

MANAGING EXTREMES **Willis Re** STATE OF THE REINSURANCE MARKET: CASUALTY

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The casualty market **Willis Re** MANAGING EXTREMES

- Analysis of casualty trends and relationships
 - Premiums and price
 - AY and CY results
 - Reserves and cash flow
 - Reinsurance implications
- Lines of business
 - Workers Compensation
 - Other Liability Occurrence
 - Medical Professional
 - Other Liability CM

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UW CYCLE - DRIVERS **Willis Re** MANAGING EXTREMES
Casualty Market

Pricing Competition

- Pricing responds to Calendar Year results
- Accident Year results ultimately reflect pricing
- Ultimate AY results affect CY results – cyclical, aka reserve development

Loss Trends

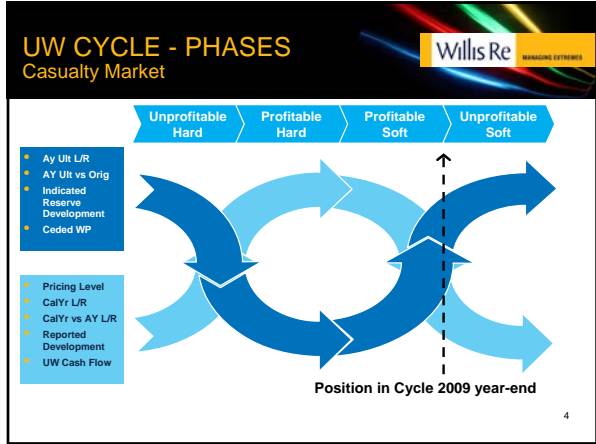
- Loss trends reflects economic, social, and legal issues – frequency / severity
- Pricing response lags loss changes – cyclical
- If losses stable, UW cycle dominated by pricing

Economic Environment

- Capital, asset, interest, and inflation changes important, but secondary issues
- Casualty pricing does not appear to be ROE based
- However, watch UW cash flows – cyclical

IMPORTANCE

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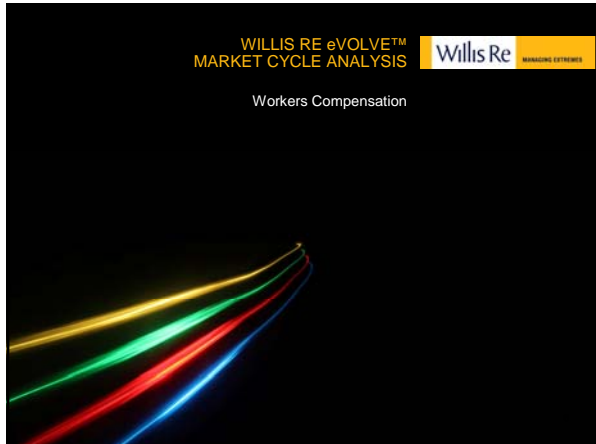


UW CYCLE - ISSUES

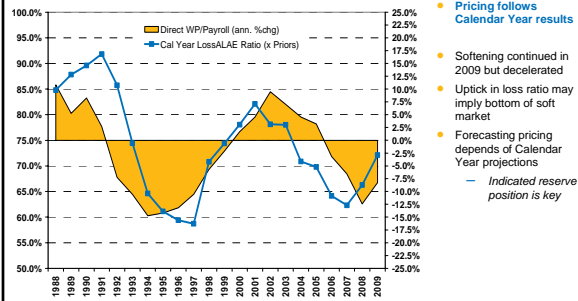
Casualty Market

Pricing Competition	Loss Trends	Economic Environment
<ul style="list-style-type: none"> - Recent profitable CY results have driven significant price decreases - Price level still declining - AY results appear to be becoming inadequate - CY will soon turn unfavorable <ul style="list-style-type: none"> • Reserve position worsening • UW cash flows negative and deteriorating <p>➤ <u>Pricing near turning point?</u></p>	<ul style="list-style-type: none"> - Benign for over a decade <ul style="list-style-type: none"> • Moderate severity trends • Declining frequency - Reform gains under pressure in various states - Possible return of inflation <ul style="list-style-type: none"> • Economic recovery • Monetary policy - CY implications <ul style="list-style-type: none"> • Pressure on AY results • Reserves reflect implicit historical inflation rate <p>➤ <u>Nowhere to go but up?</u></p>	<ul style="list-style-type: none"> - Industry emerged from recent turmoil relatively unscathed <ul style="list-style-type: none"> • Watch treasury yields - Pricing did not respond to increase in capital costs - Need to bolster liquidity <ul style="list-style-type: none"> • Will insurers compete to generate cash? - Business cycle downturn reducing policies <ul style="list-style-type: none"> • Will insurers compete to cover fixed costs? <p>➤ <u>Wildcard?</u></p>

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Workers Compensation pricing vs. CY results



- Pricing follows Calendar Year results
 - Softening continued in 2009 but decelerated
 - Uptick in loss ratio may imply bottom of soft market
 - Forecasting pricing depends of Calendar Year projections
- Indicated reserve position is key

Workers Compensation reinsurance market trends



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|--|--|
| <ul style="list-style-type: none"> • Working layer market pricing <ul style="list-style-type: none"> — Stable / seeking increases — Primary pricing is an issue — Investment income pressures | <ul style="list-style-type: none"> • Catastrophe market pricing <ul style="list-style-type: none"> — Softening continues, at a slower rate — No capacity shortage — Aggregate exposures dropping with payrolls: drop recognized by reinsurers — Minimum premiums apply for higher layers |
|--|--|

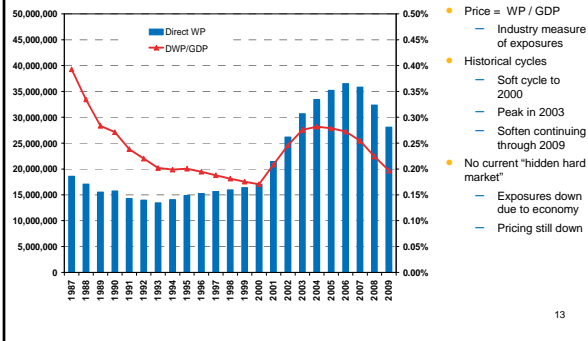
WILLIS RE eVOLVETM MARKET CYCLE ANALYSIS



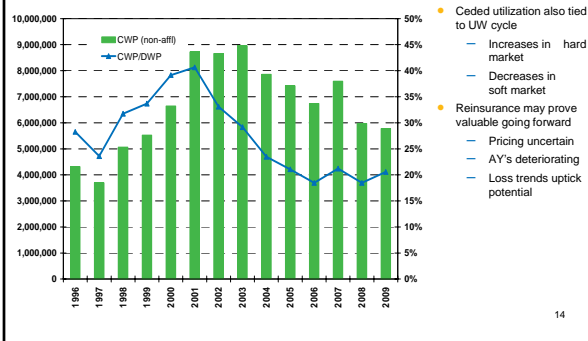
Other Liability Occurrence



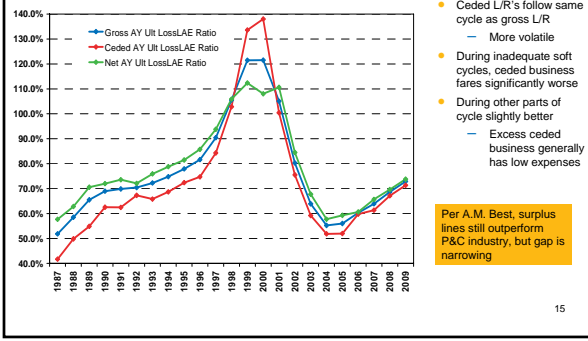
Other Liability (Occ.) premium & price



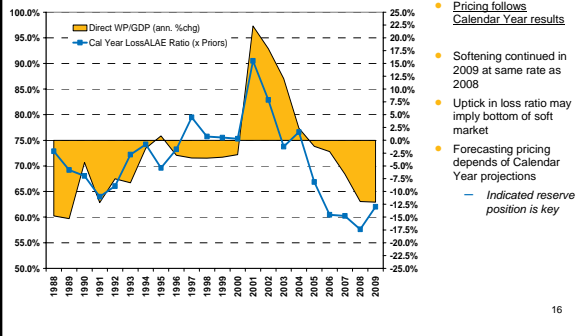
Other Liability (Occ.) ceded premium & utilization



Other Liability (Occ.) AY gross, ceded, net results



Other Liability (Occ.) pricing vs. CY results



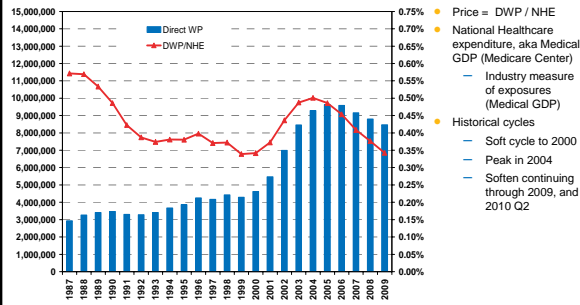
Other Liability (Occ.) reinsurance market trends

- CY mentality more prevalent in primary market than reinsurance market
 - Cedants seeking to convert pro rata programs to XOL
- Reinsurers remain disciplined
 - Pricing stable / seeking increases
 - Primary pricing is an issue
 - Investment income pressures
 - Seeking tighter exclusions
 - Reinsurers playing defense on select clients
- Start-up capacity difficult to obtain

Medical Professional Liability



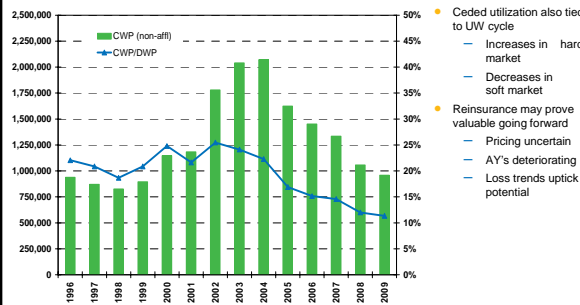
Medical Professional (CM) premium & price



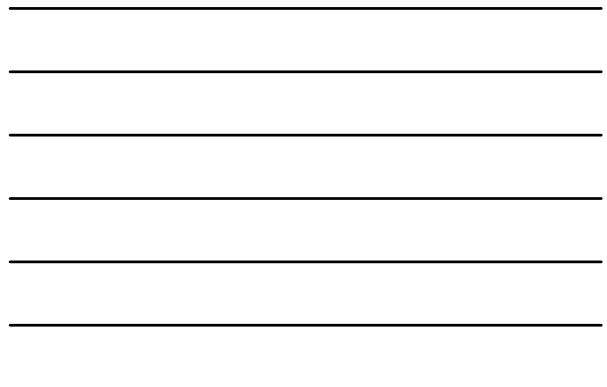
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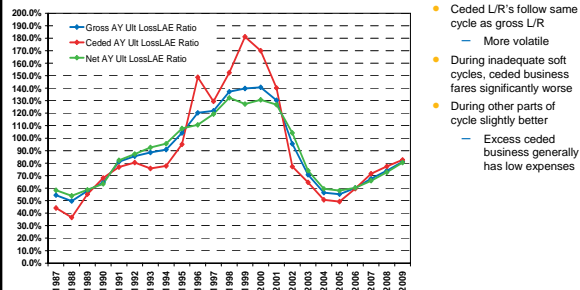
Medical Professional (CM) ceded premium & utilization



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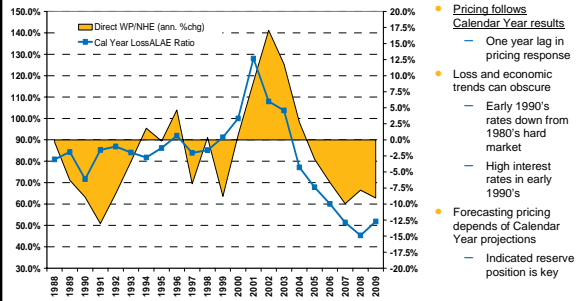
Medical Professional (CM) AY gross, ceded, net results



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Medical Professional (CM) pricing vs. CY results



Medical Professional (CM) reinsurance market trends



- Reinsurers view:
 - Physicians / Surgeons base rates and ILFs more adequate than original rates for Hospitals
 - Differential viewed as wider on rates than on ILFs
 - Frequency trends seen as stable, severity as increasing
- Capacity is stable to increasing
- Coverage terms remaining stable
- Reinsurers “playing defense” on select clients

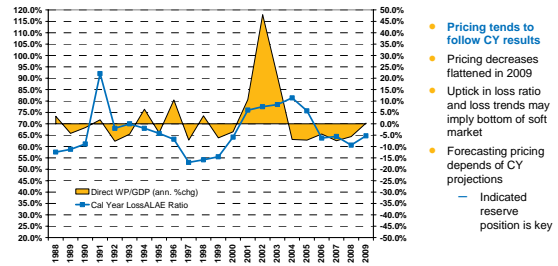
WILLIS RE eVOLVETM MARKET CYCLE ANALYSIS



Other Liability (CM)



Other Liability (CM) pricing vs. CY results



- Pricing tends to follow CY results
- Pricing decreases flattened in 2009
- Uptick in loss ratio and loss trends may imply bottom of soft market
- Forecasting pricing depends of CY projections
- Indicated reserve position is key

Other Liability (CM) reinsurance market trends

- Reinsurers taking very different approach towards established players vs. new entrants
- Public D&O - Wary of aggregation, a preference for QS
- Financial E&O behaving like Public D&O
- P/NP D&O, other PI finding adequate support
- EPL concerns with economic state

Summary – Economy/UW Cycle

- Exposures flat to declining
- Some industries more acutely affected by economy (construction in WC/GL)
- DWP down overall, with insurers looking to retain more of it
- Recent CY results suggest cycle may be turning

Summary – Reinsurance Market

- Capital - supply up
- Demand – down as cedants retain more
- Could/should make for reinsurance that is “easy” to get, but...
 - Rates down relative to historical
 - Reinsurer wariness prevents further price cuts

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Summary – Reinsurers showing discipline

- Not softening rates as much
- Not increasing ceding commissions
- Holding terms and conditions
- Managing limits/lines extended
- Scrutinizing exposure sources
 - Difficult time to start writing a new product/industry class
- Waiting for primary prices to firm up

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Summary – Reinsurers are wary

- Investment income concerns
- Scrutinizing underlying exposures
- Excluding types of loss (Chinese drywall, lead paint, etc.)
- Watchful of original terms and conditions
 - Multi-year, erosion of exclusions, throw in coverage, etc.
- Not wanting to write “pure risk” XOL as retentions rise
 - Min premiums, authorizing partial lines

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Questions & Comments?

- Questions can be directed to tim.pollis@willis.com
- Thanks!

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