Mega-Trends Influencing the Future of Auto Insurance

National Auto Insurance ExecuSummit
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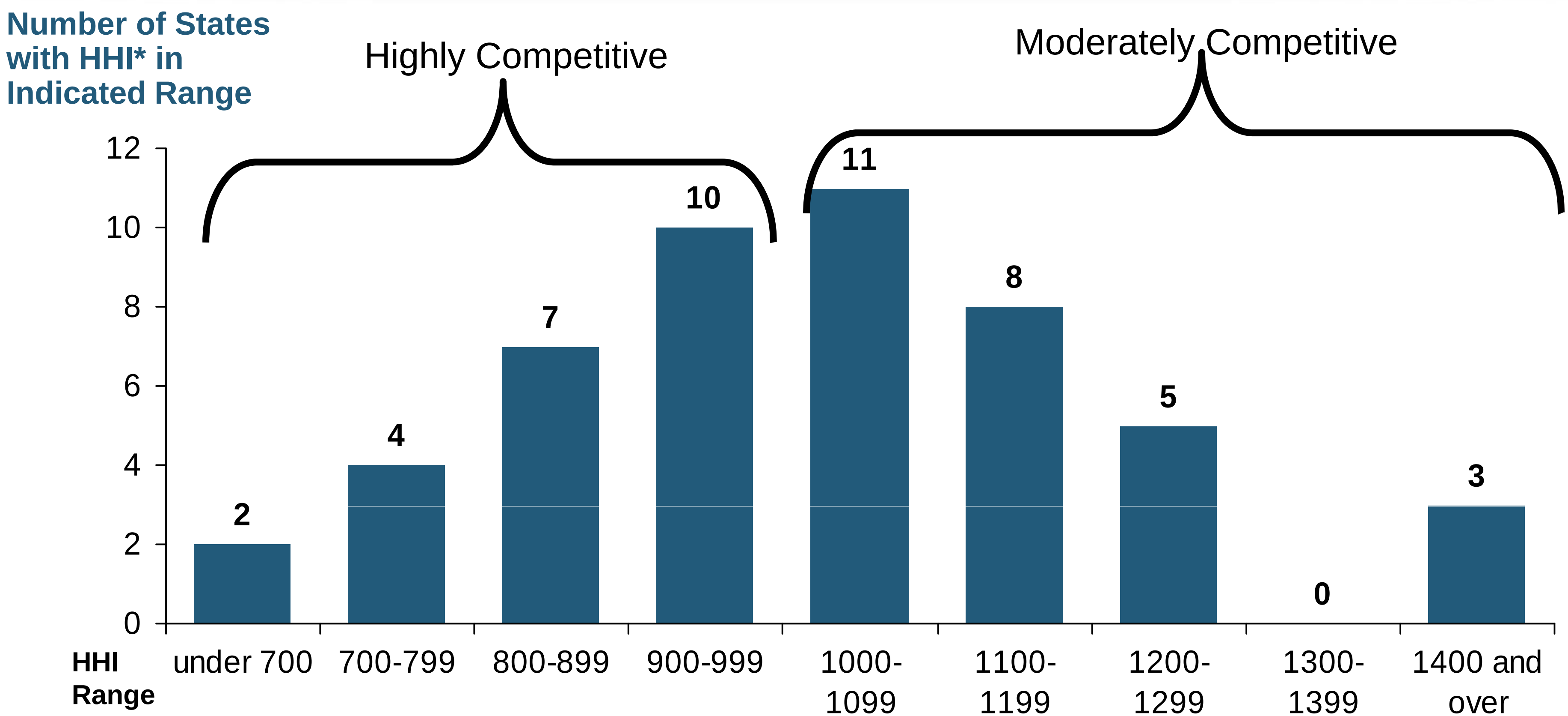
Competition in the Auto Insurance Market

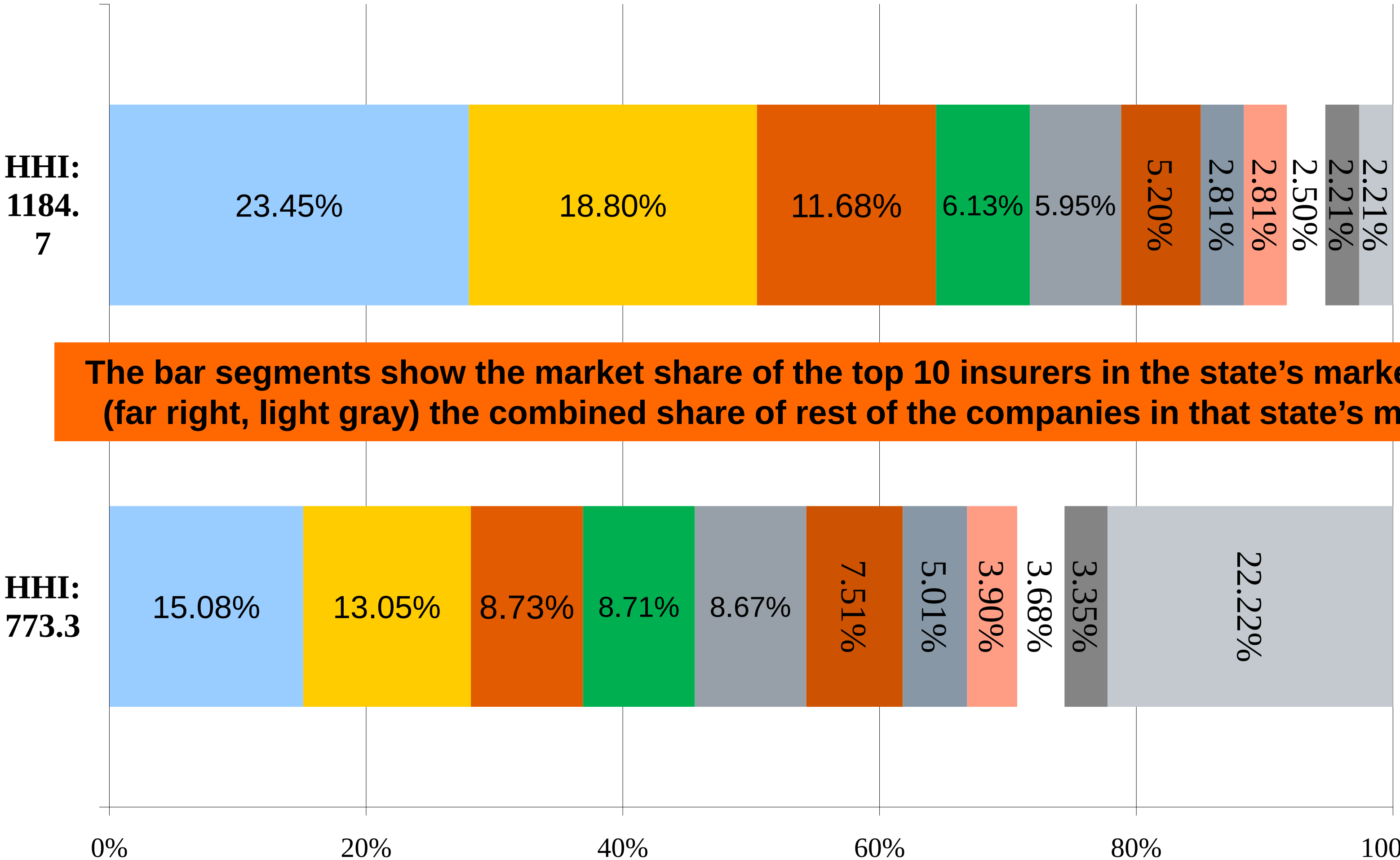
In Many States, the PP Auto Market in 2009 was Highly Competitive



An HHI Under 1000 is Generally Considered a Highly Competitive Market; HHIs Between 1000 and 1800 Indicate a Moderately Competitive Market; Over 1800 Suggests a Concentrated Market

*Herfindahl-Hirschman Index, a standard measure of market concentration
Sources: Insurance Information Institute research from SNL Financial.

What HHIs of 775 and 1200 Look Like

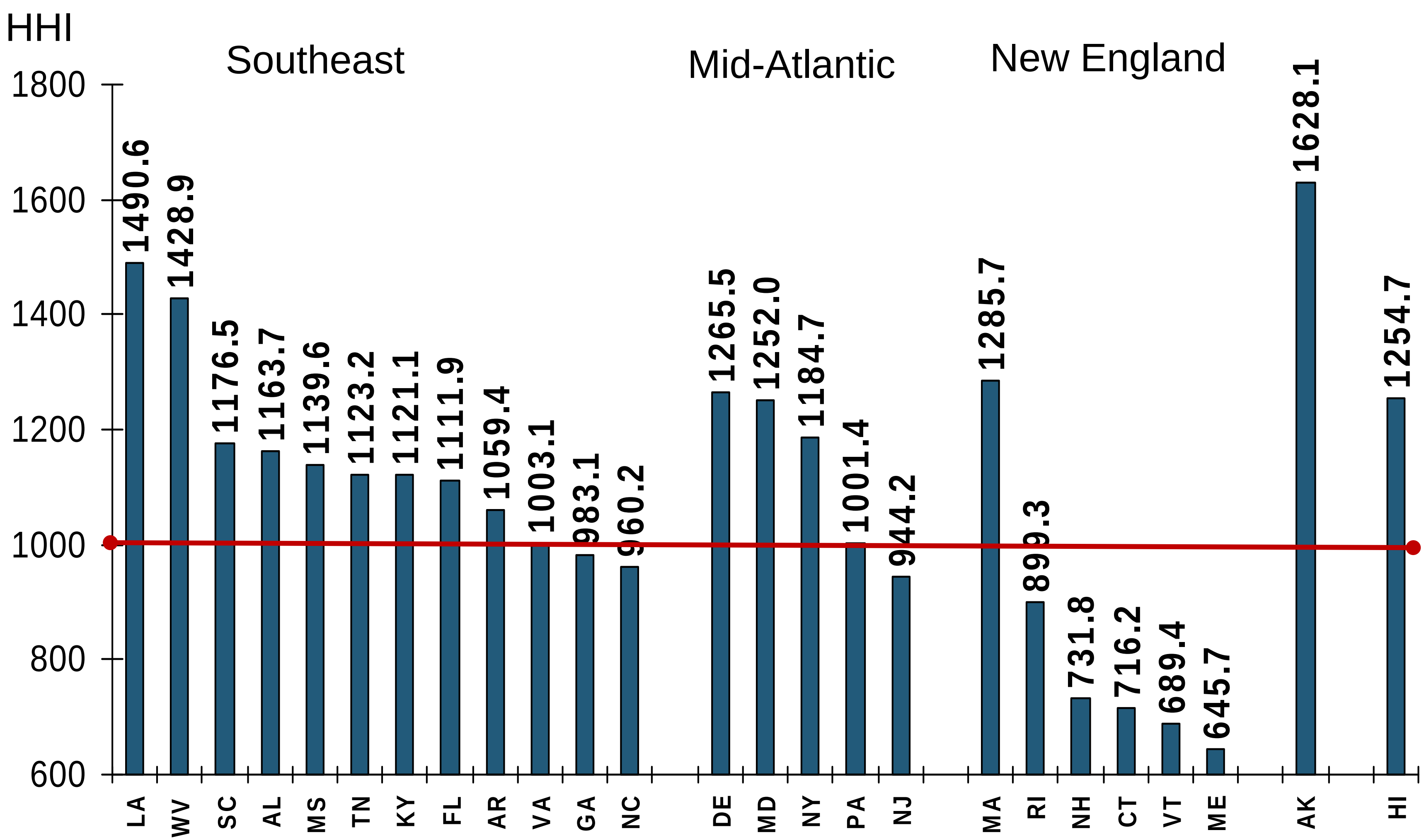


The bar segments show the market share of the top 10 insurers in the state's market plus (far right, light gray) the combined share of rest of the companies in that state's market

In the Highly Competitive Market, The Top 10 Carriers Have 77.8% Market Share; In the Moderately Competitive Market, the Top 10 Have 97.8%

Sources: SNL Financial; Insurance Information Institute

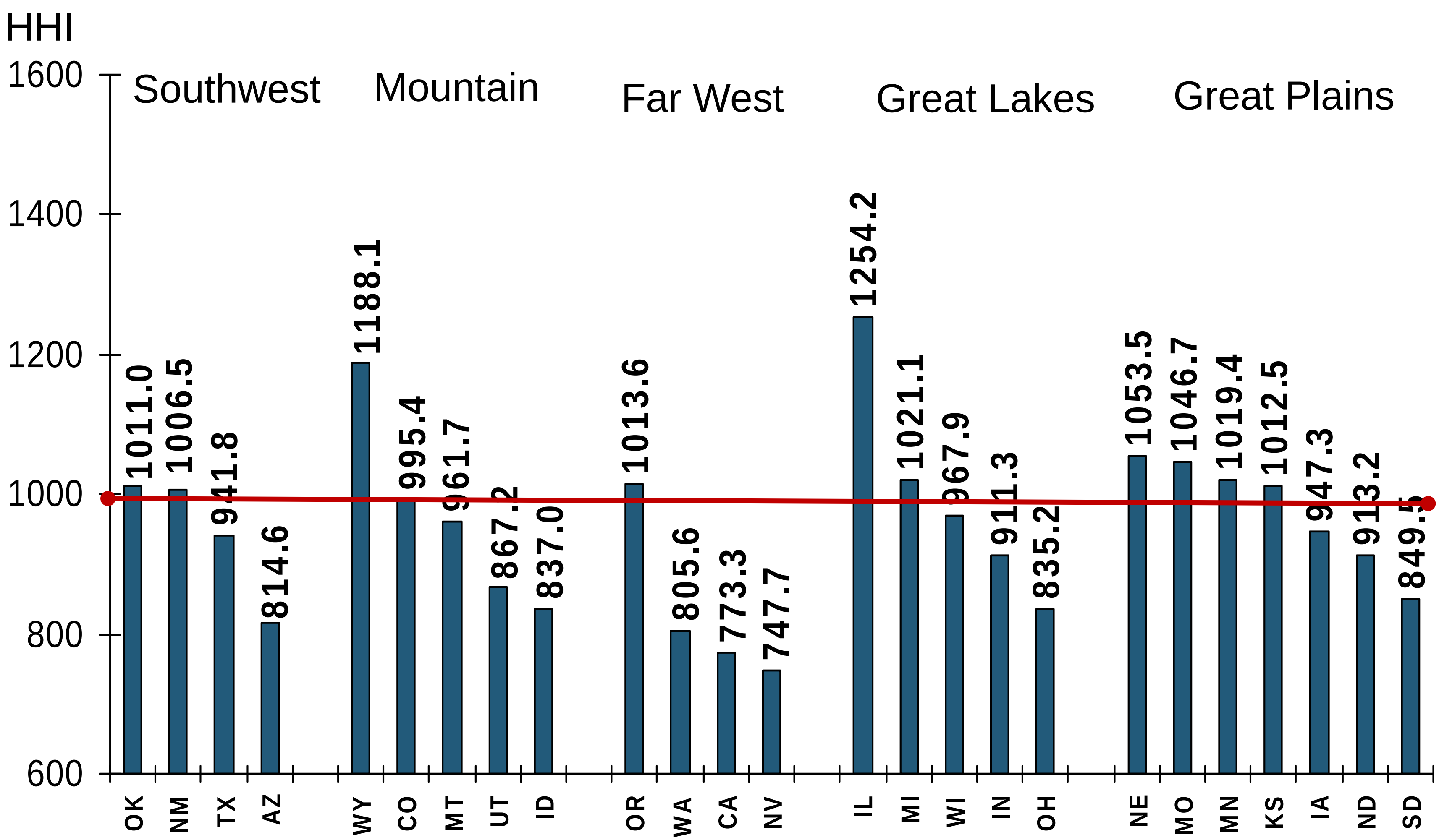
PP Auto Competitive Environment Varies by State and Region*



*Data for 2009

Sources: SNL Financial; Insurance Information Institute.

PP Auto Competitive Environment Varies by State and Region* (cont'd)

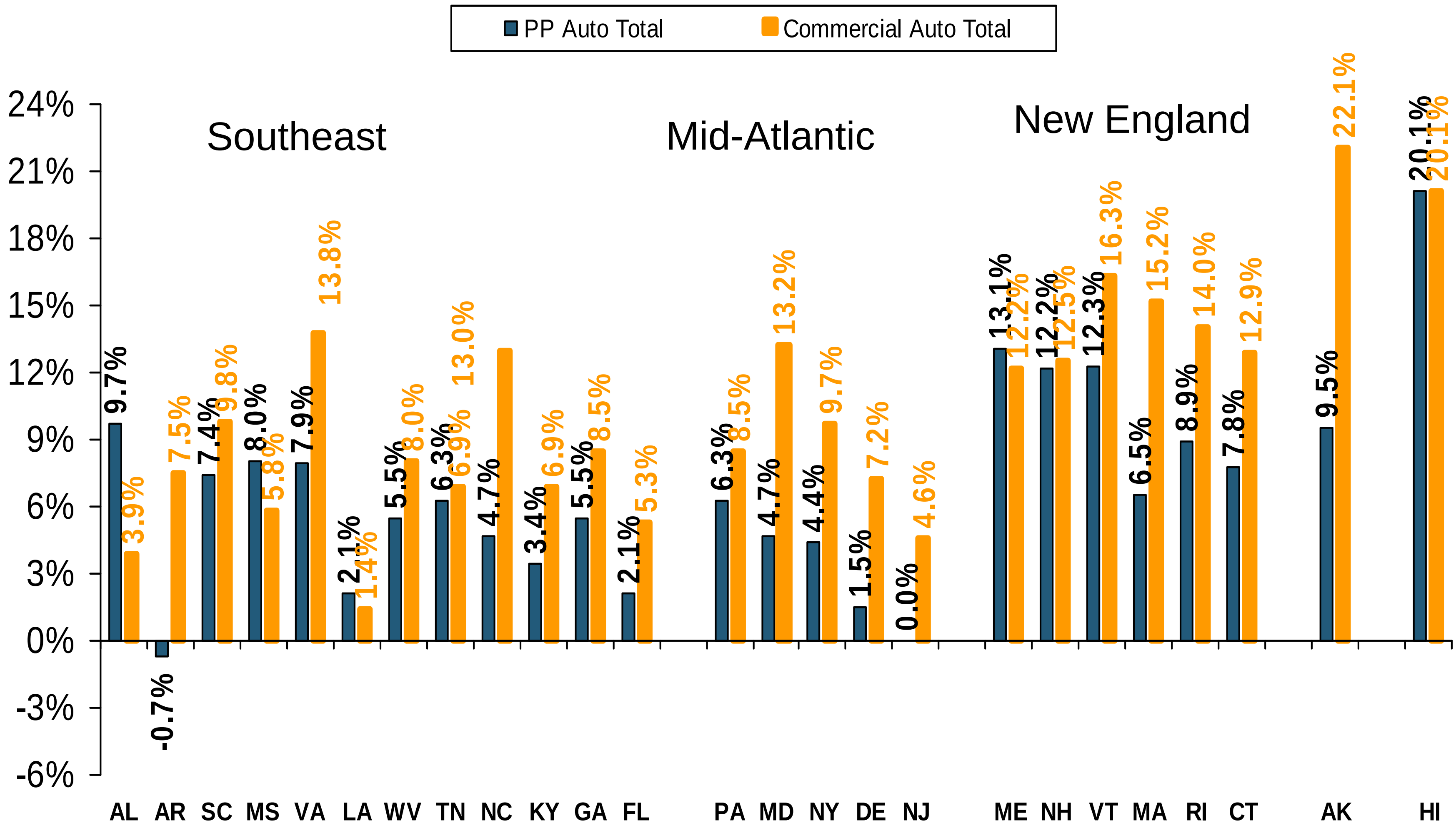


*Data for 2009

Sources: SNL Financial; Insurance Information Institute.

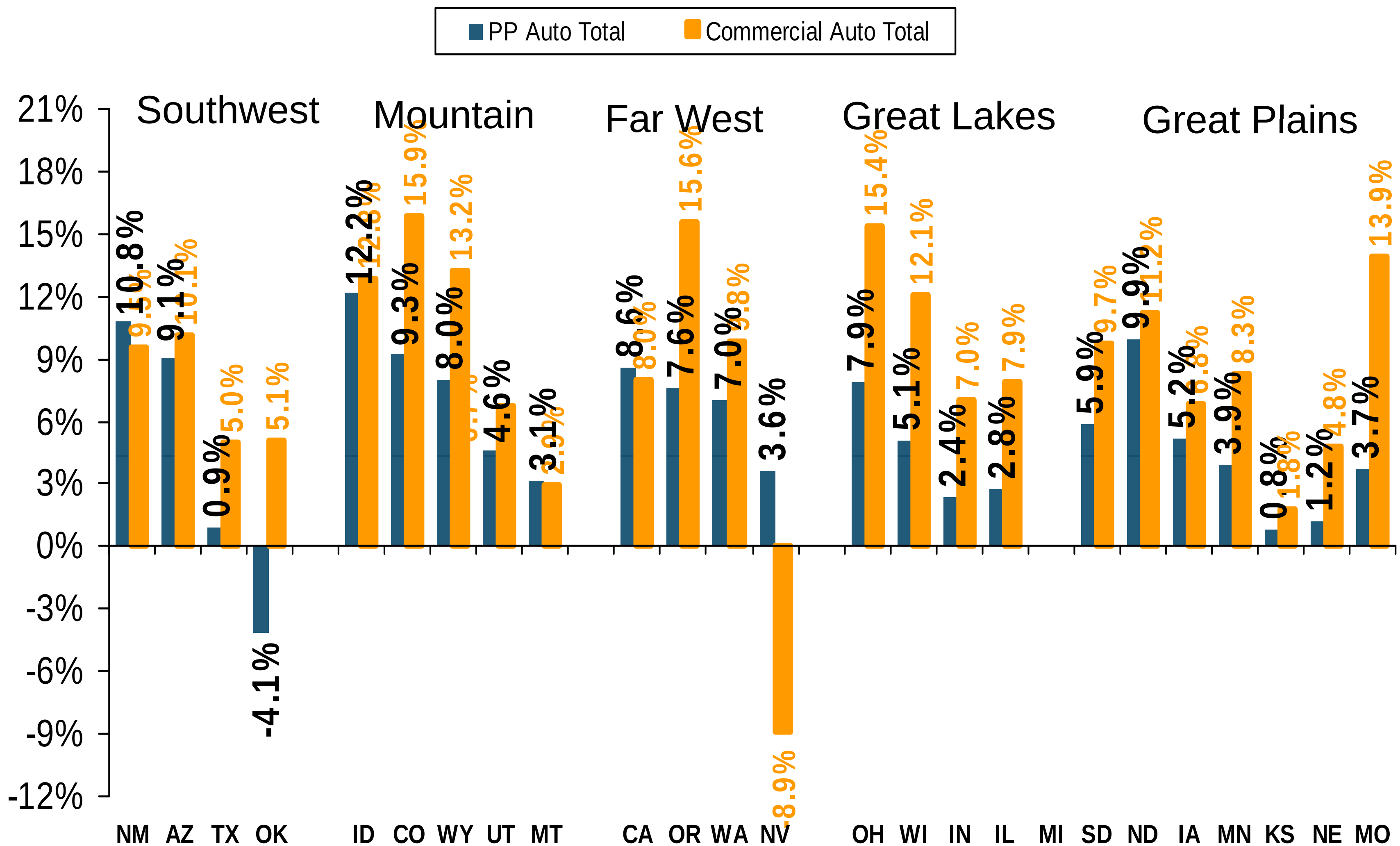
Profitability in the Auto Insurance Market

Auto Insurance Return on Net Worth, 2008, Varies by Line, State and Region



Sources: NAIC Report on Profitability by Line by State in 2008, pp. 103-104, 109-110; Insurance Information Institute.

Auto Insurance Return on Net Worth, 2008, Varies by Line, State and Region

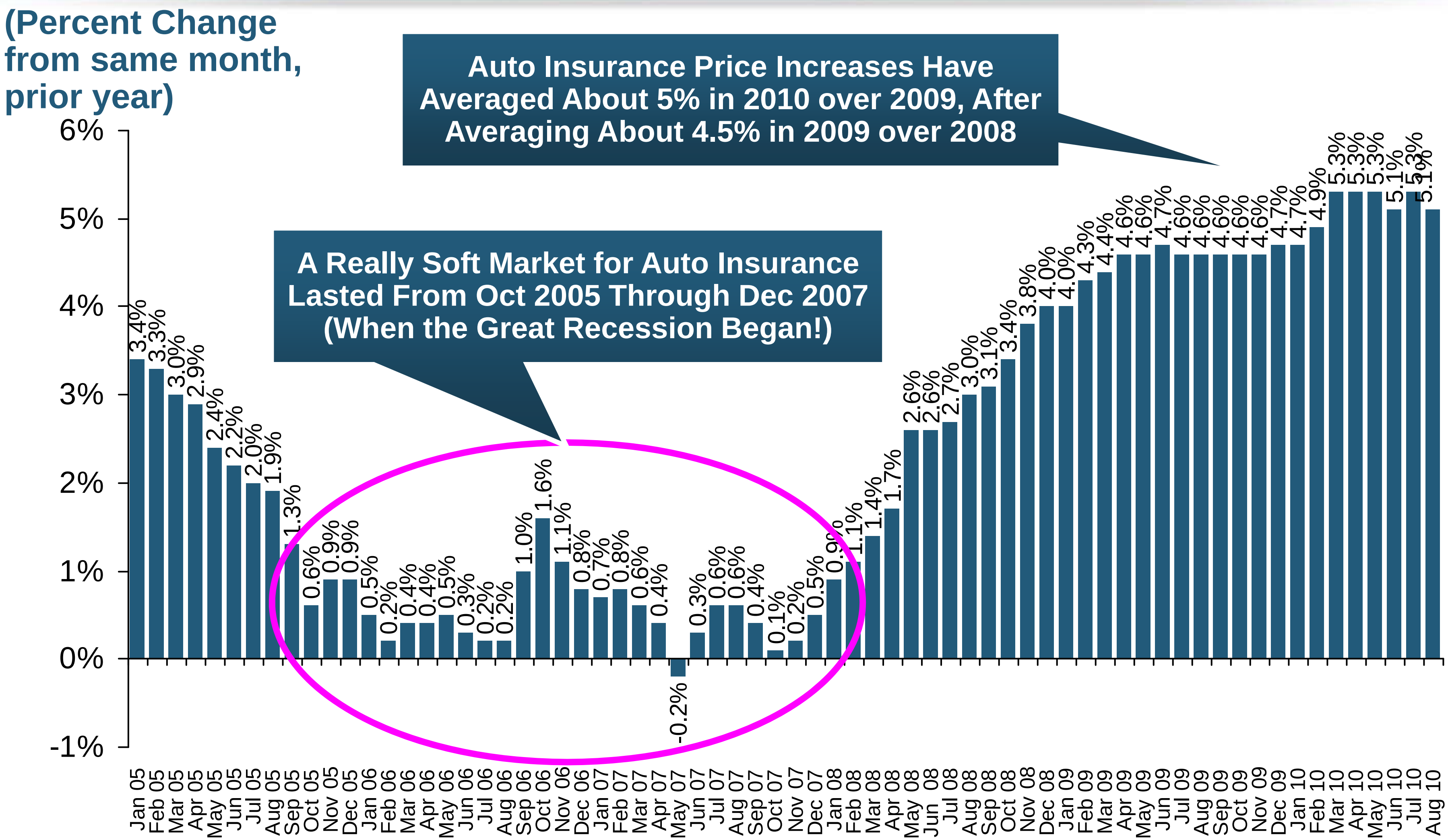


Sources: NAIC Report on Profitability by Line by State in 2008, pp. 103-104, 109-110; Insurance Information Institute.

Premium Growth Trends in Auto Insurance

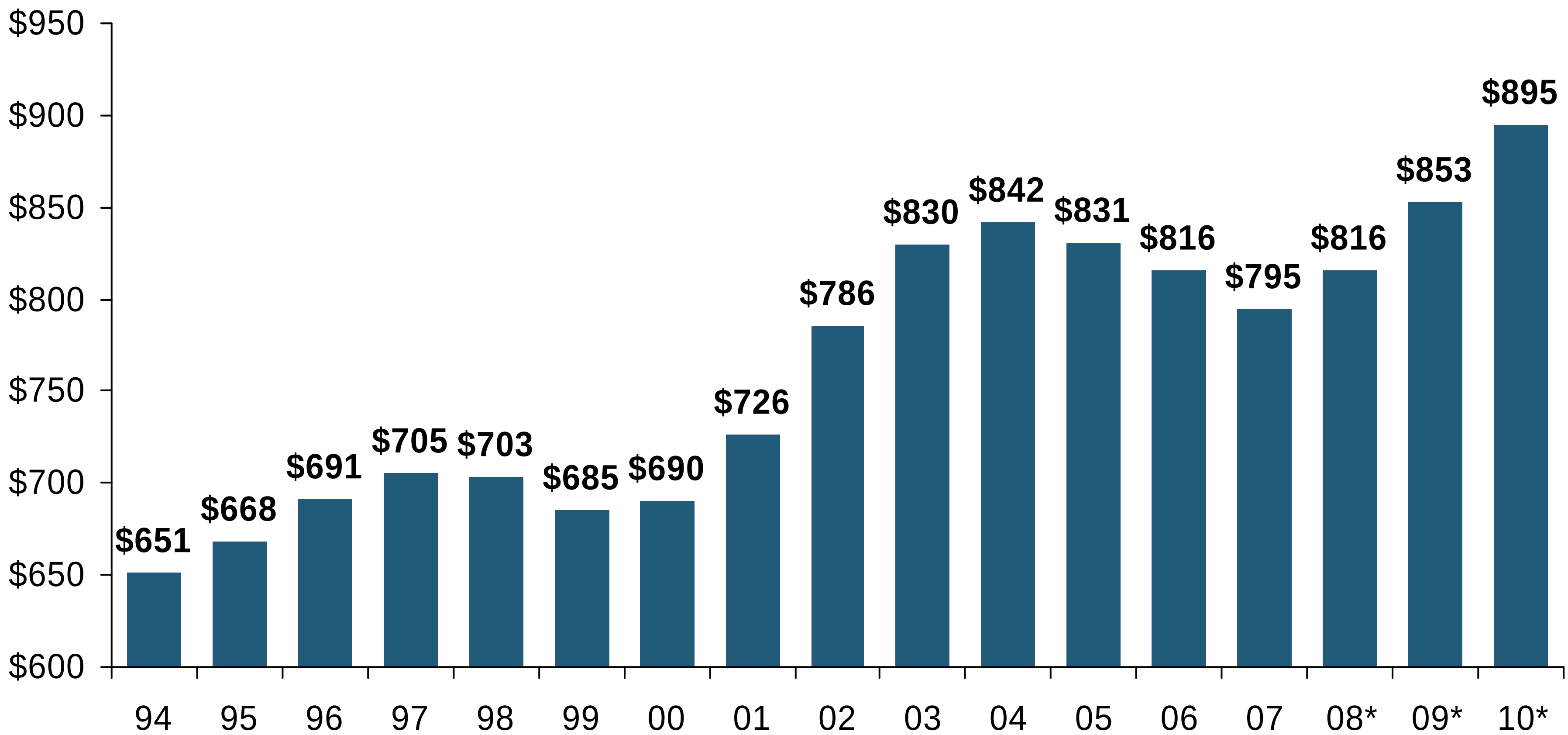
They're Not In Sync With the Economy

Monthly Change* in Auto Insurance Prices, 2005-2010



*Percentage change from same month in prior year, seasonally adjusted.
Sources: US Bureau of Labor Statistics; Insurance Information Institute

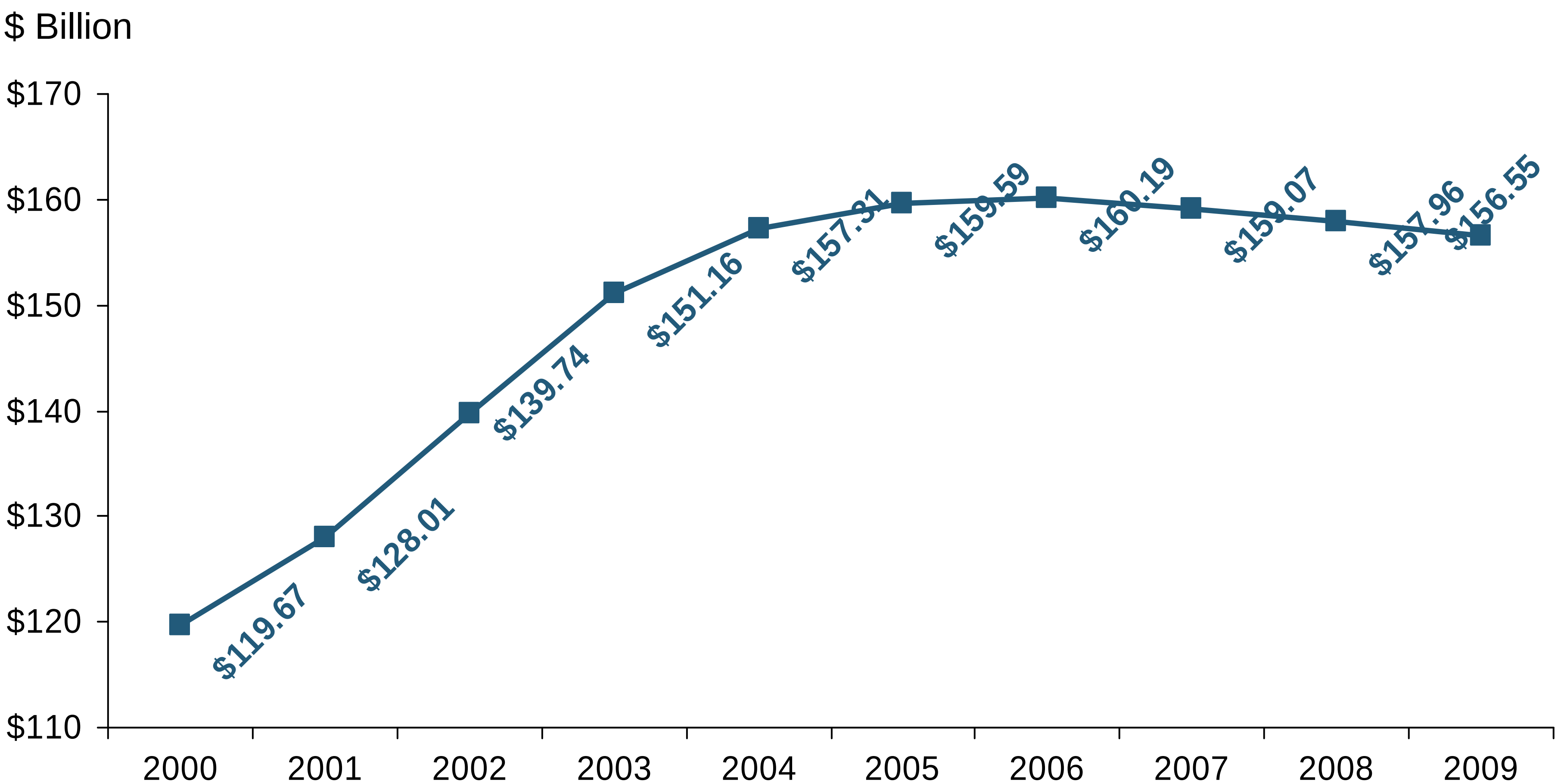
Average Expenditures on Auto Insurance



Countrywide Auto Insurance Expenditures Increased 2.6% in 2008 and 4.5% Pace in 2009 (est.) and 5% in 2010 (est.)

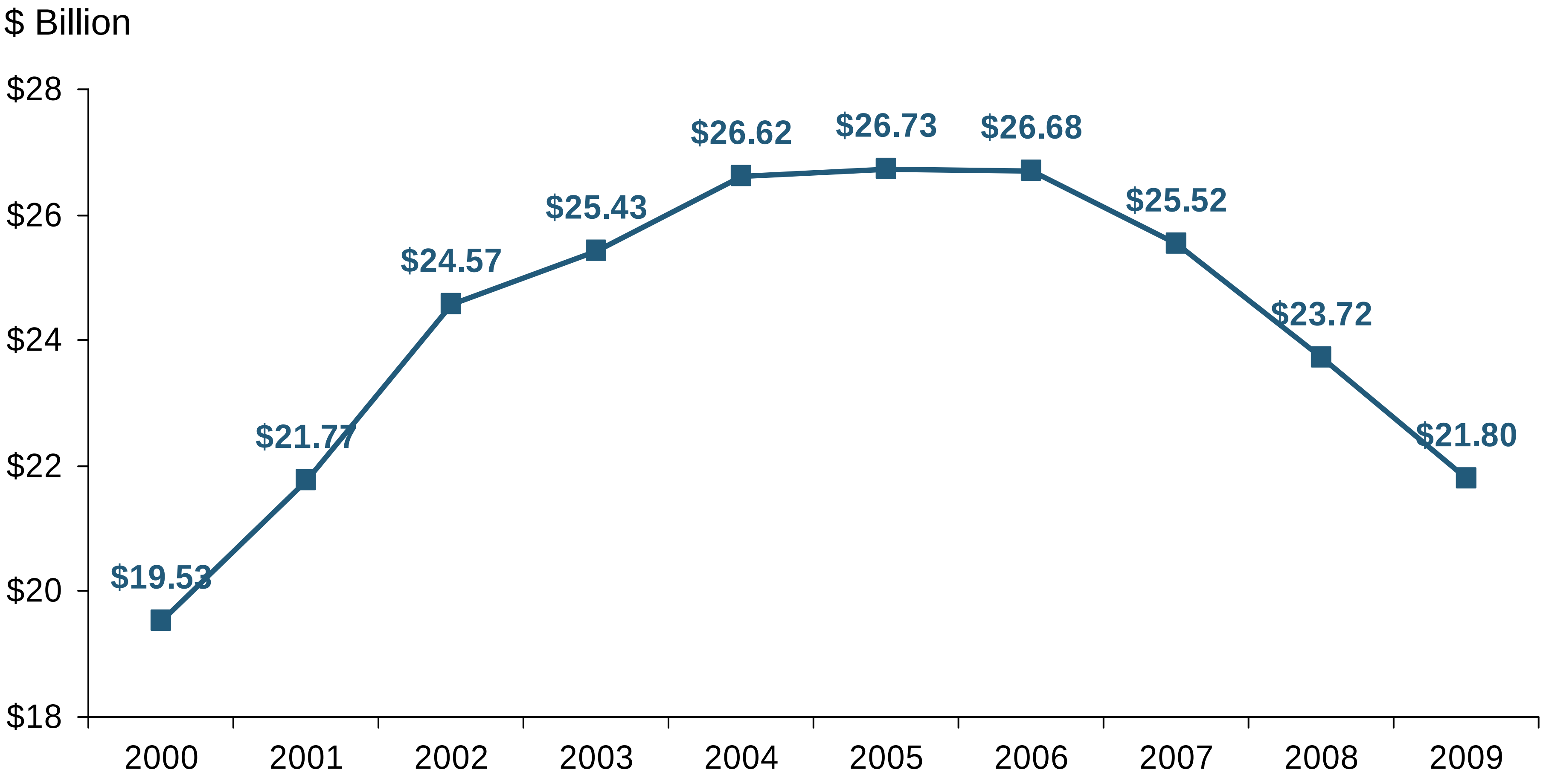
* Insurance Information Institute Estimates/Forecasts
Sources: NAIC, Insurance Information Institute estimates 2008-2010 based on CPI data for Auto Insurance.

Private Passenger Auto Insurance Net Written Premium, 2000–2009



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

Commercial Auto Insurance Net Written Premium, 2000–2009



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

Exposure Drivers in Auto Insurance

Registered Passenger Cars and Other 2-axle, 4-tire Vehicles

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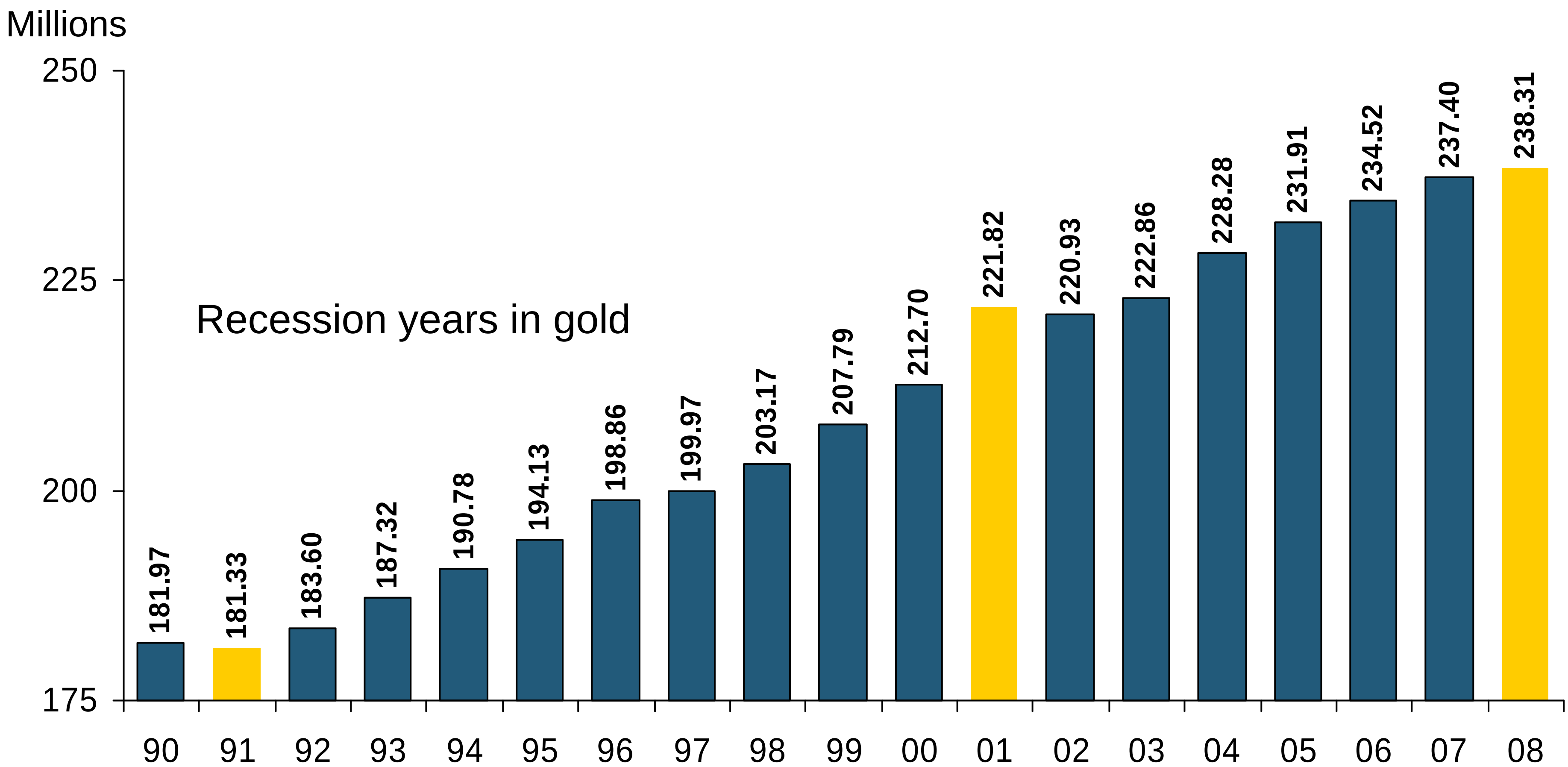
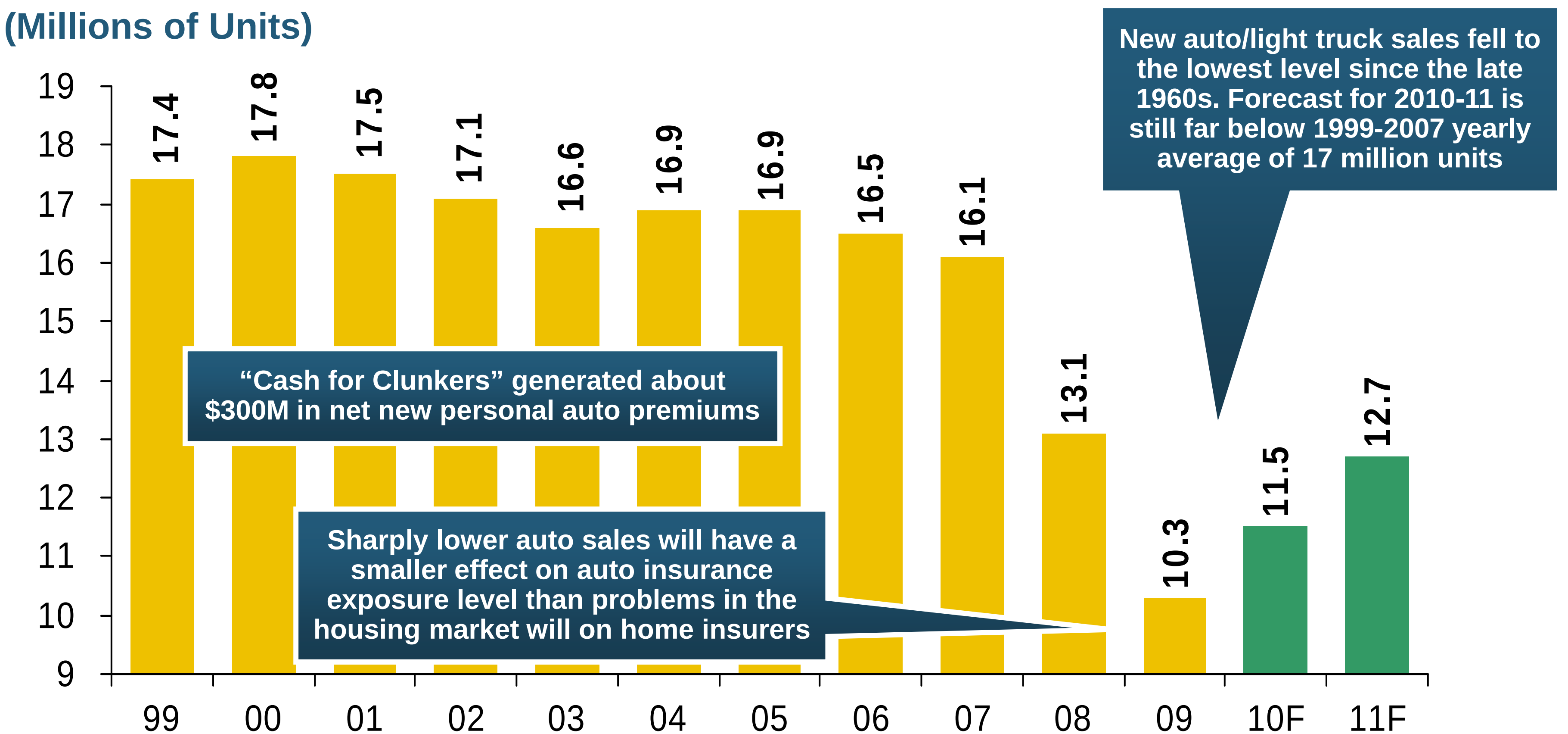


It is likely that the number of vehicles dropped during and following the "Great Recession." Recovery depends on employment and lending trends.

Sources: http://www.bts.gov/publications/national_transportation_statistics/html/table_01_11.html
Insurance Information Institute

Auto/Light Truck Sales, 1999-2011F



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

Source: U.S. Department of Commerce; Blue Chip Economic Indicators (9/10); Insurance Information Institute.

Miles Driven*, 1990–2010**

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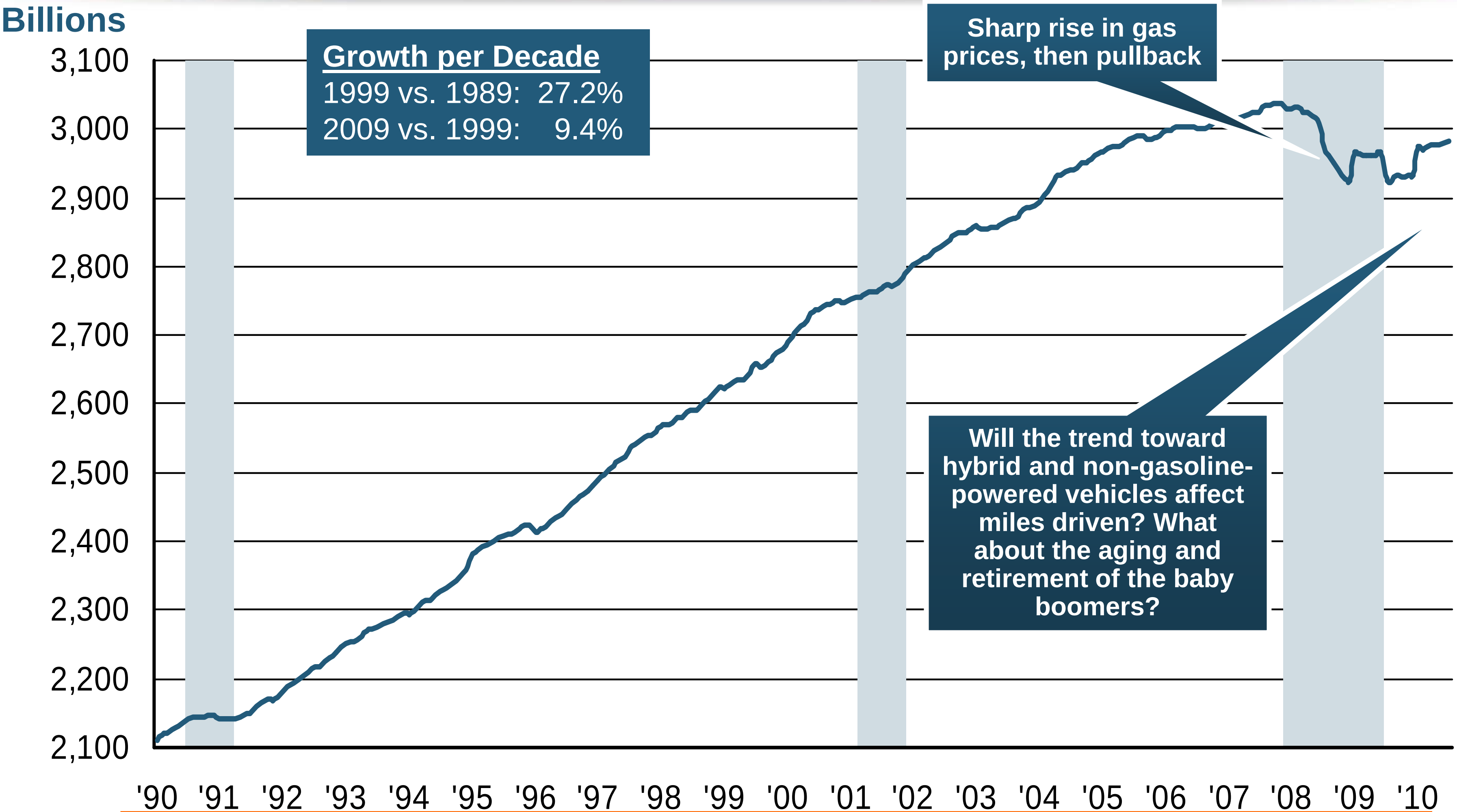

Two of the past three recessions temporarily slowed the rise in miles driven.

*Moving 12-month total **Most recent month is July 2010. Note: Recessions indicated by gray shaded columns.

Sources: Federal Highway Administration (http://www.fhwa.dot.gov/ohim/tvtw/tvtpage.cfm);
National Bureau of Economic Research (recession dates); Insurance Information Institute.

Do Changes in Miles Driven Affect Auto Collision Claim Frequency? No.

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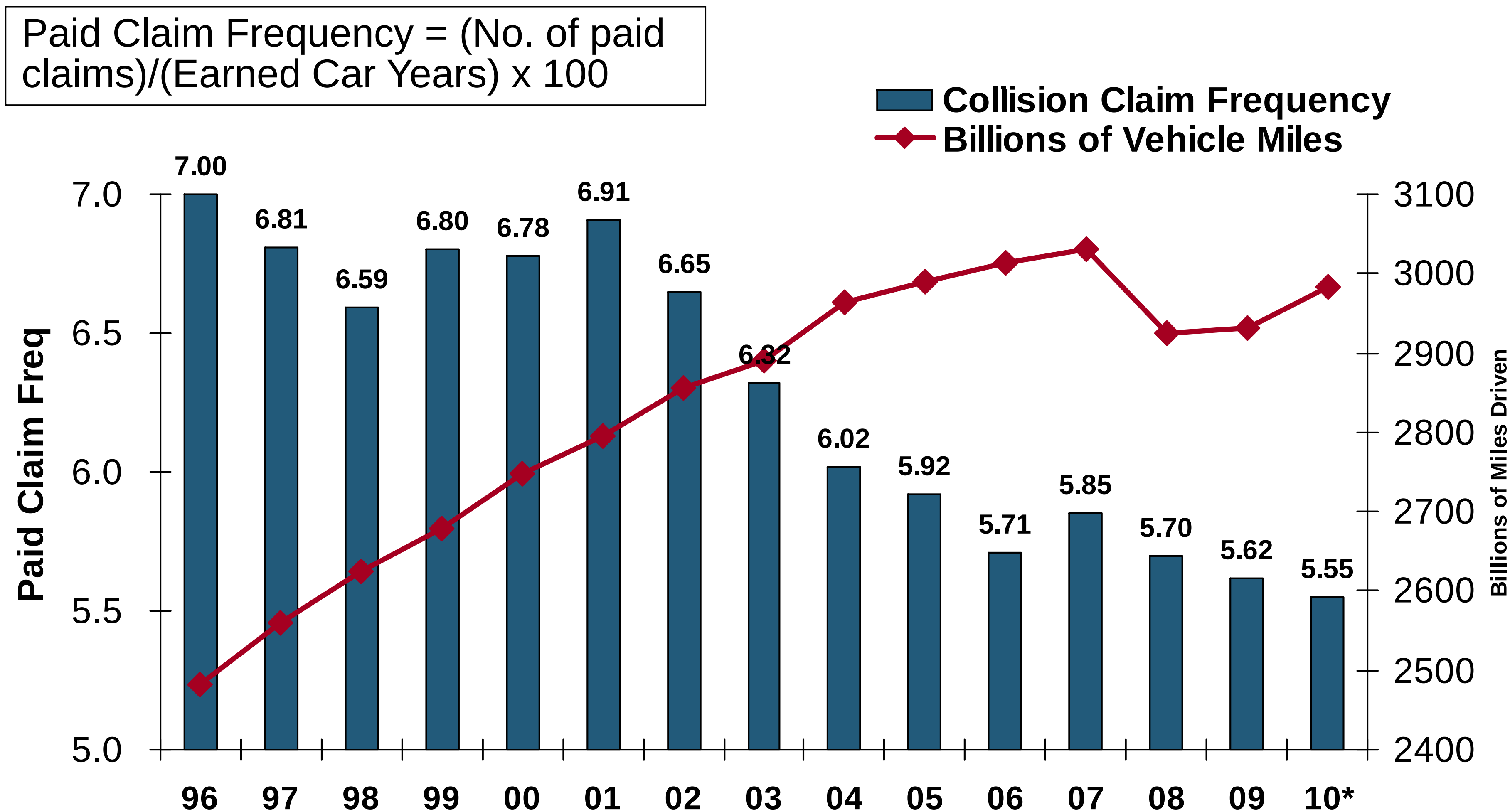


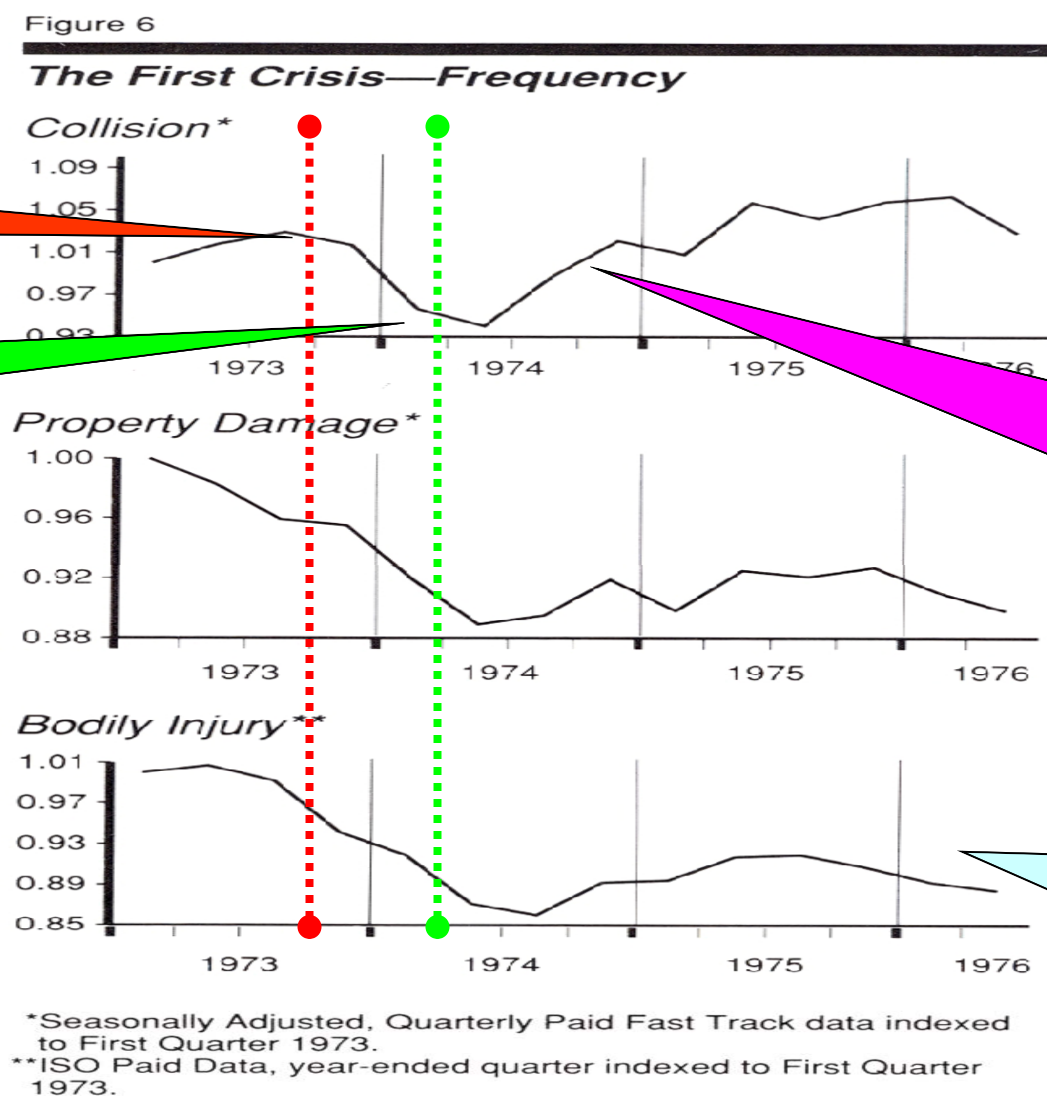
Sources: Federal Highway Administration (http://www.fhwa.dot.gov/ohim/tvtw/09dectvt/page2.cfm; ISO Fast Track Monitoring System, *Private Passenger Automobile Fast Track Data*: 2nd Qtr. 2010, published Sep. 30, 2010 and earlier reports. *2010 FHWA and ISO figures are for 12 months ending 6/30/2010.

Auto Insurance: Claim Frequency Impacts of Energy Crisis/Recession of 1973/74

Oct. 17, 1973: Arab oil embargo begins

March 17, 1974: Arab oil states announce end to embargo

Driving Stats
- Gas prices rose 35-40%
- Miles driven fell 6.7% in 1974



Frequency Effects of the Embargo:
Collision: -7.7%
PD: -9.5%
BI: -13.3%

Collision frequency began to rebound almost immediately after the embargo ended and reached pre-embargo levels within 9 months

Liability claim frequency remained below pre-embargo levels for 2 years

Source: ISO, US DOT.

Auto Insurance: Claim Severity Impacts of Energy Crisis/Recession of 1973/74

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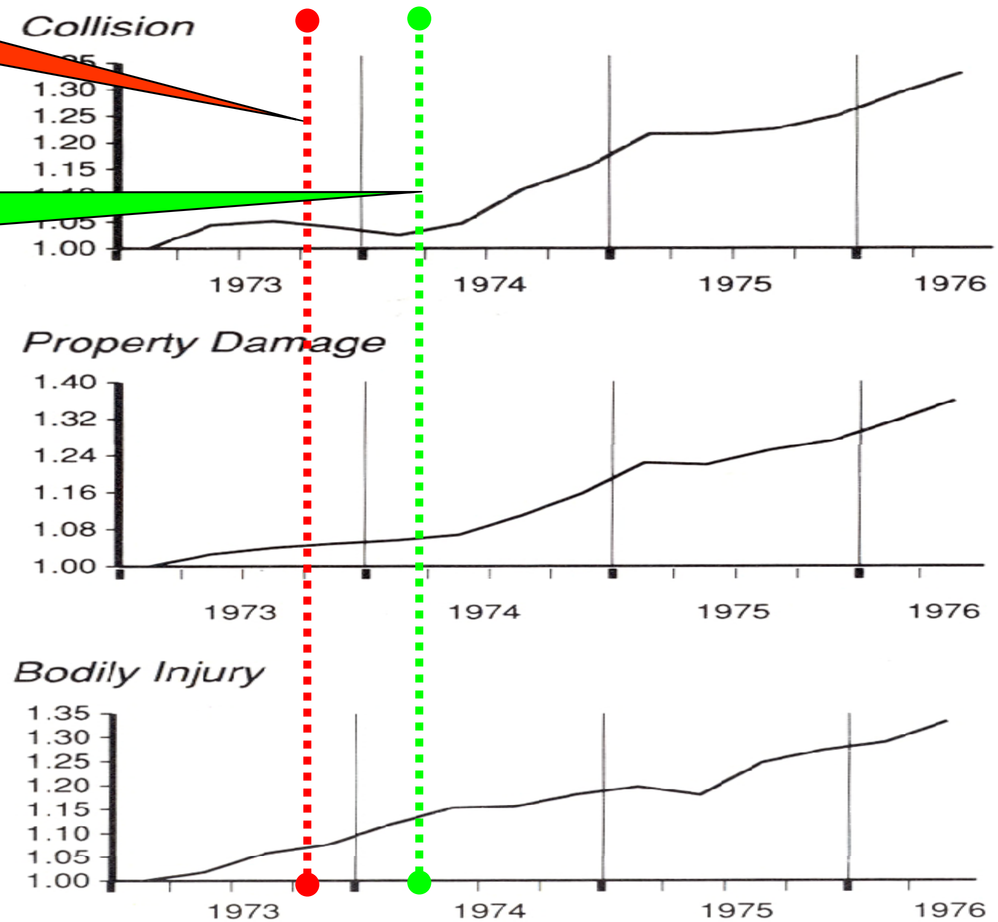
Oct. 17, 1973: Arab oil embargo begins

March 17, 1974: Arab oil states announce end to embargo

Driving Stats
- **Gas prices rose 35-40%**
- **Miles driven fell 6.7% in 1974**

Figure 7

The First Crisis—Severity*



*Seasonally Adjusted, Quarterly Paid Fast Track data indexed to First Quarter 1973.

Severity Effects of the Embargo
Collision: -7.5%
PD: +15.9%
BI: N/A*

Collision severity began to rebound almost immediately after the embargo ended;

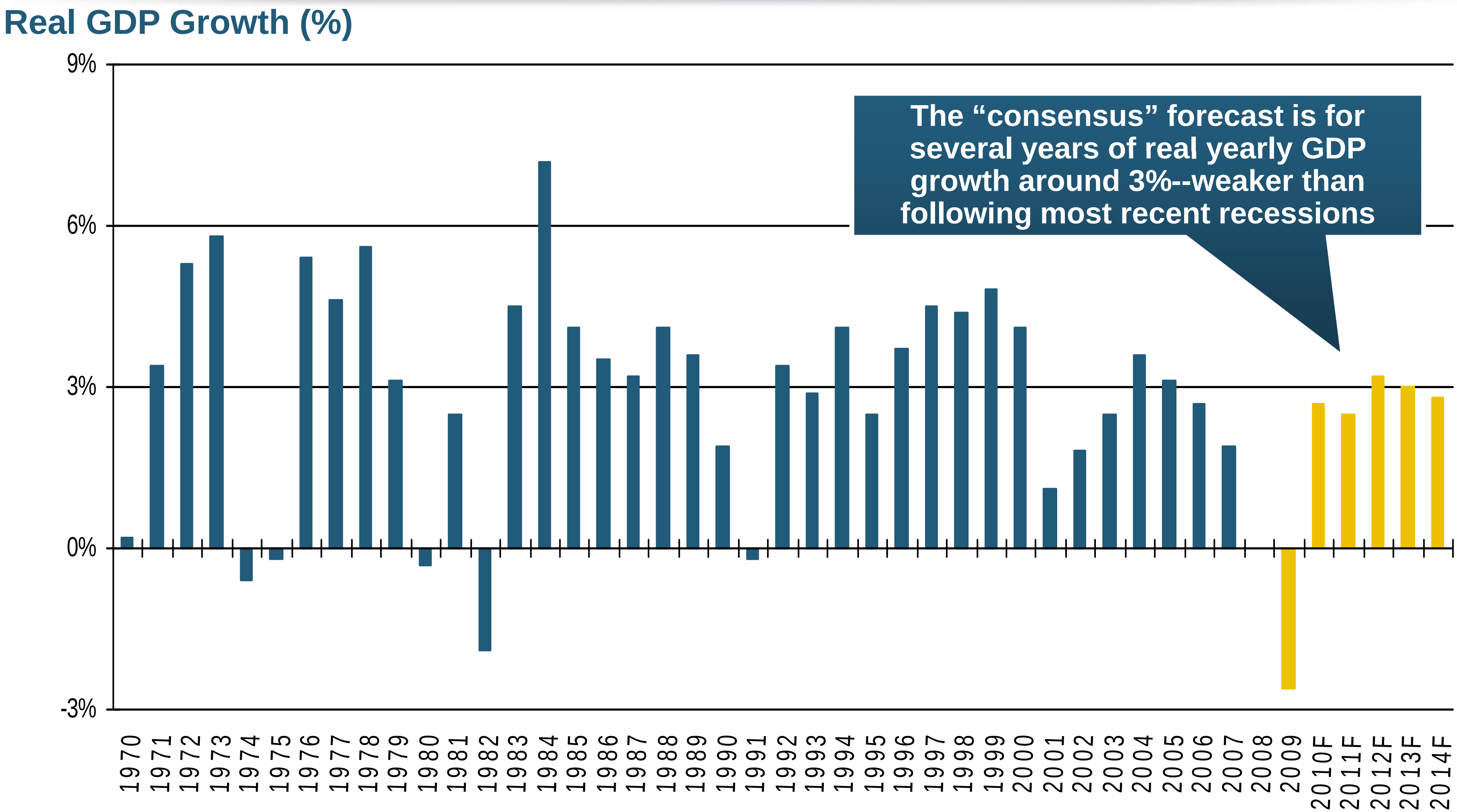
PD liability severity accelerated as inflation rose;

No discernable trend change in BI liability severity trend.

Source: ISO.

Commercial Auto Will Also See Slow Growth

Real GDP Growth, Yearly, 1970-2014F



Estimates/Forecasts from Blue Chip Economic Indicators, 10/2010 issue.

Sources: (GDP) U.S. Department of Commerce at http://www.bea.gov/national/xls/gdpchg.xls.

Recovery in Capacity Utilization is a Positive Sign for Commercial Exposures

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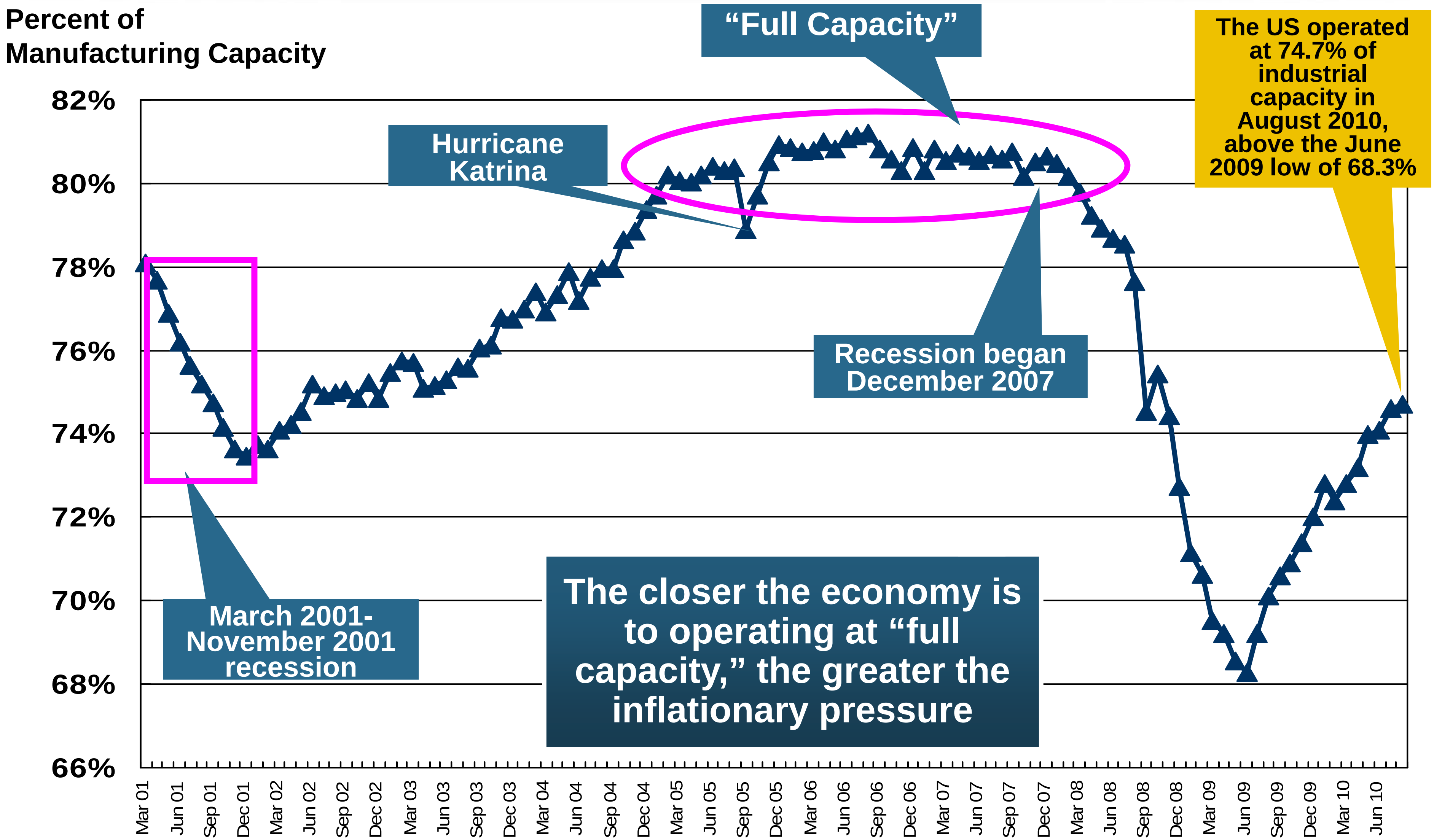

Source: Federal Reserve Board statistical releases at http://www.federalreserve.gov/releases/g17/Current/default.htm.

Business Bankruptcy Filings, 1980-2010:Q2

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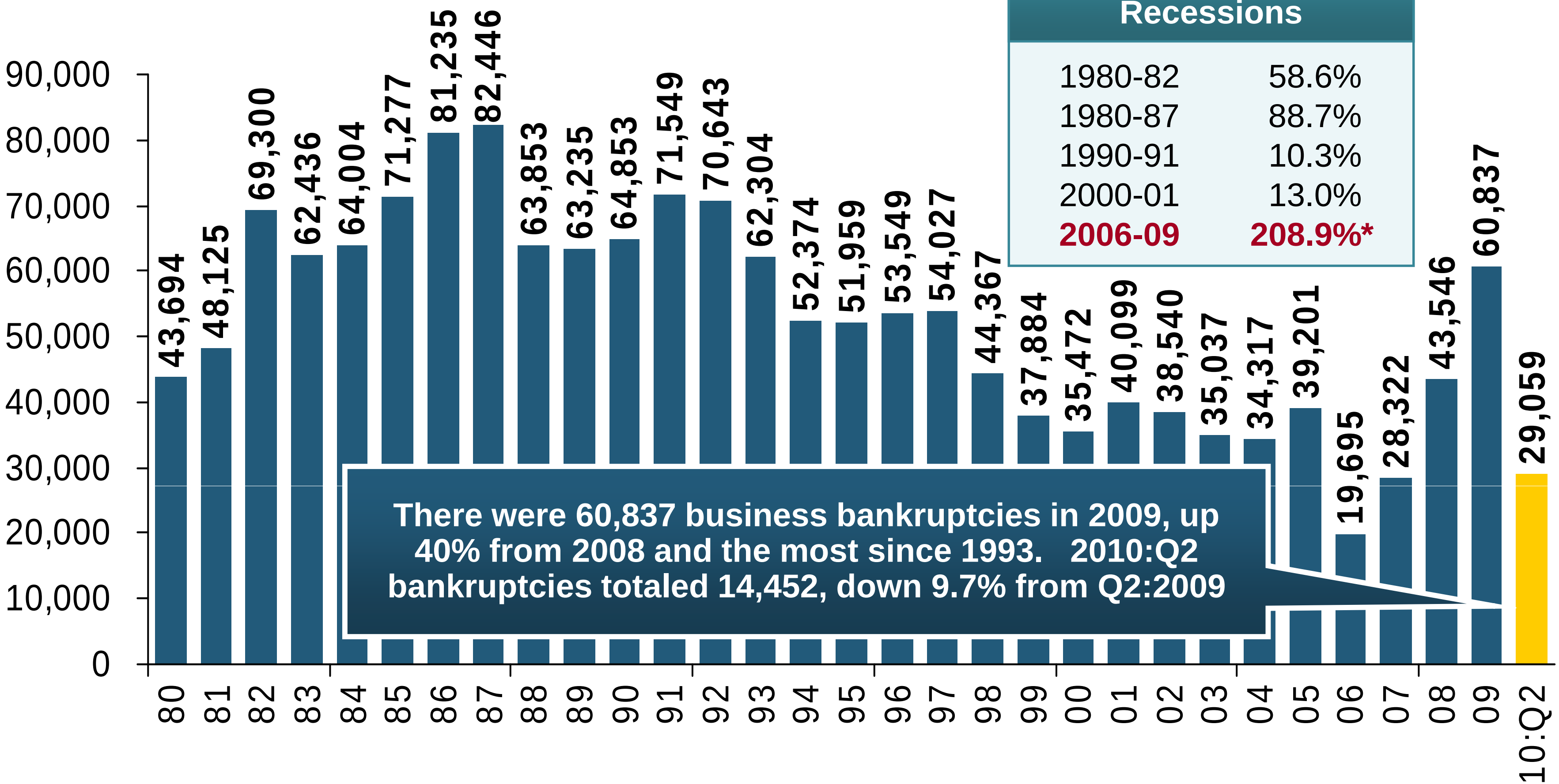

% Change Surrounding Recessions

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

Source: American Bankruptcy Institute; Insurance Information Institute

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

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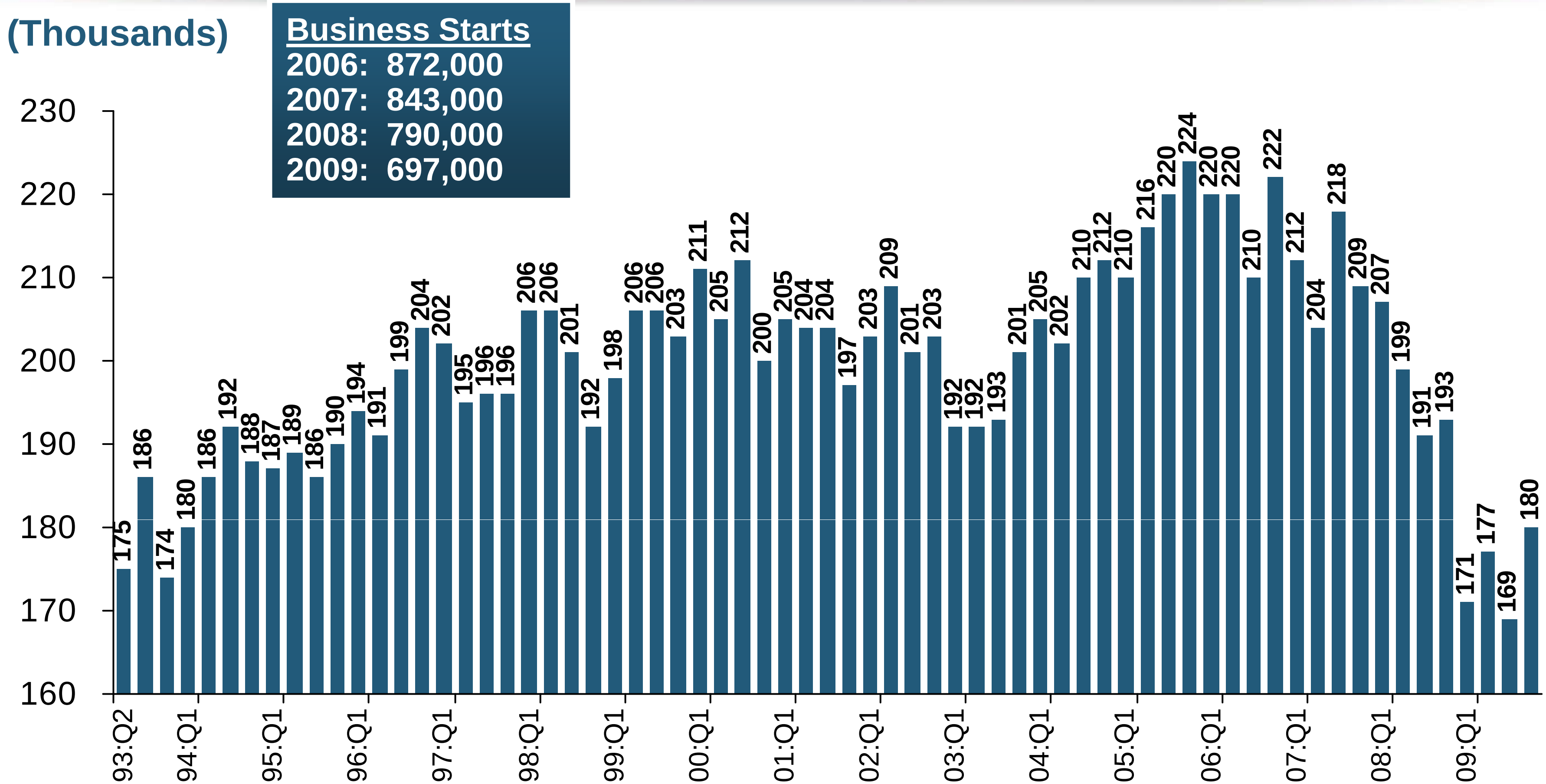
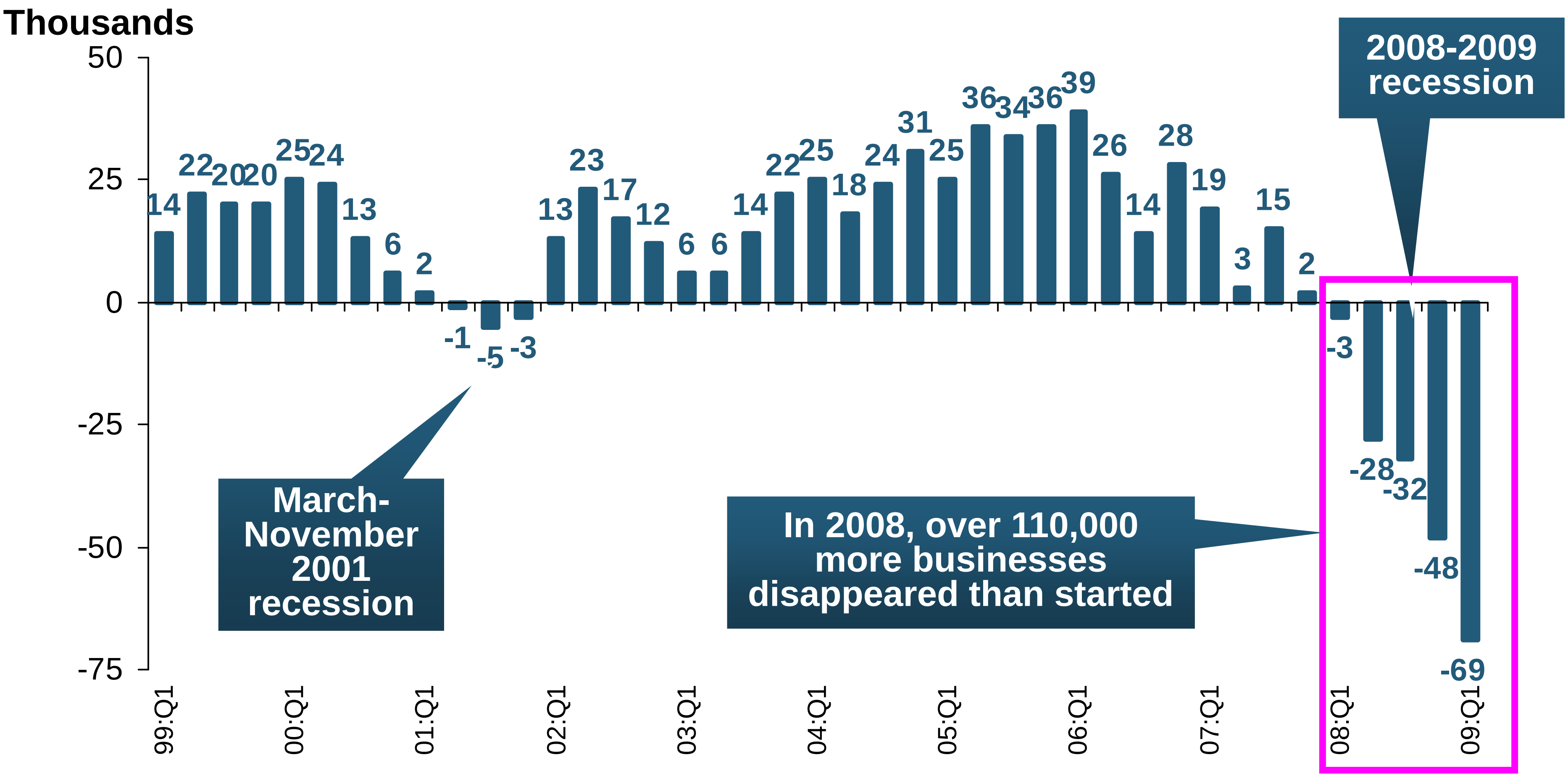


Business Starts Are Down Nearly 20% in the Current Downturn, Holding Back Most Types of Commercial Insurance Exposure

*Latest available as of October 11, 2010, seasonally adjusted

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

Net New Business Formations* 1999:Q1-2009:Q1*



Net Business Formations Likely Were Positive Again, at Least in the Fourth Quarter of 2009 and into 2010.

*Seasonally adjusted. Net formations equals Business "births" minus business "deaths." Latest data on business "deaths" is for 2009:Q1.
Sources: Bureau of Labor Statistics at http://www.bls.gov/news.release/cewbd.t07.htm ; Insurance Information Institute.

Unemployment and Underemployment Rates: Is the Worst Over?

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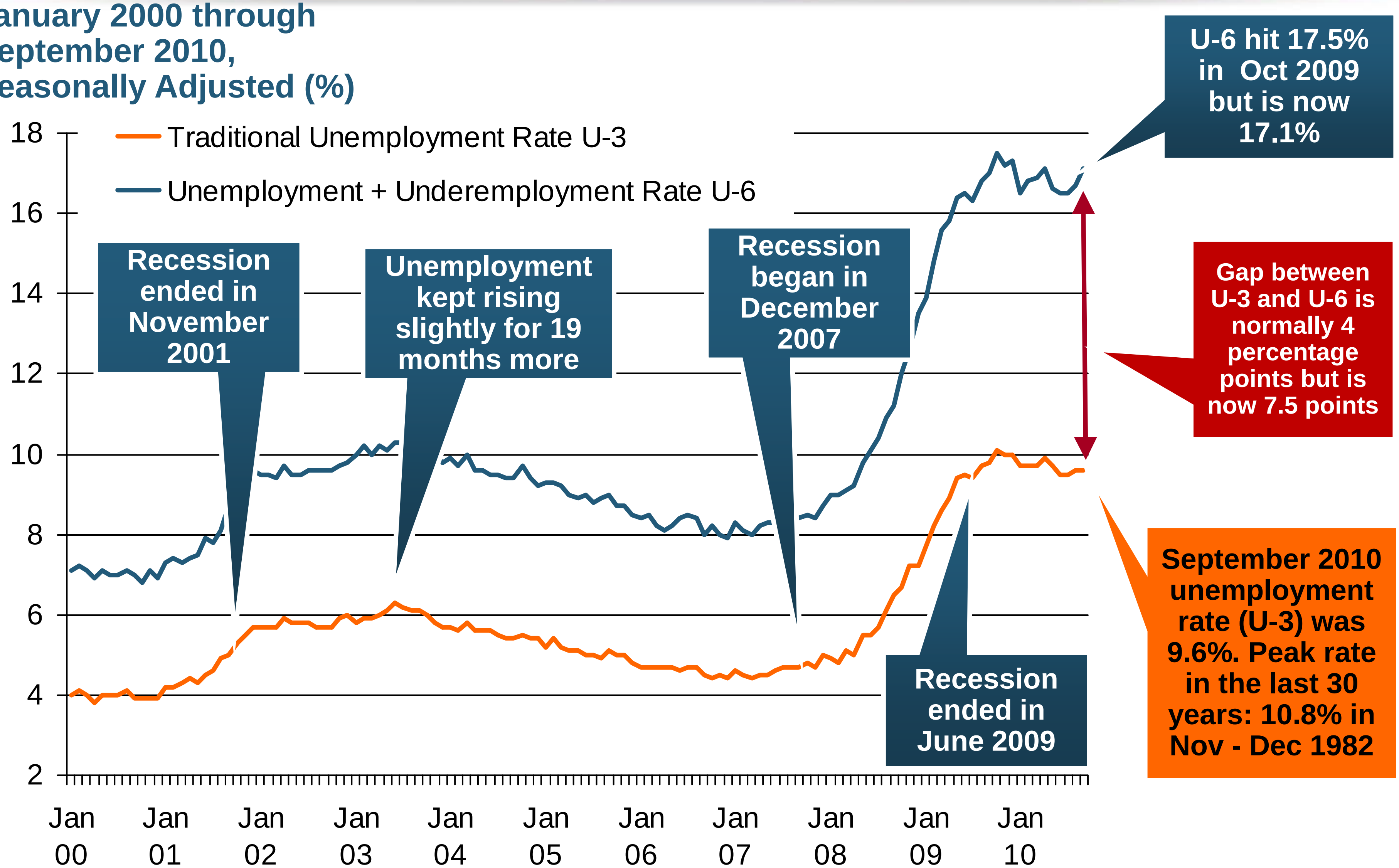
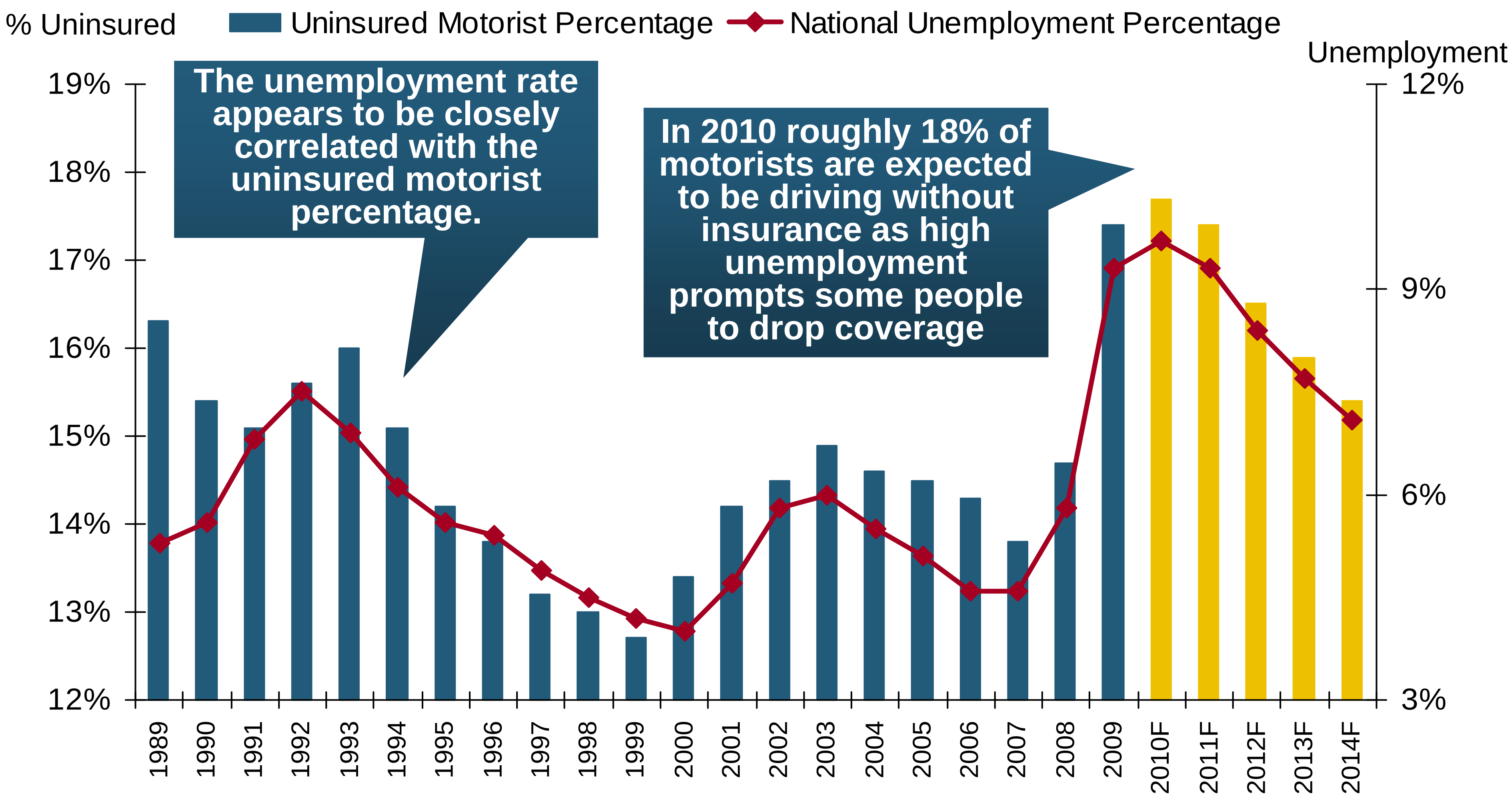
January 2000 through September 2010, Seasonally Adjusted (%)



Source: U.S. Bureau of Labor Statistics; Insurance Information Institute.

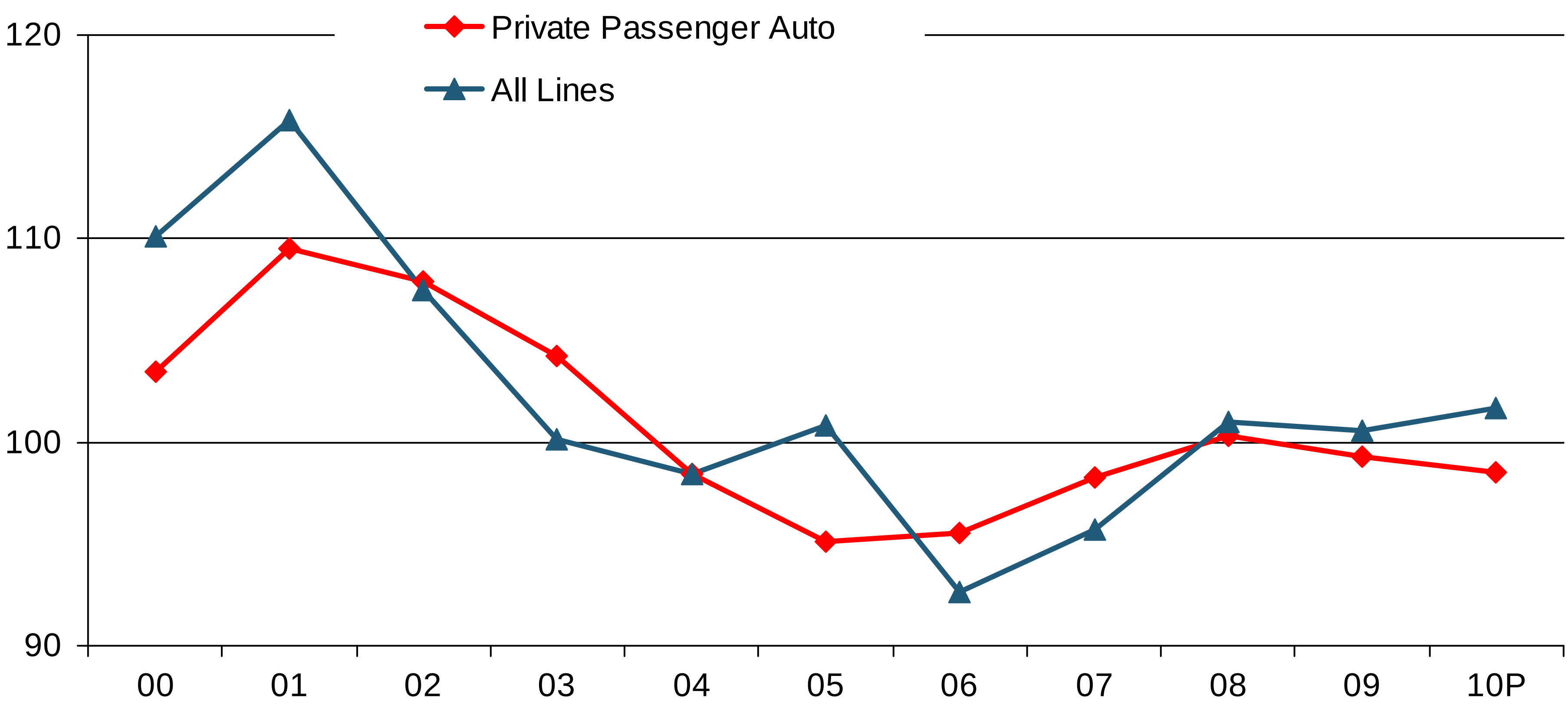
Unemployment's Effect on Percent of Uninsured Motorists, 1989-2014F



Source: *Uninsured Motorists, 2008* Edition, Insurance Research Council; Blue Chip Economic Indicators (Unemployment data, including forecasts); Insurance Information Institute. The regression equation IRC developed is Y=0.103 + 0.7659X, where X= the unemployment rate and Y is the estimated percent of uninsured motorists.

Underwriting Trends in Auto Insurance

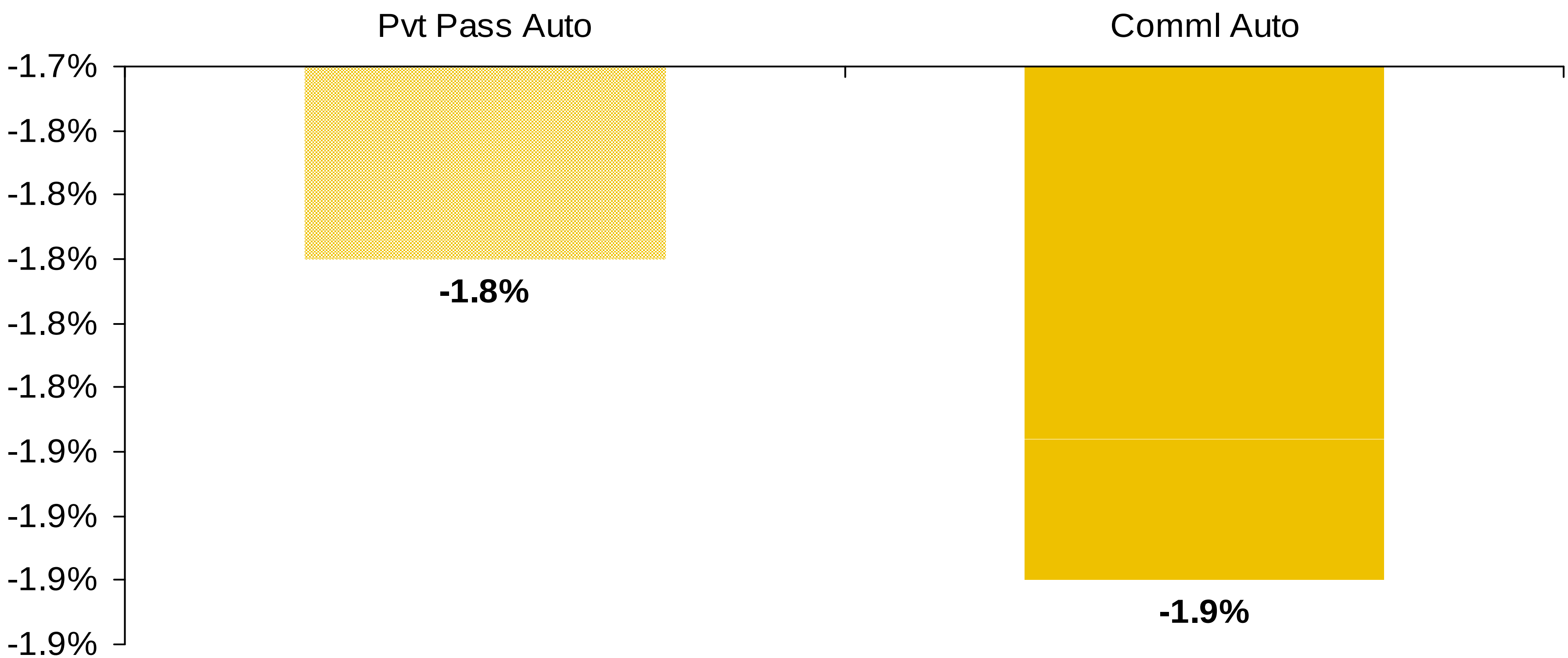
Auto Combined Ratios vs. All Lines, 2000–2010P*



Taking the U.S. as a Whole, Private Passenger Auto Combined Ratios Were Under 100 From 2004 Through 2010 (except for 100.3 in 2008)

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

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



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

*Based on 2008 Invested Assets and Earned Premiums
Source: A.M. Best; Insurance Information Institute.

Claim Trends

Rising Severity Held in Check by Falling Frequency:

Can That Pattern Be Sustained?

PPAuto Bodily Injury Liability: Severity Trends Offset the Decline in Frequency

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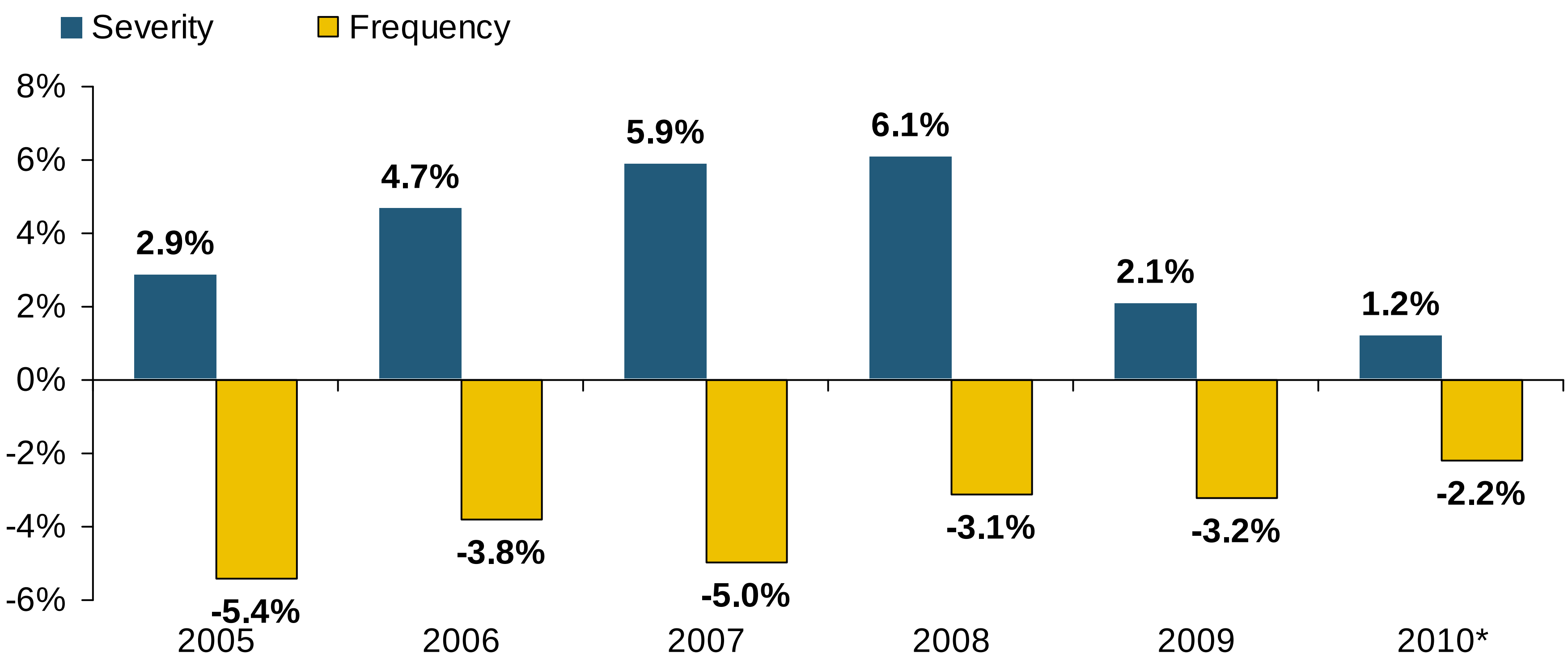
Annual Change, 2005 through 2010*



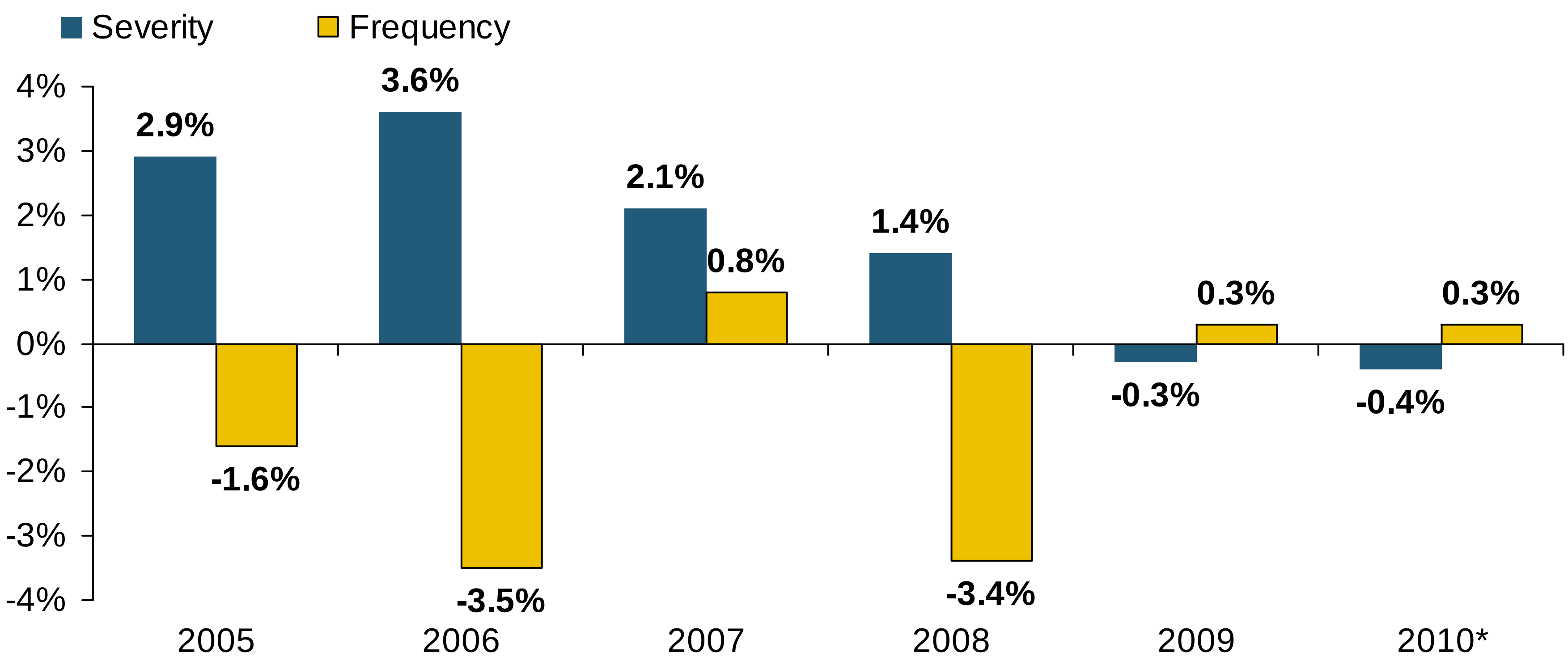
Cost Pressures Will Increase if BI Severity Increases Outpace Declines in Frequency

*For 2010, data are for the 4 quarters ending with 2010:Q2.

Source: ISO/PCI *Fast Track* data; Insurance Information Institute

PPAuto Property Damage Liability: Frequency, Severity Trends Offset in 2009/10

Annual Change, 2005 through 2010*



Stable Severity/Frequency Trends Keeping PD Costs in Check, But Are These Trends Sustainable?

*For 2010, data are for the 4 quarters ending with 2010:Q2.

Source: ISO/PCI *Fast Track* data; Insurance Information Institute

No-Fault (PIP) Liability: Frequency & Severity Trends Are Adverse*

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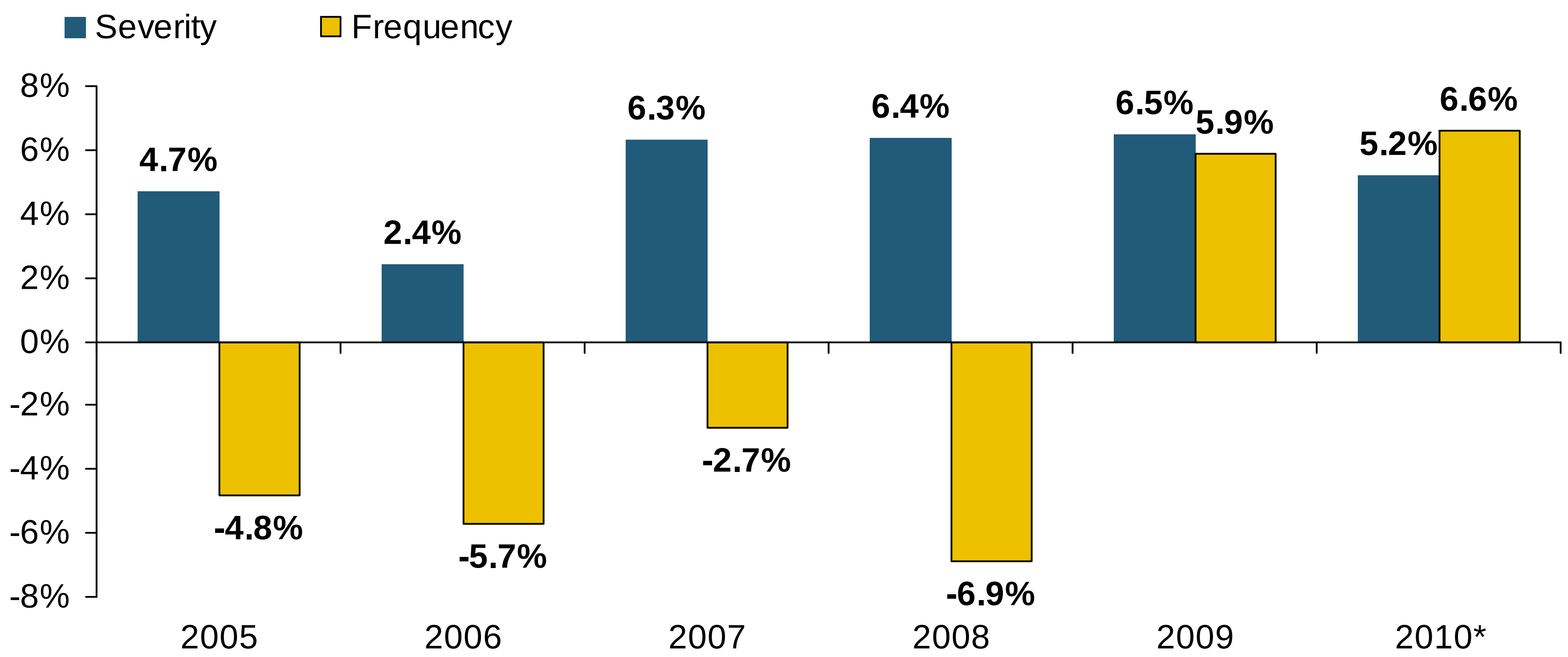
Annual Change, 2005 through 2010*



Multiple States Are Experiencing Severe Fraud and Abuse Problems in their No-Fault Systems, Especially FL, MI, NY and NJ

*No-fault states included are: FL, HI, KS, KY, MA, MI, MN, NY, ND and UT; 2010 data are for the 4 quarters ending 2010:Q2.
Source: ISO/PCI *Fast Track* data; Insurance Information Institute

Collision Coverage: Frequency and Severity Trends Have Been Favorable

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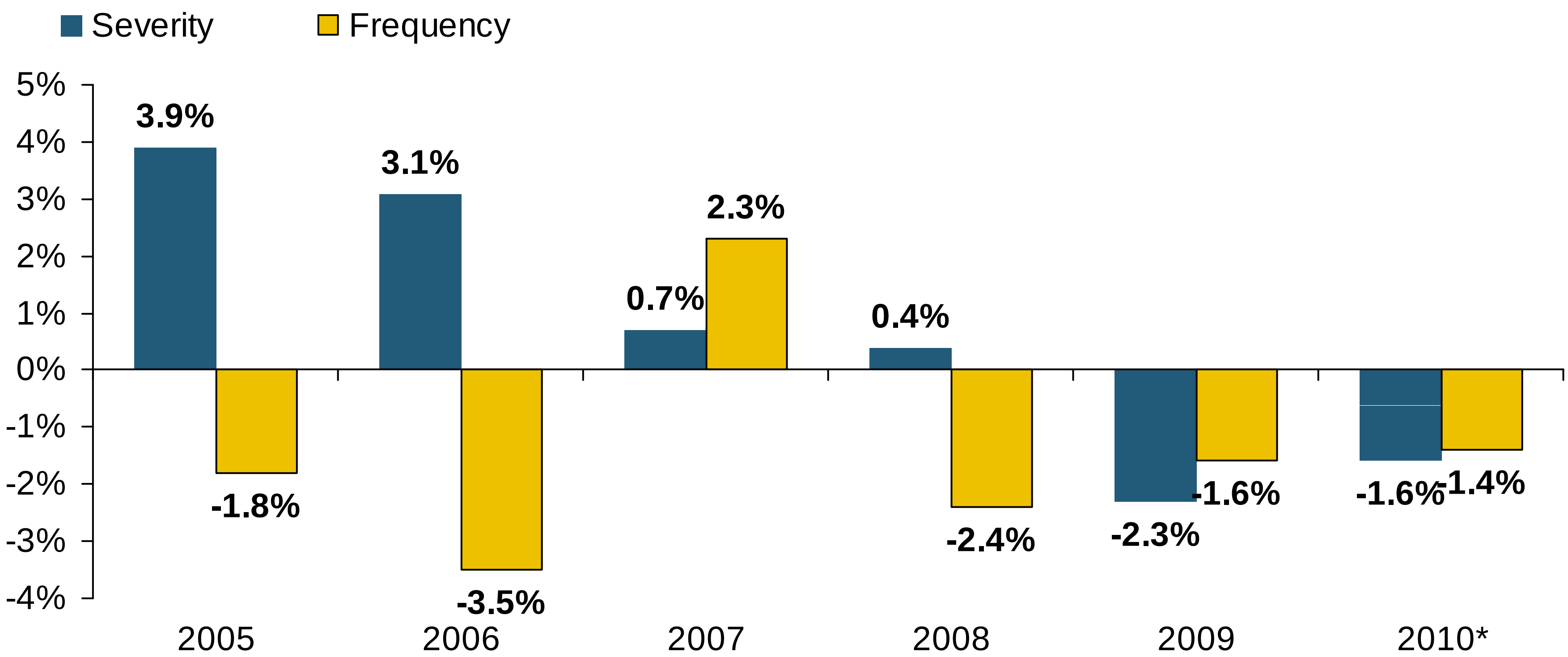
Annual Change, 2005 through 2010*



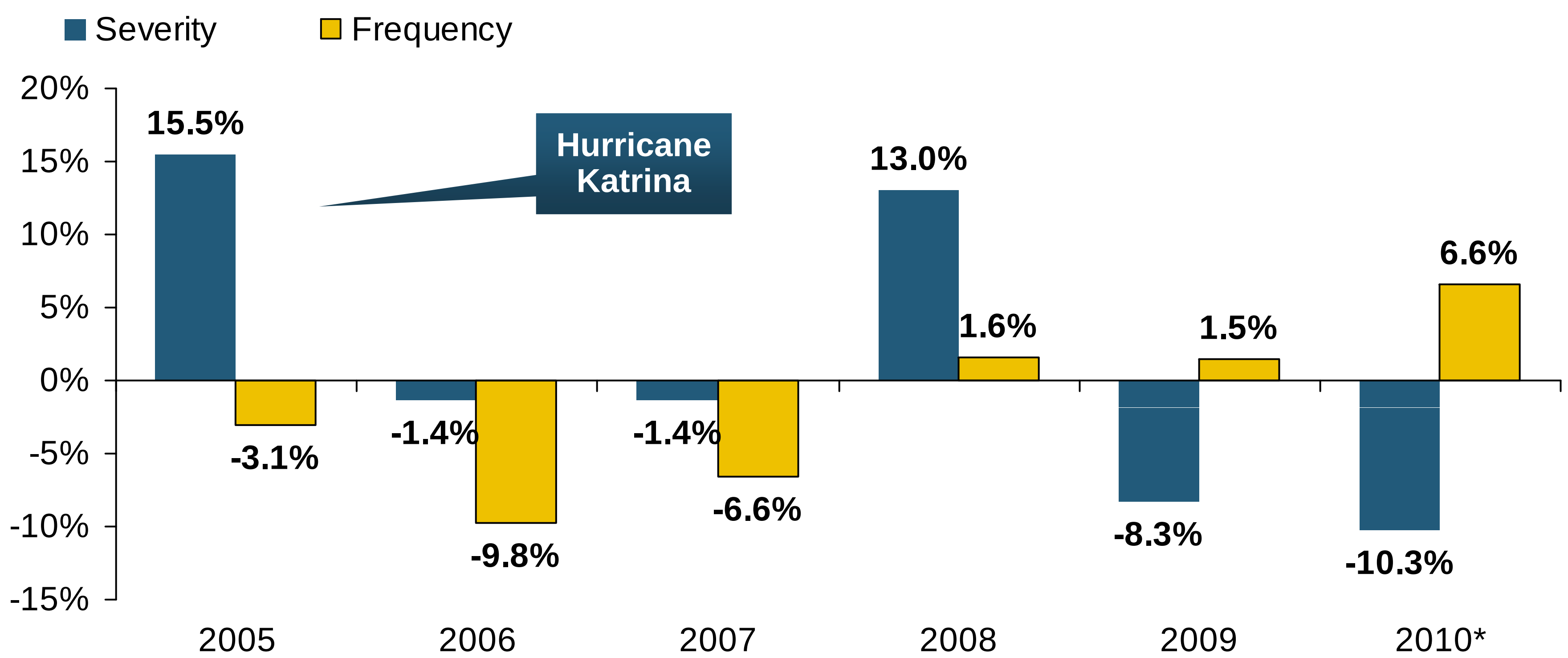
The Recession, High Fuel Prices Have Helped Push Down Frequency and Temper Severity, But this Trend Will Likely Be Reversed Based on Evidence from Past Recoveries

*For 2010, data are for the 4 quarters ending with 2010:Q2.

Source: ISO/PCI *Fast Track* data; Insurance Information Institute

Comprehensive Coverage: Severity Trends Very Favorable in 2009/2010

Annual Change, 2005 through 2010*



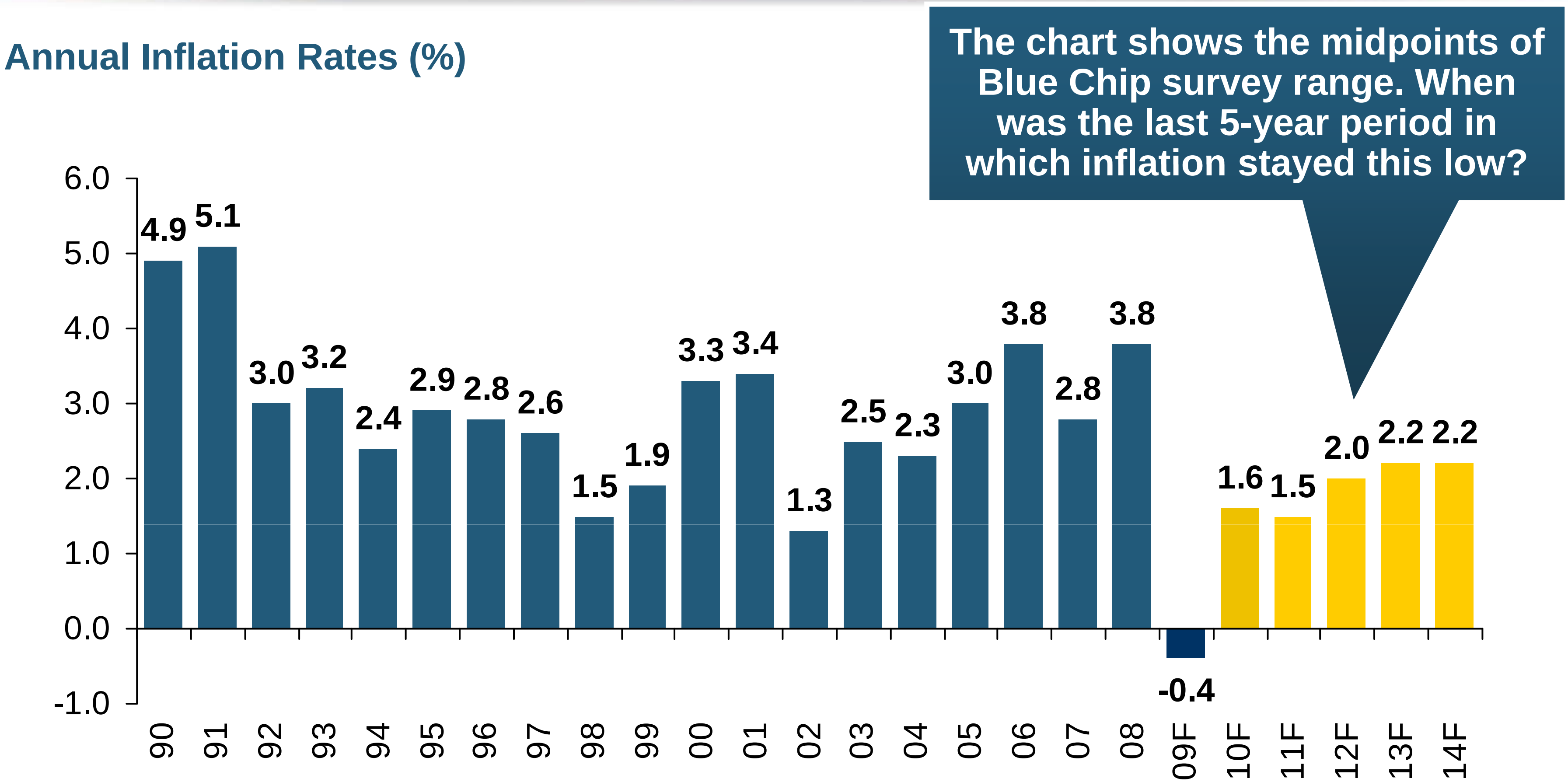
Weather Creates Volatility for Comprehensive Coverage; Recession Has Helped Push Down Frequency and Temper Severity, But This Factors Will Weaken as Economy Recovers

*For 2010, data are for the 4 quarters ending with 2010:Q2.
Source: ISO/PCI *Fast Track* data; Insurance Information Institute

Inflation

Subdued Inflation Doesn't Reflect P/C Cost Pressures

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



The Consumer Price Index is Forecast to Remain Unusually Low for Several Years

Sources: U.S. Bureau of Labor Statistics (history); Blue Chip Economic Indicators, Oct 2010 (forecasts).

Auto BI Liability Insurers Feel Higher Inflation than the CPI Measures

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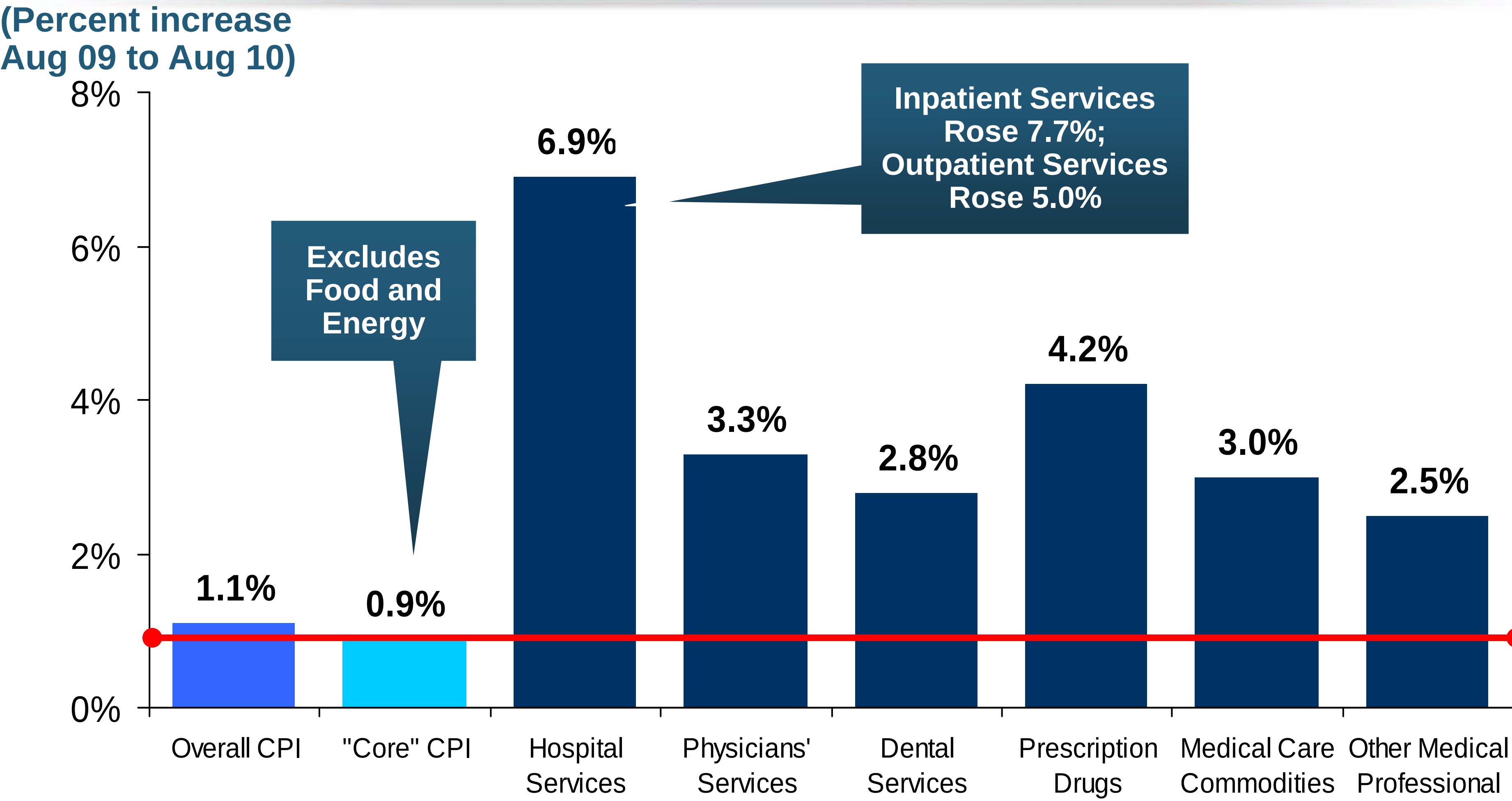

Healthcare Costs Are a Major Auto BI Liability Insurance Cost Driver. They Are Likely to Increase Faster than the CPI for the Next Few Years, at Least

Source: Bureau of Labor Statistics; Insurance Information Institute.

Auto Physical Damage Insurers Feel Higher Inflation than the CPI Measures

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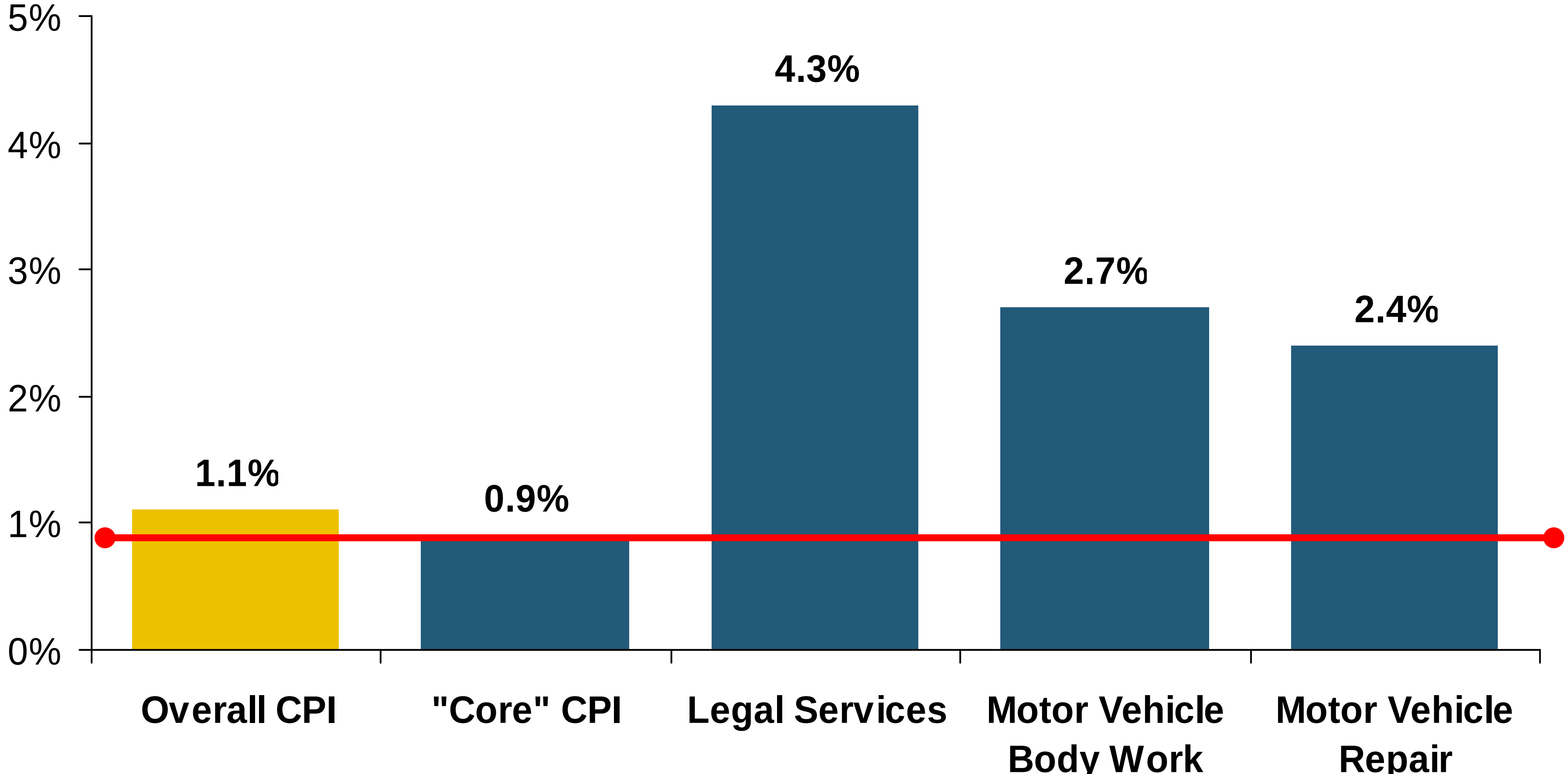
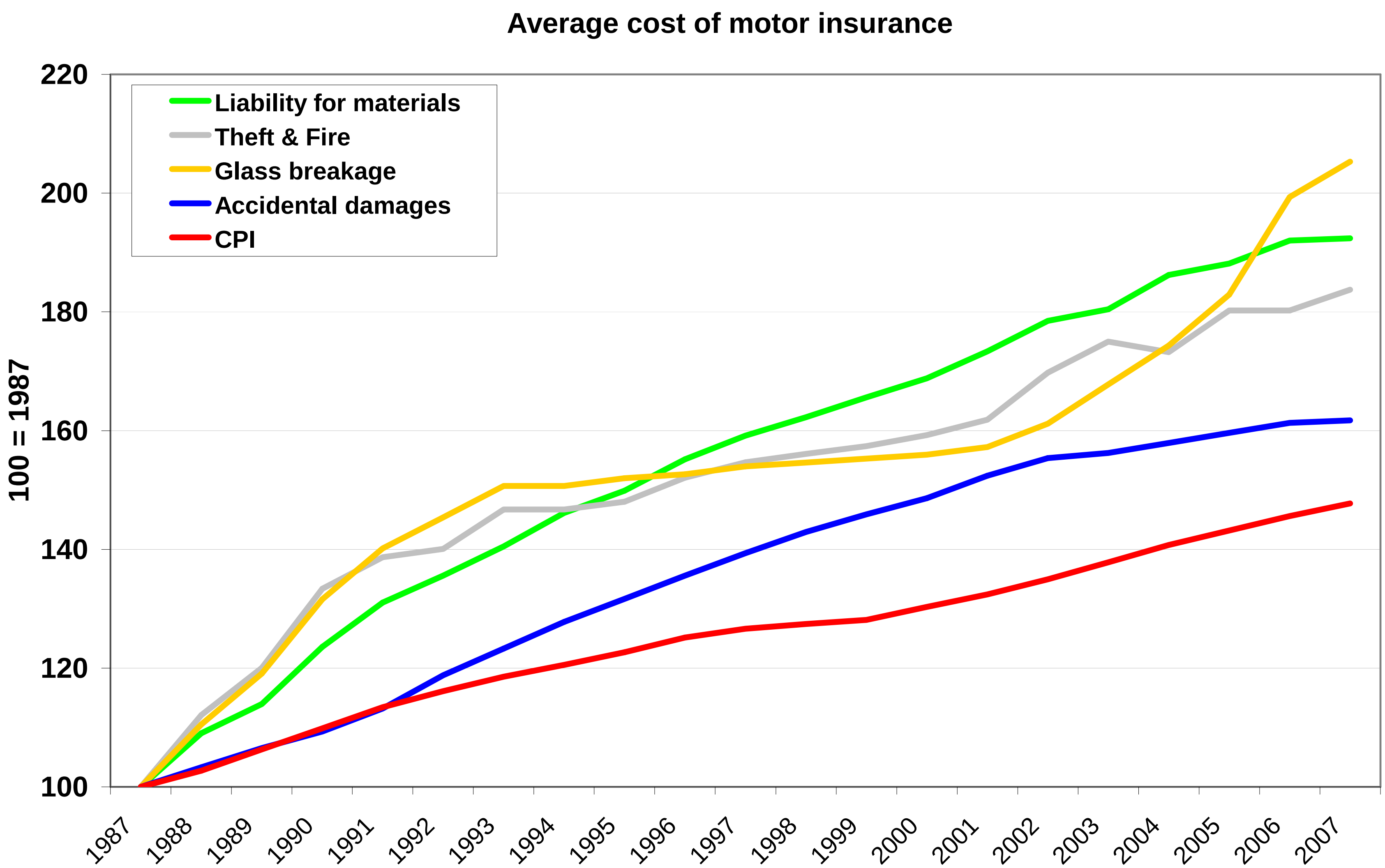
(Percent increase Aug 09 to Aug 10)



Legal/Tort Costs and Auto Repair Costs Are Major Auto Physical Damage Insurance Cost Drivers That Are Expected to Increase Above the Inflation Rate Indefinitely

Sources: U.S. Dept of Labor, Bureau of Labor Statistics; Insurance Information Institute

All Segments of French Motor Insurance Costs Have Grown Faster than the CPI for Over 20 Years



Source : Fédération Française des Sociétés d'Assurance

Top Risks for Auto Insurers if Inflation Is Reignited

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- **Rising Claim Severities**
  - Cost of claims settlement rises across the board (property and liability)
- **Rate Inadequacy**
  - Rates inadequate due to low trend assumptions arising from use of historical data
- **Reserve Inadequacy**
  - Reserves may develop adversely and become inadequate (deficient)
- **Burn Through on Retentions**
  - Retentions, deductibles burned through more quickly
- **Reinsurance Penetration/Exhaustion**
  - Higher costs ➔ risks burn through their retentions more quickly, tapping into reinsurance more quickly and potentially exhausting their reinsurance more quickly

Source: Insurance Information Institute.

We Can Have Inflation Despite High Unemployment

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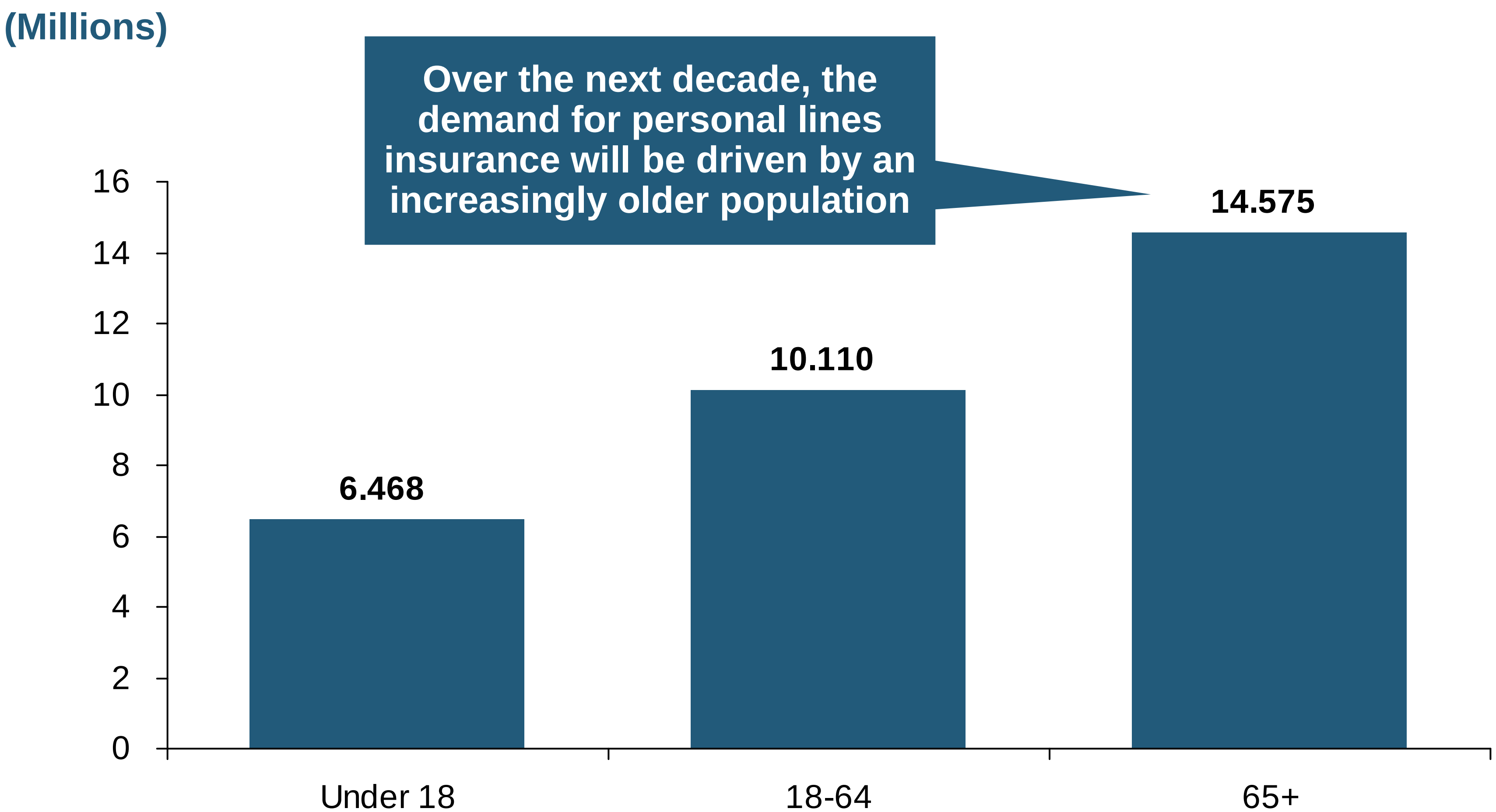
- We can "import" inflation.
  - For example, China is raising interest rates to tame a growing inflation rate. If the prices of things we import rise, importers will try to pass these increases along to buyers.
  - And if the dollar depreciates vs. currencies of nations from which we import, the dollar price of imports will rise.
- We ***had*** high inflation during the 1980 and 1981-82 recessions.

The Aging Population

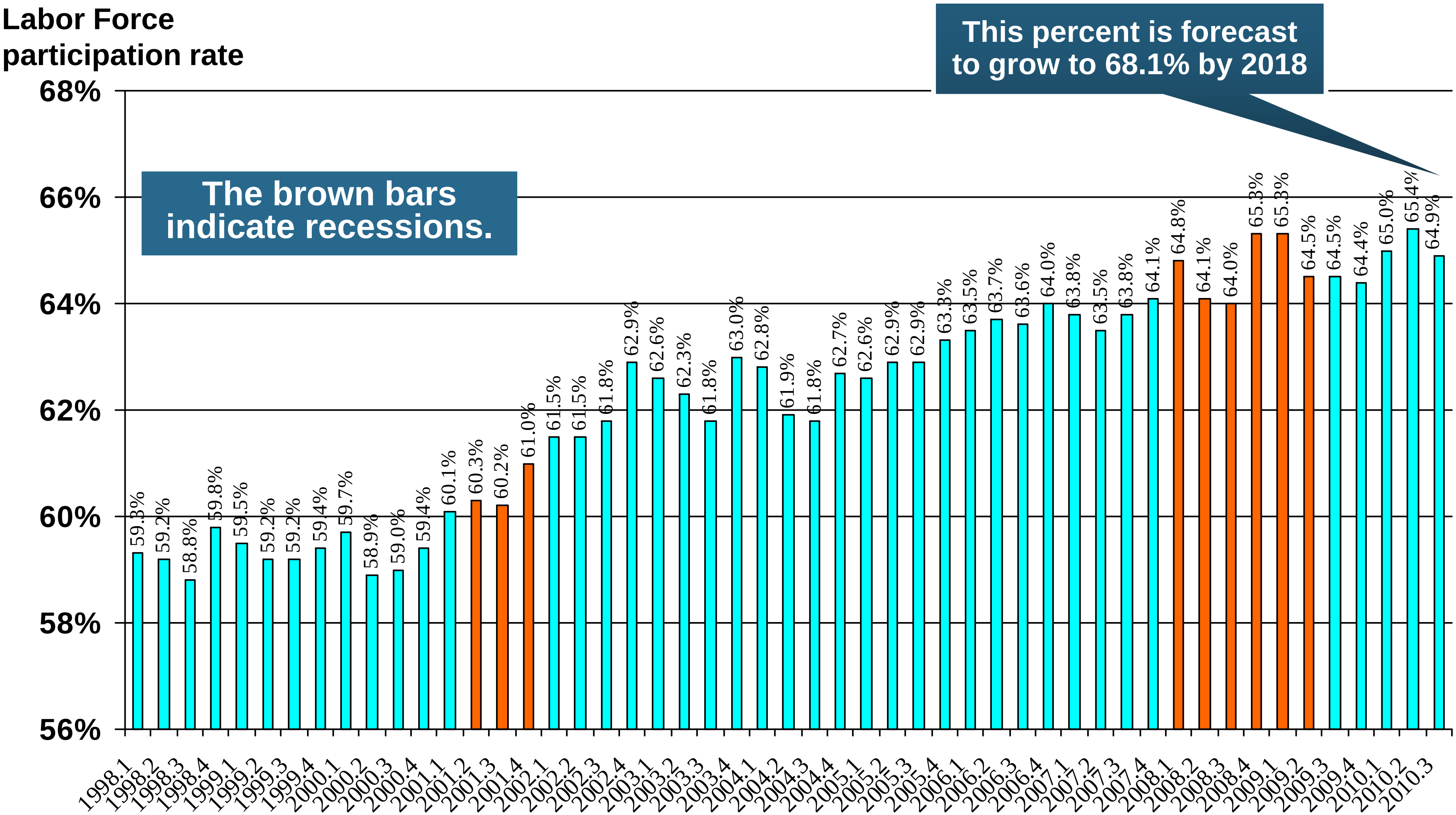
Increase in Population by Age Category, 2010 to 2020



Claim Trends in Personal Lines Will Shift With Demographics; Insurers Must Adapt

Source: US Census Bureau

Labor Force Participation Rate, Ages 55-64, Quarterly, 1998-2010:Q3



The labor force participation rate for workers 55-64 grew from about 59% in 2000 to 64% by 2006 and then flattened, but might be inching up again.

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

Labor Force Participation Rate, Ages 55-64, Quarterly, 1998-2018P

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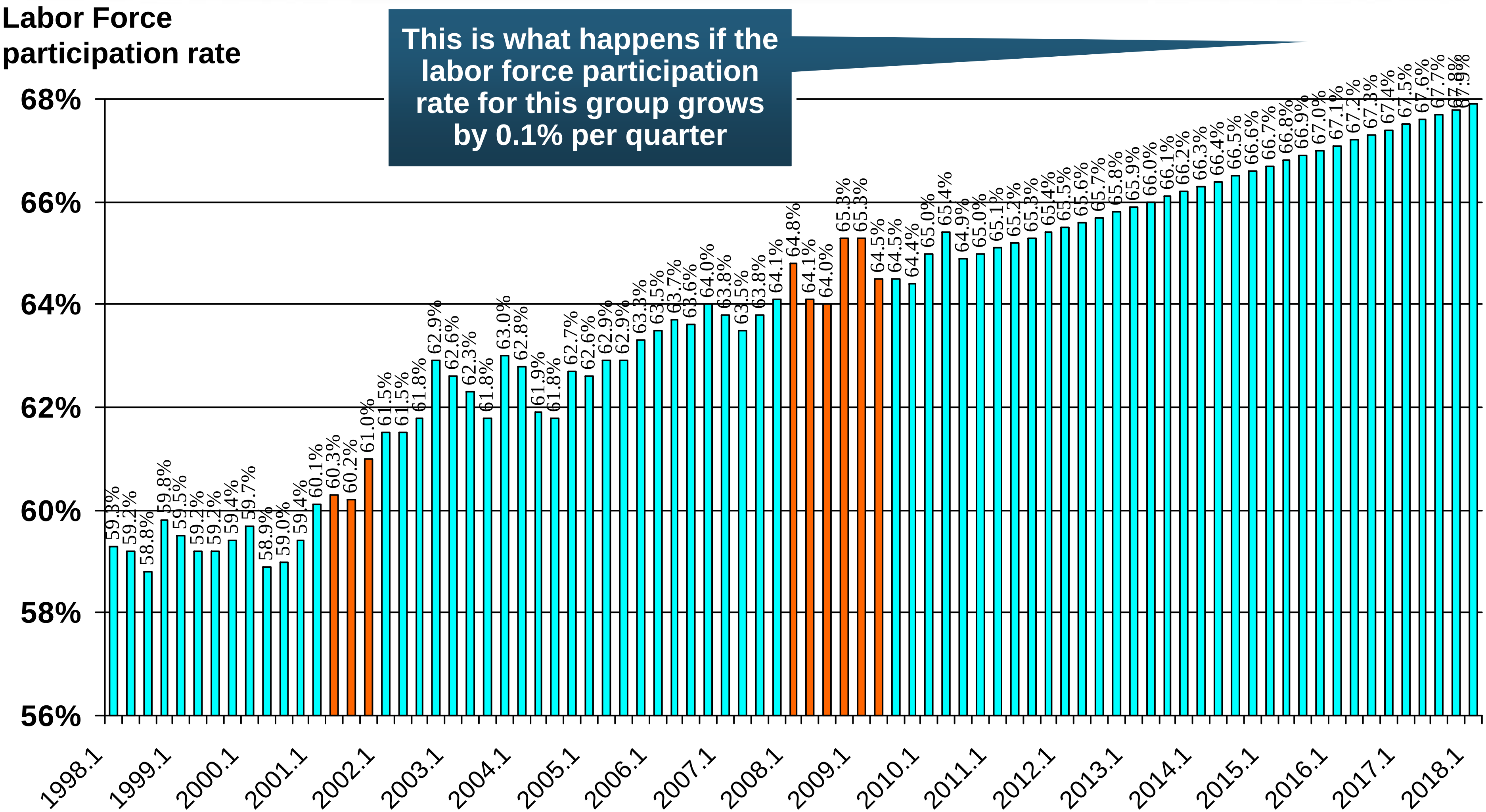

Source: US Bureau of Labor Statistics, US Department of Labor; Insurance Information Institute.

Labor Force Participation Rate, Ages 65-69, Quarterly, 1998-2010:Q3

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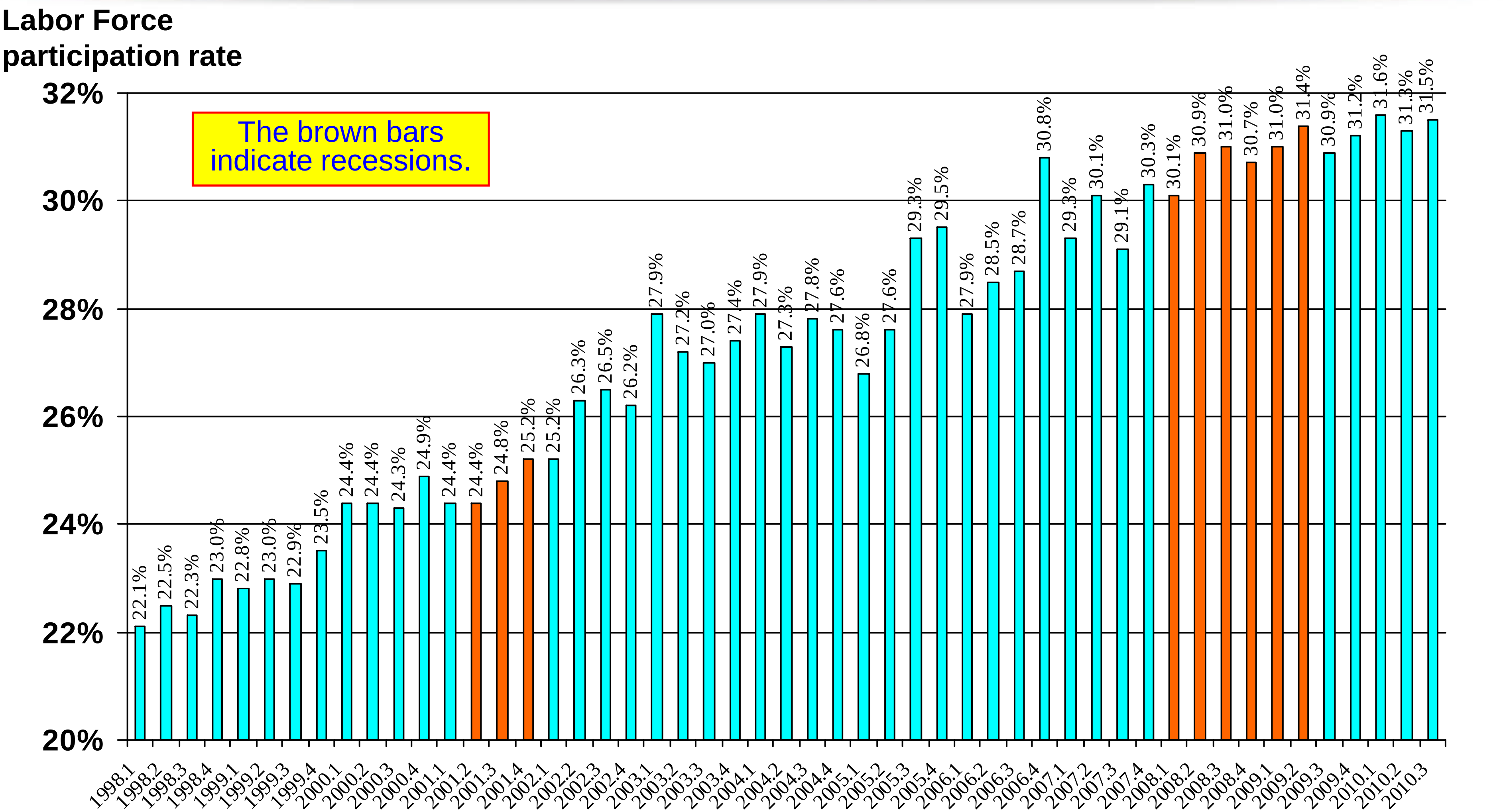
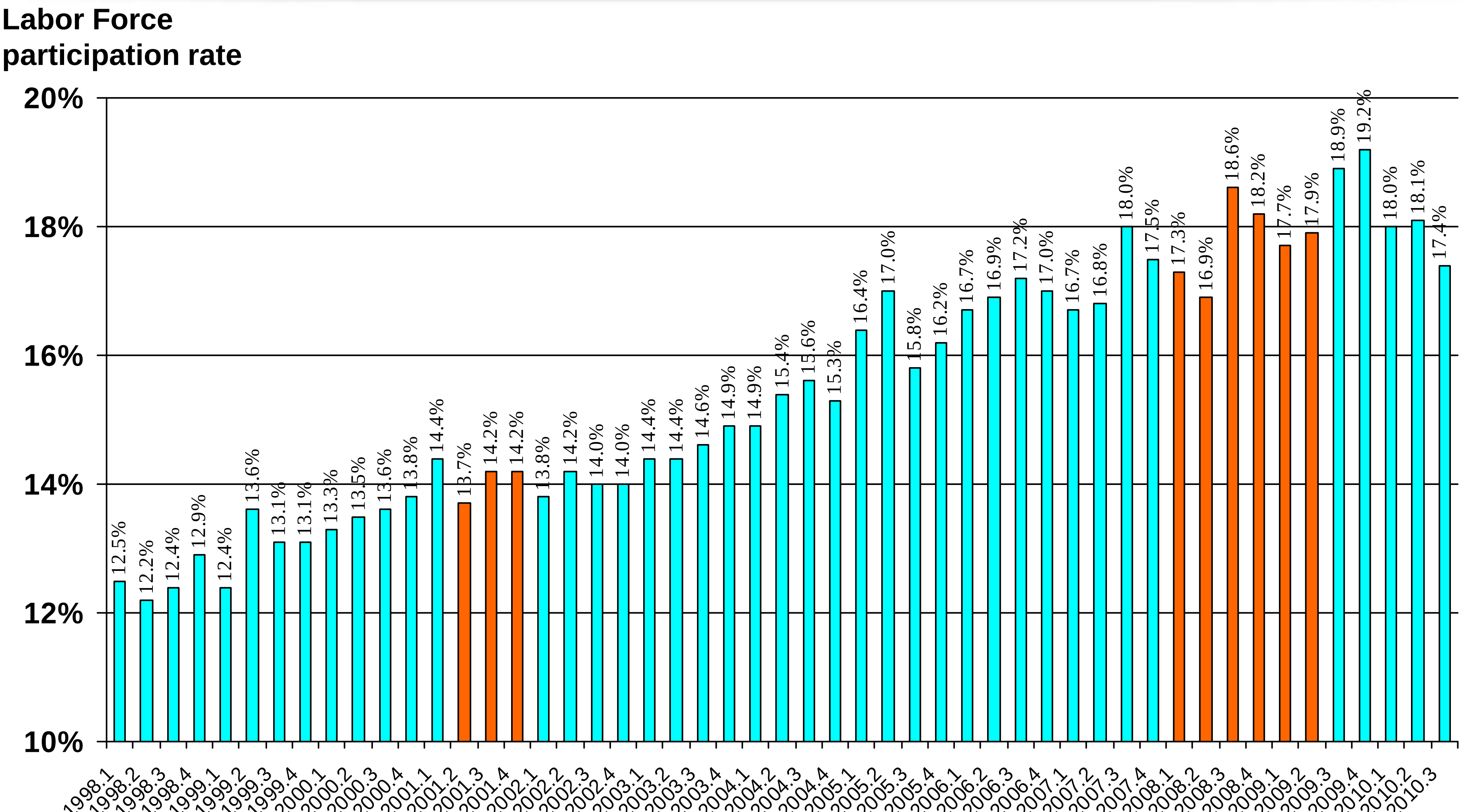


The labor force participation rate for workers 65-69 might grow even faster in the future as seniors find they can't fully retire on their meager retirement savings.

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

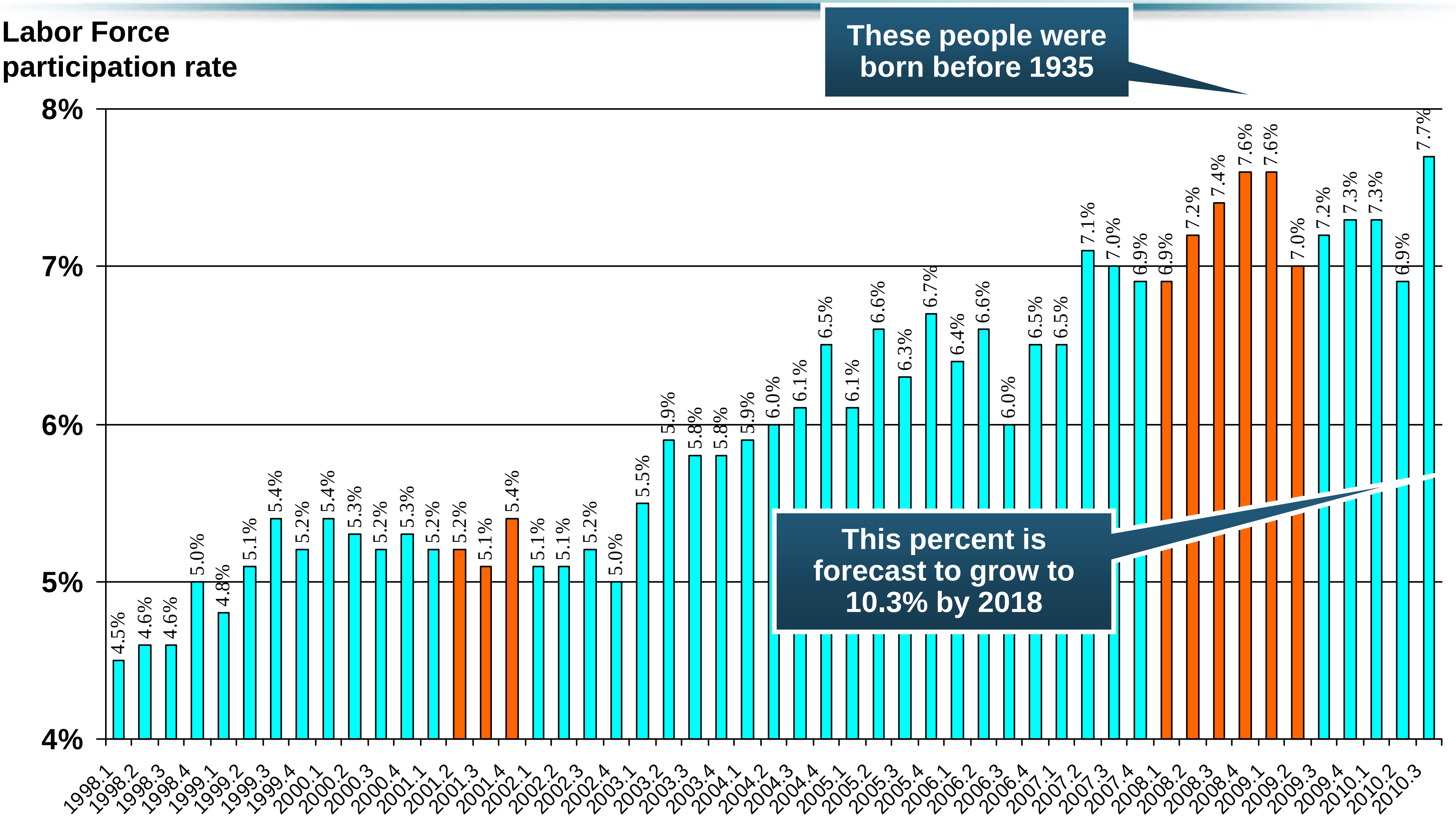
Labor Force Participation Rate, Ages 70-74, Quarterly, 1998-2010:Q3



The labor force participation rate for workers 70-74 grew by about 50% since 1998, but growth has stalled since the Great Recession began.

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

Labor Force Participation Rate, Ages 75 & over, Quarterly, 1998-2010:Q3



The labor force participation rate for workers 70-74 grew by about 50% since 2002, but growth has stalled since the Great Recession began.

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

Younger and Older Drivers Are Over-Represented in Fatal Crashes

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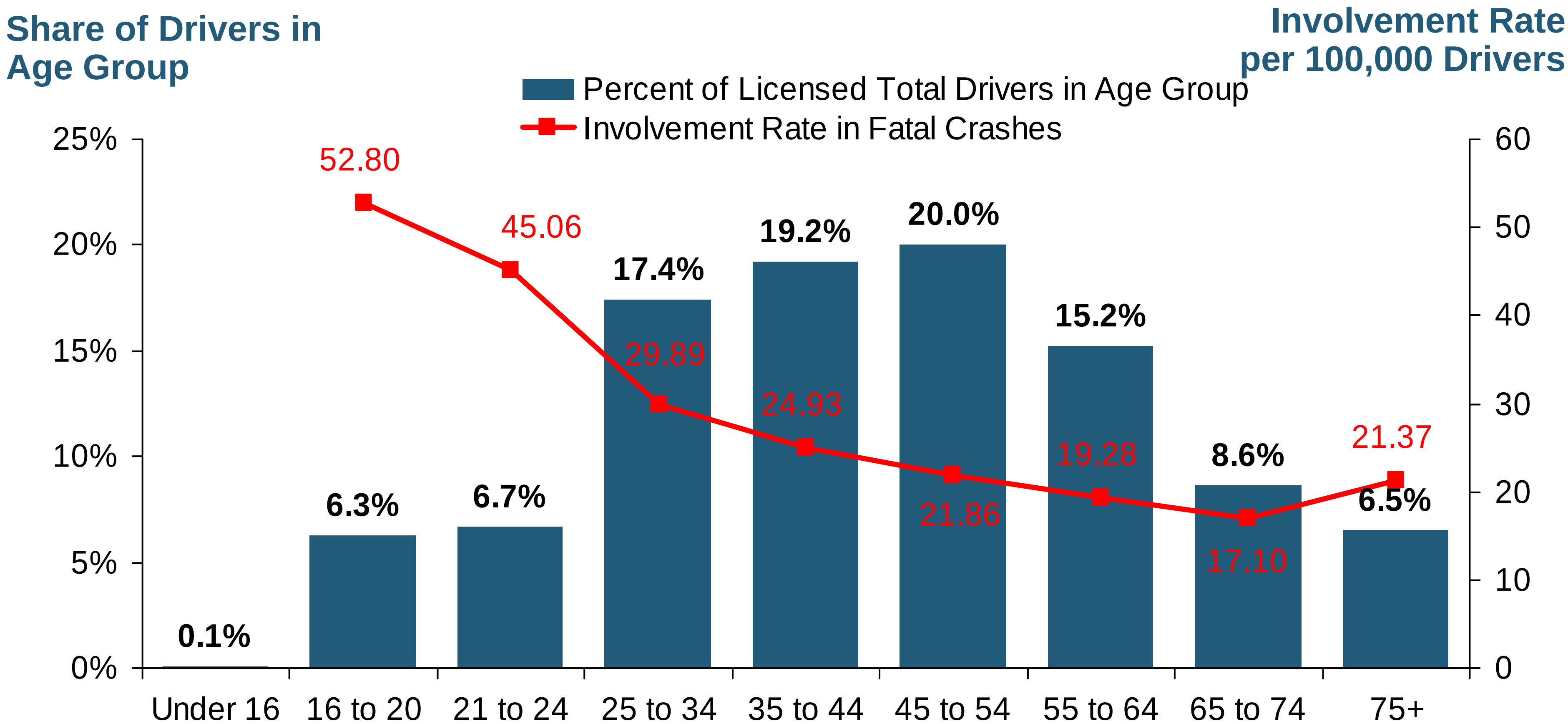
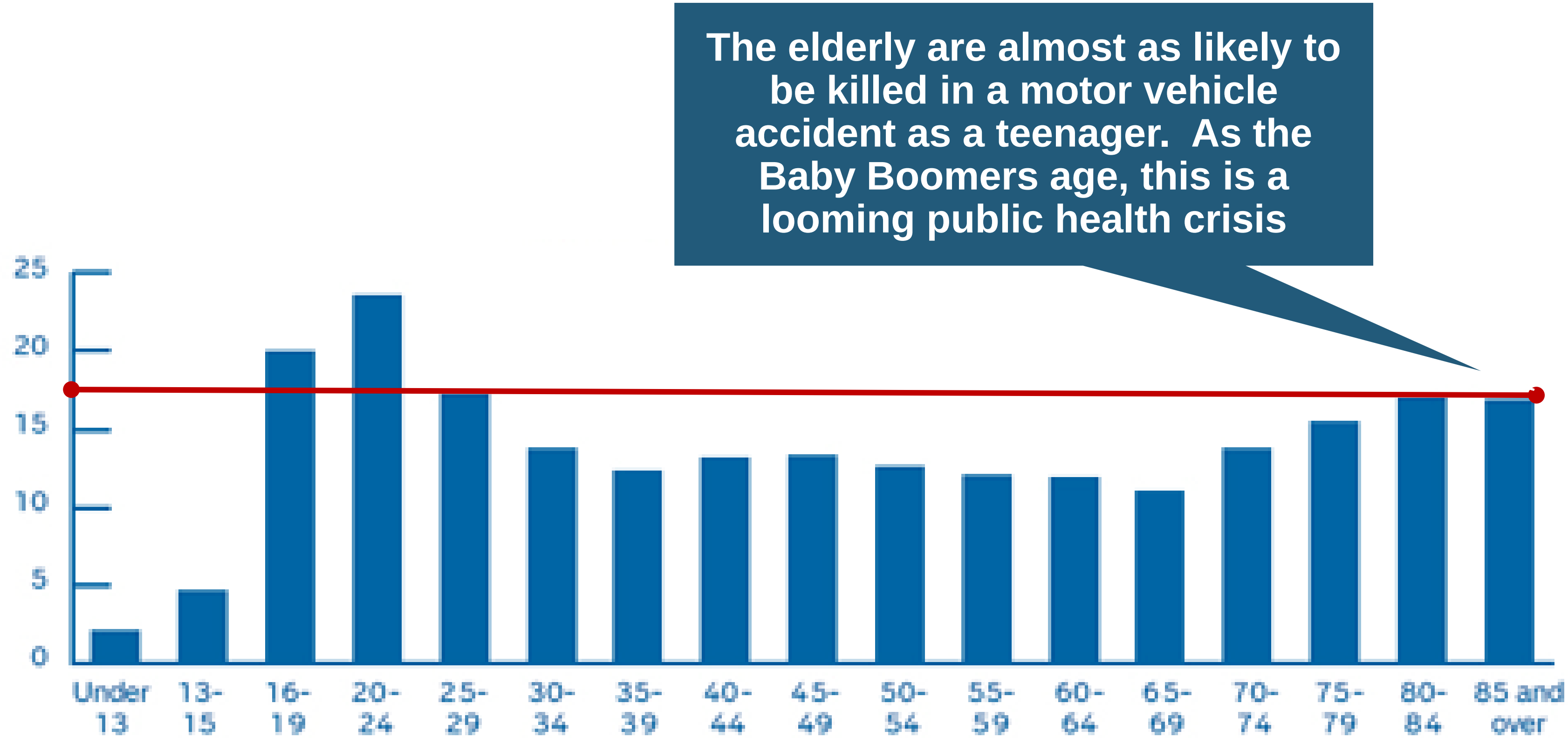


Immigration and High Birth Rates in Some Demographic Groups, Combined With Baby Boomers Aging Creates Challenges for Insurers and Auto Safety Experts

Sources: US DOT, NHTSA, Federal Highway Administration; Insurance Information Institute

Motor Vehicle Deaths per 100,000 Persons by Age, 2008



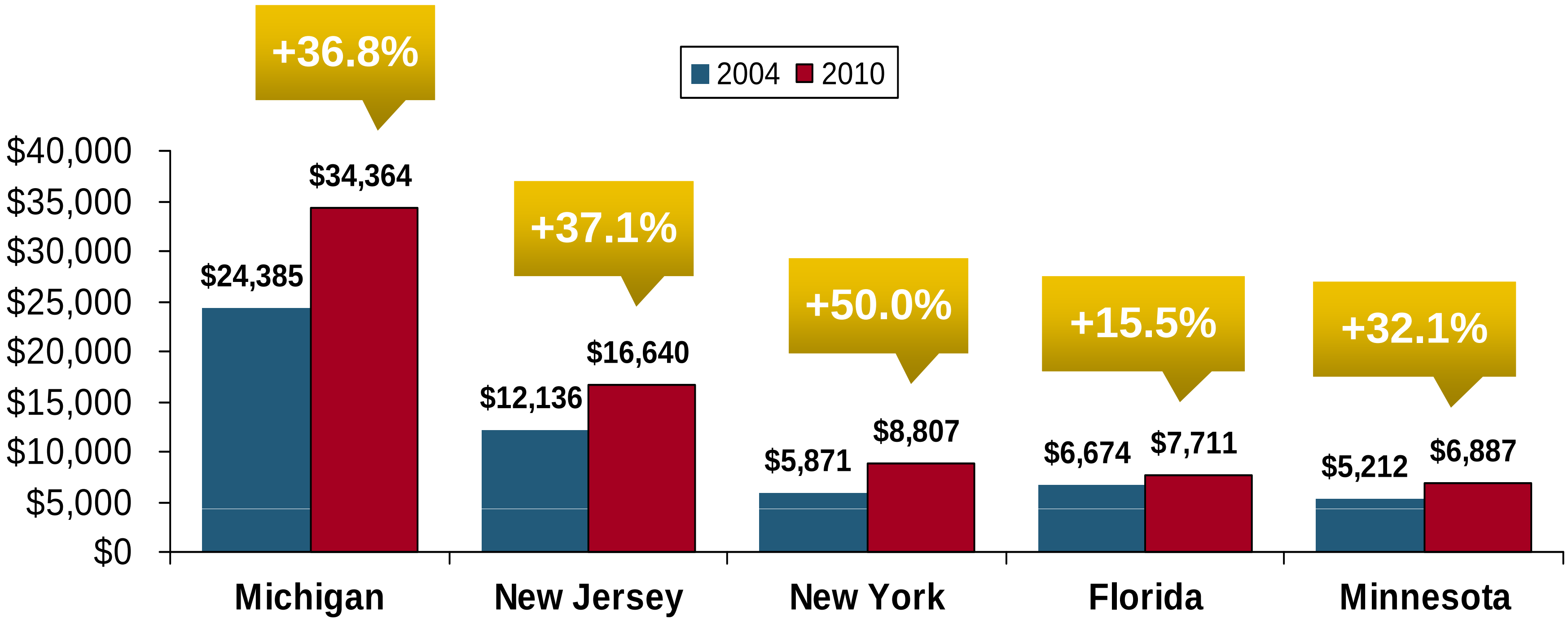
Problem: How to Keep the Elderly Safe in Cars (Not Just When They're Behind the Wheel)

Sources: Insurance Institute for Highway Safety; Insurance Information Institute

Fraud & Abuse in Private Passenger Auto Insurance

Skyrocketing No-Fault (PIP) Claim Costs Are a Major Concern in Several States

Increase in No-Fault Claim Severity: 2004-2010*



The no-fault systems in MI, NJ, NY, FL, and MN are under stress due to rising fraud and abuse which will ultimately lead to higher premiums for drivers

*2010 figure is for the 4 quarters ending 2010:Q2.

Sources: Insurance Information Institute research from ISO/PCI *Fast Track* data.

New York State No-Fault Claim Severity, 2001:Q1–2010:Q2

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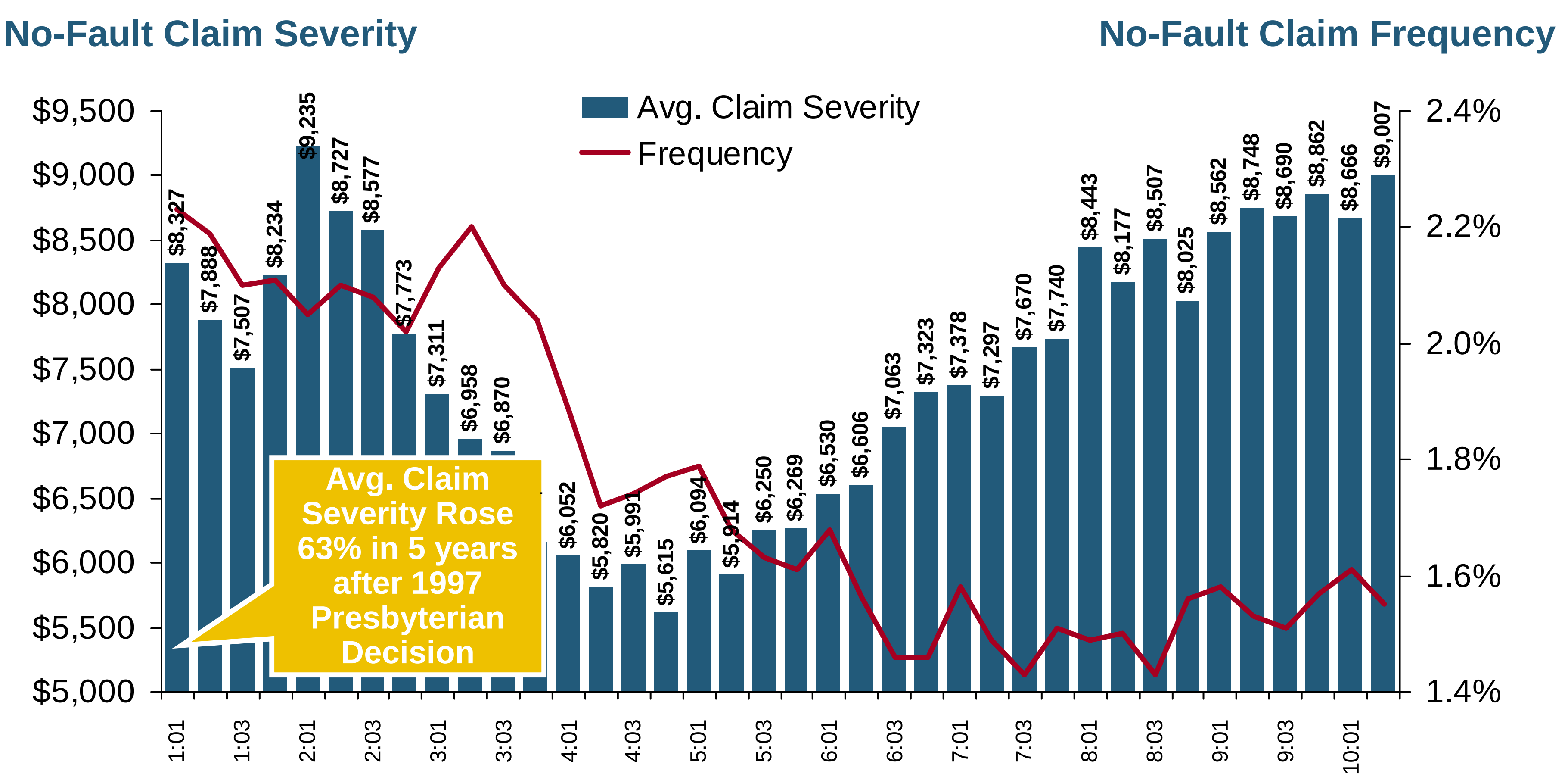

About 20% of No-Fault Claim Costs Are Attributable to Fraud and Abuse

Sources: ISO/PCI *Fast Track* data; Insurance Information Institute.

Estimated Per-Claim Cost of No-Fault Fraud in New York State, 2005-2010F*

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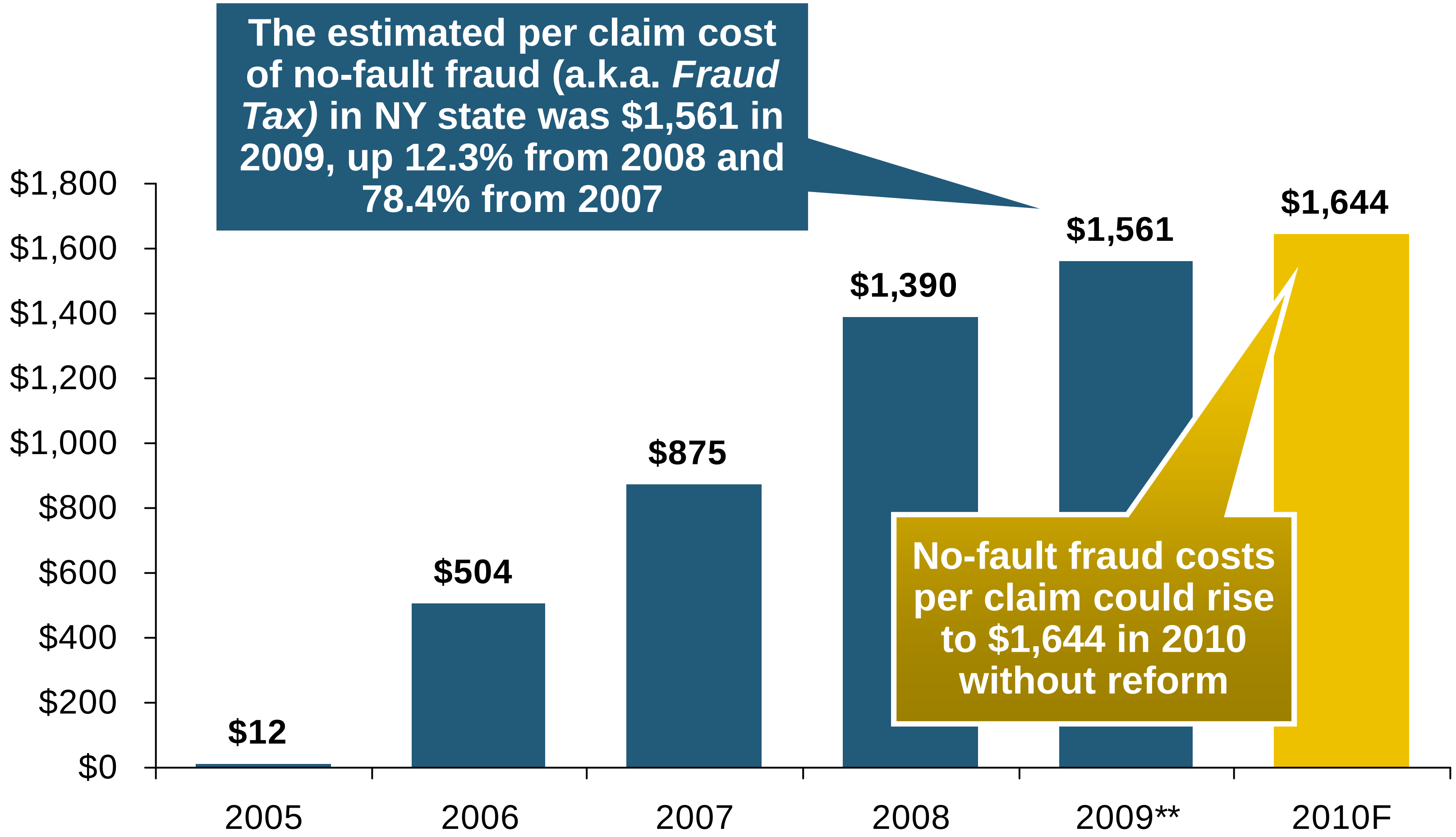

*No-fault severity reached a post-reform low in 2004 before, hence selection of 2005 as the first year of analysis. Actual no-fault losses in 2005 and beyond are higher than estimates indicate due to base level of fraud imbedded in 2004 data.
**2009 figure is estimated based on 4 quarters ending 2009:Q3 (latest available).
Source: Insurance Information Institute analysis and research.

Insurance Information Institute Online:

www.iii.org

Thank you for your time and your attention!