Reasons for Optimism in the P-C Insurance Industry

Challenges & Opportunities: 2011 & Beyond

Professional Insurance Association of Ohio
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Presentation Outline

- Reasons for Optimism, Causes for Concern
- Insurance Industry Financial Overview & Outlook
  - Profitability
  - Premium Growth
  - Capital & Capacity
  - Underwriting Performance: Commercial & Personal 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: Personal & 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 Will Begin in 2nd 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

Source: Insurance Information Institute.
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, Energy

Source: Insurance Information Institute.
Profitability

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

- 2005 ROE* = 9.6%
- 2006 ROE = 12.7%
- 2007 ROE = 10.9%
- 2008 ROE = 0.3%
- 2009 ROAS¹ = 5.8%
- 2010:H1 ROAS = 6.3%

P-C Industry 2010:H1 profits rose $10.6B from $6.0B in 2009:H1, due mainly to $2.2B in realized capital gains vs. -$11.1B in previous realized capital losses.
P/C Profitability Is Cyclical and Volatile

Sources: ISO, Fortune; Insurance Information Institute.
The P/C Insurance Industry Well Short of Its Cost of Capital in 2008 but Narrowed the Gap in 2009 and 2010

US P/C Insurers Missed Their Cost of Capital by an Average 6.7 Points from 1991 to 2002, but on Target or Better 2003-07, Fell Short in 2008-2010

The Cost of Capital is the Rate of Return Insurers Need to Attract and Retain Capital to the Business

* Return on average surplus in 2008-2010 excluding mortgage and financial guaranty insurers.
Source: The Geneva Association, Insurance Information Institute
Median ROE for Insurers vs. Financial Firms & Other Key Industries 2009

(Profits as a % of Stockholders’ Equity)

<table>
<thead>
<tr>
<th>Industry</th>
<th>ROE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Food Consumer Products</td>
<td>21%</td>
</tr>
<tr>
<td>Pharmaceuticals</td>
<td>21%</td>
</tr>
<tr>
<td>Computers, Office Equip.</td>
<td>19%</td>
</tr>
<tr>
<td>Health Insurance &amp; Mgd. Care</td>
<td>14%</td>
</tr>
<tr>
<td>Specialty Retailers</td>
<td>14%</td>
</tr>
<tr>
<td>Energy</td>
<td>12%</td>
</tr>
<tr>
<td>All Industries</td>
<td>10.5%</td>
</tr>
<tr>
<td>Diversified Financials</td>
<td>9%</td>
</tr>
<tr>
<td>Telecommunications</td>
<td>9%</td>
</tr>
<tr>
<td>Utilities</td>
<td>9%</td>
</tr>
<tr>
<td>P/C Insurance (Stock)</td>
<td>7%</td>
</tr>
<tr>
<td>L/H Insurance (Stock)</td>
<td>7%</td>
</tr>
<tr>
<td>Entertainment</td>
<td>5%</td>
</tr>
<tr>
<td>Commercial Banks</td>
<td>4%</td>
</tr>
<tr>
<td>P/C Insurance (Mutual)*</td>
<td>3.5%</td>
</tr>
<tr>
<td>L/H Insurance (Mutual)</td>
<td>0%</td>
</tr>
</tbody>
</table>

Stock P/C insurers earned a 7% ROE in 2009, below the 10.5% earned by the Fortune 500 as a whole and well below health insurers’ 14%. P/C Mutuals’ average ROE was 3.5%.

Commercial bank ROE was 4% in 2009

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

Combined Ratio / ROE

A combined ratio of about 100 generated a 7% ROE in 2009, 10% in 2005 and 16% in 1979

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.
Profitability in Ohio P/C Insurance Markets

Analysis by Line and Nearby State Comparisons
P/C profitability was higher on average in OH vs. the US overall between 1999-2008

OH: 8.5%
US: 7.0%
Pvt. Pass. Auto profitability was higher on average in OH vs. the US overall between 1999-2008.

OH: 11.2%
US: 7.5%

Sources: NAIC.
Commercial Auto profitability was higher on average in OH vs. the US overall between 1999-2008.

- OH: 9.7%
- US: 7.9%

Sources: NAIC.
Commercial MP profitability was higher on average in OH vs. the US overall between 1999-2008

OH: 9.2%
US: 7.4%

Sources: NAIC.
Homeowners profitability was lower on average in OH vs. the US overall between 1999-2008:

- OH: 2.6%
- US: 4.6%

Sources: NAIC.
All Lines: 10-Year Average RNW OH & Nearby States

1999-2008

- **Ohio**: 8.5%
- **Indiana**: 7.9%
- **U.S.**: 7.0%
- **Illinois**: 6.7%
- **Michigan**: 6.4%
- **Pennsylvania**: 6.3%
- **Kentucky**: 6.2%

Source: NAIC, Insurance Information Institute
PP Auto: 10-Year Average RNW OH & Nearby States

1999-2008

- Ohio: 11.1%
- Indiana: 8.8%
- U.S.: 7.5%
- Illinois: 7.9%
- Michigan: 6.3%
- Pennsylvania: 6.5%
- Kentucky: 1.1%

Source: NAIC, Insurance Information Institute.
Comm. Auto: 10-Year Average RNW OH & Nearby States

1999-2008

- Ohio: 9.7%
- Indiana: 9.3%
- U.S.: 8.3%
- Illinois: 7.9%
- Michigan: 9.5%
- Pennsylvania: 7.0%
- Kentucky: 5.2%

Source: NAIC, Insurance Information Institute
Comm. M-P: 10-Year Average RNW OH & Nearby States

1999-2008

- Ohio: 9.2%
- Indiana: 4.6%
- U.S.: 7.4%
- Illinois: 10.1%
- Michigan: 11.1%
- Pennsylvania: 8.1%
- Kentucky: 6.4%

Source: NAIC, Insurance Information Institute
HO: 10-Year Average RNW OH & Nearby States

1999-2008

-6.6% -2.6% 4.6% 2.1% 3.6% 14.0%

-10% -5% 0% 5% 10% 15% 20%

-3.1%

Source: NAIC, Insurance Information Institute
Average auto insurance expenditures in OH ranked 41st in the U.S.

*Latest available.
Source: NAIC; Insurance Information Institute.
Average homeowners insurance expenditures in OH ranked 45th in the U.S.

*Latest available.
Source: NAIC; Insurance Information Institute.
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

Source: Insurance Information Institute (I.I.I.) updates and research; The Financial Services Roundtable; Adapted from summary by Dewey & LeBoeuf LLP
Financial Stability Oversight Council created to oversee systemic risk of large financial holding companies) [a.k.a. TOO BIG TOO FAIL]

- P/C insurers potentially could be determined to present systemic risk to the financial system and thus be supervised by the Federal Reserve.
- Such supervision would subject such insurers to prudential standards, if the Council determines that financial distress at the company would pose a threat to the U.S. financial system.

Orderly Liquidation

- The legislation provides an “Orderly Liquidation Authority” mechanism whereby the FDIC would have enhance powers to resolve distress at financial institutions.
- Insurance holding companies and any non-insurance subsidiaries of insurers may be subject to this authority.

Source: Insurance Information Institute (I.I.I.) updates/research; The Financial Services Roundtable; Adapted from summary by Dewey & LeBoeuf LLP
Issues Related to Systemic Risk & Resolution Authority

Orderly Liquidation (cont.)

- Insurers are generally exempt from the liquidation authority, but the FDIC would have “backup authority” to place an insurer into orderly liquidation under state law if the state regulator has not done so within 60 days of a systemic risk determination.

Liquidation Fund Assessments

- The liquidation fund would be funded by assessments on large financial companies, potentially including insurers.
- But the insurance industry already has a funding system (state guaranty funds) to pay for the unwinding of failed companies. Therefore, contributions to these state guaranty funds must be considered.

Source: Insurance Information Institute (I.I.I.) updates/research; The Financial Services Roundtable; Adapted from summary by Dewey & LeBoeuf LLP
Federal Insurance Office (FIO): What Would it Do?

Duties of the Federal Insurance Office

- Establishes office within US Treasury headed by a Director appointed by Treasury Secretary, and charged with:
  - Monitor the insurance industry to gain expertise (oversight extends to all lines of insurance except health insurance, long-term care insurance and federal crop insurance).
  - Identify regulatory gaps that could contribute to a systemic crisis in the insurance industry or the U.S. financial system.
  - Gather information from the insurance industry in order to analyze such data and issue reports. May require insurers, with exception of small insurers which are exempt, to submit data and FIO director can issue subpoenas to gain such info.
  - Deal with international insurance matters.
  - Monitor the extent to which underserved communities have access to affordable insurance products.

Source: Insurance Information Institute (I.I.I.) updates/research; The Financial Services Roundtable; Adapted from summary by Dewey & LeBoeuf LLP
Federal Insurance Office (FIO): What Would It Do? (Cont.)

Duties of the Federal Insurance Office

- Establishes office within US Treasury headed by a Director appointed by Treasury Secretary, and charged with:
  - Make recommendations to the FSOC on whether an insurer (incl. reinsurers) poses a systemic risk and should be placed under supervision of the Federal Reserve.
  - Annual reports to Congress and the President on the insurance industry are required.
  - A study on the modernization of insurance regulation in the U.S. is required within 18 months, as is a report on the U.S. and global reinsurance market.
  - Oversee the federal Terrorism Risk Insurance Program.
  - Insurance will continue to be regulated by the states, but the FIO has limited preemption authority over state law in cases where it determines that state law is inconsistent with a negotiated international agreement and treats a non-U.S. insurer less favorably than a U.S. insurer.

Source: Insurance Information Institute (I.I.I.) updates/research; The Financial Services Roundtable; Adapted from summary by Dewey & LeBoeuf LLP
Title V of the Dodd-Frank bill includes the Nonadmitted and Reinsurance Reform Act (NRRA), comprising two parts:

- **Surplus Lines:**
  - Provides that the home state of the insured will have exclusive authority to regulate the placement of nonadmitted insurance.
  - Only the insured’s home state will be permitted to collect premium taxes on nonadmitted insurance.
  - The legislation also establishes a uniform system for allocation of premium tax obligations through an interstate compact or other procedures established by the states.
  - The NRRA would also establish uniform standards for surplus lines eligibility criteria by requiring capital and surplus requirements for U.S.-domiciled insurers conform to those in the NAIC’s Nonadmitted Insurance Model Act.

Source: Insurance Information Institute (I.I.I.) updates/research; The Financial Services Roundtable; Adapted from summary by Dewey & LeBoeuf LLP
Title V of the Dodd-Frank bill includes the Nonadmitted and Reinsurance Reform Act (NRRA), comprising two parts:

- Reinsurance:
  - NRRA’s reinsurance part provides that a ceding insurer’s state of domicile will be the single point of regulation with respect to credit for reinsurance, provided it is an NAIC-accredited state.
  - It also provides that a ceding insurer’s state of domicile will be the single point of regulation for purposes of:
    - The rights of the parties to provide for dispute resolution through arbitration agreements
    - Choice of law
    - Imposition of standard terms different than those in the reinsurance contract
  - The reinsurance part also provides that a reinsurer’s state of domicile will be solely responsible for regulating the reinsurer’s solvency, providing it is an NAIC-accredited state.

Source: Insurance Information Institute (I.I.I.) updates/research; The Financial Services Roundtable; Adapted from summary by Dewey & LeBoeuf LLP
Derivatives and Bureau of Consumer Financial Protection

- Derivatives:
  - The bill would require most standardized derivatives to be routed through clearinghouses and traded on exchanges.
  - Two new classes of regulated entities would be created: swap dealers and major swap participants.
  - Both would be required to register with the SEC and/or the CFTC and would be subject to margin, capital, record-keeping and business conduct requirements.

- Bureau of Consumer Financial Protection:
  - The Bill creates a new federal level entity within the Federal Reserve with the authority to regulate financial products offered to consumers.
  - Insurance products are specifically exempted from this bureau’s authority.

Source: Insurance Information Institute (I.I.I.) updates/research; The Financial Services Roundtable; Adapted from summary by Dewey & LeBoeuf LLP
A total of at least 243 new rulemakings are expected under the Dodd-Frank financial reform by Federal Agency.*

* Total eliminates double counting for joint rule-makings and this estimate only includes explicit rule-makings in the bill, and thus likely represents a significant underestimate.

Resolution Authority/Systemic Risk: Regulators may seize and break-up troubled financial firms whose collapse might cause widespread damage (i.e., systemically important companies)

- Regulator would recoup fees with more than $50B in assets
- Sets up liquidation procedure run by FDIC
- Establishes 10-member oversight council to monitor and address risks to financial stability
- Eliminates Office of Thrift Supervision (regulator of AIG’s holding company, not its insurance units which were (are) state regulated)

Volcker Rule: Largely bars largest firms largest investment firms from trading with their own funds

- Exempts insurers, asset managers and trust/custody banks, though Fed could impose Volcker Rule and capital standards on individual firms if warranted

Derivatives: Requires routine derivatives to be traded on exchanges and routed through clearinghouses

- Imposes capital, margin, reporting and record keeping and business conduct rules on firms that deal in derivatives

Consumer Financial Protection Bureau: To housed within Fed

- Will it be limited to banks/creditors

Office of National Insurance: To be established within Treasury to monitor and gather information in the insurance industry

2010 Property and Casualty Insurance Report Card

Source: Heartland Institute, May 2010

Not Graded: District of Columbia
Mississippi
Louisiana
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 287 banks have gone under as of 9/10/10)
    - *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*)

Source: Insurance Information Institute
Reasons Why P/C Insurers Have Fewer Problems Than Banks

A Superior Risk Management Model

- **Emphasis on Underwriting**
  - Matching of risk to price (via experience and modeling)
  - Limiting of potential loss exposure
  - *Some banks sought to maximize volume and fees and disregarded risk*

- **Strong Relationship Between Underwriting and Risk Bearing**
  - Insurers always maintain a stake in the business they underwrite, keeping “skin in the game” at all times
  - *Banks and investment banks package up and securitize, severing the link between risk underwriting and risk bearing, with (predictably) disastrous consequences – straightforward moral hazard problem from Econ 101*

- **Low Leverage**
  - Insurers do not rely on borrowed money to underwrite insurance or pay claims → *There is no credit or liquidity crisis in the insurance industry*

- **Conservative Investment Philosophy**
  - High quality portfolio that is relatively less volatile and more liquid

- **Comprehensive Regulation of Insurance Operations**
  - The business of insurance remained comprehensively regulated whereas a separate banking system had evolved largely outside the auspices and understanding of regulators (e.g., hedge funds, private equity, complex securitized instruments, credit derivatives – CDS’s)

- **Greater Transparency**
  - Insurance companies are an open book to regulators and the public

Source: Insurance Information Institute
Obama Administration Proposal to Scale Back Terrorism Risk Insurance Program

<table>
<thead>
<tr>
<th>Administration’s Budget Proposal for FY 2011:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Includes proposal to scale back federal support for terrorism risk insurance program</td>
</tr>
<tr>
<td>Proposal projects savings of $249 million from 2011-2020</td>
</tr>
<tr>
<td>Administration’s justification is that this would “encourage the private sector to better mitigate terrorism risk through other means, such as developing alternative reinsurance options and building safer buildings.”</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Key Concerns</th>
<th>Among Industry Observers Over Proposed Reduction in Federal Support</th>
</tr>
</thead>
<tbody>
<tr>
<td>Suggestion of changes to law would have detrimental effect on availability and affordability of terrorism insurance</td>
<td></td>
</tr>
<tr>
<td>A 2009 Aon study estimated some 70-80 percent of the commercial property insurance market would revert to absolute exclusions for terrorism, if TRIA is changed.</td>
<td></td>
</tr>
</tbody>
</table>

Source: Budget of the U.S. Government Fiscal Year 2011
## Reasons Why Concerns Are Mounting in 2010

- Perception (Reality) that U.S. vulnerability is rising
- Thwarted Christmas Day attack by “underwear bomber”
  - And new bin Laden tape claiming al Qaeda is responsible
- Foiled NYC Subway Bomber Plot (Zazi case)
- *Failed Times Square Car Bombing on May 1*
- Trials of Guantanamo 9/11 suspects in Manhattan Court (?)
- U.K. in January Raised Terror Alert Status to 2\textsuperscript{nd} Highest Level
- Increased anti-terror efforts, including full-body scans
- Effort by government to appear more vigilant, prepared
- Rise of groups such al Qaeda in the Arabian Peninsula
- U.S. military surge in Afghanistan operations
- Most buyers/producers haven’t thought about coverage recently
- *Obama Administration’s Intent to Reduce Support for TRIA*
Shifting Legal Liability & Tort Environment

Is the Tort Pendulum Swinging Against Insurers?
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

Source: Insurance Information Institute
Trial Bar Priorities

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

Source: Institute for Legal Reform.
## Trial Lawyer Poll: Which Areas Offer the Greatest Potential Benefit?

<table>
<thead>
<tr>
<th>Top Categories</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Environmental</td>
<td>14%</td>
</tr>
<tr>
<td>Insurance coverage</td>
<td>13%</td>
</tr>
<tr>
<td>Mortgage fraud</td>
<td>12%</td>
</tr>
<tr>
<td>Nursing home/ seniors issues</td>
<td>11%</td>
</tr>
<tr>
<td>Bad-faith against insurance companies</td>
<td>10%</td>
</tr>
</tbody>
</table>

*41 different practice areas were included as categories*

Source: Institute for Legal Reform poll, December 2009.
Cost of US Tort System ($ Billions)

Tort costs consumed 1.79% of GDP in 2008, down from 2.24% in 2003

Per capita “tort tax” was $? in 2009, up from $838 in 2008 and $636 in 2000

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

* 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
### 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

#### 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

#### Drop-offs
- Maine
- Vermont
- Kansas

#### Rising Above
- Texas
- South Carolina
- Hawaii

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*Midwest/West has mix of good and bad states.*

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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

Source: American Tort Reform Association; Insurance Information Institute
Average Jury Awards 1999 - 2008

Source: Jury Verdict Research; Insurance Information Institute.

*Award trends in wrongful deaths of adult males.
Source: Jury Verdict Research; Insurance Information Institute.
Sum of Top 10 Jury Awards 2004-2009

<table>
<thead>
<tr>
<th>Year</th>
<th>Award Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>$5,159</td>
</tr>
<tr>
<td>2005</td>
<td>$2,954</td>
</tr>
<tr>
<td>2006</td>
<td>$815</td>
</tr>
<tr>
<td>2007</td>
<td>$616</td>
</tr>
<tr>
<td>2008</td>
<td>$1,344</td>
</tr>
<tr>
<td>2009</td>
<td>$1,511</td>
</tr>
</tbody>
</table>

## 2009 Top Ten Jury Verdicts

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

Source: Lawyers USA, January 15, 2010.
### 2008 Top Ten Jury Verdicts

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

Source: Lawyers USA, January 13, 2009.
Medical Malpractice Tort Cost: Growth Continues, Though Modestly

($ Billions)

Over the period from 1990 through 2008, medical malpractice tort costs rose 224%, more than double the 101% increase in tort costs generally.

Med mal tort costs actually declined in 2008 for the first time since 1985.

Sources: Towers Perrin; Insurance Information Institute
The average Med Mal jury award has been relatively flat in recent years.

Average Medical Malpractice Jury Award: 2002 - 2008

Source: Jury Verdict Research; Insurance Information Institute.
How the Risk Dollar is Spent (2008)

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

**Firms w/Revenues < $1 Billion**
- Property Premiums, 15%
- Other Costs, 21%
- Admin Costs, 9%
- Prof. Liability Costs, 9%
- Retained WC Losses, 10%
- WC Premiums, 7%
- Total Mgmt. Liab., 5%
- Liability Retained Losses, 9%

**Firms w/Revenues > $1 Billion**
- Property Premiums, 12%
- Other Costs, 15%
- Admin Costs, 7%
- Prof. Liability Costs, 4%
- Retained WC Losses, 22%
- WC Premiums, 6%
- Total Mgmt. Liab., 5%
- Liability Retained Losses, 10%

Source: 2009 RIMS Benchmark Survey; Insurance Information Institute
Average Total Limits Purchased by All U.S. Firms* ($ Millions)

*Includes underlying primary limits
Source: Limits of Liability 2008, Marsh, Inc.
Excess Liability Market Capacity
North America ($ Billions)

In 2008, capacity is back to 2000 levels.

Source: Marsh, 2008 Limits of Liability Report
Insurer Defense & Cost Containment Expenses as a % of Incurred Losses, 2005-2008*

*Net of reinsurance, excl. state funds. **Liability portion only. ***Excludes products liability.
Source: National Association of Insurance Commissioners (NAIC) Annual Statement Database, via Highline Data, LLC; Insurance Information Institute.
After surging in 2007 and 2008, litigation activity related to the financial crisis began to ebb after financial markets began to recover in the 2nd quarter of 2009.

Source: Stanford University School of Law (securities.stanford.edu); Insurance Information Institute
The Financial Crisis and Poor Labor Market Conditions Have Contributed to a Surge Employment Discrimination Charges

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

Source: A.M. Best; Insurance Information Institute.
Impairment Rates Are Highly Correlated With Underwriting Performance and Reached Record Lows in 2007/08

Source: A.M. Best; Insurance Information Institute
Despite financial market turmoil and a soft market in 2009, 76% of ratings actions by A.M. Best were affirmations; just 2.9% were downgrades and 3.2% were upgrades.


Source: A.M. Best.
Deficient Loss Reserves and Inadequate Pricing Are the Leading Cause of Insurer Impairments, Underscoring the Importance of Discipline. Investment Catastrophe Losses Play a Much Smaller Role.
P/C Premium Growth Primarily Driven by the Industry’s Underwriting Cycle, Not the Economy
Soft Market Appears to Persist in 2010 but May Be Easing: Relief in 2011?

Net Written Premiums Fell 0.7% in 2007 (First Decline Since 1943) by 2.0% in 2008, and 4.2% in 2009, the First 3-Year Decline Since 1930-33.

NWP was flat with 0.0% growth in 10:H1 vs. -4.4% in 09:H1

Shaded areas denote “hard market” periods
Sources: A.M. Best (historical and forecast), ISO, Insurance Information Institute.
Countrywide Auto Insurance Expenditures Increased 2.6% in 2008 and 3.5% Pace in 2009 (est.) and 4% in 2010 (est.)

* Insurance Information Institute Estimates/Forecasts
Source: NAIC, Insurance Information Institute estimates 2008-2010 based on CPI data.
Auto Insurance Price Increases Seem to Have Leveled Off in Recent Months, Averaging 4.5% for All of 2009

* Percentage change from same month in prior year.
Average Premium for Home Insurance Policies**

* Insurance Information Institute Estimates/Forecasts  **Excludes state-run insurers.
Source: NAIC, Insurance Information Institute estimates 2008-2010 based on CPI data.
Average Commercial Rate Change, All Lines, (1Q:2004–2Q:2010)

(Percent)

Source: Council of Insurance Agents & Brokers; Insurance Information Institute
Change in Commercial Rate Renewals, by Line: 2010:Q2

Percentage Change (%)

Most Major Commercial Lines Renewed Down in Q2:2010 at a Faster Pace than a year Earlier

Source: Council of Insurance Agents and Brokers; Insurance Information Institute.
Change in Commercial Rate Renewals, by Account Size: 1999:Q4 to 2010:Q2

Percentage Change (%)

Peak = 2001:Q4 +28.5%

Market has Been Soft for 6 years and Remains Soft as Capital is Restored and Underwriting Losses Remain Modest

Pricing Turned Negative in Early 2004 and Has Been Negative Ever Since

Trough = 2007:Q3 -13.6%

KRW Effect

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

1999:Q4 = 100

Pricing today is where it was in Q4:2000 (pre-9/11)

Source: Council of Insurance Agents and Brokers; Insurance Information Institute.
Capital/Policyholder Surplus (US)

Shrinkage, but Not Enough to Trigger Hard Market
Surplus as of 6/30/10 was a near-record $530.5B, up from $437.1B at the crisis trough at 3/31/09. Prior peak was $521.8 as of 9/30/07. Surplus as of 6/30/10 is now 1.7% above 2007 peak; Crisis trough was as of 3/31/09 → 16.2% below 2007 peak.

“Surplus” is a measure of underwriting capacity. It is analogous to “Owners Equity” or “Net Worth” in non-insurance organizations.

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

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

2007:Q3 Previous Surplus Peak

Surplus set a new record in 2010:Q1*

Quarterly Surplus Changes Since 2009:Q1 Trough

<table>
<thead>
<tr>
<th>Quarter</th>
<th>Value</th>
<th>Change</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>09:Q1</td>
<td>-$84.7B</td>
<td>-16.2%</td>
<td></td>
</tr>
<tr>
<td>09:Q2</td>
<td>-$58.8B</td>
<td>-11.2%</td>
<td></td>
</tr>
<tr>
<td>09:Q3</td>
<td>-$31.8B</td>
<td>-5.9%</td>
<td></td>
</tr>
<tr>
<td>09:Q4</td>
<td>-$10.3B</td>
<td>-2.0%</td>
<td></td>
</tr>
<tr>
<td>10:Q1</td>
<td>+$18.9B</td>
<td>+3.6%</td>
<td></td>
</tr>
<tr>
<td>10:Q2</td>
<td>-$10.2B</td>
<td>-1.9%</td>
<td></td>
</tr>
</tbody>
</table>

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

Sources: ISO, A.M. Best.
Paid-in Capital, 2005–2010: H1

($ Billions)

Paid-in capital for insurance operations in 2009:H1 was $2.3B. In 2010:H1 it was a record $23.8B.

In 2010:H1 One Insurer’s Paid-in Capital Rose by $22.5B as Part of an Investment in a Non-insurance Business

Source: ISO.
Global Reinsurance Capacity Shrank in 2008, Mostly Due to Investments

Global Reinsurance Capacity

Source of Decline in 2008

Realized Capital Losses
55%

31%

14%

Change in Unrealized Capital Losses
Hurricanes

Global Reinsurance Capacity Fell by an Estimated 17% in 2008

The Financial Crisis at its Peak Ranks as the Largest “Capital Event” Over the Past 20+ Years

<table>
<thead>
<tr>
<th>Event</th>
<th>Insured Loss to Surplus Rate (Percent)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hurricane Hugo (6/30/1989)</td>
<td>3.3%</td>
</tr>
<tr>
<td>Hurricane Andrew (6/30/1992)</td>
<td>9.6%</td>
</tr>
<tr>
<td>Northridge Earthquake (12/31/93)</td>
<td>6.9%</td>
</tr>
<tr>
<td>Sept. 11 Attacks (6/30/01)</td>
<td>10.9%</td>
</tr>
<tr>
<td>Florida Hurricanes (6/30/04)</td>
<td>6.2%</td>
</tr>
<tr>
<td>Hurricane Katrina (6/30/05)</td>
<td>13.8%</td>
</tr>
<tr>
<td>Financial Crisis as of 3/31/09**</td>
<td>16.2%</td>
</tr>
</tbody>
</table>

* 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*

Surplus growth is now positive but premiums continue to fall, a departure from the historical pattern

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

$ 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

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.
Capital losses have turned to capital gains, aiding earnings.

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

Treasury yield curve is near its most depressed level in at least 45 years. Investment income is falling as a result.

Stock Dividend Cuts Have Further Pressured Investment Income

Sources: Board of Governors of the United States Federal Reserve Bank; Insurance Information Institute.
Treasury Yields Are Low and Expected to Remain Low Through 2011

Short-term yields remain very depressed, impacting insurers’ ability to generate investment earnings.

The ability of reserves releases to favorably impact calendar year results will diminish over time as reserved redundancies fall.

Sources: Board of Governors of the United States Federal Reserve Bank; Blue Chip Economic Indicators, 9/10; Insurance Information Institute.
Reduction in Combined Ratio Necessary to Offset 1% Decline in Investment Yield to Maintain Constant ROE, by Line*

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

*Based on 2008 Invested Assets and Earned Premiums
**US domestic reinsurance only
Source: A.M. Best; Insurance Information Institute.
Portfolio Facts

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

Sources: NAIC; Insurance Information Institute research.
Underwriting Trends – Financial Crisis Does Not Directly Impact Underwriting Performance: Cycle, Catastrophes Were 2008’s Drivers
As Recently as 2001, Insurers Paid Out Nearly $1.16 for Every $1 in Earned Premiums

Heavy Use of Reinsurance Lowered Net Losses

Relatively Low CAT Losses, Reserve Releases

Relatively Low CAT Losses, Reserve Releases

As Recently as 2001, Insurers Paid Out Nearly $1.16 for Every $1 in Earned Premiums

Heavy Use of Reinsurance Lowered Net Losses

Relatively Low CAT Losses, Reserve Releases

Relatively Low CAT Losses, Reserve Releases

Lower CAT Losses, More Reserve Releases


Sources: A.M. Best, ISO.
Underwriting Gain (Loss)
1975–2010:H1*

Cumulative underwriting deficit from 1975 through 2009 is $445B

The industry recorded a $5.1B underwriting loss in 2010:H1 compared to $2.1B in 2009:H1

Large Underwriting Losses Are NOT Sustainable in Current Investment Environment

* Includes mortgage and financial guarantee insurers.
Sources: A.M. Best, ISO; Insurance Information Institute.
Prior year reserve releases totaled $8.8 billion in the first half of 2010, up from $7.1 billion in the first half of 2009.

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.
Calendar Year vs. Accident Year
P/C Combined Ratio: 1992–2010E¹

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

Note: 2005 reserve development excludes a $6 billion loss portfolio transfer between American Re and Munich Re. Including this transaction, total prior year adverse development in 2005 was $7 billion. The data from 2000 and subsequent years excludes development from financial guaranty and mortgage insurance.

Sources: Barclay’s Capital; A.M. Best.
Number of Years with Underwriting Profits by Decade, 1920s–2000s

- 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.

Sources: A.M. Best (historical) Conning forecasts for 2010 - 2012; Insurance Information Institute.
Net 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.

Sources: A.M. Best (historical) Conning forecasts for 2010 - 2012; Insurance Information Institute.
Insurance, Monopoly and Workers Compensation: in Ohio

What Does Economics Have to Say About Monopoly in Workers Compensation Insurance Markets?

The Debate Over WC in Ohio
**Figure 1: Economic Test for Rationalization of Monopoly, 2010 vs. 1910**

<table>
<thead>
<tr>
<th>Economic Tests that Could Be Used to Rationalize the Existence of Monopoly in Workers Compensation</th>
<th>Do the Criteria Apply in 2010?</th>
<th>Observations</th>
<th>Did the Criteria Apply in 1910?</th>
<th>Observations</th>
</tr>
</thead>
</table>
| Does any insurer have exclusive ownership of a resource, expertise or capital necessary to write workers compensation coverage? | No | • 46 states allow private sector competition  
• 764 private insurers wrote workers comp insurance in these 46 states in 2009 | Possibly | • State insurers often would have been in a better position to secure capital, data |
| Do any insurers have an exclusive patent or process necessary to write workers compensation insurance? | No | • Actuarial and underwriting methodologies for workers compensation are similar throughout the industry  
• Necessary skills/expertise and technology can be readily acquired through training or purchase | N/A | • There were established actuarial or underwriting procedures for WC in 1910 |
| Do high fixed costs render the cost of providing workers compensation too high unless there is just a single provider of coverage? | No | • The marginal cost of offering workers comp in Ohio is relatively low, especially for insurers already offering the coverage in other states | Yes (in Some States) | • Creating a WC product and distribution system would have been costly |

Source: Insurance Information Institute
Rationale for Government Monopoly & The Standard Monopoly Critique

- Governments Do Not Create or Sanction Monopolies for the Purpose of Wealth Creation

- Governments Create Monopolies When They Believe the Public Interest Is Being Served
  - To provide a necessary service that otherwise would be unavailable
  - To provide a service that otherwise would be unaffordable to most
  - To create an unavoidable service (e.g., toll road)

- Any Level of Government Can Create a Monopoly: Federal, State, Local

Standard Critique of Monopoly

- Monopolies (Including Government Monopolies) Produce Products and Services that Are of Inferior Quality
  - Due to the fact that the monopolist has no market-based incentive to provide high-quality service or to improve
  - Market share and finances are guaranteed by the government
  - No external benchmark for performance
  - In contrast, competition drives sellers to improve/innovate or lose market share

- The Quality-of-Product Issue is One of the Most Frequently Leveled Criticisms Against Government Monopolies
  - Examples: DMVs, highway maintenance, education, sanitation, public safety
Competition and Workers Compensation in the 21st Century: Market Observations

- **46 or the 50 State Allow Competition in their Worker Comp Markets**
  - Means most states believe competition in WC markets is feasible and desirable
  - Also implies that insurance departments can adequately regulate WC market

- **764 Insurers (Comprised of 314 Insurance Groups) Wrote Workers Coverage in 2009**
  - By U.S. Dept. of Justice standards, the WC market in every non-monopolistic fund state fits the definition of “competitive” (no antitrust concerns)
  - Even the largest WC carrier had only an 11% market share nationally in 2009

- **Barriers to Entry in Workers Compensation Are Low**
  - New insurers can enter WC markets with relative ease

- **Many Insurers Compete in States Near/Like Ohio**
  - IN: 88; PA: 85; IL: 95; MI: 62; WI: 82
  - If OH were competitive today, 65-85 private insurers would likely be writing coverage

- **No Traditional Economic Criteria that Would Justify the Existence of Monopoly Exist in 2010**
  - In 1910, the situation was different

- **Residual Market Shares Are Very Small and Are Shrinking**
  - Nationally, WC residual market share was just 5% of DPW in 2009 (NCCI states)
  - Combined underwriting loss of these states was just $75 million in 2009
Where Will the Growth in WC Exposure Come From?

Industry and Occupation Growth Analysis

WC exposure growth the fastest in the health, science and tech areas

<table>
<thead>
<tr>
<th>Occupations</th>
<th>Percent change</th>
<th>Number of new jobs (in thousands)</th>
<th>Wages (May 2008 median)</th>
<th>Education/ training category</th>
</tr>
</thead>
<tbody>
<tr>
<td>Biomedical engineers</td>
<td>72</td>
<td>11.6</td>
<td>$ 77,400</td>
<td>Bachelor's degree</td>
</tr>
<tr>
<td>Network systems and data communications analysts</td>
<td>53</td>
<td>155.8</td>
<td>71,100</td>
<td>Bachelor's degree</td>
</tr>
<tr>
<td>Home health aides</td>
<td>50</td>
<td>460.9</td>
<td>20,460</td>
<td>Short-term on-the-job training</td>
</tr>
<tr>
<td>Personal and home care aides</td>
<td>46</td>
<td>375.8</td>
<td>19,180</td>
<td>Short-term on-the-job training</td>
</tr>
<tr>
<td>Financial examiners</td>
<td>41</td>
<td>11.1</td>
<td>70,930</td>
<td>Bachelor's degree</td>
</tr>
<tr>
<td>Medical scientists, except epidemiologists</td>
<td>40</td>
<td>44.2</td>
<td>72,590</td>
<td>Doctoral degree</td>
</tr>
<tr>
<td>Physician assistants</td>
<td>39</td>
<td>29.2</td>
<td>81,230</td>
<td>Master's degree</td>
</tr>
<tr>
<td>Skin care specialists</td>
<td>38</td>
<td>14.7</td>
<td>28,730</td>
<td>Postsecondary vocational award</td>
</tr>
<tr>
<td>Biochemists and biophysicists</td>
<td>37</td>
<td>8.7</td>
<td>82,840</td>
<td>Doctoral degree</td>
</tr>
<tr>
<td>Athletic trainers</td>
<td>37</td>
<td>6.0</td>
<td>39,640</td>
<td>Bachelor's degree</td>
</tr>
<tr>
<td>Physical therapist aides</td>
<td>36</td>
<td>16.7</td>
<td>23,760</td>
<td>Short-term on-the-job training</td>
</tr>
<tr>
<td>Dental hygienists</td>
<td>36</td>
<td>62.9</td>
<td>66,570</td>
<td>Associate degree</td>
</tr>
<tr>
<td>Veterinary technologists and technicians</td>
<td>36</td>
<td>28.5</td>
<td>28,900</td>
<td>Associate degree</td>
</tr>
<tr>
<td>Dental assistants</td>
<td>36</td>
<td>105.6</td>
<td>32,380</td>
<td>Moderate-term on-the-job training</td>
</tr>
<tr>
<td>Computer software engineers, applications</td>
<td>34</td>
<td>175.1</td>
<td>85,430</td>
<td>Bachelor's degree</td>
</tr>
<tr>
<td>Medical assistants</td>
<td>34</td>
<td>163.9</td>
<td>28,300</td>
<td>Moderate-term on-the-job training</td>
</tr>
<tr>
<td>Physical therapist assistants</td>
<td>33</td>
<td>21.2</td>
<td>46,140</td>
<td>Associate degree</td>
</tr>
<tr>
<td>Veterinarians</td>
<td>33</td>
<td>19.7</td>
<td>79,050</td>
<td>First professional degree</td>
</tr>
<tr>
<td>Self-enrichment education teachers</td>
<td>32</td>
<td>81.3</td>
<td>35,720</td>
<td>Work experience in a related occupation</td>
</tr>
<tr>
<td>Compliance officers, except agriculture, construction, health and safety, and transportation</td>
<td>31</td>
<td>80.8</td>
<td>48,890</td>
<td>Long-term on-the-job training</td>
</tr>
</tbody>
</table>

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

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

<table>
<thead>
<tr>
<th>Occupations</th>
<th>Number of new jobs (in thousands)</th>
<th>Percent change</th>
<th>Wages (May 2008 median)</th>
<th>Education/ training category</th>
</tr>
</thead>
<tbody>
<tr>
<td>Registered nurses</td>
<td>581.5</td>
<td>22</td>
<td>$ 62,450</td>
<td>Associate degree</td>
</tr>
<tr>
<td>Home health aides</td>
<td>460.9</td>
<td>50</td>
<td>20,460</td>
<td>Short-term on-the-job training</td>
</tr>
<tr>
<td>Customer service representatives</td>
<td>399.5</td>
<td>18</td>
<td>29,860</td>
<td>Moderate-term on-the-job training</td>
</tr>
<tr>
<td>Combined food preparation and serving workers, including fast food</td>
<td>394.3</td>
<td>15</td>
<td>16,430</td>
<td>Short-term on-the-job training</td>
</tr>
<tr>
<td>Personal and home care aides</td>
<td>375.8</td>
<td>46</td>
<td>19,180</td>
<td>Short-term on-the-job training</td>
</tr>
<tr>
<td>Retail salespersons</td>
<td>374.7</td>
<td>8</td>
<td>20,510</td>
<td>Short-term on-the-job training</td>
</tr>
<tr>
<td>Office clerks, general</td>
<td>358.7</td>
<td>12</td>
<td>25,320</td>
<td>Short-term on-the-job training</td>
</tr>
<tr>
<td>Accountants and auditors</td>
<td>279.4</td>
<td>22</td>
<td>59,430</td>
<td>Bachelor's degree</td>
</tr>
<tr>
<td>Nursing aides, orderlies, and attendants</td>
<td>276.0</td>
<td>19</td>
<td>23,850</td>
<td>Postsecondary vocational award</td>
</tr>
<tr>
<td>Postsecondary teachers</td>
<td>256.9</td>
<td>15</td>
<td>58,830</td>
<td>Doctoral degree</td>
</tr>
<tr>
<td>Construction laborers</td>
<td>255.9</td>
<td>20</td>
<td>28,520</td>
<td>Moderate-term on-the-job training</td>
</tr>
<tr>
<td>Elementary school teachers, except special education</td>
<td>244.2</td>
<td>16</td>
<td>49,330</td>
<td>Bachelor's degree</td>
</tr>
<tr>
<td>Truck drivers, heavy and tractor-trailer</td>
<td>232.9</td>
<td>13</td>
<td>37,270</td>
<td>Short-term on-the-job training</td>
</tr>
<tr>
<td>Landscaping and groundskeeping workers</td>
<td>217.1</td>
<td>18</td>
<td>23,150</td>
<td>Short-term on-the-job training</td>
</tr>
<tr>
<td>Bookkeeping, accounting, and auditing clerks</td>
<td>212.4</td>
<td>10</td>
<td>32,510</td>
<td>Moderate-term on-the-job training</td>
</tr>
<tr>
<td>Executive secretaries and administrative assistants</td>
<td>204.4</td>
<td>13</td>
<td>40,030</td>
<td>Work experience in a related occupation</td>
</tr>
<tr>
<td>Management analysts</td>
<td>178.3</td>
<td>24</td>
<td>73,570</td>
<td>Bachelor's or higher degree, plus work experience</td>
</tr>
<tr>
<td>Computer software engineers, applications</td>
<td>175.1</td>
<td>34</td>
<td>85,430</td>
<td>Bachelor's degree</td>
</tr>
<tr>
<td>Receptionists and information clerks</td>
<td>172.9</td>
<td>15</td>
<td>24,550</td>
<td>Short-term on-the-job training</td>
</tr>
<tr>
<td>Carpenters</td>
<td>165.4</td>
<td>13</td>
<td>38,940</td>
<td>Long-term on-the-job training</td>
</tr>
</tbody>
</table>

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

(Thousands)

Health Care and Social Assistance: 4,017
Professional, Scientific, Tech. Srvs.: 2,657
Education Services: 1,683
Administration, Support, Waste Mgmt & Removal: 1,431
Accommodation & Food Services: 838
Government: 788
Other Services (excl. Govt.): 704
Retail Trade: 654
Transportation and Warehousing: 446
Finance & Insurance: 322
Arts, Entertainment & Recreation: 304
Wholesale Trade: 256
Real Estate, Rental & Leasing: 236
Information: 118
Mgmt. of Companies & Enterprises: 102


Health, Science and Education will be important sources of exposure growth for WC insurers this decade.
Employment in high WC frequency/severity occupational classes will be flat over the next decade. Construction is expected to rebound from its recession lows but the long-term decline in US manufacturing employment will continue.

*Category includes truck drivers and drivers/sales personnel.

Many High Hazard Occupations Have Declined Disproportionately Over the Past Decade

Change in Employment (%), 2000 vs. 2009*

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

*I.I.I. calculations based on monthly seasonally adjusted data converted to annual averages.
Claim Trends in Auto Insurance

Rising Costs Held in Check by Falling Frequency: Can That Pattern Be Sustained?
Bodily Injury: Severity Trends Generally Above Decline in Frequency

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:Q1.
Source: ISO/PCI Fast Track data; Insurance Information Institute
Property Damage Liability: Frequency and Severity Trends Nearly Offset in 2009/10

Annual Change, 2005 through 2010*

- Frequency
- Severity

-1.6% 3.6% 2.1% 1.4% 0.3% 0.6%

2005 2006 2007 2008 2009 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:Q1.
Source: ISO/PCI Fast Track data; Insurance Information Institute
No-Fault (PIP) Liability: Frequency and Severity Trends Are Adverse*

Annual Change, 2005 through 2010*

- Frequency: 4.7%, 2.4%, 6.3%, 6.4%, 6.5%, 7.4%
- Severity: -4.8%, -5.7%, -2.7%, -6.9%, 5.9%, 5.0%

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:Q1.

Source: ISO/PCI Fast Track data; Insurance Information Institute
Collision Coverage: Frequency and Severity Trends Have Been Favorable

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:Q1.
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:Q1.
Source: ISO/PCI Fast Track data; Insurance Information Institute
The Economic Storm

What the Financial Crisis and Recession Mean for the Industry’s Exposure Base, Growth and Profitability
US Real GDP Growth*

The Q4:2008 decline was the steepest since the Q1:1982 drop of 6.8%

Recession began in Dec. 2007. Economic toll of credit crunch, housing slump, labor market contraction has been severe but modest recovery is underway.

Economic growth up sharply in late 2009 with rebuilding of inventories and stimulus. More moderate growth expected in 2010/11 but no “double dip”

Demand Commercial Insurance Continues To Be Impacted by Sluggish Economic Conditions

* Estimates/Forecasts from Blue Chip Economic Indicators.
Source: US Department of Commerce, Blue Economic Indicators 7/10; Insurance Information Institute.
Length of US Business Cycles, 1929–Present*

Duration (Months)

Average Duration**
Recession = 10.4 Mos
Expansion = 60.5 Mos

Length of Expansions Greatly Exceeds Contractions

The “Great Recession” lasted 18 months, longest since Great Depression

** Post-WW II period through end of most recent expansion.
Sources: National Bureau of Economic Research; Insurance Information Institute.
Real GDP Growth vs. Real P/C
Premium Growth: Modest Association

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

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

Sources: A.M. Best, US Bureau of Economic Analysis, Blue Chip Economic Indicators, 9/10; Insurance Information Institute
Will Future Tax Policy Impact P/C Insurance Industry Exposure and Growth?

Various Tax Proposals for 2011 Could Have Significant Impacts on the P/C Insurance Industry for Years to Come
# Potential Impacts of Current Federal Tax Proposals on P/C Insurance Industry

<table>
<thead>
<tr>
<th>Proposal</th>
<th>Potential P/C Insurance Industry Impact</th>
<th>P/C Lines that Benefit</th>
</tr>
</thead>
</table>
| 100% Expensing of New Investment in Plant & Equipment in 2011 and Continuation of Bonus Depreciation | Could produce a 5-10% surge in investment in physical plant and equipment in 2011 which will need to be insured immediately. Although the proposal only “steals” investment from the future, this provides a permanent benefit to commercial insurers since insurance coverage must be purchased sooner and be maintained. New construction activity boosts WC and surety. | • Commercial Property  
• Construction  
• Commercial Liability  
• Commercial Auto  
• Specialty Lines  
• Excess & Surplus  
• Workers Comp  
• Surety  
• Reinsurance |
| Reinstall 36% and 39.6% Rates for High Income Taxpayers >$250K            | Potential damage to new/small business formation and growth. Weakness in these areas has hurt p/c insurance exposure and tax hikes could depress insurance exposure in this segment | • None |
| Continue 2001 and 2003 Tax Cuts for All Taxpayers                        | Should produce an environment that more beneficial to recovery in small business segment & associate insurance exposures | • Small Business Commercial Lines  
• Personal Lines |

Sources: Proposals from Tax Policy Center; P/C discussion is Insurance Information Institute research.
### Potential Impacts of Current Federal Tax Proposals on P/C Insurance Industry (cont’d)

<table>
<thead>
<tr>
<th>Proposal</th>
<th>Potential P/C Insurance Industry Impact</th>
<th>P/C Lines that Benefit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Impose 20% Tax Rate for Capital Gains and Dividends for High Income Taxpayers</td>
<td>The increase in dividends and capital gains taxes makes private investment less attractive. Under current law the rate is 15%. Additional taxes on investment would presumably result in a marginal but negative impact on p/c insurance exposure.</td>
<td>•None</td>
</tr>
<tr>
<td>Payroll Tax Holiday</td>
<td>Reducing the cost of hiring workers would theoretically reduce the cost of employment and should spark hiring, increasing overall employment and payrolls</td>
<td>•Workers comp</td>
</tr>
<tr>
<td>Limit Value of Itemized Deductions to 28% for High Income Taxpayers</td>
<td>Will have an unambiguously negative impact on charitable giving. Nonprofit sector will be negatively impacted.</td>
<td>•None (Commercial lines products Designed for NPOs would be negatively impacted; This is a large p/c market.)</td>
</tr>
</tbody>
</table>

Sources: Proposals (except Payroll Tax Holiday) from Tax Policy Center; P/C discussion is Insurance Information Institute research.
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

Mountain States
- Rocky Mountain: 2.2%
- Plains: 2.0%

Plains States
- Great Lakes: -0.4%
- Mideast: 1.3%
- New England: 1.0%

Southwest States
- Southwest: 1.7%

Lowest Quintile
- Far West: 0.6%

Highest Quintile
- US = 0.7
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

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

Massive Job Losses Sapped the Economy and Commercial/Personal Lines Exposure, But Trend is Improving
Unemployment and Underemployment Rates: Rocketed Up in 2008-09; Stabilizing in 2010?

January 2000 through August 2010, Seasonally Adjusted (%)

- Traditional Unemployment Rate U-3
- Unemployment + Underemployment Rate U-6

- Recession ended in November 2001
- Unemployment kept rising for 19 more months
- Recession began in December 2007

U-6 went from 8.0% in March 2007 to 17.5% in Oct 2009; Stood at 16.7% in July 2010

Unemployment rate was 9.6% in August

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

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

US Unemployment Rate

Rising unemployment eroded payrolls and workers comp’s exposure base.

Unemployment likely peaked at 10% in late 2009.

Unemployment forecasts remain stubbornly high through 2011

* = actual;          = forecasts

Sources: US Bureau of Labor Statistics; Blue Chip Economic Indicators (9/10); Insurance Information Institute
Unemployment will remain high even under the most optimistic of scenarios, but forecasts are being revised downwards.

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

Sources: Blue Chip Economic Indicators (9/10); Insurance Information Institute
Unemployment Rates Vary Widely by State and Region: July 2010*

Unemployment in July was far above average in OH, 10.3% vs. 9.5% nationally.

*Provisional figures for July 2010, seasonally adjusted.
Unemployment Rates Vary Widely by State and Region: July 2010* (cont’d)

*Provisional figures for July 2010, seasonally adjusted.
The job gain and loss figures in 2010 are severely distorted by the hiring and termination of temporary Census workers. So far in 2010, 763,000 *private sector* jobs have been created.

Job losses since the recession began in Dec. 2007 peaked at 8.4 million in Dec. 09; stands at 7.7 million through August 2010; 14.9 million people are now defined as unemployed.

*Estimate based on Reuters poll of economists.

Labor Underutilization: Broader than Just Unemployment

% of Labor Force

Marginally Attached and Unemployed Persons Account for 16.7% of the Labor Force in August 2010 (1 Out 6 People). Unemployment Rate Alone was 9.6%. Underutilization Shows a Broader Impact on WC and Other Commercial Exposures

NOTE: Marginally attached workers are persons who currently are neither working nor looking for work but indicate that they want and are available for a job and have looked for work sometime in the recent past. Discouraged workers, a subset of the marginally attached, have given a job-market related reason for not looking currently for a job. Persons employed part time for economic reasons are those who want and are available for full-time work but have had to settle for a part-time schedule.

The US Economy Lost About 8.4 Million Jobs in the Two Years from Dec. 07 – Dec. 09.

As employment expands, workers comp will be among the first lines to see exposure gains.
Estimated Effect of Recessions* on Payroll (Workers Comp Exposure)

(Percent Change) (All Post WWII Recessions)

Recessions in the 1970s and 1980s saw smaller exposure impacts because of continued wage inflation, a factor not present during the 2007-2009 recession.

The Dec. 2007 to mid-2009 recession caused the largest impact on WC exposure in 60 years.

Recession Dates (Beginning/Ending Years)


*Data represent maximum recorded decline over 12-month period using annualized quarterly wage and salary accrual data.
Source: Insurance Information Institute research; Federal Reserve Bank of St. Louis (wage and salary data); National Bureau of Economic Research (recession dates).
Frequency: 1926–2008
A Long-Term Drift Downward

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

Note: Recessions indicated by gray bars.
Sources: NCCI from US Bureau of Labor Statistics; National Bureau of Economic Research
Insurance Industry
Employment Trends: 1990-2010

Robert P. Hartwig, Ph.D., CPCU, President & Economist
Insurance Information Institute ♦ 110 William Street ♦ New York, NY 10038
Tel: 212.346.5520 ♦ Cell: 917.453.1885 ♦ bobh@iii.org ♦ www.iii.org
September 2010 Report: Employment Highlights*

- **P-C Insurers**
  - Employment down by 400 (-0.1%) vs. June 2010
  - Employment down by 17,700 (-3.7%) vs. July 2009

- **Reinsurers**
  - Employment up by 100 (+0.4%) vs. June 2010
  - Employment down by 1,400 (-5.1%) vs. July 2009

- **Claims Adjusters**
  - Employment up by 400 (+0.9%) vs. June 2010
  - Employment down by 4,800 (-9.9%) vs. July 2009

- **Insurance Agents & Brokers**
  - Employment up by 700 (+0.1%) vs. June 2010
  - Employment down by 16,300 (-2.5%) vs. July 2009

- **Life Insurers**
  - Employment down by 1,200 (-0.3%) vs. June 2010
  - Employment down by 5,500 (-1.6%) vs. July 2009

- **Health/Medical Insurers**
  - Employment down by 4,100 (-0.9%) vs. June 2010
  - Employment down by 7,200 (-1.6%) vs. July 2009

*Data are through July 2010 and are preliminary (i.e., subject to later revision)
Baselines:
U.S. Employment Trends
U.S. Nonfarm Employment, Monthly, 1990–2010*

*As of August 2010; Not seasonally adjusted

Note: Recessions indicated by gray shaded columns.
Sources: US Bureau of Labor Statistics; National Bureau of Economic Research (recession dates); Insurance Information Institutes.

*As of August 2010; Not seasonally adjusted

Note: Recessions indicated by gray shaded columns.

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

Soft Market, Difficult Economy, Outsourcing, Productivity Enhancements and Consolidation Have Contributed to Industry’s Job Losses
As of July 2010, P/C insurance industry employment was down by 26,900 or 5.5% to 464,200 since the recession began in Dec. 2007 (compared to overall US employment decline of 7.2%).

*As of July 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.
As of July 2010, Life insurance industry employment was down by 10,400 or 2.9% to 343,900 since the recession began in Dec. 2007 (compared to overall US employment decline of 7.2%).

*As of July 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.
As of July 2010, Health-Medical insurance industry employment was down by 11,300 or 2.6% to 430,600 since the recession began in Dec. 2007 (compared to overall US employment decline of 7.2%).

*As of July 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.
As of July 2010, US employment in the reinsurance industry was down by 1,000 or 3.7% to 25,900 since the recession began in Dec. 2007 (compared to overall US employment decline of 7.2%).

*As of July 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.
As of July 2010, employment at insurance agencies and brokerages was down by 47,900 or 7.0% to 631,700 since the recession began in Dec. 2007 (compared to overall US employment decline of 7.2%).

*As of July 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.
As of July 2010, claims adjusting employment was down by 8,100 or 15.6% to 43,900 since the recession began in Dec. 2007 (compared to overall US employment decline of 7.2%).

*As of July 2010; Not seasonally adjusted.
Note: Recessions indicated by gray shaded columns.
Sources: US Bureau of Labor Statistics; National Bureau of Economic Research (recession dates); Insurance Information Institutes.
U.S. Employment in Third-Party Administration of Insurance Funds: 1990–2010*

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

Note: Recessions indicated by gray shaded columns.

Sources: US Bureau of Labor Statistics; National Bureau of Economic Research (recession dates); Insurance Information Institutes.
Crisis-Driven Exposure Drivers

Economic Obstacles to Growth in P/C Insurance
Auto/Light Truck Sales, 1999-2011F

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

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

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

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

Source: U.S. Department of Commerce; Blue Chip Economic Indicators (9/10); Insurance Information Institute.
New home starts plunged 34% from 2005-2007; drop through 2009 was 72% (est.); A net annual decline of 1.49 million units, lowest since records began in 1959.

I.I.I. estimates that each incremental 100,000 decline in housing starts costs home insurers $87.5 million in new exposure (gross premium). The net exposure loss in 2009 vs. 2005 is estimated at about $1.3 billion.

Little Exposure Growth Likely for Homeowners Insurers Due to Weak Home Construction Forecast for 2010-2011. Also Affects Commercial Insurers with Construction Risk Exposure, Surety.
Percent Changes in Residential Fixed Investment, 2006:Q2-2010:Q1*

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

*seasonally adjusted
Source: U.S. Department of Commerce, Bureau of Economic Analysis
Average size of completed new homes often falls in recessions (yellow bars), but historically bounces back in expansions.

The trend to building larger homes reversed in 2008, affecting exposure growth beyond the decline in number of units built. Trend may now be reversing.

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

The unemployment rate appears to be closely correlated with the uninsured motorist percentage. In 2010 roughly 18% of motorists are expected to be driving without insurance as high unemployment prompts some people to drop coverage.

Source: Uninsured Motorists, 2008 Edition, Insurance Research Council; Blue Chip Economic Indicators (Unemployment data, including forecasts); Insurance Information Institute.
New Boat Sales Symptomatic of Decline in Insured Exposure Growth for Luxury/Discretionary Items

Boat sales fell by 16% in 2008 and the value of those sales plunged by 21%

There were 60,837 business bankruptcies in 2009, up 40% from 2008 and the most since 1993. 2010:H1 bankruptcies totaled 29,059, down 4% from H1:2009, but still very high by historical standards.

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*

180,000 businesses started in 2009:Q4, the best quarter in 2009. 2009 was the slowest year for new business starts since 1993.

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

Thousands


April 2010: Many banks are maintaining tight loan standards; some are tightening further; virtually no one loosening; Hurts business formation/expansion and commercial exposure

FDIC-Insured Institutions Had $541.1B (-13.1%) Less in Outstanding Loans in These Three Categories at Year-end 2009 vs. 2008, and Even Less at End of 2010:Q1

<table>
<thead>
<tr>
<th>Category</th>
<th>2008</th>
<th>2009</th>
<th>2010:Q1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Construction and Development Secured by Real Estate</td>
<td>$590.9</td>
<td>$451.5</td>
<td>$417.97</td>
</tr>
<tr>
<td>Commercial and Industrial</td>
<td>$1,494.0</td>
<td>$1,220.8</td>
<td>$1,187.61</td>
</tr>
<tr>
<td>1-4 Family Residential Mortgages</td>
<td>$2,045.2</td>
<td>$1,916.7</td>
<td>$1,887.37</td>
</tr>
</tbody>
</table>

Source: FDIC Quarterly Banking Profile, First Quarter 2010, Table II-A
Investment in Equipment & Software is forecast to be positive in both 2010 and 2011.

Investment in Structures is forecast to be down in 2010 and low in 2011. This will hold exposure in many commercial lines down.

Sources: Bureau of Economic Analysis, U.S. Department of Commerce (history); Wells Fargo Securities Economics Group, Monthly Outlook, April 7, 2010 (forecasts)
Total Industrial Production

2007:Q1 to 2011:Q4F (%)

Economic slowdown is reducing industrial production.

Industrial Production is Aided by a Rebuild of Inventories, Gradual Economic Recovery and Stimulus Program (Q2:09 through 2010).

End of Recession in mid-2009, Stimulus Program Benefited Industrial Production and Insurance Exposure Both Directly and Indirectly, Albeit it Very Modestly; Stimulus Effect is Waning in 2010 and Will Be Gone in 2011.

Sources: US Bureau of Labor Statistics; Blue Chip Economic Indicators (9/10); Insurance Information Institute
Recovery in Capacity Utilization is a Positive Sign for Insurance Exposure

Percent of Capacity Utilized (Manufacturing, Mining, Utilities)

“Full Capacity”

Recession began December 2007

Manufacturing capacity stood at 74.8% in July 2010, above the June 2009 low of 68.2% but well below the pre-crisis peak of 80%+

The closer the economy is to operating at “full capacity,” the greater the demand for insurance

March 2001- November 2001 recession

Recession began December 2007

State & Local Government Finances in Dire Straits

Large, Long-Term Cuts Necessary to Align Spending with Shrinking Tax Revenues
Year-Over-Year Change in Quarterly US State Tax Revenues, Inflation Adjusted

State tax revenues are beginning a slow recovery in 2010.

Nationwide, state-tax collections for fiscal year 2009 declined by a record $63 billion, or 8.2 percent from the previous year. That loss is roughly twice the amount states gained in fiscal relief from the federal stimulus package. Receipts now beginning to recover.

States Revenues Were Up 2.2% in Q2 2010, the 2nd Consecutive Quarter of Revenue Increase. Public Infrastructure Spending is Still Likely to Remain Depressed, Dampening Related Insurance Exposures and Demand.
Debt issued by state and local governments has soared by 100% between 1999 and 2009.

Many States/Localities Are in Dire Fiscal Straights, but the Default Rate on Moody’s-Rated Muni Debt is Just 0.09% over the Past 10 Years. Just 1 State Has Defaulted in the Past 100 Years (AR). Default Rate on Munis During the Great Depression was 1.8%, 97% of Which Was Ultimately Recovered.

Source: Federal Reserve Board of Governors, Flow of Funds Accounts from Credit Suisse.
State and Local Expenditures vs. Tax Receipts, 1960-2010:Q1

The gap between state and local governments revenues and expenditures is at a 50-year high and is widening.

Many States/Localities Are in Dire Fiscal Straights, but the Default Rate on Moody’s-Rated Muni Debt is Just 0.09% over the Past 10 Years. Just 1 State Has Defaulted in the Past 100 Years (AR). Default Rate on Munis During the Great Depression was 1.8%, 97% of Which Was Ultimately Recovered.

Source: Bureau of Economic Analysis and Credit Suisse estimates.
Inflation Trends: Concerns Over Stimulus Spending and Monetary Policy

Mounting Pressure on Claim Cost Severities?
Annual Inflation Rates (CPI-U, %), 1990–2011F

Inflation peaked at 5.6% in August 2008 on high energy and commodity crisis. The recession and the collapse of the commodity bubble have reduced inflationary pressures.

There is So Much Slack in the US Economy Inflation Should Not Be a Concern Through 2010/11, but Deficits and Monetary Policy Remain Longer Run Concerns.

Sources: US Bureau of Labor Statistics; Blue Chip Economic Indicators, 9/10 (forecasts).
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)

Inpatient Services Rose 6.7%; Outpatient Services Rose 7.4%

Excludes Food and Energy

2.7% 1.8% 6.9%

Overall CPI "Core" CPI Hospital Services Physicians' Services Dental Services Prescription Drugs Medical Care Commodities Medical CPI

Average annual increase in WC medical severity from 1995 through 2009 was nearly twice the medical CPI (7.6% vs. 3.9%). New healthcare reform legislation is unlikely to have any impact on the gap.

Tort Cost Growth & Medical Cost Inflation vs. Overall Inflation (CPI-U), 1961-2009E*

Tort costs move with inflation but at twice the rate of inflation

Tort system is an inflation amplifier
- Tort costs: +8.4%
- Med costs: +5.9%
- Overall inflation: +4.2%

Are there healthcare reform spillover effects?

* CPI-U and medical costs as of Sept 2009; Tort figure is for full-year 2009 from Tillinghast.
### Top Concerns/Risks for Insurers if Inflation Is Reignited

<table>
<thead>
<tr>
<th>Concerns</th>
<th>The Federal Reserve Has Flooded Financial System with Cash (Turned on the Printing Presses), the Federal Gov’t Has Approved a $787B Stimulus and the Deficit is Expected to Mushroom to $1.8 Trillion. All Are Potentially Inflationary.</th>
</tr>
</thead>
<tbody>
<tr>
<td>What are the potential impacts for insurers?</td>
<td></td>
</tr>
<tr>
<td>What can/should insurers do to protect themselves from the risks of inflation?</td>
<td></td>
</tr>
</tbody>
</table>

### Key Risks From Sustained/Accelerating Inflation

- **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.
Top Concerns/Risks for Insurers if Deflation Becomes a Reality

**Concerns**

Deflation is defined as a sustained decline in the general price level. It can result from the reduction in the supply of money or credit or reductions in government, personal or investment spending. When deflation takes hold, the incentive is to defer purchases until prices decline further. This depresses aggregate demand, increases unemployment and triggers recessions.

- What are the potential impacts for insurers?
- What can/should insurers do to protect themselves from the risks of deflation?

**Key Risks**

From Sustained Deflation Inflation

- **Reduced Exposures**
  - Deflation is likely accompanied (potentially severe) recession, depressing insurance demand

- **Reduced Investment Earnings**
  - Deflationary periods that interest rates drop to very low levels. Stock markets may fall as the economy struggles with recessions and reduced corporate earnings.

- **Underwriting Profitability**
  - Lack of investment earnings makes sustained underwriting profitability a necessity

- **Rates**
  - Regulatory, buyer and market pressure will be biased strongly toward rate reduction

- **Lost Costs**
  - Even with a general decline in price levels insurers may experience rising costs in coverages vulnerable to medical claim costs, tort inflation and demand surge

Source: Insurance Information Institute.
Primary Causes
and Major Bouts of Deflation

Deflation is:
- A falling general price level
  - Note: this is different from
    - A fall in the rate of increase of the general price level;
      - This is called disinflation
    - A fall in the prices of some items or category of items
- For a prolonged period
- That is expected to continue indefinitely

Deflation results from some or all of:
- A surge in productivity, generally from technological innovation
- A steep and prolonged drop in the money supply
- A steep and prolonged recession
  - Note: this is different from a fall in the rate of increase of the price level

Major US Bouts of Deflation
- 1920-22
- 1930-33

Broad Impact of Deflation

Deflation causes...

- Consumers to delay buying things
  - They expect to buy those things later at lower prices
- A drop in the level of aggregate demand, from the delay in consumption
- A transfer of wealth
  - From borrowers and holders of illiquid assets
  - To savers/lenders and holders of liquid assets and currency
- A drop in the level of business investment
  - Following the drop in aggregate demand
  - Slack in capacity if the economy is in recession
  - Increased likelihood of lower profits or losses as selling prices drop below costs

What History Teaches Us About Deflation and the P-C Industry
1920-1950: Inflation, Deflation and the P-C Industry’s Combined Ratio*

From Year-end 1929 Through 1932, the Industry’s Combined Ratio Rose from 96.3 to 104.9 as the CPI Dropped. But from 1933 into the 1950s, the Combined Ratio Remained Below 100 Even as Prices Slowly Rose, Then Shot Up after WWII.

*From 1920-1934, stock companies only
Sources: Best’s Aggregates & Averages; http://www.rateinflation.com/consumer-price-index/usa-historical-cpi.php?form=usacpi
1920-1950: Inflation, Deflation and P-C Industry Profitability*


*stock companies only

Deflation’s Effects on the P-C Insurance Industry

- **Lower Claim Severities**
  - Particularly for property claims, severity drops for many items that insurers pay for

- **Rate contingency margins increase**
  - At least until rate construction reflects persistently declining claims severity, margins will be higher than otherwise due to high trend assumptions arising from use of historical data

- **Reserve Releases?**
  - Reserves may develop beneficially to become “redundant”

- **Lower Claim Frequency as Fewer Claims Reach Deductible, Retention Levels**

- **Less Use of Reinsurance**
  - Lower costs ➔ risks burn through their retentions less quickly, reaching policy limits less quickly
Catastrophic Loss – Catastrophe Losses Trends Are Trending Adversely
US Insured Catastrophe Losses

2000s: A Decade of Disaster
2000s: $193B (up 117%)
1990s: $89B

$100 Billion CAT Year is Coming Eventually

First Half 2010 CAT Losses Were Down 19% or $1.4B from first half 2009

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

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

Avg. CAT Loss Component of the Combined Ratio by Decade

1960s: 1.04
1970s: 0.85
1980s: 1.31
1990s: 3.39
2000s: 3.52

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.
The 12 Jan. Haiti quake killed 225,500 people, caused $8B+ in economic damage, but little in the way of insured losses.

Chilean earthquake (mag. 8.8) on 27 Feb. produced at least $4 billion in insured losses, $20 billion in economic losses. Most costly insurance event in 2010.

Severe winter weather in the Eastern US produced insured losses of produced at least $1B in insured losses and $2B in economic losses.

Winter Storm Xynthia produced at least $2B in insured losses and $4B in economic losses.
## Largest International Oil Well Blowouts by Volume, as of July 12, 2010*

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

## Probabilty of Landfall of at Least One Major Hurricane (CAT 3-4-5) in 2010*

<table>
<thead>
<tr>
<th>Region</th>
<th>Average Over Last Century</th>
<th>2010 Forecast*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Entire U.S. Coastline</td>
<td>52%</td>
<td>76%</td>
</tr>
<tr>
<td><strong>U.S. East Coast Incl. FL Peninsula</strong></td>
<td><strong>31%</strong></td>
<td><strong>51%</strong></td>
</tr>
<tr>
<td>Gulf Coast from FL Panhandle to Brownsville, TX</td>
<td>30%</td>
<td>50%</td>
</tr>
<tr>
<td>Caribbean</td>
<td>42%</td>
<td>65%</td>
</tr>
</tbody>
</table>

*Forecast as of June 2, 2010.
Source: Colorado State University, Department of Atmospheric Sciences; Insurance Information Institute.

The Probability of a Major Hurricane Making Landfall Somewhere Along the US Coast is Greatly Elevated in 2010, Including a 50% Chance Along the Oil Spill-Impacted Gulf Coast.
Outlook for 2010 North Atlantic Hurricane Season*

<table>
<thead>
<tr>
<th>Forecast Parameter</th>
<th>Average (1950-2000)</th>
<th>2010 Forecast*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Named Storms</td>
<td>9.6</td>
<td>18</td>
</tr>
<tr>
<td>Named Storm Days</td>
<td>49.1</td>
<td>90</td>
</tr>
<tr>
<td>Hurricanes</td>
<td>5.9</td>
<td>10</td>
</tr>
<tr>
<td>Hurricane Days</td>
<td>24.5</td>
<td>40</td>
</tr>
<tr>
<td>Major Hurricanes</td>
<td>2.3</td>
<td>5</td>
</tr>
<tr>
<td>Major Hurricane Days</td>
<td>5.0</td>
<td>13</td>
</tr>
<tr>
<td>Accumulated Cyclone Energy</td>
<td>96.1</td>
<td>185</td>
</tr>
<tr>
<td>Net Tropical Cyclone Activity</td>
<td>100%</td>
<td>195%</td>
</tr>
</tbody>
</table>

The 2010 Hurricane Season is Expected to Be Nearly Twice as Active as the Long-Run Average (195% of Normal)

*Forecast as of June 2, 2010.
Source: Colorado State University, Department of Atmospheric Sciences; Insurance Information Institute.
Number of events in first half of 2010 is close to the annual totals from five of past ten years.

Source: MR NatCatSERVICE © 2010 Munich Re
Thunderstorm losses have quadrupled since 1980.

First Half 2010
$3.0 Bn

Source: Property Claims Service, MR NatCatSERVICE © 2010 Munich Re
Average annual winter storm losses have increased over 50% since 1980.

Severe winter storms in early 2010 caused major damage to energy infrastructure.

First Half 2010
$2.4 Bn

Source: Property Claims Service, MR NatCatSERVICE
There were 7 Significant Natural Catastrophes in the United States in 2009.
Florida Accounted for 19% of All US Insured CAT Losses from 1980-2008: $57.1B out of $297.9B

* All figures (except 2006-2008 loss) have been adjusted to 2005 dollars.
Source: PCS division of ISO.
Top 12 Most Costly Disasters in US History

(Insured Losses, 2009, $ Billions)

Hurricane Katrina Remains, By Far, the Most Expensive Insurance Event in US and World History

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

Sources: PCS; Insurance Information Institute inflation adjustments.
Reinsurance plays a very large role in claims payouts associated with major catastrophes.

<table>
<thead>
<tr>
<th>Event</th>
<th>Share of Losses Paid by Reinsurers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hurricane Hugo (1989)</td>
<td>30%</td>
</tr>
<tr>
<td>Hurricane Andrew (1992)</td>
<td>25%</td>
</tr>
<tr>
<td>Sept. 11 Terrorist Attack (2001)</td>
<td>60%</td>
</tr>
<tr>
<td>2004 Hurricane Season</td>
<td>20%</td>
</tr>
<tr>
<td>2005 Hurricane Season</td>
<td>45%</td>
</tr>
<tr>
<td>2008 Texas Hurricane</td>
<td>33%</td>
</tr>
</tbody>
</table>

Source: Wharton Risk Center, Disaster Insurance Project, Renaissance Re, Insurance Information Institute.
Total Value of Insured Coastal Exposure

(2007, $ Billions)

- Florida: $2,458.6
- New York: $2,378.9
- Texas: $895.1
- Massachusetts: $772.8
- New Jersey: $635.5
- Connecticut: $479.9
- Louisiana: $224.4
- S. Carolina: $191.9
- Virginia: $158.8
- Maine: $146.9
- North Carolina: $132.8
- Alabama: $92.5
- Georgia: $85.6
- Delaware: $60.6
- New Hampshire: $55.7
- Mississippi: $51.8
- Rhode Island: $54.1
- Maryland: $14.9

$159B Insured Coastal Exposure in Virginia in 2007

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

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

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

Source: PIPSO; Insurance Information Institute
Insurance Information Institute Online:

www.iii.org

Thank you for your time and your attention!

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