

CASE Atlanta

State of the Reinsurance Market

James Hole

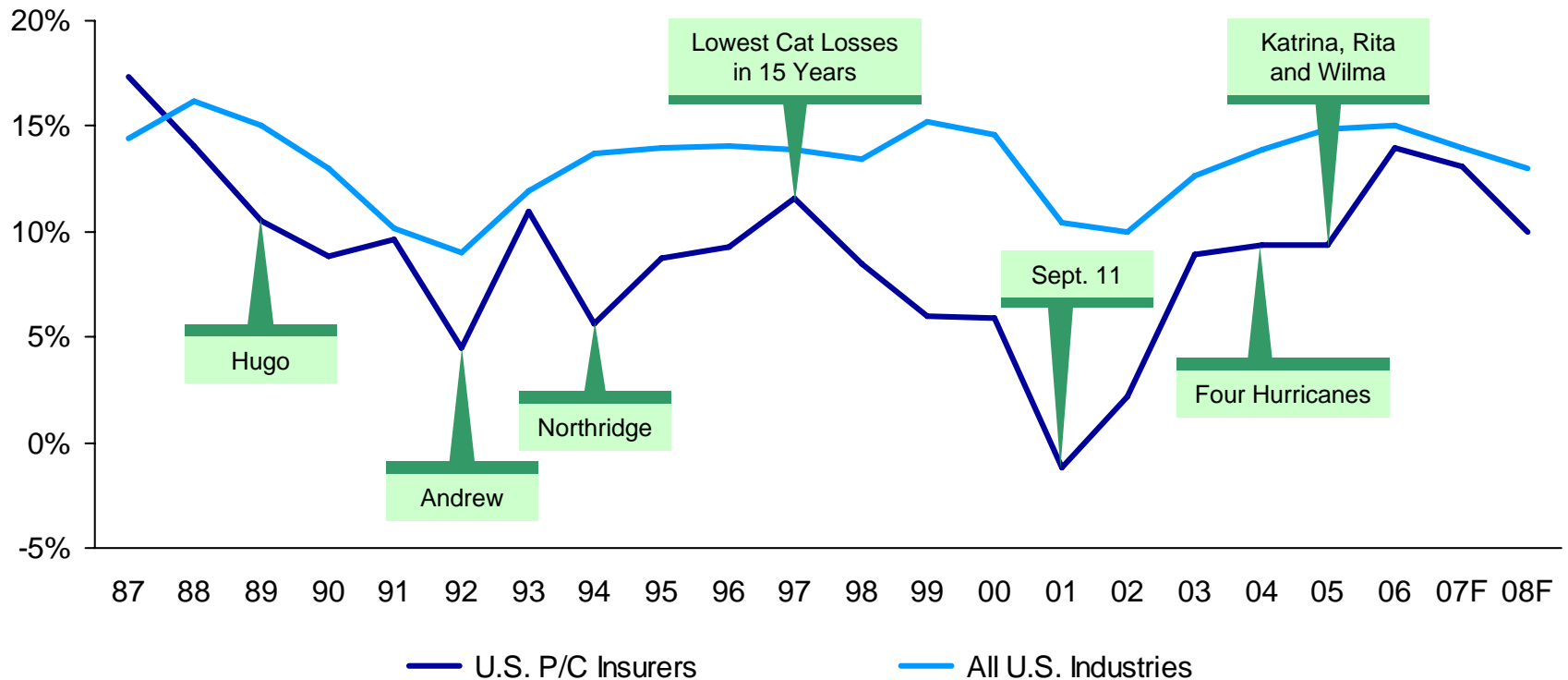
September 2008

State of the Reinsurance Market

- **P/C profitability and the resultant soft market**
- New capacity and the supply/demand equation
- Capital management
- Rating agencies and ERM
- 2008 catastrophe activity
- Florida and other notable legislative actions
- Outlook for 2008 – 2009

P/C ROE vs. all industries

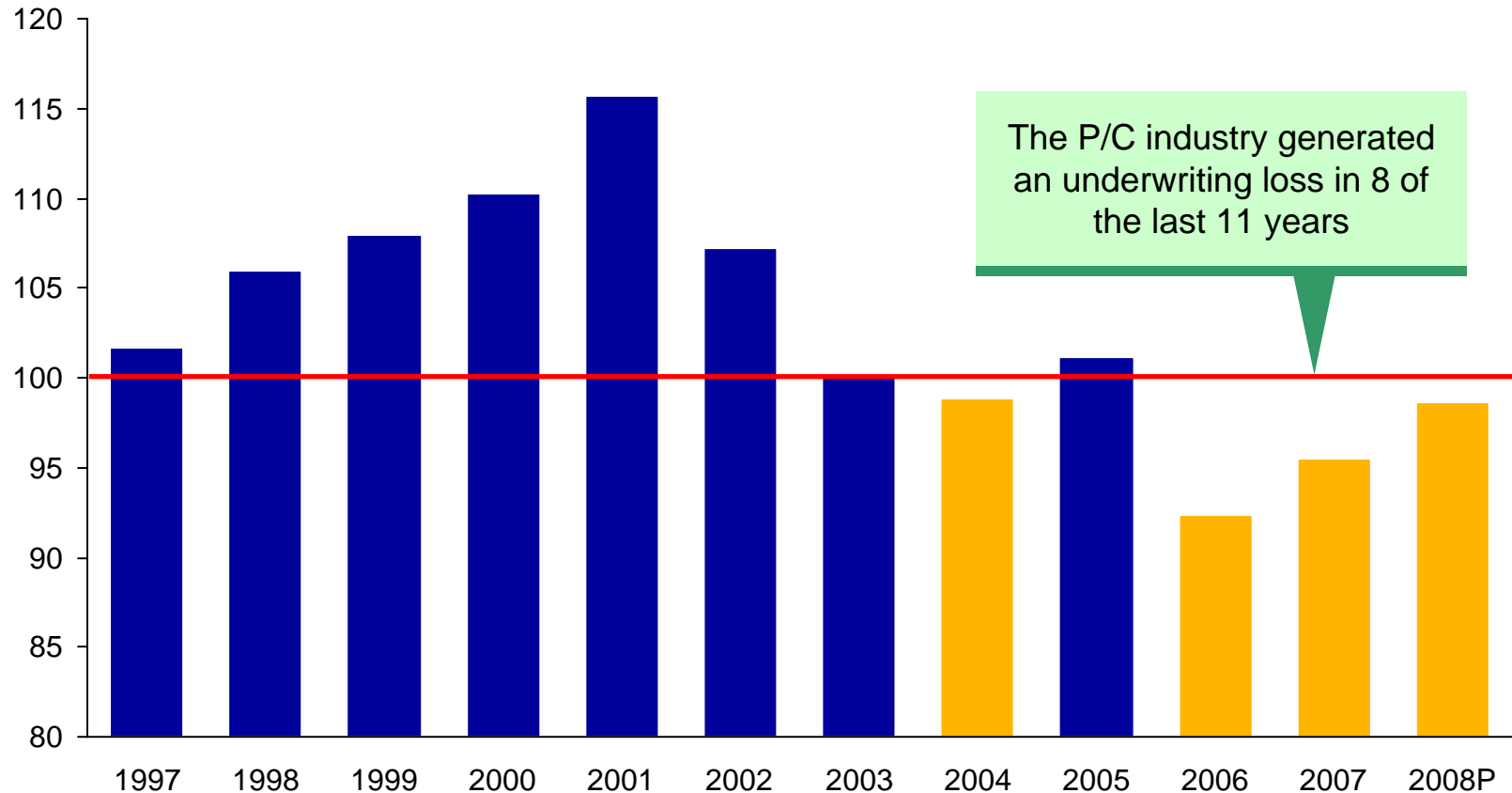
P/C Profit is Cyclical, Volatile and Vulnerable



Source: Insurance Information Institute.

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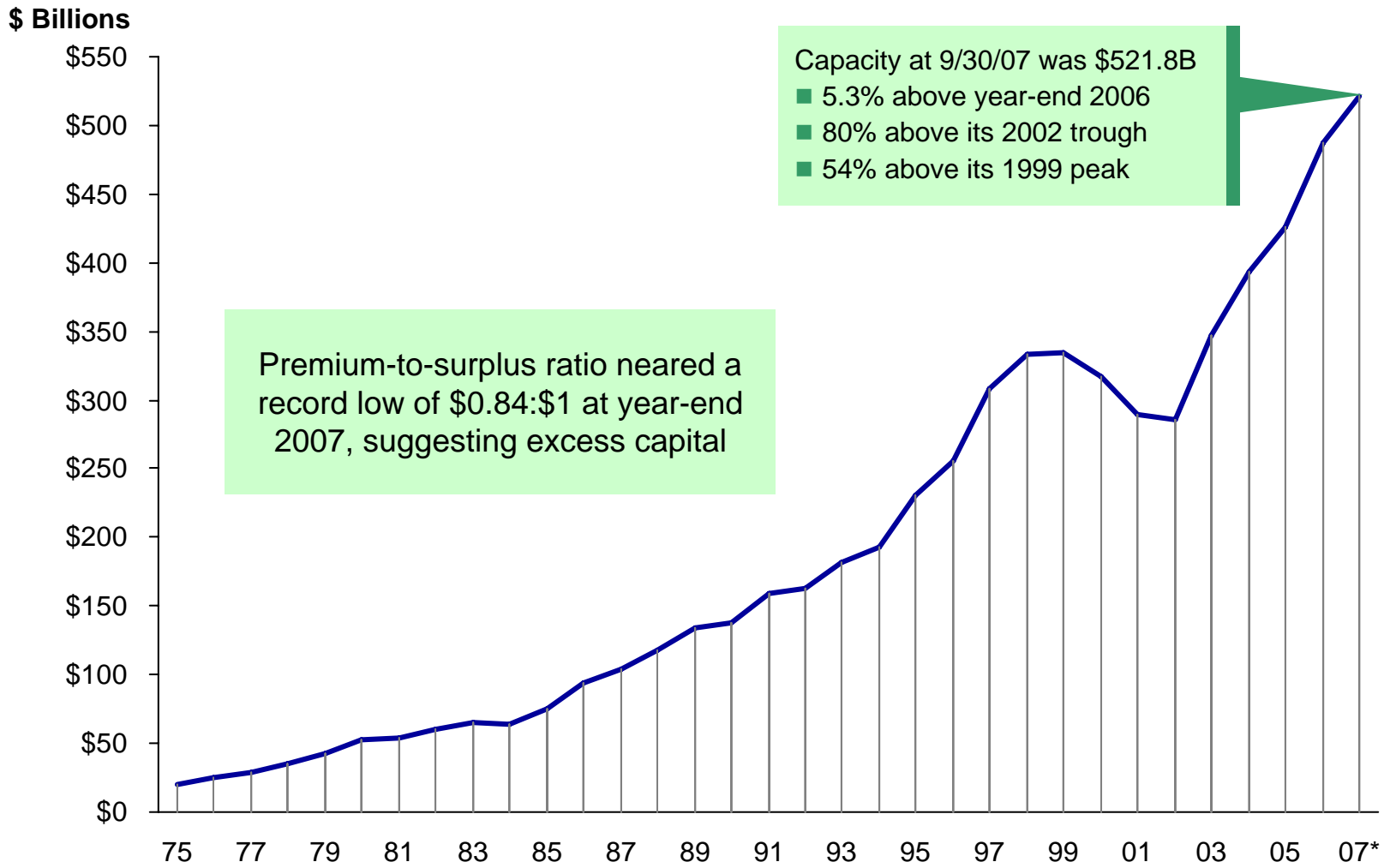
P/C combined ratios — 1997 - 2008P



Source: Towers Perrin, A.M. Best.

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P/C insurance: Surplus trends



* As of September 30, 2007.

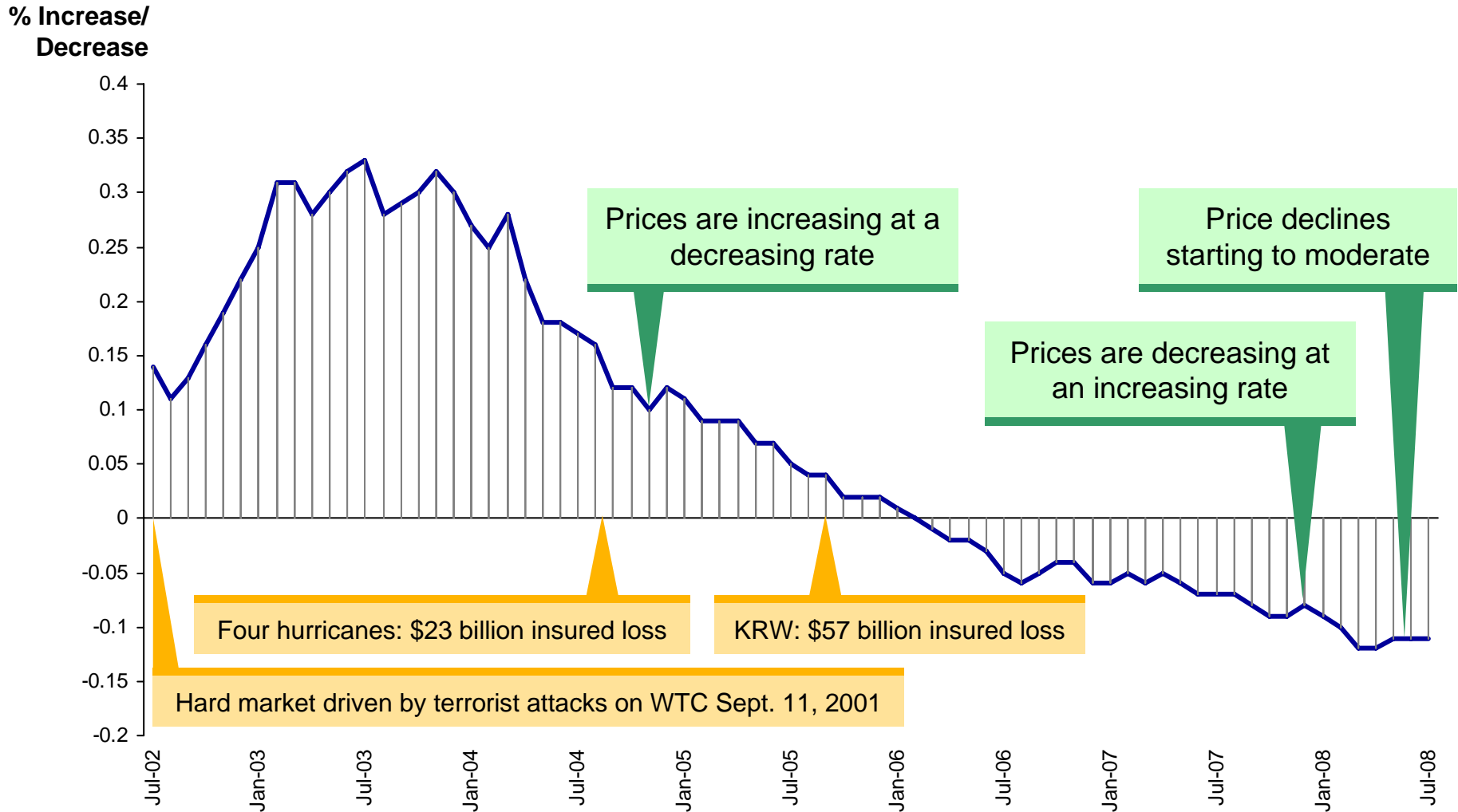
Source: A.M. Best, ISO, Insurance Information Institute.

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The P/C soft market phase accelerates

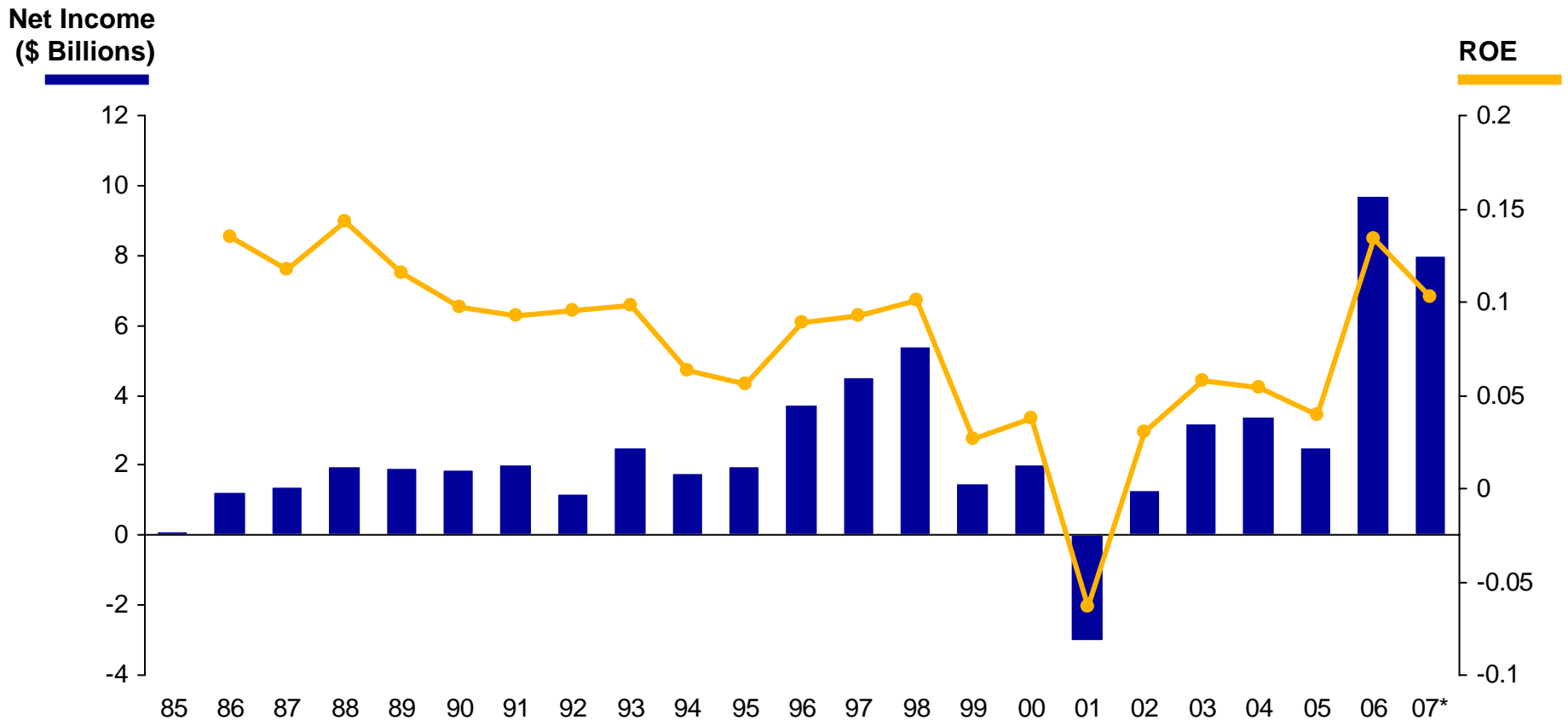


Source: Market Scout, ISO, Towers Perrin.

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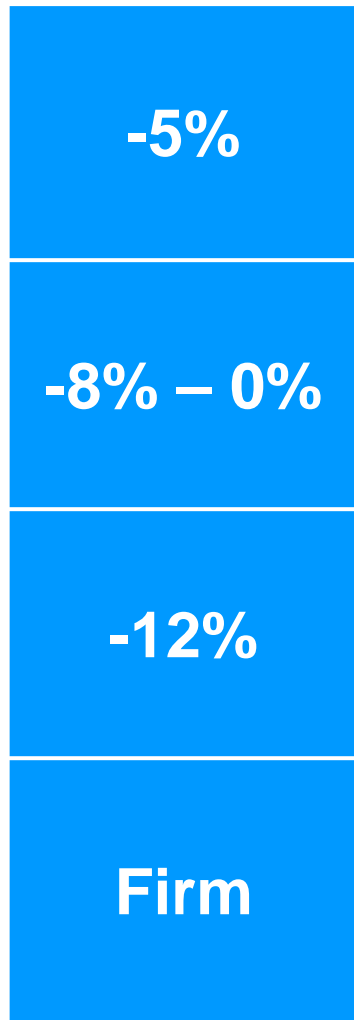
U.S. reinsurer net income and ROE 1985 – 2007*

Reinsurer Profitability Rebounded Post-Katrina, But is Now Falling



*2007 ROE figure is III estimate based return on average 2007 surplus.
Source: Reinsurance Association of America.

Signs of a soft reinsurance market

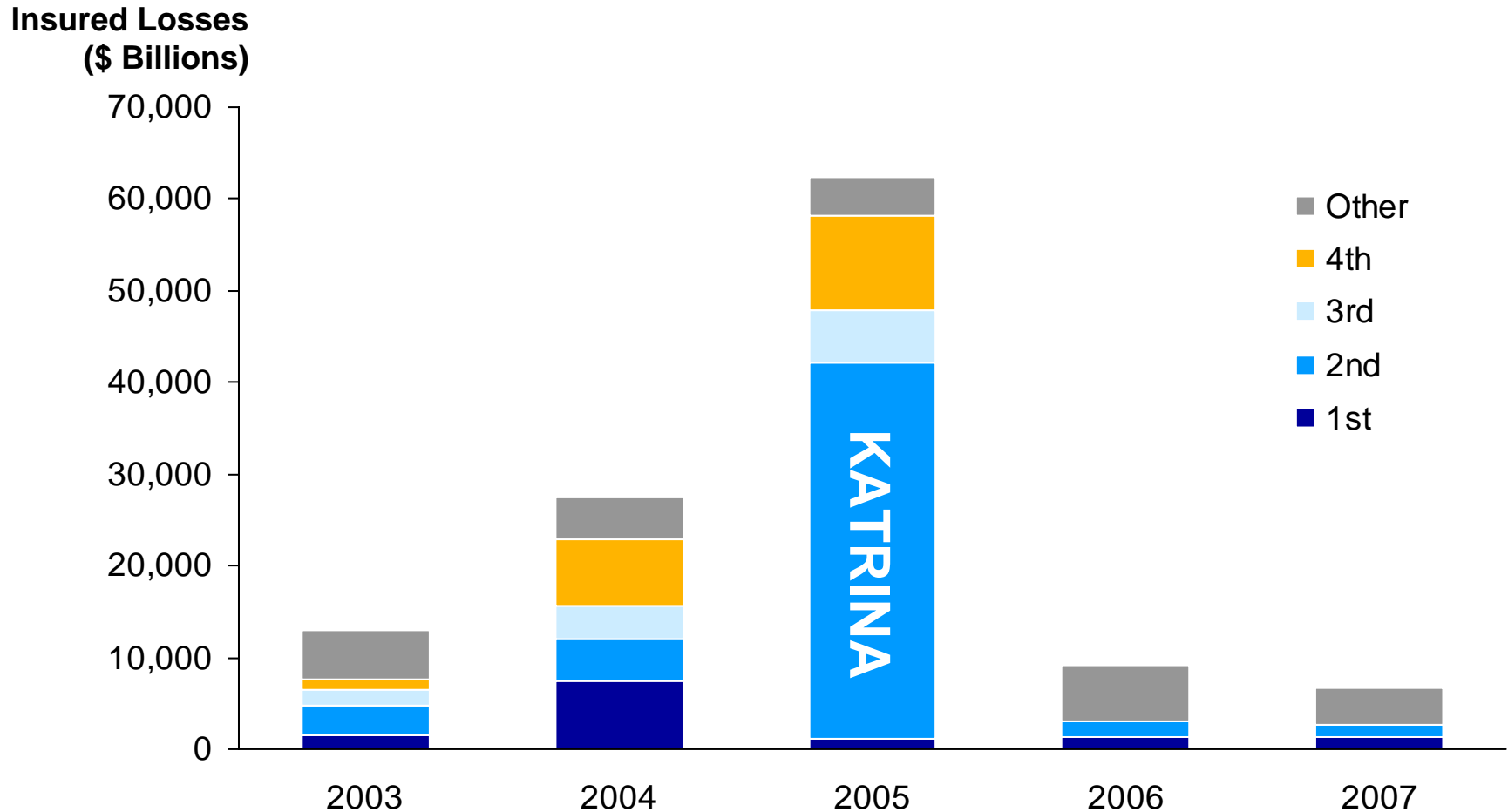


- Average price reduction on a risk-adjusted basis, high variation around mean
- Range of price changes for major global reinsurance markets
- Net reduction in premiums for Swiss Re; claims it turned away underpriced business — i.e., < 14% ROE
 - The question is, who picked it up?
- Reinsurers claim that they've held the line on terms and conditions

Source: S&P: 2008 Reinsurance Renewals: Underwriting Discipline Takes Center Stage As Price Adequacy Declines Further.

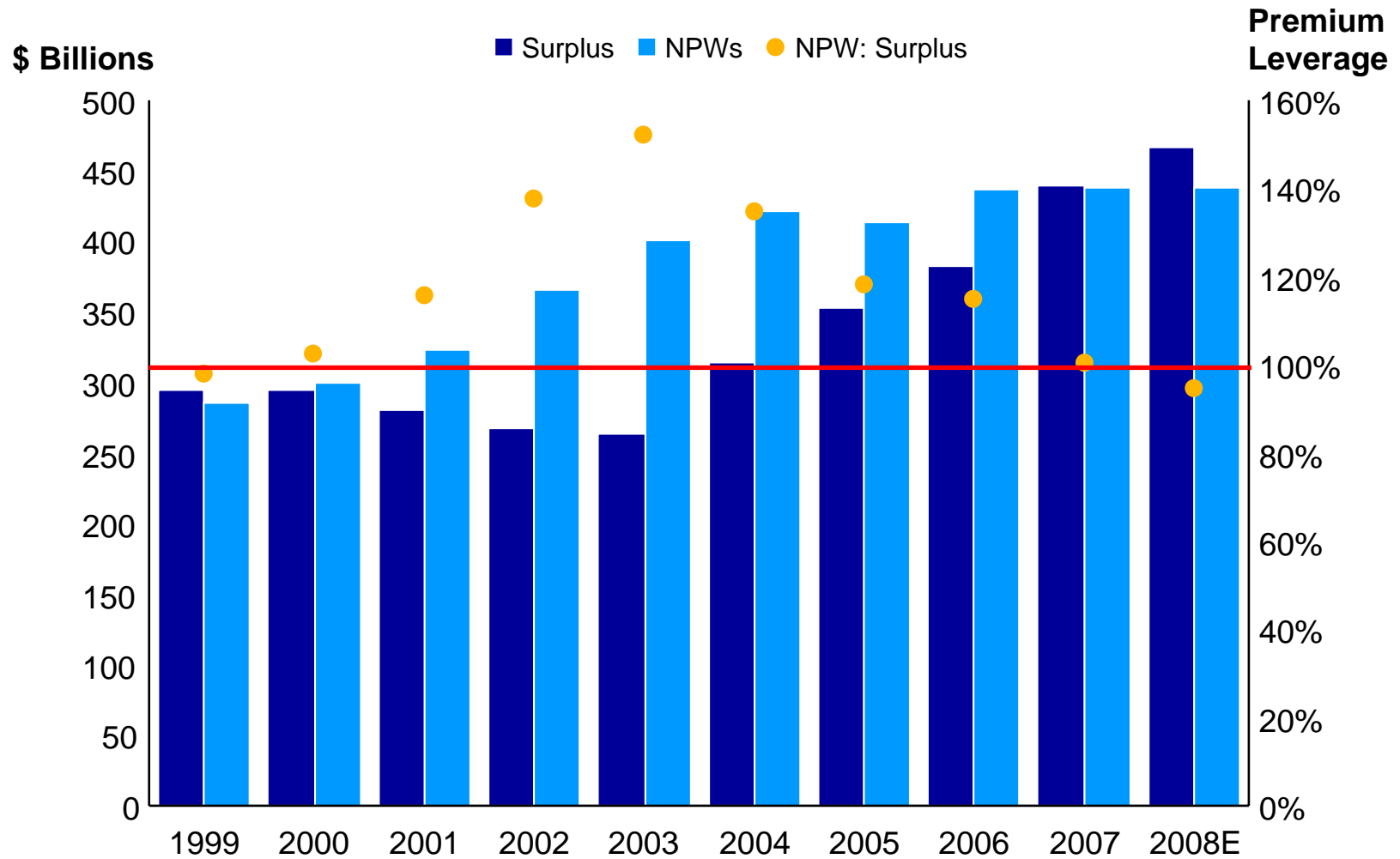
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Benign cat years in 2006 and 2007 = strong reinsurer balance sheets



Note: Each layer represents a major catastrophe with insured losses > \$1B. Other includes all cat events < \$1B.
Source: ISO PCS, Towers Perrin.

Analysts estimate U.S. P/C reinsurance industry is overcapitalized by \$100 – \$150B



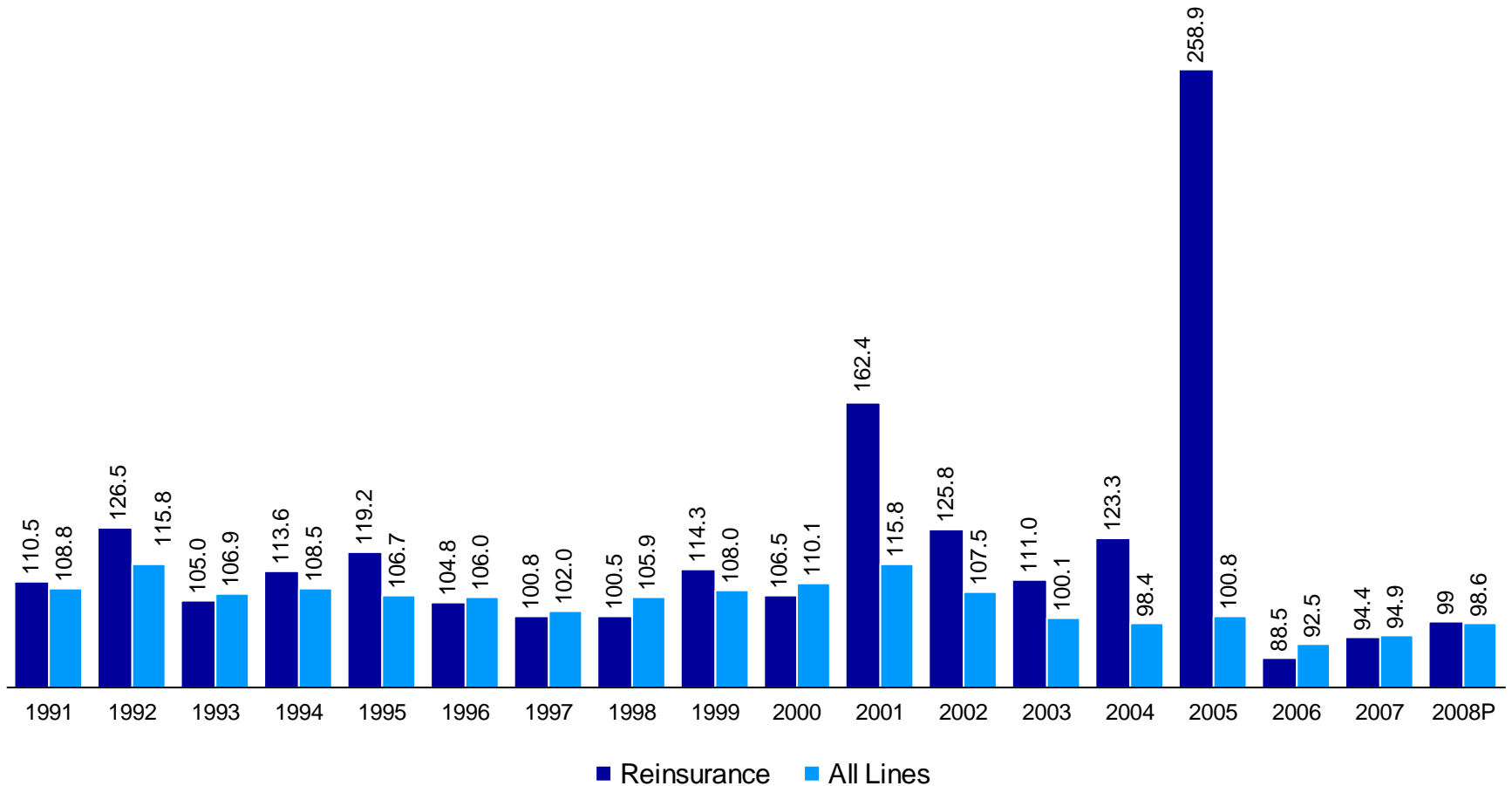
Note: Surplus & Premium does not include National Indemnity.
 Source: A.M. Best, Dowling & Partners, ISO.

What's driving reinsurers to hold more capital?

- Recalibrated catastrophe models (RMS/AIR)
- Rating agencies = more stringent capital models
- Uncertainty/fear
 - Catastrophe
 - Will 2008 be another 2004 or 2005 cat year?
 - Tight credit markets
 - Will I be able to raise capital after big loss?
- Loss cost inflation
 - Barrel of oil >\$100
 - Steel/building materials

U.S. reinsurers: Greater volatility than P/C industry

Combined Ratio (%)



Source: A.M. Best.

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Will this soft cycle be different?

Positive Factors

Investment Gains	■ Sharp stock price declines and falling interest rates will drive portfolio yields down and contribute to U/W discipline
Sarbanes-Oxley	■ SOX should lead to better financial management; rapid recognition of deficient or redundant reserves
Rating Agencies	■ Focused on cycle management and ERM; quicker to downgrade
Information Systems	■ Better tools enable management to more quickly identify and make adjustments to price, underwriting and changing market conditions
Analysts/Investors	■ Less fixated on growth, more on ROE through soft market

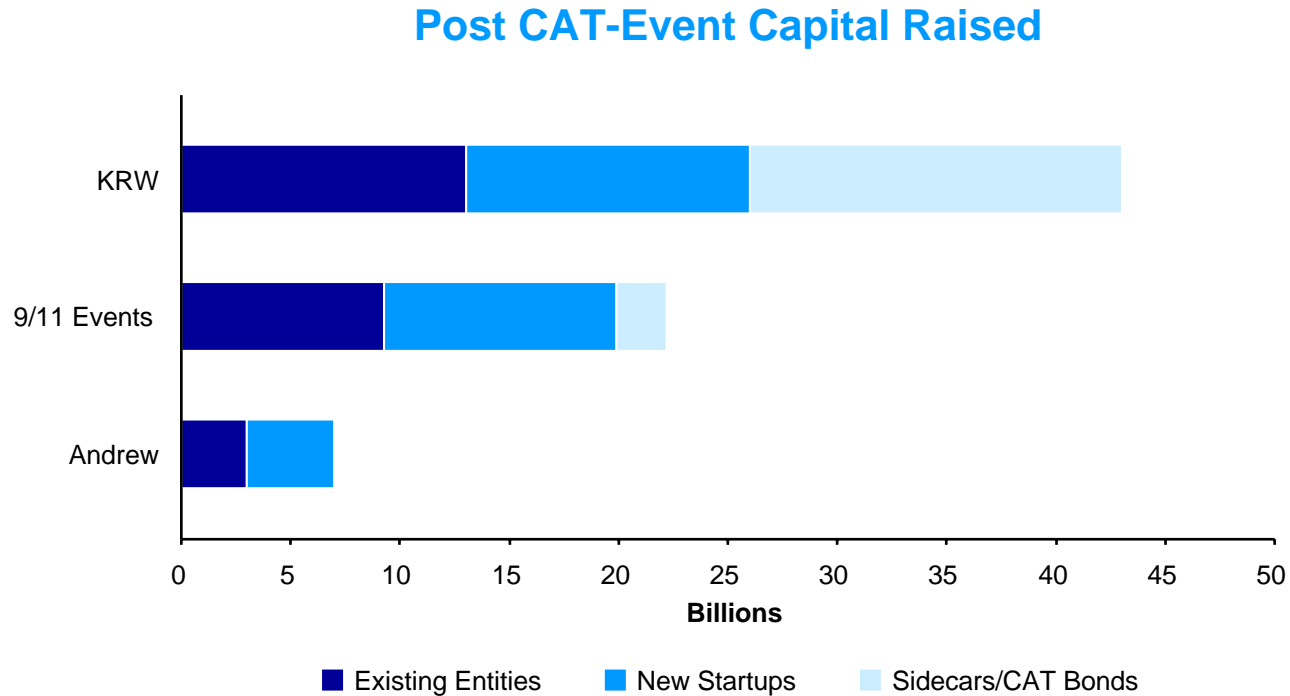
Negative Factors

Capacity	■ Excess capital will likely lead to increased price competition and a liberalization of terms and conditions
Reserves	■ Reserves are in best shape in decades, with releases diminishing in 2008 and 2009, which could extend the depth and length of cycle

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Post cat-event capital raised



	Andrew	9/11 Events	KRW
New Capital Raised	\$7.0B	\$22.2B	\$43.0B
Estimated Loss Industrywide	\$15.5B	\$37.0B	\$57.9B
Capital % of Estimated Loss	45.2%	59.9%	74.3%

Source: Reinsurance Association of America.

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New reinsurers: Post-KRW

Company	Estimated Capital (\$MM)	Lead Investors
Aeolus Re	500	Warburg Pincus, Peter Appel, et al.
Amlin Bermuda	1,000	Amlin
Ariel Re	1,000	Kramer, Blackstone, Texas Pacific, et al.
Arrow Capital	102	Goldman Sachs
Flagstone Re	552	Lehman Bros., Haverford
Harbor Point Re	502	Chubb Inc., Stone Point Capital
Hiscox Bermuda	502	Hiscox plc
Lancashire	1,065	Capital Z, Crestview, Cypress et al.
New Castle Re	500	Citadel
Omega Specialty	150	Omega plc
Validus Re	1,000	Aquiline, Goldman, Merrill, Vestar
Total	7,871	

Source: Towers Perrin.

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Sidecars expiring in 2007

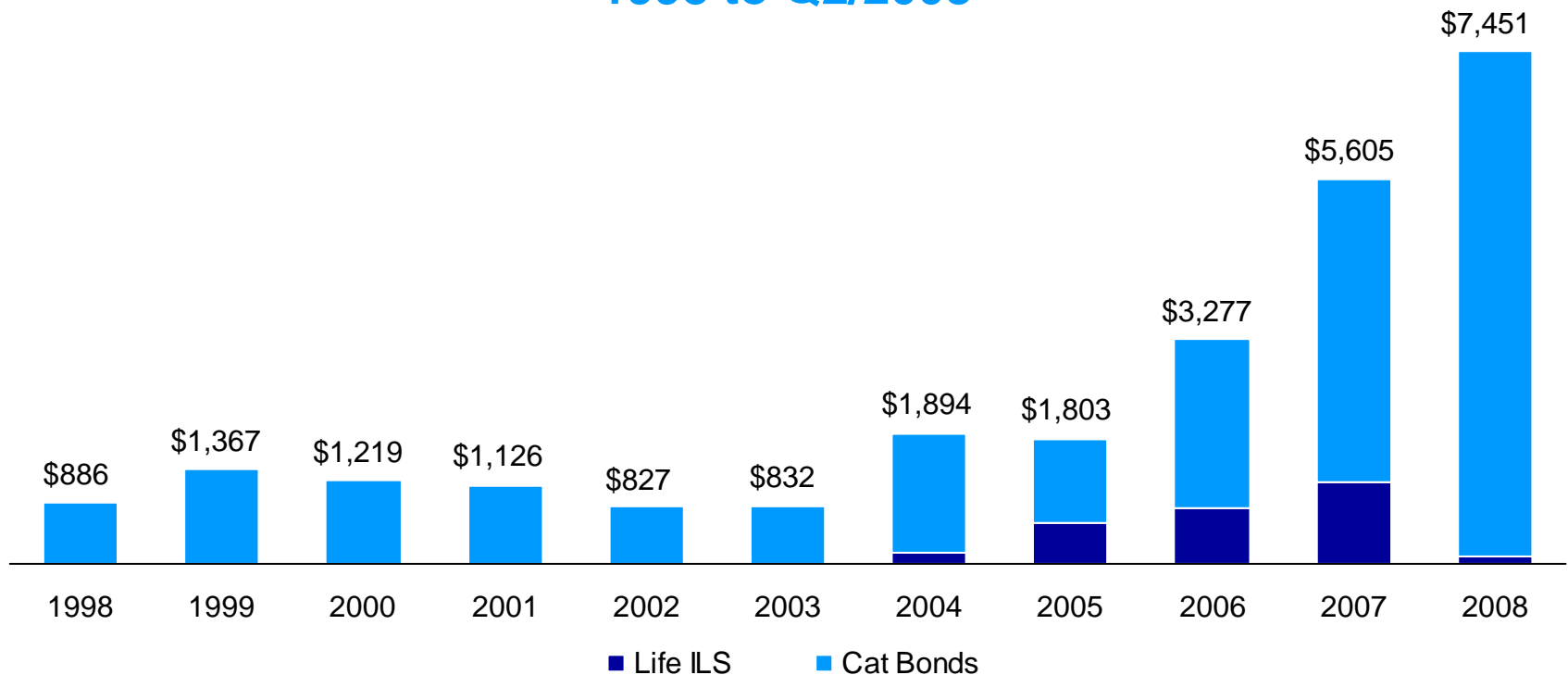
Issue Date	Vehicle	Sponsor	Capital Amount	Peril Type
11-07	Norton Re II Ltd.	Brit Insurance	118.2	Multiperil
11-07	Cyrus Re II Ltd.	XL Re	140.0	Multiperil: property
7-07	Mont Gele Re Ltd.	Flagstone Re	60.0	Multiperil; property, energy, marine, aviation, work comp
5-07	Emerson Re Ltd.	CIG Re/New Castle Re	500.0	Natural perils; predominantly personal insurance
5-07	Starbound Re II Ltd.	Renaissance Re	341.5	Florida wind
3-07	Kepler Holdings Ltd.	Hannover Re	200.0	Worldwide natural perils; segregated cell
1-07	Kaith Re Ltd.	Hannover Re	106.0	Multiperil
1-07	MaRI Ltd.	Marsh/ACE	400.0	U.S. commercial property
	Total		1,865.7	

Source: A.M. Best.

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Annual catastrophe bond transactions volume, 1997 – 2007

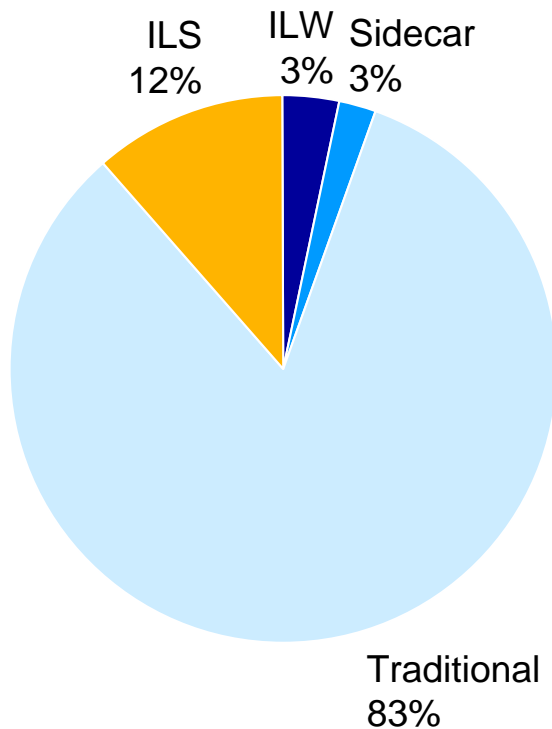
Total ILS Issuance Q1 to Q1 1998 to Q2/2008



Note: "Sidecar" transactions and certain life securitizations not included here; could add a further estimated \$4 billion to the combined 2006 and 3/2007 totals.

Source: Lane Financial, L.L.C.

The majority of reinsurance capital still comes from traditional sources



Source: Swiss Re.

20%

**Five-year compound
annual growth rate of
insurance-linked
securities**

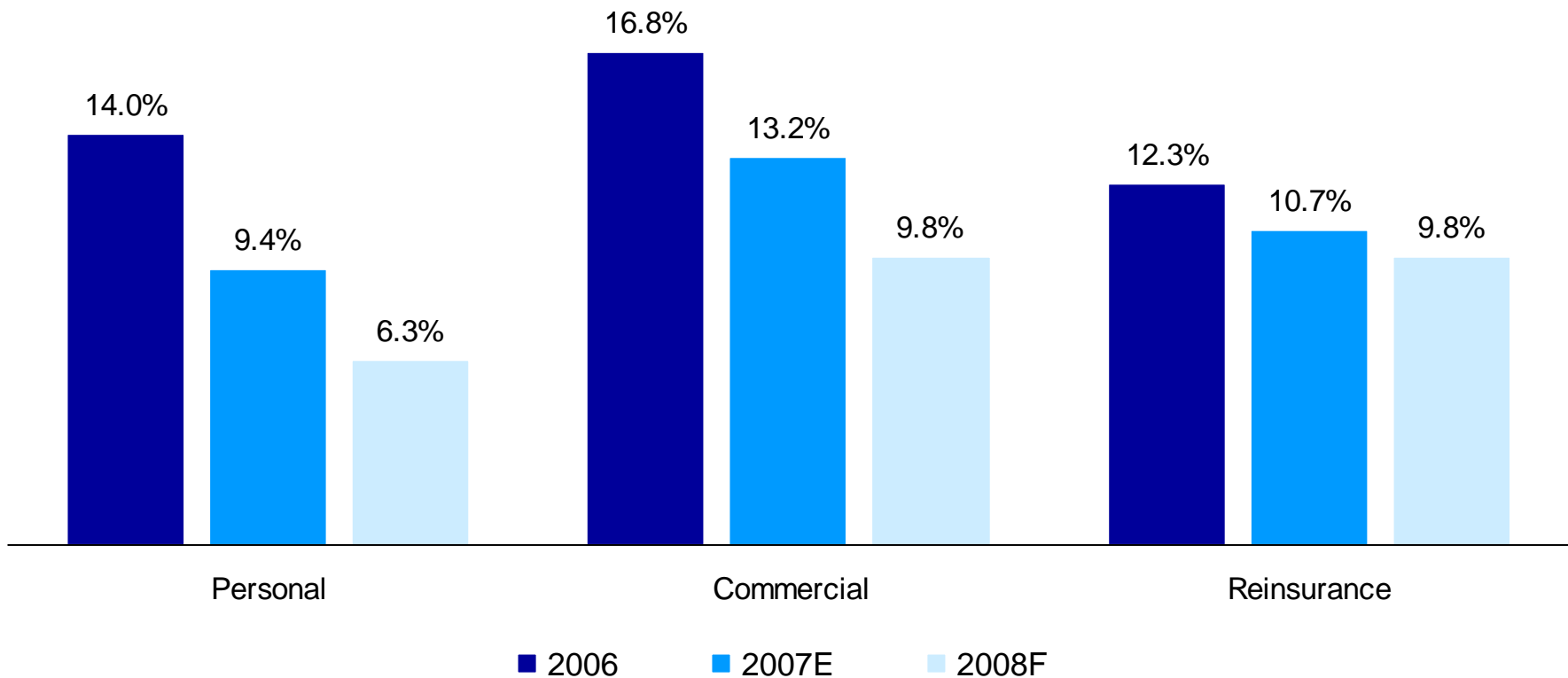
Source: Standard & Poor's.

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P/C insurance: ROEs by segment

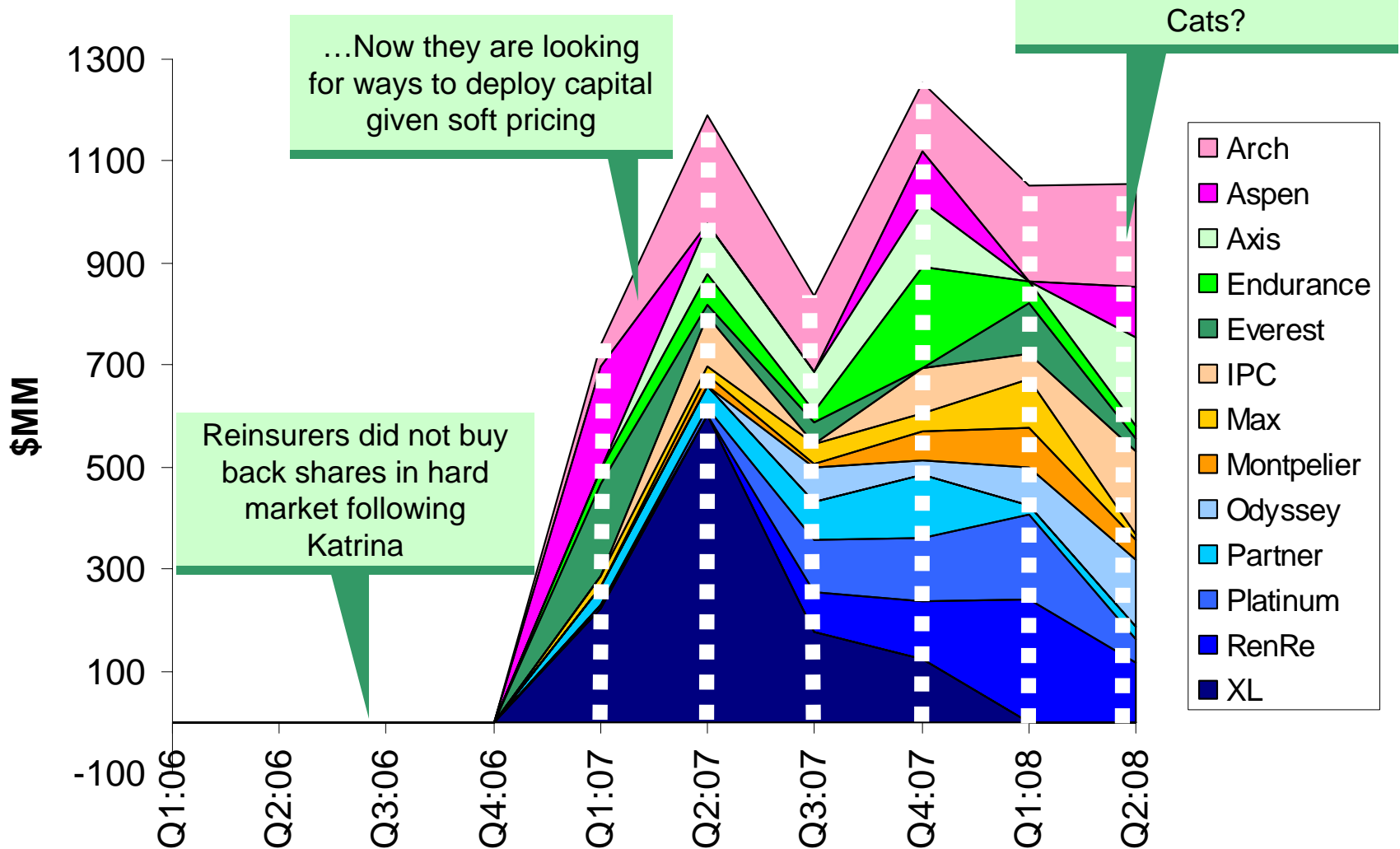
- ROEs declining as underwriting results deteriorate
- Rating agencies/investors demand stable cross-cycle ROEs



Source: A.M. Best Review & Preview (historical and forecast).

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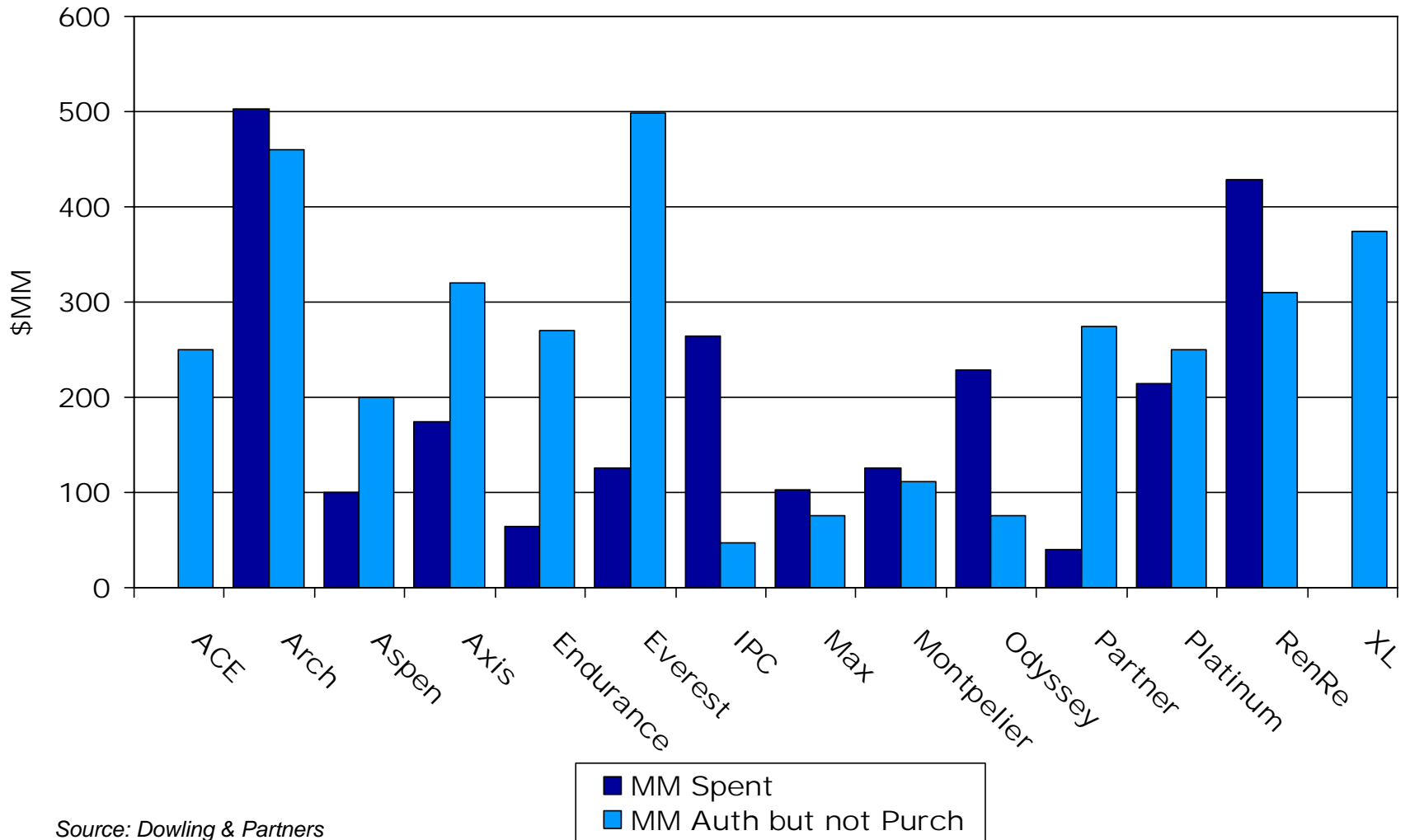
Reinsurer Buybacks Accelerate in Overcapitalized Environment



Source: Dowling & Partners

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Reinsurer Buybacks Completed in 2008



Source: Dowling & Partners

Acquisition/diversification

Bermuda to London

- Validus Re
- Talbot
- Ariel Re
- Atrium
- Montpelier
- Syndicate 5151

London to Bermuda

- Catlin
- Amlin
- Hiscox



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Reinsurer financial strength is paramount in a soft cycle

Rk	Reinsurer	2006	S&P Rating			ROE	
		Market Share	2001	2004	2007	2007	5 Year
1	Munich Re	18%	AAA	A+	AA-	15.5	9.8
2	Swiss Re*	17%	AAA	AA	AA-	10.5	10.6
3	Berkshire Hathaway Re	8%	AAA	AAA	AAA	12.2	18.7
4	Hannover Re	7%	AA+	AA-	AA-	22.0 [†]	15.1
5	Lloyd's	6%	A	A	A+	31.4 [†]	n/a
6	SCOR**	3%	AA-	BBB+	A-	15.4 [†]	-7.0
7	Reinsurance Grp of America, Inc.	3%	A	A-	A-	n/a	n/a
8	Everest Re	3%	AA-	AA-	AA-	25.2 [†]	10.2
9	PartnerRe	3%	AA	AA-	AA-	24.4 [†]	21.0
10	Transatlantic Holdings Inc.	3%	AA	AA	AA-	12.1	11.5

* Swiss Re acquired GE Insurance Solutions on June 9, 2006. Figures for Swiss Re are based on Swiss Re's published financials for 2006 and don't reflect GEIS's premium for the full year.

**2006 data includes consolidation of SCOR and Revios.

[†]2006 numbers.

Source: S&P 2007 Global Reinsurance Highlights.

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1	Munich Re	18%	A++	A+	A+	15.5	9.8
2	Swiss Re*	17%	A++	A+	A+	10.5	10.6
3	Berkshire Hathaway Re	8%	A++	A++	A++	12.2	18.7
4	Hannover Re	7%	A+	A	A	22.0 [†]	15.1
5	Lloyd's	6%	A-	A	A	31.4 [†]	n/a
6	SCOR*	3%	A+	B++	A-	15.4	-7.0
7	Reinsurance Grp of America, Inc.	3%	A+	A+	A+	n/a	n/a
8	Everest Re	3%	A+	A+	A+	25.2 [†]	10.2
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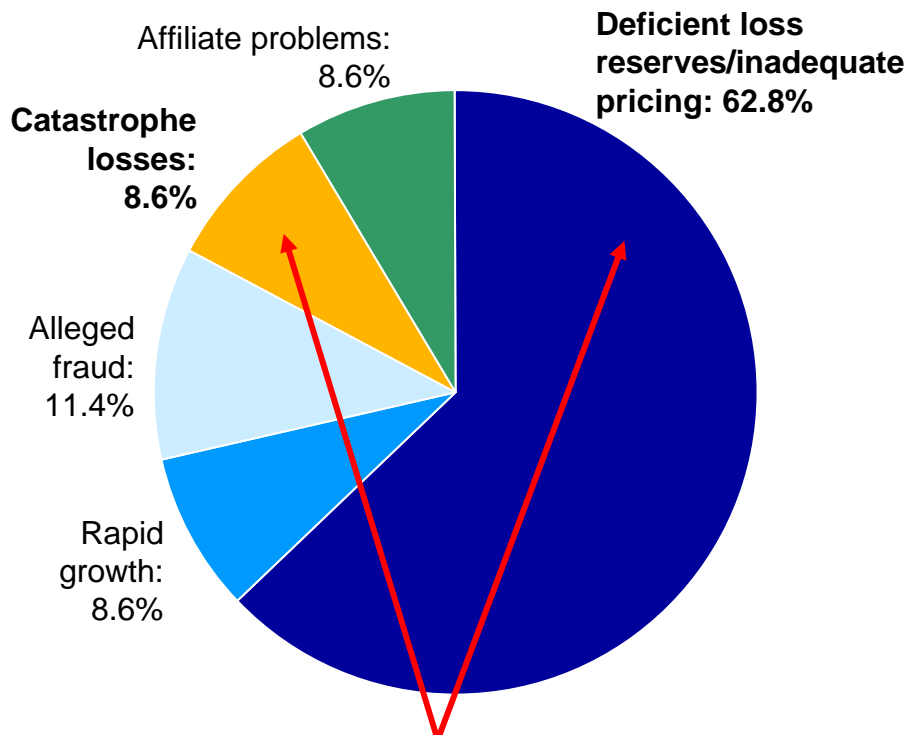
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Reinsurer failures in 2004 – 2005

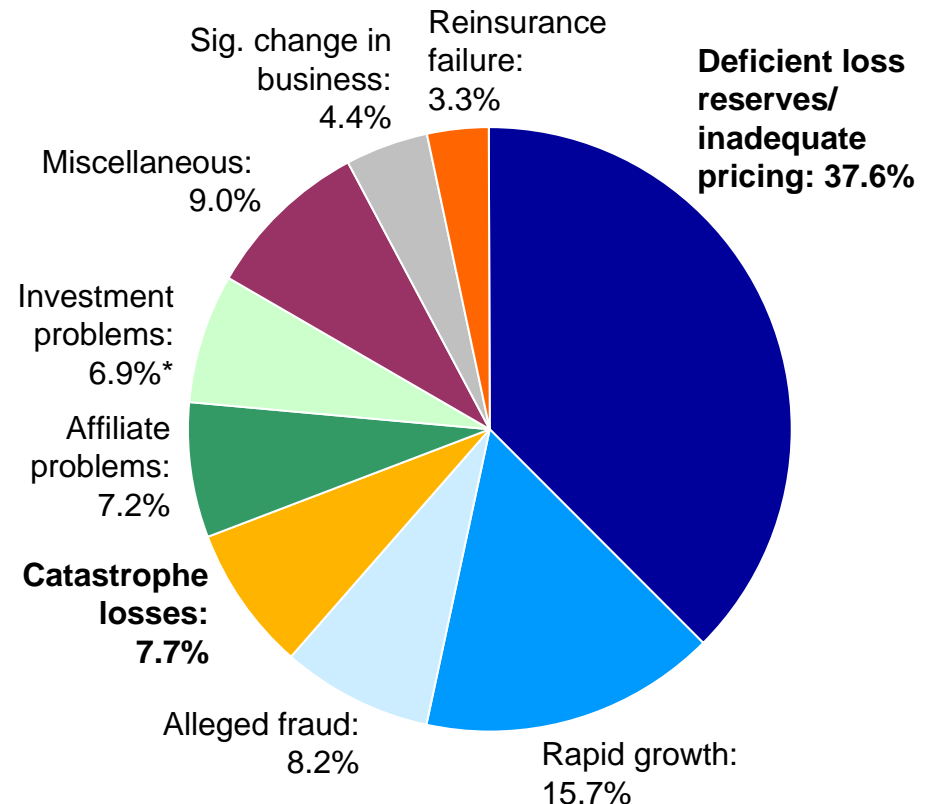
Reinsurer	A.M. Best Rating			
	2003	2004	2005	2006
PXRE Group Ltd.	A	A	A-	NR-4
Quanta Capital Holdings, Ltd.	A-	A-	A-	NR-4
Olympus Re	A-	A-	B+	NR-4
Alea Group Holdings	A-	A-	B++	NR-4
Western General	A	A	B++	NR-4

Reasons for U.S. P/C insurer impairments, 1969 – 2005/6

2003 – 2005



1969 – 2006

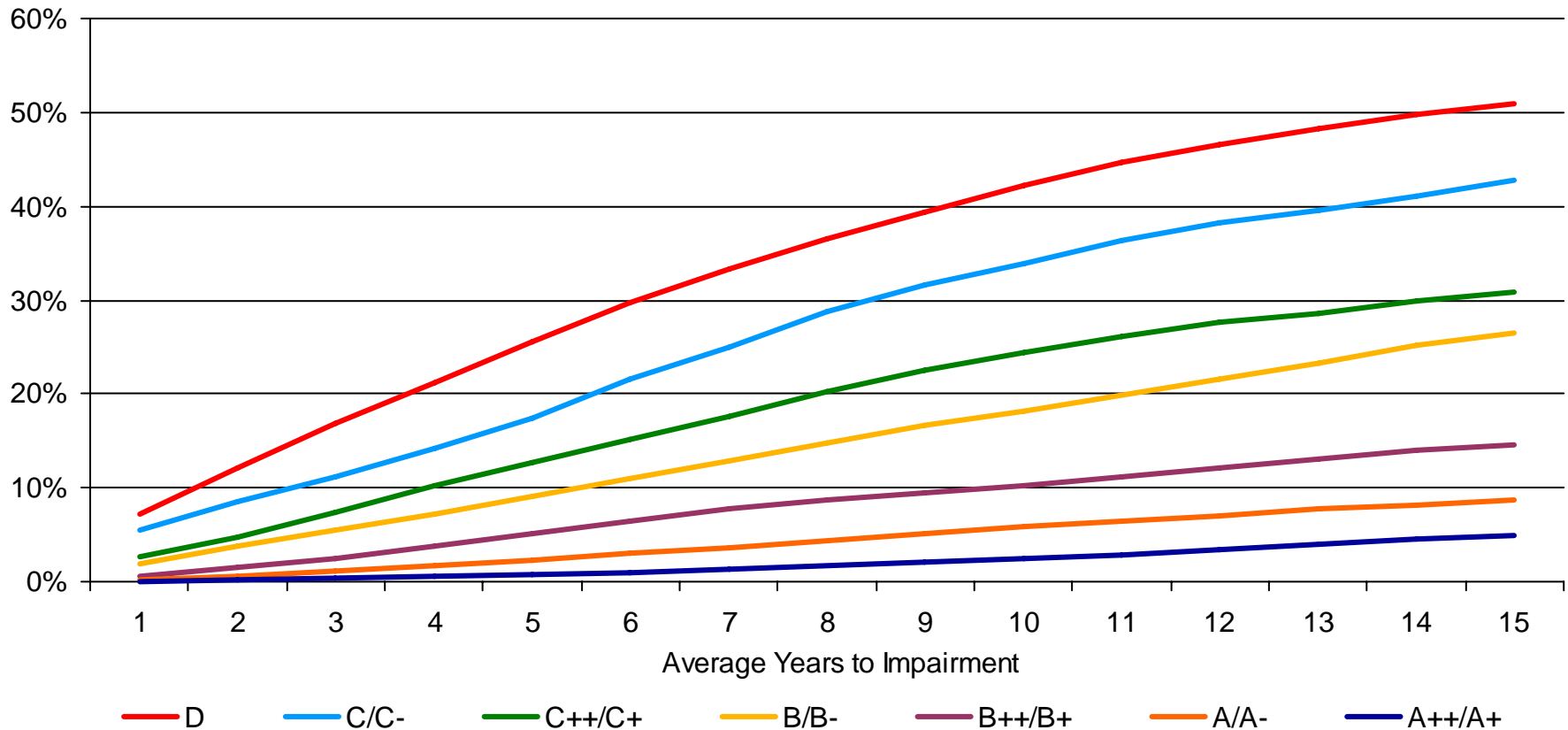


Deficient reserves, CAT losses are more important factors in recent years

*Includes overstatement of assets.
Source: A.M. Best.

Cumulative average impairment rates by best financial strength rating*

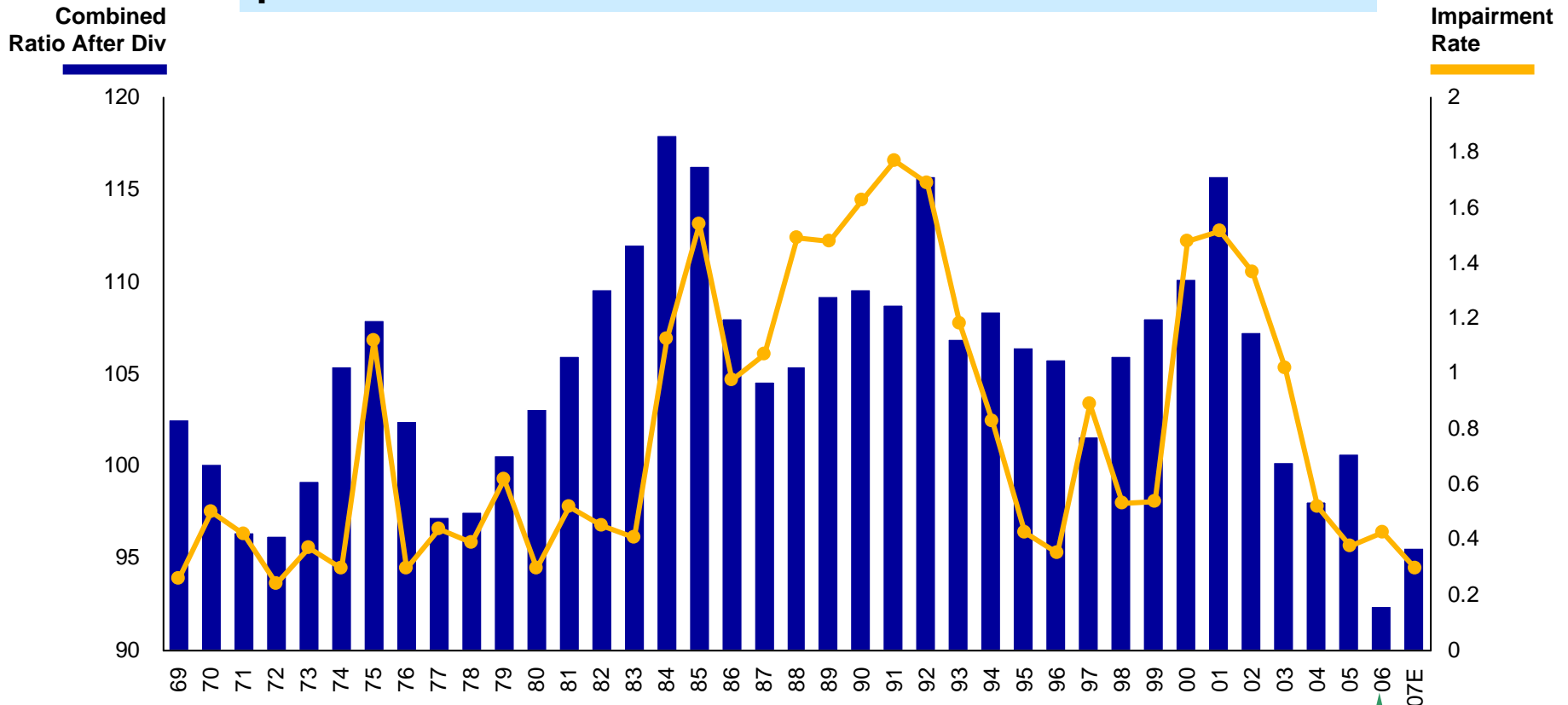
Insurers with strong ratings are far less likely to become impaired over long periods of time. Especially important in long-tailed lines.



*U.S. P/C and L/H companies, 1977 – 2002.
Sources: A.M. Best: *Best's Impairment Rate and Rating Transition Study — 1977 – 2002*, March 1, 2004.

P/C insurer impairment frequency vs. combined ratio, 1969 – 2007E

Impairment rates are highly correlated with underwriting performance and could reach near-record low in 2007



2006 impairment rate was 0.43%, or one in 233 companies — half the 0.86% average since 1969; 2007 will be lower; record is 0.24% in 1972

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

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Rating agencies focus on ERM and cycle management

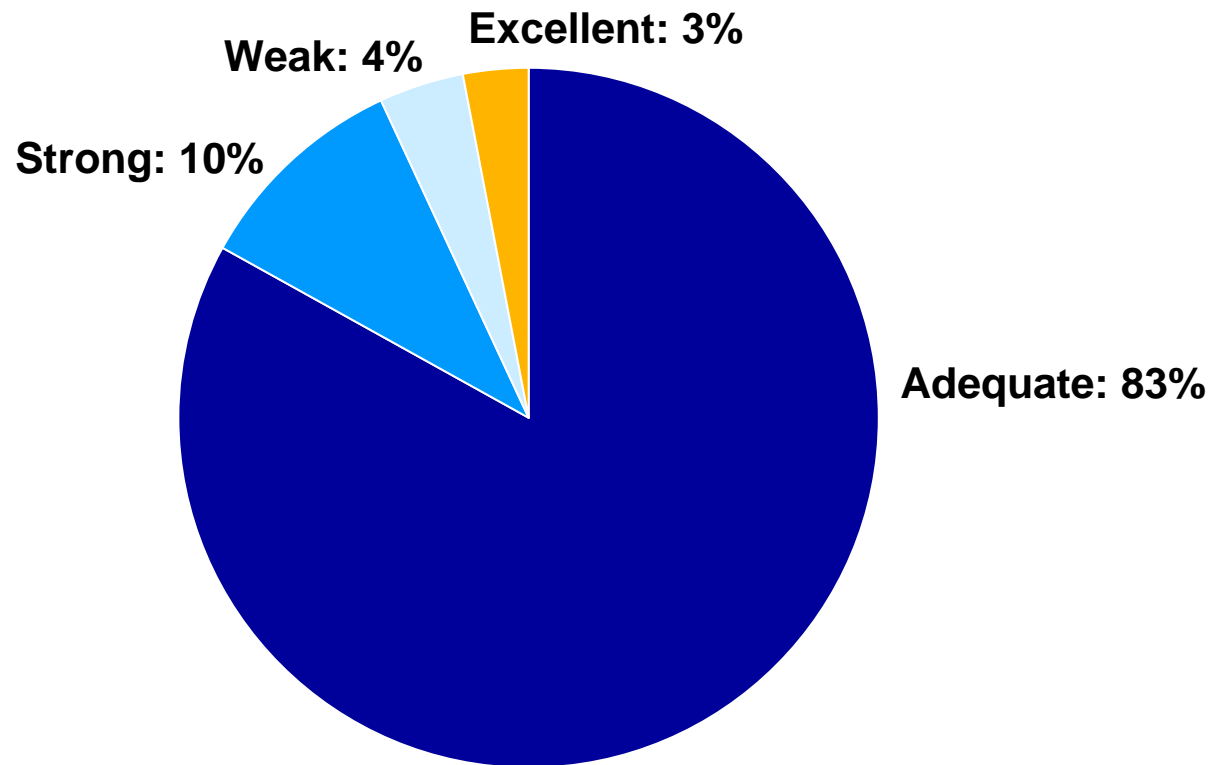
Hot Buttons

- Enterprise risk management
- Cycle management/price adequacy
- Catastrophe risk management
- Reserve stability
- Growth objectives
- Loss cost estimates
- Capital inertia

ERM rating distribution — S&P

Global ERM Score Distribution, 2007

Total Companies: 274



Source: Standard & Poor's 2008.

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A.M. Best hot button: Cycle management

Monitoring the Cycle

- Clearly articulated profit objectives over cycle
- Measuring and monitoring the cycle by tracking trends with market rates and terms
- Active research process to gauge market pricing actions and competitor behaviors

Cycle Management Execution

- Effective price monitoring of actual vs. expected losses and frequent pricing reviews
- Predetermined floors for minimum adequate pricing levels (e.g., “walk-away” prices)
- Clear process to reallocate capital and capacity
- Effective expense management

Continued...

A.M. Best hot button: Cycle management

Standards and Guidelines

- Authority levels are restructured as cycles change or tolerance levels change
- Minimum rates and terms are promulgated/adjusted by senior management
- Pricing trends are frequently reviewed and linked directly to reserve development process
- Conservative approach taken to prior year reserve releases

Compensation and Incentives

- Adherence to underwriting fundamentals and audit results drive rewards of underwriting staff
- Distributor compensation is linked to profitable growth and risk profile of submissions

Track Record

- Management track record of “walking the talk”
- Demonstrable competitive advantage(s) relative to peers
- Pre-tax ROR advantage over extended period (five-year for short-tail; ten-year for long-tail)

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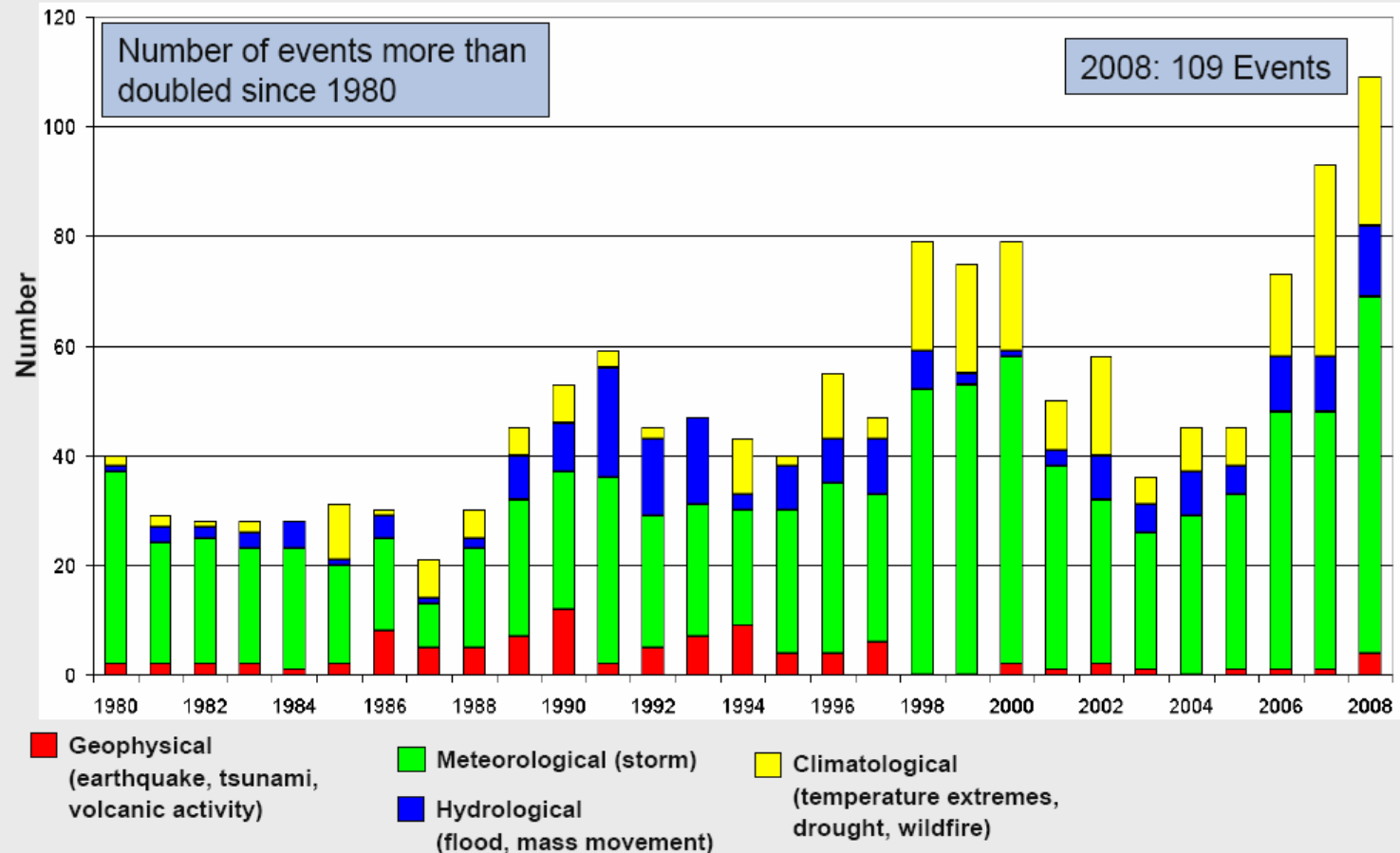
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2008 activity is robust thus far

Natural Disasters in the United States, 1980 - 2008



Number of events (January – June only)



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Source: MR NatCatSERVICE

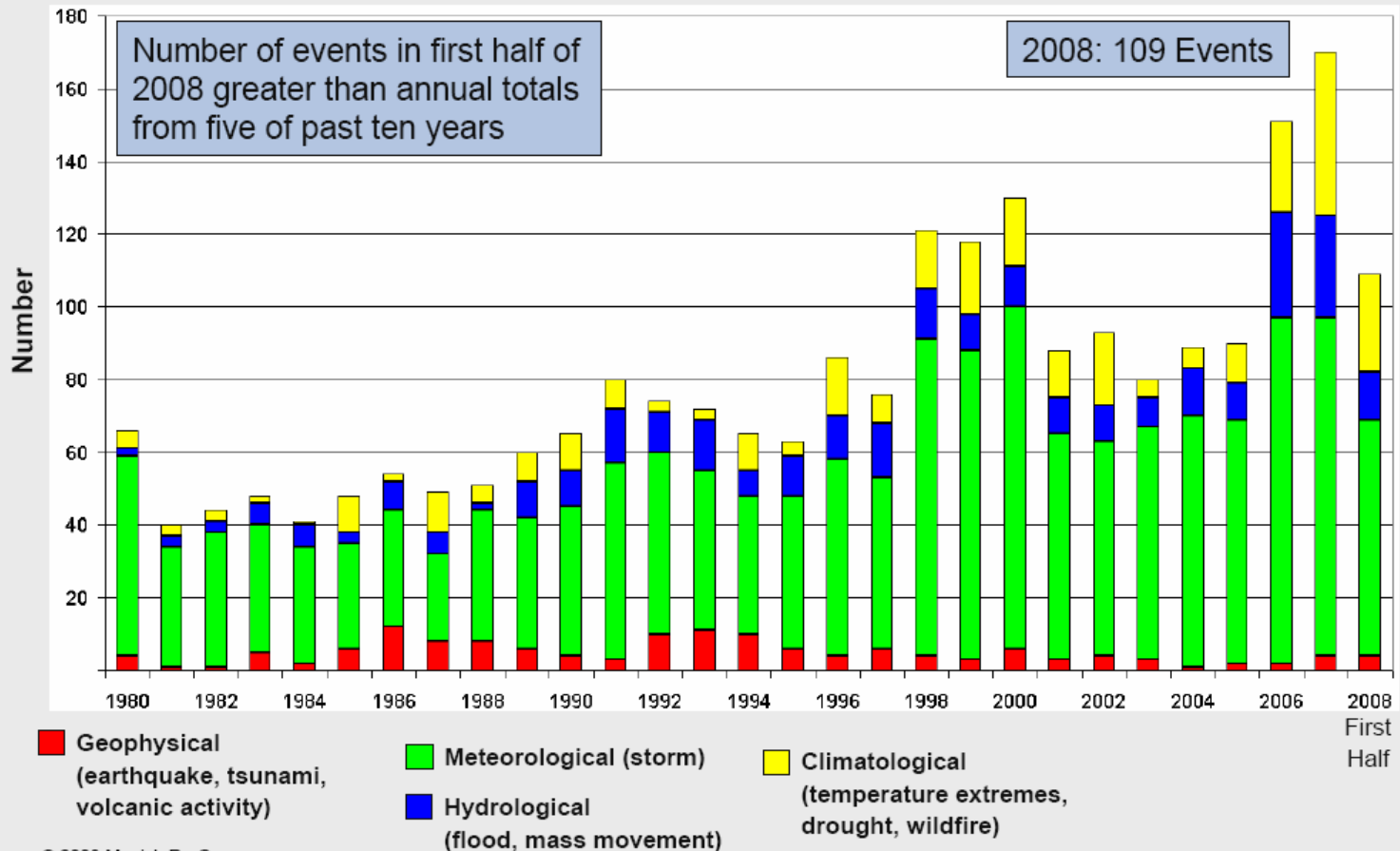
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Will 2008 be a record cat year?

Natural Disasters in the United States, 1980 - 2008



Number of events (Annual Totals 1980 – 2007 vs. First Half 2008)



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Source: MR NatCatSERVICE

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2008 North Atlantic hurricane season

- All major forecasting groups forecast “above average activity” for the season
- Forecast numbers increased in August based on an active early season
- Accumulated Cyclone Energy (ACE) Index is 187% above normal at current date

Group*	Named Storms	Hurricanes	Intense Hurricanes
<i>Long-term Average</i>	9.6	5.9	2.3
NHC	18	9	5
K/G	15	8	4
TSR	14.4	7.7	3.4
UK Met	15	—	—
As of 8/28/08	8	3	1

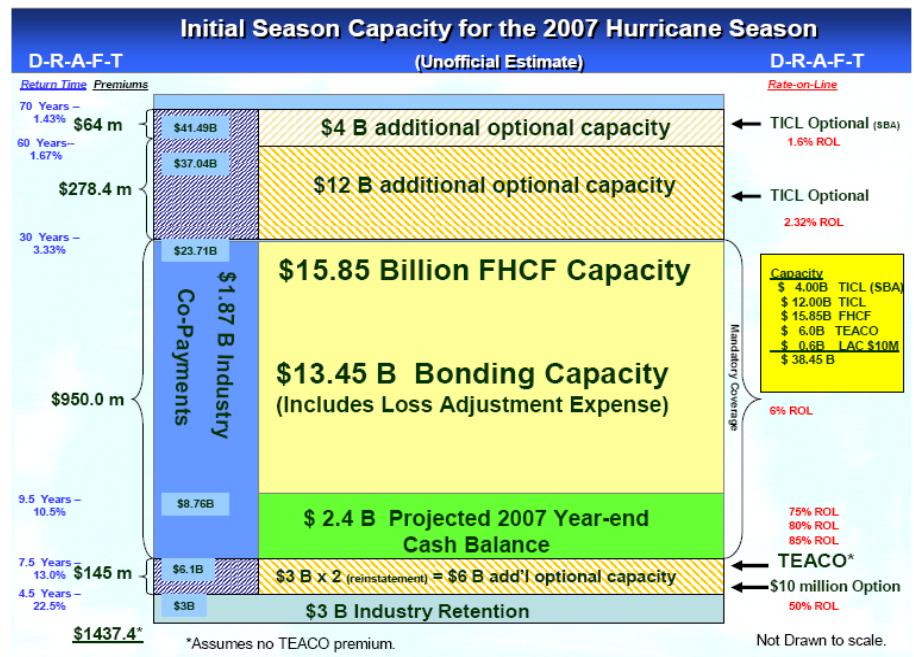
*NHC = National Hurricane Center; K/G = Klotzbach & Gray; TSR = Tropical Storm Risk; UK Met = United Kingdom Meteorological Office.

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Florida legislation has changed the reinsurance landscape

- Florida legislators *did not* scale back on the amount of coverage provided by FHCF
- Plan would have reduced the size of FHCF from \$28B to \$25B; \$3B back to the private reinsurance market
- Fitch: FL homeowner insurance market would “effectively collapse” if a \$50B event were to occur — funding shortfall of \$36.5B
- FL CFO Alex Sink is concerned about FL’s bonding capacity



Florida turned to Berkshire for put-option capital

- Effectively guarantees liquidity in the event of a major catastrophe
- Berkshire will buy \$4B of FHCF bonds if: >\$25B Cat
- Bonds characteristics
 - 30-year term
 - Tax-free
 - 6.5% Coupon
- Cost to FHCF = \$224 Million

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Big questions 2008 – 2009

- How will reinsurers manage capital?
- Will M&A and diversification accelerate?
- Will capital markets stay the course?
- Frequency/severity of nat cat?
- Will tax laws change?
- How will reinsurers meet 13% – 15% ROEs?
- Loss cost trends...will they increase?
- Will the U.S. regulatory framework change significantly?
- Election '08...Republican or Democrat?