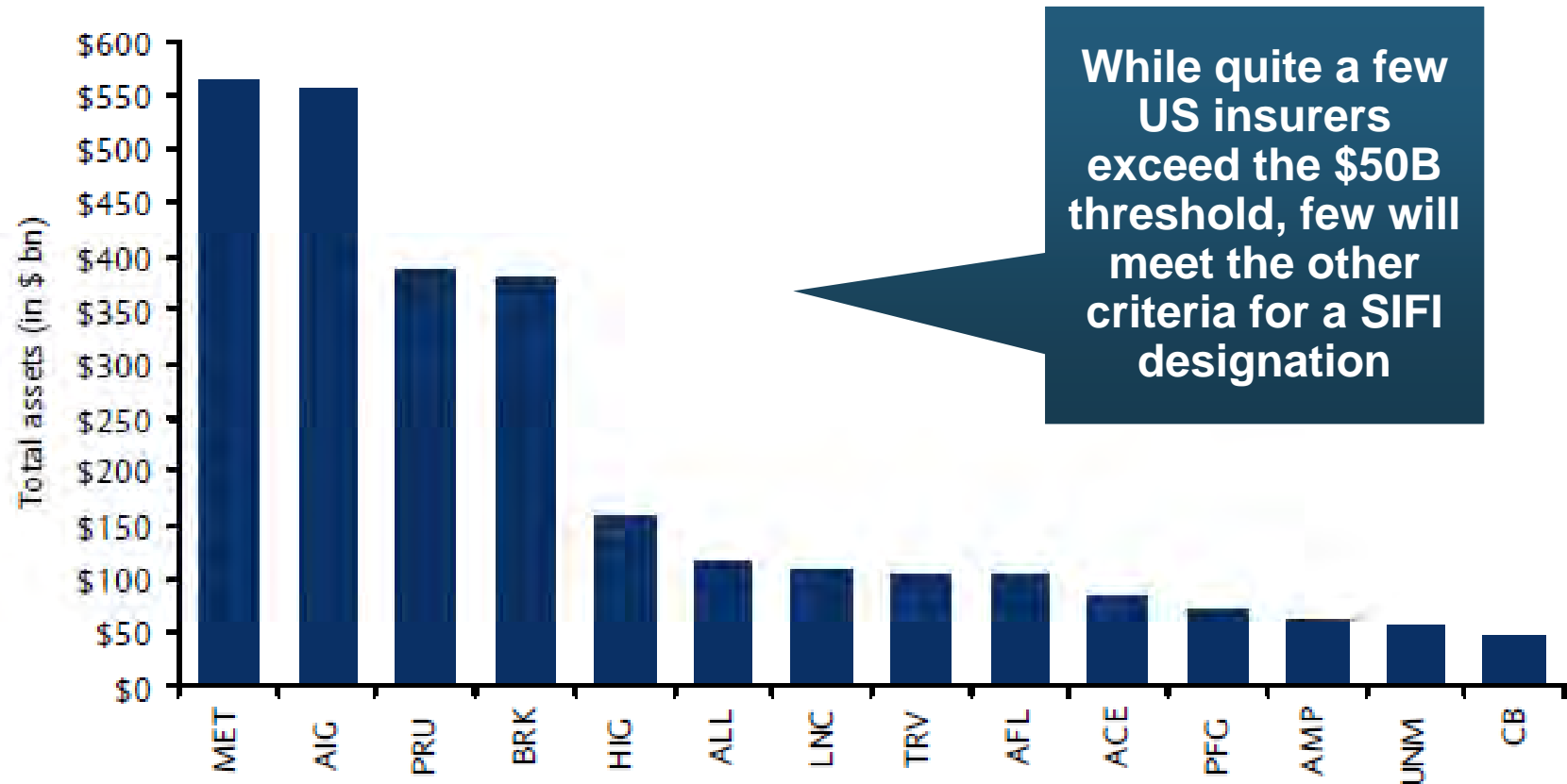
- **Treasury Secretary and FSOC Chair: Timothy Geithner**
- **Federal Reserve Chairman: Ben Bernanke**
- **Securities & Exchange Commission Chairman: Mary Shapiro**
- **Commodities Futures Trading Commission Chairman: Gary Gensler**
- **National Credit Union Administration Chairman: Debbie Matz**
- **(Acting) Comptroller of the Currency: John Walsh**
- **Federal Housing Finance Agency (Acting) Director: Edward DeMarco**
- **Consumer Financial Protection Bureau Director: *Position is Currently Vacant***
- **Independent Insurance Expert: Roy Woodall**

➤ There are 2 nonvoting members of the FSOC representing insurance interests

➤ Federal Insurance Office Director Mike McGraith

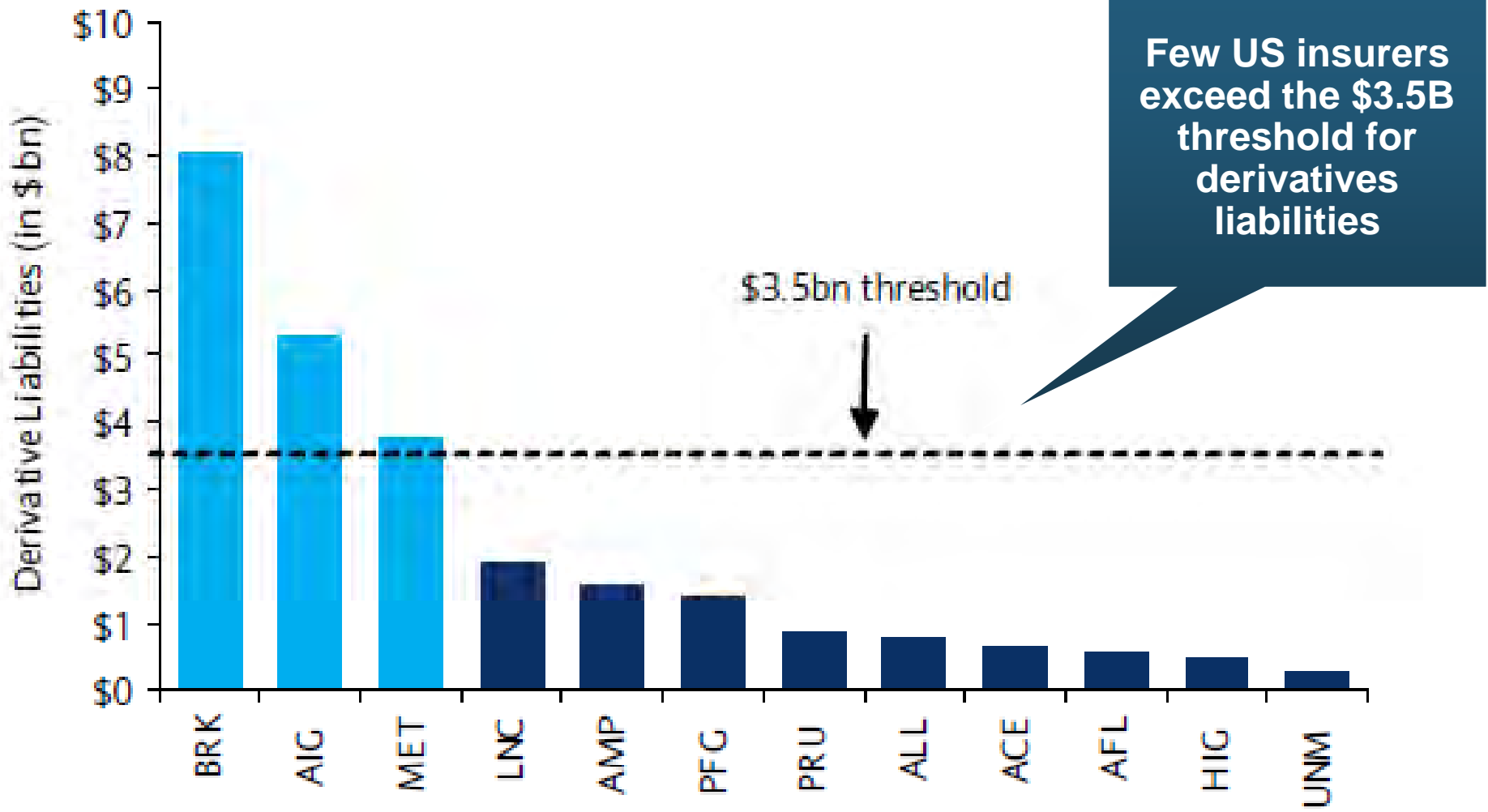
➤ John Huff, Director of the Missouri Insurance Department

Total Assets Greater than \$50 Billion: Publically Traded US Insurers



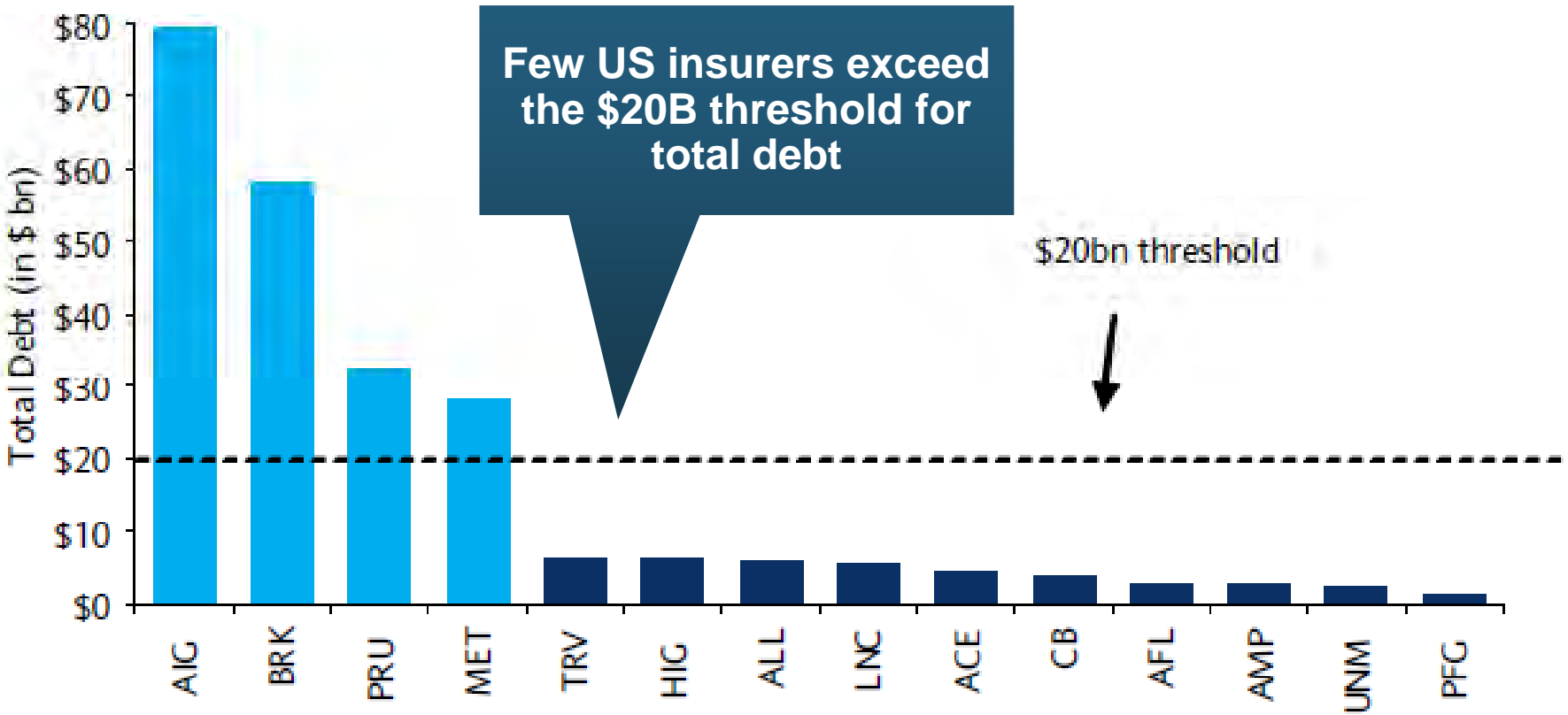
Note: Total assets excluding separate accounts as of 2Q11.

Derivative Liabilities: Publically Traded US Insurers



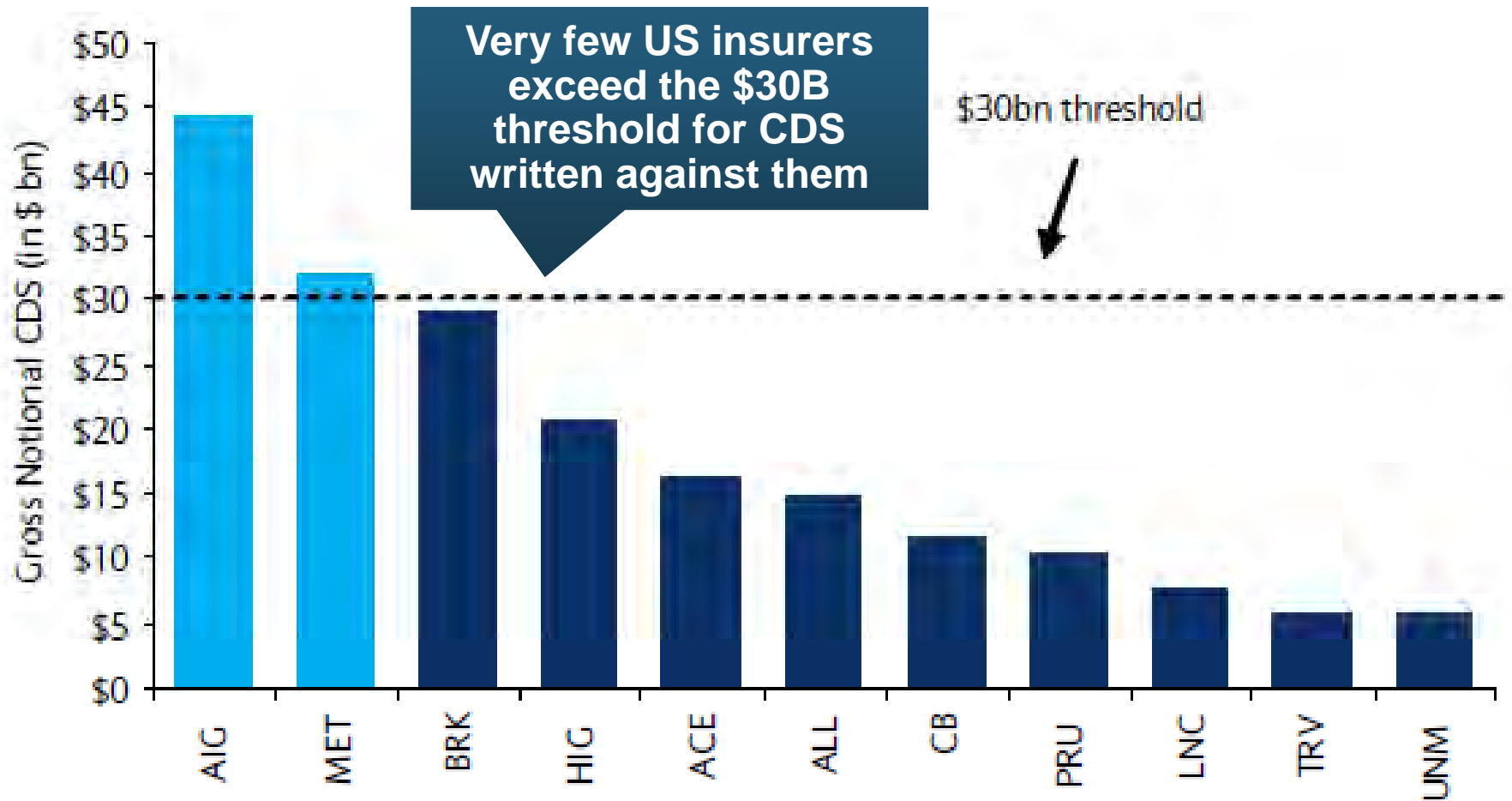
Source: Barclays Capital

Total Debt: Publically Traded US Insurers



Note: Includes short-term and long-term debt outstanding.

Gross Notional Credit Default Swaps: Publically Traded US Insurers



Note: Gross notional CDS outstanding as of October 7 2011.

Dodd-Frank Implementation: *Federal Insurance Office: Very Quiet*

Federal Insurance Office Update: *Activity Update*

■ FIO's First Director Did Not Assume Office Until June 1, 2011

- Former Illinois Insurance Director Michael McGraith
- Small staff (10-12) and modest budget
- McGraith has made few appearances or public comments



■ Study on State of Insurance Regulation Due Jan. 21, 2012

- Report will likely review previously identified inefficiencies and strengths of current regulatory system with an eye toward modernization.

■ Treasury Will Likely Exert Heavy Influence on the Report



“The states remain the functional regulators, [but] the federal government will work toward modernizing and improving our system of insurance regulation.”

*Neal Wolin, Deputy Secretary
Treasury Department*

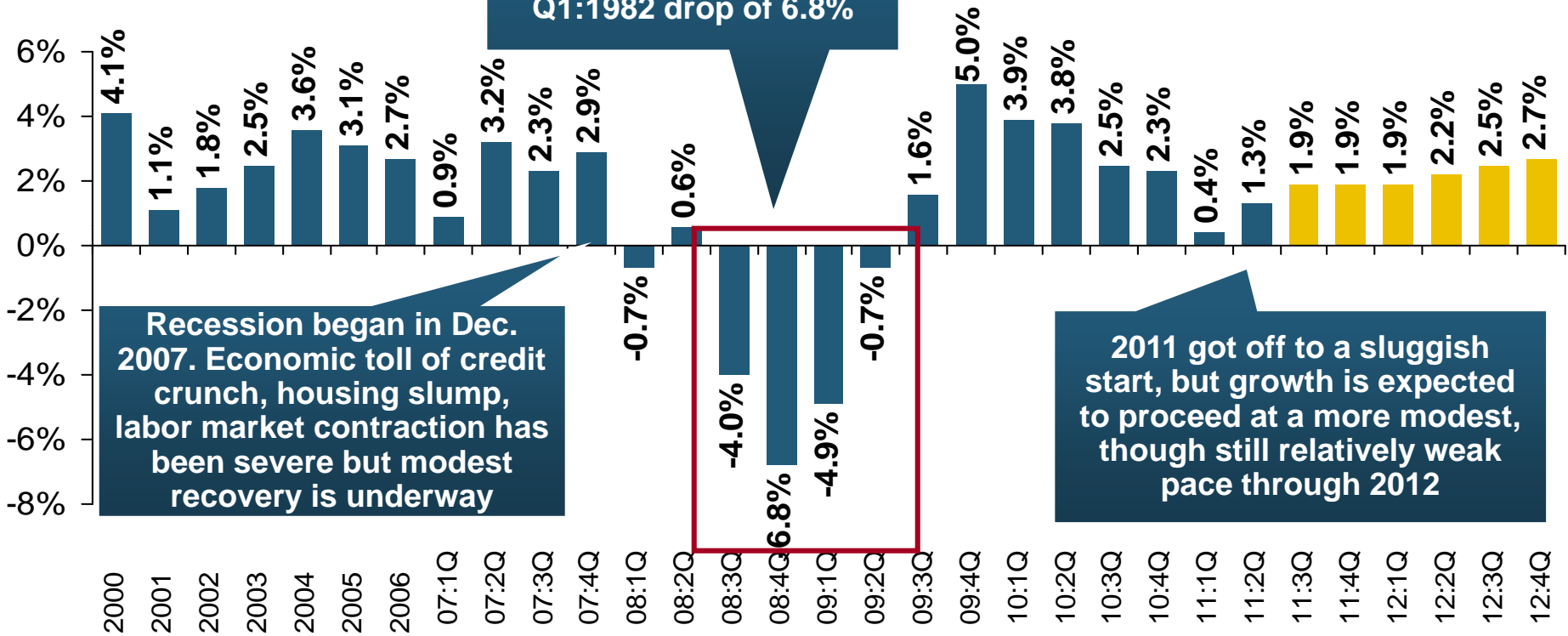
**Former President of P/C
Insurance at The Hartford**

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

**Growth Would Also Help Absorb
Excess Capital**

US Real GDP Growth*

Real GDP Growth (%)



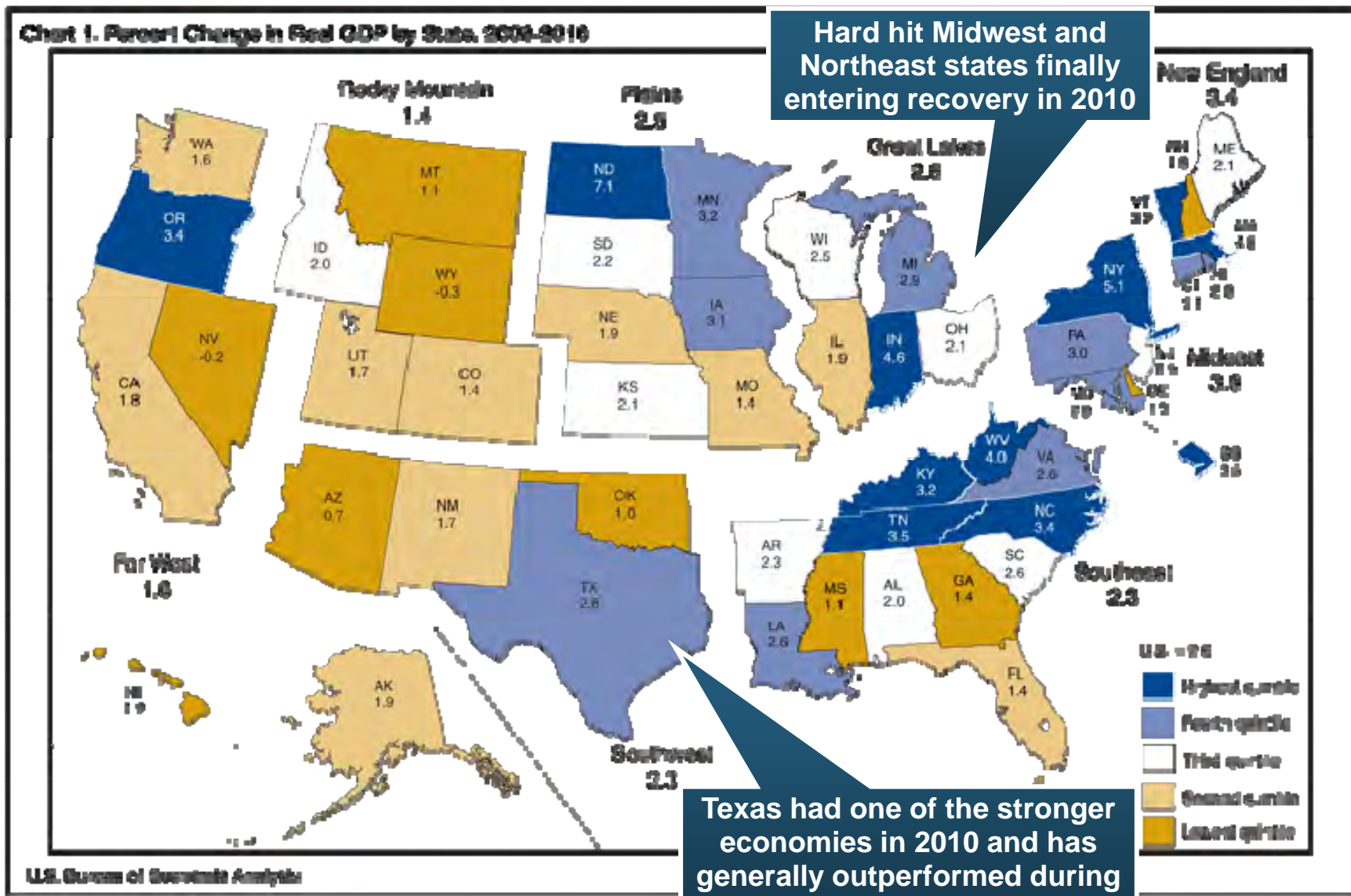
Demand for Insurance Continues To Be Impacted by Sluggish Economic Conditions, but the Benefits of Even Slow Growth Will Compound and Gradually Benefit the Economy Broadly

* Estimates/Forecasts from Blue Chip Economic Indicators.

Source: US Department of Commerce, Blue Economic Indicators 10/11; Insurance Information Institute.

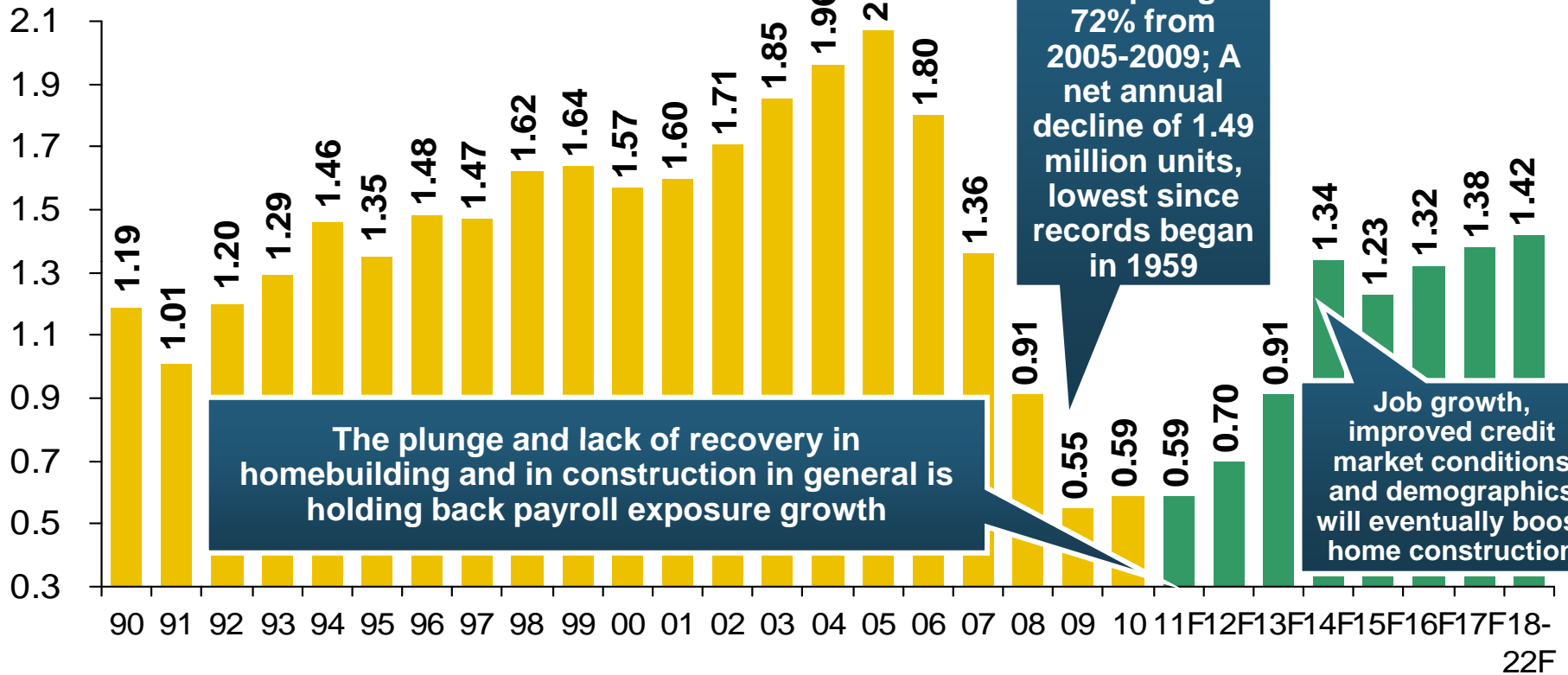
2011 Financial Overview

State Economic Growth Varied in 2010



New Private Housing Starts, 1990-2022F

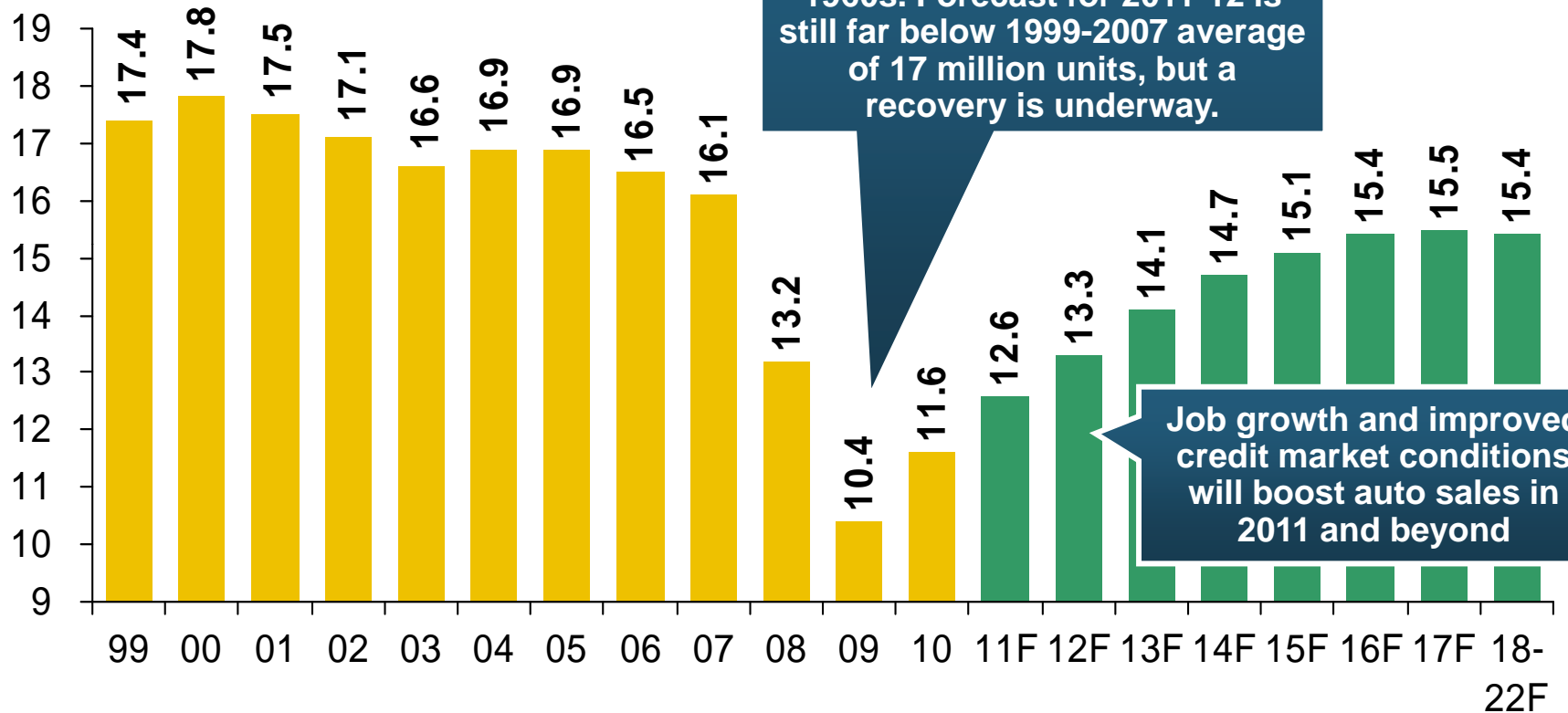
(Millions of Units)



Little Exposure Growth Likely for Homeowners Insurers Until 2014. Also Affects Commercial Insurers with Construction Risk Exposure, Surety

Auto/Light Truck Sales, 1999-2022F

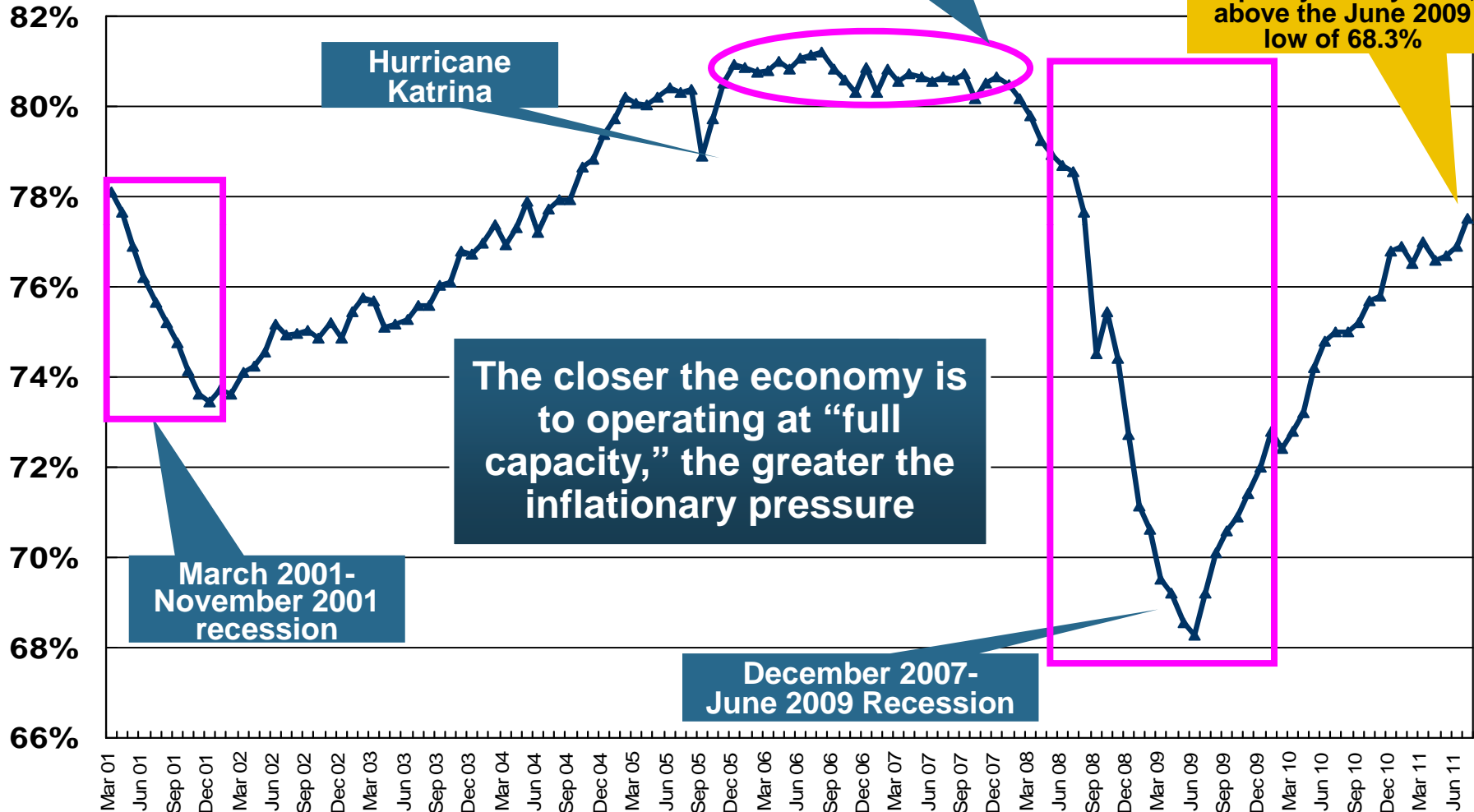
(Millions of Units)



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

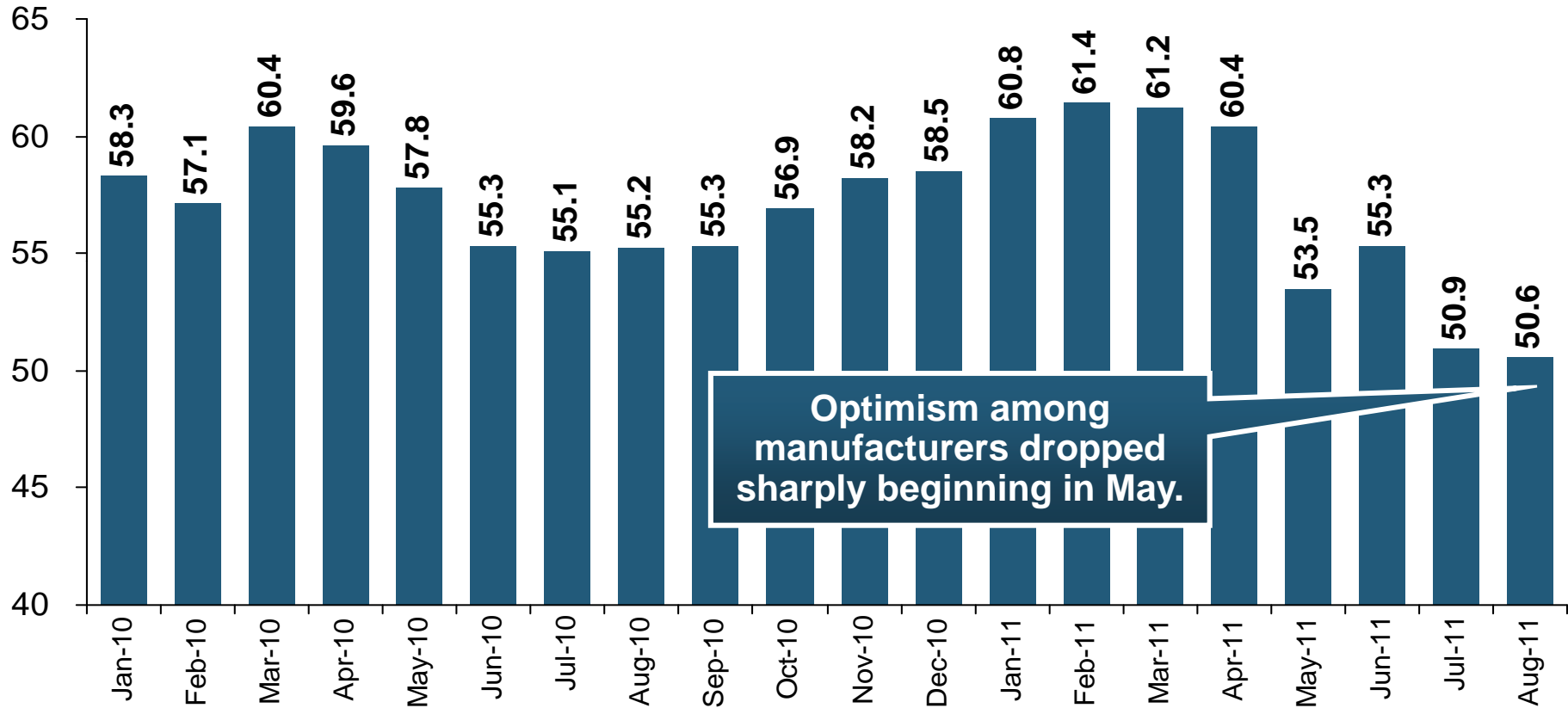
Recovery in Capacity Utilization is a Positive Sign for Commercial Exposures

Percent of Industrial Capacity



ISM Manufacturing Index (Values > 50 Indicate Expansion)

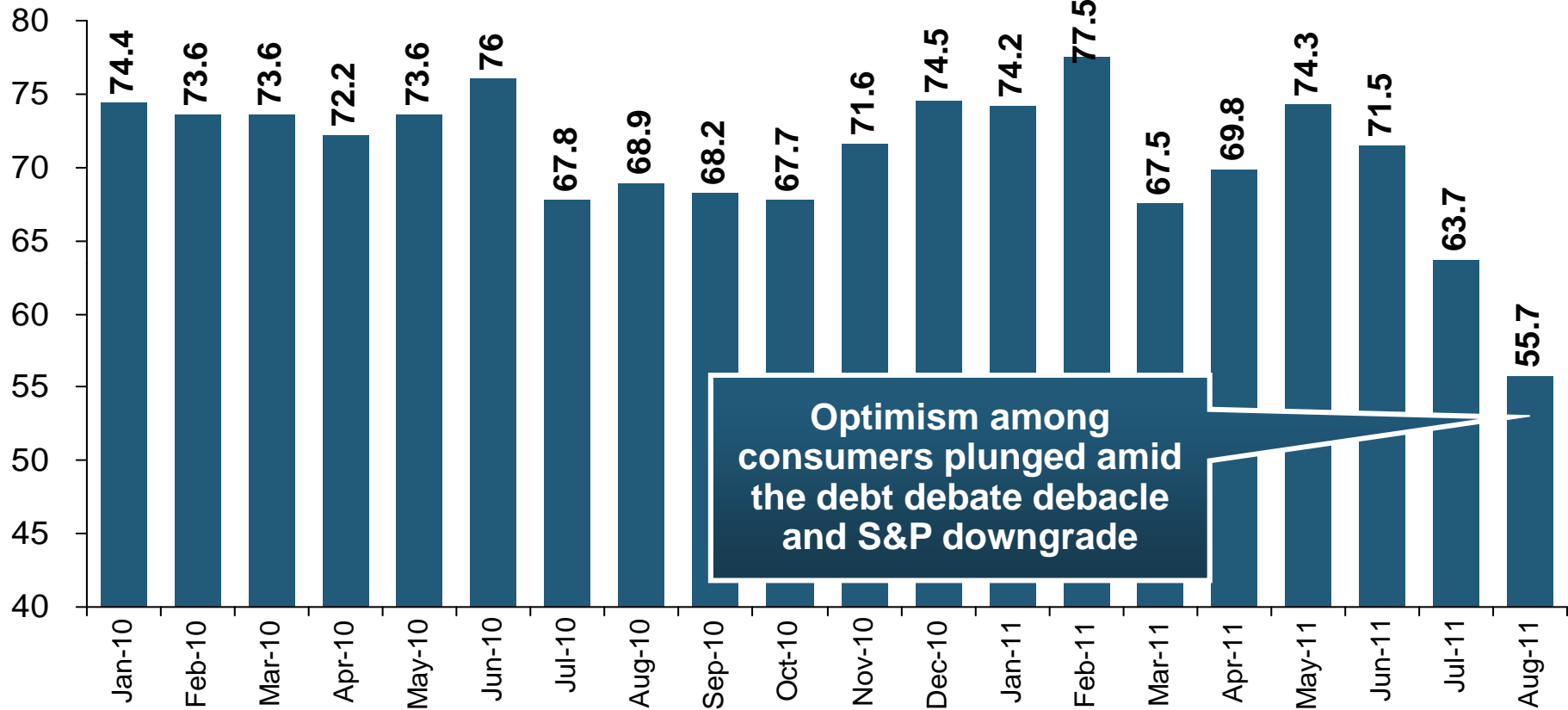
January 2010 through August 2011



**The manufacturing sector has been expanding and adding jobs.
The question is whether this will continue.**

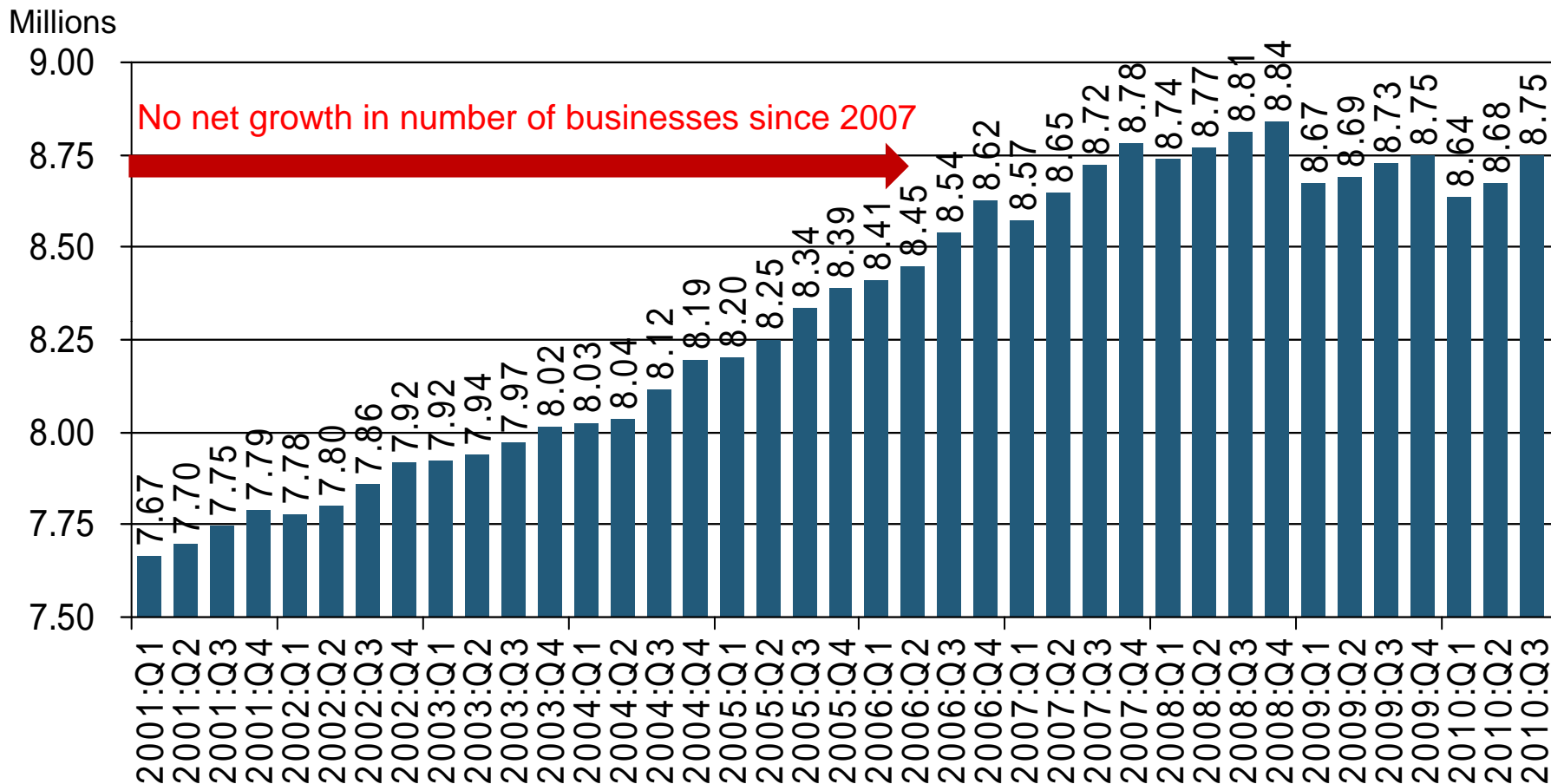
Consumer Sentiment Survey (1966 = 100)

January 2010 through August 2011



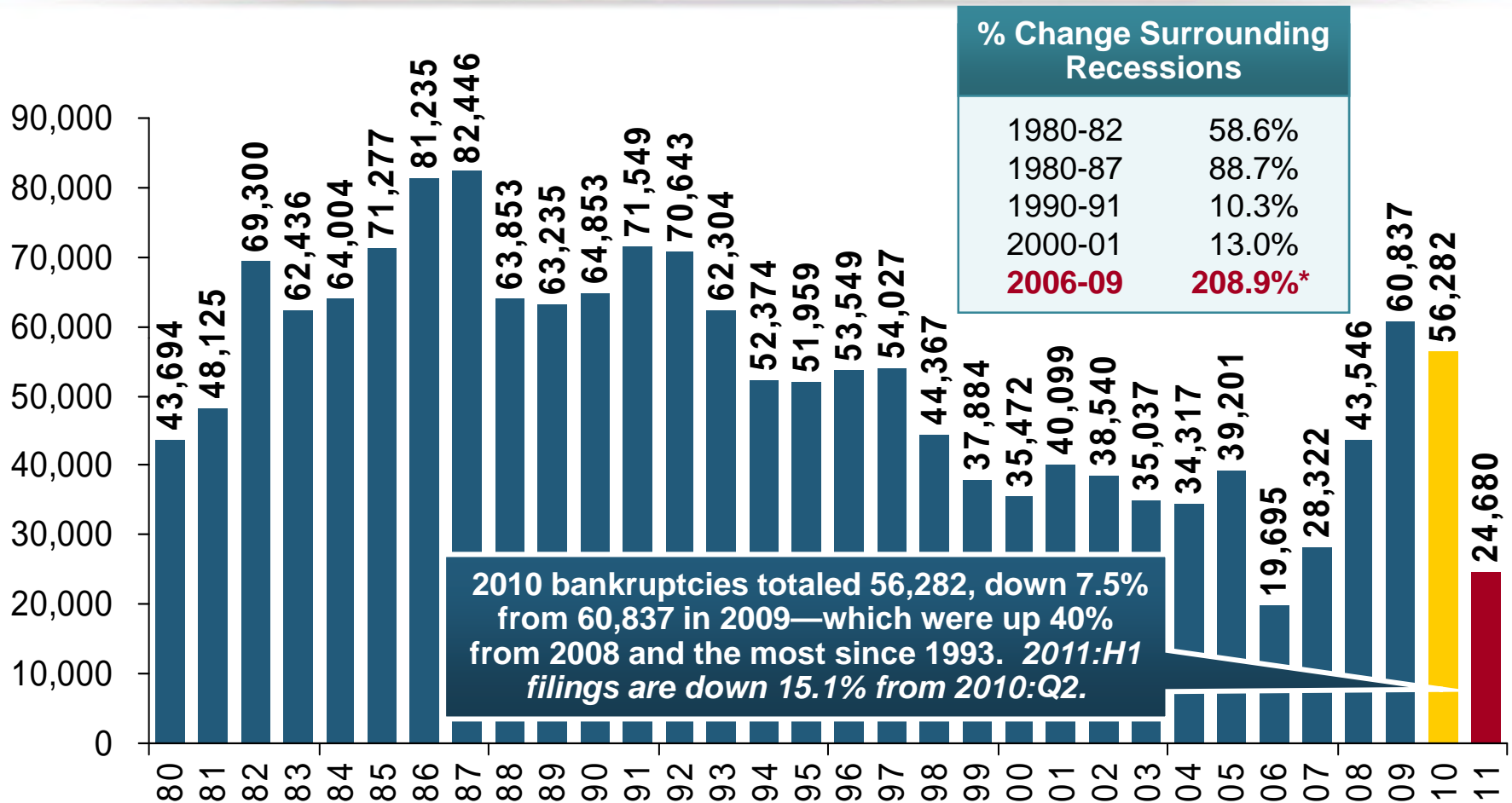
Consumer confidence has been low for years amid high unemployment, falling home prices and other factors adversely impact consumers.

Number of Private Business Establishments, 2001:Q1-2010:Q3



**In 2009:Q1 a net of 165,000 businesses disappeared.
By 2010:Q3 73,000 new ones appeared,
returning us to the level first attained three years before, in 2007:Q3.**

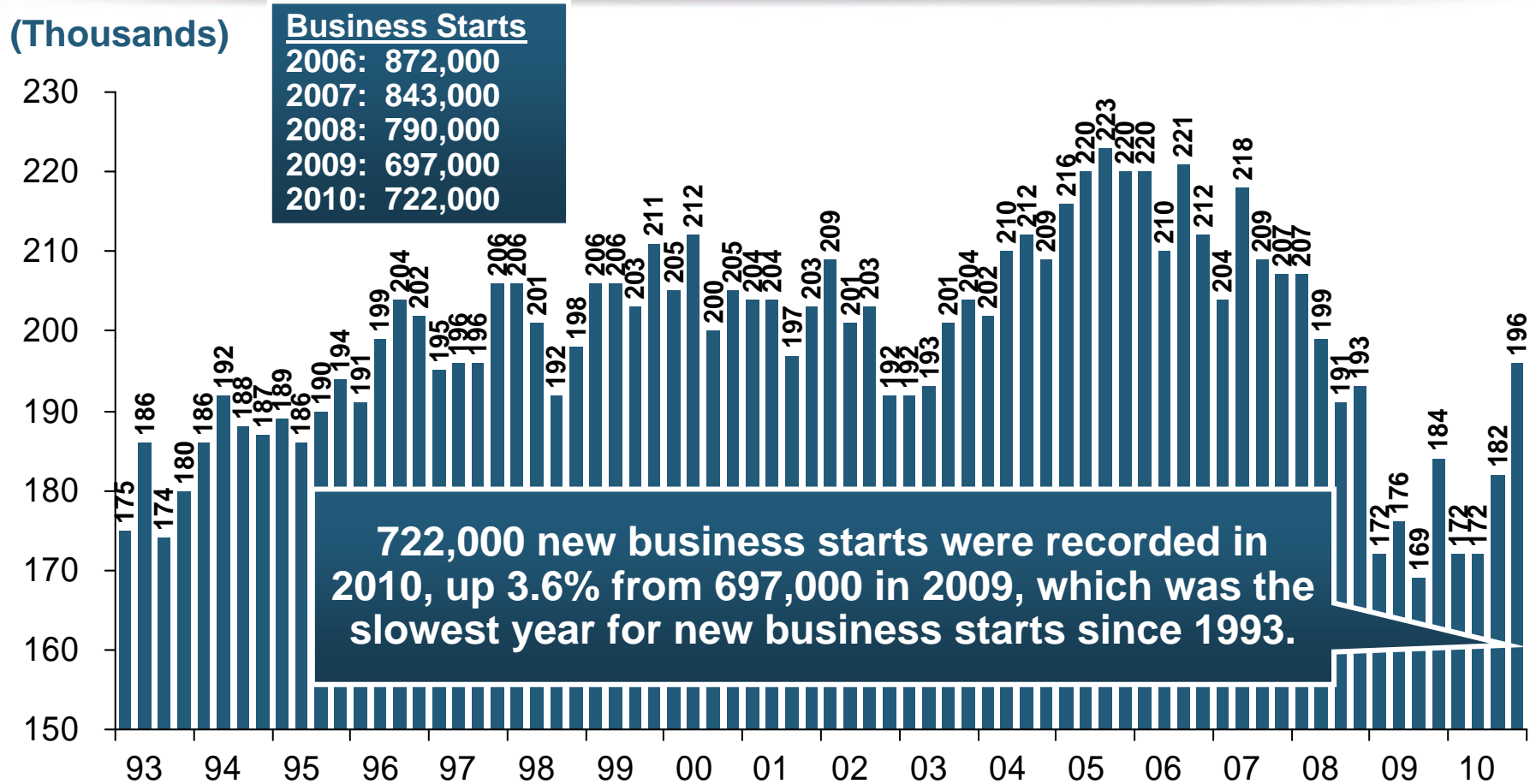
Business Bankruptcy Filings, 1980-2011:H1



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 – 2010:Q4*



Business Starts Were Down Nearly 20% in the Recession, Holding Back Most Types of Commercial Insurance Exposure

* Data through December 31, 2010 are the latest available as of September 8, 2011; Seasonally adjusted
 Source: Bureau of Labor Statistics, <http://www.bls.gov/news.release/cewbd.t08.htm>.

11 Industries for the Next 10 Years: Insurance Solutions Needed

Health Care

Health Sciences

Energy (Traditional)

Alternative Energy

Agriculture

Natural Resources

Environmental

Technology (incl. Biotechnology)

Light Manufacturing

Export-Oriented Industries

Shipping (Rail, Marine, Trucking)



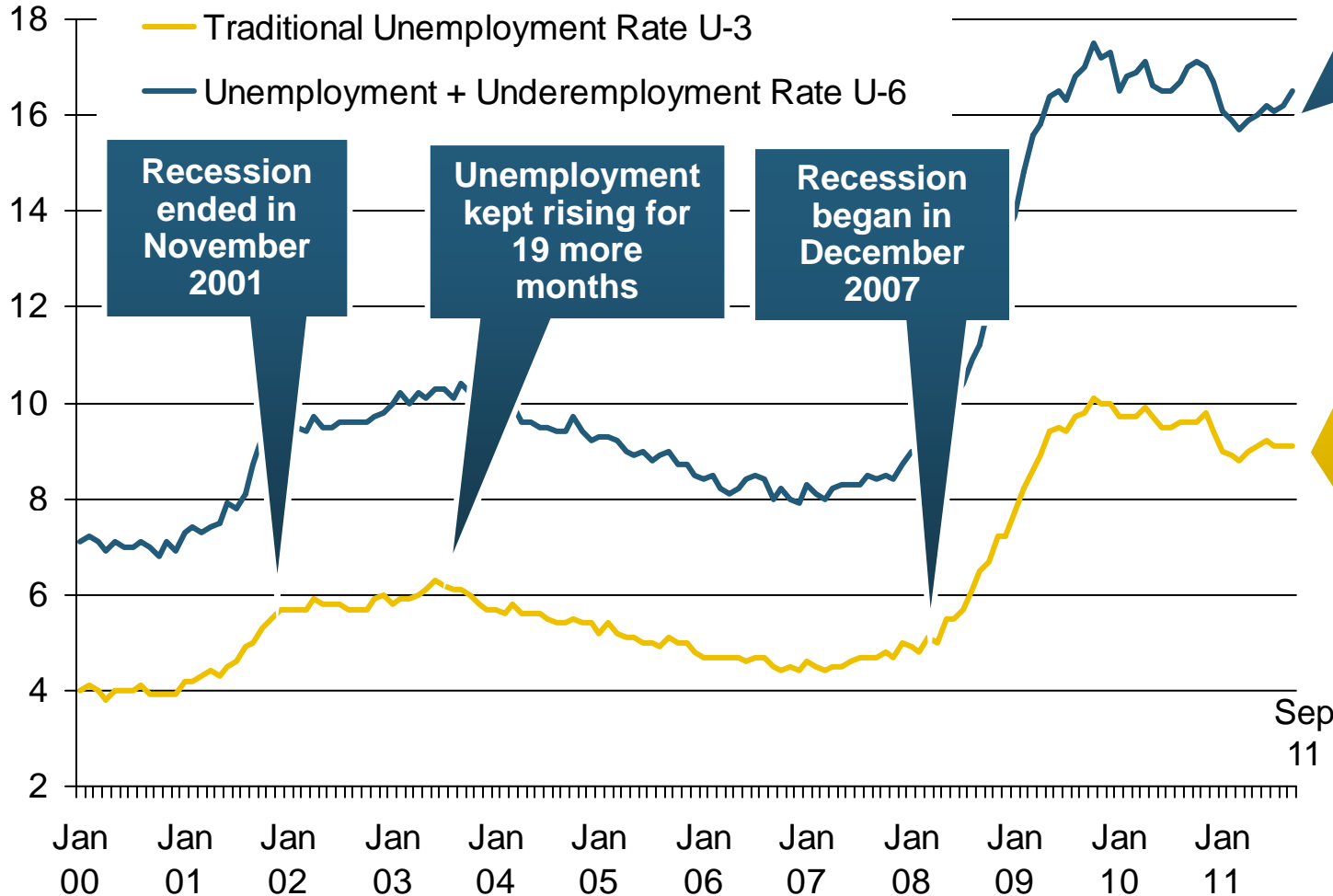
Many industries are poised for growth, but many insurers do not write in these economic segments

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 2011

January 2000 through September 2011, Seasonally Adjusted (%)



U-6 went from 8.0% in March 2007 to 17.5% in October 2009; Stood at 16.5% in Sept. 2011

Unemployment stood at 9.1% in September

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

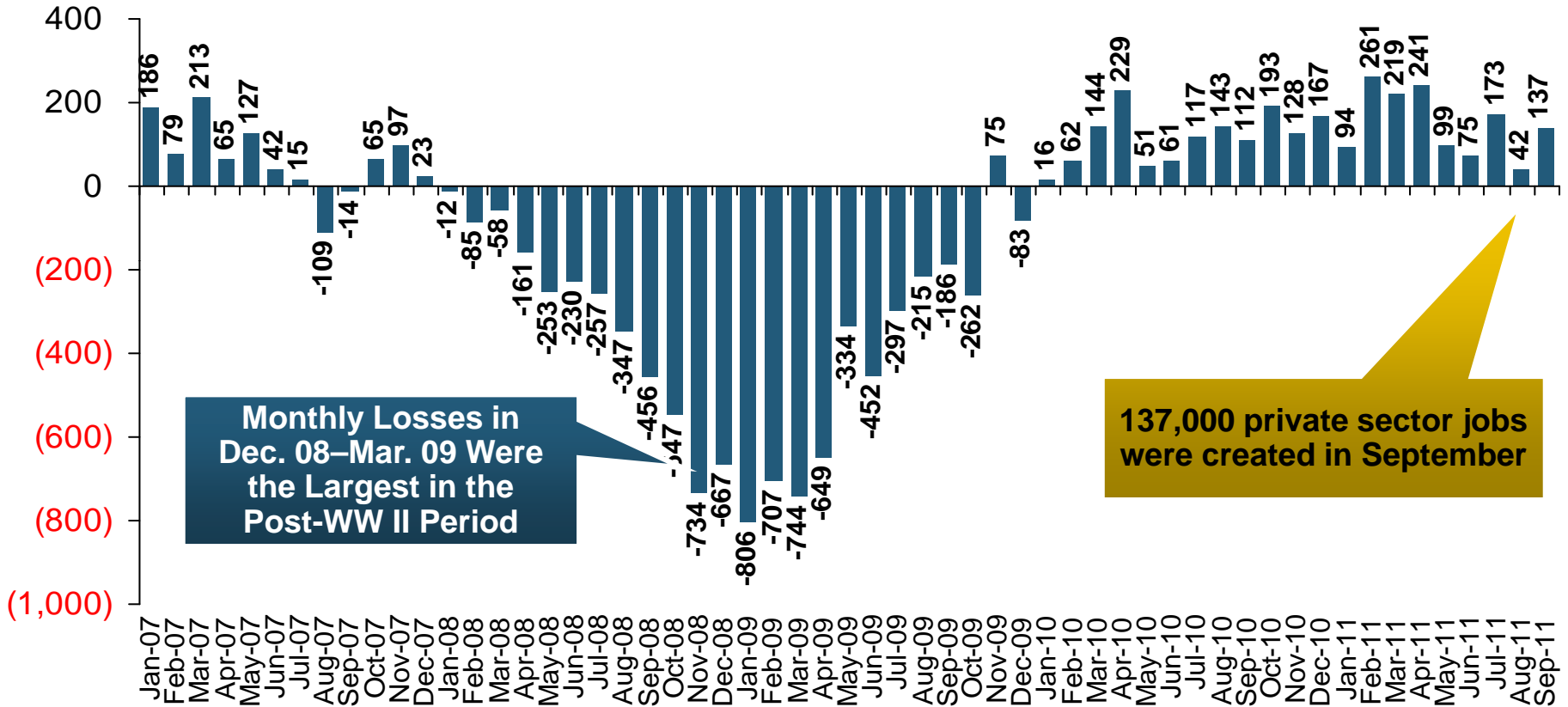
Peak rate in the last 30 years: 10.8% in November - December 1982

Stubbornly high unemployment and underemployment will constrain overall economic growth

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

Monthly Change in Private Employment

January 2008 through September 2011* (Thousands)



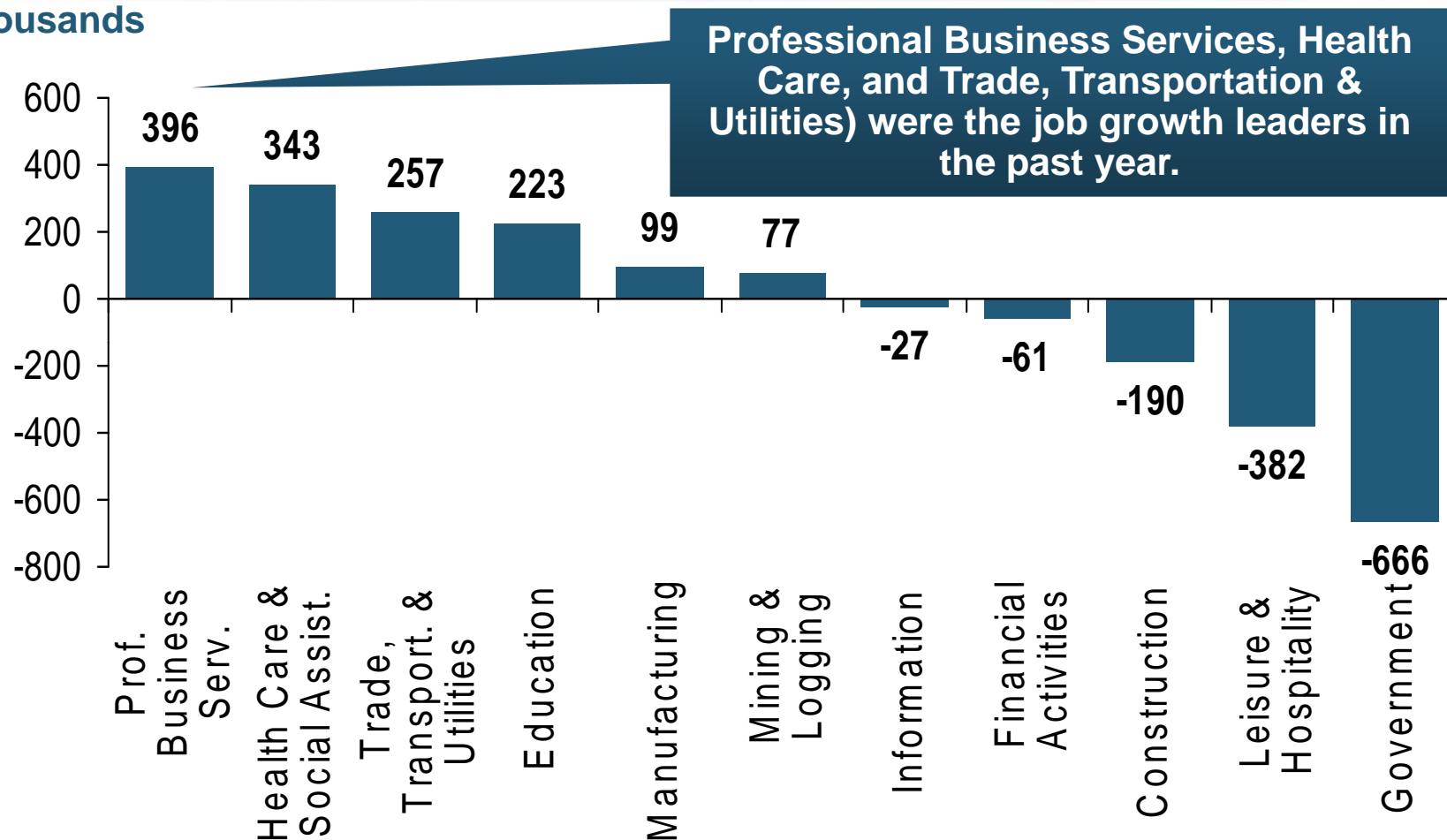
Monthly Losses in Dec. 08–Mar. 09 Were the Largest in the Post-WW II Period

137,000 private sector jobs were created in September

Private Employers Added 2.764 million Jobs Since Jan. 2010 After Having Shed 4.66 Million Jobs in 2009 and 3.81 Million in 2008 (State and Local Governments Have Shed Hundreds of Thousands of Jobs)

Change in Number Employed in Select Industries, June 2011 vs. June 2010

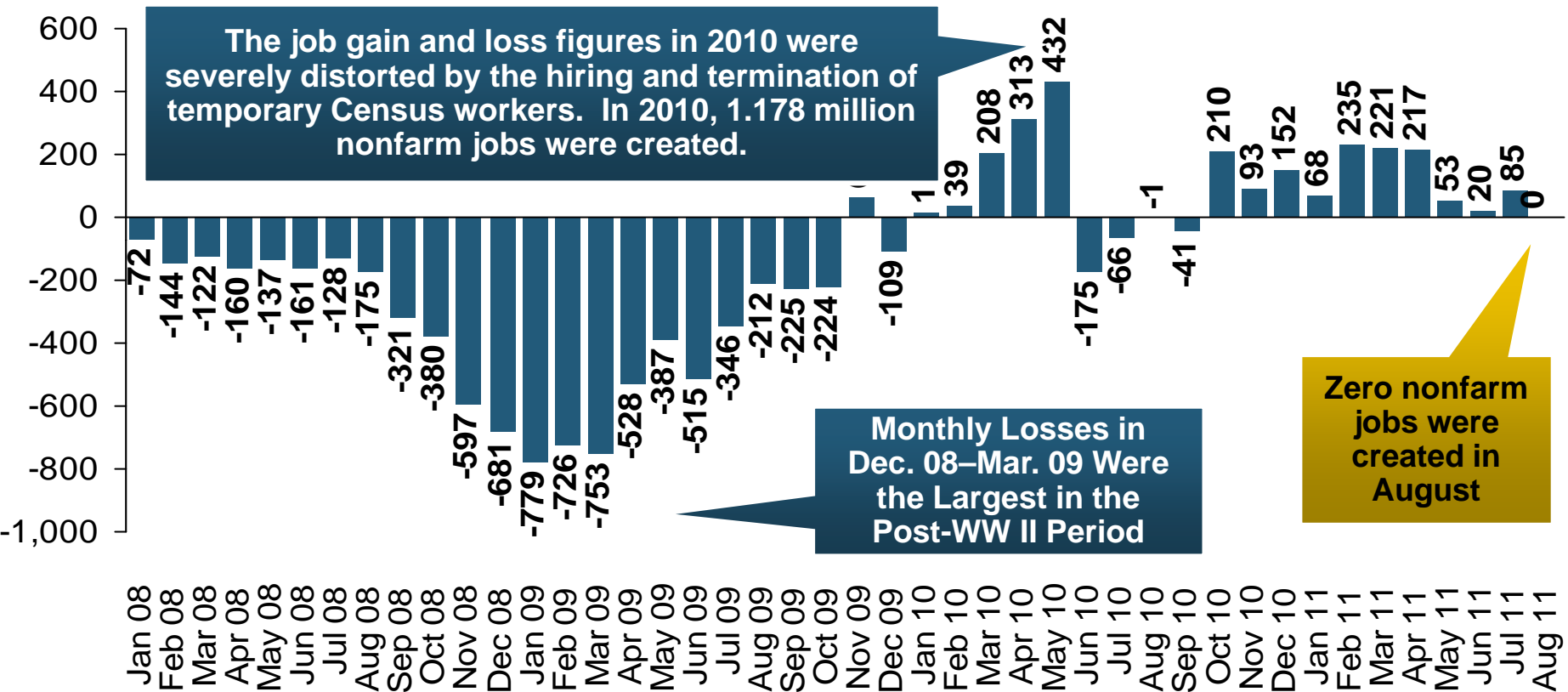
Thousands



There is a great deal of variation in employment growth by industry, indicating a very uneven and slow recovery

Monthly Change Employment*

January 2008 through August 2011* (Thousands)

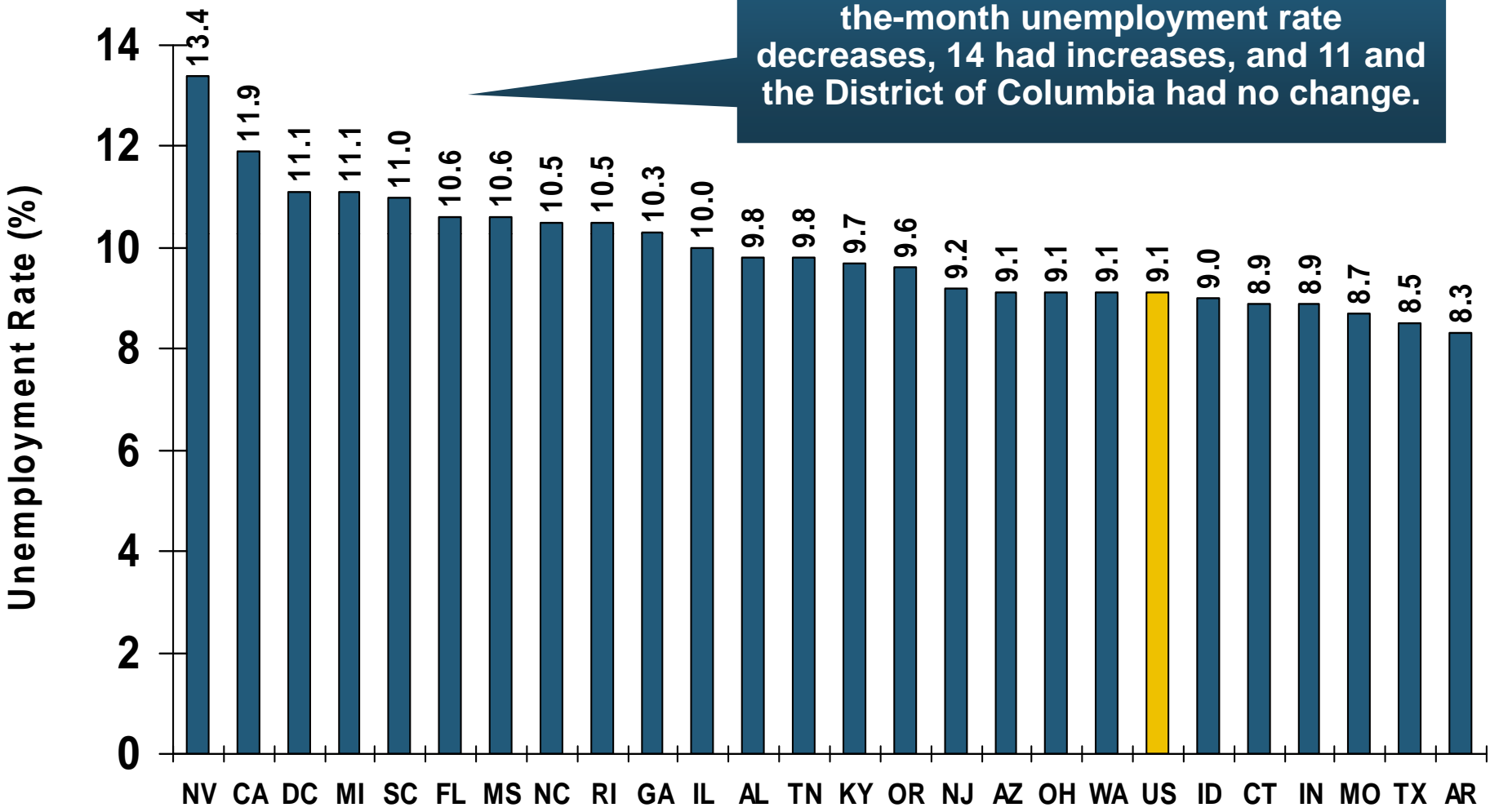


Job Losses Since the Recession Began in Dec. 2007 Peaked at 8.4 Mill in Dec. 09; 14.0 Million People are Now Defined as Unemployed

Unemployment Rates by State, September 2011: Highest 25 States*



In September, 25 states reported over-the-month unemployment rate decreases, 14 had increases, and 11 and the District of Columbia had no change.



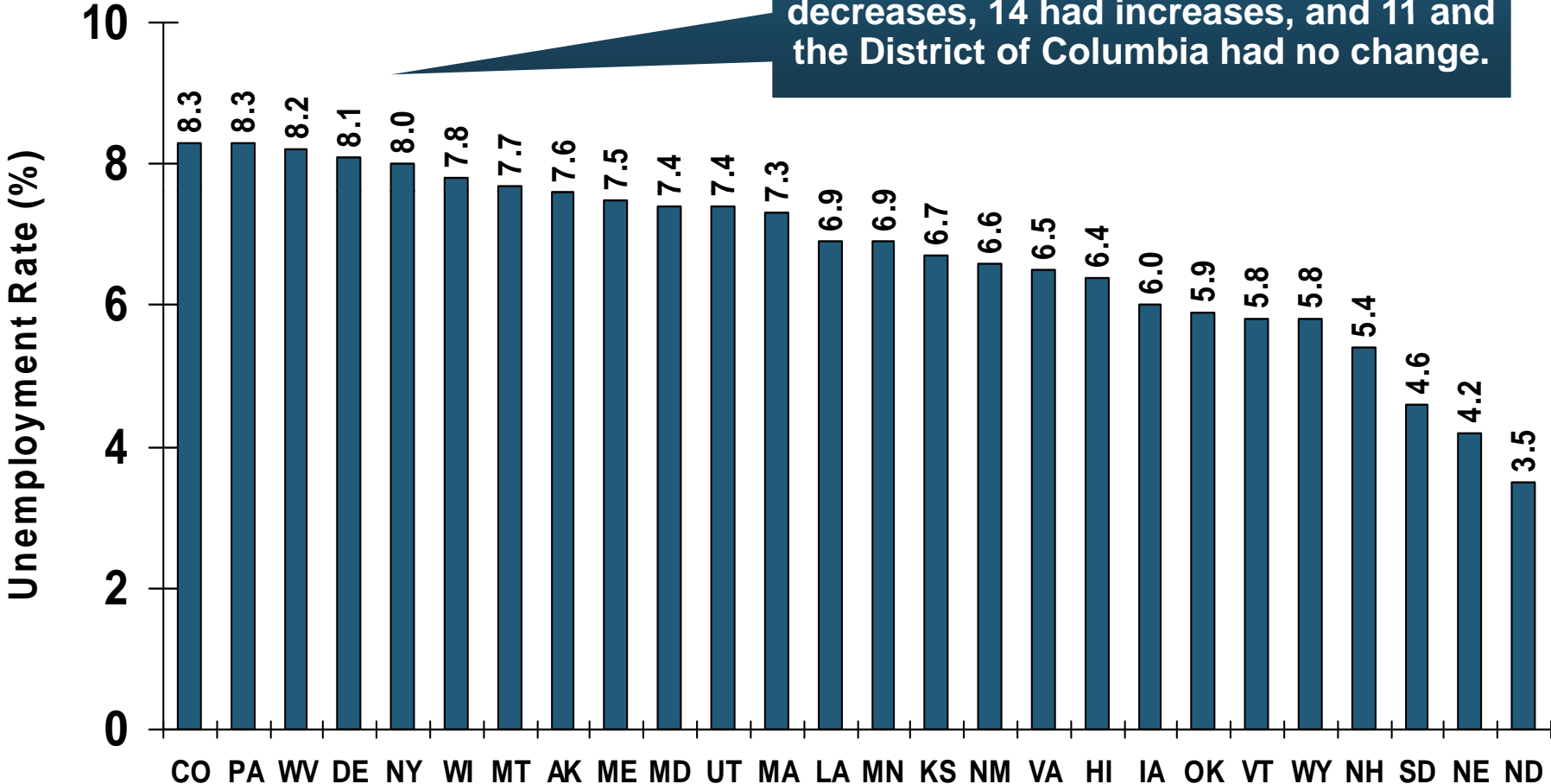
*Provisional figures for September 2011, seasonally adjusted.

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

Unemployment Rates By State, September 2011: Lowest 25 States*

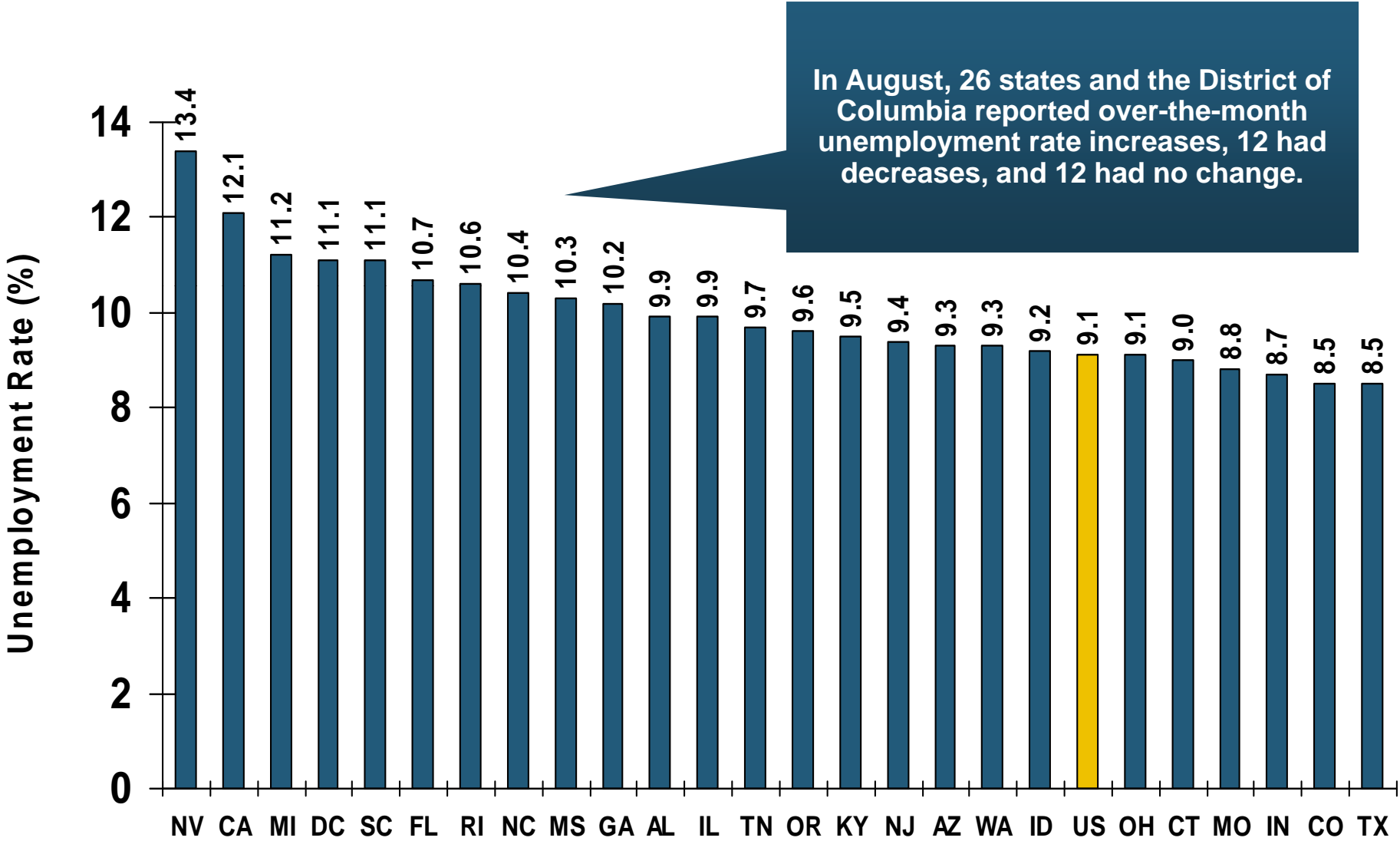


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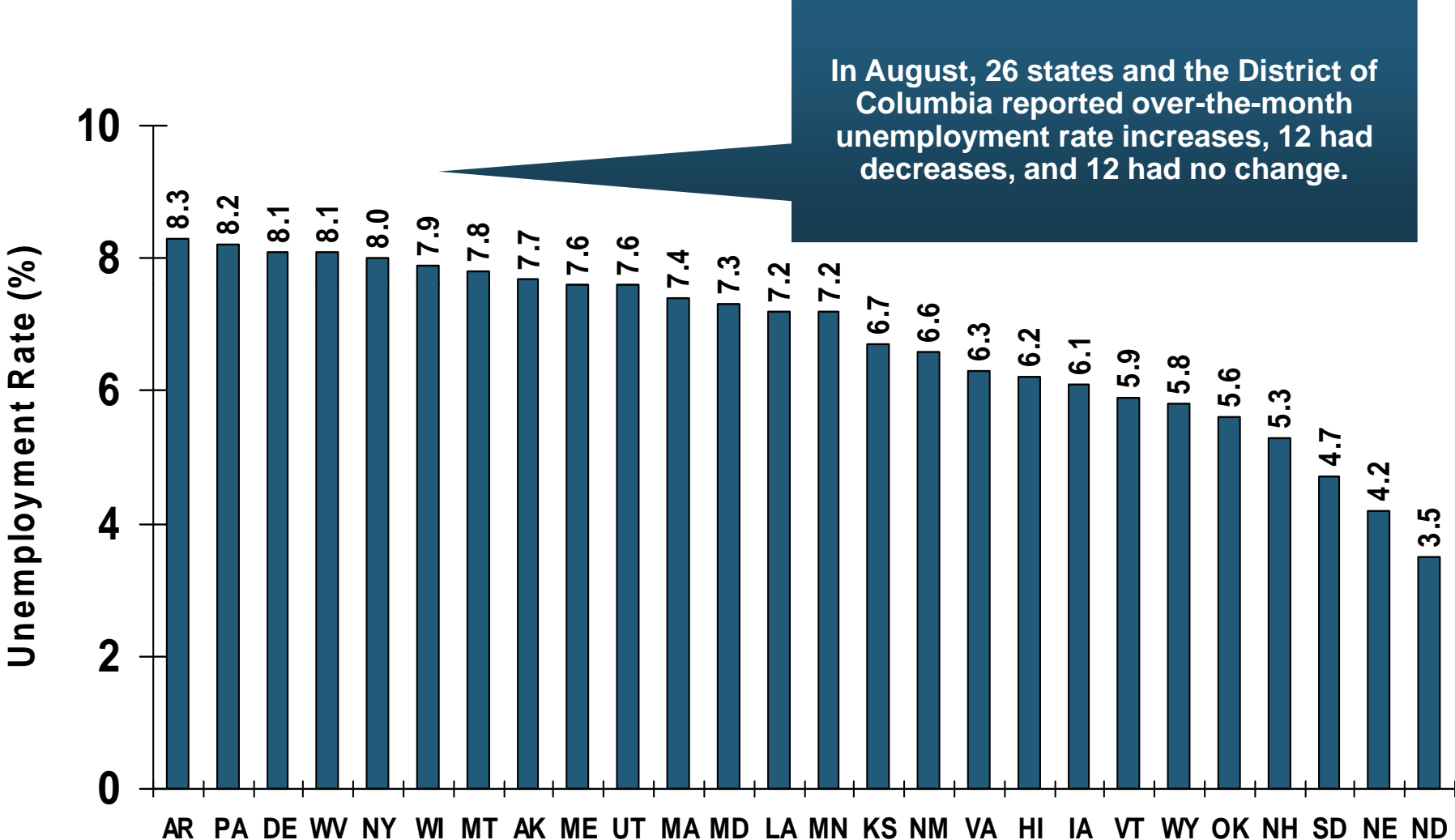
Unemployment Rates by State, August 2011: Highest 25 States*



*Provisional figures for August 2011, seasonally adjusted.

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

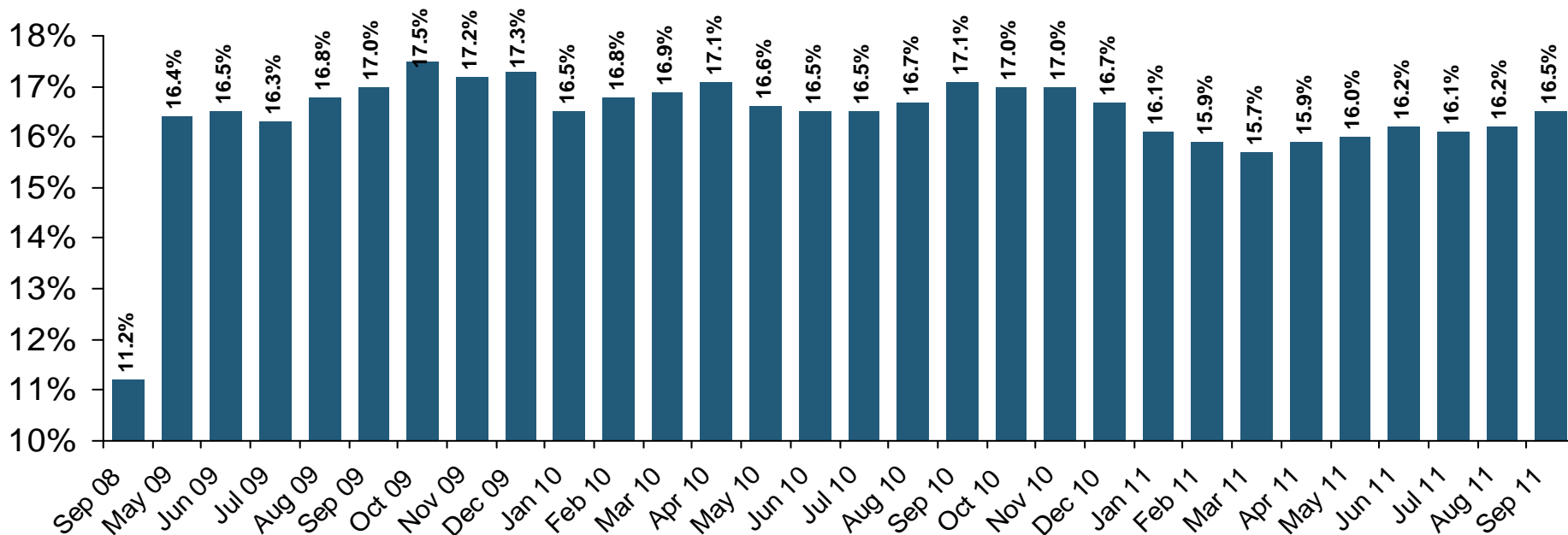
Unemployment Rates By State, August 2011: Lowest 25 States*



*Provisional figures for August 2011, seasonally adjusted.
Sources: US Bureau of Labor Statistics; Insurance Information Institute.

Labor Underutilization: Broader than Just Unemployment

% of Labor Force



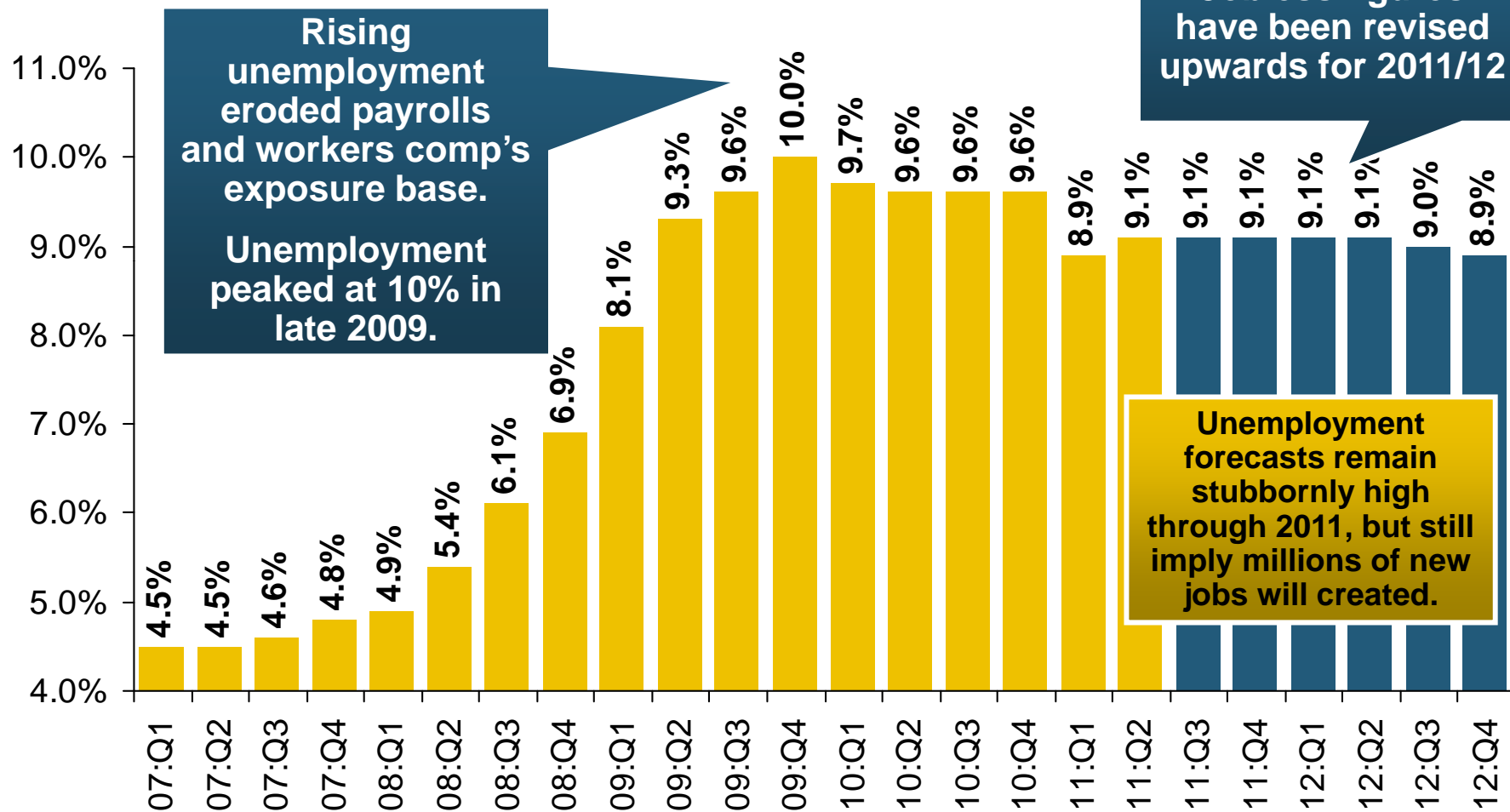
Marginally Attached and Unemployed Persons Account for 16.5% of the Labor Force in September 2011 (1 Out Every 6 People). Unemployment Rate Alone was 9.1%. Underutilization Shows a Broader Impact on WC and Other Commercial Exposures

NOTE: Marginally attached workers are persons who currently are neither working nor looking for work but indicate that they want and are available for a job and have looked for work sometime in the recent past. Discouraged workers, a subset of the marginally attached, have given a job-market related reason for not looking currently for a job. Persons employed part time for economic reasons are those who want and are available for full-time work but have had to settle for a part-time schedule.

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

US Unemployment Rate

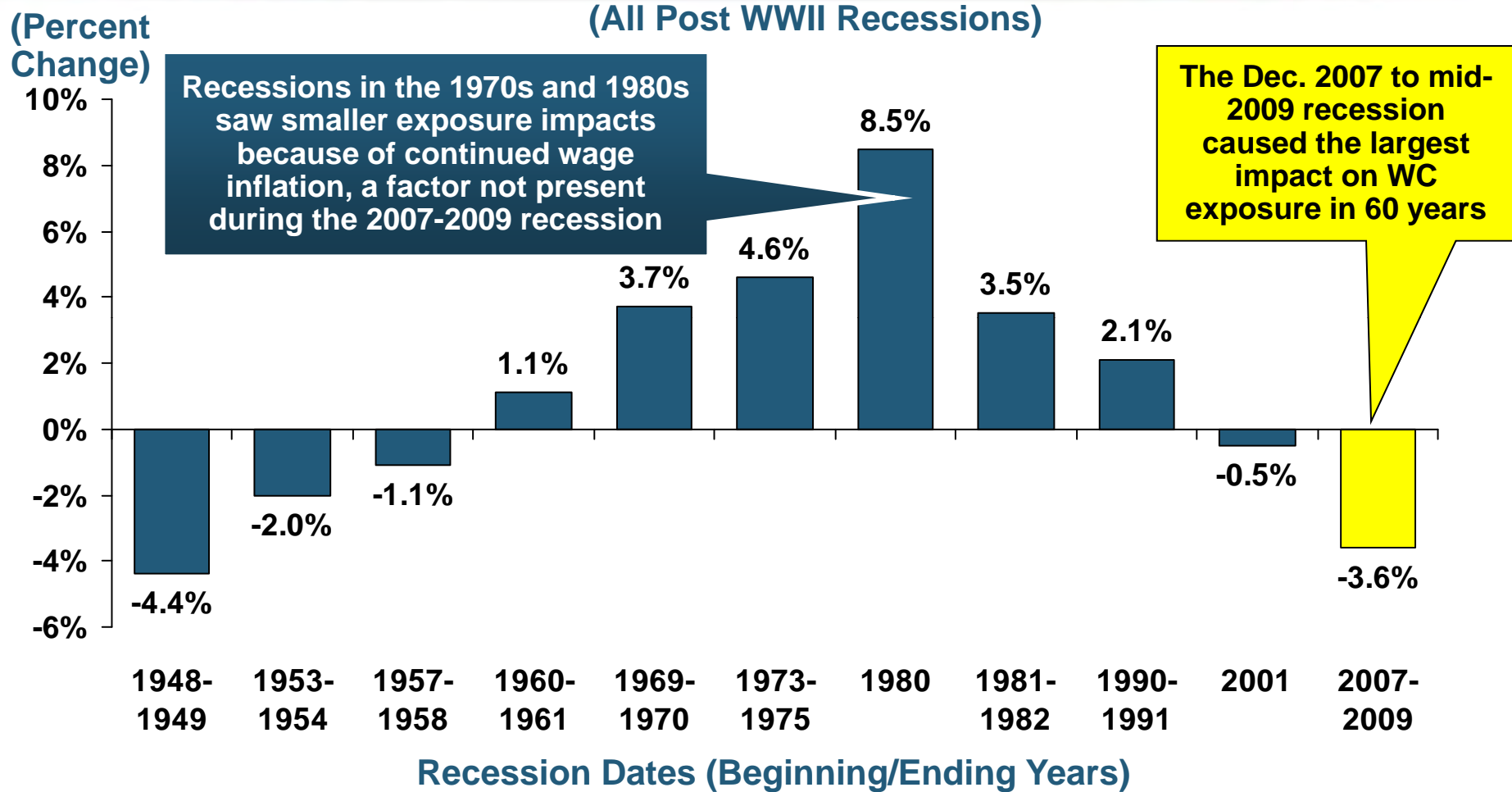
2007:Q1 to 2012:Q4F*



*  = actual;  = forecasts

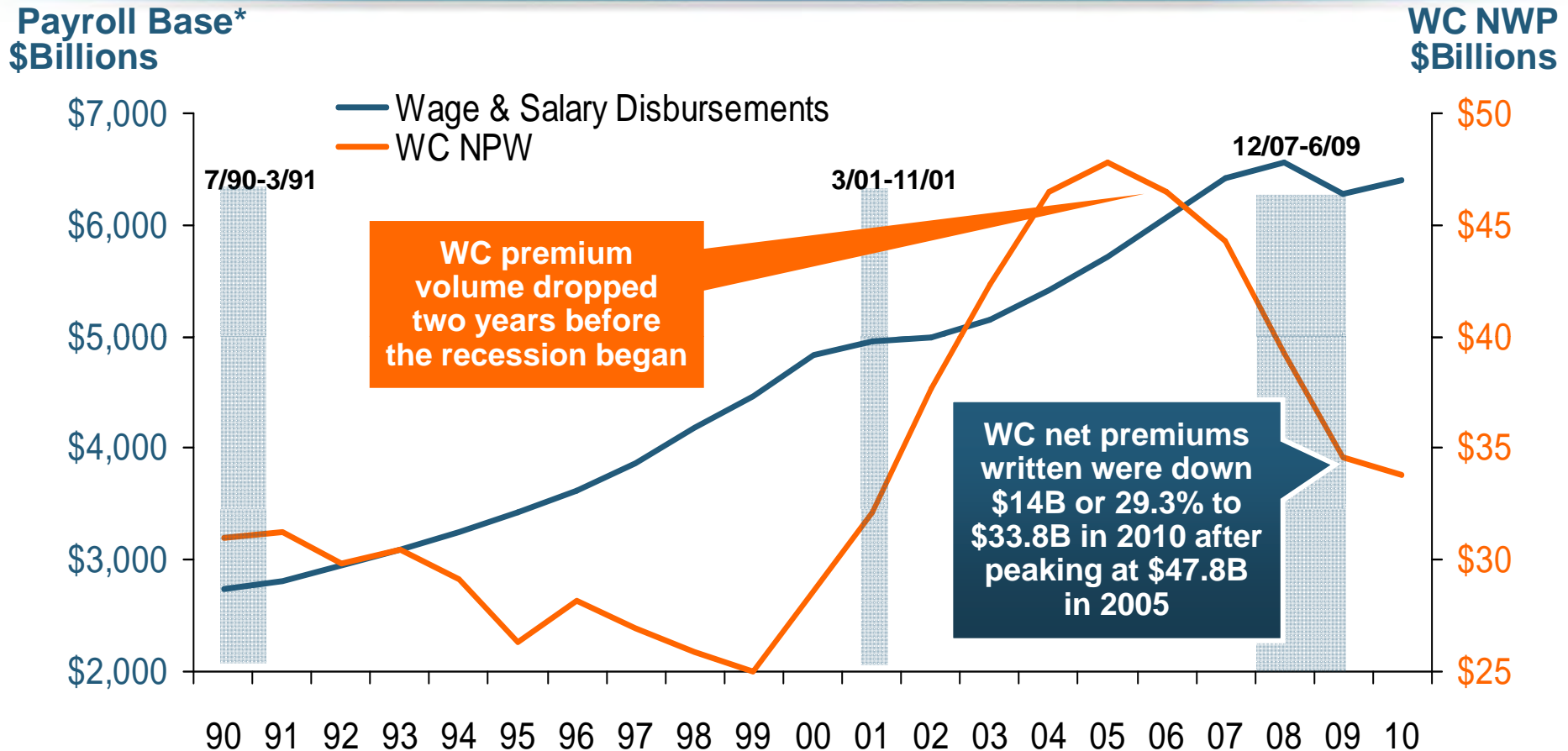
Sources: US Bureau of Labor Statistics; Blue Chip Economic Indicators (10/11); Insurance Information Institute

Estimated Effect of Recessions* on Payroll (Workers Comp Exposure)



*Data represent maximum recorded decline over 12-month period using annualized quarterly wage and salary accrual data
 Source: Insurance Information Institute research; Federal Reserve Bank of St. Louis (wage and salary data); National Bureau of Economic Research (recession dates).

Wage and Salary Disbursements (Payroll Base) vs. Workers Comp Net Written Premiums



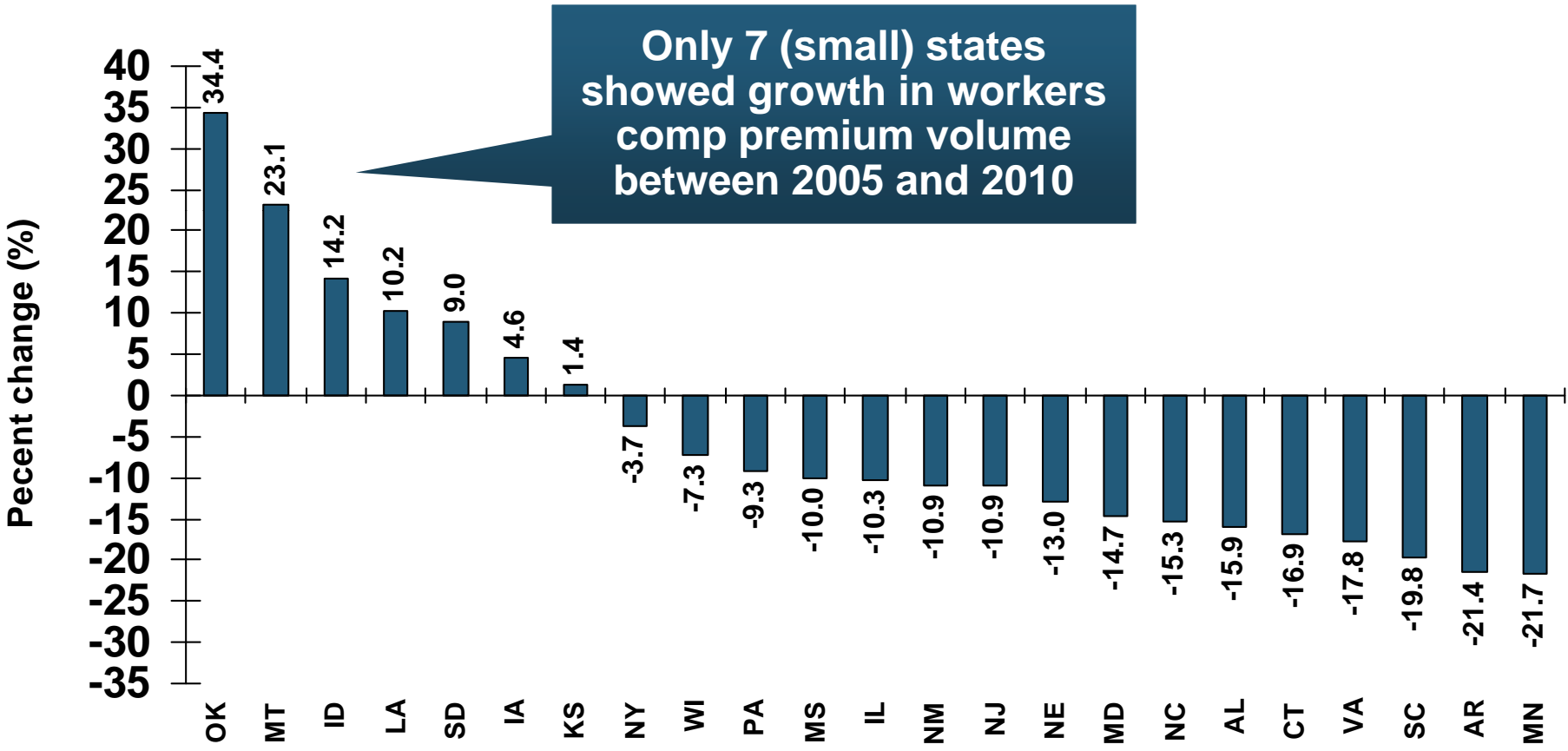
29% of NPW has been eroded away by the soft market and weak economy

*Private employment; 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.

Direct Premiums Written: Worker's Comp Percent Change by State, 2005-2010*

Top 25 States

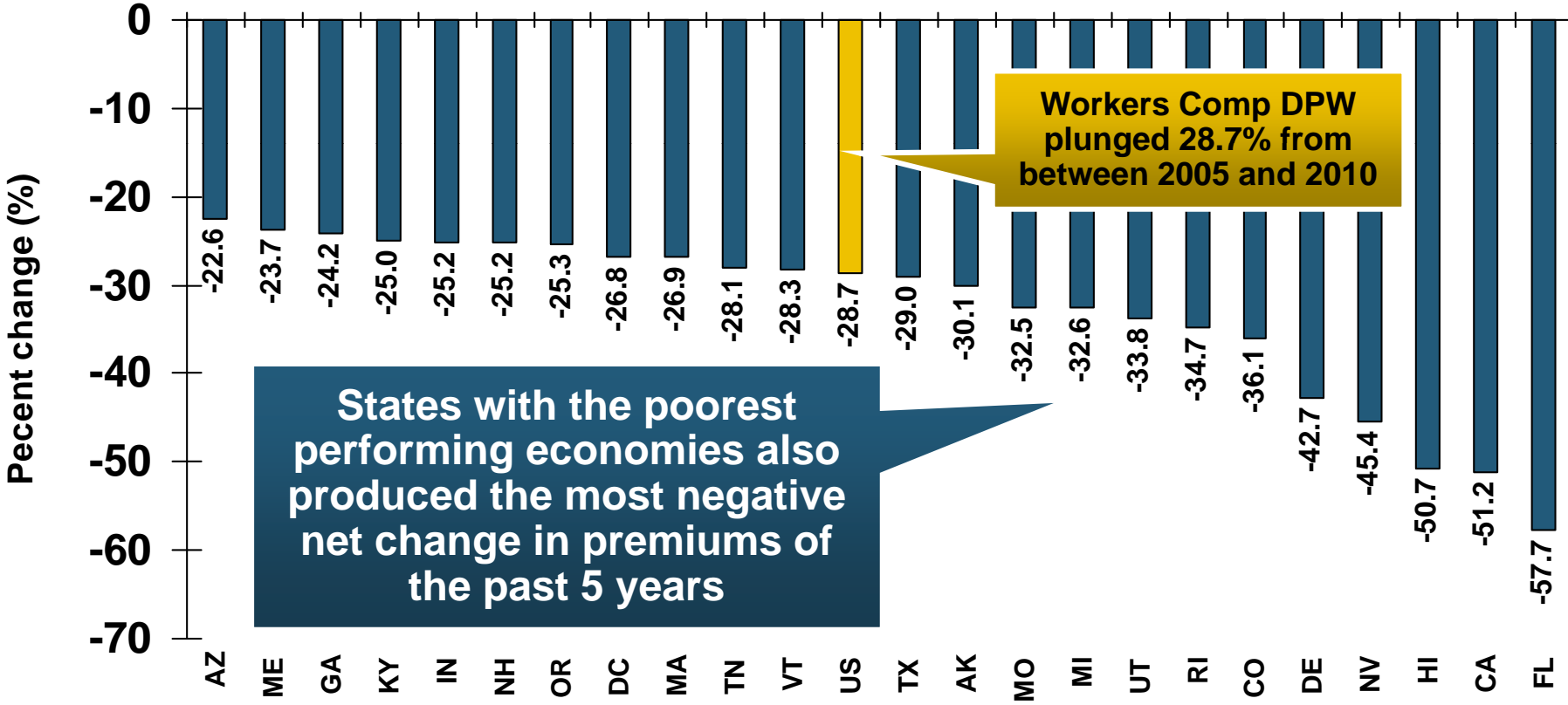


*Excludes monopolistic fund states: ND, OH, WA, WY as well as WV, which transitioned to a competitive structure during this period.

Sources: SNL Financial LC.; Insurance Information Institute.

Direct Premiums Written: Worker's Comp Percent Change by State, 2005-2010*

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.

Insurance Information Institute Online:

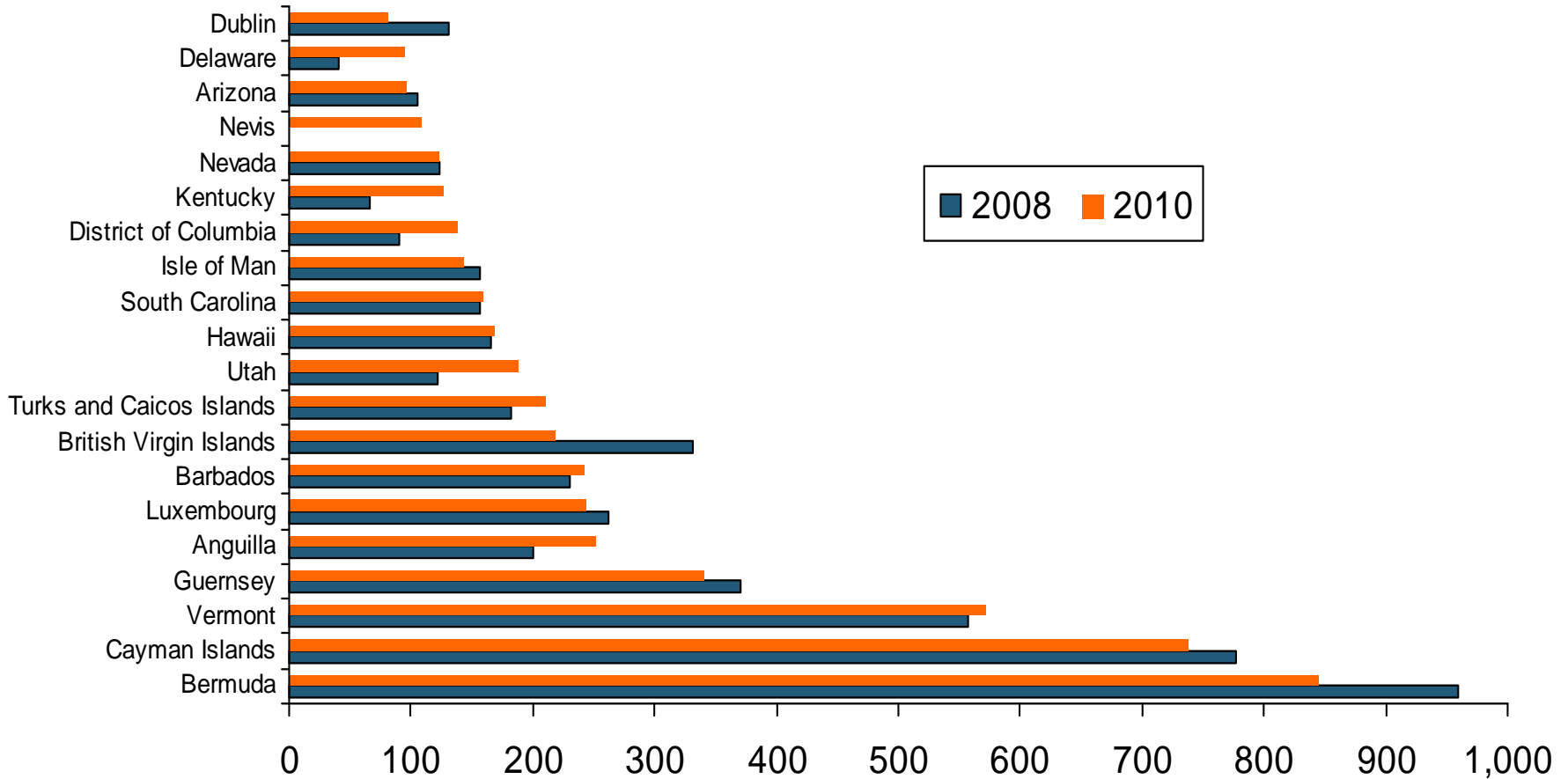
www.iii.org

*Thank you for your time
and your attention!*

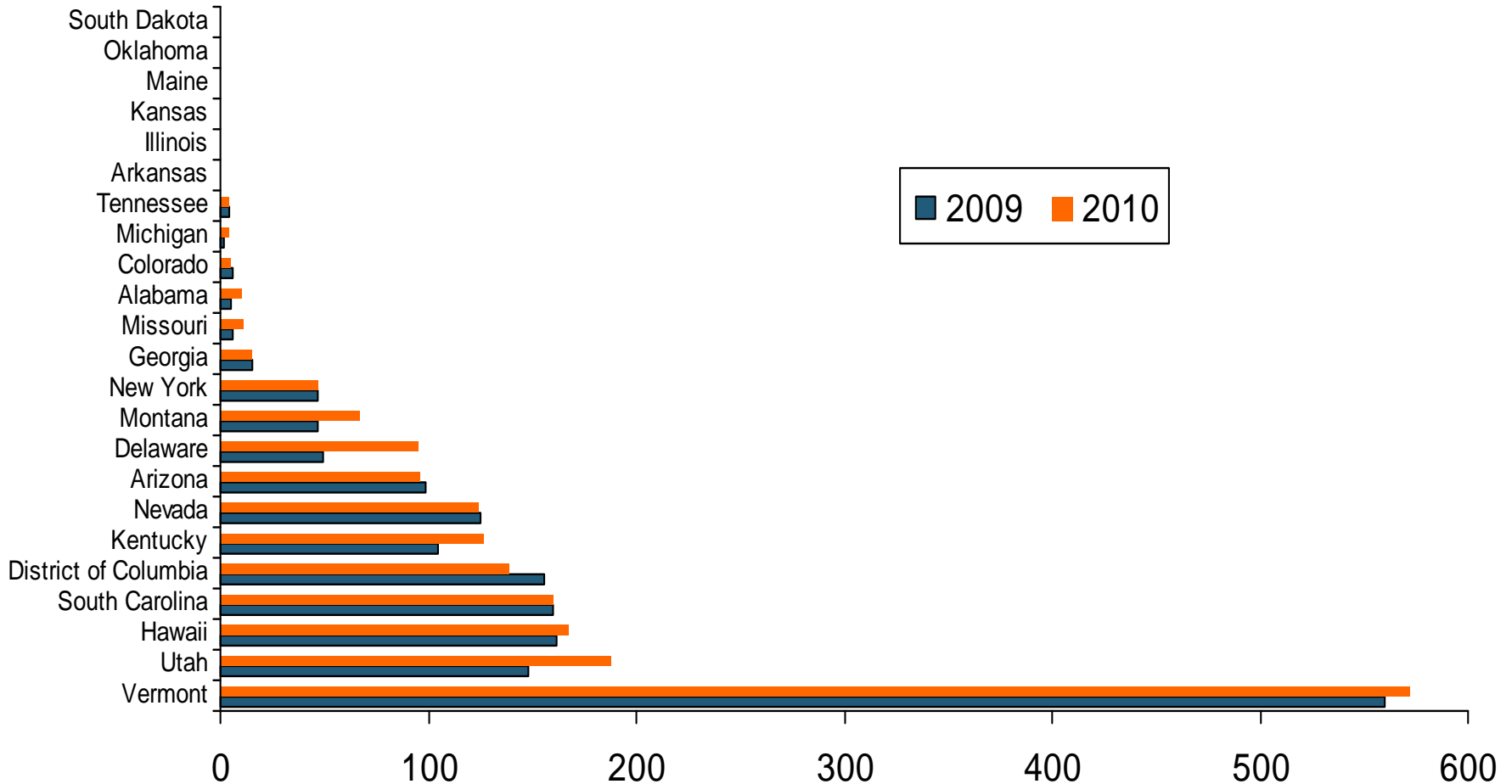
Twitter: twitter.com/bob_hartwig

Download at www.iii.org/presentations

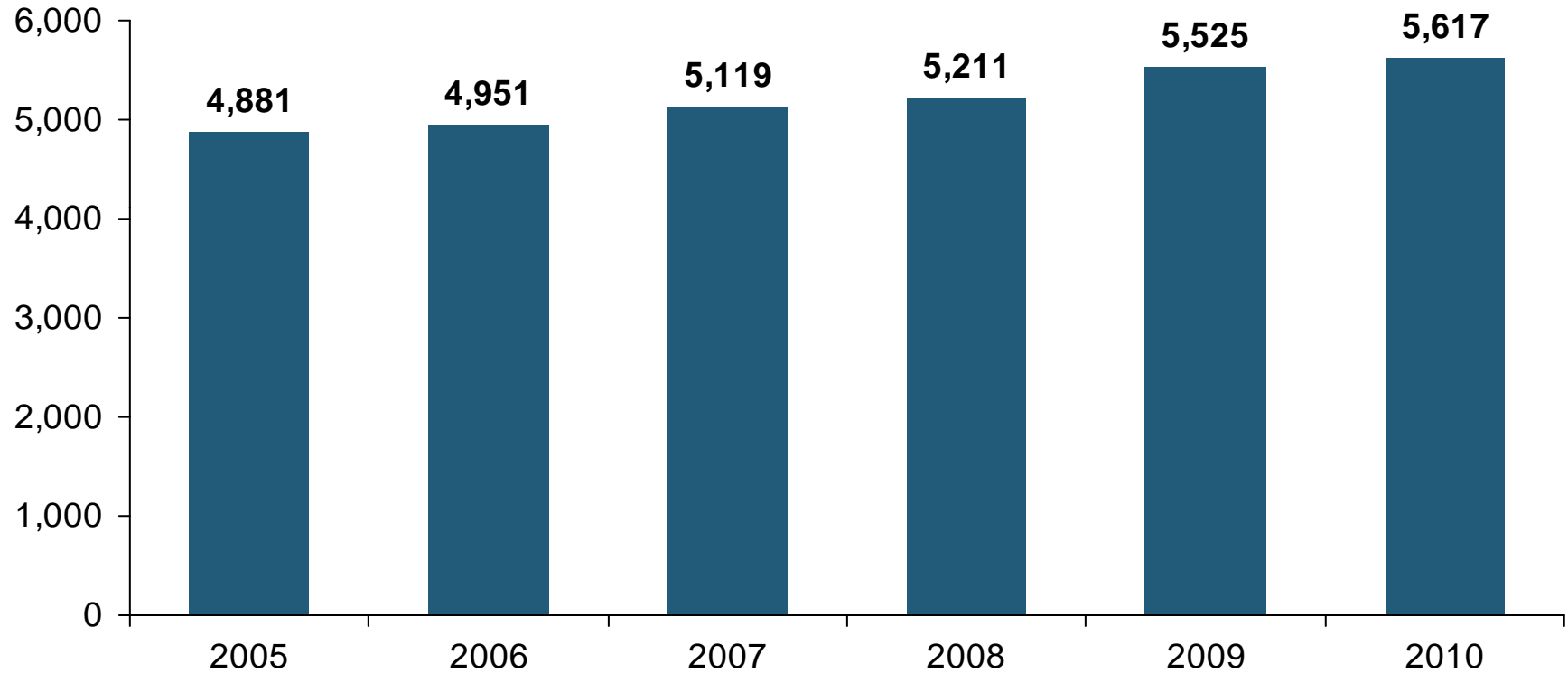
Leading Captive Domiciles, 2008-2010



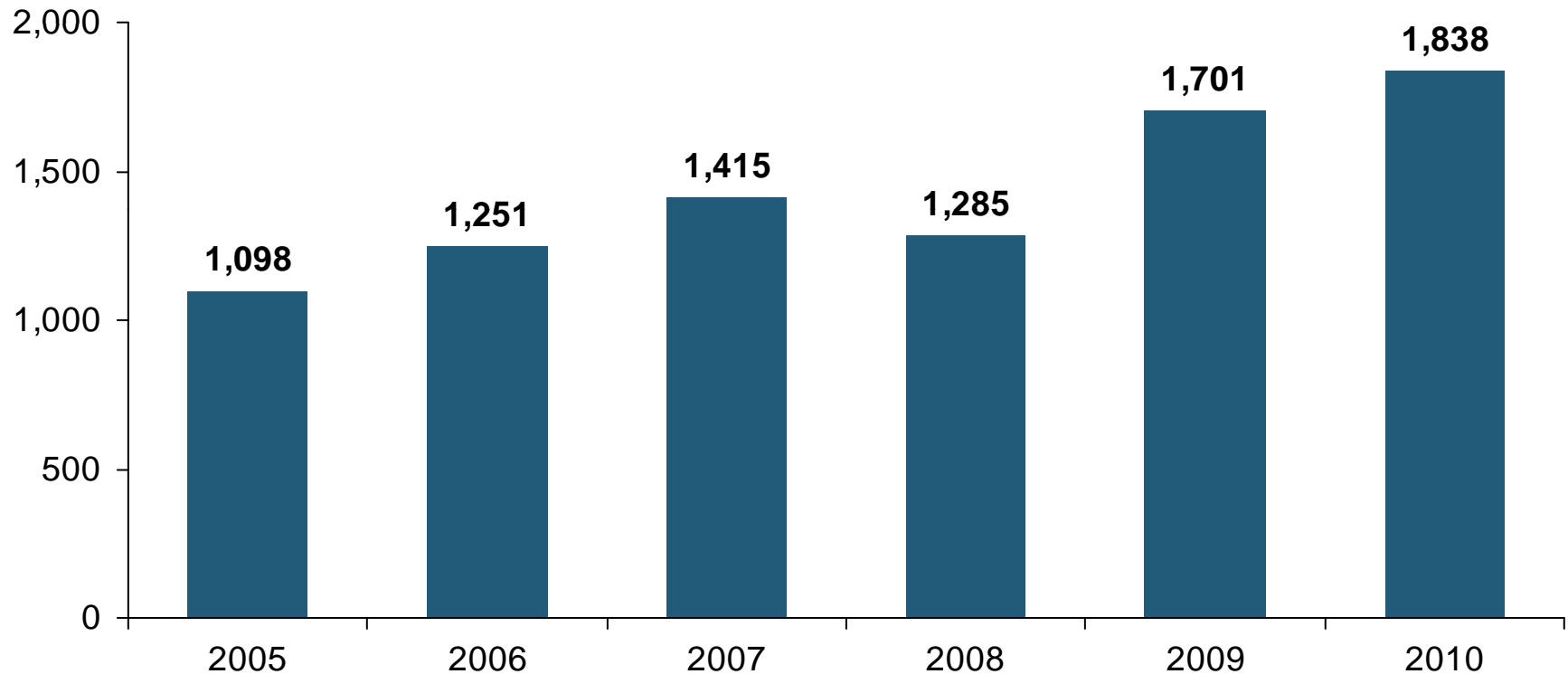
Captives by State, 2009-2010



World Captive Growth, 2005-2010



State Captive Growth, 2005-2010



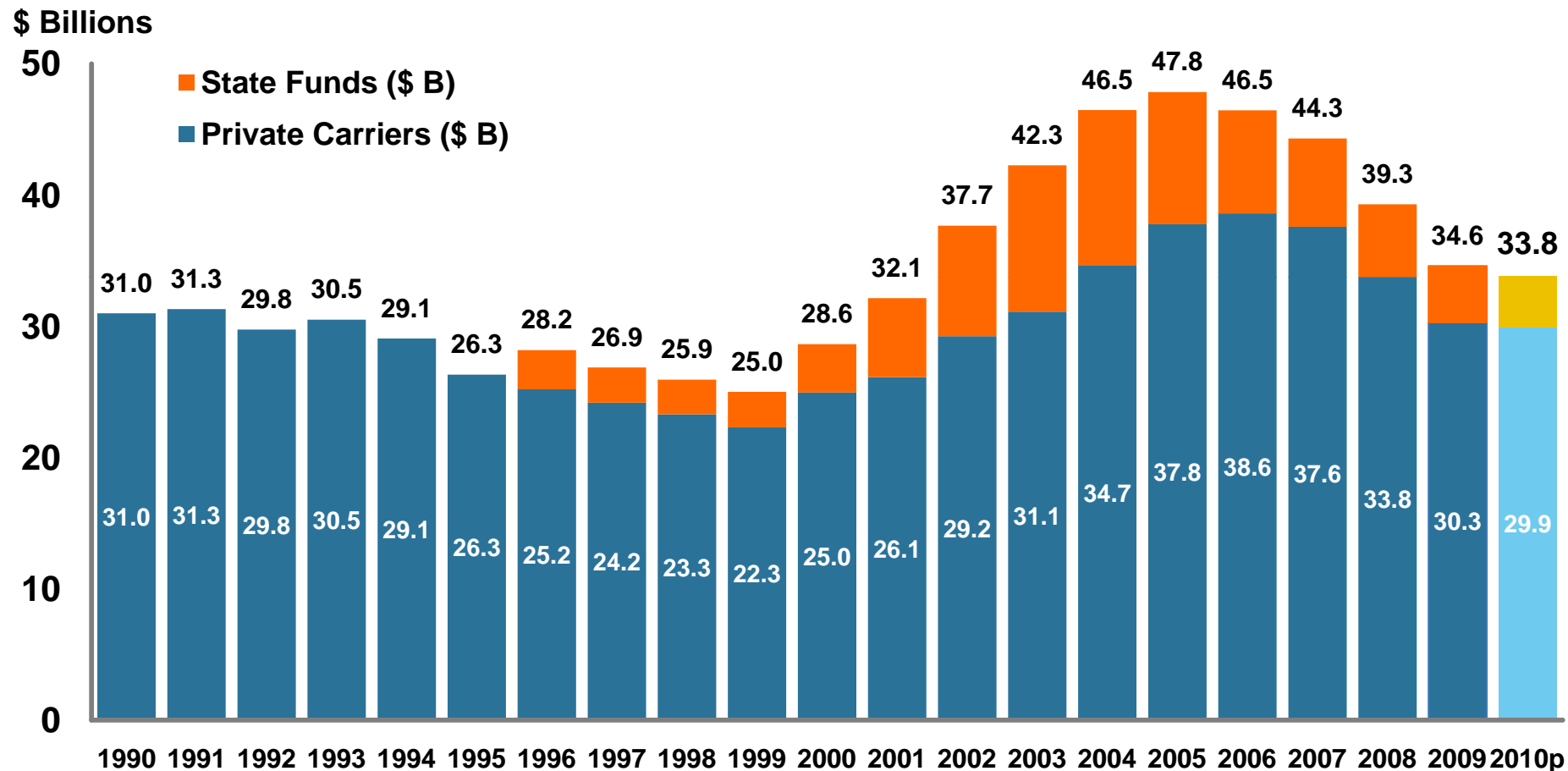


Workers Compensation Operating Environment

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

Workers Compensation Premium Continues Its Sharp Decline

Net Written Premium



p Preliminary

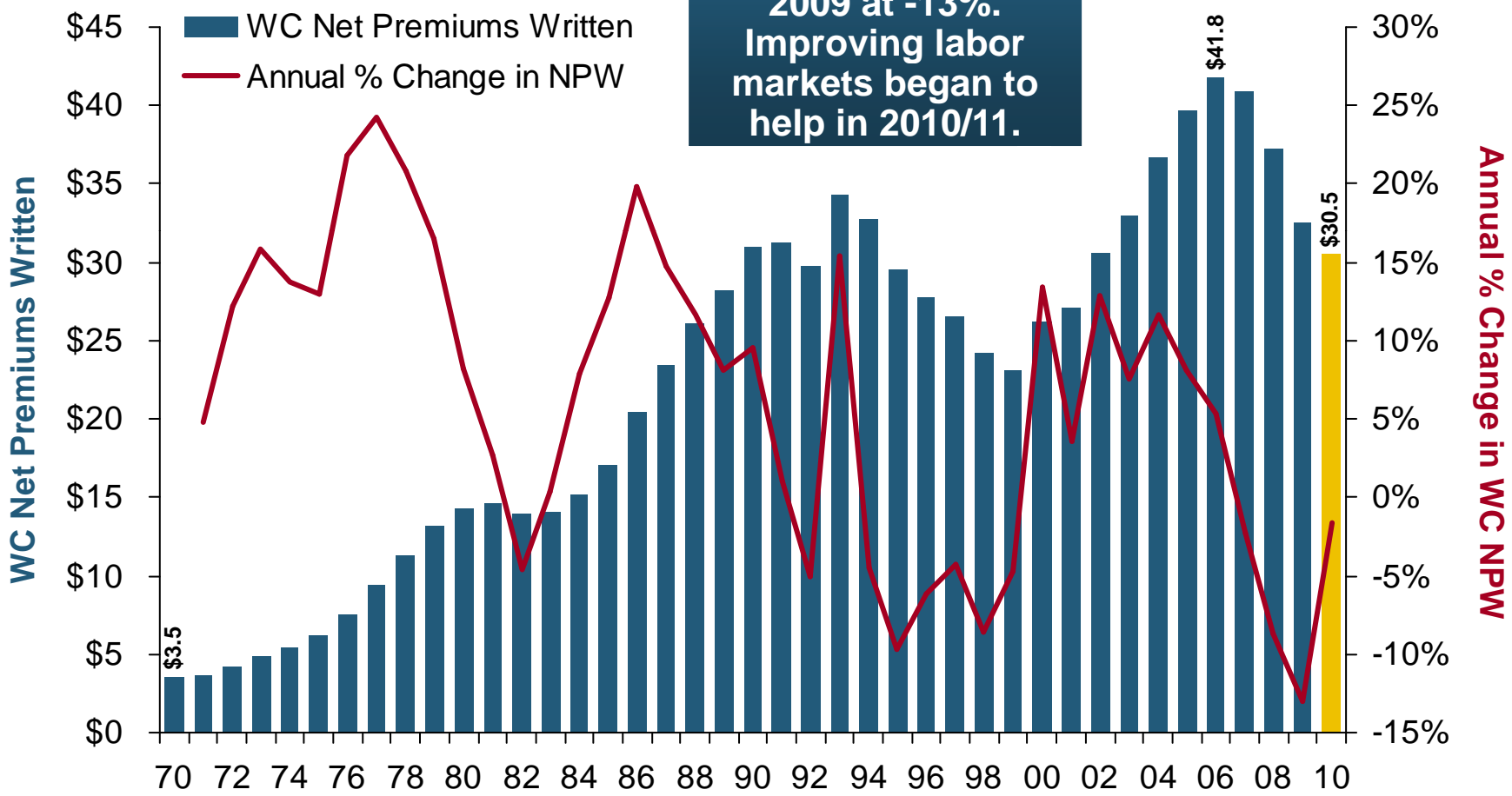
Source: 1990–2009 Private Carriers, *Best's Aggregates & Averages*; 2010p, NCCI

1996–2010p 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

Workers Compensation Net Premiums Written and Annual Growth Rates: 1970-2010P

(\$ Billions)

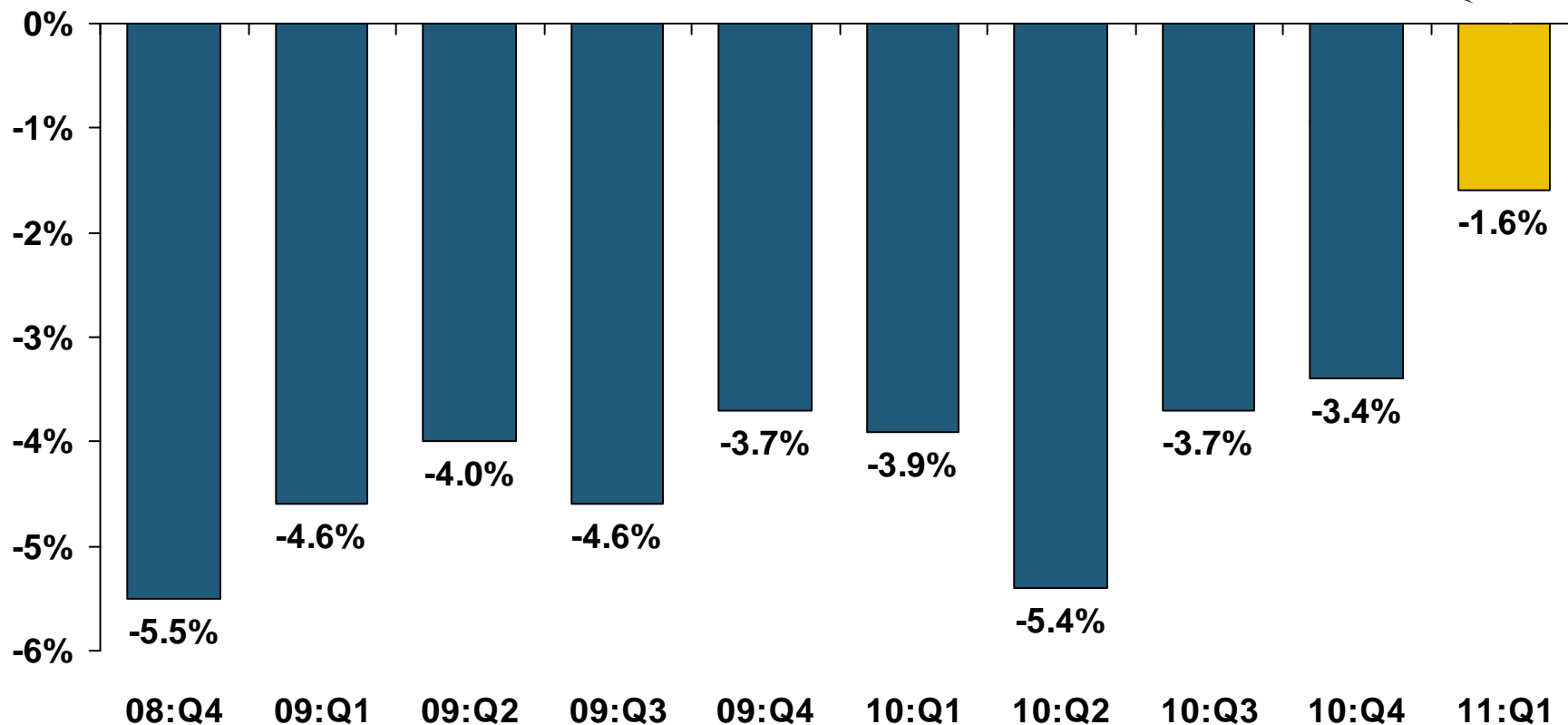


Sources: A.M. Best (1973-2009); Insurance Information Institute calculations and estimates for 2010.

Workers Comp Rate Changes, 2008:Q4 – 2011:Q1

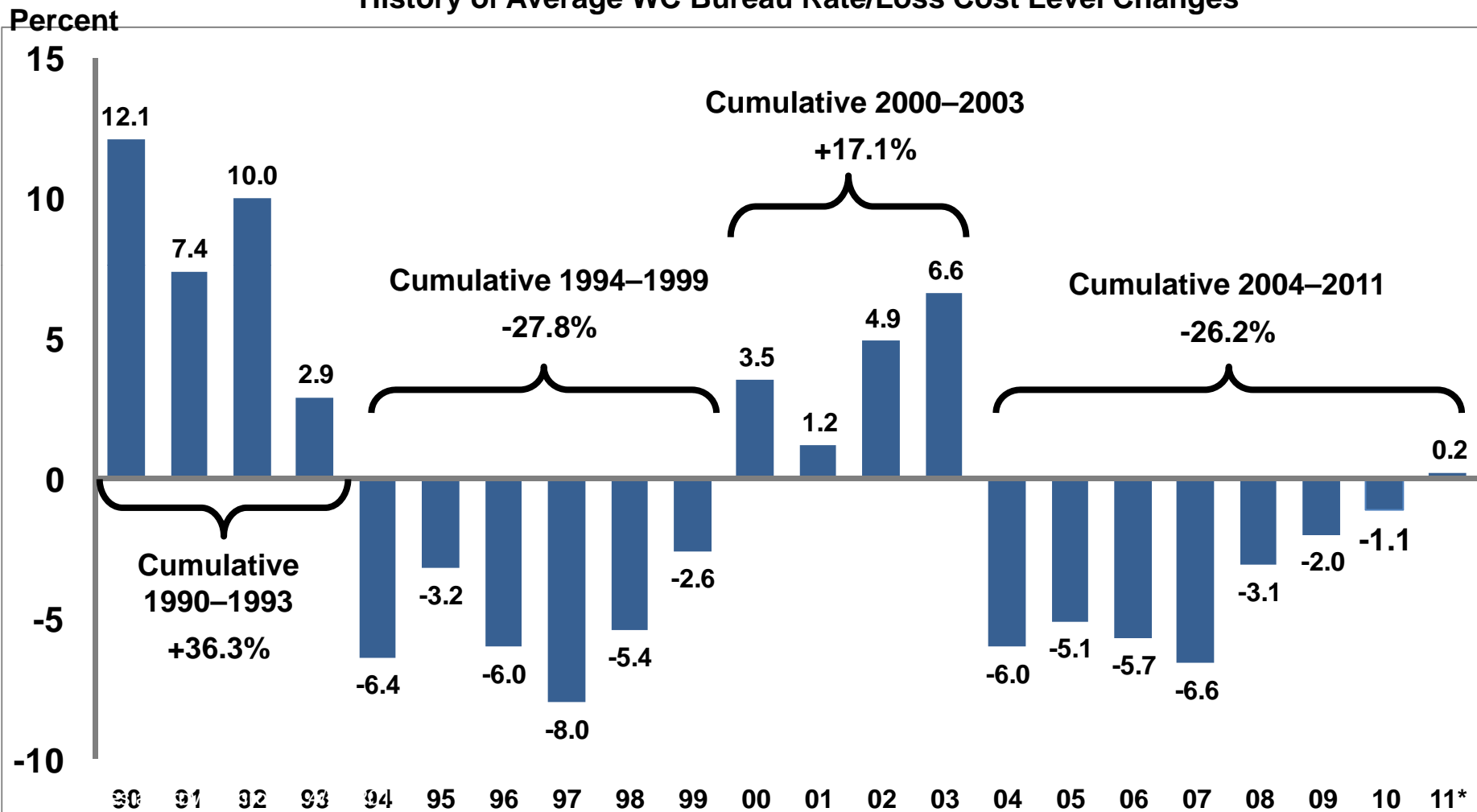
(Percent
Change)

The Q1 2011 WC rate
change was the smallest
decrease in many years



Average Approved Bureau Rates/Loss Costs

History of Average WC Bureau Rate/Loss Cost Level Changes



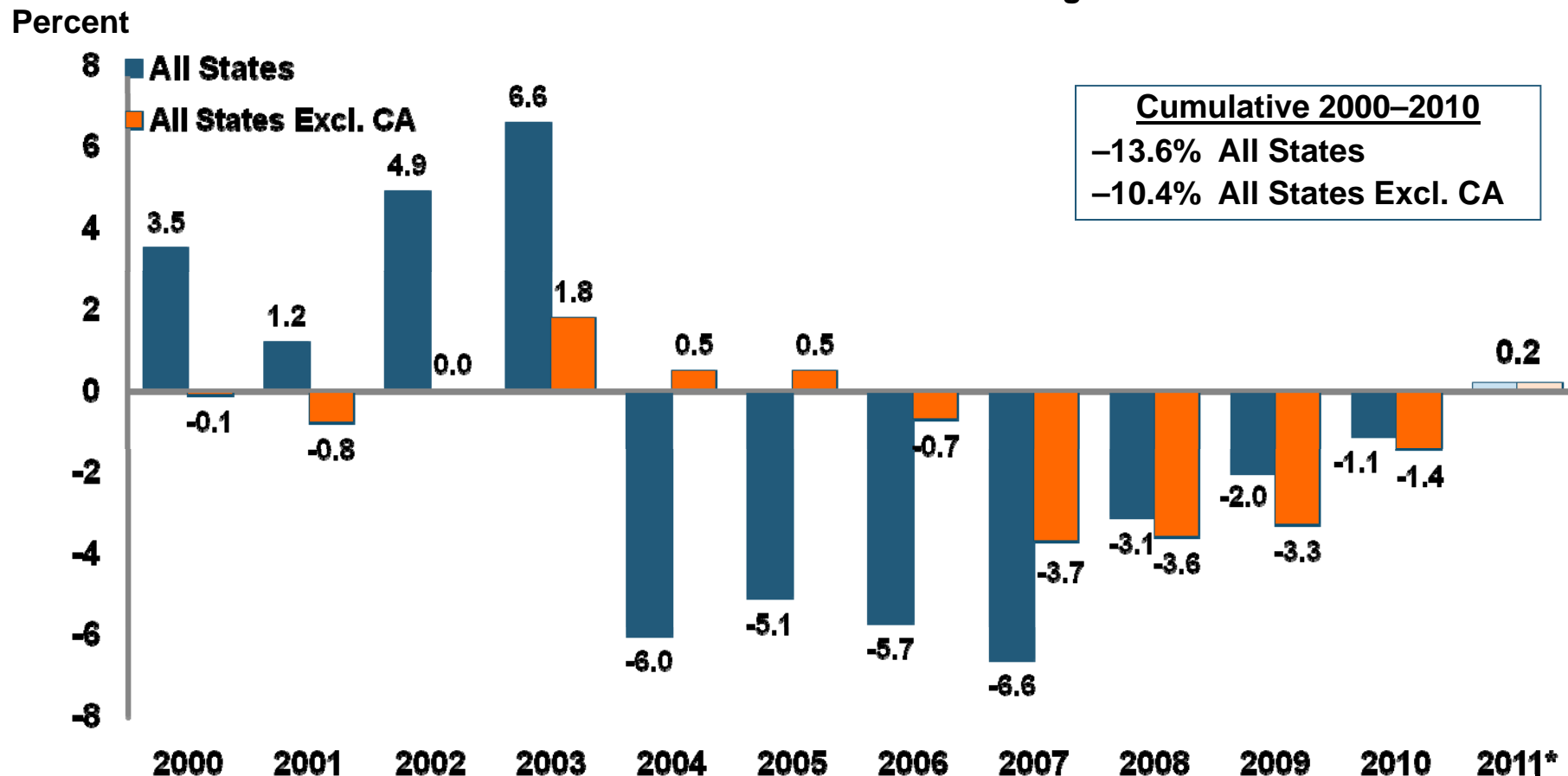
*States approved through 4/8/11.

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

Source: NCCI.

Average Approved Bureau Rates/Loss Costs

All States vs. All States Excluding California



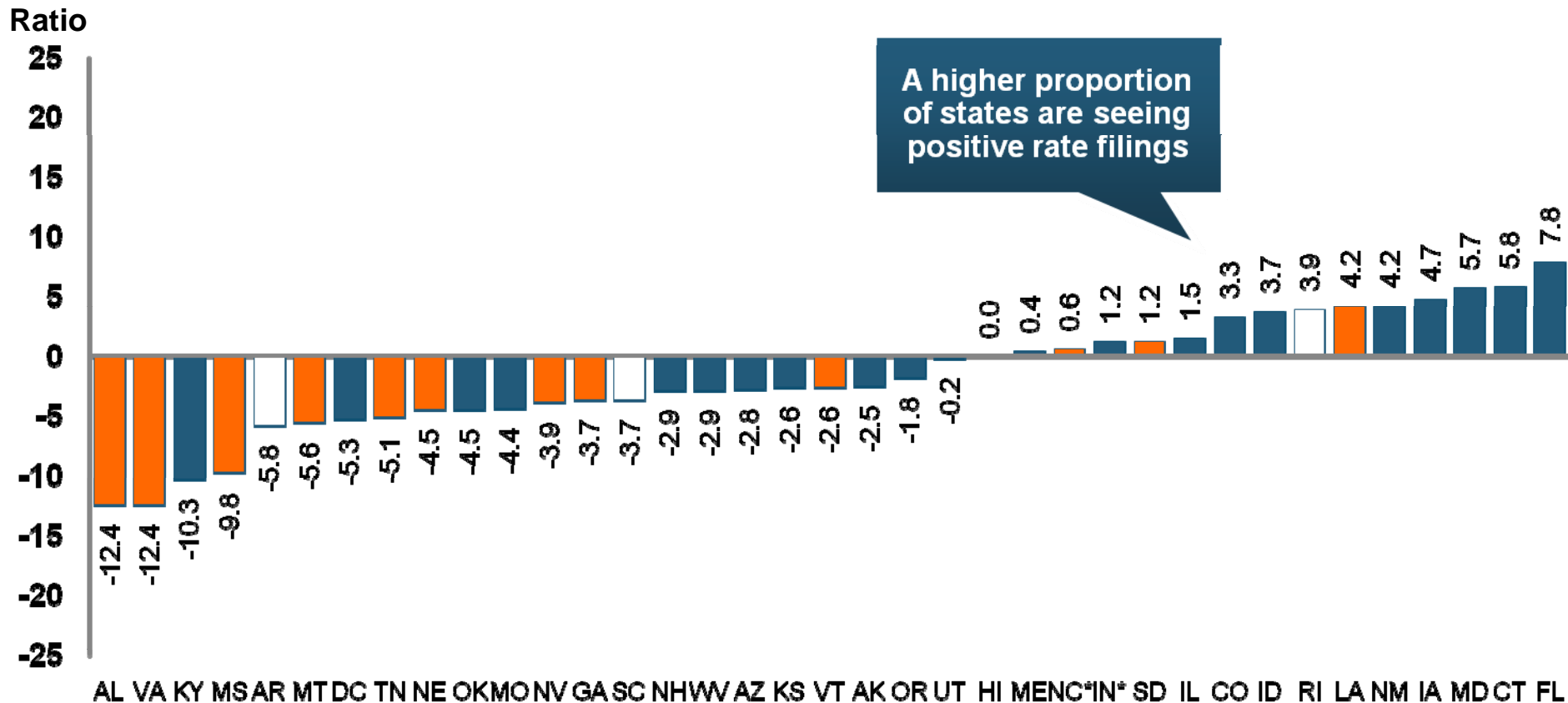
* States approved through 4/8/2011

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

Source: NCCI

Current NCCI Voluntary Market Filed Rate/Loss Cost Changes

Excludes Law-Only Filings



A higher proportion of states are seeing positive rate filings

■ Effective Dates 1/1/2011 and Prior ■ Effective Dates Subsequent to 1/1/2011 □ Filed and Pending

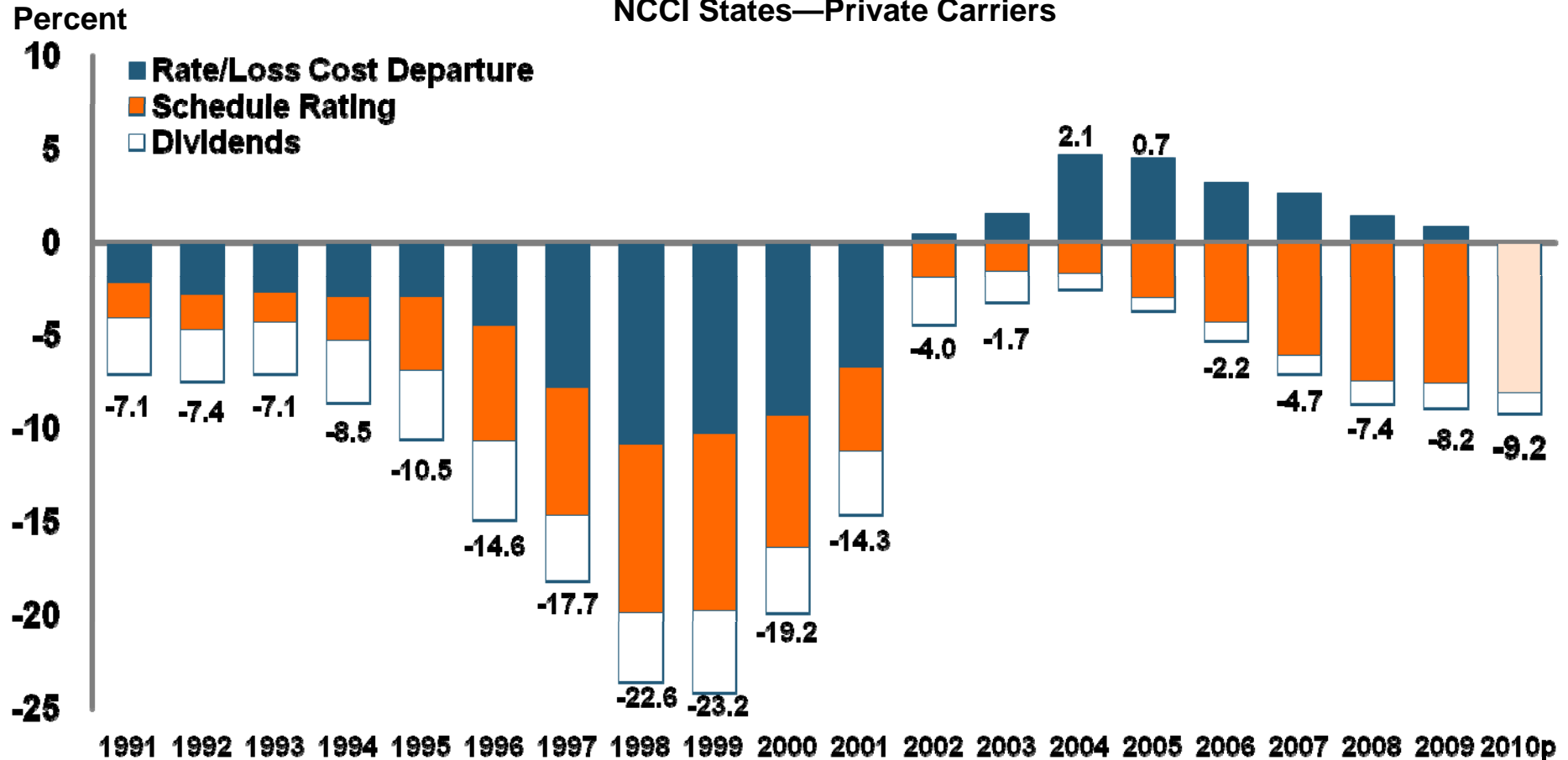
States filed through 4/15/2011

•IN and NC filed in cooperation with state rating bureau

Source: NCCI

Impact of Discounting on Workers Compensation Premium

NCCI States—Private Carriers



p Preliminary

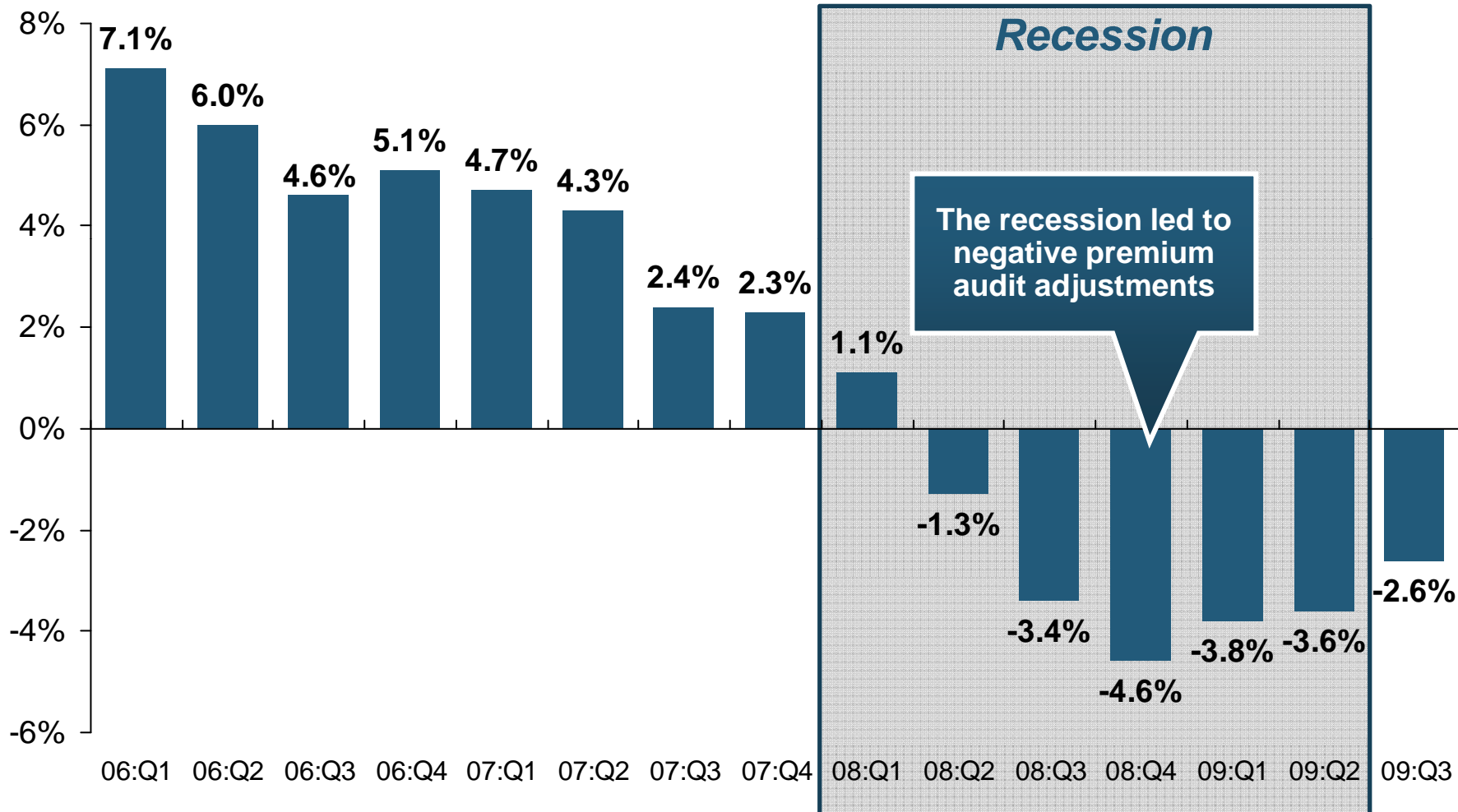
Dividend ratios are based on calendar year statistics

NCCI benchmark level does not include an underwriting contingency provision

Based on data through 12/31/2010 for the states where NCCI provides ratemaking services

Source: NCCI

Final Premium vs. Estimated Premium by Policy Effective Quarter: 2006:Q1 – 2009:Q3

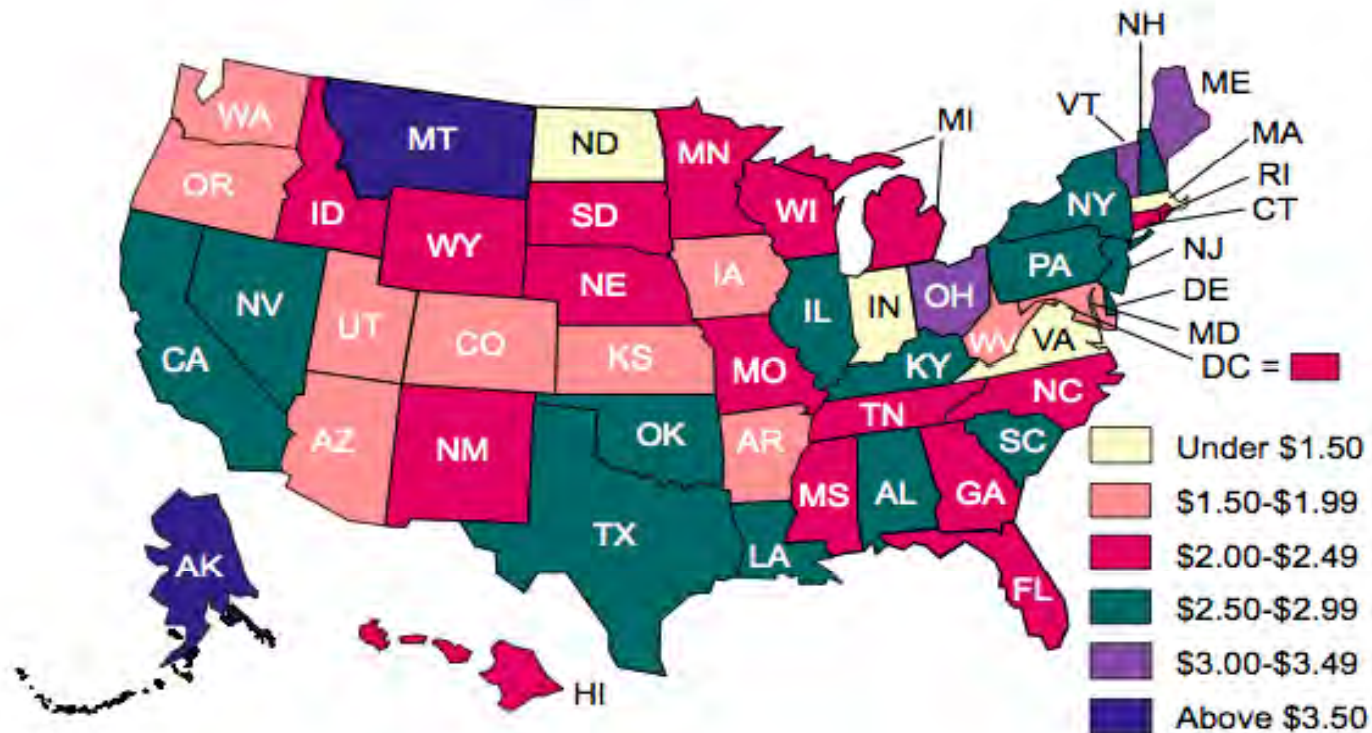


Note: WC Statistical Plan audited premium compared to policy-estimated premium. Based on states where NCCI provides ratemaking services, including state funds; excludes high deductible policies and mid-term cancellations.

Source: NCCI

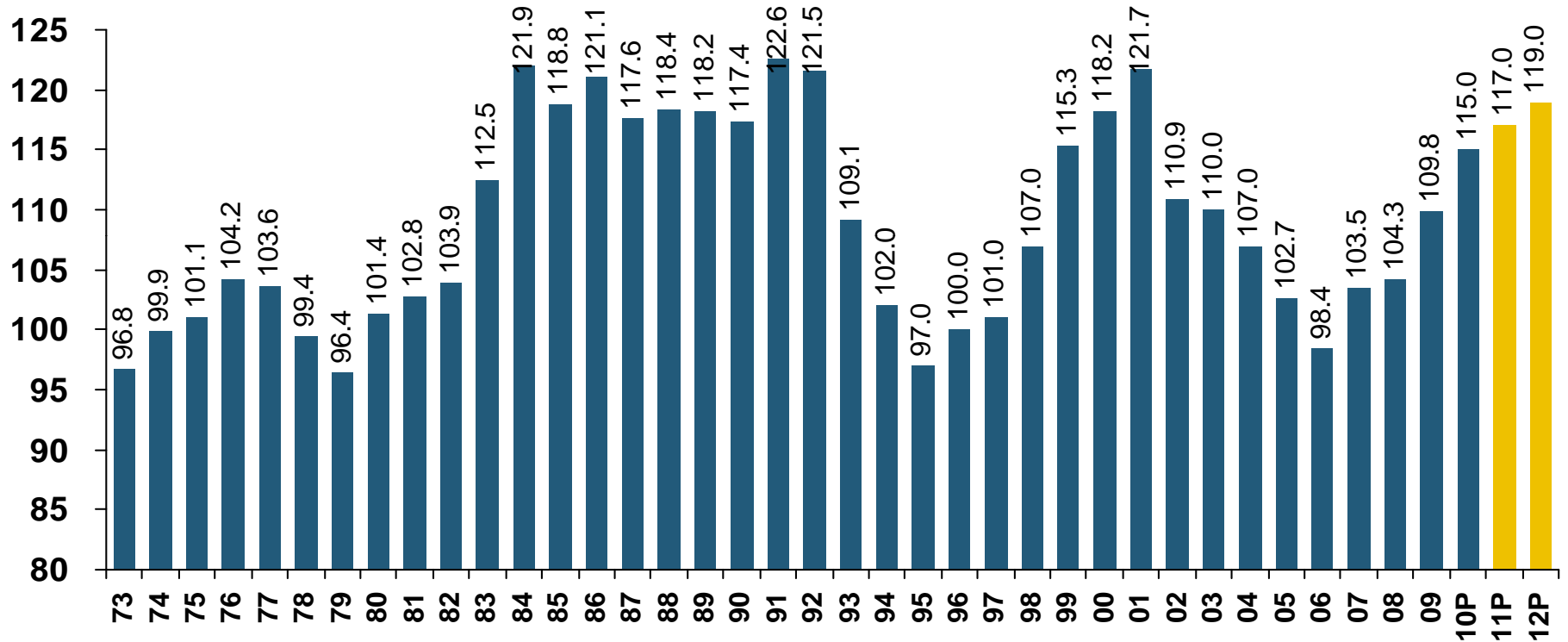
Comparison of State WC rates

WC rates, on average, do not appear to be significantly higher or lower in states with workers comp state funds



California's WC rates are about average

Workers Compensation Combined Ratio: 1973–2012P



Workers Comp Underwriting Results Are Deteriorating Markedly