The Financial Crisis & Its Impacts on the Insurance Industry

Challenges Amid the Economic and Regulatory Storm

Mississippi State University Insurance Day
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Presentation Outline

- **Financial Crisis & The Weakening Economy: Insurance Impacts for the P/C Insurance Industry**
  - **Recession, Growth & Insurance**
- **Economic Stimulus Package**
  - **Impacts & Implications for P/C Insurers**
- **Financial Strength & Ratings**
- **P/C Insurance Industry Overview & Outlook**
  - **Profitability**
  - **Premium Growth**
  - **Underwriting Performance**
  - **Financial Market Impacts**
- **Capital & Capacity**
- **Regulatory Response to Crisis**
  - **Emerging Blueprint of Regulatory Overhaul**

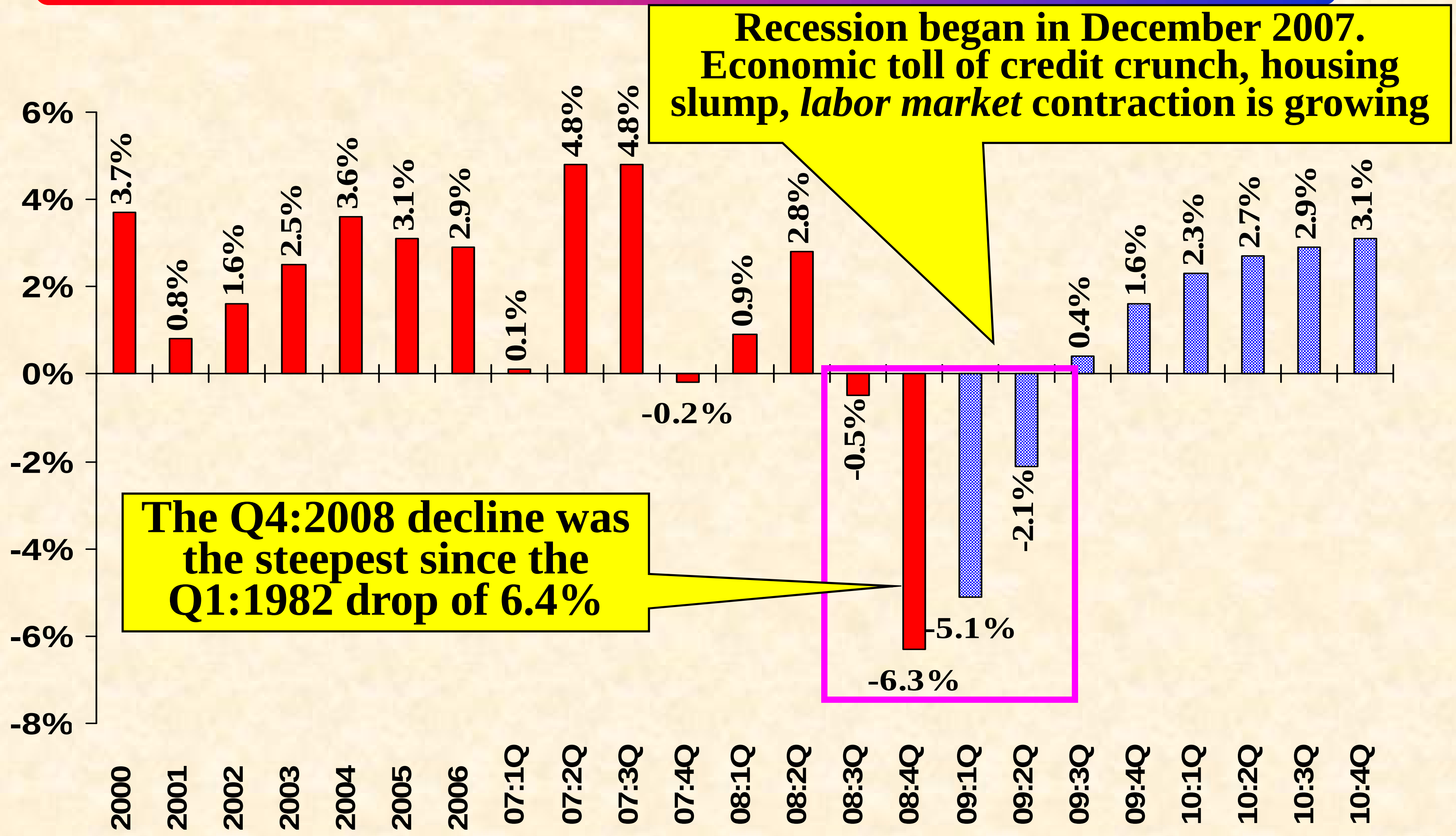
Q & A

THE ECONOMIC STORM

What the Financial Crisis and Deep Recession Mean for the P/C Insurance Industry

Exposure & Claim Cost Effects

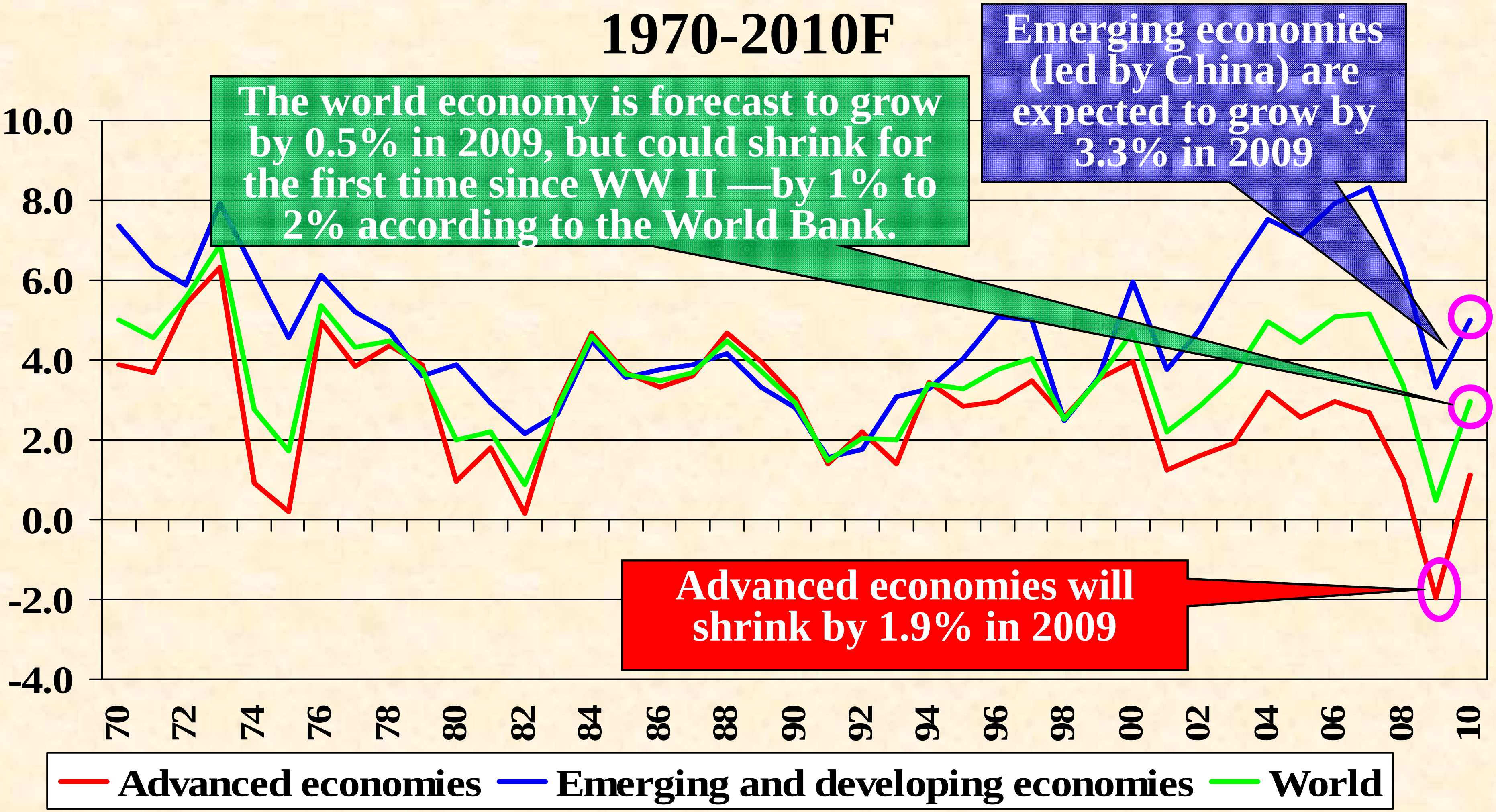
*Real GDP Growth**



*Yellow bars are Estimates/Forecasts from Blue Chip Economic Indicators.

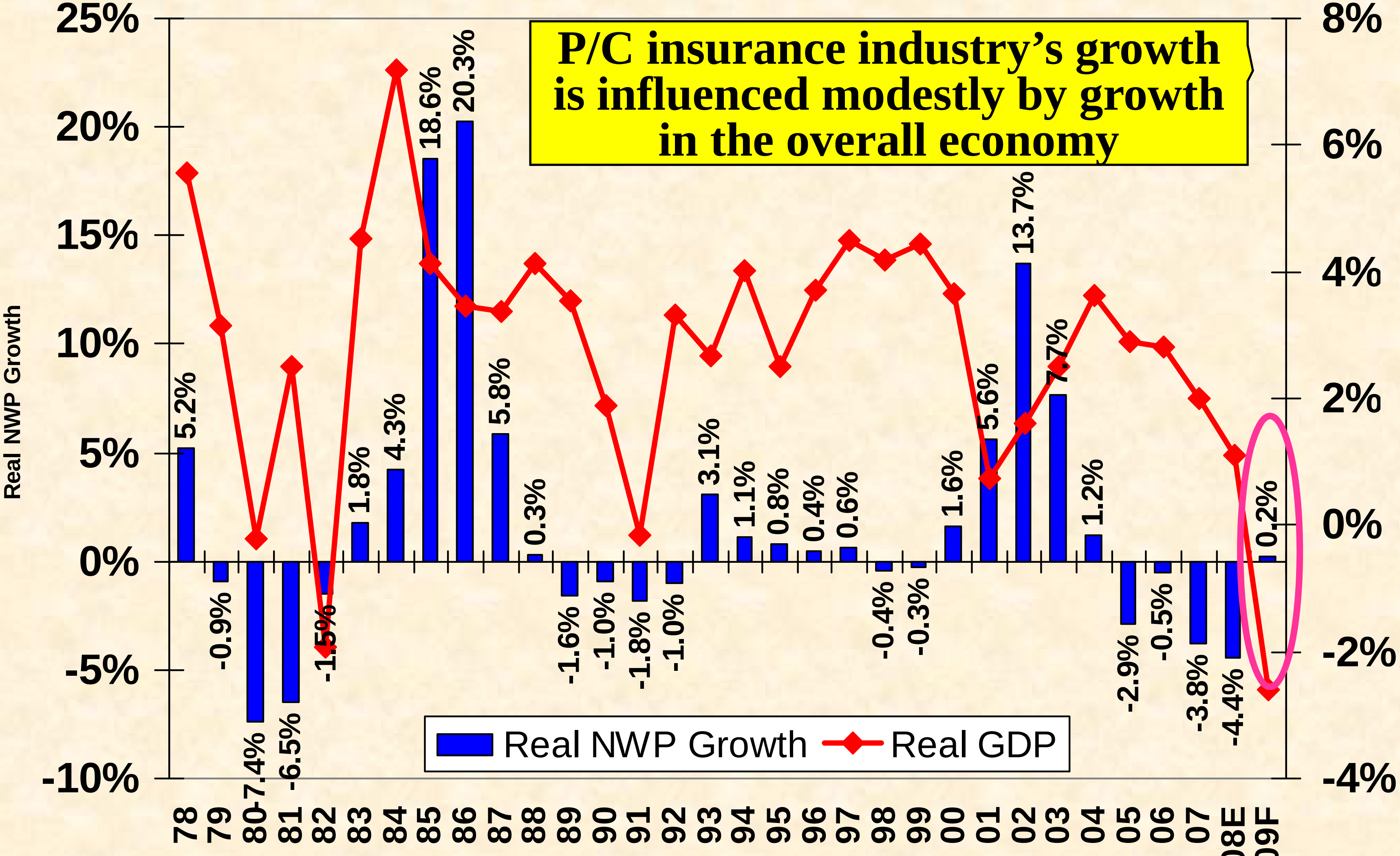
Source: US Department of Commerce, Blue Economic Indicators 4/09; Insurance Information Institute.

GDP Growth: Advanced & Emerging Economies vs. World



Source: International Monetary Fund, World Economic Outlook Update, Jan. 28, 2009; Ins. Info. Institute.

Real GDP Growth vs. Real P/C Premium Growth: Modest Association



Sources: A.M. Best, US Bureau of Economic Analysis, Blue Chip Economic Indicators, 4/09; Insurance Information Inst.

Length of US Recessions, 1929-Present*

"We will rebuild. We will recover."

--President Barack Obama addressing a joint session of Congress

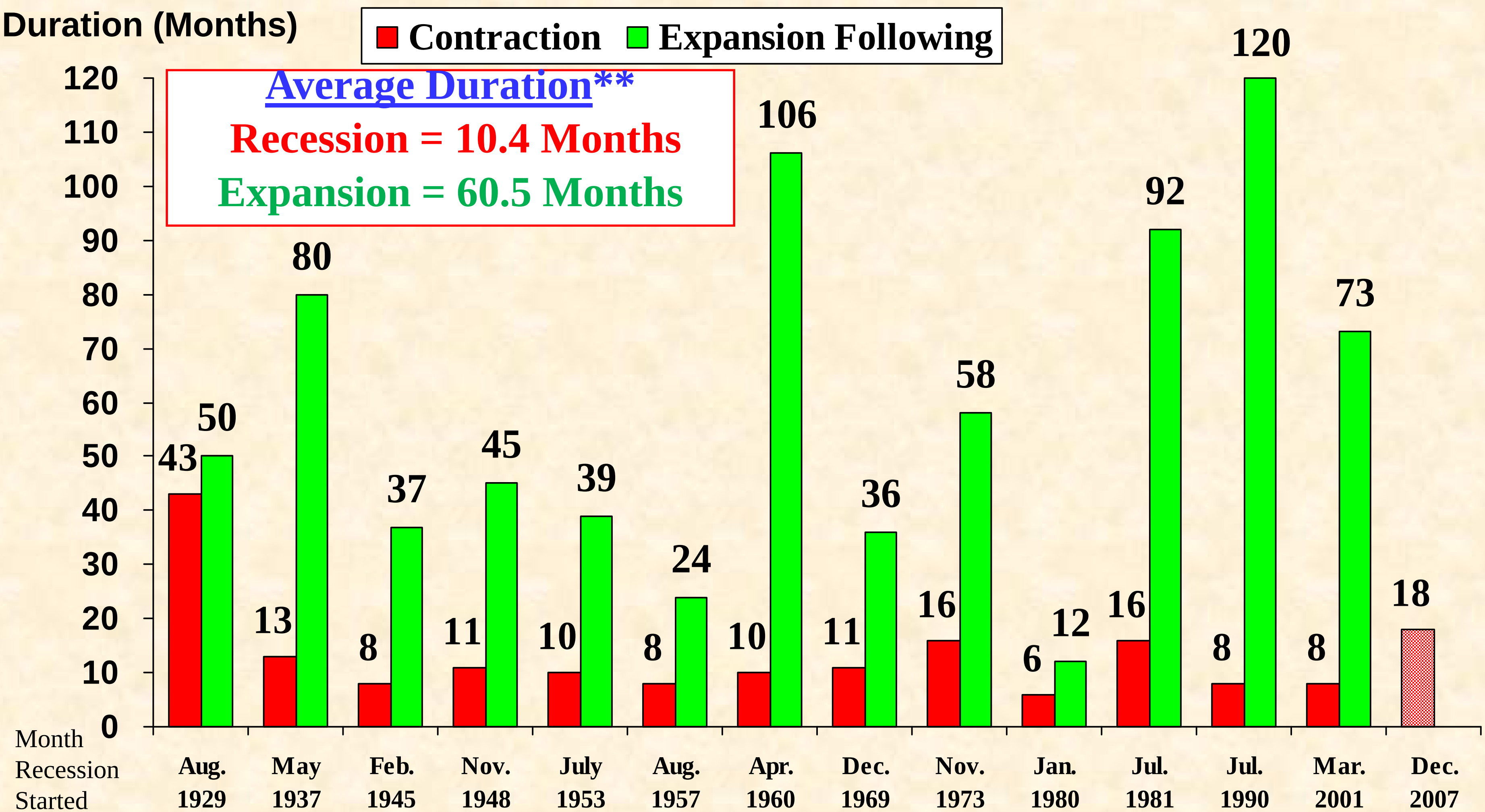
February 24, 2009

Current recession began in Dec. 2007 and is already the longest since 1981. It is now also the longest recession since the Great Depression.

* As of May 2009, inclusive

Sources: National Bureau of Economic Research; Insurance Information Institute.

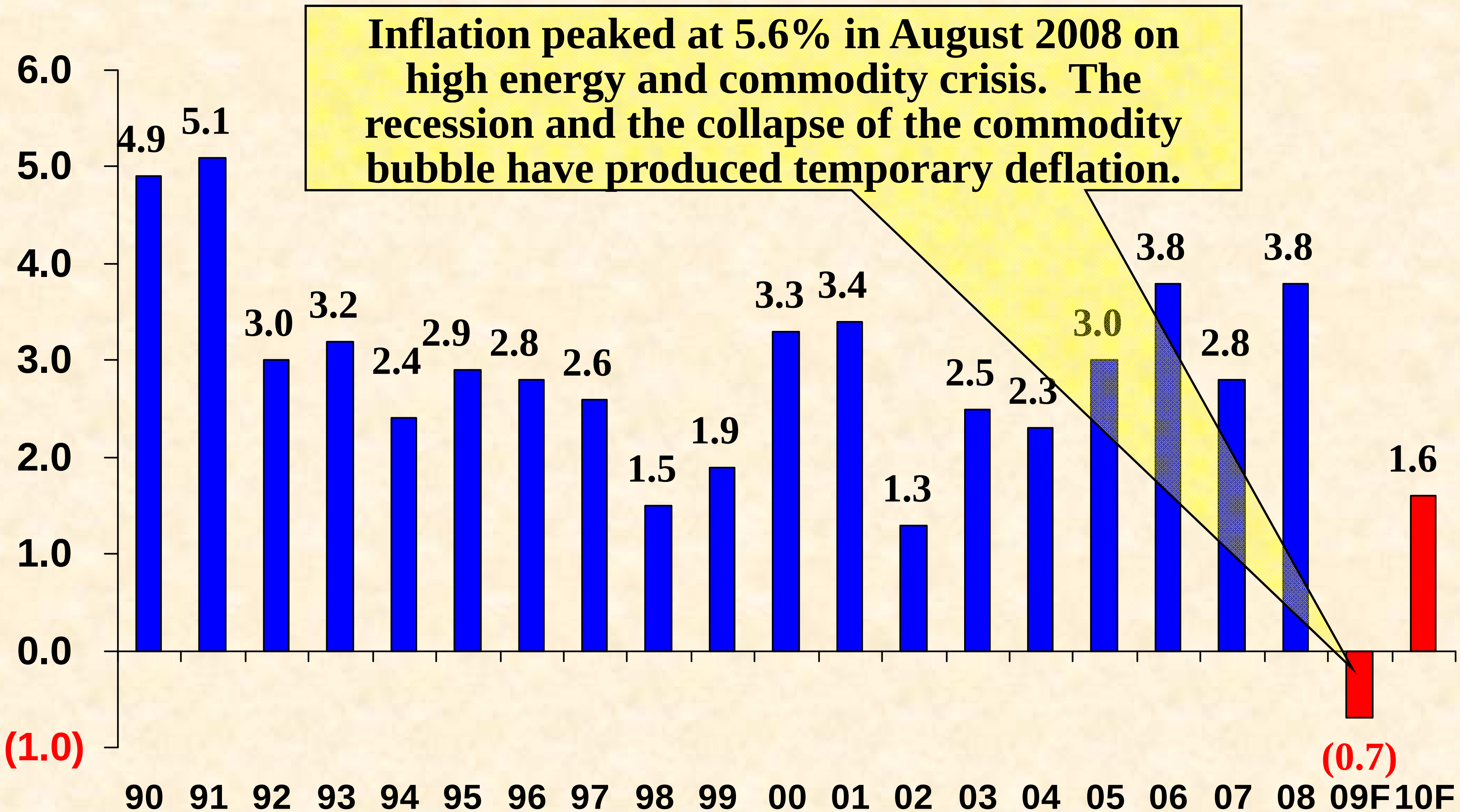
Length of U.S. Business Cycles, 1929-Present*



* As of May 2009, inclusive; **Post-WW II period through end of most recent expansion.

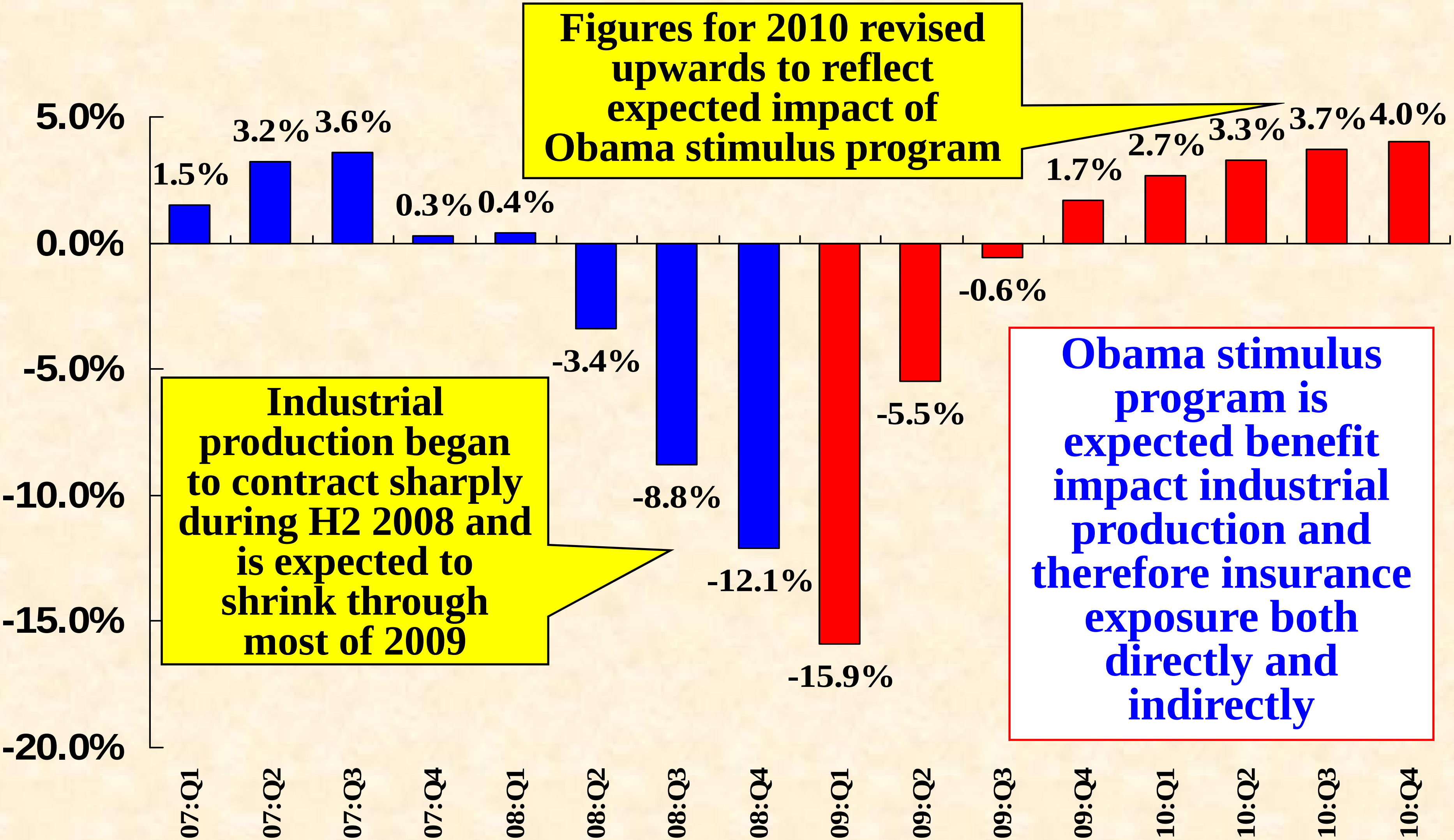
Sources: National Bureau of Economic Research; Insurance Information Institute.

Annual Inflation Rates (CPI-U, %), 1990-2010F



Sources: US Bureau of Labor Statistics; Blue Chip Economic Indicators, April 10, 2009 (forecasts).

Total Industrial Production, (2007:Q1 to 2010:Q4F)



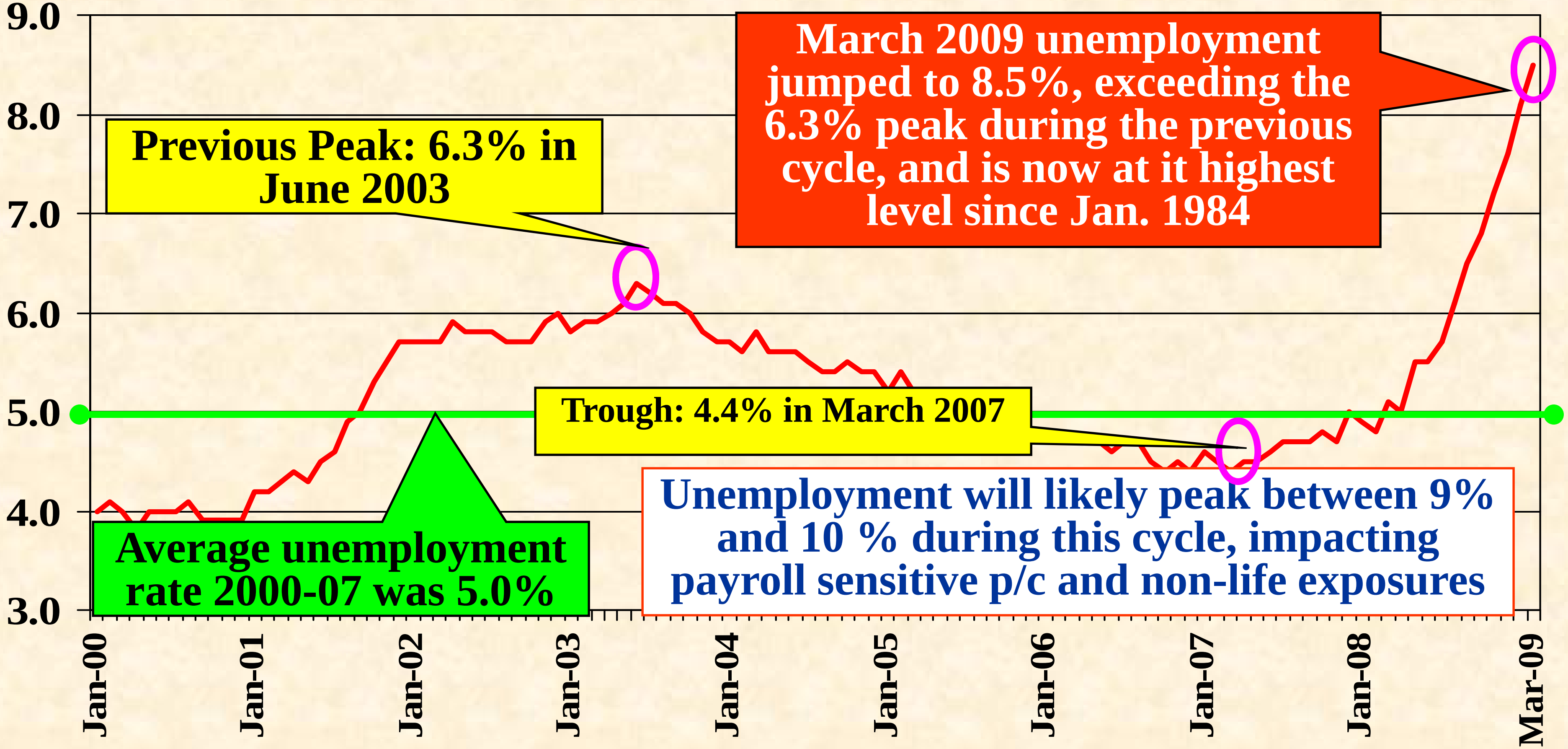
Sources: US Bureau of Labor Statistics; Blue Chip Economic Indicators (4/09); Insurance Info. Inst.

Labor Market Trends

Fast & Furious: Massive Job Losses Sap the Economy and Workers Comp Exposure

Unemployment Rate: On the Rise

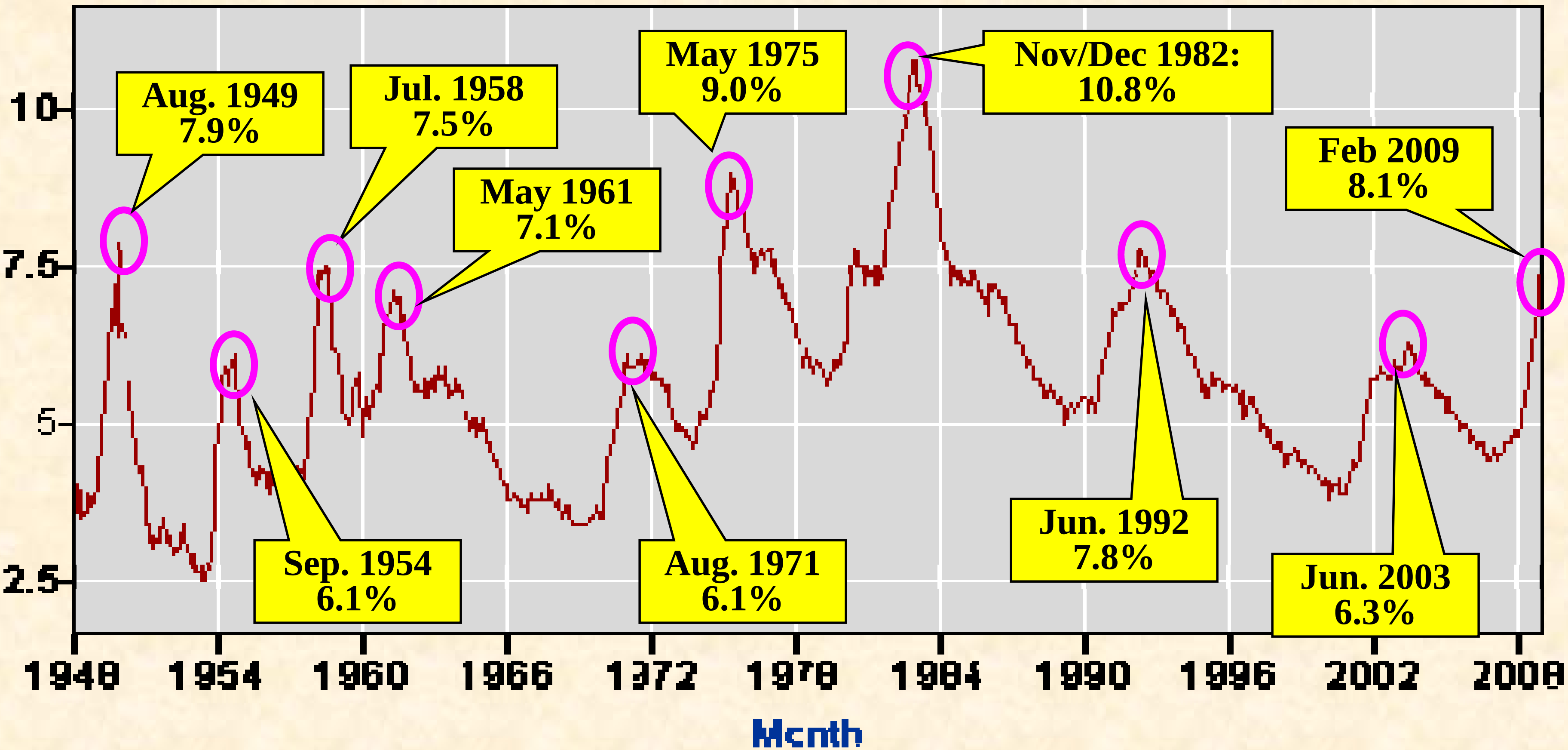
January 2000 through March 2009



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

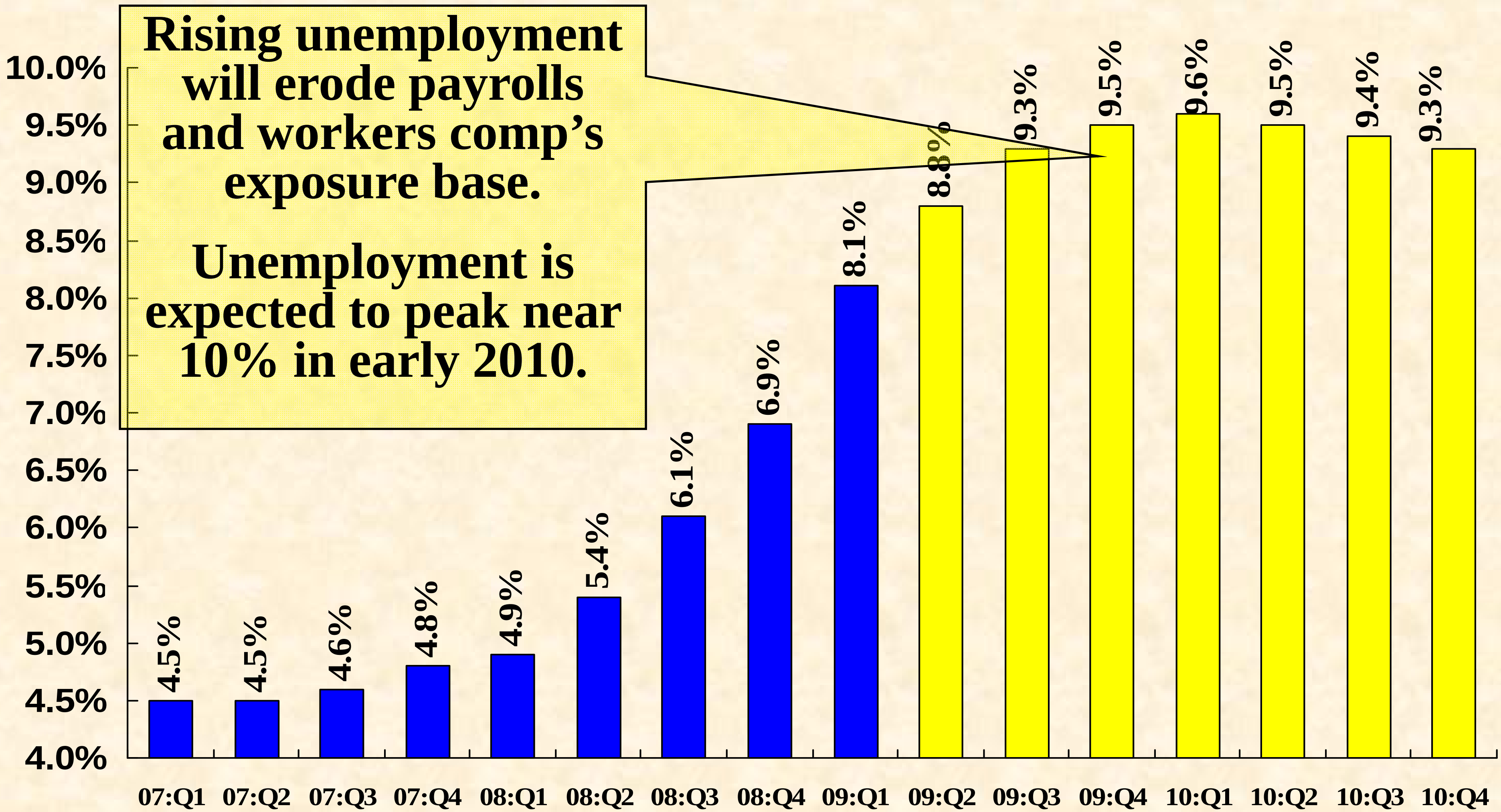
US Unemployment Rate: A Volatile History *(update)*

January 1948 through February 2009



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

U.S. Unemployment Rate, (2007:Q1 to 2010:Q4F)*

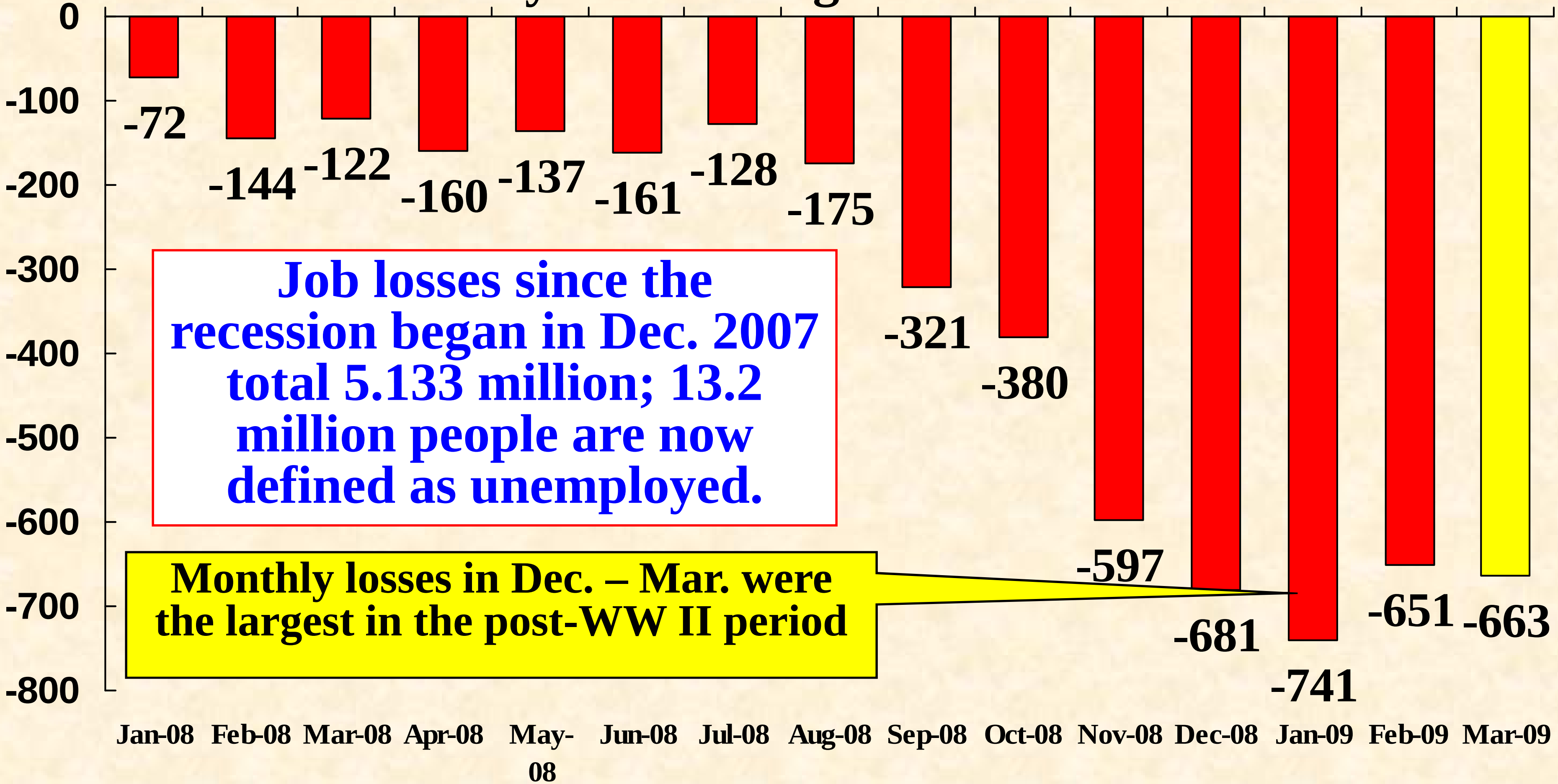


* Blue bars are actual; Yellow bars are forecasts

Sources: US Bureau of Labor Statistics; Blue Chip Economic Indicators (4/09); Insurance Info. Inst.

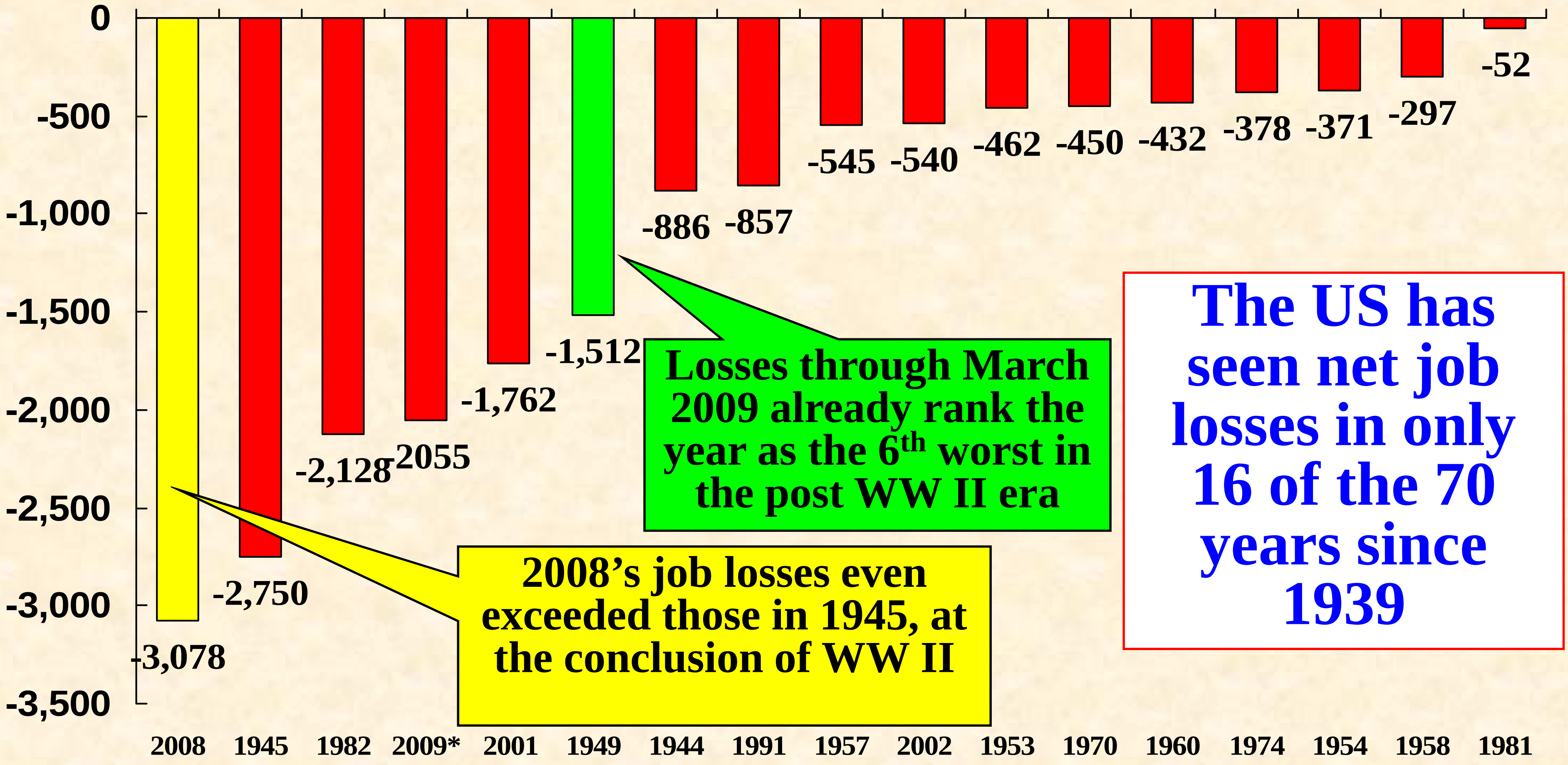
Monthly Change Employment (Thousands)*

January 2008 through March 2009



Source: US Bureau of Labor Statistics: http://www.bls.gov/ces/home.htm; Insurance Info. Institute

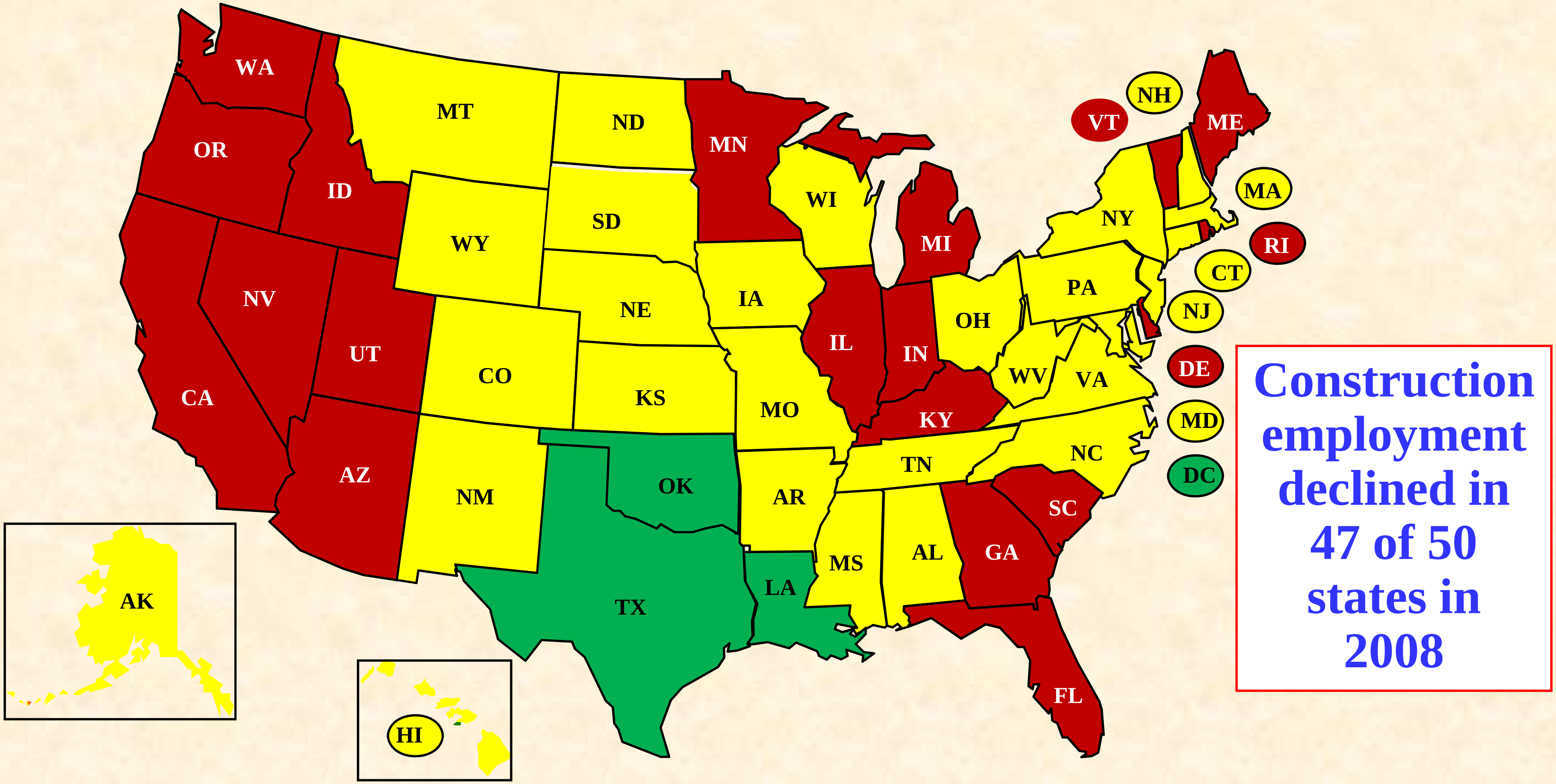
Years With Job Losses: 1939-2009 (Thousands)*



The US has seen net job losses in only 16 of the 70 years since 1939

*Through March 2009.
Source: Insurance Information Institute research from US Bureau of Labor Statistics data: http://www.bls.gov/ces/home.htm.

State Construction Employment, Dec. 2007 – Dec. 2008



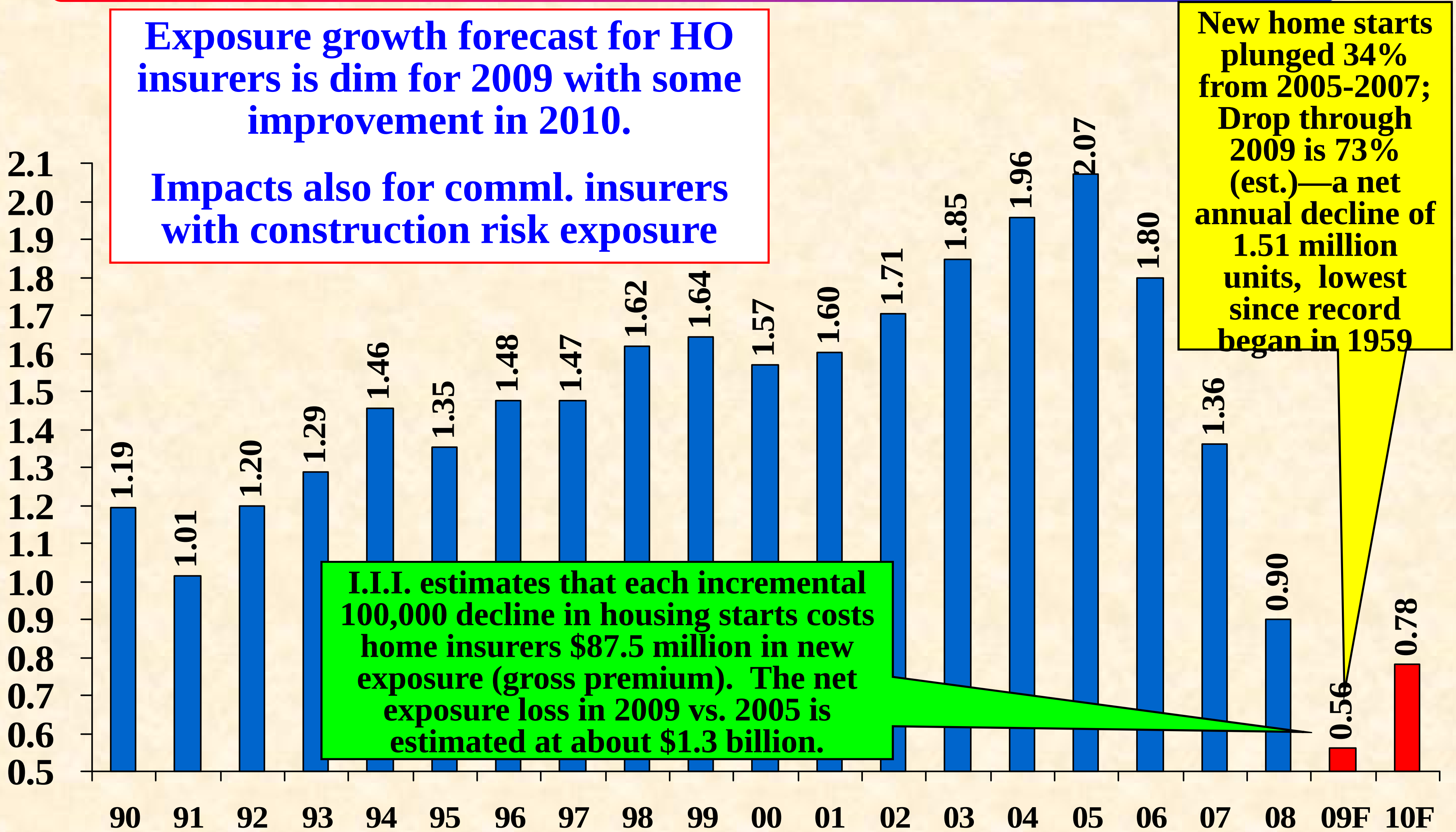
0% to 4% | -0.1% to -8.5% | -8.8% to -22%

Sources: Associated General Contractors of America from Bureau of Labor Statistics; Insurance Information Institute.

Crisis-Driven Exposure Implications

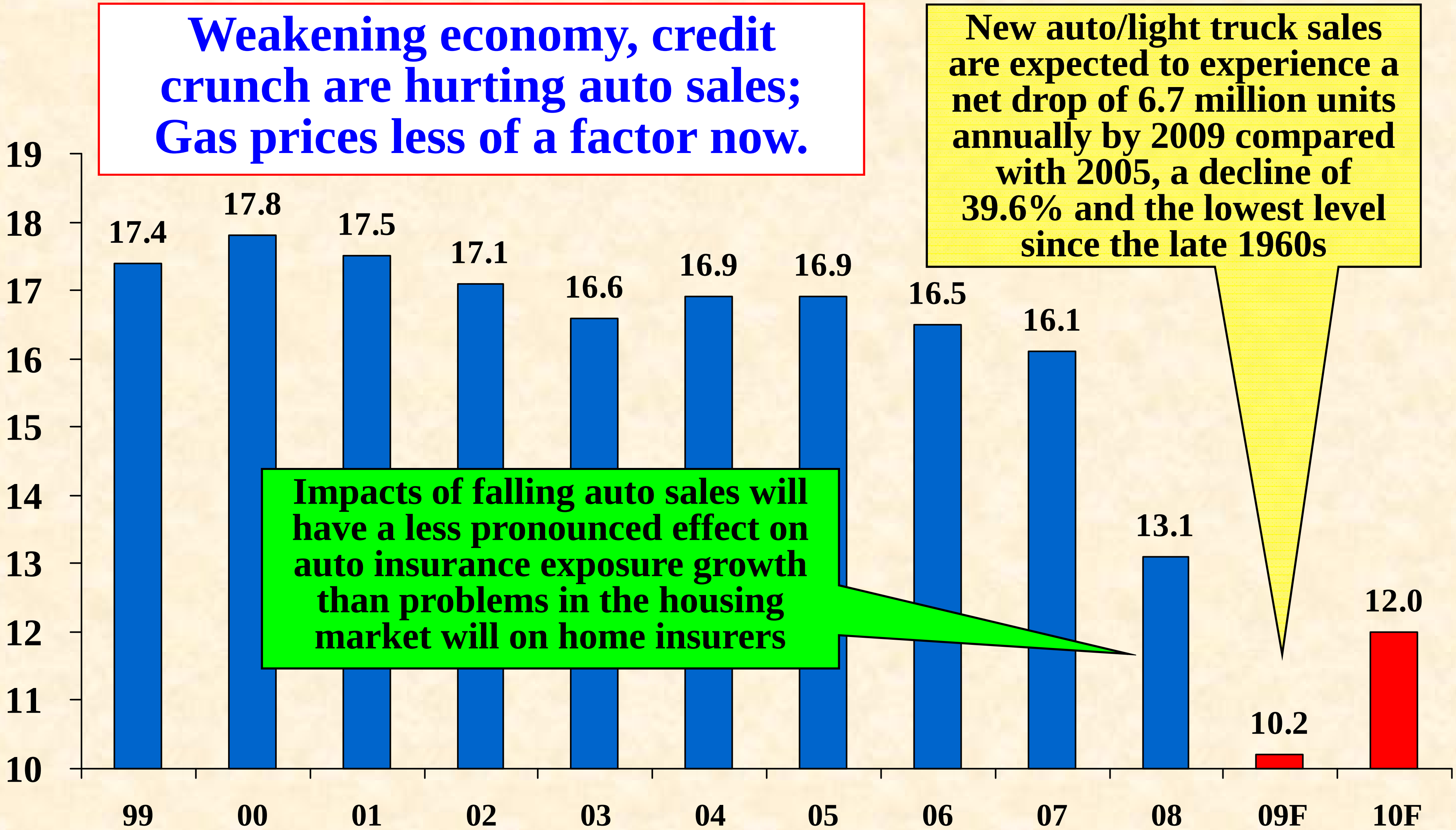
Home, Auto Exposure Growth Slows as Sales Nosedive

New Private Housing Starts, 1990-2010F (Millions of Units)



Source: US Department of Commerce; Blue Chip Economic Indicators (4/09); Insurance Information Inst.

Auto/Light Truck Sales, 1999-2010F (Millions of Units)



Source: US Department of Commerce; Blue Chip Economic Indicators (4/09); Insurance Information Inst.

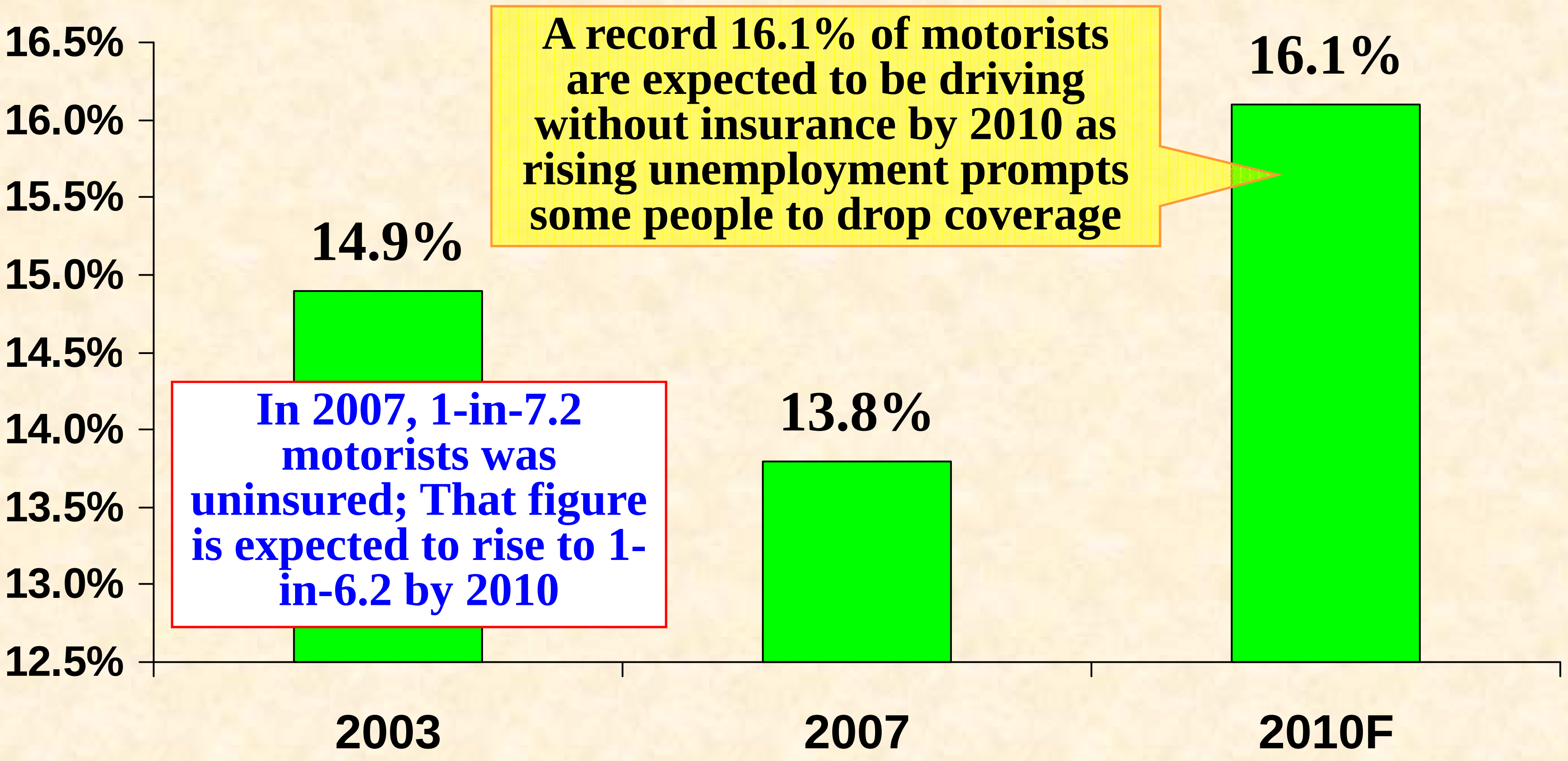
Crisis Implications

Top Crisis-Driven Claim Issues for Personal Lines Insurers

Summary of Short-Run Impacts of Stimulus Package on P/C Insurance

- **CLAIMING BEHAVIOR**
  - **Claim frequency falls with miles driven. History: Drop is temporary.**
  - **Claim severity continues to rise: med costs, collisions repair costs up**
  - **Likely maintenance on homes, cars deferred→claim. freq/sev. impact?**
- **PURCHASING BEHAVIOR: Efforts to Economize**
  - **More shopping around**
  - **Increased deductibles**
  - **Dropping optional coverages (collision, comprehensive)**
  - **Lower limits**
  - **Insuring fewer vehicles (3 or 4th vehicle sold)**
  - **Insuring older vehicles (old cars retained, new car purchases deferred)**
- **UNINSURED/UNDERINSURED MOTORIST % RISES**
  - **Expected to rise from 13.8% in 2007 to 16.1% in 2010**
- **FRAUD & ABUSE:**
  - **Evidence emerging of increased frequency of "give-ups" where car owners underwater on payments commit fraud to obtain insurance money (e.g., car arson, fabricated theft, etc.)**
  - **Anecdotal evidence of owner-caused home arson**

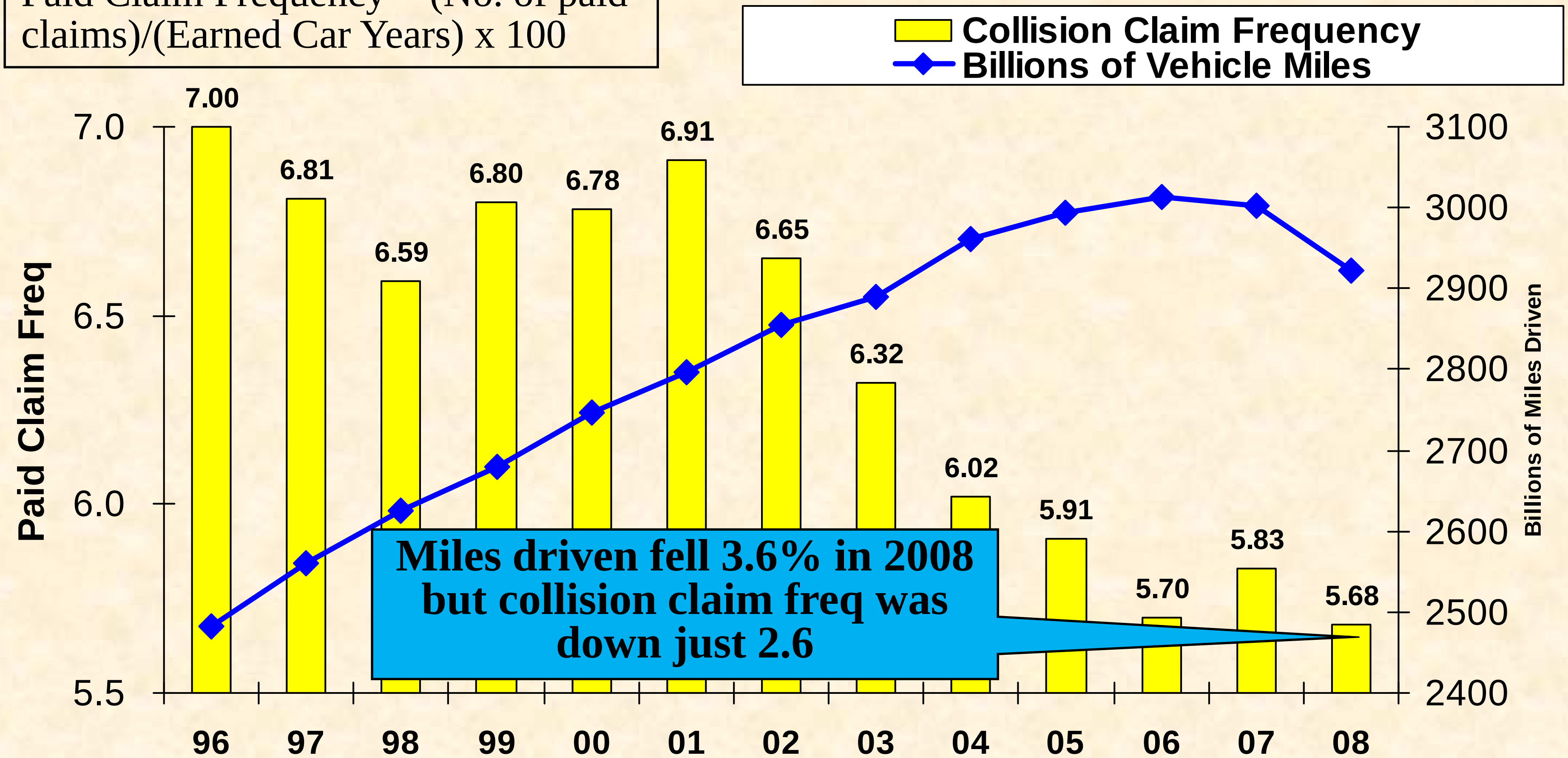
Percentage Motorists Driving Without Insurance, 2003-2010F



Source: *Uninsured Motorists, 2008* Edition, Insurance Research Council; Insurance Information Institute

Do Changes in ***Miles Driven*** *Affect Auto Collision Claim Frequency?*

Paid Claim Frequency = (No. of paid claims)/(Earned Car Years) x 100



Sources: Federal Highway Administration (http://www.fhwa.dot.gov/ohim/tvtw/08septvt/index.cfm; ISO Fast Track Monitoring System, *Private Passenger Automobile Fast Track Data*: Nine Months 2008, published April 1, 2009 and earlier reports. *2008 ISO figure is for 4 quarters ending Q4 2008.

Auto Insurance: Claim Frequency Impacts of Energy Crisis of 1973/4

Oct. 17, 1973: Arab oil embargo begins

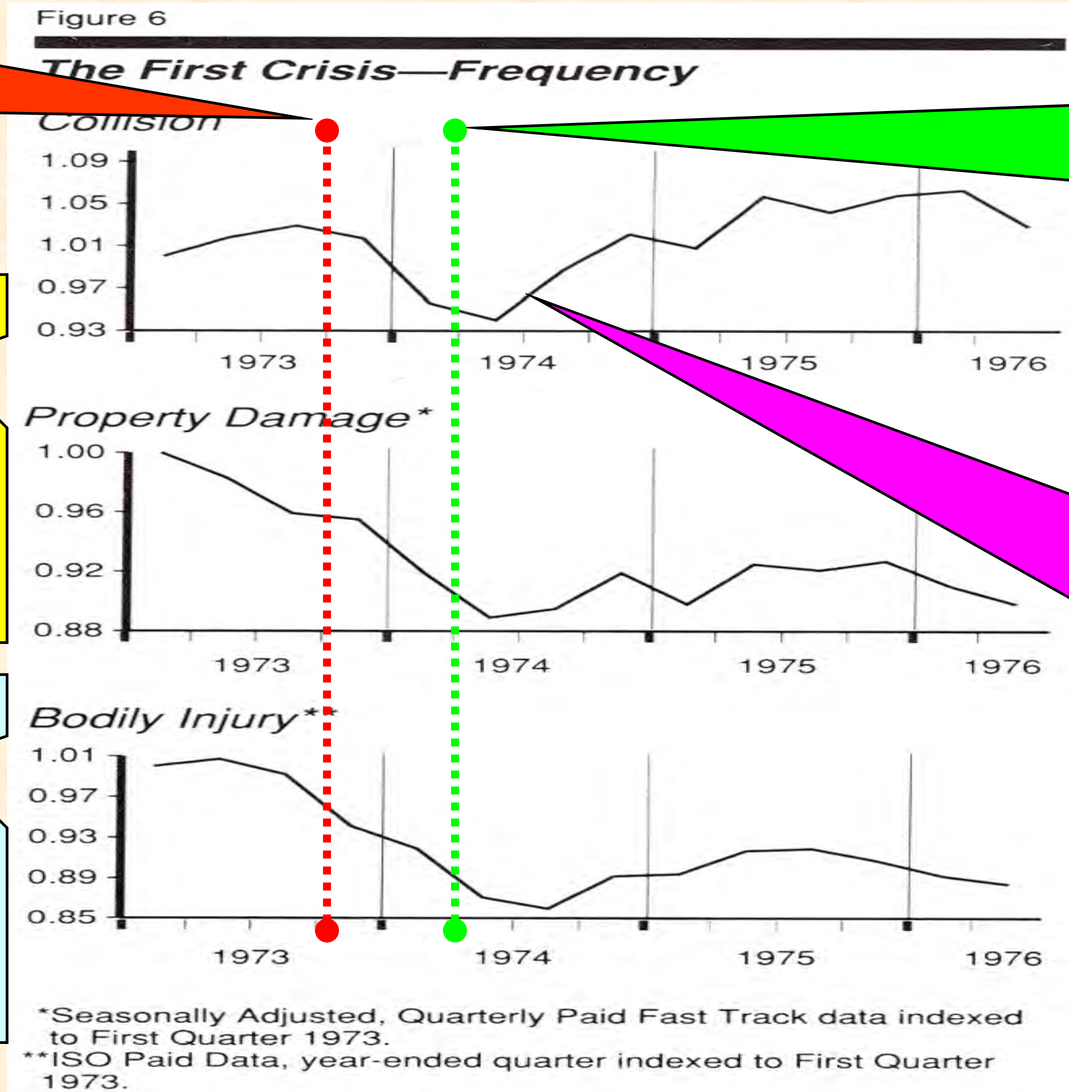
March 17, 1974: Arab oil states announce end to embargo

Frequency Impacts

Collision: -7.7%

PD: -9.5%

BI: -13.3%



Frequency began to rebound almost immediately after the embargo ended

Driving Stats

Gas prices rose 35-40%

Miles driven fell 6.7% in 1974

Source: ISO, US DOT.

GREEN SHOOTS

Is the Recession Nearing an End?

Hopeful Signs That the Economy Will Begin to Recover Soon

- Recession Appears to be Bottoming Out, Freefall Has Ended
  - Pace of GDP shrinkage is beginning to diminish
  - Pace of job losses is leveling off
  - Major stock market indices well off record low, anticipating recovery
  - Some signs of retail sales stabilization are evident
- Financial Sector is Stabilizing
  - Banks are reporting quarterly profits
  - Many banks expanding lending to credit worthy people & businesses
- Housing Sector Likely to Find Bottom Soon
  - Home are much more affordable (attracting buyers)
  - Mortgage rates are at multi-decade lows (attracting buyers)
  - Freefall in housing starts and existing home sales is ending
- Inflation & Energy Prices Are Under Control
- Consumer & Business Debt Loads Are Shrinking

Source: Ins. Info. Inst.

THE $787 BILLION ECONOMIC STIMULUS

Sectoral Impacts & Implications for P/C Insurance

Summary of Short-Run Impacts of Stimulus Package on P/C Insurance

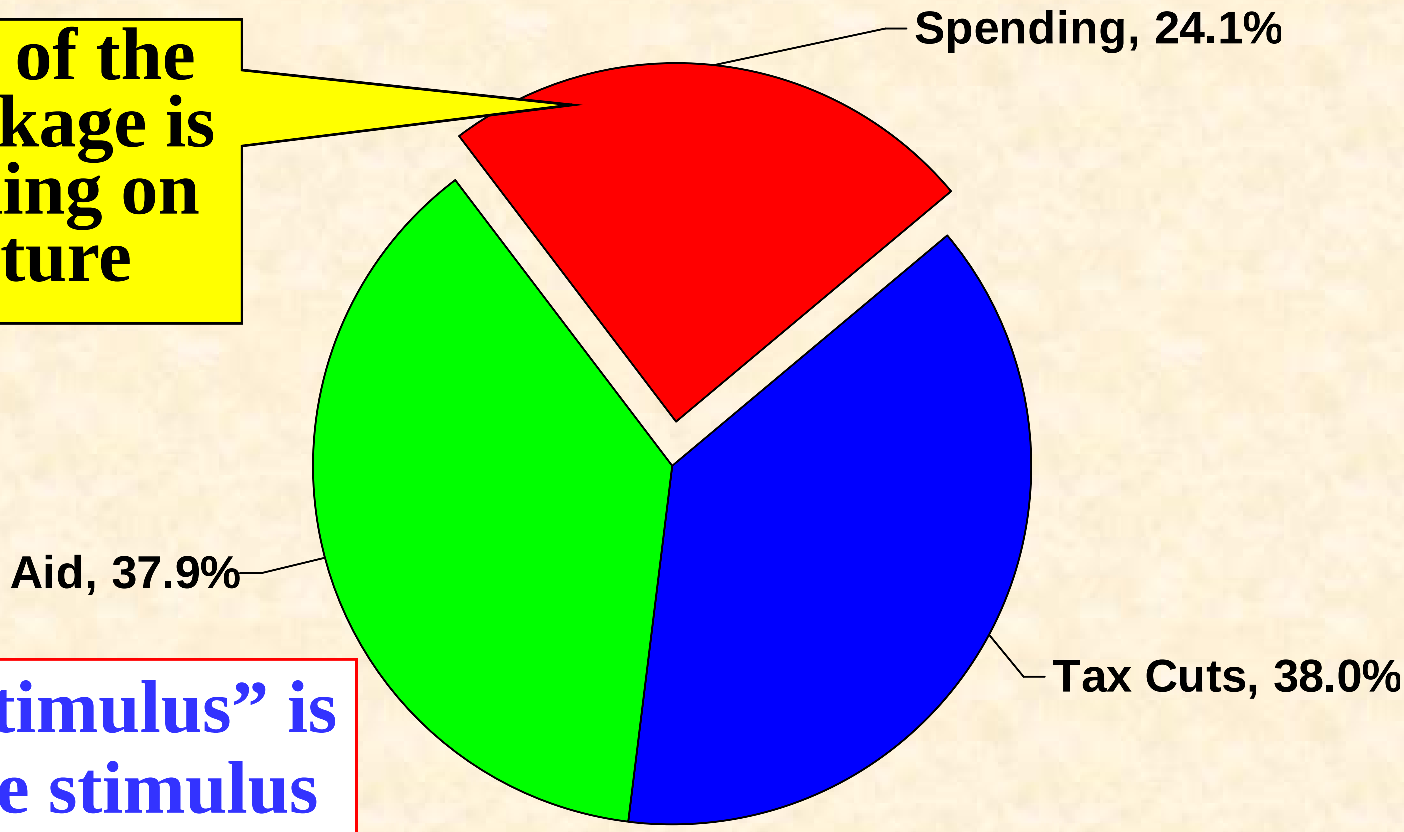
- **No Stimulus Provisions Specifically Address P/C Insurance**
  - **Spending, Aid and Tax Reductions benefit other industries, state and local governments, as well as individual and some corporate taxpayers**
- **Stimulus Package is Unlikely to Increase Net Premiums Written by More Than 1% or Approx. $4.5 Bill. by Year-End 2010**
- **"Direct" Impact to P/C Insurers Results Primarily from Increased Demand for Commercial Insurance**
  - **Primarily the result of increased infrastructure spending and the resulting need to insure workers, property and protect against liability risks**
  - **Because the primary objective of the stimulus is employment related, workers compensation will be the p/c line that benefits the most**
  - **Assuming the target of 3.5 million jobs created or preserved is achieved, private workers comp NPW (new and preserved) could amount to as much as $1.1 billion**
  - **Other commercial lines to benefit: surety, commercial auto, inland marine**
- **Other "Direct" P/C Demand Benefits Will Be Minimal**
  - **Tax provisions providing incentives to buy cars and homes and accelerate the depreciation of equipment will have little net impact on exposure**
  - **Some additional premium may be generated as older cars and equipment are replaced with new and more valuable (and therefore more expensive to insure)**

Summary of Short-Run Impacts of Stimulus Package on P/C Insurance (cont'd)

- **"Indirect" Impacts: Limited Gains for P/C Insurers**
  - **If stimulus is successful at increasing disposable and corporate income via tax reductions and "multiplier" income and employment effects, then spending could rise and produce some additional insurable exposure growth for p/c insurers**
- **Investment Portfolio Impacts**
  - **It is impossible to discern what, if any, impact the stimulus will have on stock and bond performance**
  - **If successful, the stimulus package (along with other initiatives) should help stabilize and reinvigorate the economy, increasing stock prices and bolstering the value of corporate and asset-backed bonds**
  - **The stimulus could be viewed as inflationary. Combined with existing large deficits and other spending initiatives, an expectation of inflation could push interest rates upward**

Economic Stimulus Package: Where the $787B Goes

Less than ¼ of the stimulus package is direct spending on infrastructure



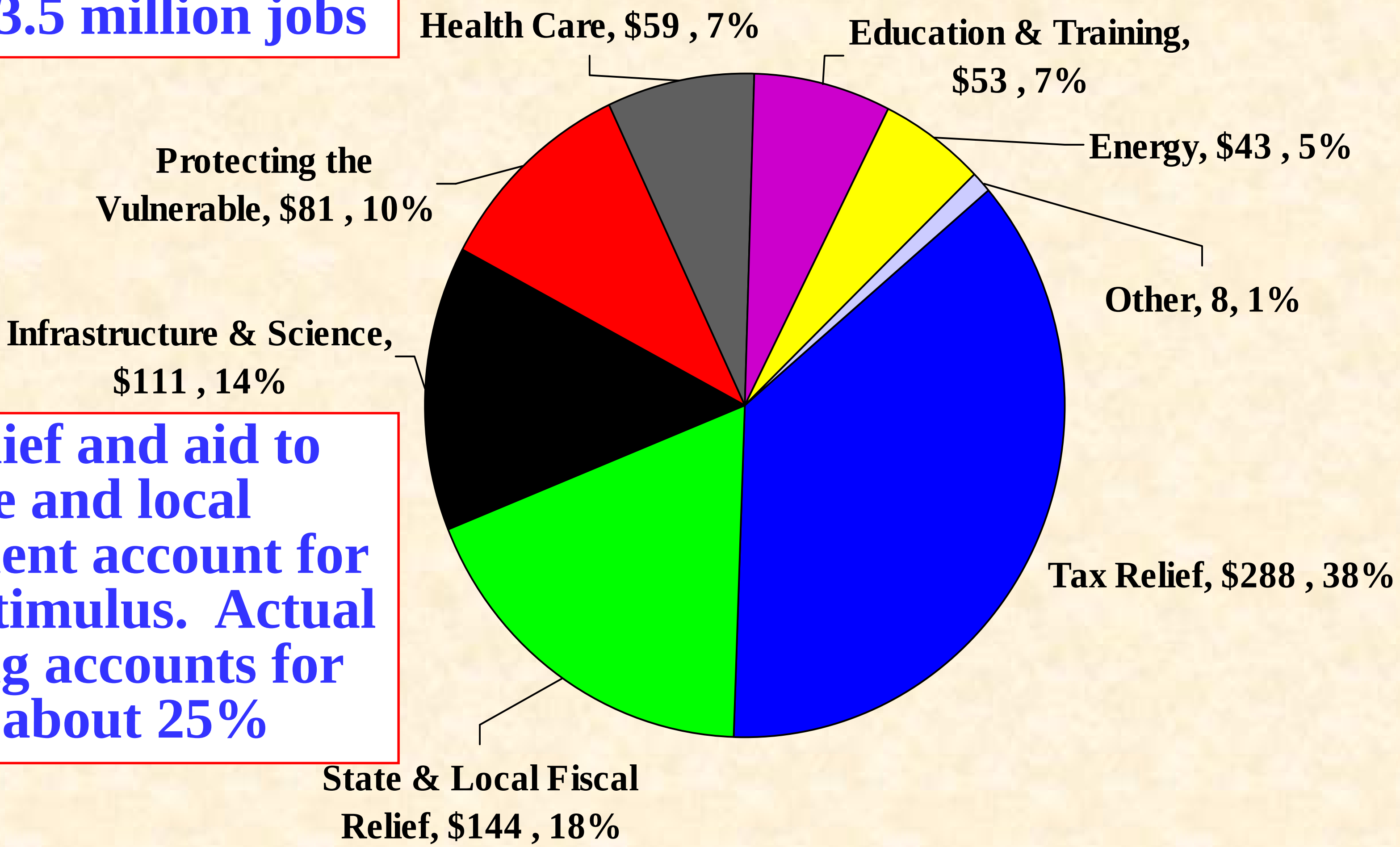
How much "stimulus" is actually in the stimulus package is open to debate and dispute

Sources: *Wall Street Journal* , 2/13/09; House Ways and Means Committee; Senate Finance Committee.

Economic Stimulus Package: Where the $787B Goes

Objective is to create or preserve 3.5 million jobs

$ Billions



Tax relief and aid to state and local government account for 56% of stimulus. Actual spending accounts for only about 25%

Source: http://www.recovery.gov/ accessed 2/18/09; Insurance Information Institute.

U.S. Economic $787B Stimulus Package: Major Spending Components

Objective is to create or preserve 3.5 million jobs

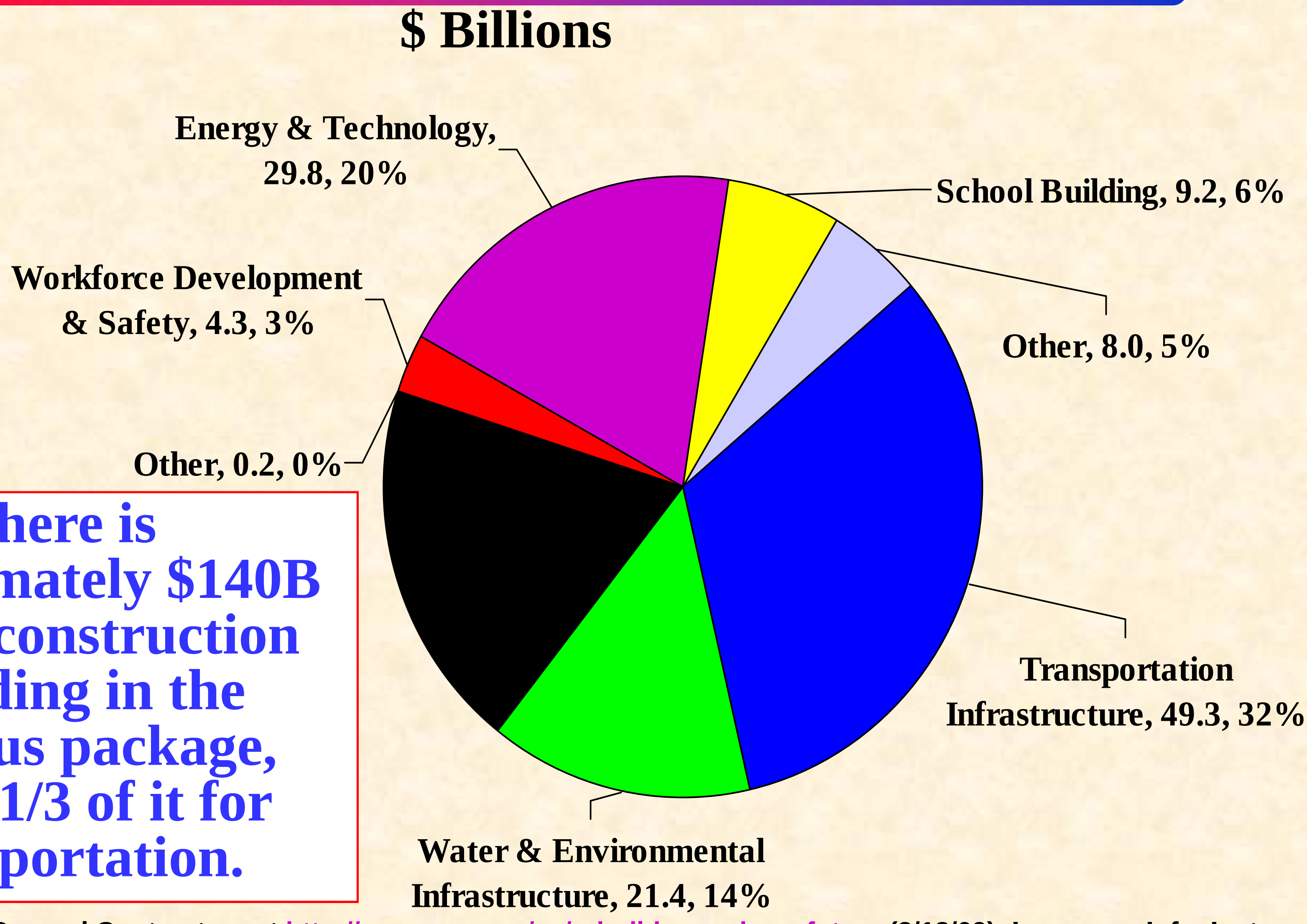
24.1% or $132.2B of the stimulus package is allocated toward direct spending. This is the component that will most directly benefit p/c insurers.

Lines Most Likely to Benefit:

Workers Comp
Commercial Auto
Inland Marine
Commercial Property & Liability
Surety

Sources: *Wall Street Journal* , 2/13/09; House Ways and Means Committee; Senate Finance Committee; Ins. Info. Inst.

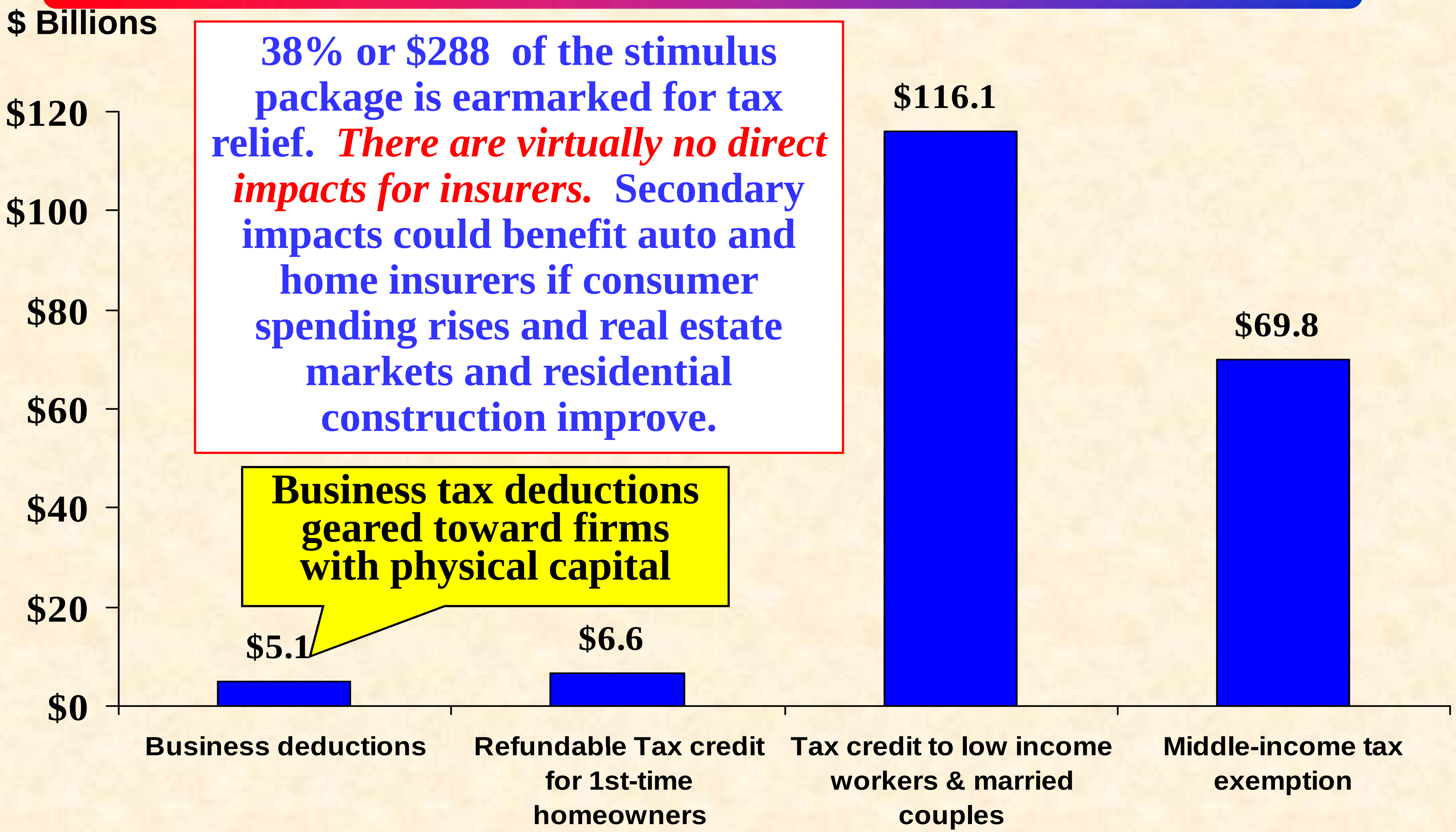
Economic Stimulus Package: $143.4 in Construction Spending



There is approximately $140B in new construction spending in the stimulus package, about 1/3 of it for transportation.

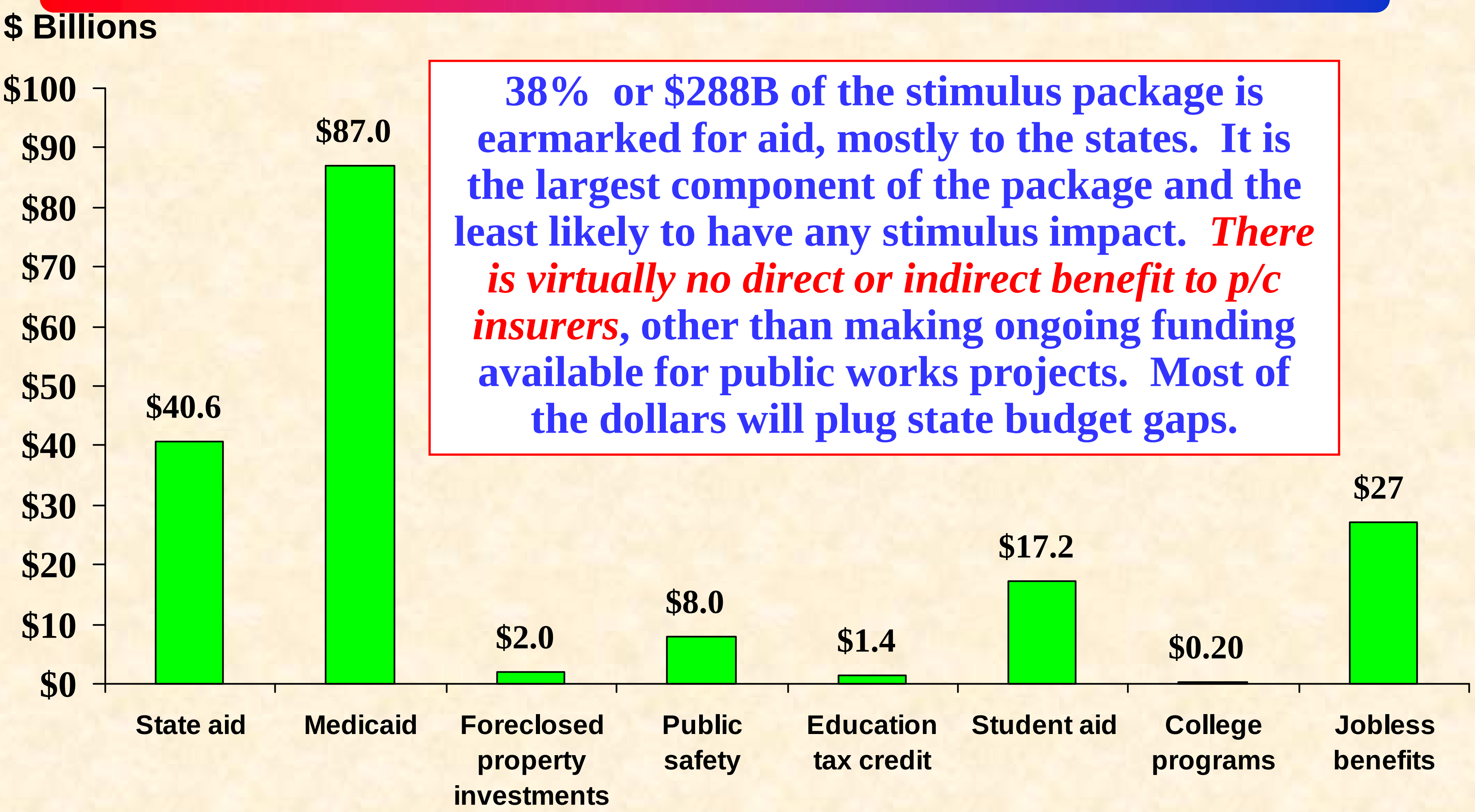
Source: Associated General Contractors at http://www.agc.org/cs/rebuild_americas_future (2/18/09); Insurance Info. Inst..

U.S. Economic $787B Stimulus Package: Major Tax Cut Components



Sources: The Wall Street Journal 2/13/09; Speaker of the House; House Ways and Means Committee; Senate Finance Committee; Insurance Information Institute.

U.S. Economic $787B Stimulus Package: Major Aid Components



38% or $288B of the stimulus package is earmarked for aid, mostly to the states. It is the largest component of the package and the least likely to have any stimulus impact. *There is virtually no direct or indirect benefit to p/c insurers*, other than making ongoing funding available for public works projects. Most of the dollars will plug state budget gaps.

Sources: The Wall Street Journal 2/13/09; Speaker of the House; House Ways and Means Committee; Senate Finance Committee; Insurance Information Institute.

State-by-State Infrastructure Spending

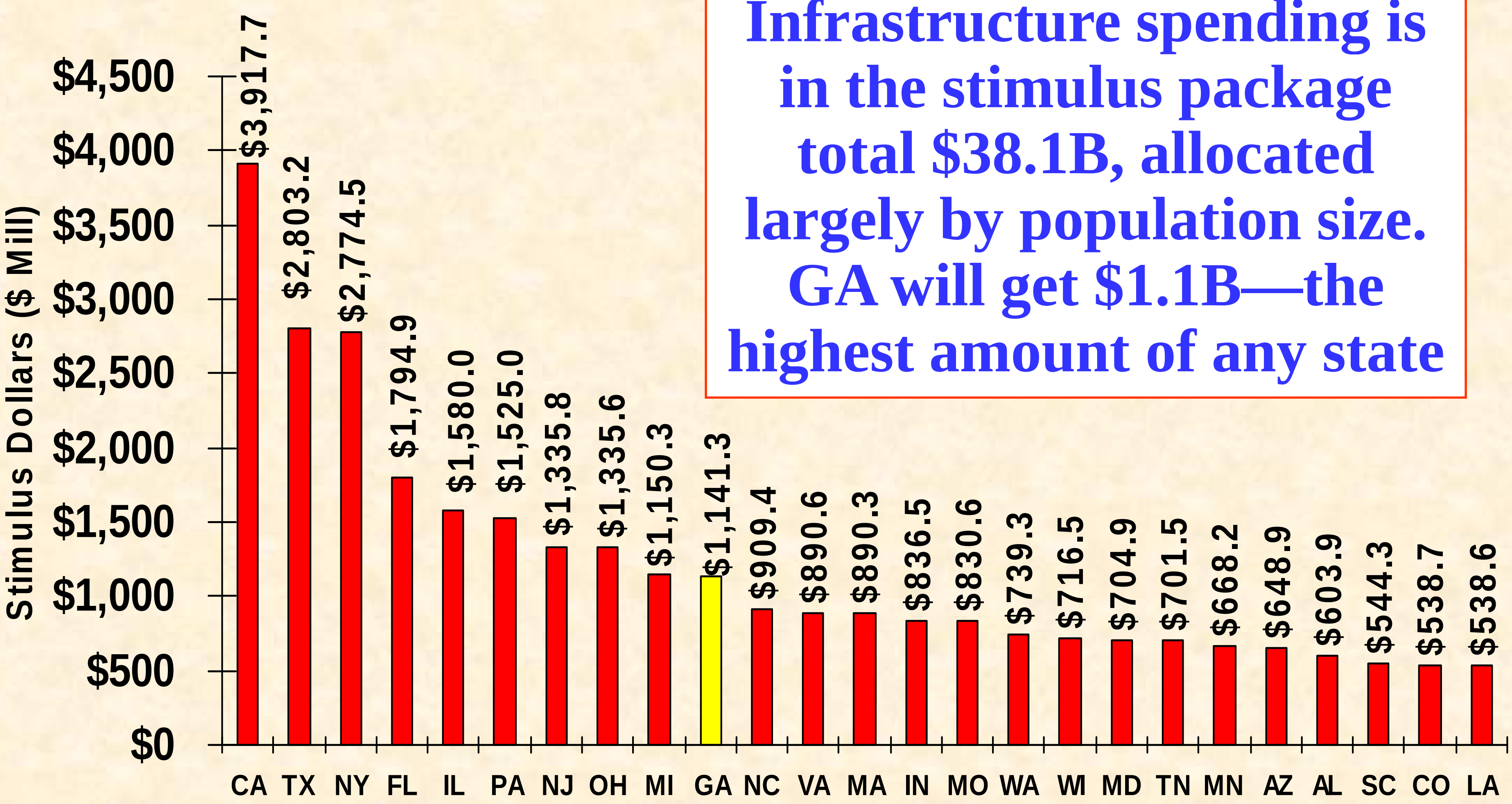
Bigger States Get More, Should Benefit Commercial Insurer Exposure

Infrastructure Stimulus Spending by State (Total = $38.1B)

State	Allocation	State	Allocation	State	Allocation
AL	$603,871,807	LA	$538,575,876	OK	$535,407,908
AK	$240,495,117	ME	$174,285,111	OR	$453,788,475
AZ	$648,928,995	MD	$704,863,248	PA	$1,525,011,979
AR	$405,531,459	MA	$890,333,825	RI	$192,902,023
CA	$3,917,656,769	MI	$1,150,282,308	SC	$544,291,398
CO	$538,669,174	MN	$668,242,481	SD	$213,511,174
CT	$487,480,166	MS	$415,257,720	TN	$701,516,776
DE	$158,666,838	MO	$830,647,063	TX	$2,803,249,599
DC	$267,617,455	MT	$246,599,815	UT	$292,231,904
FL	$1,794,913,566	NE	$278,897,762	VT	$150,666,577
GA	$1,141,255,941	NV	$270,010,945	VA	$890,584,959
HI	$199,866,172	NH	$181,678,856	WA	$739,283,923
ID	$219,528,313	NJ	$1,335,785,100	WV	$290,479,108
IL	$1,579,965,373	NM	$299,589,086	WI	$716,457,120
IN	$836,483,568	NY	$2,774,508,711	WY	$186,111,170
IA	$447,563,924	NC	$909,397,136	U.S. Territories	$238,045,760
KS	$413,837,382	ND	$200,318,301		
KY	$521,153,404	OH	$1,335,600,553	Total	$38,101,898,173

Sources: USA Today, 2/17/09; House Transportation and Infrastructure Committee; the Associated Press.

Infrastructure Stimulus Spending By State: Top 25 States ($ Millions)

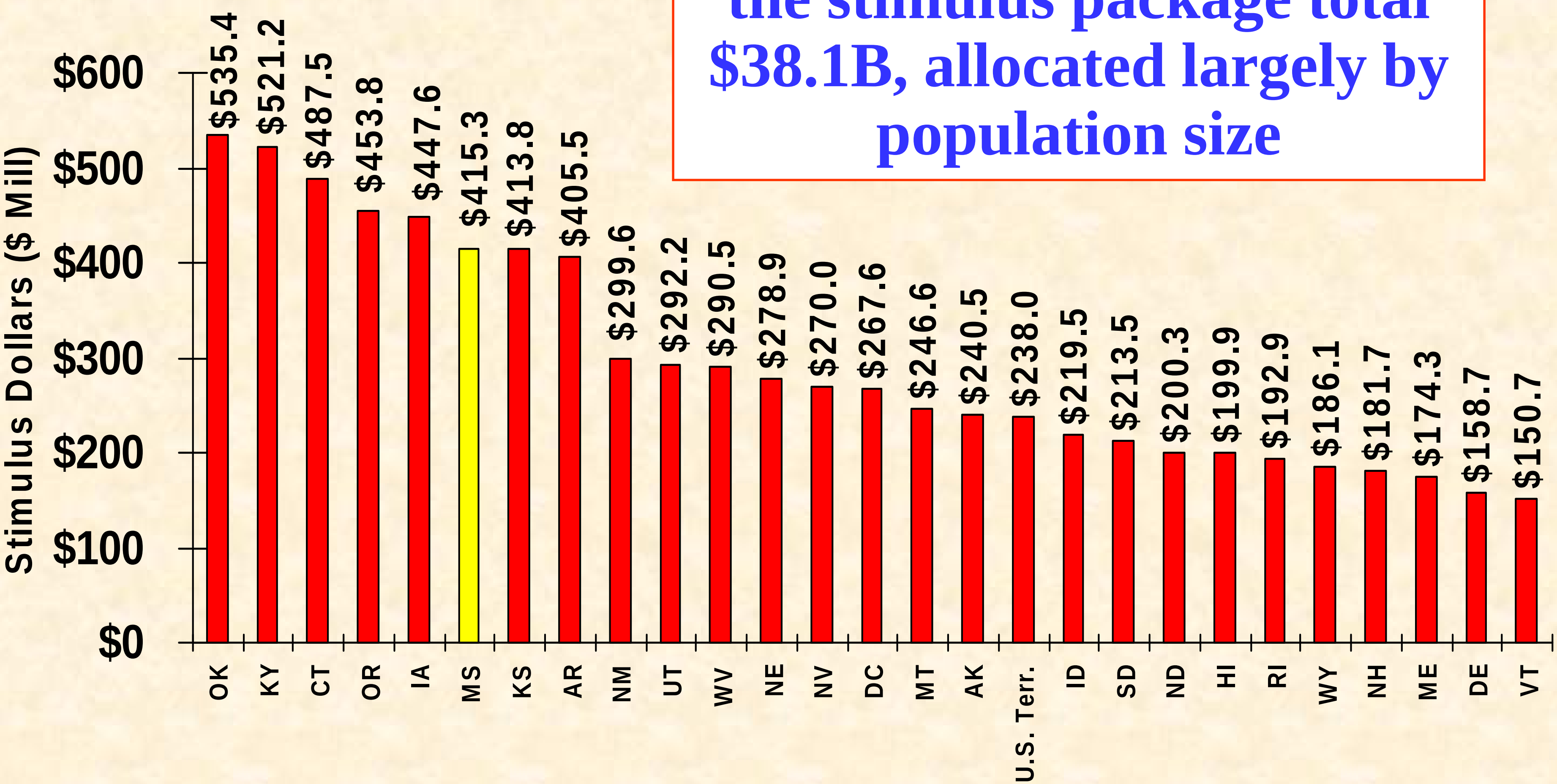


Infrastructure spending is in the stimulus package total $38.1B, allocated largely by population size. GA will get $1.1B—the highest amount of any state

Sources: USA Today 2/19/09; House Transportation and Infrastructure Committee; the Associated Press.

Infrastructure Stimulus Spending By State: Bottom 25 States ($ Millions)

Infrastructure spending is in the stimulus package total $38.1B, allocated largely by population size



Sources: USA Today 2/19/09; House Transportation and Infrastructure Committee; the Associated Press.

Expected Number of Jobs Gained or Preserved by Stimulus Spending

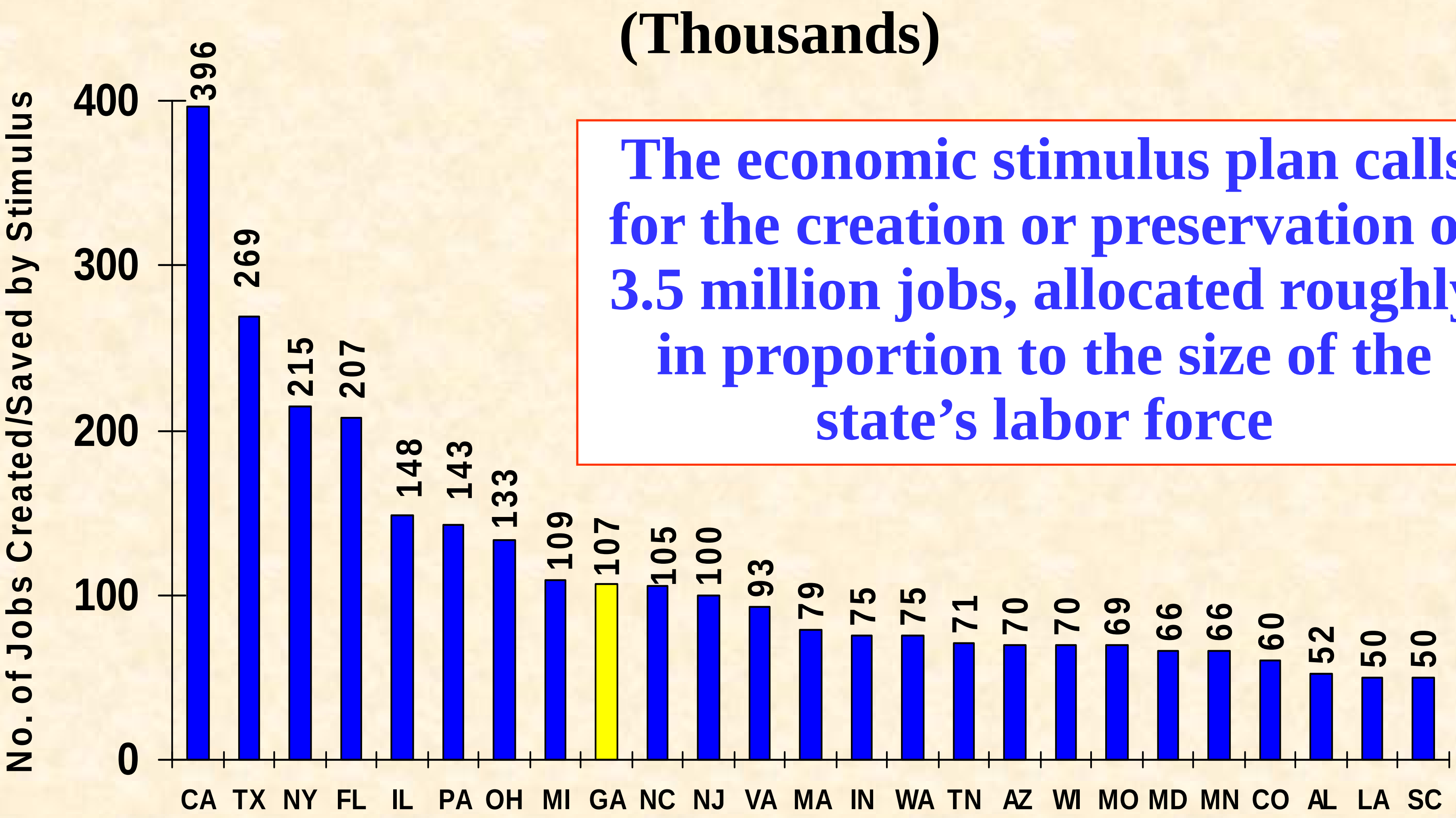
Larger States = More Jobs Workers Comp Benefits

Estimated Job Effect of Stimulus: Jobs Created/Saved By State = 3.5 Mill Total

State	Jobs Created	State	Jobs Created	State	Jobs Created
AL	52,000	LA	50,000	OK	40,000
AK	8,000	ME	15,000	OR	44,000
AZ	70,000	MD	66,000	PA	143,000
AR	32,000	MA	79,000	RI	12,000
CA	396,000	MI	109,000	SC	50,000
CO	60,000	MN	66,000	SD	10,000
CT	41,000	MS	30,000	TN	71,000
DE	11,000	MO	69,000	TX	269,000
DC	12,000	MT	11,000	UT	32,000
FL	207,000	NE	23,000	VT	8,000
GA	107,000	NV	34,000	VA	93,000
HI	16,000	NH	16,000	WA	75,000
ID	17,000	NJ	100,000	WV	20,000
IL	148,000	NM	22,000	WI	70,000
IN	75,000	NY	215,000	WY	8,000
IA	37,000	NC	105,000		
KS	33,000	ND	9,000		
KY	48,000	OH	133,000	Total	3,467,000

Sources: http://www.recovery.gov/; Council of Economic Advisers; Insurance Information Institute.

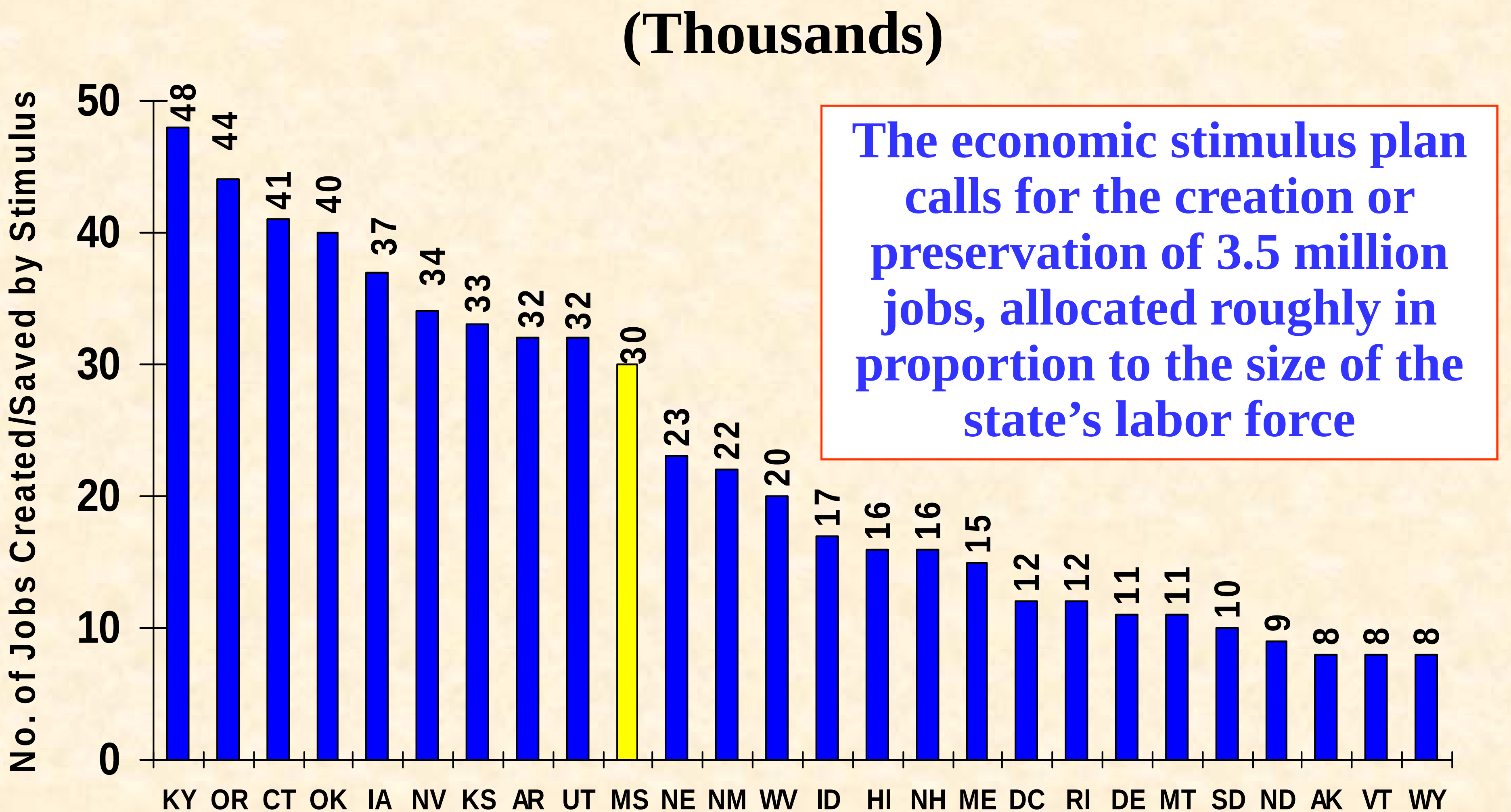
Estimated Job Effect of Stimulus Spending By State: Top 25 States



The economic stimulus plan calls for the creation or preservation of 3.5 million jobs, allocated roughly in proportion to the size of the state's labor force

Sources: http://www.recovery.gov/; Council of Economic Advisers Insurance Information Institute.

Estimated Job Effect of Stimulus Spending By State: Bottom 25 States



Sources: http://www.recovery.gov/; Council of Economic Advisers Insurance Information Institute.

Stimulus: Reading The Economic Tea Leaves for the Next 4 to 8 Years

- **Growing Role of Government: 2009 Stimulus Package and Other Likely Spending Initiatives Guarantee that Government Will Play a Much Larger Role Than at Any Other Time in Recent History**
  - **Every industry, including insurance, will and must attempt to maximize direct and indirect benefits from this paradigm shift**
- **Obama Administration Priorities: Stimulus Package Acts as "Economic Tea Leaf" on the Administration's Fiscal Priorities for the Next Several Years**
- **These Include:**
  - **Alternative Energy**
  - **Health Care**
  - **Education**
  - **Aging/New Infrastructure**
  - **Environment**
- **Stimulus is Only One Leg of the Stool**
  - **(1) Stimulus; (2) Housing, and (3) Financial Services Reform**

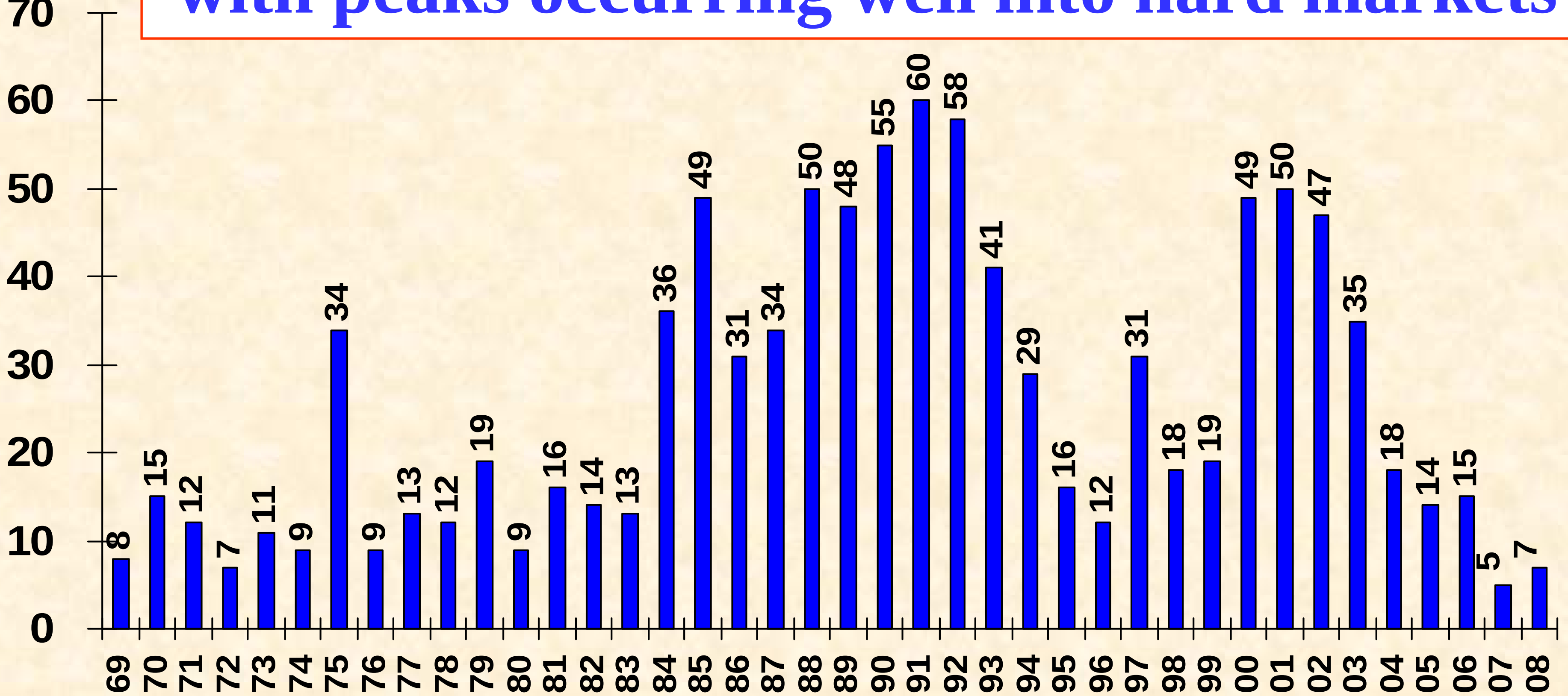
Source: Insurance Information Institute

FINANCIAL STRENGTH & RATINGS

Industry Has Weathered the Storms Well

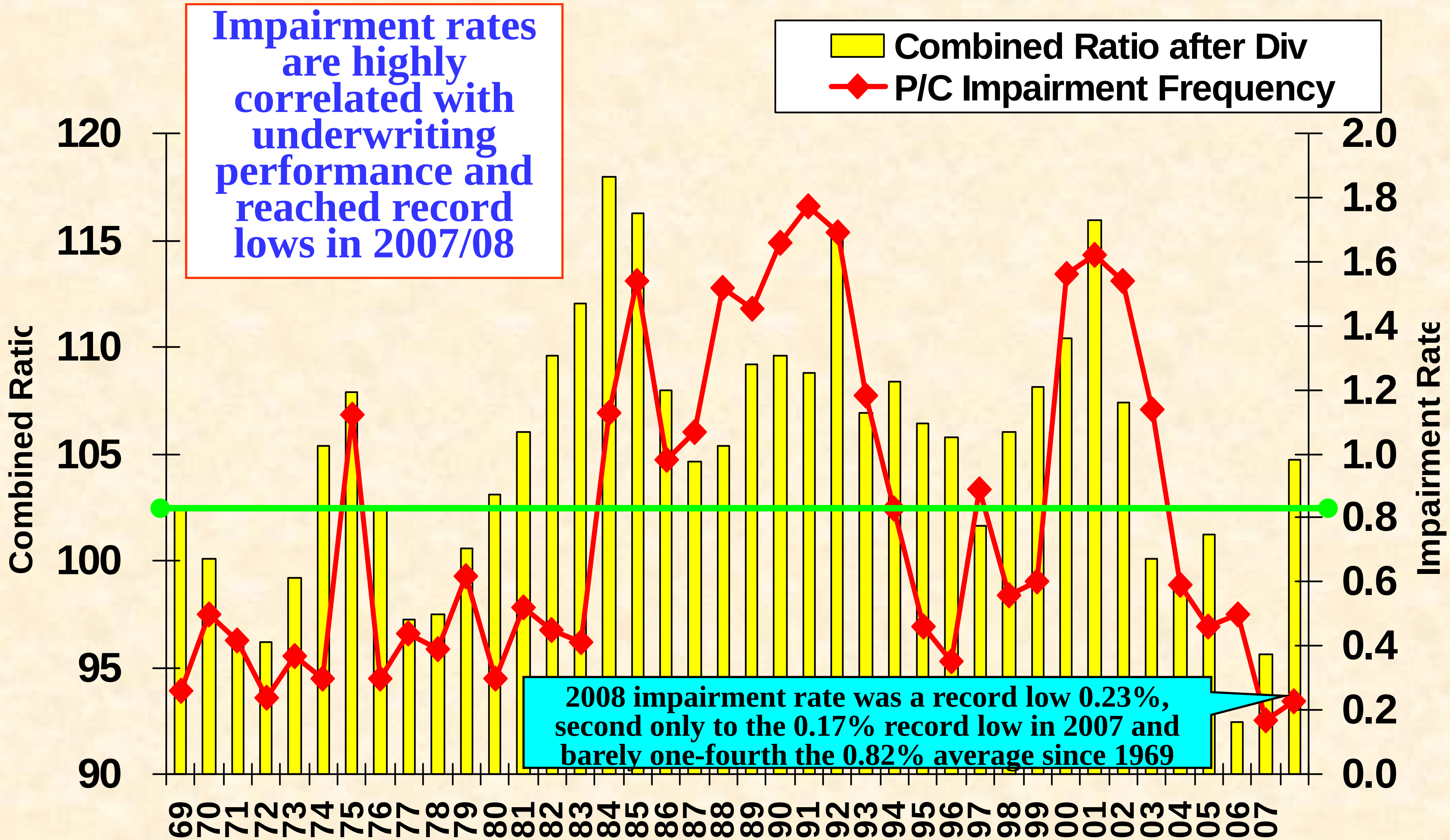
P/C Insurer Impairments, 1969-2008

The number of impairments varies significantly over the p/c insurance cycle, with peaks occurring well into hard markets



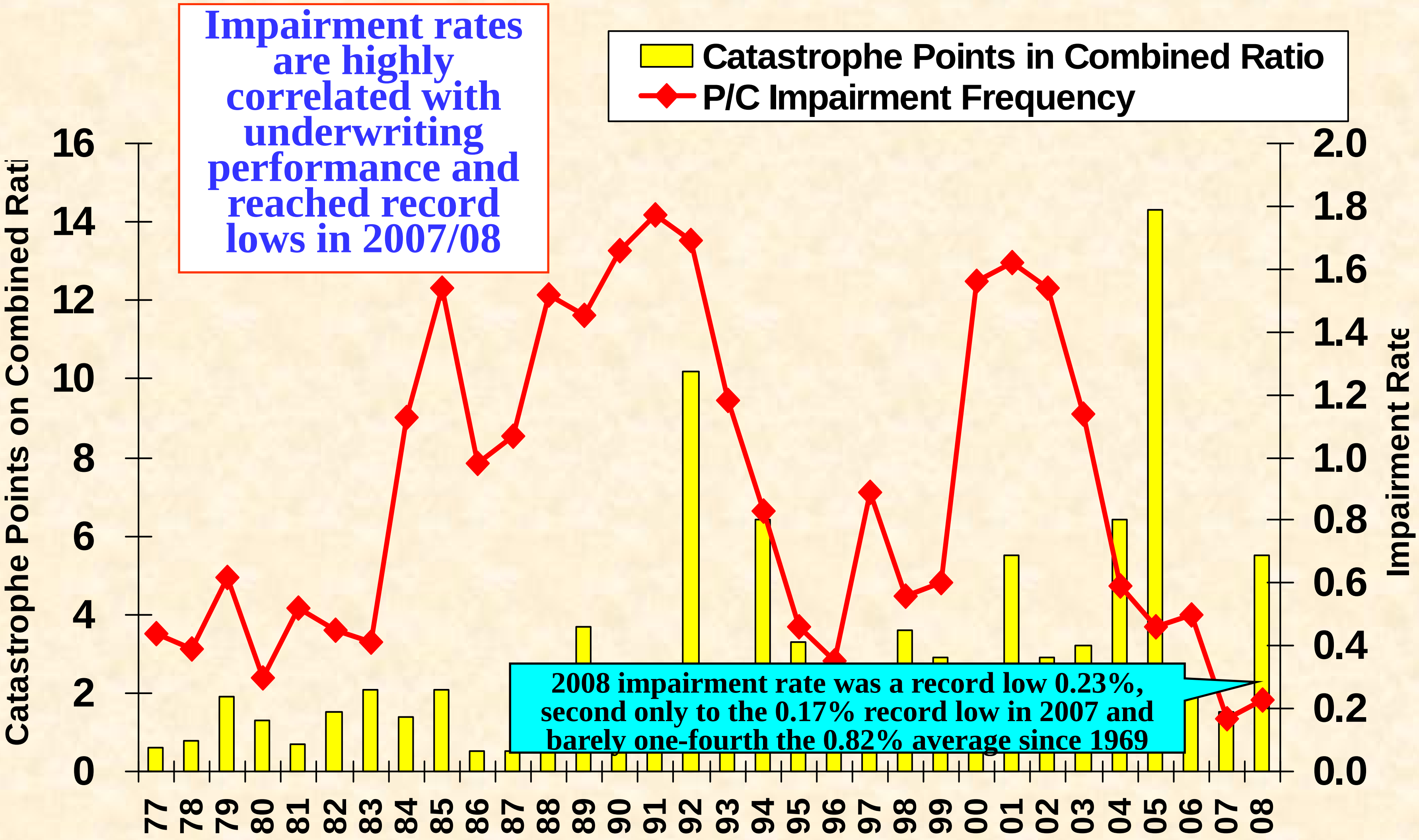
Source: A.M. Best; Insurance Information Institute

P/C Insurer Impairment Frequency vs. Combined Ratio, 1969-2008



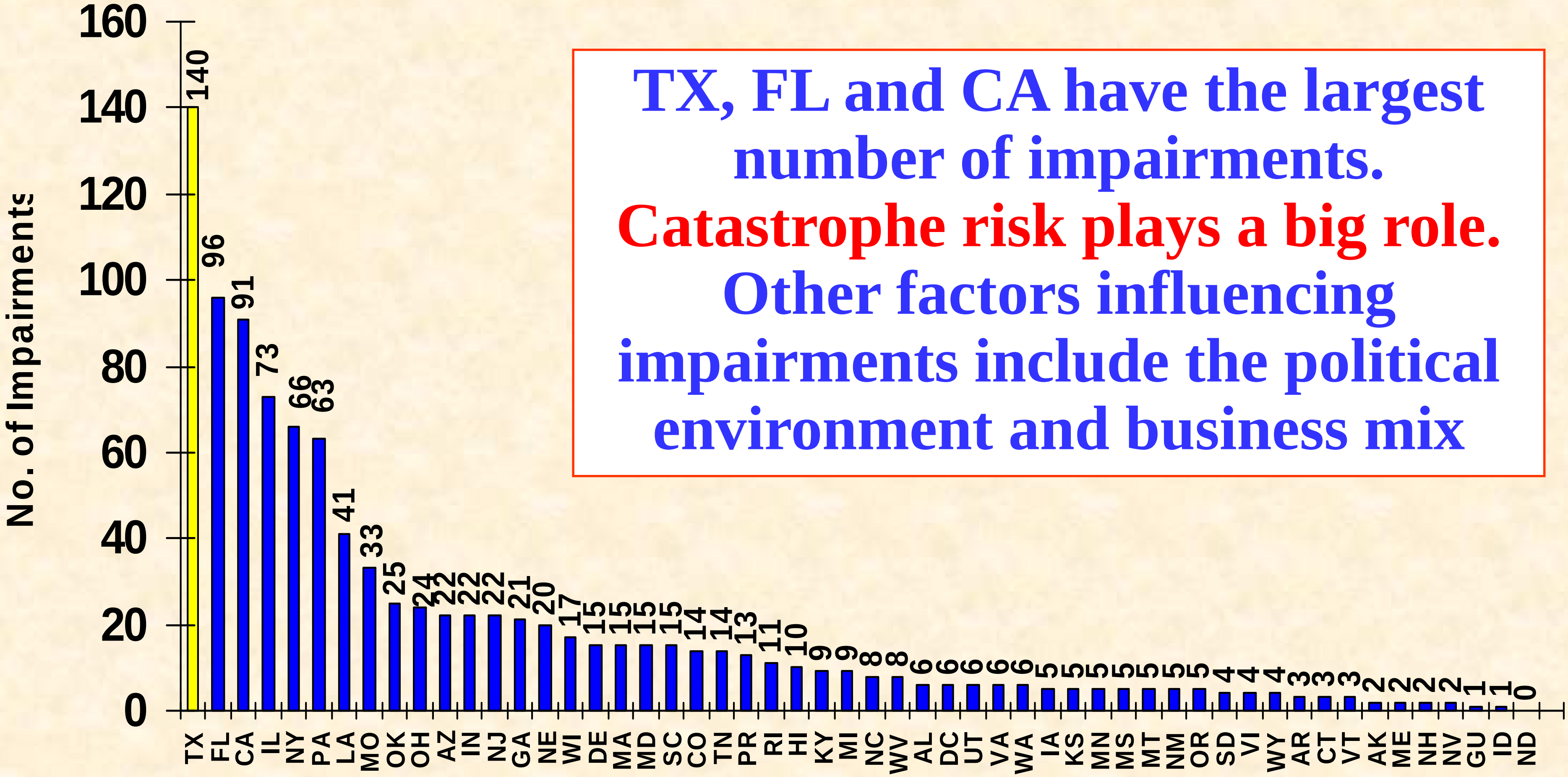
Source: A.M. Best; Insurance Information Institute

P/C Impairment Frequency vs. Catastrophe Points in Combined Ratio, 1977-2008



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

Number of Impairments by State, 1969-2008

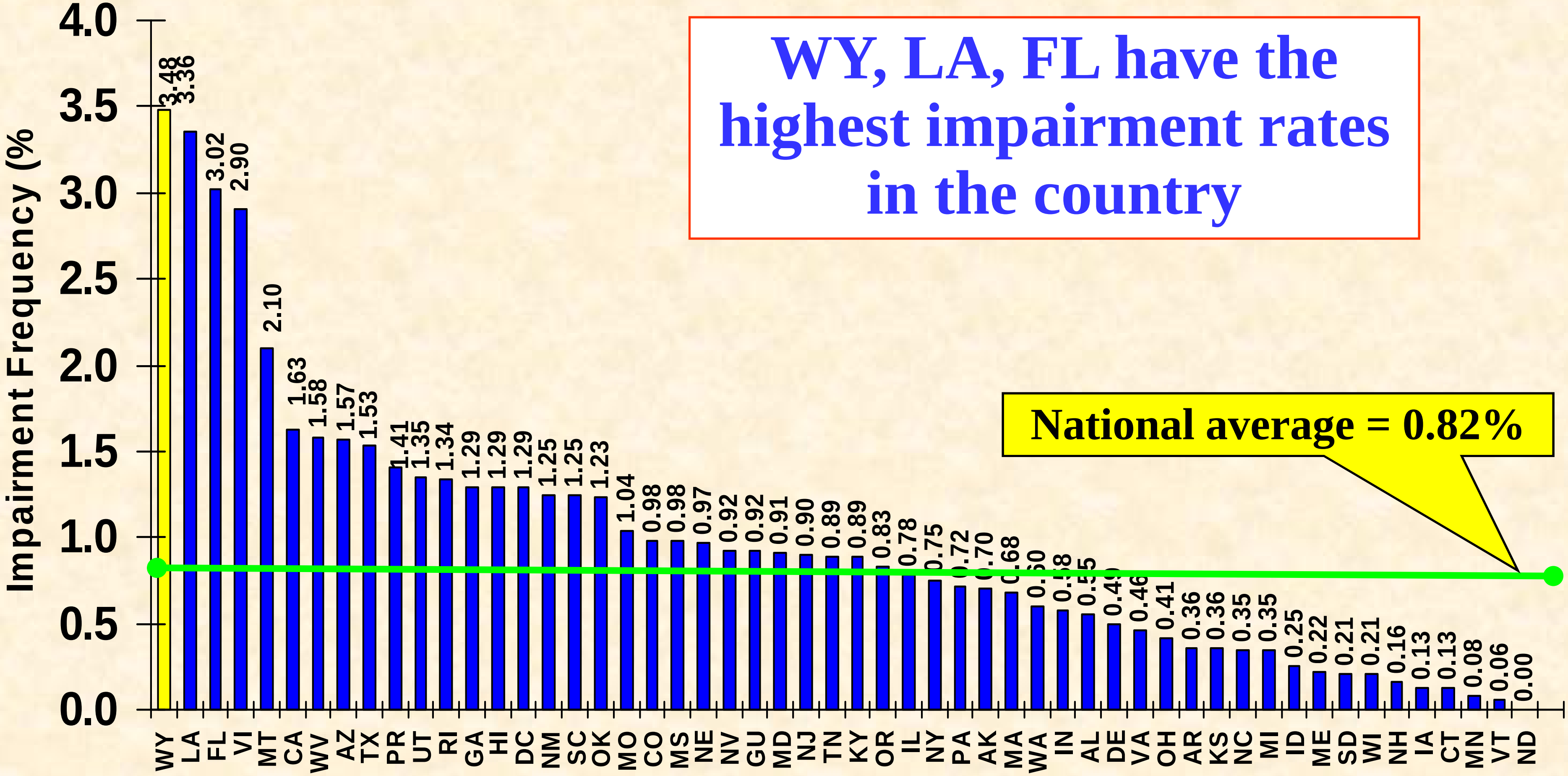


TX, FL and CA have the largest number of impairments. Catastrophe risk plays a big role. Other factors influencing impairments include the political environment and business mix

Source: A.M. Best; Insurance Information Institute

Frequency of Impairments by State, 1969-2008

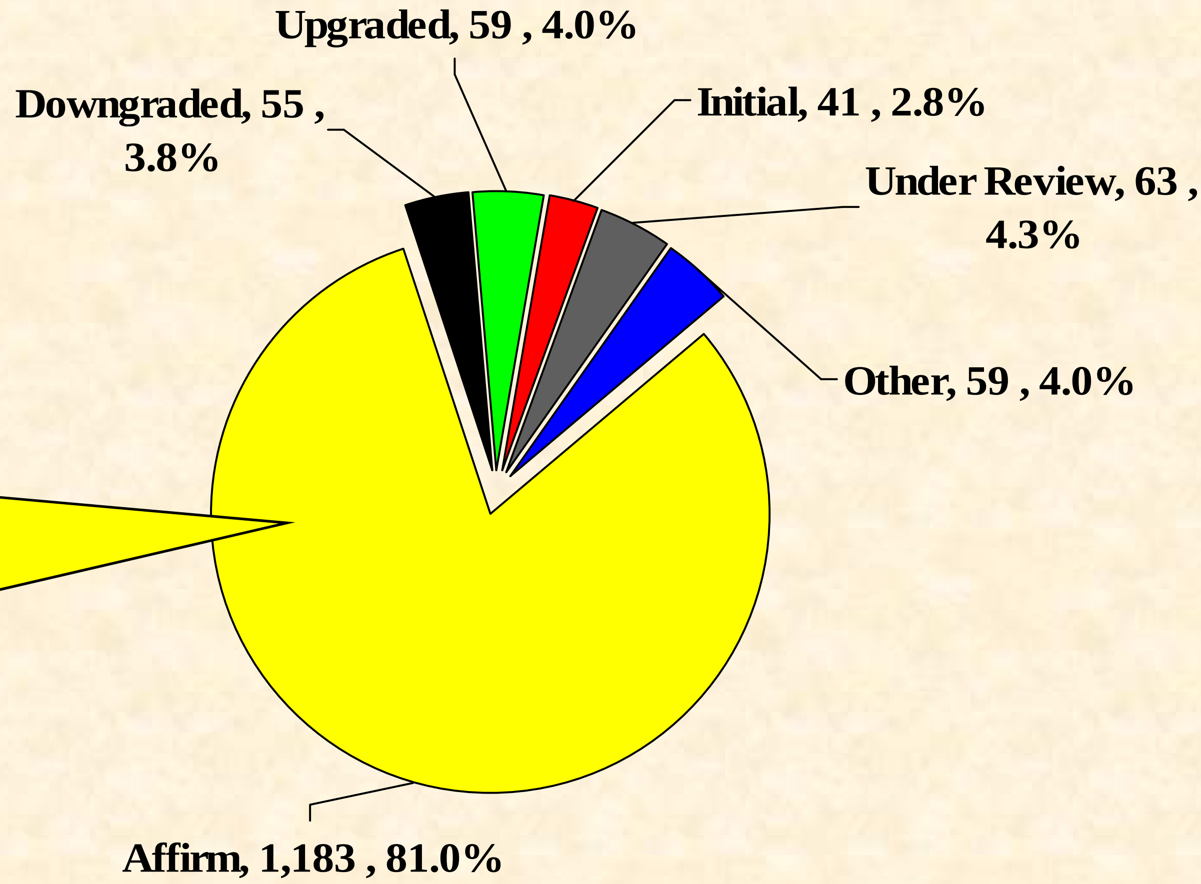
(Impairments per 100 Insurers Domiciled in State)



Source: A.M. Best; Insurance Information Institute

Summary of A.M. Best's P/C Insurer Ratings Actions in 2008*

P/C insurance is by design a resilient in business. The dual threat of financial disasters and catastrophic losses are anticipated in the industry's risk management strategy.



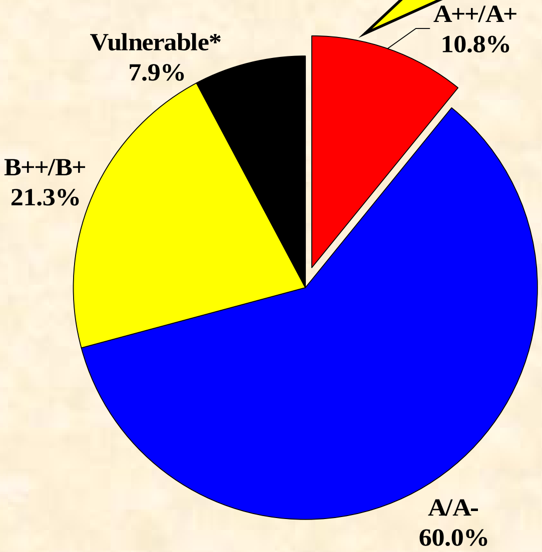
Despite financial market turmoil, high cat losses and a soft market in 2008, 81% of ratings actions by A.M. Best were affirmations; just 3.8% were downgrades and 4.0% upgrades

*Through December 19.
Source: A.M. Best.

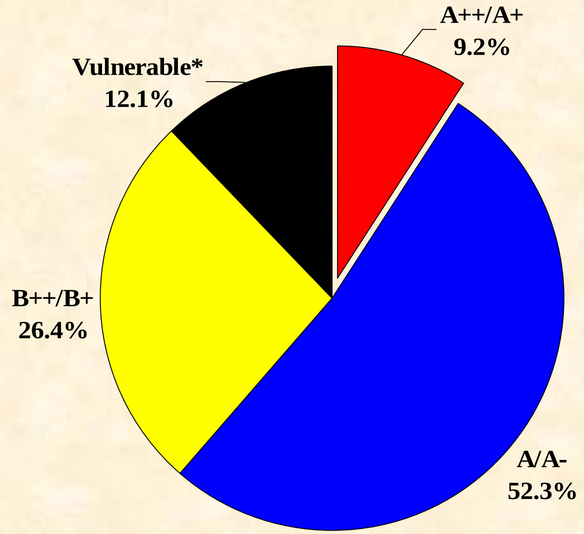
Historical Ratings Distribution,
US P/C Insurers, 2008 vs. 2005 and 2000

2008

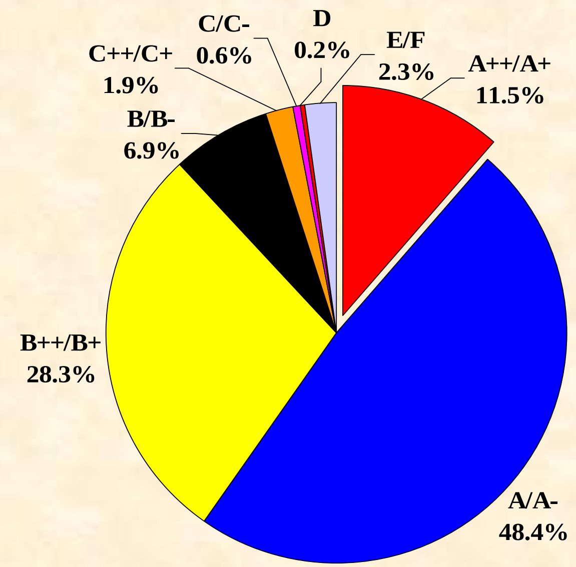
A++/A+ and A/A- gains



2005



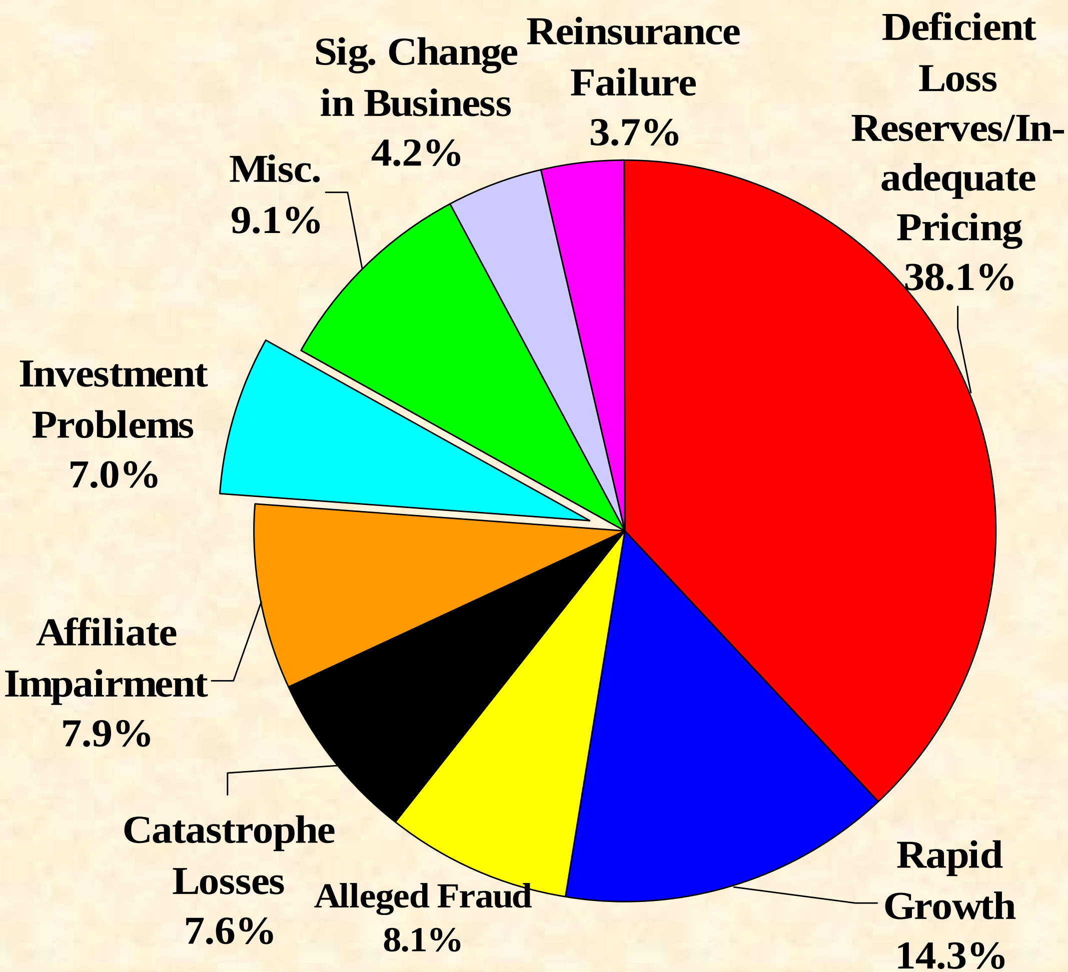
2000



P/C insurer financial strength has improved since 2005 despite financial crisis

Source: A.M. Best: *Rating Downgrades Slowed but Outpaced Upgrades for Fourth Consecutive Year,* Special Report, November 8, 2004 for 2000; 2006 and 2009 *Review & Preview*. *Ratings 'B' and lower.

Reasons for US P/C Insurer Impairments, 1969-2008



Deficient loss reserves and inadequate pricing are the leading cause of insurer impairments, underscoring the importance of discipline. Investment catastrophe losses play a much smaller role.

Source: A.M. Best: *1969-2008 Impairment Review*, Special Report, Apr. 6, 2008

Critical Differences Between P/C Insurers and Banks

Superior Risk Management Model & Low Leverage Make a Big Difference

How 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 50 banks have gone under as of 4/17)**
    - ***The Promise is Being Fulfilled***
  - **Renew existing policies (banks are reducing and eliminating lines of credit)**
  - **Write new policies (banks are turning away people who want or need to borrow)**
  - **Develop new products (banks are scaling back the products they offer)**

Source: Insurance Information Institute

Reasons Why P/C Insurers Have Fewer Problems Than Banks: A Superior Risk Management Model

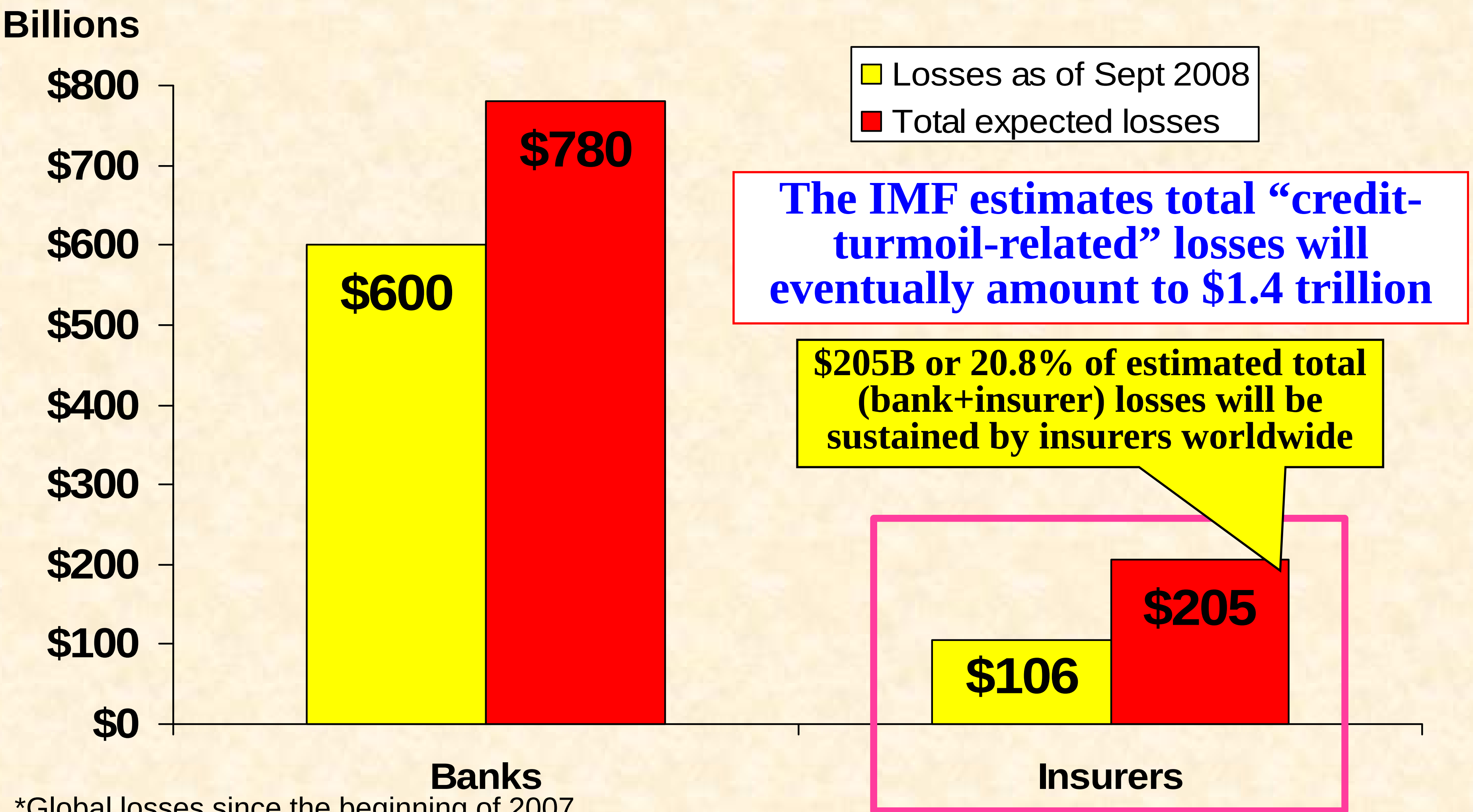
- ***Emphasis on Underwriting***
  - **Matching of risk to price (via experience and modeling)**
  - **Limiting of potential loss exposure**
  - ***Some banks sought to maximize volume and fees and disregarded risk***
- ***Strong Relationship Between Underwriting and Risk Bearing***
  - **Insurers always 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

The Financial Crisis in Perspective

Bank vs. Insurer Impacts

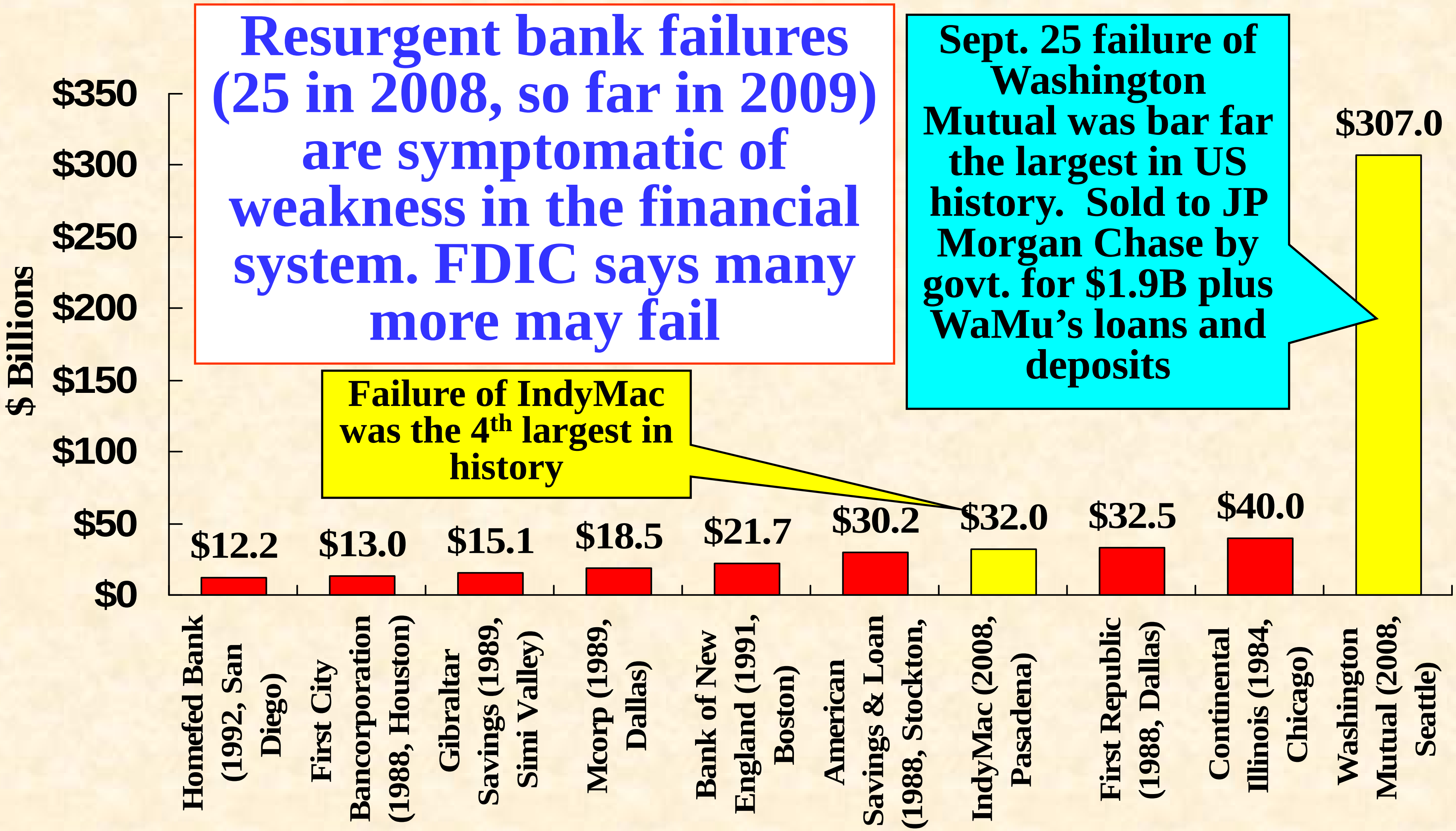
Financial Institutions Globally Facing Huge Losses from the Credit Crunch*



*Global losses since the beginning of 2007.

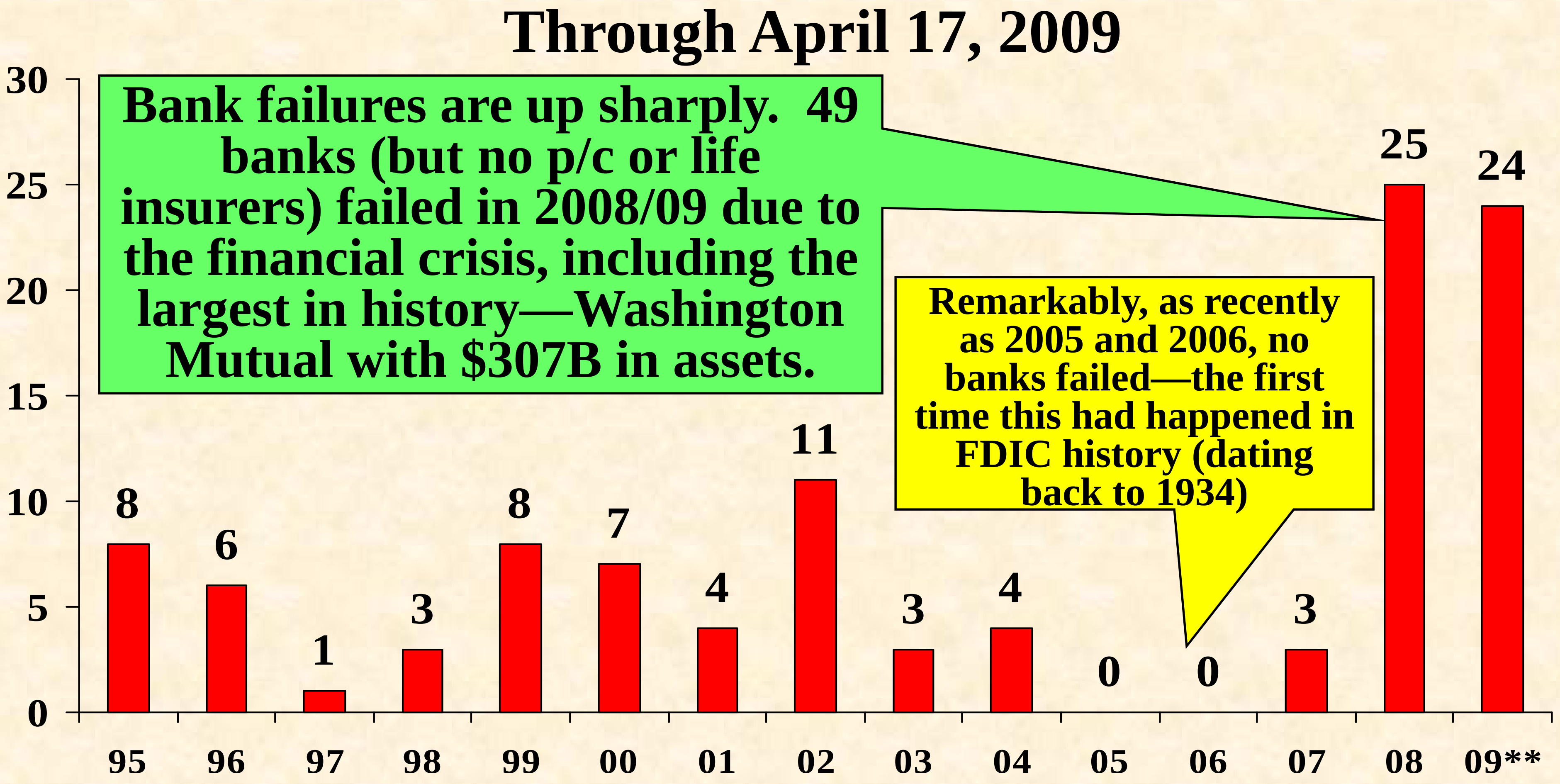
Source: IMF Global Financial Stability Report, October 2008, IIF, Bloomberg, cited in a presentation by Thomas Hess (Chief Economist, Swiss Re) October 23, 2008, accessed via Geneva Association web site.

Top 10 Largest Bank Failures



Source: FDIC; Insurance Information Institute research.

US Bank Failures:*
1995-2009**

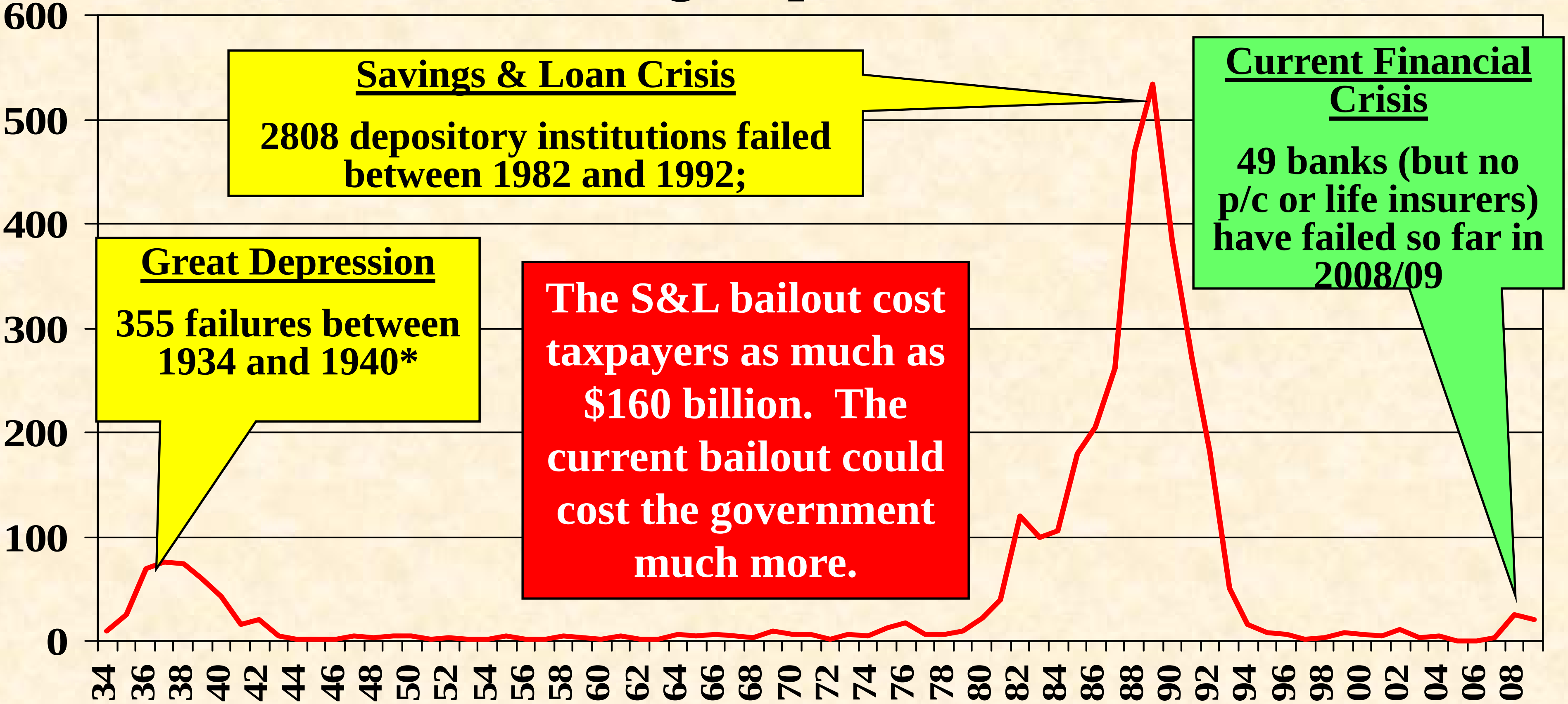


*Includes all commercial banking and savings institutions. **Through April 17.

Source: FDIC: http://www.fdic.gov/bank/historical/bank/index.html; Insurance Info. Institute

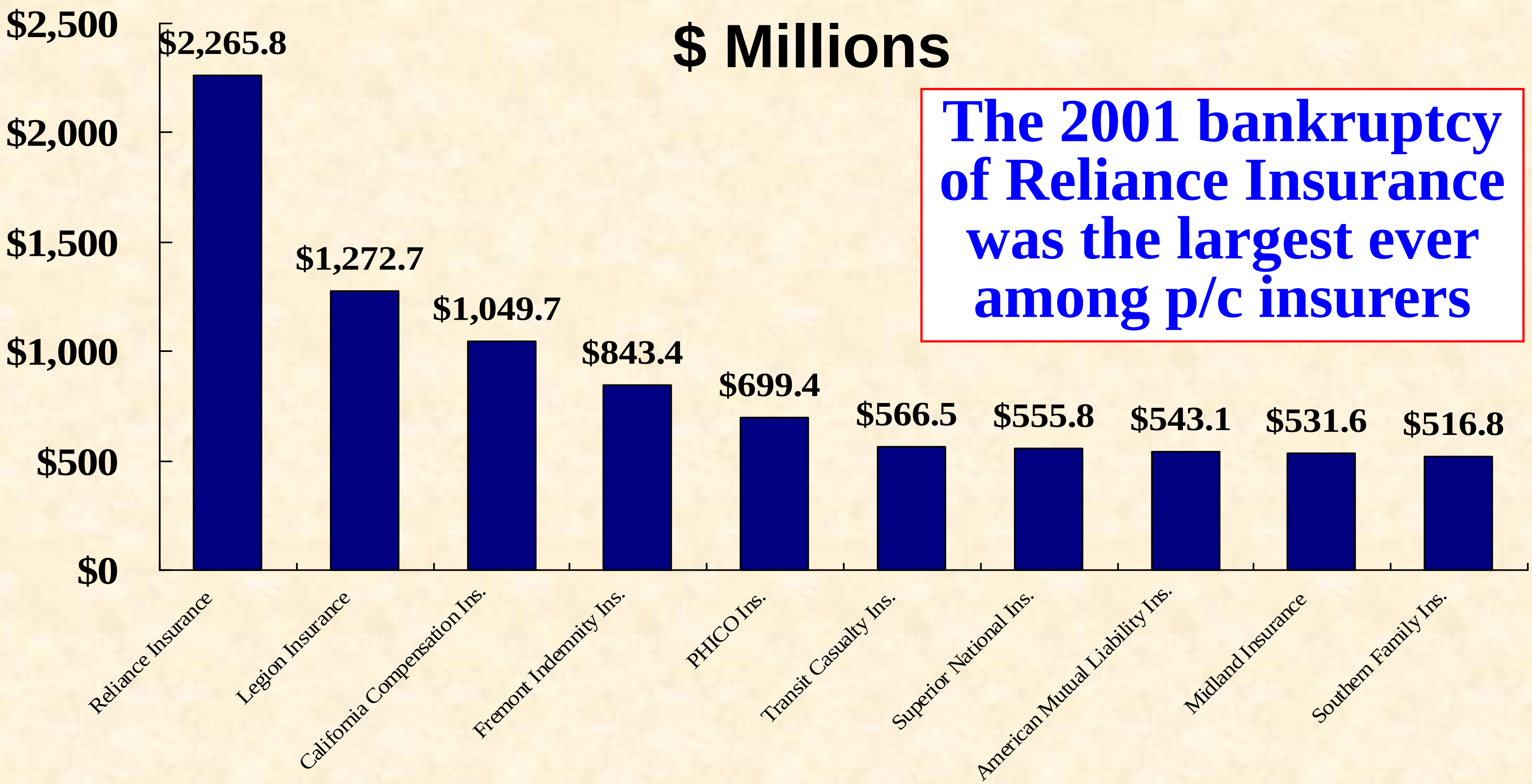
US Bank Failures:*
1934-2009**

Through April 17, 2009



*Includes all commercial banking and savings institutions.
**Data begin in 1934, the year the FDIC was established.
Source: FDIC: http://www.fdic.gov/bank/historical/bank/index.html; Insurance Info. Institute

Top 10 P/C Insolvencies, Based Upon Guaranty Fund Payments*



* Disclaimer: This is not a complete picture. If anything the numbers are understated as some states have not reported in certain years.

Source: National Conference of Insurance Guaranty Funds, as of September 17, 2008.

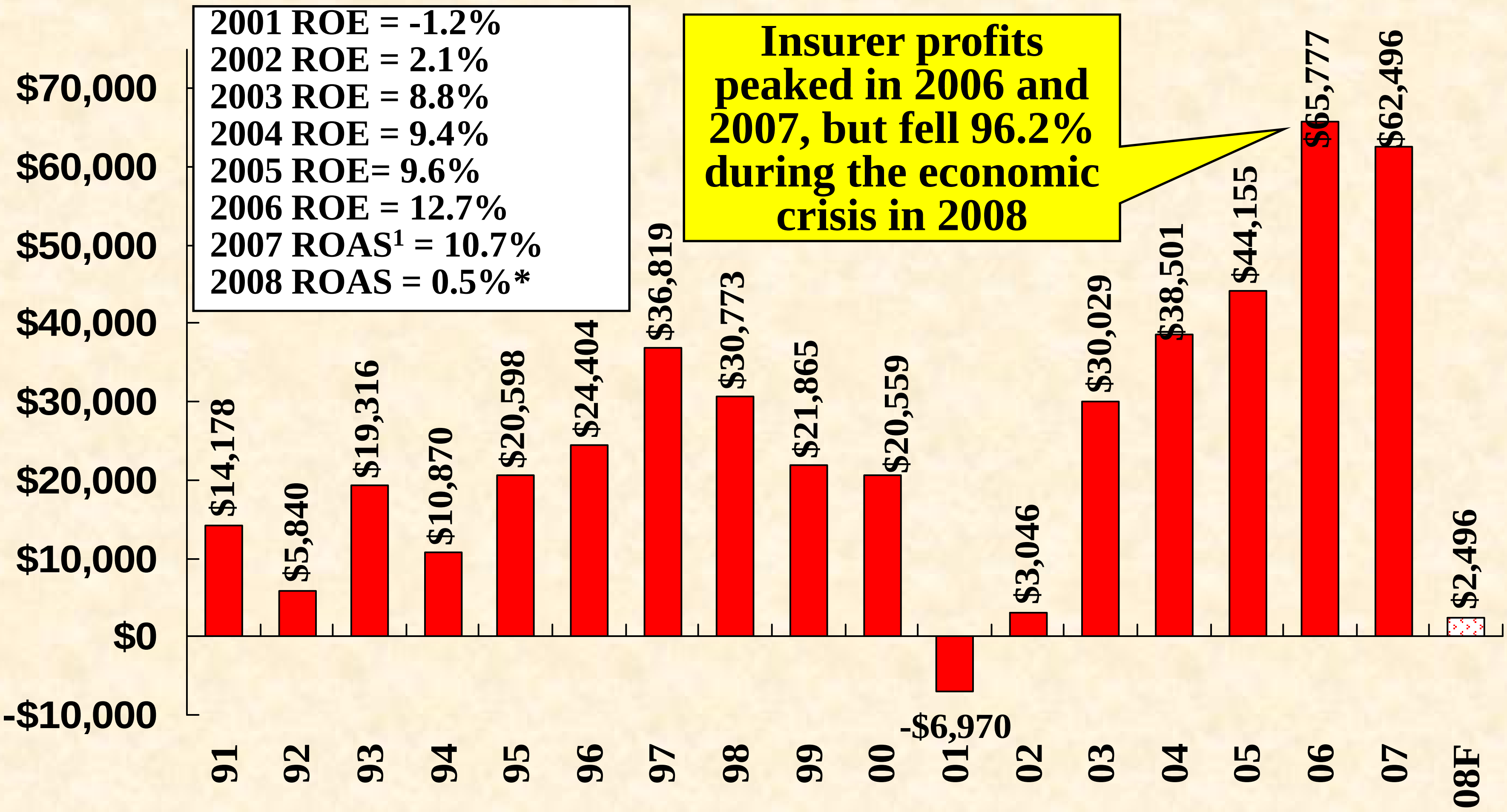
P/C INSURANCE FINANCIAL PERFORMANCE

A Resilient Industry in Challenging Times

Profitability

Historically Volatile

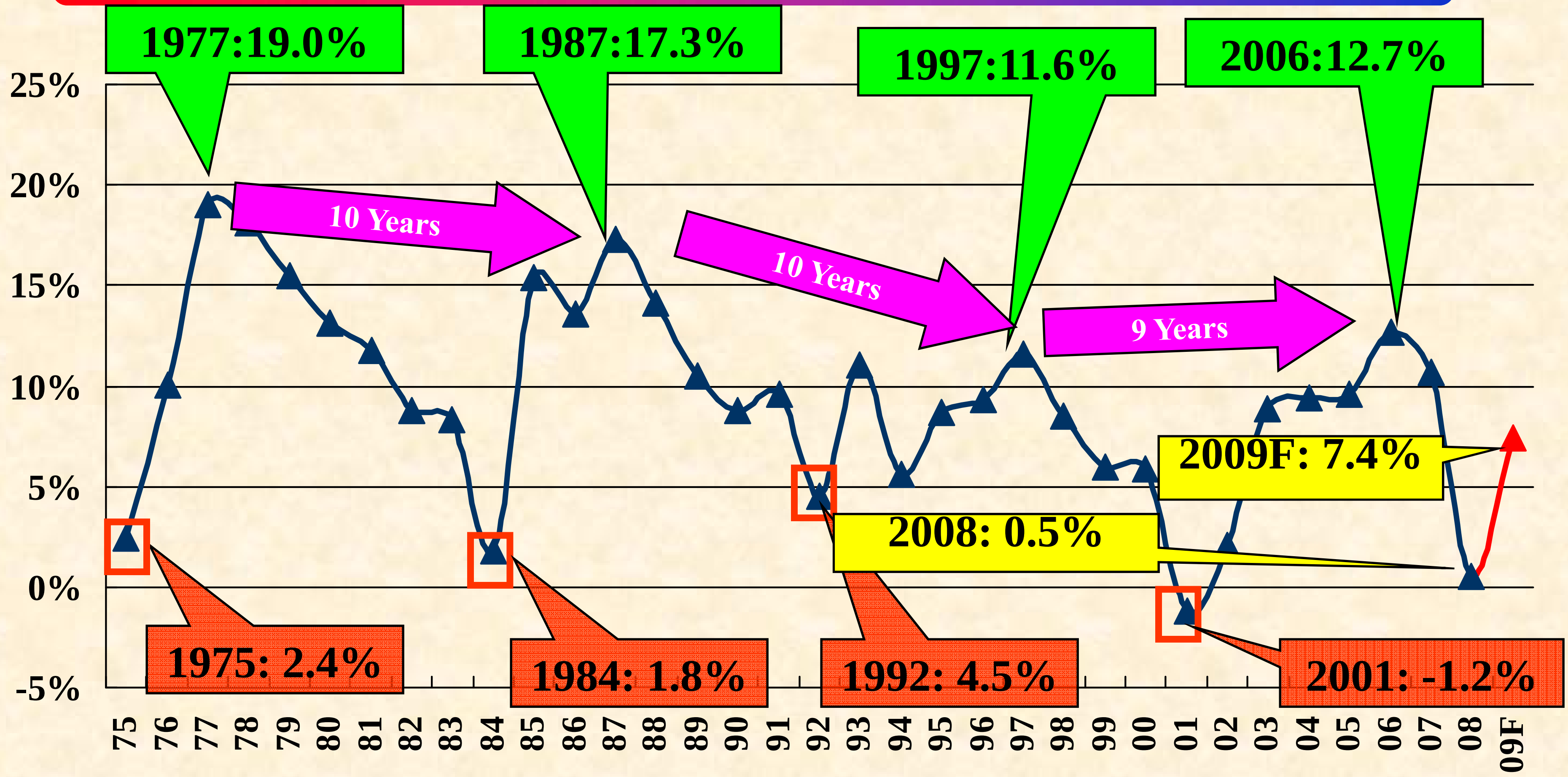
P/C Net Income After Taxes 1991-2008F ($ Millions)*



*ROE figures are GAAP; [1]Return on avg. Surplus. Excluding Mortgage & Financial Guarantee insurers yields an 4.2% ROAS for 2008.

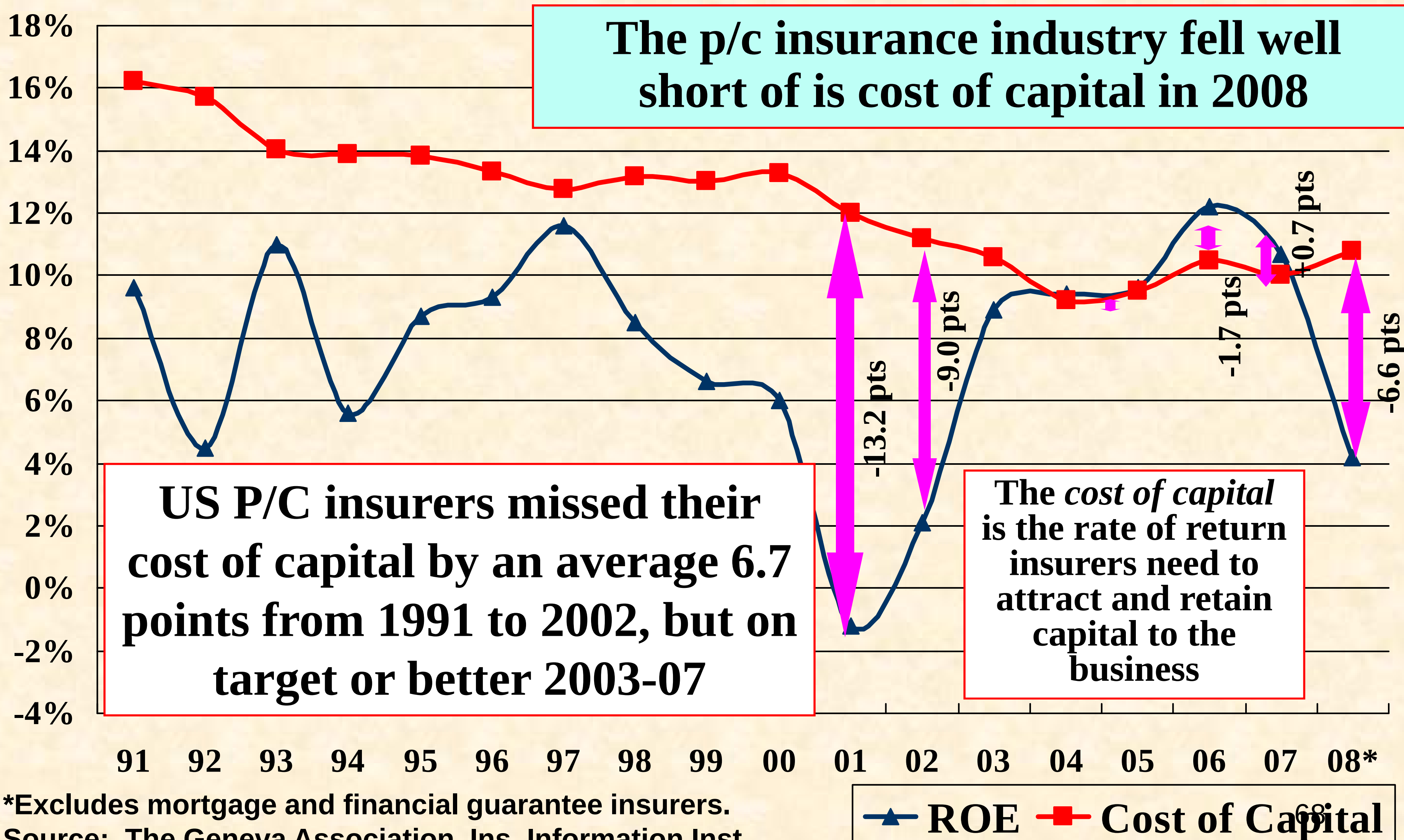
Sources: A.M. Best, ISO, Insurance Information Inst.

P/C Insurance Industry ROEs, 1975 – 2009F*



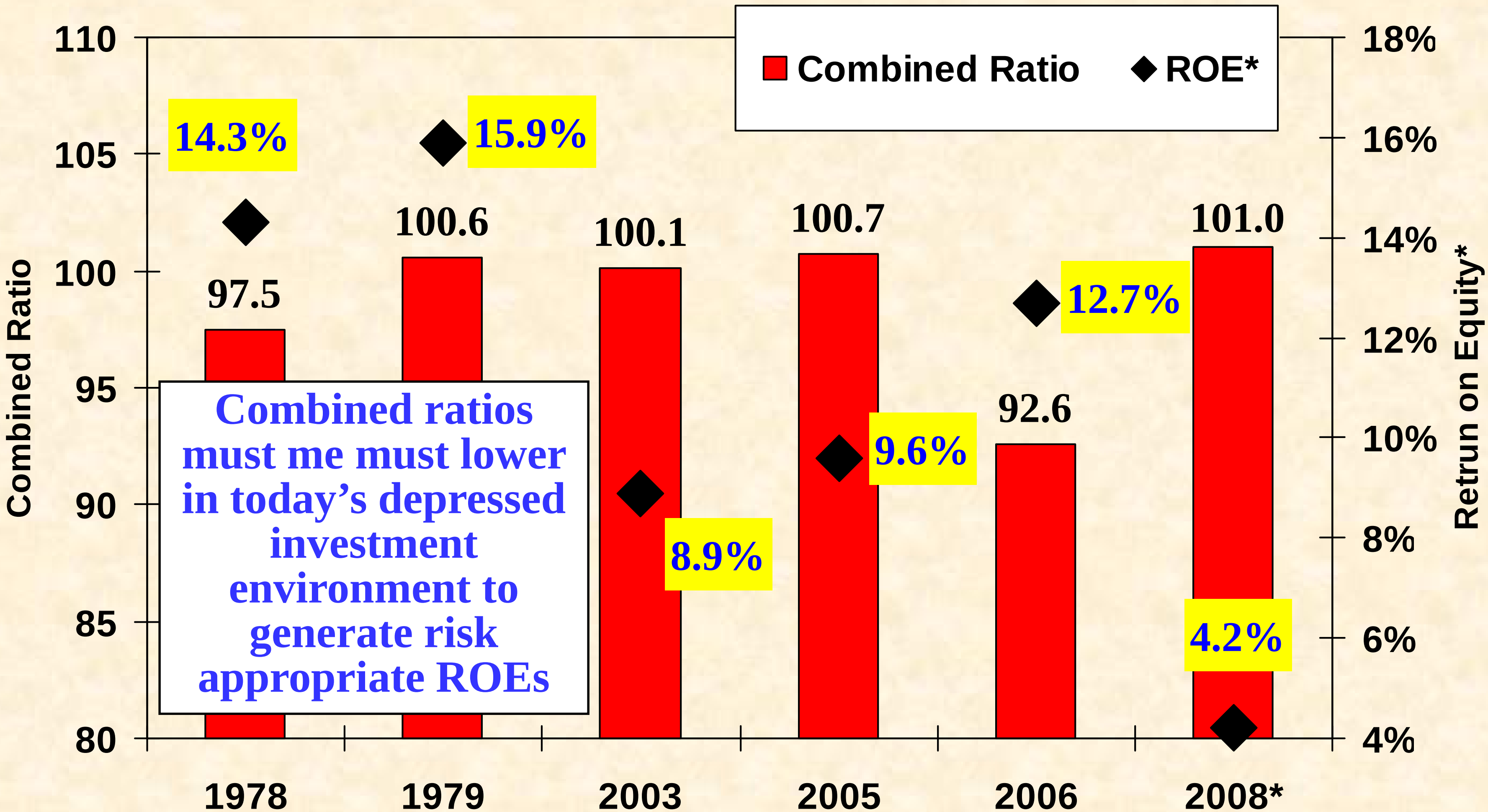
Note: 2008 result excluding Mortgage & Financial Guarantee insurers is 4.2%.
Sources: ISO; A.M. Best (2009F); Insurance Information Institute.

ROE vs. Equity Cost of Capital: US P/C Insurance:1991-2008



*Excludes mortgage and financial guarantee insurers.
Source: The Geneva Association, Ins. Information Inst.

A 100 Combined Ratio Isn't What it Used to Be: 95 is Where It's At



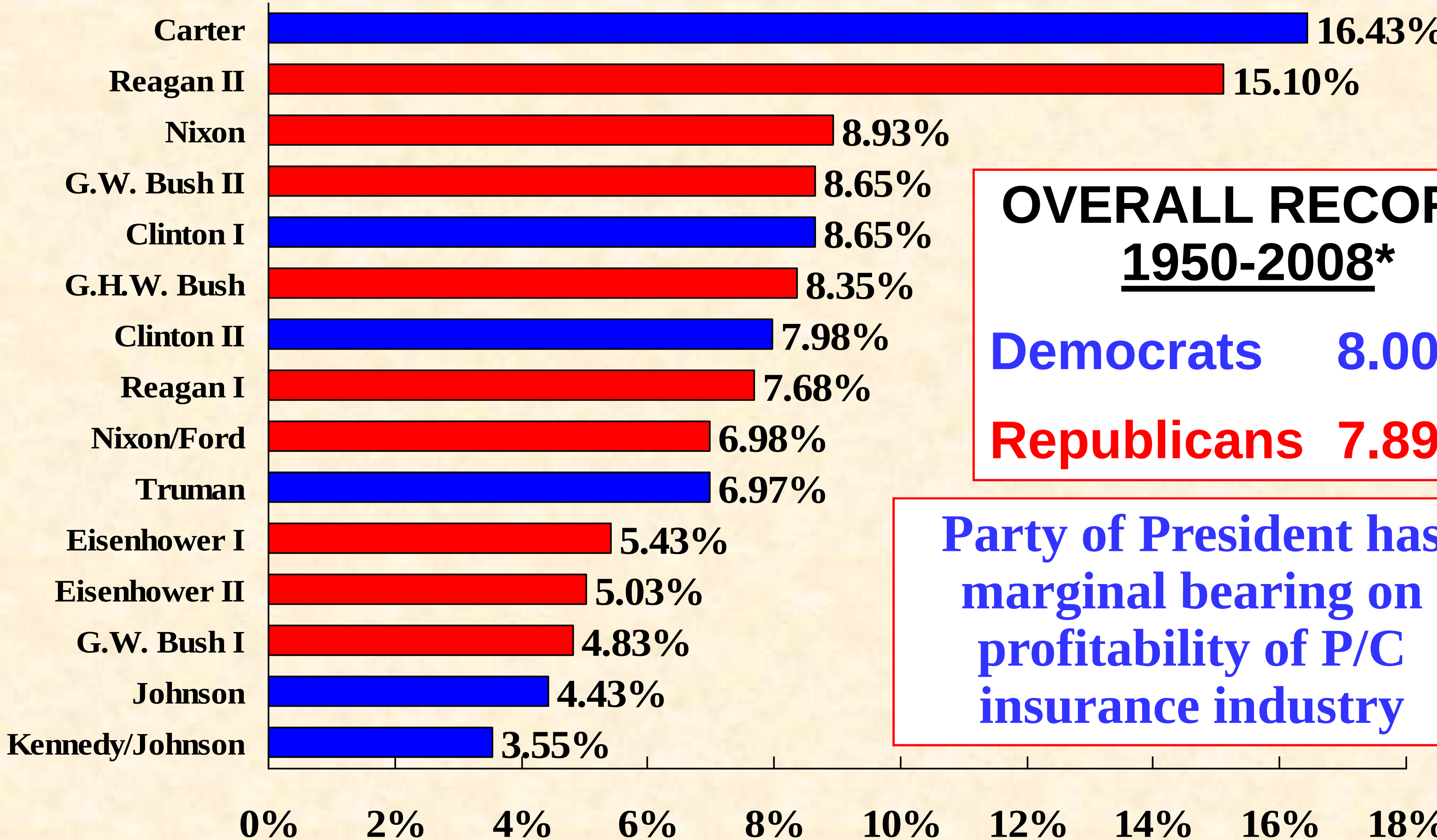
* 2008 figure is return on average statutory surplus. Excludes mortgage and financial guarantee insurers.

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

Presidential Politics & P/C Insurance

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

P/C Insurance Industry ROE by Presidential Administration,1950-2008*



OVERALL RECORD:
1950-2008*

Democrats	**8.00%**
Republicans	**7.89%**

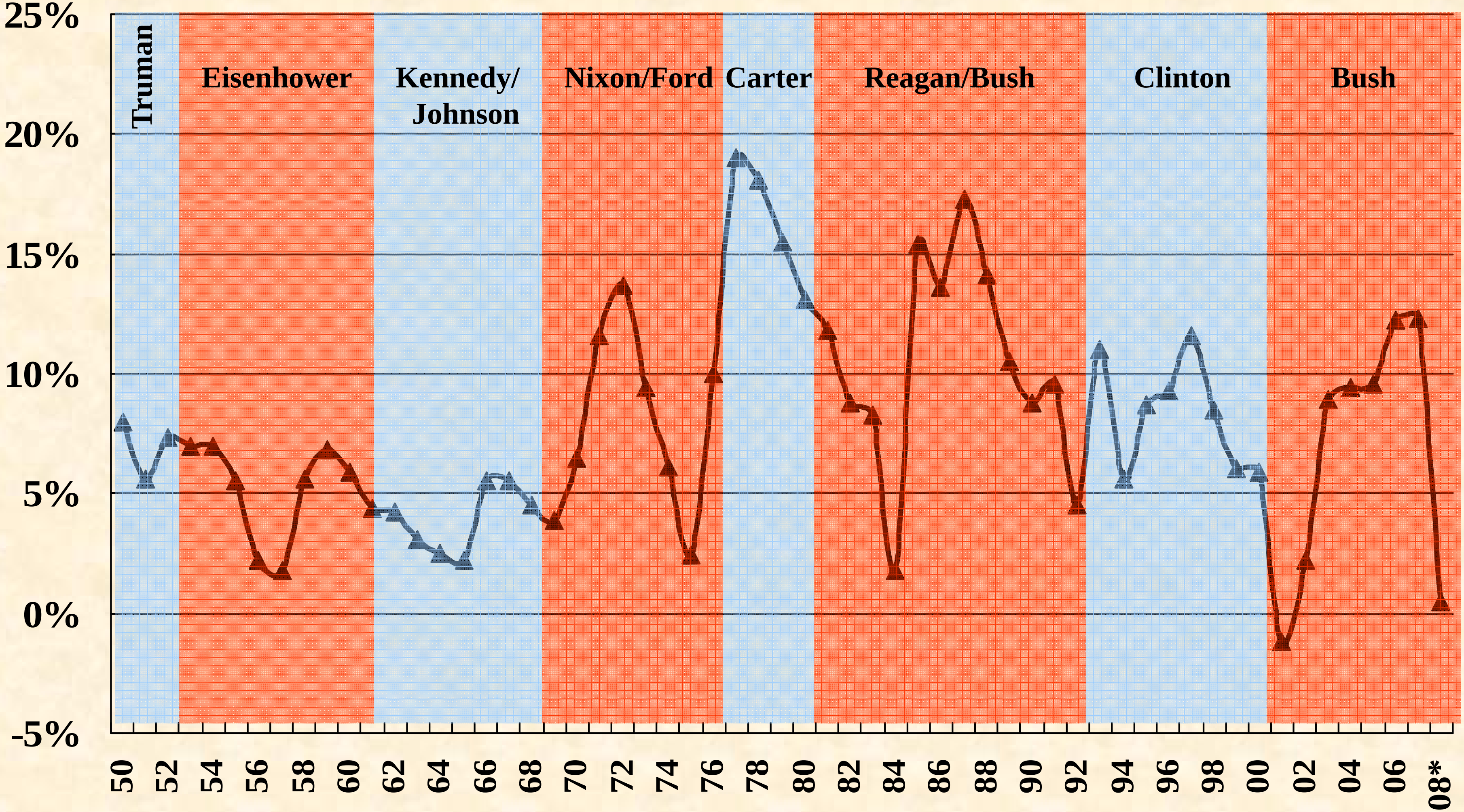
Party of President has marginal bearing on profitability of P/C insurance industry

*Truman administration ROE of 6.97% based on 3 years only, 1950-52.

Source: Insurance Information Institute

P/C Insurance Industry ROE by Presidential Party Affiliation, 1950–2008*

BLUE = Democratic President **RED** = Republican President

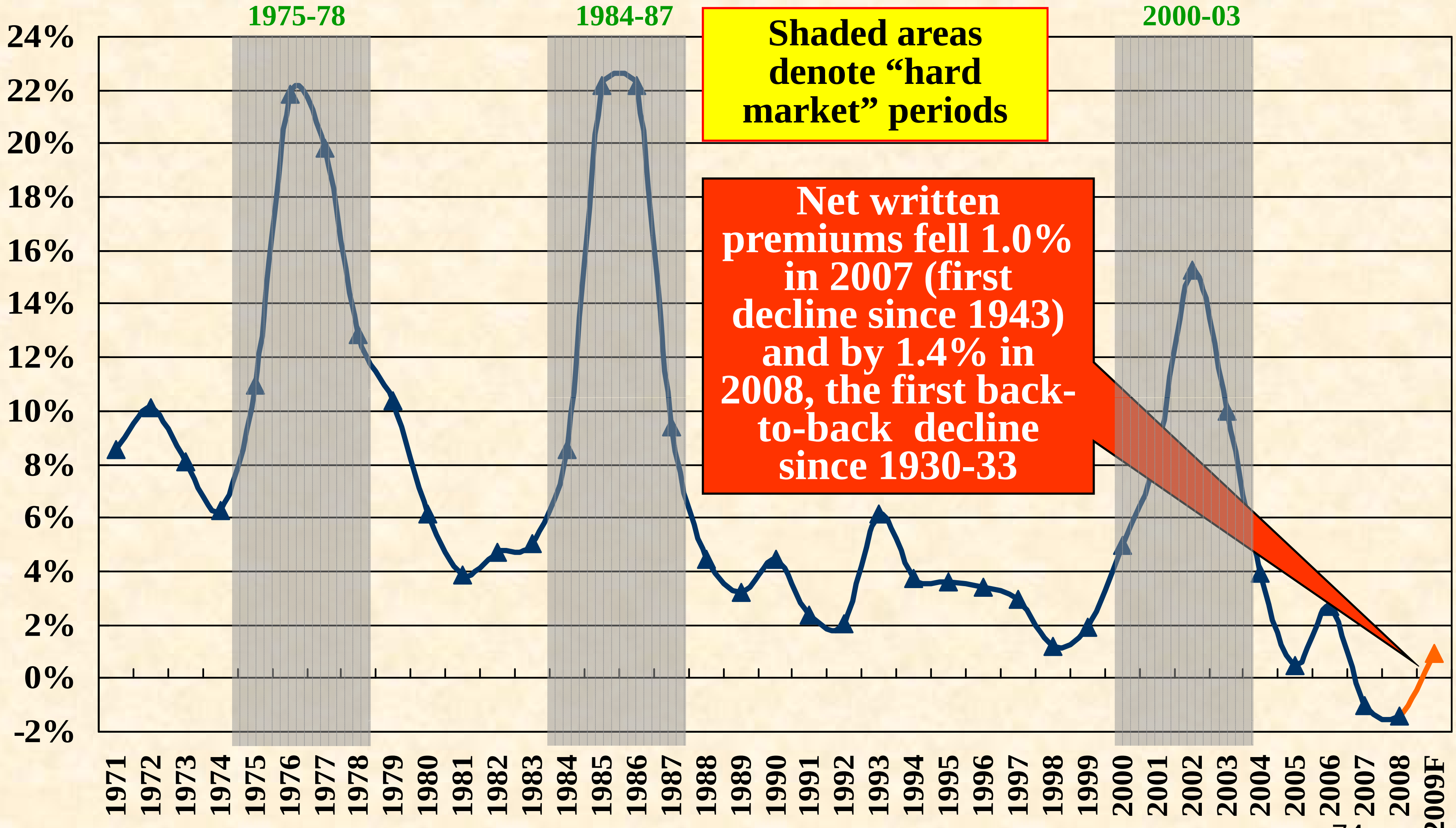


Source: Insurance Information Institute. *2008 based 9-month data.

P/C Premium Growth

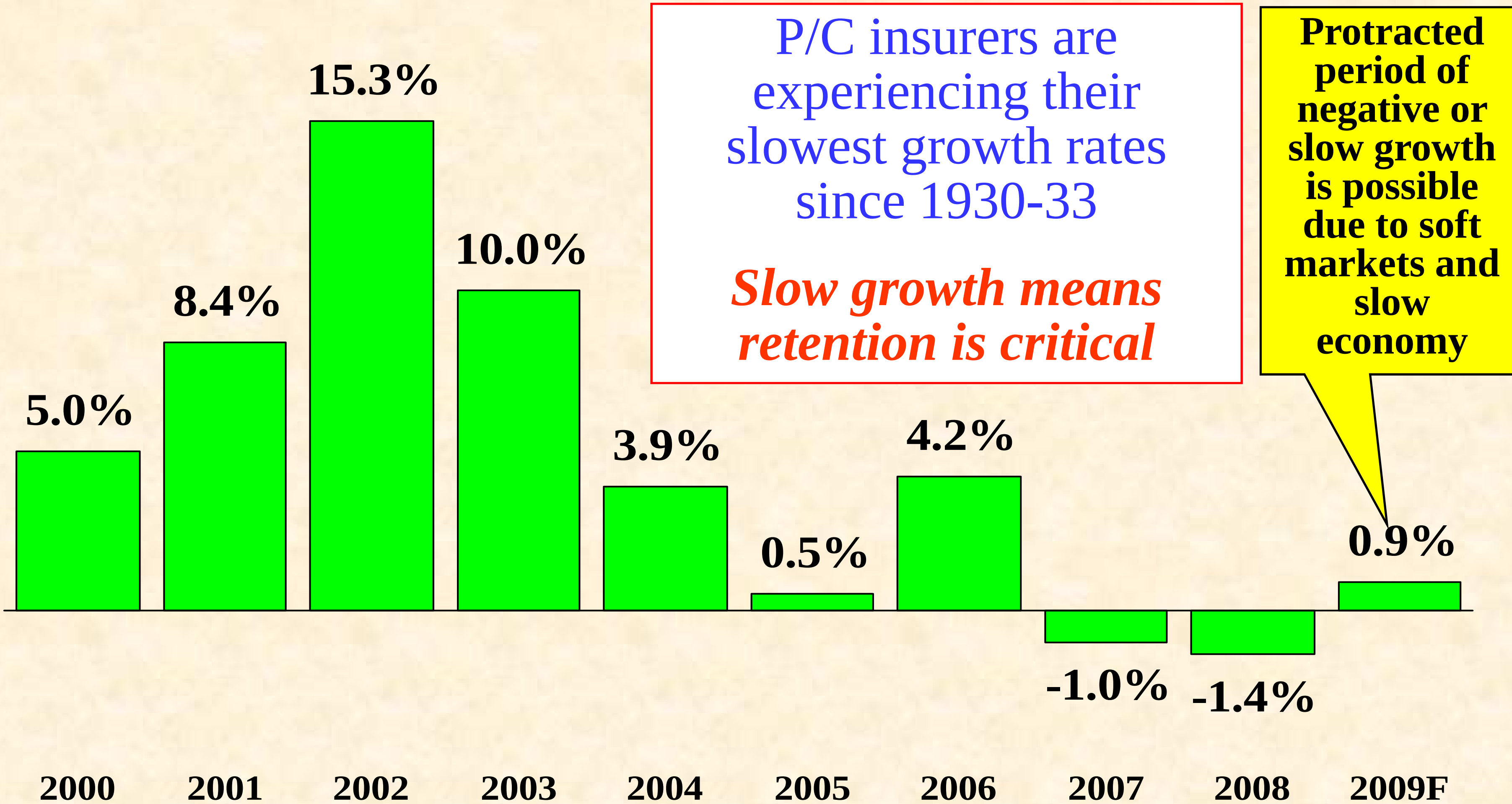
Primarily Driven by the Industry's Underwriting Cycle, Not the Economy

Strength of Recent Hard Markets by NWP Growth



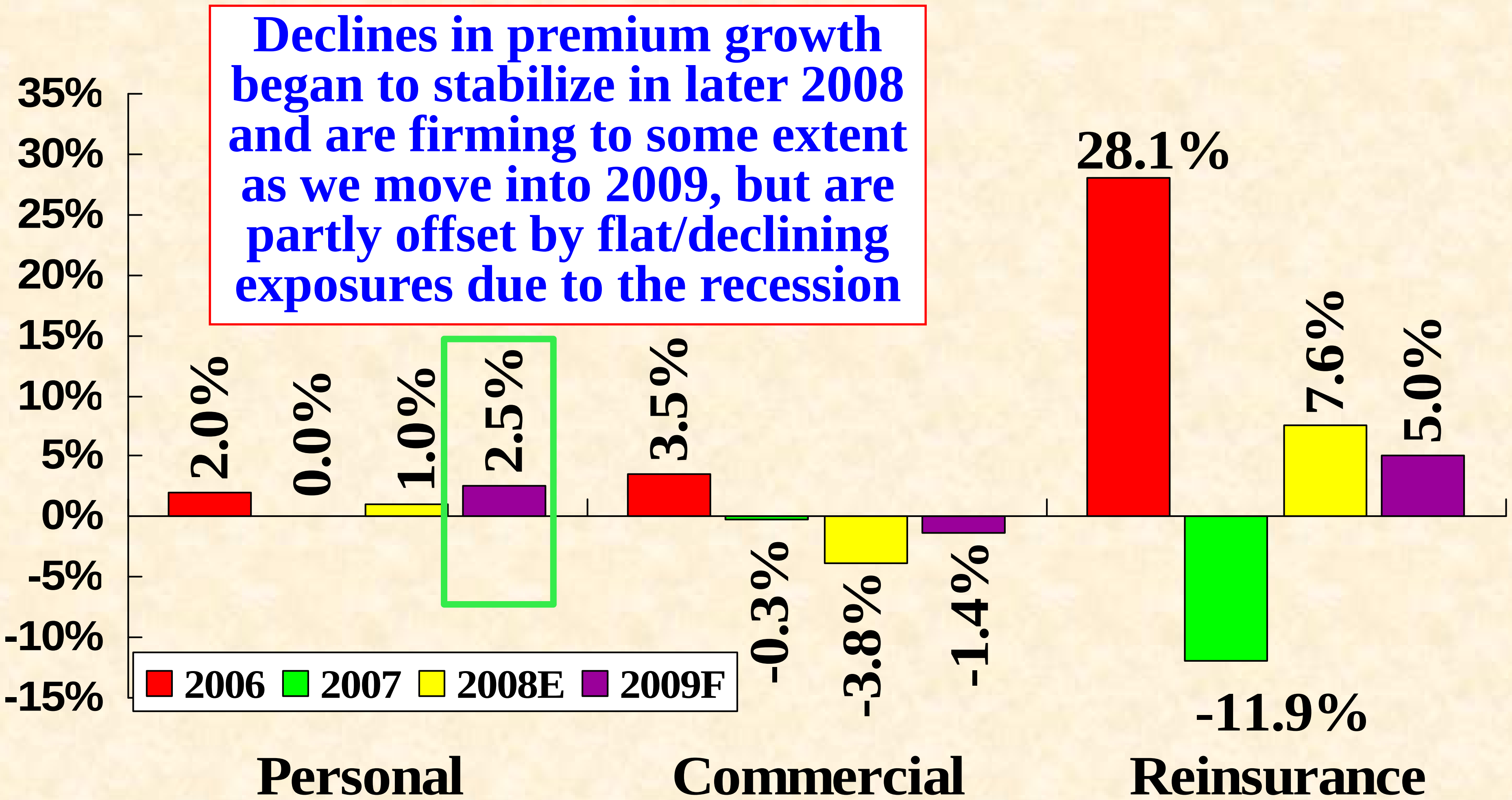
Sources: A.M. Best (historical and forecast), ISO, Insurance Information Institute

Year-to-Year Change in Net Written Premium, 2000-2009F*



*2008 figure is from ISO. Excluding Mortgage & Financial Guarantee insurers = -1.5%.
Source: A.M. Best (historical and forecast)

Personal/Commercial Lines & Reinsurance NPW Growth, 2006-2009F

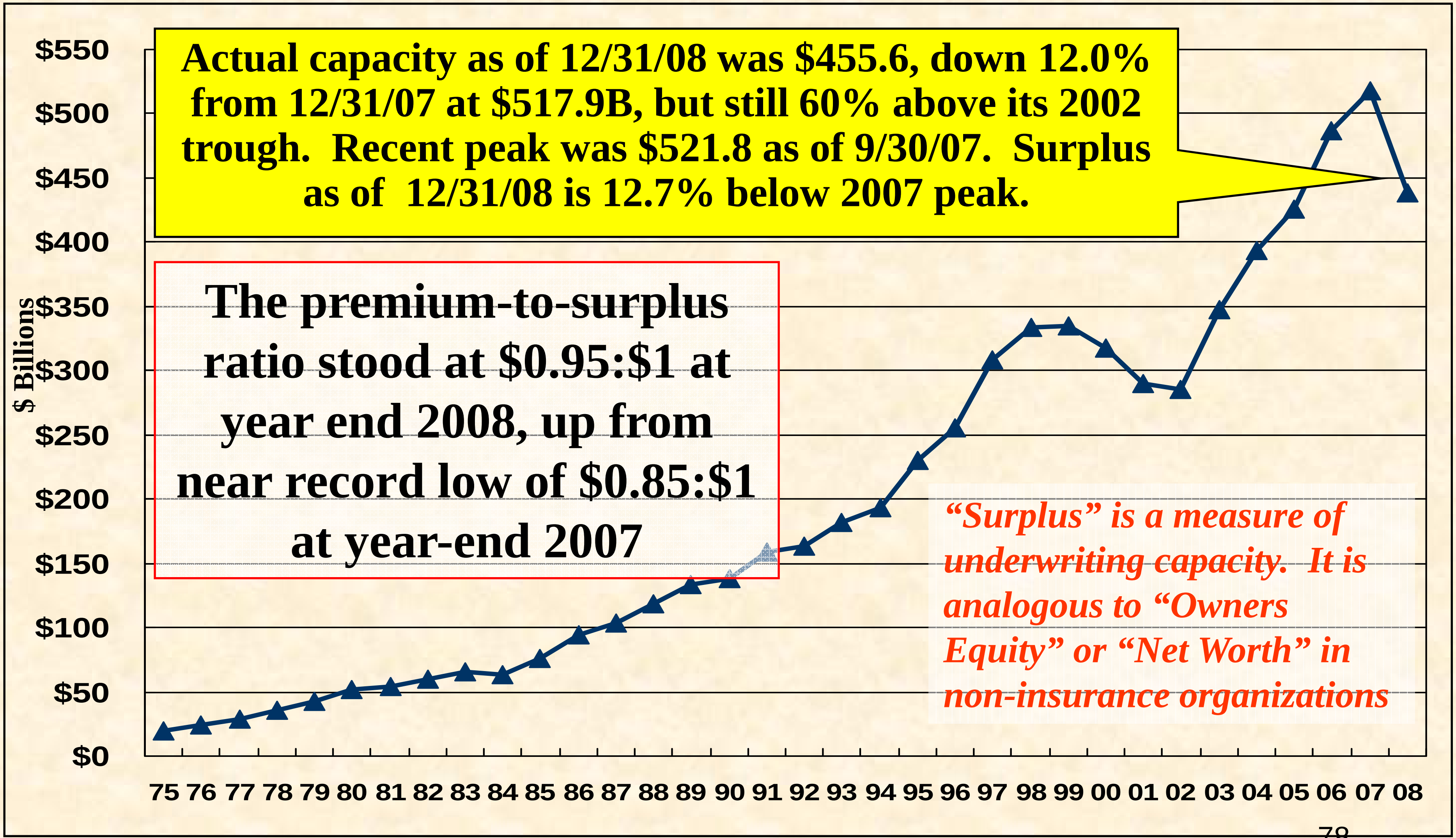


Sources: A.M. Best Review & Preview, Feb. 2009

Capital/ Policyholder Surplus

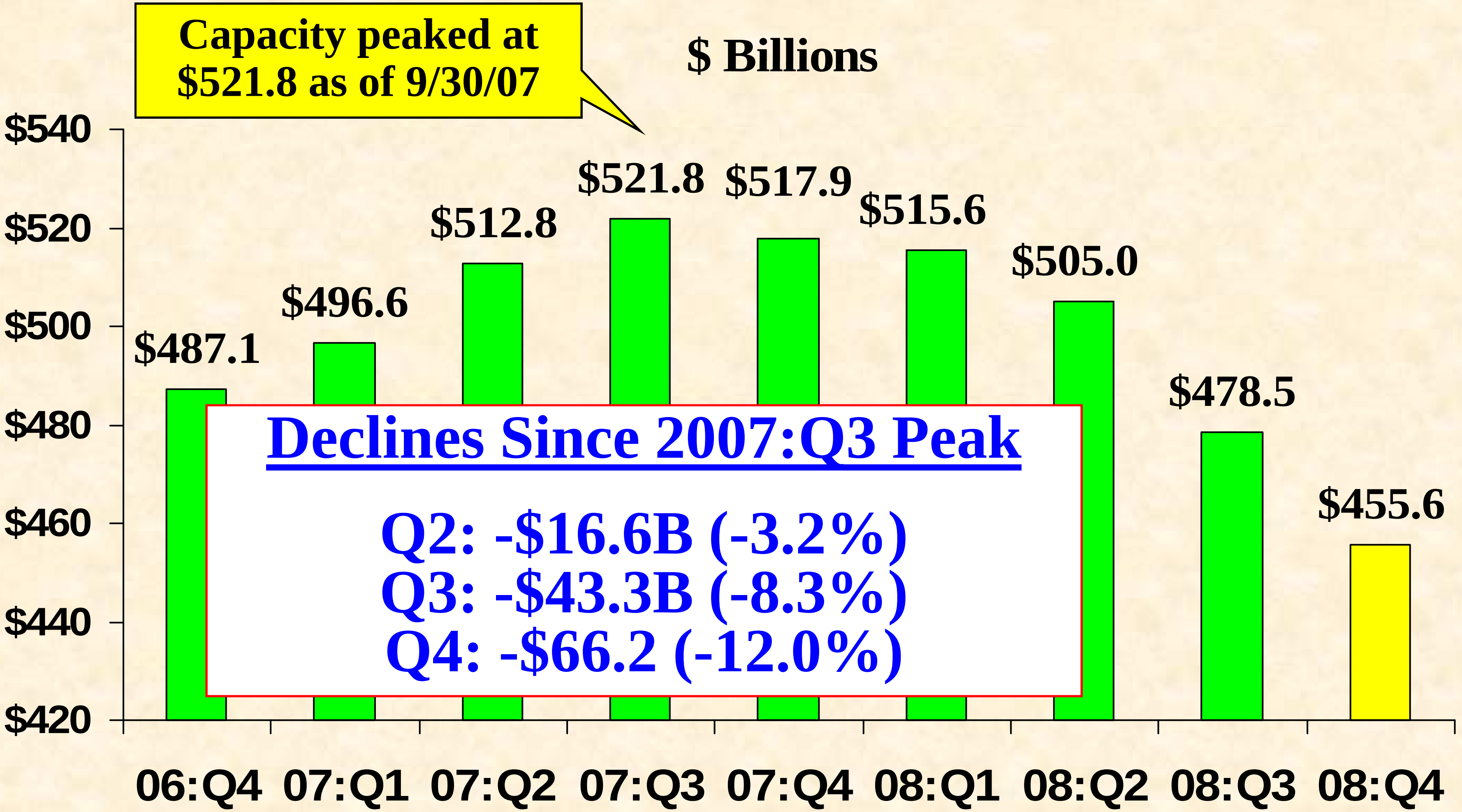
Shrinkage, but Capital is Within Historic Norms

U.S. Policyholder Surplus: 1975-2008*



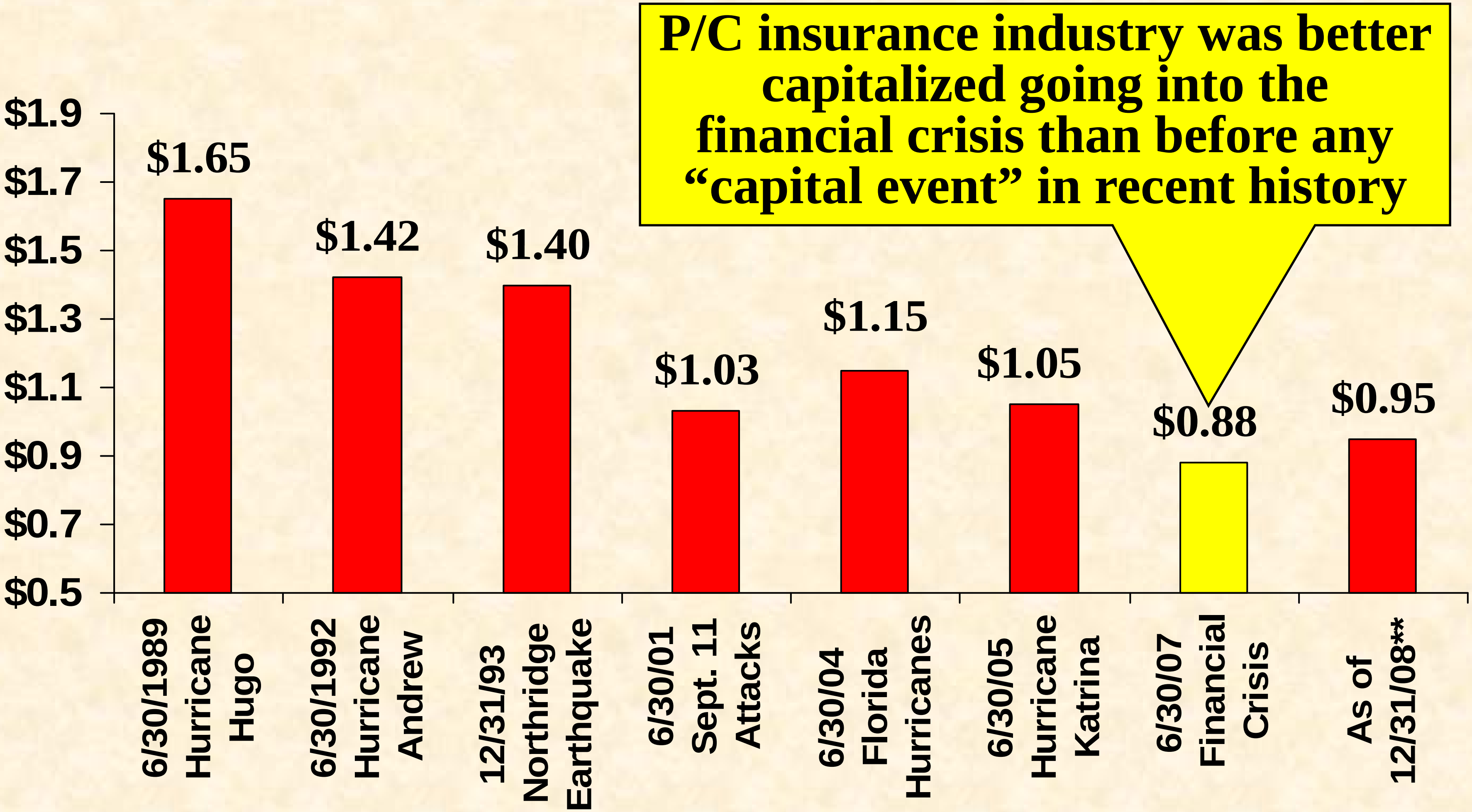
Source: A.M. Best, ISO, Insurance Information Institute. *As of 12/31/08

Policyholder Surplus, 2006:Q4 – 2008:Q4



Source: ISO.

Premium-to-Surplus Ratios Before Major Capital Events*

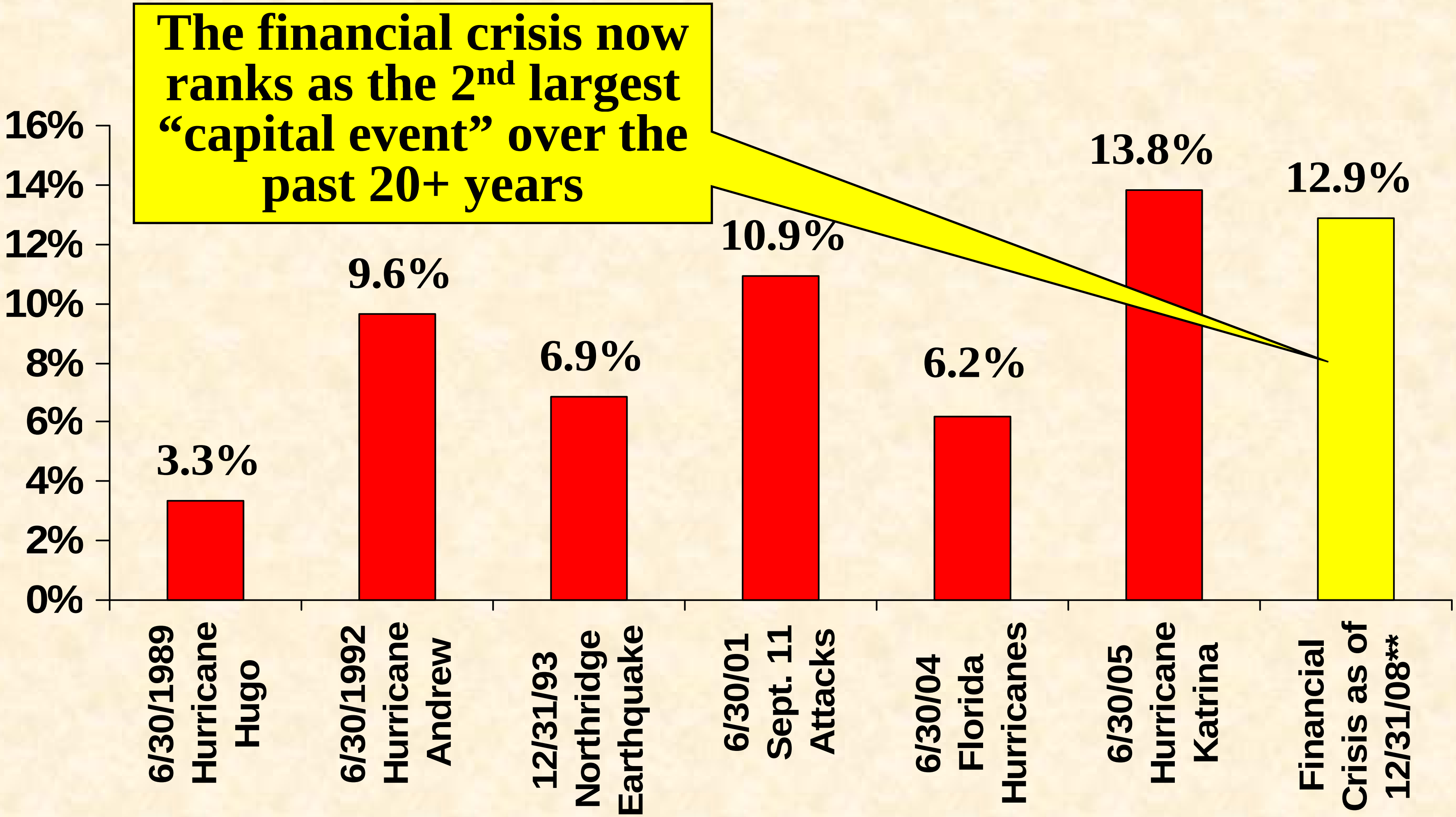


*Ratio is for end of quarter immediately prior to event. Date shown is end of quarter prior to event.

**Latest available

Source: PCS; Insurance Information Institute.

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

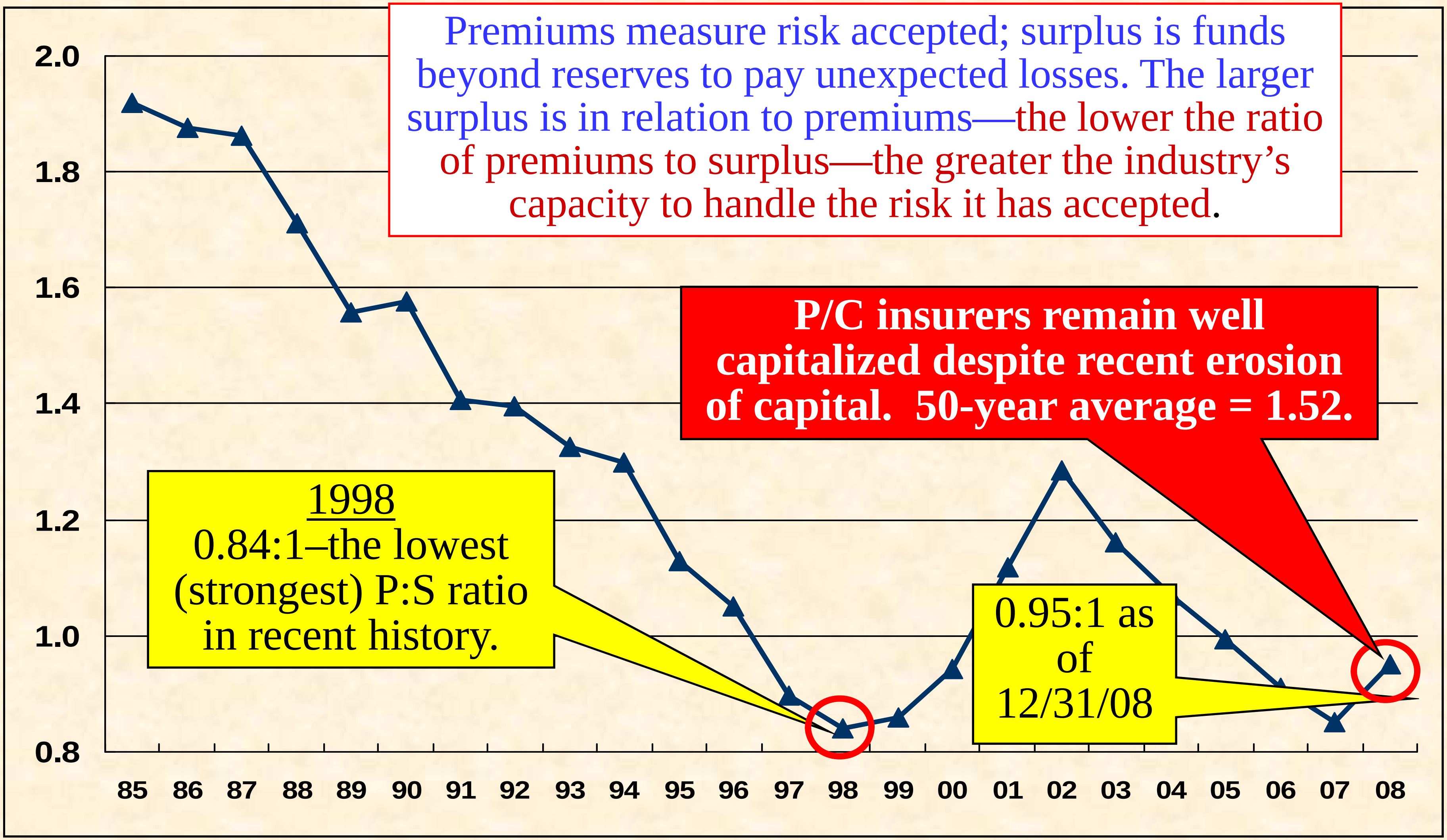


*Ratio is for end-of-quarter surplus immediately prior to event. Date shown is end of quarter prior to event.

**Latest available

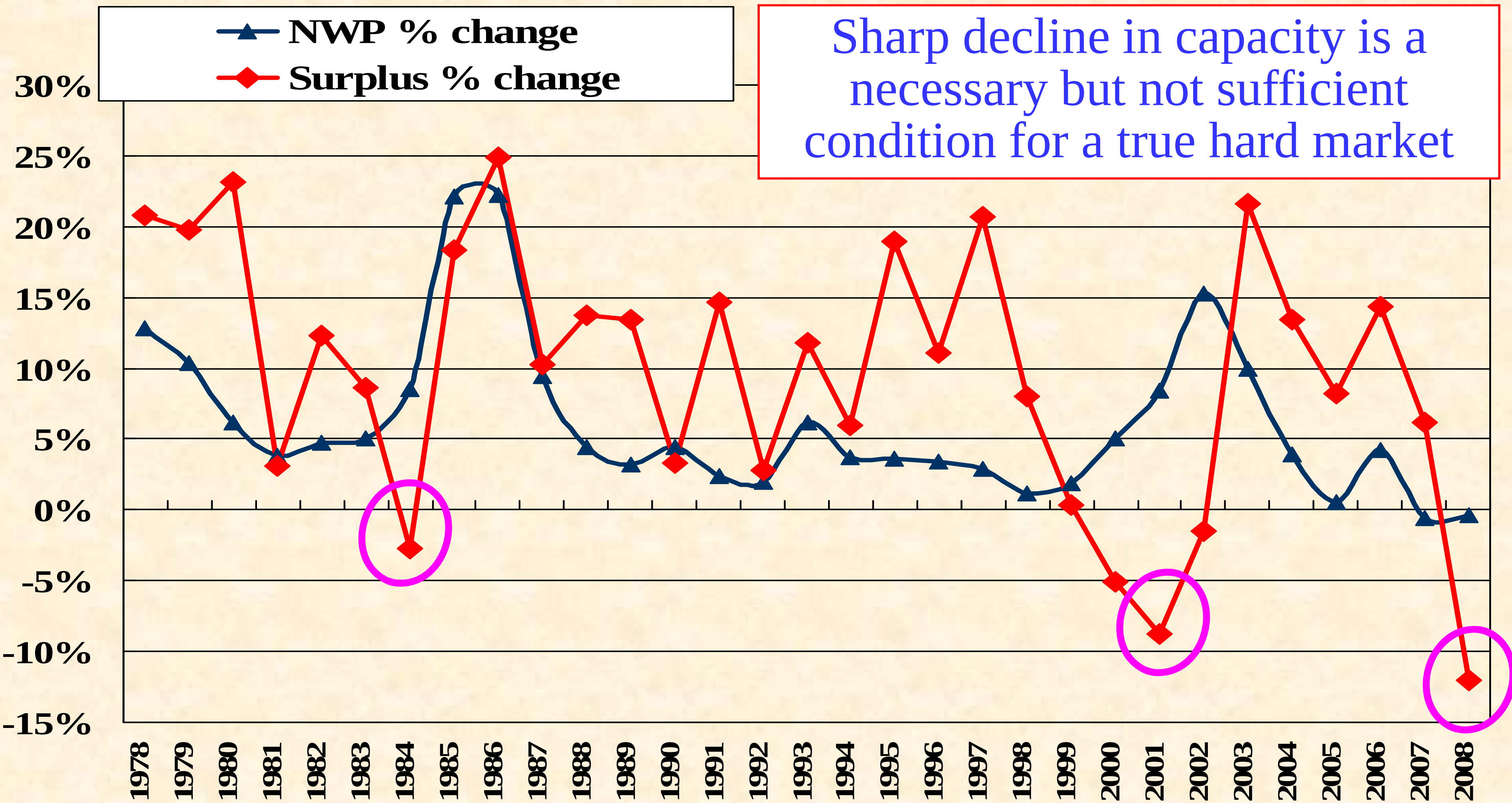
Source: PCS; Insurance Information Institute.

U.S. P/C Industry Premiums-to-Surplus Ratio: 1985-2008



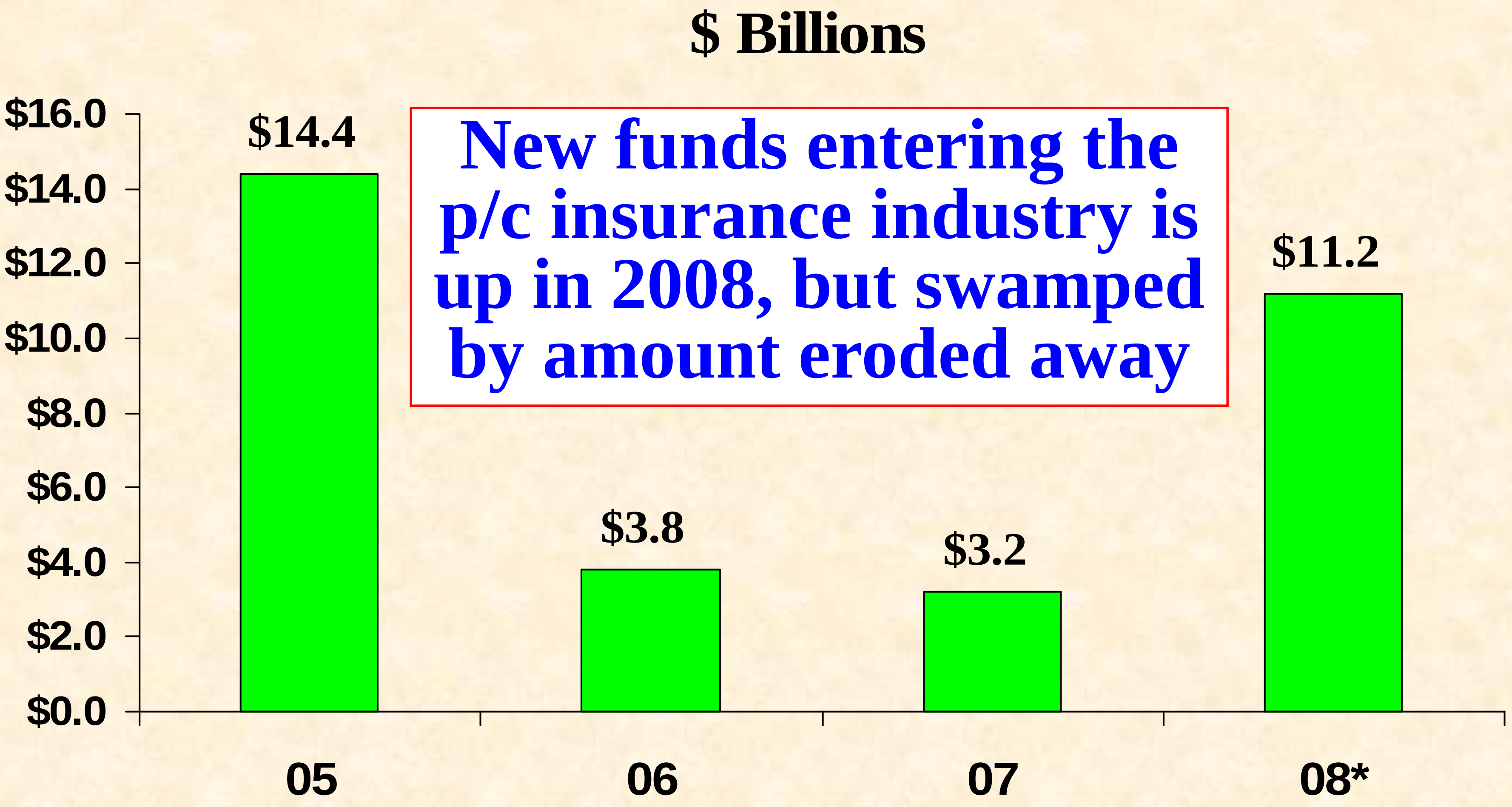
Sources: A.M. Best, ISO, Insurance Information Institute.

Historically, Hard Markets Follow When Surplus "Growth" is Negative



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

New Funds Contributing to US Policyholder Surplus, 2005-2008



*Through Q4 2009 (latest available).

Source: ISO; Insurance Information Institute

Investment Performance

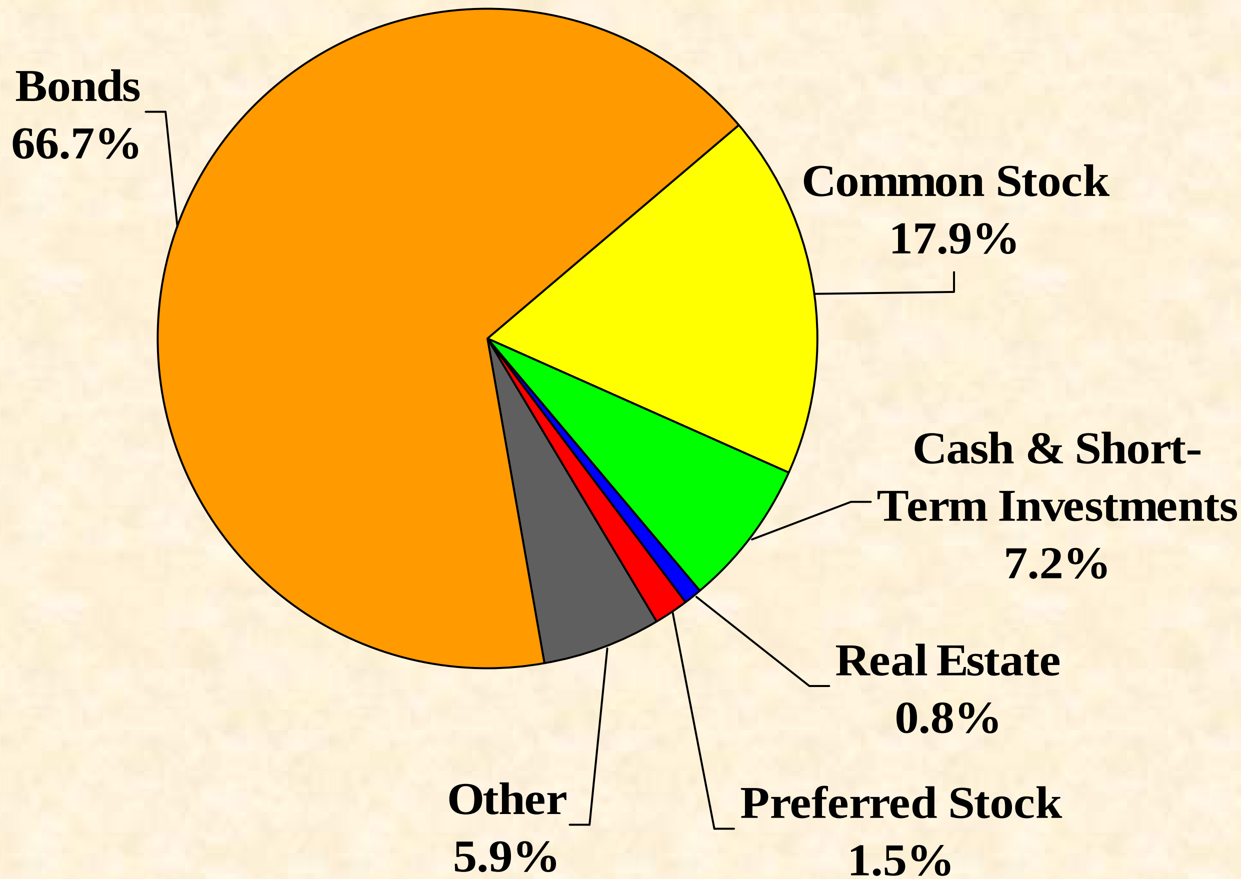
Investments are the Principle Source of Declining Profitability

Distribution of P/C Insurance Industry's Investment Portfolio

As of December 31, 2007

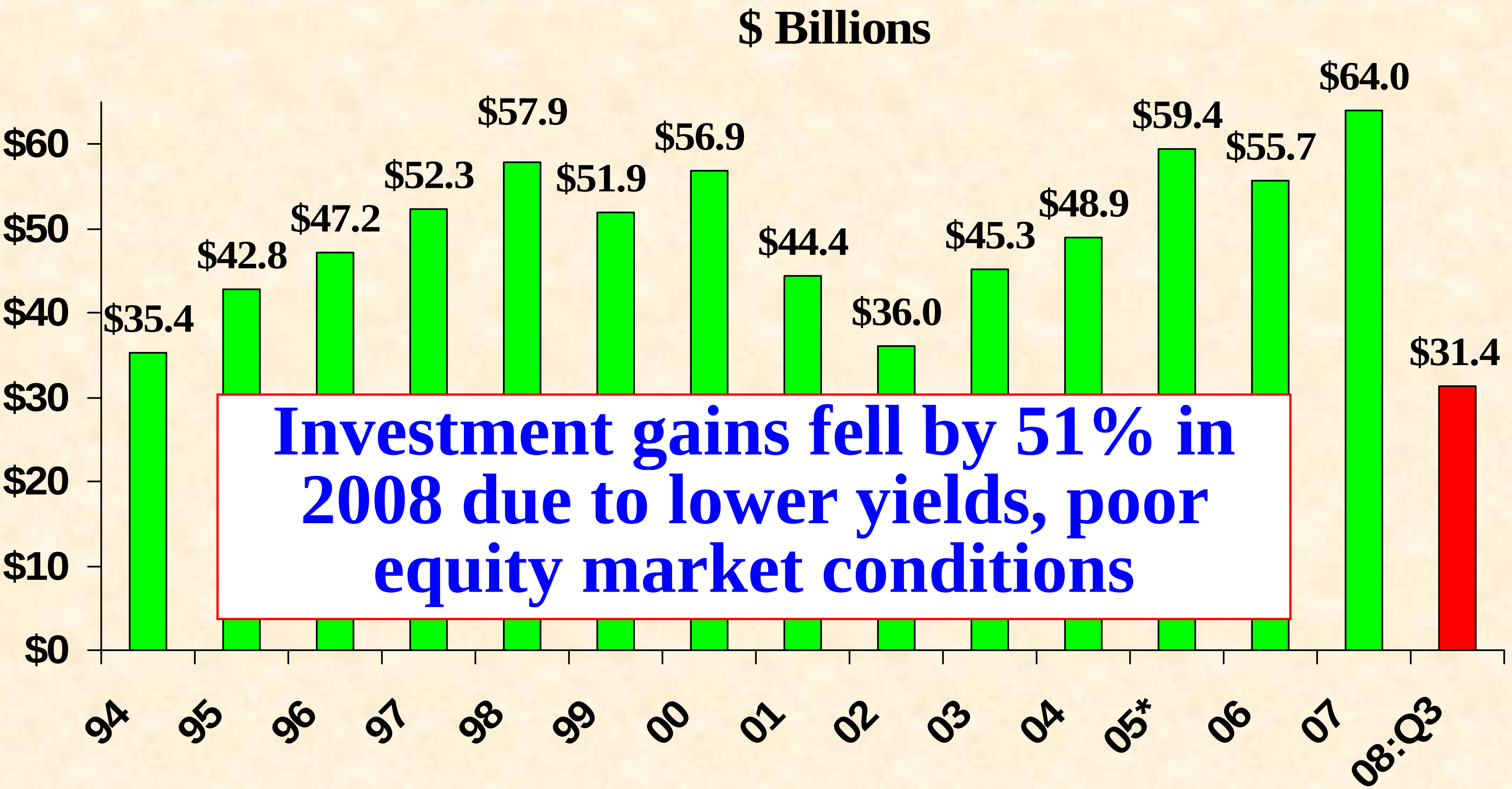
Portfolio Facts

- Invested assets totaled $1.3 trillion as of 12/31/07
- Insurers are generally conservatively invested, with 2/3 of assets invested in bonds as of 12/31/07
- Only about 18% of assets were invested in common stock as of 12/31/07
- Even the most conservative of portfolios was hit hard in 2008



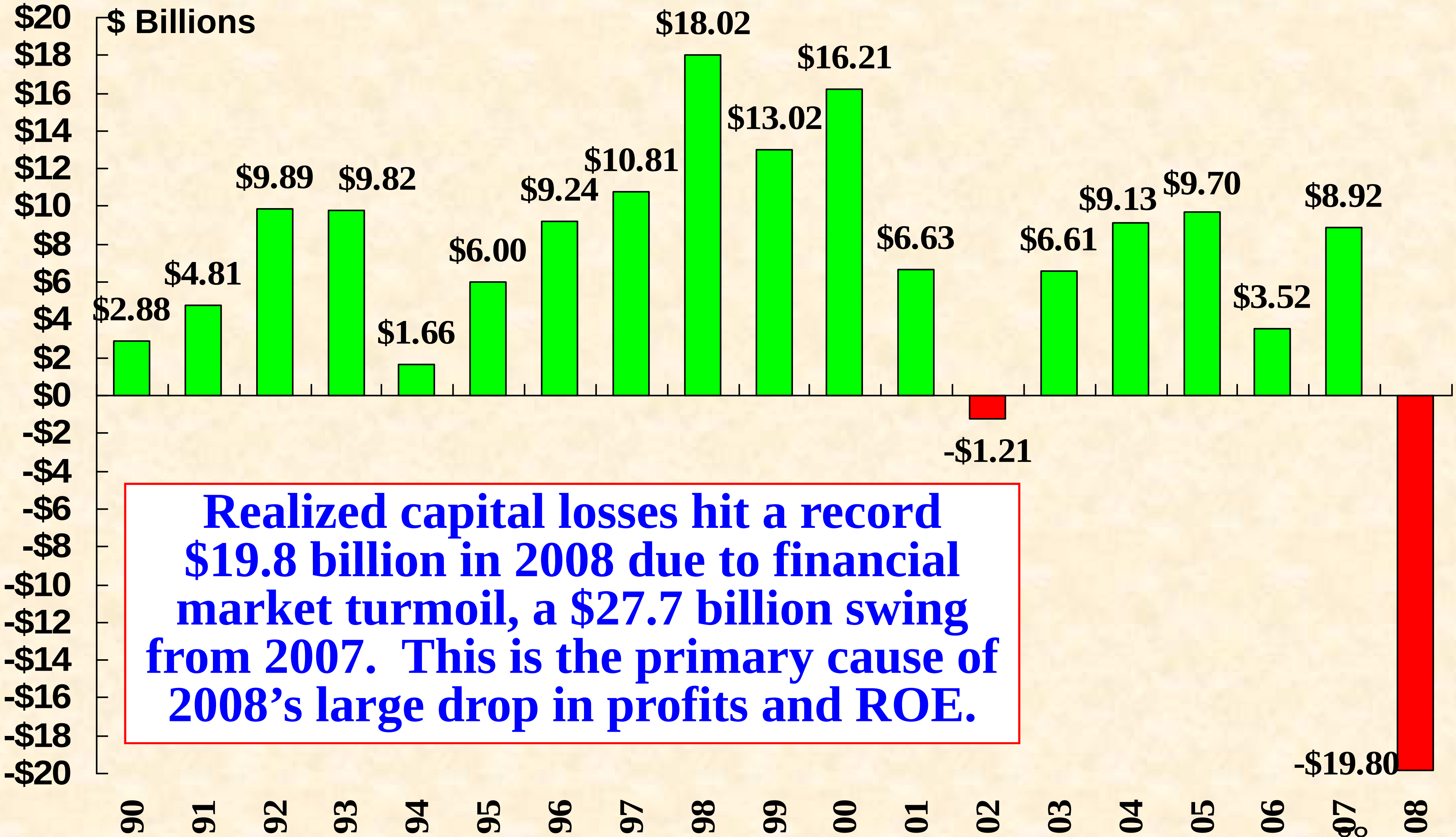
Source: NAIC; Insurance Information Institute research;.

Property/Casualty Insurance Industry Investment Gain:1994- 2008[1]



[1]Investment gains consist primarily of interest, stock dividends and realized capital gains and losses.
2006 figure consists of $52.3B net investment income and $3.4B realized investment gain.
*2005 figure includes special one-time dividend of $3.2B.
Sources: ISO; Insurance Information Institute.

P/C Insurer Net Realized Capital Gains, 1990-2008



Realized capital losses hit a record $19.8 billion in 2008 due to financial market turmoil, a $27.7 billion swing from 2007. This is the primary cause of 2008's large drop in profits and ROE.

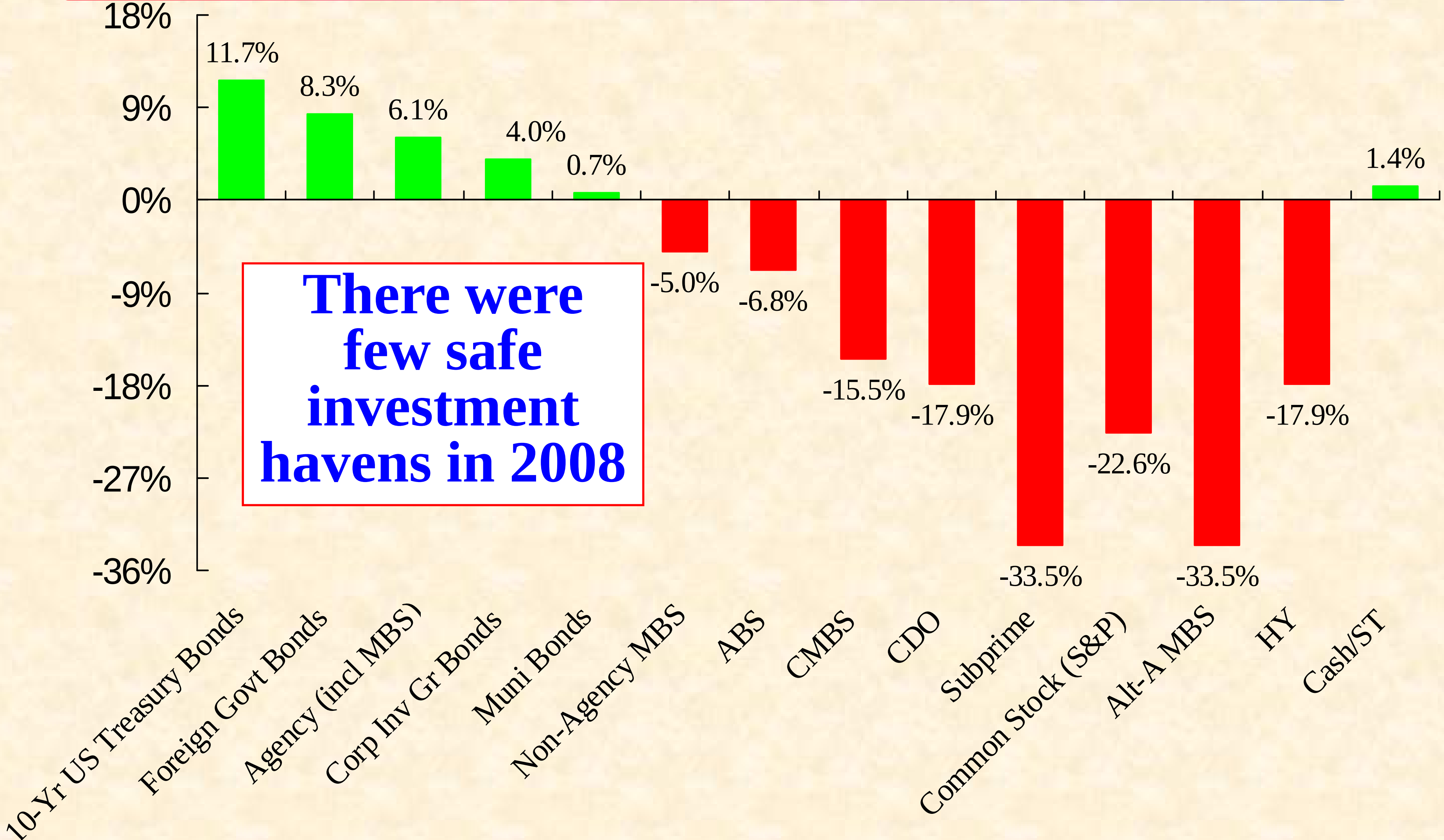
Sources: A.M. Best, ISO, Insurance Information Institute.

Total Returns for Large Company Stocks: 1970-2009*

S&P 500 is down 3.7% in 2009*

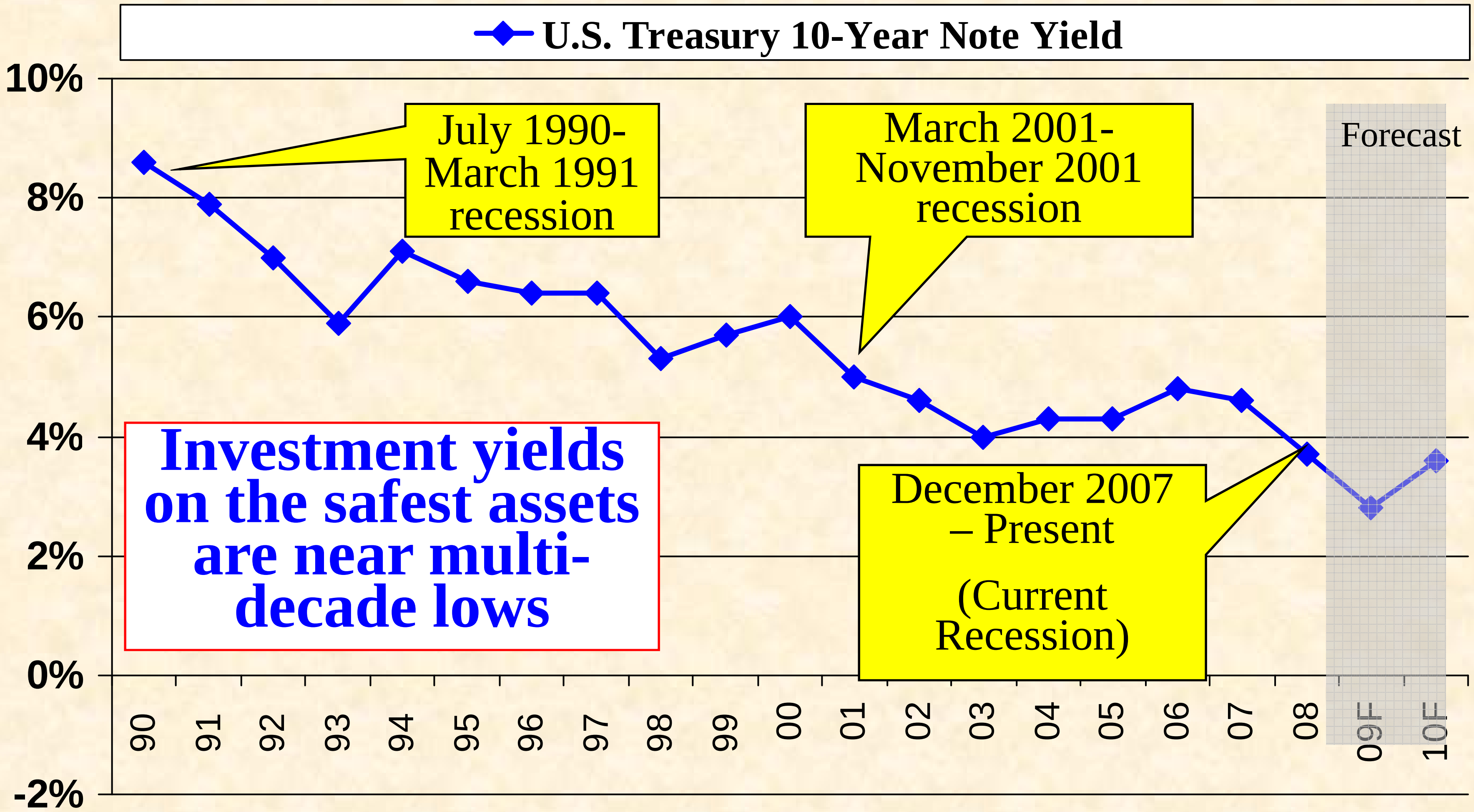
Source: Ibbotson Associates, Insurance Information Institute. *Through April 17, 2009.

Asset Class Investment Benchmarks, 4Q:2008



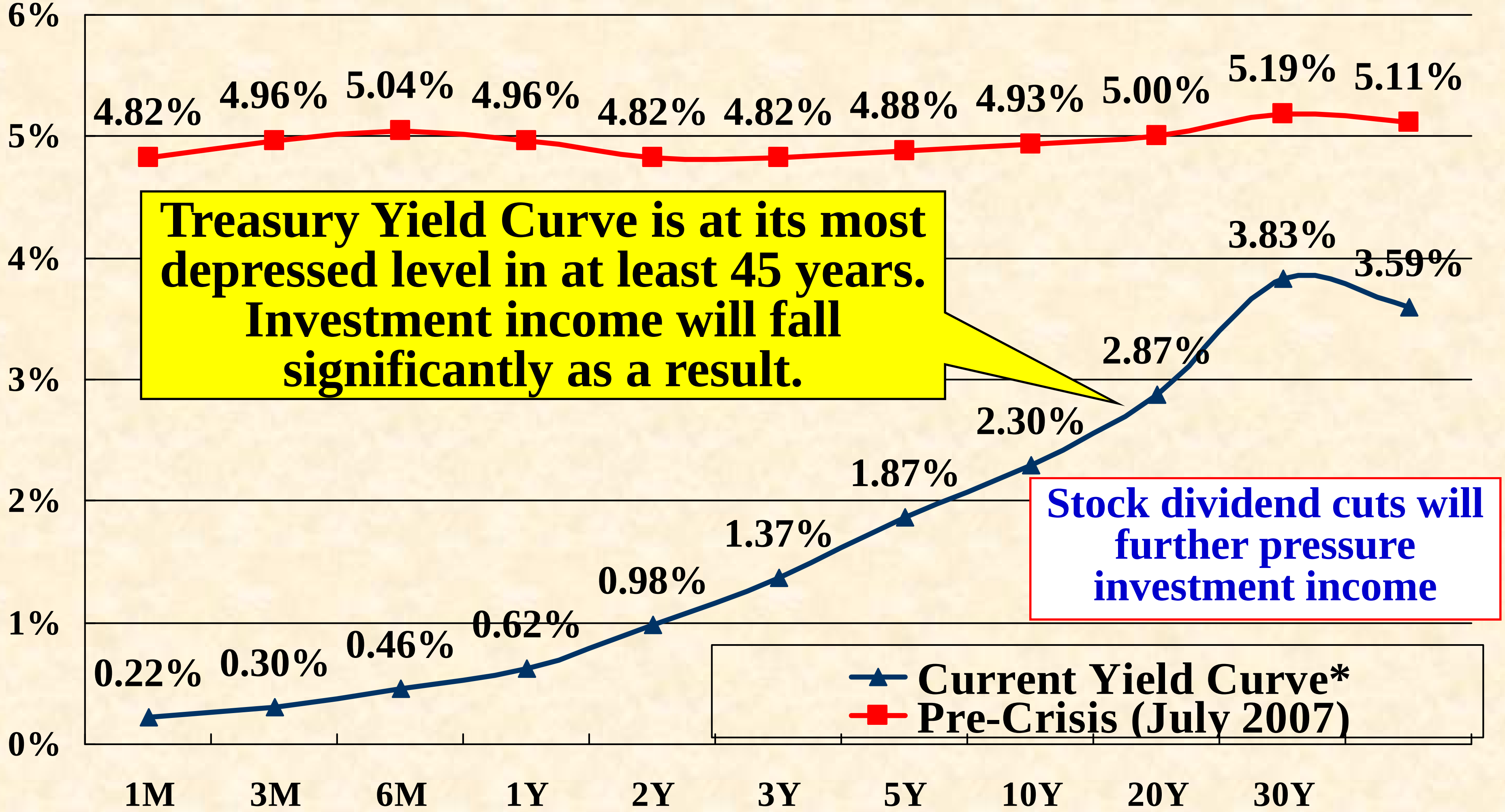
Source: Jay Gelb, P&C Insurance 2009/10 Outlook, Barclays Capital Research, January 6, 2009, Appendix B

Treasury Bond Yields Have Generally Been Falling



Sources: US Bureau of Labor Statistics (history); Blue Chip Economic Indicators, February 2009 issue (forecasts)

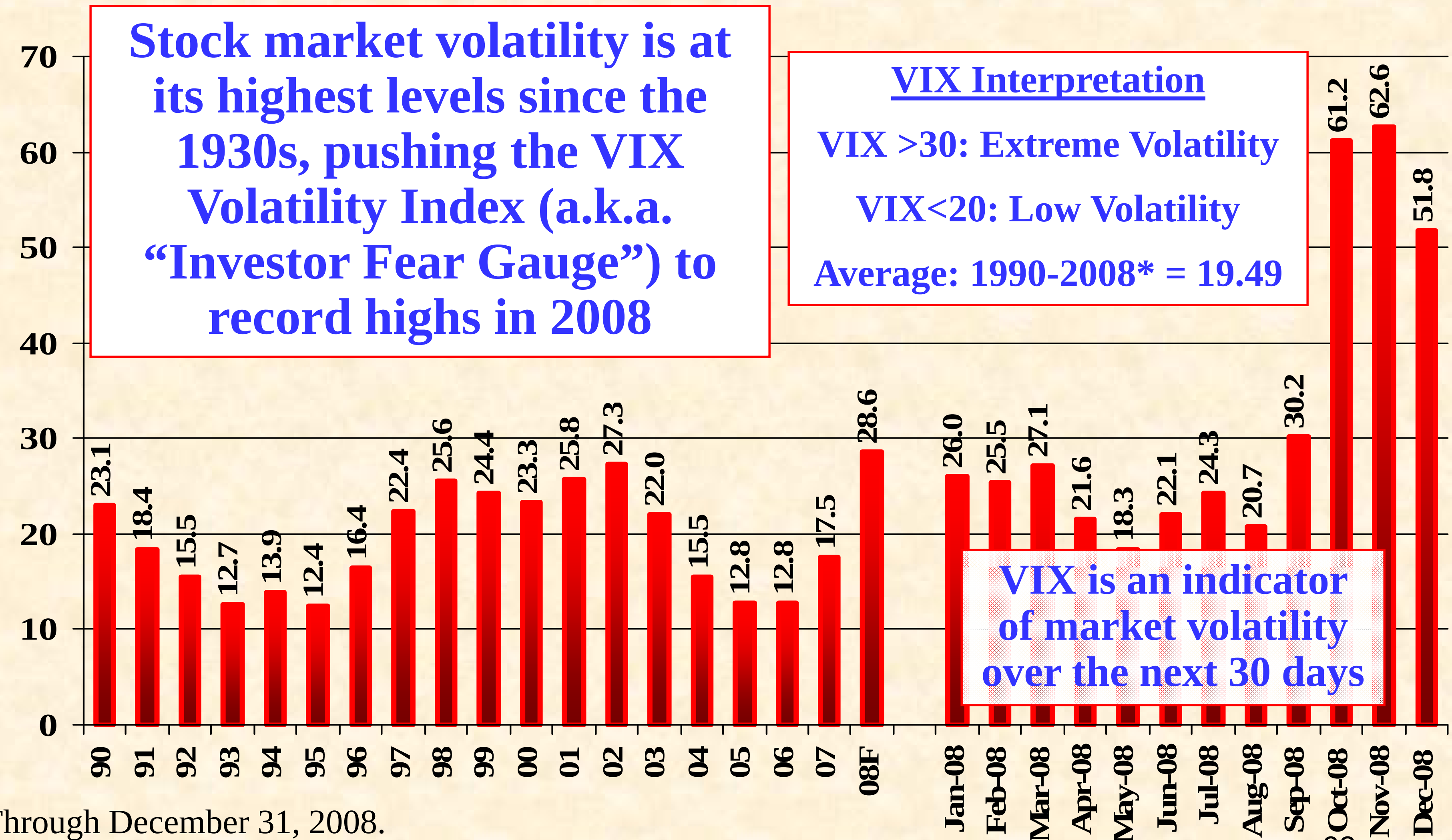
Treasury Yield Curves: Pre-Crisis vs. Current*



***February 2009.**

Sources: Federal Reserve; Insurance Information Institute.

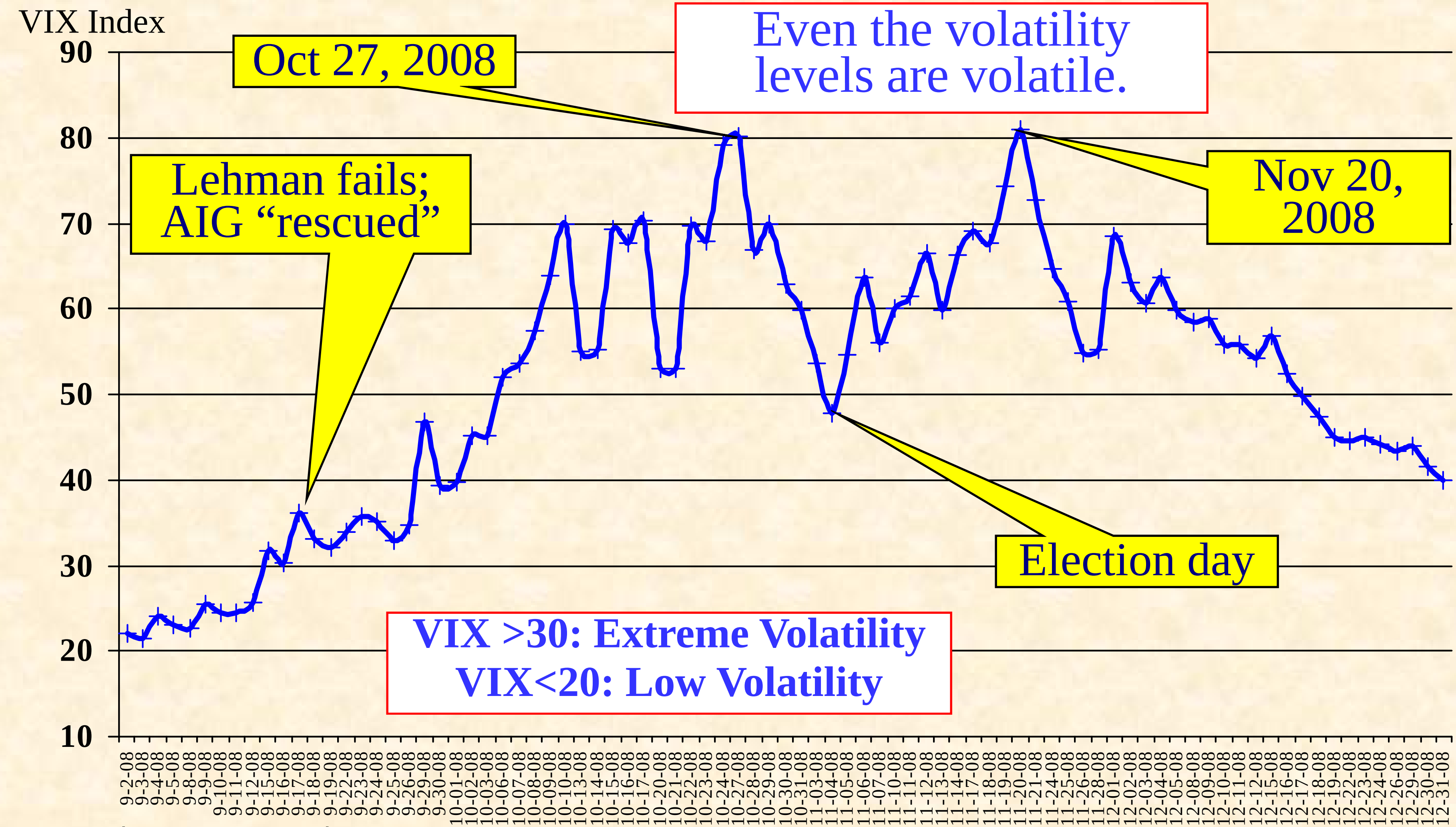
VIX Volatility Index: Stock Market Volatility at Record Highs in 2008*



*Through December 31, 2008.

Sources: Chicago Board Options Exchange: http://www.cboe.com/micro/vix/historical.aspx

Stock Market Daily Volatility in 2008: Heading to “Normal”?*



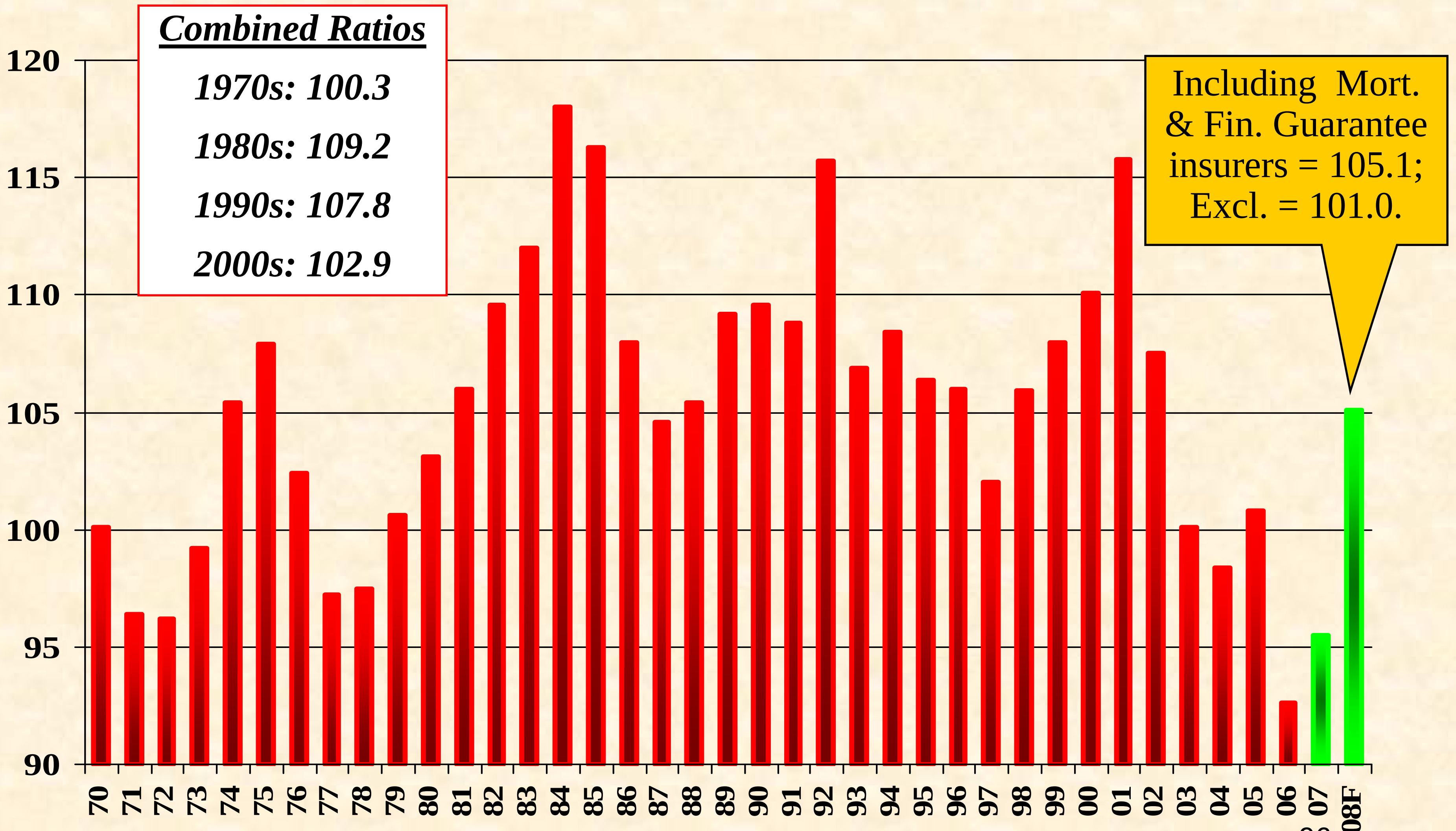
*September 2 to December 31, 2008.

Source: Chicago Board Options Exchange: http://www.cboe.com/micro/vix/historical.aspx

Underwriting Trends

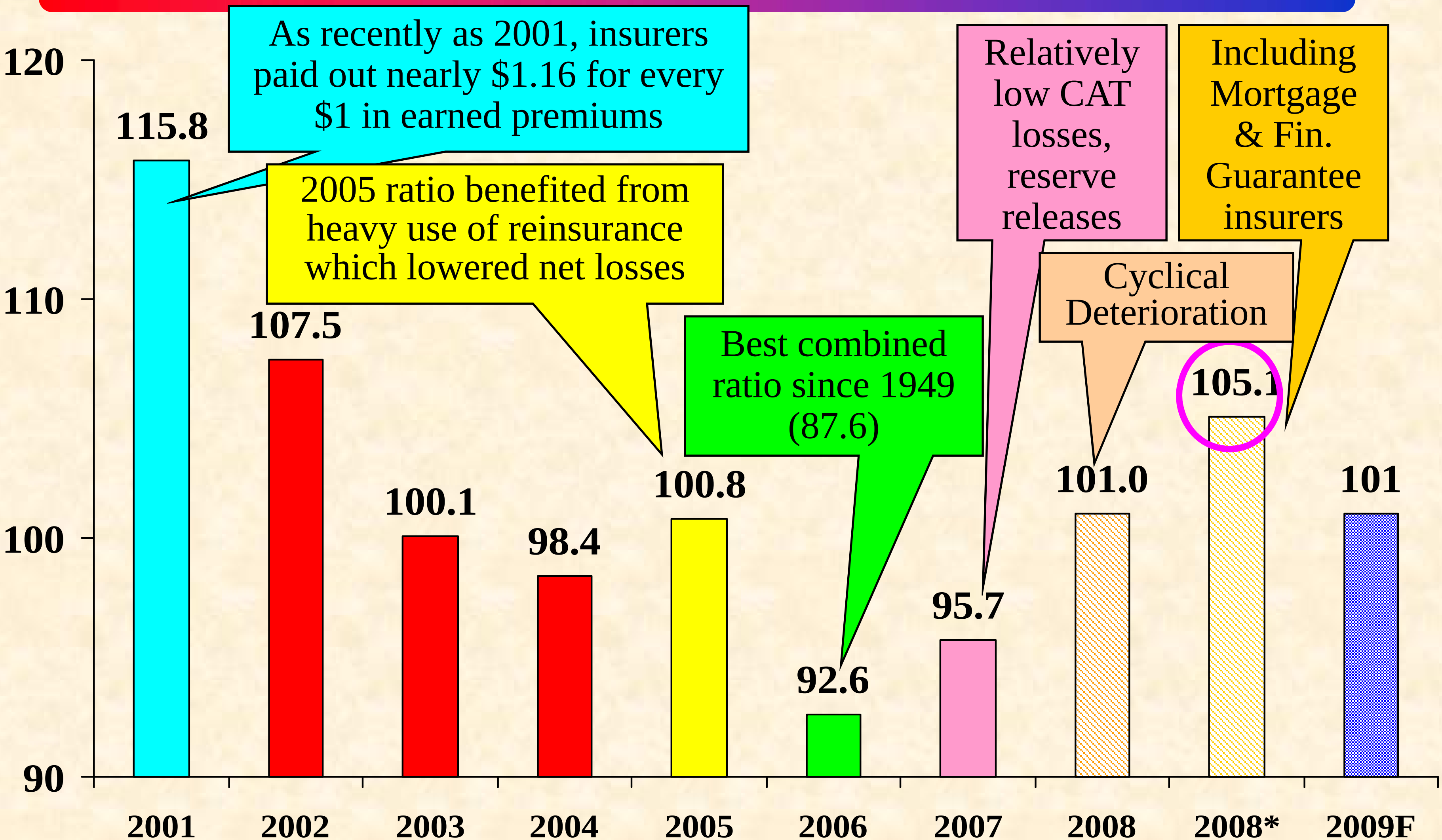
Financial Crisis Does *Not* Directly Impact Underwriting Performance: Cycle, Catastrophes Were 2008's Drivers

P/C Insurance Combined Ratio, 1970-2008F*



Sources: A.M. Best; ISO, III *Excluding mortgage & financial guarantee insurers in 2008 = 101.0.

P/C Insurance Industry Combined Ratio, 2001-2009E

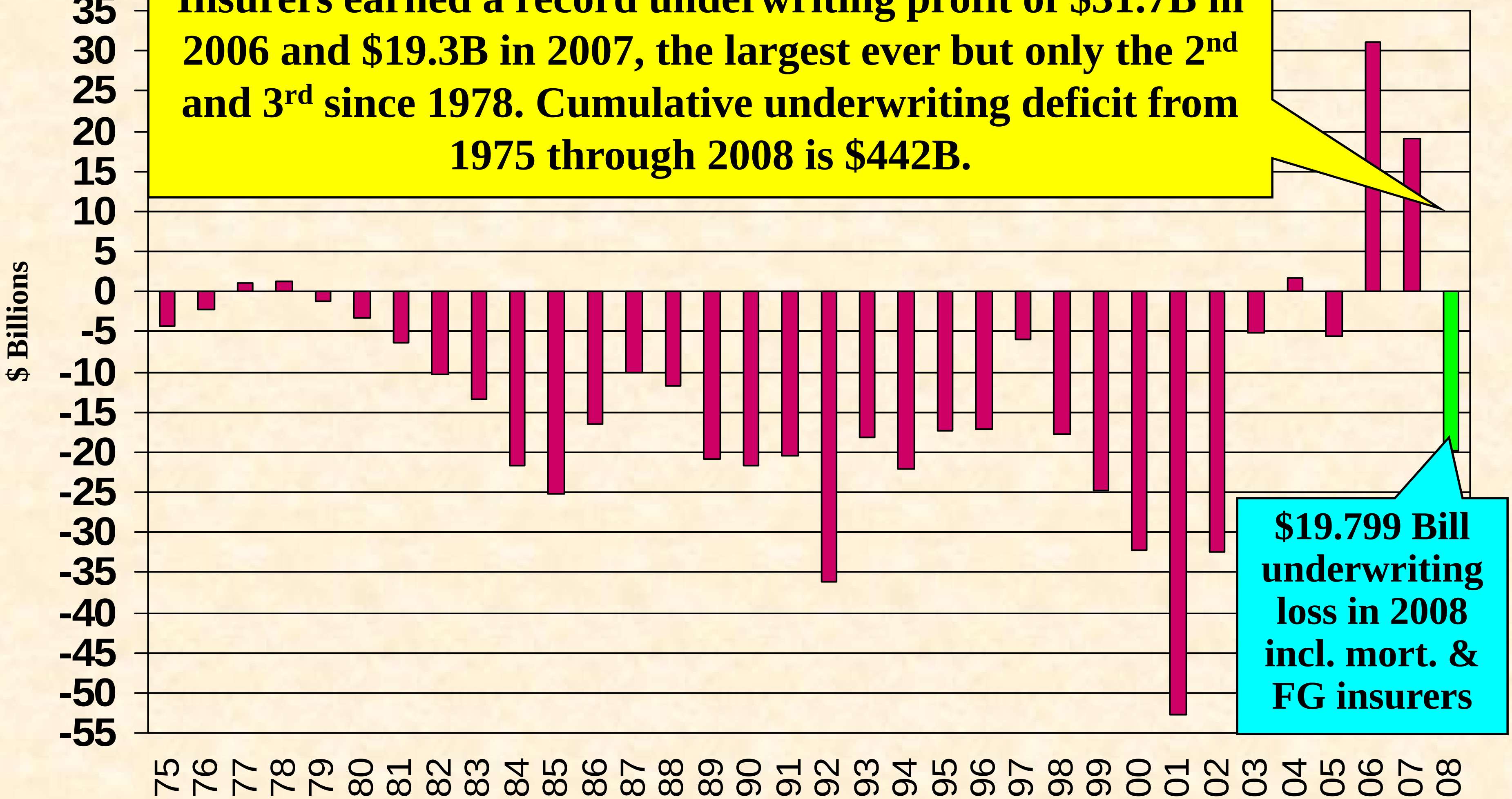


*Includes Mortgage & Financial Guarantee insurers.

Sources: A.M. Best.

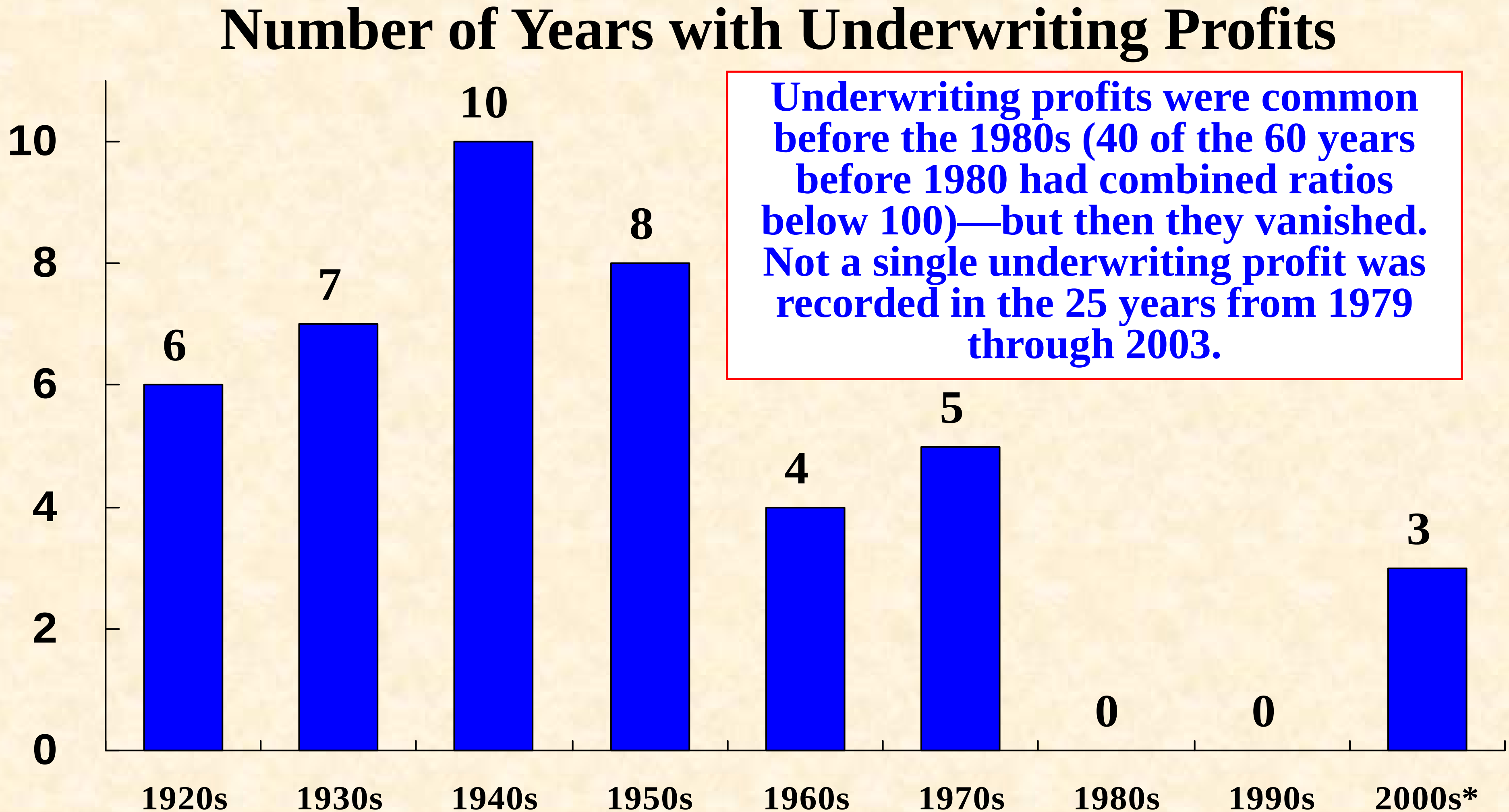
*Underwriting Gain (Loss) 1975-2008**

Insurers earned a record underwriting profit of $31.7B in 2006 and $19.3B in 2007, the largest ever but only the 2nd and 3rd since 1978. Cumulative underwriting deficit from 1975 through 2008 is $442B.



Source: A.M. Best, ISO; Insurance Information Institute * Includes mortgage & finl. guarantee insurers

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



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

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

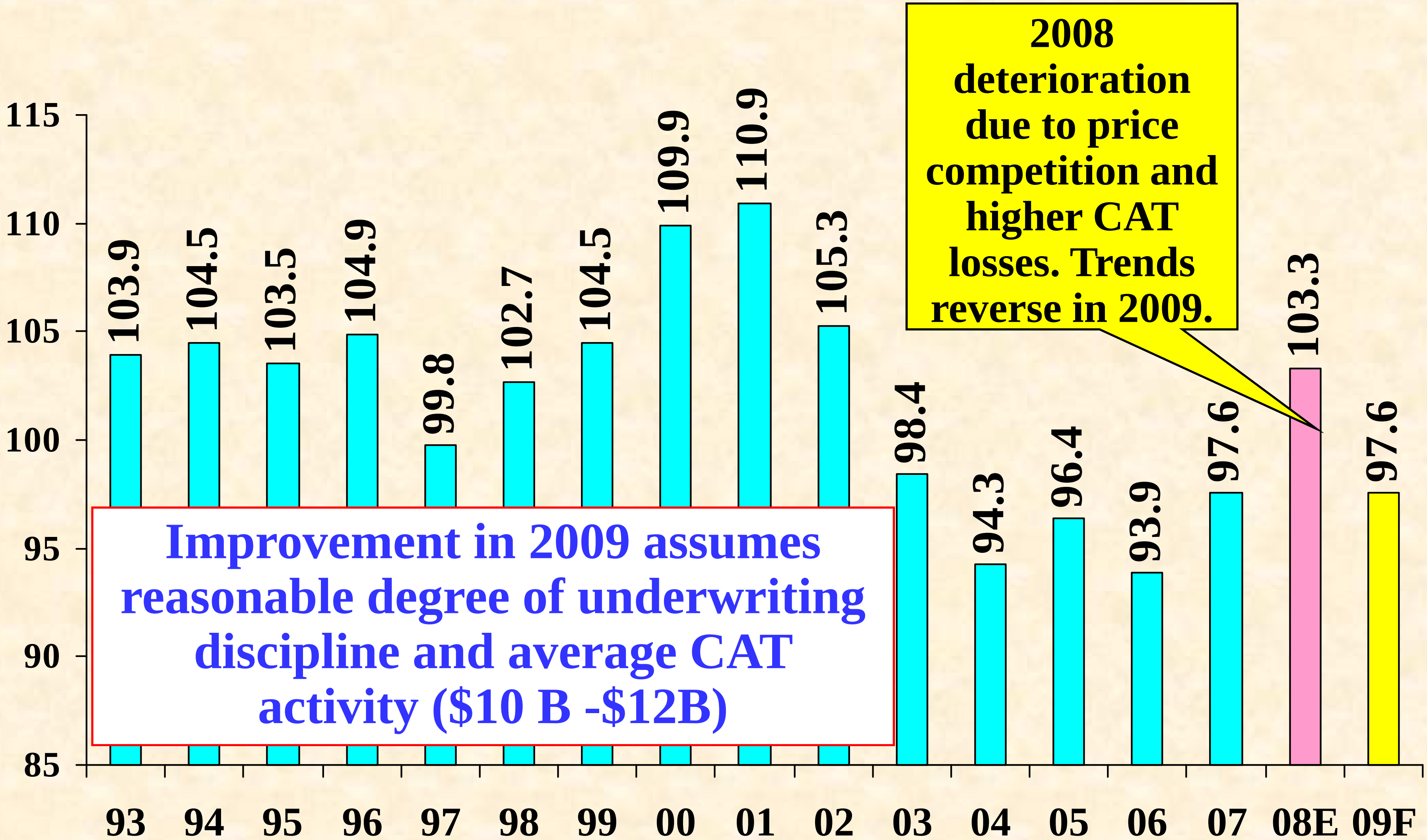
*2000 through 2008.

Personal Lines

Auto (~75% of Market)

Home (~25%)

Personal Lines Combined Ratio, 1993-2009F

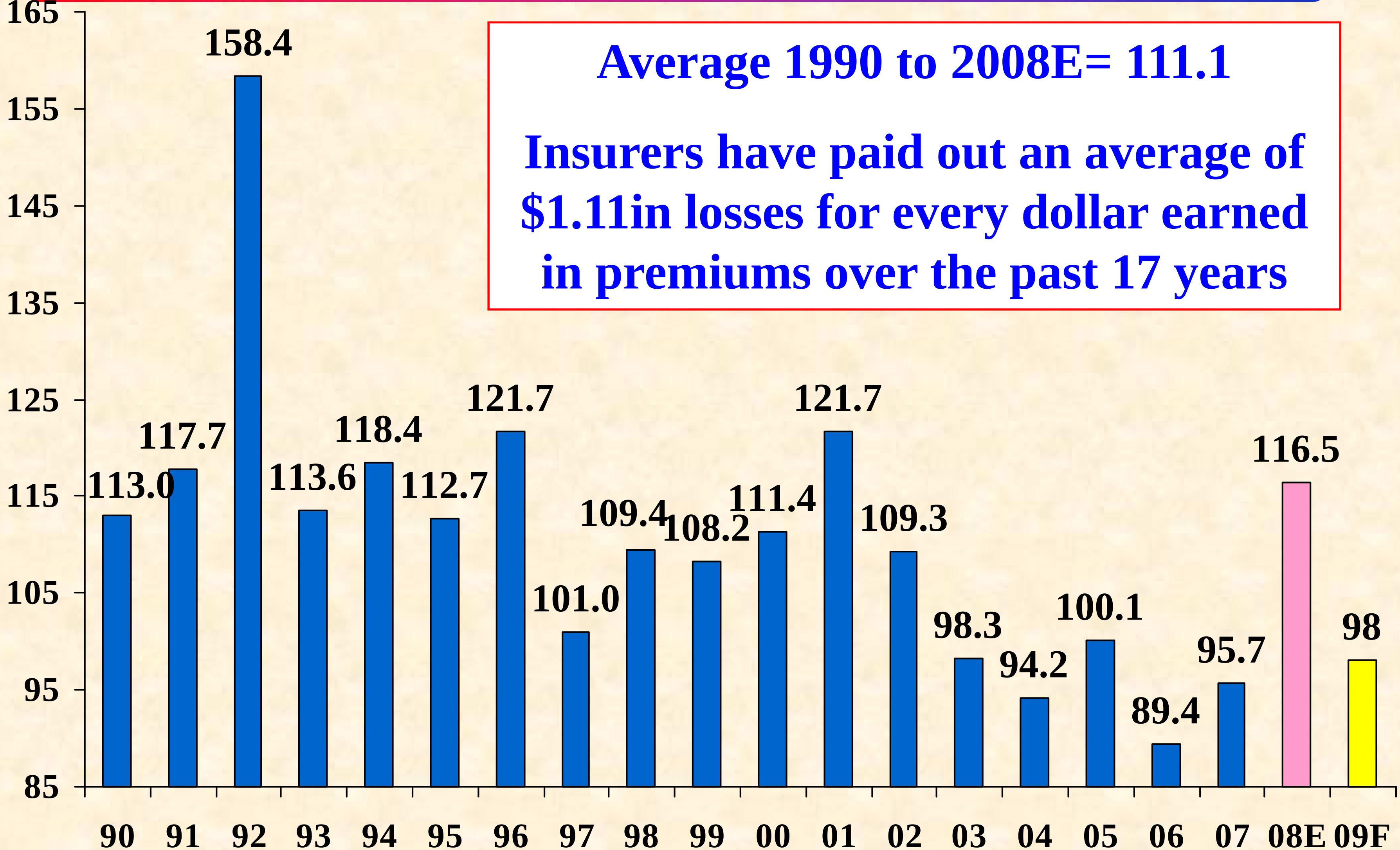


Source: A.M. Best (historical and forecast).

Homeowners Insurance Combined Ratio

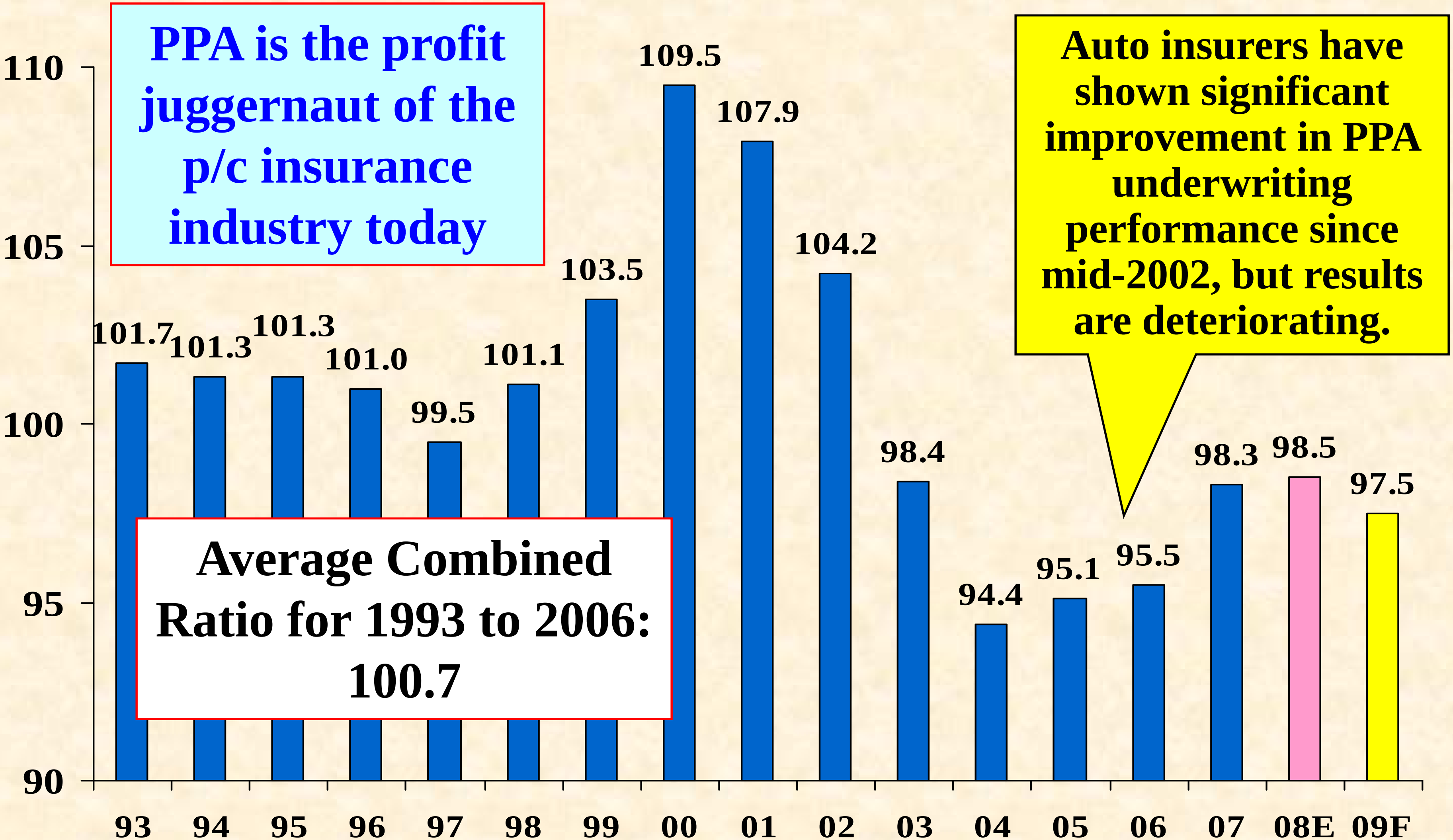
Average 1990 to 2008E= 111.1

Insurers have paid out an average of $1.11in losses for every dollar earned in premiums over the past 17 years



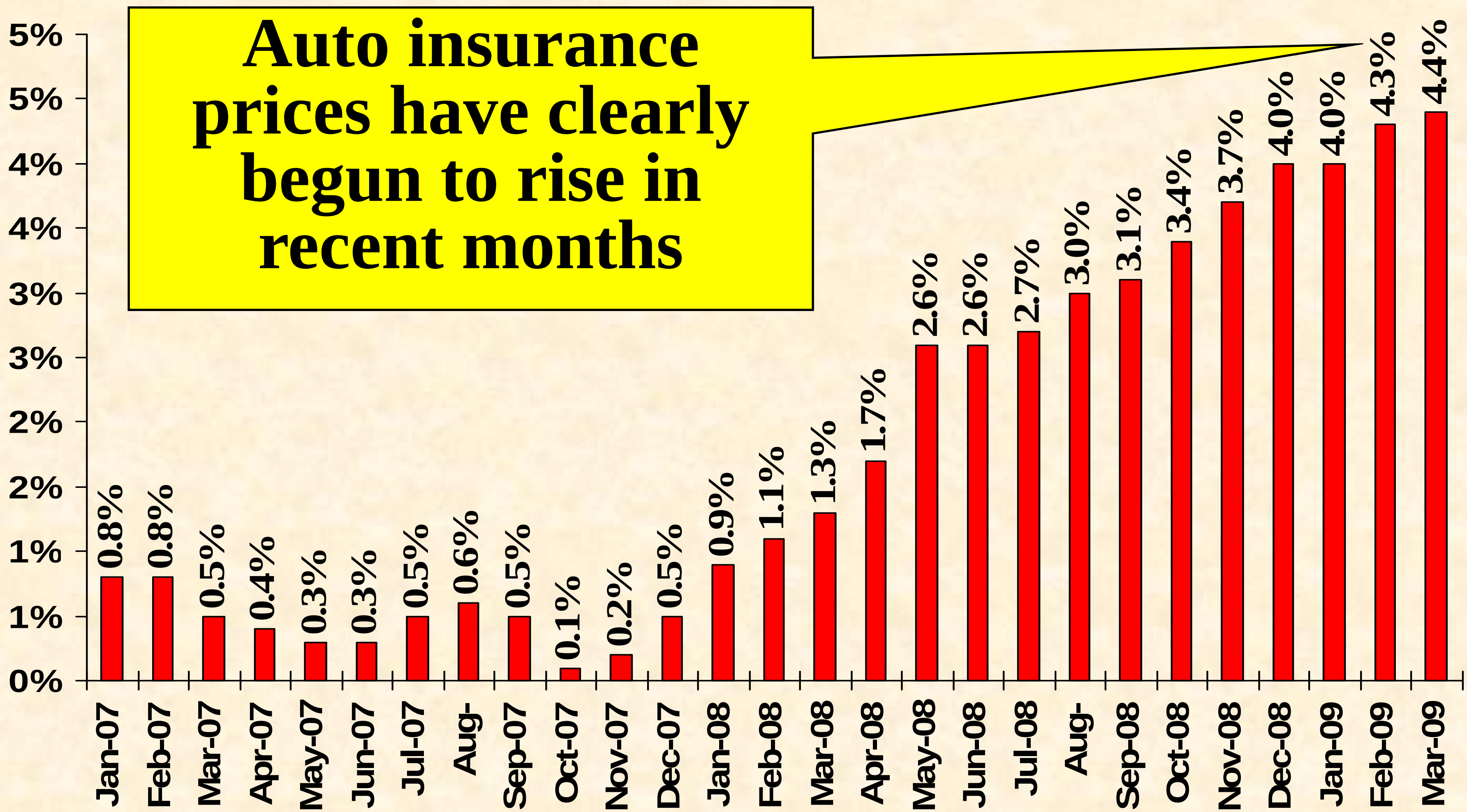
Sources: A.M. Best (historical and forecasts)

Private Passenger Auto (PPA) Combined Ratio



Sources: A.M. Best (historical and forecasts)

Monthly Change in Auto Insurance Prices*

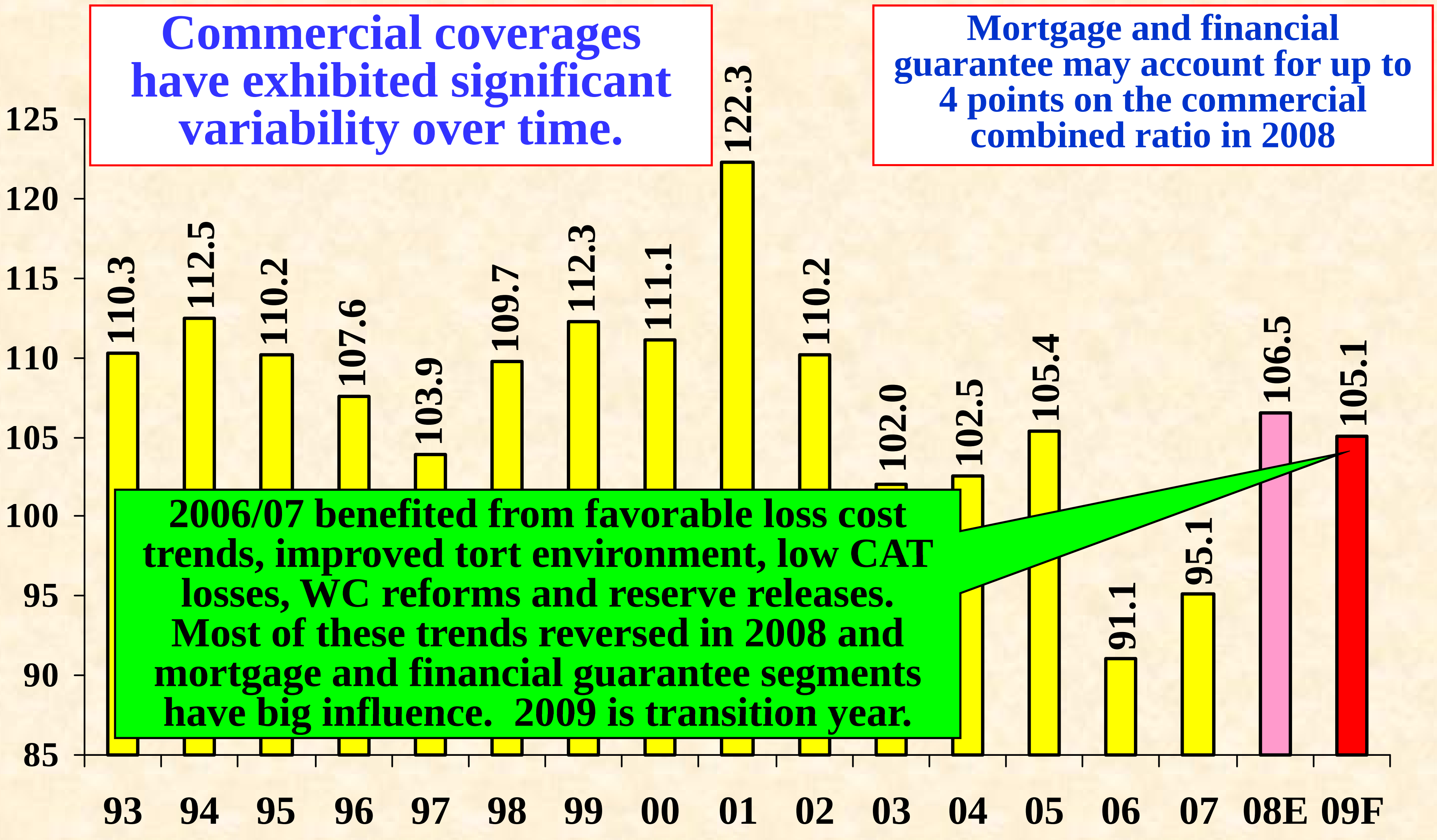


*Percentage change from same month in prior year.

Source: US Bureau of Labor Statistics

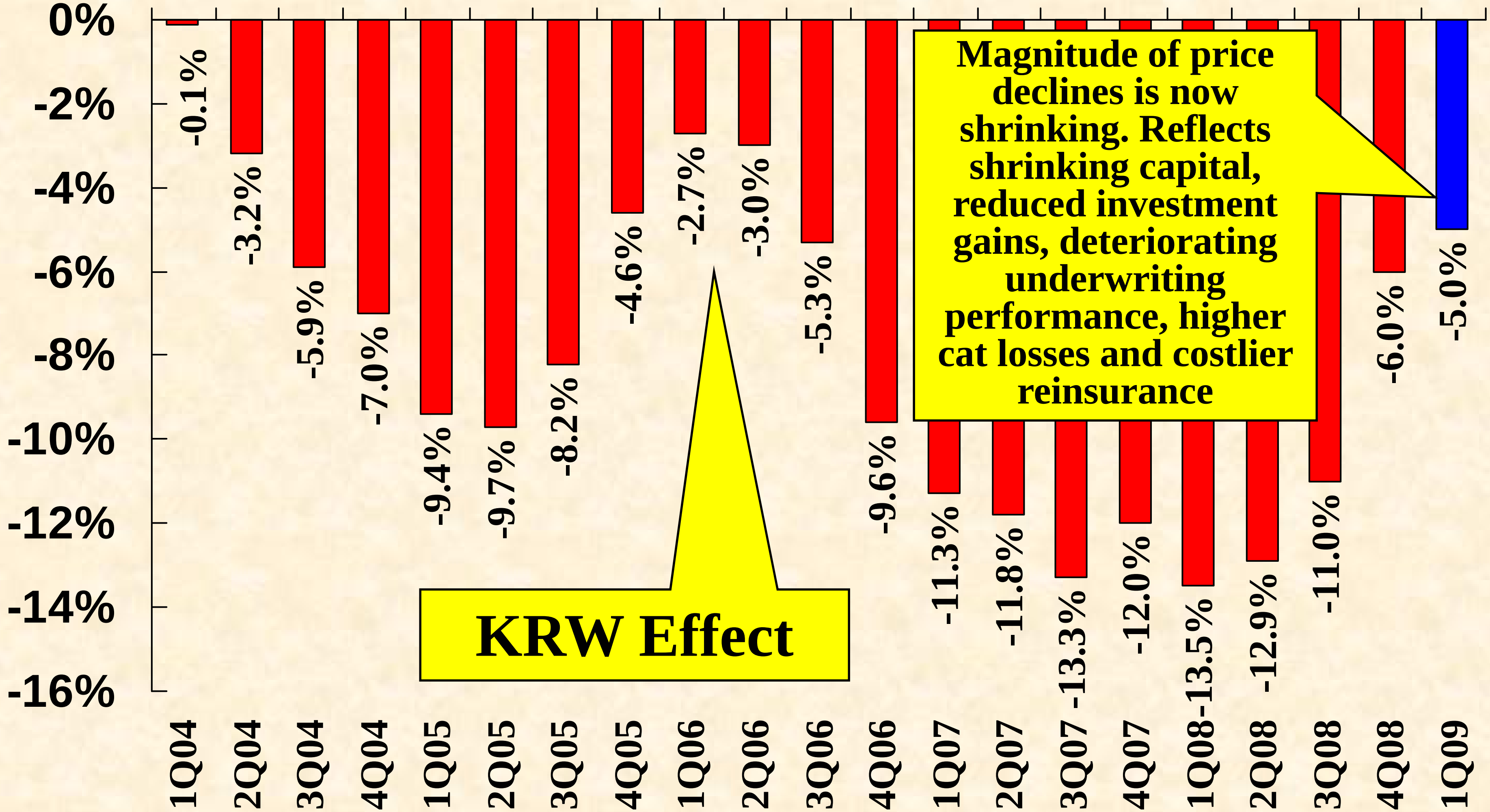
Commercial Lines

Commercial Lines Combined Ratio, 1993-2009F



Sources: A.M. Best (historical and forecasts)

Average Commercial Rate Change, All Lines, (1Q:2004 – 1Q:2009)

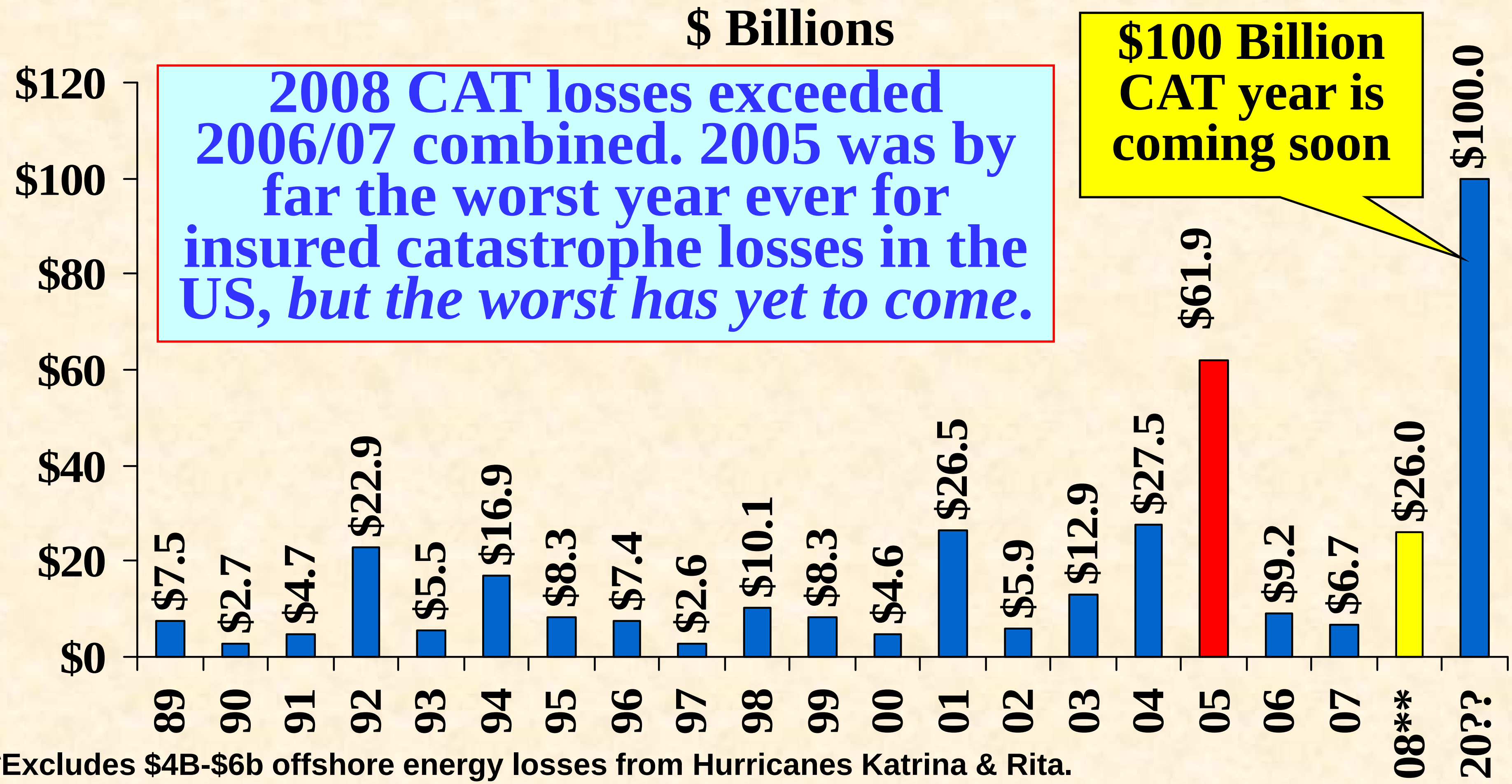


Source: Council of Insurance Agents & Brokers; Insurance Information Institute

Catastrophe Losses

Impacting Underwriting Results and the Bottom Line

U.S. Insured Catastrophe Losses*



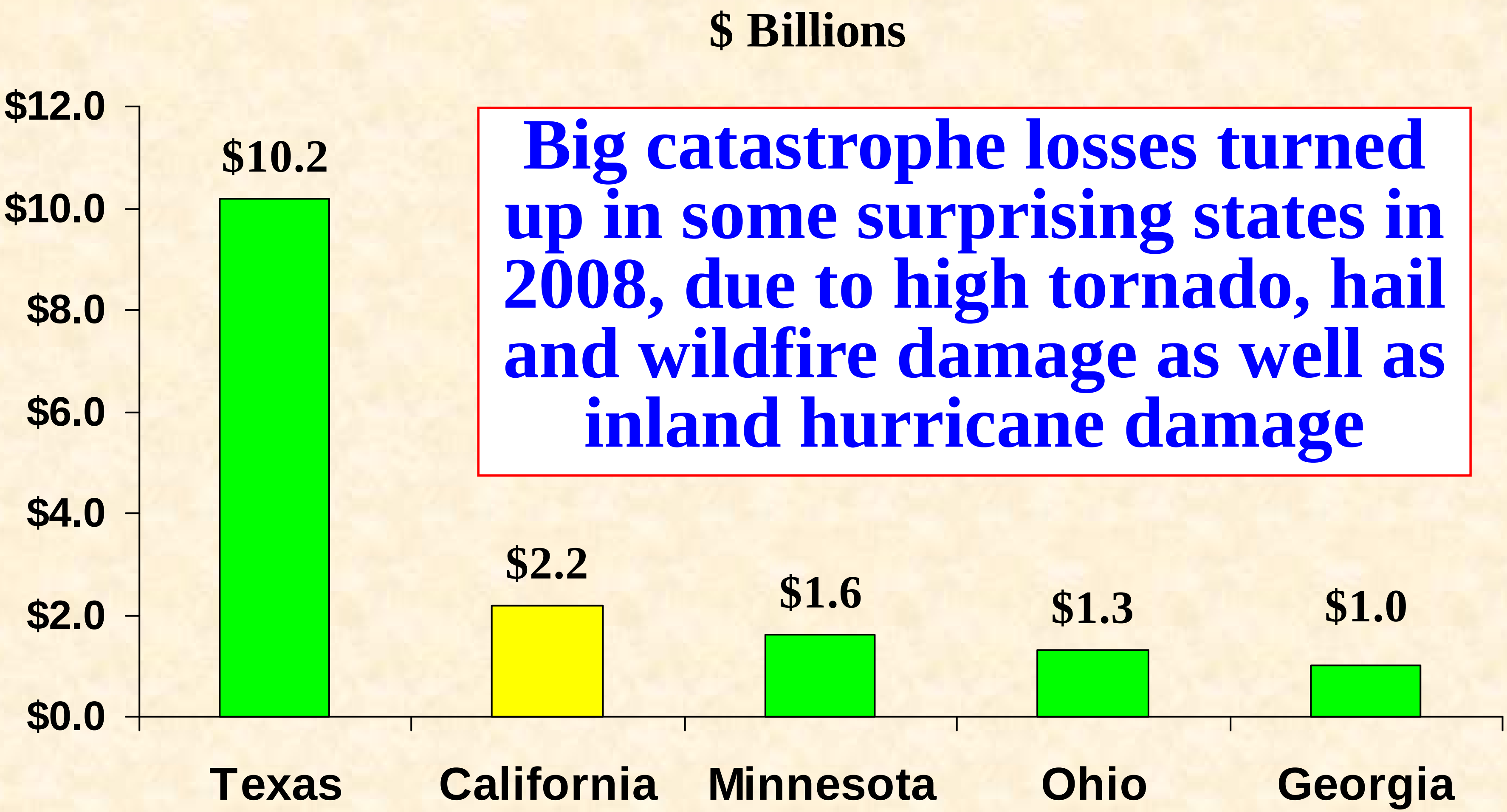
*Excludes $4B-$6b offshore energy losses from Hurricanes Katrina & Rita.

**Based on PCS data through Dec. 31. PCS $2.1B loss of for Gustav. $10.655B for Ike of 12/05/08.

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.

Source: Property Claims Service/ISO; Insurance Information Institute

States With Highest Insured Catastrophe Losses in 2008



Source: PCS; Insurance Information Institute.

Top 12 Most Costly Disasters in US History, (Insured Losses, $2007)

*PCS estimate as of 12/15/08.

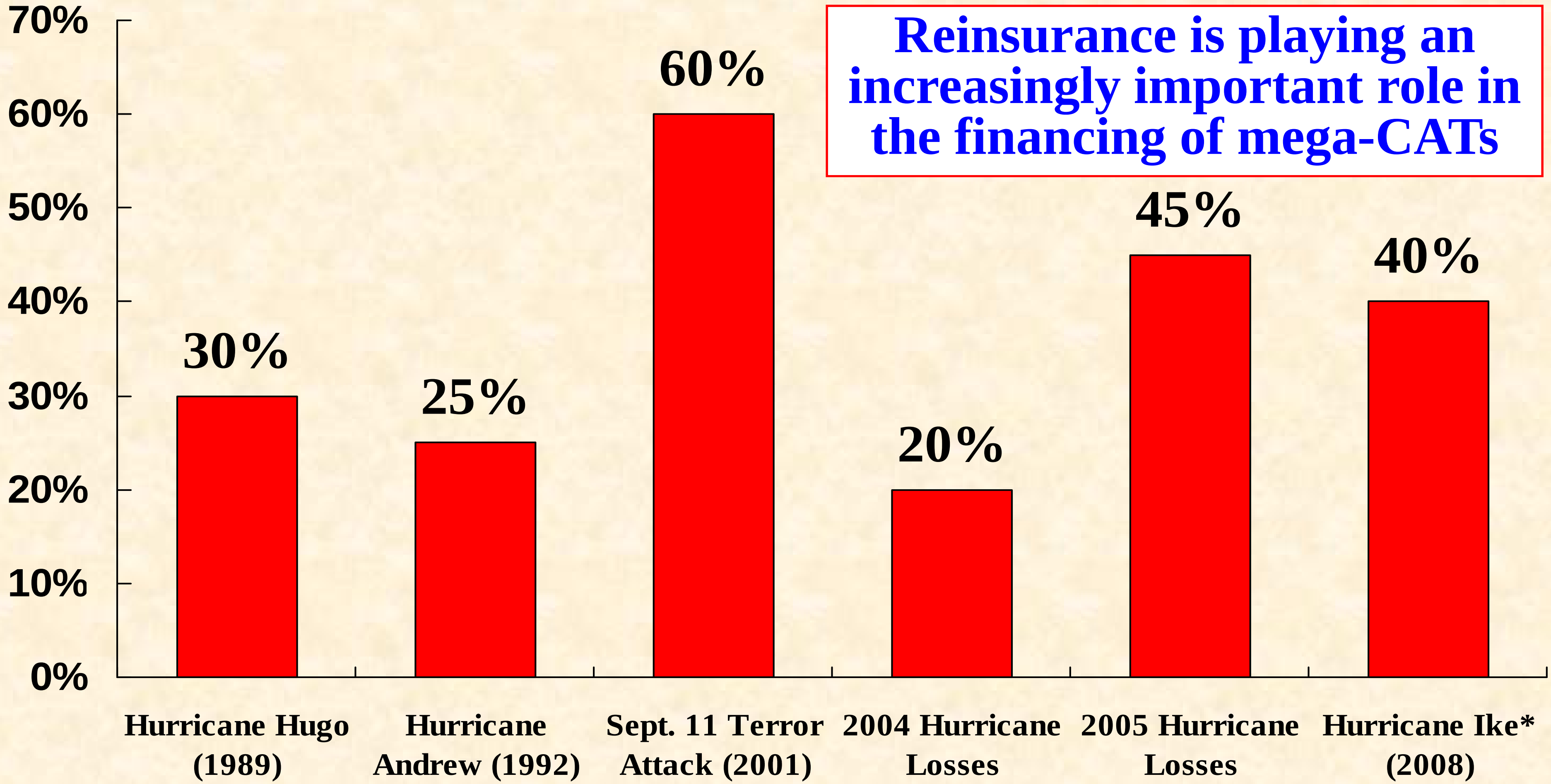
Sources: ISO/PCS; AIR Worldwide, RMS, Eqecat; Insurance Information Institute inflation adjustments.

Number of PCS Catastrophe Events, 1998-2008*

*PCS defines a catastrophe as an even that caused at least $25 million in insured property damage and affects and significant number of policyholders and insurers.

Source: PCS; Insurance Information Institute

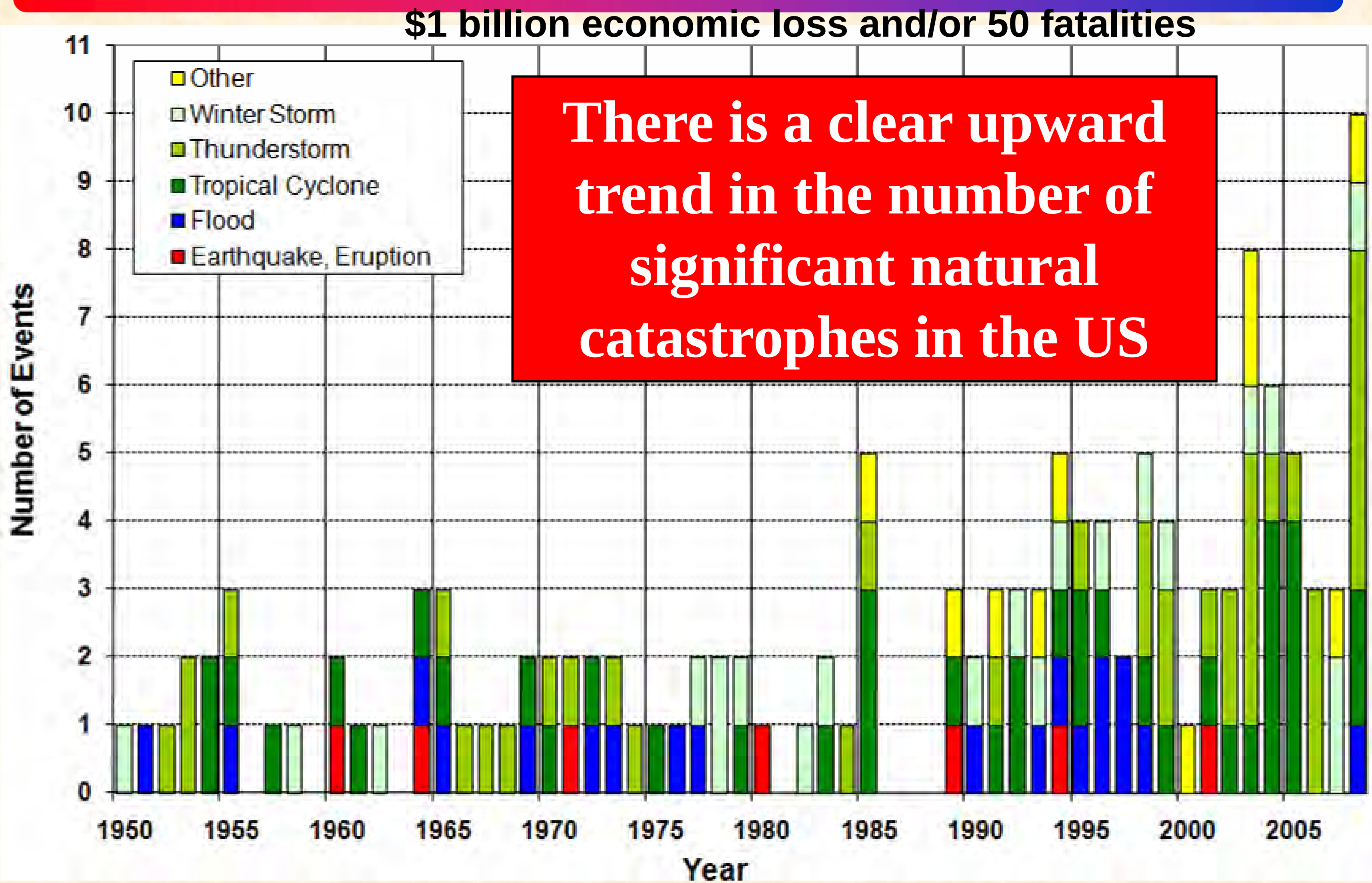
Share of Losses Paid by Reinsurers, by Disaster*



***Excludes losses paid by the Florida Hurricane Catastrophe Fund, a FL-only windstorm reinsurer, which was established in 1994 *after* Hurricane Andrew. FHCF payments to insurers are estimated at $3.85 billion for 2004 and $4.5 billion for 2005. Ike share is an estimate as of 2/9/09.**

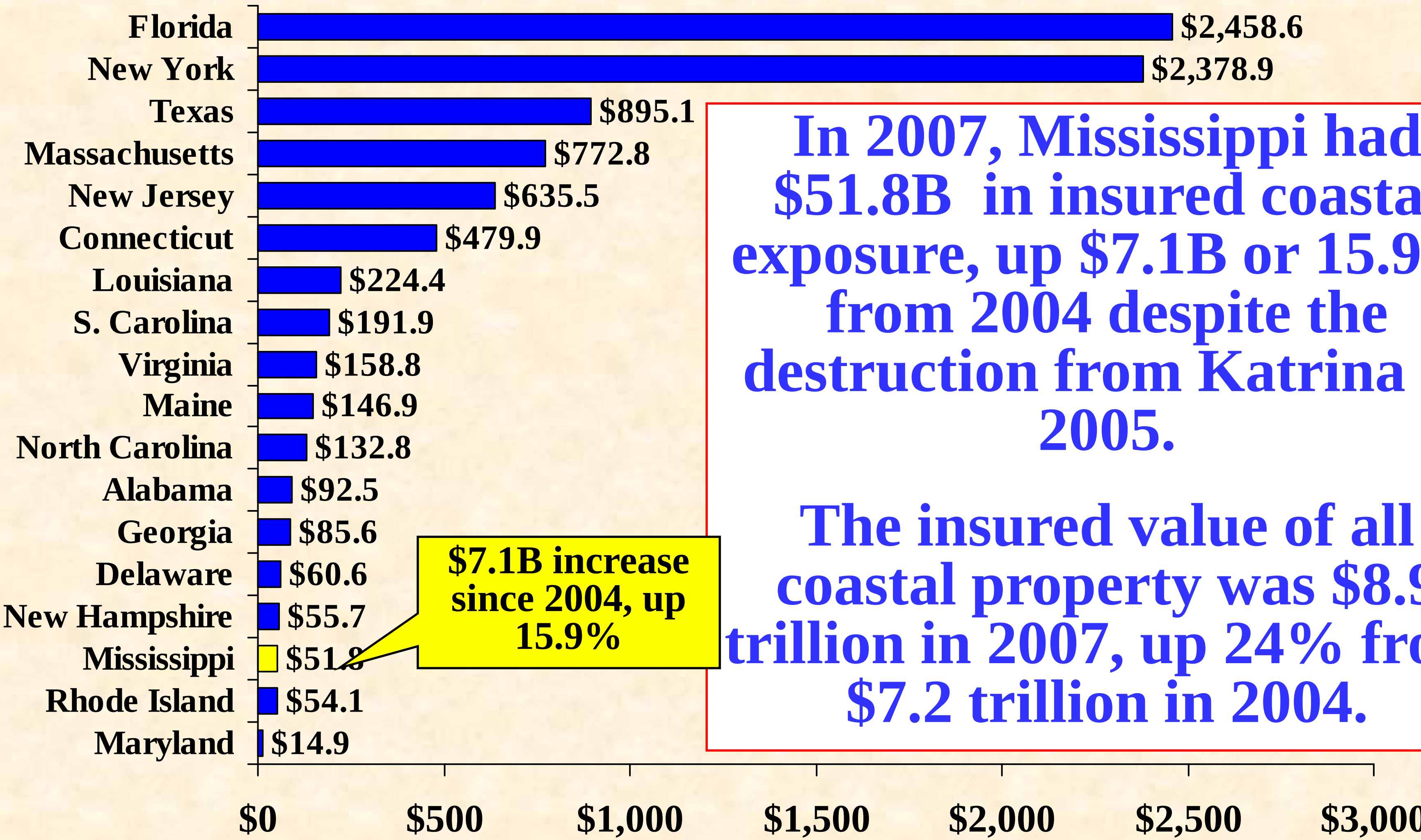
Sources: Wharton Risk Center, Disaster Insurance Project; Insurance Information Institute.

Number of U.S. Significant Natural Catastrophes*,1950 – 2008



Sources: Munich Re NatCat*SERVICE* **$1 billion economic loss and/or 50 fatalities.*

Total Value of Insured Coastal Exposure (2007, $ Billions)



In 2007, Mississippi had $51.8B in insured coastal exposure, up $7.1B or 15.9% from 2004 despite the destruction from Katrina in 2005.

The insured value of all coastal property was $8.9 trillion in 2007, up 24% from $7.2 trillion in 2004.

Source: AIR Worldwide

Key Issues & Threats Facing P/C Insurers Amid Financial Crisis

Manageable Challenges

Important Issues & Threats Facing P/C Insurers in 2009

1. **Reloading Capital After "Capital Event"**
   - Continued asset price erosion coupled with major "capital event" could lead to shortage of capital among *some* companies
   - P/C insurers have come to assume that large amounts of capital can be raised quickly and cheaply after major events (post-9/11, Katrina). This assumption may be incorrect in the current environment.
   - Cost of capital is *much* higher today, reflecting both scarcity & risk
   - Implications: P/C insurers need to protect capital today and develop detailed contingency plans to raise fresh capital & generate internally
2. **Long-Term Loss of Investment Return**
   - Low interest rates, risk aversion toward equities and many categories of fixed income securities lock in a multi-year trajectory toward ever lower investment gains
   - Many insurers have not adjusted to this new investment paradigm
   - Regulators will not readily accept it; Many will reject it
   - Implication 1: Industry must be prepared to operate in environment with investment earnings accounting for a smaller fraction of profits
   - Implication 2: Implies underwriting discipline of a magnitude not witnessed in this industry in more than 30 years
   - Lessons from the period 1920-1975

Source: Insurance Information Inst.

Important Issues & Threats Facing P/C Insurers in 2009 *(cont'd)*

3. **Regulatory Overreach**
   - **P/C insurers get swept into vast federal regulatory overhaul and subjected to inappropriate , duplicative and costly regulation**

4. **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**
   - **Historically extremely costly to p/c insurance industry**

Source: Insurance Information Inst.

AFTERSHOCK: Regulatory Response Could Be Harsh

All Financial Segments Including Insurers Will Be Impacted

Emerging Blueprint for Financial Services Regulatory Overhaul

Phase I: Systemic Risk Regulation/Regulator

- Identification of systemic risk points in the financial system
- Design of appropriate regulation to prevent future collapses
- Will require international consultation (US can't manage systemic risk alone)

- **Oversight Responsibility: Likely With Federal Reserve**
  - Fed would have capacity and power to assess risk across financial markets regardless of corporate form and to intervene when appropriate*
  - Fed could oversee (according to House FS Committee Chairman Barney Frank:
    - Hedge funds (need to ensure "complete transparency")
    - Credit ratings agencies
    - Executive compensation (to curb "perverse risk incentives")
  - TIMELINE: Frank wants "general outline" by April 2 meeting of G20 industrialized and developing nations

*http://financialservices.house.gov/press110/press0320082.shtml

Source: *Wall Street Journal*, "Frank Backs Regulator for Systemic Risk," 2/4/09, p. C3; I.I.I. research.

Possible Regulatory Scenarios for P/C Insurers as of Year-End 2009

- **Status Quo:** **P/C Insurers Remain Entirely Under Regulatory Supervision of the States**
  - Unlikely, but some segments of the industry might welcome this outcome above all others
- **Federal Regulation:** **Everything is Regulated by Feds**
  - Unlikely that states will be left totally in the cold
- **Optional Federal Charter (OFC):** **Insurers Could Choose Between Federal and State Regulation**
  - Unlikely to be implemented as envisioned for past several years by OFC supporters
- **Dual Regulation:** **Federal Regulation Layer Above State**
  - Feds assume solvency regulation, states retain rate/form regulation
- **Hybrid Regulation:** **Feds Assume Regulation of Large Insurers at the Holding Company Level**
- **Systemic Risk Regulator:** **Feds Focus on Regulation of Systemic Risk Points in Financial Services Sector**
  - What are these points for insurers? P/C vs. Life?

Source: Insurance Information Inst.

Insurance Information Institute On-Line

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THANK YOU FOR YOUR TIME AND

YOUR ATTENTION!

P/C Insurance in the Post-Catastrophe World

- **Investment Earnings Will Shrink Dramatically for an Extended Period of Time: Federal Reserve Policy, Shrinking Dividends, Aversion to Stocks**
  - **Trajectory toward lower investment earnings is being locked in**
- **Insurers Will Return to Their Underwriting Roots: Extended Period of Low Investment Exert Pressure to Generate Underwriting Profits Since 1960s**
  - **Chastened and "derisked" but facing the same (or higher) expected losses, insurers must work harder to match risk to price**
- **P/C Insurers: Profitable Before, During & *After* Crisis: Resiliency Once Again Proven**
  - **Directly the result of industry's risk management practices**

Source: Insurance Information Inst.