



Is the World Becoming a Riskier Place?

P/C Insurance Industry in the Age of Uncertainty

Insurance Council of Texas Annual Symposium
Austin, TX
July 15, 2011

Download at www.iii.org/presentations

Robert P. Hartwig, Ph.D., CPCU, President & Economist

Insurance Information Institute ♦ 110 William Street ♦ New York, NY 10038

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

Presentation Outline

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

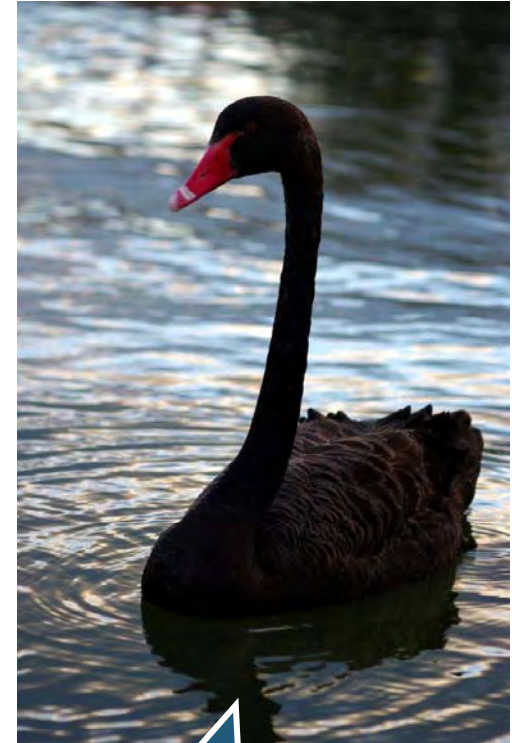
What in the World Is Going On?

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

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

Uncertainty, Risk and Fear Abound

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

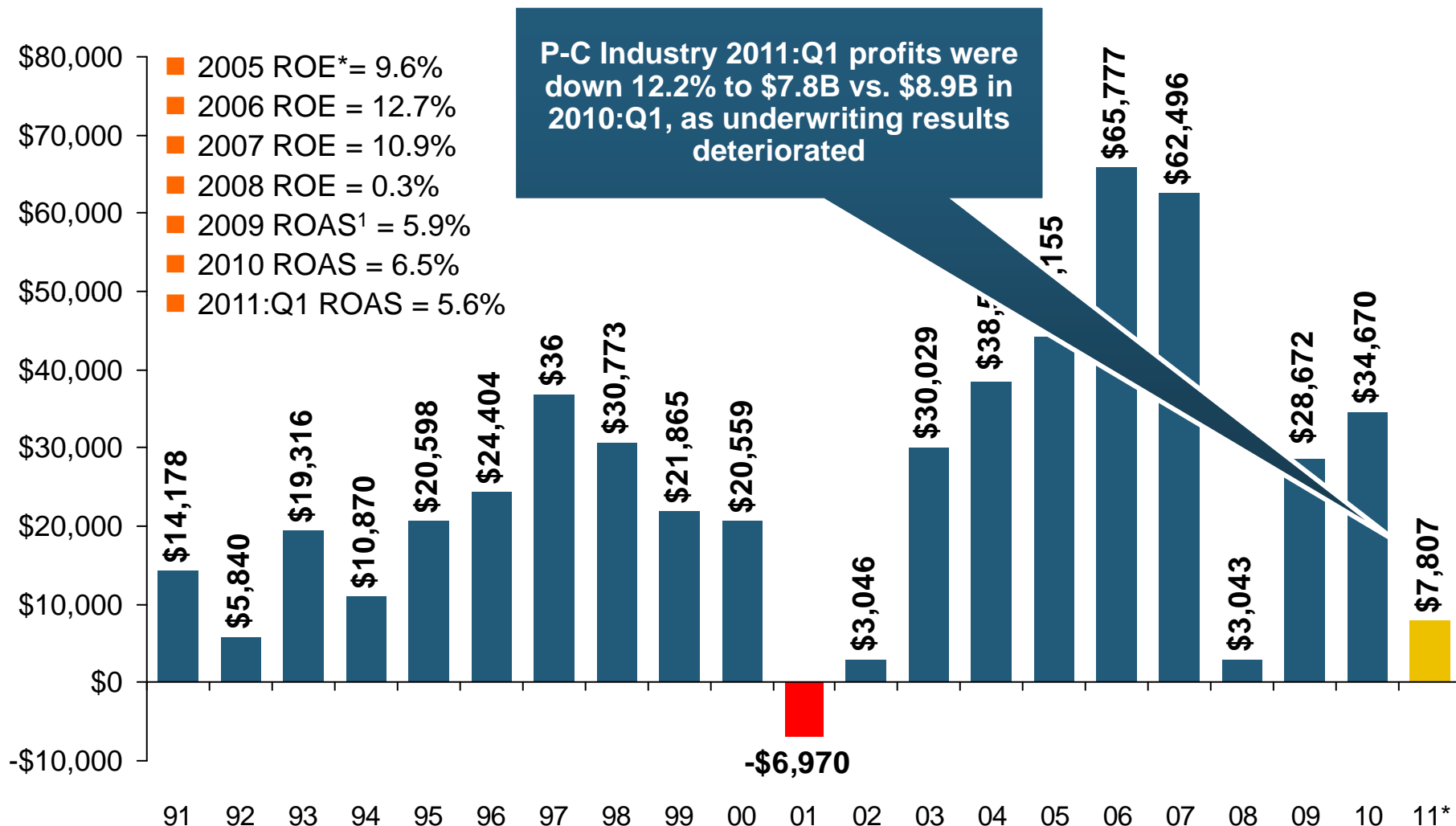


Are “Black Swans”
everywhere or
does it just seem
that way?

P/C Insurance Industry Financial Overview

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

P/C Net Income After Taxes 1991–2011:Q1 (\$ Millions)

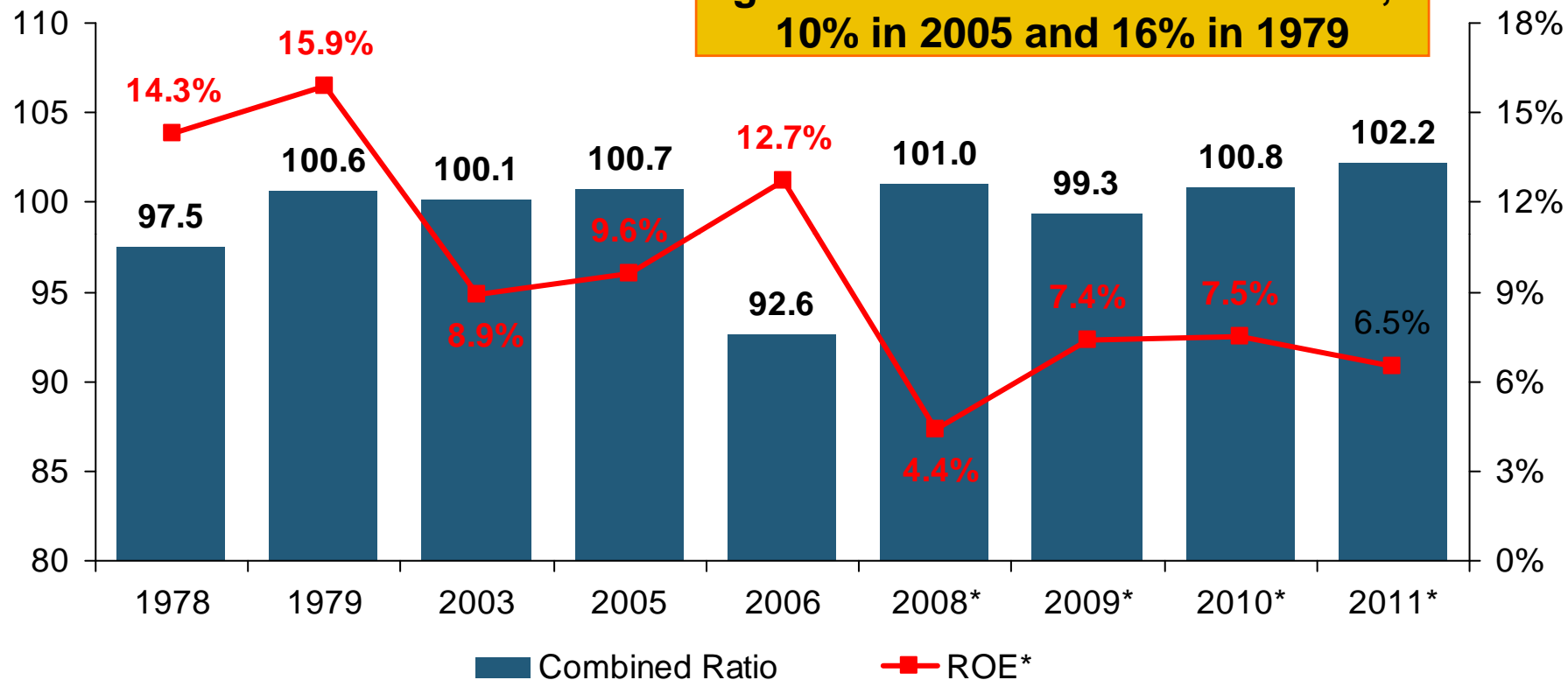


* ROE figures are GAAP; ¹Return on avg. surplus. Excluding Mortgage & Financial Guaranty insurers yields a 6.5% ROAS for 2011:Q1, 7.5% for 2010 and 7.4% for 2009.

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

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

Combined Ratio / ROE

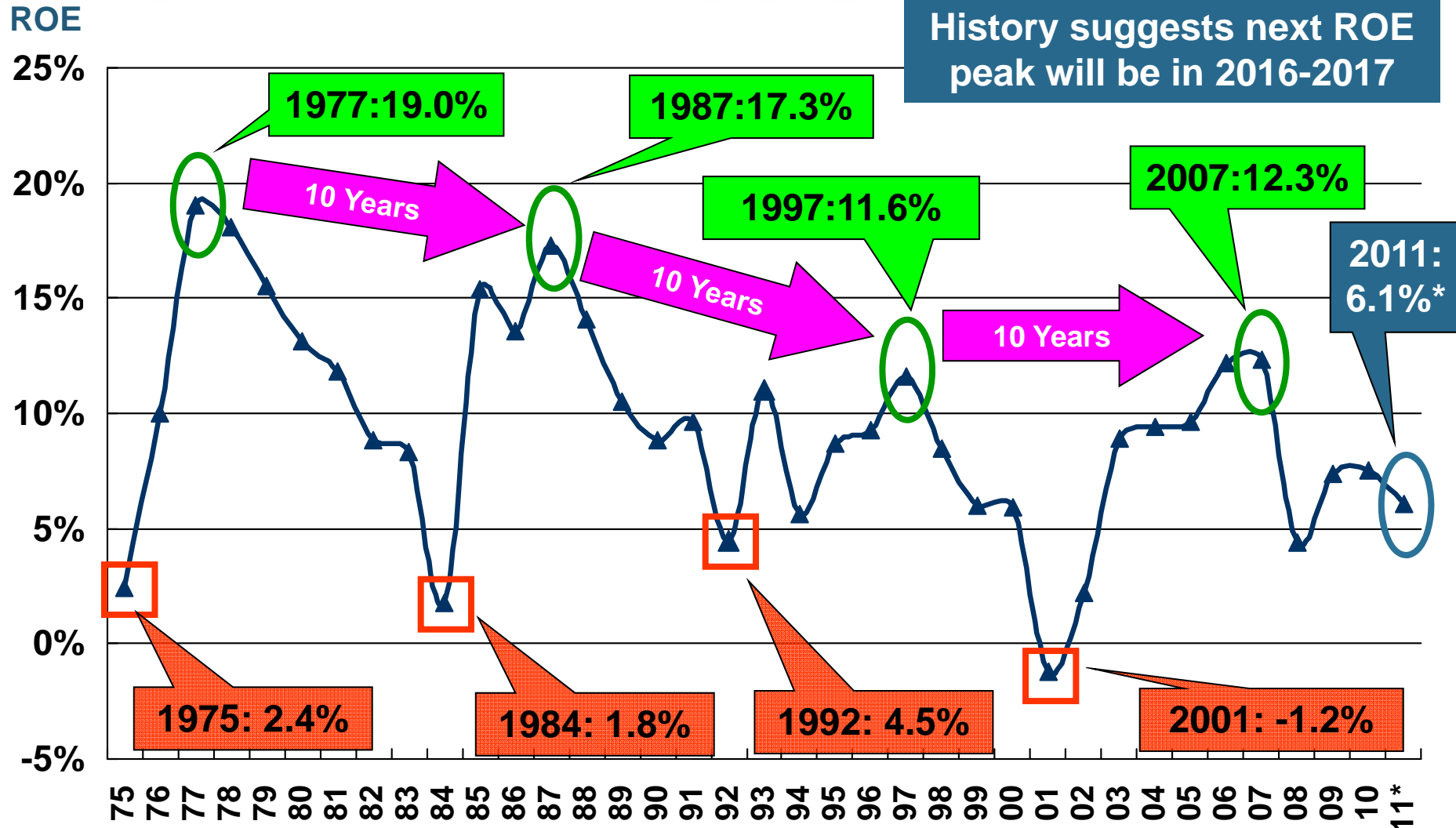


Combined Ratios Must Be Lower in Today's Depressed Investment Environment to Generate Risk Appropriate ROEs

* 2009 and 2010 figures are return on average statutory surplus. 2008 -2011 figures exclude mortgage and financial guaranty insurers

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

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



*Profitability = P/C insurer ROEs are I.I.I. estimates. 2011 figure is an estimate based on annualized ROAS for Q1 data.

Note: Data for 2008-2011 exclude mortgage and financial guaranty insurers.

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

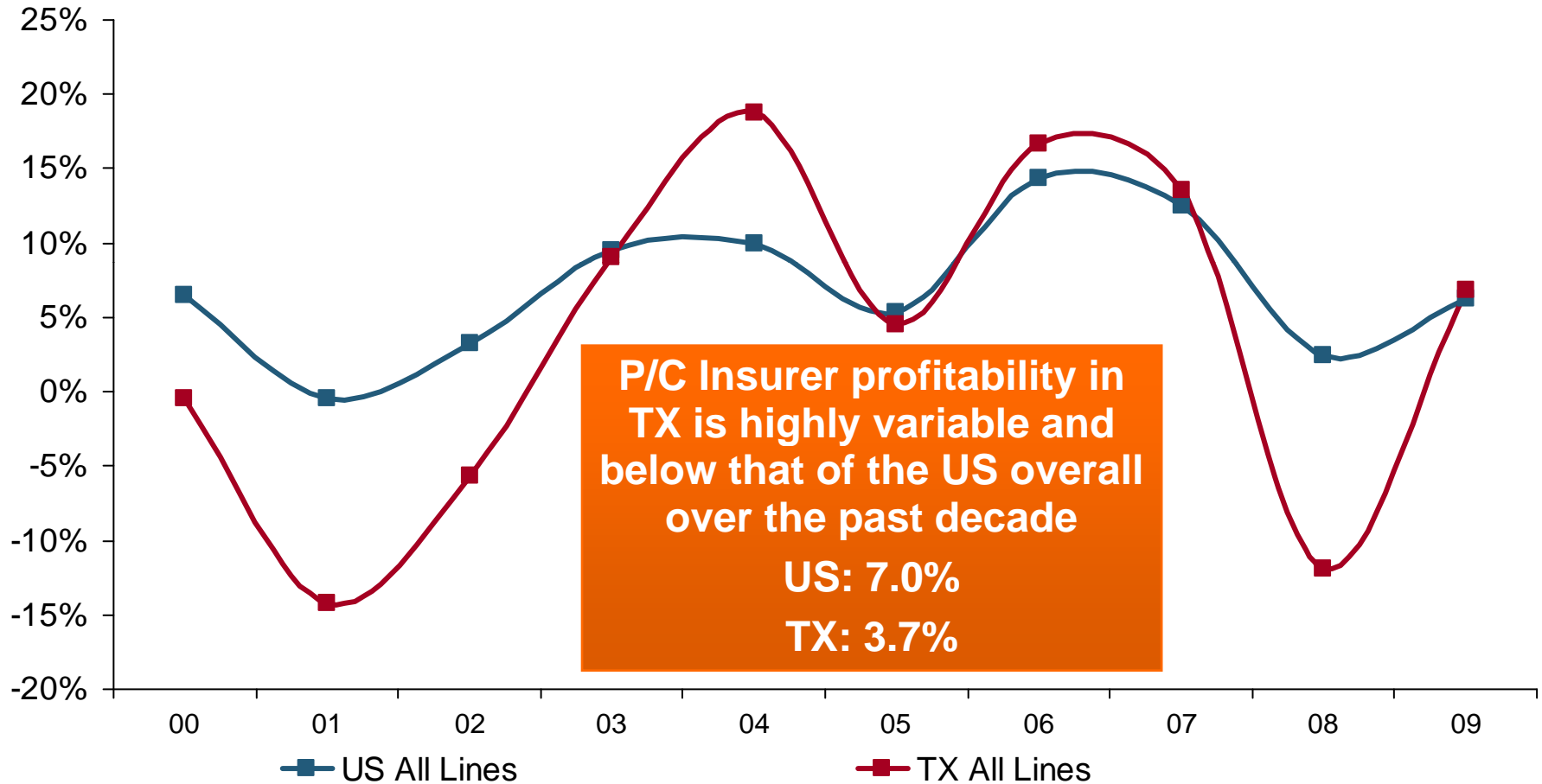


Profitability and Growth in Texas P/C Insurance Markets

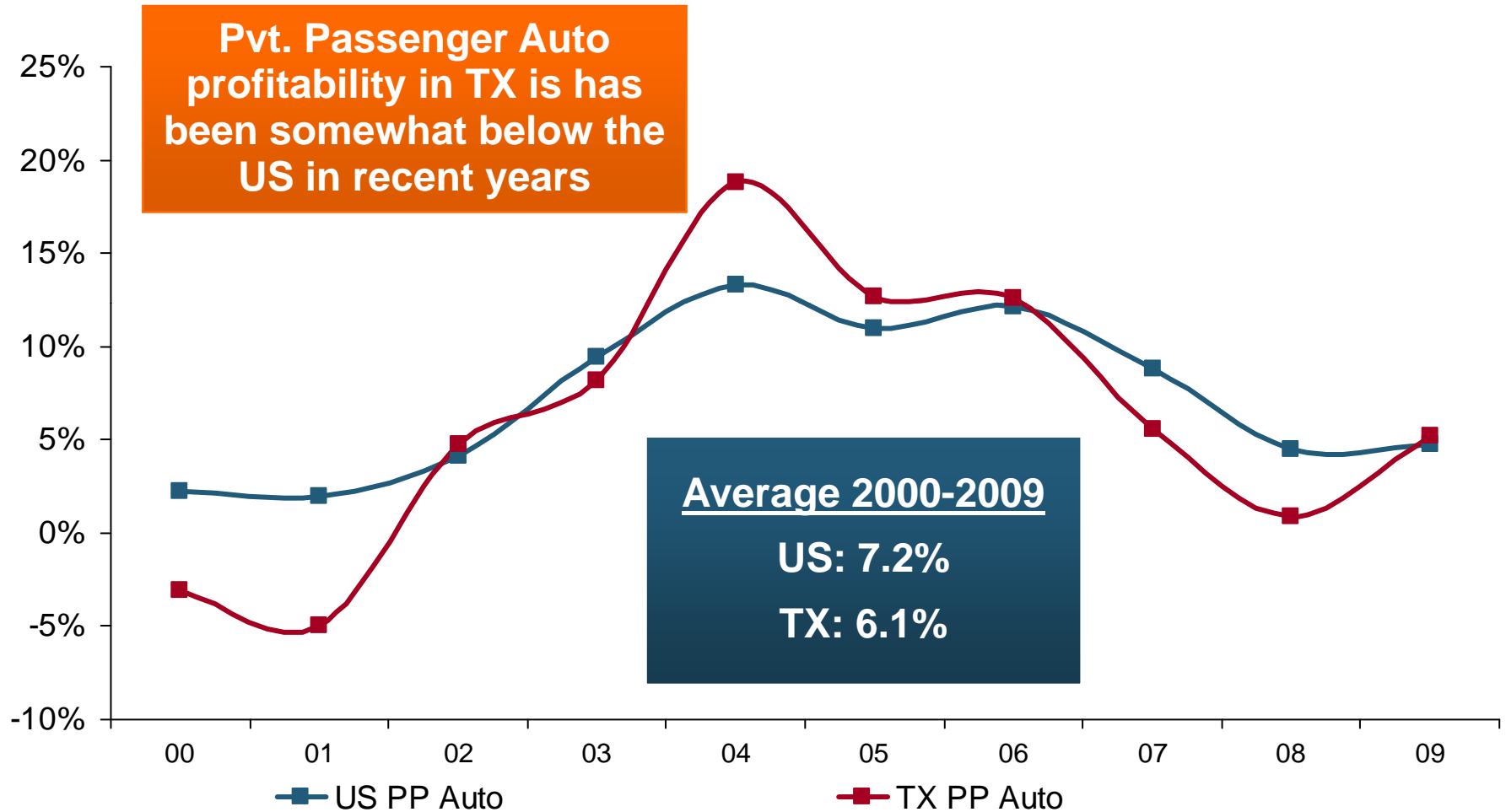
Analysis by Line and Nearby State Comparisons

RNW All Lines: TX vs. U.S., 2000-2009

(Percent)

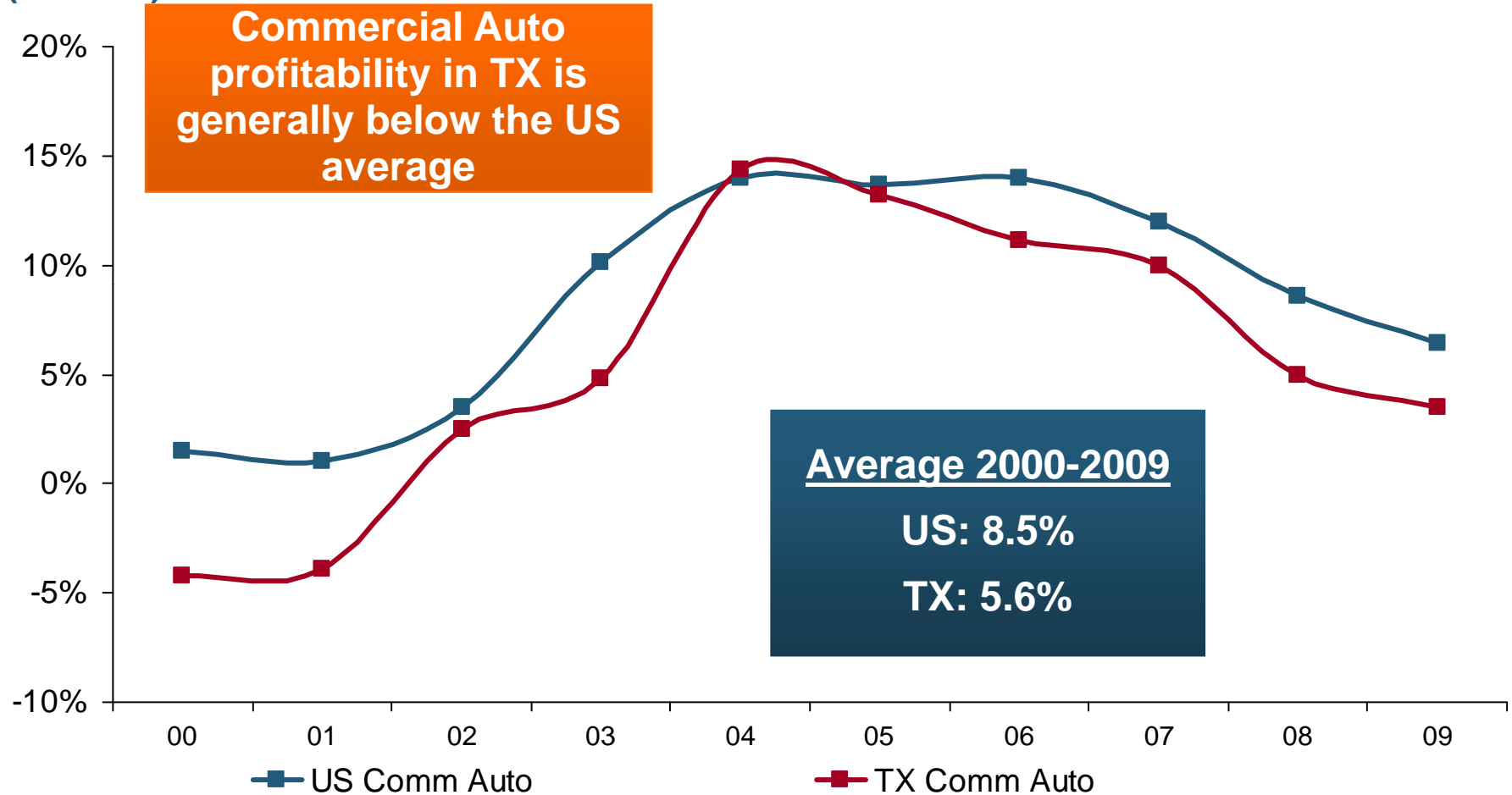


RNW PP Auto: TX vs. U.S., 2000-2009



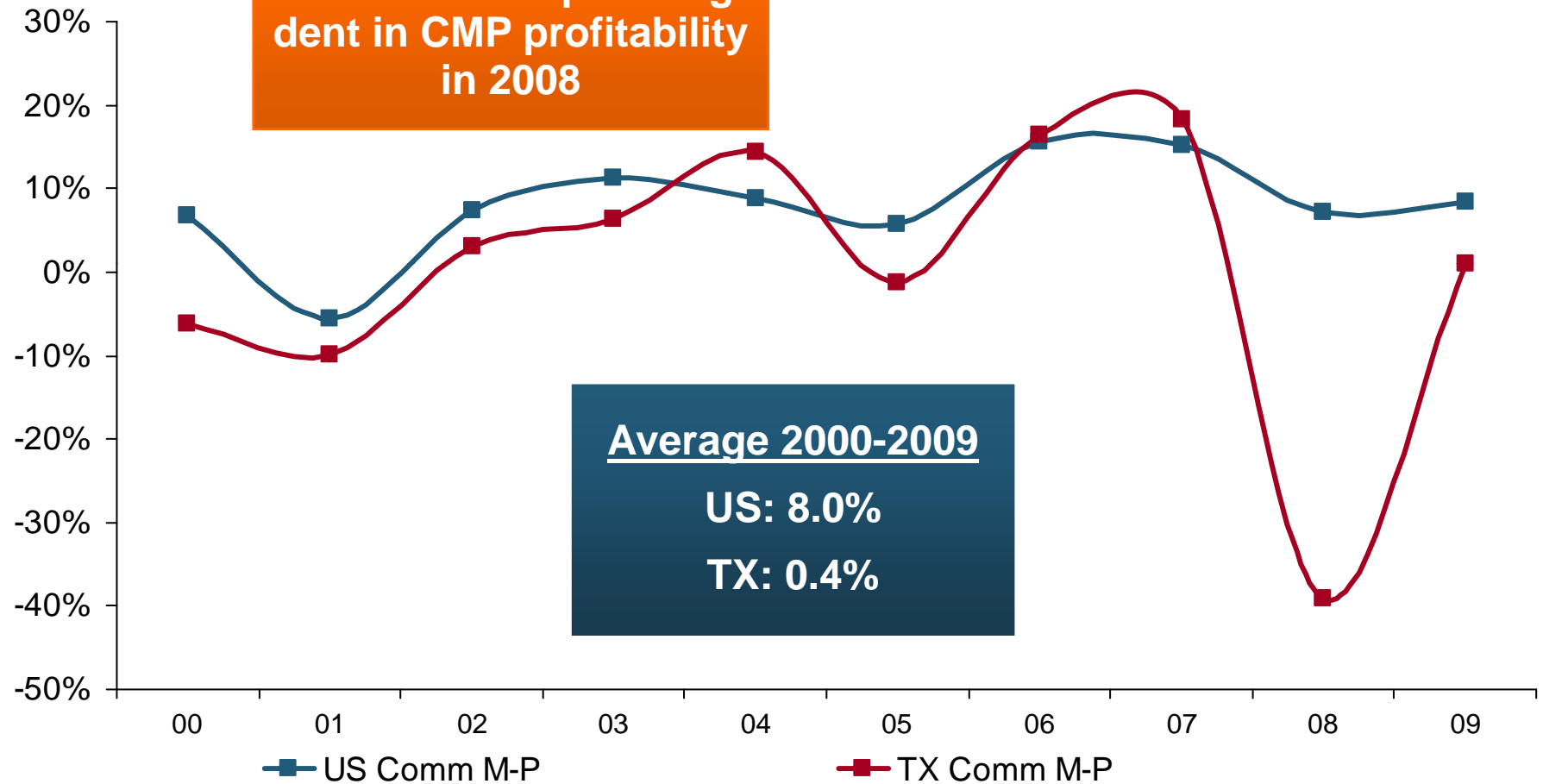
RNW Comm. Auto: TX vs. U.S., 2000-2009

(Percent)



RNW Comm. Multi-Peril: TX vs. U.S., 2000-2009

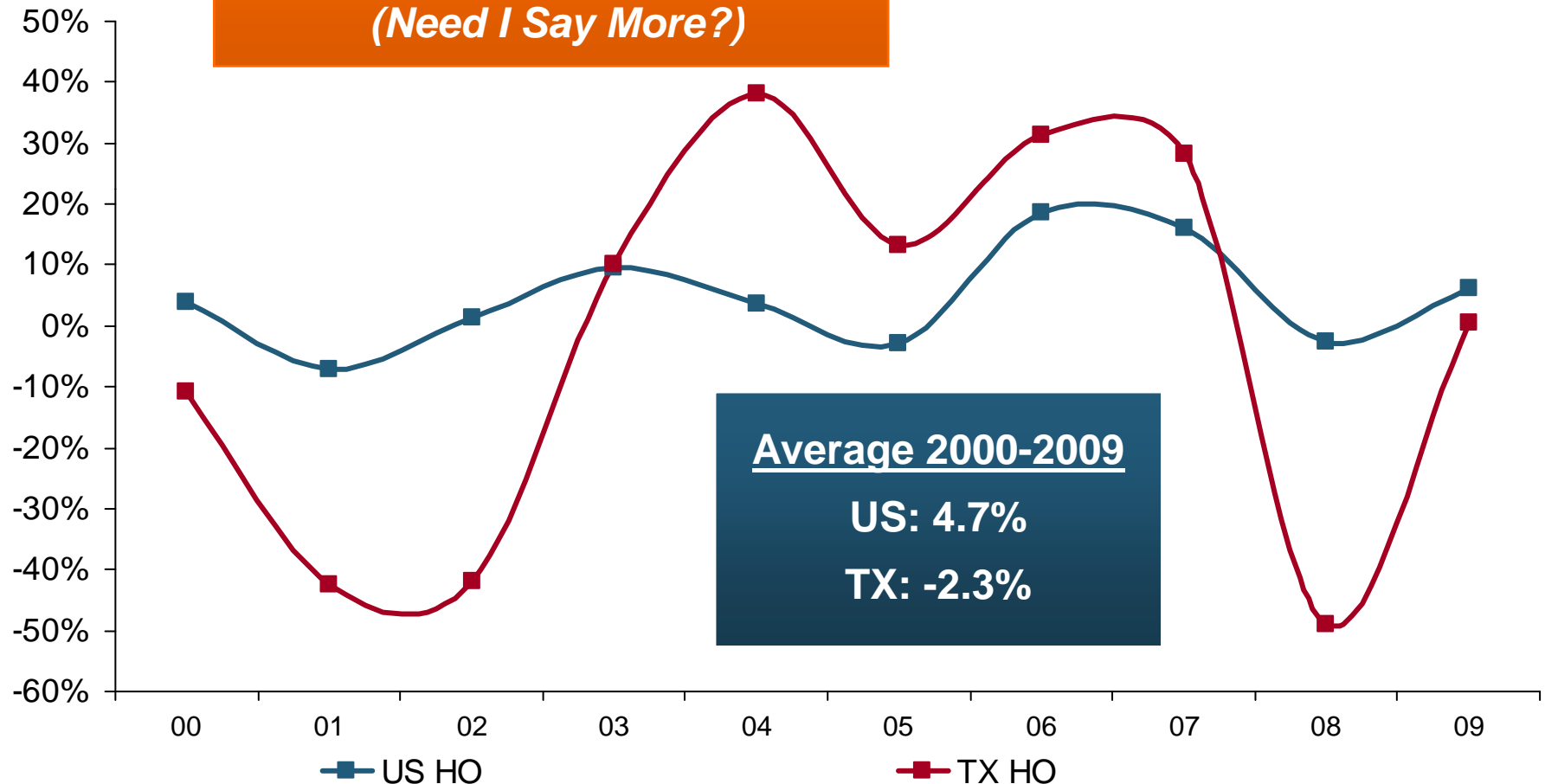
(Percent)



RNW Homeowners: TX vs. U.S., 2000-2009

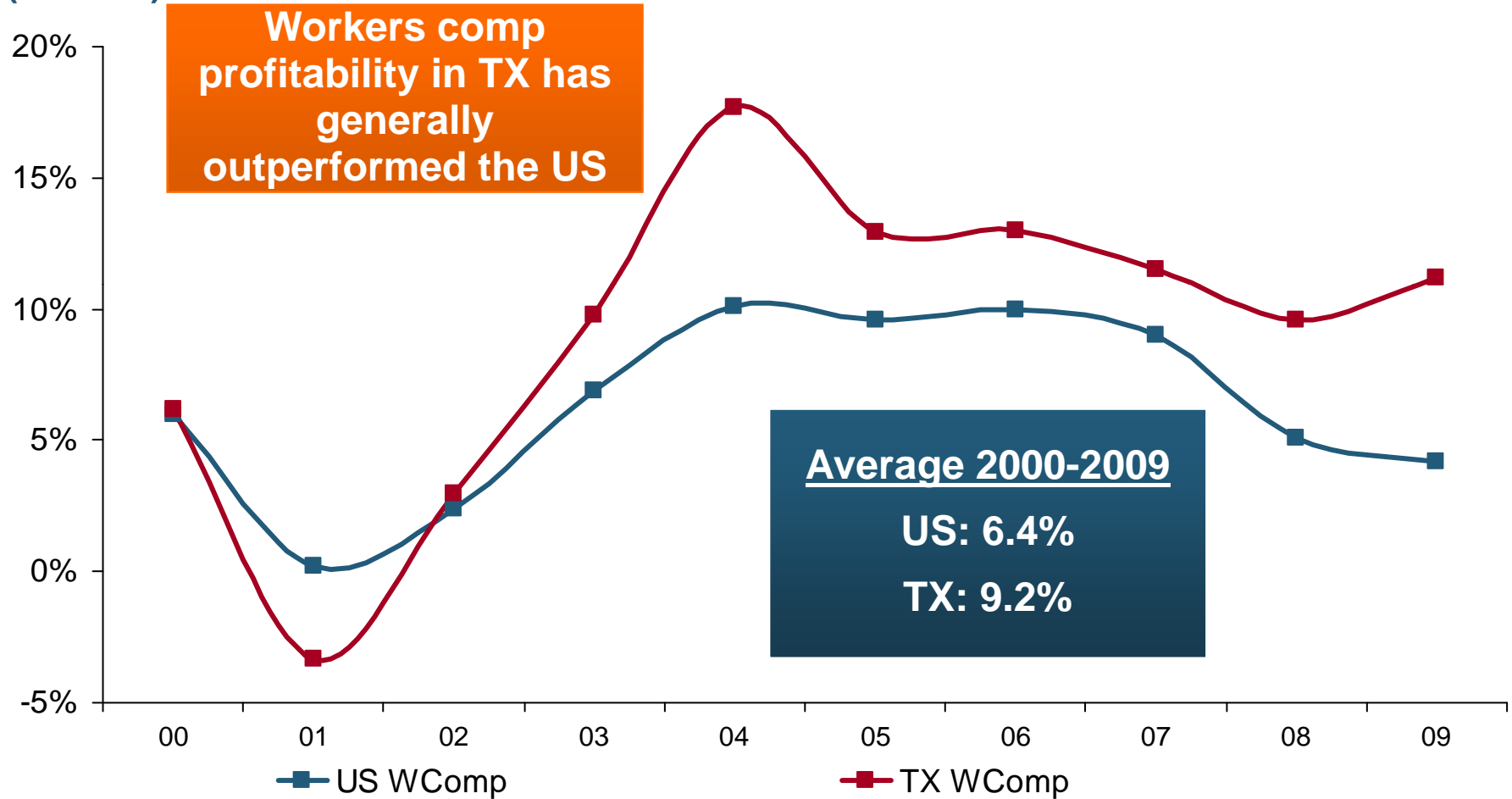
(Percent)

Homeowners Profitability: Mold,
Hurricanes, Hail & Tornadoes
(Need I Say More?)

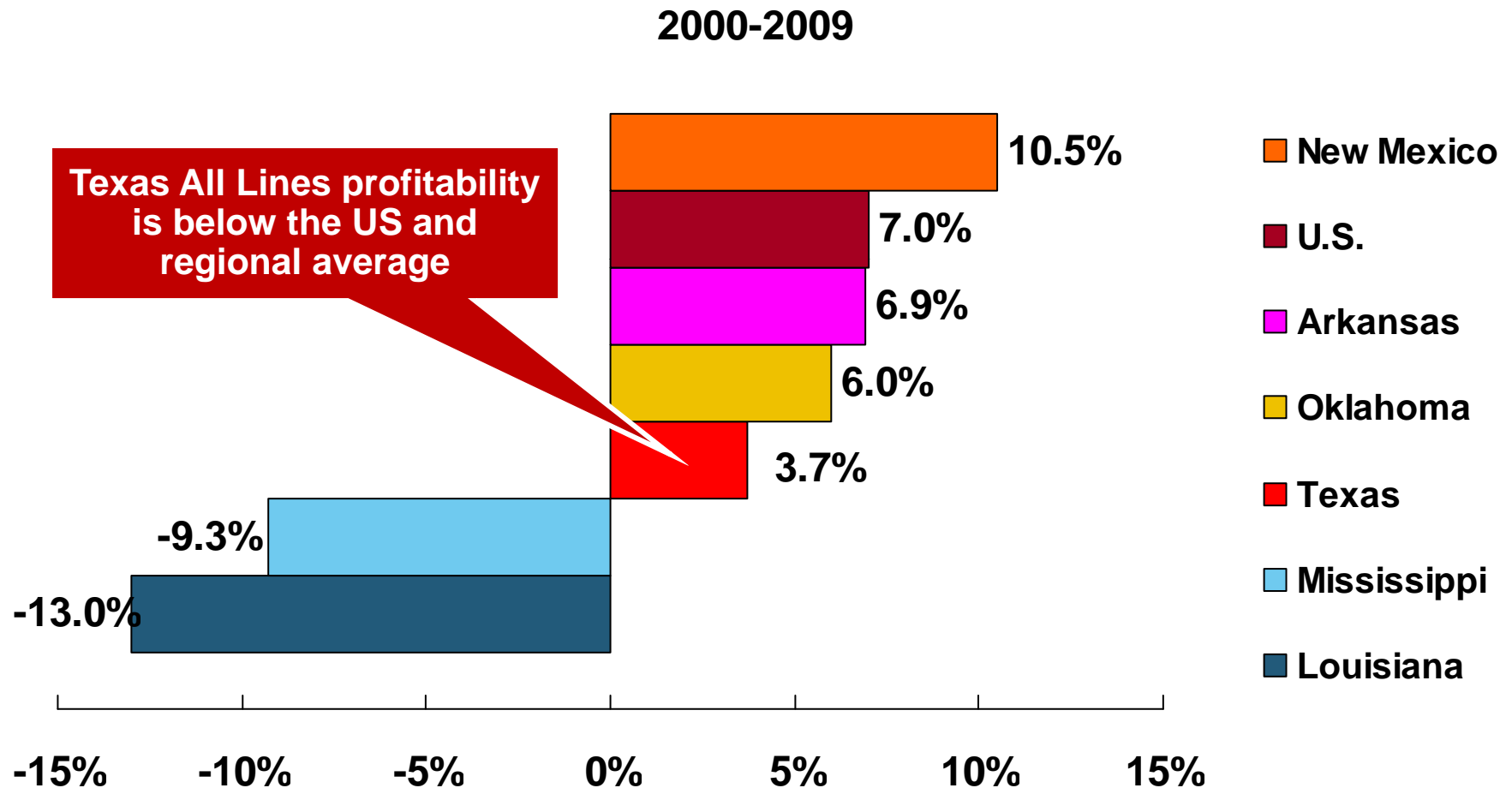


RNW Workers Comp: TX vs. U.S., 2000-2009

(Percent)



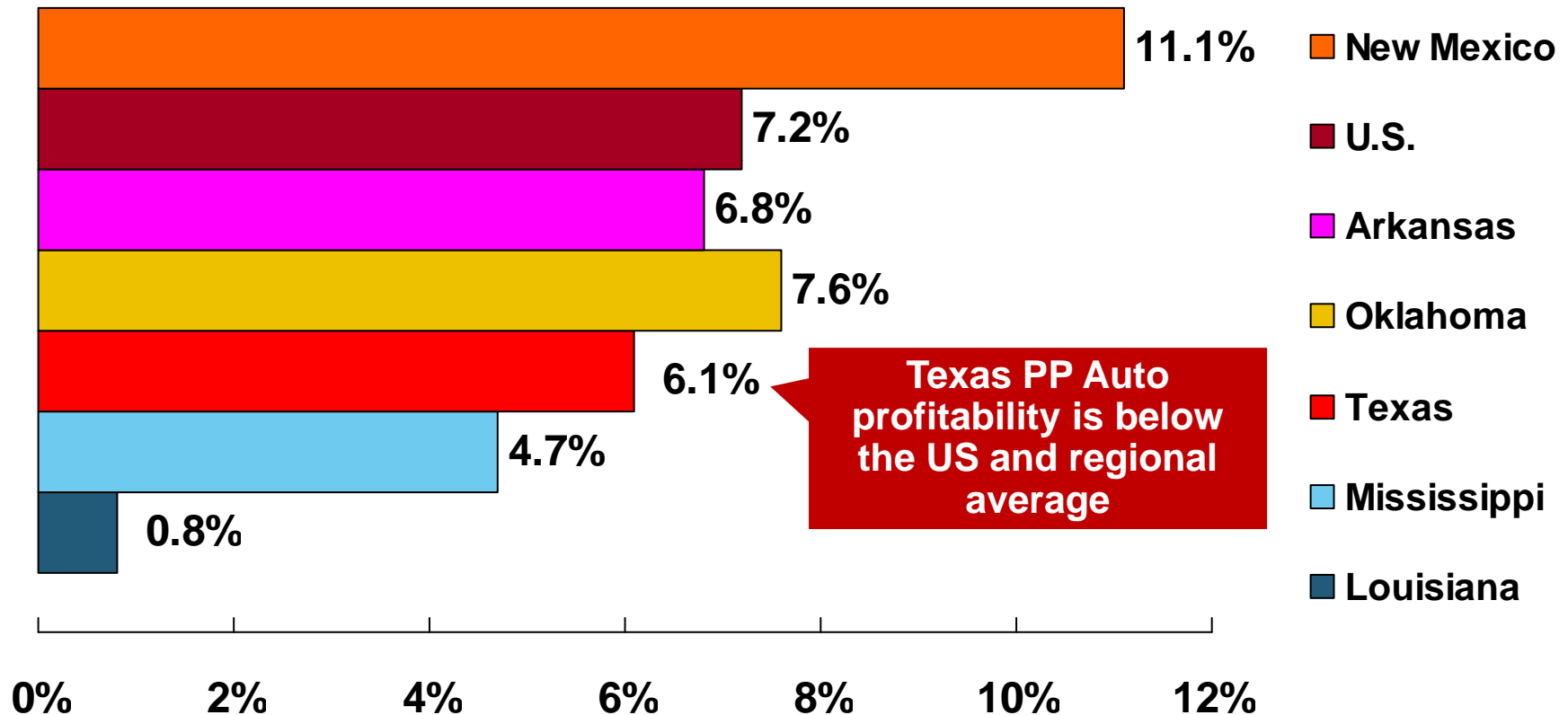
All Lines: 10-Year Average RNW TX & Nearby States



Source: NAIC, Insurance Information Institute

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

2000-2009



Source: NAIC, Insurance Information Institute

Top Ten Most Expensive And Least Expensive States For Automobile Insurance, 2008 (1)

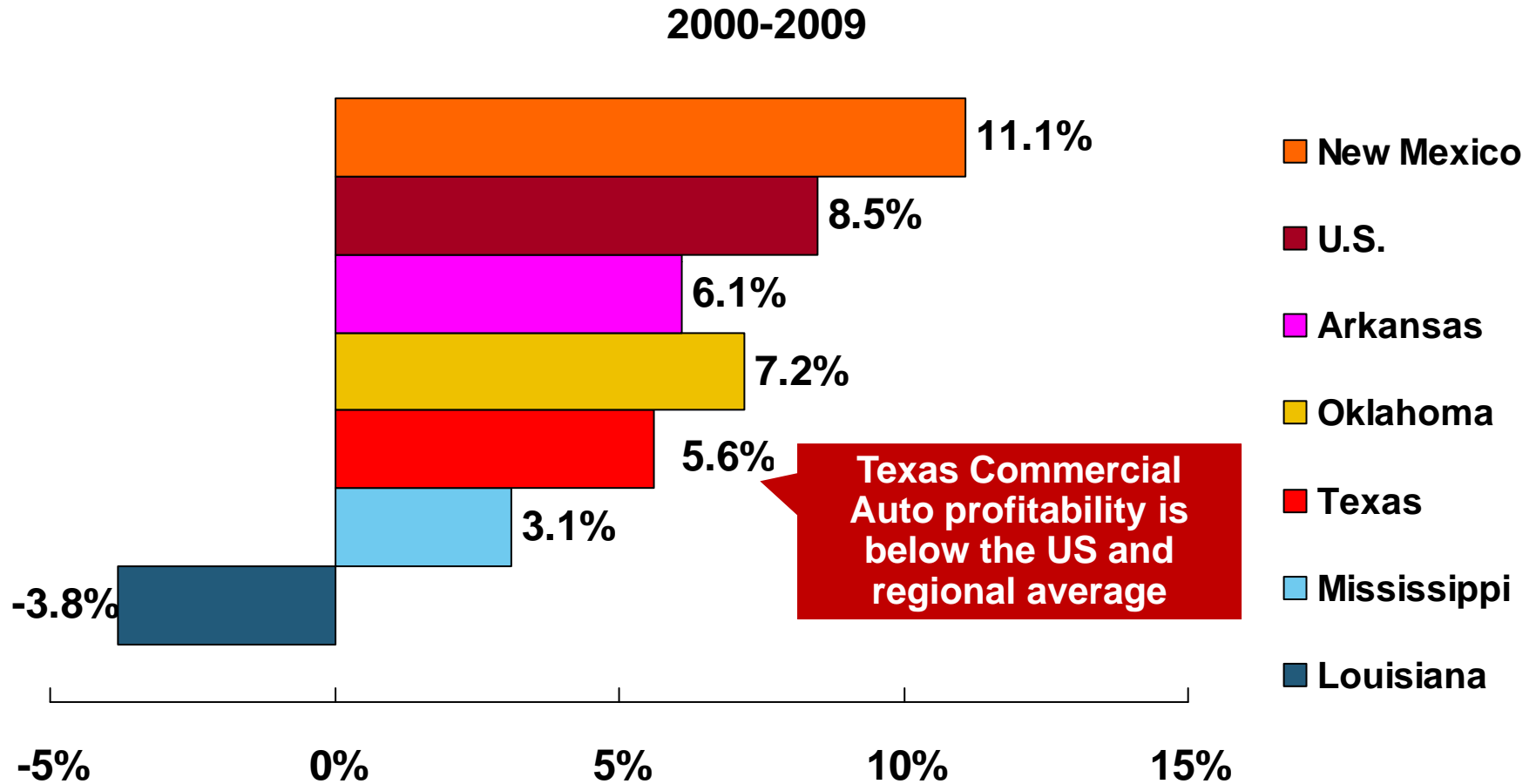
Rank	Most expensive states	Average expenditure	Rank	Least expensive states	Average expenditure
1	D.C.	\$1,126	1	North Dakota	\$503
2	Louisiana	1,105	2	Iowa	519
3	New Jersey	1,081	3	South Dakota	520
4	Florida	1,055	4	Nebraska	547
5	New York	1,044	5	Idaho	562
6	Delaware	1,007	6	Kansas	576
7	Rhode Island	986	7	Wisconsin	581
8	Nevada	970	8	North Carolina	595
9	Connecticut	950	9	Maine	600
10	Maryland	922	10	Indiana	612

Texas ranked 15th in 2008, with an average expenditure for auto insurance of \$854.

(1) Based on average automobile insurance expenditures.

Source: © 2010 National Association of Insurance Commissioners.

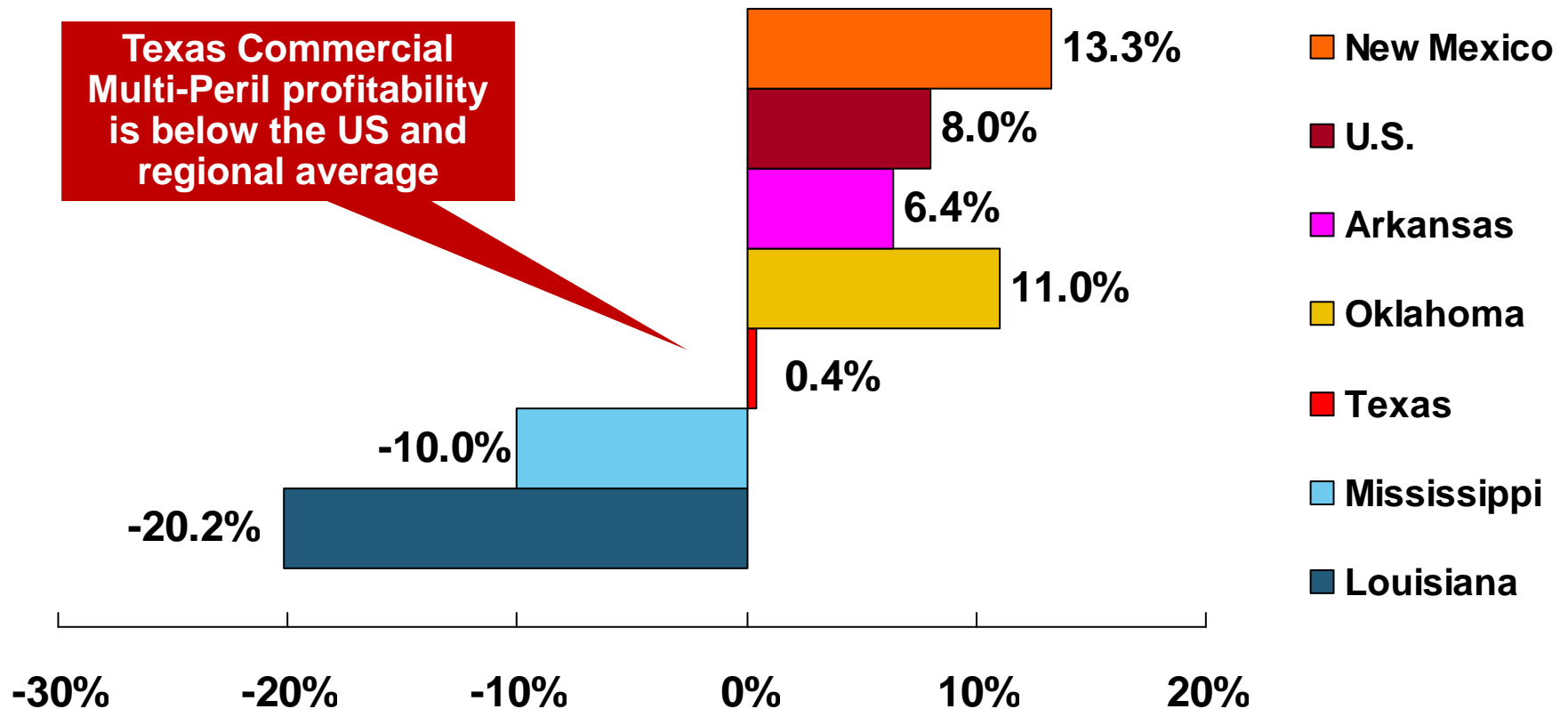
Comm. Auto: 10-Year Average RNW TX & Nearby States



Source: NAIC, Insurance Information Institute

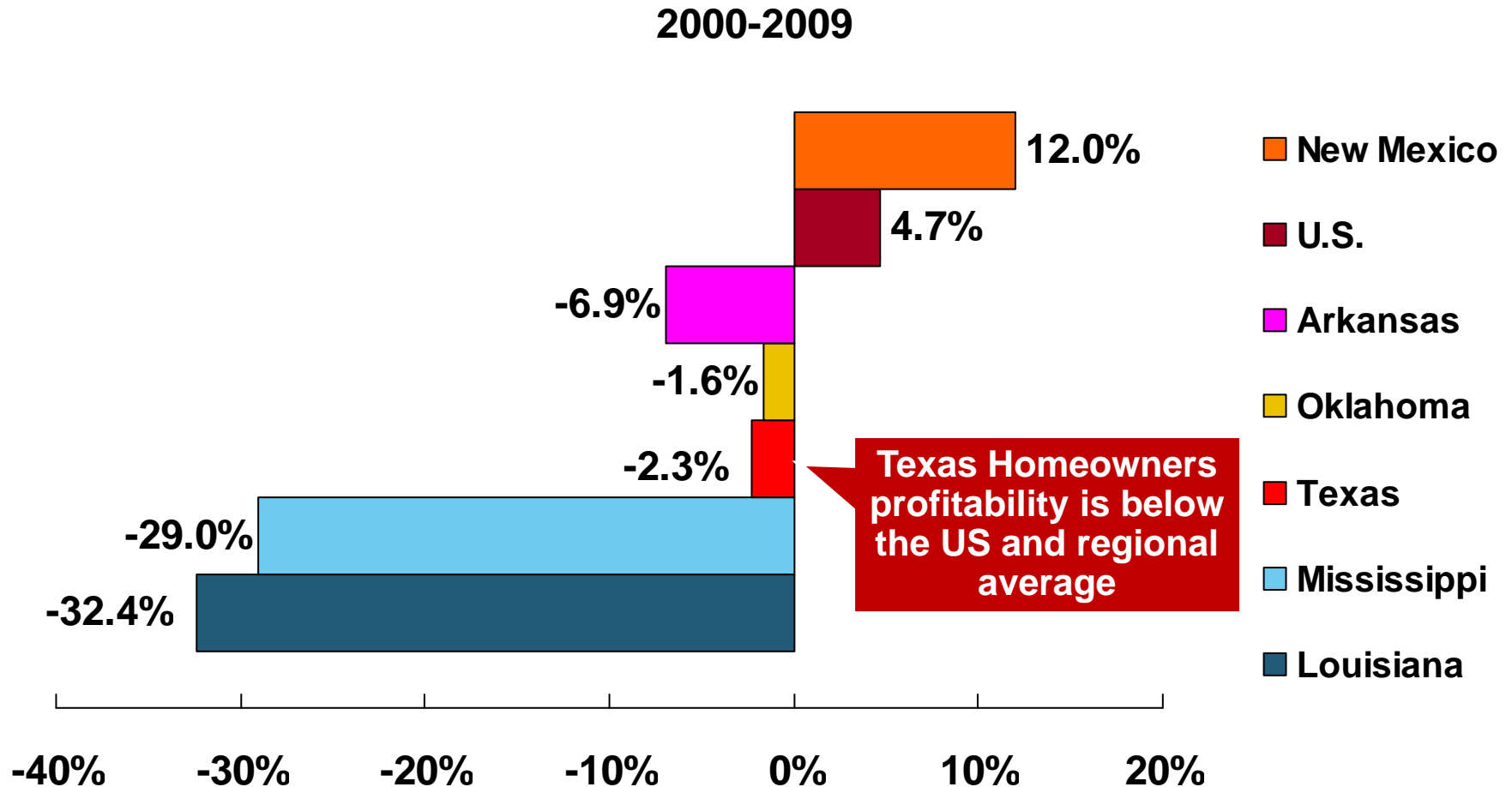
Comm. M-P: 10-Year Average RNW TX & Nearby States

2000-2009



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, 2008 (1)

Texas ranked as the most expensive state for homeowners insurance in 2008, with an average expenditure of \$1,460.

Rank	Most expensive states	Average expenditure	Rank	Least expensive states	Average expenditure
1	Texas (3)	\$1,460	1	Idaho	\$387
2	Florida (4)	1,390	2	Utah	432
3	Louisiana	1,155	3	Oregon	439
4	Oklahoma	1,048	4	Washington	471
5	Massachusetts	1,026	5	Wisconsin	503
6	New York	983	6	Delaware	535
7	Connecticut	980	7	Ohio	565
8	Mississippi	980	8	Maine	572
9	D.C.	926	9	Pennsylvania	586
10	Kansas	916	10	Kentucky	601

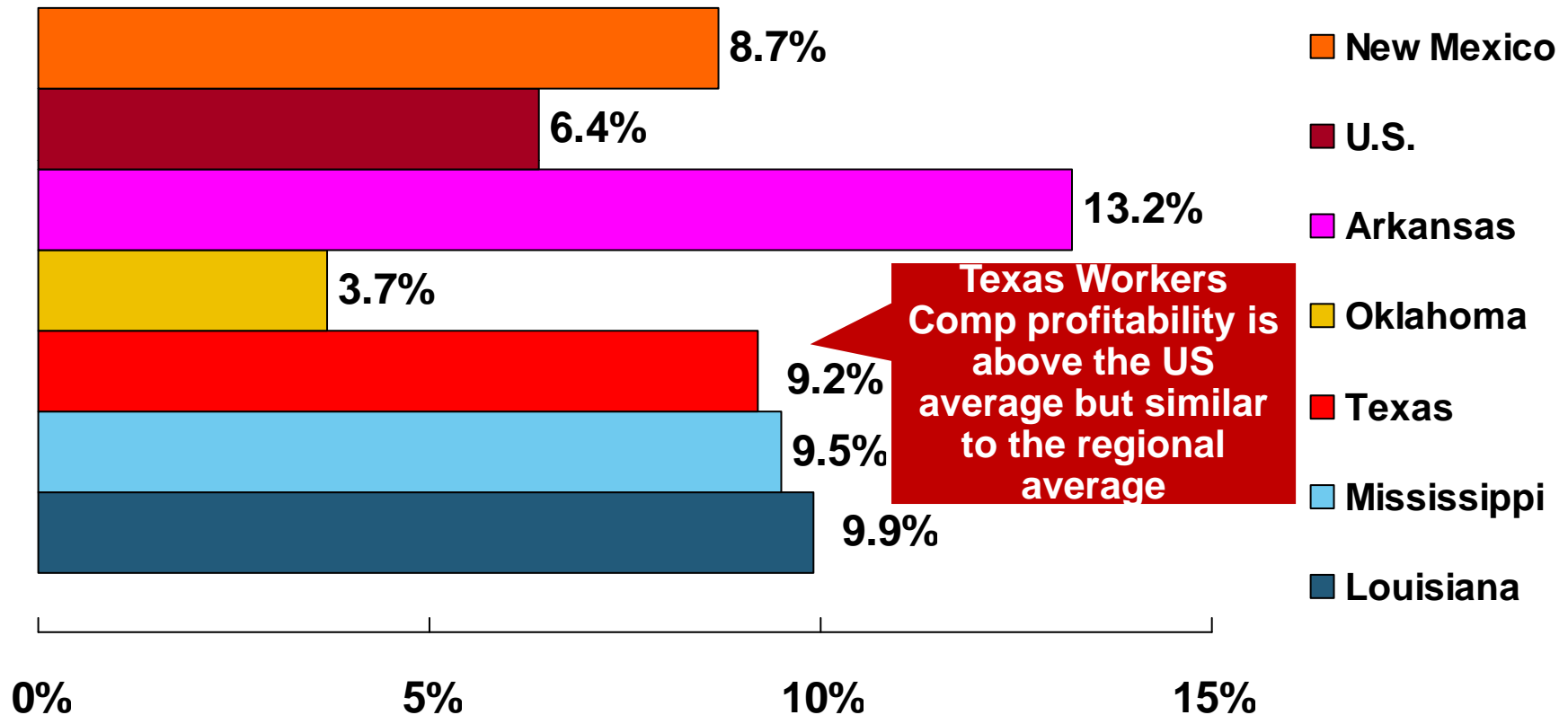
- (1) States with the same premium receive the same rank.
- (2) Based on the HO-3 homeowner package policy for owner-occupied dwellings, 1 to 4 family units. Provides "all risks" coverage (except those specifically excluded in the policy) on buildings and broad named-peril coverage on personal property, and is the most common package written.
- (3) The Texas Department of Insurance developed home insurance policy forms that are similar but not identical to the standard forms.
- (4) 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.

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: © 2010 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

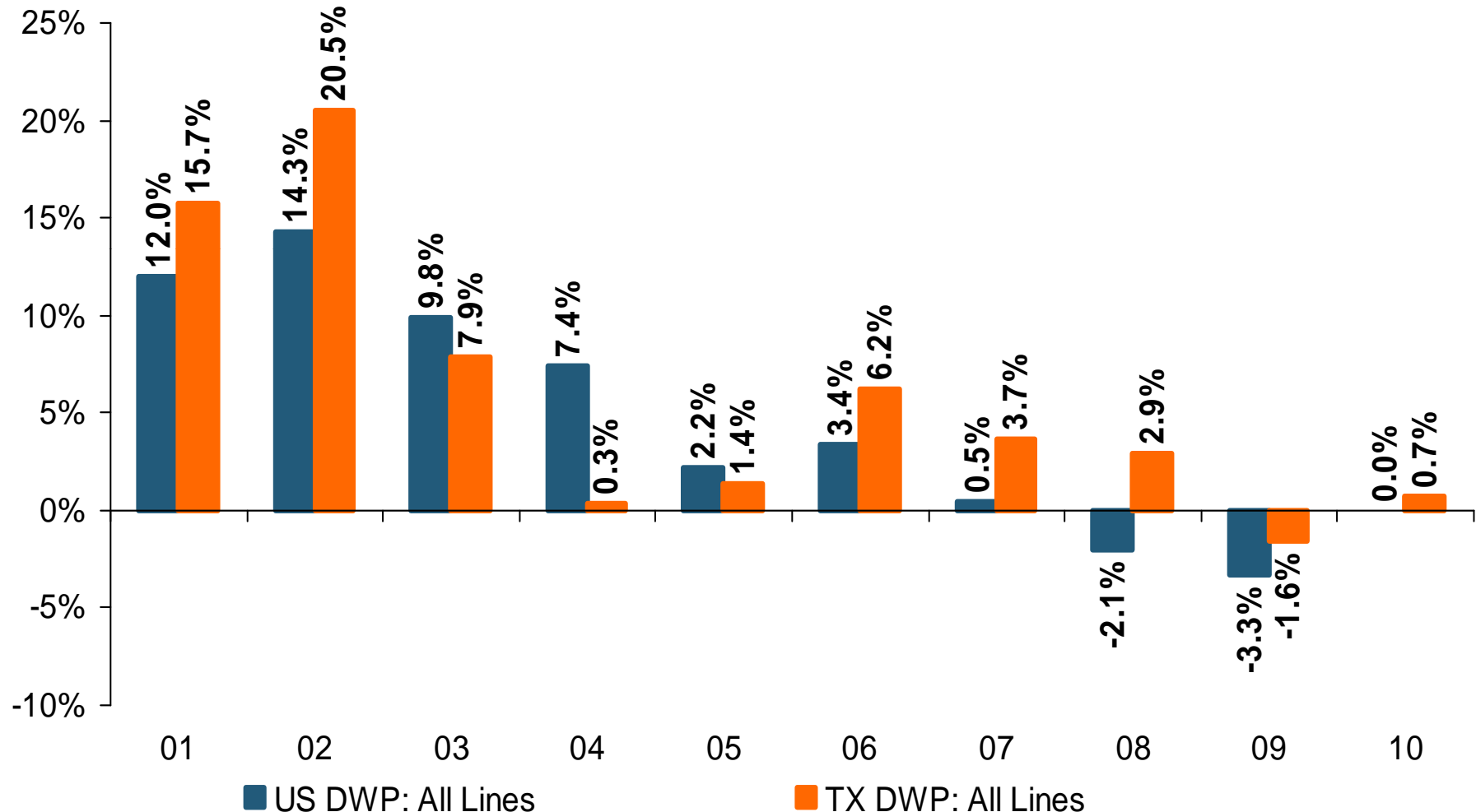
2000-2010



Source: NAIC, Insurance Information Institute

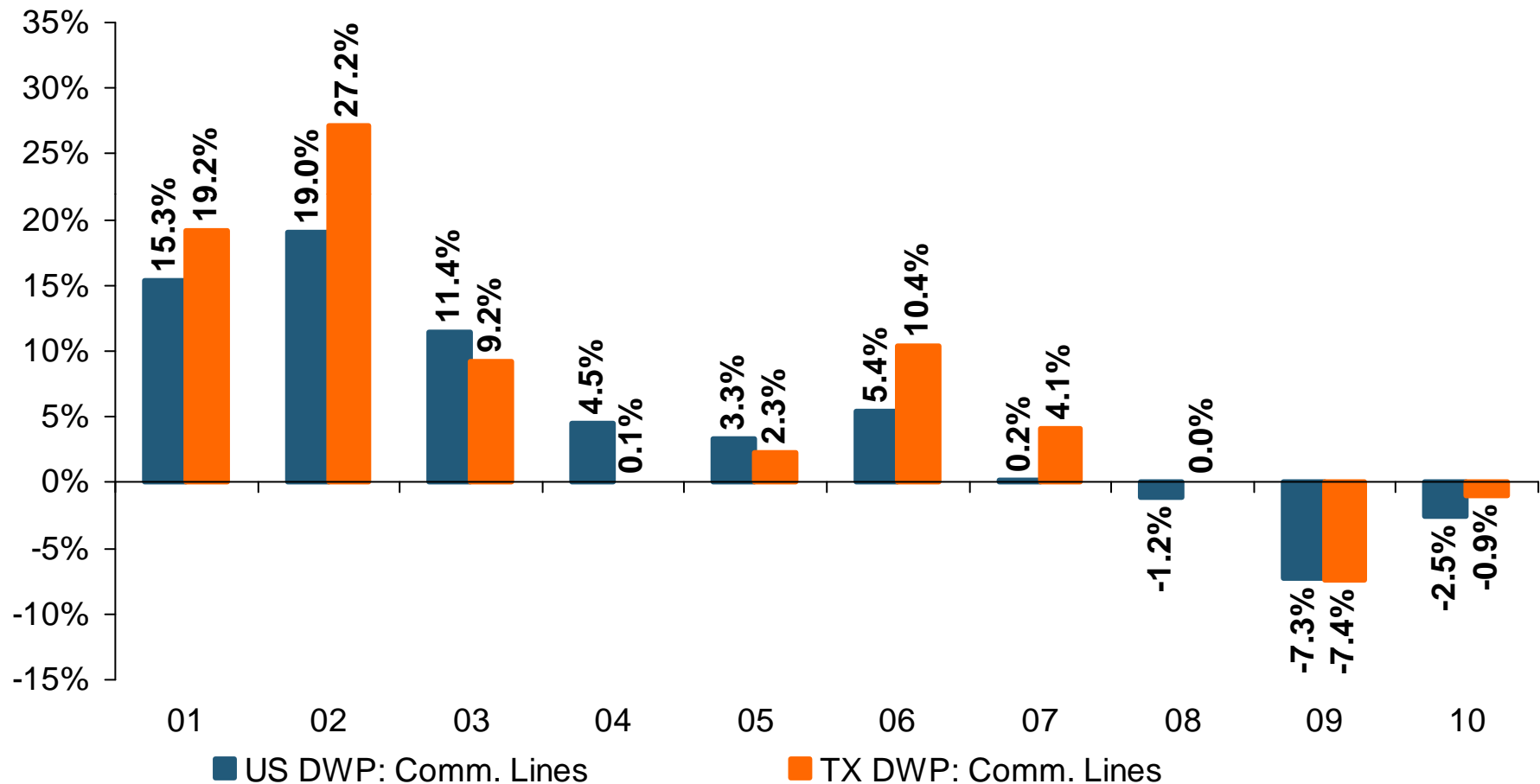
All Lines DWP Growth: TX vs. U.S., 2001-2010

(Percent)



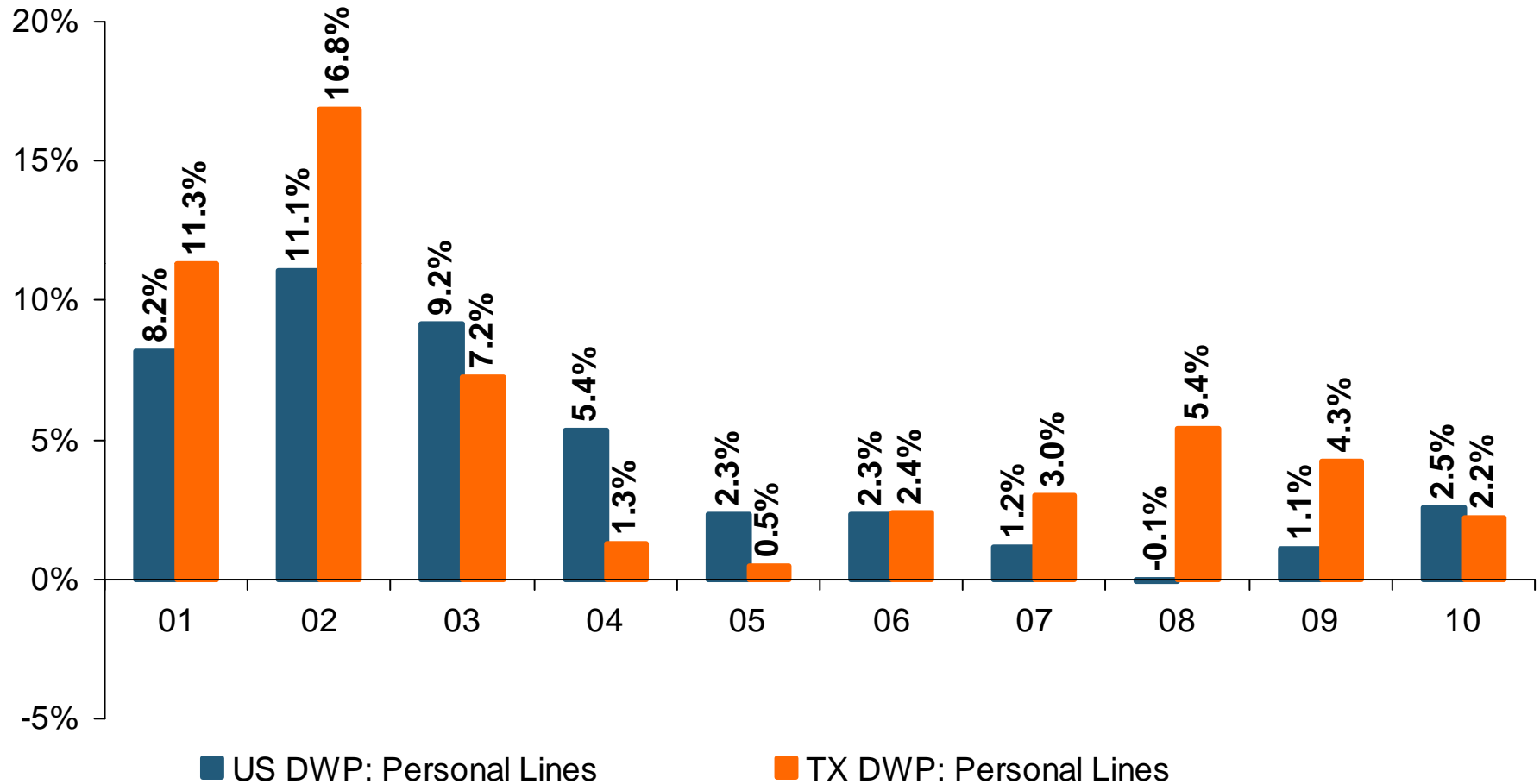
Comm. Lines DWP Growth: TX vs. U.S., 2001-2010

(Percent)



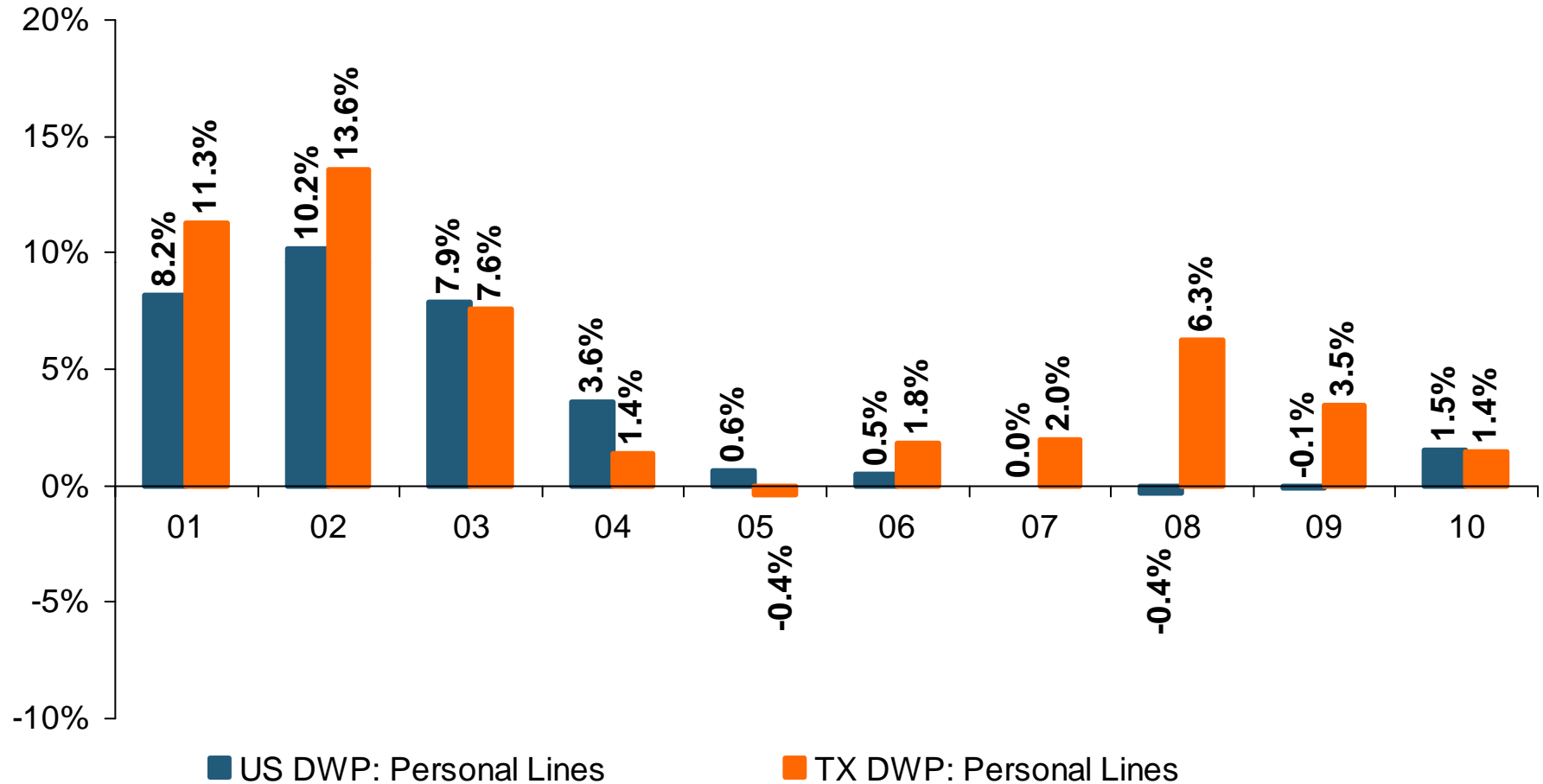
Personal Lines DWP Growth: TX vs. U.S., 2001-2010

(Percent)



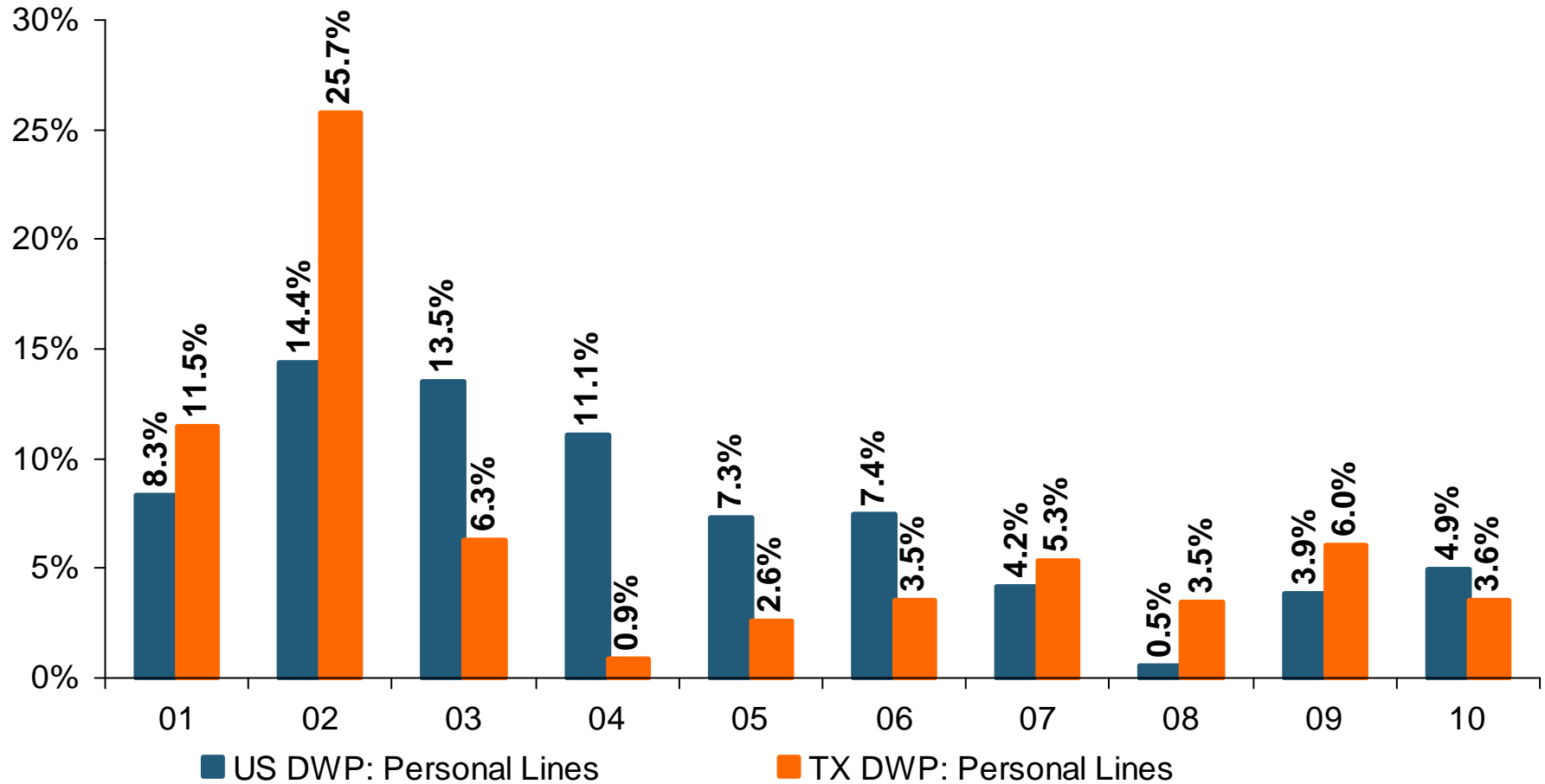
Private Passenger Auto DWP Growth: TX vs. U.S., 2001-2010

(Percent)



Homeowner's MP DWP Growth: TX vs. U.S., 2001-2010

(Percent)



Catastrophe Loss Developments and Trends

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

Global Catastrophe Loss Summary: First Half 2011

■ 2011 Is Already (as of June 30) the *Highest* Loss Year on Record Globally

- ◆ Extraordinary accumulation of severe natural catastrophe: Earthquakes, tsunami, floods and tornadoes are the primary causes of loss

■ \$260 Billion in *Economic* Losses Globally

- ◆ New record for the first six months, exceeding the previous record of \$220B in 2005
- ◆ Economy is more resilient than most pundits presume

■ \$55 Billion in *Insured* Losses Globally

- ◆ More than double the first half 2010 amount
- ◆ Over 4 times the 10-year average

■ \$27 Billion in *Economic* Losses in the US

- ◆ Represents a 129% increase over the \$11.8 billion amount through the first half of 2010

■ \$17.3 Billion in *Insured* Losses in the US Arising from 100 CAT Events

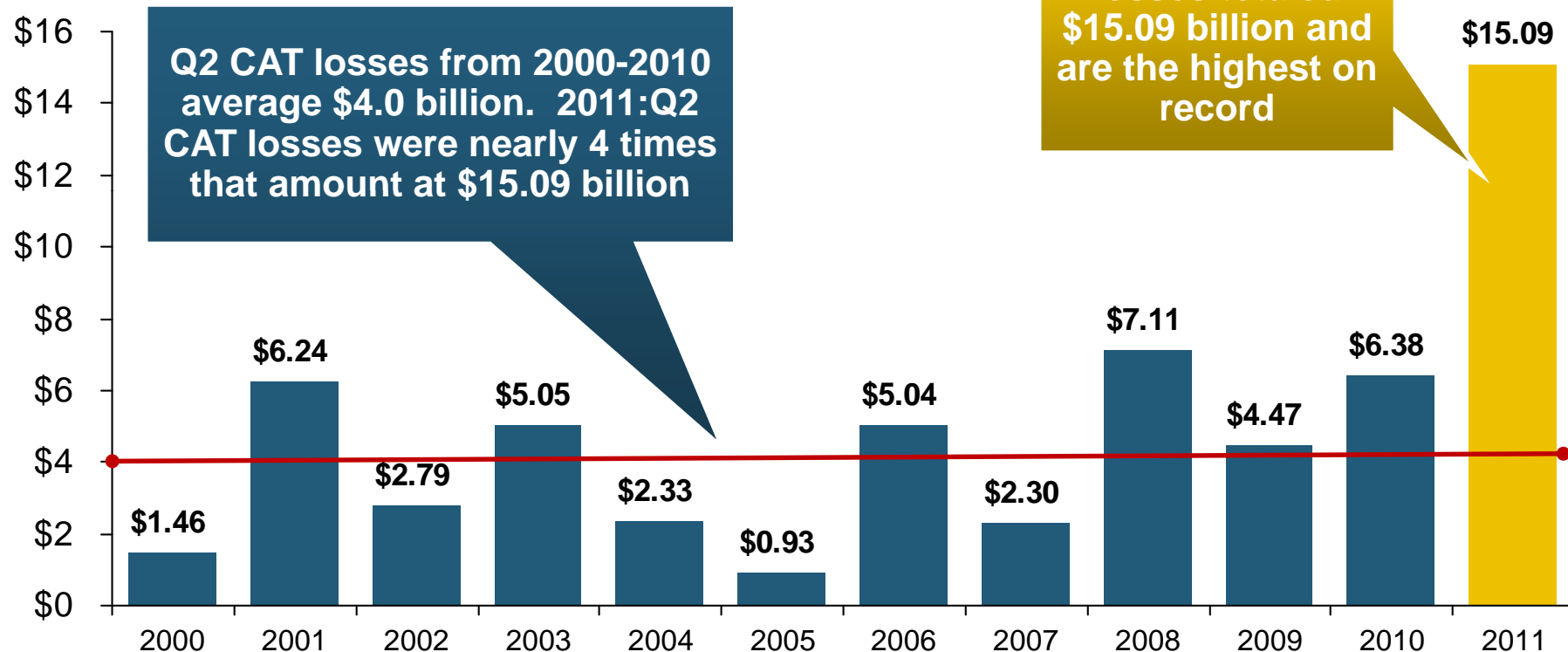
- ◆ Represents a 162% increase over the \$6.6 billion amount through the first half of 2010

Insured Loss Estimates for Selected Major Catastrophes in 2011

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

US Second Quarter Insured Catastrophe Losses, 2000–2011

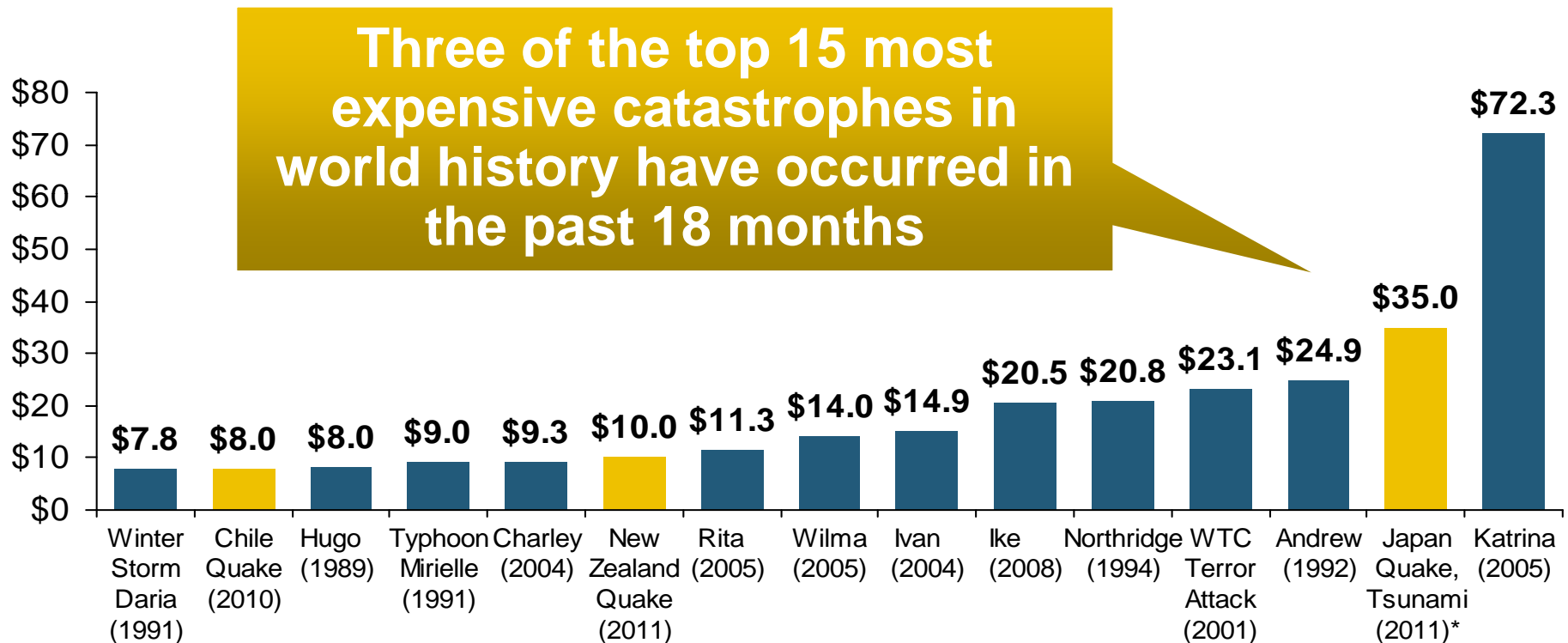
\$ Billions



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

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

(Insured Losses, 2010 Dollars, \$ Billions)



*Through June 20, 2011. 2011 disaster figures are estimates; Figures include federally insured flood losses, where applicable.

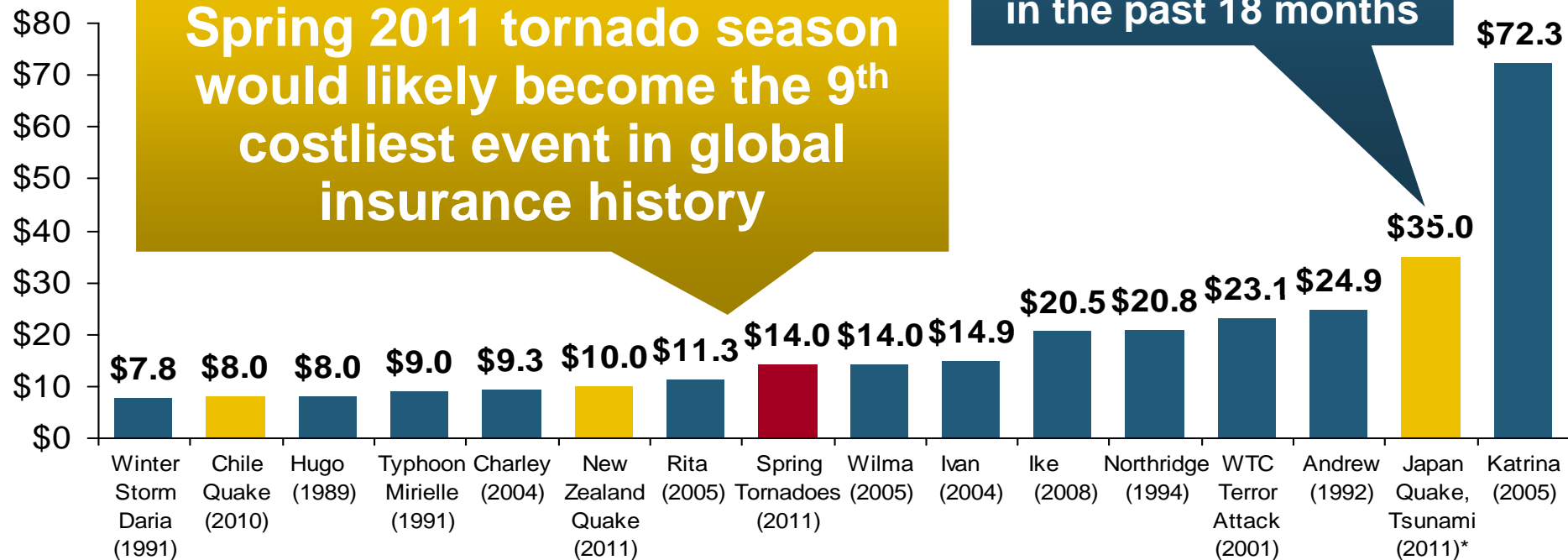
Sources: Swiss Re *sigma* 1/2011; AIR Worldwide, RMS, Eqecat; Insurance Information Institute.

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

(Insured Losses, 2010 Dollars, \$ Billions)

Taken as a single event, the Spring 2011 tornado season would likely become the 9th costliest event in global insurance history

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

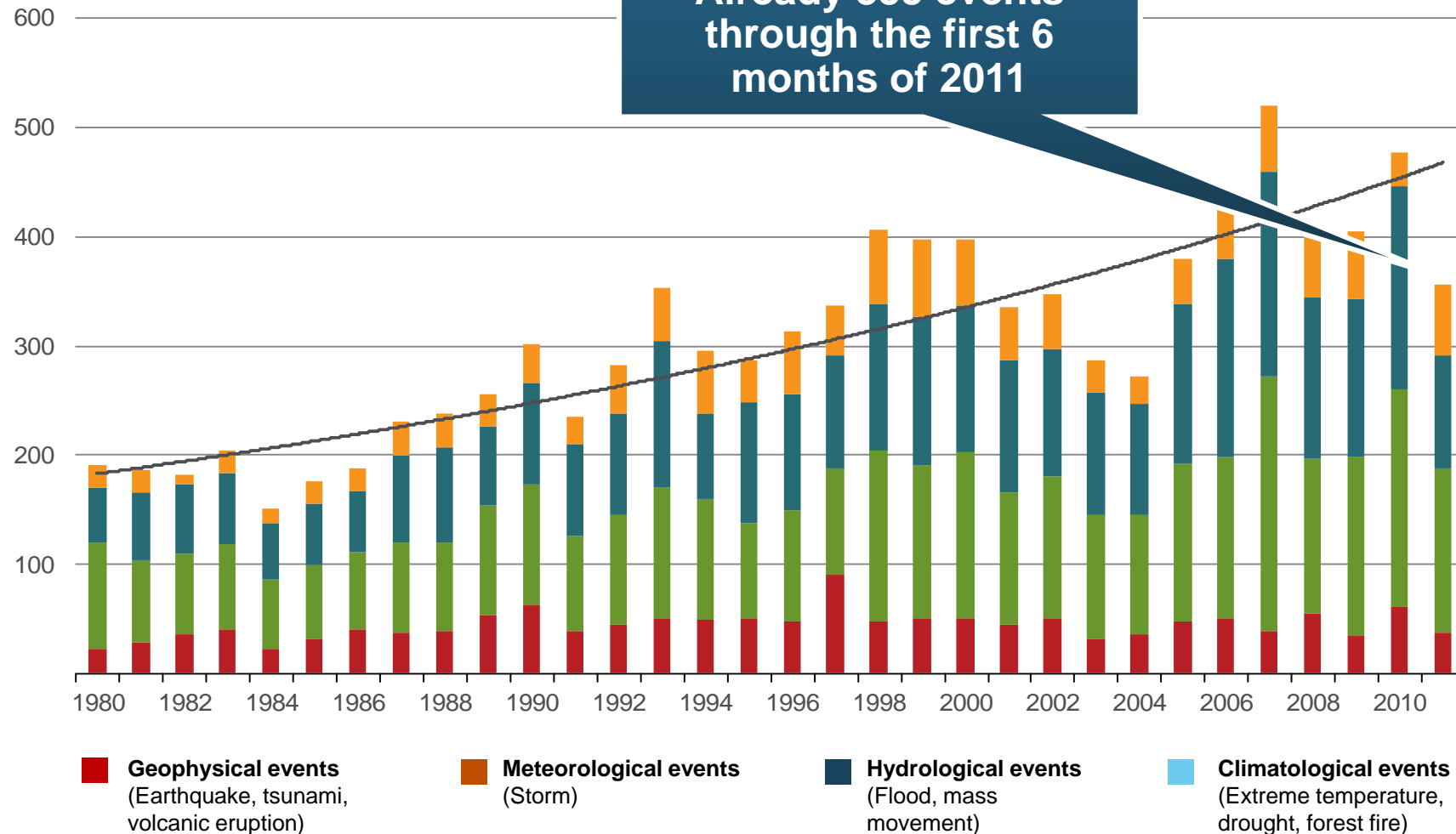


*Through June 20, 2011. 2011 disaster figures are estimates; Figures include federally insured flood losses, where applicable.

Sources: Swiss Re *sigma* 1/2011; AIR Worldwide, RMS, Eqecat; Insurance Information Institute.

Worldwide Natural Disasters, 1980 – 2011*

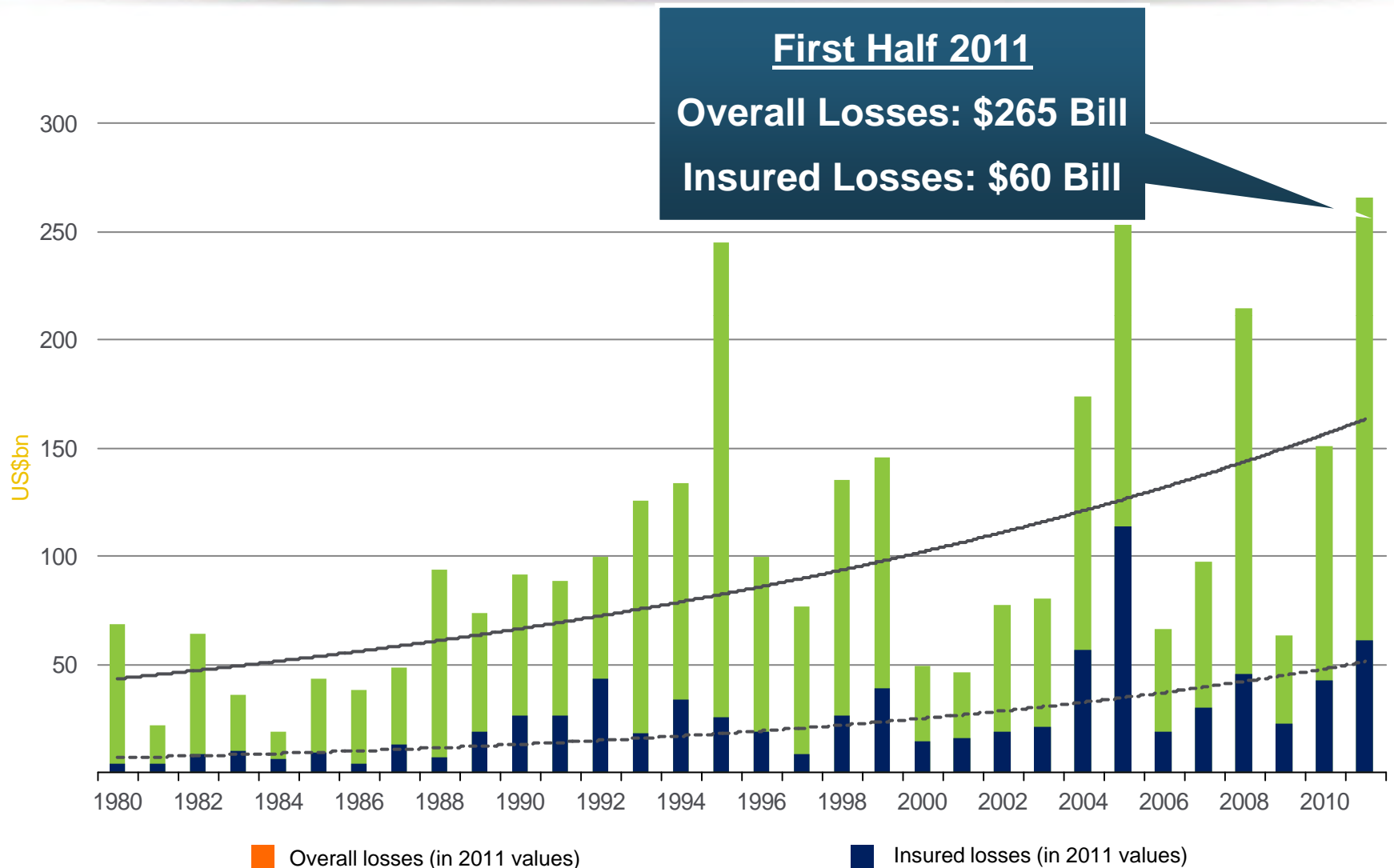
Number of Events



*2011 figure is through June 30.

Source: MR NatCatSERVICE

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



*2011 figure is through June 30.

Source: MR NatCatSERVICE

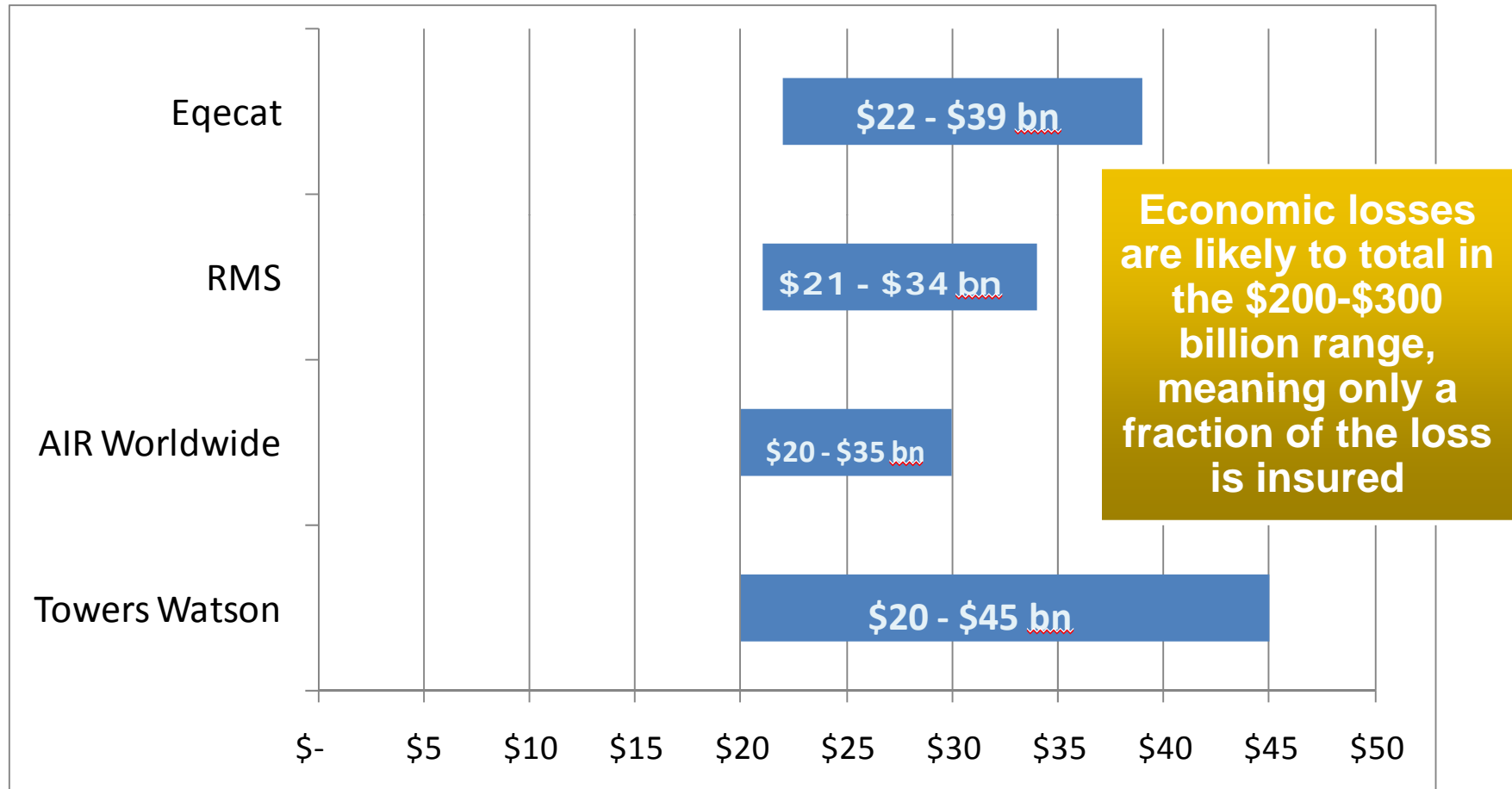


JAPAN EARTHQUAKE/TSUNAMI & NUCLEAR DISASTER

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

Insured Japan Earthquake Loss Estimates*

(Insured Losses, \$ Billions)

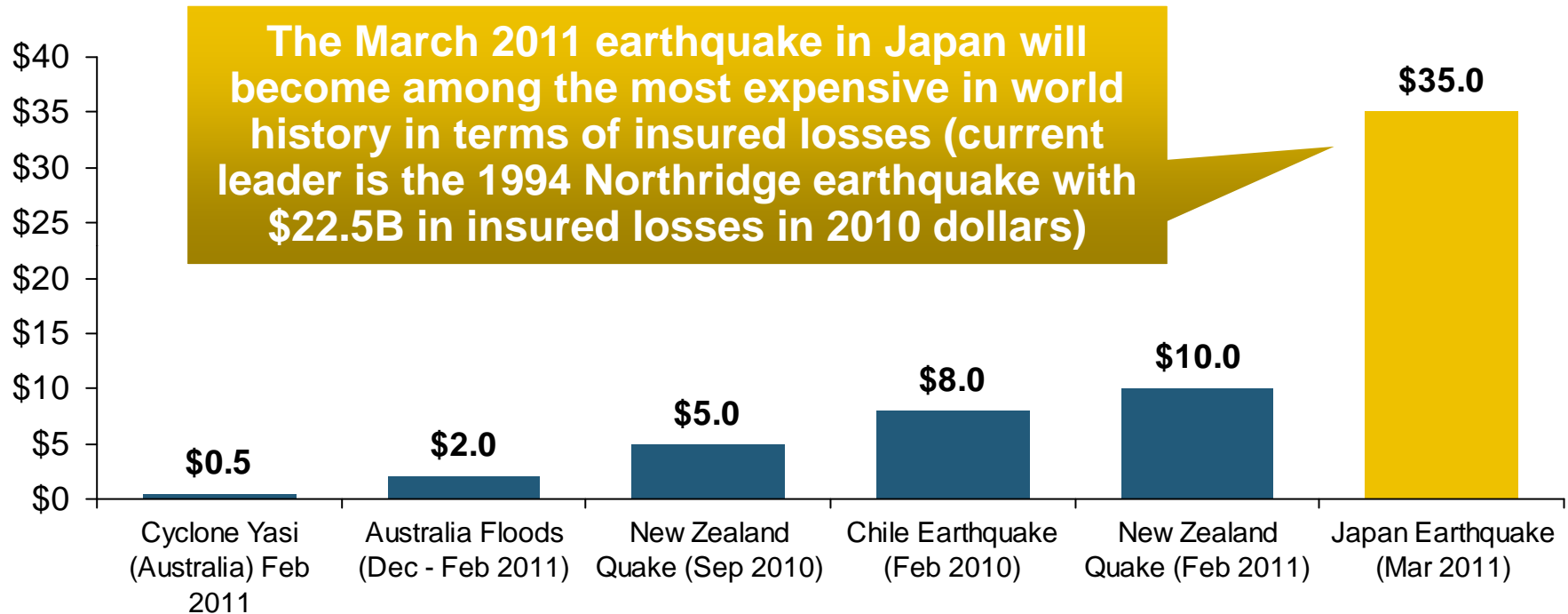


*As of June 17, 2011. Towers Watson estimate includes \$3.0 (low) to \$4.9 billion (high) in life insurance losses. RMS estimate includes insured life/health losses of \$3 to \$8 billion.

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

Recent Major Non-US Catastrophe Losses

(Insured Losses, \$US Billions)



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

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

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

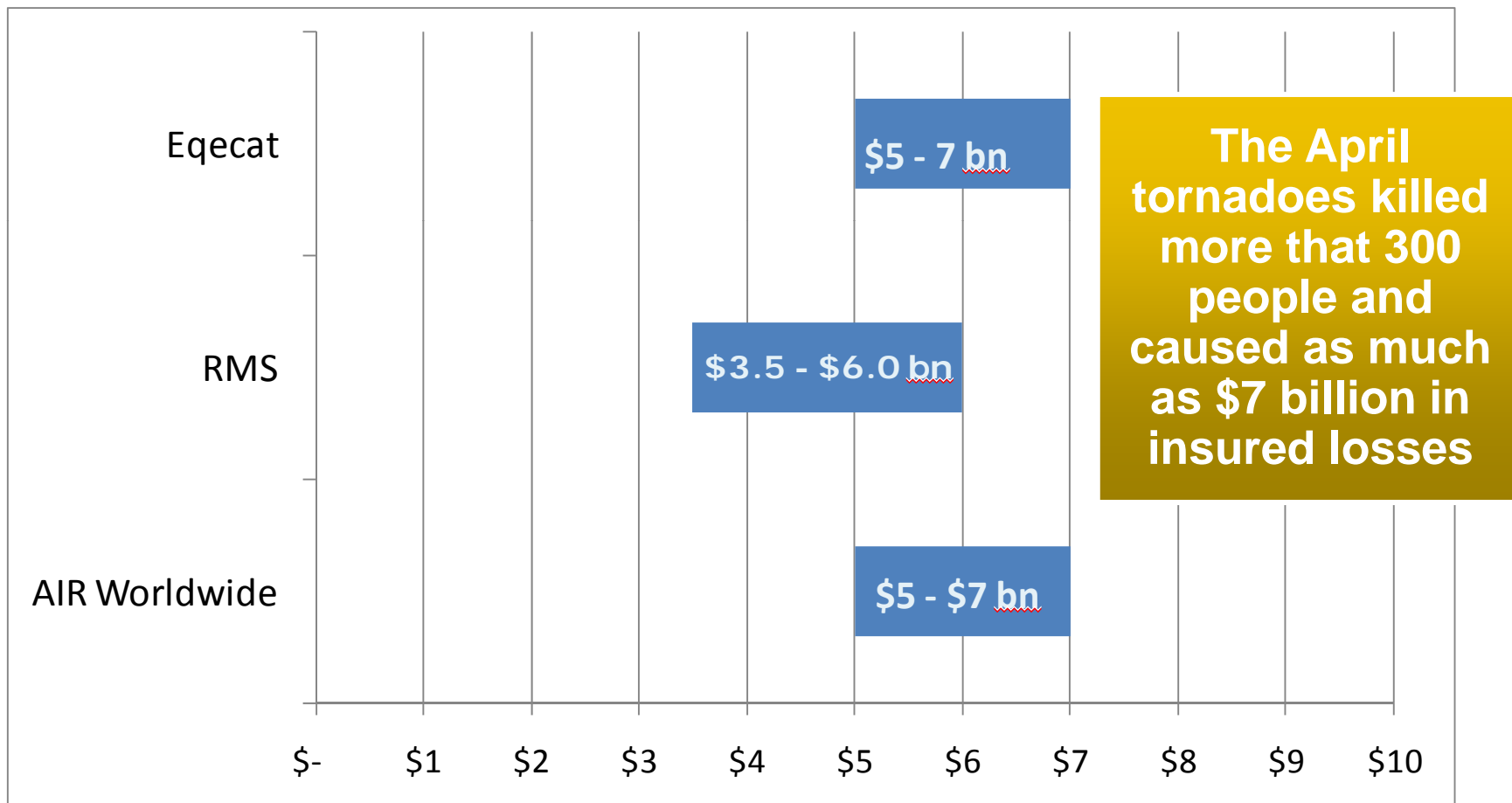


SPRING 2011 TORNADO OUTBREAK

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

Insured Loss Estimates from April 2011 Tornadoes*

(Insured Losses, \$ Billions)

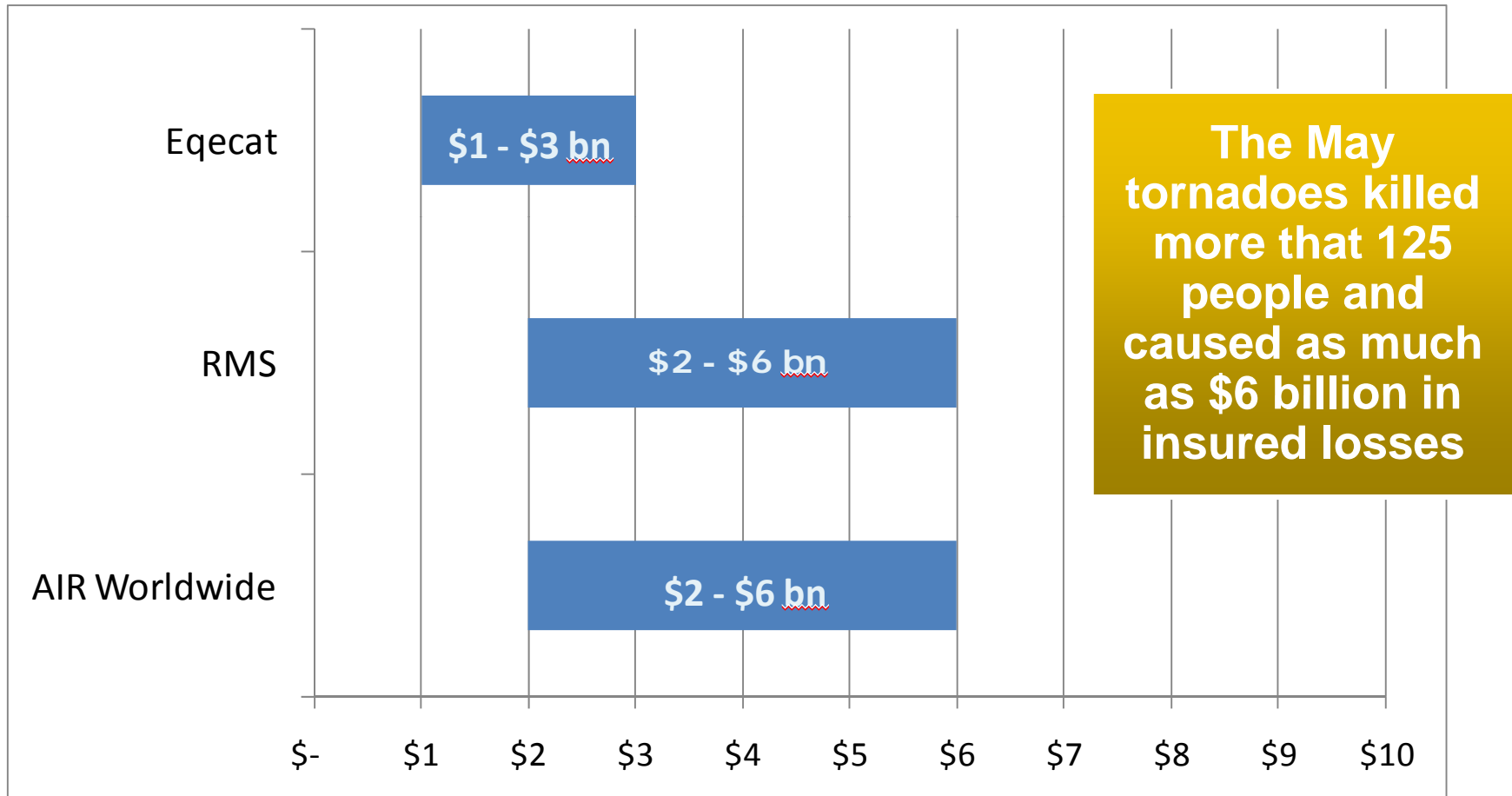


*As of June 17, 2011.

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

Insured Loss Estimates from May 2011 (Joplin) Tornadoes*

(Insured Losses, \$ Billions)



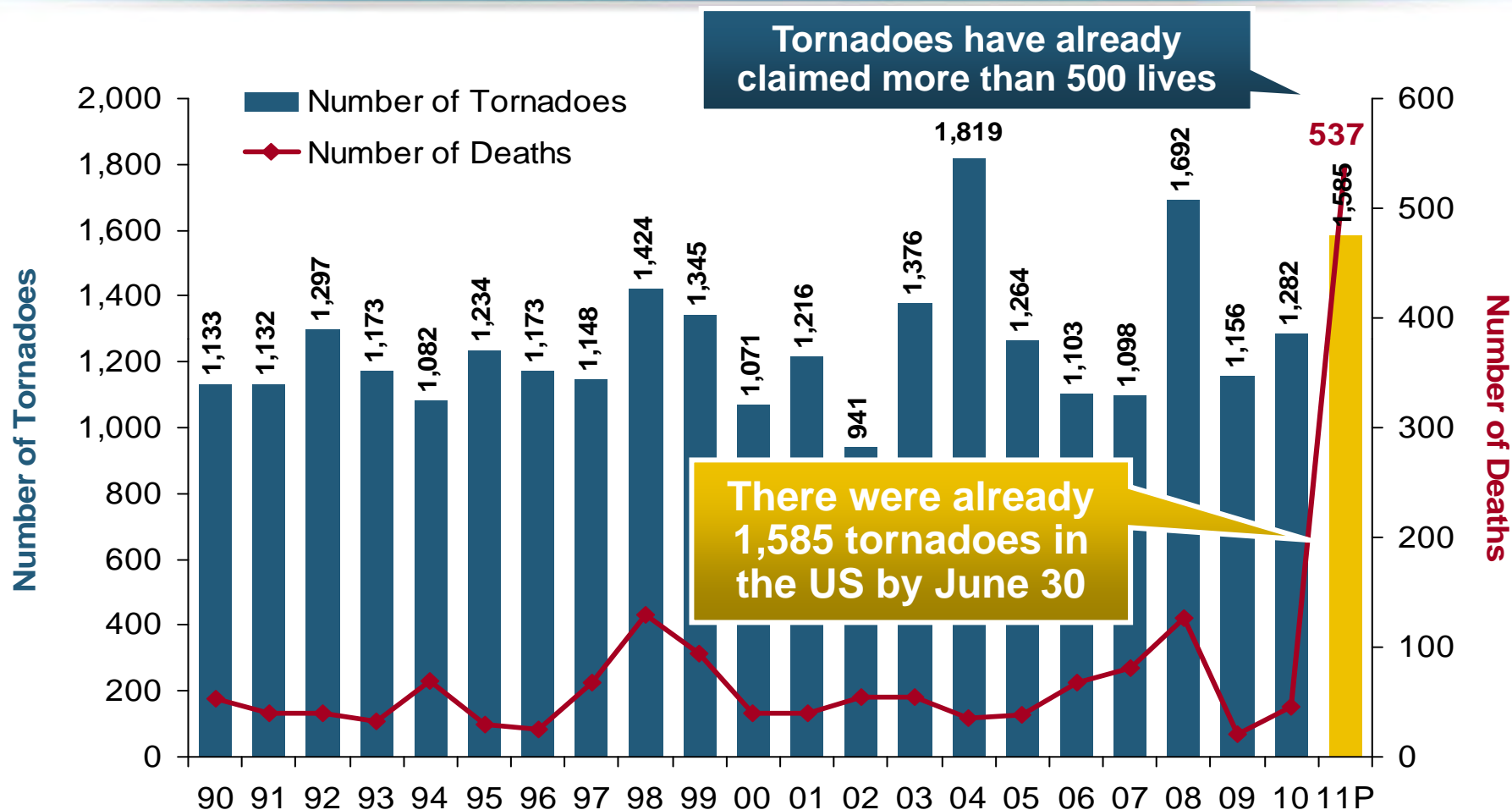
*As of June 17, 2011.

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

Summary of Recent Tornado Activity

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

Number of Tornadoes and Related Deaths, 1990 – 2011*



Insurers Expect to Pay \$2 Billion on 165,000 Claims Arising from the April 2011 Tornadoes in the Birmingham and Tuscaloosa Areas

*2011 is preliminary data through June 30.

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

Insurers Making a Difference in Impacted Communities



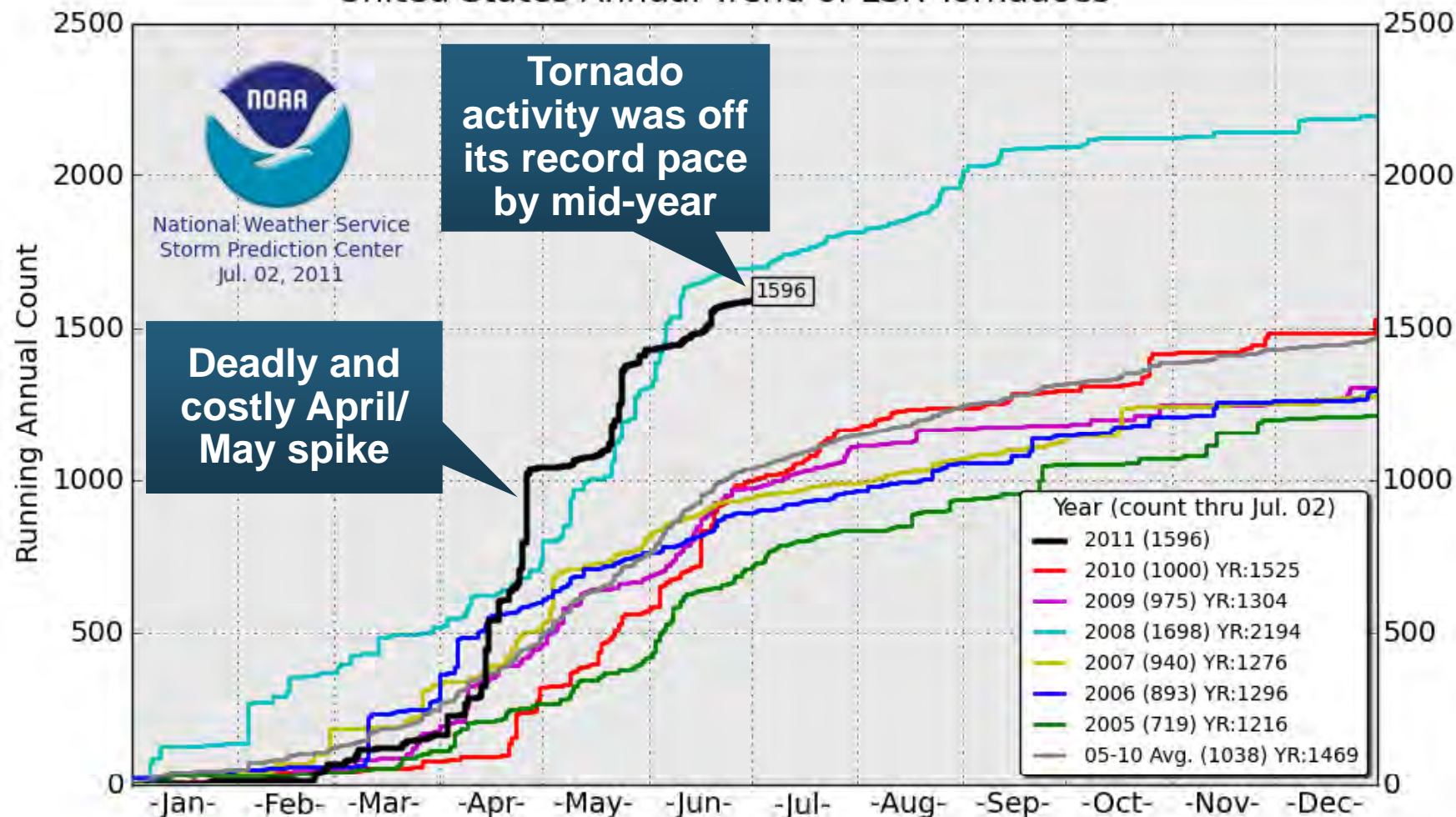
Destroyed home in Tuscaloosa. Insurers will pay some 165,000 claims totaling \$2 billion in the Tuscaloosa/Birmingham areas alone.

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



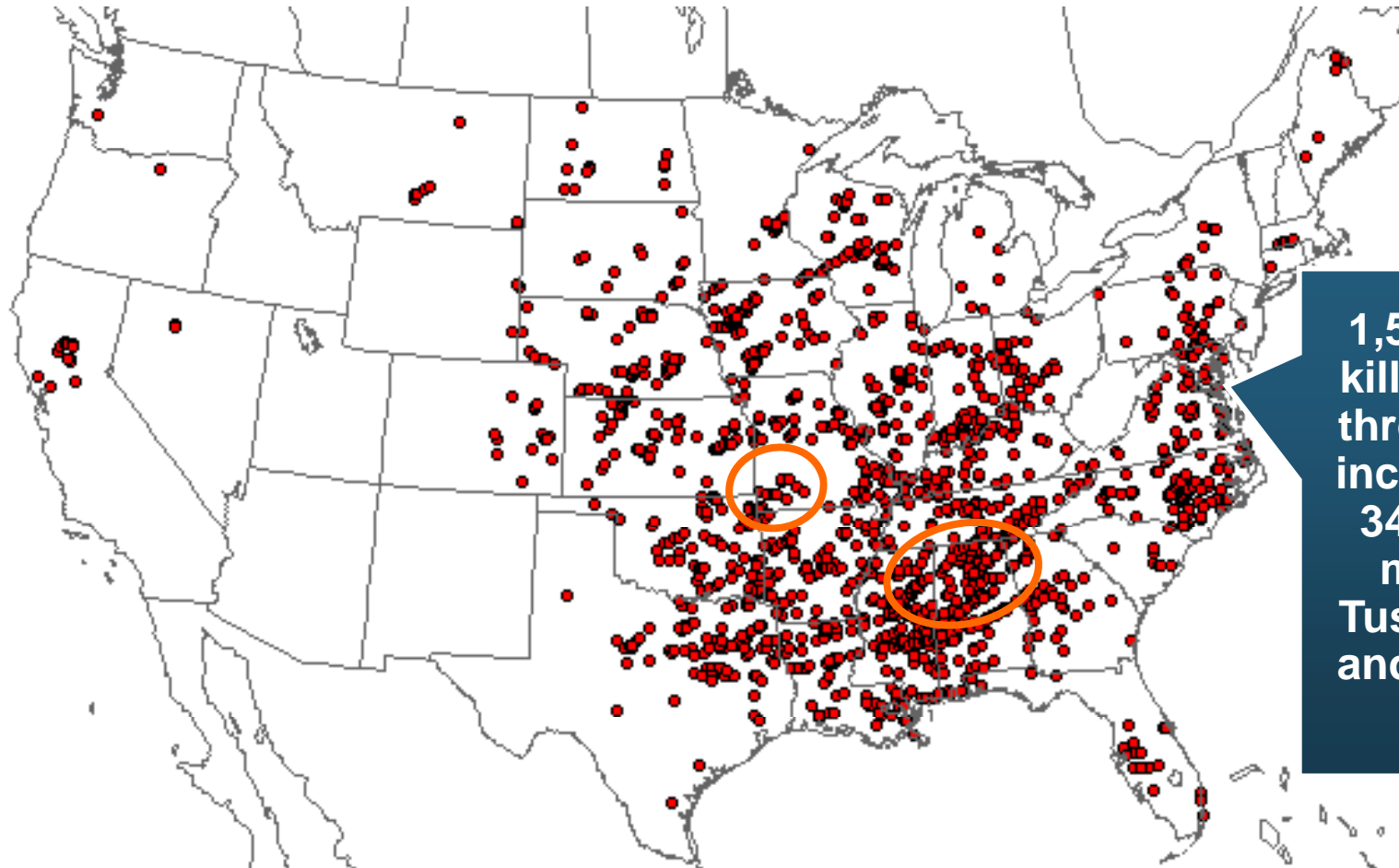
U.S. Tornado Count, 2005-2011*

United States Annual Trend of LSR Tornadoes*



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

Location of Tornadoes in the US, January 1—June 30, 2011



1,585 tornadoes
killed 537 people
through June 30,
including at least
340 on April 26
mostly in the
Tuscaloosa area,
and 130 in Joplin
on May 22



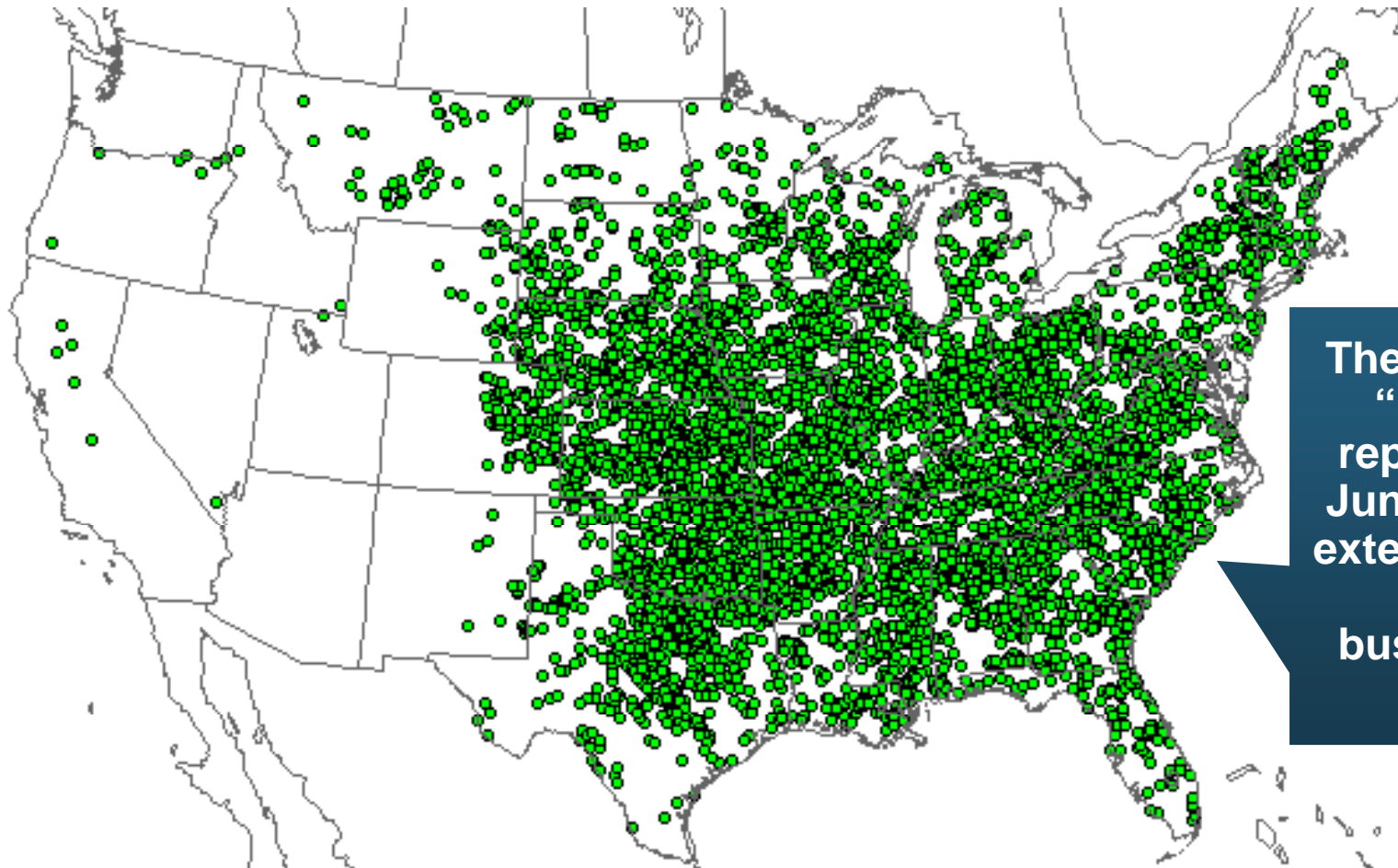
PRELIMINARY SEVERE WEATHER
REPORT DATABASE (ROUGH LOG)

NOAA/Storm Prediction Center Norman, Oklahoma

Tornado Reports
January 01, 2011 - June 30, 2011

Updated: Thursday June 30, 2011 11:49 CT

Location of Large Hail Reports in the US, January 1—June 30, 2011



There were 7,176
“Large Hail”
reports through
June 30, causing
extensive damage
to homes,
businesses and
vehicles



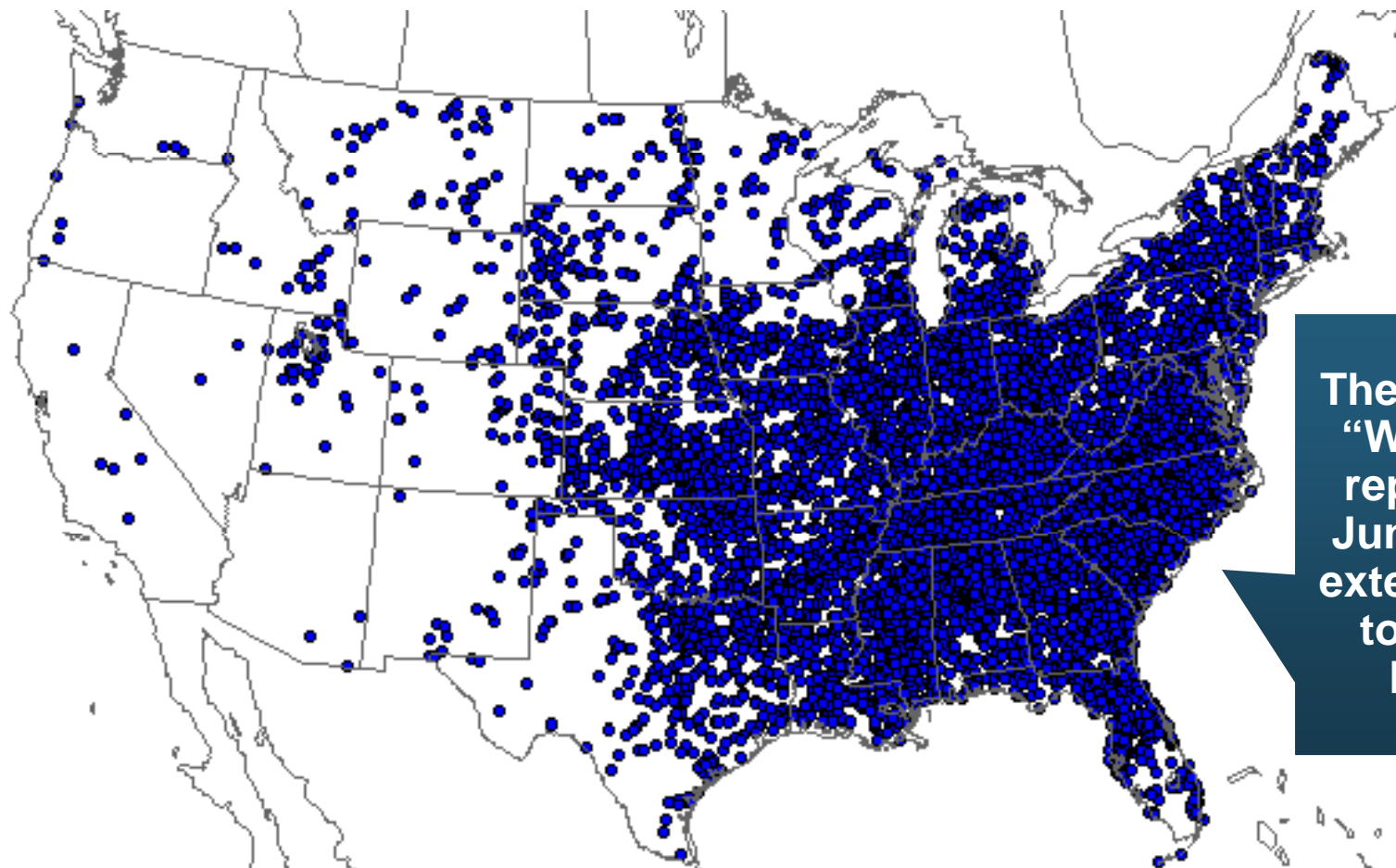
PRELIMINARY SEVERE WEATHER
REPORT DATABASE (ROUGH LOG)

NOAA/Storm Prediction Center Norman, Oklahoma

Hail Reports
January 01, 2011 - June 30, 2011

Updated: Thursday June 30, 2011 11:49 CT

Location of Wind Damage Reports in the US, January 1—June 30, 2011



There were 11,283
“Wind Damage”
reports through
June 30, causing
extensive damage
to homes and,
businesses



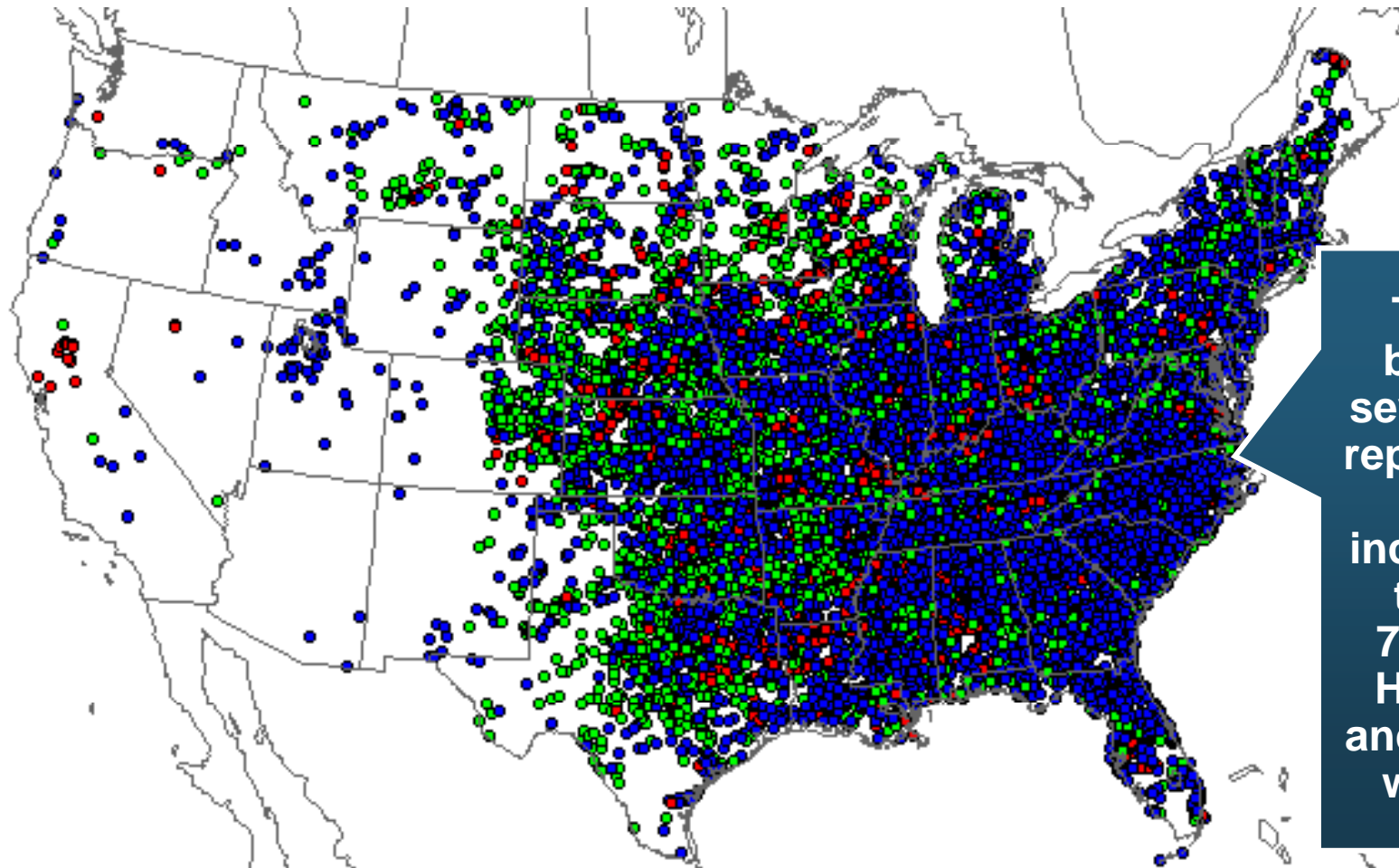
PRELIMINARY SEVERE WEATHER
REPORT DATABASE (ROUGH LOG)

NOAA/Storm Prediction Center Norman, Oklahoma

Wind Reports
January 01, 2011 - June 30, 2011

Updated: Thursday June 30, 2011 11:49 CT

Severe Weather Reports, January 1—June 30, 2011



There have been 20,044 severe weather reports through June 30; including 1,585 tornadoes; 7,176 “Large Hail” reports and 11,283 high wind events



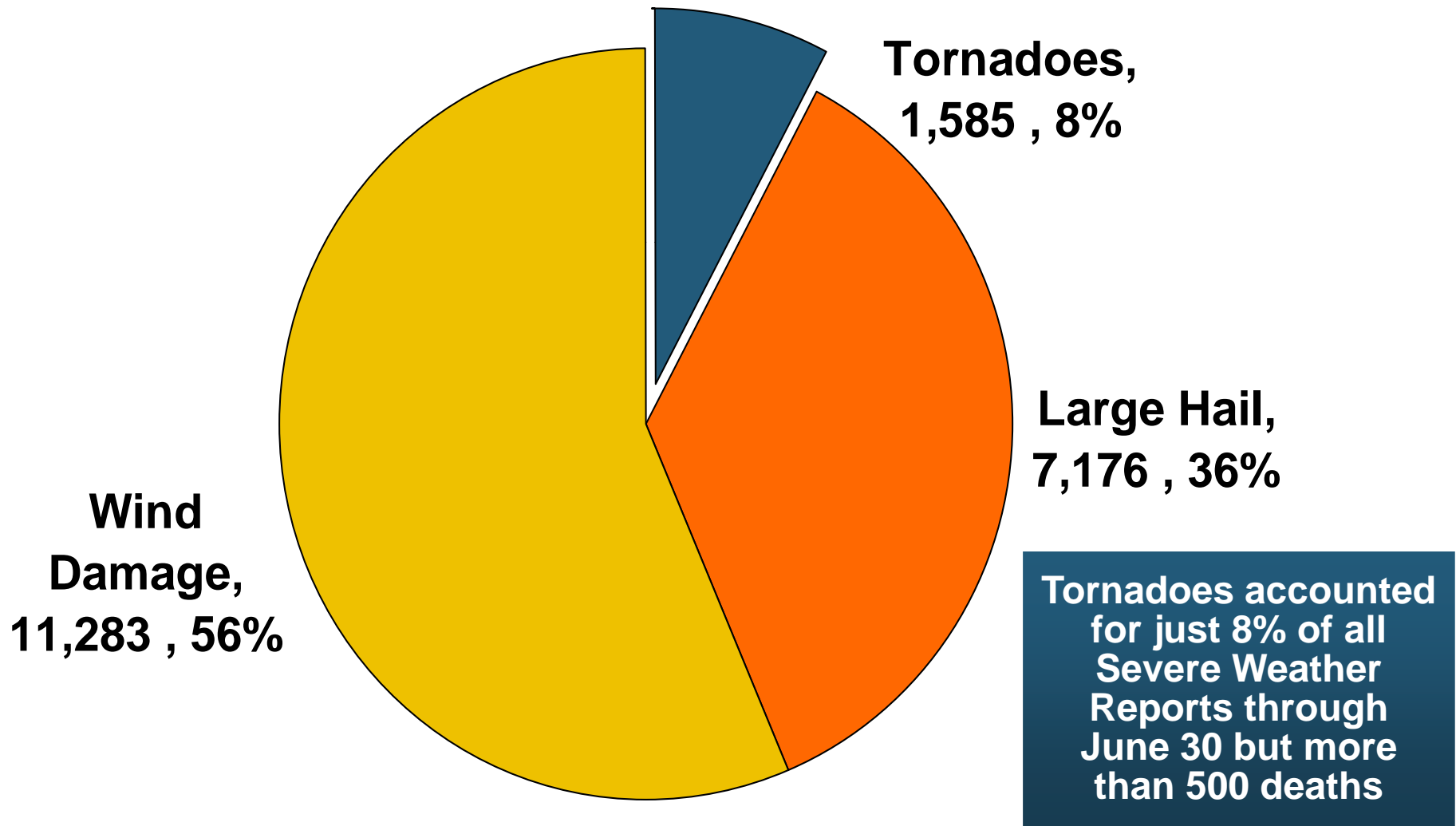
PRELIMINARY SEVERE WEATHER
REPORT DATABASE (ROUGH LOG)

NOAA/Storm Prediction Center Norman, Oklahoma

Severe Weather Reports
January 01, 2011 - June 30, 2011

Updated: Thursday June 30, 2011 11:49 CT

Number of Severe Weather Reports in US, by Type: January 1—June 30, 2011

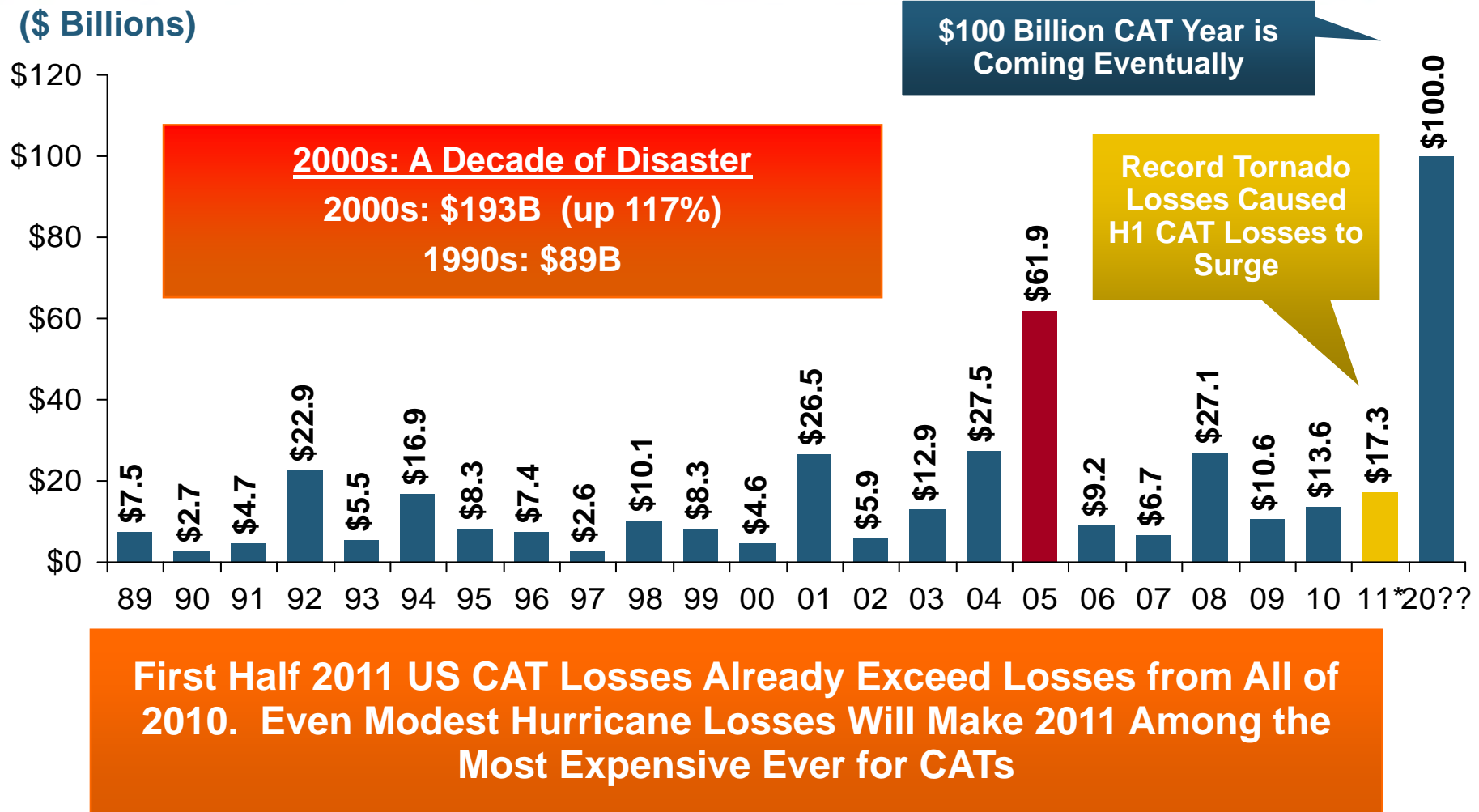




US CATASTROPHE INSURED LOSS UPDATE

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

US Insured Catastrophe Losses



*First half 2011.

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

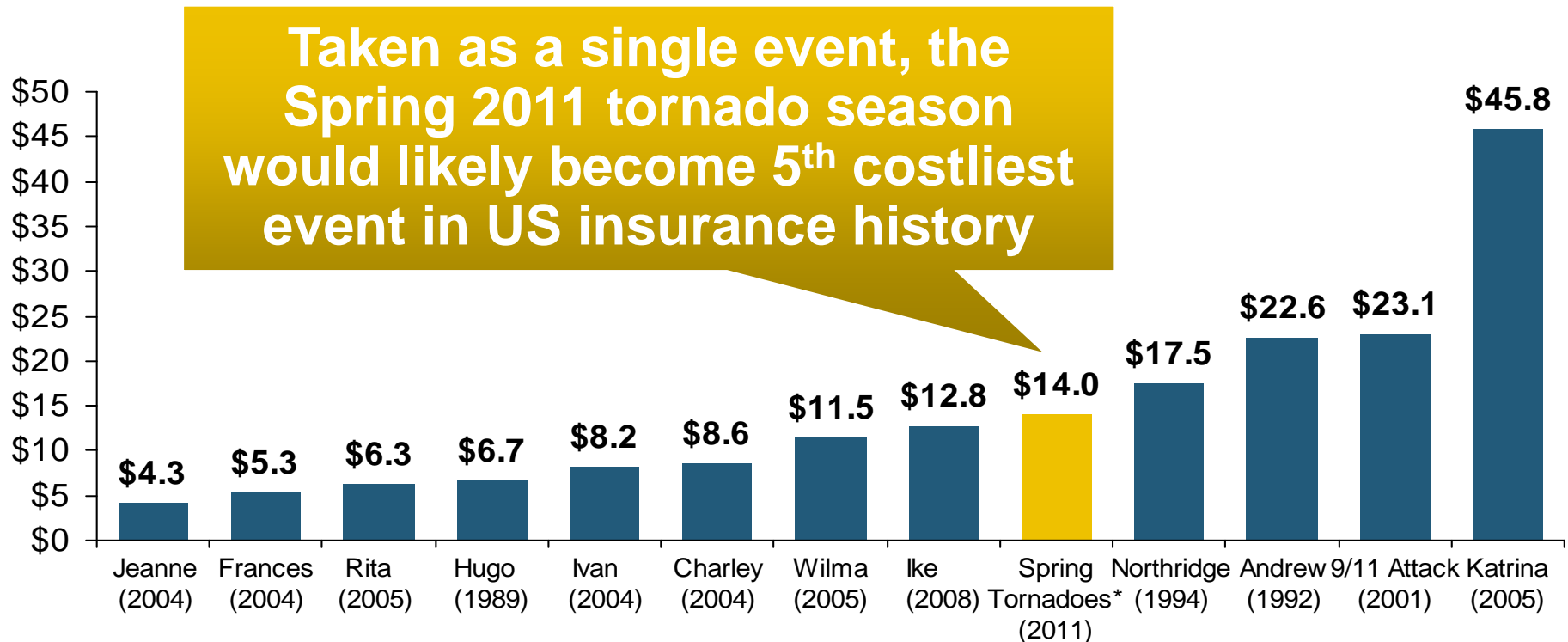
Sources: Property Claims Service/ISO; Insurance Information Institute.

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

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

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

(Insured Losses, 2010 Dollars, \$ Billions)



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

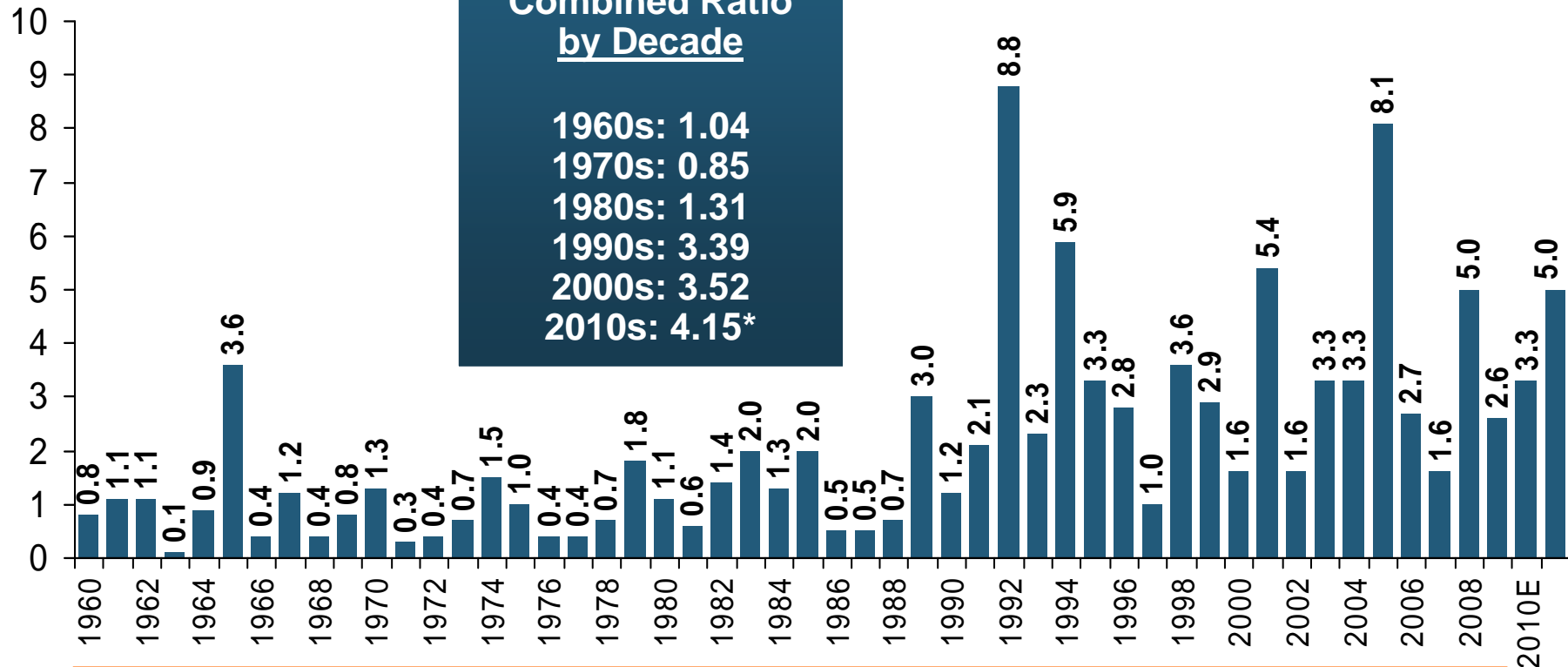
Sources: PCS; Insurance Information Institute inflation adjustments.

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

Combined Ratio Points

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

1960s: 1.04
1970s: 0.85
1980s: 1.31
1990s: 3.39
2000s: 3.52
2010s: 4.15*



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

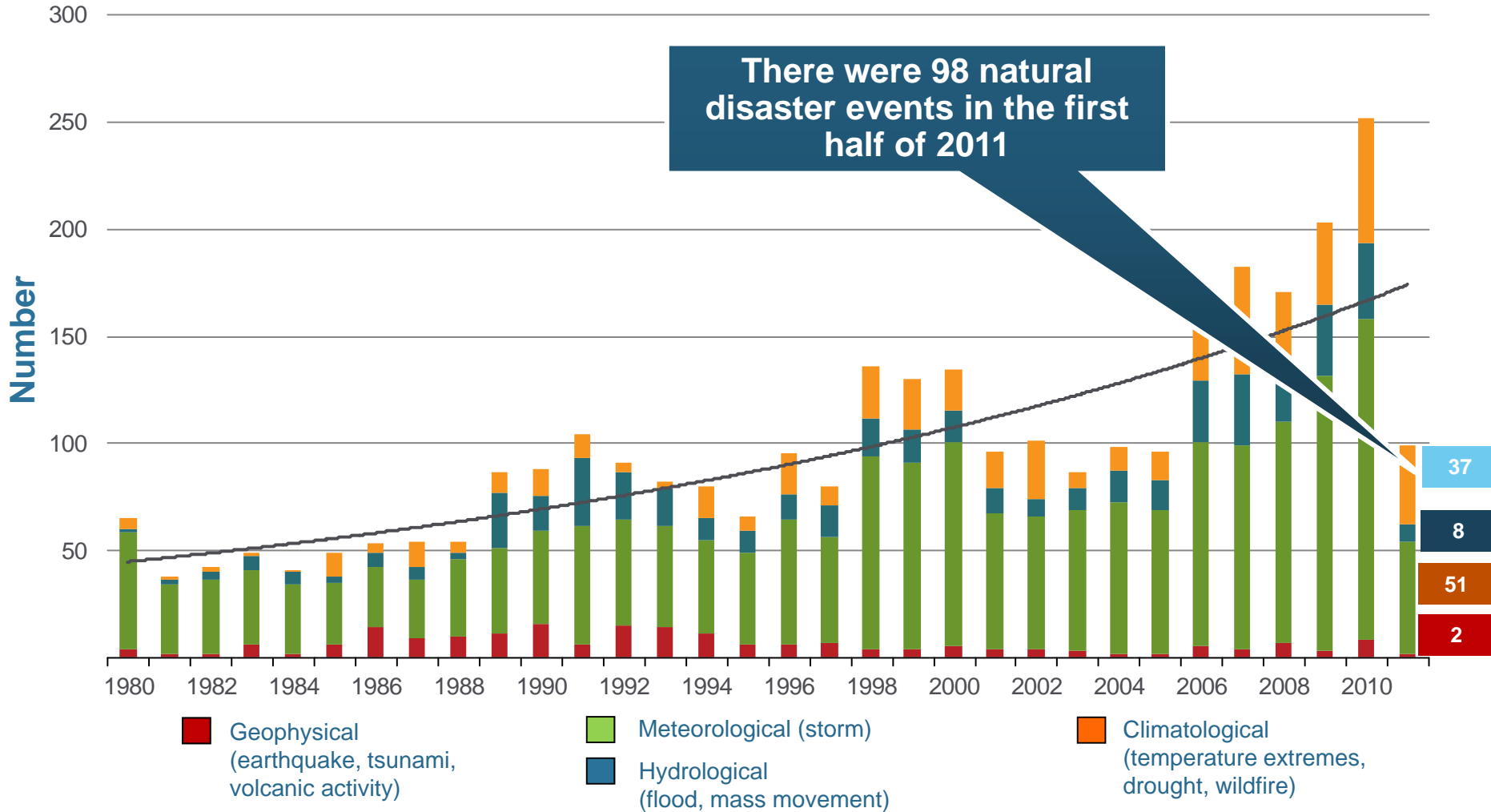
*Insurance Information Institute estimates for 2010 and 2011:H1

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

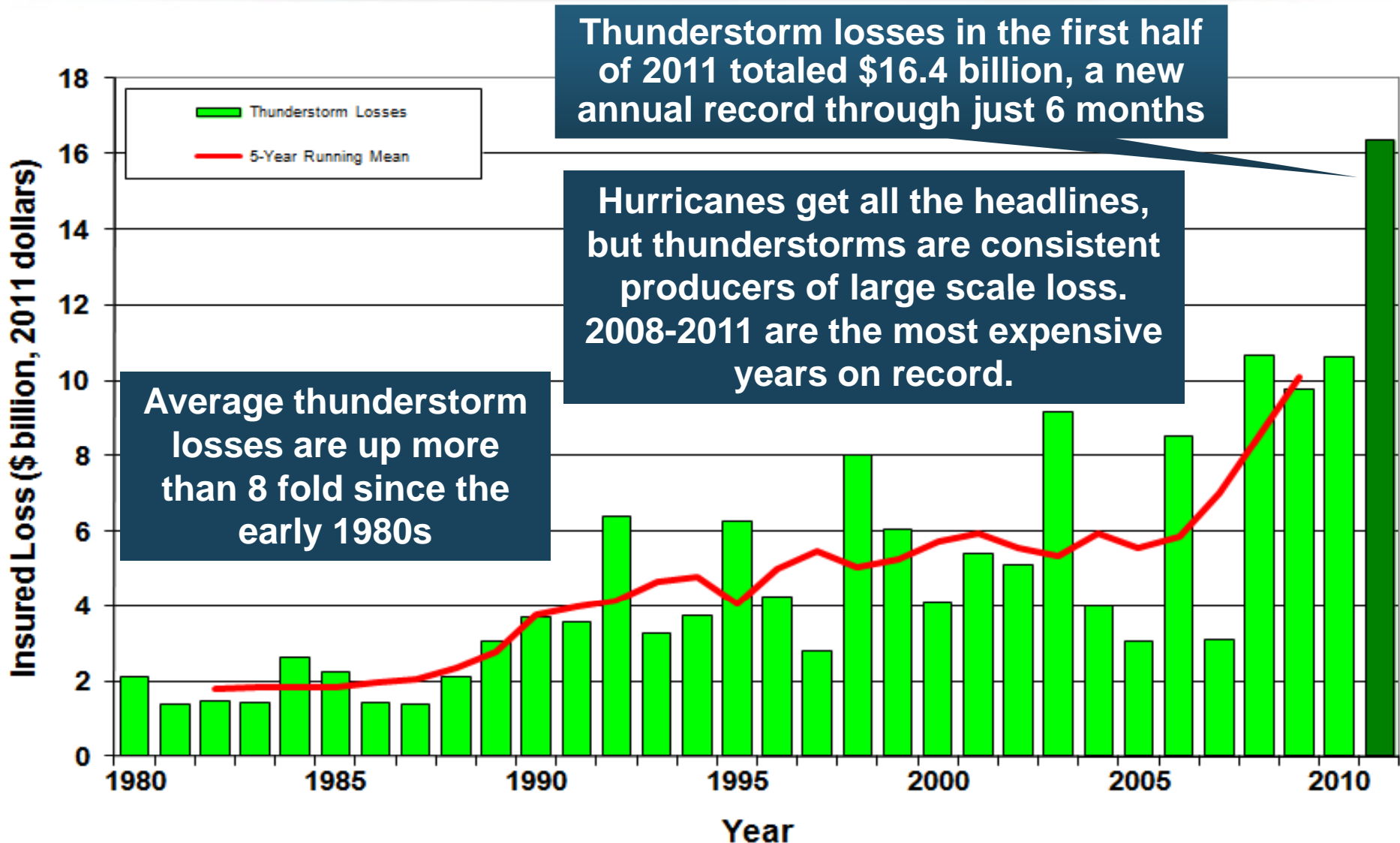
Source: ISO; Insurance Information Institute.

Natural Disasters in the United States, 1980 – 2011*

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



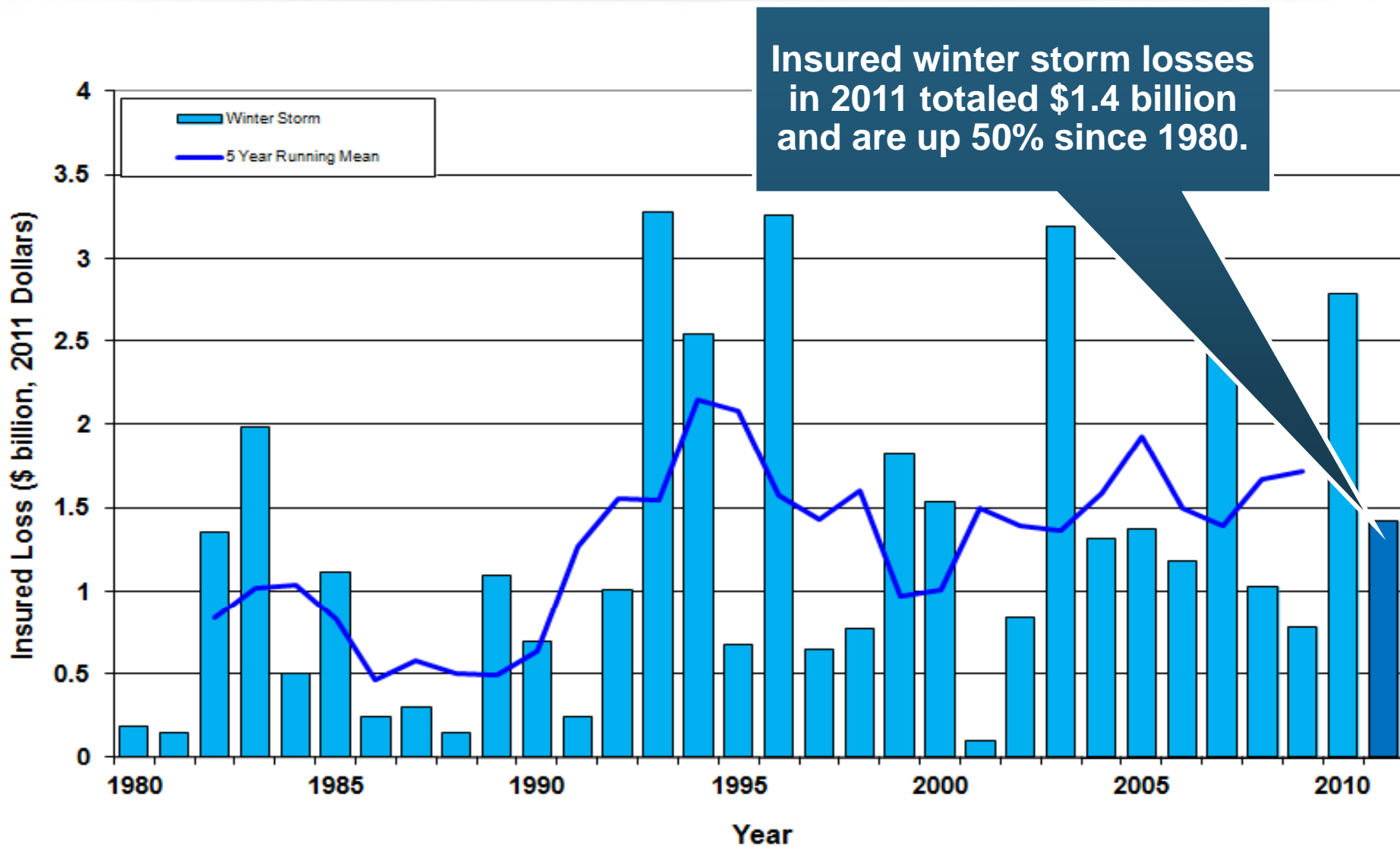
U.S. Thunderstorm Loss Trends, 1980 – 2011*



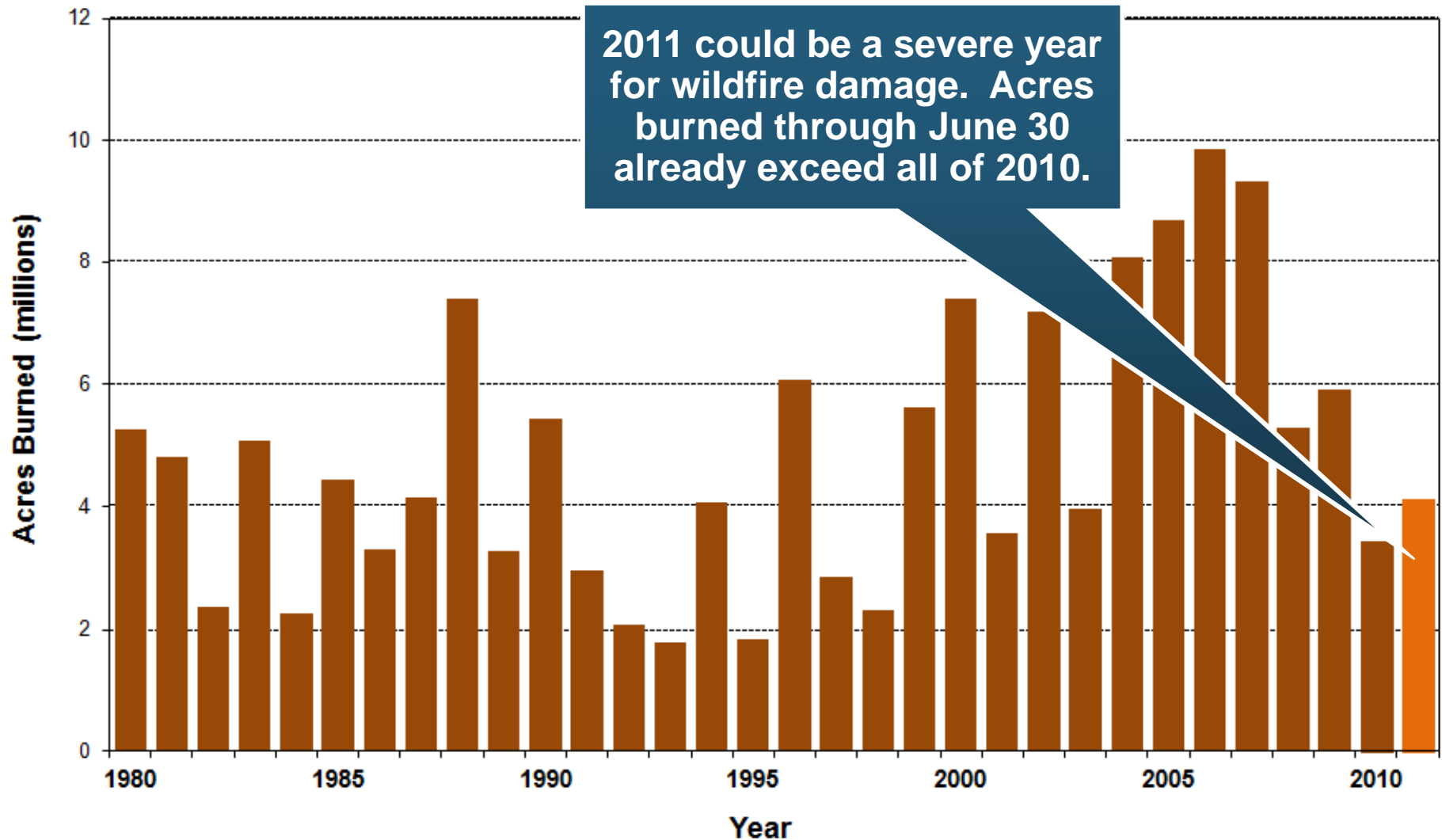
*Through June 30, 2011.

Source: Property Claims Service, MR NatCatSERVICE

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



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



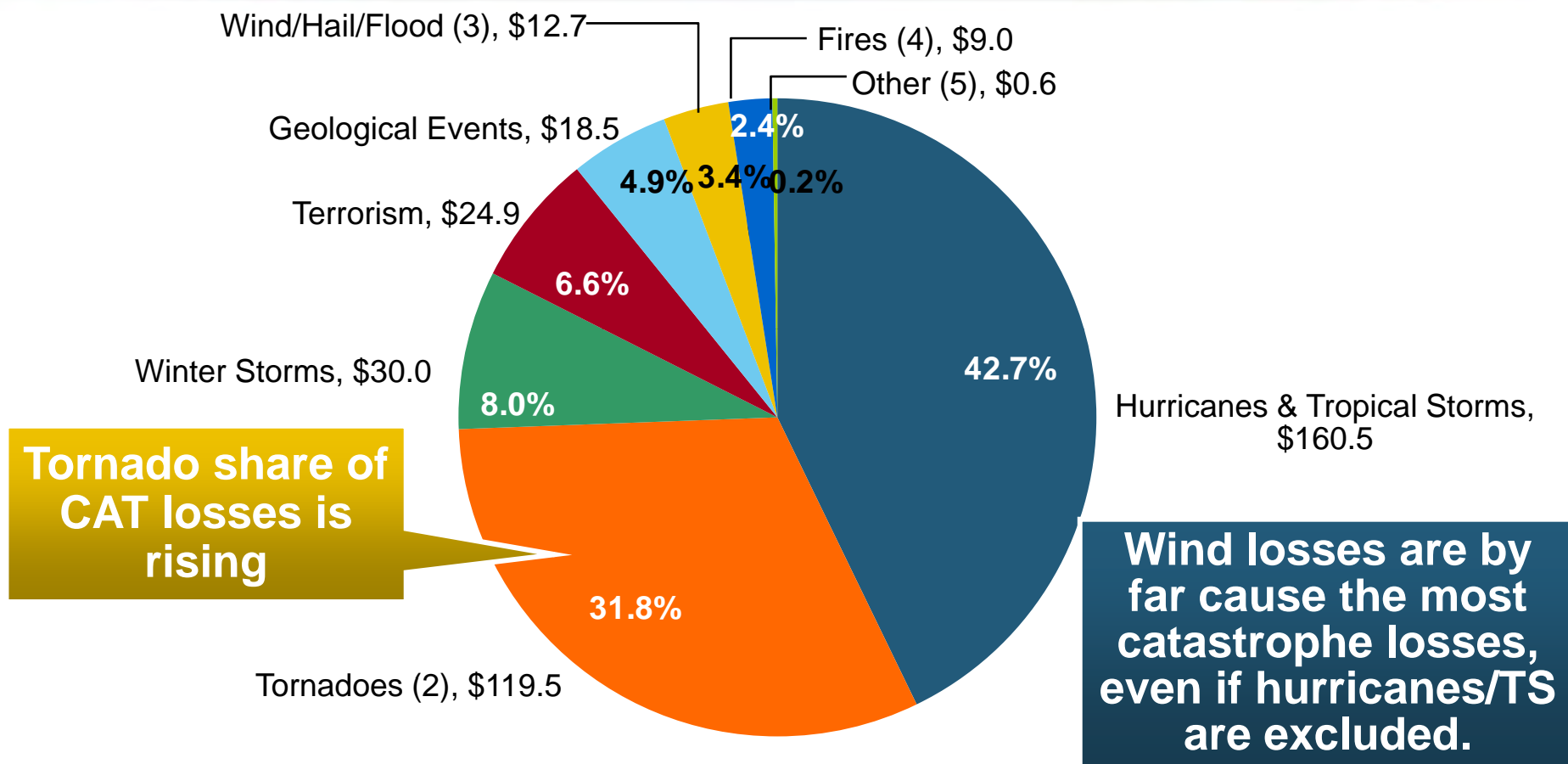
Notable Wildfires in 2011

April – June

- ***Texas: Over 3 million acres burned in west Texas from 12 major seats of fire. Over 200 homes and businesses destroyed, \$50 million insured loss.***
- Arizona and New Mexico: “Wallow” fire largest in AZ history at 538,000 acres, Las Conchas fire near Los Alamos, 30 buildings destroyed.



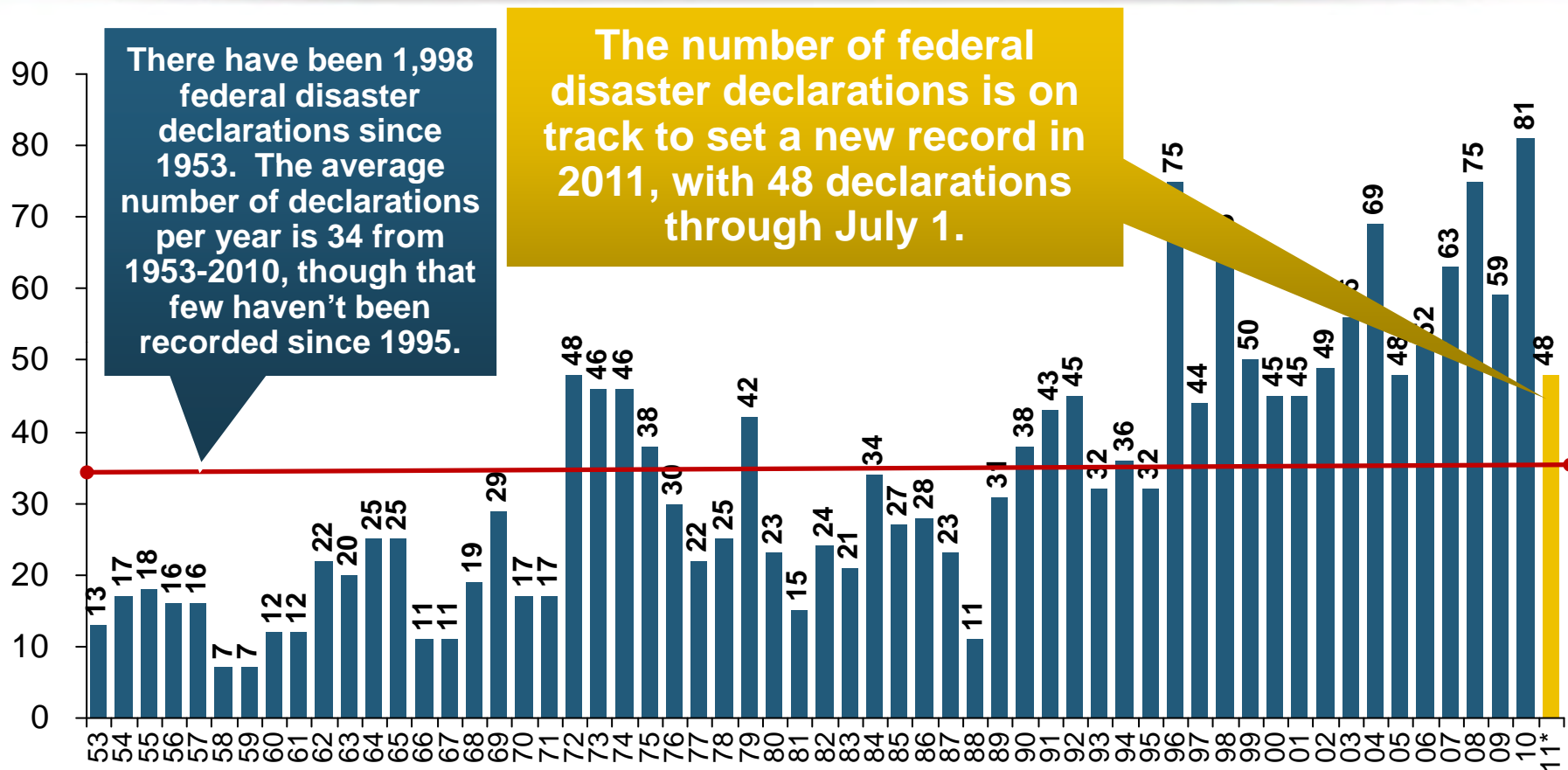
Inflation Adjusted U.S. Catastrophe Losses by Cause of Loss, 1990–2011:H1¹



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

Source: ISO's Property Claim Services Unit.

Number of Federal Disaster Declarations, 1953-2011*

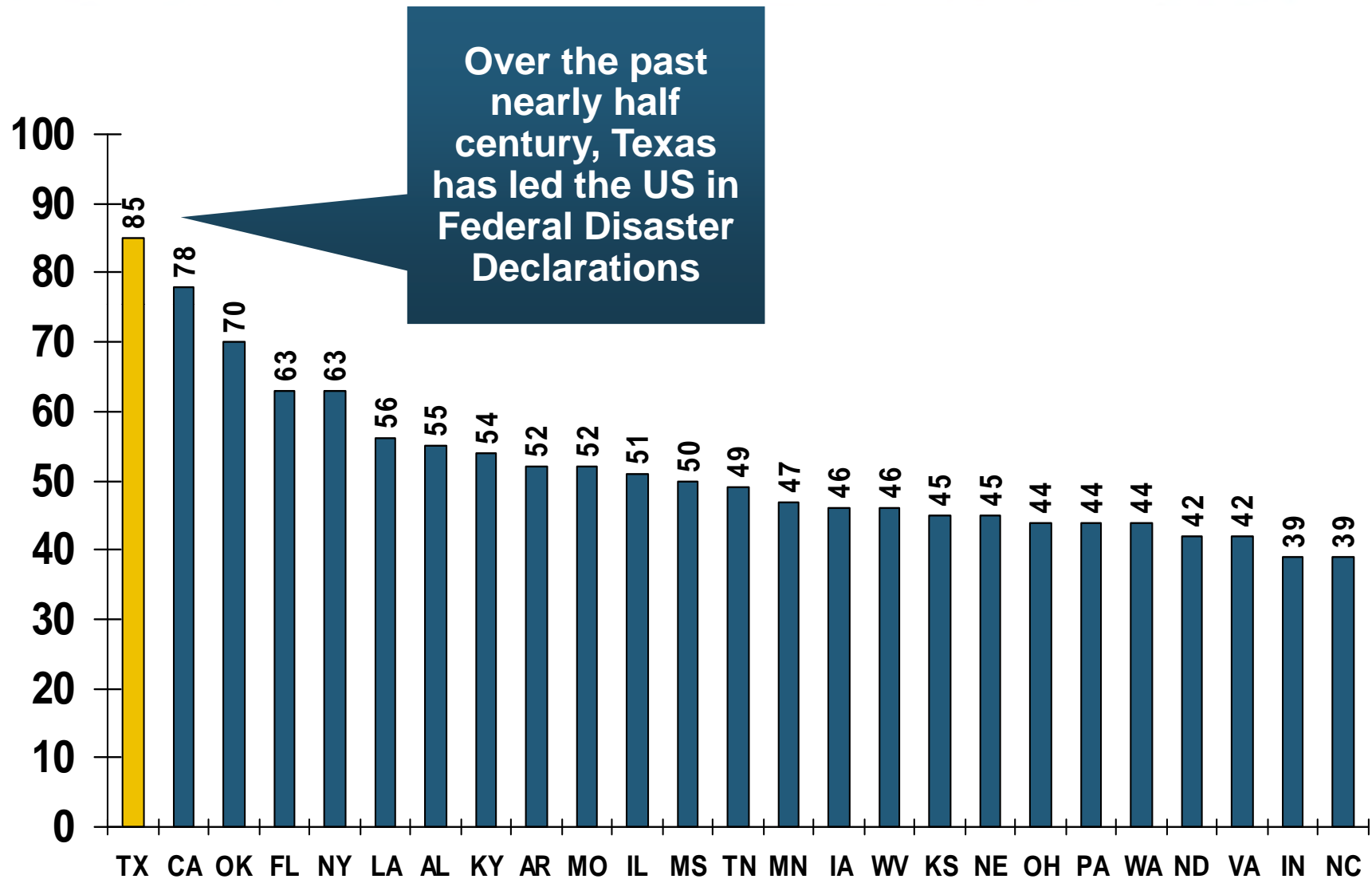


The Number of Federal Disaster Declarations Is Rising

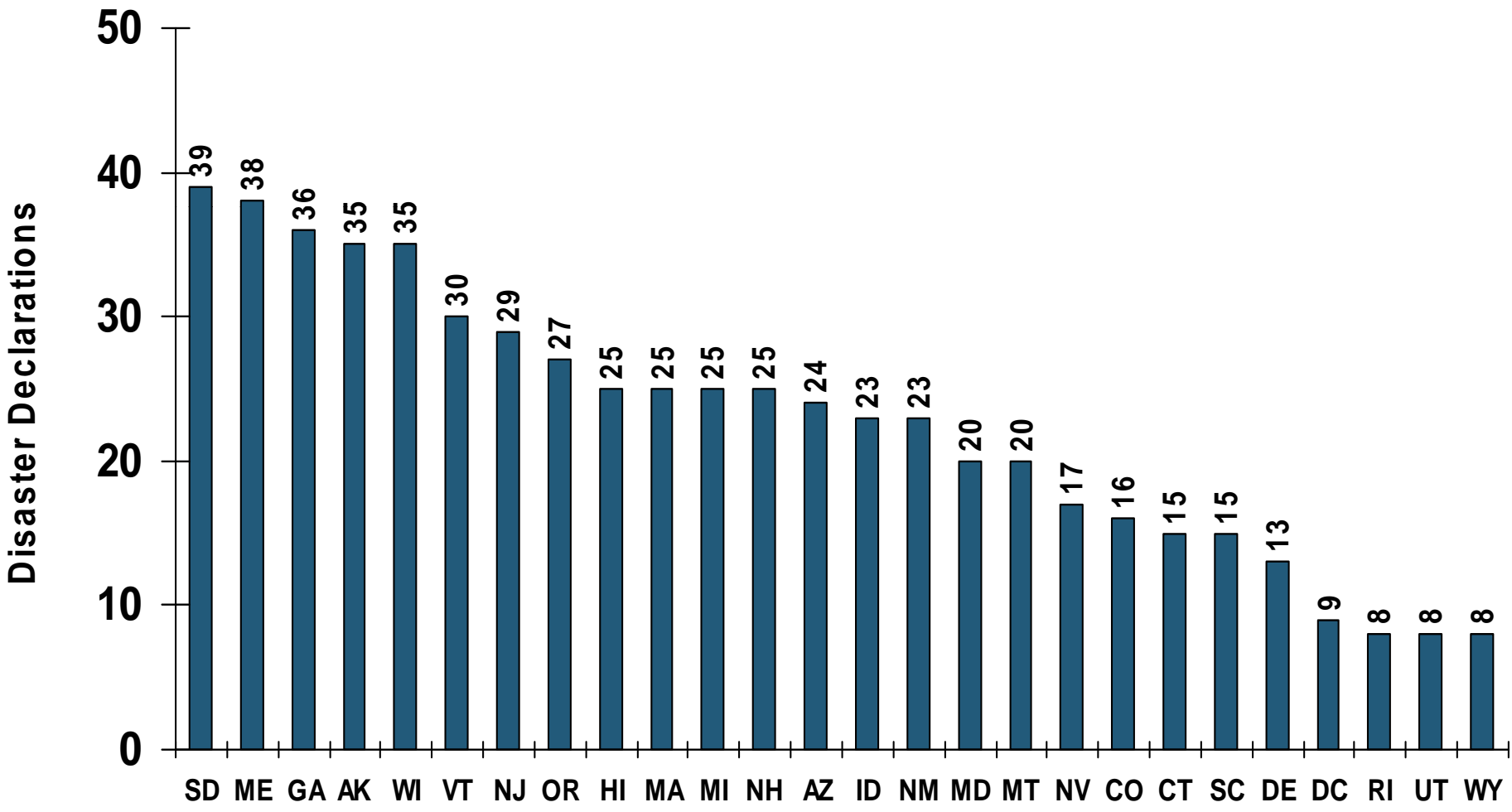
*Through July 1, 2011.

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

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



Federal Disasters Declarations by State, 1953 – June 30, 2011: Lowest 25 States



Source: FEMA.

The BIG Question: When Will the Market Turn?

Insurance Cycle Dynamics

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

Criteria	Status	Comments
Sustained Period of Large Underwriting Losses	<i>Not Yet Happened</i>	<ul style="list-style-type: none"> • Apart from Q2:2011, overall p/c underwriting losses remain modest • Combined ratios (ex-Q2 CATs) still in low 100s (vs. 110+ at onset of last hard market) • Prior-year reserve releases continue reduce u/w losses, boost ROEs
Material Decline in Surplus/ Capacity	<i>Surplus is At/Near Record High</i>	<ul style="list-style-type: none"> • Surplus hit a record \$565B as of 3/31/11 • Analysts est. excess surplus of \$75-\$100B • Some excess capacity may still remain in reinsurance markets • Weak growth in demand for insurance is insufficient to absorb much excess capacity
Tight Reinsurance Market	<i>Somewhat in Place</i>	<ul style="list-style-type: none"> • Higher prices in Asia/Pacific • Modestly improved pricing for US risks
Renewed Underwriting & Pricing Discipline	<i>Not Broadly Evident</i>	<ul style="list-style-type: none"> • Commercial lines pricing trends remain negative • Competition remains intense as many seek to maintain market share • Terms & conditions—no broad tightening

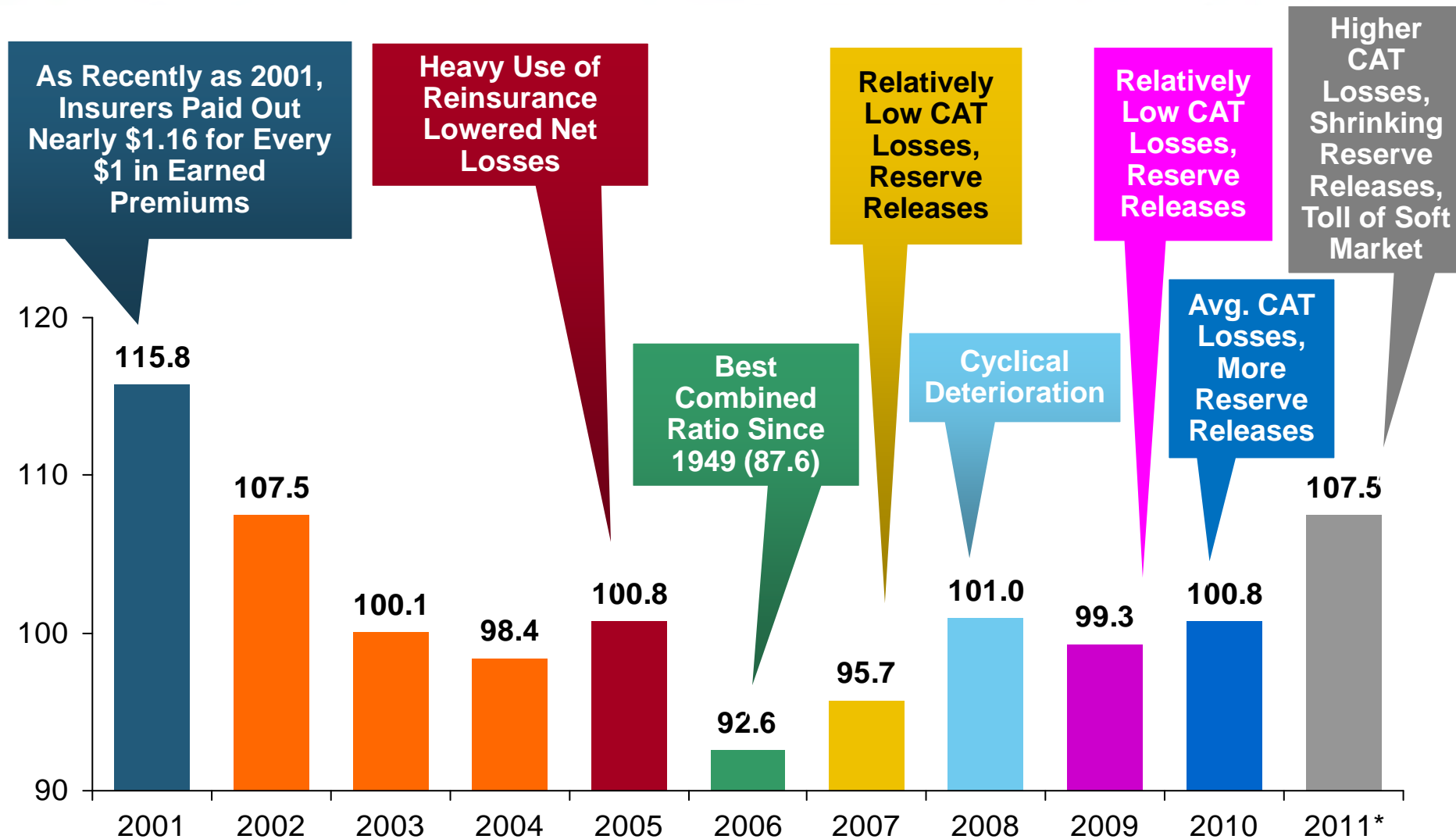
Do the Property Catastrophe Events of 2011 Impact Casualty Markets?

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

1. UNDERWRITING

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

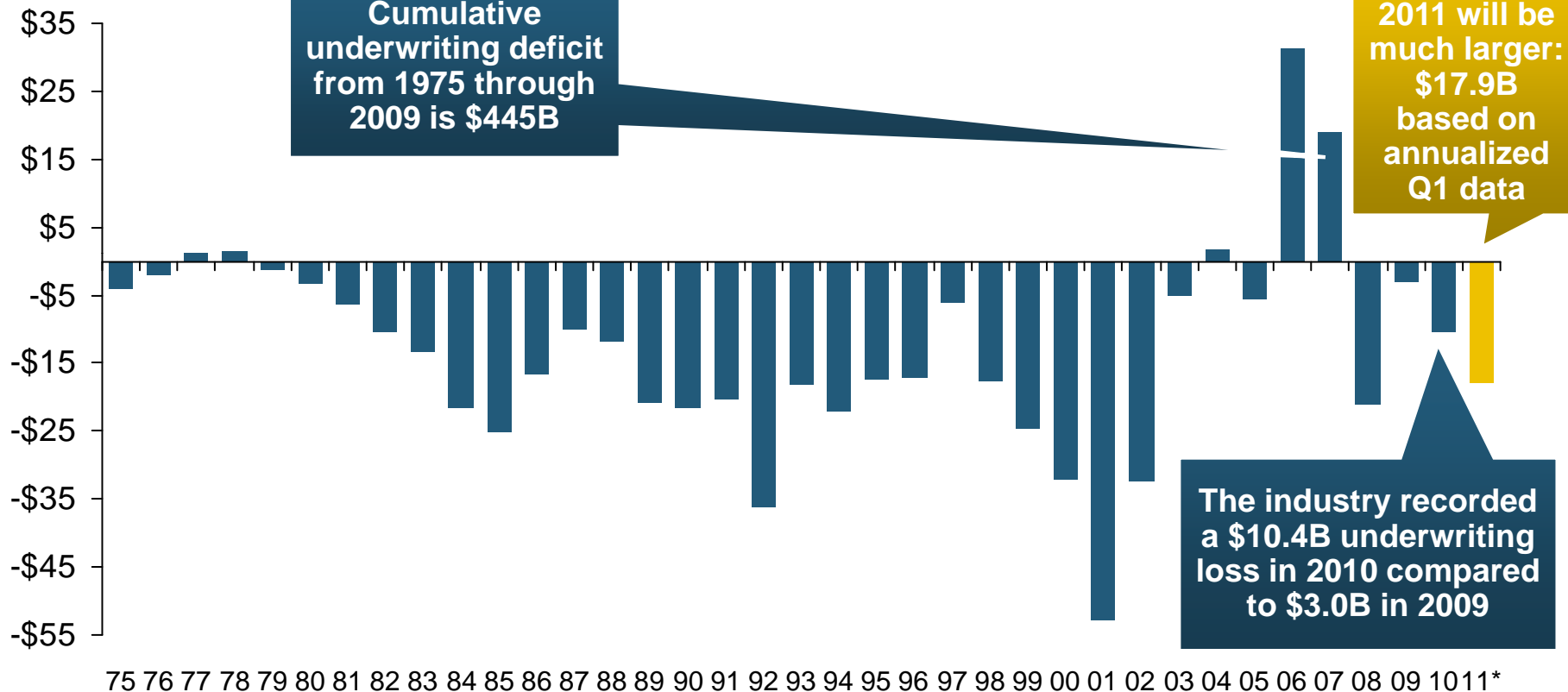
P/C Insurance Industry Combined Ratio, 2001–2011:H1*



* Excludes Mortgage & Financial Guaranty insurers 2008--2011. Including M&FG, 2008=105.1, 2009=100.7, 2010=102.4, 2011=109.1
Sources: A.M. Best, ISO.; III Estimated for 2011:H1 (Q1 actual ex-M&FG was 102.2).

Underwriting Gain (Loss) 1975–2011*

(\$ Billions)



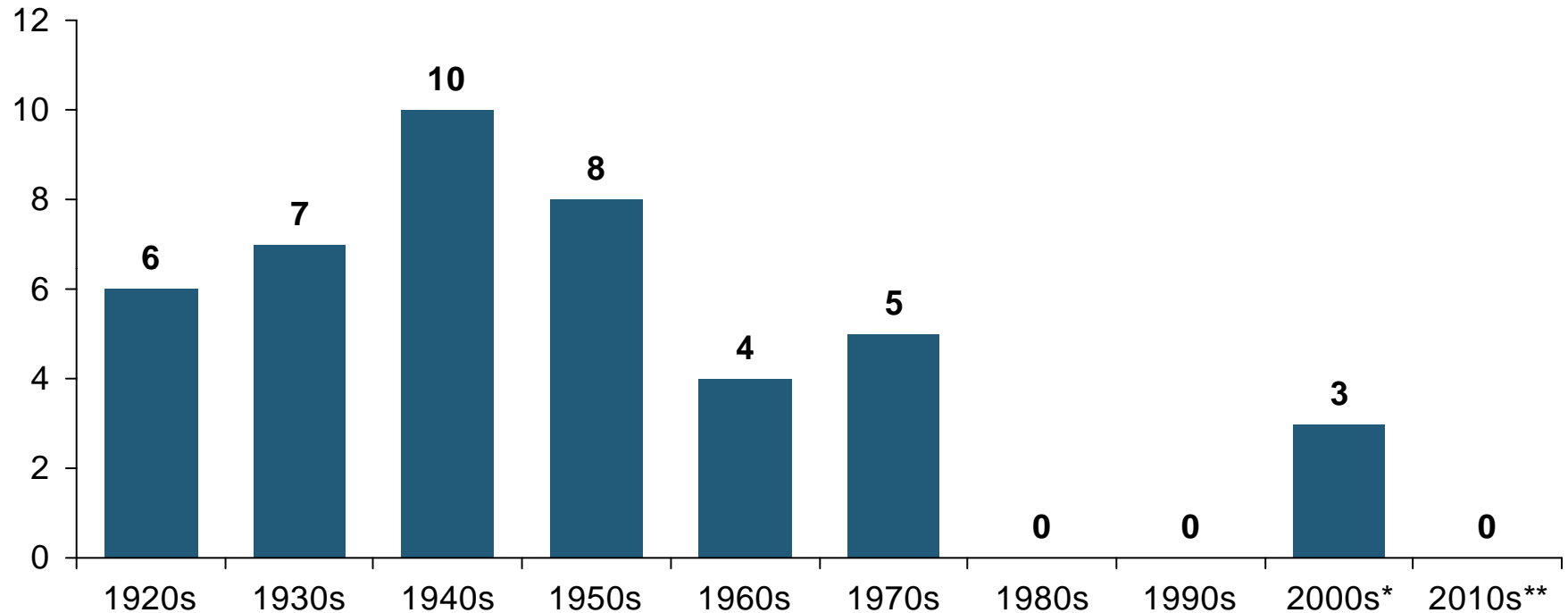
**Large Underwriting Losses Are *NOT* Sustainable
in Current Investment Environment**

* Includes mortgage and financial guaranty insurers in all years. 2011 figure is annualized based on actual Q1 underwriting losses of \$4.463 billion.

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

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

Number of Years with Underwriting Profits



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

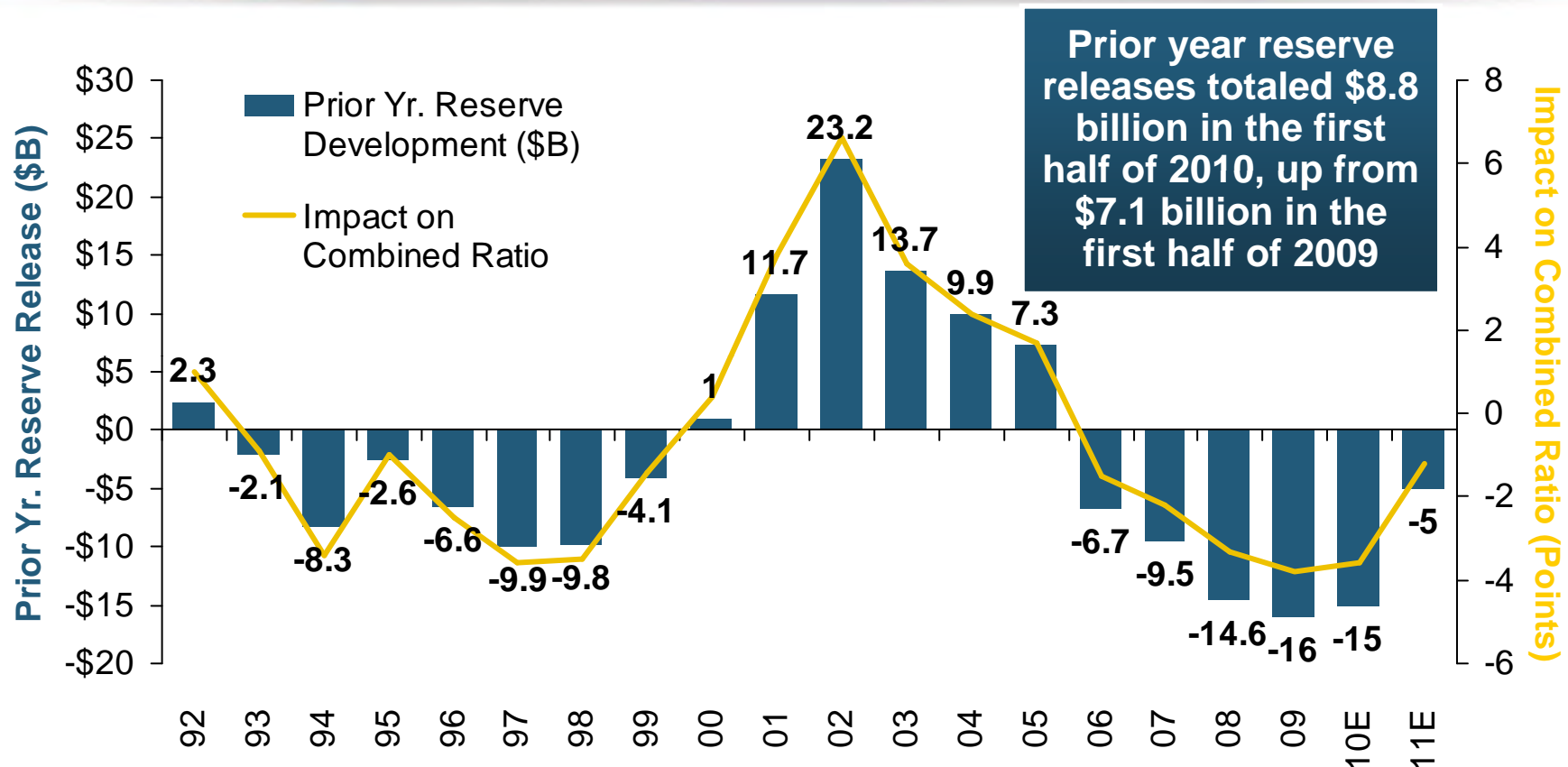
total to 4 years with an underwriting profit.

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

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

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

P/C Reserve Development, 1992–2011E



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

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

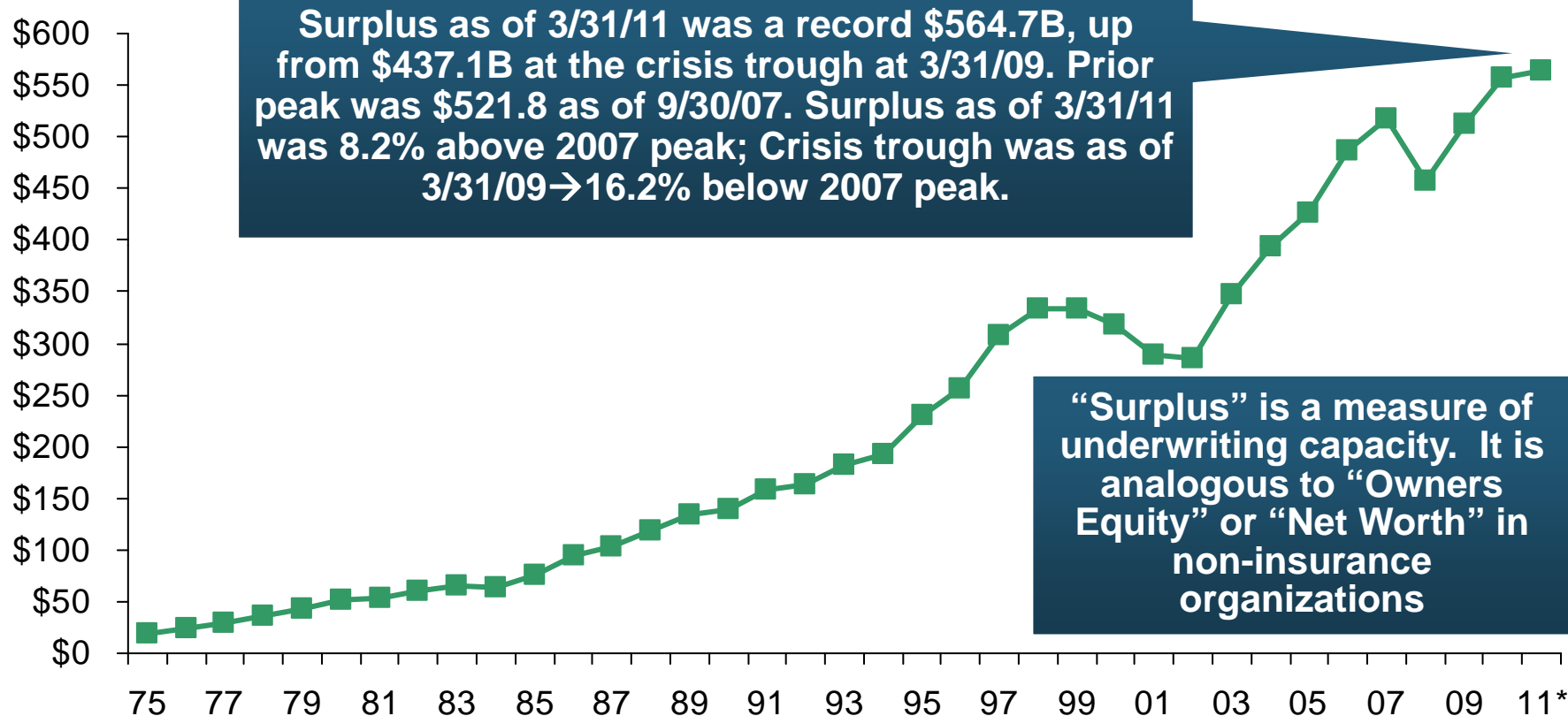
Sources: Barclay's Capital; A.M. Best.

2. SURPLUS/CAPITAL/CAPACITY

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

US Policyholder Surplus: 1975–2011*

(\$ Billions)

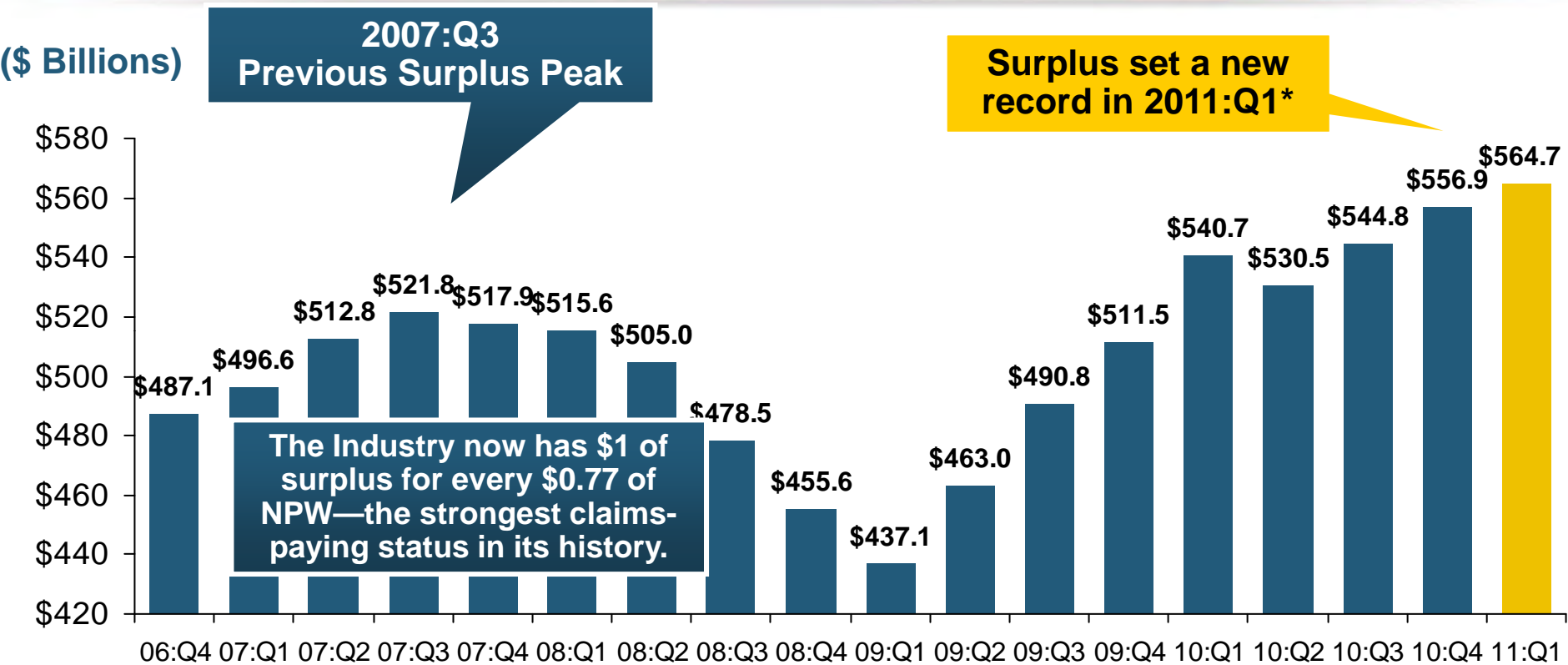


The Premium-to-Surplus Ratio Stood at \$0.77:\$1 as of 3/31/11, A Near Record Low (at Least in Recent History)**

* As of 3/31/11.

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

Policyholder Surplus, 2006:Q4–2011:Q1



Quarterly Surplus Changes Since 2007:Q3 Peak

09:Q1: -\$84.7B (-16.2%)

09:Q2: -\$58.8B (-11.2%)

09:Q3: -\$31.0B (-5.9%)

09:Q4: -\$10.3B (-2.0%)

10:Q1: +\$18.9B (+3.6%)

10:Q2: +\$8.7B (+1.7%)

10:Q3: +\$23.0B (+4.4%)

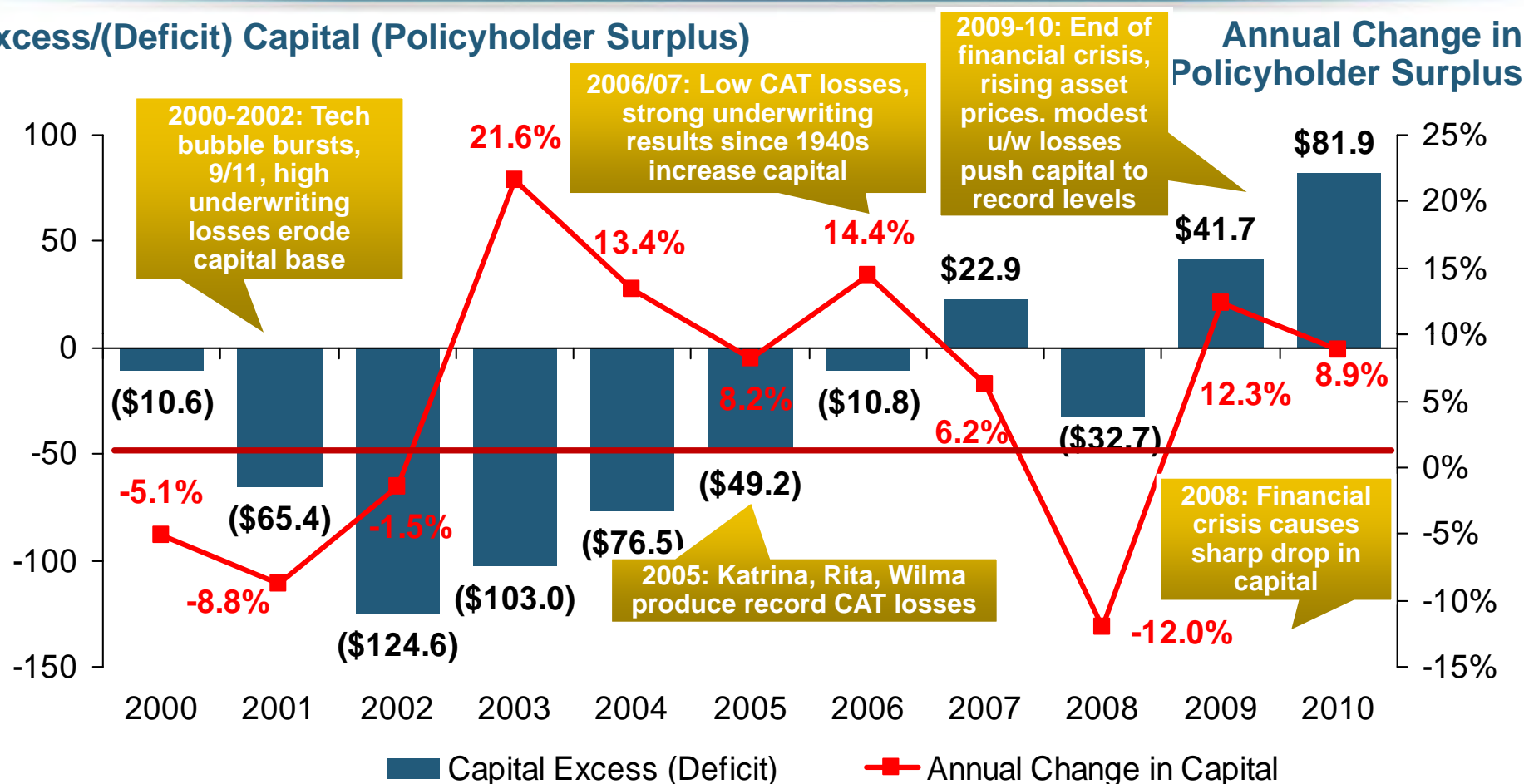
10:Q4: +\$35.1B (+6.7%)

11:Q1: +\$42.9B (+8.2%)

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

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

Excess/(Deficit) Capital (Policyholder Surplus)



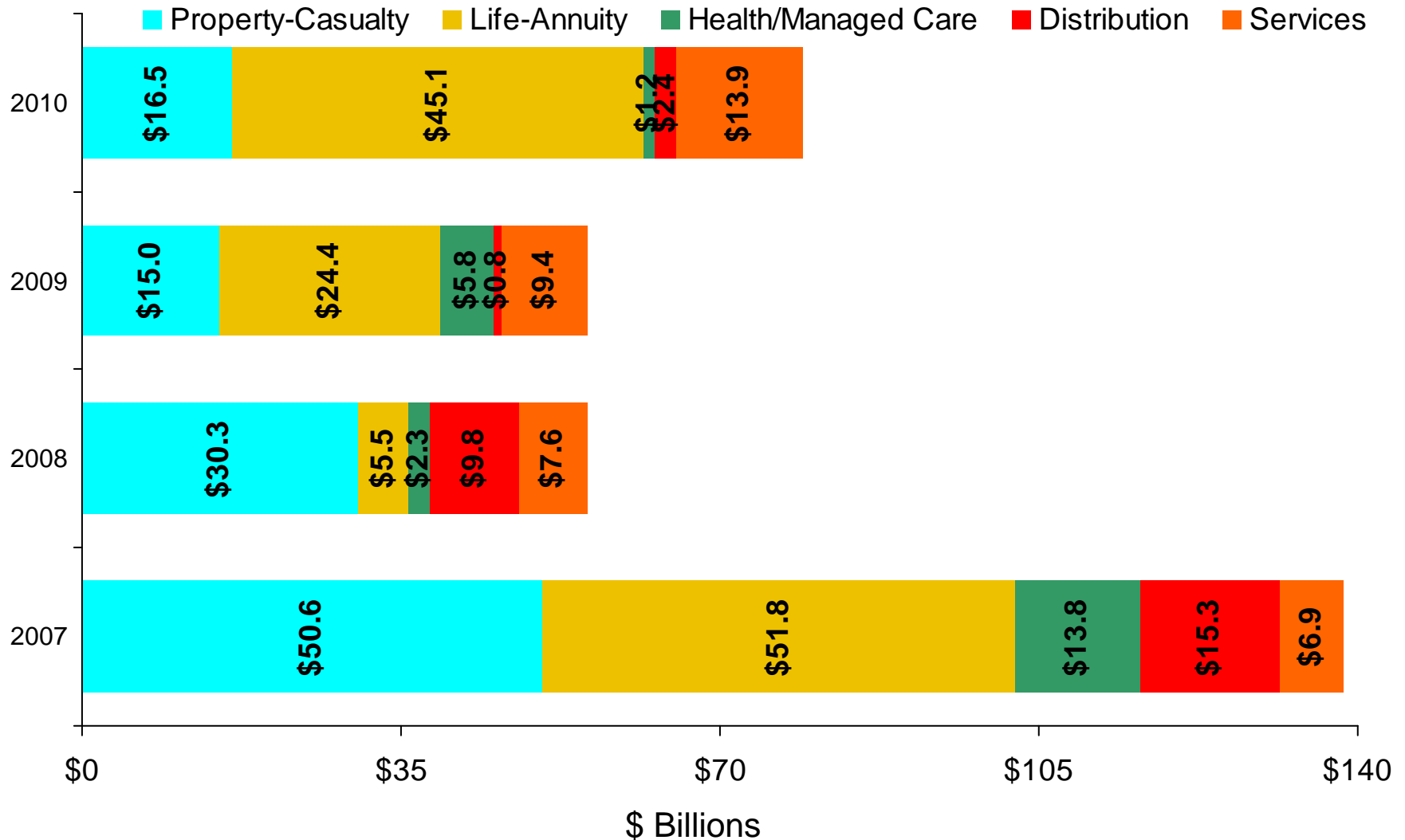
Record Policyholder Surplus (Capital) Has Resulted Significant Excess Capital in the P/C Insurance Sector As of Year End 2010. Deteriorating Underwriting Losses, Higher CAT Activity, More Modest Market Returns Will Likely Shrink Excess Capital in 2011.

Note: The assumption of a 0.9:1 P/S ratio is derived from a Feb. 2011 announcement by Advisen, Ltd., that the US P/C insurance industry has \$74 billion in excess capital. The implied P/S ratio (calculated by III) is 0.88:1, which was rounded to 0.9:1.

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

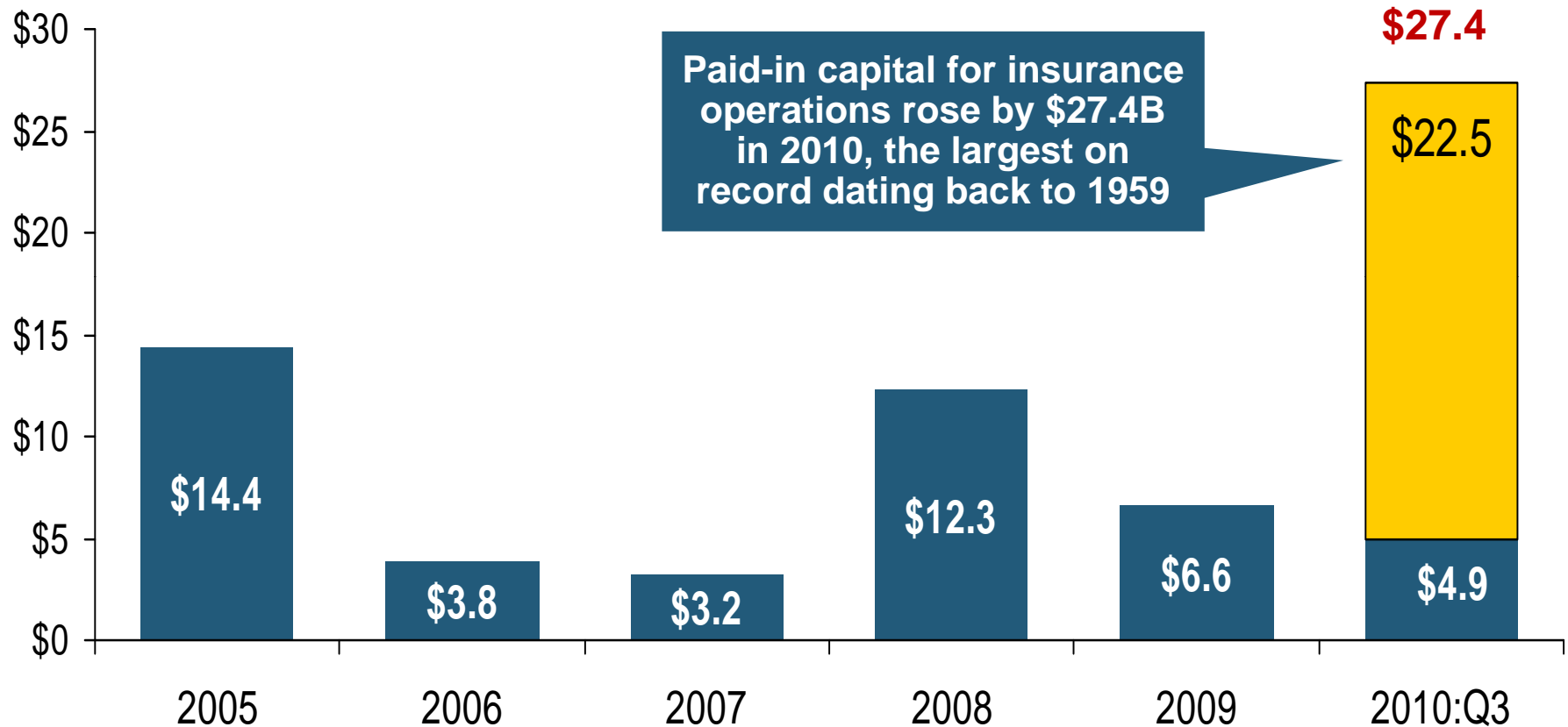
* Net Premiums Written

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



Paid-in Capital, 2005–2010

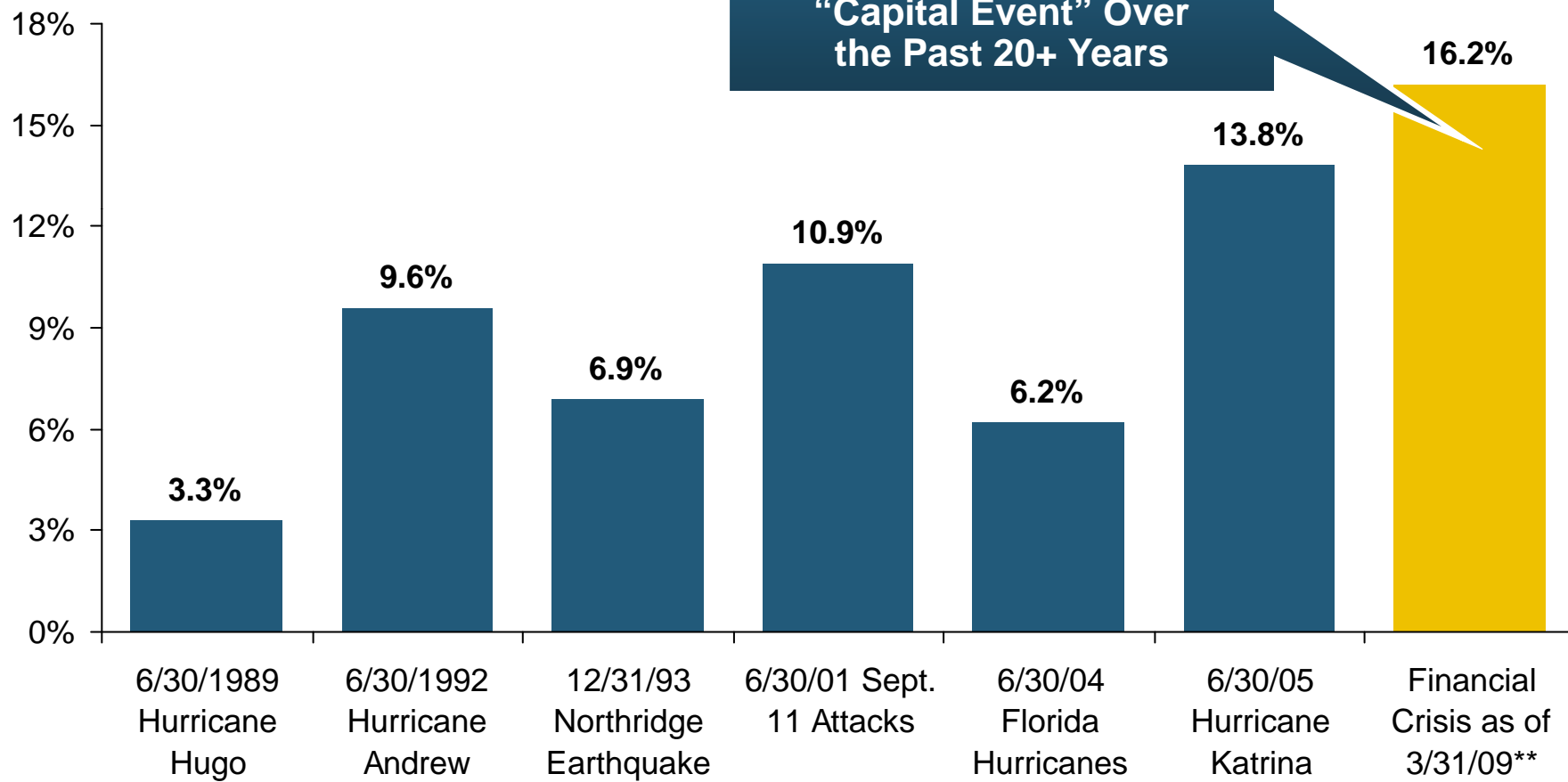
(\$ Billions)



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

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

(Percent)



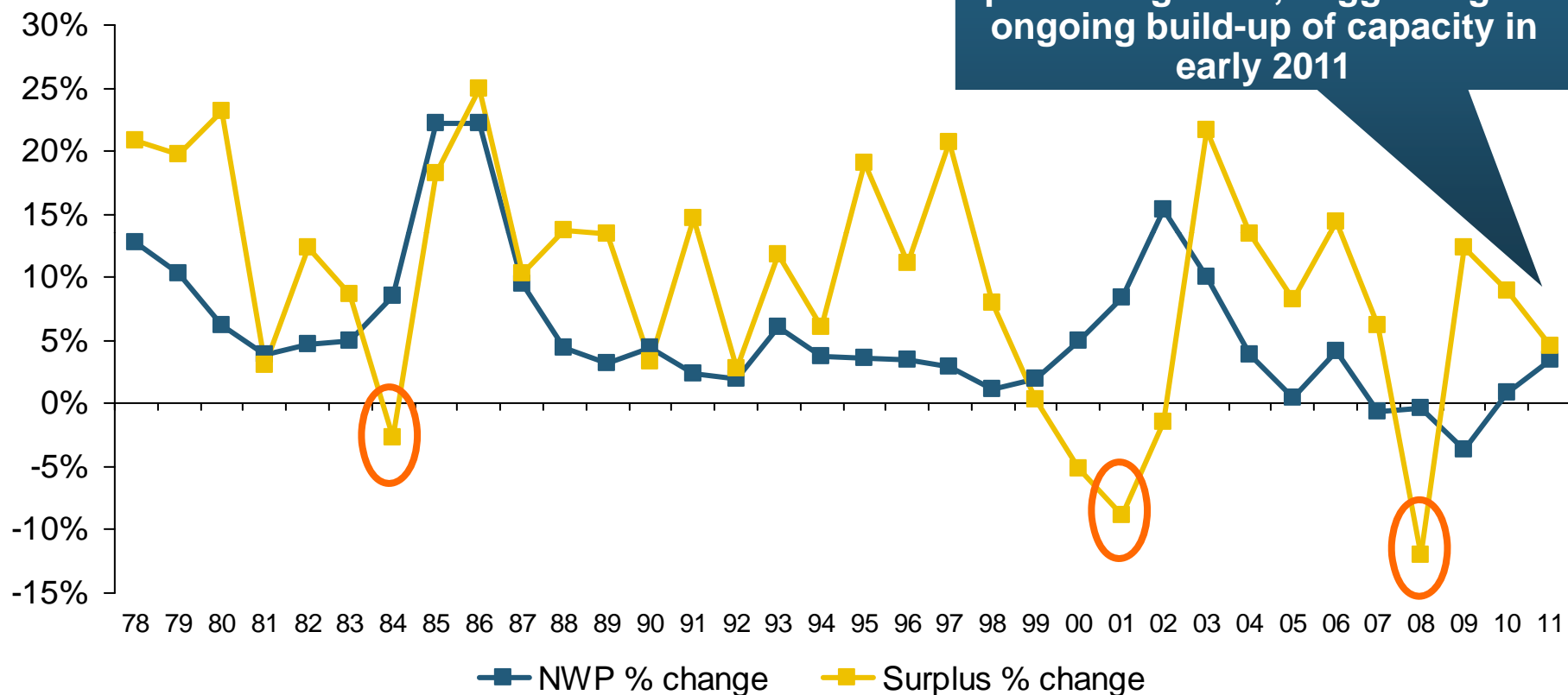
* Ratio is for end-of-quarter surplus immediately prior to event. Date shown is end of quarter prior to event

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

Source: PCS; Insurance Information Institute

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

(Percent)

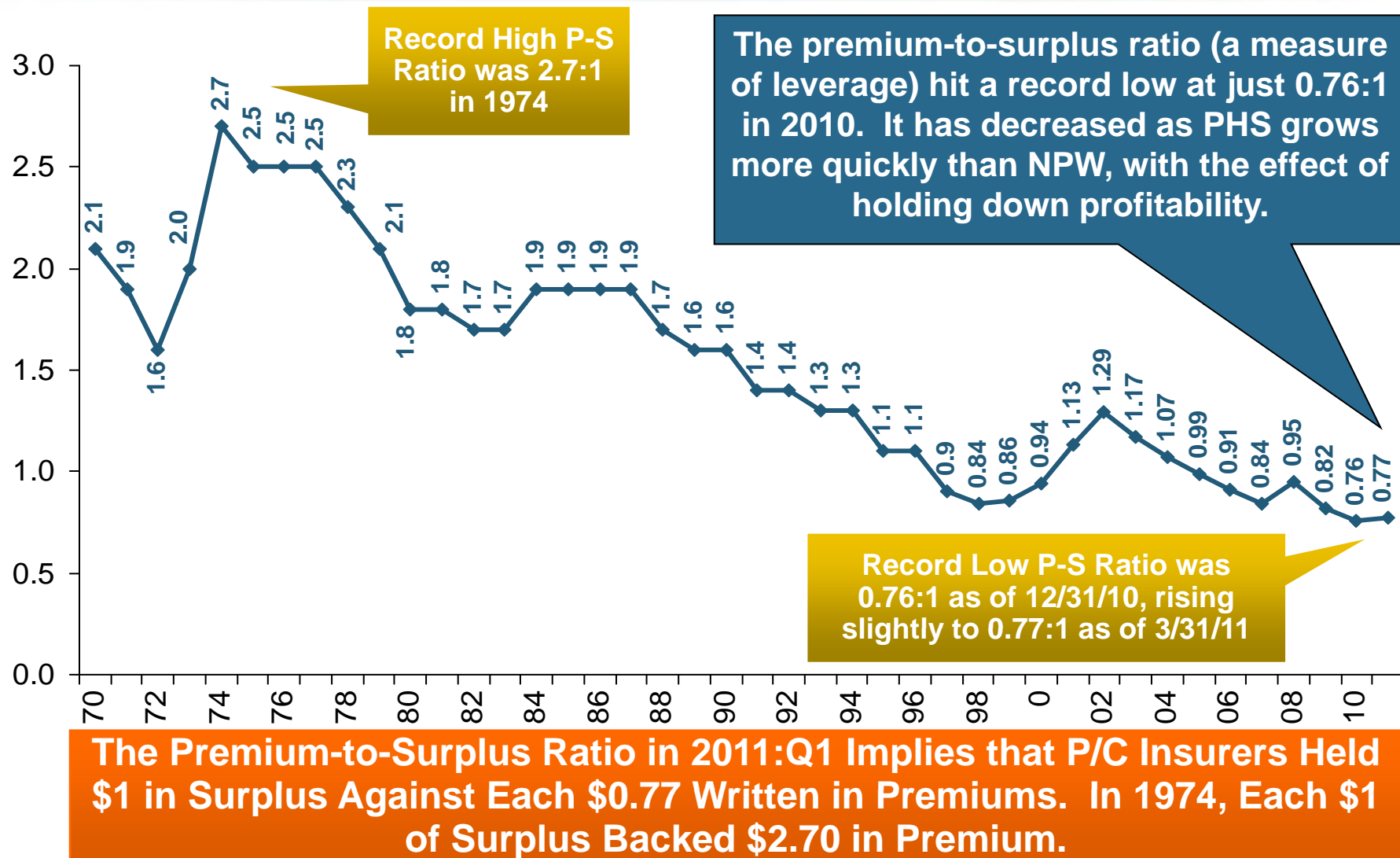


Sharp Decline in Capacity is a Necessary but Not Sufficient Condition for a True Hard Market

* 2011 NWP and Surplus figures are % changes as of Q1:11 vs. Q1:10.

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

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



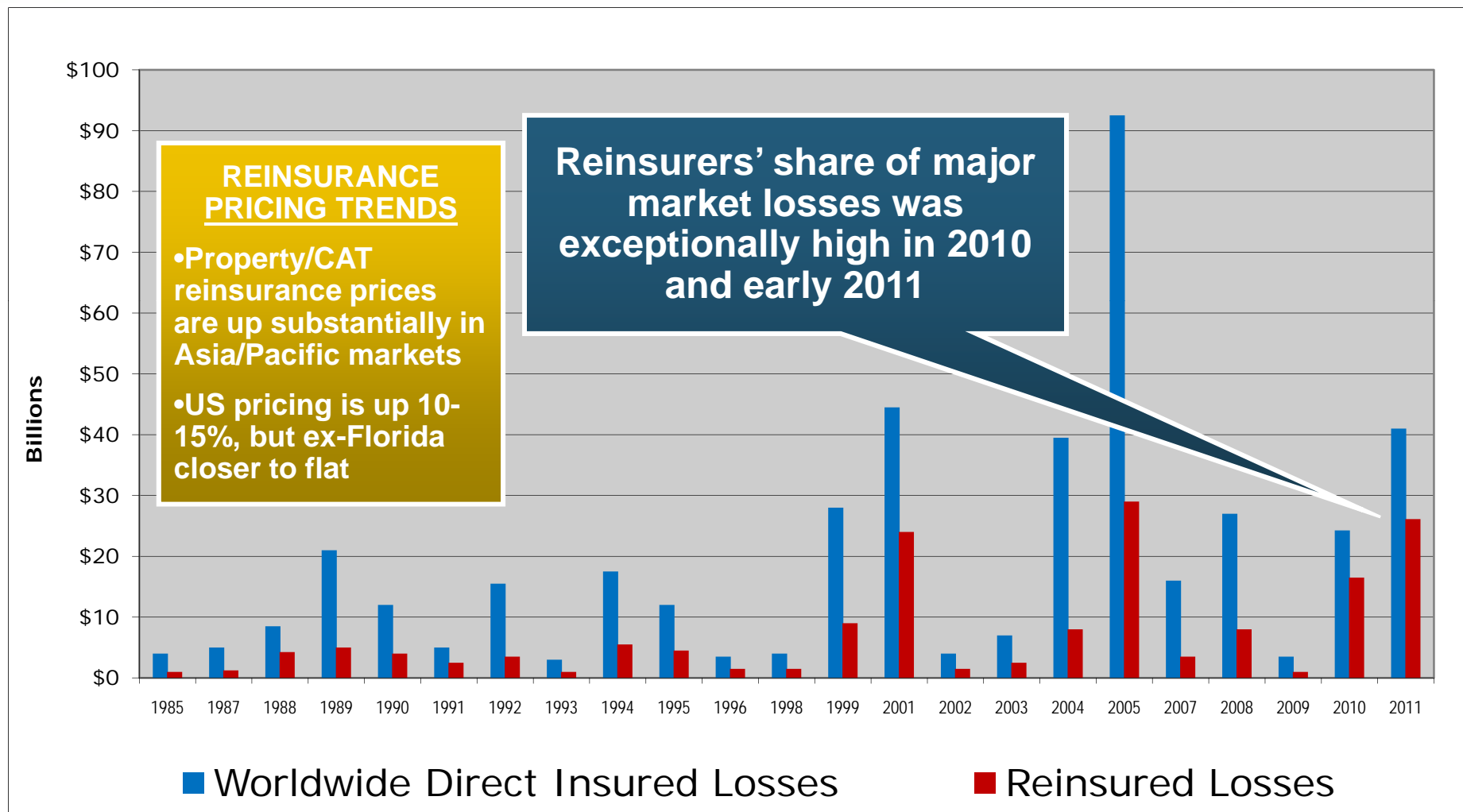
*2011 data are as of 3/31/11.

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

3. REINSURANCE MARKET CONDITIONS

**Has Record Global
Catastrophes Activity
Erased Enough Capacity
to Turn Markets?**

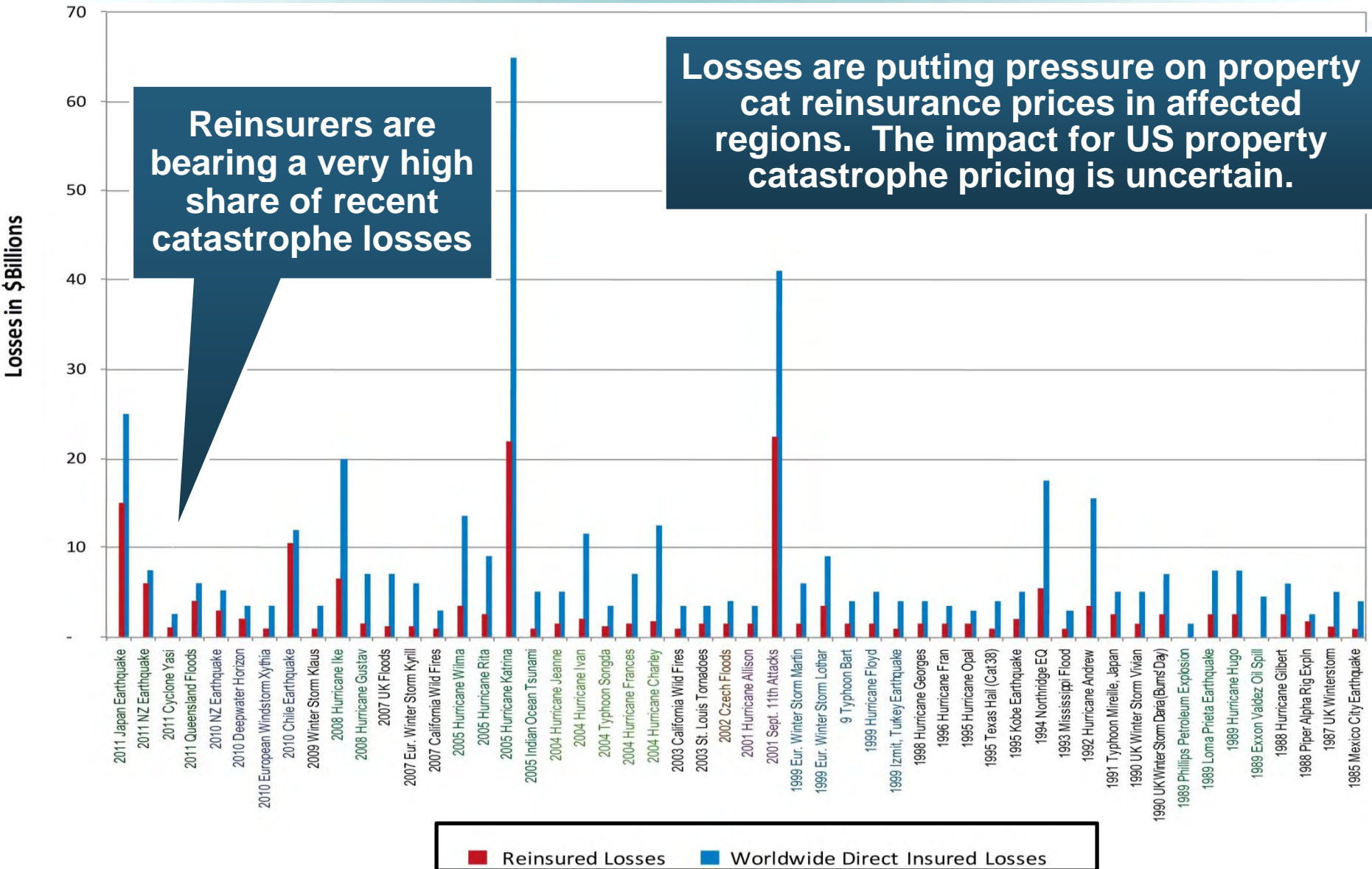
Significant Market Losses, 1985-2011*



Source: Holborn; RAA.

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

Significant Market Losses by Event, 1985-2011*



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

Outlook for the 2011 Atlantic Hurricane Season

**If Expected Above Average
Activity Produces Costly
Landfalls, Reinsurance
Markets Could Harden
Significantly**

Outlook for 2011 Hurricane Season: 75% More Active Than Average

	Average*	2005 (Katrina Year)	2011F
Named Storms	9.6	28	16
Named Storm Days	49.1	115.5	80
Hurricanes	5.9	14	9
Hurricane Days	24.5	47.5	35
Intense Hurricanes	2.3	7	5
Intense Hurricane Days	5.0	7	10
Accumulated Cyclone Energy	96.1	NA	160
Net Tropical Cyclone Activity	100%	275%	175%

*Average over the period 1950-2000.

Source: Dr. Philip Klotzbach and Dr. William Gray, Colorado State University, June 1, 2011.

Probability of Major Hurricane Landfall (CAT 3, 4, 5) in 2011

	Average*	2011F
Entire US Coast	52%	72%
US East Coast Including Florida Peninsula	31%	48%
Gulf Coast from FL Panhandle to Brownsville, TX	30%	47%
<i>ALSO...Above-Average Major Hurricane Landfall Risk in Caribbean for 2011 (61% vs. 42%)</i>		

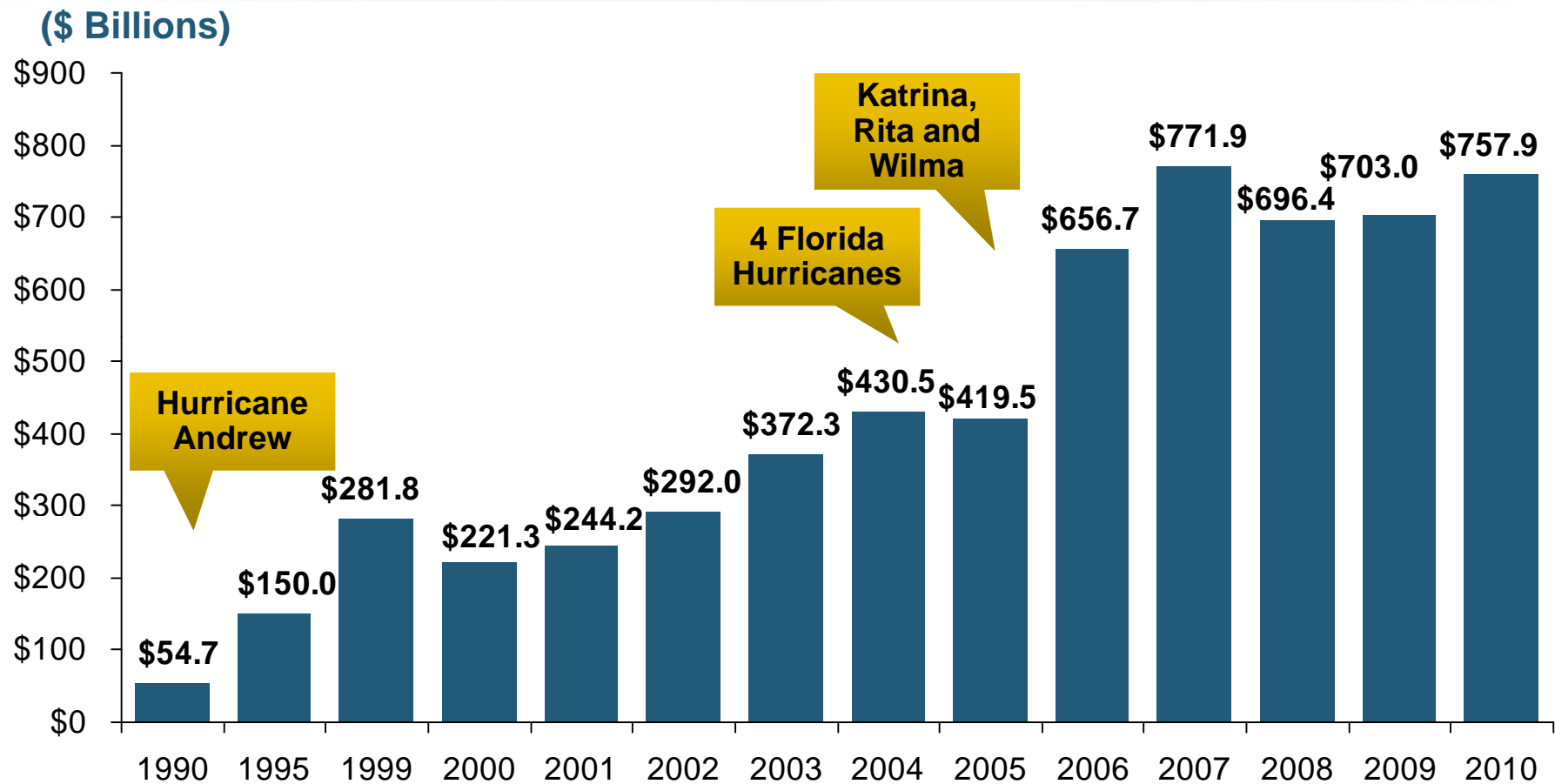
*Average over the period 1950-2000.

Source: Dr. Philip Klotzbach and Dr. William Gray, Colorado State University, June 1, 2011.

US Property Residual Markets Remain Under Strain

**Most States Fail to Address
Their Vulnerabilities to
Catastrophic Coastal Loss**

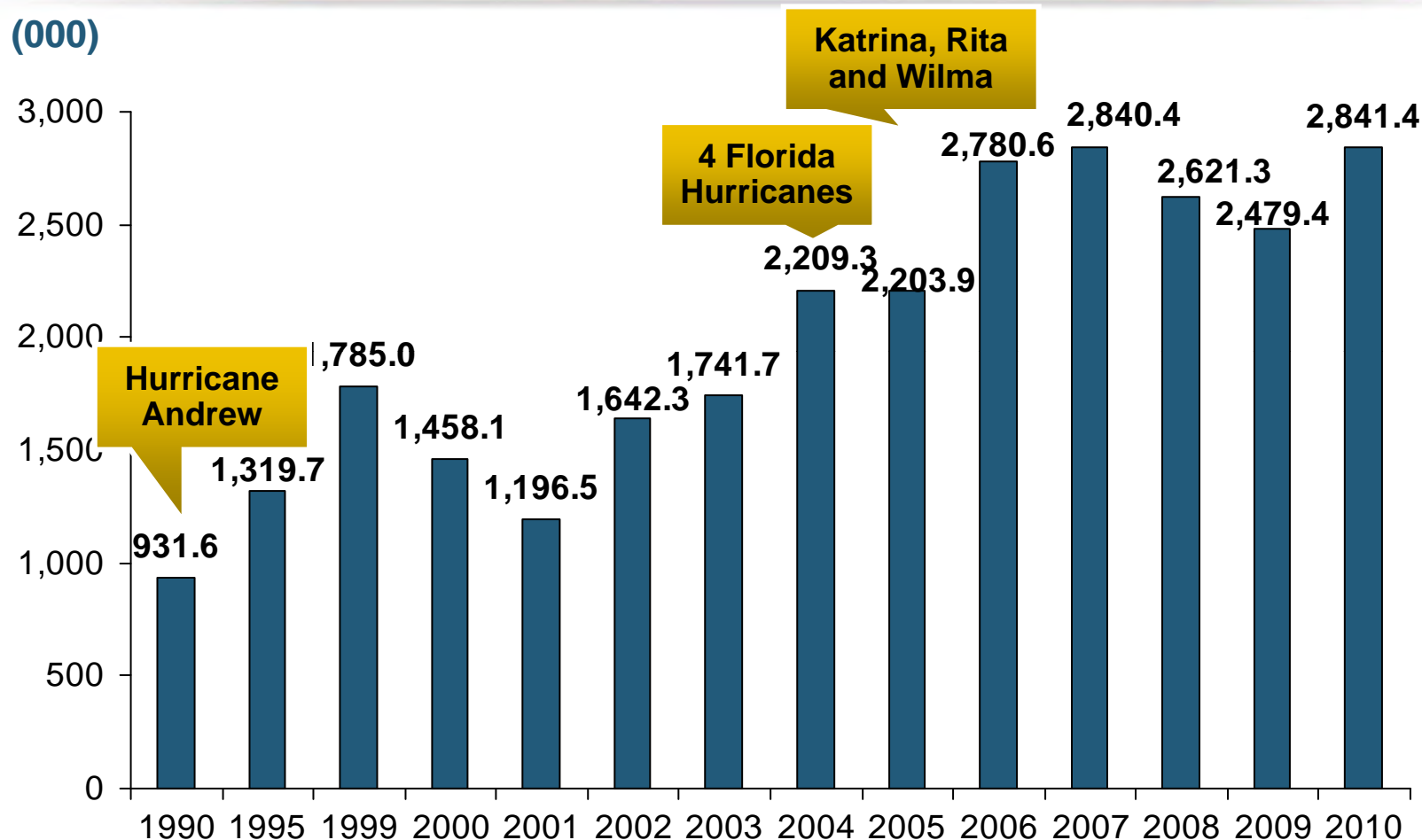
U.S. Residual Market Exposure to Loss (\$ Billions)



In the 21-year period between 1990 and 2010, total exposure to loss in the residual market (FAIR & Beach/Windstorm) Plans has surged from \$54.7 billion in 1990 to \$757.9 billion in 2010.

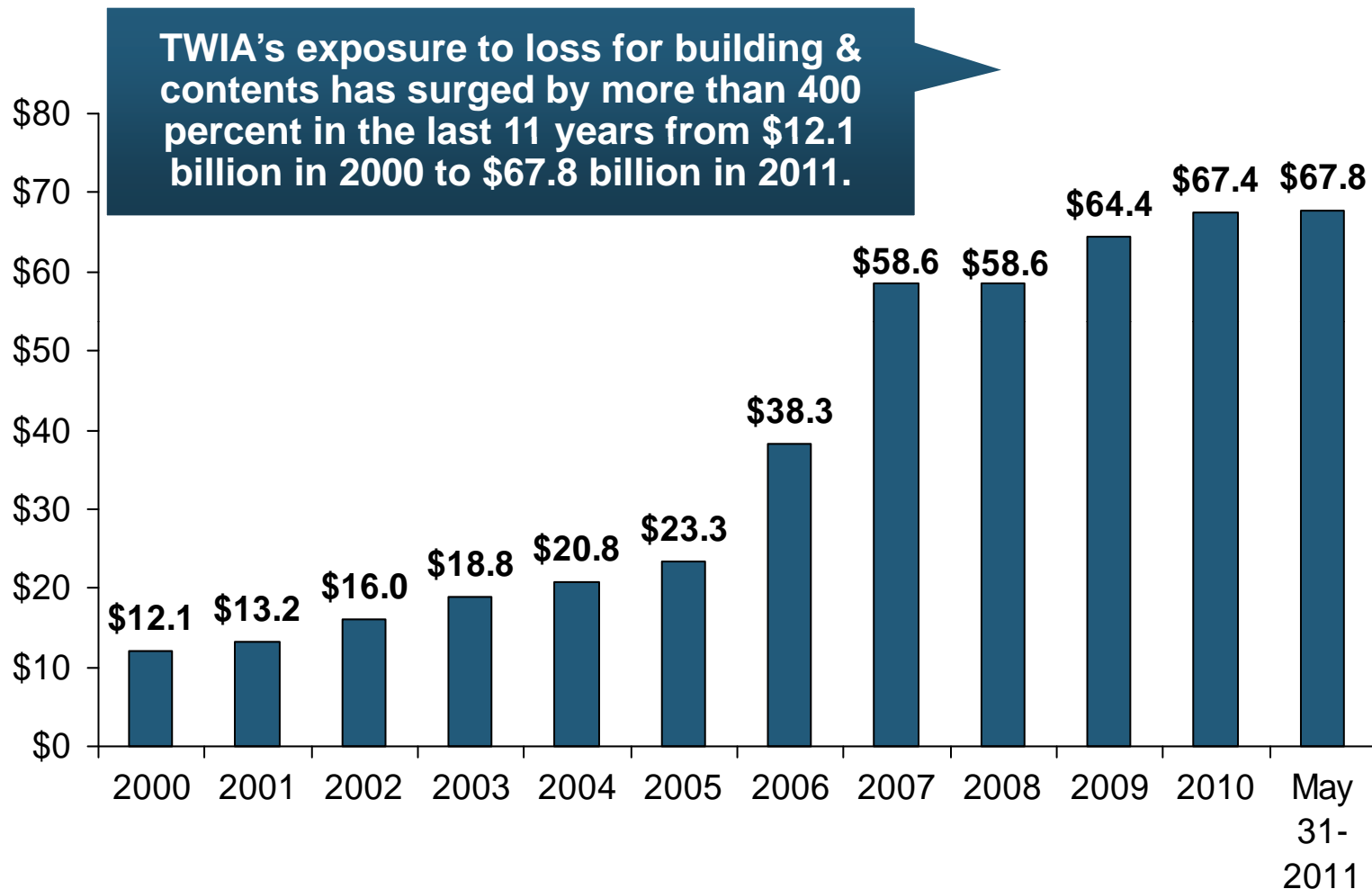
Source: PIPSO; Insurance Information Institute (I.I.I.); <http://www.iii.org/pr/last-resort-2010>.

U.S. Residual Market: Total Policies In-Force (1990-2010) (000)

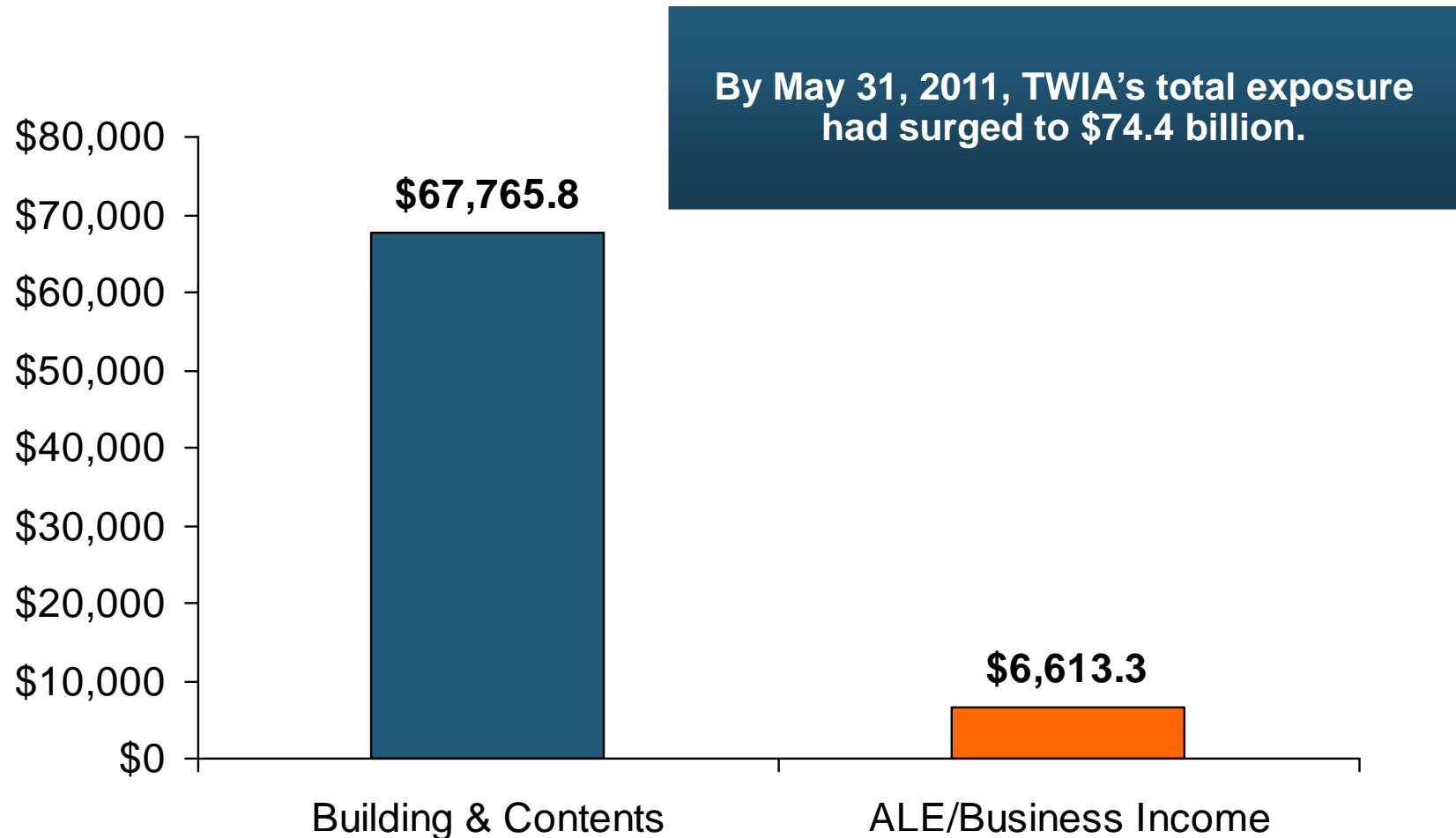


In the 21-year period between 1990 and 2010, the total number of policies in-force in the residual market (FAIR & Beach/Windstorm) Plans has more than tripled.

Texas Windstorm Insurance Association (TWIA): Exposure to Loss (Building & Contents Only) (\$ Billions)



Texas Windstorm Insurance Association (TWIA) Total Exposure to Loss (Millions of Dollars)



Source: TWIA at 05/31/11, Texas Department of Insurance

Texas Windstorm Insurance Association (TWIA) New Financial Structure



Texas Windstorm Insurance Association
Funding as Provided by HB 4409
per Conference Committee Report



New TWIA financing structure made available up to \$2.5 billion to fund losses via three post-event bonding layers. The new structure eliminated the unlimited assessment on TWIA member insurers and does not call for TWIA to purchase reinsurance.

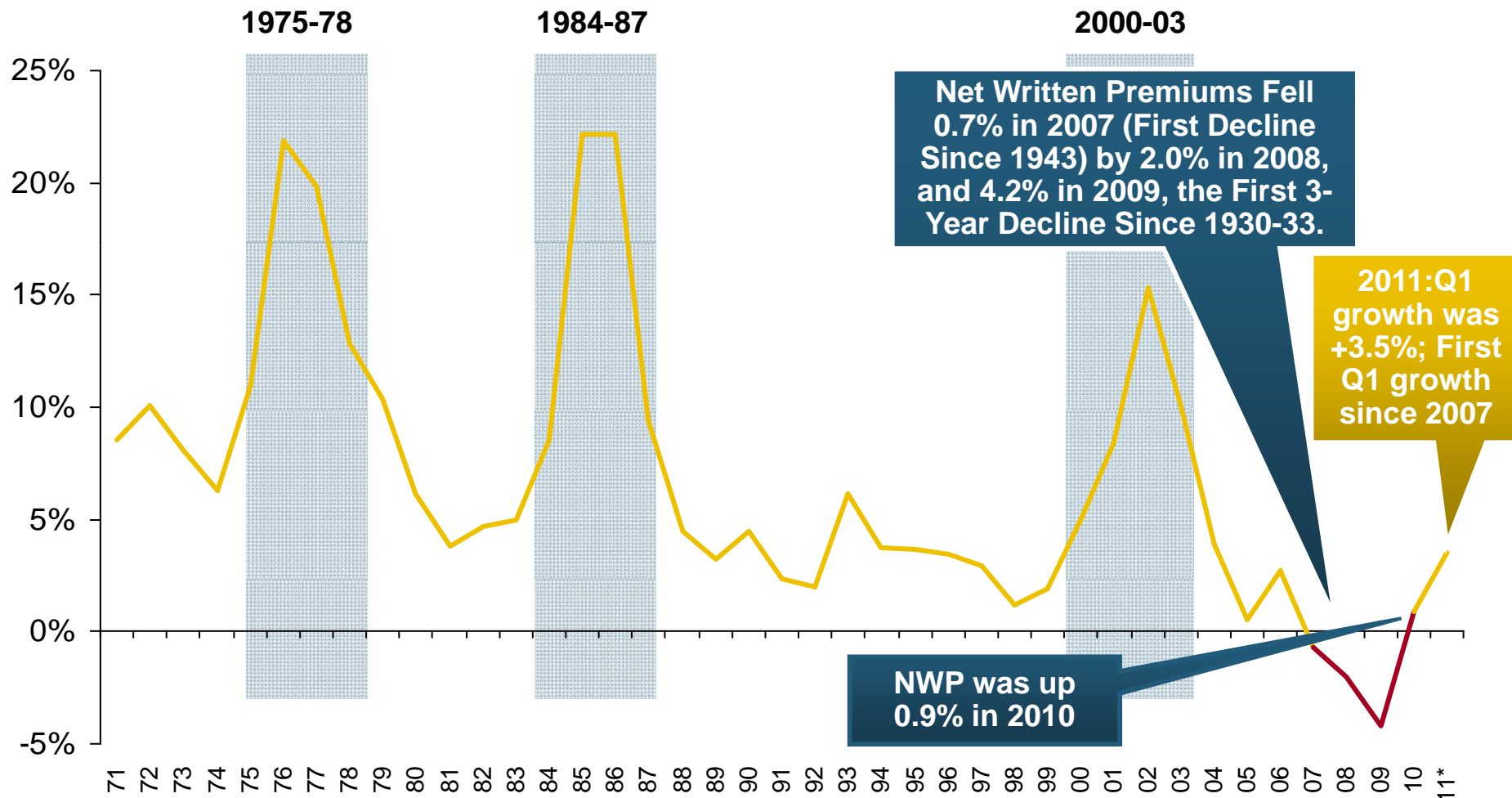
Notes: Storm frequencies based on an average of AIR and RMS modeled losses using TWIA exposures as of 12/31/08
Bond costs estimated based on 10-year terms and 6% interest
Estimated annual costs assume the maximum amount of each class of bonds are issued
Financial instruments, including commercial paper, may be used to pay losses until post-event bonds are issued

4. RENEWED PRICING DISCIPLINE

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

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

(Percent)

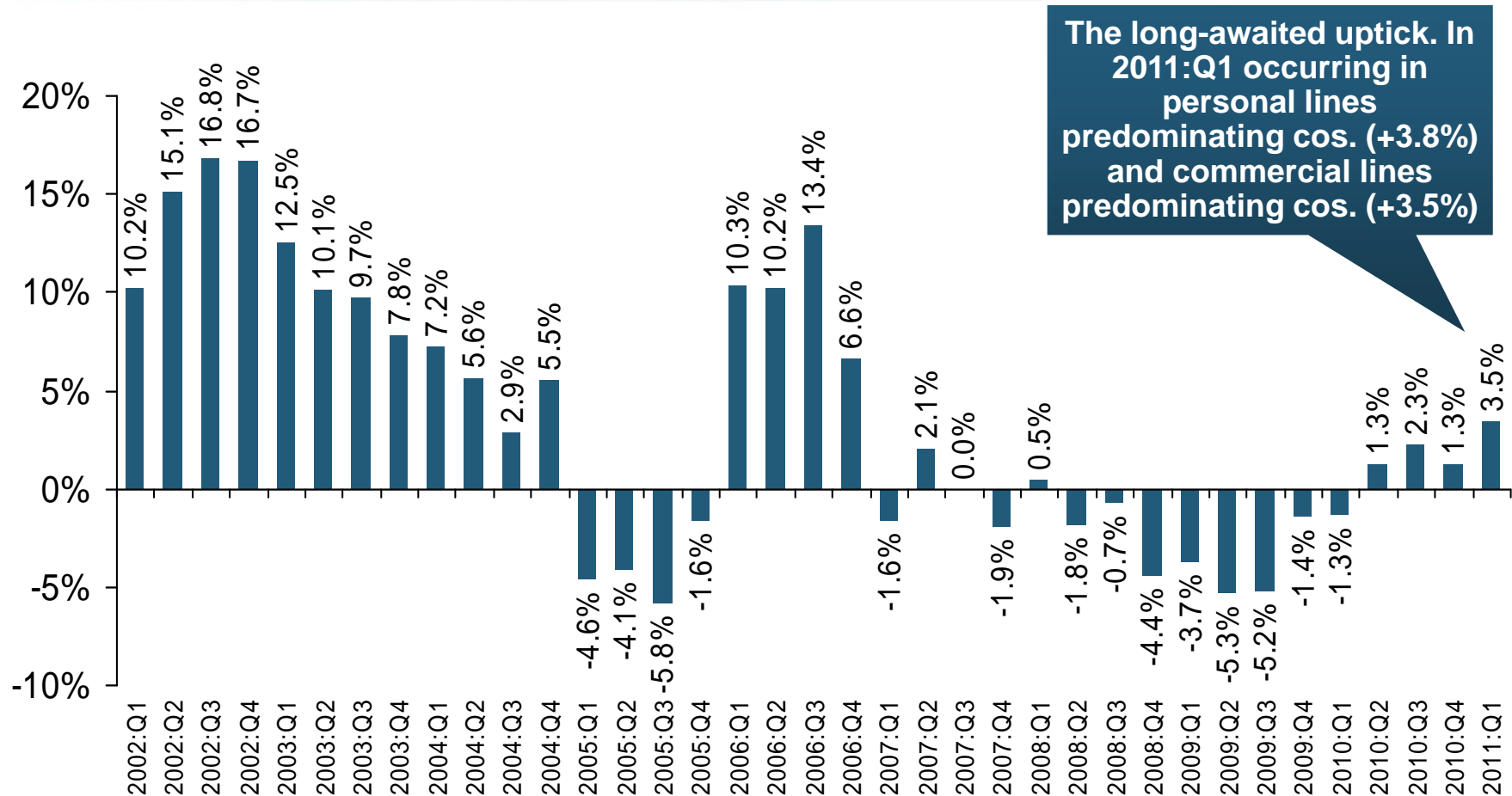


*2011 figure is an estimate based on Q1 data.

Shaded areas denote "hard market" periods

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

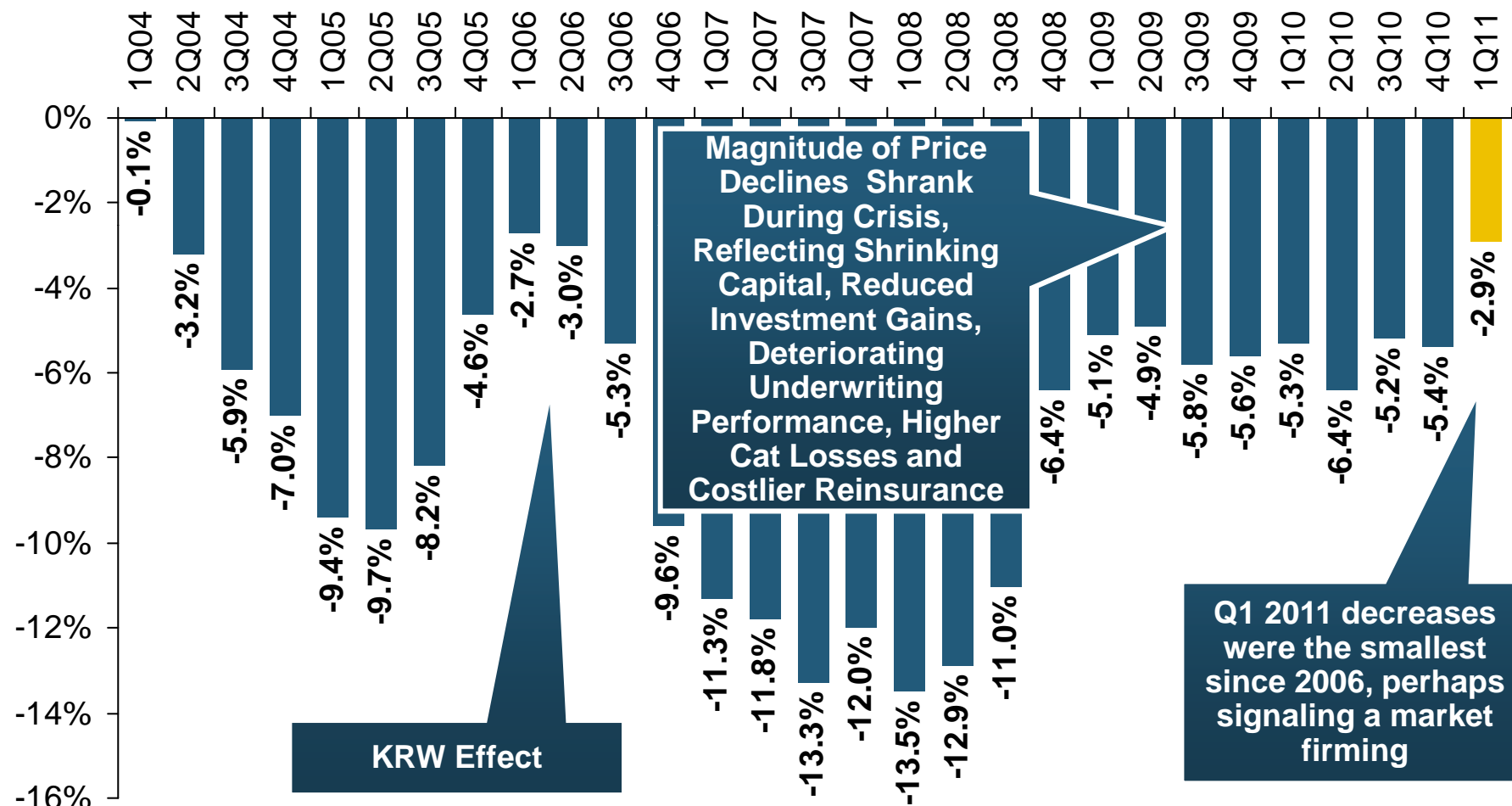
P/C Net Premiums Written: % Change, Quarter vs. Year-Prior Quarter



**Finally! Back-to-back quarters of net written premium growth
(vs. the same quarter, prior year)**

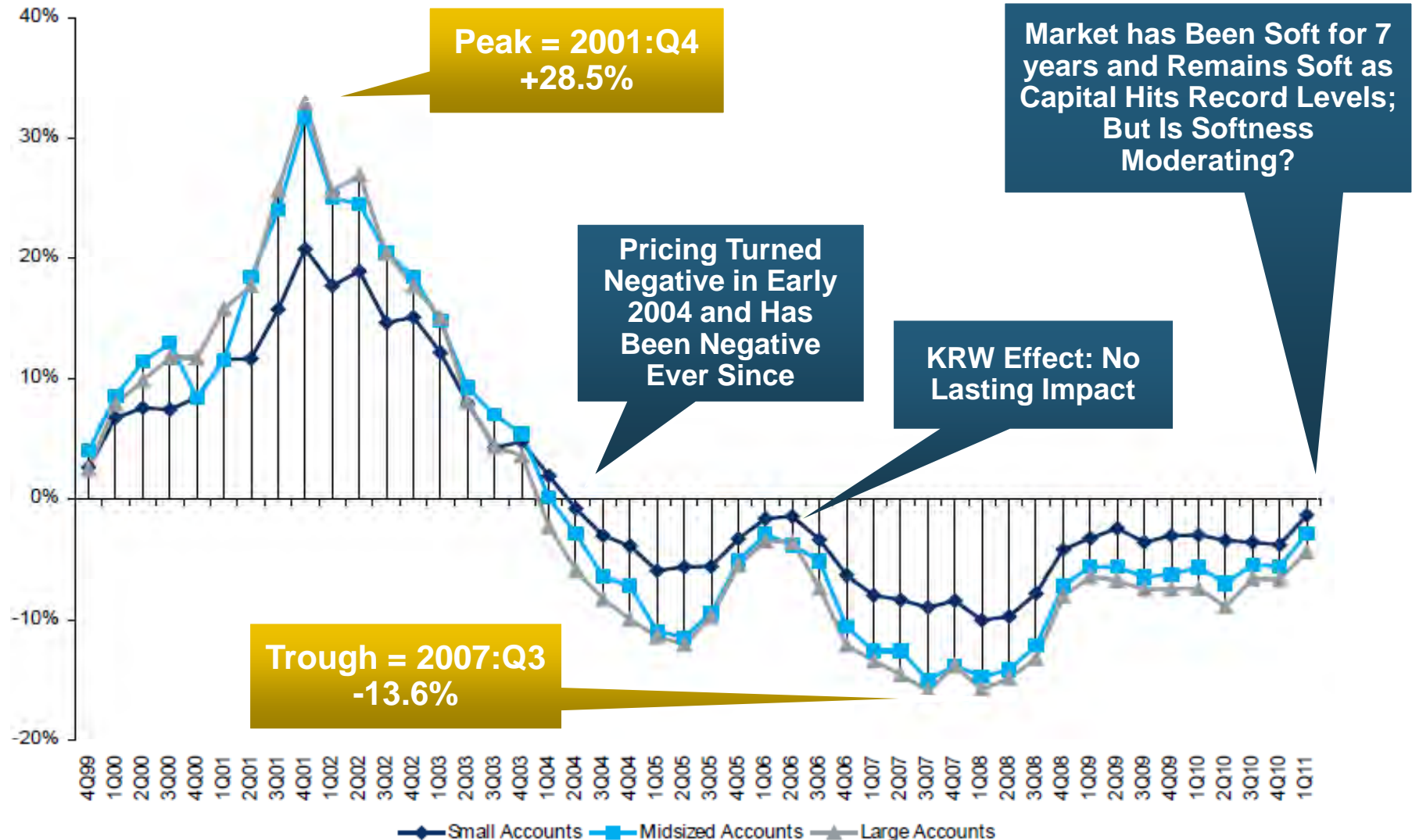
Average Commercial Rate Change, All Lines, (1Q:2004–1Q:2011)

(Percent)



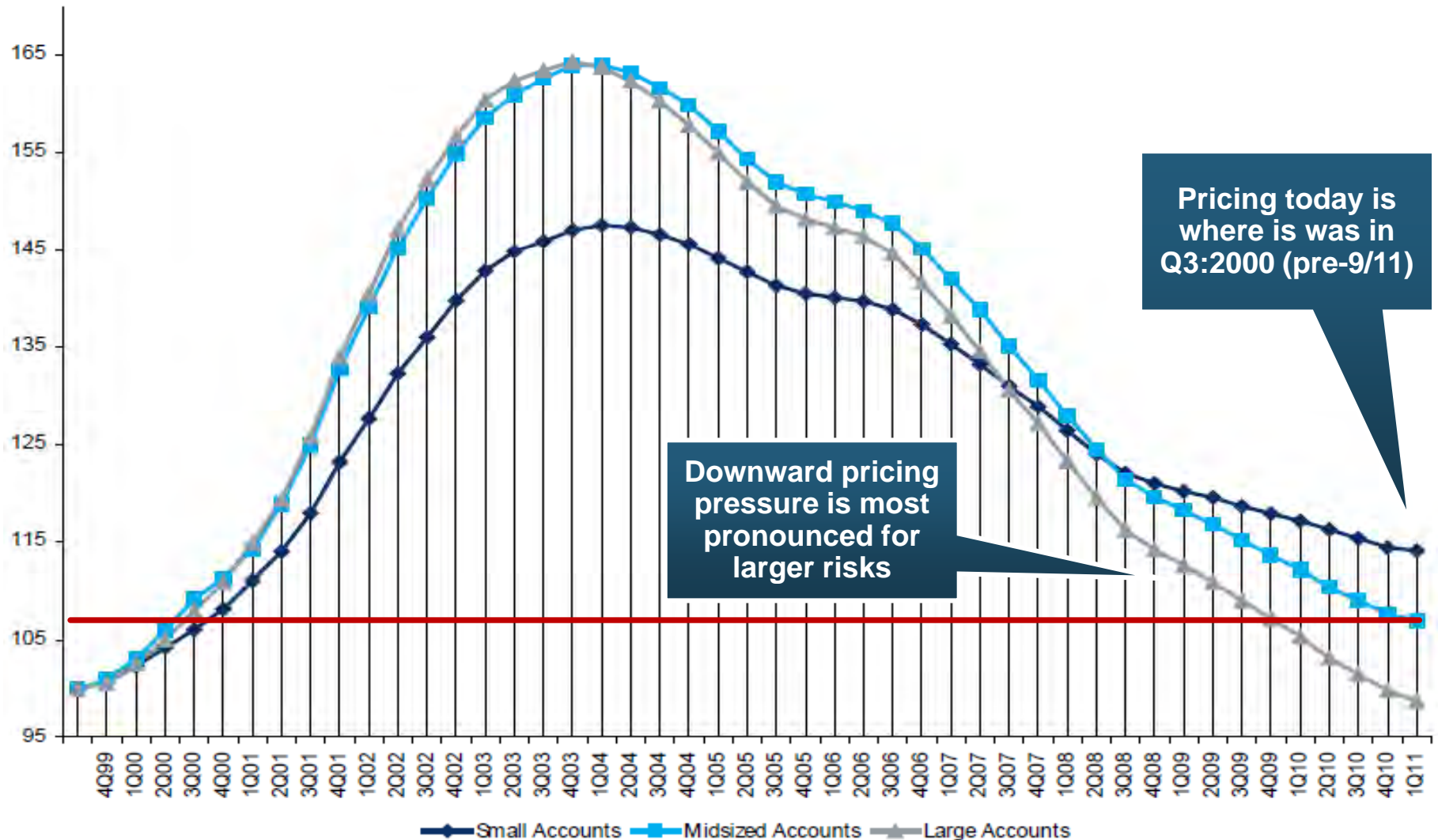
Change in Commercial Rate Renewals, by Account Size: 1999:Q4 to 2011:Q1

Percentage Change (%)

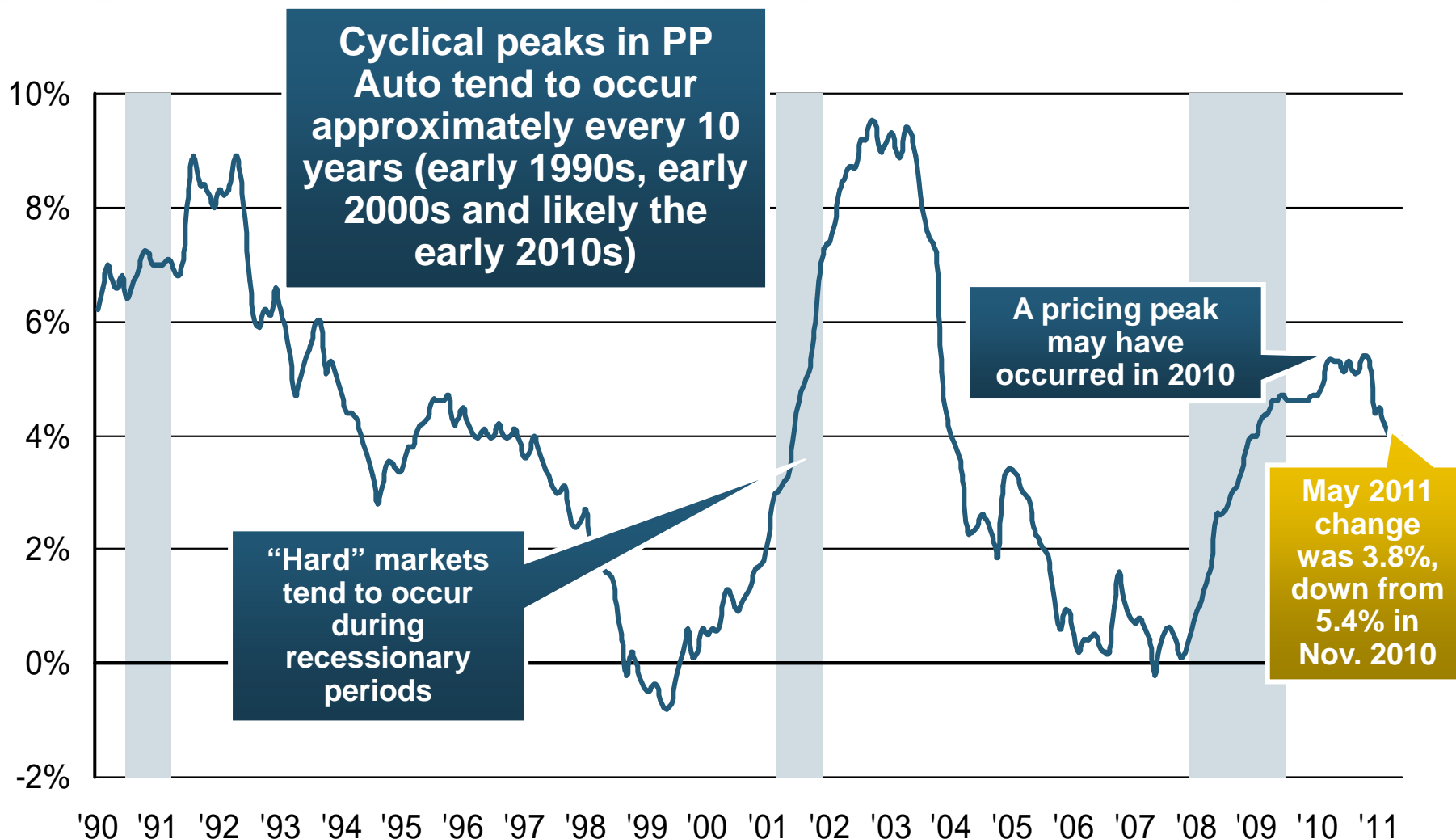


Cumulative Qtrly. Commercial Rate Changes, by Account Size: 1999:Q4 to 2011:Q1

1999:Q4 = 100



Monthly Change* in Auto Insurance Prices, 1991–2011*



*Percentage change from same month in prior year; through May 2011; seasonally adjusted

Note: Recessions indicated by gray shaded columns.

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

Other Cycle-Influencing Factors

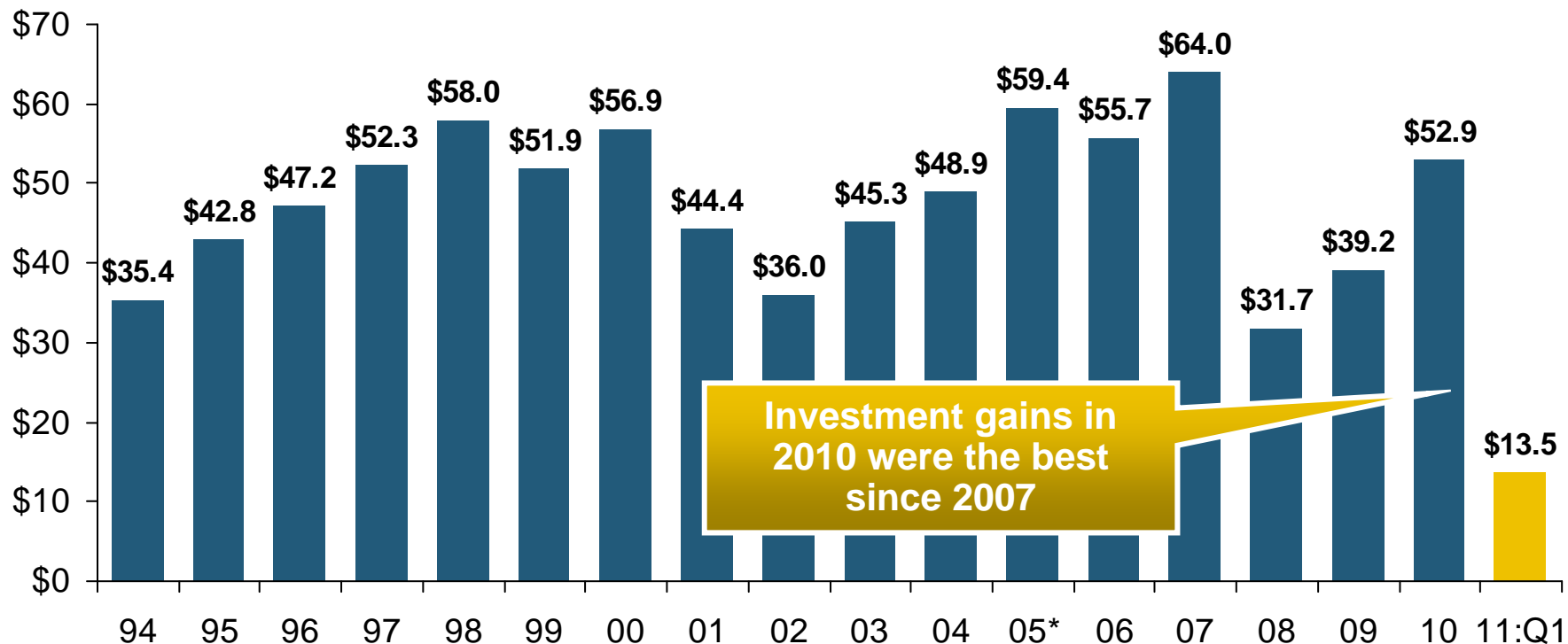
**Could Other Factors Act as
a Catalyst to Turn the
Market?**

INVESTMENTS: THE NEW REALITY

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

Property/Casualty Insurance Industry Investment Gain: 1994–2011:Q1¹

(\$ Billions)



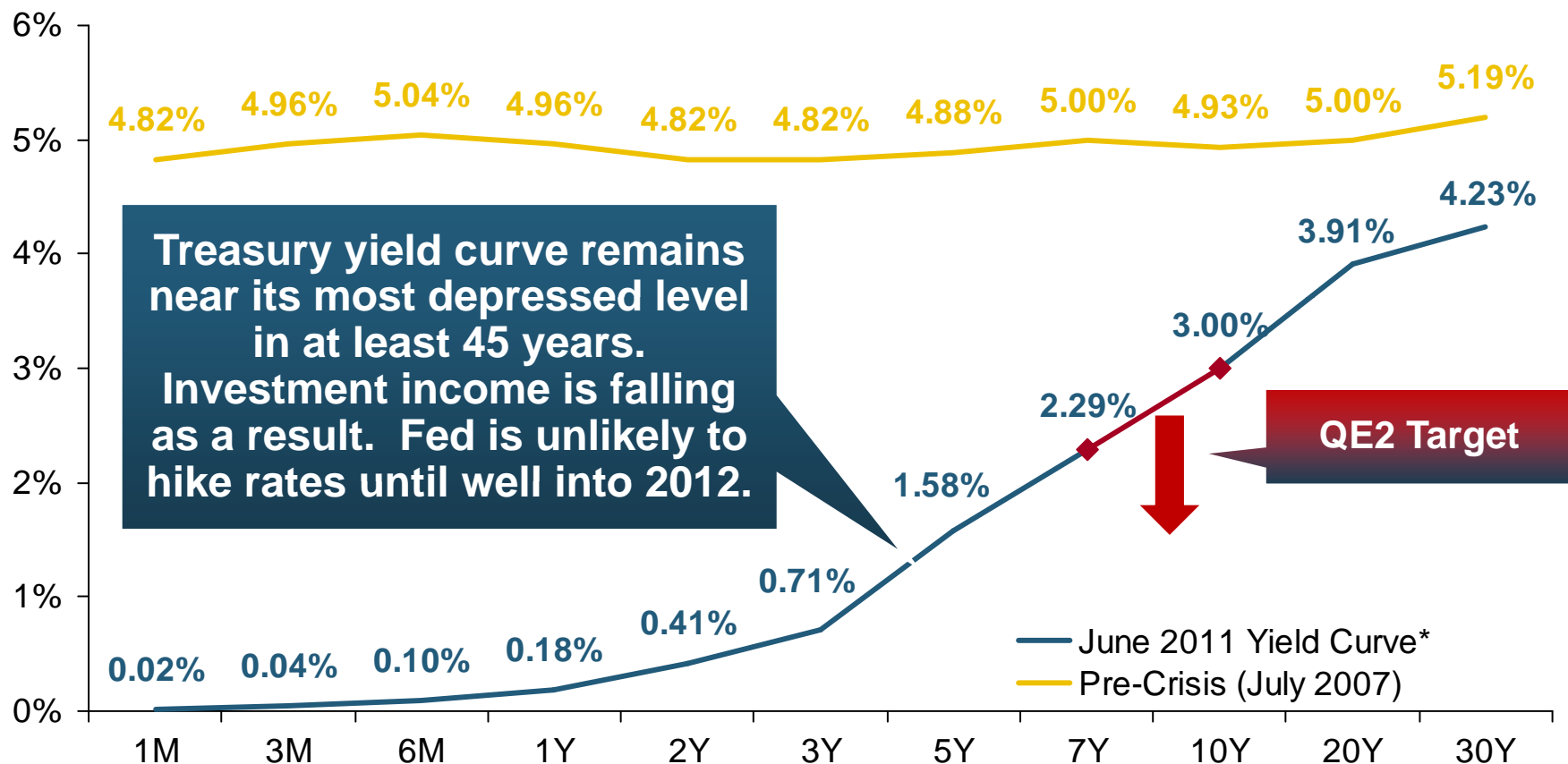
Investment Gains Recovered Significantly in 2010 Due to Realized Investment Gains; The Financial Crisis Caused Investment Gains to Fall by 50% in 2008

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

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

Sources: ISO; Insurance Information Institute.

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

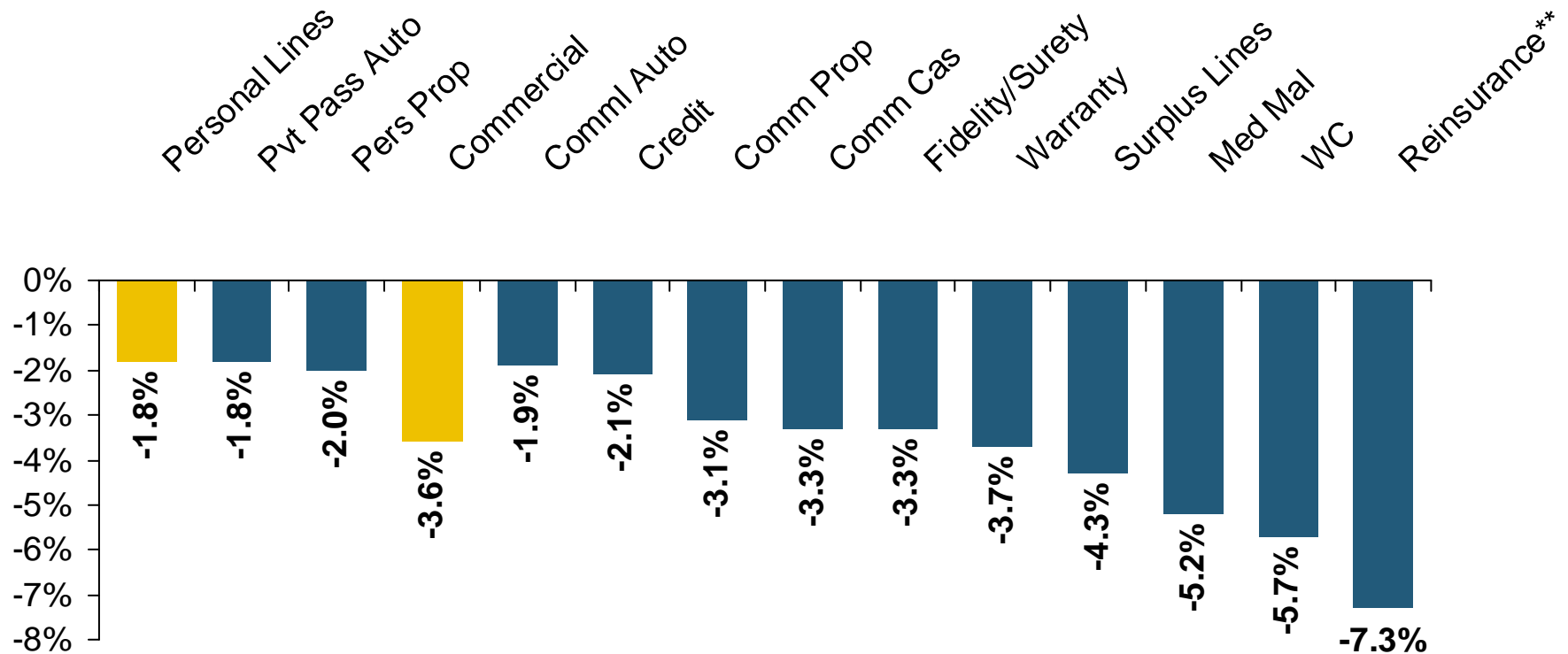


The End of the Fed's Quantitative Easing Is Unlikely to Push Interest Rates Up Substantially Given Ongoing Economic Weakness

*Average of daily rates.

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

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



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

*Based on 2008 Invested Assets and Earned Premiums

**US domestic reinsurance only

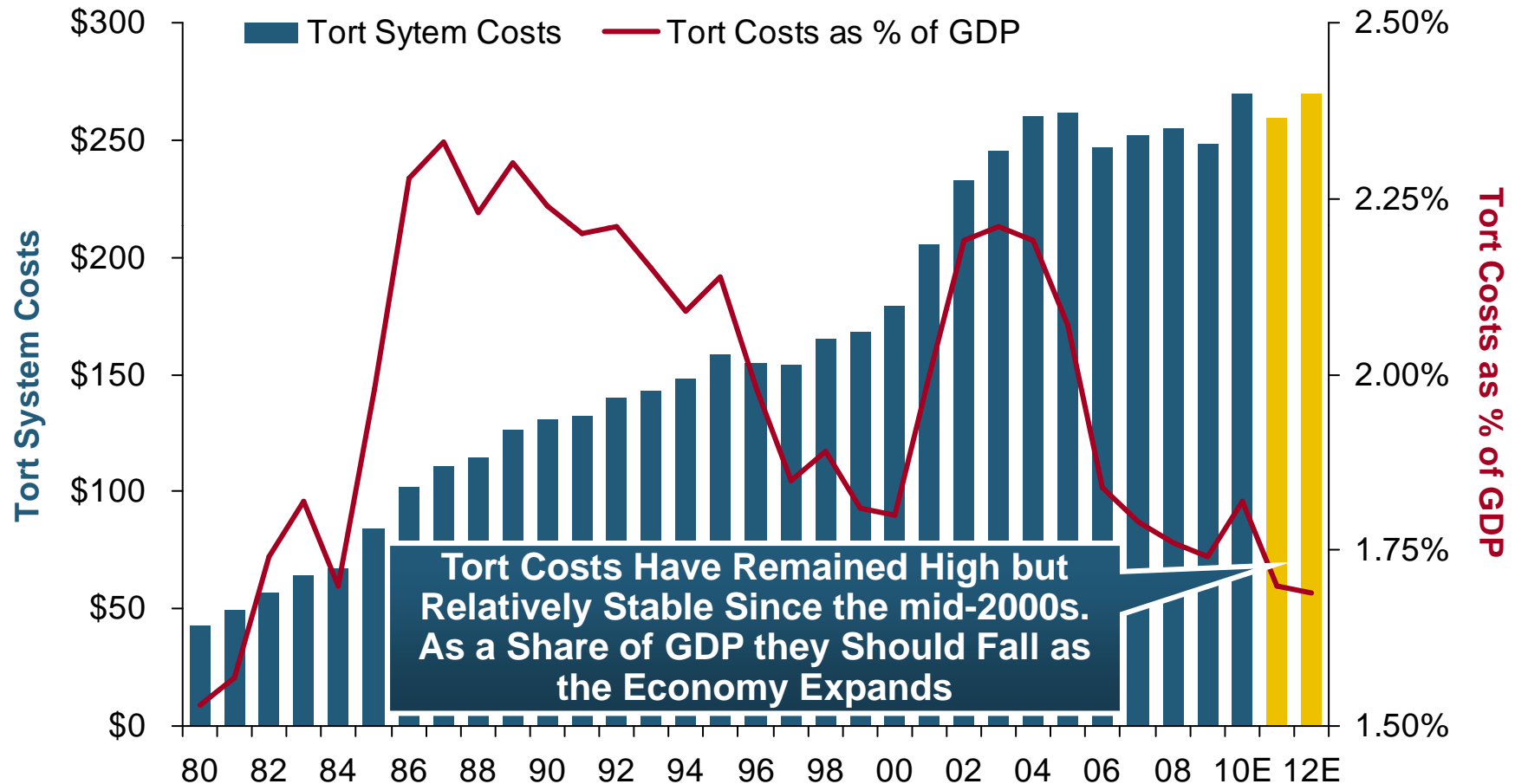
Source: A.M. Best; Insurance Information Institute.

Shifting Legal Liability & Tort Environment

Is the Tort Pendulum Swinging Against Insurers?

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

(\$ Billions)



Business Leaders Ranking of Liability Systems in 2010

Best States

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

New in 2010

- North Dakota
- Massachusetts
- South Dakota

Drop-offs

- Maine
- Vermont
- Kansas

Midwest/West has mix of good and bad states.

Worst States

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

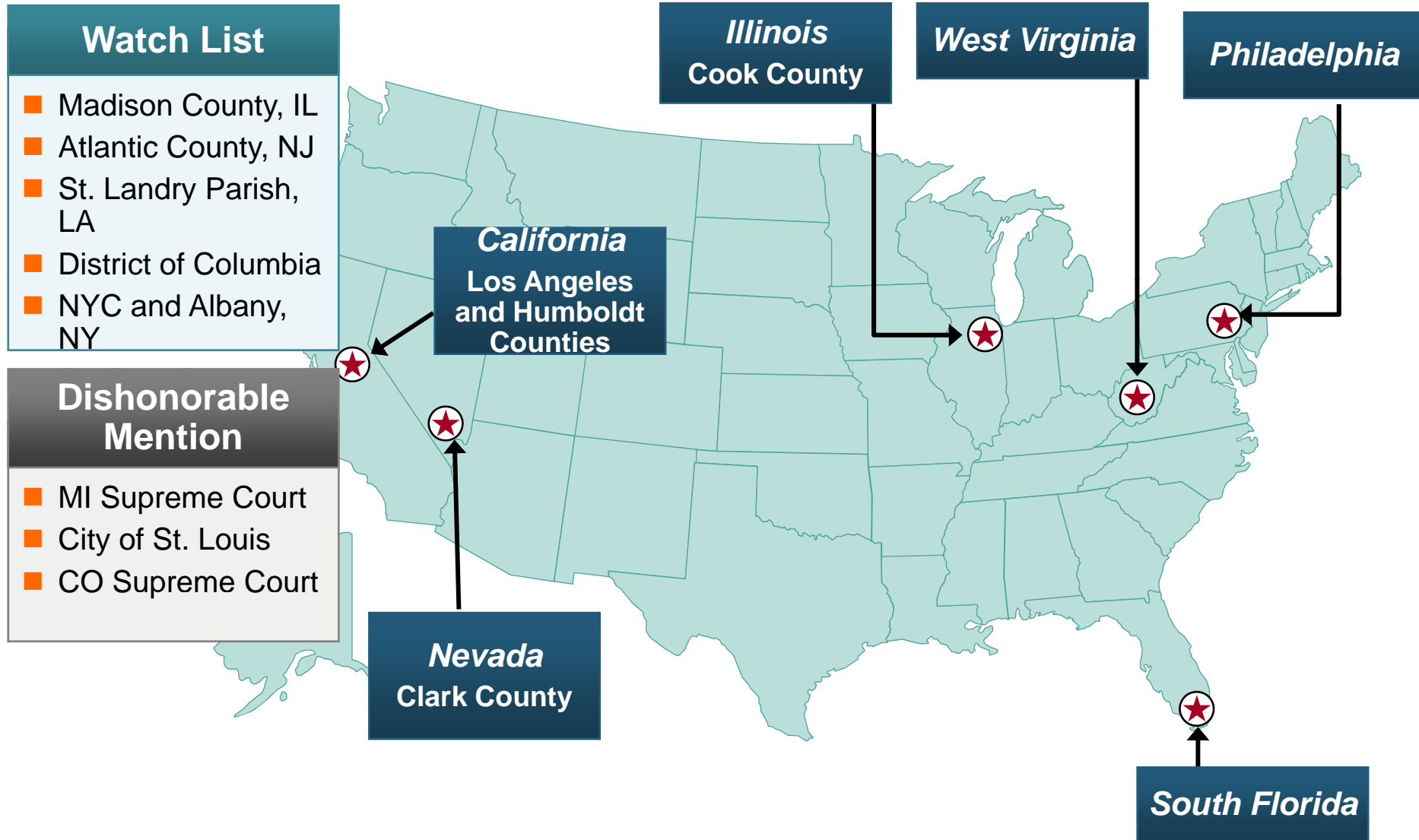
Newly Notorious

- New Mexico
- Montana
- Arkansas

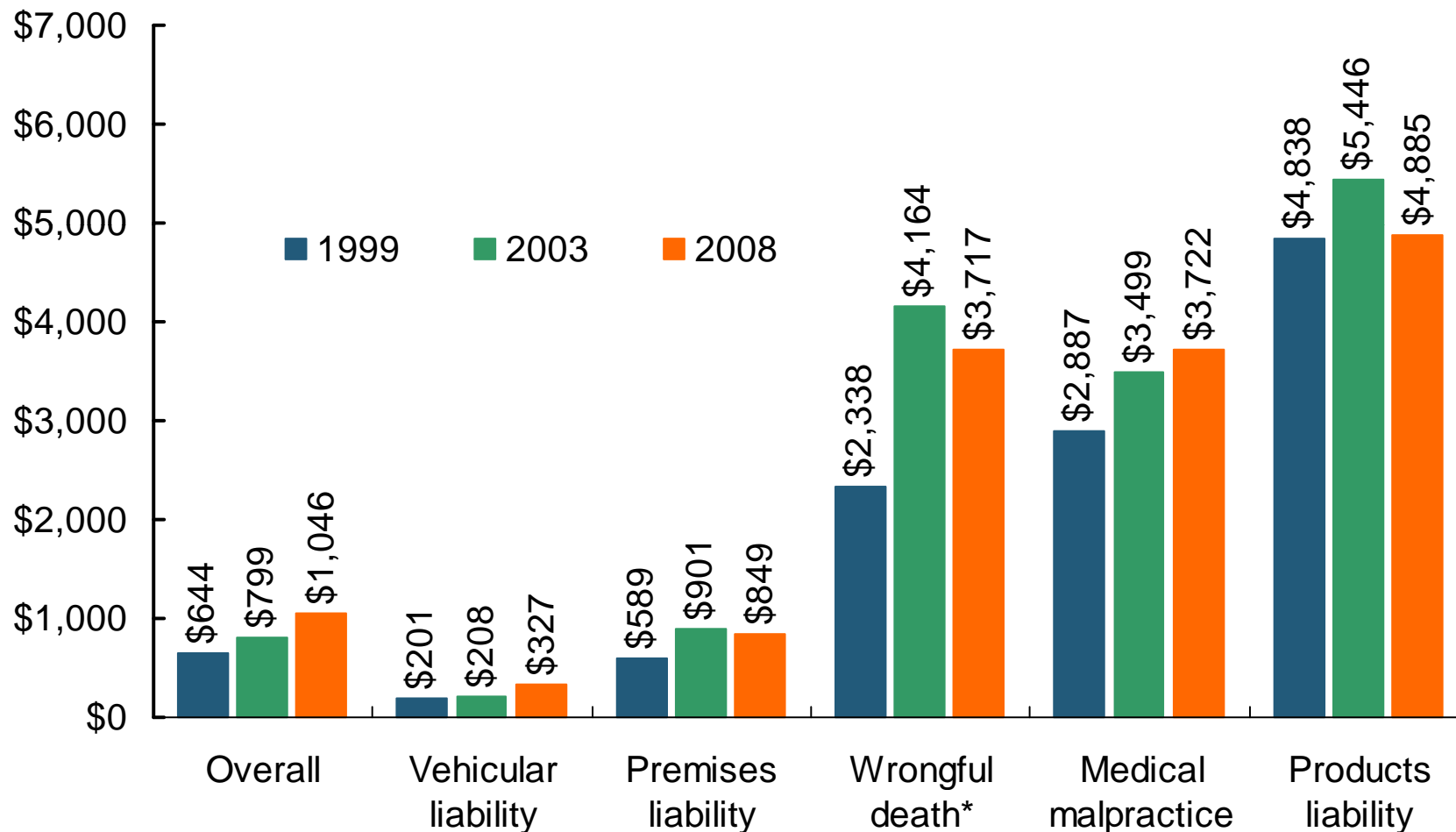
Rising Above

- **Texas**
- South Carolina
- Hawaii

The Nation's Judicial Hellholes: 2010



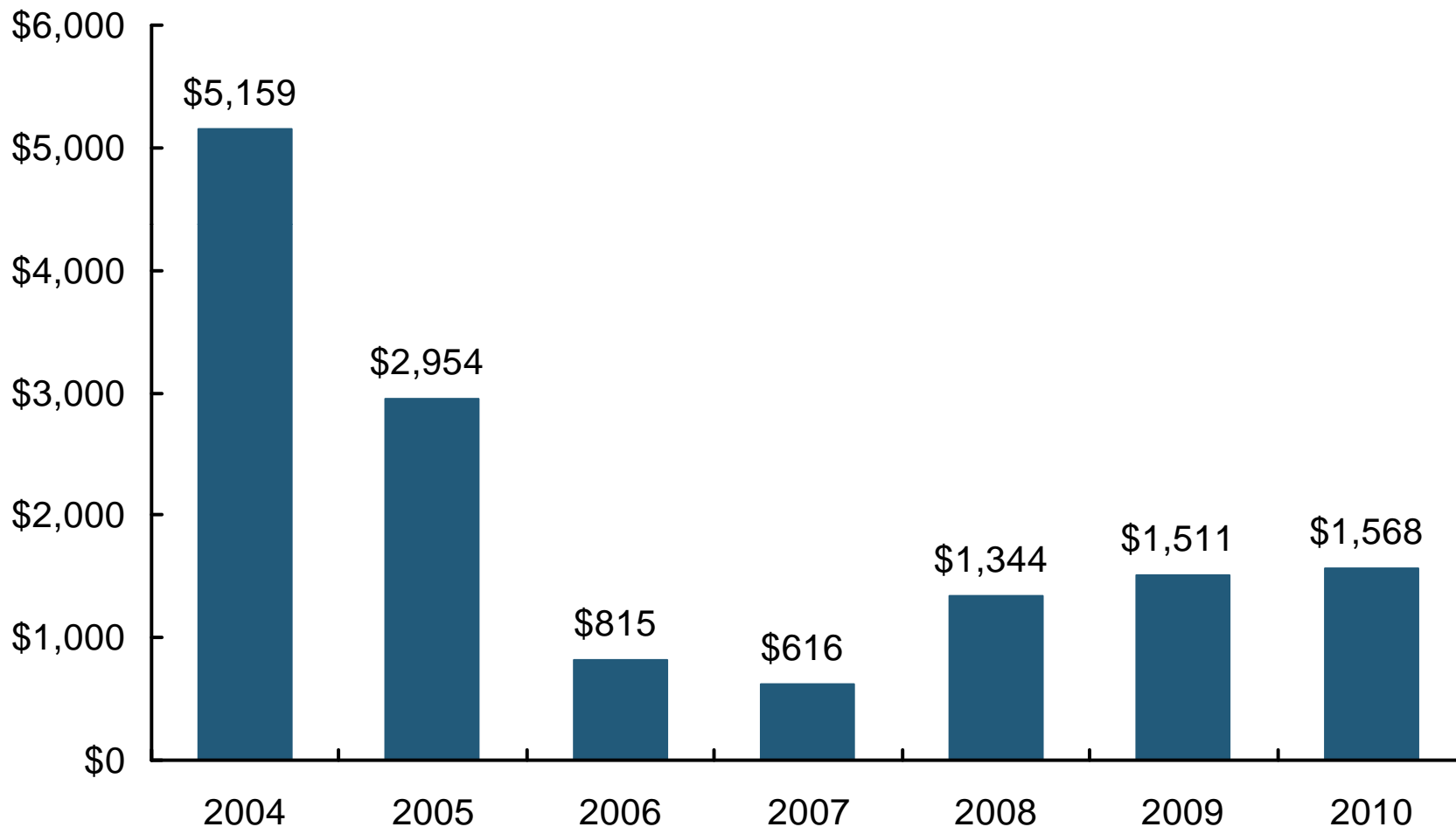
Avg. Jury Awards 1999 vs. 2003 and 2008



*Award trends in wrongful deaths of adult males.

Source: Jury Verdict Research; Insurance Information Institute.

Sum of Top 10 Jury Awards 2004-2010



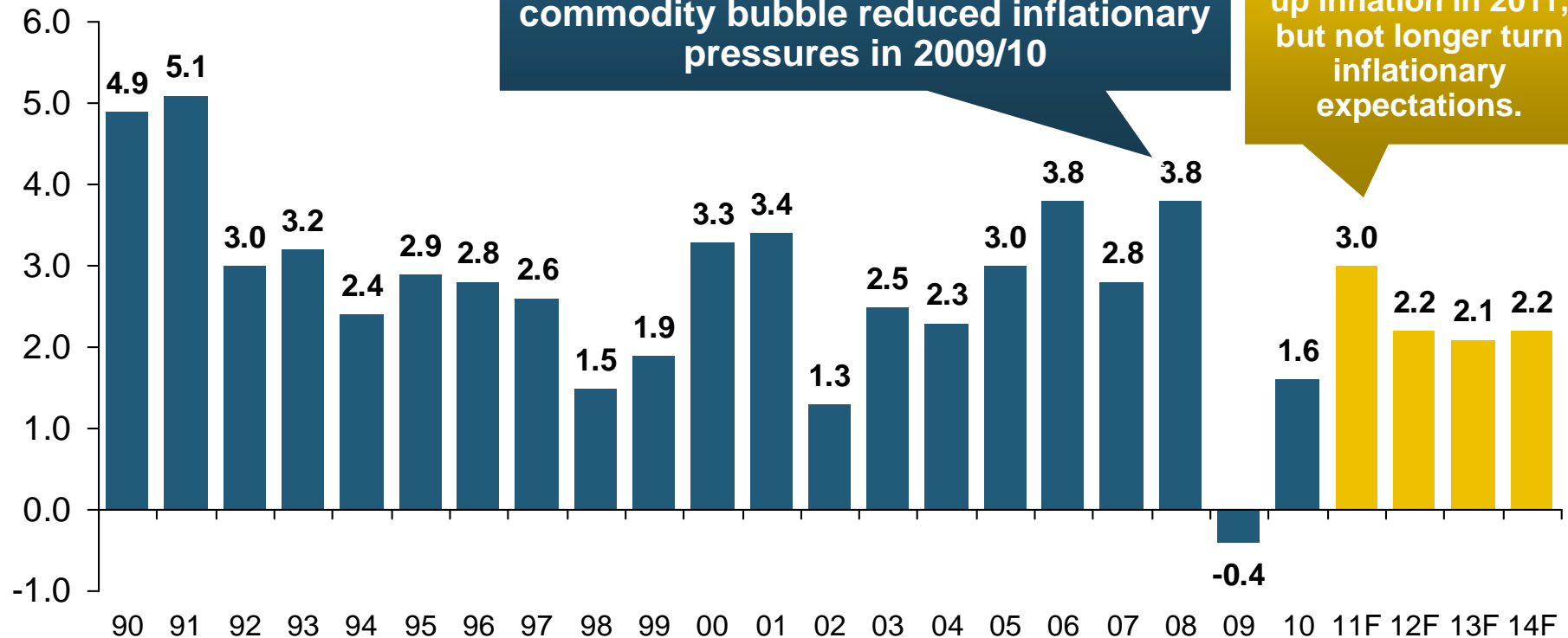
Source: Insurance Information Institute from Lawyers USA, January 2005, 2006, 2007, 2008, 2009, and 2010.

Inflation

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

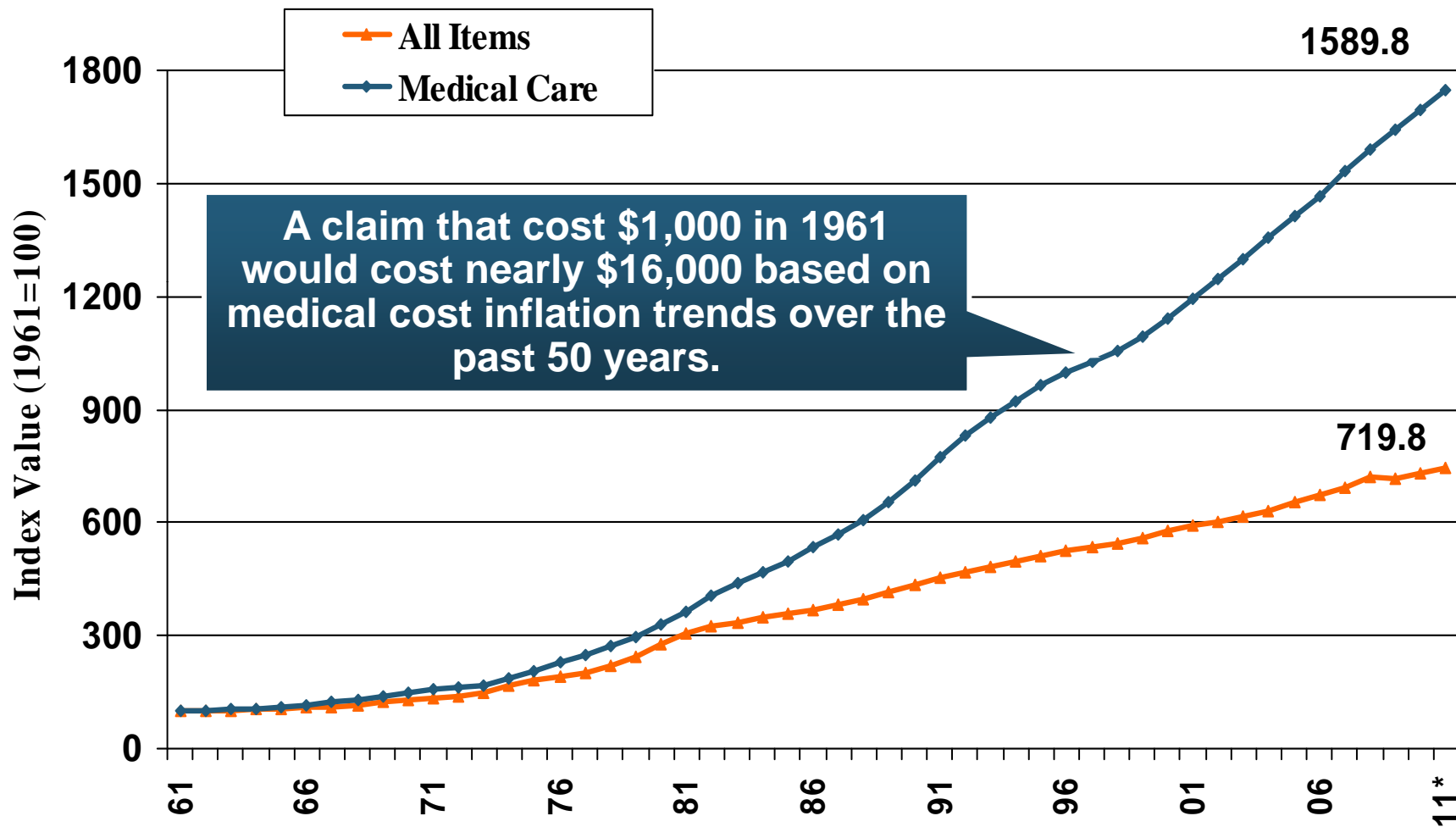
Annual Inflation Rates, (CPI-U, %), 1990–2014F

Annual Inflation Rates (%)



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

Medical Cost Inflation Has Outpaced Overall Inflation Over 50 Years



*Based on change from Feb. 2011 to Feb. 2010 (latest available)

Source: Department of Labor (Bureau of Labor Statistics)

Regulatory Environment & Financial Services Reform

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

Financial Services Reform: *What does it mean for insurers?*

The Dodd Frank Wall Street Reform and Consumer Protection Act

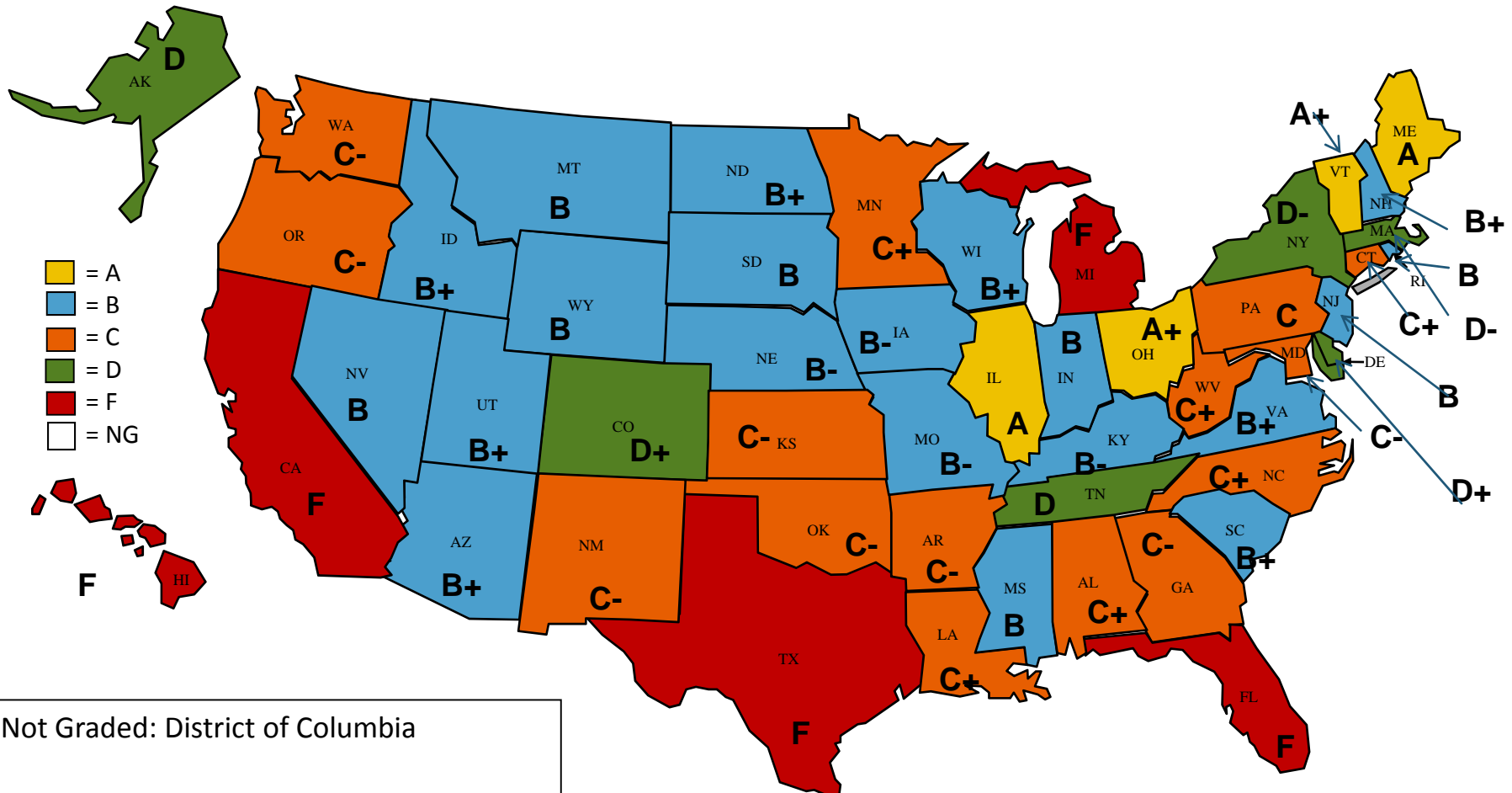
■ Systemic Risk and Resolution Authority

- Creates the Financial Stability Oversight Council and the Office of Financial Research
- Regulator representative is MO Insurance Commissioner Huff
- *No industry representative has been appointed yet*
- Imposes heightened federal regulation on large bank holding companies and “systemically risky” nonbank financial companies, including insurers
- ***Concern some insurers may be labeled as systemically risky based on size alone***

■ Federal Insurance Office (FIO)

- Establishes the FIO (while maintaining state regulation of insurance) within the Department of Treasury, headed by a Director appointed by the Secretary of Treasury
- FIO will have authority to monitor the insurance industry, identify regulatory gaps that could contribute to systemic crisis
- **IL Insurance Director Michael McGraith will become first FIO Director on June 1**
- **Creation of Federal Advisory Committee on Insurance to Advise FIO**
- ***CONCERN: FIO morphs into quasi/shadow or actual regulator***

2010 Property and Casualty Insurance Report Card

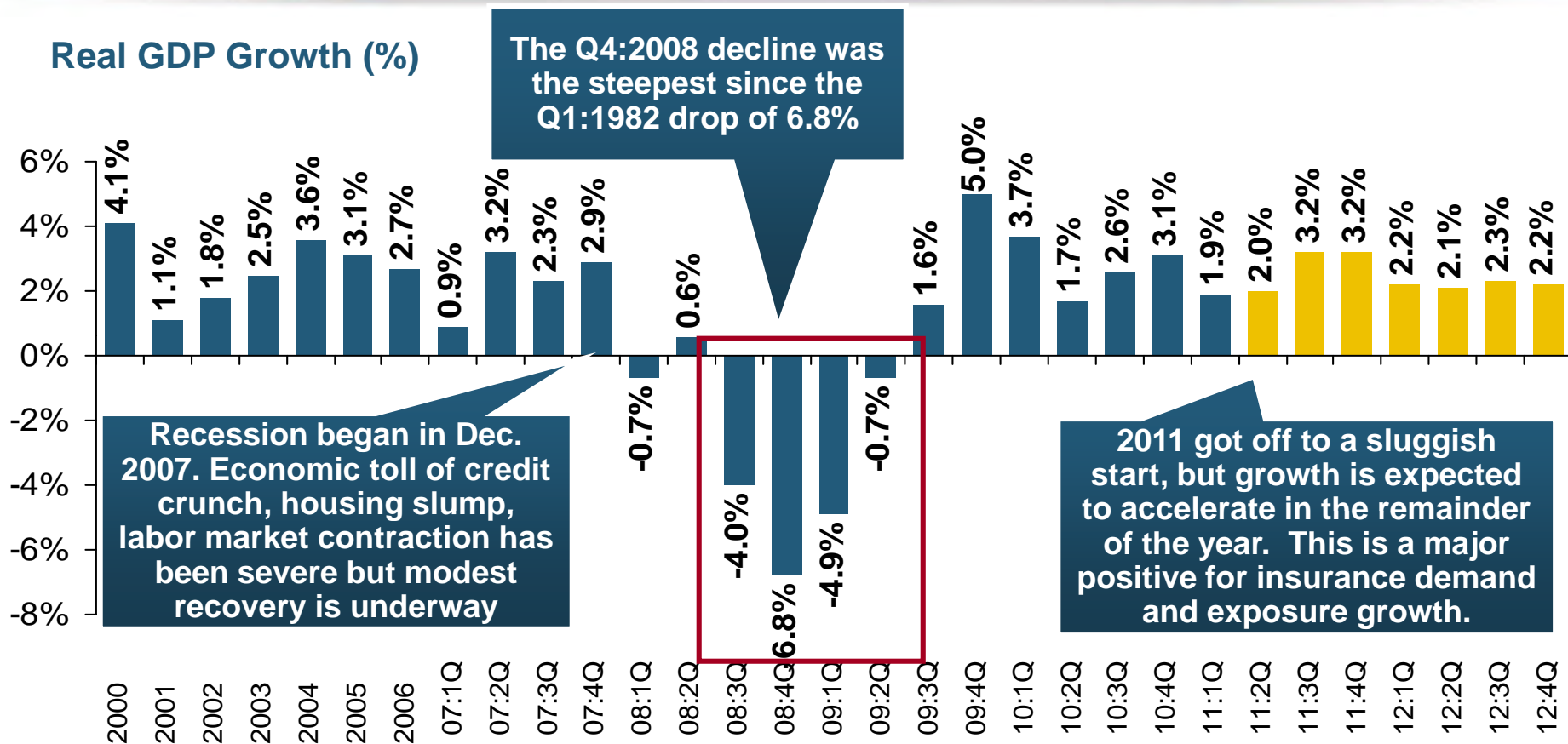


The Strength of the Economy Will Influence P/C Insurer Growth Opportunities

**Growth Would Also Help Absorb
Excess Capital**

US Real GDP Growth*

Real GDP Growth (%)



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

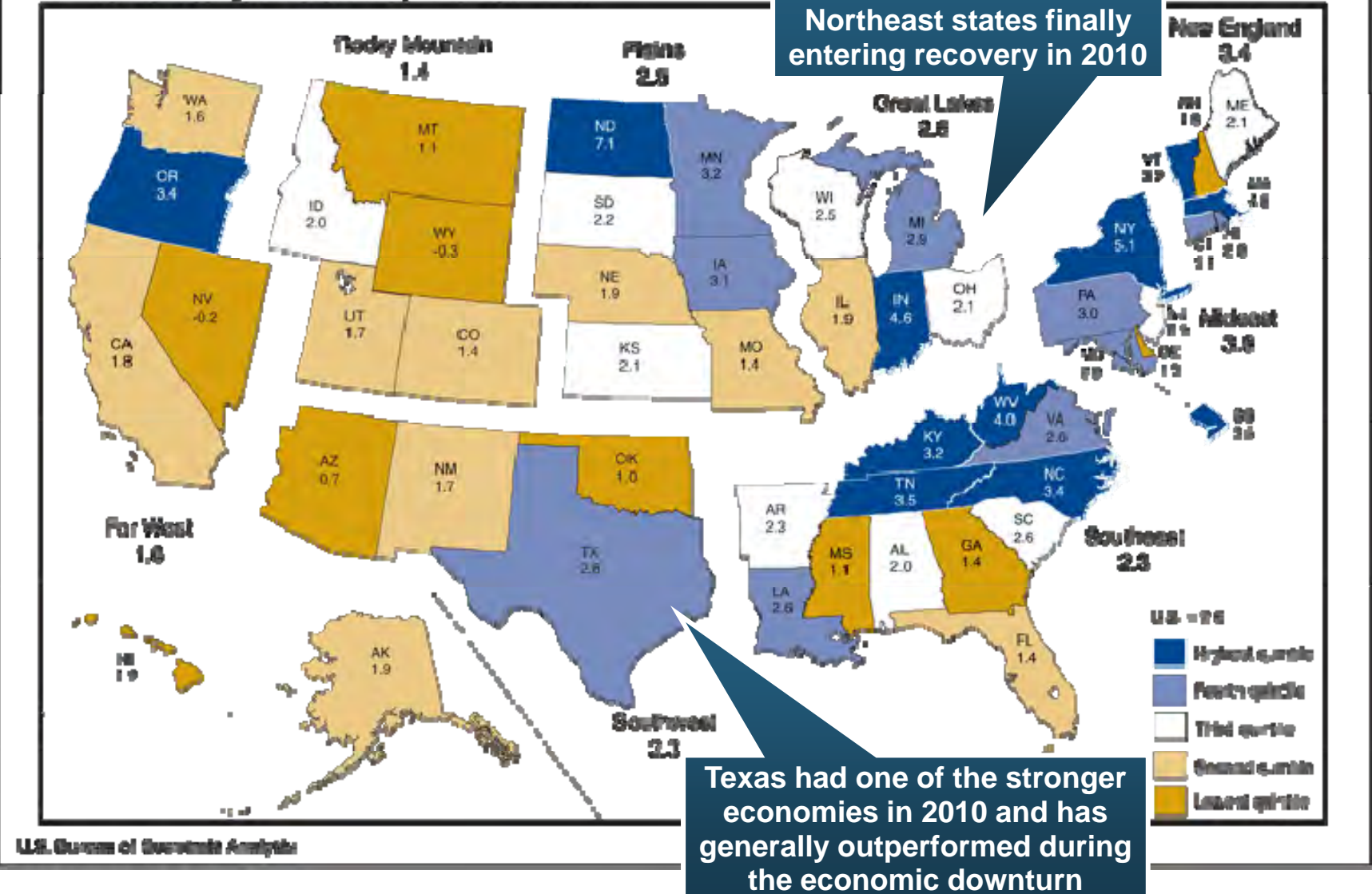
* Estimates/Forecasts from Blue Chip Economic Indicators.

Source: US Department of Commerce, Blue Economic Indicators 7/11; Insurance Information Institute.

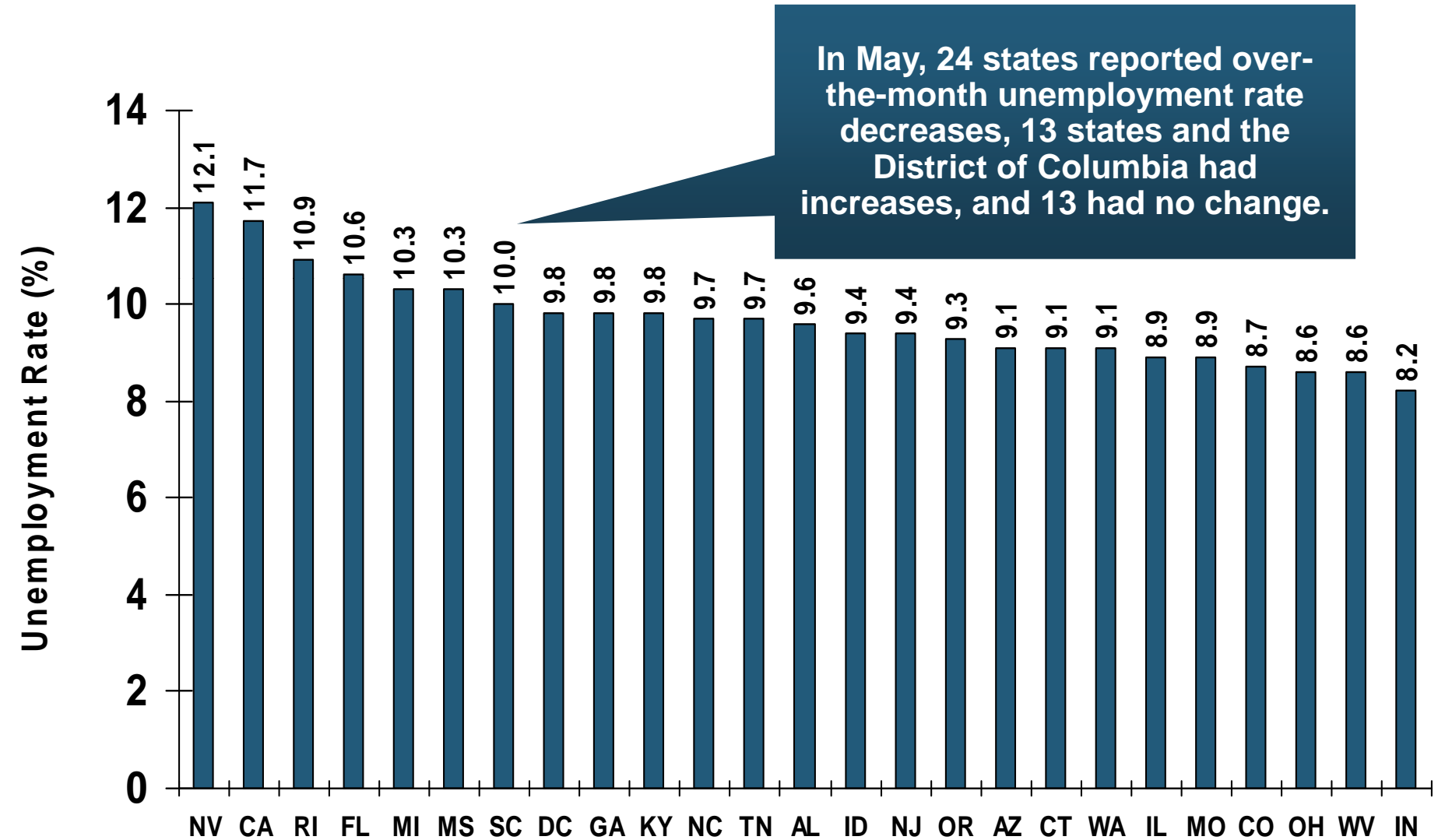
2011 Financial Overview

State Economic Growth Varied in 2010

Chart 1. Percent Change in Real GDP by State, 2009-2010



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

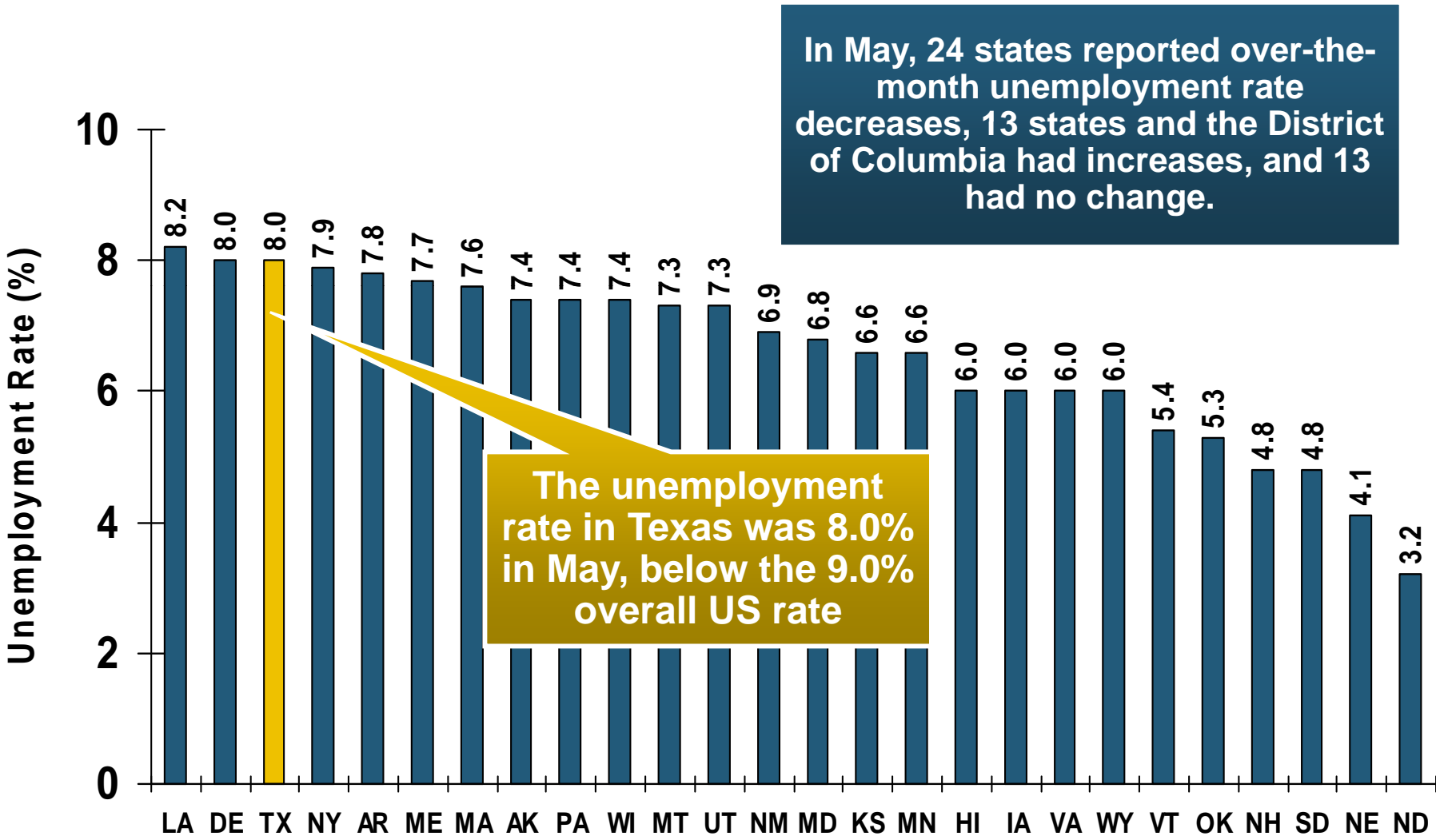


*Provisional figures for May 2011, seasonally adjusted.

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

Unemployment Rates By State, May 2011:

Lowest 25 States*



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

Insurance Information Institute Online:

www.iii.org

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

Twitter: twitter.com/bob_hartwig