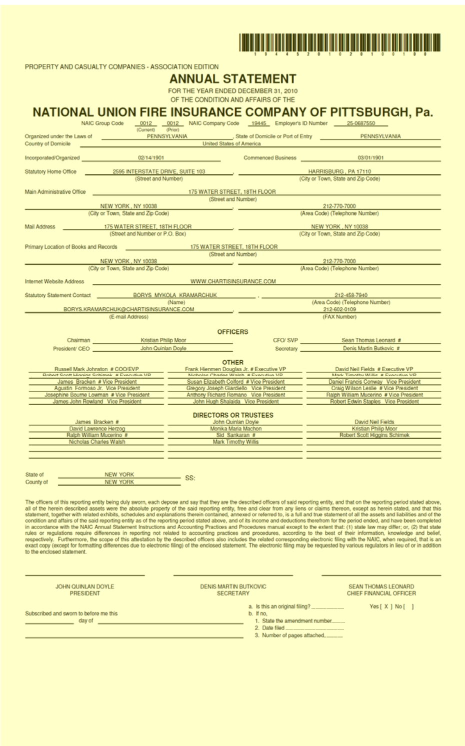
Navigating Today's Underwriting Cycle

Stephen J. Mildenhall
May 11, 2010

Disclosure and Disclaimer

- Accent
- US-centric view



PROPERTY AND CASUALTY COMPANIES - ASSOCIATION EDITION

ANNUAL STATEMENT

FOR THE YEAR ENDED DECEMBER 31, 2010
OF THE CONDITION AND AFFAIRS OF THE

NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, Pa.

NAIC Group Code 0012 (Current) 0012 (Prior) NAIC Company Code 19445 Employer's ID Number 25-0687550

Organized under the Laws of PENNSYLVANIA, State of Domicile or Port of Entry PENNSYLVANIA
Country of Domicile United States of America

Incorporated/Organized 02/14/1901 Commenced Business 03/01/1901

Statutory Home Office 2595 INTERSTATE DRIVE, SUITE 103 (Street and Number), HARRISBURG, PA 17110 (City or Town, State and Zip Code)

Main Administrative Office 175 WATER STREET, 18TH FLOOR (Street and Number)
NEW YORK, NY 10038 (City or Town, State and Zip Code), 212-770-7000 (Area Code) (Telephone Number)

Mail Address 175 WATER STREET, 18TH FLOOR (Street and Number or P.O. Box), NEW YORK, NY 10038 (City or Town, State and Zip Code)

Primary Location of Books and Records 175 WATER STREET, 18TH FLOOR (Street and Number)
NEW YORK, NY 10038 (City or Town, State and Zip Code), 212-770-7000 (Area Code) (Telephone Number)

Internet Website Address WWW.CHARTISINSURANCE.COM

Statutory Statement Contact BORYS MYKOLA KRAMARCHUK (Name), 212-458-7940 (Area Code) (Telephone Number)
BORYS.KRAMARCHUK@CHARTISINSURANCE.COM (E-mail Address), 212-602-0109 (FAX Number)

OFFICERS

Chairman Kristian Philip Moor — CFO/ SVP Sean Thomas Leonard #
President/ CEO John Quinlan Doyle — Secretary Denis Martin Butkovic #

OTHER

Russell Mark Johnston # COO/EVP	Frank Hienmen Douglas Jr. # Executive VP	David Neil Fields # Executive VP
Robert Scott Higgins Schimek # Executive VP	Nicholas Charles Walsh # Executive VP	Mark Timothy Willis # Executive VP
James Bracken # Vice President	Susan Elizabeth Colford # Vice President	Daniel Francis Conway Vice President
Agustin Formoso Jr. Vice President	Gregory Joseph Giardiello Vice President	Craig Wilson Leslie # Vice President
Josephine Bourne Lowman # Vice President	Anthony Richard Romano Vice President	Ralph William Mucerino # Vice President
James John Rowland Vice President	John Hugh Shalaida Vice President	Robert Edwin Staples Vice President

DIRECTORS OR TRUSTEES

James Bracken #	John Quinlan Doyle	David Neil Fields
David Lawrence Herzog	Monika Maria Machon	Kristian Philip Moor
Ralph William Mucerino #	Sid Sankaran #	Robert Scott Higgins Schimek
Nicholas Charles Walsh	Mark Timothy Willis	

State of NEW YORK
County of NEW YORK SS:

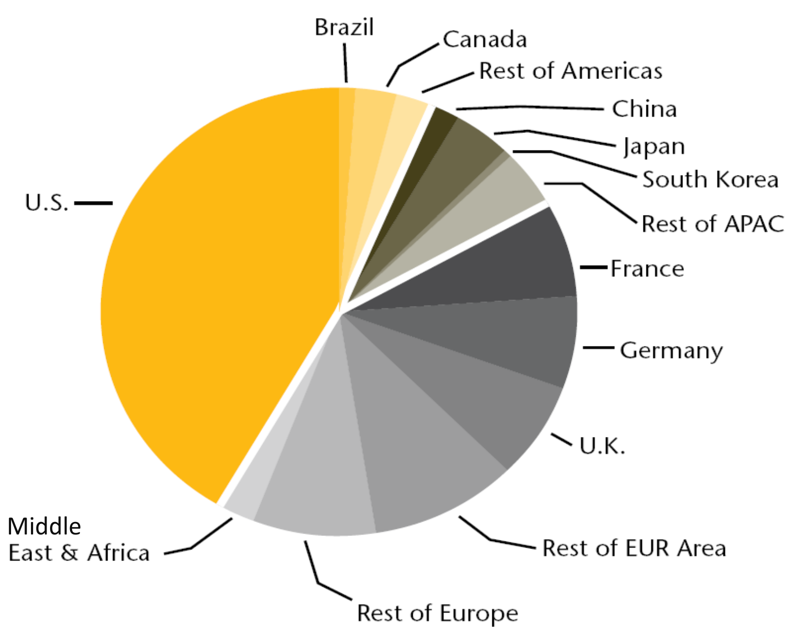
The officers of this reporting entity being duly sworn, each depose and say that they are the described officers of said reporting entity, and that on the reporting period stated above, all of the herein described assets were the absolute property of the said reporting entity, free and clear from any liens or claims thereon, except as herein stated, and that this statement, together with related exhibits, schedules and explanations therein contained, annexed or referred to, is a full and true statement of all the assets and liabilities and of the condition and affairs of the said reporting entity as of the reporting period stated above, and of its income and deductions therefrom for the period ended, and have been completed in accordance with the NAIC Annual Statement Instructions and Accounting Practices and Procedures manual except to the extent that: (1) state law may differ; or, (2) that state rules or regulations require differences in reporting not related to accounting practices and procedures, according to the best of their information, knowledge and belief, respectively. Furthermore, the scope of this attestation by the described officers also includes the related corresponding electronic filing with the NAIC, when required, that is an exact copy (except for formatting differences due to electronic filing) of the enclosed statement. The electronic filing may be requested by various regulators in lieu of or in addition to the enclosed statement.

JOHN QUINLAN DOYLE, PRESIDENT — DENIS MARTIN BUTKOVIC, SECRETARY — SEAN THOMAS LEONARD, CHIEF FINANCIAL OFFICER

Subscribed and sworn to before me this ____ day of ____

a. Is this an original filing? Yes [X] No [ ]
b. If no,
1. State the amendment number
2. Date filed
3. Number of pages attached

$388B Global Property Premium



World ….as in World Series

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Navigating Today's Underwriting Cycle

Navigating

Maps & sextants

Where are we?

Predictions?

Today's

Different today?

How?

Why?

Underwriting Cycle

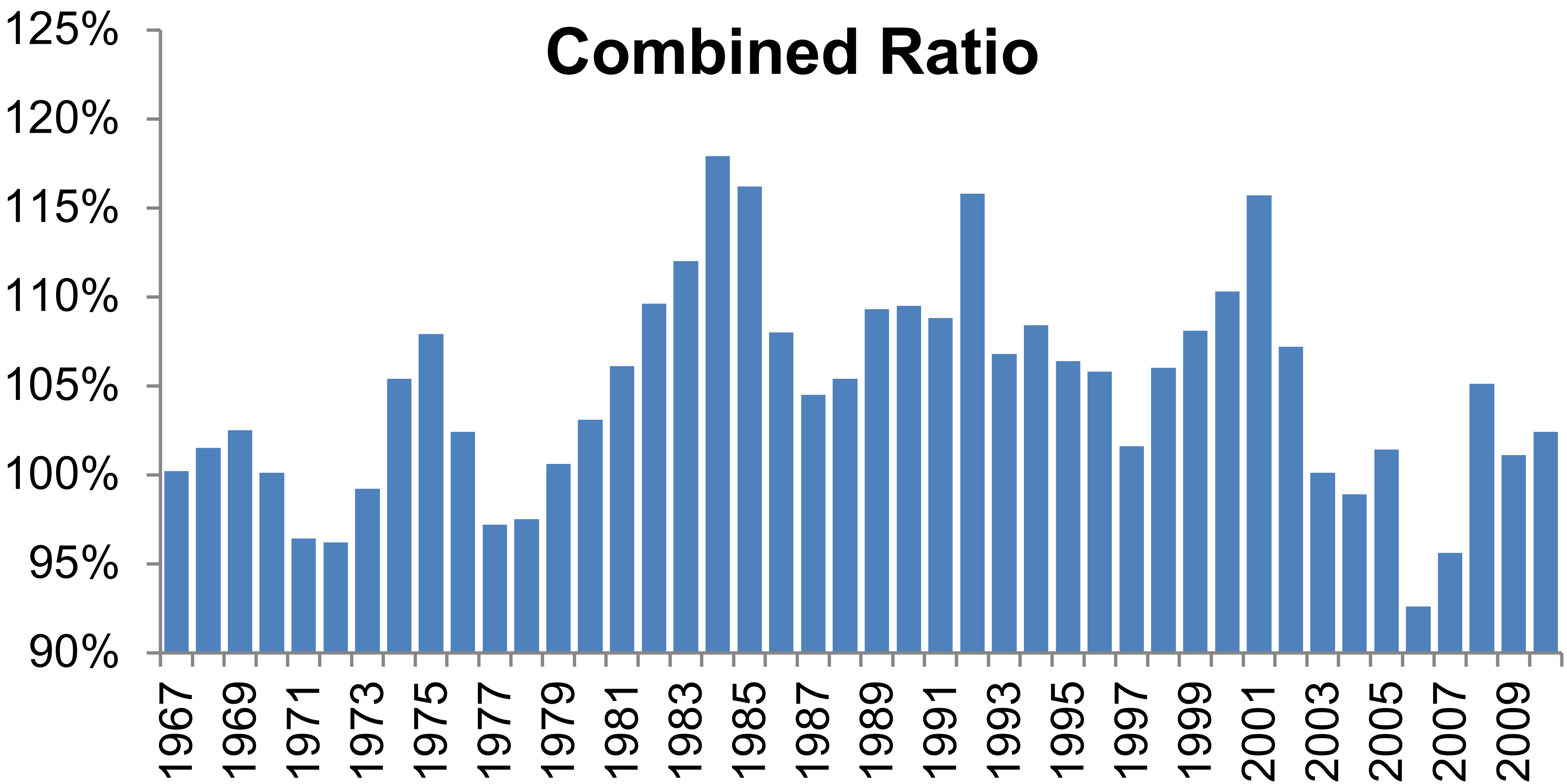
What is the cycle?

Why is there a cycle?

Ups and downs

Q. What is the right price for underwriting an insurance risk?
A. It is where the perfume of the premium overcomes the pong of the peril.

What is the Cycle?



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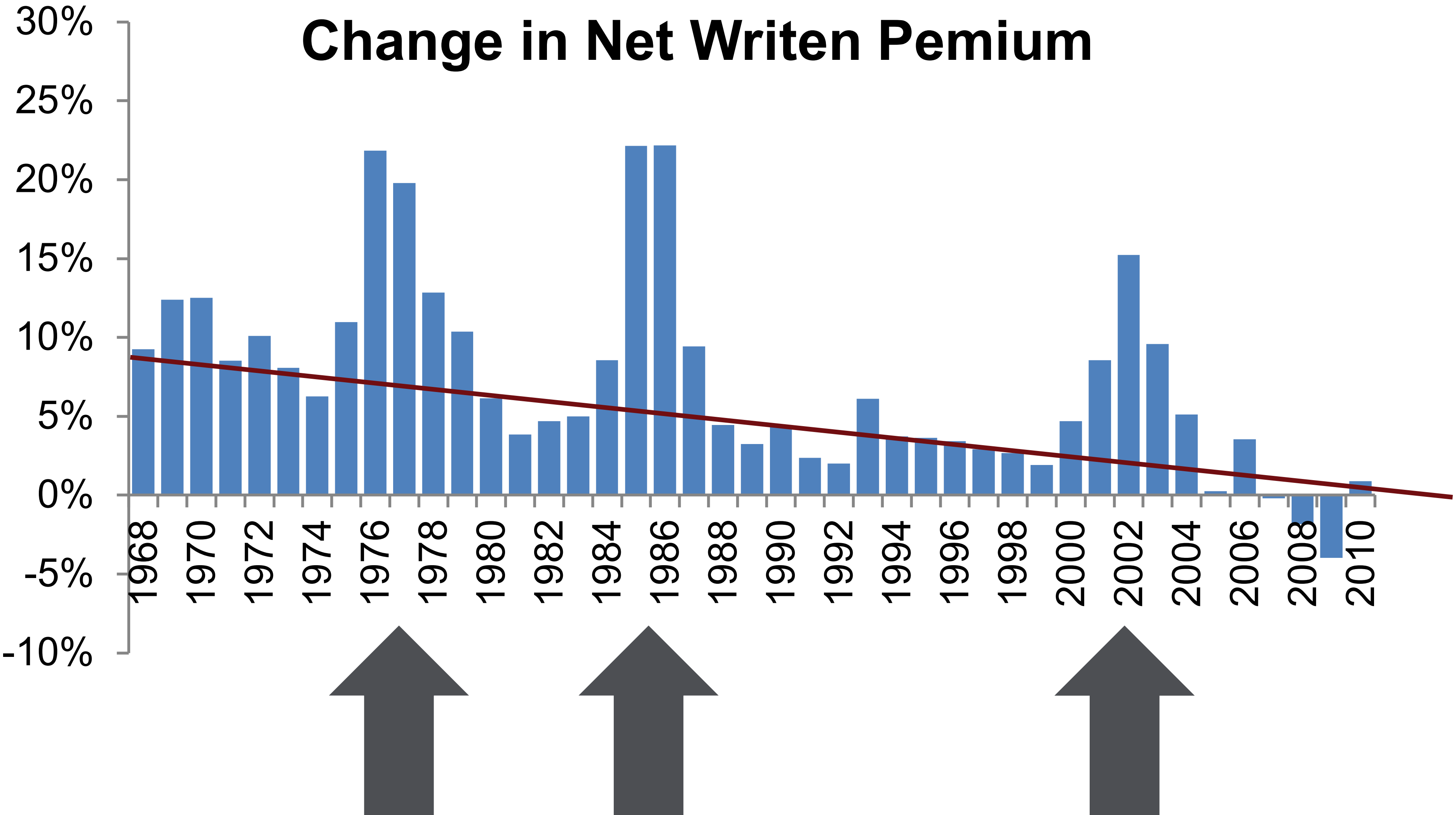
What is the Cycle?



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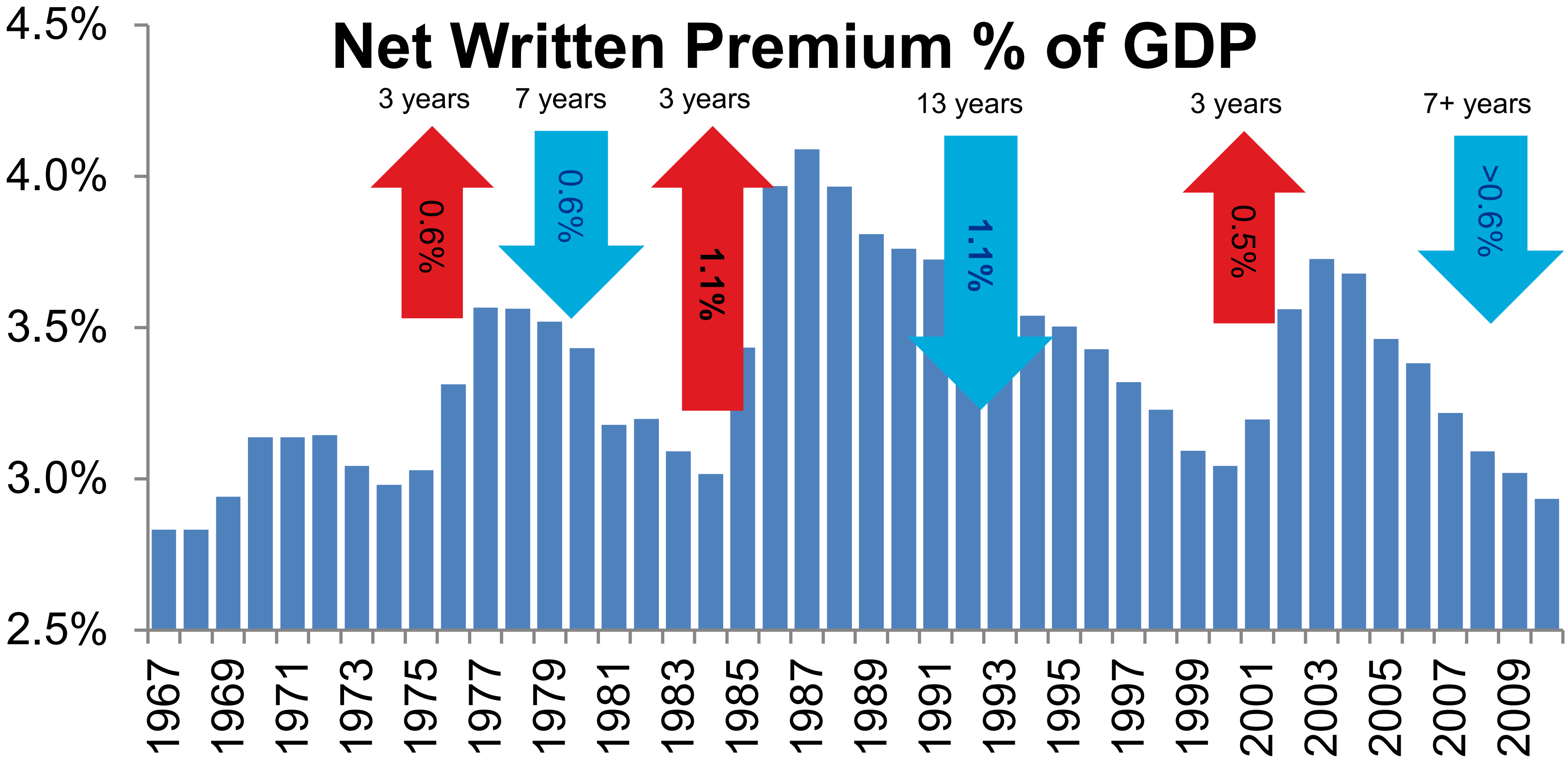
What is the Cycle?



Why is there a Cycle?

- Capital
  – Supply and demand driven
  – Capital markets inefficiencies (in) and regulatory constraints (out)

- Inability to manage capital: surplus grows more quickly than premium

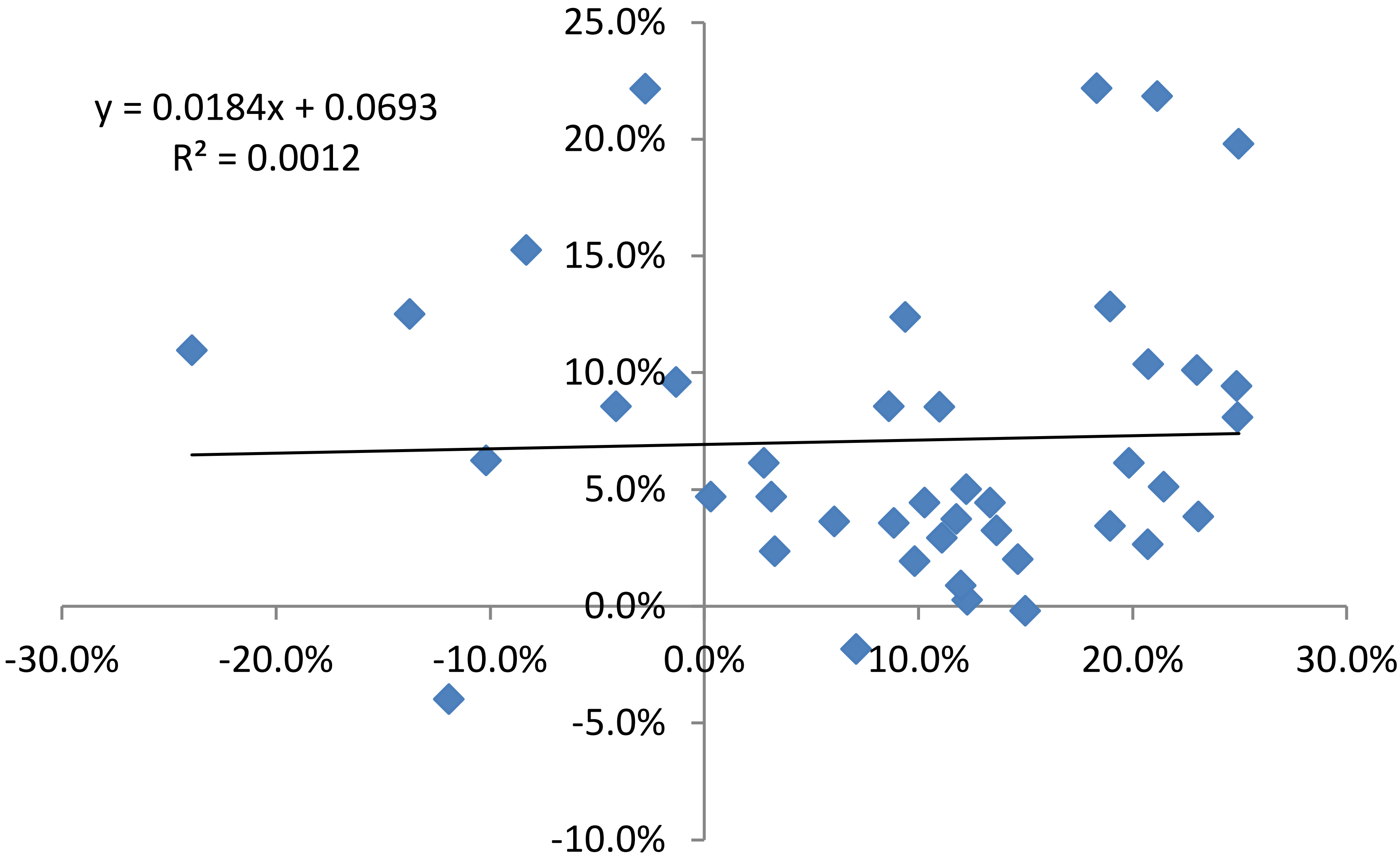
- Operating Cash Flow or Investment Income
  – Market will not turn while there are funds to invest

- Past losses or past premium
  – Underwriting results drive market turn

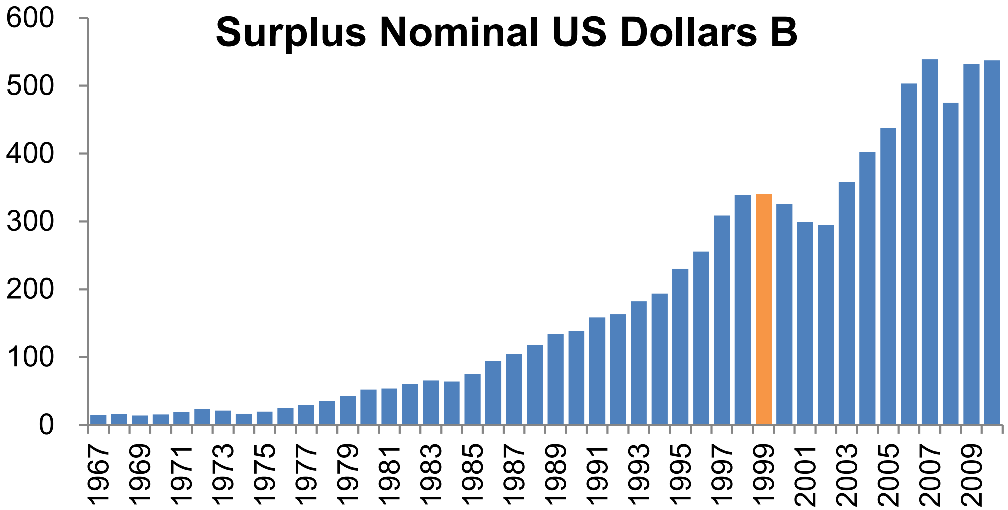
- Inadequacies in actuarial methods, reserving cycle

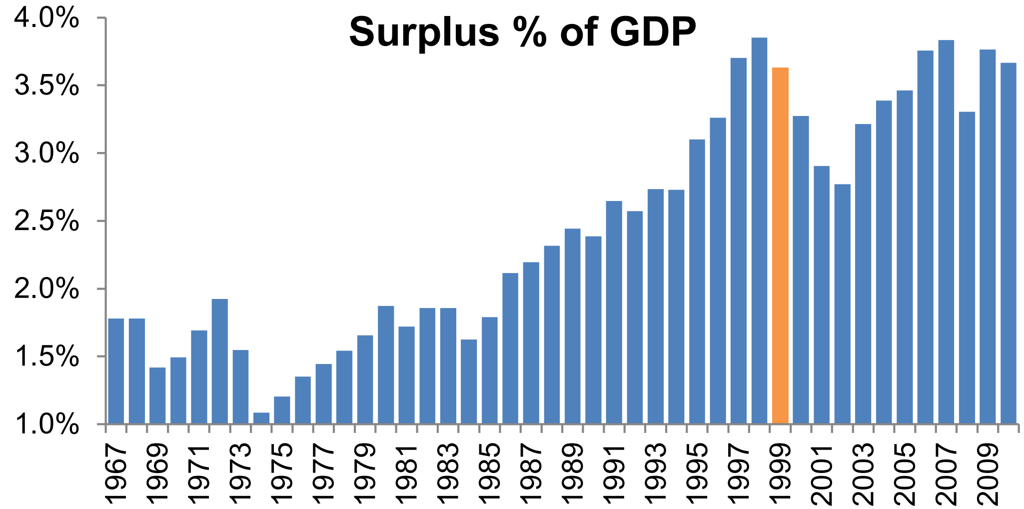
Why is there a Cycle: Capital Driven?

Prior Year Change in Surplus vs. Change in Premium



Change in Surplus vs. Change in Surplus/GDP

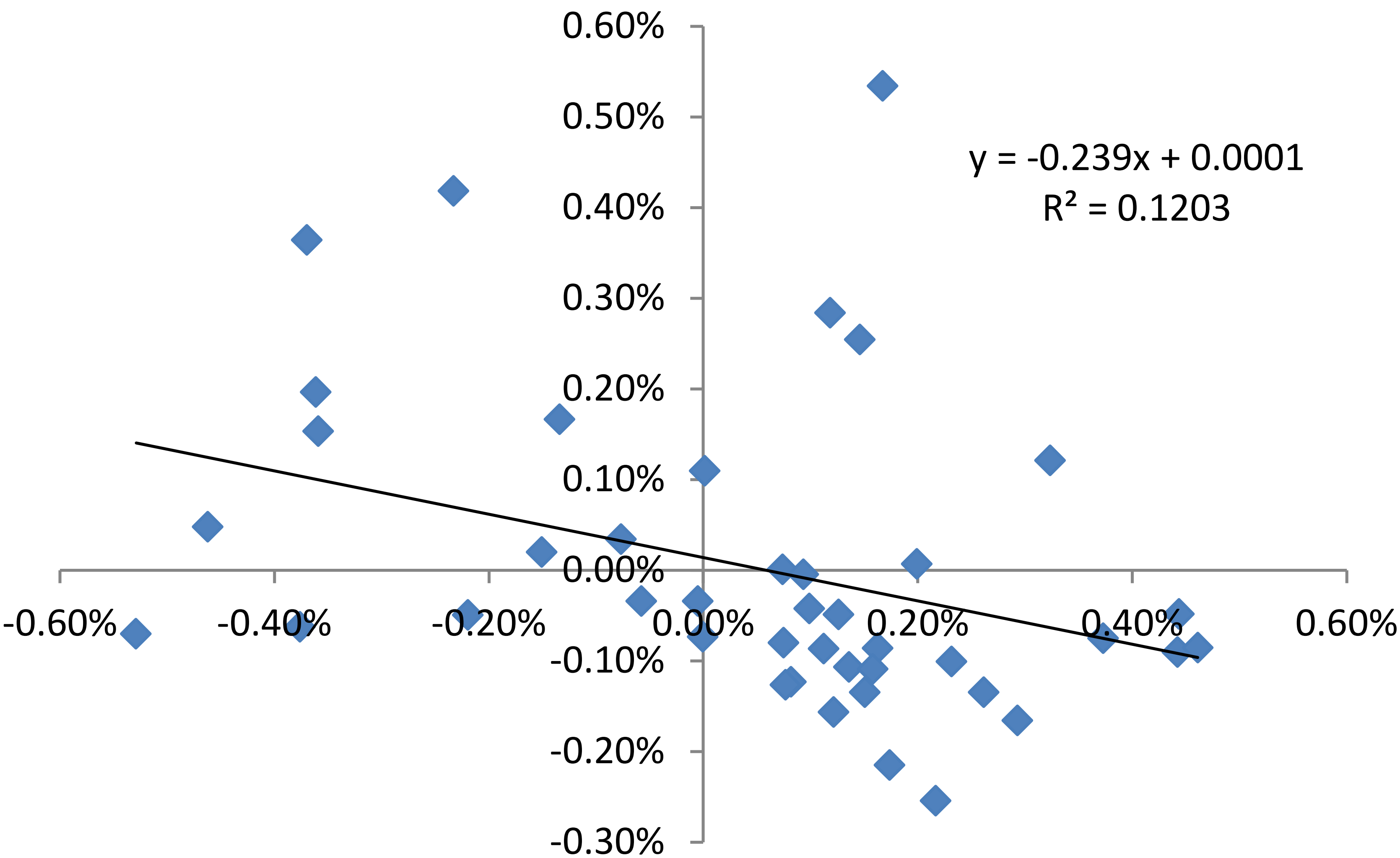




- Change in surplus relative to GDP is a more informative variable than straight change in surplus
- Industry surplus grew 1999 over 1998, but shrank moderately as a percentage of GDP
- Cat reinsurance: surplus relative to measured PML

Why is there a Cycle: Capital Driven?

Prior Year Change in Surplus/GDP vs. Change in Premium/GDP



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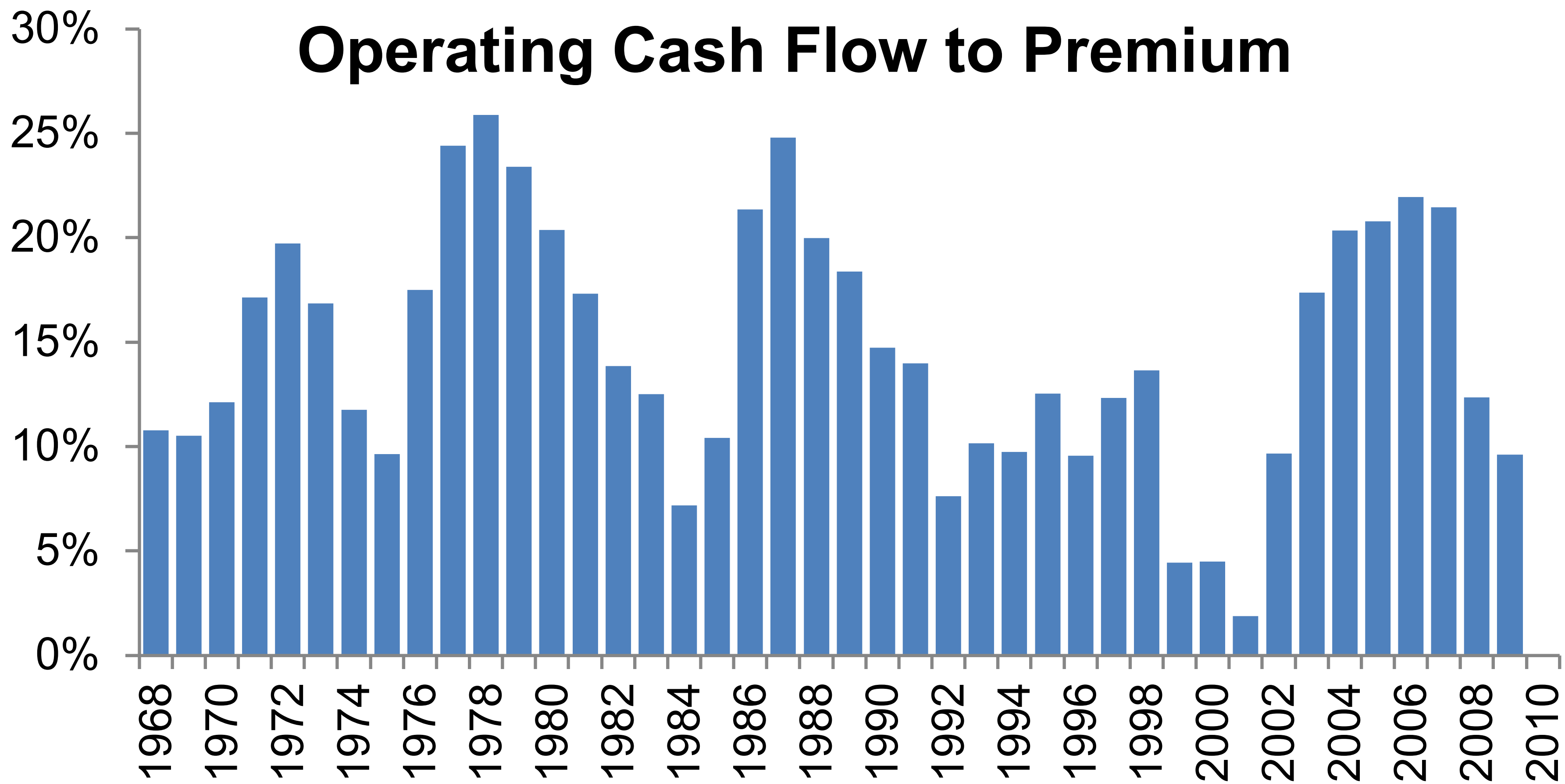
Why is there a Cycle?



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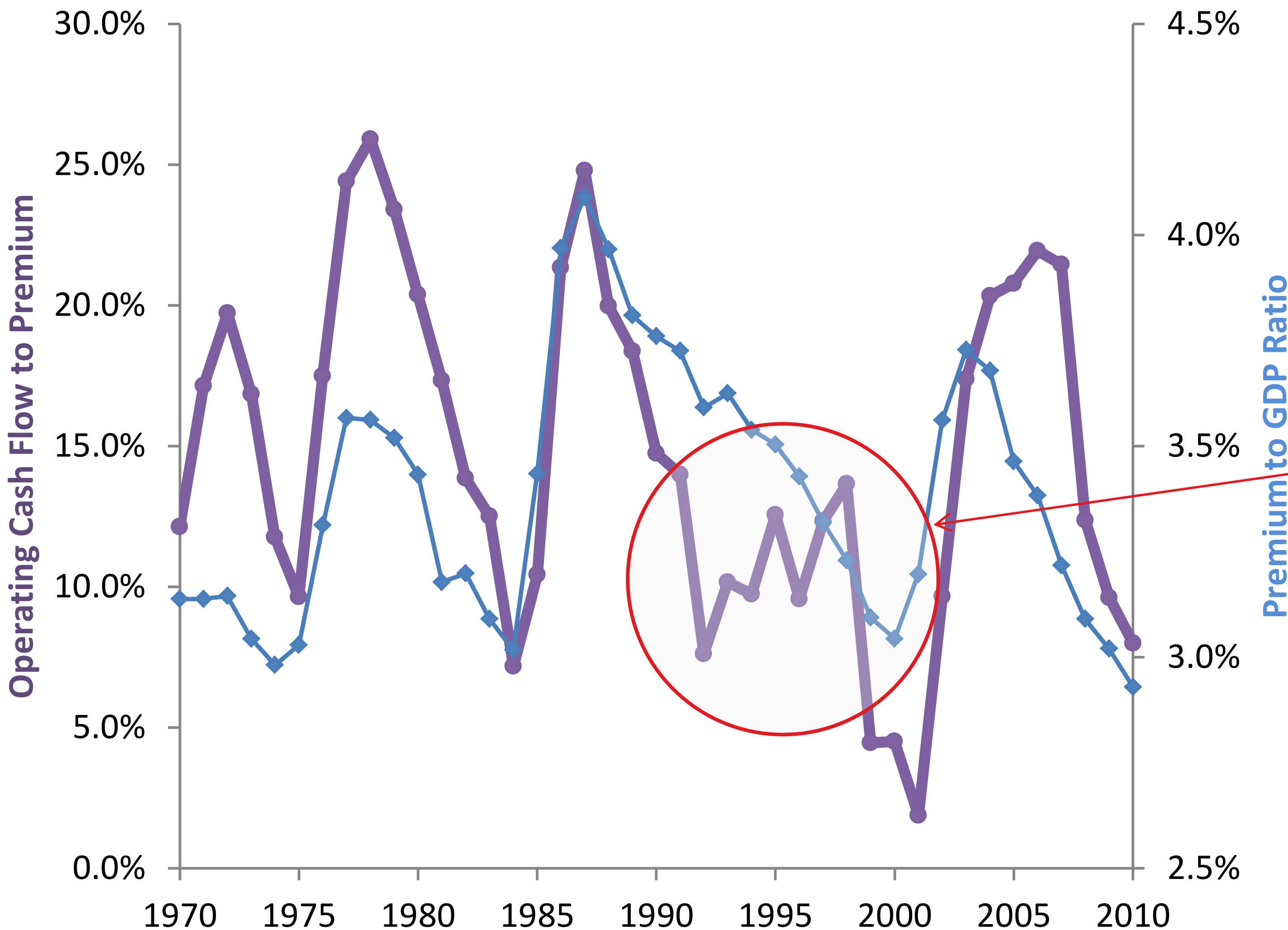
Why is there a Cycle?

Operating Cash Flow and Premium to GDP



Peaks and troughs align

Strong investment income keeps cash flow positive in late 1990s and prolongs soft market

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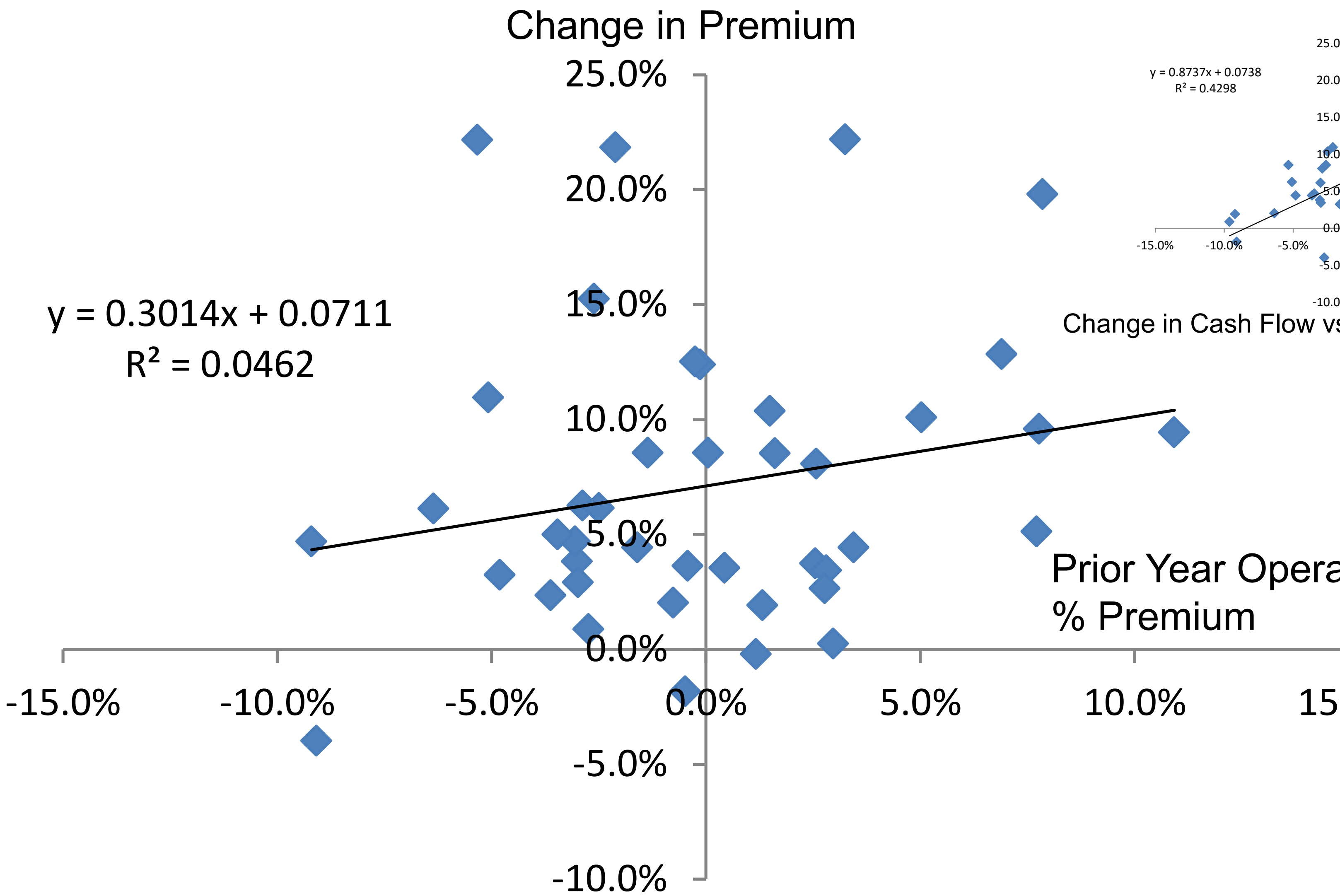
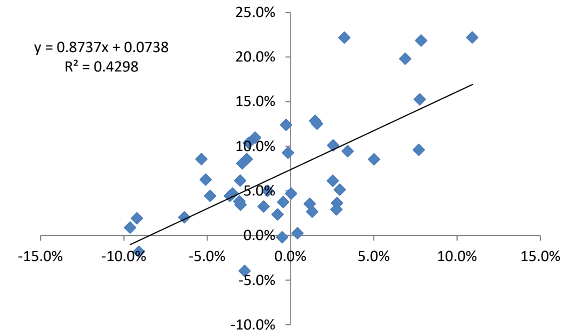
Why is there a Cycle?
Not Strongly Predicted by Operating Cash Flow





Change in Cash Flow vs. Change in Premium

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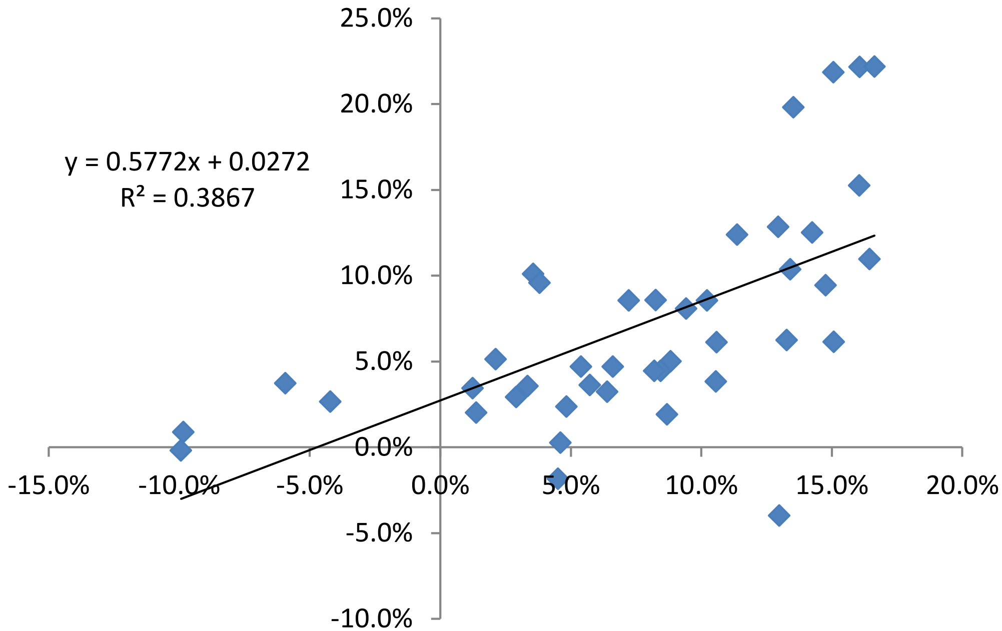
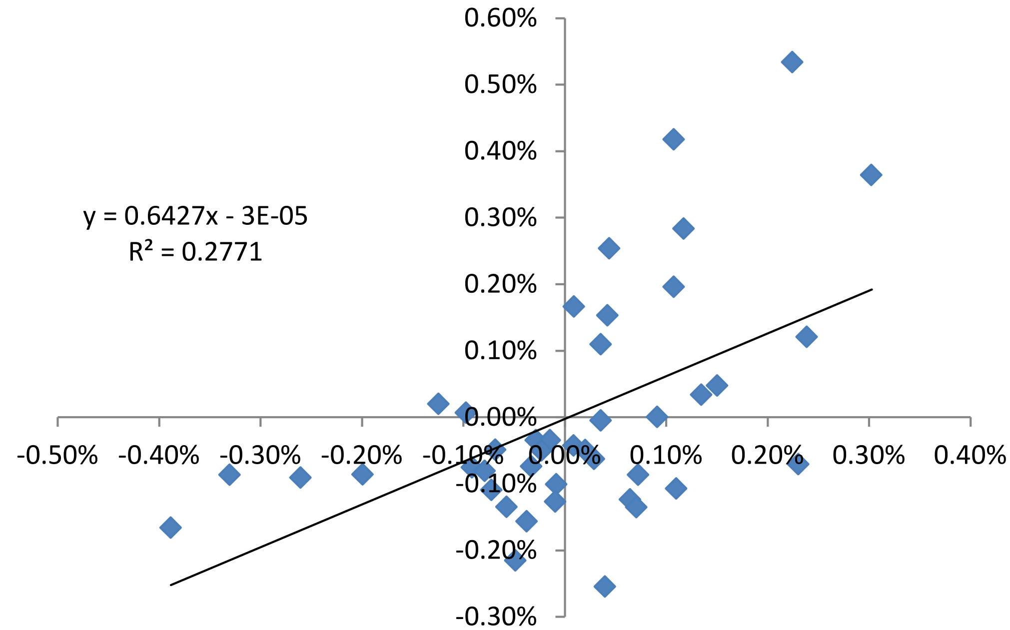
Why is there a Cycle?

Prior Year Change in Loss vs. Current Year Change in Premium





Prior year change in calendar year incurred loss (x-axis) vs. current year change in premium

Prior year change in calendar year incurred loss / GDP (x-axis) vs. current year change in premium / GDP

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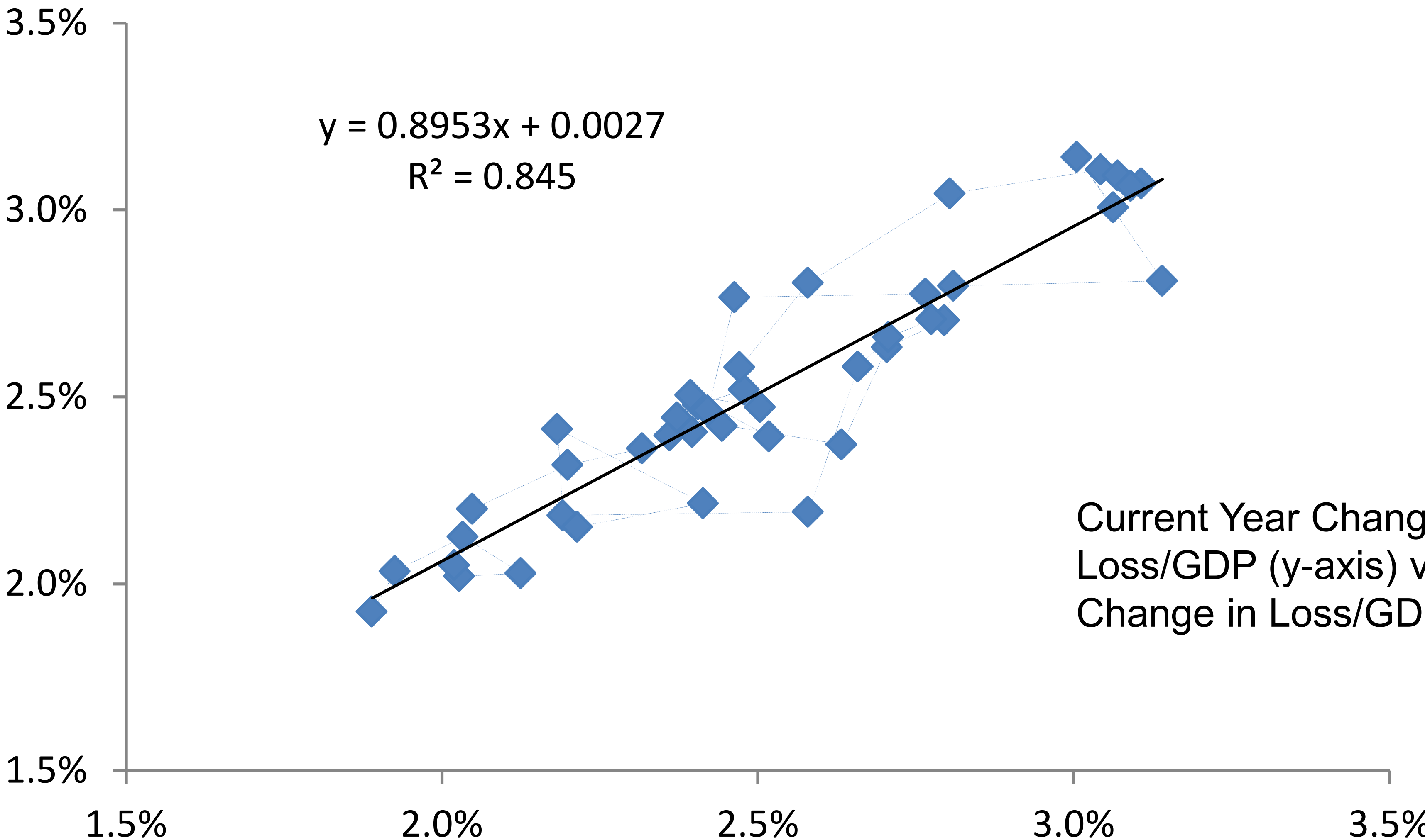
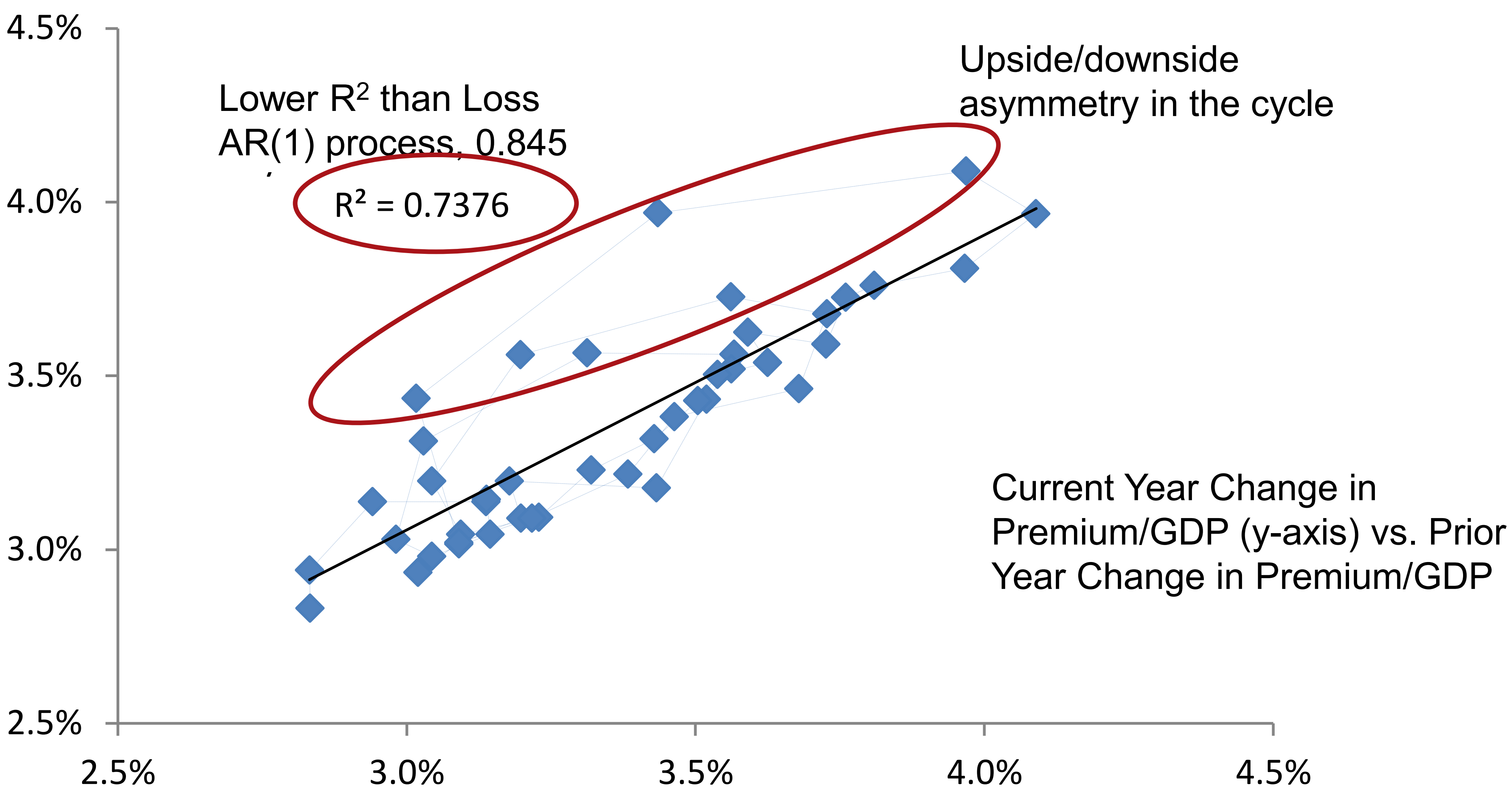
Why is there a Cycle?

Prior Year Change in Loss/GDP vs. Current Year Change



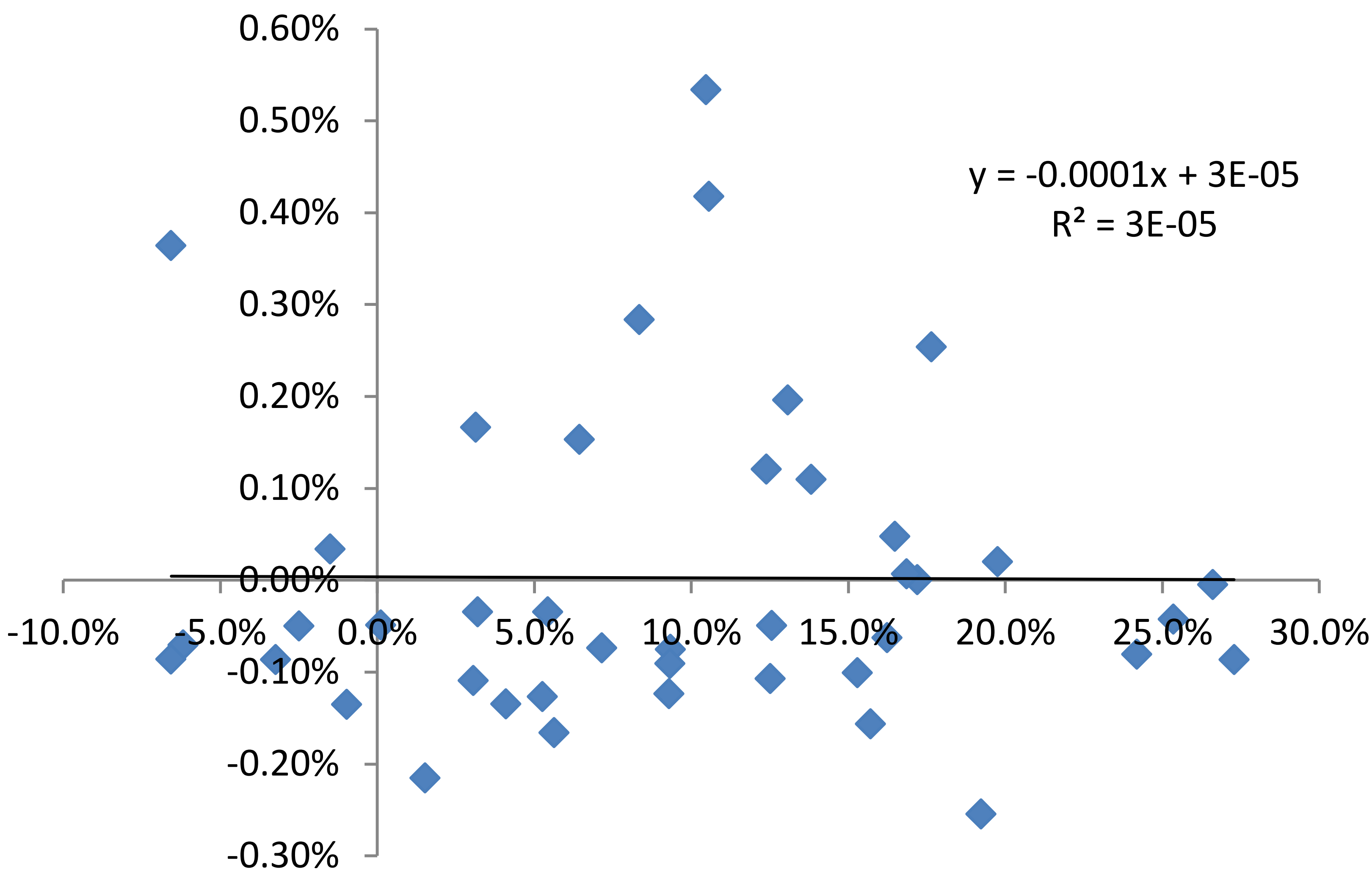
Current Year Change in Loss/GDP (y-axis) vs. Prior Year Change in Loss/GDP

Why is there a Cycle?
Prior Year Premium/GDP vs. Current Year Change



Why is there a Cycle?

Prior Year Change in Inv. Inc. Current Year Change Premium/GDP



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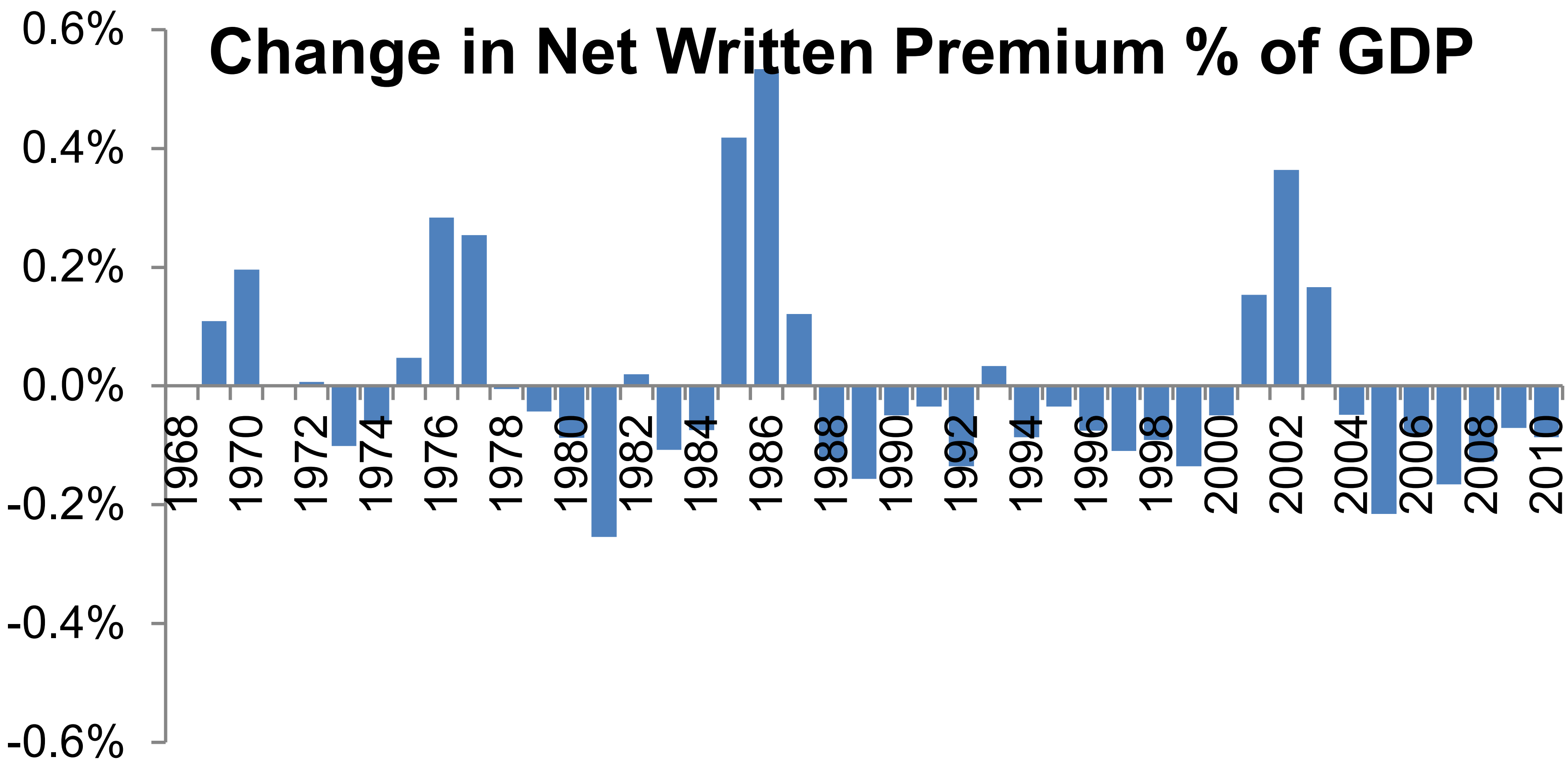
Why is there a Cycle?

- Prior year capital, loss and premium predictive, with expected signs
- Operating cash flows and investment income are not predictive
- Asymmetry: “up the elevator, down the escalator”
- Hardening phases easier to understand than softening

Up the Elevator and Down the Escalator



Is the Cycle Different Today?

- Long period of favorable frequency trends
  - All liability lines have experienced favorable frequency trends and controlled severity trends
  - Headlines around property and reserve releases

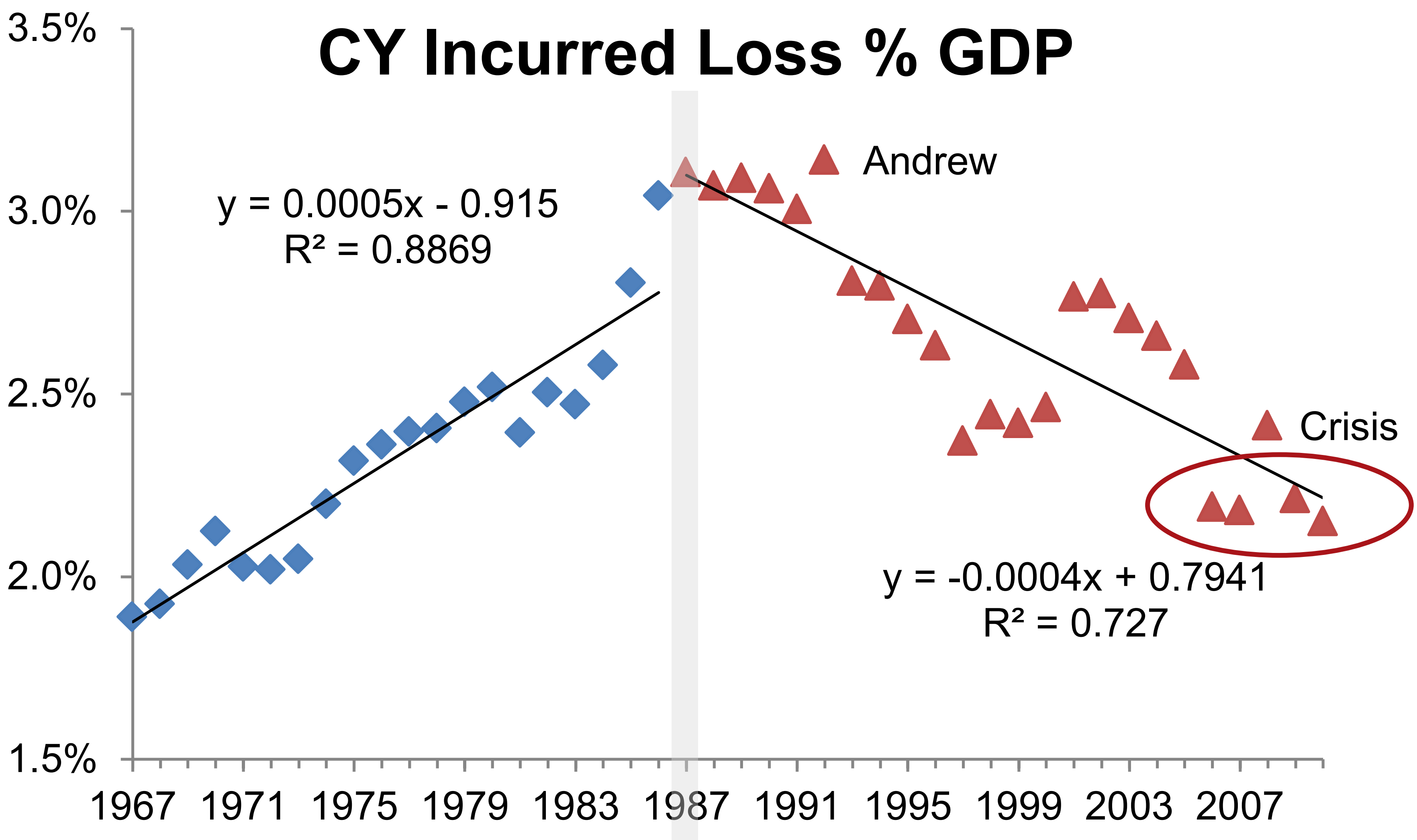
- Professional, transparent reinsurers and new capital at Lloyds have not supported soft market pricing
  - Big increase in retentions for casualty lines…and lost out on profitable business
  - No Unicover, working casualty treaties

- Historically favorable combined ratios…but historically low leverage ratios and low investment returns that change the target combined

- Continued focus on rate monitoring from soft market

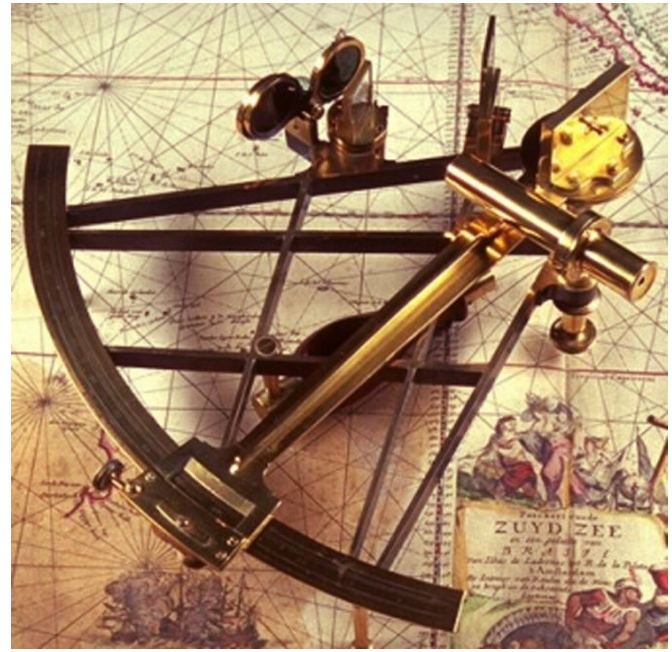
…Yes

A Different Cycle Since 1987 Tax Reform



Maps and Sextants: Navigation Tools

- ERM / ECM, cat models, capital models, predictive models
- Solvency II: unclear if S2 will be a net benefit
- Property driven problems vs. liability in 1980s and 1990s…but property risk “understood” using catastrophe models and absorbed by new startups
- Easy to talk about courage when the line is in the distance
- Tools don’t make the decisions easier



There is nothing complex about the cycle. It is about having the courage of your convictions to act with strength.
Rolf Tolle

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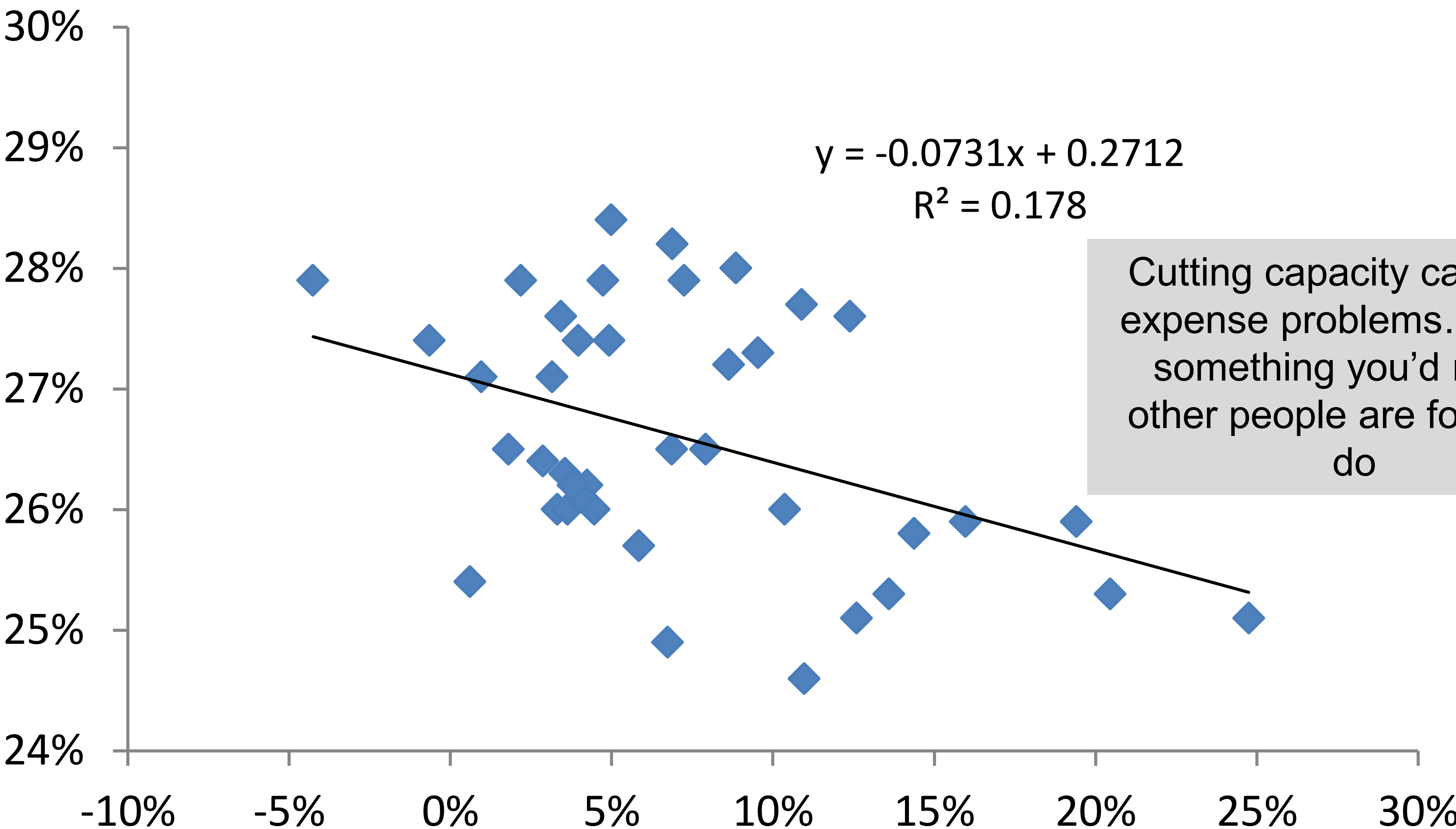
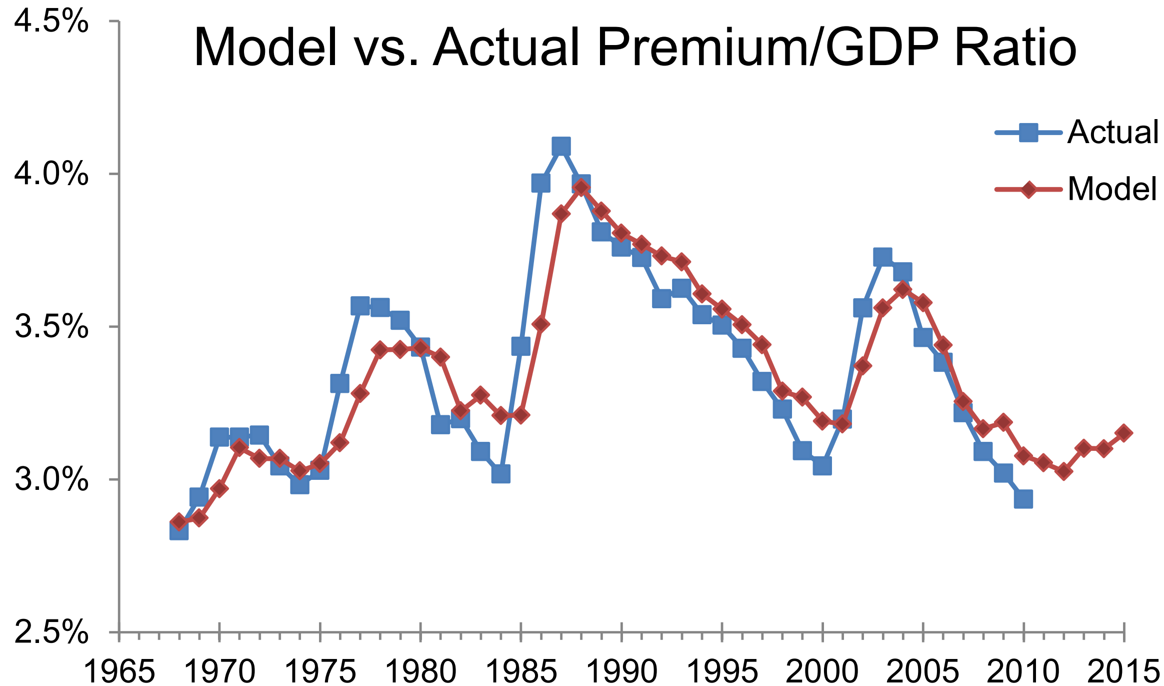
Change in Premium vs. Expense Ratio



Cutting capacity can drive expense problems…and is something you'd rather other people are forced to do

Where are we Now?

- Model of premium/GDP cycle based on prior year loss/GDP and premium/GDP ratios
- Predicts slight bottoming of market but no convincing hardening
- With 2011 loss/GDP like 2008, 0.2 points of GDP higher, model shows 0.7 point increase in premium/GDP ratio for 2012, to 3.1%

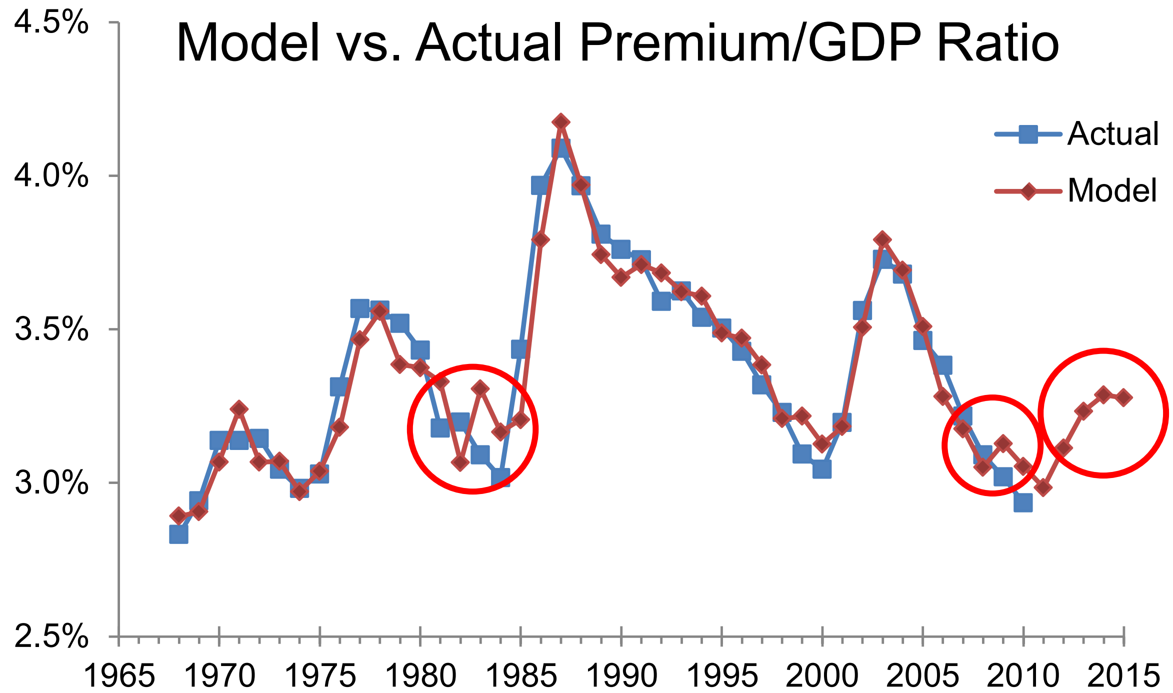


Cycle Model Statistics

	Parameter	Std. Error	p Value
Constant	0.007	0.0025	0.7%
Prior Loss/GDP	0.370	0.1196	0.4%
Prior Premium/GDP	0.512	0.1306	0.0%
Second Prior Premium/GDP			
Regression R^2	78.8%		

Where are we Now?

- Add second prior year premium/GDP ratio to model
- R^2 improves from 79% to 91%
- Predicts slight bottoming of market but no convincing hardening
- With 2011 loss/GDP like 2008, 0.2 points of GDP higher, model shows 0.9 point increase in premium/GDP ratio for 2012, to 3.3%



Cycle Model Statistics

	Parameter	Std. Error	p Value
Constant	0.010	0.0017	7.9E-07
Prior Loss/GDP	0.426	0.0798	4.4E-06
Prior Premium/GDP	1.053	0.1149	1.2E-08
Second Prior Premium/GDP	-0.673	0.0936	2.8E-11
Regression R^2	90.9%		

Predictions

- Market cycle model predicting bottom/slight turn to market
  - Loss level to GDP key driver of future turn, currently at historically low levels
  - Premium components of model consistent with auto regressive noise theory

- A real hard market will be casualty driven
  - Property driven turn to market will be more localized and short lived because of capital sitting on sidelines waiting for profitable opportunities
  - Harder to get capital into a casualty New Co as reserve issues will make investors skittish about injecting new capital
  - 1985 turn, most severe in recent memory, was liability driven

- Possible drivers of casualty based turn – manifest through reserve development
  - Liability catastrophe(s)
  - Reversal of current, favorable frequency trends
  - Severity inflation (not in next 12-18 months)
  - More militant and successful trial bar lawyers

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