



# **Overview and Outlook for the P-C Insurance Industry: *Challenges & Opportunities for 2011 & Beyond***

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- **Reasons for Optimism, Causes for Concern**
- **Insurance Industry Financial Overview & Outlook**
  - ◆ Profitability
  - ◆ Premium Growth
  - ◆ Capital & Capacity
  - ◆ Underwriting Performance: Commercial Lines
  - ◆ Financial/Investment Review & Outlook
- **Financial Strength Overview**
- **Financial Services Reform: Impacts on the Insurance Industry**
- **Tort System Review: Overview and Causes for Concern**
- **Performance by Segment/Line**
  - ◆ Personal & Commercial Lines
- **The Global Economic Storm: Financial Crisis & Recession**
  - ◆ Crisis-Driven Exposure Issues: Commercial Lines
  - ◆ Exposure, Growth & Profitability
- **Catastrophe Losses**
- **Q&A**

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

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

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

- **P/C Insurance Industry Capacity as of 6/30/10 Is at Record Levels and Has Recovered 100%+ of the Capital Lost During the Financial Crisis**
  - ◆ As of 12/31/09 capacity was within 2% of pre-crisis high
- **Record Capacity, Depressed Exposures Mean that Generally Soft Market Conditions Will Persist through 2010 and Potentially into 2011**
- **There is No Catalyst for a Robust Hard Market at the Current Time**
- **High Global First Half 2010 CAT Losses Insufficient to Trigger Hard Market**
  - ◆ Localized insurance and reinsurance impacts are occurring, especially earthquake coverage in Latin/South America, Offshore Energy Markets, European Wind Cover
- **Inflation Outlook for US and Major European Economies and Japan is Tame**
  - ◆ Will temper claims inflation
  - ◆ Deflation is highly unlikely
- **Financial Strength & Ratings of Global (Re)Insurance Industries Remained Strong Throughout the Financial Crisis in Sharp Contrast With Banks**
- **Insurers Avoided the Most Draconian Outcomes in Financial Services Reform Legislation**
- **Tort Environment in US is Beginning to Deteriorate; No Tort Reform in US**
- **Major Transformation of US Economy Underway with Major Opportunities for Insurers through 2020 in Health, Tech, Natural Resources, Ag., Energy**

# 11 Industries for the Next 10 Years: Insurance Solutions Needed

**Health Care**

**Health Sciences**

**Energy (Traditional)**

**Alternative Energy**

**Agriculture**

**Natural Resources**

**Environmental**

**Technology (incl. Biotechnology)**

**Light Manufacturing**

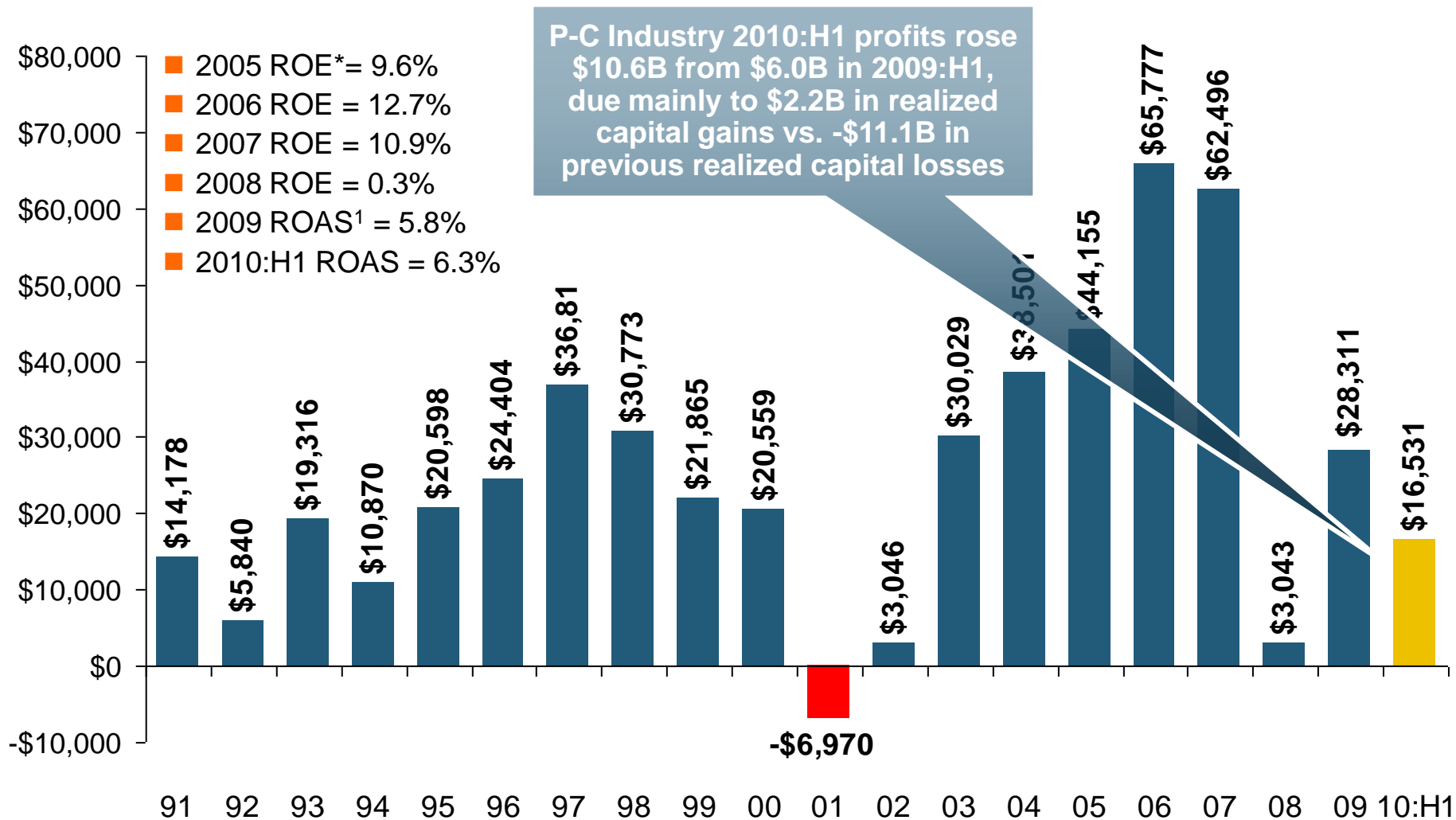
**Export-Oriented Industries**

**Shipping (Rail, Marine)**

# Profitability

**Historically Volatile**

# P/C Net Income After Taxes 1991–2010:H1 (\$ Millions)

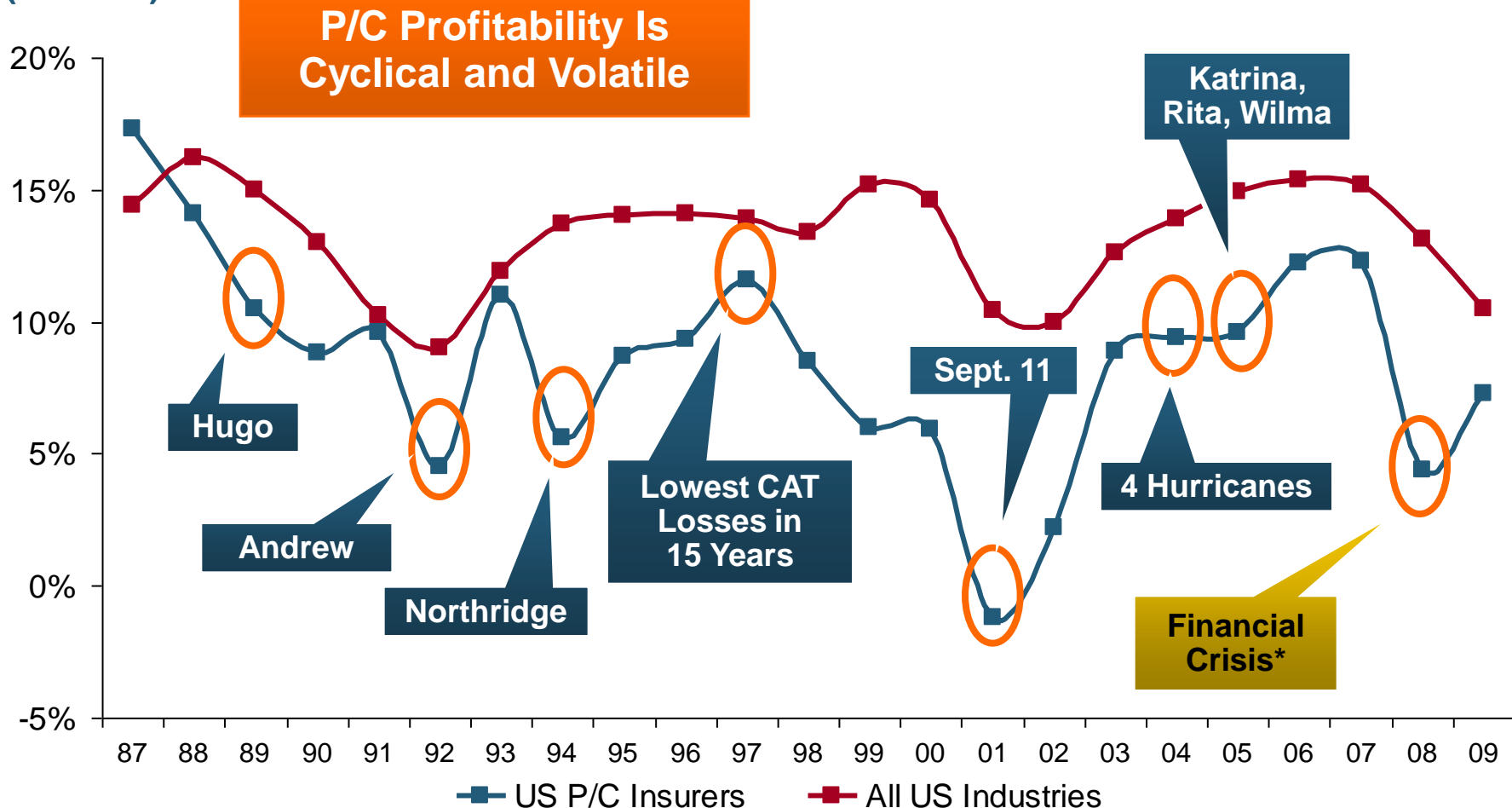


\* ROE figures are GAAP; <sup>1</sup>Return on avg. surplus. Excluding Mortgage & Financial Guaranty insurers yields a 7.5% ROAS for 2010:H1 and 4.6% for 2009. 2009:H1 net income was \$19.2 billion and \$10.2 billion in 2008:H1 excluding M&FG.

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

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

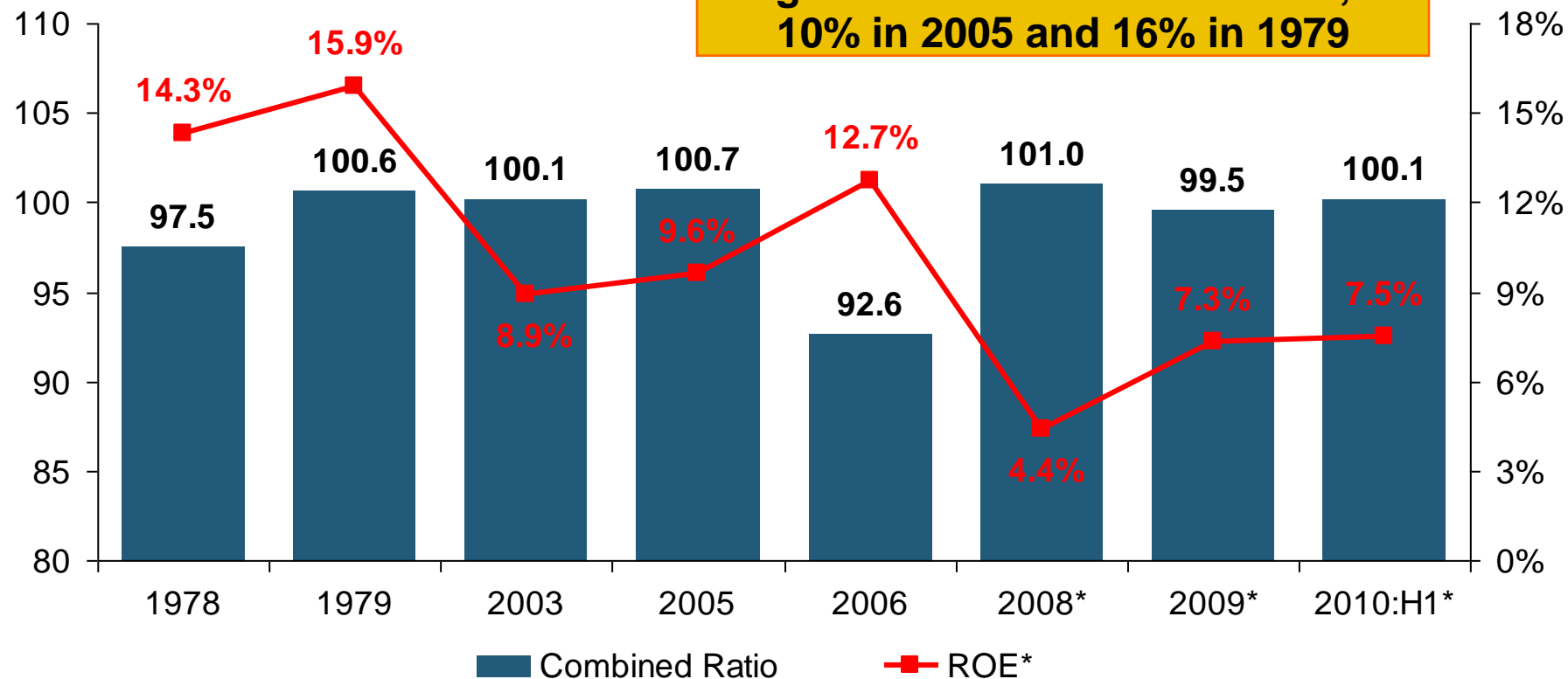
(Percent)



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

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

## Combined Ratio / ROE



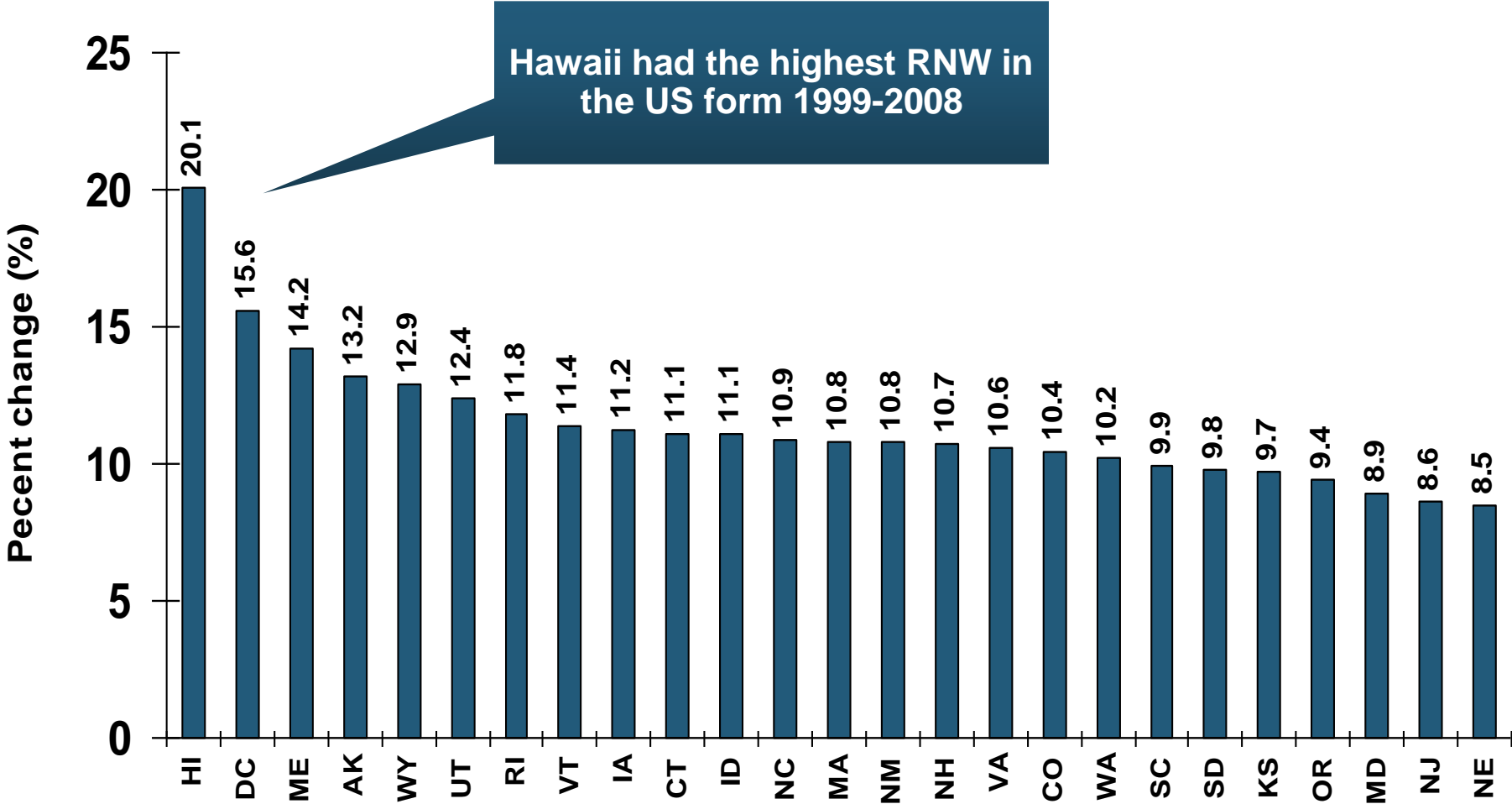
**Combined Ratios Must Be Lower in Today's Depressed Investment Environment to Generate Risk Appropriate ROEs**

\* 2009 and 2010:Q1 figures are return on average statutory surplus. 2008, 2009 and 2010:H1 figures exclude mortgage and financial guaranty insurers

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

# Return of Net Worth: 10-Year Average, 1999-2008\*: All Lines

## Top 25 States

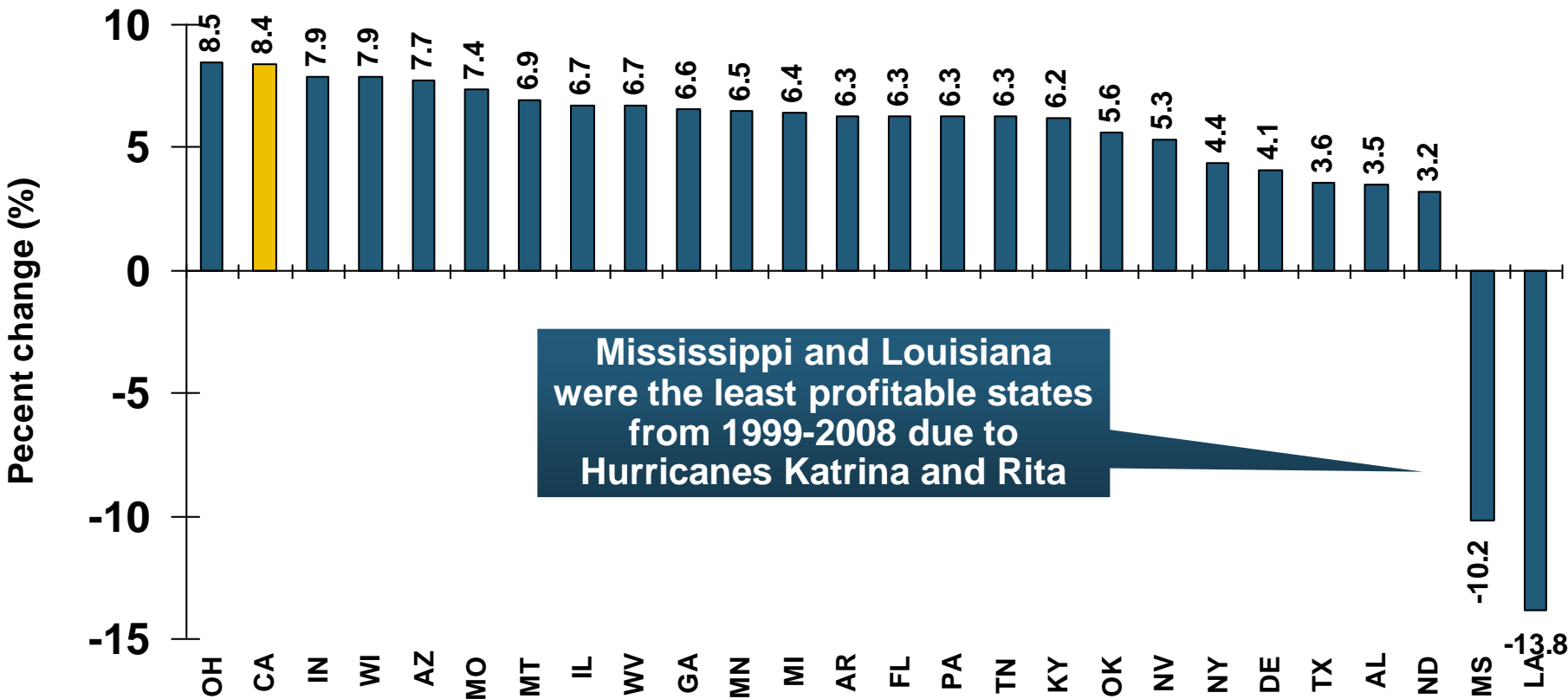


\*Latest available.

Source: 2009 NAIC Report on Profitability.

# Return of Net Worth: 10-Year Average, 1999-2008: All Lines

## Bottom 25 States



Sources: 2009 NAIC Report on Profitability.

# **Will the 2010 Midterm Election Results Impact P/C Insurer Profitability & Performance?**

**Yes, But Most Impact is on  
Structure, Legislation and  
Regulation**

# The 2010 Midterm Elections:

## *What do the results mean for insurers?*

### ■ Catastrophe Financing

- Supporters of Homeowners Defense Act (e.g., Rep. Neil, D-FL) defeated; Act proposed a larger role for the federal govt. in financing natural catastrophe losses
- Rep. Gene Taylor (D-MS) defeated: He supported adding wind to NFIP
- Unclear if flood program once again winds up in limbo

### ■ Health Care Reform (Obamacare)

- Promises to “repeal and replace” aren’t credible (Senate and White House still Democratically controlled); Object is to starve implementation via low/no funding
- Obamacare and Boehnercare will do little to control the trajectory of costs
- Impacts on benefits business
- Republicans need plan to deal with entitlement (Medicare) to cut budget

### ■ Dodd-Frank

- Likely few major provisions impact insurers the most (e.g., creation of FIO) unlikely to be affected

# The 2010 Midterm Elections:

## *What do the results mean for insurers?*

### ■ Tort Reform

- Tort was not a major issue in the 2010 campaign, but the new House can be expected to be receptive to the idea of federal tort reform, unlike prior Congresses since 2006
- Fewer new pieces of legislation likely to spawn tort actions (e.g., climate change)
- State legislatures and governorships more receptive to tort reforms

### ■ Taxes/Fiscal Policy

- Odds of an across-the-board continuation of Bush tax cuts more likely; Benefits small business and high net worth individuals and their insurers.
- Immediate expensing of new investment in 2011?? Good for p/c exposures.

### ■ Regulatory/Business Policy

- More pro-business stance
- Should help stimulate commercial exposures (WC payrolls, property & liability)
- Ohio monopolistic state fund → Move to competitive structure?

# **Financial Services Reform**

**Insurers Are Impacted,  
But Not Significantly**

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

## The Dodd Frank Wall Street Reform and Consumer Protection Act

### ■ Systemic Risk and Resolution Authority

- Creates the Financial Stability Oversight Council and the Office of Financial Research
- Imposes heightened federal regulation on large bank holding companies and “systemically risky” nonbank financial companies, including insurers

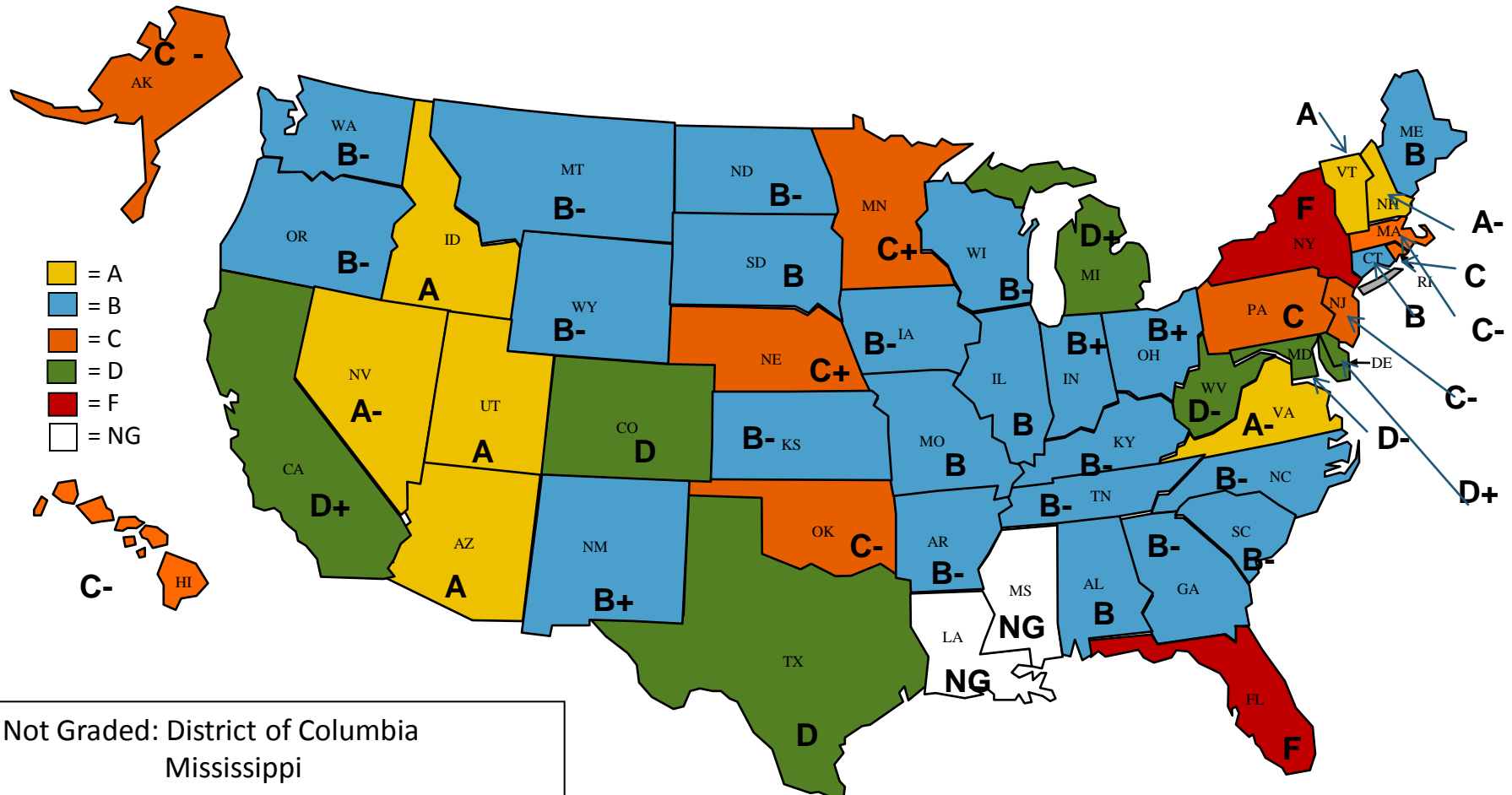
### ■ Federal Insurance Office (FIO)

- Establishes the FIO (while maintaining state regulation of insurance) within the Department of Treasury, headed by a Director appointed by the Secretary of Treasury
- FIO will have authority to monitor the insurance industry, identify regulatory gaps that could contribute to systemic crisis
- **CONCERN: FIO morphs into quasi/shadow or actual regulator**

### ■ Surplus Lines/Reinsurance

- Title V of the Dodd-Frank bill includes, as a separate subtitle, the Nonadmitted and Reinsurance Reform Act (NRRA), which eliminates regulatory inefficiencies associated with surplus lines insurance and reinsurance

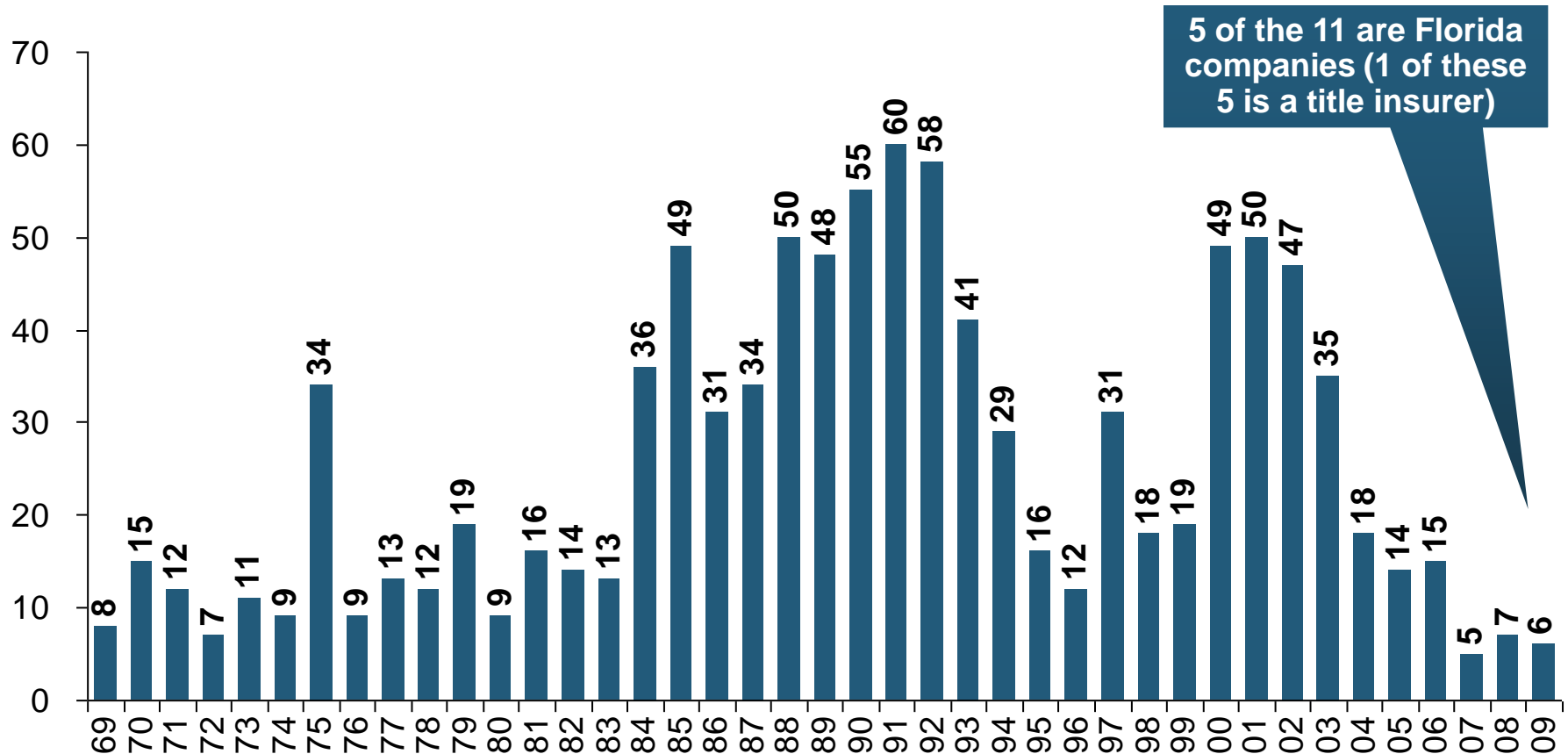
# 2010 Property and Casualty Insurance Report Card



# **Financial Strength & Ratings**

**Industry Has Weathered  
the Storms Well**

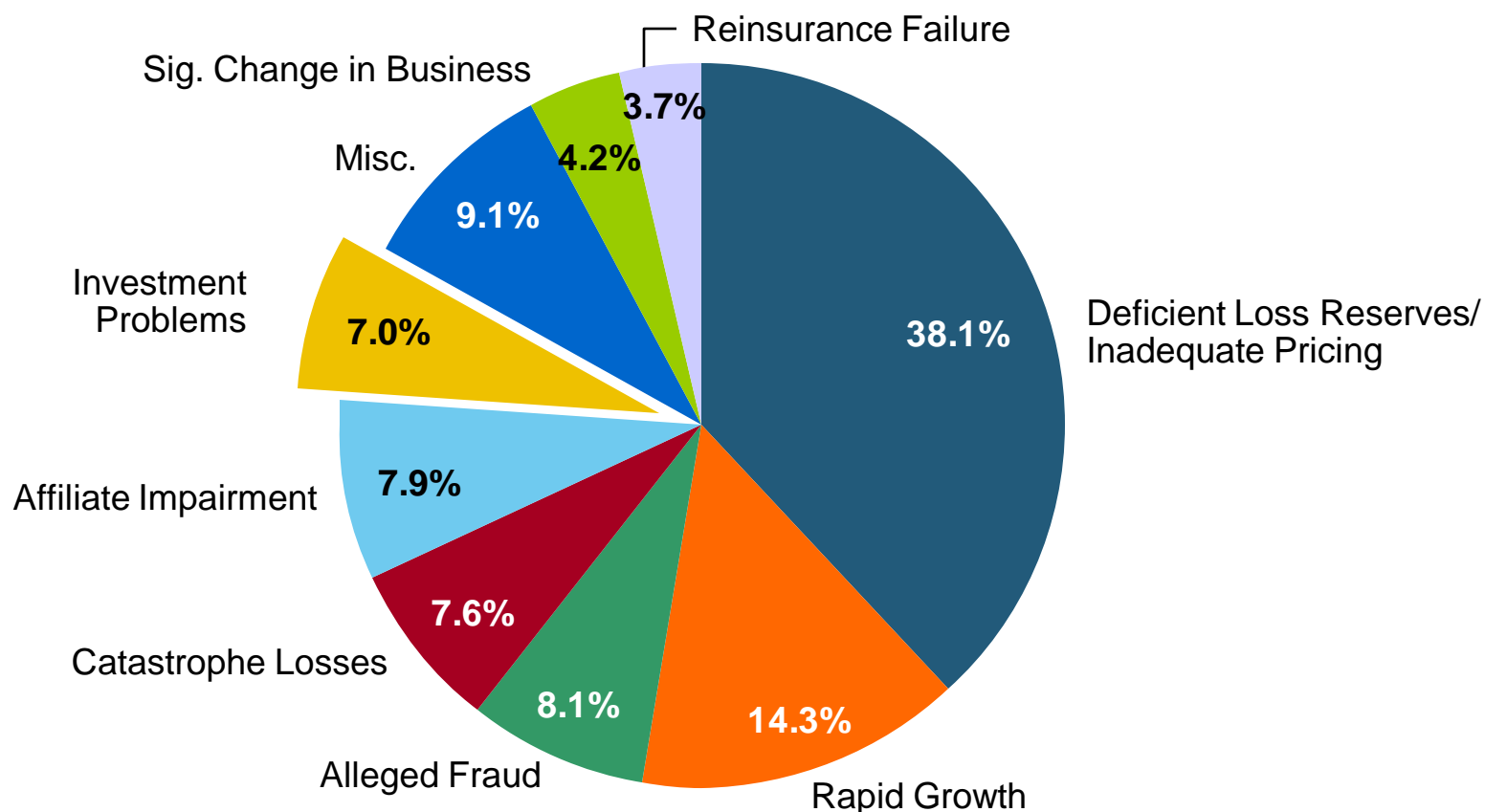
# P/C Insurer Impairments, 1969–2009



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

# 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**



# **Critical Differences Between P/C Insurers and Banks**

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

# How P/C Insurance Industry Stability Has Benefitted Consumers

## Bottom Line:

- Insurance markets – unlike banking – are operating **normally**
- The basic function of insurance – the orderly transfer of risk from client to insurer – **continues uninterrupted**
- This means that insurers continue to:
  - ◆ Pay claims (whereas 307 banks have gone under as of 10/22/10)
    - **The promise is being fulfilled**
  - ◆ Renew existing policies (*banks are reducing and eliminating lines of credit*)
  - ◆ Write new policies (*banks are turning away people and businesses who want or need to borrow*)
  - ◆ Develop new products (*banks are scaling back the products they offer*)
  - ◆ Compete intensively (*banks are consolidating, reducing consumer choice*)

# **Shifting Legal Liability & Tort Environment**

## **Is the Tort Pendulum Swinging Against Insurers?**

# Important Issues & Threats Facing Insurers: 2010–2015



## Emerging Tort Threat

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

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

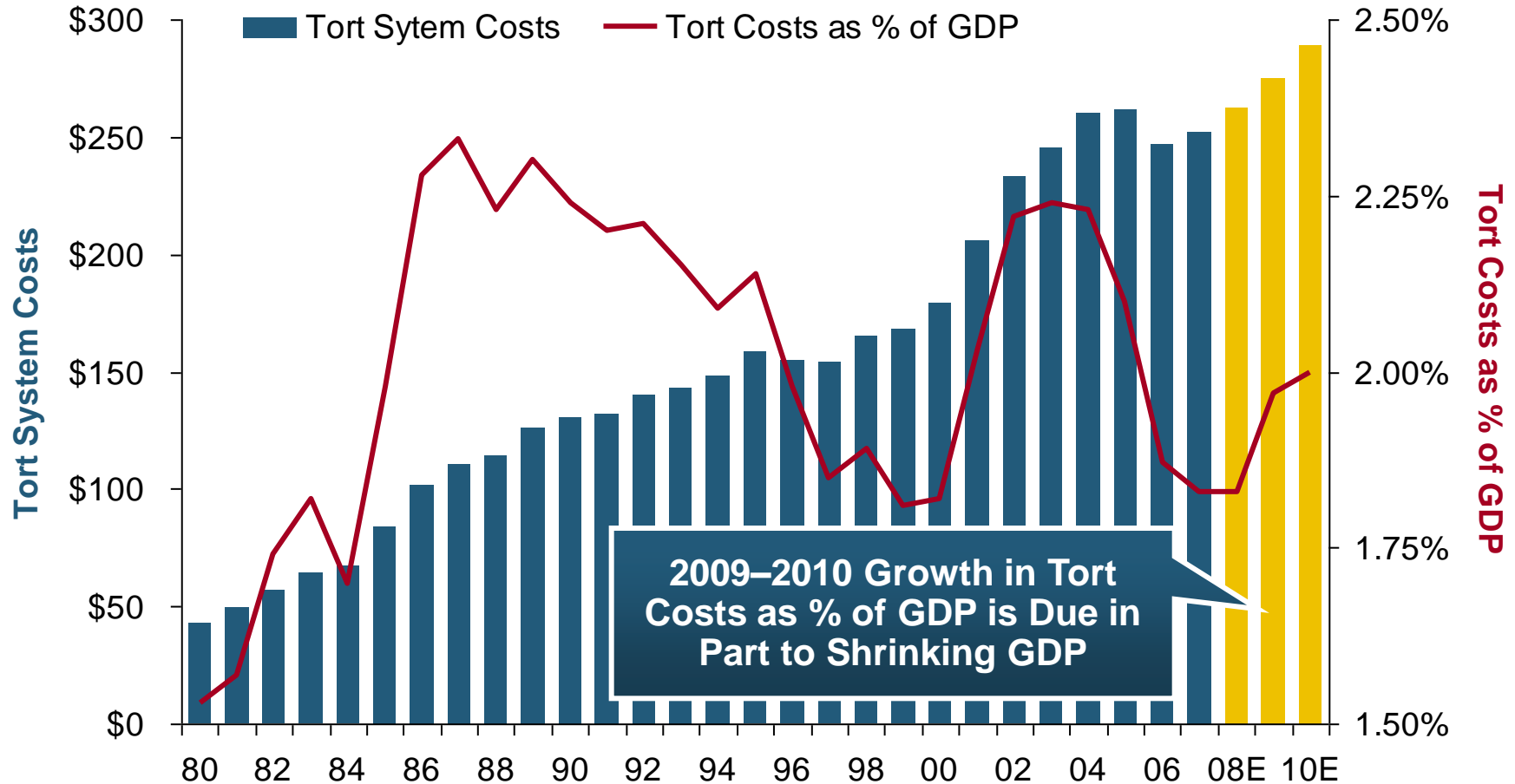


AMERICAN  
ASSOCIATION *for*  
**JUSTICE**

- **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**

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

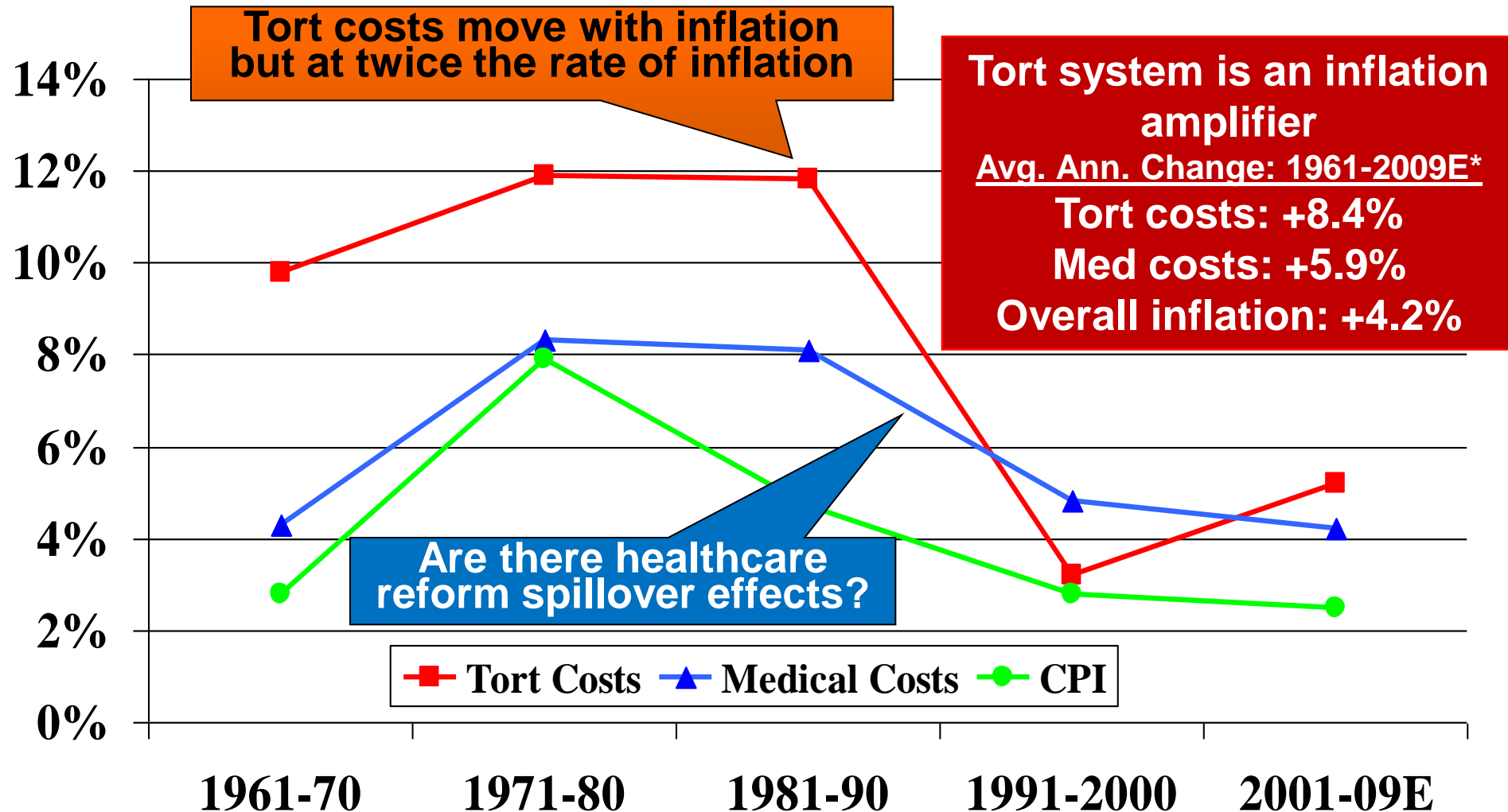
(\$ Billions)



\* 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

# 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.

# Business Leaders Ranking of Liability Systems in 2009\*

## ■ Best States

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

### New in 2009

- North Dakota
- Massachusetts
- South Dakota

### Drop-offs

- Maine
- Vermont
- Kansas

Midwest/West has mix of good and bad states.

## ■ Worst States

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

### Newly Notorious

- New Mexico
- Montana
- Arkansas

### Rising Above

- **Texas**
- South Carolina
- Hawaii

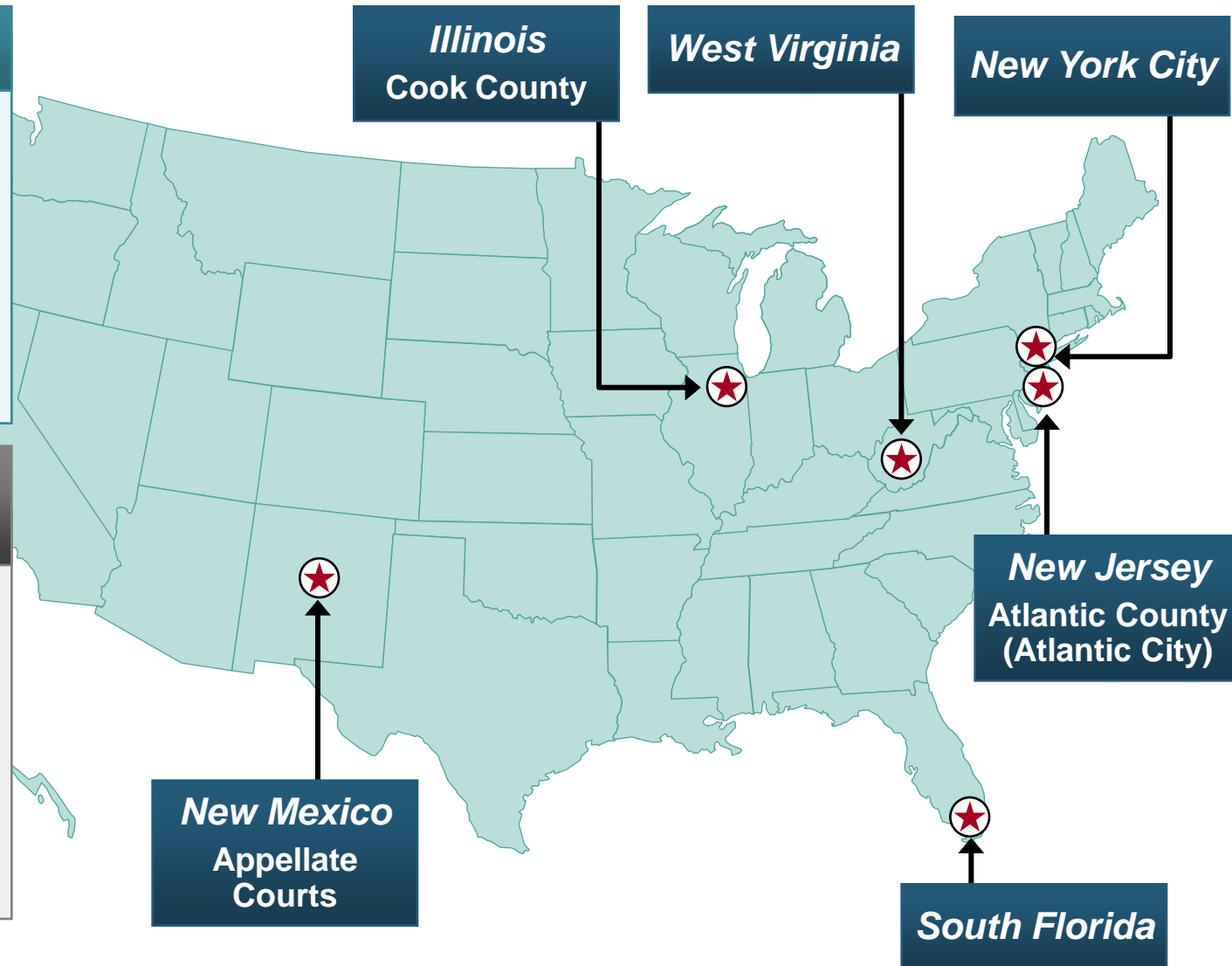
# The Nation's Judicial Hellholes: 2010

## Watch List

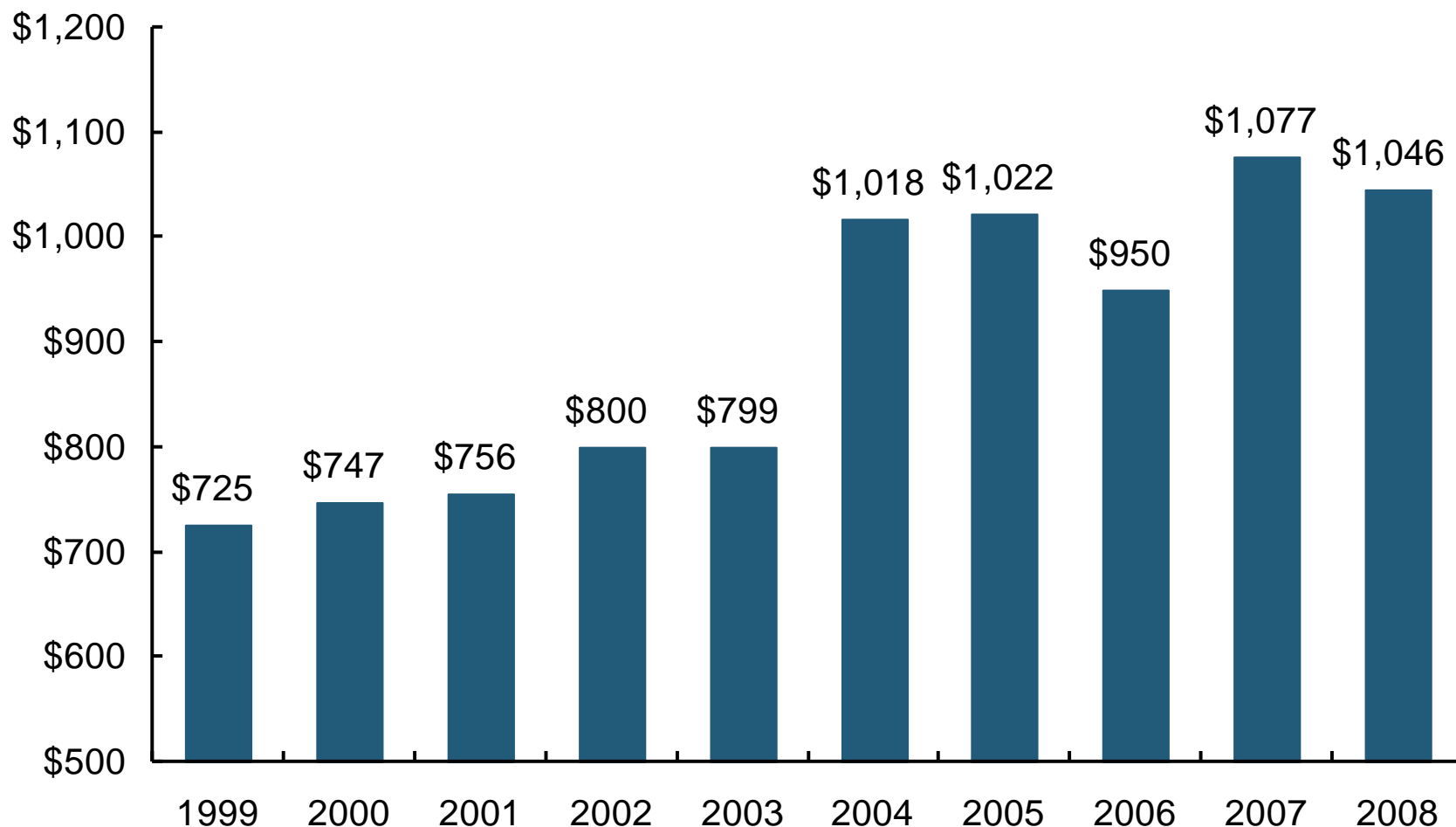
- California
- Alabama
- Madison County, IL
- Jefferson County, MS
- Texas Gulf Coast
- Rio Grande Valley, TX

## Dishonorable Mention

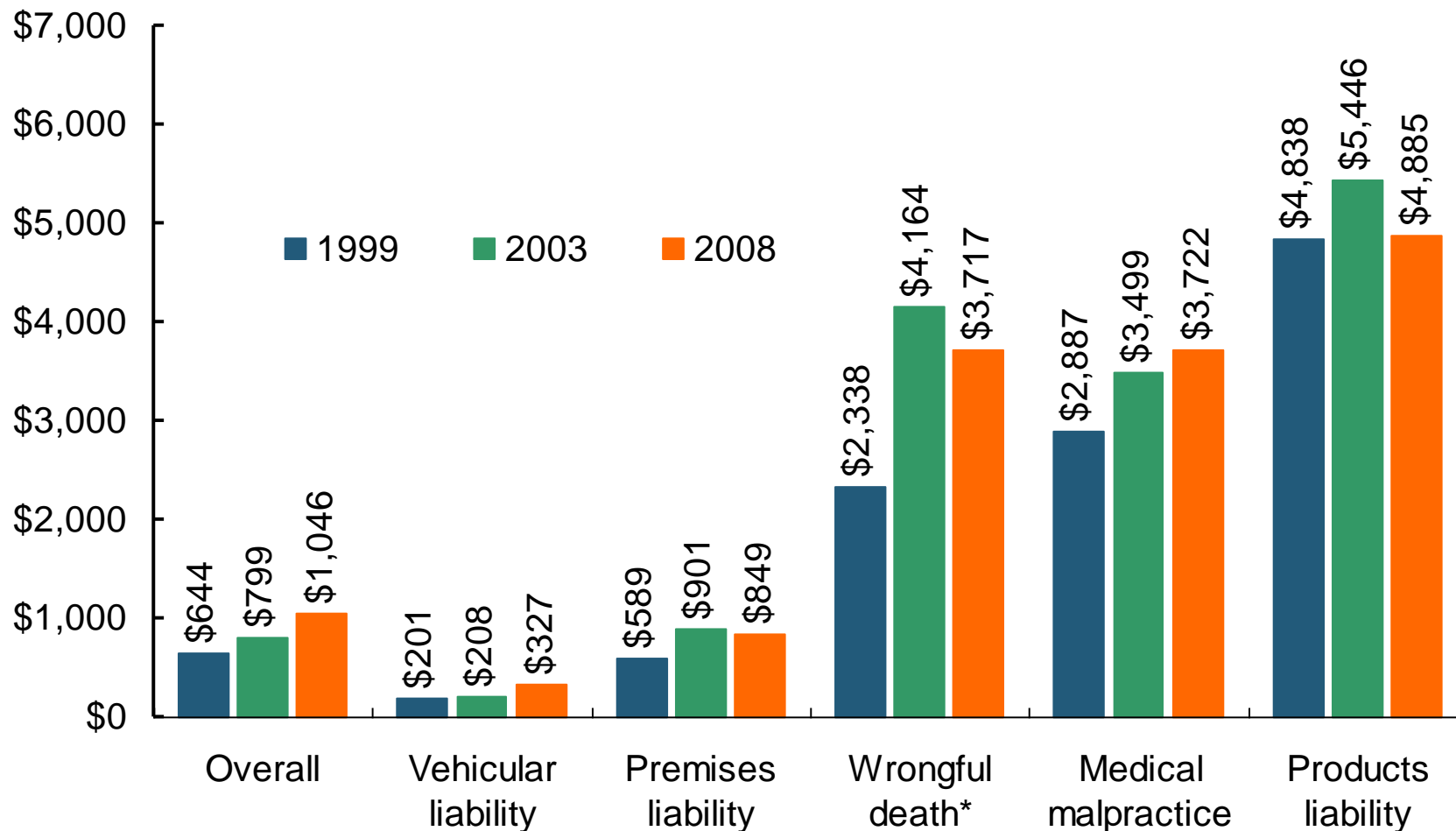
- AR Supreme Court
- MN Supreme Court
- ND Supreme Court
- PA Governor
- MA Supreme Judicial Court
- Sacramento County



# Average Jury Awards 1999 - 2008



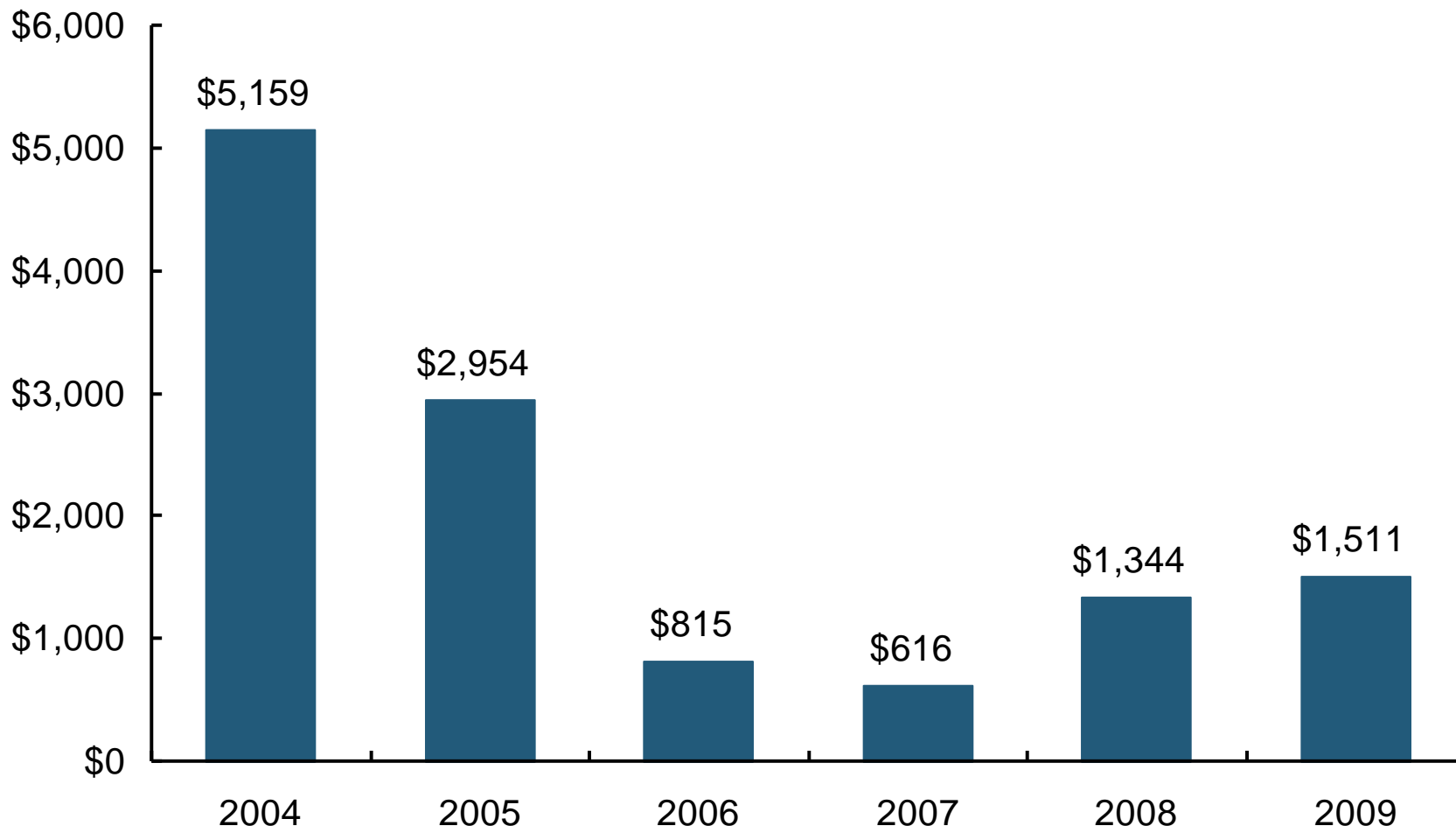
# Avg. Jury Awards 1999 vs. 2003 and 2008



\*Award trends in wrongful deaths of adult males.

Source: Jury Verdict Research; Insurance Information Institute.

# Sum of Top 10 Jury Awards 2004-2009



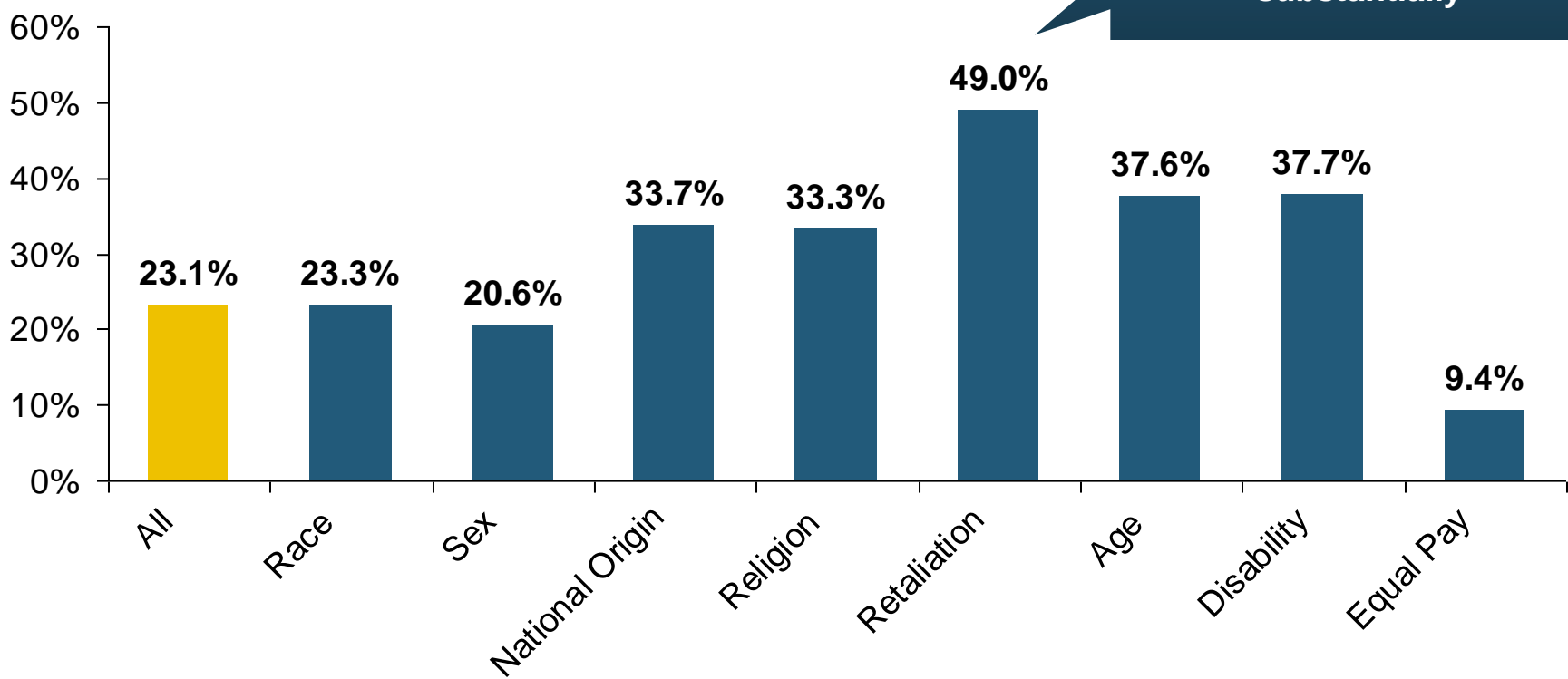
Source: Insurance Information Institute from Lawyers USA, January 2005, 2006, 2007, 2008, 2009 and 2010.

# 2009 Top Ten Jury Verdicts

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

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

Change in Charges Filed (%)



Retaliation and age discrimination suits are up substantially

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

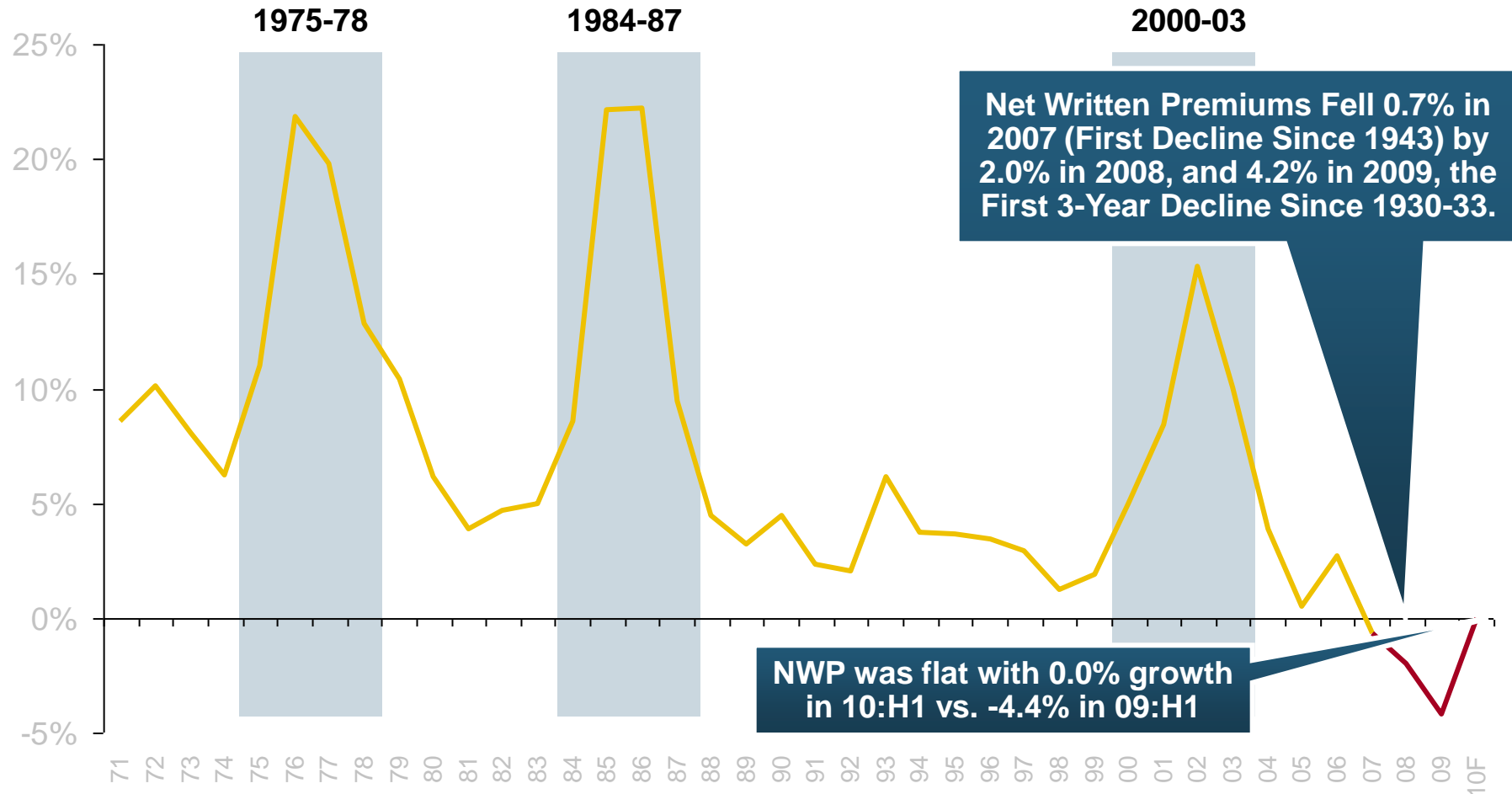
Source: Equal Opportunity Employment Commission; Insurance Information Institute.

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

**Personal and Commercial Lines  
Pricing Trends**

# Soft Market Appears to Persist in 2010 but May Be Easing: Relief in 2011?

(Percent)



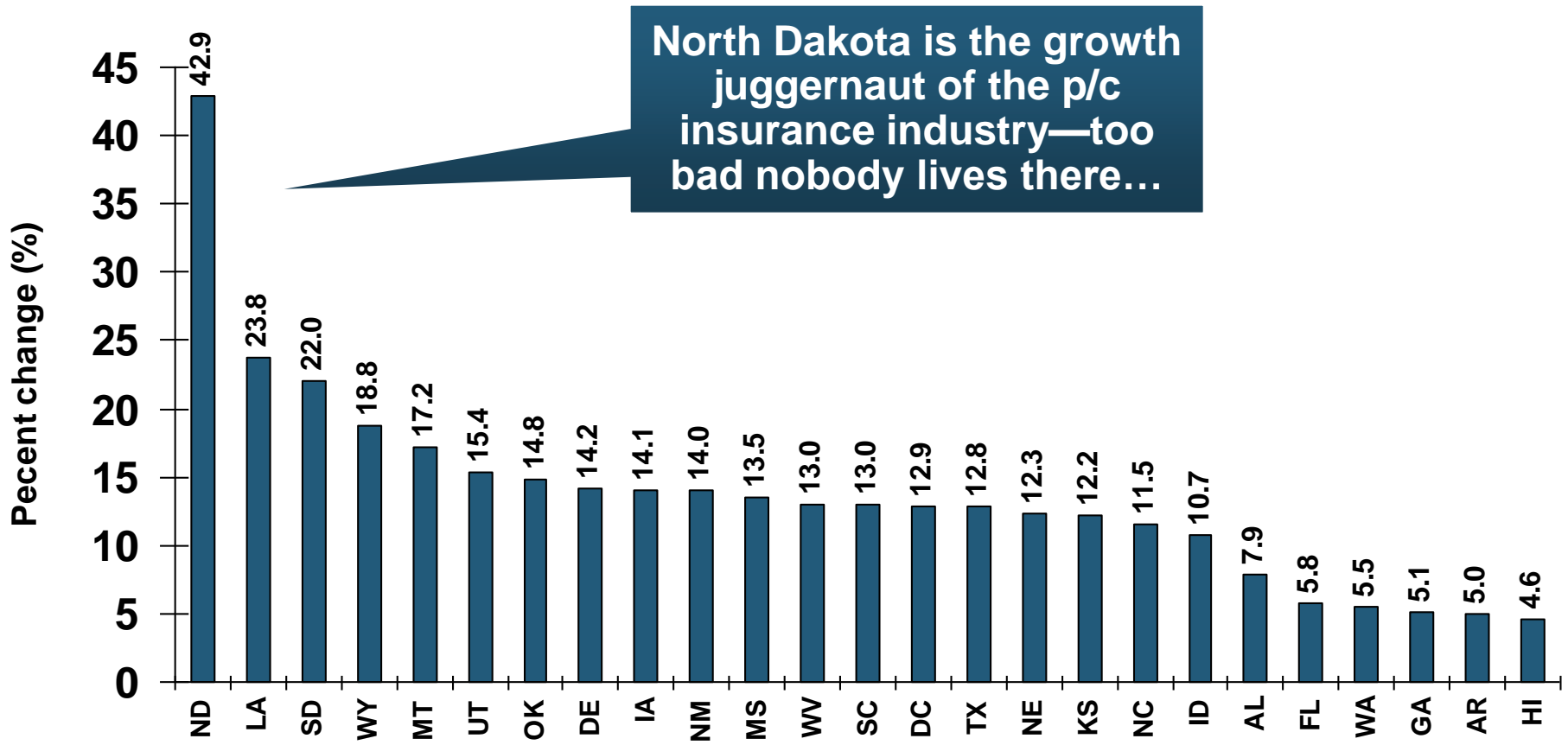
Shaded areas denote "hard market" periods

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

# Direct Premiums Written: All Lines

## Percent change by State, 2004-2009

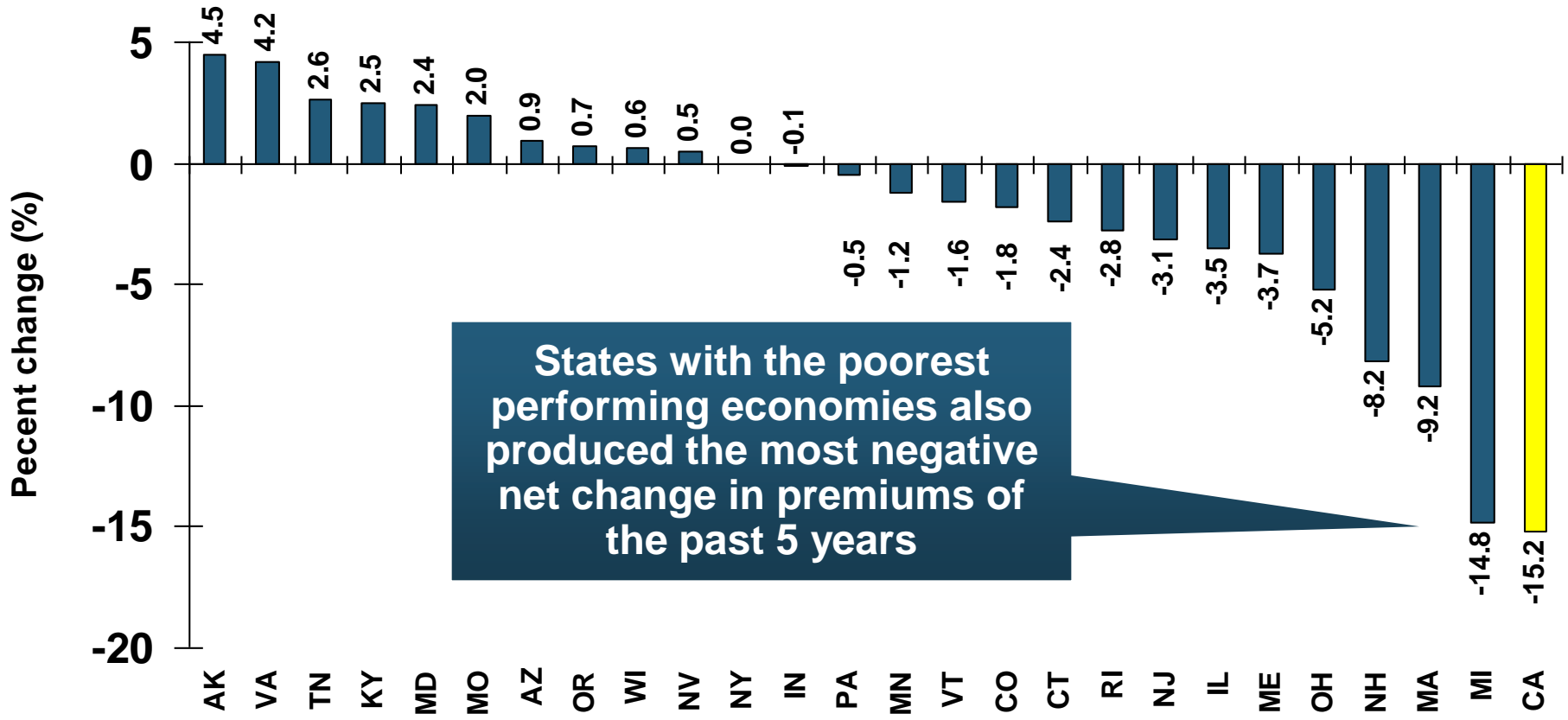
### Top 25 States



# Direct Premiums Written: All Lines

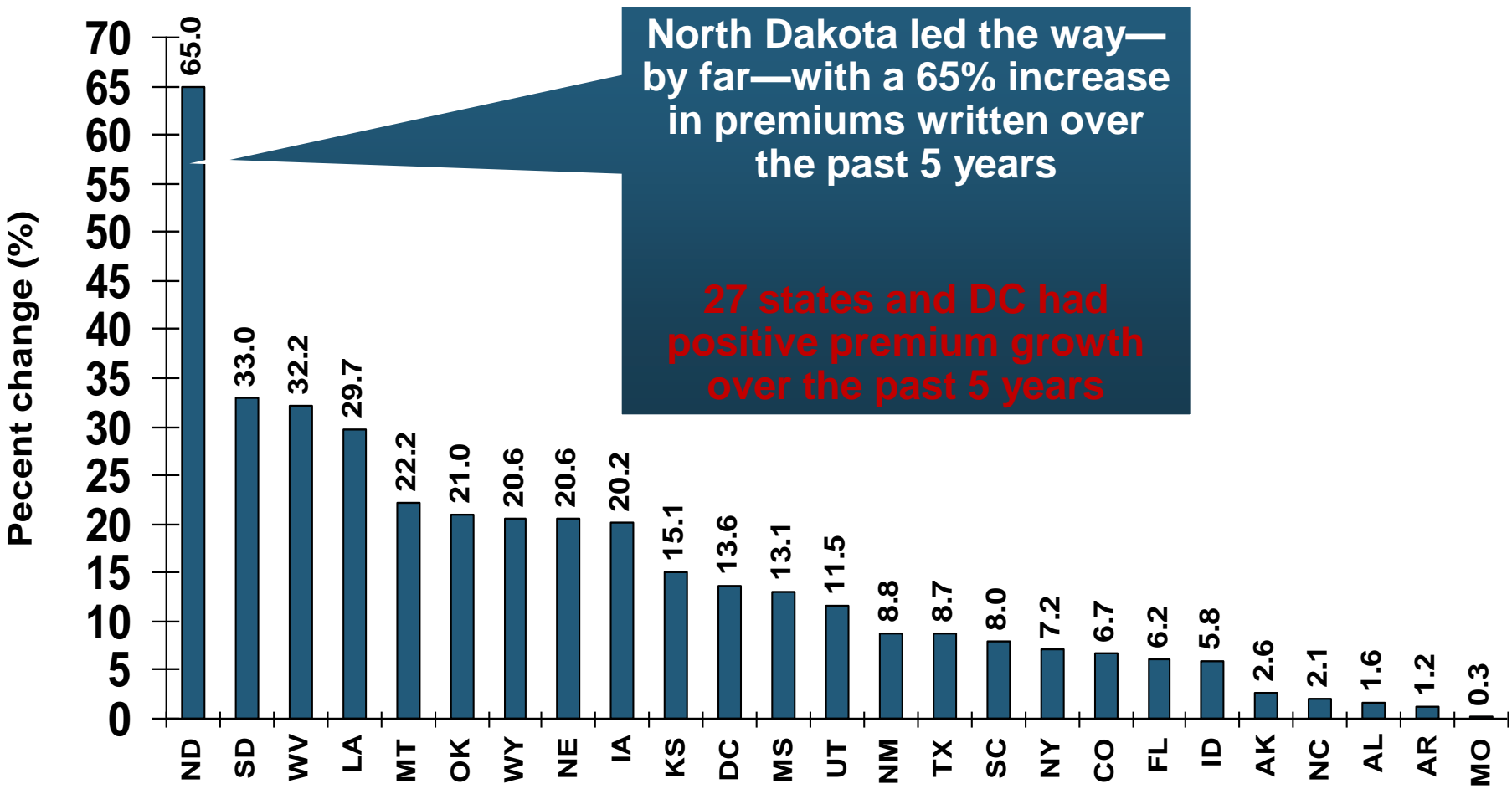
## Percent change by State, 2004-2009

### Bottom 25 States



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

## Top 25 States

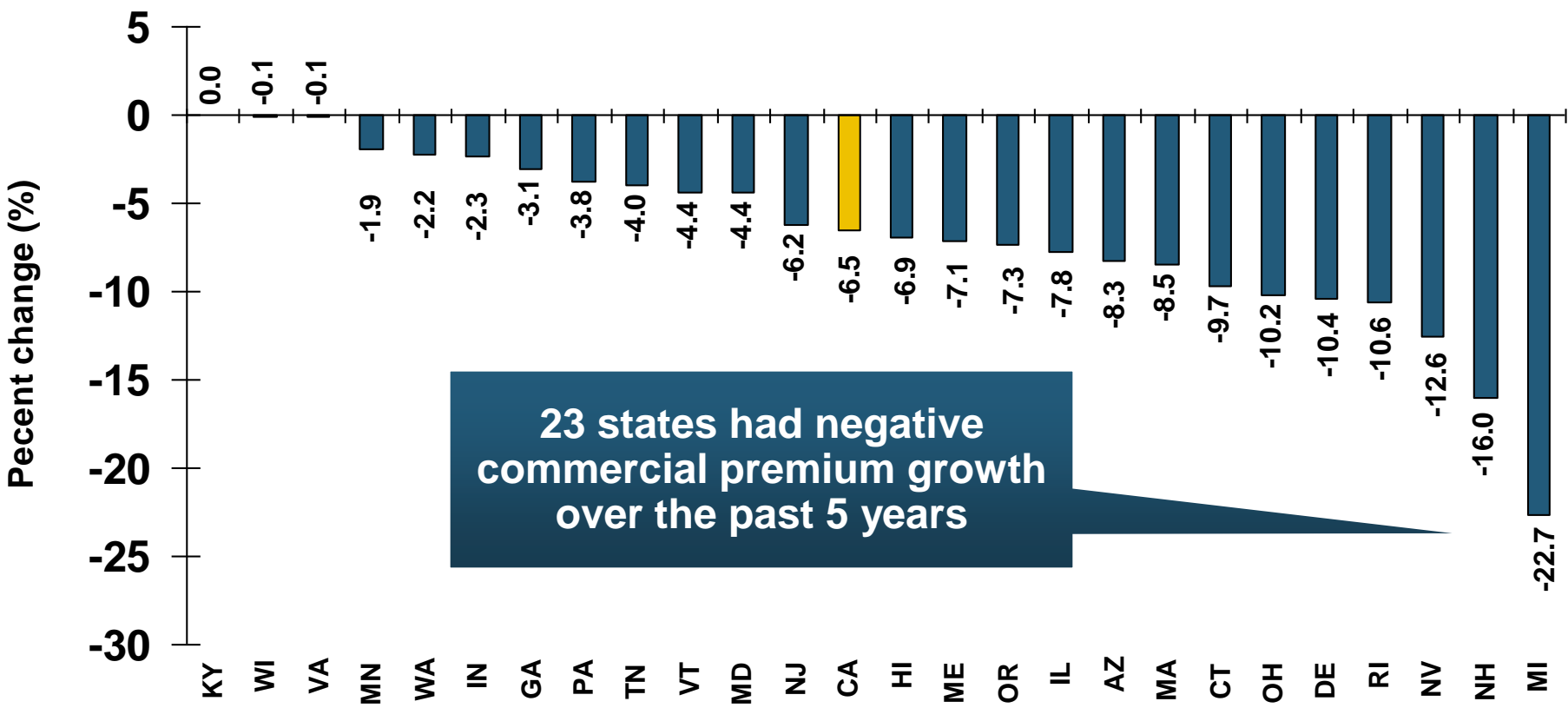


Sources: SNL Financial LC.; Insurance Information Institute.

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



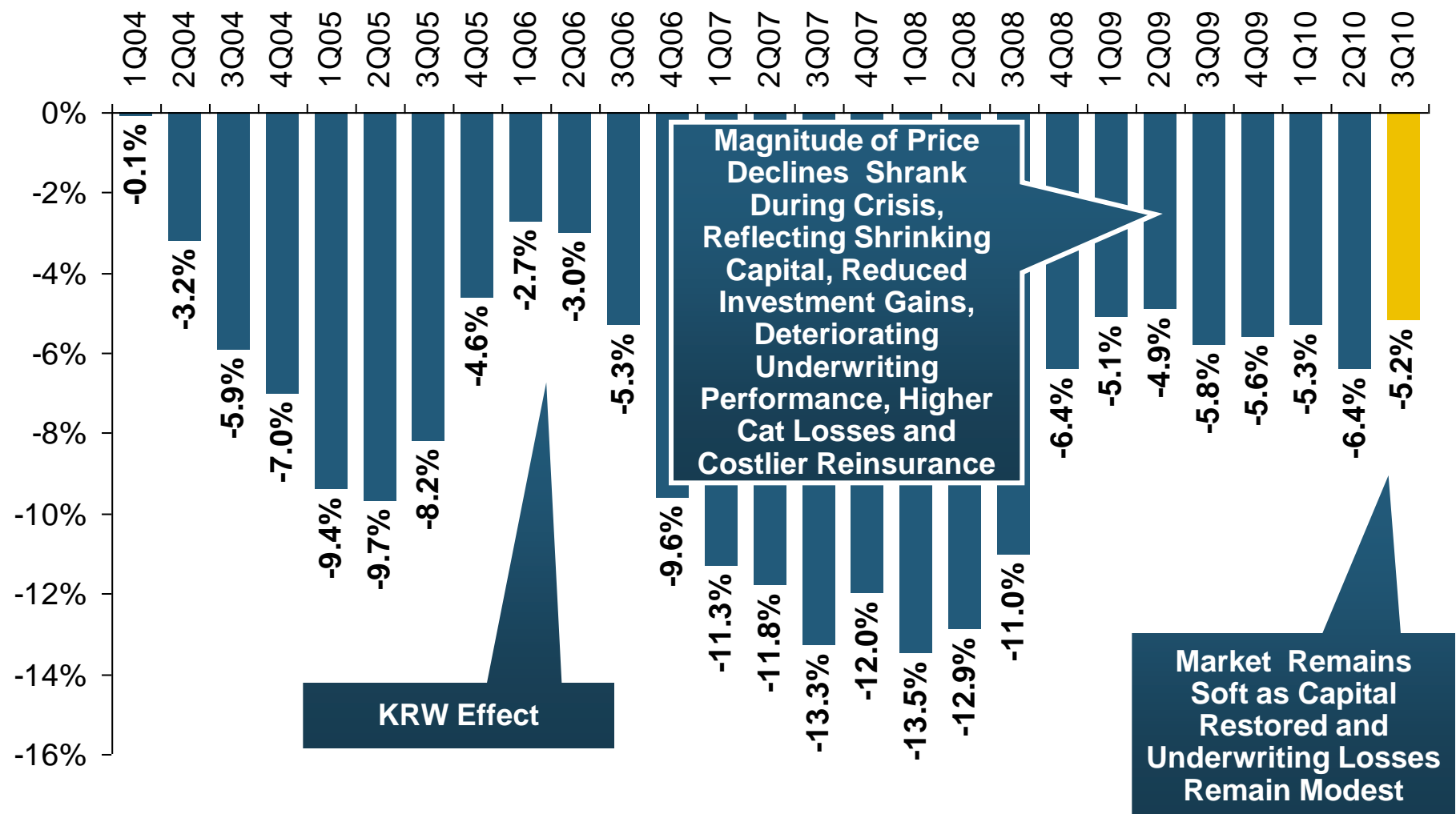
## Bottom 25 States



Sources: SNL Financial LC.; Insurance Information Institute.

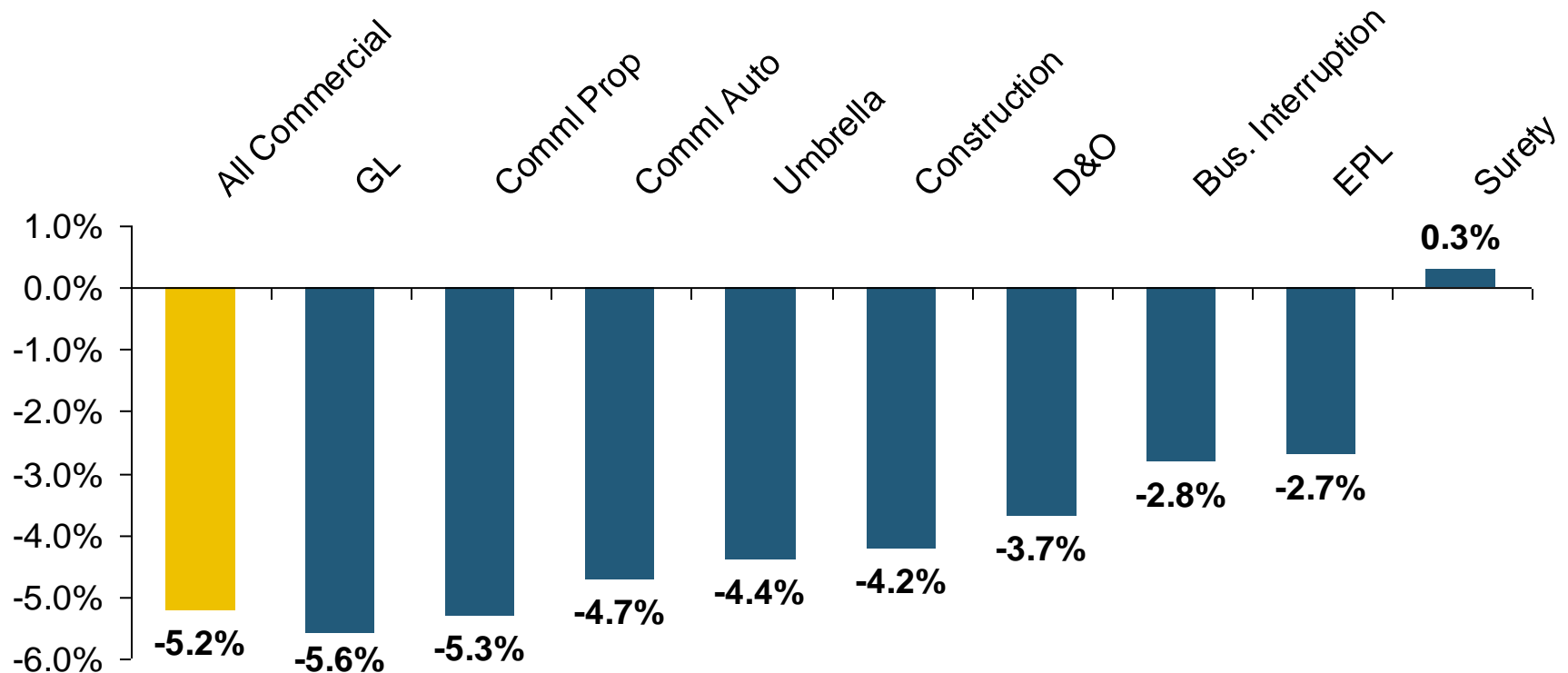
# Average Commercial Rate Change, All Lines, (1Q:2004–3Q:2010)

(Percent)



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

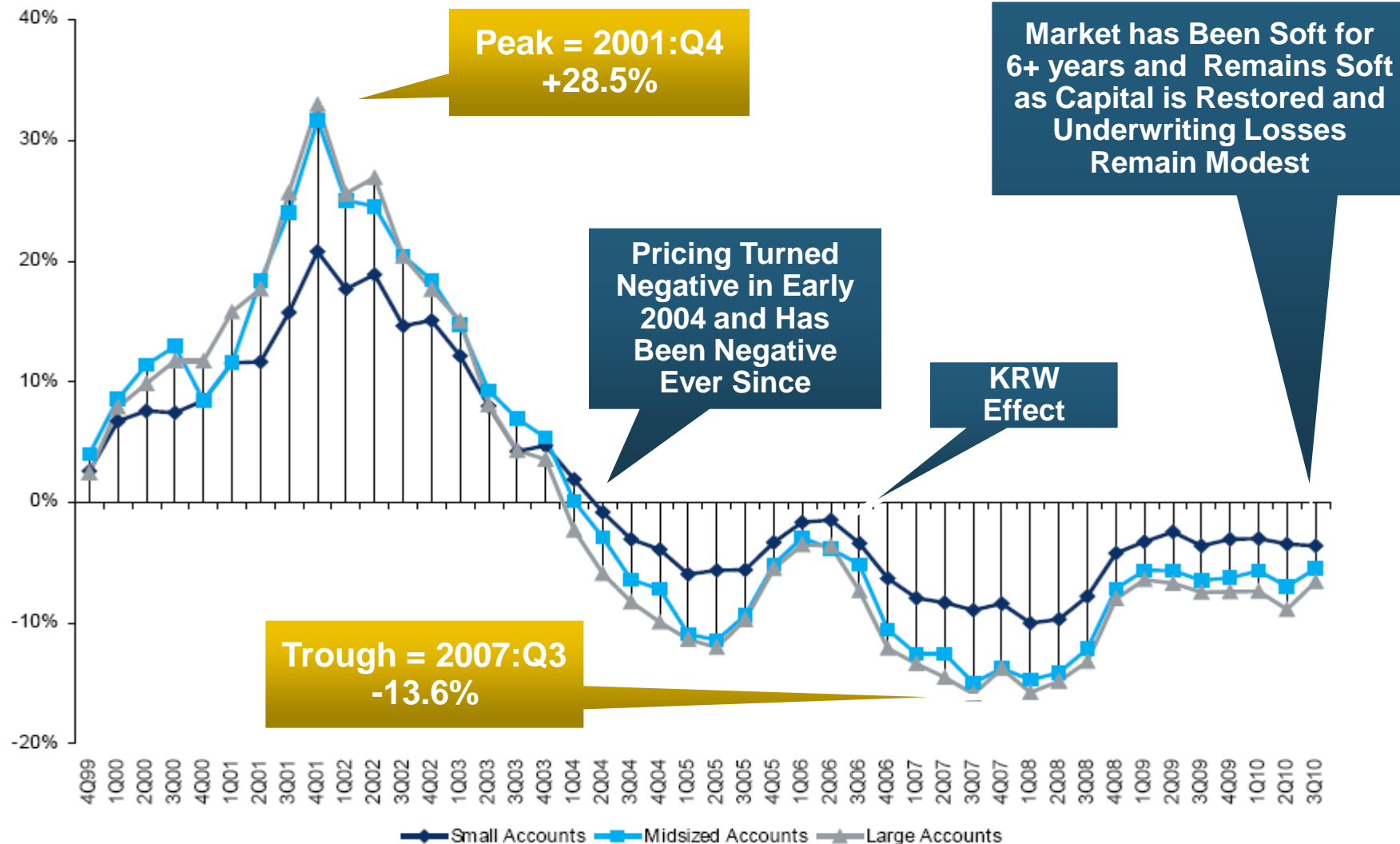
Percentage Change (%)



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

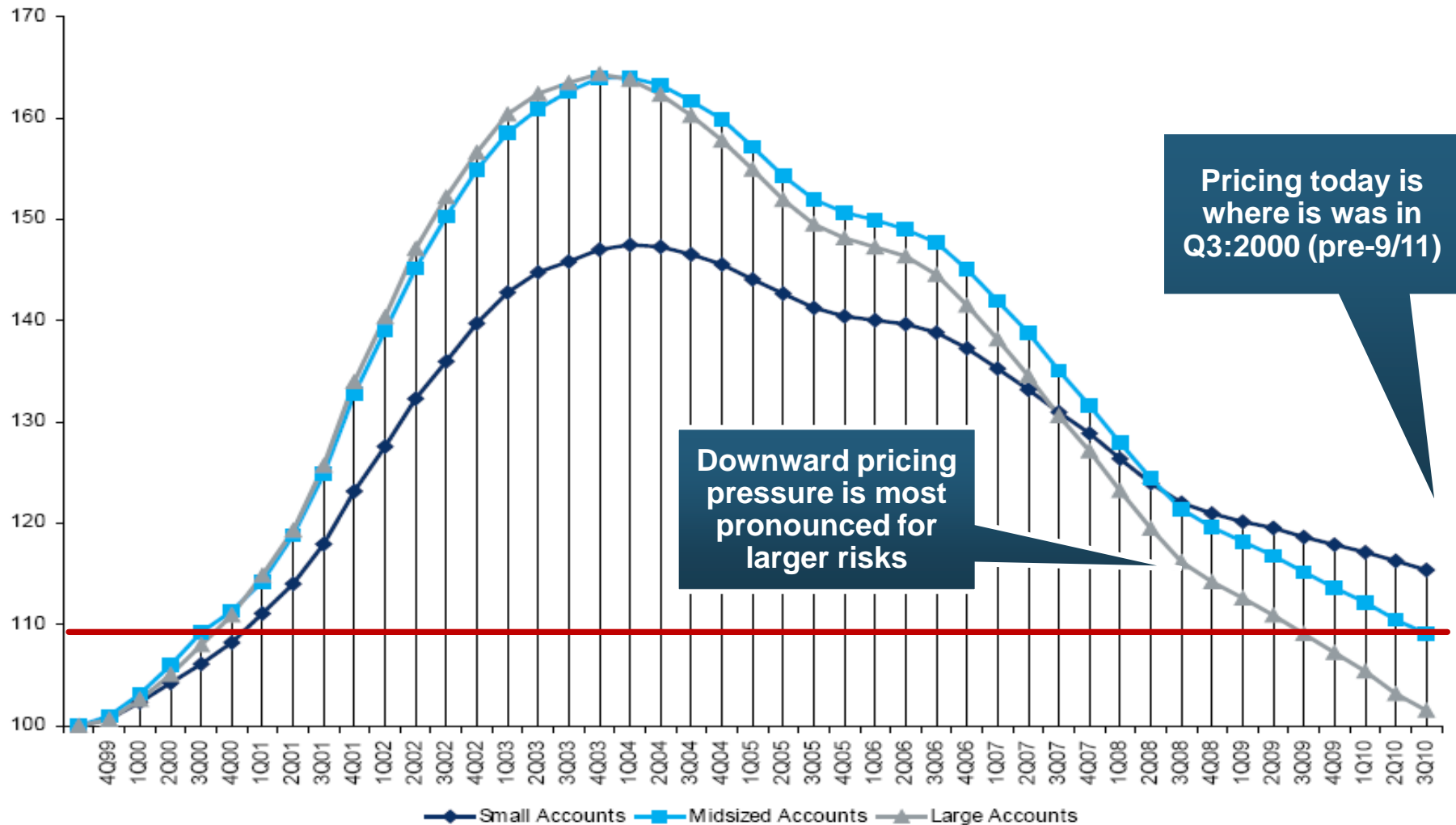
# Change in Commercial Rate Renewals, by Account Size: 1999:Q4 to 2010:Q3

Percentage Change (%)



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

1999:Q4 = 100

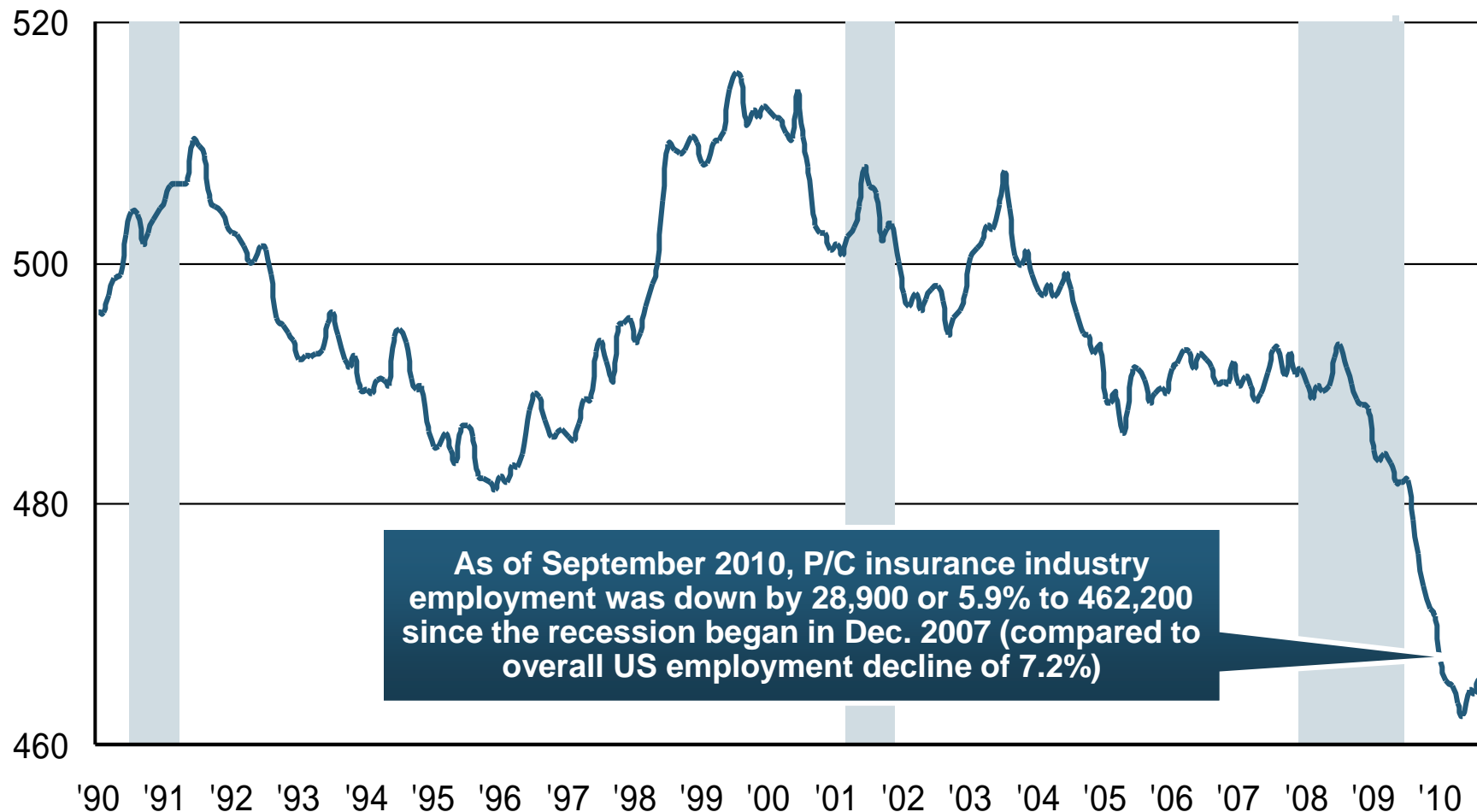


# **Insurance Industry Employment Trends**

**Soft Market, Difficult Economy,  
Outsourcing, Productivity  
Enhancements and  
Consolidation Have Contributed  
to Industry's Job Losses**

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

Thousands



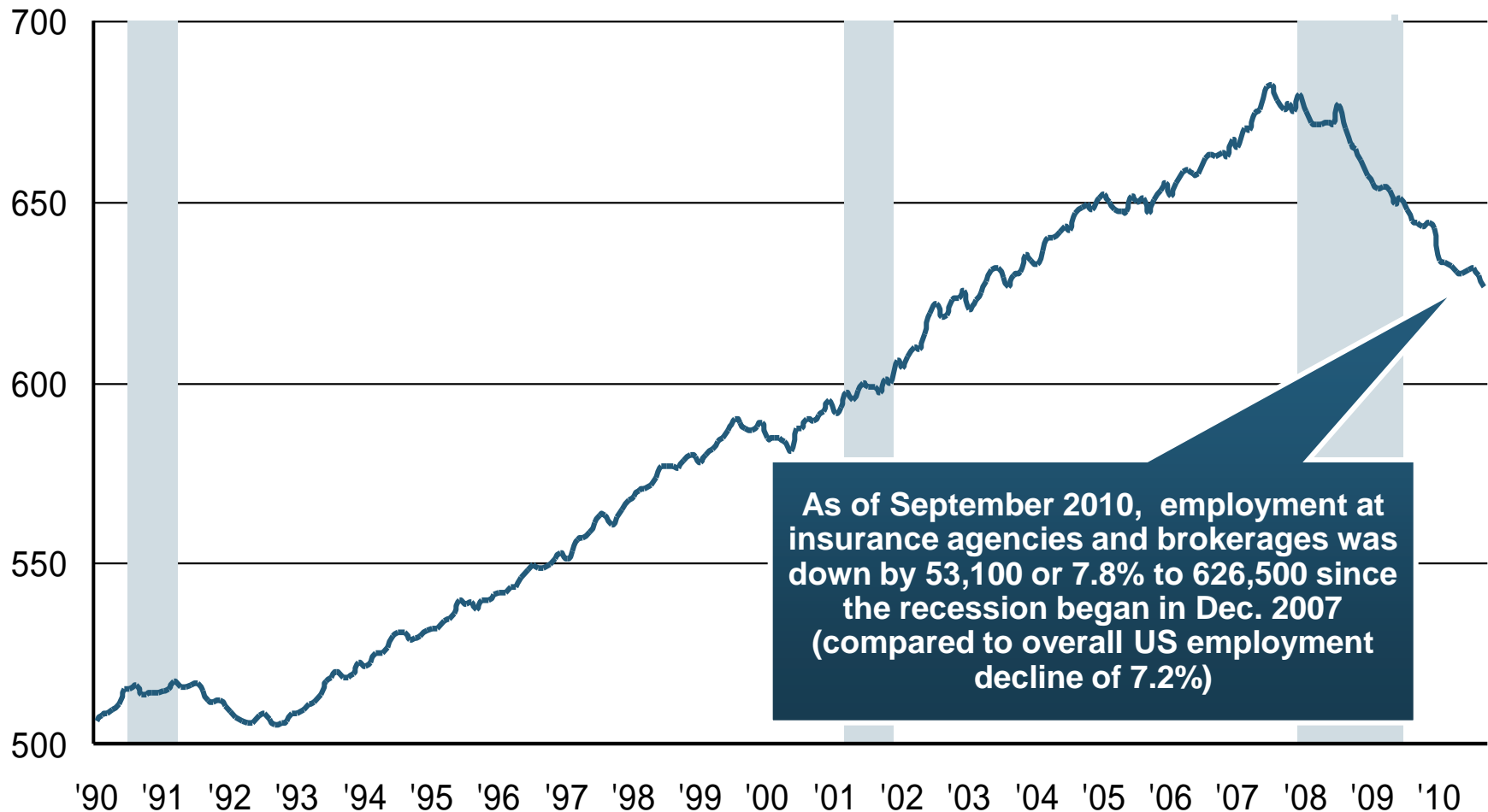
\*As of September 2010; Not seasonally adjusted; Does not including agents & brokers

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 September 2010; Not seasonally adjusted. Includes all types of insurance.

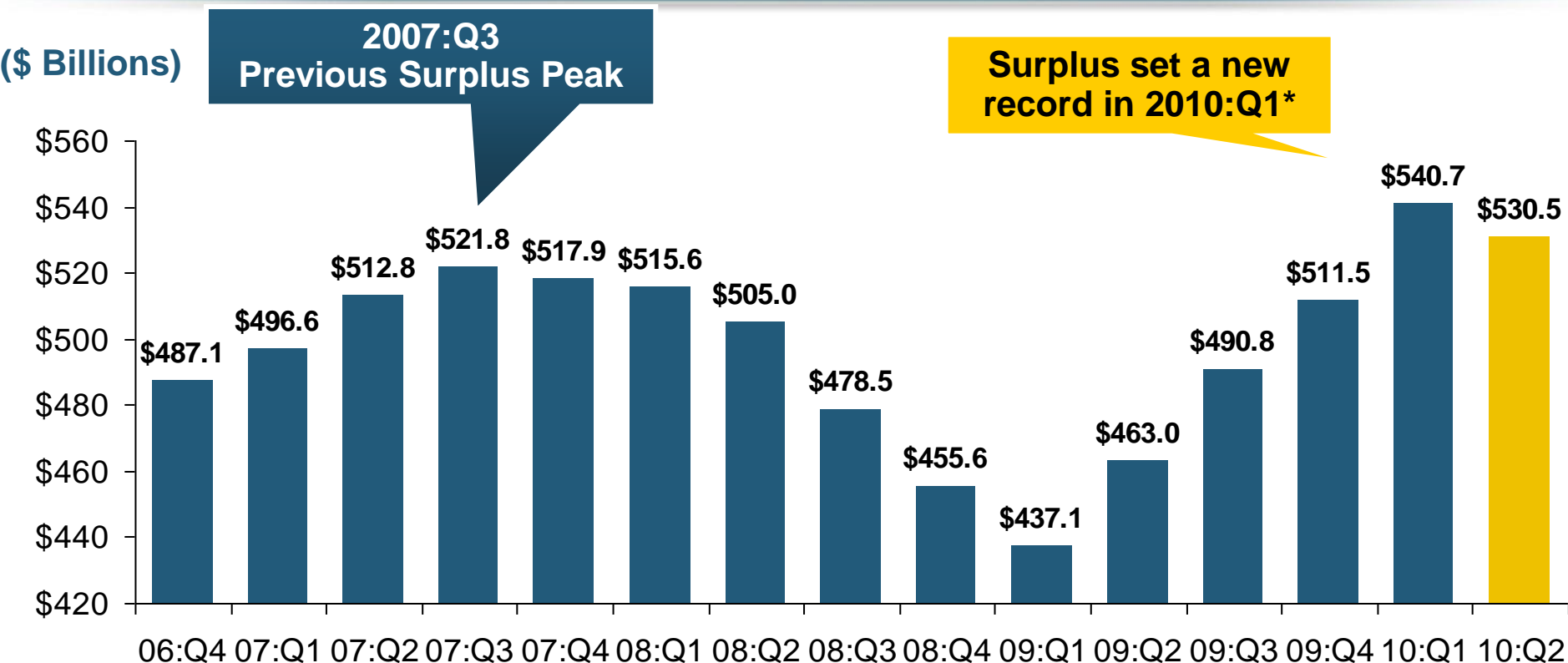
Note: Recessions indicated by gray shaded columns.

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

# **Capital/Policyholder Surplus (US)**

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

# Policyholder Surplus, 2006:Q4–2010:Q2



## Quarterly Surplus Changes Since 2009:Q1 Trough

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

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

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

**10:Q2: -\$10.2B (-1.9%)**

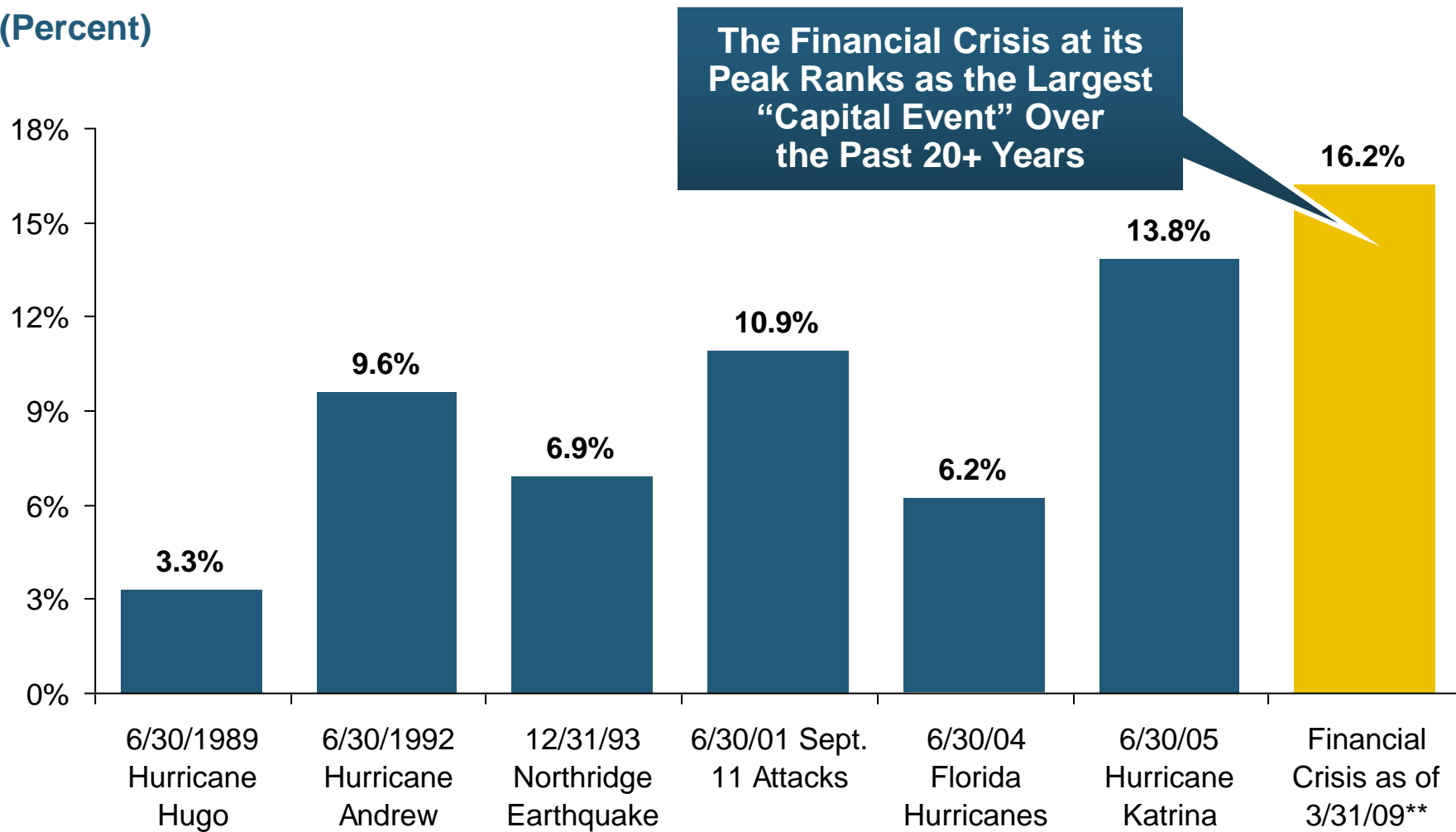
**09:Q3: -\$31.8B (-5.9%)**

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

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

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

(Percent)



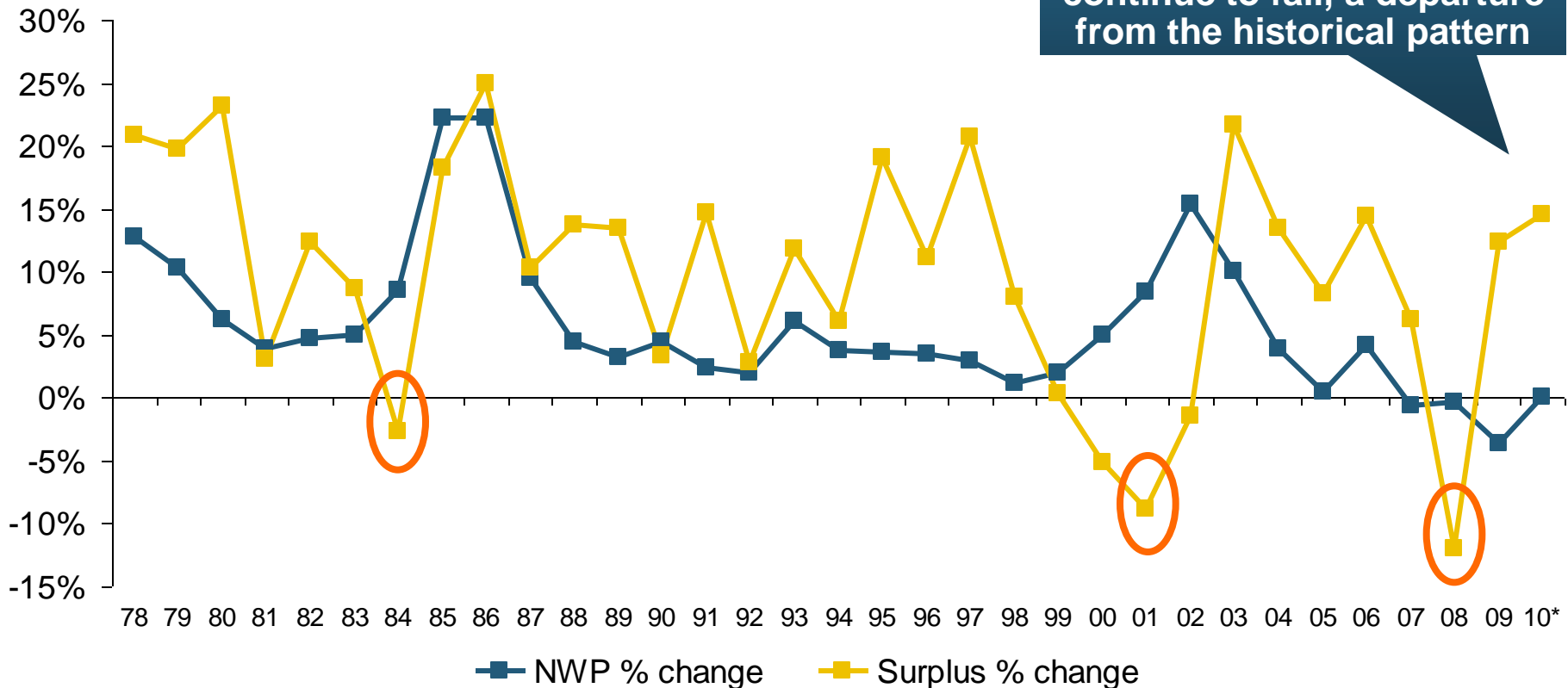
\* Ratio is for end-of-quarter surplus immediately prior to event. Date shown is end of quarter prior to event

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

Source: PCS; Insurance Information Institute

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

(Percent)



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

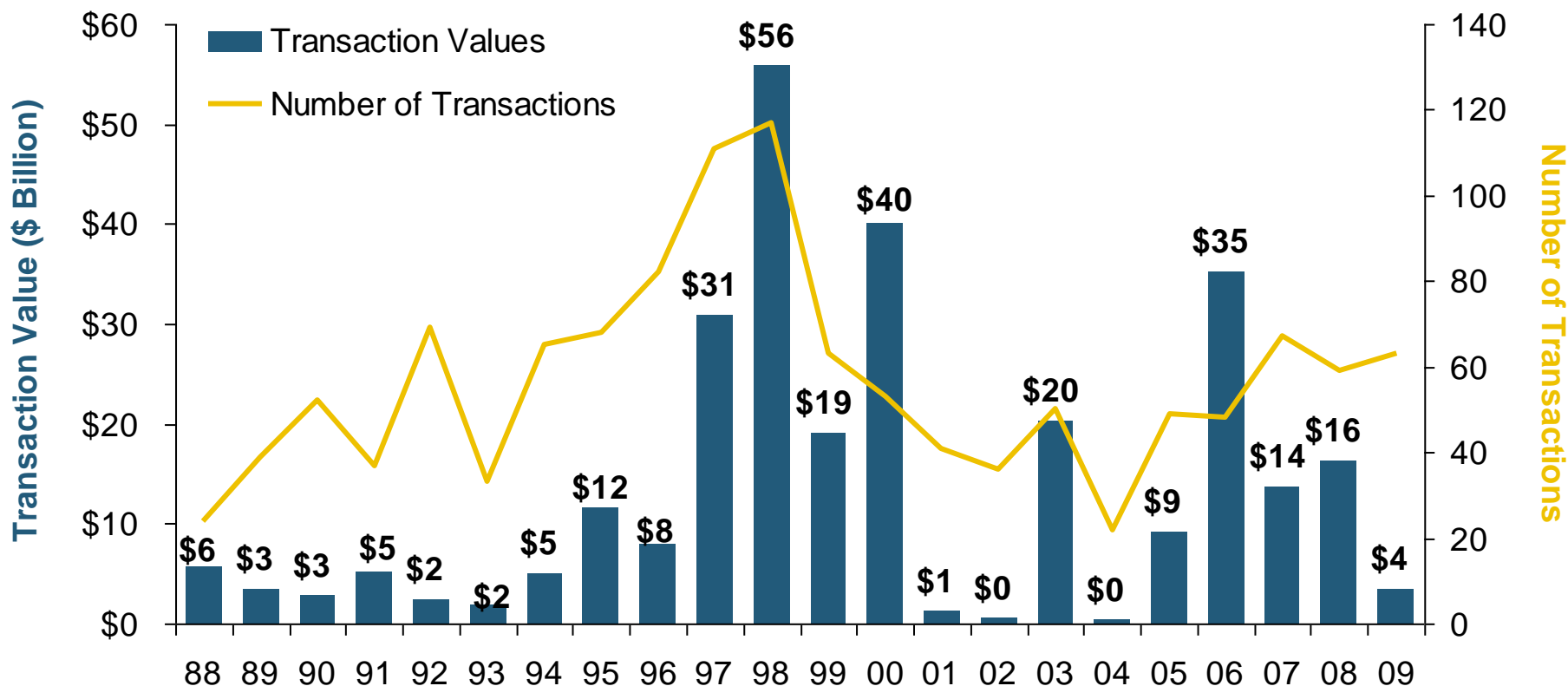
\* 2010 NWP and Surplus figures are % changes as of H1:10 vs H1:09.

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.

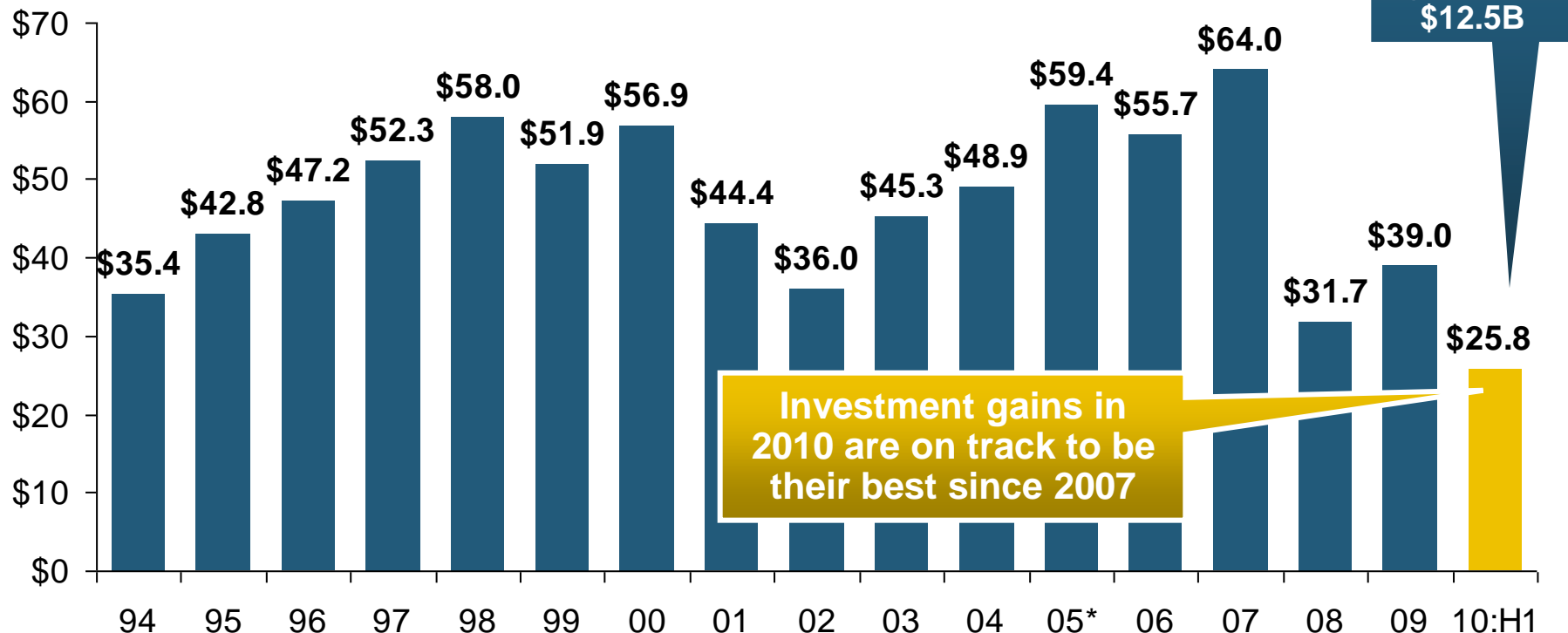
Source: Conning Research & Consulting.

# **Investment Performance**

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

# Property/Casualty Insurance Industry Investment Gain: 1994–2010:H1<sup>1</sup>

(\$ Billions)



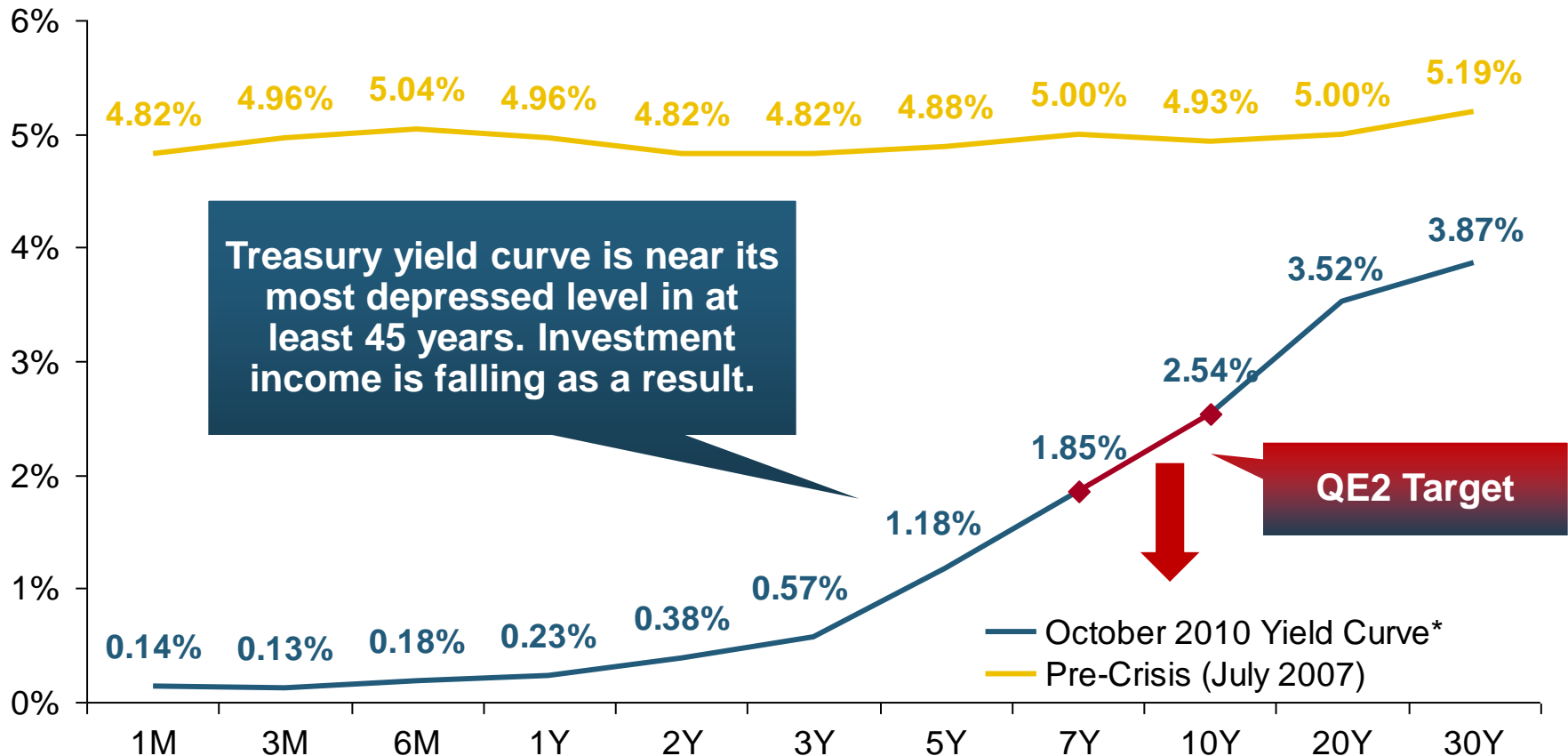
**In 2008, Investment Gains Fell by 50% Due to Lower Yields and Nearly \$20B of Realized Capital Losses**  
**2009 Saw Smaller Realized Capital Losses But Declining Investment Income**  
**Investment Gains Are Recovering So Far in 2010**

<sup>1</sup> Investment gains consist primarily of interest, stock dividends and realized capital gains and losses.

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

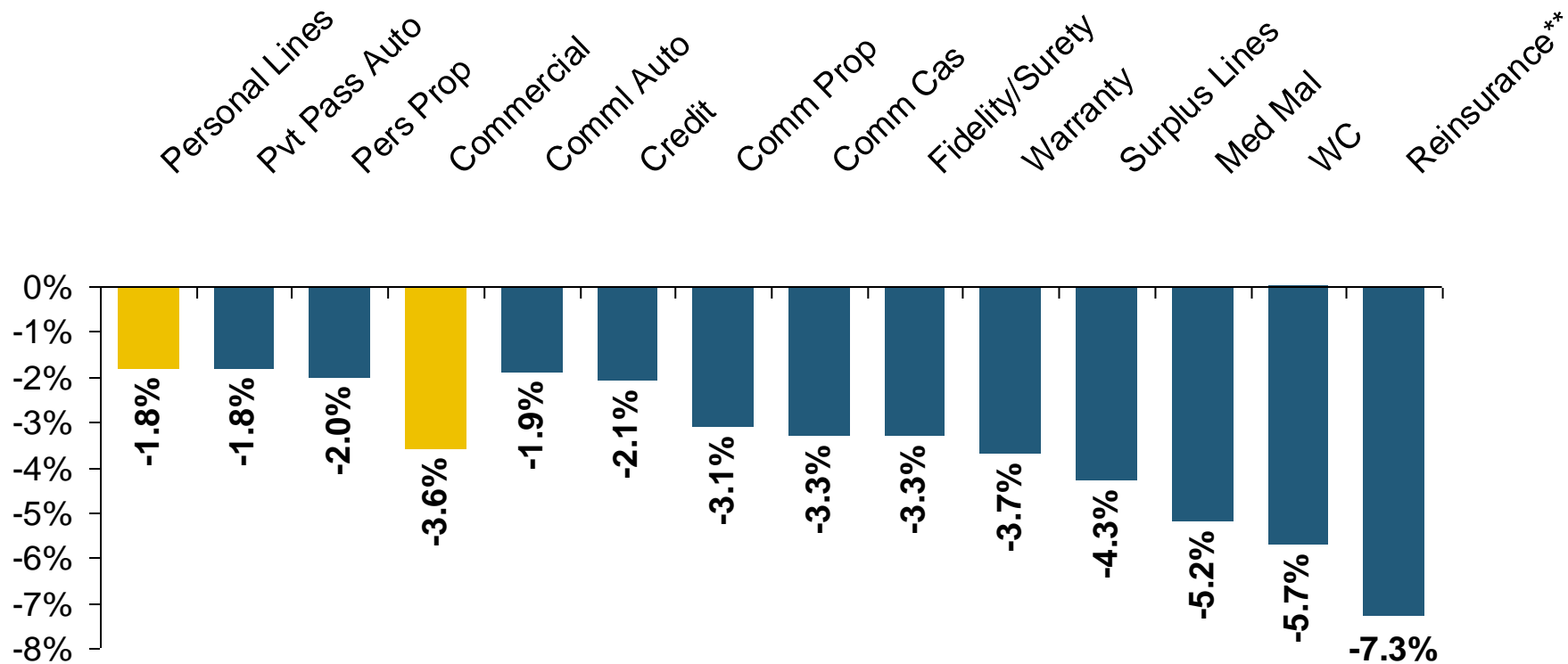
Sources: ISO; Insurance Information Institute.

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



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

# 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**

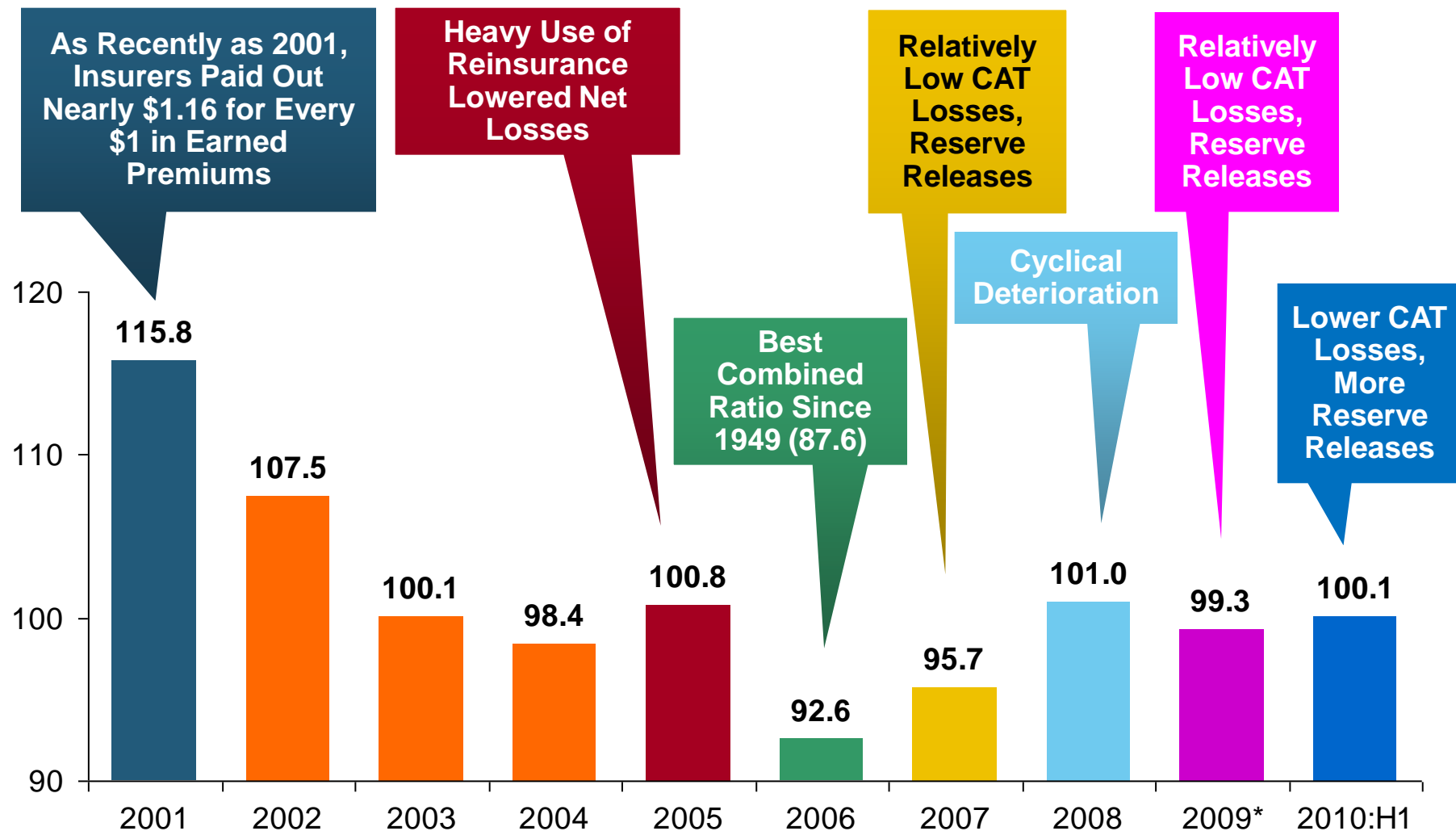
\*Based on 2008 Invested Assets and Earned Premiums

\*\*US domestic reinsurance only

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

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

# P/C Insurance Industry Combined Ratio, 2001–2010:H1\*

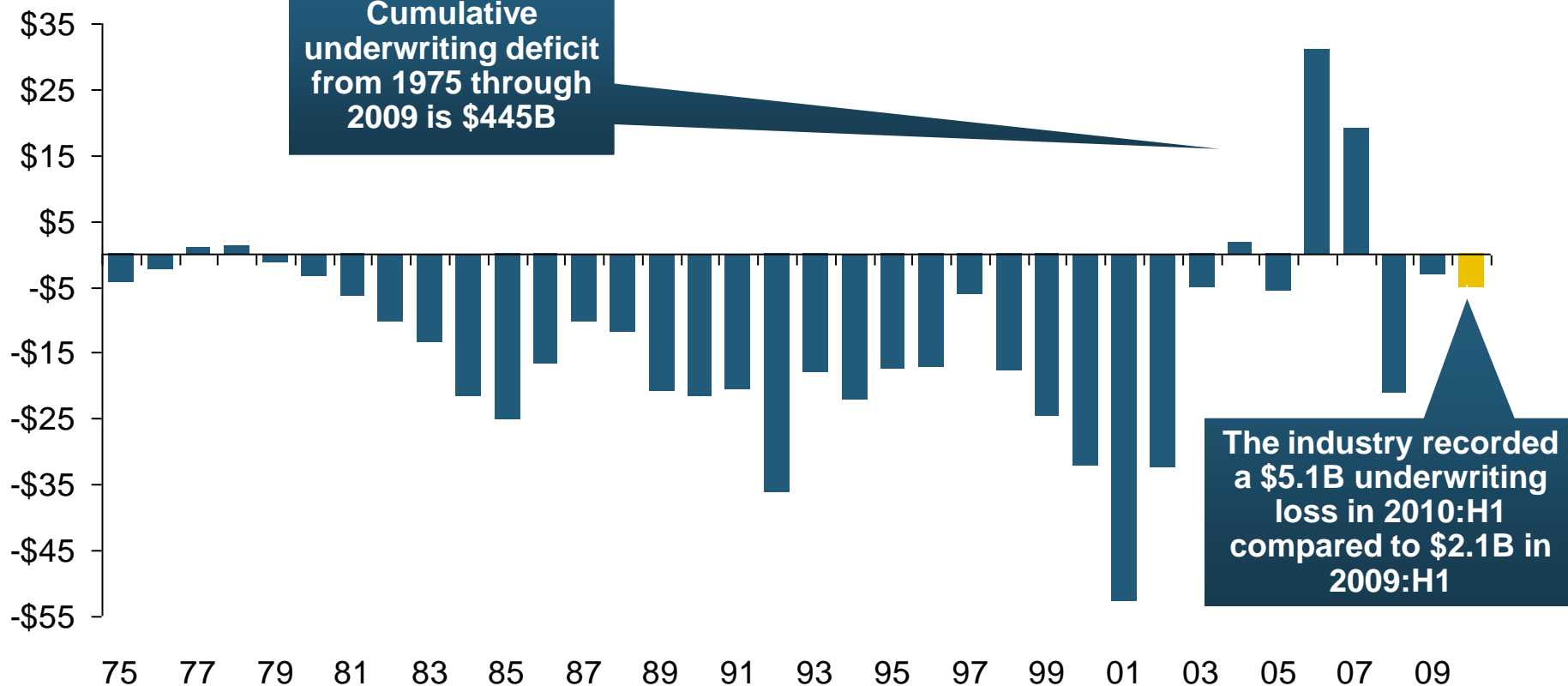


\* Excludes Mortgage & Financial Guaranty insurers in 2008, 2009 and 2010. Including M&FG, 2008=105.1, 2009=100.7, 2010:H1=101.7

Sources: A.M. Best, ISO.

# Underwriting Gain (Loss) 1975–2010:H1\*

(\$ Billions)

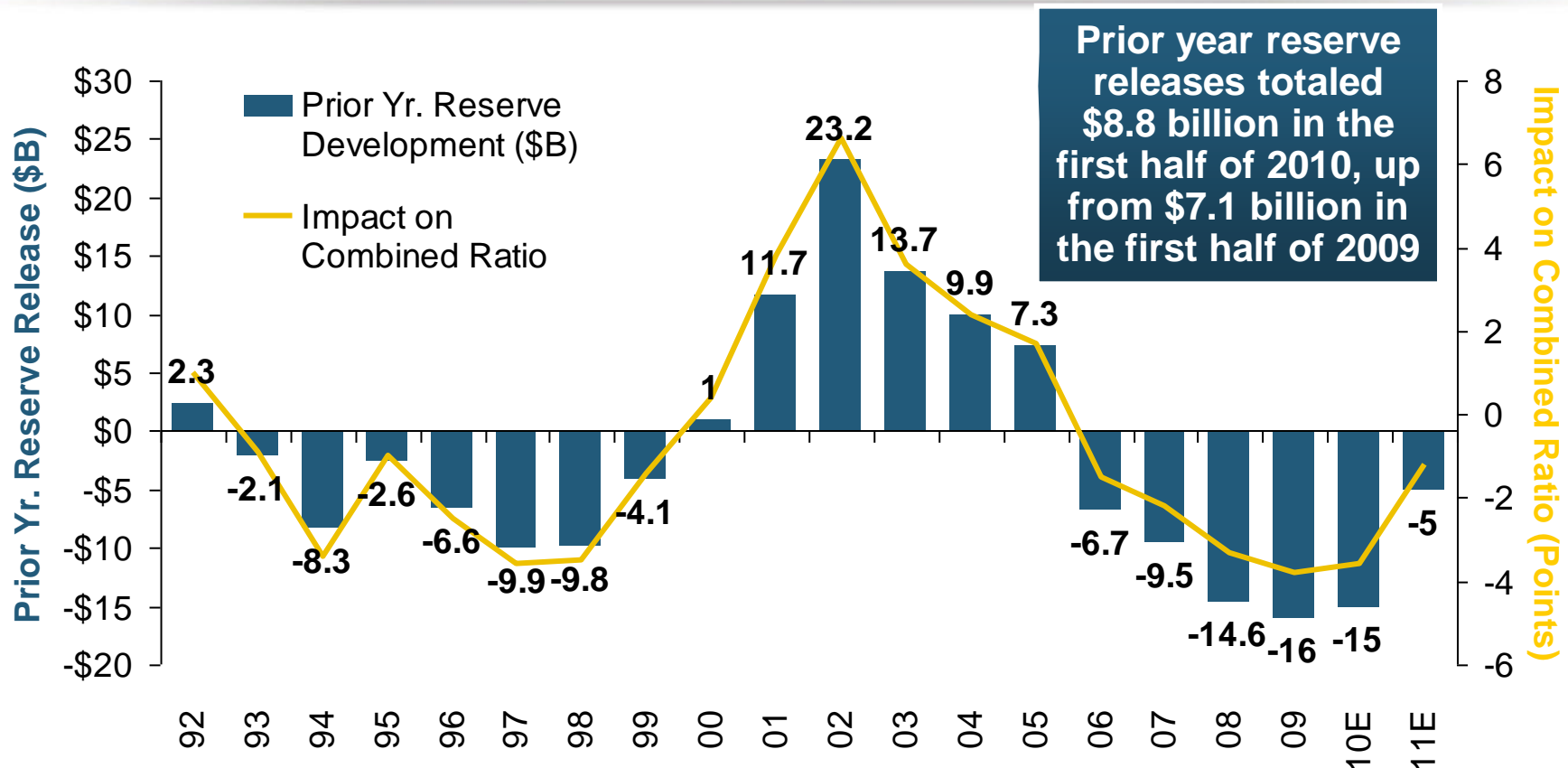


**Large Underwriting Losses Are *NOT* Sustainable  
in Current Investment Environment**

\* Includes mortgage and financial guarantee insurers.

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

# P/C Reserve Development, 1992–2011E



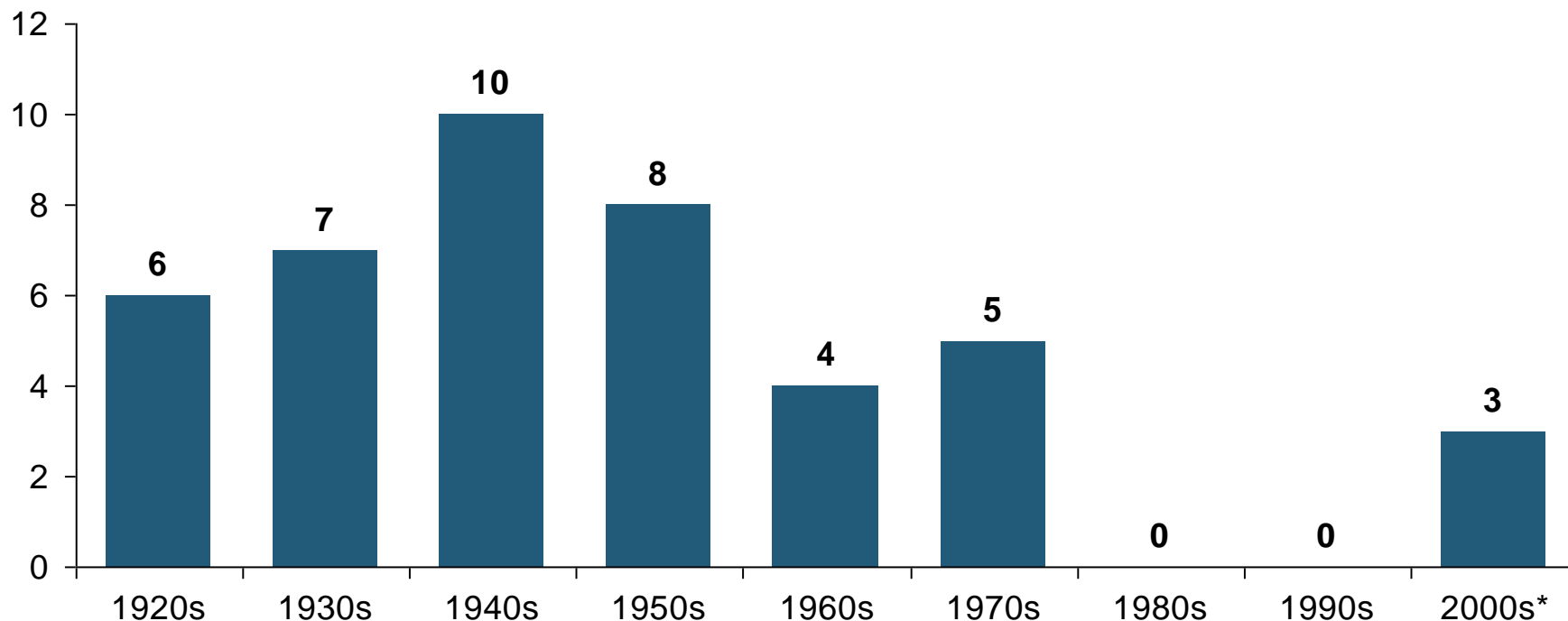
**Reserve Releases Are Continuing Strong in 2010 But Should Begin to Taper Off in 2011**

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.

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

Number of Years with Underwriting Profits



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

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

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

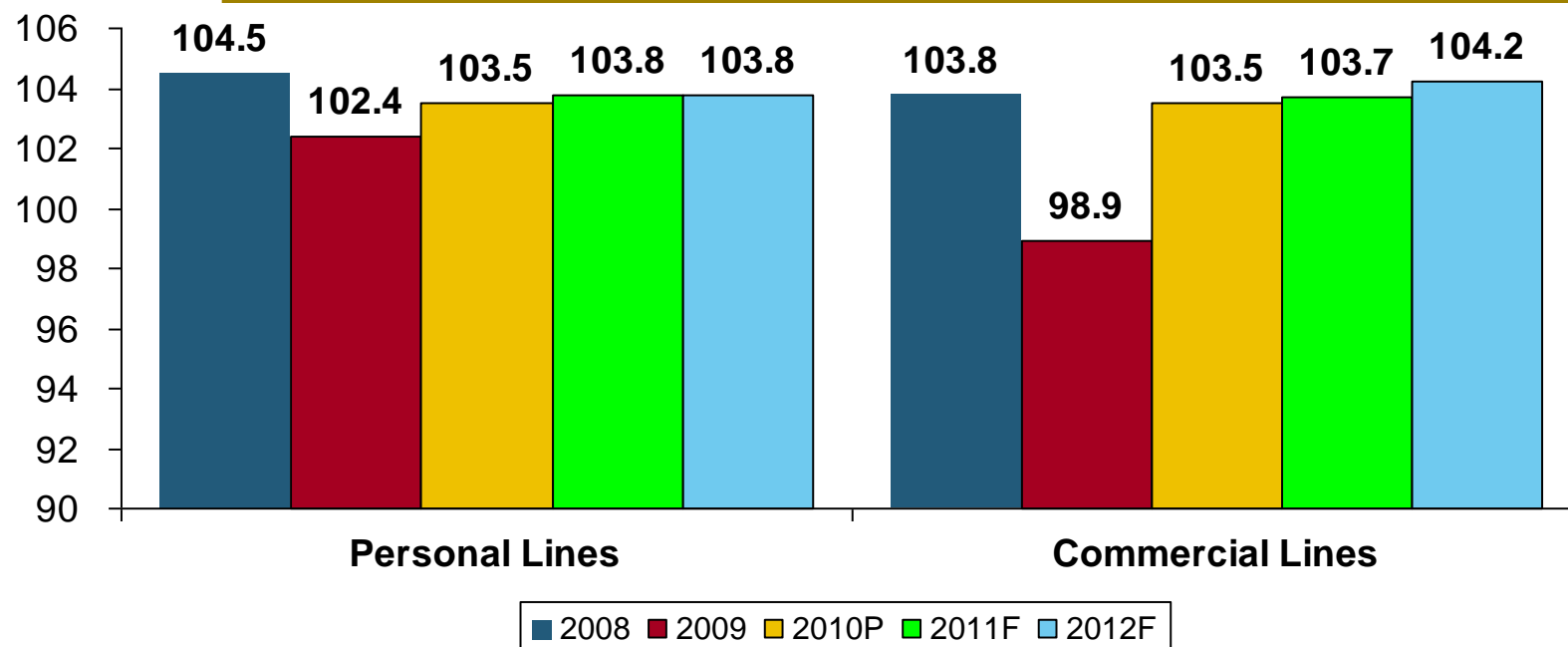
Sources: Insurance Information Institute research from A.M. Best Data.



# Performance by Segment: Commercial/Personal Lines

# Calendar Year Combined Ratios by Segment: 2008-2012F

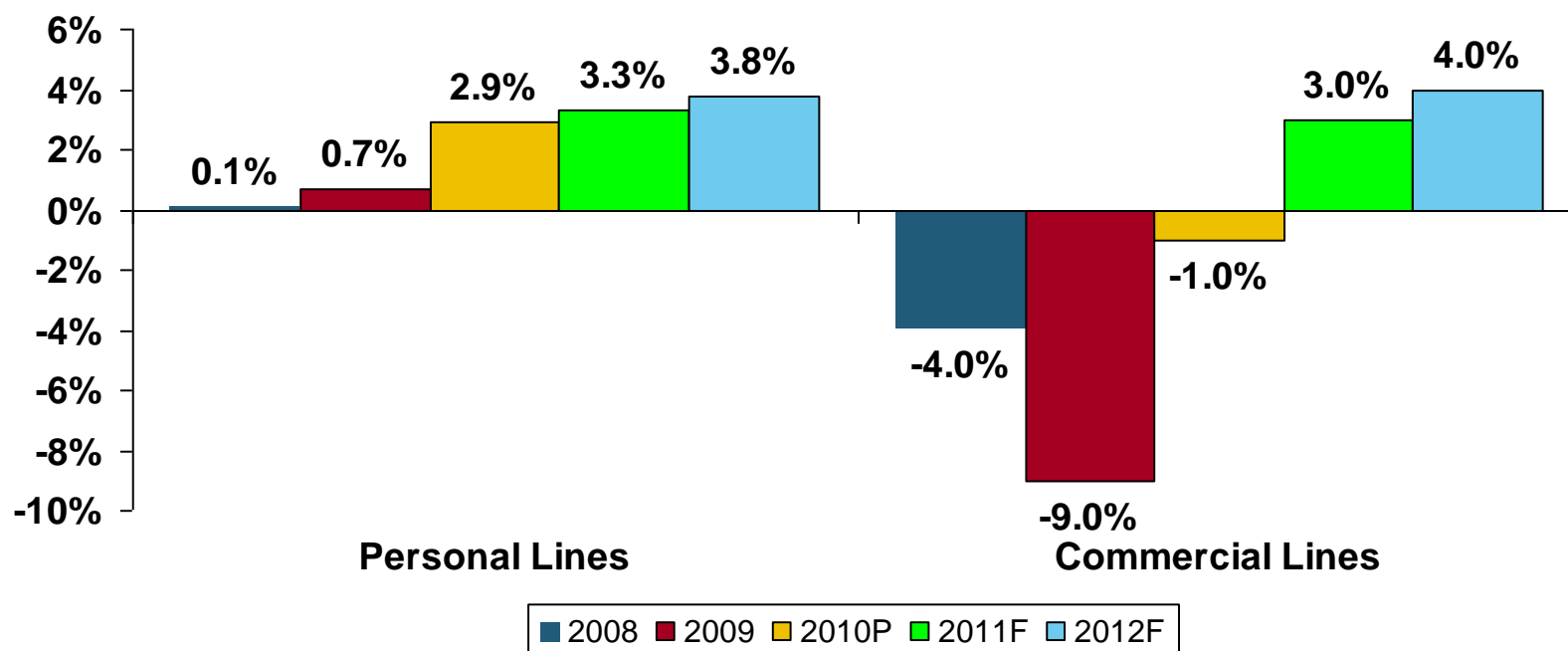
Personal lines combined ratio is expected to remain stable in 2010 while commercial lines and reinsurance deteriorate



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

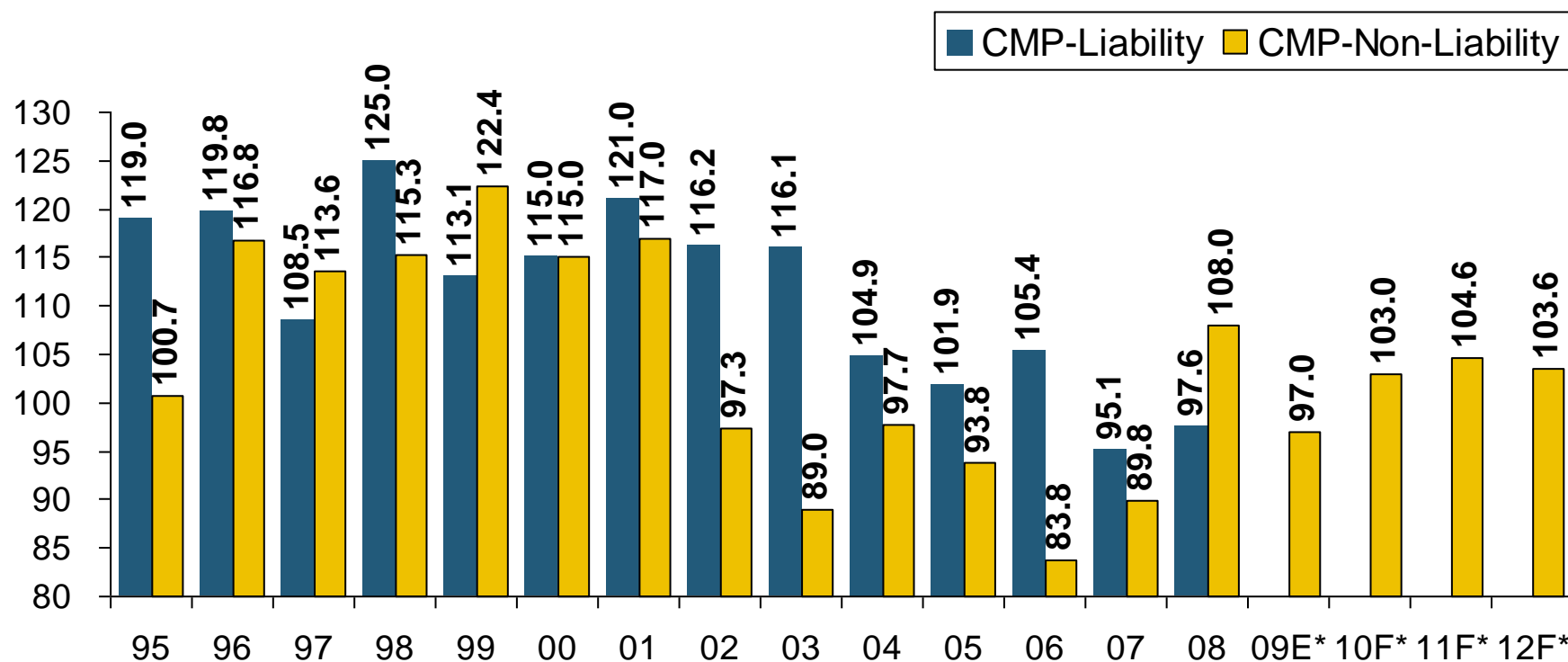
# Direct Written Premium Growth by Segment: 2008-2012F

**Personal lines will show growth in 2010 while commercial lines is expected to continue to shrink**



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

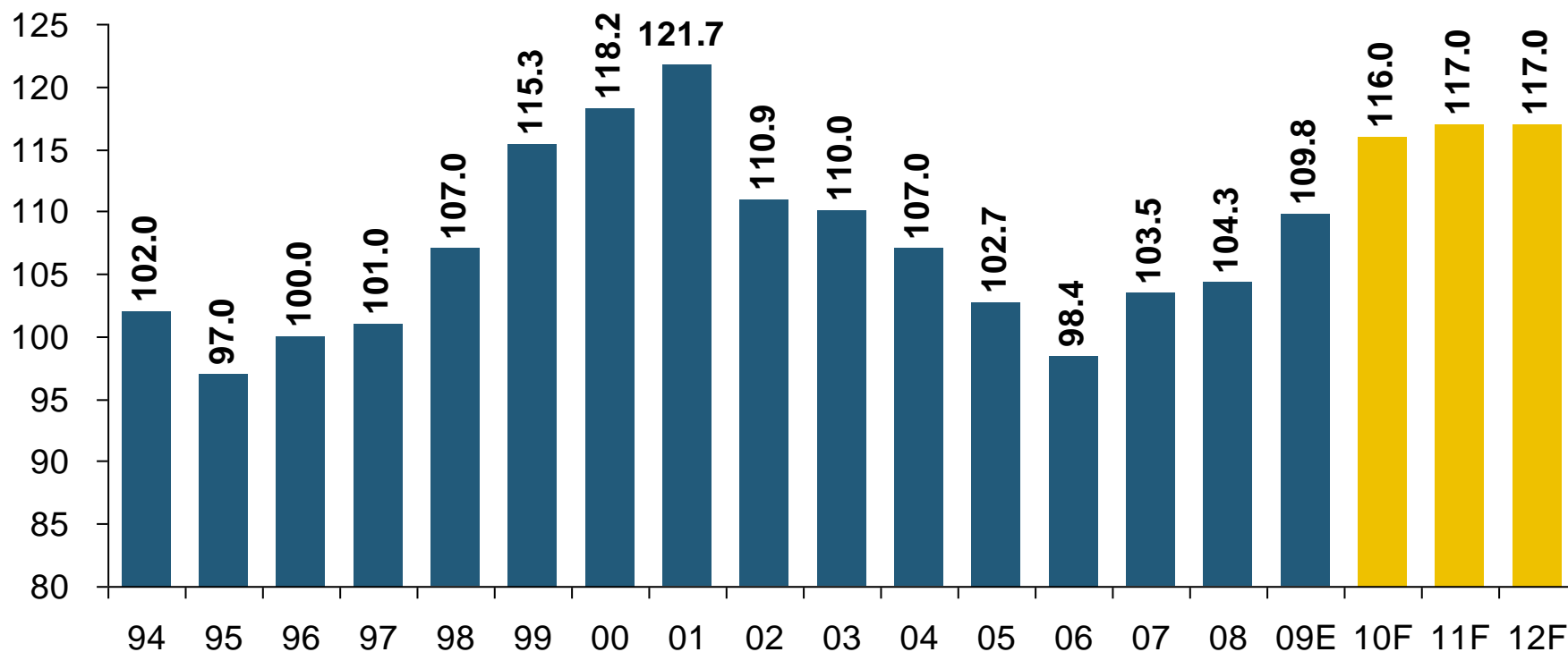
# Commercial Multi-Peril Combined Ratio: 1995–2012F\*



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

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

# Workers Compensation Combined Ratio: 1994–2012F



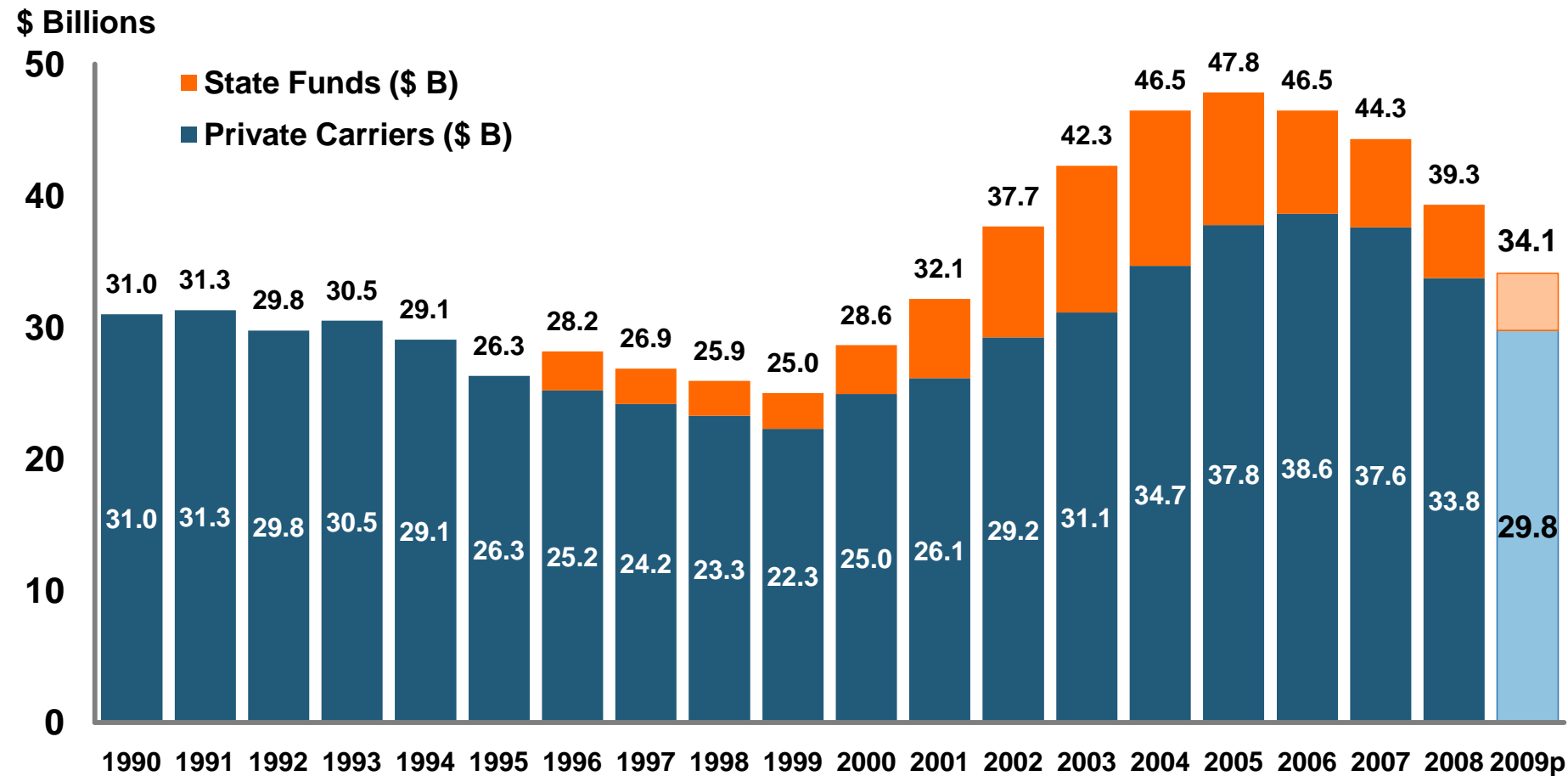
**Workers Comp Underwriting Results Are Deteriorating Markedly**

# **Workers Compensation Operating Environment**

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

# Workers Compensation Premium Continues Its Sharp Decline

## Net Written Premium



p Preliminary

Source: 1990–2008 Private Carriers, *Best's Aggregates & Averages*; 2009p, NCCI

1996–2009p State Funds: AZ, CA, CO, HI, ID, KY, LA, MD, MO, MT, NM, OK, OR, RI, TX, UT Annual Statements

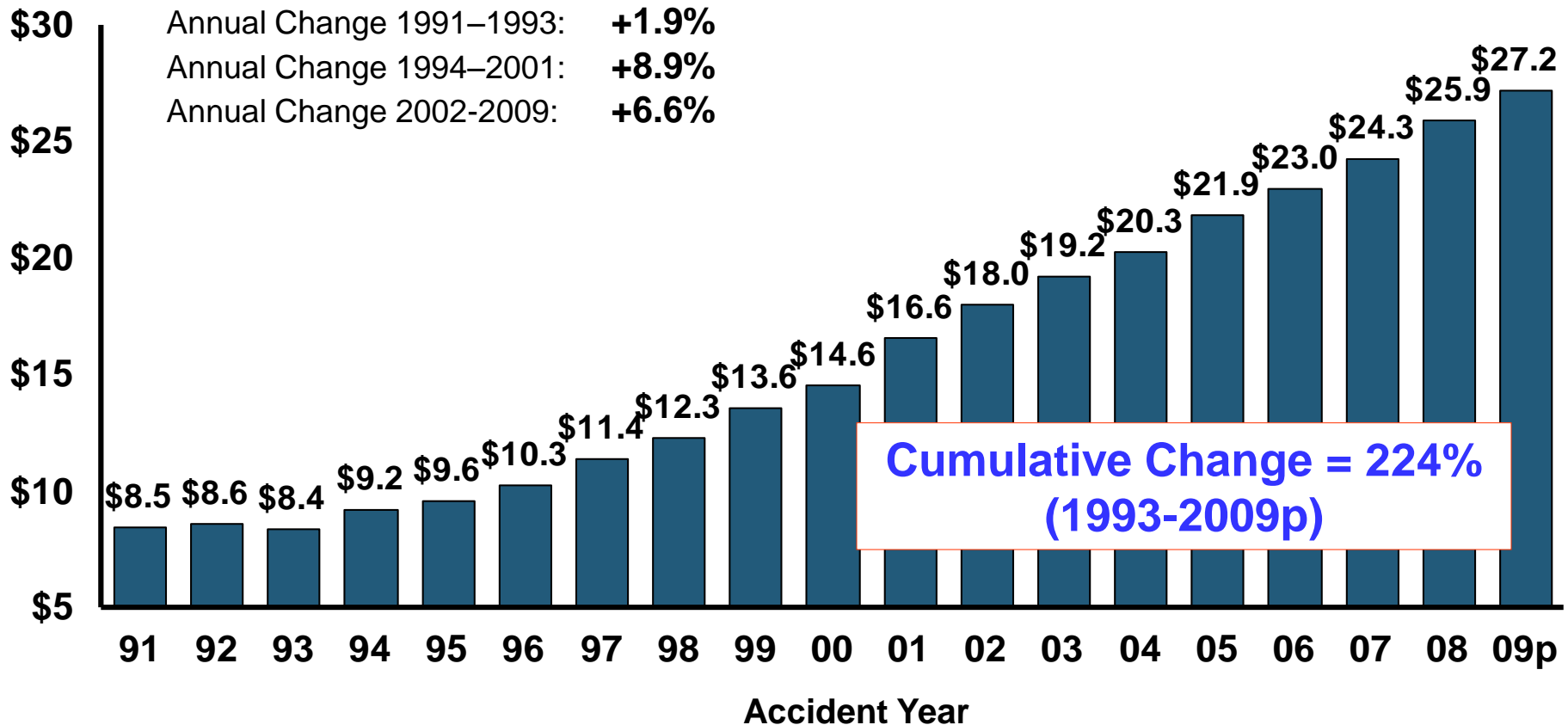
State Funds available for 1996 and subsequent

# **Workers Compensation 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)

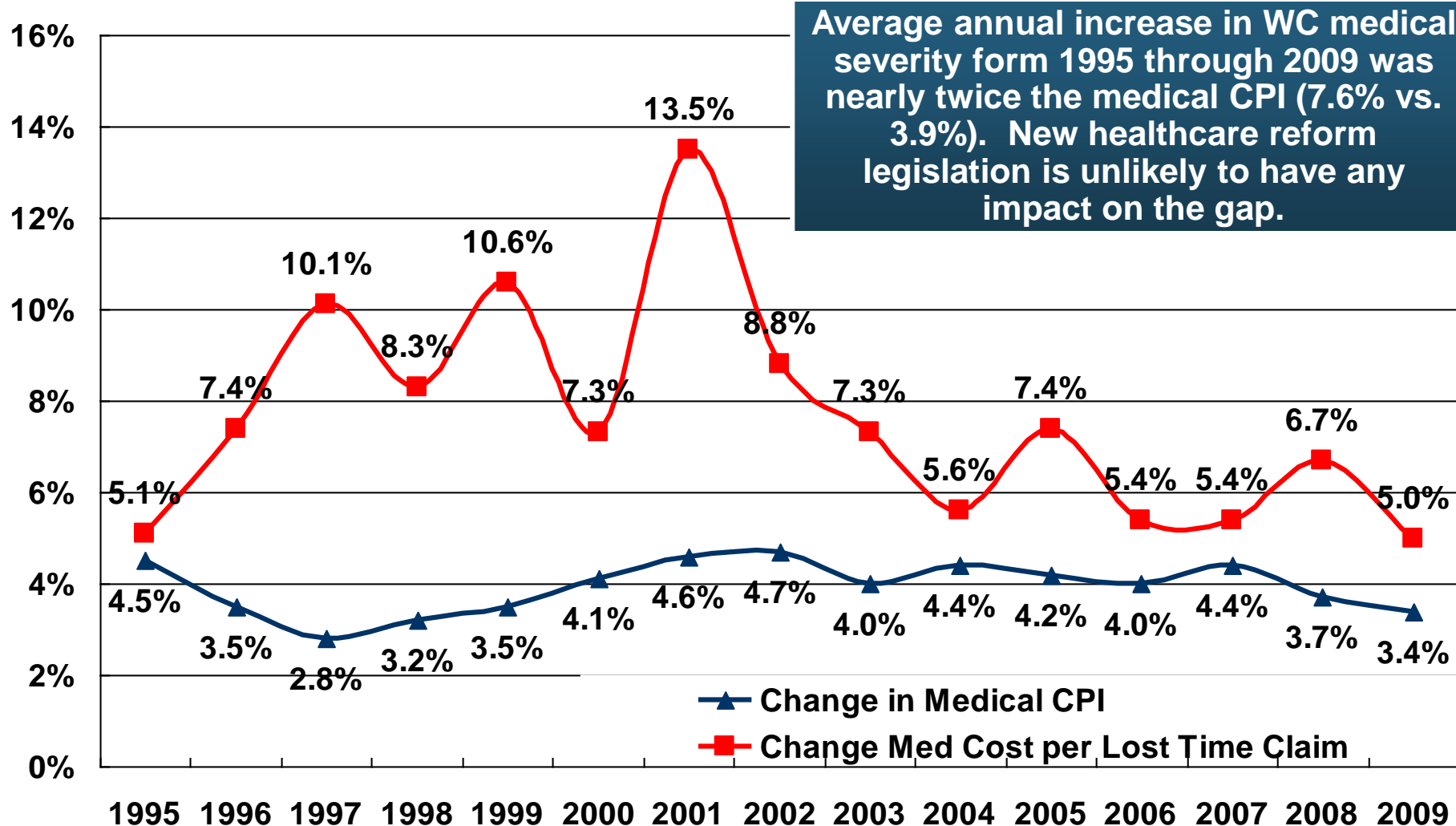


2009p: Preliminary based on data valued as of 12/31/2009

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

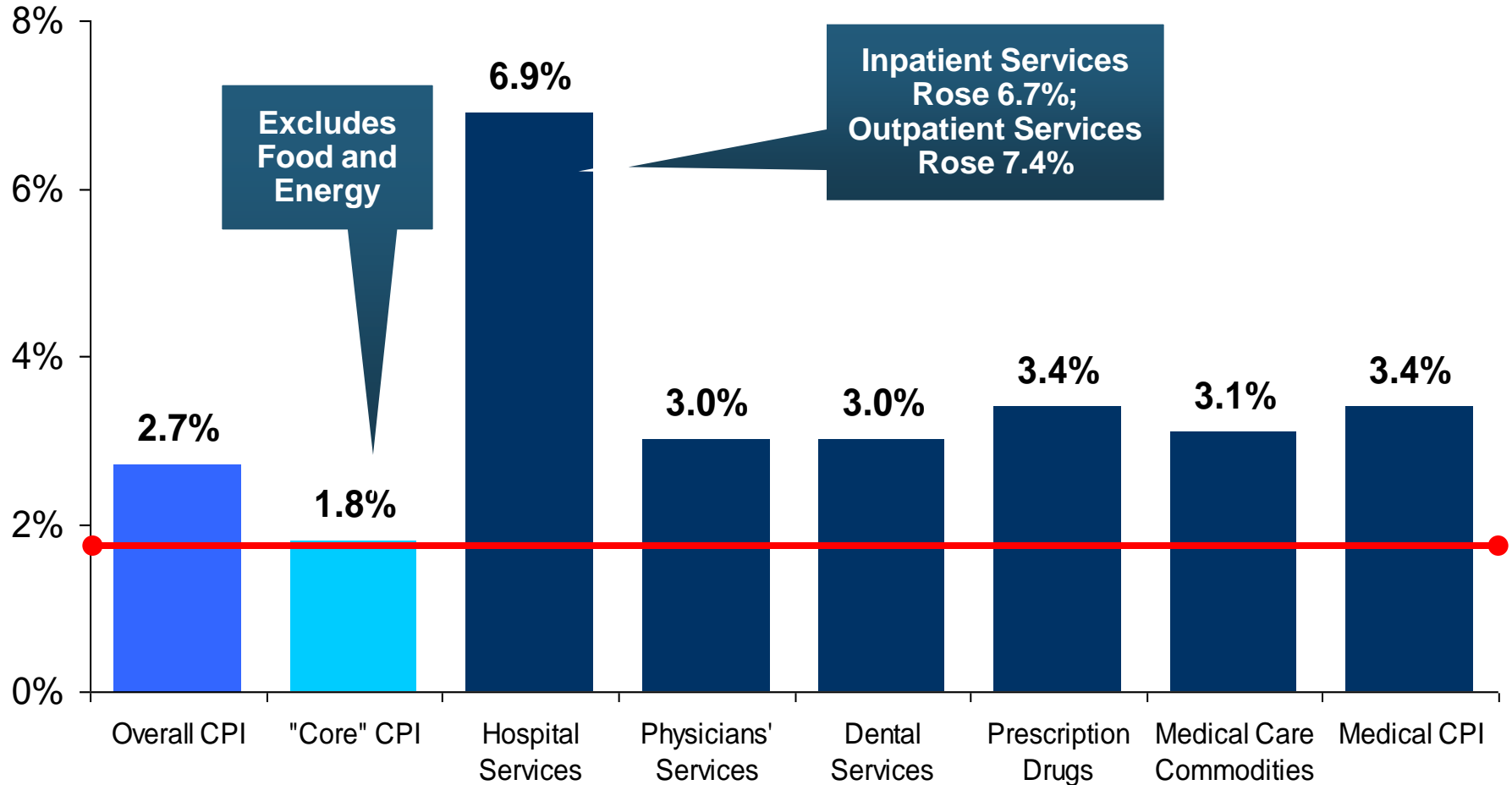
Based on the states where NCCI provides ratemaking services; Excludes the effects of deductible policies

# WC Medical Severity Rising at Twice the Medical CPI Rate



# 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**

# **Where Will the Growth in WC Exposure Come From?**

## **Industry and Occupation Growth Analysis**

# 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

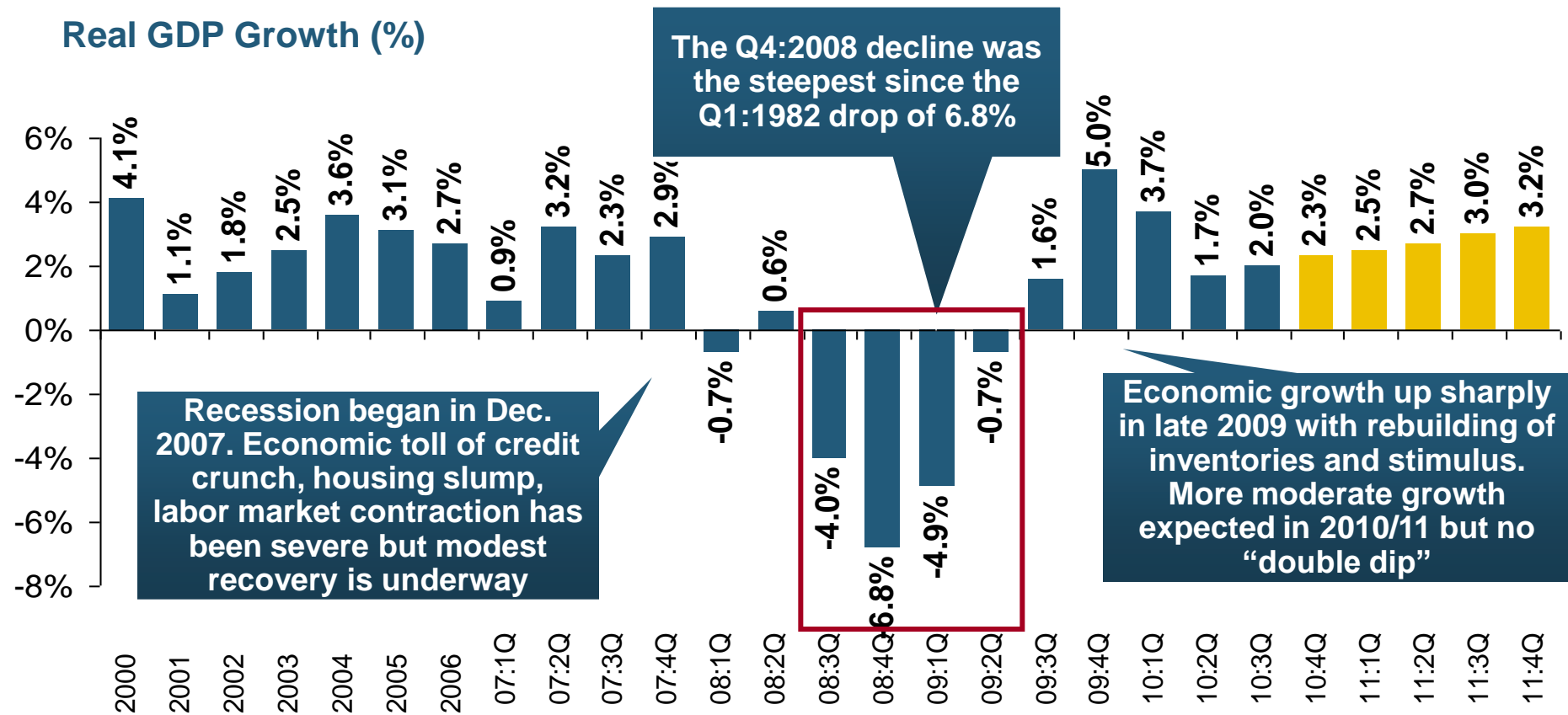
**SOURCE: BLS Occupational Employment Statistics and Division of Occupational Outlook**

# **The Economic Storm**

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

# US Real GDP Growth\*

Real GDP Growth (%)



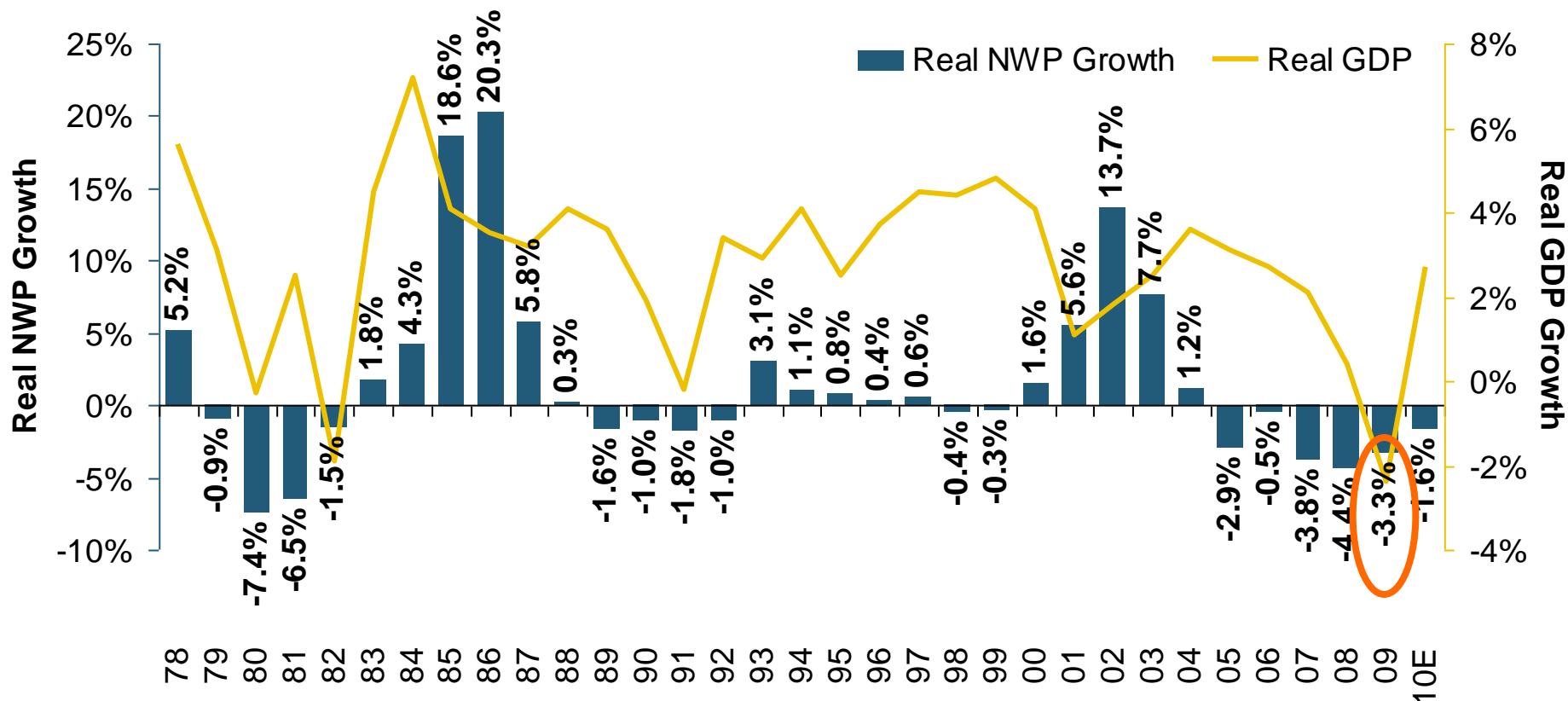
**Demand Commercial Insurance Continues To Be Impacted by Sluggish Economic Conditions, but the Benefits of Even Slow Growth Will Compound and Gradually Benefit the Economy Broadly**

\* Estimates/Forecasts from Blue Chip Economic Indicators.

Source: US Department of Commerce, Blue Economic Indicators 10/10; 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**

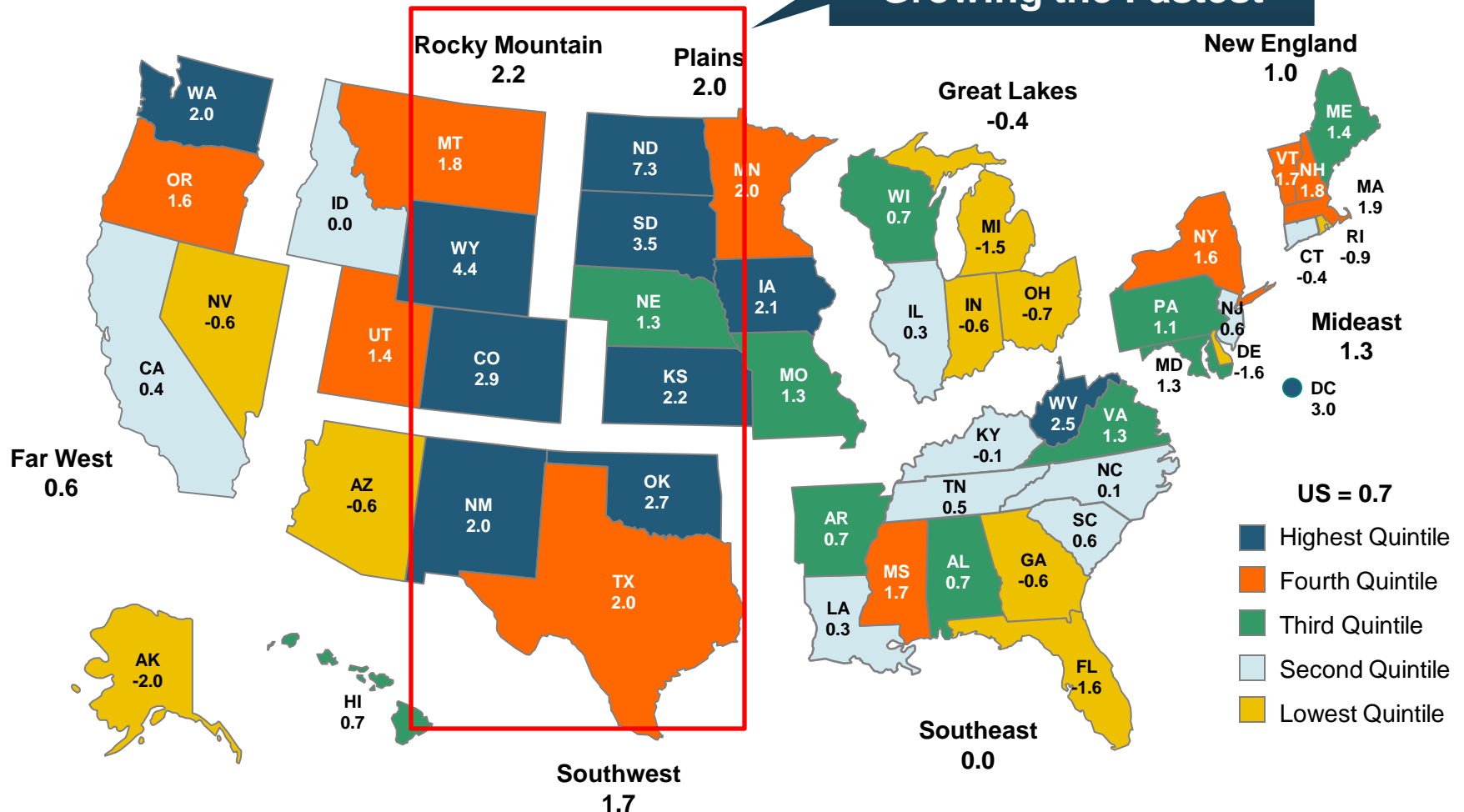
# **Regional Differences Will Significantly Impact P/C Markets**

**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

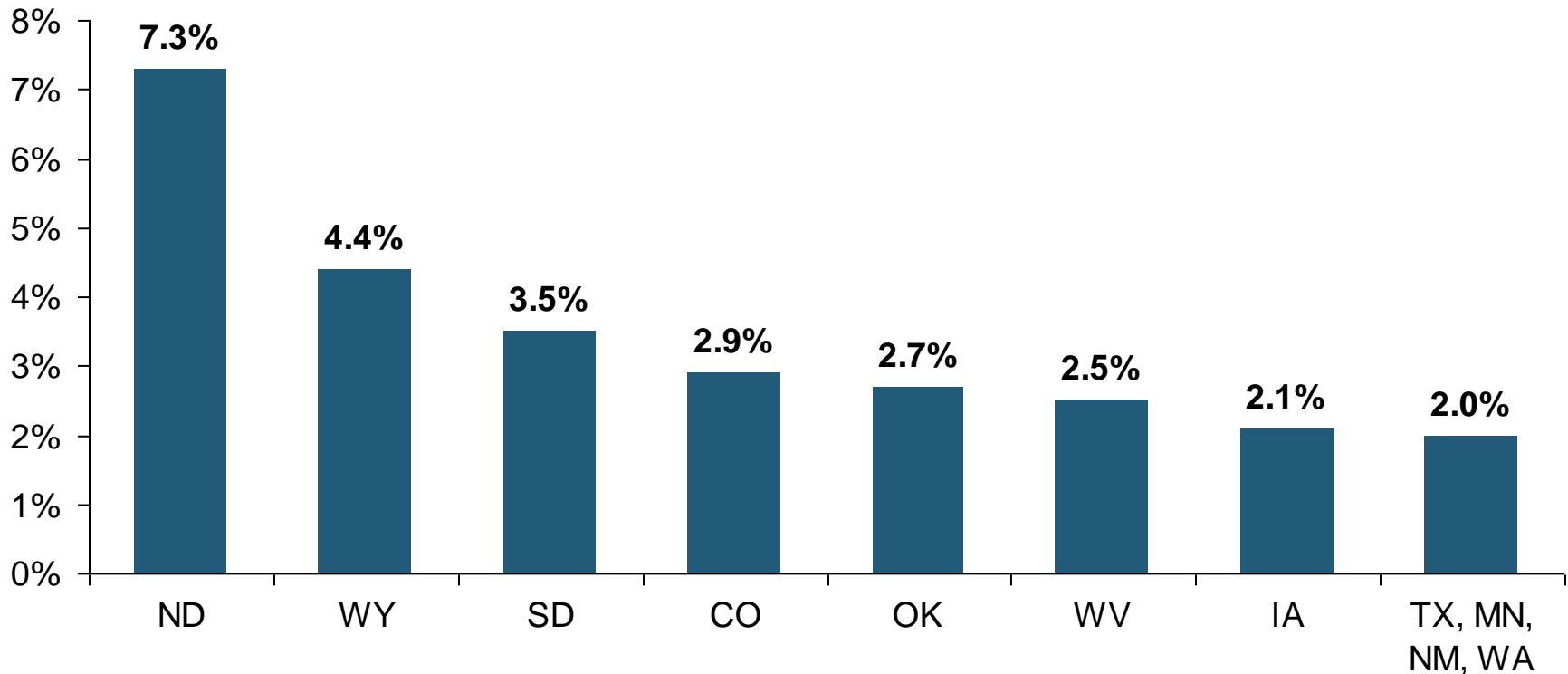
Percent Change in Real GDP by State, 2007–2008

Mountain, Plains States  
Growing the Fastest



# Fastest Growing States in 2008: Plains, Mountain States Lead

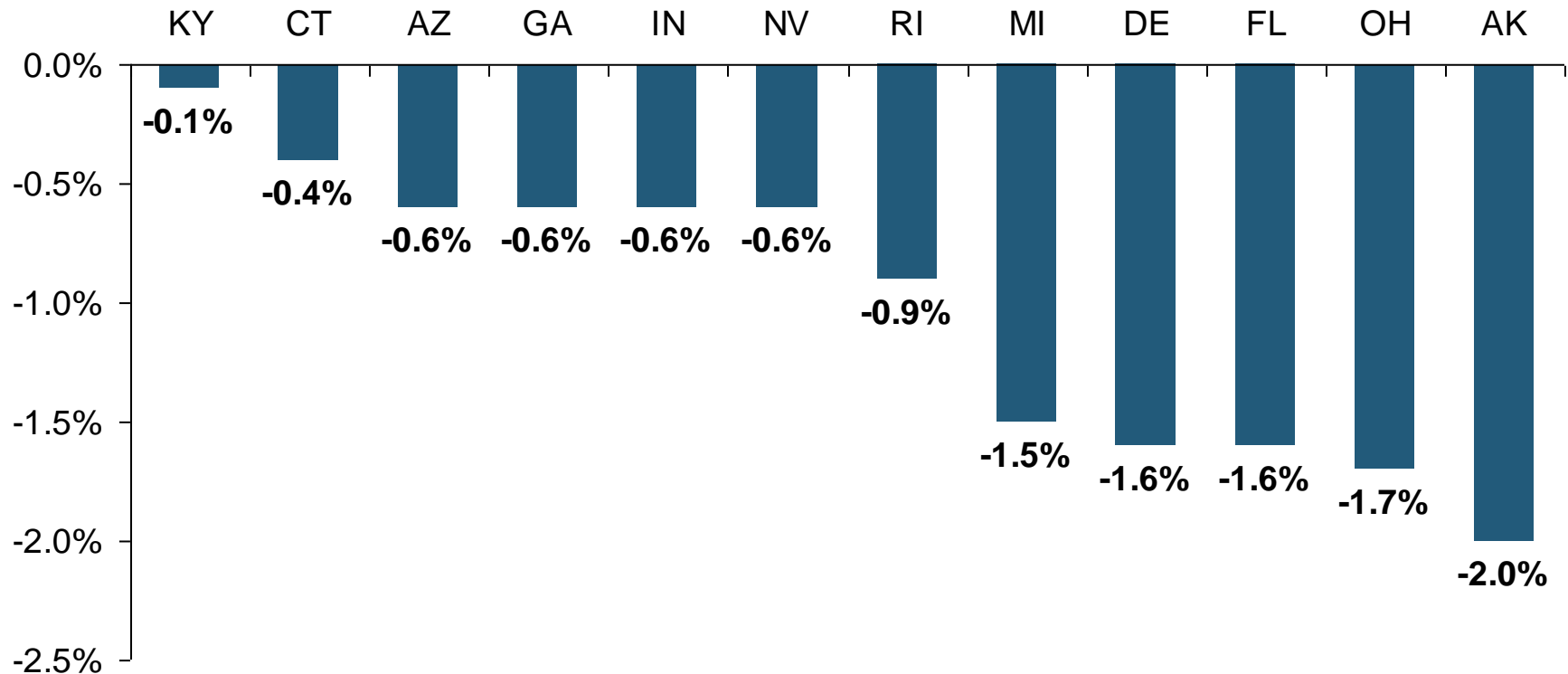
## Real State GDP Growth (%)



**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 (%)



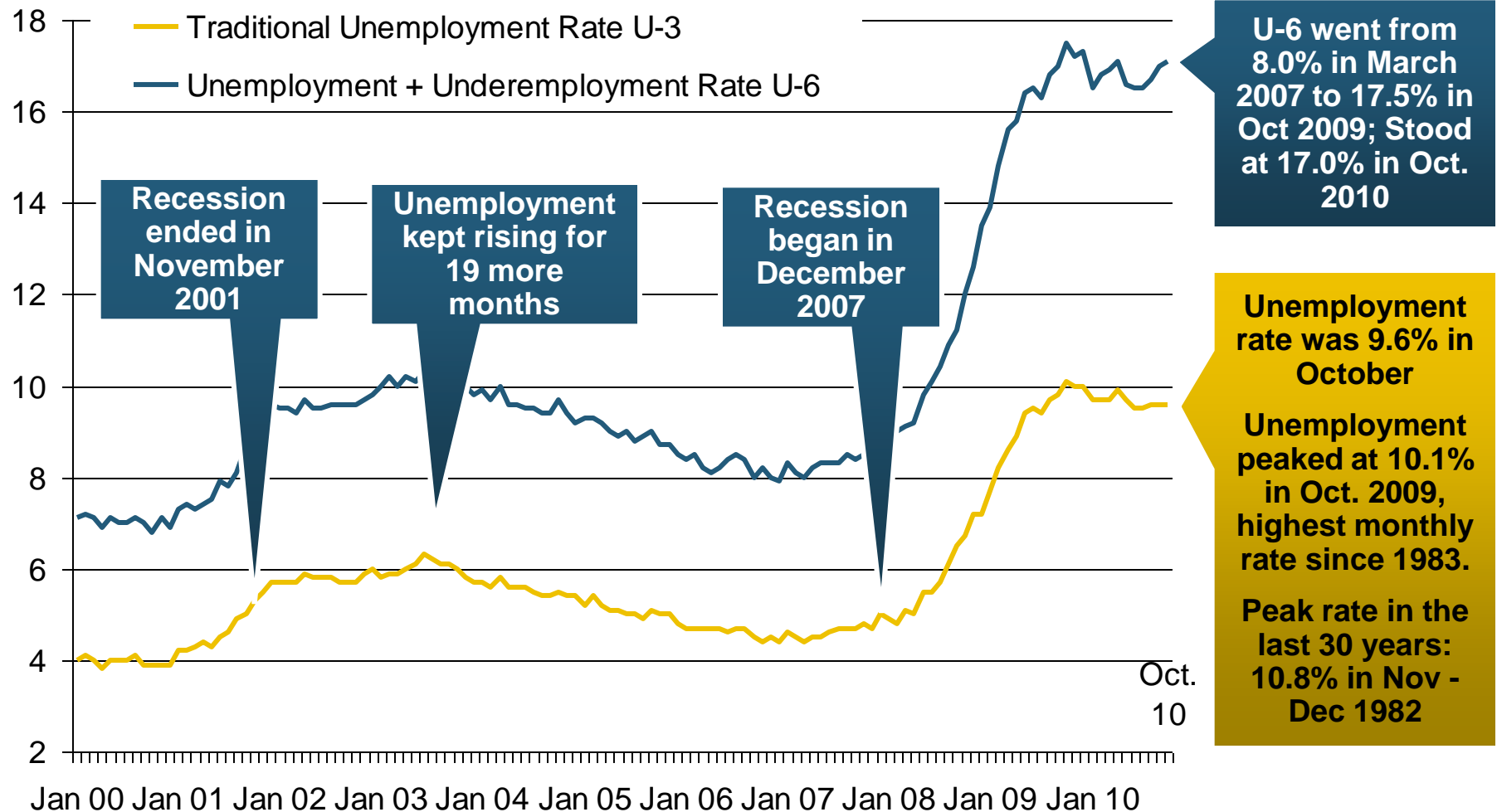
**States in the North, South, East, Midwest and West All Represented  
Among Hardest Hit, But for Differing Reasons**

# **Labor Market Trends**

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

# Unemployment and Underemployment Rates: Rocketed Up in 2008-09; Stabilized in 2010

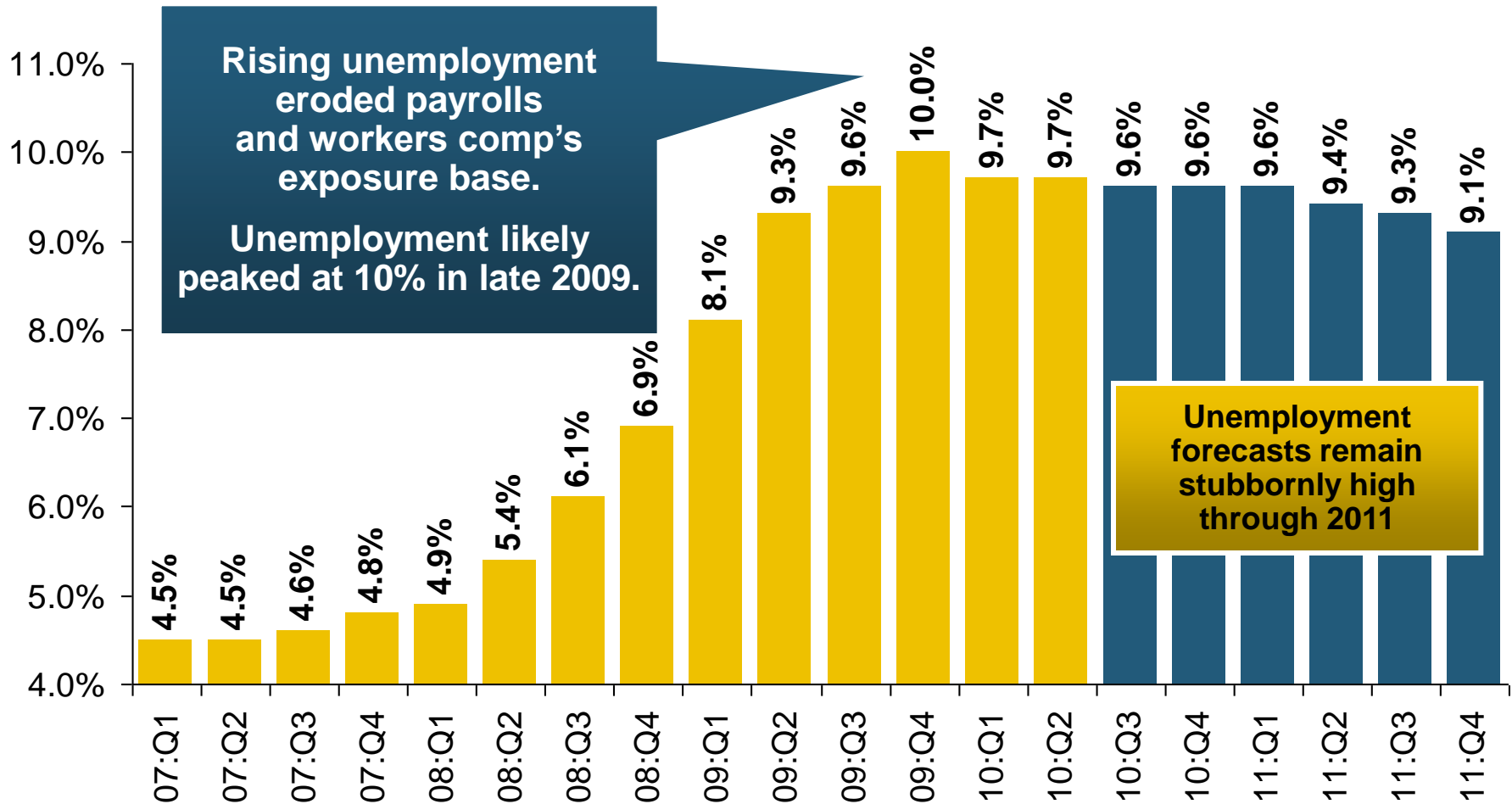
January 2000 through October 2010, Seasonally Adjusted (%)



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

# US Unemployment Rate

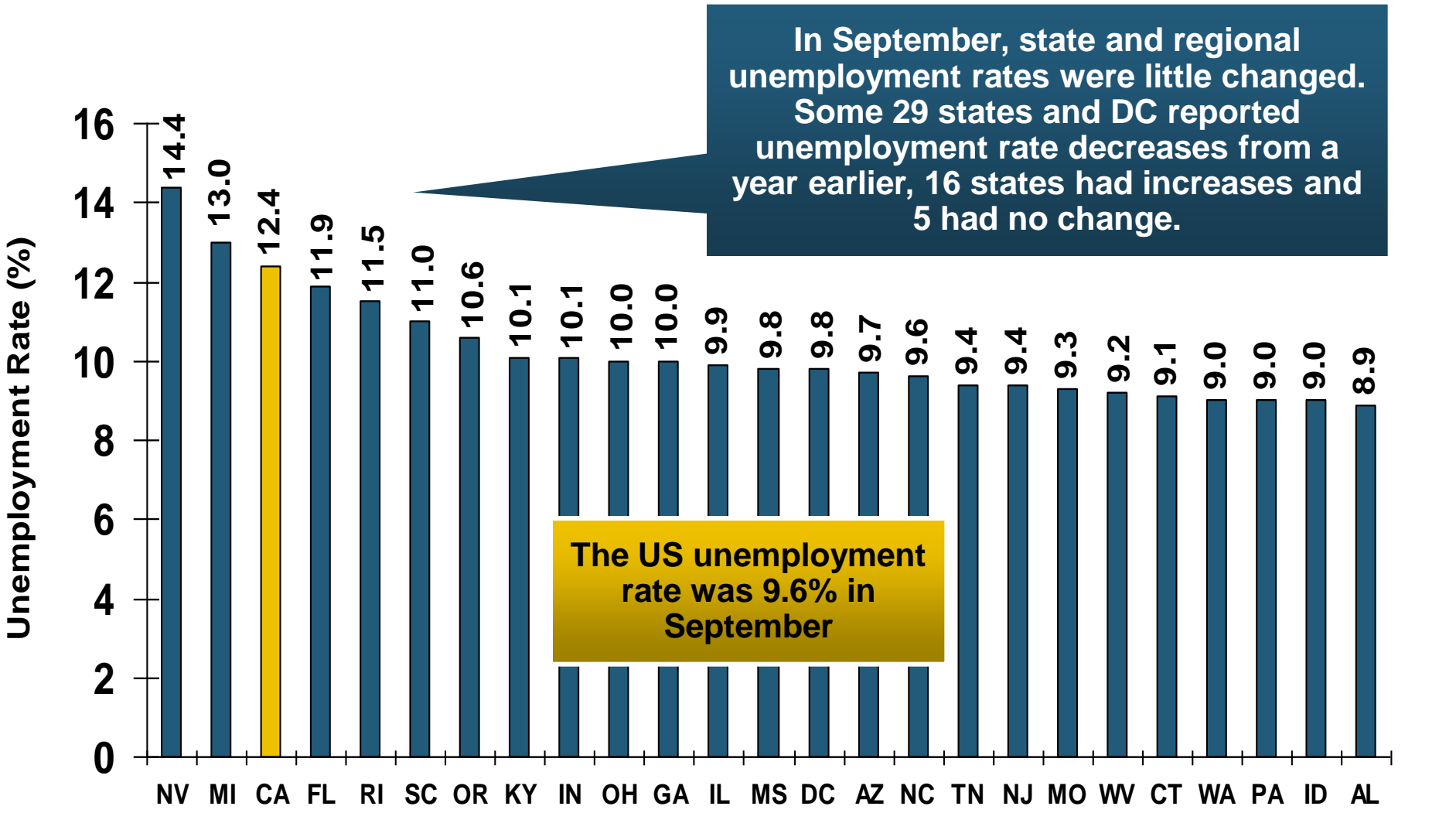
2007:Q1 to 2011:Q4F\*



\* ■ = actual; ■ = forecasts

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

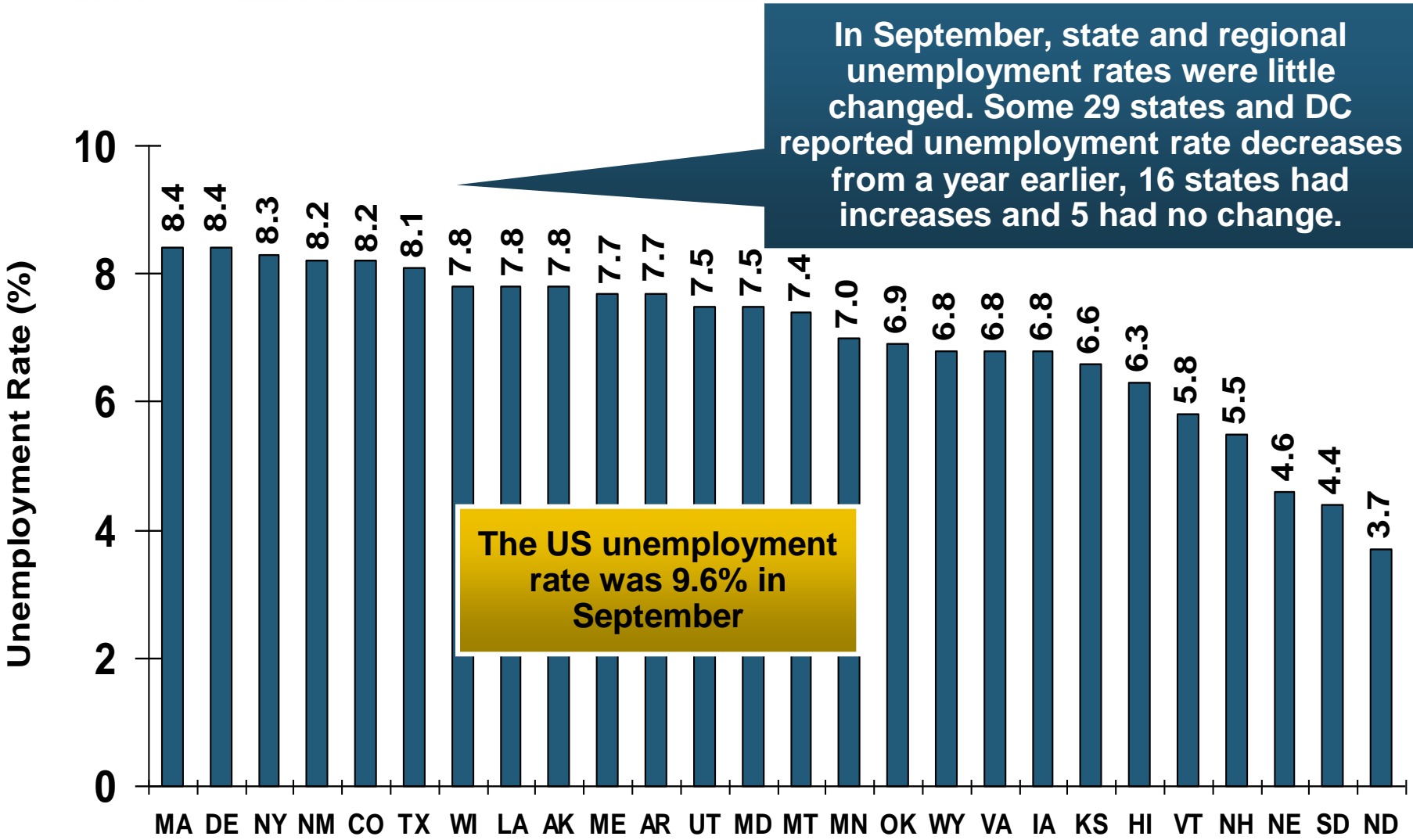
# Unemployment Rates by State, September 2010: Highest 25 States\*



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

# Unemployment Rates By State, September 2010: Insurance Information Institute

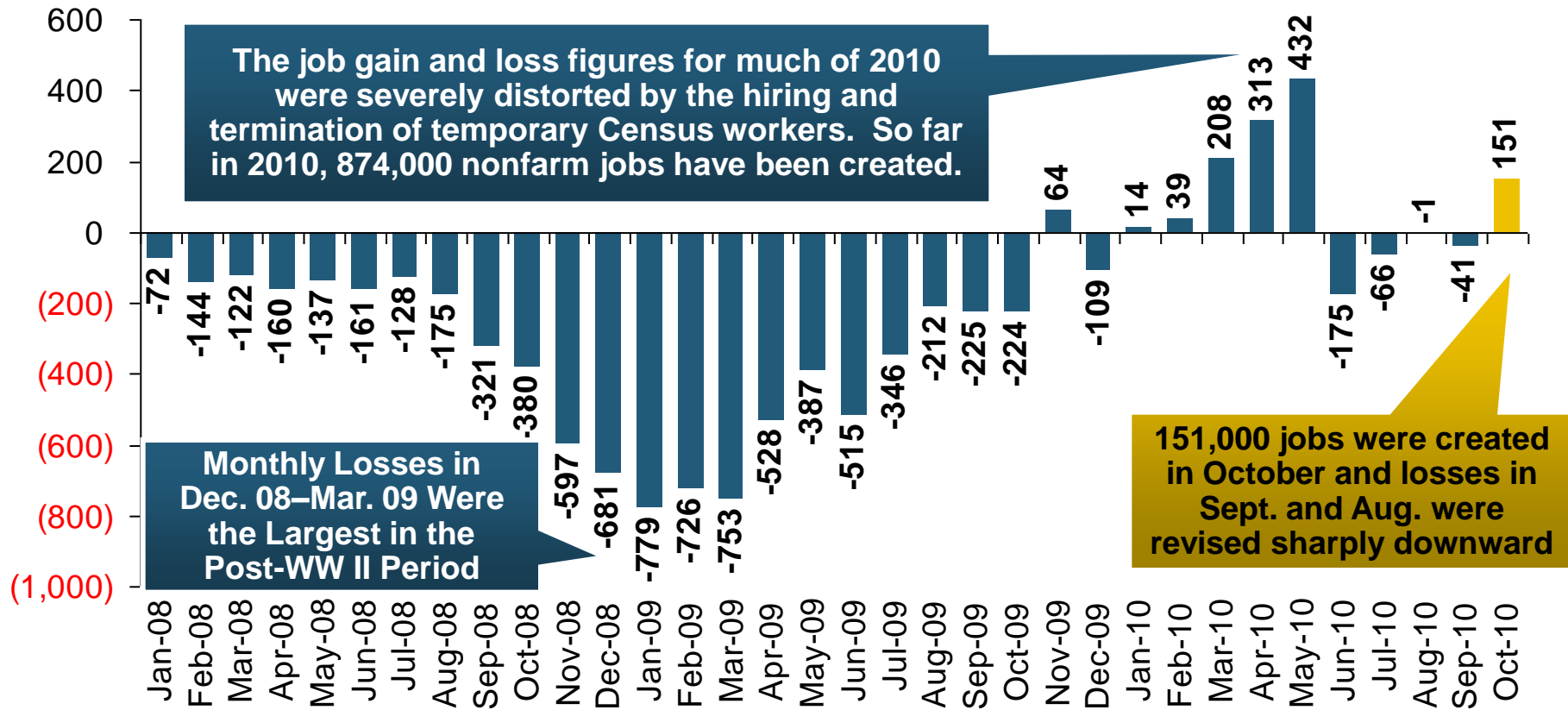
## Lowest 25 States\*



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

# Monthly Change Employment

January 2008 through October 2010\* (Thousands)



**Job Losses Since the Recession Began in Dec. 2007 Peaked at 8.4 Mill in Dec. 09; Stands at 7.5 Million Through October 2010; 14.8 Million People are Now Defined as Unemployed**

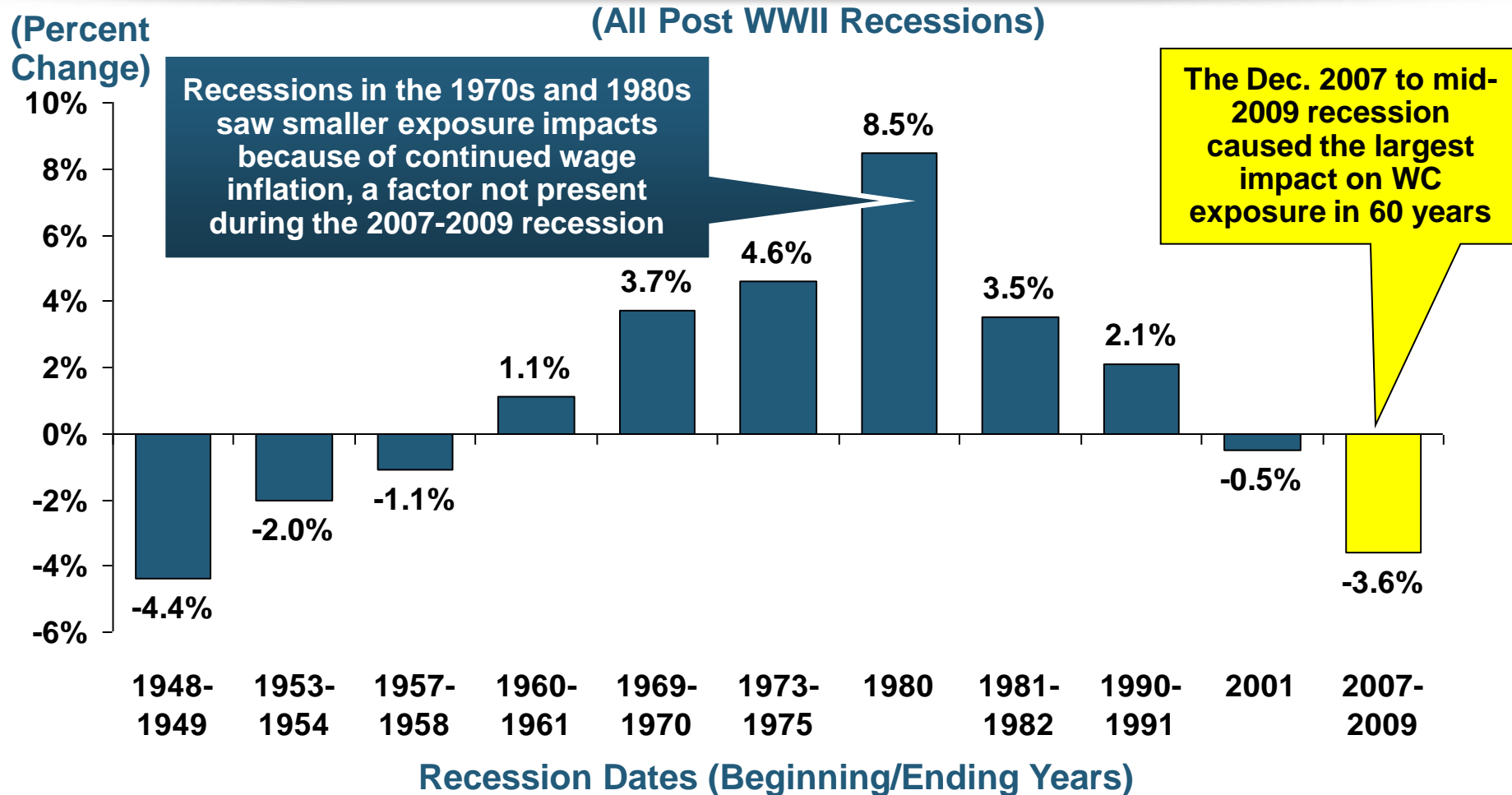
# Change in Employment Level for Select Industries, Oct. 2010 vs. Sept. 2010

Change in Thousands



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

# 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

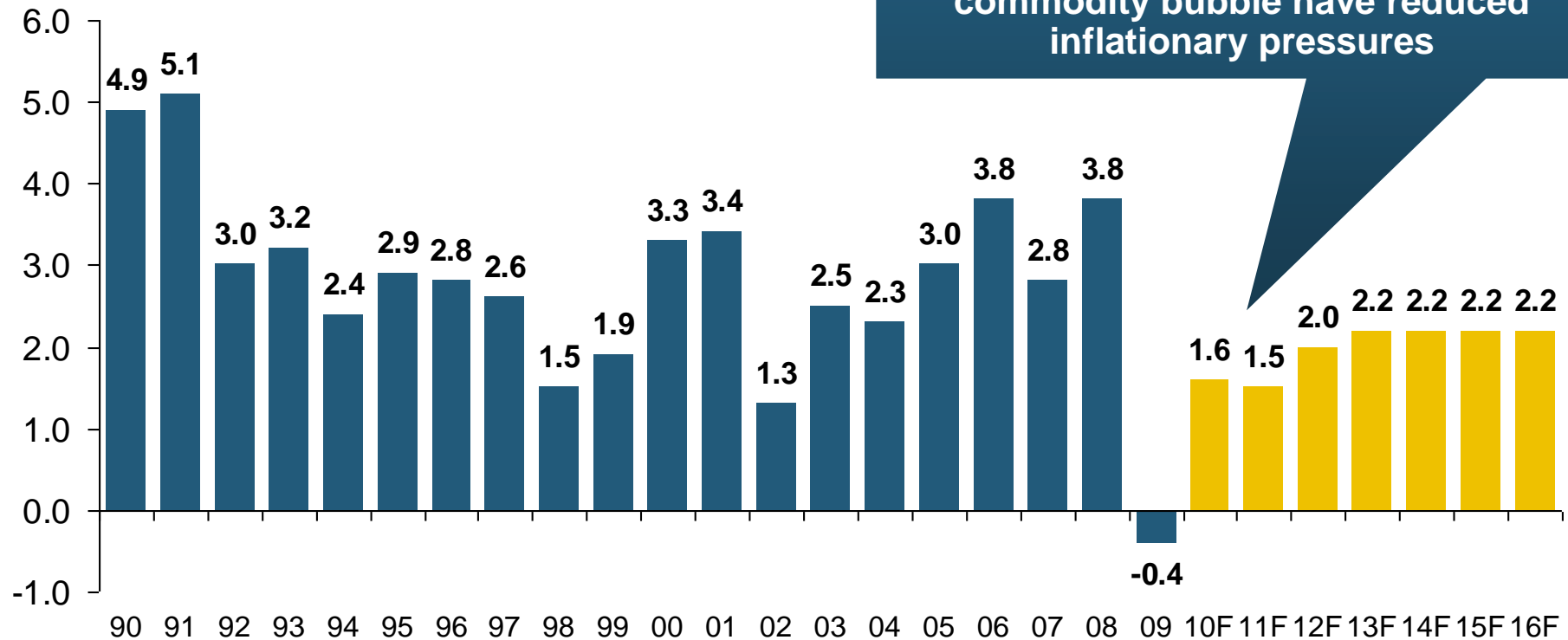
Source: Insurance Information Institute research; Federal Reserve Bank of St. Louis (wage and salary data); National Bureau of Economic Research (recession dates).

# **Inflation Trends: Benign Inflation Tempers Claim Severity**

**Fed Efforts to Stimulate Inflation Will  
Ultimately Pressure Claim  
Cost Severities**

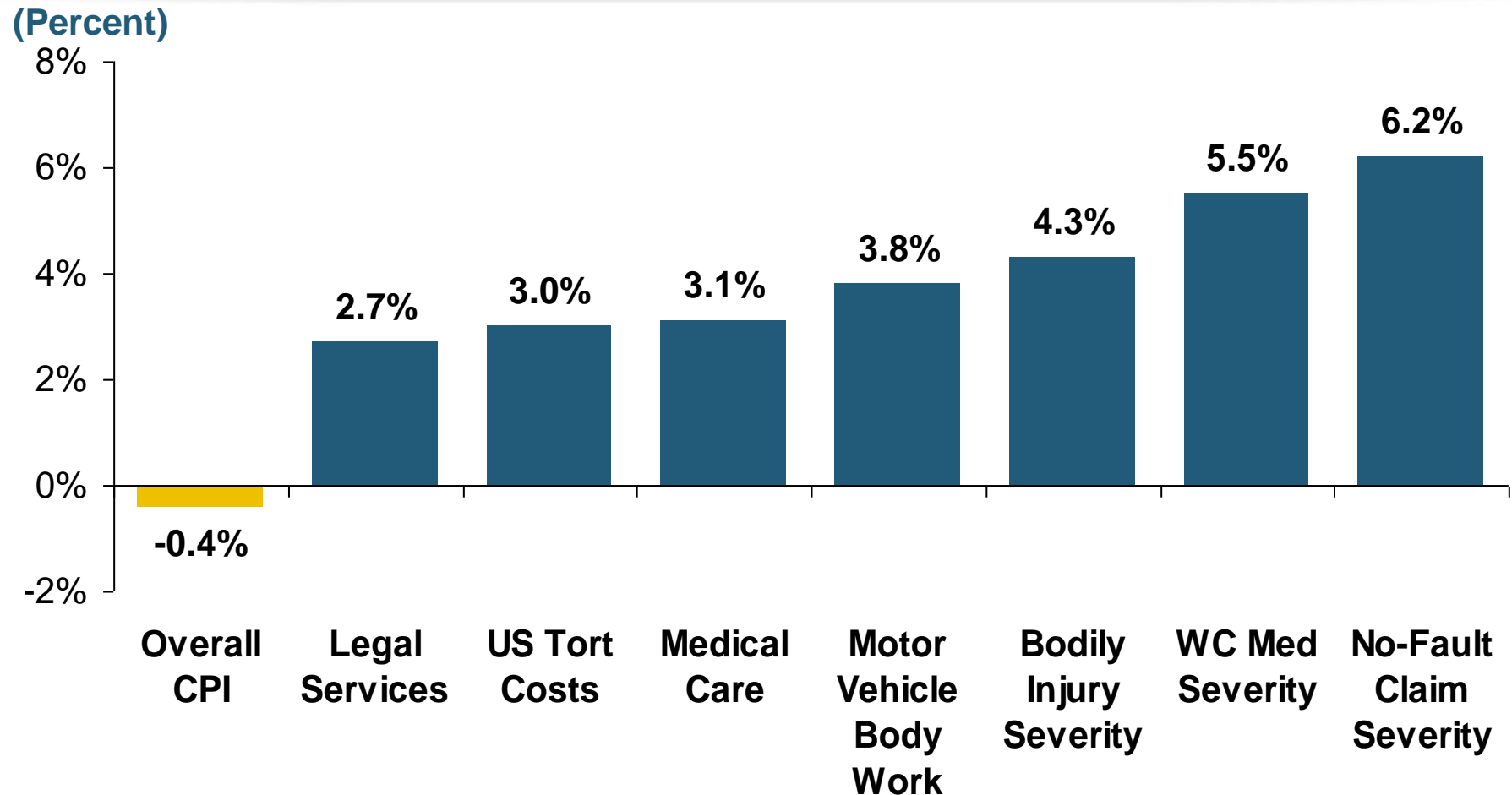
# Annual Inflation Rates (CPI-U, %), 1990–2016F

Annual Inflation Rates (%)



**There is So Much Slack in the US Economy Inflation Should Not Be a Concern Through 2010-12 Despite Fed's Quantitative Easing Efforts. Deficits and Monetary Policy Remain Longer Run Concerns**

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

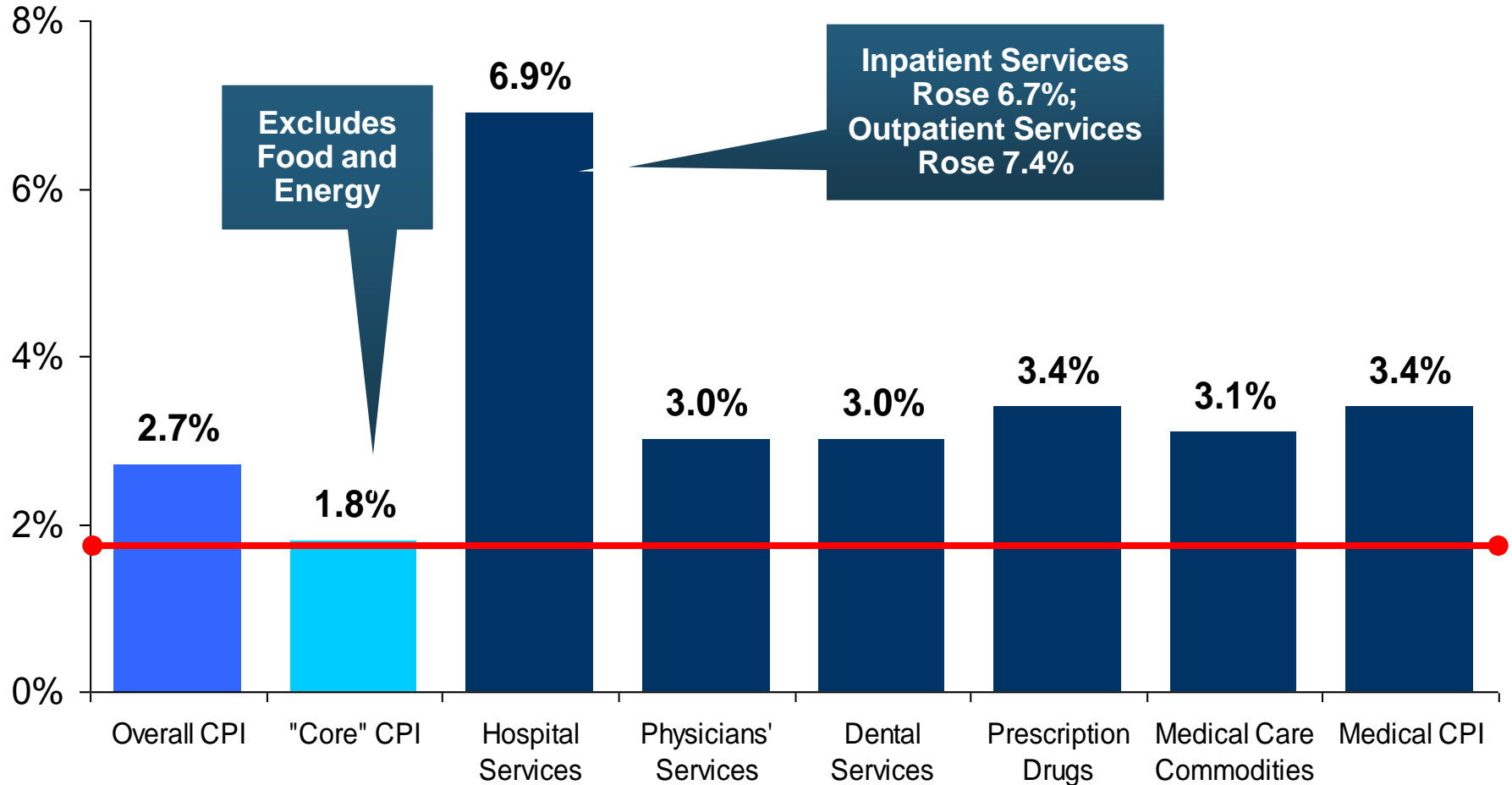


**Healthcare and Legal/Tort Costs Are a Major P/C Insurance Cost Driver. These Are Expected to Increase Above the Overall Inflation Rate (CPI) Indefinitely**

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)

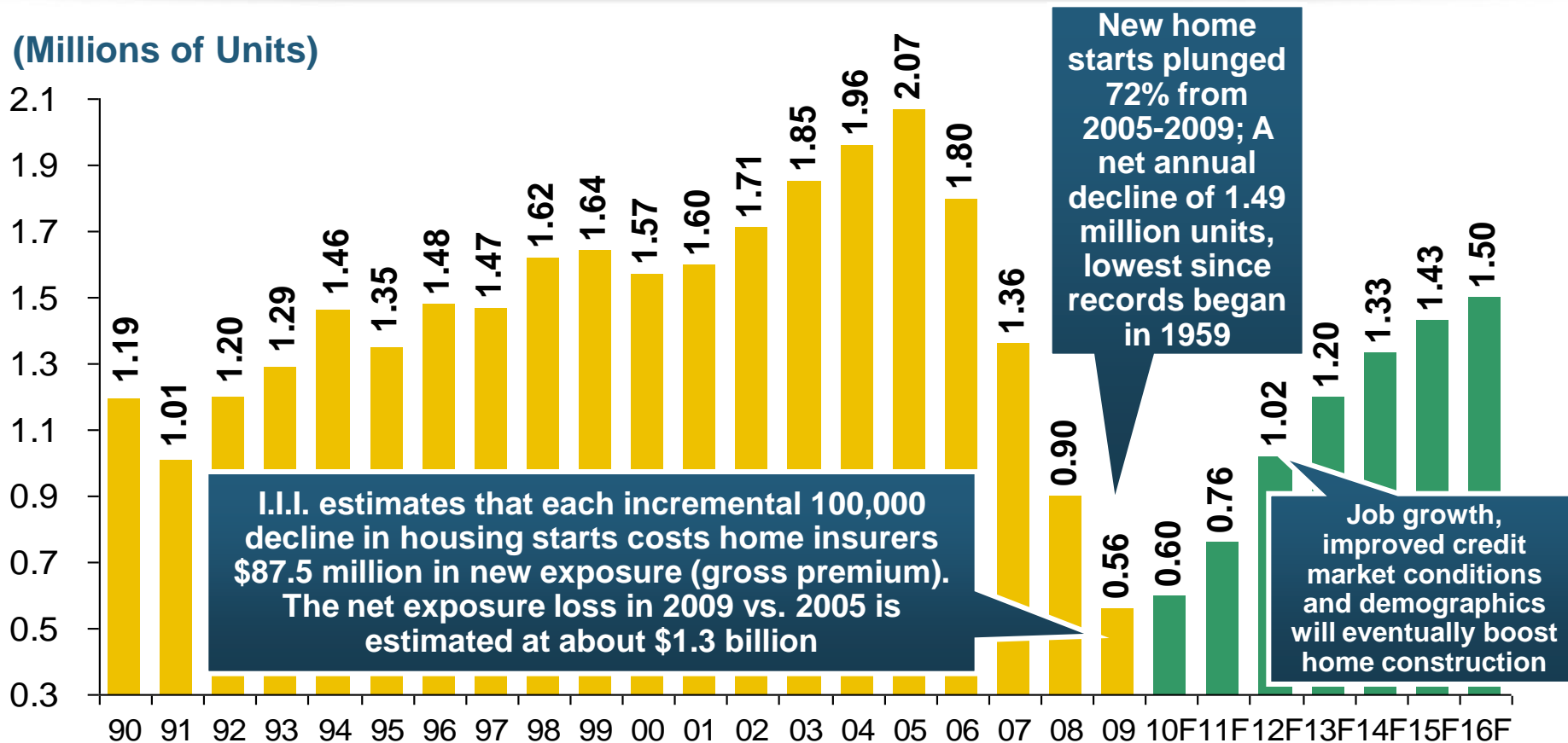


**Healthcare Costs Are a Major WC Insurance Cost Driver. They Are Likely to Increase Faster than the CPI for the Next Few Years, at Least**

# **Crisis-Driven Exposure Drivers**

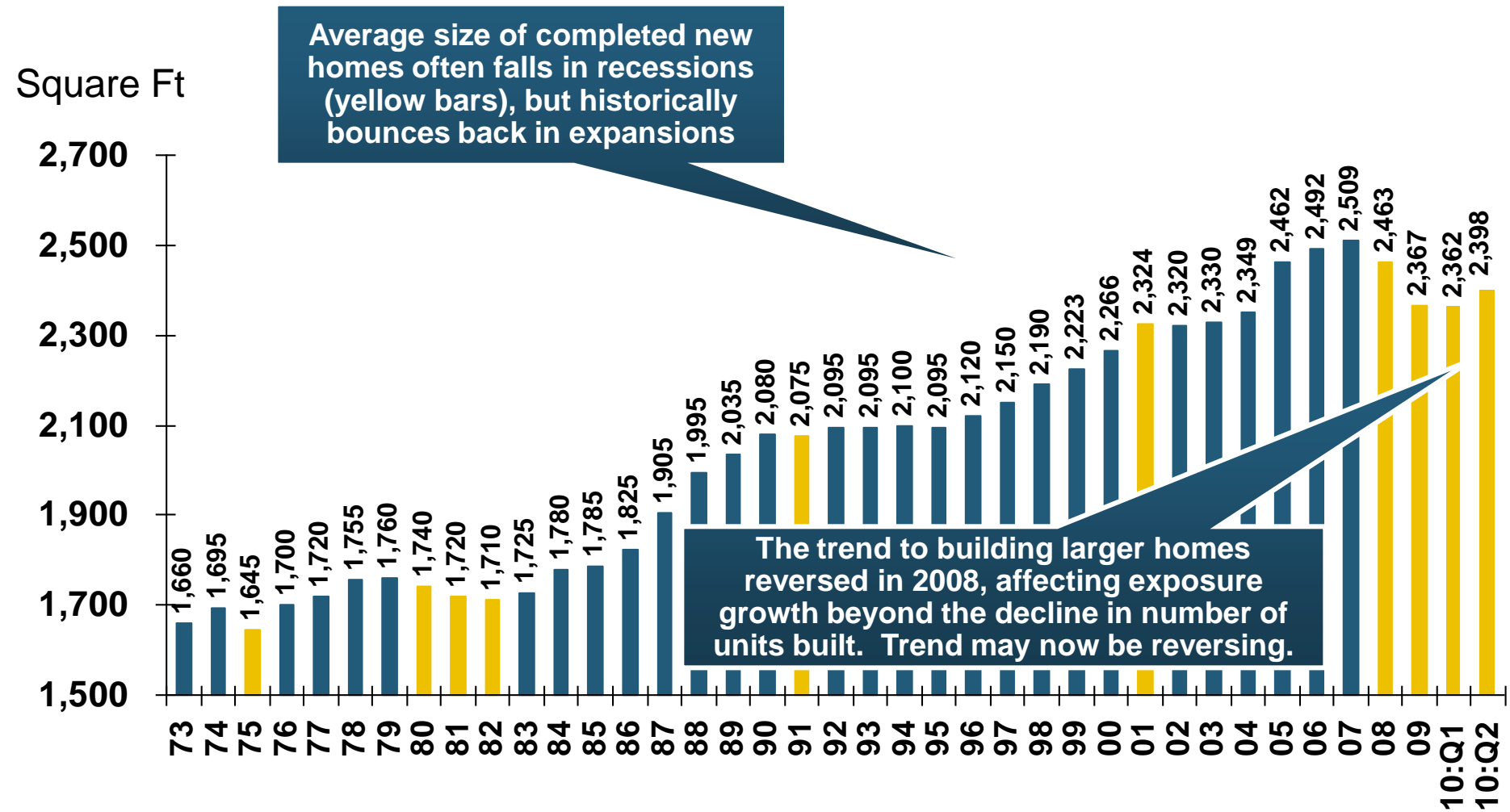
**Economic Obstacles  
to Growth in P/C Insurance Will  
Slowly Be Cleared Away**

# New Private Housing Starts, 1990-2016F

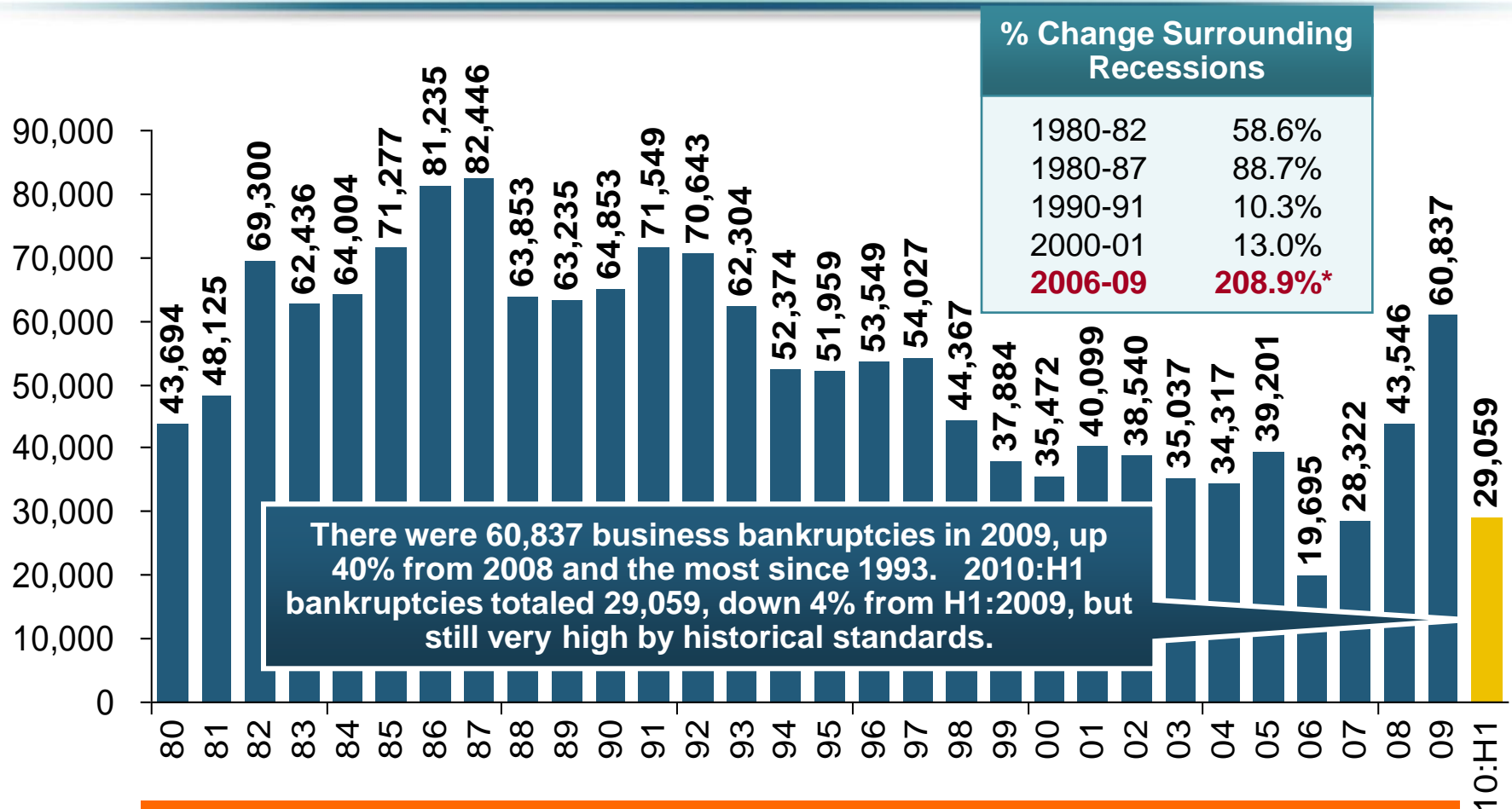


**Little Exposure Growth Likely for Homeowners Insurers Until 2012.  
Also Affects Commercial Insurers with Construction Risk Exposure, Surety**

# Average Square Footage of Completed New Homes in U.S., 1973-2010:Q2



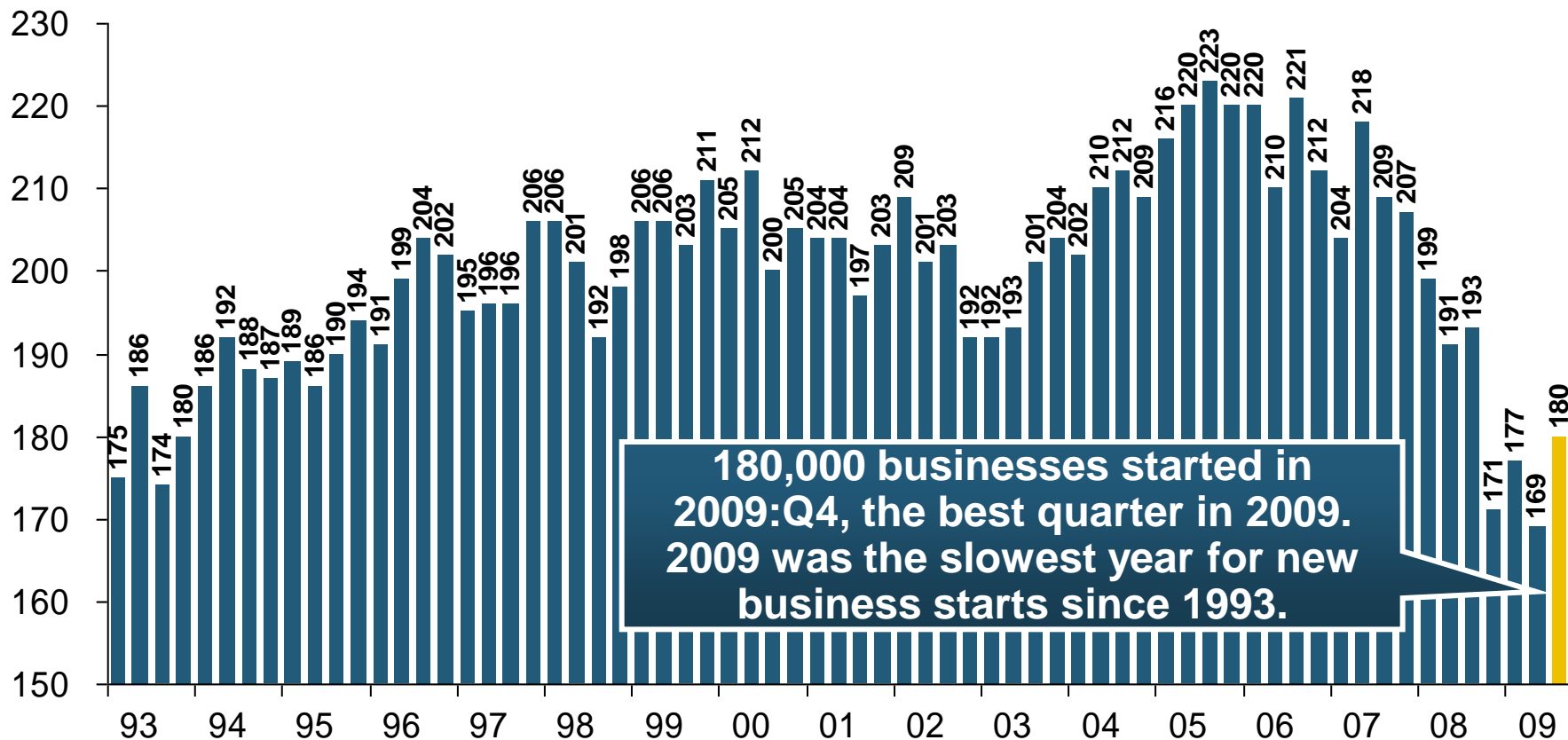
# Business Bankruptcy Filings, 1980-2010:H1



**Significant Exposure Implications for All Commercial Lines.  
There Are Some Preliminary Indications that Business  
Bankruptcies Are Beginning to Decline.**

# Private Sector Business Starts, 1993:Q2 – 2009:Q4\*

(Thousands)



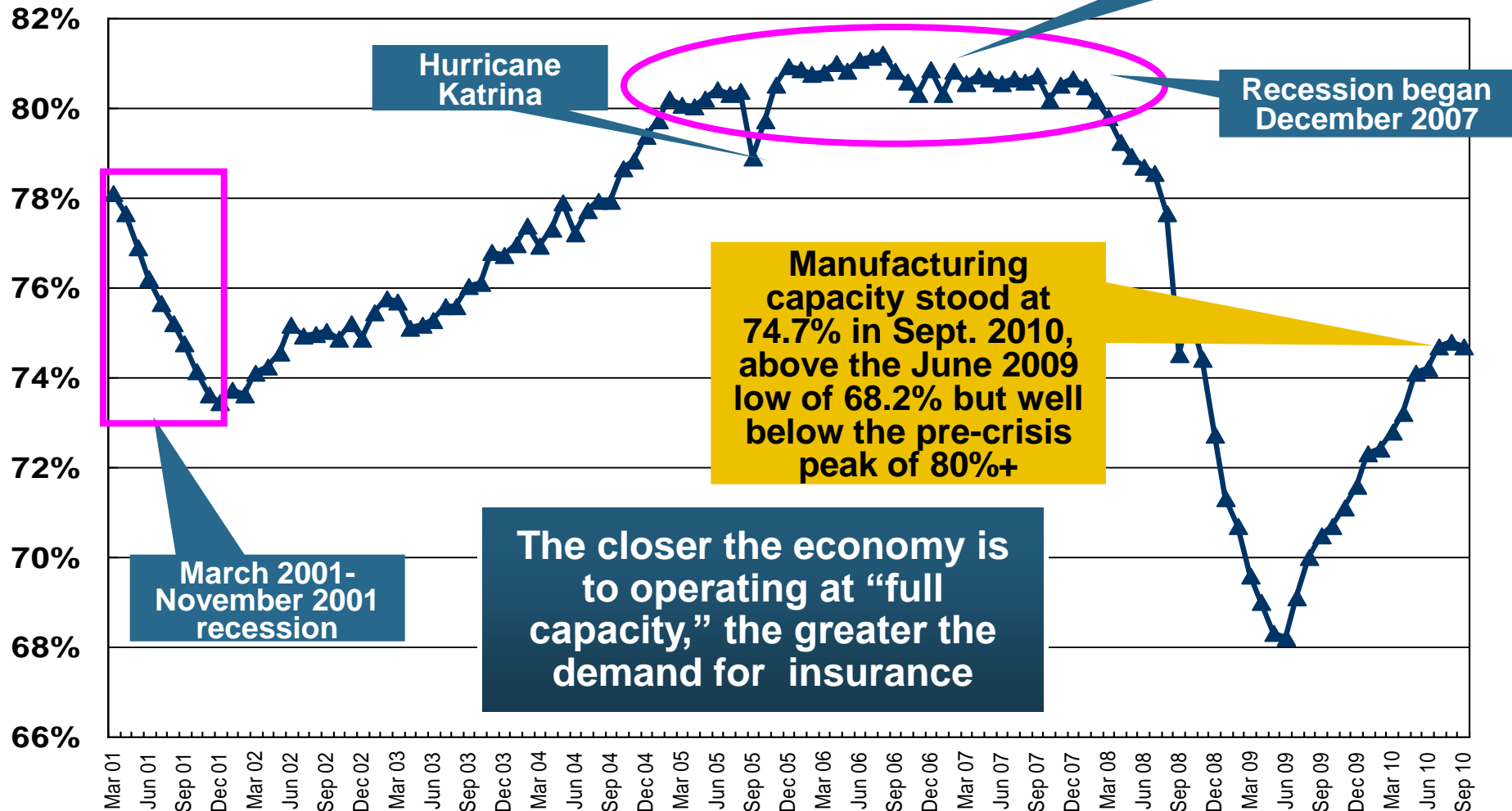
**Business Starts Are Down Nearly 20% in the Current Downturn,  
Holding Back Most Types of Commercial Insurance Exposure**

\*Latest available as of September 12, 2010, seasonally adjusted

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

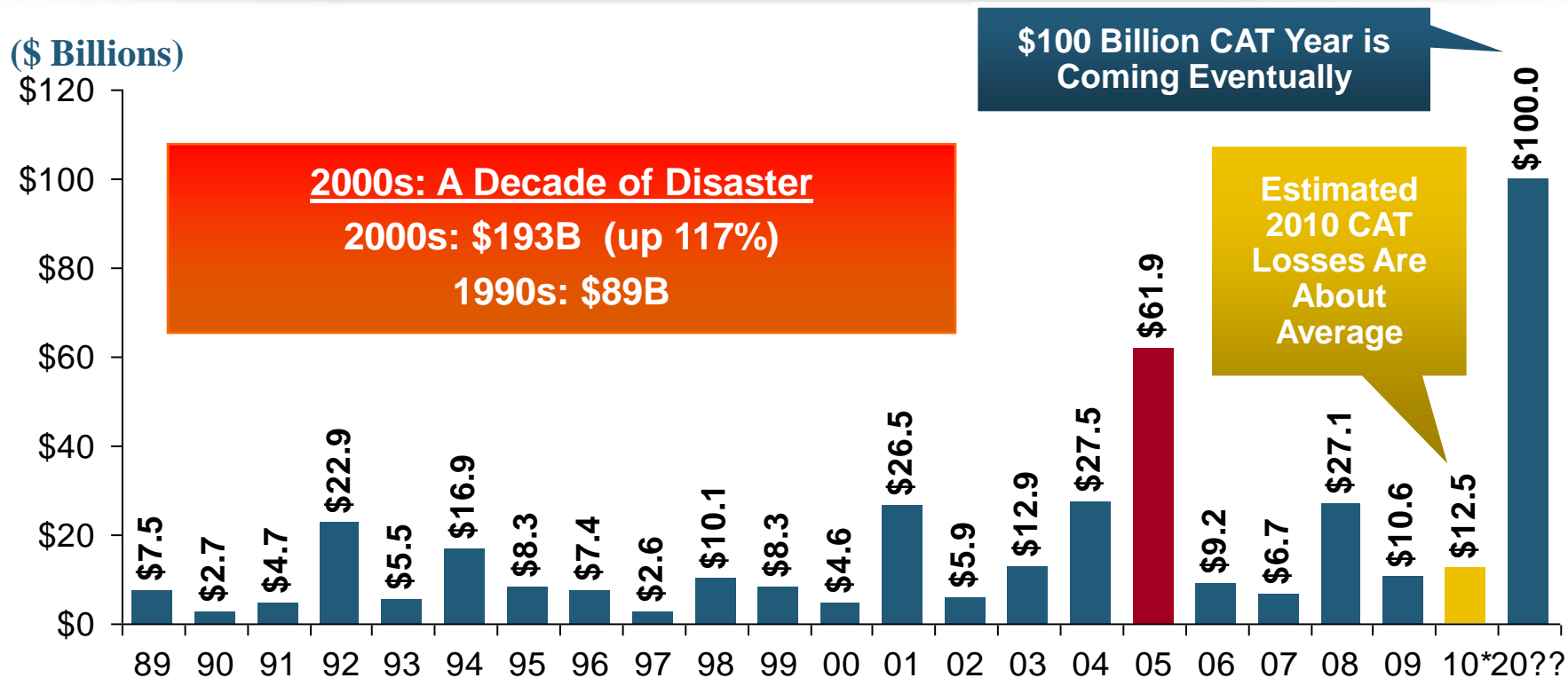
# Recovery in Capacity Utilization is a Positive Sign for Insurance Exposure

Percent of Capacity Utilized  
(Manufacturing, Mining, Utilities)



# **Catastrophic Loss – Catastrophe Losses Trends Are Trending Adversely**

# US Insured Catastrophe Losses



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

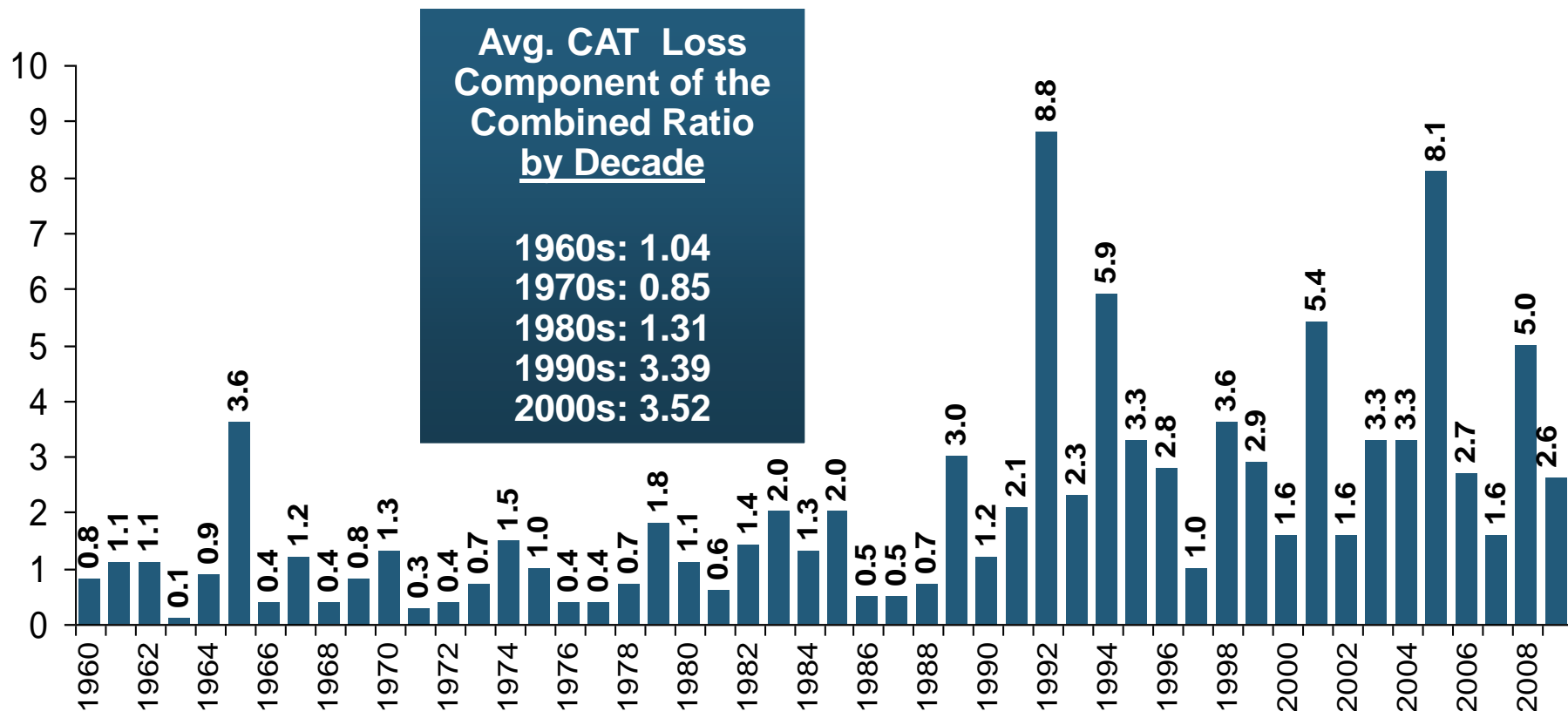
\*Estimate through December 31, 2010.

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

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

# Combined Ratio Points Associated with Catastrophe Losses: 1960 – 2009

## Combined Ratio Points

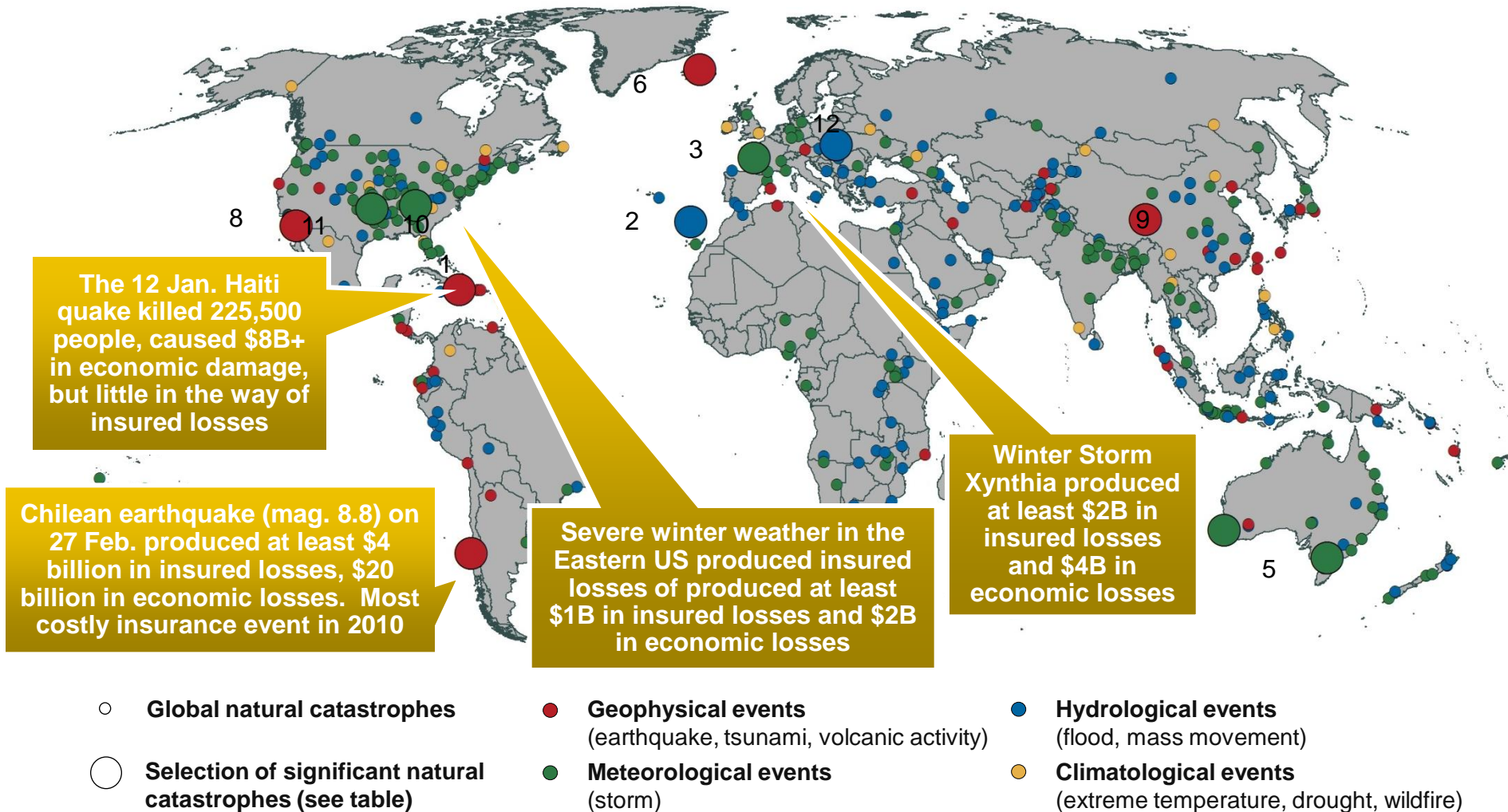


**The Catastrophe Loss Component of Private Insurer Losses Has Increased Sharply in Recent Decades**

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.

# Global Natural Catastrophes: January – June 2010



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

Date	Well	Location	Bbl Spilled
<b>April 20 2010- July 12, 2010</b>	<b>Deepwater Horizon</b>	<b>Gulf of Mexico, USA</b>	<b>est. 4,900,000</b>
June 1979-April 1980	Ixtoc I	Bahia del Campeche, Mexico	3,300,000
October 1986	Abkatun 91	Bahia del Campeche, Mexico	247,000
April 1977	Ekofisk Bravo	North Sea, Norway	202,381
January 1980	Funiwa 5	Forcados, Nigeria	200,000
October 1980	Hasbah 6	Gulf, Saudi Arabia	105,000
December 1971	Iran Marine International	Gulf, Iran	100,000
January 1969	Alpha Well 21 Platform A	Pacific, CA, USA	100,000
March 1970	Main Pass Block 41 Platform C	Gulf of Mexico	65,000
October 1987	Yum II/Zapoteca	Bahia del Campeche, Mexico	58,643
December 1970	South Timbalier B-26	Gulf of Mexico, USA	53,095

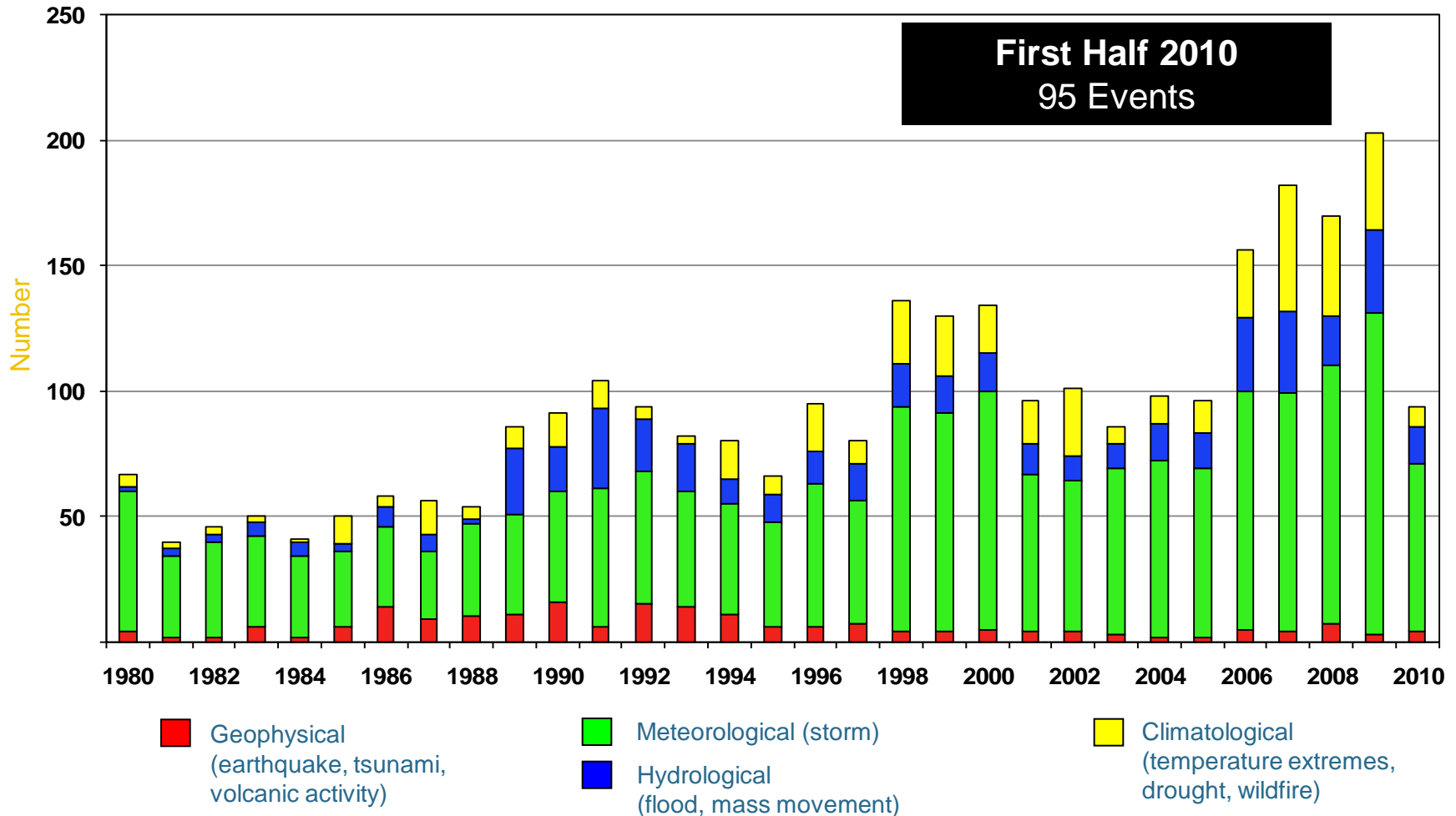
\*Date well was capped. Federal government estimate as of August 2, 2010. Does not include offset for any amounts recovered.

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

# Natural Disasters in the United States, 1980 – 2010

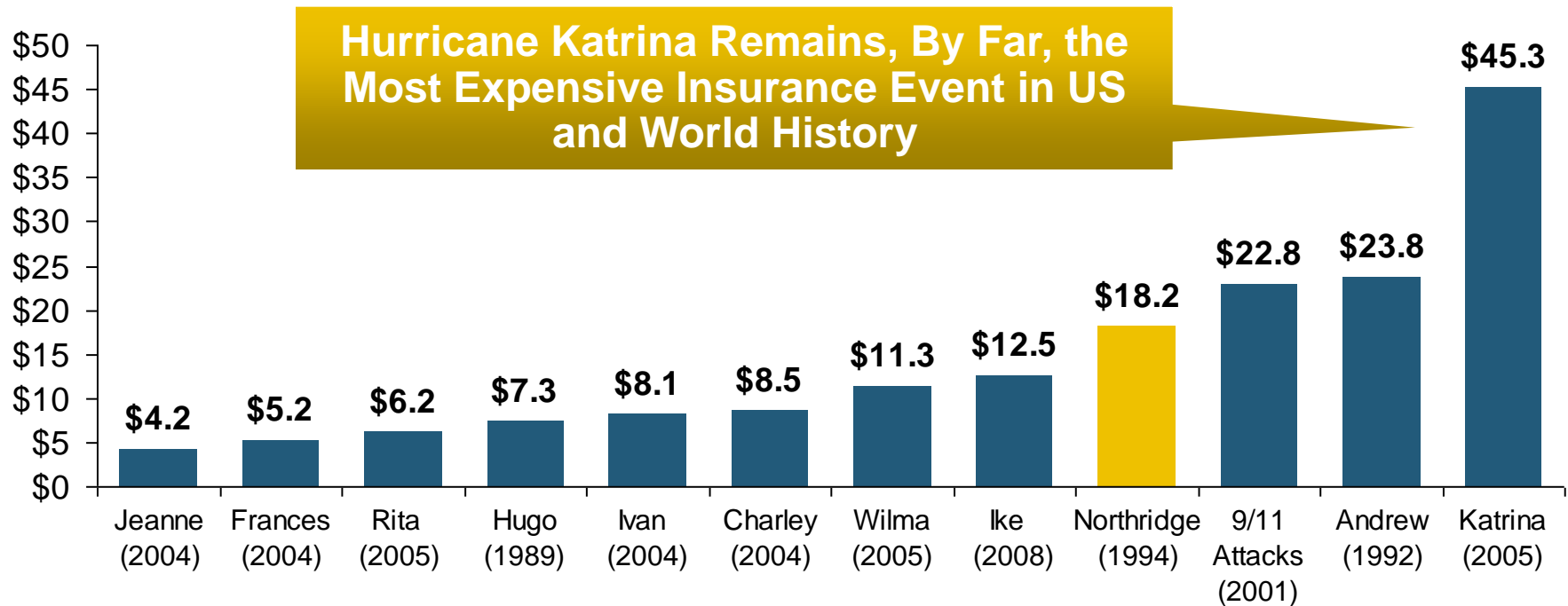
Number of Events (Annual Totals 1980 – 2009 vs. First Half 2010)

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



# Top 12 Most Costly Disasters in US History

(Insured Losses, 2009, \$ Billions)



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

Insurance Information Institute Online:

**[www.iii.org](http://www.iii.org)**

*Thank you for your time  
and your attention!*

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