

# Industry Surveys

## Insurance: Property-Casualty

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# Insurers poised for a solid 2004

Property-casualty (P/C) insurers are poised to produce very solid underwriting results in 2004, assuming current trends of adequate premium pricing and favorable loss trends continue. Although underwriting margins in the first quarter of 2004 were aided by an adequate level of premium rates coupled with an improvement in loss cost trends across both the commercial and personal lines of business, an increase in price competition in a number of lines of business could restrain net written premium growth in 2004.

Standard & Poor's Equity Research Group has lowered its forecast for net written premiums in 2004 to \$440.7 billion, from \$465.0 billion. Our revised estimate assumes a written premium growth rate of 8.6% above 2003 written premium levels of \$405.9 billion. Embedded in our estimate are the following assumptions: written premiums for personal lines will increase by 8.0% to approximately \$188.2 billion in 2004 (versus \$174.3 billion in 2003), that balanced lines underwriters produce an 8.0% growth in written premiums to around \$81.1 billion in 2004 (\$75.1 billion), and that commercial lines underwriters net a 9.5% increase in written premiums to approximately \$171.4 billion (\$156.5 billion).

### Full-year 2003 underwriting results show marked improvement

Based on the latest available aggregate industry operating data released in late April 2004 by the Insurance Services Office (ISO), an industry research and data collection organization, the property-casualty industry's operating results showed a marked improvement during 2003. We attribute these healthy results to a combination of premium rate adequacy, coupled with a fairly benign loss cost environment and the absence of any significant one-time catastrophic events.

Net written premiums for the representative companies in the ISO study advanced

9.8%, to \$405.9 billion in 2003, from \$369.7 billion in 2002. This rate of premium growth, while adequate, was slightly below our forecast of annual premium volume of \$415 billion, or annual written premium growth of around 12%. The shortfall from our estimate occurred primarily in the commercial lines arena, where the rate of premium price increases began to slow. Commercial lines insurers in the ISO study reported a 10.7% rise in net written premiums during 2003, for annual written premium volume of \$156.5 billion (versus \$141.3 billion of premiums written in 2002).

These results add empirical evidence to the anecdotal evidence that emerged throughout the year, as insurance companies commented that the rate of renewal price increases on numerous commercial lines policies was being pressured by an uptick in competitive pressures. Many insurers noted that commercial property lines of coverage and some standard casualty lines (like commercial multiperil) were experiencing some price competition, and that renewal rates ranged from flat in some cases to increases in the "low single-digit range." Specialty commercial casualty lines (like directors and officers liability coverage, for example) continued to garner mid-teen rate increases. After several years of fairly aggressive premium price hikes, however, the rate of increases was beginning to level off.

Personal lines insurers, which are subject to more government regulation than are commercial lines insurers (and which consequently may encounter more difficulty in raising premium rates), posted a healthy 10.0% rise in net written premiums in 2003. This group of insurers, which primarily underwrite personal automobile and homeowners' coverage, wrote \$174.3 billion of premiums in 2003, compared with \$158.5 billion in 2002. Balanced lines underwriters posted the lowest rate of written premium growth in 2003. This group, which under-

**PROPERTY-CASUALTY OPERATING RESULTS***(In millions of dollars)*

YEAR	UNDERWRITING GAIN (LOSS)	INVESTMENT INCOME	PRETAX INCOME
2002*	(32,371)	40,111	7,740
2001	(52,523)	38,980	(13,543)
2000	(32,271)	41,938	9,668
1999	(24,764)	40,061	15,297
1998	(17,669)	41,097	23,427
1997	(6,030)	41,499	35,469
1996	(17,162)	37,962	20,801
1995	(17,375)	36,834	19,459
1994	(22,083)	33,687	11,604
1993	(18,094)	32,645	14,551

\*Latest available.

Source: A.M. Best Co.

writes both personal and commercial lines coverage, wrote \$75.1 billion of premiums in 2003, up 7.4% from \$69.9 billion in premiums written in 2002. Although this rate of growth was adequate, it was less than we expected. However, this shortfall mainly reflected certain company-specific strategies aimed at reducing the writing of certain types of policies.

The favorable written premium growth trends that were underway in 2002 translated into relatively healthy rates of earned premium growth in 2003. (Note: Earned premiums are a revenue component on insurers' income statements. For a detailed explanation of how written premiums flow through the income statement into earned premiums, please refer to the "How the Industry Operates" section of this *Survey*.) For insurers in the ISO study, earned premiums advanced 11.4% in 2003, to \$388.1 billion, from \$348.5 billion in 2002. Although this rate of earned premium growth was down a bit from the 11.9% rate of growth produced in 2002, it contrasted rather sharply with the paltry 1.8% rise in earned premiums reported in 1999. The annual rate of earned premium growth during 1997–2003 averaged 5.9%.

### Investment income growth restrained by low interest rates

Net investment income is typically the second largest revenue component for property-casualty insurers (behind earned premiums), sometimes accounting for one-third or more of total revenues. During 2003, the relatively

low interest rate environment, which depressed investment yields on fixed income investments, was the main culprit behind the tepid growth in investment income. Indeed, many companies warned in their guidance for coming periods that low interest rates would continue to constrain their net investment income growth. Net investment income for insurers in the ISO study advanced only 4.0% to \$38.7 billion in 2003, from \$37.2 billion in 2002. Although this rate of growth was subdued, it represented a pickup from first-half 2003 growth of around 2.2%.

However, a rebound in both the equity and fixed income markets during 2003 helped produce a turnaround in net realized investment gains for insurers in the ISO study. During 2003, this representative group reported net realized investment gains of more than \$6.9 billion. This was in marked contrast to the more than \$1.2 billion of realized investment losses the industry had to absorb in 2002. (Note: after-tax realized investment gains and/or losses are typically excluded from analysts' estimates of net operating earnings for insurance companies.)

Another positive sign that emerged during 2003 was the level of unrealized investment gains many property-casualty insurers had amassed. For insurers in the ISO study, unrealized investment gains totaled more than \$25.2 billion in 2003. This represented a marked turnaround from 2002, when the industry had nearly \$20.8 billion in unrealized investment losses.

### Loss cost growth still constrained

Revenue growth for property-casualty insurers in 2003 was aided by several factors: the double-digit rate of earned premium growth, modestly higher net investment income, and a turnaround in realized investment gains. However, industry profitability was significantly enhanced by the favorable loss cost trends at play throughout the year. Because losses (or claim costs) and loss adjustment expenses are by far the largest expense item facing an insurer, a change in the direction of these expenses can have a rather large impact on an insurer's bottom line. Examples of loss costs include expenses associated with auto and home repairs, as well as medical costs.

Insurers in the ISO study reported a fractional (0.4%) rise in incurred losses during

2003, to \$239.7 billion (or approximately 61.8% of earned premiums), from \$238.8 billion (or 68.5% of earned premiums) in 2002. Incurred loss adjustment expenses (*i.e.*, the costs associated with settling claims) rose more rapidly, increasing 11.8% in 2003, to \$50.1 billion, from \$44.8 billion in 2002. Taken together, loss and loss adjustment expenses (LAE) were up a restrained 2.2% in 2003, to \$289.8 billion, from \$283.6 billion in 2002. This rate of increase is the smallest in the seven years between 1997 and 2003. During that period, the average annual rate of loss and LAE increases was 5.3%, including a 15.3% rise in 2001 (due mainly to costs associated with the September 11 terrorist attacks).

Catastrophe losses are a component of the industry's aggregate loss cost figures. A catastrophe is defined as an event or a series of related events that produces \$25 million in insured losses. Data obtained from ISO indicate that catastrophe losses totaled \$12.9 billion in 2003, up sharply from \$5.9 billion in 2002. There were no high-profile catastrophes in 2003; rather, a series of severe storms caused the bulk of the losses.

Another factor that can greatly affect profitability is the level of loss reserves. Loss reserves are the funds insurers set aside to pay future claims. Insurers in the ISO study reported a 7.7% rise in reserves for losses and loss adjustment expenses, to \$424.9 billion in 2003, from \$394.6 billion in 2002. This follows a 6.1% rise in loss and LAE reserves during 2002. This level of increase in loss reserves did not surprise us, given the growing concern among industry participants over the adequacy of loss reserves for certain commercial casualty insurance underwritten during the most competitive period of the market cycle (*i.e.*, from 1997 to 2000). However, during the 1997–2003 period, loss and LAE reserves increased at an average annual rate of less than 2.4%.

Favorable trends in top-line growth and the modest increase in loss costs offset the rise in loss reserves during 2003. This led to a significant year-to-year improvement in underwriting results. According to the ISO data, insurers' pretax underwriting losses totaled \$4.6 billion (or approximately 1.2% of earned premiums) in 2003, a distinct improvement from underwriting losses of \$30.8 billion (or about 8.8% of earned premiums) in 2002.

## Combined ratio highlights improved underwriting results

The combined ratio statistics reported for 2003 illustrate very clearly the magnitude of the property-casualty industry's improved underwriting results. The combined ratio is a key measure of underwriting performance. It is the sum of the loss ratio, the expense ratio, and (where applicable) the dividend ratio. A combined ratio below 100% indicates an underwriting profit, while one in excess of 100% points to an underwriting loss. (For more information on the combined ratio and its implications for insurer profitability, see the "How to Analyze a Property-Casualty Insurer" and "Key Industry Ratios and Statistics" sections of this *Survey*.)

Property-casualty insurers in the ISO study reported a combined ratio of 100.1% in 2003. This represented a rather marked improvement over 2002's combined ratio of 107.3%. Every segment of the industry saw improved underwriting results. Commercial lines insurers' underwriting results showed the greatest degree of improvement: a combined ratio of 101.2% in 2003, versus 109.8% in 2002. However, the personal lines segment was the only one to show an underwriting profit in 2003, with a combined ratio of 97.7%, versus 104.5% in 2002. Balanced lines underwriters, which have struggled with a number of adverse company-specific underwriting trends, posted a combined ratio of 103.2% in 2003, versus 109.0% in 2002.

The improvement in underlying loss trends helped offset the surge in catastrophe losses during 2003. As a result, the industry's loss ratio (equal to incurred losses and loss adjustment expenses divided by net earned premiums) declined to 74.7%, from 81.4% in 2002. Commercial lines writers led the way with a better claims picture, posting a loss ratio of 75.6% in 2003, versus 83.1% in 2002. Personal lines writers also produced some rather impressive results, with a loss ratio of 73.5% in 2003, versus 80.0% in 2002. One of the main drivers behind the personal lines improvement occurred in automobile loss trends, in both frequency (*i.e.*, how often losses occur) and severity (how costly they are). Balanced lines underwriters also saw an improved loss picture: their loss

**ESTIMATED CHANGES IN POLICYHOLDERS' SURPLUS***(Total property-casualty industry, in billions of dollars)*

ITEM	2001	2002	2003
Policyholders' surplus—beg. of period	317.3	289.6	285.4
Operating income	(13.8)	5.6	33.7
Realized capital gains	6.6	(1.2)	6.9
Income taxes	0.2	(1.3)	(10.8)
Net after-tax income	(7.0)	3.1	29.8
Unrealized capital gains (loss)	(18.0)	(20.8)	25.2
Stockholder dividends & other	(11.8)	(7.1)	(9.1)
New funds	12.9	18.8	11.5
Misc. surplus change	(3.8)	1.8	4.1
Policyholders' surplus—end of period	289.6	285.4	347.0

Source: Insurance Services Office.

ratio improved to 75.5% in 2003 from 81.1% in 2002.

The industry's expense picture also brightened a bit in 2003, with the expense ratio (equal to other underwriting expenses divided by net written premiums) declining to 24.9%, from 25.4% in 2002. We were a bit surprised by the modest improvement, particularly since these expenses were being divided over a growing premium base. However, after several years of cutting expenses, we assume a number of insurers began investing in their core business again. Commercial lines underwriters showed the most improvement in their expense ratio, posting a 25.1% ratio in 2003 versus 26.0% in 2002. Personal lines writers also shaved a little off their overhead, with an expense ratio of 23.7% in 2003, versus 23.9% in 2002. Balanced lines underwriters posted an expense ratio of 27.3% in 2003, unchanged from a year earlier.

The dividend ratio for the entire industry also inched downward in 2003, to 0.5% from 0.6% in 2002. Commercial lines writers posted a dividend ratio of 0.4% in 2003, versus 0.7% in 2002. Balanced lines underwriters also ratcheted down their dividend ratio to 0.4% in 2003, from 0.6% in 2002. However, personal lines insurers saw a slight increase in their dividend ratio in 2003, to 0.6% from 0.5% in 2002.

### Surplus also rises

An improvement in underwriting performance, coupled with a turnaround in investment results, helped propel the industry's surplus upward in 2003. Surplus

for the property-casualty industry refers to its capital, or net worth (the amount by which the industry's assets exceed its liabilities). Surplus is often referred to as statutory surplus under statutory accounting principles, and it is analogous to shareholders' equity under generally accepted accounting principles. At December 31, 2003, the property-casualty insurance industry had total surplus of \$347.0 billion, up nearly 22% from \$285.4 billion at year-end 2002. The last time industry surplus rose to this degree was in 1997, when surplus growth was 20.7%.

Since surplus rose faster than written premiums, the industry's leverage declined. Leverage in this instance refers to the extent to which an insurer uses its capital (or surplus) to support the writing of business (or premiums). The ratio of net written premiums to surplus is a means by which one can quantify this practice. (For a more detailed explanation of leverage, see the "How to Analyze a Property-Casualty Insurance Company" section of this *Survey*.)

The ratio of net written premiums to policyholder surplus for the 12 months ended December 31, 2003, was 1.17-to-1. This compares with a net written-premiums-to-surplus ratio of 1.30-to-1 at year-end 2002. To put this in context, in 2003 insurers wrote \$1.17 worth of premiums for every \$1 of surplus. During 2002, the average insurer underwrote \$1.30 worth of premiums for every \$1 of surplus. Regulators typically allow insurers to underwrite \$2.00 worth of premiums for every \$1.00 of surplus.

Using the 2-to-1 premium-to-surplus ratio as our guide, we can roughly estimate that the industry had approximately \$144 billion of "excess" surplus or capital at December 31, 2003. We derived this number by using the \$405.9 billion in net written premiums and \$347.0 billion of policyholder surplus as inputs into our equation. To support this level of written premium growth, the industry would need approximately \$203 billion of surplus (or capital). The difference between actual surplus (\$347 billion) and "required" surplus (\$203 billion) is our so-called excess surplus of \$144 billion. We estimate that this excess surplus could support another \$288 billion in written premiums.

While this exercise helps to illustrate the industry's financial condition and leverage,

it needs to be examined against a backdrop of numerous other considerations. First, although companies might be permitted to leverage their surplus to this degree, very few actually do. Second, a significant component in the growth of surplus during 2003 came in the form of unrealized investment gains. These gains tend to be volatile and could reverse course. Finally, although the industry has been adding to its loss reserves, we continue to believe that loss reserves for long-tail casualty lines of business underwritten in prior years remain inadequate. An increase in these reserve levels could erode a lot of the excess surplus. ■





## INDUSTRY PROFILE

# Managing risk in a changing environment

The US property-casualty (P/C) industry comprises thousands of companies, each vying for a share of the multibillion-dollar market for personal and commercial lines insurance coverage. However, the market is dominated by a small group of companies.

According to the latest available data from A.M. Best Co., a provider of insurance company ratings and information, the 10 largest property-casualty insurer groups (based on net written premium volume for property-casualty insurance) wrote just over \$171.8 billion of premiums in 2002. That accounted for approximately 45.3% of that year's \$378.9 billion in industrywide written

premiums. The five largest insurer groups wrote approximately \$119.8 billion in premiums, for a market share of around 31.6%. The two largest P/C insurers — State Farm Group and Allstate Insurance Group — had a 17.4% share of the US property-casualty market. Combined, they wrote some \$66.1 billion in premiums in 2002.

Some US companies (notably American International Group) have a long-established presence in numerous overseas markets, and several large property-casualty insurers have sought to increase their presence in certain overseas markets. For the most part, however, most US-based P/C insurers operate primarily in the United States.

### TOP 20 PROPERTY-CASUALTY UNDERWRITERS — 2002\*

(Ranked by net premiums written)

UNDERWRITER	NET PREMIUMS WRITTEN† (MIL. \$)	2001 RANK	2000 RANK
1. State Farm Group	42,747	1	1
2. Allstate Ins. Group	23,342	2	2
3. American Int'l Group	21,046	4	4
4. Zurich/Farmers Group	17,428	3	3
5. Berkshire Hathaway Ins. Gp.	15,204	5	5
6. Travelers PC Group	11,882	6	6
7. Nationwide Group	11,741	7	7
8. Liberty Mutual	10,574	8	8
9. Progressive Insurance Gp.	9,456	10	11
10. The Hartford Ins. Group	8,395	14	10
11. CNA Financial	8,340	9	9
12. Chubb	7,811	13	13
13. USAA Group	6,967	11	12
14. St. Paul	5,813	12	15
15. State Compensation Insurance Fund of Calif.	5,350	21	7
16. American Family Ins. Gp.	4,878	19	18
17. GE Global Ins. Gp.	4,644	20	14
18. SAFECO	4,585	15	16
19. Anthem Group	4,421	17	19
20. Erie Insurance Group	3,330	25	26

\*Latest available. †US only.  
Source: A.M. Best Co.

## INDUSTRY TRENDS

The foremost trend affecting most property-casualty insurers is an upturn in premium rates. After years of extremely competitive premium pricing conditions brought on by an overabundance of underwriting capacity, signs of pricing strength in some commercial lines first emerged in 2000 and continued through 2001 and 2002 and well into 2003. However, emerging evidence suggests that the rate of premium price hikes is moderating. This is particularly true in the more commodity-type standard lines of coverage and in certain property lines of coverage. Highly specialized coverage lines continue to garner relatively aggressive rate increases.

In addition, the industry is facing the threat of costly asbestos claims for which it may be under-reserved. After appearing to have stabilized, asbestos claims are on the rise again, as many claimants are seeking to tap the deep pockets of insurers. Some industry experts have estimated that the ultimate liability for asbestos-related losses could approach \$200 billion, with the US insurance



industry responsible for \$55 billion to \$65 billion of that total.

Another recent trend that has affected the insurance industry (and the broader financial services industry as well) is a lapse in large-scale merger and acquisition (M&A) activity. Historically, insurers often attempted to offset slowing premium growth by joining forces in an effort to become more cost efficient. The results have not been entirely positive, however, and many companies have suffered from post-merger integration pains. Although some signs of life began to return to the M&A arena in late 2003, Standard & Poor's does not expect a widespread consolidation trend among property-casualty insurers (similar to what transpired in the banking industry during the 1990s) to materialize.

A parallel trend affecting certain areas of the industry has been a widespread re-evaluation of business models. The concept of the financial services conglomerate has fallen from favor, and in some cases, insurers are narrowing their focus. However, some property-casualty insurers, particularly personal lines carriers, have expanded into the retirement savings market. Still others, primarily commercial lines insurers, have expanded overseas in an attempt to offset slower growth in the maturing domestic market.

Among other efforts, many insurers have focused on improving their distribution systems as a means of spurring growth and regaining a competitive edge. Most insurers are publicly committed to maintaining their traditional agency distribution, but are exploring other ways to get the product to the customer in a more economical fashion. Some are actively developing direct marketing channels, including Internet advertising and sales. Many have also joined forces with banks and brokerage firms to expand their distribution channels by selling insurance products through those firms' branch networks.

### **Insurance premiums rising, but at a slower rate**

The key condition affecting the property-casualty insurance industry today is a bit of a slowdown in the rate of premium increases. After nearly a decade of weak premium rates brought on by excess underwriting capacity, premium rates began to strengthen in late

2000. That pricing strength continued into 2001 and accelerated after the September 11 terrorist attacks that year. Standard & Poor's currently estimates that written premiums will total approximately \$440.7 billion in 2004, up approximately 8.6% from 2003 written premiums of \$405.9 billion (as discussed in the "Current Environment" section of this *Survey*). Against a backdrop of higher (albeit moderating) premium rates, we also expect to see a continuation of tightened policy terms. Changes will include higher deductibles and lower coverage limits. Indeed, the market may see increasingly limited availability of coverage, as insurers move to reduce exposure in response to the heightened risk of terrorist activities, rising loss costs, and the industry's declining surplus. As a result, a number of commercial insureds may again seek alternatives to the traditional insurance market.

### **Commercial clients may seek alternatives**

Commercial clients that need to manage risk have two options within the traditional market. One is to transfer that risk to an insurance company through the purchase of an insurance policy. The second traditional method is to "self-insure"; that is, to retain the risk and allocate funds to meet the expected costs. These risk management tools have historically been used to manage the majority of commercial lines risk. During the 1980s, when the amount of available commercial liability insurance was insufficient to meet demand, a number of alternative risk transfer (ART) mechanisms were established. These mechanisms, including captive insurers and risk retention groups, are being increasingly used again.

◆ **Captives.** This is a type of insurance company created and wholly owned by one or more noninsurers for the purpose of providing its creators with insurance protection. A "pure" captive insures only the risks of its parent company. These entities neither spread nor transfer risk; thus, they technically do not provide insurance.

A study published in April 2002 by A.M. Best estimated that there were 3,861 captives worldwide, accounting for \$50.2 billion in premiums in 2000, up from 3,776 captives accounting for \$38.9 billion in premiums in 1999. The majority of offshore captives that

cover US-based risks are domiciled in Bermuda, where they can take advantage of certain tax savings and regulation that is relatively more lenient than in the United States. A number of US states have welcomed captive insurers. Vermont is home to more than 360 captive insurers. As of early 2002, captives licensed in Vermont included those set up by PepsiCo Inc. and US Bancorp.

◆ **Risk retention groups.** These entities are formed by companies within a common industry (airlines, for example) that join together to provide members with insurance protection. A risk retention group is a corporation owned and operated by its members. It must be chartered and licensed as a liability insurance company under the laws of at least one state. The group can write insurance in other states.

#### ARTs may broaden scope

The creation of these two alternative risk transfer mechanisms was facilitated by the passage of the Product Liability Risk Retention Act of 1981, which was enacted to solve the shortage of liability insurance. The act was expanded in 1986 to include all areas of commercial liability, except workers' compensation.

In the wake of September 11, 2001, many in the insurance industry are pushing to expand the scope of this law, so that it may also apply to the property insurance market. Indeed, A.M. Best projected in 2002 (latest available) that 50% of the US commercial insurance market would use some form of alternative risk transfer mechanism by the end of 2003, up from 30% in 1996.

#### Rising asbestos claims threaten profits

A combination of social, economic, and legal changes have led to an escalation in asbestos and asbestos-related claims in recent years. That trend is likely to continue. According to the American Insurance Association, an industry trade group, if the tragic events of September 2001 had not occurred, asbestos and asbestos-related issues would be front and center on lobbyists' and Congress's agendas. Asbestos, the common name for a group of naturally occurring silicate minerals, was used in a variety of commercial and consumer products,

including roofing and flooring, fireproofing, and thermal insulation. Because of widespread use of this product decades ago, millions of people were exposed to this cancer-causing agent.

The initial wave of asbestos claims, which began more than 20 years ago, was primarily targeted at companies that manufactured asbestos and asbestos-related products. Liability claims made in connection with these lawsuits typically came under a portion of a manufacturer's liability policy that had strict limits on insurers' liability.

These resources were depleted, however, as many asbestos manufacturers filed for bankruptcy protection under the weight of their asbestos liability. The second, and more costly, wave of litigation involves those companies that used asbestos products. These claims are being filed under a more general area of a company's liability insurance policy — one that typically has less strict coverage limits. Consequently, insurers' liabilities for claim costs have escalated.

The impact on insurers from the shift in the type of claims being filed is being exacerbated by an overall increase in the number of claims filed. Many unions and lawyers are urging workers and others who may have had contact with asbestos to file claims, warning that if they later develop an illness, there may not be enough resources left to pay their claims. According to the latest data available from the Insurance Services Office (ISO), an industry research and data collection organization, the number of asbestos cases pending in US courts doubled to about 200,000 in 1999 from 100,000 in 1993. By mid-2003, that number had risen to more than 625,000. Published reports estimate that the ultimate number of asbestos claims could rise to well over one million.

Another development that has prompted more people to file claims has been the lack of any meaningful reform in the way cases are settled. A 1999 Supreme Court decision ruled that a class action settlement of claims against Fibreboard Corp., a major asbestos producer, could not proceed because funds might be exhausted before all claims were paid. In addition, because the Supreme Court would not give a number of these cases class action status, the number of cases has increased.

### Asbestos reserves appear inadequate

The potential financial impact on insurers is difficult to quantify, given the level of uncertainty surrounding this litigation. Nevertheless, a survey published in mid-2001 by Tillinghast-Towers Perrin, an actuarial consulting firm, estimated that the final tab from asbestos could reach \$200 billion. Tillinghast estimated that the US insurance industry would bear about 30% of the total cost, or between \$55 billion and \$65 billion. An estimated 31% would be borne by overseas insurers. Manufacturers, suppliers, and other users of asbestos products would pay out the remaining 39%.

According to data obtained from the ISO, insurers paid out \$3.4 billion in environmental and asbestos (E&A) losses in 2002, up from \$3.3 billion in 2001. However, E&A incurred losses and loss adjustment expenses more than doubled in 2002 to \$7.8 billion, from \$3.5 billion in 2001. In each of the five years from 1996 through 2001, however, insurers paid out more than they reserved for E&A loss and loss adjustment expenses. As a result, industry reserves for E&A losses declined from \$28.2 billion at year-end 1996 to \$22.6 billion at year-end 2001. Industry reserves increased to \$26.6 billion at year-end 2002. We anticipate that reserves will show another healthy increase at year-end 2003, given a number of large one-time reserve increases taken by some companies. However, we continue to be concerned about the adequacy of asbestos reserves, given the increase in claim activity and severity.

### M&A activity rebounded in 2003

Thanks to a handful of relatively large, high profile deals announced throughout the insurance sector, merger and acquisition (M&A) activity in 2003 picked up considerably from 2002's depressed levels. A recovery in industry pricing fundamentals, coupled with a more buoyant equity market and US economy during 2003, helped provide the necessary catalysts.

According to information obtained from SNL Securities Inc., a financial services research and data collection firm, a total of 76 insurance-related deals valued at approximately \$56.4 billion were announced during 2003. This contrasts rather sharply with the 71 deals valued at just \$8.0 billion that were announced in 2002. The property-casualty

segment led the industry in both deal volume and activity. During 2003, 43 deals were announced, valued at \$22.2 billion. This compares with 39 deals valued at only \$439.6 million announced in 2002 and 50 deals valued at \$2.2 billion announced in 2000.

The largest deal within the property-casualty industry (and the second largest deal in the overall insurance industry) occurred as a "merger of equals" between The St. Paul Companies and Travelers Property Casualty that was valued at some \$16.1 billion when it was announced November 17, 2003. The transaction, under which each Travelers common share was exchanged for 0.4334 of a share of common stock of The St. Paul Companies, was completed on April 1, 2004. The combined entity, renamed The St. Paul Travelers Companies Inc., is the second largest commercial lines property-casualty insurer (behind American International Group), with combined net written premium volume of more than \$20 billion (based on estimated pro forma 2003 data).

Despite the rebound in M&A activity that occurred in 2003, we do not anticipate a trend of broad-based, large-scale mergers (like the one that created St. Paul Travelers) continuing through 2004. Indeed, as organic growth opportunities remain attractive amid an adequate pricing environment, the option of merging and consolidating to increase efficiencies becomes less desirable to property-casualty underwriters. Moreover, the pattern and composition of M&A activity in 2003 resembled that of prior years, with one sizable deal and a number of smaller transactions.

### The changing nature of consolidation activity

In the industry's consolidation phase of the early to mid-1990s, the companies being acquired were considered vulnerable. In most cases, they had made some missteps and had fallen on hard financial times. Opportunistic acquirers quickly snapped up these "bargain" companies. Subsequently, however, many deals took on a strategic thrust, such as diversification or expansion abroad.

In the aftermath of September 11, 2001, and after nearly a decade of inadequate reserve levels for certain liability claims, a number of insurers may find themselves financially vulnerable. Some of these insurers could be acquired, if the price were right. Given the general wari-

ness toward traditional M&A in the present environment, however, we doubt that all of these companies will be snapped up.

### Backtracking from conglomeration

Another trend that may emerge as a result of recent events is “de-conglomeration” — a narrowing of business focus, as opposed to diversification into a wide range of market segments.

Perhaps no company in the financial services industry better embodied the concept of diversification through acquisitions than Citigroup Inc. This financial services conglomerate, which is based in New York City, operates in more than 100 countries and territories and has a presence in virtually every segment of the financial services marketplace, from insurance to consumer and commercial banking to investment services.

Citigroup was created in 1998, with Citicorp’s historic acquisition of Travelers Corp. — the first merger of a bank and an insurance company. Following that deal, Congress enacted financial services deregulation legislation that made similar deals possible. It was widely anticipated that Citigroup’s business model — that of a broad-based financial services conglomerate — would be copied by many competitors. That trend, however, has not materialized so far.

Moreover, in late 2001 Citigroup re-evaluated its business mix and decided to spin off its Travelers Property Casualty unit. Citigroup spun off about 20% of Travelers in a March 2002 initial public offering, and completed a tax-free distribution of most of the balance (excluding about 9.9%) to its shareholders during the third quarter of 2002.

Because investors today cast a wary eye on companies with complicated accounting practices and/or financial structures, many corporations will likely rethink their growth and diversification strategies. Many will likely seek to grow within their core business lines rather than broadening into other segments of the financial services market.

### Expanding overseas as an option

As financial services companies rethink their diversification strategies, some will consider expanding overseas as a means of ramping up growth. Traditionally, most insurance companies have tended to limit their scope of opera-

tions to their home turf, with US-based insurers writing insurance primarily in the United States, and their European counterparts remaining largely in their own domestic markets. More recently, however, two factors — the globalization of US businesses and a faster rate of economic growth in many areas outside the United States — have led a number of insurers to venture abroad.

Despite the opportunities for faster growth afforded by overseas markets, we don’t anticipate that a large number of US primary insurers will expand abroad in the near future. This reflects the regional and national thrust of most primary insurers, especially those that write such personal lines as homeowners’ and personal auto insurance. Concerns over language and cultural differences, plus differing consumer attitudes and customs, have left many insurers wary of expanding into unknown markets. Exacerbating these concerns is the fear of corruption, especially in developing countries where growth opportunities are the greatest.

Nevertheless, for insurance companies that choose to expand abroad, the returns can be handsome. For example, American International Group, perhaps the most global of all US-based insurance companies, has long had a presence in more than 100 other countries. AIG’s international network stretches across Asia and the Pacific Rim to Latin America, Europe, Africa, and the Middle East.

The tremendous opportunities that exist overseas can be costly to realize. For some insurers, having a global presence does not make sense. In late June 2001, Allstate Corp., the nation’s second-largest property-casualty insurer, decided to sell its direct auto insurance business in Germany and Italy to London-based Direct Line, a subsidiary of The Royal Bank of Scotland, for an undisclosed amount. In a written release, Allstate said that despite the “significant business opportunities” to be found in overseas markets, the company believed that its “best opportunities in the immediate term are closer to home.”

### Internet and e-commerce offer opportunity and challenge

Allstate Corp.’s plan, first announced in November 1999, to aggressively expand its direct selling and Internet-based distribution

capabilities, while maintaining its commitment to its 15,200-member captive agency sales force, exemplifies both the opportunities and the challenges facing insurers in today's technology-driven marketplace. Historically, insurers have relied on agents (independent and captive) as their primary distribution channel. However, the converging financial services marketplace, coupled with changing consumer preferences and technological innovations, has forced insurers to rethink this strategy. Indeed, preliminary results of a survey conducted by Tillinghast-Towers Perrin found that 76% of property-casualty insurance chief executives cited "distribution effectiveness and productivity" as a key issue affecting their industry.

Nonetheless, many insurers still lag behind their banking and brokerage peers in their online presence. Although virtually every insurer has a Web site, most of these amount to online brochures offering general product information and instructions on how to contact a local agent. Some firms (like GEICO Corp., Progressive Corp., and a division of Berkshire Hathaway Inc.) that primarily use direct-marketing techniques such as toll-free phone numbers have such information available for visitors to their Web sites.

Many in the industry view personal lines insurance products like auto and homeowners' coverage as relatively well suited to online or direct distribution because they are fairly simple, commodity products (versus more complicated commercial lines coverage). However, certain obstacles still exist, such as the need for a customer to sign his or her name to an insurance policy to make it binding. Legislation covering electronic signatures may offer a solution to this dilemma. Another obstacle is that many consumers find it daunting enough to buy insurance face-to-face from a trained sales representative, and even more so online. Nonetheless, as they become increasingly comfortable with simple transactions on the Internet (like buying toys or books), consumers are likely to be more willing to go online for insurance purchases.

The largest obstacle is likely the industry's own attitude. Despite the fact that agents' share of the market has eroded, most insurers still rely heavily on this form of distribution. According to a survey conducted by Datamonitor, a research firm, and published by A.M. Best, captive agents were expected

to see their share of the property-casualty insurance market slip to 48.8% in 2003, down from 56.5% in 1998. Independent agents may have seen their share decline to a projected 23.3% in 2003, from 27.0% in 1998. For 2003, the Internet was projected to account for some 7.3% of property-casualty insurance sales, up from less than 1% in 1998.

While agency systems can be expensive to maintain, many insurers still view them as an effective means of distributing their products, especially for those insurers that subscribe to the paradigm "insurance is sold, not bought." Furthermore, in the past many insurers built sizable market shares by relying on a network of independent and captive agents. Most are hesitant to push other distribution channels that compete directly with their agents. In many ways, Allstate's plan — to shift its distribution strategy without alienating its agents — is representative of the challenge facing the industry as a whole.

### **Banks enter the fray**

Life insurers have long waged a turf war with banks over the sale of life insurance products through bank branches. Now it looks as though property-casualty insurers will also likely square off with banks. This cloud may have a silver lining, however: the result could be a new distribution channel for insurers.

In several overseas markets, banks already have a fairly well established presence in markets for personal lines such as life and property-casualty insurance. Moreover, in several countries, a number of large insurance companies and banks have formally teamed up through mergers to create bank/insurance powerhouses.

Legislation has given banks permission to underwrite insurance in the United States. However, considering the level of capital required, the slow growth prospects, and the relatively high degree of earnings volatility inherent in the property-casualty insurance business, not all US banks have been or will be eager to underwrite insurance products. Consequently, we anticipate that many banks that want to expand in this direction will initially seek joint venture agreements with property-casualty insurers. These arrangements could actually help insurers widen their



distribution channels and, if structured correctly, could prove mutually beneficial.

Proponents claim that such arrangements can benefit both banks and insurers. Banks, they say, get the opportunity to offset slowing loan growth with new sources of fee income, while insurers can widen their distribution channels. Moreover, for insurers, distributing their products through banks offers a low-cost means of reaching the fairly underserved middle-class market. Estimates from Datamonitor indicated that banks could have accounted for some 23% of insurance distribution in the United States in 2003.

Savings-oriented products — including individual annuities, ordinary life insurance, and credit life insurance (which pays off certain debts in the event of the policyholder's death) — currently constitute the bulk of insurance sales made through banks and securities brokers. However, sales of some P/C products — like personal auto coverage and homeowners' policies — are growing. Because these products are like commodities, they are well suited to the banking distribution channel.

The ability to discover and leverage alternative distribution channels is a critical success factor for property-casualty insurers. That fact is not lost on the Hartford Financial Services Group. This leading insurer has joined forces with a number of large banks to provide personal automobile and homeowners' insurance coverage to the banks' retail and credit card customers.

The losers in this scenario are independent insurance agents. In fact, many insurers have become reluctant to disclose the level or scope of their distribution agreements with banks for fear of jeopardizing their relationships with their independent agents. As more and more insurers team up with banks, however, independent agents will have no choice but to carve out other niches, such as focusing on the high-end insurance market for wealthy individuals or selling insurance to lower-income individuals.

Despite the fact that a number of banks already offer an array of personal lines insurance, we do not anticipate that many banks will graduate to selling commercial property-casualty insurance, particularly the more complex liability lines of coverage. Nevertheless, distribution through the

bank channel is something with which most personal lines writers will soon have to contend. For companies that recognize that the lines separating the various sectors of the financial services industry are blurring, this could be a positive trend and a means of expanding their distribution systems. For those that refuse to acknowledge the presence of banks in the insurance marketplace, the consequences could be dire.

## HOW THE INDUSTRY OPERATES

The property-casualty (P/C) insurance industry is essentially a risk-bearing enterprise. In the event of a loss, insurance is a means by which the burden of that loss — whether related to the destruction of property or an incurred liability — is shared. Typical property-casualty policies include auto coverage, workers' compensation coverage, homeowners' coverage, and others.

There are two kinds of ownership structures in the P/C industry: mutual and stock. A mutual insurance company is owned by its policyholders, and its capital is called policyholders' surplus. State Farm Group — the largest property-casualty insurer in the United States, based on premium volume — is a mutual insurance company.

The second-largest P/C insurer, Allstate Insurance Group, is a stock insurance company. Investors (that is, shareholders) are issued stock as evidence of their ownership interest, which is represented by shareholders' equity.

### The money flows in...

Regardless of an insurance company's ownership structure, the insurance business is one of shared risk. Insurers collect payments in the form of premiums from people who face similar risks. A portion of those payments is set aside to cover policyholders' losses. Therefore, earned premiums are typically an insurer's primary revenue source.

At the time a policy is issued, it is recorded on the insurer's books as a written premium. Then, over the life of the policy, the premium is "earned," or recognized as revenue, on a fractional basis. These premiums are classified as deferred revenues and assigned to an unearned premium reserve,

which is listed as a liability on an insurer's financial statement.

There's usually a lag of about 12 months between the time a policy is written and the time the full premium is recognized as revenue. For example, a \$600 premium for a year of auto insurance coverage would be "earned" by the insurer at the rate of \$50 a month for 12 months. (The flow of funds is shown in detail in the cash flow diagram.)

After premiums, the second-largest component of insurer revenues is investment income. This is derived from investing the funds set aside for loss reserves and unearned premium reserves and from policyholders' surplus or shareholders' equity.

The third, and usually smallest, revenue component is realized investment gains; this component is the most volatile and hardest to predict. Realized investment gains arise from the sale of securities (usually stocks and bonds) in an insurer's investment portfolio. Because the timing and magnitude of the gains depend on conditions in the securities markets, which by their nature are dynamic, it is difficult to forecast realized investment gains.

### ...and the money flows out

An insurer's revenue must cover a variety of expenses. One expense is the commission paid to the insurance broker, agent, or salesperson for selling a policy; this is usually deducted immediately from the collected premium. The insurance company generally accounts for this commission by deducting it from its policyholders' surplus account and crediting it to the unearned premium reserve.

After commissions are paid, premium dollars are used to cover a variety of expenses. The largest expense facing a property-casualty insurer is losses, also referred to as policyholder claims. Funds are also used to pay claims-related expenses and loss adjustment expenses, including insurance adjusters' fees and litigation expenses. Insurers also face expenses related to the underwriting process, such as salaries for actuarial staff. The underwriting profit (or loss) is determined by subtracting these expenses from earned premiums.

Like most other companies, insurers incur various other operating expenses and interest costs. Pretax profits are calculated by subtracting these expenses from underwriting

profits. Finally, after-tax (or net) income is derived by taking pretax profits and subtracting dividends and federal and state income taxes.

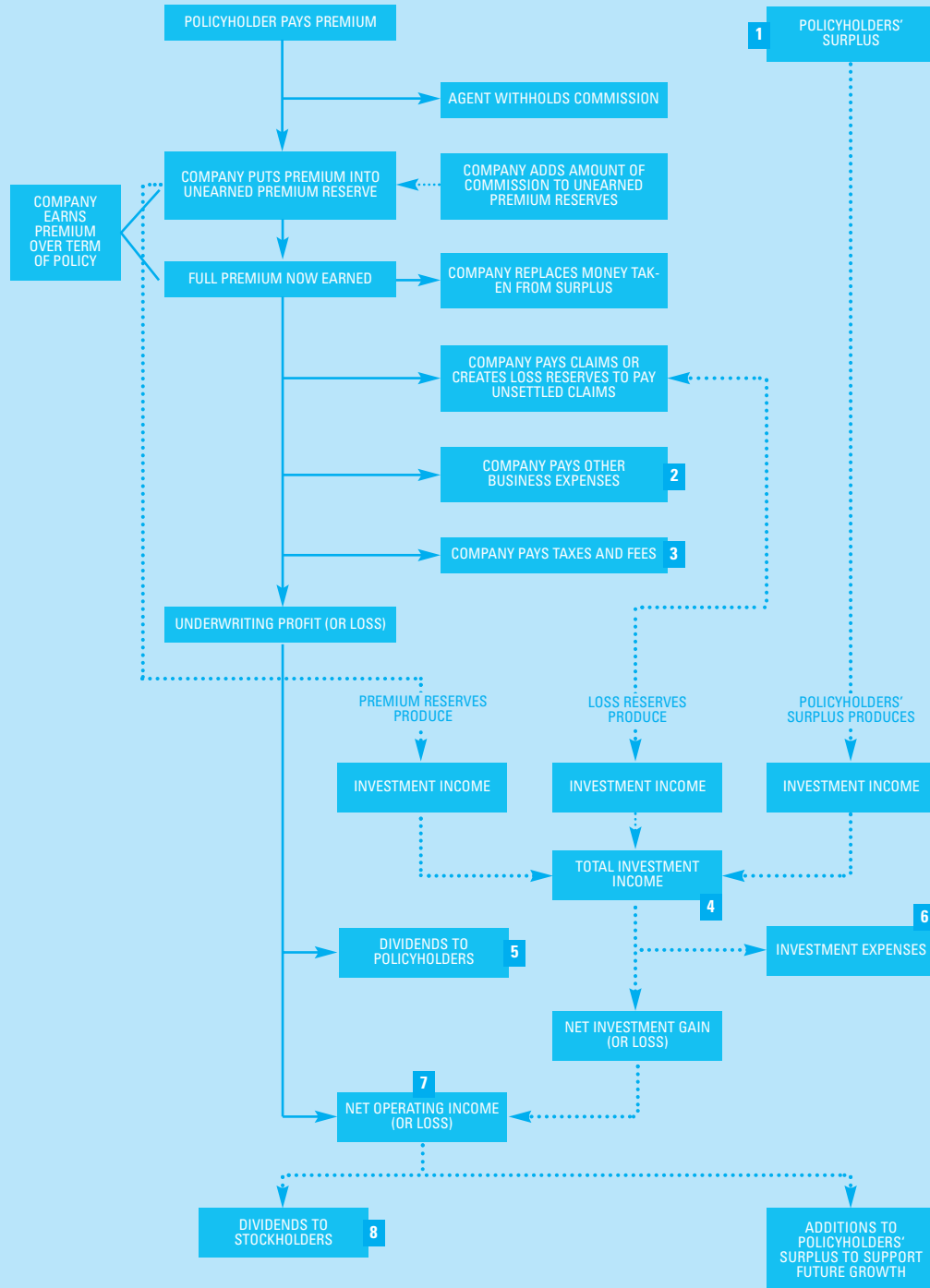
According to the most recent A.M. Best survey of approximately 22,400 property-casualty insurers, net written premiums for this representative group (which serves as a proxy for the entire P/C industry) rose nearly 15% to \$378.9 billion in 2002, from \$329.6 billion in 2001 (as restated). Net earned premiums advanced some 14.8% to \$357.5 billion in 2002, from \$311.5 billion in 2001 (as originally reported).

Underwriting results improved considerably over 2001 results, which were hurt by losses related to the September 11 terrorist attacks. According to initial estimates from the Insurance Services Office (ISO), an industry research and data collection organization, insured losses from the terrorist attacks were expected to range from \$30 billion to \$70 billion, a total that has not subsequently been changed. However, many of these costs will likely be absorbed by overseas reinsurers (and thus are not reflected in the aggregate underwriting data contained herein).

According to the ISO's property claim services unit, 25 catastrophes occurred in 2002 that produced losses of \$5.9 billion. (A catastrophe is defined as an incident or series of incidents causing insured losses of \$25 million or more.) This contrasts rather sharply with 2001, when 20 catastrophes produced reported losses of \$28.1 billion. Included in the 2001 catastrophe losses was an estimated \$9 billion in reported losses from the September 11 terrorist attacks. (Note: This number will continue to rise over time as more claim information becomes available.) Consequently, total incurred losses rose a modest 5.0% to \$246.2 billion in 2002, from \$234.5 billion in 2001. Incurred losses in 2001 rose nearly 17% from 2000's levels. Loss adjustment expenses (which are the expenses incurred in settling claims) increased a surprising 11.5% to \$45.6 billion in 2002, from \$40.9 billion in 2001. Other underwriting expenses advanced 11.0% to \$95.7 billion in 2002, from \$86.2 billion in 2001.

The modest rise in incurred losses was partly offset by the double-digit increase in both loss adjustment expenses and other underwriting costs. As a result, total underwriting expenses were \$387.2 billion in 2002, up



**CASH FLOW DIAGRAM—PROPERTY-CASUALTY INSURANCE COMPANIES***(A simplified model)***1** The excess of assets over liabilities.**2** Overhead costs — rent, salaries, etc.**3** Federal, state, local taxes, licenses, and fees.**4** Includes interest, dividends, rents, and realized capital gains.**5** On certain lines only.**6** Costs of operating the company's investment program.**7** If underwriting loss exceeds investment gain, there will be a net operating loss.**8** Applies only in the case of capital stock companies.

Source: Insurance Information Institute.

## PROPERTY-CASUALTY OPERATIONS

(In millions of dollars)

	1999	2000	2001	2002*
Net premiums written	286,934	299,652	323,510	369,673
% change from previous year	1.9	4.4	8.0	14.3
Net premiums earned	282,791	294,024	311,529	348,507
% change from previous year	5.3	8.8	16.7	1.8
Incurred losses	184,609	200,943	234,518	238,815
Loss adjustment expense	37,660	37,838	40,882	44,825
Underwriting gain/loss	(23,076)	(31,220)	(52,602)	(30,840)
Net investment gain	51,871	56,908	44,370	36,010
Pretax operating income	14,426	9,857	(13,800)	5,581
Net income after taxes	21,865	20,559	(6,970)	3,046

\*Latest available.

Source: Insurance Services Office.

7.0% from \$361.8 billion in 2001.

Nevertheless, the underwriting losses for this group narrowed in 2002, to \$29.7 billion, from \$50.2 billion in 2001.

Contributions from investment activities were mixed in 2002, owing to a continued weak equity market and a relatively low interest rate environment. Net investment income rose 6.4% in 2002, to \$40.1 billion, from \$37.7 billion in 2001. However, this modest growth was offset by a decline of some 58% in net realized investment gains (to \$2.8 billion in 2002 from \$6.6 billion in 2001). As a result, total investment results declined 3.2% in 2002, to \$42.9 billion, from \$44.3 billion in 2001.

However, the sharp reduction in underwriting losses offset the mixed contributions from investment activities during 2002. As a result, the participants in the A.M. Best survey reported net income of \$9.2 billion in 2002. This represented a significant turnaround from the net loss of just under \$7.0 billion reported in 2001.

### Keep the cash circulating

Many property-related insurance claims are settled relatively quickly. They are often referred to as “short-tail” liabilities because the period between the incident causing the loss — such as a storm that damages a home — and the claim settlement is relatively short. Because of this, P/C insurers maintain the vast majority of their assets in highly liquid investments that can be quickly converted to cash. This liquidity ensures that policyholders can be paid promptly in the event of a loss.

Based on statistics from A.M. Best (which includes both mutual and stock insurance companies in its survey), total assets of the P/C industry equaled \$1.1 trillion at year-end 2002, up 13% from \$972.7 billion at year-end 2001. Of the total year-end 2002 assets, investments constituted 77.4%, or approximately \$851.7 billion. As a portion of invested assets, bonds accounted for 67%. Other investments included common stocks, 16%; preferred stocks, 1%; and cash and short-term investments, 7%. The remaining 9% of the P/C industry’s investments were in mortgage loans, real estate, and other investments.

An insurer derives funds for investment from three primary sources: its loss reserves, its unearned premium reserve, and its policyholders’ surplus. Loss reserves — the funds set aside to pay claims — are by far the largest component of the property-casualty industry’s liabilities. For the insurers in the A.M. Best survey, loss and loss adjustment reserves (including related reinsurance obligations) amounted to \$419.9 billion at year-end 2002, or about 56% of total liabilities of \$750.9 billion.

The second-largest liability on an insurer’s books, and a principal source of investment income, is the unearned premium reserve. At year-end 2002, unearned premiums for the insurers in the A.M. Best survey equaled \$158.6 billion, or just over 21% of total liabilities. The unearned premium reserve represents the liability for that portion of a written premium that has been charged to the policyholder, but has not yet been used. Using our earlier example of the \$600 annual auto insurance premium, the unearned premium reserve would total \$550 at the end of the first month, because \$50 (or 1/12th) of the annual premium had been “earned,” or accounted for as an earned premium on the insurer’s books.

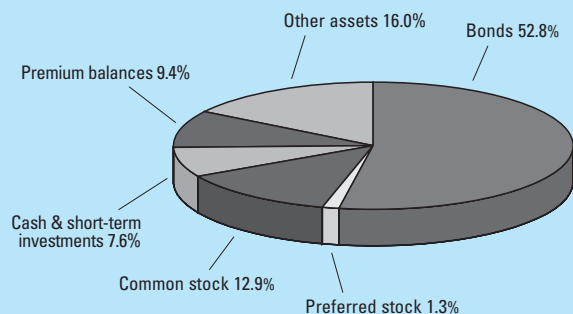
### Loss reserves: the financial buffer

As the largest component of an insurer’s liabilities, loss reserves have an important bearing on financial results. An insurer’s prosperity depends largely on its ability to quantify accurately the ultimate cost of the losses from the risks it assumes.

When reserve levels are too high — that is, when an insurer sets aside too much money to pay future claims — profits appear

### DISTRIBUTION OF ASSETS — 2002\*

(Total US property-casualty industry, in percent)



\*Latest available.  
Source: A.M. Best Co.

lower than they actually are. Consequently, premium rates might not appear high enough to cover losses, causing the insurer to raise its rates unnecessarily. Conversely, if reserves are too low, profits will be inflated, leading an insurer to lower its rates inappropriately. In either situation, once losses develop, inaccurate reserve levels will ultimately have to be adjusted. Such erratic accounting adjustments can make an insurer's financial position seem unstable.

Establishing premium and loss reserve levels require an insurer to estimate the ultimate value of future losses, which is extremely difficult to do accurately. Along with the unpredictability of natural disasters, forecasts of future losses are subject to several other variables, including (but not limited to) real economic growth, inflation, interest rates, sociopolitical trends, judicial rulings, and voter initiatives.

Moreover, the trend in recent years toward a greater proportion of the insurance business being written in casualty lines has made the reserving process even more difficult. It is considerably harder to estimate the ultimate losses from casualty lines than from property lines such as homeowners' coverage, because casualty lines have "long tails." That is, the period between the origination of the policy, the event leading to a claim, and the subsequent payment of that claim may be years or even decades. Inflation can have a highly negative impact on the insurer's eventual costs as the liability's "tail" lengthens. On the plus side, however, this characteristic of casualty lines lets the insurer invest those premium dollars for a longer time.

### Estimating the losses...

The calculation of loss reserves involves considering four different kinds of losses, each with differing levels of uncertainty.

◆ **Losses that have been incurred, reported, and settled, but not yet paid.** These losses are the most certain of the four loss types. Because the size of the ultimate loss has been established, setting aside an accurate reserve level is easiest here.

◆ **Losses that have been incurred and reported, but not settled.** These carry a slightly increased level of uncertainty. Here, the insurer is aware that a loss has occurred, but final payment terms have not yet been established.

◆ **Losses that have been incurred and reported but not settled, due to a liability.** Because such losses usually involve longer-tail liabilities, calculating the ultimate cost of settlement is more difficult.

◆ **Losses that have been incurred, but not reported (IBNR).** These losses carry the most uncertainty. In some cases, insurers know about IBNR losses and try to make preliminary loss estimates. For example, suppose an earthquake hit a certain area on December 30 and a local P/C insurer ends its fiscal year on December 31. In its year-end statements, the insurer could estimate its earthquake-related IBNR loss based on its experience in prior earthquakes.

In other cases, however, IBNR losses emerge years after the damage first occurs. Such losses are very difficult to predict. For example, the various asbestos lawsuits that have recently plagued P/C insurers relate to injuries incurred many years ago, but which were reported much later.

### ...and calculating the loss reserves

Most insurance companies assign the task of establishing appropriate loss reserve levels to their actuarial staffs. Actuaries — specialists trained in mathematics, statistics, and accounting — are responsible for calculating premium rates, reserves, and dividends. They use a variety of quantitative methods to establish loss reserves. The five most commonly used methods are the following:

◆ **Claim-file estimates plus.** This method establishes the estimated liability for reported losses by aggregating pending claim-file estimates (such as estimates being prepared by the claims department), from which payments that have already been made are deducted. To this total are added formula calculations for additional payments on closed claims that will be reopened and for IBNR losses. The sum of the component parts constitutes the full loss liability as of the end of the accounting period.

This method, considered the least sophisticated, is appropriate for property lines in which claim frequency is low and the range of loss costs is sizable. Furthermore, its dependence on claims department estimates exposes it to a degree of subjectivity.

◆ **Extrapolation from accumulated paid losses.** This method indirectly estimates the liability by extrapolating losses paid to date. Although this method is regarded as simple to apply, its use is limited to coverages where payment patterns are relatively consistent.

The percentage of losses paid to ultimate incurred losses is calculated for various stages of development for prior years. From this history, percentages paid are selected for each stage of development. The amount of losses paid to date for the period under review is then divided by the appropriate percentage, to arrive at the estimated ultimate loss cost. The amount of losses paid to date is subtracted from this figure to produce the estimated loss liability.

◆ **Counts and average costs of incurred losses.** This method indirectly establishes the liability for losses from loss counts and average costs. The projected number of loss units is obtained from the number of loss units received to date, based on percentages reported in prior years at the same stage of development.

The average cost of loss units closed to date is calculated and compared with average closed costs of prior years at the same stage of development. The estimated ultimate average cost so derived is then multiplied by the projected ultimate number of loss units, to arrive at the total estimated ultimate loss. Losses paid to date are then subtracted to obtain the estimated liability.

◆ **Counts and average values of unpaid losses.** This method directly establishes the li-

ability from loss counts and average values of unpaid losses. In this case, a selected average value is applied to the number of loss units. If the data are based on reported losses, the selected average value is applied to the number of open loss units, and a separate calculation for IBNR losses is necessary. If the data are based on accidents incurred, the selected average value is based on the total number of open and IBNR losses.

◆ **Loss ratio.** This method estimates the ultimate loss by using an estimated loss ratio. Selected for whatever period of coverage is involved, the ratio is applied to the applicable earned premiums, producing the estimated ultimate losses incurred for that period. Losses paid to date on accidents occurring during the period are deducted from this total to derive the estimated total loss liability.

This overview illustrates the various methods used to quantify an insurer's estimated liability for losses as of the evaluation date. Obviously, a great deal more detail and considerable judgment are involved in applying these methods. Furthermore, no single method is ideal for all situations, and the method chosen by a particular insurer will depend on that company's unique experience and product mix. In fact, many companies use more than one method to ensure a high degree of accuracy and reliability.

For a more detailed discussion of the various loss-reserving methods, Standard & Poor's recommends *Property & Casualty Insurance Accounting*, published by the Insurance Accounting and Systems Association.

## Surplus funds: capital counts

After investment assets and loss reserves, the third largest component of an insurer's balance sheet is policyholders' surplus, analogous to shareholders' equity. At December 31, 2002 (latest available), the insurers in the A.M. Best study had an aggregate surplus of \$291.1 billion, up fractionally from the year-end 2001 surplus of \$289.6 billion.

Policyholders' surplus is one of the indicators that state regulators use to monitor and control insurers' solvency and growth. Industry surplus (sometimes referred to as capital or equity) appreciates or depreciates through retained earnings or losses, unreal-

ized gains or losses from investment portfolios, and additions to investors' capital.

Typically, regulators permit insurers to leverage their surplus to a certain extent, allowing them to underwrite business equal to two to three times the amount of their surplus. Regulators tend to give insurers more leeway on the short-tail property lines than on the long-tail casualty lines, because of the former's relatively greater predictability of underwriting performance.

Thus, as the industry has increased its exposure to casualty lines, its leverage has declined. Industry leverage has also declined because of overcapacity. (Industry surplus leverage is discussed further in the "How to Analyze a Property-Casualty Insurer" section of this *Survey*.)

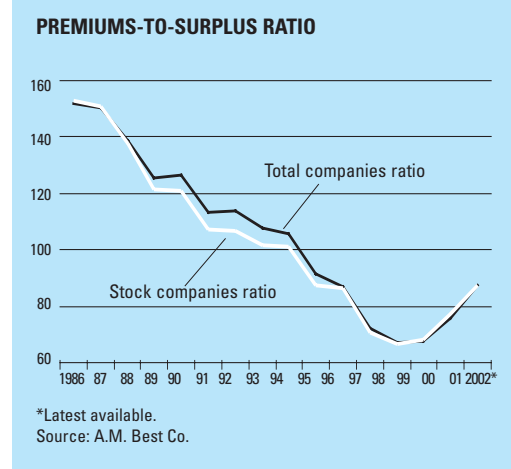
### Two accounting methods used

Property-casualty insurers generally account for their surplus by using statutory accounting principles (SAP), which require them to expense immediately all costs related to writing business, rather than by using generally accepted accounting principles (GAAP), which attempt to match an insurer's income and expenses by prorating the costs of an insurance policy over its assumed life.

Many insurers report their financial results using both accounting systems. They report their results to regulators using SAP; for investors, they use GAAP. (Many analysts, however, also use SAP financial statements when analyzing an insurer.) This difference largely reflects the disparate priorities of shareholders, investors, and regulators. Shareholders and investors are likely to be most interested in a company's ability to earn a profit, while regulators' primary concern is the company's solvency — its ability to meet policyholder obligations.

The primary difference between GAAP and SAP lies in an accounting concept known as the matching principle. Under GAAP accounting, an insurer charges expenses to the period in which they were used to generate revenues. Under SAP accounting, expenses are recognized as soon as they occur.

For example, when an insurer uses SAP, any expenses associated with writing an insurance policy — such as commissions and other underwriting expenses — are immediately deducted from income. Under GAAP



accounting, these same charges are treated as assets — referred to as “deferred policy acquisition costs” — and are amortized over the insurance policy's life. Hence, the more conservative SAP emphasizes a company's solvency. An insurer's income and surplus tend to be lower under SAP than under GAAP, which emphasizes the firm's ongoing profitability.

### Forms of ownership

A property-casualty insurer's ownership structure can take one of two forms: that of a publicly held stock insurance company or that of a mutual insurance company owned by its policyholders. In addition, a company can be structured as a hybrid mutual holding company.

### Stock insurance companies

Stock insurance companies, as their name implies, are owned by shareholders, who can buy or sell shares in the public stock market. The capital of a stock insurance company is called shareholders' equity. Since these companies are publicly held, they are required to file quarterly financial reports with the Securities and Exchange Commission. Thus, obtaining timely financial information about these companies is relatively easy.

As publicly owned companies, these insurance companies are obligated to provide the most favorable return on shareholders' capital. Sometimes this goal may conflict with the interests of policyholders. For example, a stockholder-owned insurer may be under pressure to keep claim costs in line in order

to return a profit to its shareholders. This scrutiny of claims, although certainly legal, may not always be in the best interest of the policyholder, who relies on the insurer to promptly pay its claim.

### **Mutual insurance companies**

Mutual insurance companies, in contrast, are owned by their policyholders. A mutual insurance company's capital is called policyholders' surplus. Because these companies are owned by their policyholders, they are not required to publicly disclose financial information. Although some mutual insurers distribute financial information to policyholders, obtaining financial information about a mutual insurer is more difficult.

In some instances, insurance companies have formed mutual holding companies to combine the benefits of mutual ownership with those of public ownership. In this case, the holding company remains in the hands of the policyholders while shares in the operating subsidiary are sold to the public. This arrangement can lead to conflicting priorities, however, as management seeks to please policyholders, who prefer that the company retain its capital to pay claims, as well as shareholders, who prefer that management use its capital to grow the business and pay dividends.

### **Demutualization**

The process by which a mutual insurance company converts to a shareholder-owned structure is called demutualization. Over the last several years, several of the nation's largest mutual insurers have demutualized. Prudential Financial Inc. completed its initial public offering in December 2001. In April 2000, Metropolitan Life Insurance Co. completed its demutualization on the heels of John Hancock Financial Services Inc., which completed its demutualization in January 2000. (Note: Manulife Financial Corp. acquired John Hancock Financial Services on April 28, 2004.)

The forces behind these high-profile demutualizations differ from those that drove a number of other companies, including The Equitable, to demutualize in the late 1980s. Back then, insurers needed access to the capital markets to sell equity and debt securities in an attempt to boost their sagging capital

bases. At that time, many companies were saddled with illiquid and underperforming real estate loans and assets, which eroded the strength of their capital bases and threatened their solvency. They needed to raise capital in order to survive.

The more recent spate of demutualizations was driven by insurers' need to increase their operating and financial flexibility. One aspect of this is the ability to issue stock. Although the merger and acquisition boom of the late 1990s has slowed considerably, the ability to acquire another company through the issuance of stock (the currency of choice in most deals) is a critical success factor for many companies. Furthermore, in this era of rewarding performance with stock options, many mutual insurers believed they were at a disadvantage in recruiting and retaining top management talent by not being able to offer this benefit to employees.

### **Lines of coverage**

Although property-casualty insurance is available on a wide variety of coverages, several lines constitute the bulk of industry premium volume, as shown in the chart entitled "Property-Casualty Industry's Product Line Distribution."

◆ **Automobile coverage.** This is the largest P/C line; it covers both physical (property) damage and car owners' liability. According to A.M. Best, this sector accounted for 43.5% of the industry's net written premium volume in 2002.

Automobile coverage (both personal and commercial) has long dominated the industry's product mix. Its growth over the past 20 years has been fueled by the adoption of mandatory automobile insurance in many states and by escalating litigation and medical care costs.

◆ **Workers' compensation.** Another major line of business for the P/C industry is workers' compensation, which accounts for just under 10% of premium volume. This business line insures organizations that are required by state laws to compensate employees who are injured or disabled because of an occupational hazard. It also helps compensate families of employees killed on the job.



## CLASSIFICATION OF NET PREMIUMS — LEADING LINES FOR STOCK PROPERTY-CASUALTY INSURANCE COMPANIES

(Premiums written, in millions of dollars and as a percentage of total)

YEAR	†AUTO LIABILITY		†AUTO PHYS. DAMAGE		WORKERS' COMPENSATION		**MISC. LIABILITY		STRAIGHT FIRE		HOMEOWNERS' MULTIPLE PERIL		COMMERCIAL MULTIPLE PERIL	
	WRITTEN	%	WRITTEN	%	WRITTEN	%	WRITTEN	%	WRITTEN	%	WRITTEN	%	WRITTEN	%
2002*	99,197	26.3	64,881	17.2	36,518	9.7	36,153	9.6	7,134	1.9	40,013	10.6	25,384	6.7
2001	89,709	27.2	59,967	18.2	31,373	9.5	25,945	7.9	4,889	1.5	35,172	10.7	22,209	6.7
2000	82,766	27.3	56,387	18.6	28,136	9.3	24,096	7.9	4,631	1.5	32,414	10.7	19,817	6.5
1999	82,469	28.5	54,294	18.7	24,607	8.5	22,292	7.7	4,646	1.6	30,662	10.6	18,931	6.5
1998	83,755	29.5	51,798	18.2	25,683	9.0	22,563	7.9	4,739	1.7	28,997	10.2	18,974	6.7
1997	83,427	29.8	48,401	17.3	26,512	9.5	23,265	8.3	4,919	1.8	26,915	9.6	18,954	6.8
1996	80,679	29.7	44,734	16.5	27,714	10.2	22,737	8.4	5,293	1.9	25,448	9.4	18,919	7.0
1995	77,558	29.4	41,611	15.8	29,538	11.2	21,698	8.2	5,176	2.0	23,987	9.1	18,844	7.1
1994	74,129	29.0	39,438	15.5	32,708	12.8	21,810	8.5	5,053	2.0	22,556	8.8	17,812	7.0
1993	71,471	29.0	38,376	15.6	34,261	13.9	20,509	8.3	4,549	1.8	21,549	8.7	17,310	7.0

\*Latest available. †Bodily injury and property damage combined. ‡Fire-theft and collision combined. \*\*Includes product liability, malpractice, etc.  
Source: A.M. Best Co.

During the 1960s and 1970s, the growth in this business line was helped by changes in certain state laws that increased mandated coverage and by the general upgrading of benefit levels. However, in the past several years, this market has contracted as corporations and local governments have sought less costly means of providing this coverage, such as self-insuring. Some insurers have also withdrawn from this line of business in response to poor underwriting results.

◆ **Other lines.** The remaining 47% or so of the market comprises a variety of types of coverage, including homeowners' multiperil coverage, commercial multiperil coverage, and an array of liability coverages.

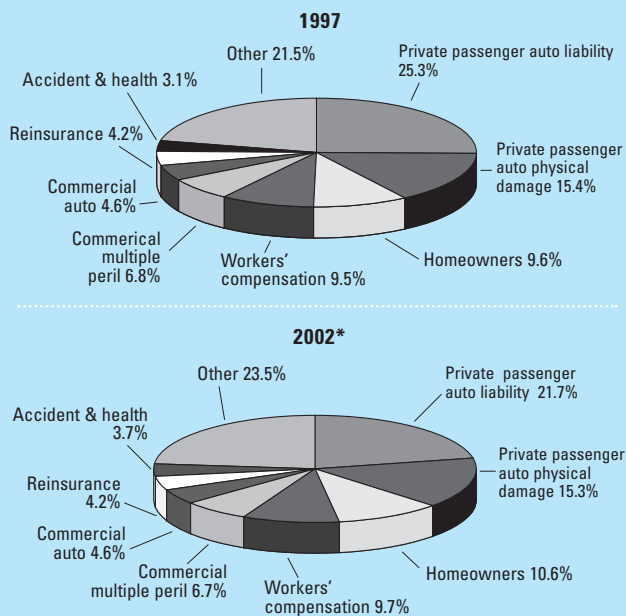
### Getting policies to the people

Insurance companies distribute their personal and commercial policies through either direct selling systems or agency systems. In a direct selling distribution system, the insurance company (sometimes referred to as a direct writer) contacts its customers ("insureds") through its own employees. Within this framework, the insurer sells policies through a number of outlets, including direct mail and company-run agencies.

Under an agency system, the insurer contracts outside agents to sell its policies in exchange for a commission. Some agents may sell only a single insurer's policies ("exclusive agents"), while others ("independent agents") may offer policies from various insurance companies.

While there are advantages and disadvantages to both systems, the tradeoff is between costs and control. A direct selling system can be expensive to establish and operate, but it gives an insurer more control over the distribution process. The agency system reduces the amount of control an insurer has over each aspect of the distribution system, but it usually offers an established network through which the insurer can distribute its products. This is es-

### PROPERTY-CASUALTY INDUSTRY'S PRODUCT-LINE DISTRIBUTION (In percent, by net premiums written)



\*Latest available.  
Source: A.M. Best Co.



pecially helpful to small and regional insurers without the means to establish their own distribution network.

### Regulation, competition hold insurers in line

The insurance industry is regulated on a state-by-state basis. Each of the 50 states and the District of Columbia has an insurance commissioner, who grants insurers operating licenses letting them conduct business within that state.

State regulators serve three primary functions. First, they monitor the financial condition and claims-paying ability of each insurance company operating in their state. Second, they serve as consumer watchdogs, ensuring that policyholders are not overcharged or discriminated against. Finally, regulators try to ensure that essential insurance coverage is readily available to all consumers.

The National Association of Insurance Commissioners (NAIC), based in Kansas City, Missouri, coordinates the activities of state insurance commissioners. Founded in 1871 as the National Convention of Insurance Commissioners, the NAIC undertook the formulation of uniform accounting procedures as one of its first actions. Today, one of the NAIC's main functions is to develop and improve insurance reporting and accounting standards and practices. These actions are intended to improve state regulators' knowledge of the financial condition of insurers in their jurisdiction.

Insurance companies are required to file a set of financial statements each year with regulators in every state in which they operate. These records, called annual statements, use statutory accounting terms to outline the company's profits, losses, and overall financial condition.

Other forms of regulation and control also govern the insurance industry. For instance, publicly held insurance companies — those that issue stock — are subject to regulation by the Securities and Exchange Commission (SEC).

Finally, the intense level of competition among industry participants in all lines also serves as a measure of control. Competition helps keep pricing in line and prevents any one participant from becoming too powerful.

## KEY INDUSTRY RATIOS AND STATISTICS

For purposes of formulating industrywide benchmarks, Standard & Poor's here defines the property-casualty insurance industry as comprising the companies that report their operating statistics to A.M. Best; there were approximately 2,402 such companies in 2002 (latest available).

The following three ratios are derived from statistics available in A.M. Best Co.'s annual publication, *Aggregates & Averages*.

► **Return on assets (ROA).** This is a measure of profitability; it's equal to net income divided by average total assets. The ROA for most property-casualty insurers typically ranges from 2.0% to 5.0%.

► **Return on equity (ROE).** Usually considered in tandem with ROA, ROE is another measure of profitability. For a stockholder-owned insurance company, ROE is calculated by dividing net income by average shareholders' equity.

To calculate the ROE for the entire property-casualty insurance industry (which includes mutual insurance companies), the denominator in this equation would be policyholders' surplus, not shareholders' equity. Policyholders' surplus is a statutory accounting term that is generally analogous to shareholders' equity. The return on equity/surplus for property-casualty insurers typically ranges from 8% to about 18%. Most insurers strive to earn an ROE of 12% to 15%. During the five years from 1998 to 2002, the average ROE for insurers in the A.M. Best universe was 1.8%. This rather meager performance largely reflected the impact of negative returns in 2001 and 2002.

► **Net investment yield.** This is a measure of investment performance; it is typically calculated as net investment income divided by average invested assets. Investment yields typically range from under 4% to well above 12%, depending on the mix of invested assets in an insurer's portfolio. For the property-casualty industry, the average yield on invested assets was 4.9% in 2002, unchanged from 2001.

The next two ratios, which measure underwriting performance, are derived from

data published quarterly by the Insurance Services Office (ISO).

► **Net premiums written to surplus.** This ratio measures the extent to which the industry (or an insurer) has leveraged its capital to write business. Sometimes referred to as a measure of capacity utilization, it is equal to net written premiums divided by policyholders' surplus.

Typically, regulators permit an insurer to have a ratio of net written premiums to surplus of 2-to-1. In other words, insurers would be permitted to write \$2 in premiums for every \$1 in capital. Despite the growth in written premiums that occurred in the 12 months ended December 31, 2003, the industry remained somewhat underleveraged. At December 31, 2003, the ratio of net written premiums to policyholders' surplus was 1.17-to-1. In other words, the industry wrote \$1.17 worth of premiums for every \$1 in capital.

► **Combined ratio.** A key measure of underwriting performance, the combined ratio is calculated by adding three figures: the loss ratio (losses plus loss adjustment expenses, divided by earned premiums), the expense ratio (other underwriting expenses divided by written premiums), and the dividend ratio (policyholder dividends divided by earned premiums). A combined ratio of 100% or less indicates an underwriting profit; in excess of 100%, it signals an underwriting loss.

Companies strive to earn a profit from underwriting, but only a small percentage actually achieves this goal. According to a study by the ISO, between 1952 and 1998, the industry earned a profit from underwriting — and achieved a combined ratio below 100% — in just 15 of those 47 years. Until the first half of 2003, the last time this happened was in 1978, when the industry's combined ratio equaled 97.5%.

A typical range for combined ratios is 100% to 110%. The loss ratio usually ranges from 60% to 80%, and the expense ratio from 25% to 35%. The dividend ratio usually ranges from 1.0% to 2.0%.

For the 12 months ended December 31, 2003, the industry's combined ratio equaled 100.1%, compared with 107.3% in the year ended December 31, 2002. The combined ratio for 2003 consisted of a loss ratio of 74.7% (versus 81.4% in the 2002 period),

an expense ratio of 24.9% (25.4%), and a dividend ratio of 0.5% (0.6%).

## HOW TO ANALYZE A PROPERTY-CASUALTY INSURANCE COMPANY

When analyzing a property-casualty (P/C) insurer, consider three central points: its profitability, or ability to make money; its liquidity, or ability to convert assets into cash to pay claims and meet other expenses; and its leverage, or the extent to which it uses its capital to produce business.

As with the markets for most other goods and services, the P/C insurance market functions within supply and demand curves. Demand for insurance is fairly stable and inelastic: it is influenced by growth in the economy (as measured by gross domestic product), the inflation rate, and the need to protect assets. The supply curve, however, moves primarily with interest rates.

### Pricing moves inversely with interest rates

Theoretically, when interest rates rise, insurers are willing to provide more insurance at the same price, because each premium dollar generates more investment income for the insurer. Thus, insurance prices decline until additional demand is stimulated or until it becomes unprofitable to provide coverage, prompting insurers to withdraw. Either way, supply and demand are brought back into balance.

The fundamental relationship between insurance pricing and interest rates, therefore, is that prices increase when interest rates fall and decline when interest rates rise. The magnitude of changes in price varies with the magnitude of changes in interest rates.

Price and premium growth levels are also influenced by competitive pressures within the industry and by each firm's capacity to underwrite. The industry is competitive and has relatively few barriers to entry, so companies tend to overreact to interest rate changes, either overpricing or underpricing as situations warrant. However, in recent years, this theory did not match reality. During a period of historically low interest rates, insurance pricing also remained competitive. This is largely attributable to an oversupply of un-

derwriting capacity, or capital, that remained within the insurance marketplace.

Prospects for inflation also play an important role in insurance prices. If claim costs are expected to rise because of inflation, a higher level of income will be needed to cover these potentially higher costs in the future. Thus, insurance companies must incorporate estimates of future inflation into their pricing structures.

When there's a wide range of inflation expectations, companies with lower-than-average estimates of future inflation may offer their products for below-average prices. Of course, insurers can often garner market share when their policies are priced below those of their competitors. Therefore, overall price trends tend to move toward the levels set by companies with a less inflationary outlook.

## Predicting profits

Two broad measures of profitability that are applicable to P/C insurance companies are return on assets (ROA) and return on equity (ROE). ROA is net income divided by average total assets. A typical range of ROAs for the P/C insurance industry is somewhere between 0.5% and 2.0%, with the average somewhere around 1.5%. ROE is calculated by dividing the insurer's net income by average shareholders' equity. Most insurers strive to achieve an ROE of at least 15%.

A property-casualty insurer's profitability depends primarily on two components: underwriting income and investment income. Below we discuss each of these components of an insurer's operating income.

## Principles of underwriting

The first element to consider when analyzing underwriting results is the rate of written premium growth. It should be compared with industry data to judge how a company stacks up against its peers.

Pay careful attention to the circumstances surrounding the rate of premium growth. For example, if a company expands its written premium base at 10% a year while the overall industry is growing at 6% a year, that company would appear to be outperforming its peer group. Presumably, the stock market would award that firm a higher valuation than some of its slower-growing counterparts would enjoy. However, if the insurer is achieving premium growth by following risky underwriting

standards — such as underpricing policies to gain market share or writing a great deal of business in a high-risk coverage line avoided by other insurers — the insurer's valuation would have to be adjusted downward.

Conversely, a company growing its premium base at a rate slower than the overall industry could be doing so because it is limiting its exposure to an unattractive class of business. For example, a number of insurers have reduced their exposure to workers' compensation insurance in response to that line's adverse claim trends. These insurers may have posted minimal written premium growth in recent years, but many have seen their profitability improve after purging these loss-laden business lines.

A final factor that affects a company's premium growth rate is the extent to which an insurer uses reinsurance, the practice of transferring some of its risk — and premium income — to reinsurance companies. In an attempt to offset slowing premium growth in the past, some insurers have reduced the level of premiums that they cede to reinsurers. Using less reinsurance lets an insurer keep more of each premium dollar, so a reduced level of reinsurance may enhance year-to-year premium growth comparisons. At the same time, using less reinsurance removes the protection it affords, potentially exposing the primary insurer to a large financial claim.

◆ **The combined ratio.** To evaluate an insurer's underwriting performance, many analysts use a statistical measure called the combined ratio. This ratio equals the sum of the loss ratio, the expense ratio, and the dividend ratio, which are described below. A combined ratio below 100% indicates an underwriting profit; one above 100% means an insurer has incurred an underwriting loss. Unless otherwise stated, most companies calculate these ratios using statutory accounting principles.

◆ **The loss ratio.** The loss ratio measures claims cost experience. It is derived by dividing losses and loss adjustment expenses by earned premiums. It typically ranges from 60% to 80%, but it can soar during a period of heavy catastrophe losses.

◆ **The expense ratio.** The expense ratio measures how cost-effectively an insurer

### UNDERWRITING EXPERIENCE — LEADING LINES FOR STOCK PROPERTY-CASUALTY INSURANCE COMPANIES

YEAR	STRAIGHT FIRE RATIOS			HOMEOWNERS' MULTIPLE PERIL RATIOS			COMMERCIAL MULTIPLE PERIL RATIOS (NONLIABILITY PORTION)			COMMERCIAL MULTIPLE PERIL RATIOS (LIABILITY PORTION)			\$WORKERS' COMPENSATION RATIOS			†AUTO LIABILITY RATIOS			‡AUTO PHYS. DAMAGE RATIOS		
	LOSS	EXP.	COMB.	LOSS	EXP.	COMB.	LOSS	EXP.	COMB.	LOSS	EXP.	COMB.	LOSS	EXP.	COMB.	LOSS	EXP.	COMB.	LOSS	EXP.	COMB.
2002*	59.1	27.9	87.1	80.4	28.5	109.3	62.4	33.0	97.2	86.1	30.1	116.2	87.1	22.5	112.2	86.1	23.6	110.1	72.2	23.1	95.9
2001	83.1	34.7	118.0	91.9	29.4	121.7	83.9	33.0	117.0	87.7	33.0	120.8	92.4	25.0	120.9	88.1	23.4	112.0	78.2	23.6	102.3
2000	75.9	37.7	113.7	80.4	30.6	111.4	79.6	35.3	115.0	80.3	34.7	115.0	89.6	25.8	120.8	88.1	24.3	113.7	78.0	24.2	103.6
1999	67.5	39.1	106.8	77.4	30.3	108.2	84.6	37.7	122.4	77.6	35.4	113.1	84.3	27.5	118.5	81.3	24.4	106.6	73.9	24.3	99.0
1998	69.3	38.0	107.7	77.8	30.8	109.4	77.8	37.3	115.3	90.1	34.8	125.0	78.2	26.3	111.2	76.4	23.5	102.0	73.8	23.7	99.7
1997	59.5	37.2	97.1	69.0	31.1	101.0	76.0	37.5	113.6	73.4	35.1	108.5	72.1	25.6	103.7	75.0	22.8	99.8	74.3	22.6	99.0
1996	58.6	35.4	94.2	91.4	29.8	121.7	80.1	36.6	116.8	84.9	34.8	119.8	72.1	24.9	102.4	77.4	21.9	100.3	79.6	21.7	102.2
1995	69.9	34.5	104.8	81.7	30.6	112.7	69.3	36.7	106.2	84.5	34.4	119.0	69.8	22.7	99.5	79.7	22.1	103.0	75.3	21.9	98.4
1994	69.9	36.5	106.6	87.2	30.8	118.4	83.0	37.3	120.3	81.9	35.3	117.2	73.6	21.0	101.6	83.1	21.8	105.7	70.9	21.7	93.4
1993	66.6	39.0	105.9	82.1	31.0	113.6	66.8	37.5	104.3	93.6	35.2	128.9	85.2	19.3	109.5	85.4	22.4	108.6	66.7	22.1	89.7

\*Latest available. NA-Not available. Exp.-Expense. Comb.-Combined. \$Including state funds. †Bodily injury and property damage combined. ‡Fire-theft and collision combined.

Source: A.M. Best Co.

writes new business. It is derived by dividing operating expenses by written premiums. It typically ranges from 25% to 35%.

◆ **The dividend ratio.** The dividend ratio, the smallest component of the combined ratio, is obtained by dividing policyholders' dividends by earned premiums. It typically ranges from 1% to 2%. (The combined ratio is often presented excluding the dividend ratio. This is the case in the "Underwriting experience" and "Premium volume and underwriting ratios" tables.)

#### Playing the investment field

Investment income is an important source of profits for property-casualty insurers. Theoretically, investment income should be

used to provide financial protection against unforeseen and unanticipated underwriting losses. Many insurers, however, have come to rely on investment income to remain profitable. When evaluating an insurer's investment portfolio, analysts review a company's asset allocation strategy, making sure its mix of invested assets is appropriate for the type of business it writes.

For most property-casualty insurers, this process is fairly straightforward: the typical P/C insurer maintains most of its invested assets in relatively liquid fixed-income or equity securities that are easily converted into cash. This is because most P/C insurance claims are settled in a relatively short amount of time. Within each asset class, such as stocks or bonds, a review of asset quality and diversification is necessary. To help in the analysis of asset quality, insurers usually provide the debt rating of bonds in their portfolio or an average debt rating for their entire portfolio.

Two important ratios used in analyzing investment results are the investment yield and the total return on the portfolio. Investment yield is usually calculated as the net investment income during a certain time period, divided by the portfolio's average value during the same period. Total return is usually calculated as net investment income plus or minus realized and unrealized gains, divided by beginning market value of the portfolio, plus or minus the weighted average of additions or dispositions.

### PREMIUM VOLUME AND UNDERWRITING RATIOS FOR THE TOTAL US PROPERTY-CASUALTY INDUSTRY

YEAR	PREMIUMS WRITTEN	PREMIUMS EARNED	†LOSS RATIO (%)	‡EXPENSE RATIO (%)	COMBINED RATIO (%)
	MILLIONS OF DOLLARS				
2002*	377,163	355,738	81.6	25.2	106.8
2001	329,249	317,109	88.5	26.6	115.1
2000	303,222	297,398	81.5	27.5	109.0
1999	289,649	285,435	78.8	27.9	106.7
1998	284,204	280,313	76.5	27.6	104.1
1997	279,686	274,668	72.8	27.1	99.9
1996	271,845	266,550	78.4	26.3	104.7
1995	263,656	258,075	78.9	26.1	105.0
1994	255,189	248,685	81.1	26.0	107.1
1993	246,428	240,234	79.5	26.2	105.7

\*Latest available. †Incurred to premiums earned. ‡Incurred to premiums written. Source: A.M. Best Co.

## Cash flow and liquidity

Liquidity is another key benchmark for analyzing a property-casualty insurer, because of the insurer's need to pay claims promptly. An insurer's sources of liquidity arise from underwriting cash flow, investment cash flow, and asset liquidation cash flow. These are all considered internal sources because they are generated by the insurer's operations.

Because of the somewhat unpredictable nature of the P/C insurance business, cash flow from underwriting activities is probably the most volatile element of an insurer's total cash flow. Nevertheless, the underwriting cash flow for most insurers is usually positive; when combined with the cash flow from investment activities, most insurers end up with a substantial positive cash flow.

## Looking at leverage

For property-casualty insurers, leverage refers to how the company uses its surplus, or capital, to write policies. The ratio of net written premiums to policyholders' surplus is usually a good indicator of the industry's capacity utilization.

Historically, insurers leveraged their surplus by a multiple of two to three, depending on the types of business they underwrote. For example, an insurer with \$10 million of surplus could probably write \$20 million to \$30 million of annual premiums. Regulators tend to give insurers more leeway in surplus leverage on shorter-tail property lines of coverage than on longer-tail liability lines, because the former have greater predictability. (The terms "short-tail" and "long-tail" refer to the time between the occurrence of a claim and its settlement; short-tail claims can usually be settled more quickly than long-tail claims.)

Thus, as the industry's exposure to casualty lines has increased, surplus leverage has decreased. Overcapacity in the insurance business has also caused surplus leverage to decline, as have strong investment returns. Thus, while regulators may still use a 2-to-1 leverage of surplus as a benchmark, this benchmark has to be considered against a backdrop of industrywide "underleverage." In fact, industry leverage had been below 1-to-1 from the mid-1990s until recently. However, in the wake of the

September 11 terrorist attacks, industry leverage has increased somewhat because of the payment of these extraordinarily large claims.

Based on data obtained from A.M. Best, a provider of insurance company ratings and information, and the Insurance Services Office, an industry research and data collection organization, the ratio of net written premiums to policyholder surplus was 1.25-to-1 at June 30, 2003 and 1.29-to-1 at December 31, 2002; both of which were up slightly from 1.12-to-1 at December 31, 2001. Using a benchmark leverage ratio of two times surplus, then the capital required to support the \$369 billion in net premiums written in the 12 months ended December 31, 2002, would be approximately \$184.5 billion. At December 31, 2002, the industry's actual surplus level stood at more than \$285 billion. The difference between actual and required surplus is more than \$100 billion; this is called excess surplus, or excess underwriting capacity.

Viewed another way, if we use a two-times-surplus leverage ratio, that excess capital could support more than another \$200 billion in written premiums. Against this backdrop of an industrywide underleveraged surplus, however, an insurer that leveraged its surplus by more than two times would probably be considered relatively highly leveraged. ■



## GLOSSARY

**Acquisition cost** — The amount of money paid by an insurance company for the purchase of another business; it includes commissions to agents and brokers and, in some cases, field supervision expenses.

**Actuary** — An insurance professional whose job is to estimate statistical risks, set premium levels, and analyze other technical aspects of insurance.

**Administrative services only (ASO) agreement** — An agreement under which an insurer provides a client with such services as actuarial work, benefit plan design, claims processing, financial advice, and report preparation. The client typically accepts the underwriting risk or self-insures.

**Agent** — A person who sells insurance policies as a representative of the insurer. An independent agent represents two or more underwriters, while an exclusive agent may be an employee or commissioned representative of a single company.

**Broker** — A producer who legally represents the buyer of insurance rather than the underwriting company. The broker deals with either agents or underwriting companies to arrange the required coverage.

**Capacity** — The level of underwriting business an insurer can support, based on its ability or willingness to accept risks, with certain protection limits.

**Captive insurer** — An insurance organization established by an entity to insure its own risks.

**Catastrophe** — An incident or series of related incidents causing insured losses of \$25 million or more. (Note: Prior to 1997, a catastrophe was defined as an event or series of related events that caused insured losses of \$5 million or more.)

**Cede** — The transfer of part of an insurer's liability to a reinsurance company. The insurer "cedes" its liability; the reinsurer "assumes" the liability.

**Combined ratio** — A financial measure of underwriting performance used in the insurance industry; it's the sum of the loss ratio, the expense ratio, and the dividend ratio. A combined ratio of less than 100% generally indicates an underwriting profit, while a ratio in excess of 100% indicates an underwriting loss.

**Convention statement** — Documents filed with state insurance departments detailing the financial statistics of individual insurance companies. Convention statements are prepared using statutory accounting principles, rather than generally accepted accounting principles.

**Dividend ratio** — Policyholders' dividends as a percentage of earned premiums. It is a component of the combined ratio.

**Earned premium** — Portion of a premium for which the insurer has already provided protection to the policyholder.

**Expense ratio** — Operating expenses as a percentage of premiums written, calculated on a statutory basis. It measures an insurer's efficiency in writing new business and is a component of the combined ratio.

**Generally accepted accounting principles (GAAP)** — An accounting method that, among other things, attempts to match income and expenses by prorating costs over the assumed life of an insurance policy. The GAAP method is used in the audited financial statements of publicly held companies. (See "statutory accounting principles.")

**Insurance examiner** — A state insurance department representative assigned to participate in the official audit and examination of insurance companies.

**Insurance in force** — The potential maximum claim against an insurer.

**Loss ratio** — An insurer's loss and loss adjustment expenses as a percentage of premiums earned, calculated on a statutory basis. A component of the combined ratio, it is a measure of an insurer's claims cost experience.

**Managing general agent (MGA)** — A special type of producer that, unlike other persons or firms selling insurance, often has "binding authority" in certain insurance and reinsurance markets. MGAs have contractual agreements whereby they can accept entire books of business on behalf of insurance and reinsurance underwriters.

**Mutual insurance company** — An incorporated insurance organization with a governing body elected by policyholders. Mutual insurance companies generally issue participating policies.

**Net operating income** — After-tax income before net realized investment gains or losses. Analysts most commonly use this measure of insurer profitability when modeling future earnings of an insurer.

**Net premiums written** — Premium income brought in by insurance companies, directly or through reinsurance, minus payments made for business reinsured.

**Nonparticipating policy** — An insurance policy in which the insurer does not distribute any part of its surplus to policyholders. Premiums are usually lower for nonparticipating policies than for comparable participating policies.

**Participating policy** — An insurance policy under which the insurer agrees to distribute to its policyholders the portion of its surplus that management does not deem necessary to retain. Such a distribution serves to reduce the premiums each policyholder has paid during the year.

**Policy reserves** — The funds that an insurer holds specifically for the fulfillment of its policy obligations.

**Premium** — The payment, or one of the periodic payments, a policyholder agrees to make for an insurance policy.

**Premium loan** — A policy loan made for the purpose of paying premiums.

**Primary insurer** — An insurance company that, either through an independent insurance agent or a broker, provides coverage in the outside market. The buyers of primary insurance are consumers.

**Producer** — A person or firm that sells insurance. A producer may be an agent or a broker.

**Reinsurance** — Coverage that a primary insurer (or “reinsured”) purchases from another company to protect itself from losses beyond a dollar amount it feels can be safely carried. This amount is normally called the reinsured’s “net line.” The reinsurance company can, in turn, reinsure through a process known as retrocession.

**Reserves** — Funds that an insurer sets aside to cover obligations to policyholders; the amount may represent both actual and potential liabilities.

**Rider** — A special provision or group of provisions that may be added to a policy to expand or limit the benefits otherwise payable.

**Statutory accounting principles (SAP)** — An accounting format used by state insurance regulators. As opposed to the generally accepted accounting principles method, statutory accounting is essentially cash-oriented (rather than accrual) and has such requirements as immediately expensing all costs related to writing business. More conservative than GAAP, SAP focuses on a firm’s ability to meet its obligations (its solvency), whereas GAAP focuses on profit growth.

**Stock insurance company** — An insurance company owned by its stockholders, who elect a board to direct the firm’s management. In general, stock companies issue nonparticipating insurance, but they may also issue participating policies.

**Surplus lines** — Generally, a risk for which no normal insurance market exists.

**Terrorist insurance** — Coverage that can be added to a property insurance program to provide protection against destruction of property by terrorists.

**Underwriting profit/loss** — Profits or losses of an insurance company that result from insurance activities, calculated on a statutory basis. A net underwriting profit or loss represents underwriting results after policyholder dividends are deducted.

**War risks insurance** — Coverage on ships or cargo against loss or damage by enemy action and against damages sustained in fighting such an action. The perils of war are excluded from most policies.



## INDUSTRY REFERENCES

### PERIODICALS

#### ***Aggregates & Averages: Property-Casualty***

##### ***Best's Review***

##### ***BestWeek***

A.M. Best Co. Inc.

Ambest Rd., Oldwick, NJ 08858

(908) 439-2200

Web site: <http://www.ambest.com>

The first is an annual that provides financial and underwriting data on the entire property-casualty insurance industry; the other two are monthly and weekly publications, respectively, that cover topics and issues in the property-casualty insurance industry.

#### ***Business Insurance***

Crain Communications Inc.

360 N. Michigan Ave., Chicago, IL 60611

(312) 649-5200

Web site: <http://www.businessinsurance.com>

Weekly; covers corporate risk, employee benefit, and managed healthcare news.

#### ***National Underwriter (Property/Casualty edition)***

The National Underwriter Co.

5081 Olympic Blvd., Erlanger, KY 41018

(800) 543-0874

Web site: <http://www.nunews.com/pandc>

Weekly newspaper; covers issues related to the property/casualty insurance market.

### BOOKS

#### ***Glossary of Insurance Terms*, 2nd ed.**

Richard V. Rupp, CPCU

Chatsworth, Calif.: NILES Publishing Co., 1996

#### ***Property & Casualty Insurance Accounting*, 8th ed.**

Insurance Accounting and Systems Association, 2003

4705 University Dr., Ste. 280, Durham, NC 27717

(919) 489-0991

Web site: <http://www.iasa.org>

### TRADE ASSOCIATIONS

#### **Insurance Information Institute (III)**

110 William St., New York, NY 10038

(212) 346-5500

Web site: <http://www.iii.org>

Nonprofit, industry-supported organization that provides information about the property-casualty insurance industry.

#### **Insurance Services Office Inc. (ISO)**

545 Washington Blvd., Jersey City, NJ 07310

(800) 888-4476

Web site: <http://www.iso.com>

Trade organization and publisher of aggregate industry underwriting statistics.

### COMPANY REPORTS

#### **ACE Limited**

17 Woodbourne Ave., Hamilton HMDX HM08, Bermuda

(441) 295-5200

Web site: <http://www.ancelimited.com>

#### **Allstate Corp.**

2775 Sanders Rd., Northbrook, IL 60062

(847) 402-5000

Web site: <http://www.allstate.com>

#### **American International Group**

80 Pine St., New York, NY 10270

(212) 770-7000

Web site: <http://www.aig.com>

#### **The Chubb Corp.**

15 Mountain View Rd., Warren, NJ 07059

(908) 903-2000

Web site: <http://www.chubb.com>

#### **Cincinnati Financial Corp.**

P.O. Box 145496, Cincinnati, OH 45250

(513) 870-2000

Web site: <http://www.cinfin.com>

#### **CNA Financial Corp.**

CNA Plaza, 333 S. Wabash Ave., Chicago, IL 60685

(312) 822-5000

Web site: <http://www.cna.com>

#### **Hartford Financial Services Group**

Hartford Plaza, 690 Asylum Ave., Hartford, CT 06115

(860) 547-5000

Web site: <http://www.thehartford.com>

#### **Progressive Corp.**

6300 Wilson Mills Rd., Mayfield Village, OH 44143

(440) 461-5000

Web site: <http://www.progressive.com>

#### **SAFECO Corp.**

SAFECO Plaza, Seattle, WA 98185

(206) 545-5000

Web site: <http://www.safeco.com>

**St. Paul Cos. Inc.**

385 Washington St., St. Paul, MN 55102  
(651) 310-7911  
Web site: <http://www.stpaul.com>

**Travelers Property Casualty Corp.**

One Tower Square, Hartford, CT 06183  
(860) 277-7234  
Web site: <http://www.travelers.com>

**XL Capital Ltd.**

XL House, One Bermudiana Rd.  
Hamilton HM 11, Bermuda  
(441) 292-8515  
Web site: <http://www.xlcapital.com>

## DEFINITIONS FOR COMPARATIVE COMPANY ANALYSIS TABLES

### Operating revenues

Net sales and other operating revenues. Excludes interest income if such income is "nonoperating." Includes franchised/leased department income for retailers and royalties for publishers and oil and mining companies. Excludes excise taxes for tobacco, liquor, and oil companies.

### Net income

Profits derived from all sources, after deductions of expenses, taxes, and fixed charges, but before any discontinued operations, extraordinary items, and dividend payments (preferred and common).

### Return on revenues

Net income divided by operating revenues.

### Return on assets

Net income divided by average total assets. Used in industry analysis and as a measure of asset-use efficiency.

### Return on equity

Net income, less preferred dividend requirements, divided by average common shareholder's equity. Generally used to measure performance and to make industry comparisons.

### Price/earnings ratio

The ratio of market price to earnings, obtained by dividing the stock's high and low market price for the year by earnings per share (before extraordinary items). It essentially indicates the value investors place on a company's earnings.

### Dividend payout ratio

This is the percentage of earnings paid out in dividends. It is calculated by dividing the annual dividend by the earnings. Dividends are generally total cash payments per share over a 12-month period. Although payments are usually calculated from the ex-dividend dates, they may also be reported on a declared basis where this has been established to be a company's payout policy.

### Dividend yield

The total cash dividend payments divided by the year's high and low market prices for the stock.

### Earnings per share

The amount a company reports as having been earned for the year (based on generally accepted accounting standards), divided by the number of shares outstanding. Amounts reported in *Industry Surveys* exclude extraordinary items.

### Tangible book value per share

This measure indicates the theoretical dollar amount per common share one might expect to receive should liquidation take place. Generally, book value is determined by adding the stated (or par) value of the common stock, paid-in capital, and retained earnings, then subtracting intangible assets, preferred stock at liquidating value, and unamortized debt discount. This amount is divided by the number of outstanding shares to get book value per common share.

### Share price

This shows the calendar-year high and low of a stock's market price.

In addition to the footnotes that appear at the bottom of each page, you will notice some or all of the following:

NA—Not available.

NM—Not meaningful.

NR—Not reported.

AF—Annual figure. Data are presented on an annual basis.

CF—Combined figure. In this case, data are not available because one or more components are combined with other items.

## COMPARATIVE COMPANY ANALYSIS — INSURANCE: PROPERTY-CASUALTY

### Operating Revenues

Ticker	Company	Yr. End	Million \$							Compound Growth Rate (%)			Index Basis (1993 = 100)				
			2003	2002	2001	2000	1999	1998	1993	10-Yr.	5-Yr.	1-Yr.	2003	2002	2001	2000	1999
ACE	* ACE LIMITED	DEC	10,689.7	7,123.0	6,644.7	5,266.7	3,017.0 A	1,406.9 A	537.9	34.8	50.0	50.1	1,987	1,324	1,235	979	561
ALL	* ALLSTATE CORP	DEC	32,149.0	29,579.0	28,865.0 A	29,134.0	26,959.0 A	25,879.0	20,946.3	4.4	4.4	8.7	153	141	138	139	129
ABK	* AMBAC FINANCIAL GP	DEC	1,256.2 D	965.3	724.5	622.5	522.6	452.3	327.6	14.4	22.7	30.1	383	295	221	190	160
BER	† BERKLEY (W R) CORP	DEC	3,630.1	2,566.1	1,941.8	1,781.3	1,673.7	1,582.5	673.3	18.4	18.1	41.5	539	381	288	265	249
CB	* CHUBB CORP	DEC	11,461.0	9,115.6	7,739.9	7,237.8	6,715.9	6,336.6	5,363.6 F	7.9	12.6	25.7	214	170	144	135	125
CINF	* CINCINNATI FINANCIAL CORP	DEC	3,181.0	2,843.0	2,561.0	2,331.0	2,128.2	2,054.3	1,442.2	8.2	9.1	11.9	221	197	178	162	148
FNF	† FIDELITY NATIONAL FINL INC	DEC	7,715.2 A	5,082.6	3,874.1	2,742.0 A	1,352.2	1,288.5 A	575.4 A	29.6	43.0	51.8	1,341	883	673	477	235
FAF	† FIRST AMERICAN CORP/CA	DEC	6,140.8	4,660.9	3,750.7 F	2,934.3 F	2,988.2 A,F	2,877.3 A,F	1,396.9	16.0	16.4	31.8	440	334	269	210	214
LFG	§ LANDAMERICA FINANCIAL GP	DEC	3,406.0 A	2,586.6	2,170.5	1,802.4	2,048.0	1,848.9 A	503.9	21.1	13.0	31.7	676	513	431	358	406
MBI	* MBIA INC	DEC	1,467.3	1,232.8	1,144.7	1,057.5	964.4	911.9 A	429.0	13.1	10.0	19.0	342	287	267	247	225
OCAS	† OHIO CASUALTY CORP	DEC	1,669.6	1,702.8	1,902.0	1,736.7	1,900.1	1,452.3 A	1,669.8	(0.0)	2.8	(1.9)	100	102	114	104	114
ORI	† OLD REPUBLIC INTL CORP	DEC	3,285.7	2,756.4	2,373.4	2,070.6	2,102.1	2,171.7	1,736.3	6.6	8.6	19.2	189	159	137	119	121
PHLY	§ PHILADELPHIA CONS HLDG CORP	DEC	616.7	456.2	332.5	273.8	196.0	138.8	43.2	30.4	34.7	35.2	1,426	1,055	769	633	453
PRA	* PROASSURANCE CORP	DEC	709.6	555.8	382.6	222.6	208.0	193.6	87.7	23.3	29.7	27.7	809	634	436	254	237
PGR	* PROGRESSIVE CORP-OHIO	DEC	11,880.5 F	9,282.9 F	7,475.5 F	6,761.9 F	6,109.5 F	5,285.0 F	1,944.6	19.8	17.6	28.0	611	477	384	348	314
RLI	§ RLI CORP	DEC	519.9	382.2	309.4	263.5	225.8	168.1	155.1	12.9	25.3	36.0	335	246	199	170	146
SAFC	* SAFECO CORP	DEC	7,503.7	7,065.1	6,862.5 D	7,118.4 F	6,717.1	6,452.1	3,516.7	7.9	3.1	6.2	213	201	195	202	191
SKP	§ SCPIE HOLDINGS INC	DEC	187.0 F	338.5	278.4	210.6	191.2	210.0	NA	NA	(2.3)	(44.8)	**	**	**	**	NA
SIGI	§ SELECTIVE INS GROUP INC	DEC	1,356.1	1,178.9	1,059.0 D	1,004.8	974.8 A	837.3 A	679.6	7.2	10.1	15.0	200	173	156	148	143
SPC	ST PAUL COS	DEC	8,854.0 C	8,918.0 A,C	8,943.0 D	8,608.0 A,C	7,569.0 D	9,108.4 A	4,460.2	7.1	(0.6)	(0.7)	199	200	201	193	170
STC	§ STEWART INFORMATION SERVICES	DEC	2,243.3	1,779.7 F	1,271.6 F	935.5 F	1,072.6 F	968.8 F	345.6	20.6	18.3	26.0	649	515	368	271	310
XL	* XL CAPITAL LTD	DEC	7,883.1	6,513.4	3,976.2 A	2,643.1	2,470.1 A	1,169.7	799.7	25.7	46.5	21.0	986	814	497	330	309
ZNT	§ ZENITH NATIONAL INSURANCE CP	DEC	849.3 D	602.2 D	622.0	459.6	492.1	636.8 A	583.3	3.8	5.9	41.0	146	103	107	79	84
<b>REINSURANCE†</b>																	
RE	† EVEREST RE GROUP LTD	DEC	4,106.7	2,557.6	1,801.5	1,479.8 A	1,306.7	1,315.2	NA	NA	25.6	60.6	**	**	**	**	NA
<b>MULTI-LINE GROUP†</b>																	
AFC	† ALLMERICA FINANCIAL CORP	DEC	3,263.6	3,316.6 C	3,311.8	3,087.9	3,145.2 D	3,432.5 A	NA	NA	(1.0)	(1.6)	**	**	**	**	NA
AFG	† AMERICAN FINANCIAL GROUP INC	DEC	3,339.8 D	3,751.1	3,923.6	3,767.1	3,334.5	4,063.2	1,763.3 A,C	6.6	(3.8)	(11.0)	189	213	223	214	189
AIG	* AMERICAN INTERNATIONAL GROUP	DEC	81,303.0	67,482.0	62,402.0 A,C	45,972.0	40,656.0 A	33,239.0	21,155.3	14.4	19.6	20.5	384	319	295	217	192
HIG	* HARTFORD FINL SVCS GRP INC	DEC	18,733.0	15,907.0	15,147.0 A	14,703.0	13,528.0	15,022.0 A	NA	NA	4.5	17.8	**	**	**	**	NA
HCC	† HCC INSURANCE HOLDINGS INC	DEC	942.0 D,F	669.4 A,F	505.5 A,F	466.2 C,F	337.0 A,F	308.0 A,F	52.3	33.5	25.1	40.7	1,801	1,280	966	891	644
HMN	† HORACE MANN EDUCATORS CORP	DEC	866.2	771.9	804.5	781.2	775.4	779.4	707.6	2.0	2.1	12.2	122	109	114	110	110
LTR	* LOEWS CORP	DEC	15,809.6 A,C	16,827.8 D,F	18,799.1 F	20,669.9	20,952.6 F	20,713.0 F	13,254.0 F	1.8	(5.3)	(6.1)	119	127	142	156	158
UTR	† UNITRIN INC	DEC	2,943.8	2,298.2 A	1,971.7	1,953.2	1,813.6 A	2,085.9 A	1,363.2	8.0	7.1	28.1	216	169	145	143	133
<b>INSURANCE BROKERS†</b>																	
AOC	* AON CORP	DEC	9,810.0 D	8,774.0	7,676.0 A	7,375.0 A	7,070.0 A	6,493.0 A	3,844.8	9.8	8.6	11.8	255	228	200	192	184
BRO	† BROWN & BROWN INC	DEC	551.0 A	455.7 A	365.0 A	209.7 A	176.4 A	153.8 A	94.4 B	19.3	29.1	20.9	584	483	387	222	187
AJG	† GALLAGHER (ARTHUR J.) & CO	DEC	1,289.5 A	1,120.8 A	903.9 A	740.6 A	605.8 A	554.5 A	317.7 A	15.0	18.4	15.1	406	353	285	233	191
HRH	§ HILB ROGAL & HOBBS CO	DEC	563.6 A	452.7 A,C	330.3 A	262.1	227.2 A	181.0	135.0 A	15.4	25.5	24.5	418	335	245	194	168
MMC	* MARSH & MCLENNAN COS	DEC	11,588.0 A	10,440.0 A	9,943.0 A	10,157.0 A	9,157.0 A	7,190.0 A	3,163.4	13.9	10.0	11.0	366	330	314	321	289

Note: Data as originally reported. † S&P 1500 Index group. \* Company included in the S&P 500. † Company included in the S&P MidCap. § Company included in the S&P SmallCap. # Of the following calendar year. \*\* Not calculated; data for base year or end year not available.  
A - This year's data reflect an acquisition or merger. B - This year's data reflect a major merger resulting in the formation of a new company. C - This year's data reflect an accounting change. D - Data exclude discontinued operations. E - Includes excise taxes. F - Includes other (nonoperating) income. G - Includes sale of leased depts. H - Some or all data are not available, due to a fiscal year change.

## Net Income

Million \$										Compound Growth Rate (%)			Index Basis (1993 = 100)				
Ticker	Company	Yr. End	2003	2002	2001	2000	1999	1998	1993	10-Yr.	5-Yr.	1-Yr.	2003	2002	2001	2000	1999
PROPERTY CASUALTY‡																	
ACE	* ACE LIMITED	DEC	1,417.5	76.5	(123.7)	543.0	365.0	560.2	223.5	20.3	20.4	1,751.7	634	34	(55)	243	163
ALL	* ALLSTATE CORP	DEC	2,720.0	1,465.0	1,167.0	2,211.0	2,720.0	3,294.0	1,301.5	7.6	(3.8)	85.7	209	113	90	170	209
ABK	* AMBAC FINANCIAL GP	DEC	628.1	432.6	432.9	366.2	307.9	254.0	179.4	13.3	19.9	45.2	350	241	241	204	172
BER	† BERKLEY (W R) CORP	DEC	337.2	175.0	(91.5)	36.2	(34.0)	58.8	51.6	20.7	41.8	92.6	654	339	(177)	70	(66)
CB	* CHUBB CORP	DEC	808.8	222.9	111.5	714.6	621.1	707.0	344.2	8.9	2.7	262.9	235	65	32	208	180
CINF	* CINCINNATI FINANCIAL CORP	DEC	374.0	238.0	193.0	118.4	254.7	241.6	202.2	6.3	9.1	57.1	185	118	95	59	126
FNF	† FIDELITY NATIONAL FINL INC	DEC	861.8	531.7	311.2	108.3	70.9	105.7	36.3	37.3	52.2	62.1	2,374	1,465	857	298	195
FAF	† FIRST AMERICAN CORP/CA	DEC	451.0	234.4	167.3	82.2	88.6	198.7	62.1	21.9	17.8	92.4	726	377	269	132	143
LFG	§ LANDAMERICA FINANCIAL GP	DEC	192.1	149.4	60.3	(80.8)	54.3	93.0	29.0	20.8	15.6	28.6	663	516	208	(279)	188
MBI	* MBIA INC	DEC	813.6	586.8	583.2	528.6	320.5	432.7	246.1	12.7	13.5	38.6	331	238	237	215	130
OCAS	† OHIO CASUALTY CORP	DEC	75.8	(0.9)	98.6	(79.2)	105.9	83.0	87.0	(1.4)	(1.8)	NM	87	(1)	113	(91)	122
ORI	† OLD REPUBLIC INTL CORP	DEC	459.8	392.9	346.9	297.6	226.8	323.7	166.4	10.7	7.3	17.0	276	236	208	179	136
PHLY	§ PHILADELPHIA CONS HLDG CORP	DEC	60.3	36.0	30.6	30.8	18.8	20.0	4.2	30.4	24.7	67.4	1,424	851	722	727	445
PRA	§ PROASSURANCE CORP	DEC	38.7	10.5	12.4	24.3	46.7	48.5	26.9	3.7	(4.4)	268.1	144	39	46	90	174
PGR	* PROGRESSIVE CORP-OHIO	DEC	1,255.4	667.3	411.4	46.1	295.2	456.7	267.3	16.7	22.4	88.1	470	250	154	17	110
RLI	§ RLI CORP	DEC	71.3	35.9	30.2	28.7	31.5	28.2	14.1	17.6	20.3	98.8	504	254	214	203	223
SAFC	* SAFECO CORP	DEC	339.2	301.1	(1,045.3)	114.6	252.2	351.9	425.9	(2.3)	(0.7)	12.7	80	71	(245)	27	59
SKP	§ SCPIE HOLDINGS INC	DEC	(12.8)	(38.4)	(58.0)	17.3	29.9	37.0	NA	NA	NM	NM	**	**	**	**	NA
SIGI	§ SELECTIVE INS GROUP INC	DEC	66.3	42.1	26.3	26.5	53.7	53.6	22.7	11.3	4.4	57.4	293	186	116	117	237
SPC	§ ST PAUL COS	DEC	699.0	249.0	(1,009.0)	1,013.0	779.0	89.3	427.6	5.0	50.9	180.7	163	58	(236)	237	182
STC	§ STEWART INFORMATION SERVICES	DEC	123.8	94.5	48.7	0.6	28.4	47.0	23.7	18.0	21.3	31.0	523	399	206	3	120
XL	* XL CAPITAL LTD	DEC	412.0	405.6	(576.1)	506.4	470.5	587.7	379.2	0.8	(6.9)	1.6	109	107	(152)	134	124
ZNT	§ ZENITH NATIONAL INSURANCE CP	DEC	65.8	1.0	(23.8)	(47.8)	54.1	19.1	53.2	2.2	28.1	6,380.9	124	2	(45)	(90)	102
REINSURANCE‡																	
RE	† EVEREST RE GROUP LTD	DEC	426.0	231.3	99.0	186.4	158.1	165.2	NA	NA	20.9	84.2	**	**	**	**	NA
MULTI-LINE GROUP‡																	
AFC	† ALLMERICA FINANCIAL CORP	DEC	86.9	(302.4)	0.1	199.9	345.1	201.2	NA	NA	(15.5)	NM	**	**	**	**	NA
AFG	† AMERICAN FINANCIAL GROUP INC	DEC	321.2	125.0	(4.8)	(47.0)	147.0	125.2	242.7	2.8	20.7	156.9	132	52	(2)	(19)	61
AIG	* AMERICAN INTERNATIONAL GROUP	DEC	9,265.0	5,519.0	5,499.0	5,636.0	5,055.0	3,766.0	1,918.1	17.1	19.7	67.9	483	288	287	294	264
HIG	* HARTFORD FINL SVCS GRP INC	DEC	(91.0)	1,000.0	549.0	974.0	862.0	1,015.0	NA	NA	NM	NM	**	**	**	**	NA
HCC	† HCC INSURANCE HOLDINGS INC	DEC	106.9	105.8	30.2	55.4	25.1	72.3	8.0	29.6	8.1	1.0	1,335	1,322	377	692	314
HMN	† HORACE MANN EDUCATORS CORP	DEC	19.0	11.3	25.6	20.8	44.5	85.3	77.2	(13.1)	(26.0)	67.4	25	15	33	27	58
LTR	* LOEWS CORP	DEC	(666.1)	982.6	(535.8)	1,876.7	521.1	464.8	594.1	NM	NM	NM	(112)	165	(90)	316	88
UTR	† UNITRIN INC	DEC	123.6	(8.2)	380.9	91.0	201.0	510.8	95.0	2.7	(24.7)	NM	130	(9)	401	96	212
INSURANCE BROKERS‡																	
AOC	* AON CORP	DEC	663.0	466.0	147.0	481.0	352.0	541.0	323.8	7.4	4.2	42.3	205	144	45	149	109
BRO	† BROWN & BROWN INC	DEC	110.3	83.1	53.9	33.2	27.2	23.1	8.0	30.0	36.8	32.7	1,379	1,039	674	415	340
AJG	† GALLAGHER (ARTHUR J.) & CO	DEC	146.2	129.7	125.3	87.8	67.8	57.4	32.3	16.3	20.6	12.7	453	402	388	272	210
HRH	§ HILB ROGAL & HOBBS CO	DEC	75.0	61.2	32.3	22.1	19.5	14.9	8.4	24.4	38.1	22.5	890	726	384	263	231
MMC	* MARSH & MCLENNAN COS	DEC	1,540.0	1,365.0	974.0	1,181.0	726.0	796.0	332.4	16.6	14.1	12.8	463	411	293	355	218

Note: Data as originally reported. ‡ S&P 1500 Index group. \* Company included in the S&P 500. † Company included in the S&P MidCap. § Company included in the S&P SmallCap. # Of the following calendar year. \*\* Not calculated; data for base year or end year not available.

		Return on Revenues (%)					Return on Assets (%)					Return on Equity (%)					
Ticker	Company	Yr. End	2003	2002	2001	2000	1999	2003	2002	2001	2000	1999	2003	2002	2001	2000	1999
PROPERTY CASUALTY†																	
ACE	* ACE LIMITED	DEC	13.3	1.1	NM	10.3	12.1	3.0	0.1	NM	1.7	1.9	18.2	0.8	NM	10.6	8.9
ALL	* ALLSTATE CORP	DEC	8.5	5.0	4.0	7.6	10.1	2.2	1.3	1.1	2.2	2.9	14.3	8.5	6.7	13.0	16.1
ABK	* AMBAC FINANCIAL GP	DEC	50.0	44.8	59.7	58.8	58.9	3.9	3.1	3.9	3.4	2.7	15.9	13.1	15.5	15.9	15.0
BER	† BERKLEY (W R) CORP	DEC	9.3	6.8	NM	2.0	NM	4.1	2.8	NM	0.7	NM	22.3	15.4	NM	5.7	NM
CB	* CHUBB CORP	DEC	7.1	2.4	1.4	9.9	9.2	2.2	0.7	0.4	2.9	2.8	10.5	3.3	1.7	10.8	10.4
CINF	* CINCINNATI FINANCIAL CORP	DEC	11.8	8.4	7.5	5.1	12.0	2.5	1.7	1.4	1.0	2.3	6.3	4.1	3.2	2.1	4.6
FNF	† FIDELITY NATIONAL FINL INC	DEC	11.2	10.5	8.0	4.0	5.2	13.7	11.0	7.5	4.5	7.1	28.1	27.3	22.7	14.1	17.1
FAF	† FIRST AMERICAN CORP/CA	DEC	7.3	5.0	4.5	2.8	3.0	10.9	7.5	6.6	3.8	4.5	27.8	19.0	16.9	9.8	11.5
LFG	§ LANDAMERICA FINANCIAL GP	DEC	5.6	5.8	2.8	NM	2.7	8.3	8.3	3.6	NM	2.8	20.1	18.8	9.9	NM	8.1
MBI	* MBIA INC	DEC	55.4	47.6	50.9	50.0	33.2	3.3	3.3	3.9	4.0	2.7	13.8	11.4	13.0	13.7	8.8
OCAS	† OHIO CASUALTY CORP	DEC	4.5	NM	5.2	NM	5.6	1.5	NM	2.2	NM	2.3	6.9	NM	9.0	NM	8.6
ORI	† OLD REPUBLIC INTL CORP	DEC	14.0	14.3	14.6	14.4	10.8	5.0	4.7	4.6	4.2	3.2	13.7	13.2	13.3	12.8	10.1
PHLY	§ PHILADELPHIA CONS HLDG CORP	DEC	9.8	7.9	9.2	11.2	9.6	3.7	3.0	3.5	4.6	3.5	11.8	7.9	10.0	17.9	12.6
PRA	* PROASSURANCE CORP	DEC	5.5	1.9	3.3	10.9	22.4	1.4	0.4	0.7	2.2	4.2	7.4	2.3	3.3	7.2	14.4
PGR	* PROGRESSIVE CORP-OHIO	DEC	10.6	7.2	5.5	0.7	4.8	8.4	5.4	3.9	0.5	3.2	28.5	19.0	13.4	1.6	11.1
RLI	§ RLI CORP	DEC	13.7	9.4	9.8	10.9	13.9	3.7	2.3	2.3	2.3	2.9	14.1	9.1	9.1	9.3	10.7
SAFC	* SAFECO CORP	DEC	4.5	4.3	NM	1.6	3.8	1.0	0.9	NM	0.4	0.8	7.2	7.5	NM	2.5	5.1
SKP	§ SCPIE HOLDINGS INC	DEC	NM	NM	NM	8.2	15.6	NM	NM	NM	2.1	3.4	NM	NM	NM	5.7	8.8
SIGI	§ SELECTIVE INS GROUP INC	DEC	4.9	3.6	2.5	2.6	5.5	2.1	1.5	1.0	1.0	2.2	9.5	6.8	4.5	4.6	9.1
SPC	ST PAUL COS	DEC	7.9	2.8	NM	11.8	10.3	1.7	0.6	NM	2.5	2.0	11.7	4.5	NM	14.8	11.8
STC	§ STEWART INFORMATION SERVICES	DEC	5.5	5.3	3.8	0.1	2.6	13.2	12.4	7.8	0.1	5.5	22.2	21.3	14.1	0.2	10.4
XL	* XL CAPITAL LTD	DEC	5.2	6.2	NM	19.2	19.0	1.0	1.2	NM	3.2	3.7	5.5	6.6	NM	9.1	9.1
ZNT	§ ZENITH NATIONAL INSURANCE CP	DEC	7.8	0.2	NM	NM	11.0	3.6	0.1	NM	NM	3.2	18.8	0.3	NM	NM	15.4
REINSURANCE‡																	
RE	† EVEREST RE GROUP LTD	DEC	10.4	9.0	5.5	12.6	12.1	3.8	2.6	1.3	2.9	2.7	15.4	11.3	6.0	12.8	11.3
MULTI-LINE GROUP‡																	
AFC	† ALLMERICA FINANCIAL CORP	DEC	2.7	NM	0.0	6.5	11.0	0.3	NM	0.0	0.6	1.2	4.0	NM	0.0	8.6	14.7
AFG	† AMERICAN FINANCIAL GROUP INC	DEC	9.6	3.3	NM	NM	4.4	1.6	0.7	NM	NM	0.9	16.9	7.8	NM	NM	9.6
AIG	* AMERICAN INTERNATIONAL GROUP	DEC	11.4	8.2	8.8	12.3	12.4	1.5	1.0	1.4	2.0	2.2	14.2	9.9	12.0	15.5	16.7
HIG	* HARTFORD FINL SVCS GRP INC	DEC	NM	6.3	3.6	6.6	6.4	NM	0.6	0.3	0.6	0.5	NM	10.1	6.7	15.1	14.5
HCC	† HCC INSURANCE HOLDINGS INC	DEC	11.3	15.8	6.0	11.9	7.5	2.5	3.1	1.0	2.1	1.2	11.1	12.9	4.7	11.2	5.6
HMN	† HORACE MANN EDUCATORS CORP	DEC	2.2	1.5	3.2	2.7	5.7	0.4	0.3	0.6	0.5	1.0	3.6	2.3	5.8	5.0	9.9
LTR	* LOEWS CORP	DEC	NM	5.8	NM	9.1	2.5	NM	1.3	NM	2.7	0.7	NM	9.4	NM	17.7	5.2
UTR	† UNITRIN INC	DEC	4.2	NM	19.3	4.7	11.1	1.5	NM	5.7	1.5	3.4	6.8	NM	21.1	5.3	11.4
INSURANCE BROKERS‡																	
AOC	* AON CORP	DEC	6.8	5.3	1.9	6.5	5.0	2.5	1.9	0.6	2.2	1.7	15.7	12.6	4.2	14.8	11.5
BRO	† BROWN & BROWN INC	DEC	20.0	18.2	14.8	15.8	15.4	13.6	13.4	14.1	13.0	11.7	24.8	29.3	36.3	29.5	29.0
AJG	† GALLAGHER (ARTHUR J.) & CO	DEC	11.3	11.6	13.9	11.9	11.2	5.4	6.6	9.9	9.0	8.2	25.5	28.8	36.5	31.5	30.2
HRH	§ HILB ROGAL & HOBBS CO	DEC	13.3	13.5	9.8	8.4	8.6	8.0	9.2	7.6	6.6	7.7	20.1	27.0	28.0	27.8	33.3
MMC	* MARSH & MCLENNAN COS	DEC	13.3	13.1	9.8	11.6	7.9	10.7	10.1	7.2	8.8	5.8	29.4	26.8	18.7	25.1	18.5

Note: Data as originally reported. ‡ S&P 1500 Index group. \* Company included in the S&P 500. † Company included in the S&P MidCap. § Company included in the S&P SmallCap. # Of the following calendar year. NM - Not meaningful.

Price / Earnings Ratio (High-Low)								Dividend Payout Ratio (%)					Dividend Yield (High-Low, %)				
Ticker	Company	Yr. End	2003	2002	2001	2000	1999	2003	2002	2001	2000	1999	2003	2002	2001	2000	1999
PROPERTY CASUALTY†																	
ACE	* ACE LIMITED	DEC	8-5	NM-NM	NM-NM	19-6	19-8	15	347	NM	21	22	3.1-1.7	3.0-1.5	3.2-1.3	3.6-1.1	2.7-1.2
ALL	* ALLSTATE CORP	DEC	11-8	20-15	28-19	15-6	12-7	24	41	47	23	18	3.1-2.1	2.7-2.0	2.5-1.7	4.0-1.5	2.6-1.5
ABK	* AMBAC FINANCIAL GP	DEC	12-7	17-12	16-10	17-7	14-10	7	9	8	9	10	1.0-0.6	0.8-0.5	0.8-0.5	1.2-0.5	0.9-0.7
BER	† BERKLEY (W R) CORP	DEC	9-6	12-9	NM-NM	34-10	NM-NM	7	10	NM	37	NM	1.1-0.7	1.2-0.9	1.5-0.9	3.7-1.1	2.6-1.4
CB	* CHUBB CORP	DEC	15-9	60-40	NM-85	22-11	21-12	32	107	209	32	35	3.4-2.1	2.7-1.8	2.4-1.6	3.1-1.5	2.9-1.7
CINF	* CINCINNATI FINANCIAL CORP	DEC	18-14	32-22	36-28	59-35	27-19	43	61	70	103	44	3.0-2.4	2.7-1.9	2.5-2.0	2.9-1.8	2.3-1.6
FNF	† FIDELITY NATIONAL FINL INC	DEC	6-4	6-4	10-5	21-6	13-6	11	7	10	16	16	2.9-1.8	1.9-1.2	2.1-1.1	2.6-0.8	2.8-1.2
FAF	† FIRST AMERICAN CORP/CA	DEC	5-4	7-5	14-6	25-8	26-8	8	10	11	19	18	2.3-1.6	2.1-1.5	1.7-0.8	2.3-0.7	2.1-0.7
LFG	§ LANDAMERICA FINANCIAL GP	DEC	5-3	5-3	15-7	NM-NM	18-5	3	3	6	NM	6	1.0-0.6	1.0-0.6	0.9-0.4	1.2-0.5	1.3-0.3
MBI	* MBIA INC	DEC	11-6	15-9	15-9	14-7	22-14	14	17	15	15	25	2.3-1.3	1.9-1.1	1.7-1.0	2.3-1.1	1.8-1.1
OCAS	† OHIO CASUALTY CORP	DEC	14-9	NM-NM	10-5	NM-NM	13-9	0	NM	0	NM	53	0.0-0.0	0.0-0.0	0.0-0.0	9.6-3.3	6.2-4.2
ORI	† OLD REPUBLIC INTL CORP	DEC	10-6	11-7	11-7	13-4	13-7	44	19	20	22	28	6.8-4.3	2.6-1.8	2.8-1.9	5.2-1.7	4.1-2.2
PHLY	§ PHILADELPHIA CONS HLDG CORP	DEC	19-10	29-16	22-13	12-6	17-7	0	0	0	0	0	0.0-0.0	0.0-0.0	0.0-0.0	0.0-0.0	0.0-0.0
PRA	§ PROASSURANCE CORP	DEC	25-15	53-35	38-23	22-10	16-10	0	0	0	0	0	0.0-0.0	0.0-0.0	0.0-0.0	0.0-0.0	0.0-0.0
PGR	* PROGRESSIVE CORP-OHIO	DEC	15-8	20-15	27-15	NM-71	43-17	2	3	5	43	6	0.2-0.1	0.2-0.2	0.3-0.2	0.6-0.2	0.4-0.1
RLI	§ RLI CORP	DEC	13-9	17-12	15-13	15-9	12-9	14	19	20	20	18	1.6-1.0	1.6-1.1	1.6-1.4	2.2-1.3	2.0-1.4
SAFC	* SAFECO CORP	DEC	16-13	16-11	NM-NM	40-20	25-11	30	32	NM	164	76	2.3-1.9	3.0-1.9	4.3-2.8	8.2-4.1	6.6-3.1
SKP	§ SCPIE HOLDINGS INC	DEC	NM-NM	NM-NM	NM-NM	20-10	14-9	NM	NM	NM	22	12	7.0-2.5	10.7-1.4	2.6-1.3	2.2-1.1	1.4-0.9
SIGI	§ SELECTIVE INS GROUP INC	DEC	13-9	19-12	26-19	24-14	11-8	24	36	56	56	30	2.8-1.9	3.1-1.9	3.0-2.1	4.1-2.3	3.6-2.6
SPC	ST PAUL COS	DEC	13-10	46-21	NM-NM	12-5	11-8	39	106	NM	24	31	4.0-2.9	5.0-2.3	3.3-2.1	5.1-1.9	4.1-2.8
STC	§ STEWART INFORMATION SERVICES	DEC	6-3	4-3	7-5	NM-NM	16-5	7	0	0	0	8	2.2-1.1	0.0-0.0	0.0-0.0	0.0-0.0	1.6-0.5
XL	* XL CAPITAL LTD	DEC	33-23	34-20	NM-NM	22-10	21-11	71	64	NM	44	48	3.0-2.2	3.2-1.9	3.0-1.9	4.6-2.0	4.2-2.3
ZNT	§ ZENITH NATIONAL INSURANCE CP	DEC	9-5	NM-NM	NM-NM	NM-NM	8-6	29	NM	NM	NM	32	5.2-3.0	4.5-3.1	4.4-3.3	5.3-3.4	5.2-3.7
REINSURANCE†																	
RE	† EVEREST RE GROUP LTD	DEC	11-6	17-9	37-22	18-5	12-6	5	7	13	6	7	0.8-0.4	0.8-0.4	0.6-0.4	1.2-0.3	1.2-0.6
MULTI-LINE GROUP†																	
AFC	† ALLMERICA FINANCIAL CORP	DEC	19-6	NM-NM	NM-NM	20-9	10-7	0	NM	NM	7	4	0.0-0.0	0.0-0.0	0.7-0.3	0.7-0.3	0.5-0.4
AFG	† AMERICAN FINANCIAL GROUP INC	DEC	6-4	17-10	NM-NM	NM-NM	18-10	11	27	NM	NM	41	2.8-1.9	2.8-1.7	5.4-3.3	5.4-3.4	4.1-2.3
AIG	* AMERICAN INTERNATIONAL GROUP	DEC	19-12	38-23	47-31	43-22	35-23	6	8	8	6	6	0.5-0.3	0.4-0.2	0.2-0.2	0.3-0.1	0.2-0.2
HIG	* HARTFORD FINL SVCS GRP INC	DEC	NM-NM	18-9	31-20	18-7	17-10	NM	26	44	22	24	3.4-1.8	2.8-1.5	2.2-1.4	3.3-1.2	2.5-1.4
HCC	† HCC INSURANCE HOLDINGS INC	DEC	19-13	17-11	57-39	24-10	49-16	17	15	47	20	39	1.3-0.9	1.3-0.9	1.2-0.8	2.0-0.8	2.5-0.8
HMN	† HORACE MANN EDUCATORS CORP	DEC	39-28	86-49	36-23	44-24	31-18	95	150	67	82	35	3.4-2.5	3.1-1.7	2.8-1.9	3.5-1.9	2.0-1.2
LTR	* LOEWS CORP	DEC	NM-NM	14-8	NM-NM	6-2	22-12	NM	13	NM	5	21	1.6-1.2	1.6-1.0	1.4-0.8	2.6-1.0	1.7-1.0
UTR	† UNITRIN INC	DEC	23-12	NM-NM	7-6	31-21	15-11	91	NM	28	114	51	7.7-3.9	6.0-3.9	4.7-3.8	5.5-3.6	4.6-3.3
INSURANCE BROKERS†																	
AOC	* AON CORP	DEC	13-8	24-8	83-55	23-11	35-19	29	50	166	47	60	3.4-2.2	6.2-2.1	3.0-2.0	4.2-2.0	3.1-1.7
BRO	† BROWN & BROWN INC	DEC	23-17	30-19	37-17	31-13	21-15	15	16	19	23	23	0.9-0.6	0.8-0.5	1.1-0.5	1.7-0.8	1.6-1.1
AJG	† GALLAGHER (ARTHUR J.) & CO	DEC	20-14	25-15	26-15	31-10	18-11	44	40	35	41	43	3.1-2.2	2.8-1.6	2.4-1.3	4.0-1.3	3.8-2.4
HRH	§ HILB ROGAL & HOBBS CO	DEC	20-13	22-13	27-14	25-15	19-10	17	17	29	40	43	1.4-0.8	1.3-0.8	2.1-1.1	2.6-1.6	4.2-2.2
MMC	* MARSH & MCLENNAN COS	DEC	19-13	23-14	33-22	31-16	35-21	52	43	58	44	62	3.9-2.7	3.1-1.9	2.6-1.7	2.7-1.4	3.0-1.8

Note: Data as originally reported. ‡ S&P 1500 Index group. \* Company included in the S&P 500. † Company included in the S&P MidCap. § Company included in the S&P SmallCap. # Of the following calendar year.



**Earnings per Share (\$)**
**Tangible Book Value per Share (\$)**
**Share Price (High-Low, \$)**

Ticker	Company	Yr. End	2003	2002	2001	2000	1999	2003	2002	2001	2000	1999	2003	2002	2001	2000	1999
<b>PROPERTY CASUALTY†</b>																	
ACE	* ACE LIMITED	DEC	5.10	0.19	(0.64)	2.37	1.88	21.87	13.98	12.83	11.08	7.49	42.80-23.59	44.98-22.01	43.19-18.10	43.94-14.06	35.25-15.50
ALL	* ALLSTATE CORP	DEC	3.87	2.07	1.62	2.97	3.40	27.89	23.52	22.35	22.26	21.09	43.27-30.05	41.95-31.03	45.90-30.00	44.75-17.19	41.00-22.88
ABK	* AMBAC FINANCIAL GP	DEC	5.90	4.08	4.10	3.49	2.93	39.71	34.20	28.26	24.60	19.23	72.21-43.79	71.25-49.86	64.00-42.20	58.31-25.92	42.00-29.79
BER	† BERKLEY (W R) CORP	DEC	4.06	2.29	(1.40)	0.63	(0.60)	19.43	15.41	11.59	10.56	8.94	36.93-24.39	27.20-19.93	25.96-15.53	21.17-6.22	16.11-8.81
CB	* CHUBB CORP	DEC	4.51	1.31	0.65	4.10	3.70	42.85	37.33	35.62	37.13	32.85	69.29-41.78	78.64-51.91	86.63-55.54	90.25-43.25	76.38-44.00
CINF	* CINCINNATI FINANCIAL CORP	DEC	2.22	1.40	1.14	0.70	1.48	36.93	32.91	35.26	35.49	31.87	39.91-31.50	45.05-30.89	40.89-32.38	41.25-24.94	40.48-28.69
FNF	† FIDELITY NATIONAL FINL INC	DEC	5.81	4.06	2.41	1.11	1.43	8.60	9.55	6.41	2.91	9.56 J	35.35-22.18	24.71-15.68	22.92-11.84	23.67-6.99	18.48-8.08
FAF	† FIRST AMERICAN CORP/CA	DEC	5.89	3.27	2.51	1.29	1.37	6.51	10.46	9.78	8.20	8.17	31.24-21.60	23.20-16.14	35.49-16.30	32.88-10.25	35.19-11.50
LFG	§ LANDAMERICA FINANCIAL GP	DEC	10.43	8.10	3.42	(6.60)	3.21	24.51	36.08	28.88	20.05	15.19	53.18-35.50	38.30-25.25	50.45-23.20	42.94-16.06	58.94-15.56
MBI	* MBIA INC	DEC	5.67	4.00	3.94	3.58	2.15	42.88	37.32	31.56	27.86	22.79	60.72-34.14	60.11-34.93	57.49-36.00	50.79-24.21	47.92-30.08
OCAS	† OHIO CASUALTY CORP	DEC	1.25	(0.01)	1.64	(1.32)	1.73	16.46	14.78	13.96	14.20	14.27	17.79-11.38	22.24-11.01	16.18-7.94	17.88-6.13	21.69-14.88
ORI	† OLD REPUBLIC INTL CORP	DEC	2.53	2.17	1.95	1.66	1.17	19.57 J	17.45 J	15.60 J	13.75 J	11.99 J	26.06-16.40	23.33-16.27	21.04-14.13	21.38-7.08	15.17-8.04
PHLY	§ PHILADELPHIA CONS HLDG CORP	DEC	2.75	1.67	1.85	2.53	1.51	23.54	20.67	18.73	11.28	10.53	52.73-28.57	48.15-26.24	41.30-24.25	30.88-14.13	25.50-10.81
PRA	* PROASSURANCE CORP	DEC	1.34	0.40	0.51	1.04	1.95	18.77	17.49	16.02	15.22	13.97	33.30-20.00	21.24-14.10	19.25-11.88	23.13-10.00	31.55-19.05
PGR	* PROGRESSIVE CORP-OHIO	DEC	5.79	3.05	1.86	0.21	1.35	23.25	17.28	14.76	13.01	12.55	84.68-46.25	60.49-44.75	50.60-27.38	37.00-15.00	58.08-22.83
RLI	§ RLI CORP	DEC	2.84	1.80	1.54	1.46	1.55	20.98	17.37	15.36	14.99	13.11	38.15-24.50	30.20-22.23	23.08-19.38	22.53-13.13	19.41-13.94
SAFC	* SAFECO CORP	DEC	2.44	2.33	(8.18)	0.90	1.90	34.92	30.69	27.72	26.55	22.80	39.79-31.79	38.00-24.99	32.95-21.50	35.88-18.00	46.75-21.81
SKP	* SCPIE HOLDINGS INC	DEC	(1.37)	(4.12)	(6.22)	1.84	2.63	20.13	23.10 J	25.88	31.57	30.24	15.90-5.71	29.60-3.73	31.40-15.18	36.94-18.31	36.06-23.69
SIGI	§ SELECTIVE INS GROUP INC	DEC	2.54	1.67	1.07	1.07	1.98	25.88	22.91	21.33	20.97	19.50	33.00-21.81	31.48-19.36	28.21-19.94	25.88-14.63	22.50-16.50
SPC	ST PAUL COS	DEC	3.00	1.09	(4.84)	4.59	3.37	22.27	20.59	21.03	30.54	26.41	39.74-29.00	50.60-23.00	54.44-34.00	57.00-21.31	37.06-25.38
STC	§ STEWART INFORMATION SERVICES	DEC	6.93	5.33	3.01	0.04	1.96	30.08	24.07	19.19	17.17	17.23	41.45-20.76	22.50-15.05	22.25-15.80	22.31-12.25	31.50-10.13
XL	* XL CAPITAL LTD	DEC	2.71	2.92	(4.55)	4.07	3.69	37.07	36.13	28.35	31.86	30.91	88.87-63.49	98.48-58.45	96.50-61.50	89.25-39.00	75.75-41.94
ZNT	§ ZENITH NATIONAL INSURANCE CP	DEC	3.50	0.05	(1.35)	(2.78)	3.15	19.16	15.77	15.15	16.47	19.32	32.85-19.15	32.25-22.00	30.70-22.80	29.75-18.75	26.69-19.25
<b>REINSURANCE†</b>																	
RE	† EVEREST RE GROUP LTD	DEC	7.89	4.60	2.14	4.06	3.26	56.84	47.00	37.16	34.42	28.55	85.25-47.90	76.50-42.59	78.50-46.51	74.75-20.69	38.94-20.50
<b>MULTI-LINE GROUP†</b>																	
AFC	† ALLAMERICA FINANCIAL CORP	DEC	1.64	(5.72)	0.00	3.75	6.27	39.47	36.69	45.20	45.71	41.33	31.35-9.82	50.80-7.04	71.75-36.70	74.25-35.06	64.81-46.06
AFG	† AMERICAN FINANCIAL GROUP INC	DEC	4.53	1.82	(0.07)	(0.80)	2.46	26.11	21.37	17.31	18.24	17.25	26.70-18.00	30.30-17.90	30.75-18.35	29.00-18.38	43.63-24.50
AIG	* AMERICAN INTERNATIONAL GROUP	DEC	3.55	2.11	2.10	2.43	2.18	24.39	20.32	19.94	16.98	14.33	66.35-42.92	80.00-47.61	98.31-66.00	103.75-52.38	75.25-51.00
HIG	* HARTFORD FINL SVCS GRP INC	DEC	(0.33)	4.01	2.31	4.42	3.83	35.00	35.31	29.81	32.98	25.16	59.27-31.64	70.24-37.25	71.15-45.50	80.00-29.38	66.44-36.50
HCC	† HCC INSURANCE HOLDINGS INC	DEC	1.69	1.70	0.52	1.11	0.51	10.02	8.54	7.07	5.23	3.97	32.09-22.30	28.95-19.11	29.65-20.50	27.19-10.94	25.13-8.00
HMN	† HORACE MANN EDUCATORS CORP	DEC	0.44	0.28	0.63	0.51	1.08	10.67	10.53	9.17	8.29	7.26	16.95-12.43	24.08-13.61	22.40-14.80	22.19-12.00	33.00-19.13
LTR	* LOEWS CORP	DEC	(4.21)	4.49	(2.75)	9.44	2.40	57.86	59.63	48.70	54.82	45.79	49.48-38.25	62.30-37.50	72.50-41.05	52.47-19.13	52.25-29.25
UTR	† UNITRIN INC	DEC	1.83	(0.12)	5.64	1.32	2.76	21.75	21.56	23.27	19.93	18.98	42.50-21.50	42.80-27.85	41.95-33.90	41.13-27.19	42.38-30.50
<b>INSURANCE BROKERS†</b>																	
AOC	* AON CORP	DEC	2.08	1.65	0.54	1.84	1.35	(0.60)	(1.41)	(2.29)	(2.03)	(3.16)	26.79-17.41	39.63-13.30	44.80-29.75	42.75-20.69	46.67-26.06
BRO	† BROWN & BROWN INC	DEC	1.61	1.24	0.86	0.58	0.50	0.40	0.17	2.77 J	2.12 J	1.88 J	37.66-26.75	37.00-24.00	31.50-14.38	17.94-7.81	10.16-7.33
AJG	† GALLAGHER (ARTHUR J.) & CO	DEC	1.63	1.49	1.48	1.12	0.93	4.40	4.44	3.60	3.75	3.14	32.74-23.28	37.24-21.70	38.82-21.88	34.25-11.53	16.56-10.56
HRH	§ HILB ROGAL & HOBBS CO	DEC	2.17	2.09	1.18	0.85	0.75	(5.08)	(3.92)	(4.54)	(4.08)	(4.32)	43.89-27.16	46.15-26.65	31.38-16.88	21.06-12.81	14.56-7.78
MMC	* MARSH & MCLENNAN COS	DEC	2.89	2.52	1.77	2.17	1.38	(0.66)	(0.72)	(0.28)	(0.45)	(2.57)	54.97-38.27	57.30-34.61	59.03-39.50	67.84-35.25	48.38-28.56

Note: Data as originally reported. § S&P 1500 Index group. \* Company included in the S&P 500. † Company included in the S&P MidCap. § Company included in the S&P SmallCap. # Of the following calendar year. J-This amount includes intangibles that cannot be identified. NM - Not meaningful.

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