The Global Economy, Rising Risk and Marine Insurance Markets

Risk and Reward in a Troubled World

San Francisco Board of Marine Underwriters

San Francisco, CA

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Presentation Outline

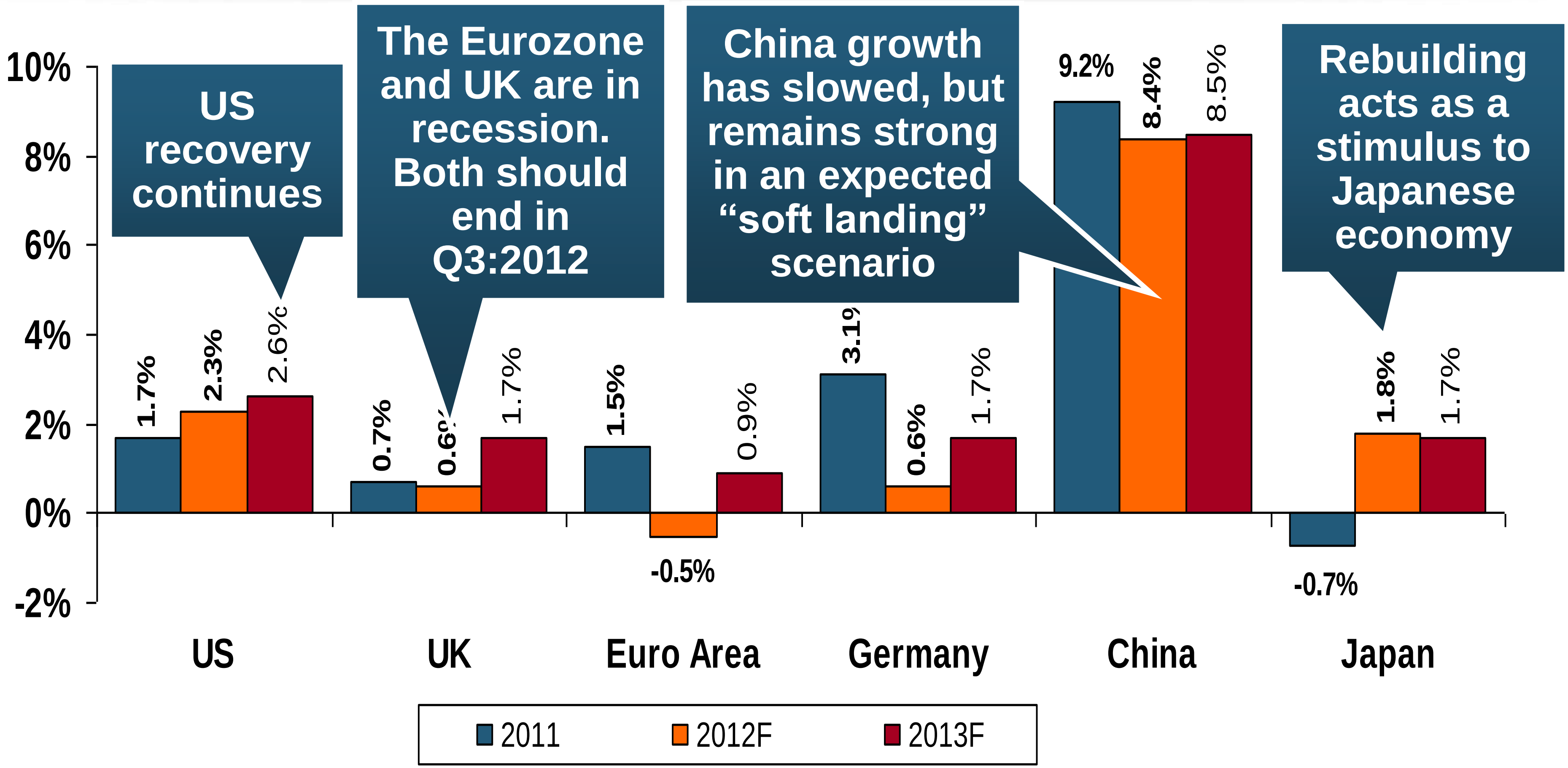
- **Global Economic Overview & Outlook**
  - International Overview
  - Emerging vs. Developing Markets
  - Global Trade Volume Forecasts: Imports/Exports
- **US Economy Overview & Outlook**
  - GDP Outlook
  - Drivers of P/C Insurance Exposures
  - Marine Drivers
  - Presidential Politics and P/C Profitability
- **The Unfortunate Nexus of Opportunity, Risk and Uncertainty**
  - The Fusion of Economic and (Geo)Political Risk
  - Top 10 Risks for the Global Economy
- **Global Catastrophe Loss Trends and Threats**
  - Was 2011 an Aberration or a Foreshadowing of the Future
- **US P/C Insurance Industry Financial Overview & Outlook**

Global Economic Outlook: Regional and Major Economy Perspectives

Strength of Economies Varies Greatly as Does Pace of Recovery from the Economic Challenges

Important Consequences for Insurer and Reinsurer Growth Opportunities

Real GDP Growth Forecasts: Major Economies: 2011 – 2013F



Growth Prospects Vary Widely by Region: Brightening in the US, Mild Recession in the Eurozone, A “Soft Landing” in China, Strength in India, Reconstruction Stimulus in Japan and Modest Growth in America’s Largest Trading Partners—Canada and Mexico.

Sources: Blue Chip Economic Indicators (4/2012 issue); Insurance Information Institute.

Real GDP Growth Forecasts: Emerging Market Regions: 2010 – 2013F

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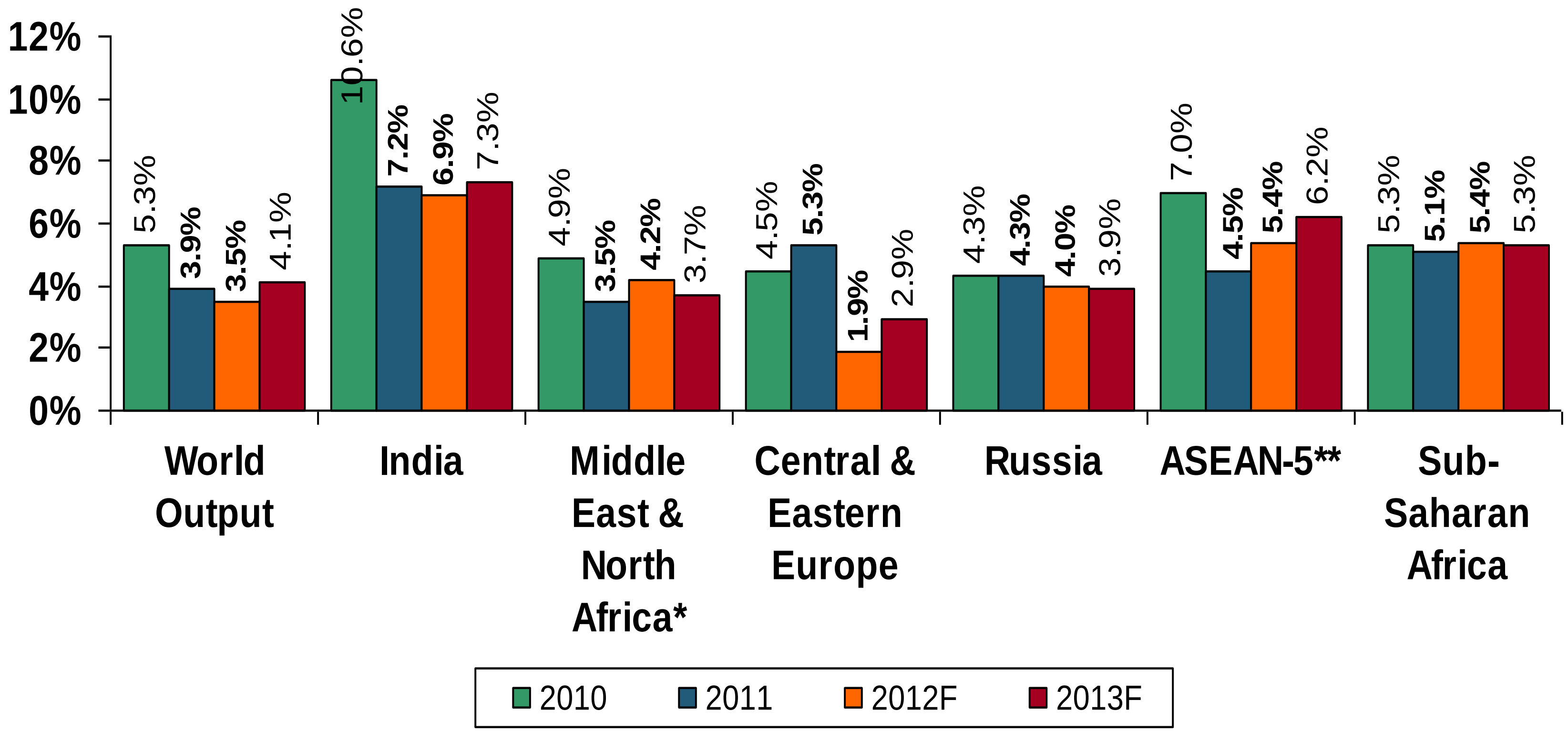
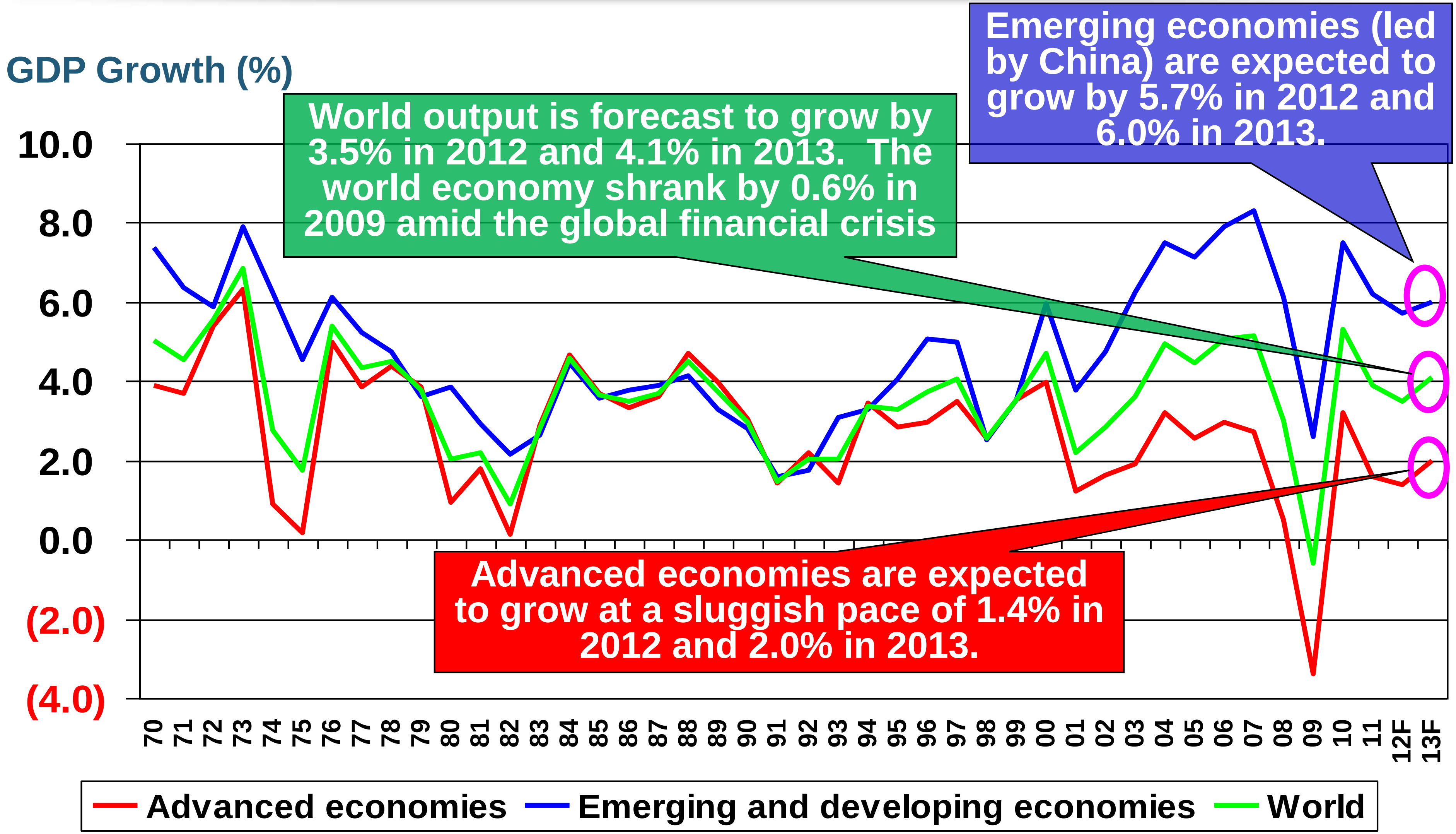


Growth Prospects Vary Widely by Region: All Regions Slowed in 2011 As Economic Recovery Encountered Many Challenges. IMF Outlook for 2012 Is Mixed With Broader, More Robust Growth in 2013 Predicted. Actual Growth in 2012 Could Surprise to the Upside.

*Excludes Libya in 2011. **Indonesia, Malaysia, Thailand, Philippines and Vietnam

Sources: IMF *World Economic Outlook* (April 2012); Insurance Information Institute.

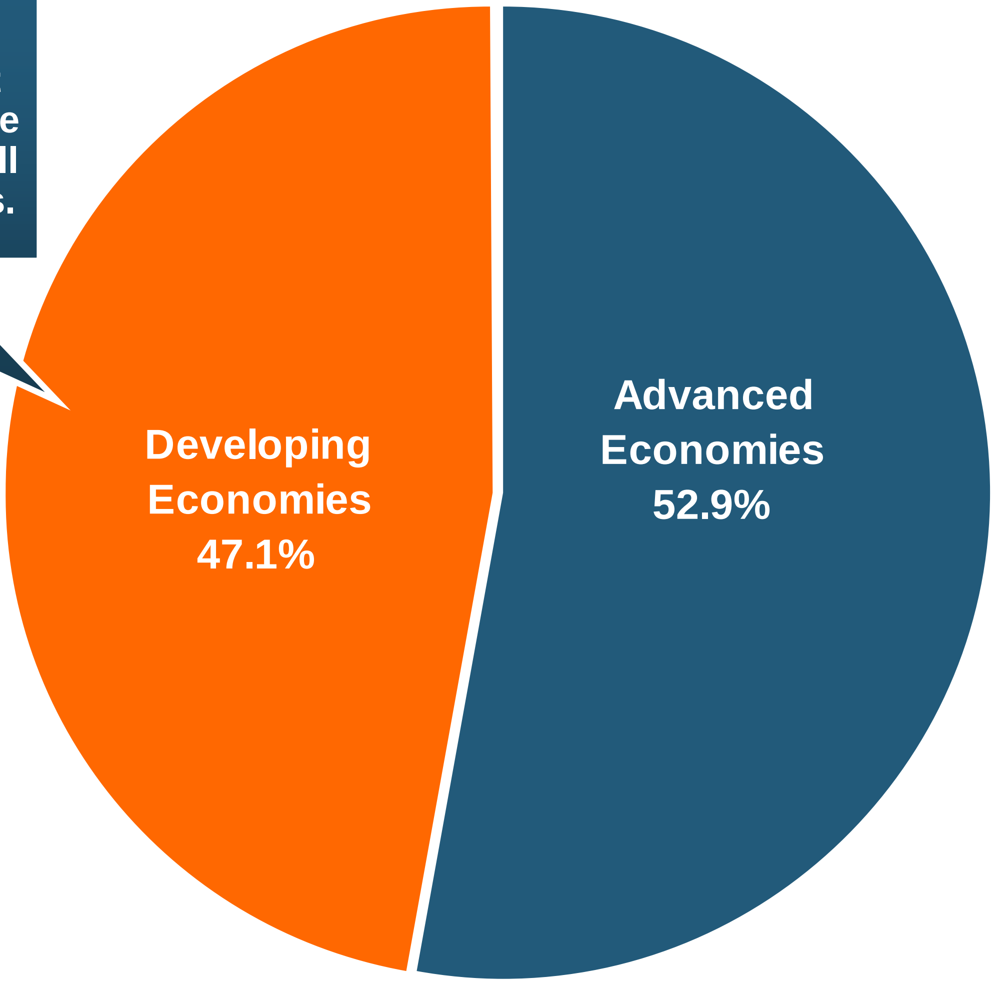
GDP Growth: Advanced & Emerging Economies vs. World, 1970-2013F



Source: International Monetary Fund, *World Economic Outlook Update*, Apr. 2012; Ins. Info. Institute.

Relative Shares of Global Output, Advanced vs. Developing Economies, 2009

The gap is closing quickly. China became the world's second largest economy in 2010 and before long the developing world's share of GDP will exceed that of advanced economies.



Source: EDC Economics, "The Moment of Truth: Global Export Forecast Fall 2010, at http://www.edc.ca/english/docs/gef_e.pdf

Current Real GDP Growth vs. Pre-Crisis Average (2000-2007 vs. 2011F-2012F*)

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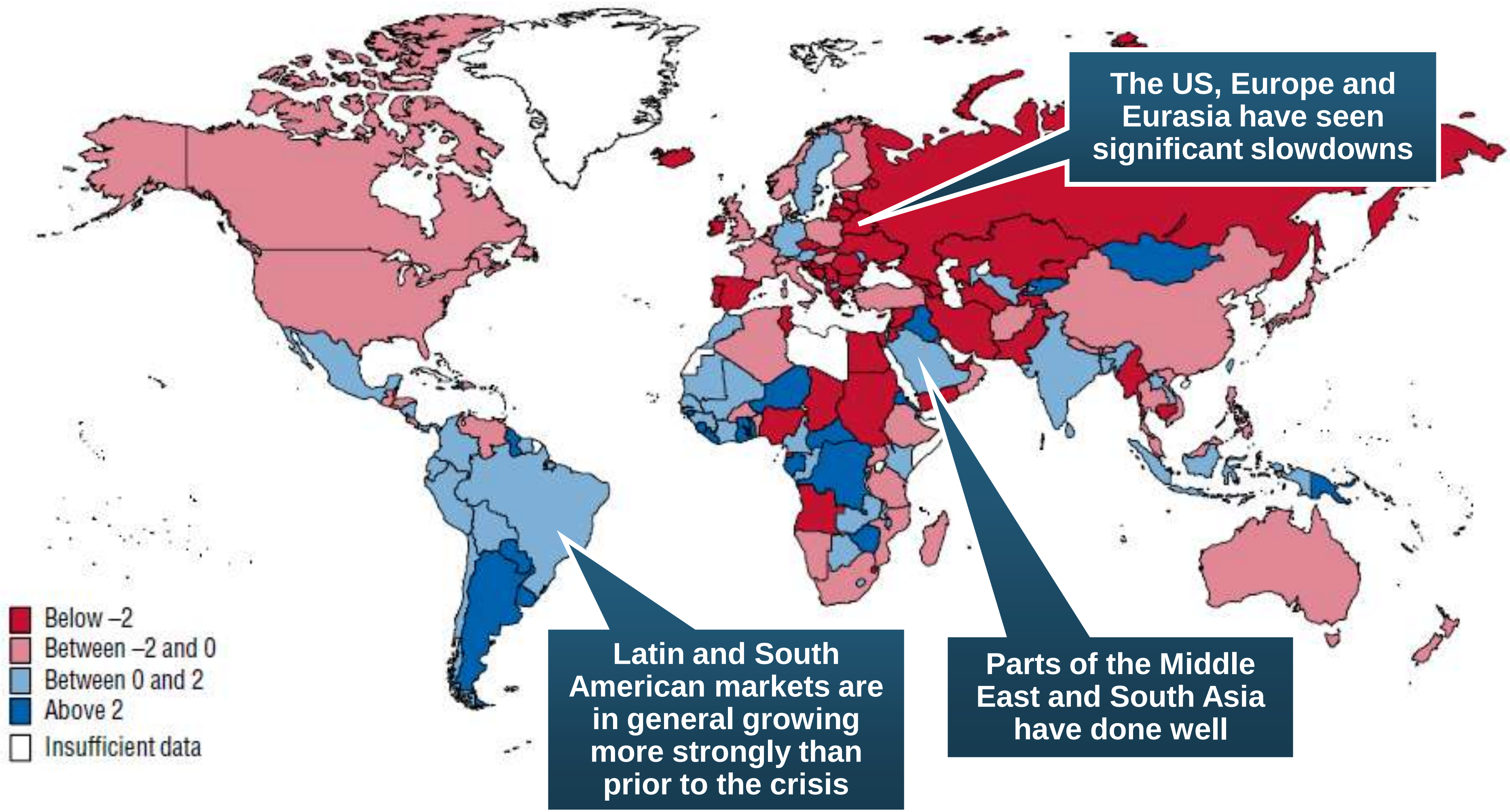

*Percentage point difference between compound annual rates of change 2000-2007 vs. forecasts for 2011-2012.

Source: IMF, World Economic Outlook, September 2011; Insurance Information Institute.

Current Real GDP Growth vs. Pre-Crisis Average (2000-2007 vs. 2011F-2012F*)

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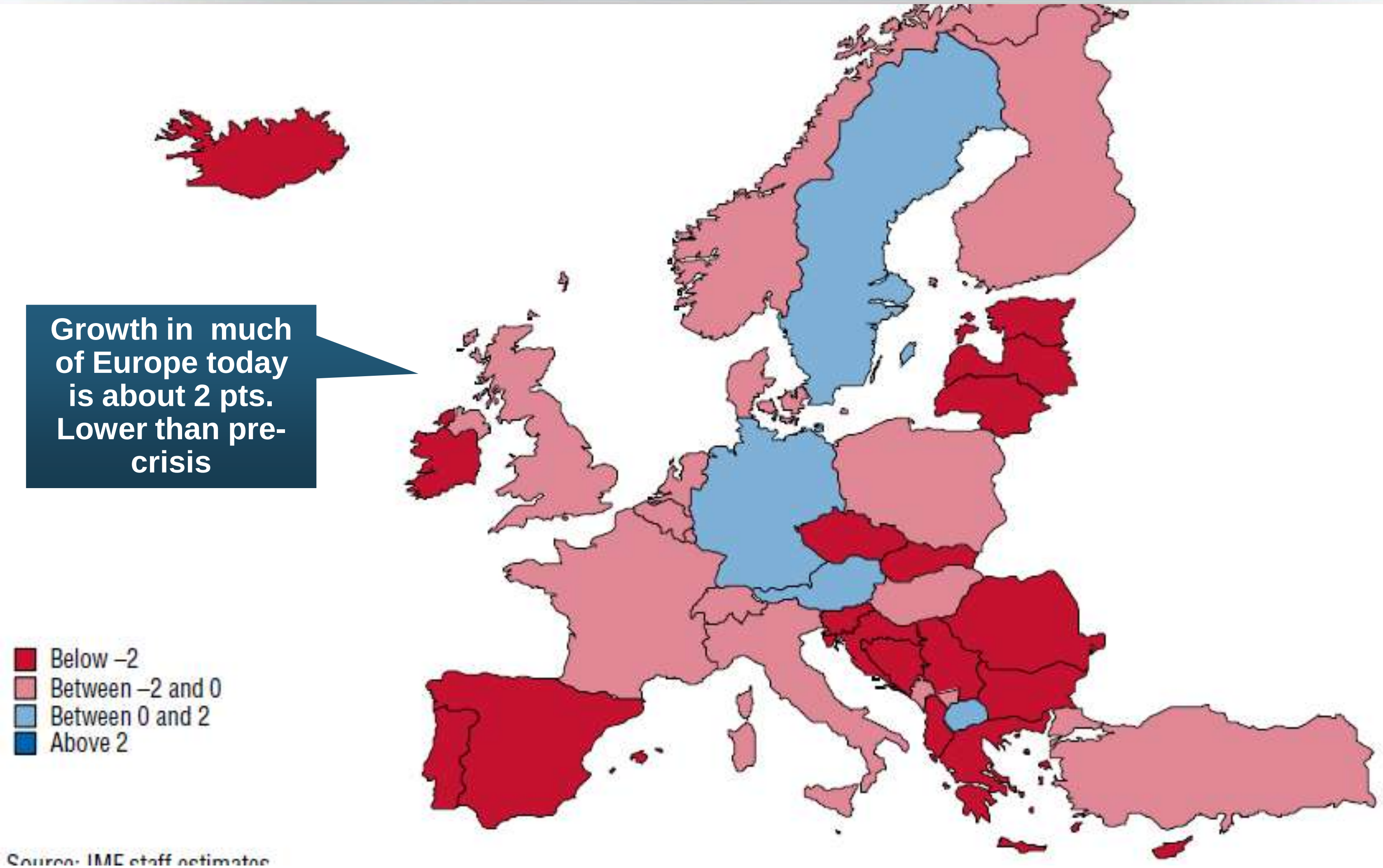

*Percentage point difference between compound annual rates of change 2000-2007 vs. forecasts for 2011-2012.

Source: IMF, World Economic Outlook, September 2011; Insurance Information Institute.

World Trade Volume: 2010—2013F

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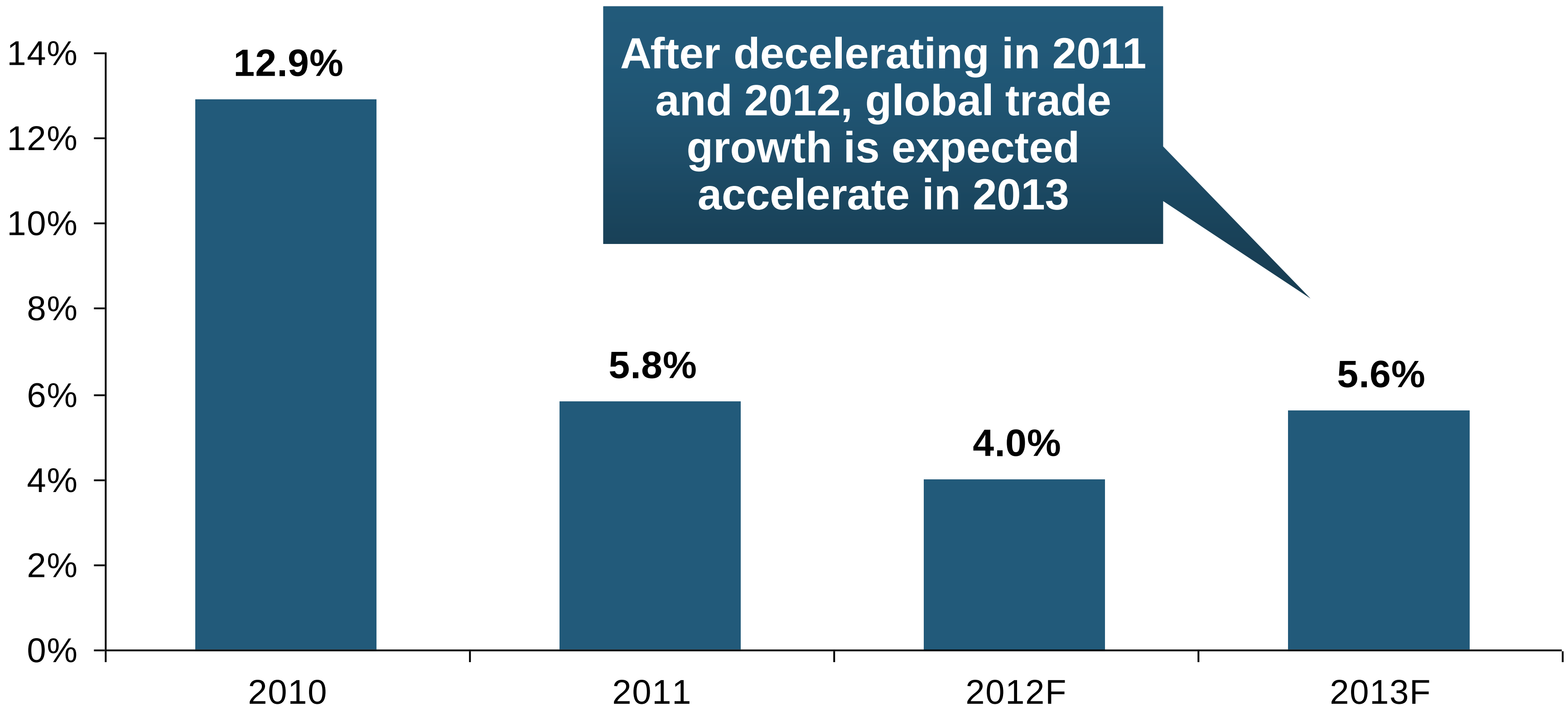
Percentage Change (%)



Growth in World Trade Volume (Imports + Exports) Has Slowed But Continues to Grow

Sources: IMF *World Economic Outlook* (April 2012); Insurance Information Institute.

World Trade Volume: Imports 2010 – 2013F

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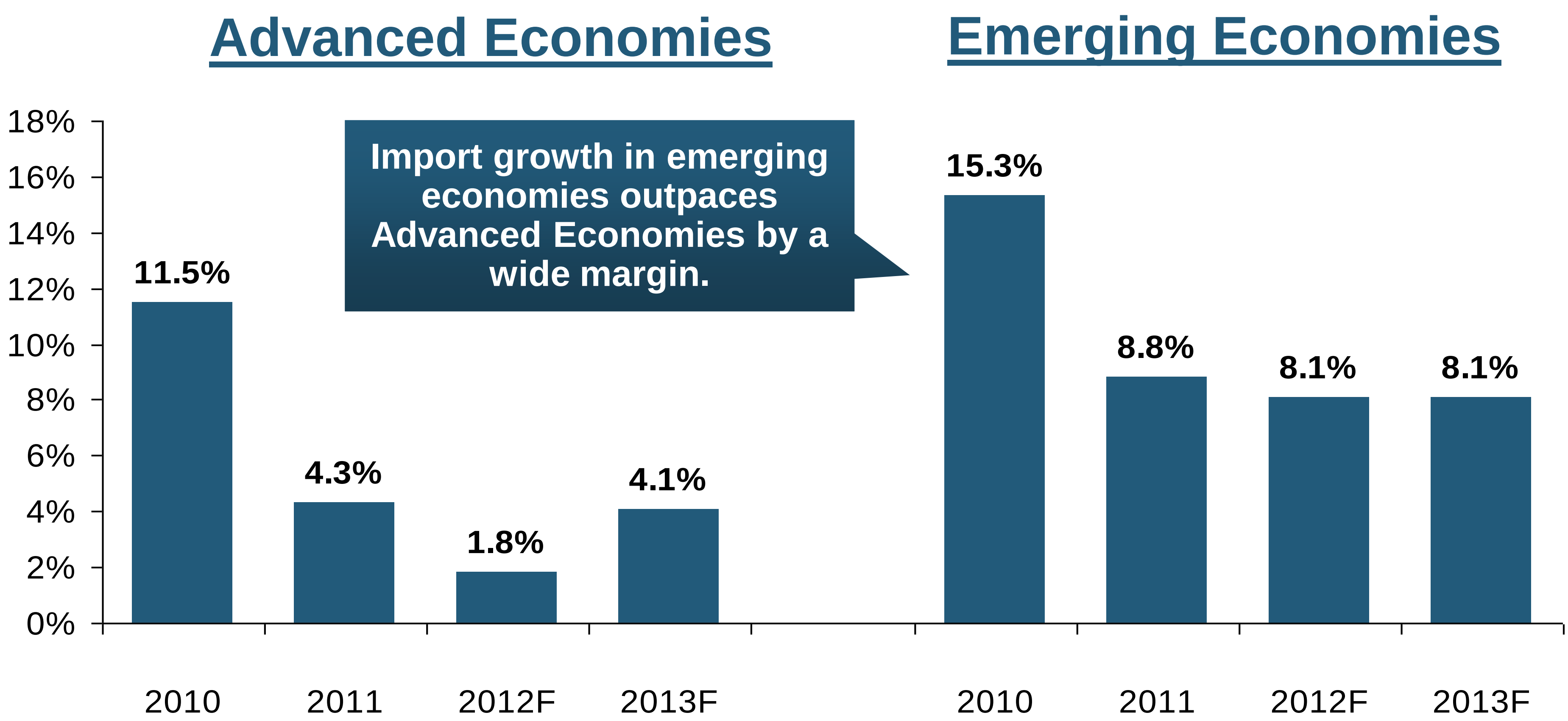
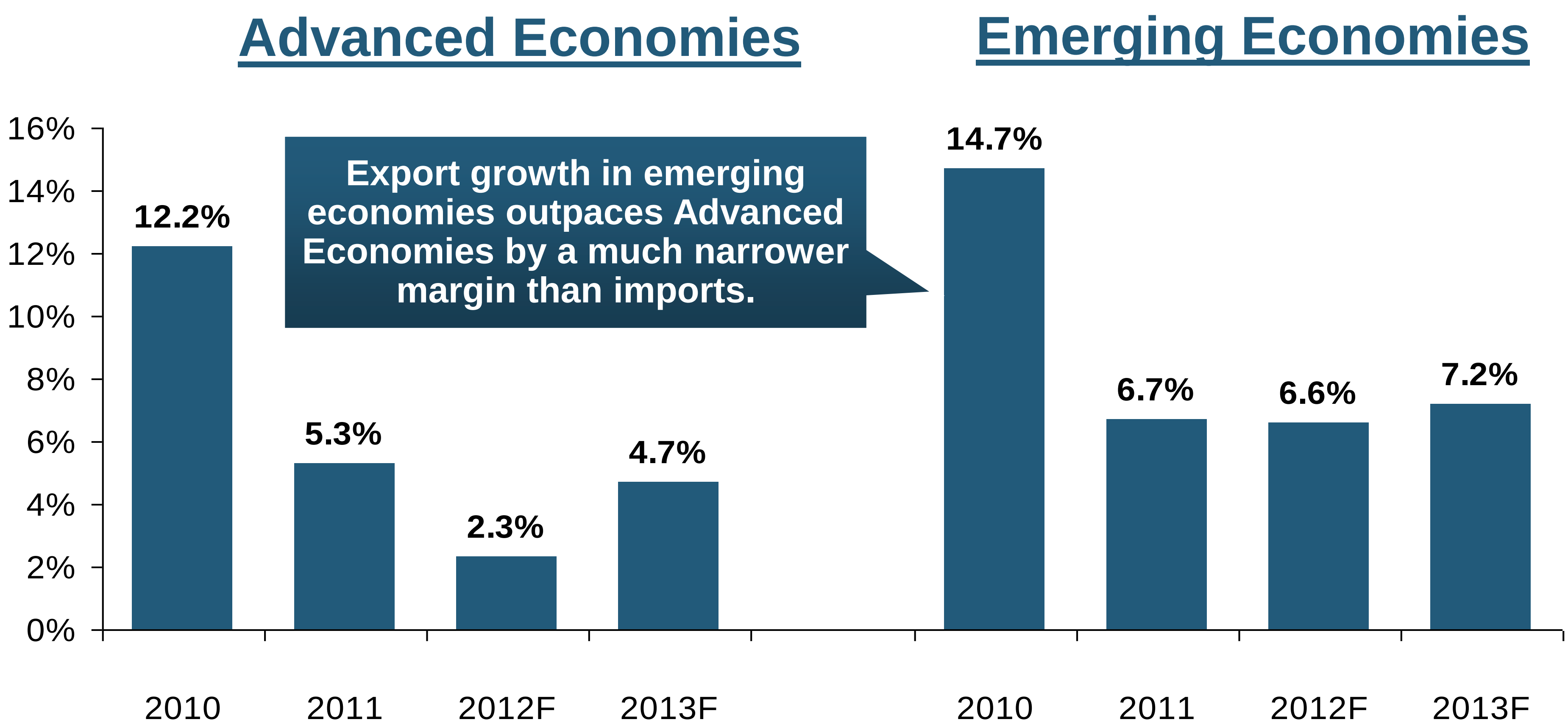
Growth (%)



Sources: IMF *World Economic Outlook* (April 2012); Insurance Information Institute.

World Trade Volume: Exports 2010 – 2013F

Growth (%)

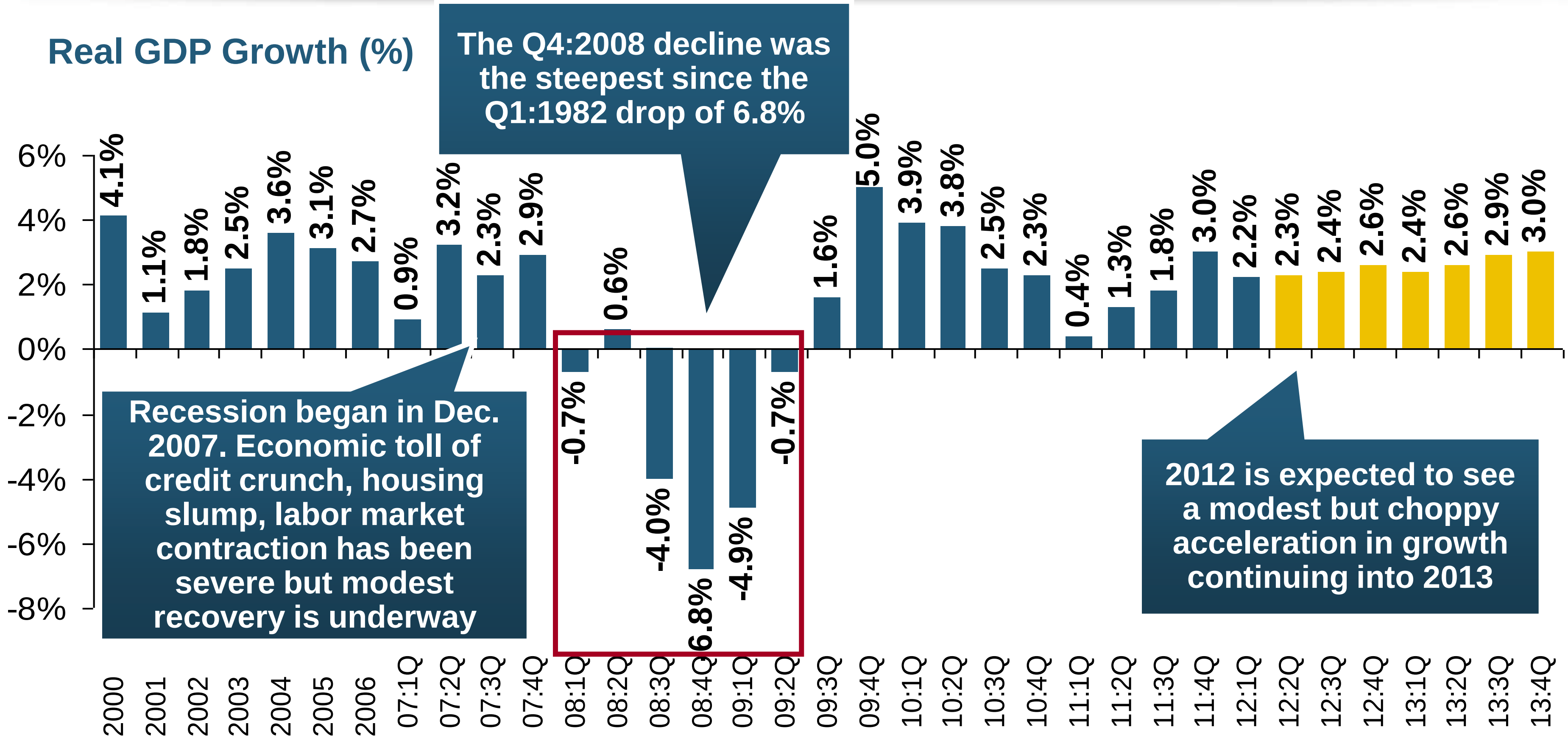


Sources: IMF *World Economic Outlook* (April 2012); Insurance Information Institute.

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

All Lines of Commercial Insurance Will Benefit, Including Marine

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 4/12; Insurance Information Institute.

Consumer Sentiment Survey *(1966 = 100)*

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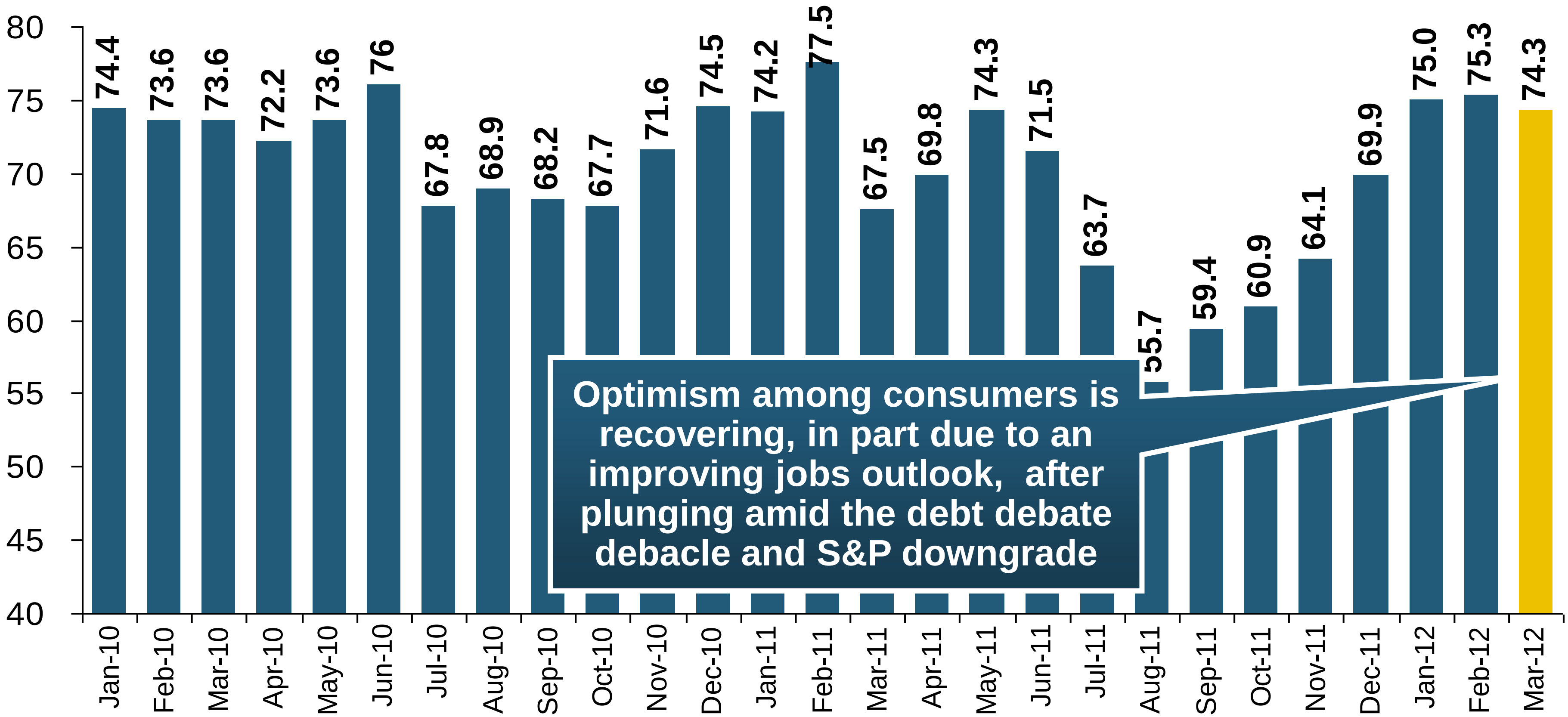
January 2010 through March 2012



Consumer confidence has been low for years amid high unemployment, falling home prices and other factors adversely impact consumers, but improved substantially in late 2011 and early 2012

Source: University of Michigan; Insurance Information Institute

Auto/Light Truck Sales, 1999-2022F

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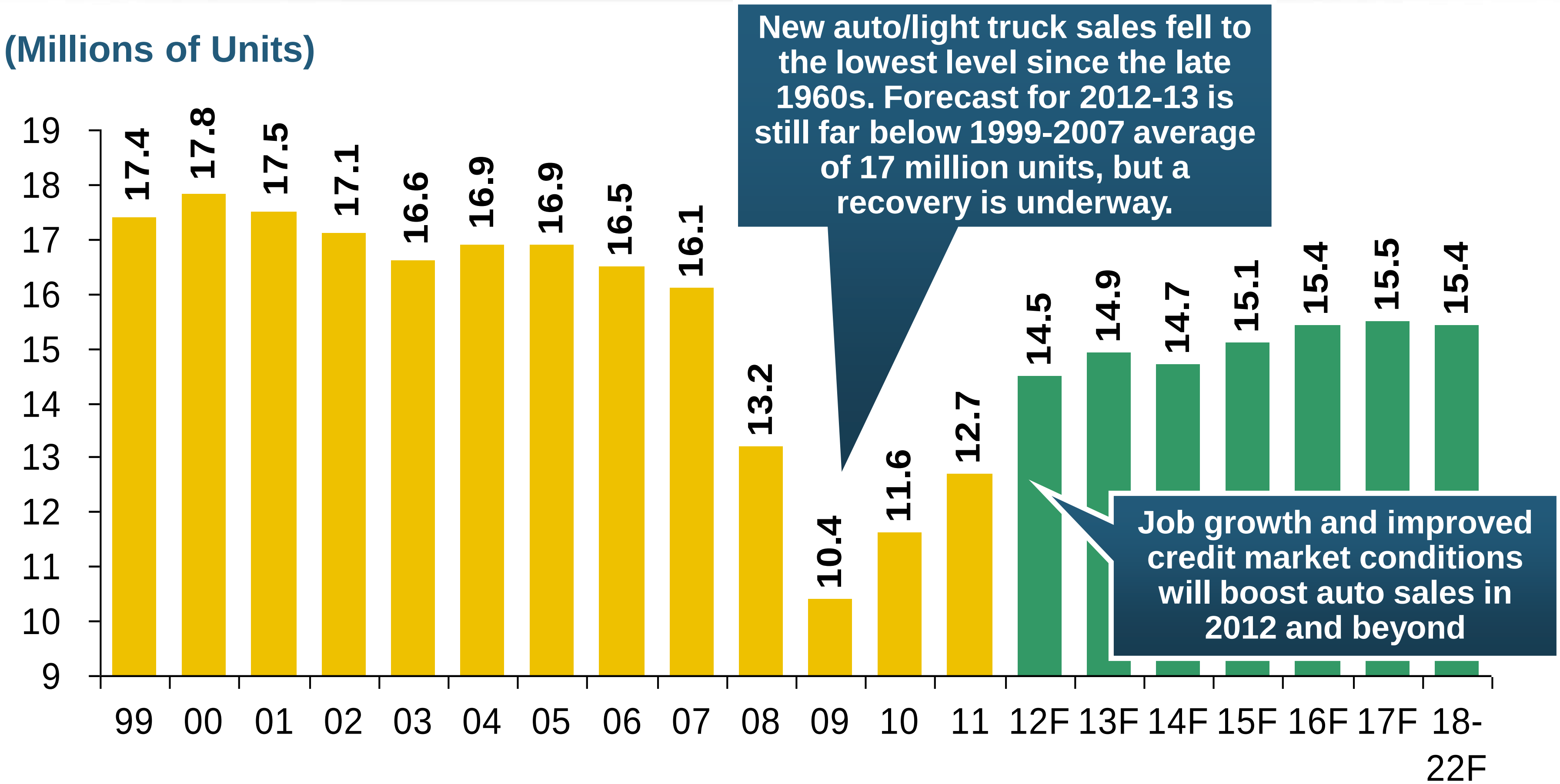

Car/Light Truck Sales Will Continue to Recover from the 2009 Low Point, Bolstering the Auto Insurer Growth and the Manufacturing Sector.

Source: U.S. Department of Commerce; Blue Chip Economic Indicators (10/11 and 4/12); Insurance Information Institute.

Value of Construction Put in Place, Feb. 2012 vs. Feb. 2011*

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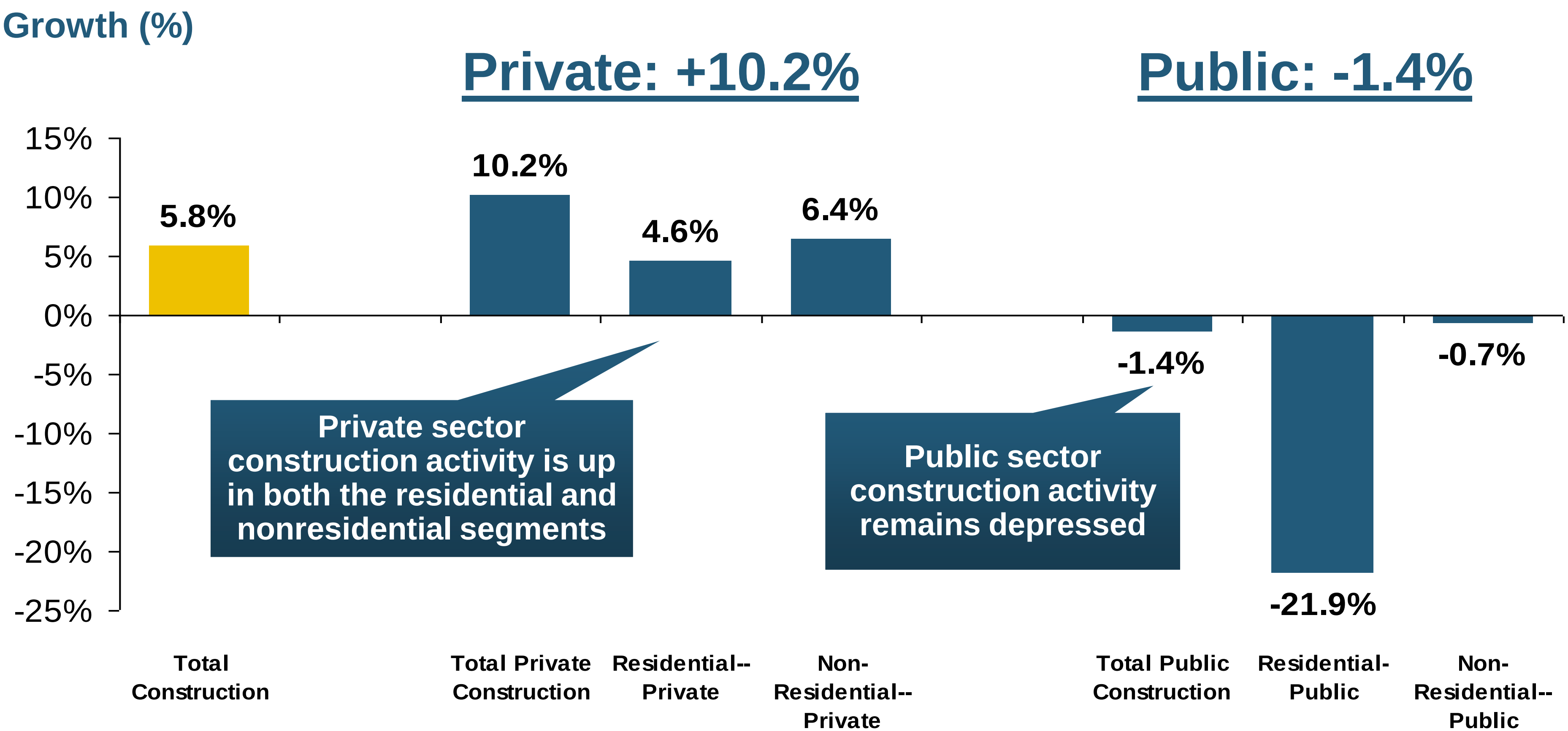
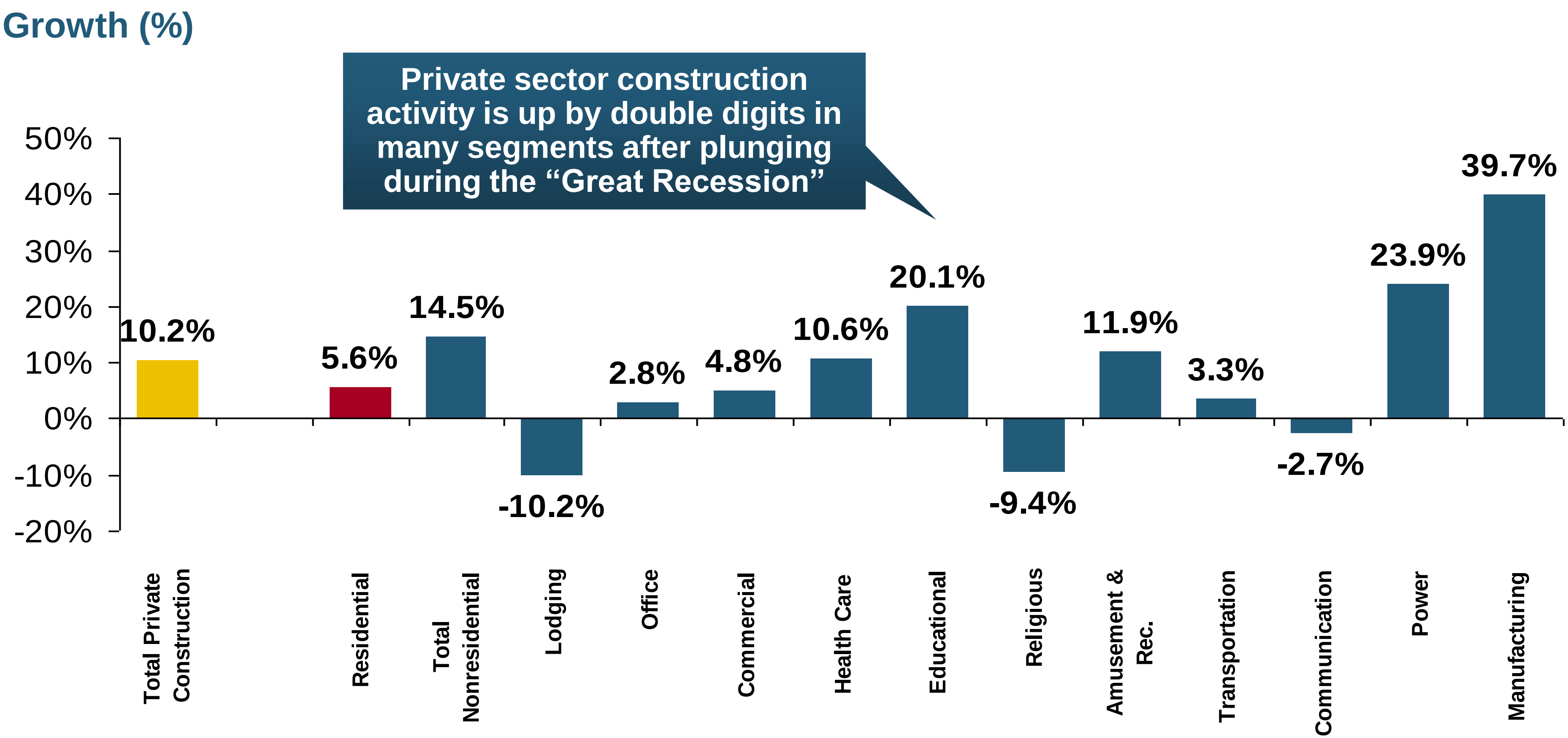


Overall Construction Activity is Up, But Growth Is Entirely in the Private Sector as State/Local Government Budget Woes Continue

*seasonally adjusted
Source: U.S. Census Bureau, http://www.census.gov/construction/c30/c30index.html ; Insurance Information Institute.

Value of Private Construction Put in Place, by Segment, Feb. 2012 vs. Feb. 2011*



Private Construction Activity is Up in Most Segments, Including Residential Construction

*seasonally adjusted
Source: U.S. Census Bureau, http://www.census.gov/construction/c30/c30index.html ; Insurance Information Institute.

ISM Manufacturing Index
(Values > 50 Indicate Expansion)

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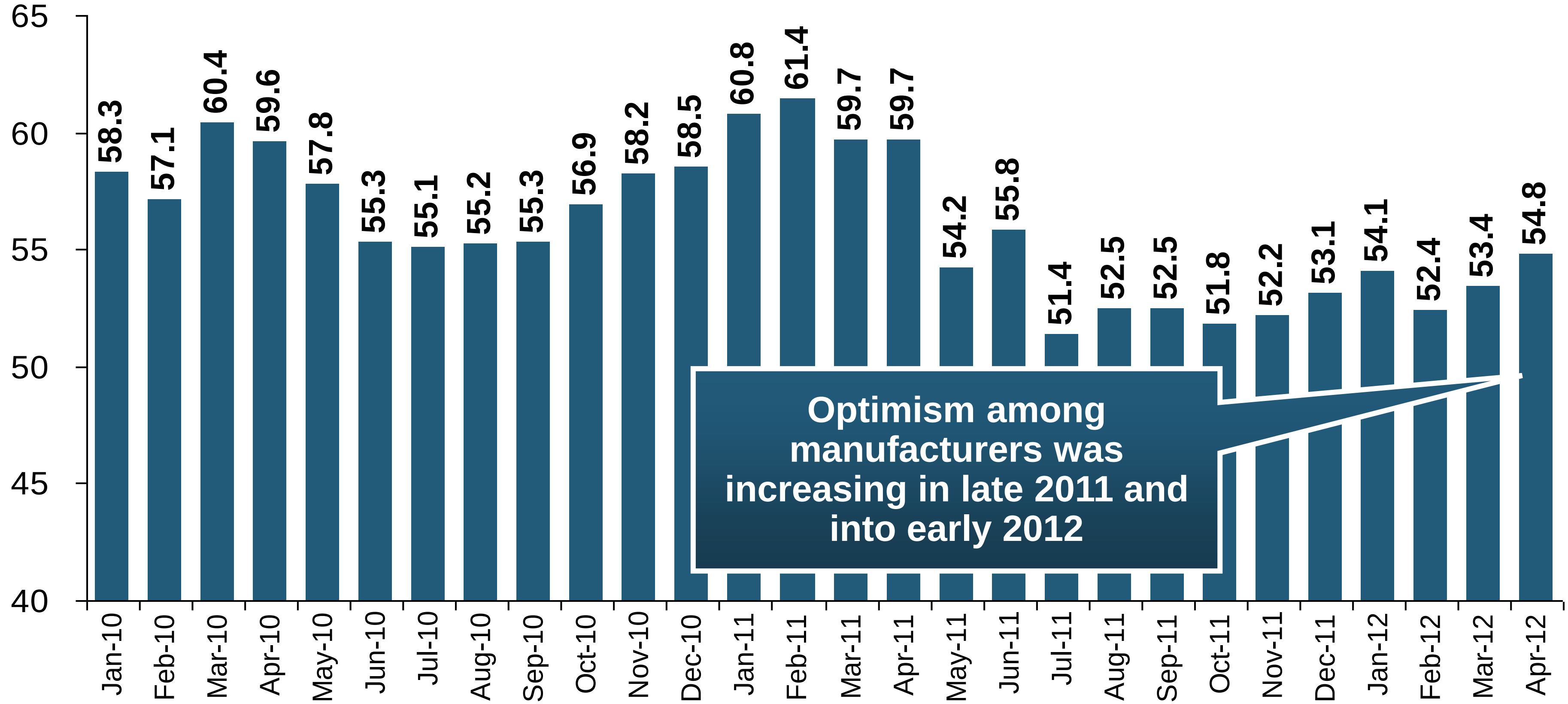
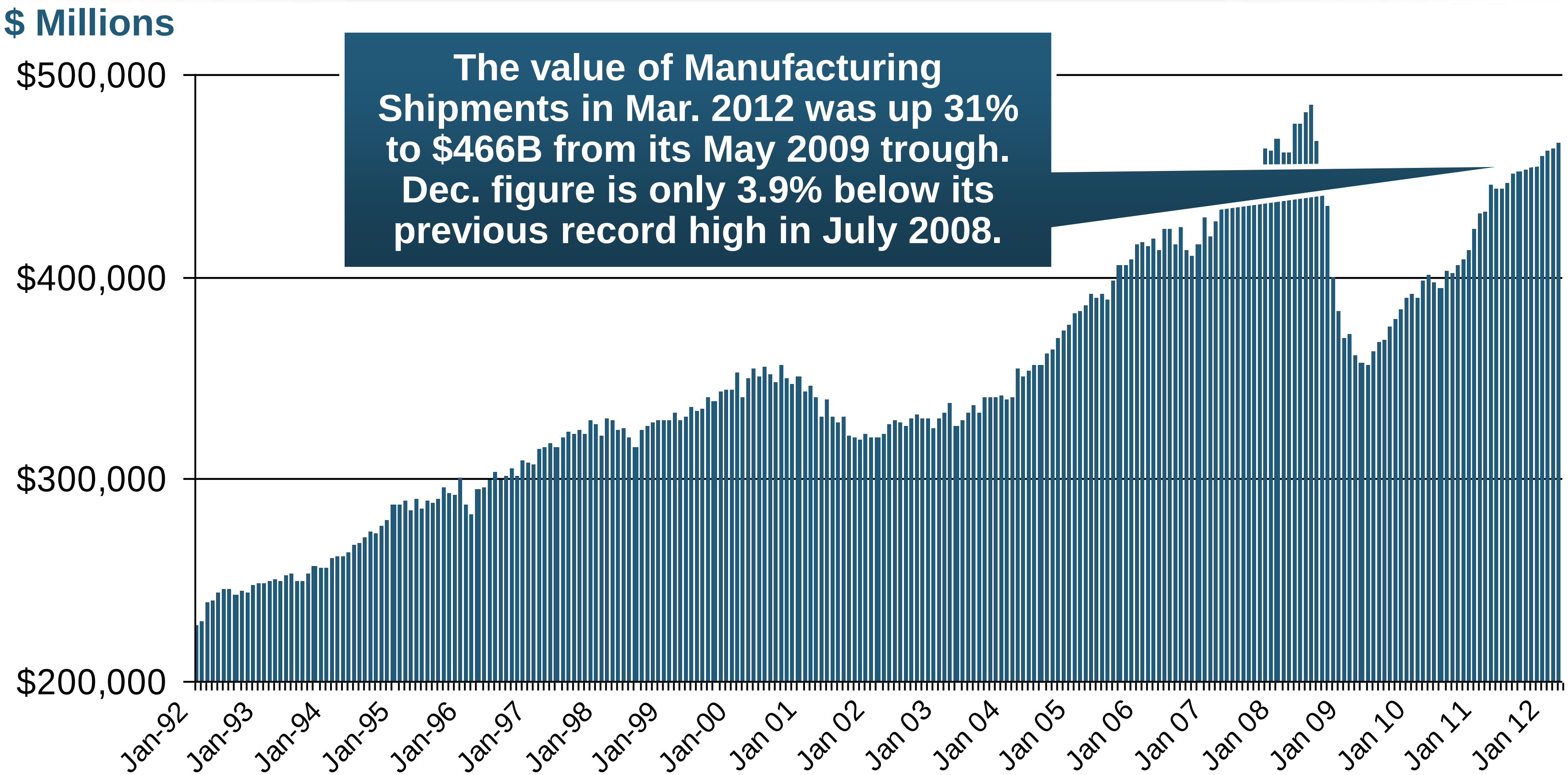
January 2010 through April 2012



The manufacturing sector has been expanding and adding jobs. The question is whether this will continue.

Source: Institute for Supply Management at http://www.ism.ws/ismreport/mfgrob.cfm; Insurance Information Institute.

Dollar Value* of Manufacturers' Shipments Monthly, Jan. 1992—Mar. 2012

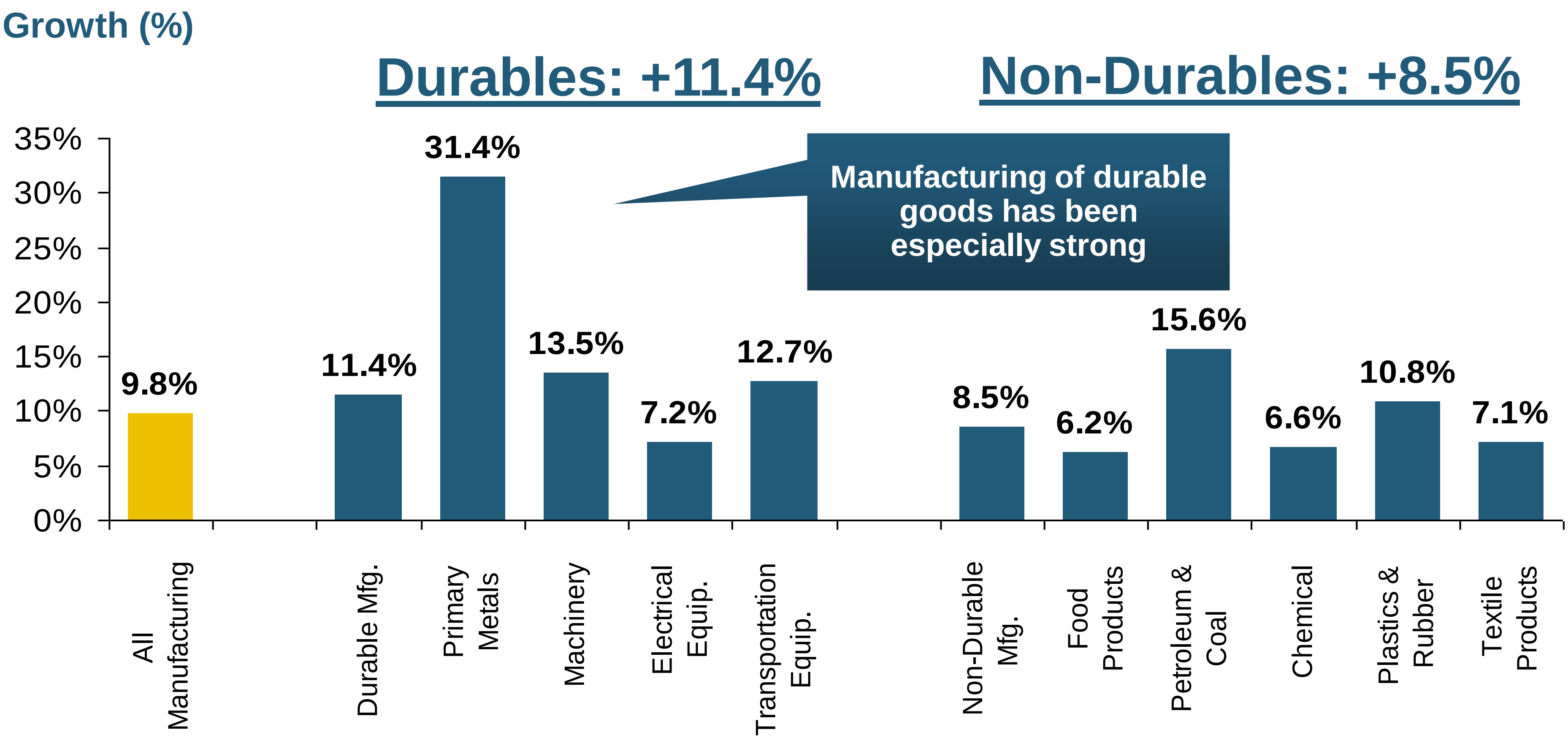


Monthly shipments are nearly back to peak (in July 2008, 8 months into the recession). Trough in May 2009. Growth from trough to March 2012 was 31%. This growth leads to gains in many commercial exposures: WC, Commercial Auto, Marine, Property and Various Liability Coverages

*seasonally adjusted

Source: U.S. Census Bureau, *Full Report on Manufacturers' Shipments, Inventories, and Orders*, http://www.census.gov/manufacturing/m3/

Manufacturing Growth for Selected Sectors, 2012 vs. 2011*



Manufacturing Is Expanding Across a Wide Range of Sectors that Will Contribute to Growth in Insurable Exposures Including: WC, Commercial Property, Commercial Auto and Many Liability Coverages

*Seasonally adjusted; Date are YTD comparing data through Feb. 2012 to the same period in 2011.
Source: U.S. Census Bureau, *Full Report on Manufacturers' Shipments, Inventories, and Orders,* http://www.census.gov/manufacturing/m3/

Recovery in Capacity Utilization is a Positive Sign for Commercial Exposures

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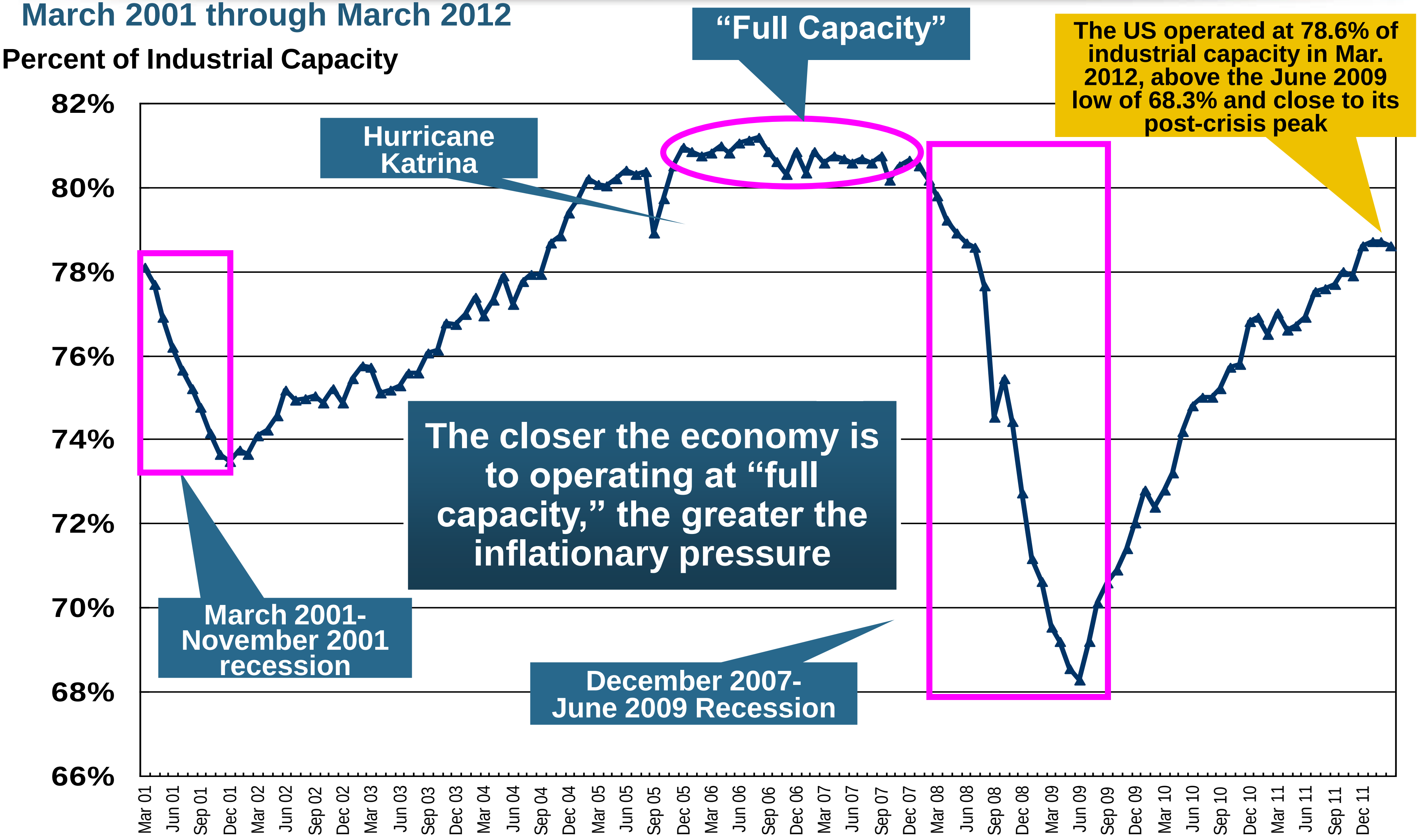
March 2001 through March 2012



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

Global Industrial Production (2000-Feb. 2012)

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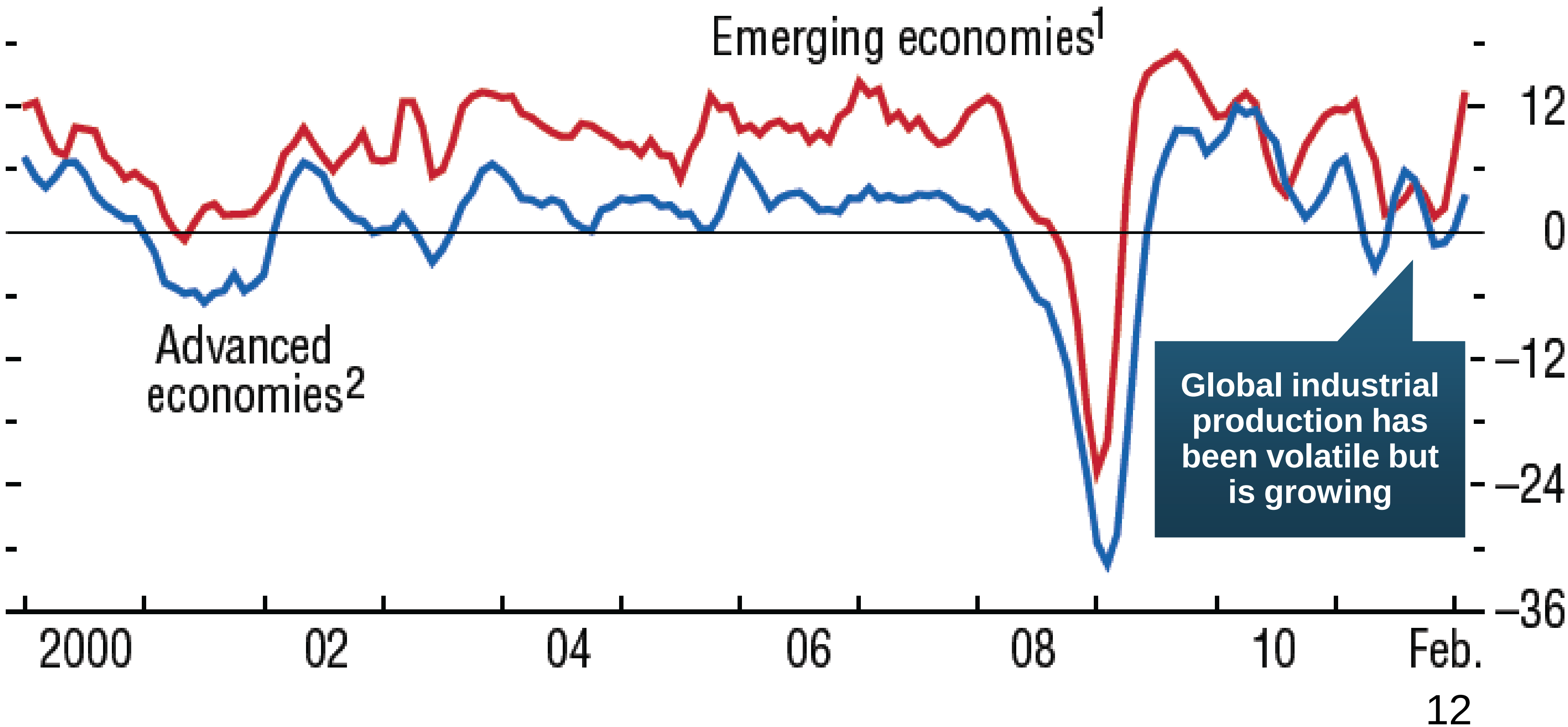
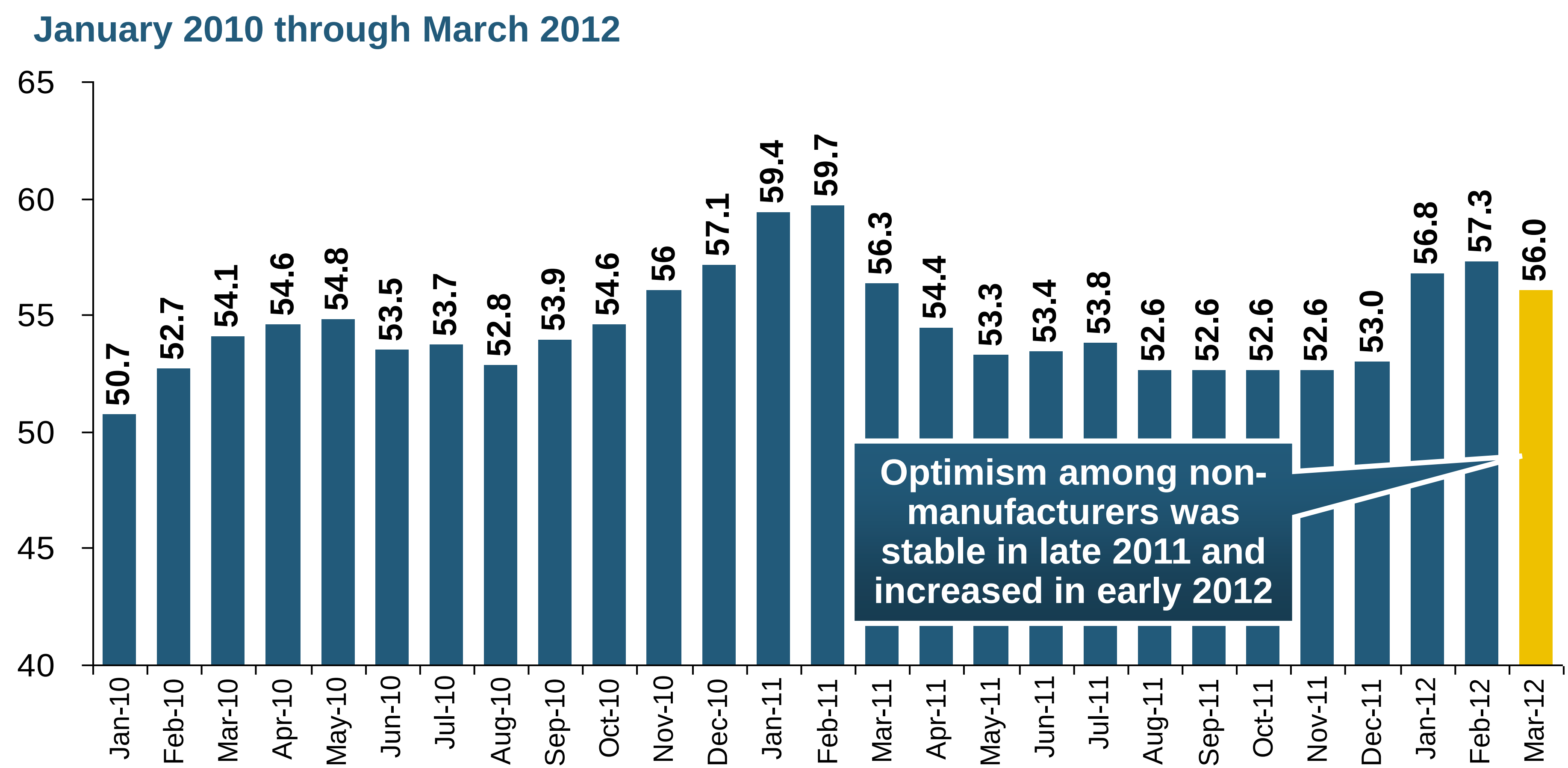


Source: IMF, World Economic Outlook, April 2012; Insurance Information Institute.

ISM Non-Manufacturing Index
(Values > 50 Indicate Expansion)



Non-manufacturing industries have been expanding and adding jobs. The question is whether this will continue.

Source: Institute for Supply Management at http://www.ism.ws/ismreport/nonmfgrob.cfm; Insurance Information Institute.

Business Bankruptcy Filings, 1980-2011

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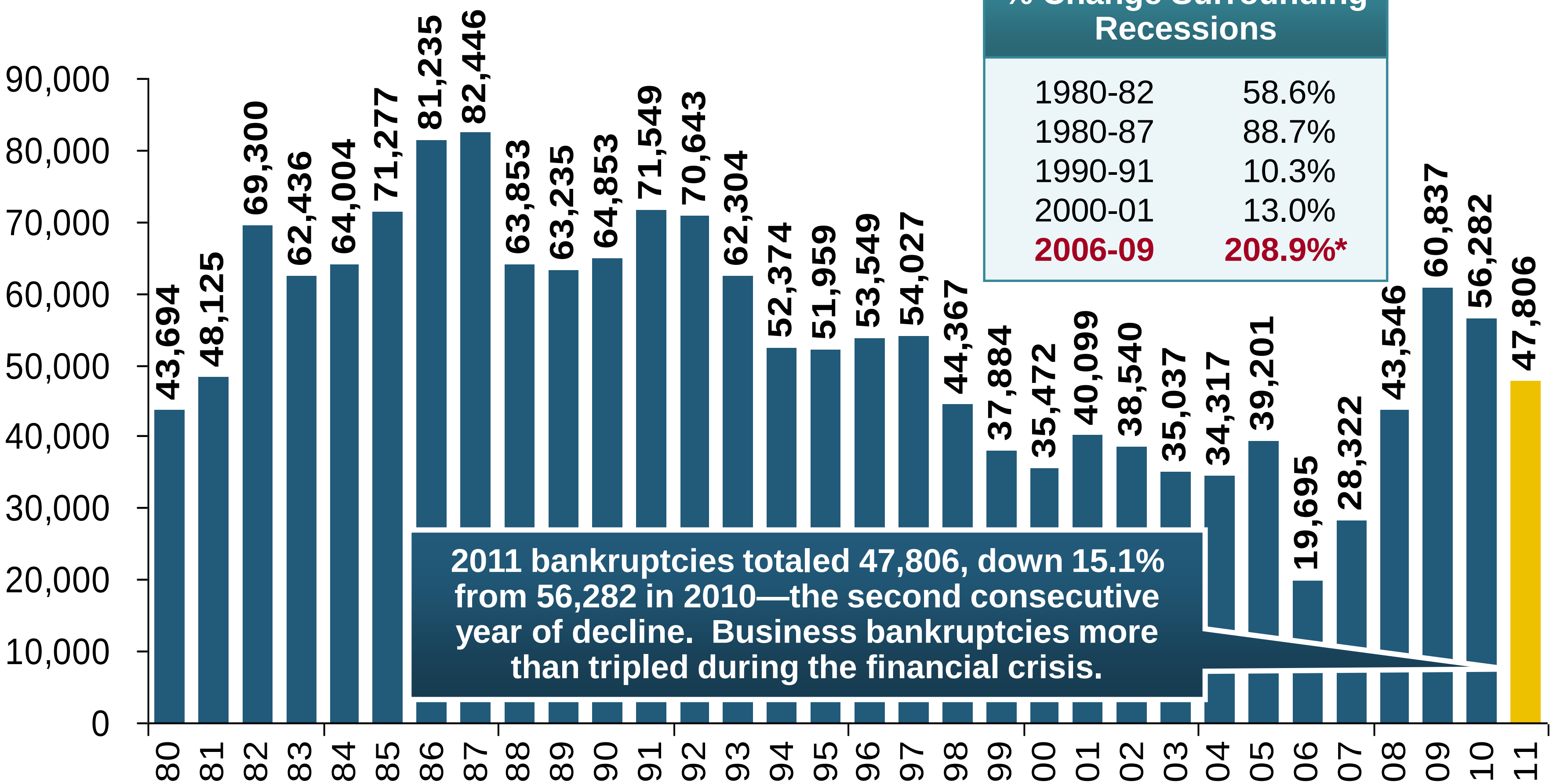

% Change Surrounding Recessions	
1980-82	58.6%
1980-87	88.7%
1990-91	10.3%
2000-01	13.0%
2006-09	**208.9%***

Significant Exposure Implications for All Commercial Lines as Business Bankruptcies Begin to Decline

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 – 2011:Q3*

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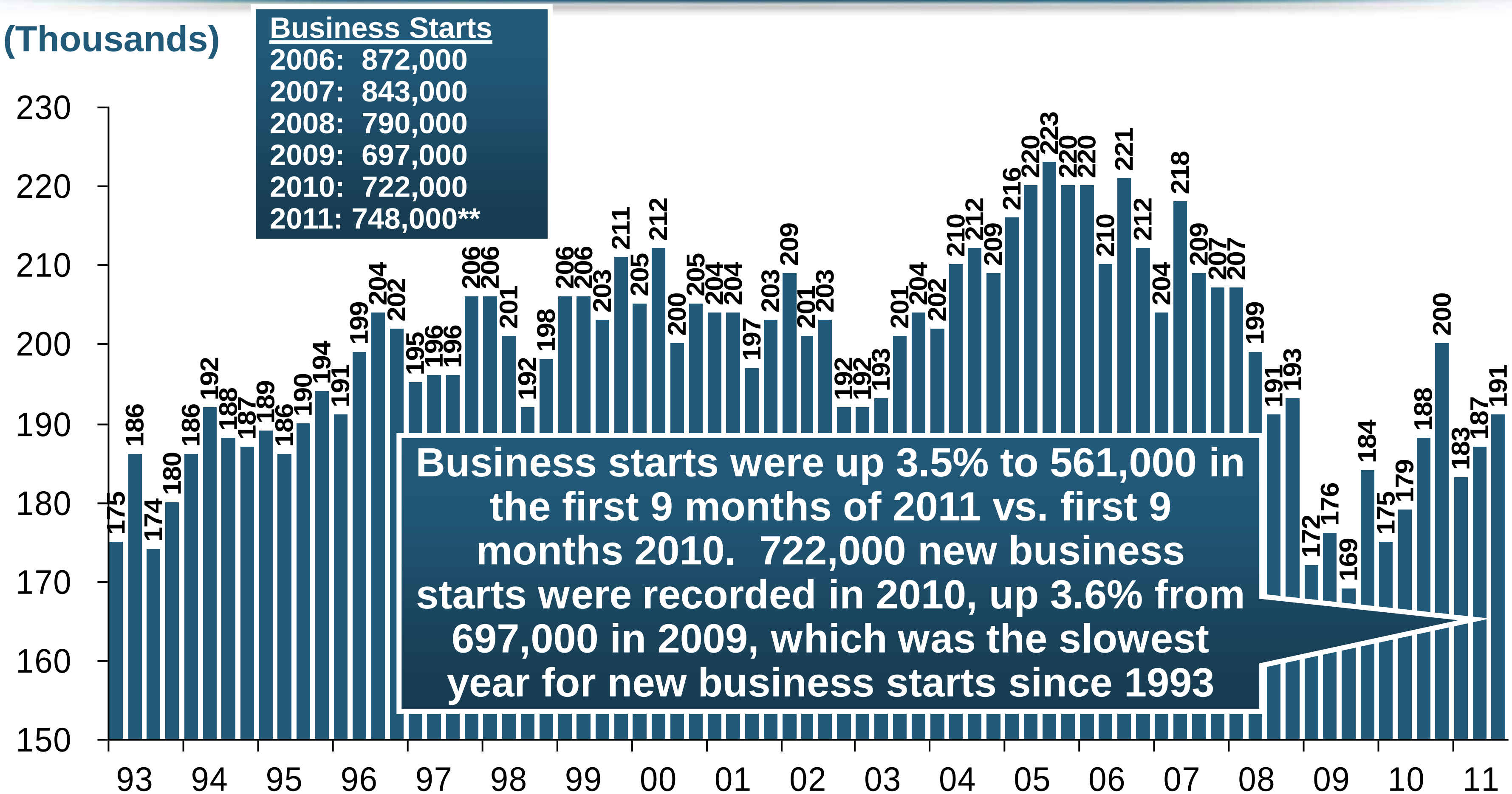

Business Starts Were Down Nearly 20% in the Recession, Holding Back Most Types of Commercial Insurance Exposure, But Are Recovering Slowly

* Data through September 30, 2011 are the latest available as of May 2, 2012; Seasonally adjusted. **Annualized based on data through 9/30.
Source: Bureau of Labor Statistics, http://www.bls.gov/news.release/cewbd.t08.htm.

12 Industries for the Next 10 Years: Insurance Solutions Needed

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

Many industries are poised for growth, though insurers' ability to capitalize on these industries varies widely

Global Oil Consumption and Price, 2008 – 2035F

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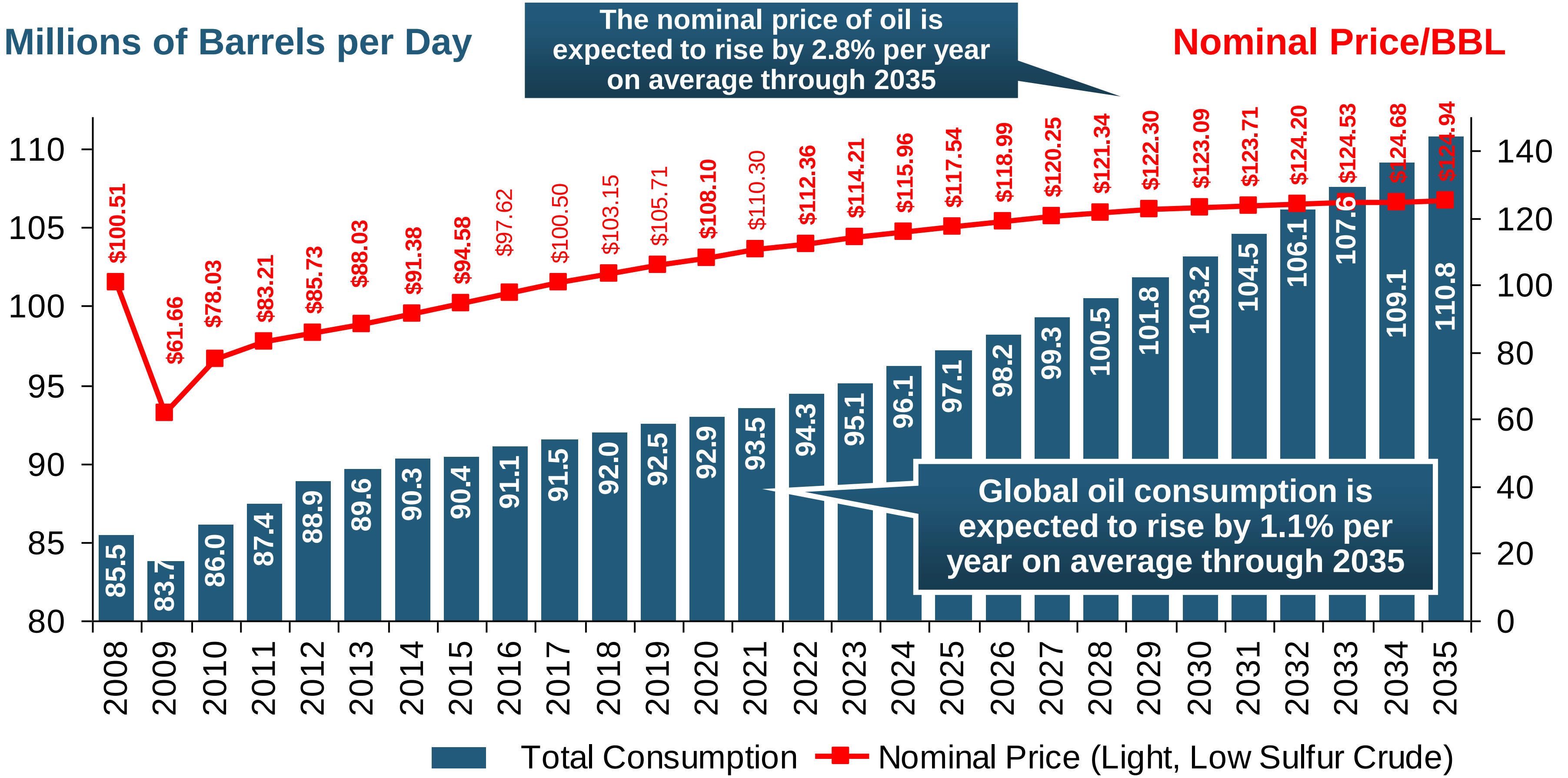

Oil Will Become Relatively More Expensive Over Time, With Price Increases Outstripping Income Growth in Many Parts of the World

*

Source: US Energy Information Administration; Insurance Information Institute

US Natural Gas Production and Non-Hydro Renewable Electricity Generation, 1990-2035P

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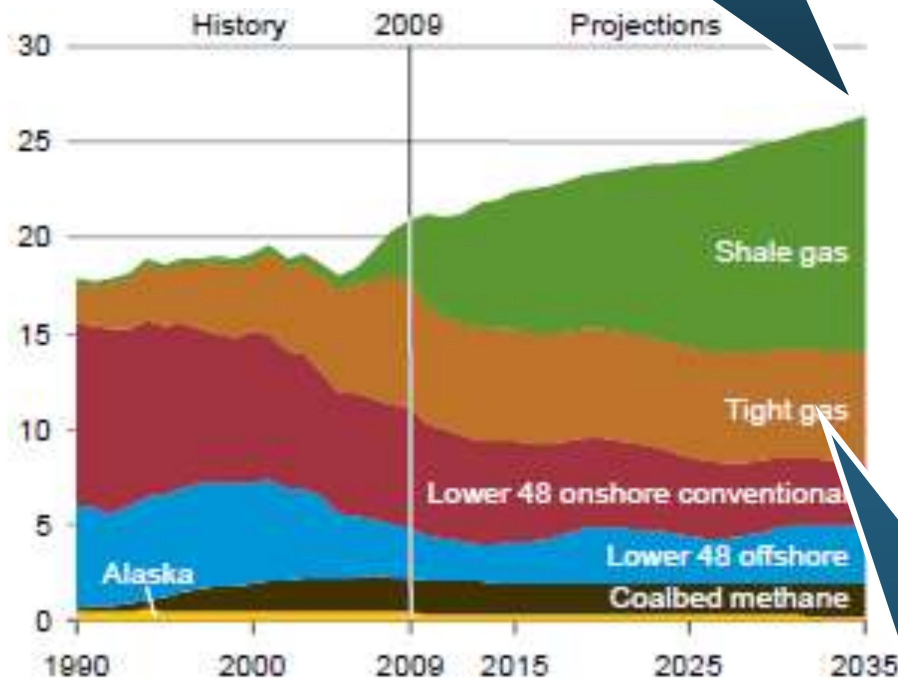
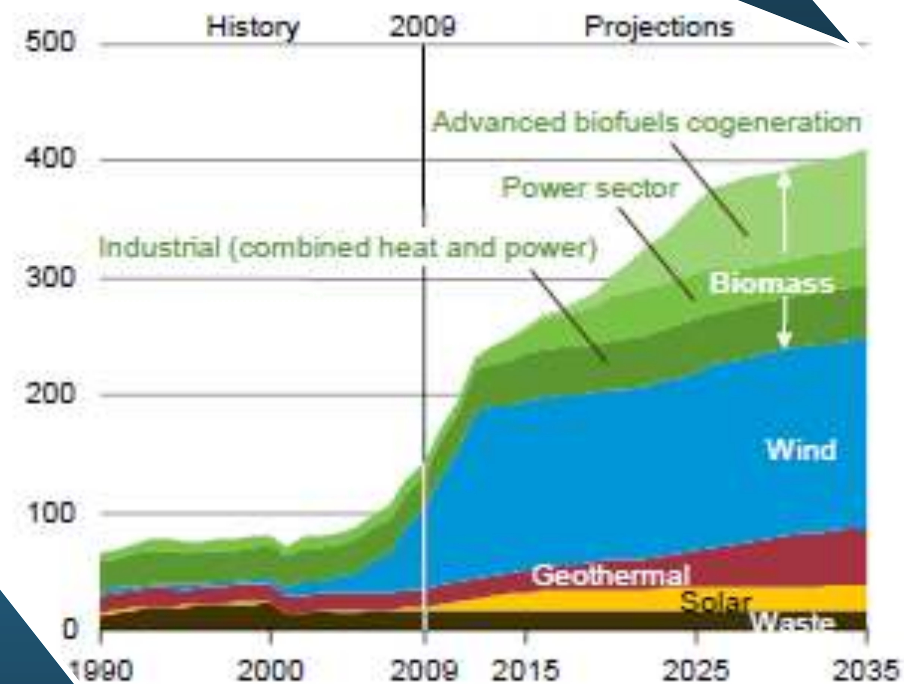
Shale gas production is expected to grow rapidly in the US

Wind is expected to account for the majority of renewable electricity generation

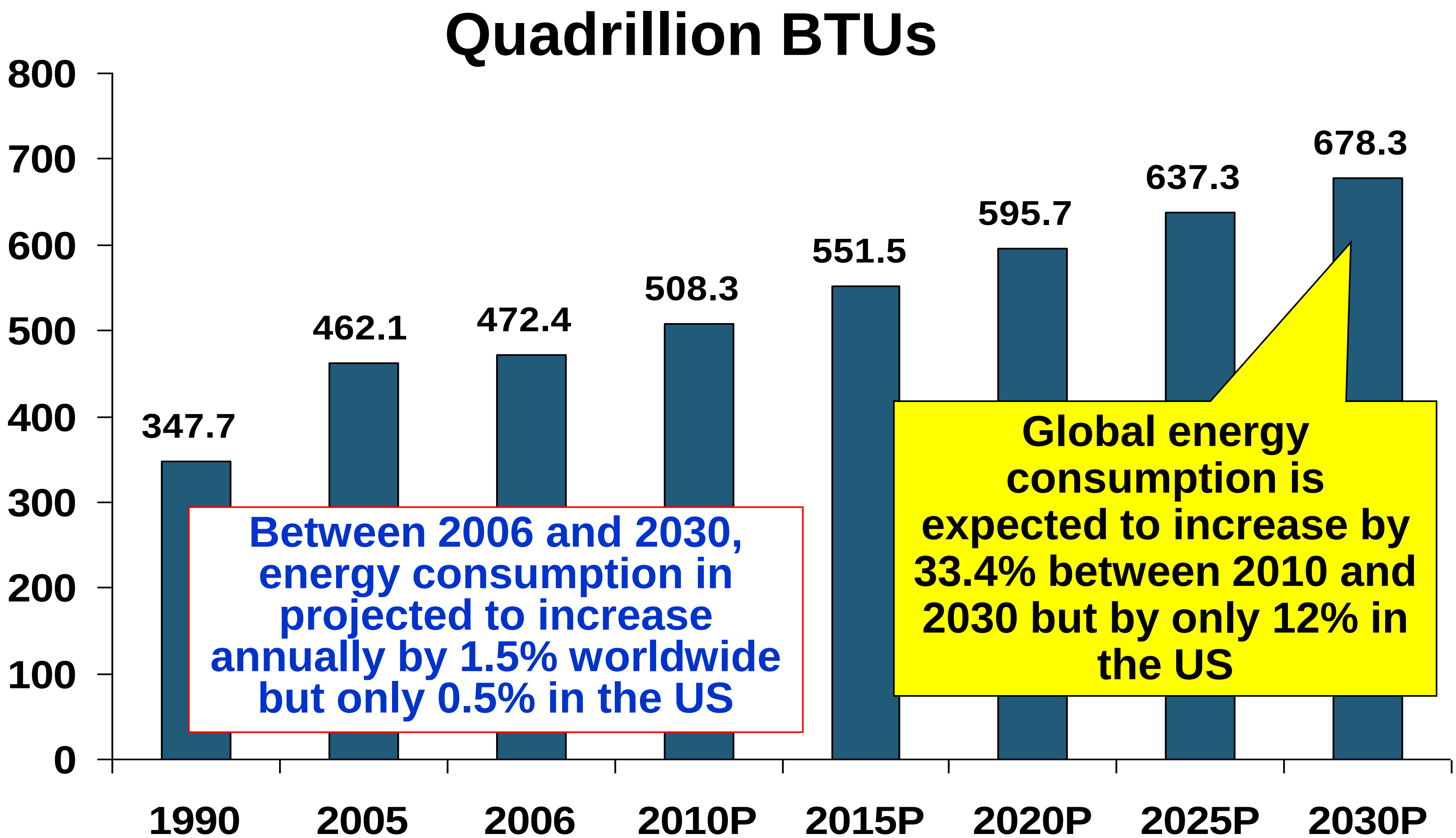




Tight gas production involves controversial hydraulic fracturing (fracking) techniques

Source: US Energy Information Administration, *Annual Energy Outlook 2011*; Insurance Information Institute.

World Primary Energy Consumption, 1990-2030P



Source: Energy Information Administration, *2009 International Energy Outlook*, Insurance Information Institute.

Presidential Politics & the P/C Insurance Industry

How Is Profitability Affected by the President's Political Party?

P/C Insurance Industry ROE by Presidential Administration, 1950- 2012*

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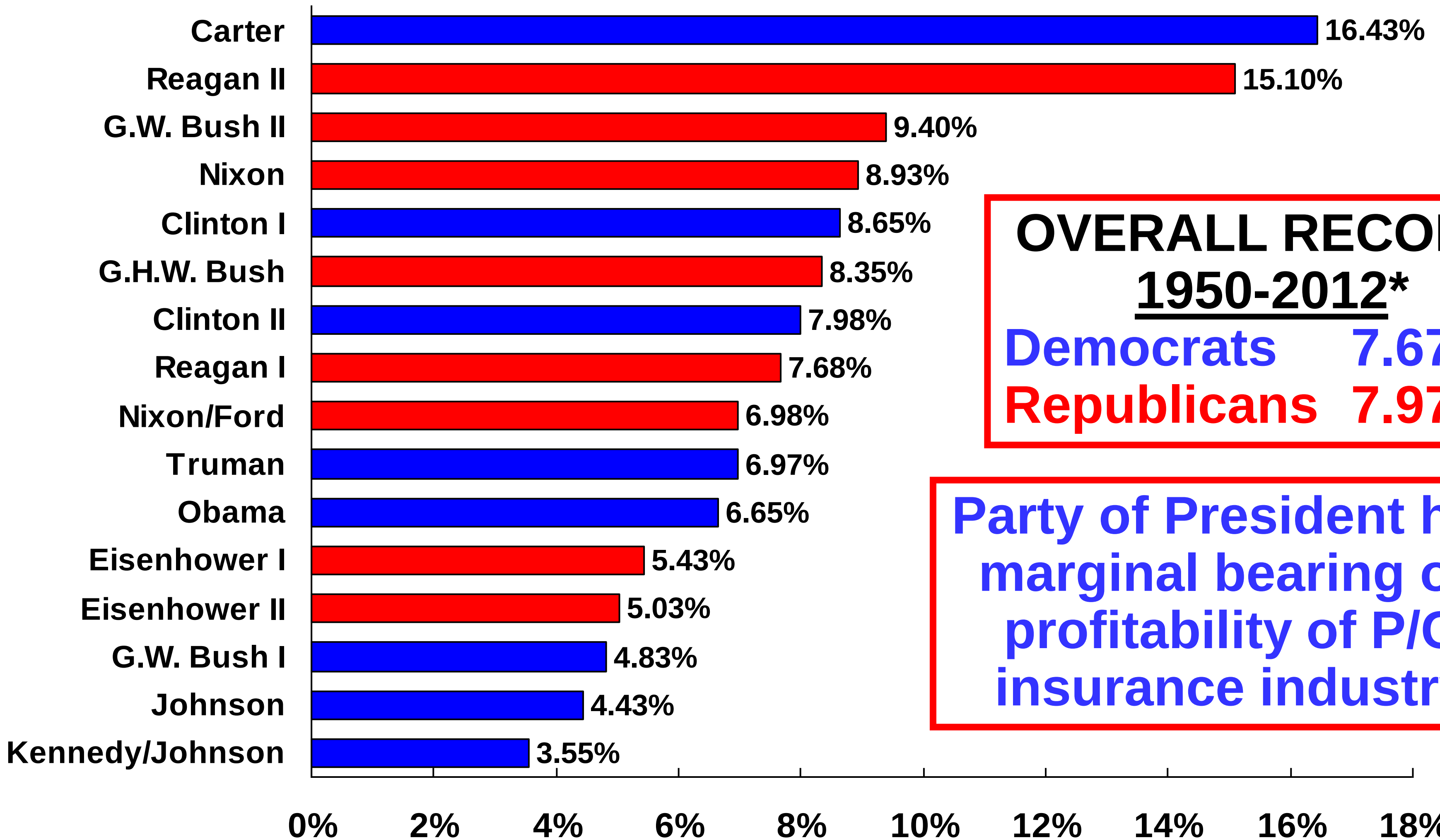


OVERALL RECORD: 1950-2012*

Democrats 7.67%

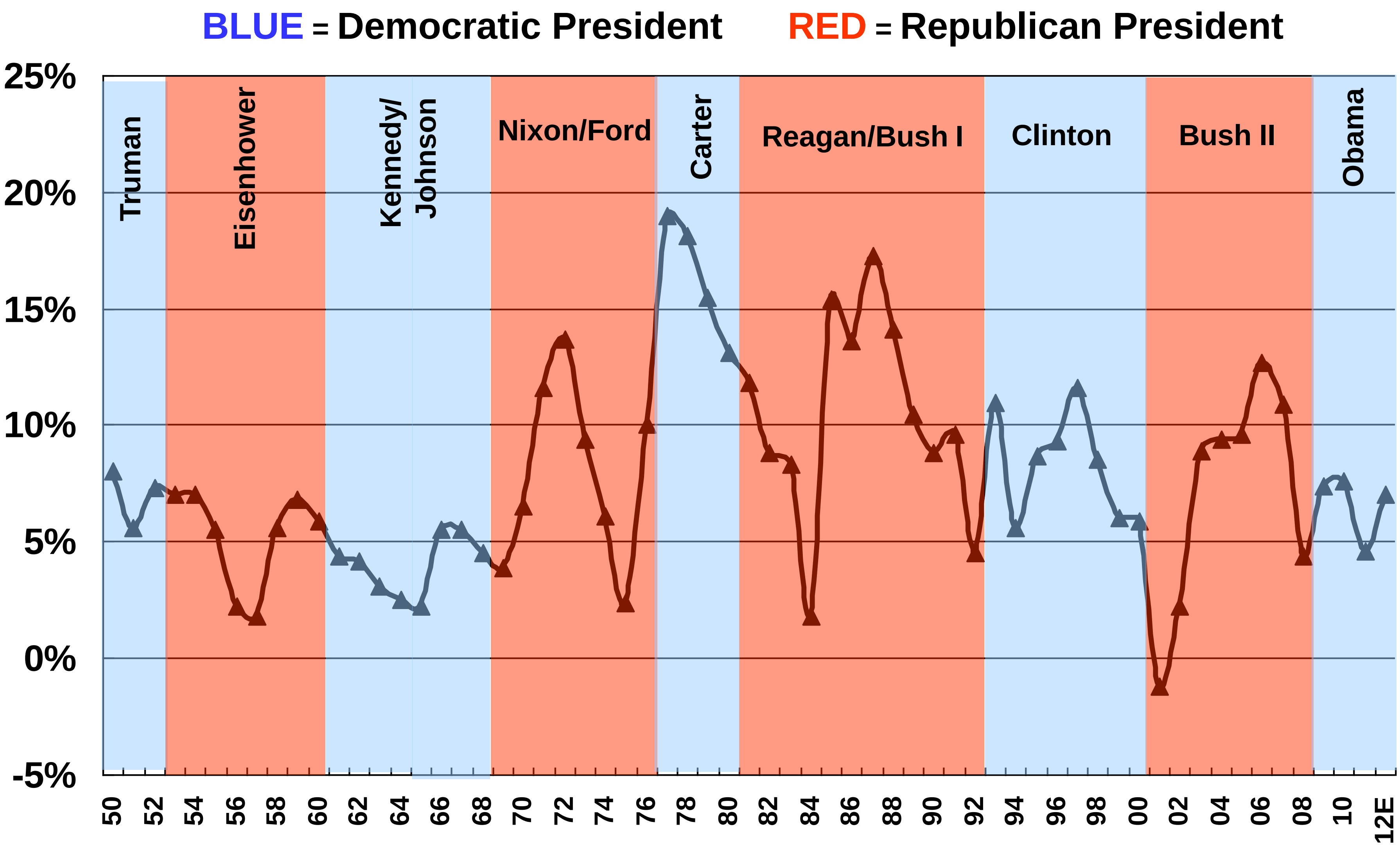
Republicans 7.97%

Party of President has marginal bearing on profitability of P/C insurance industry

*Truman administration ROE of 6.97% based on 3 years only, 1950-52; ROEs for the years 2008 forward exclude mortgage and financial guaranty segments. Estimated ROE for 2012 = 7.0%.

Source: Insurance Information Institute

P/C insurance Industry ROE by Presidential Party Affiliation, 1950- 2012*



*ROEs for the years 2008 forward exclude mortgage and financial guaranty segments; Estimated 2012 ROE = 7.0%

Source: Insurance Information Institute

Election 2012: Political Issues Impacting Insurers

- **Presidential Race Is Tight**
- **Potential for Senate to Flip Republican**
- **Affordable Care Act/Health Care Reform (ObamaCare)**
  - Romney, Republicans generally vow to repeal the Act
  - Complete repeal is unlikely as several popular ACA provisions are already implemented
  - Supreme Court will rule on the constitutionality of the Act in June; Outcome uncertain
- **Dodd-Frank Act/Financial Services Reform & Implementation**
  - Republicans refer to DFA as a “confidence killer” and want it scaled back
  - Outright repeal is highly unlike irrespective of election outcome
  - Systemic criteria have been developed; Designations in late 2012
  - Financial Stability Oversight Council: Current/future composition impacted by election
  - Changes to DFA and/or implementation will have little impact on P/C insurers
- **Key Committee Shifts Possible**
  - **Senate Banking Chair:** Tim Johnson (D-SD) → Richard Shelby (R-AL)
  - **House Finl. Svcs. Chair:** Spencer Bachus (R-AL) → Jeb Hensarling (R-TX) (term limits)
    - If House flipped Chair would go to Maxine Waters (D-CA)
- **Federal Insurance Office**
  - If Romney wins, he will appoint a new Treasury Secretary
  - FIO leadership, agenda and funding could be impacted
  - Secretary Geithner likely to step down after election even if Obama is re-elected
- **Agent Licensing, NFIP**

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The Unfortunate Nexus: Opportunity, Risk & Instability

Most of the Global Economy's Future Gains Will be Fraught with Much Greater Risk and Uncertainty than in the Past

Global Real (Inflation Adjusted) Nonlife Premium Growth: 1980-2010

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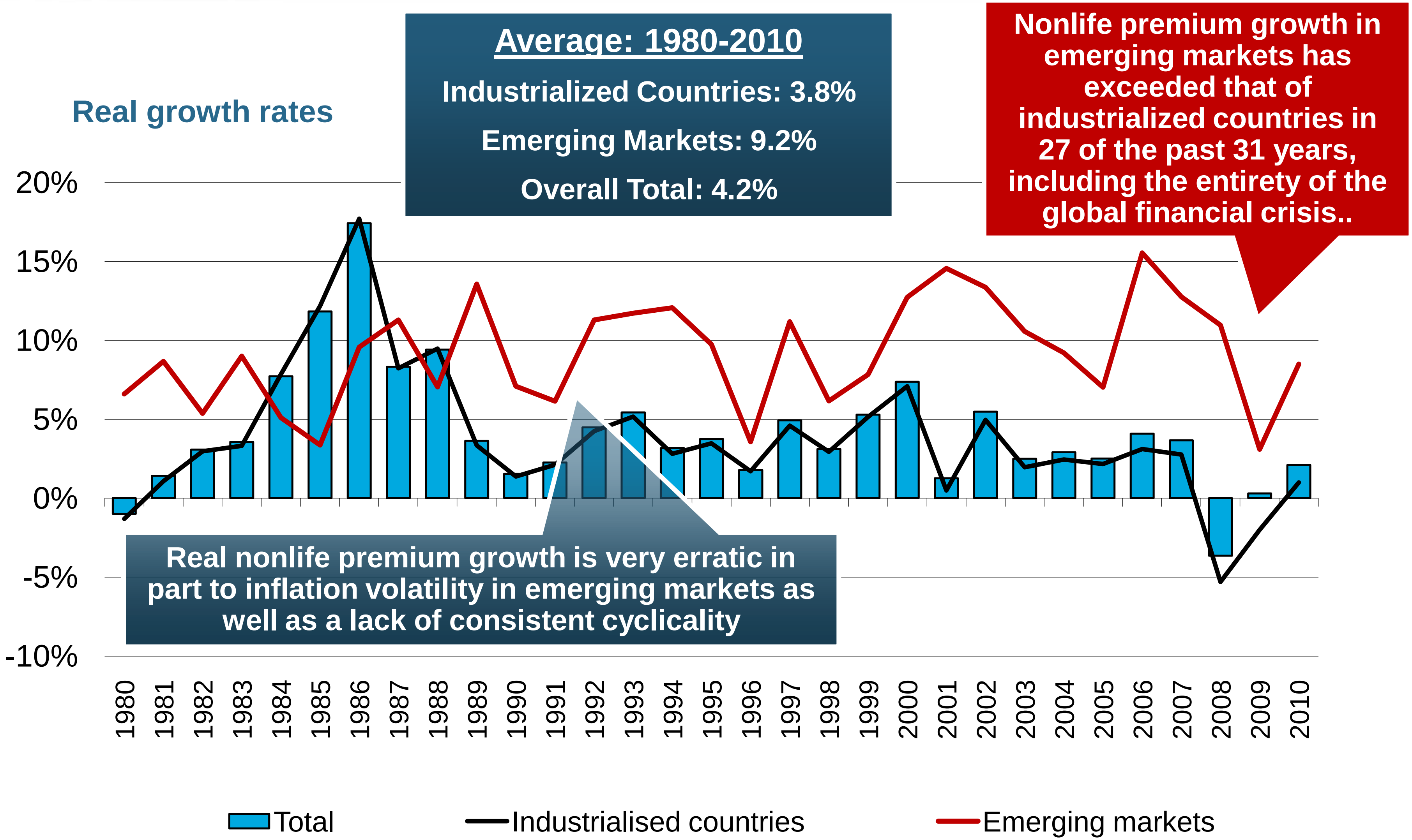
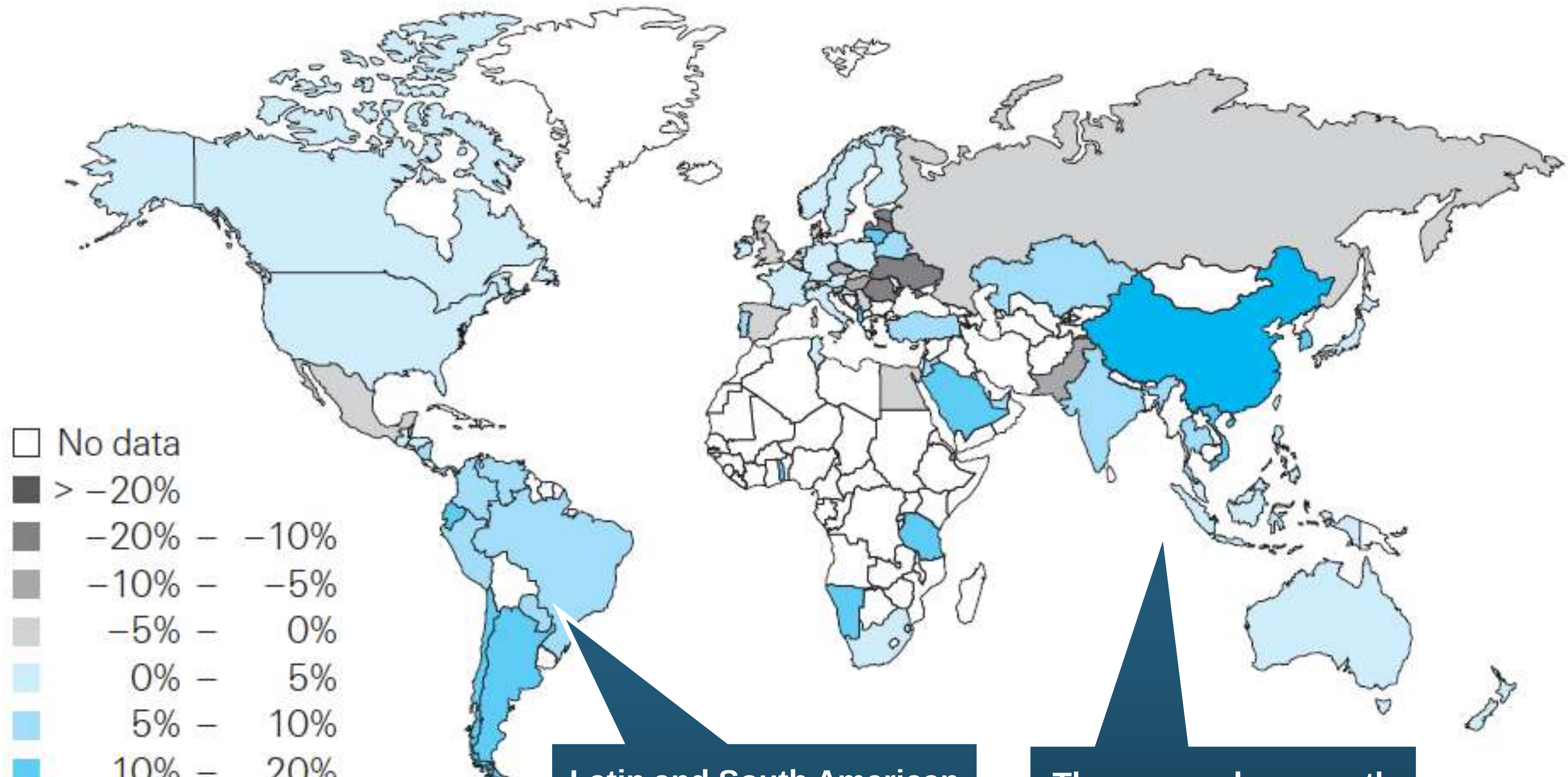


Source: Swiss Re, *sigma*, No. 2/2010.

Nonlife Real Premium Growth in 2010

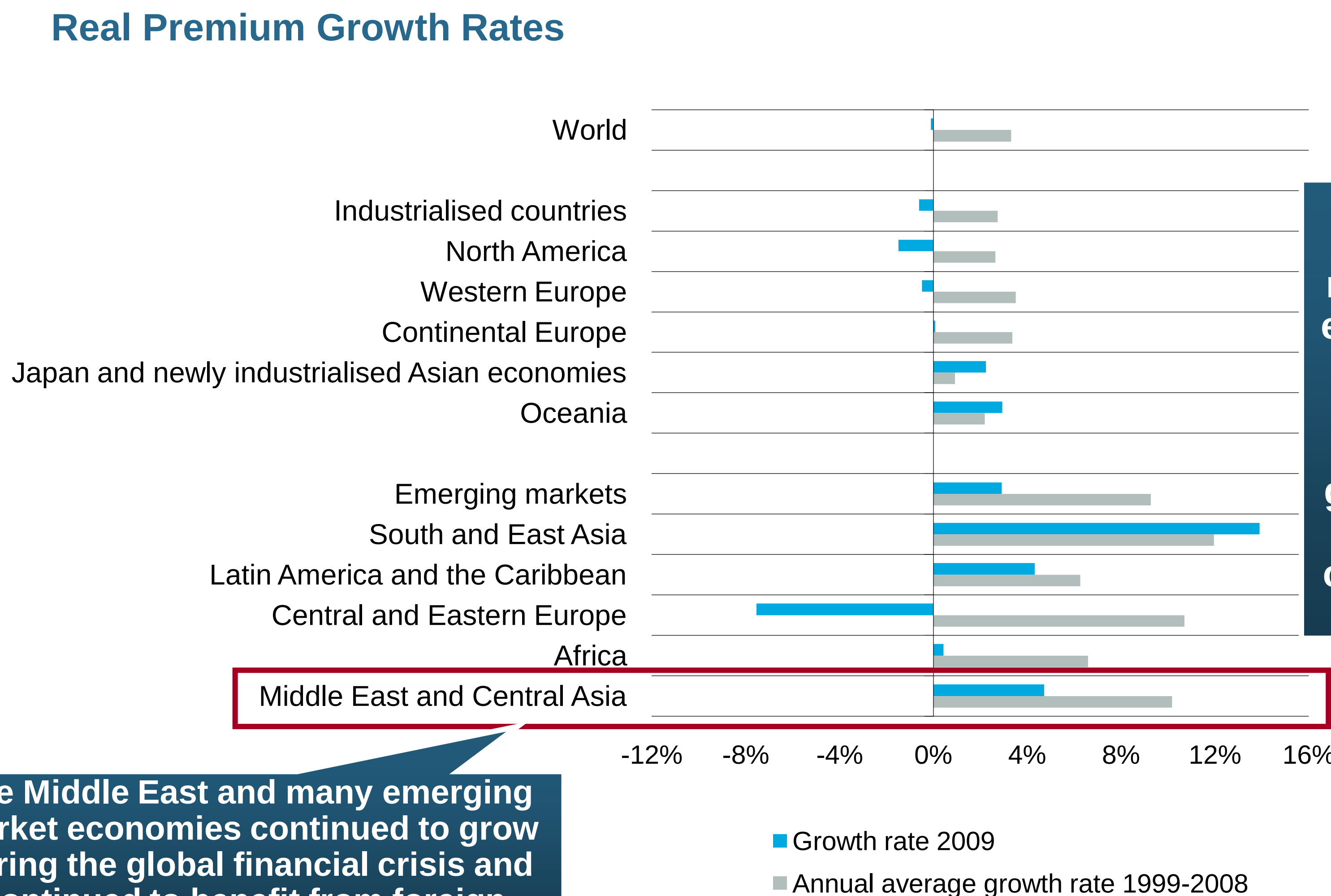


Latin and South American markets performed relatively well during and after the global financial crisis in terms of growth

There was also growth in the Middle East, East and South Asia as well as Australia and New Zealand

Source: Swiss Re, *sigma*, No. 2/2011.

Nonlife Real Premium Growth Rates by Region: 2000-2009 and 2010



Every emerging market region except Central and Eastern Europe experienced growth during the financial crisis and into 2010

The Middle East and many emerging market economies continued to grow during the global financial crisis and continued to benefit from foreign direct investment

Source: Swiss Re, *sigma*, No. 2/2011.

Distribution of Nonlife Premium: Industrialized vs. Emerging Markets, 2009

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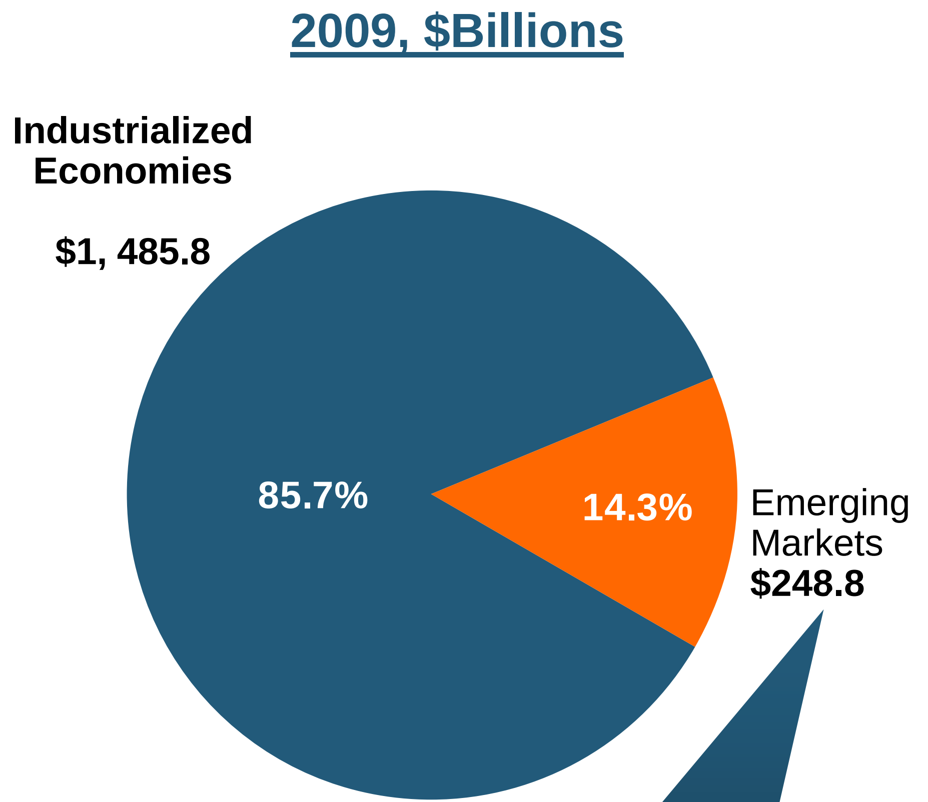
Premium Growth Facts

- Although premium growth throughout the industrialized world was negative in 2009, its share of global nonlife premiums remained very high at nearly 86%--accounting for nearly $1.5 trillion in premiums.
- The financial crisis and sluggish recovery in the major insurance markets will accelerate the expansion of the emerging market sector



Developing markets now account for 47% of global GDP but just 14% of nonlife premiums

Sources: Swiss Re; Insurance Information Institute research.

Political Risk in 2011/12: Greatest Business Opportunities Are Often in Risky Nations

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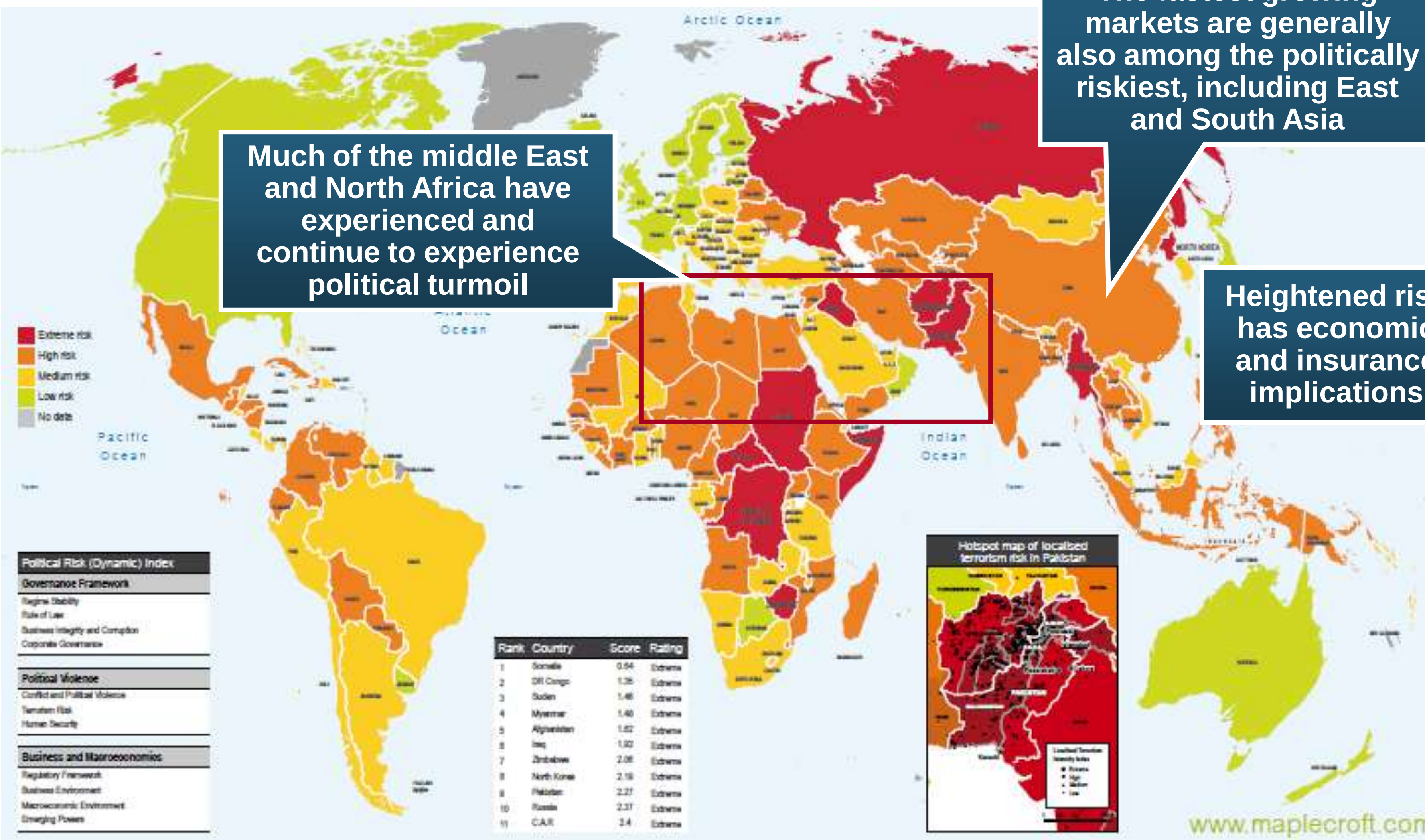

Much of the middle East and North Africa have experienced and continue to experience political turmoil

The fastest growing markets are generally also among the politically riskiest, including East and South Asia

Heightened risk has economic and insurance implications

Source: Maplecroft

The "Arab Spring" Has Increased Uncertainty in an Already Volatile Part of the World

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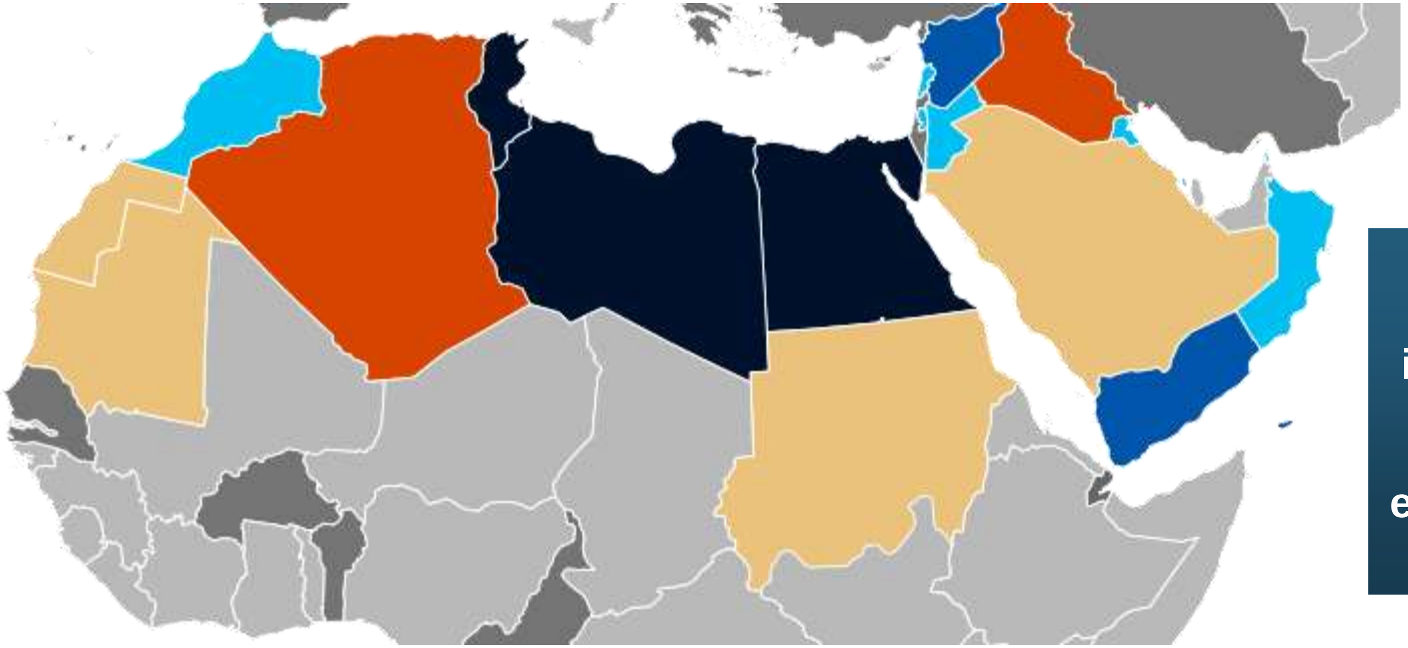
Some energy-rich nations have been among the most unstable in 2011/12

Arab Spring
الربيع العربي



■ Government overthrown ■ Sustained civil disorder and governmental changes
■ Protests and governmental changes ■ Major protests ■ Minor protests
■ Protests outside the Arab world

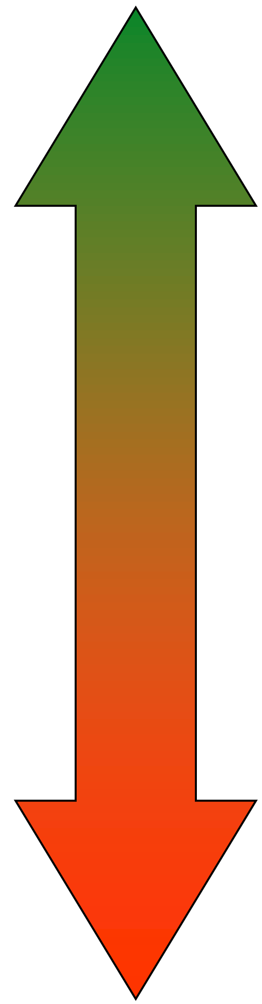
Longer-run, significant investment and insurance opportunities exist throughout the region

Source: Wikipedia as of Nov. 7, 2011; Insurance Information Institute research.

Country Risk

The risk that country-specific factors could adversely affect an insurer's ability to pay its financial obligations

Economic Risk		Macroeconomy
		Prospects
		Government Finance
Political Risk		Business Environment
		Government Stability
		Social Stability
		Legal System
Financial System Risk	Non-Insurance	Banking System
		Reporting Standards & Regulation
		Sovereign Debt
		Government & Legislation
	Insurance	Supervisory Authority
		Insurer Accountability



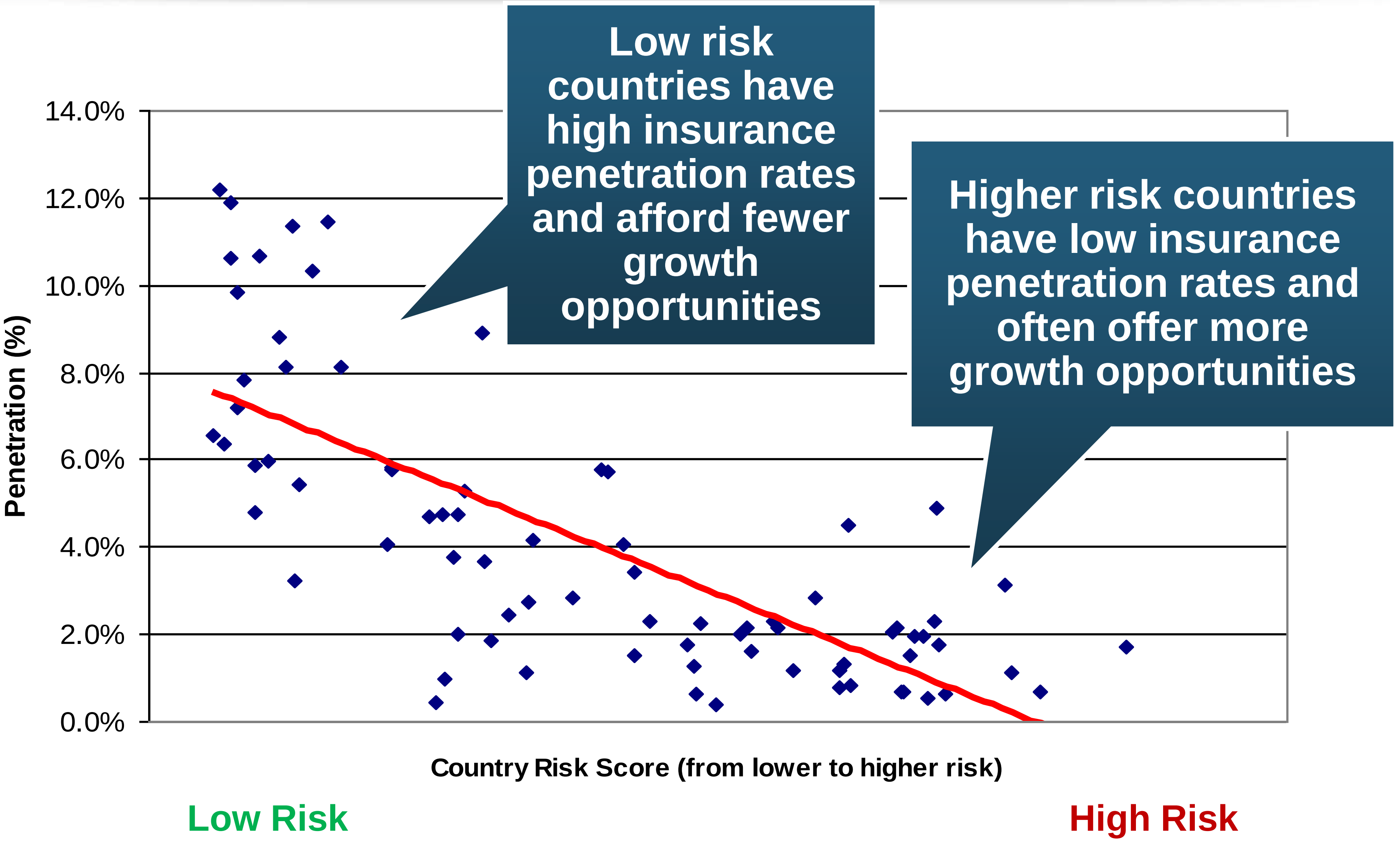
CRT-1
Lowest Risk

CRT-3
Moderate Risk

CRT-5
Highest Risk

Source: A.M. Best.

Country Risk Relates to Insurance Market Development



Source: A.M. Best.

GDP Per Capita Drives Insurance Market Penetration

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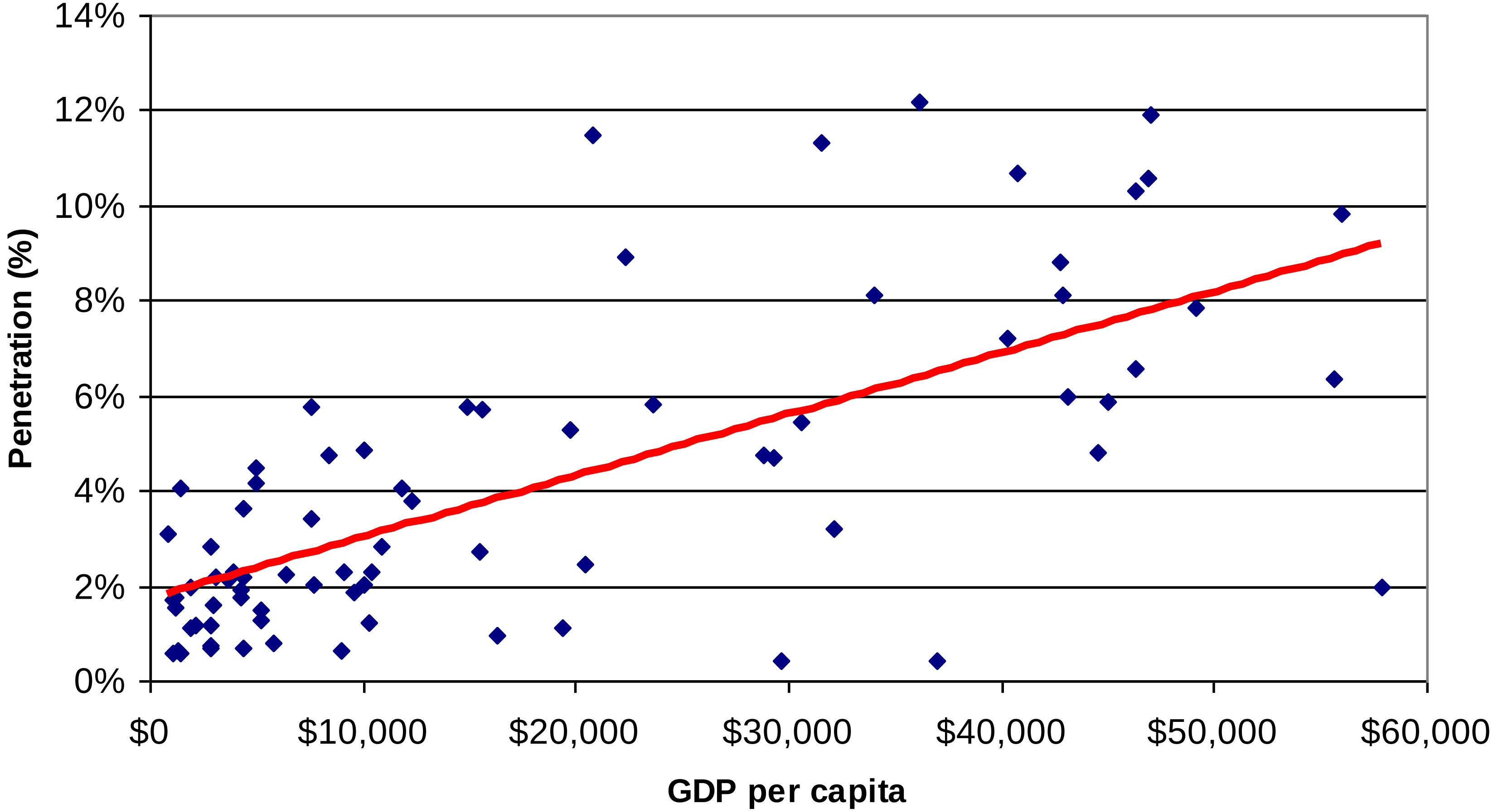

Source: A.M. Best.

Summary of 10 Greatest Potential Threats to Global Economy as of May 2012

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1. **Armed Conflict in the Middle East, Disrupting Oil Markets**
   - $200/bbl oil is possible; Severe supply disruptions
   - Result→serious damage to the global economy, killing fragile recovery
2. **Rising Oil Prices**
   - Even in the absence of armed conflict, oil prices slowing growth
   - Sustained $10/bbl increase → -0.2% on global GDP in Year 1; -0.5% Year 2
3. **Sovereign Debt Concerns in Europe (was #1 threat in 2011)**
   - Contagion spreads beyond Greece→Spain, Italy, Portugal, etc.
   - EU political/economic solution fails resulting in disorderly default
   - Sharp drift to the left in Europe & lose of resolve to address Eurozone problems
4. **"Hard Landing" of Chinese Economy**
   - A sharp decline in China's GDP would damage global economies
5. **Mega-Catastrophe Trends Continue at Record Pace**
   - Catastrophes trimmed 0.5% off global GDP in 2011
   - Massive disruptions to fragile global supply chains
6. **Sudden Weakening of US Economy**
7. **Intensification of Geopolitical Instability (esp. Middle & Far East)**
8. **Disintegration of Eurozone *(Political Failure)***
9. **Commodity Price Inflation (apart from oil)**
10. **Large-Scale Cyber Attack/Terrorism Attack (including cyberterror)**

Global Catastrophe Loss Developments and Trends

2011 Rewrote Catastrophe Loss and Insurance History

But Will Losses Turn the Market?

Global Catastrophe Loss Summary: 2011

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- **2011 Was the *Highest* Loss Year on Record for Economic Losses Globally**
  - Extraordinary accumulation of severe natural catastrophe: Earthquakes, tsunami, floods and tornadoes are the primary causes of loss
- **$380 Billion in *Economic* Losses Globally (New Record)**
  - New record, exceeding the previous record of $270B in 2005
- **$105 Billion in *Insured* Losses Globally**
  - 2011 losses were 2.5 times 2010 insured losses of $42B
  - Second only to 2005 on an inflation adjusted basis (new record on a unadjusted basis)
  - Over 5 times the 30-year average of $19B
- **$72.8 Billion in *Economic* Losses in the US**
  - Represents a 129% increase over the $11.8 billion amount through the first half of 2010
- **$35.9 Billion in *Insured* Losses in the US Arising from 171 CAT Events**
  - Fifth highest year on record
  - Represents 51% increase over the $23.8 billion total in 2010

Source: Munich Re; Insurance Information Institute.

Natural Loss Events, 2011

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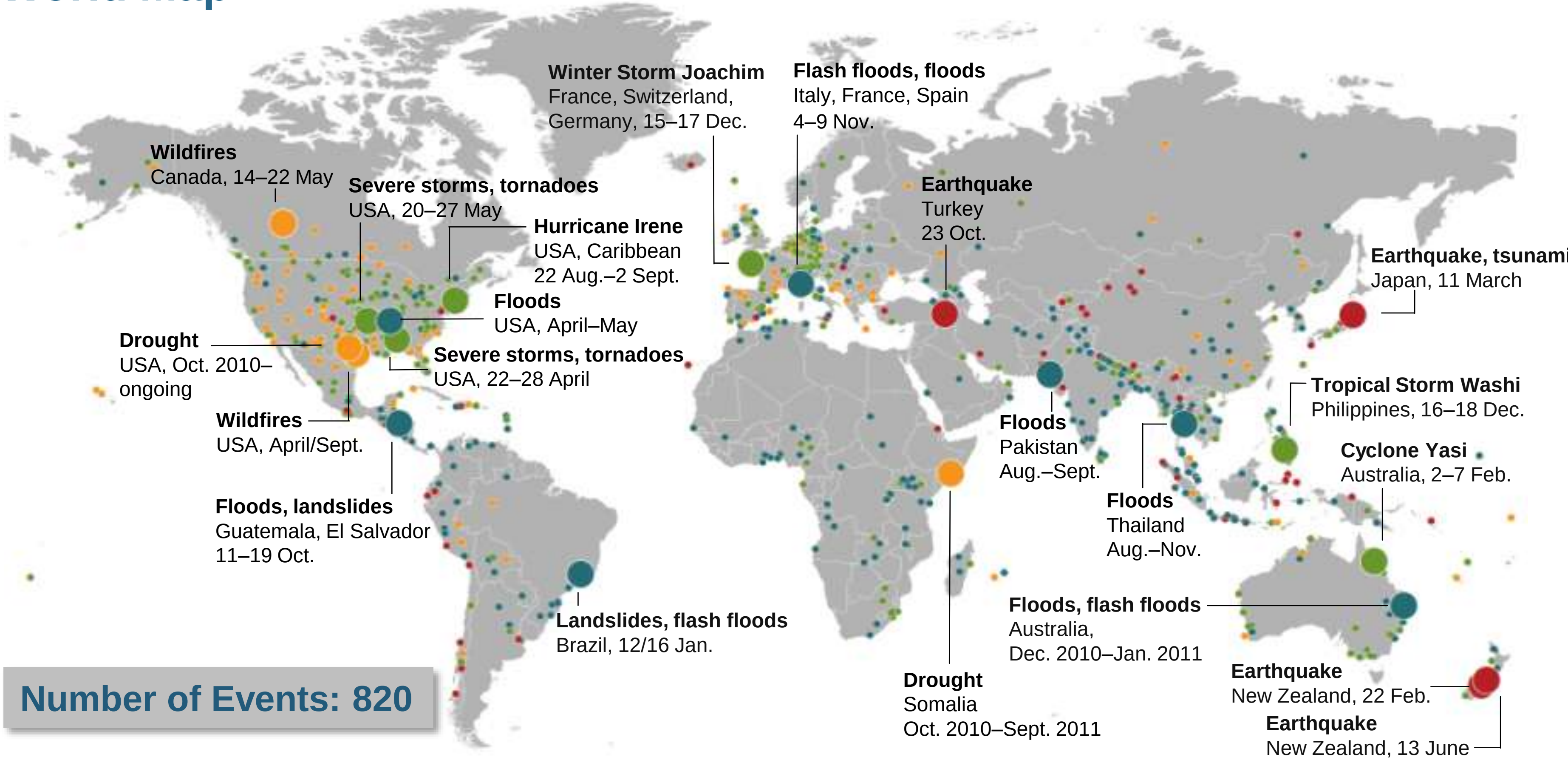
World Map



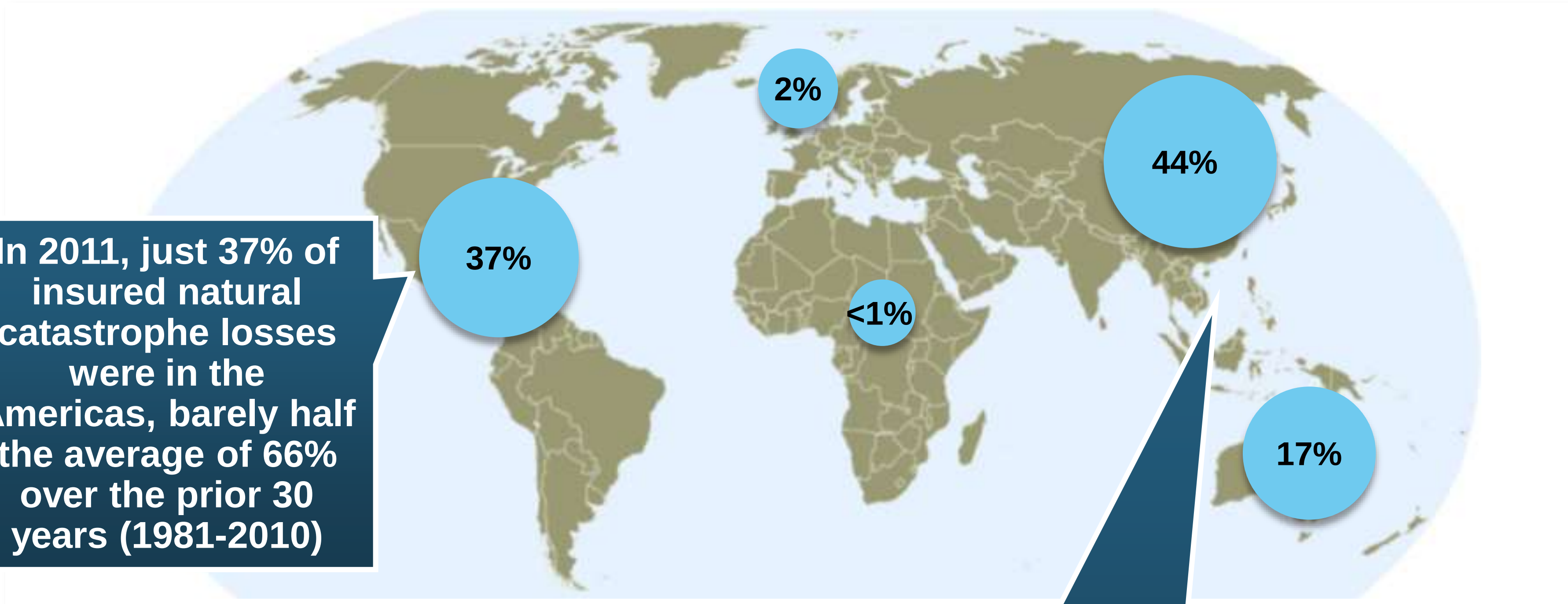
Number of Events: 820

Natural catastrophes	**Geophysical events** (earthquake, tsunami, volcanic activity)	**Hydrological events** (flood, mass movement)
Selection of significant loss events (see table)	**Meteorological events** (storm)	**Climatological events** (extreme temperature, drought, wildfire)

Source: MR NatCat*SERVICE*

Natural Catastrophes Worldwide 2011

Insured losses US$ 105bn - Percentage distribution per continent



In 2011, just 37% of insured natural catastrophe losses were in the Americas, barely half the average of 66% over the prior 30 years (1981-2010)

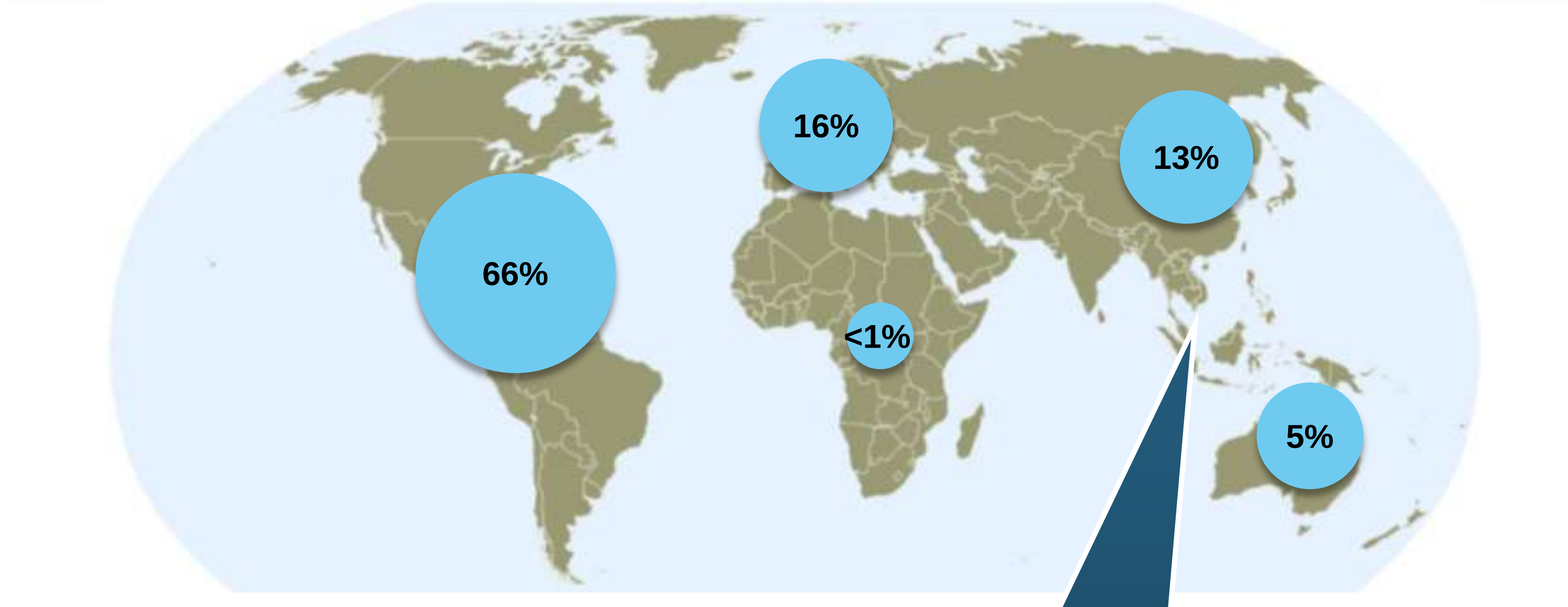
Continent	Insured losses US$ m
America (North and South America)	40,000
Europe	2,000
Africa	Minor damages
Asia	45,000
Australia/Oceania	18,000

In 2011, 61% of insured natural catastrophe losses were in the Asia/Pacific region, nearly 3.5 times the average of 13% over the prior 30 years (1981-2010)

Source: MR NatCat*SERVICE*

Natural Catastrophes Worldwide 1980 – 2011

Insured losses US$ 870bn - Percentage distribution per continent



Continent	Insured losses US$ m
America (North and South America)	566,000
Europe	146,000
Africa	2,000
Asia	115,000
Australia/Oceania	41,000

In 2011, 61% of natural catastrophe losses were in the Asia/Pacific region, nearly 3.5 times the average of 13% over the prior 30 years (1981-2010)

Source: MR NatCat*SERVICE*

Worldwide Natural Disasters 1980–2011, Overall and Insured Losses

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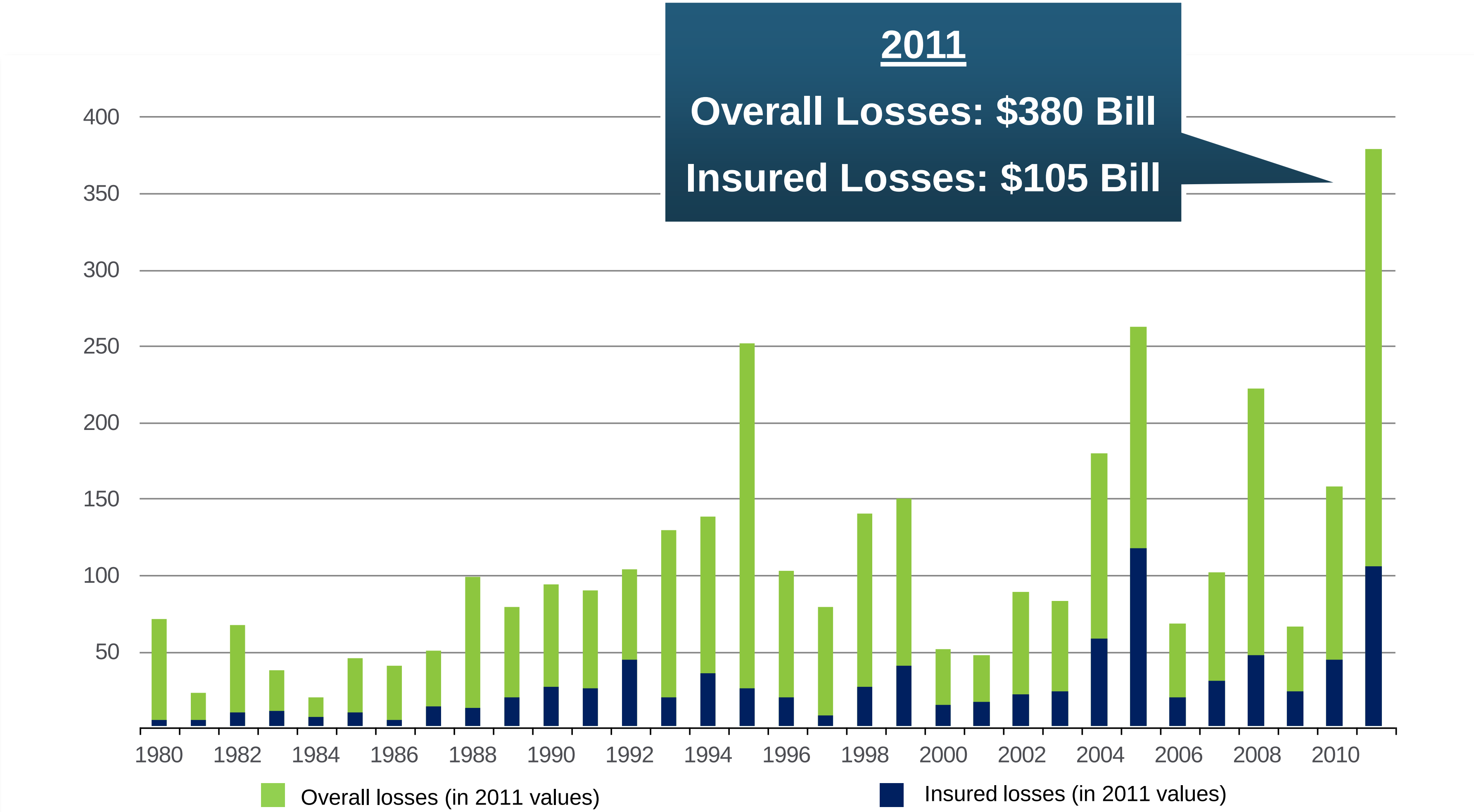
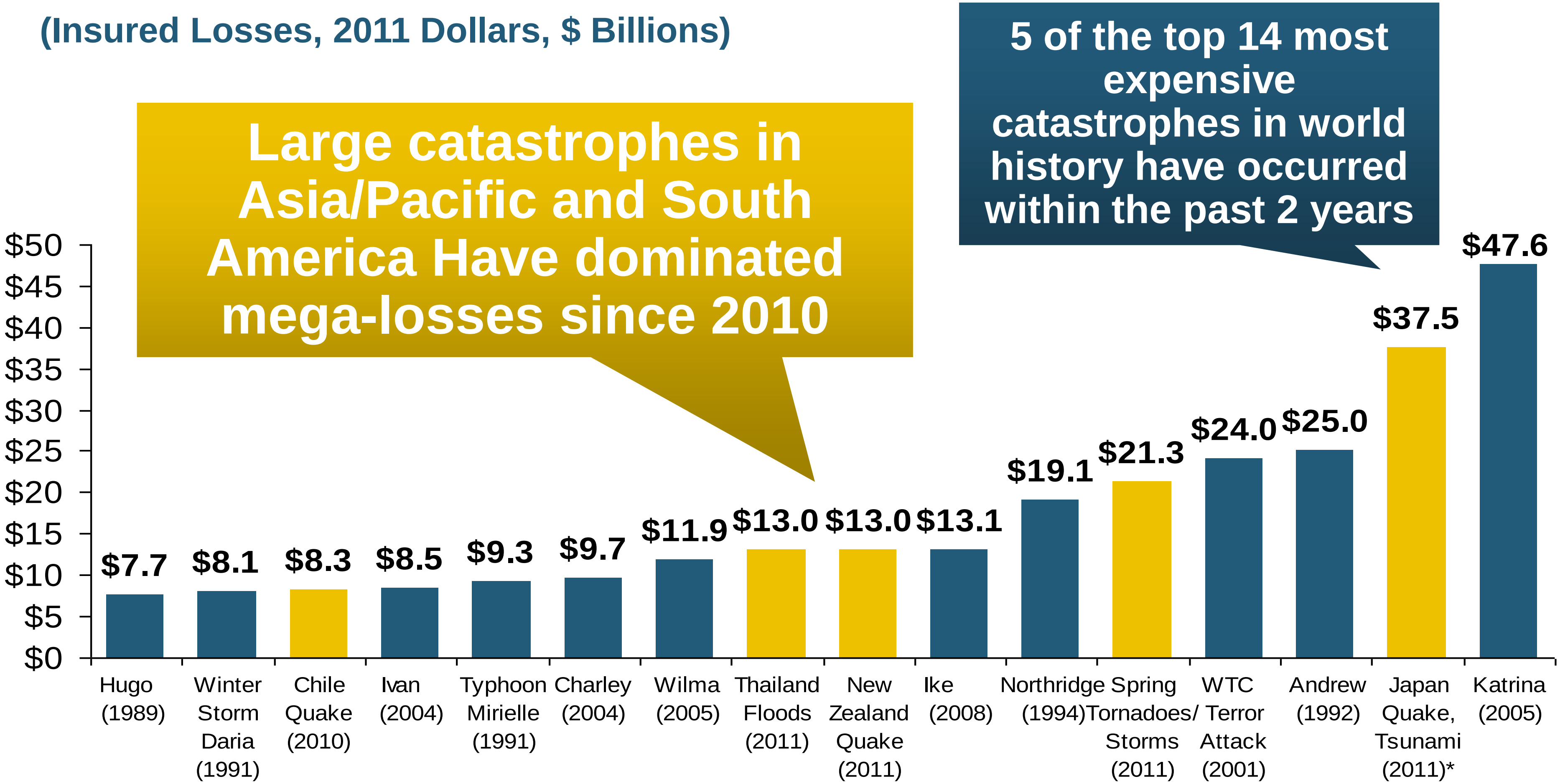
(Insured Losses, 2011 Dollars, $ Billions)



Source: MR NatCat*SERVICE*

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

(Insured Losses, 2011 Dollars, $ Billions)

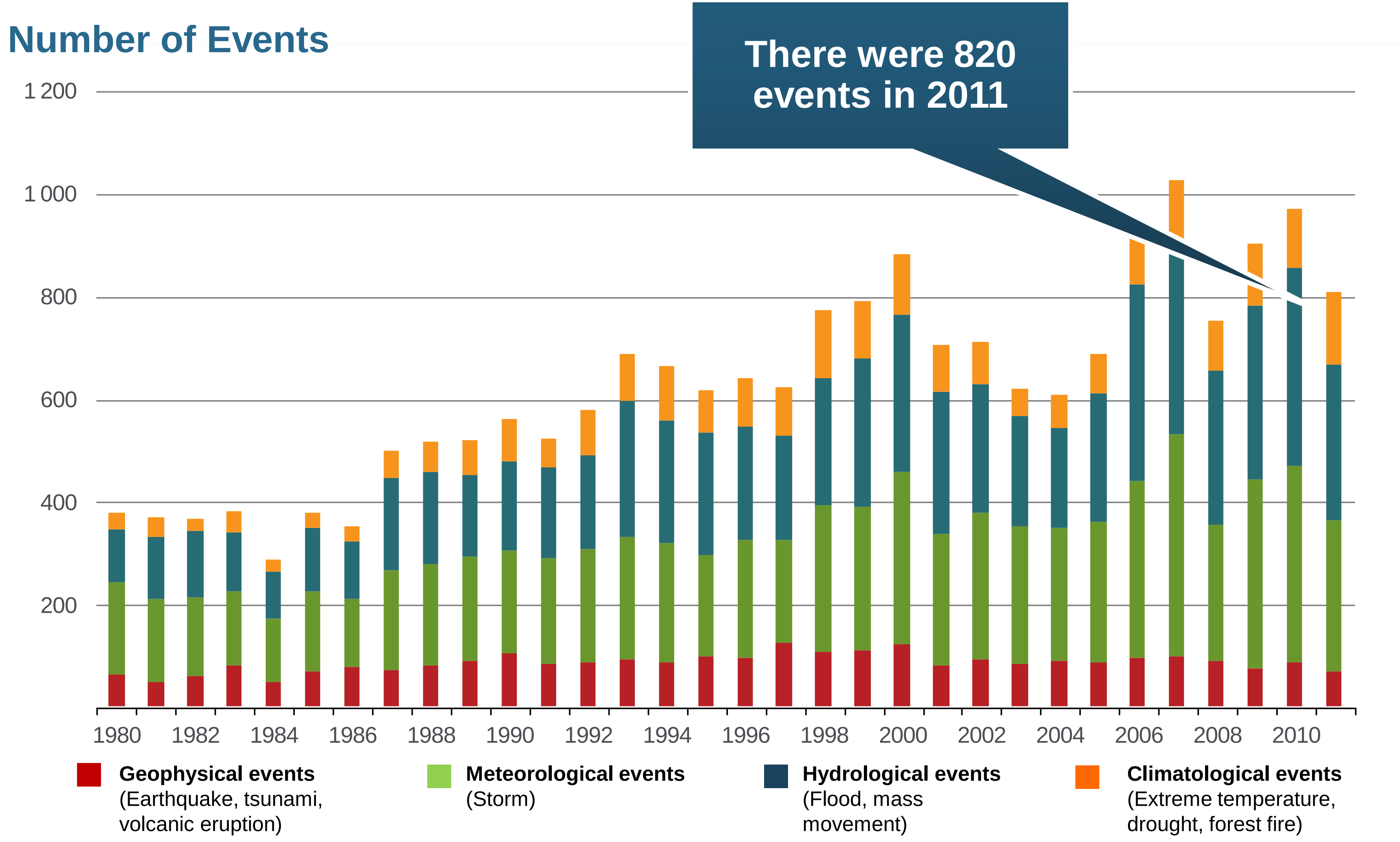


*Average of range estimates of $35B - $40B as of 1/4/12; Privately insured losses only.

**Figures do not include federally insured flood losses.

Sources: Swiss Re *sigma 1/2011*; Munich Re; Insurance Information Institute research.

Worldwide Natural Disasters, 1980 – 2011



Source: MR NatCat*SERVICE*

Natural Catastrophes in Asia 1980 – 2011

Overall and insured losses in 2011 Dollars

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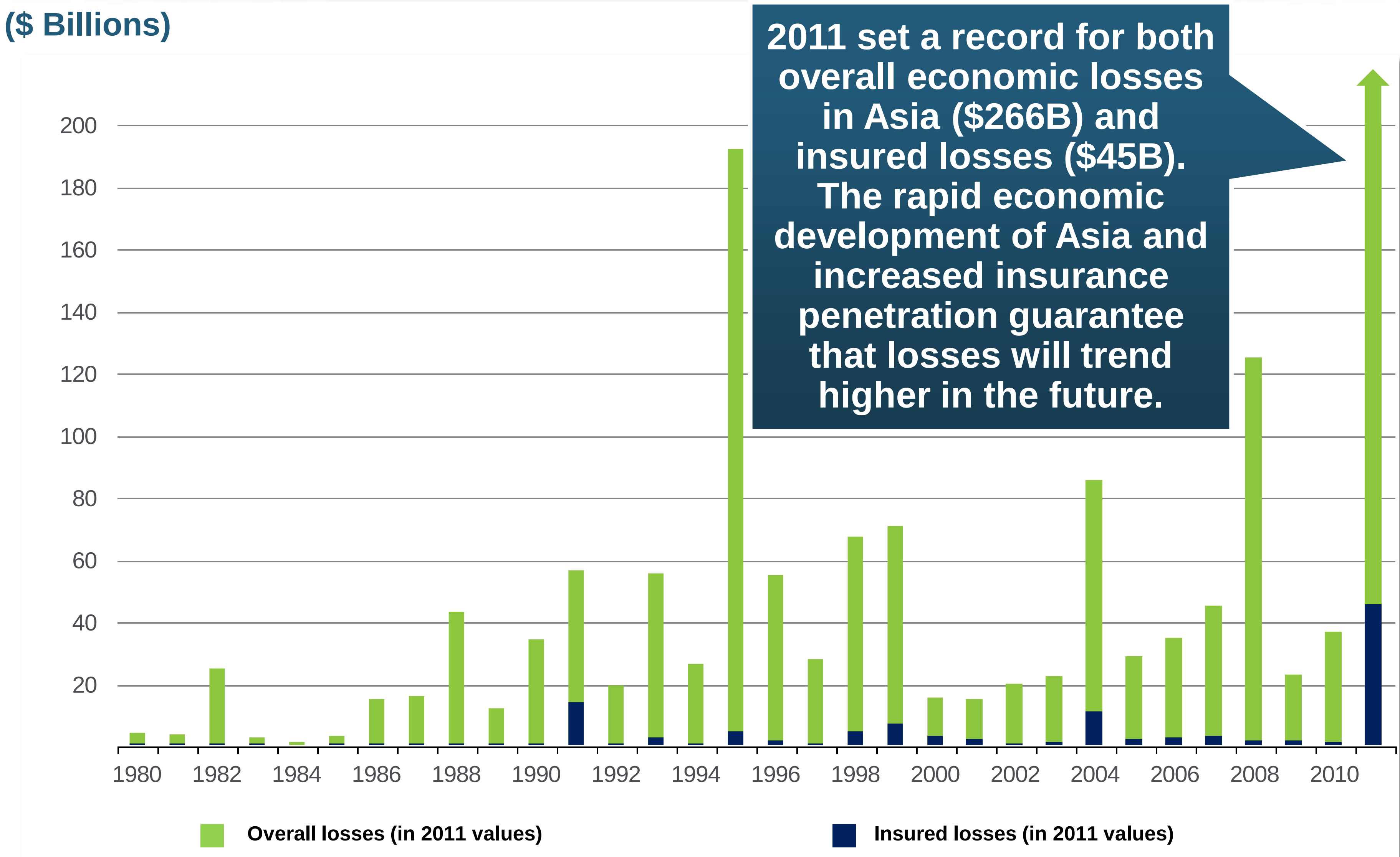

Source: MR NatCat*SERVICE*

U.S. Insured Catastrophe Loss Update

2011 Was One of the Most Expensive Years on Record

Top 14 Most Costly Disasters in U.S. History

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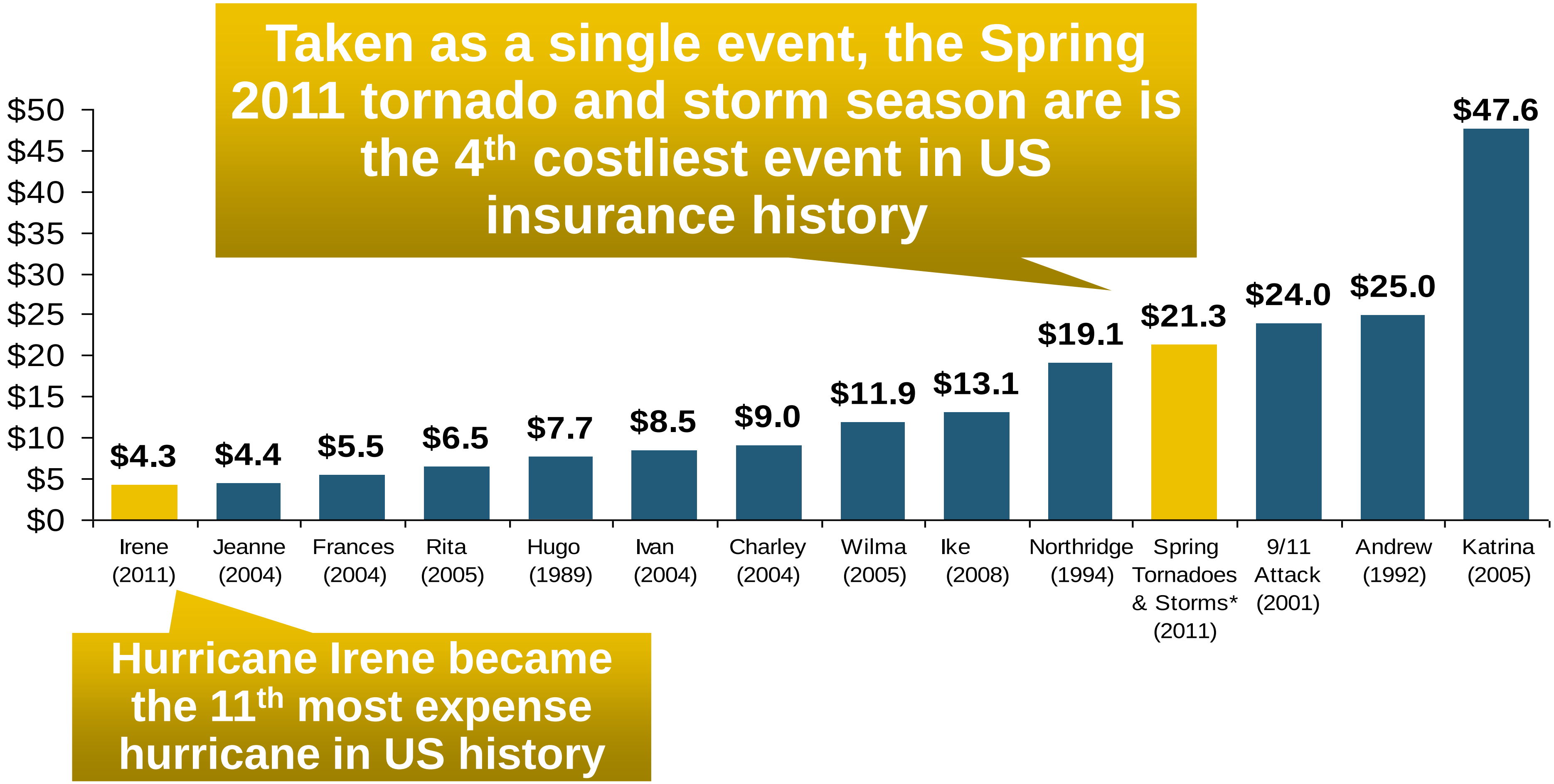
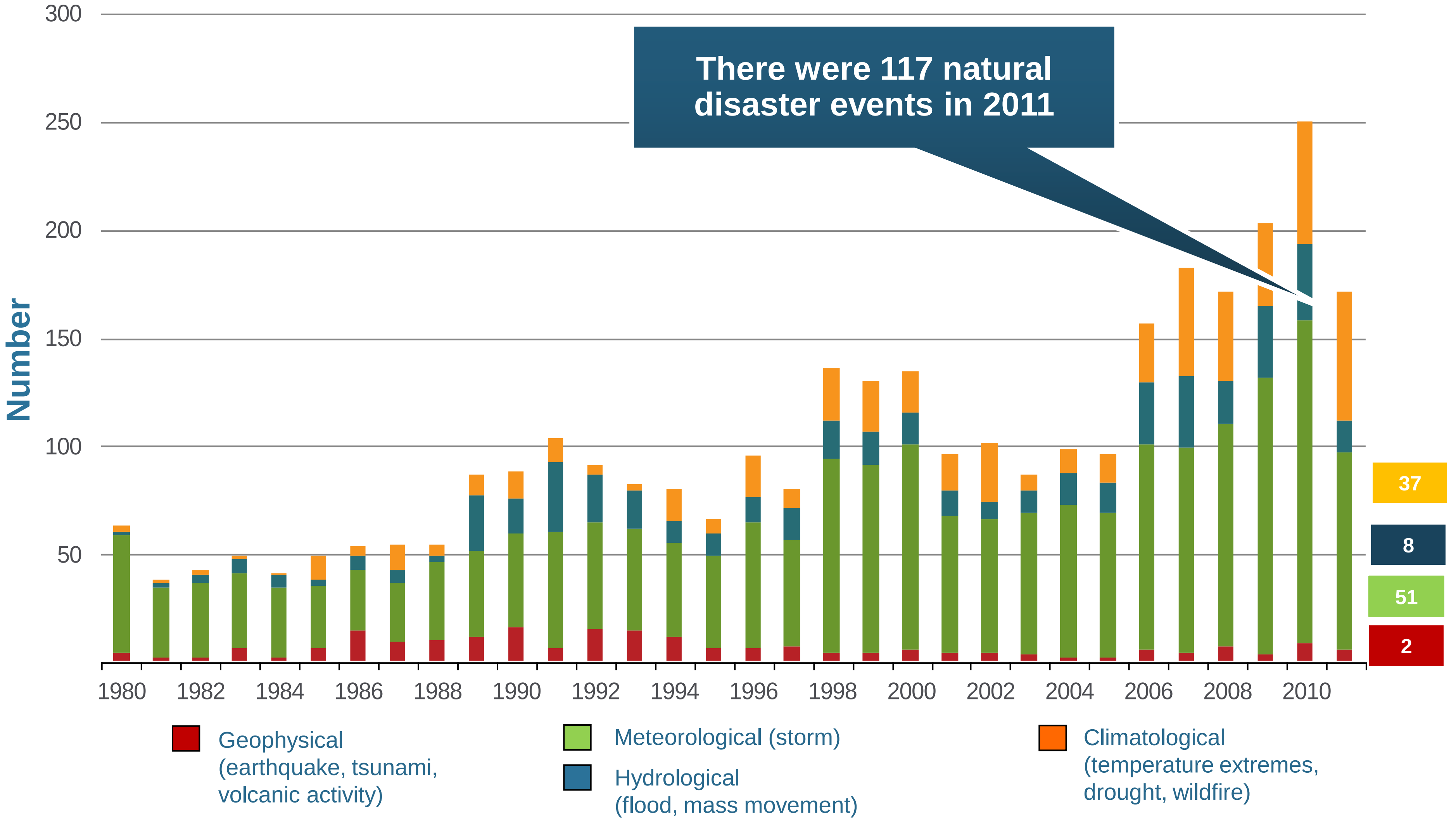
(Insured Losses, 2011 Dollars, $ Billions)



*Losses will actually be broken down into several "events" as determined by PCS. Includes losses for the period April 1 – June 30.
Sources: PCS; Insurance Information Institute inflation adjustments.

Natural Disasters in the United States, 1980 – 2011

Number of Events (Annual Totals 1980 – 2011)



Source: MR NatCat*SERVICE*

Losses Due to Natural Disasters in the US, 1980–2011 (Overall & Insured Losses)

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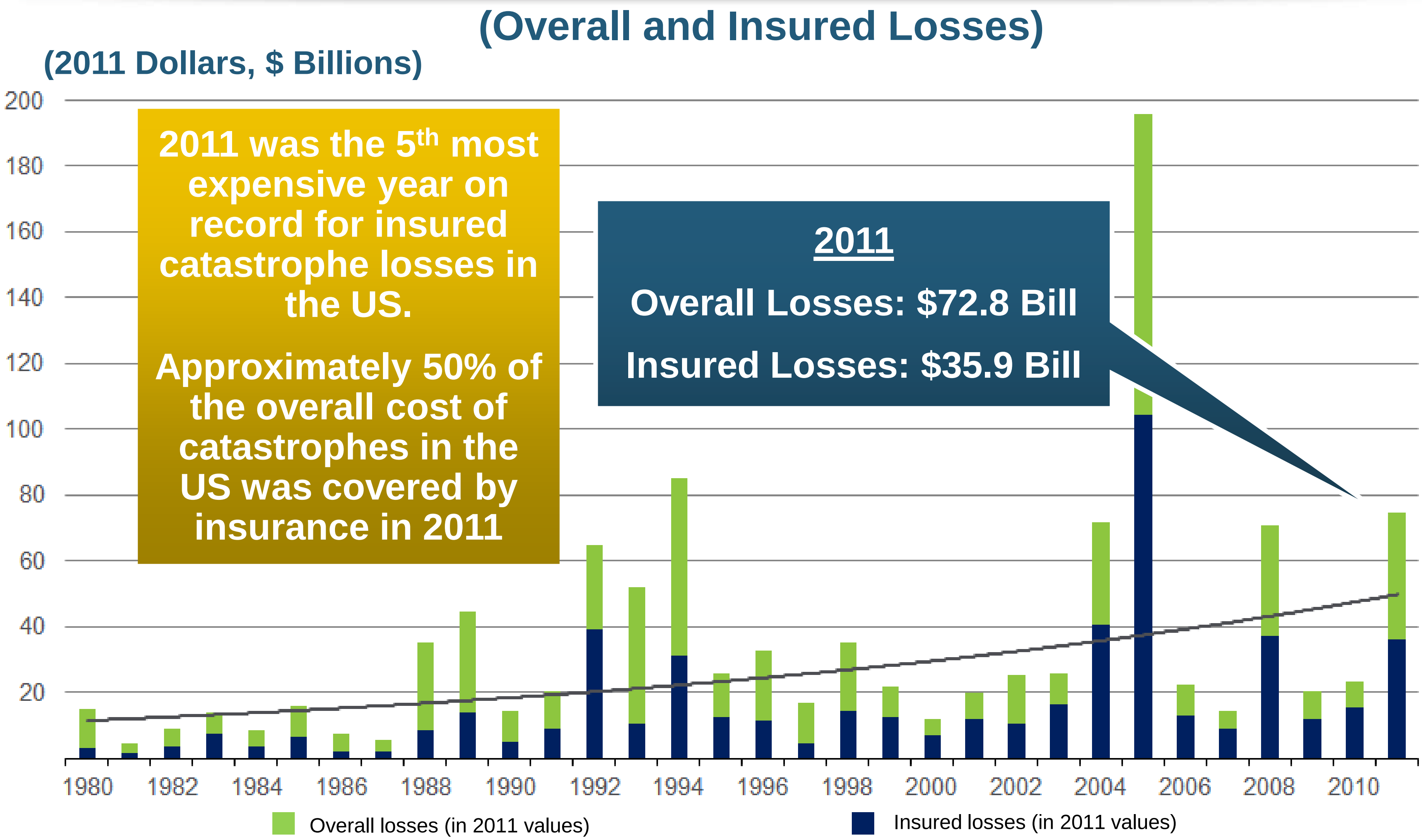
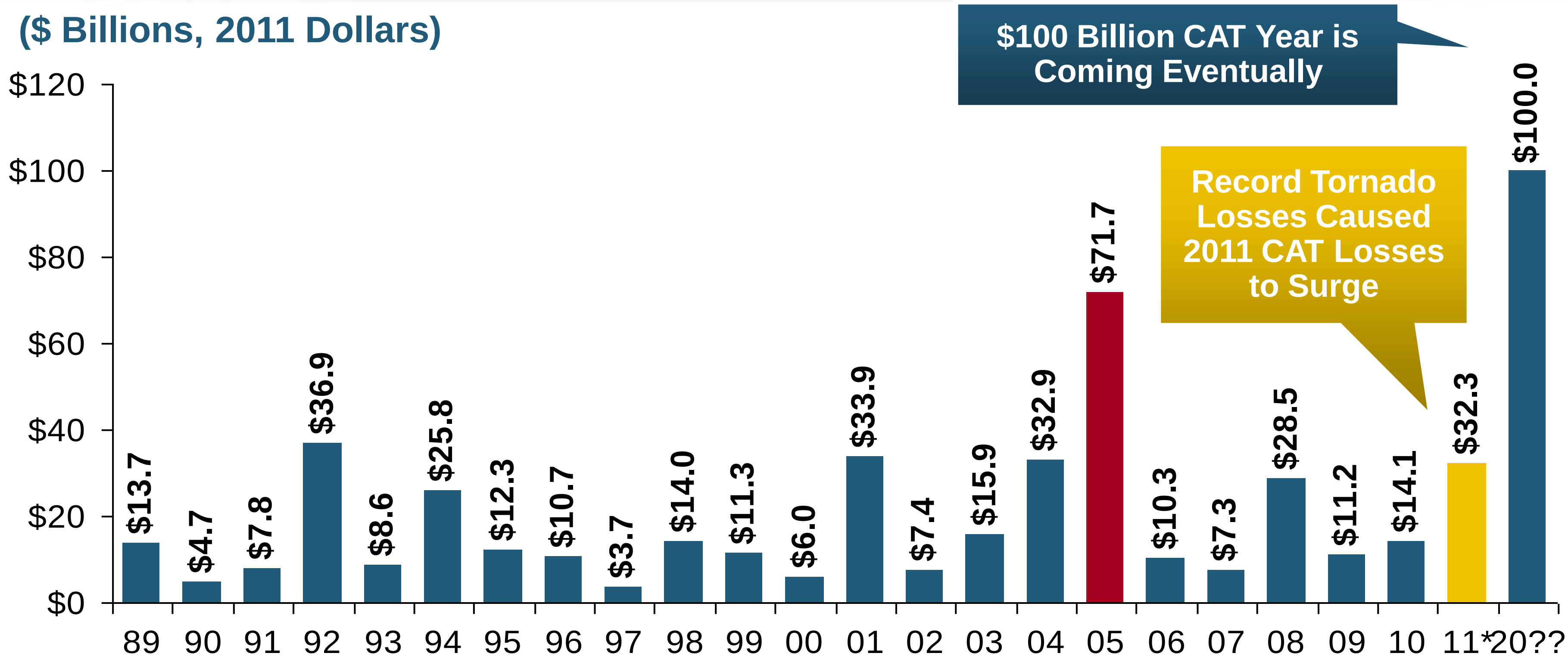


Source: MR NatCat*SERVICE*

US Insured Catastrophe Losses



US CAT Losses in 2011 Were the 5th Highest in US History on An Inflation Adjusted Basis

*PCS figure as of April 6, 2012.

Note: 2001 figure includes $20.3B for 9/11 losses reported through 12/31/01 ($25.9B 2011 dollars). Includes only business and personal property claims, business interruption and auto claims. Non-prop/BI losses = $12.2B ($15.6B in 2011 dollars.)

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

Natural Disaster Losses in the United States: 2011

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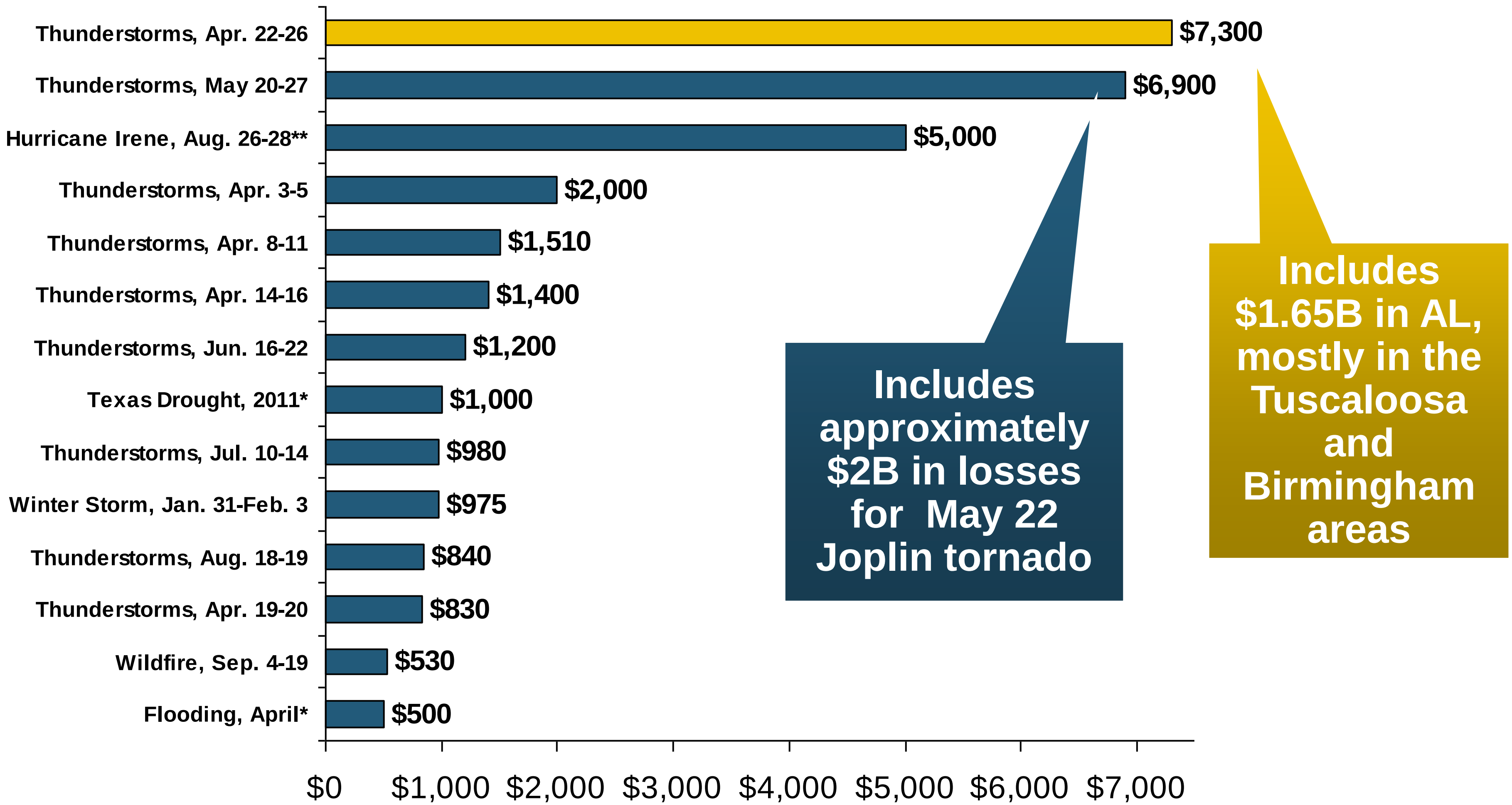
As of Jan. 1, 2012	Number of Events	Fatalities	Estimated Overall Losses (US $m)	Estimated Insured Losses (US $m)
Severe Thunderstorm	69	617	46,548	25,813
Winter Storm	9	67	2,708	2,017
Flood	14	20	2,705	535
Earthquake	5	1	257	50
Tropical Cyclone	3	0	10,700	5,510
Wildfire	58	15	1,922	855
Other	2	33	8,000	1,000

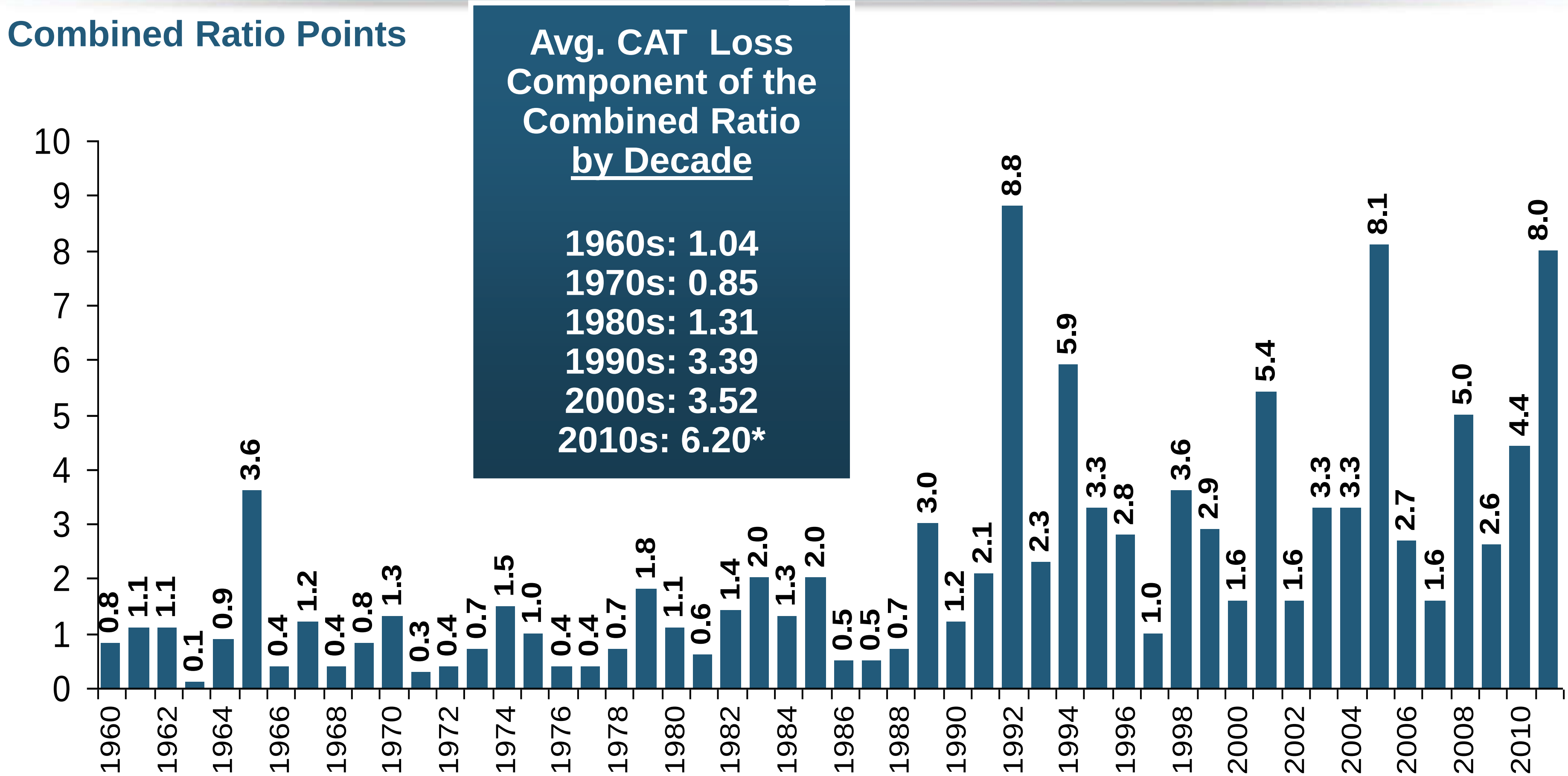
Source: MR NatCat*SERVICE*

2011's Most Expensive Catastrophes, Insured Losses



**Includes $700 million in flood losses insured through the National Flood Insurance Program.
Source: PCS except as noted by "*" which are sourced to Munich Re; Insurance Information Institute.

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



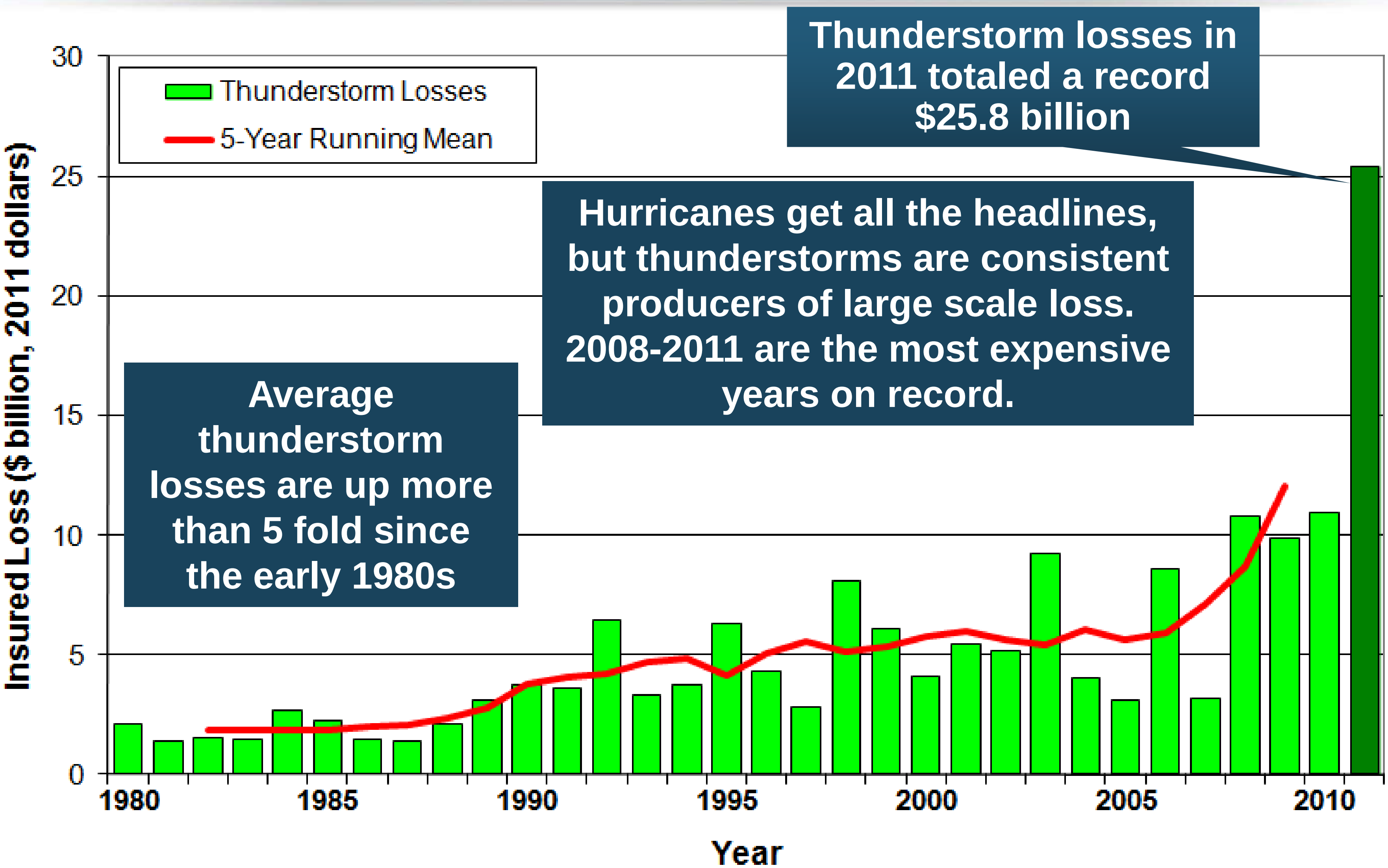
The Catastrophe Loss Component of Private Insurer Losses Has Increased Sharply in Recent Decades

*Insurance Information Institute estimates for 2010 and 2011 based on A.M. Best data.

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.

U.S. Thunderstorm Loss Trends, 1980 – 2011



Source: Property Claims Service, MR Nat*CatSERVICE*

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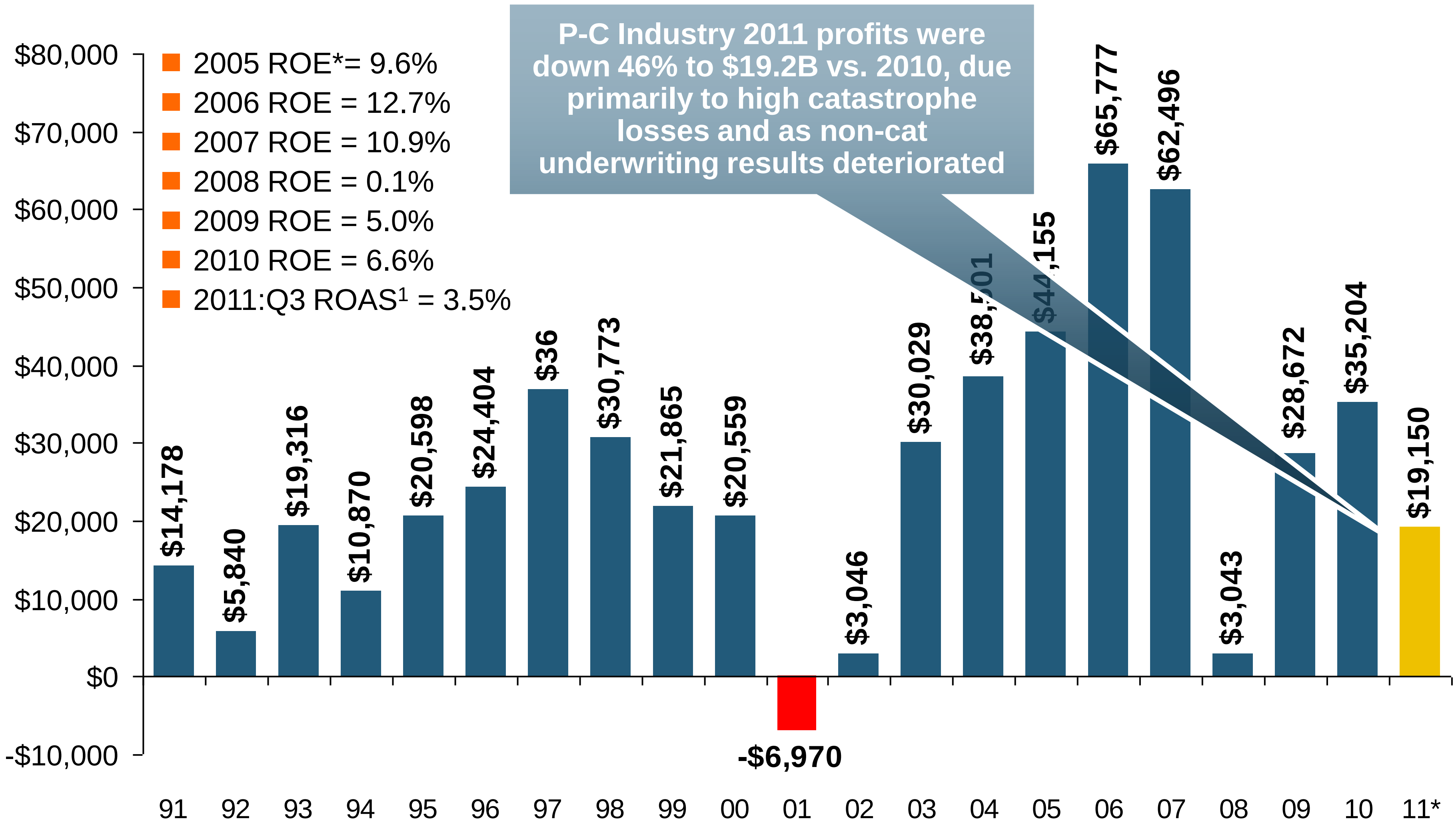
P/C Insurance Industry Financial Overview

Profit Recovery Was Set Back in 2011 by High Catastrophe Loss & Other Factors

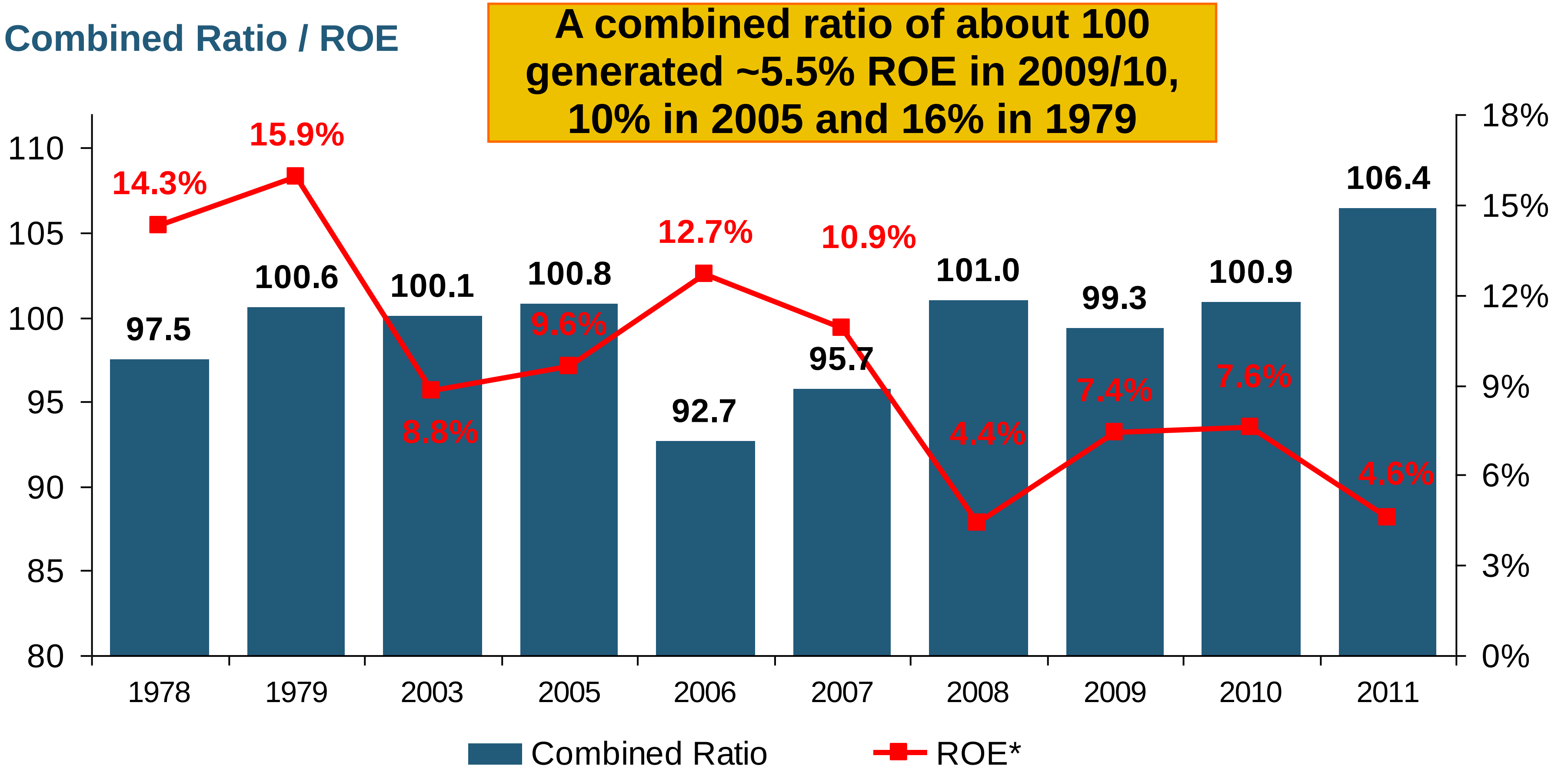
P/C Net Income After Taxes 1991–2011 ($ Millions)



* ROE figures are GAAP; [1]Return on avg. surplus. Excluding Mortgage & Financial Guaranty insurers yields a 4.6% ROAS for 2011, 7.6% for 2010 and 7.4% for 2009.

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

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

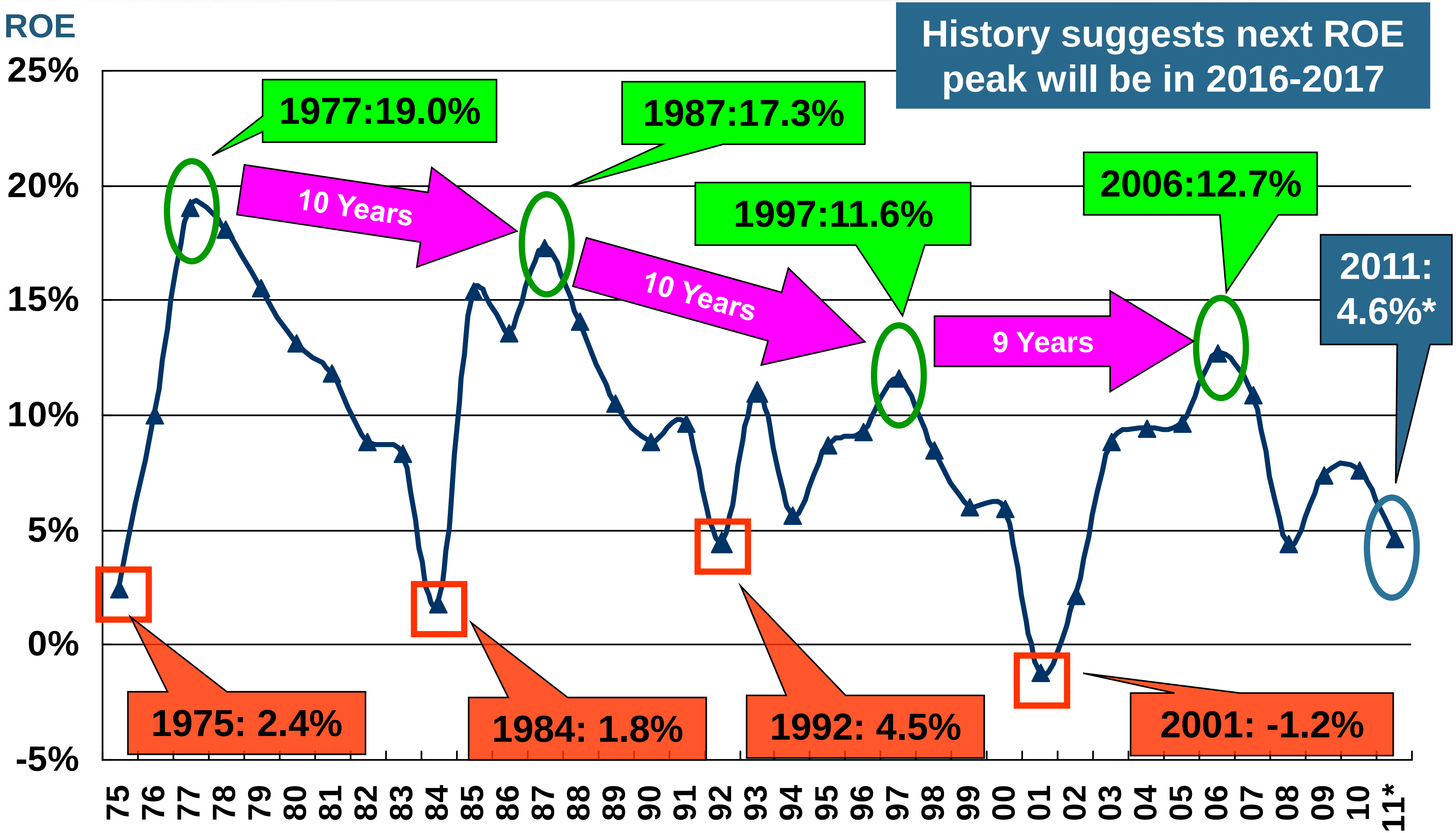


Combined Ratios Must Be Lower in Today's Depressed Investment Environment to Generate Risk Appropriate ROEs

* 2008 -2011 figures are return on average surplus and exclude mortgage and financial guaranty insurers. 2011 combined ratio including M&FG insurers is 108.2, ROAS = 3.5%.

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

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



*Profitability = P/C insurer ROEs are I.I.I. estimates. 2011 figure is an estimate based on ROAS data. Note: Data for 2008-2011 exclude mortgage and financial guaranty insurers. For 2011:Q3 ROAS = 3.5% including M&FG.
Source: Insurance Information Institute; NAIC, ISO, A.M. Best.

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The BIG Question: When Will the Market Turn?

Are Catastrophes and Other Factors Pressuring Insurance Markets?

Criteria Necessary for a "Market Turn": *All Four Criteria Must Be Met*

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Criteria	Status	Comments
Sustained Period of Large Underwriting Losses	*Early Stage, Inevitable*	•Apart from 2011 CAT losses, overall p/c underwriting losses remain modest •Combined ratios (ex-CATs) still in low 100s (vs. 110+ at onset of last hard market) •Prior-year reserve releases continue to reduce u/w losses, boost ROEs, though more modestly
Material Decline in Surplus/ Capacity	*Entered 2011 At Record High; Only Small Decline*	•Surplus hit a record $565B as of 3/31/11 •Fell just 1.6% through 12/31/11 from 12/31/10 •Will likely see new record in 2012 •Little excess capacity remains in reinsurance markets •Modest growth in demand for insurance is insufficient to absorb much excess capacity
Tight Reinsurance Market	*Somewhat in Place*	•Much of the global "excess capacity" was eroded by cats •Higher prices in Asia/Pacific •Modestly higher pricing for US risks
Renewed Underwriting & Pricing Discipline	*Some Firming esp. in Property, WC*	•Commercial lines pricing trends have turned from negative to flat and now positive, esp. Property & WC; •Competition remains intense as many seek to maintain market share

Sources: Barclays Capital; Insurance Information Institute.

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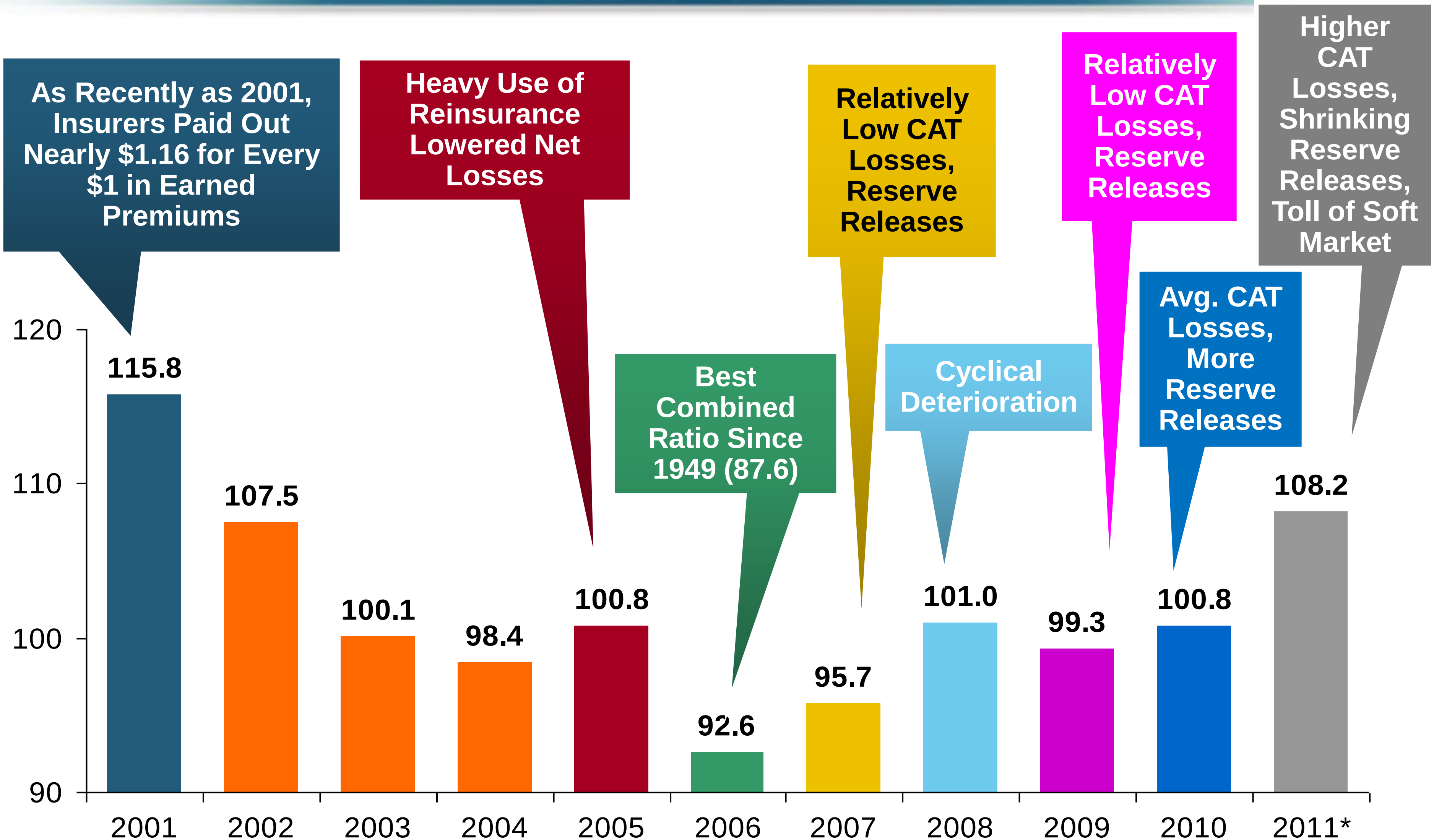
1. UNDERWRITING

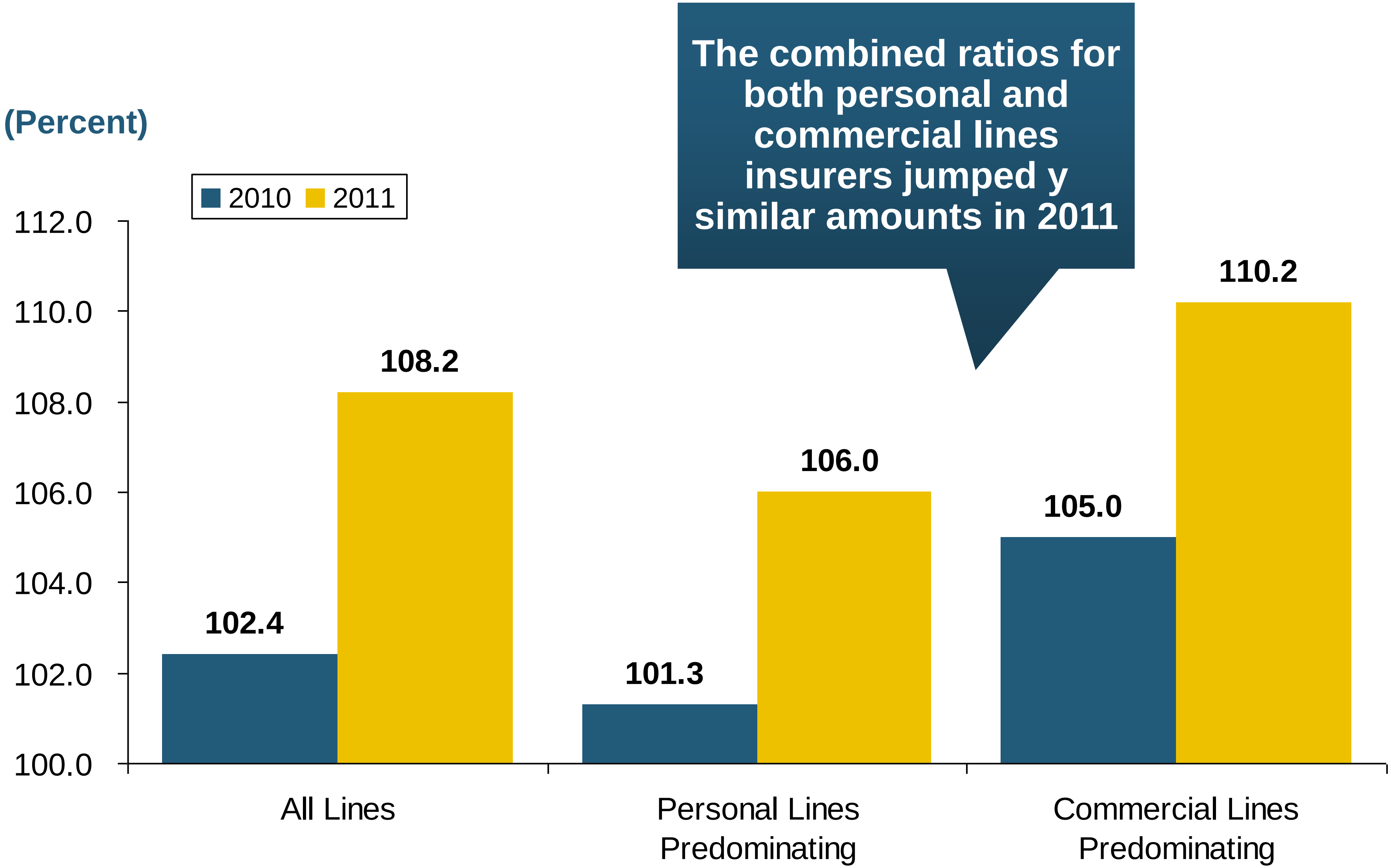
Have Underwriting Losses Been Large Enough for Long Enough to Turn the Market?

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



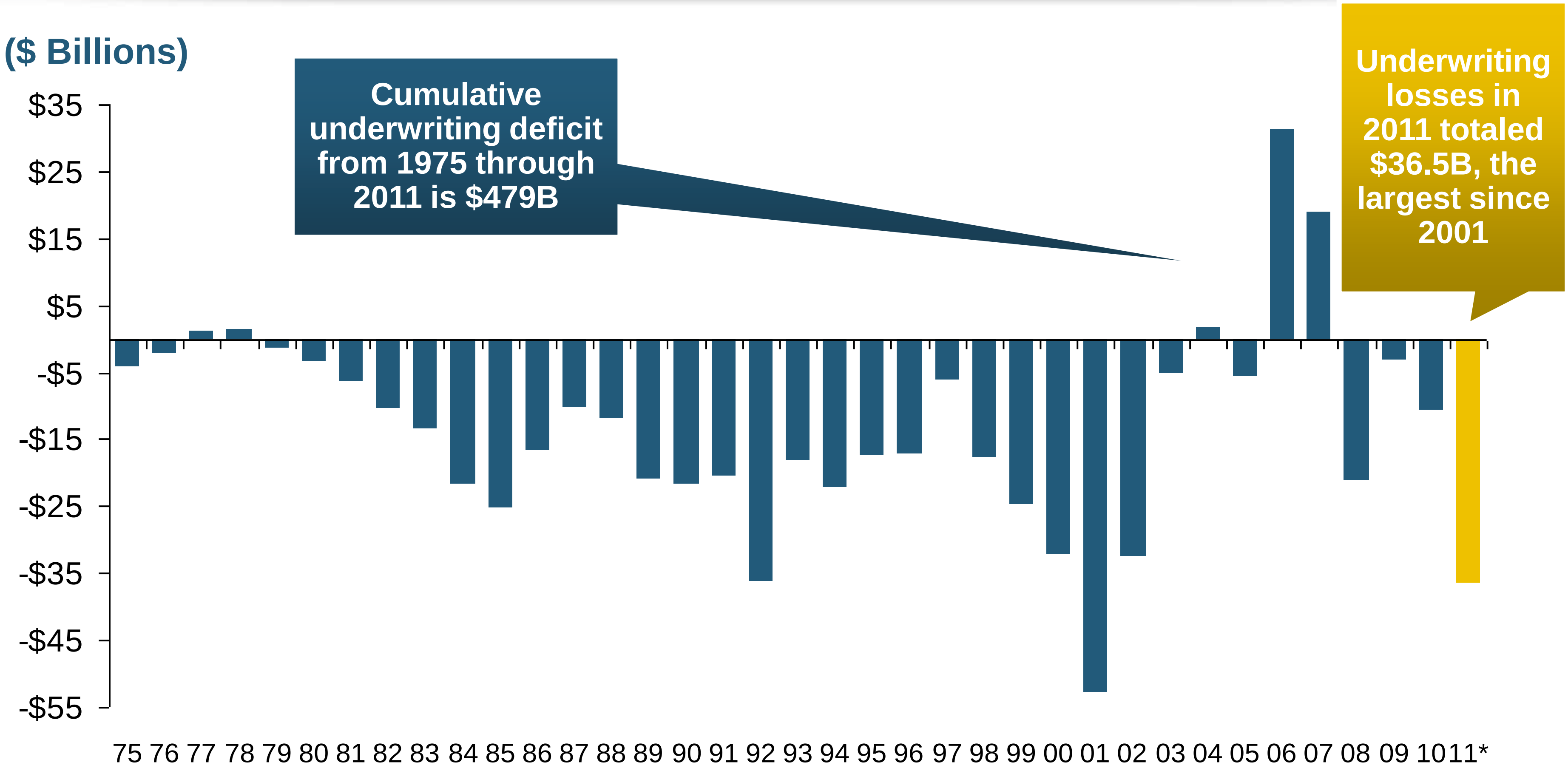
* Excludes Mortgage & Financial Guaranty insurers 2008--2011. Including M&FG, 2008=105.1, 2009=100.7, 2010=102.4, 2011=106.4
Sources: A.M. Best, ISO.

Combined Ratios by Predominant Business Segment, 2011 vs. 2010



Source: ISO/PCI; Insurance Information Institute

Underwriting Gain (Loss) 1975–2011E*

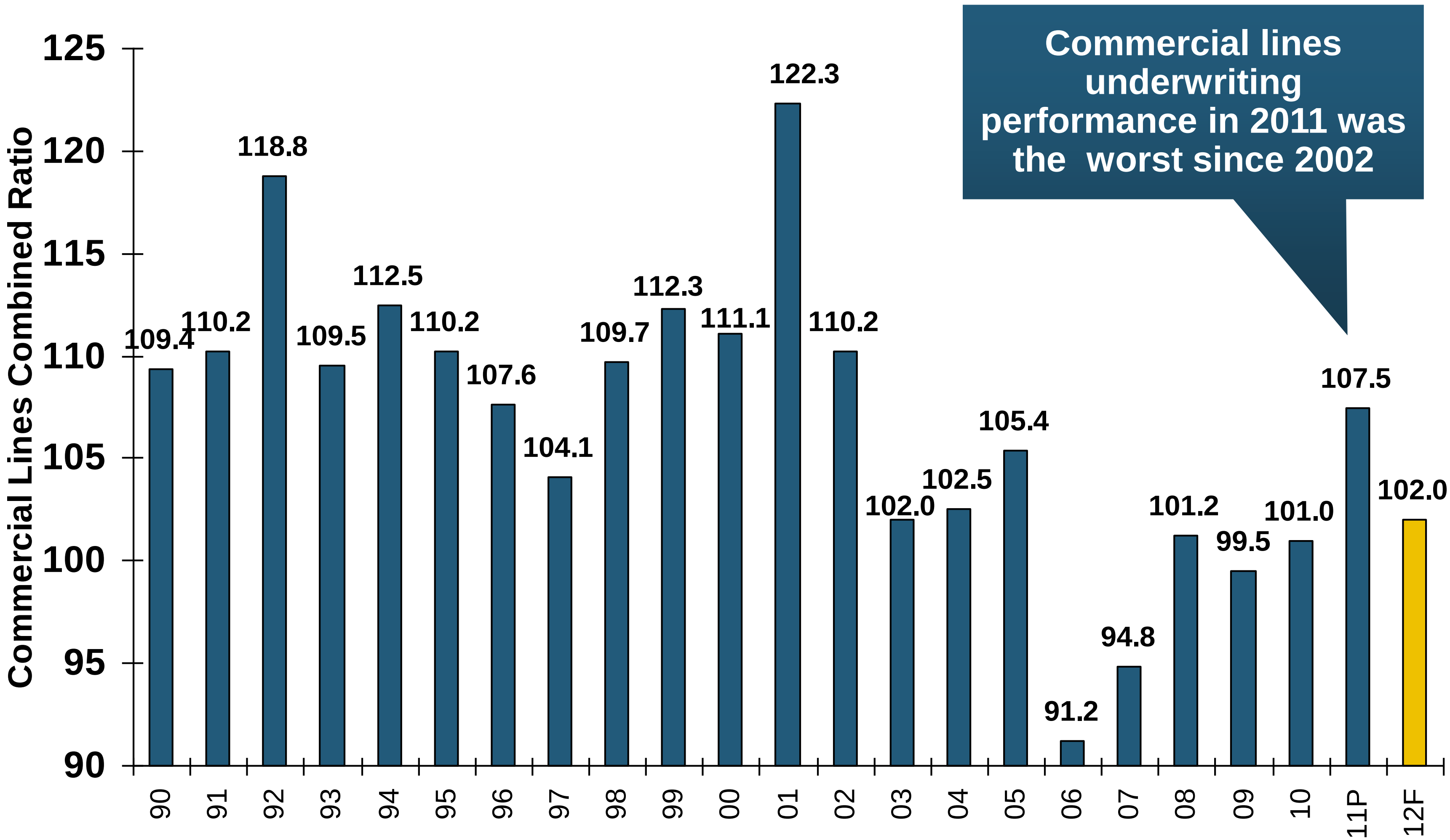


Large Underwriting Losses Are *NOT* Sustainable in Current Investment Environment

* Includes mortgage and financial guaranty insurers in all years

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

Commercial Lines Combined Ratio, 1990-2012F*



*2007-2012 figures exclude mortgage and financial guaranty segments.
Source: A.M. Best; Insurance Information Institute

P/C Reserve Development, 1992–2013F

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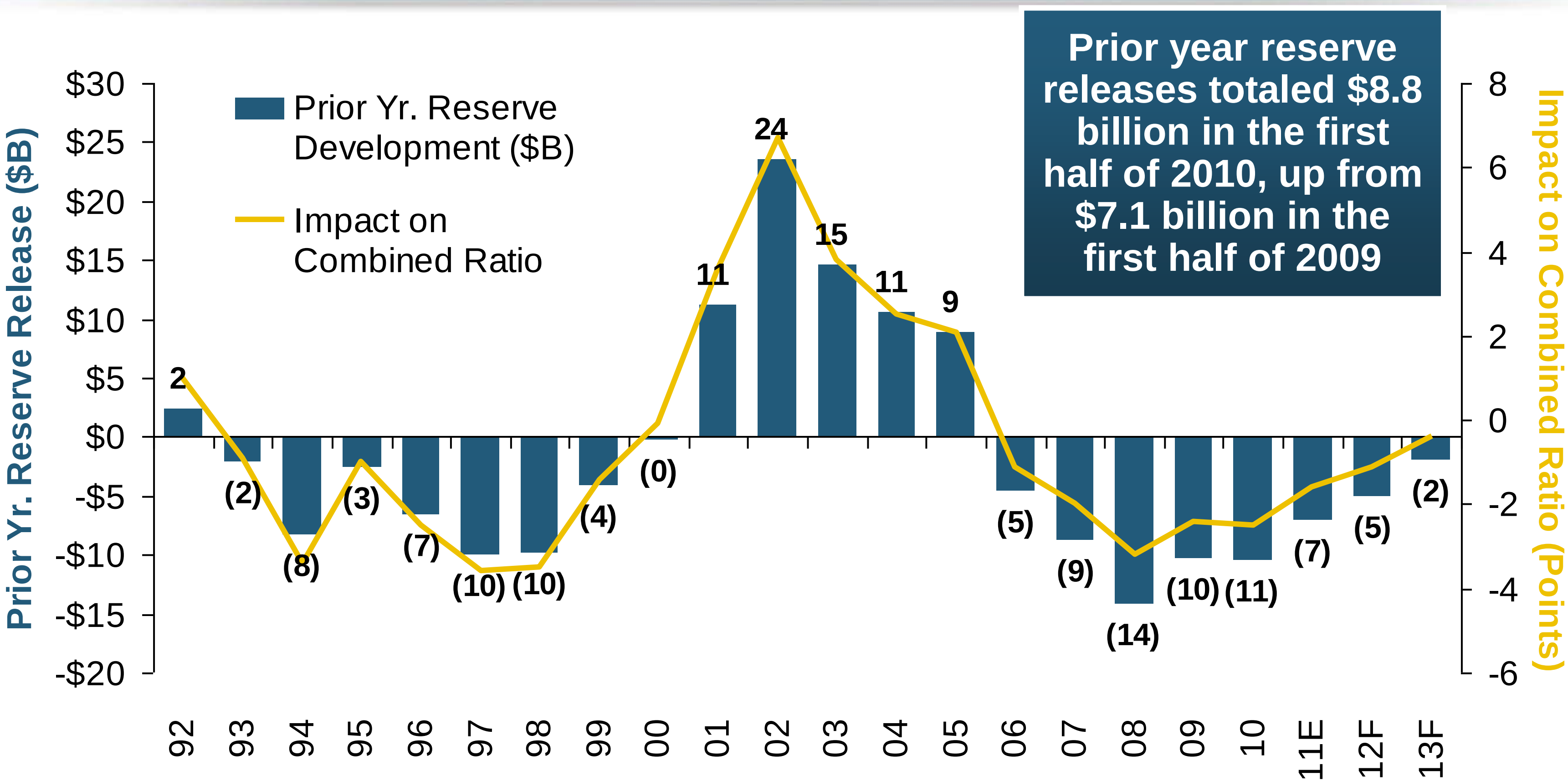

Reserve Releases Remained Strong in 2010 But Tapered Off in 2011. Releases Are Expected to Further Diminish in 2012 and 2103

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: Barclays Capital; A.M. Best.

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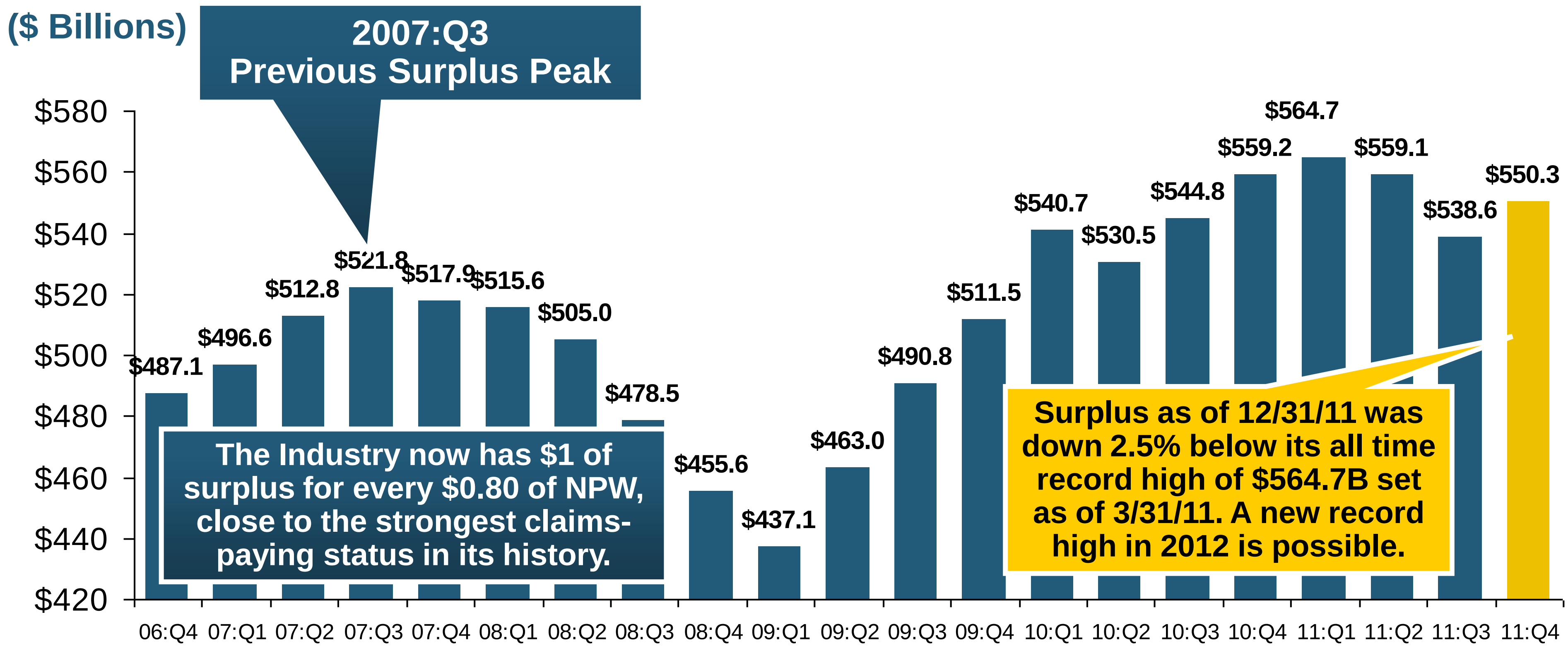
2. SURPLUS/CAPITAL/CAPACITY

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

Policyholder Surplus, 2006:Q4–2011:Q4



*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.

Sources: ISO, A.M .Best.

Quarterly Surplus Changes Since 2011:Q1 Peak

11:Q2: -$5.6B (-1.0%)

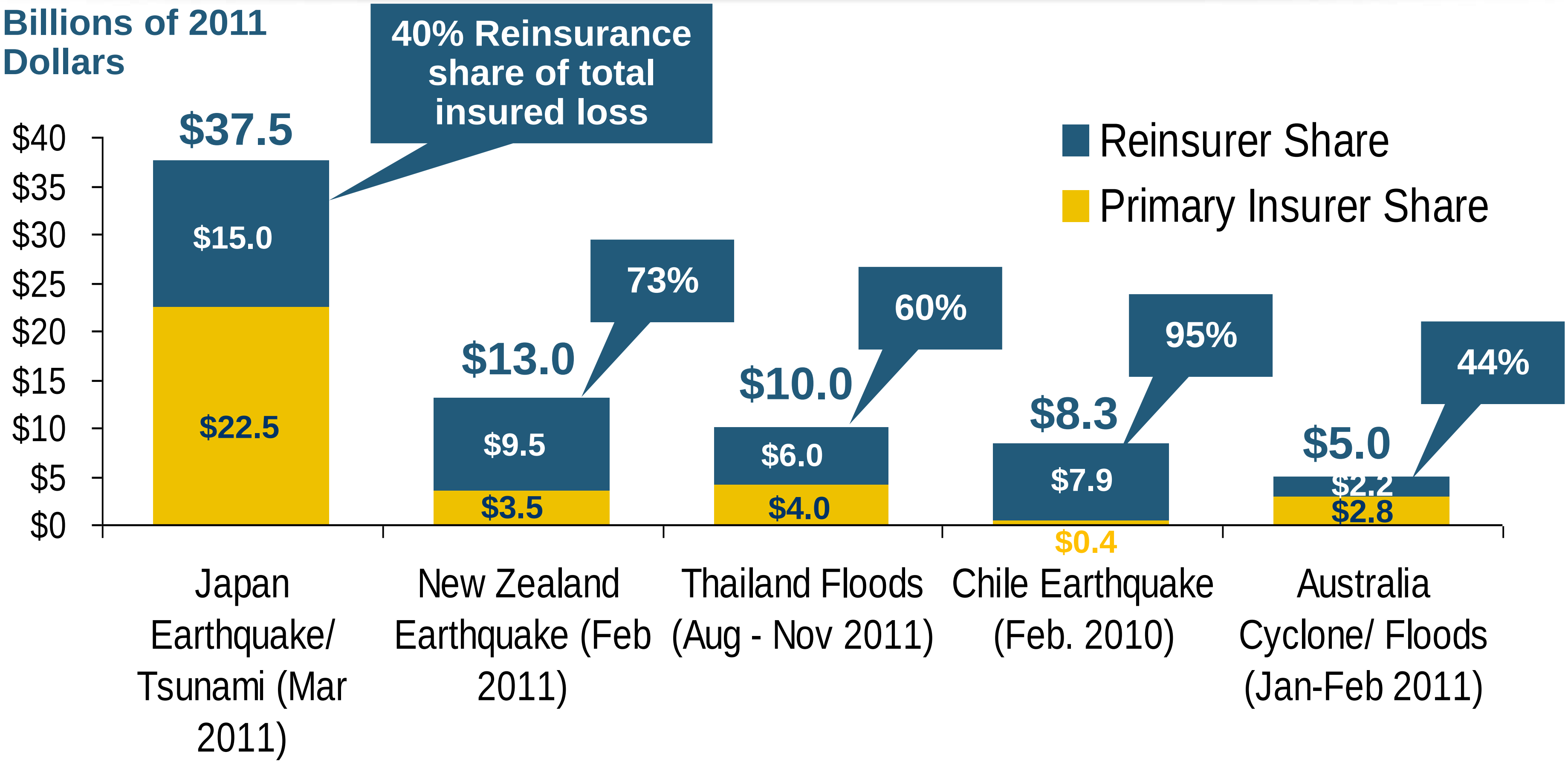
11:Q3: -$26.1B (-4.6%)

11:Q4: -$14.3B (-2.5%)

3. REINSURANCE MARKET CONDITIONS

Record Global Catastrophes Activity is Pressuring Pricing

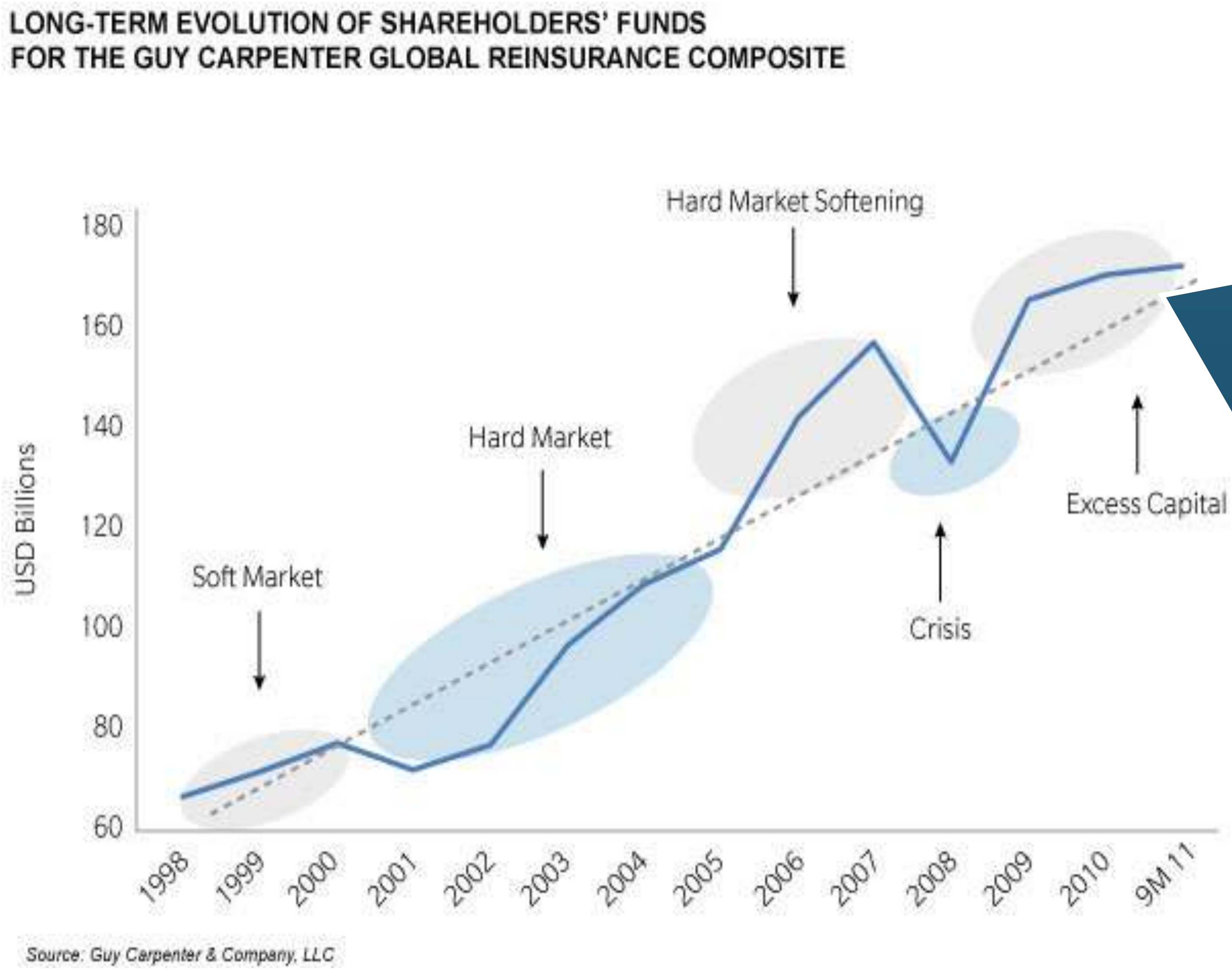
Reinsurer Share of Recent Significant Market Losses



Reinsurers Paid a High Proportion of Insured Losses Arising from Major Catastrophic Events Around the World in Recent Years

Source: Insurance Information Institute from reinsurance share percentages provided in RAA, ABIR and CEA press release, Jan. 13, 2011.

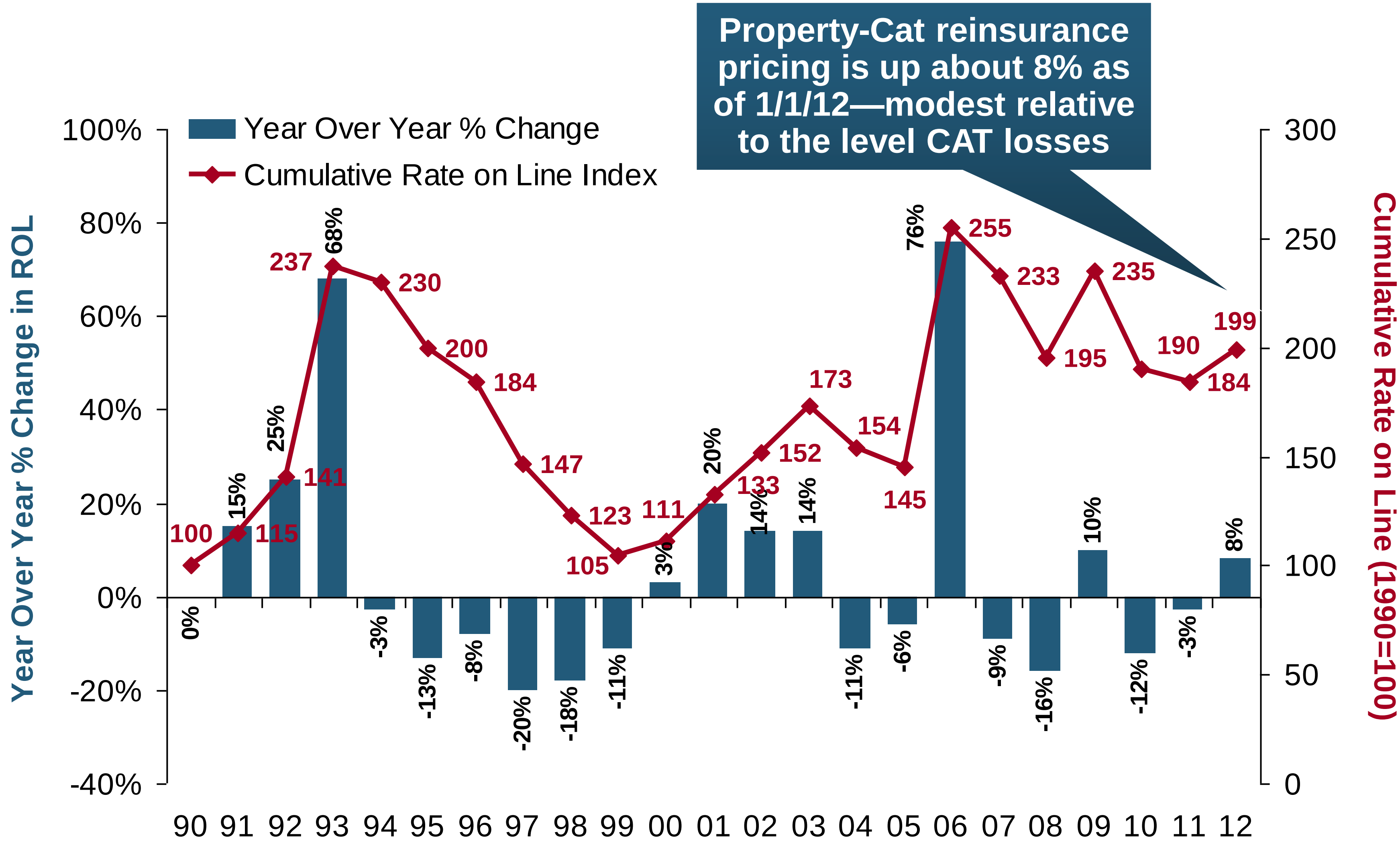
Historical Capital Levels of Guy Carpenter Reinsurance Composite, 1998—3Q11



Most excess reinsurance capacity was removed from the market in 2011, but there does not appear to be a shortage, leading to modest increases in 2012 reinsurance renewals except in areas hit hard by CATs.

Source: Guy Carpenter, *GC Capital Ideas.com,* February 28, 2012.

Global Property Catastrophe Rate on Line Index, 1990—2012 (as of Jan. 1)



Sources: Guy Carpenter; Insurance Information Institute.

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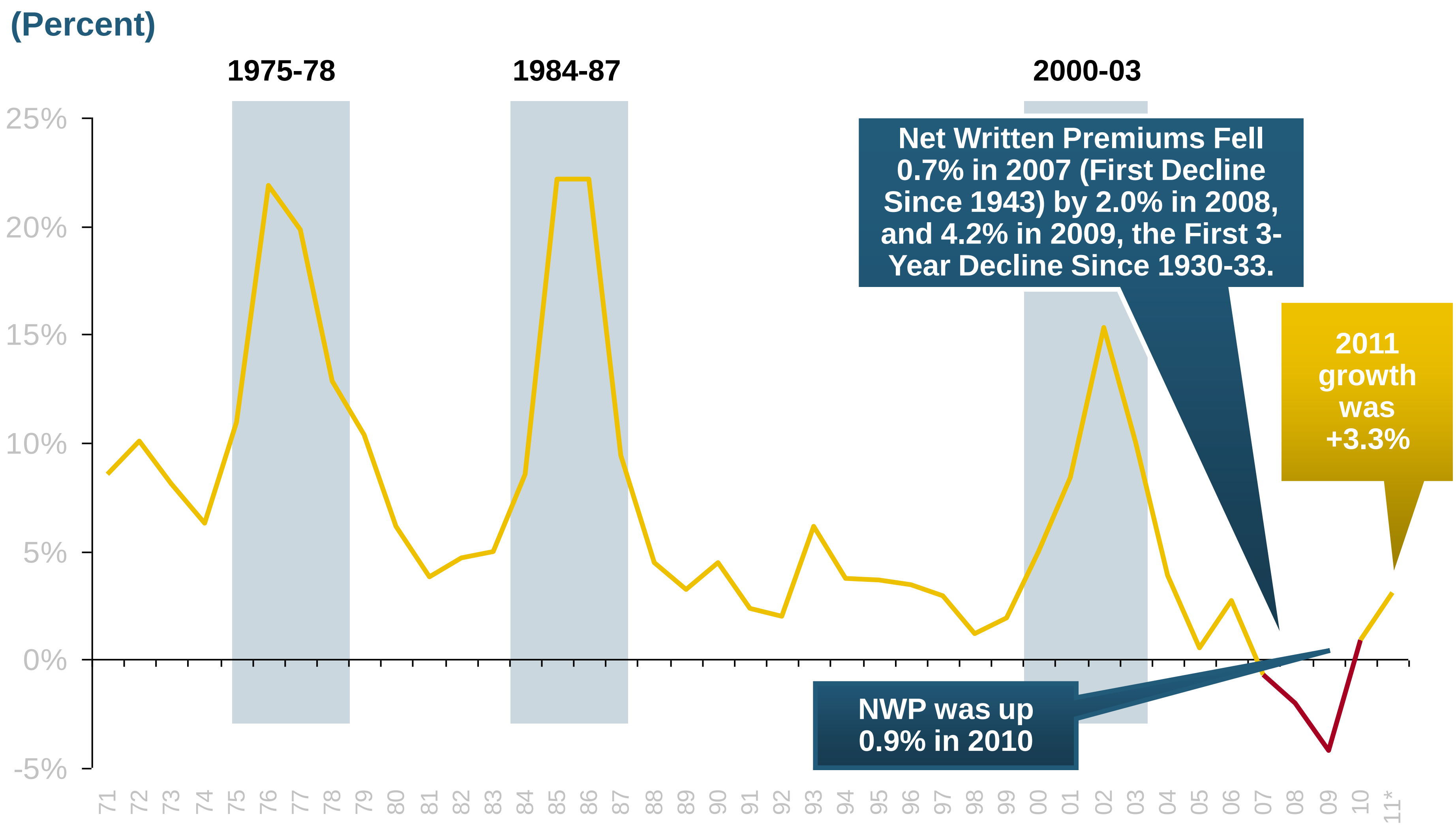
4. RENEWED PRICING DISCIPLINE

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

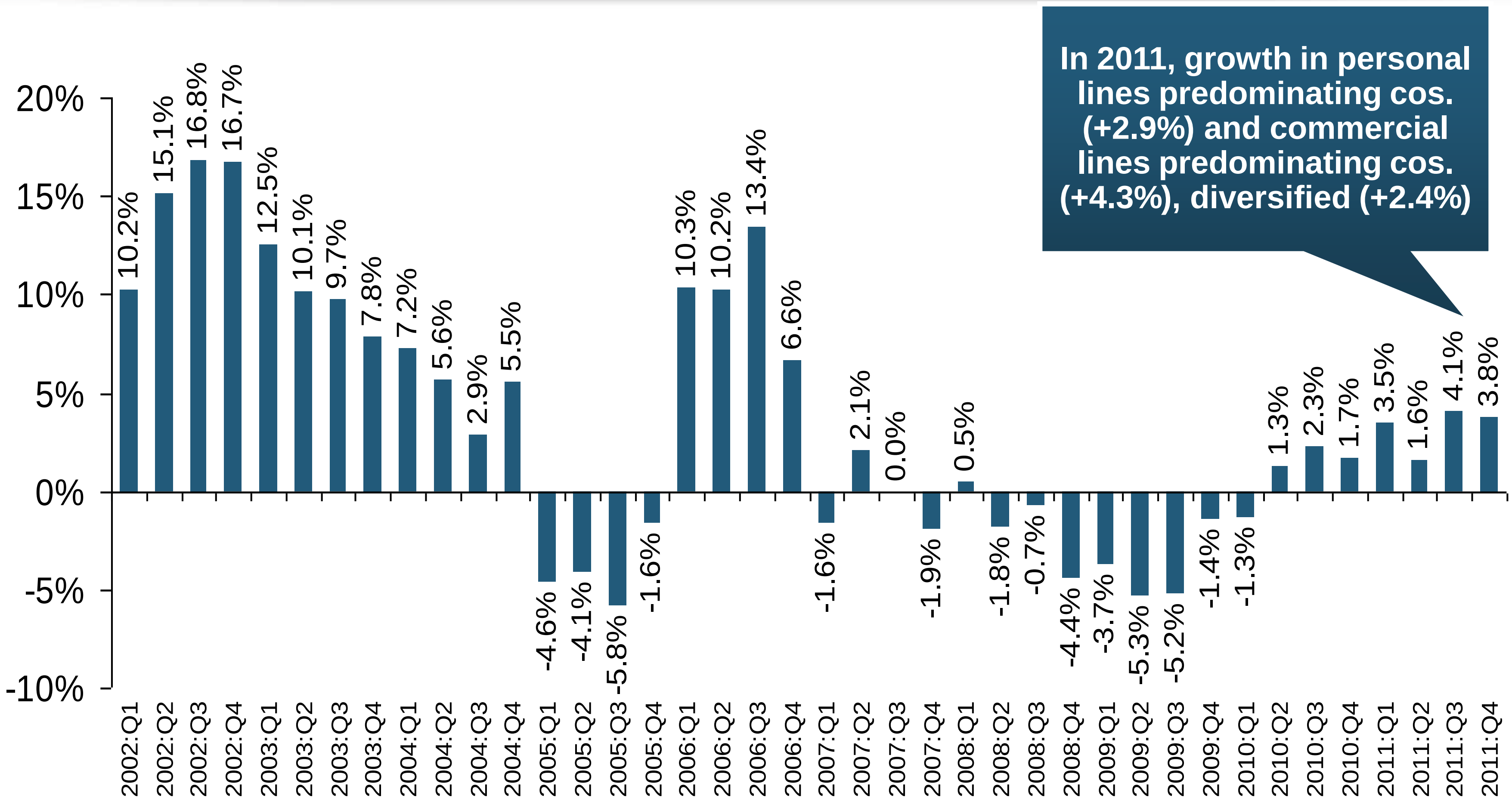
Premium Growth Is Up Modestly: More in 2012?



Shaded areas denote “hard market” periods

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

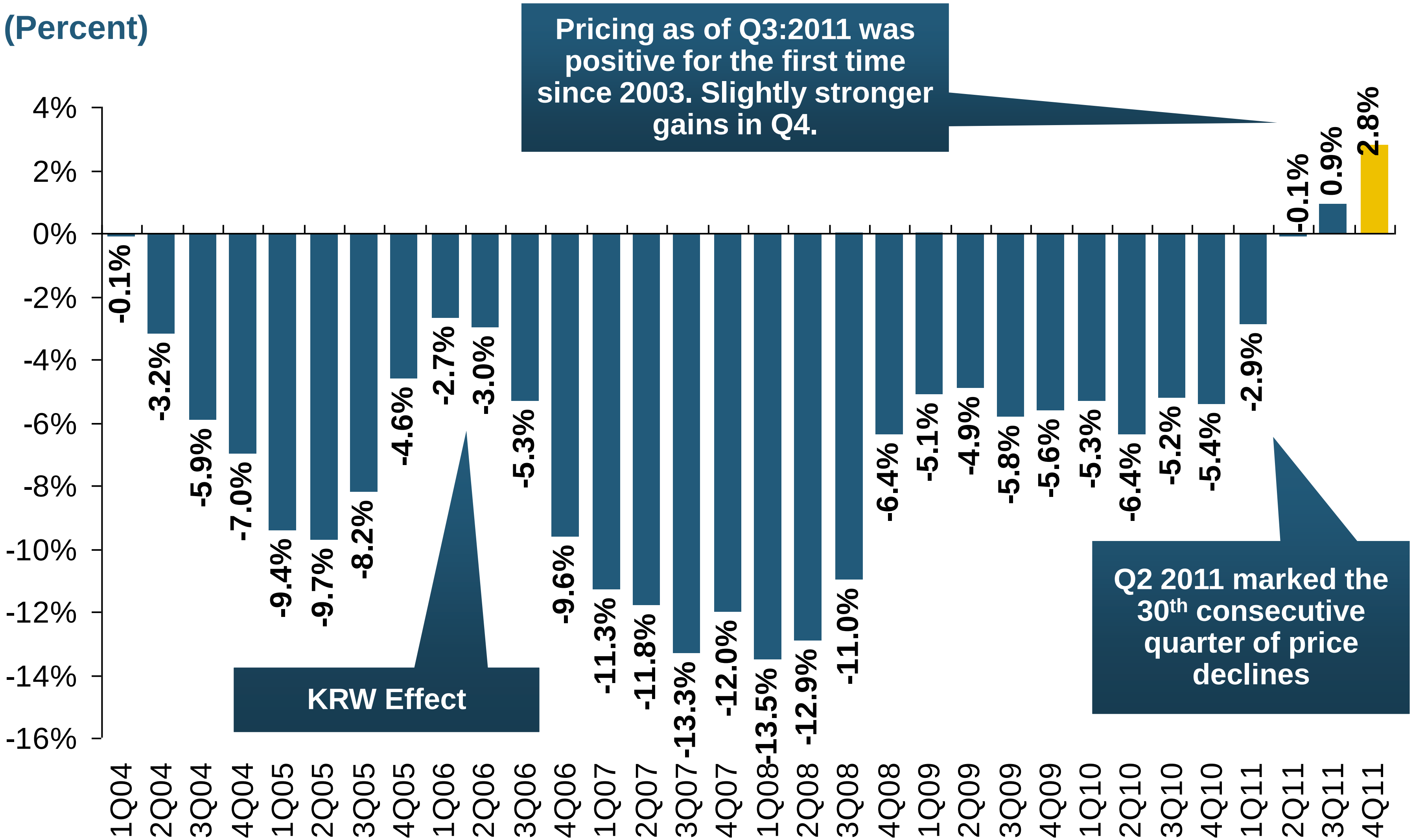
P/C Net Premiums Written: % Change, Quarter vs. Year-Prior Quarter



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

Sources: ISO, Insurance Information Institute.

Average Commercial Rate Change, All Lines, (1Q:2004–4Q:2011)



Source: Council of Insurance Agents & Brokers (1Q04-4Q11); Insurance Information Institute

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

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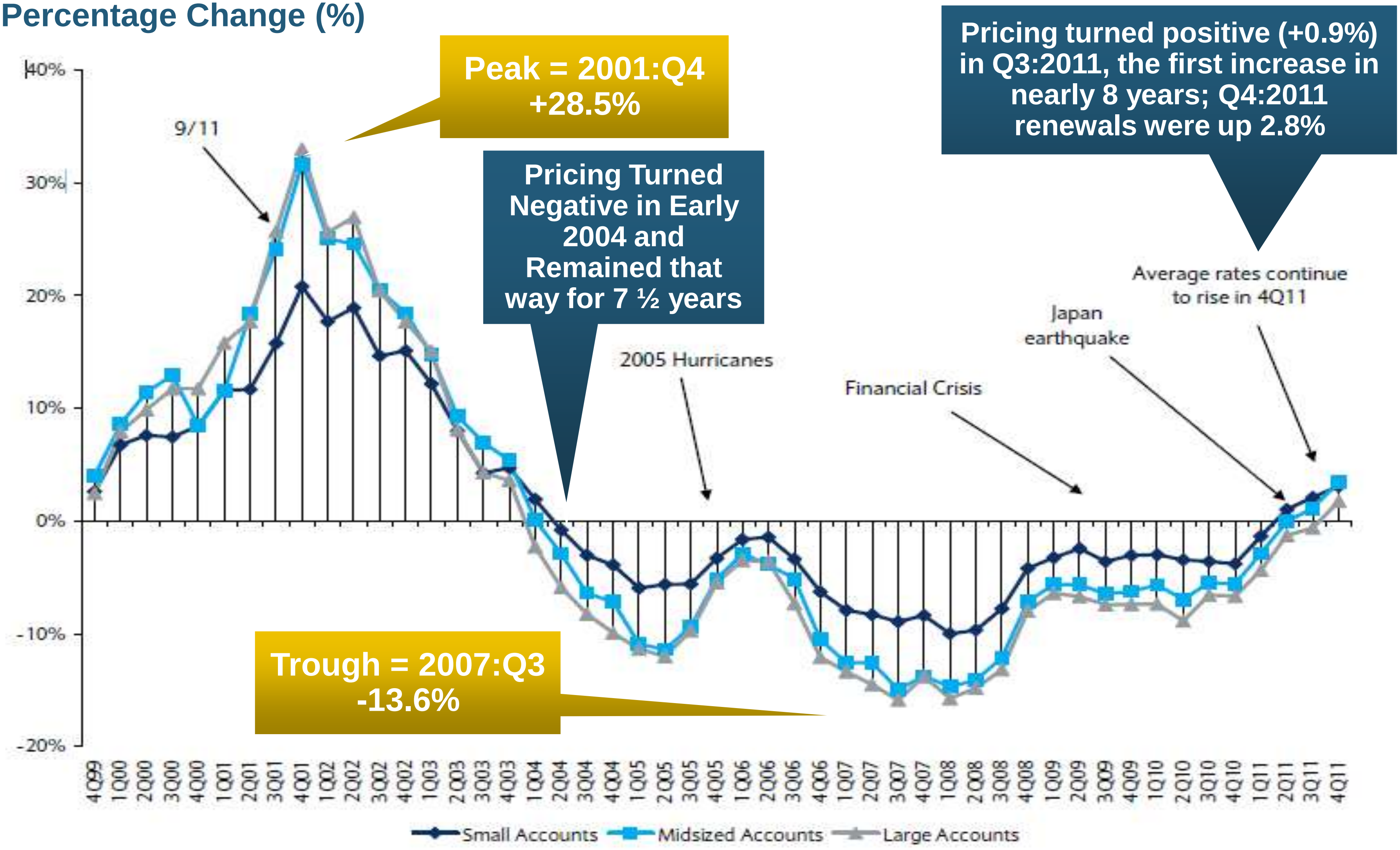
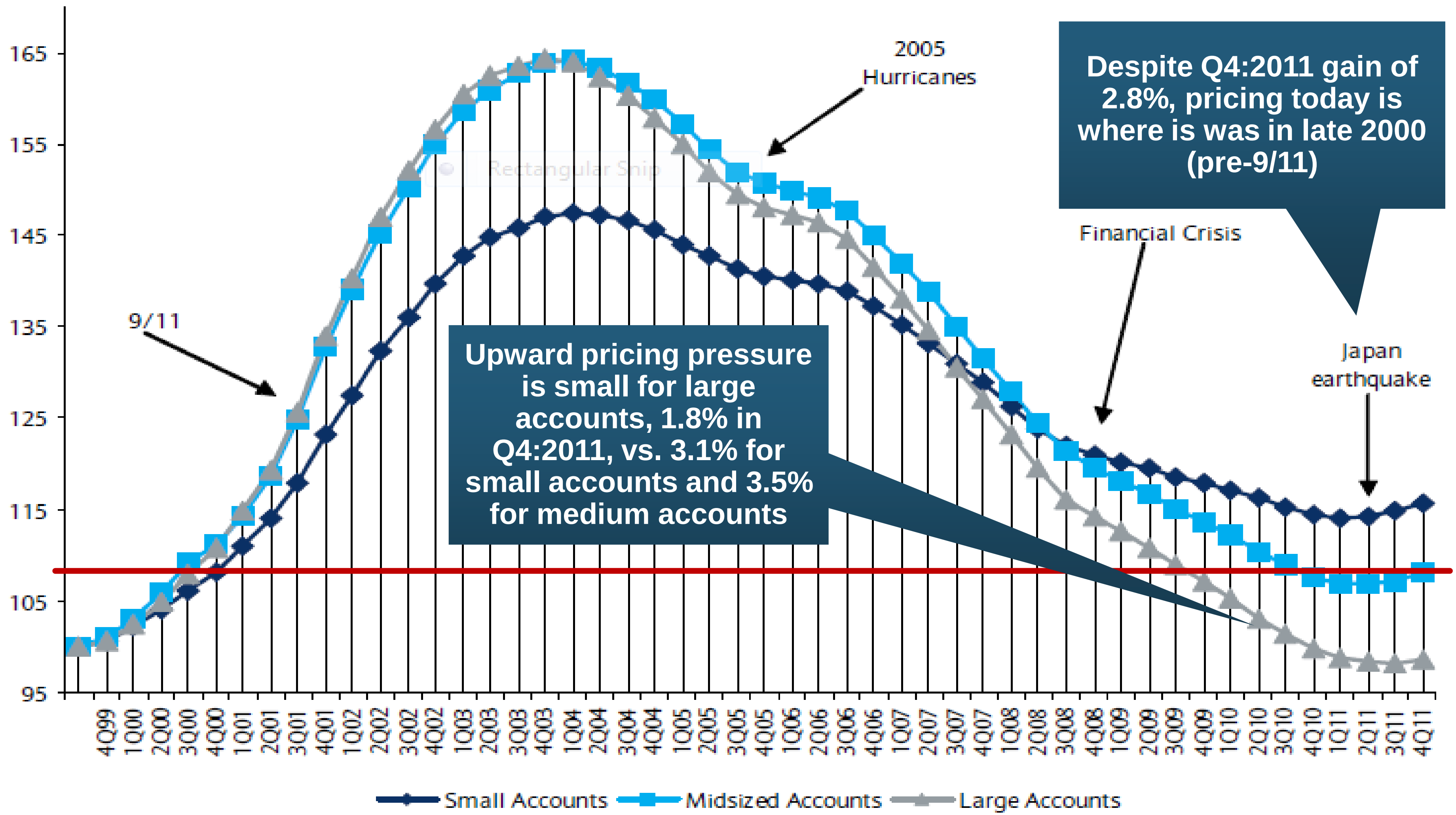
Percentage Change (%)



Source: Council of Insurance Agents and Brokers; Barclay's Capital; Insurance Information Institute.

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

1999:Q4 = 100



Source: Council of Insurance Agents and Brokers; Barclay's Capital; Insurance Information Institute.

Change in Commercial Rate Renewals, by Line: 2011:Q4

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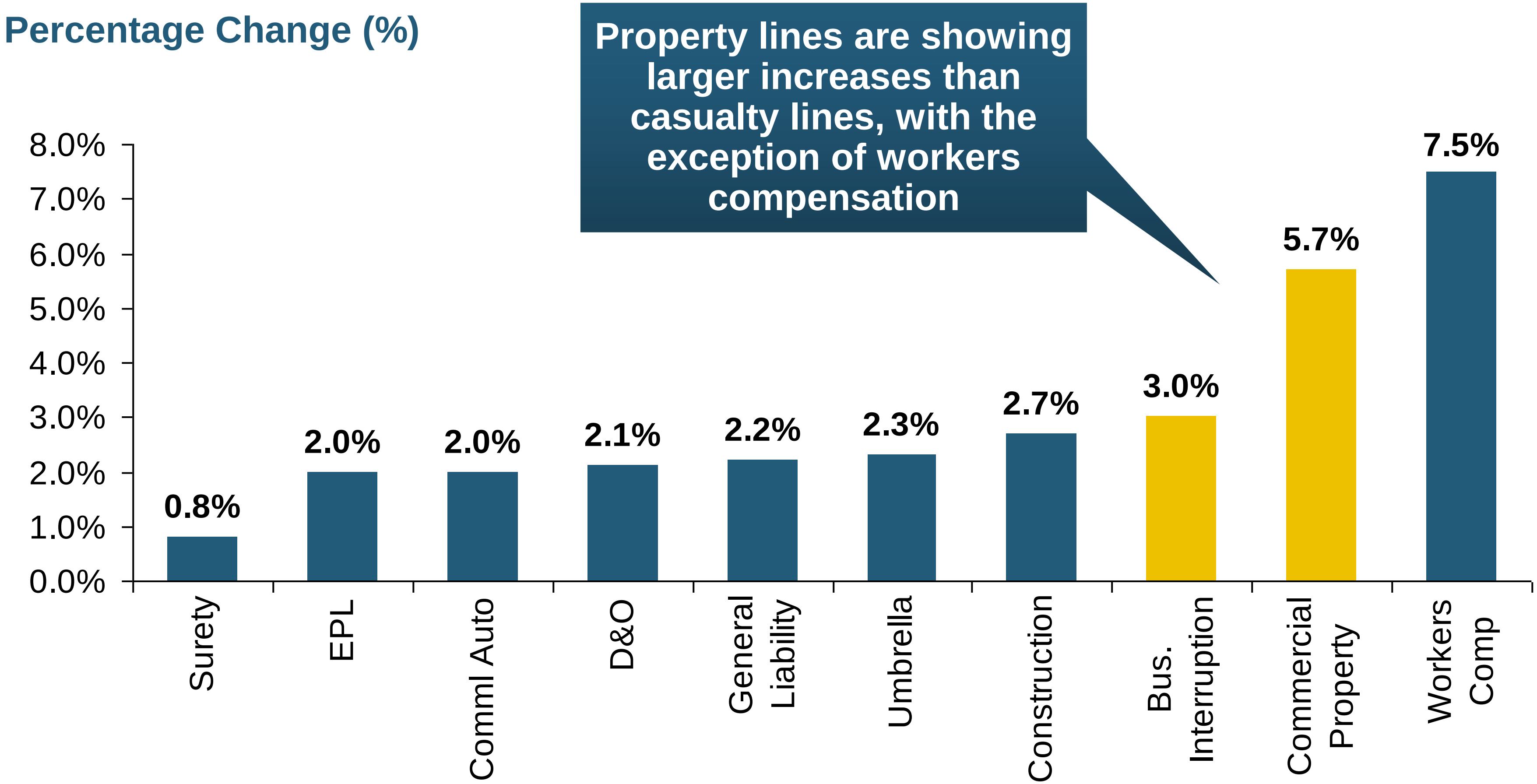
Property lines are showing larger increases than casualty lines, with the exception of workers compensation



Major Commercial Lines Renewed Uniformly Upward in Q4:2011 for Only the Second Time Since 2003; Property Lines & Workers Comp Leading the Way

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

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INVESTMENTS: THE NEW REALITY

How Much of a Threat Are Persistently Low Interest Rates for (Re)Insurers?

Insurers Have Not Yet Fully Adapted to a Persistently Low Interest Rate Environment

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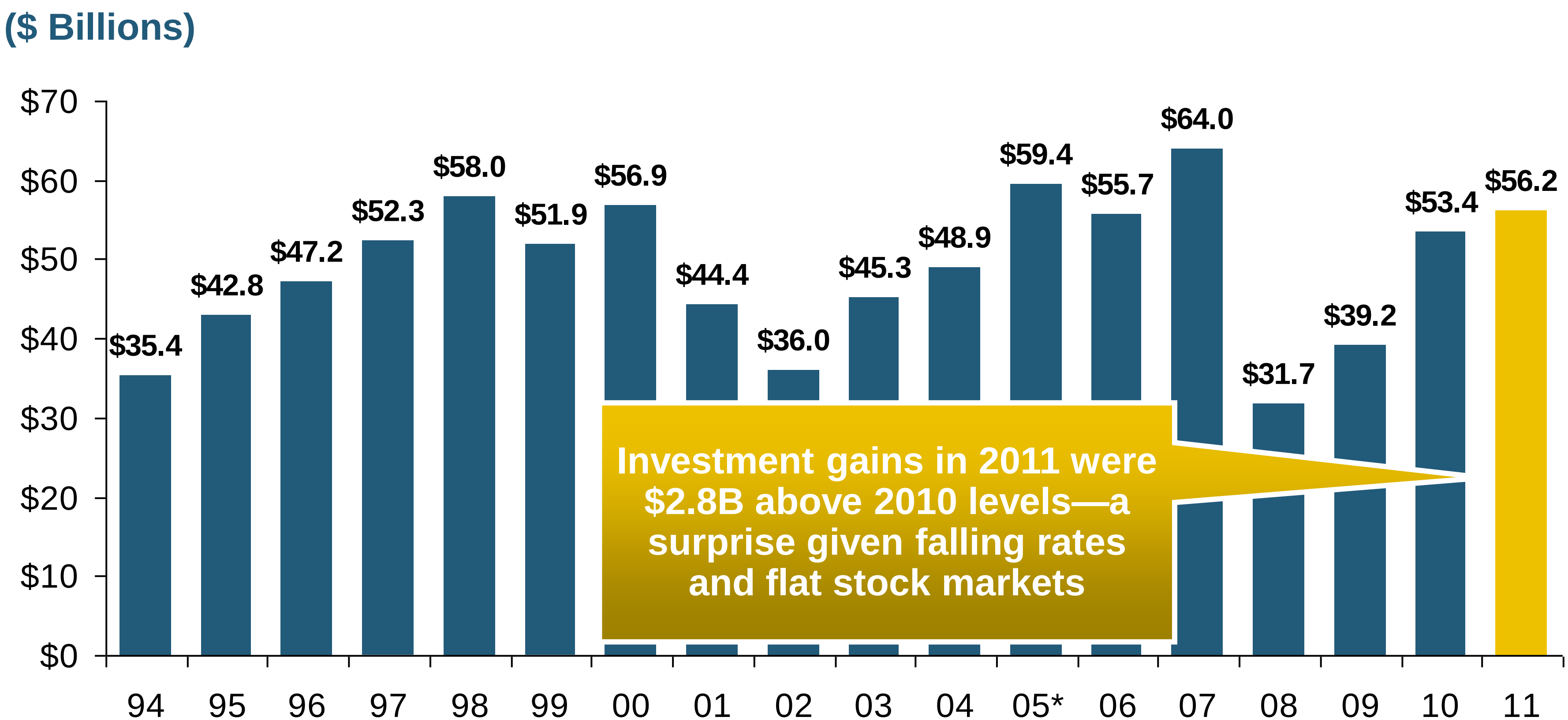
- **No Expectation that Rates Would Be:**
  - **Pushed to Such Low Levels**
  - **Pushed Down so Rapidly**
  - **Held to Such Low Levels for So Long**
  - **Suppressed via Unprecedented Aggressiveness of the Federal Reserve**
    - **Use of traditional and unconventional tools (QE)**
    - **Unconventional 's policies couldn't be anticipated, esp. QE1, 2 (3?)**
- **Competitive Pressure→Protracted Soft Market**
- **Ability to Release Prior Reserves Eases Urgency**
- **Realization of Capital Gains**

Property/Casualty Insurance Industry Investment Income: 2000–2013F[1]

Investment Income in 2011 Was Surprisingly Strong, Though Investment Income Is Likely to Weaken in 2012 Due to Persistently Low Interest Rates

[1] Investment gains consist primarily of interest and stock dividends.
*2012F-201F based on Conning projections.
Sources: ISO; Conning Research & Consulting; Insurance Information Institute.

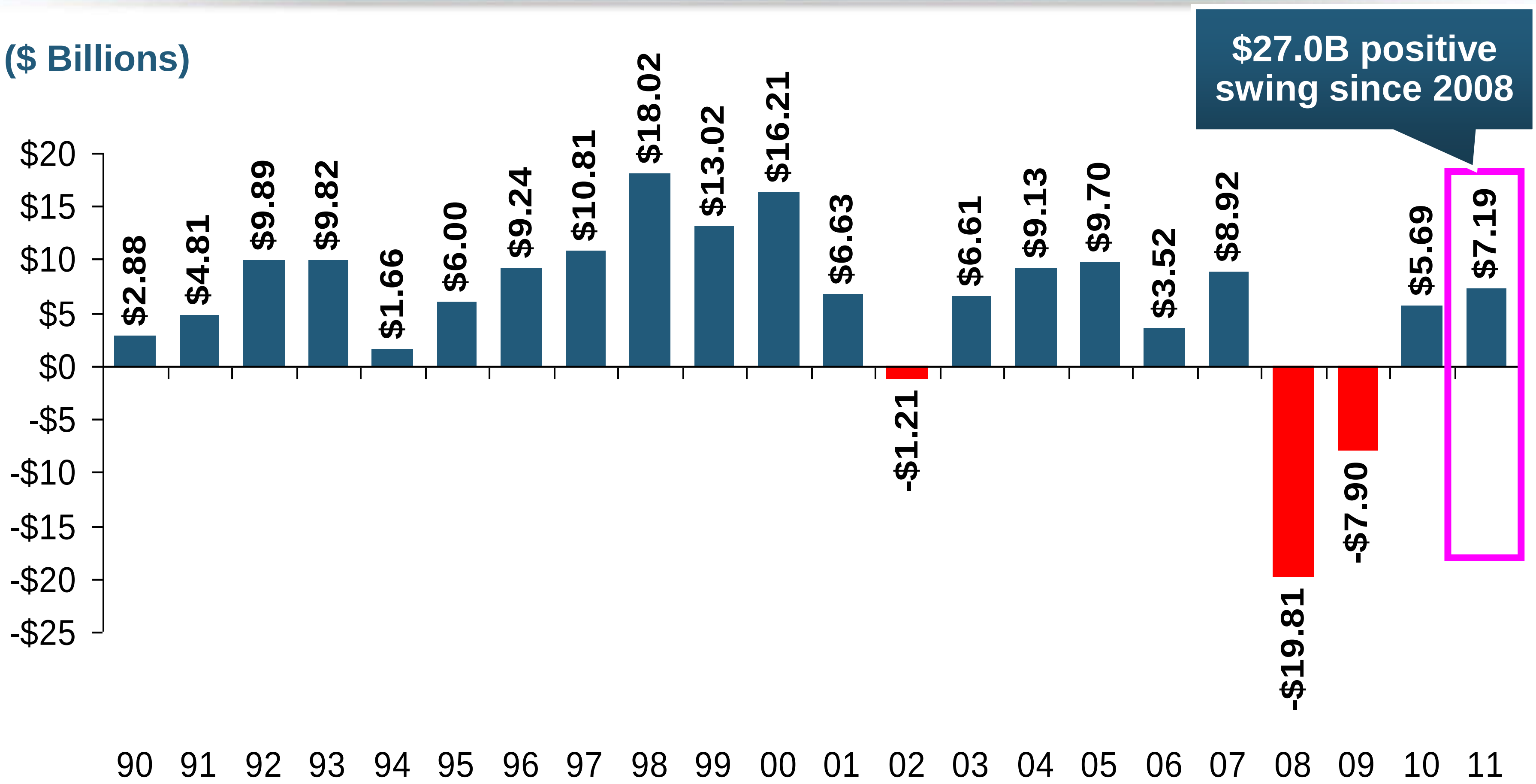
Property/Casualty Insurance Industry Investment Gain: 1994–2011:Q4[1]



Investment Gains in 2011 Were Surprisingly Robust. Investment Gains Recovered Significantly in 2011 Due to Realized Investment Gains; The Financial Crisis Caused Investment Gains to Fall by 50% in 2008

[1] Investment gains consist primarily of interest, stock dividends and realized capital gains and losses.
* 2005 figure includes special one-time dividend of $3.2B.
Sources: ISO; Insurance Information Institute.

P/C Insurer Net Realized Capital Gains/Losses, 1990-2011



Insurers Posted Net Realized Capital Gains in 2010 and 2011 After Following Two Years of Realized Losses During the Financial Crisis. Realized Capital Losses Were the Primary Cause of 2008/2009's Large Drop in Profits and ROE

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

U.S. 10-Year Treasury Note Yields: A Long Downward Trend, 1990–2012*

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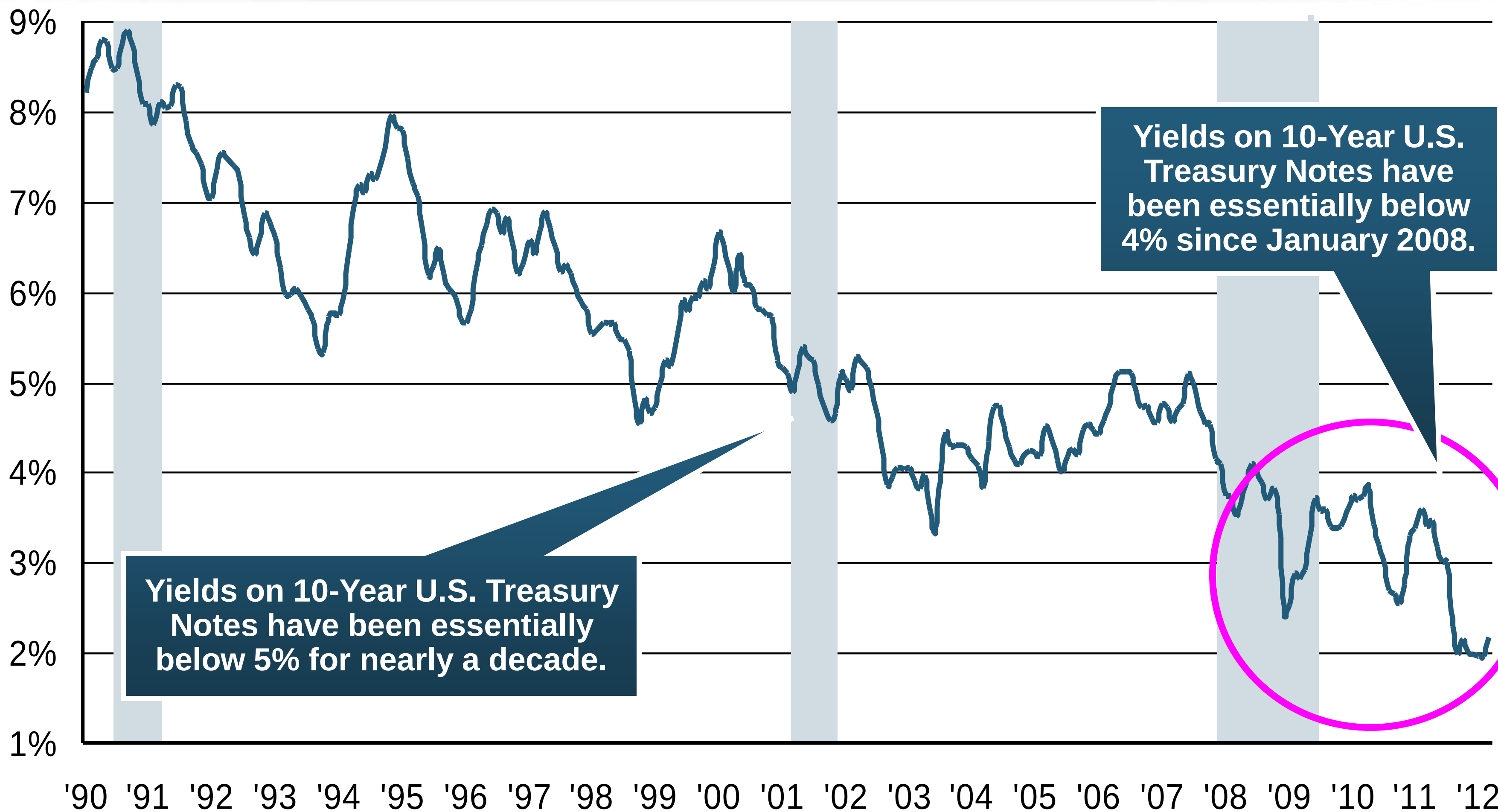

Since roughly 80% of P/C bond/cash investments are in 10-year or shorter durations, most P/C insurer portfolios will have low-yielding bonds for years to come.

*Monthly, through March 2012. Note: Recessions indicated by gray shaded columns.

Sources: Federal Reserve Bank at http://www.federalreserve.gov/releases/h15/data/Monthly/H15_TCMNOM_Y10.txt
National Bureau of Economic Research (recession dates); Insurance Information Institutes.

Treasury Yield Curves: Pre-Crisis (July 2007) vs. Mar. 2012

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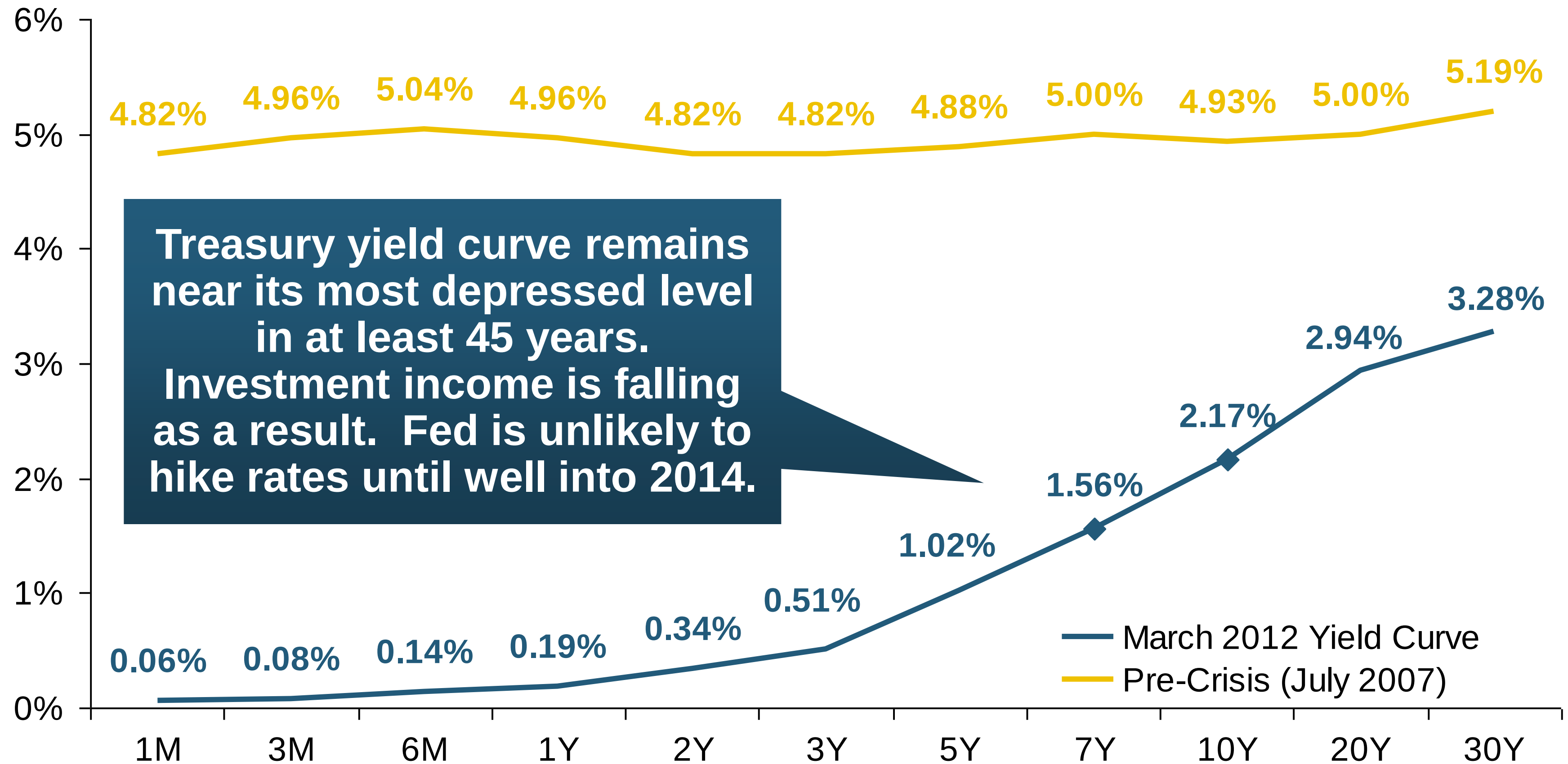
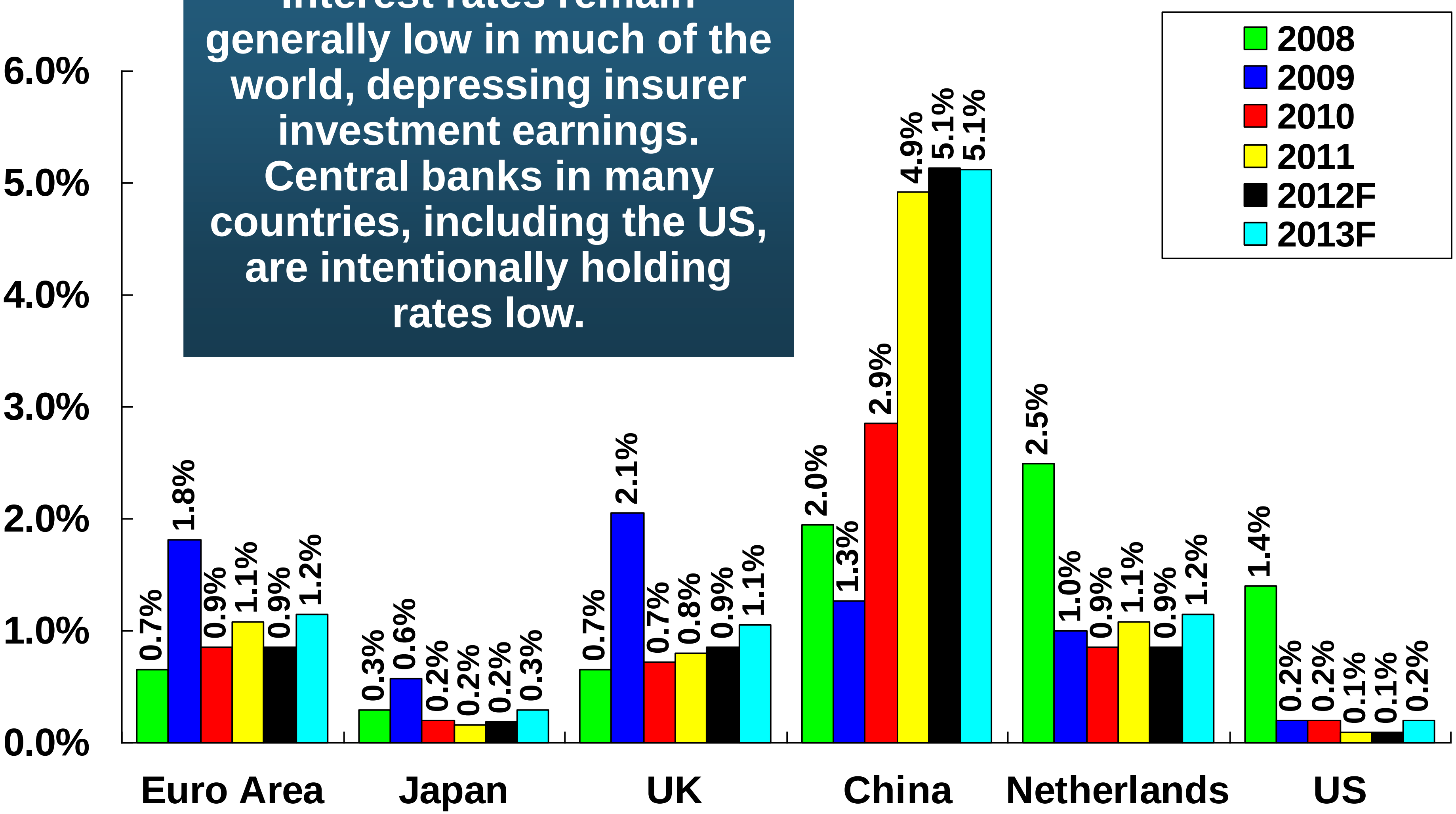


The Fed Is Actively Signaling that it Is Determined to Keep Rates Low Through Late 2014

Source: Federal Reserve Board of Governors; Insurance Information Institute.

3-Month Interest Rates for Major Global Economies, 2008-2013F

Interest rates remain generally low in much of the world, depressing insurer investment earnings. Central banks in many countries, including the US, are intentionally holding rates low.



Source: Blue Chip Economic Indicators, Apr. 2012 edition.

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

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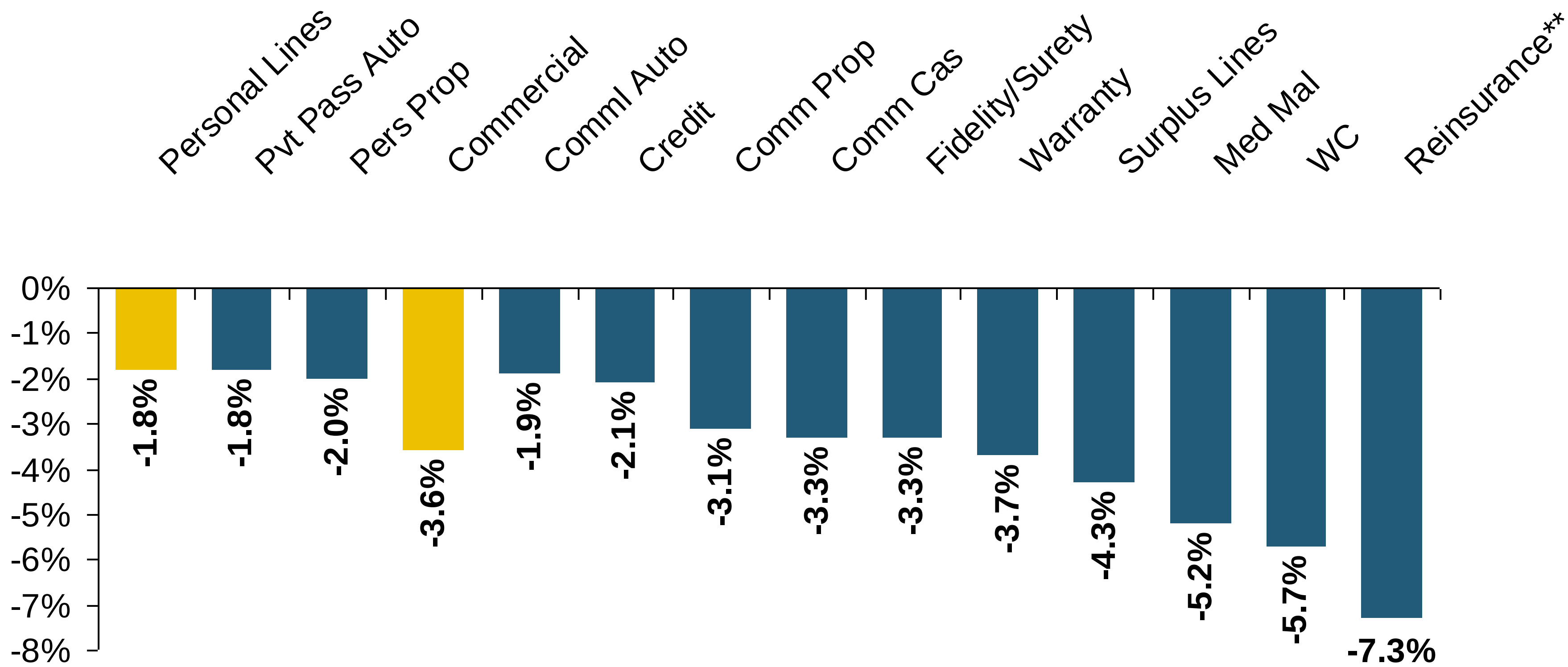

Lower Investment Earnings Place a Greater Burden on Underwriting and Pricing Discipline

*Based on 2008 Invested Assets and Earned Premiums

**US domestic reinsurance only

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

Insurance Information Institute Online:

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Thank you for your time and your attention!

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