The Credit Crisis:

What Went Wrong?

35th General Assembly of the Geneva Association
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Five Distinguishing Characteristics of the Credit Crisis

1. The crisis originated not in small or financially immature economies fraught with political risk as in the past (e.g., Latin America) but in large, well established and sophisticated financial markets, primarily the United States.

2. The crisis was created and exacerbated by some of the largest, most sophisticated financial institutions in the world, suggesting a collapse of basic risk management.

3. The crisis was triggered, transmitted and fueled not by widespread defaults on debt instruments as in past credit crises but through excessive leverage (borrowing) and widespread securitization of complex structured financial products. The leverage amplified even small changes in real (or perceived) risk associated with the underlying debt instruments which were then transmitted globally via securitization.
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4. Regulatory and accounting mechanisms for identifying, monitoring, quantifying and controlling excessive exposure to credit risk were at best ineffective and at worst outright failures

- Raises fundamental questions regarding the current nature and form of regulation, its adequacy as well as necessary proscriptive changes to prevent such collapses in the future
- Do mark-to-market requirements exacerbate the problem?

5. Traditional economic policy tools (such as central bank interest rate reductions and fiscal stimulus initiatives) were not designed to manage credit and liquidity crises and are therefore are of limited effectiveness.
Credit Crisis
Media Coverage of the Insurance Industry

Bond Insurance Dominated Headlines
Media Coverage of Subprime Exposure of Insurers*

January 2007—May 2008

Peak of media coverage of subprime issue pertaining to insurers was Feb. 2008*

Coverage has receded to pre-crisis levels

Source: Lexis/Nexis searches.

*Excluding bond/monoline insurers.
The peak of media coverage of bond insurance issue was in February 2008, with near collapse of several bond insurers. Coverage has receded to near pre-crisis levels.

Media coverage of bond (monoline) insurers dominated headlines during the first 5 months of 2008.

Sources: Insurance Information Institute from Lexis/Nexis search.
Peak of media coverage of D&O/E&O insurance issue was Jan. 2008

Media coverage has receded to pre-crisis levels

Source: Lexis/Nexis searches.
Credit Crisis

Public Public
Perceptions of the
Insurance Industry

Consumers Concerns
POLL: Has the Insurance Industry Been Affected by the Downturn in the Economy?

Nearly 3 in 4 Americans believe that the economic downturn has adversely affected the insurance industry.

- Yes: 74%
- No: 17%
- Don't Know: 9%

70% of those polled believe that the recent national economic and financial conditions harm insurers’ ability to pay claims and sell insurance.

Affects Ability to Pay Claims
- 12%

Affects Ability to Sell Insurance
- 8%

Doesn't Affect Ability to Pay Claims or Sell Insurance
- 7%

Don't Know
- 3%

78% of those polled believe that an insurer’s financial strength is “Extremely” or “Very” important.

POLL: What is the MOST Important Quality to You When You Choose and Insurer?

Americans are nearly equally divided between price, service and financial strength when it comes to the most important quality of their insurer.

Price: 31%
Service: 31%
Financial Strength & Stability: 35%
Don't Know: 3%

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Download at:
www.iii.org/media/presentations/CreditCrisis

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