



The Workers Compensation Marketplace: *Focus on North Carolina*

**North Carolina Workers Compensation
Insurance Symposium**

Winston, NC

August 2, 2010

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

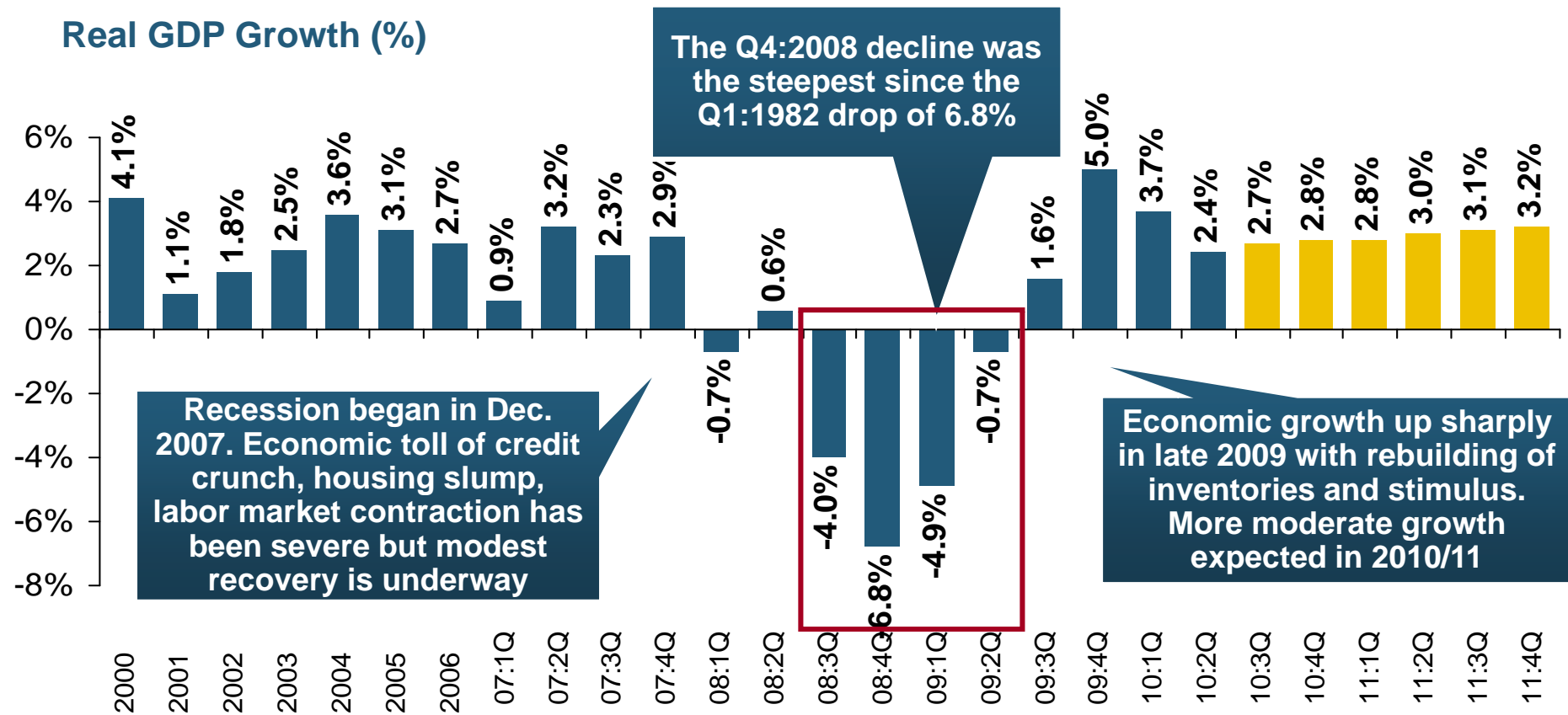
- **Workers Compensation and the Economy**
 - ◆ Regional Differences
 - ◆ Labor Market Trends
- **Crisis-Driven Exposure Drivers in Workers Comp**
 - ◆ Trends in Business Bankruptcies and New Business Formation
 - ◆ Measures of Production and Capacity Utilization
- **Sources of Growth in Workers Compensation**
 - ◆ Industry and Occupation Growth Analysis through 2018
- **Key Issues Facing Workers Comp Insurers in the Decade Ahead**
 - ◆ Investment Outlook, Regulation, Torts, Terrorism, Healthcare Reform
- **Workers Compensation Operating Environment**
 - ◆ Premium Growth
 - ◆ Underwriting Performance
 - ◆ Medical and Indemnity Claims Cost Trends
- **P/C Financial Overview**
- **Q&A**

Workers Compensation and the Economy

**Workers Comp Exposure and
Performance is Intimately Linked to
the Economy and Labor Market**

US Real GDP Growth*

Real GDP Growth (%)



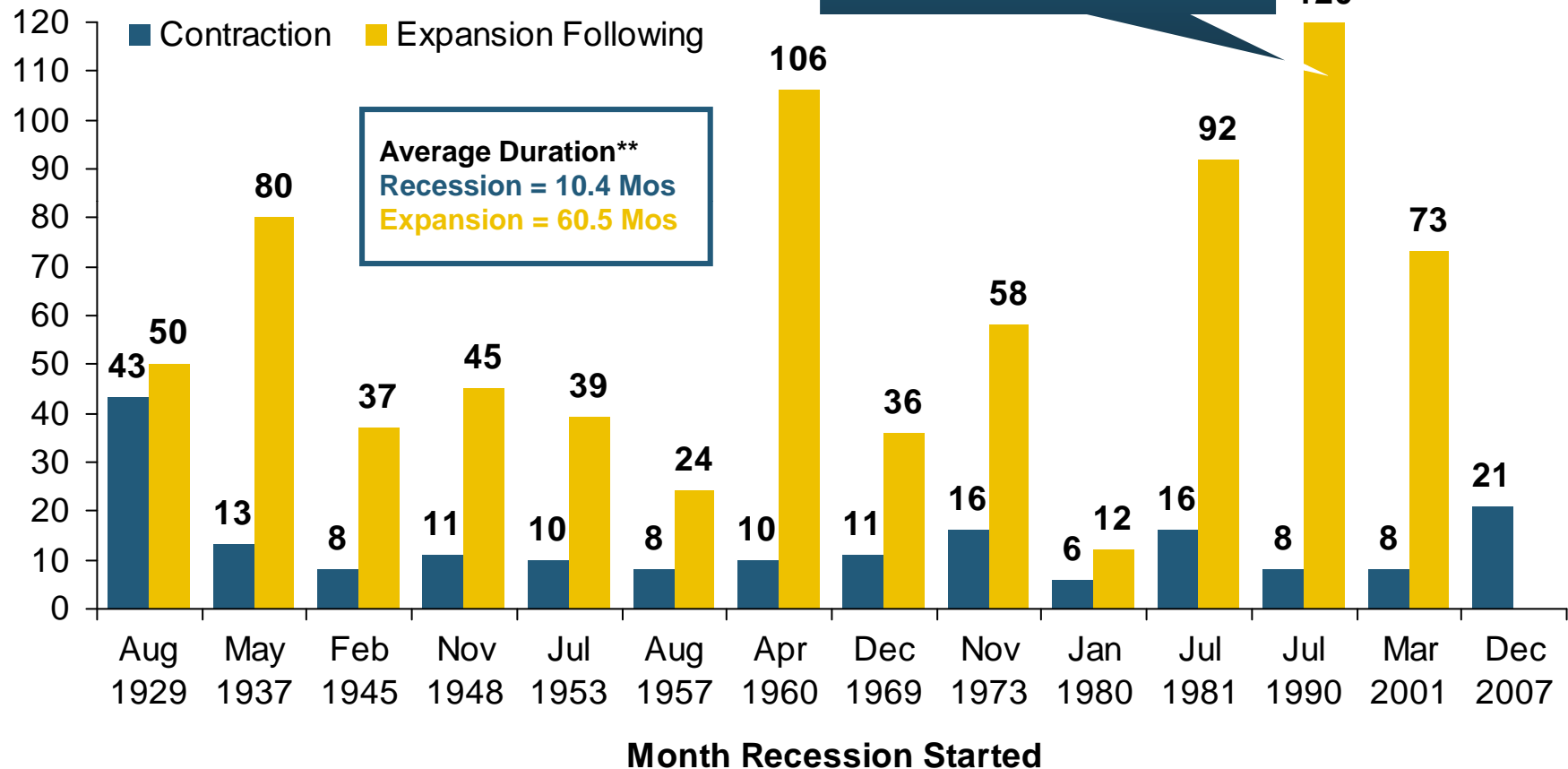
Demand for Energy and Commercial Insurance Have Been Impacted by Sluggish Economic Conditions

* 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)

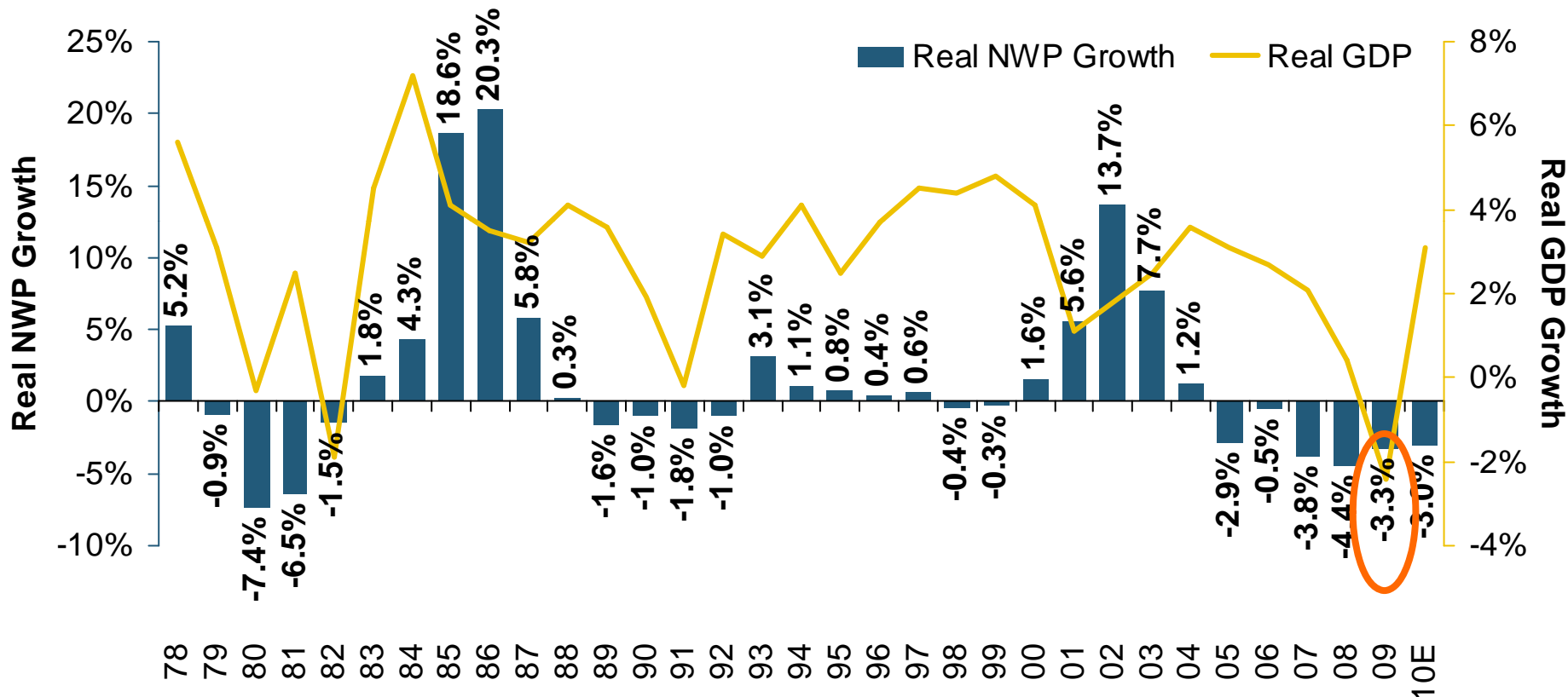


*August 2010 (likely the “official end” of recession was June 2009) ** Post-WW II period through end of most recent expansion.

Sources: National Bureau of Economic Research; Insurance Information Institute.

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**



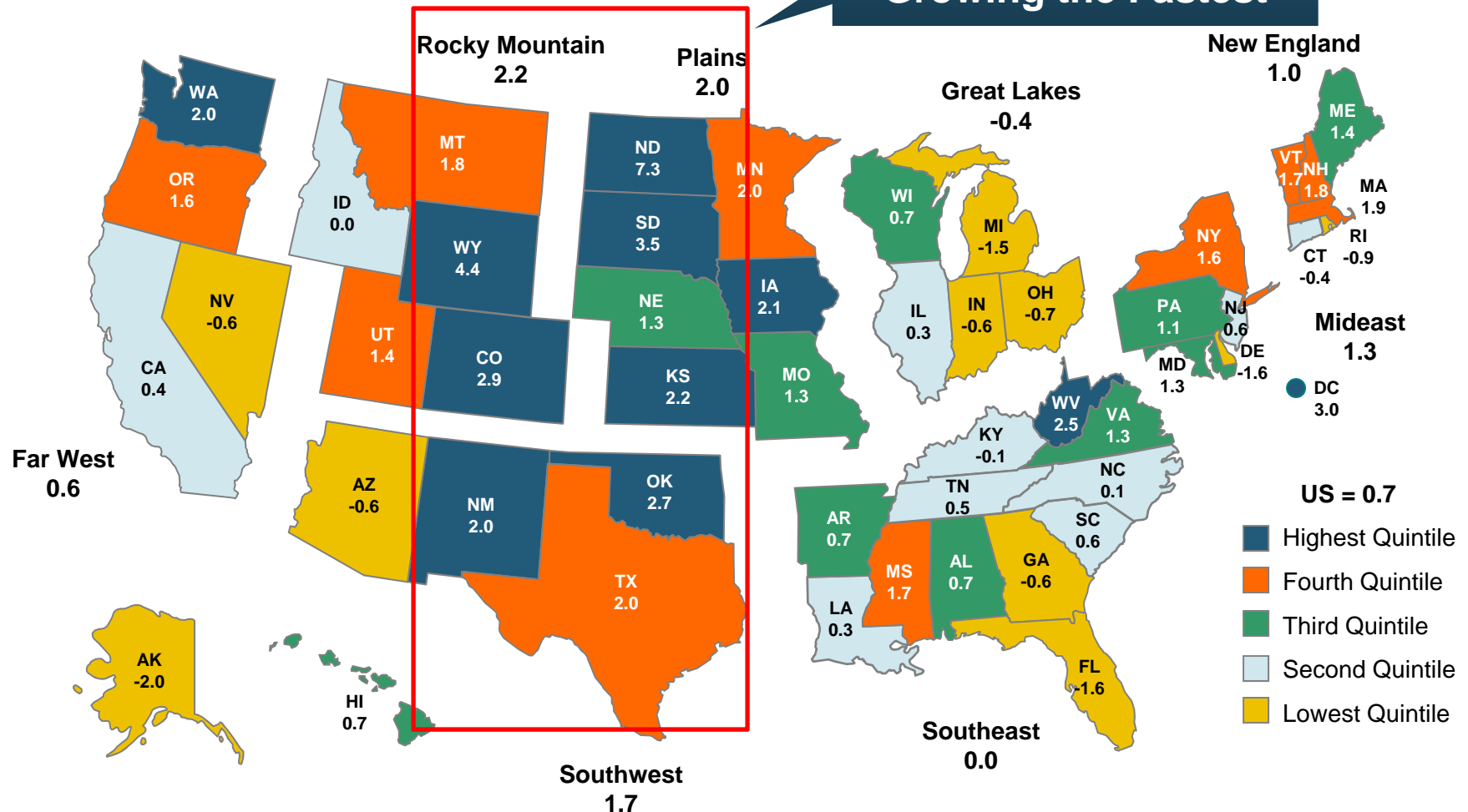
Regional Differences Will Significantly Impact P/C Markets

**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

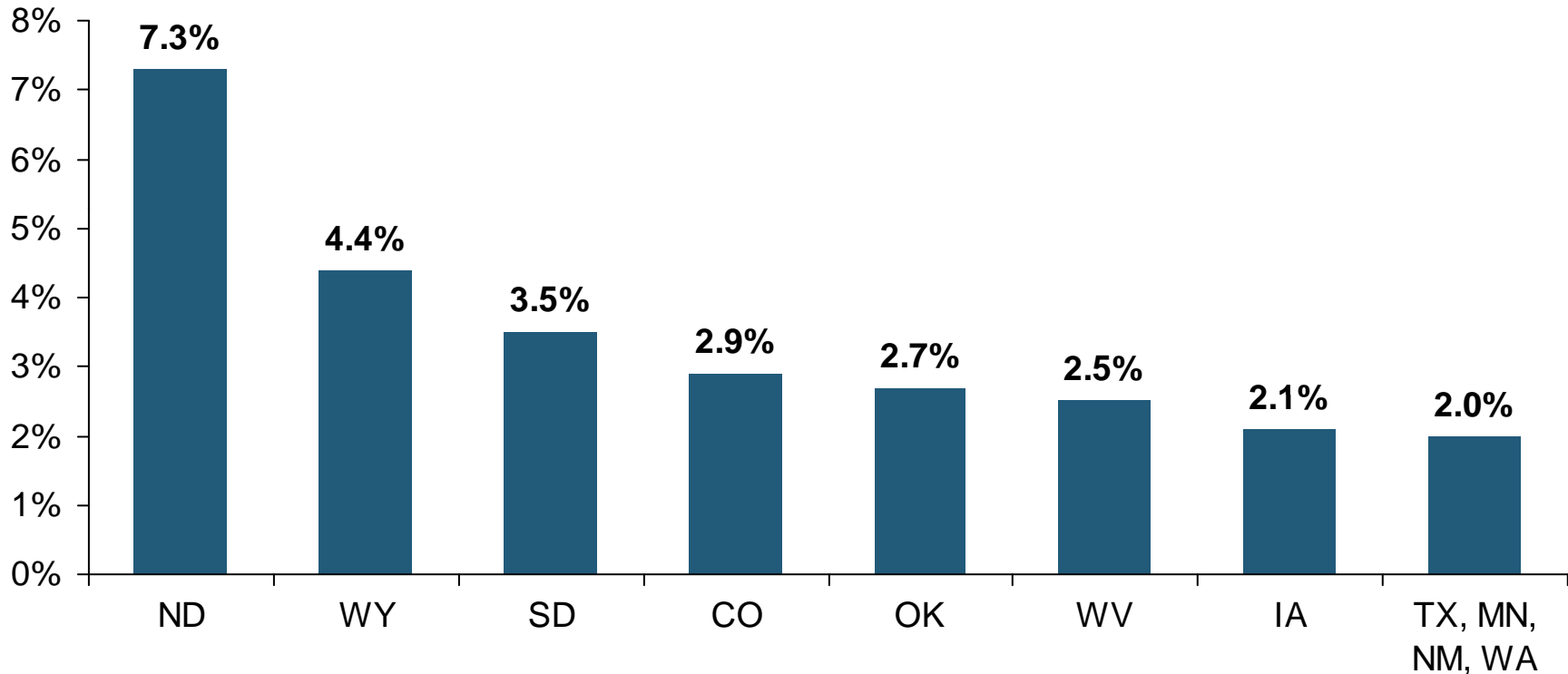
Percent Change in Real GDP by State, 2007–2008

**Mountain, Plains States
Growing the Fastest**



Fastest Growing States in 2008: Plains, Mountain States Lead

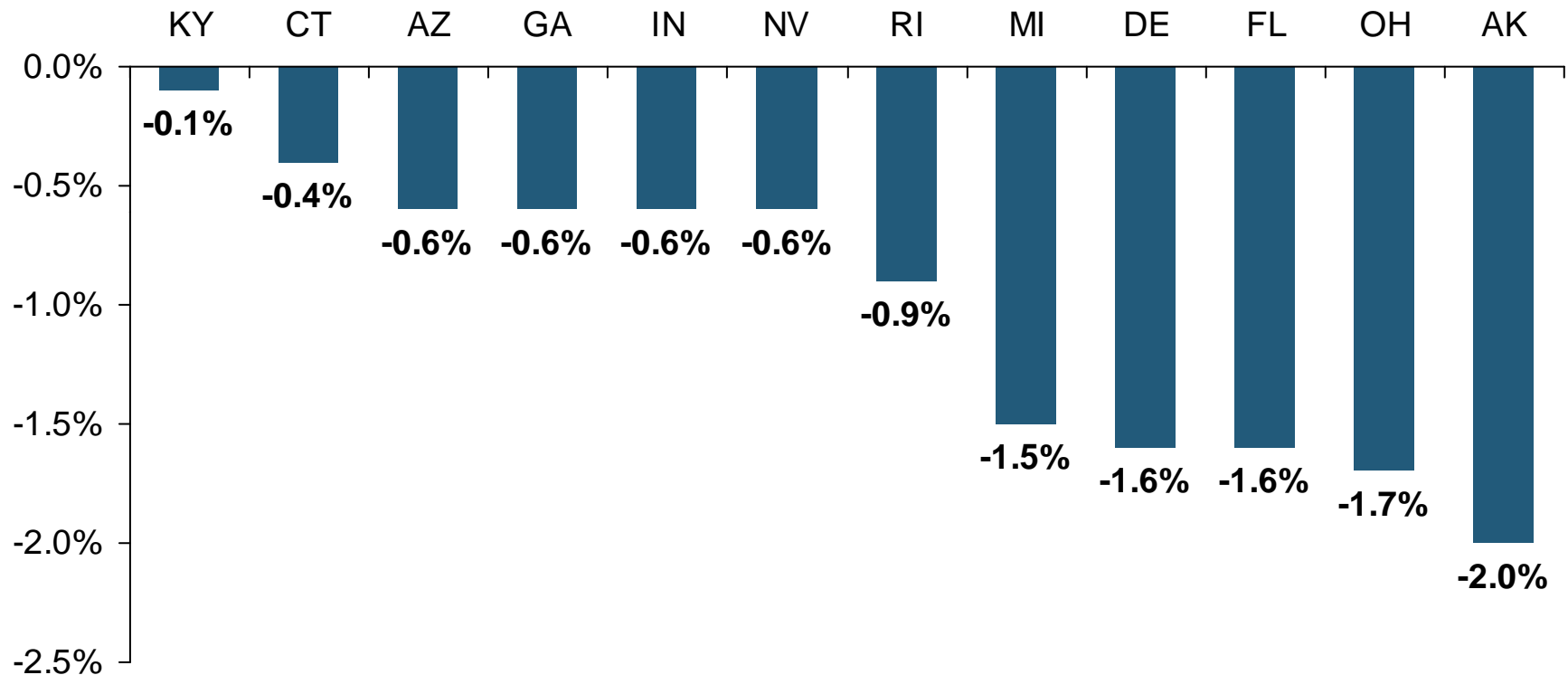
Real State GDP Growth (%)



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

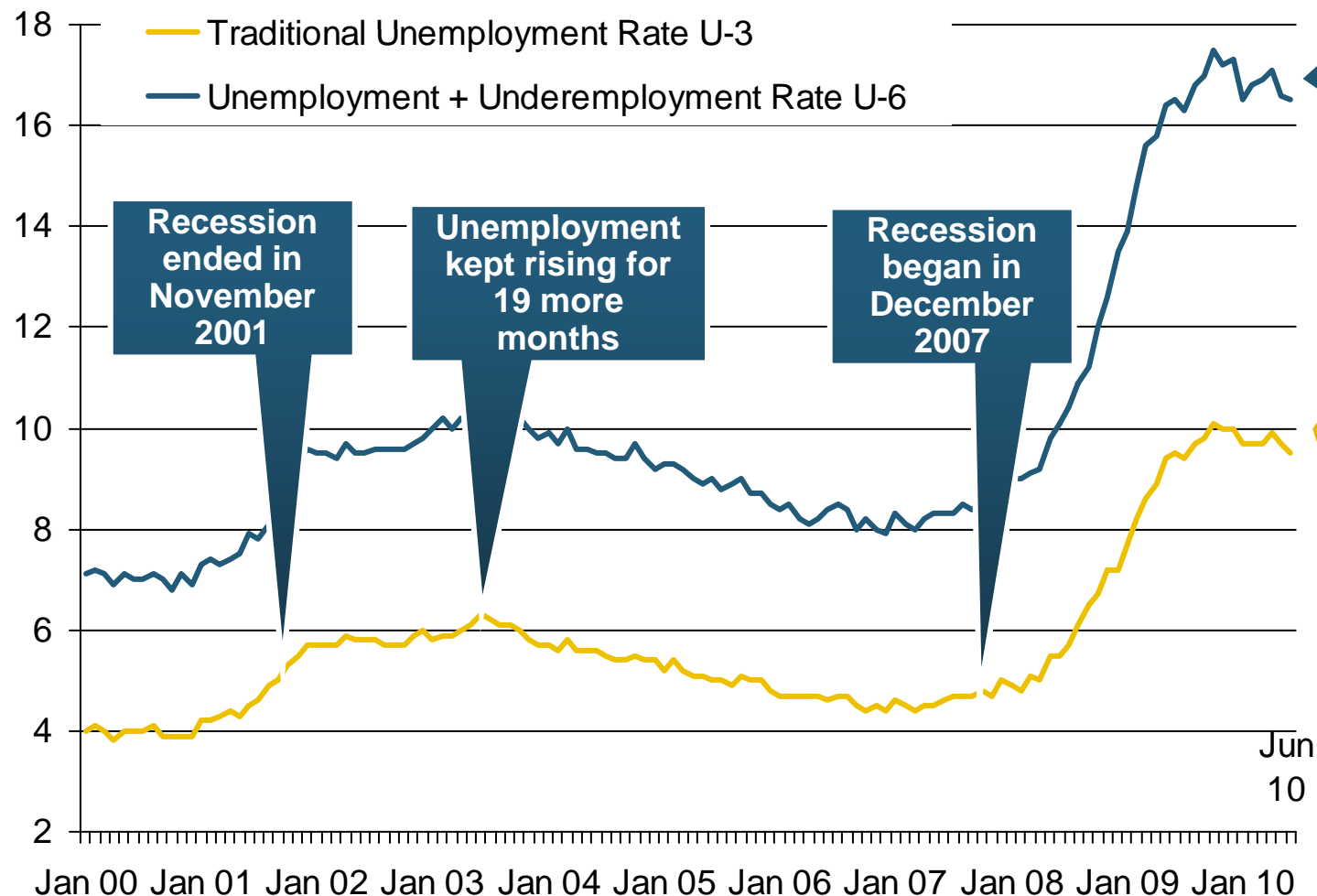
Labor Market Trends

**Massive Job Losses Sapped the
Economy and the Workers Comp
Payroll Exposure Base**

The Long Road to Recovery

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

January 2000 through June 2010, Seasonally Adjusted (%)



U-6 went from 8.0% in March 2007 to 17.5% in Oct 2009; Stood at 16.5% in June 2010

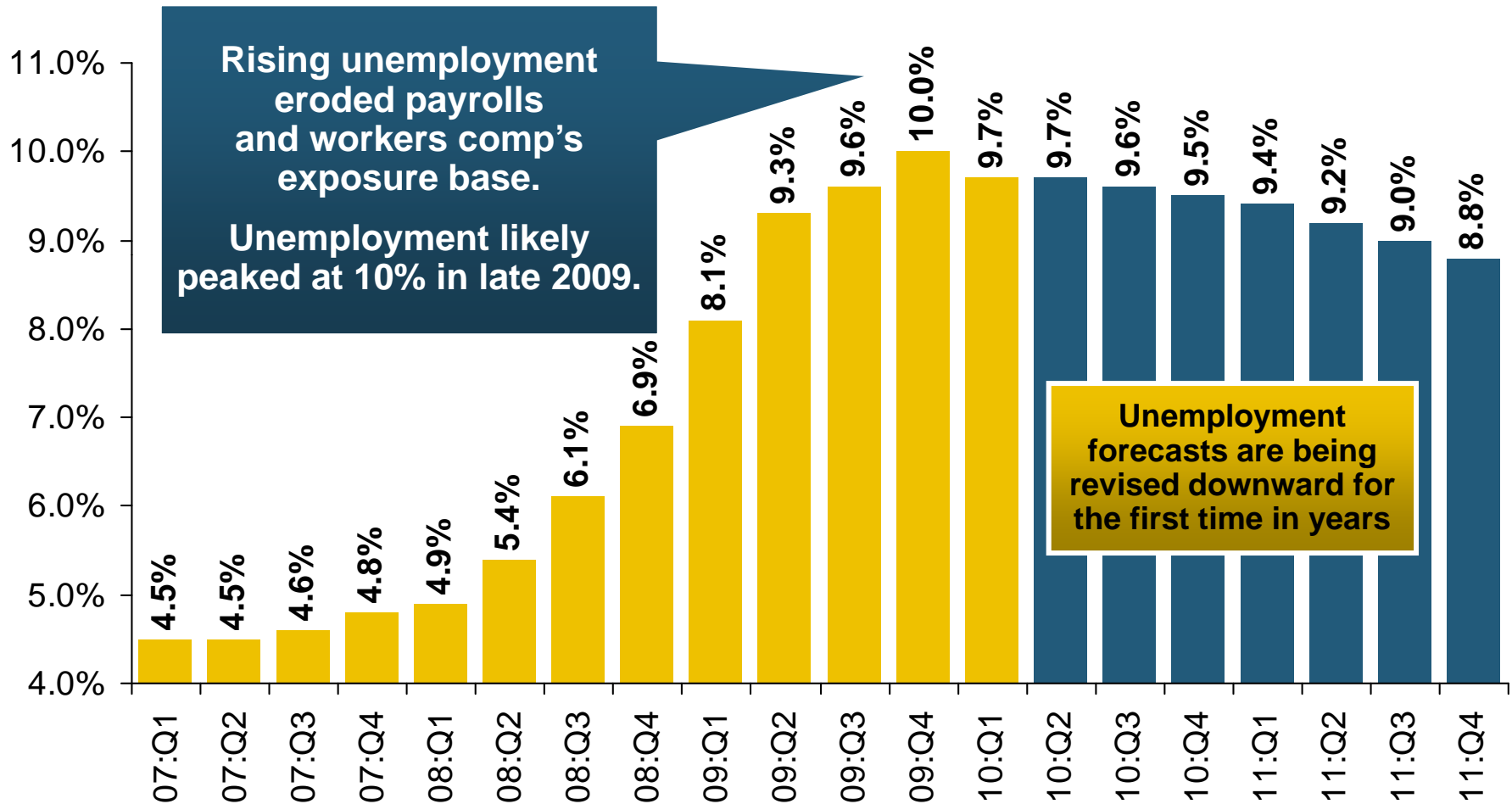
Unemployment rate was 9.5% in June

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

Peak rate in the last 30 years: 10.8% in Nov - Dec 1982

US Unemployment Rate

2007:Q1 to 2011:Q4F*

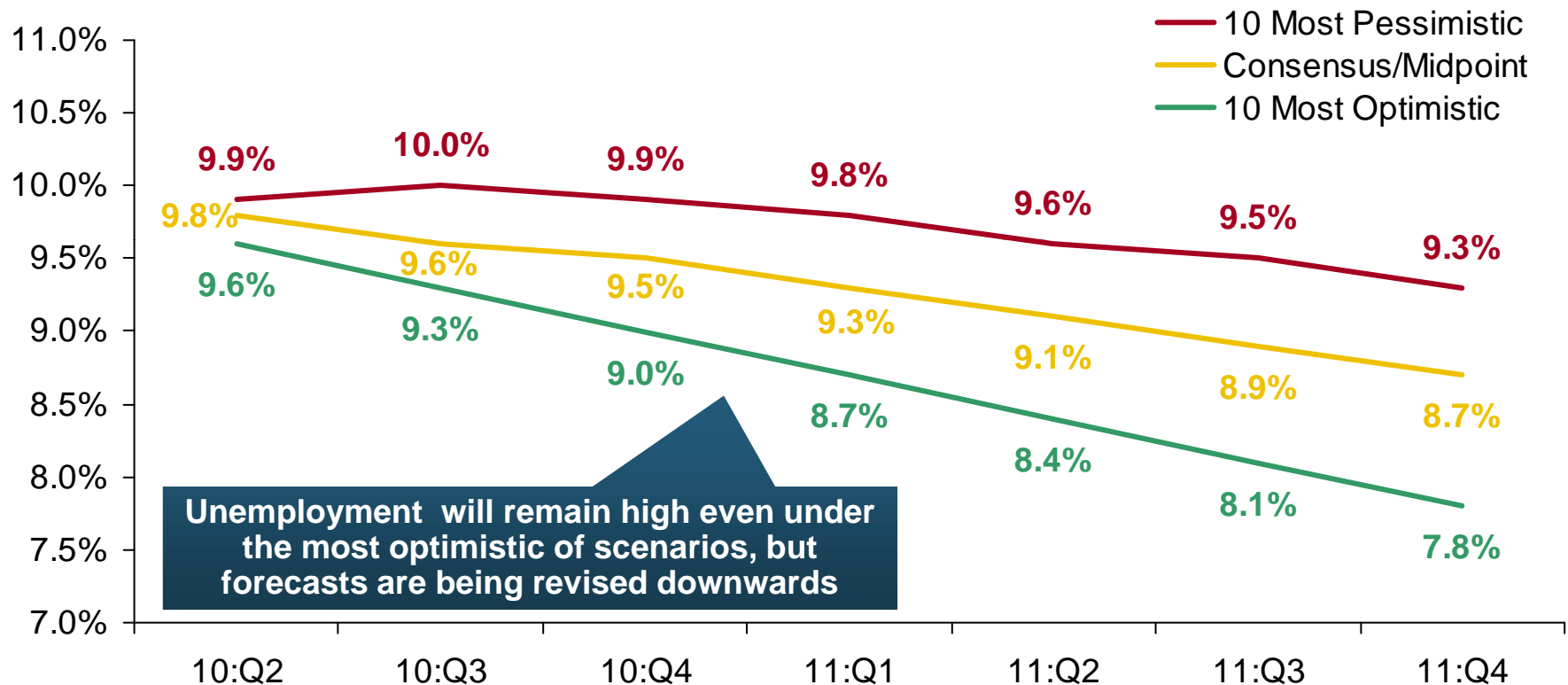


* ■ = actual; ■ = forecasts

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

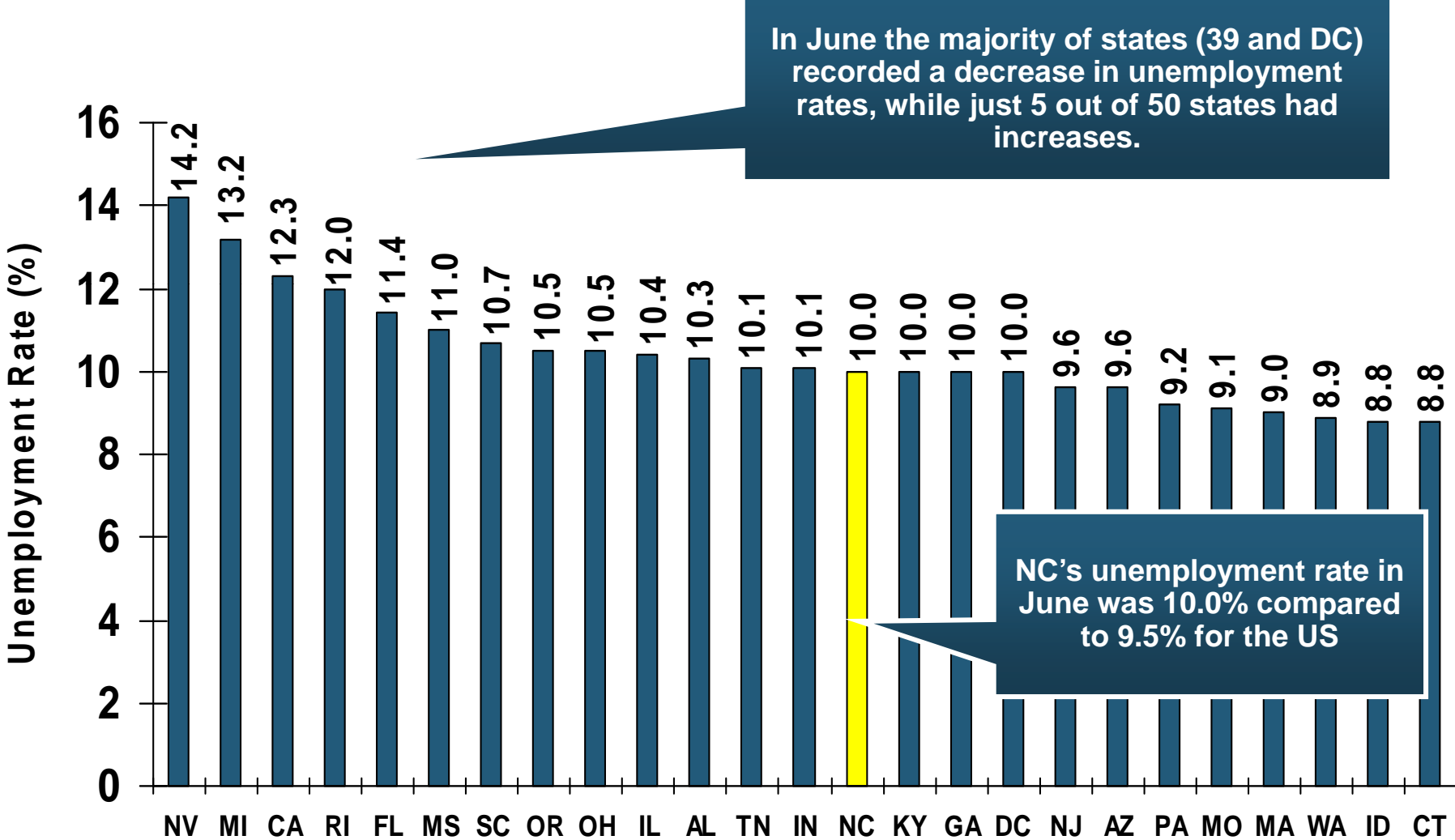
US Unemployment Rate Forecasts

Quarterly, 2010:Q1 to 2011:Q4



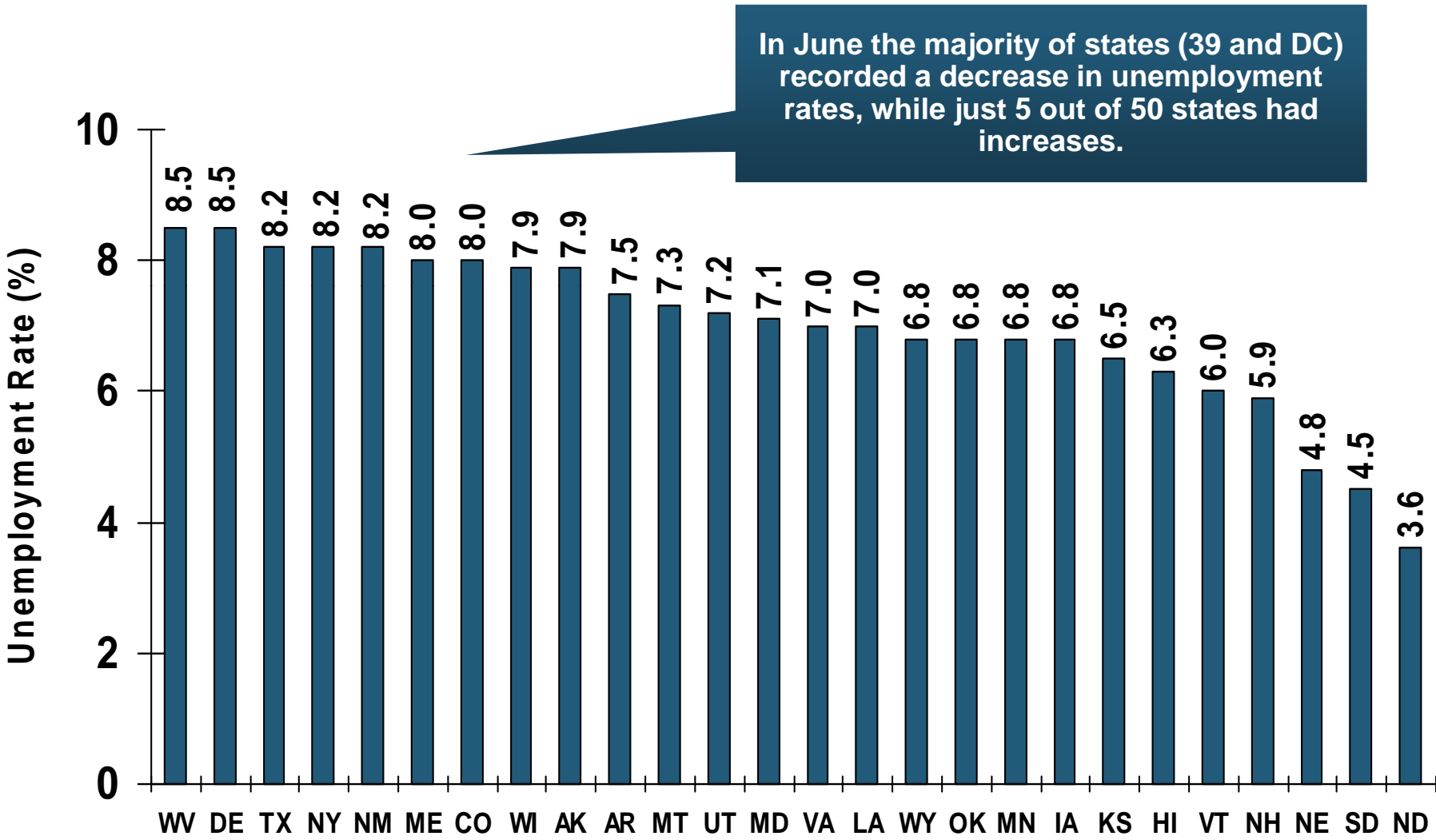
Stubbornly High Unemployment Will Slow the Recovery of the Workers Comp Exposure Base

Unemployment Rates by State, June 2010: Highest 25 States*



*Provisional figures for June 2010, seasonally adjusted.
Sources: US Bureau of Labor Statistics; Insurance Information Institute.

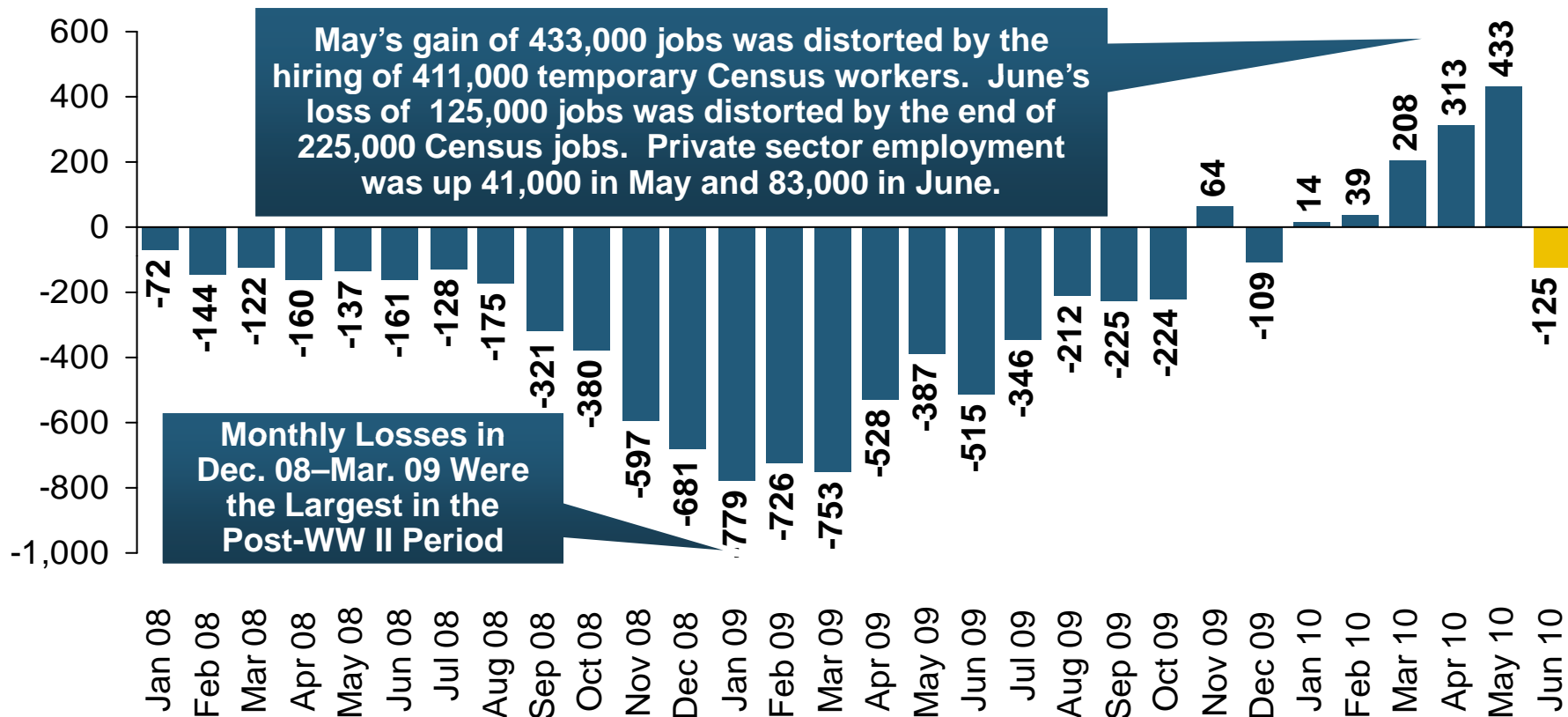
Unemployment Rates By State, June 2010: Lowest 25 States*



*Provisional figures for June 2010, seasonally adjusted.
Sources: US Bureau of Labor Statistics; Insurance Information Institute.

Monthly Change Employment*

January 2008 through June 2010* (Thousands)



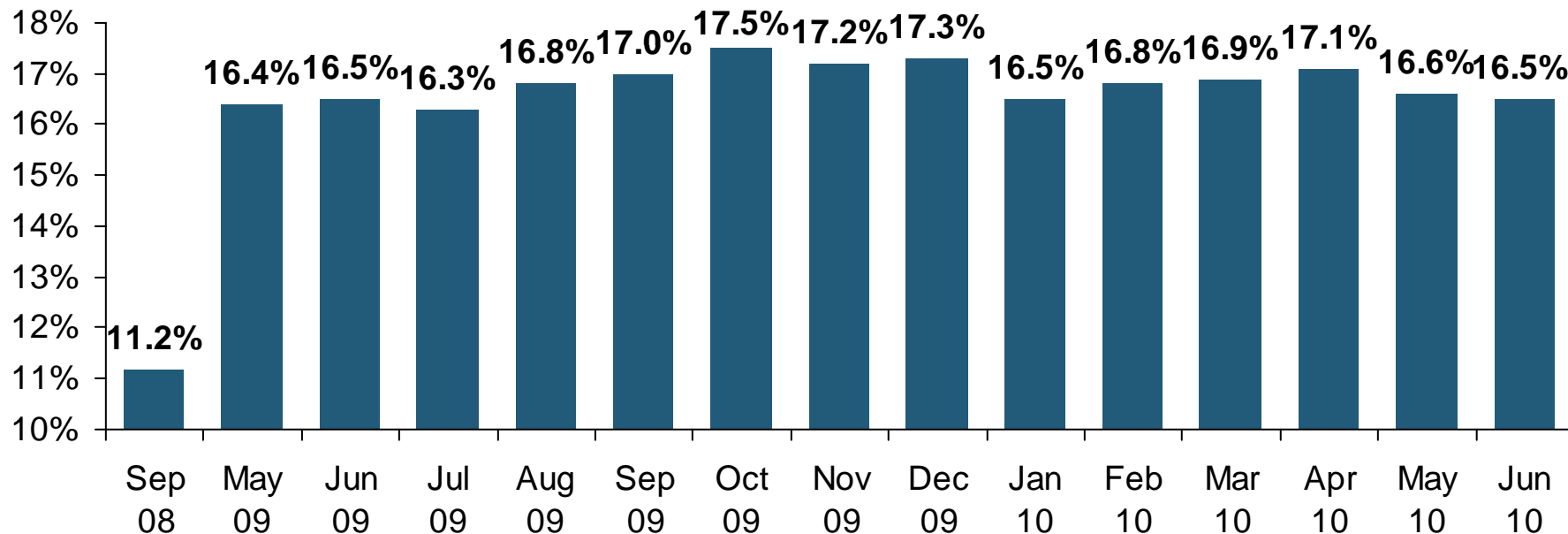
Job Losses Since the Recession Began in Dec. 2007 Peaked at 8.4 Mill in Dec. 09; Stands at 7.4 Million Through June 2010; 14.6 Million People are Now Defined as Unemployed

*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



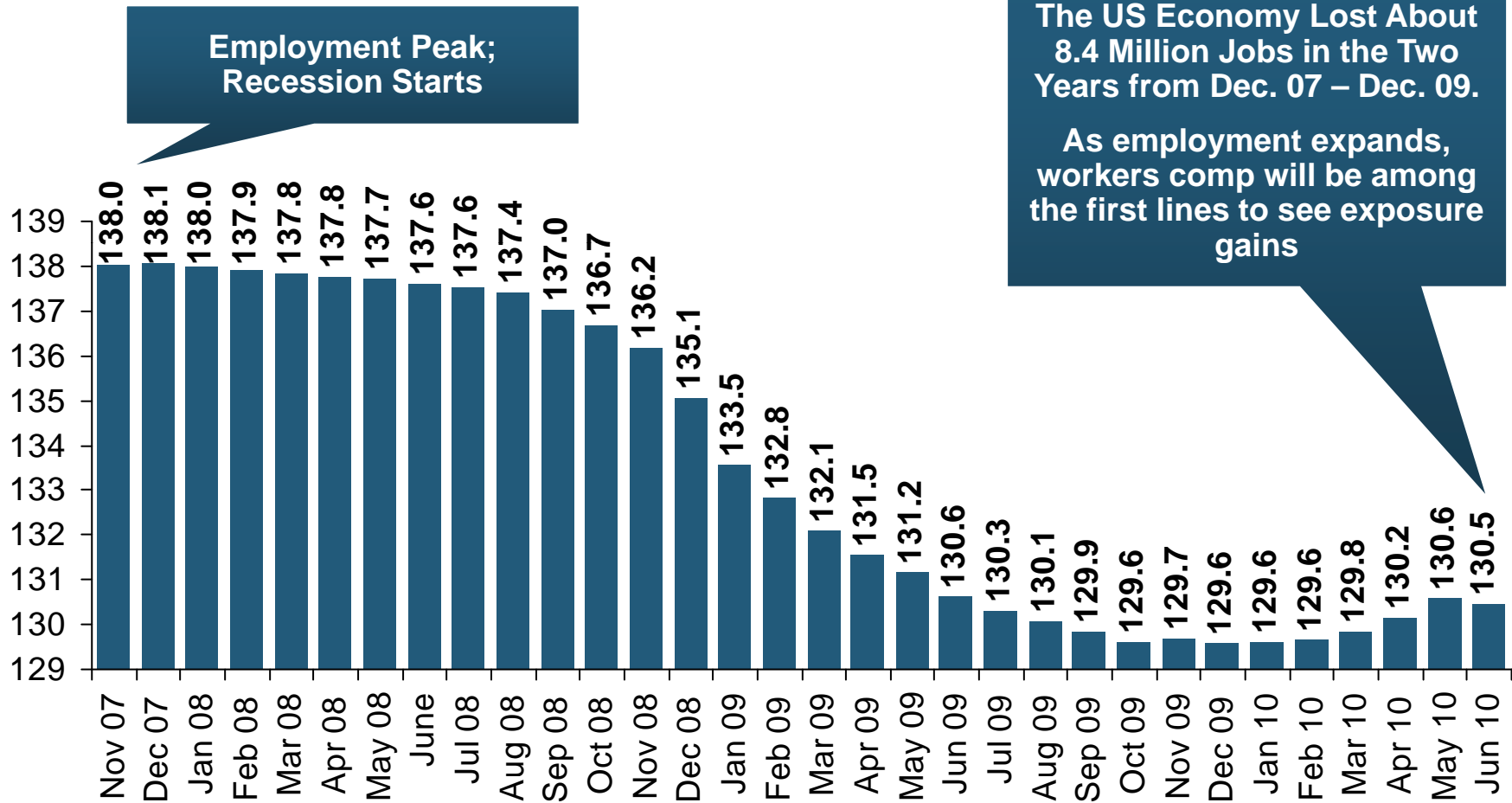
Marginally Attached and Unemployed Persons Account for 16.5% of the Labor Force in June 2010 (1 Out 6 People). Unemployment Rate Alone was 9.5%. Underutilization Shows a Broader Impact on WC and Other Commercial Exposures

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)

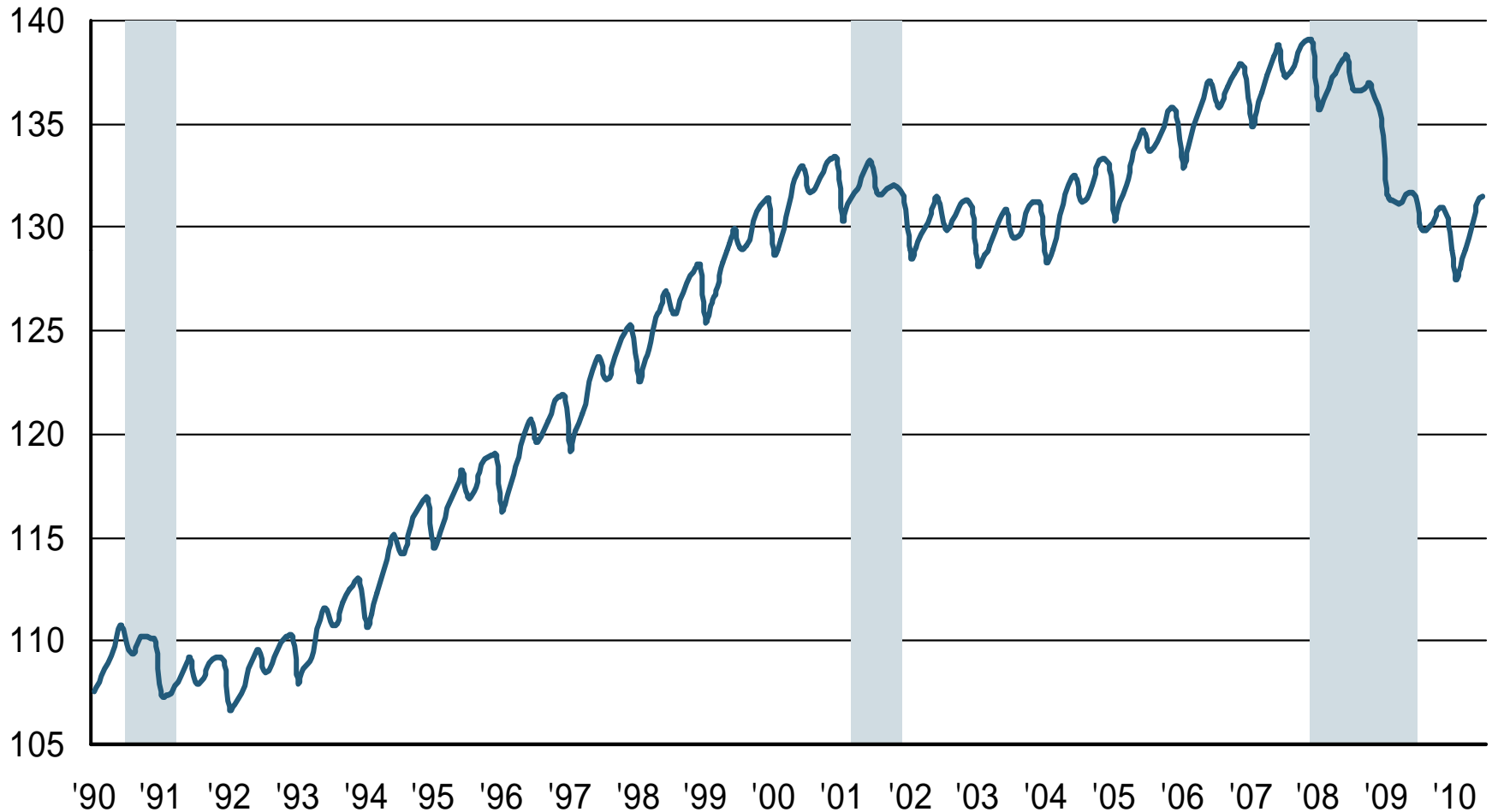


Seasonally adjusted.

Source: US Bureau of Labor Statistics

U.S. Nonfarm Employment, Monthly, 1990–2010*

Millions



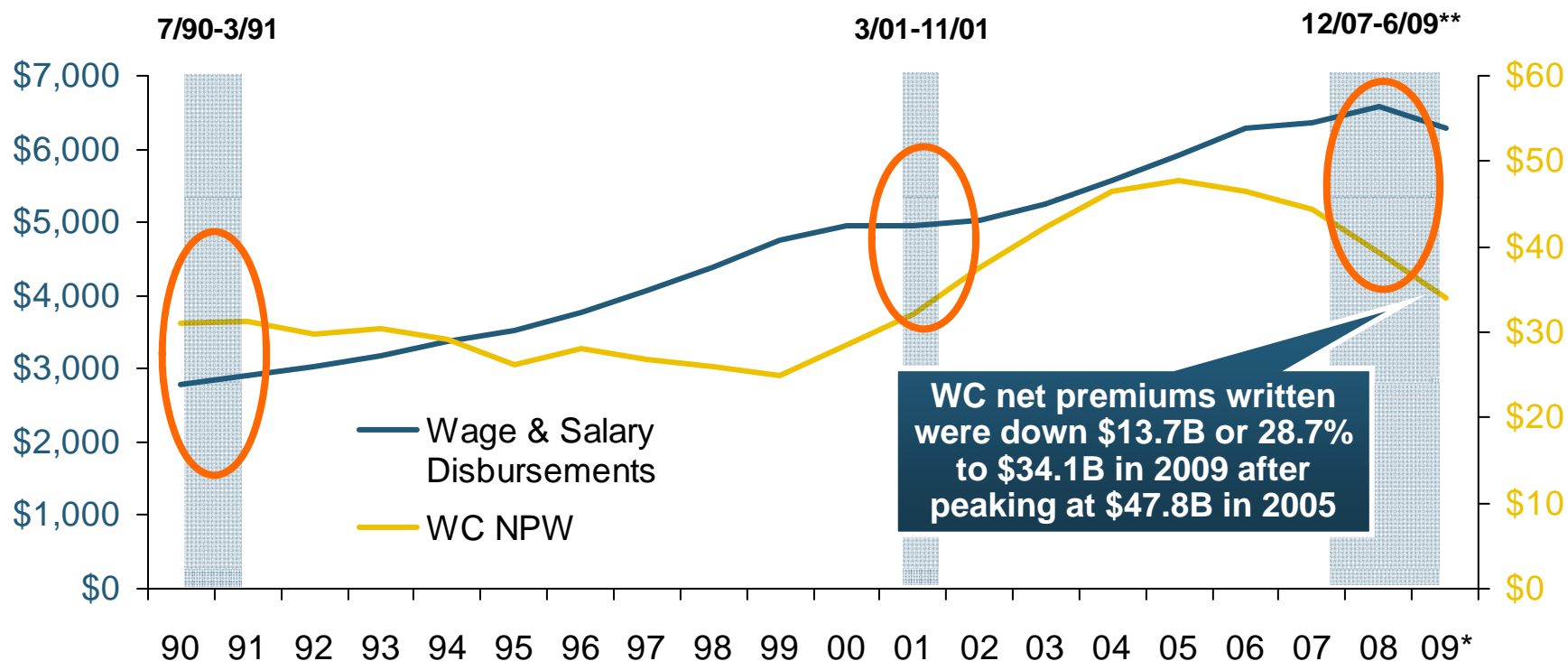
*As of June 2010; Not seasonally adjusted

Note: Recessions indicated by gray shaded columns.

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

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

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



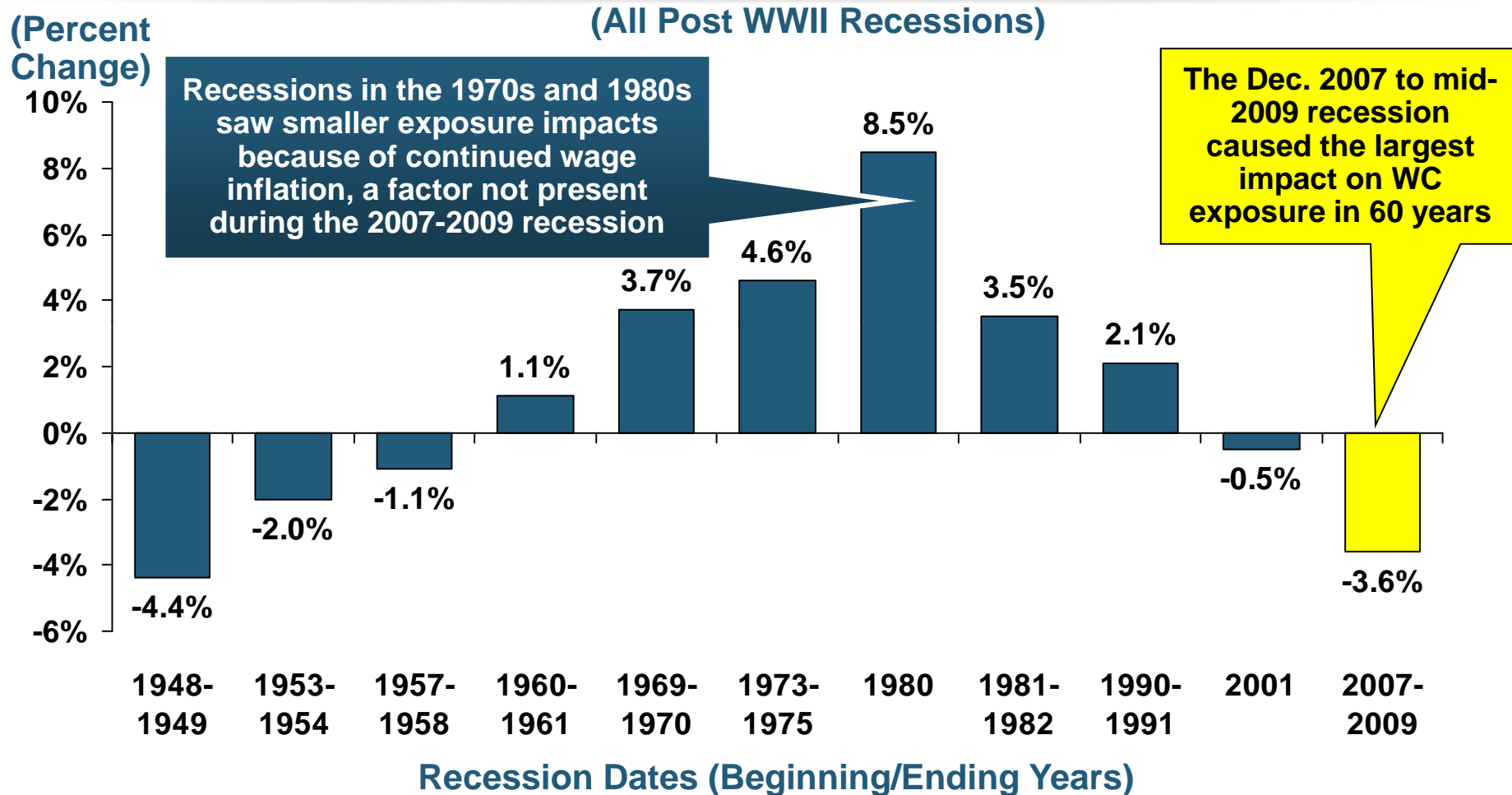
Weakening Payrolls Have Eroded \$2B+ in Workers Comp Premiums; Nearly 29% of NPW Has Been Eroded Away by the Soft Market and Weak Economy

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

**Estimated "official" end of recession June 2009.

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).

Contributions to WC Net Written Premium Decline

Calendar Years 2007–2009

2-Year Change in Countrywide NWP

-23%

Known Pricing Impacts

Change in Bureau Rates and Loss Costs **-7%**

Change in Carrier Pricing **-4%**

Economic Impacts

Change in Total Payroll **-4%**

Impact of Recession on Industry Group Mix **-4% to -6%**

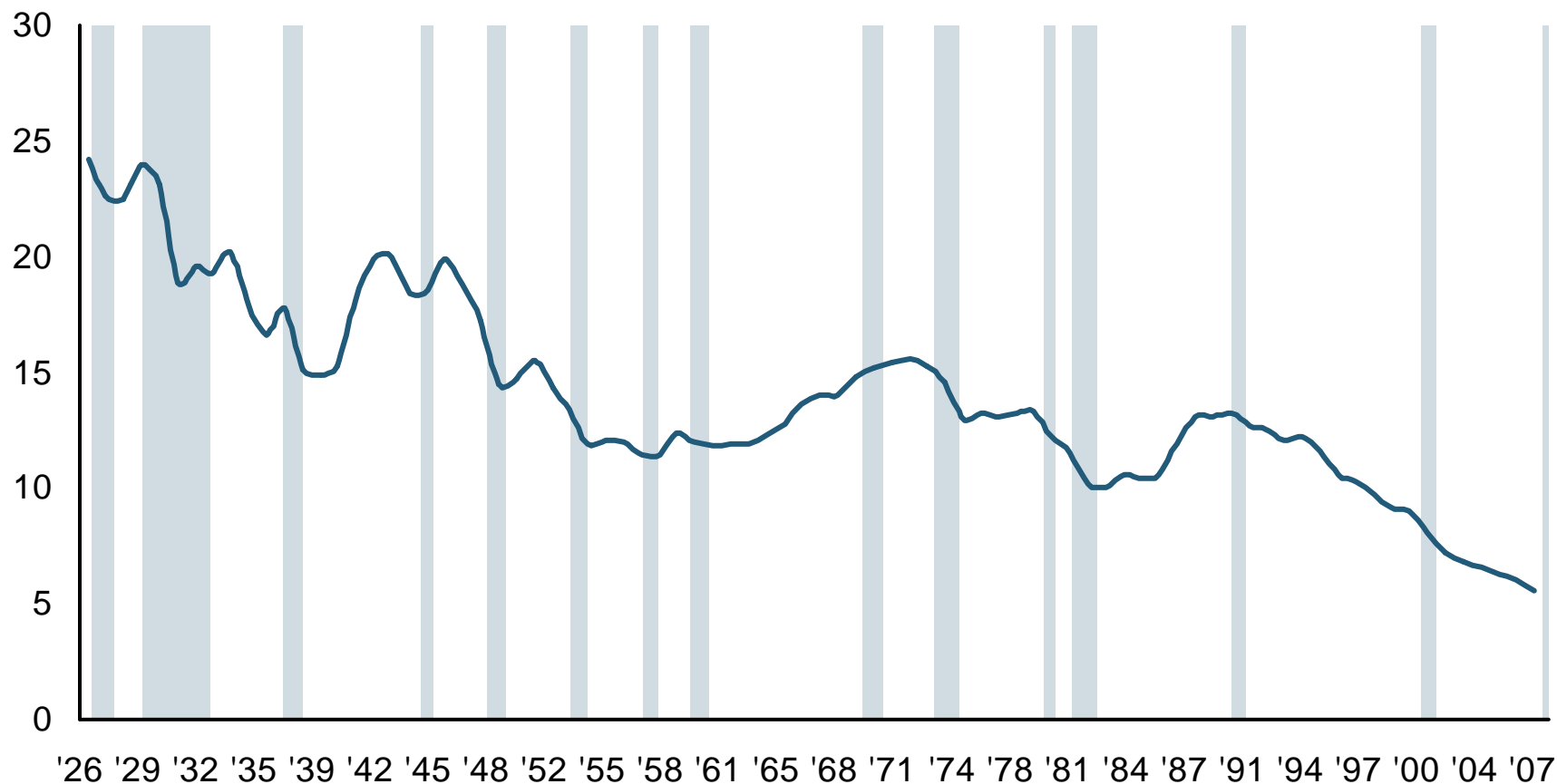
Impact of Recession by Firm Size **-4% to -6%**

Other Impacts **+1% to -2%**

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

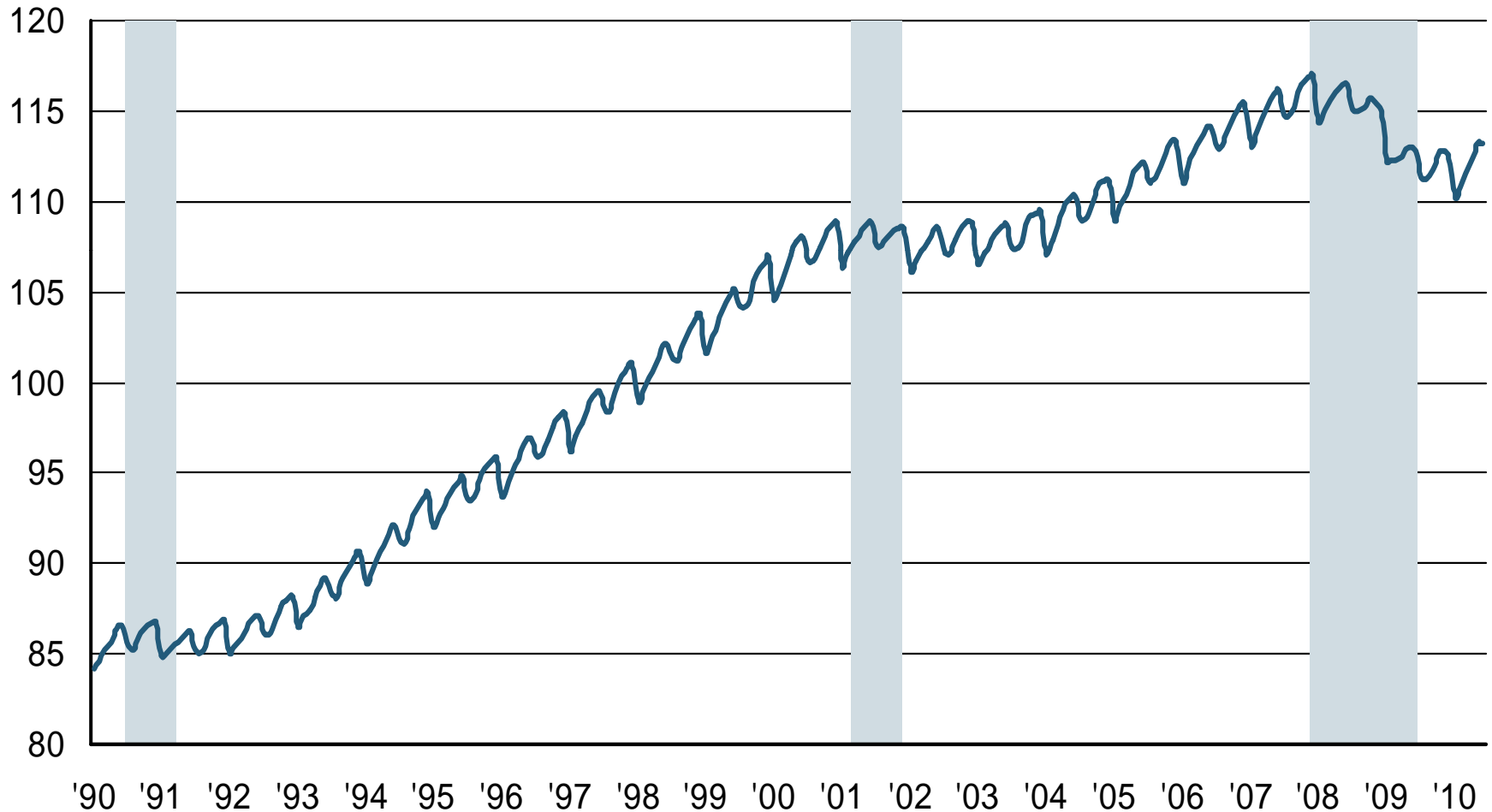


Insurance Industry Employment Trends

**Soft Market, Difficult Economy,
Outsourcing Have Contributed to
Industry's Job Losses**

U.S. Employment in Service Industries, Monthly, 1990–2010*

Millions



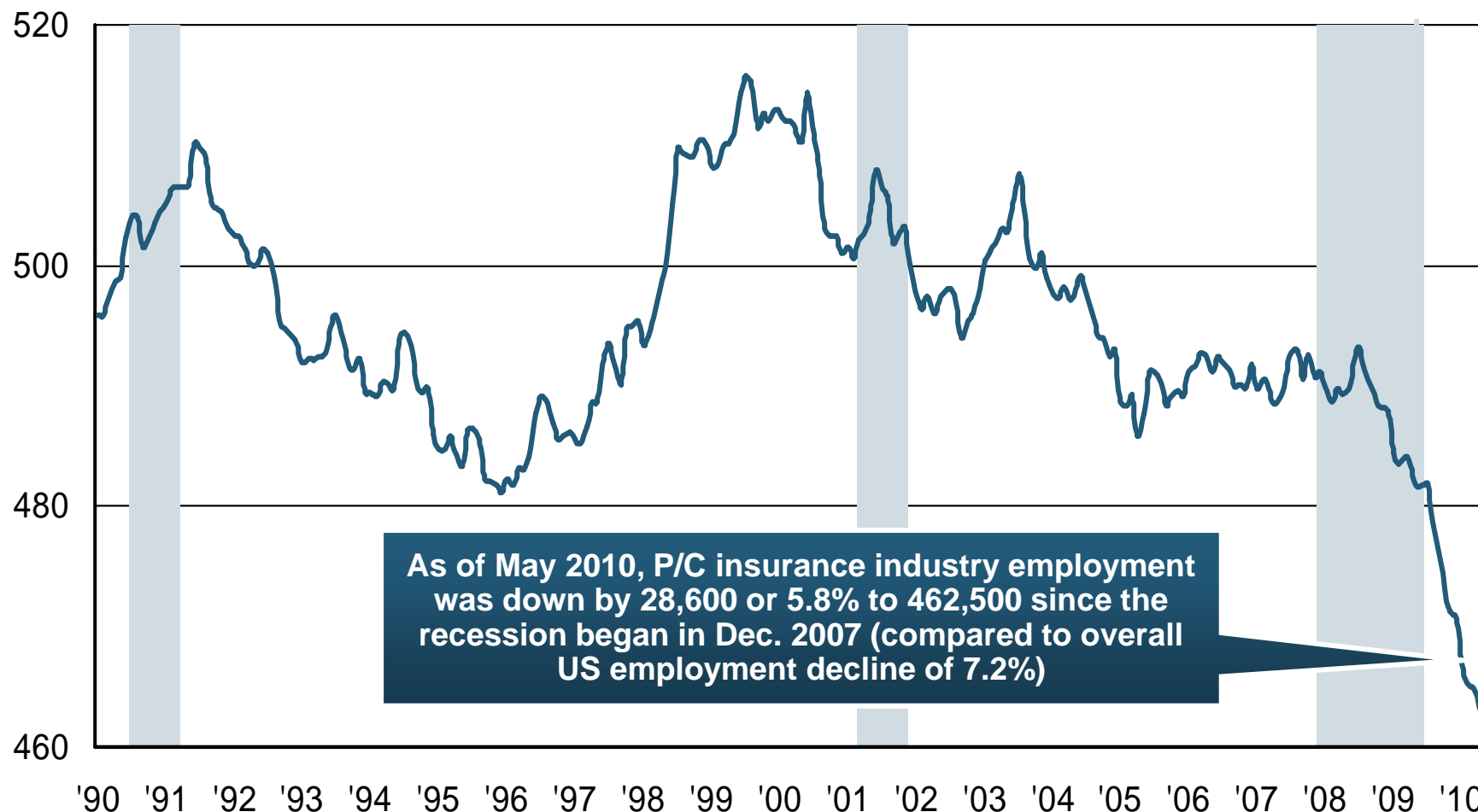
*As of June 2010; Not seasonally adjusted

Note: Recessions indicated by gray shaded columns.

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

U.S. Employment in the Direct P/C Insurance Industry: 1990–2010*

Thousands



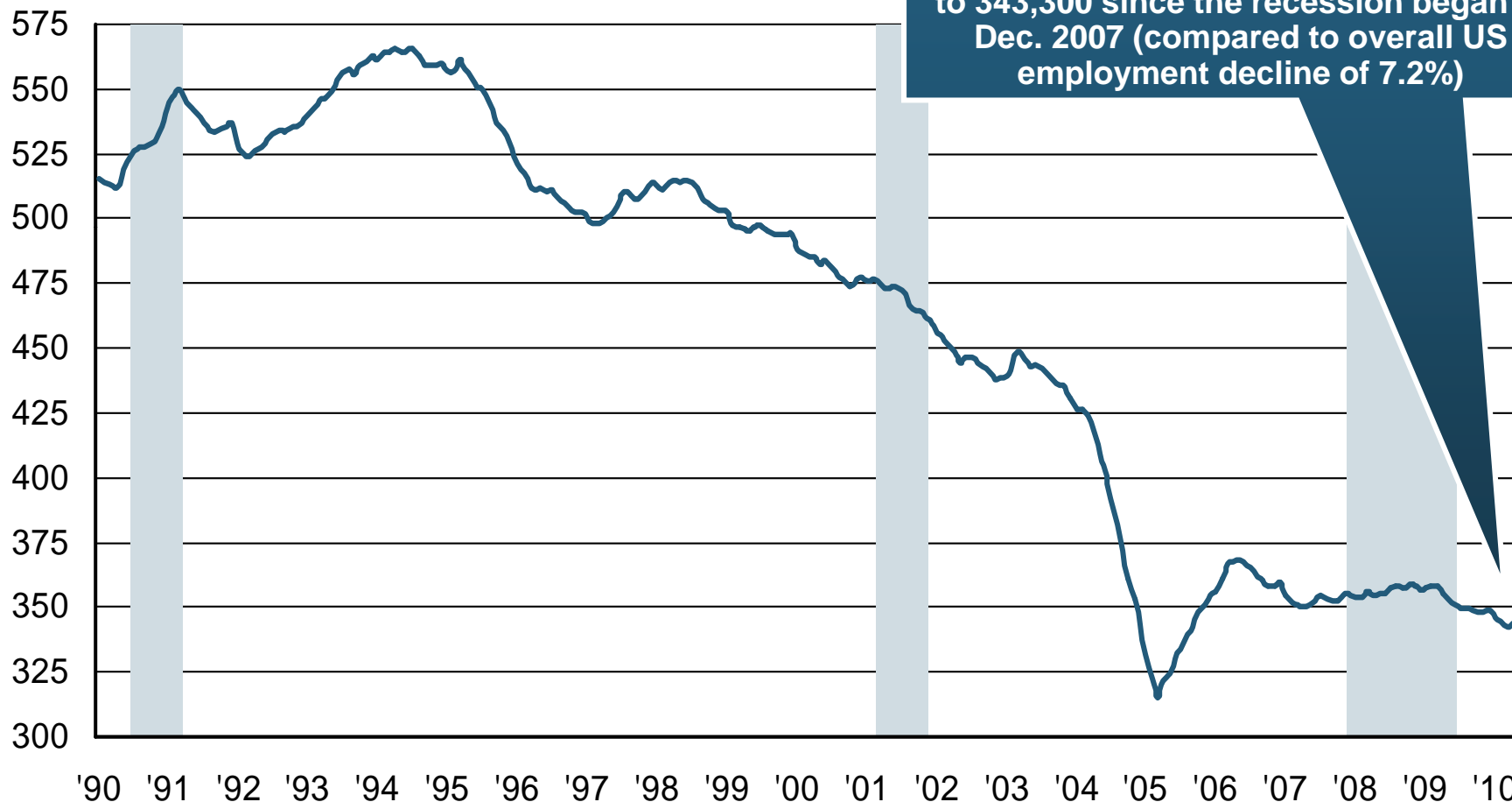
*As of May 2010; Not seasonally adjusted; Does not including agents & brokers

Note: Recessions indicated by gray shaded columns.

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

U.S. Employment in the Direct Life Insurance Industry: 1990–2010*

Thousands



As of May 2010, Life insurance industry employment was down by 11,100 or 3.1% to 343,300 since the recession began in Dec. 2007 (compared to overall US employment decline of 7.2%)

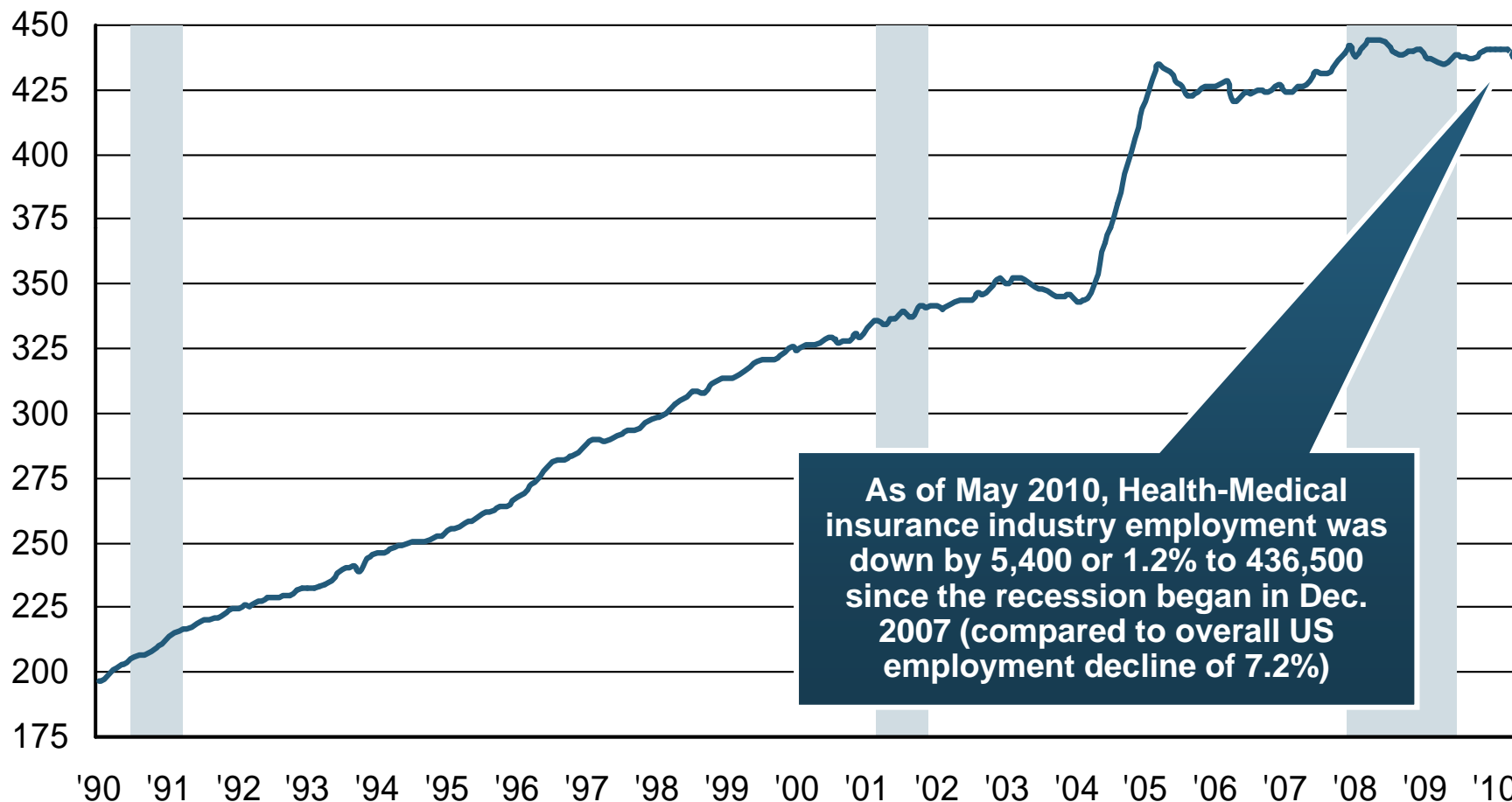
*As of May 2010; Not seasonally adjusted; Does not including agents & brokers

Note: Recessions indicated by gray shaded columns.

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

U.S. Employment in the Direct Health-Medical Insurance Industry: 1990–2010*

Thousands



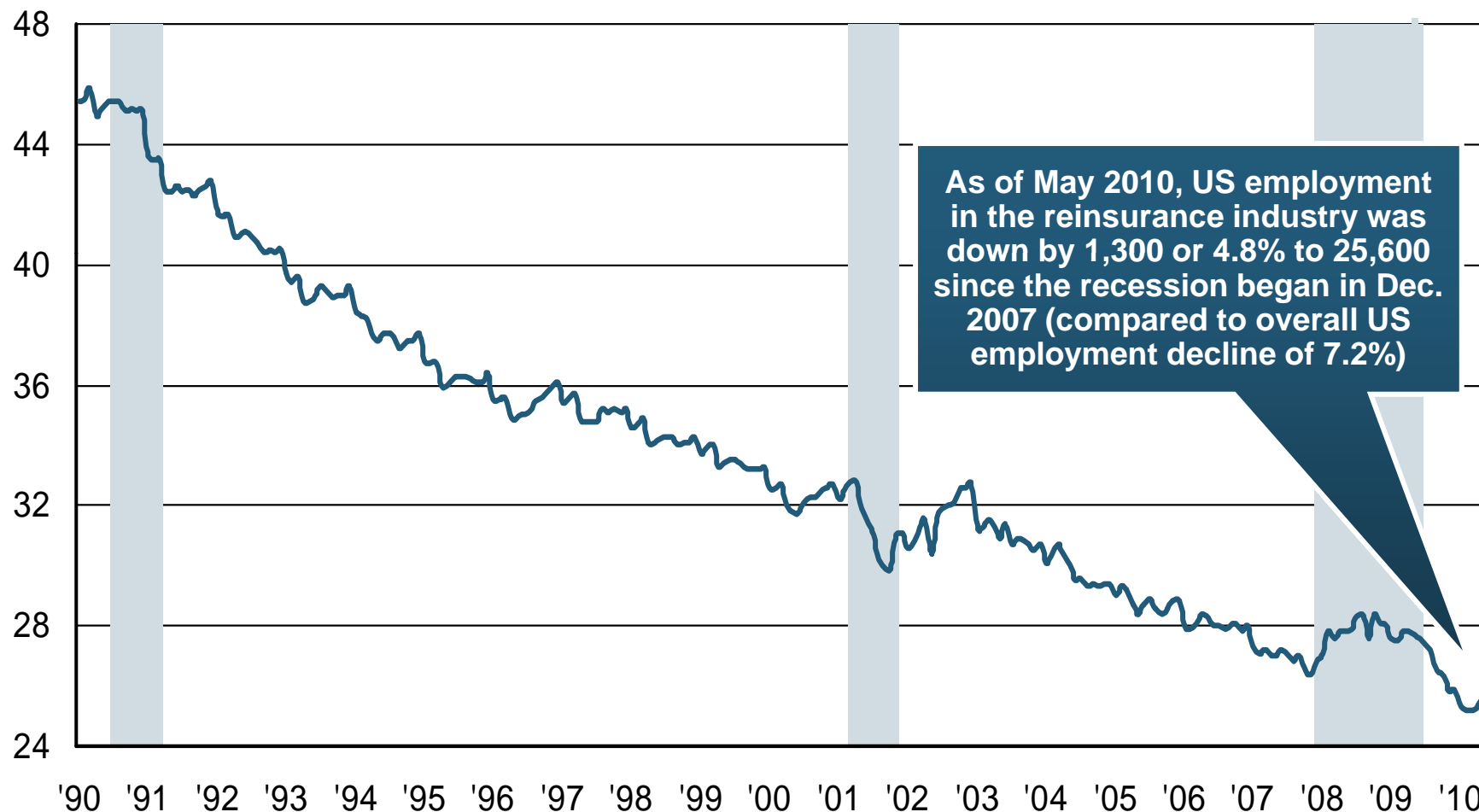
*As of May 2010; Not seasonally adjusted; Does not including agents & brokers

Note: Recessions indicated by gray shaded columns.

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

U.S. Employment in the Reinsurance Industry: 1990–2010*

Thousands



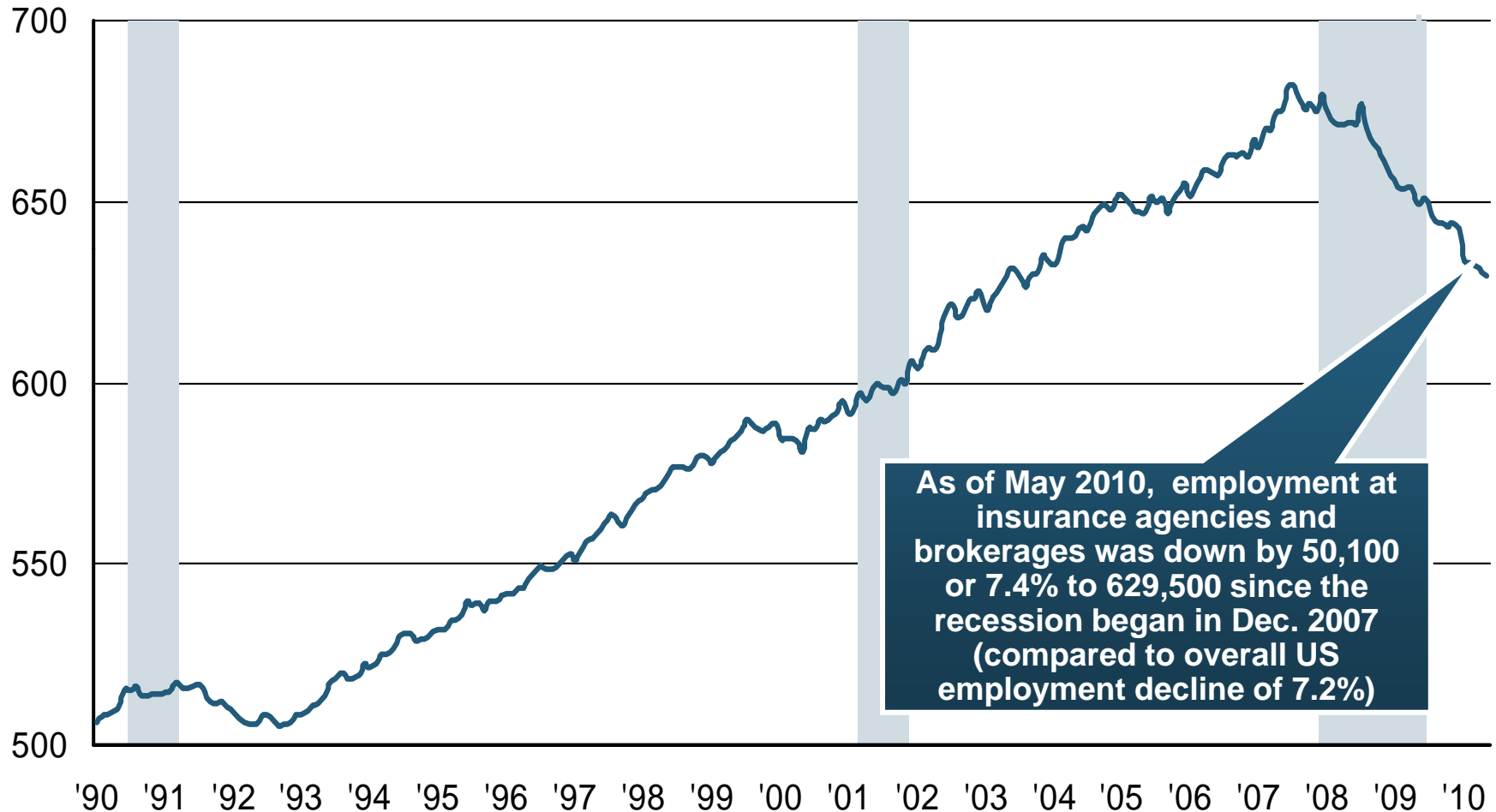
*As of May 2010; Not seasonally adjusted; Does not including agents & brokers

Note: Recessions indicated by gray shaded columns.

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

U.S. Employment in Insurance Agencies & Brokerages: 1990–2010*

Thousands



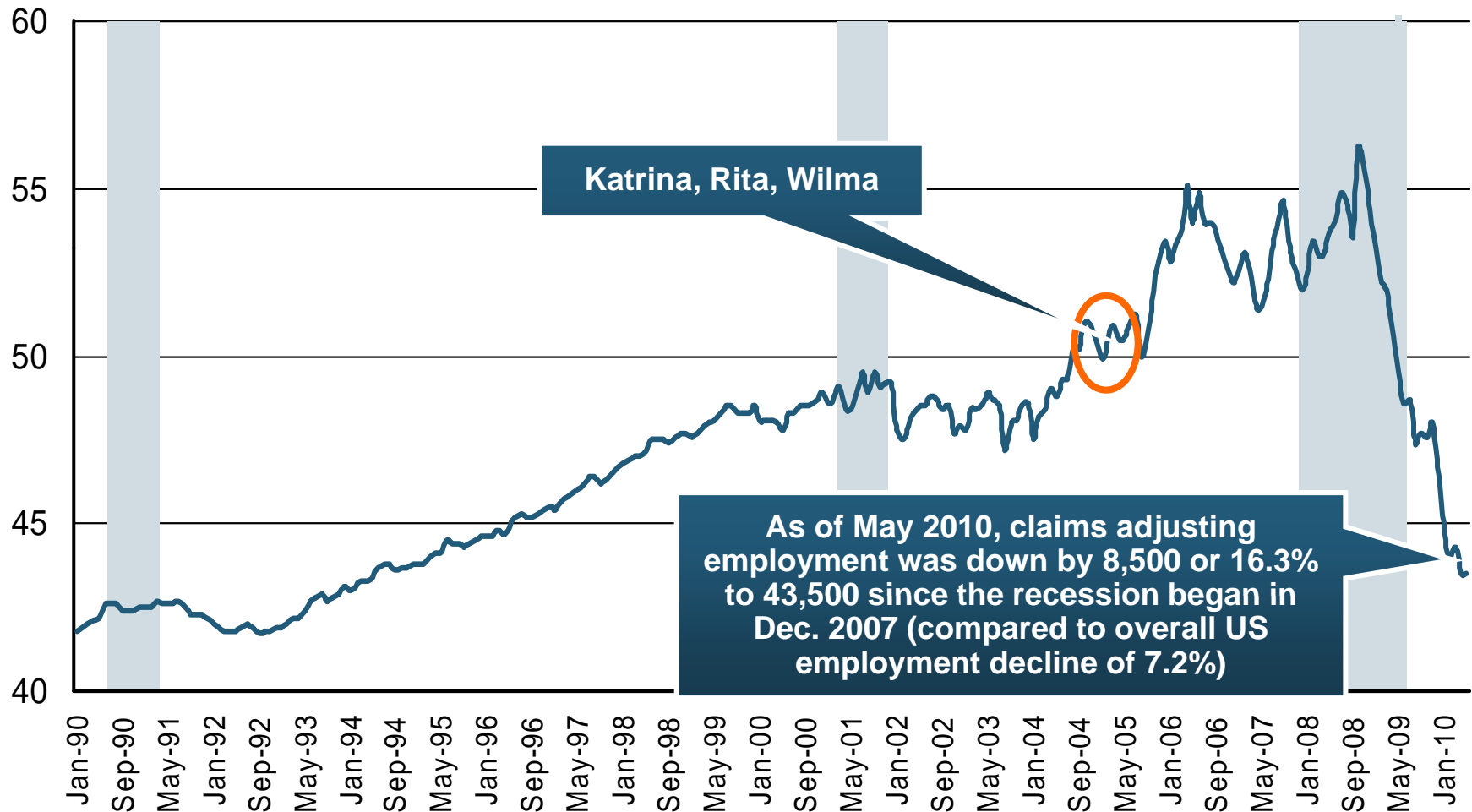
*As of May 2010; Not seasonally adjusted. Includes all types of insurance.

Note: Recessions indicated by gray shaded columns.

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

U.S. Employment in Insurance Claims Adjusting: 1990–2010*

Thousands



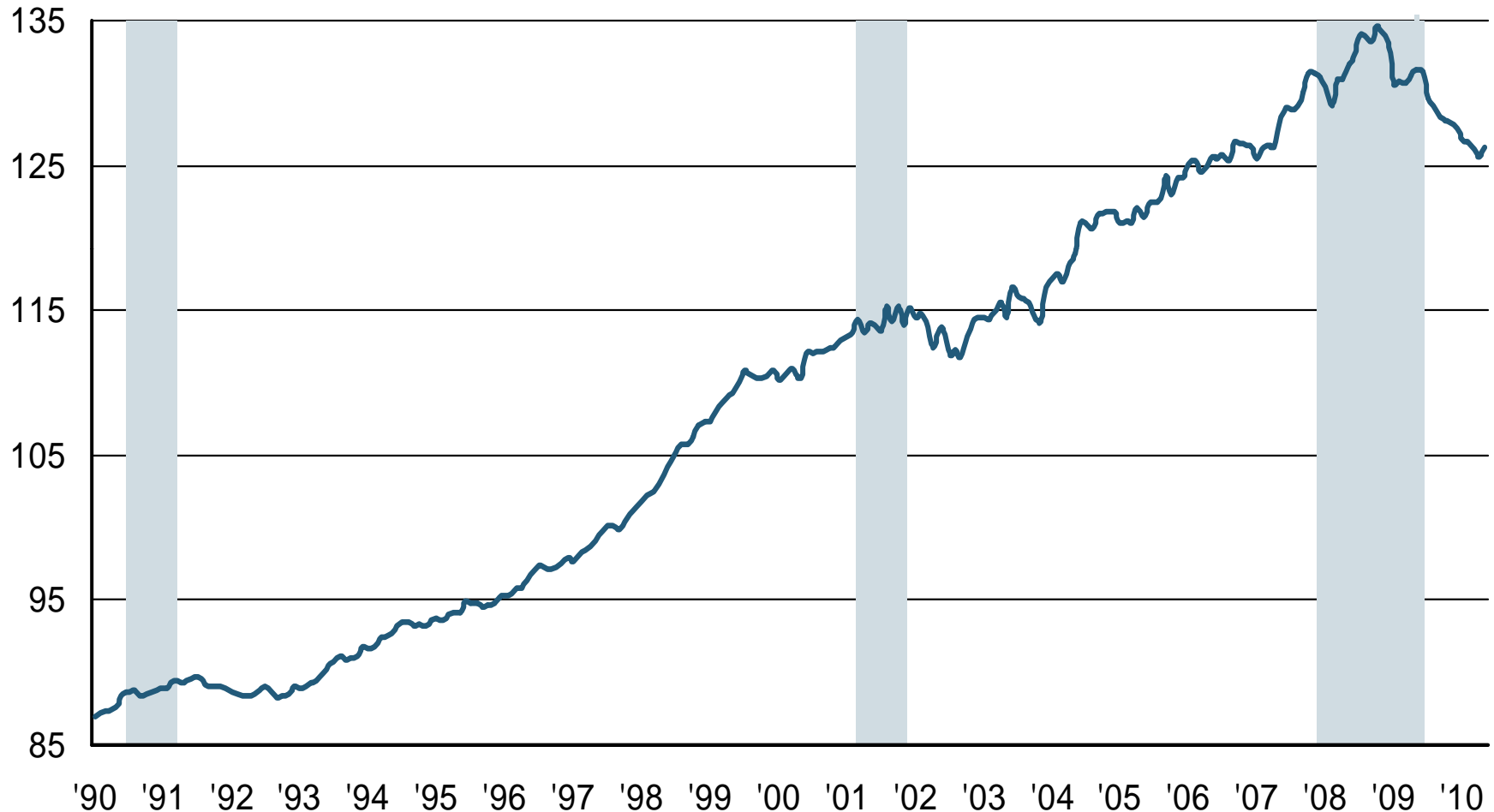
*As of May 2010; Not seasonally adjusted.

Note: Recessions indicated by gray shaded columns.

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

U.S. Employment in Third-Party Administration of Insurance Funds: 1990–2010*

Thousands



*As of May 2010; Not seasonally adjusted. Includes all types of insurance.

Note: Recessions indicated by gray shaded columns.

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

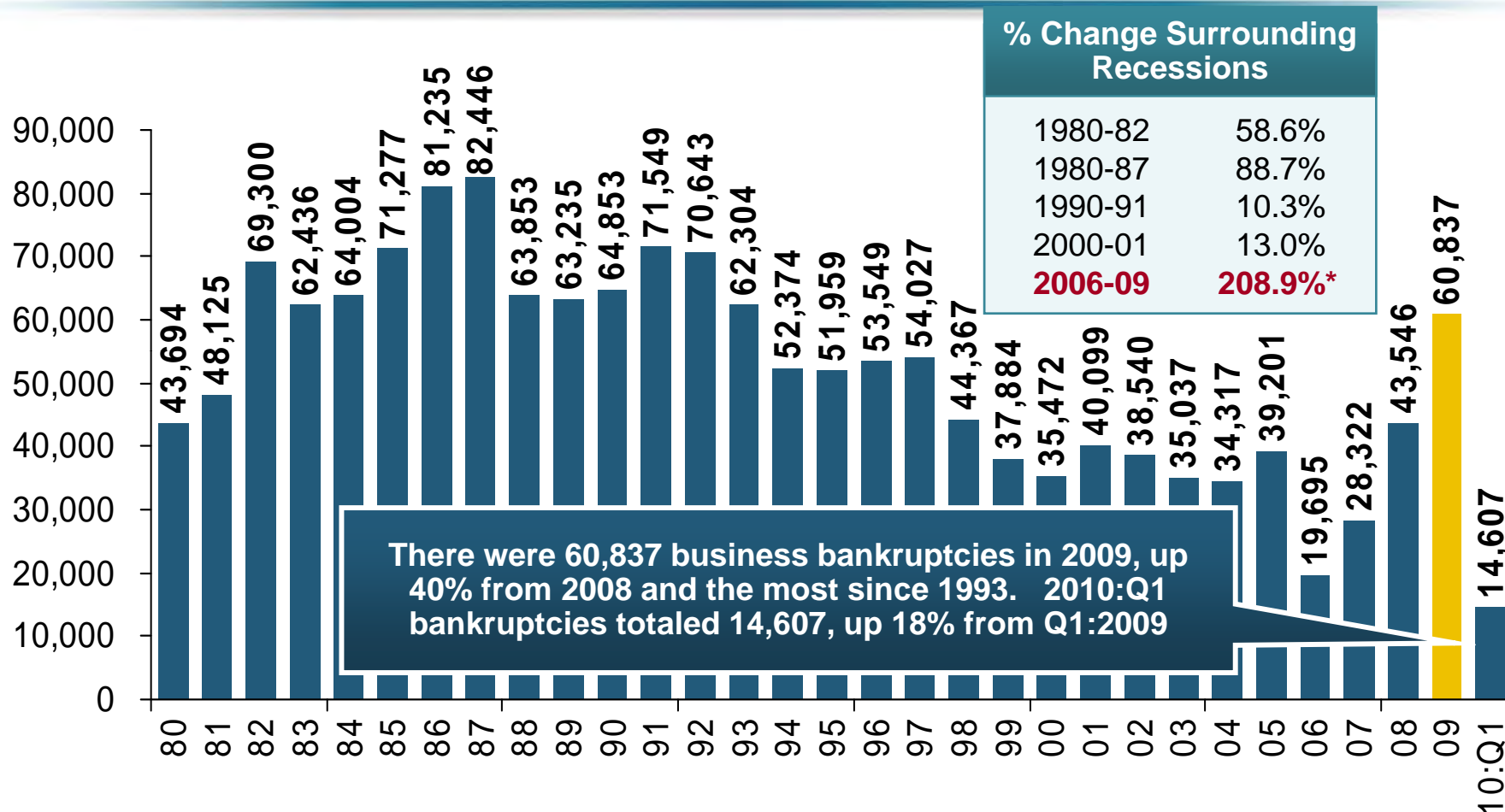


Crisis and Recovery-Driven Exposure Drivers in WC

**Myriad of Impacts on Workers
Comp Exposure**

Filling the Economic Crater

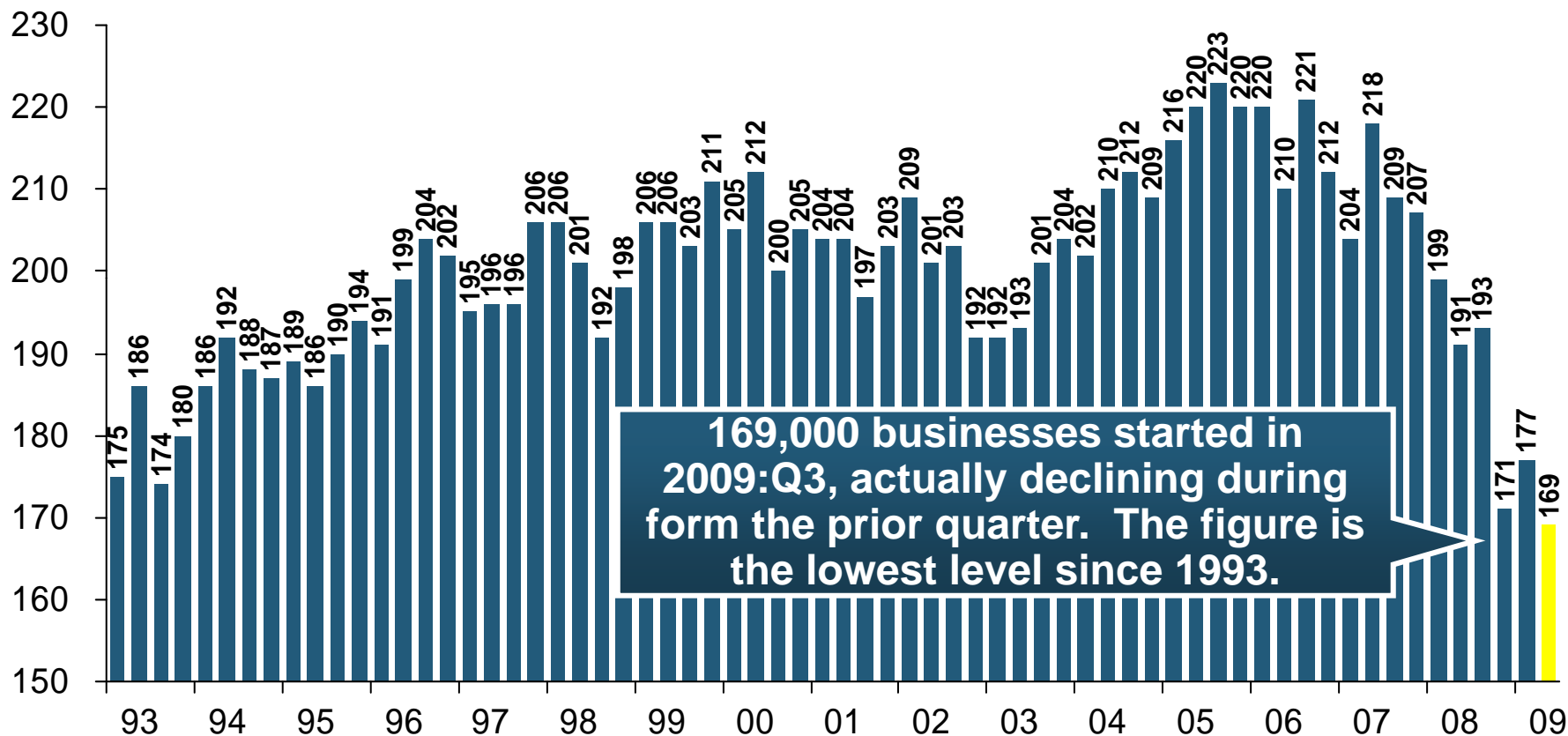
Business Bankruptcy Filings, 1980-2010:Q1



Significant Exposure Implications for All Commercial Lines

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

(Thousands)



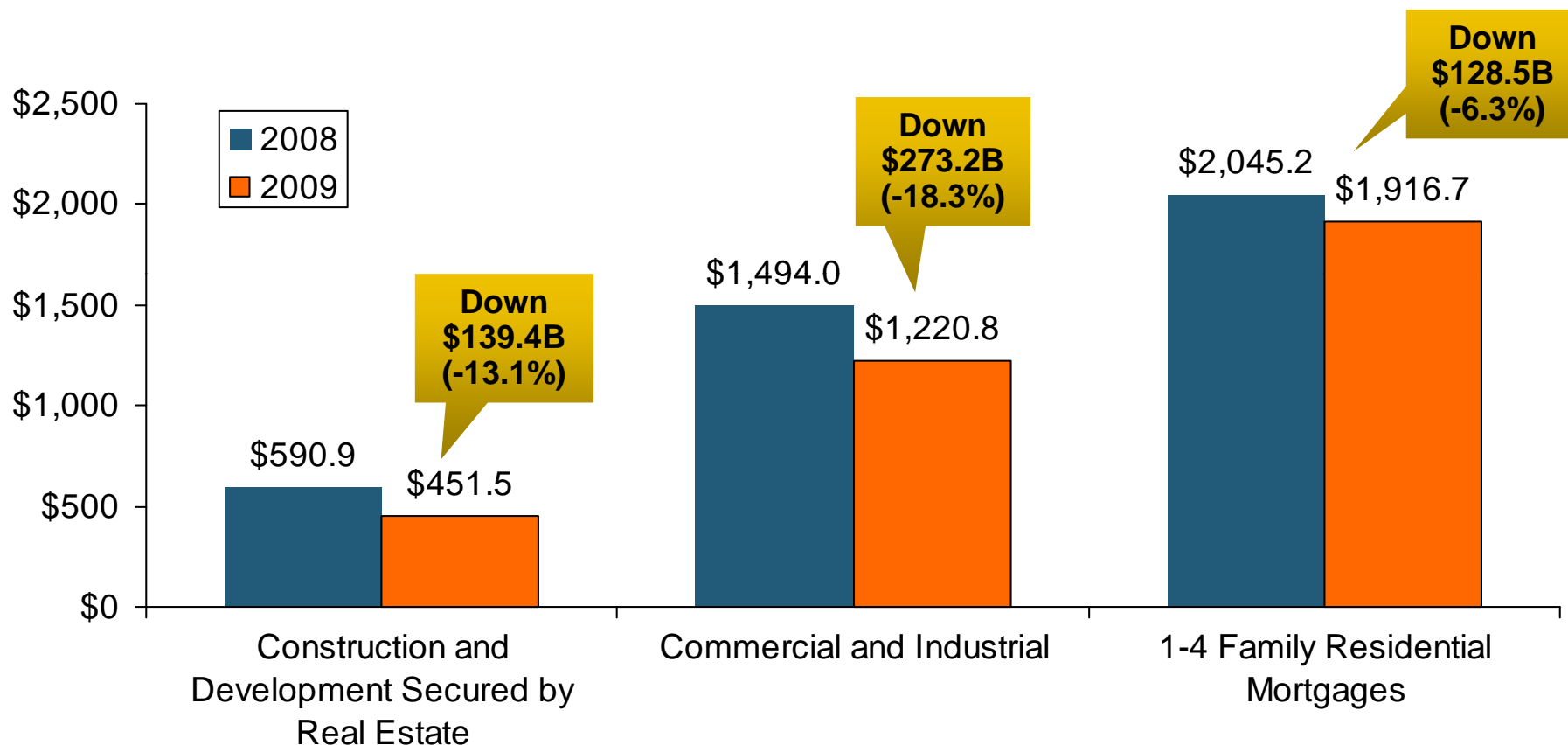
**Business Starts Are Down Nearly 20% in the Current Downturn,
Holding Back Most Types of Commercial Insurance Exposure**

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

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

Amount of Outstanding Loans by FDIC-Insured Institutions, 2009 vs. 2008

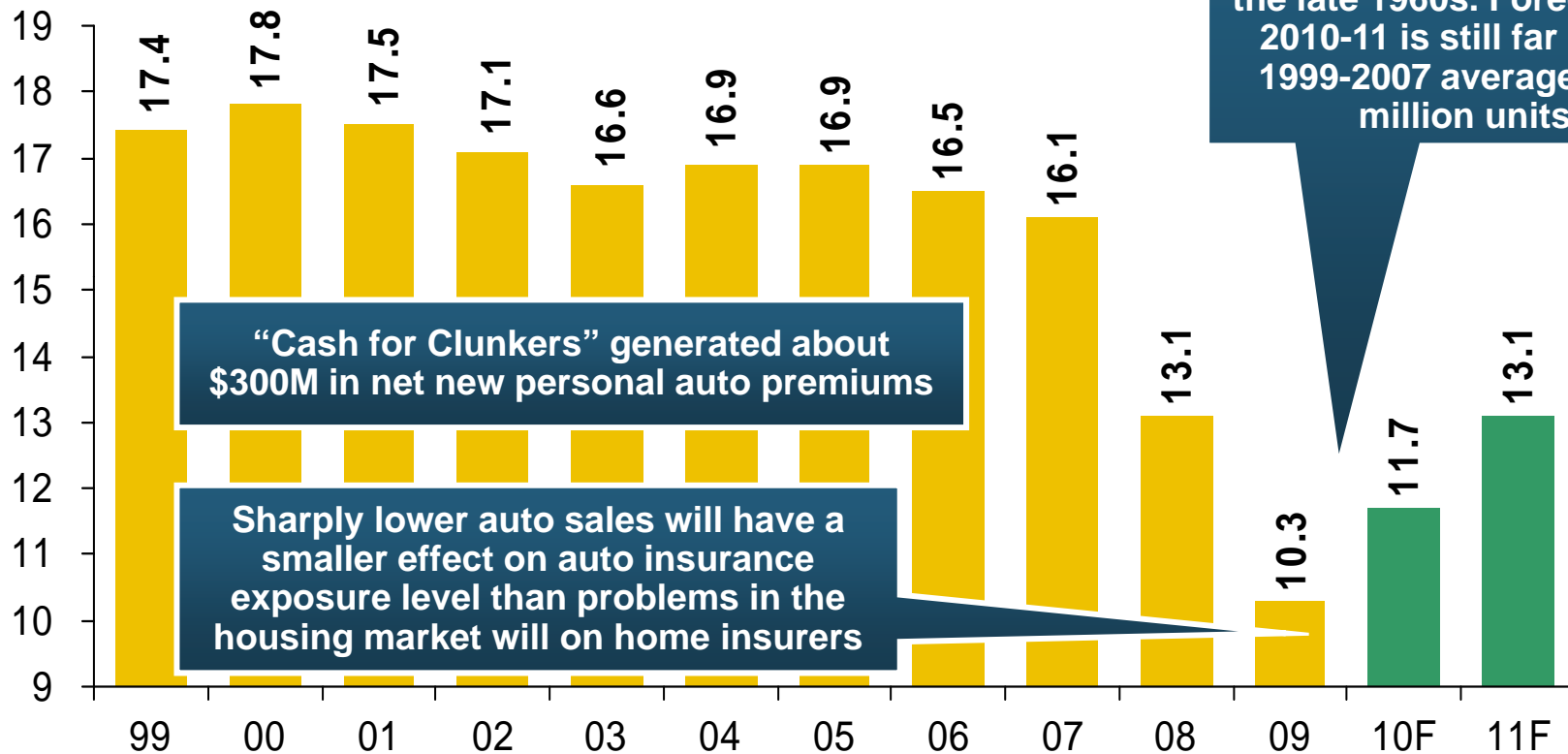
\$Billions



FDIC-Insured Institutions Had \$541.1B (-13.1%) Less in Outstanding Loans in These Three Categories at Year-end 2009 vs. 2008

Auto/Light Truck Sales, 1999-2011F

(Millions of Units)



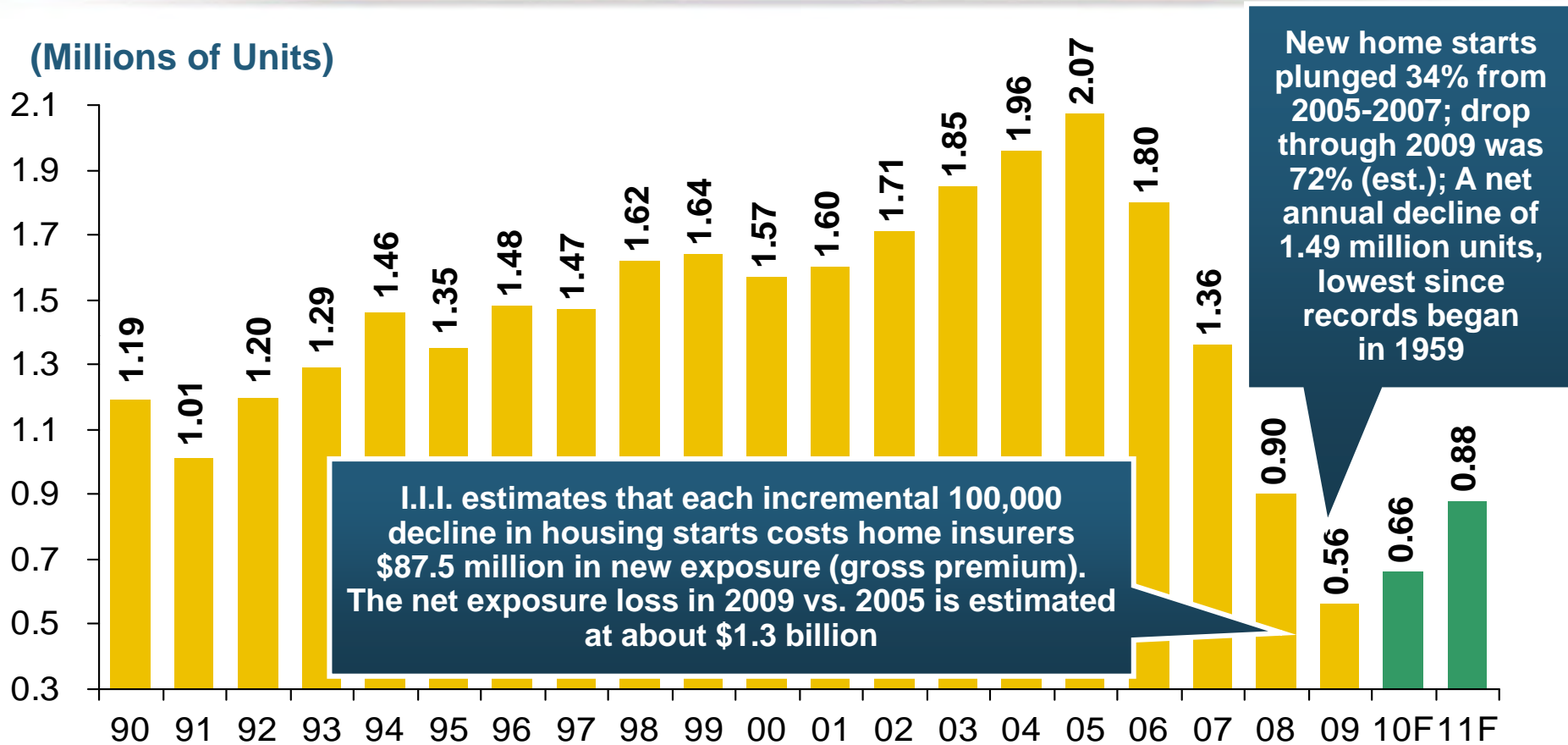
“Cash for Clunkers” generated about \$300M in net new personal auto premiums

Sharply lower auto sales will have a smaller effect on auto insurance exposure level than problems in the housing market will on home insurers

New auto/light truck sales fell to the lowest level since the late 1960s. Forecast for 2010-11 is still far below 1999-2007 average of 17 million units

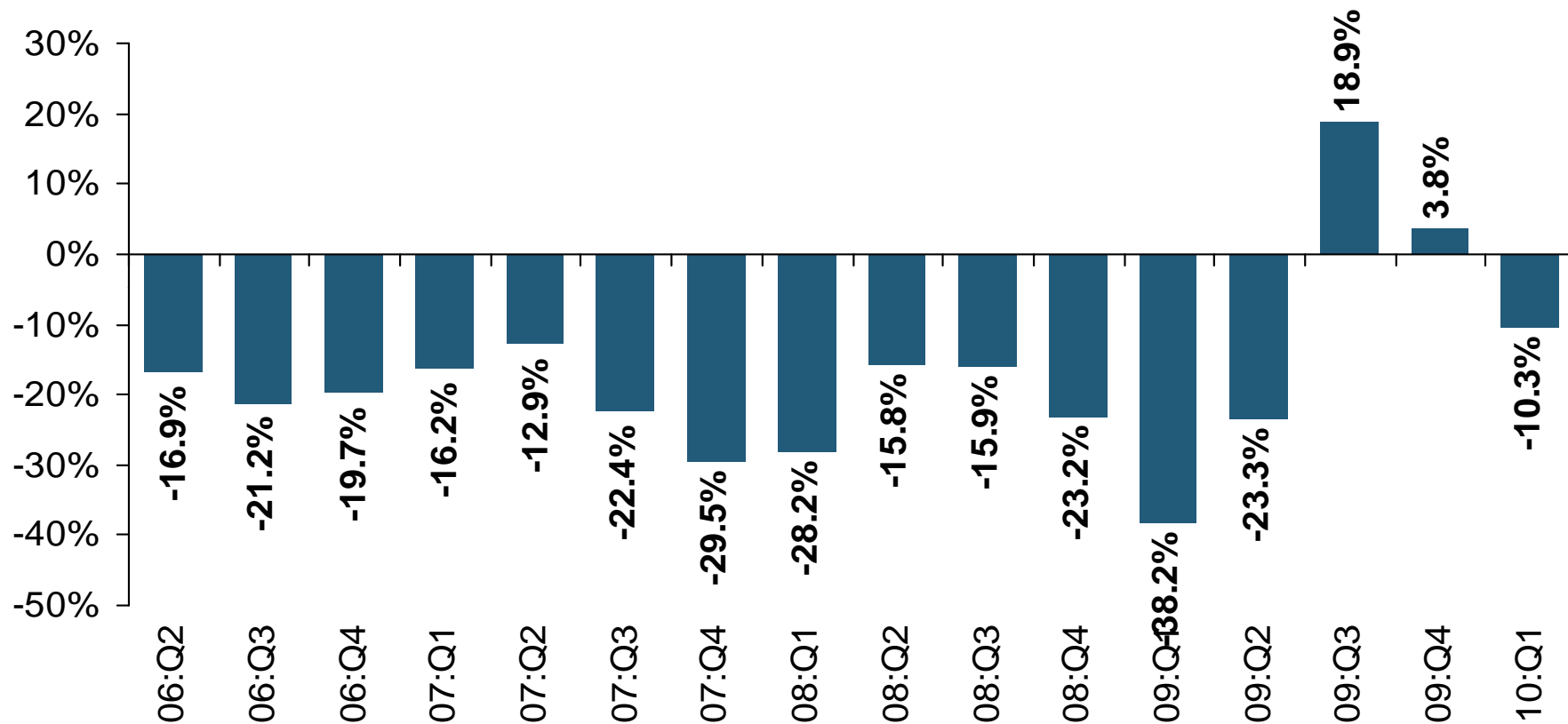
Car/Light Truck Sales Will Recover from the 2009 Low Point, but High Unemployment, Tight Credit Are Still Restraining Sales; Gas Prices Could Once Again Become a Factor, Too

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*

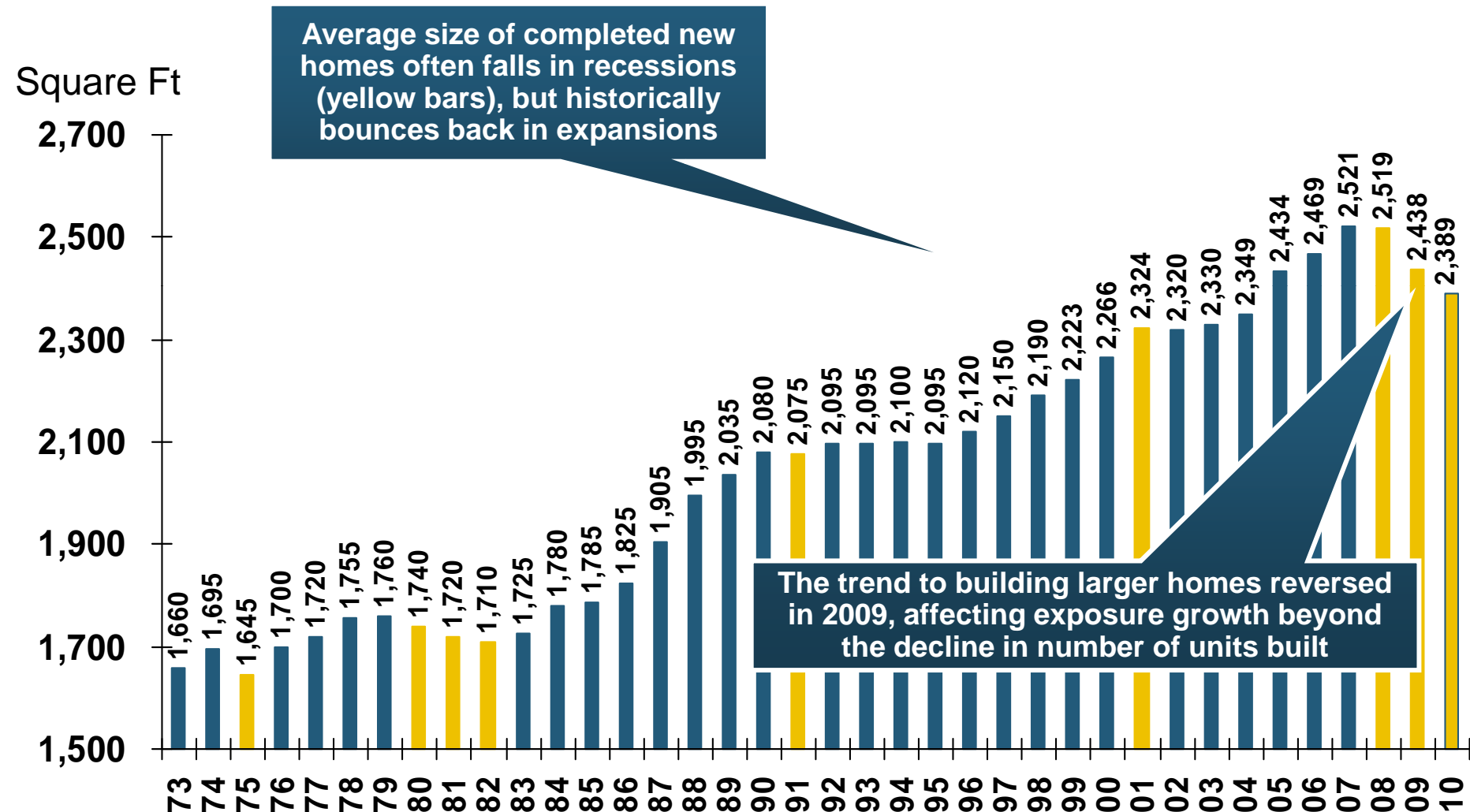


The Drop in 2006 is in Relation to the Record 2.07 Million Units Started in 2005; 1.8 Million Units Were Started That Year. The 2010:Q1 Drop Supports the Weak Home Construction Forecast for 2010-2011.

*seasonally adjusted

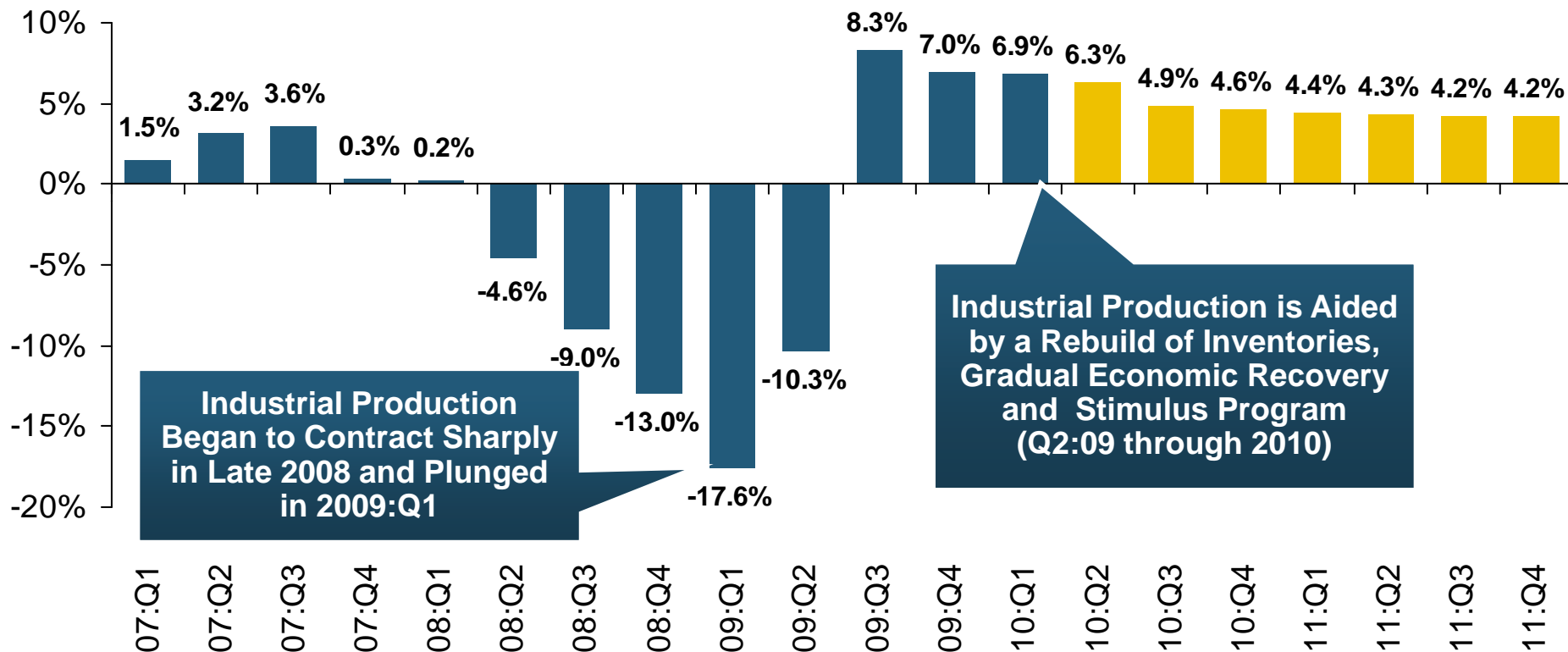
Source: U.S. Department of Commerce, Bureau of Economic Analysis

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



Total Industrial Production

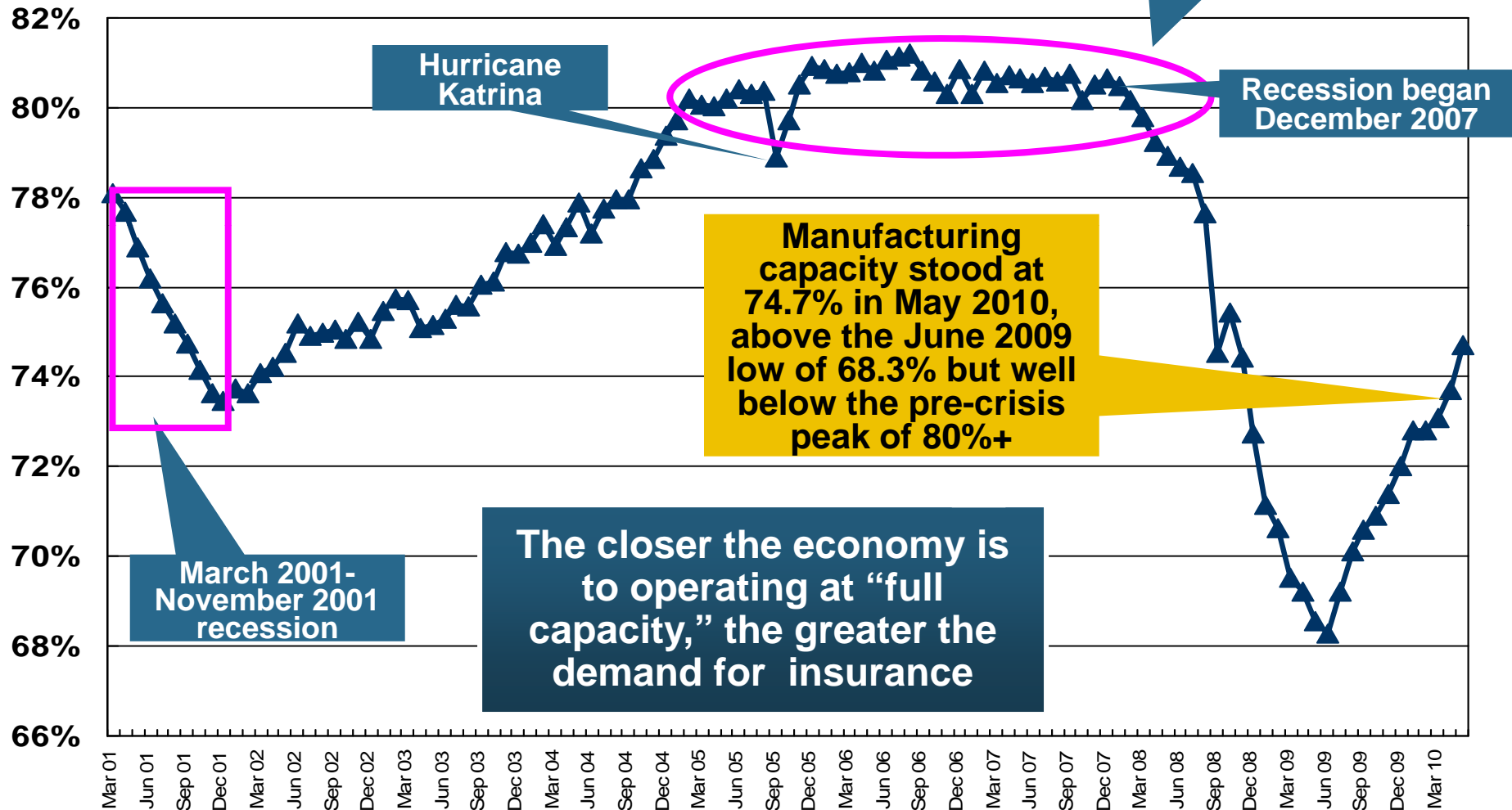
2007:Q1 to 2011:Q4F (%)



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

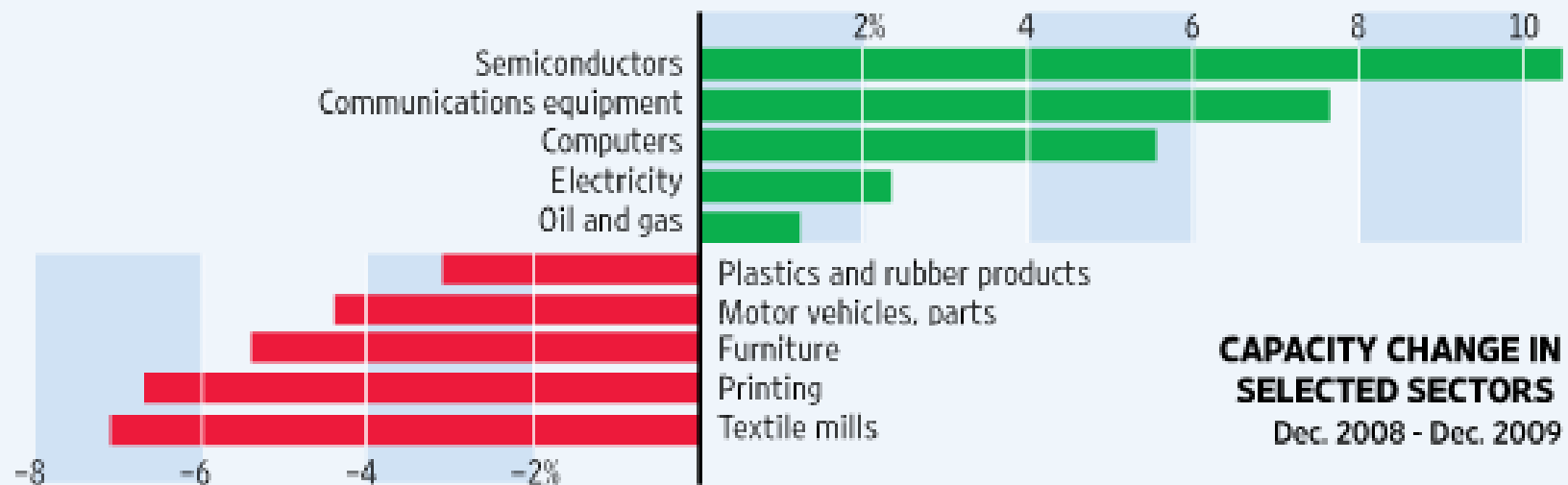


Source: Federal Reserve Board statistical releases at <http://www.federalreserve.gov/releases/g17/Current/default.htm>.

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.

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*

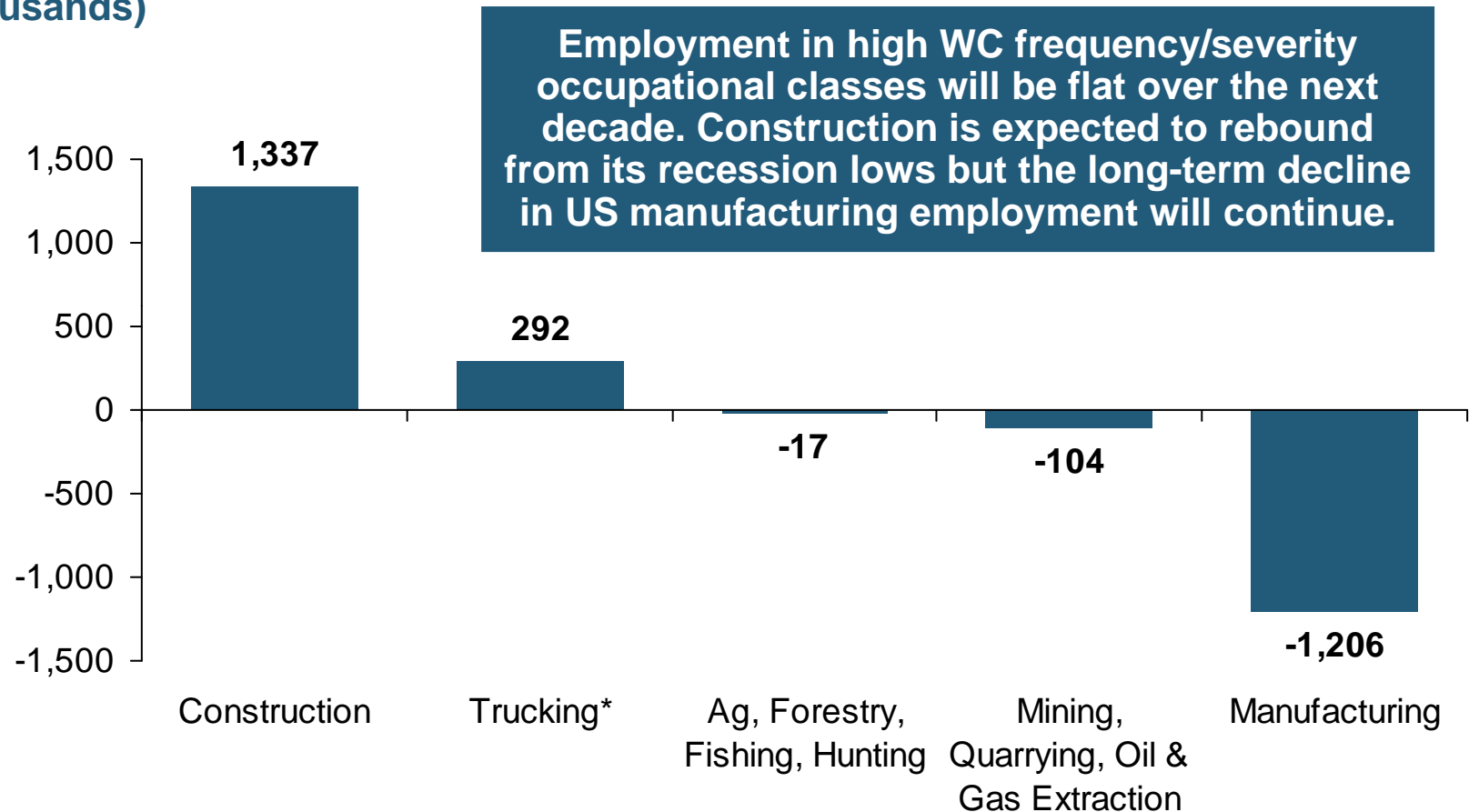
Dollar growth in WC exposures should grow the most (at current rate levels) in the health and services industries

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

(Thousands)

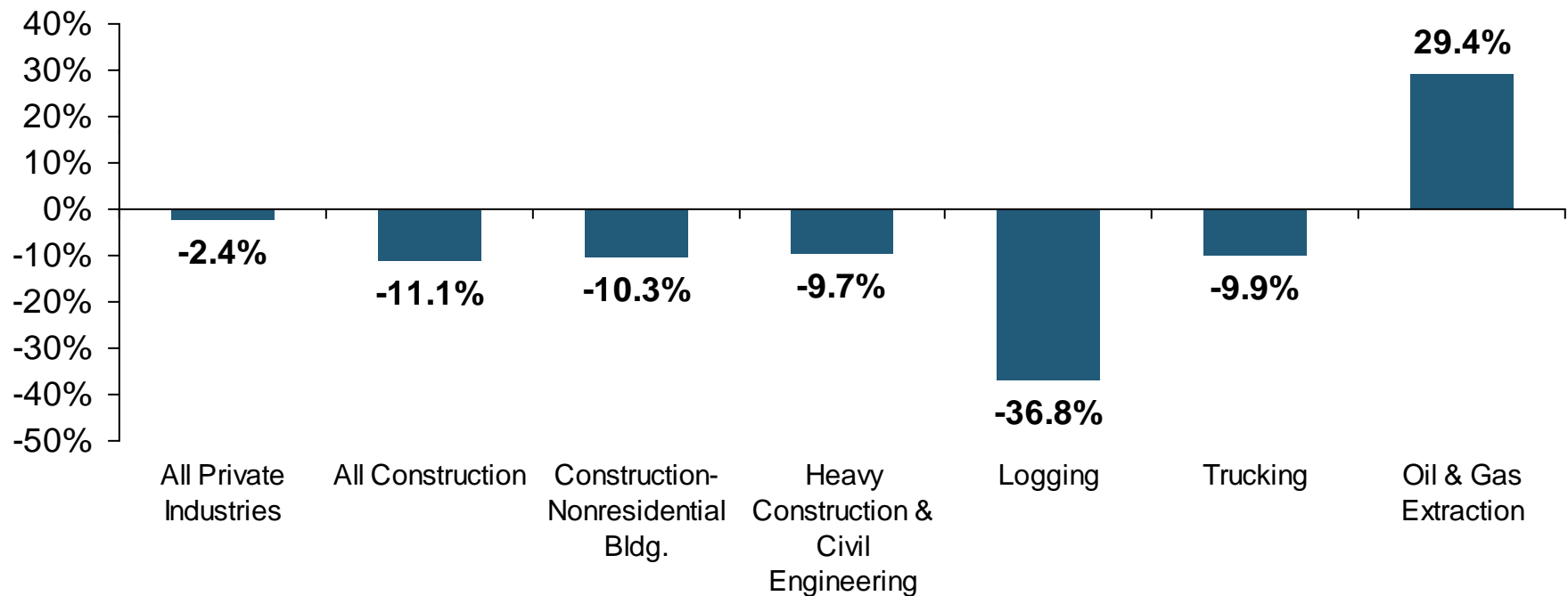


*Category includes truck drivers and drivers/sales personnel.

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*



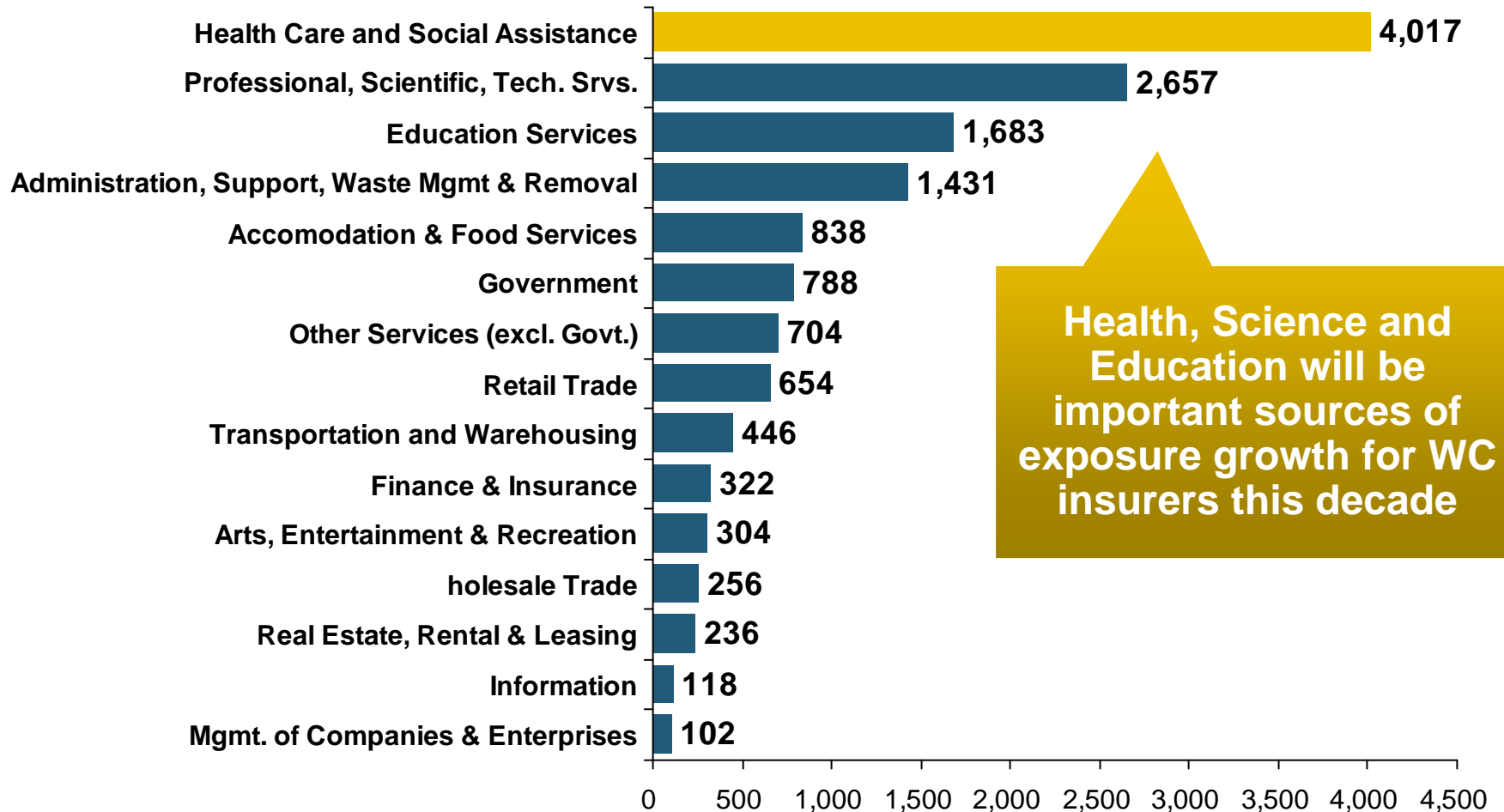
Most of the Loss of Jobs in High Hazard Classes Occurred Since 2007 with the Onset of the “Great Recession”

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

Source: US Bureau of Labor; Insurance Information Institute.

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

(Thousands)

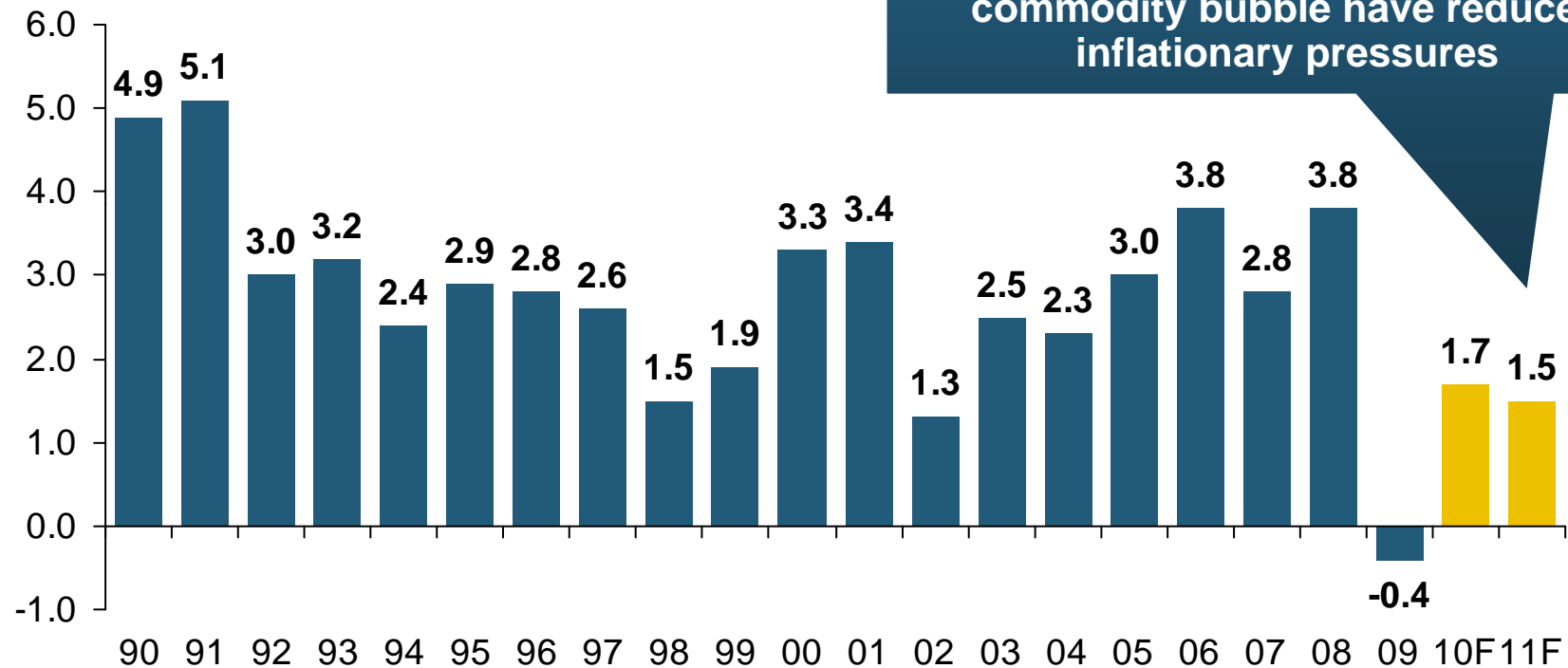


**Inflation Trends:
*Concerns Over Stimulus Spending
and Monetary Policy***

**Mounting Pressure on Claim
Cost Severities?**

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

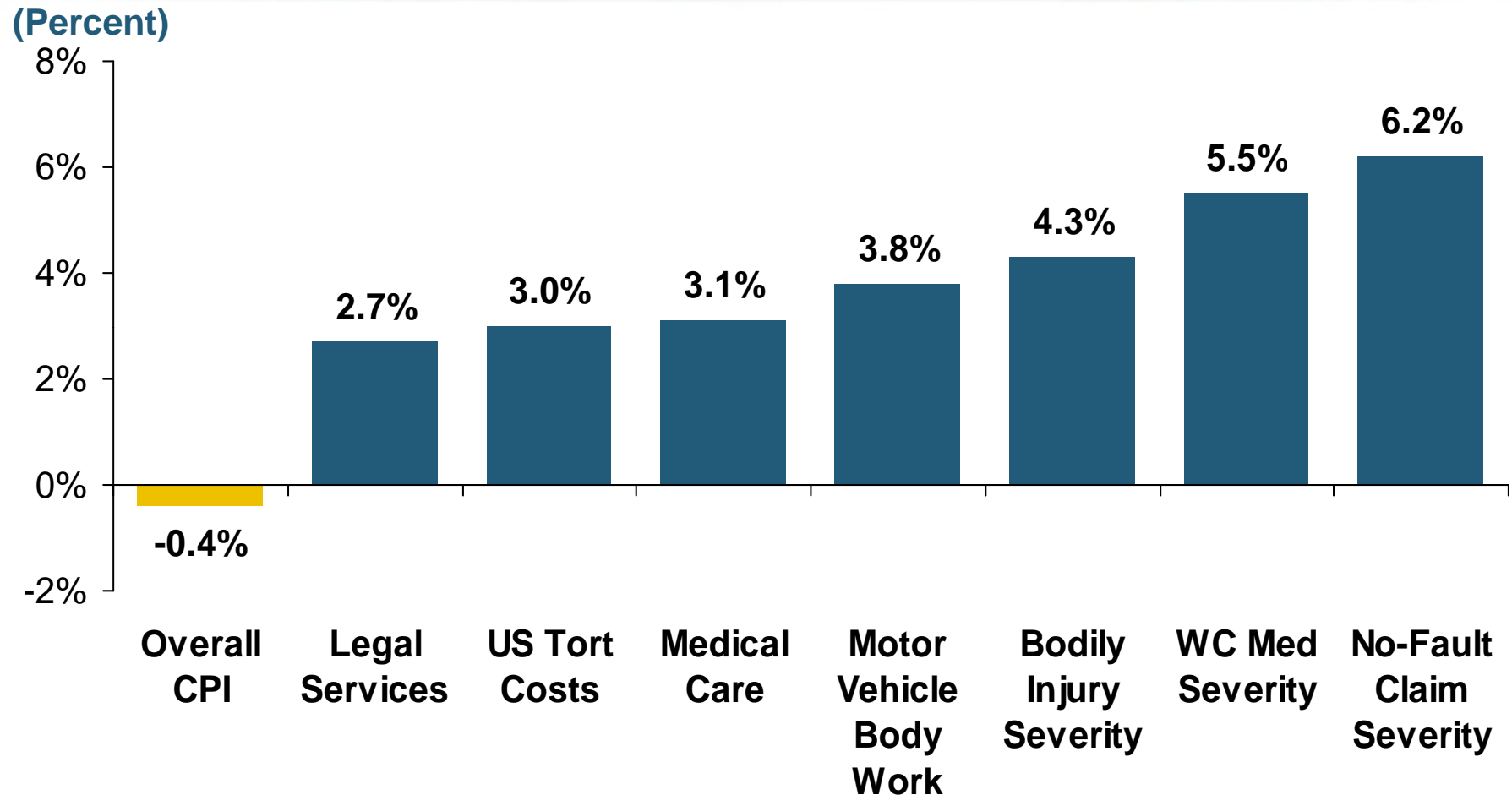
Annual Inflation Rates (%)



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

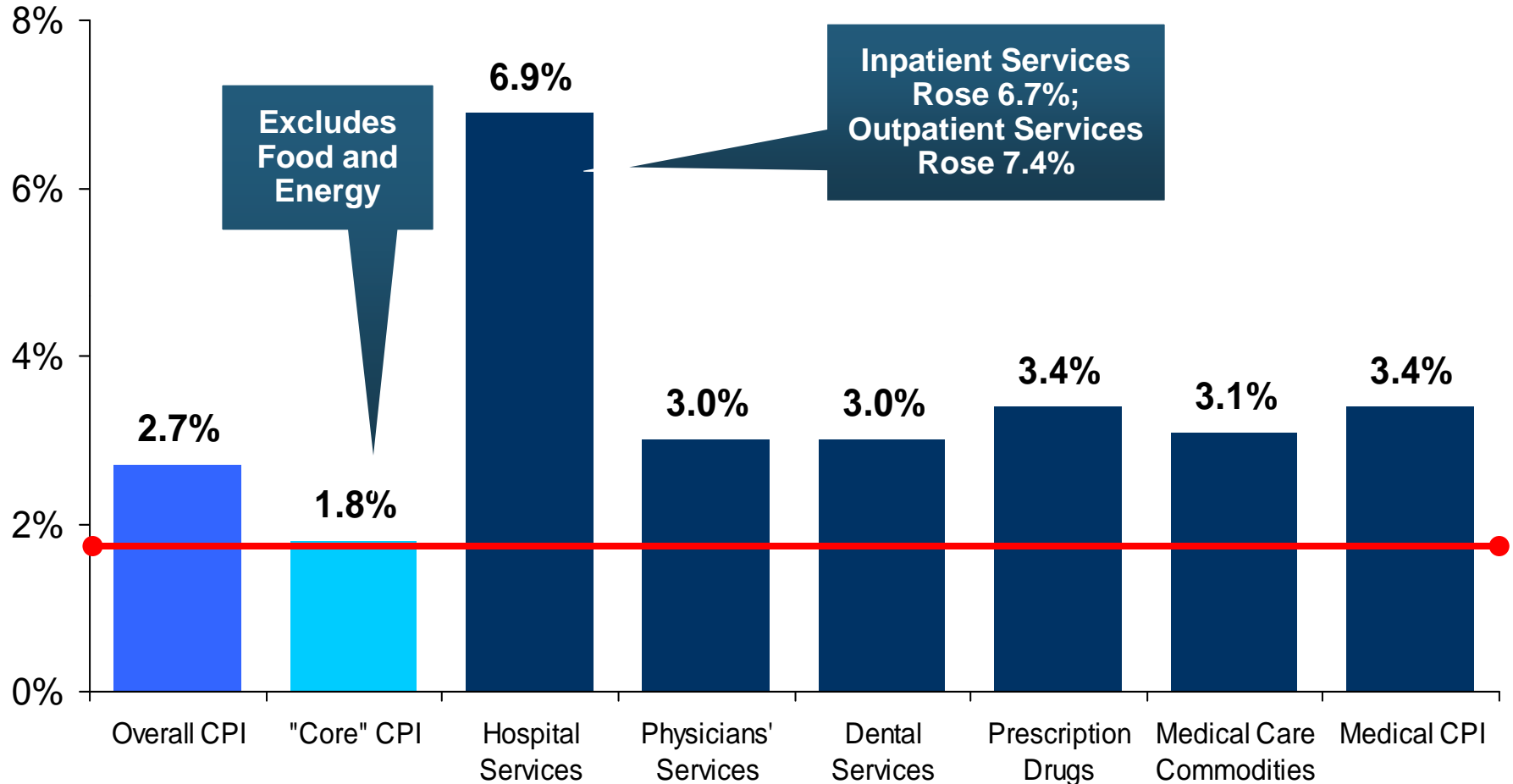


Healthcare and Legal/Tort Costs Are a Major P/C Insurance Cost Driver. These Are Expected to Increase Above the Overall Inflation Rate (CPI) Indefinitely

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.

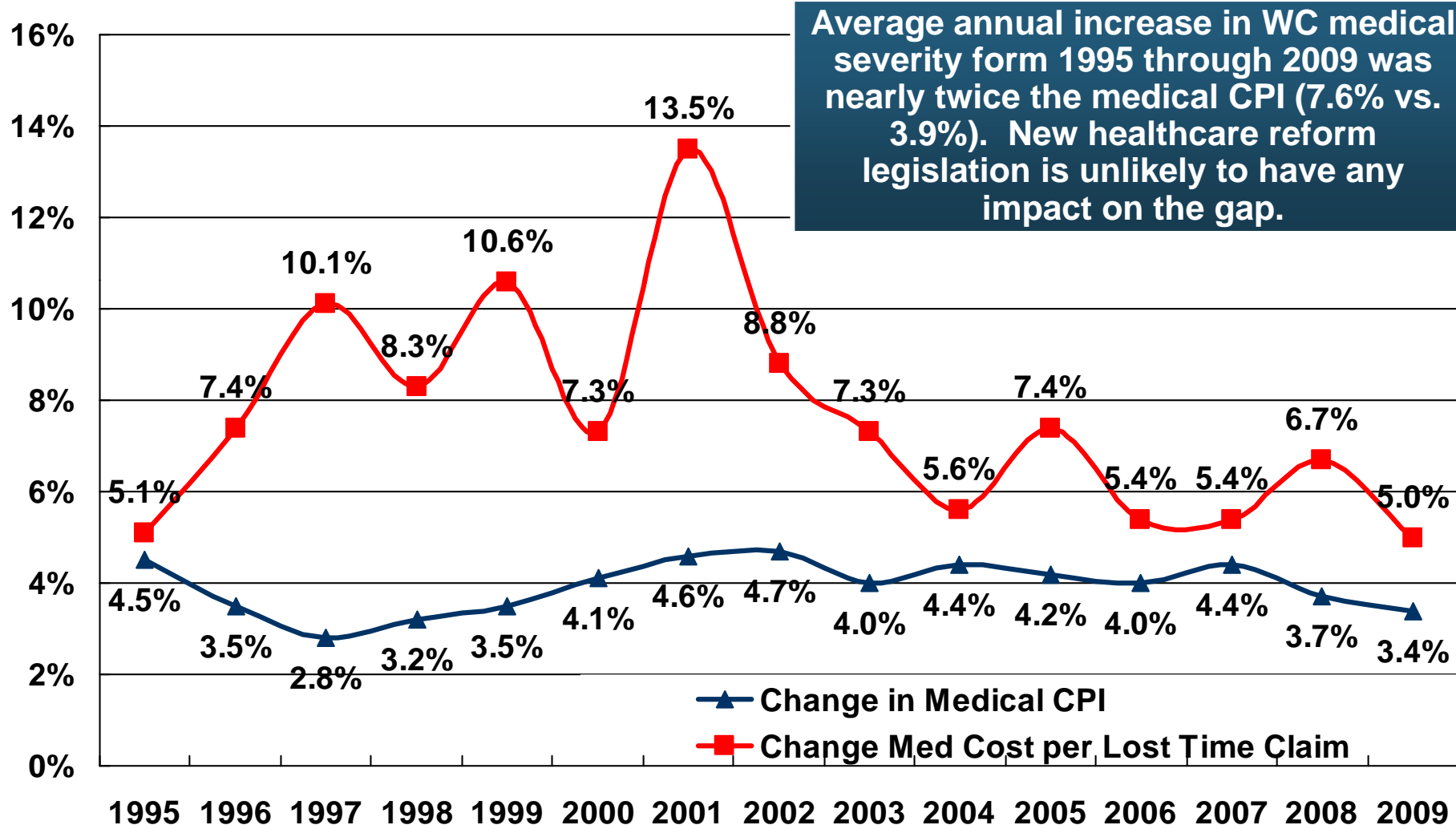
WC Insurers Experience Inflation More Intensely than 2009 CPI Suggests

(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 Risks for WC Insurers if Inflation Is Reignited

■ 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)

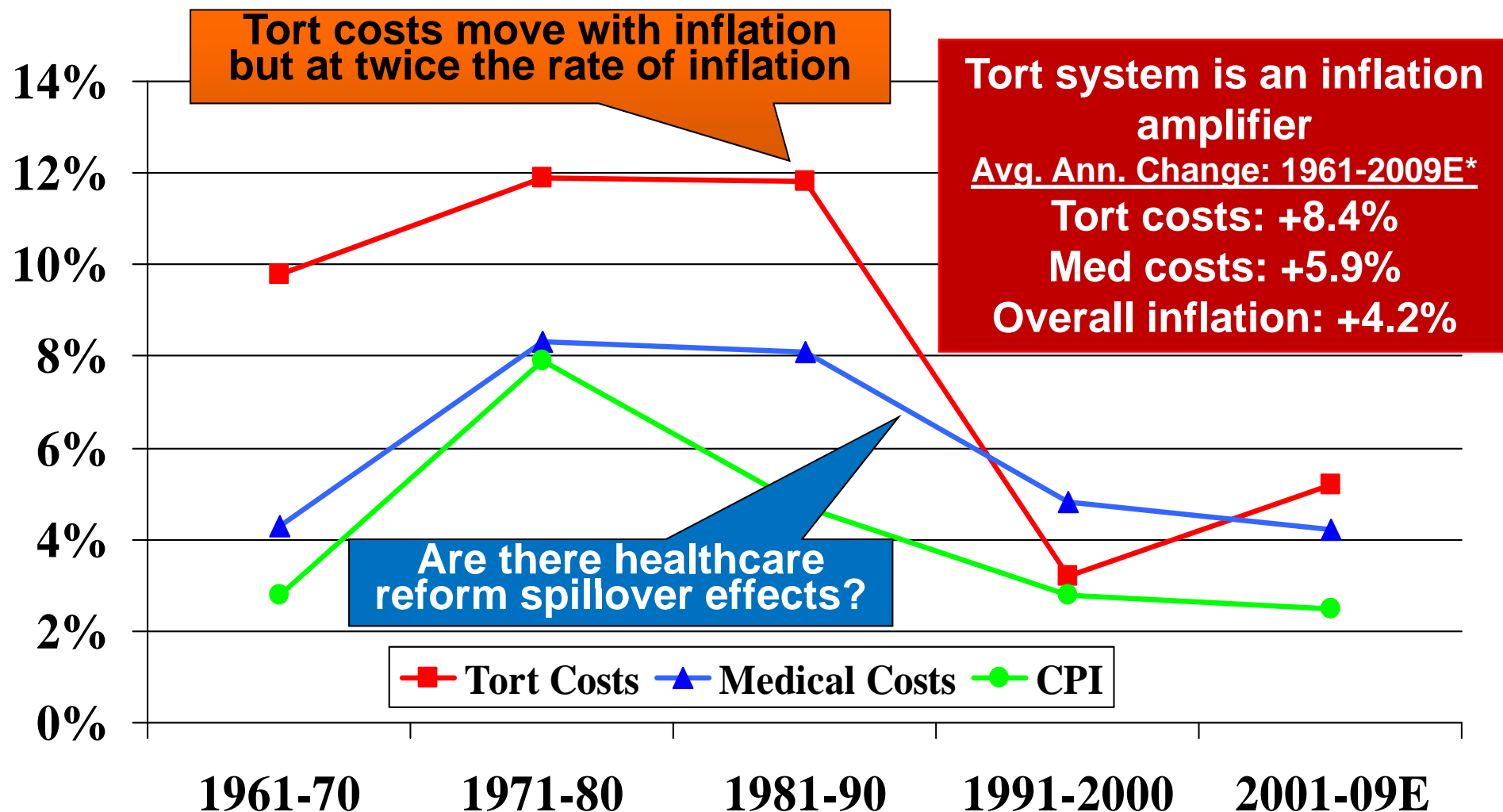
■ Burn Through on Retentions

- ◆ 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.

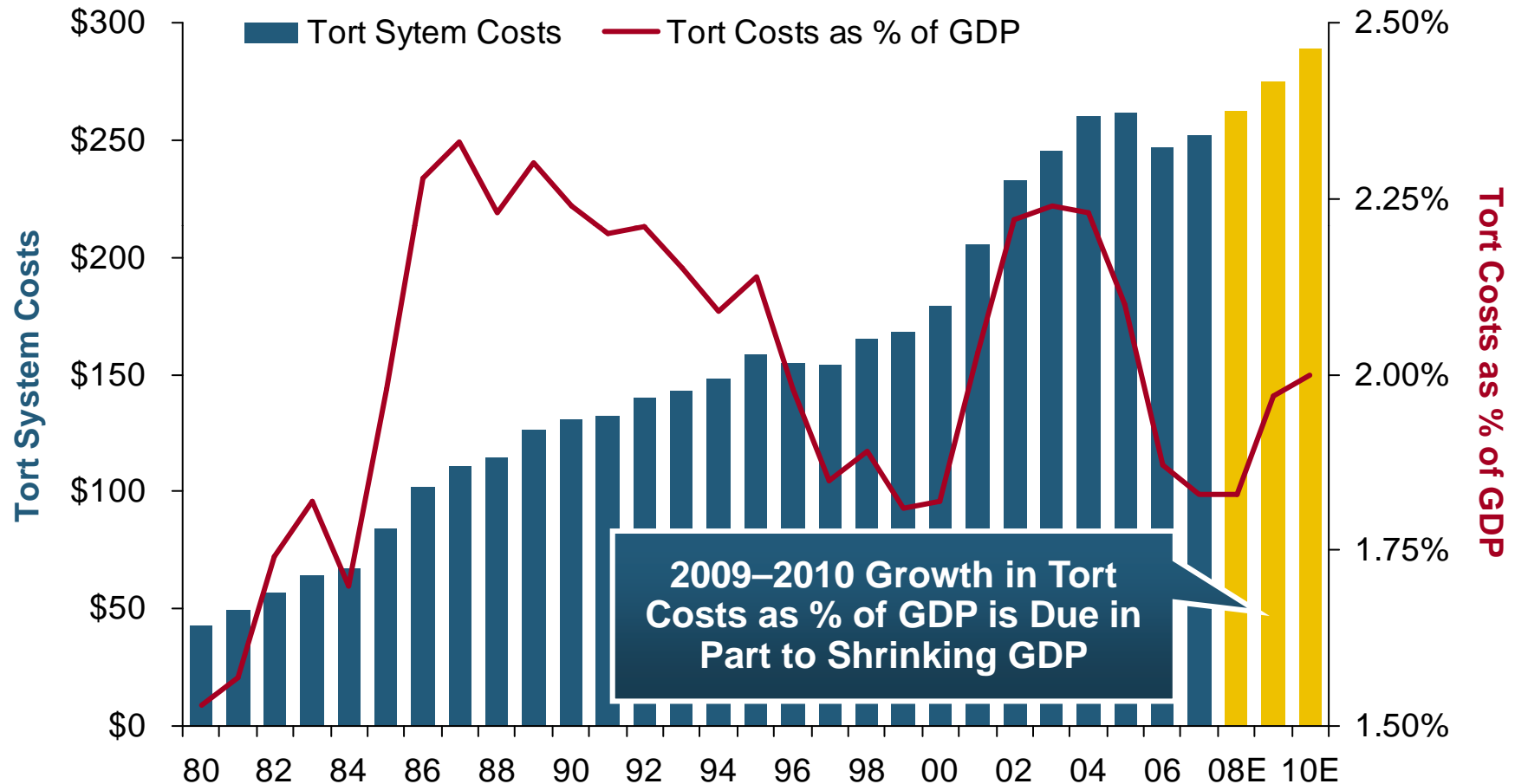
Source: U.S. Bureau of Labor Statistics; Tillinghast-Towers Perrin, *2008 Update on U.S. Tort Costs*; I.I.I.

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)



* 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

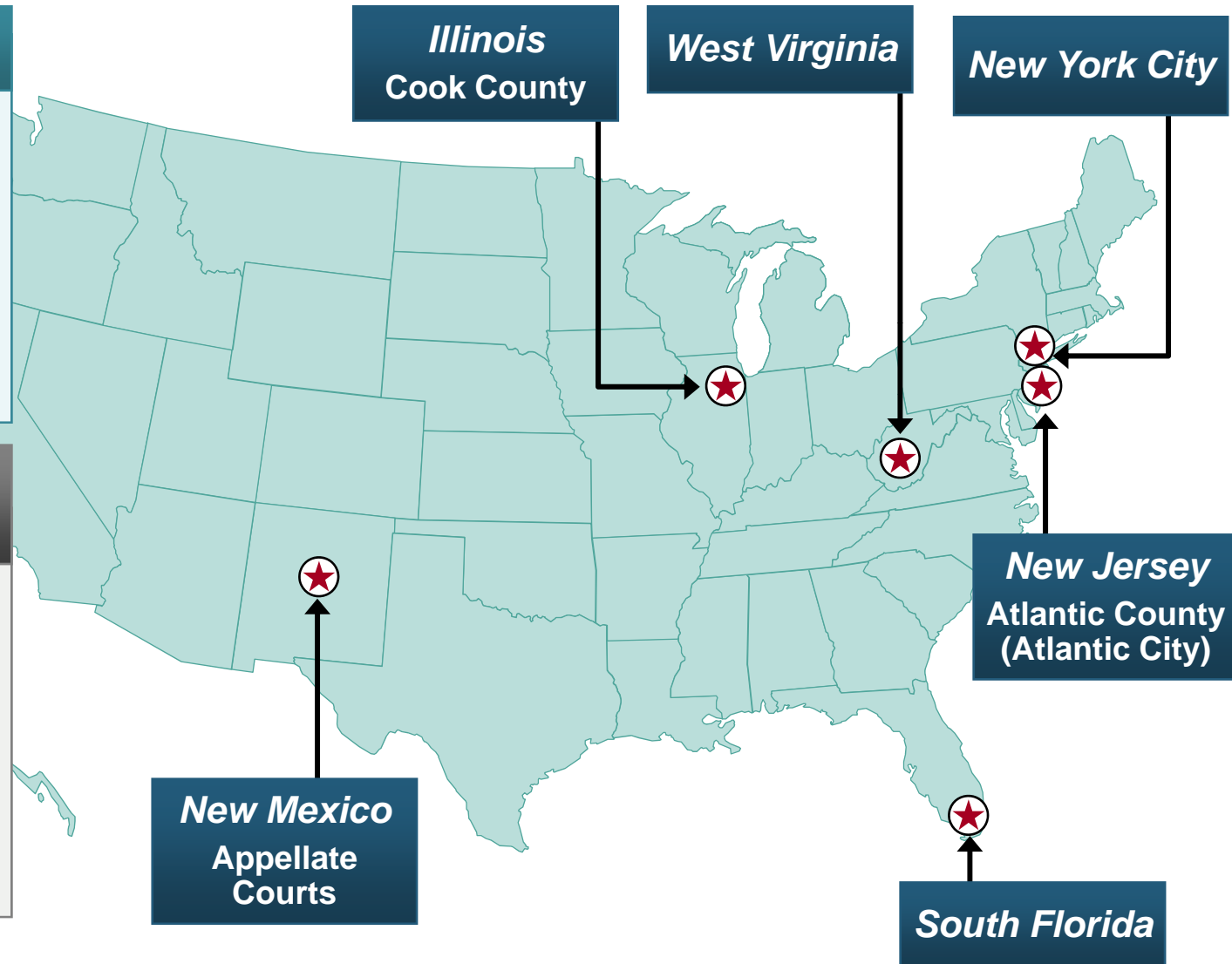
The Nation's Judicial Hellholes: 2010

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

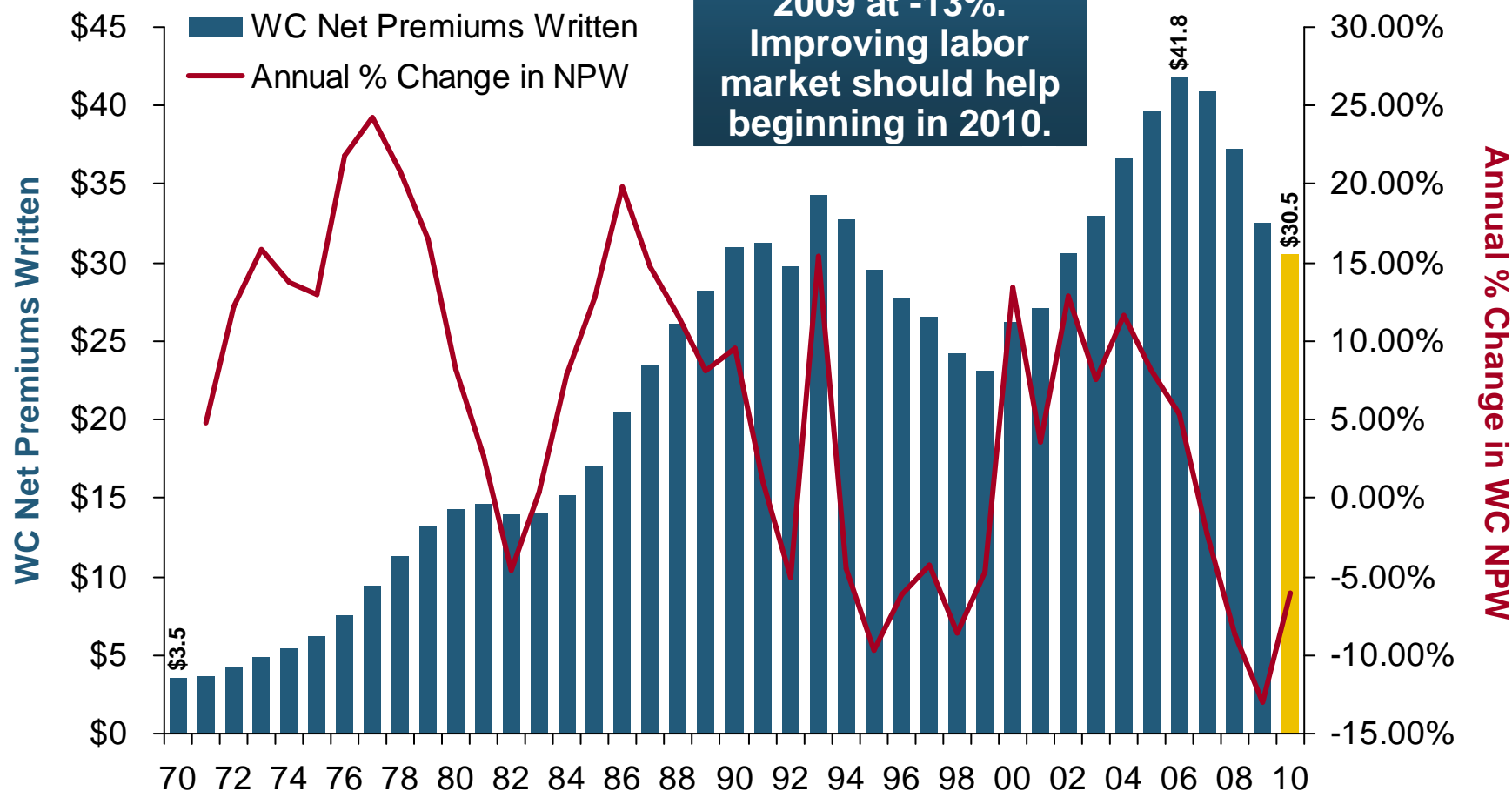


Workers Compensation Operating Environment

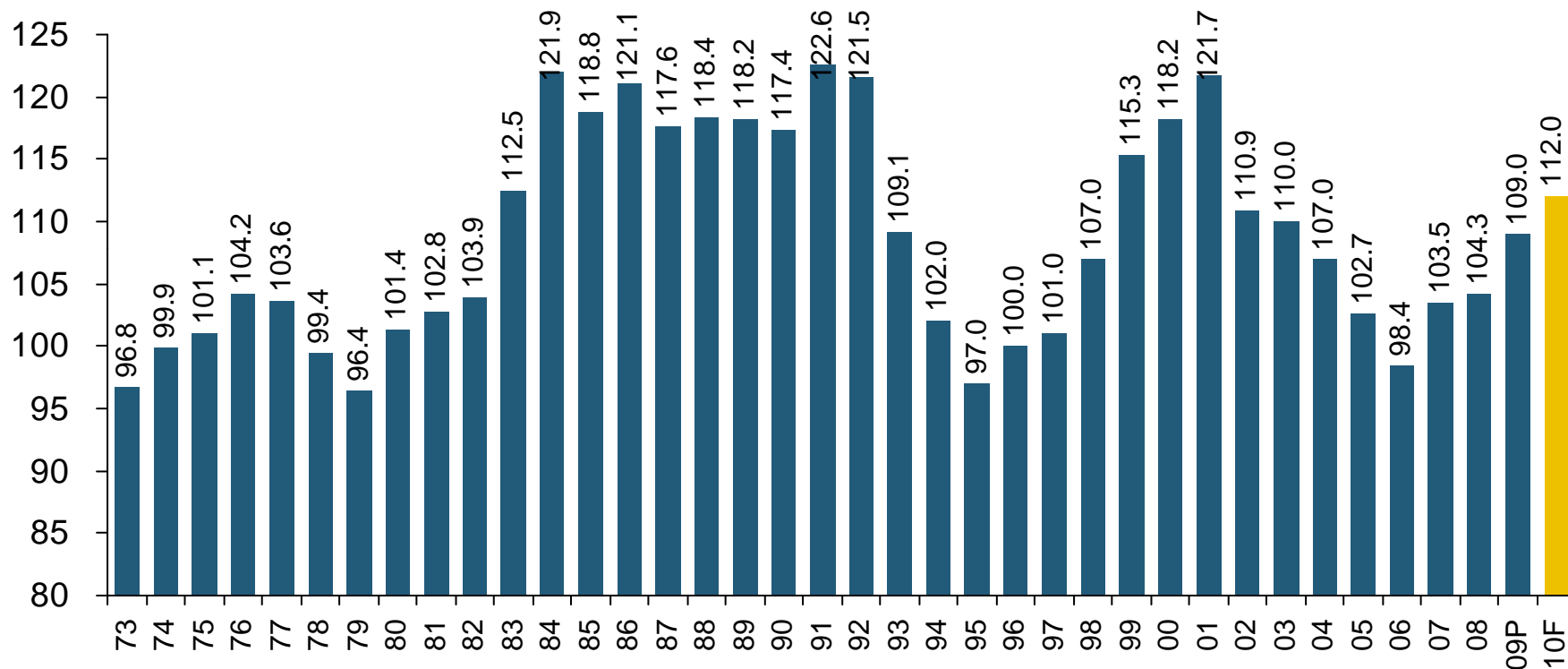
**The Weak Economy and Soft Market Have
Made the Workers Comp Operating
Increasingly Challenging**

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

(\$ Billions)



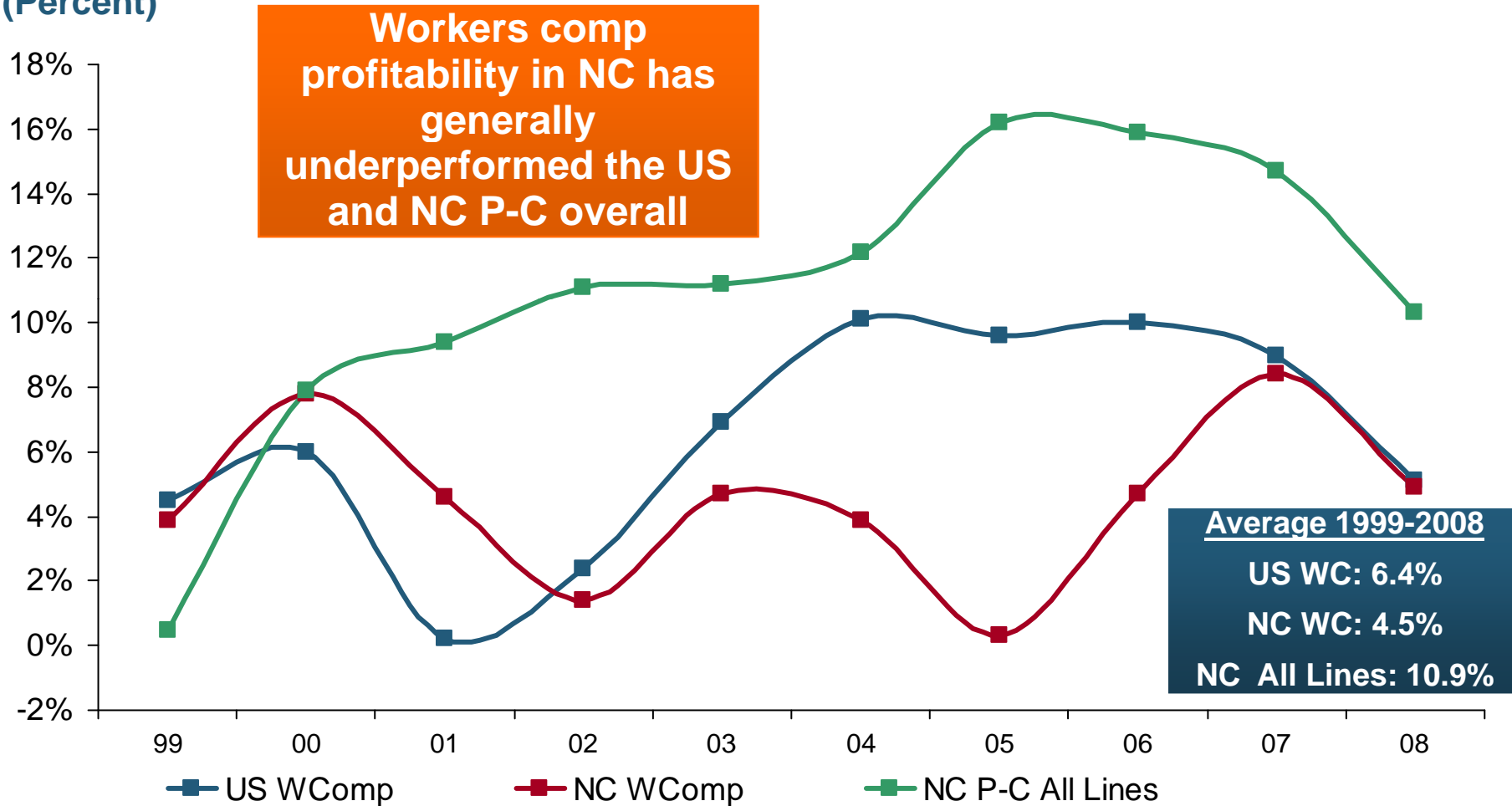
Workers Compensation Combined Ratio: 1973–2010F



Workers Comp Underwriting Results Are Deteriorating Markedly

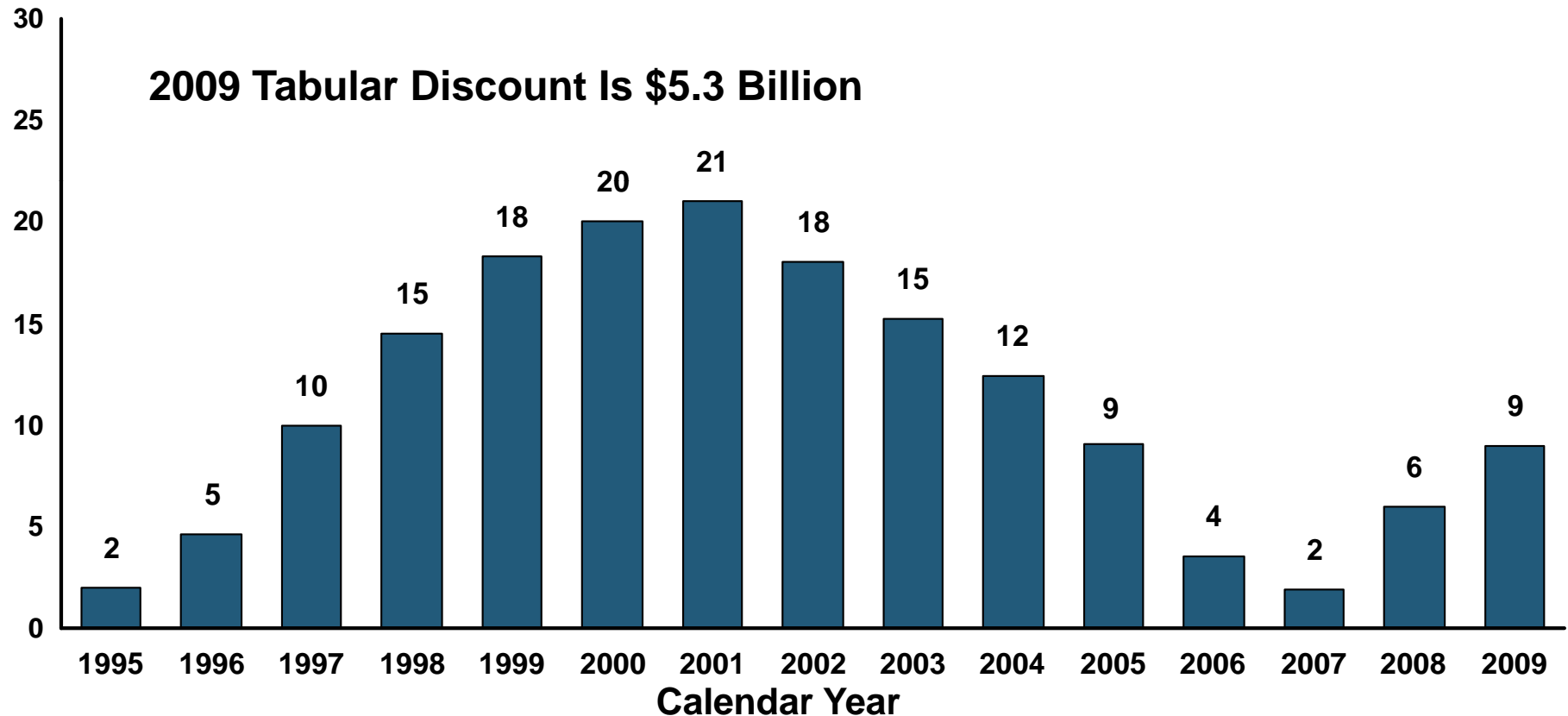
Return on Net Worth for Workers Comp: NC vs. US and NC All P-C Lines, 1999-2008

(Percent)



Calendar Year Reserve Deficiency Increased in 2009

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

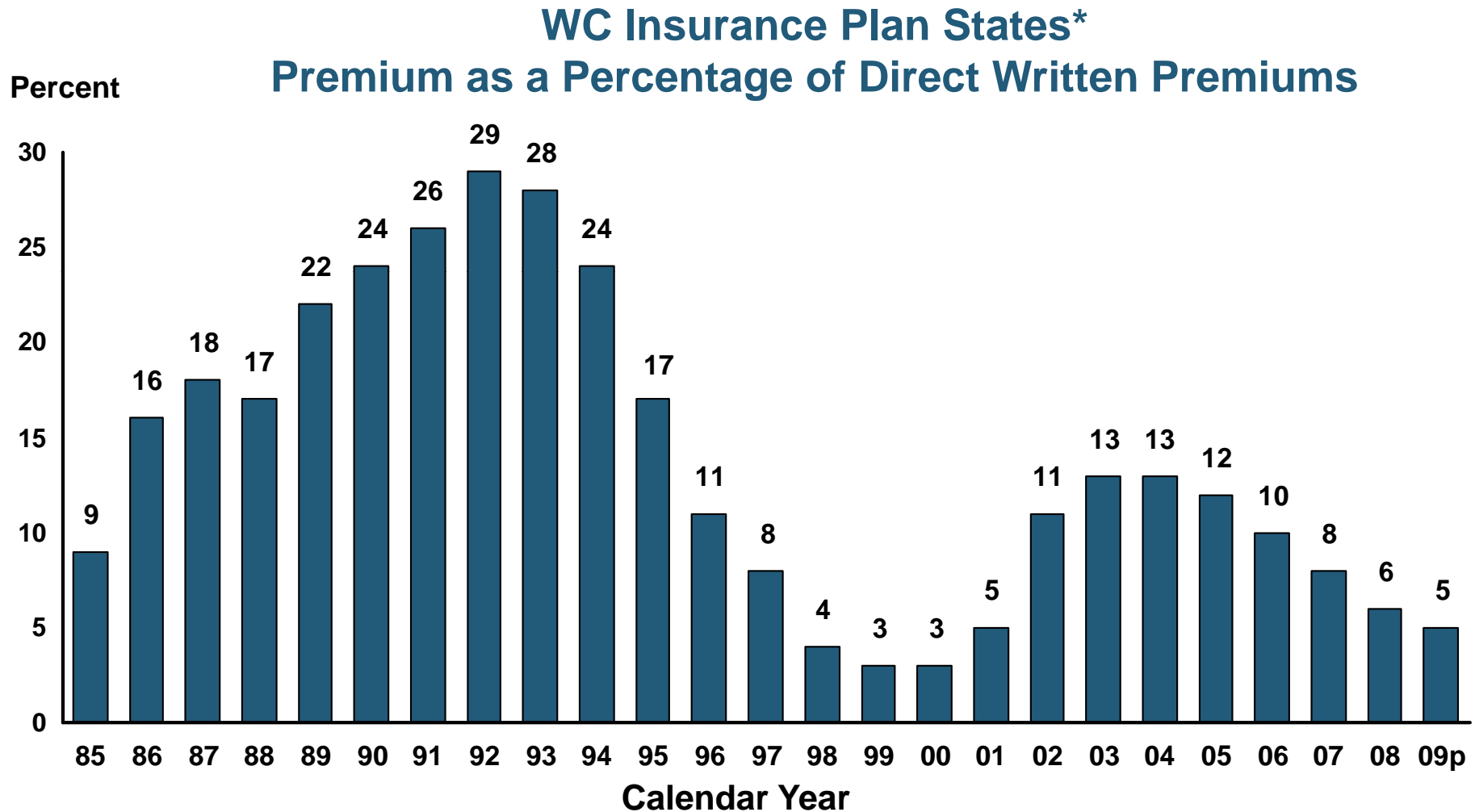


Considers all reserve discounts as deficiencies

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

Source: NCCI analysis

WC Residual Market Shares Continue to Decline



*NCCI Plan states plus DE, IN, MA MI, NJ, NC

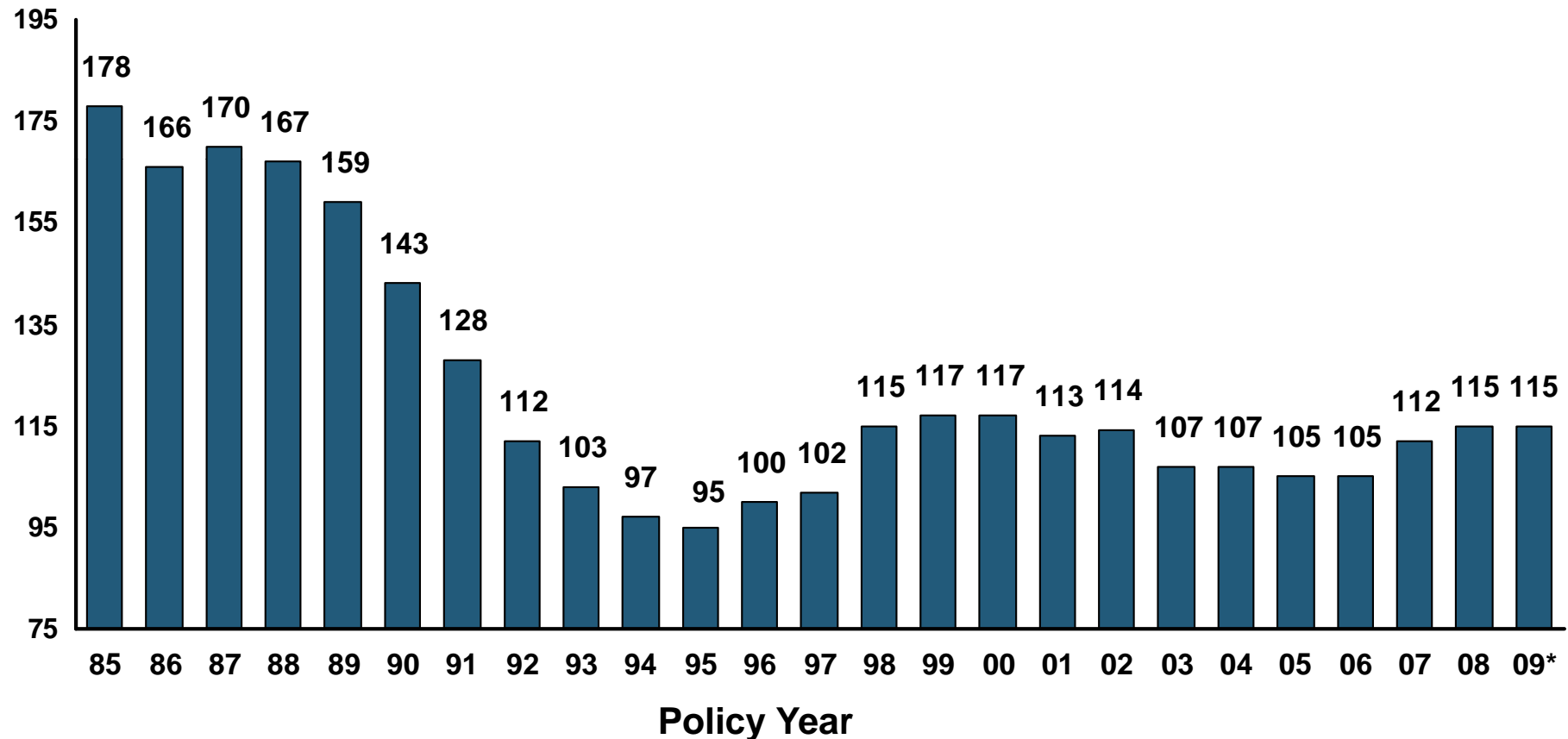
p: Preliminary

Source: NCCI.

WC Residual Market Shares Continue to Decline

NCCI-Serviced WC Residual Market Plans as of December 31, 2009

Percent

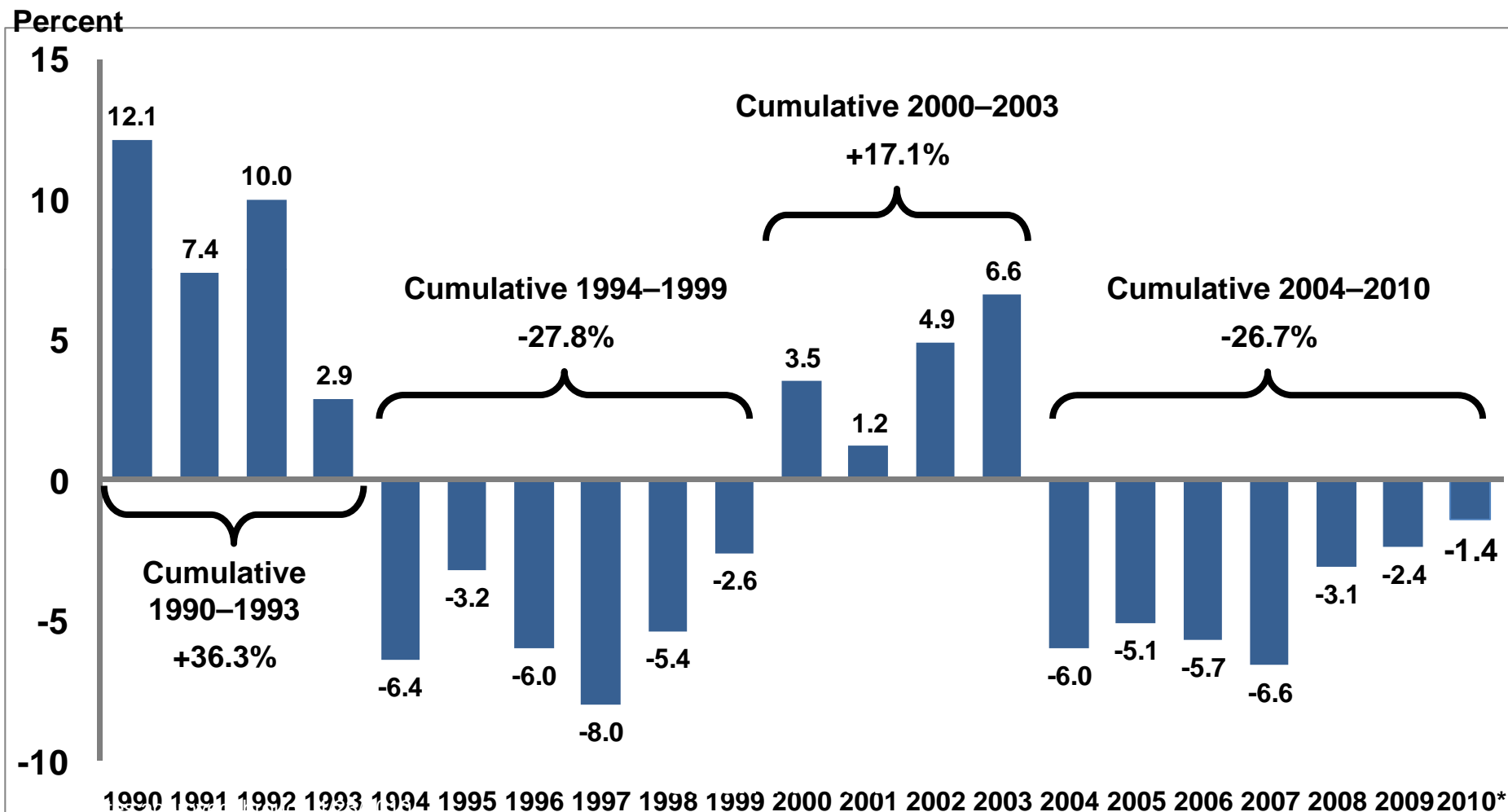


*Incomplete policy year projected to ultimate.

Source: NCCI.

Average Approved Bureau Rates/Loss Costs

History of Average WC Bureau Rate/Loss Cost Level Changes



*States approved through 4/23/10.

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

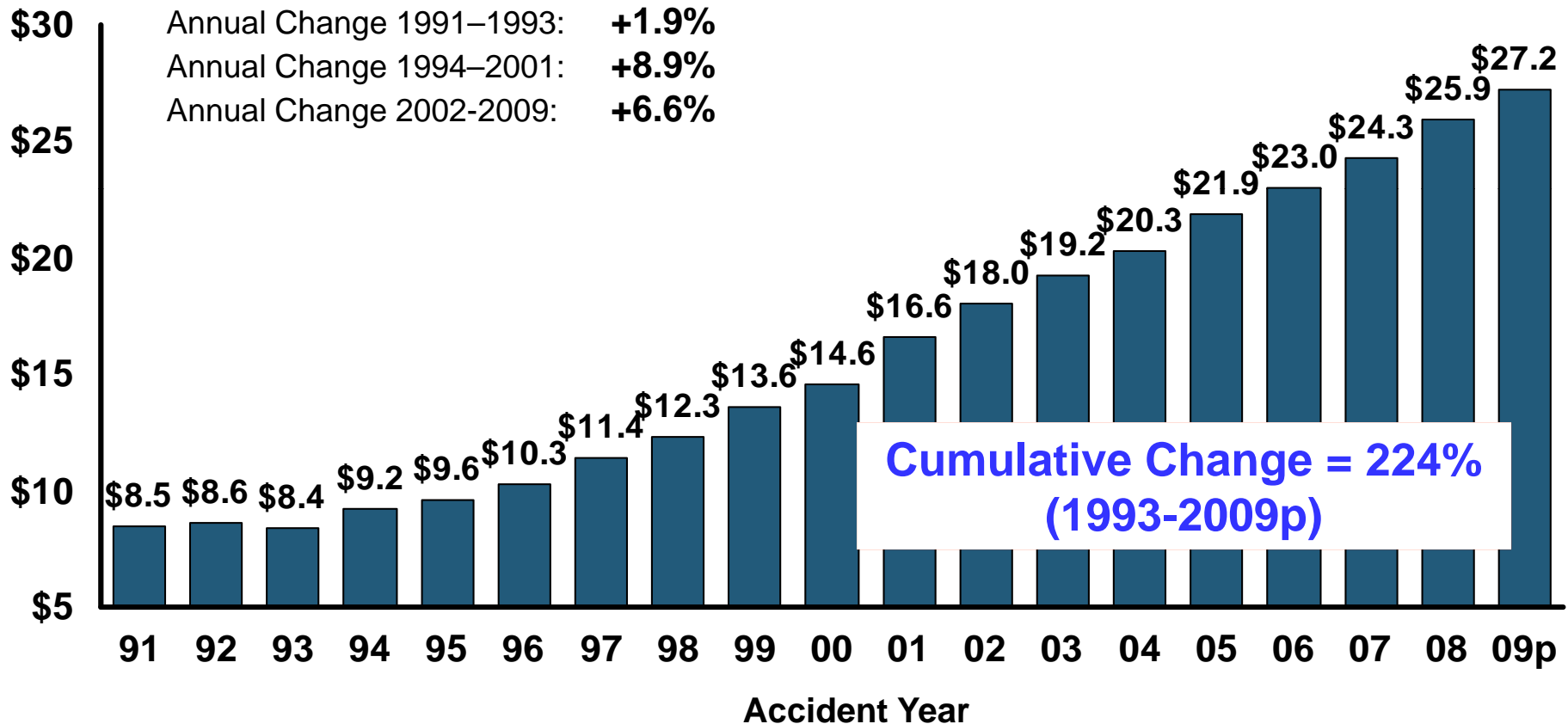
Source: NCCI.

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)

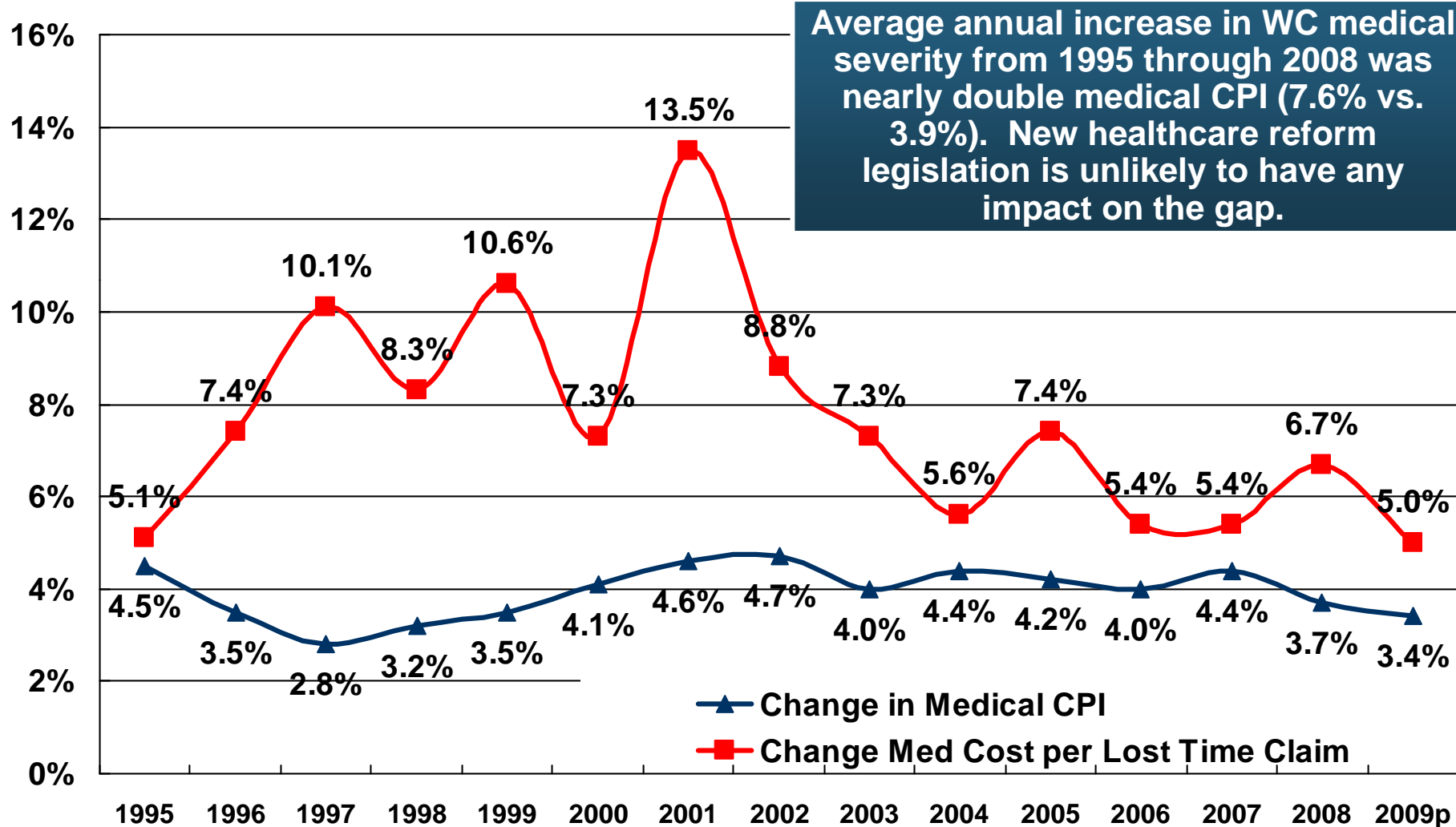


2009p: Preliminary based on data valued as of 12/31/2009

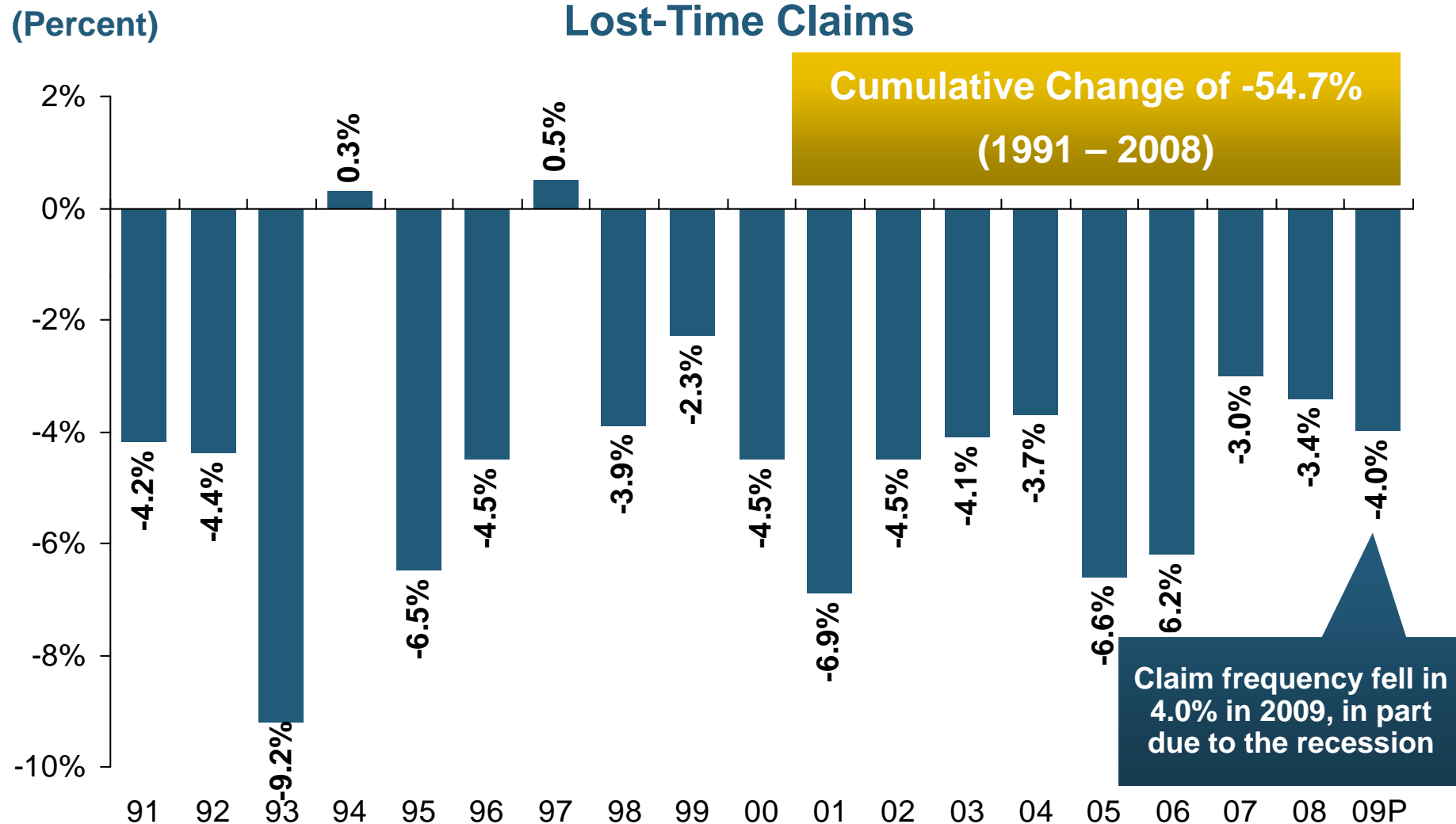
1991-2008: Based on data through 12/31/2008, developed to ultimate

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*



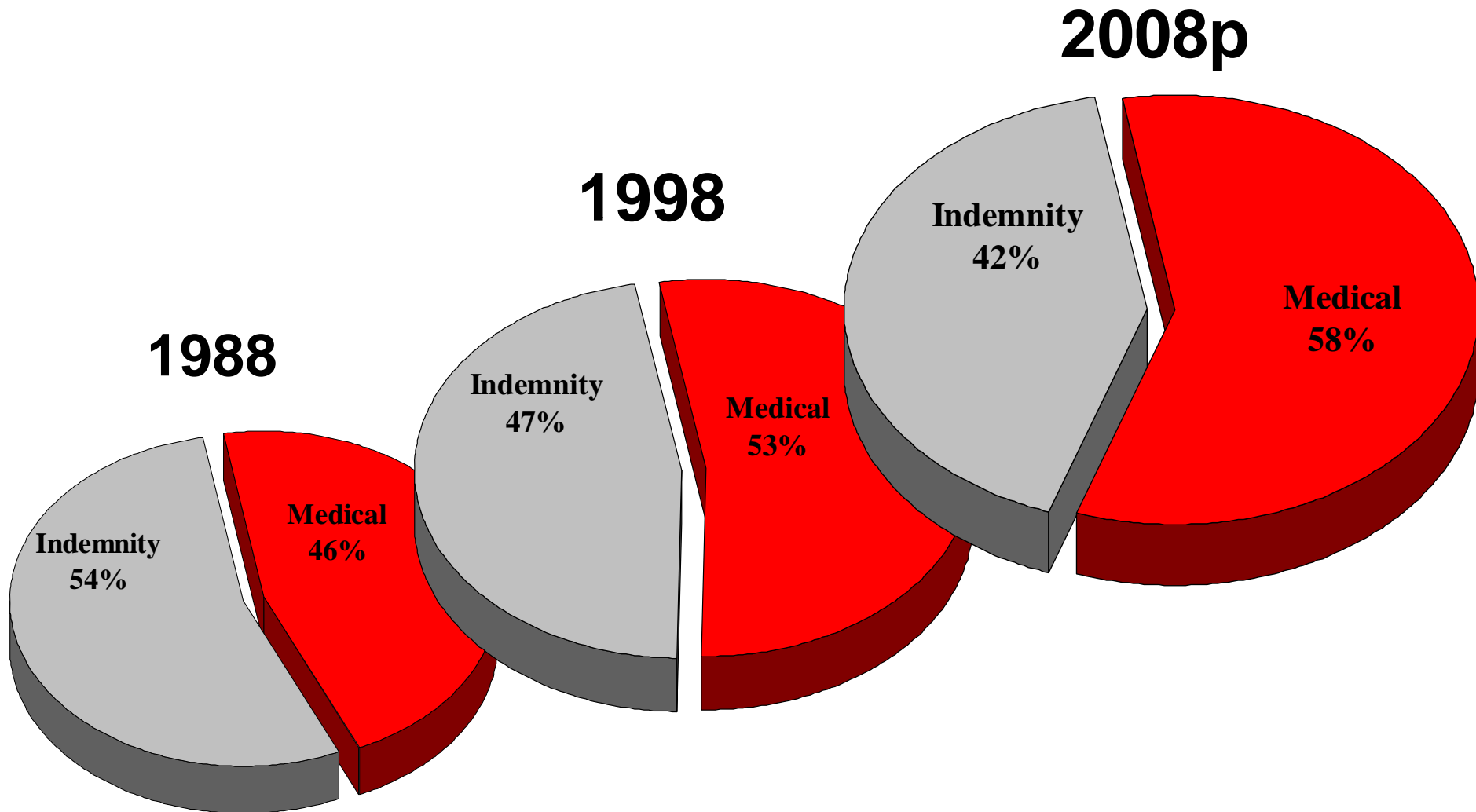
2009p: Preliminary based on data valued as of 12/31/2009;

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

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

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

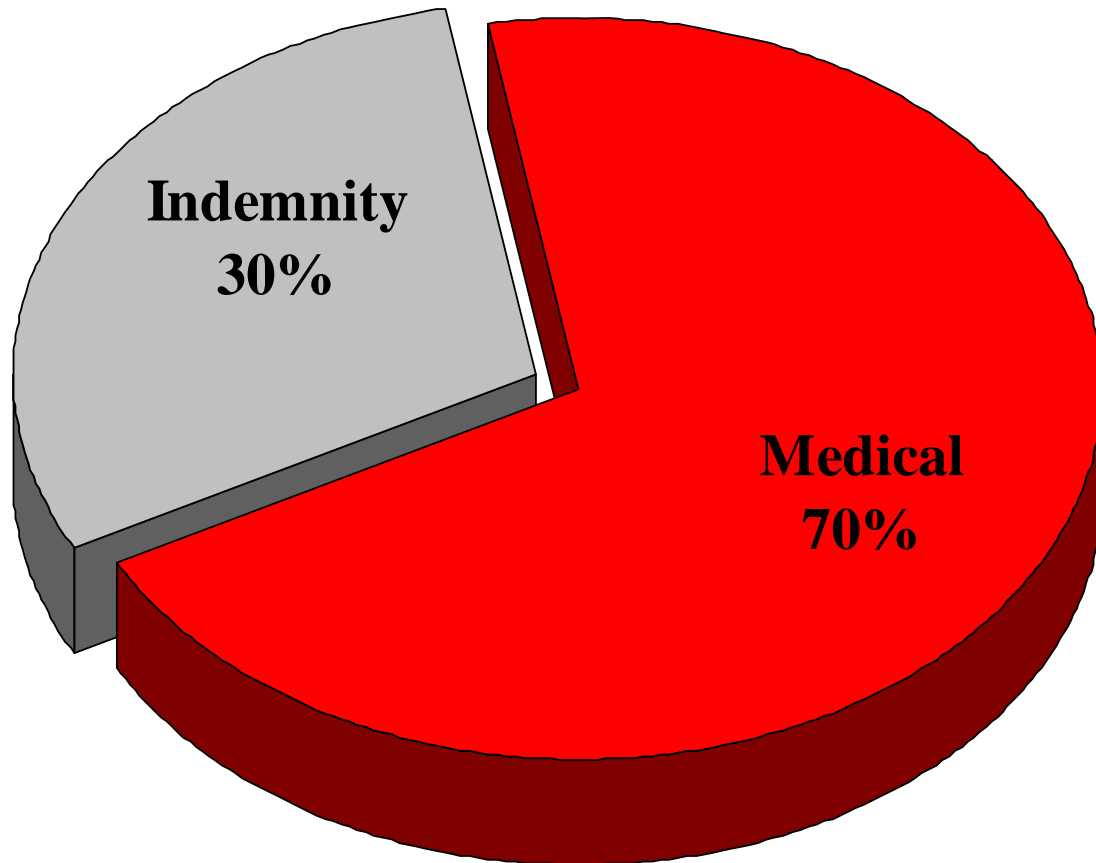
Med Costs Share of Total Costs is Increasing Steadily



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



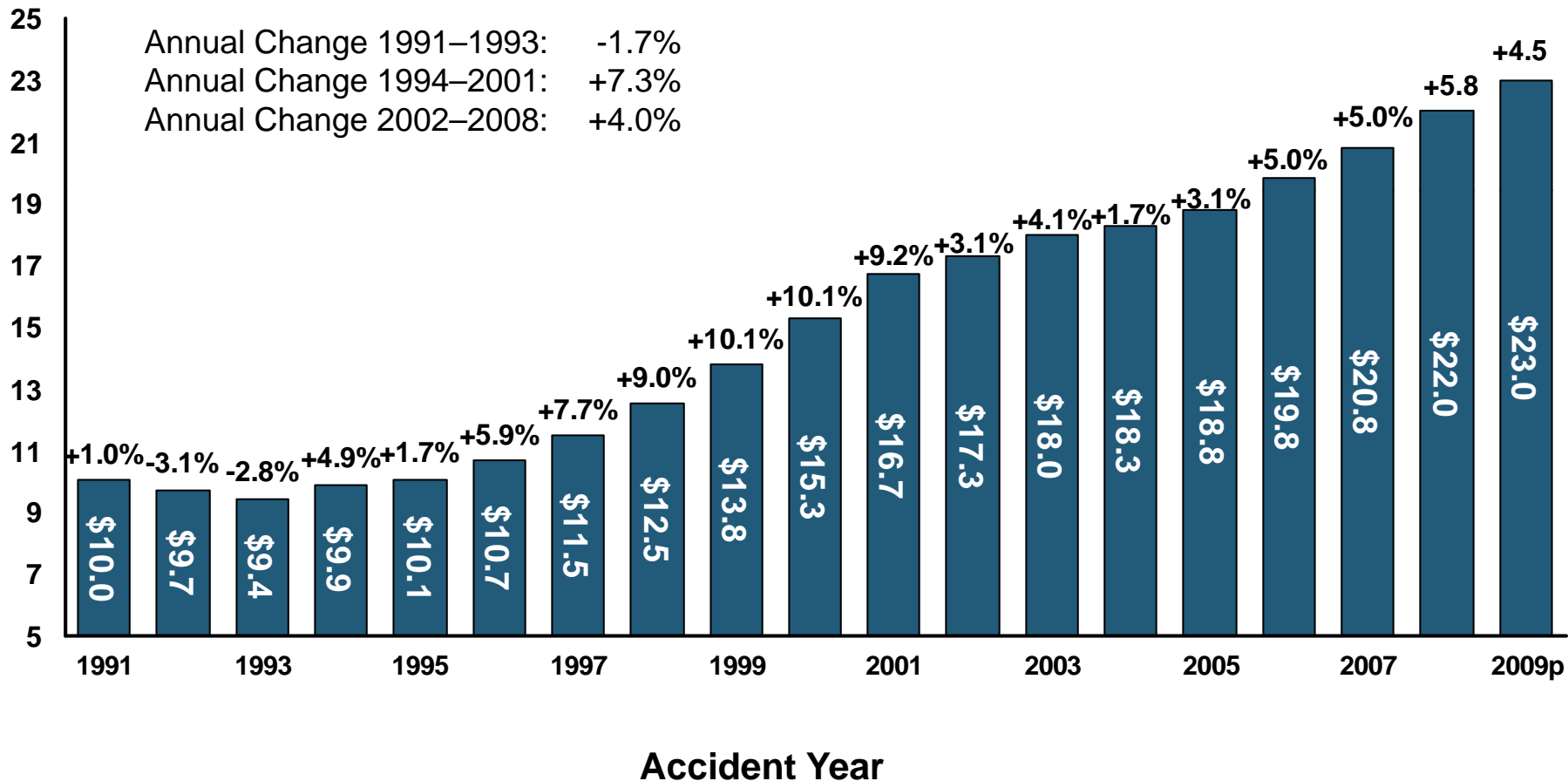
This trend will likely be supported by the increased labor force participation of workers age 55 and older.

Indemnity Claim Cost Trends

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

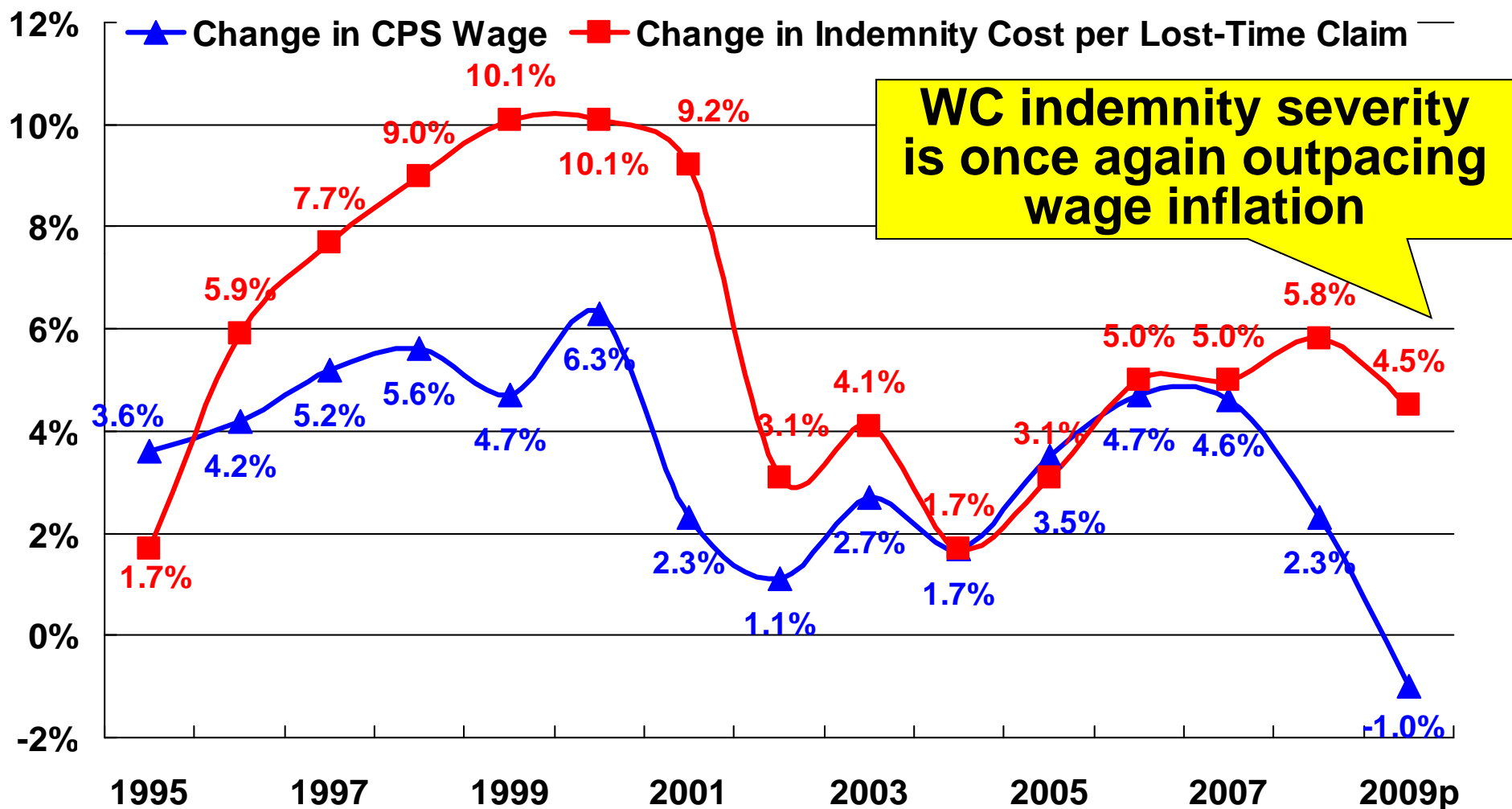
Workers Comp Indemnity Claim Costs Continue to Grow

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



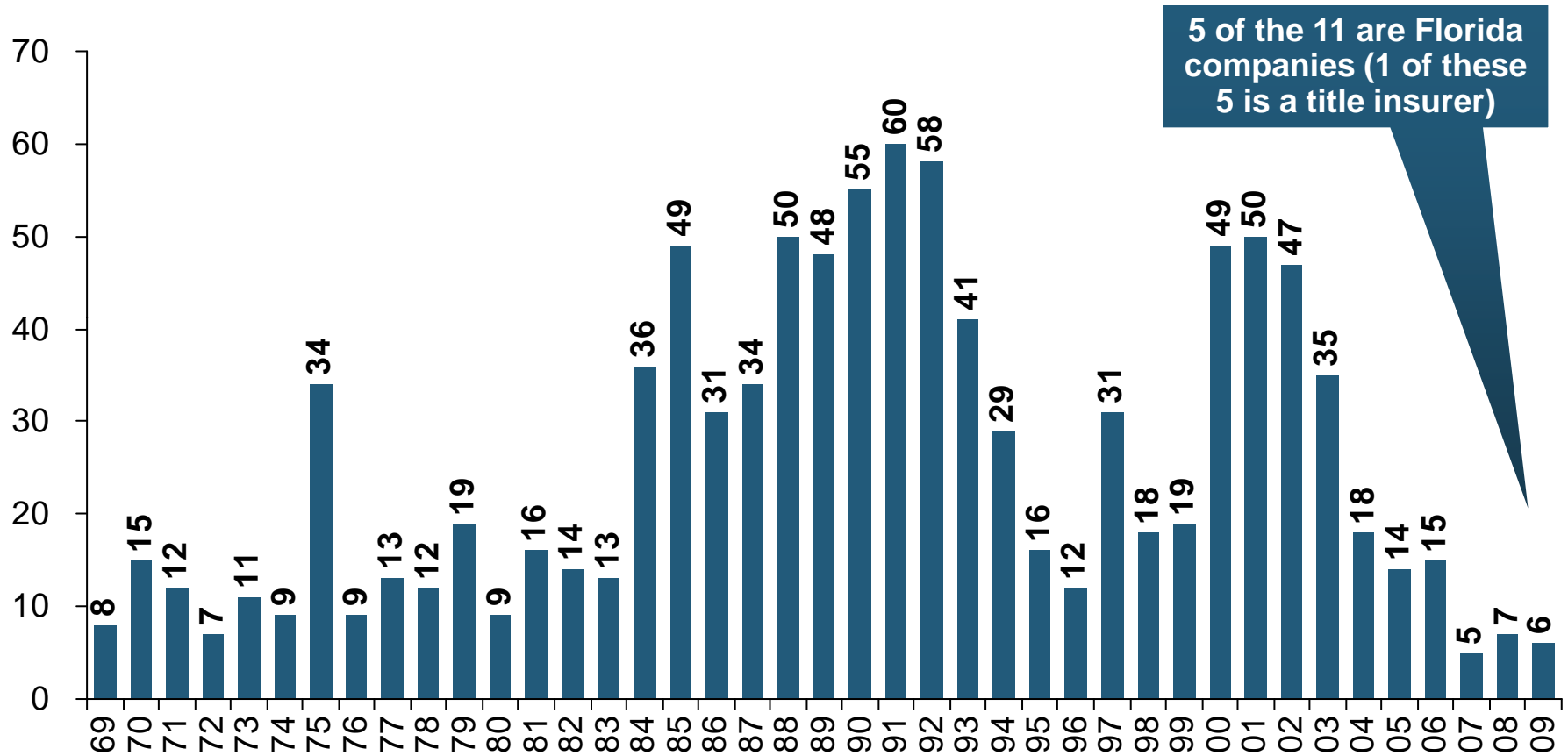
2009p: Preliminary based on data valued as of 12/31/2009; 1991-2008: Based on data through 12/31/2008, developed to ultimate. Based on the states where NCCI provides ratemaking services. Excludes the effects of deductible policies. CPS = Current Population Survey.
Source: NCCI



P/C Insurance Industry Financial Strength & Ratings

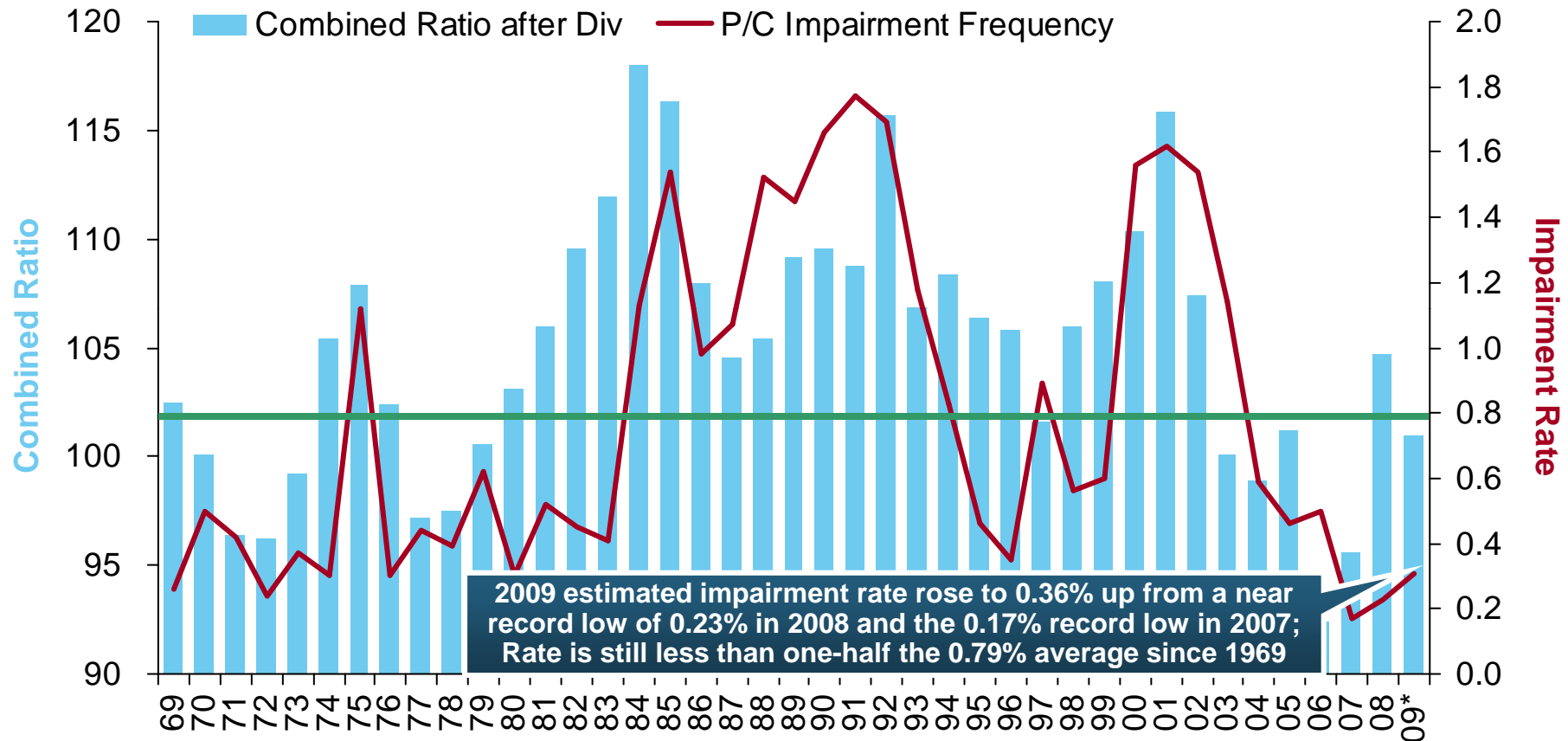
**Industry Has Weathered
the Storms Well**

P/C Insurer Impairments, 1969–2009



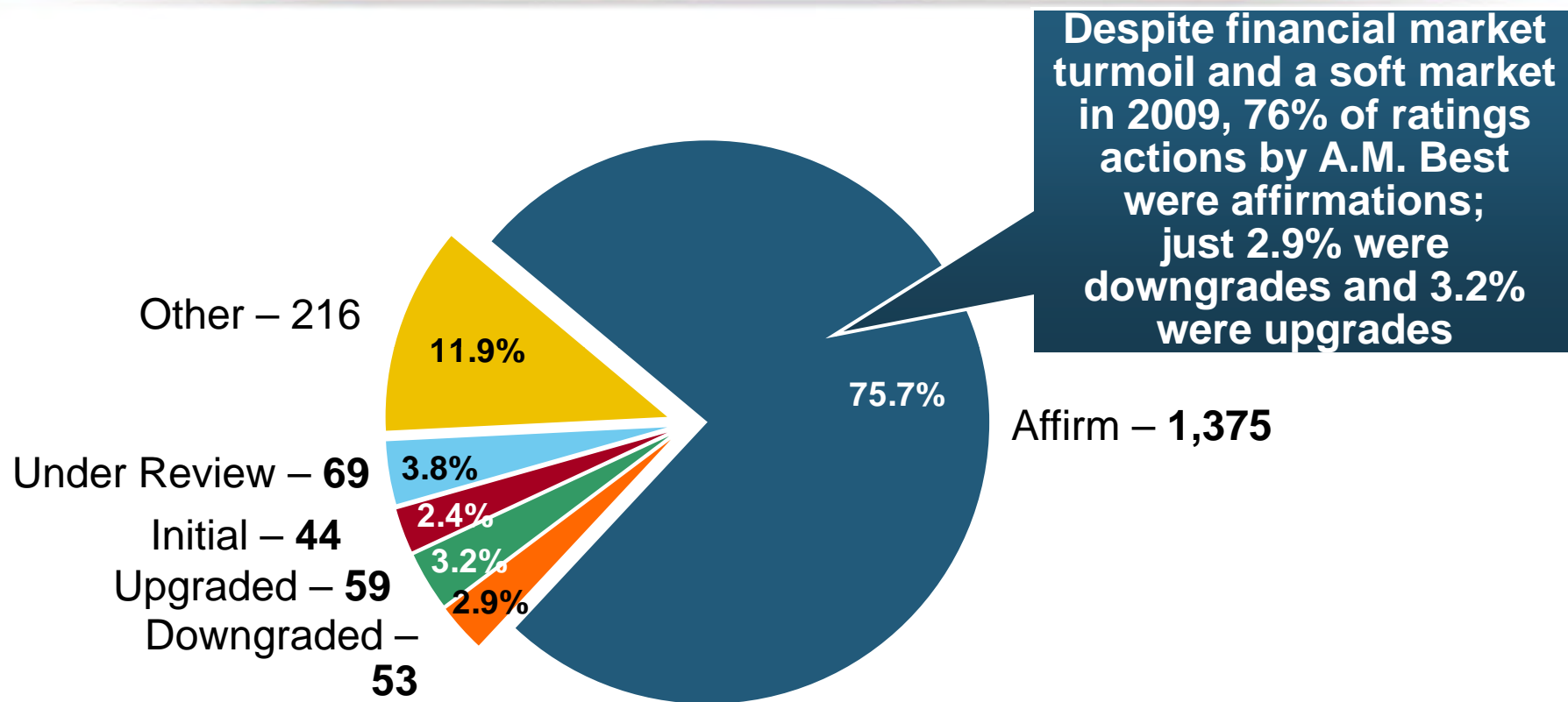
The Number of Impairments Varies Significantly Over the P/C Insurance Cycle, With Peaks Occurring Well into Hard Markets

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

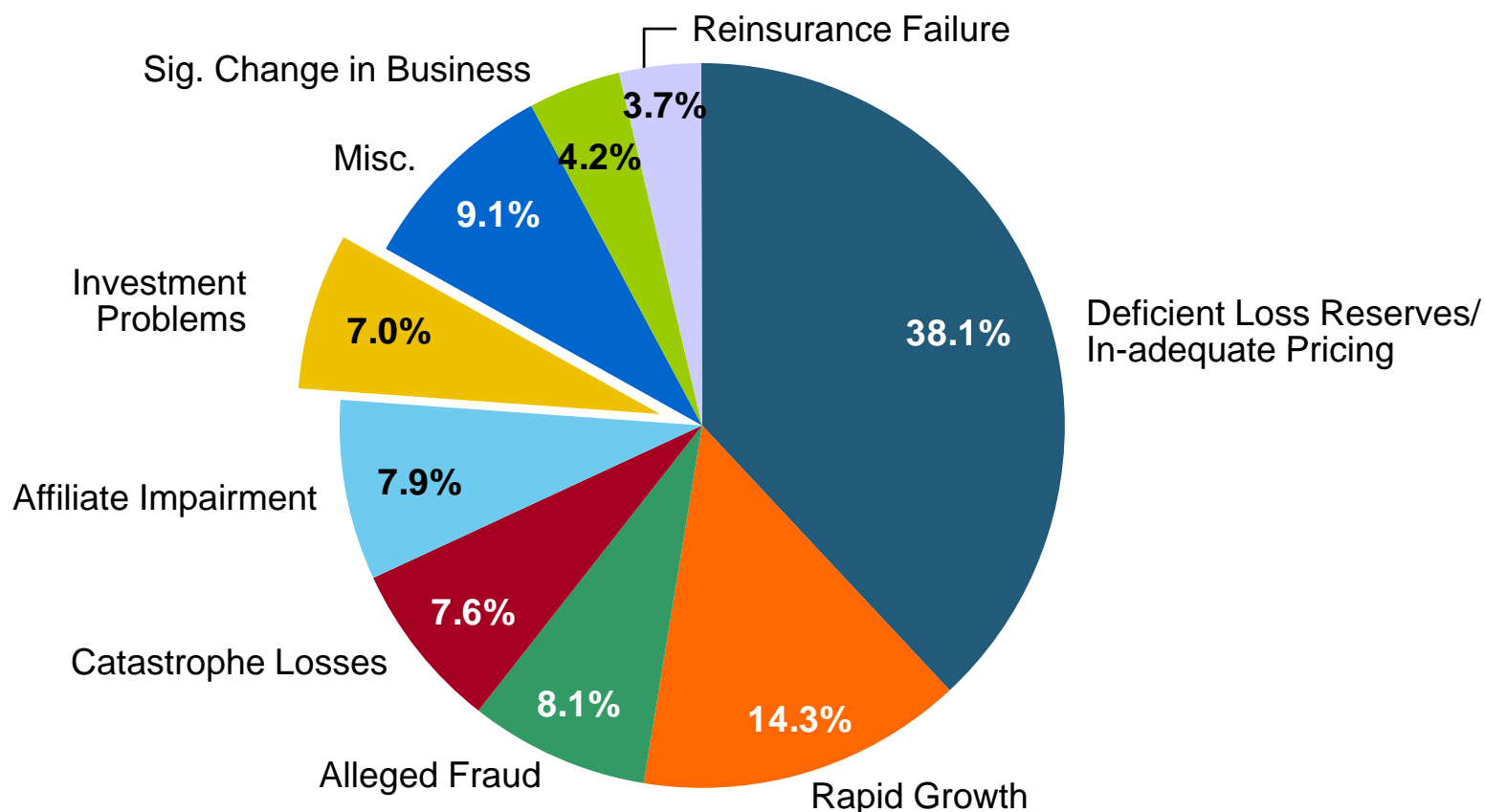
Summary of A.M. Best's P/C Insurer Ratings Actions in 2009



**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



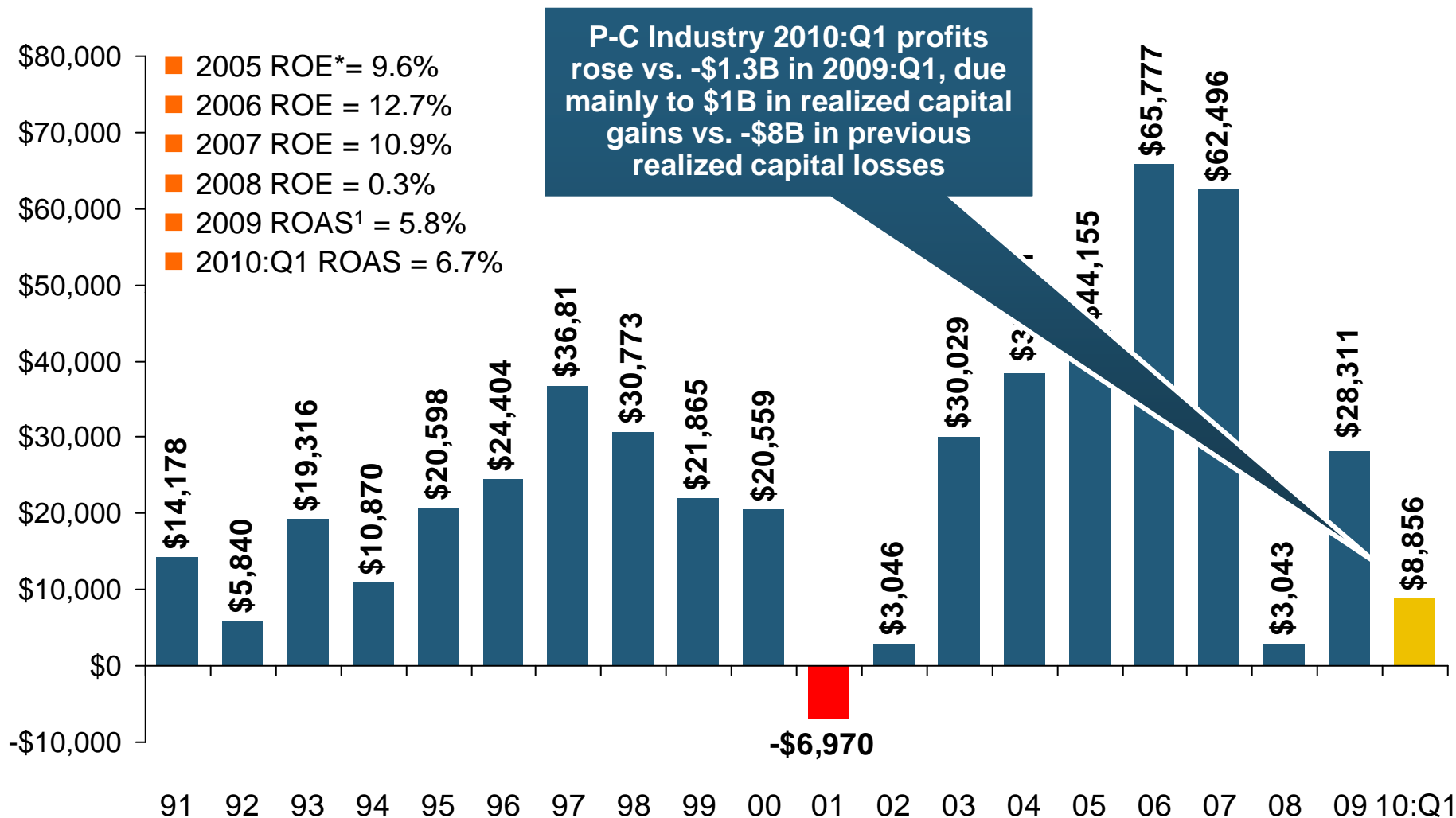
P/C Insurance Financial Performance

A Resilient Industry in Challenging Times

Profitability

Historically Volatile

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

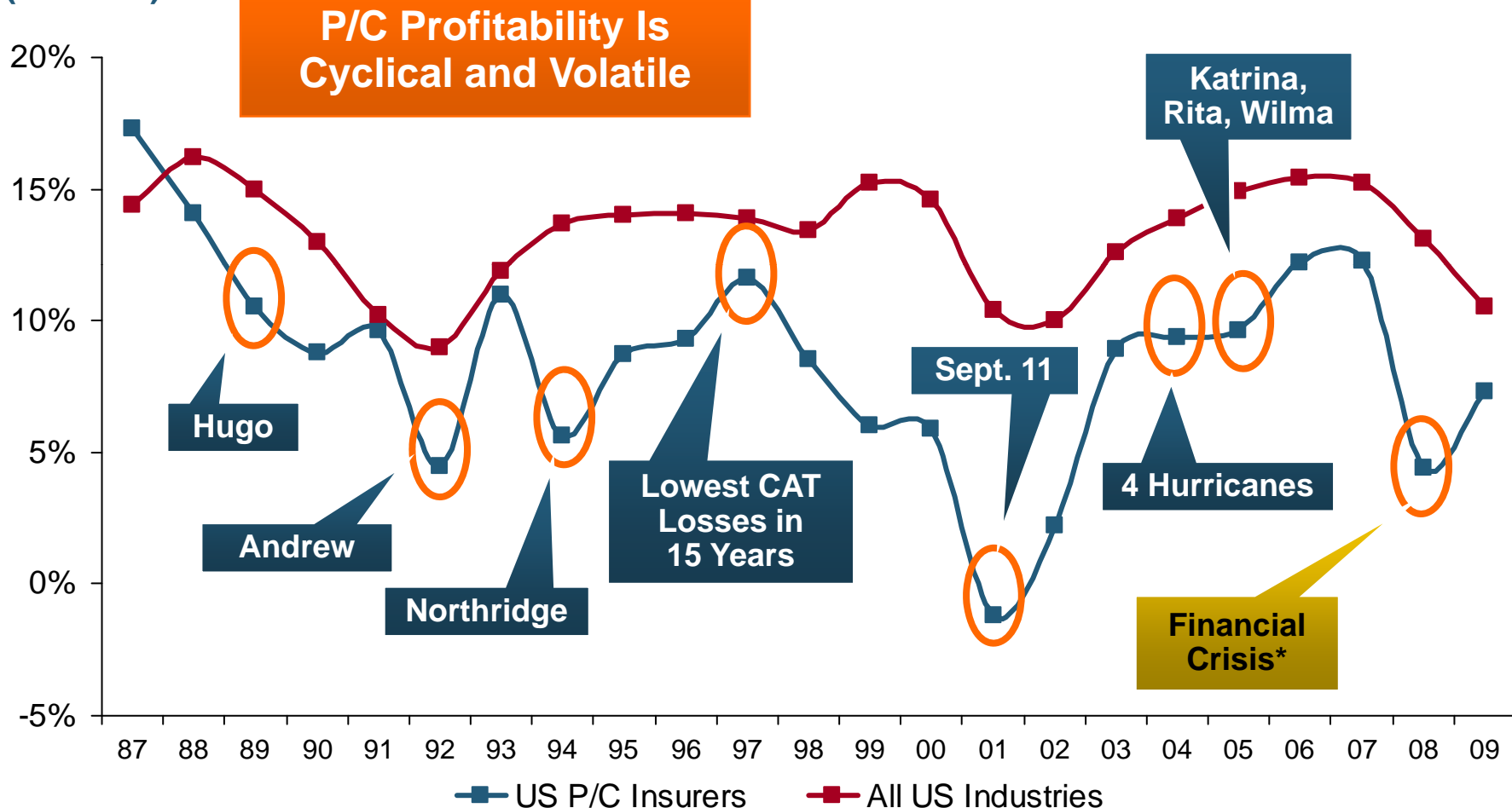


* ROE figures are GAAP; ¹Return on avg. surplus. Excluding Mortgage & Financial Guaranty insurers yields an 8.3% ROAS for 2010:Q1, 7.3% for 2009 and 4.4% for 2008. 2009 net income was \$34.5 billion and \$20.8 billion in 2008 excluding M&FG.

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

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

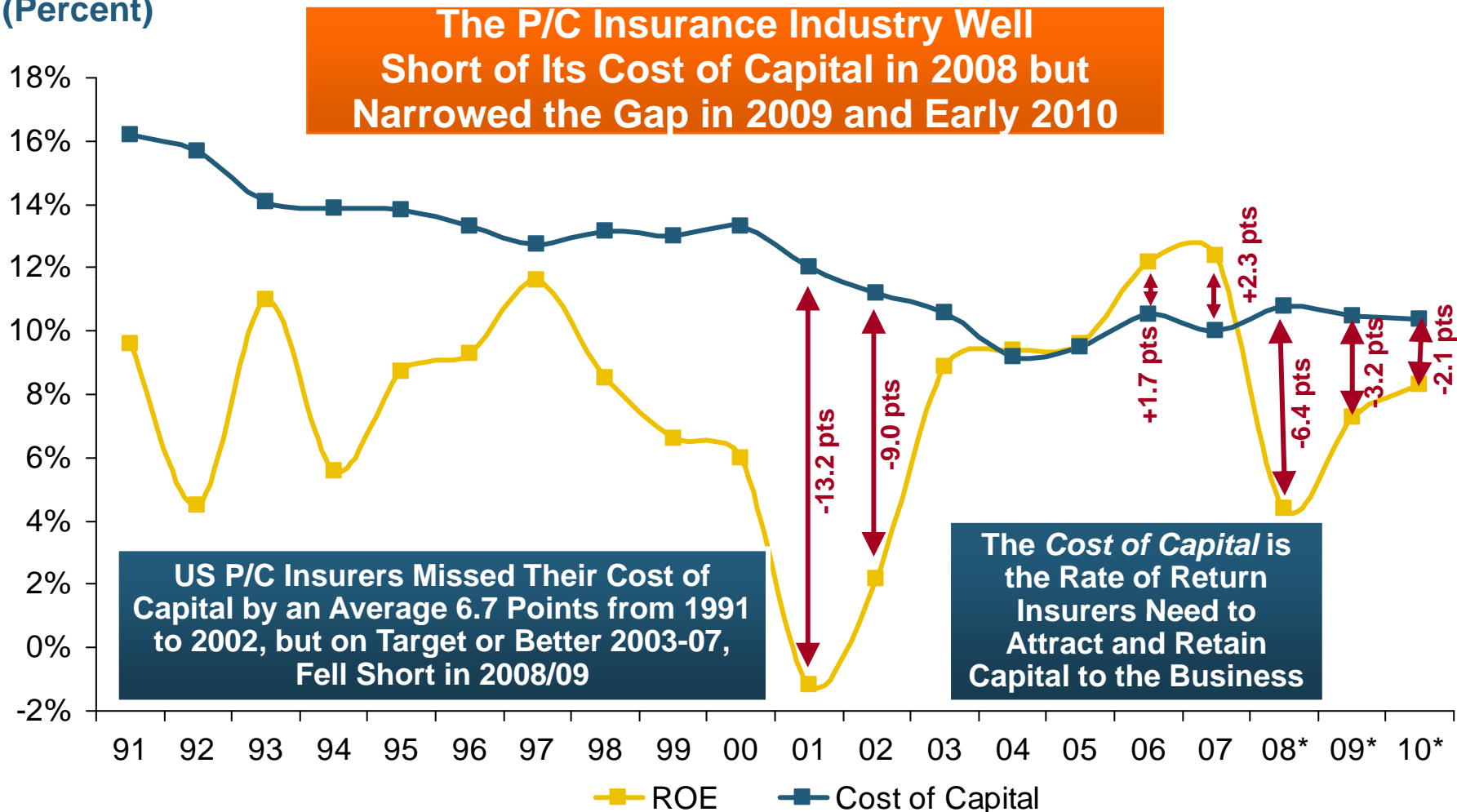
(Percent)



* 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)

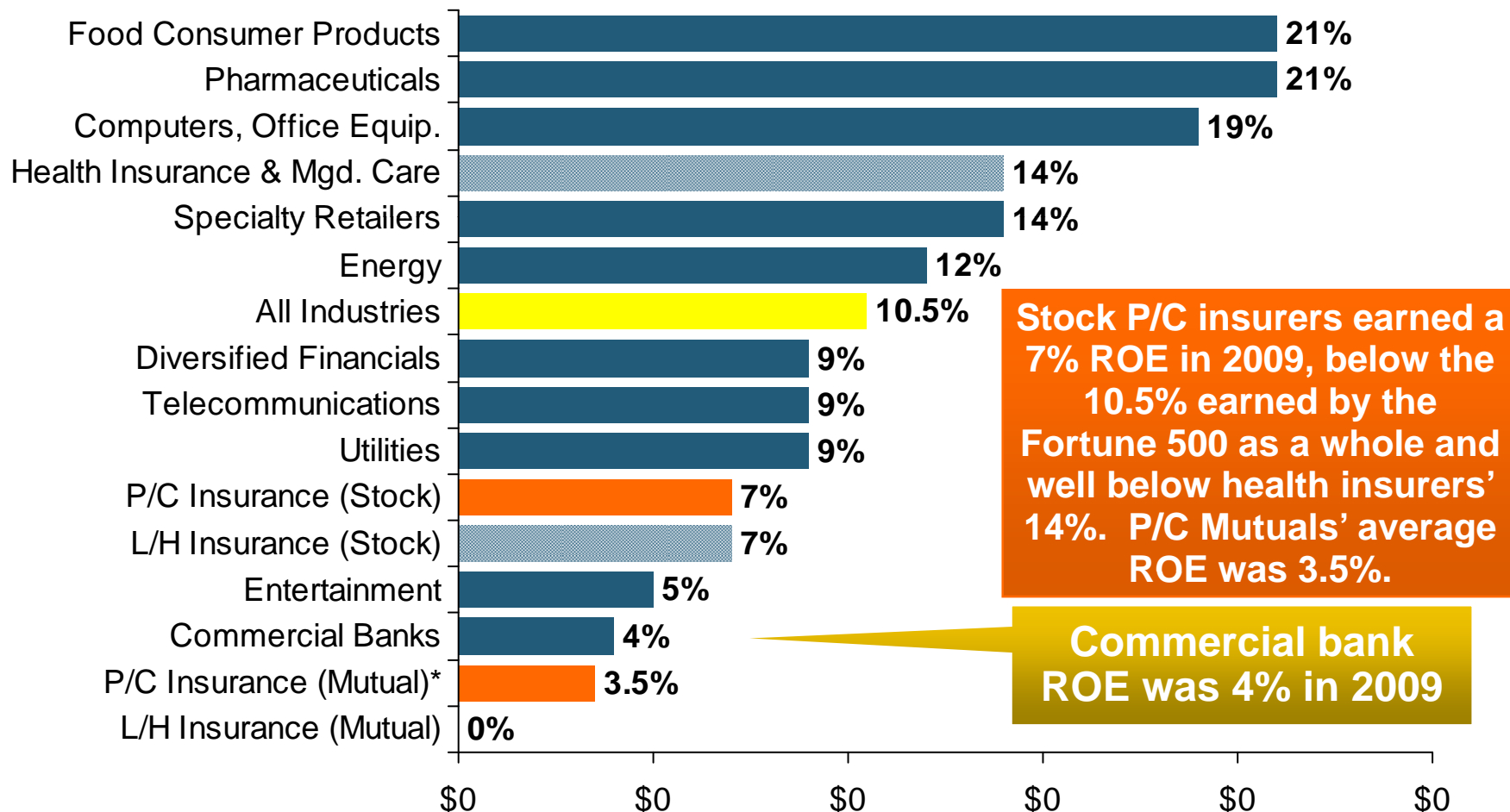


* Return on average surplus in 2008/09 excluding mortgage and financial guaranty insurers.

Source: The Geneva Association, Insurance Information Institute

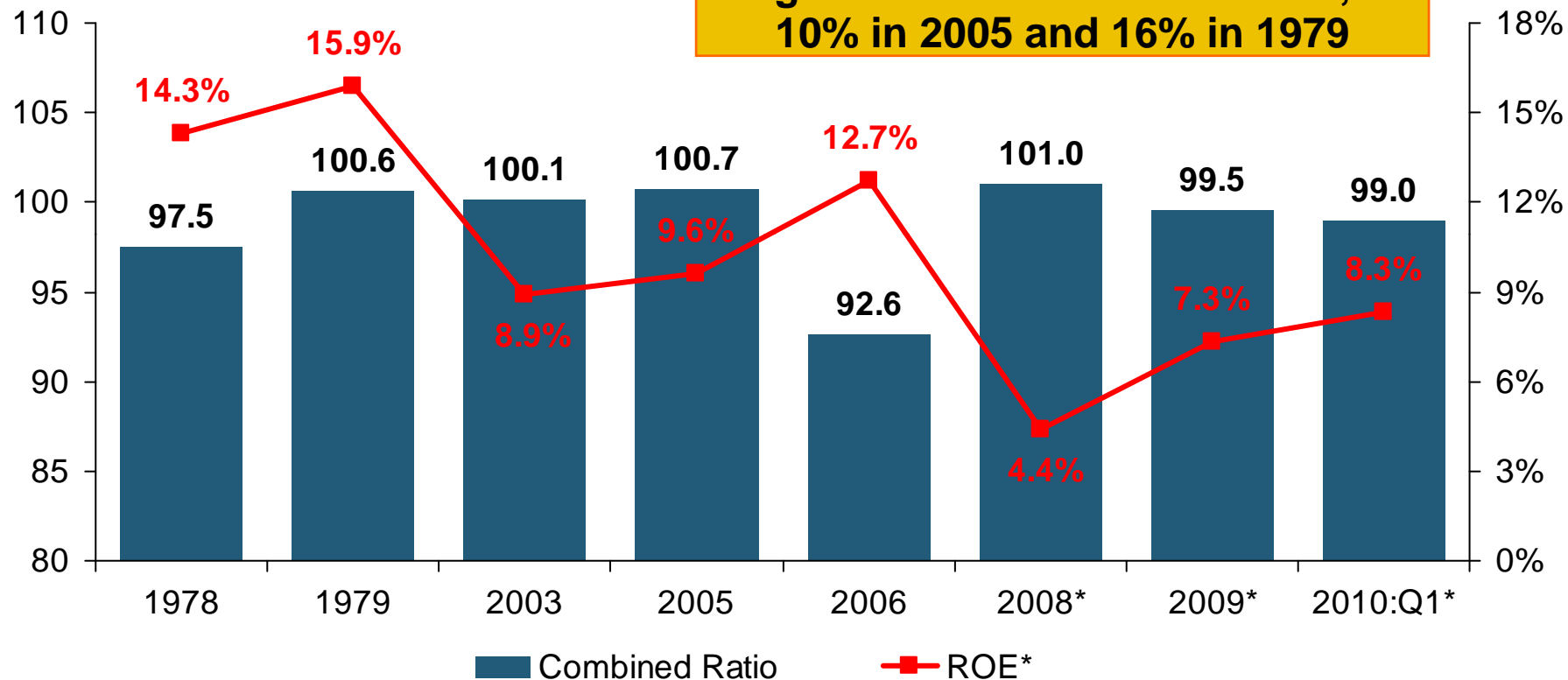
Median ROE for Insurers vs. Financial Firms & Other Key Industries 2009

(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

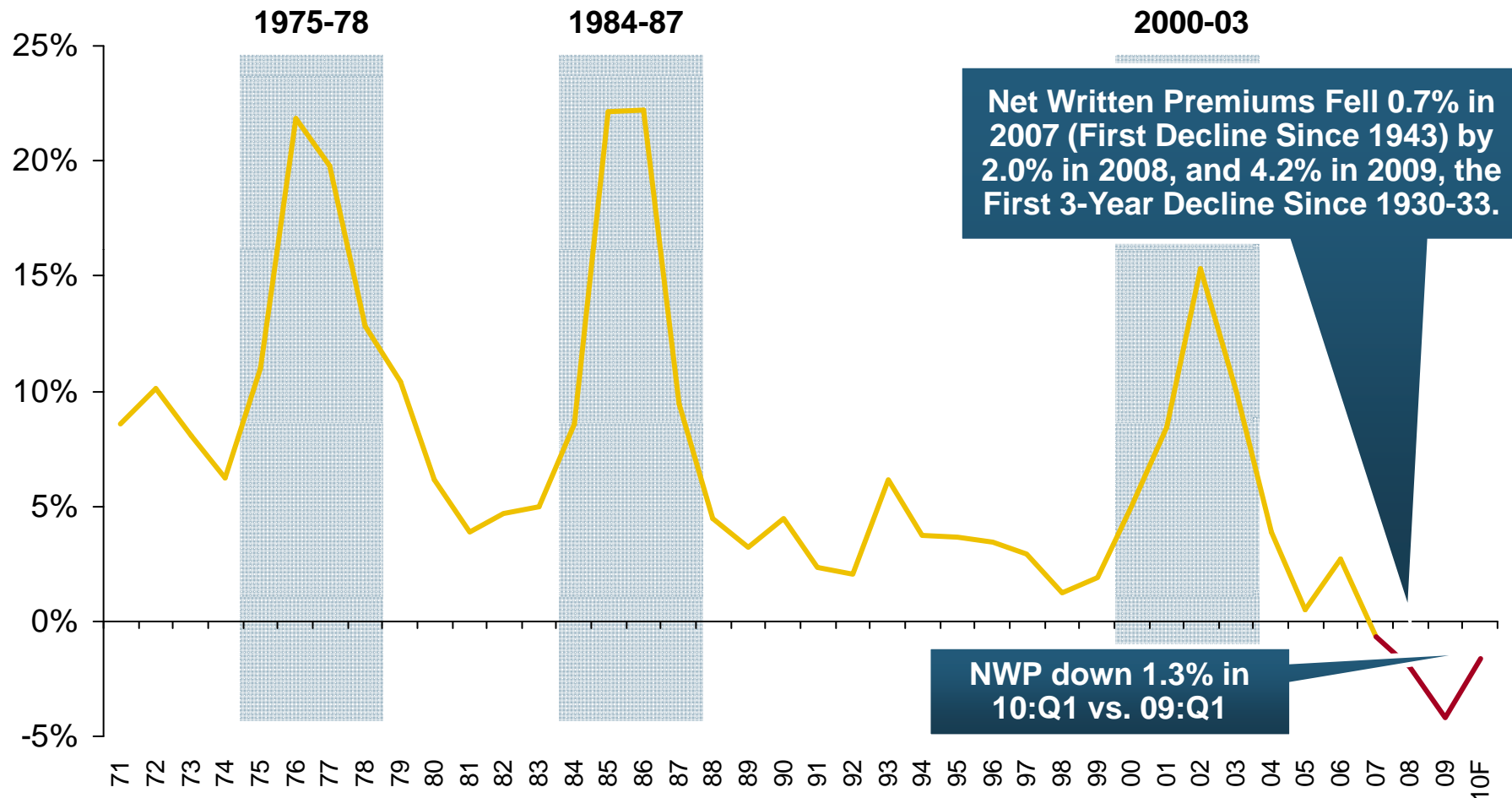
* 2009 and 2010:Q1 figures are return on average statutory surplus. 2008, 2009 and 2010:Q1 figures exclude mortgage and financial guarantee insurers

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

**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)

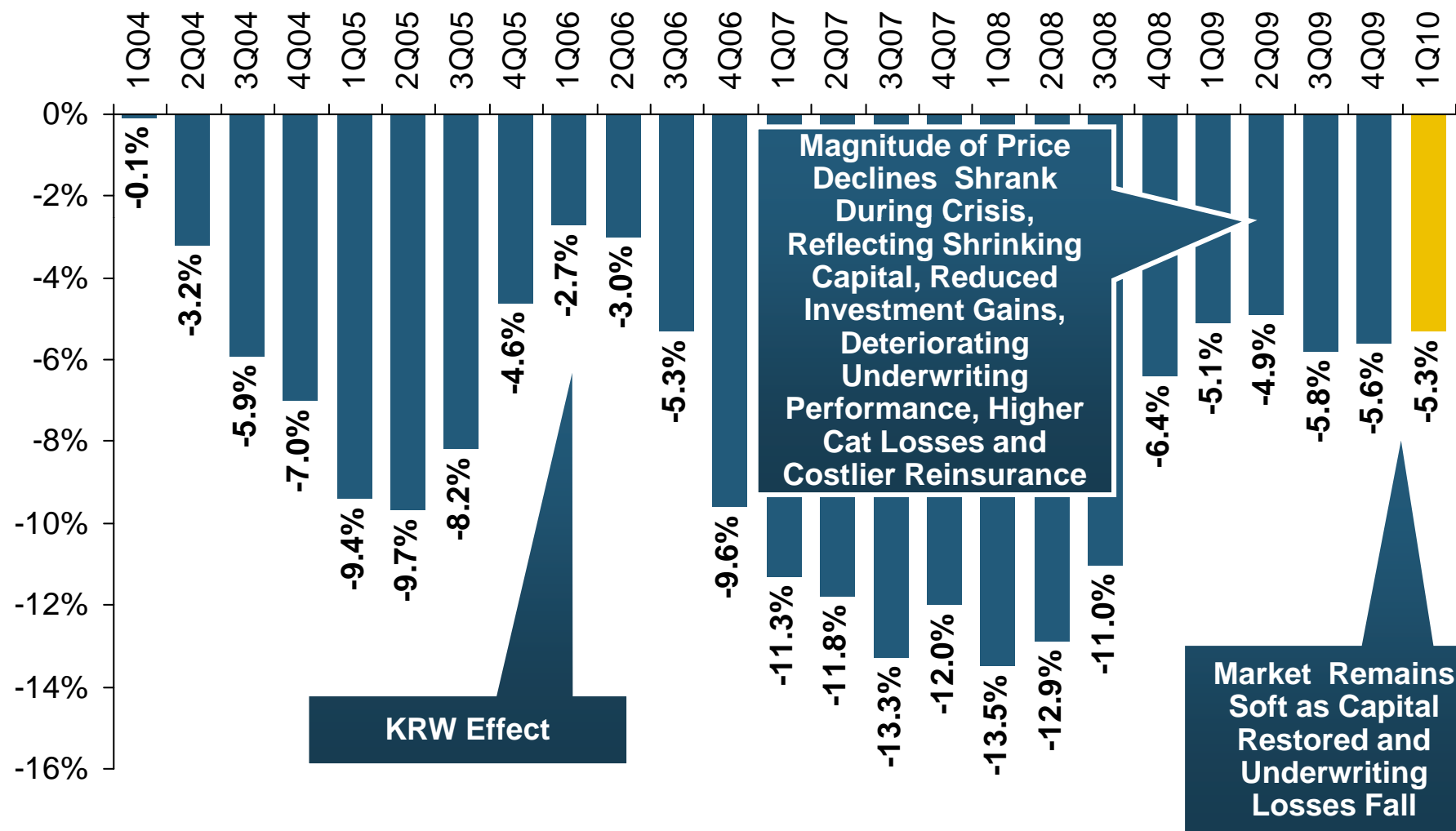


Shaded areas denote "hard market" periods

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

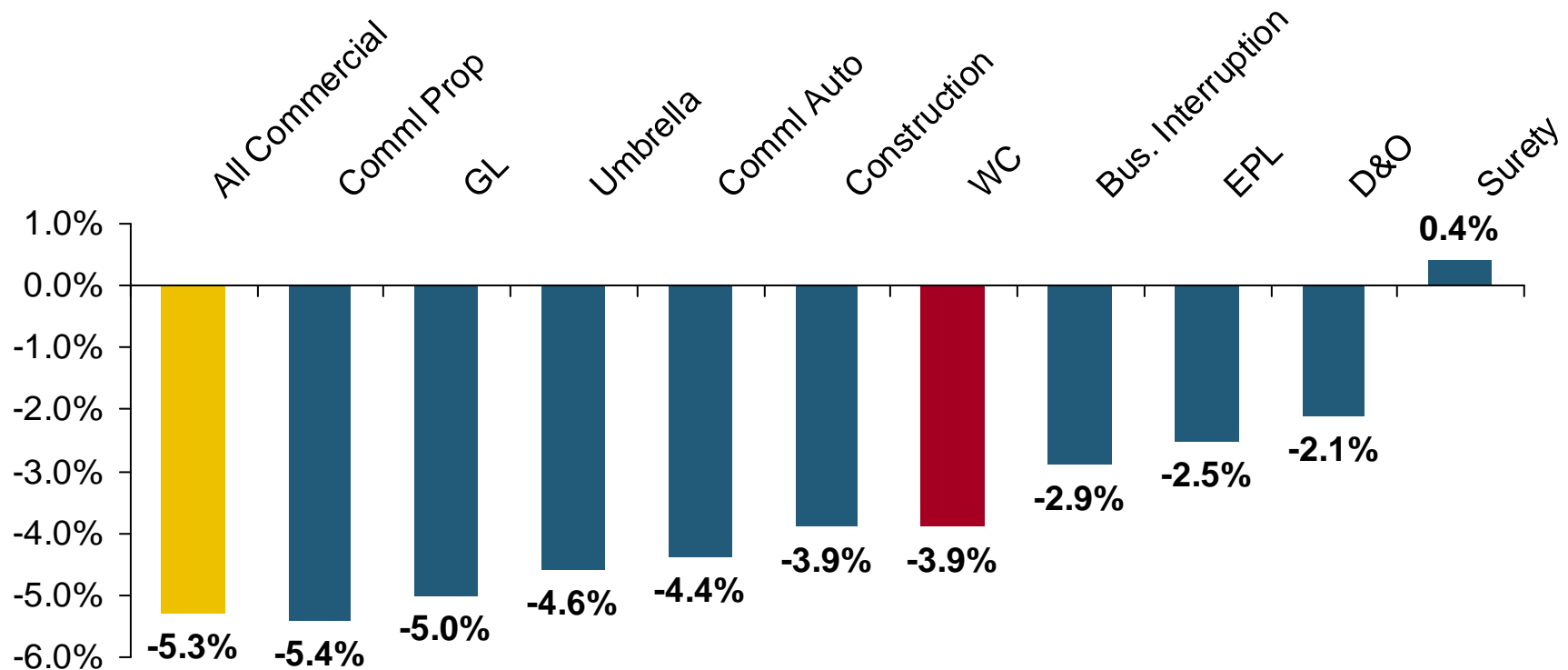
Average Commercial Rate Change, All Lines, (1Q:2004–1Q:2010)

(Percent)



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

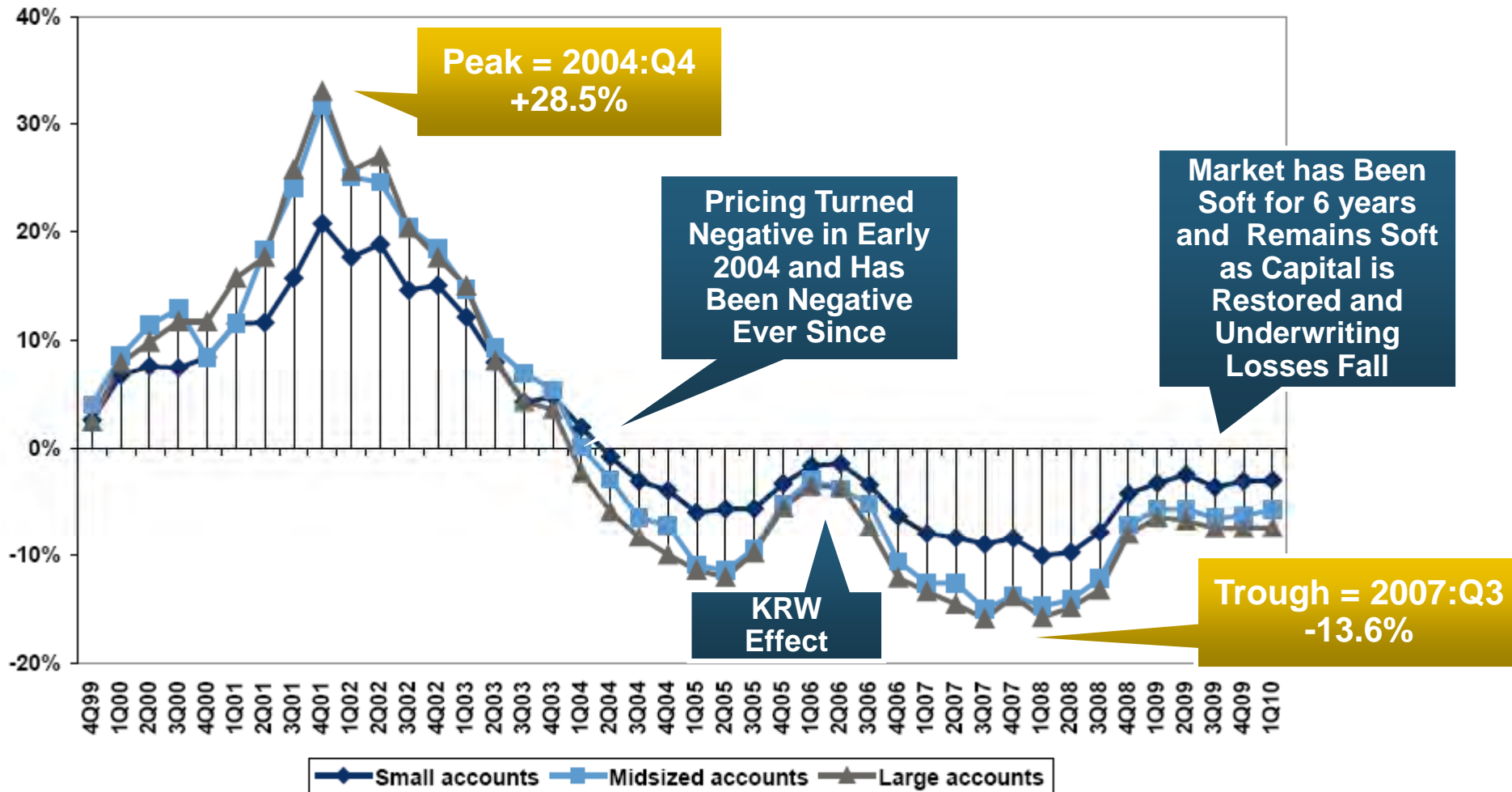
Percentage Change (%)



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

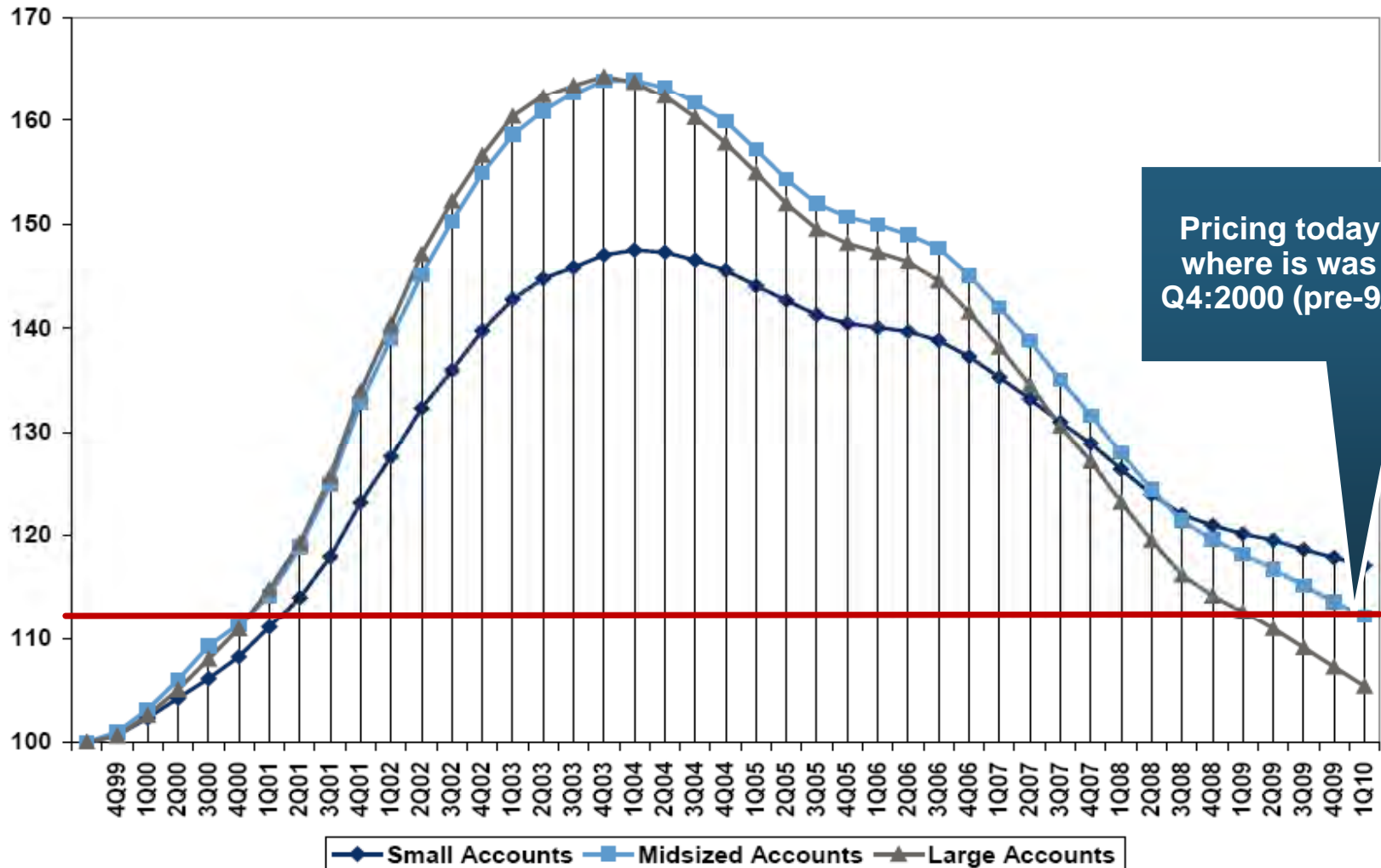
Change in Commercial Rate Renewals, by Account Size: 1999:Q4 to 2010:Q1

Percentage Change (%)



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

1999:Q4 = 100

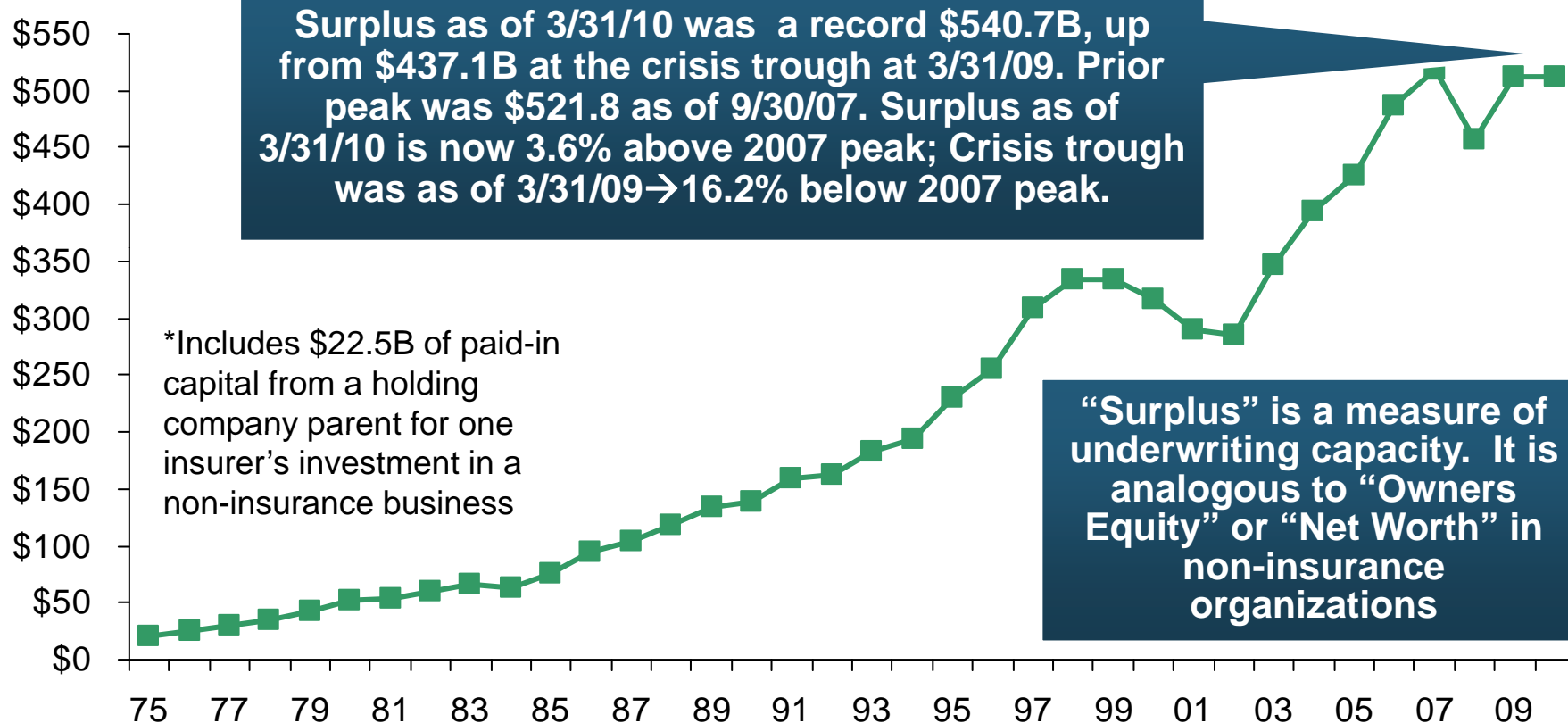


Capital/Policyholder Surplus (US)

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

US Policyholder Surplus: 1975–2010*

(\$ Billions)

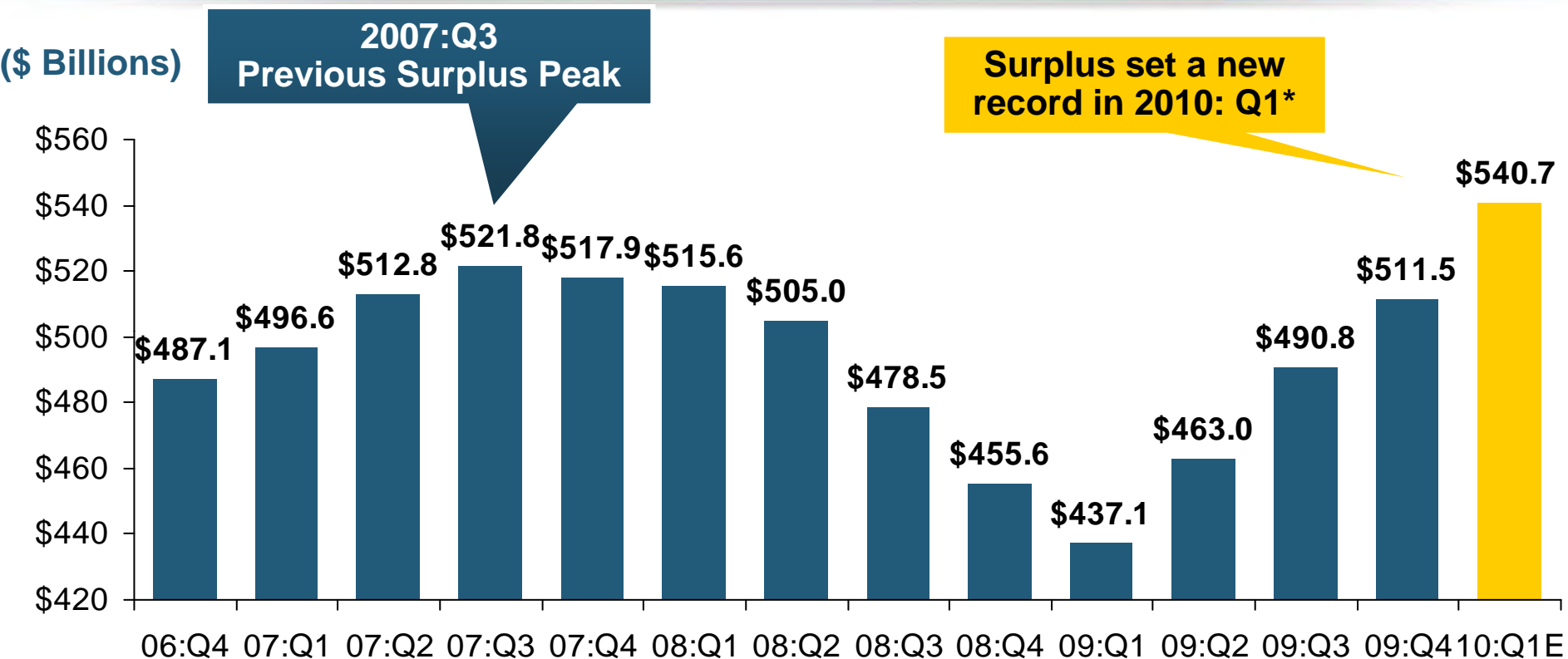


The Premium-to-Surplus Ratio Stood at \$0.82:\$1 as of 12/31/09, A Record Low (at Least in Recent History)

* 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

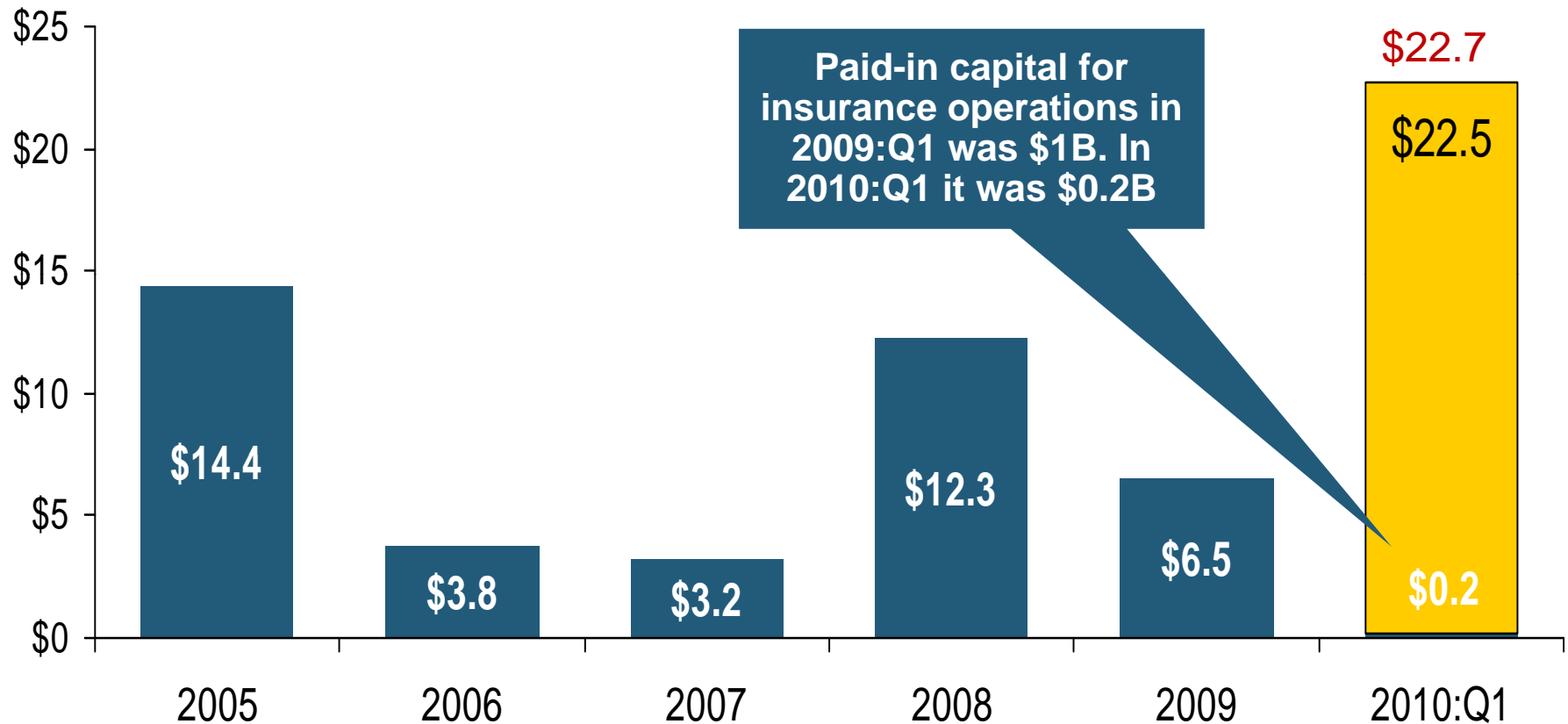
08:Q2: -\$16.6B (-3.2%)
08:Q3: -\$43.3B (-8.3%)
08:Q4: -\$66.2B (-12.9%)
09:Q1: -\$84.7B (-16.2%)

09:Q2: -\$58.8B (-11.2%)
09:Q3: -\$31.8B (-5.9%)
09:Q4: -\$10.3B (-2.0%)
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

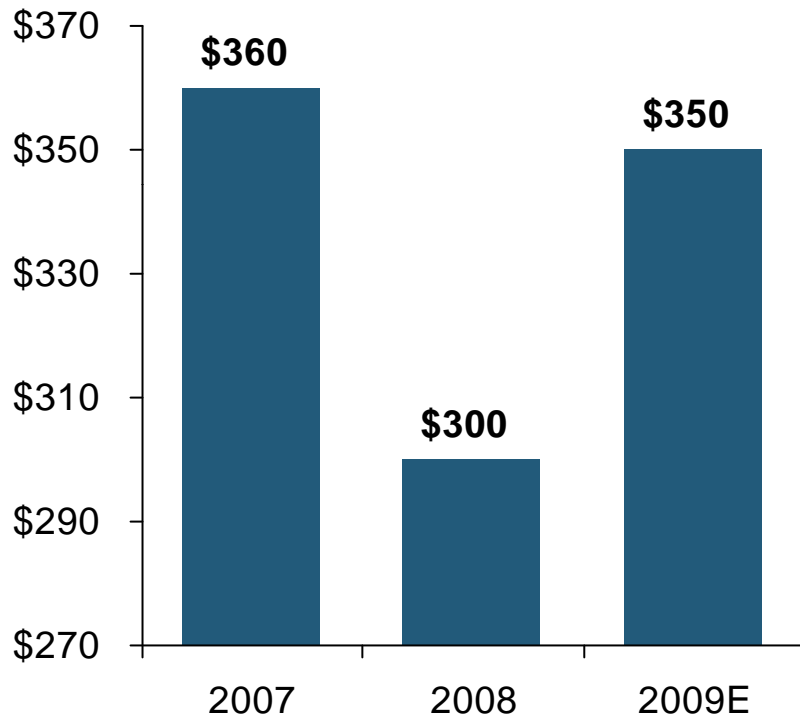
(\$ Billions)



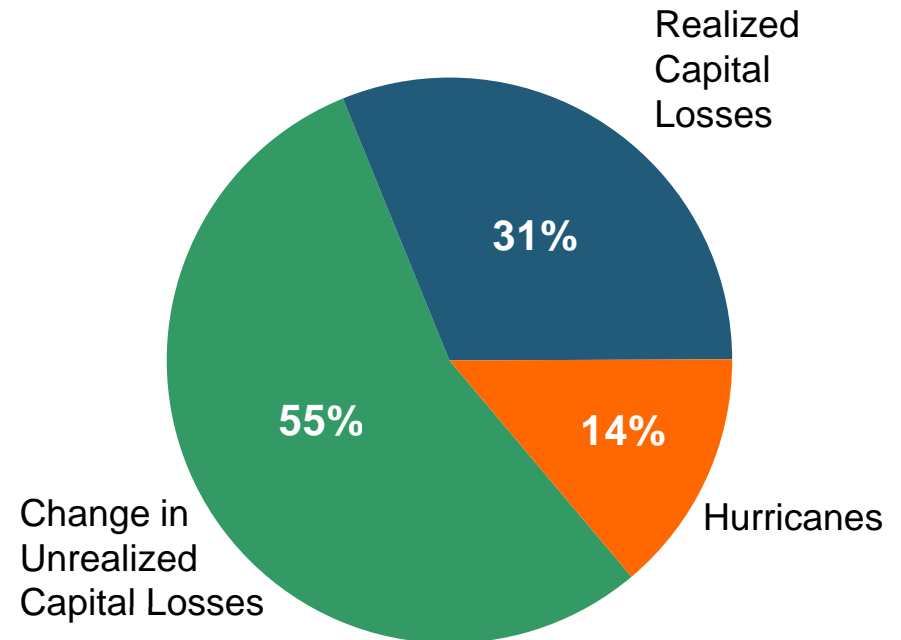
In 2010:Q1 One Insurer's Paid-in Capital Rose by \$22.5B as Part of an Investment in a Non-insurance Business

Global Reinsurance Capacity Shrank in 2008, Mostly Due to Investments

Global Reinsurance Capacity



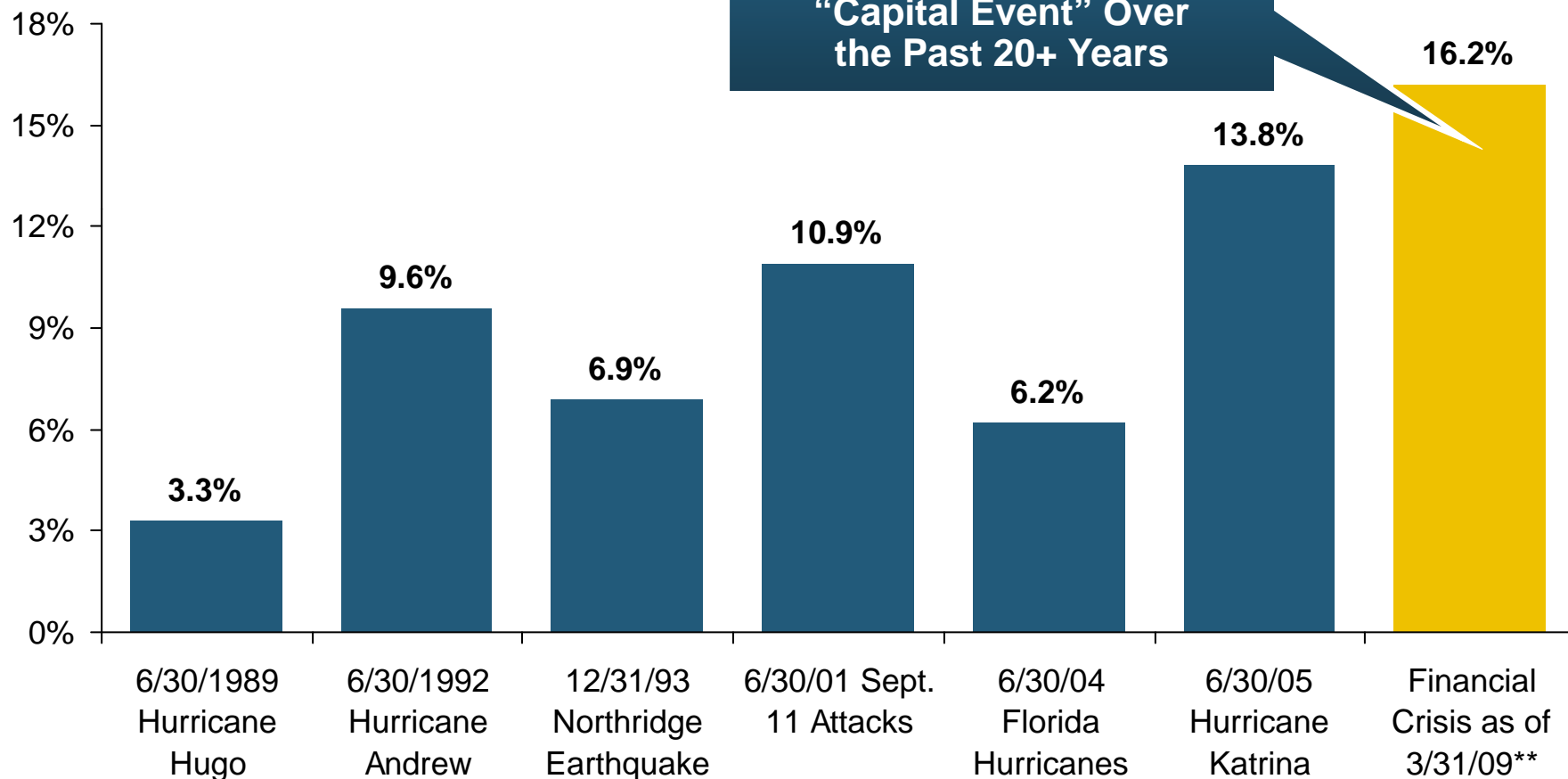
Source of Decline in 2008



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

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

(Percent)

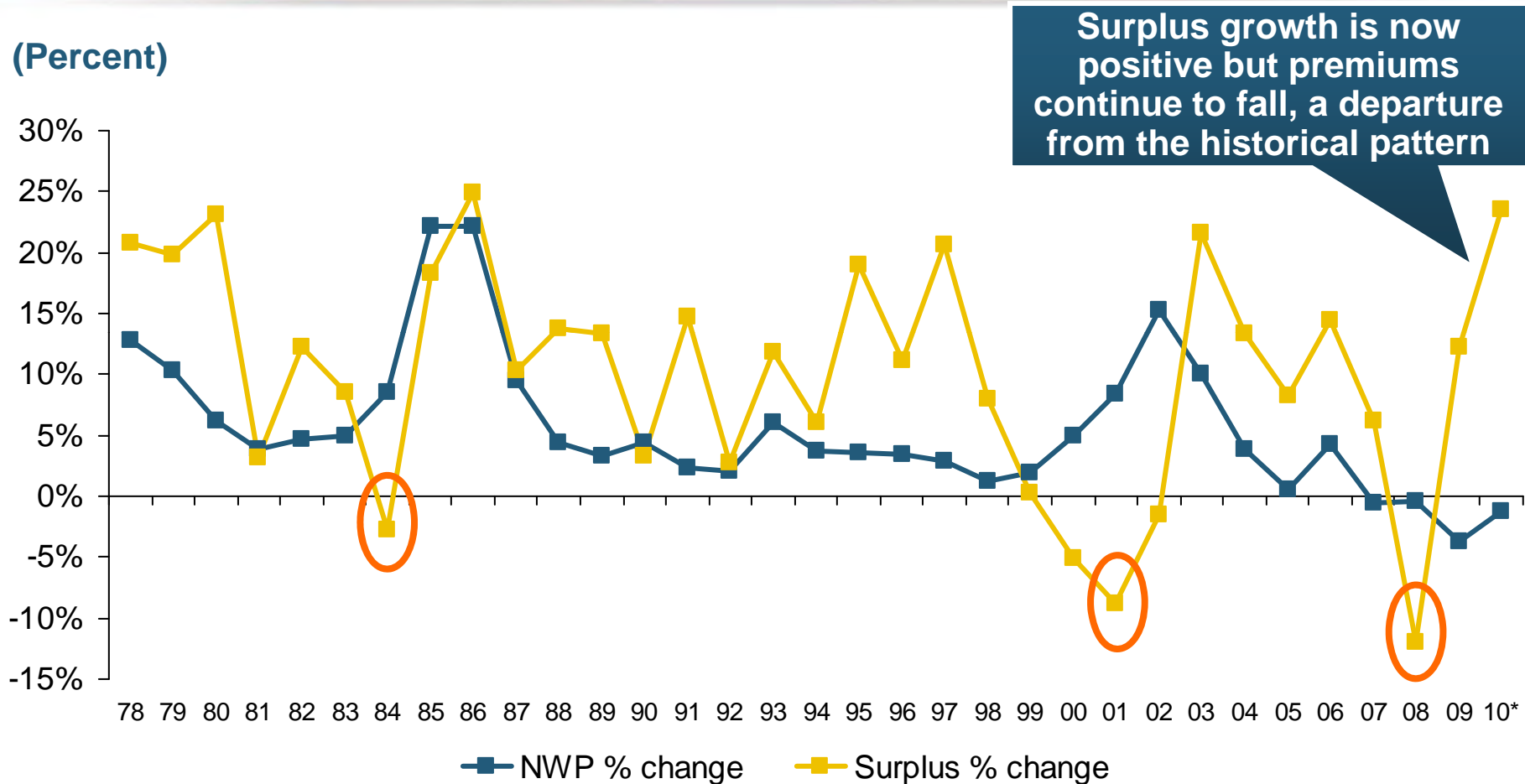


* Ratio is for end-of-quarter surplus immediately prior to event. Date shown is end of quarter prior to event

** 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

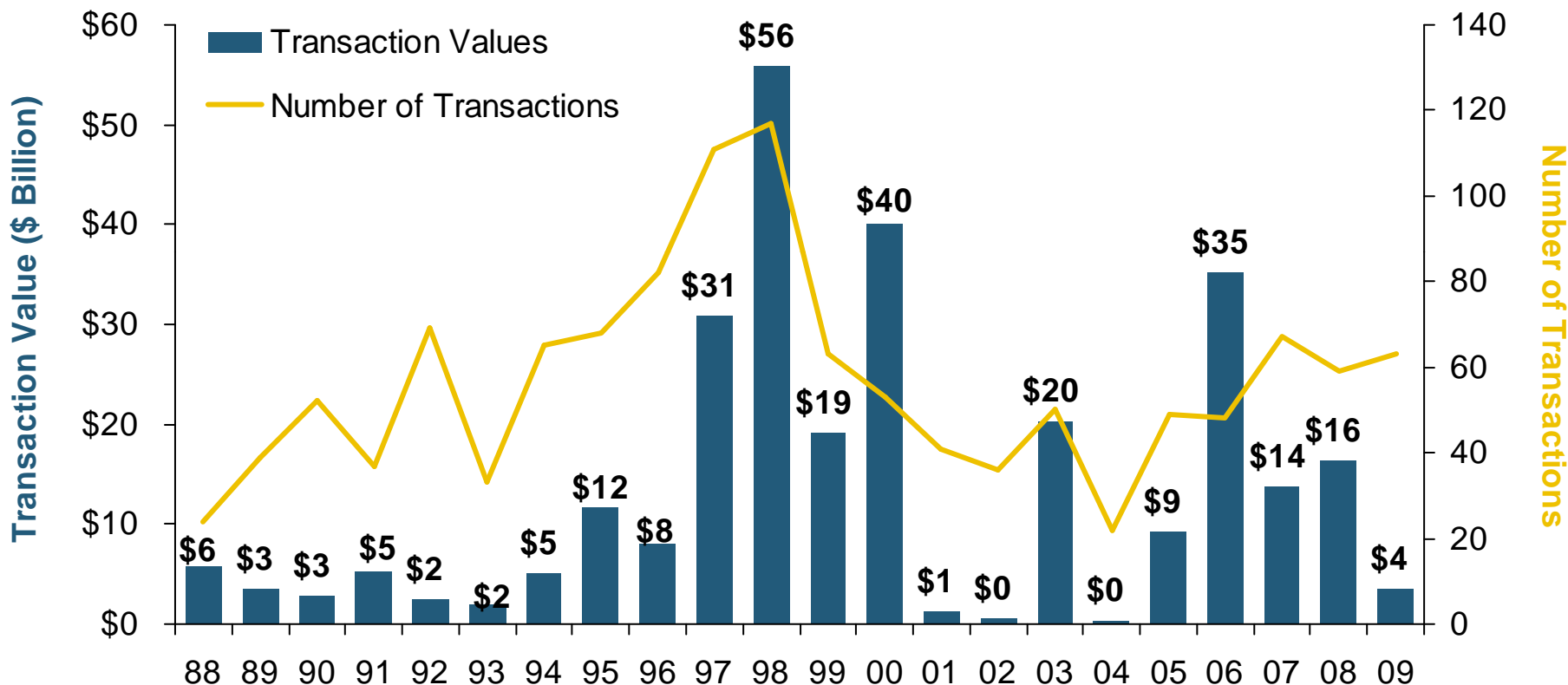
* 2010 NWP and Surplus figures are % changes as of Q1:10 vs Q1:09. Adjusting for unique transaction of insurer the increase is 18.4%.

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.

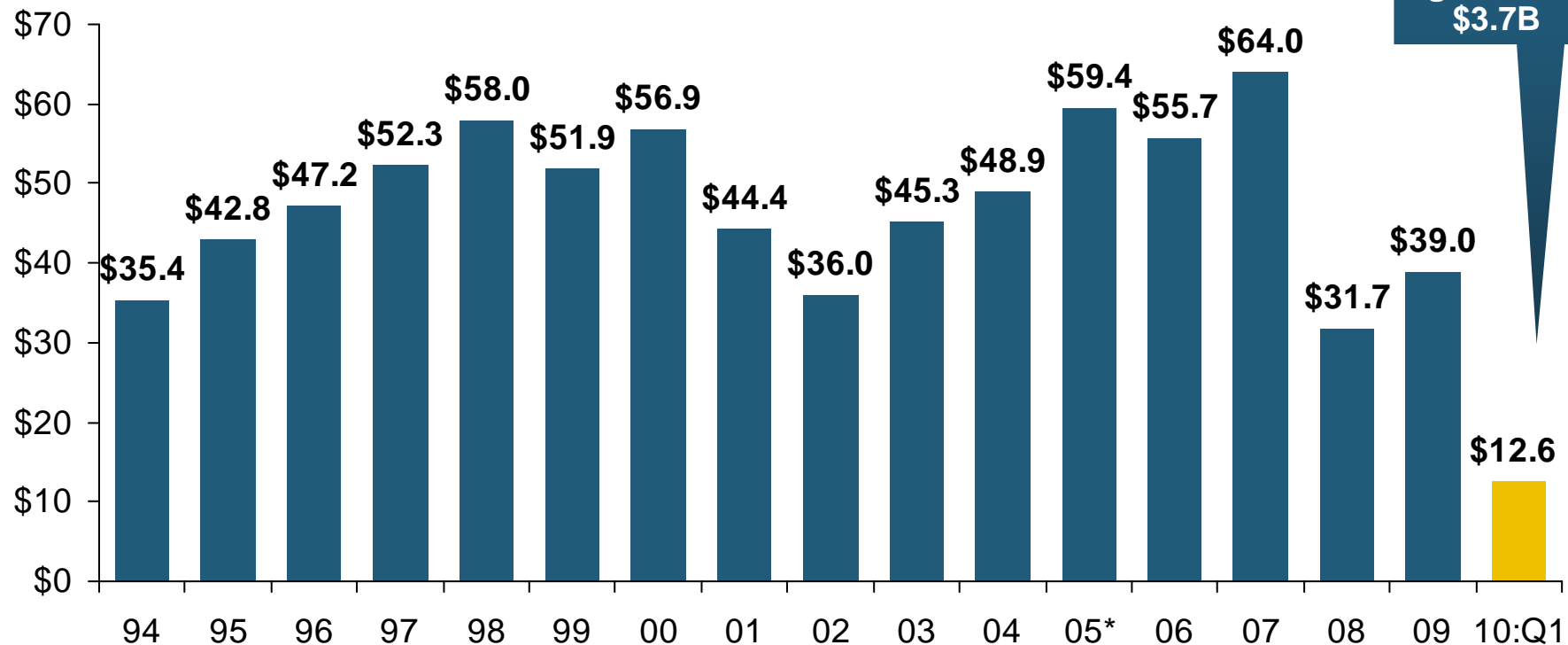
Source: Conning Research & Consulting.

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**

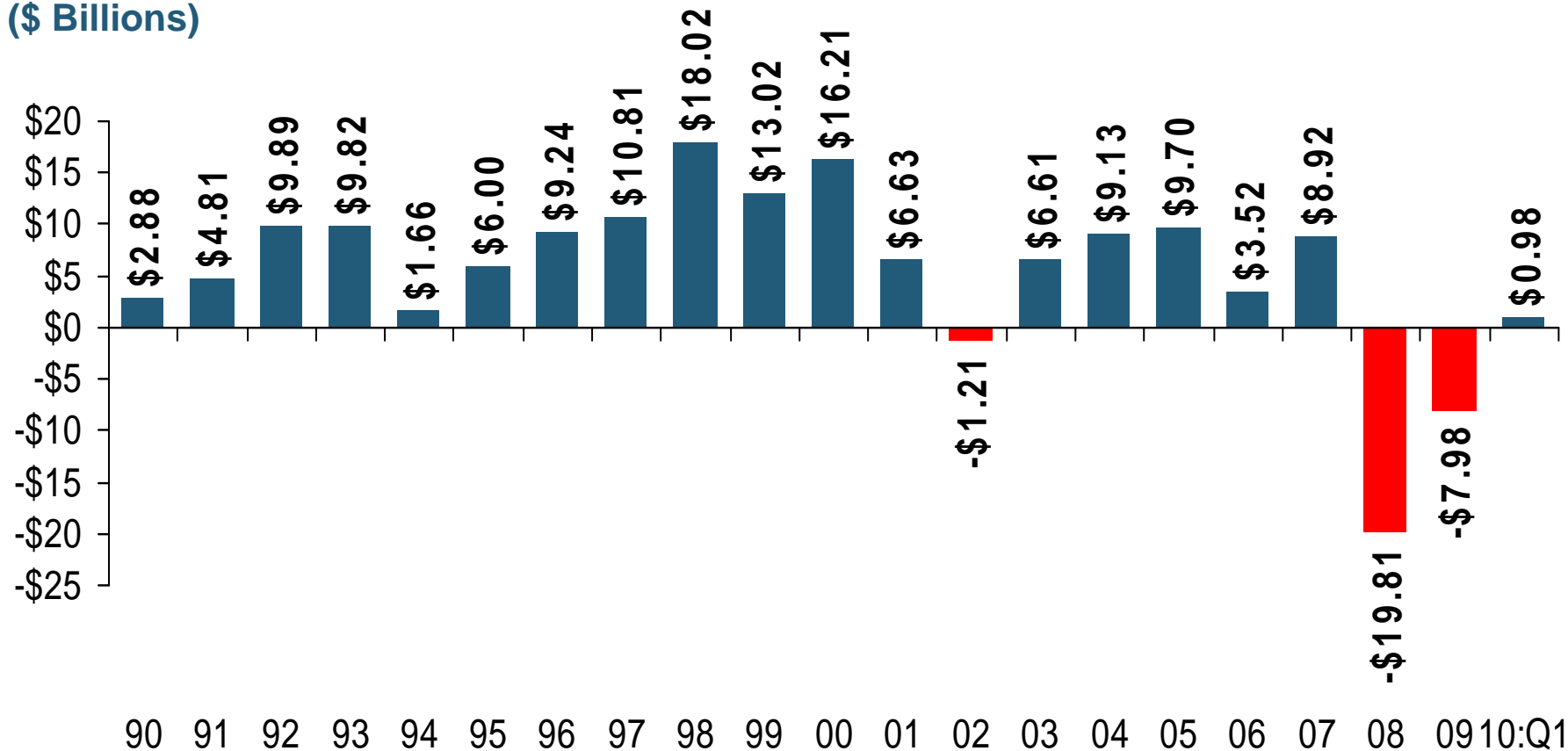
¹ Investment gains consist primarily of interest, stock dividends and realized capital gains and losses.

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

Sources: ISO; Insurance Information Institute.

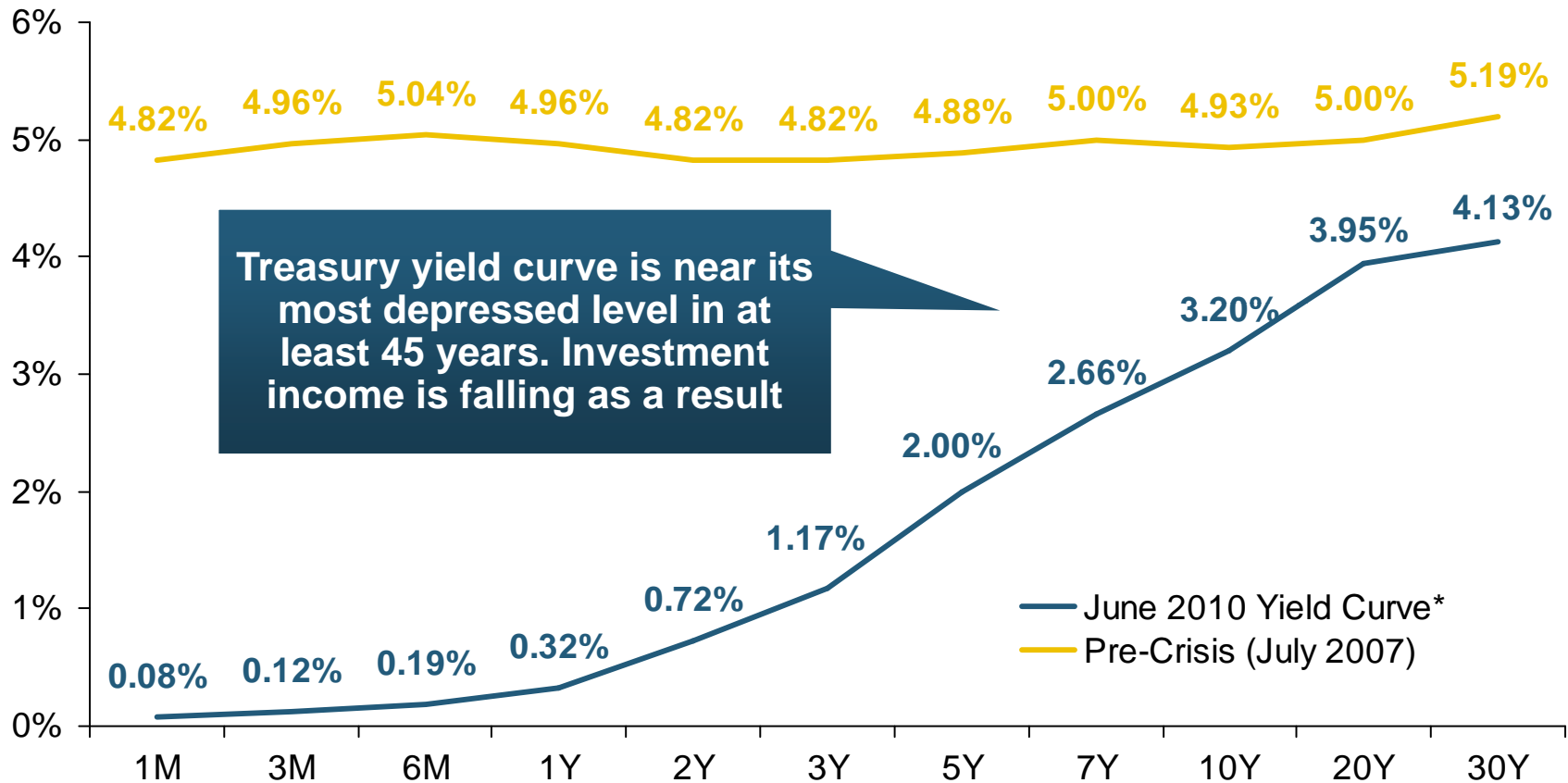
P/C Insurer Net Realized Capital Gains, 1990-2010:Q1

(\$ Billions)



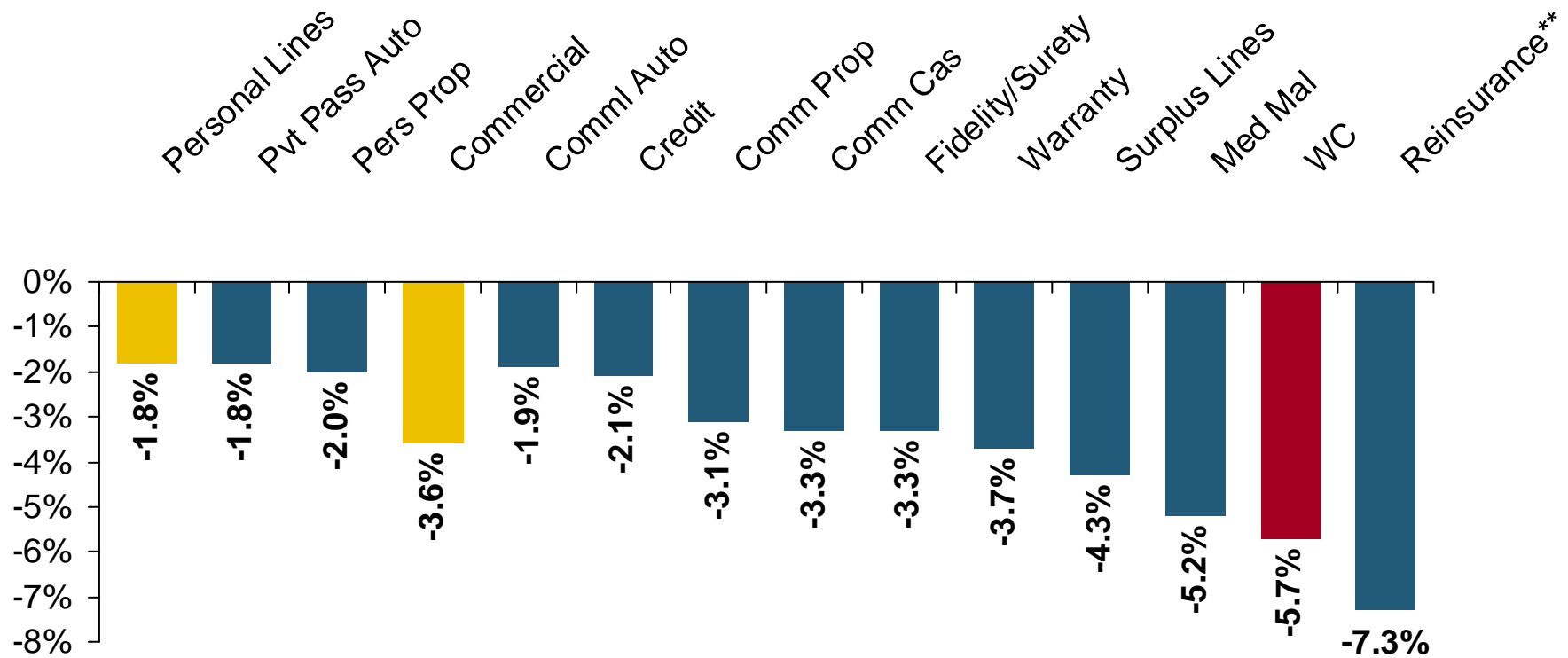
**Realized Capital Losses Were the Primary Cause
of 2008/2009's Large Drop in Profits and ROE**

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

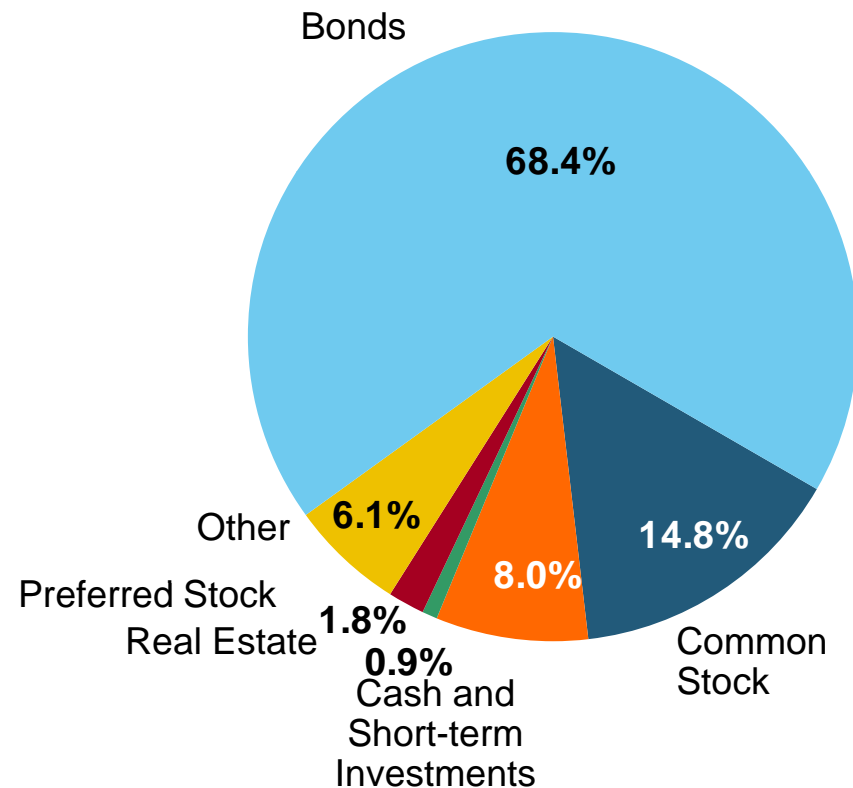
Source: A.M. Best; Insurance Information Institute.

Distribution of P/C Insurance Industry's Investment Portfolio

Portfolio Facts

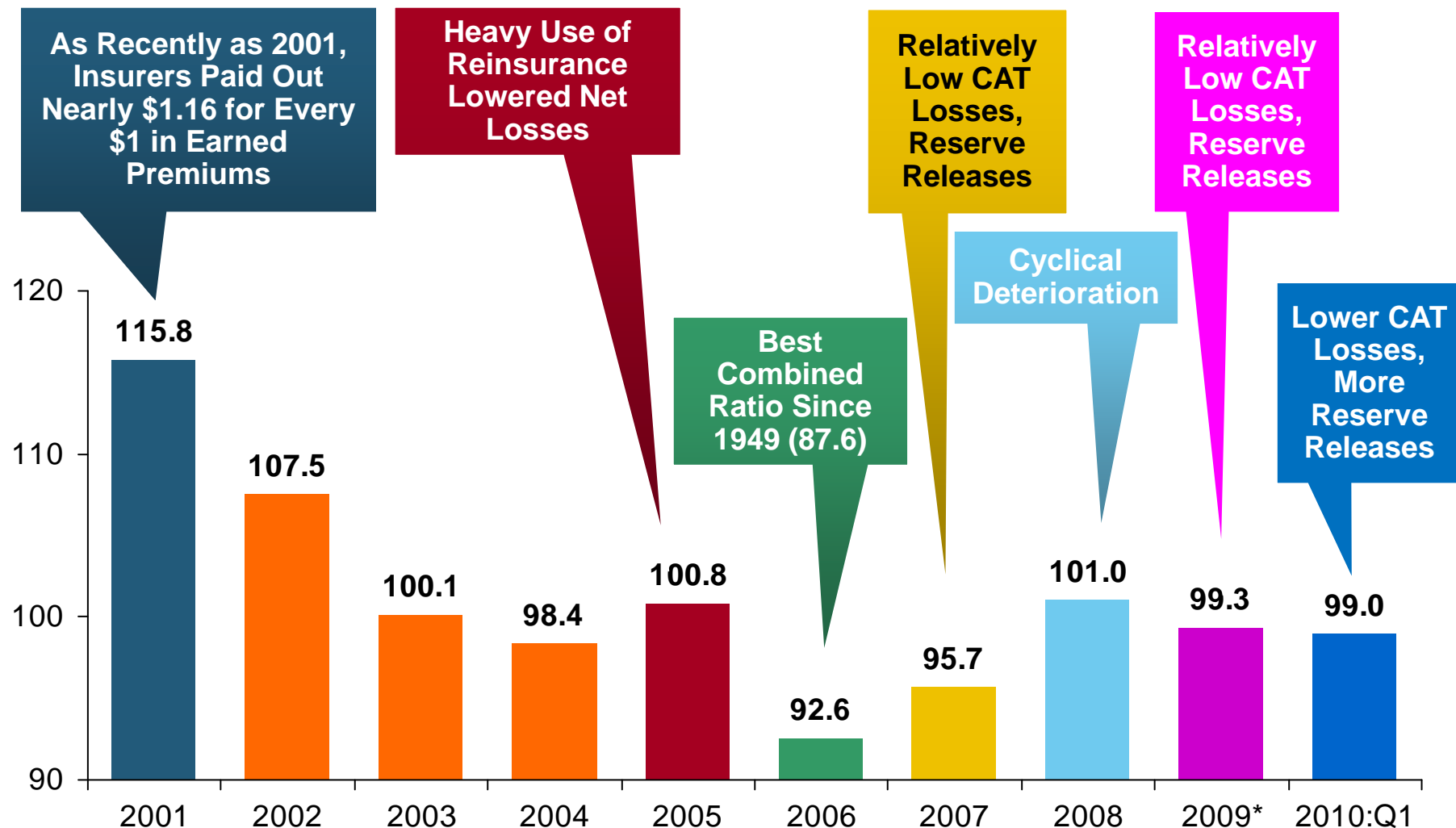
- Invested assets totaled \$1.214 trillion as of 12/31/08
- Insurers are generally conservatively invested, with more than 2/3 of assets invested in bonds as of 12/31/08
- Only about 15% of assets were invested in common stock as of 12/31/08
- Even the most conservative of portfolios was hit hard in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

As of December 31, 2008



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

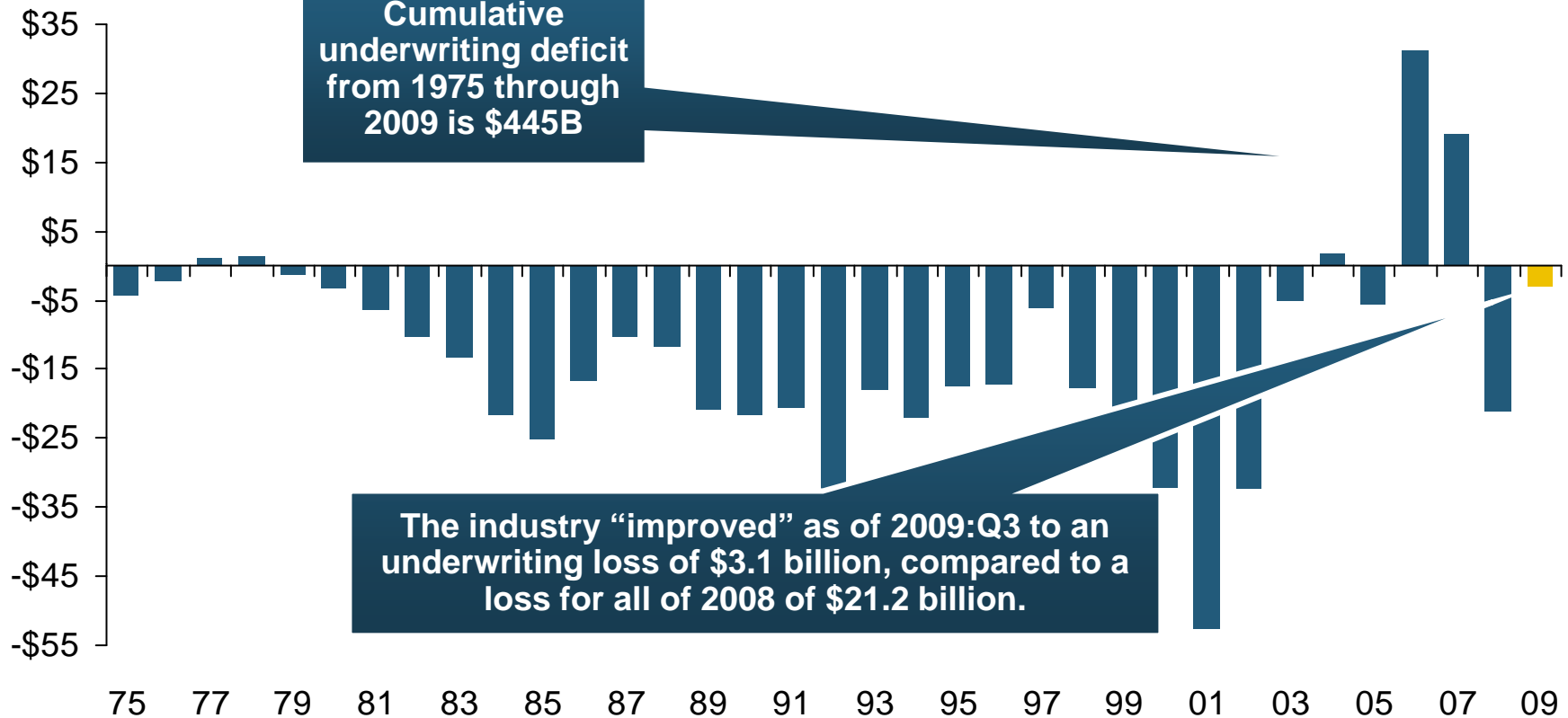
P/C Insurance Industry Combined Ratio, 2001–2010:Q1*



* 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)

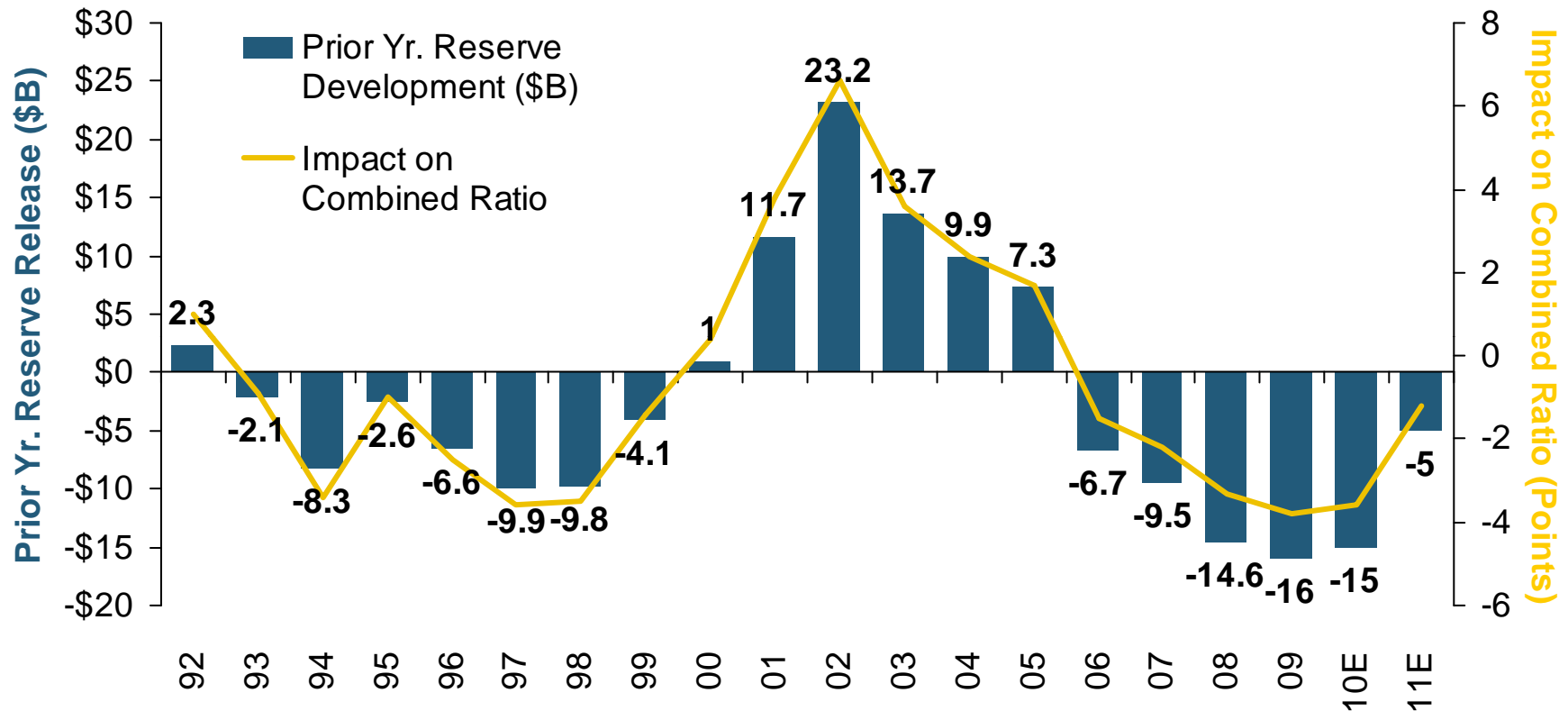


**Large Underwriting Losses Are *NOT* Sustainable
in Current Investment Environment**

* Includes mortgage and financial guarantee insurers.

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

P/C Reserve Development, 1992–2011E



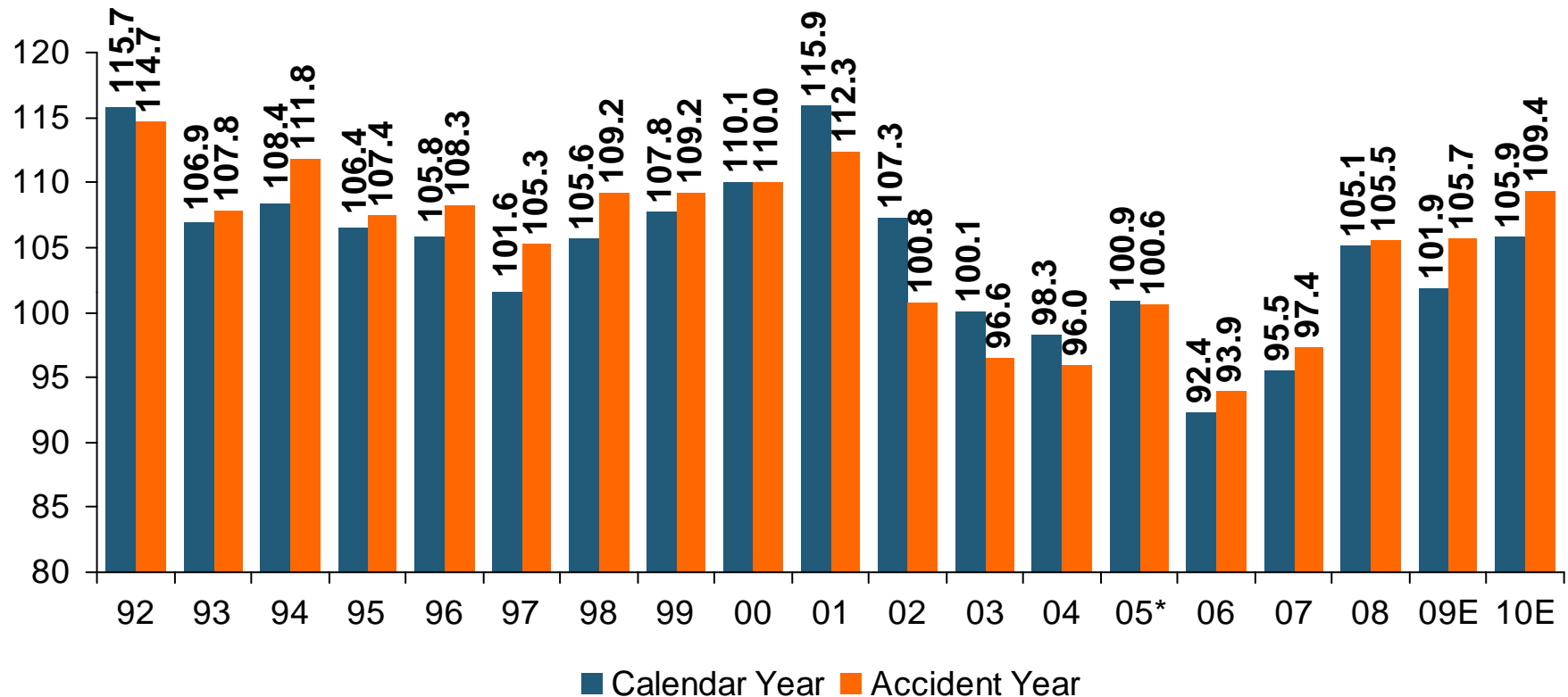
**Reserve Releases Will Expected to Taper Off
in 2010 and Drop Significantly in 2011**

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



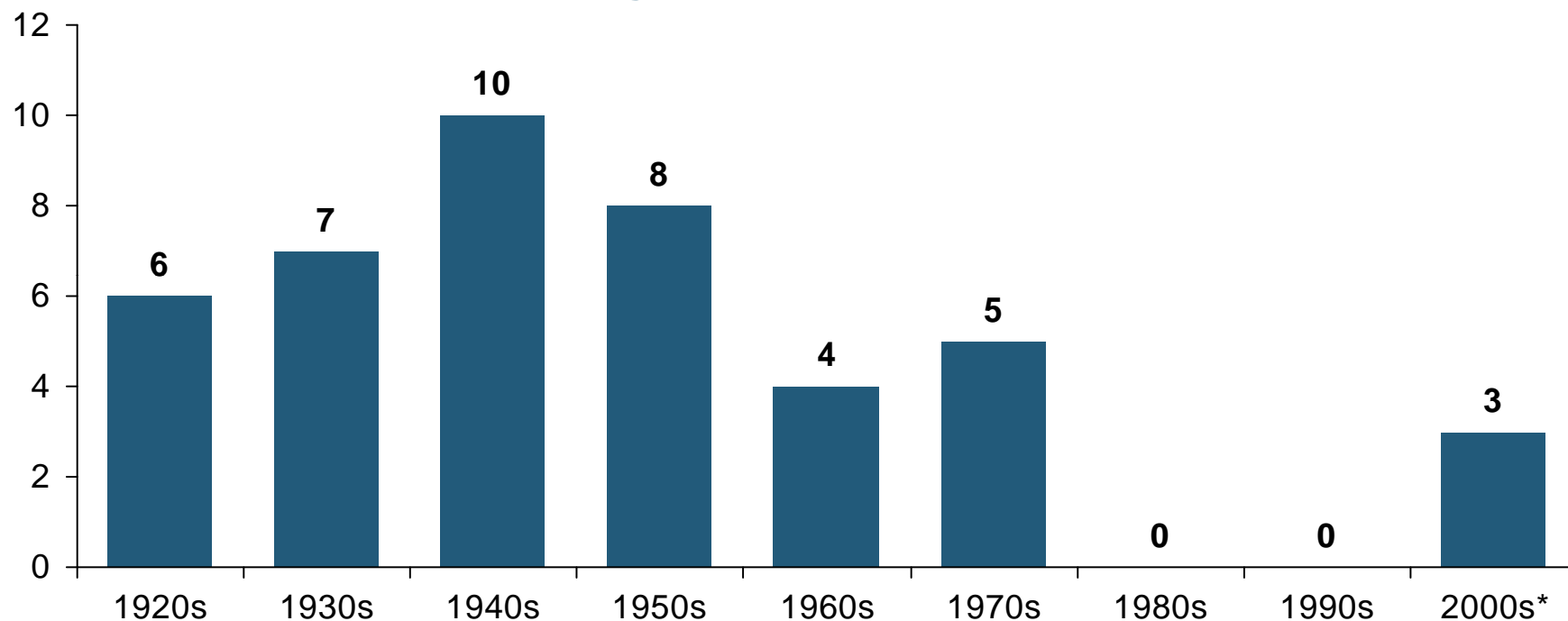
Accident Year Results Show a More Significant Deterioration in Underwriting Performance. Calendar Year Results Are Helped by Reserve Releases

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.

- **The Workers Compensation Line Has Been Significantly Impacted by The Weak Economy**
 - ◆ Recouping exposure losses will take years
- **Large Differences in Growth Prospects for Different Parts of the US, as well as Various Industries and Occupations Important to WC**
 - ◆ High hazard classes are always impacted disproportionately during recessions and some are in the midst of secular declines
- **The New Decade Brings Numerous Operating Challenges**
- **Impacts of Regulatory/Legislative Changes Still Not Completely Known**
- **Overall P/C Operating Environment to Become More Challenging**
- **Growth Likely in Overall P/C Insurance Industry in 2011 for the First Time Since 2006**

Insurance Information Institute Online:

www.iii.org

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

Twitter: twitter.com/bob_hartwig