



The Road Ahead: P-C Insurance in the Post-Crisis World *Focus on Texas Markets*

**Insurance Council of Texas Insurance Symposium
Austin, TX
July 15, 2010**

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- **Reasons for Optimism, Causes for Concern**
- **Insurance Industry Financial Overview & Outlook**
 - ◆ Profitability
 - ◆ Premium Growth
 - ◆ Underwriting Performance: Commercial & Personal Lines
 - ◆ Financial Market Impacts
- **Profitability in Texas P/C Insurance Markets**
- **Financial Services Reform: Impacts on the Insurance Industry**
- **Capital & Capacity**
- **Tort System Review: Overview and Causes for Concern**
- **Performance by Segment/Line**
 - ◆ Focus Medical Professional Liability Insurance and Workers Comp
- **Financial Strength & Ratings**
- **The Global Economic Storm: Financial Crisis & Recession**
 - ◆ Crisis-Driven Exposure Issues: Personal & Commercial Lines
 - ◆ Exposure, Growth & Profitability
- **Catastrophe Losses**

Reasons for Optimism, Causes for Concern in the P/C Insurance Industry

- **Economic Recovery in US is Self-Sustaining: No Double Dip Recession**
- **European Debt Crisis Will Pass; Concerns are Overblown**
 - ◆ Volatility will remain a reality, however
- **Era of Mass P/C Insurance Exposure Destruction Has Ended**
 - ◆ But restoration of destroyed exposure will take 3+ years in US
- **No Secondary Spike in Unemployment or Swoon in Payrolls/WC Exposure**
 - ◆ But job and wage growth remains sluggish
- **Exposure Growth Will Begin in Earnest in 2nd Half 2010, Accelerate in 2011**
- **Increase in Demand for Commercial Insurance is in its Earliest Stages and Will Accelerate in 2011**
 - ◆ Includes workers comp, commercial auto, marine, many liability coverages, D&O
 - ◆ Laggards: Property, inland marine, aviation
 - ◆ Personal Lines: Auto leads, homeowners lags
- **P/C Insurance Industry Will See Growth in 2011 for the First Time Since 2006**
- **Investment Environment Is/Remains Much More Favorable**
 - ◆ Volatility, however, will persist and yields remain low
 - ◆ Both are critical issues in long-tailed commercial lines like WC, Med Mal, D&O

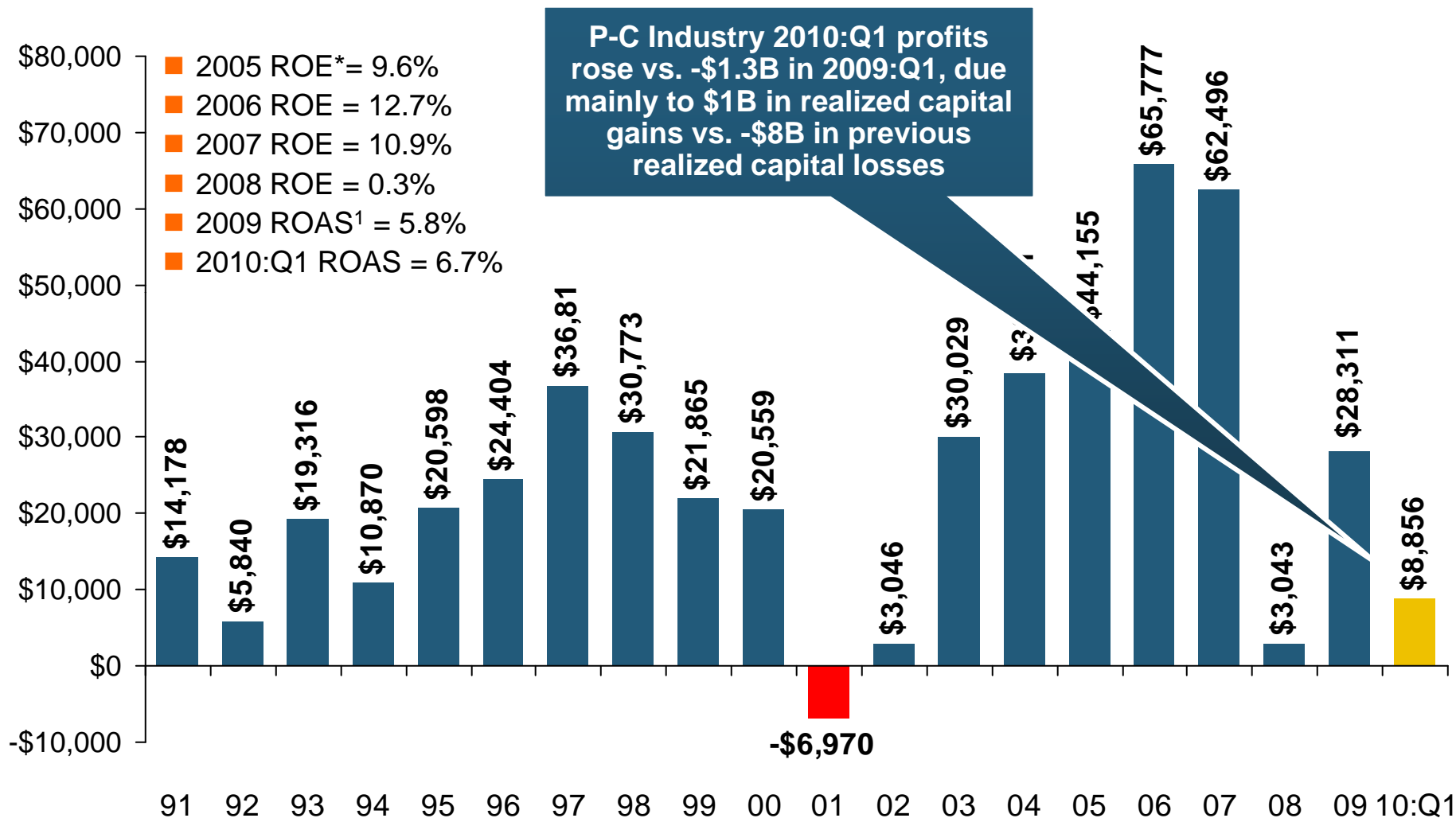
Reasons for Optimism, Causes for Concern in the P/C Insurance Industry

- **P/C Insurance Industry Capacity as of 3/31/10 Is at Record Levels and Has Recovered 100%+ of the Capital Lost During the Financial Crisis**
 - ◆ As of 12/31/09 capacity was within 2% of pre-crisis high
- **Record Capacity, Depressed Exposures Mean that Generally Soft Market Conditions Will Persist through 2010 and Potentially into 2011**
- **There is No Catalyst for a Robust Hard Market at the Current Time**
- **High Global First Half 2010 CAT Losses Insufficient to Trigger Hard Market**
 - ◆ Localized insurance and reinsurance impacts are occurring, especially earthquake coverage in Latin/South America, Offshore Energy Markets, European Wind Cover
- **Inflation Outlook for US and Major European Economies and Japan is Tame**
 - ◆ Will temper claims inflation
- **Financial Strength & Ratings of Global (Re)Insurance Industries Remained Strong Throughout the Financial Crisis in Sharp Contrast With Banks**
- **Insurers Have Avoided (So Far) the Most Draconian Outcomes in Financial Services Reform Legislation**
- **Tort Environment in US is Beginning to Deteriorate; No Tort Reform in US**
- **Major Transformation of US Economy Underway with Major Opportunities for Insurers through 2020 in Health, Tech, Natural Resources, Energy**

Profitability

Historically Volatile

P/C Net Income After Taxes 1991–2010:Q1 (\$ Millions)

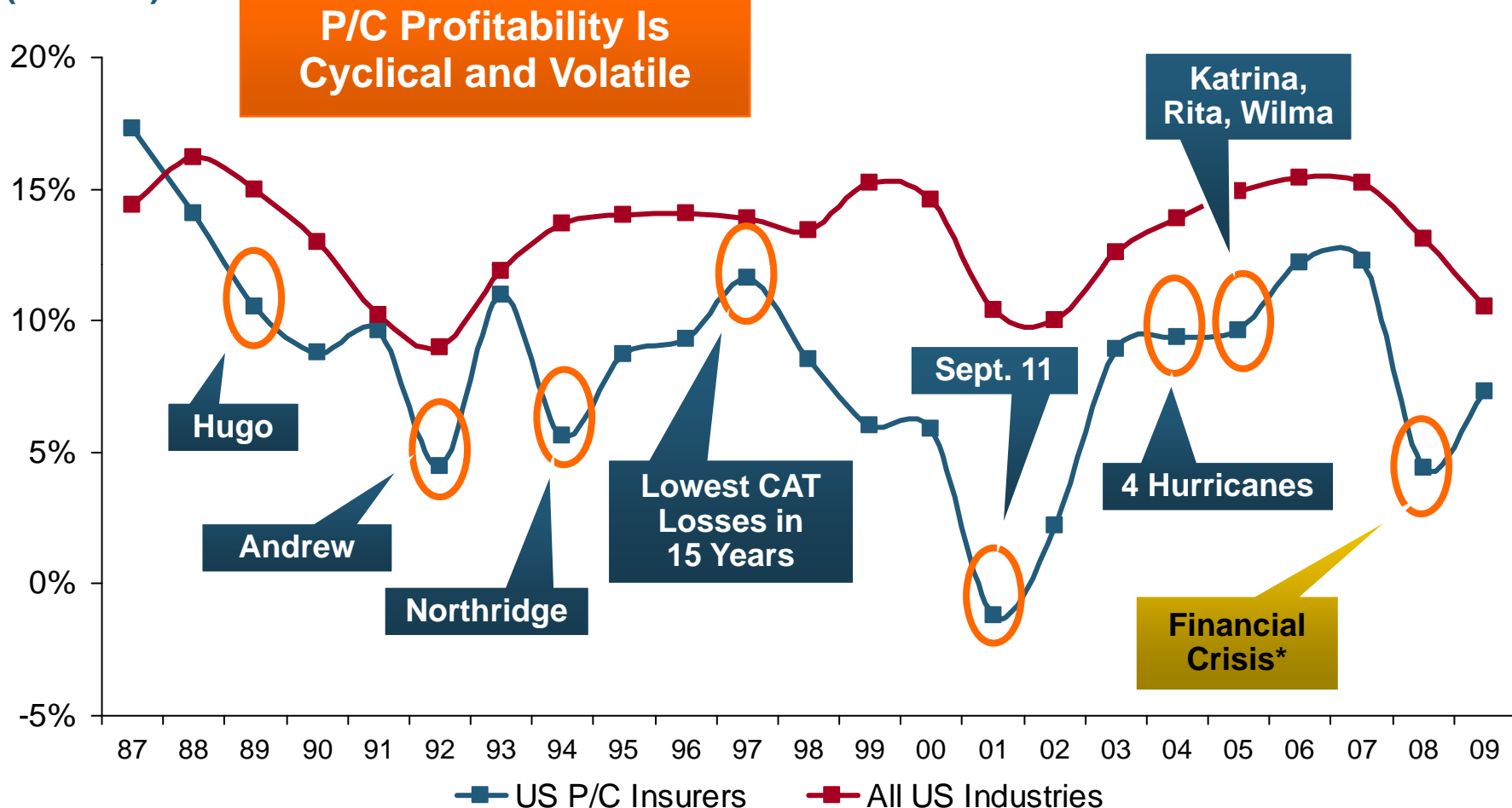


* ROE figures are GAAP; ¹Return on avg. surplus. Excluding Mortgage & Financial Guaranty insurers yields an 8.3% ROAS for 2010:Q1, 7.3% for 2009 and 4.4% for 2008. 2009 net income was \$34.5 billion and \$20.8 billion in 2008 excluding M&FG.

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

ROE: P/C vs. All Industries 1987–2009*

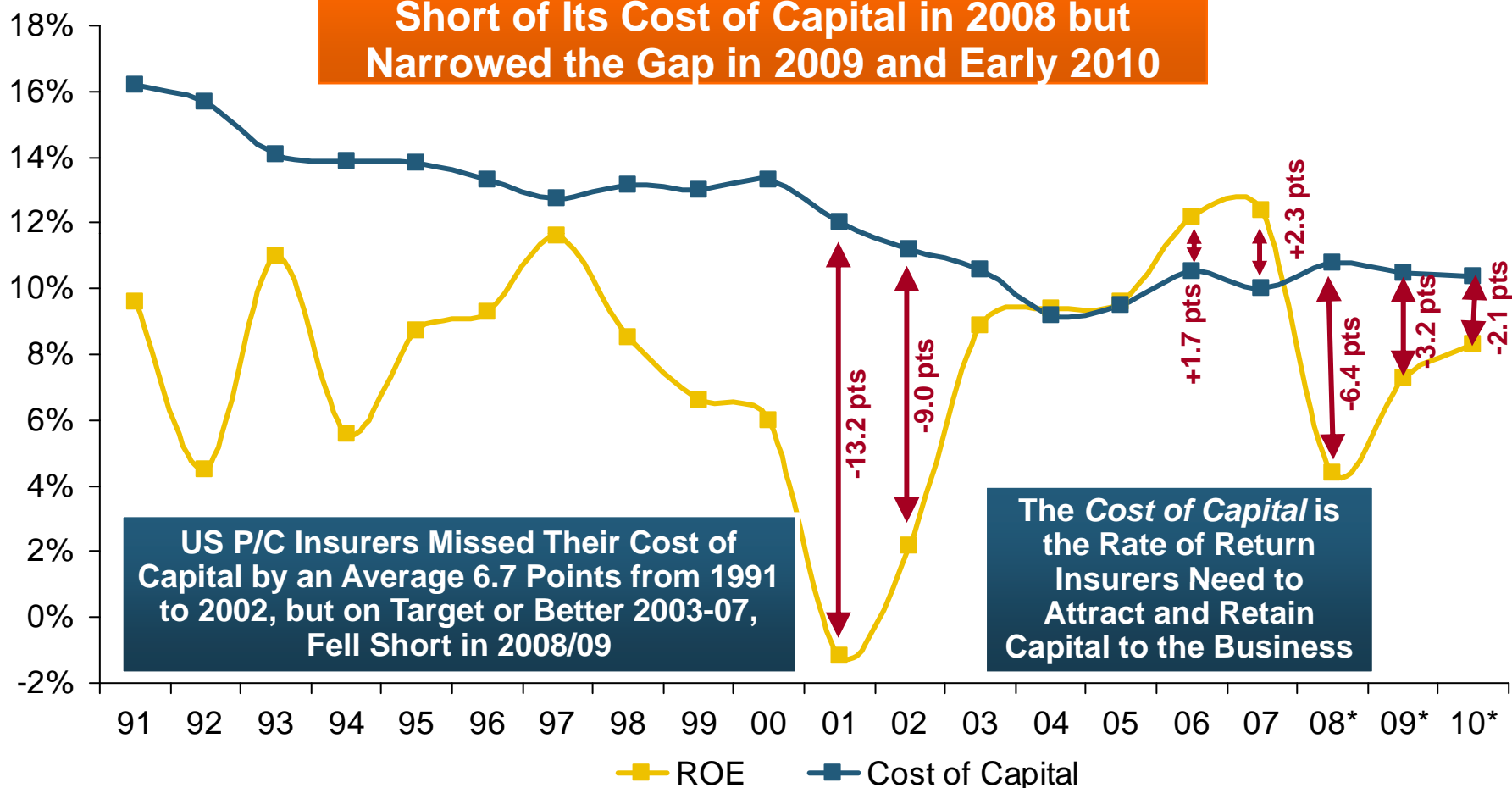
(Percent)



* Excludes Mortgage & Financial Guarantee in 2008 and 2009.
 Sources: ISO, *Fortune*; Insurance Information Institute.

ROE vs. Equity Cost of Capital: U.S. P/C Insurance:1991-2010*

(Percent)

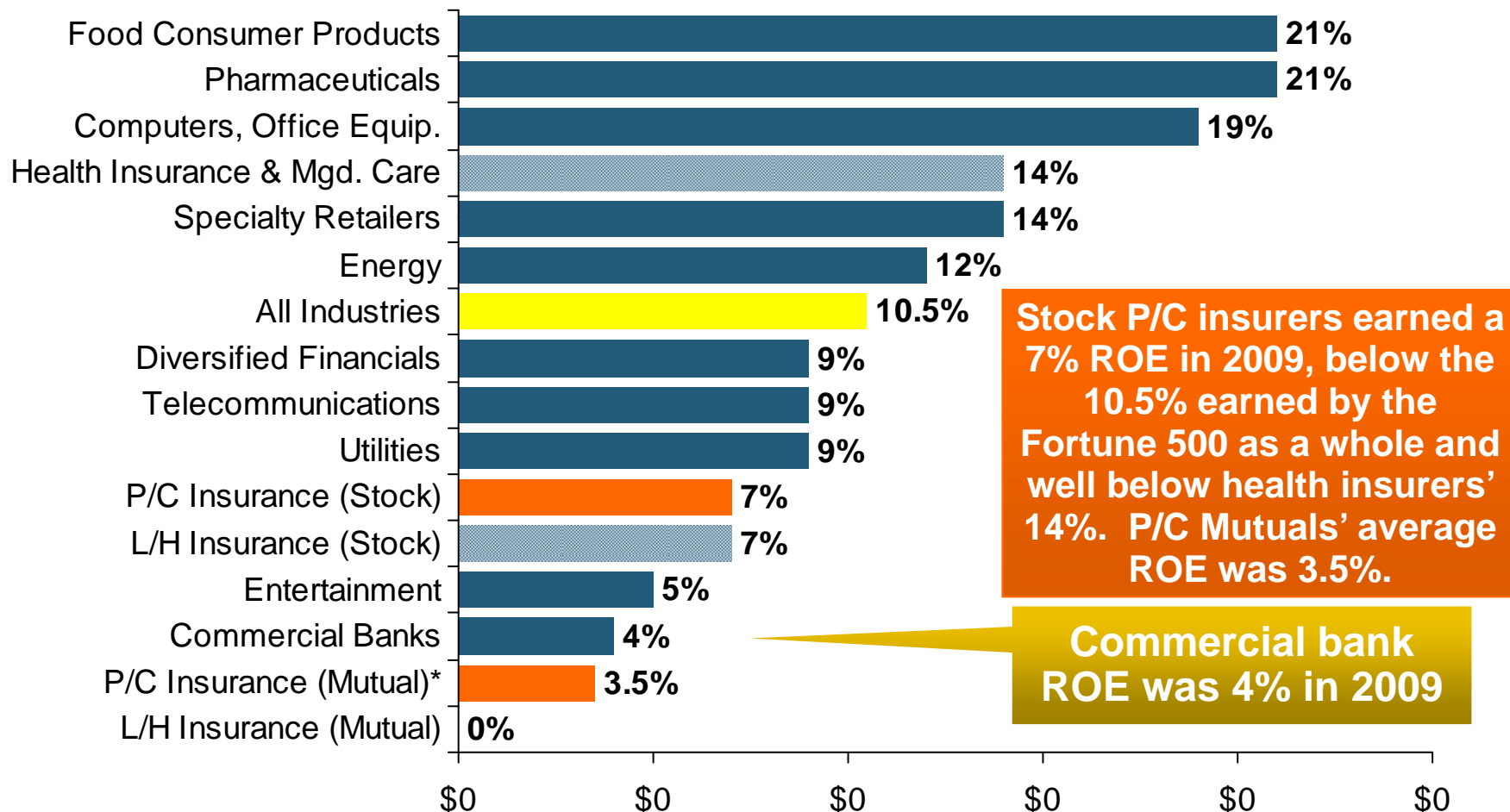


* Return on average surplus in 2008/09 excluding mortgage and financial guaranty insurers.

Source: The Geneva Association, Insurance Information Institute

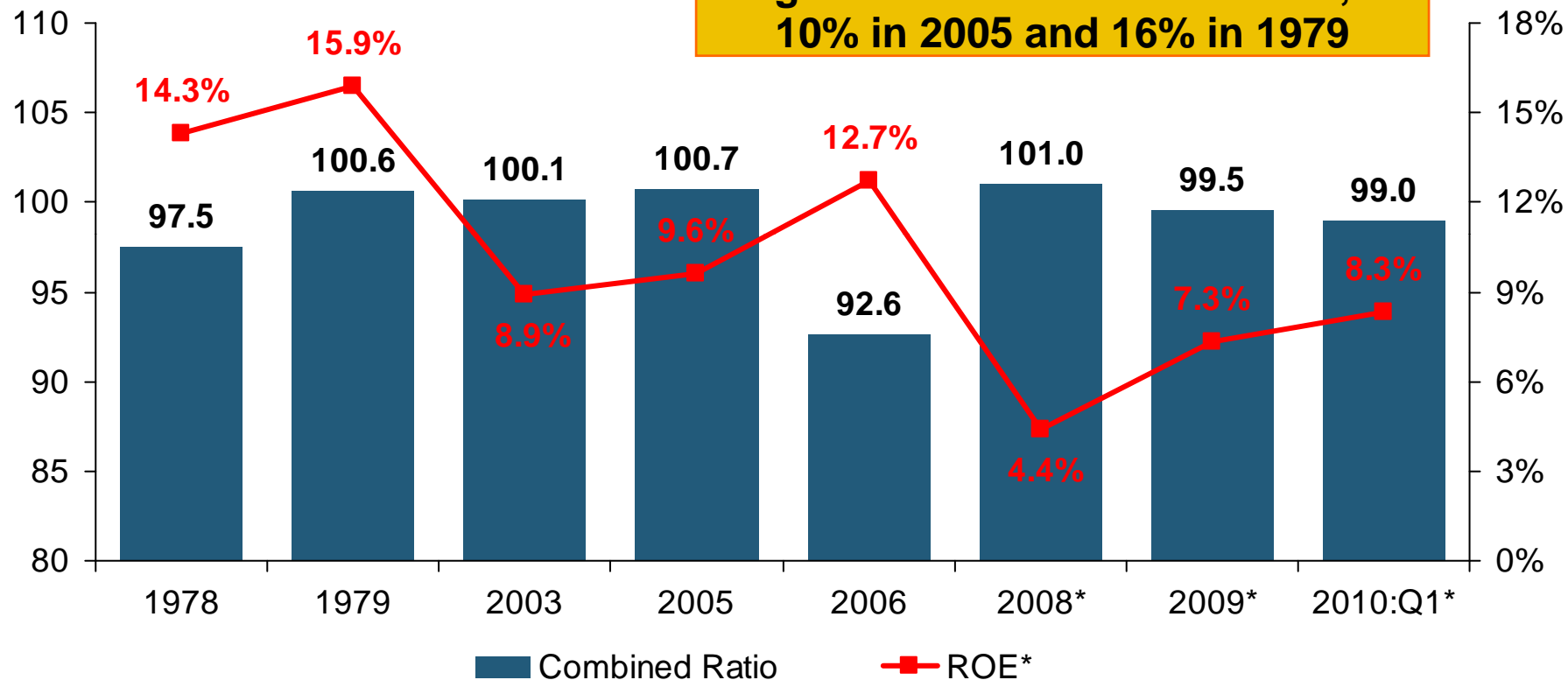
Median ROE for Insurers vs. Financial Firms & Other Key Industries 2009

(Profits as a % of Stockholders' Equity)



A 100 Combined Ratio Isn't What It Once Was: 90-95 Is Where It's At Now

Combined Ratio / ROE



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

* 2009 and 2010:Q1 figures are return on average statutory surplus. 2008, 2009 and 2010:Q1 figures exclude mortgage and financial guarantee insurers

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

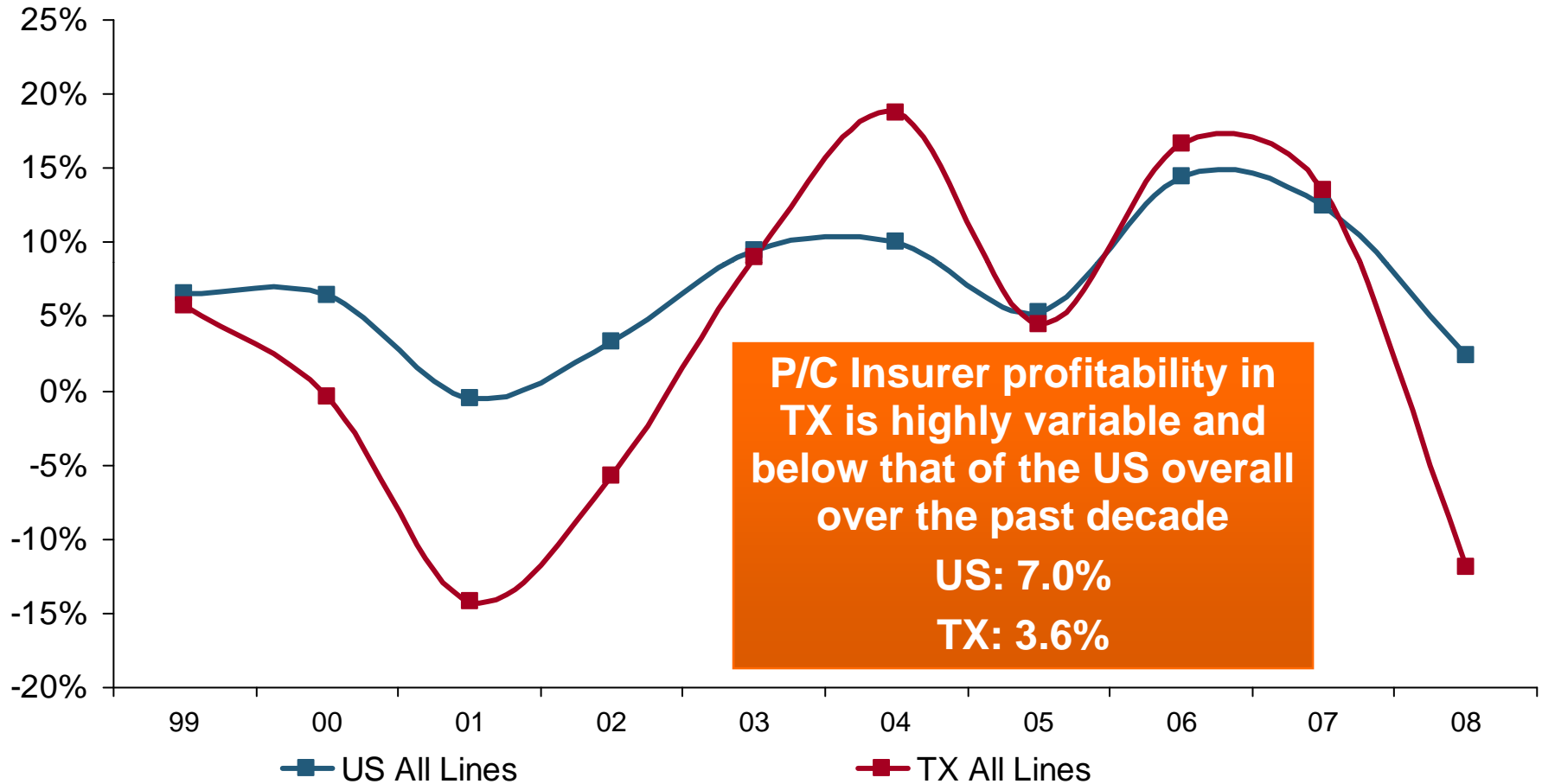


Profitability in Texas P/C Insurance Markets

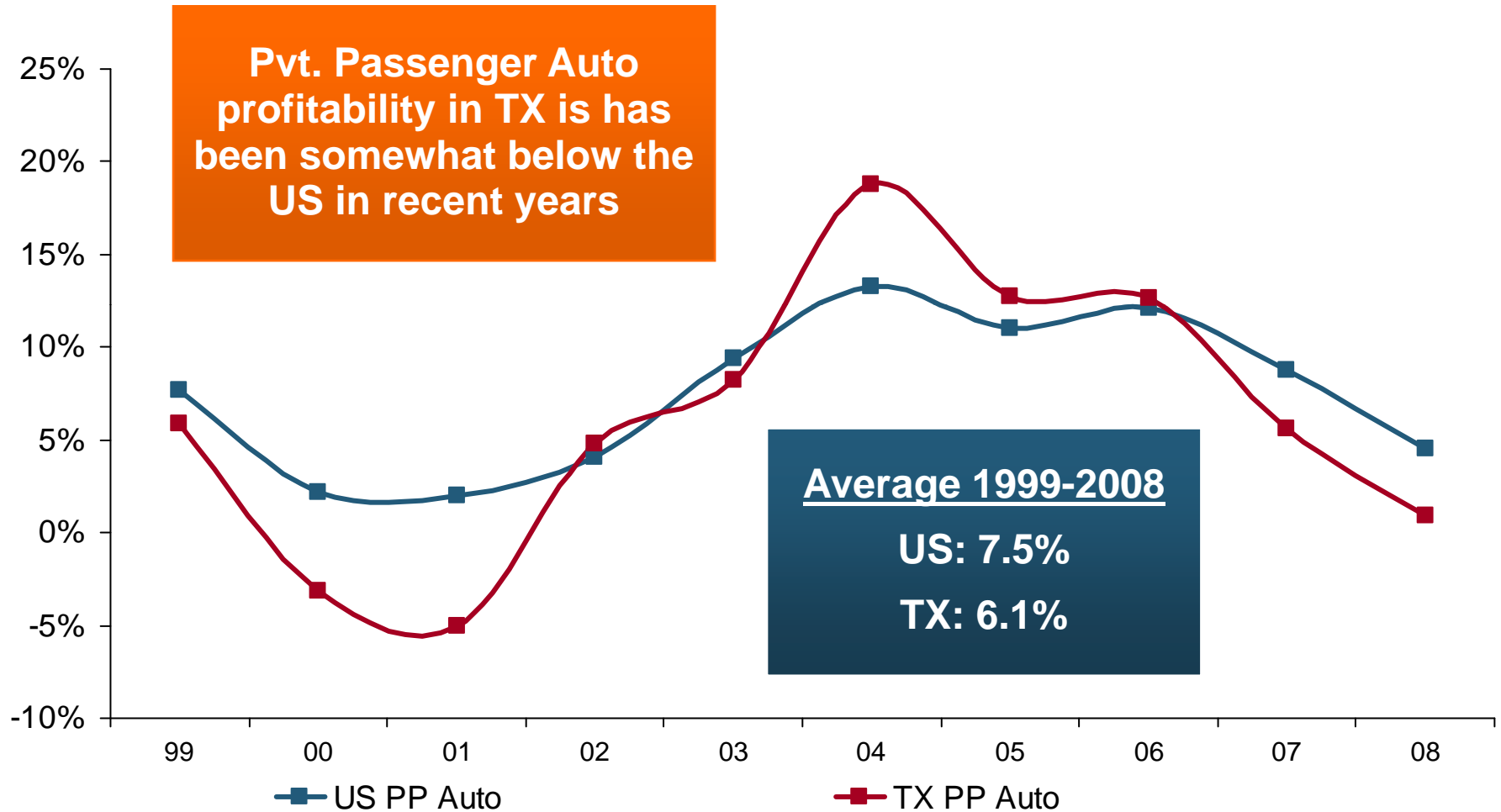
Analysis by Line and Nearby State Comparisons

RNW All Lines: TX vs. U.S., 1999-2008

(Percent)

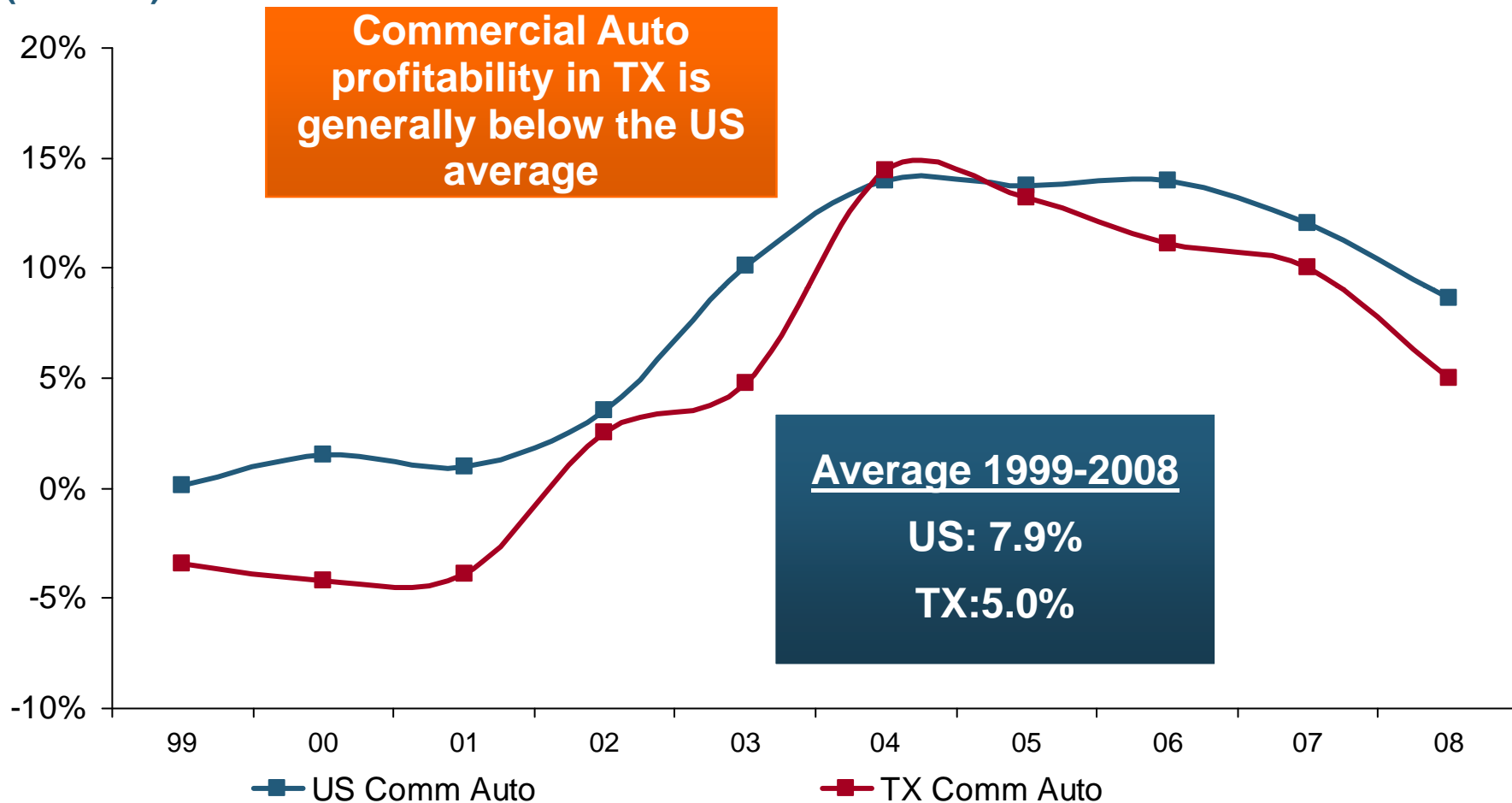


RNW PP Auto: TX vs. U.S., 1999-2008



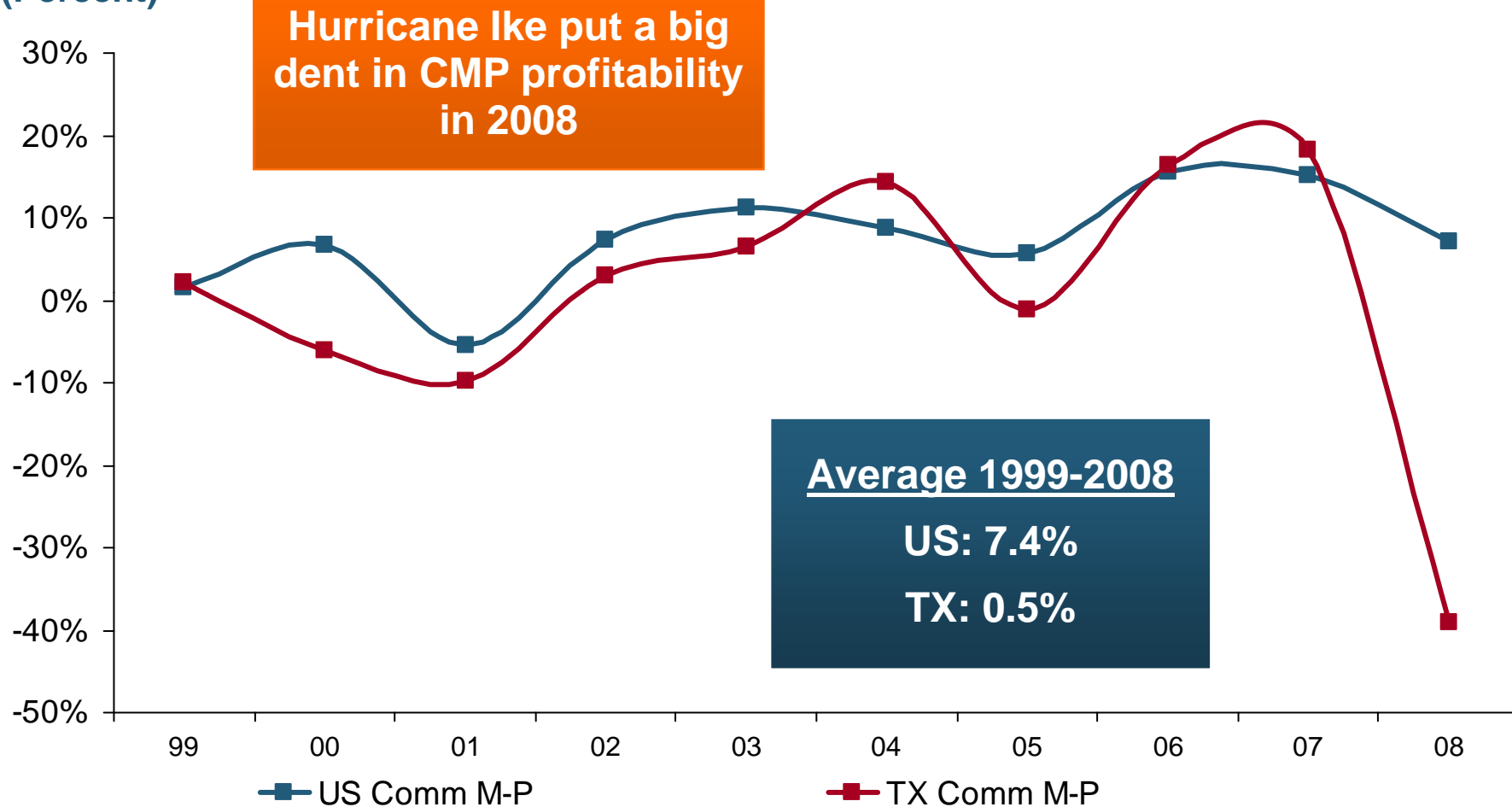
RNW Comm. Auto: TX vs. U.S., 1999-2008

(Percent)



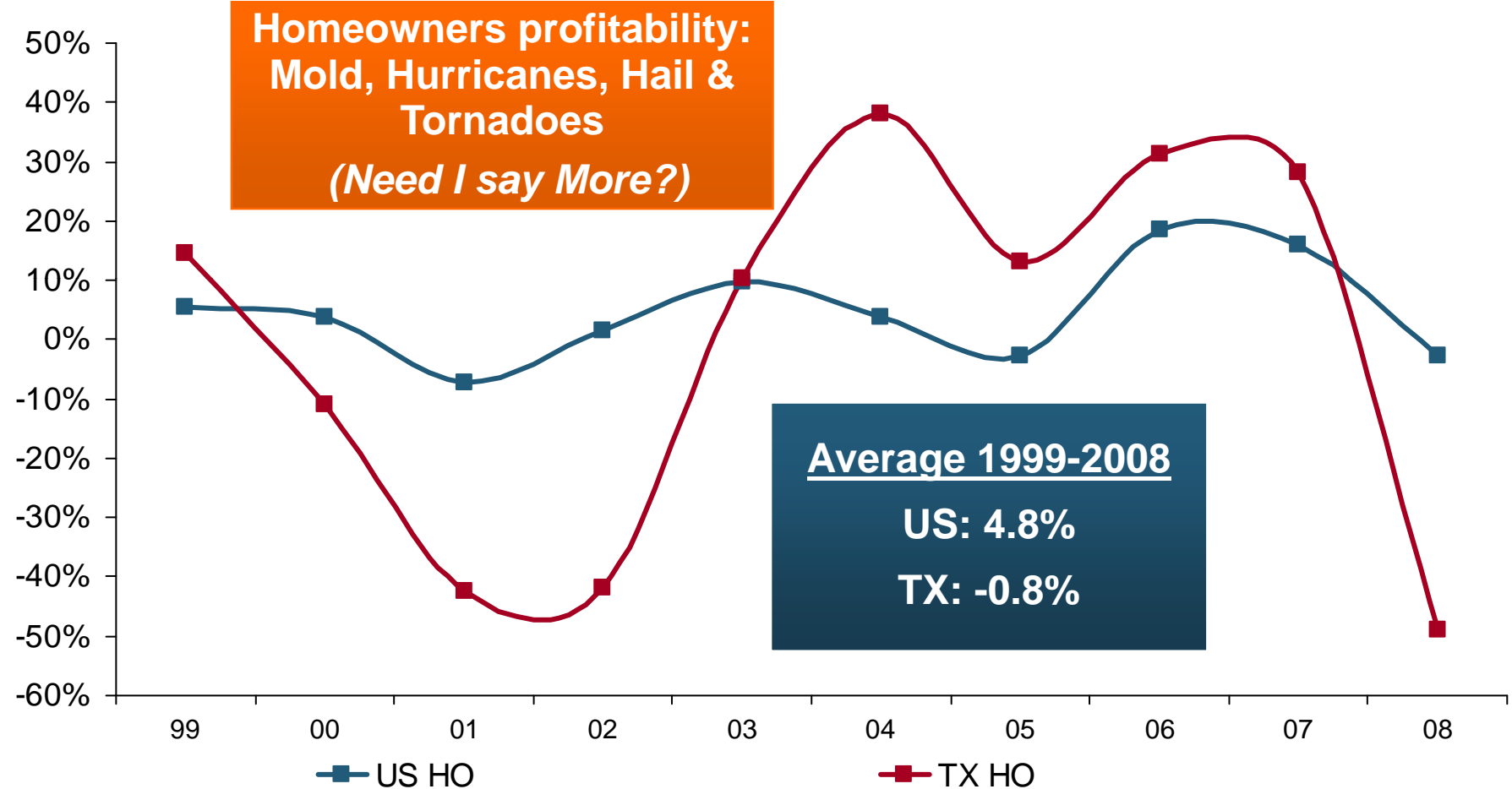
RNW Comm. Multi-Peril: TX vs. U.S., 1999-2008

(Percent)



RNW Homeowners: TX vs. U.S., 1999-2008

(Percent)



Texans Have Found the Solution to Reducing Hurricane Loss Frequency



Though still in the testing phase, some property owners along the Texas Gulf coast are erecting “Private Property” signs to keep hurricanes out. They are said to be filing a request for a mitigation credit with TDI.

Me on vacation, July 4, 2010, in Port Aransas, TX, at “Virginia’s On the Bay” Restaurant



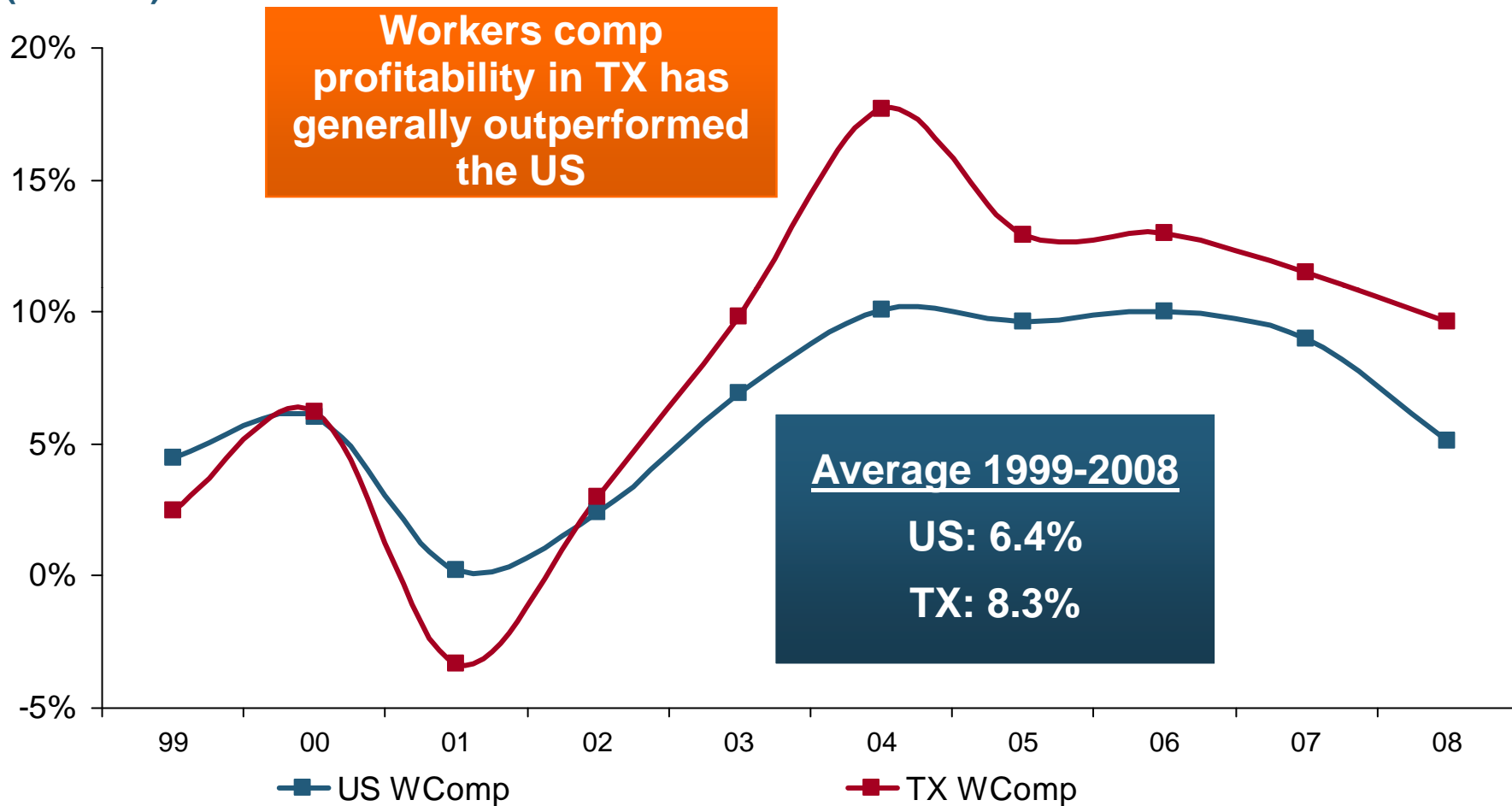
Texas Tar Balls: Long a Fixture on Texas Beaches



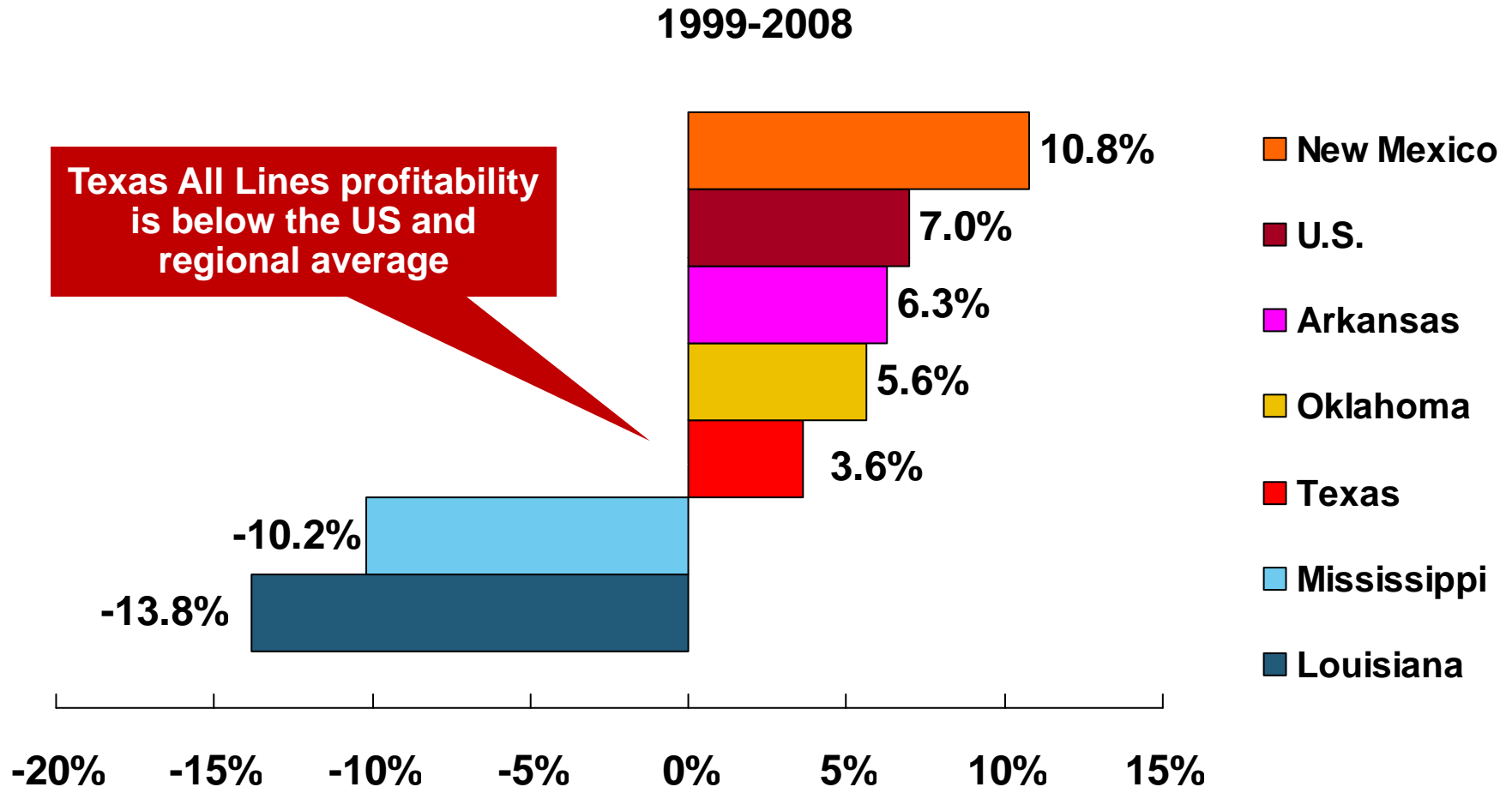
Tar balls gathered on Port Aransas Beach on July 3, 2010. These have nothing to do with the Deepwater Horizon event.

RNW Workers Comp: TX vs. U.S., 1999-2008

(Percent)



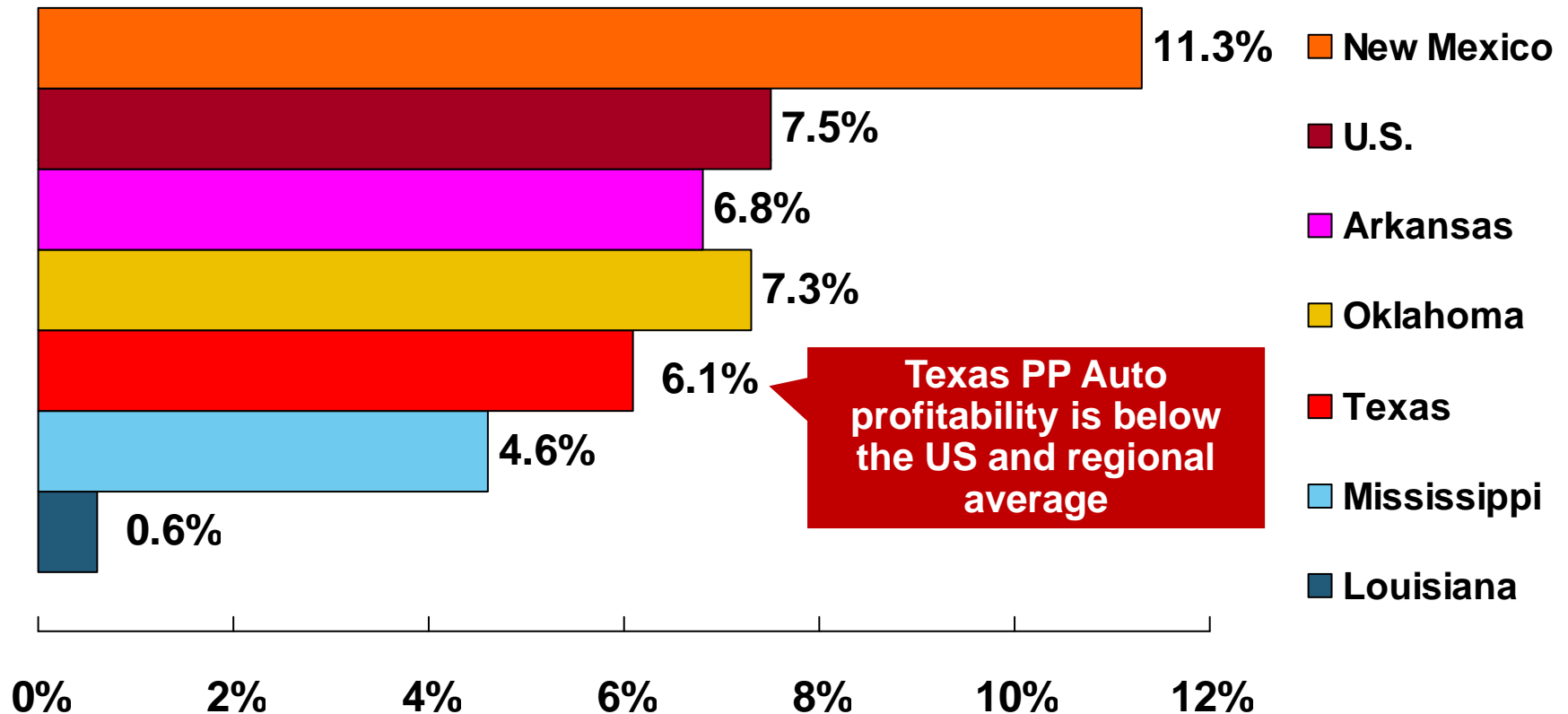
All Lines: 10-Year Average RNW TX & Nearby States



Source: NAIC, Insurance Information Institute

PP Auto: 10-Year Average RNW TX & Nearby States

1999-2008



Source: NAIC, Insurance Information Institute

Top Ten Most Expensive And Least Expensive States For Automobile Insurance, 2007 (1)

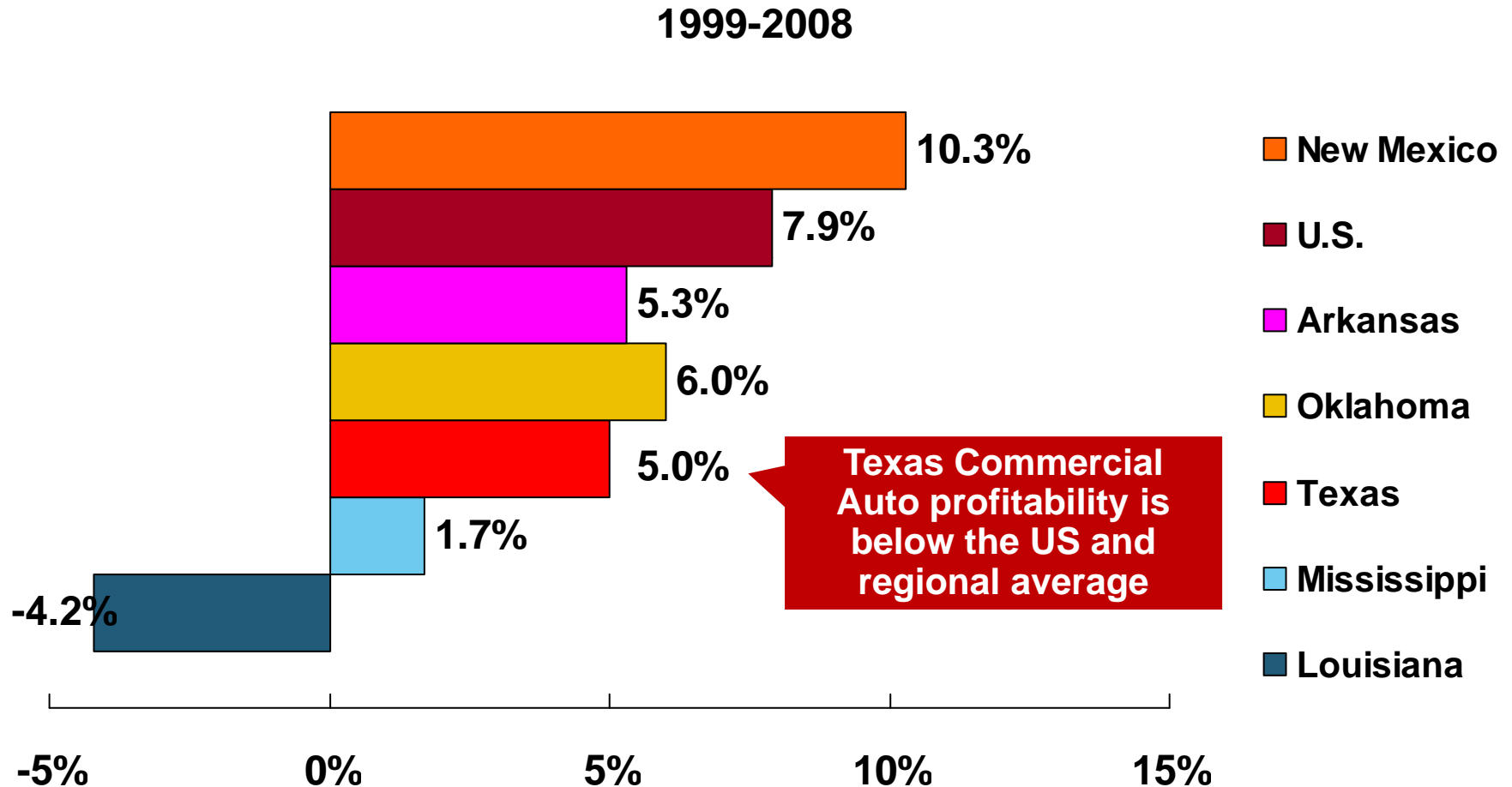
| Rank | Most expensive states | Average expenditure | Rank | Least expensive states | Average expenditure |
|------|-----------------------|---------------------|------|------------------------|---------------------|
| 1 | D.C. | \$1,140 | 1 | North Dakota | \$512 |
| 2 | New Jersey | 1,104 | 2 | Iowa | 518 |
| 3 | Louisiana | 1,096 | 3 | South Dakota | 534 |
| 4 | New York | 1,047 | 4 | Nebraska | 554 |
| 5 | Florida | 1,043 | 5 | Idaho | 564 |
| 6 | Rhode Island | 1,017 | 6 | Kansas | 568 |
| 7 | Delaware | 1,012 | 7 | Wisconsin | 582 |
| 8 | Nevada | 1,000 | 8 | North Carolina | 591 |
| 9 | Massachusetts | 981 | 9 | Maine | 611 |
| 10 | Connecticut | 964 | 10 | Indiana | 618 |

Texas ranked 19th in 2007, with an average expenditure for auto insurance of \$808.

(1) Based on average automobile insurance expenditures.

Source: © 2009 National Association of Insurance Commissioners.

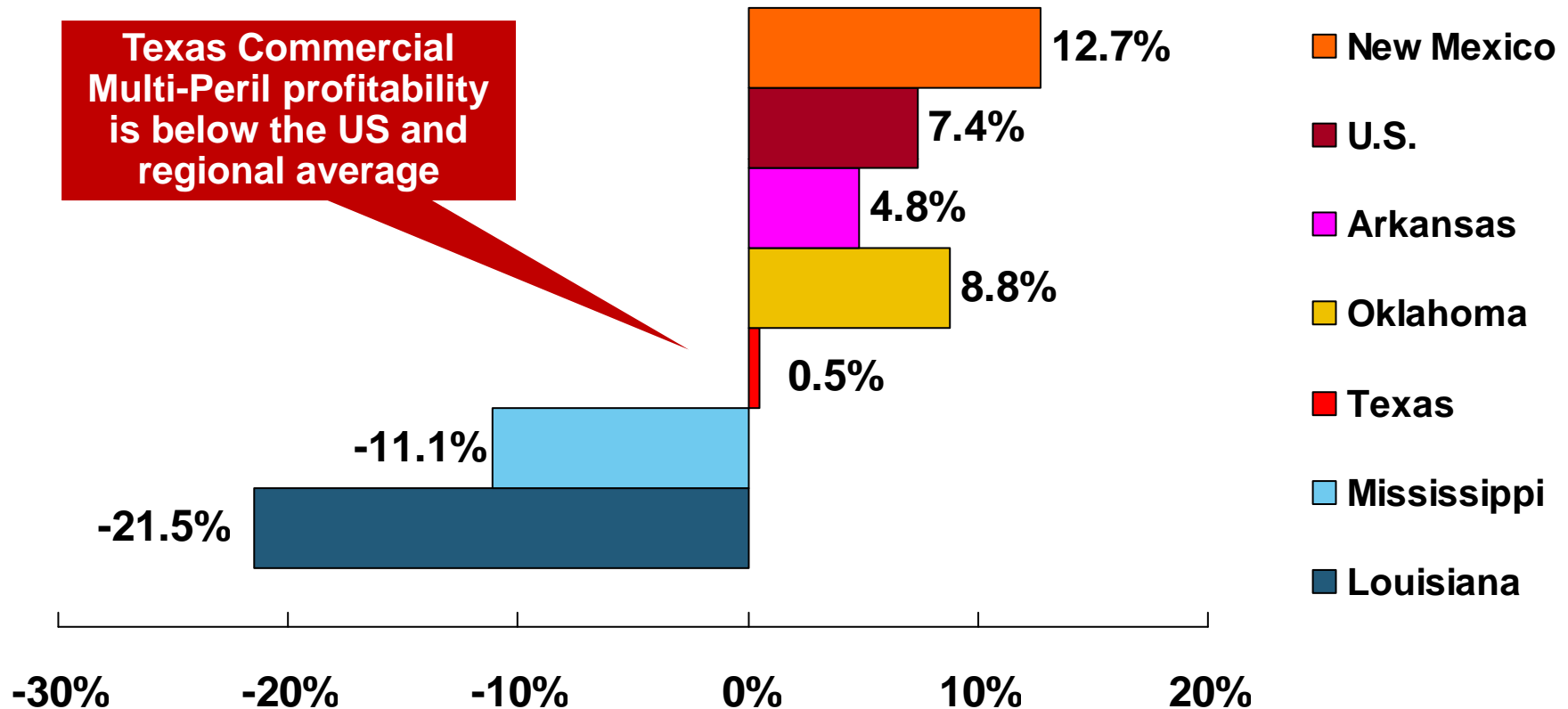
Comm. Auto: 10-Year Average RNW TX & Nearby States



Source: NAIC, Insurance Information Institute

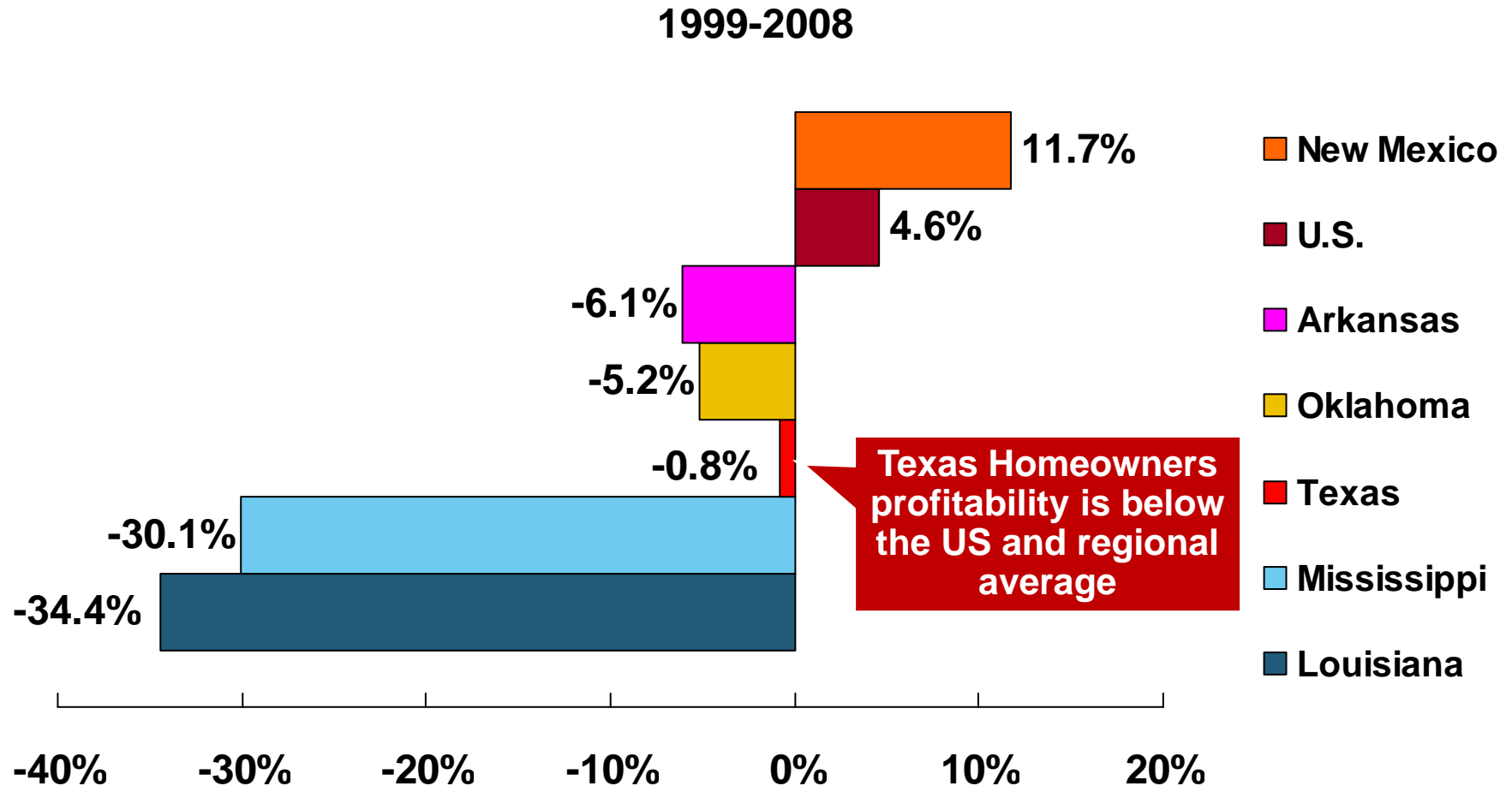
Comm. M-P: 10-Year Average RNW TX & Nearby States

1999-2008



Source: NAIC, Insurance Information Institute

Homeowners: 10-Year Average RNW TX & Nearby States



Source: NAIC, Insurance Information Institute

Top Ten Most Expensive And Least Expensive States For Homeowners Insurance, 2007 (1)

Texas ranked as the second most expensive state for homeowners insurance in 2007, with an average expenditure of \$1,448.

| Rank | Most expensive states | Average expenditure | Rank | Least expensive states | Average expenditure |
|------|-----------------------|---------------------|------|------------------------|---------------------|
| 1 | Florida (2) | \$1,534 | 1 | Idaho | \$422 |
| 2 | Texas (3) | 1,448 | 2 | Wisconsin | 491 |
| 3 | Louisiana | 1,400 | 3 | Oregon | 496 |
| 4 | D.C. | 1,089 | 4 | Utah | 505 |
| 5 | Oklahoma | 1,054 | 5 | Washington | 506 |
| 6 | Massachusetts | 1,023 | 6 | Ohio | 540 |
| 7 | Mississippi | 1,019 | 7 | Delaware | 559 |
| 8 | Rhode Island | 950 | 8 | Kentucky | 578 |
| 9 | New York | 936 | 9 | Maine | 596 |
| 10 | Connecticut | 929 | 10 | Iowa | 610 |

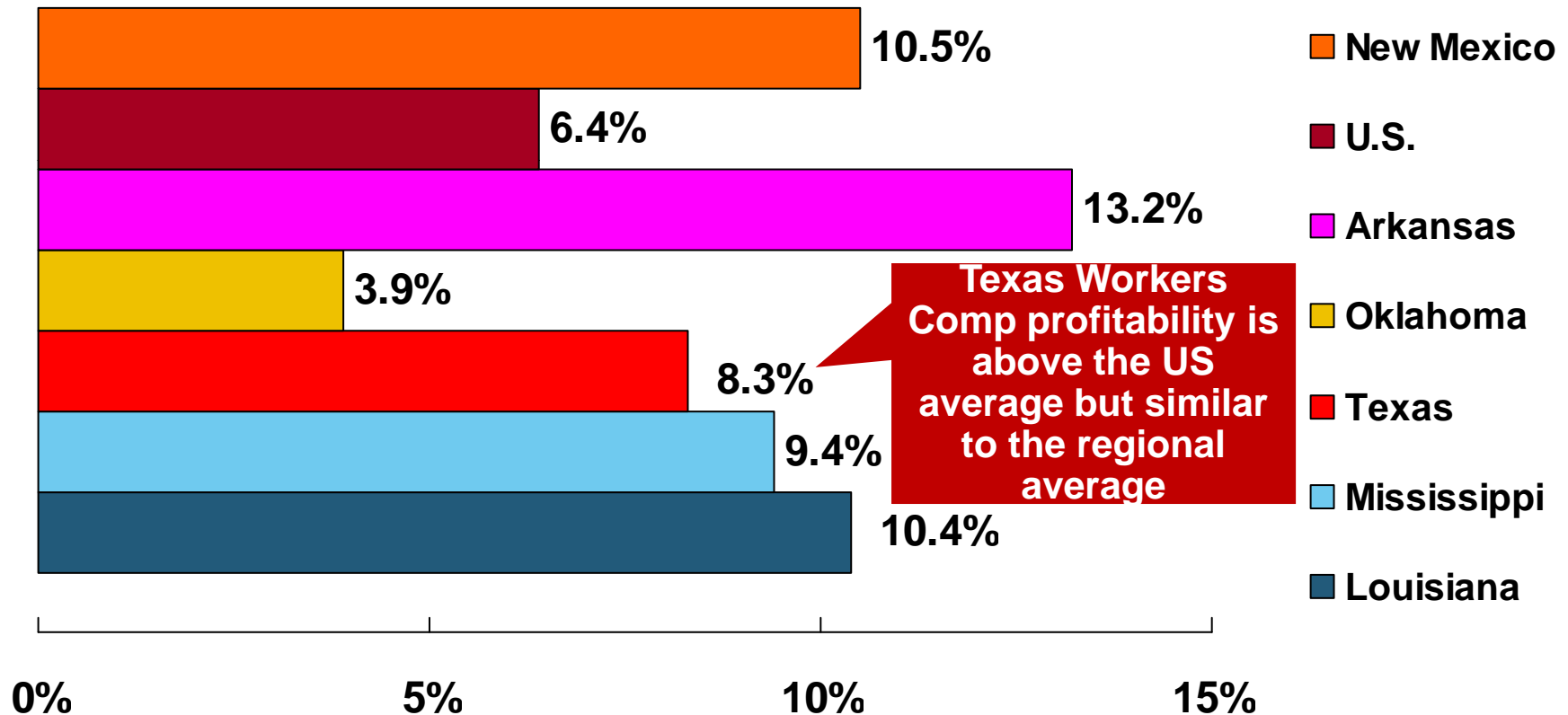
- (1) Based on the HO-3 homeowner package policy for owner-occupied dwellings, 1 to 4 family units. Provides “all risks” coverage (except those specifically excluded in the policy) on buildings and broad named-peril coverage on personal property, and is the most common package written.
- (2) Florida data excludes policies written by Citizen's Property Insurance Corporation, the state's insurer of last resort, and therefore are not directly comparable to other states.
- (3) The Texas Department of Insurance developed home insurance policy forms that are similar but not identical to the standard forms.

Note: Average premium=Premiums/exposure per house years. A house year is equal to 365 days of insured coverage for a single dwelling. The NAIC does not rank State Average Expenditures and does not endorse any conclusions drawn from this data.

Source: © 2009 National Association of Insurance Commissioners (NAIC). Reprinted with permission. Further reprint or distribution strictly prohibited without written permission of NAIC.

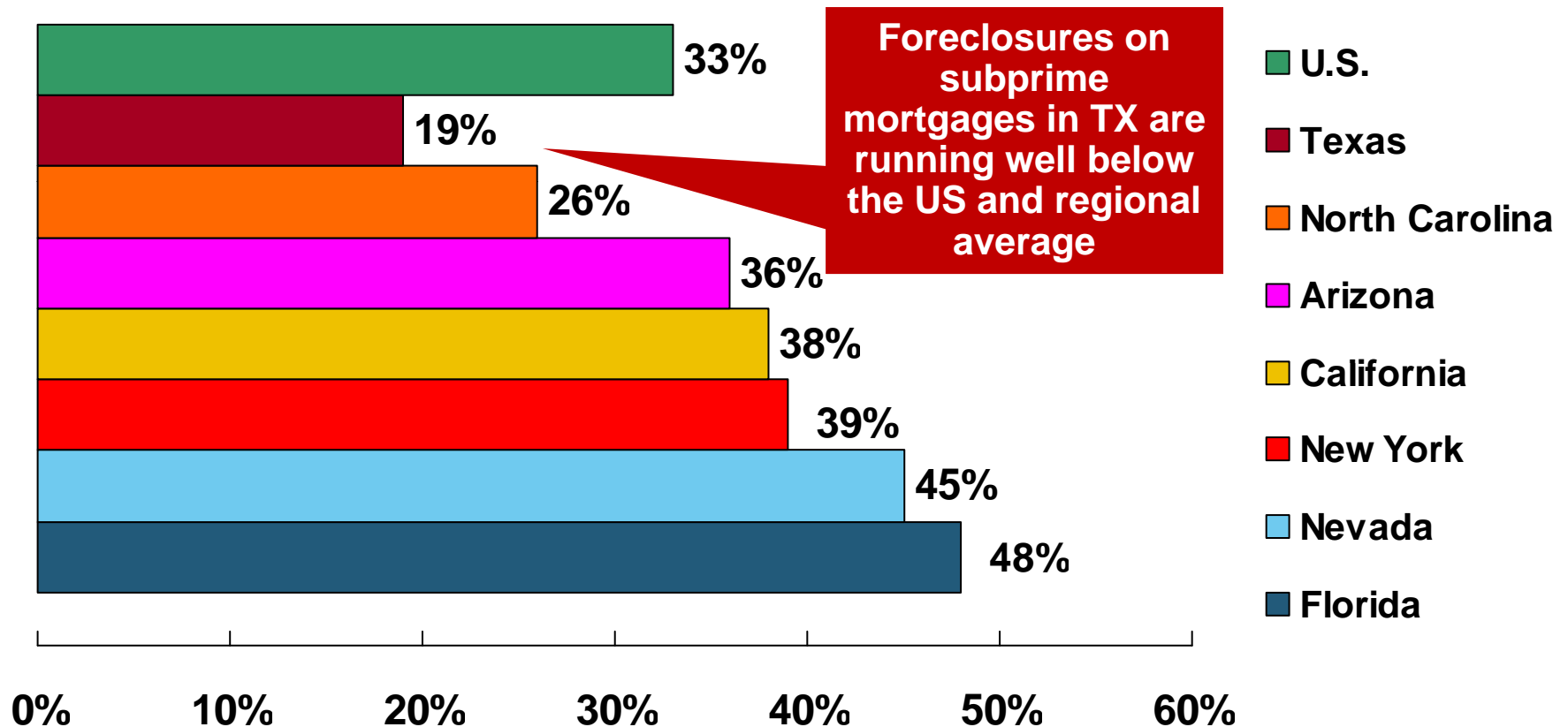
Workers Comp: 10-Year Average RNW TX & Nearby States

1999-2008



Source: NAIC, Insurance Information Institute

Percentage of Subprime Mortgages in Foreclosure, as of April 2010*



*Or at least 90 days delinquent

Source: New York Federal Reserve; Wall Street Journal, *Housing's Fragile States*, 06/30/10

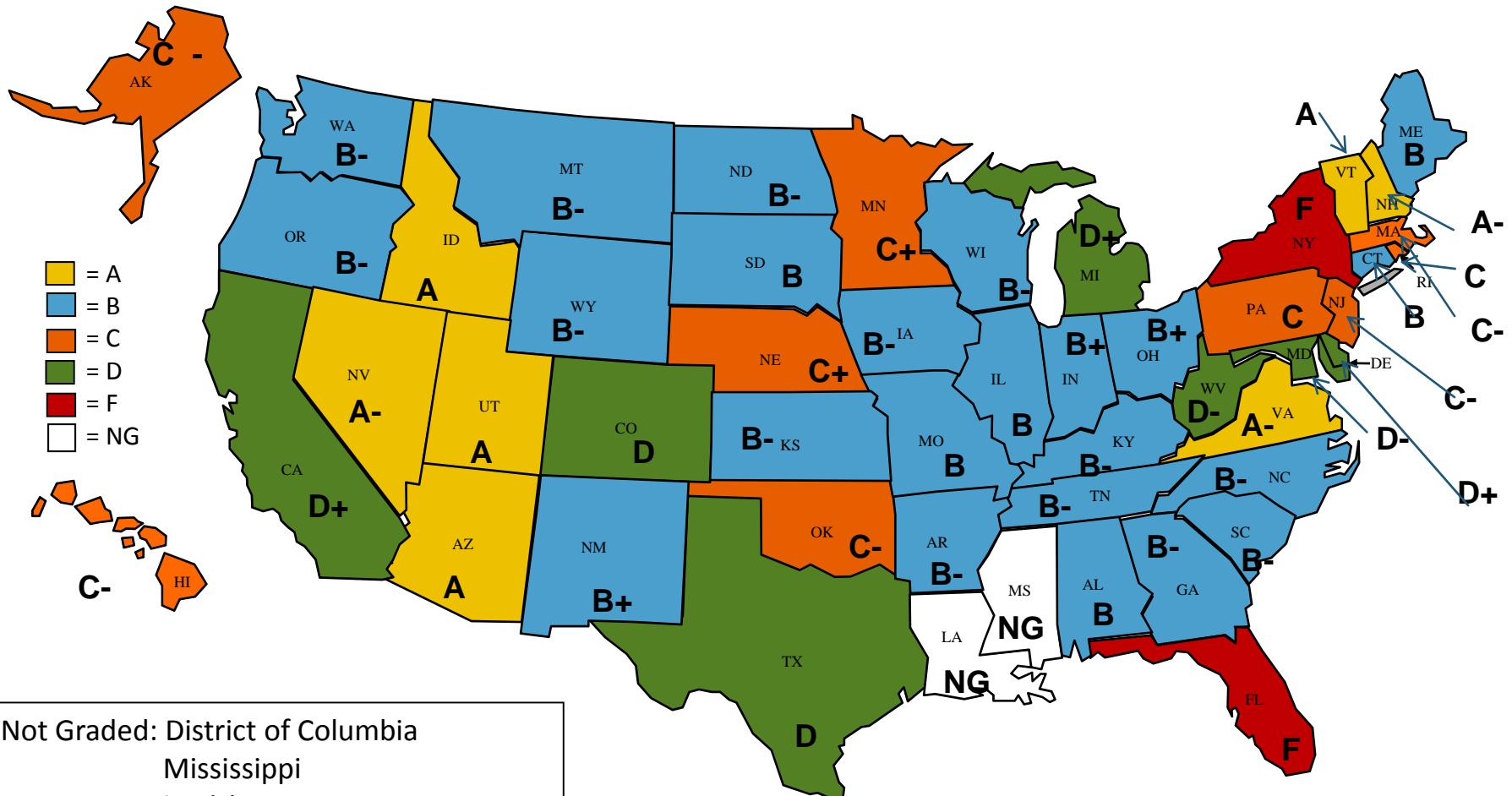
Financial Services Reform

**Insurers Are Impacted,
But Not Significantly**

Financial Services Reform: Impact on Insurers

- **Resolution Authority/Systemic Risk:** Regulators may seize and break-up troubled financial firms whose collapse might cause widespread damage (i.e., systemically important companies)
 - Regulator would recoup fees with more than \$50B in assets
 - Sets up liquidation procedure run by FDIC
 - Establishes 10-member oversight council to monitor and address risks to financial stability
 - Eliminates Office of Thrift Supervision (regulator of AIG's holding company, not its insurance units which were (are) state regulated)
- **Volcker Rule:** Largely bars largest firms largest investment firms from trading with their own funds
 - Exempts insurers, asset managers and trust/custody banks, though Fed could impose Volcker Rule and capital standards on individual firms if warranted
- **Derivatives:** Requires routine derivatives to be traded on exchanges and routed through clearinghouses
 - Imposes capital, margin, reporting and record keeping and business conduct rules on firms that deal in derivatives
- **Consumer Financial Protection Bureau:** To be housed within Fed
 - Will be limited to banks/creditors
- **Office of National Insurance:** To be established within Treasury to monitor and gather information in the insurance industry

2010 Property and Casualty Insurance Report Card



Critical Differences Between P/C Insurers and Banks

**Superior Risk Management Model and
Low Leverage Make a Big Difference**

How P/C Insurance Industry Stability Has Benefitted Consumers

Bottom Line:

- Insurance markets – unlike banking – are operating **normally**
- The basic function of insurance – the orderly transfer of risk from client to insurer – **continues uninterrupted**
- This means that insurers continue to:
 - ◆ Pay claims (whereas 258 banks have gone under as of 7/9/10)
 - **The promise is being fulfilled**
 - ◆ Renew existing policies (*banks are reducing and eliminating lines of credit*)
 - ◆ Write new policies (*banks are turning away people and businesses who want or need to borrow*)
 - ◆ Develop new products (*banks are scaling back the products they offer*)
 - ◆ Compete intensively (*banks are consolidating, reducing consumer choice*)

Reasons Why P/C Insurers Have Fewer Problems Than Banks

A Superior Risk Management Model

■ Emphasis on Underwriting

- ◆ Matching of risk to price (via experience and modeling)
- ◆ Limiting of potential loss exposure
- ◆ *Some banks sought to maximize volume and fees and disregarded risk*

■ Strong Relationship Between Underwriting and Risk Bearing

- ◆ **Insurers always maintain a stake in the business they underwrite, keeping “skin in the game” at all times**
- ◆ *Banks and investment banks package up and securitize, severing the link between risk underwriting and risk bearing, with (predictably) disastrous consequences – straightforward moral hazard problem from Econ 101*

■ Low Leverage

- ◆ Insurers do not rely on borrowed money to underwrite insurance or pay claims → ***There is no credit or liquidity crisis in the insurance industry***

■ Conservative Investment Philosophy

- ◆ High quality portfolio that is relatively less volatile and more liquid

■ Comprehensive Regulation of Insurance Operations

- ◆ The business of insurance remained comprehensively regulated whereas a separate banking system had evolved largely outside the auspices and understanding of regulators (e.g., hedge funds, private equity, complex securitized instruments, credit derivatives – CDS's)

■ Greater Transparency

- ◆ Insurance companies are an open book to regulators and the public

Obama Administration Proposal to Scale Back Terrorism Risk Insurance Program

5 Administration's Budget Proposal for FY 2011:

- Includes proposal to scale back federal support for terrorism risk insurance program
- Proposal projects savings of \$249 million from 2011-2020
- Administration's justification is that this would "encourage the private sector to better mitigate terrorism risk through other means, such as developing alternative reinsurance options and building safer buildings."

Key Concerns

Among Industry Observers Over Proposed Reduction in Federal Support

- Suggestion of changes to law would have detrimental effect on availability and affordability of terrorism insurance
- A 2009 Aon study estimated some 70-80 percent of the commercial property insurance market would revert to absolute exclusions for terrorism, if TRIA is changed.

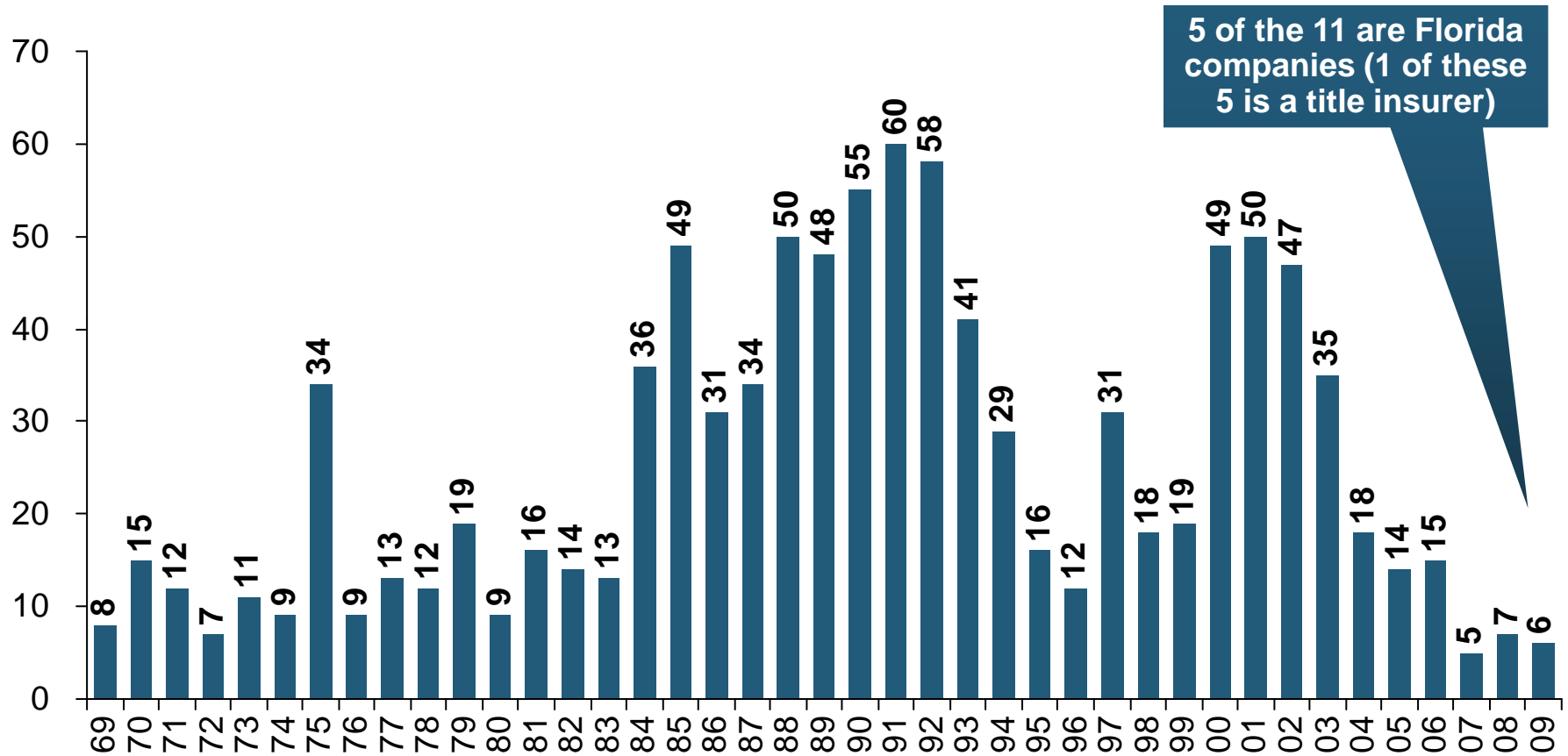
Reasons Why Concerns Are Mounting in 2010

- Perception (Reality) that U.S. vulnerability is rising
- Thwarted Christmas Day attack by “underwear bomber”
 - And new bin Laden tape claiming al Qaeda is responsible
- Foiled NYC Subway Bomber Plot (Zazi case)
- *Failed Times Square Car Bombing on May 1*
- Trials of Guantanamo 9/11 suspects in Manhattan Court (?)
- U.K. in January Raised Terror Alert Status to 2nd Highest Level
- Increased anti-terror efforts, including full-body scans
- Effort by government to appear more vigilant, prepared
- Rise of groups such al Qaeda in the Arabian Peninsula
- U.S. military surge in Afghanistan operations
- Most buyers/producers haven’t thought about coverage recently
- *Obama Administration’s Intent to Reduce Support for TRIA*

Financial Strength & Ratings

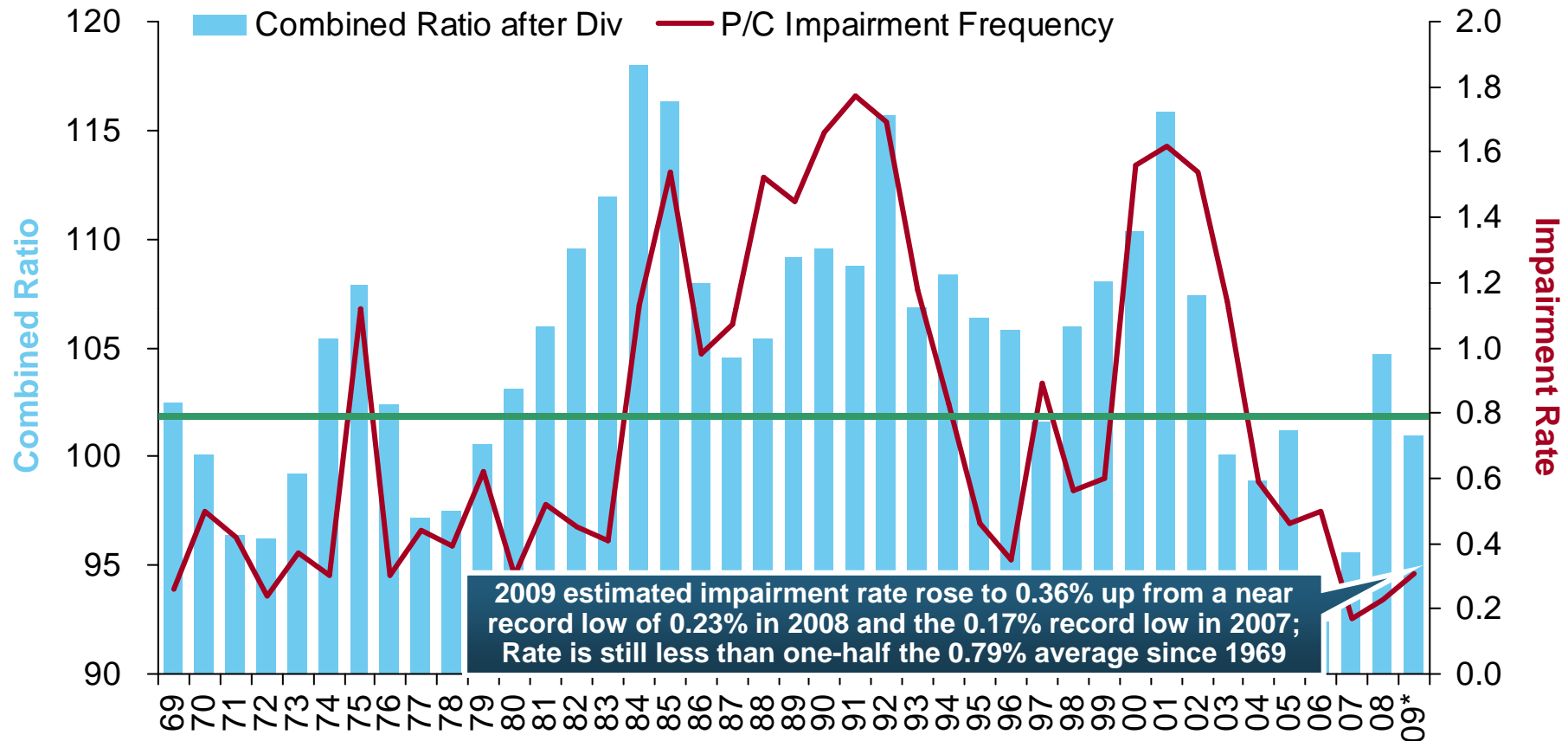
**Industry Has Weathered
the Storms Well**

P/C Insurer Impairments, 1969–2009



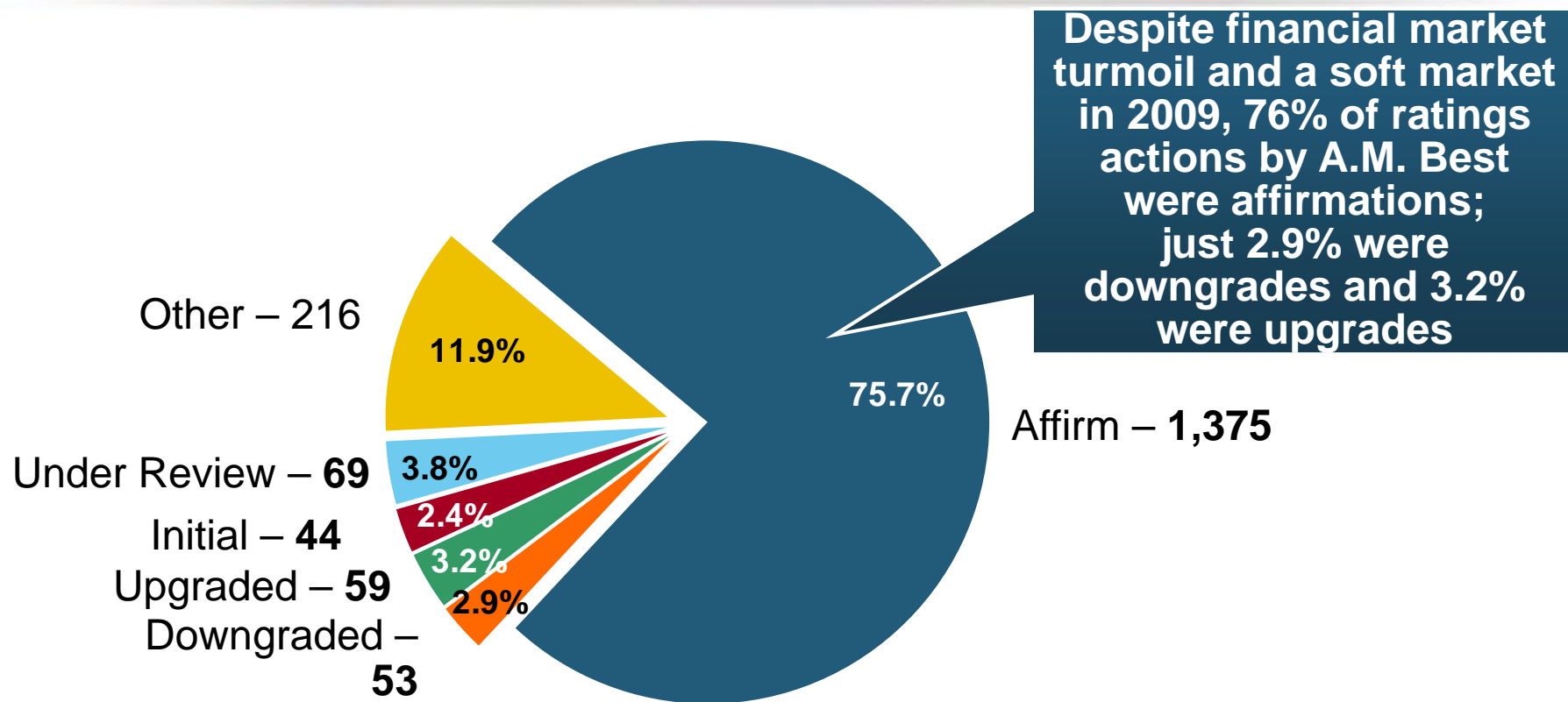
The Number of Impairments Varies Significantly Over the P/C Insurance Cycle, With Peaks Occurring Well into Hard Markets

P/C Insurer Impairment Frequency vs. Combined Ratio, 1969-2009



Impairment Rates Are Highly Correlated With Underwriting Performance and Reached Record Lows in 2007/08

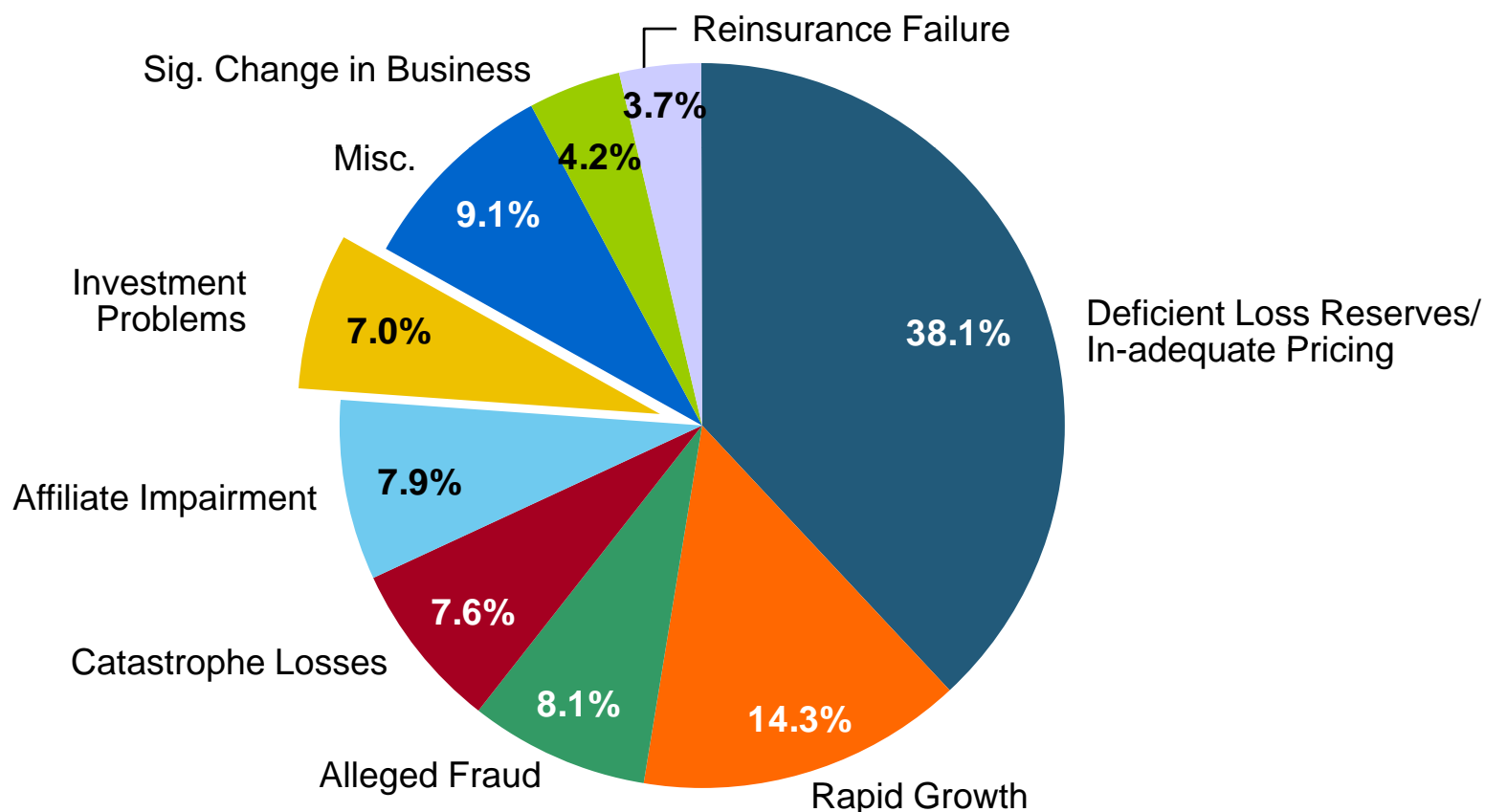
Summary of A.M. Best's P/C Insurer Ratings Actions in 2009



**P/C Insurance is by Design a Resilient Business.
The Dual Threat of Financial Disasters and Catastrophic Losses
Are Anticipated in the Industry's Risk Management Strategy**

Reasons for US P/C Insurer Impairments, 1969–2008

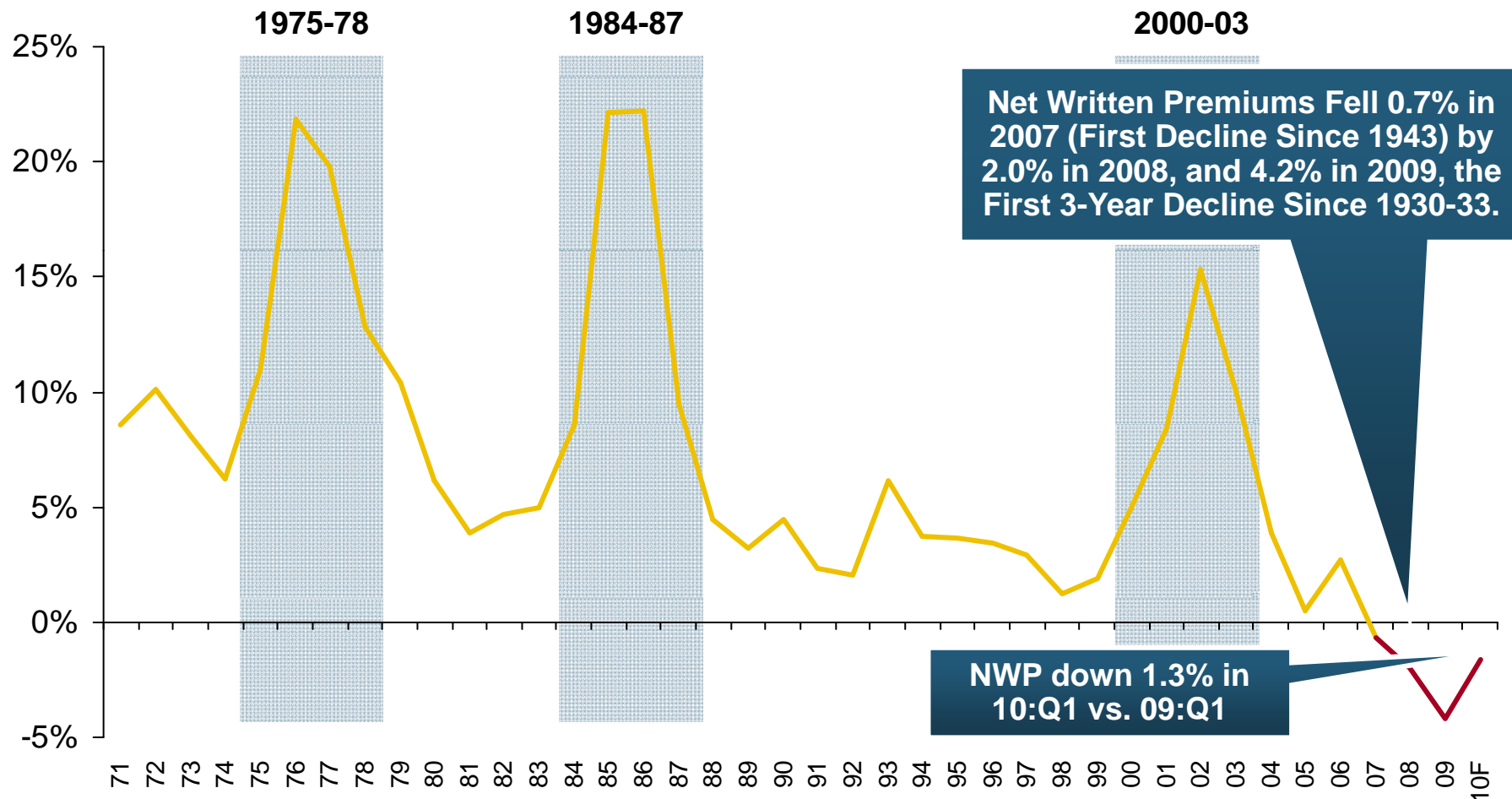
Deficient Loss Reserves and Inadequate Pricing Are the Leading Cause of Insurer Impairments, Underscoring the Importance of Discipline. Investment Catastrophe Losses Play a Much Smaller Role



**P/C Premium Growth
Primarily Driven by the
Industry's Underwriting Cycle,
Not the Economy**

Soft Market Appears to Persist in 2010. Relief in 2011?

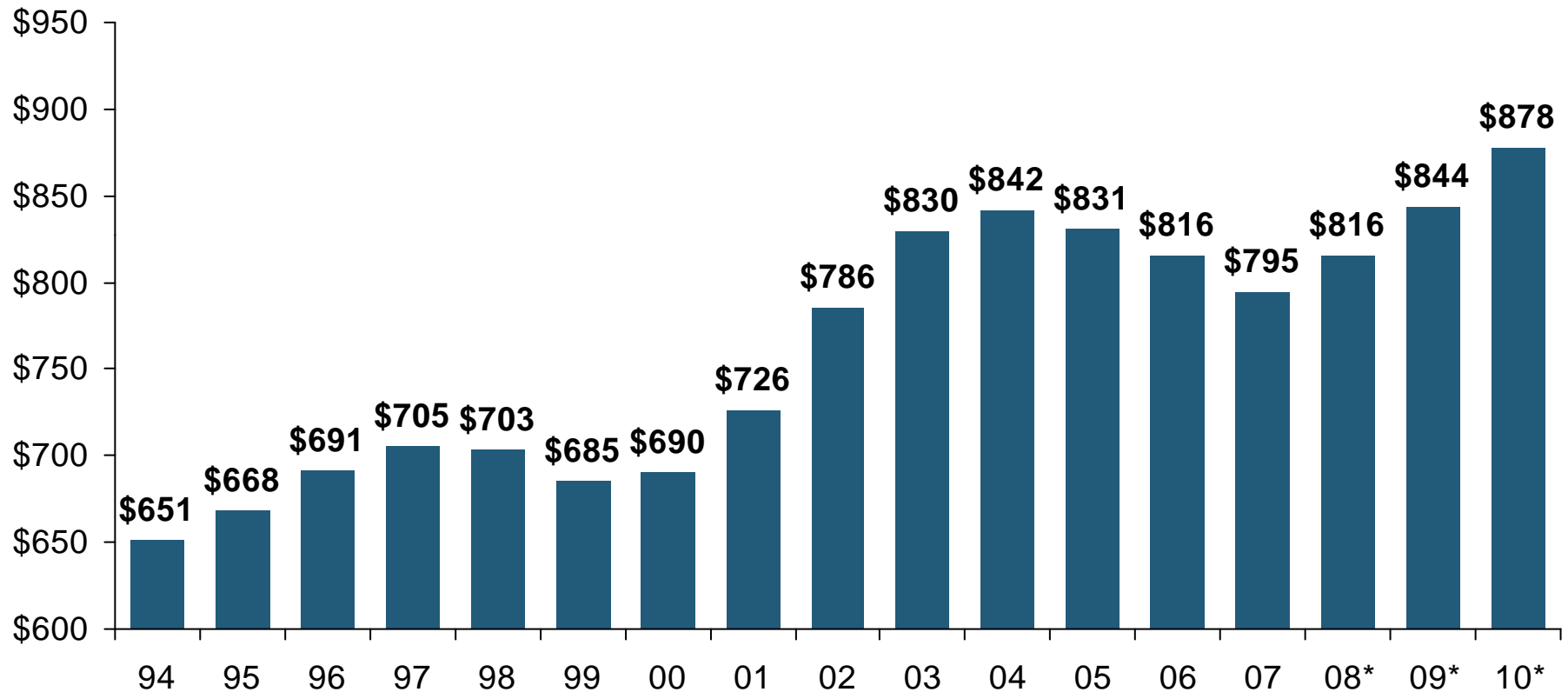
(Percent)



Shaded areas denote "hard market" periods

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

Average Expenditures on Auto Insurance



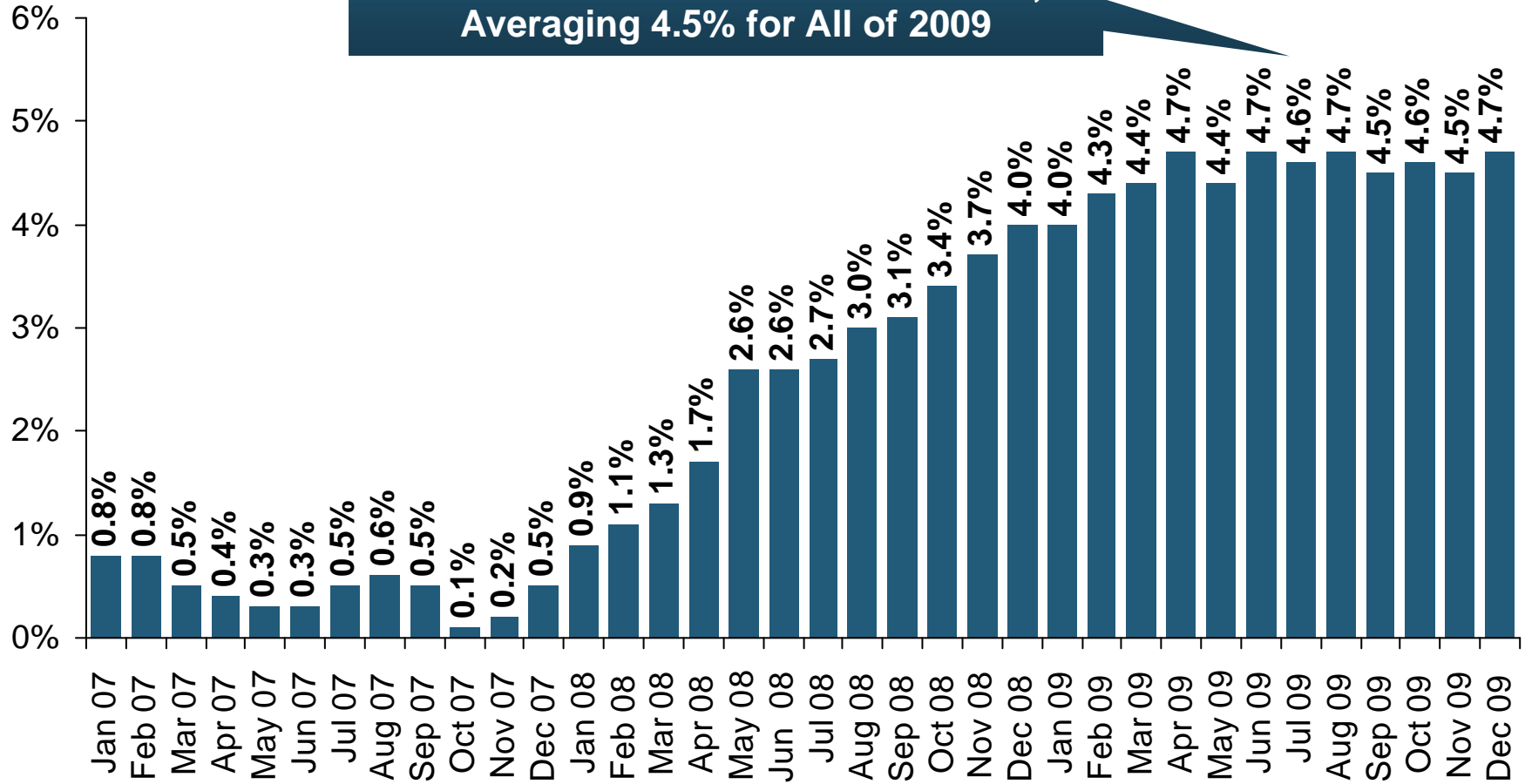
**Countrywide Auto Insurance Expenditures Increased
2.6% in 2008 and 3.5% Pace in 2009 (est.) and 4% in 2010 (est.)**

* Insurance Information Institute Estimates/Forecasts
Source: NAIC, Insurance Information Institute estimates 2008-2010 based on CPI data.

Monthly Change in Auto Insurance Prices*

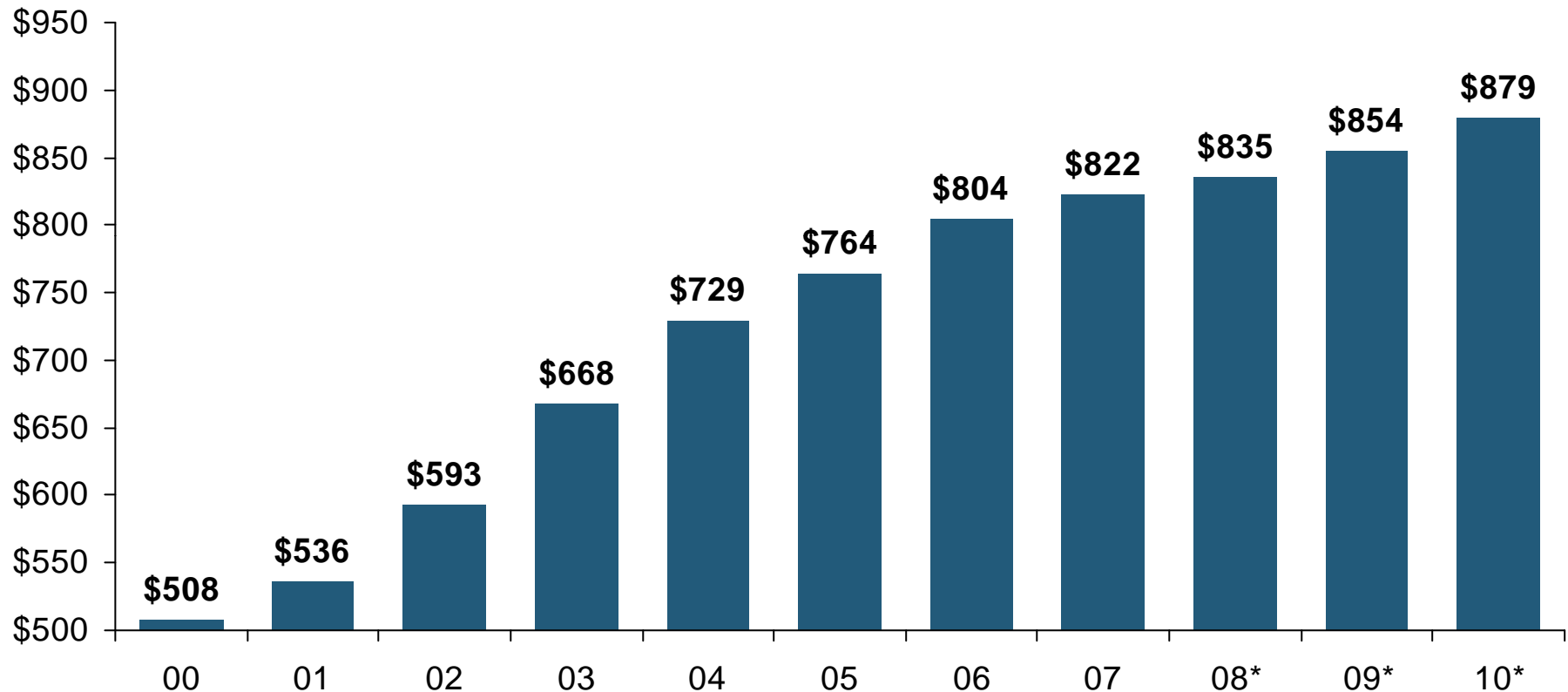
(Percent)

Auto Insurance Price Increases Seem to Have Levelled Off in Recent Months, Averaging 4.5% for All of 2009



* Percentage change from same month in prior year.
Source: US Bureau of Labor Statistics

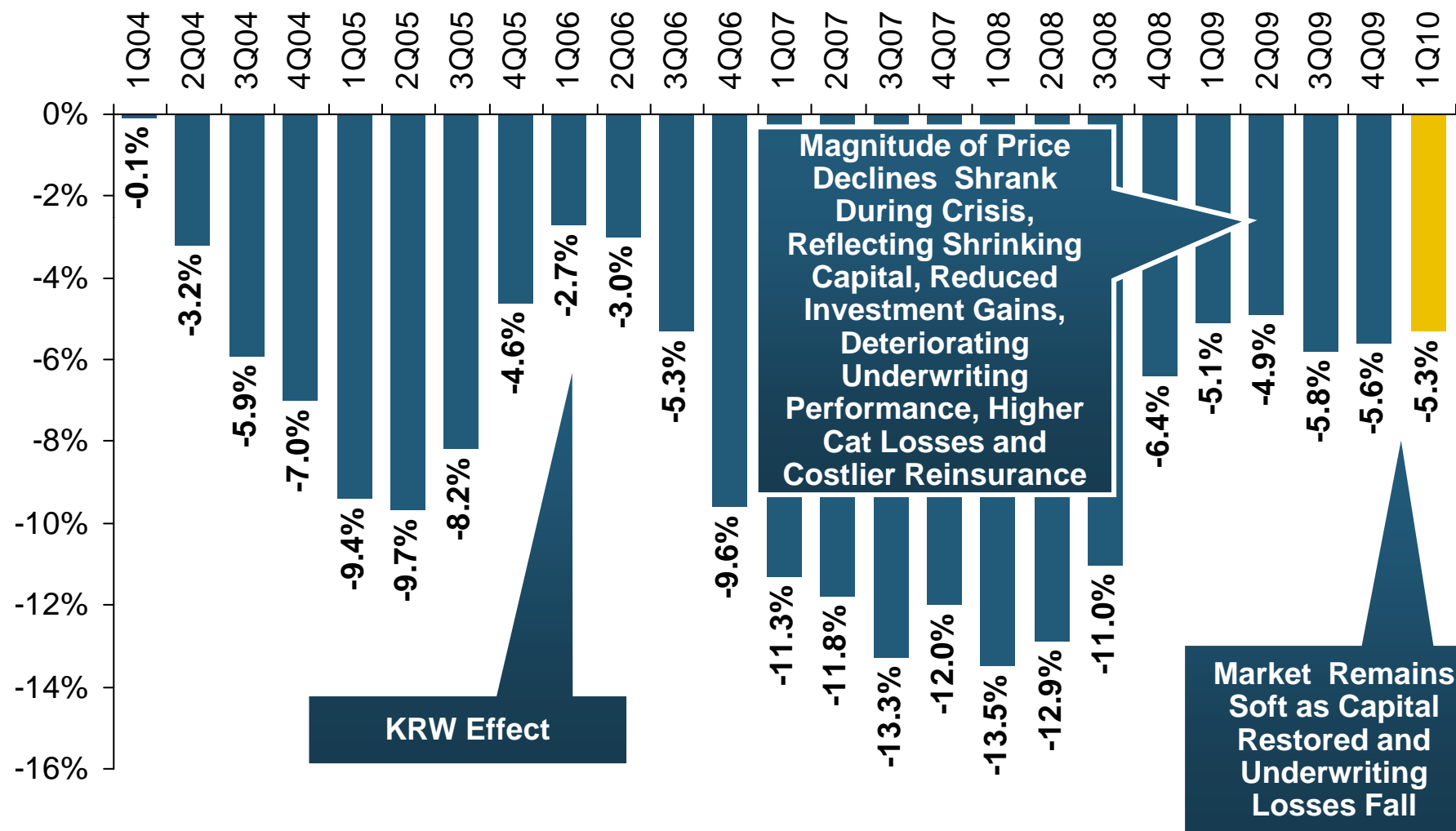
Average Premium for Home Insurance Policies**



* Insurance Information Institute Estimates/Forecasts **Excludes state-run insurers.
Source: NAIC, Insurance Information Institute estimates 2008-2010 based on CPI data.

Average Commercial Rate Change, All Lines, (1Q:2004–1Q:2010)

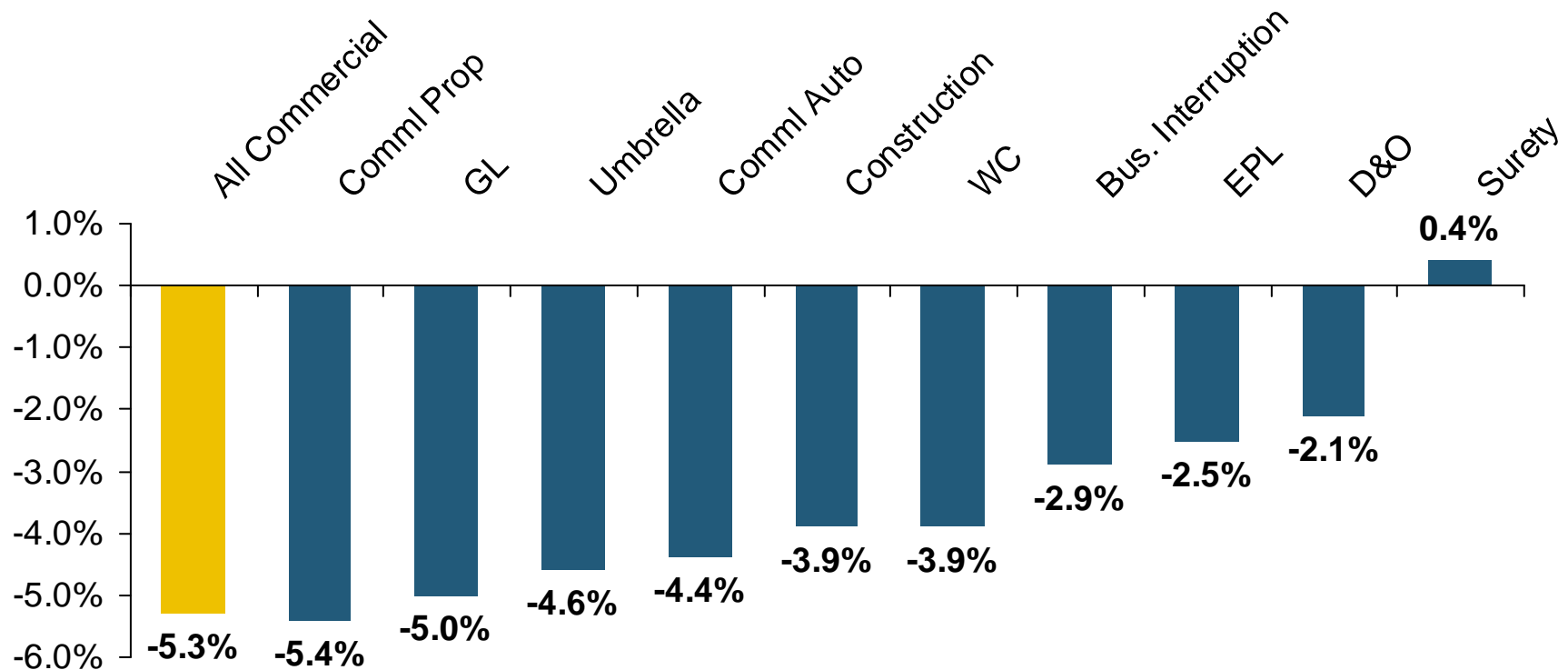
(Percent)



Source: Council of Insurance Agents & Brokers; Insurance Information Institute

Change in Commercial Rate Renewals, by Line: 2010:Q1

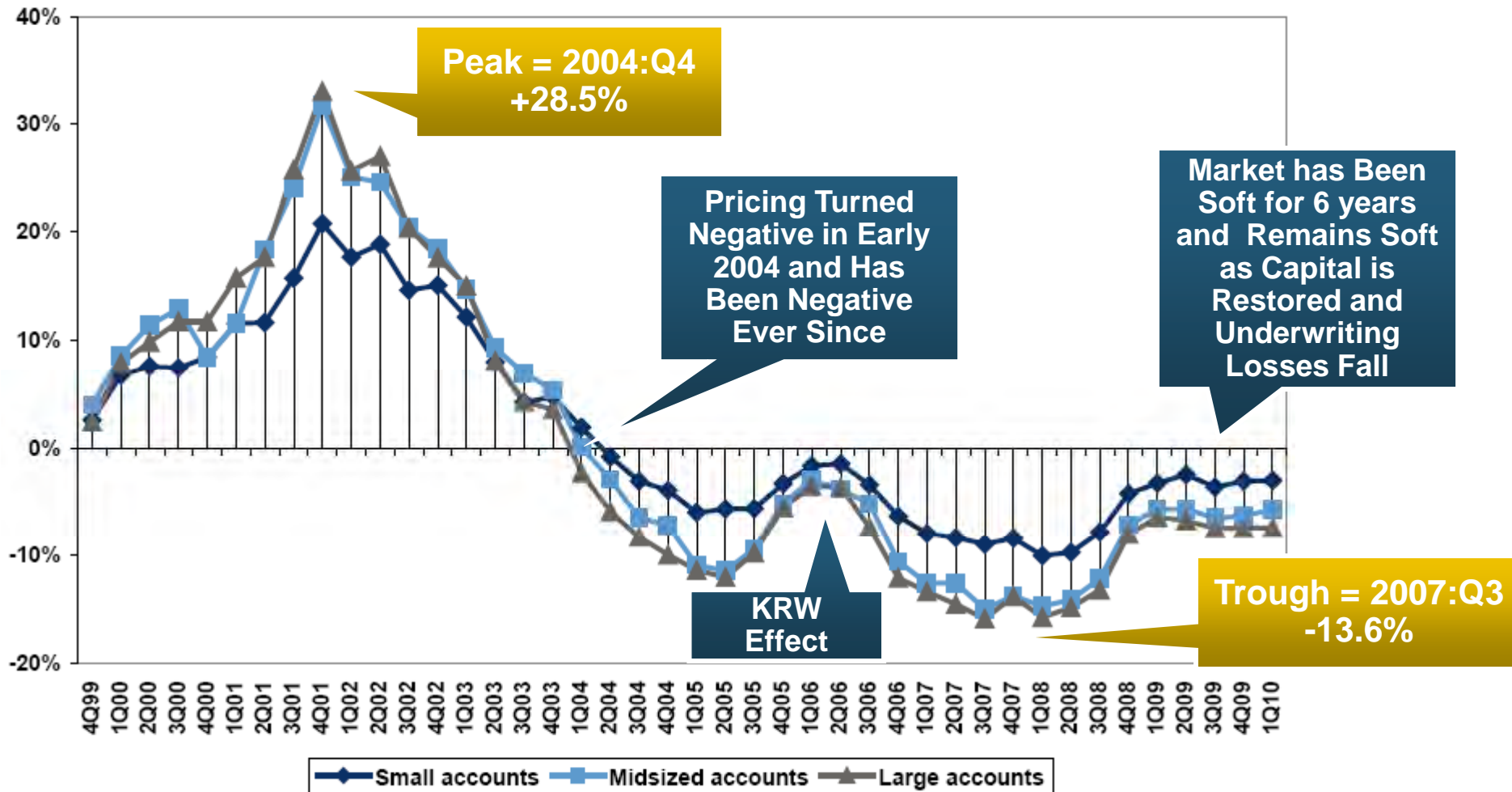
Percentage Change (%)



Most Major Commercial Lines Renewed Down in Q1:2010 by Roughly the Same Margin as a Year Earlier

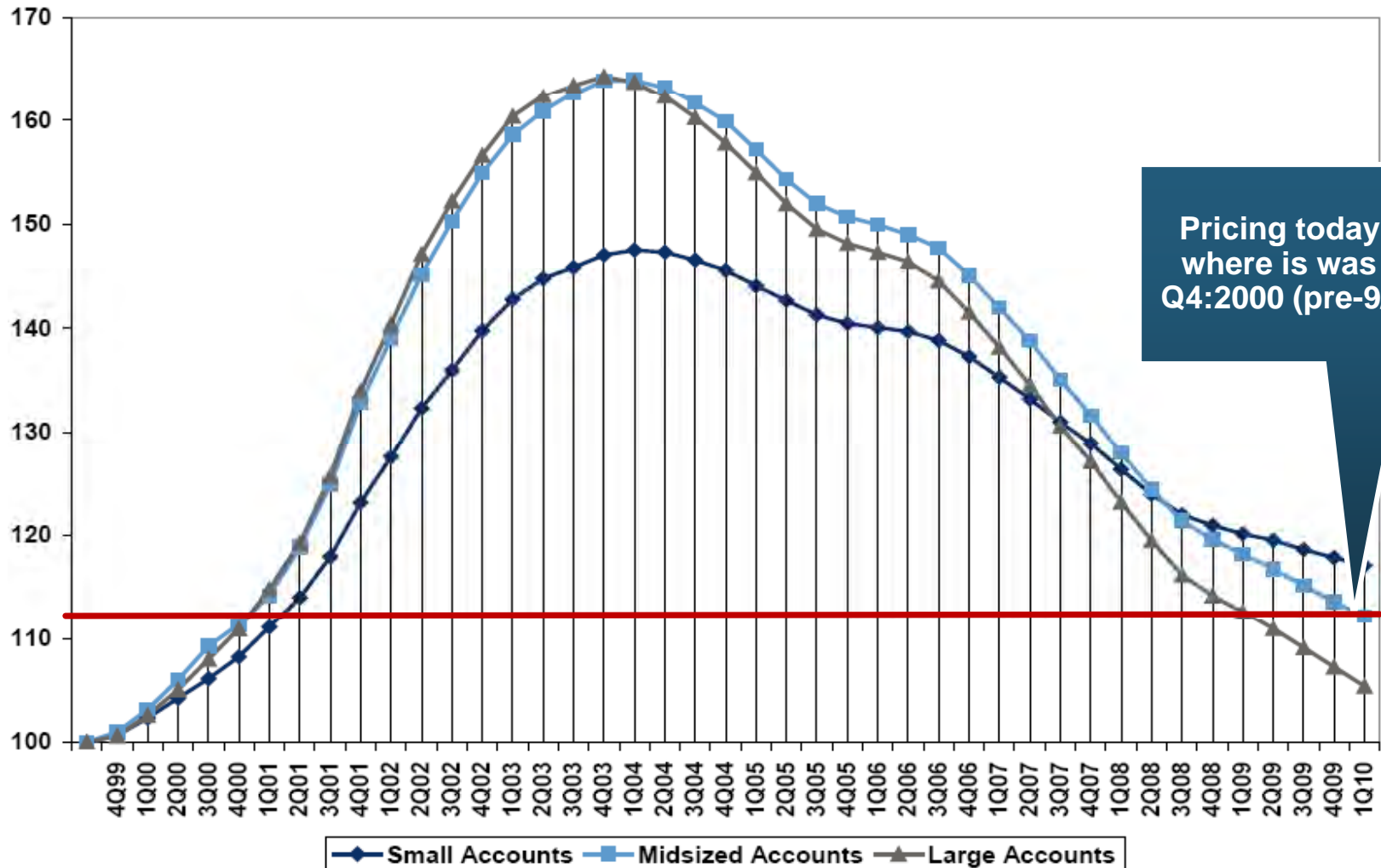
Change in Commercial Rate Renewals, by Account Size: 1999:Q4 to 2010:Q1

Percentage Change (%)



Cumulative Qtrly. Commercial Rate Changes, by Account Size: 1999:Q4 to 2010:Q1

1999:Q4 = 100



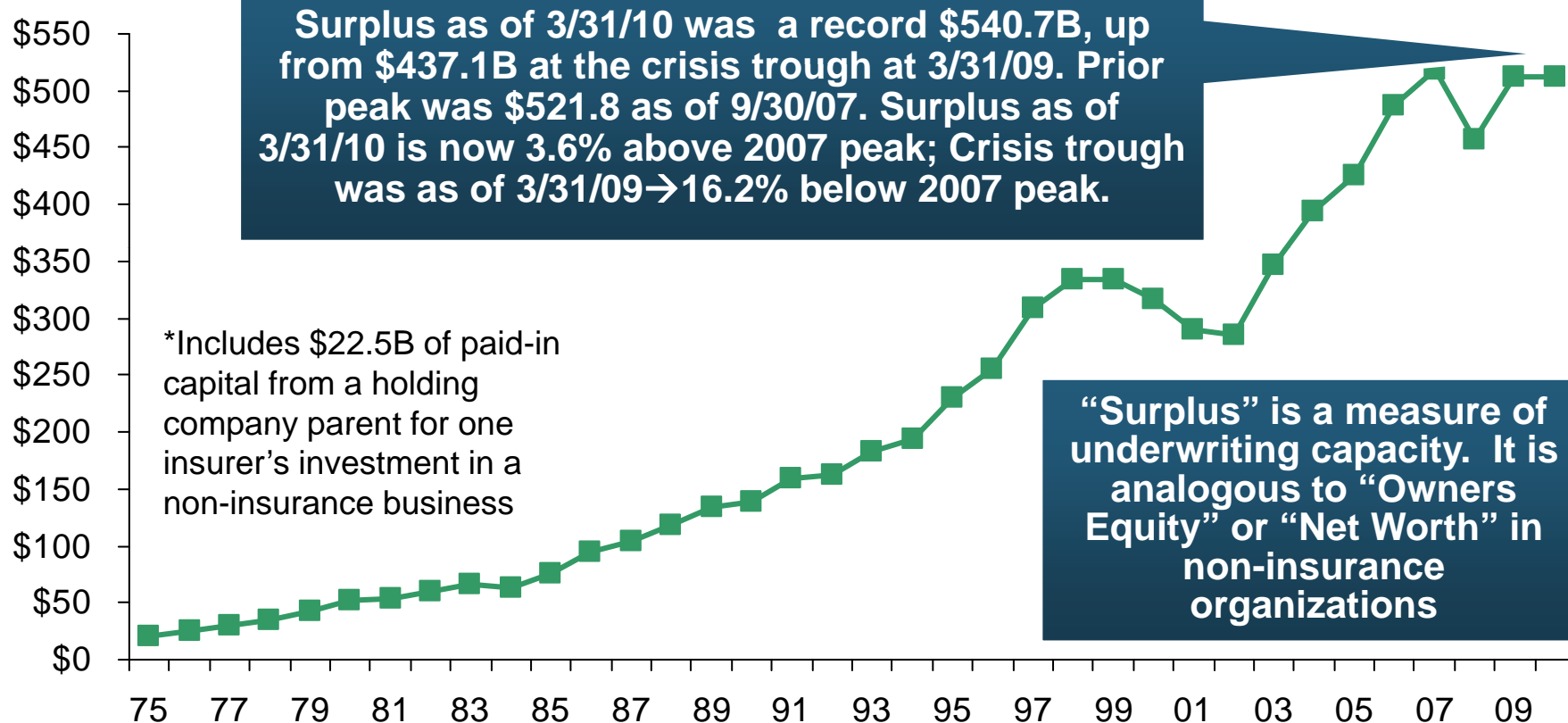
Pricing today is where it was in Q4:2000 (pre-9/11)

Capital/Policyholder Surplus (US)

**Shrinkage, but Not Enough
to Trigger Hard Market**

US Policyholder Surplus: 1975–2010*

(\$ Billions)

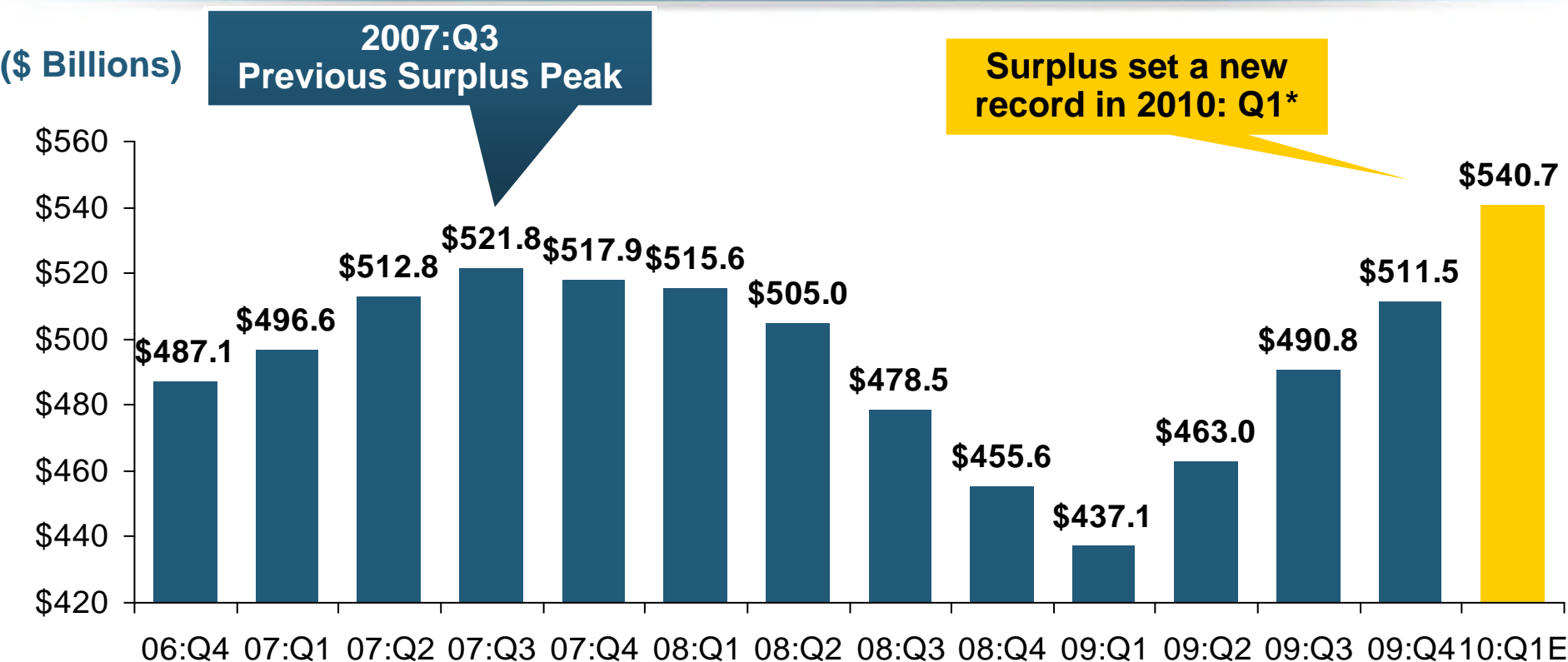


The Premium-to-Surplus Ratio Stood at \$0.82:\$1 as of 12/31/09, A Record Low (at Least in Recent History)

* As of 3/31/10

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

Policyholder Surplus, 2006:Q4–2010:Q1E



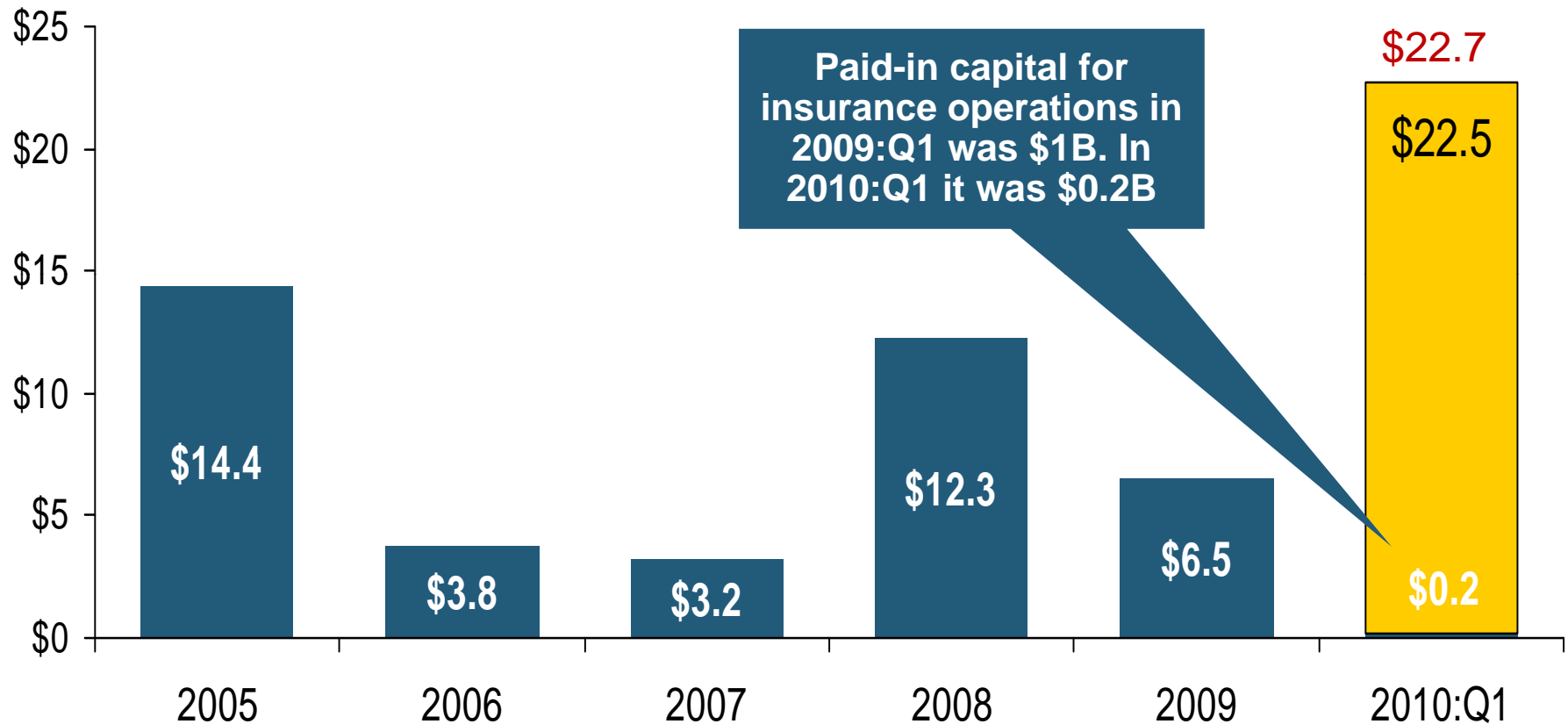
Quarterly Surplus Changes Since 2007:Q3 Peak

| | |
|---------------------------------|---------------------------------|
| 08:Q2: -\$16.6B (-3.2%) | 09:Q2: -\$58.8B (-11.2%) |
| 08:Q3: -\$43.3B (-8.3%) | 09:Q3: -\$31.8B (-5.9%) |
| 08:Q4: -\$66.2B (-12.9%) | 09:Q4: -\$10.3B (-2.0%) |
| 09:Q1: -\$84.7B (-16.2%) | 10:Q1: +\$18.9B (+3.6%) |

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

Paid-in Capital, 2005–2010:Q1

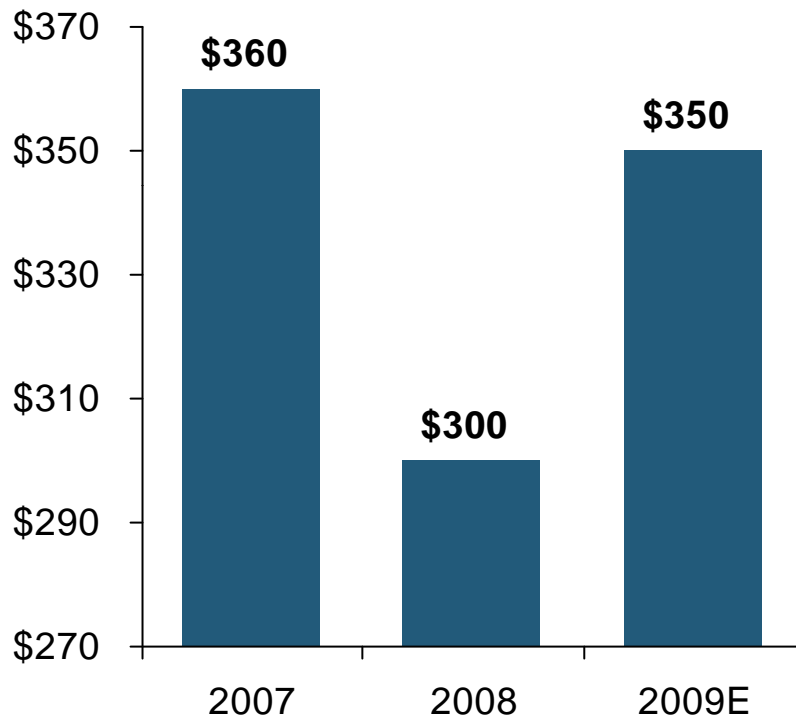
(\$ Billions)



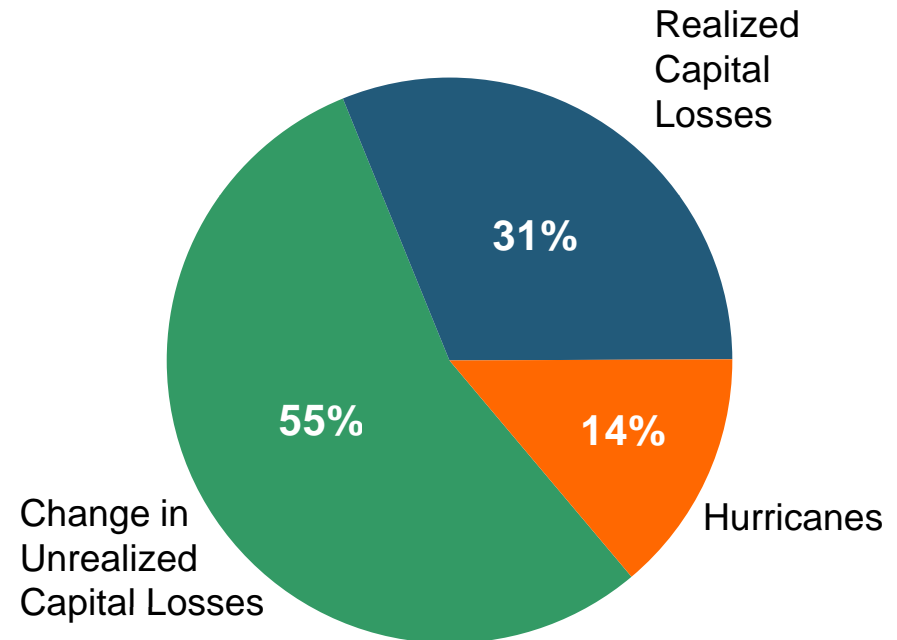
In 2010:Q1 One Insurer's Paid-in Capital Rose by \$22.5B as Part of an Investment in a Non-insurance Business

Global Reinsurance Capacity Shrank in 2008, Mostly Due to Investments

Global Reinsurance Capacity



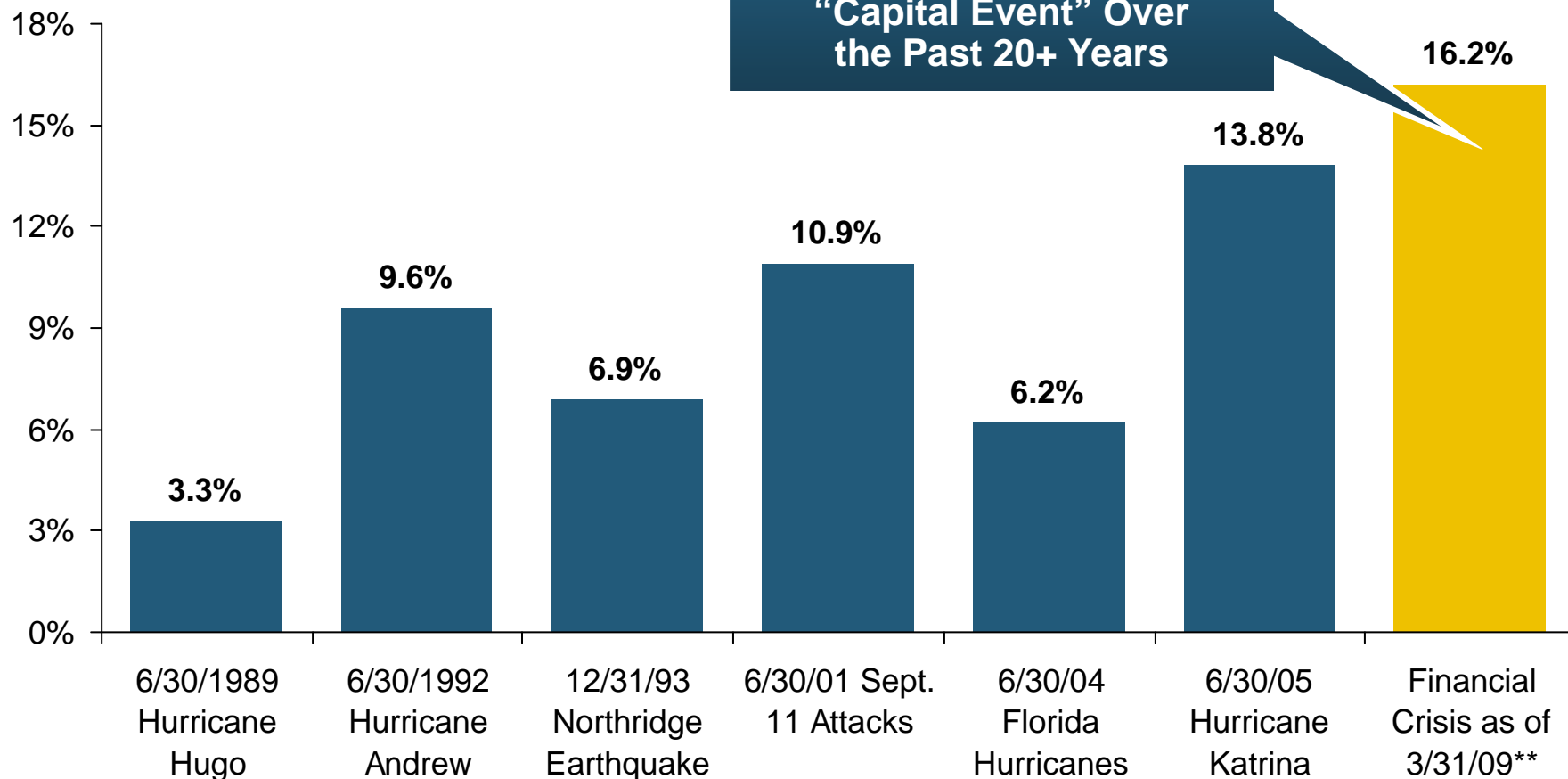
Source of Decline in 2008



**Global Reinsurance Capacity
Fell by an Estimated 17% in 2008**

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

(Percent)

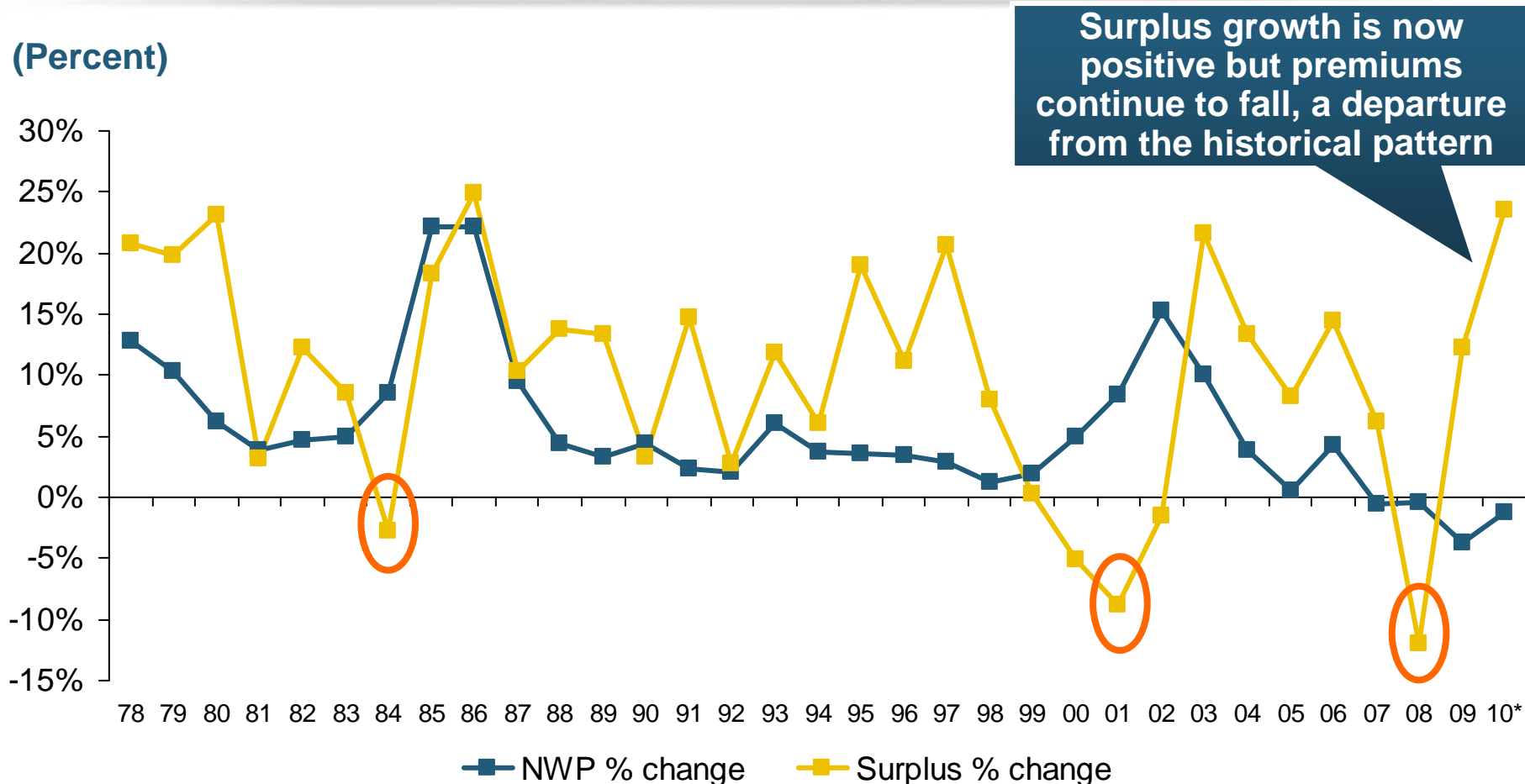


* Ratio is for end-of-quarter surplus immediately prior to event. Date shown is end of quarter prior to event

** 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*



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

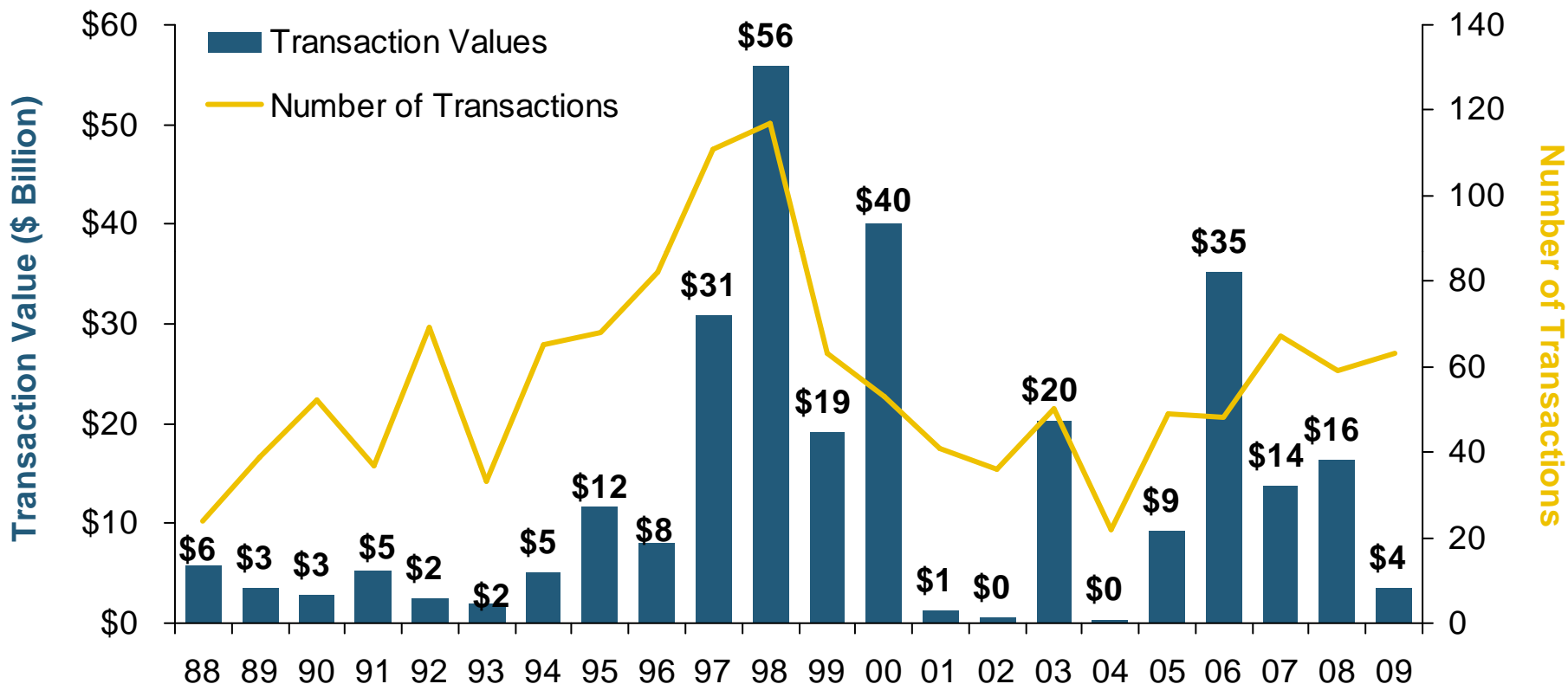
* 2010 NWP and Surplus figures are % changes as of Q1:10 vs Q1:09. Adjusting for unique transaction of insurer the increase is 18.4%.

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

Merger & Acquisition

**Barriers to Consolidation Will
Diminish in 2010**

U.S. P/C Insurance-Related M&A Activity, 1988–2009



**\$ Value of Deals Down 78%
in 2009, Volume Up 7%**

**2010: No Mega Deals So Far, Despite
Record Capital, Slow Growth and Improved
Financial Market Conditions**

Note: U.S. Company was the acquirer and/or target.

Source: Conning Research & Consulting.

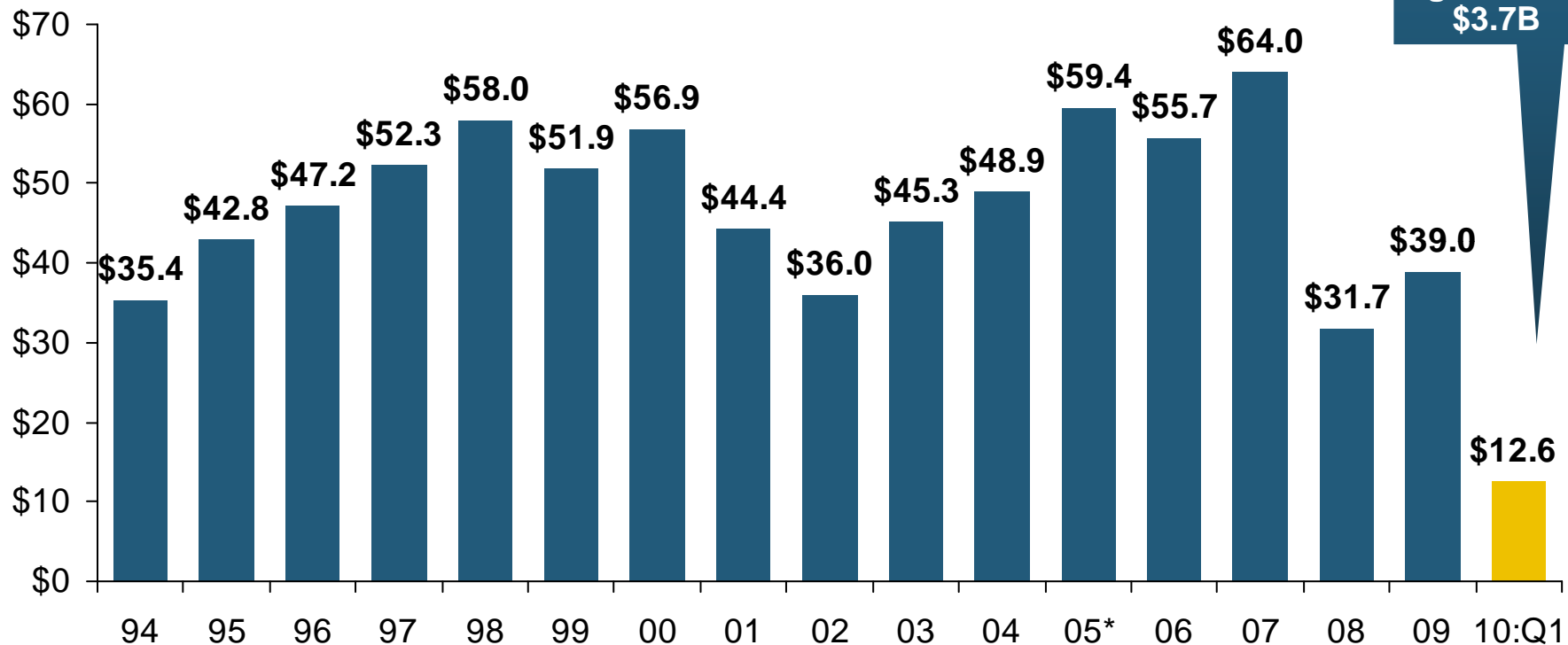


Investment Performance

**Investments Are a Principle
Source of Declining Profitability**

Property/Casualty Insurance Industry Investment Gain: 1994–2010:Q1¹

(\$ Billions)



**In 2008, Investment Gains Fell by 50% Due to Lower Yields and
Nearly \$20B of Realized Capital Losses
2009 Saw Smaller Realized Capital Losses But Declining Investment Income**

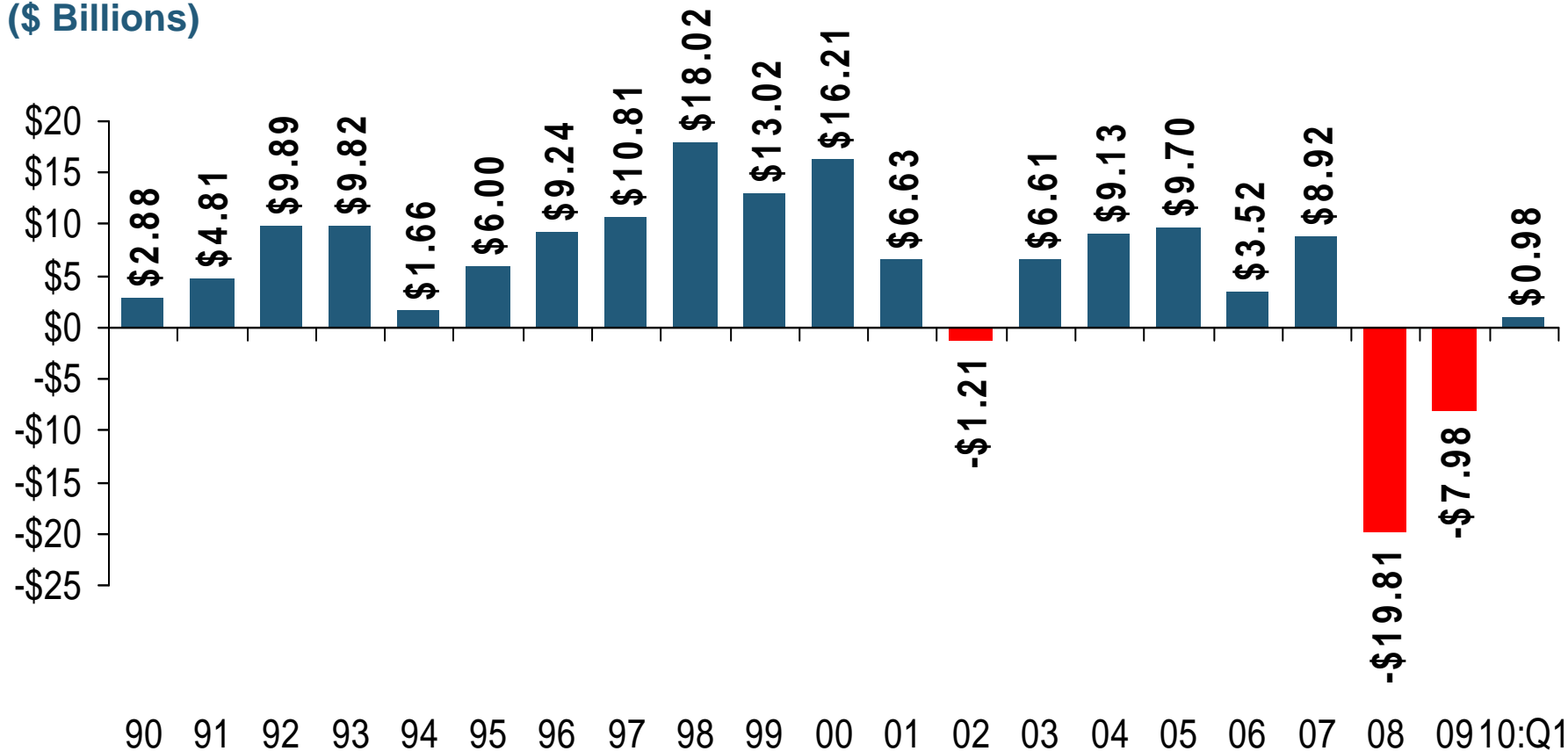
¹ Investment gains consist primarily of interest, stock dividends and realized capital gains and losses.

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

Sources: ISO; Insurance Information Institute.

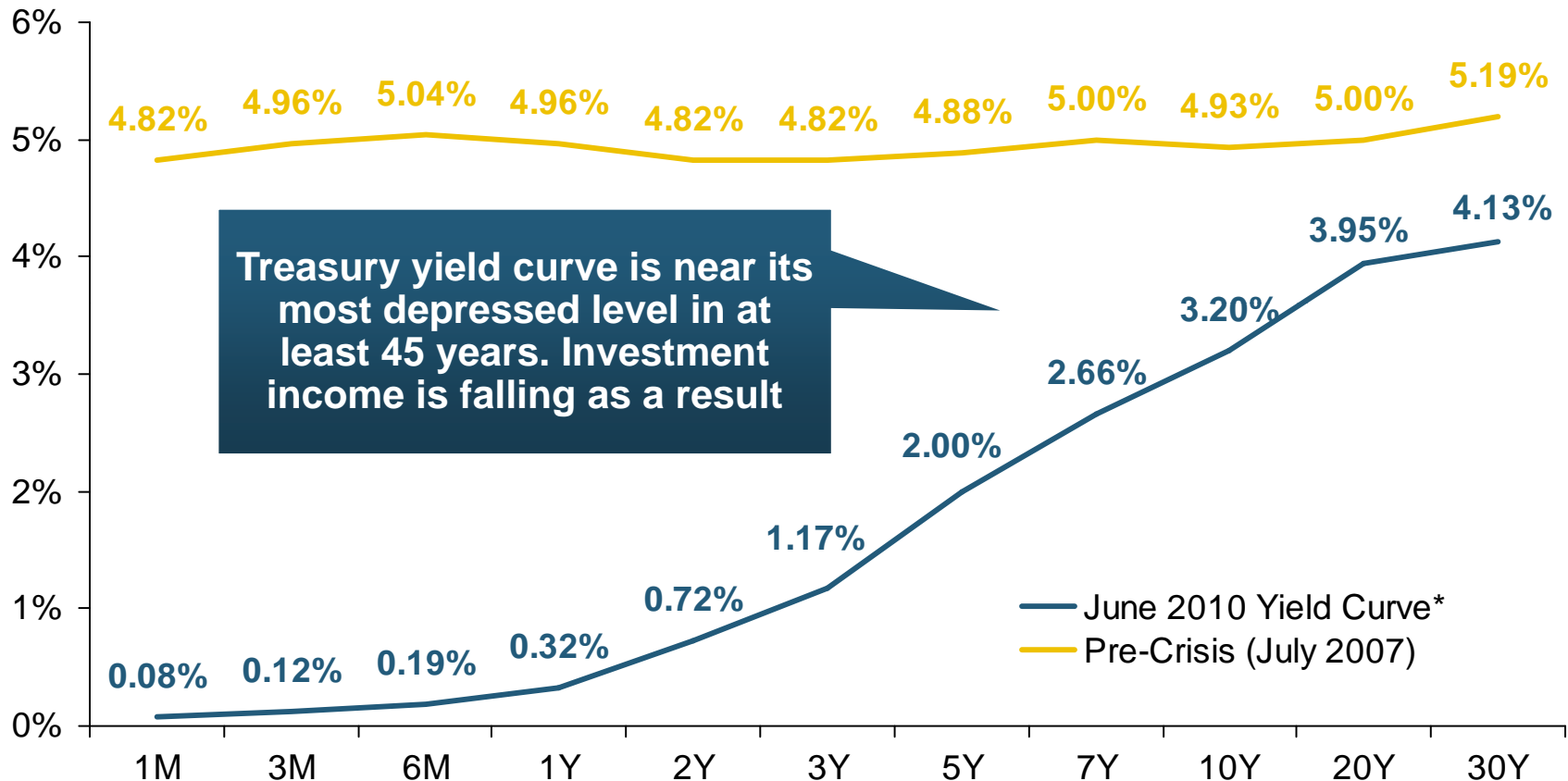
P/C Insurer Net Realized Capital Gains, 1990-2010:Q1

(\$ Billions)



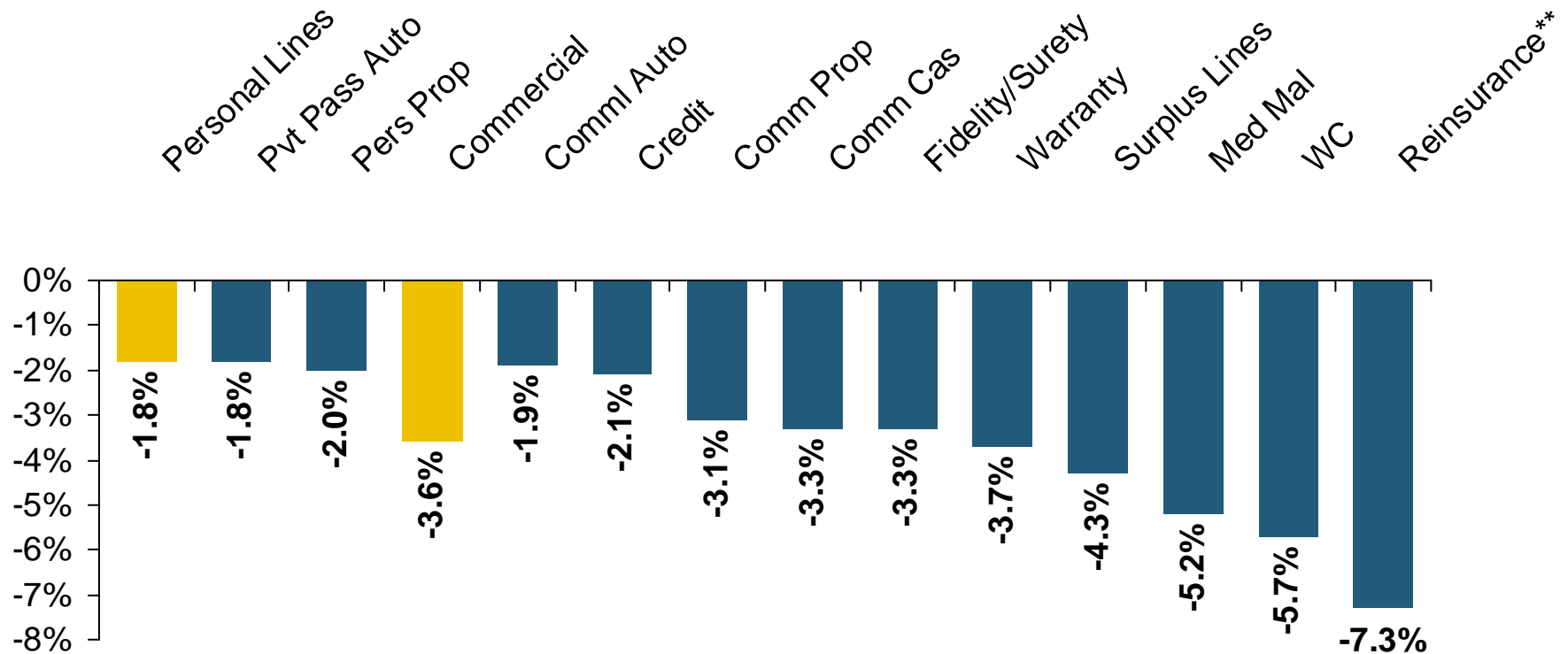
**Realized Capital Losses Were the Primary Cause
of 2008/2009's Large Drop in Profits and ROE**

Treasury Yield Curves: Pre-Crisis (July 2007) vs. June 2010



Stock Dividend Cuts Have Further Pressured Investment Income

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

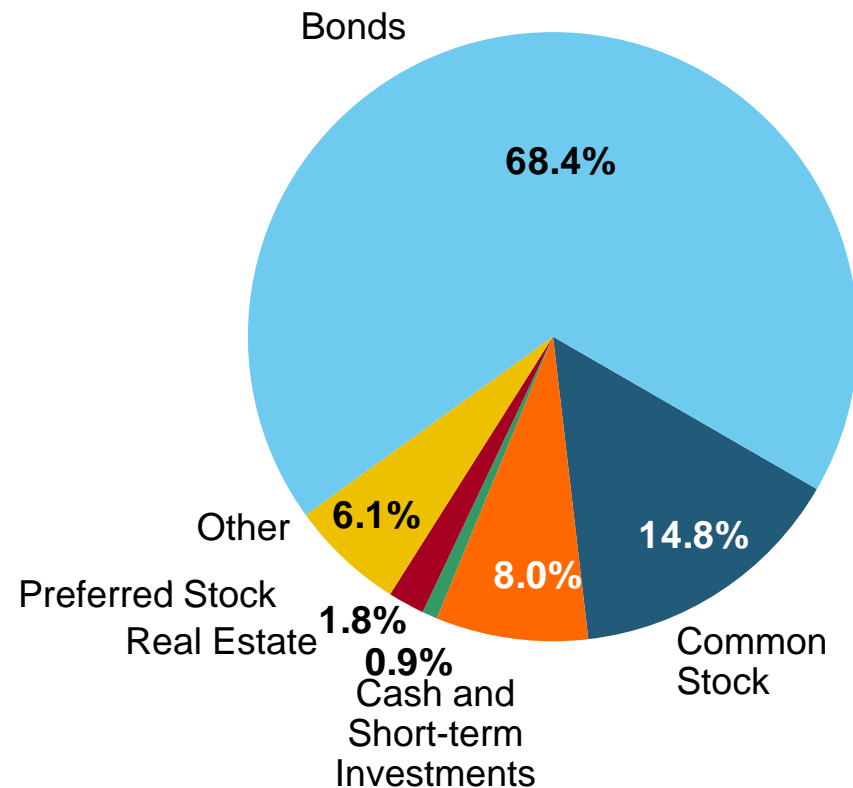
Source: A.M. Best; Insurance Information Institute.

Distribution of P/C Insurance Industry's Investment Portfolio

Portfolio Facts

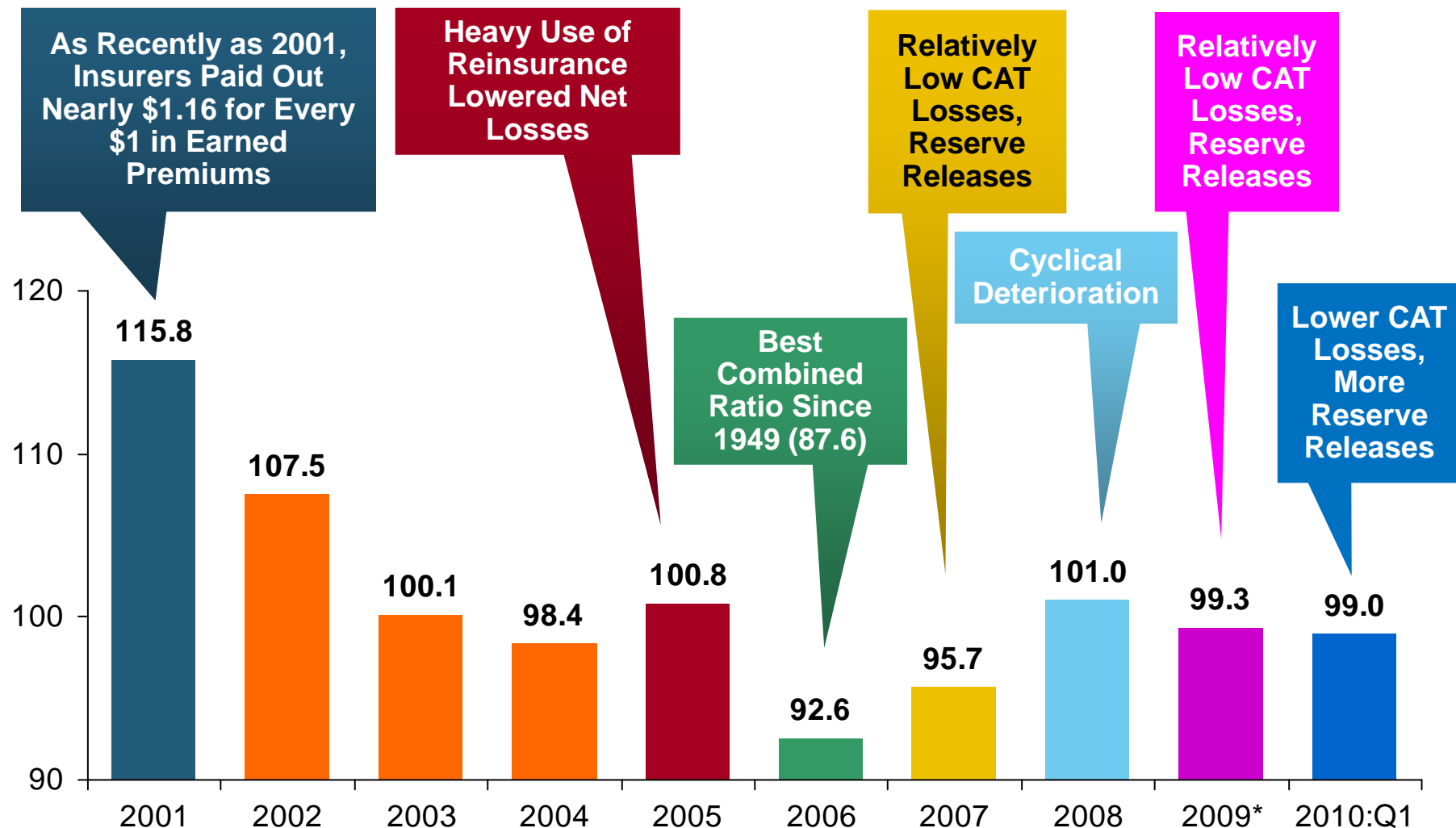
- Invested assets totaled \$1.214 trillion as of 12/31/08
- Insurers are generally conservatively invested, with more than 2/3 of assets invested in bonds as of 12/31/08
- Only about 15% of assets were invested in common stock as of 12/31/08
- Even the most conservative of portfolios was hit hard in 2008

As of December 31, 2008



**Underwriting Trends –
Financial Crisis Does *Not*
Directly Impact Underwriting
Performance: Cycle, Catastrophes
Were 2008's Drivers**

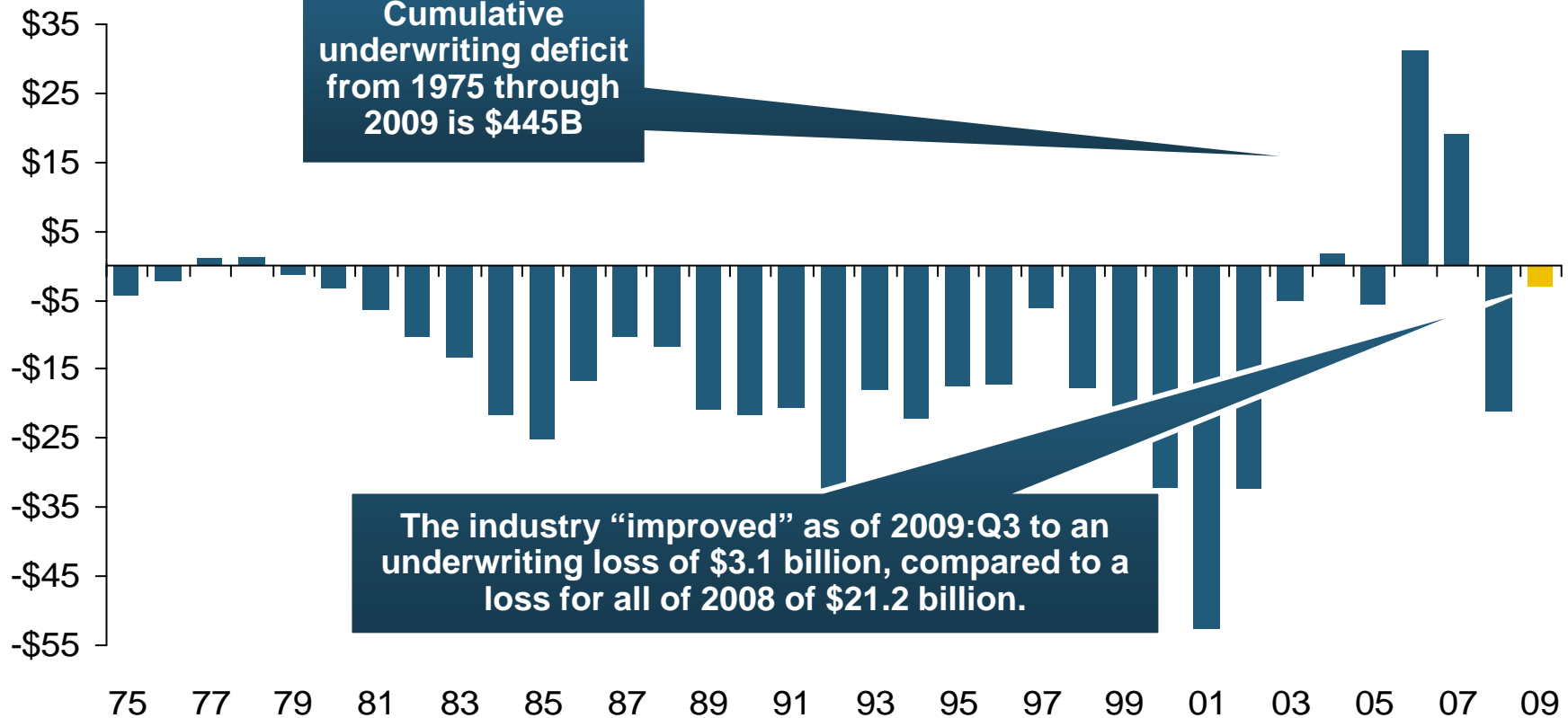
P/C Insurance Industry Combined Ratio, 2001–2010:Q1*



* Excludes Mortgage & Financial Guaranty insurers in 2008, 2009 and 2010. Including M&FG, 2008=105.1, 2009=100.7, 2010:Q1=101.1
Sources: A.M. Best, ISO.

Underwriting Gain (Loss) 1975–2009*

(\$ Billions)

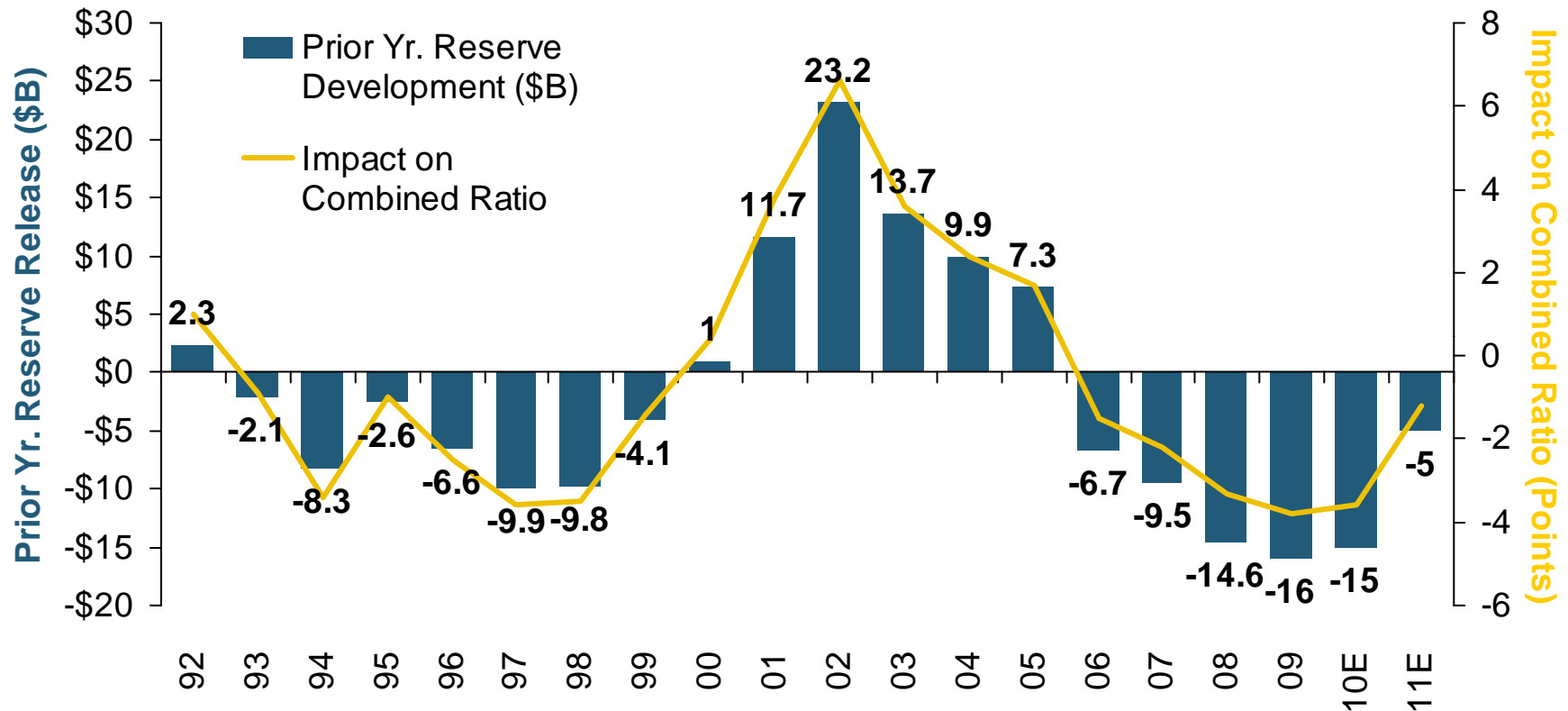


**Large Underwriting Losses Are *NOT* Sustainable
in Current Investment Environment**

* Includes mortgage and financial guarantee insurers.

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

P/C Reserve Development, 1992–2011E

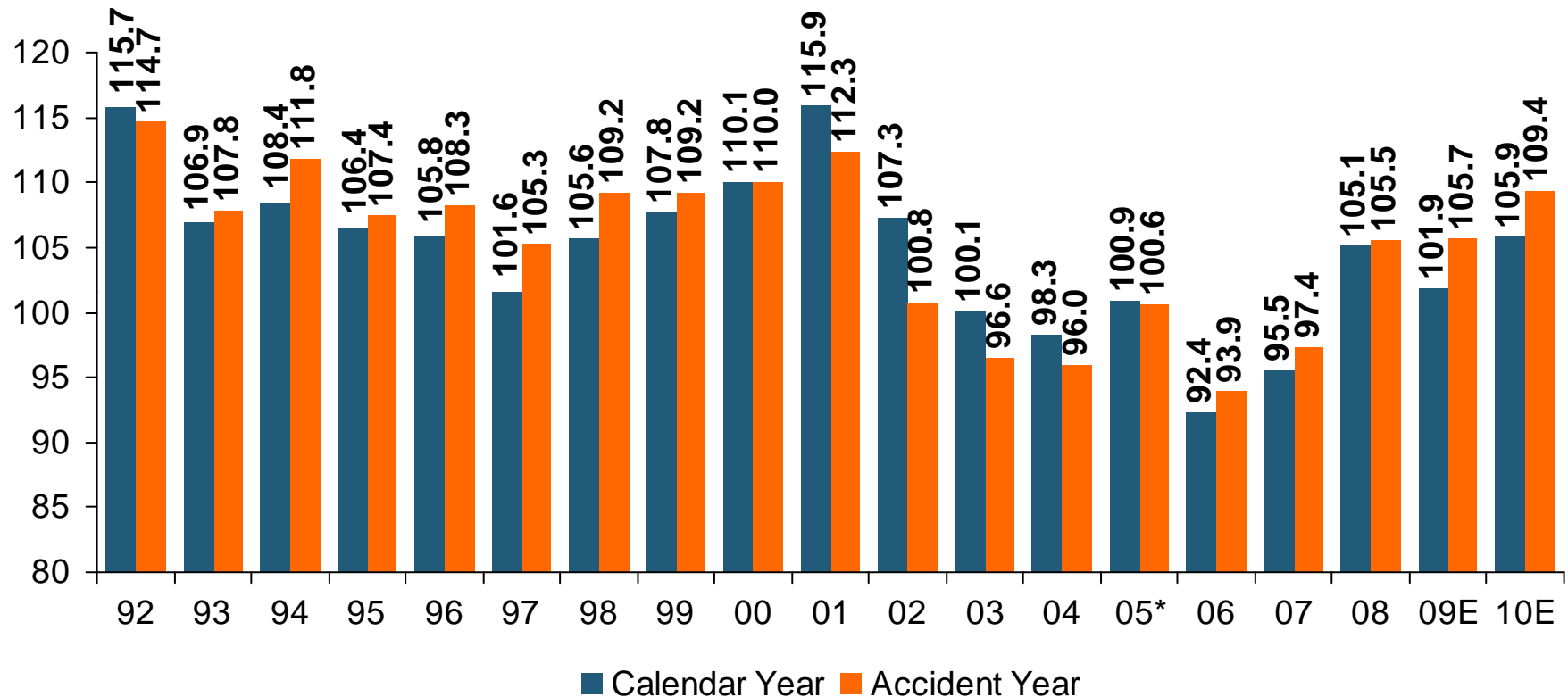


**Reserve Releases Will Expected to Taper Off
in 2010 and Drop Significantly in 2011**

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.

Calendar Year vs. Accident Year P/C Combined Ratio: 1992–2010E¹



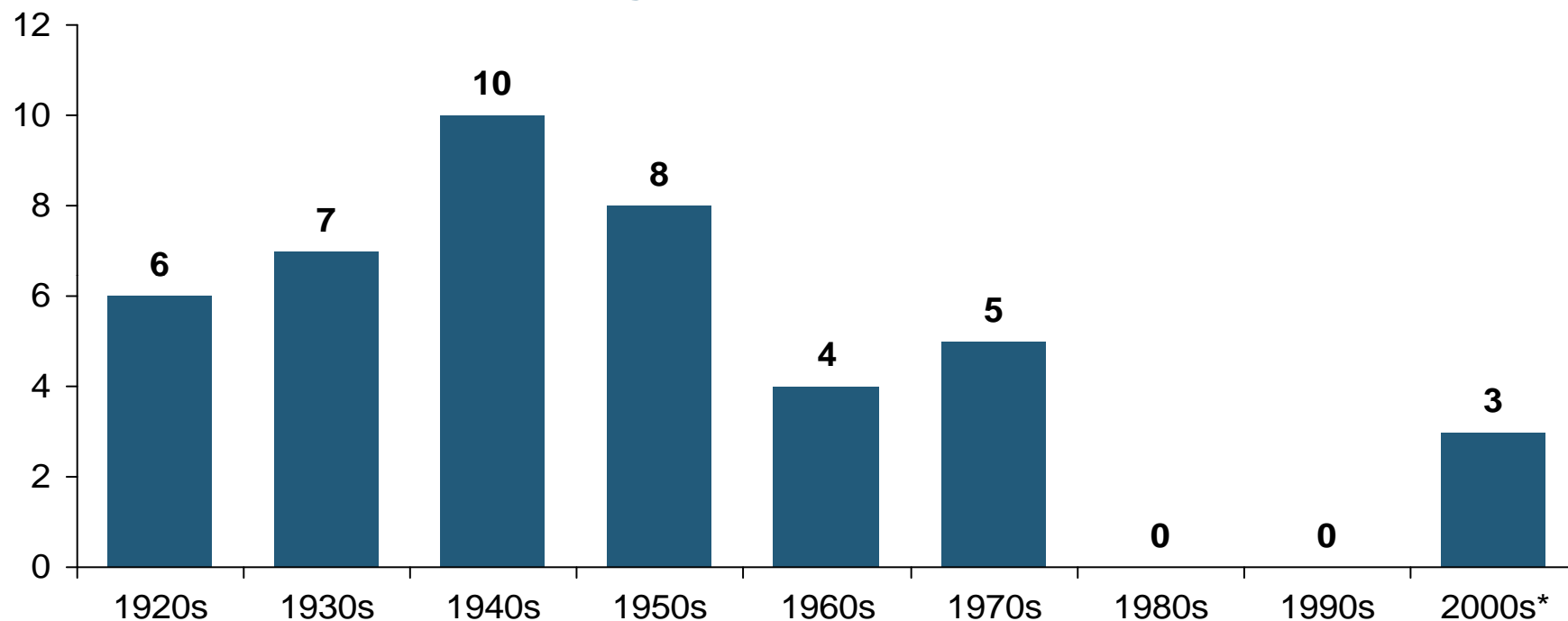
Accident Year Results Show a More Significant Deterioration in Underwriting Performance. Calendar Year Results Are Helped by Reserve Releases

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.

Number of Years with Underwriting Profits by Decade, 1920s–2000s

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**

* 2000 through 2009. 2009 combined ratio excluding mortgage and financial guaranty insurers was 99.3, which would bring the 2000s total to 4 years with an underwriting profit.

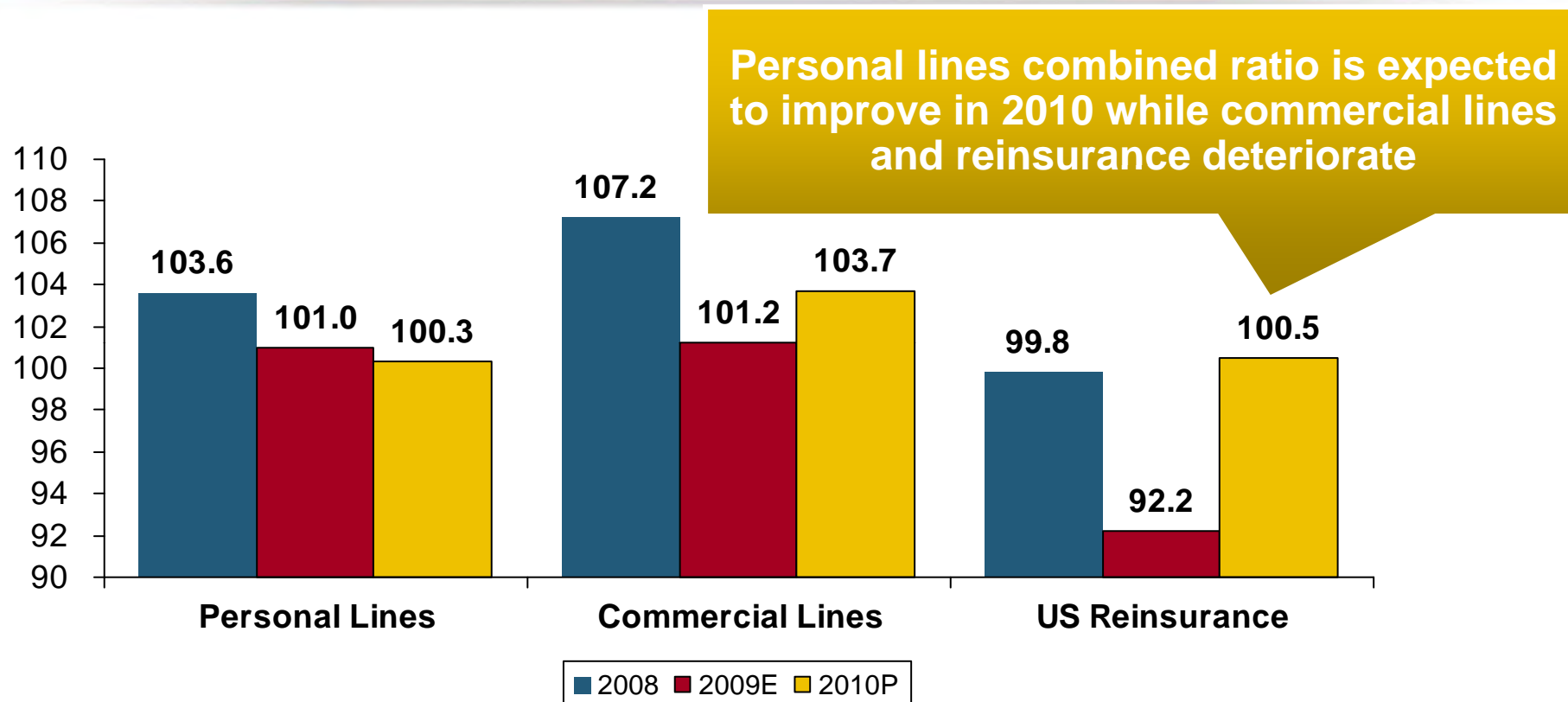
Note: Data for 1920–1934 based on stock companies only.

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



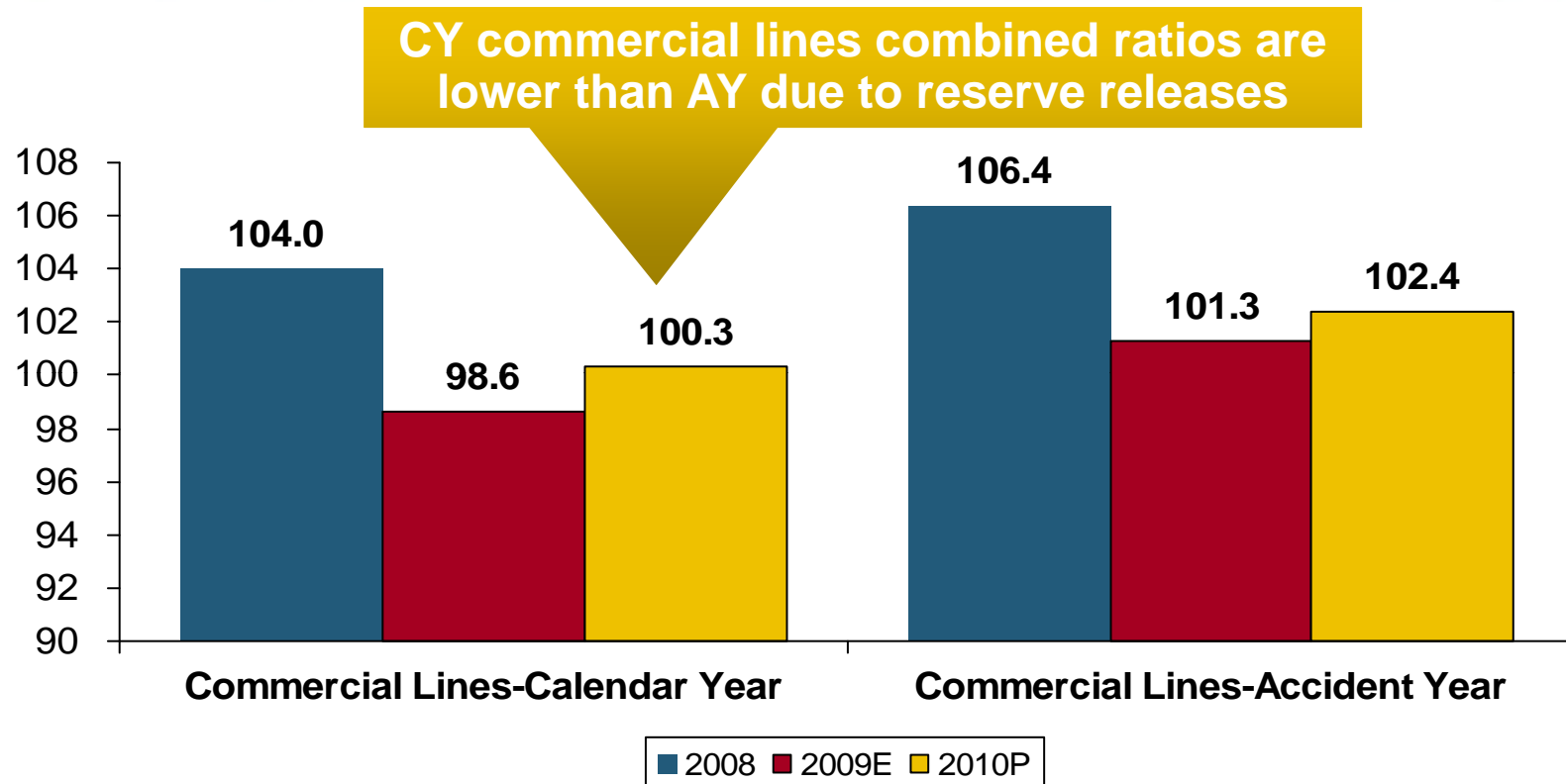
Performance by Segment: Commercial/Personal Lines & Reinsurance

Calendar Year Combined Ratios by Segment: 2008-2010P



Overall deterioration in 2010 underwriting performance is due to expected return to normal catastrophe activity along with deteriorating underwriting performance related to the prolonged commercial soft market

Calendar vs. Accident Year Combined Ratios by Segment: 2008-2010P*

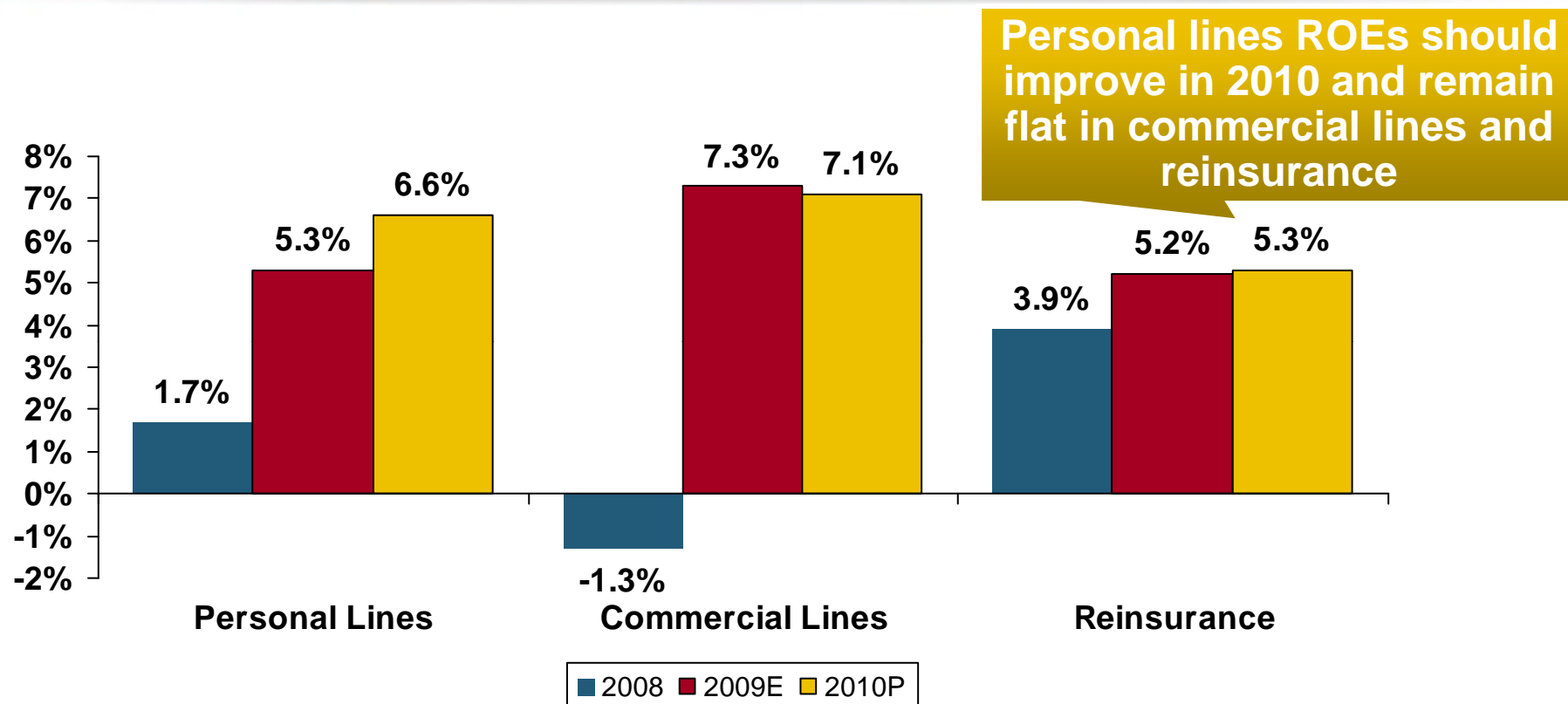


The ability of reserves releases to favorably impact calendar year results will diminish over time reserved redundancies fall

*Normalized to reflect average/typical level of catastrophe losses.

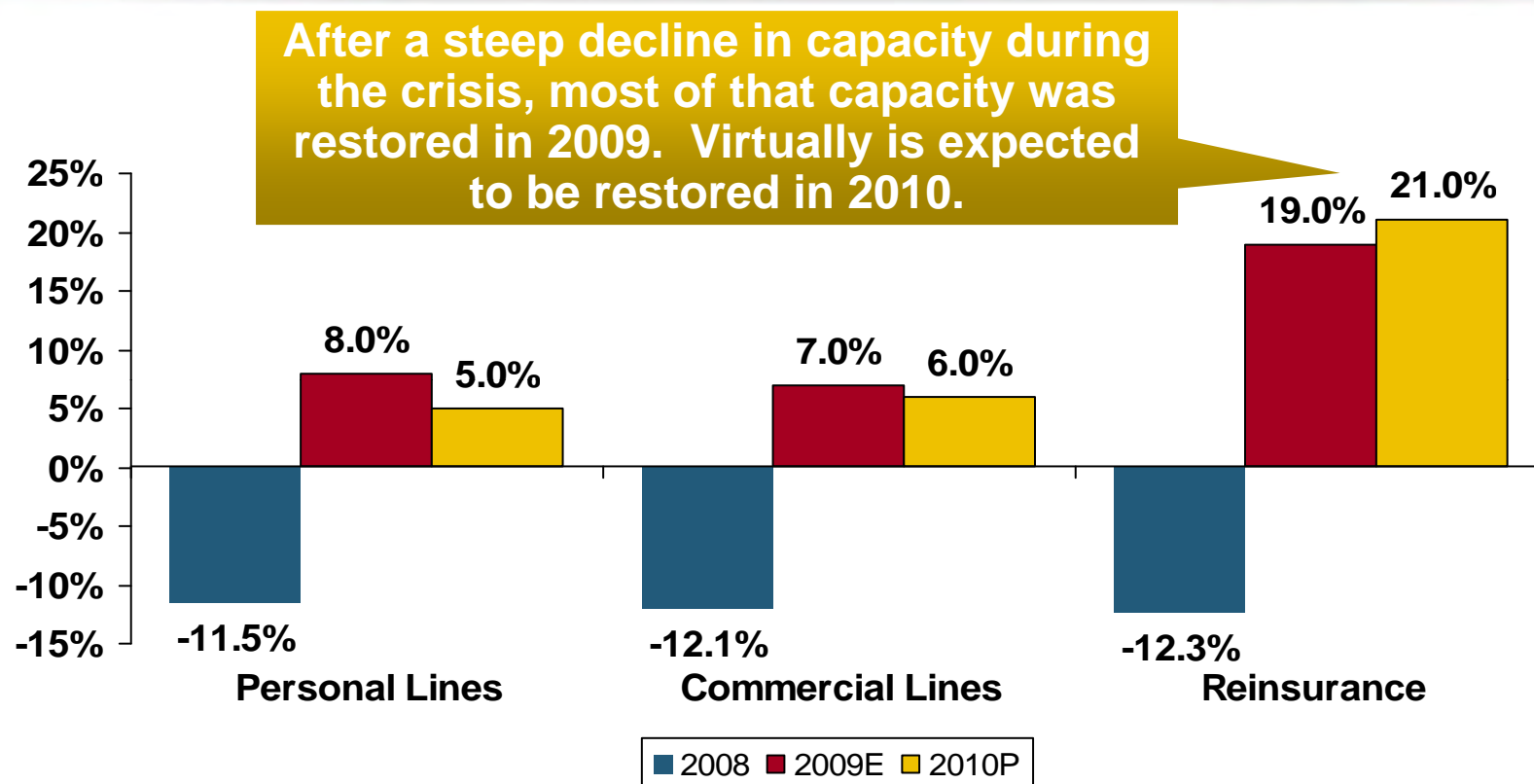
Sources: A.M. Best (historical and estimates/projected for 2009 and 2010); Insurance Information Institute.

After-Tax Return on Surplus (ROE) by Segment: 2008-2010P



Profitability will rise or stabilize across most p/c lines, barring a financial crisis relapse or major catastrophic losses

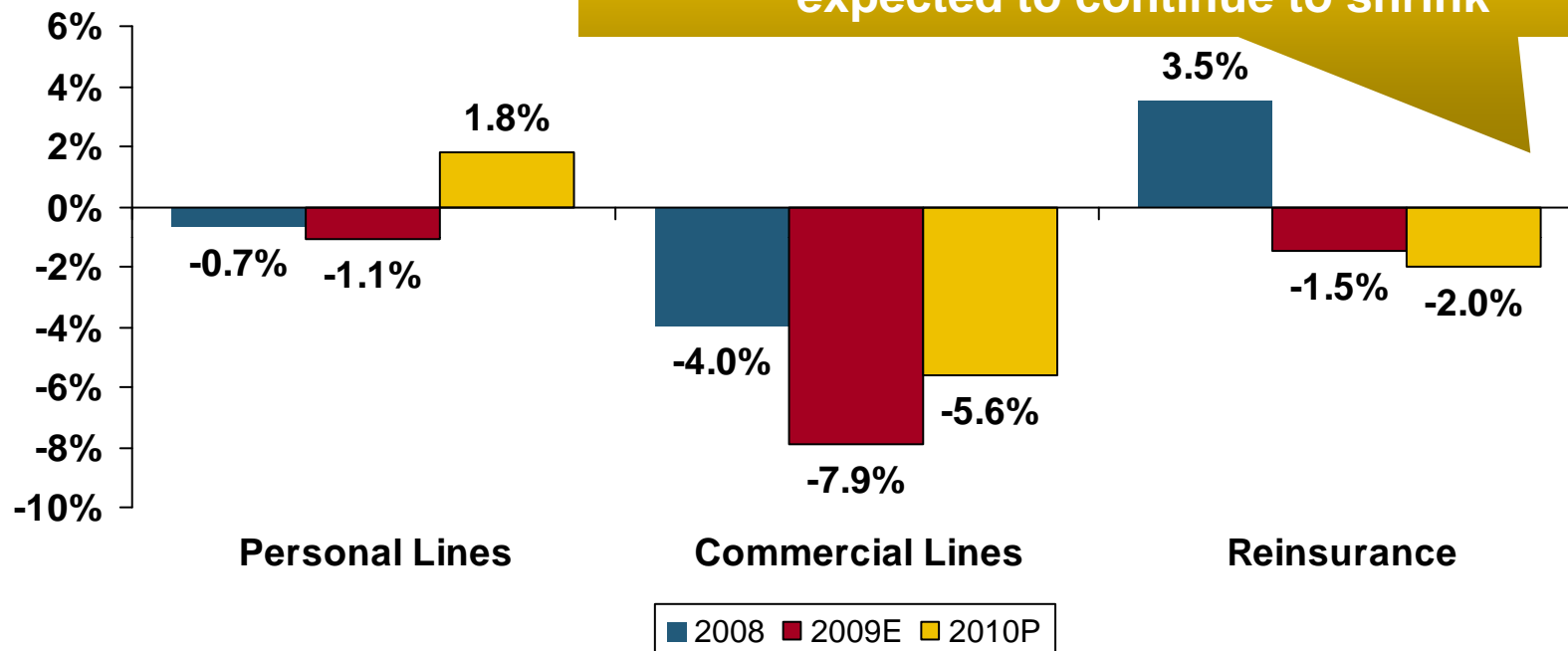
Change in Policyholder Surplus by Segment: 2008-2010P



Rapid growth in policyholder surplus to pre-crisis levels combined with ongoing slow growth or declines in premiums (esp. in commercial lines) implies a build-up of excess capacity—a major factor in weak commercial lines and reinsurance pricing

Net Written Premium Growth by Segment: 2008-2010P

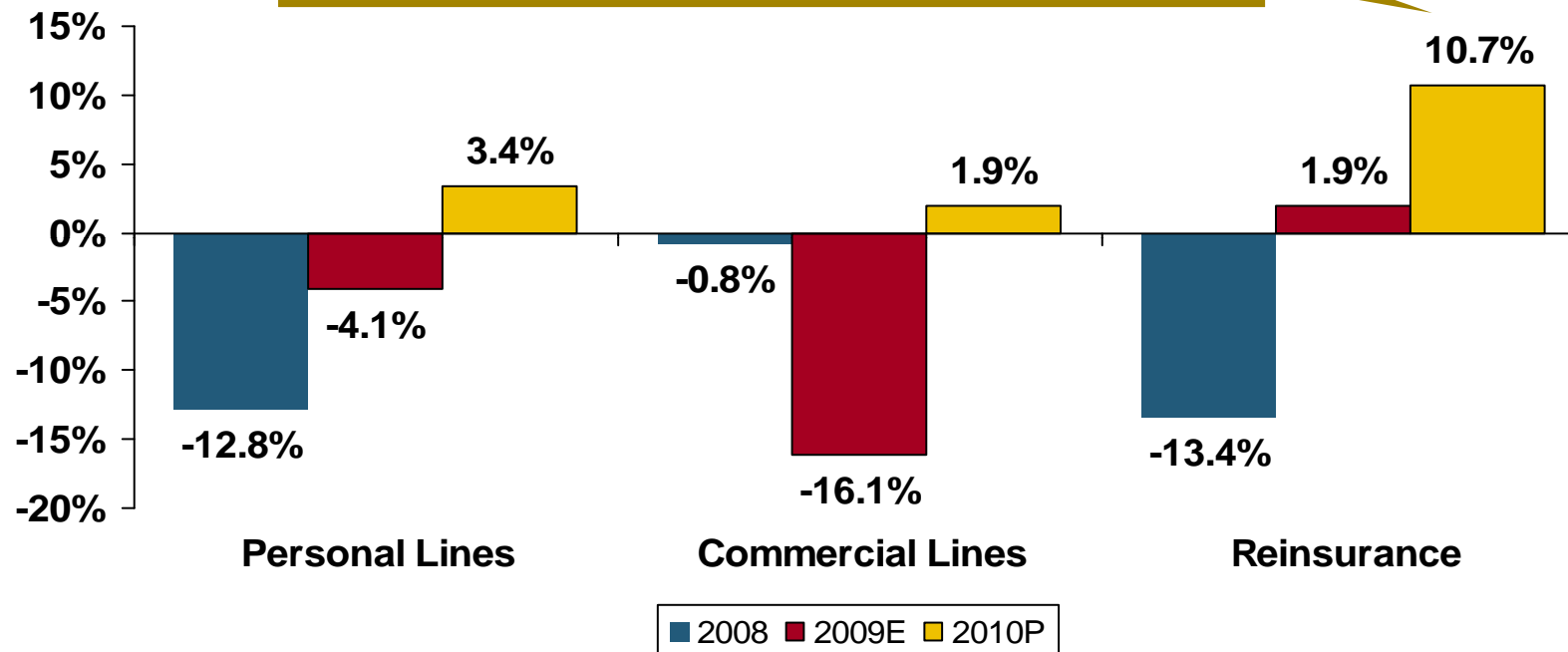
Personal lines will return to growth in 2010 while commercial lines and reinsurance are expected to continue to shrink



Rate and exposure are more favorable in personal lines, whereas a prolonged soft market and sluggish recovery from the recession weigh on commercial lines. Low catastrophe losses and ample capacity are holding down reinsurance prices while higher insurer retentions impact premiums

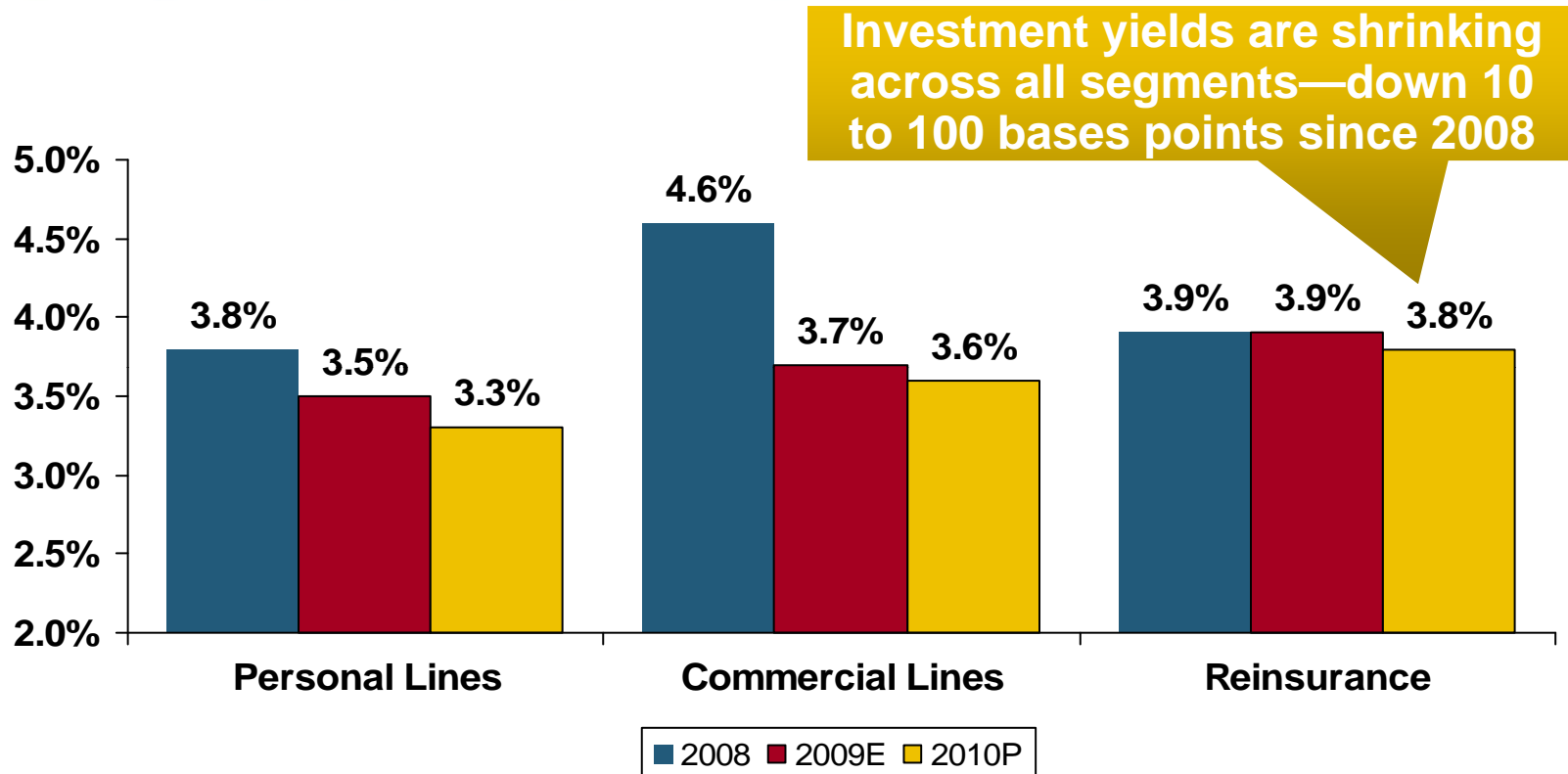
Change in Net Investment Income by Segment: 2008-2010P*

Net investment income is expected to begin to recover in all segments in 2010



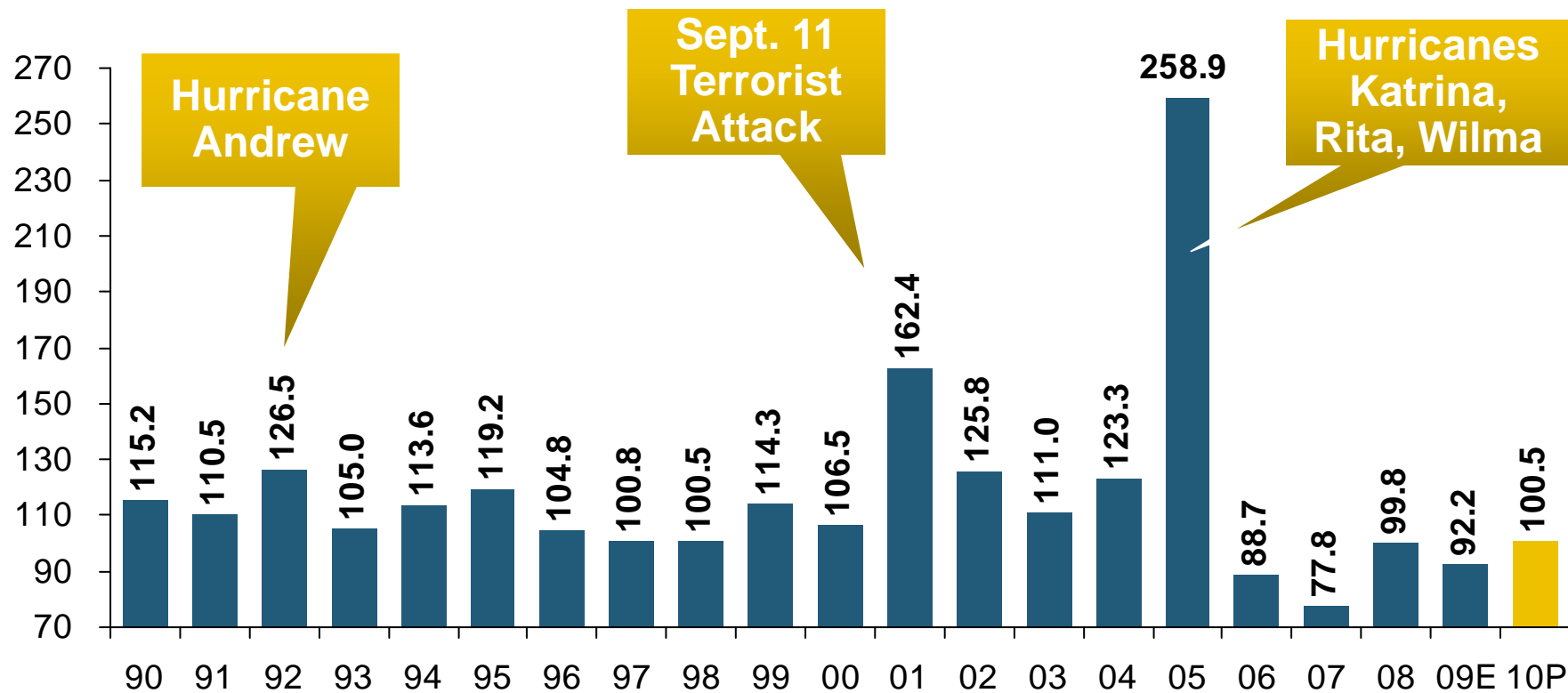
Investment income consists primarily of interest on bonds and stock dividends. Both were hit hard during the financial crisis as the Fed slashed interest rates to near zero and corporations cut dividends. A recovery in investment asset values beginning in Q2 2009—which reduced realized capital losses—has helped offset some of the decrease in investment income.

Investment Yield by Segment: 2008-2010P*



The Fed slashed interest rates in 2008 and has kept them low since, eroding the yield on all types of bonds, especially US Treasury securities. Yields will not recover until the Fed begins monetary policy tightening.

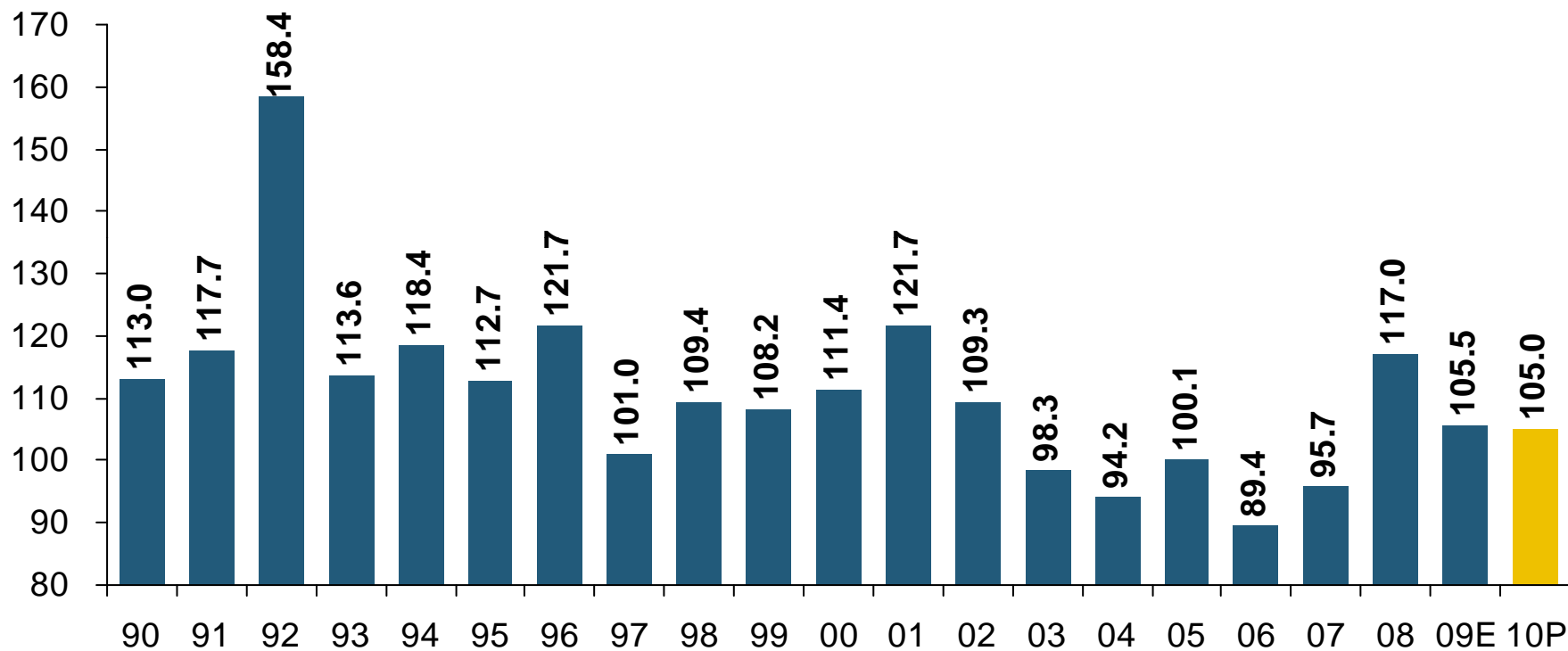
Reinsurance Combined Ratio: 1990–2010P



Reinsurance is a Highly Volatile Line and the Future is Unlikely to be Any Different

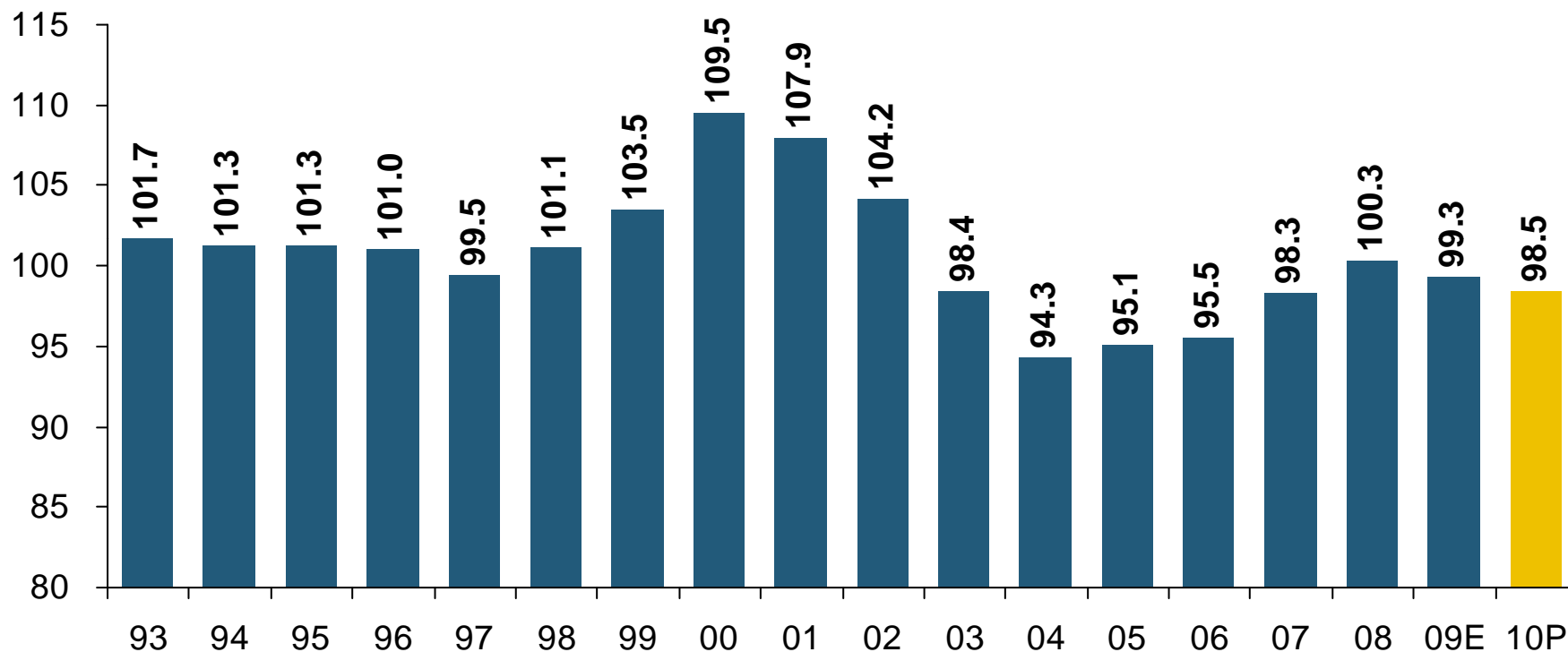
Note: 2008-2010 figures are from A.M. Best's *P/C Review and Preview*, February 8, 2010.
Sources: A.M. Best *Aggregates & Averages* for years 1990-2007; Insurance Information Institute.

Homeowners Insurance Combined Ratio: 1990–2010P



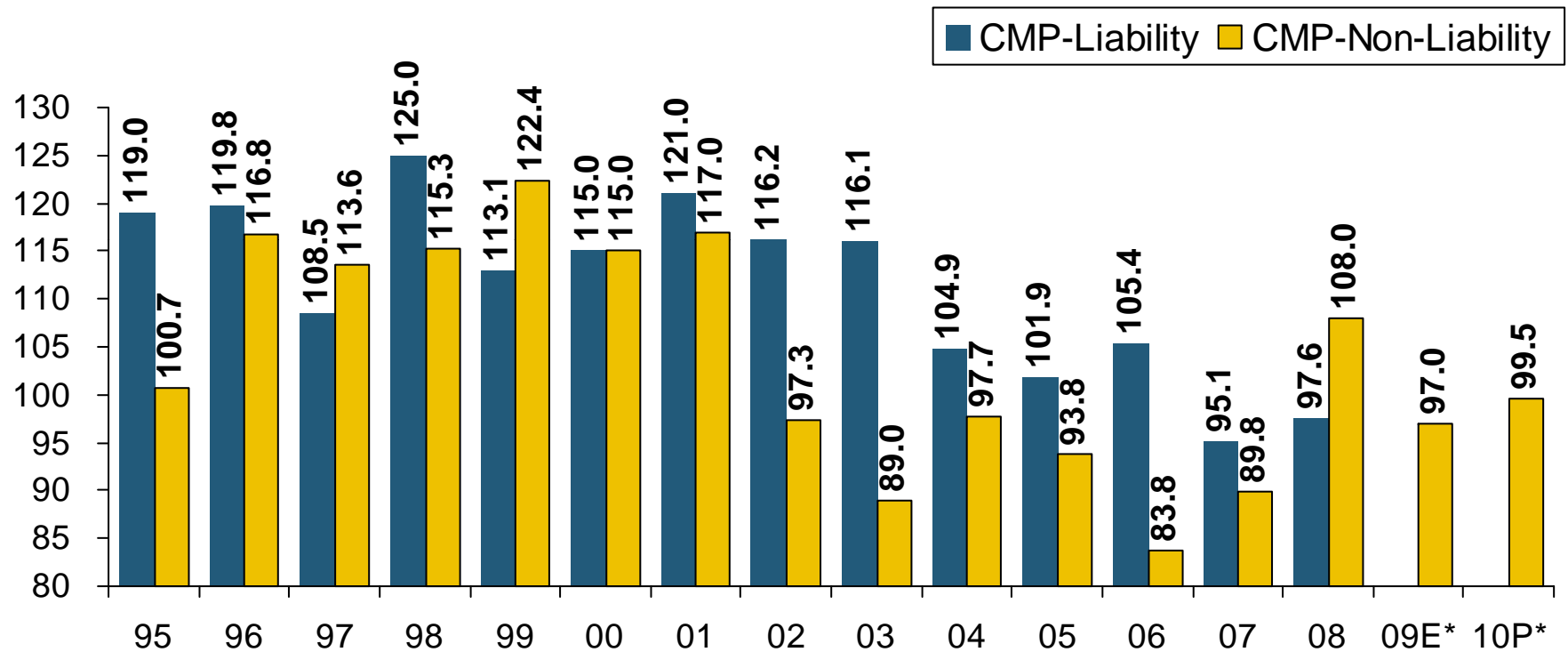
Homeowners Line Is Expected to Be Marginally Profitable Overall in 2010, but in Many States Could Be Quite Profitable. Volatility Due to Catastrophe Losses Will Persist

Private Passenger Auto Combined Ratio: 1993–2010P



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

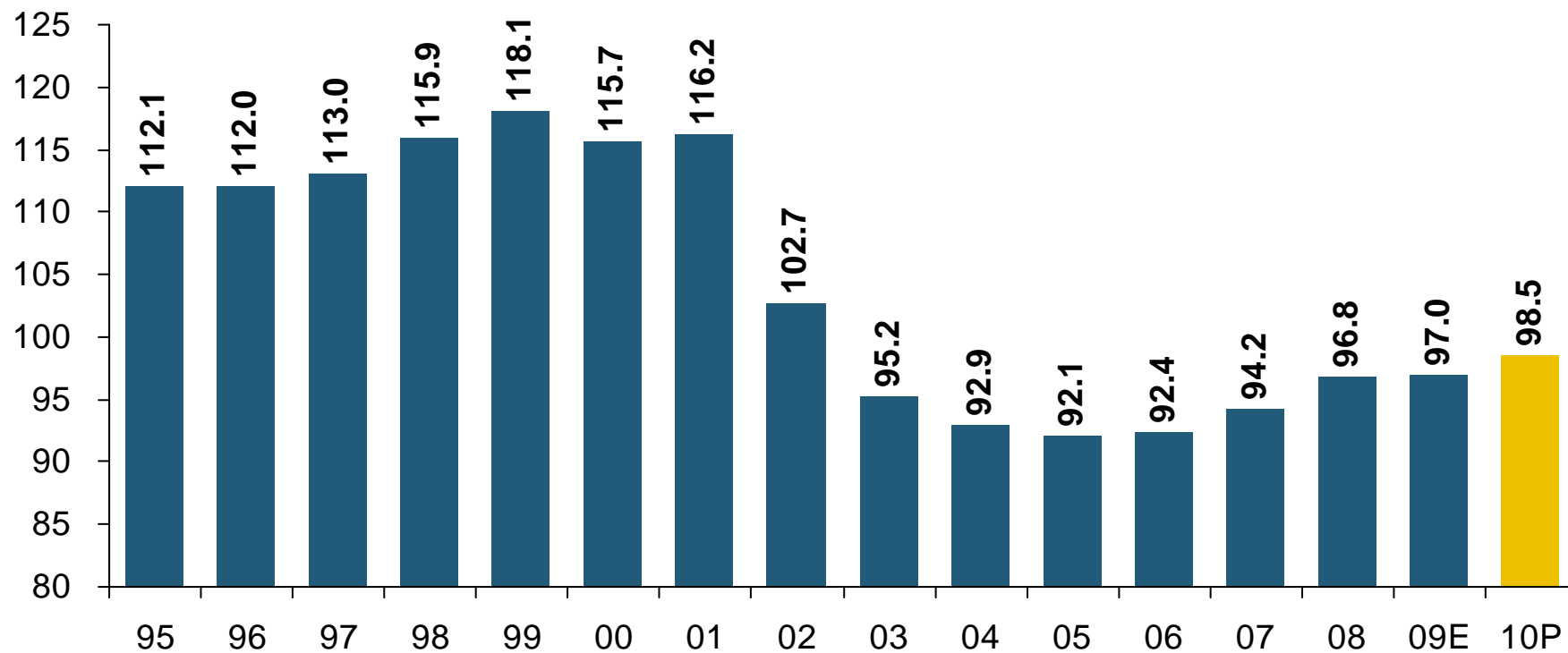
Commercial Multi-Peril Combined Ratio: 1995–2010P



Commercial Multi-Peril is Expected to Continue to Perform Reasonably Well

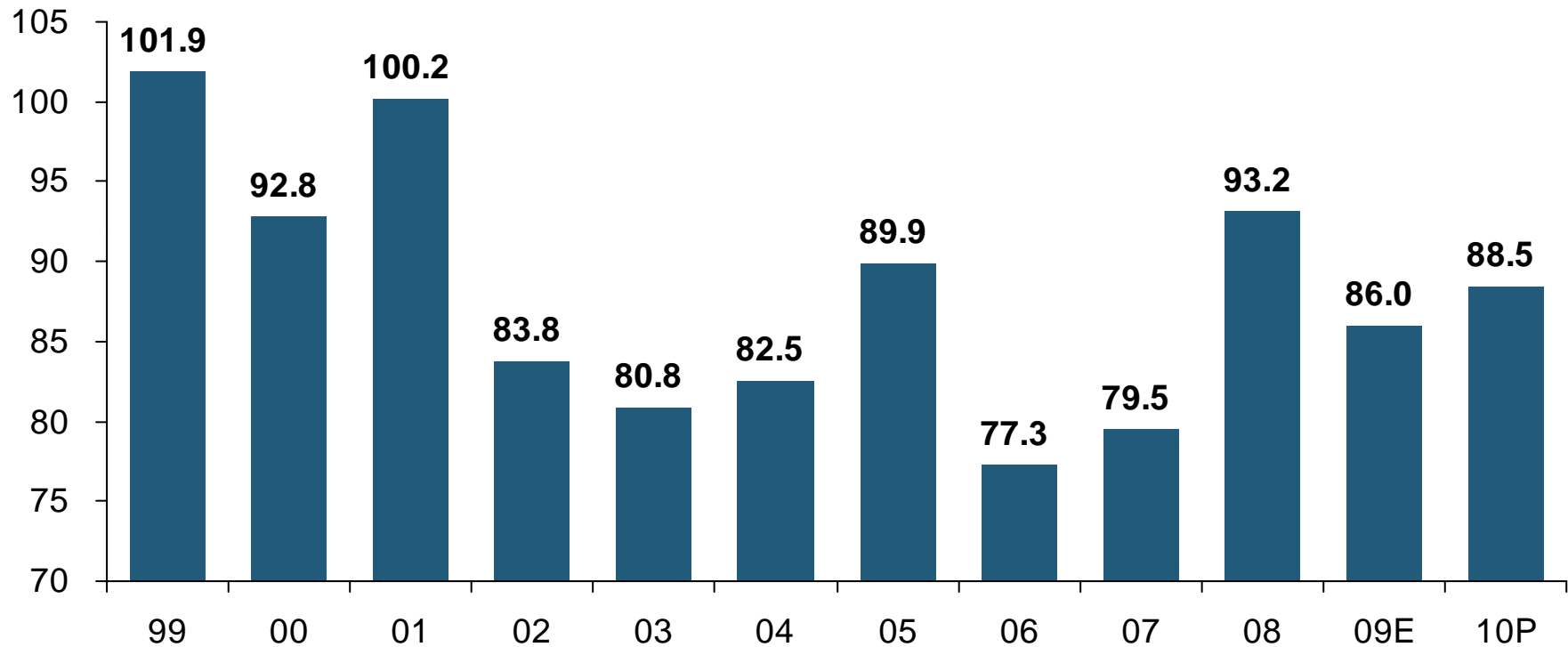
*2009E and 2010P figures are for the combined liability and non-liability components.
Sources: A.M. Best; Insurance Information Institute.

Commercial Auto Combined Ratio: 1993–2010P



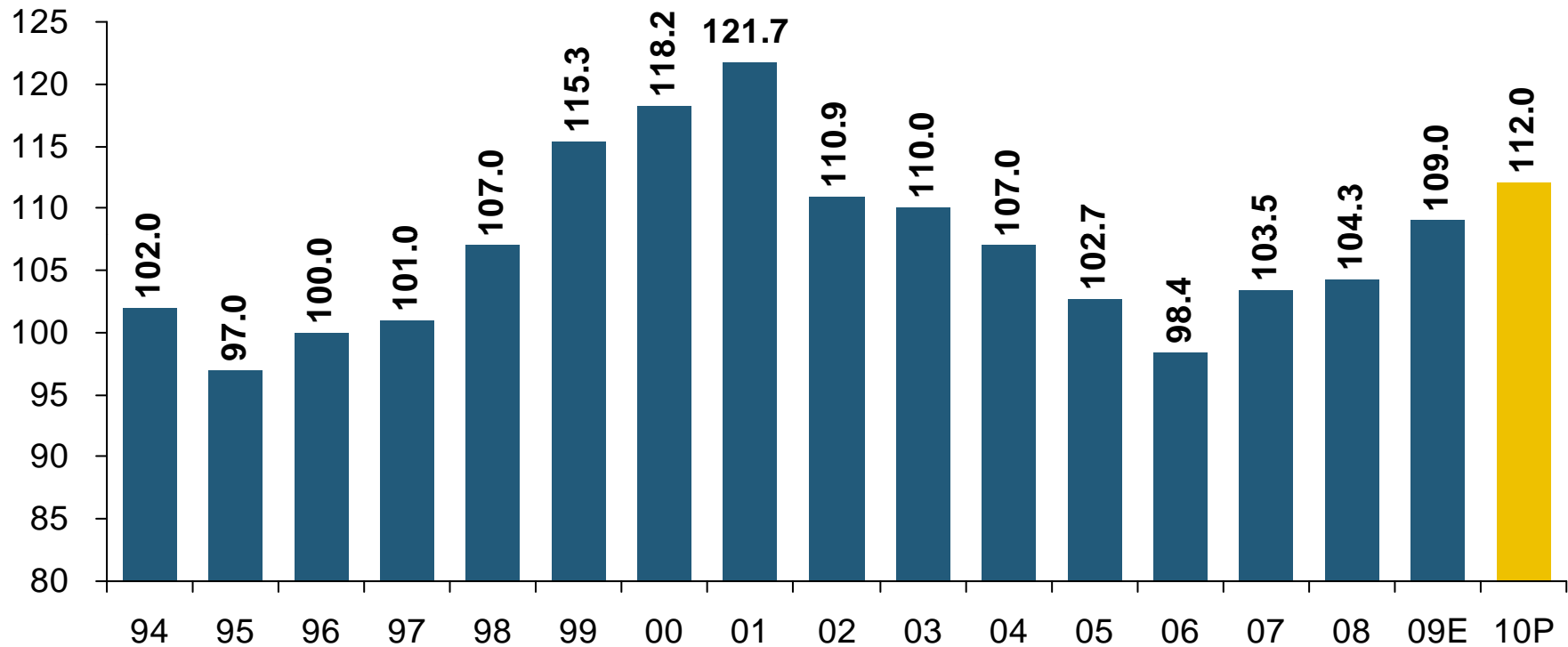
Commercial Auto is Expected to Remain Reasonably Profitable in 2010

Inland Marine Combined Ratio: 1999–2010P



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

Workers Compensation Combined Ratio: 1994–2010P



Workers Comp Underwriting Results Are Deteriorating Markedly

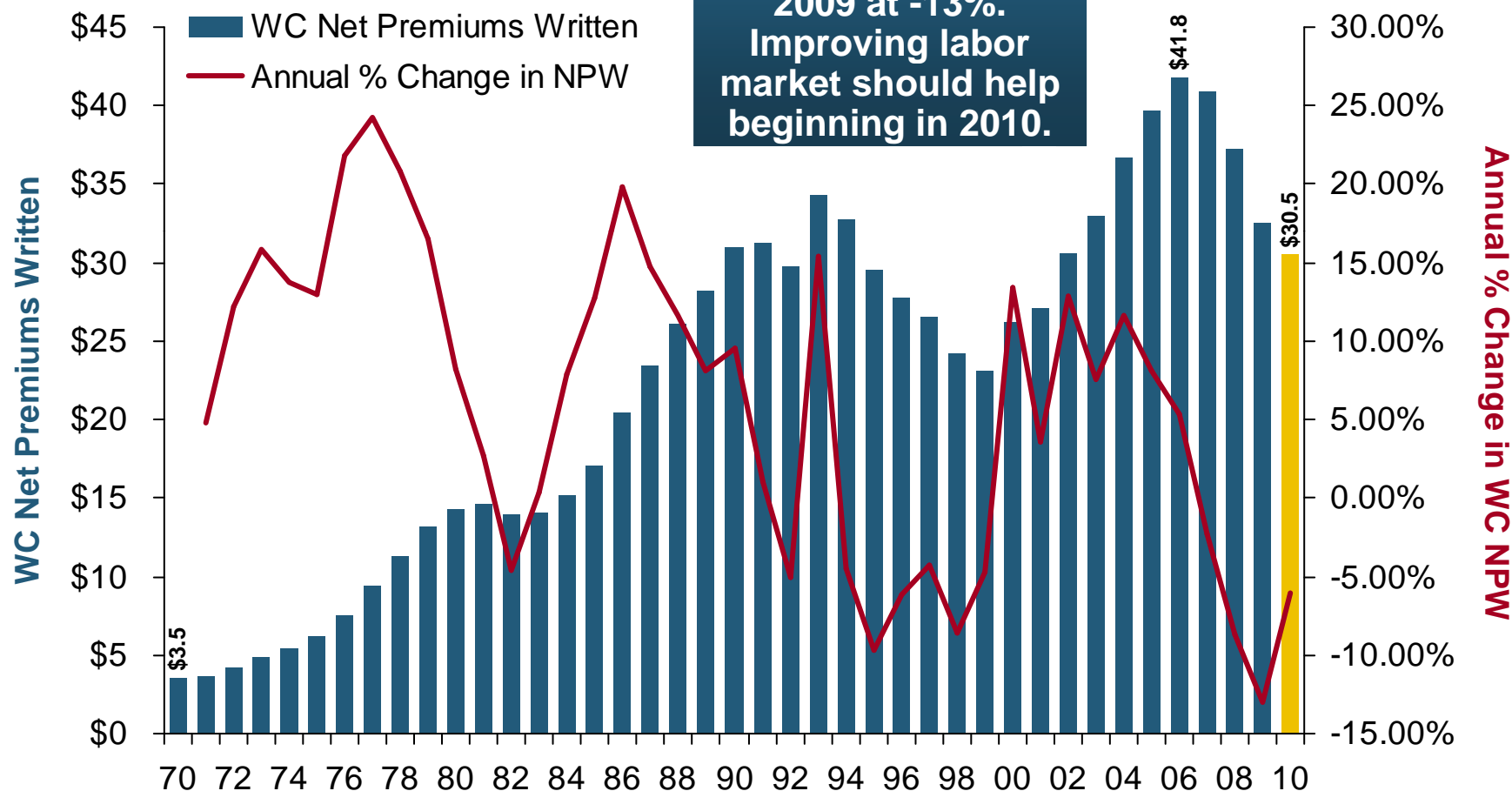


Workers Compensation Operating Environment

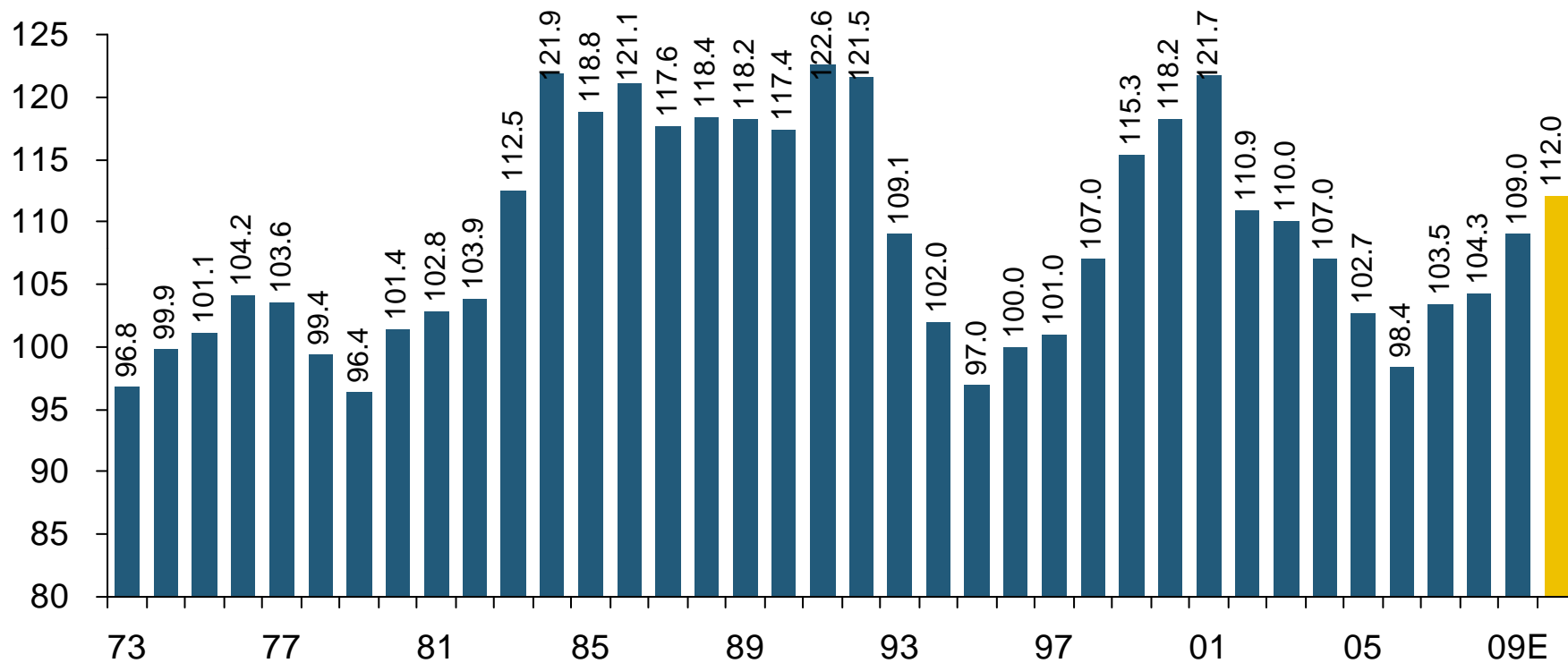
**The Weak Economy and Soft Market Have
Made the Workers Comp Operating
Increasingly Challenging**

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

(\$ Billions)



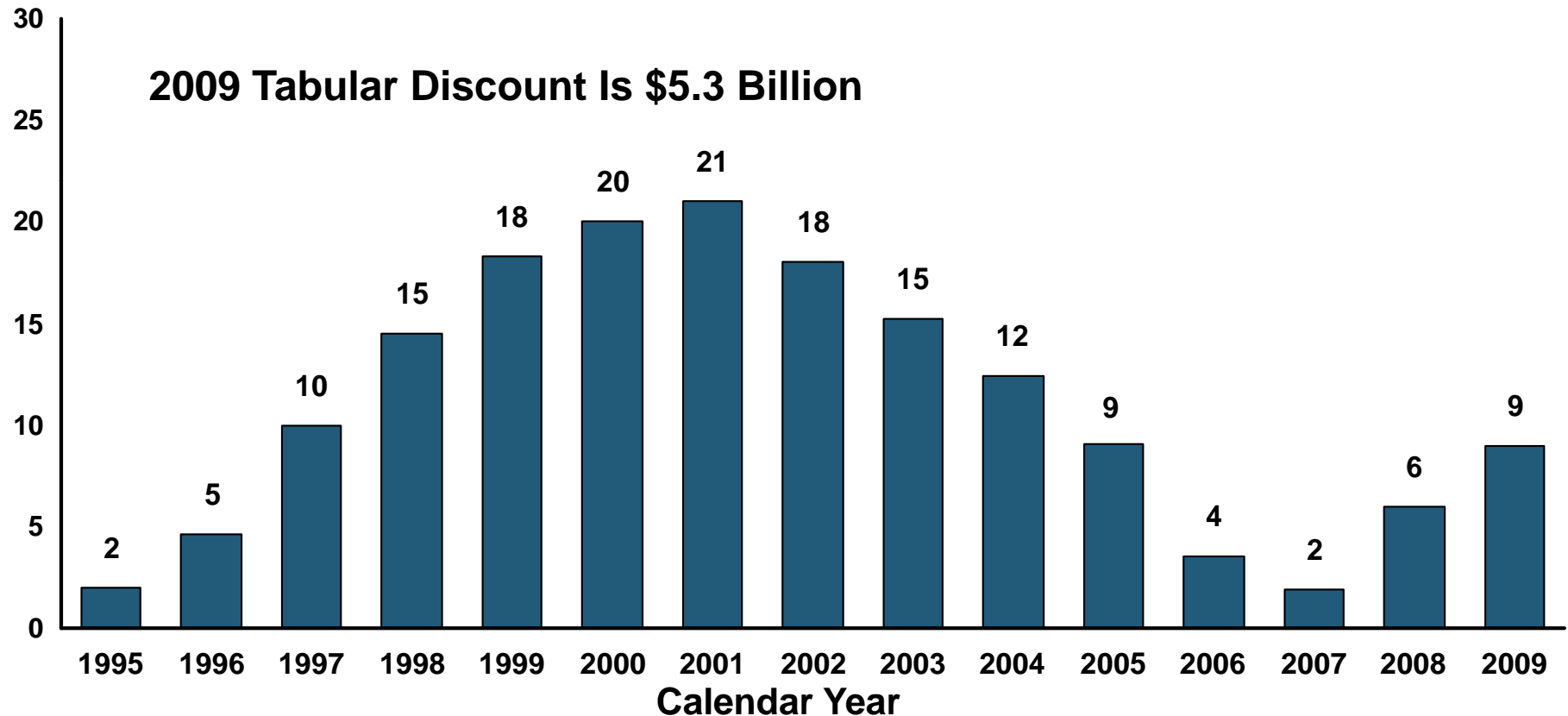
Workers Compensation Combined Ratio: 1973–2010P



Workers Comp Underwriting Results Are Deteriorating Markedly

Calendar Year Reserve Deficiency Increased in 2009

\$ Billions WC Loss and LAE Reserve Deficiency: Private Carriers



Considers all reserve discounts as deficiencies

Loss and LAE figures are based on NAIC Annual Statement data for each valuation date and NCCI latest selections

Source: NCCI analysis

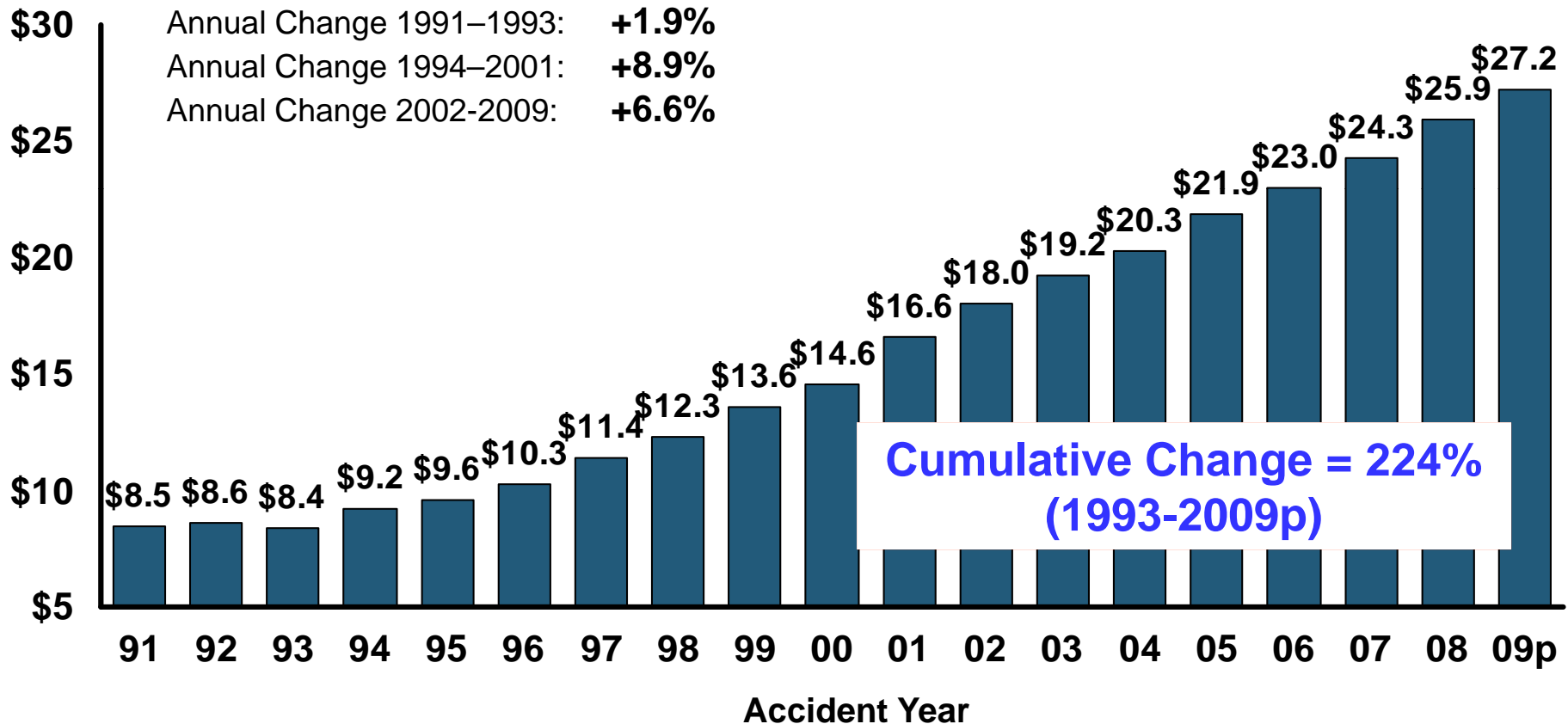


Workers Compensation Medical & Indemnity Claim Cost Trends

Rising Medical Costs Exert Pressure While Indemnity Costs Rise Well Ahead of Wage Inflation

Workers Comp Medical Claim Costs Continue to Rise

Medical Claim Cost (\$000s)

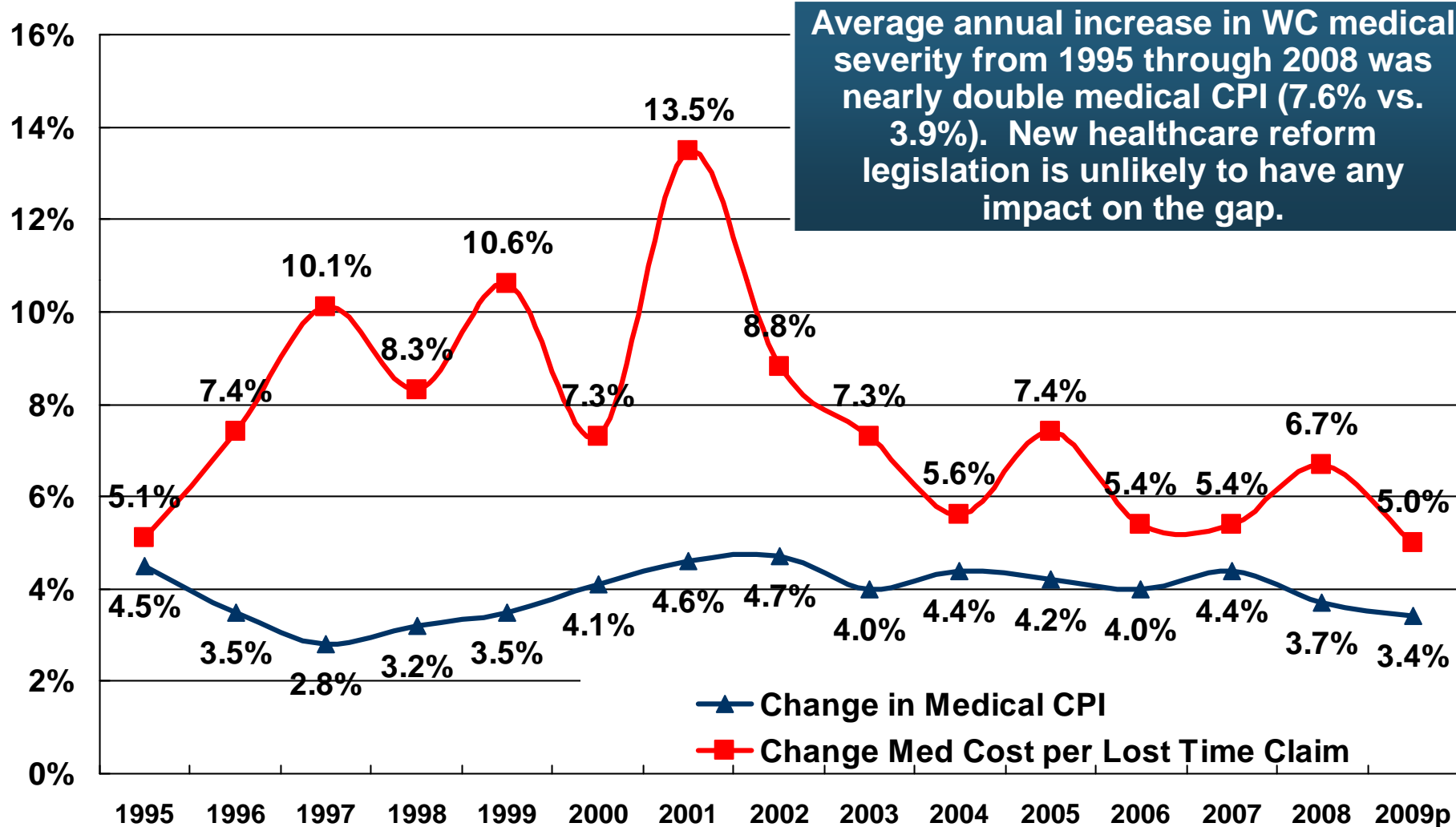


2009p: Preliminary based on data valued as of 12/31/2009

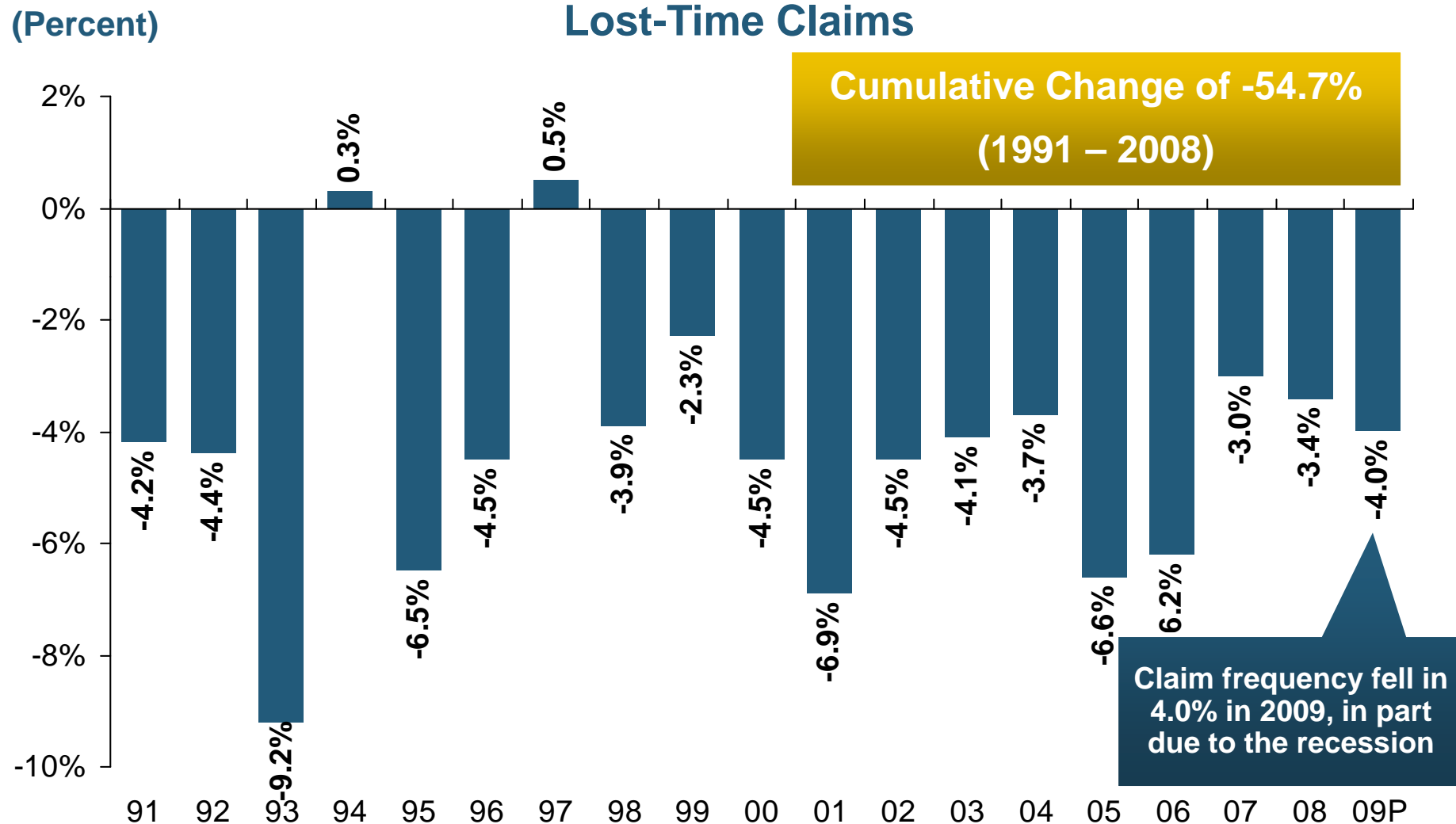
1991-2008: Based on data through 12/31/2008, developed to ultimate

Based on the states where NCCI provides ratemaking services; Excludes the effects of deductible policies

WC Medical Severity Rising at Nearly Twice the Medical CPI Rate



Workers Compensation Lost-Time Claim Frequency Continues to Decline*

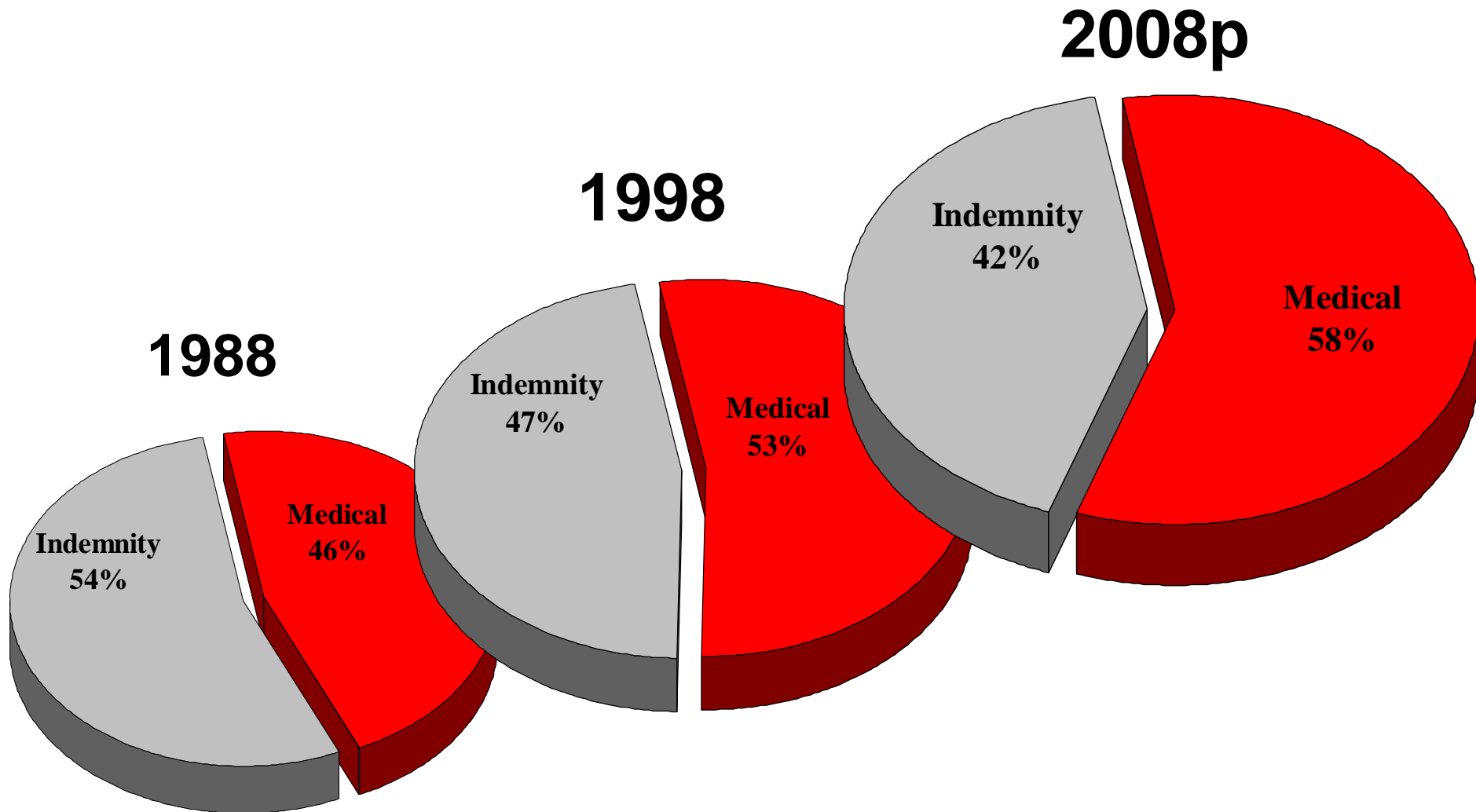


2009p: Preliminary based on data valued as of 12/31/2009;
1991-2008: Based on data through 12/31/2008, developed to ultimate

*Frequency is defined as the number of lost-time claims per 100,000 workers.

Based on the states where NCCI provides ratemaking services including state funds; Excludes the effects of deductible policies

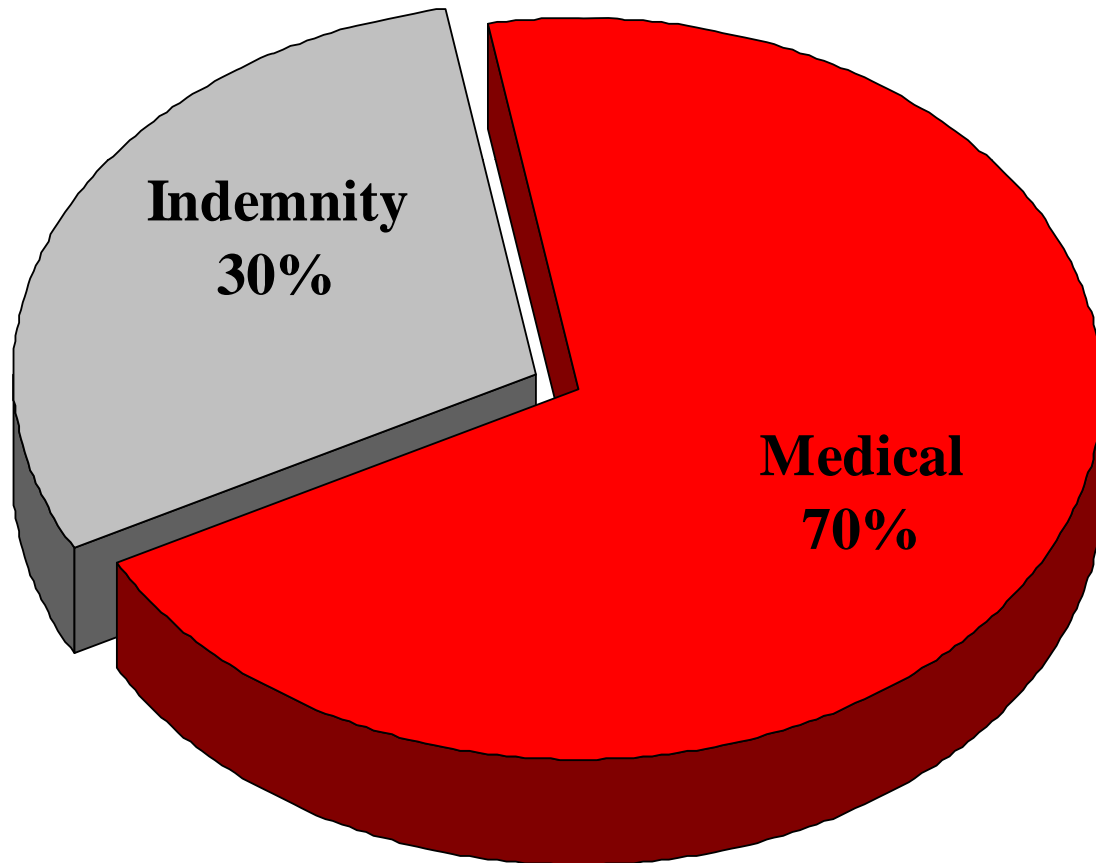
Med Costs Share of Total Costs is Increasing Steadily



Source: NCCI (based on states where NCCI provides ratemaking services).

WC Med Cost Will Equal 70% of Total by 2018 if Trends Hold

2018 Estimate



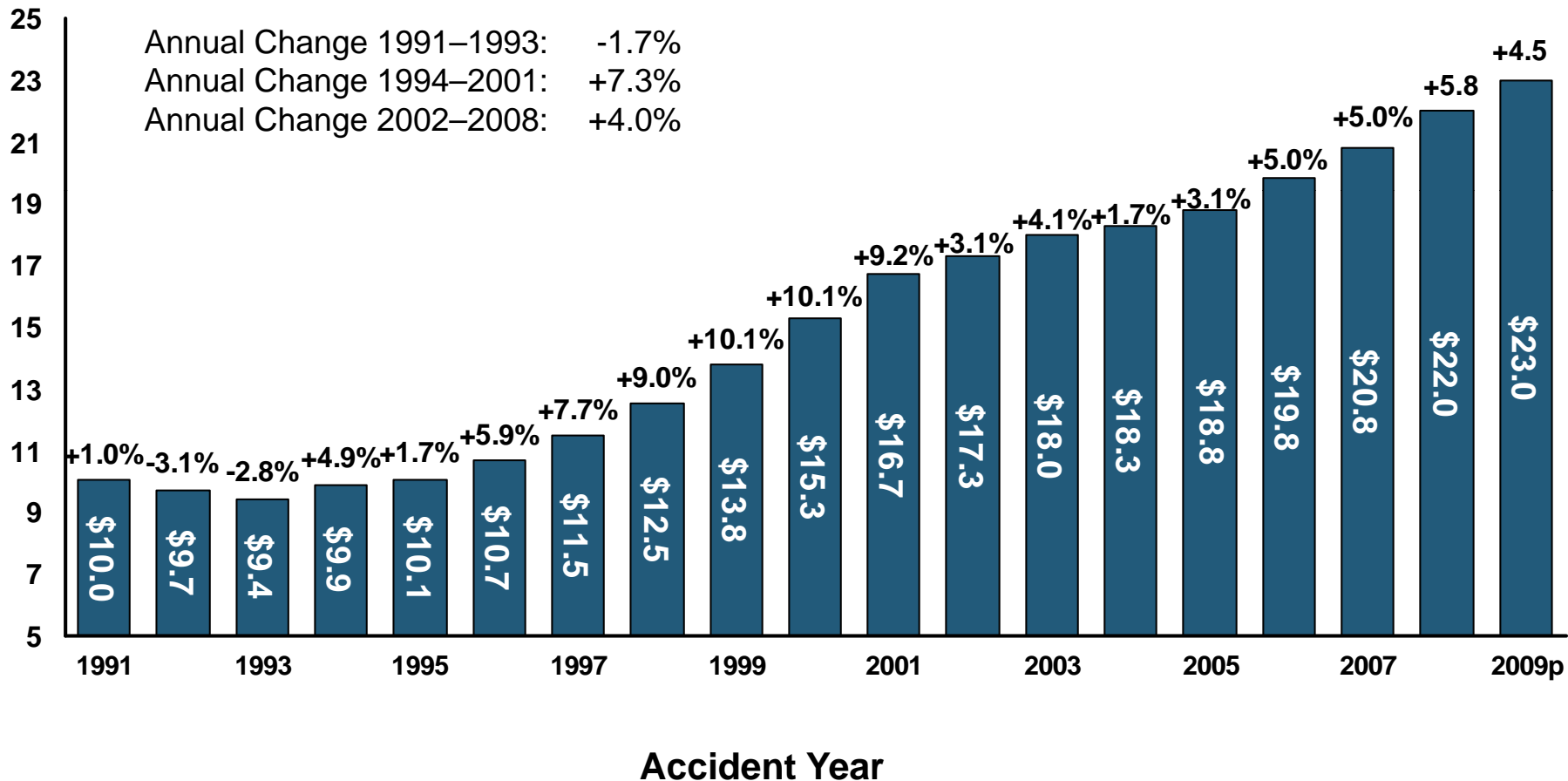
This trend will likely be supported by the increased labor force participation of workers age 55 and older.

Indemnity Claim Cost Trends

**Indemnity Costs Continue to Rise at a
Pace Above Wage Inflation**

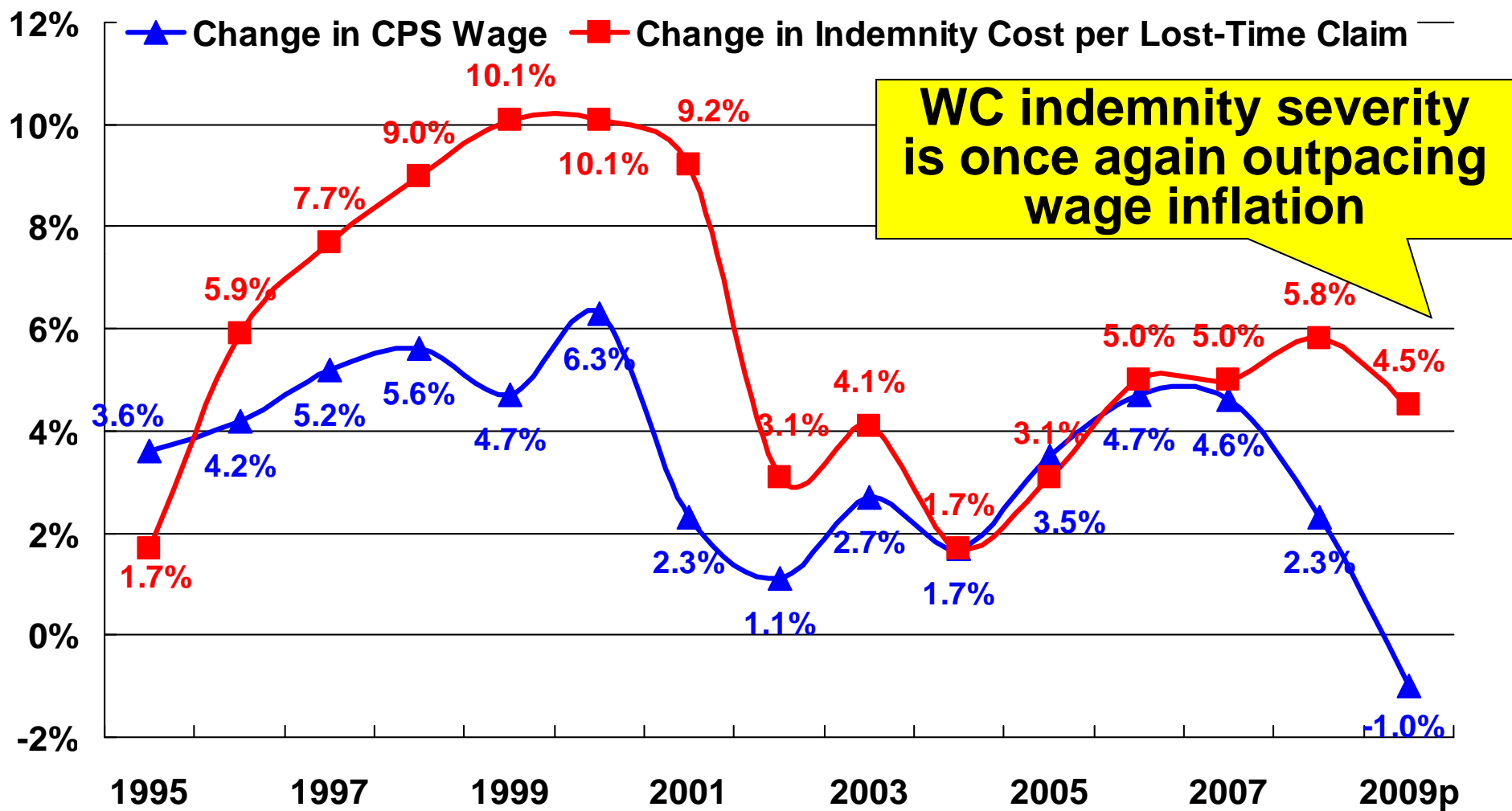
Workers Comp Indemnity Claim Costs Continue to Grow

Indemnity
Claim Cost (\$ 000s)



2009p: Preliminary based on data valued as of 12/31/2009
1991–2008: Based on data through 12/31/2008, developed to ultimate
Based on the states where NCCI provides ratemaking services
Excludes the effects of deductible policies

WC Indemnity Severity vs. Wage Inflation



2009p: Preliminary based on data valued as of 12/31/2009; 1991-2008: Based on data through 12/31/2008, developed to ultimate. Based on the states where NCCI provides ratemaking services. Excludes the effects of deductible policies. CPS = Current Population Survey.
Source: NCCI

Where Will the Growth in WC Exposure Come From?

Industry and Occupation Growth Analysis

Fastest Growing Occupations, 2008–2018:

Health/Science/Tech Dominate

WC exposure growth the fastest in the health, science and tech areas

| Occupations | Percent change | Number of new jobs (in thousands) | Wages (May 2008 median) | Education/training category |
|--|----------------|-----------------------------------|-------------------------|---|
| Biomedical engineers | 72 | 11.6 | \$ 77,400 | Bachelor's degree |
| Network systems and data communications analysts | 53 | 155.8 | 71,100 | Bachelor's degree |
| Home health aides | 50 | 460.9 | 20,460 | Short-term on-the-job training |
| Personal and home care aides | 46 | 375.8 | 19,180 | Short-term on-the-job training |
| Financial examiners | 41 | 11.1 | 70,930 | Bachelor's degree |
| Medical scientists, except epidemiologists | 40 | 44.2 | 72,590 | Doctoral degree |
| Physician assistants | 39 | 29.2 | 81,230 | Master's degree |
| Skin care specialists | 38 | 14.7 | 28,730 | Postsecondary vocational award |
| Biochemists and biophysicists | 37 | 8.7 | 82,840 | Doctoral degree |
| Athletic trainers | 37 | 6.0 | 39,640 | Bachelor's degree |
| Physical therapist aides | 36 | 16.7 | 23,760 | Short-term on-the-job training |
| Dental hygienists | 36 | 62.9 | 66,570 | Associate degree |
| Veterinary technologists and technicians | 36 | 28.5 | 28,900 | Associate degree |
| Dental assistants | 36 | 105.6 | 32,380 | Moderate-term on-the-job training |
| Computer software engineers, applications | 34 | 175.1 | 85,430 | Bachelor's degree |
| Medical assistants | 34 | 163.9 | 28,300 | Moderate-term on-the-job training |
| Physical therapist assistants | 33 | 21.2 | 46,140 | Associate degree |
| Veterinarians | 33 | 19.7 | 79,050 | First professional degree |
| Self-enrichment education teachers | 32 | 81.3 | 35,720 | Work experience in a related occupation |
| Compliance officers, except agriculture, construction, health and safety, and transportation | 31 | 80.8 | 48,890 | Long-term on-the-job training |

SOURCE: BLS Occupational Employment Statistics and Division of Occupational Outlook

Occupations with Largest Numerical Growth, 2008–2018: *Health, Services Dominate*

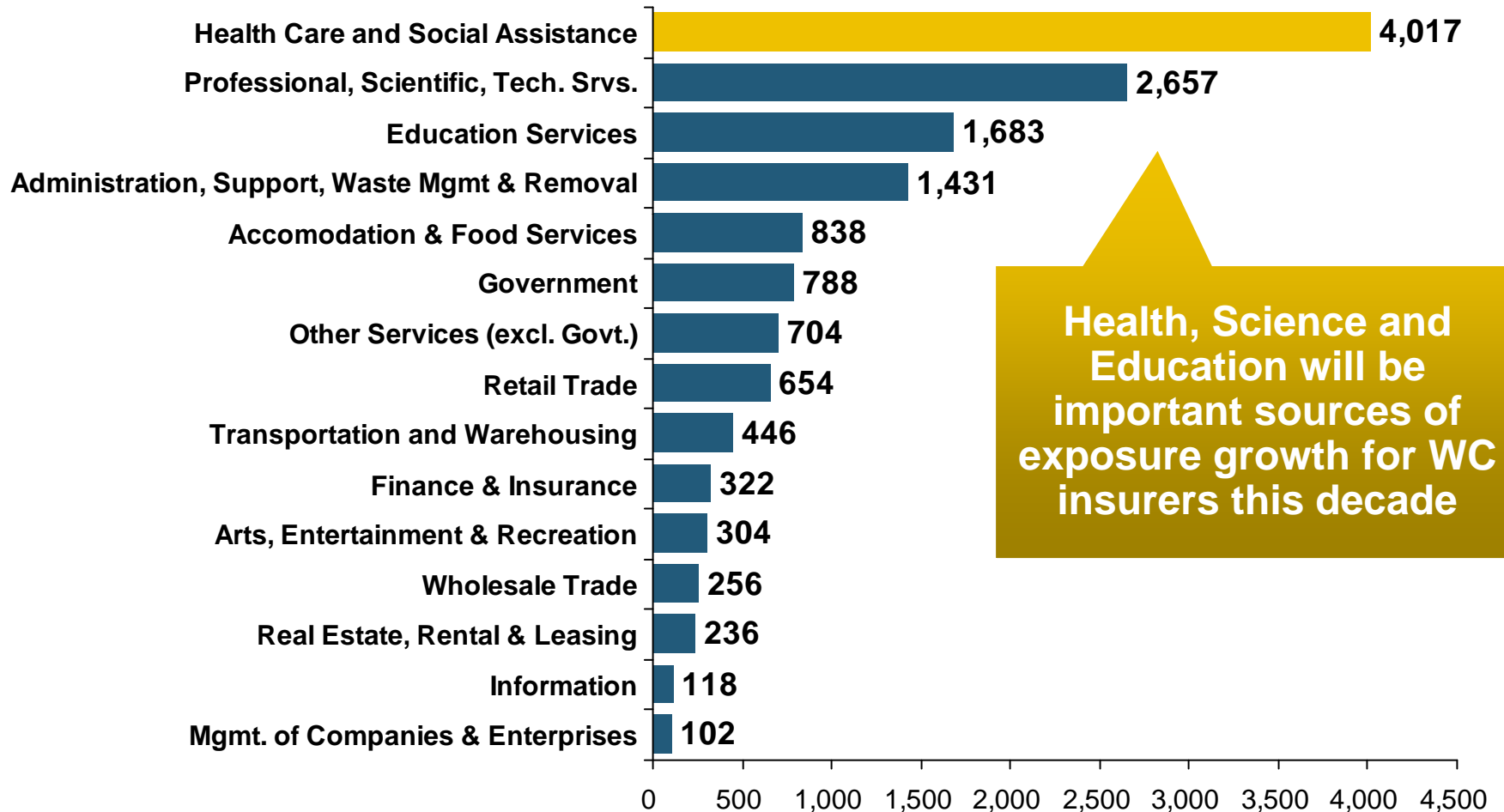
Dollar growth in WC exposures should grow the most (at current rate levels) in the health and services industries

| Occupations | Number of new jobs (in thousands) | Percent change | Wages (May 2008 median) | Education/training category |
|--|-----------------------------------|----------------|-------------------------|---|
| Registered nurses | 581.5 | 22 | \$ 62,450 | Associate degree |
| Home health aides | 460.9 | 50 | 20,460 | Short-term on-the-job training |
| Customer service representatives | 399.5 | 18 | 29,860 | Moderate-term on-the-job training |
| Combined food preparation and serving workers, including fast food | 394.3 | 15 | 16,430 | Short-term on-the-job training |
| Personal and home care aides | 375.8 | 46 | 19,180 | Short-term on-the-job training |
| Retail salespersons | 374.7 | 8 | 20,510 | Short-term on-the-job training |
| Office clerks, general | 358.7 | 12 | 25,320 | Short-term on-the-job training |
| Accountants and auditors | 279.4 | 22 | 59,430 | Bachelor's degree |
| Nursing aides, orderlies, and attendants | 276.0 | 19 | 23,850 | Postsecondary vocational award |
| Postsecondary teachers | 256.9 | 15 | 58,830 | Doctoral degree |
| Construction laborers | 255.9 | 20 | 28,520 | Moderate-term on-the-job training |
| Elementary school teachers, except special education | 244.2 | 16 | 49,330 | Bachelor's degree |
| Truck drivers, heavy and tractor-trailer | 232.9 | 13 | 37,270 | Short-term on-the-job training |
| Landscaping and groundskeeping workers | 217.1 | 18 | 23,150 | Short-term on-the-job training |
| Bookkeeping, accounting, and auditing clerks | 212.4 | 10 | 32,510 | Moderate-term on-the-job training |
| Executive secretaries and administrative assistants | 204.4 | 13 | 40,030 | Work experience in a related occupation |
| Management analysts | 178.3 | 24 | 73,570 | Bachelor's or higher degree, plus work experience |
| Computer software engineers, applications | 175.1 | 34 | 85,430 | Bachelor's degree |
| Receptionists and information clerks | 172.9 | 15 | 24,550 | Short-term on-the-job training |
| Carpenters | 165.4 | 13 | 38,940 | Long-term on-the-job training |

SOURCE: BLS Occupational Employment Statistics and Division of Occupational Outlook

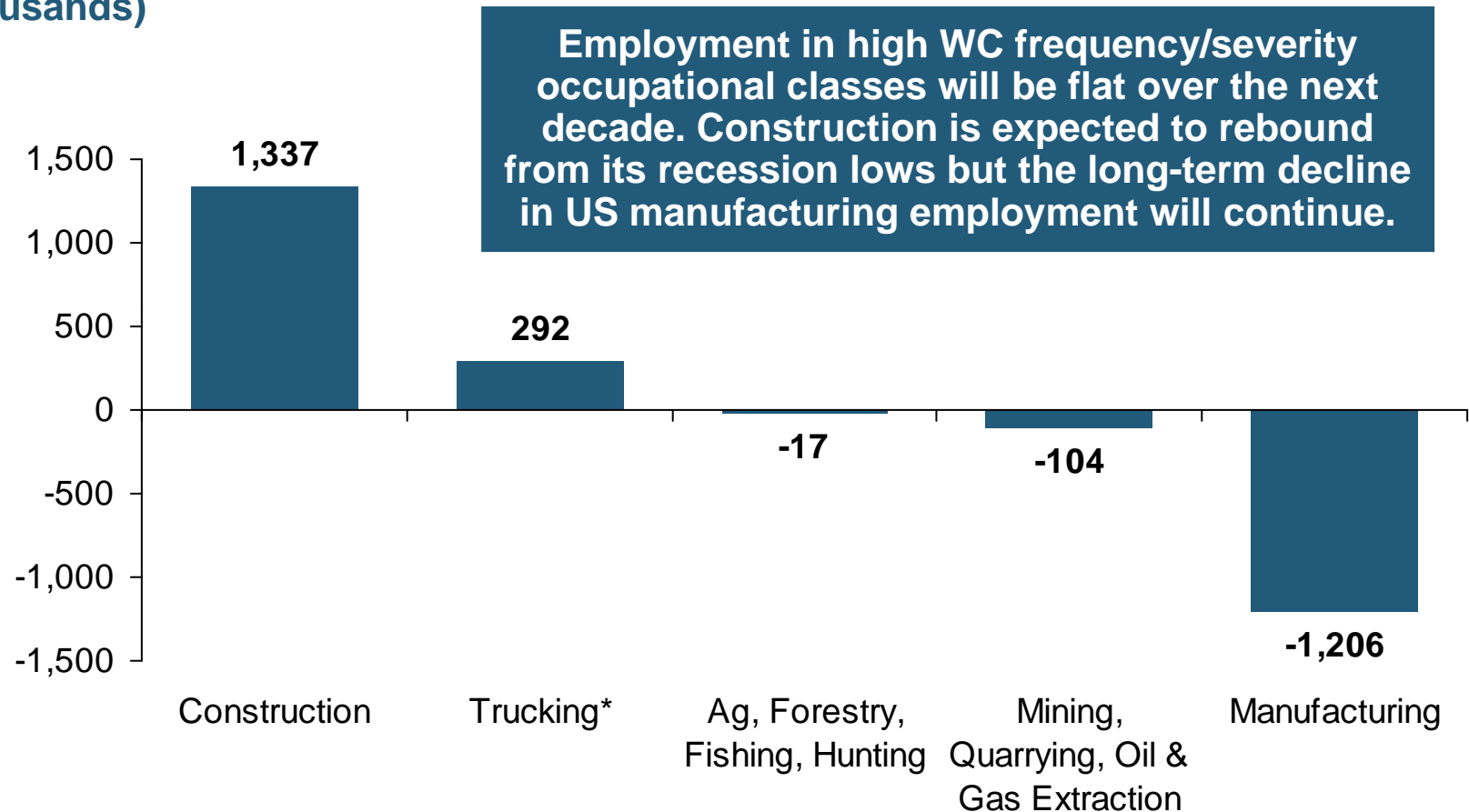
Numeric Change in Wage and Salary Employment in Service-Providing Industries: 2008-2018P

(Thousands)



Numeric Change in Wage & Salary Employment in Goods-Producing & Trucking Industries: 2008-2018P

(Thousands)

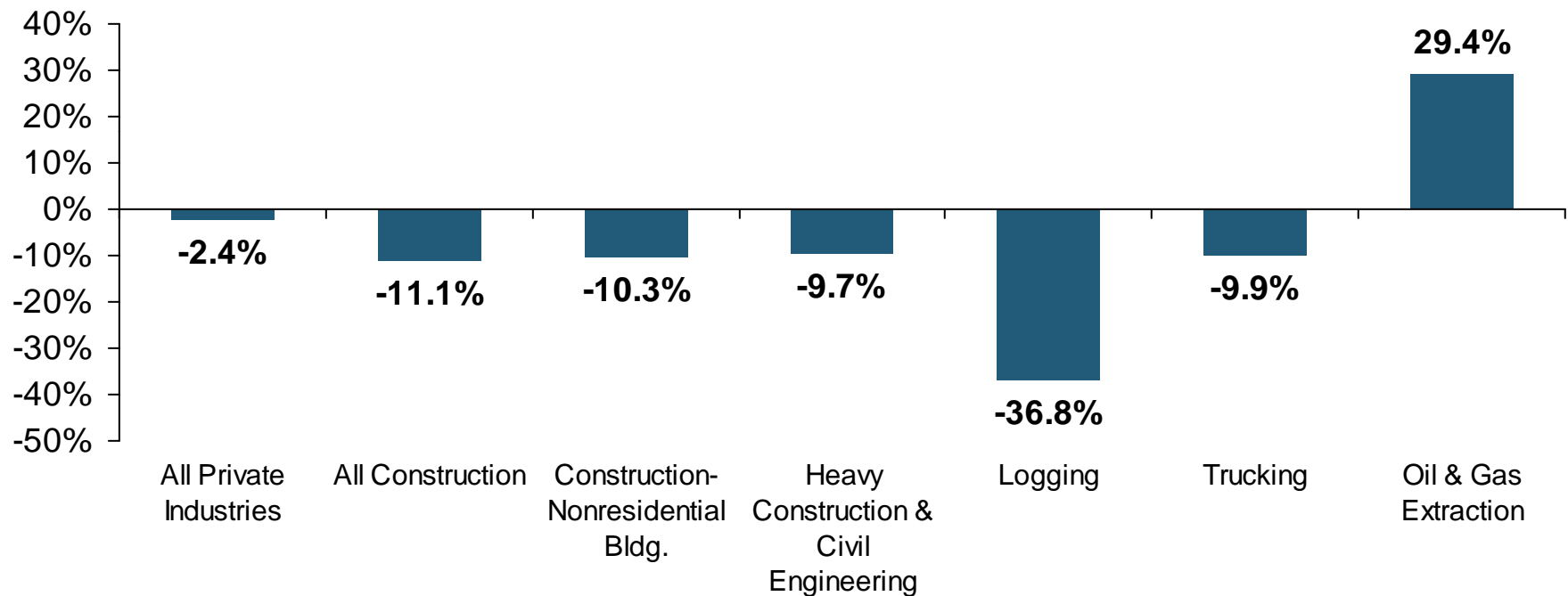


*Category includes truck drivers and drivers/sales personnel.

Sources: US Bureau of Labor Statistics: *Occupational Outlook Handbook, 2010-2011 Edition*; Insurance Information Institute

Many High Hazard Occupations Have Declined Disproportionately Over the Past Decade

Change in Employment (%), 2000 vs. 2009*



Most of the Loss of Jobs in High Hazard Classes Occurred Since 2007 with the Onset of the “Great Recession”

*I.I.I. calculations based on monthly seasonally adjusted data converted to annual averages.

Source: US Bureau of Labor; Insurance Information Institute.

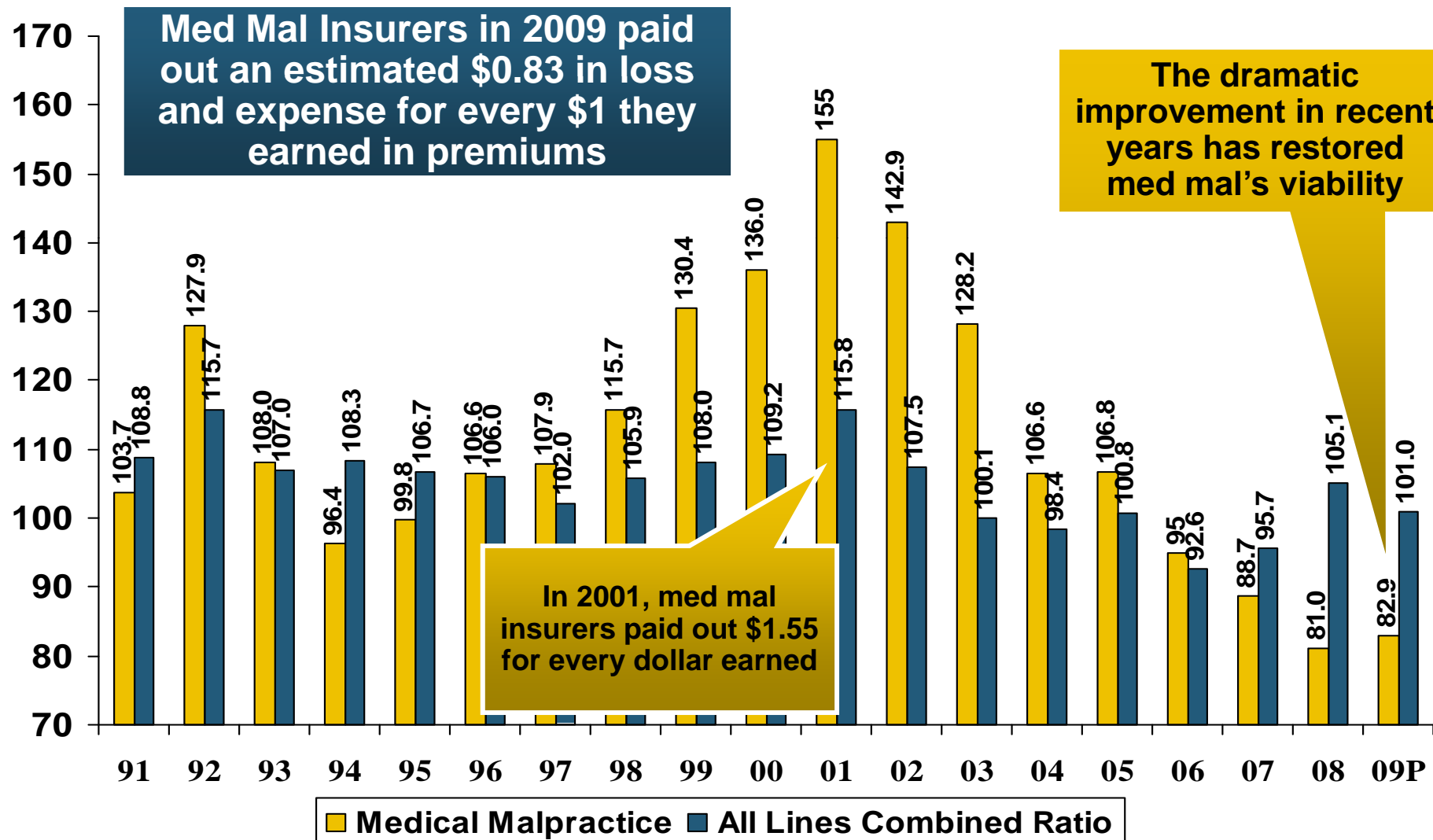
Medical Professional Liability

What a Difference a Few Years Makes

Trends & Challenges in Medical Professional Liability Insurance

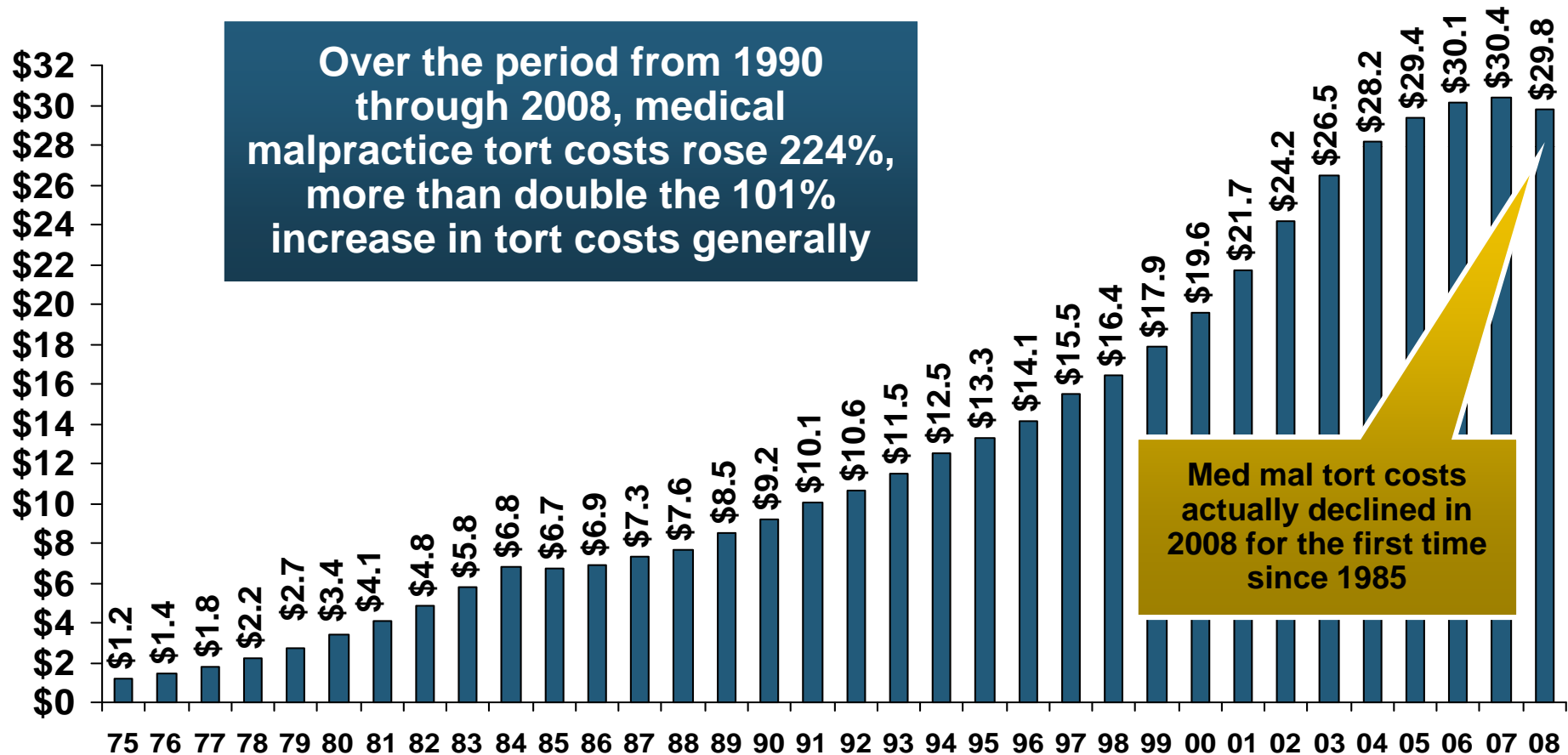
- Continued Stable/Moderate Loss Frequency
- Minimal/Small Growth in Claim Severity
- Continued Prior-Year Reserve Development Leading to Reserve Releases
- Continued Improvements in Loss Control and Risk Management Among Medical Professionals
- Investments More Stable than Industry Overall
- Very Price Competitive Environment
- Challenges to Tort Reform in Several Jurisdictions (e.g. IL, GA)
 - ◆ Caps were struck down in the past in OR, NH and WI
 - ◆ WA Supreme Court: No certificate of merit needed for plaintiff to pursue suit

Medical Malpractice Combined Ratio

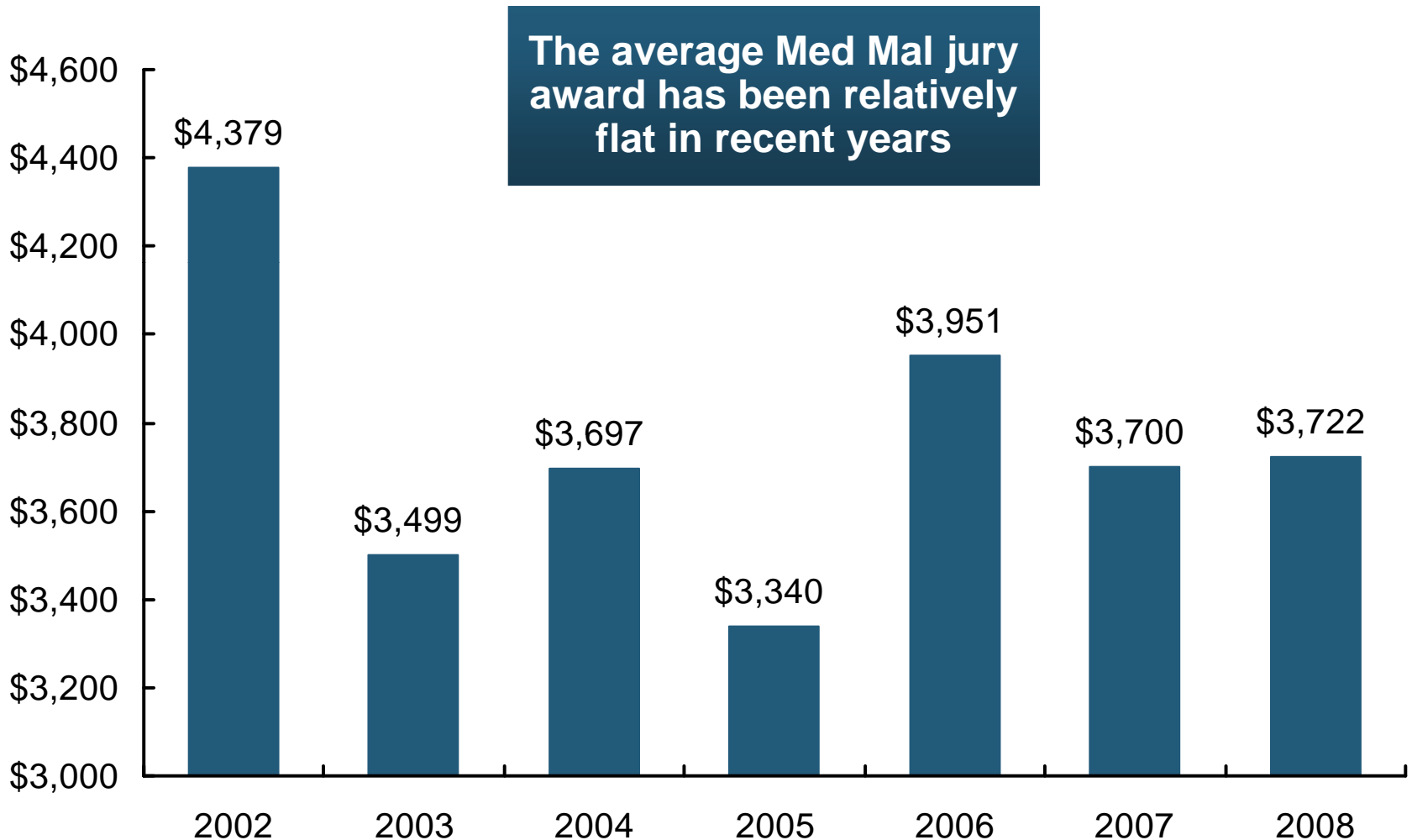


Medical Malpractice Tort Cost: Growth Continues, Though Modestly

(\$ Billions)



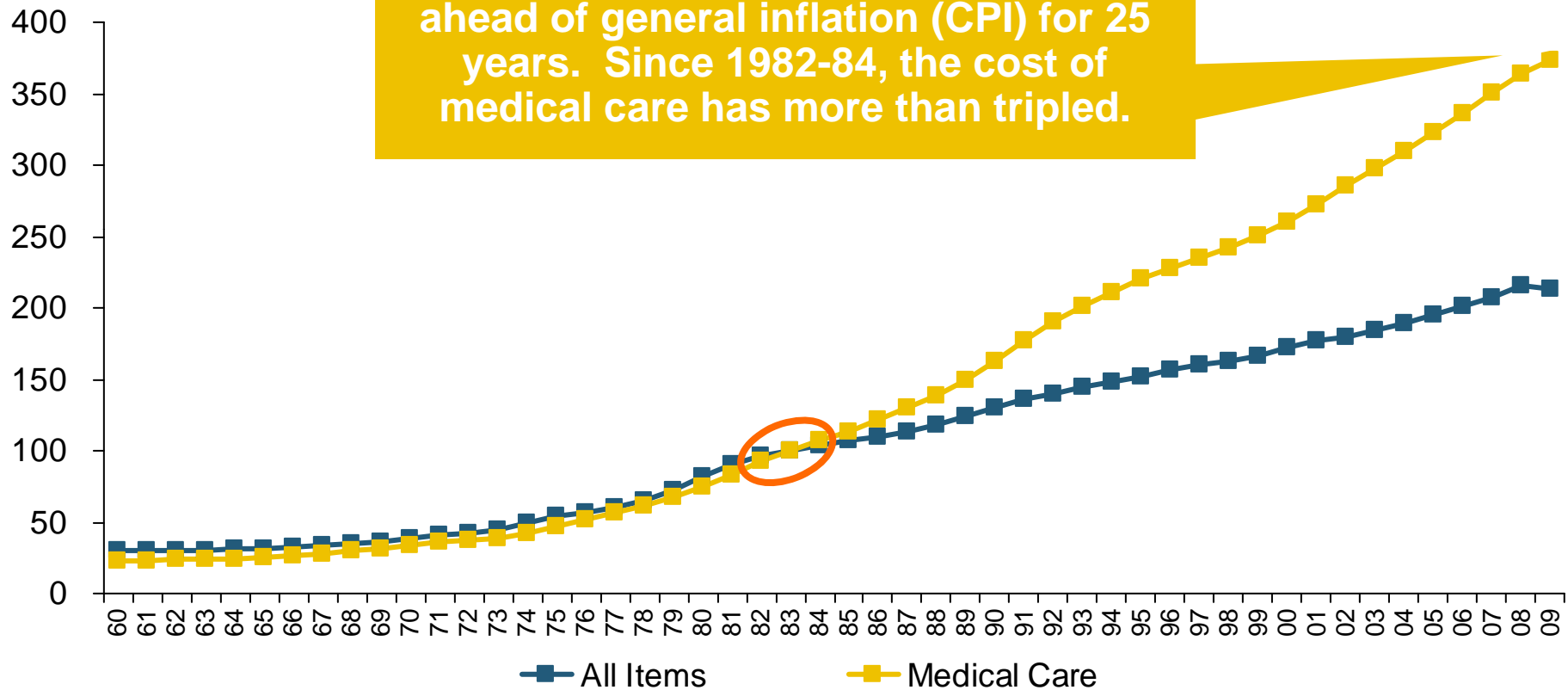
Average Medical Malpractice Jury Award: 2002 - 2008



Consumer Price Index for Medical for All Items vs. Medical Care, 1960-2009*

(1982-1984 = 100)

Medical Care inflation has been surging ahead of general inflation (CPI) for 25 years. Since 1982-84, the cost of medical care has more than tripled.



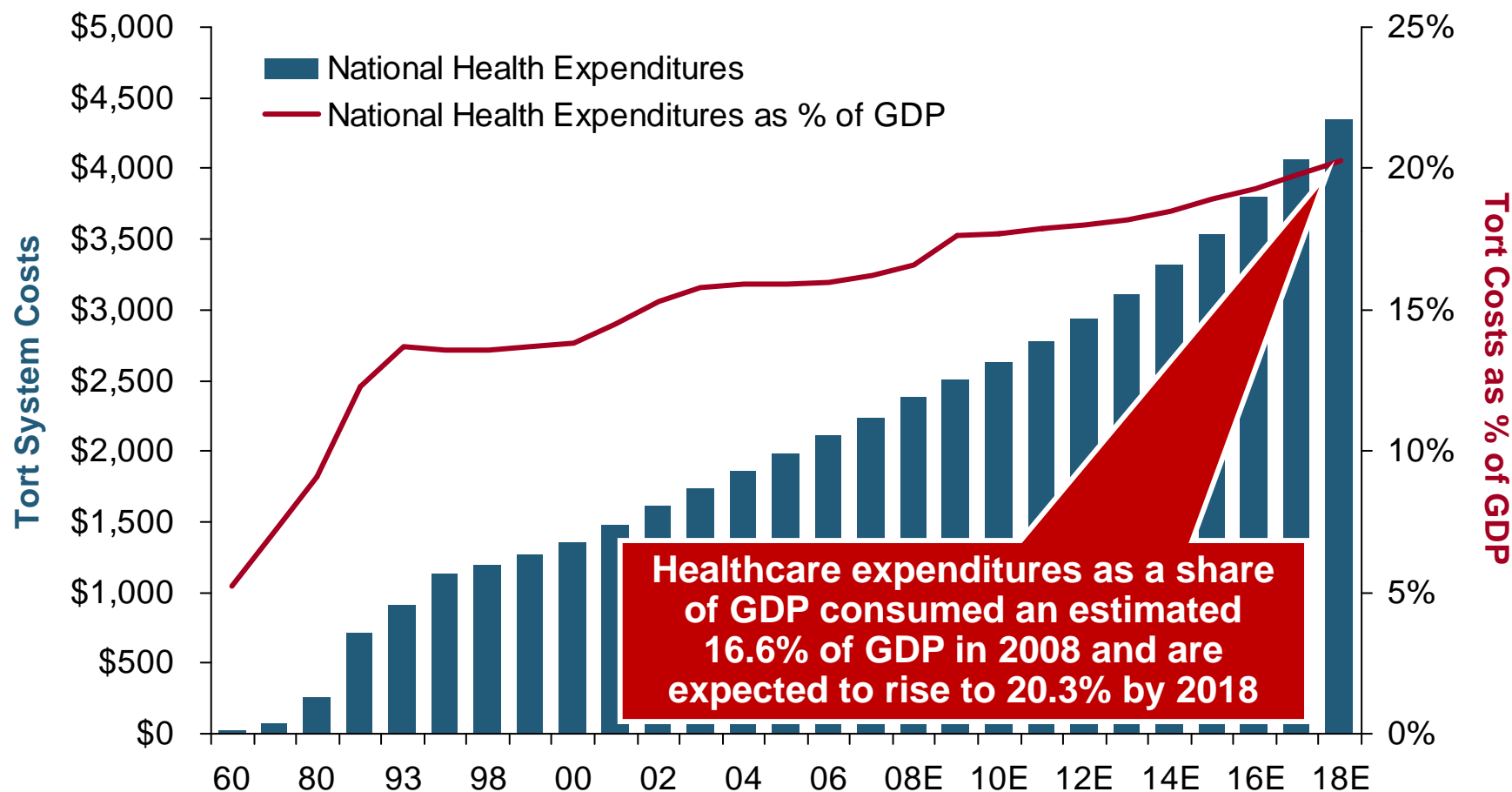
Medical Costs Will Continue to Rise Relatively Rapidly Despite Healthcare Reform

* Through June 30, 2009

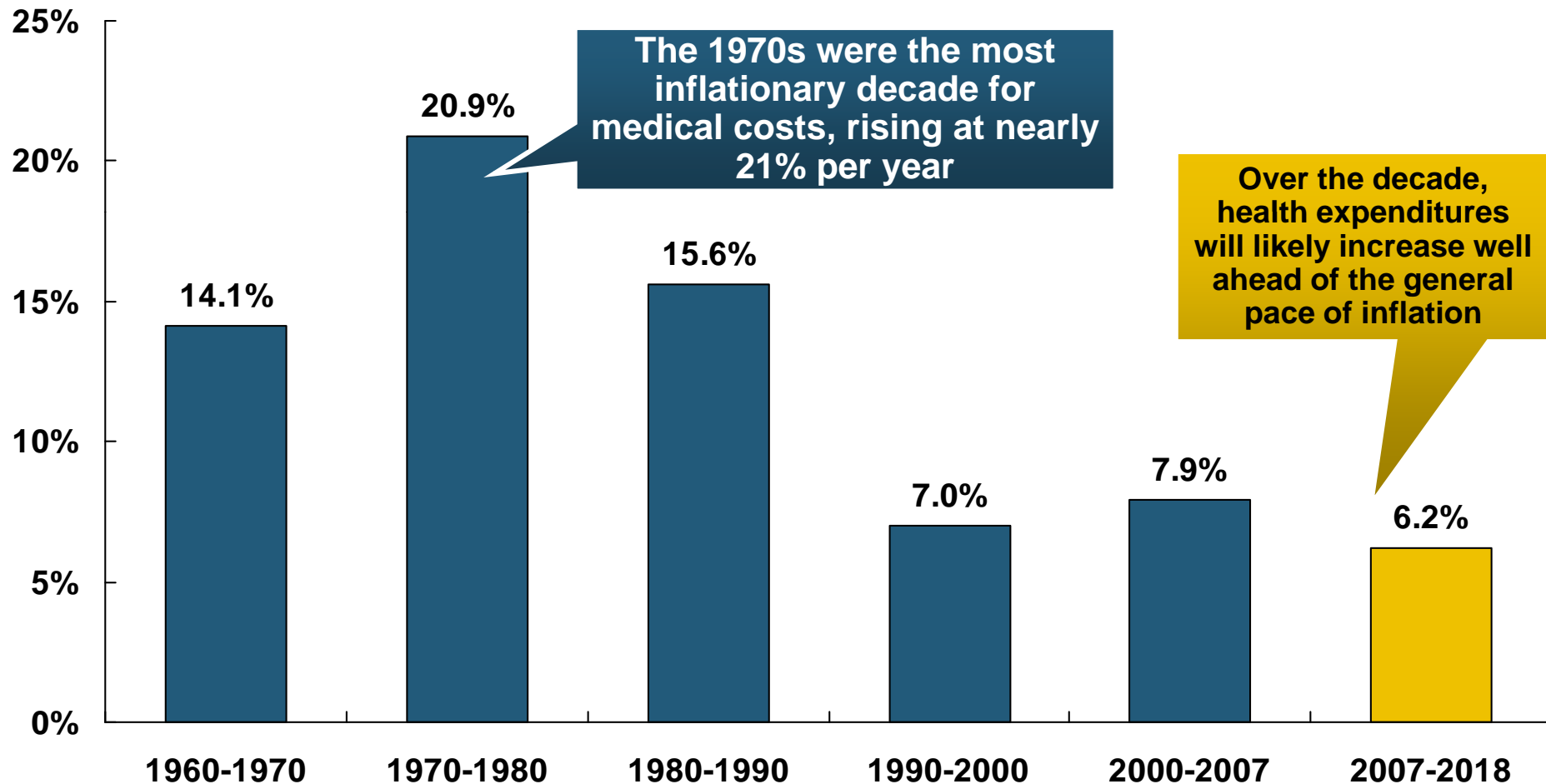
Sources: Bureau of Labor Statistics, Insurance Information Institute

National Health Expenditures and Expenditures as a Share of GDP, 1960-2018E

(\$ Billions)



Average Annual Growth in US Per Capita Health Care Costs, 1960-2018F



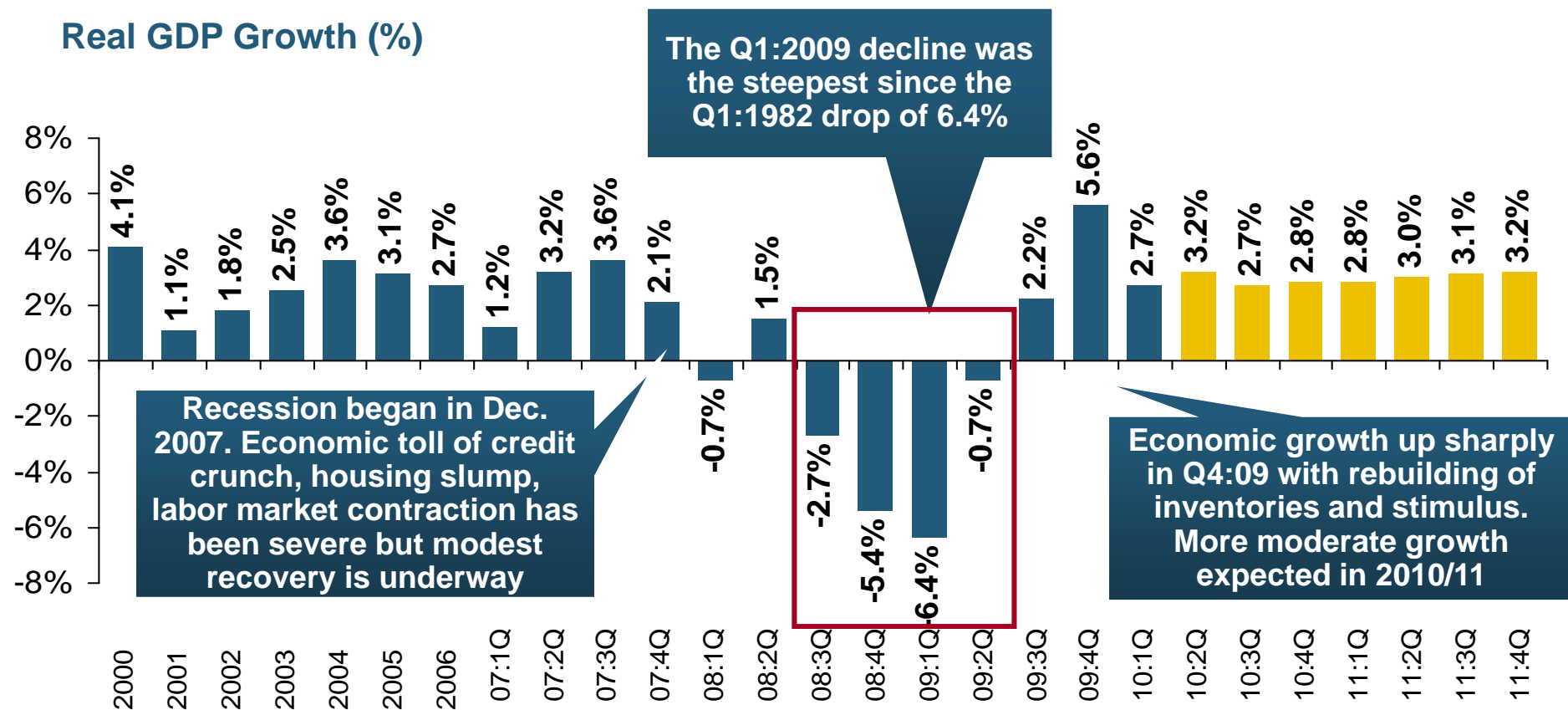
Source: Insurance Information Institute calculations based on data from the Centers for Medicare & Medicaid Services, Office of the Actuary.

The Economic Storm

**What the Financial Crisis and
Recession Mean for the Industry's
Exposure Base, Growth and
Profitability**

US Real GDP Growth: Exerts a Strong Influence on Energy Demand*

Real GDP Growth (%)



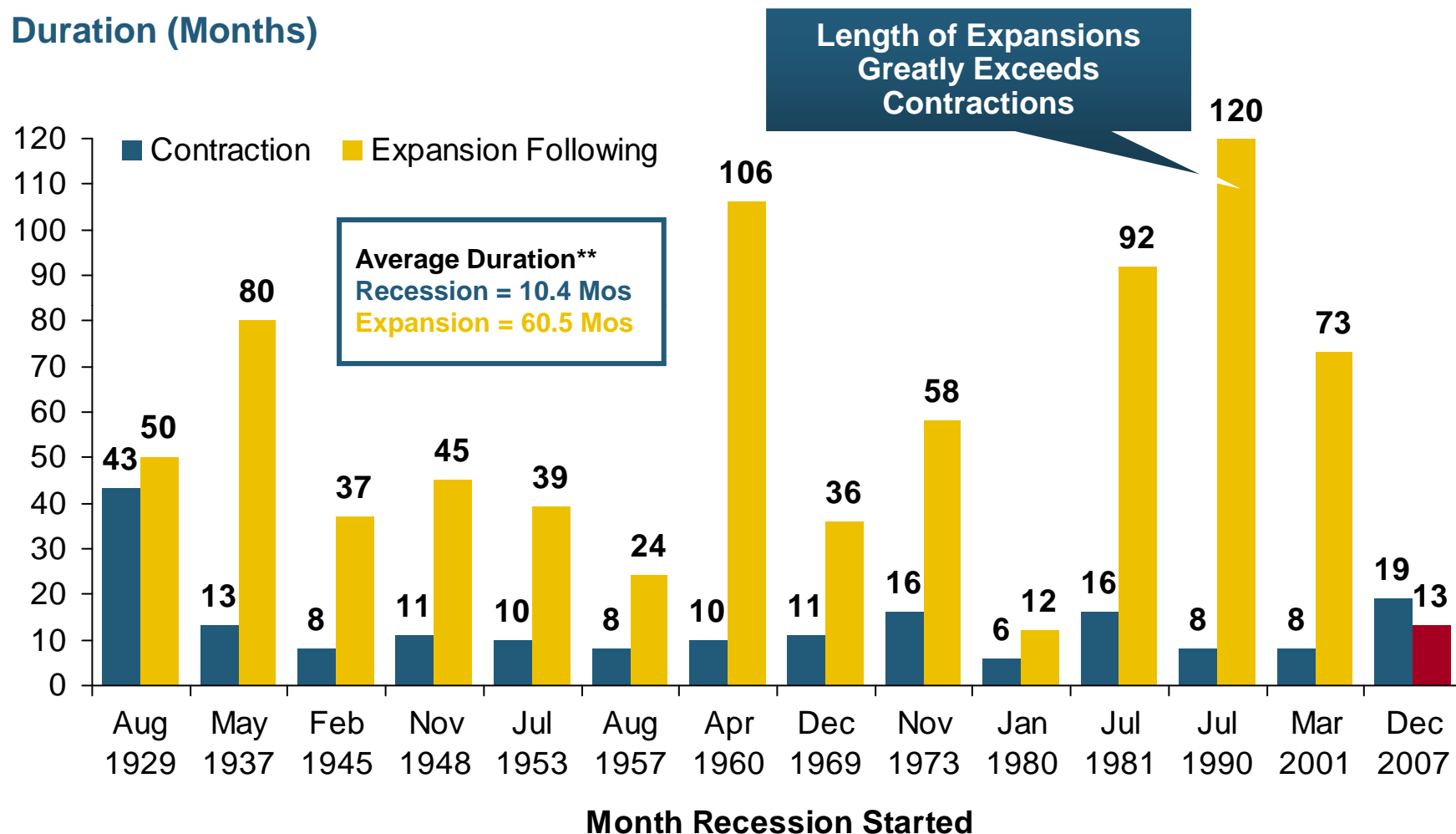
Demand for Energy and Commercial Insurance Have Been Impacted by Sluggish Economic Conditions

* ■ Estimates/Forecasts from Blue Chip Economic Indicators.

Source: US Department of Commerce, Blue Economic Indicators 7/10; Insurance Information Institute.

Length of US Business Cycles, 1929–Present*

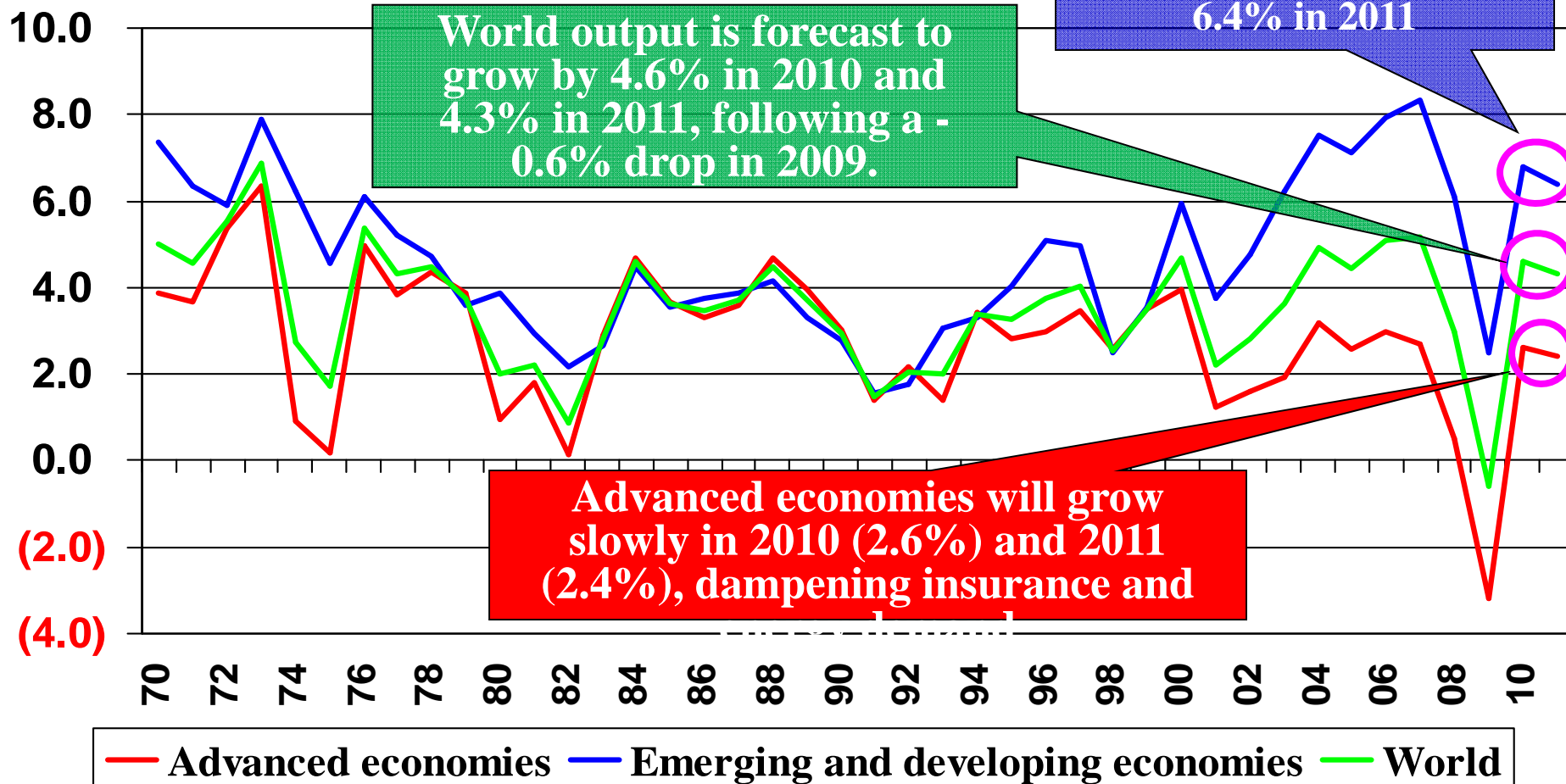
Duration (Months)



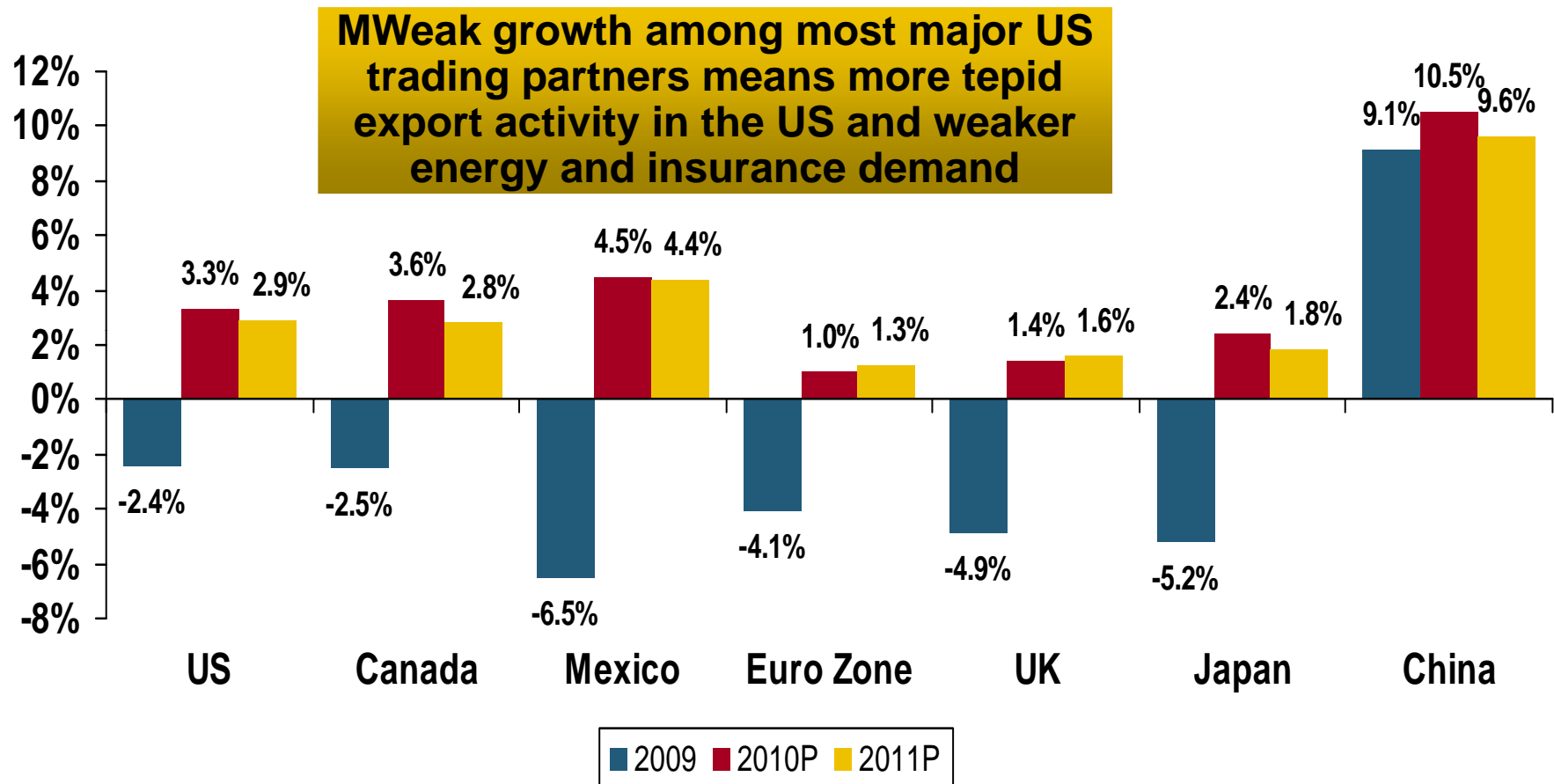
* Through July 2010. Assumes “official” end of recession was June 2009. ** Post-WW II period through end of most recent expansion.
 Sources: National Bureau of Economic Research; Insurance Information Institute.

GDP Growth: Advanced & Emerging Economies vs. World, 1970-2011F

GDP Growth (%)



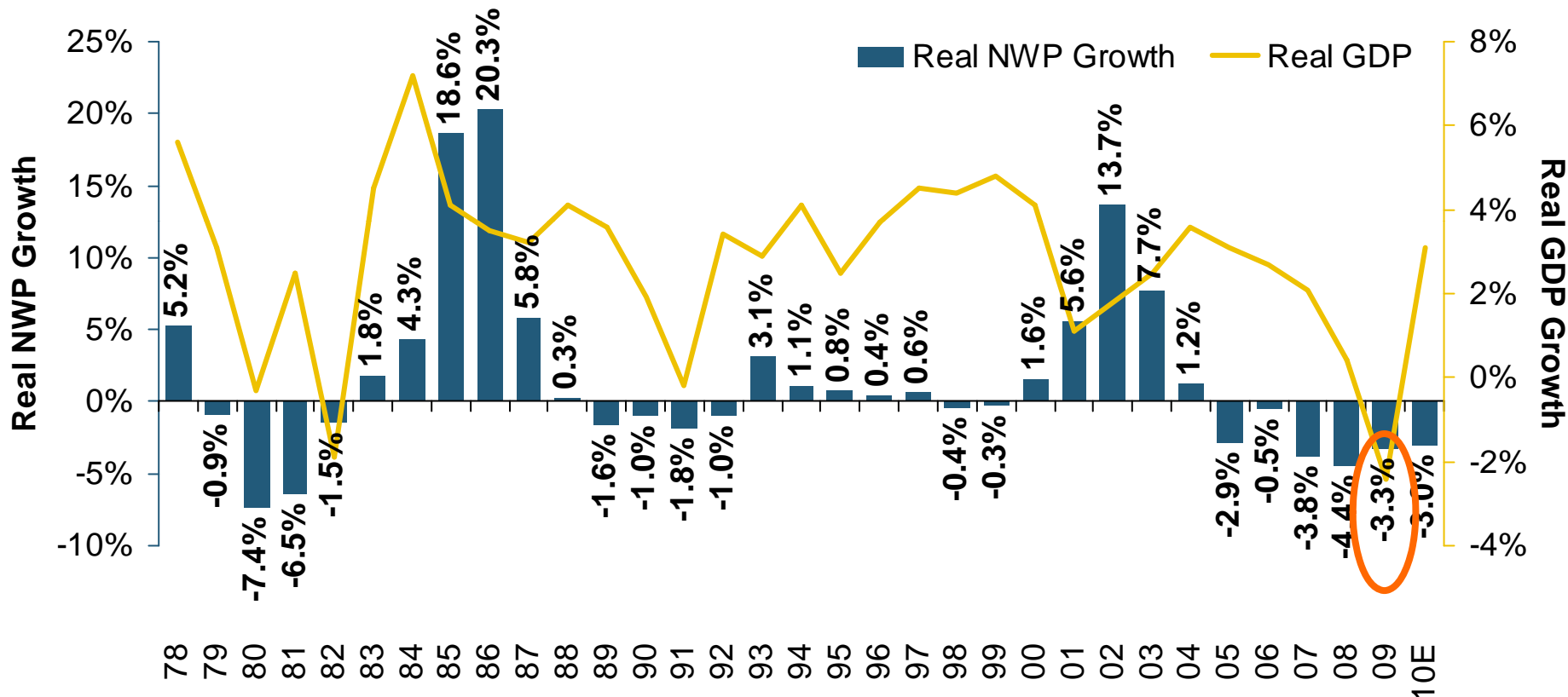
Economic Growth: US & Major Trading Partners: 2009-2011P



Outlook uncertain: The world economy is recovering from the global crisis, but at different speeds in different parts of the world. Insurance and energy demand will vary regionally and by industry.

Real GDP Growth vs. Real P/C Premium Growth: Modest Association

Real GDP Growth vs. Real P/C (%)



**P/C Insurance Industry's Growth is Influenced Modestly
by Growth in the Overall Economy**

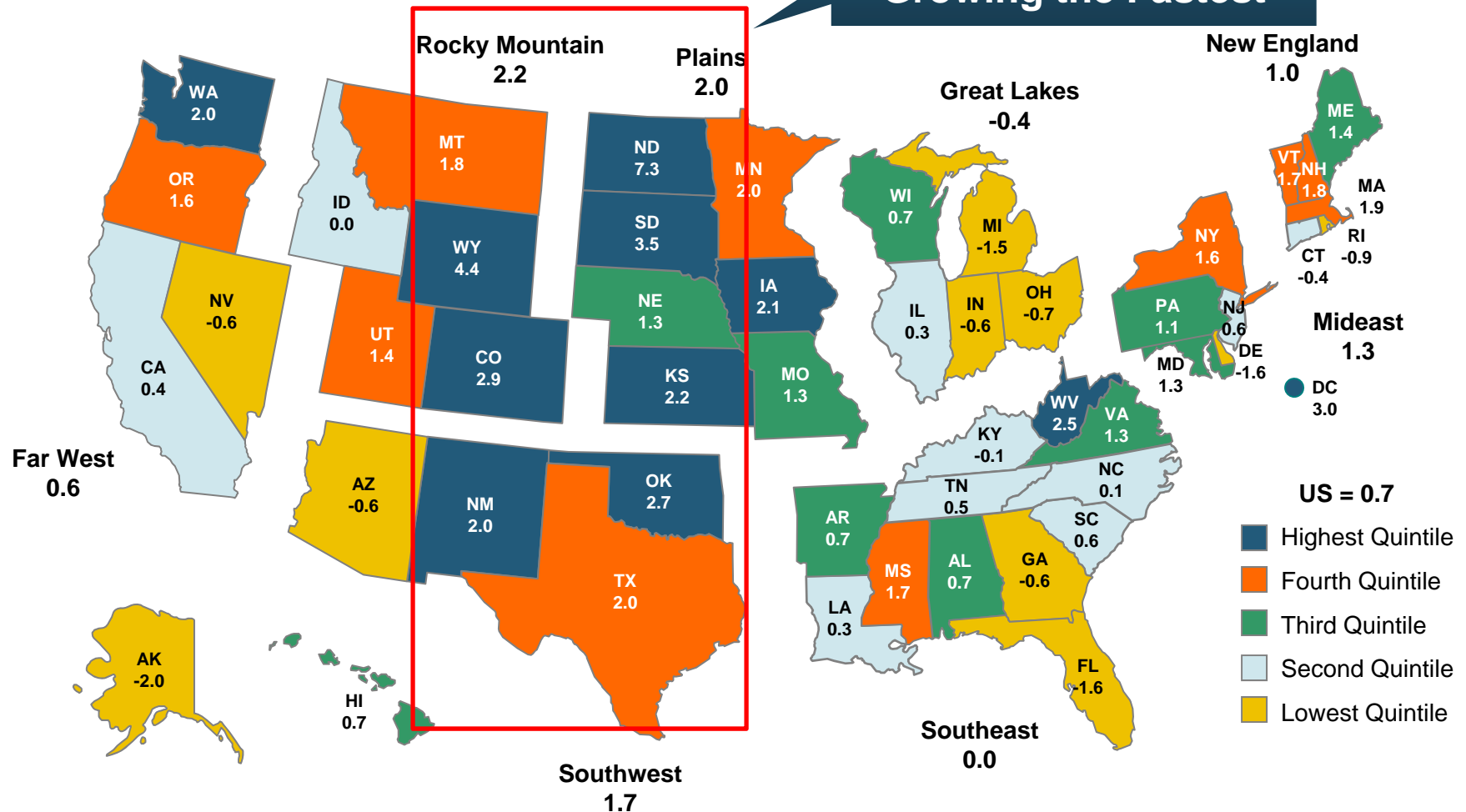
Regional Differences Will Significantly Impact P/C Markets

**Recovery in Some Areas Will
Begin Years Ahead of Others
and Speed of Recovery Will Differ
by Orders of Magnitude**

State Economic Growth Varied Tremendously in 2008

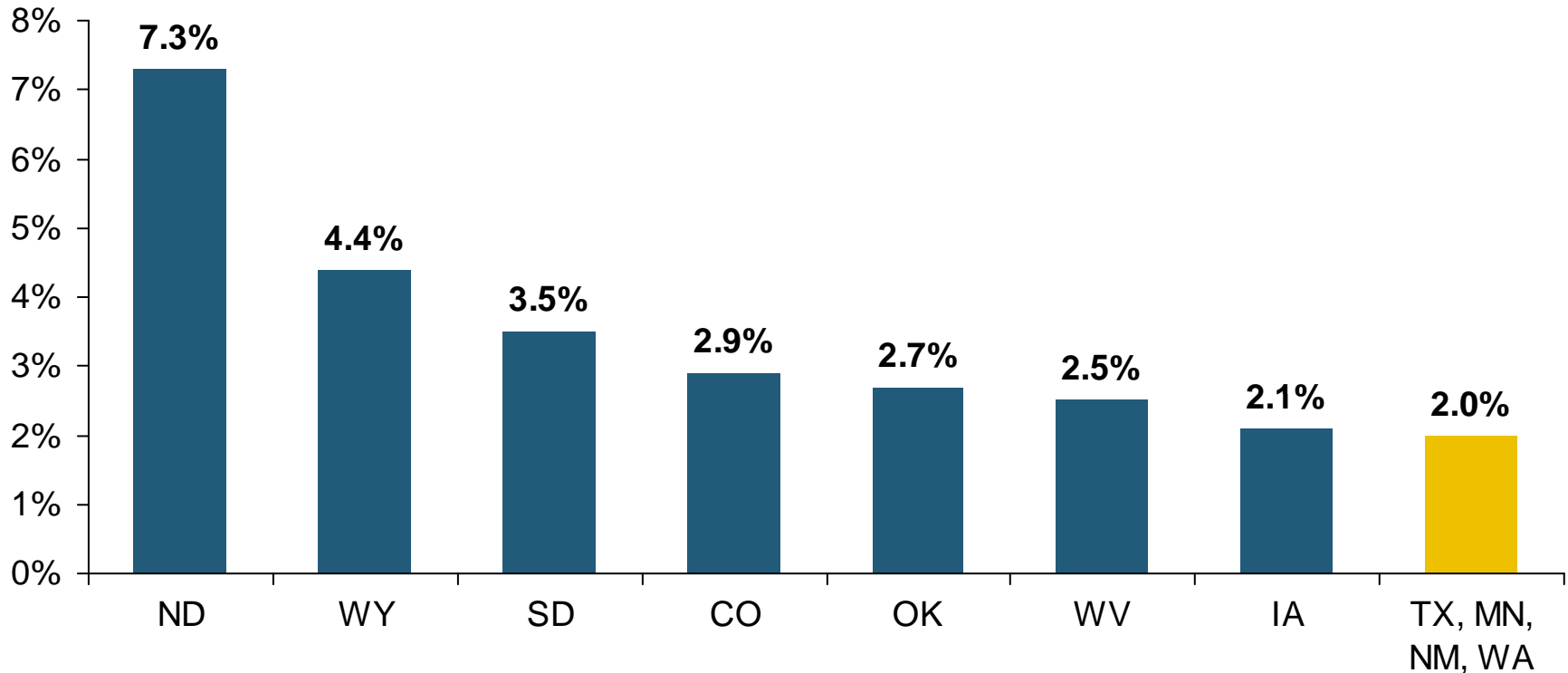
Percent Change in Real GDP by State, 2007–2008

**Mountain, Plains States
Growing the Fastest**



Fastest Growing States in 2008: Plains, Mountain States Lead

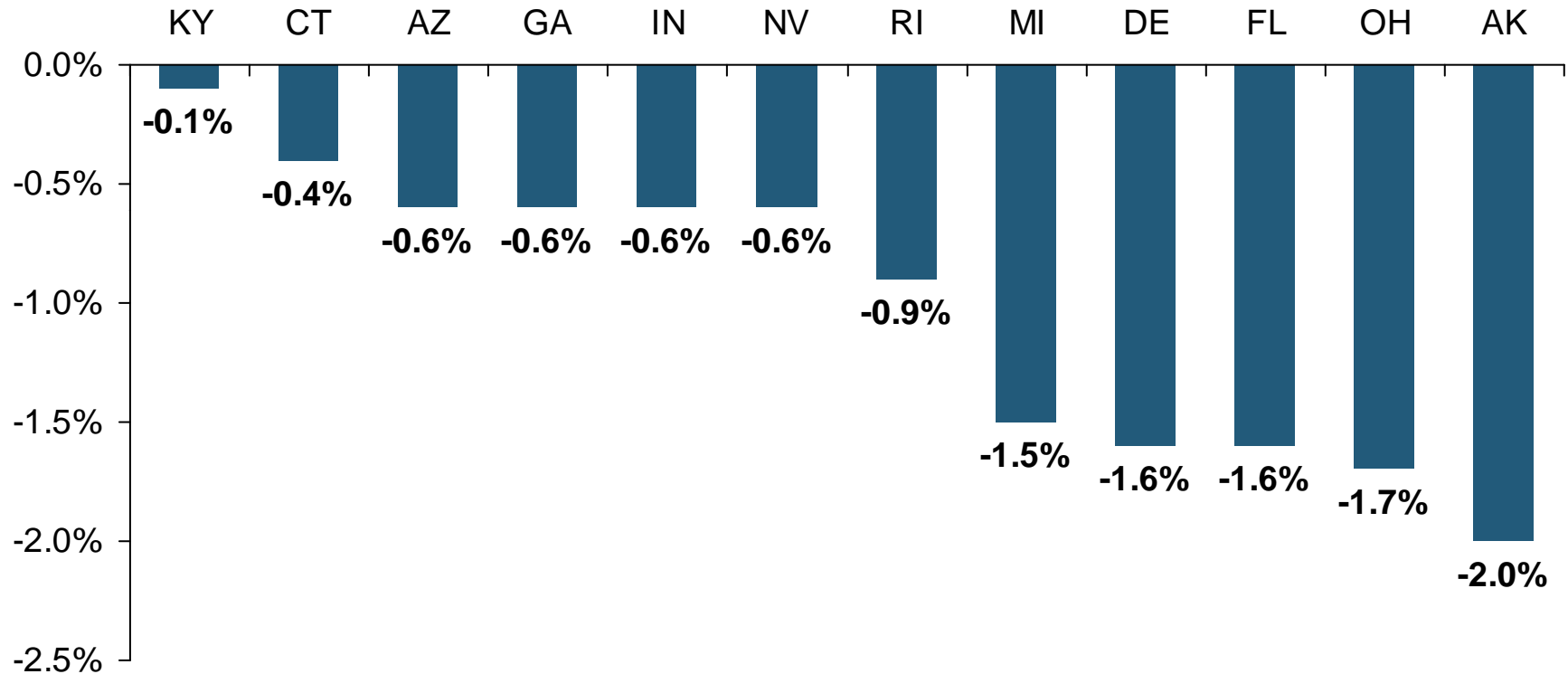
Real State GDP Growth (%)



Natural Resource and Agricultural States Have Done Better Than Most Others Recently, Helping Insurance Exposure in Those Areas

Slowest Growing States in 2008: Diversity of States Suffering

Real State GDP Growth (%)



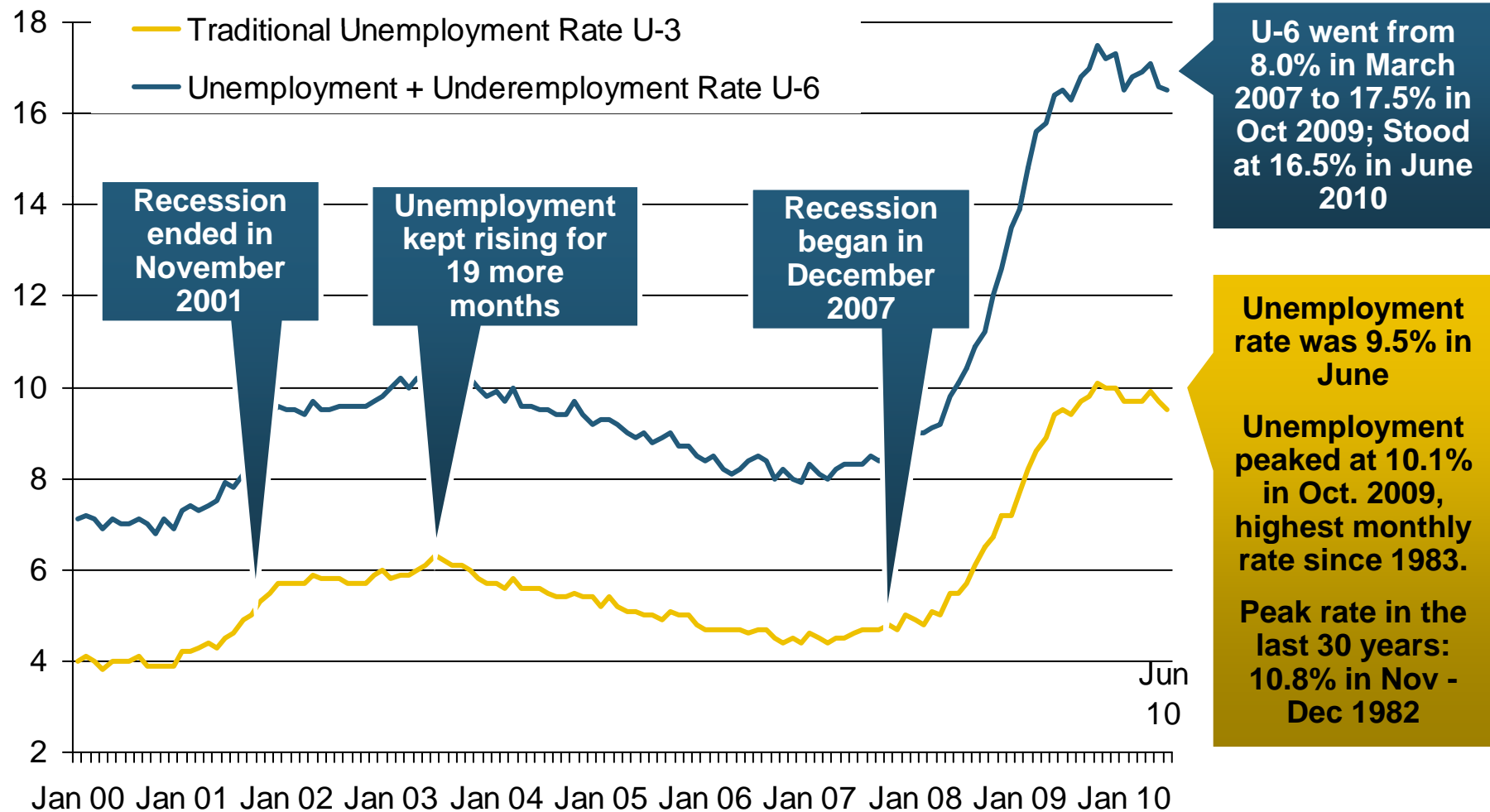
**States in the North, South, East and West All Represented Among
Hardest Hit, But for Differing Reasons**

Labor Market Trends

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

Unemployment and Underemployment Rates: Rocketed Up in 2008-09; Stabilizing in 2010?

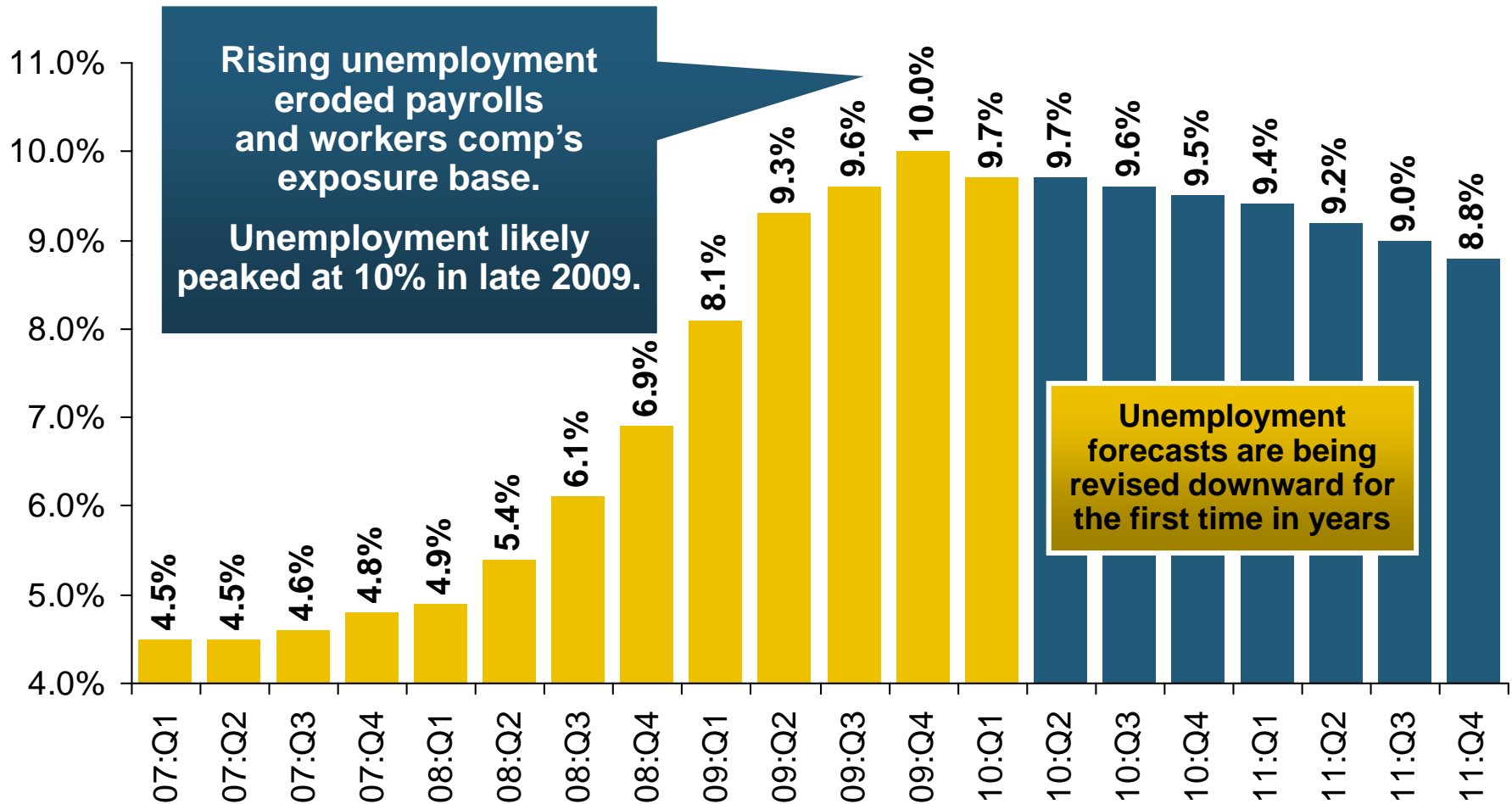
January 2000 through June 2010, Seasonally Adjusted (%)



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

US Unemployment Rate

2007:Q1 to 2011:Q4F*

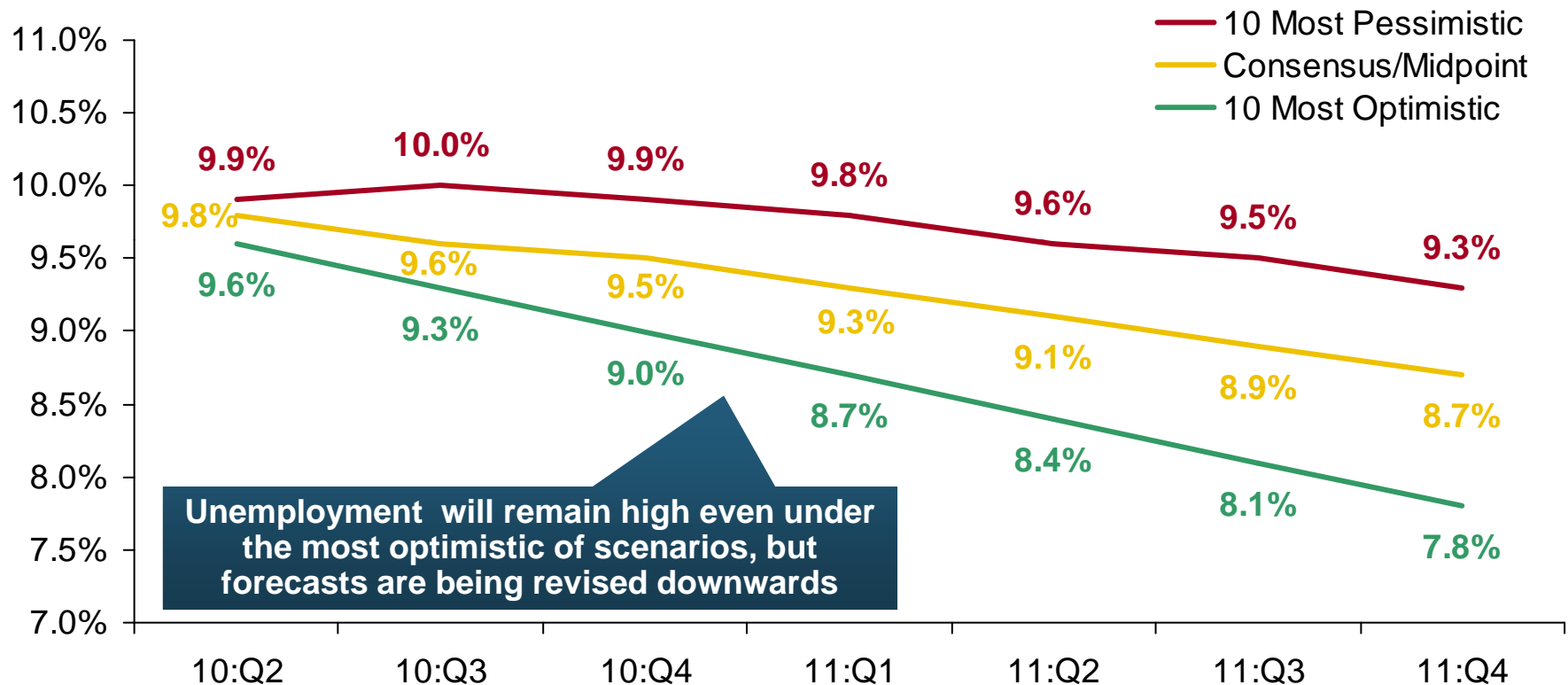


* ■ = actual; ■ = forecasts

Sources: US Bureau of Labor Statistics; Blue Chip Economic Indicators (7/10); Insurance Information Institute

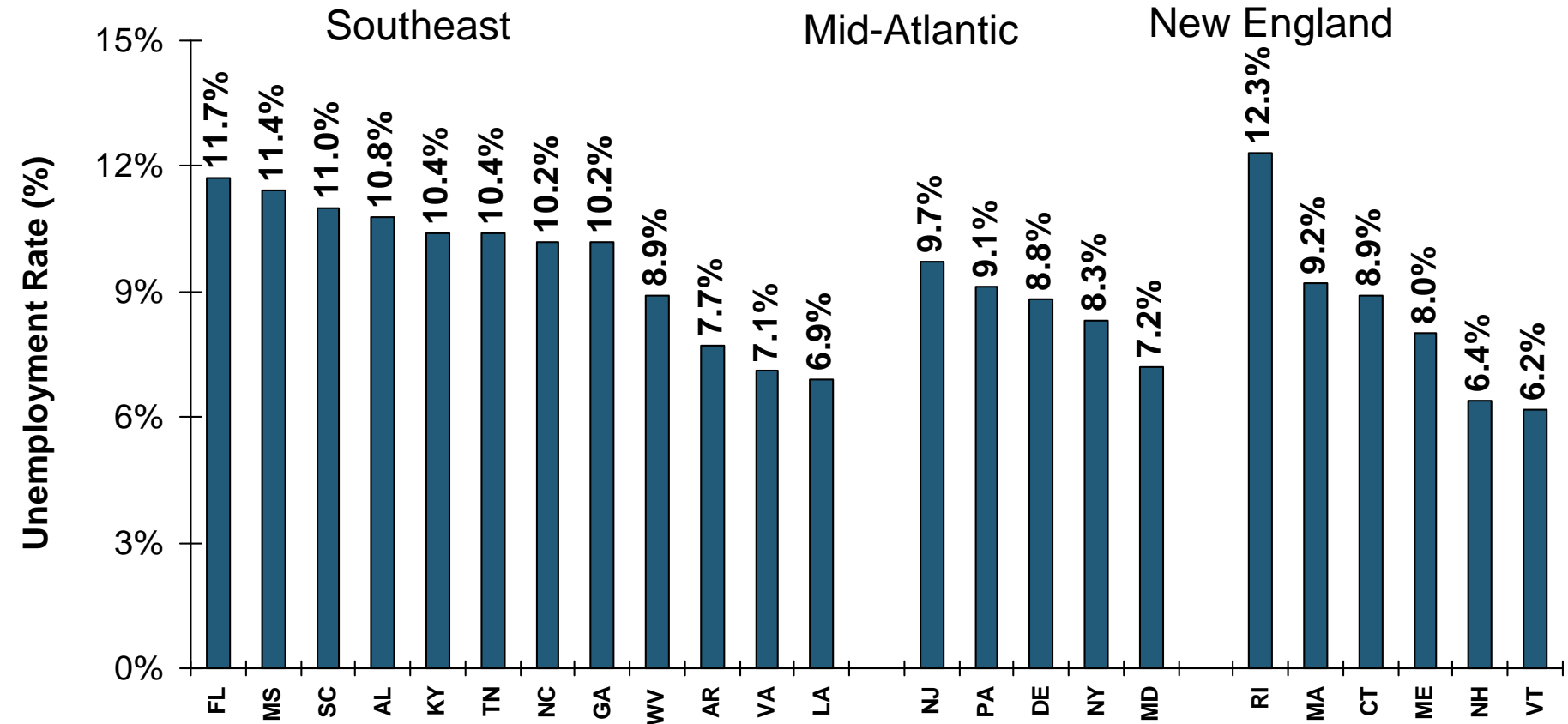
US Unemployment Rate Forecasts

Quarterly, 2010:Q1 to 2011:Q4



Stubbornly High Unemployment Will Slow the Recovery of the Workers Comp Exposure Base

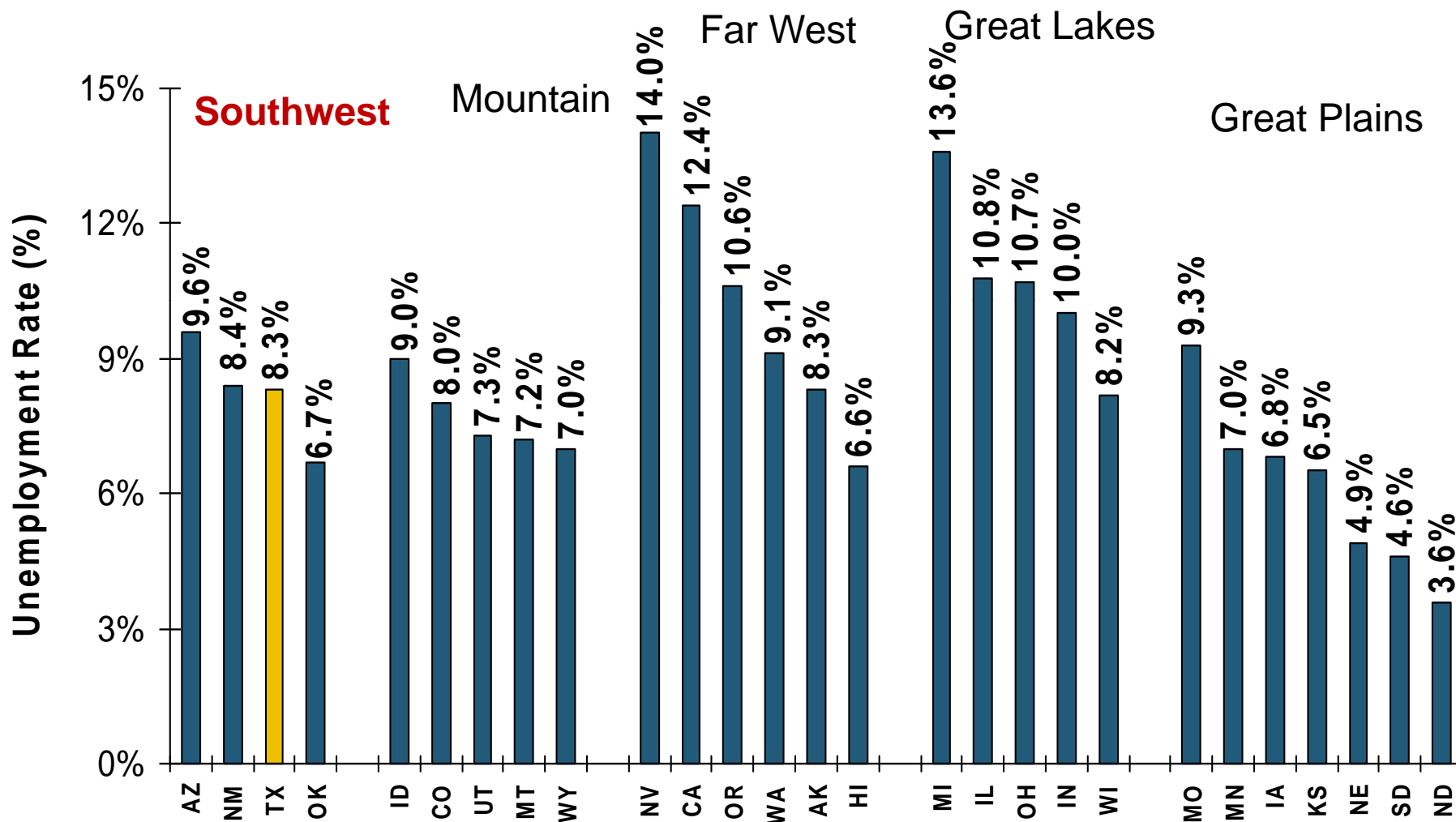
Unemployment Rates Vary Widely by State and Region*



*Provisional figures for May 2010, seasonally adjusted.

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

Unemployment Rates Vary Widely by State and Region* (cont'd)

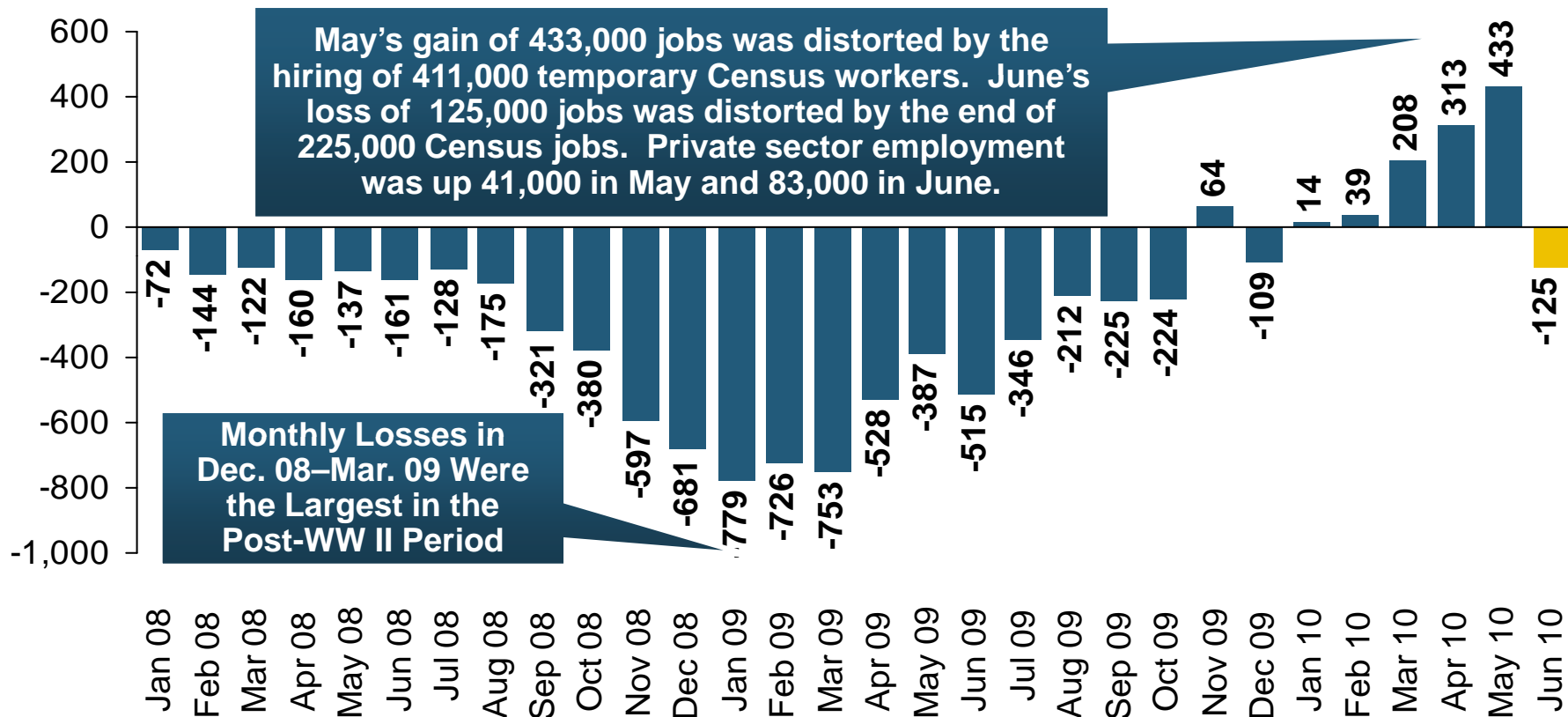


*Provisional figures for May 2010, seasonally adjusted.

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

Monthly Change Employment*

January 2008 through June 2010* (Thousands)



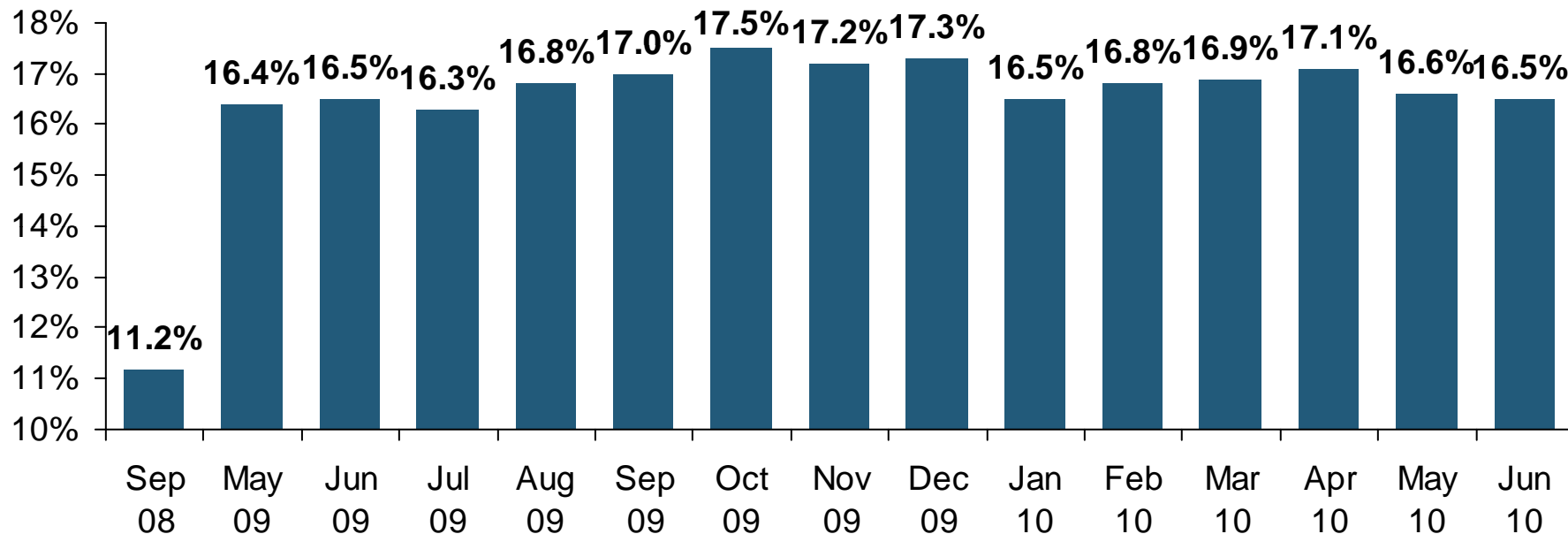
Job Losses Since the Recession Began in Dec. 2007 Peaked at 8.4 Mill in Dec. 09; Stands at 7.4 Million Through June 2010; 14.6 Million People are Now Defined as Unemployed

*Estimate based on Reuters poll of economists.

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

Labor Underutilization: Broader than Just Unemployment

% of Labor Force



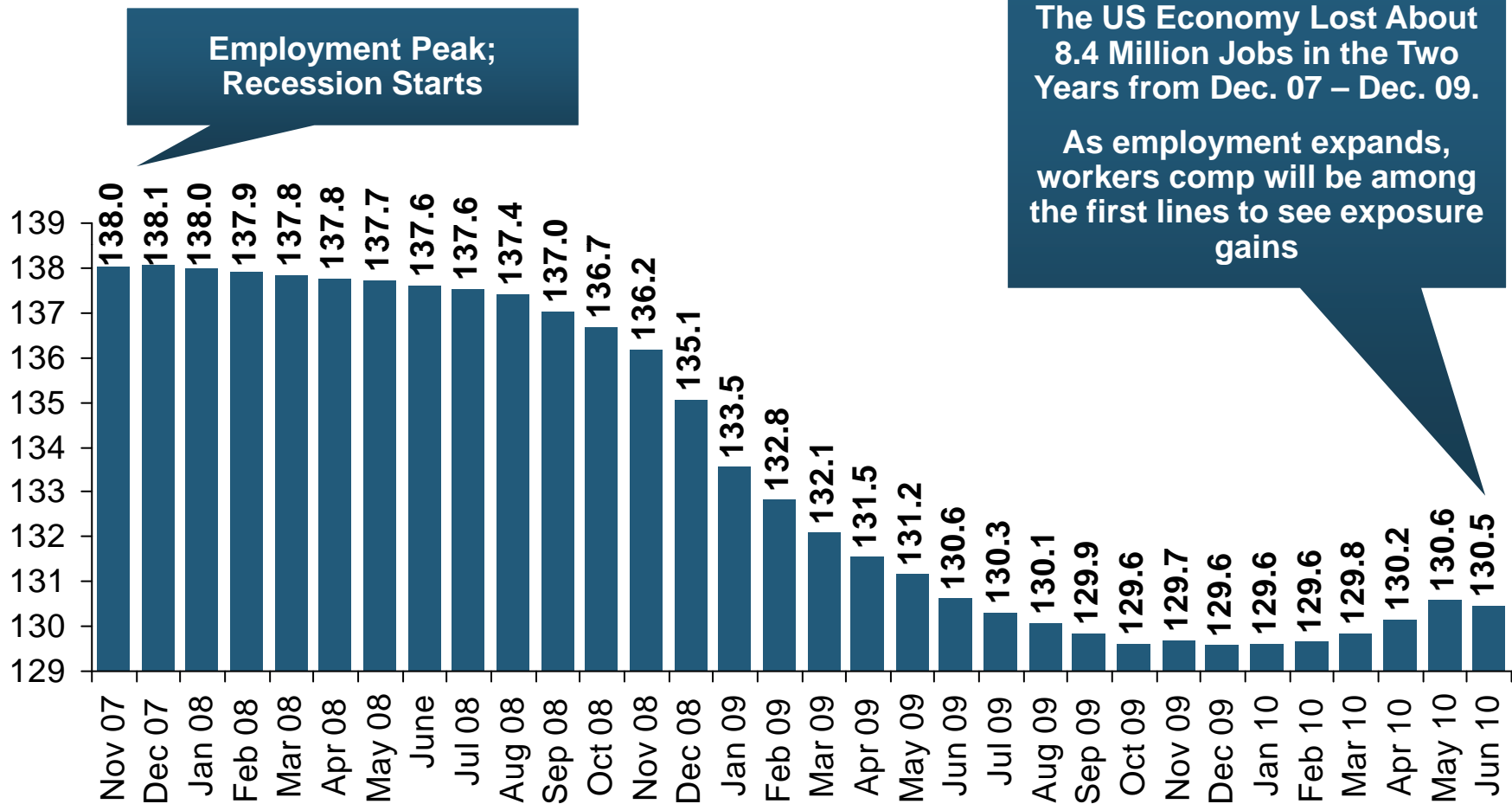
Marginally Attached and Unemployed Persons Account for 16.5% of the Labor Force in June 2010 (1 Out of 6 People). Unemployment Rate Alone was 9.5%. Underutilization Shows a Broader Impact on WC and Other Commercial Exposures

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 Nonfarm Private Employment

Monthly, Nov 2007 – June 2010 (Millions)

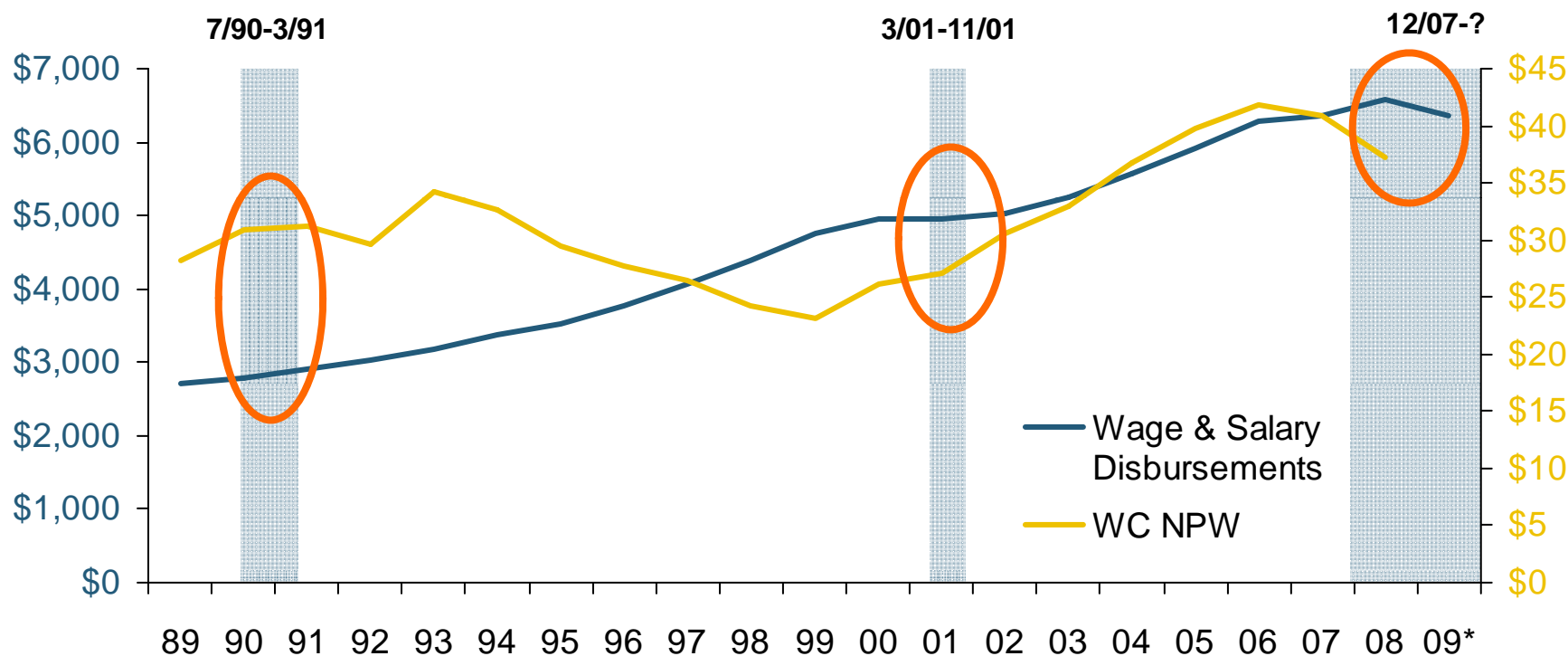


Seasonally adjusted.

Source: US Bureau of Labor Statistics

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

Wage & Salary Disbursement (Private Employment) vs. WC NWP (\$ Billions)

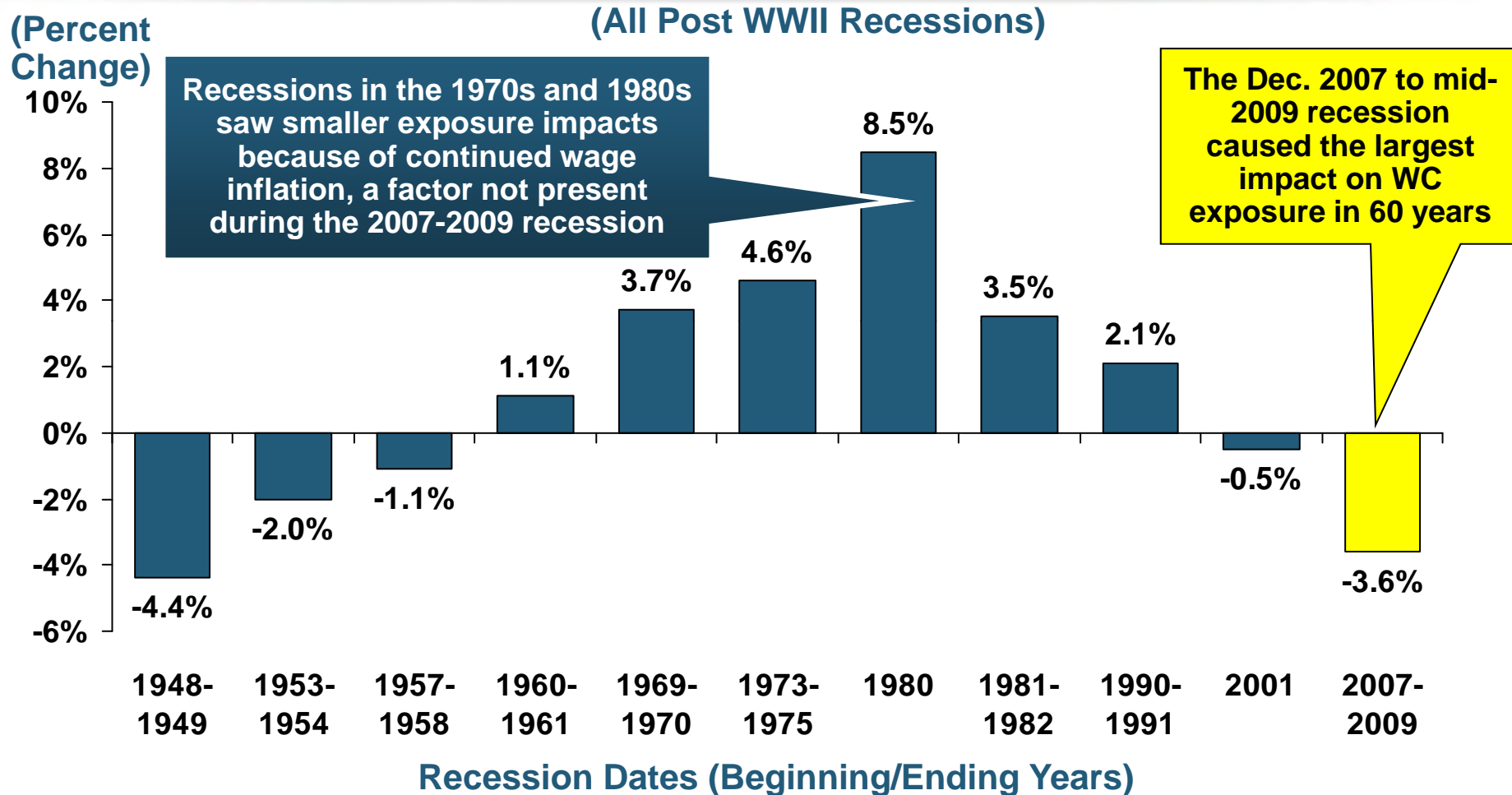


Weakening Payrolls Have Eroded \$2B+ in Workers Comp Premiums

* Average Wage and Salary data as of 10/1/2009. Shaded areas indicate recessions

Source: US Bureau of Economic Analysis; Federal Reserve Bank of St. Louis at <http://research.stlouisfed.org/fred2/series/WASCUR> ; I.I.I. Fact Books

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

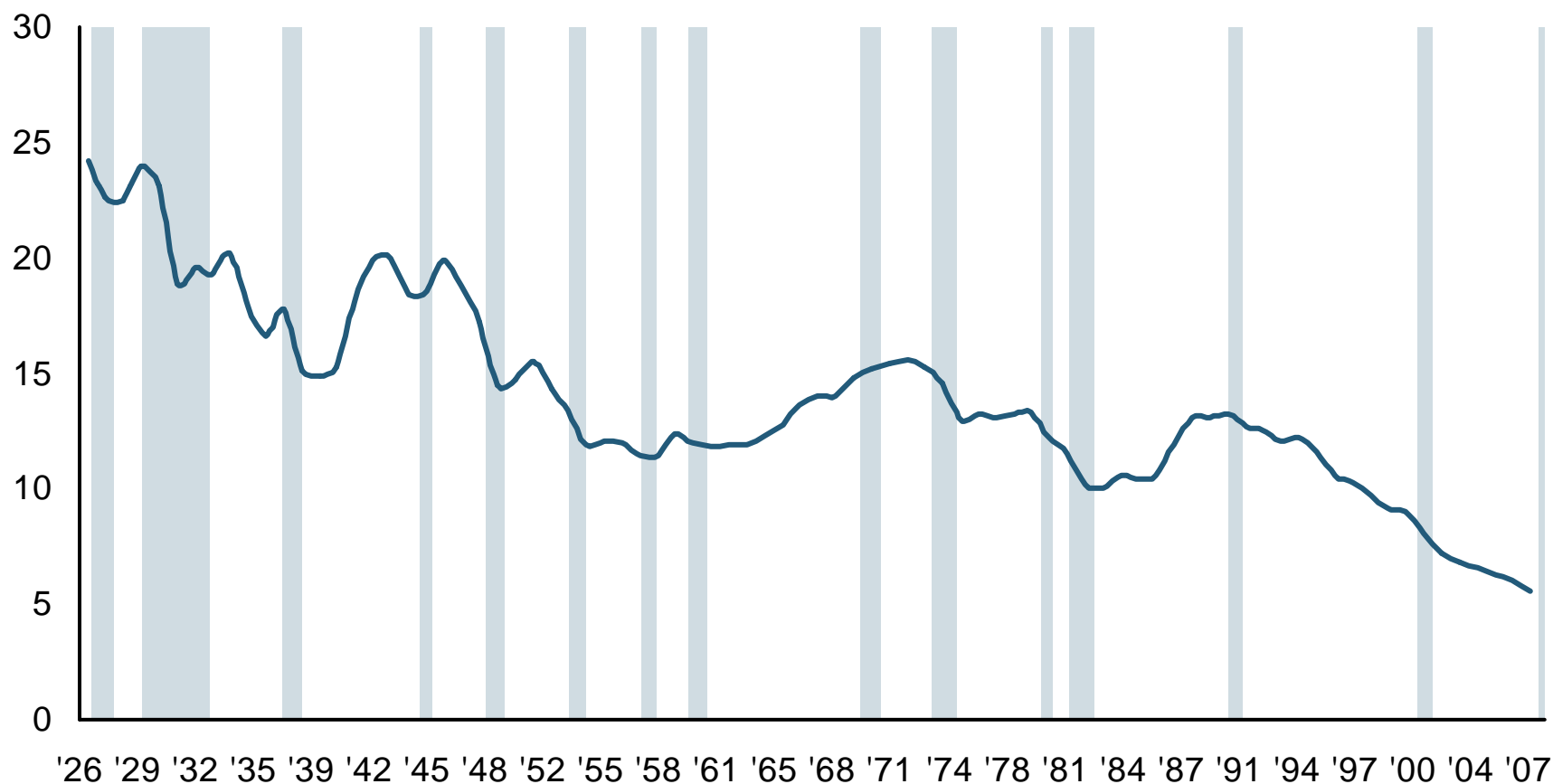


*Data represent maximum recorded decline over 12-month period using annualized quarterly wage and salary accrual data
Source: Insurance Information Institute research; Federal Reserve Bank of St. Louis (wage and salary data); National Bureau of Economic Research (recession dates).

Frequency: 1926–2008

A Long-Term Drift Downward

Manufacturing – Total Recordable Cases
Rate of Injury and Illness Cases per 100 Full-Time Workers



Note: Recessions indicated by gray bars.

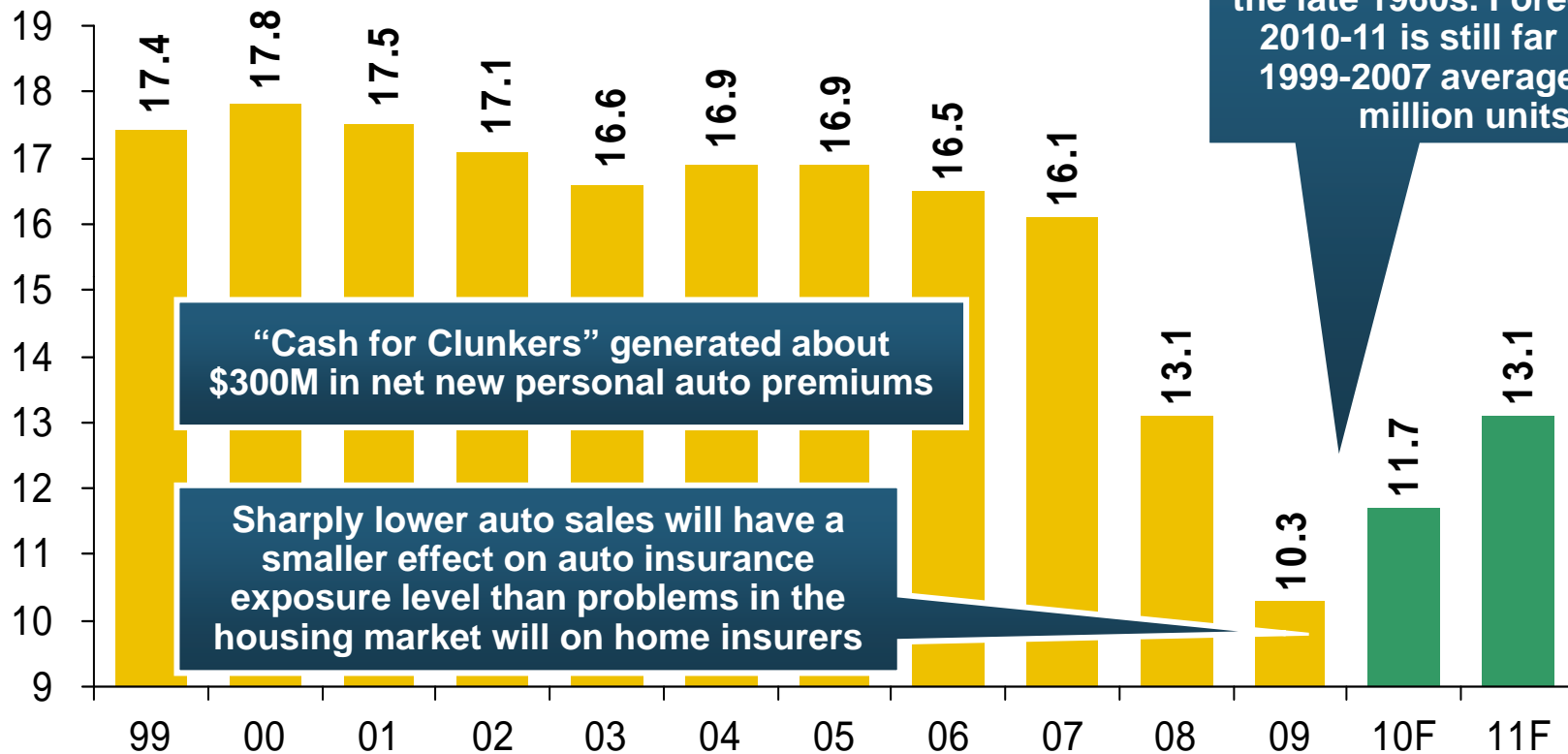
Sources: NCCI from US Bureau of Labor Statistics; National Bureau of Economic Research

Crisis-Driven Exposure Drivers

**Economic Obstacles
to Growth in P/C Insurance**

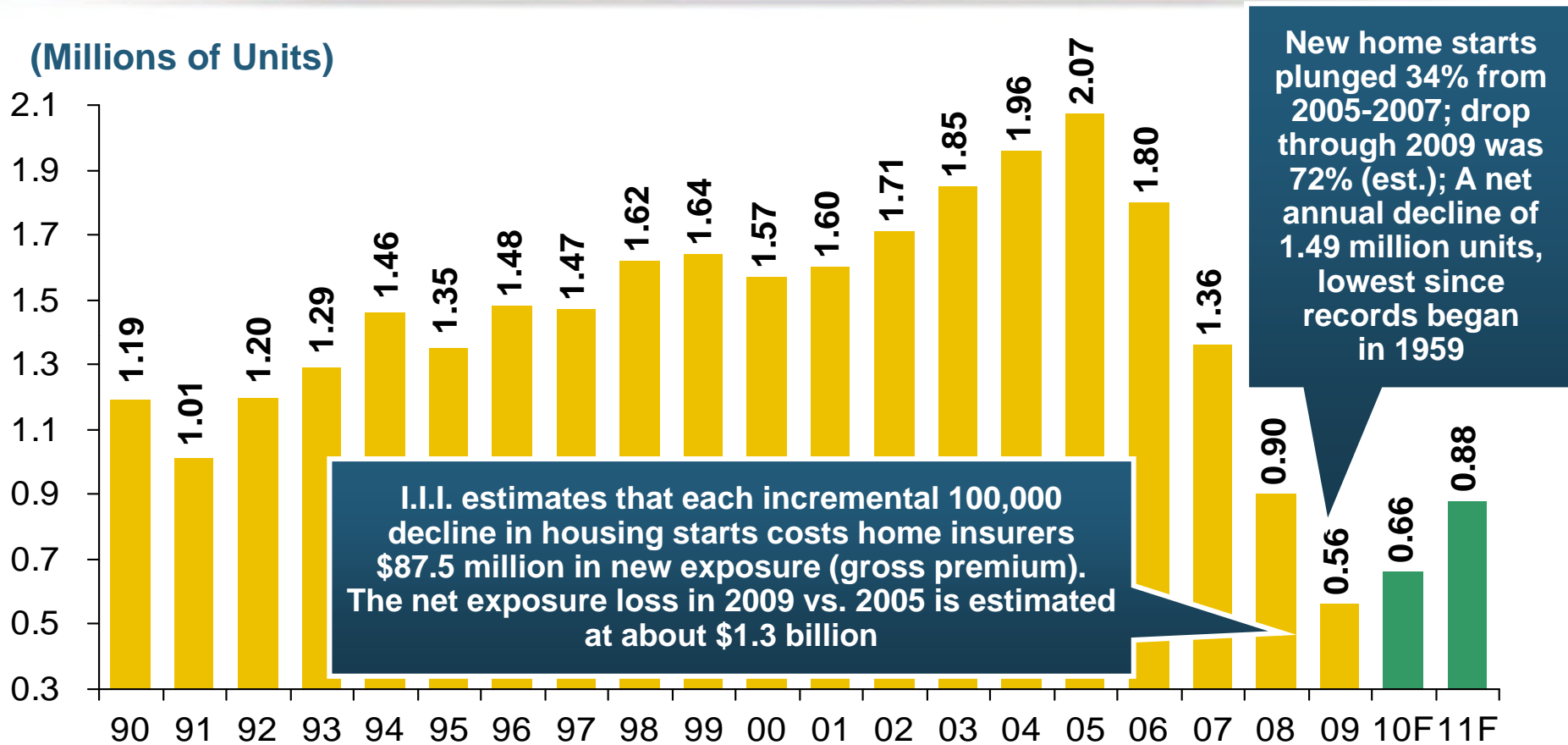
Auto/Light Truck Sales, 1999-2011F

(Millions of Units)



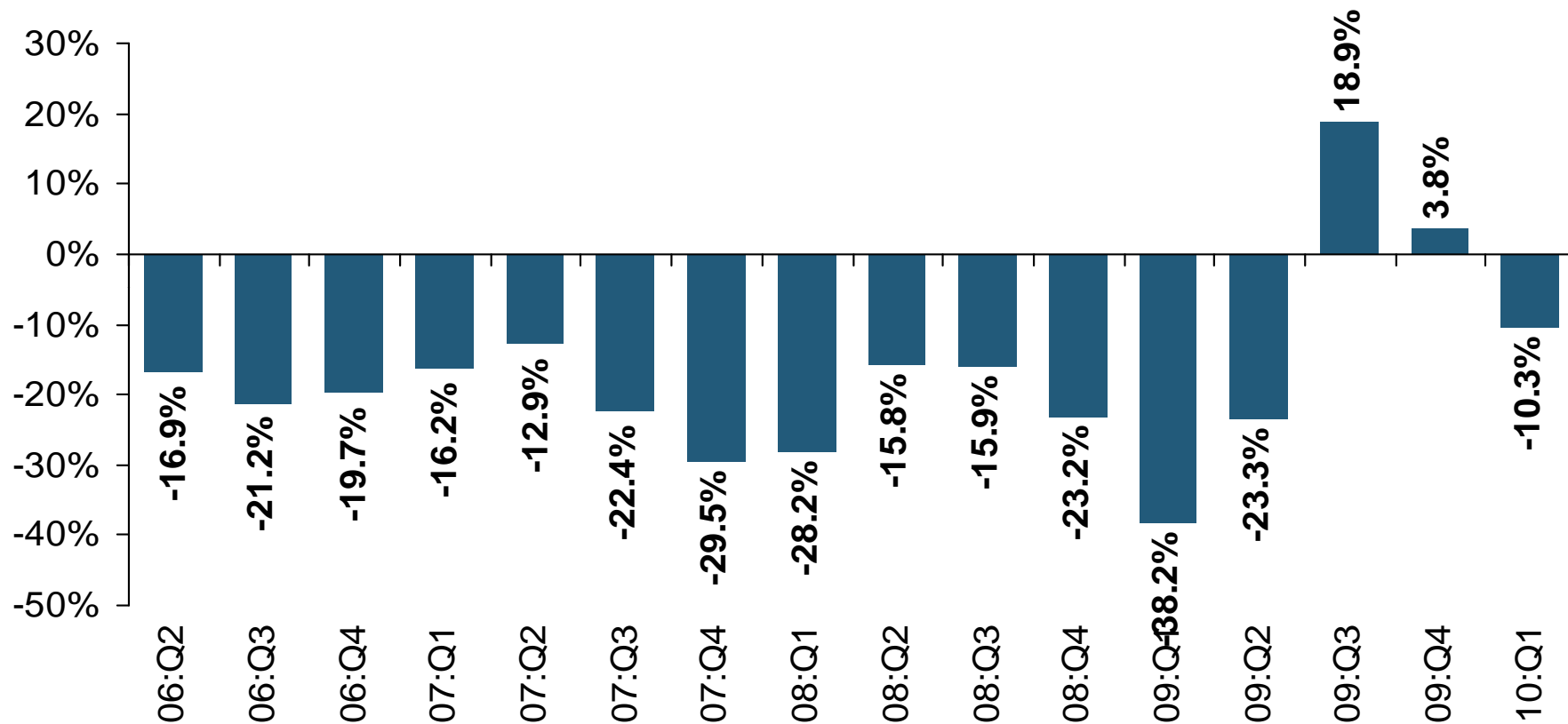
Car/Light Truck Sales Will Recover from the 2009 Low Point, but High Unemployment, Tight Credit Are Still Restraining Sales; Gas Prices Could Once Again Become a Factor, Too

New Private Housing Starts, 1990-2011F



**Little Exposure Growth Likely for Homeowners Insurers
Due to Weak Home Construction Forecast for 2010-2011.
Also Affects Commercial Insurers with Construction Risk Exposure, Surety**

Percent Changes in Residential Fixed Investment, 2006:Q2-2010:Q1*

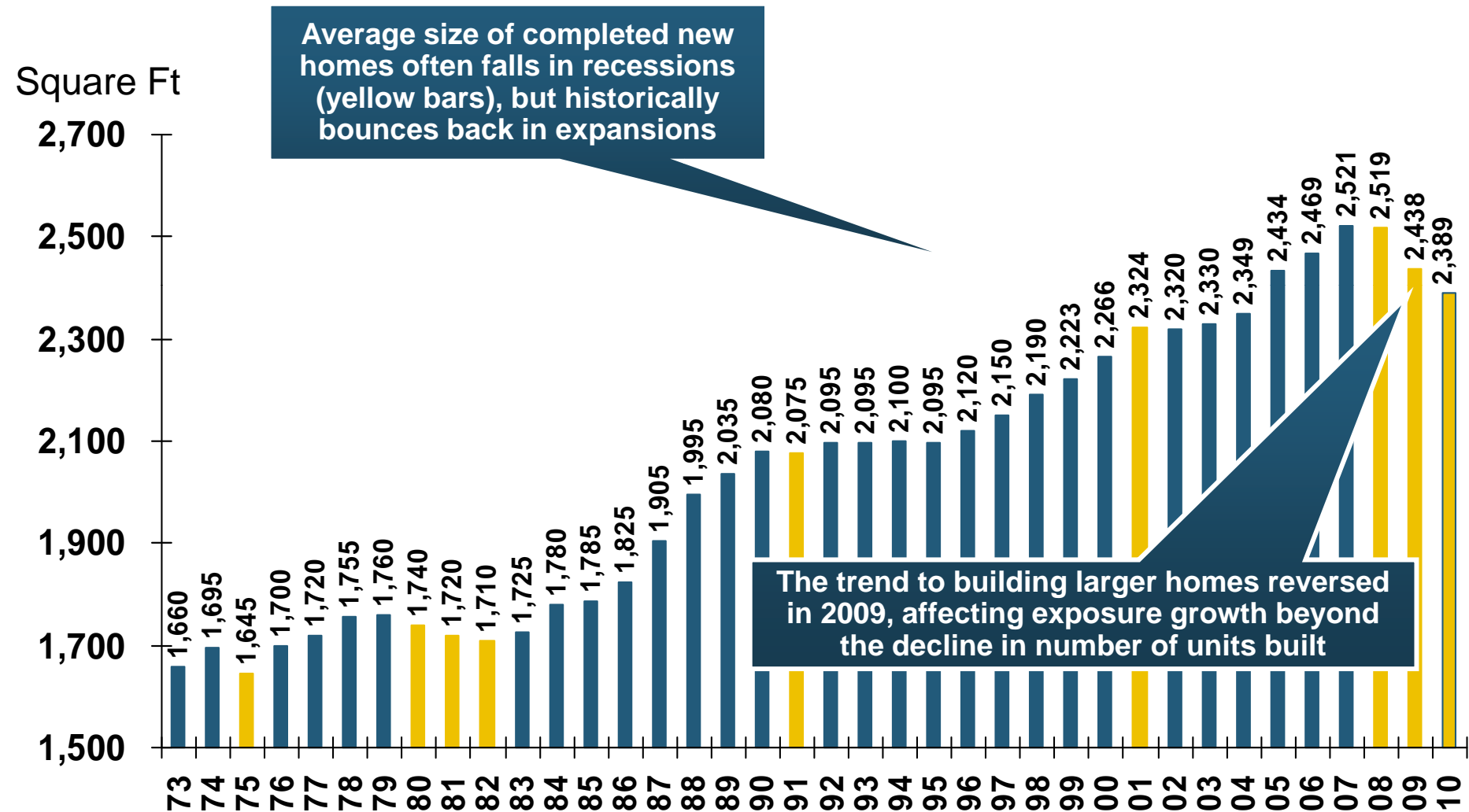


The Drop in 2006 is in Relation to the Record 2.07 Million Units Started in 2005; 1.8 Million Units Were Started That Year. The 2010:Q1 Drop Supports the Weak Home Construction Forecast for 2010-2011.

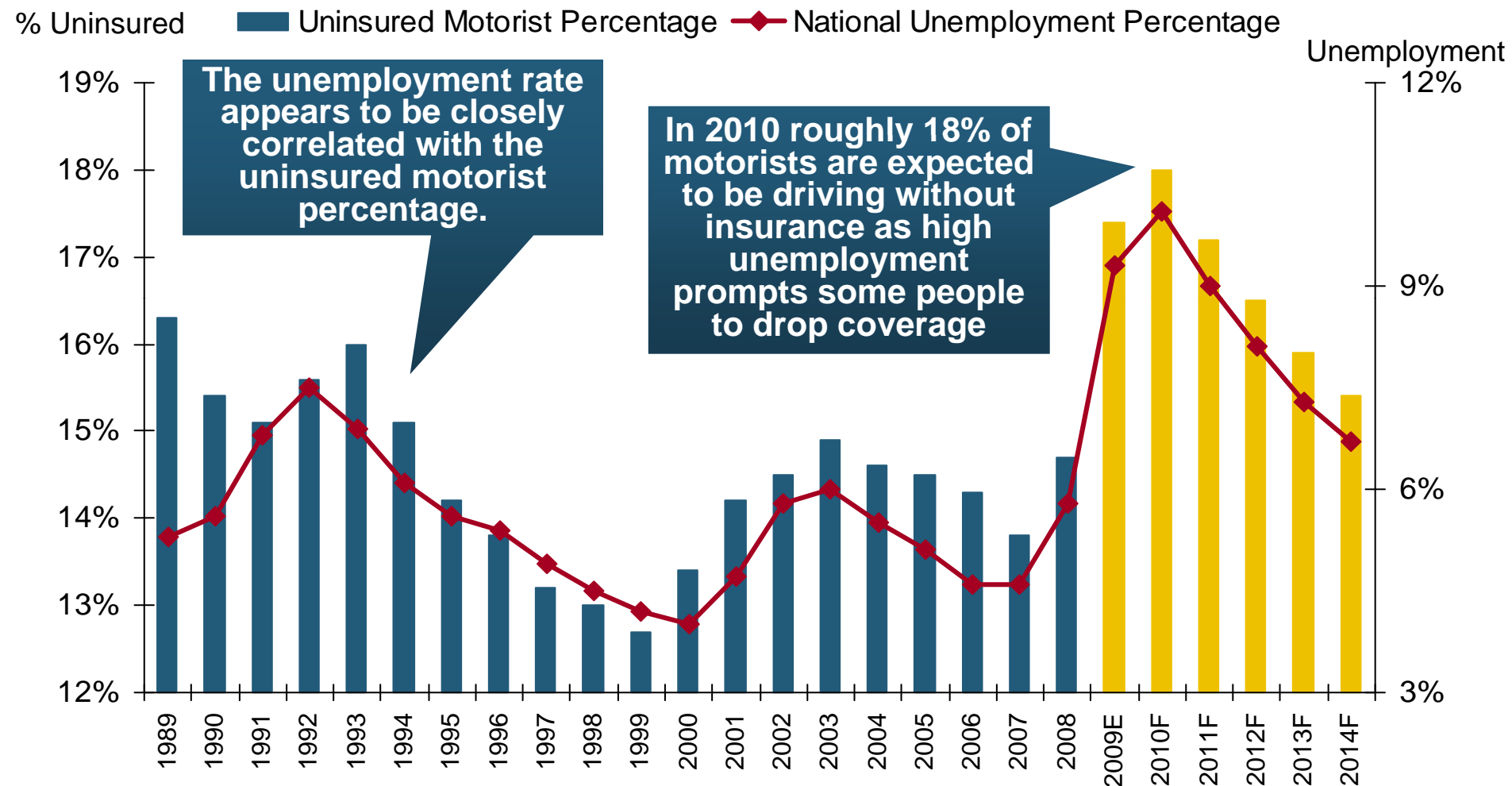
*seasonally adjusted

Source: U.S. Department of Commerce, Bureau of Economic Analysis

Average Square Footage of Completed New Homes in U.S., 1973-2010:Q1

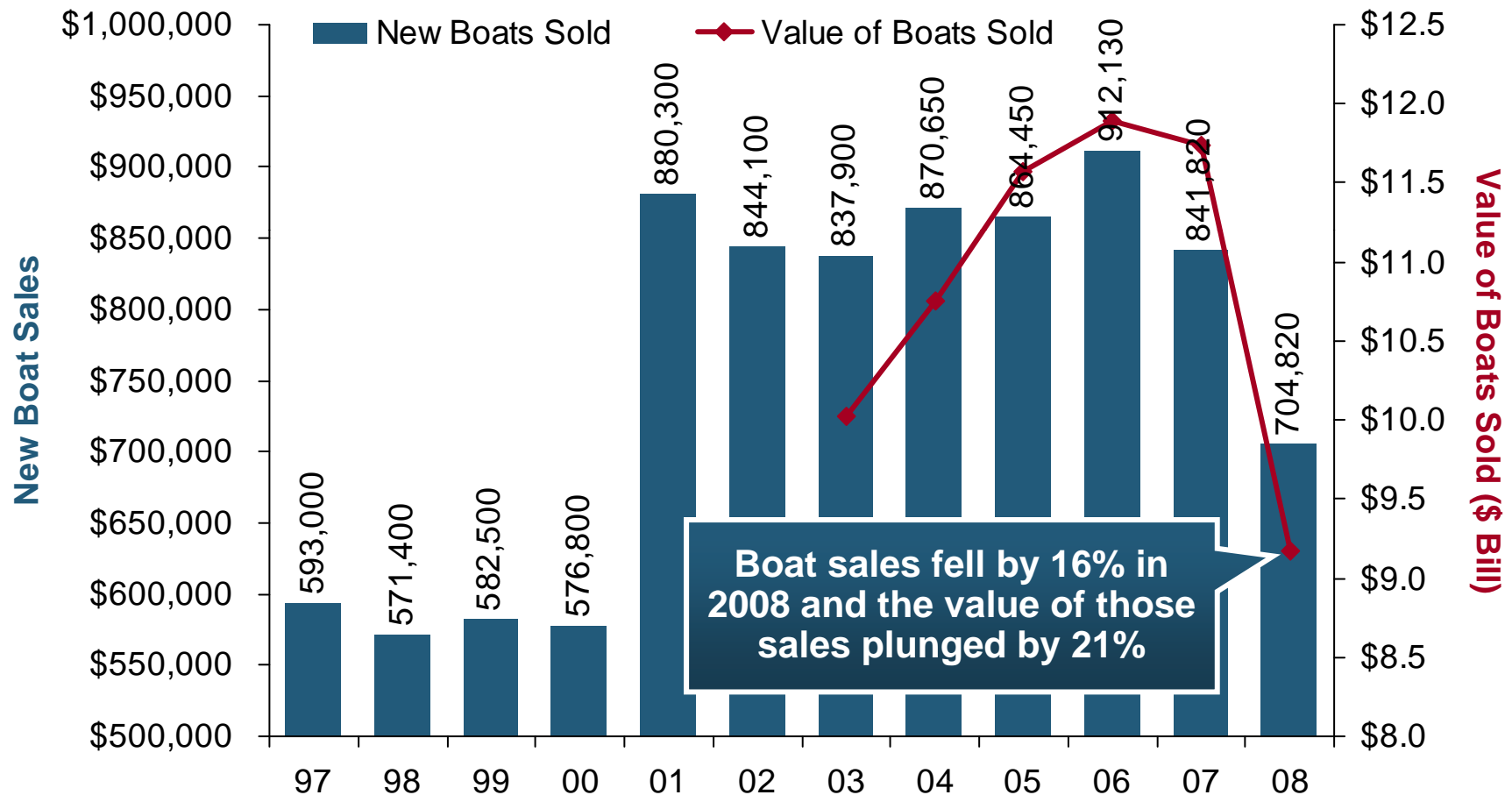


Unemployment's Effect on Percent of Uninsured Motorists, 1989-2014F

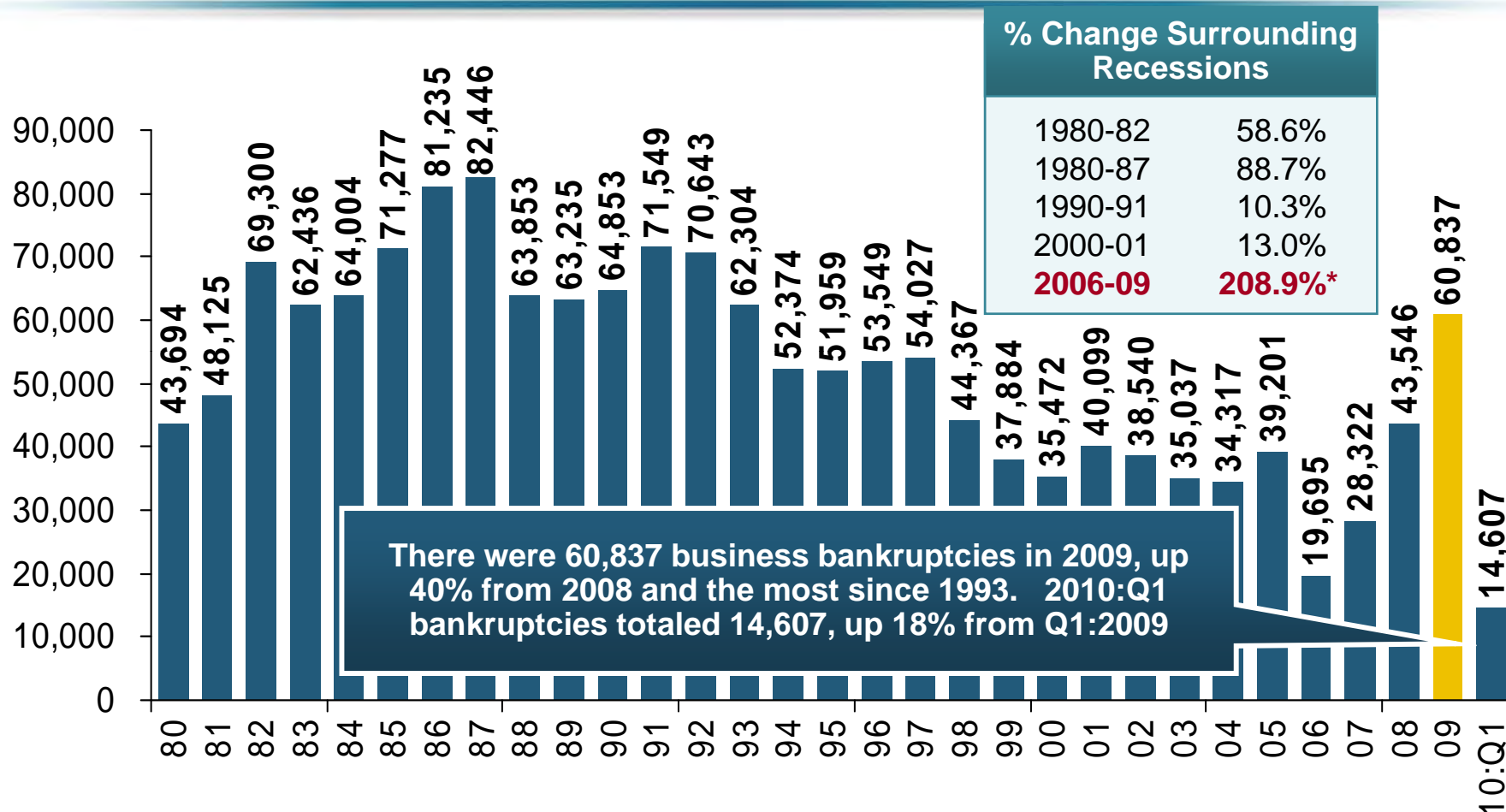


Source: *Uninsured Motorists*, 2008 Edition, Insurance Research Council; Blue Chip Economic Indicators (Unemployment data, including forecasts); Insurance Information Institute.

New Boat Sales Symptomatic of Decline in Insured Exposure Growth for Luxury/Discretionary Items



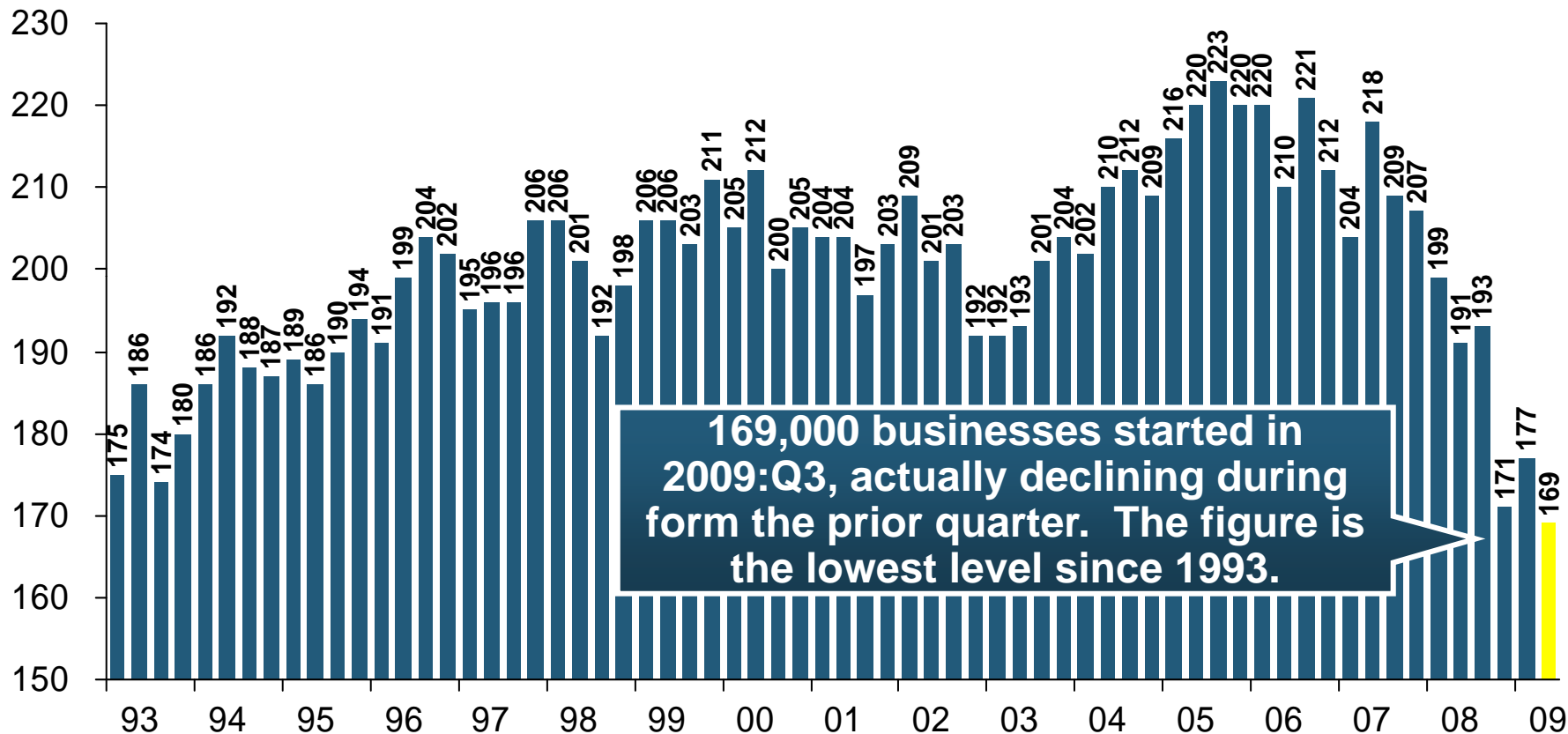
Business Bankruptcy Filings, 1980-2010:Q1



Significant Exposure Implications for All Commercial Lines

Private Sector Business Starts, 1993:Q2 – 2009:Q3*

(Thousands)



**Business Starts Are Down Nearly 20% in the Current Downturn,
Holding Back Most Types of Commercial Insurance Exposure**

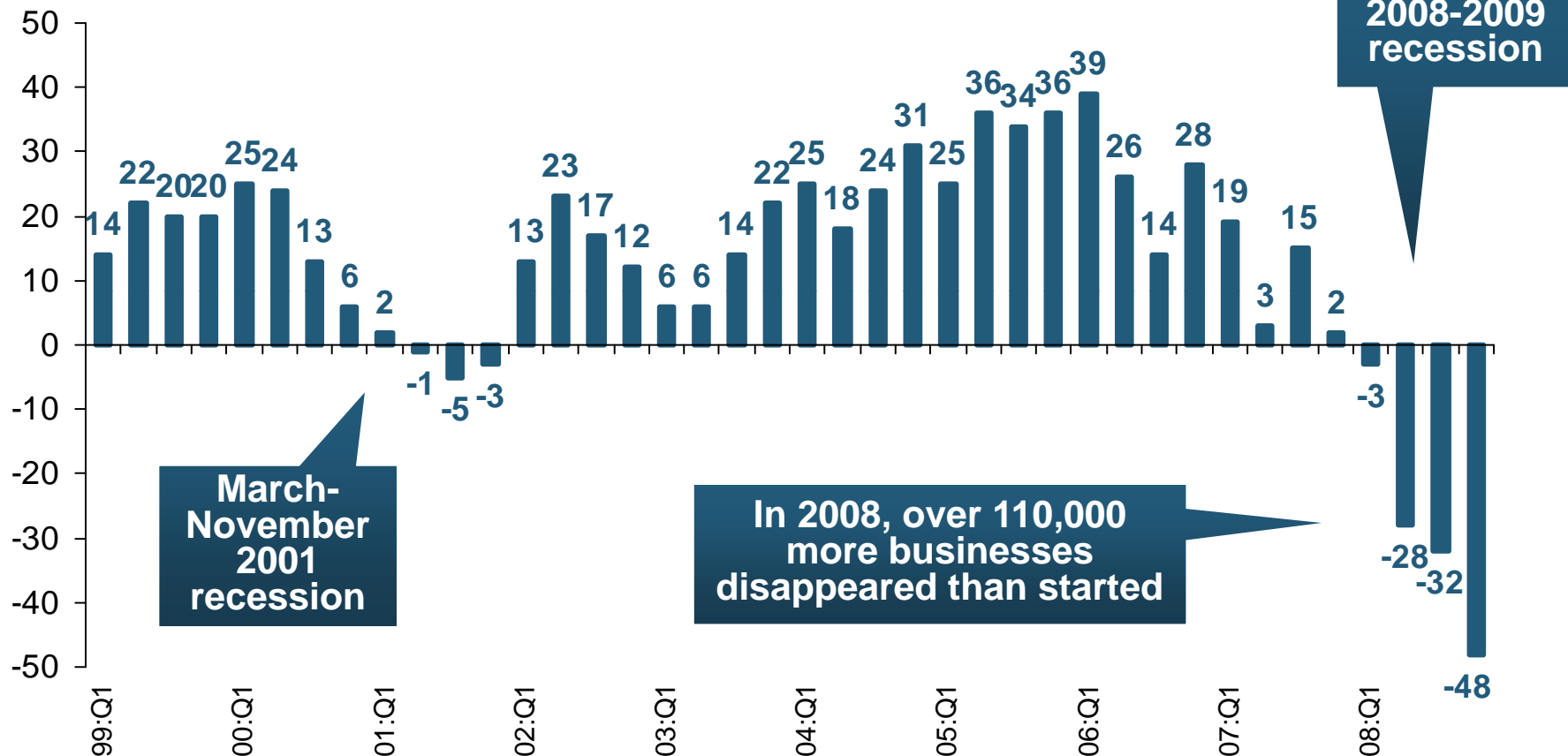
*Latest available as of June 7, 2010, seasonally adjusted

Source: Bureau of Labor Statistics, <http://www.bls.gov/news.release/cewbd.t07.htm>.

Net New Business Formations*

1999:Q1-2008:Q4*

Thousands



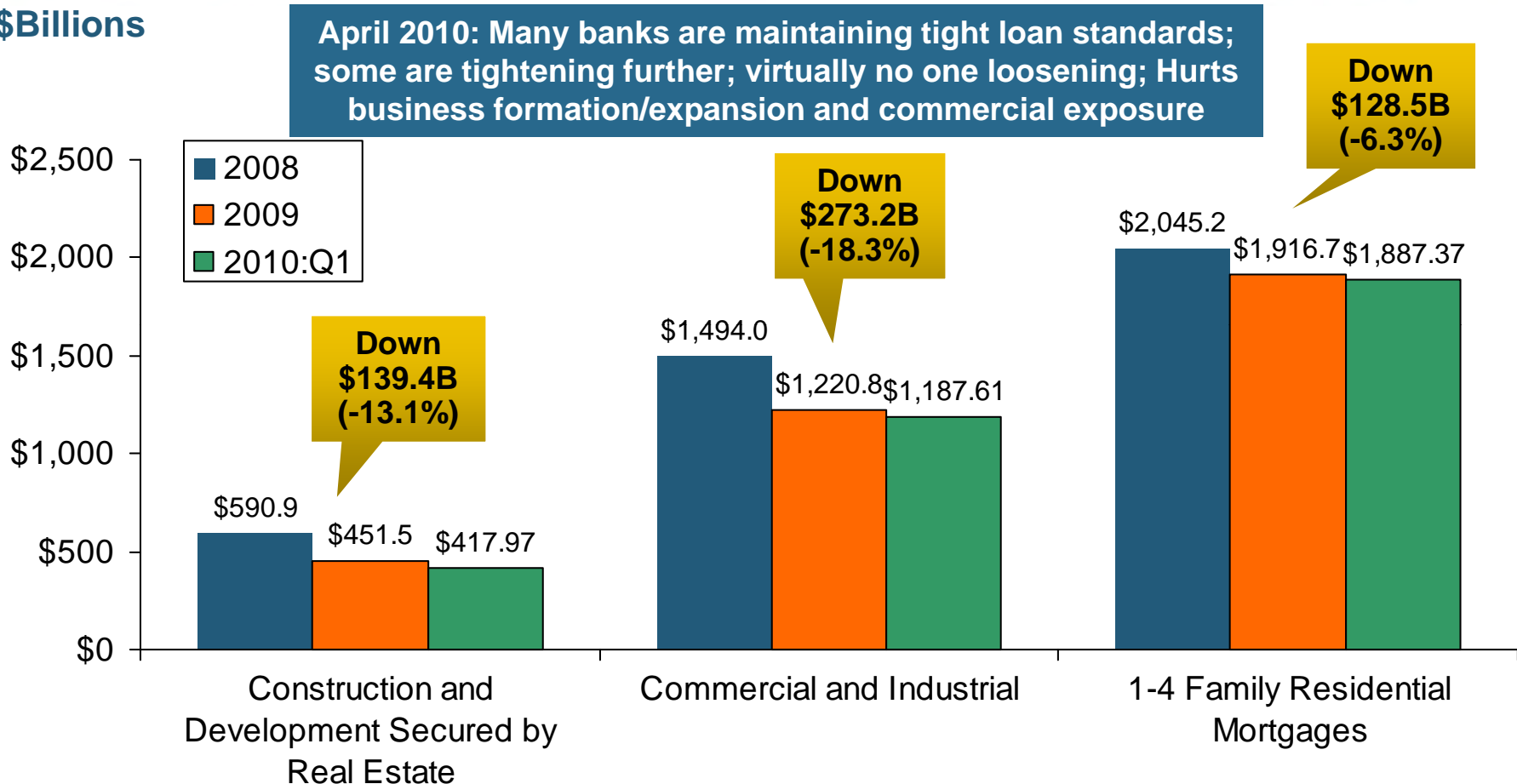
**Net Business Formations Likely Were Positive Again,
at Least in the Second Half of 2009 and into 2010.**

*Business "births" minus business "deaths." Latest data on business "deaths" is for 2008:Q4.

Sources: Bureau of Labor Statistics at <http://www.bls.gov/news.release/cewbd.t07.htm> ; Insurance Information Institute.

FDIC-Insured Banks Are Reducing Credit: 2008, 2009, 2010:Q1

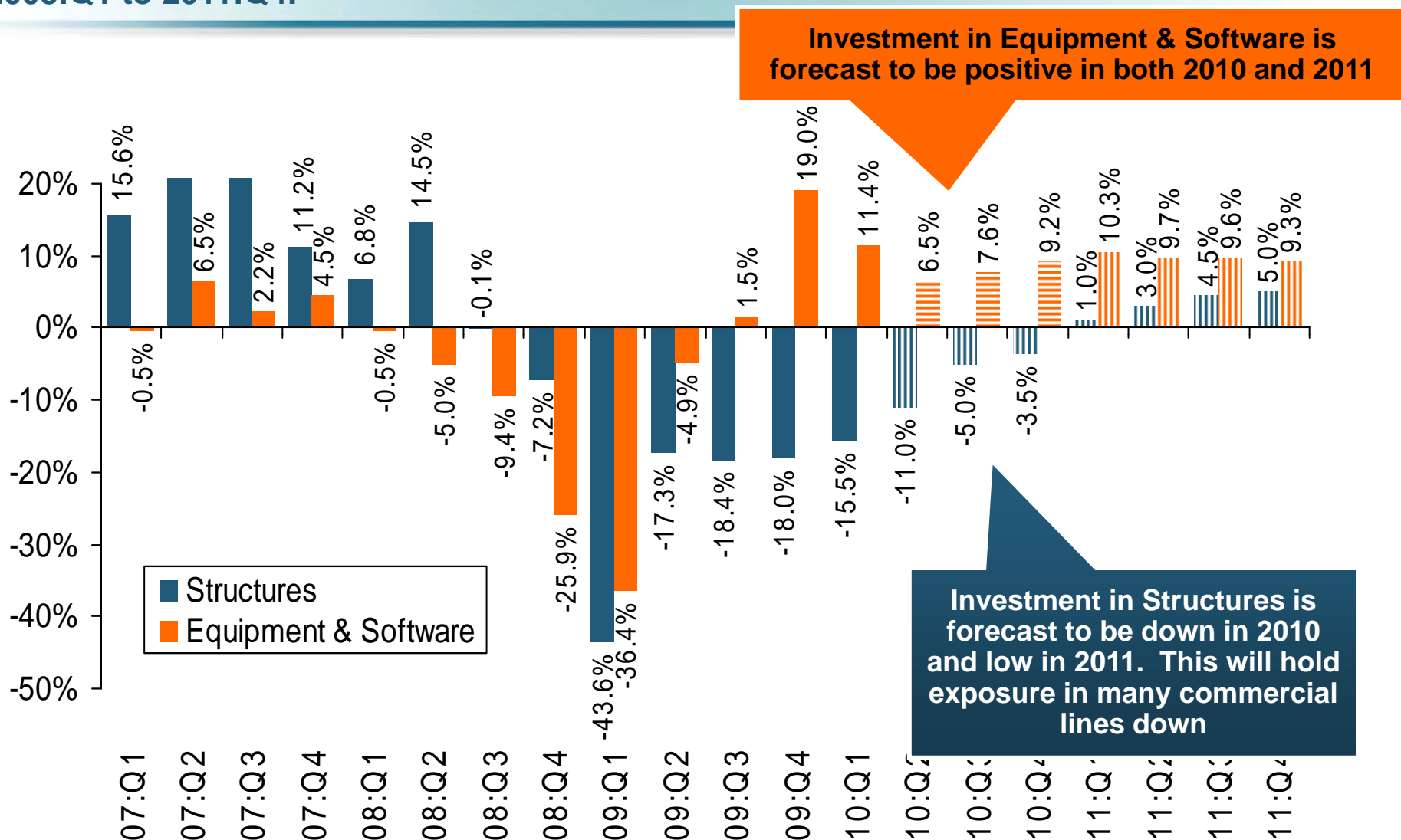
\$Billions



FDIC-Insured Institutions Had \$541.1B (-13.1%) Less in Outstanding Loans in These Three Categories at Year-end 2009 vs. 2008, and Even Less at End of 2010:Q1

Business Fixed Investment

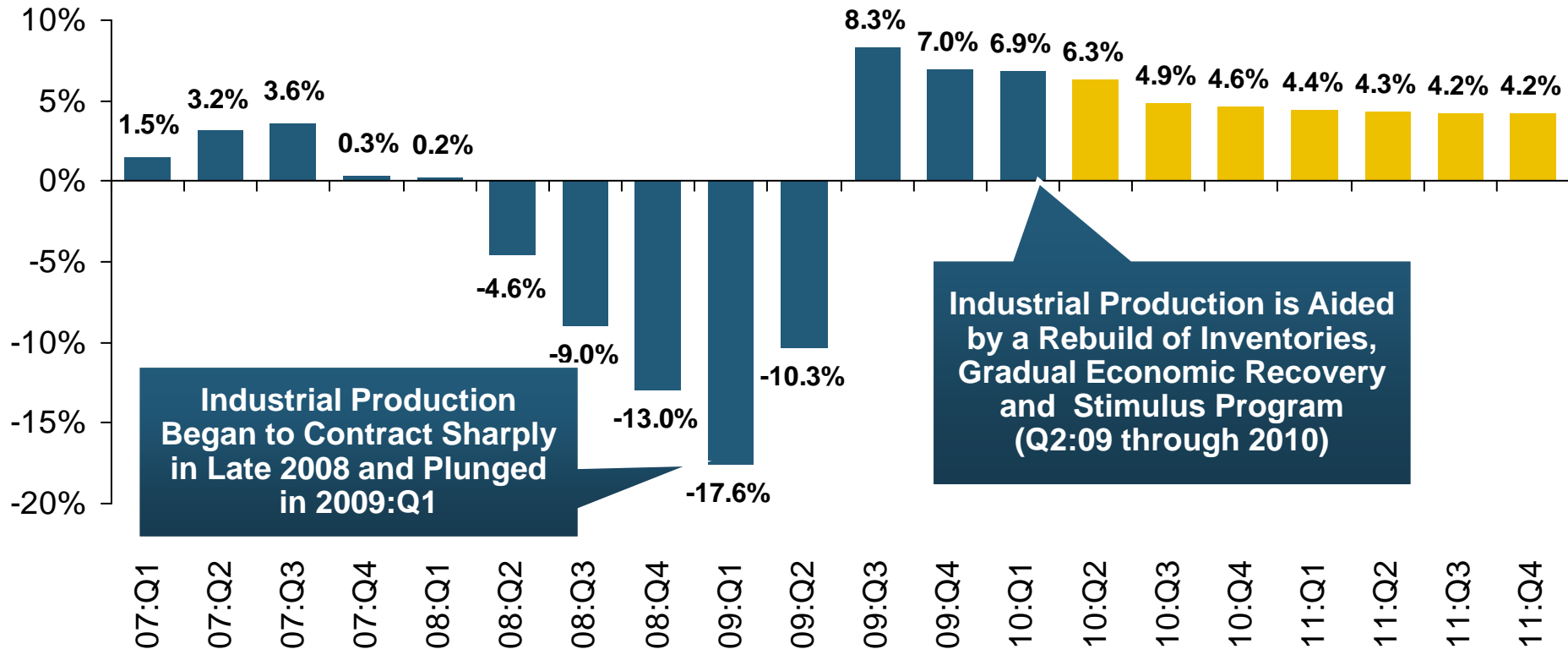
2008:Q1 to 2011:Q4F



Sources: Bureau of Economic Analysis, U.S. Department of Commerce (history); Wells Fargo Securities Economics Group, Monthly Outlook, April 7, 2010 (forecasts)

Total Industrial Production

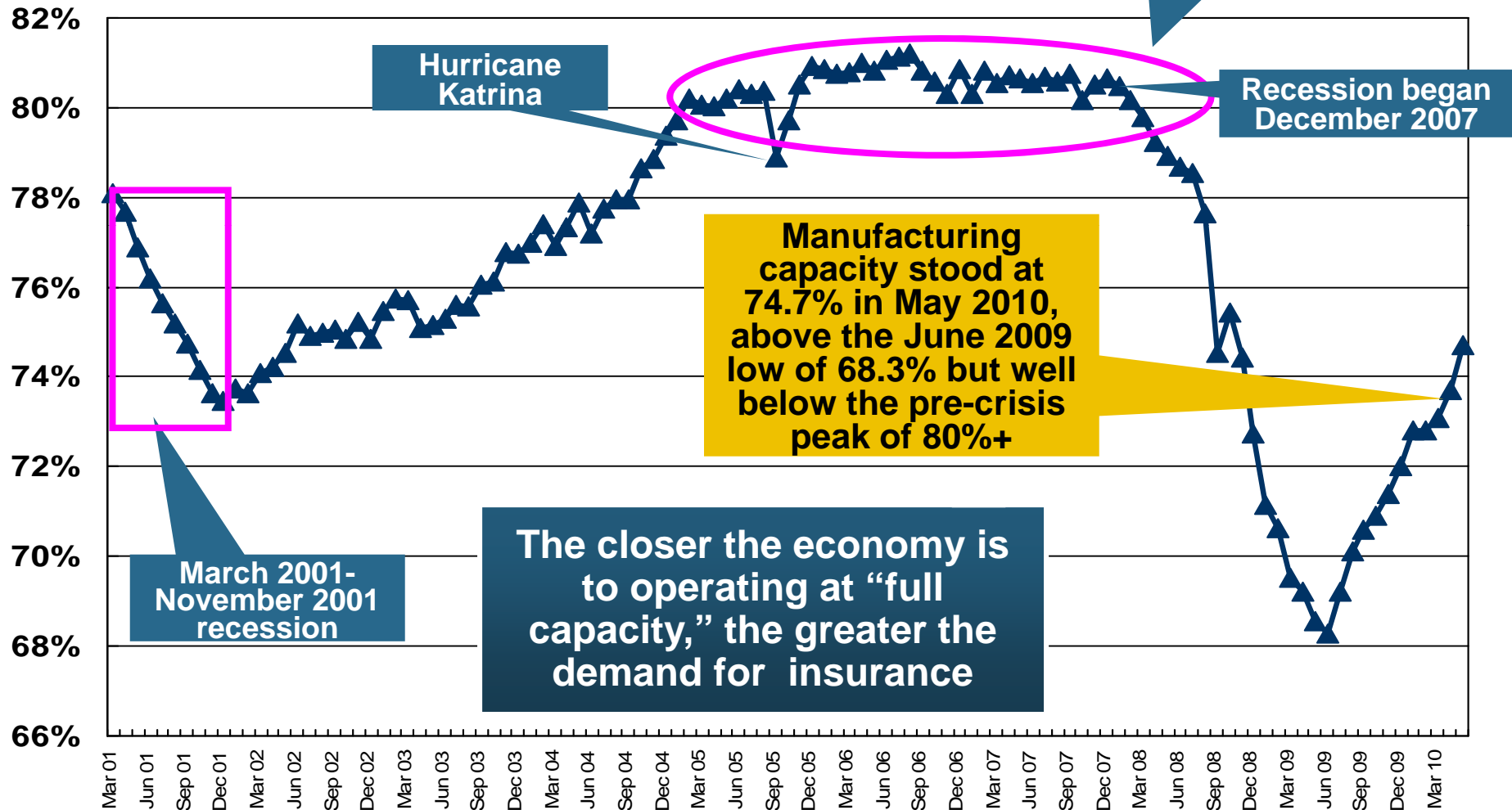
2007:Q1 to 2011:Q4F (%)



End of Recession in mid-2009, Stimulus Program Benefited Industrial Production and Insurance Exposure Both Directly and Indirectly, Albeit it Very Modestly; Stimulus Effect is Waning in 2010 and Will Be Gone in 2011.

Recovery in Capacity Utilization is a Positive Sign for Energy & Insurance

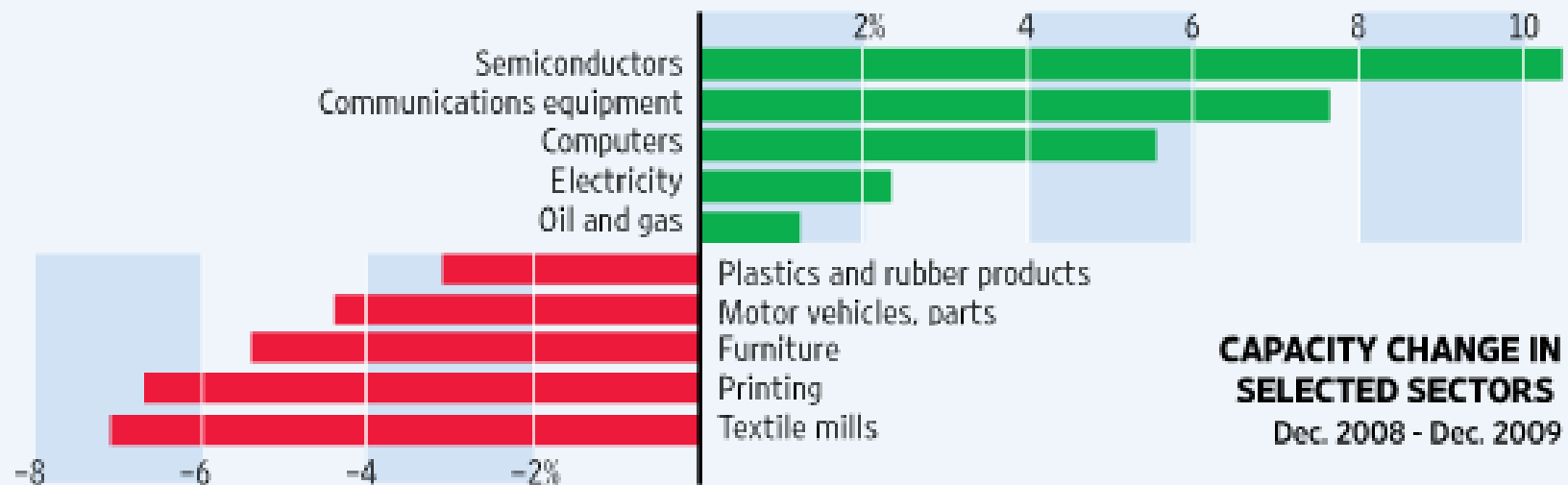
Percent of
Manufacturing Capacity



But Some Industrial Production Capacity Has Vanished

Winners and Losers

The recession is reshaping U.S. industry as companies add capacity in some areas and cut in others.



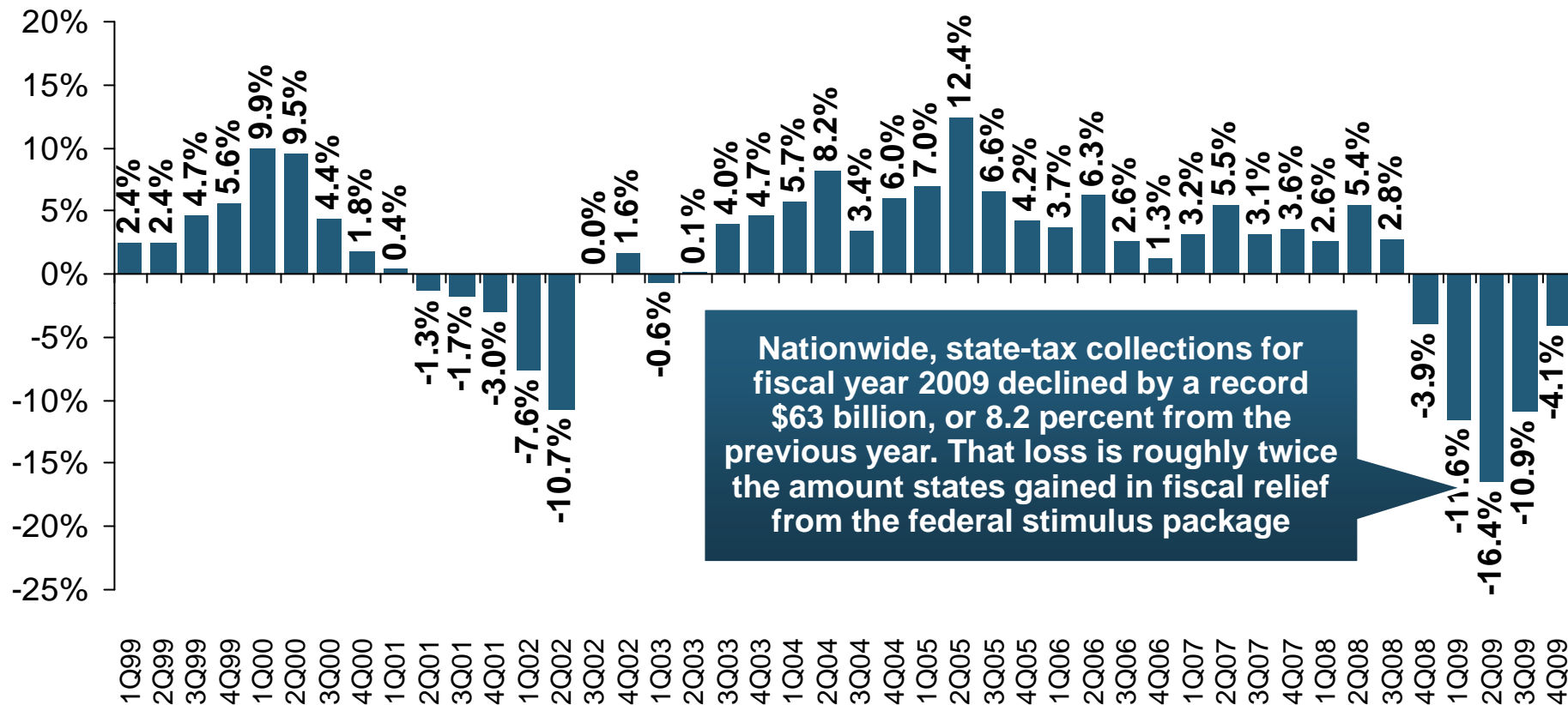
Source: Federal Reserve

Some unused capacity is gone, and in other industries new capacity is needed, so the economy might be closer to full capacity than the industrial production numbers indicate. If so, this might spur inflation sooner than expected.

State & Local Government Finances in Dire Straits

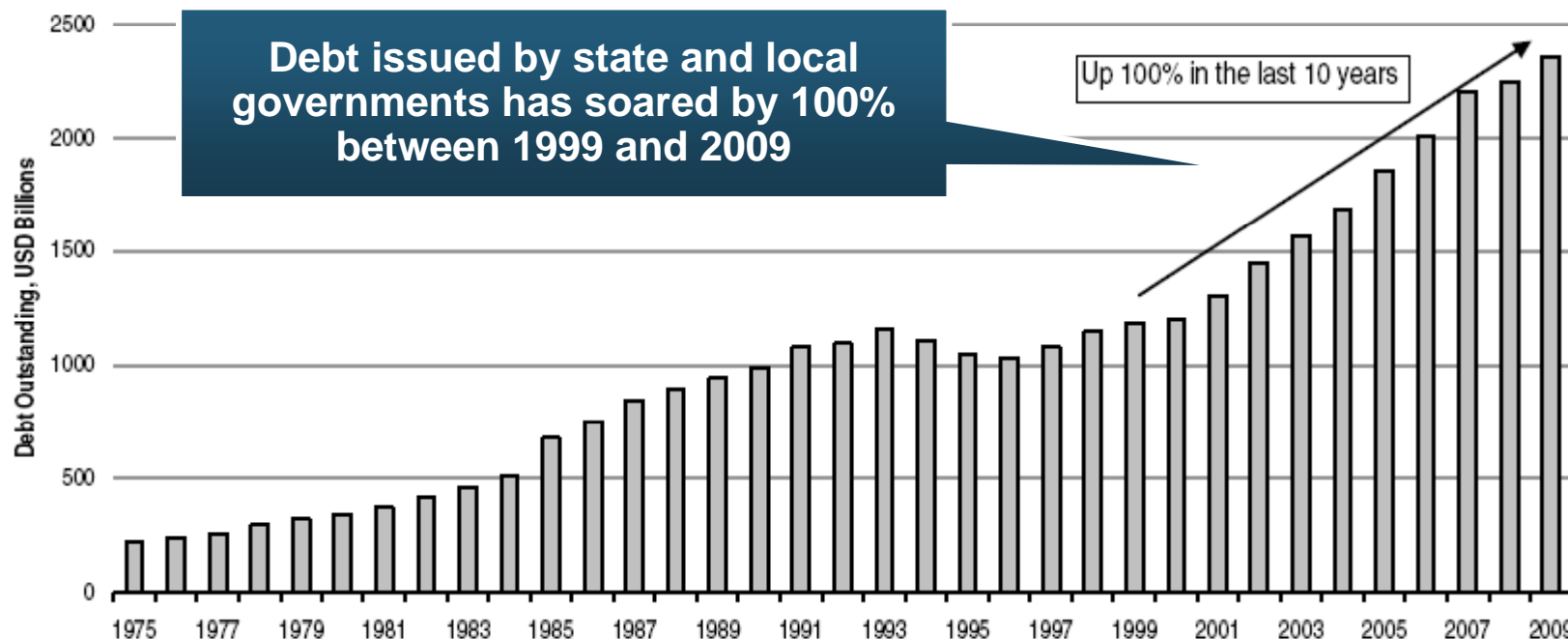
**Large, Long-Term Cuts Necessary
to Align Spending with Shrinking
Tax Revenues**

Year-Over-Year Change in Quarterly US State Tax Revenues, Inflation Adjusted



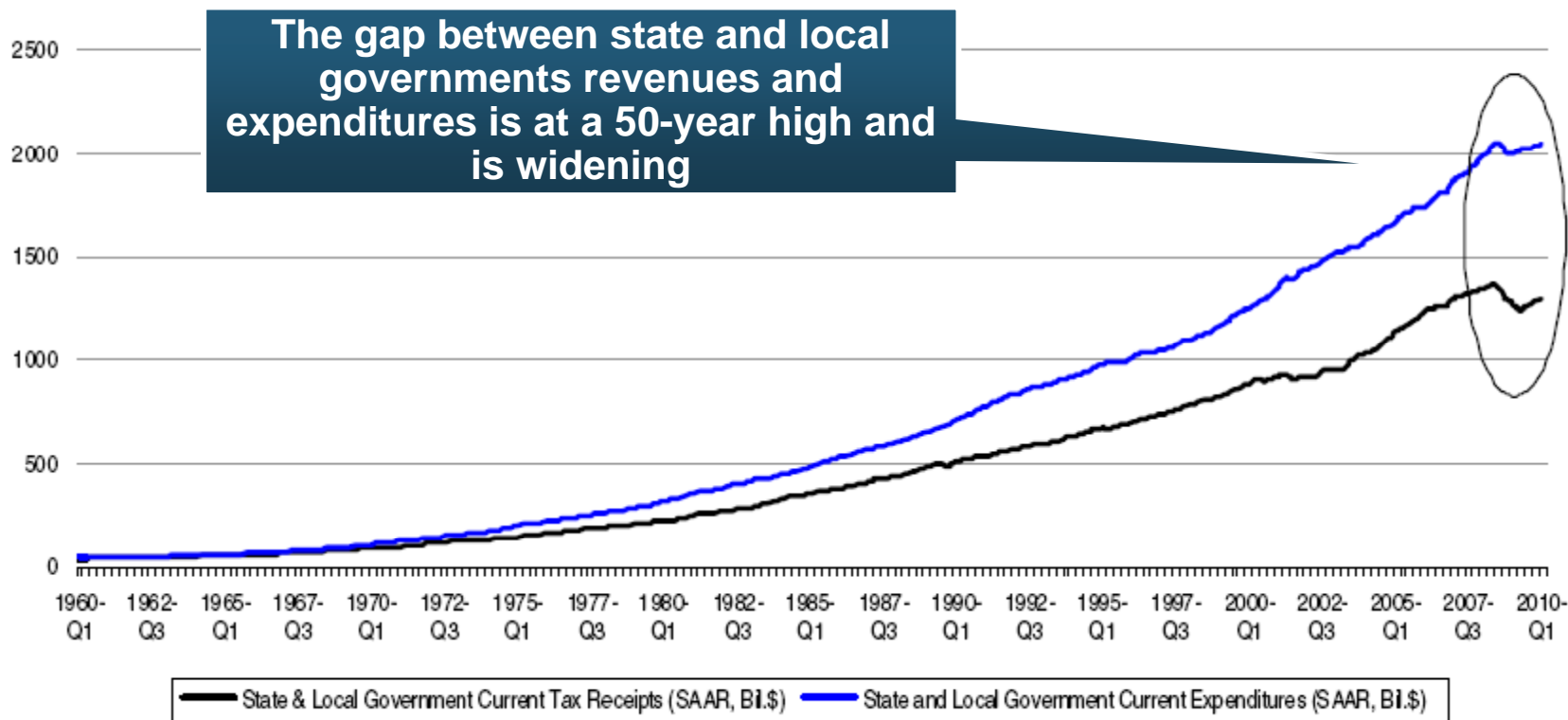
States Revenues Were Down 4.4% in Q4 2009, the 5th Consecutive Quarter of Revenue Decline. This Will Impact Public Infrastructure Spending Significantly and Related Insurance Exposures and Demand.

State and Local Debt Outstanding, 1975-2009



Many States/Localities Are in Dire Fiscal Straights, but the Default Rate on Moody's-Rated Muni Debt is Just 0.09% over the Past 10 Years. Just 1 State Has Defaulted in the Past 100 Years (AR). Default Rate on Munis During the Great Depression was 1.8%, 97% of Which Was Ultimately Recovered

State and Local Expenditures vs. Tax Receipts, 1960-2010:Q1



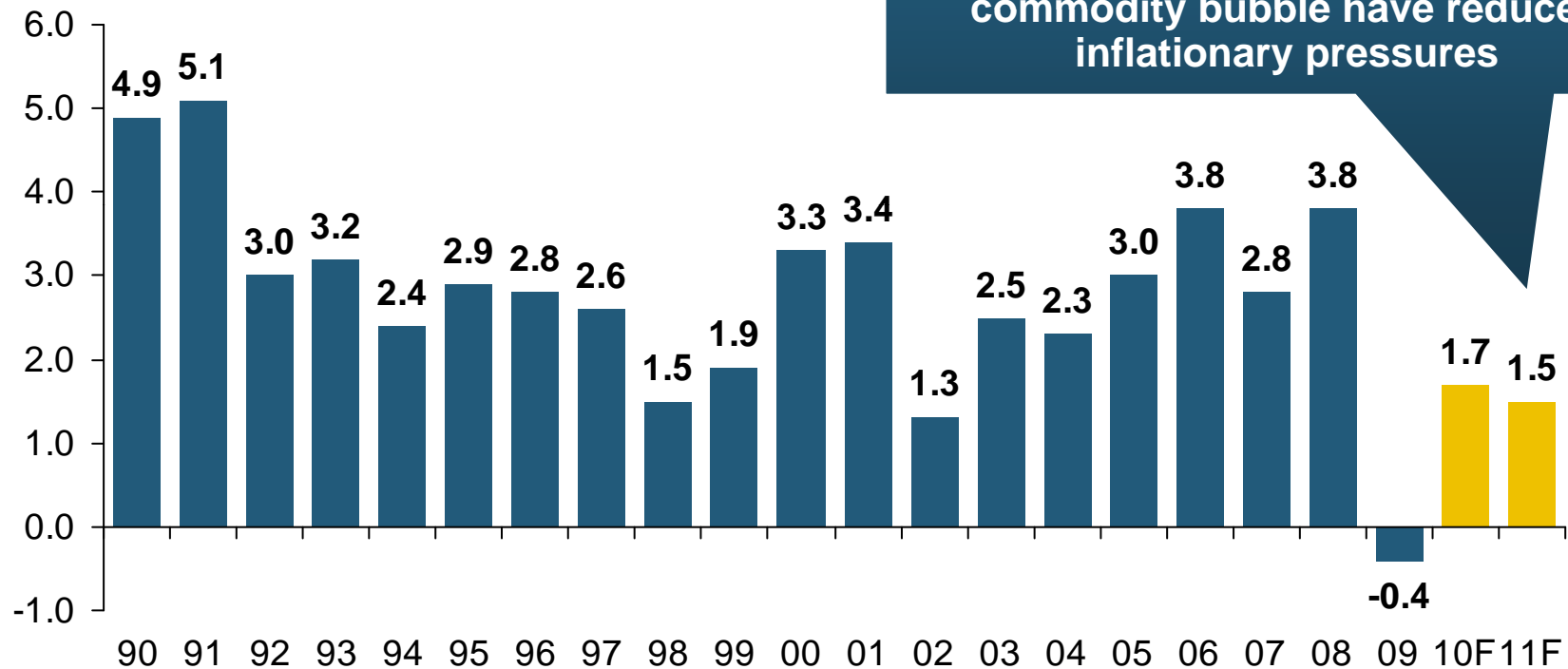
Many States/Localities Are in Dire Fiscal Straights, but the Default Rate on Moody's-Rated Muni Debt is Just 0.09% over the Past 10 Years. Just 1 State Has Defaulted in the Past 100 Years (AR). Default Rate on Munis During the Great Depression was 1.8%, 97% of Which Was Ultimately Recovered

**Inflation Trends:
*Concerns Over Stimulus Spending
and Monetary Policy***

**Mounting Pressure on Claim
Cost Severities?**

Annual Inflation Rates (CPI-U, %), 1990–2011F

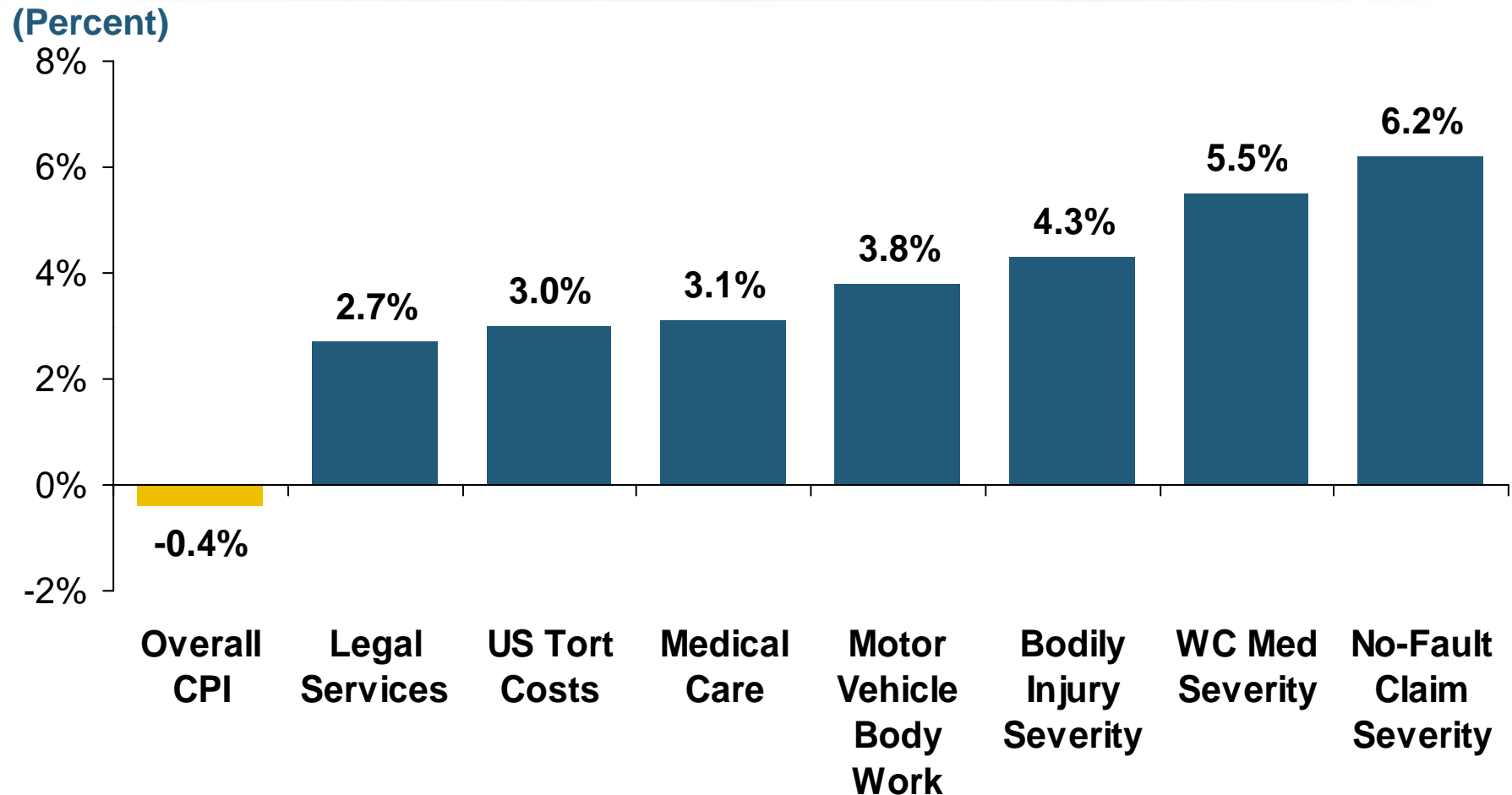
Annual Inflation Rates (%)



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

There is So Much Slack in the US Economy Inflation Should Not Be a Concern Through 2010/11, but Deficits and Monetary Policy Remain Longer Run Concerns

P/C Insurers Experience Inflation More Intensely than 2009 CPI Suggests

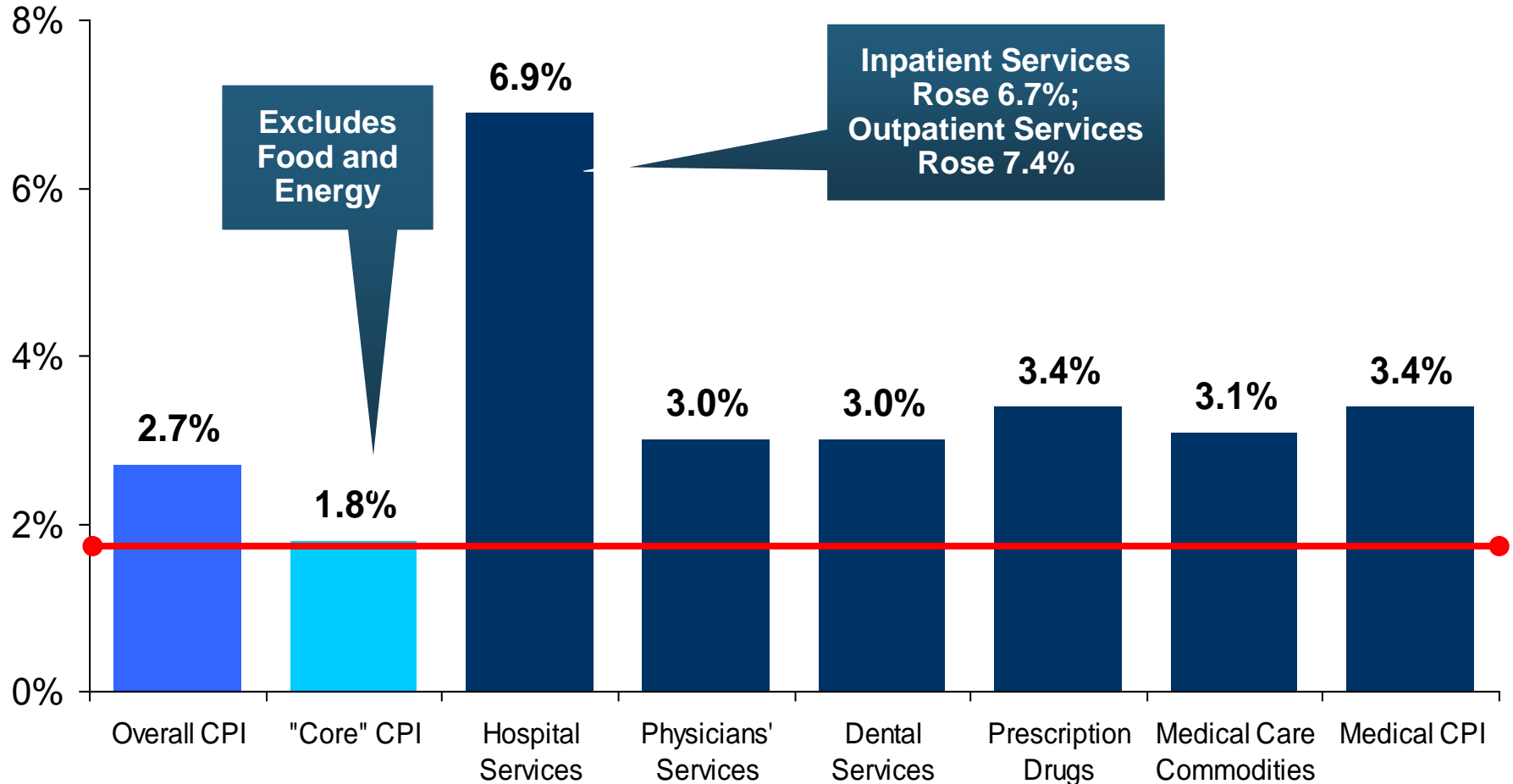


Healthcare and Legal/Tort Costs Are a Major P/C Insurance Cost Driver. These Are Expected to Increase Above the Overall Inflation Rate (CPI) Indefinitely

Source: CPI is Blue Chip Economic Indicator 2009 estimate, 12/09; Legal services, medical care and motor vehicle body work are avg. monthly year-over-year change from BLS; BI and no-fault figures from ISO Fast Track data for 4 quarters ending 09:Q3. Tort costs is 2009 Towers-Perrin estimate. WC figure is I.I.I. estimate based on historical NCCI data.

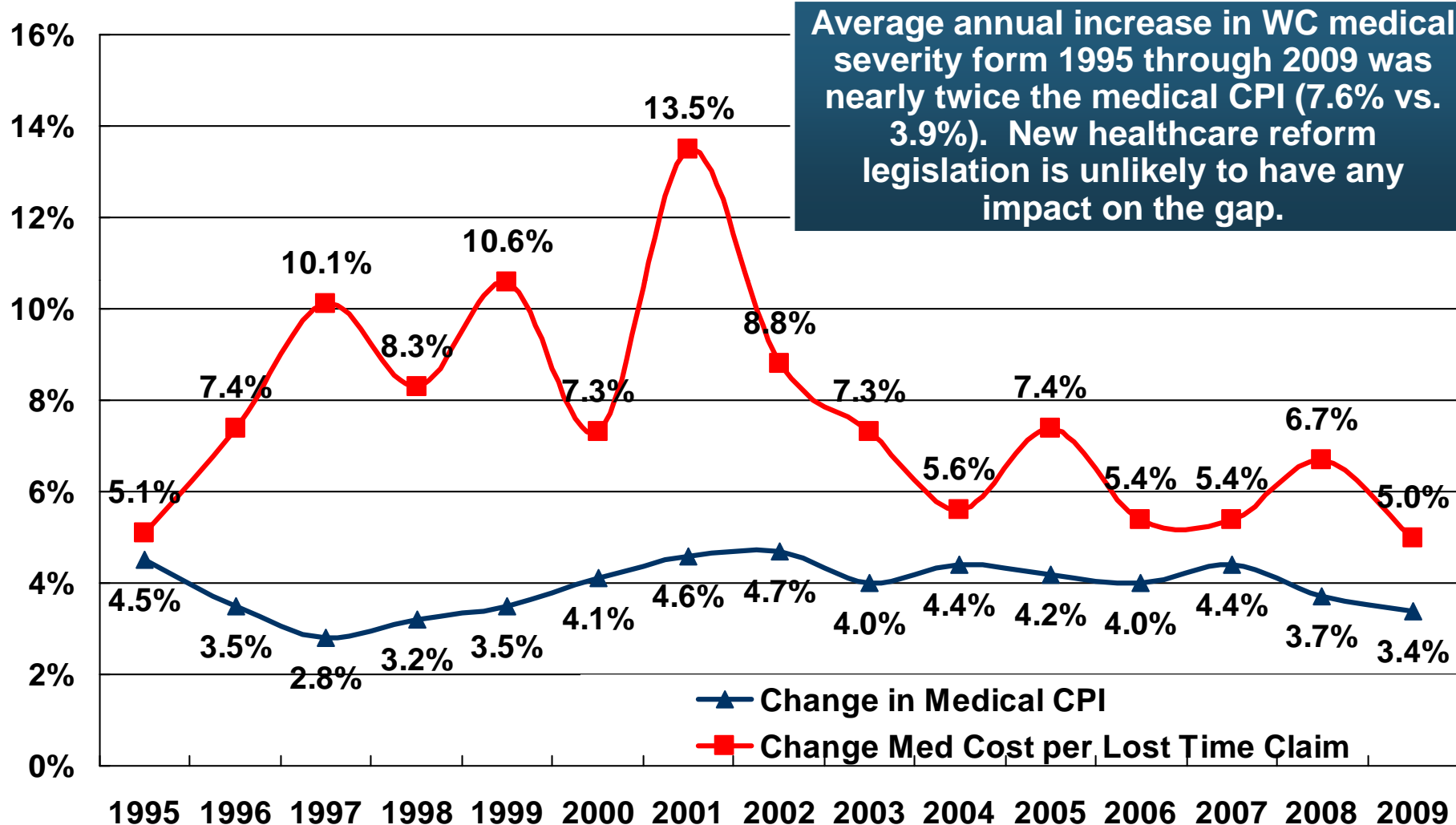
WC Insurers Experience Inflation More Intensely than 2009 CPI Suggests

(Percent increase Dec 08 to Dec 09)



Healthcare Costs Are a Major WC Insurance Cost Driver. They Are Likely to Increase Faster than the CPI for the Next Few Years, at Least

WC Medical Severity Rising at Twice the Medical CPI Rate



Top Concerns/Risks for Insurers if Inflation Is Reignited

Concerns

The Federal Reserve Has Flooded Financial System with Cash (Turned on the Printing Presses), the Federal Gov't Has Approved a \$787B Stimulus and the Deficit is Expected to Mushroom to \$1.8 Trillion. All Are Potentially Inflationary.

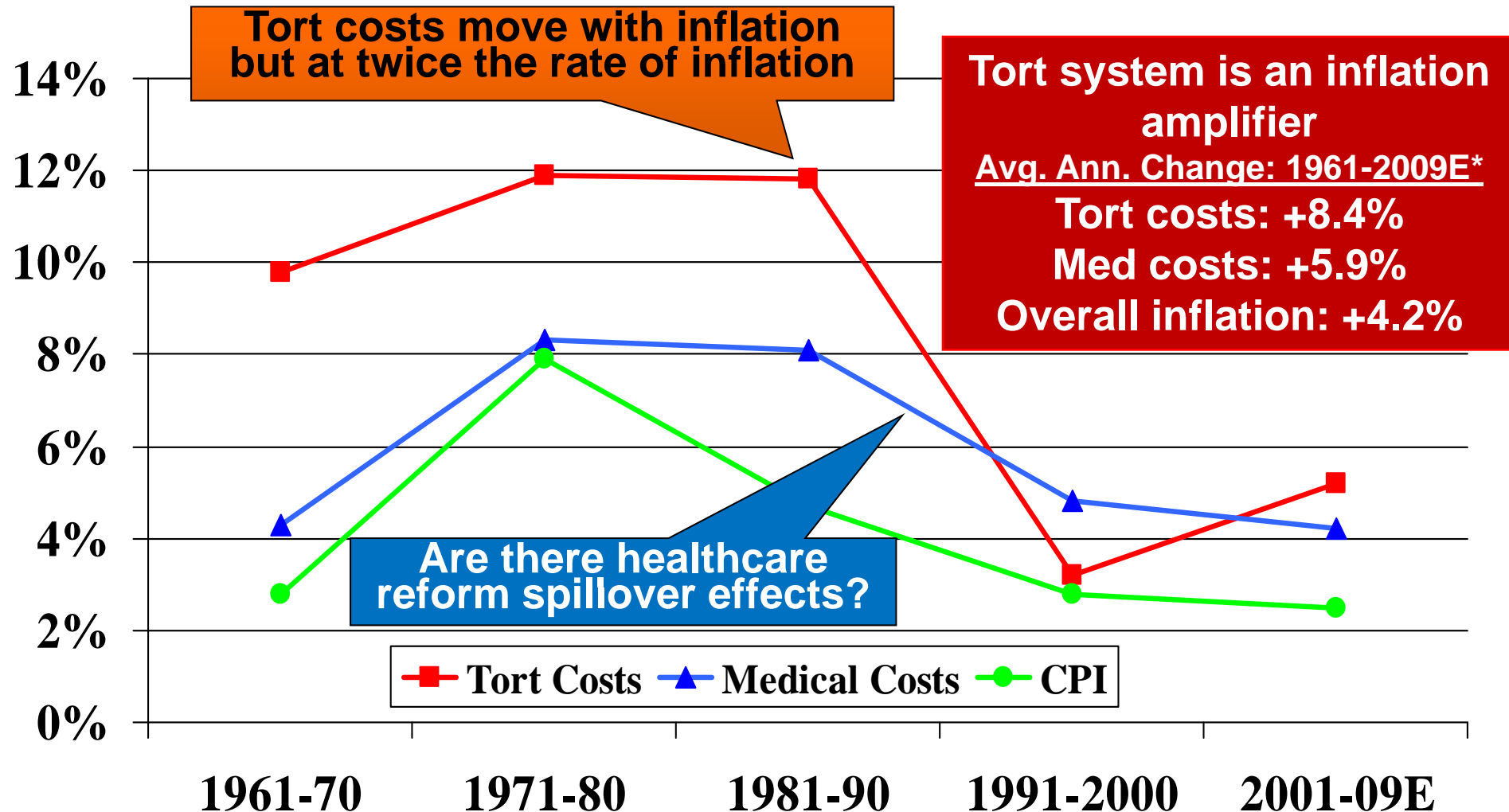
- What are the potential impacts for insurers?
- What can/should insurers do to protect themselves from the risks of inflation?

Key Risks

From Sustained/Accelerating Inflation

- **Rising Claim Severities**
 - ◆ Cost of claims settlement rises across the board (property and liability)
- **Rate Inadequacy**
 - ◆ Rates inadequate due to low trend assumptions arising from use of historical data
- **Reserve Inadequacy**
 - ◆ Reserves may develop adversely and become inadequate (deficient)
- **Burn Through on Retentions**
 - ◆ Retentions, deductibles burned through more quickly
- **Reinsurance Penetration/Exhaustion**
 - ◆ Higher costs → risks burn through their retentions more quickly, tapping into reinsurance more quickly and potentially exhausting their reinsurance more quickly

Tort Cost Growth & Medical Cost Inflation vs. Overall Inflation (CPI-U), 1961-2009E*



* CPI-U and medical costs as of Sept 2009; Tort figure is for full-year 2009 from Tillinghast.

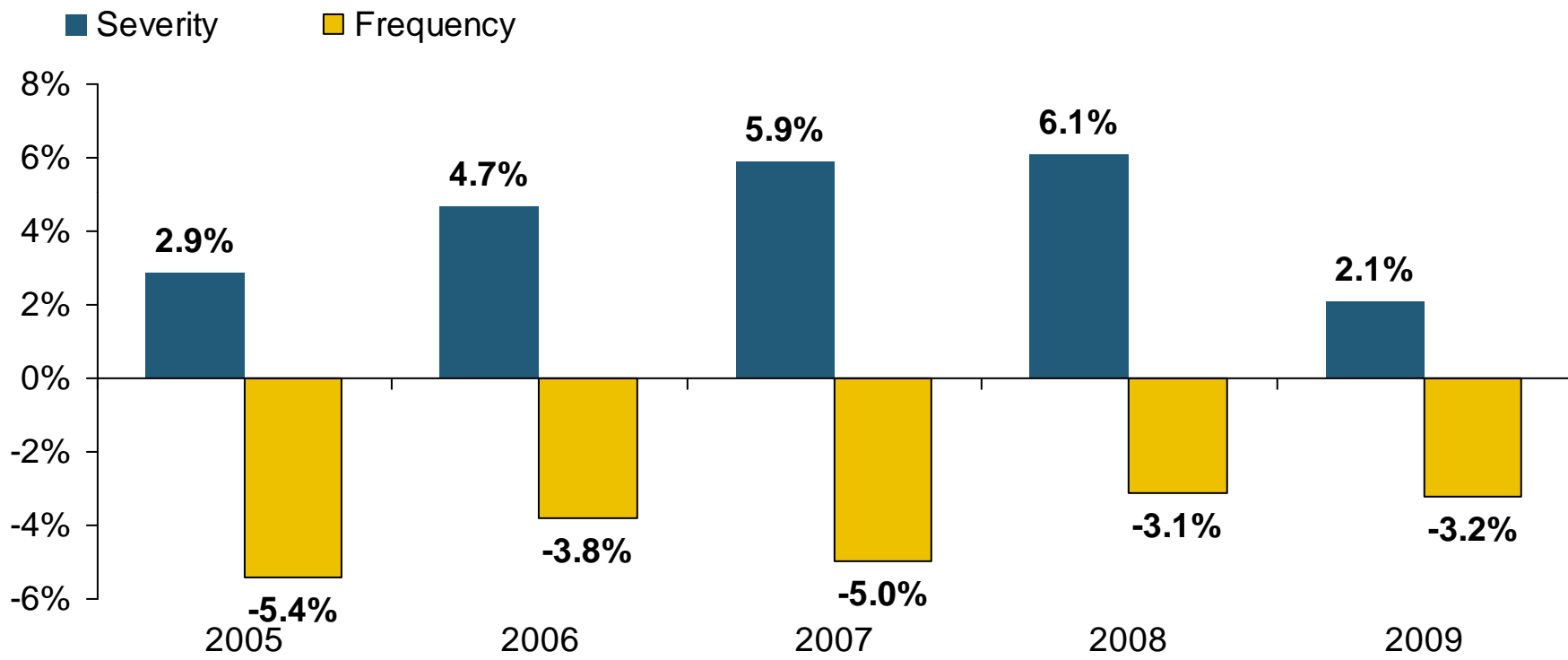
Source: U.S. Bureau of Labor Statistics; Tillinghast-Towers Perrin, *2008 Update on U.S. Tort Costs*; I.I.I.

Claim Trends in Auto Insurance

**Rising Costs Held in Check by
Falling Frequency:
Can That Pattern Be Sustained?**

Bodily Injury: Severity Trends Generally Above Decline in Frequency

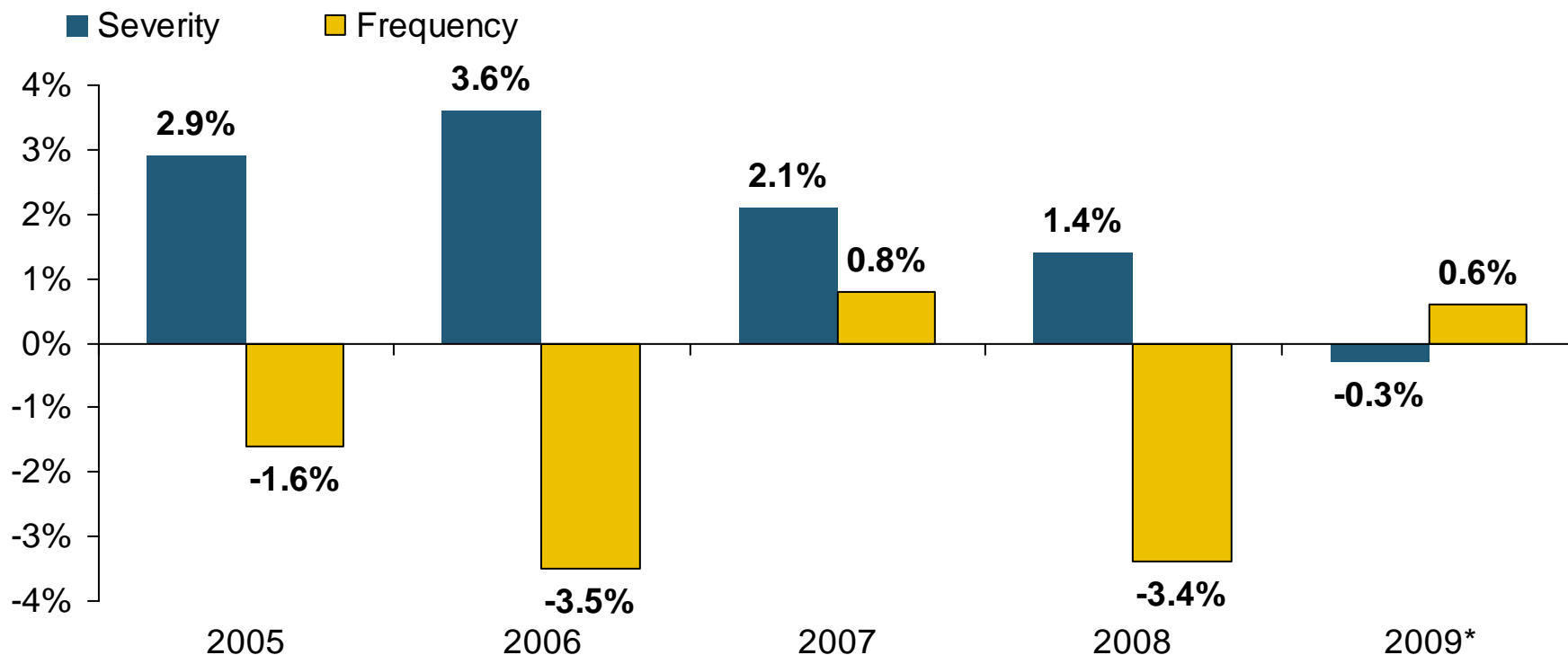
Annual Change, 2005 through 2009



Cost Pressures Will Increase if Current BI Frequency and Severity Trends Continue

Property Damage Liability: Frequency and Severity Trends Nearly Offset in 2009

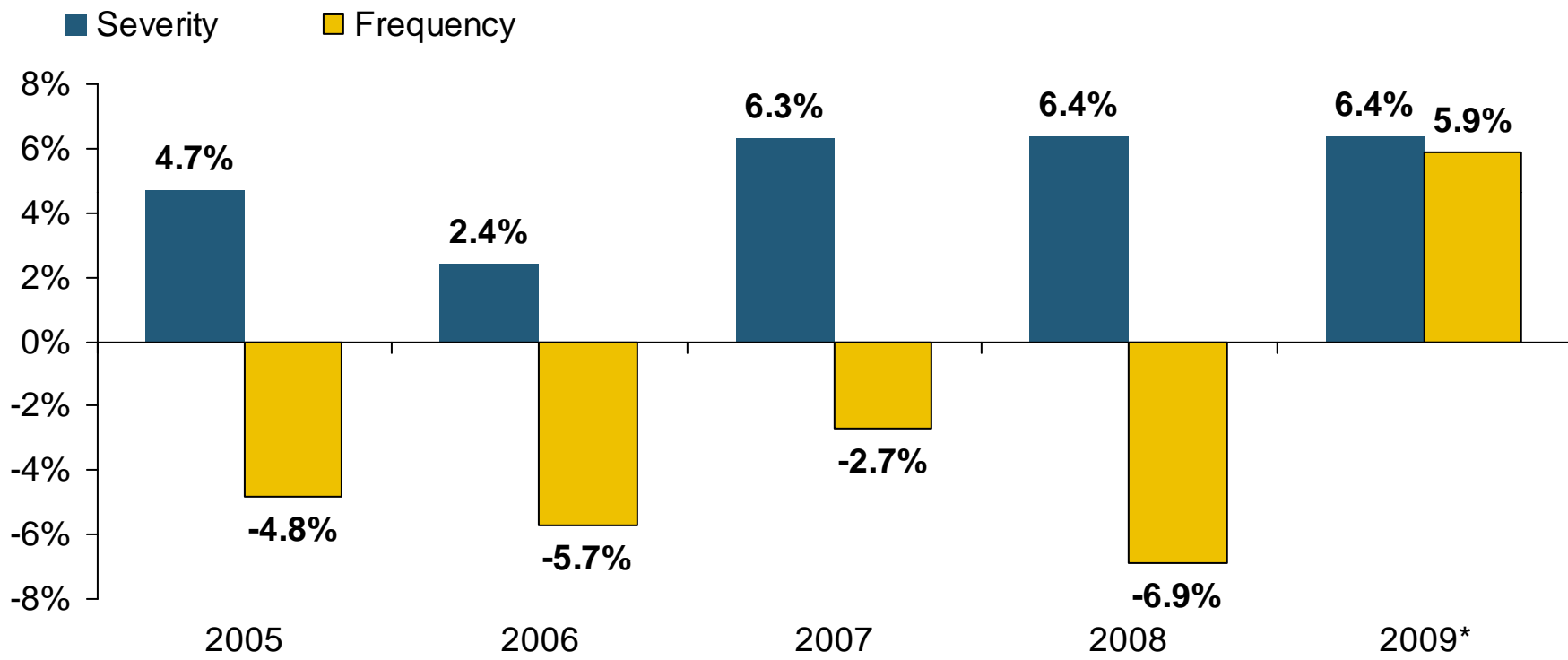
Annual Change, 2005 through 2009



Favorable Severity/Frequency Trends Keeping PD Costs in Check, But Are These Trends Sustainable?

No-Fault (PIP) Liability: Frequency and Severity Trends Are Adverse*

Annual Change, 2005 through 2009

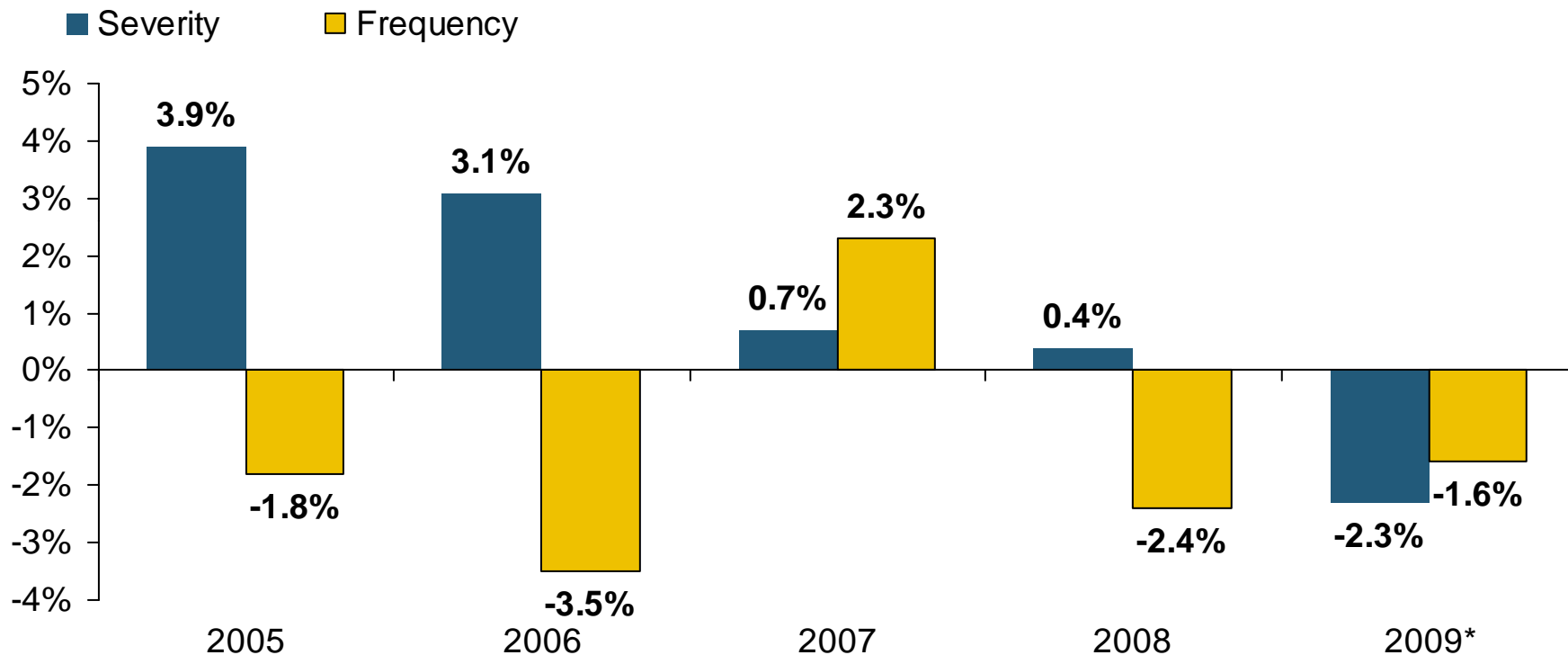


Multiple States Are Experiencing Severe Fraud and Abuse Problems in their No-Fault Systems, Especially FL, MI, NY and NJ

*No-fault states included are: FL, HI, KS, KY, MA, MI, MN, NY, ND and UT.
Source: ISO/PCI *Fast Track* data; Insurance Information Institute

Collision Coverage: Frequency and Severity Trends Have Been Favorable

Annual Change, 2005 through 2009

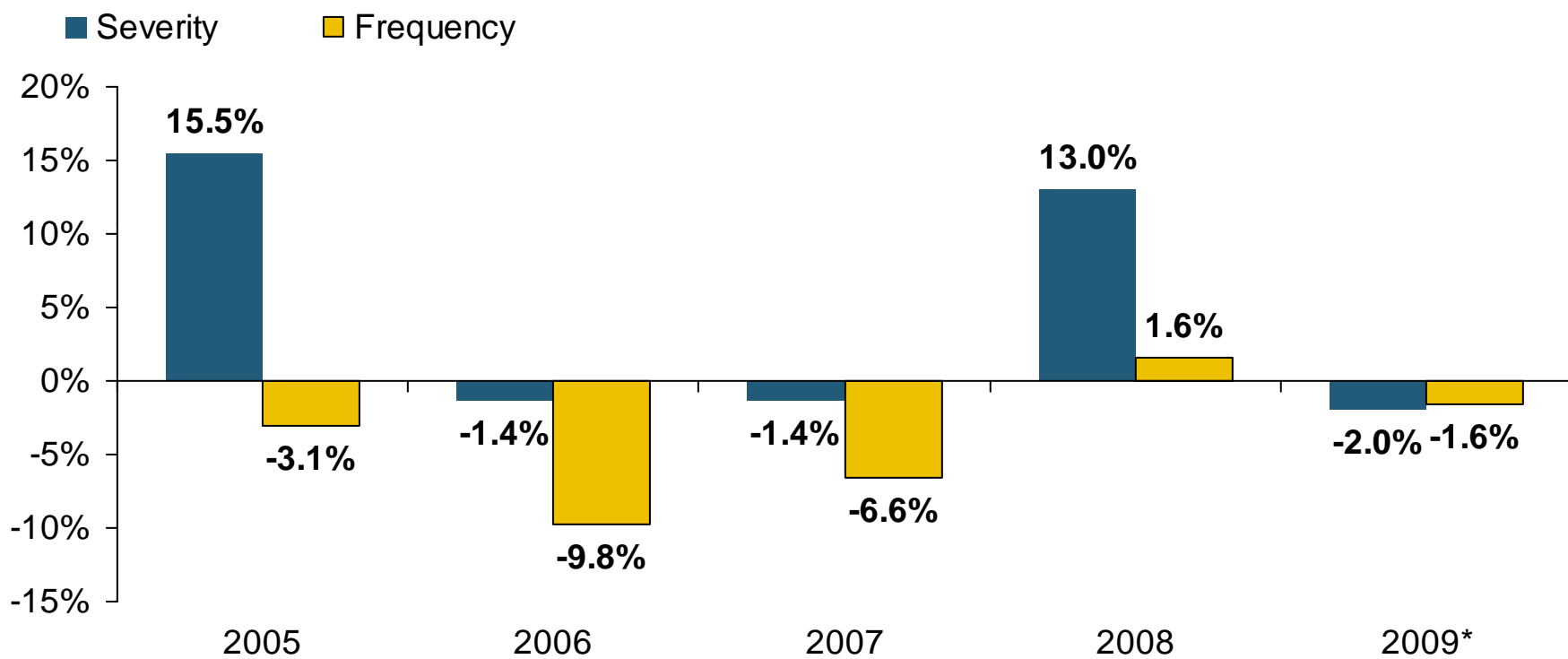


The Recession, High Fuel Prices Have Helped Push Down Frequency and Temper Severity, But this Trend Will Likely Be Reversed Based on Evidence from Past Recoveries

Comprehensive Coverage: Frequency and Severity Trends Favorable in 2009



Annual Change, 2005 through 2009



Weather Creates Volatility for Comprehensive Coverage; Recession Has Helped Push Down Frequency and Temper Severity, But This Factors Will Weaken as Economy Recovers

Source: ISO/PCI *Fast Track* data; Insurance Information Institute

Shifting Legal Liability & Tort Environment

Is the Tort Pendulum Swinging Against Insurers?

Important Issues & Threats Facing Insurers: 2010–2015



Emerging Tort Threat

- No tort reform (or protection of recent reforms) is forthcoming from the current Congress or Administration
- Erosion of recent reforms is a certainty (already happening)
- Innumerable legislative initiatives will create opportunities to undermine existing reforms and develop new theories and channels of liability
- Torts twice the overall rate of inflation
- Influence personal and commercial lines, esp. auto liability
- Historically **extremely** costly to p/c insurance industry
- Leads to reserve deficiency, rate pressure

Bottom Line: Tort “crisis” is on the horizon and will be recognized as such by 2012–2014



- Reverse U.S. Supreme Court decisions on pleadings
- Eliminate pre-dispute arbitration
- Erode federal preemption
- Expand securities litigation
- Pass Foreign Manufactures Legal Accountability Act
- Grant enforcement authorities to state
- Confirm pro-trial lawyer judges – “Federalize Madison County”
- Roll back existing legal reforms

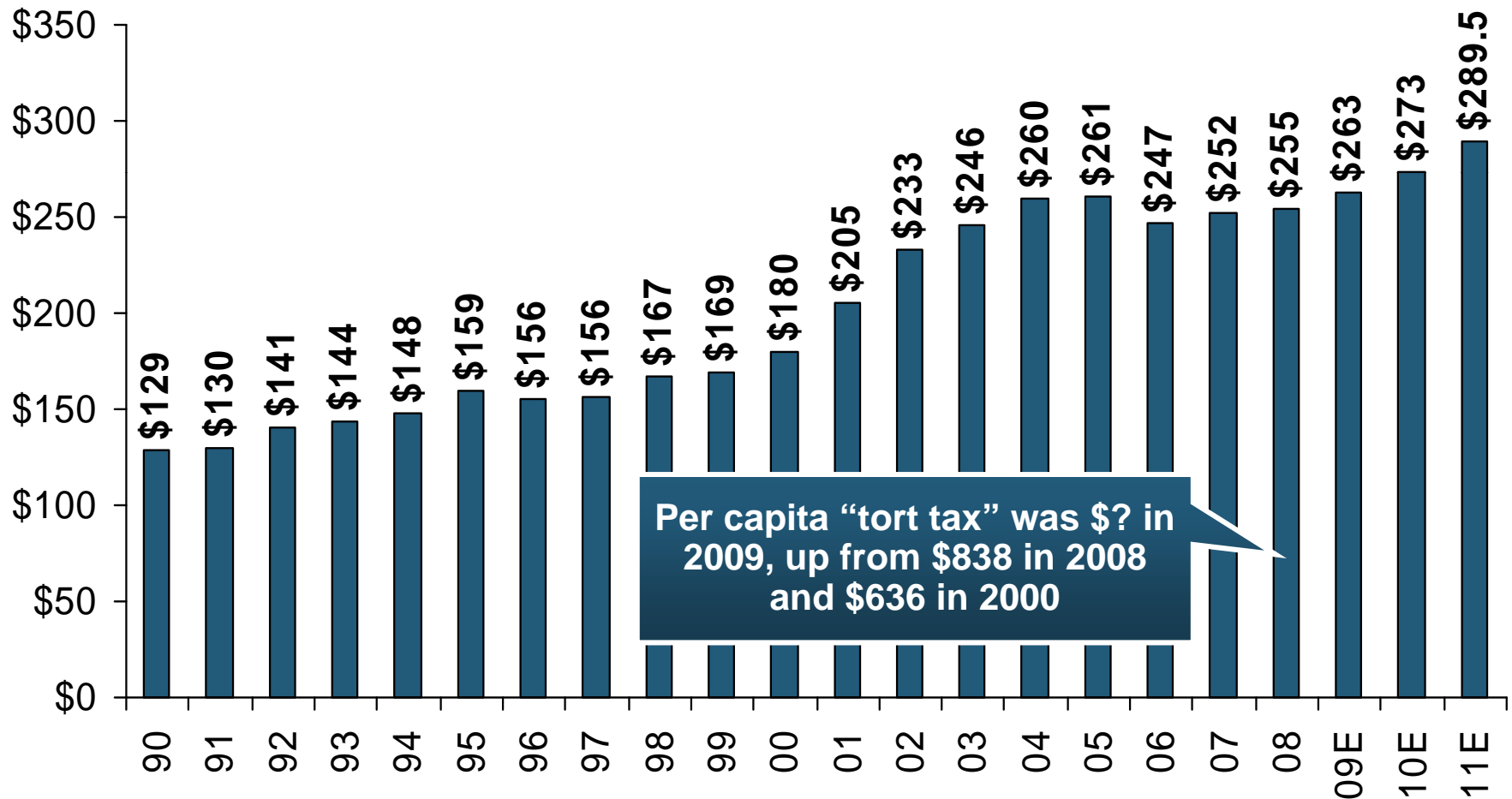
Trial Lawyer Poll: Which Areas Offer the Greatest Potential Benefit?

| Top Categories | Percentage |
|---------------------------------------|------------|
| Environmental | 14% |
| Insurance coverage | 13% |
| Mortgage fraud | 12% |
| Nursing home/seniors issues | 11% |
| Bad-faith against insurance companies | 10% |

41 different practice areas were included as categories

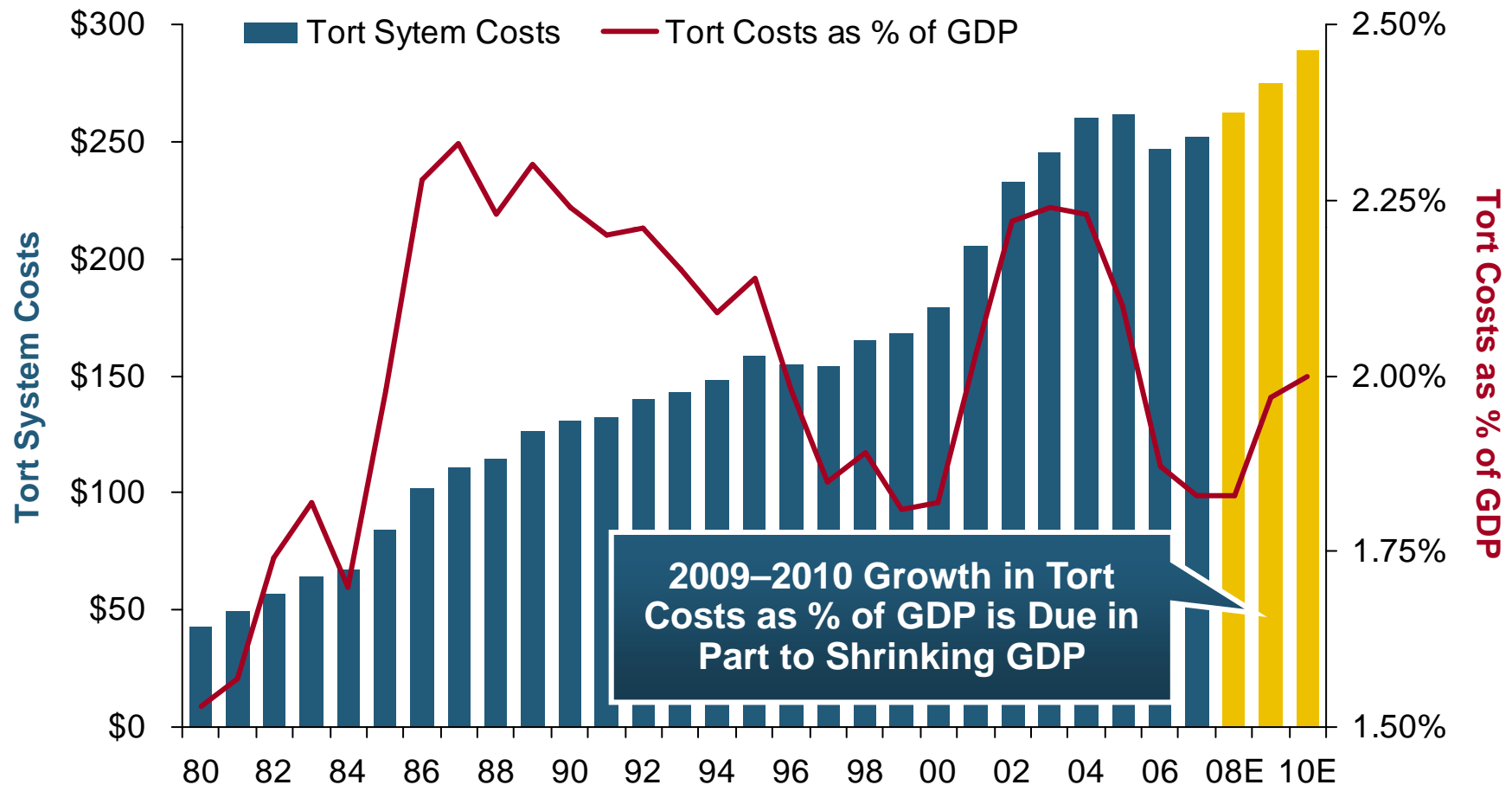
Cost of US Tort System (\$ Billions)

Tort costs consumed 1.79% of GDP in 2008, down from 2.24% in 2003



Over the Last Three Decades, Total Tort Costs* as a % of GDP Appear Somewhat Cyclical

(\$ Billions)



* Excludes the tobacco settlement, medical malpractice

Sources: Tillinghast-Towers Perrin, *2008 Update on US Tort Cost Trends*, Appendix 1A; I.I.I. calculations/estimates for 2009 and 2010

Business Leaders Ranking of Liability Systems in 2009*

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 2009

- 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

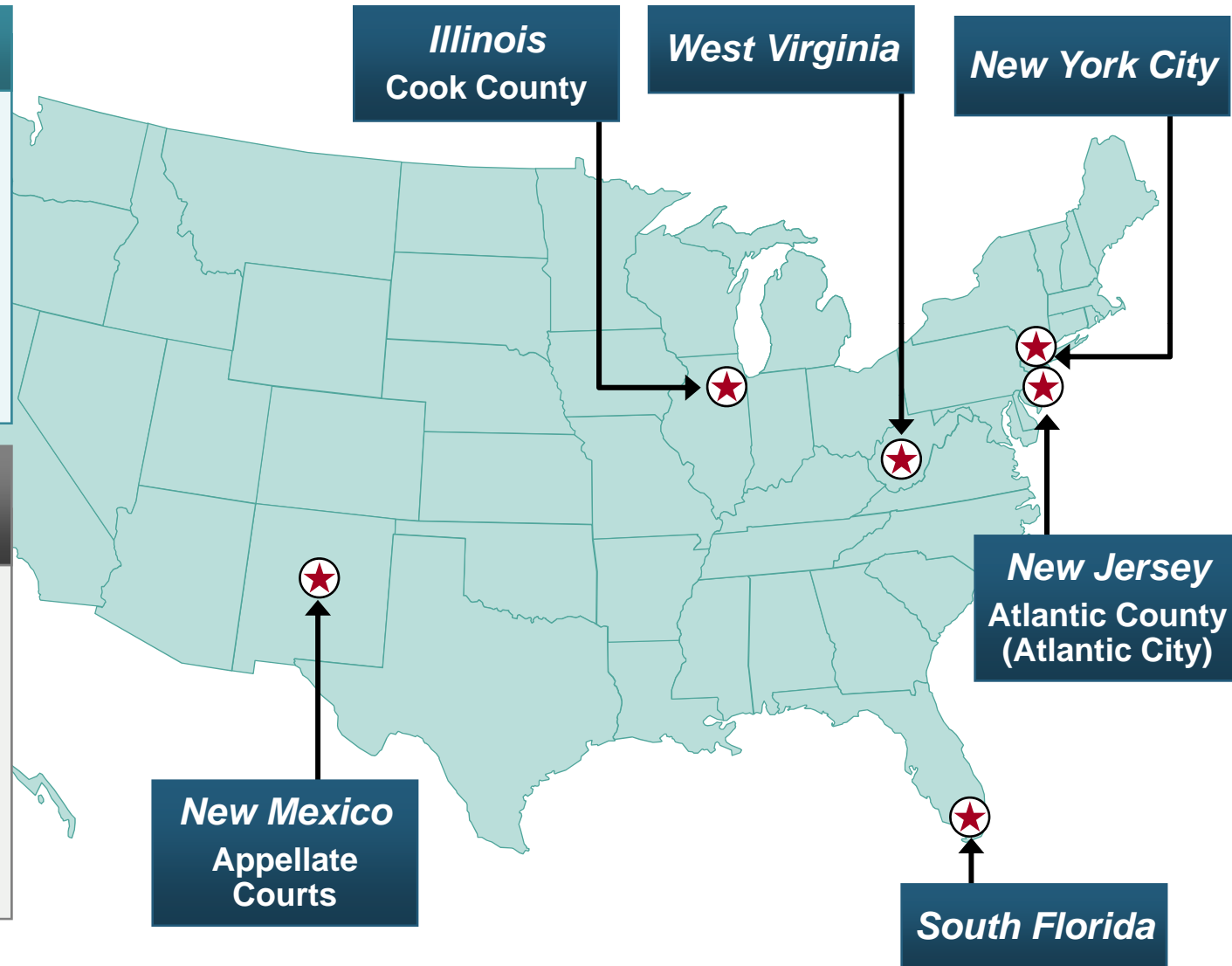
The Nation's Judicial Hellholes: 2010

Watch List

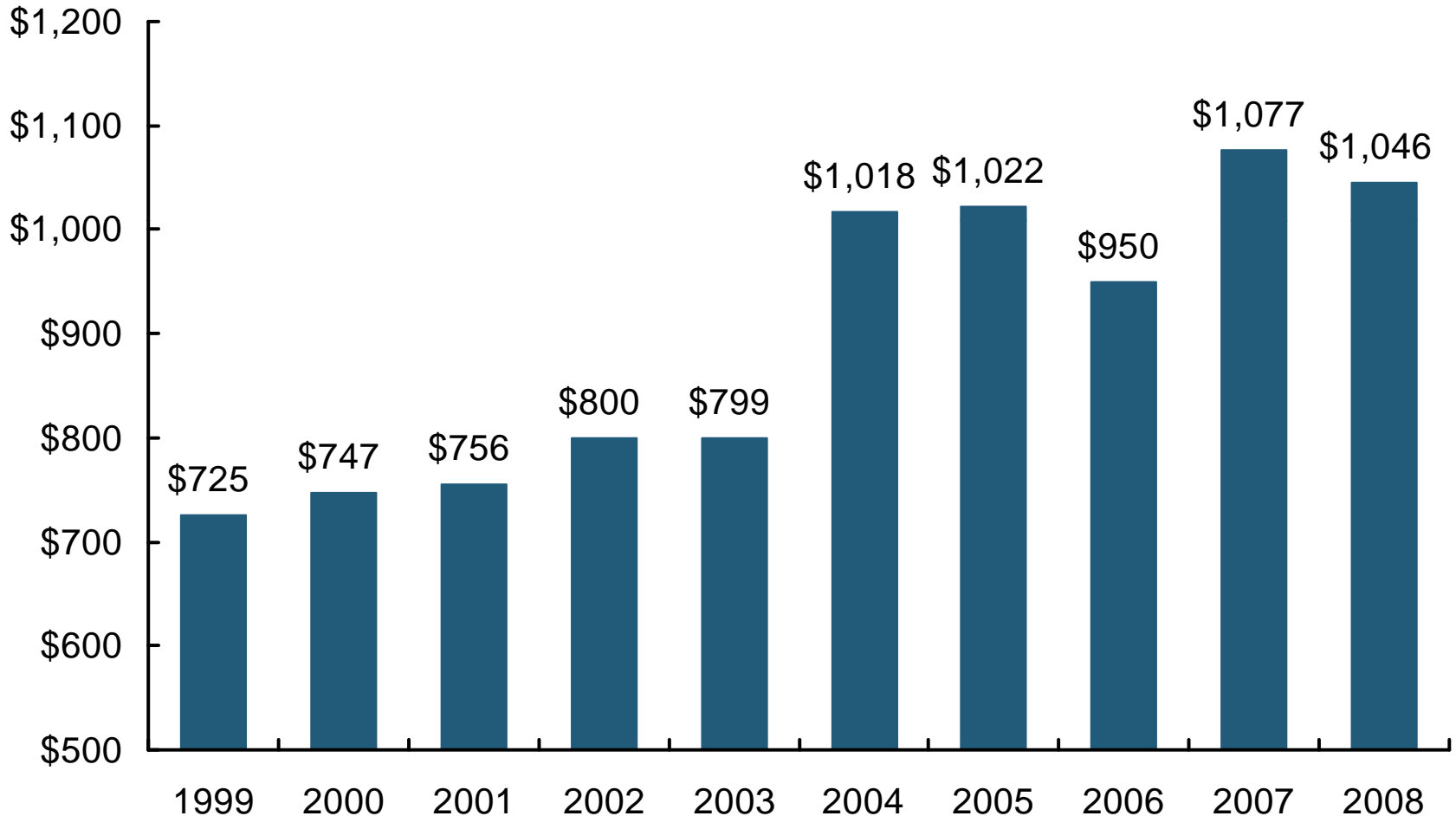
- California
- Alabama
- Madison County, IL
- Jefferson County, MS
- Texas Gulf Coast
- Rio Grande Valley, TX

Dishonorable Mention

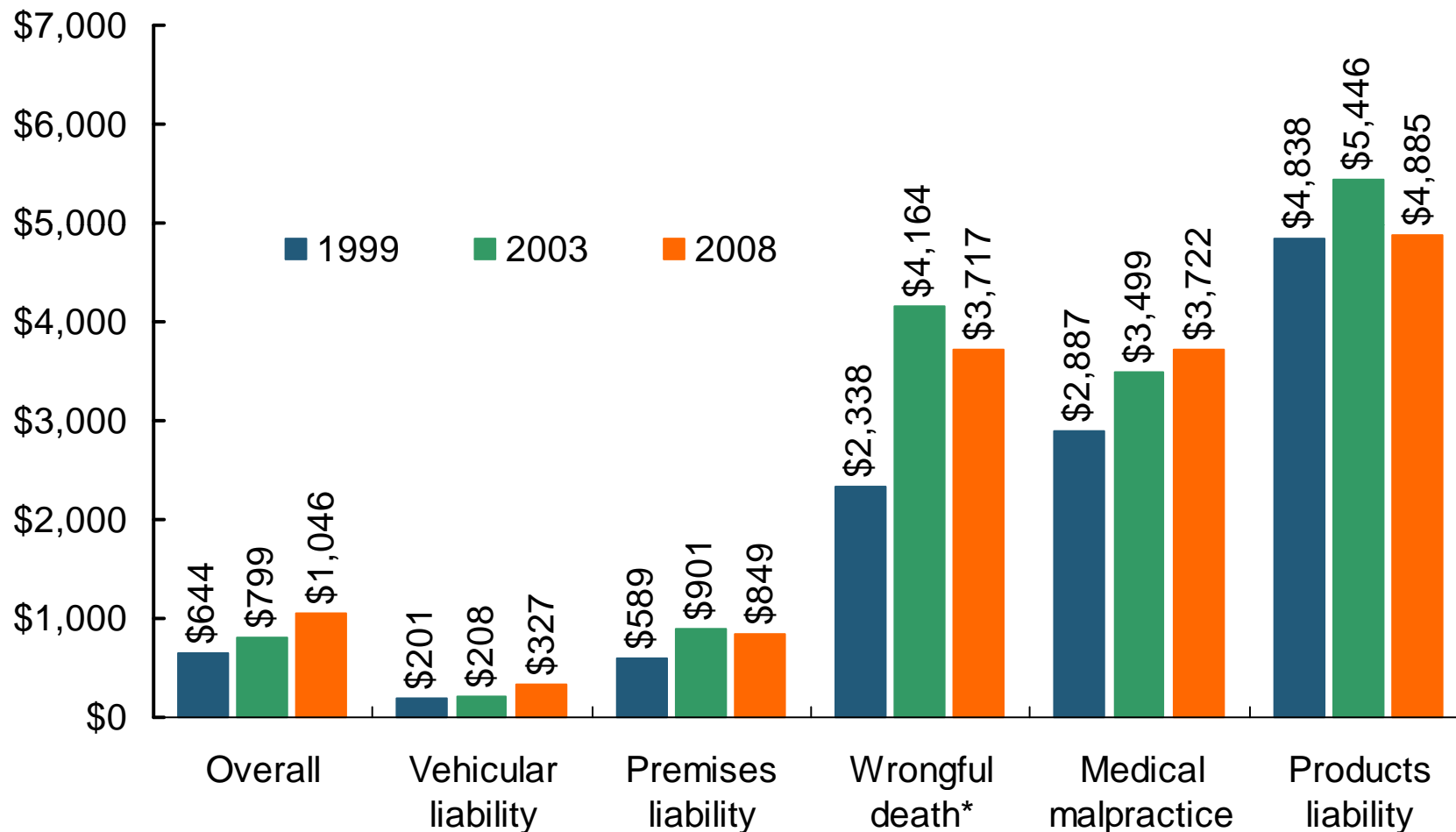
- AR Supreme Court
- MN Supreme Court
- ND Supreme Court
- PA Governor
- MA Supreme Judicial Court
- Sacramento County



Average Jury Awards 1999 - 2008



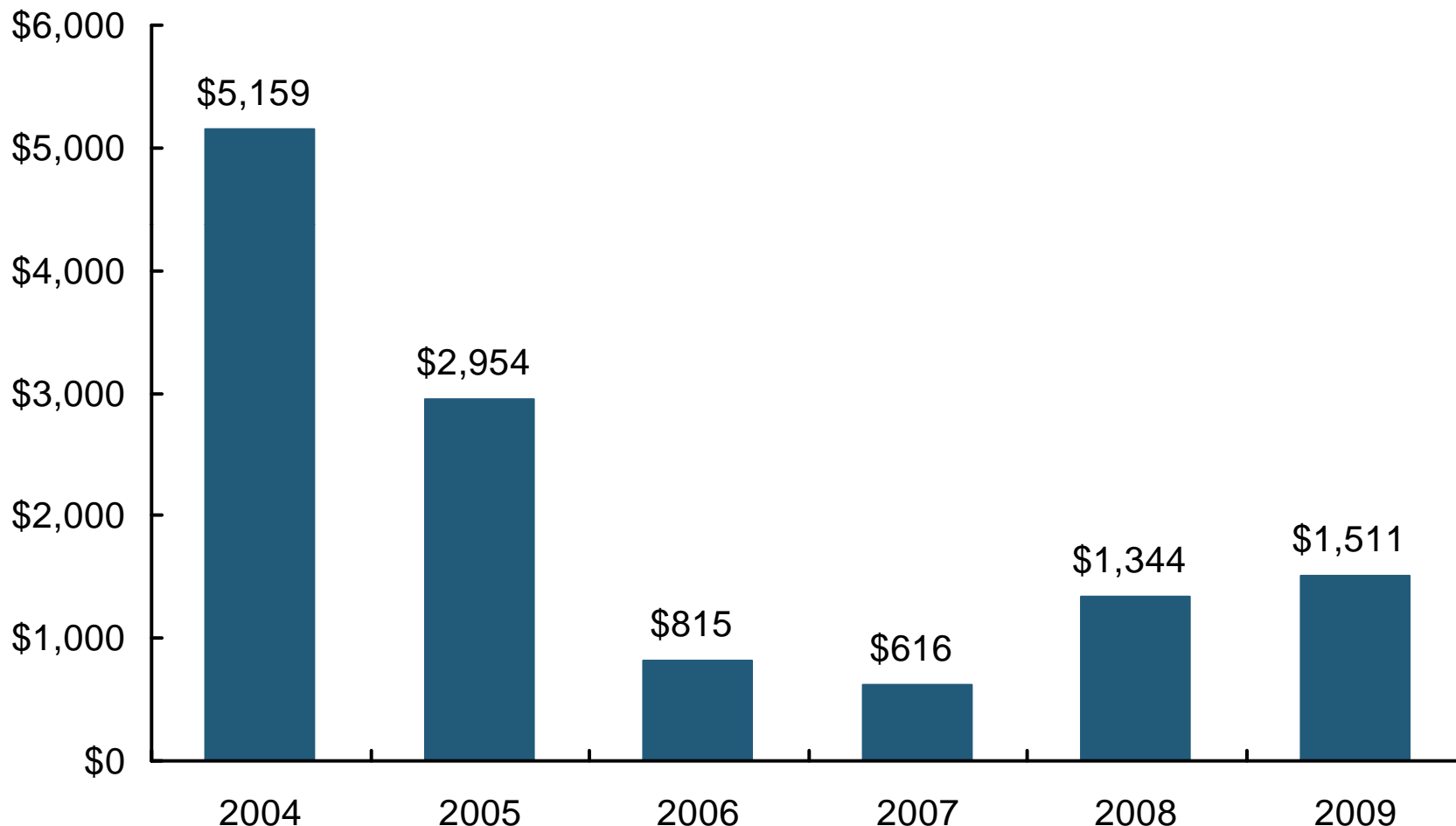
Avg. Jury Awards 1999 vs. 2003 and 2008



*Award trends in wrongful deaths of adult males.

Source: Jury Verdict Research; Insurance Information Institute.

Sum of Top 10 Jury Awards 2004-2009



Source: Insurance Information Institute from Lawyers USA, January 2005, 2006, 2007, 2008, 2009 and 2010.

2009 Top Ten Verdicts

| Value | Issue | State |
|----------------------------|---|---------------------|
| \$370 Million | Defamation | California |
| \$330 Million | Personal Injury (Drunk driving case) | Florida |
| \$300 Million | Personal Injury (Tobacco verdict) | Florida |
| \$89 Million | Personal Injury (Drunk driving case) | Missouri |
| \$78.75 Million | Personal Injury (Prempro) | New Jersey |
| \$77.4 Million | Medical Malpractice | New York |
| <i>\$71 Million</i> | <i>Conversion and Breach of Fiduciary Duty</i> | <i>Texas</i> |
| <i>\$70 Million</i> | <i>Workers Comp Case</i> | <i>Texas</i> |
| \$65 Million | Personal Injury | Florida |
| \$60 Million | Medical Malpractice | New York |

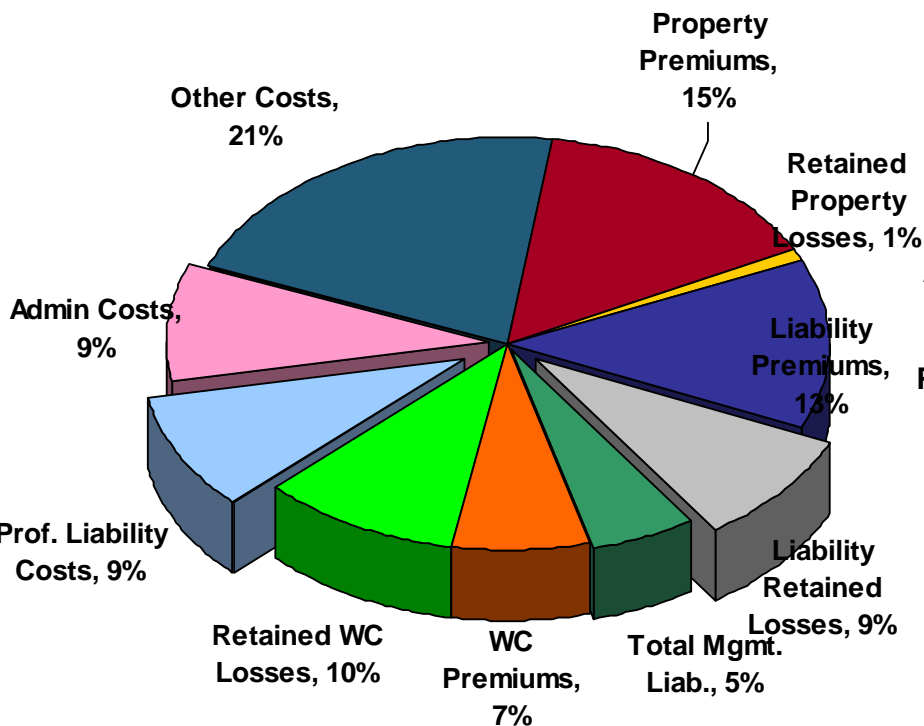
2008 Top Ten Verdicts

| Value | Issue | State |
|----------------------|--|---------------------|
| \$388 Million | Fraud, Intentional Infliction of Emotional Distress | Nevada |
| \$316 Million | Breach of Contract | Georgia |
| \$188 Million | Defamation | New York |
| \$85 Million | Premises Liability | Pennsylvania |
| \$84 Million | Negligence, Personal Injury | Texas |
| \$66 Million | Breach of Fiduciary Duty | Oklahoma |
| \$60 Million | Insurance Bad Faith | Nevada |
| \$55 Million | Negligence | California |
| \$54 Million | Wrongful Death | Georgia |
| \$48 Million | Negligence | Indiana |

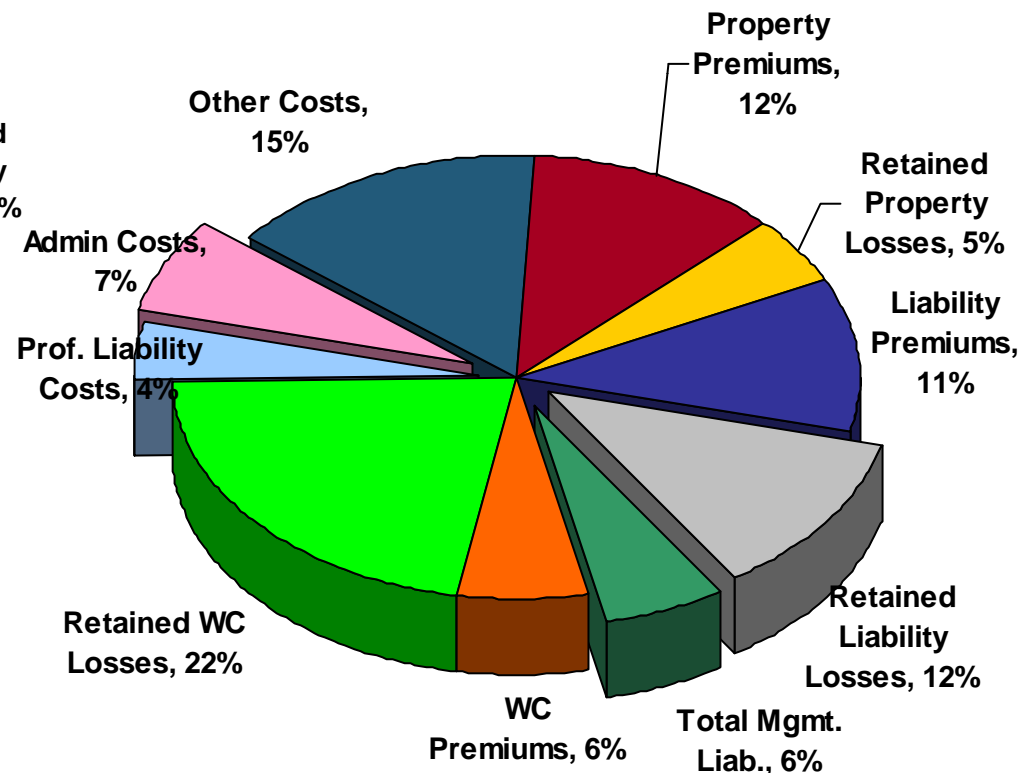
How the Risk Dollar is Spent (2008)

Total liability costs account for about 30% of the risk dollar

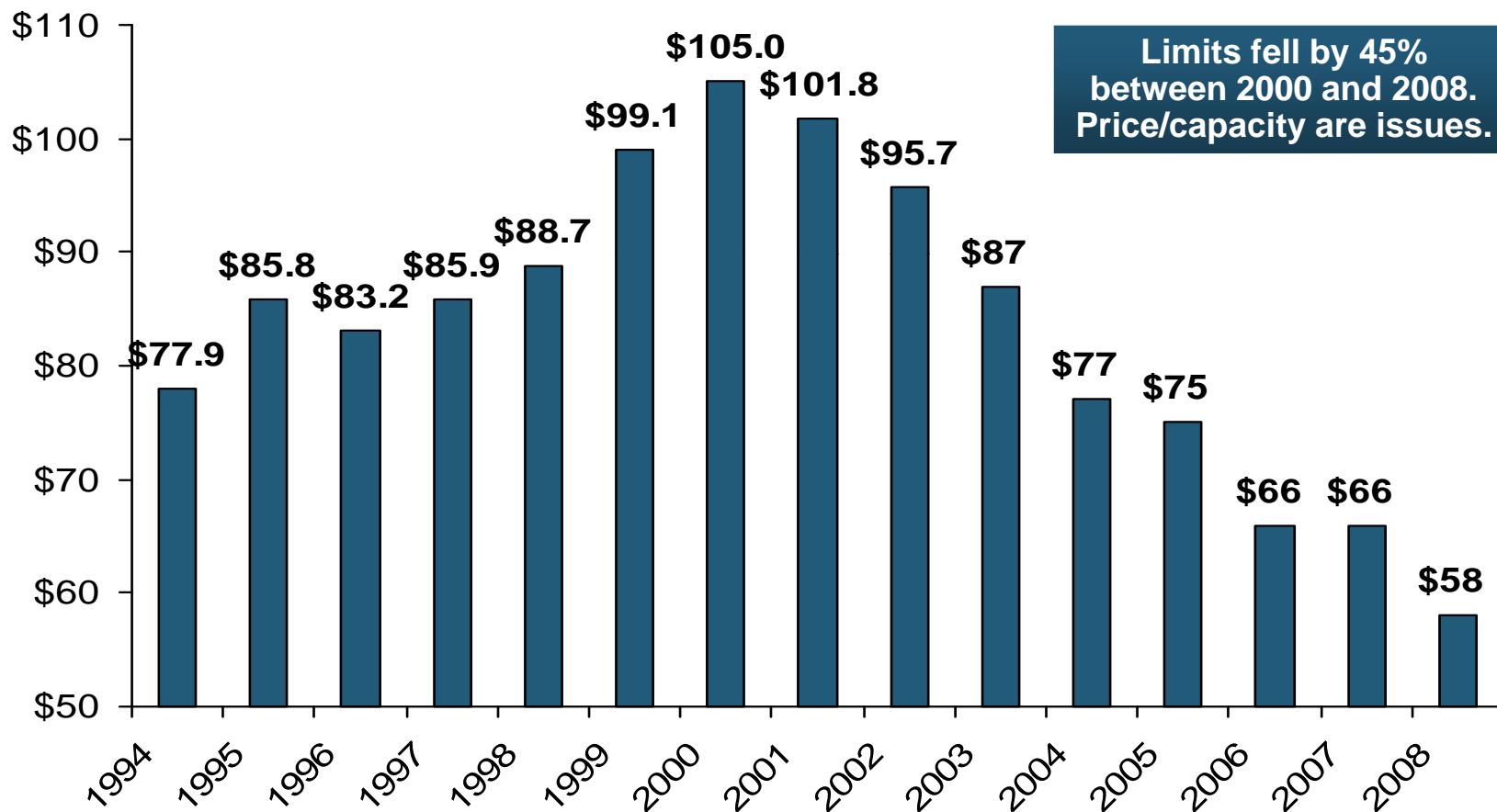
Firms w/Revenues < \$1 Billion



Firms w/Revenues > \$1 Billion



Average Total Limits Purchased by All U.S. Firms* (\$ Millions)

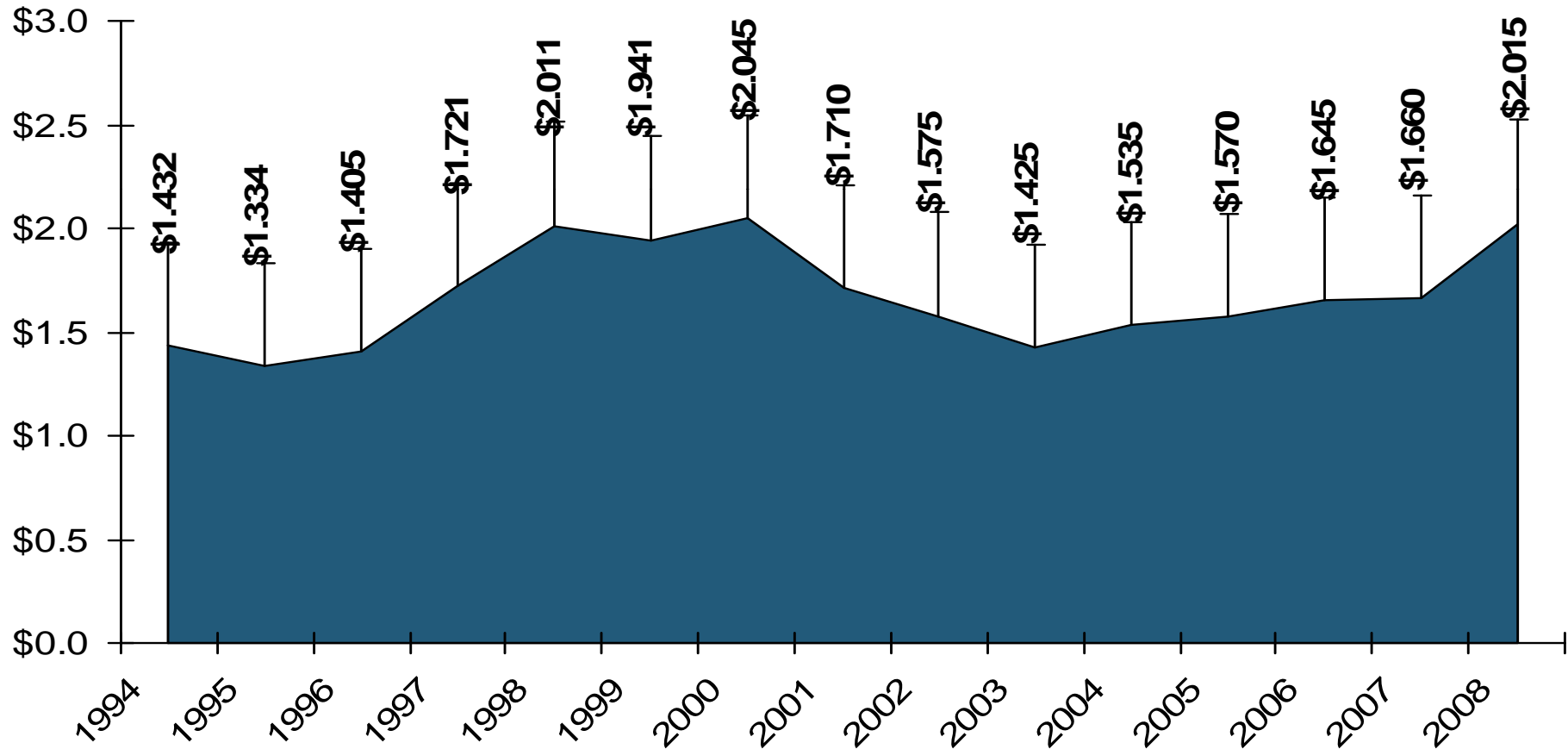


*Includes underlying primary limits

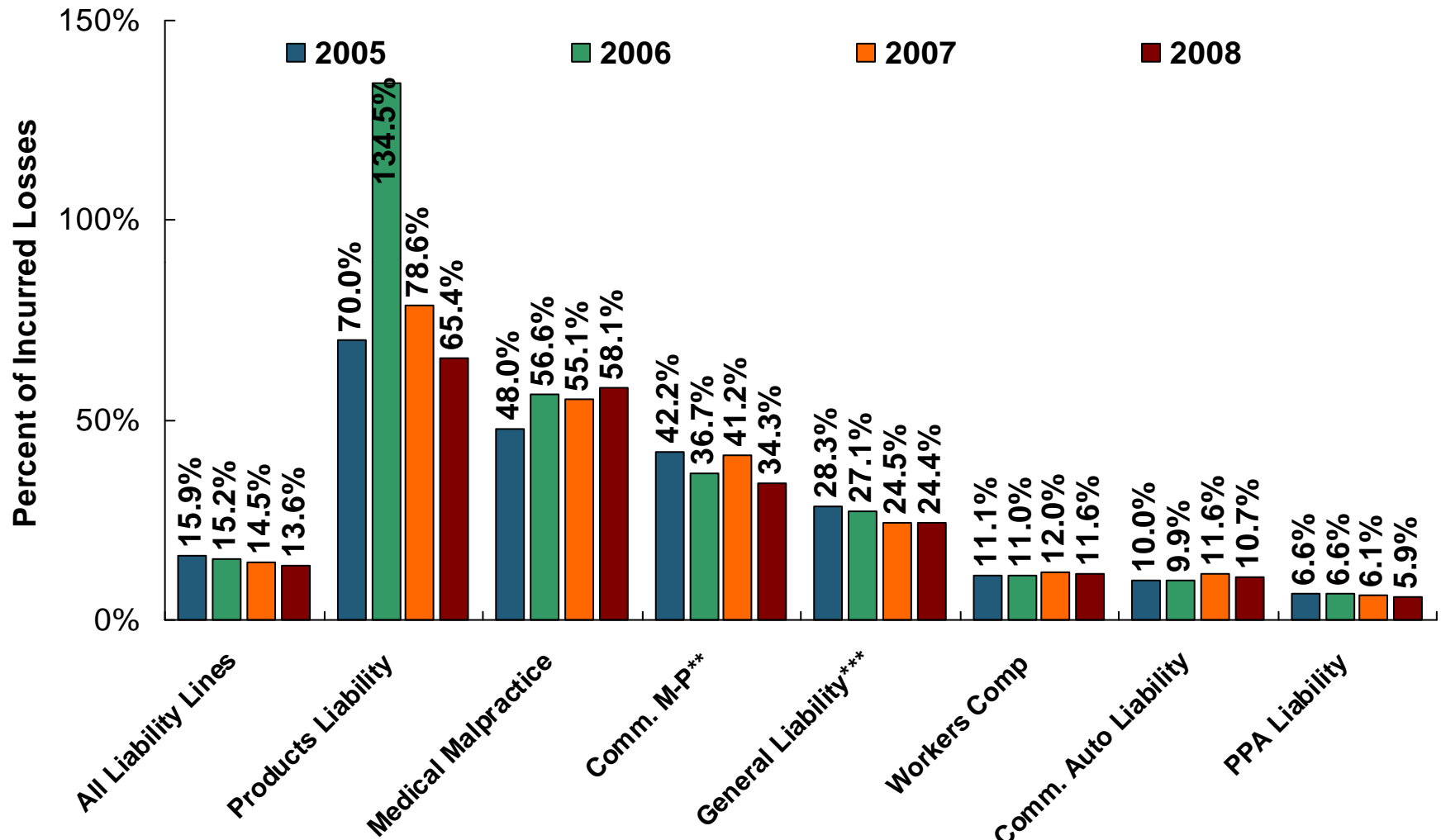
Source: *Limits of Liability 2008*, Marsh, Inc.

Excess Liability Market Capacity North America (\$ Billions)

In 2008, capacity is back to 2000 levels.



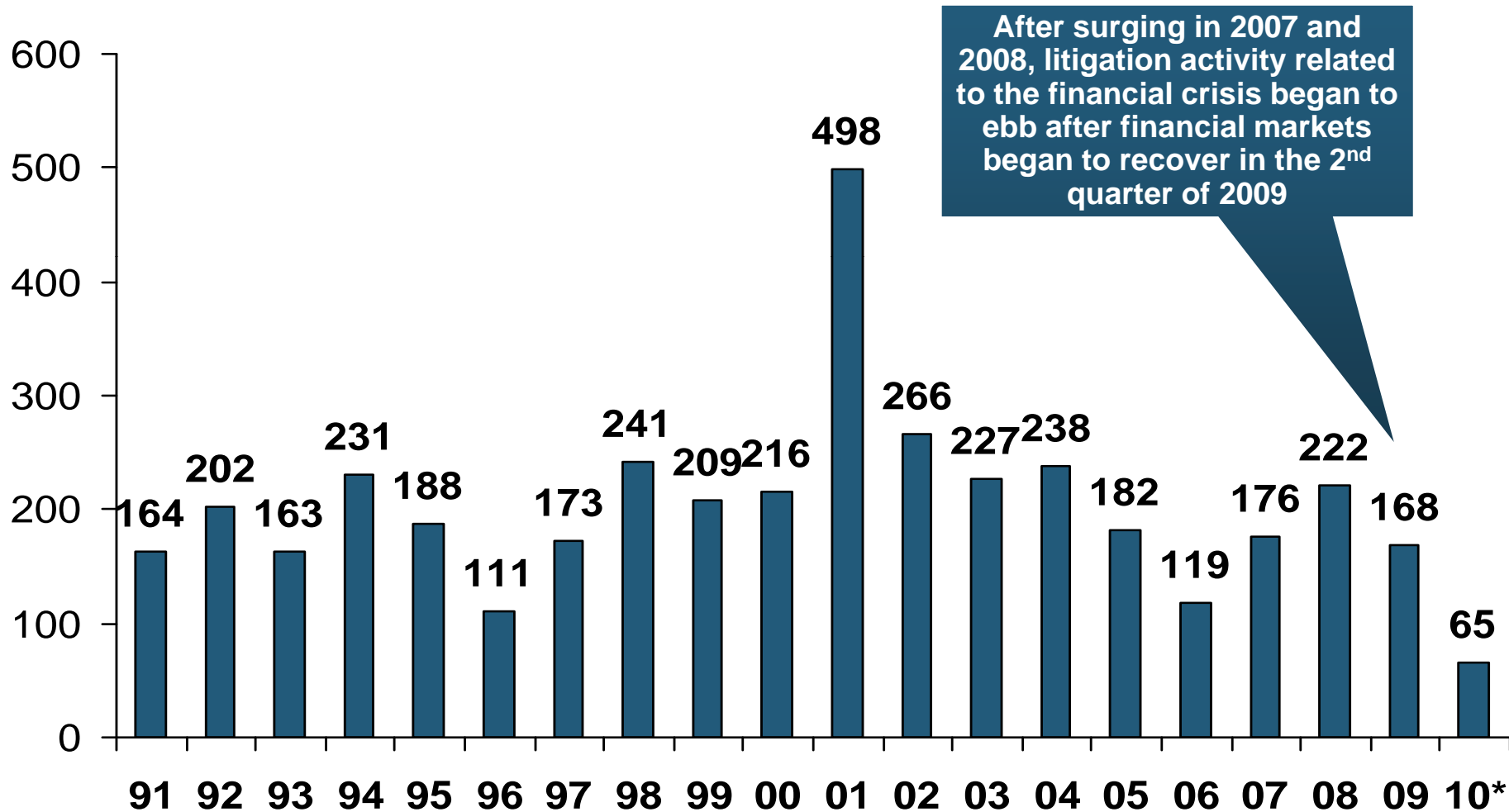
Insurer Defense & Cost Containment Expenses as a % of Incurred Losses, 2005-2008*



*Net of reinsurance, excl. state funds. **Liability portion only. ***Excludes products liability.

Source: National Association of Insurance Commissioners (NAIC) Annual Statement Database, via Highline Data, LLC; Insurance Information Institute.

Shareholder Class Action Lawsuits*

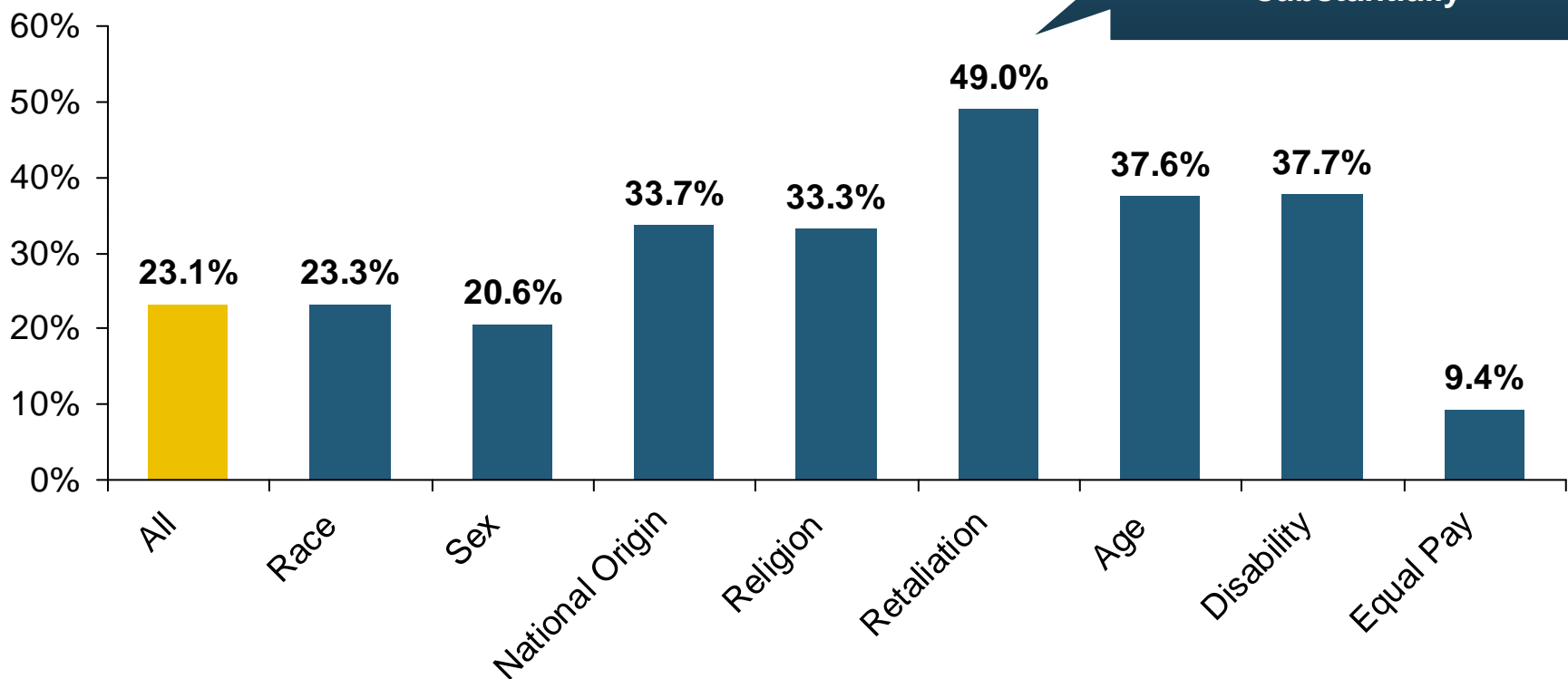


*Securities fraud suits filed in U.S. federal courts as of June 25, 2010.

Source: Stanford University School of Law (securities.stanford.edu); Insurance Information Institute

Discrimination Charges Filed with EEOC by Type: Percent Change FY06-FY09

Change in Charges Filed (%)

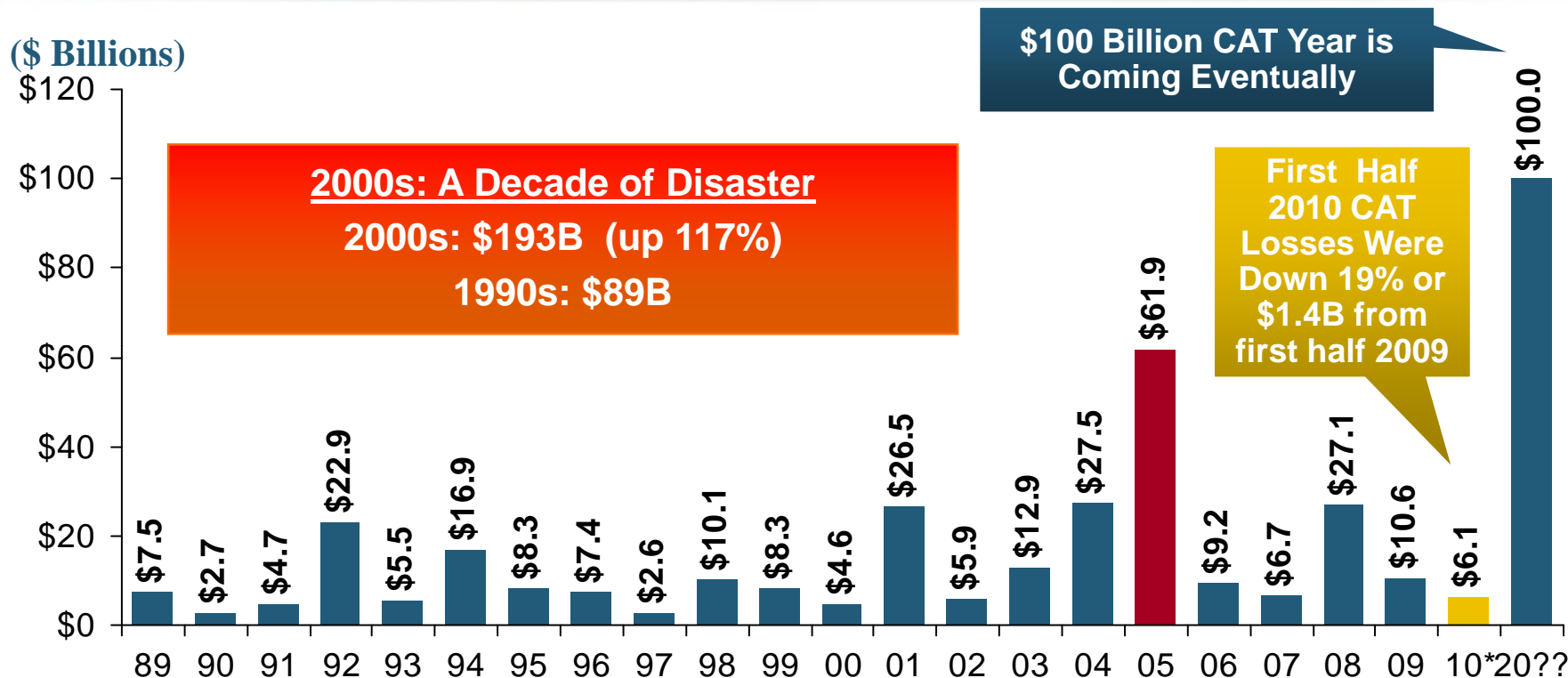


Retaliation and age discrimination suits are up substantially

The Financial Crisis and Poor Labor Market Conditions Have Contributed to a Surge Employment Discrimination Charges

Catastrophic Loss – Catastrophe Losses Trends Are Trending Adversely

US Insured Catastrophe Losses



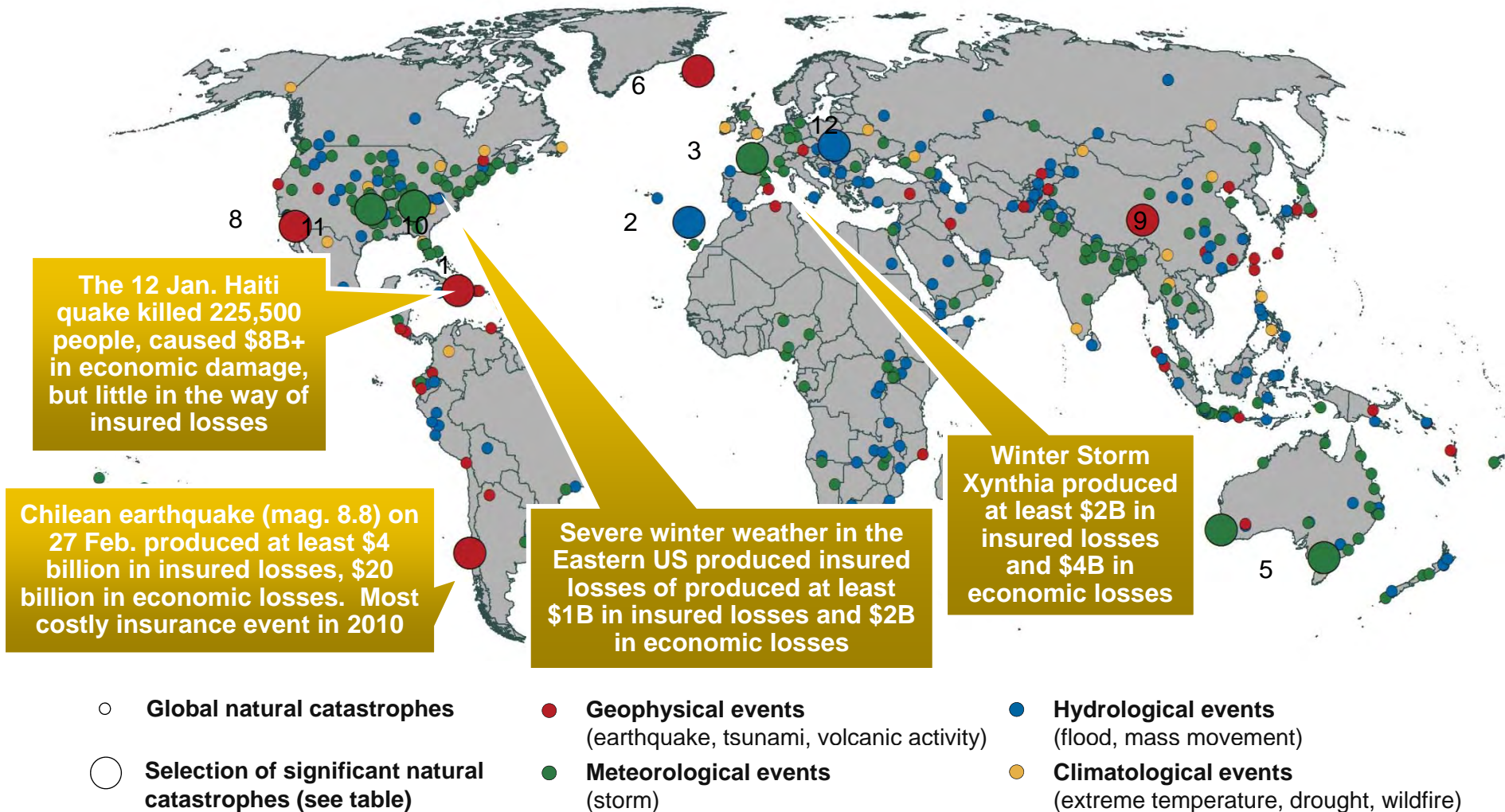
2010 CAT Losses Are Running Below 2009, So Far
Figures Do Not Include an Estimate of Deepwater Horizon Loss

*Through June 30, 2010.

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; Munich Re; Insurance Information Institute.

Global Natural Catastrophes: January – June 2010



Probability of Landfall of at Least One Major Hurricane (CAT 3-4-5) in 2010*

| Region | Average Over Last Century | 2010 Forecast * |
|--|---------------------------|-----------------|
| Entire U.S. Coastline | 52% | 76% |
| U.S. East Coast Incl. FL Peninsula | 31% | 51% |
| Gulf Coast from FL Panhandle to Brownsville, TX | 30% | 50% |
| Caribbean | 42% | 65% |

The Probability of a Major Hurricane Making Landfall Somewhere Along the US Coast is Greatly Elevated in 2010, Including a 50% Chance Along the Oil Spill-Impacted Gulf Coast

*Forecast as of June 2, 2010.

Source: Colorado State University, Department of Atmospheric Sciences; Insurance Information Institute.

Outlook for 2010 North Atlantic Hurricane Season*

| Forecast Parameter | Average (1950-2000) | 2010 Forecast * |
|--------------------------------------|------------------------|--------------------|
| Named Storms | 9.6 | 18 |
| Named Storm Days | 49.1 | 90 |
| Hurricanes | 5.9 | 10 |
| Hurricane Days | 24.5 | 40 |
| Major Hurricanes | 2.3 | 5 |
| Major Hurricane Days | 5.0 | 13 |
| Accumulated Cyclone Energy | 96.1 | 185 |
| Net Tropical Cyclone Activity | 100% | 195% |

The 2010 Hurricane Season is Expected to Be Nearly Twice as Active as the Long-Run Average (195% of Normal)

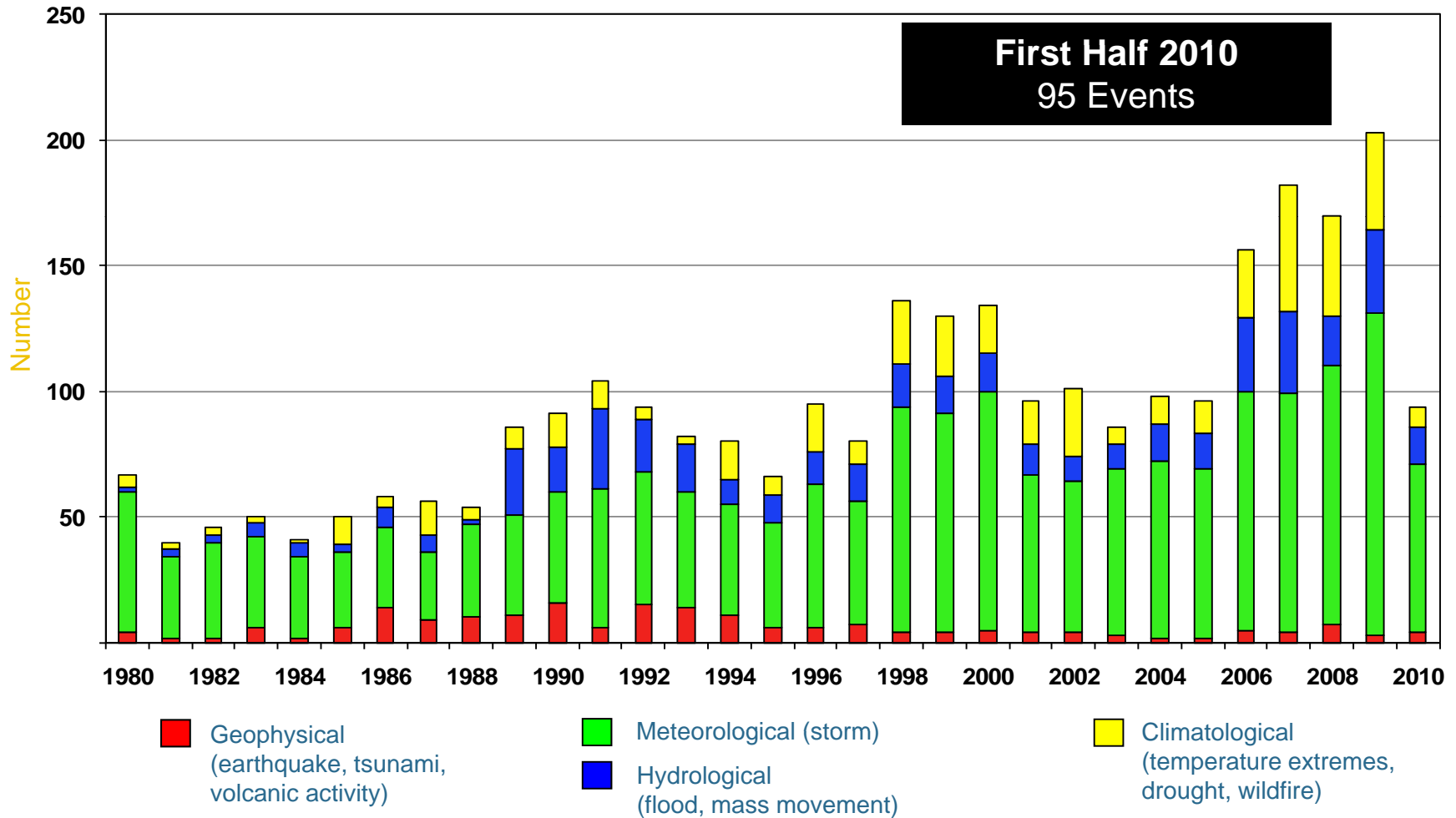
*Forecast as of June 2, 2010.

Source: Colorado State University, Department of Atmospheric Sciences; Insurance Information Institute.

Natural Disasters in the United States, 1980 – 2010

Number of Events (Annual Totals 1980 – 2009 vs. First Half 2010)

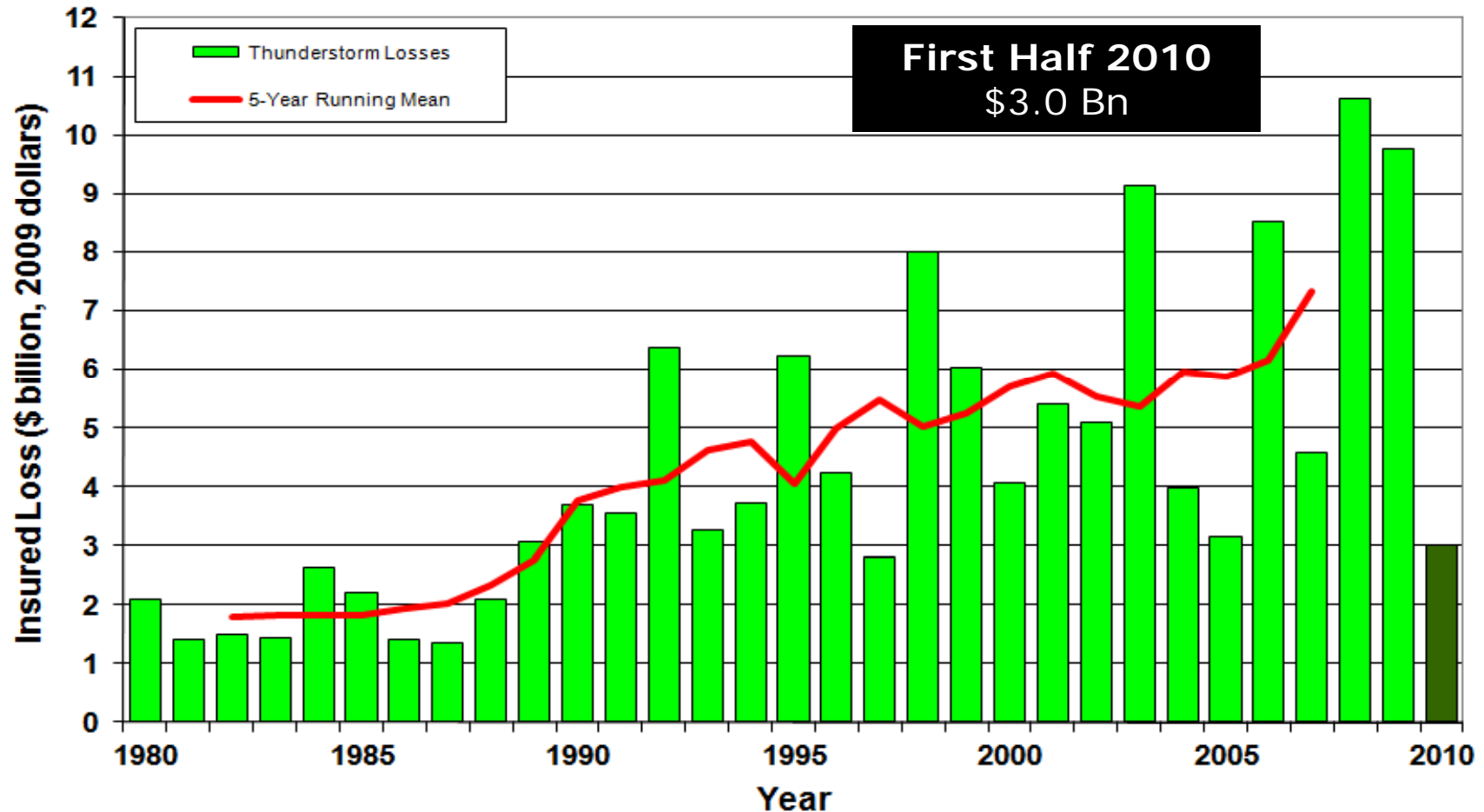
Number of events in first half of 2010 is close to the annual totals from five of past ten years.



U.S. Thunderstorm Loss Trends

Annual Totals 1980 – 2009 vs. First Half 2010

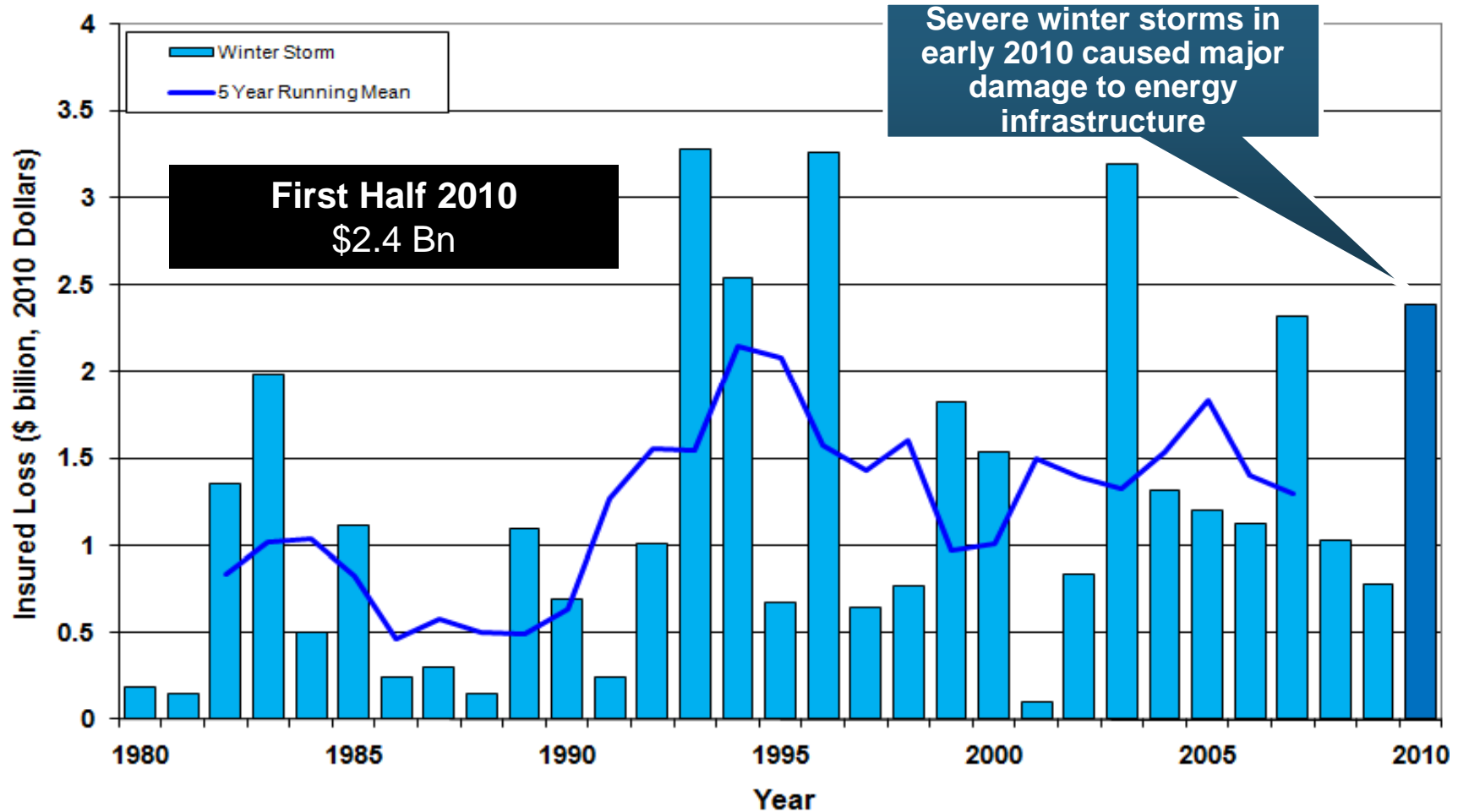
Thunderstorm losses have quadrupled since 1980.



U.S. Winter Storm Loss Trends

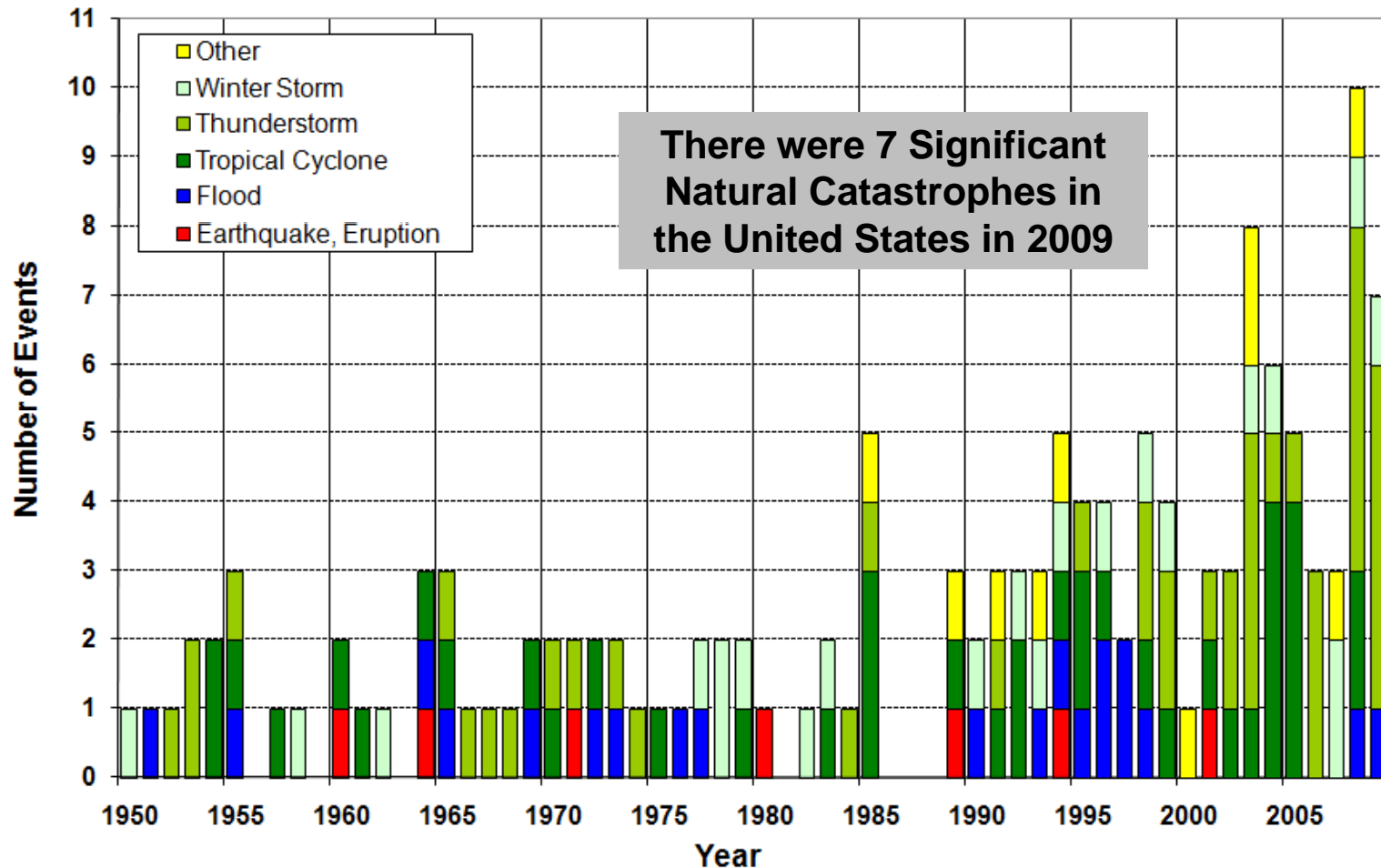
Annual totals 1980 – 2009 vs. First Half 2010

Average annual winter storm losses have increased over 50% since 1980.



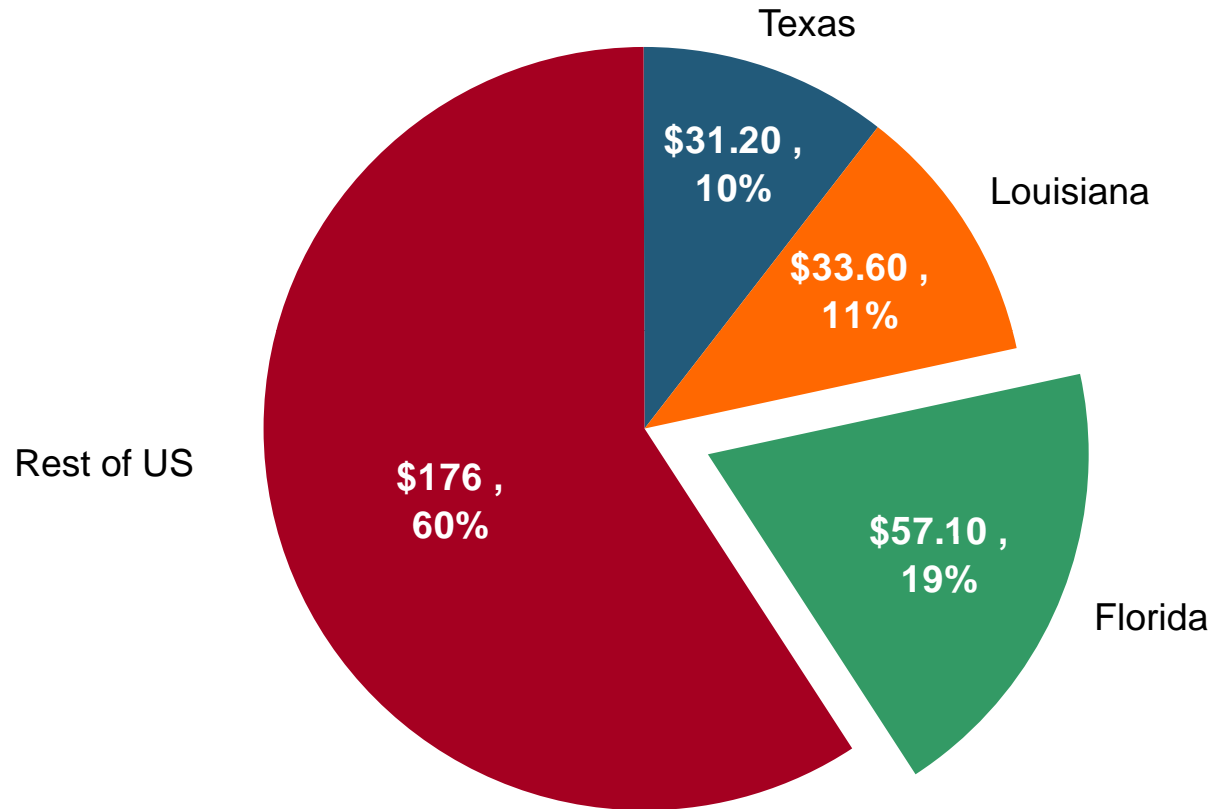
U.S. Significant Natural Catastrophes, 1950 – 2009

Number of Events (\$1+ Bill economic loss and/or 50+ fatalities)



Distribution of US Insured CAT Losses: TX, FL, LA vs. US, 1980-2008*

(\$ Billions)



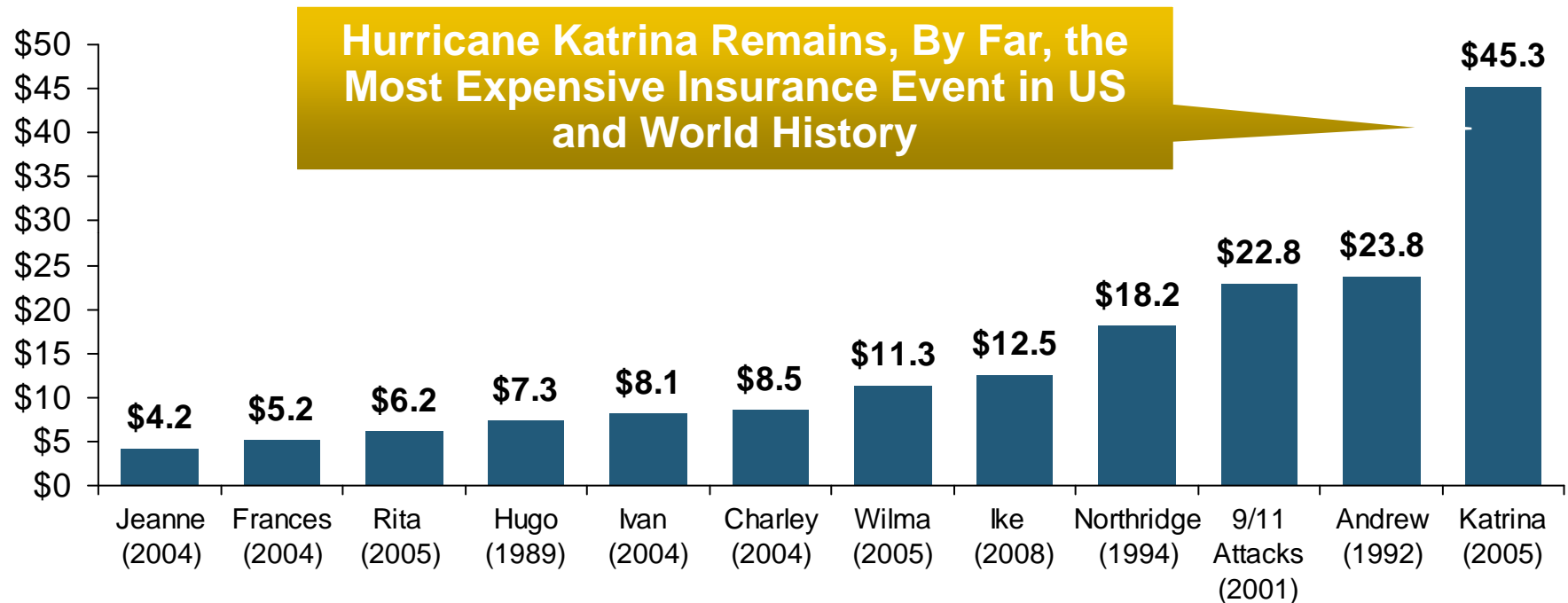
**Florida Accounted for 19% of All US Insured CAT Losses
from 1980-2008: \$57.1B out of \$297.9B**

* All figures (except 2006-2008 loss) have been adjusted to 2005 dollars.

Source: PCS division of ISO.

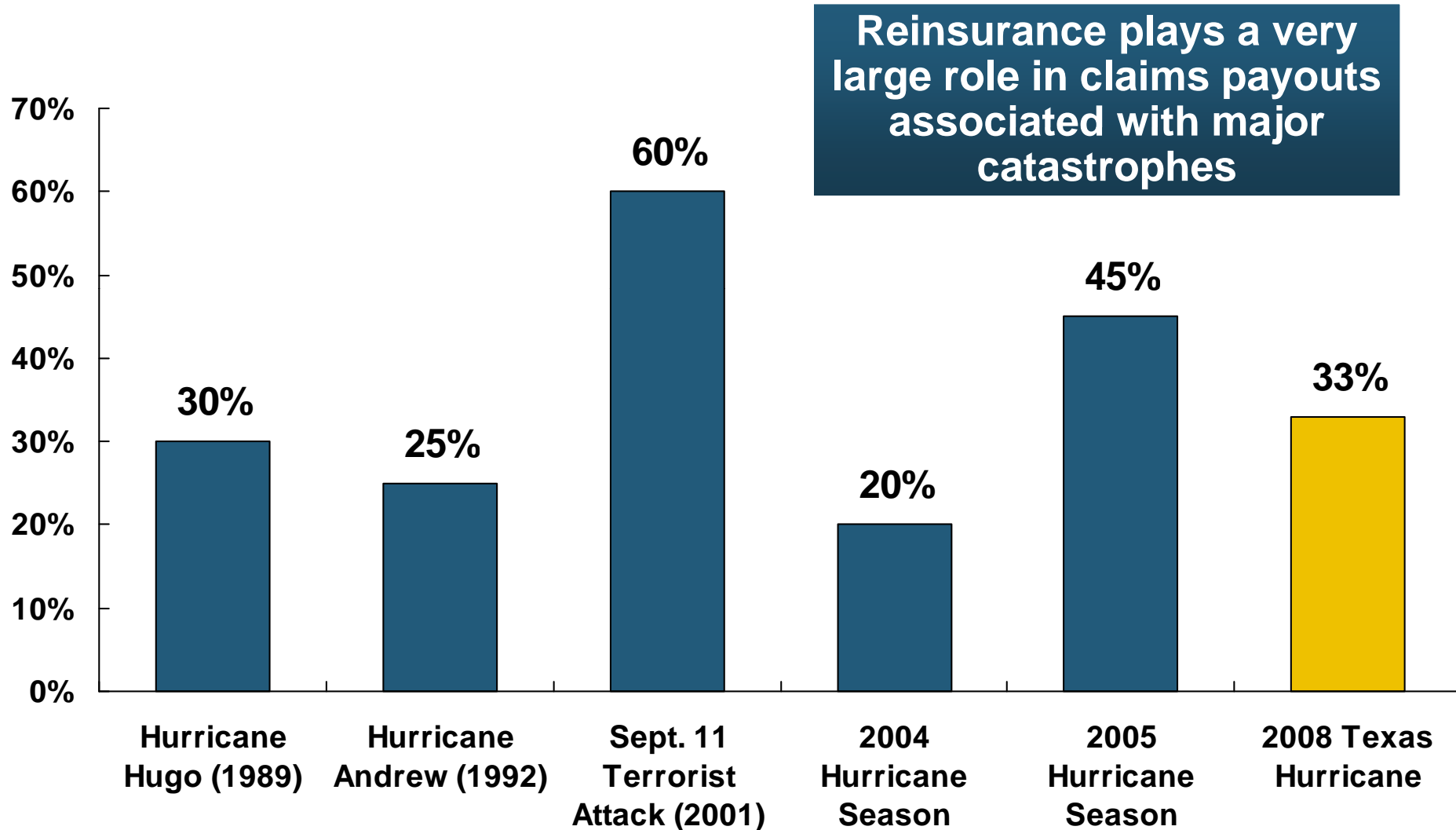
Top 12 Most Costly Disasters in US History

(Insured Losses, 2009, \$ Billions)



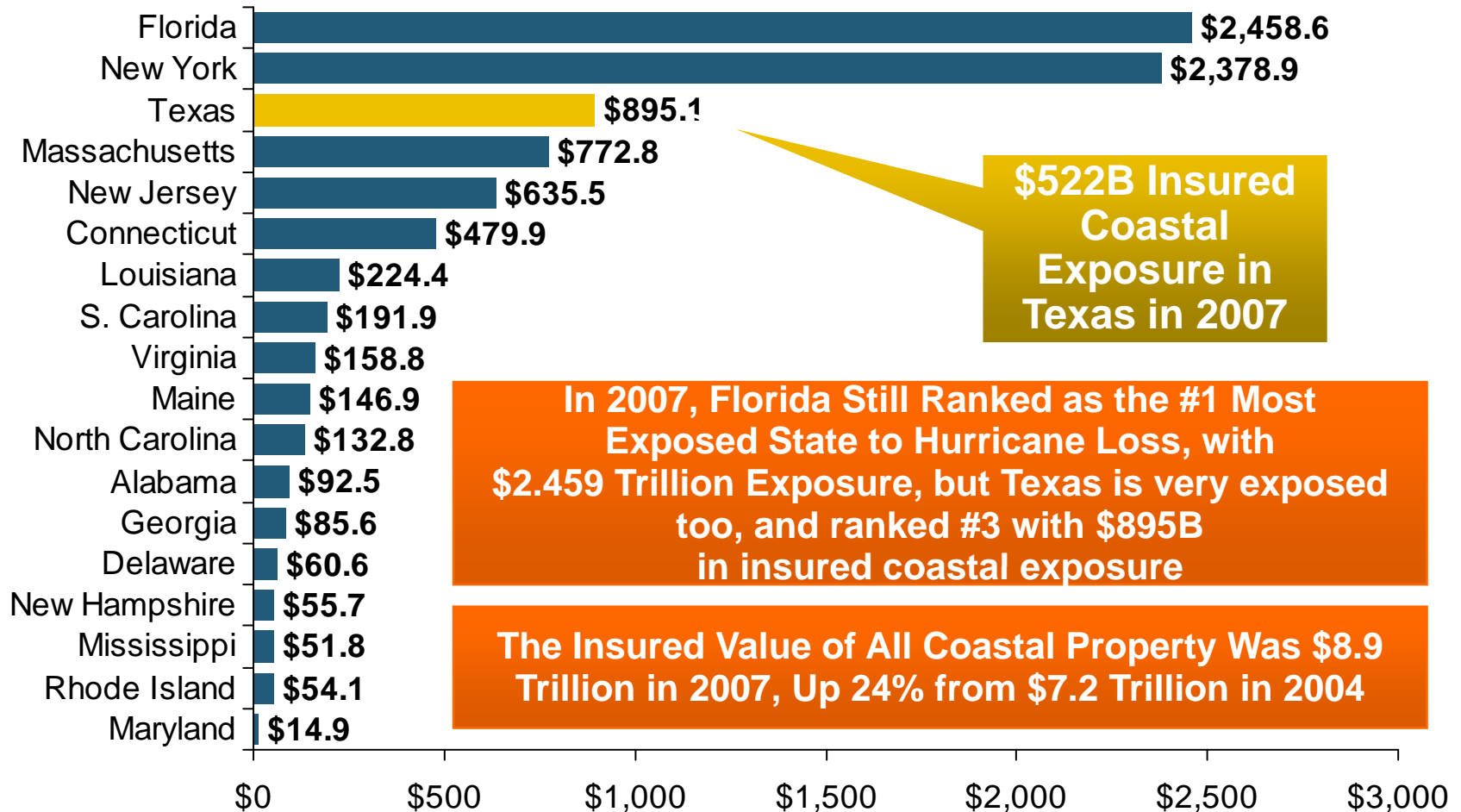
**8 of the 12 Most Expensive Disasters in US History
Have Occurred Since 2004;
*8 of the Top 12 Disasters Affected FL***

Share of Losses Paid by Reinsurers for Major Catastrophic Events



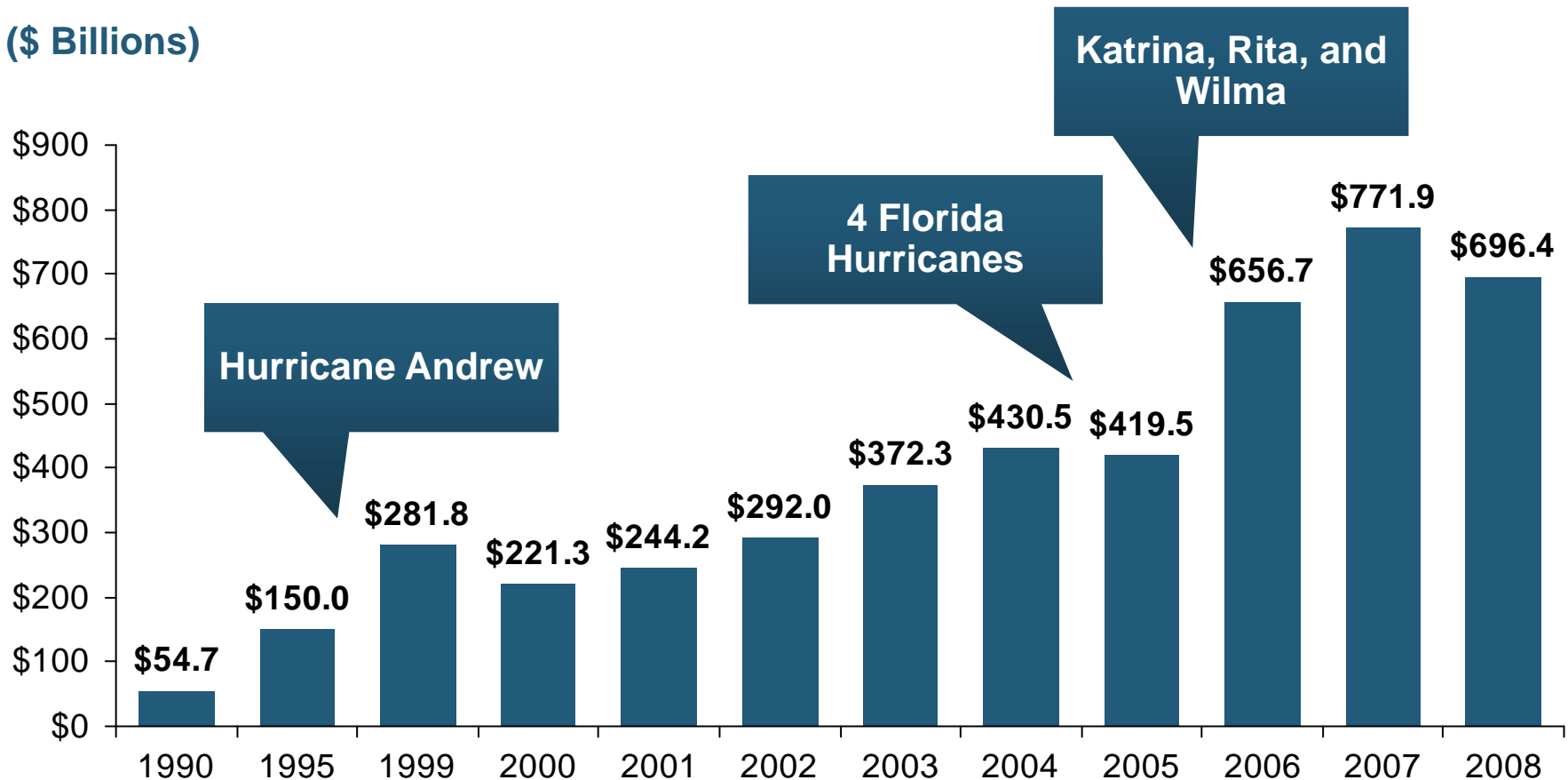
Total Value of Insured Coastal Exposure

(2007, \$ Billions)



US Residual Market Exposure to Loss

(\$ Billions)



In the 19-year Period Between 1990 and 2008, Total Exposure to Loss in the Residual Market (FAIR & Beach/Windstorm) Plans Has Surged from \$54.7B in 1990 to \$696.4B in 2008

The Deepwater Horizon Disaster

Insurance and Energy Market Implications

Largest International Oil Well Blowouts by Volume, as of July 12, 2010

| Date | Well | Location | Bbl Spilled |
|------------------------------|-------------------------------|----------------------------|-------------------------------------|
| April 20 2010-present | Deepwater Horizon | Gulf of Mexico, USA | est. 4,050,000 thru July 12* |
| June 1979-April 1980 | Ixtoc I | Bahia del Campeche, Mexico | 3,300,000 |
| October 1986 | Abkatun 91 | Bahia del Campeche, Mexico | 247,000 |
| April 1977 | Ekofisk Bravo | North Sea, Norway | 202,381 |
| January 1980 | Funiwa 5 | Forcados, Nigeria | 200,000 |
| October 1980 | Hasbah 6 | Gulf, Saudi Arabia | 105,000 |
| December 1971 | Iran Marine International | Gulf, Iran | 100,000 |
| January 1969 | Alpha Well 21 Platform A | Pacific, CA, USA | 100,000 |
| March 1970 | Main Pass Block 41 Platform C | Gulf of Mexico | 65,000 |
| October 1987 | Yum II/Zapoteca | Bahia del Campeche, Mexico | 58,643 |
| December 1970 | South Timbalier B-26 | Gulf of Mexico, USA | 53,095 |

*Based on estimate of 50,000 barrels per day for 78 days derived from Flow Rate Technical Group whose members include U.S. Geological Survey (USGS), NOAA, Bureau of Ocean Energy Management (part of DOE) and outside academics. Does not include offset for any amounts recovered.

Source: American Petroleum Institute (API), 09/18/2009; <http://www.api.org/ehs/water/spills/upload/356-Final.pdf> and updates from the Insurance Information Institute.

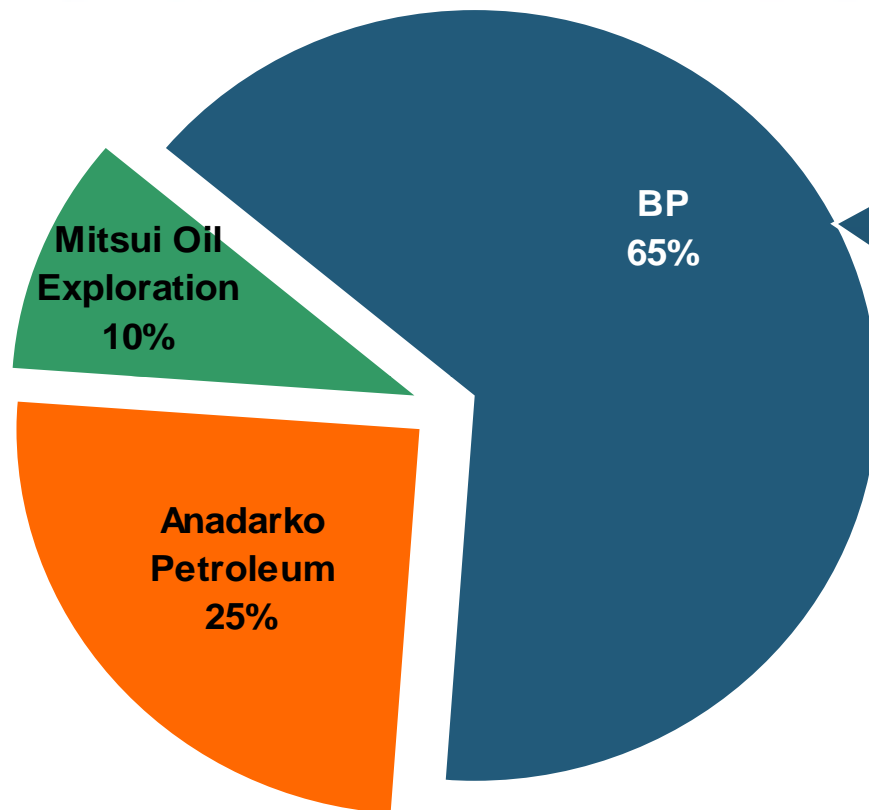
Gulf Coast Near Deepwater Horizon Site



On April 20, 2010, an explosion and fire occurred on the offshore drilling rig Deepwater Horizon, which had been drilling an exploratory well in approx. 5,000 ft of water in the Gulf of Mexico, 52 miles SE of Venice, Louisiana.

The platform subsequently sank, with 11 crewmembers presumed dead, and the uncompleted well leaking oil.

Operating Group for Deepwater Horizon: Joint Venture



The operating group for Deepwater Horizon is a joint venture led by BP.

BP has said it will assume liability for all “legitimate claims caused by the oil spill.

BP is self-insured, so large portion of losses will not hit the insurance industry.

On June 1, 2010, U.S. Attorney General said federal authorities have opened criminal and civil investigations into the spill.

As of early July, BP says that its costs have exceeded \$3 billion, including \$105 million paid on 32,000 claims. BP CEO Tony Hayward is insisting *“Other parties besides BP may be responsible for costs and liabilities arising from the oil spill, and we expect those parties to live up to their obligations.”* But Anadarko accuses BP of gross negligence.

Oil Spill Testimony by I.I.I.

Hearing on the Liability and Financial Responsibility for Oil Spills under the Oil Pollution Act of 1990 and Related Statutes

House Committee on Transportation and Infrastructure

Testimony of
Robert P. Hartwig, Ph.D., CPCU
President & Economist
Insurance Information Institute
New York, NY

June 9, 2010
Washington, DC





The Deepwater Horizon Disaster: *Insurance Market Impacts*

***Insurance Information Institute
June 28, 2010***

Download at www.iii.org/presentations

Robert P. Hartwig, Ph.D., CPCU, President & Economist
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Tel: 212.346.5520 ♦ Cell: 917.453.1885 ♦ bobh@iii.org ♦ www.iii.org

■ Insured Loss:

- The loss is a major event for the offshore energy insurance and reinsurance market
- Companies with direct exposure to the Deepwater Horizon oil rig are insured for losses totaling between \$1.4 billion and \$3.5 billion, according to initial reports
- The risks are well-syndicated, with the insured loss spread across a broad range of insurers and reinsurers on a global scale
- Since BP, which owns 65% of the Deepwater Horizon consortium self insures, a large portion of the losses **will not** hit the insurance industry.
- Lawsuits against equipment manufacturers, suppliers and sub-contractors, and business interruption claims, will likely increase total insured losses.
- BP said it will assume liability for all legitimate claims caused by the oil spill. Primary liability for clean up costs will be with BP consortium.

Insured Implications of the Deepwater Horizon Oil Spill in the Gulf

- **Direct Insurance Payouts from Insured Deepwater Parties**
- **Other Indemnification Processes**
 - ◆ BP claims process
 - ◆ \$20B Feinberg-administered fund
 - ◆ Litigation
- **Coverage Issues**
 - ◆ Oil contaminated water from flood/storm surge
 - ◆ Wind-blown oil
 - ◆ Business Interruption
- **Price and Availability of Coverage for Offshore Operators**
- **Hostile Regulatory Environment for Offshore Oil & Gas Concerns**
 - ◆ Revisions to Oil Pollution Act of 1990
 - ◆ Increased financial responsibility requirements
 - ◆ Impacts demand for energy insurance products and ancillary services/coverages
- **Carryover to Onshore Oil & Gas Operators and Utilities**
- **Politicization of the Issue**
- **Impact on Carbon Legislation**

Insured Implications of the Deepwater Horizon Oil Spill in the Gulf

- Coverage Questions
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Insurance Information Institute Online:

www.iii.org

***Thank you for your time
and your attention!***

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