



---

# Good Fundamentals but not a Hard Market for Property & Casualty Insurers

# Discussion Topics

1. **Credit Ratings**
2. **Rating Trends in North American P&C Insurance**
3. **Personal Lines Outlook**
4. **Commercial Lines Outlook**
5. **Commercial Casualty Reserve Profile**
6. **Sensitivity to Interest Rate Changes**

# Global Long-Term Rating Scale

## Investment -Grade

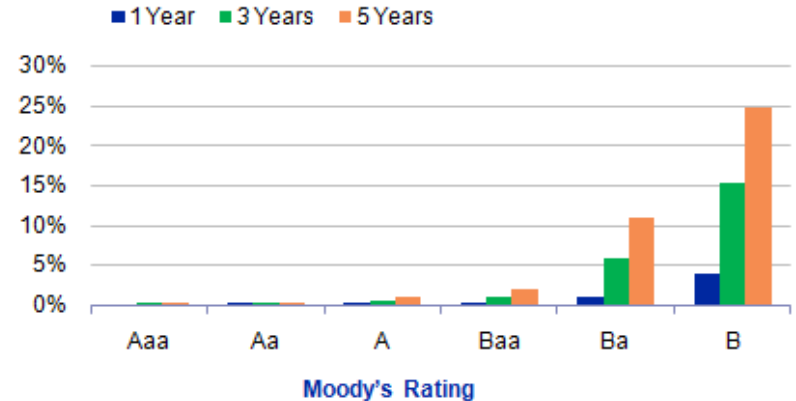
Aaa	Highest quality, lowest credit risk
Aa	High quality, very low credit risk (Aa1, Aa2, Aa3)
A	Upper-medium grade, low credit risk (A1, A2, A3)
Baa	Medium grade, moderate credit risk (Baa1, Baa2, Baa3)

## Speculative -Grade

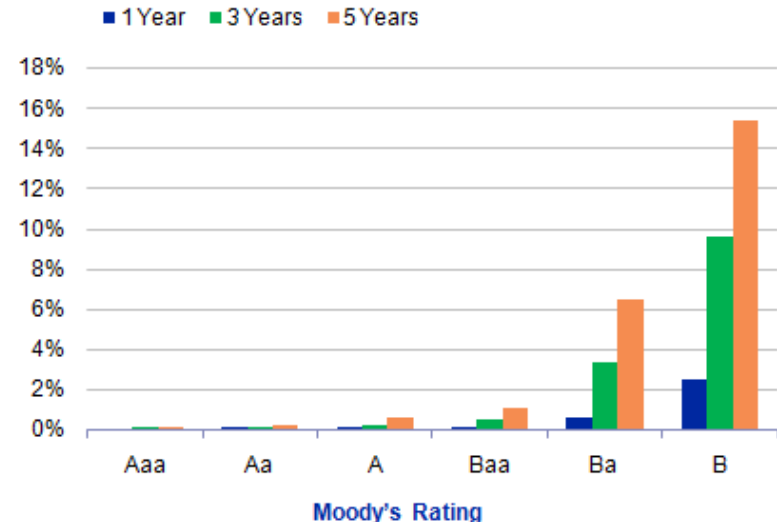
Ba	Speculative, substantial credit risk (Ba1, Ba2, Ba3)
B	Speculative, high credit risk (B1, B2, B3)
Caa	Speculative, very high credit risk (Caa1, Caa2, Caa3)
Ca	Highly speculative, likely in/near default, some recovery
C	Lowest rated, typically in default, little recovery

Source: Moody's Annual Default Study: Corporate Default and Recovery Rates, Feb 28, 2013, Exhibits 22 & 34

## Default Probabilities

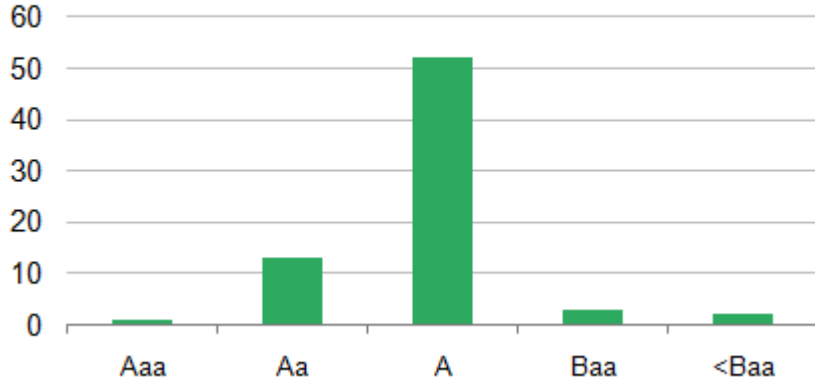


## Expected Loss

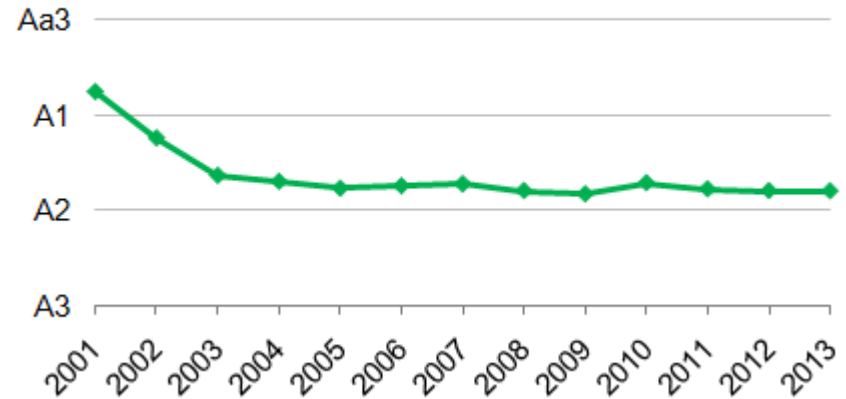


# Ratings Trends in North American P&C: Stable Outlook

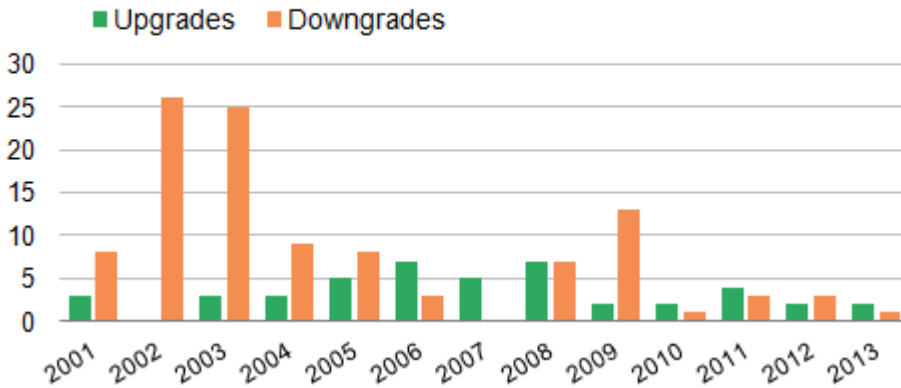
## Rating Distribution (71 Groups)



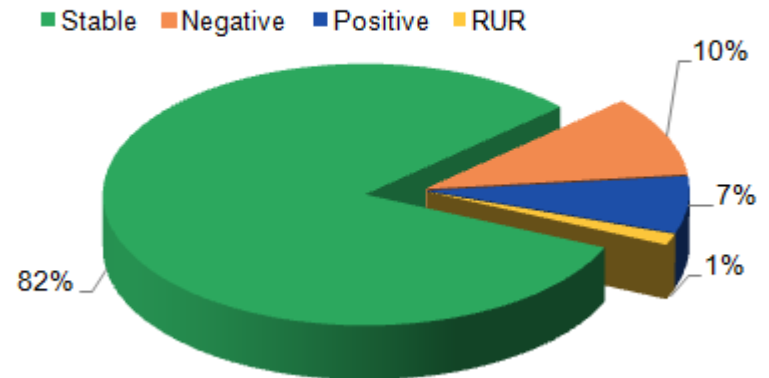
## Average IFS Rating



## Upgrades and Downgrades



## Outlook Distribution



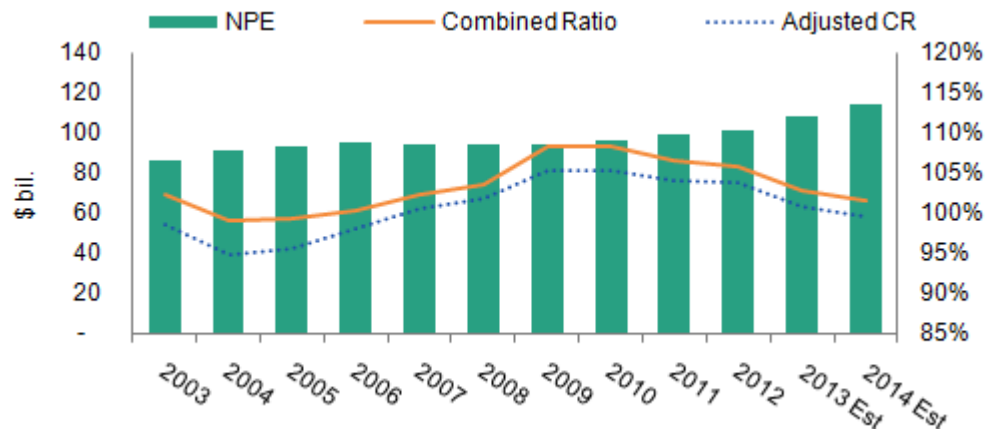
as of Sept. 1, 2013

# Personal Lines: Underwriting Discipline Drives Margin Improvement

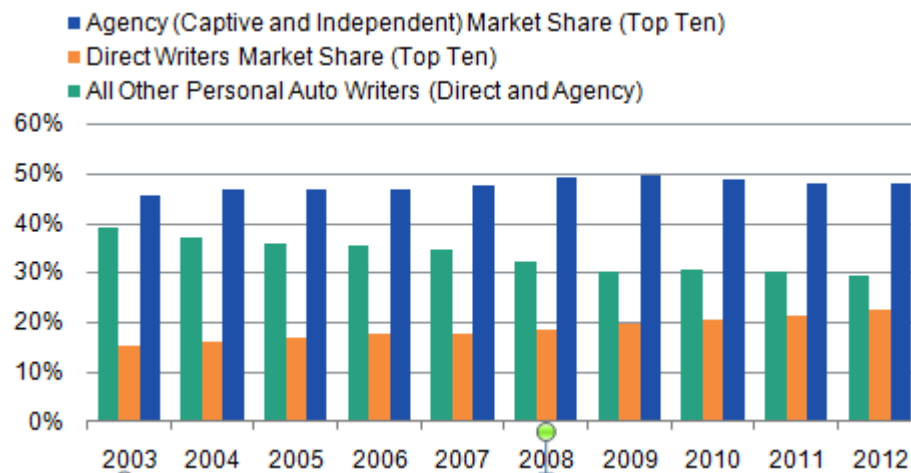
- » Auto rate increases are moderating but keeping pace with loss cost trends
- » Direct auto writers continue to gain market share; agency writers shifting focus towards growth after re-underwriting efforts
- » Homeowners' rates continue to rise but at a slower pace; ex-cat underlying combined ratios improve
- » Balance sheets – capital, investments, liquidity – in good shape
- » Persistent catastrophe risk: focus on geographic concentrations given multitude of severe convective storms

Source : Moody's, SNL Financial LC. Contains Copyrighted And Trade Secret Materials Distributed Under License From SNL, For Recipient's Internal Use Only

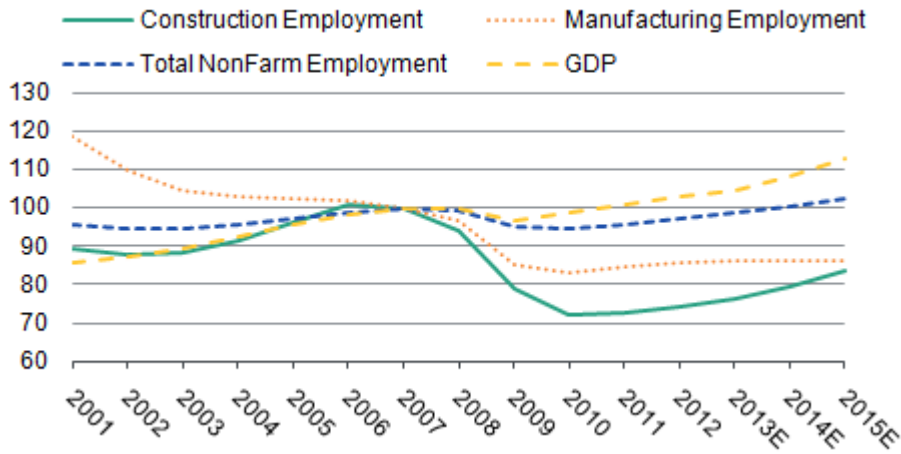
## Personal Auto Liability – Growth & Profitability



## Personal Auto Market Share



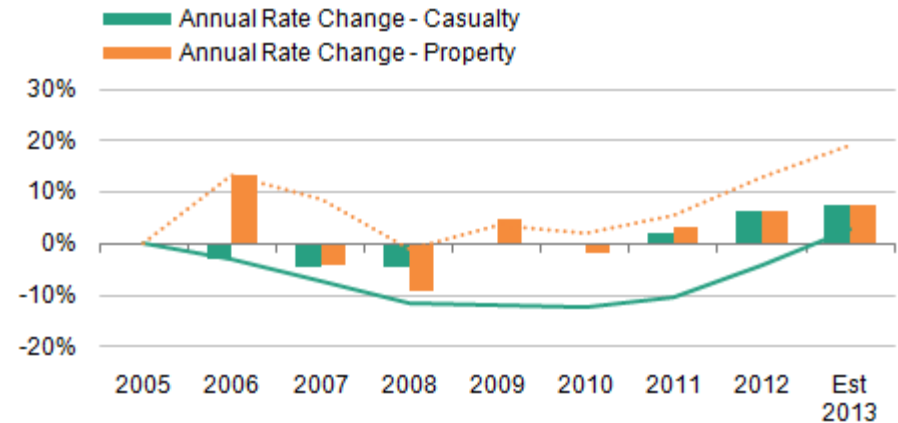
# Commercial Lines: Favorable Pricing and Ample Capital



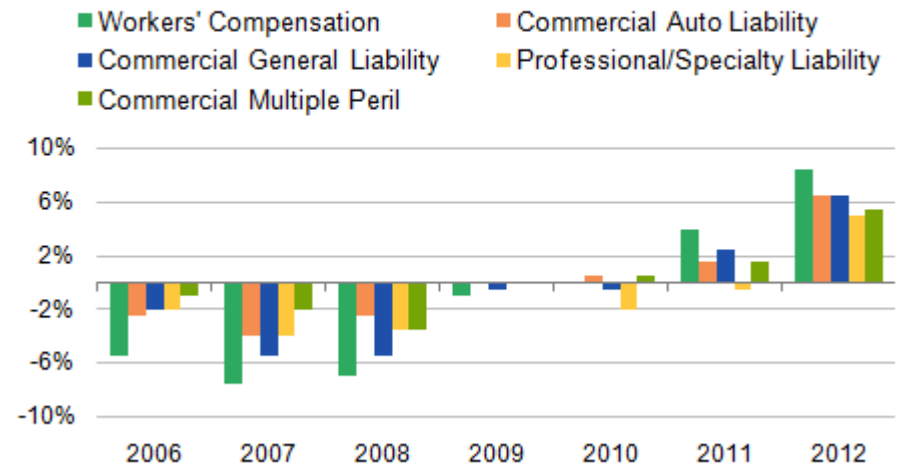
Source: Moody's Analytics

- » Exposure growth consistent with gradually improving employment and GDP trends
- » Low interest rates continue to support a favorable rate environment
- » Favorable pricing trends will continue but may be peaking given ample capacity
- » Greater susceptibility to loss of momentum in property and large account business

## Moody's Survey Results



## Moody's Survey Results

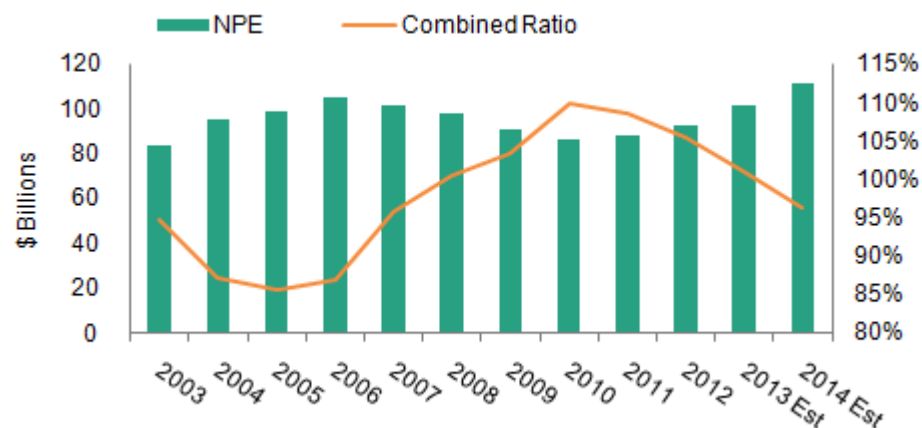


# Commercial Lines: Favorable Pricing and Ample Capital

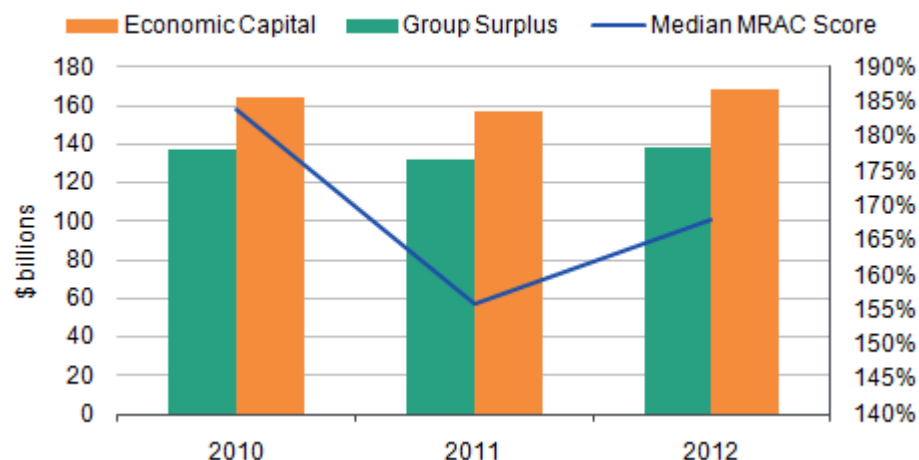
- » Price discipline will push commercial casualty underwriting profitability into favorable territory
- » Each percent increase in investment yield is equivalent to about five combined ratio points for four long tail casualty lines
- » Capital supporting risks remains ample, risk adjusted capital adequacy remains solid
- » Enhanced risk selection and capital management narrow the amplitude of the pricing cycle

Source : Moody's, SNL Financial LC. Contains Copyrighted And Trade Secret Materials Distributed Under License From SNL, For Recipient's Internal Use Only

## Major Commercial Casualty Lines' Profitability



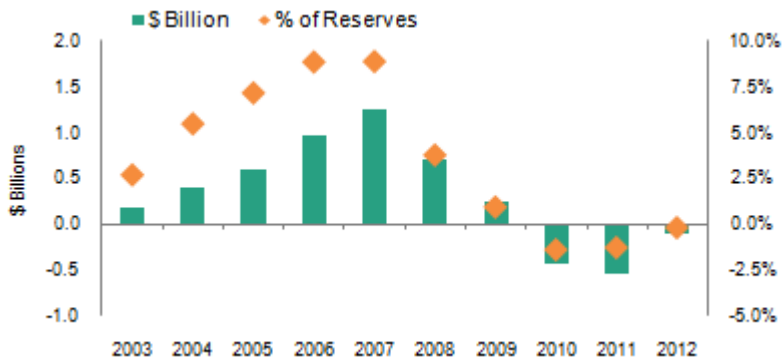
## Capital Adequacy of Rated Commercial Carriers



# Commercial Casualty Reserve Profile

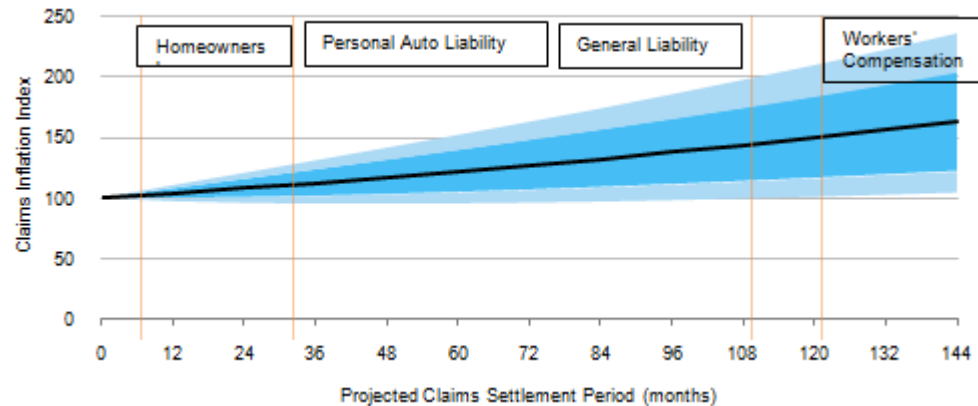
## Commercial Liability Lines

Reserve Position by Accident Year

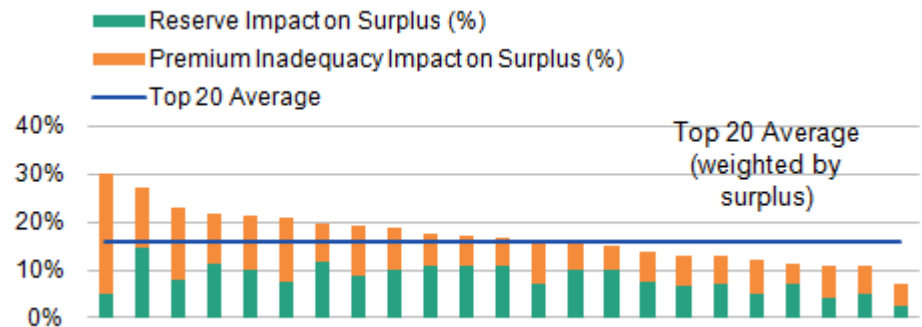


- » Reserves still redundant overall, but with diminishing redundancies to boost future earnings
- » The margin for error to cushion reserve volatility has narrowed
- » Inflation risk not a current threat, but a significant long-term risk

## Build-up of Forecast Error in Claims Inflation for Long-tail Reserves



## US Top 20: Adverse Surplus Impact of Unexpected Medical and Liability Claims Inflation



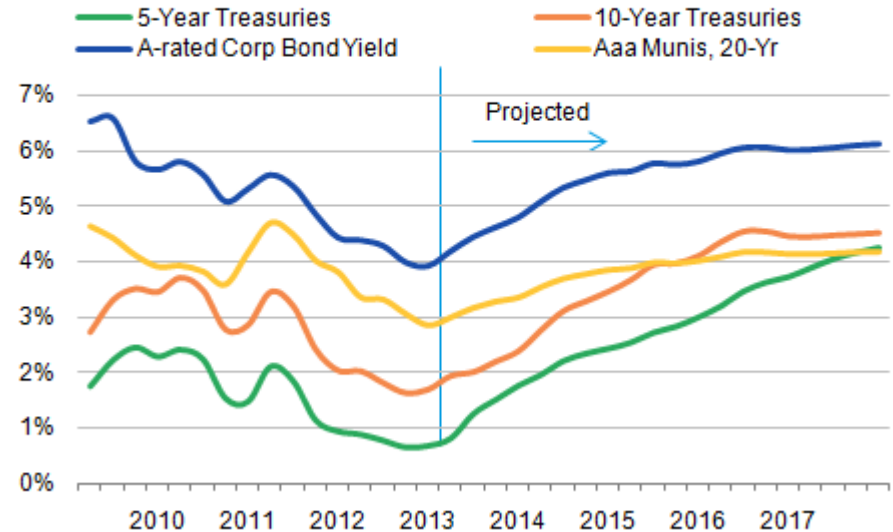
Source : Moody's, SNL Financial LC. Contains Copyrighted And Trade Secret Materials Distributed Under License From SNL - For Recipient's Internal Use Only



# Sensitivity to Interest Rates - Rising Yield Scenario

- » Publicly traded rated P&C companies have a medium duration of 4.0 and weighted average duration of 4.3
- » We estimate that each 100 bp rate rise will cause a \$40 billion market value loss (7% of surplus) offset to a degree by higher investment income
- » Strong liquidity at insurance operating companies, the practice of holding bonds long term, and the unlikely need to liquidate investment portfolios, moderates the risk of market value declines.
- » Sharp interest rate spike coupled with unexpected increase in claims inflation could be problematic for insurers

## Moody's Central Economic Scenario Forecast



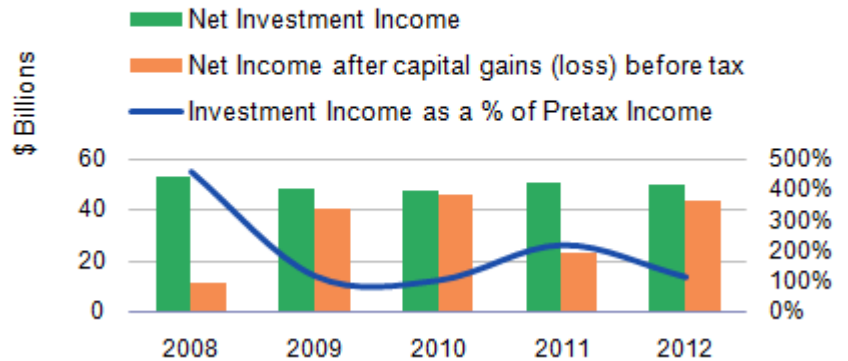
Date	Estimated Effective Duration	Total Fixed Income Investments (\$ billions)	Total Surplus (\$ billions)	80 BP Interest Rate Rise	ESTIMATED INDUSTRY LOSS FOR:		EST. LOSS AS A % OF EQUITY OF EQUITY (STAT SURPLUS):	
					100 BP Interest Rate Rise	80 BP Interest Rate Rise	100 BP Interest Rate Rise	80 BP Interest Rate Rise
12/31/2012	4.3	903	598	31	39	5%	7%	
12/31/2011	4.5	902	562	32	41	6%	7%	

Source : Moody's, SNL Financial LC. Contains Copyrighted And Trade Secret Materials Distributed Under License From SNL, For Recipient's Internal Use Only

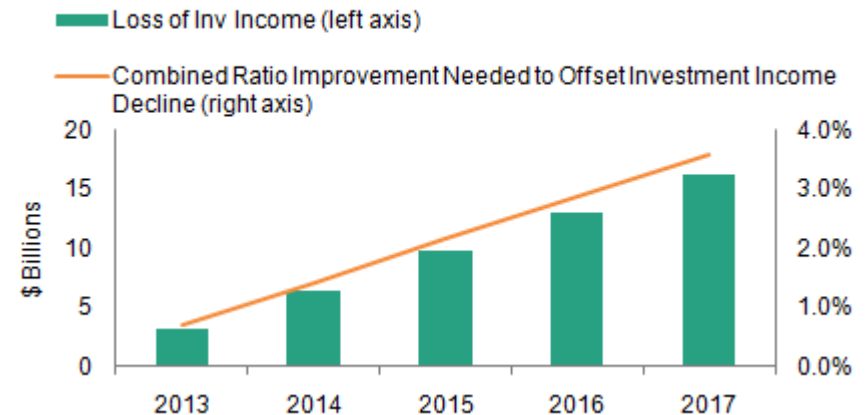
# Sensitivity to Interest Rates - Low Yield Scenario

- » Investment income makes up more than 100% of total pretax income.
- » We estimate that average new money rates were about 2.4% during Q1 2013 based on current bond allocations.
- » Using conservative assumptions, if rates were to return and continue at these levels, the impact would be a \$16 billion decline in annual industry investment income by 2017.
- » The industry's combined ratio would need to decline by about 3.6 percentage points to make up for this projected loss in investment income over the next five years.

## Contribution of Investment Income to Earnings



## Investment Income vs. Combined Ratio



Optional contact information  
or office address here



© 2013 Moody's Investors Service, Inc. and/or its licensors and affiliates (collectively, "MOODY'S"). All rights reserved.

CREDIT RATINGS ISSUED BY MOODY'S INVESTORS SERVICE, INC. ("MIS") AND ITS AFFILIATES ARE MOODY'S CURRENT OPINIONS OF THE RELATIVE FUTURE CREDIT RISK OF ENTITIES, CREDIT COMMITMENTS, OR DEBT OR DEBT-LIKE SECURITIES, AND CREDIT RATINGS AND RESEARCH PUBLICATIONS PUBLISHED BY MOODY'S ("MOODY'S PUBLICATIONS") MAY INCLUDE MOODY'S CURRENT OPINIONS OF THE RELATIVE FUTURE CREDIT RISK OF ENTITIES, CREDIT COMMITMENTS, OR DEBT OR DEBT-LIKE SECURITIES. MOODY'S DEFINES CREDIT RISK AS THE RISK THAT AN ENTITY MAY NOT MEET ITS CONTRACTUAL, FINANCIAL OBLIGATIONS AS THEY COME DUE AND ANY ESTIMATED FINANCIAL LOSS IN THE EVENT OF DEFAULT. CREDIT RATINGS DO NOT ADDRESS ANY OTHER RISK, INCLUDING BUT NOT LIMITED TO: LIQUIDITY RISK, MARKET VALUE RISK, OR PRICE VOLATILITY. CREDIT RATINGS AND MOODY'S OPINIONS INCLUDED IN MOODY'S PUBLICATIONS ARE NOT STATEMENTS OF CURRENT OR HISTORICAL FACT. CREDIT RATINGS AND MOODY'S PUBLICATIONS DO NOT CONSTITUTE OR PROVIDE INVESTMENT OR FINANCIAL ADVICE, AND CREDIT RATINGS AND MOODY'S PUBLICATIONS ARE NOT AND DO NOT PROVIDE RECOMMENDATIONS TO PURCHASE, SELL, OR HOLD PARTICULAR SECURITIES. NEITHER CREDIT RATINGS NOR MOODY'S PUBLICATIONS COMMENT ON THE SUITABILITY OF AN INVESTMENT FOR ANY PARTICULAR INVESTOR. MOODY'S ISSUES ITS CREDIT RATINGS AND PUBLISHES MOODY'S PUBLICATIONS WITH THE EXPECTATION AND UNDERSTANDING THAT EACH INVESTOR WILL MAKE ITS OWN STUDY AND EVALUATION OF EACH SECURITY THAT IS UNDER CONSIDERATION FOR PURCHASE, HOLDING, OR SALE.

ALL INFORMATION CONTAINED HEREIN IS PROTECTED BY LAW, INCLUDING BUT NOT LIMITED TO, COPYRIGHT LAW, AND NONE OF SUCH INFORMATION MAY BE COPIED OR OTHERWISE REPRODUCED, REPACKAGED, FURTHER TRANSMITTED, TRANSFERRED, DISSEMINATED, REDISTRIBUTED OR RESOLD, OR STORED FOR SUBSEQUENT USE FOR ANY SUCH PURPOSE, IN WHOLE OR IN PART, IN ANY FORM OR MANNER OR BY ANY MEANS WHATSOEVER, BY ANY PERSON WITHOUT MOODY'S PRIOR WRITTEN CONSENT.

All information contained herein is obtained by MOODY'S from sources believed by it to be accurate and reliable. Because of the possibility of human or mechanical error as well as other factors, however, all information contained herein is provided "AS IS" without warranty of any kind. MOODY'S adopts all necessary measures so that the information it uses in assigning a credit rating is of sufficient quality and from sources MOODY'S considers to be reliable including, when appropriate, independent third-party sources. However, MOODY'S is not an auditor and cannot in every instance independently verify or validate information received in the rating process. Under no circumstances shall MOODY'S have any liability to any person or entity for (a) any loss or damage in whole or in part caused by, resulting from, or relating to, any error (negligent or otherwise) or other circumstance or contingency within or outside the control of MOODY'S or any of its directors, officers, employees or agents in connection with the procurement, collection, compilation, analysis, interpretation, communication, publication or delivery of any such information, or (b) any direct, indirect, special, consequential, compensatory or incidental damages whatsoever (including without limitation, lost profits), even if MOODY'S is advised in advance of the possibility of such damages, resulting from the use of or inability to use, any such information. The ratings, financial reporting analysis, projections, and other observations, if any, constituting part of the information contained herein are, and must be construed solely as, statements of opinion and not statements of fact or recommendations to purchase, sell or hold any securities. Each user of the information contained herein must make its own study and evaluation of each security it may consider purchasing, holding or selling.

NO WARRANTY, EXPRESS OR IMPLIED, AS TO THE ACCURACY, TIMELINESS, COMPLETENESS, MERCHANTABILITY OR FITNESS FOR ANY PARTICULAR PURPOSE OF ANY SUCH RATING OR OTHER OPINION OR INFORMATION IS GIVEN OR MADE BY MOODY'S IN ANY FORM OR MANNER WHATSOEVER.

MIS, a wholly-owned credit rating agency subsidiary of Moody's Corporation ("MCO"), hereby discloses that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by MIS have, prior to assignment of any rating, agreed to pay to MIS for appraisal and rating services rendered by it fees ranging from \$1,500 to approximately \$2,500,000. MCO and MIS also maintain policies and procedures to address the independence of MIS's ratings and rating processes. Information regarding certain affiliations that may exist between directors of MCO and rated entities, and between entities who hold ratings from MIS and have also publicly reported to the SEC an ownership interest in MCO of more than 5%, is posted annually at [www.moody.com](http://www.moody.com) under the heading "Shareholder Relations — Corporate Governance — Director and Shareholder Affiliation Policy."

For Australia only: Any publication into Australia of this document is pursuant to the Australian Financial Services License of MOODY'S affiliate, Moody's Investors Service Pty Limited ABN 61 003 399 657 AFSL 336969 and/or Moody's Analytics Australia Pty Ltd ABN 94 105 136 972 AFSL 383569 (as applicable). This document is intended to be provided only to "wholesale clients" within the meaning of section 761G of the Corporations Act 2001. By continuing to access this document from within Australia, you represent to MOODY'S that you are, or are accessing the document as a representative of, a "wholesale client" and that neither you nor the entity you represent will directly or indirectly disseminate this document or its contents to "retail clients" within the meaning of section 761G of the Corporations Act 2001. MOODY'S credit rating is an opinion as to the creditworthiness of a debt obligation of the issuer, not on the equity securities of the issuer or any form of security that is available to retail clients. It would be dangerous for retail clients to make any investment decision based on MOODY'S credit rating. If in doubt you should contact your financial or other professional adviser.