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Overview & Outlook for the P/C Insurance Industry

Challenges and Opportunities for 2011 and Beyond

PCI Joint Underwriting and Marketing Seminar
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Presentation Outline

- **Reasons for Optimism, Causes for Concern in the P/C Insurance Industry**
- **P/C Profitability Overview & Outlook**
- **The Elusive Market Turn: When, Why, How and *IF***
  - Pricing: Up, Down or Sideways?
  - Underwriting Trends: Drivers of Future Market Firming?
  - Investments: New Investment Reality Not Reflected in Pricing
  - Expenses: Cyclical Increase
  - Leverage/Capital Management: Excess Capacity and Squeezing it Out
- **M&A Activity in the P/C Insurance Industry**
- **External Factors Influencing Profitability**
  - Tort System Review: Overview and Causes for Concern
  - Inflation
- **Growth in the Aftermath of the Great Recession**
  - Crisis-Driven Exposure Issues: Commercial Lines
- **Global Issues Impacting P/C Insurance**
- **Catastrophe Loss Review**
- **Social Media Strategy**
- **Q&A**

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

The Outlook for the Economy Has Brightened, But the Outlook for P/C Insurance Is Mixed

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

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- **Economic Recovery in US is Self-Sustaining and Strengthening**
  - No Double Dip or Second Recession
  - Economy is more resilient than most pundits presume
- **Consumer Confidence is Gradually Improving**
- **Consumer Spending is Recovering Gradually**
- **Consumer and Business Lending Are Expanding**
- **Housing Market Remains Weak, but Some Improvement Expected in 2011**
- **Inflation Remains Tame**
  - Runaway inflation is highly unlikely; Fed has things under control
  - Deflation—threat has disappeared
- **Private Sector Hiring is Consistently Positive for 14 Months**
  - Acceleration in hiring later in 2011 compared to 2010
  - No significant secondary spike in unemployment
- **Japan Threat to Global Economy Overstated**
- **Sovereign Debt, Muni Bond "Crises" Overblown**
- **Current Middle East Turmoil Poses Only Moderate Risk to US Economy**
- **Interest Rates Are Rising but Remain Low by Historical Standards**
- **Stock and Bond Markets More Stable, Less Volatile**
- **Political Environment Is More Hospitable to Business Interests**

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

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- **Era of Mass P/C Insurance Exposure Destruction Has Ended**
  - Personal and commercial exposure growth is virtually certain in 2011
  - But restoration of destroyed exposure will take 3-5 years in US
- **Exposure Growth Returned in in 2nd Half 2010, Will Accelerate in 2011**
- **P/C Industry Saw Growth in 2010 (+0.8%) for the First Time Since 2006**
- **Increasing Private Sector Hiring Will Drive Payrolls/WC Exposures**
  - Wage growth is also positive and could modestly accelerate
- **Increase in Demand for Commercial Insurance Is in its Earliest Stages and Will Accelerate in 2011**
  - **Includes workers comp, commercial auto, marine, many liability coverages, D&O**
  - **Laggards: Property, inland marine, aviation**
  - **Personal Lines: Auto leads, homeowners lags**
- **Investment Environment Is/Remains Much More Favorable**
  - Return of realized capital gains as a profit driver
  - Interest rates are low but are rising→Boost to investment income
- **Agent Commissions Should Begin to Rise in 2011**
- **Demand, Capital Management Strategies Will Temper Overcapitalization**

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

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- **Economic Recovery Is Not as Broad Based as Past Recoveries**
  - Housing, Construction remain weak
- **Recovery Is Uneven**
  - Certain states remain in recession and recoveries will lag: CA, FL, MI, NV
- **Credit Markets Are Not Completely Yet Healed**
  - While the financial sector has strengthened, hundreds more banks failures are possible
- **Consumers/Businesses Will Remain Cautious in their Borrowing/Spending**
- **Energy and Commodity Price Volatility Are Serious Economic Risks**
  - Effects can be disruptive to a fragile recovery even without igniting overall inflation
  - Concern over serial bubbles in various economic sectors on a global scale
- **Financial Markets, While Calm Now, Remain Jittery**
  - Markets buy into “crisis du jour” mindset quickly; Another “Flash Crash” possibility
  - Currency risk is elevated
- **Minor Muni Bond Default(s) Could Result in Irrational Market Response**
- **Potential for Botched Implementation of Dodd-Frank**
  - Systemic risk definition may be too broad
  - Banks will eventually find a way to screw up the economy—again
- **Strength of Admin/Congress Commitment to Pro-Business Policies Unclear**

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

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- **Exposure Loss Was Extraordinary, Concentrated in Commercial Lines**
  - Will take years to restore lost capacity
  - Capacity will not be restored in the same industrial or geographic sectors
  - Public sector pain has a long way to go
- **Consumers Emerged from the Crisis Much More Cost Conscious**
  - Quicker to shop/switch; Price elasticity of demand is higher
  - Heightens retention challenge
- **Commercial Customers Remain Comfortable/Able Retaining More Risk**
  - "Leakage" remains a problem (ART, captives, self insurance, large ded. progs.)
- **Strength of Recovery Insufficient to Absorb Excess Capital or Firm Pricing**
- **P/C Insurance Industry Capacity as of 12/31/10 Is at Record Levels and Has Recovered 100%+ of the Capital Lost During the Financial Crisis**
  - The industry is overcapitalized by approximately $100 billion
  - Record capacity, depressed exposures (S>D) mean that generally soft market conditions will persist through 2011
- **There is No Catalyst for a Robust Hard Market at the Current Time**
- **Pricing Today Does Not Reflect New Investment Realties or Underlying Deterioration in Underwriting Performance Masked by Release of Prior-Year Reserves**

Source: Insurance Information Institute.

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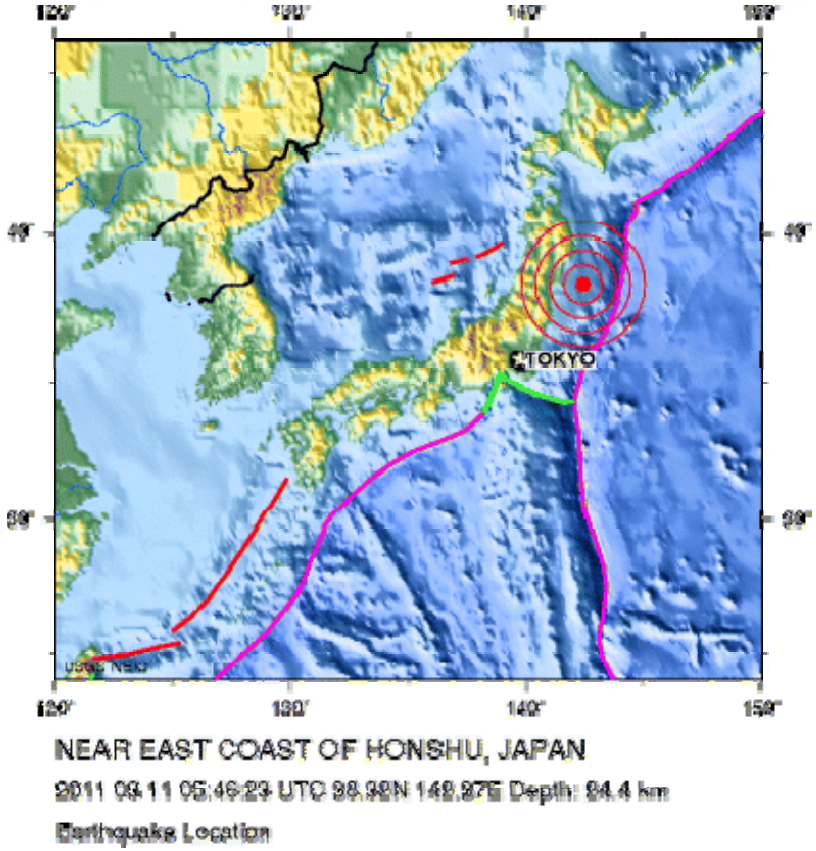
Summary of Japan Earthquake

The March 11 Quake is Just the Most Recent of Several Large Catastrophe Losses

Location of March 11, 2011 Earthquake Near Sendai, Honshu, Japan



LOCATION

130 km (80 miles) E of **Sendai, Honshu, Japan**
178 km (110 miles) E of **Yamagata, Honshu, Japan**
178 km (110 miles) ENE of **Fukushima, Honshu, Japan**
373 km (231 miles) NE of **TOKYO, Japan**

March 11 Earthquake Facts as of 3/24/2011

- Magnitude 9.0 earthquake struck Japan at 2:46PM local time (2:46AM Eastern) off the northeast cost of Honshu, 80 miles east of the city of Sendai
- Quake is among the 5 strongest in recorded history and the strongest in the 140 years for which records have been kept in Japan
- 11,000+ fatalities
- Economic loss: $100 - $300 bn
- Insured losses up to $35 bn
- Significant tsunami damage was recorded in Japan; relatively minor damage on the U.S. West Coast

Source: US Geological Service; Insurance Information Institute.

Insured Japan Earthquake Loss Estimates*

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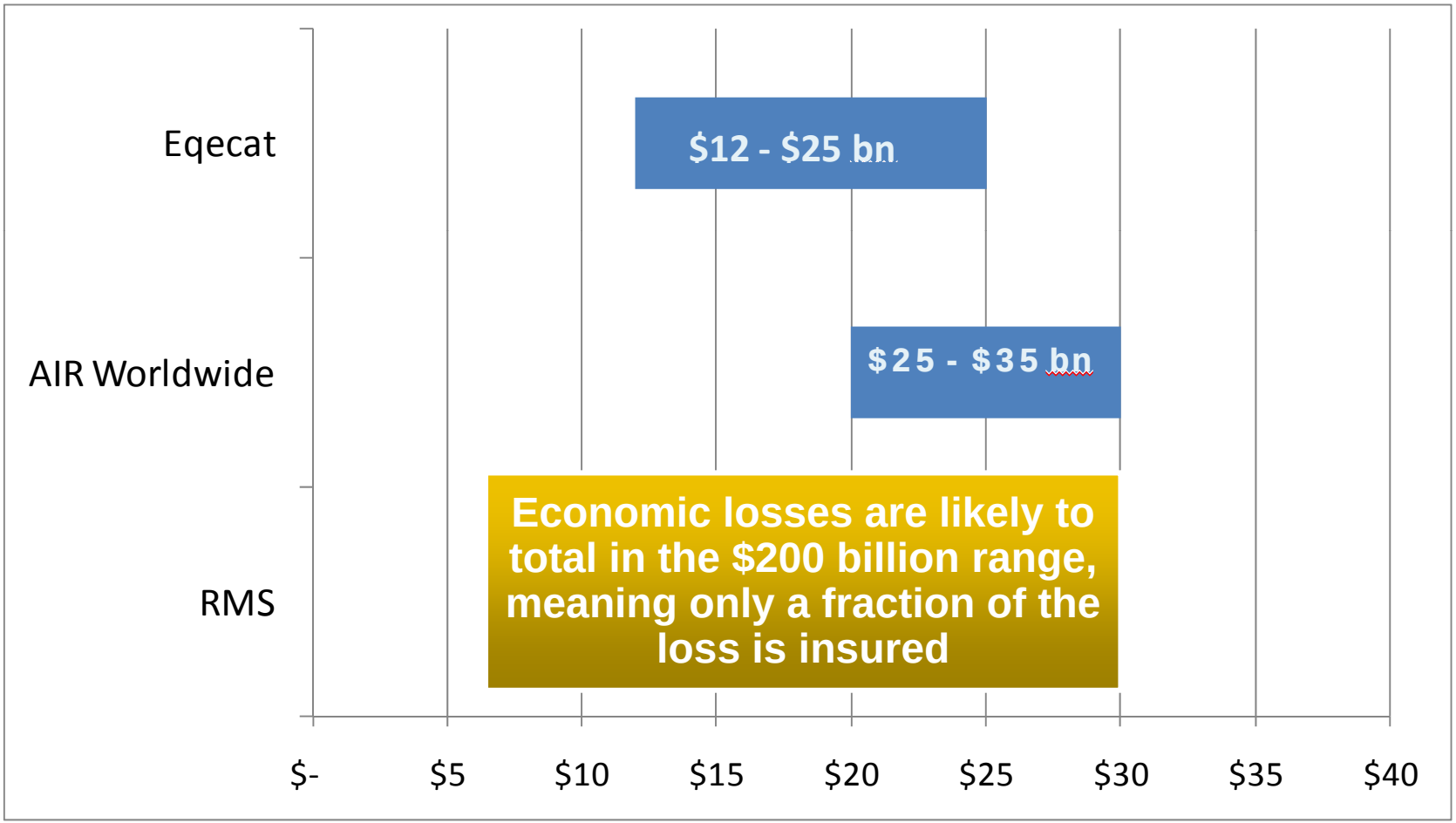
(Insured Losses, $ Billions)



*As of March 29, 2011. Figures do not include insured tsunami losses.
Sources: AIR Worldwide, Eqecat; Insurance Information Institute.

Top 20 Nonlife Insurance Companies in Japan by DPW, 2008

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Rank	Companies	Direct premiums written, 2008		Market share	Cumulative Market Share
		JPY (millions)	U.S. ($ millions)		
1	Tokio & Marine Nichido	$2,032,131.2	$19,660.9	24.0%	24.0%
2	Sompo Japan	1,504,262.7	14,553.8	17.8	41.8%
3	Mitsui Sumitomo	1,455,161.8	14,078.7	17.2	59.0%
4	Aioi	897,182.6	8,680.3	10.6	69.6%
5	Nipponkoa	728,262.9	7,046.0	8.6	78.2%
6	Nisay Dowa	361,530.7	3,497.8	4.3	82.5%
7	Fuji	329,345.7	3,186.4	3.9	86.4%
8	AIU	253,522.8	2,452.8	3.0	89.4%
9	Kyoei	199,393.1	1,929.1	2.4	91.8%
10	Nisshin	149,735.8	1,448.7	1.8	93.6%
11	American Home	82,889.8	802.0	1.0	94.6%
12	Asahi	73,600.1	712.1	0.9	95.5%
13	Sony	60,868.3	588.9	0.7	96.2%
14	ACE	54,876.2	530.9	0.7	96.9%
15	Zurich	45,471.3	439.9	0.5	97.4%
16	SECOM	44,245.0	428.1	0.5	97.9%
17	Sumi Sei	33,594.0	325.0	0.4	98.3%
18	AXA	30,418.9	294.3	0.4	98.7%
19	Mitsui Direct	29,471.9	285.1	0.4	99.1%
20	Daido	15,690.4	151.8	0.2	99.3%

Source: © AXCO 2011.

Recent Major Catastrophe Losses

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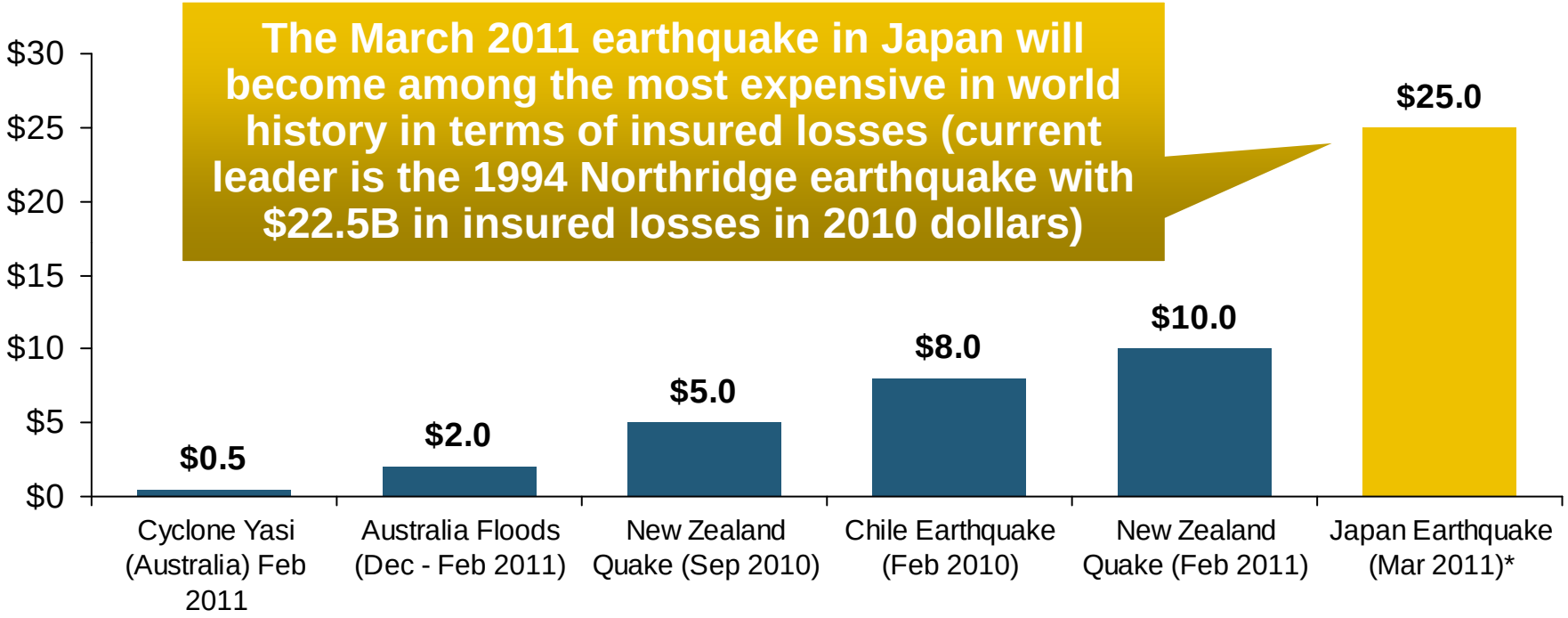
(Insured Losses, $US Billions)



Insured Losses from Recent Major Catastrophe Events Exceed $50 Billion, an Estimated $48 Billion of that from Earthquakes

*Midpoint of AIR Worldwide estimated insured loss range of $15 billion to $35 billion as of March 13, 2011. Does not include tsunami losses.

Sources: Insurance Council of Australia, Munich Re, AIR Worldwide; Insurance Information Institute.

Nonlife Insurance Market Impacts of Japan Earthquake

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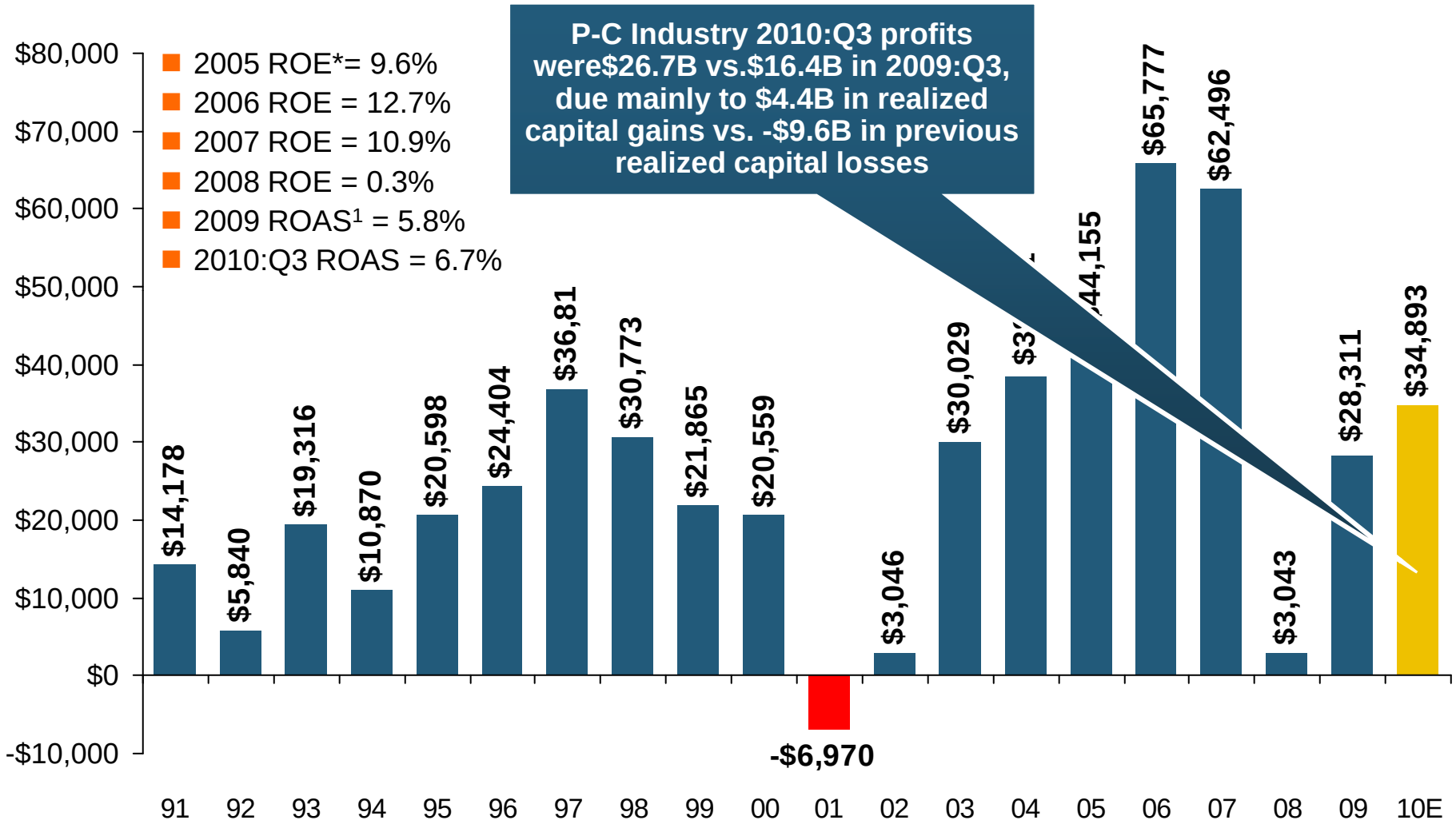
- **Primary Insurance: Downgrades of Some Domestic Japanese Insurers**
- **Significant Absorption of Loss by Japanese Government**
  - Residential earthquake damage
  - Nuclear-related property and liability damage
- **Market Share of Foreign Primary Insurers in Japan is Small**
  - Not a capital event for any non-Japanese primary insurer
- **Significant Impacts for Global Reinsurers**
  - Property-Catastrophe covers on Commercial Lines
  - Business Interruption
  - Contingent Business Interruption
- **Currently an Earnings Event for Global Reinsurers**
  - Not a capital event: Global reinsurance markets entered 2011 with record capital
- **Cost of Property/Catastrophe Reinsurance Rising in Japan, New Zealand, Australia**
  - Up for all; Magnitude of increase is sensitive to size of loss
- **Reinsurance Coverage Remains Available in Affected Regions**
- **Little (If Any) Impact of Cost of US Property-Cat Reinsurance**
  - Market remains well capitalized and competitive
  - Elevated global cat activity could halt price declines for property/cat reinsurance

P/C Insurance Industry Financial Overview

Profit Recovery Continues
Early Stage Growth Begins

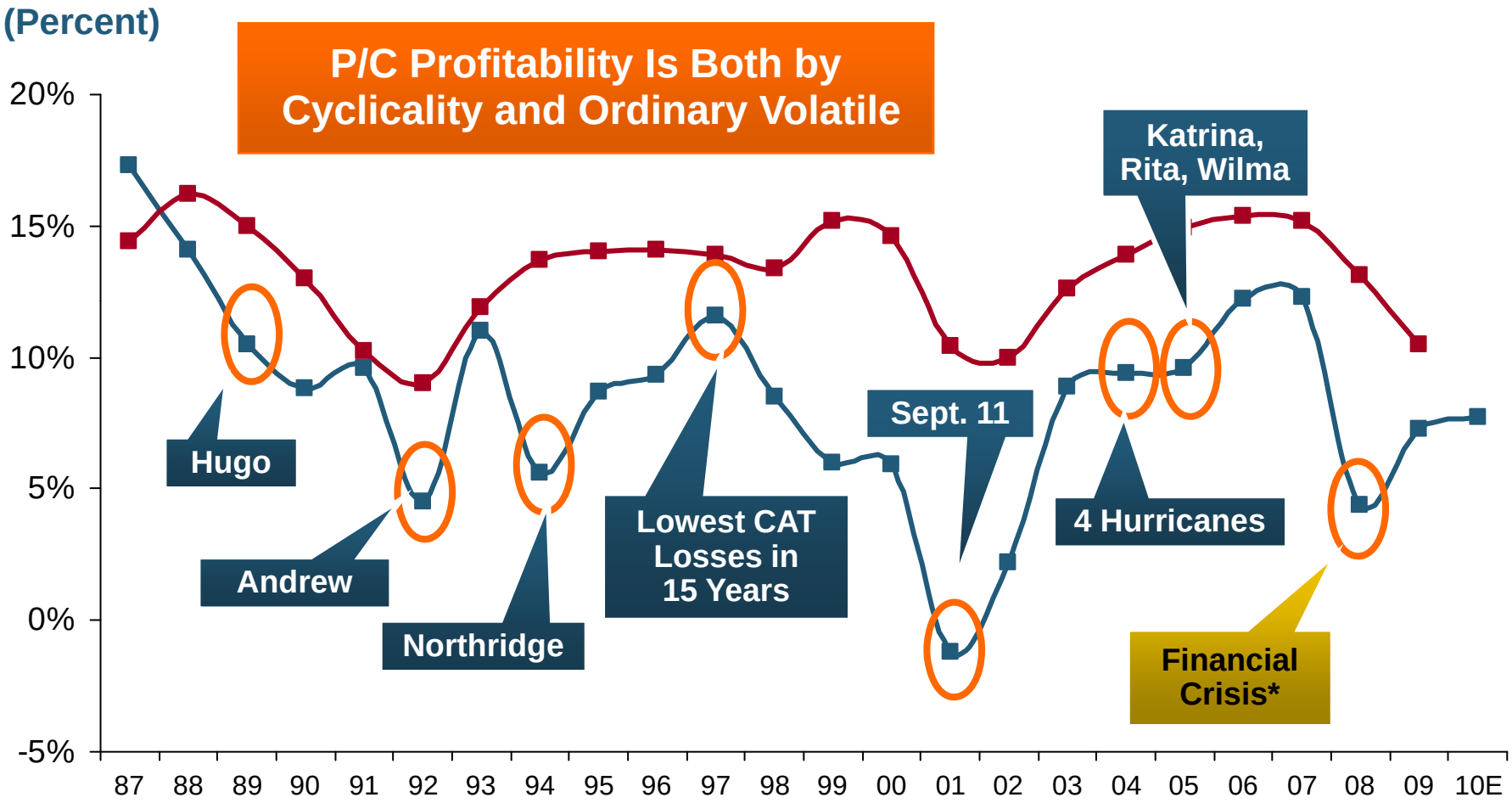
P/C Net Income After Taxes 1991–2010E ($ Millions)



* ROE figures are GAAP; [1]Return on avg. surplus. Excluding Mortgage & Financial Guaranty insurers yields a 7.7% ROAS for 2010:Q3 and 4.6% for 2009. 2009:Q3 net income was $29.8 billion excluding M&FG.

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

ROE: Property/Casualty Insurance, 1987–2010E*



* Excludes Mortgage & Financial Guarantee in 2008 - 2010.
Sources: ISO, *Fortune*; Insurance Information Institute figure for 2010 is actual through 2010:Q3.

ROE vs. Equity Cost of Capital: U.S. P/C Insurance:1991-2010:H1*

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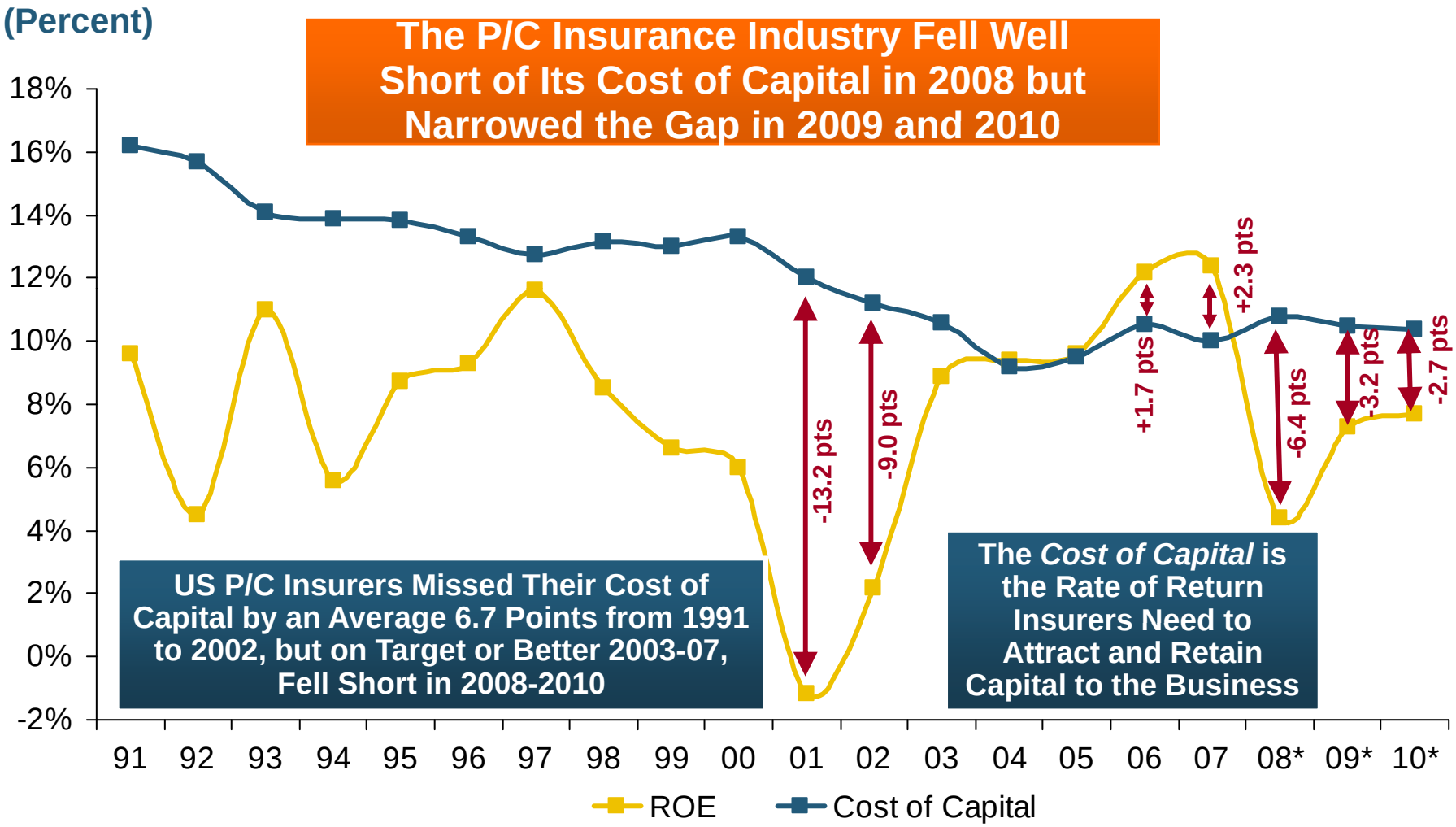

* Return on average surplus in 2008-2010 excluding mortgage and financial guaranty insurers.
Source: The Geneva Association, Insurance Information Institute

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

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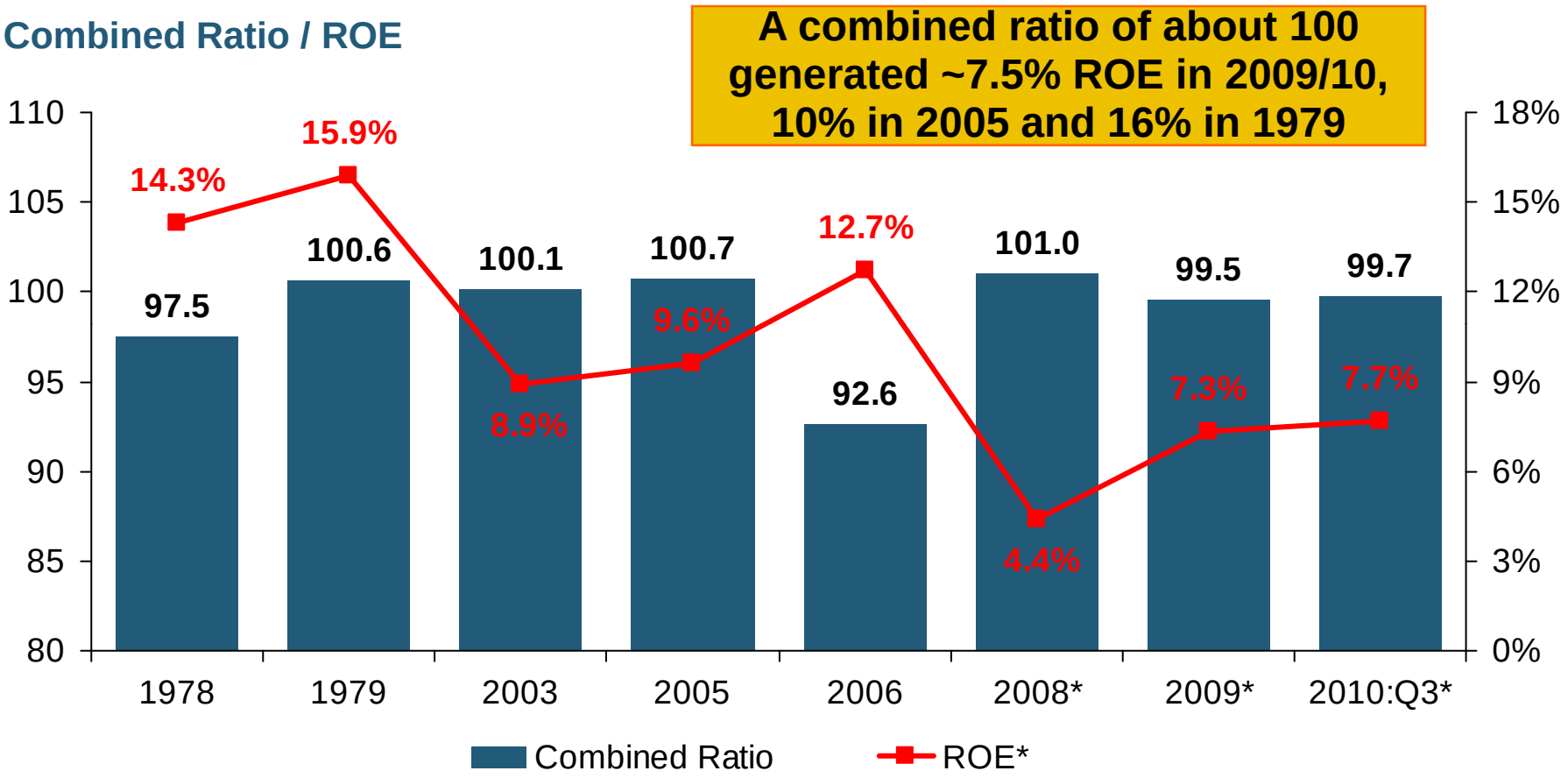

Combined Ratios Must Be Lower in Today's Depressed Investment Environment to Generate Risk Appropriate ROEs

* 2009 and 2010:Q3 figures are return on average statutory surplus. 2008, 2009 and 2010:H1figures exclude mortgage and financial guaranty insurers

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

RNW for Major P/C Lines, 2000-2009 Average

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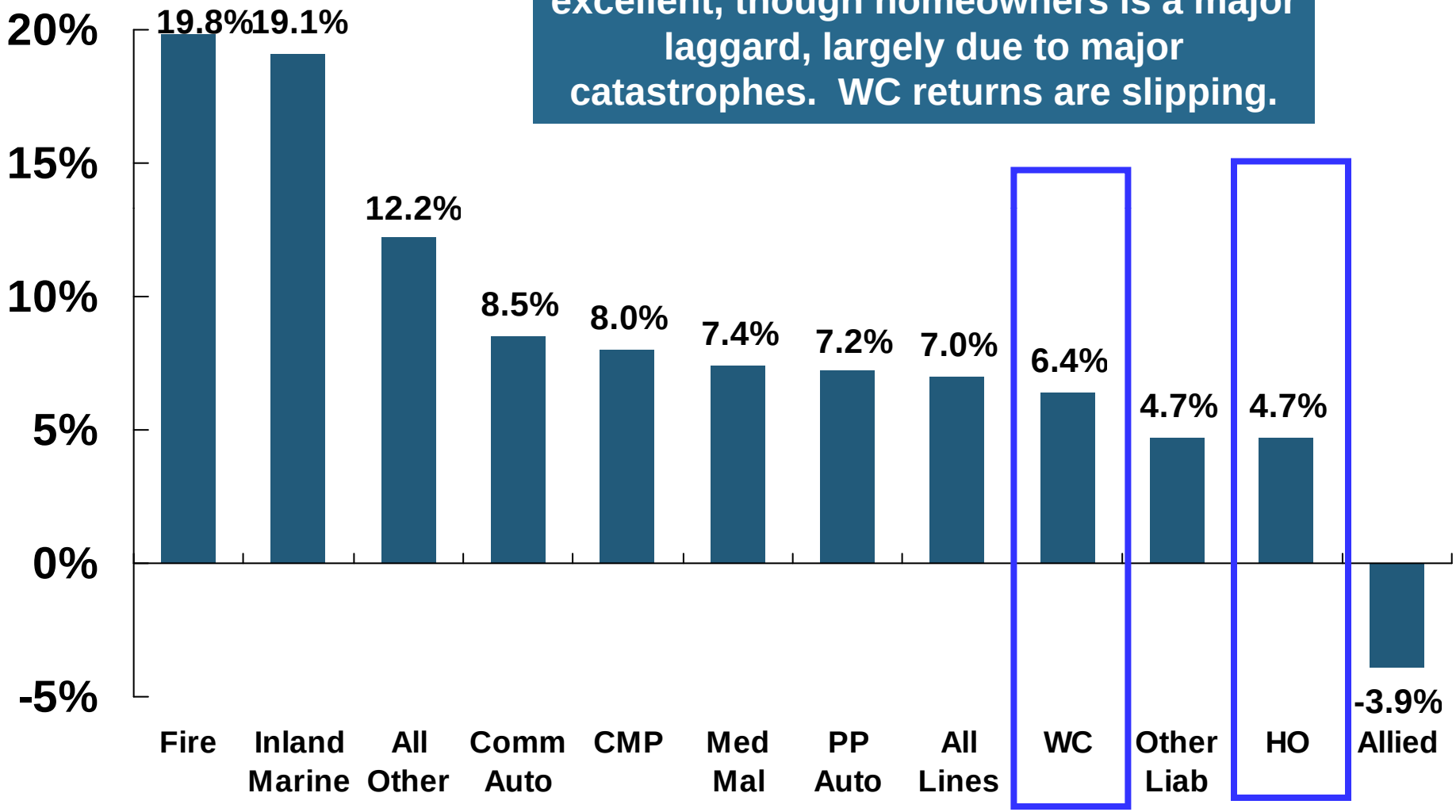
10-year returns for some lines are excellent, though homeowners is a major laggard, largely due to major catastrophes. WC returns are slipping.



Source: NAIC; Insurance Information Institute

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The Elusive Market Turn

When, Why, How and

IF

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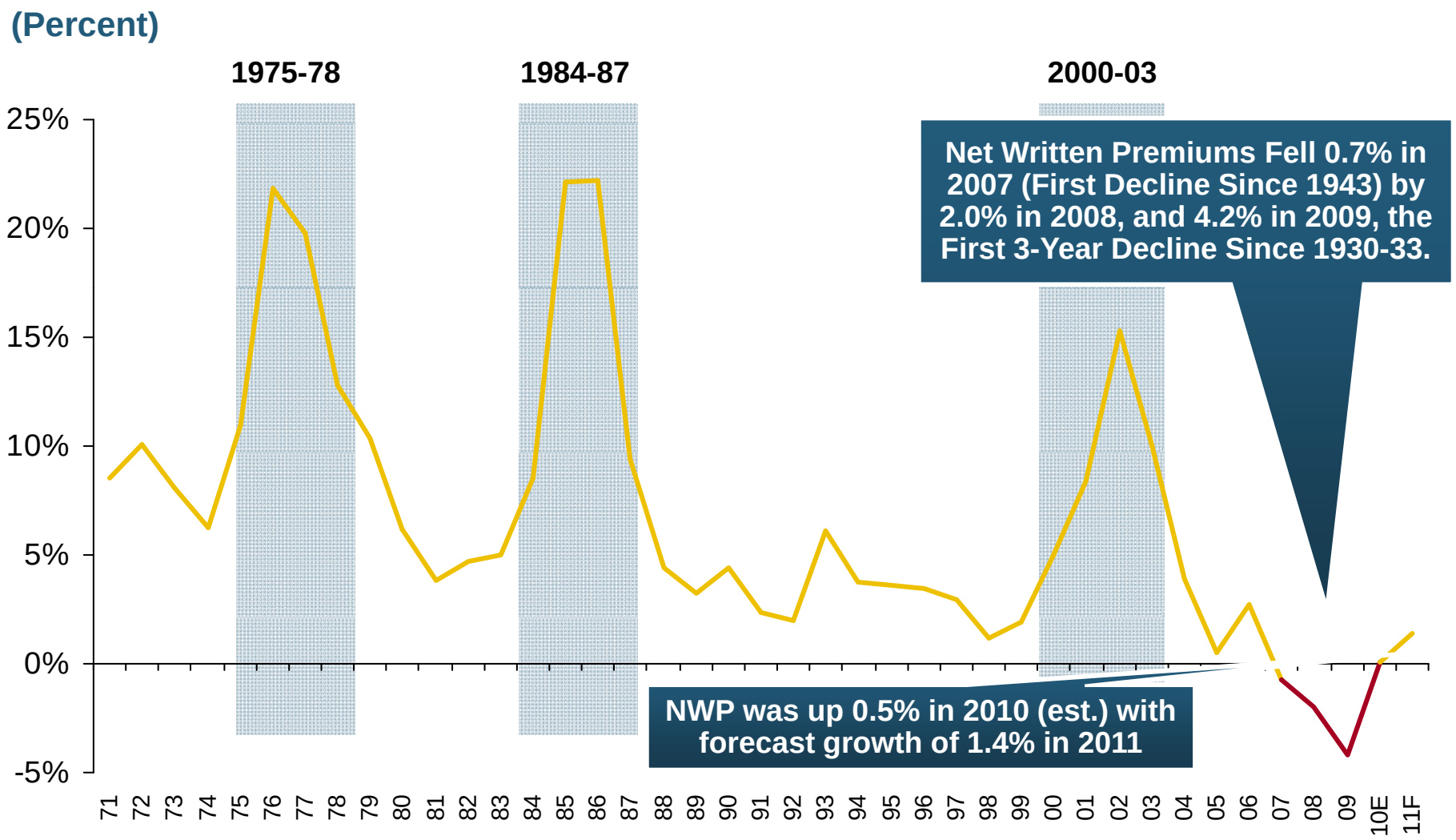
PREMIUM TRENDS

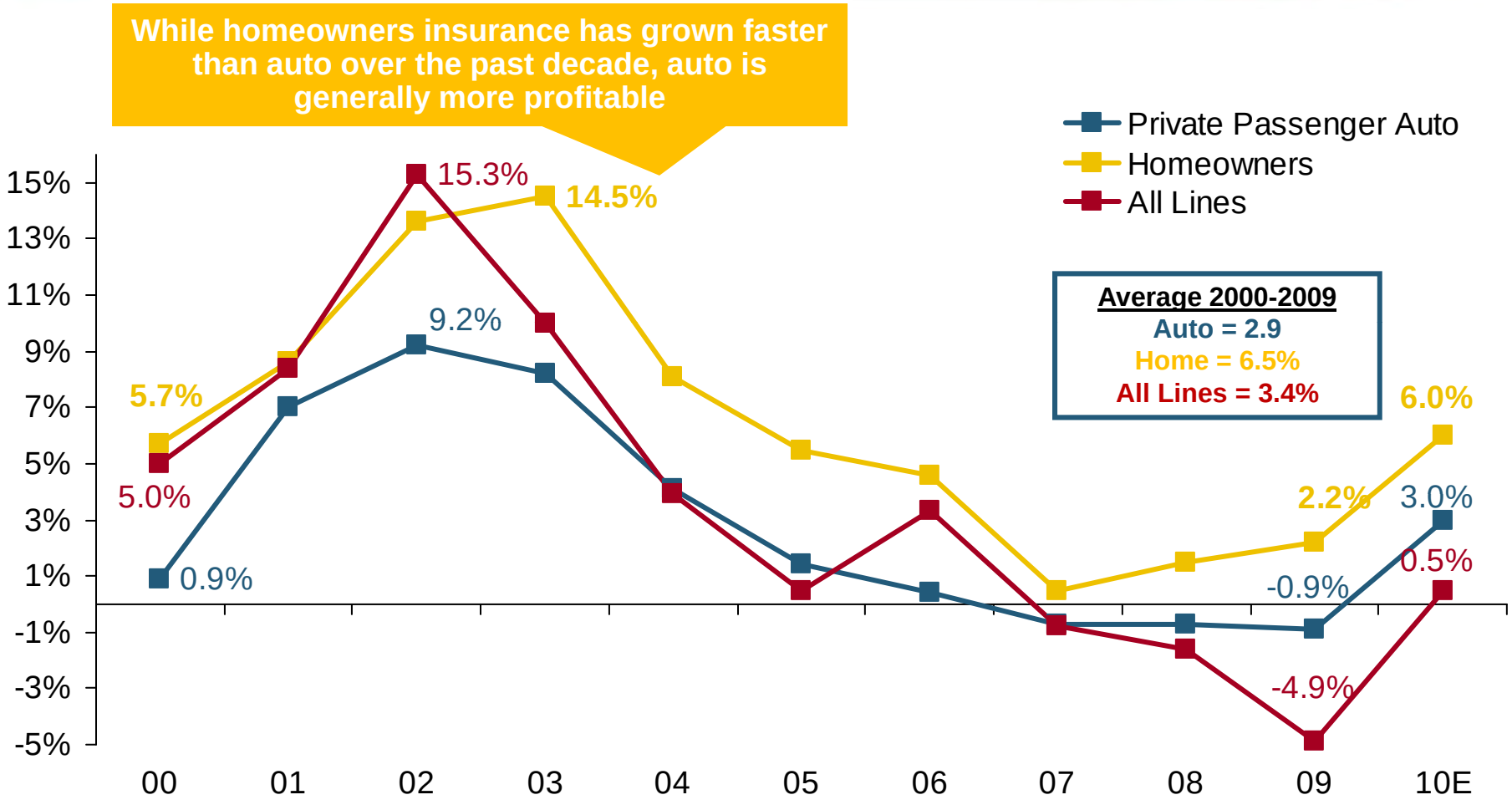
Winds of Change or Moving Sideways?

Soft Market Persisted in 2010 but May Be Easing: Relief in 2011?



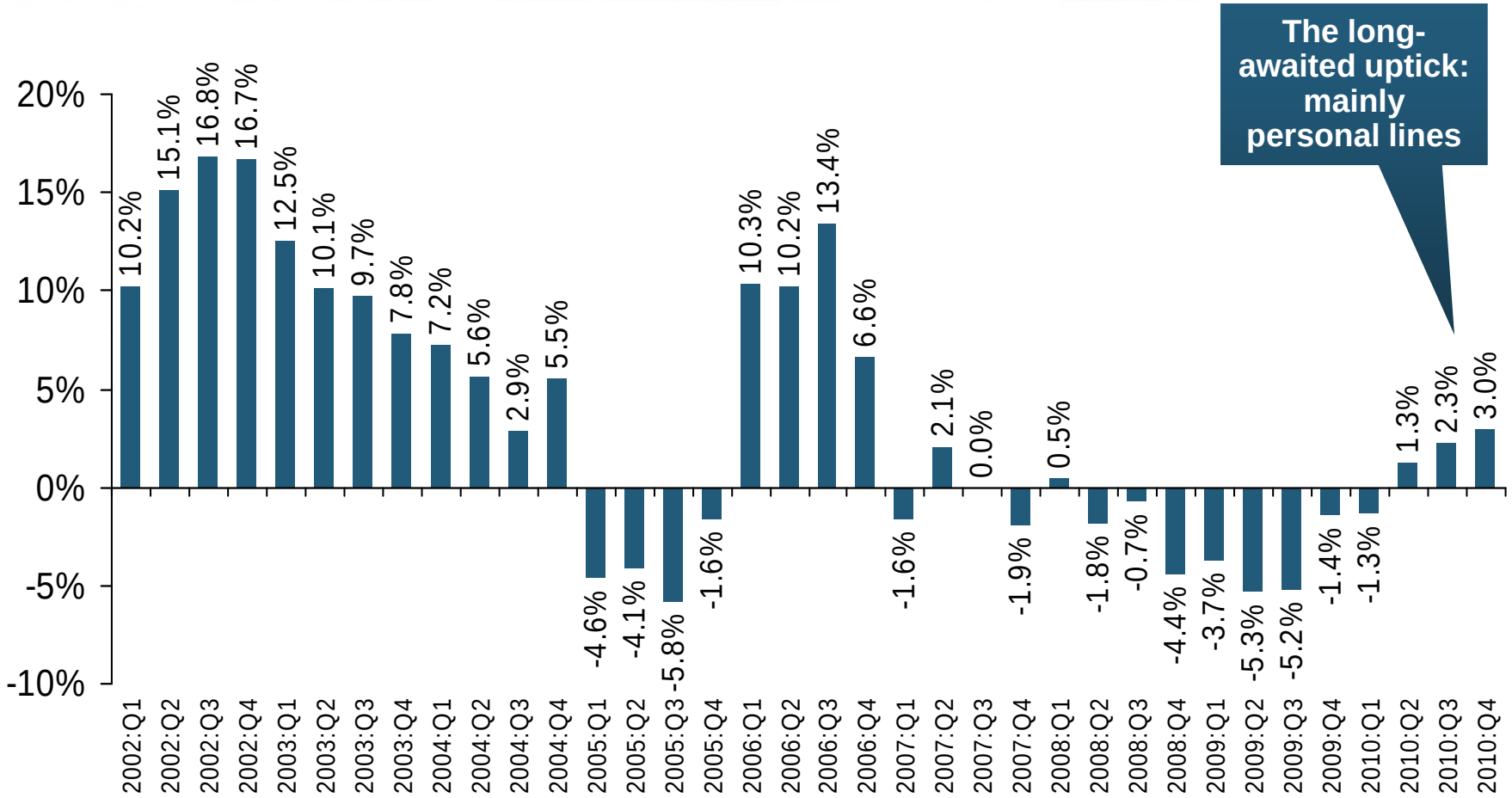
Shaded areas denote "hard market" periods
Sources: A.M. Best (historical and forecast), ISO, Insurance Information Institute.

Auto & Home vs. All Lines, Net Written Premium Growth, 2000–2010E



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

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

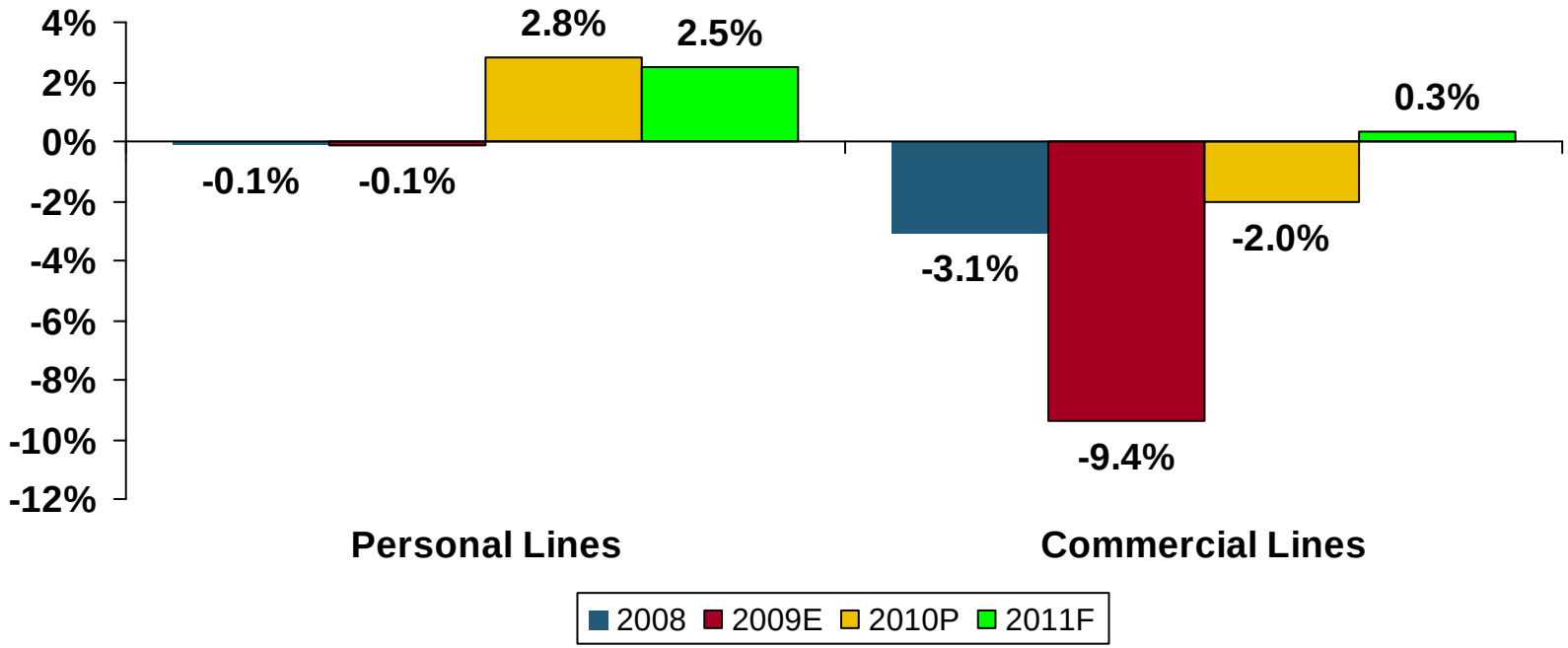


Finally! Back-to-back quarters of net written premium growth (vs. the same quarter, prior year)

Sources: ISO, Insurance Information Institute.

Net Written Premium Growth by Segment: 2008-2011F

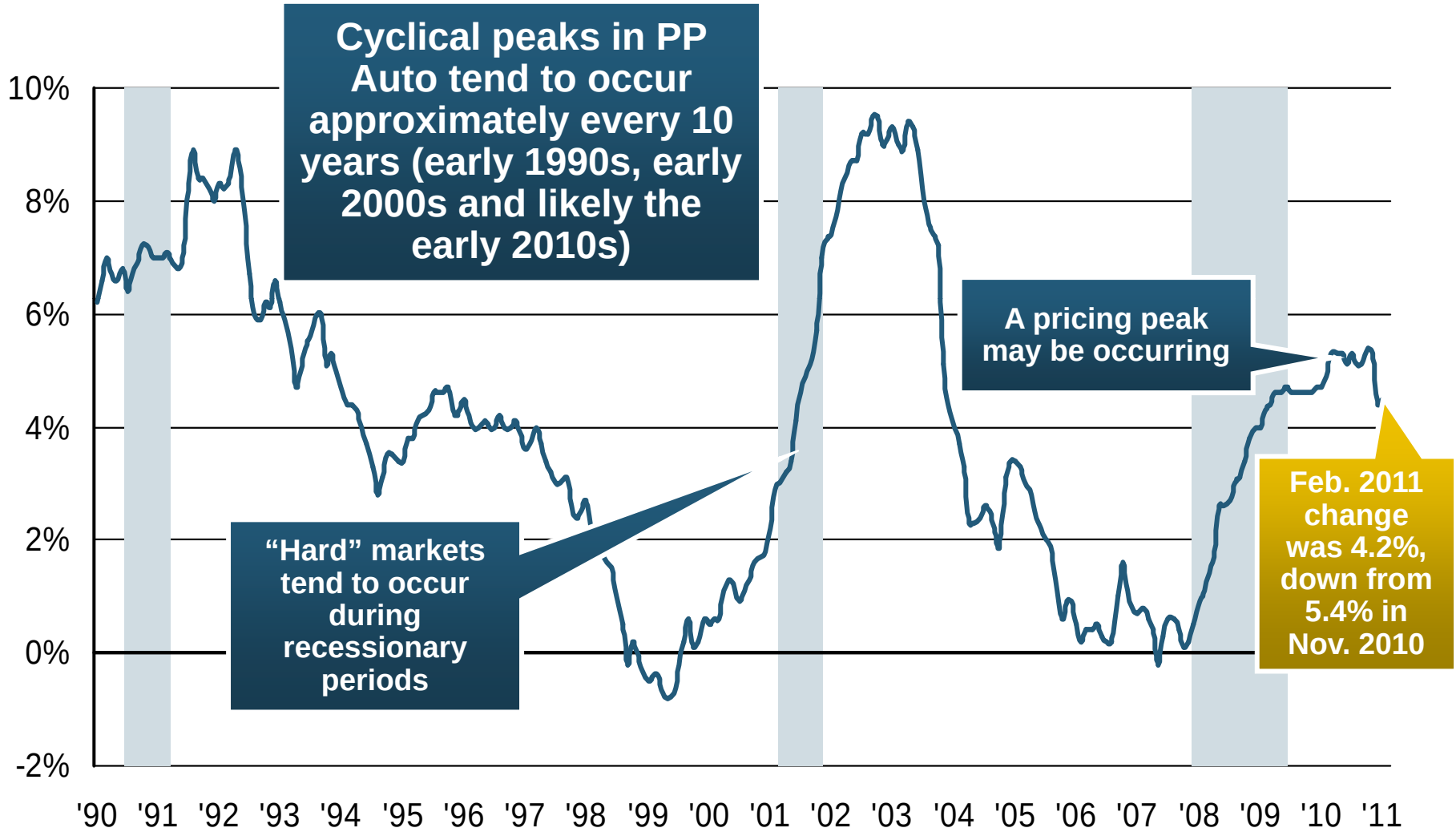
Personal lines growth resumed in 2010 and will continue in 2011, while commercial lines contracted again in 2010 and but will stabilize in 2011



Rate and exposure are more favorable in personal lines, whereas a prolonged soft market and sluggish recovery from the recession weigh on commercial lines.

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

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

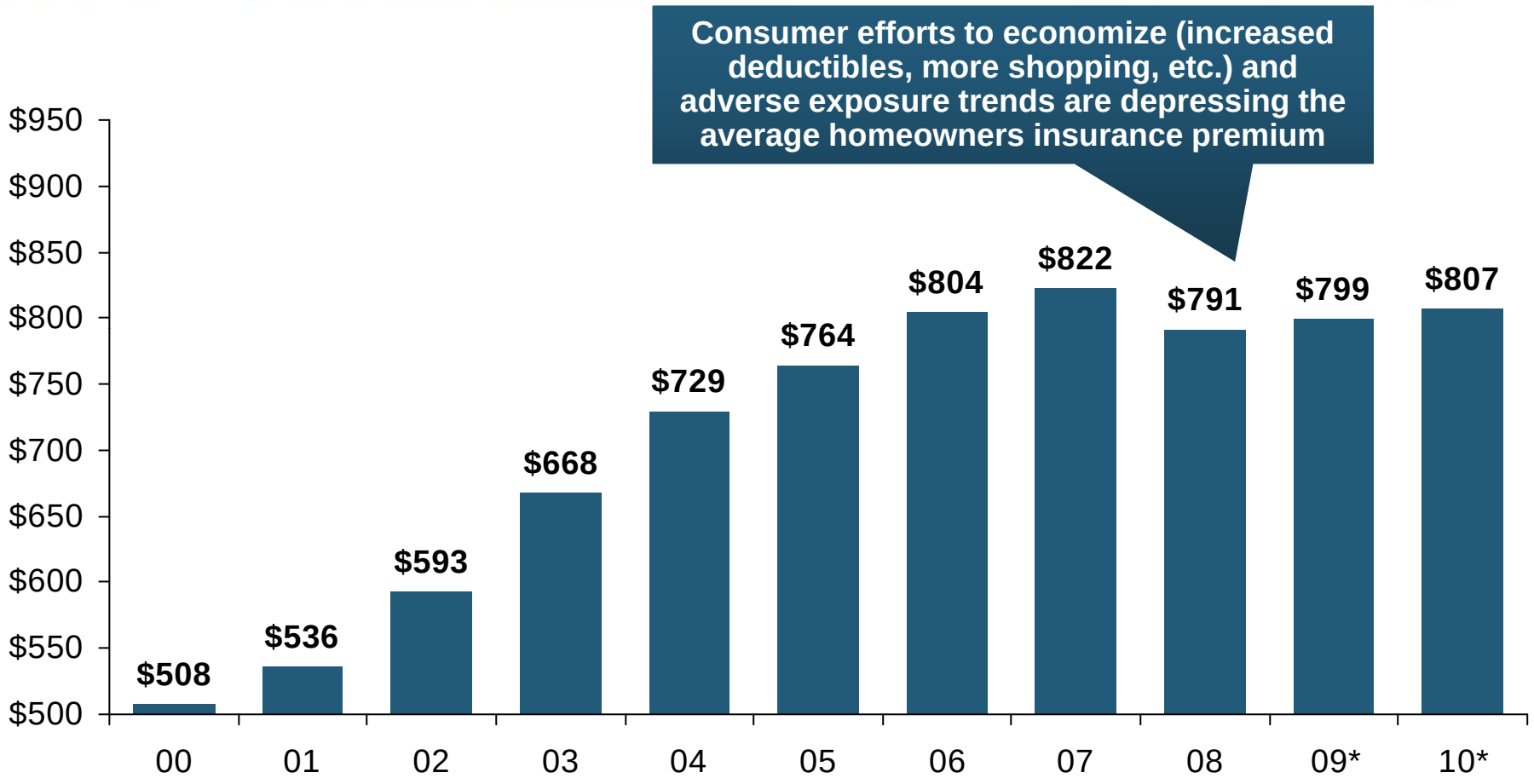


*Percentage change from same month in prior year; through February 2011; seasonally adjusted

Note: Recessions indicated by gray shaded columns.

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

Average Premium for Home Insurance Policies**



* Insurance Information Institute Estimates/Forecasts **Excludes state-run insurers.
Source: NAIC, Insurance Information Institute estimates 2009-2010 based on CPI and other data.

Average Commercial Rate Change, All Lines, (1Q:2004–3Q:2010)

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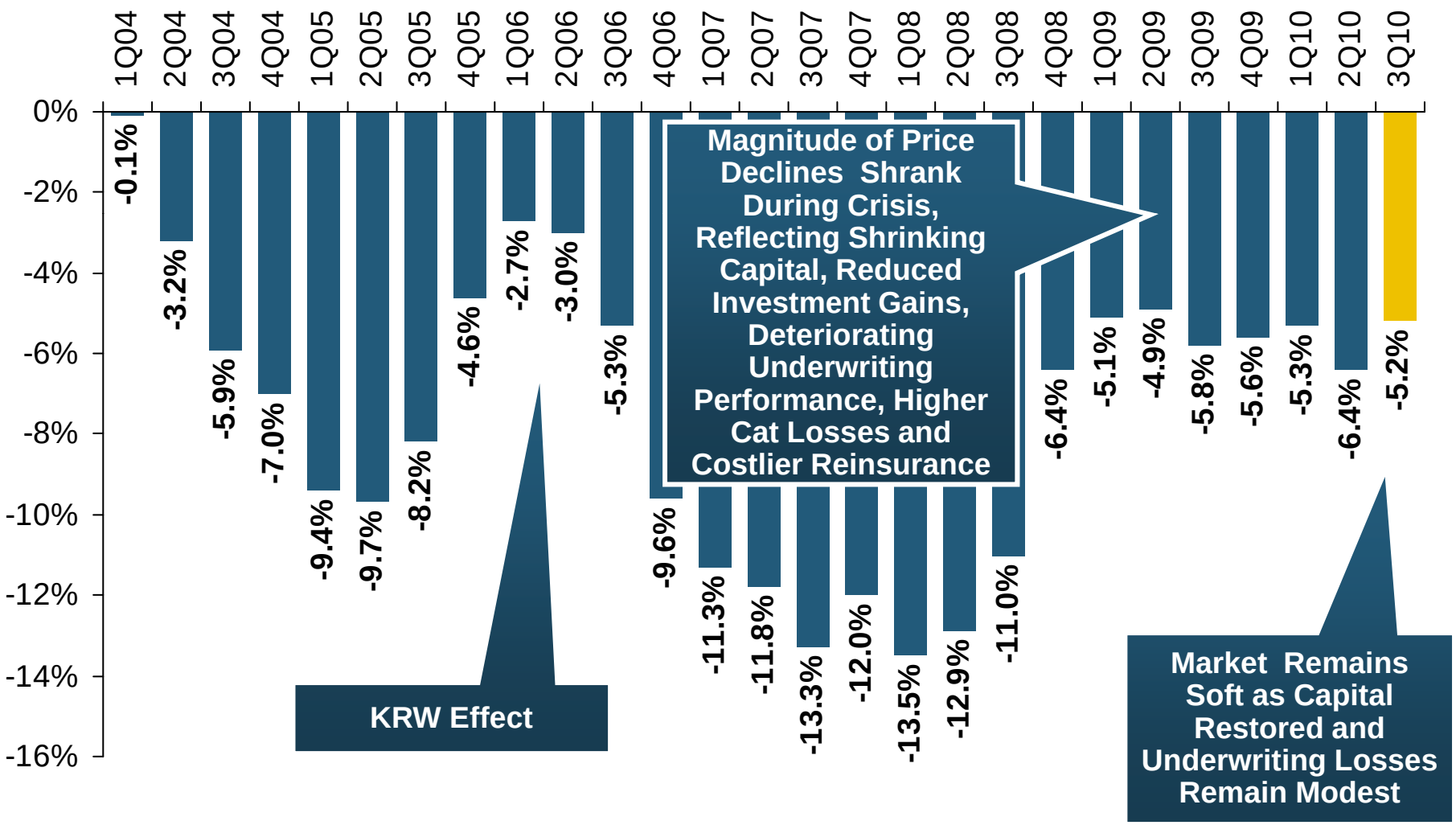
(Percent)



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

Change in Commercial Rate Renewals, by Account Size: 1999:Q4 to 2010:Q3

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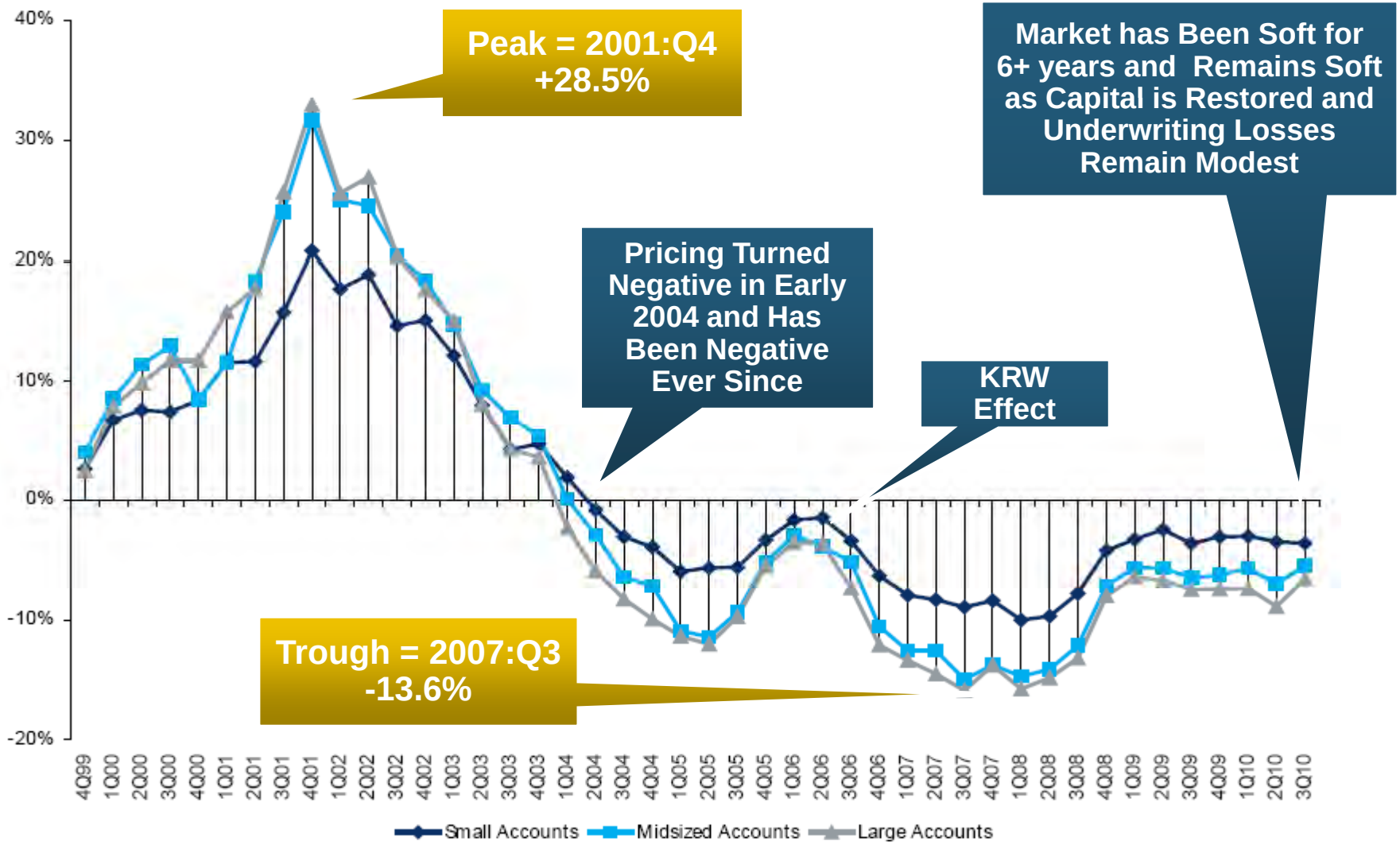
Percentage Change (%)



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

Cumulative Qtrly. Commercial Rate Changes, by Account Size: 1999:Q4 to 2010:Q3

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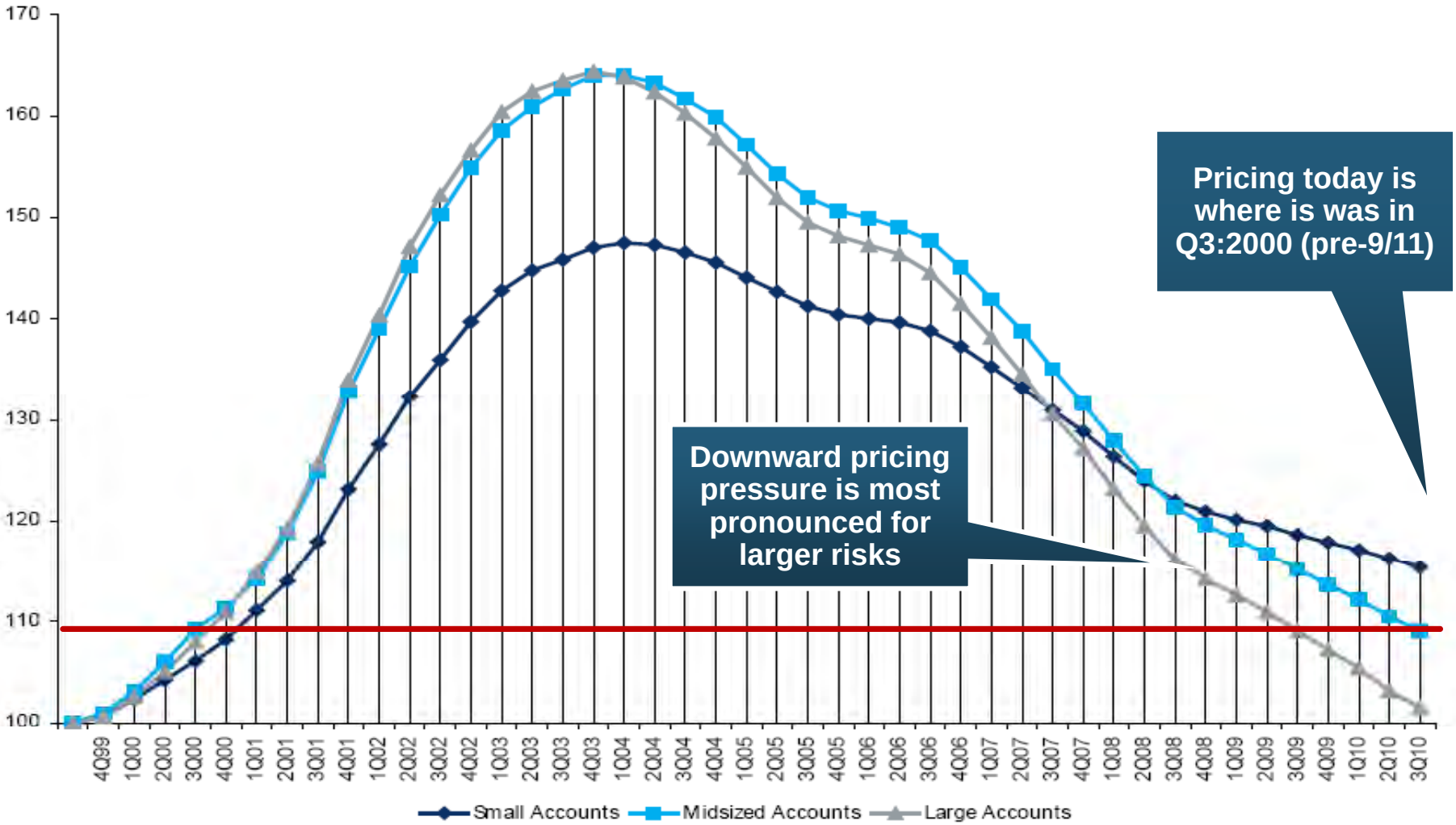
1999:Q4 = 100



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

Change in Commercial Rate Renewals, by Line: 2010:Q3

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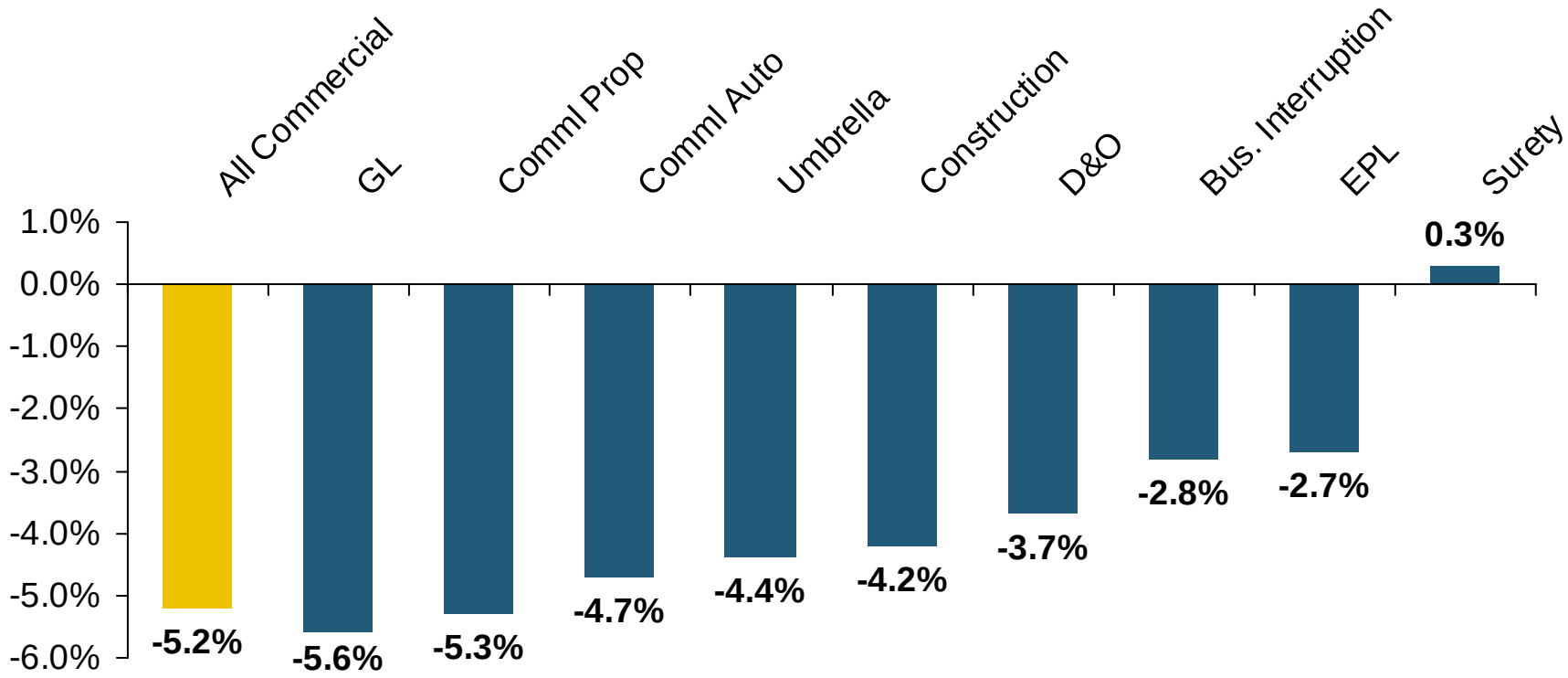
Percentage Change (%)



Most Major Commercial Lines Renewed Down in Q3:2010 at a Pace Similar to that of a Year Earlier

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

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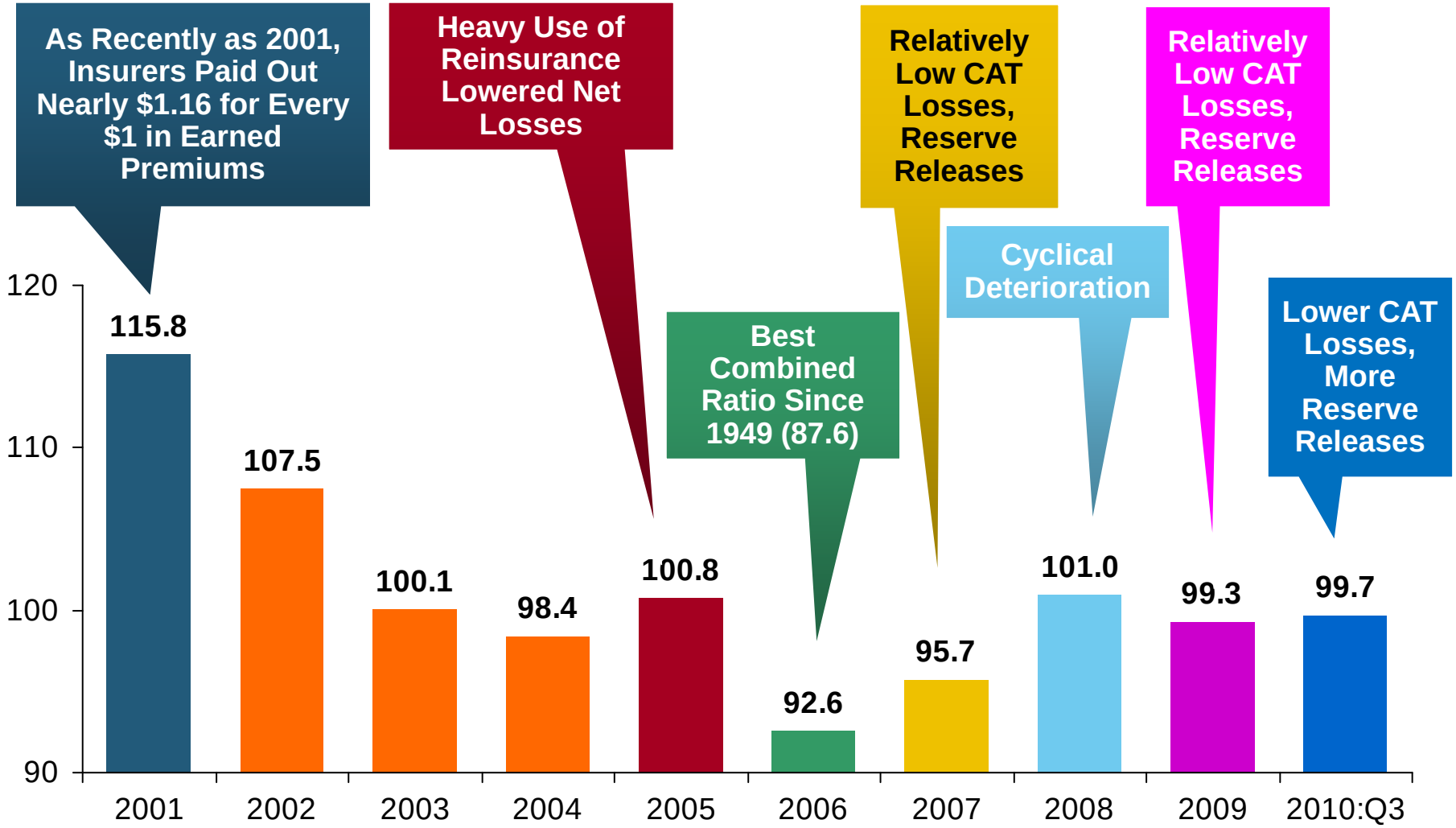
UNDERWRITING

Cyclicality is Driven Primarily by the Industry's Underwriting Cycle, Not the Economy

P/C Insurance Industry Combined Ratio, 2001–2010:Q3*

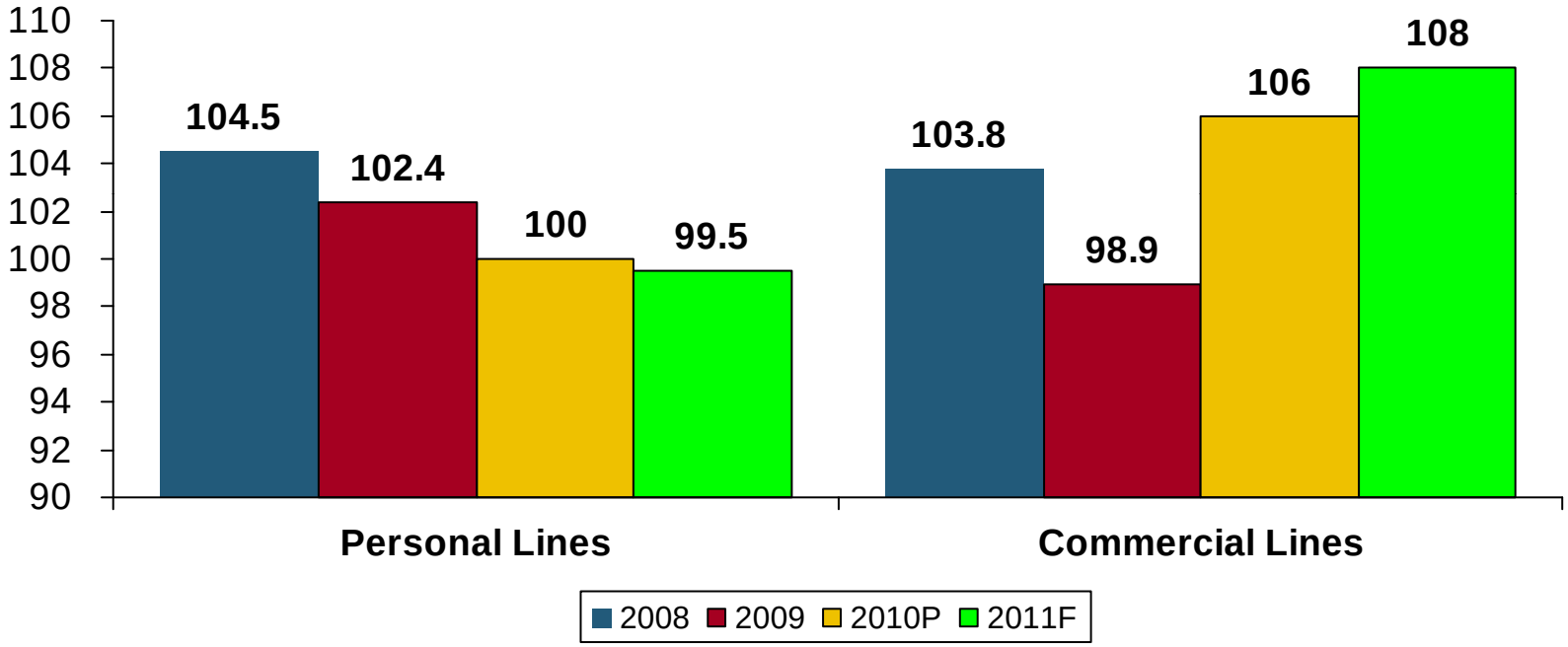


* Excludes Mortgage & Financial Guaranty insurers in 2008, 2009 and 2010. Including M&FG, 2008=105.1, 2009=100.7, 2010:Q3=101.2

Sources: A.M. Best, ISO.

Calendar Year Combined Ratios by Segment: 2008-2011F

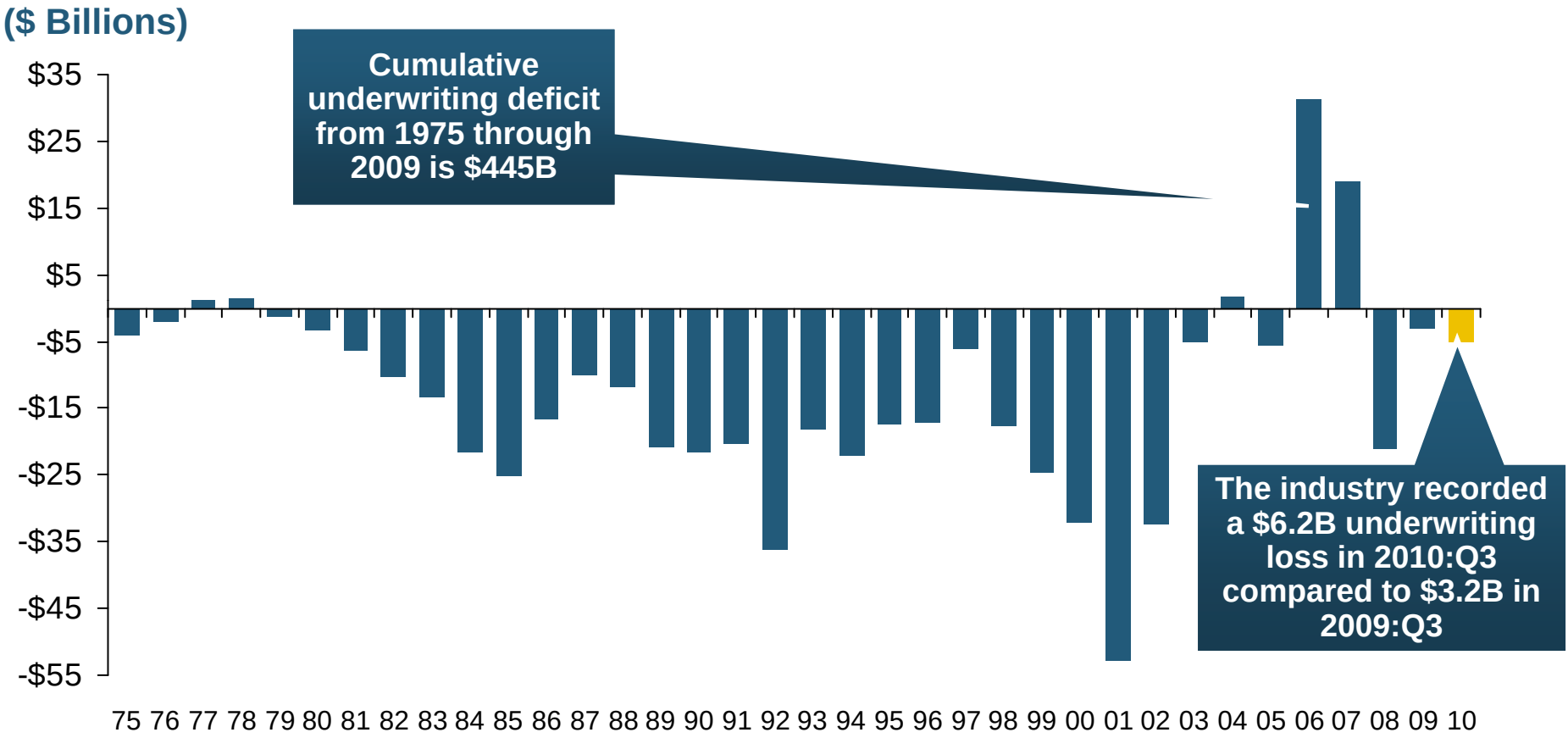
Personal lines combined ratio is expected to remain stable in 2010 while commercial lines and reinsurance deteriorate



Overall deterioration in 2011 underwriting performance is due to expected return to normal catastrophe activity along with deteriorating underwriting performance related to the prolonged commercial soft market

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

Underwriting Gain (Loss) 1975–2010:Q3*



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

* Includes mortgage and financial guaranty insurers.

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

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

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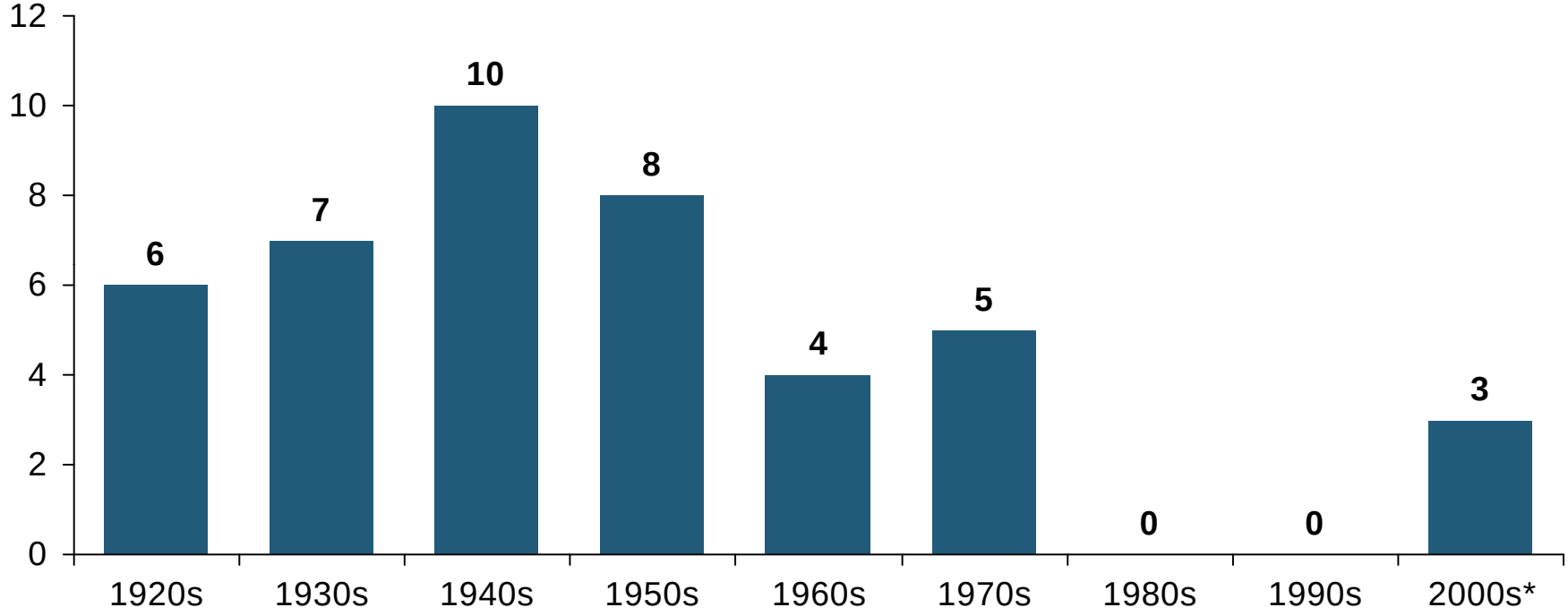
Number of Years with Underwriting Profits



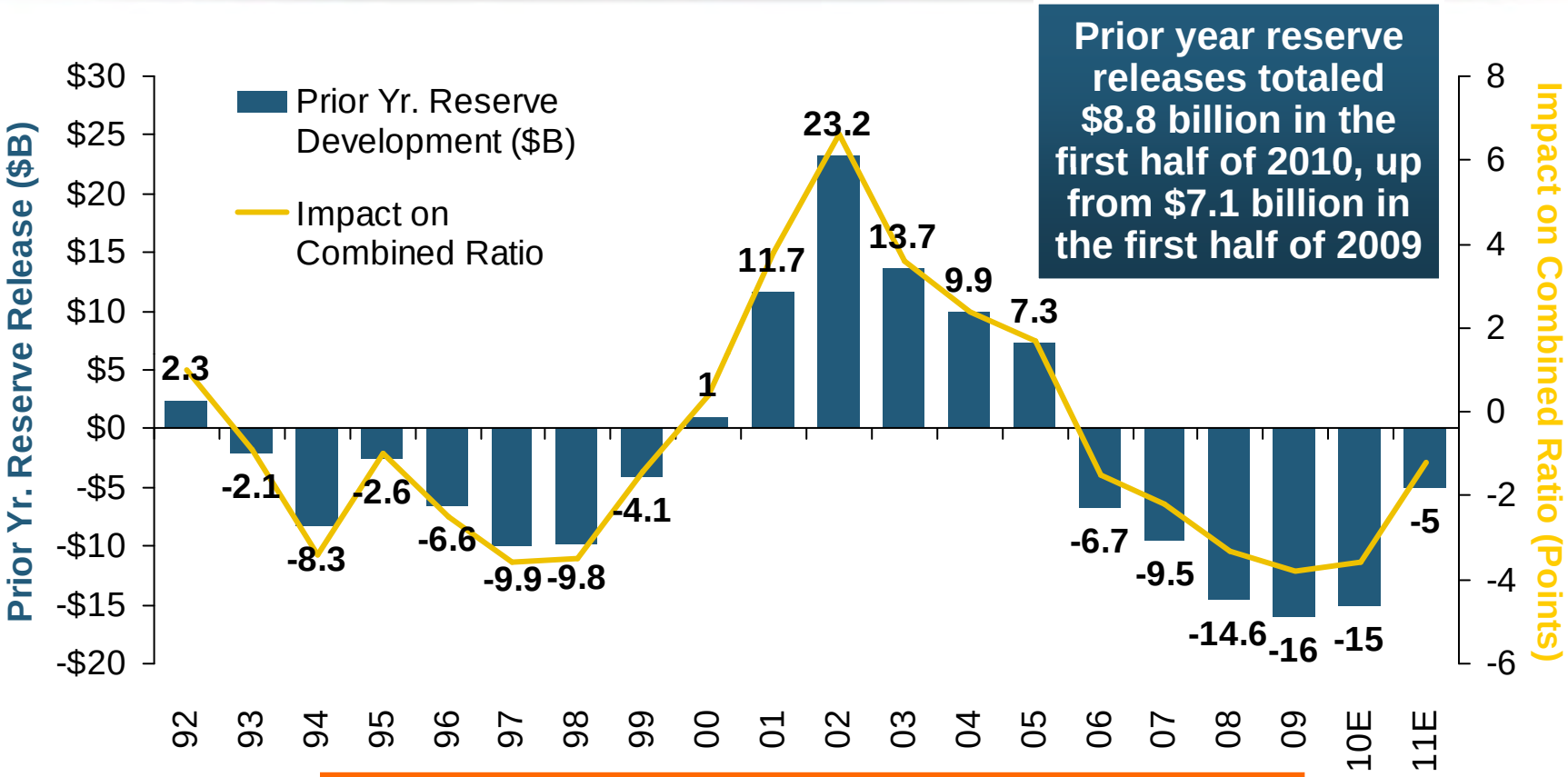
Underwriting Profits Were Common Before the 1980s (40 of the 60 Years Before 1980 Had Combined Ratios Below 100) – But Then They Vanished. Not a Single Underwriting Profit Was Recorded in the 25 Years from 1979 Through 2003

* 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.

P/C Reserve Development, 1992–2011E

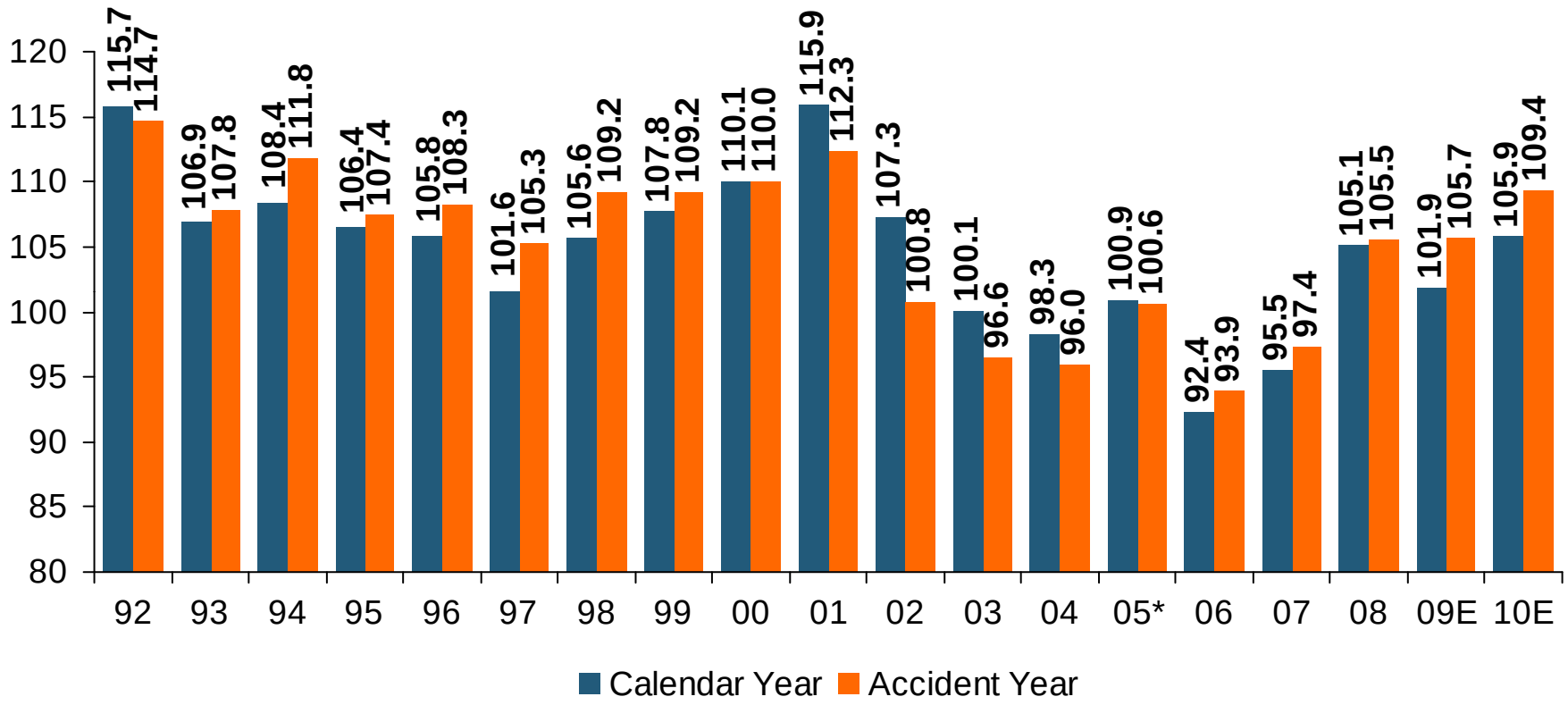


Reserve Releases Are Remained Strong in 2010 But Should Begin to Taper Off in 2011

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.

Calendar Year vs. Accident Year P/C Combined Ratio: 1992–2010E[1]

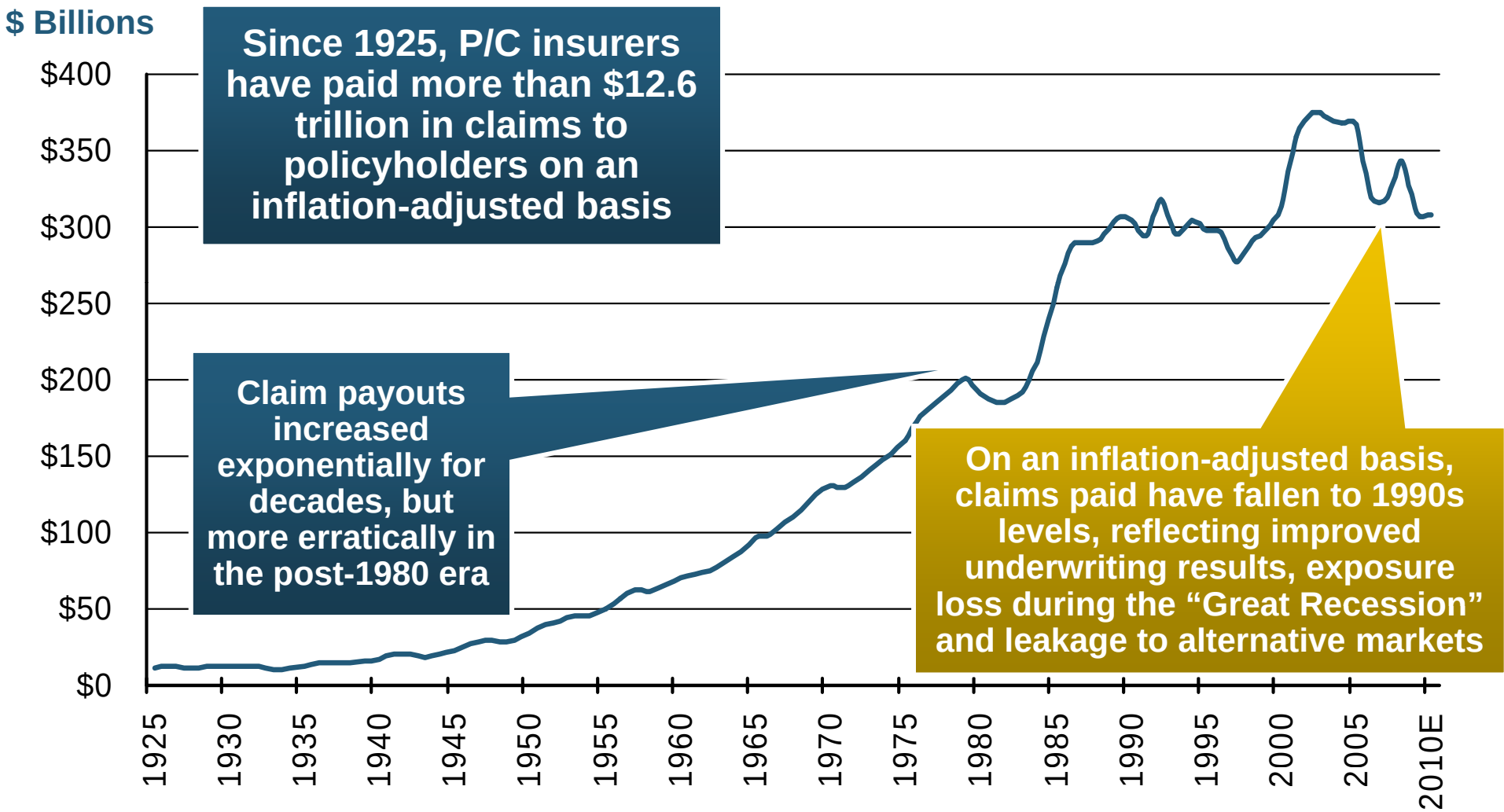


Accident Year Results Show a More Significant Deterioration in Underwriting Performance. Calendar Year Results Are Helped by Reserve Releases

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.

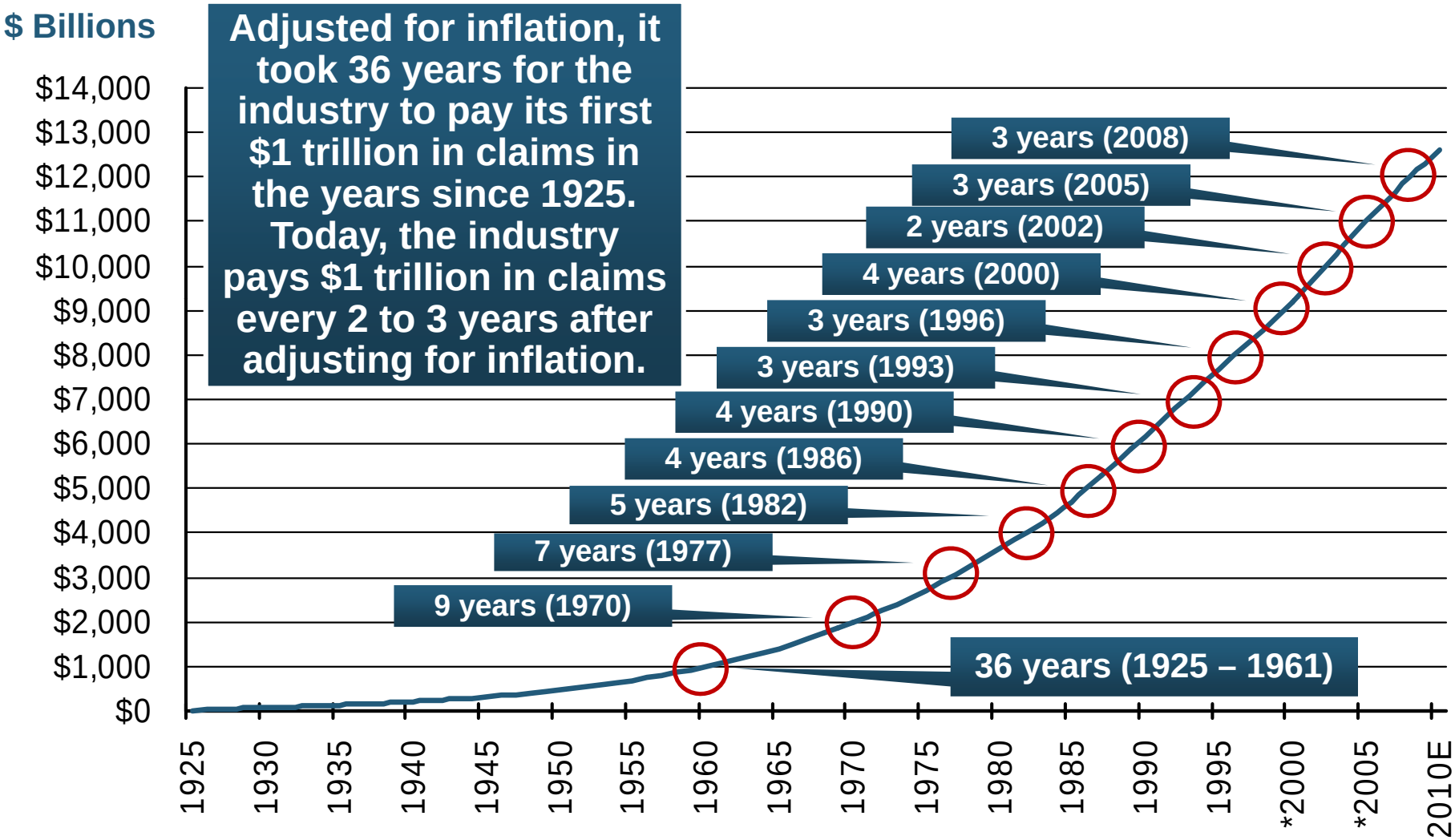
Sources: Barclay's Capital; A.M. Best.

Inflation-Adjusted Dollar Value of Claims Paid by P/C Insurers, 1925–2010E*



*1925 – 1934 stock companies only. Includes workers compensation state funds 1998-2006.
Sources: Insurance Information Institute research and calculations from A.M. Best data.

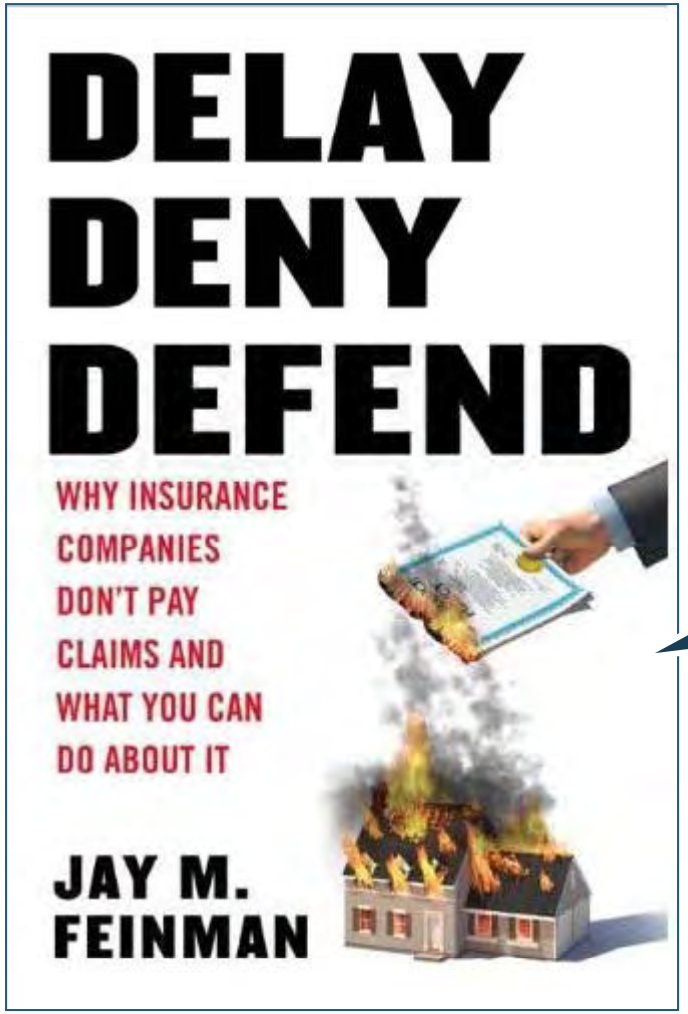
Cumulative Value of Inflation-Adjusted Claims Paid by P/C Insurers, 1925–2010E*



*1925 – 1934 stock companies only. Includes workers compensation state funds 1998-2006.

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

$12.5 Trillion of Paid Claims and Someone Still Writes a Book With This Title?



This book by a Rutgers University law professor asserts that insurers do everything possible to avoid paying legitimate claims.

I debated the thesis of Prof. Feinman's book and refuting his allegations in a debate in New Orleans on March 24.

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INVESTMENTS: THE NEW REALITY

Investment Performance is a Key Driver of Profitability

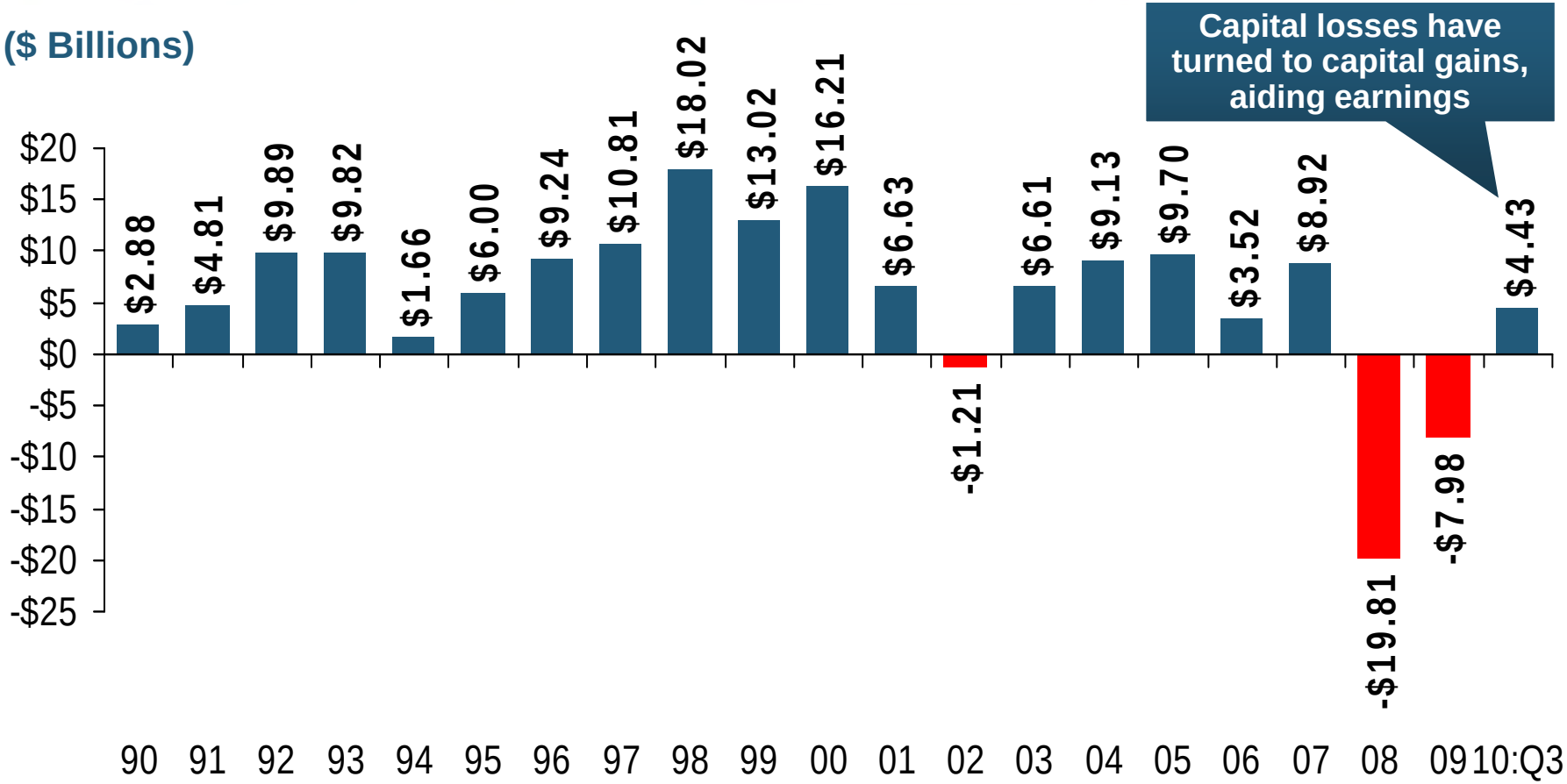
Does It Influence Underwriting or Cyclicality?

Property/Casualty Insurance Industry Investment Gain: 1994–2010:Q3[1]

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
Investment Gains Recovered Significantly in 2010

[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.

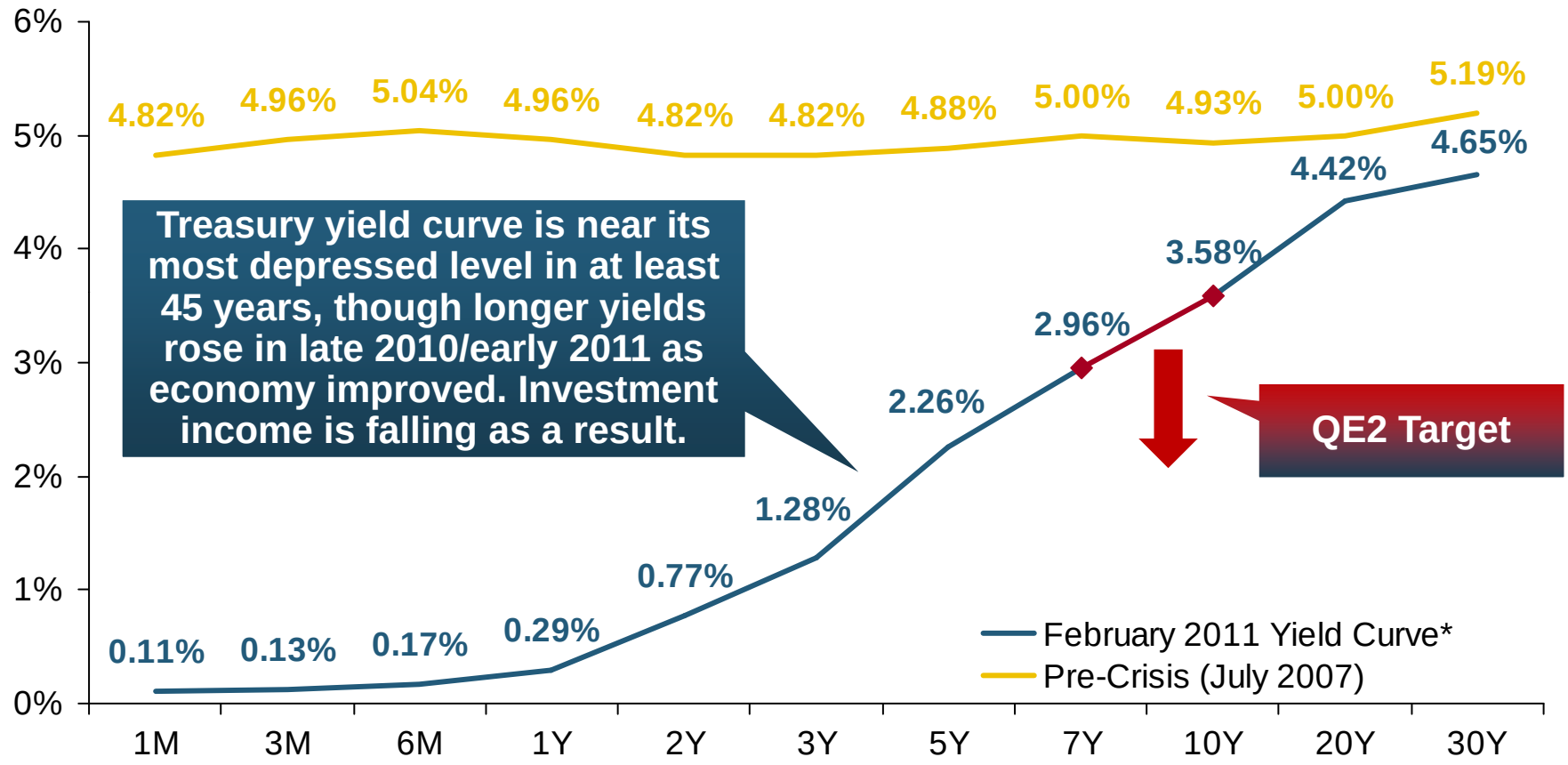
P/C Insurer Net Realized Capital Gains, 1990-2010:Q3



Realized Capital Losses Were the Primary Cause of 2008/2009's Large Drop in Profits and ROE and Were a Major Driver of Its Recovery in 2010

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

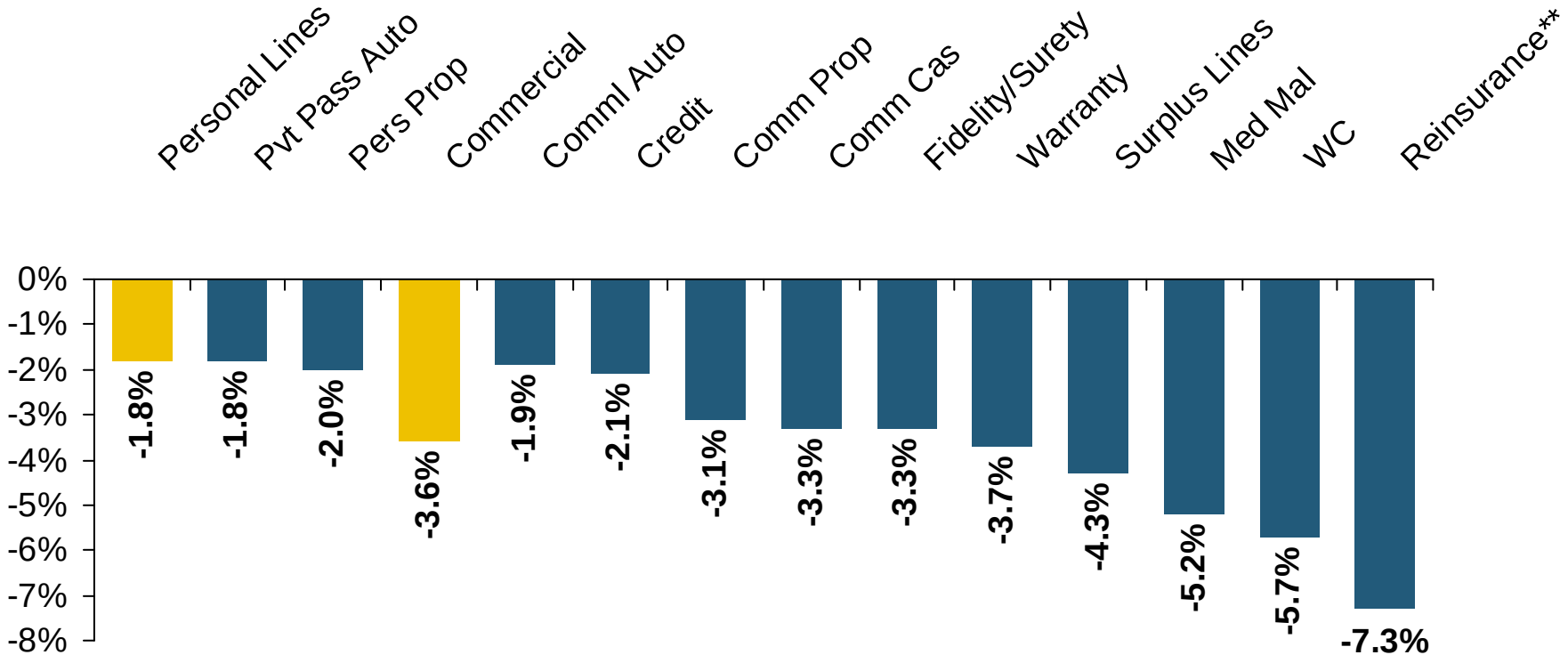
Treasury Yield Curves: Pre-Crisis (July 2007) vs. February 2011



The Fed's Announced Intention to Pursue Additional Quantitative Easing Could Depress Rates in the 7 to 10-Year Maturity Range through June

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.

Distribution of P/C Insurance Industry's Investment Portfolio

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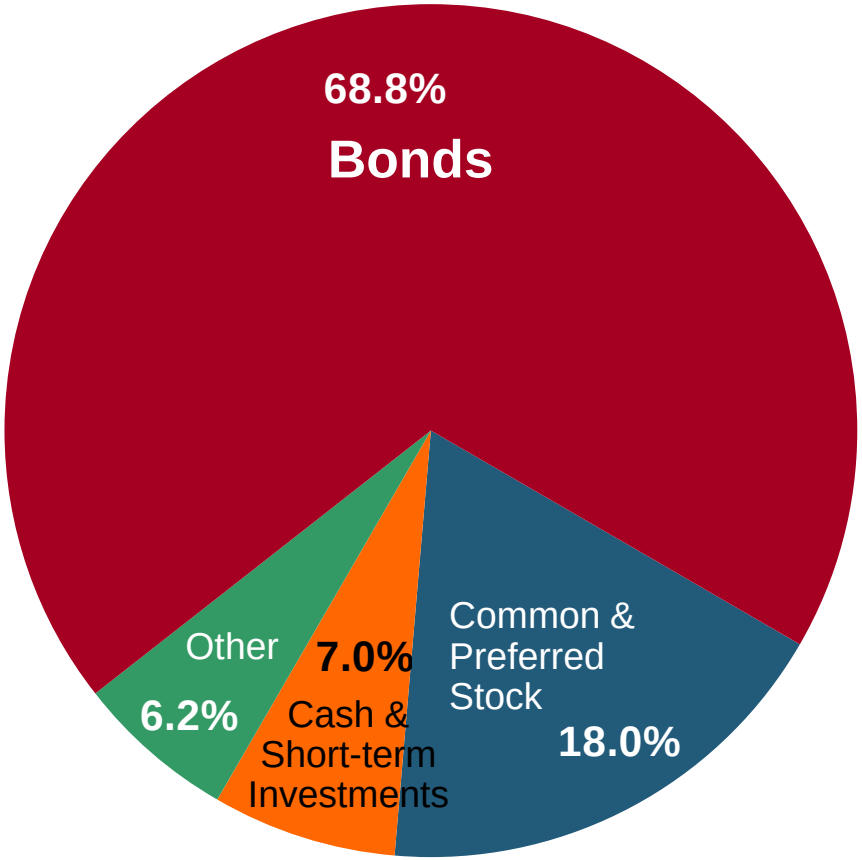
Portfolio Facts as of 12/31/2009

- Invested assets totaled $1.26 trillion
- Generally, insurers invest conservatively, with over 2/3 of invested assets in bonds
- Only 18% of invested assets were in common or preferred stock

As of December 31, 2009



*Net admitted assets.

Sources: NAIC; Insurance Information Institute research.

2011 Financial Overview

About Half of the P/C Insurance Industry's Bond Investments Are in Municipal Bonds

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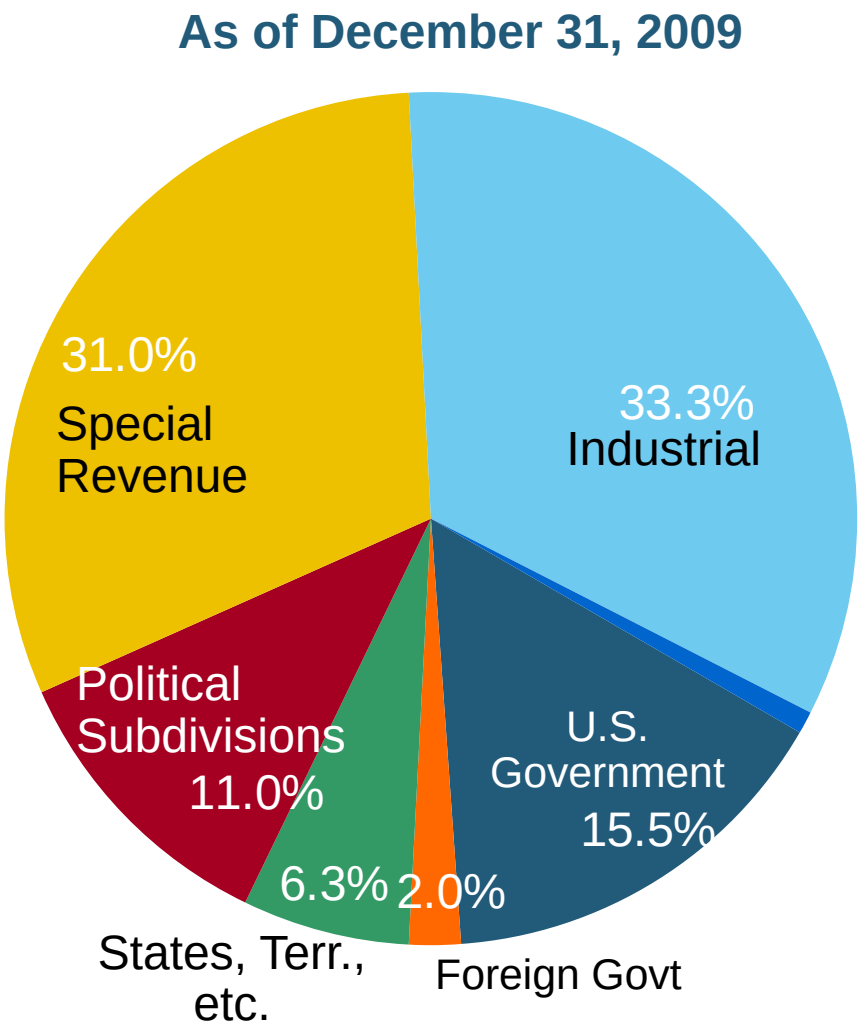
Bond Investment Facts as of 12/31/09

- Investments in "Political Subdivision [of states]" bonds were $102.5 billion
- Investments in "States, Territories, & Possessions" bonds were $58.9 billion
- Investments in "Special Revenue" bonds were $288.2 billion
- All state, local, and special revenue bonds totaled 48.2% of bonds, about 35.7% of total invested assets



Sources: NAIC, via SNL Financial; Insurance Information Institute research.

Municipal Bonds: Recent Issues

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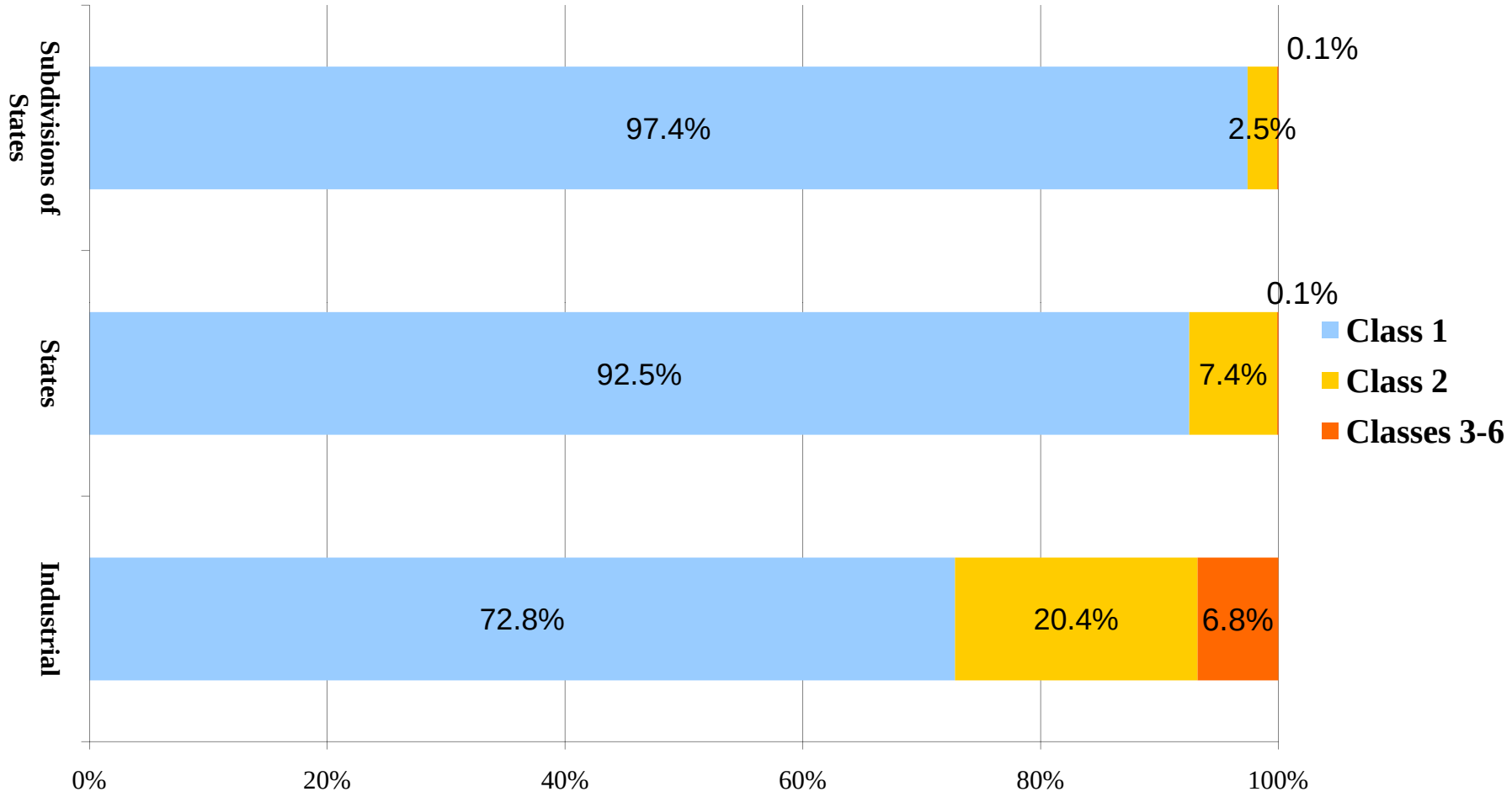
- **Most Government Entities Are Under Financial Distress**
  - Plunging tax receipts, higher outlays, pension obligations
- **Analyst Meredith Whitney in Dec. 2010 Said (on 60 Minutes) that a "Spate" of 50-100 Sizeable Defaults Totaling "Hundreds of Billions of Dollars**
  - Few other analysts believe such and outcome is likely, though most acknowledge that some are likely
- **The 3 Major Ratings Agencies Report Cumulative Muni Bond Default Rates Ranging from 0.04% to 0.29% from 2000-2009**
  - These figures indicate that muni defaults are very rare
  - Longer-term review corroborates rarity of such defaults
  - Even in the event of default municipalities often (eventually) make good on the debt
- **Municipalities Have Many Tools to Meet Obligations**
- **Revenues to State and Local Governments Are Starting to Recover**

2011 Financial Overview
When P/C Insurers Invest in Higher Risk Bonds, It's Corporates, Not Munis



The NAIC's Securities Valuation Office puts bonds into one of 6 classes: class 1 has the lowest expected impairments; successively higher numbered classes imply increasing impairment likelihood.

Data are as of year-end 2009. Sources: SNL Financial; Insurance Information Institute.

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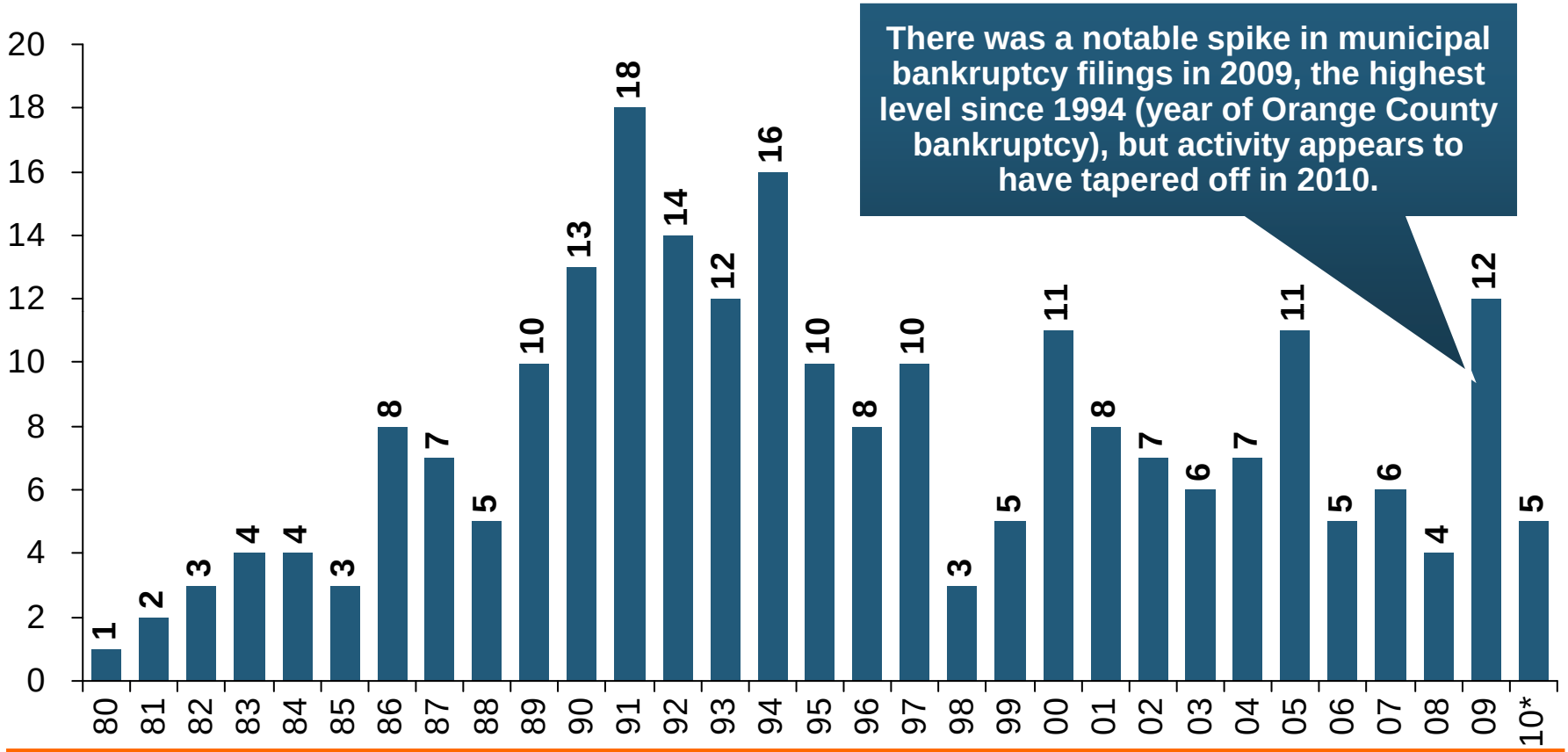
MUNICIPAL BOND CONCERNS

Collapse of Muni Bond Market is Highly Unlikely

Chapter 9 Bankruptcy Filings: 1980-2010:Q3



Chapter 9 bankruptcy allows for the reorganization of "municipalities," which include cities, towns, villages, counties, taxing districts, municipal utilities and school districts.

*Through Q3 2010.

Note: Chapter 9 bankruptcy allows for the reorganization of

Source: American Bankruptcy Institute; Insurance Information Institute.

Muni Bond Issuance: 2000 – 2011*

Muni issuance is was down in early 2011 after the end of a special federal program in 2010 and amid the fiscal problems of many states and municipalities

*Through March 4, 2011

Source: Thompson Reuters; Wall Street Journal; Insurance Information Institute.

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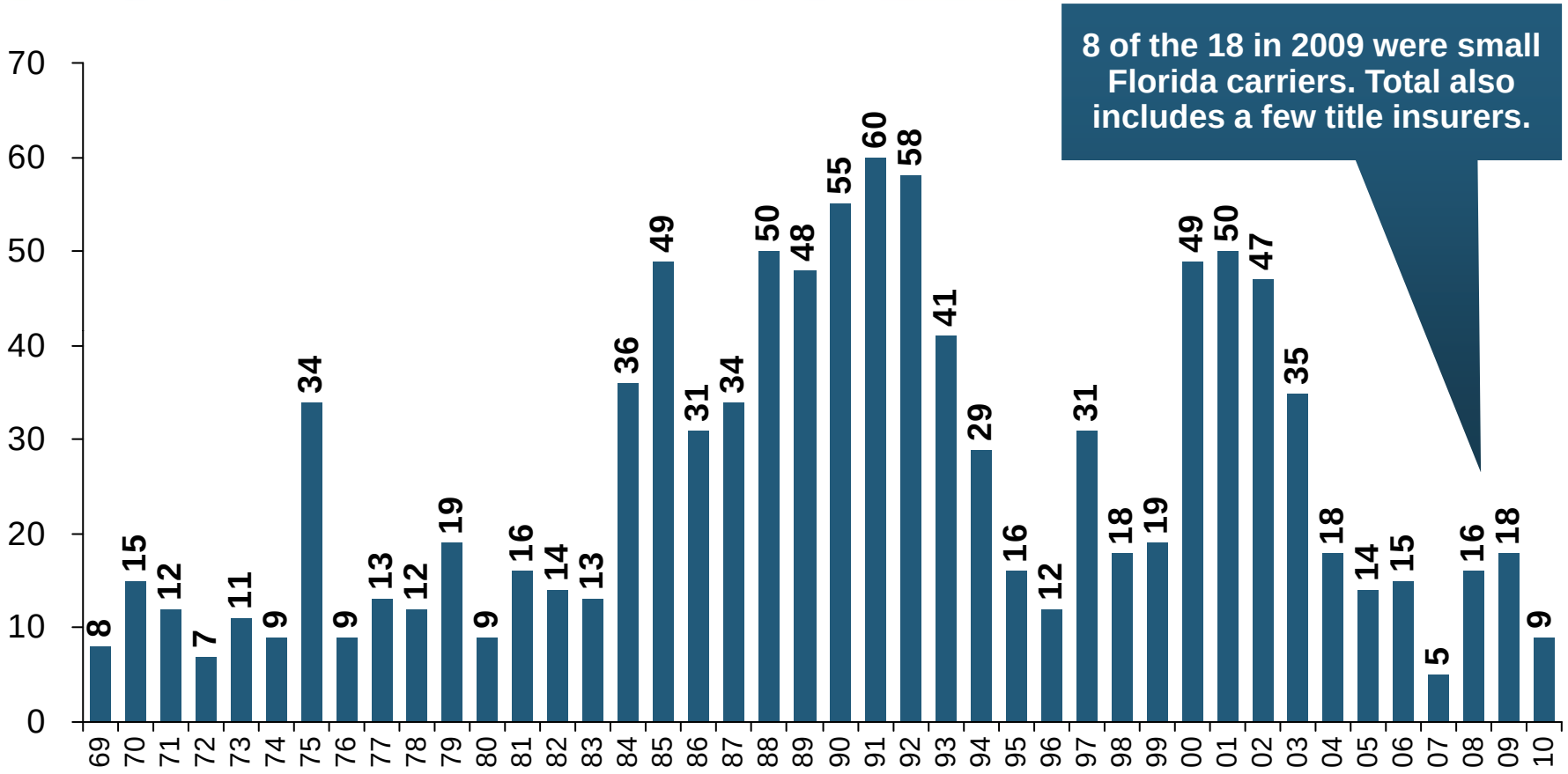
Financial Strength & Underwriting

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

P/C Insurer Impairments, 1969–2010E*

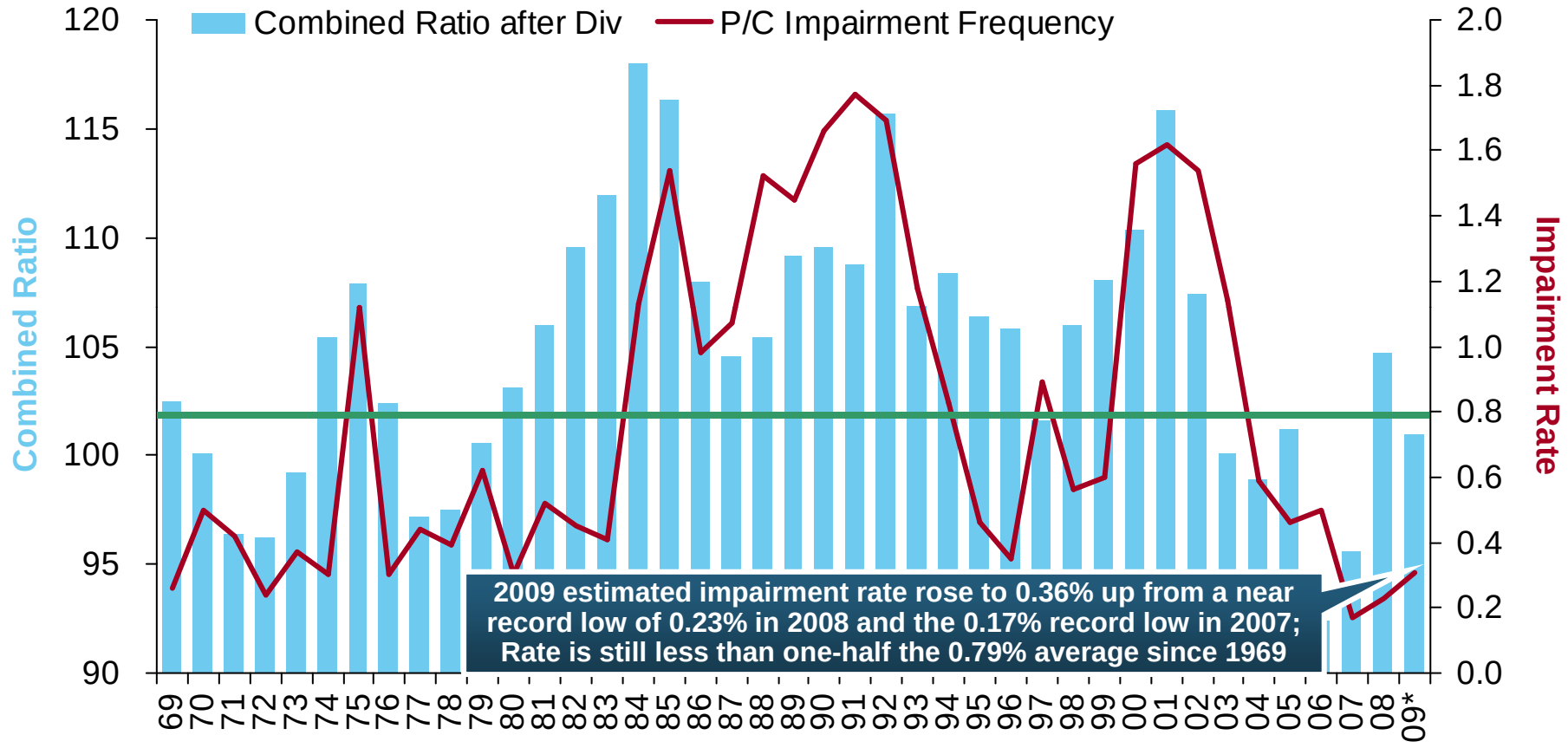


The Number of Impairments Varies Significantly Over the P/C Insurance Cycle, With Peaks Occurring Well into Hard Markets

*2010 estimate.

Source: A.M. Best Special Report "1969-2009 Impairment Review," June 21, 2010; Insurance Information Institute.

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

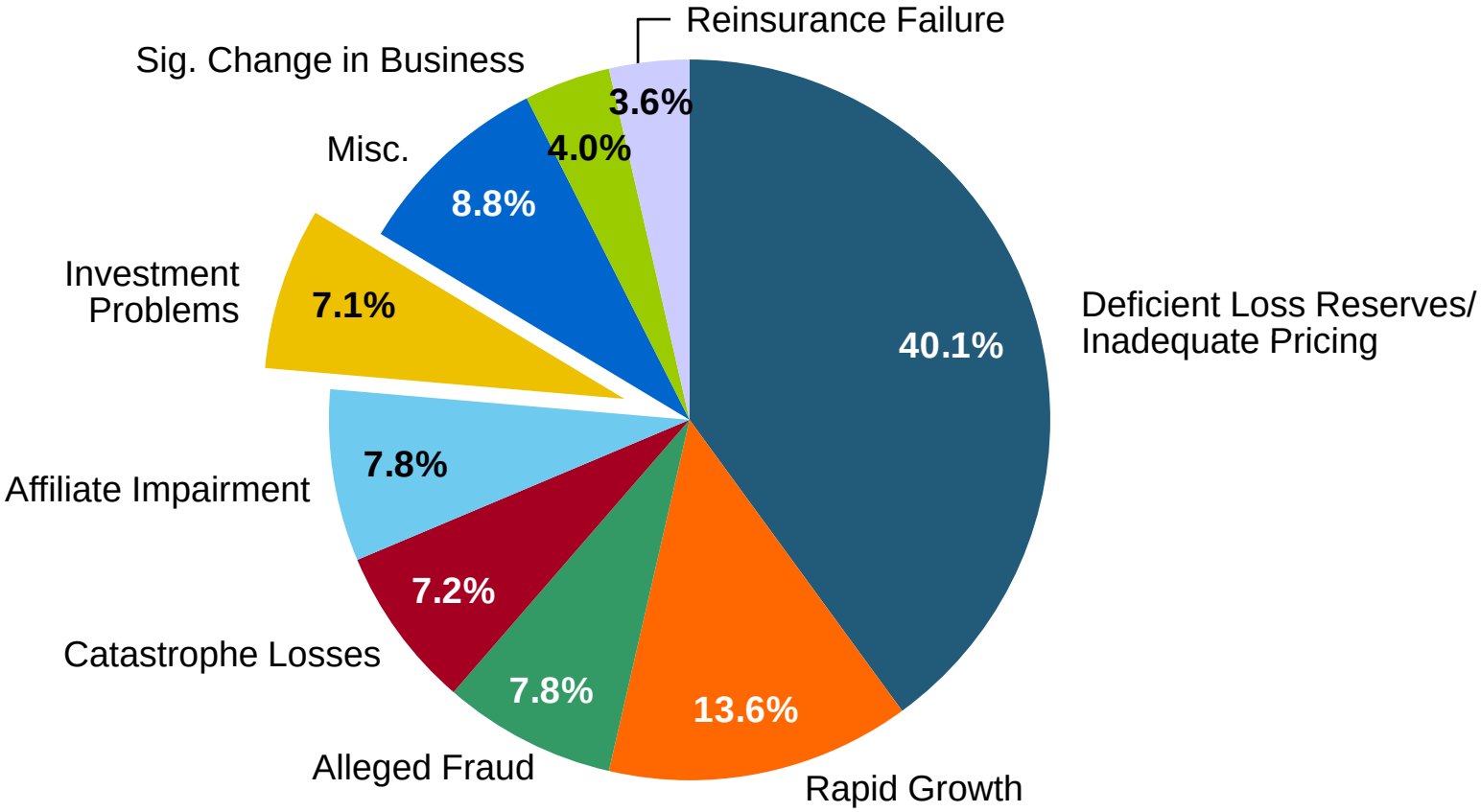


Impairment Rates Are Highly Correlated With Underwriting Performance and Reached Record Lows in 2007/08

Source: A.M. Best; Insurance Information Institute

Reasons for US P/C Insurer Impairments, 1969–2009

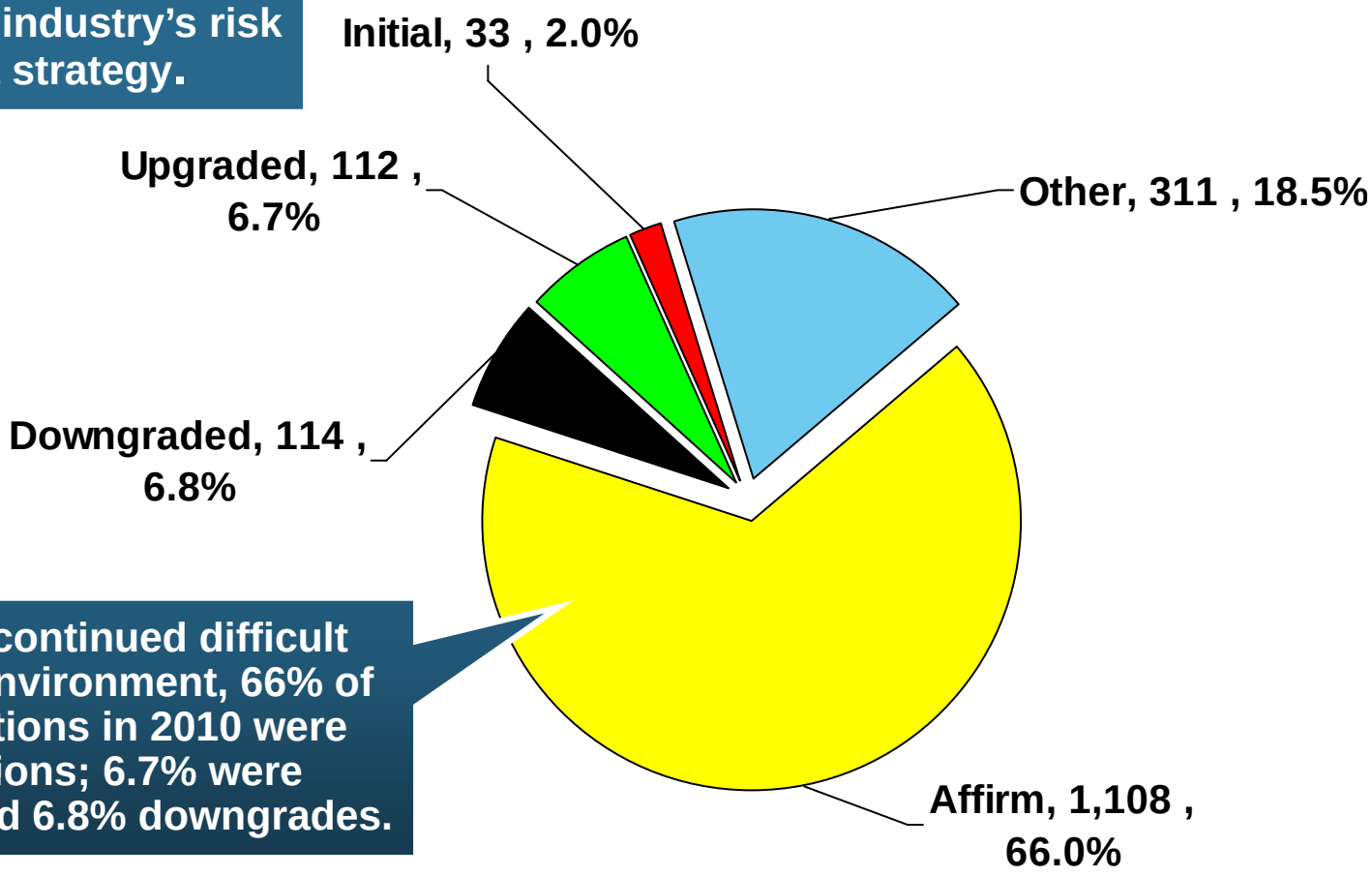
Historically, Deficient Loss Reserves and Inadequate Pricing Are By Far the Leading Cause of P-C Insurer Impairments. Investment and Catastrophe Losses Play a Much Smaller Role



Source: A.M. Best: *1969-2009 Impairment Review*, Special Report, June 21, 2010

Summary of A.M. Best's P/C Insurer Ratings Actions in 2010

P/C insurance is by design a resilient in business. The dual threat of financial disasters and catastrophic losses are anticipated in the industry's risk management strategy.

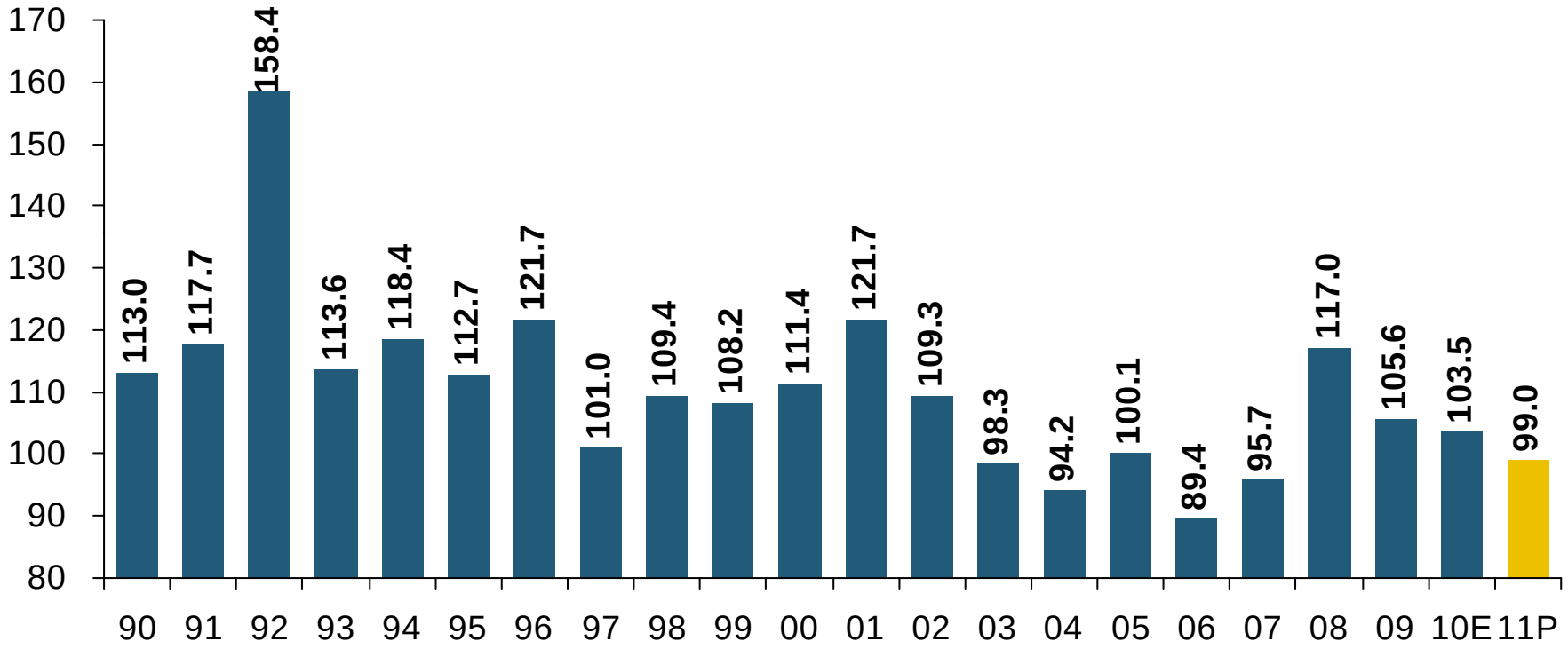


Despite a continued difficult operating environment, 66% of ratings actions in 2010 were affirmations; 6.7% were upgrades and 6.8% downgrades.

Source: A.M. Best.

Performance by Segment: Commercial/Personal Lines & Reinsurance

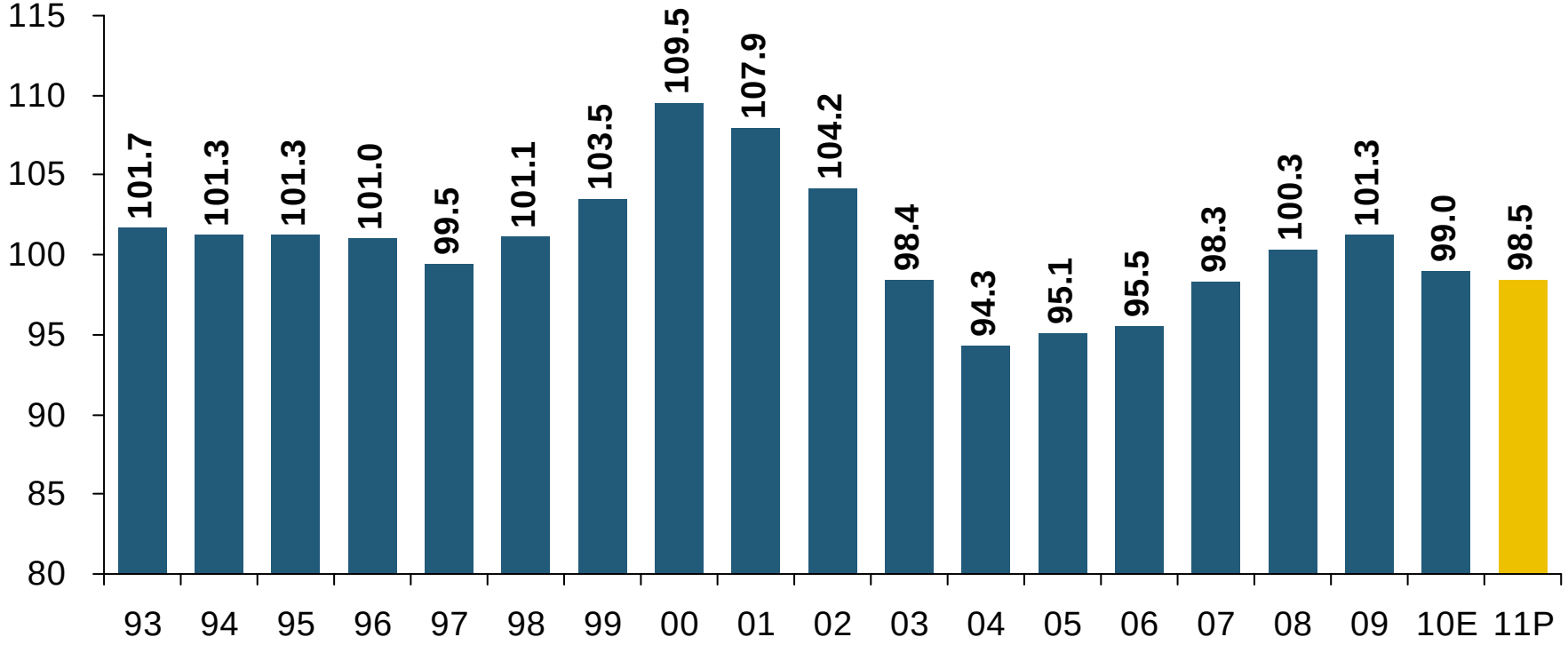
Homeowners Insurance Combined Ratio: 1990–2011P



Homeowners Line Is Expected to Improve in 2011. Extreme Regional Variation Can Be Expected Due to Local Catastrophe Loss Activity

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

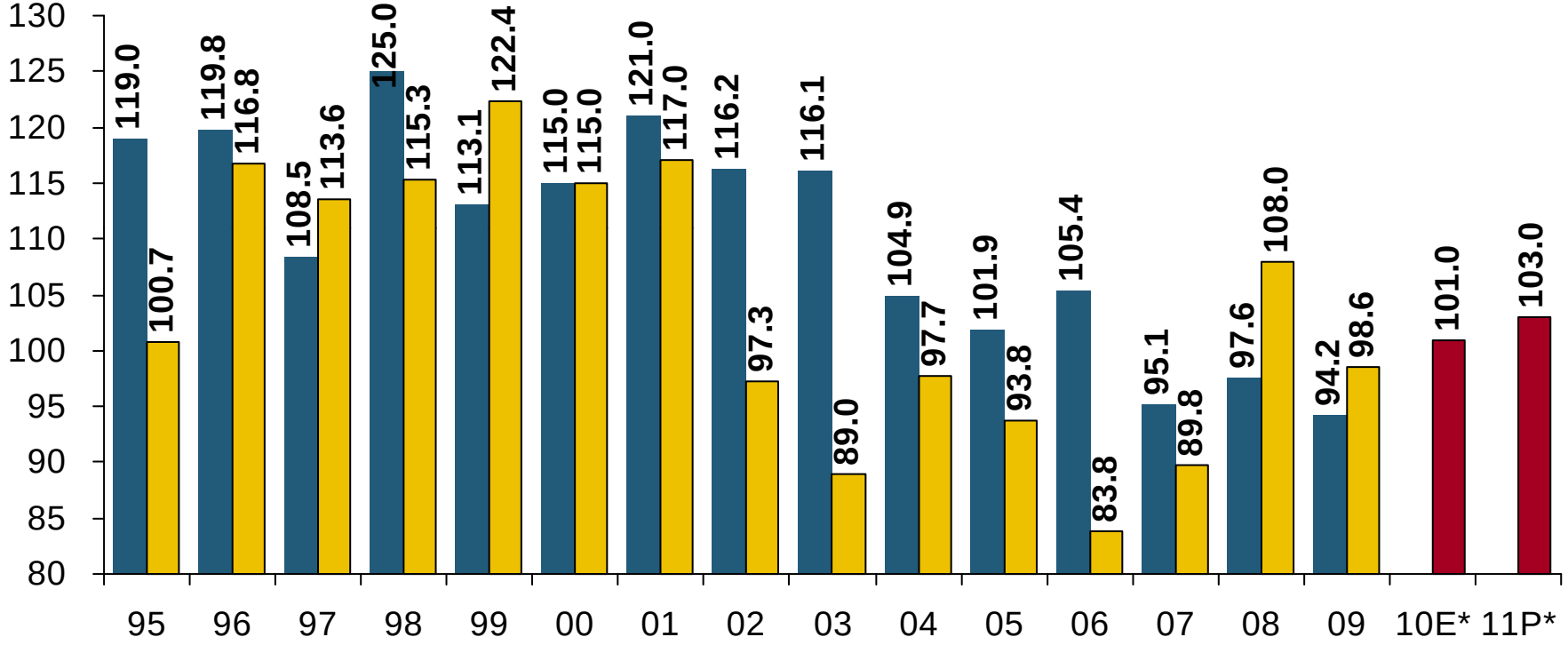
Private Passenger Auto Combined Ratio: 1993–2011P



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

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

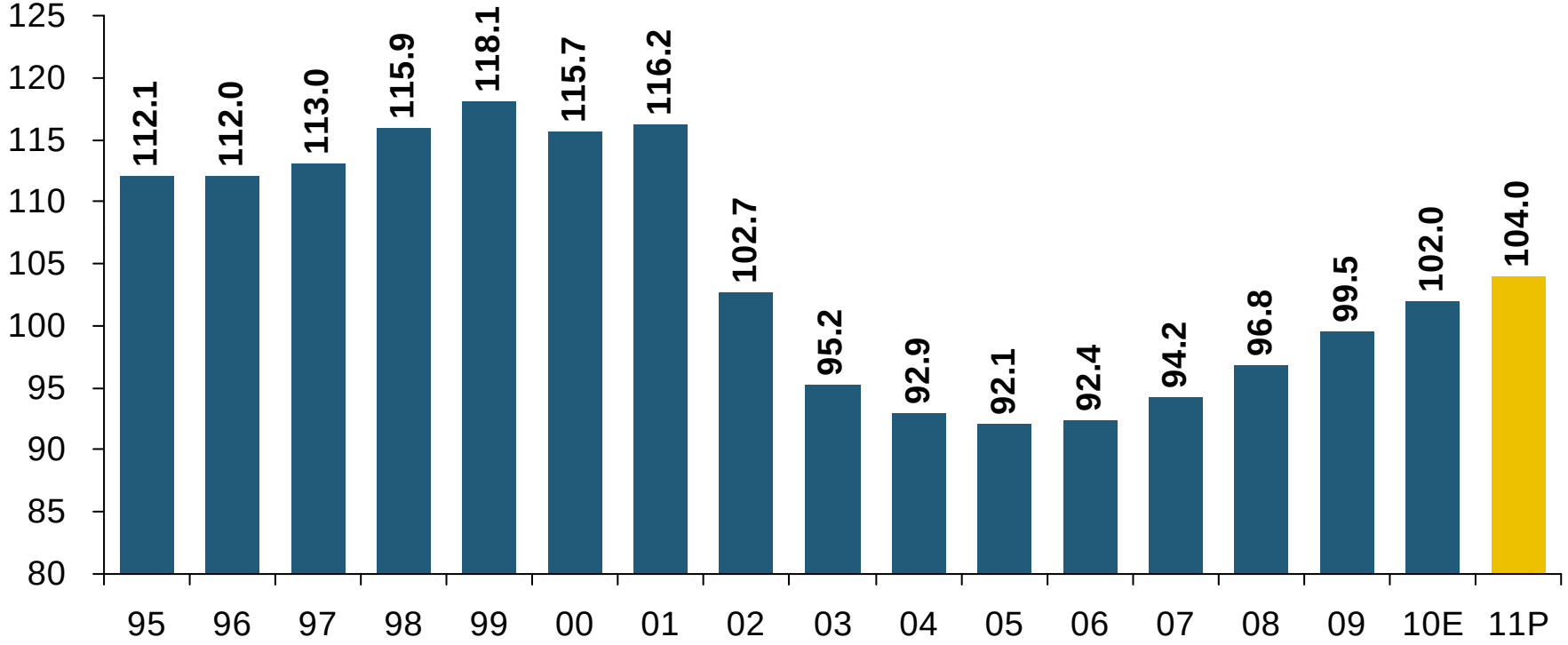
Commercial Multi-Peril Combined Ratio: 1995–2011P



Commercial Multi-Peril Underwriting Performance is Expected to Deteriorate Modestly

*2010Eand 2011P figures are for the combined liability and non-liability components.
Sources: A.M. Best; Insurance Information Institute.

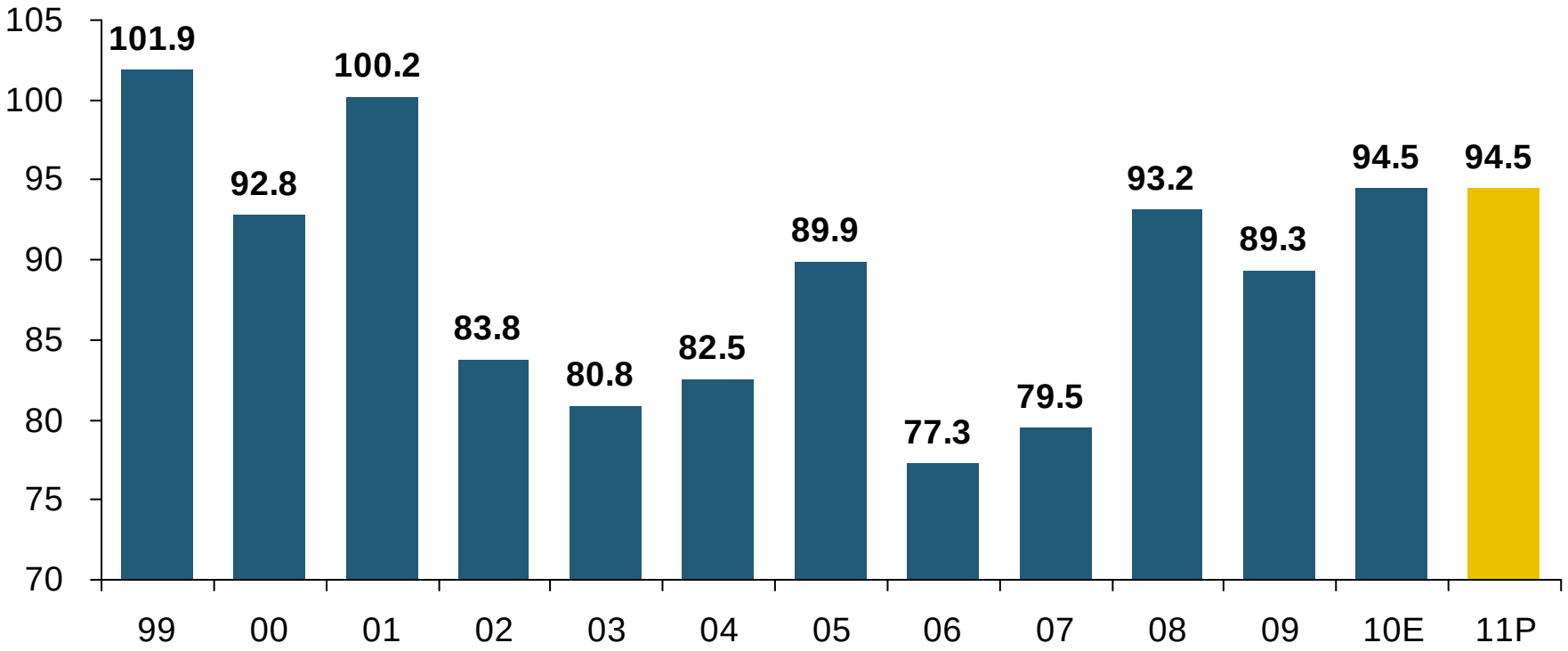
Commercial Auto Combined Ratio: 1993–2011P



Commercial Auto Underwriting Performance is Expected to Deteriorate Modestly

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

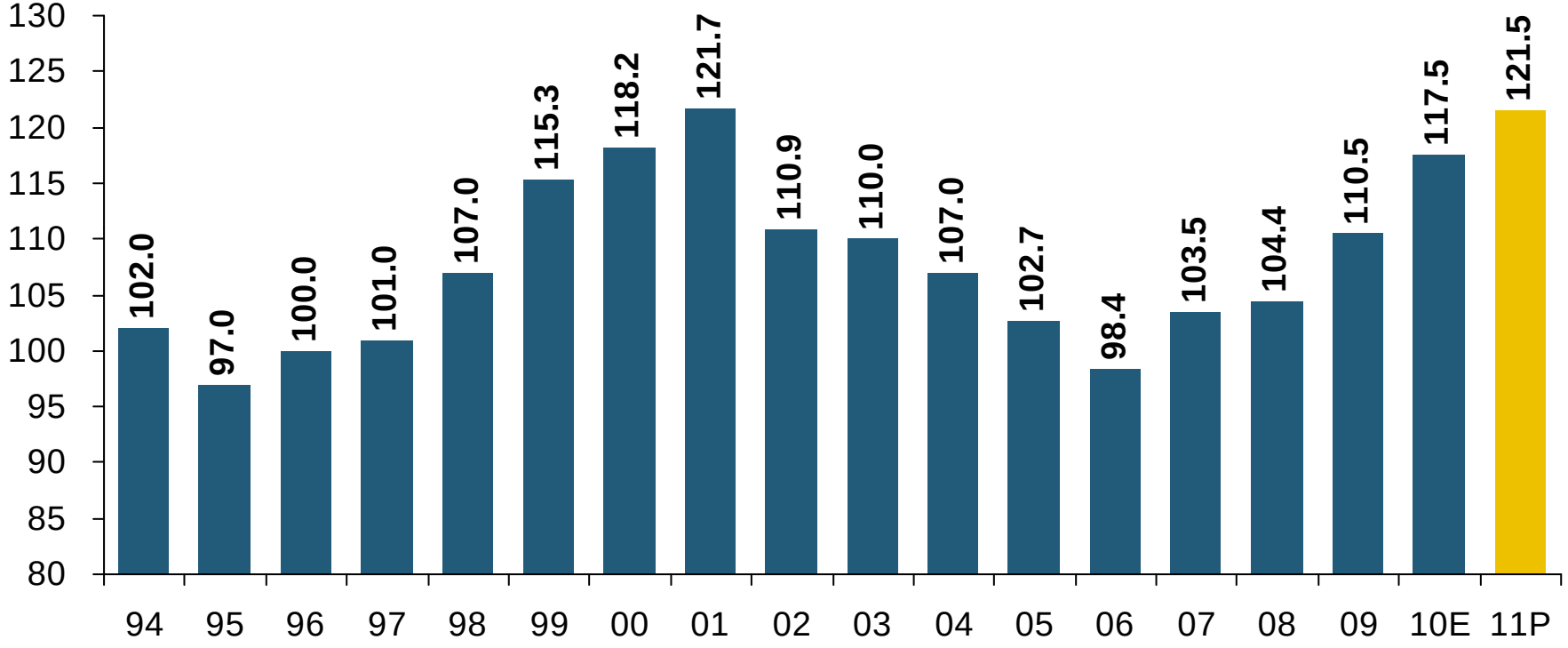
Inland Marine Combined Ratio: 1999–2011P



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

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

Workers Compensation Combined Ratio: 1994–2011P



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

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

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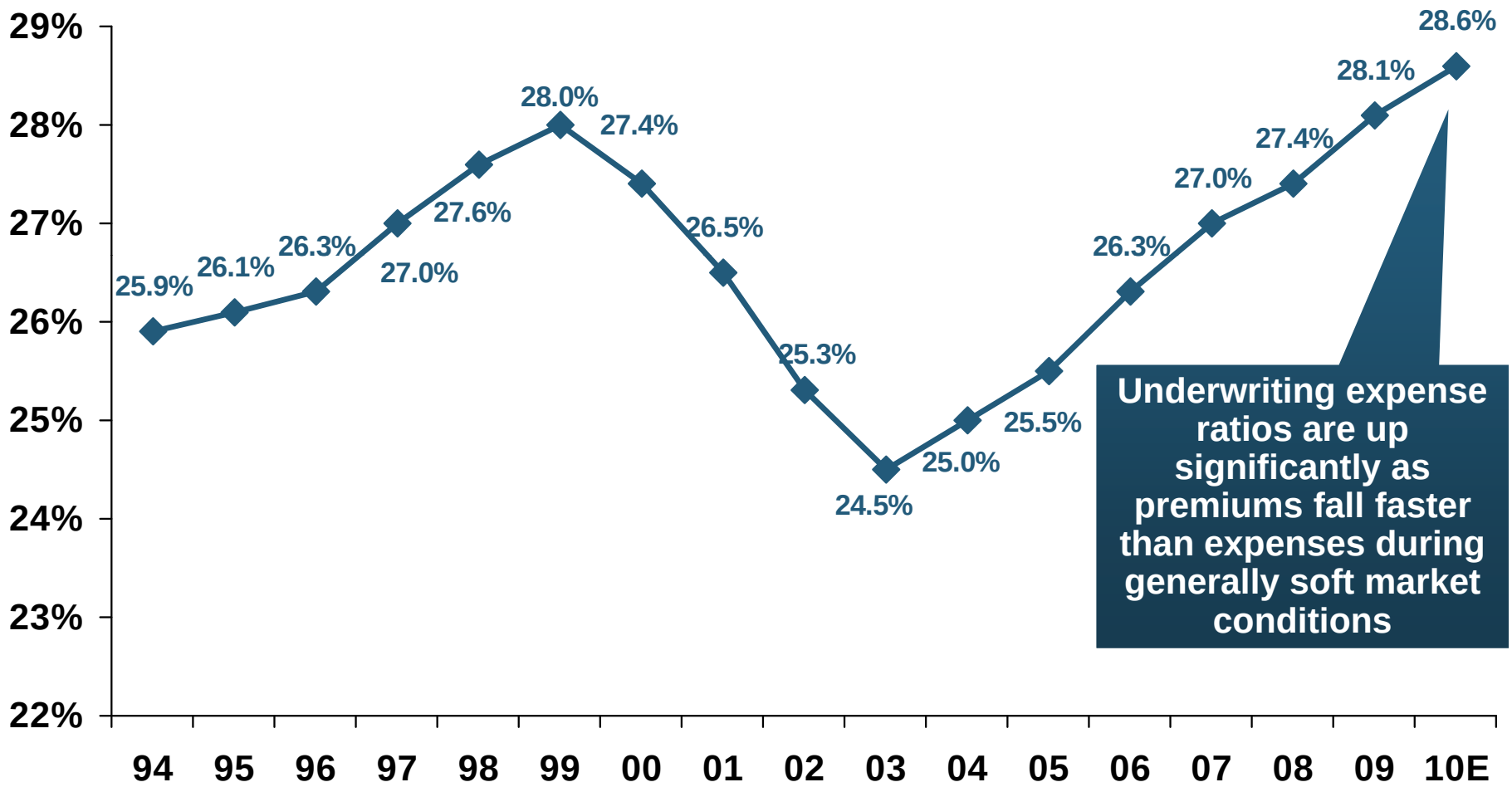
EXPENSES

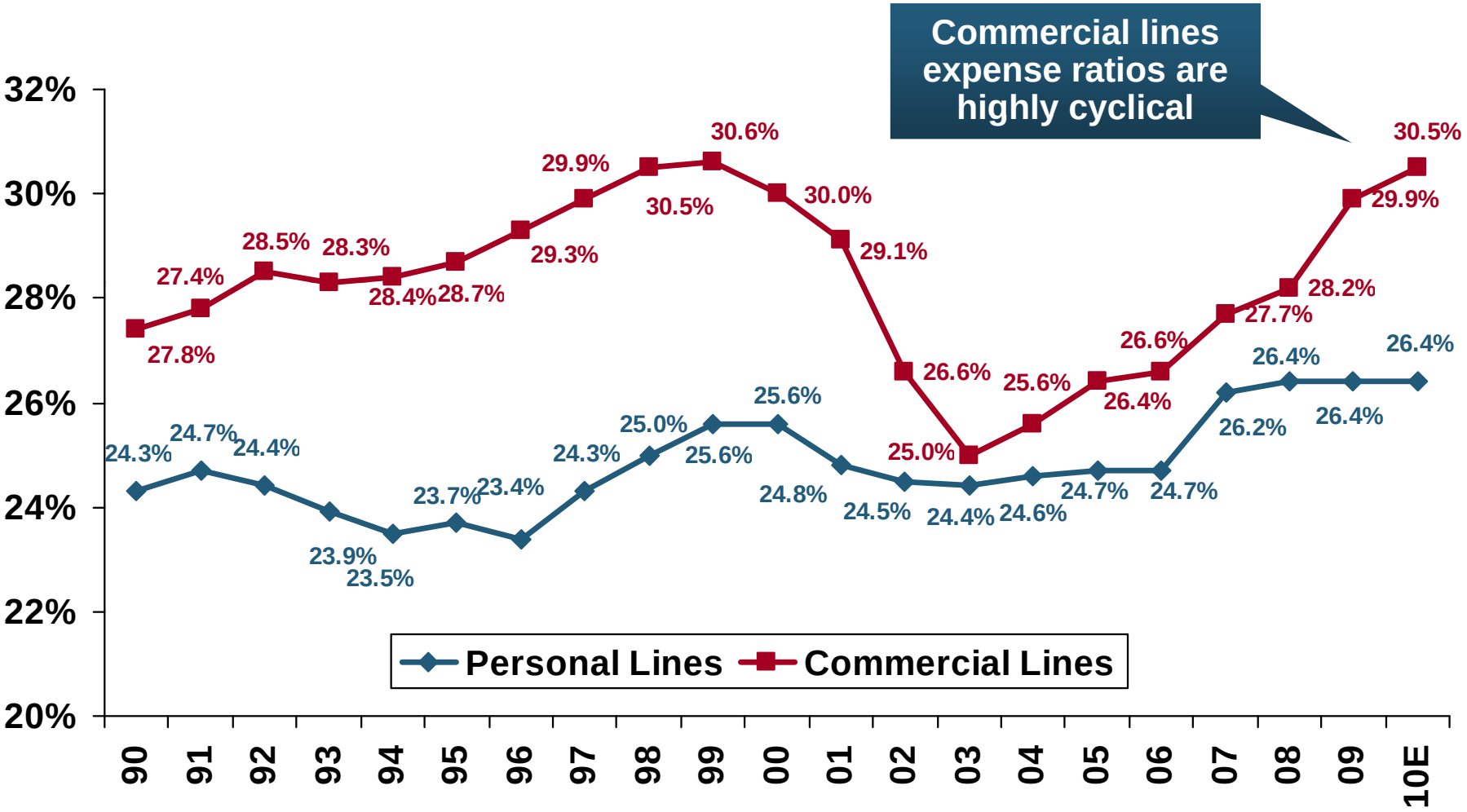
Expense Ratios Are Highly Cyclical and Contribute Deteriorating Underwriting Performance

Underwriting Expense Ratio* All P/C Lines, 1994-2010E**



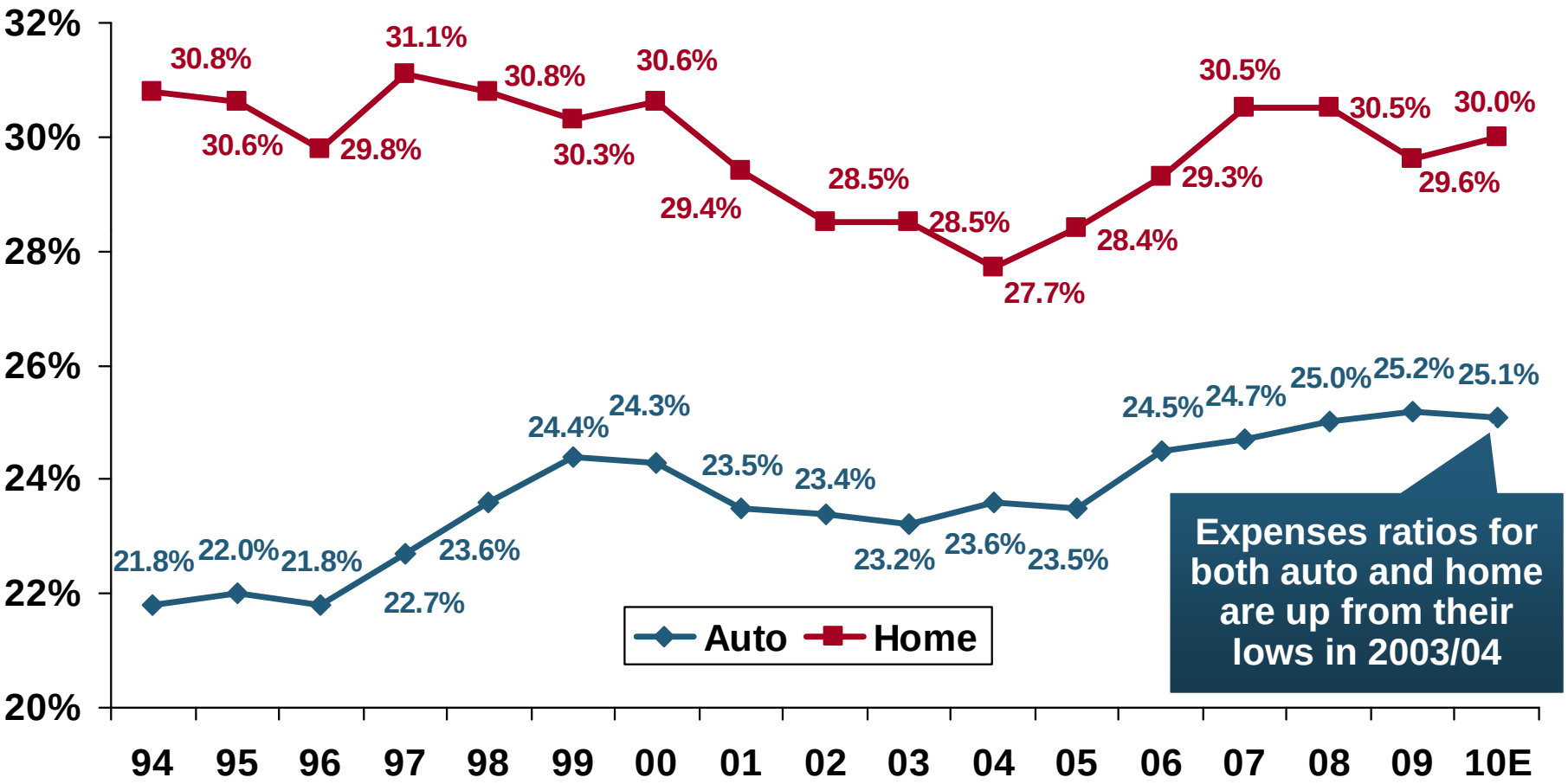
*Ratio of expenses incurred to net premiums written.
**2010 figure based on data through 2010:Q3.
Source: A.M. Best; Insurance Information Institute.

Underwriting Expense Ratio*:
Personal vs. Commercial Lines, 1990-2010E**



*Ratio of expenses incurred to net premiums written.
**2010 figures are estimates.
Source: A.M. Best; Insurance Information Institute.

Underwriting Expense Ratio*
Personal Lines (Auto & Home), 1994-2010E**



*Ratio of expenses incurred to net premiums written.
**2010 figures are estimates.
Source: A.M. Best; Insurance Information Institute.

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CAPITAL MANAGEMENT & LEVERAGE

Excess Capital is a Major Obstacle to a Market Turn;

Capital Management Decisions Will Impact Market Direction

US Policyholder Surplus: 1975–2010*

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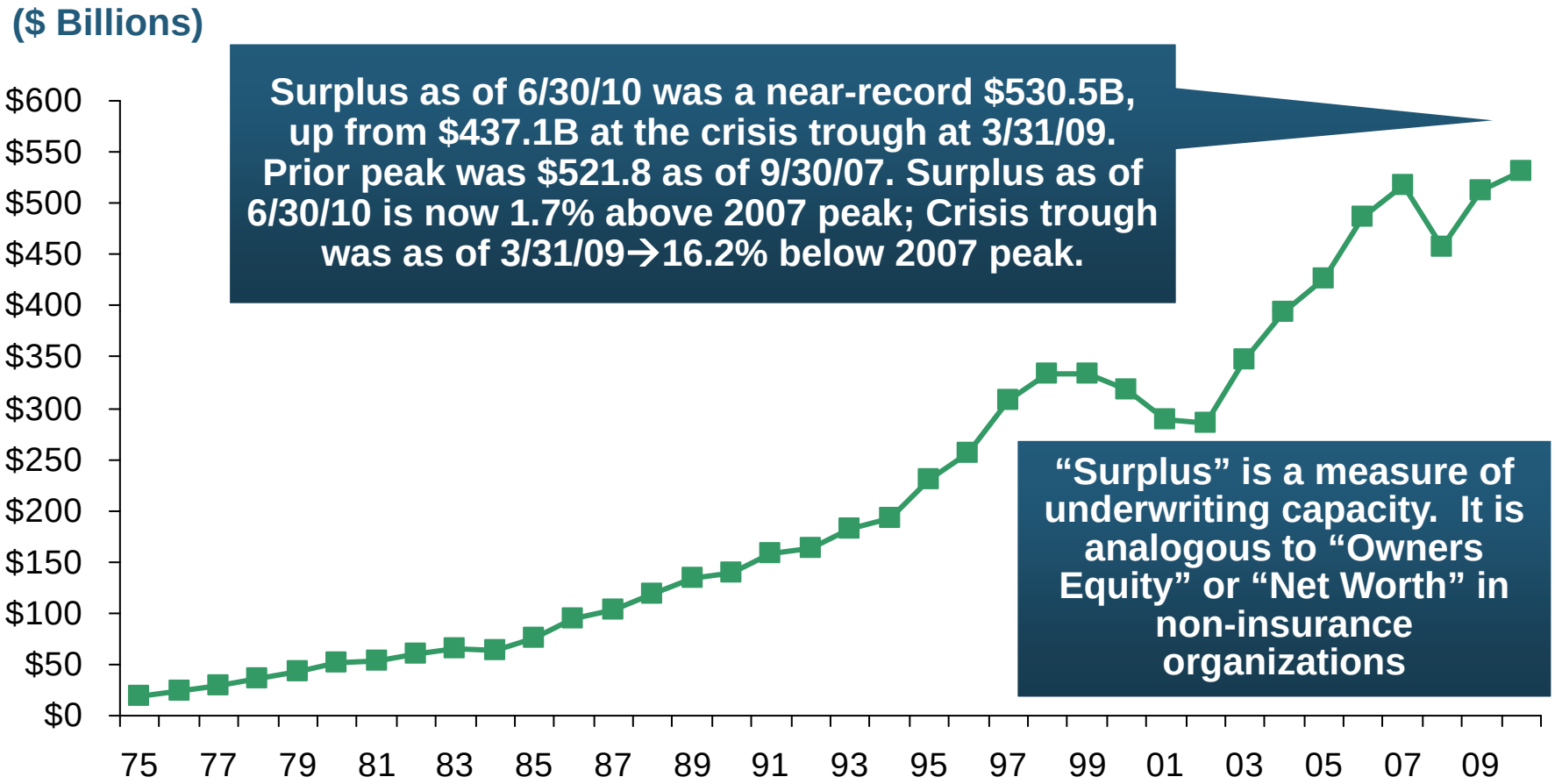
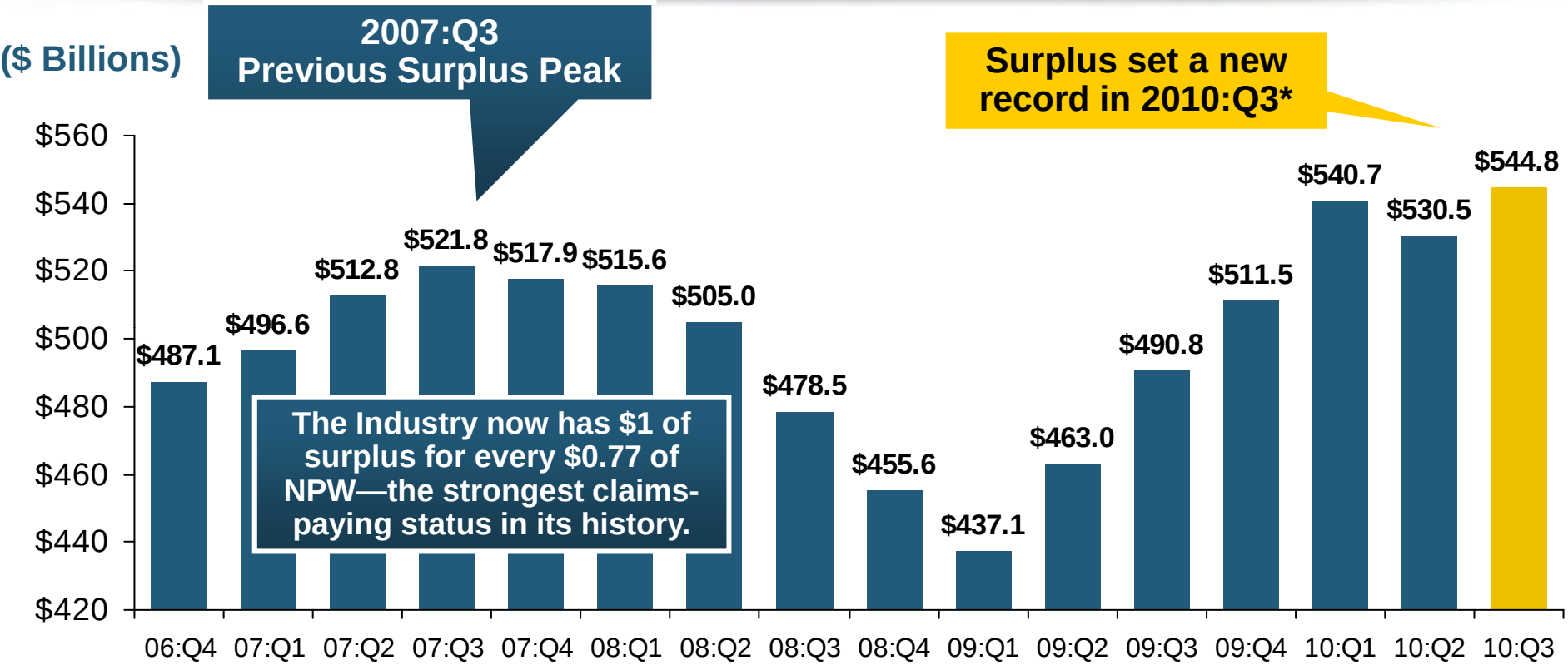


The Premium-to-Surplus Ratio Stood at $0.80:$1 as of 6/30/10, A Record Low (at Least in Recent History)**

* As of 6/30/10; **Calculated using annualized net premiums written based on H1 2010 data.

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

Policyholder Surplus, 2006:Q4–2010:Q3



*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.

Quarterly Surplus Changes Since 2007:Q3 Peak

09:Q1: -$84.7B (-16.2%)	10:Q1: +$18.9B (+3.6%)
09:Q2: -$58.8B (-11.2%)	10:Q2: +$8.7B (+1.7%)
09:Q3: -$31.0B (-5.9%)	10:Q3: +$23.0B (+4.4%)
09:Q4: -$10.3B (-2.0%)	

Sources: ISO, A.M .Best.

Paid-in Capital, 2005–2010:Q3

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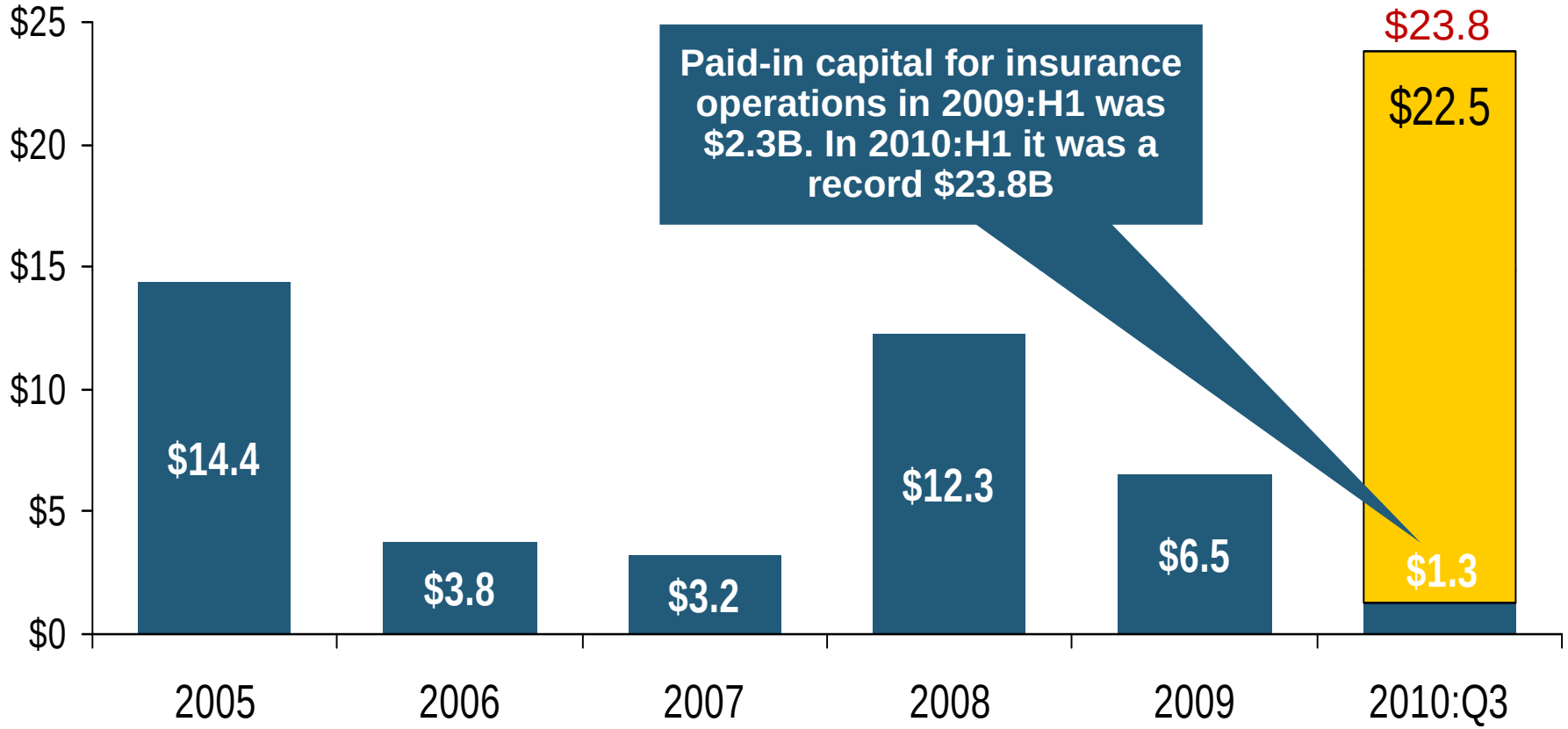
($ Billions)



In 2010:Q3 One Insurer's Paid-in Capital Rose by $22.5B as Part of an Investment in a Non-insurance Business

Source: ISO.

Global Reinsurance Capacity Shrank in 2008, Mostly Due to Investments

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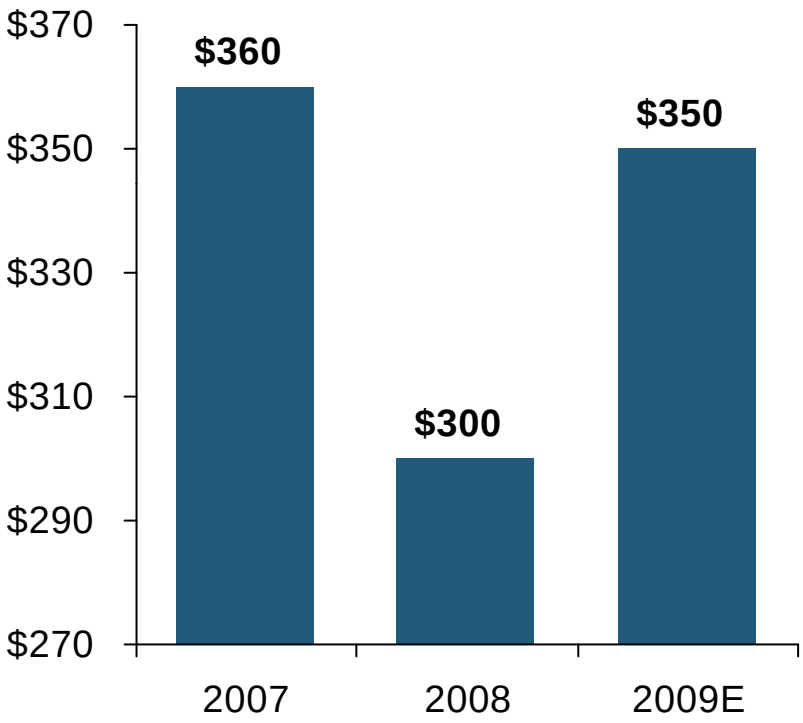
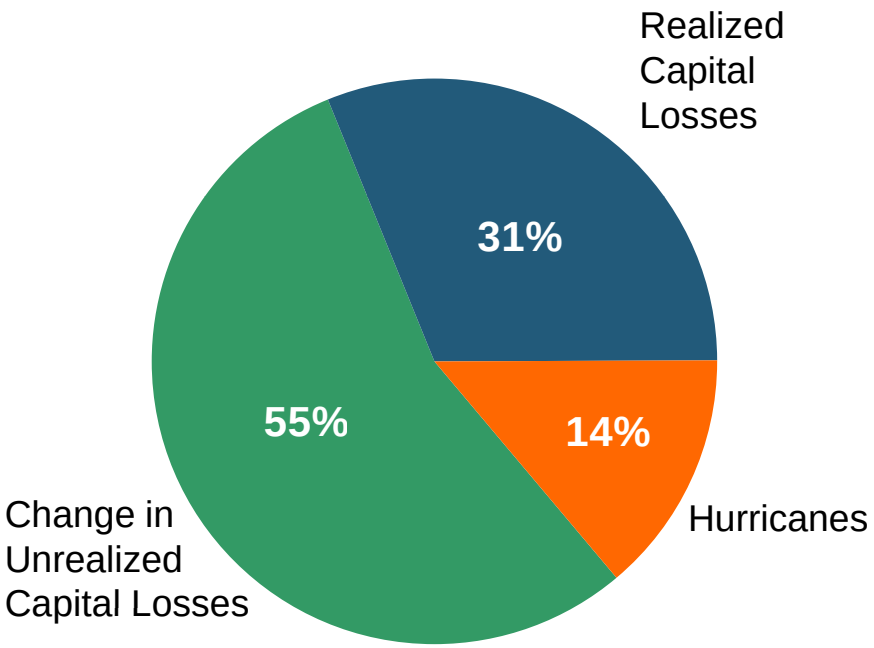
Global Reinsurance Capacity



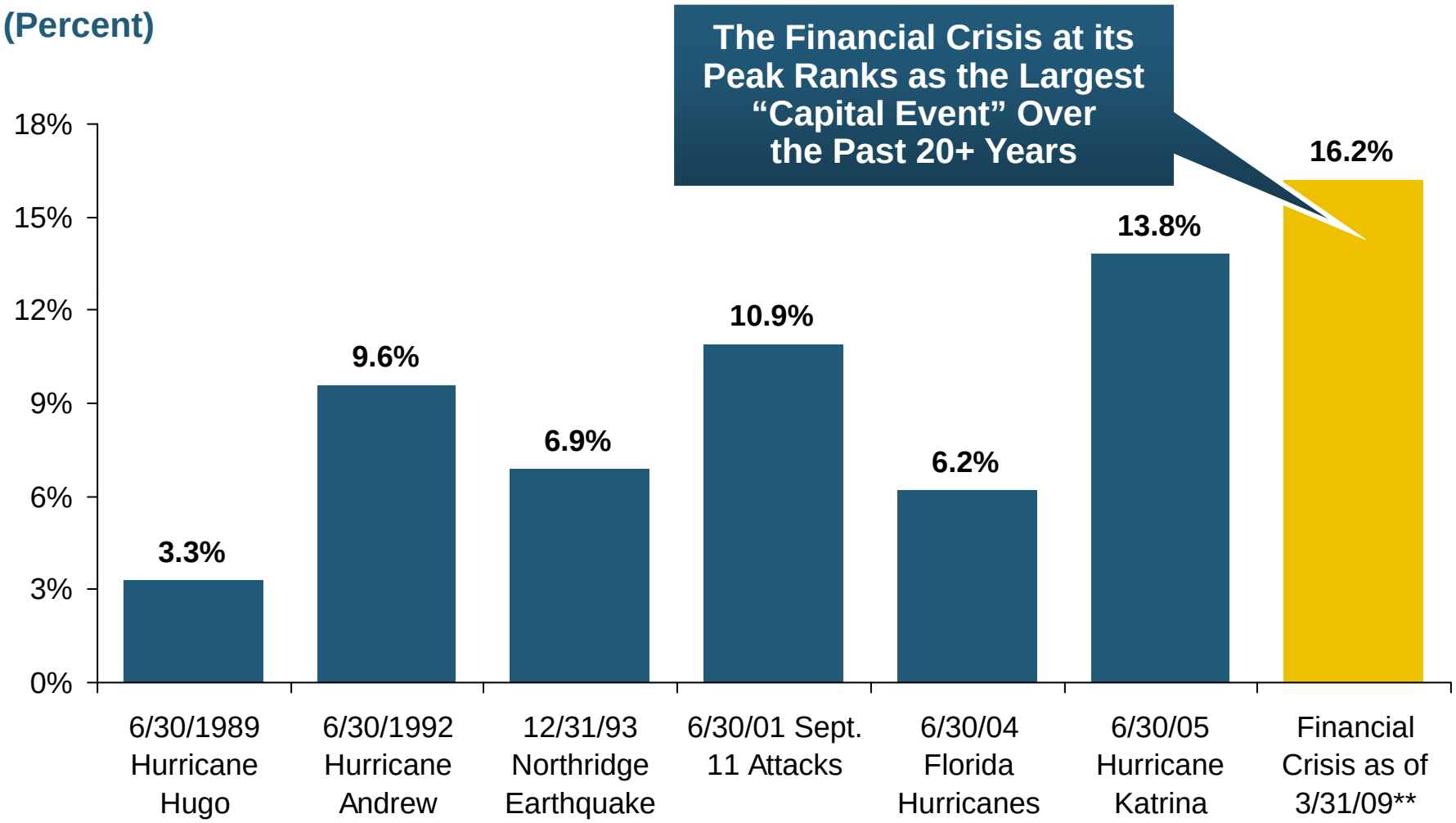
Source of Decline in 2008



Global Reinsurance Capacity Fell by an Estimated 17% in 2008

Source: AonBenfield Reinsurance Market Outlook 2009; Insurance Information Institute estimate for 2009.

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



* 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*

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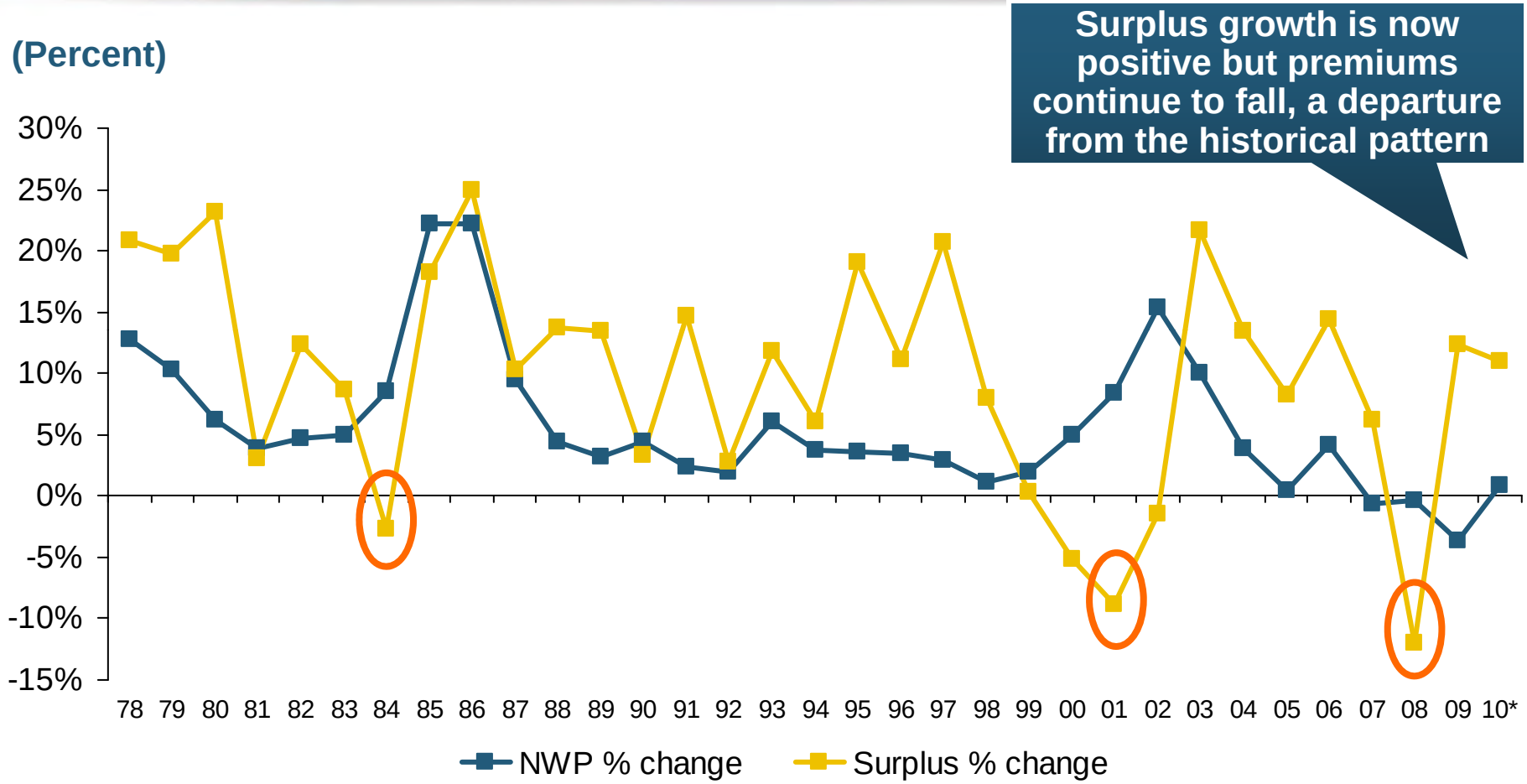

Sharp Decline in Capacity is a Necessary but Not Sufficient Condition for a True Hard Market

* 2010 NWP and Surplus figures are % changes as of Q3:10 vs Q3:09.

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

Ratio of Net Premiums Written to Policyholder Surplus, 1970-2010*

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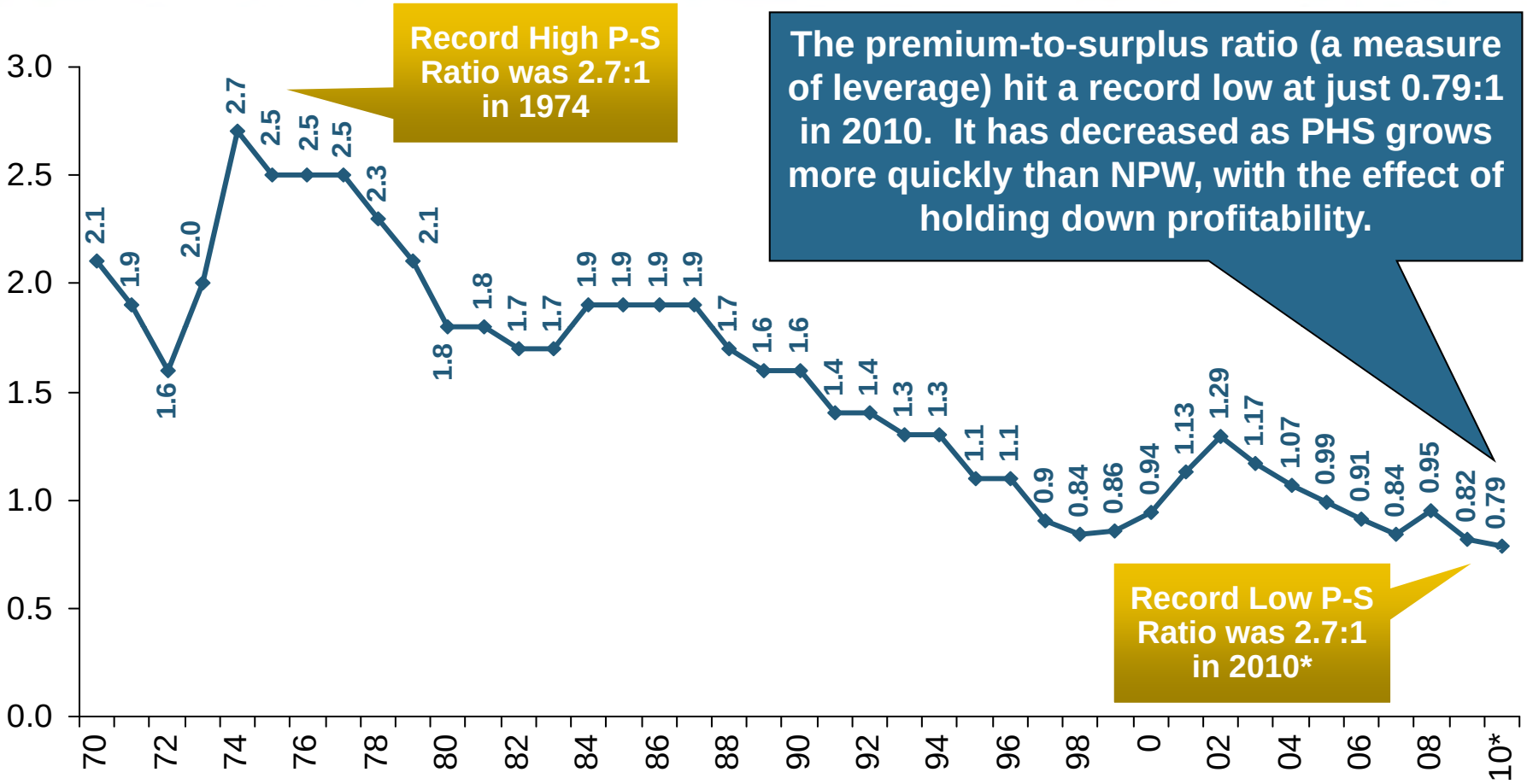

The Premium-to-Surplus Ratio in 2010 Implies that P/C Insurers Held $1 in Surplus Against Each $0.79 Written in Premiums. In 1974, Each $1 of Surplus Backed $2.70 in Premium.

*2010 data are is estimated using annualized NWP data through 2010:Q3.

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

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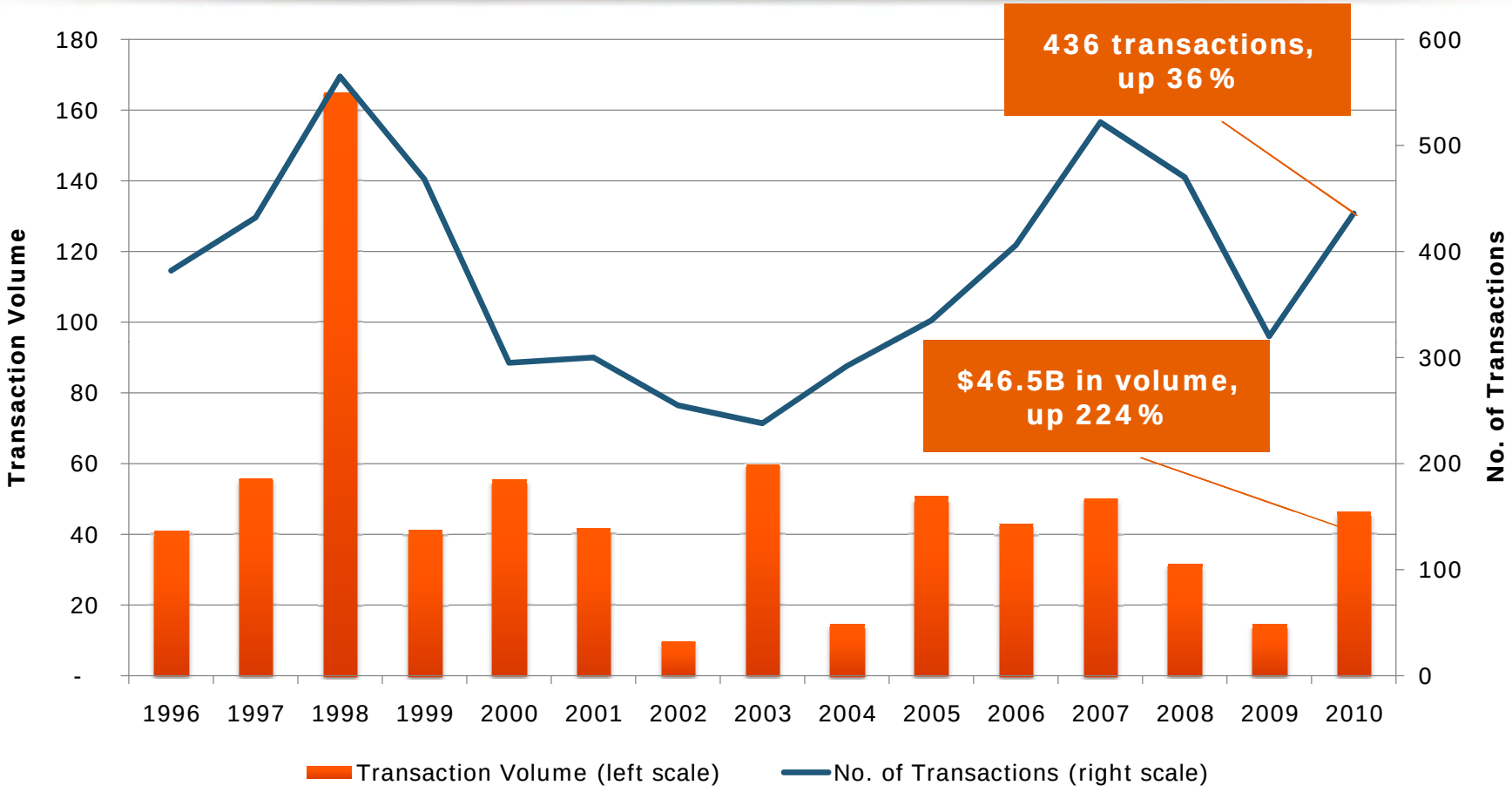
Merger & Acquisition

Capital Cycles Can Drive Consolidation

2010: U.S. Insurance M&A Bounces Back (All Segments)



U.S. activity rebounded from lows recorded in 2009. M&A also made a comeback worldwide, with global activity rising 20%.

Sources: Conning Research Consulting; Insurance Information Institute.

U.S. P/C Insurance-Related M&A Activity, 1988–2010E*

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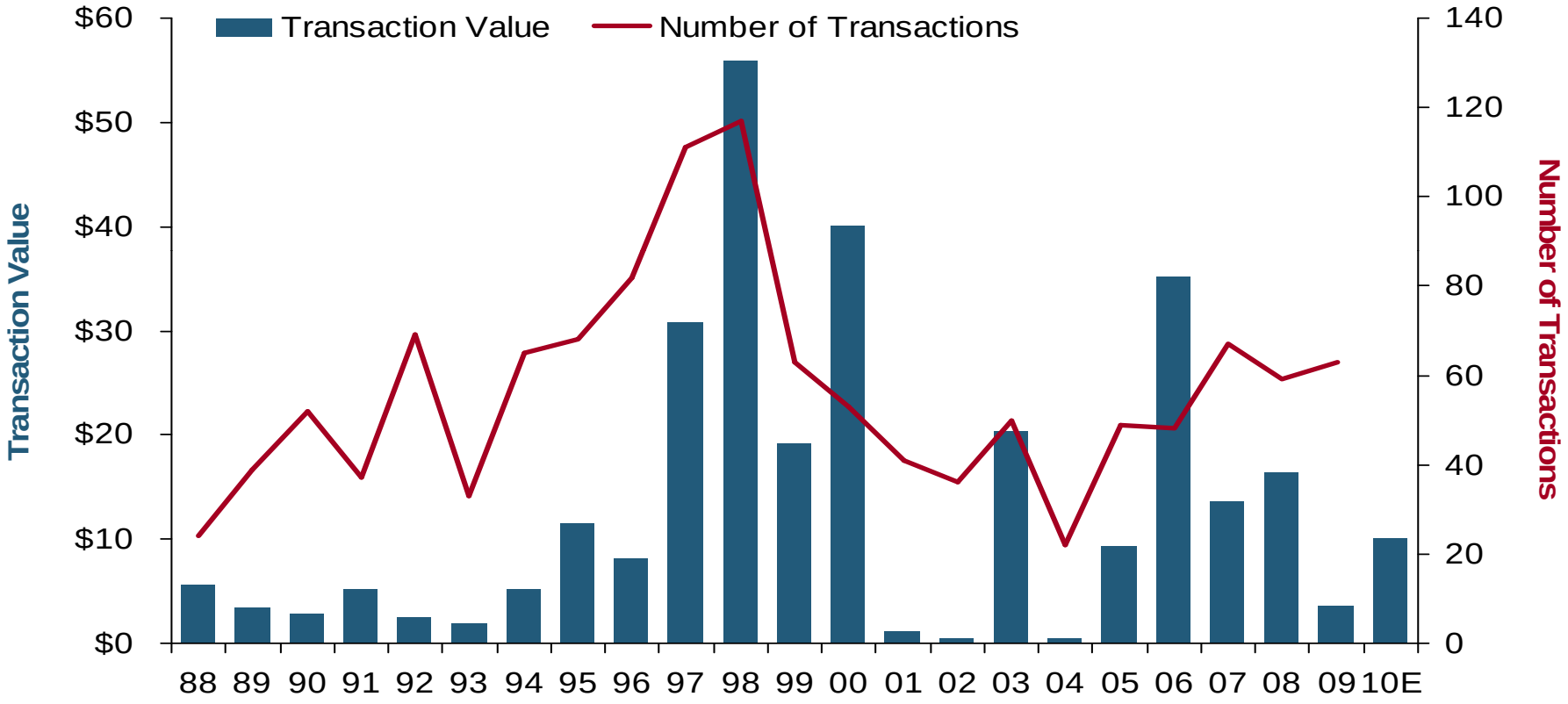
($ Billions)



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

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

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

Source: Conning Research & Consulting. *2010E is derived from A.M. Best data for p/c insurers only (excludes brokers/agencies)

U.S. P/C M&A Activity Rising, Volume Bouncing Back

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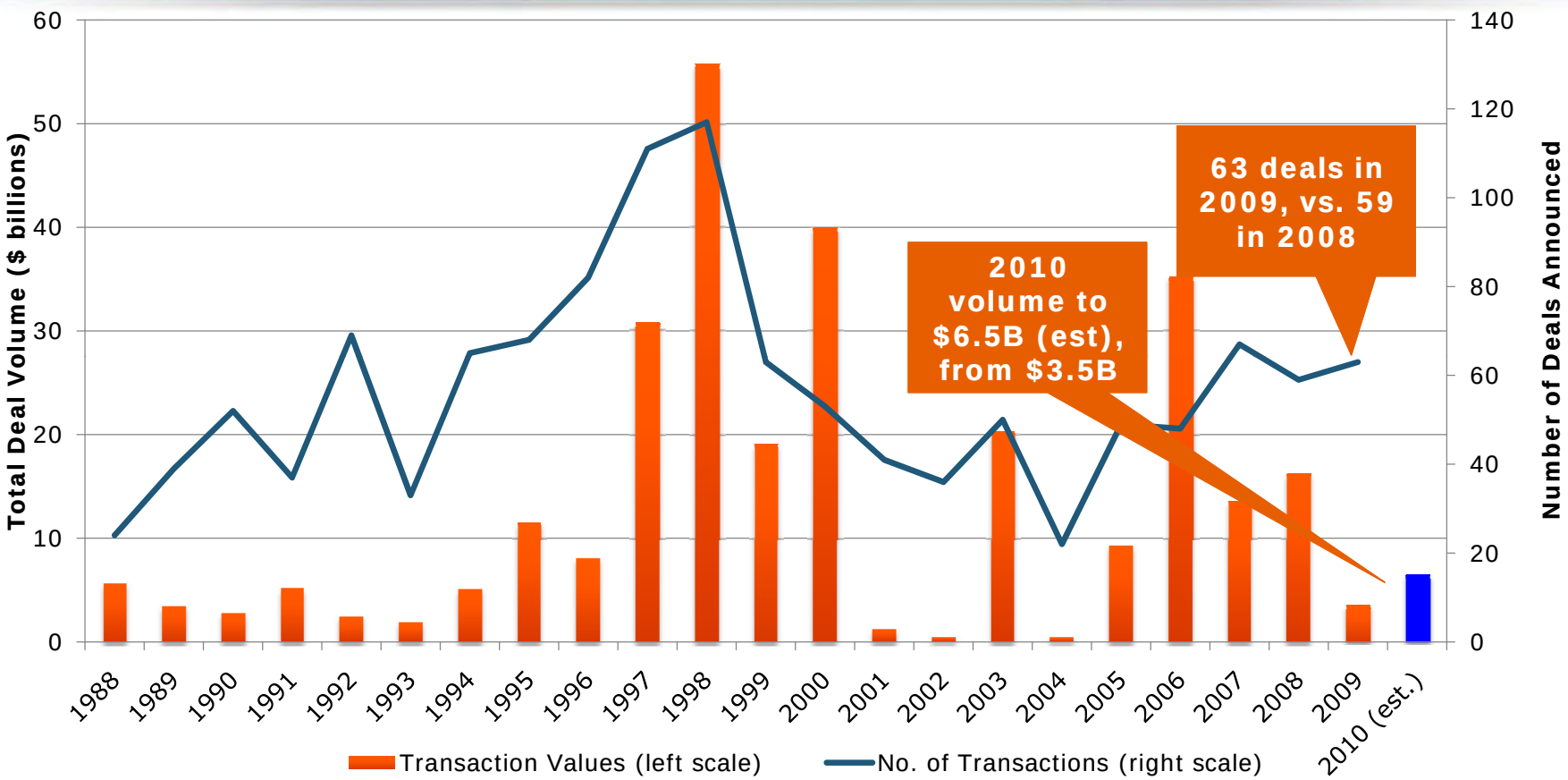
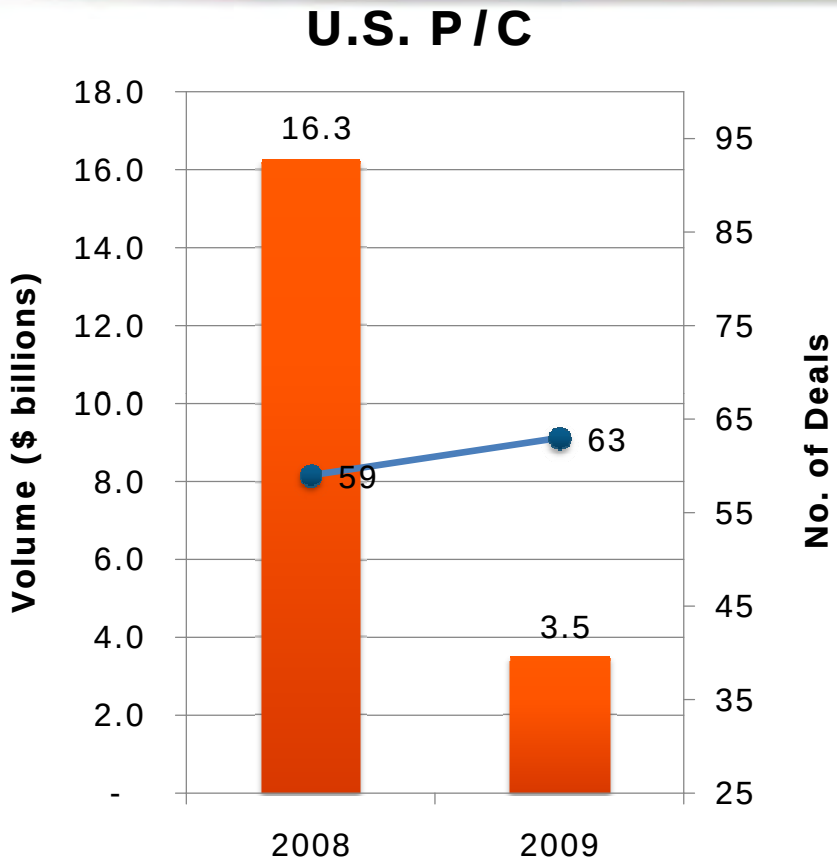
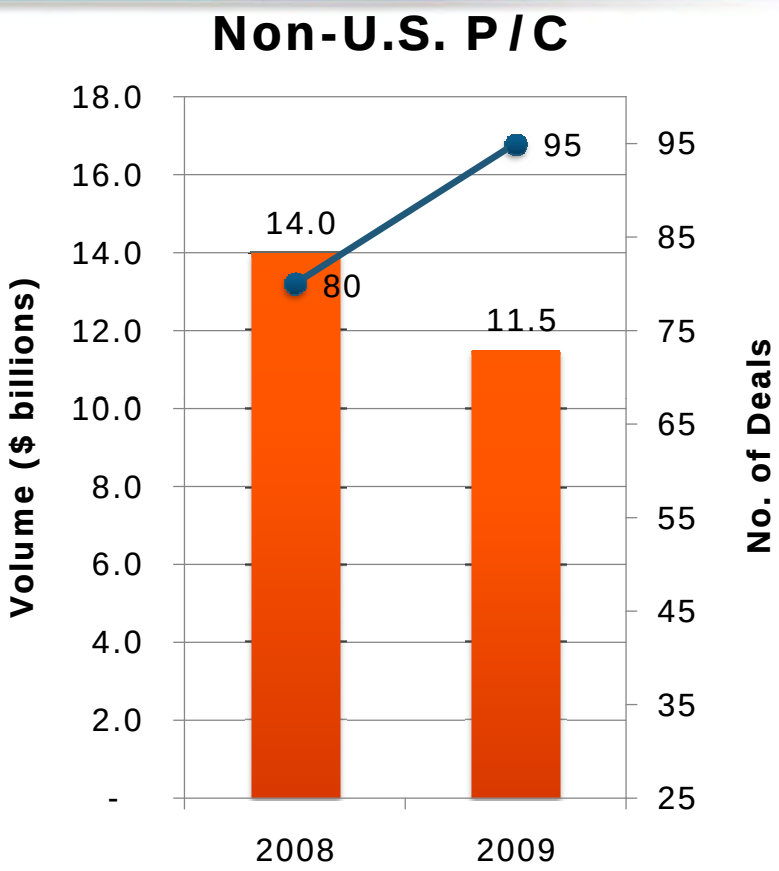


After a severe drop due to the capital crunch, M&A volume began to rebound in 2010. Levels remain below 1998-2000 and 2006 peaks.

Sources: Conning Research & Consulting through 2009; 2010 vol. est. from A.M. Best (2010 deal count N/A); Insurance Information Institute.

2009: More M&A activity outside U.S.





Non-U.S. activity exceeded U.S. activity in number and volume. Non-U.S. volume fell, but not as sharply as in U.S.

Sources: Conning Research Consulting; Insurance Information Institute.

2009: Five Largest U.S. Deals

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Buyer	Target	Value (millions)	Motivation
Zurich Financial Services AG	21st Century Insurance Group	$1.900	AIG asset sale
Fairfax Financial Holdings	Odyssey Re Holding Corp.	960	Topping off ownership
Medical Professional Mutual Insurance Co.	Fincor Holdings, Inc.	237	Consolidation
Tower Group, Inc.	Specialty Underwriters Alliance, Inc.	107	Geographic expansion/Diversification of operations
Emerging Capital Partners	Nouvelle Societe Interafricaine d'Assurance Participatiion S.A. (Cote d'Ivoire)	48	Investment in Africa's financial sector

Only one deal exceeded $1 Billion in 2009, vs. two in 2008 that exceeded $4 billion apiece (Liberty buying Safeco and Tokio's acquisition of Philadelphia Insurance Cos.)

Sources: Conning Research Consulting; Insurance Information Institute.

2009: Five Largest Non-U.S. Deals

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Buyer	Target	Value (millions)	Motivation
Banque Nationale de Paris Paribas Assurance (France)	Fortis Insurance Belgium (Belgium)	1,861	Fortis Bank forced to sell insurance assets
Partner Re Ltd. (Bermuda)	Paris Re Holdings Ltd (Switzerland)	1,716	Consolidation
Validus Holdings, Ltd. (Bermuda)	IPC Holdings Ltd. (Bermuda)	1,650	Consolidation
Polish State (Poland)	PZU S.A. (Poland)	1,200	Privatization of state assets
Porto Seguro S.A. (Brazil)	Seguros de Automovel e Residencia S.A (Brazil)	855	Consolidation and access to bank clients

One significant deal had no announced value – combination of Mitsui Sumitomo, Aioi Insurance and Nissay Dowa General in Japan. They merged for economies of scale in shrinking Japanese market.

Sources: Conning Research Consulting; Insurance Information Institute.

2010: Ten Largest U.S. Deals

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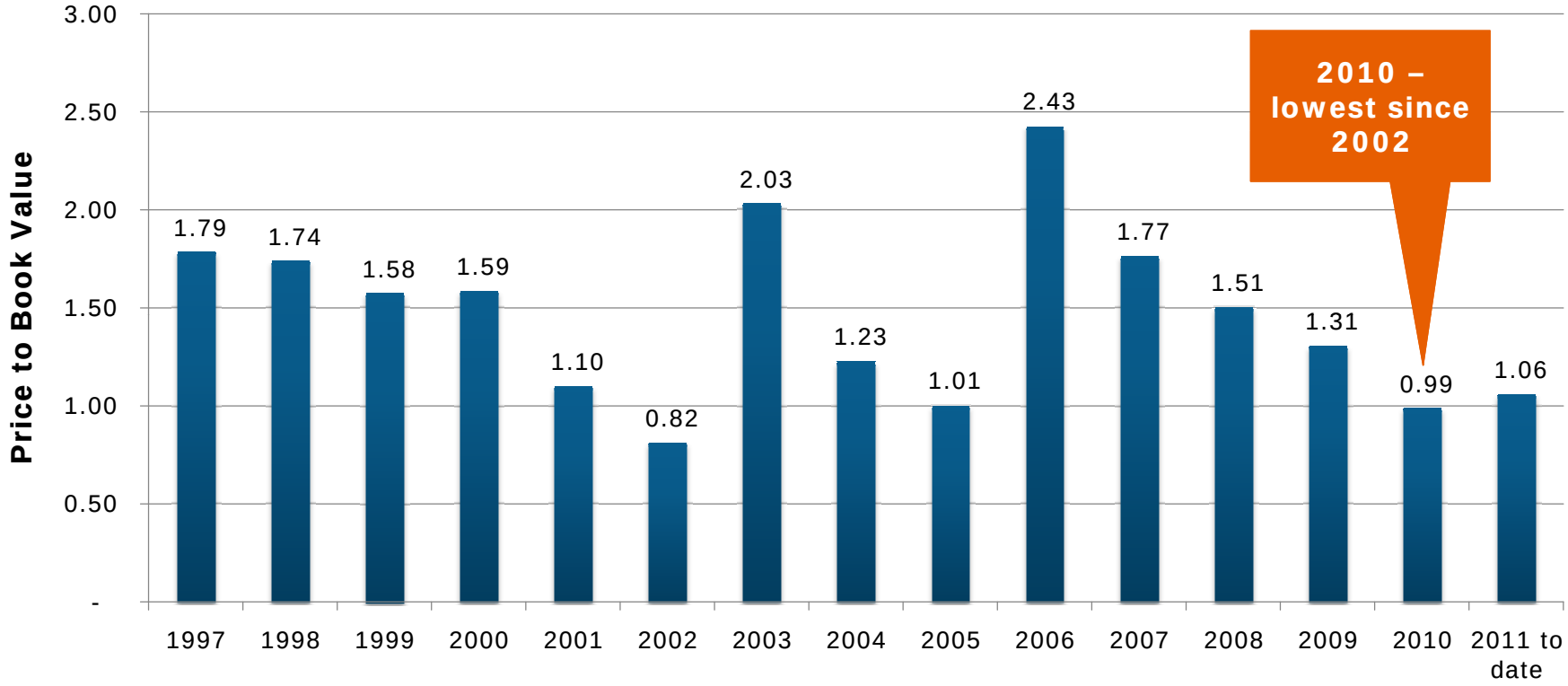
Merger & Acquisition	Approximate Value ($ millions)
Max Capital/Harbor Point	3,500
Fairfax Financial/Zenith National	1,300
Ace Ltd./Rain and Hail Insurance Services	1,100
QBE/NAU	565
Doctors Co./American Physicians Capital	386
Fairfax Financial/General Fidelity Insurance	328
Fairfax Financial/First Mercury Financial	294
QBE/RenaissanceRe U.S. operations	275
Southwest Insurance Partners/Lightyear Capital	250
ProSight Specialty Insurance/NYMAGIC	230

Mergers were a way to expand in preferred markets amid the slow growth post-recession. Acquirers generally had abundant capital. Terms and conditions for financing were advantageous.

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

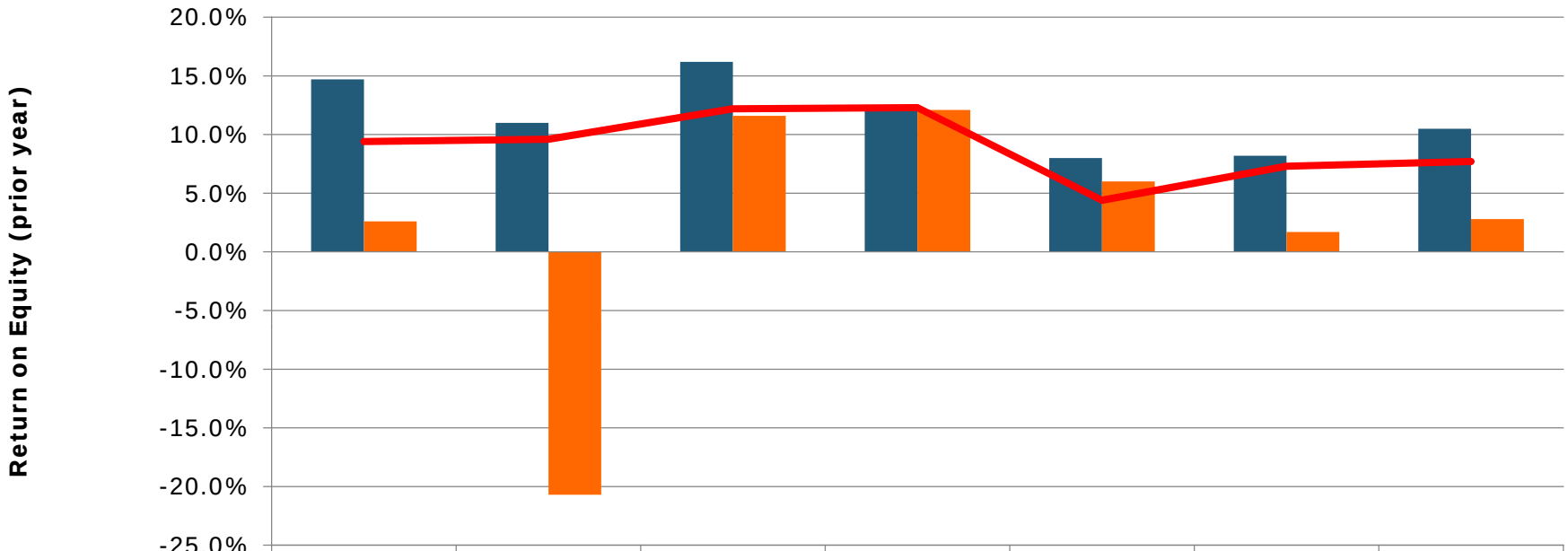
Valuations may have bottomed out



So far this year, 10 deals have been announced, worth nearly $2 billion.

Sources: SNL Financial; Insurance Information Institute.

Buyers are consistently more profitable than targets, rest of industry

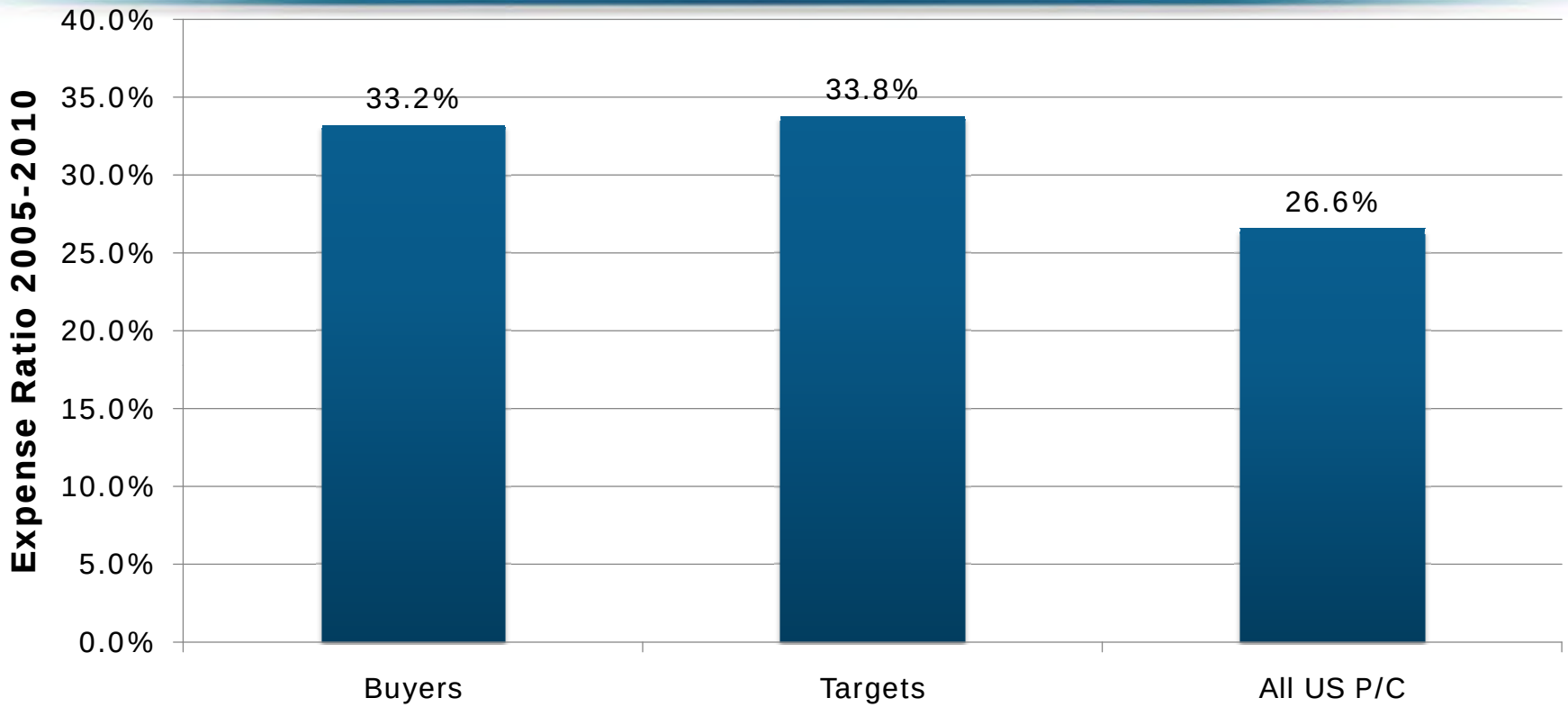


	2005	2006	2007	2008	2009	2010	2011 to date
Buyers	14.7%	11.0%	16.2%	12.0%	8.0%	8.2%	10.5%
Targets	2.6%	-20.7%	11.6%	12.1%	6.0%	1.7%	2.8%
US P/C Industry	9.4%	9.6%	12.2%	12.3%	4.4%	7.3%	7.7%

The year before merger, eventual targets have earnings that lag industry average. Buyers' earnings are higher than the industry.

Sources: SNL Financial; Insurance Information Institute.

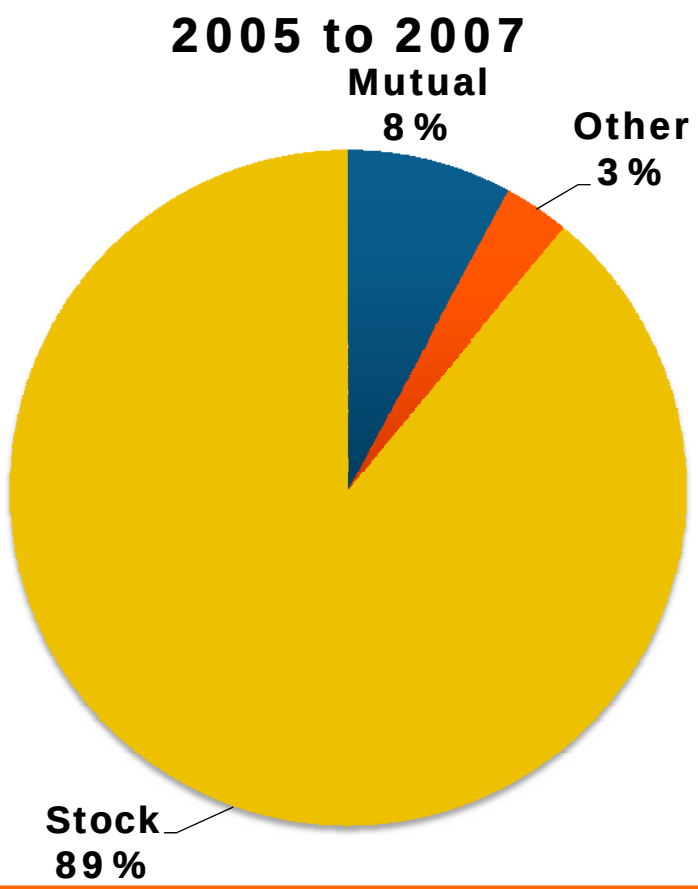
Firms on both sides of merger have higher expense ratios than industry

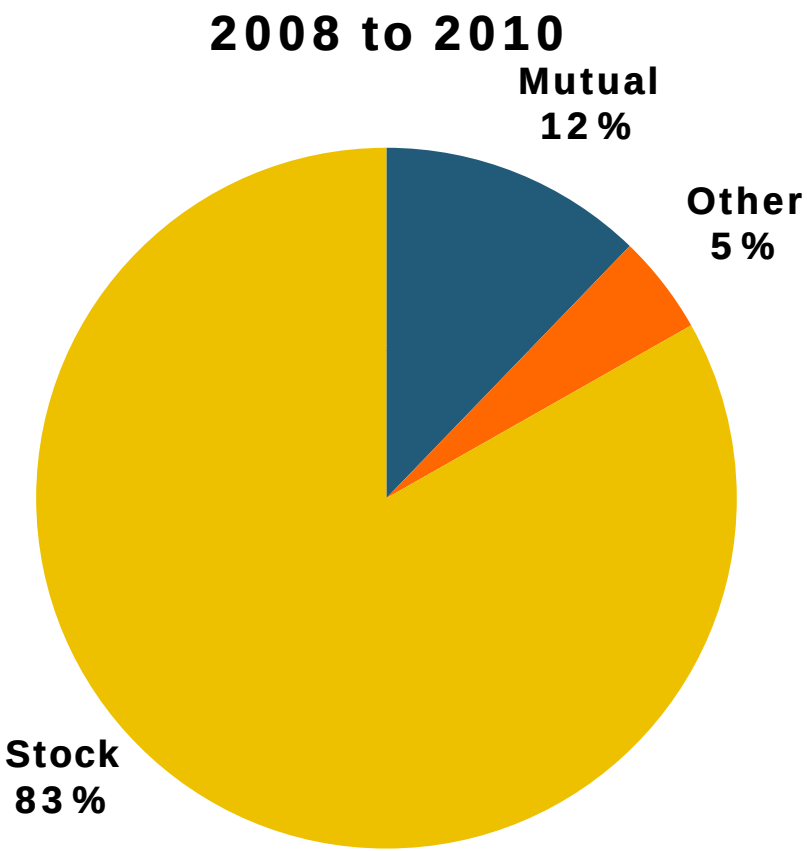


M&A targets have slightly higher expense ratios than buyers. Both run higher expense ratios than the industry overall.

Sources: SNL Financial; Insurance Information Institute.

Type of acquisition is shifting





There were 16 mutual targets in 2008-2010, up from 10 in the three prior years.

Sources: SNL Financial; Insurance Information Institute.

2010: Affiliations continue

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- NLC Insurance Cos./Hingham Mutual Fire
- Danbury Insurance/Casco Indemnity
- Texas Farm Bureau/Farm Bureau County Mutual (Texas)
- Cooperative Mutual (NE)/Austin Mutual
- Wisconsin America Mutual/Western National

Smaller (sometimes distressed) carriers affiliate with regionals or super-regionals.

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

2011 Forecast (A.M. Best)

- Activity to increase, especially among commercial lines
  - Slow economic growth, limited opportunities
  - Advantageous financing
  - Need to use capital more efficiently
- Possible obstacles
  - Low valuations deter sellers
  - Companies might prefer to wait out soft market

Looking Ahead

- Smaller scale M&A is more likely than “mega deals”
  - Stock valuations remain low
  - Number of actual acquirers and targets is limited
  - Biggest growth opportunities are abroad/life sector
- Incentives for Smaller Size Firms to Merge
  - Economies of scale
  - Inability to make necessary investments in technology
  - Key markets hit hard by economic downturn (e.g., small commercial, contractors, construction, etc.)
  - Poor financials
  - Capital issues

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Secondary Considerations
OPERATING ENVIRONMENT
REGULATORY ENVIRONMENT

Many Other Factors Influence P/C Insurer Profitability

Shifting Legal Liability & Tort Environment

Is the Tort Pendulum Swinging Against Insurers?

Important Issues & Threats Facing Insurers: 2011–2015

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Emerging Tort Threat

- No tort reform (or protection of recent reforms) is forthcoming from the current Congress or Administration
- Erosion of recent reforms has already occurred
- Legislative initiatives in 2009/10 were tort friendly
- New Congress will have tempering effect on what could have been tort disaster
- Torts twice the overall rate of inflation
- Influence personal and commercial lines, esp. auto liability
- Historically ***extremely*** costly to p/c insurance industry
- Leads to reserve deficiency, rate pressure

Bottom Line: **Tort "crisis" is less likely from rapid deterioration in the tort system overall, but costs still remain entrenched in the system**

Source: Insurance Information Institute

Cost of US Tort System ($ Billions)

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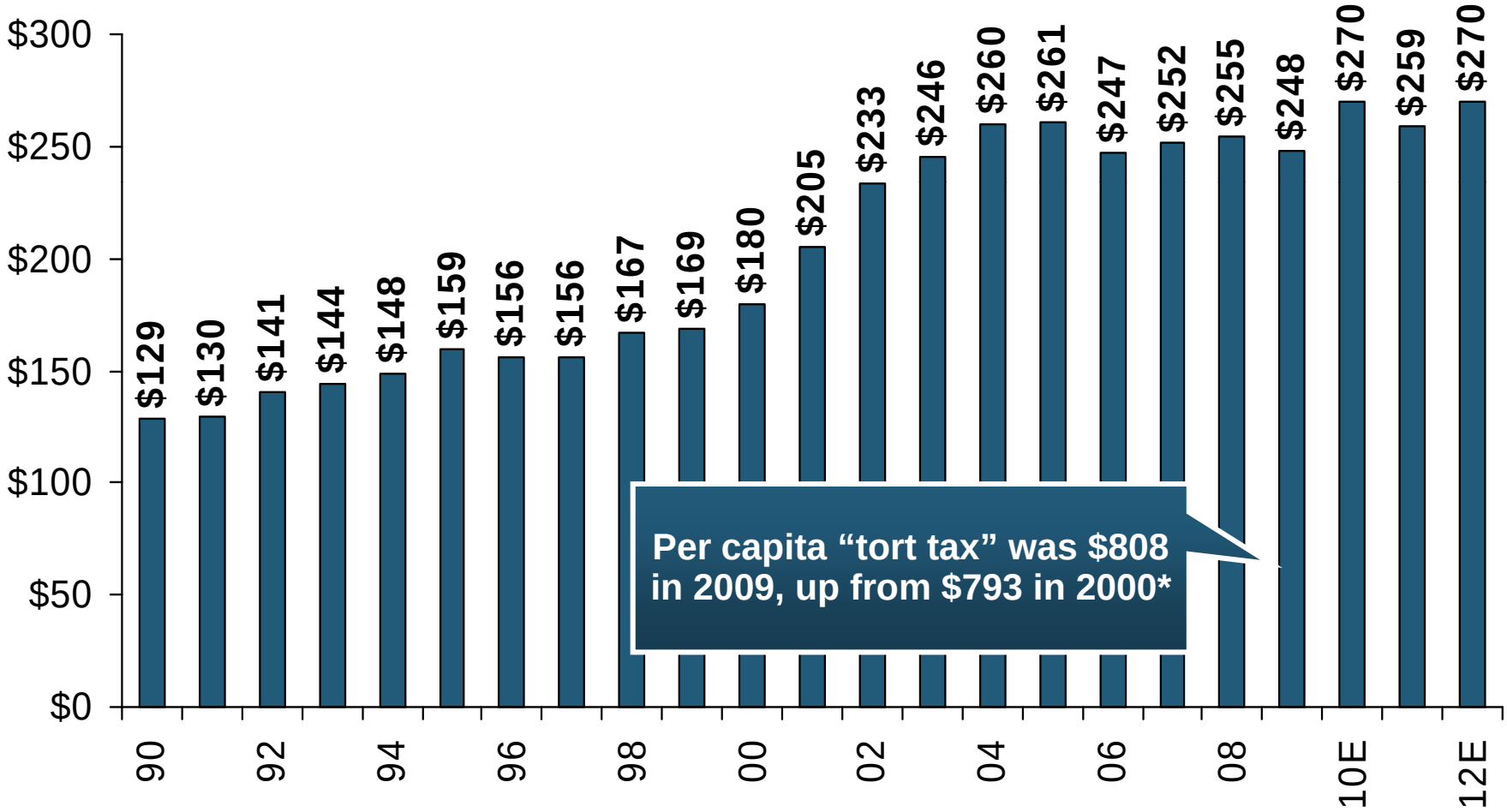
Tort costs consumed 1.74% of GDP in 2009, down from 2.21% in 2003



* Restated in 2009 dollars, based on CPI.

Source: Towers Watson, *2010 Update on US Tort Cost Trends.*

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

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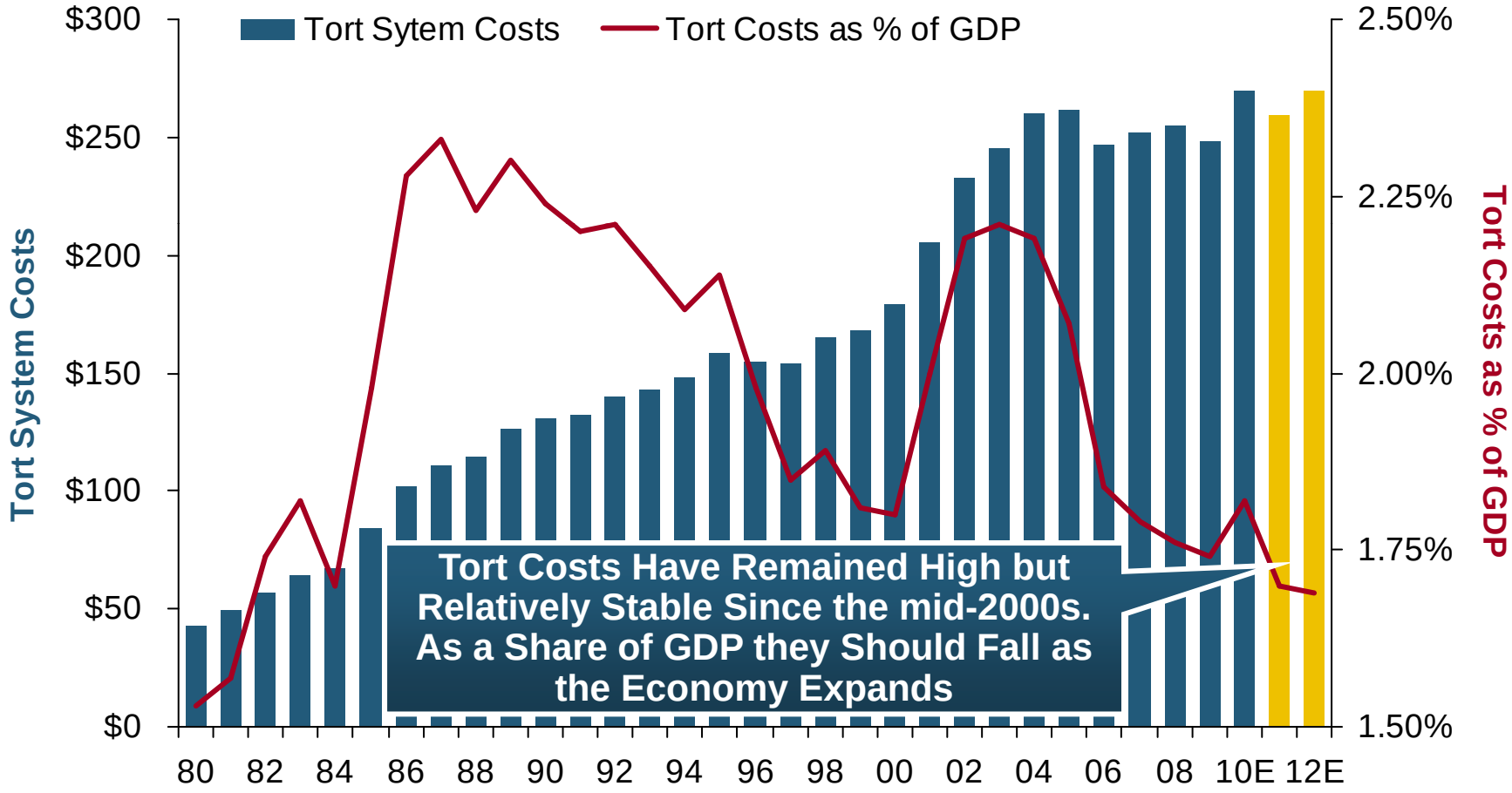
($ Billions)



Sources: Towers Watson, *2010 Update on US Tort Cost Trends*, Appendix 1A

Trial Bar Priorities

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

Source: Institute for Legal Reform.

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

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

41 different practice areas were included as categories

Source: Institute for Legal Reform poll, December 2009.

Business Leaders Ranking of Liability Systems in 2010

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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

Source: US Chamber of Commerce 2010 State Liability Systems Ranking Study; Insurance Info. Institute.

The Nation's Judicial Hellholes: 2010

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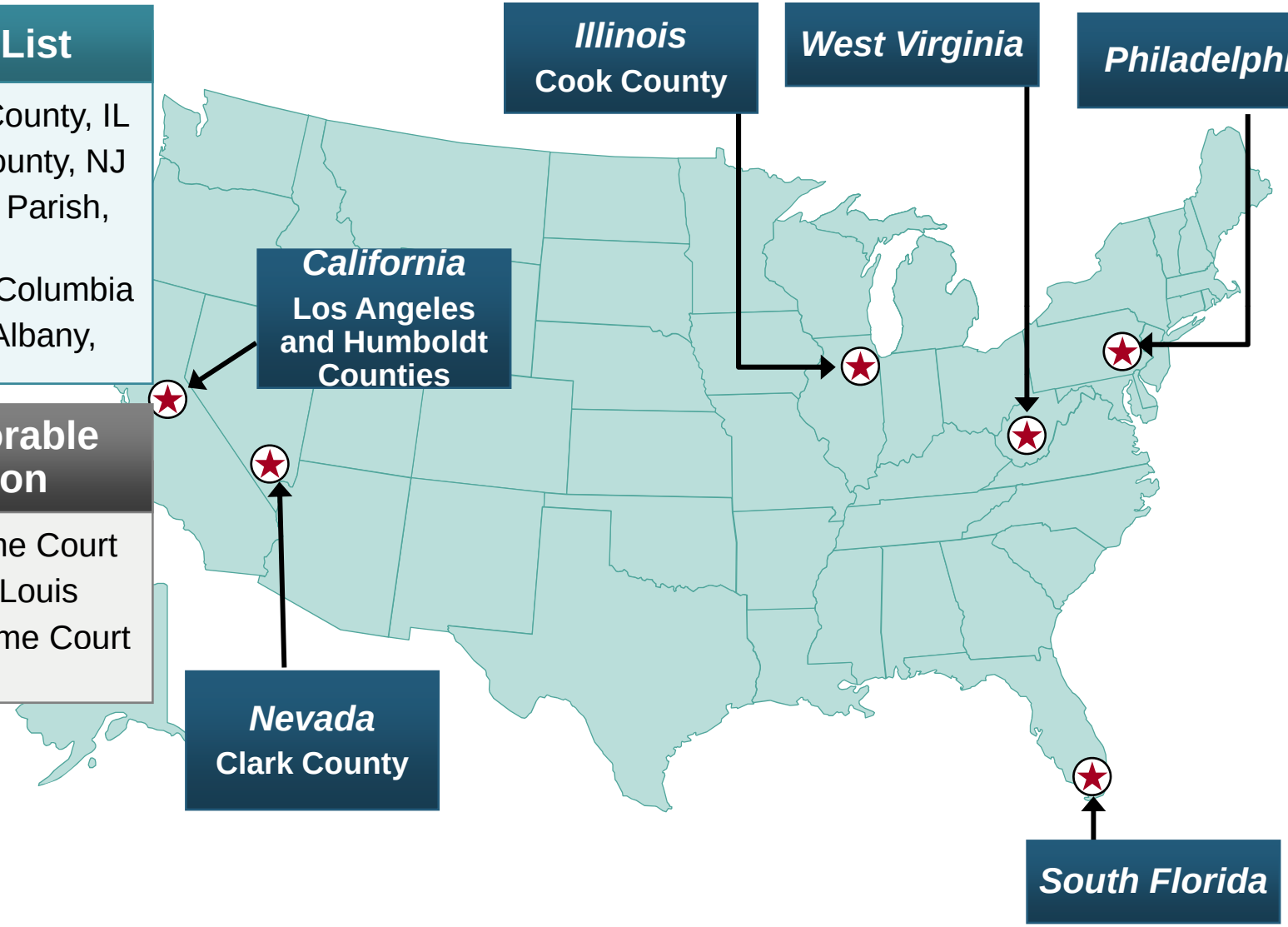
Watch List

- Madison County, IL
- Atlantic County, NJ
- St. Landry Parish, LA
- District of Columbia
- NYC and Albany, NY

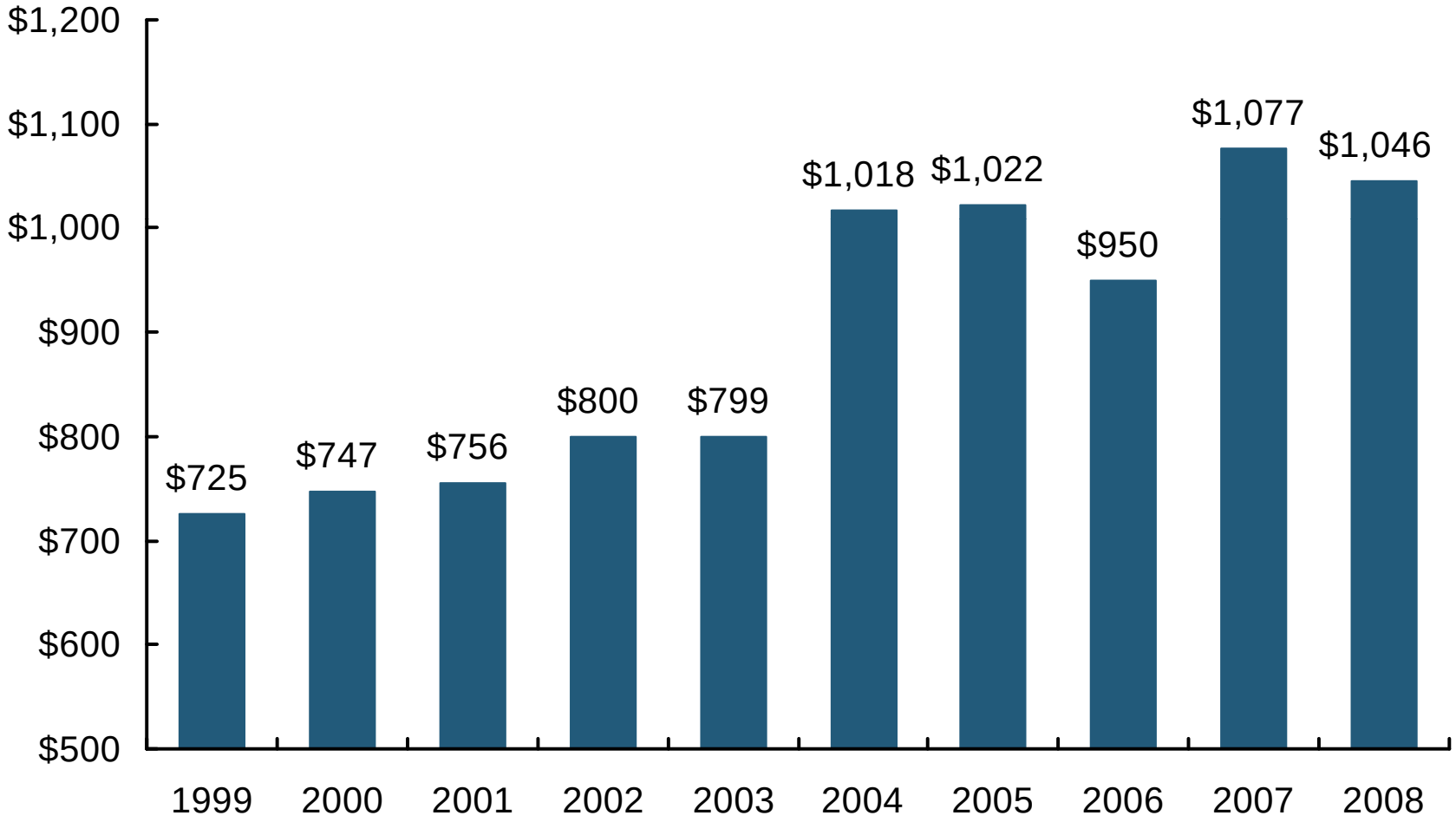
Dishonorable Mention

- MI Supreme Court
- City of St. Louis
- CO Supreme Court



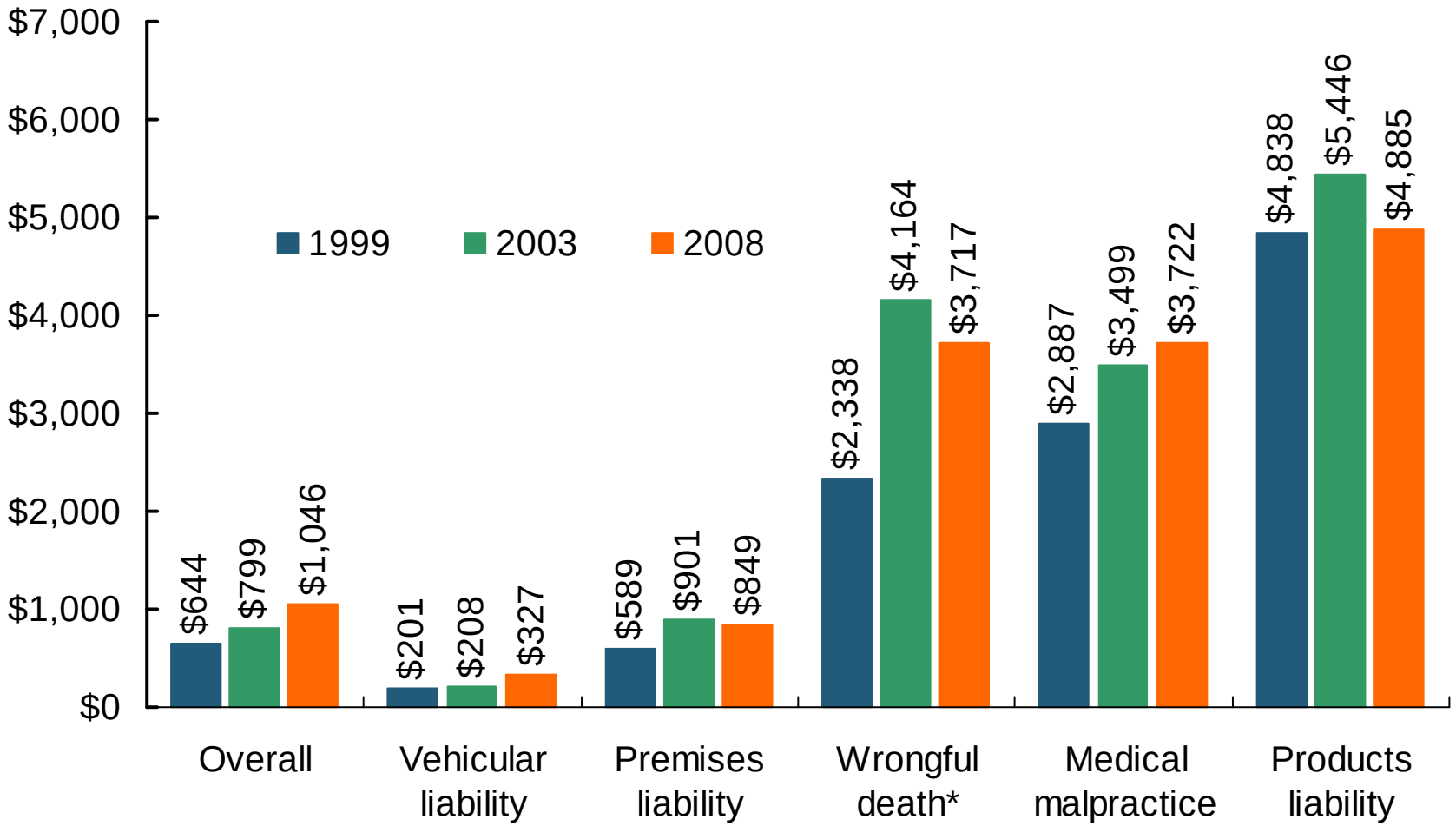
Source: American Tort Reform Association; Insurance Information Institute

Average Jury Awards 1999 - 2008



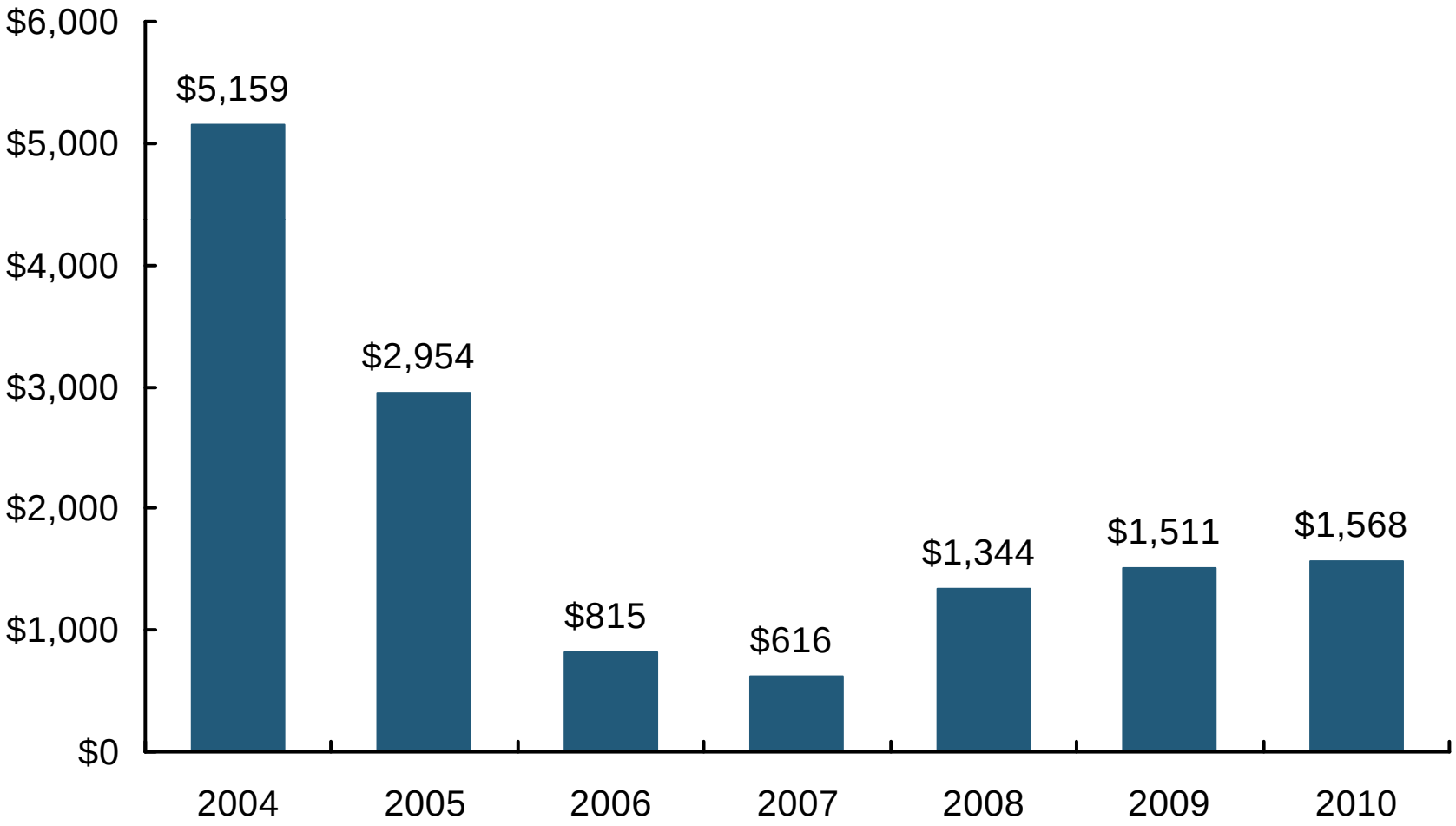
Source: Jury Verdict Research; Insurance Information Institute.

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.

2010 Top Ten Jury Verdicts

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Value	Issue	State
$505.1 Million	Products Liability	Nevada
$208.8 Million	Personal Injury (Asbestos/Mesothelioma case)	California
$152 Million	Wrongful Death (Tobacco verdict)	Massachusetts
$132.5 Million	Personal Injury (Ford rollover retrial)	Mississippi
$124.5 Million	Personal Injury (Passenger van rollover case)	Texas
$103 Million	Legal Malpractice/Breach of Fiduciary Duty	Mississippi
$90.8 Million	Products Liability, Wrongful Death (Tobacco verdict)	Florida
$89 Million	Personal Injury, Products Liability	Pennsylvania
$82.5 Million	Wrongful Death	Texas
$80 Million	Wrongful Death (Tobacco verdict)	Florida

Source: Lawyers USA, January 18, 2011.

2009 Top Ten Jury Verdicts

INSURANCE INFORMATION INSTITUTE

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

Source: Lawyers USA, January 15, 2010.

2008 Top Ten Jury Verdicts

INSURANCE INFORMATION INSTITUTE

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

Source: Lawyers USA, January 13, 2009.

Medical Malpractice Tort Cost: Growth Continues, Though Modestly

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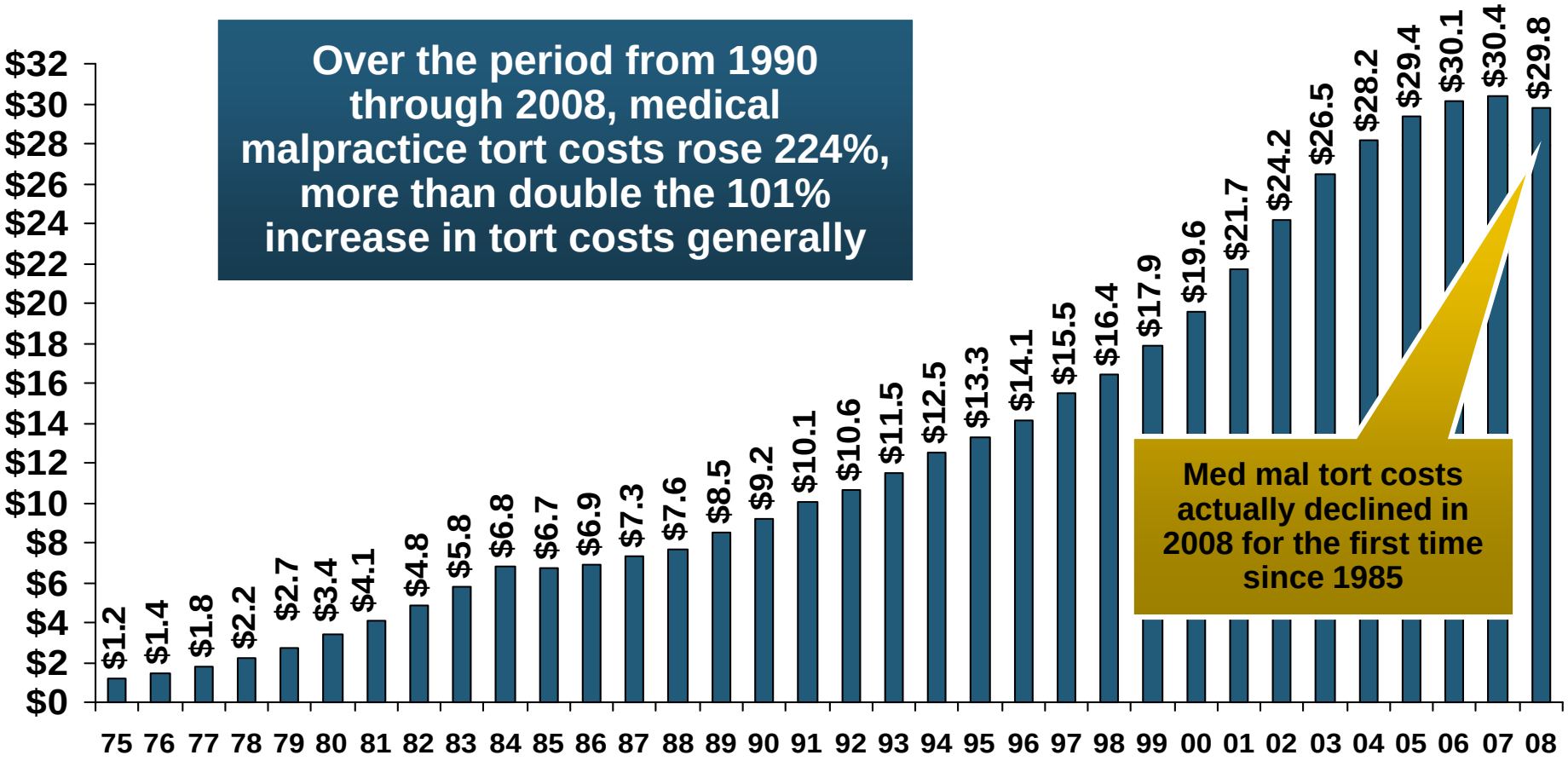
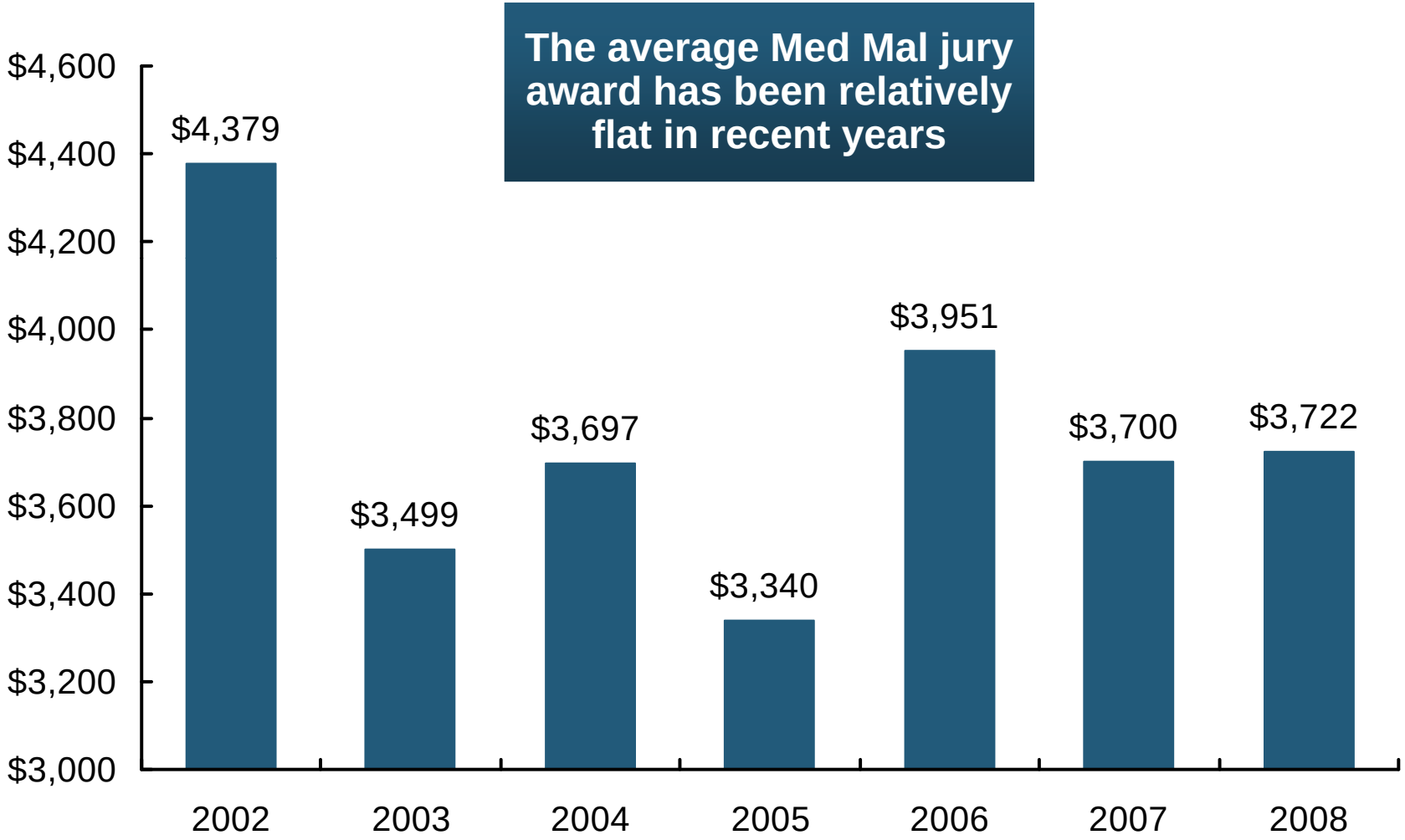
($ Billions)



Sources: Towers Perrin; Insurance Information Institute

Average Medical Malpractice Jury Award: 2002 - 2008



Source: Jury Verdict Research; Insurance Information Institute.

How the Risk Dollar is Spent (2009)

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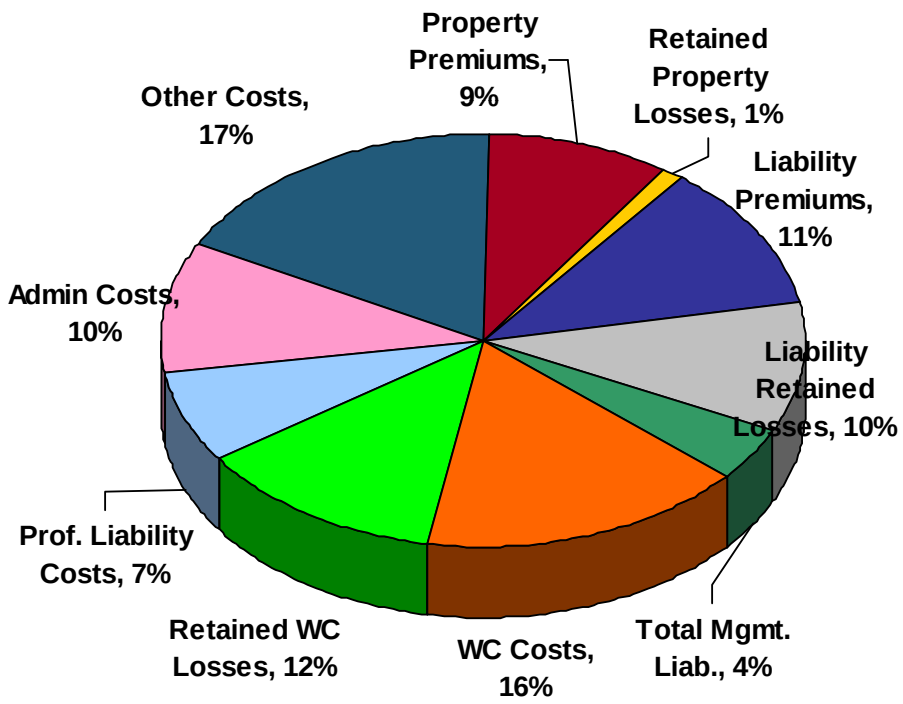
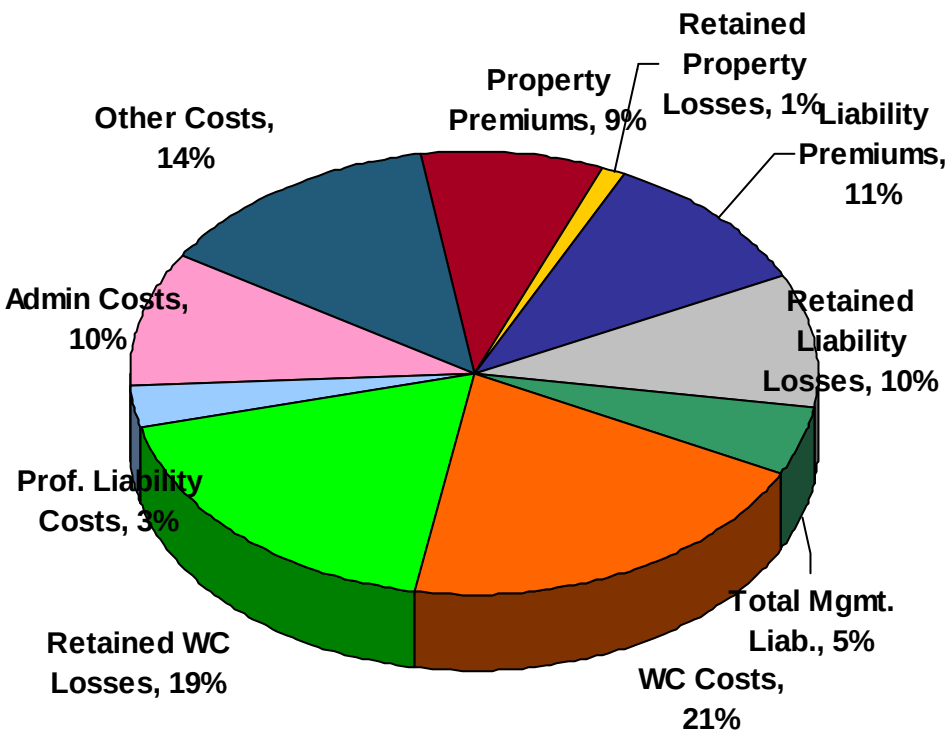
Total liability costs account for about 30% of the risk dollar

Firms w/Revenues < $1 Billion

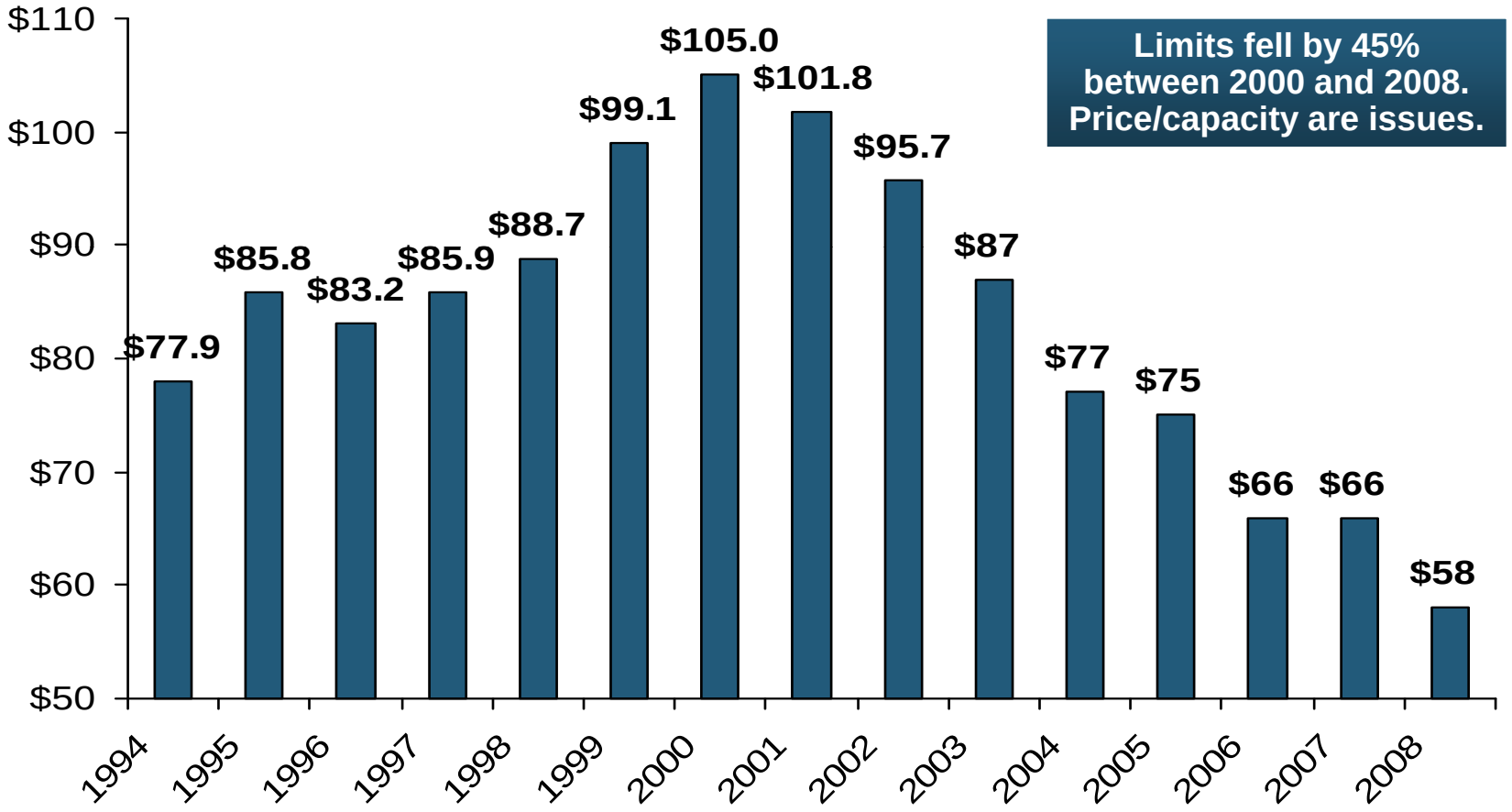


Firms w/Revenues > $1 Billion



Source: 2010 RIMS Benchmark Survey; Insurance Information Institute

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



*Includes underlying primary limits
Source: *Limits of Liability 2008,* Marsh, Inc.

Excess Liability Market Capacity North America ($ Billions)

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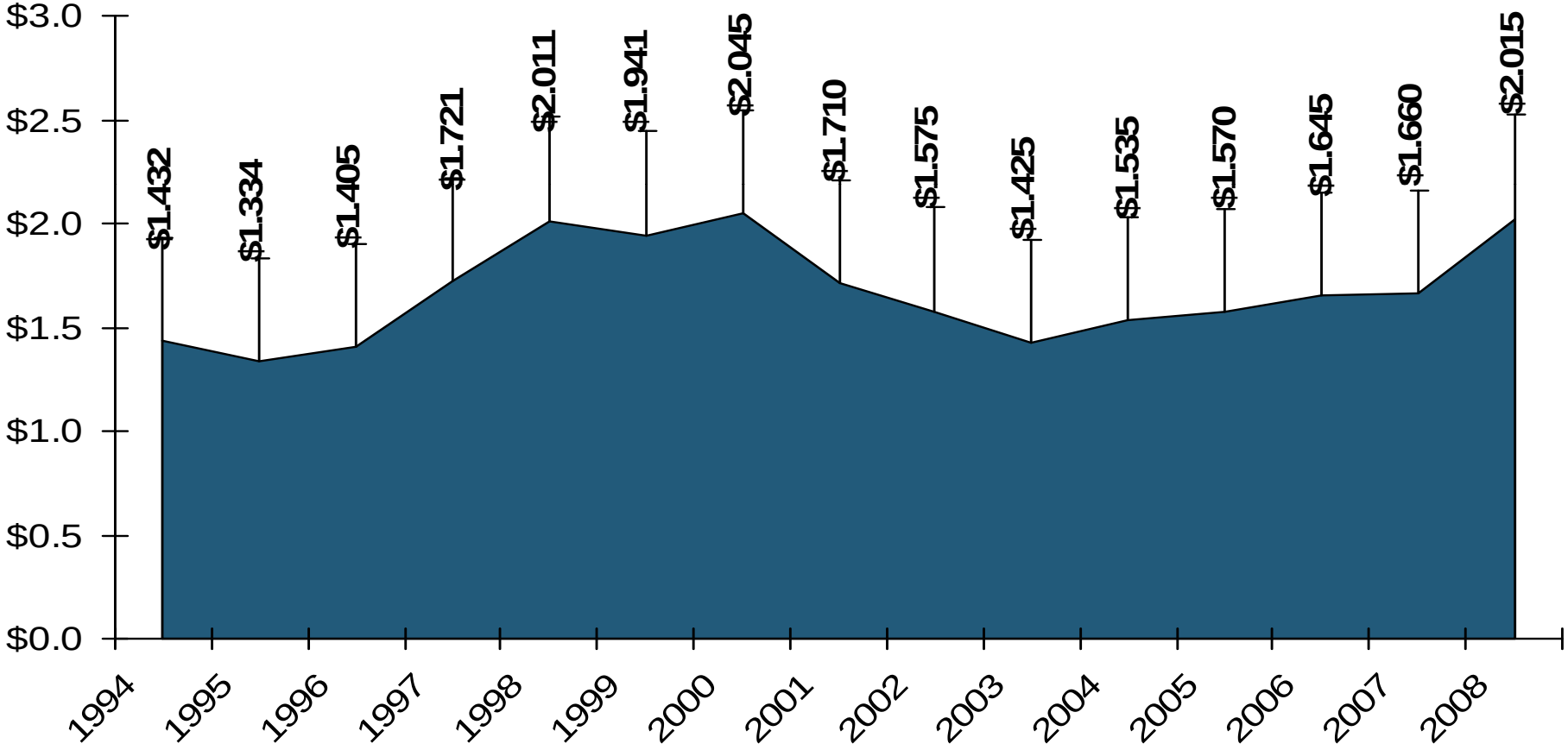
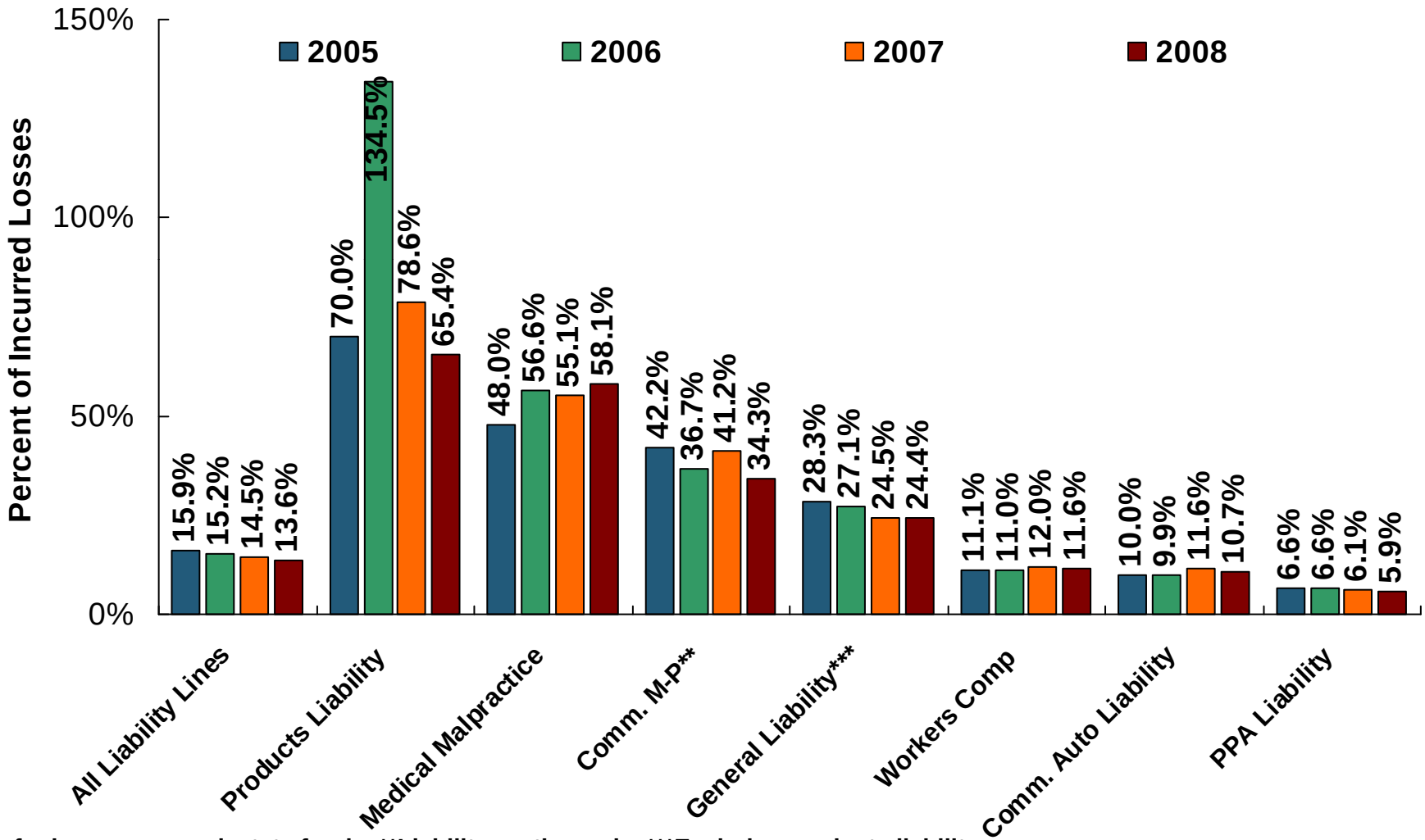
In 2008, capacity is back to 2000 levels.



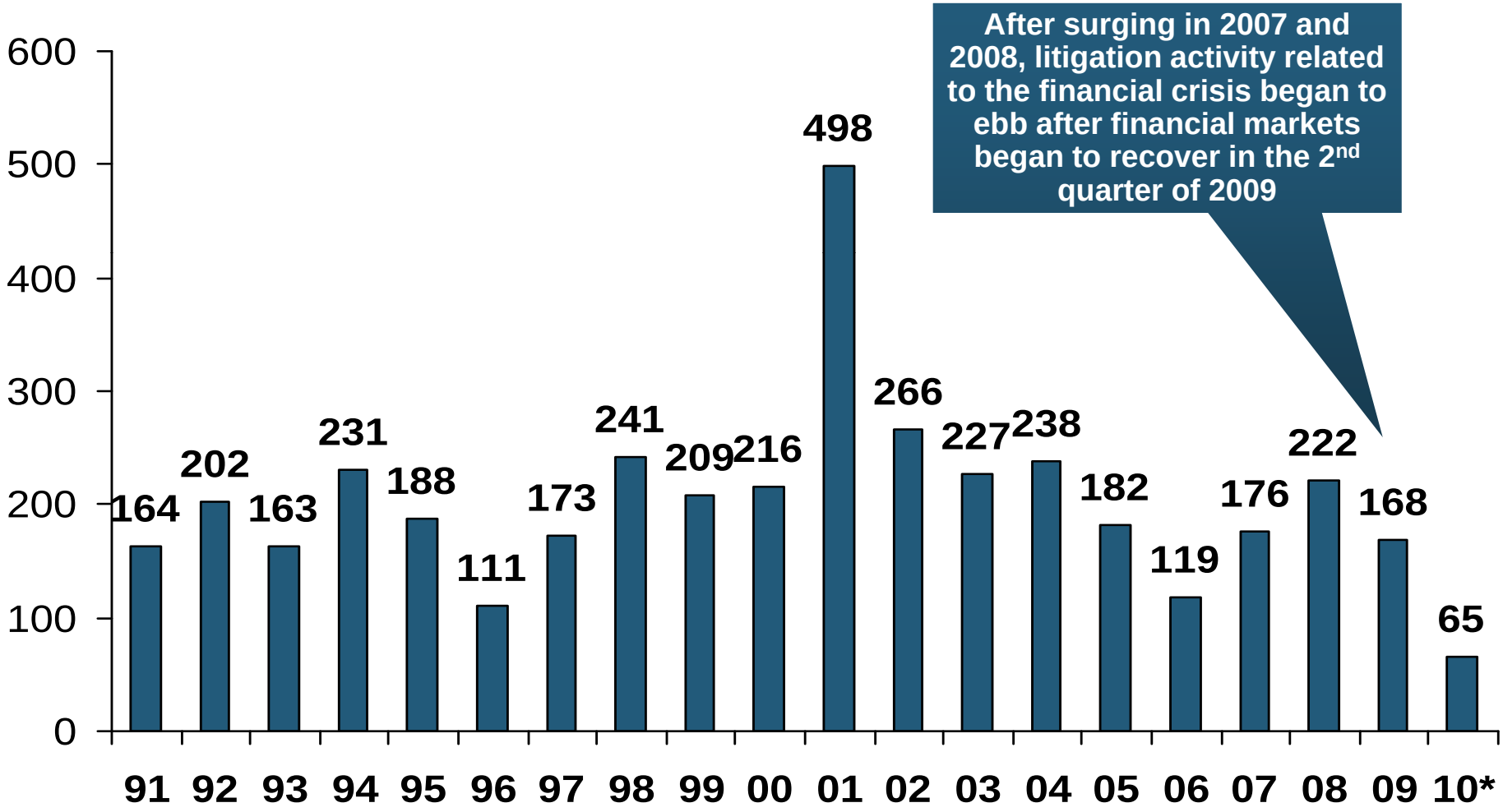
Source: Marsh, 2008 Limits of Liability Report

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



*Net of reinsurance, excl. state funds. **Liability portion only. ***Excludes products liability.
Source: National Association of Insurance Commissioners (NAIC) Annual Statement Database, via Highline Data, LLC; Insurance Information Institute.

Shareholder Class Action Lawsuits*



*Securities fraud suits filed in U.S. federal courts as of June 25, 2010.
Source: Stanford University School of Law (securities.stanford.edu); Insurance Information Institute

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

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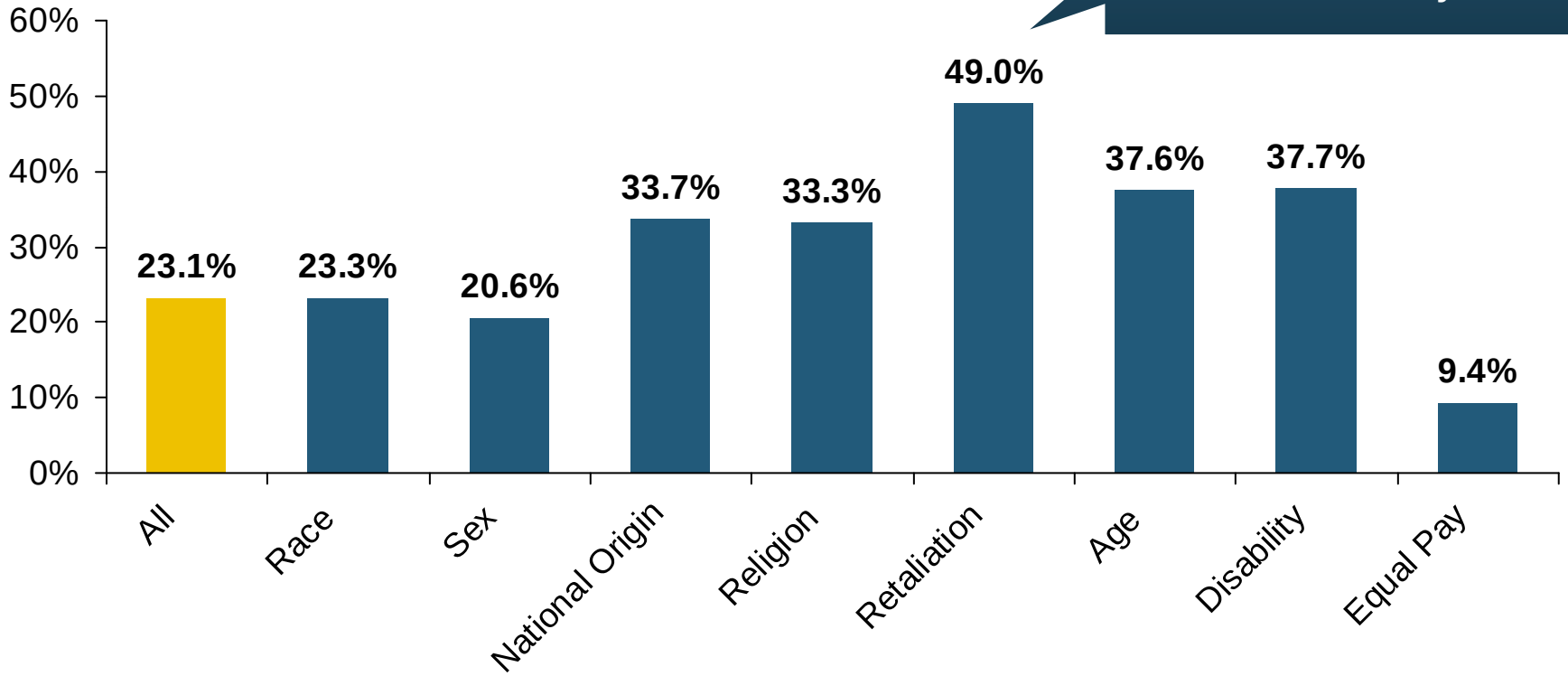
Change in Charges Filed (%)

Retaliation and age discrimination suits are up substantially



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

Source: Equal Opportunity Employment Commission; Insurance Information Institute.

Inflation

Is it a Threat to Claim Cost Severities

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

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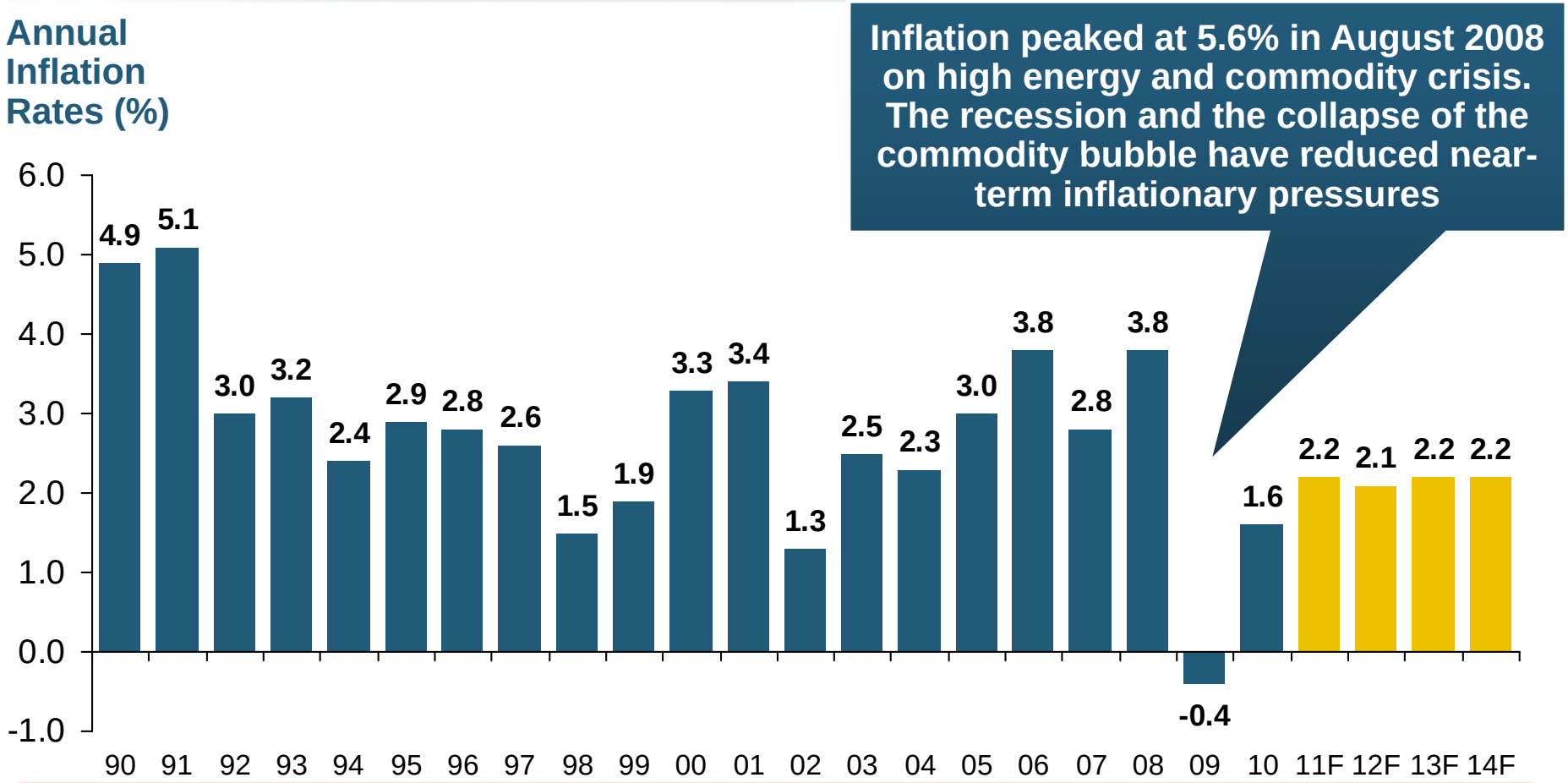
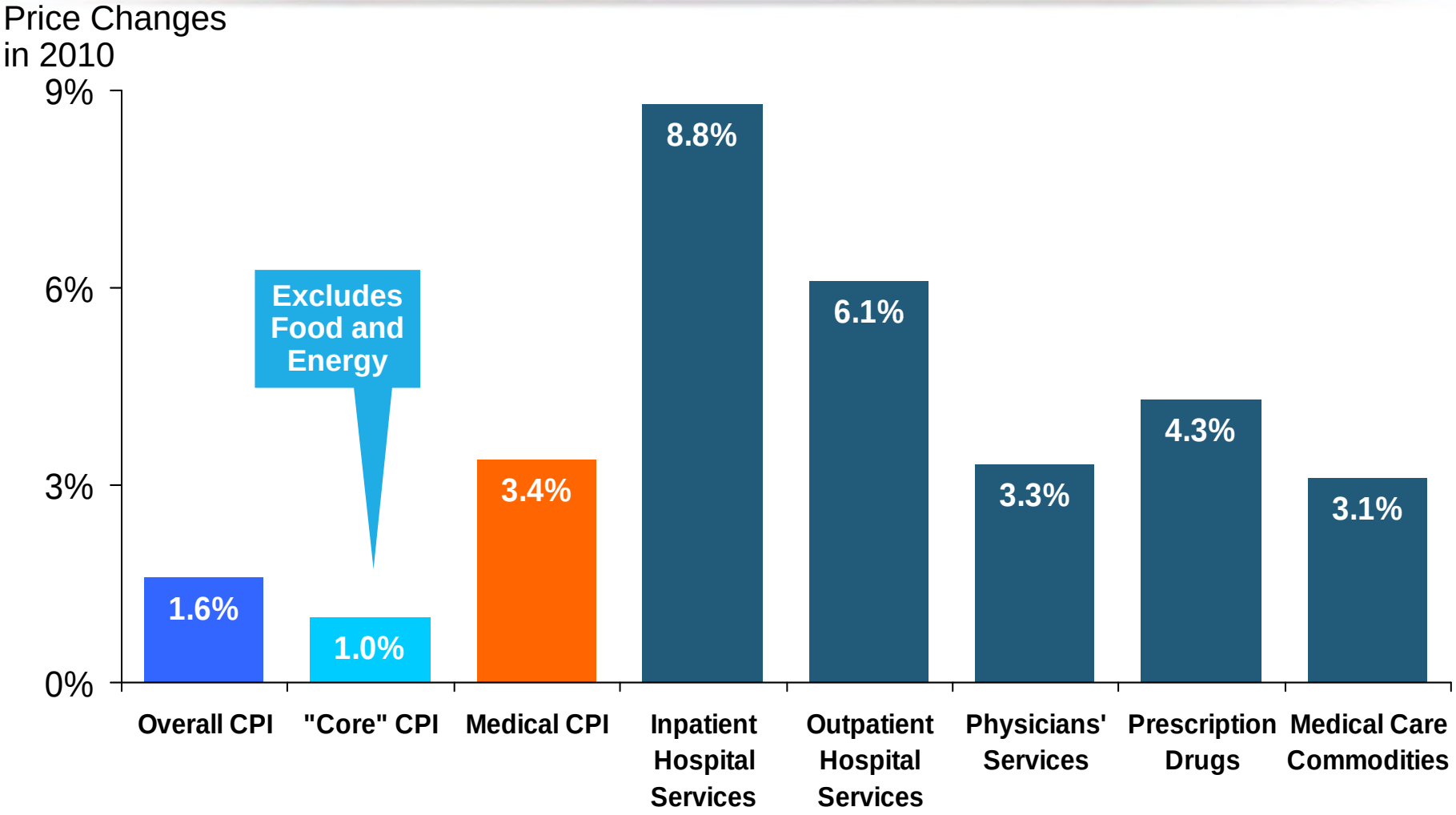


The slack in the U.S. economy suggests that inflation should not heat up before 2012, but other forces (commodity prices, inflation in countries from which we import, etc.), plus U.S. debt burden, remain longer-run concerns

Sources: US Bureau of Labor Statistics; Blue Chip Economic Indicators, 10/10 and 3/11 (forecasts).

P/C Insurance Claim Cost Drivers Grow Faster than even the Medical CPI Suggests



Healthcare costs are a major liability, med pay, and PIP claim cost driver. They are likely to grow faster than the CPI for the next few years, at least

Source: Bureau of Labor Statistics; Insurance Information Institute.

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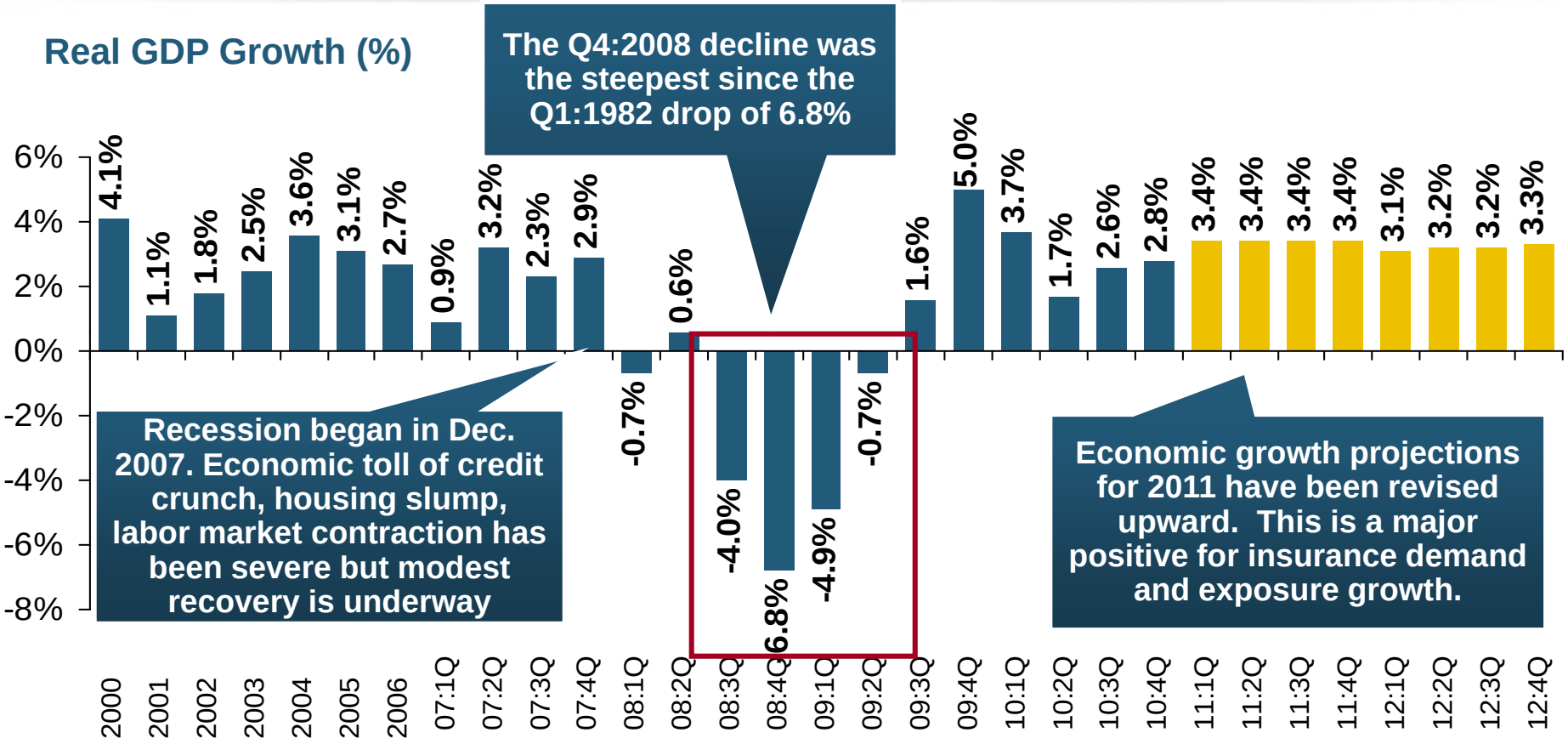
Economic Issues for the Next 3-5 Years

Growth in the Wake of the "Great Recession"

US 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 3/11; Insurance Information Institute.

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

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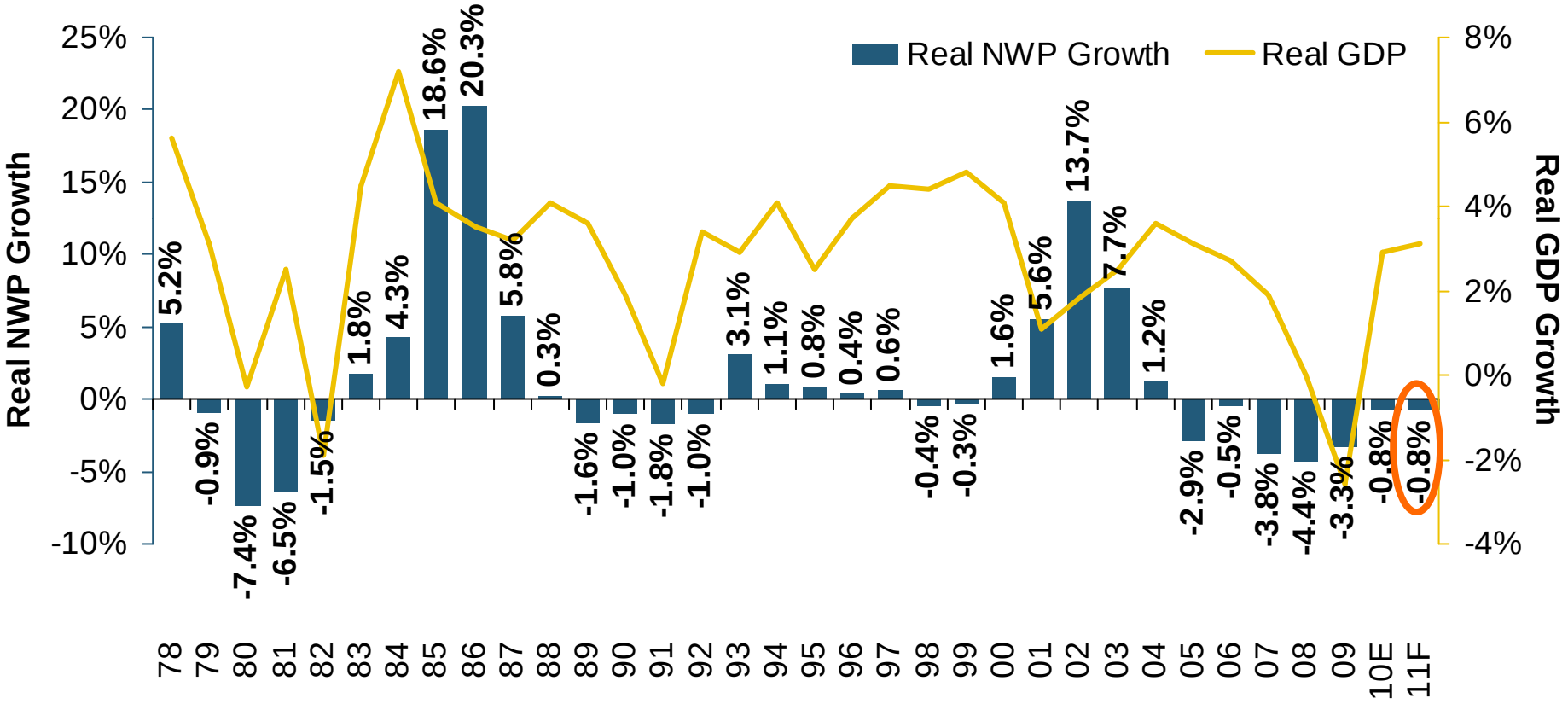
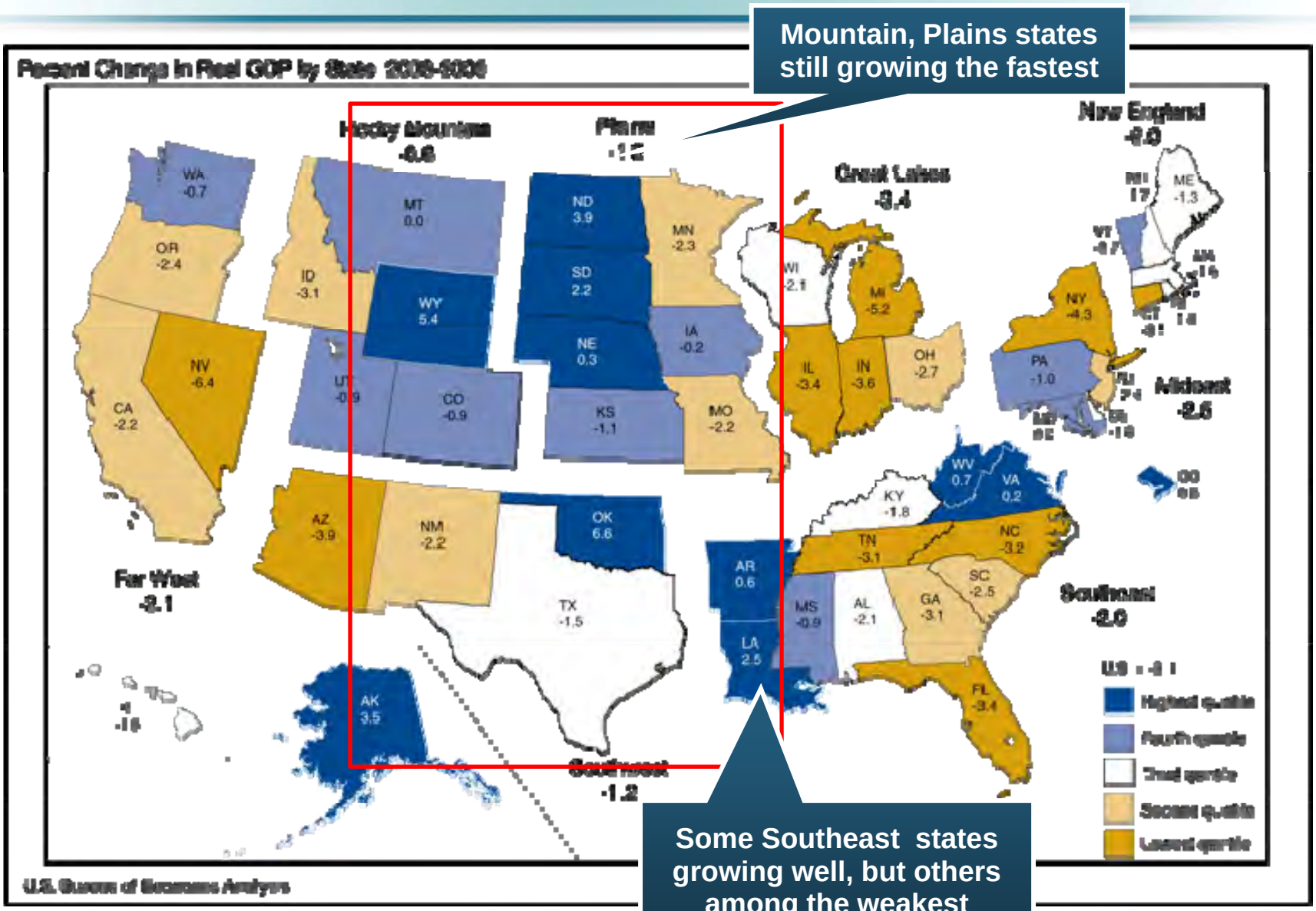
Real GDP Growth vs. Real P/C (%)



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

Sources: A.M. Best, US Bureau of Economic Analysis, Blue Chip Economic Indicators, 3/11; Insurance Information Institute

2011 Financial Overview
State Economic Growth Varied in 2009



Some Southeast states growing well, but others among the weakest

Direct Premiums Written: All Lines Percent Change by State, 2004-2009

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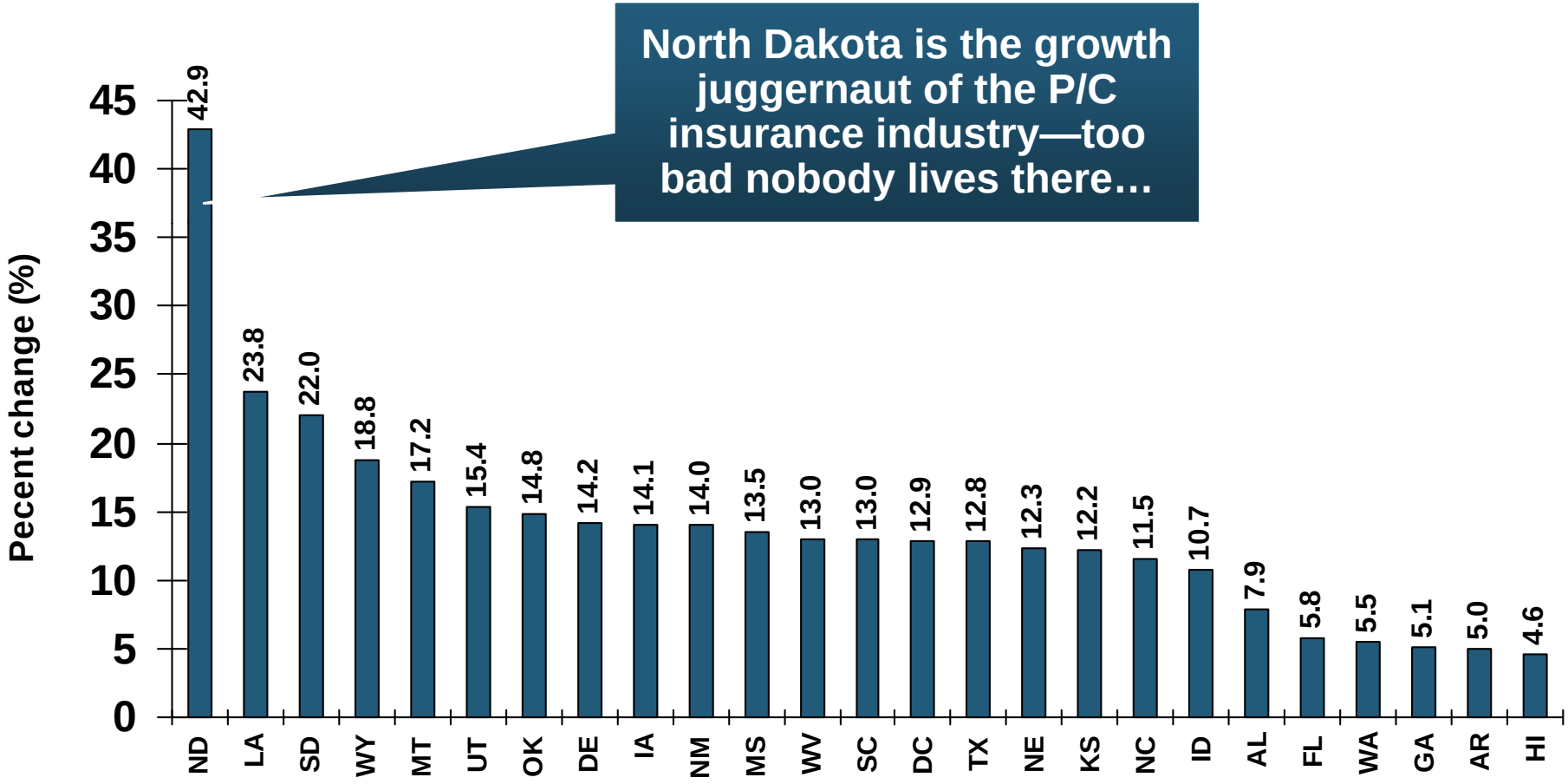
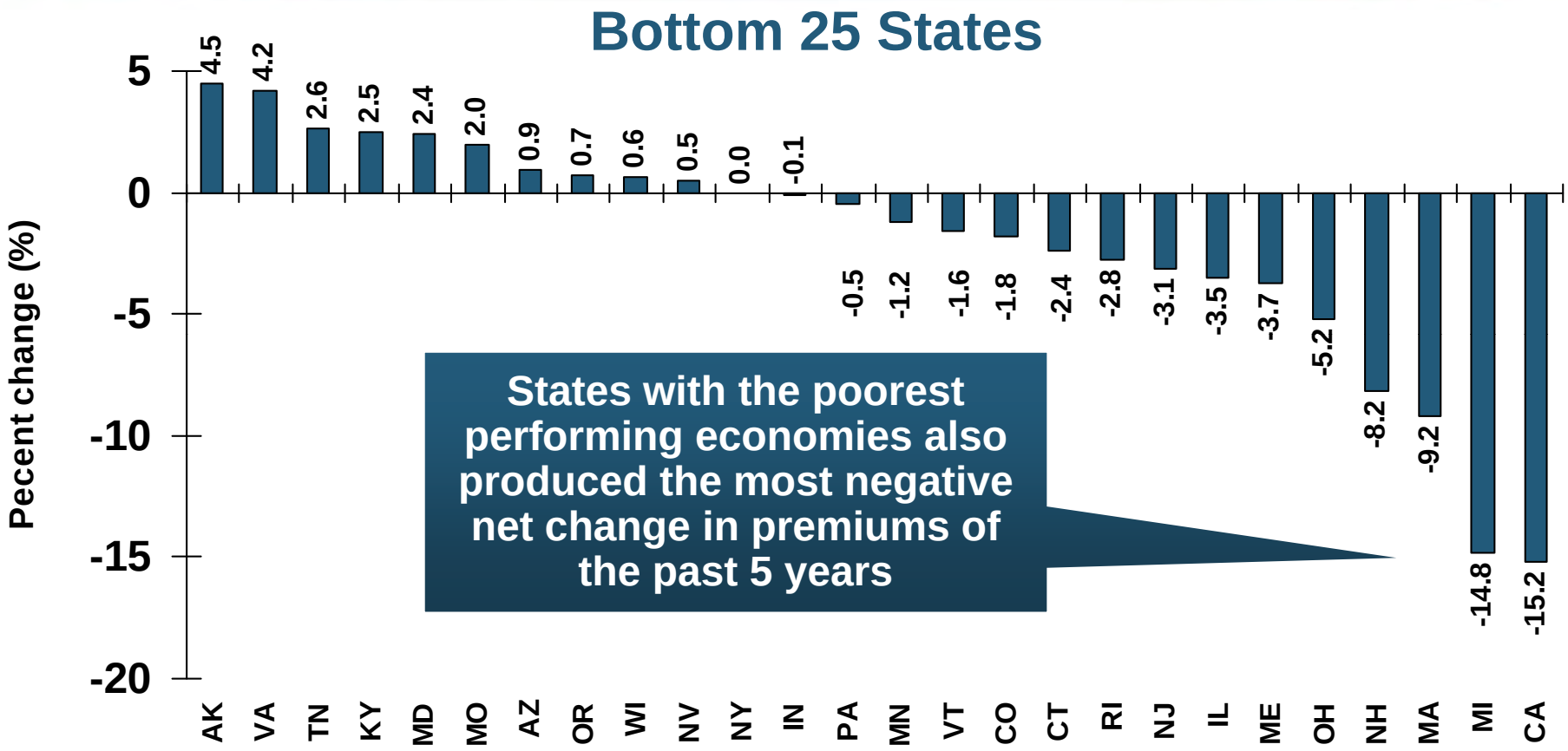
Top 25 States



Sources: SNL Financial LC.; Insurance Information Institute.

Direct Premiums Written: All Lines Percent Change by State, 2004-2009



Over the 5 years from 2004-2009, 15 states saw premiums *shrink*, one had no growth, and 4 others grew premiums by less than 1%

Sources: SNL Financial LC; Insurance Information Institute.

11 Industries for the Next 10 Years: Insurance Solutions Needed

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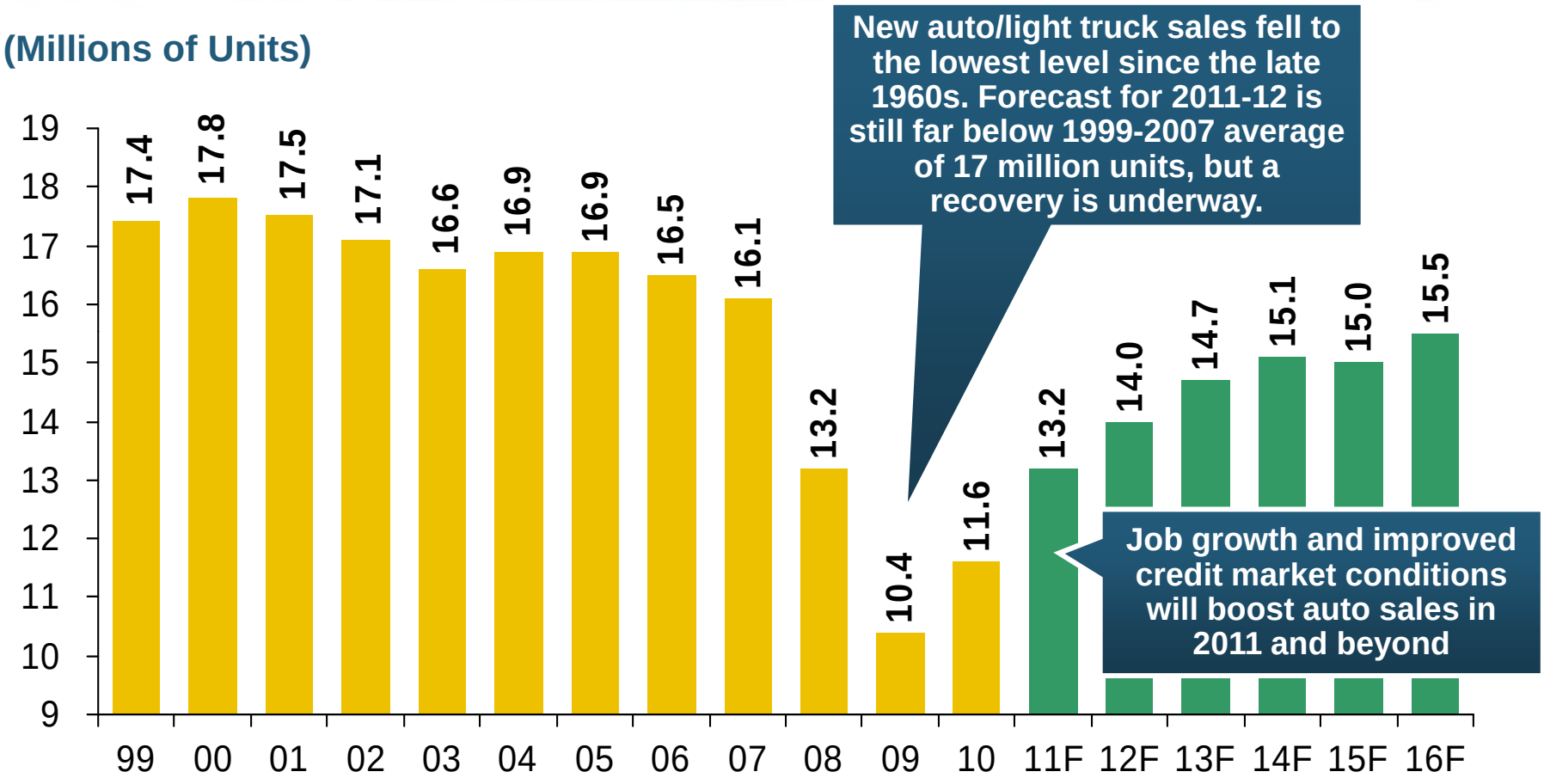
- Health Care
- Health Sciences
- Energy (Traditional)
- Alternative Energy
- Agriculture
- Natural Resources
- Environmental
- Technology (incl. Biotechnology)
- Light Manufacturing
- Export-Oriented Industries
- Shipping (Rail, Marine)

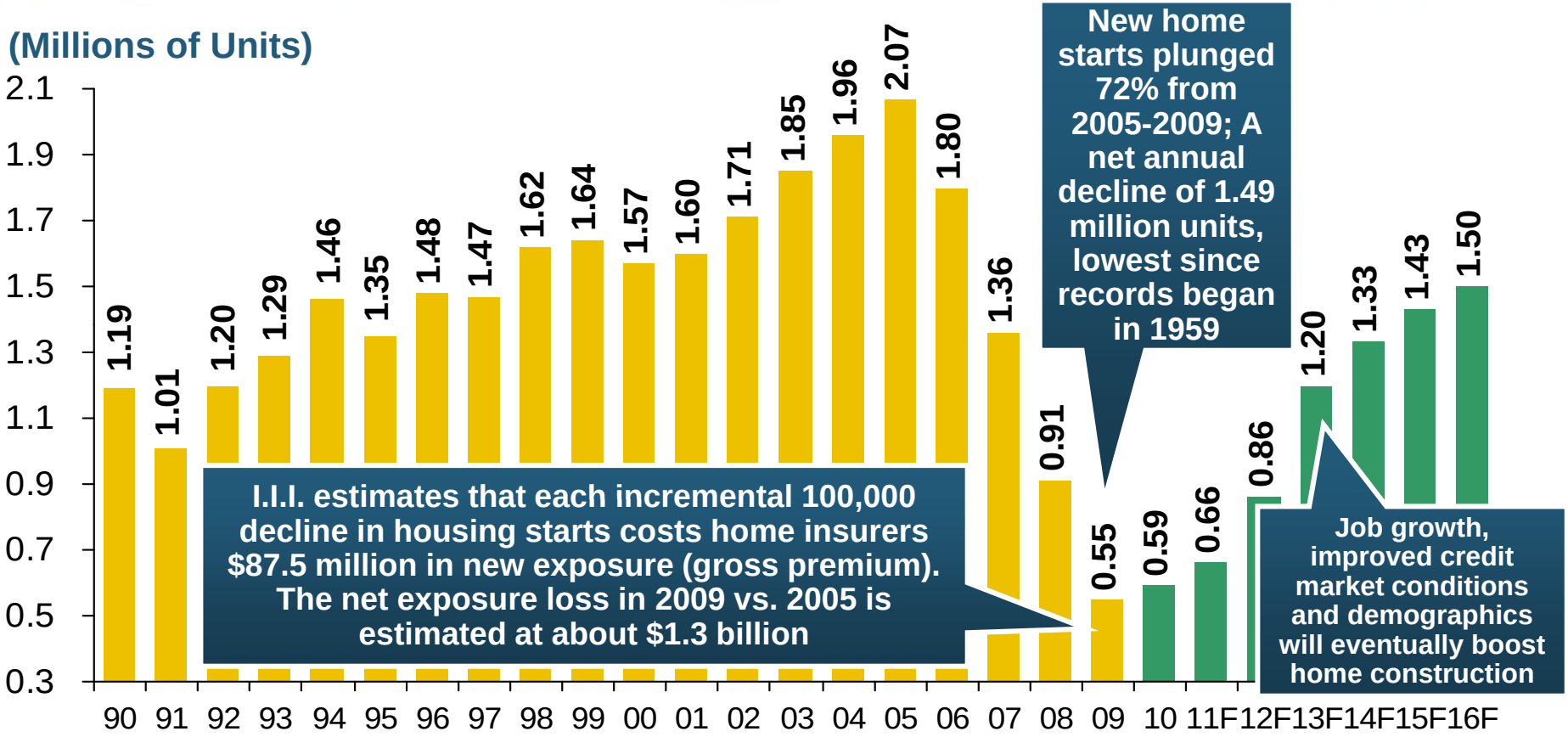
Auto/Light Truck Sales, 1999-2016F



Car/Light Truck Sales Will Continue to Recover from the 2009 Low Point, but High Unemployment, Tight Credit Are Still Restraining Sales in 2011

Source: U.S. Department of Commerce; Blue Chip Economic Indicators (10/10 and 3/11); Insurance Information Institute.

New Private Housing Starts, 1990-2016F

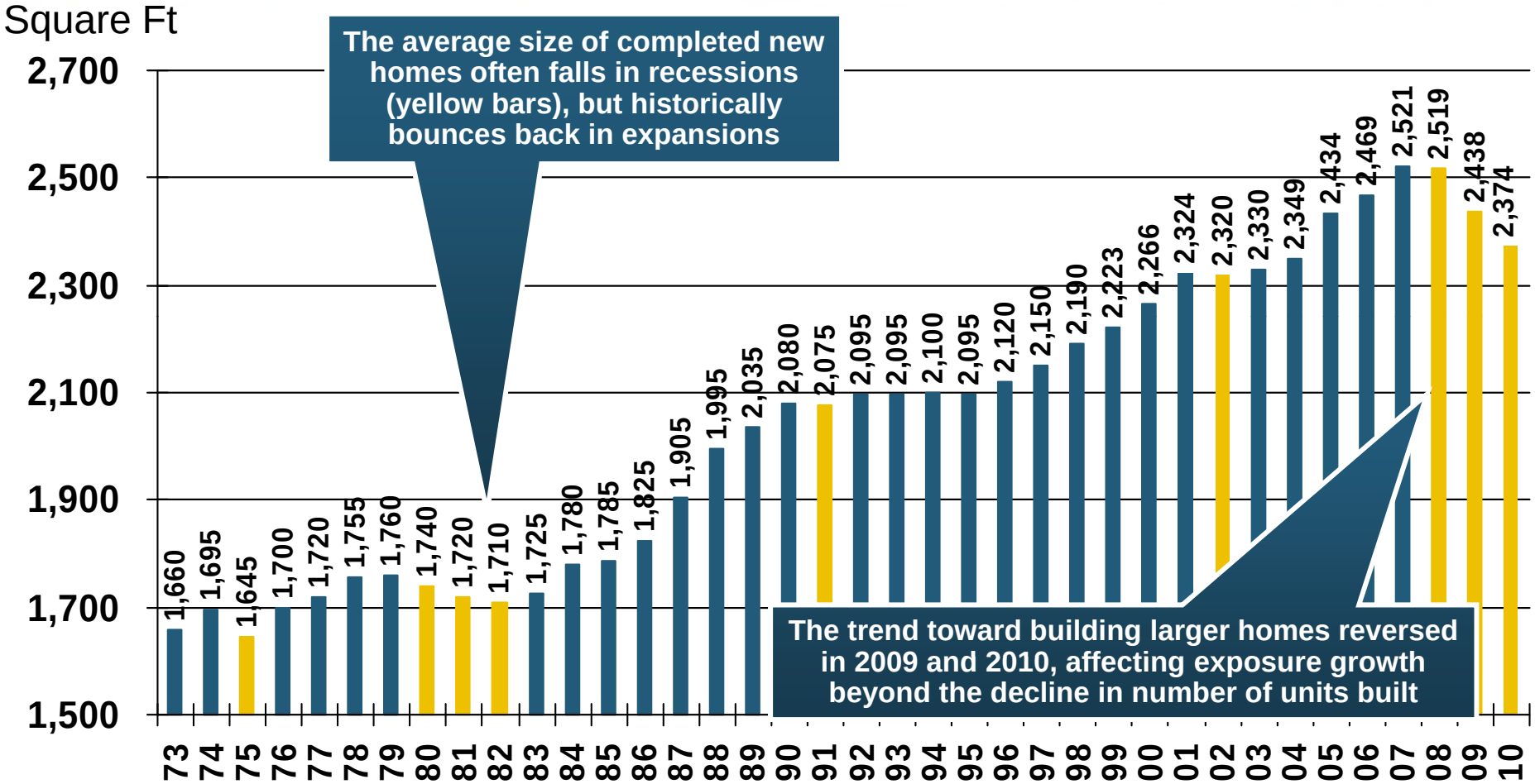


Little Exposure Growth Likely for Homeowners Insurers Until 2013. Also Affects Commercial Insurers with Construction Risk Exposure, Surety

Source: U.S. Department of Commerce; Blue Chip Economic Indicators (10/10 and 3/11); Insurance Information Institute.

2011 Financial Overview

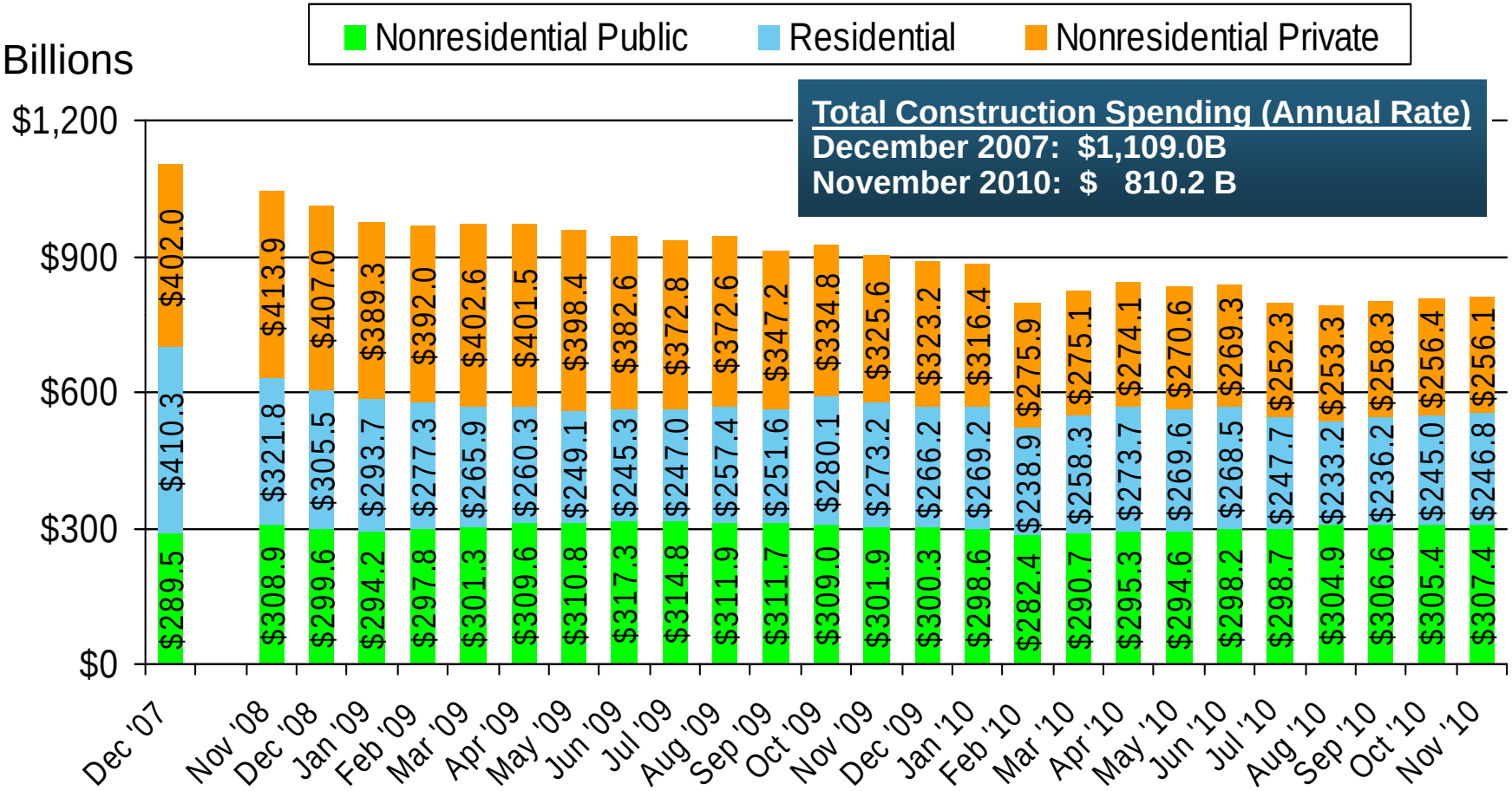
Average Square Footage of Completed New Homes in U.S., 1973-2010*



The average size of completed new homes fell by 145 square feet (5.75%) from 2008-2010, the largest recession-based drop in nearly four decades

*2010 figure is weighted average square feet of completed homes in first three quarters of 2010
Source: U.S. Census Bureau: http://www.census.gov/const/www/quarterly_starts_completions.pdf; Insurance Information Institute.

2011 Financial Overview
Value* of Construction Put In Place



Since the recession started, private residential and nonresidential construction together are down $300 billion (annual rate), a drop of 38%. This affects property, surety, and other construction-related exposures

*Seasonally adjusted annual rate

Source: http://www.census.gov/const/C30/release.pdf

2011 Financial Overview

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

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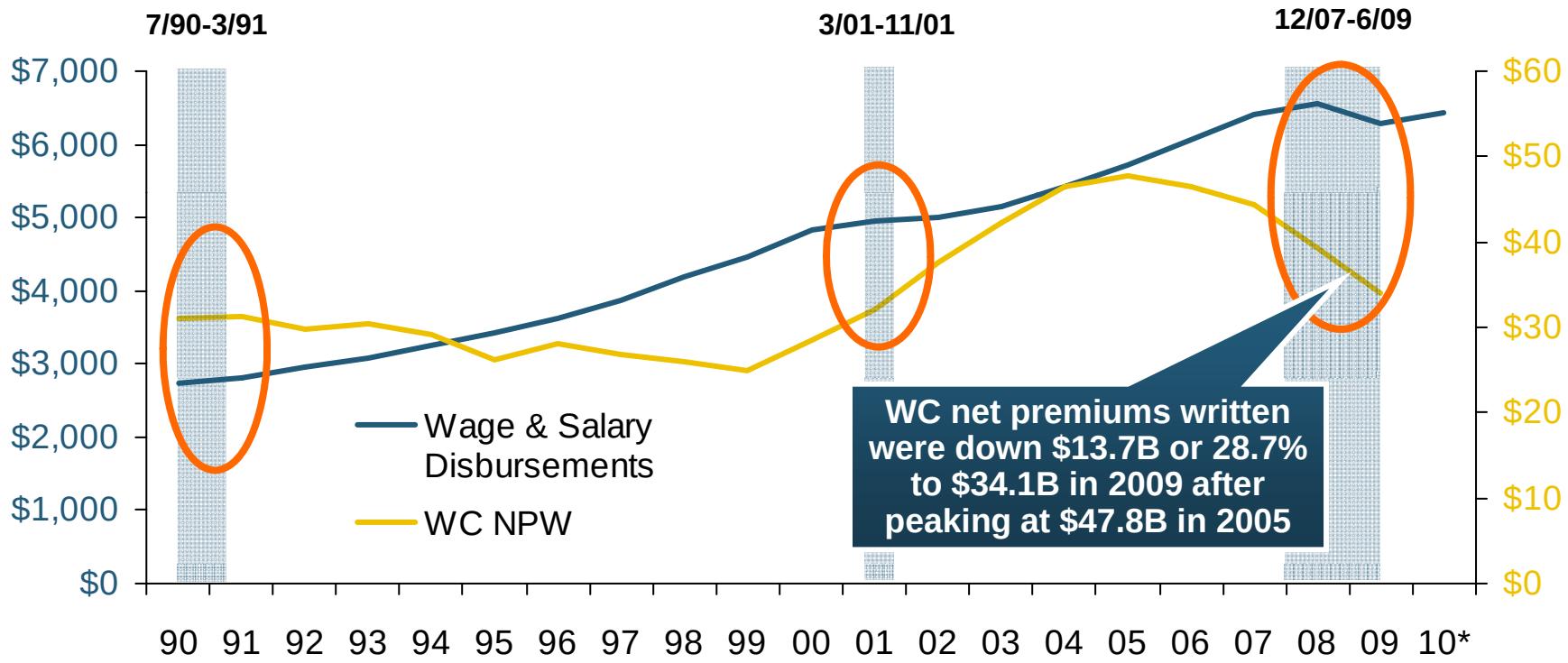
Wage and Salary Disbursement (Private Employment) vs. WC NWP ($ Billions)

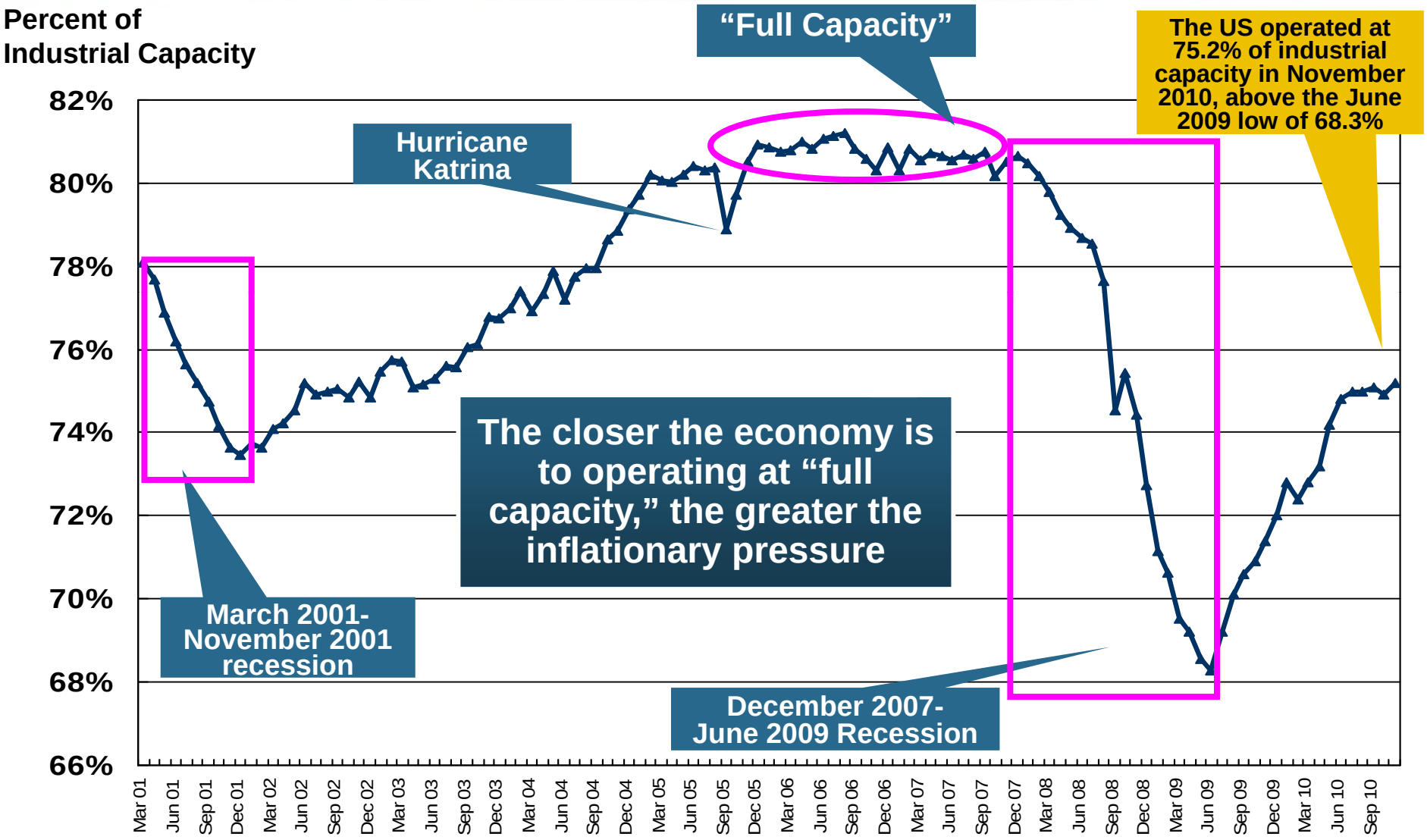


Weakening payrolls have eroded $2B+ in workers comp premiums; nearly 29% of NPW has been eroded away by the soft market and weak economy

* Average Wage and Salary data as of 7/1/2010. 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

Recovery in Capacity Utilization is a Positive Sign for Commercial Exposures



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

Business Bankruptcy Filings, 1980-2010:Q3

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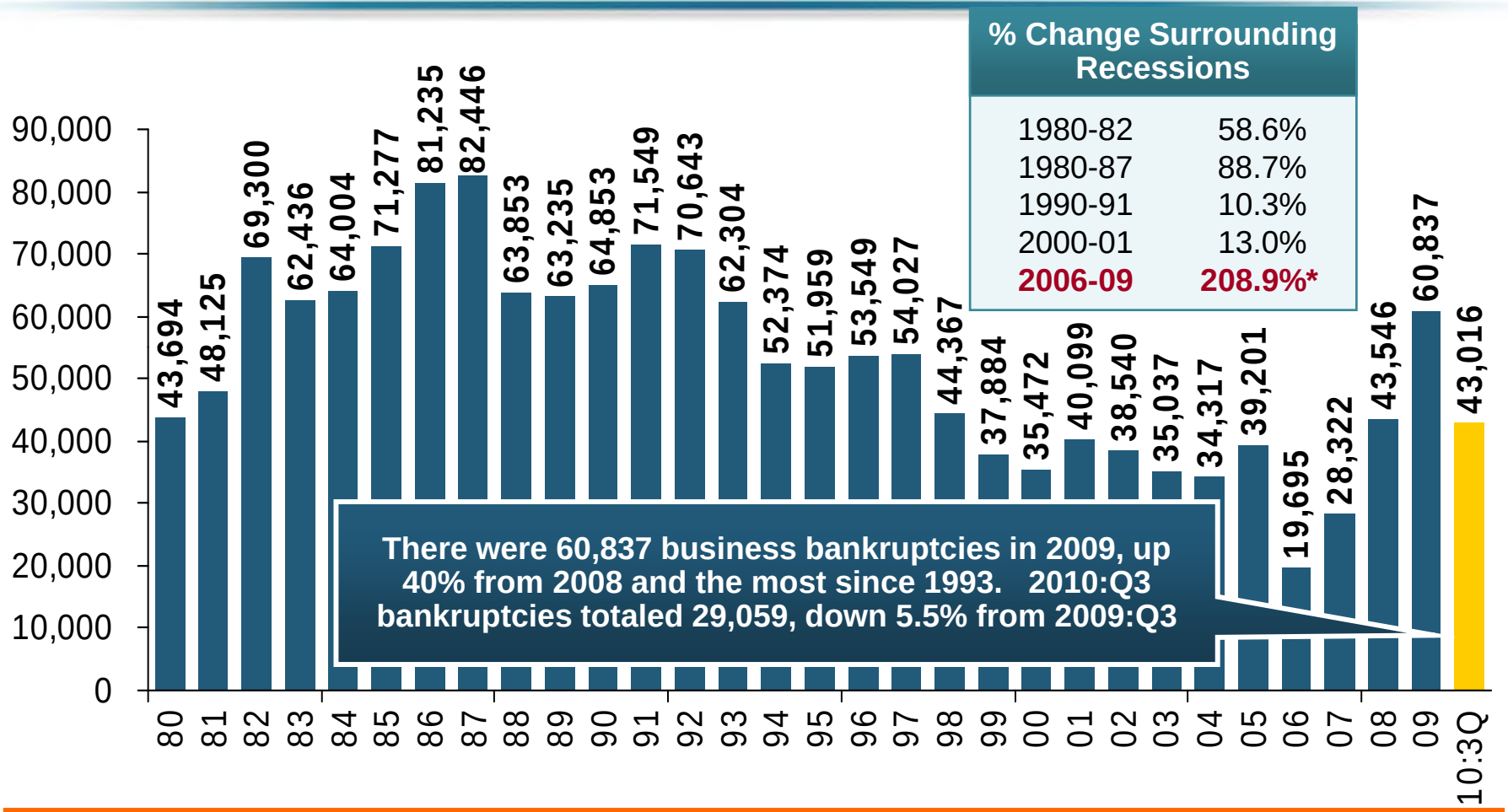

% Change Surrounding Recessions	
1980-82	58.6%
1980-87	88.7%
1990-91	10.3%
2000-01	13.0%
2006-09	**208.9%***

There were 60,837 business bankruptcies in 2009, up 40% from 2008 and the most since 1993. 2010:Q3 bankruptcies totaled 29,059, down 5.5% from 2009:Q3

Significant Exposure Implications for All Commercial Lines

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

Private Sector Business Starts, 1993:Q2 – 2010:Q2*

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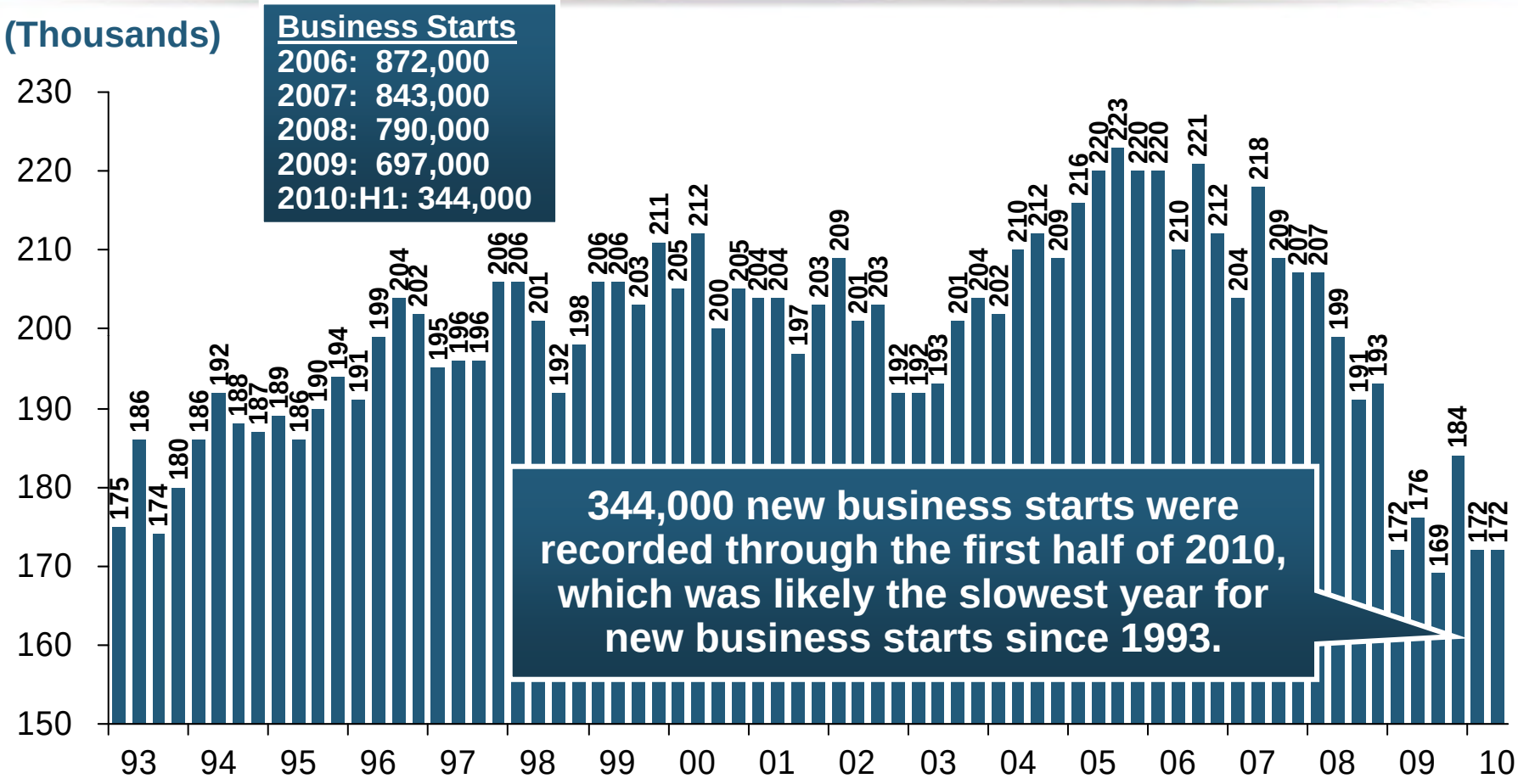


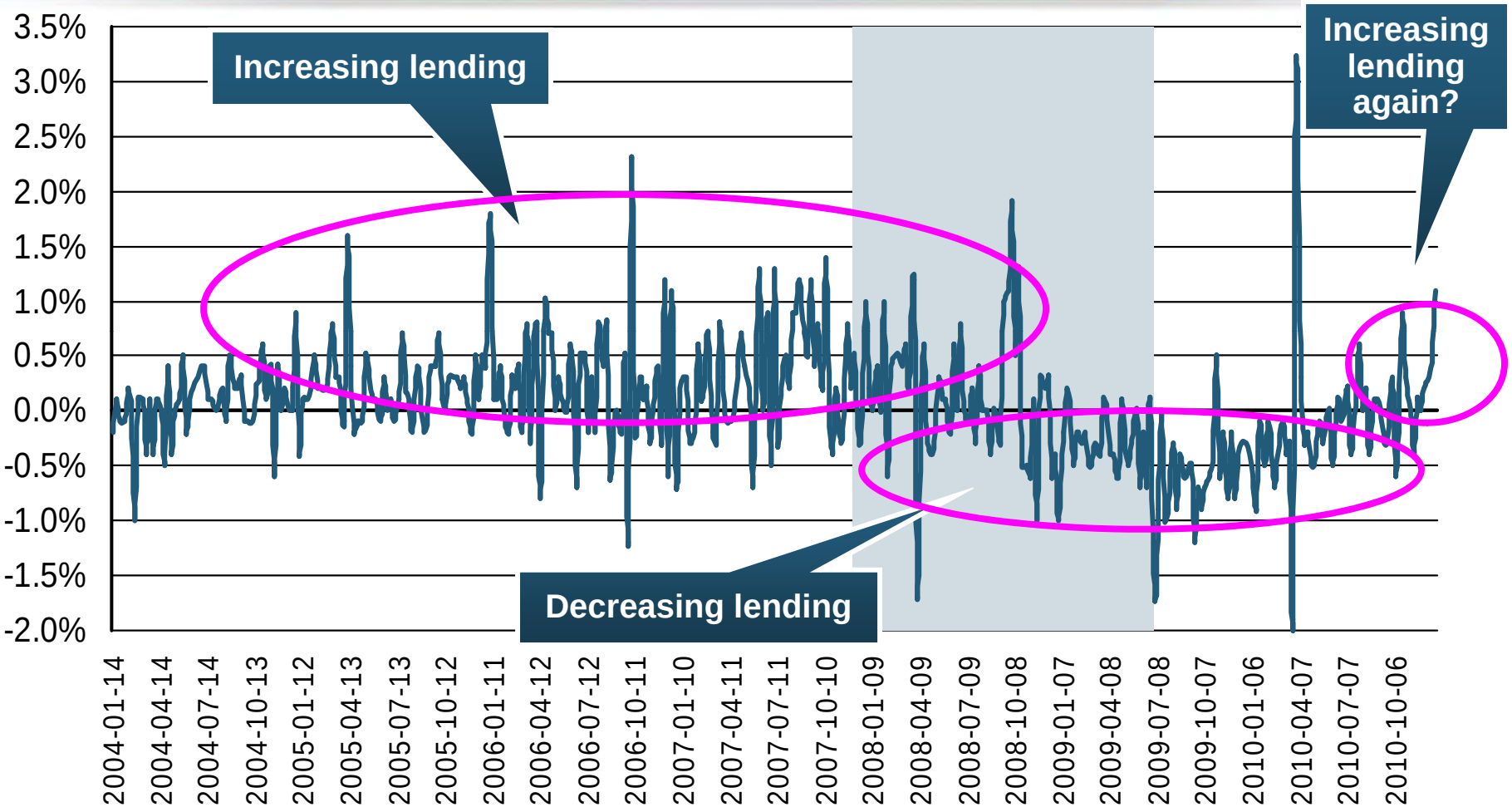
Business Starts Were Down Nearly 20% in the Recession, Holding Back Most Types of Commercial Insurance Exposure

* Data through June 30, 2010 are the latest available as of March 10, 2011; Seasonally adjusted

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

2011 Financial Overview

Weekly Percentage Change in Commercial and Industrial Loans by Large U.S. Banks, 2004-2010



Lending peak: $827.3 billion at mid-October 2008;
Trough $600.5 billion at mid-October 2010; Latest (12/20/2010) $619.9 billion

Note: Recession indicated by gray shaded column.

Sources http://research.stlouisfed.org/fred2/series/CIBOARD/downloaddata?cid=100 ; National Bureau of Economic Research (recession dates); Insurance Information Institute.

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Labor Market Trends

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

Unemployment and Underemployment Rates: Falling Faster in 2011?

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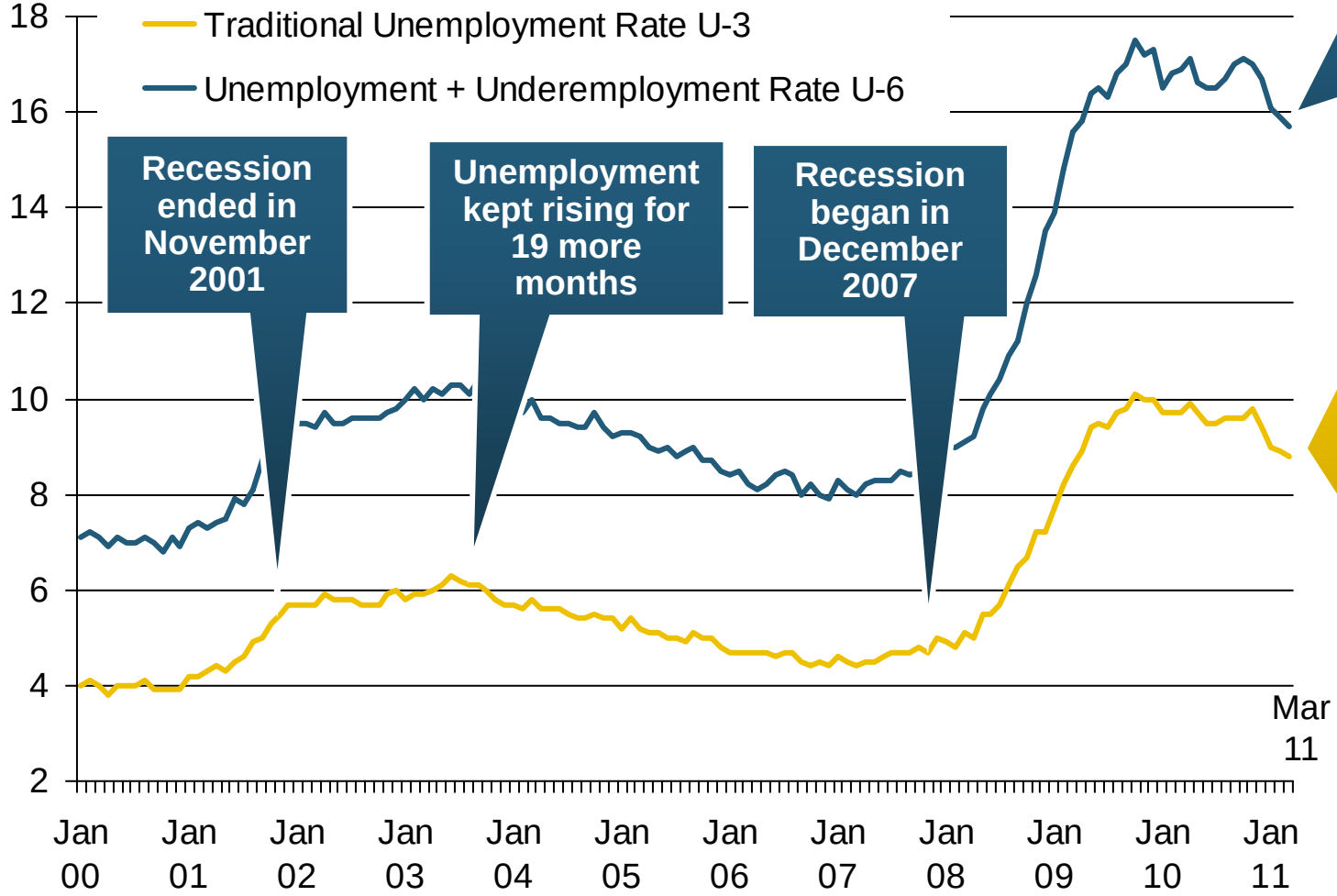
January 2000 through March 2011, Seasonally Adjusted (%)



U-6 went from 8.0% in March 2007 to 17.5% in October 2009; Stood at 15.7% in March 2011

Unemployment rate fell to 8.8% in March

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

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

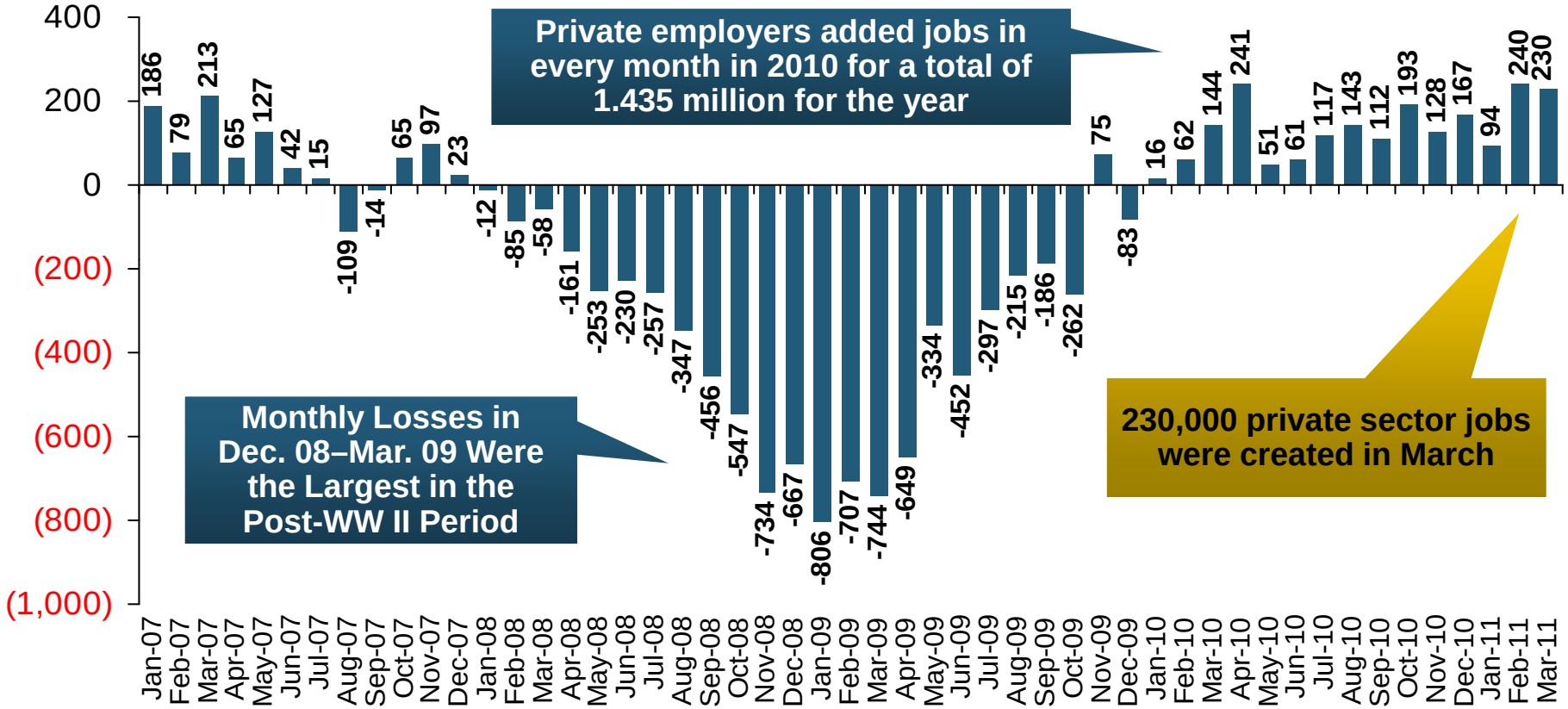
Stubbornly high unemployment and underemployment will constrain payroll growth, which directly affects WC exposure

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

Monthly Change in Private Employment

INSURANCE INFORMATION INSTITUTE

January 2008 through March 2011* (Thousands)



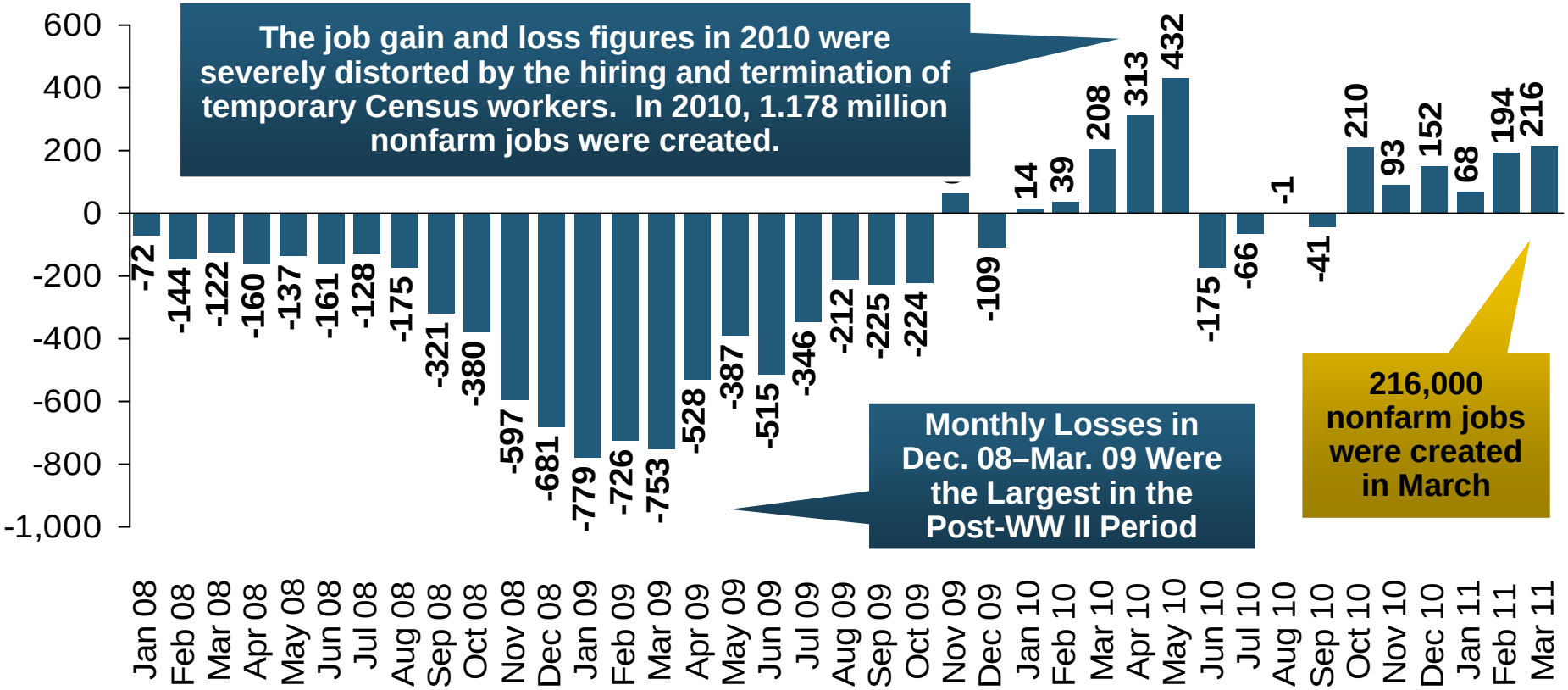
Private Employers Added 1.999 million Jobs Since Jan. 2010 After Having Shed 4.66 Million Jobs in 2009 and 3.81 Million in 2008 (Local Govt. Employment is Down 416,000 Since Sept. 2008 Peak)

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

Monthly Change Employment*

INSURANCE INFORMATION INSTITUTE

January 2008 through March 2011* (Thousands)



Job Losses Since the Recession Began in Dec. 2007 Peaked at 8.4 Mill in Dec. 09; Stands at 6.2 Million Through March 2011; 13.5 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

US Unemployment Rate

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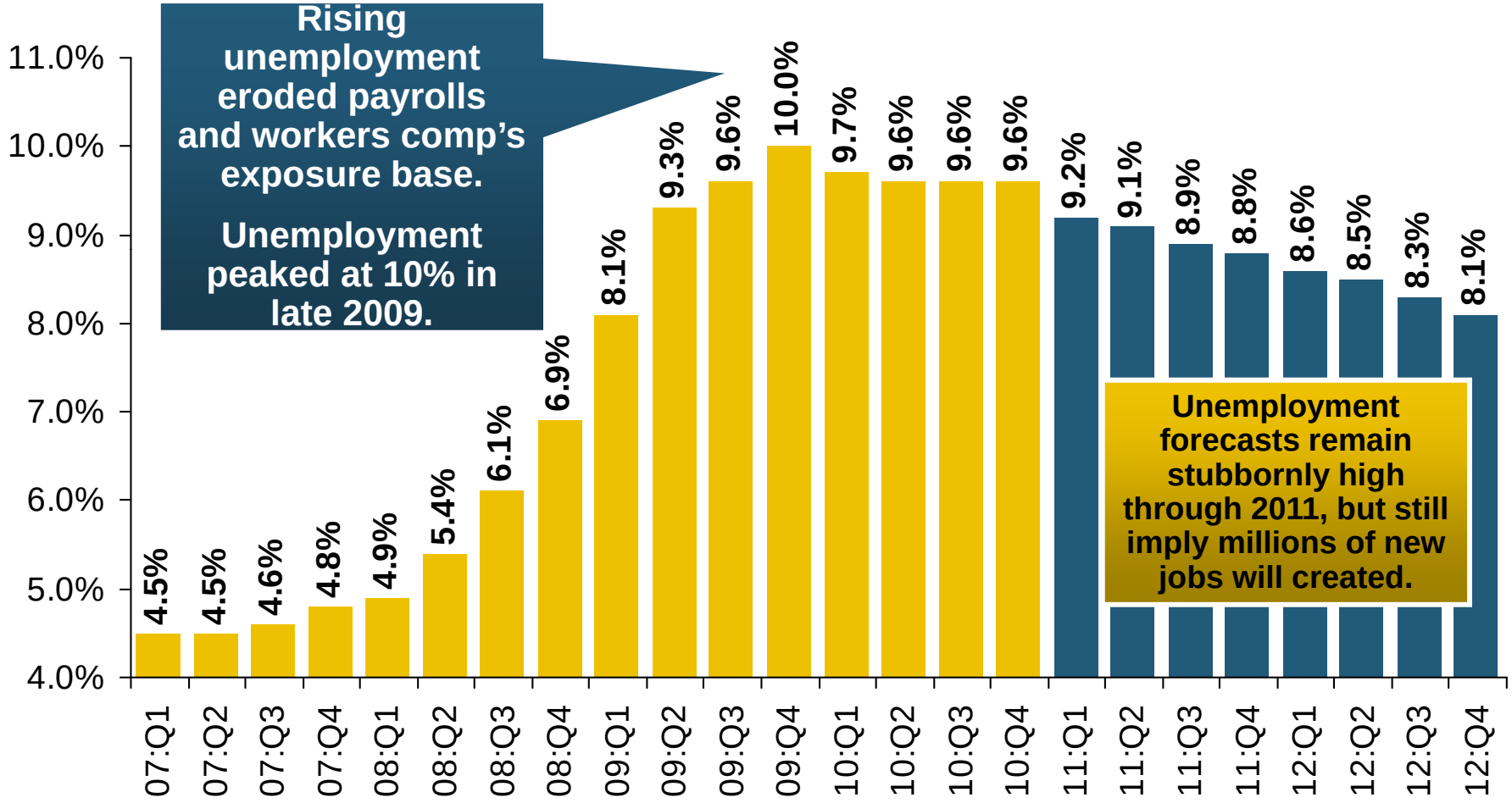
2007:Q1 to 2012:Q4F*



* = actual; = forecasts

Sources: US Bureau of Labor Statistics; Blue Chip Economic Indicators (3/11); Insurance Information Institute

US Unemployment Rate Forecasts

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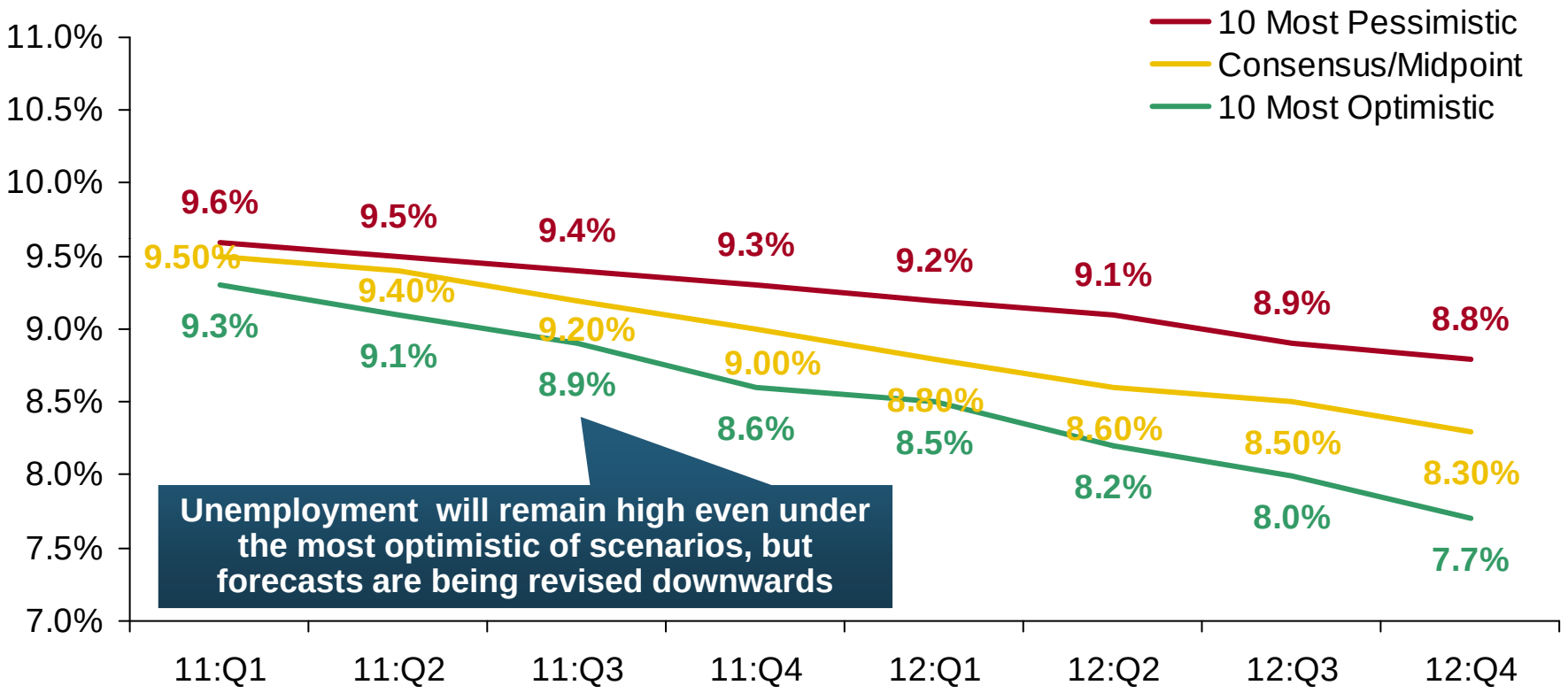
Quarterly, 2011:Q1 to 2012:Q4

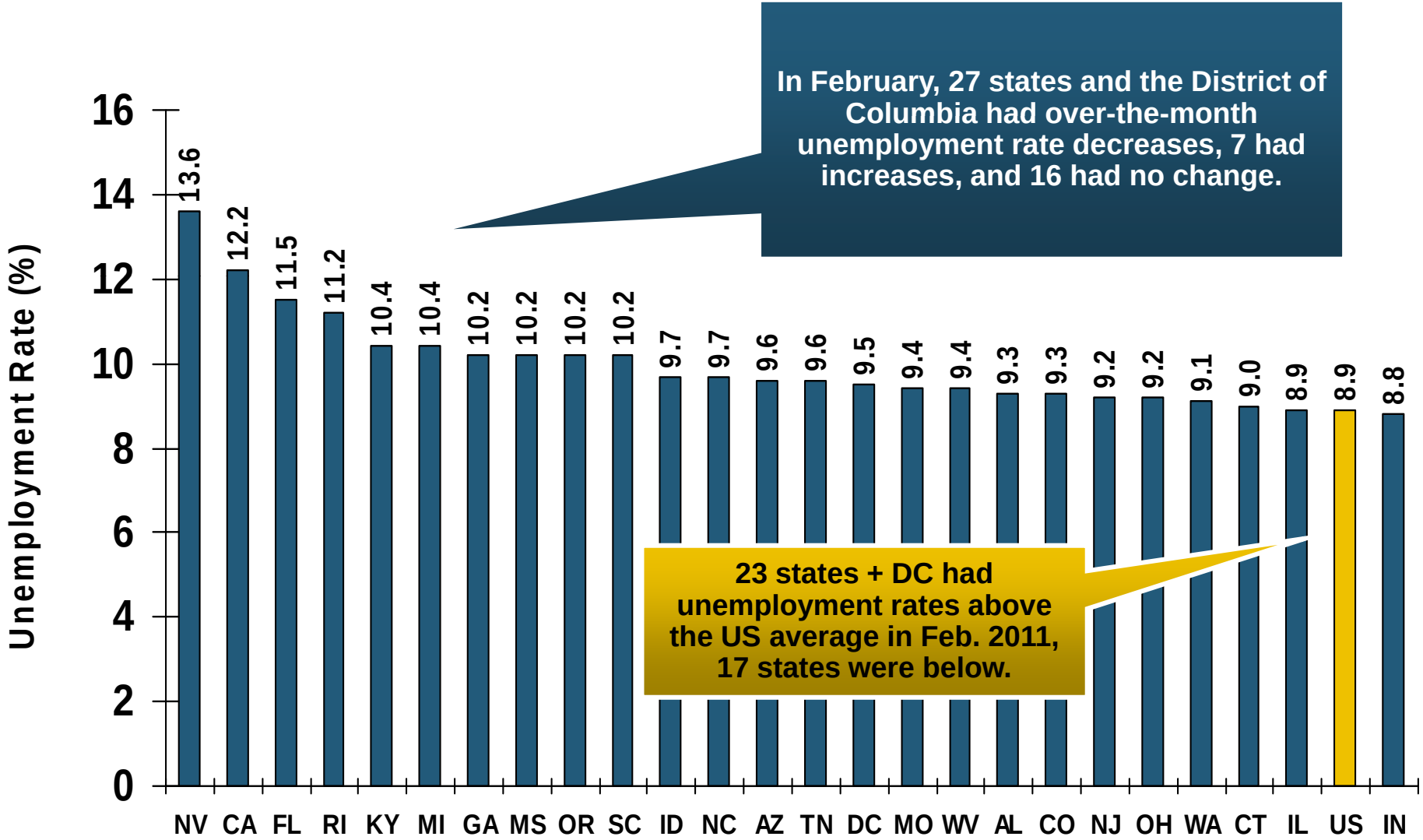


Unemployment will remain high even under the most optimistic of scenarios, but forecasts are being revised downwards

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

Sources: Blue Chip Economic Indicators (2/11); Insurance Information Institute

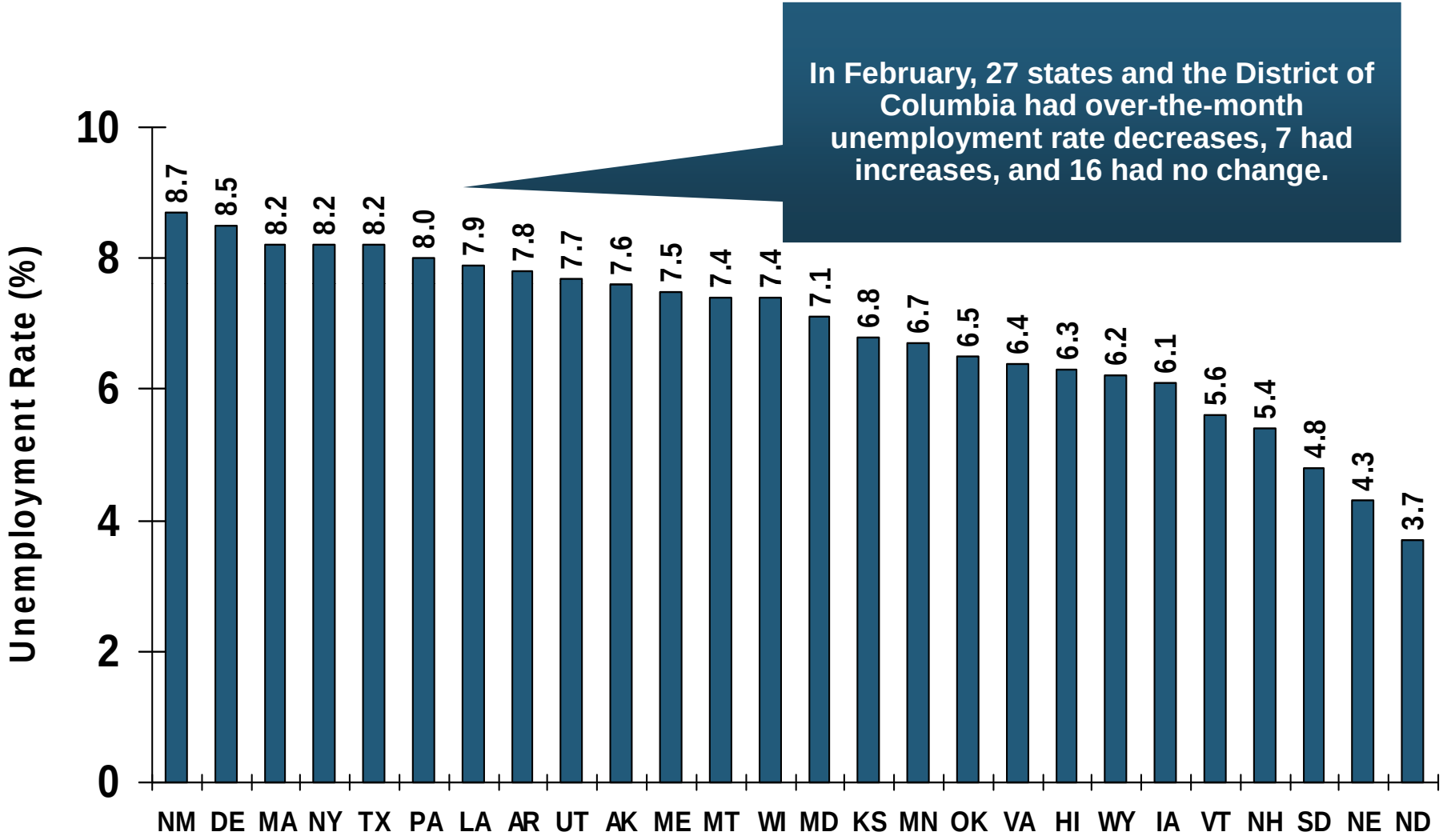
Unemployment Rates by State, February 2011: Highest 25 States*



*Provisional figures for February 2011, seasonally adjusted.

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

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



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

Labor Underutilization: Broader than Just Unemployment

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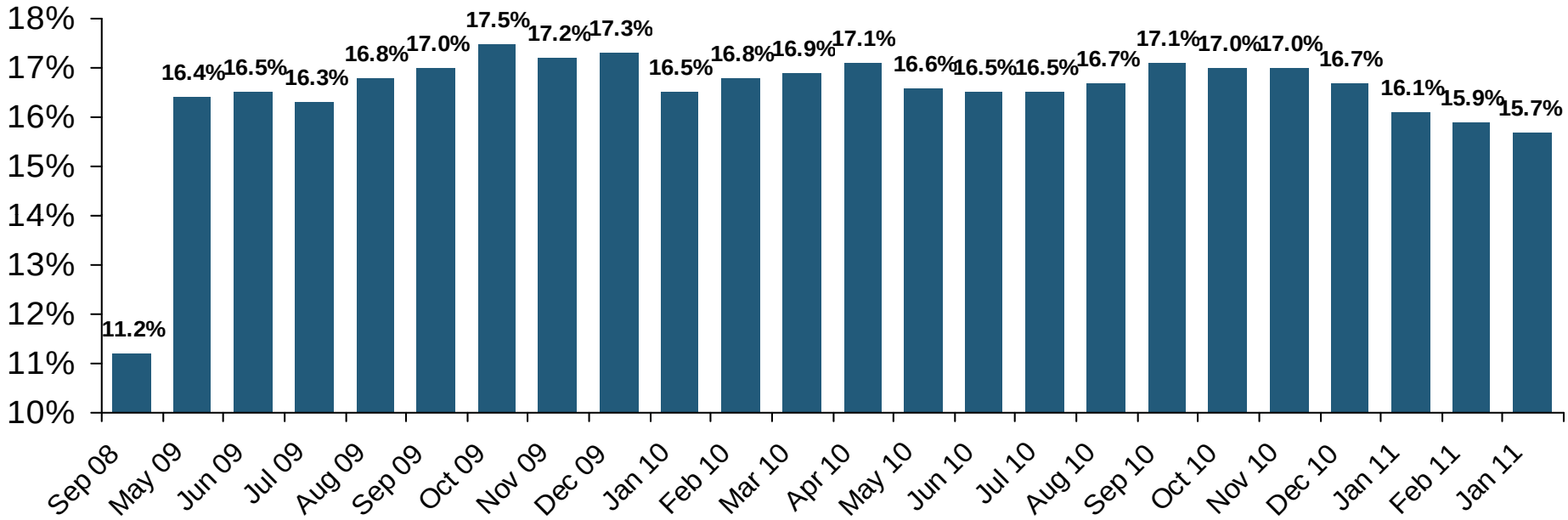
% of Labor Force



Marginally Attached and Unemployed Persons Account for 15.7% of the Labor Force in March 2011 (1 Out Every 6.4 People). Unemployment Rate Alone was 8.8%. 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

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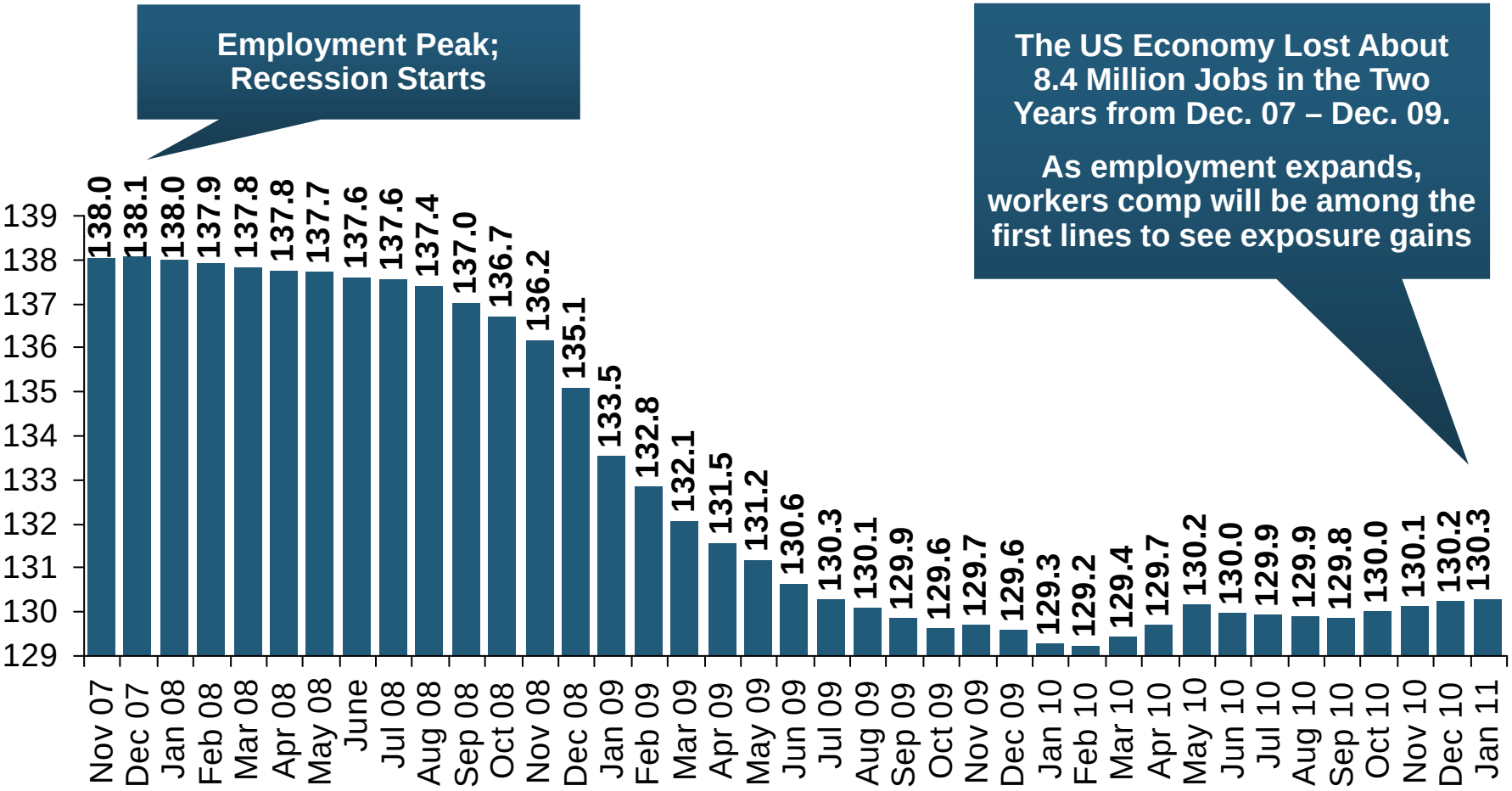
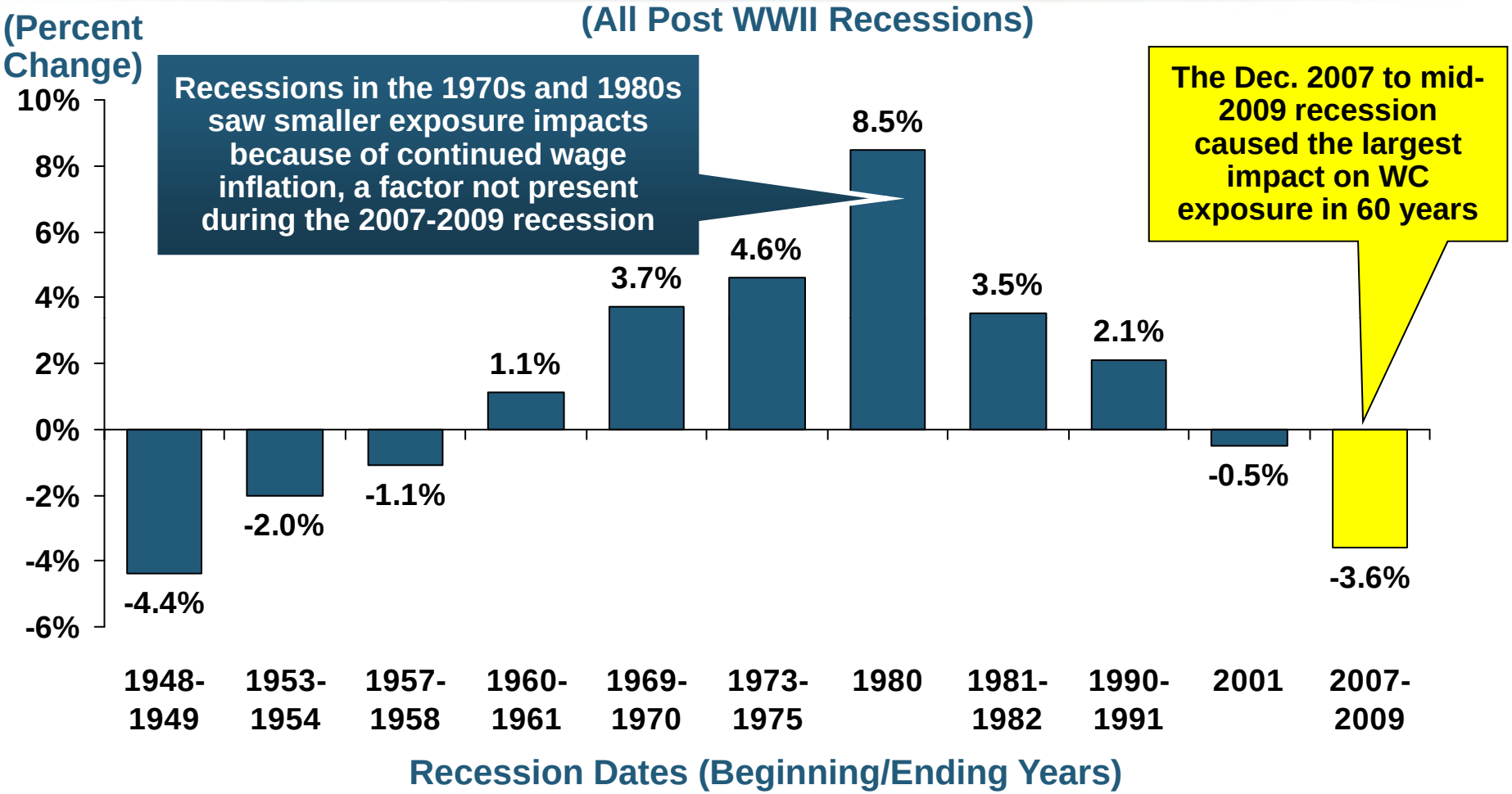
Monthly, Nov 2007 – January 2011 (Millions)



Seasonally adjusted.
Source: US Bureau of Labor Statistics

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



*Data represent maximum recorded decline over 12-month period using annualized quarterly wage and salary accrual data

Source: Insurance Information Institute research; Federal Reserve Bank of St. Louis (wage and salary data); National Bureau of Economic Research (recession dates).

Frequency: 1926–2008
A Long-Term Drift Downward

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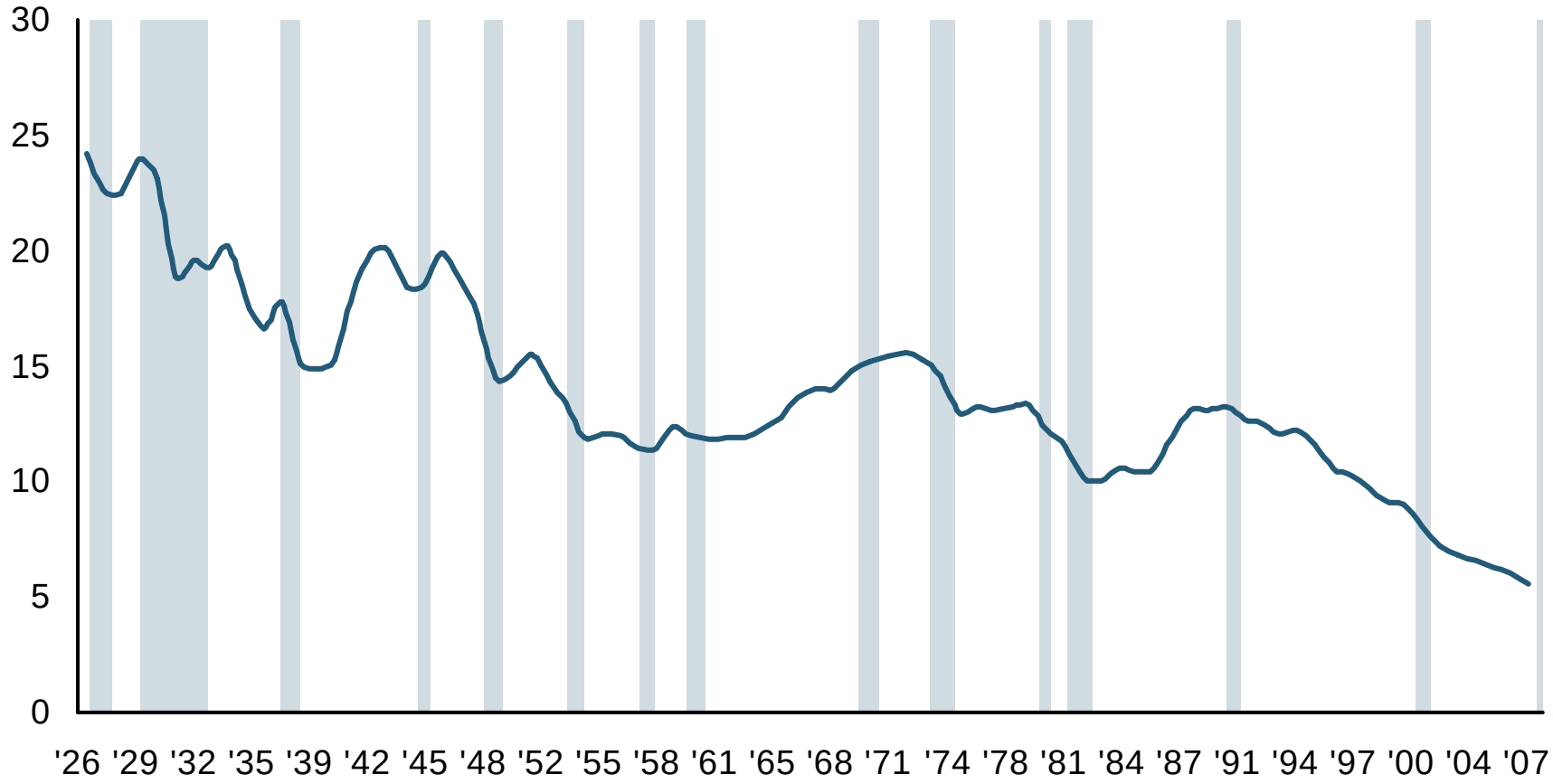
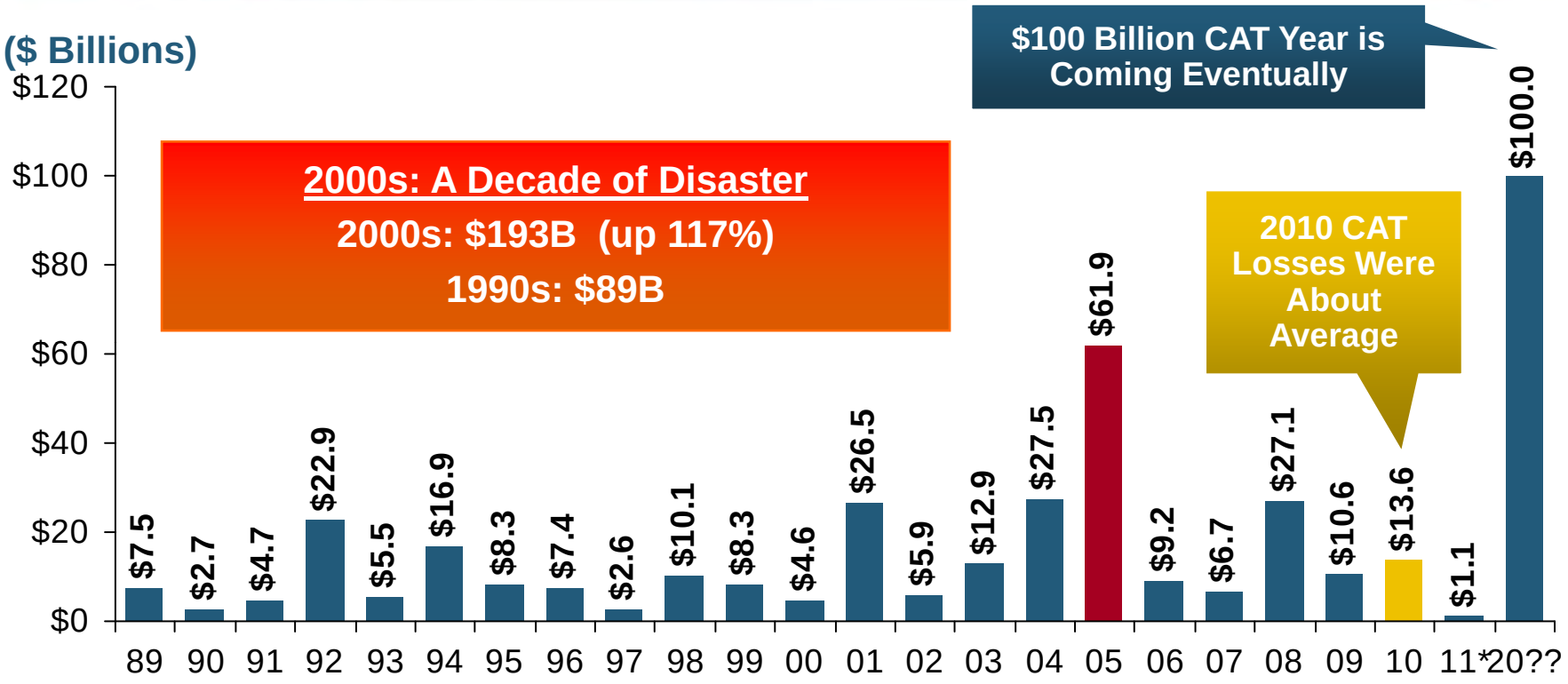
Manufacturing – Total Recordable Cases
Rate of Injury and Illness Cases per 100 Full-Time Workers



Note: Recessions indicated by gray bars.
Sources: NCCI from US Bureau of Labor Statistics; National Bureau of Economic Research

Catastrophic Loss – Catastrophe Losses Trends Are Trending Adversely

US Insured Catastrophe Losses



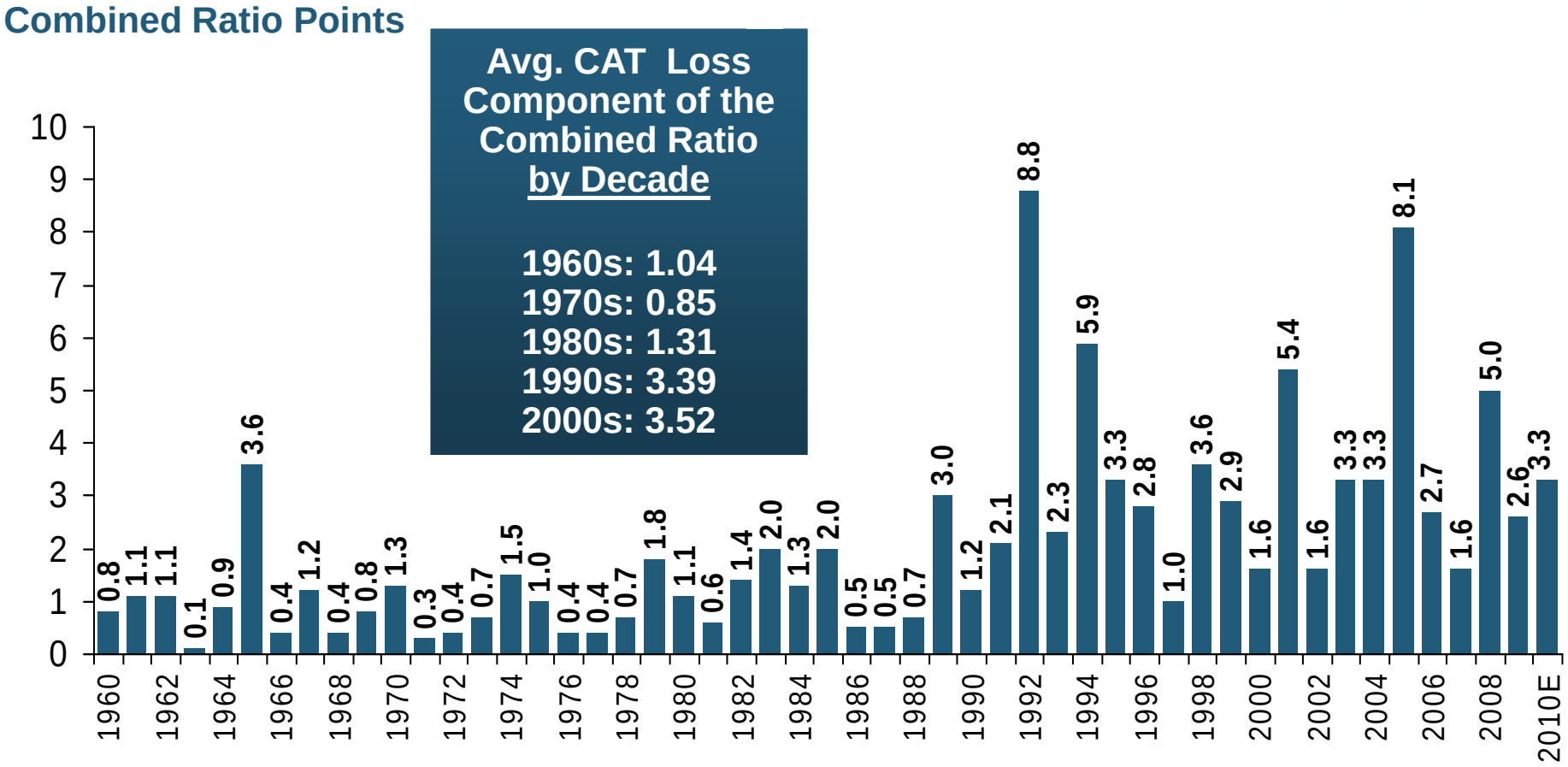
2010 CAT Losses Were Close to "Average"
Figures Do Not Include an Estimate of Deepwater Horizon Loss

*First quarter 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; Munich Re; Insurance Information Institute.

Combined Ratio Points Associated with Catastrophe Losses: 1960 – 2010E

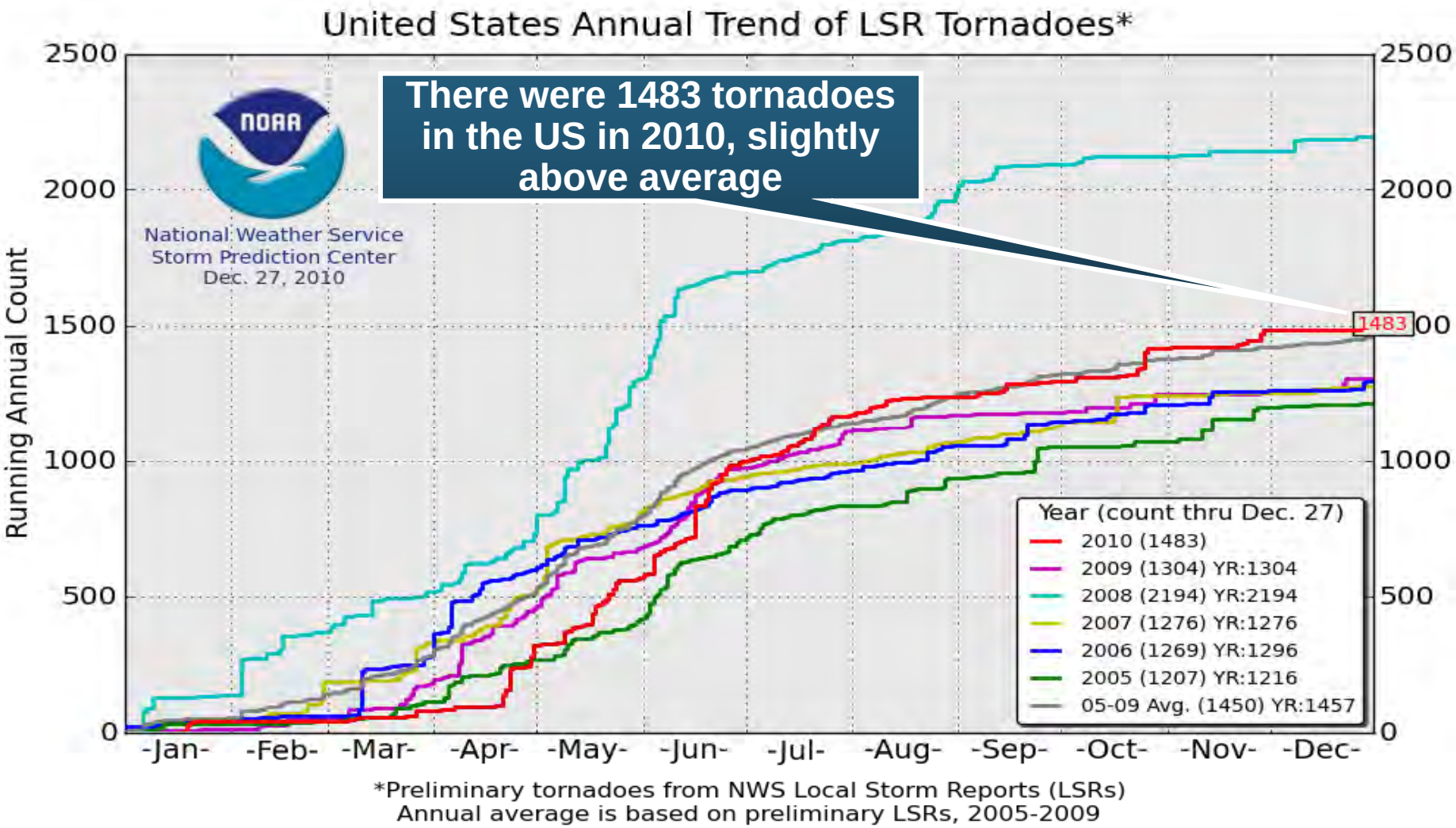


The Catastrophe Loss Component of Private Insurer Losses Has Increased Sharply in Recent Decades

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

Source: ISO; Insurance Information Institute estimate for 2010.

U.S. Tornado Count, 2010



Source: NOAA

U.S. Thunderstorm Loss Trends

Annual Totals 1980 – 2009 vs. First Half 2010

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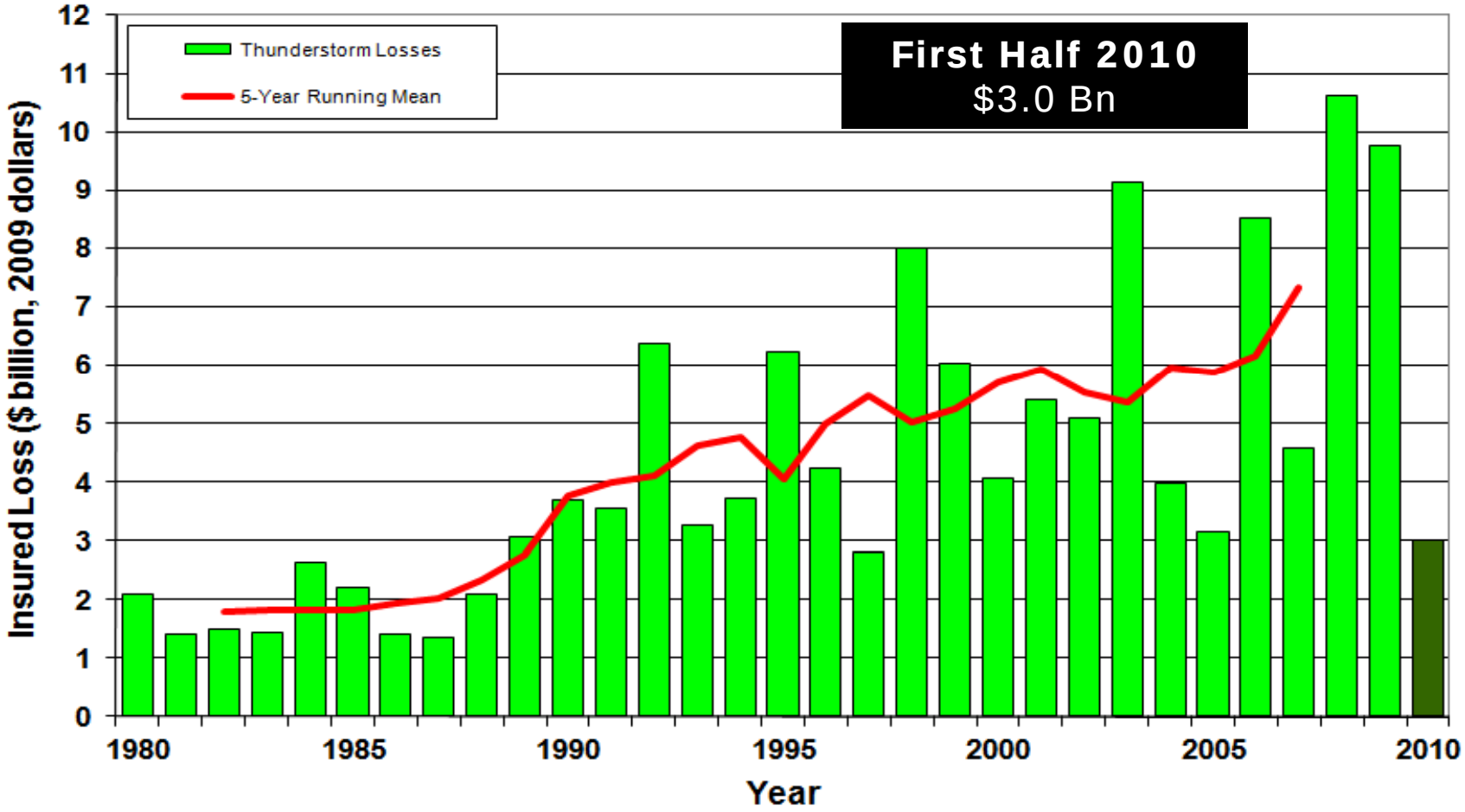
Thunderstorm losses have quadrupled since 1980.



Source: Property Claims Service, MR NatCat*SERVICE*

U.S. Winter Storm Loss Trends

Annual totals 1980 – 2009 vs. First Half 2010

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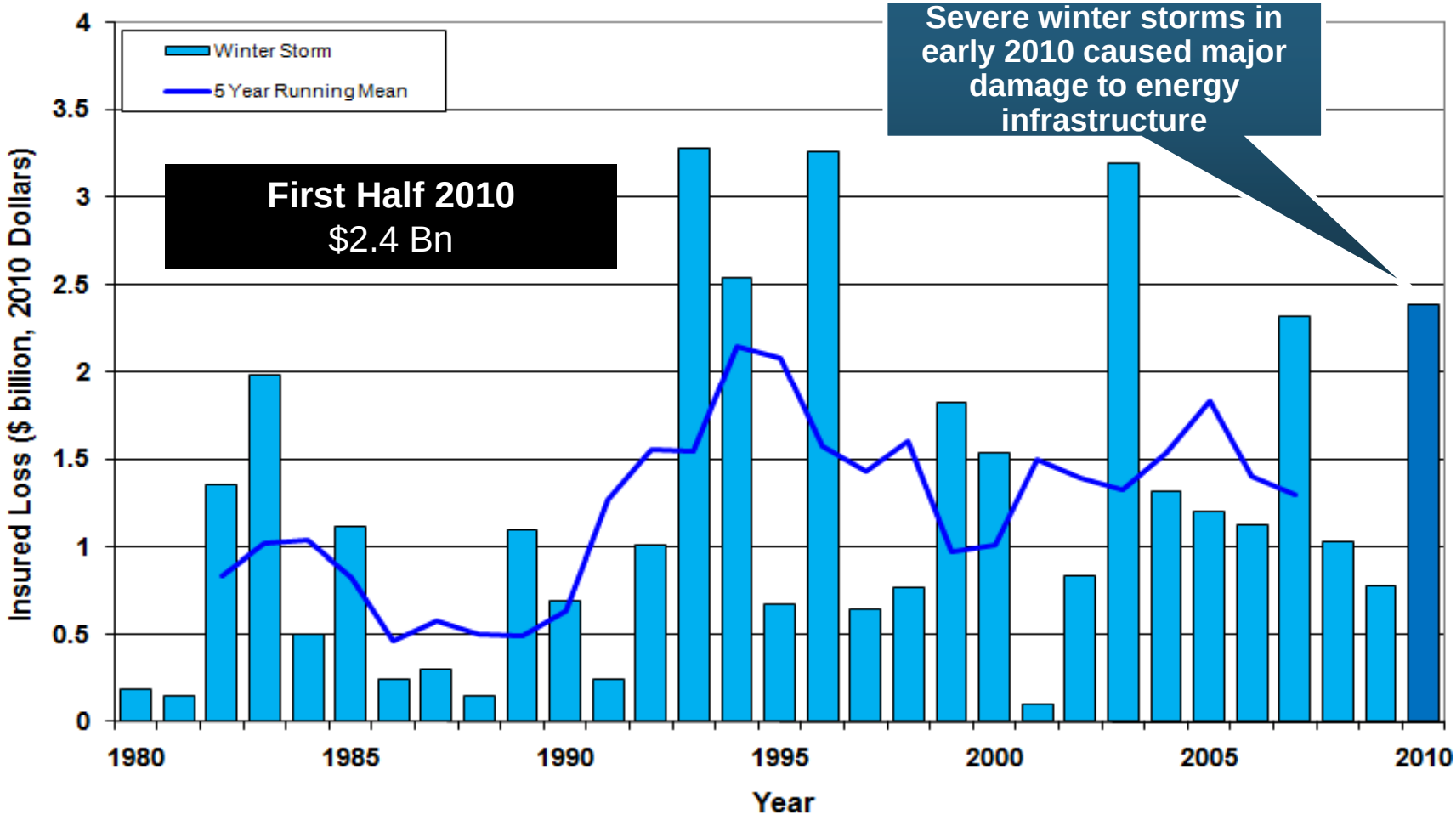
Average annual winter storm losses have increased over 50% since 1980.



Source: Property Claims Service, MR NatCat*SERVICE*

Distribution of US Insured CAT Losses: TX, FL, LA vs. US, 1980-2010*

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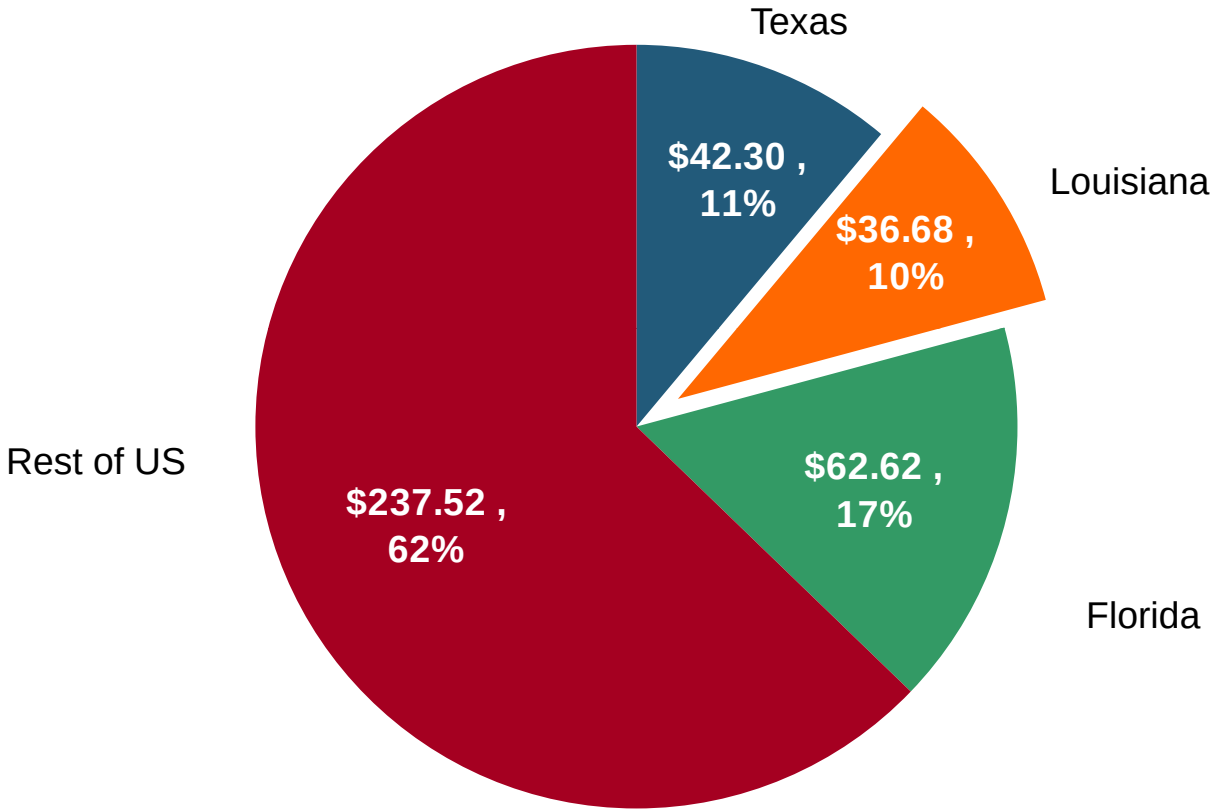
($ Billions)



Louisiana Accounted for 10% of All US Insured CAT Losses from 1980-2010: $36.7B out of $237.5B

* Adjusted to 2010 dollars.
Source: PCS division of ISO; Insurance Information Institute.

Top 12 Most Costly Disasters in US History

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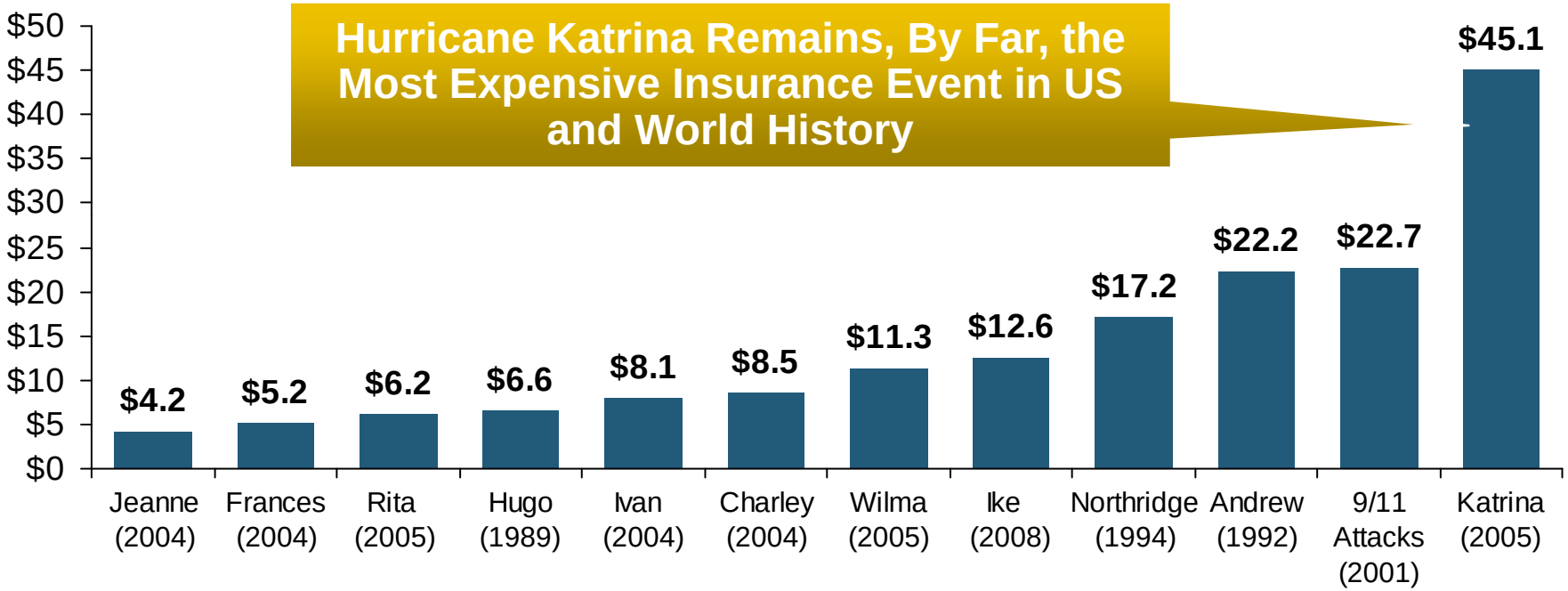
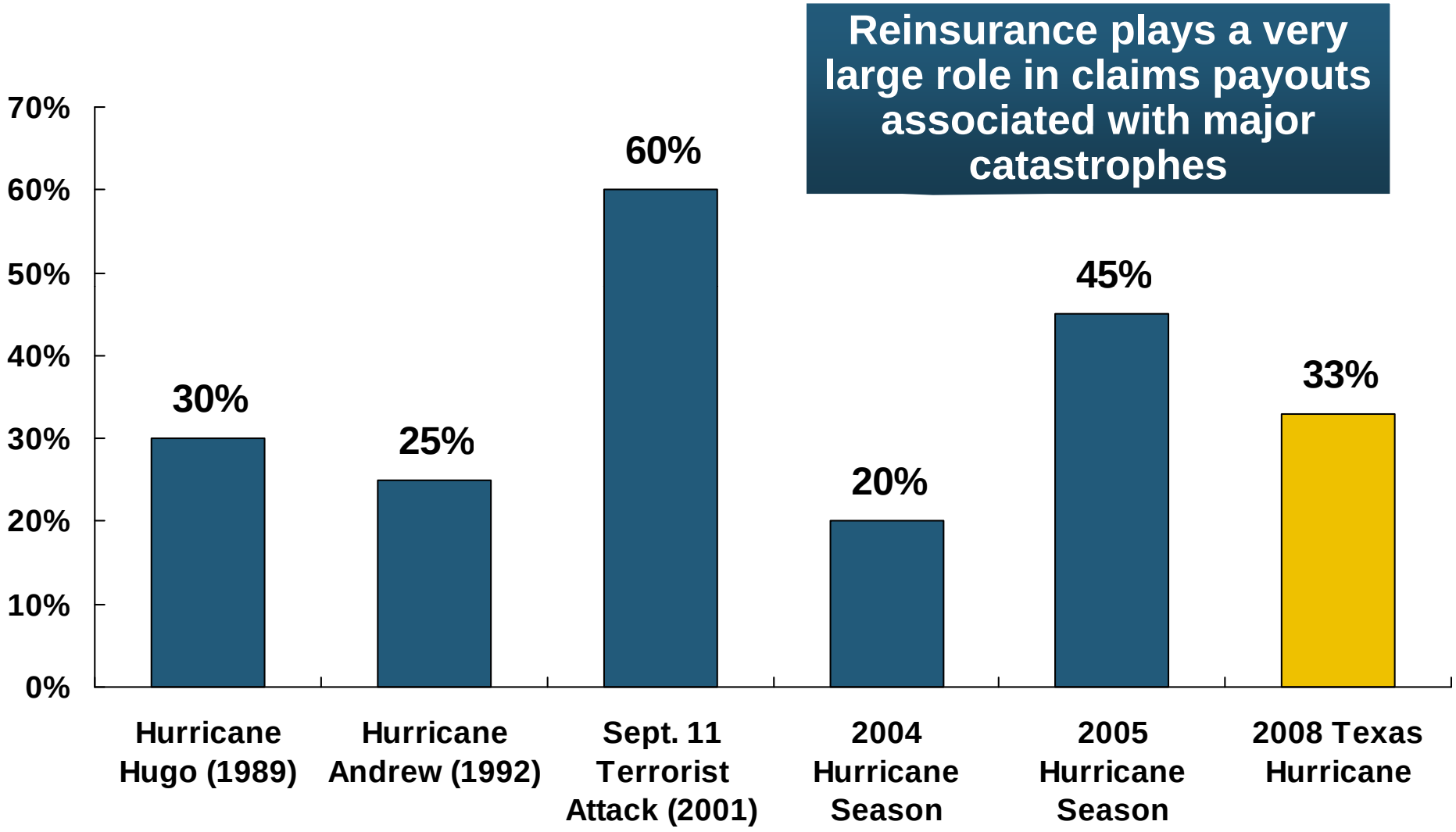
(Insured Losses, 2009, $ Billions)



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

Sources: PCS; Insurance Information Institute inflation adjustments.

Share of Losses Paid by Reinsurers for Major Catastrophic Events

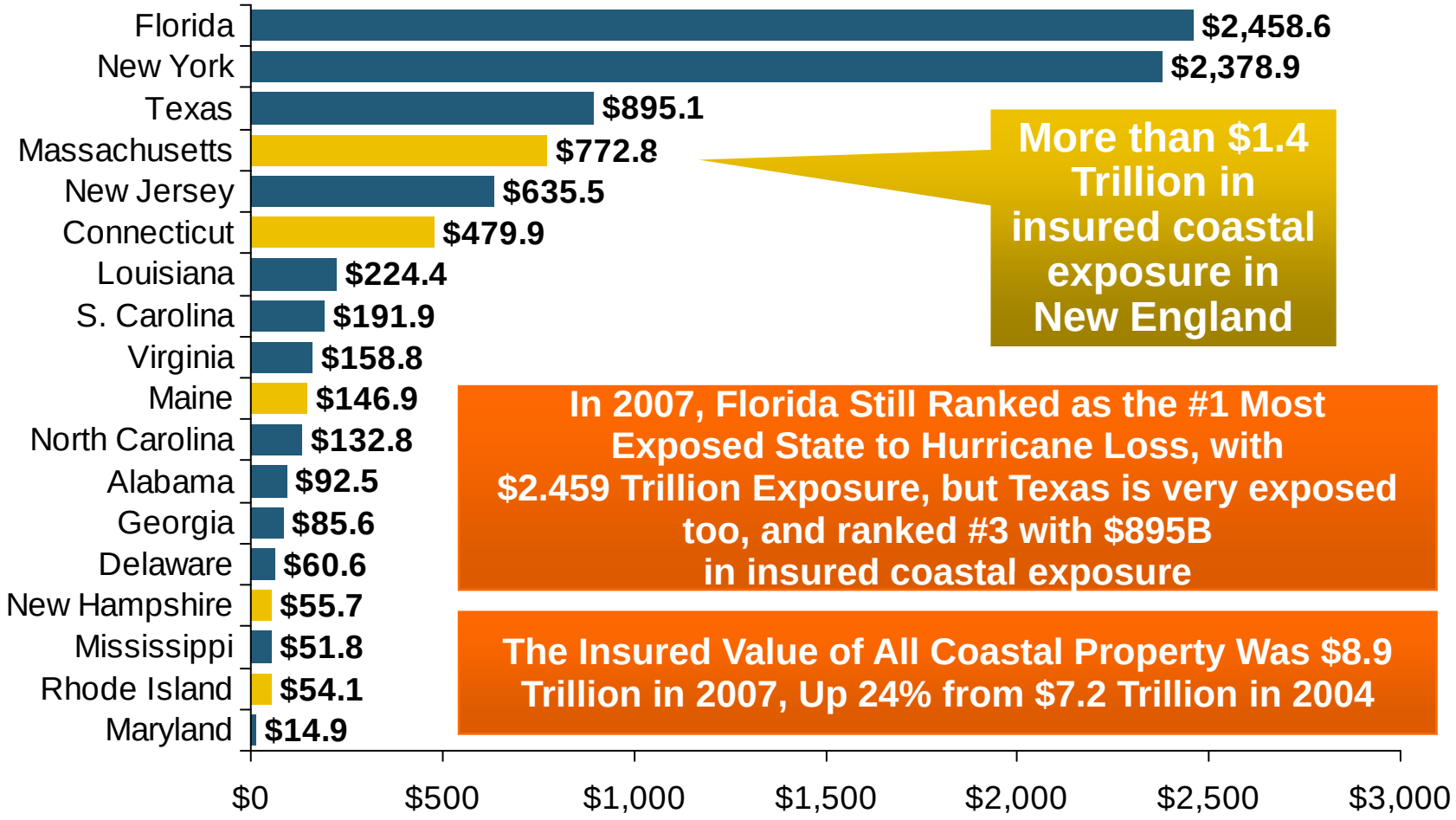


Source: Wharton Risk Center, Disaster Insurance Project, Renaissance Re, Insurance Information Institute.

Total Value of Insured Coastal Exposure

INSURANCE INFORMATION INSTITUTE

(2007, $ Billions)



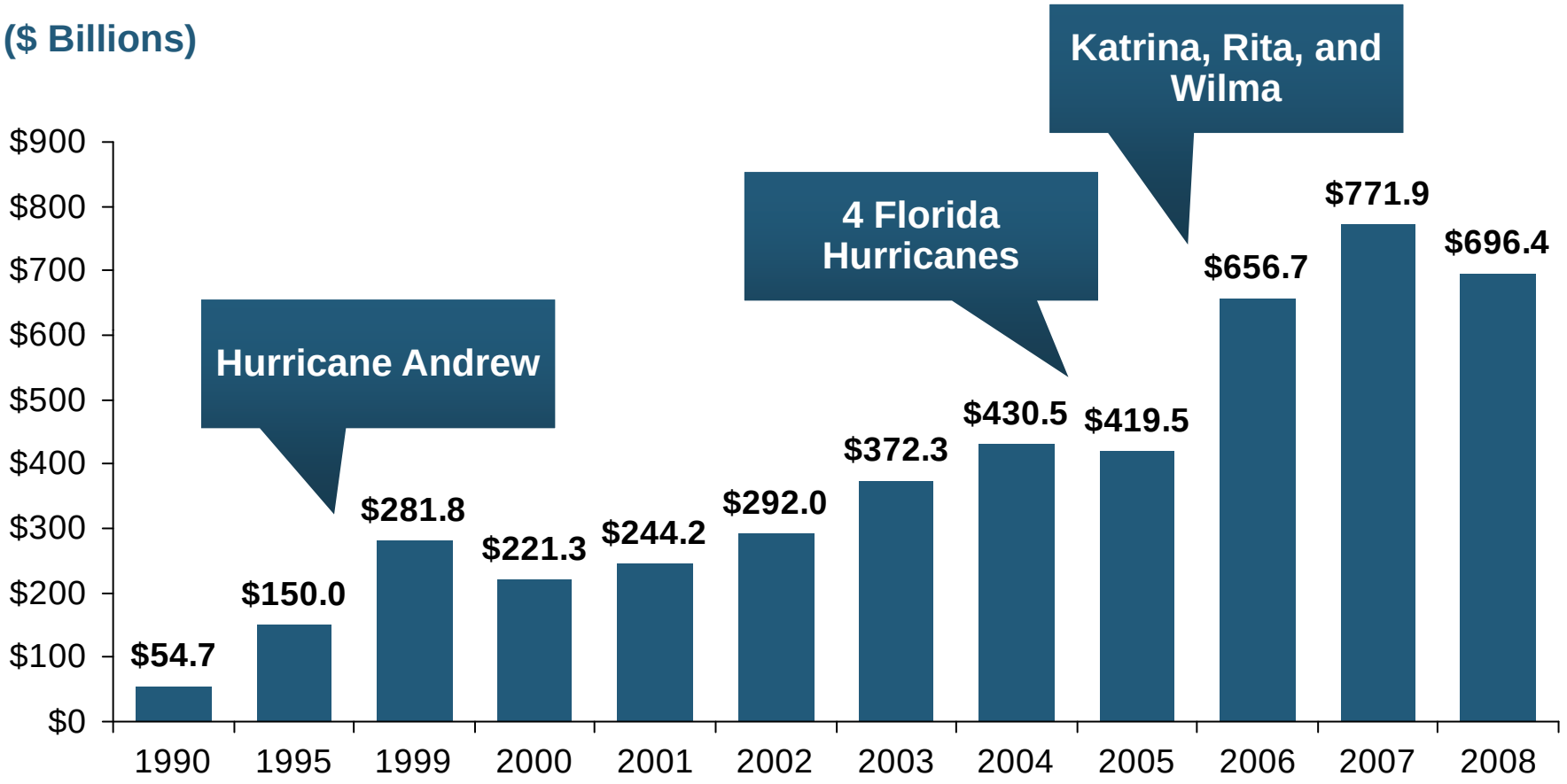
More than $1.4 Trillion in insured coastal exposure in New England

In 2007, Florida Still Ranked as the #1 Most Exposed State to Hurricane Loss, with $2.459 Trillion Exposure, but Texas is very exposed too, and ranked #3 with $895B in insured coastal exposure

The Insured Value of All Coastal Property Was $8.9 Trillion in 2007, Up 24% from $7.2 Trillion in 2004

Source: AIR Worldwide

US Residual Market Exposure to Loss



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

Source: PIPSO; Insurance Information Institute

Insurance Information Institute Online:

www.iii.org

Thank you for your time and your attention!

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