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# Mergers & Acquisitions: Current Opportunities & The Role of the Actuary

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# Presentation Outline

- Recent News & Transactions
- Factors Contributing to Increased Activity
- Roles for Actuaries

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# Recent News & Transactions

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## From the News Services...

- “Ernst & Young Issues 2008 US Outlook for Property/Casualty Insurance Industry” (PRNewswire 1/23/08)
  - “Margin pressure and continued pricing erosion will put increasing pressure on the insurance industry to achieve top line objectives in 2008”
- “Insurance Equity Analysts (Accenture) ... Predict Increased M&A Activity” (Accenture 4/11/08, 71% expect significant increase)
- “of 670 senior executives worldwide...68 percent expected (inorganic growth) to be more than 10 percent in the next 18 months” (Marsh, Mercer and Kroll, Insurance Journal 4/15/08)
- “Acquisitions and Investments May Dominate 2008 as Property/Casualty Underwriting Goes Soft” (BestWire 4/28/08)

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## From the News Services...

- “Industry Observers (Towers Perrin, Accenture) Expect Soft Market to Start a Significant M&A Push” (BestWire 5/5/08)
- “only 20% of international M&A in 2007 involved a U.S. entity at all.” (Conning 5/28/08)
- “Foreign Nations May Target Insurers for Acquisition” (NU Online News 7/2/08)
- “More M&A Activity on Tap for Industry” (NU Online News 7/11/08, Keefe, Bruyette, & Woods)
- “Tokio Marine's Purchase of Philadelphia Consolidated Showcases Attractive U.S. Buying Climate” (BestWire 11/08)

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# Recent Transactions - Domestic

- Liberty Mutual acquired Safeco Corp.
- Liberty Mutual acquired Ohio Casualty
- ProCentury merged with Meadowbrook
- Wells Fargo acquired Wachovia
- ProAssurance to acquire Georgia Lawyers
- Fidelity National Financial bid on LandAmerica Financial Group

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# Recent Transactions - International

- Maiden Insurance (BDA) acquires GMAC Insurance
- Bermuda Based Allied World acquired U.S. Darwin Professional Underwriters
- Tokio Marine Holdings acquires Philadelphia Consolidated Holding
- Millea Holding buys Kiln Ltd.
- QBE Insurance acquires Unigard & General Casualty
- Mapfre acquired Commerce Group
- Allianz invests \$2.5B in Hartford Insurance Group
- Tower Group to acquire CastlePoint

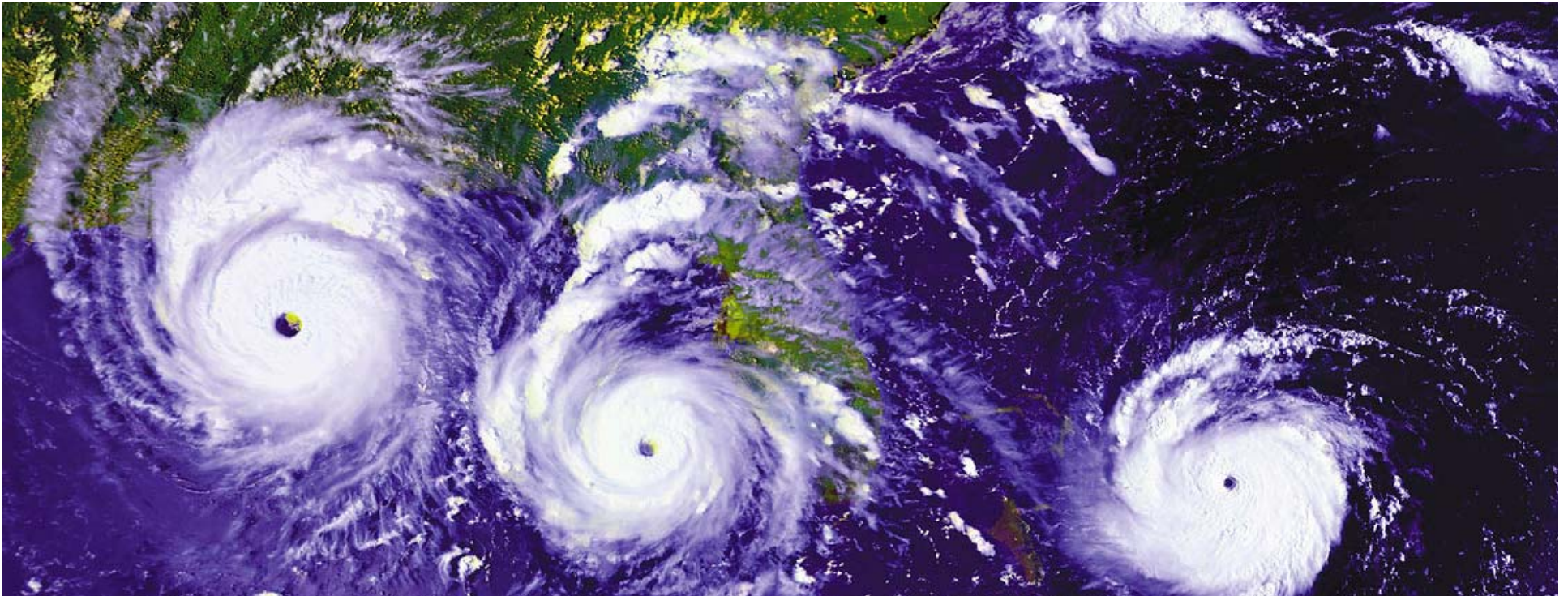
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# Contributing Factors

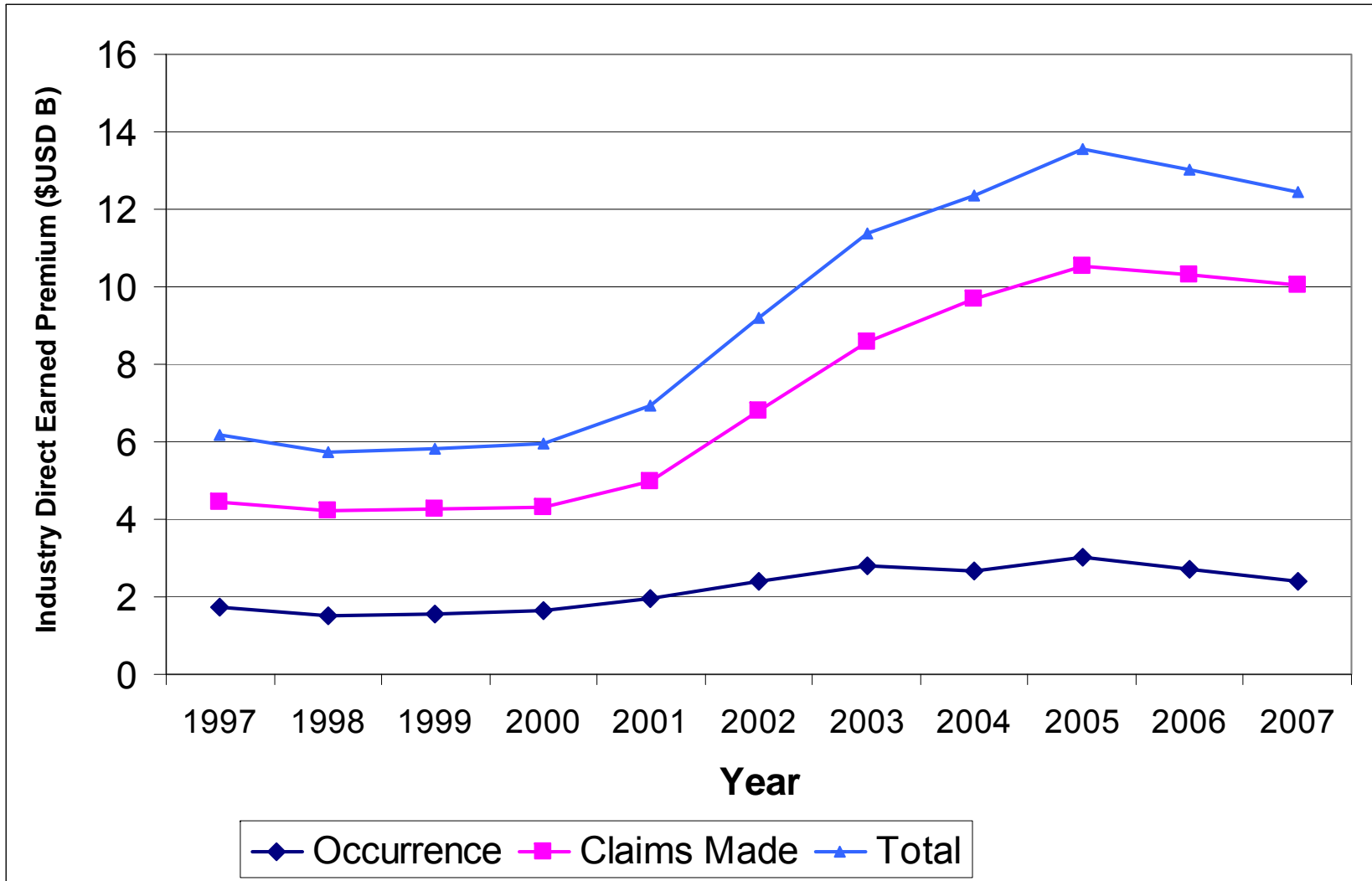


# Perfect Storms Come Ashore

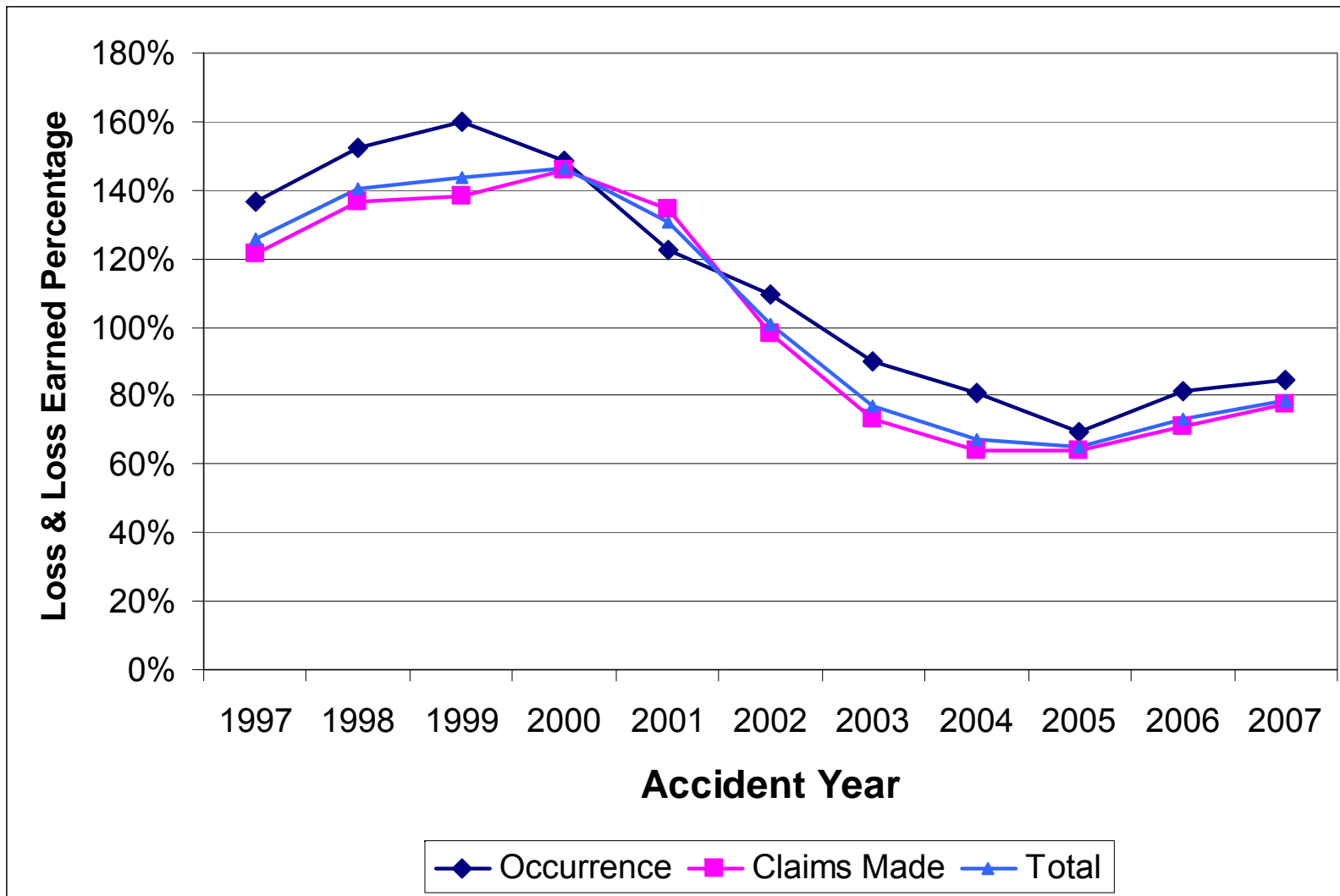
- Soft Market → ↓ Growth/Income → ↓ Stock Prices
- Foreign Exchange Rates
- Insurance Regulation



# Industry Medical Malpractice Earned Premium



# Industry Medical Malpractice Loss & LAE Ratios

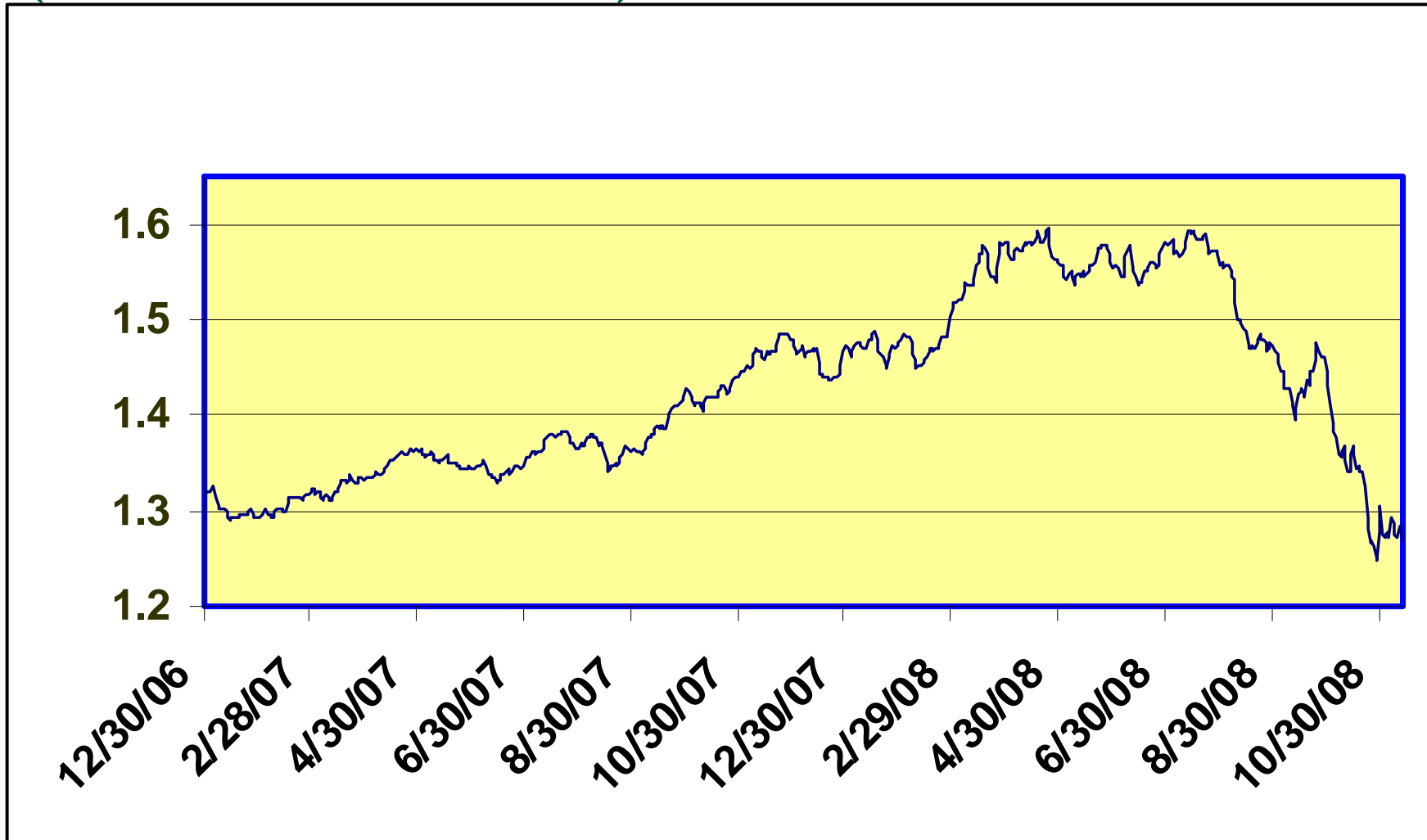




Stocks of many publicly-traded insurers are priced 40% or more below that of a year ago.

# U.S. Dollars versus Euro

(Has the bubble burst?)



# Yen per 1 U.S. Dollar



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# Is a Federal Option Inevitable?

- “Maine Senator Calls Federal Insurance Regulation 'Hot Issue” (BestWire 4/4/08)
- “Economists Argue Federal Role Essential to Future of Insurance” (BestWire 7/14/08)
- “NAIFA Formalizes 'Conditional' OFC Support” (BestWire 9/11/08)
- “The Cost of Regulation”  
U.S. insurers pay \$1.5 billion for states to regulate them.  
*Outcomes vary widely.* (Best's Review September 2008)
- “Industry Pros Say U.S. Can't Compete With Bermuda” (BestWire 10/27/08)

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# Other Current Acquisition Incentives

- Emergency Economic Stabilization Act
  - May Provide Opportunities
- Enhanced Tax Incentive: Built-In Losses
  - IRS Notice Stimulates Interest in Acquisitions of Financial Institutions with Quality Asset Issues



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# Roles for Actuaries

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# Actuarial Roles in M&A

- What you can reasonably expect
- Reserving
- Ratemaking
- Customer Responses

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# Reasonable Expectations

- Actuarial Standard of Practice No. 41 “Actuarial Communications” (ASOP 41) states:

“(A)n actuarial report should identify the data, assumptions, and methods used by the actuary with sufficient clarity that another actuary qualified in the same practice area could make an objective appraisal of the reasonableness of the actuary’s work as presented in the actuary’s report.”

# Reserving Issues for Actuaries in M&A

- Are the reserves reasonable?
- How “material” are the RMADs (risk of material adverse deviation)? Are there others?
- Is the SAO properly prepared?
- Has the opining actuary changed in recent years? Why? How did their estimates compare?
- How has the reserve run-off performed?
- Does reinsurance present any specific concerns?
- How much variability is there in the reserves?
  - What would be a reasonable reserve guarantee?
- Are there other issues (PDR, DDR, ERE) that need to be considered?

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# Ratemaking Issues for Actuaries in M&A

- Are the current rates adequate?
- What is the current competitive position?
  - Rate comparisons
  - Conversion/hit ratios
  - Retention ratios & renewal premium changes
- Is the current rate/price monitoring reasonable?

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# Ratemaking Issues for Actuaries in M&A

- How do the products compare/mesh with yours?
- How does the policy management/pricing software compare/mesh with yours?
- What is the quality of the current ratemaking data?
- What is the current level of ratemaking sophistication? (Problem or opportunity?)

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# Customer Response Issues in M&A

The total may not equal the sum of the parts

- Agency/Distribution Issues

- Where will overlaps in agency networks create problems?
  - Regional personnel
  - Relationships between agents
  - Concentration in a specific market
- Where will new products create growth opportunities?

- Customer Issues

- Will hit ratios and retention ratios be impacted?
- Will renewal pricing change be impacted?
- What pricing issues will be caused by migrating from one product to another?

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# Parting Thoughts

The Chinese use two brush strokes to write the word 'crisis.' One brush stroke stands for danger; the other for opportunity. In a crisis, be aware of the danger - but recognize the opportunity.

John F. Kennedy

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