

# Trends & Challenges in the Property Insurance Business Today

**Institute for Building & Home Safety Annual Congress**

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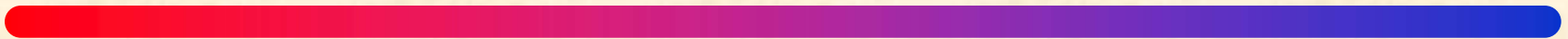


# *Presentation Outline*

- **Overall P/C Insurance Industry Performance**
  - What's more important—property *or* casualty?
- **Property Insurance Performance**
  - Personal Lines (Homeowners)
  - Commercial Property
- **Property Insurance & the Economy: Exposure Analysis**
- **Pricing Trends in Property Insurance**
- **Catastrophe Issues:**
  - Natural Disasters
  - Trial lawyer-made disasters
  - Terrorism
- **Q&A**

# *P/C FINANCIAL OVERVIEW*

*How Much Does Property  
Insurance Matter?*





# *Highlights: Property/Casualty*

## *First Half 2003*

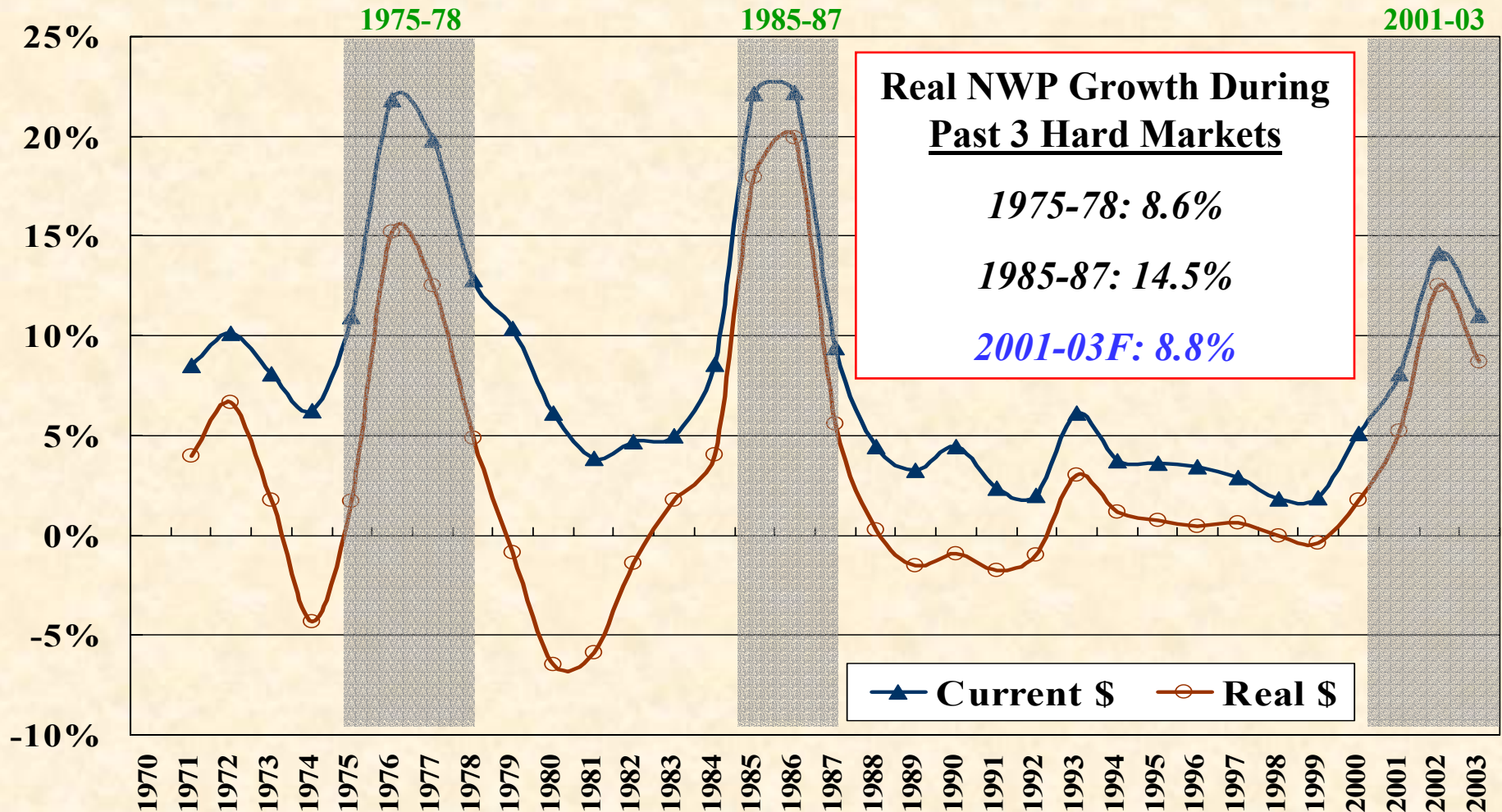
	<b>2003</b>	<b>2002</b>	<b>Change</b>
Net Written Prem.	202,828	182,760	+11.0%
Loss & LAE	142,129	134,897	+5.4%
Net UW Gain (Loss)	(2,070)	(11,422)	-81.9%
Net Inv. Income	18,268	17,894	+2.1%
Net Income (a.t.)	14,496	4,371	+231.6%
Surplus*	312,455	284,300	+9.9%
Combined Ratio	99.8	105.1	-5.3 pts.

\*Comparison with year-end 2002





# Strength of Recent Hard Markets by Real NWP Growth



Note: Shaded areas denote hard market periods.  
Source: A.M. Best, Insurance Information Institute

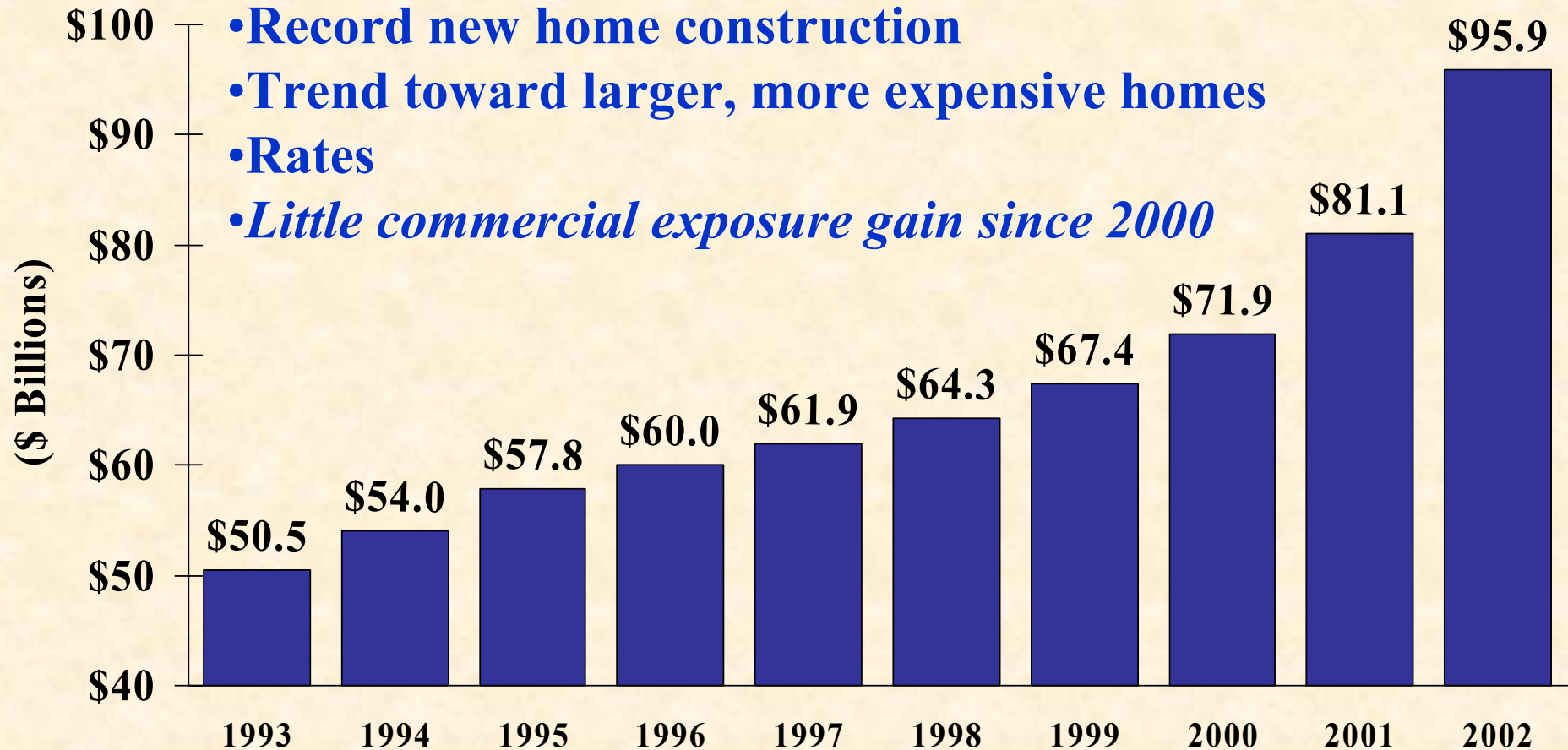
\*2003 figure is estimate on first half result.



# Property Insurance Direct Premiums Written\*

## Revenue Growth Drivers:

- Record new home construction
- Trend toward larger, more expensive homes
- Rates
- *Little commercial exposure gain since 2000*

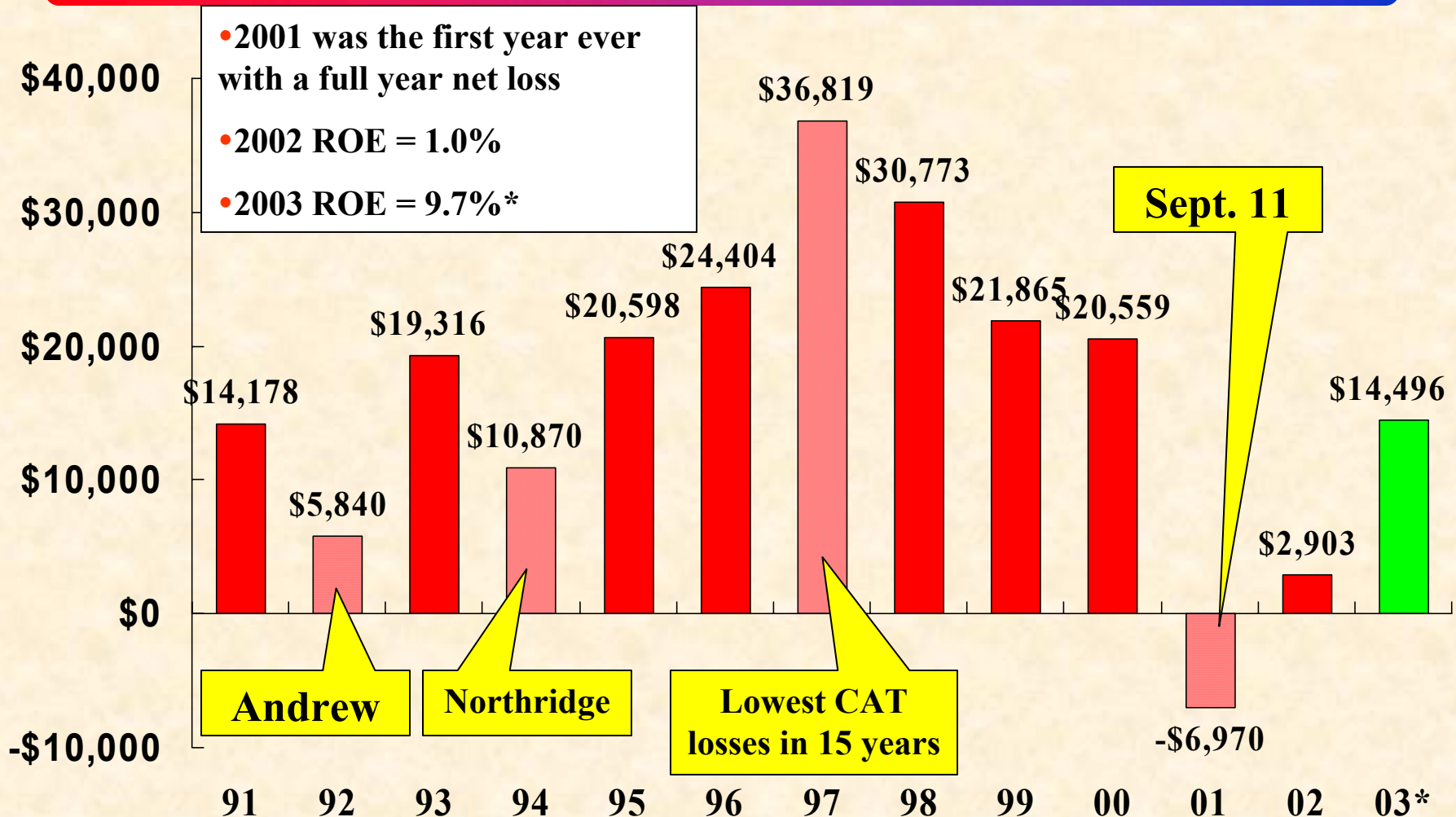


\*Includes Fire, Allied Lines, Multi Peril Crop, Federal Flood, Farm & Homeowners Multi-Peril, CMP-non liability, Inland Marine, Earthquake & Burglary & Theft

Source: Best's Aggregates & Averages - Property/Casualty; Insurance Information Institute



# *P/C Net Income After Taxes* *1991-2003\* (\$ Millions)*



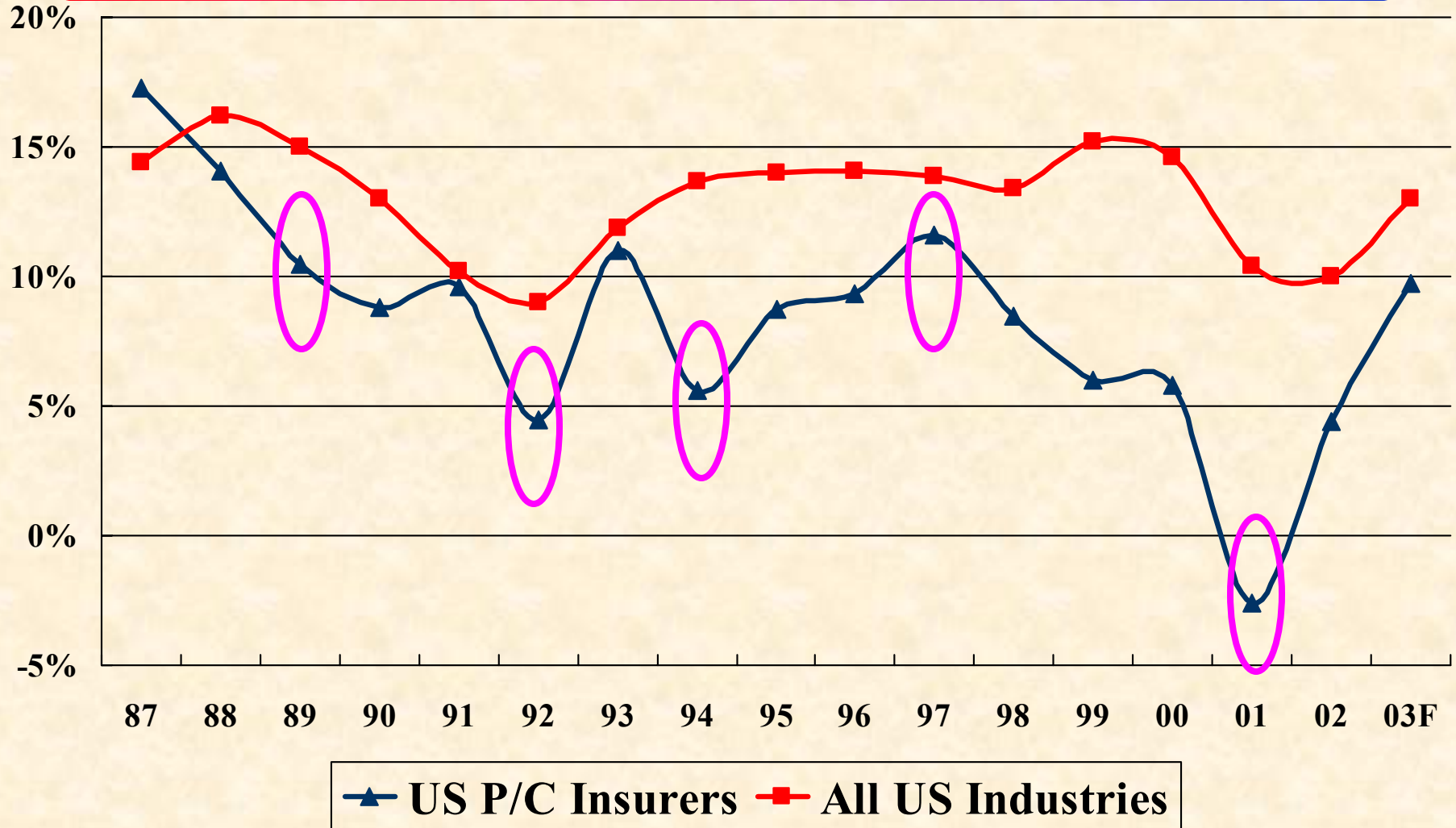
\*First half 2003

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



# ROE: P/C vs. All Industries

## 1987–2003E\*



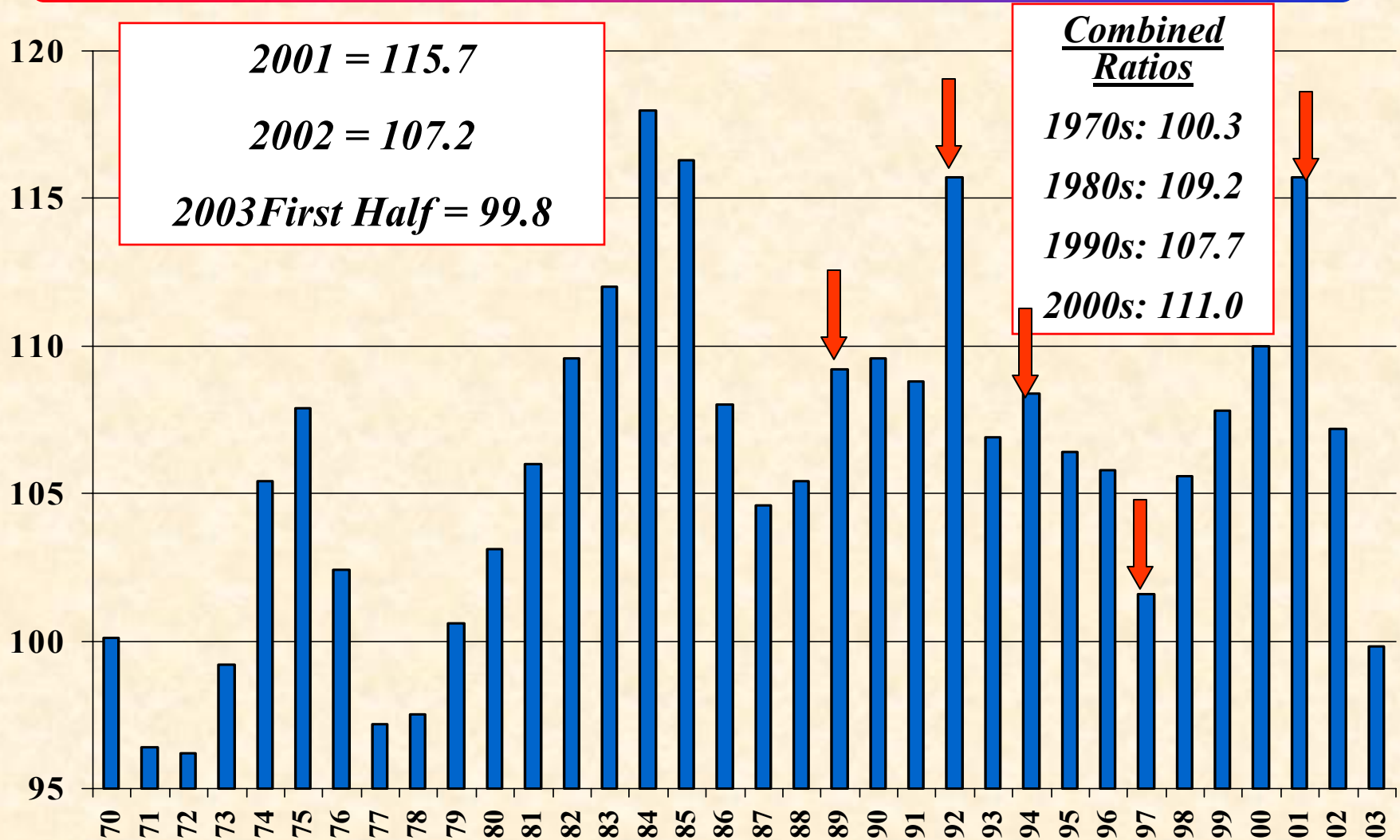
\*2003 p/c estimate based on first half data.

Source: Insurance Information Institute; *Fortune*





# *P/C Industry Combined Ratio*



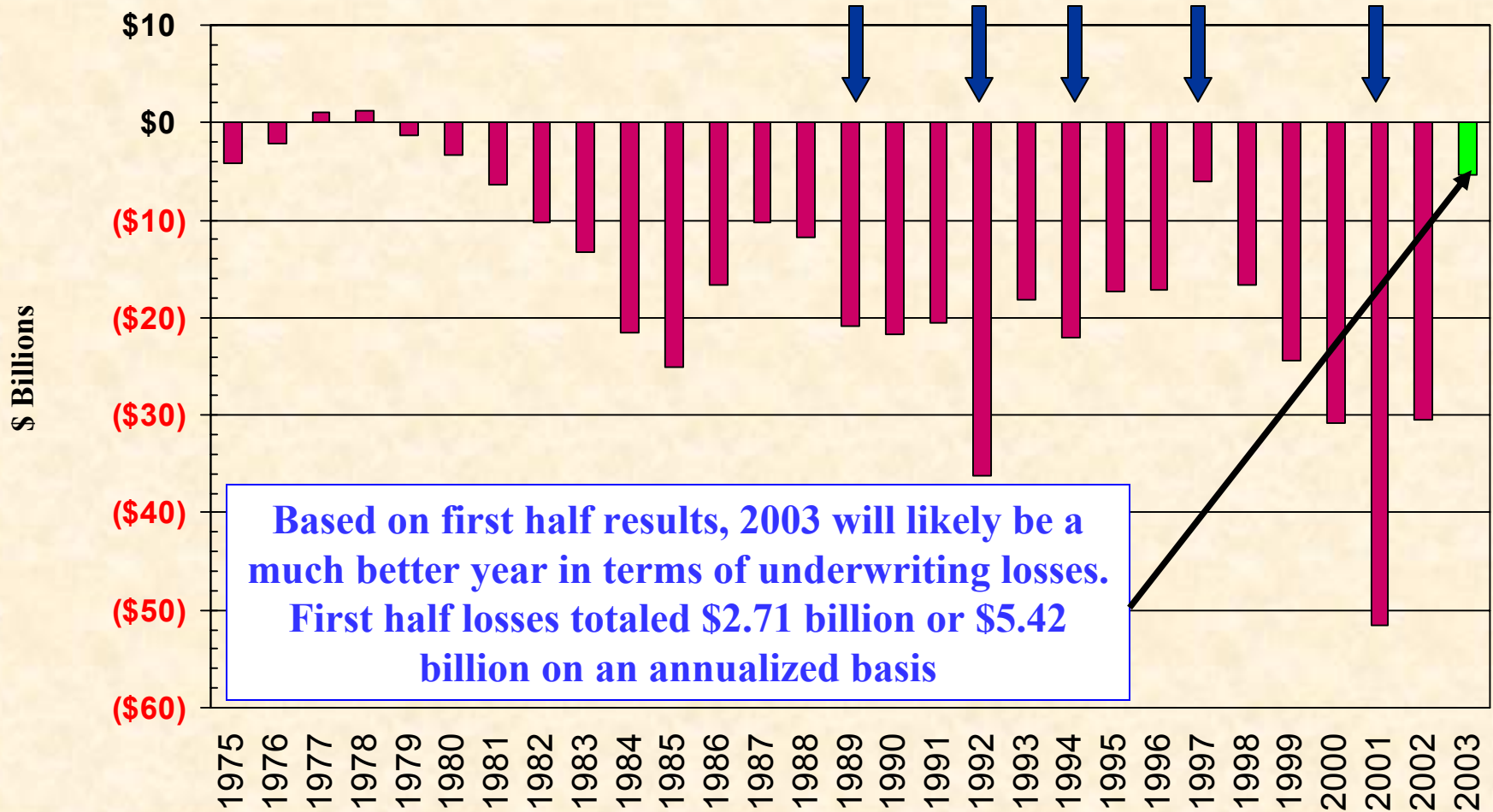
Sources: A.M. Best; ISO, III

\*Based on First Half 2003 results.



# *Underwriting Gain (Loss)*

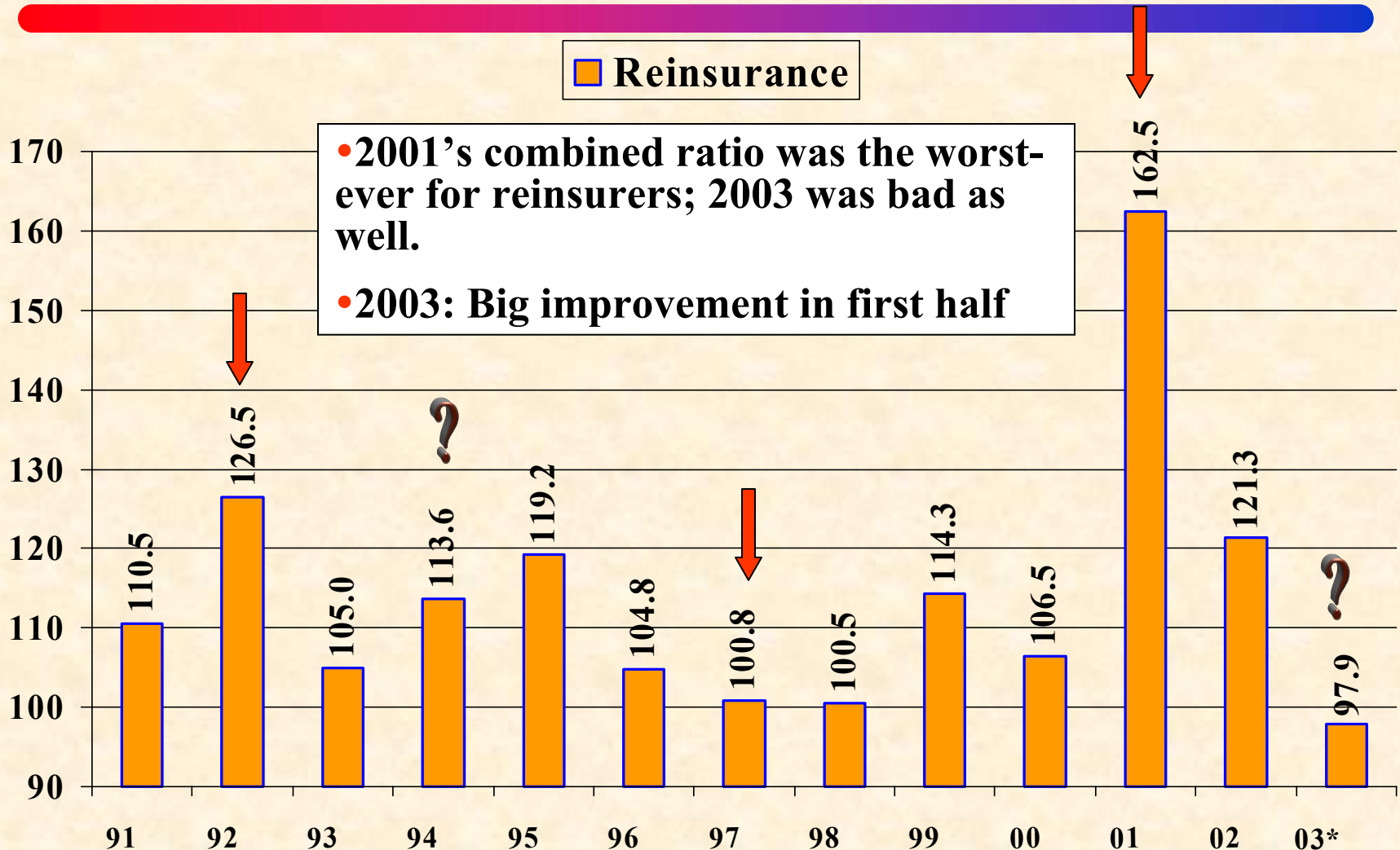
## *1975-2003\**



\*2003 figure of \$5.42 billion is annualized based on first quarter underwriting loss of \$2.71 billion  
Source: A.M. Best, Insurance Information Institute



# Combined Ratio: Reinsurers

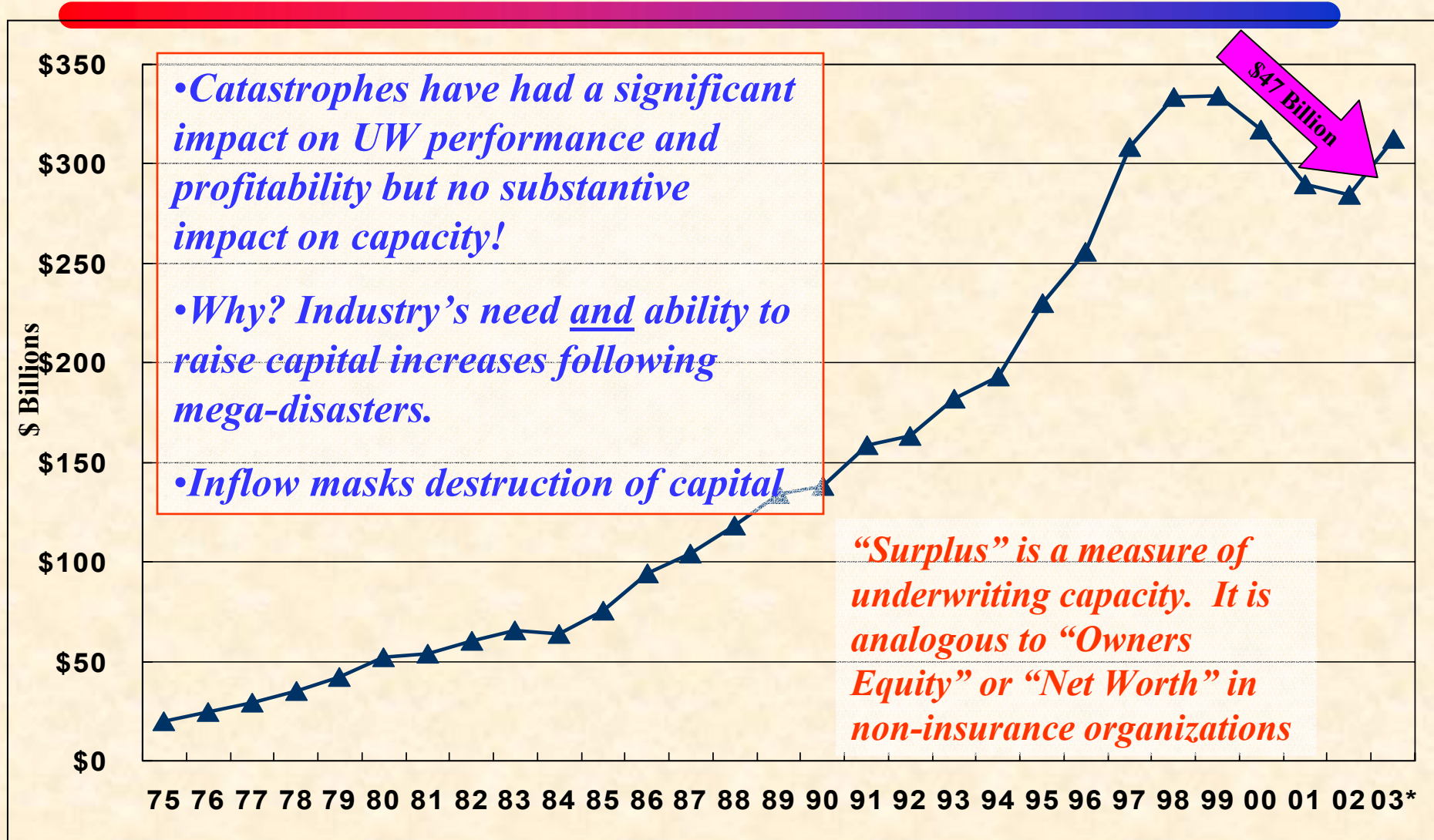


\*First half 2003 figures for full industry from ISO; 1<sup>st</sup> half reinsurance figures from RAA.

Source: A.M. Best, ISO, Reinsurance Association of America, Insurance Information Institute



# U.S. Policyholder Surplus: 1975-2003\*

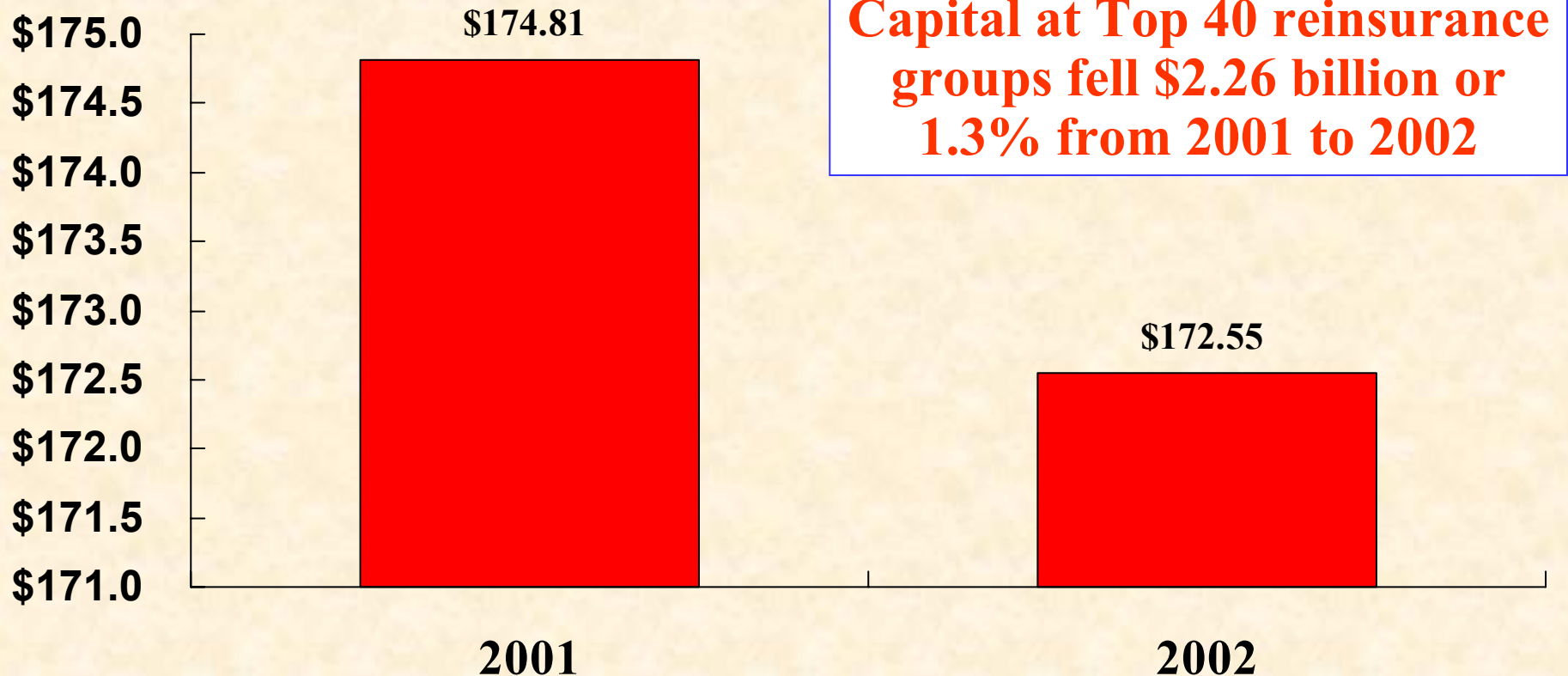






# Shareholders' Funds: Top 40 Reinsurance Groups\*

**\$ Billions**

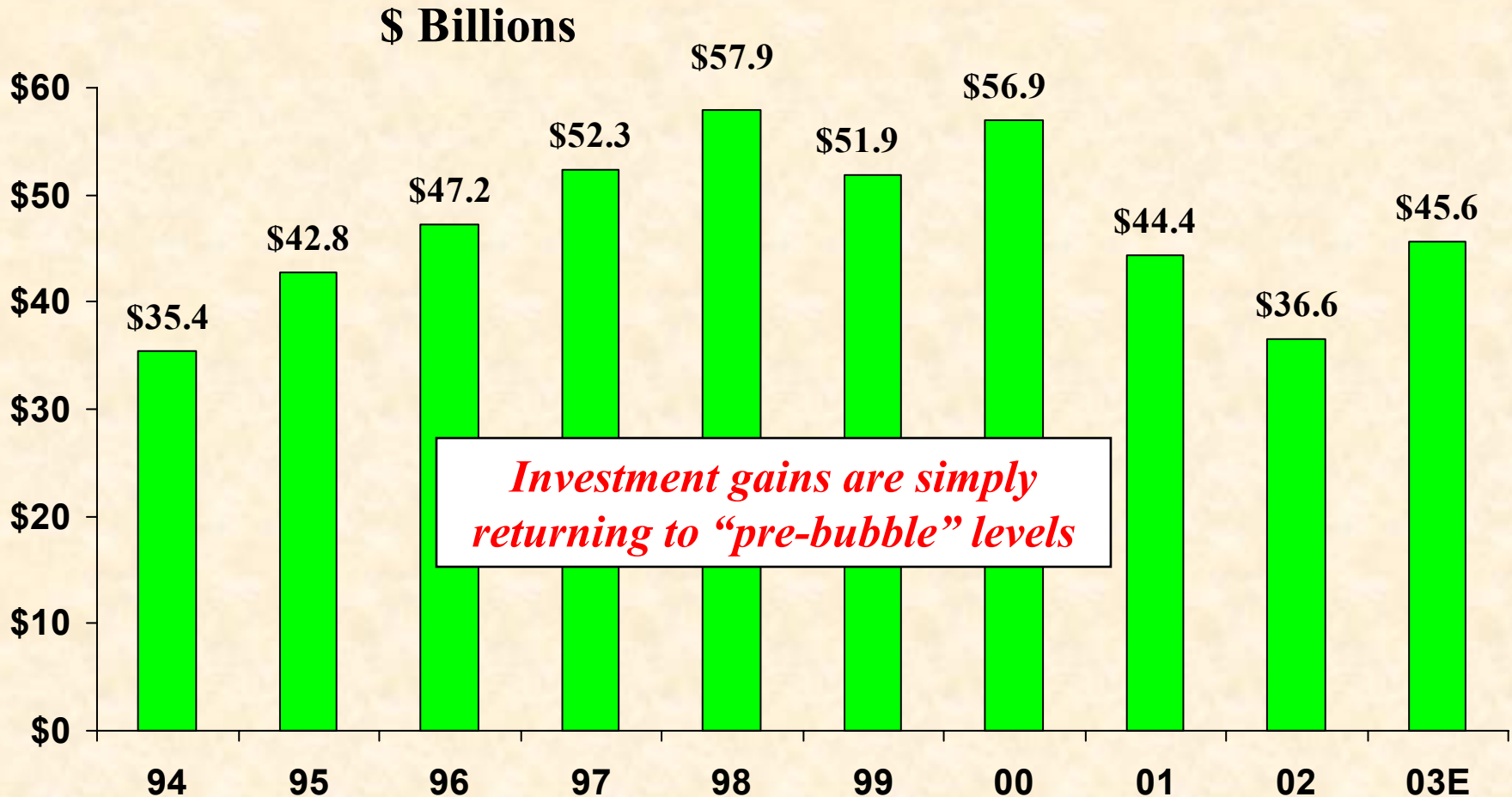


\*By net reinsurance premiums written.  
Source: *Global Reinsurance Highlights 2003*, Standard & Poor's





# Property/Casualty Insurance Industry Investment Gain\*

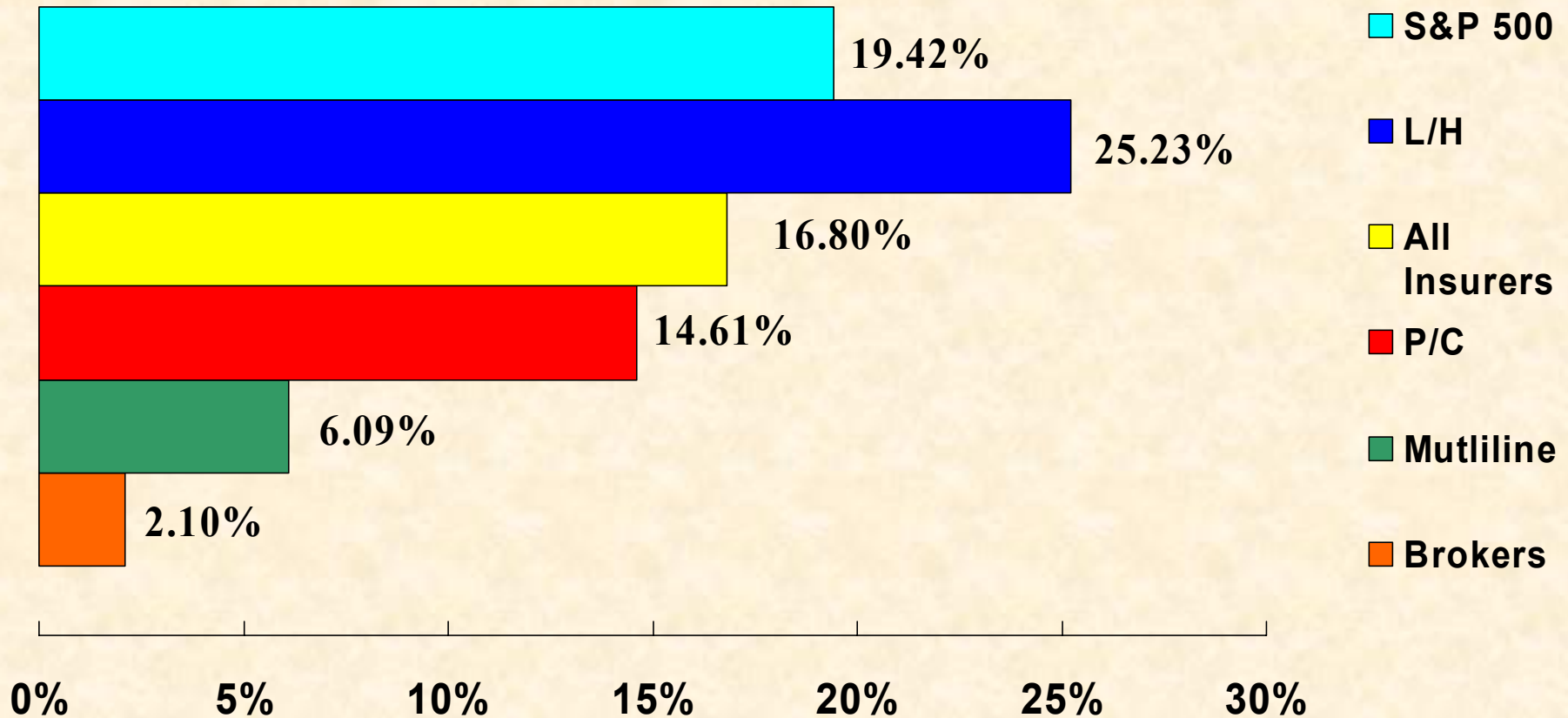


\*Investment gains consists primarily of interest, stock dividends and realized capital gains and losses.  
Source: Insurance Services Office; Insurance Information Institute estimate annualized as of 6/30/03.



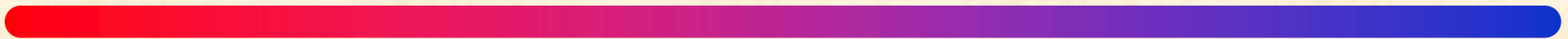
# *Insurer Stocks: Underperforming the S&P 500*

**Total Return 2003 YTD Through October 31, 2003**



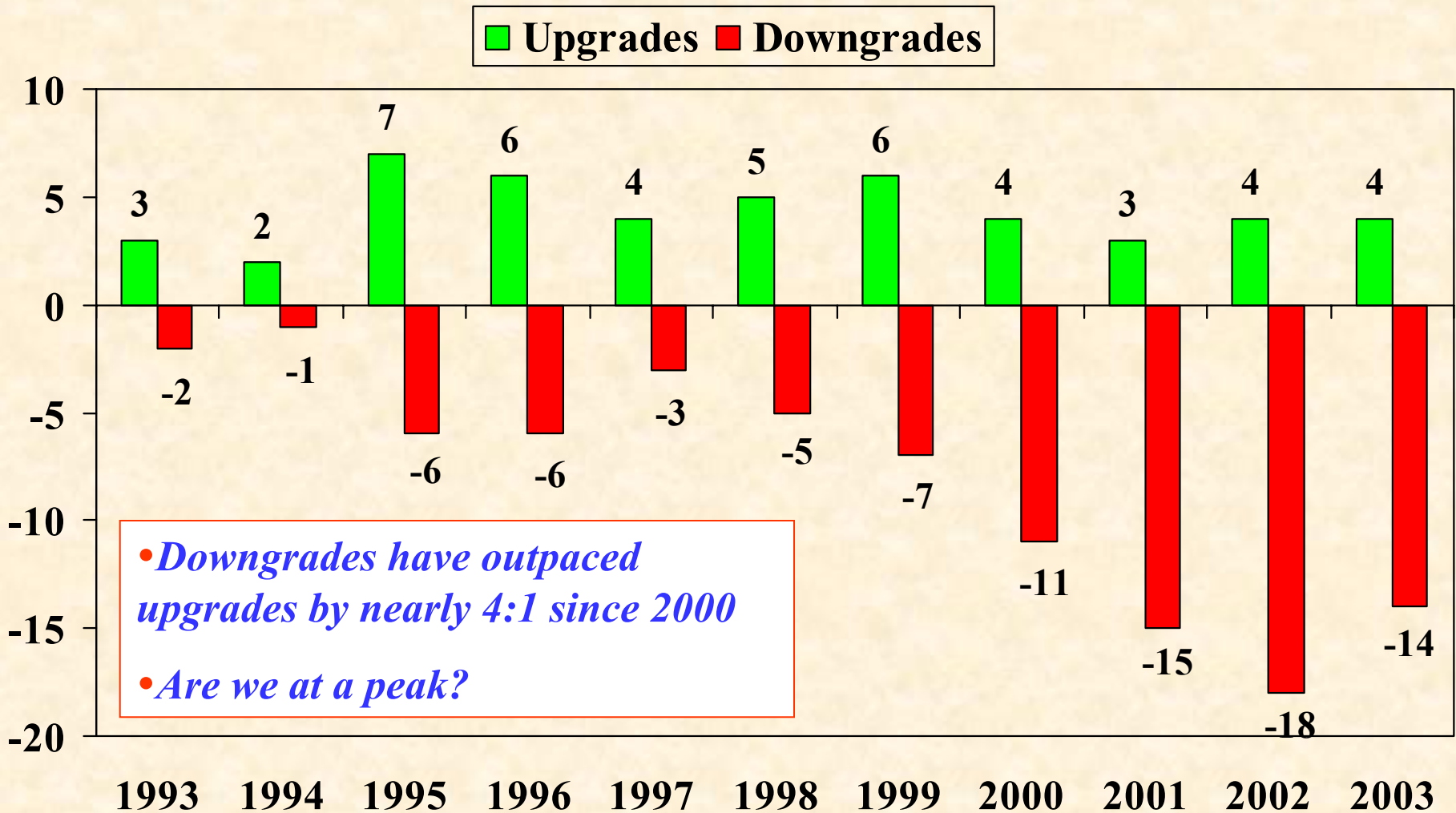
Source: SNL Securities, Insurance Information Institute

***RATINGS,  
SOLVENCY &  
REINSURANCE  
ISSUES***





# Number of Insurer Upgrades vs. Downgrades, 1993 to 2003\*

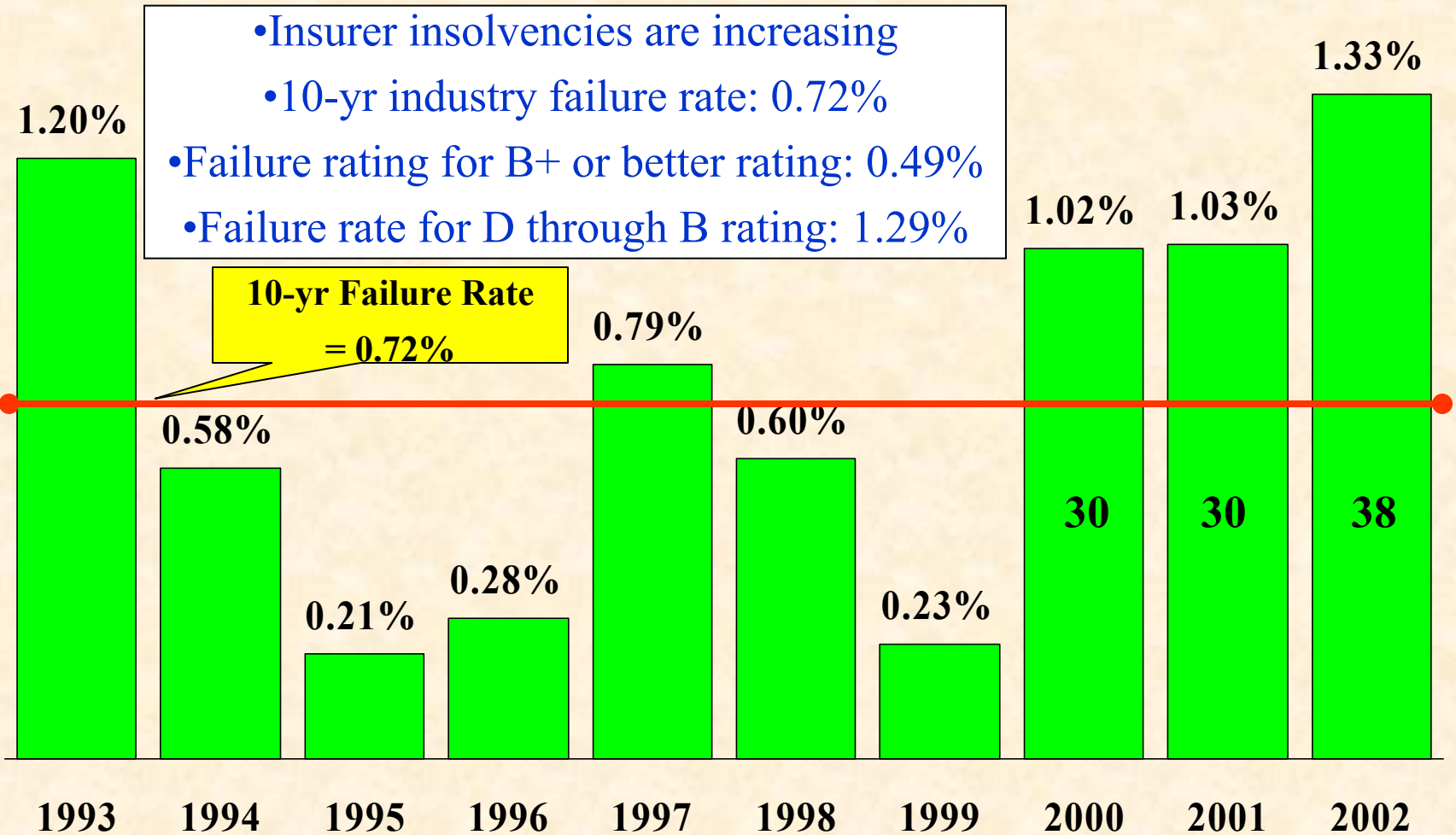


\*North American insurance holding companies through October 17, 2003

Source: Standard & Poor's



# *P/C Company Insolvency Rates, 1993 to 2002*

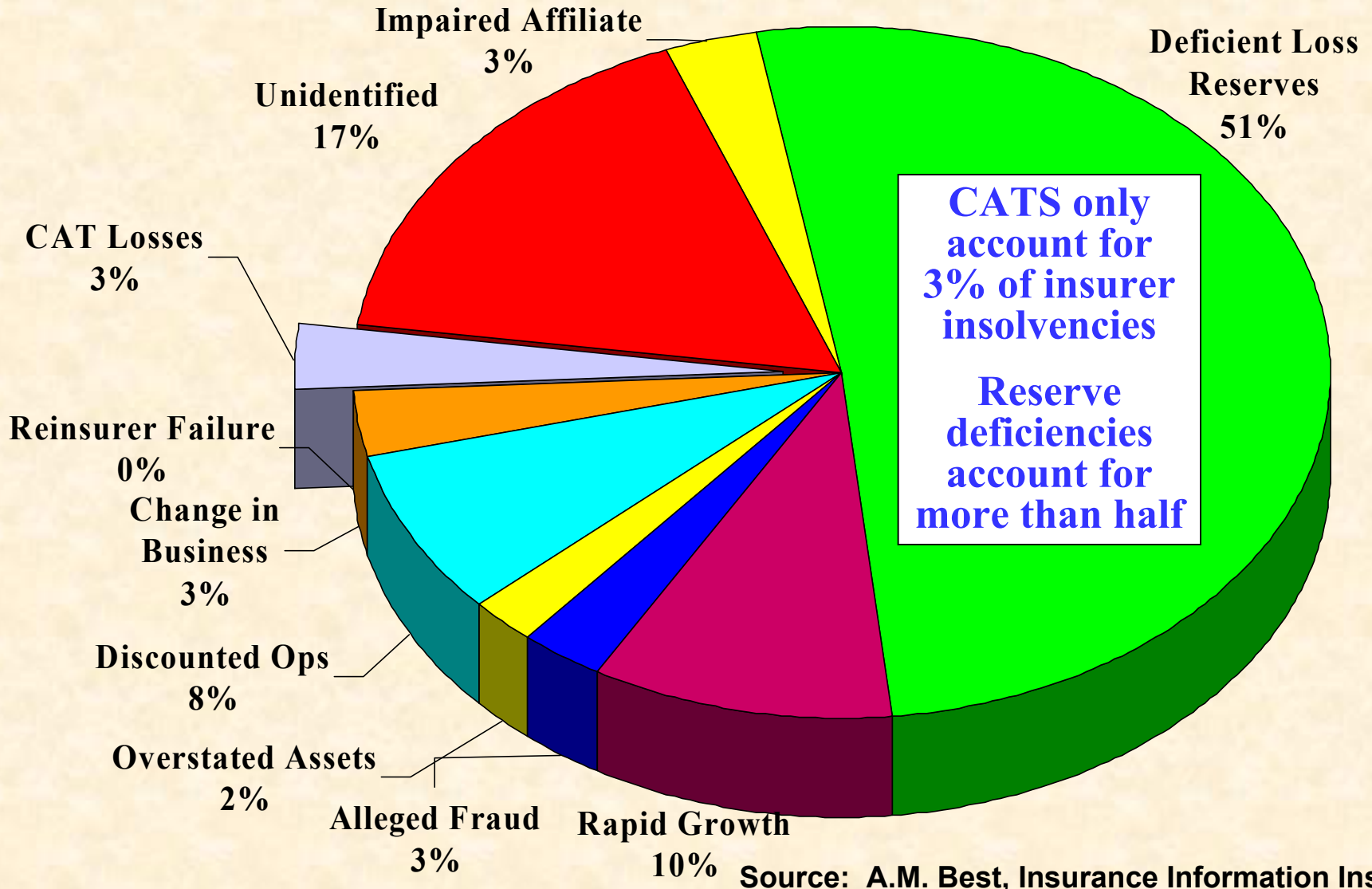






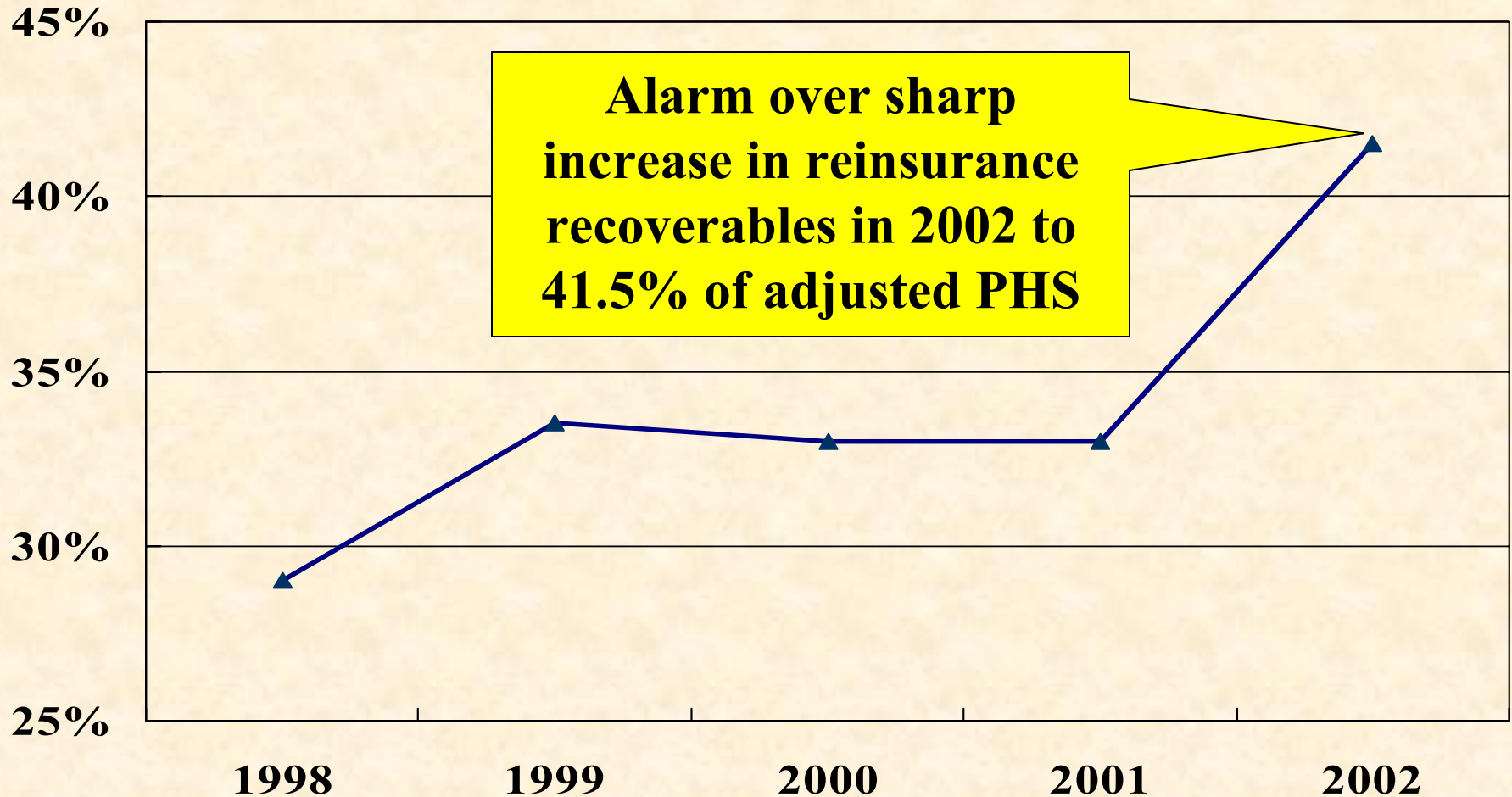
# *Reason for P/C Insolvencies*

*(218 Insolvencies, 1993-2002)*





# *US P/C Net Net Reinsurance Recoverables as % of Adjusted PHS*

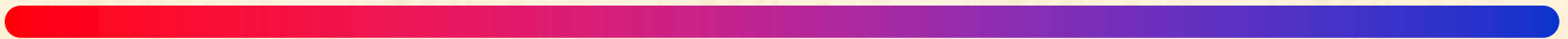


Source: Reinsurance Association of America from Thompson Financial OneSource database.

***HOMEOWNERS INSURANCE:***

***Recent Financial***

***Performance***

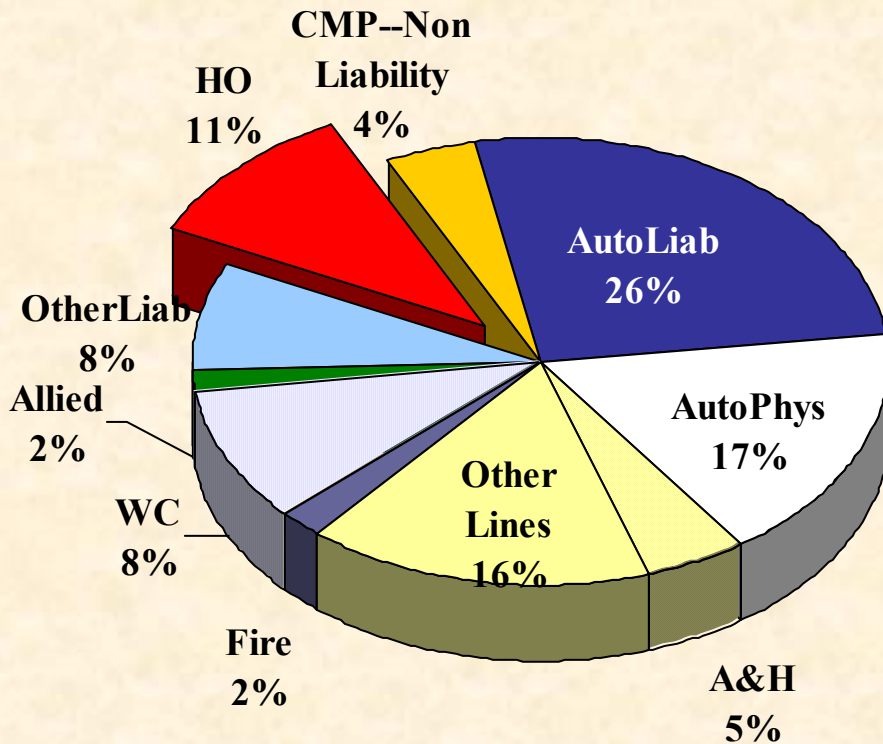




# Industry Net Premiums Written by Product Lines

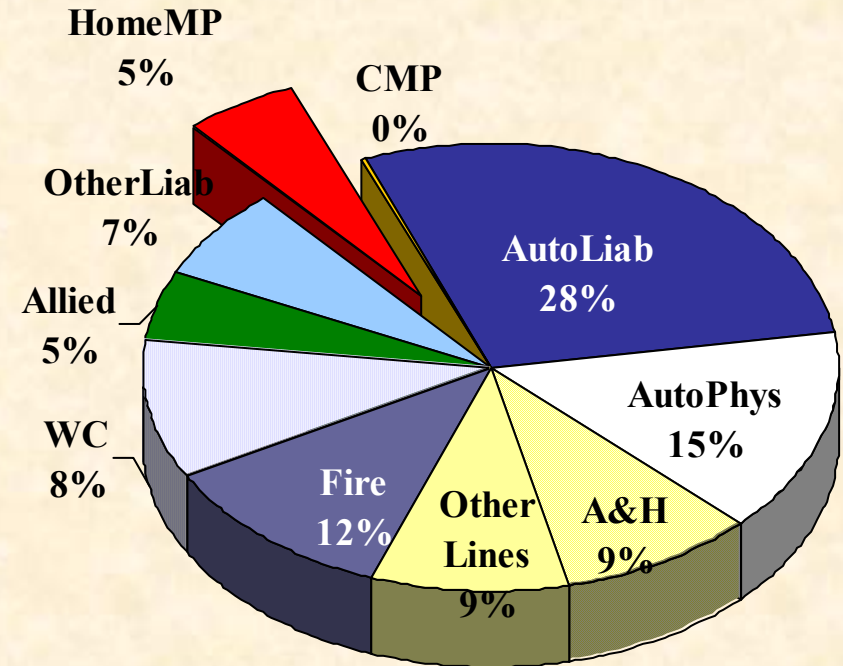
2002

NPW=\$377.2 Billion



1960

NPW=\$14.7 Billion

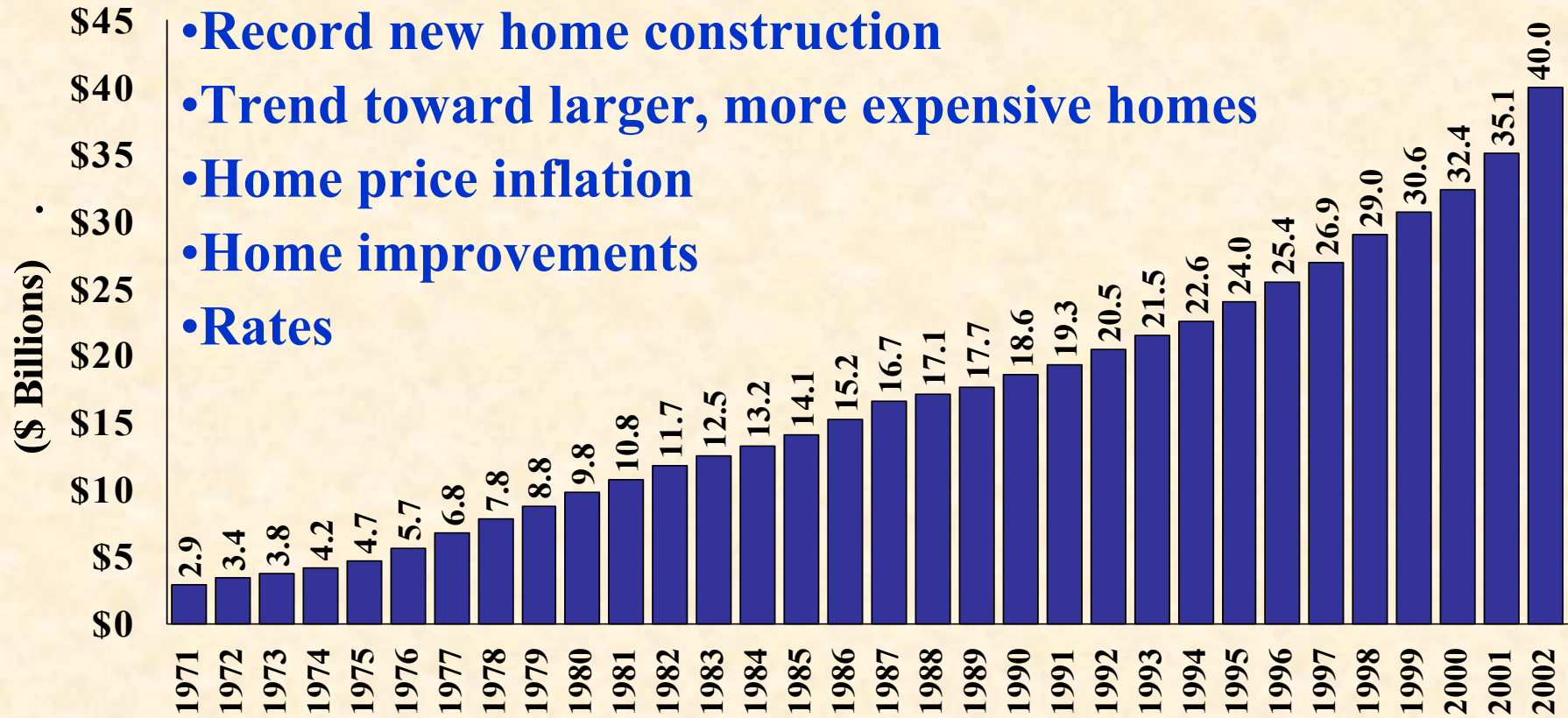




# Homeowners Multi-Peril Insurance Net Premiums Written

## Revenue Growth Drivers:

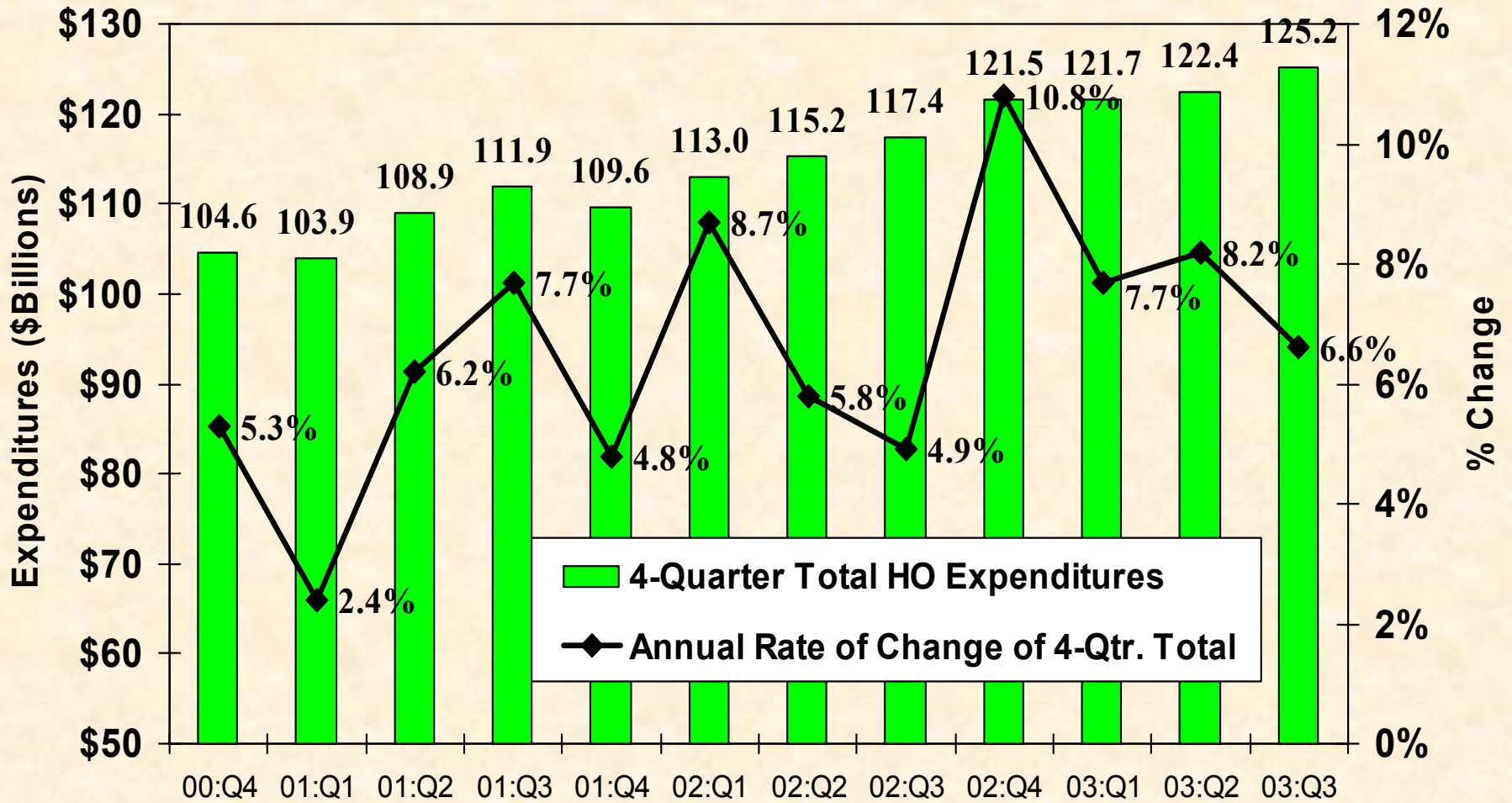
- Record new home construction
- Trend toward larger, more expensive homes
- Home price inflation
- Home improvements
- Rates







# Home Remodeling Expenditures are at a Record High

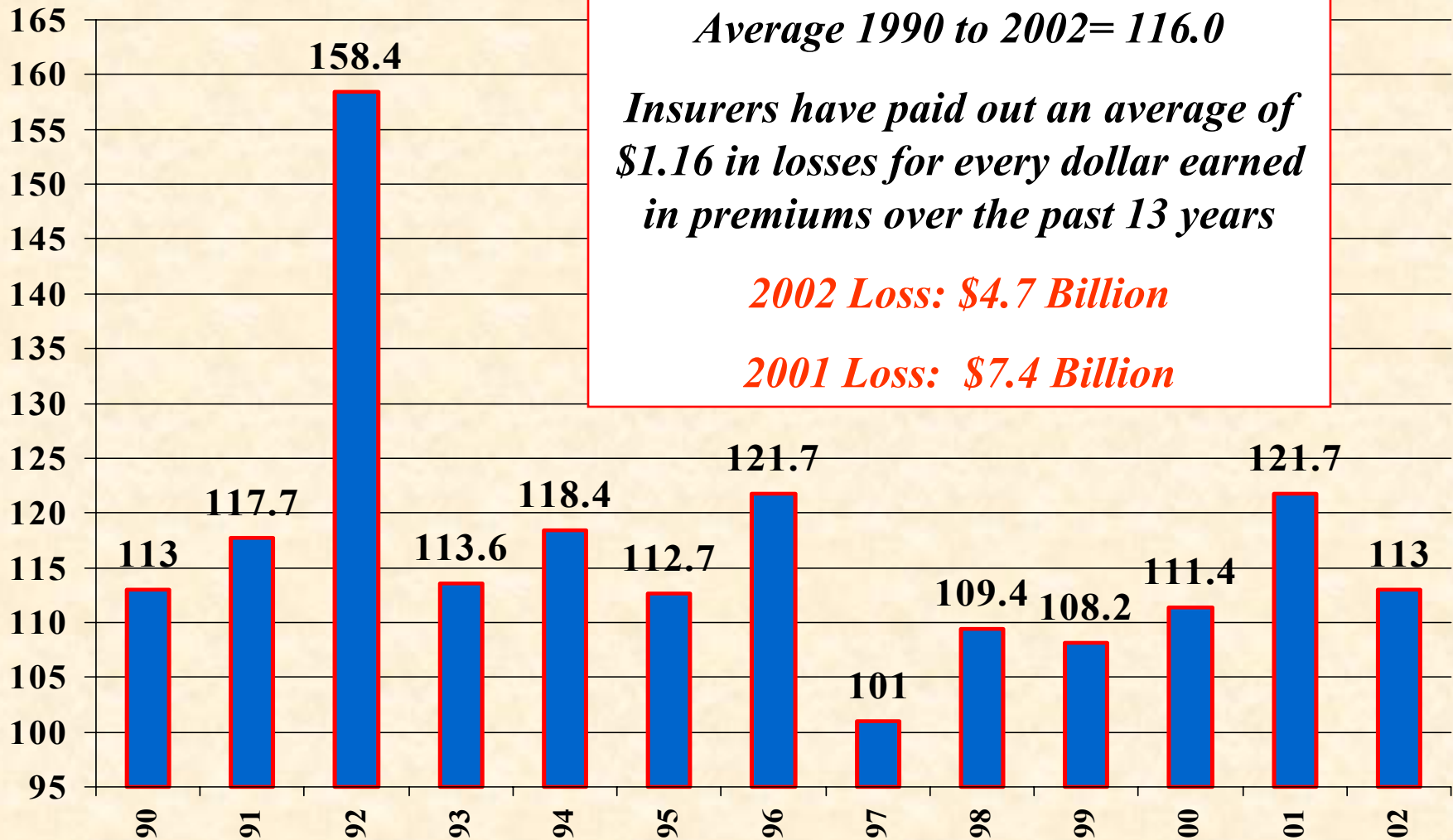


\* Figures are annualized based on most recent quarter's data..

Source: Joint Center for Housing Studies; Insurance Information Institute

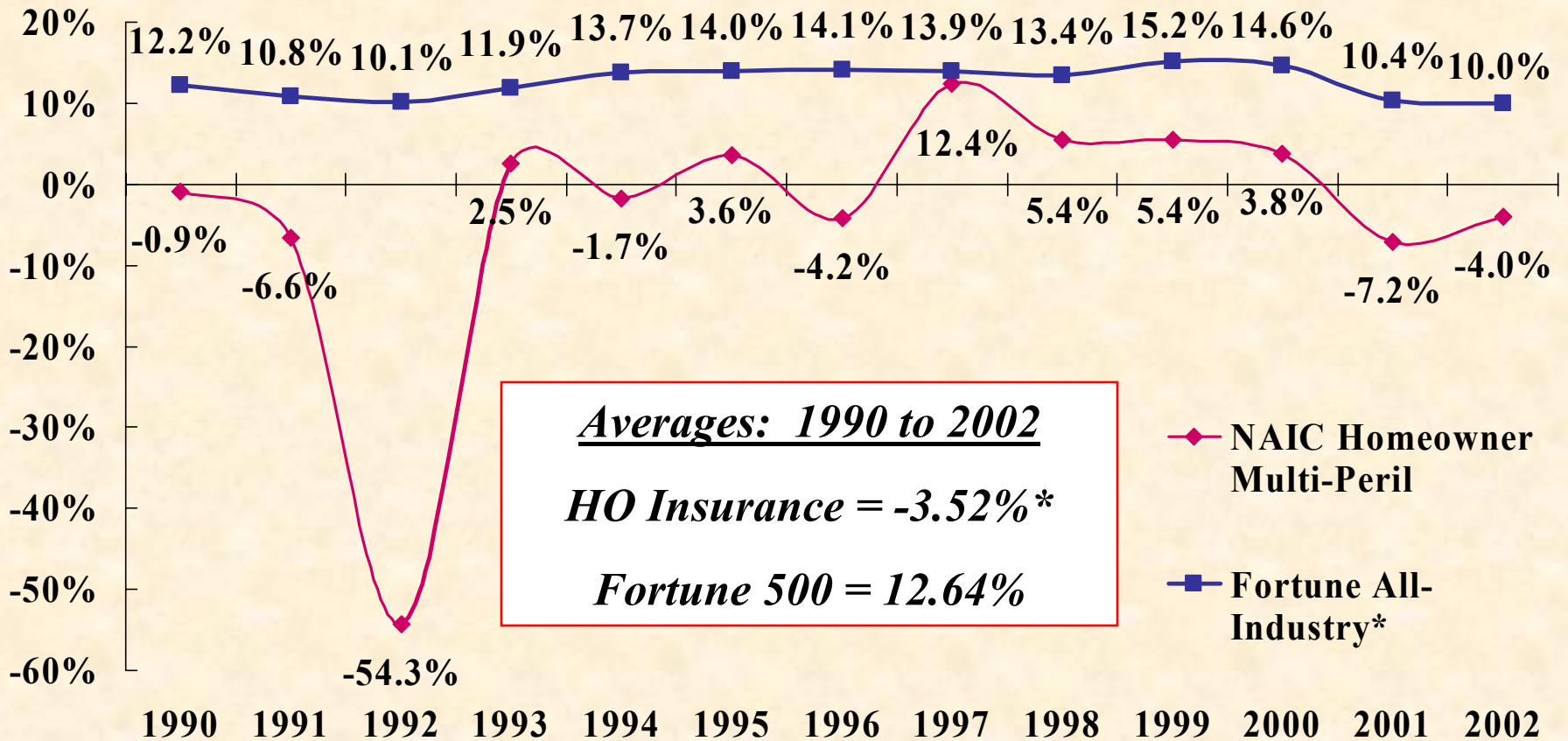


# Homeowners Insurance Combined Ratio





# Rates of Return on Net Worth



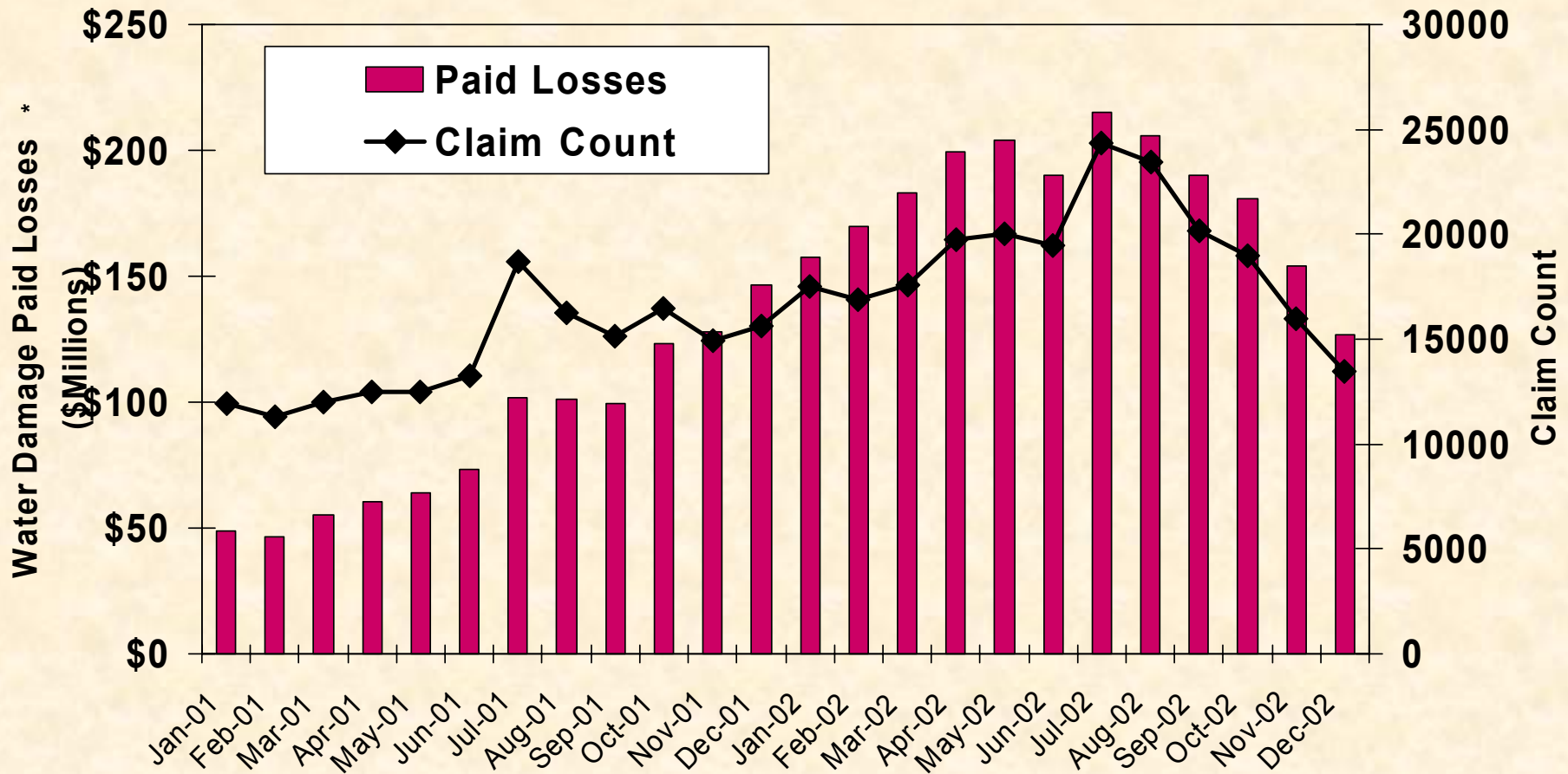
Source: NAIC, Insurance Information Institute

\* Average is 0.71% if excluding 1992 (year of Hurricanes Andrew and Iniki).

Note: 2002 Homeowners figure is III estimate.



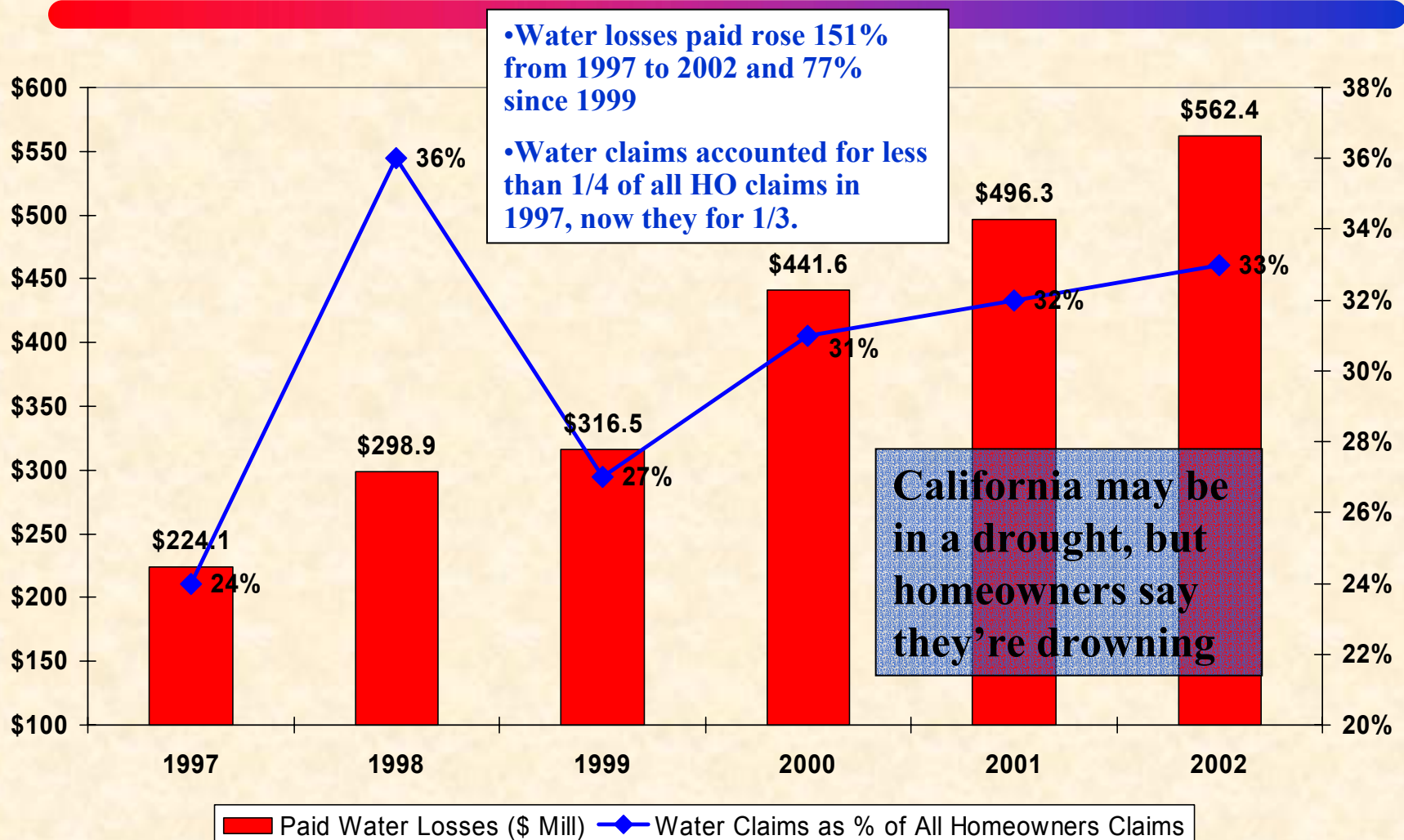
# Texas: Mold Losses/Claims Are Finally Moderating\*



\* Data are for TDI Cause 61: Discharge – Other Damage. Not all claims in cause 61 are mold and mold claims may also arise from other (non-water) causes of loss.



# California: Surging Water Claim Frequency and Costs: Symptom of Growing Mold Problem





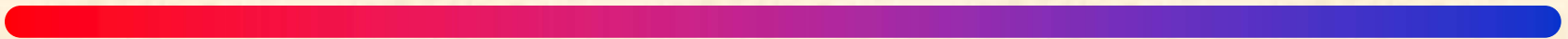


# *Where are the Next Battlefields for Mold?*

- Homeowners issue probably crested in 2002
- Migration to commercial area affects many lines:
  - Commercial Property      Commercial Liability
  - Products Liability      Builders Risk/Construction Defects
  - Workers Comp...
- Hot Spots:
  - Apartments/Condos/Co-ops      Office Structures (e.g., IBM)
  - Schools      Municipal Buildings
  - Cars? (GM case in NC)
- Trend toward class actions since science doesn't support massive individual non-economic damages
  - Much more lucrative for trial lawyers to form class

***COMMERCIAL PROPERTY  
INSURANCE:***

***Recent Financial  
Performance***

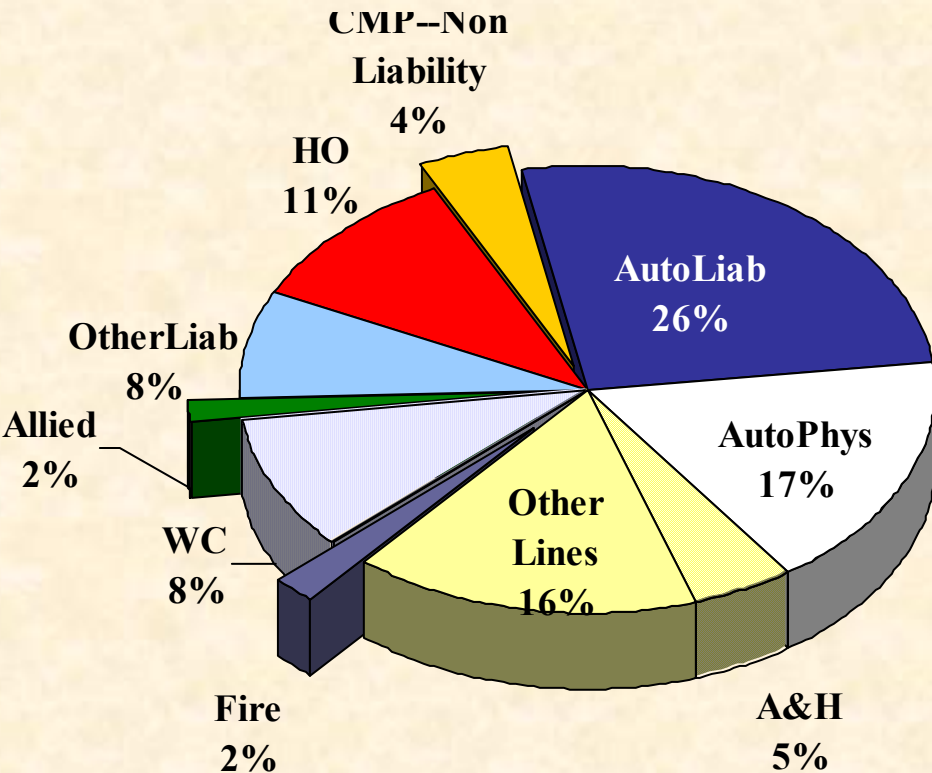




# Industry Net Premiums Written by Product Lines

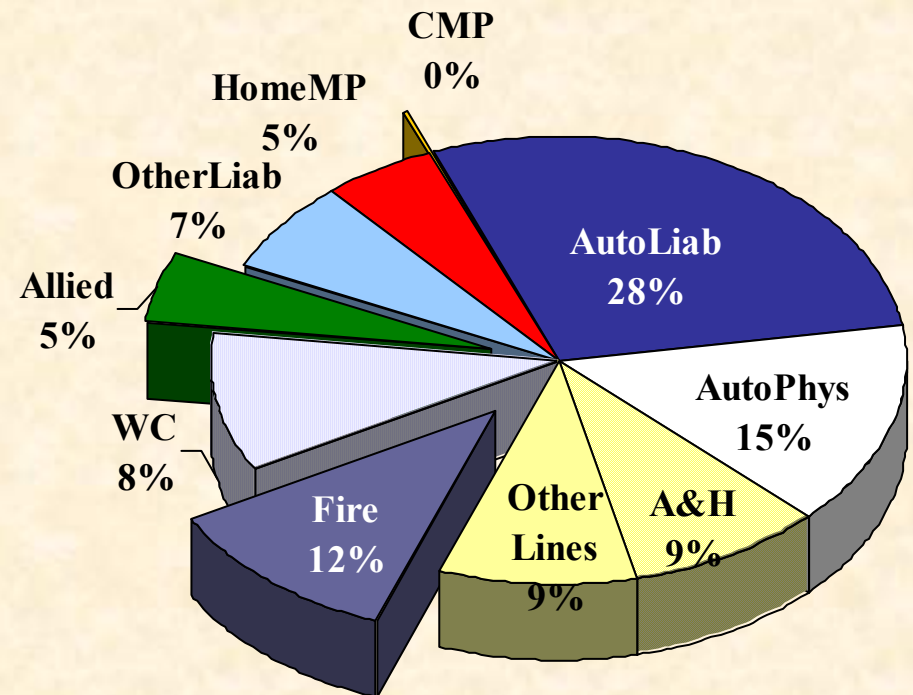
2002

NPW=\$377.2 Billion



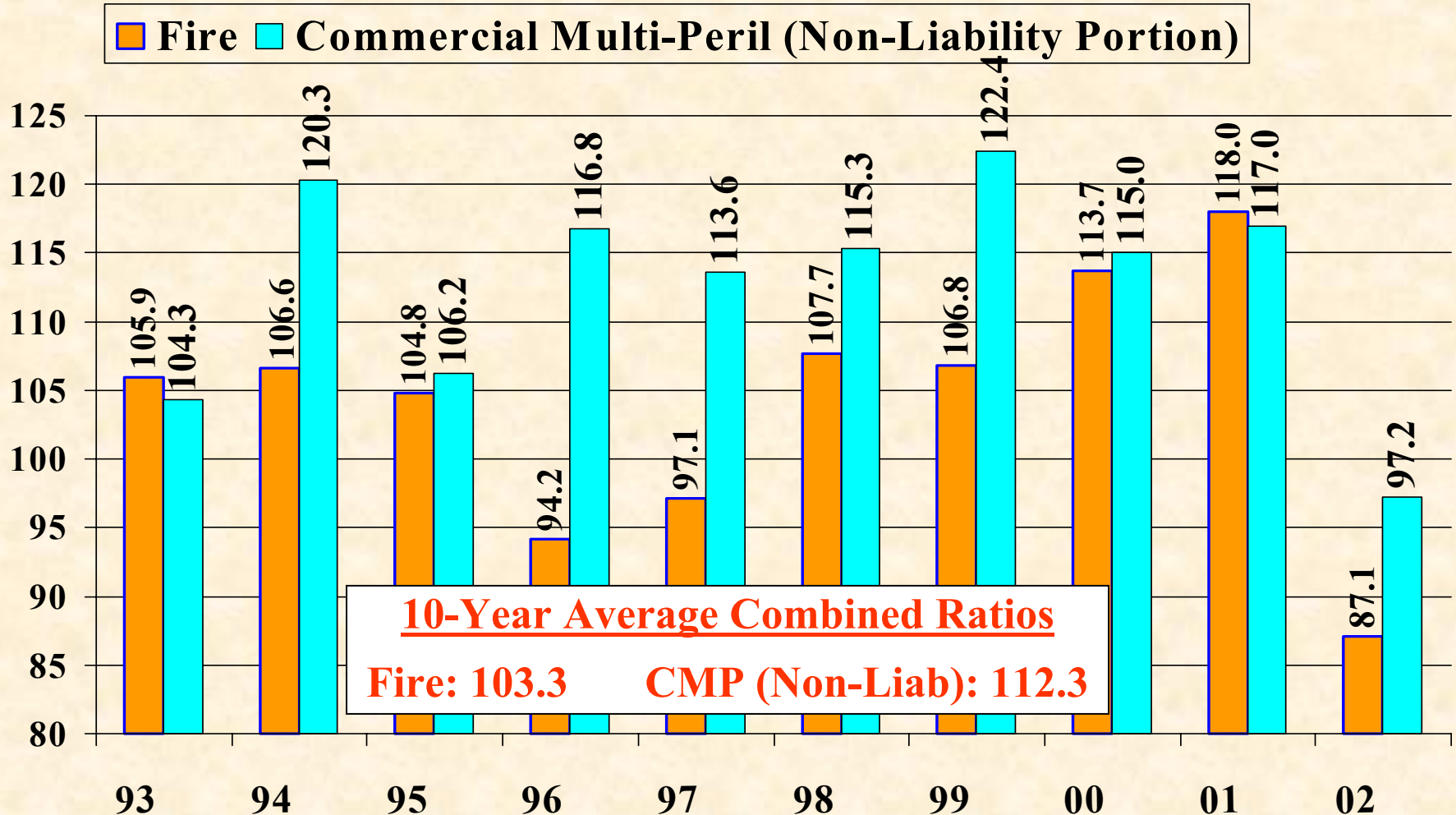
1960

NPW=\$14.7 Billion





# Fire & CMP (Non-Liability Portion) Combined Ratios





# *Construction Defect Problem*

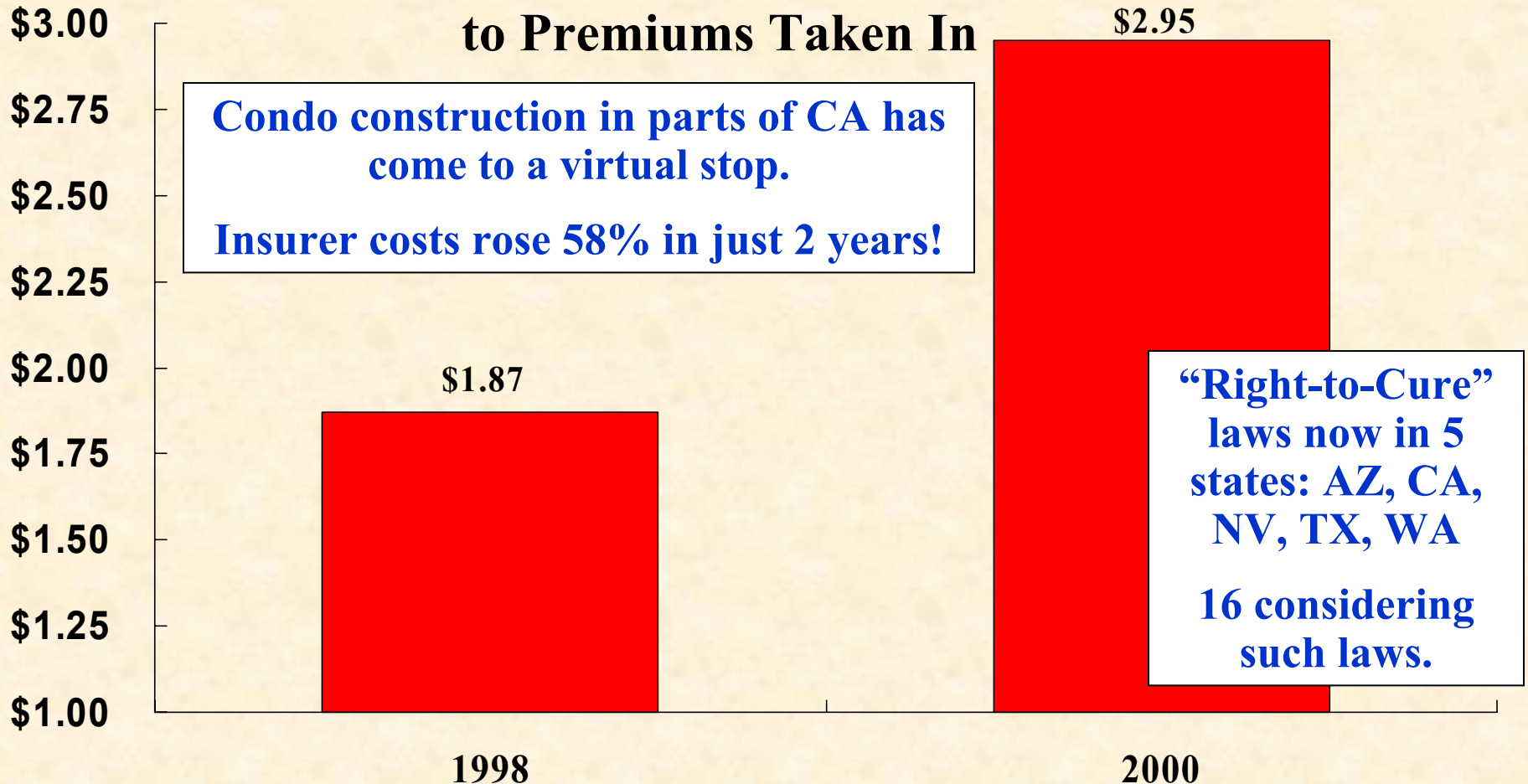
- **Growing number of lawsuits target:**
  - **Builders, Contractors, Developers, Sub-Contractors, Material Suppliers, Product Manufacturers, Architects & Engineers.**
- **Construction defect claims include:**
  - **Subsidence, collapse, cracks in walls & foundations.**
  - **Leaking roofs, windows, doors, foundations.**
  - **Dry rot of wood or other building materials, pest infestations.**
  - **Mold, code violations, improper specification of building materials.**
- **Hotspots:**
  - **California, Nevada, Colorado, Texas, the Carolinas, Florida, New York.**





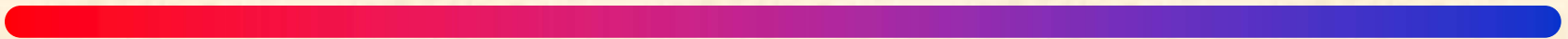
# *Construction Defect Litigation Destroying CA Condo Market*

## **Ratio of Losses Paid Out to Premiums Taken In**



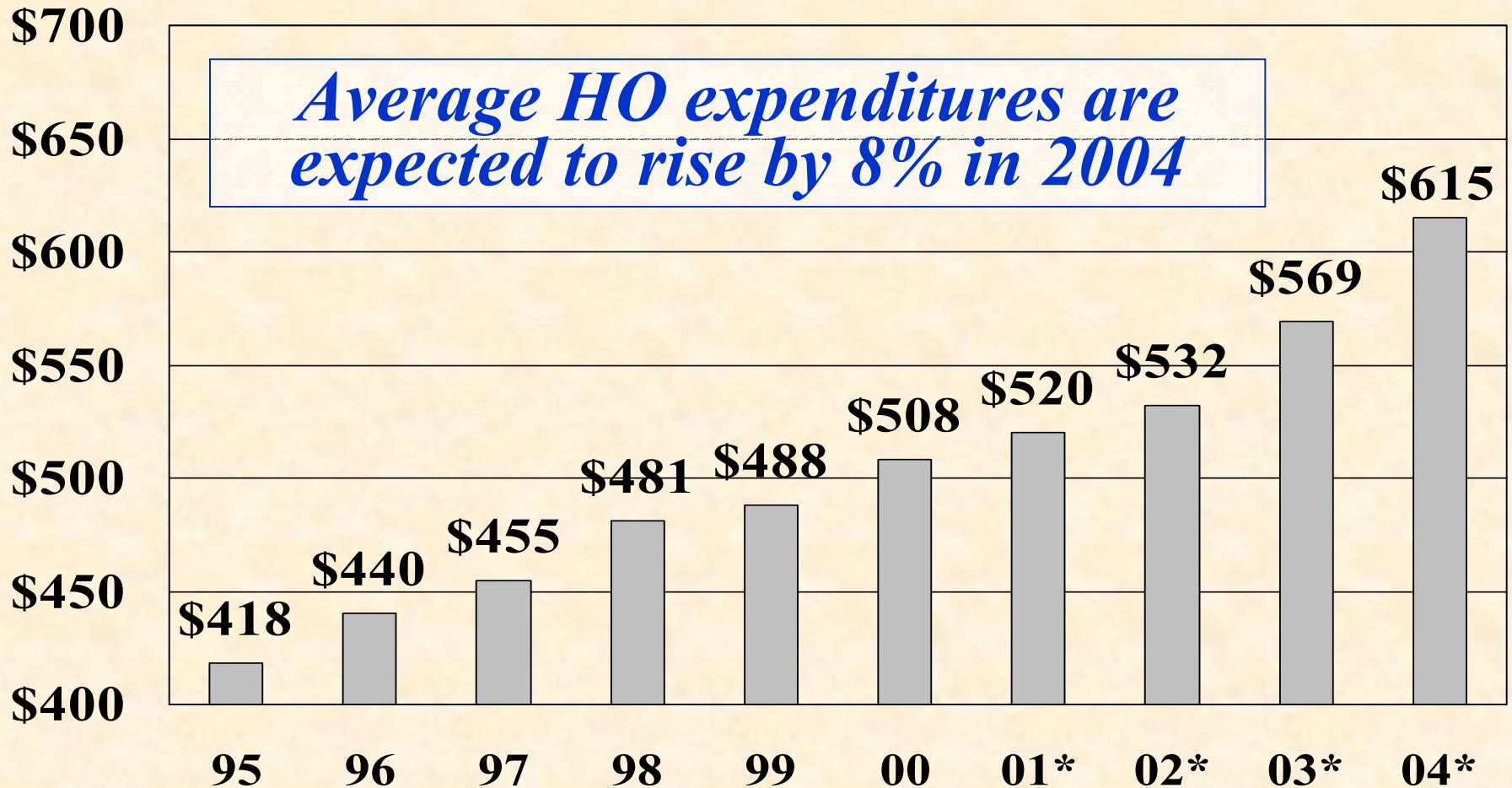
# *PRICING:*

*Are Risk & Price Better  
Matched?*





# Average Expenditures on Homeowners Insurance



\*Insurance Information Institute Estimates/Forecasts

Source: NAIC, Insurance Information Institute

# *Reasons for Rising HO*

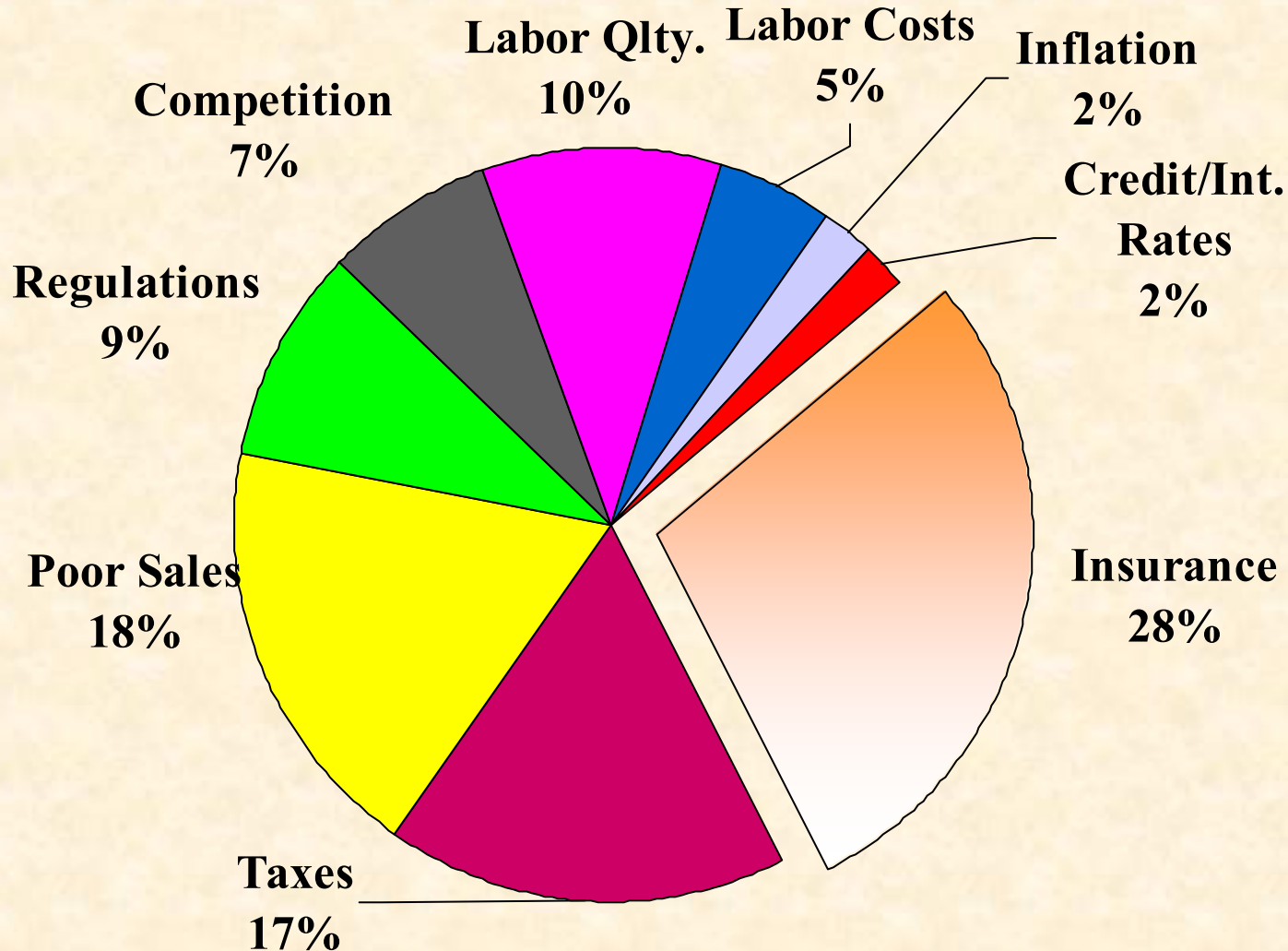


## *Insurance Prices*

- Enormous underwriting losses are the primary reason for rising homeowners insurance rates today
  - Function of frequency/severity of claims and events
- Home price/repair inflation
- Constant threats:
  - CAT losses (>\$100B since 1990); Not just hurricanes/earthquakes, but also major hail/wind events
- New issues such as “toxic” mold cost billions; no prior premium collected
- Litigation is a problem (property & liability related)
- Falling capacity; Rising reinsurance costs
- Attempts to weaken insurers ability to underwrite
  - Credit restrictions raise costs for millions (WA, MD & others)
  - CA “emergency” reg. preventing insurers from using claims history in coverage decisions (Safeco moratorium on new HO policies)



# *Insurance is the Biggest Concern of Small Business Owners*

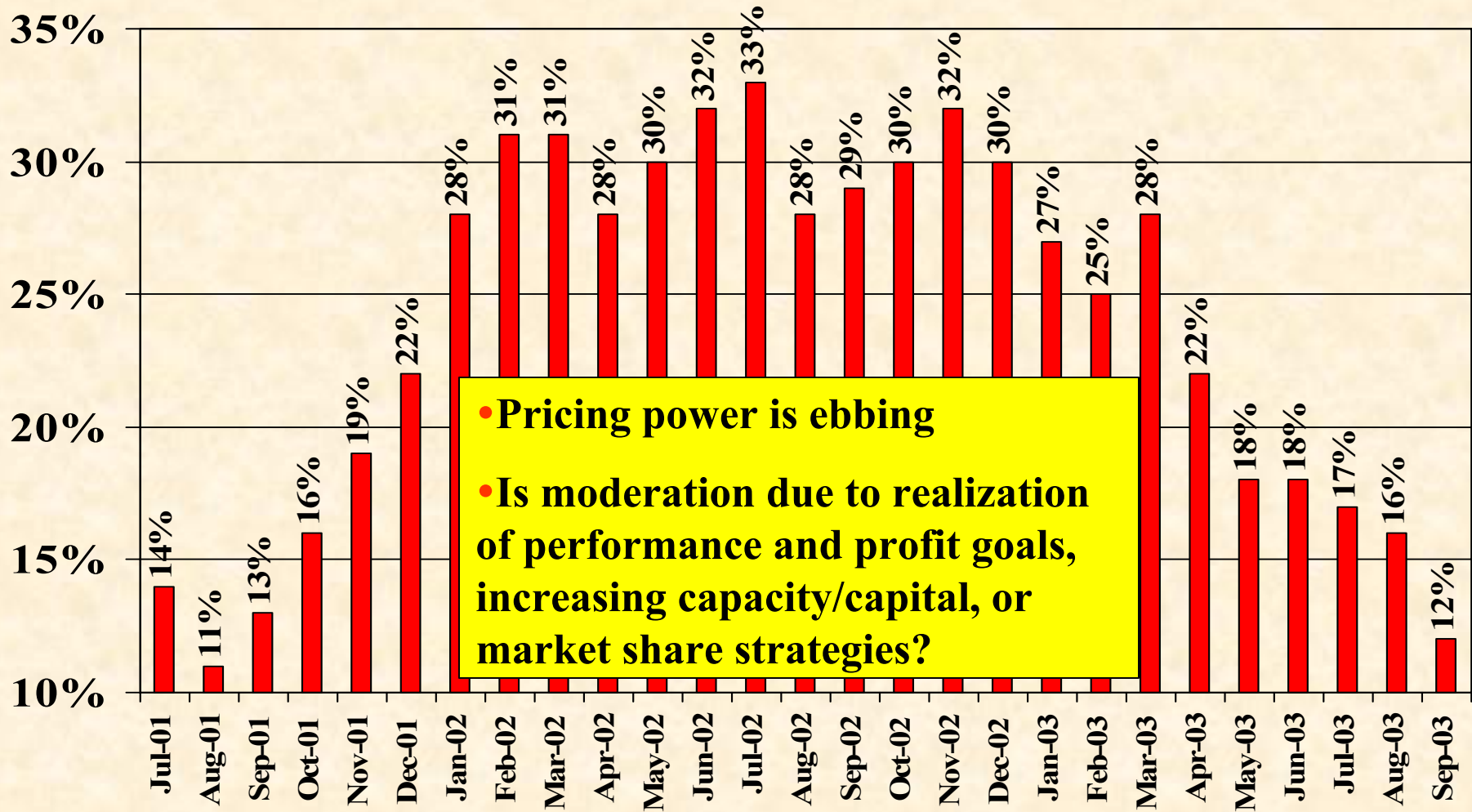






# PRICING

## Commercial Premium Rate Changes Highly Cyclical





# *Council of Insurance Agents & Brokers Rate Survey*

## Third Quarter 2003

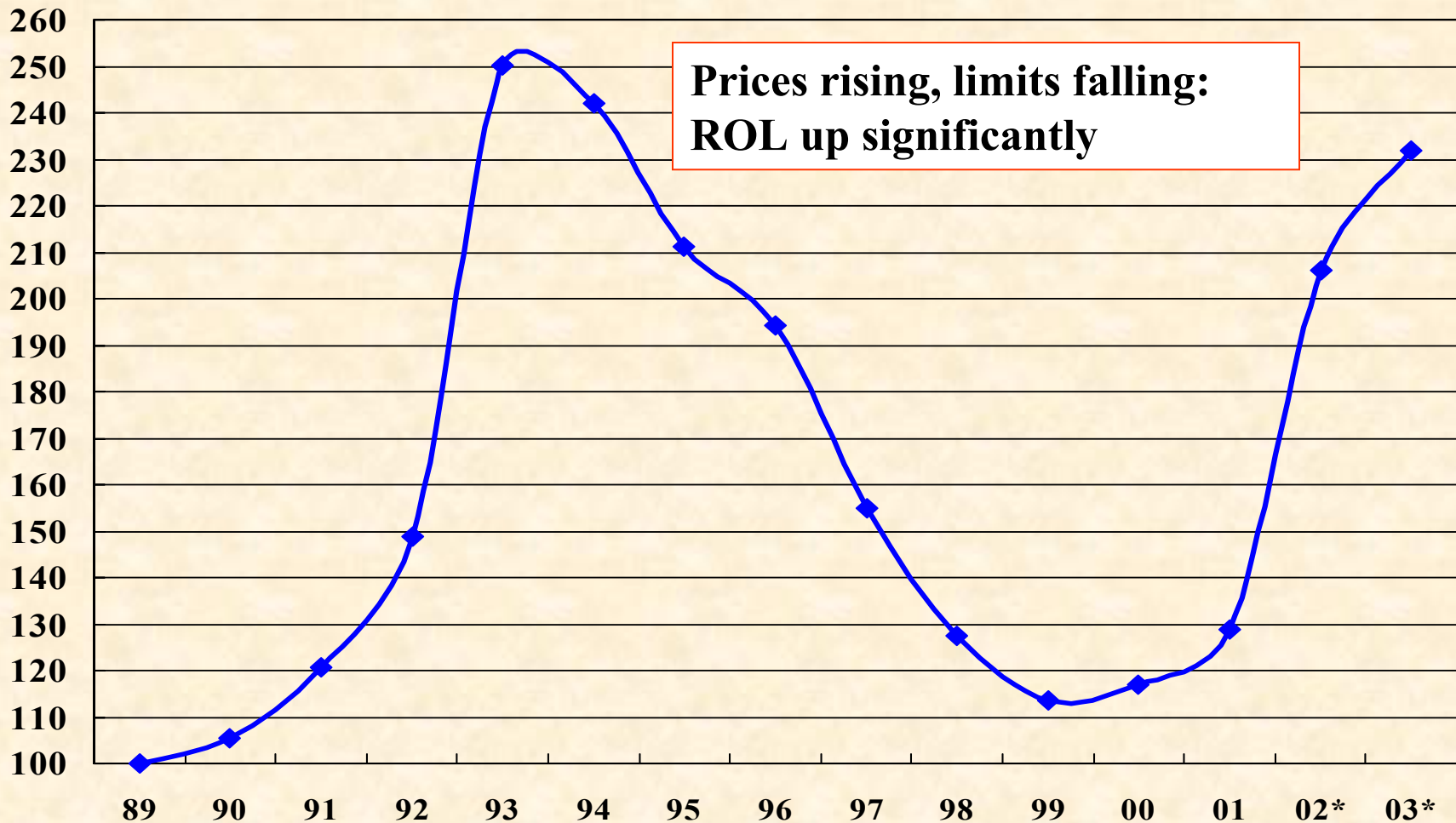
### Premium Rate Changes By Line of Business

	Down 1-10%	No Change	Up 1-10%	10-20%	20-30%	30-50%	50%-100%
Comm. Auto	12%	14%	42%	30%	0%	0%	0%
Workers Comp	10%	17%	31%	21%	8%	2%	2%
General Liability	9%	21%	39%	24%	4%	1%	1%
Comm. Umbrella	6%	17%	27%	33%	11%	4%	0%
D&O	0%	10%	22%	34%	16%	7%	2%
Comm. Property*	24%	26%	28%	9%	2%	1%	0%
Construction Risk	3%	16%	26%	23%	13%	2%	2%
Terrorism*	6%	48%	15%	5%	1%	1%	0%
Business Interr.	11%	33%	34%	8%	2%	0%	0%
Surety Bonds	28%	18%	9%	9%	4%	2%	0%
Med Mal	0%	2%	7%	9%	19%	10%	2%

Source: Council of Insurance Agents & Brokers.



# Rate On Line Index (1989=100)

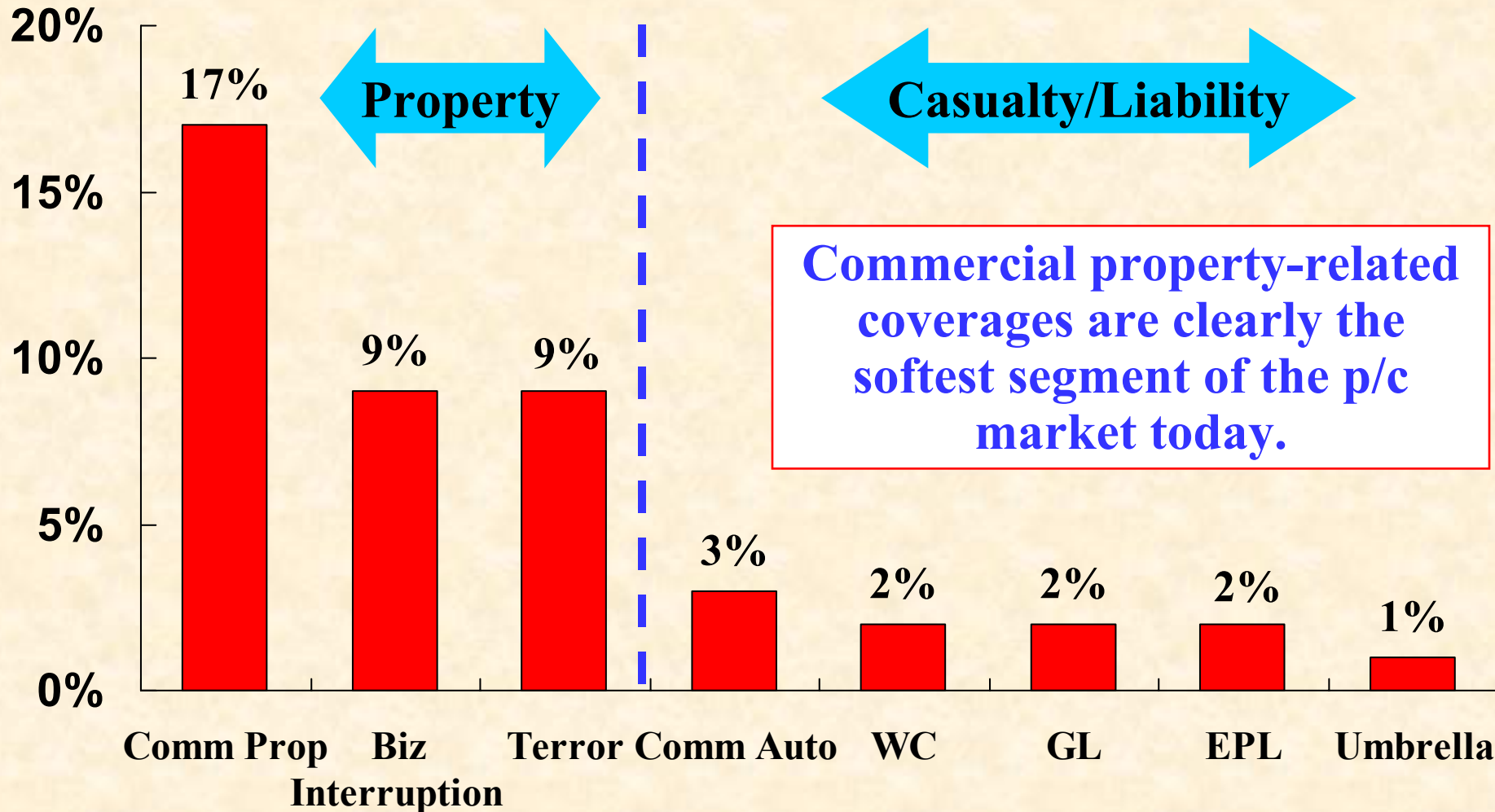


Source: Guy Carpenter

\* III Estimate

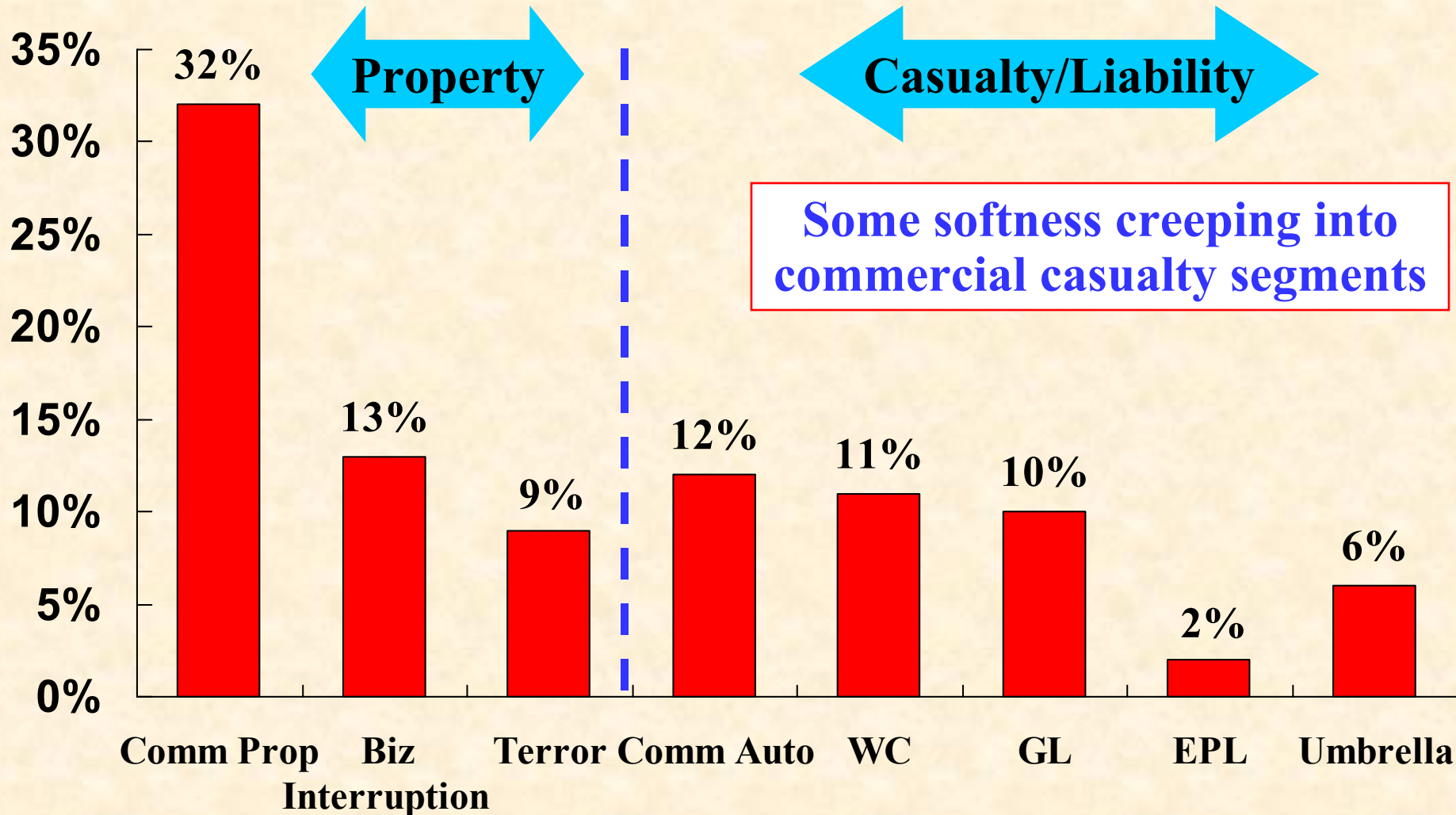


# *P/C Soft Spots: % Accounts With Negative Price Change (2<sup>nd</sup> Qtr 2003)*





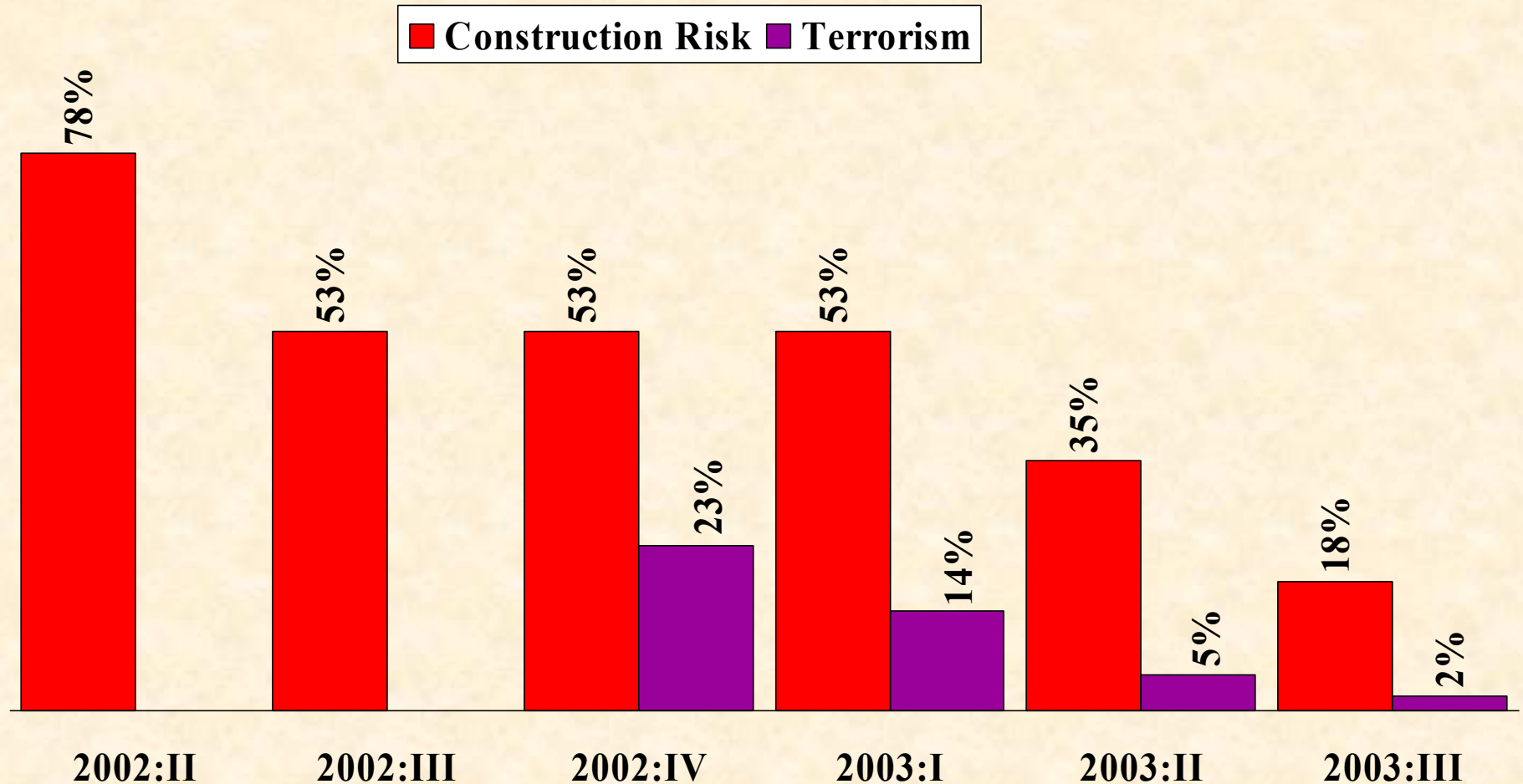
# *P/C Soft Spots: % Accounts With Negative Price Change (3rd Qtr 2003)*



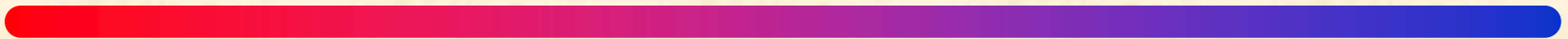




# *Proportion of Accounts Renewing With Increase of 20% or More, (Select Lines)*

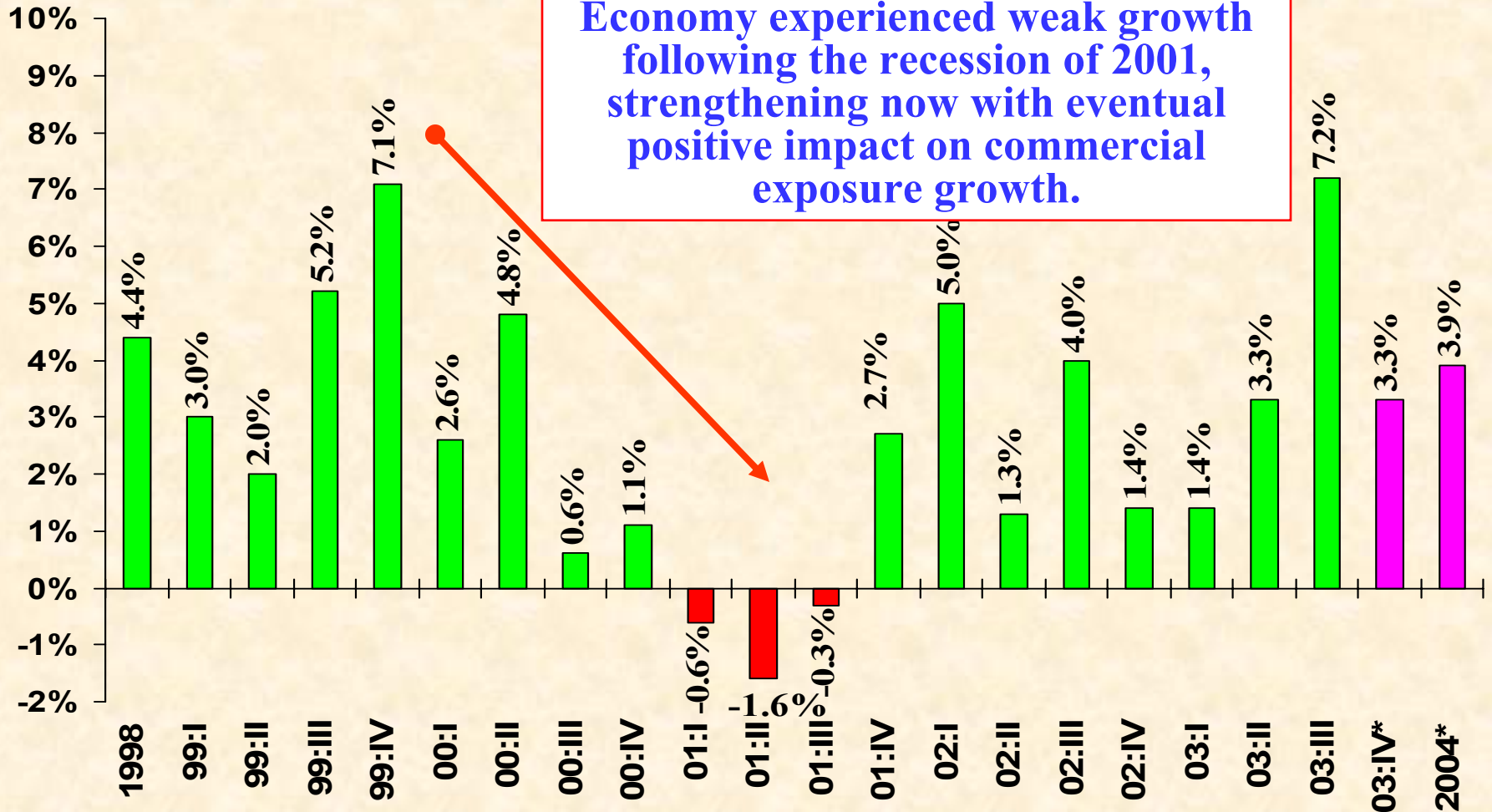


***PROPERTY INSURANCE  
EXPOSURE &  
THE ECONOMY***





# Real GDP Growth

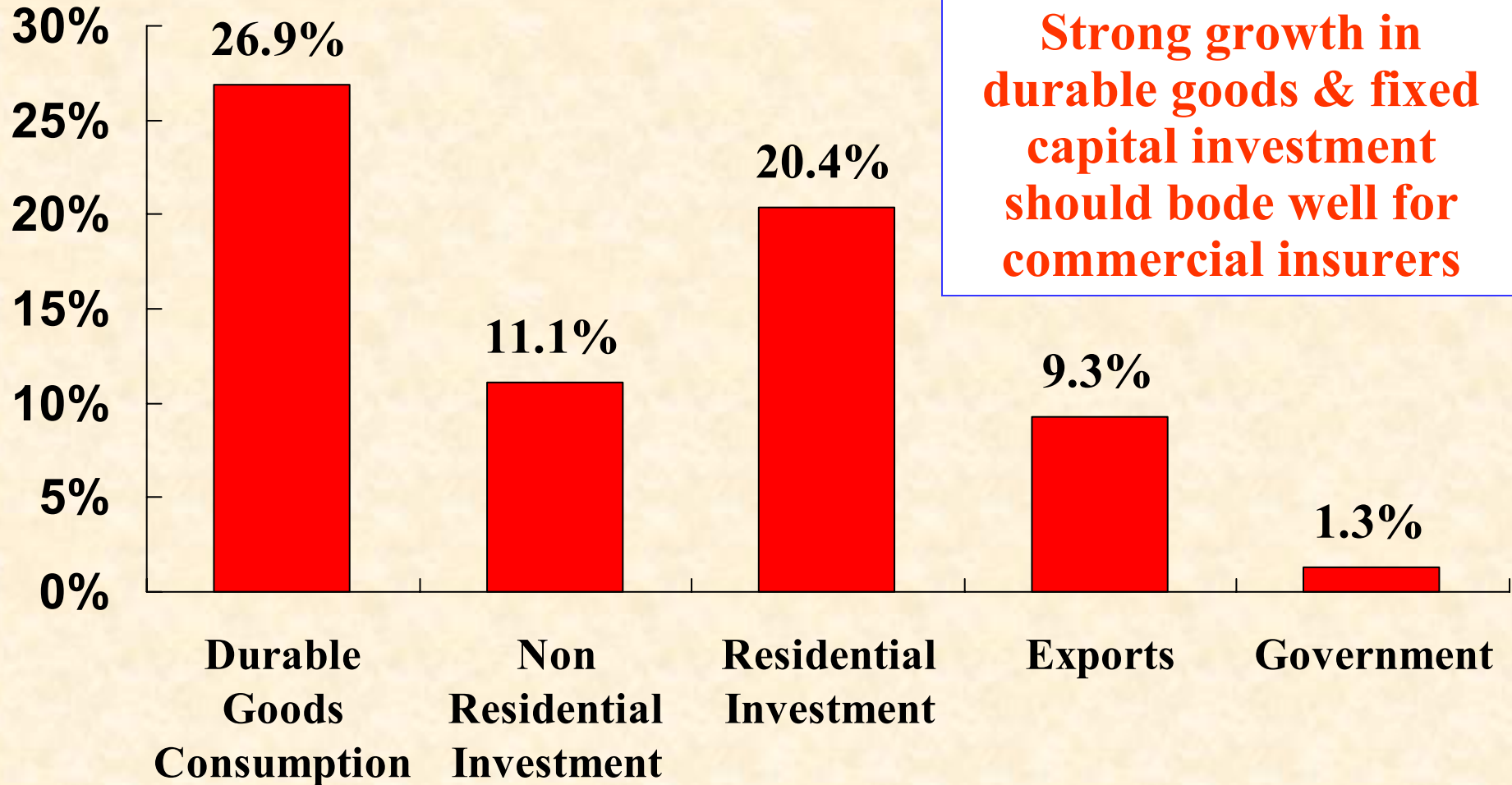


\*Estimate/Forecast

Source: US Department of Commerce, Blue Economic Indicators 10/03; Insurance Information Institute.

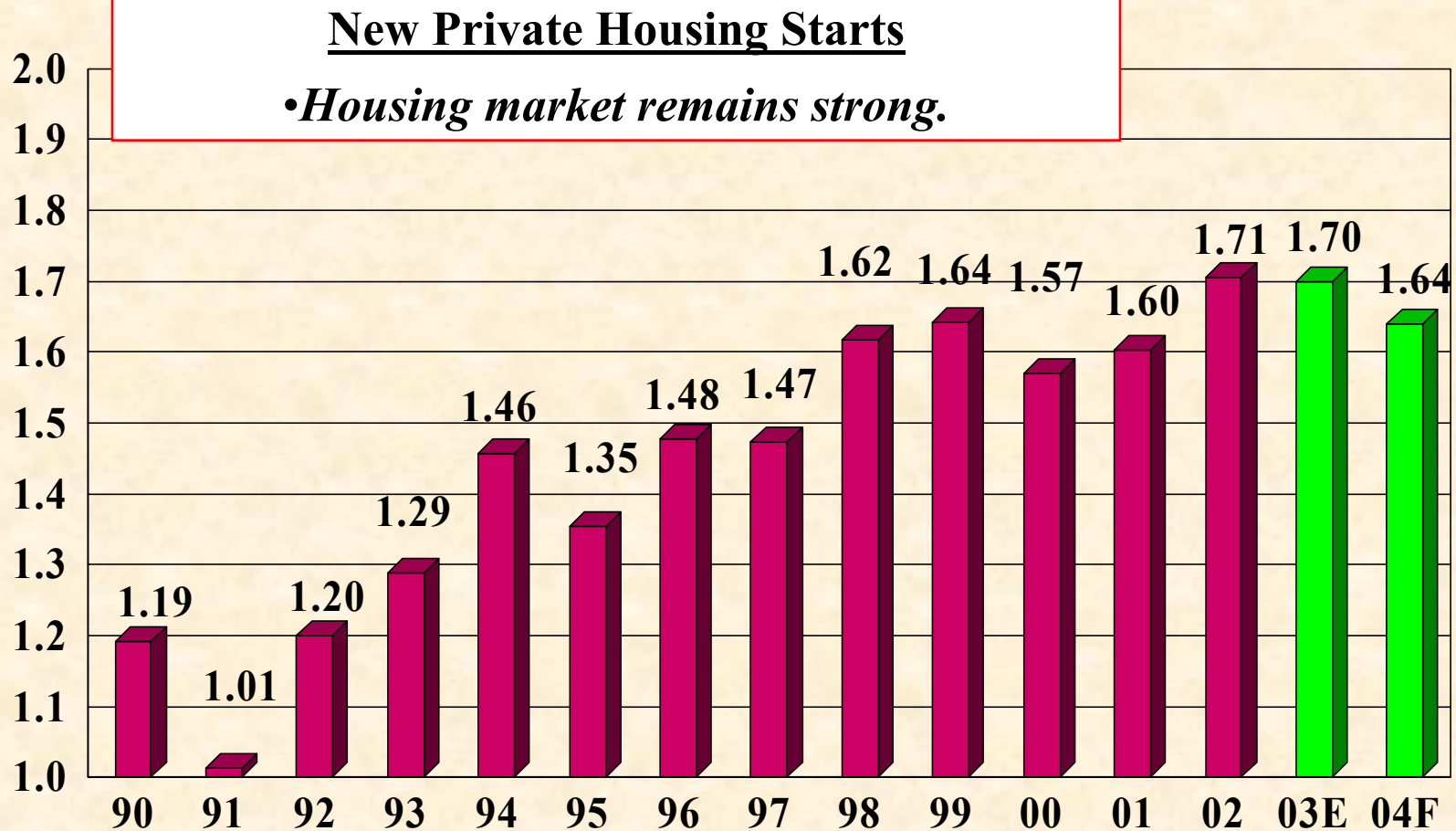


# *Change in Selected Components of GDP Growth (3<sup>rd</sup> Qtr 2003)*





# *New Private Housing Starts* *(Millions of Units)*

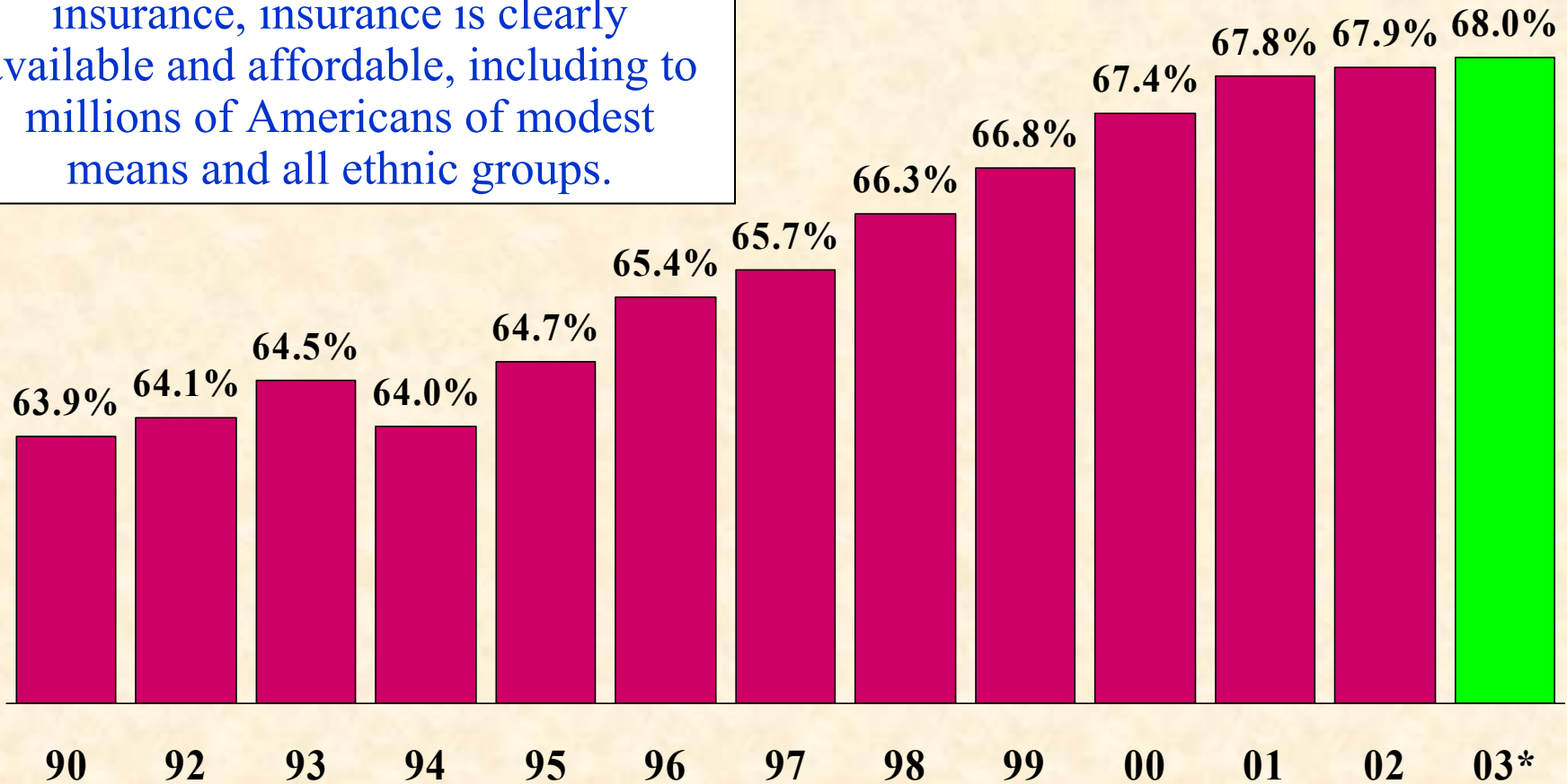






# Homeownership Rates, 1990 to 2003\*

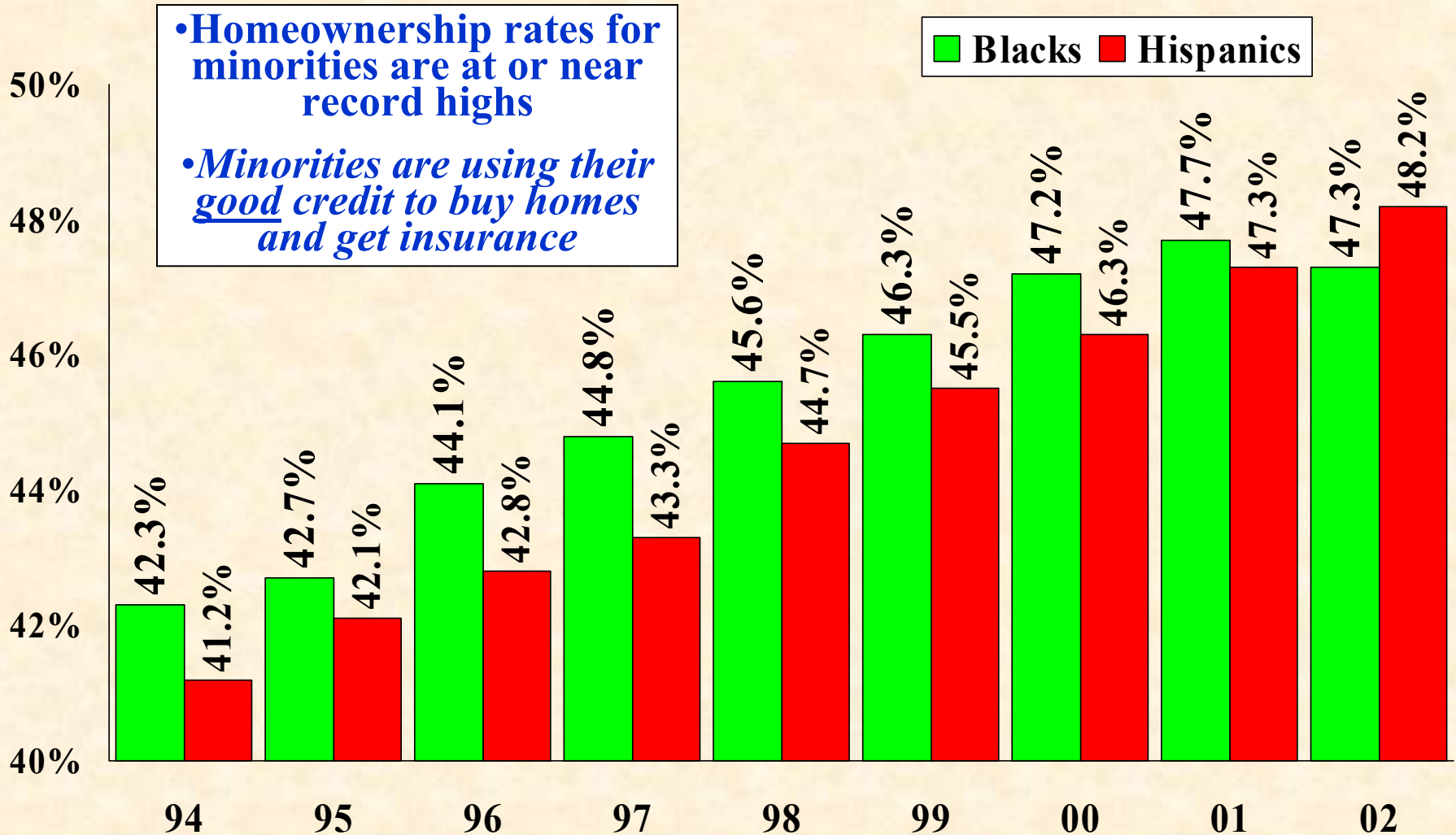
Homeownership is at a record high. Because you can't buy a home without insurance, insurance is clearly available and affordable, including to millions of Americans of modest means and all ethnic groups.



\* First Quarter  
Source: U.S. Census Bureau

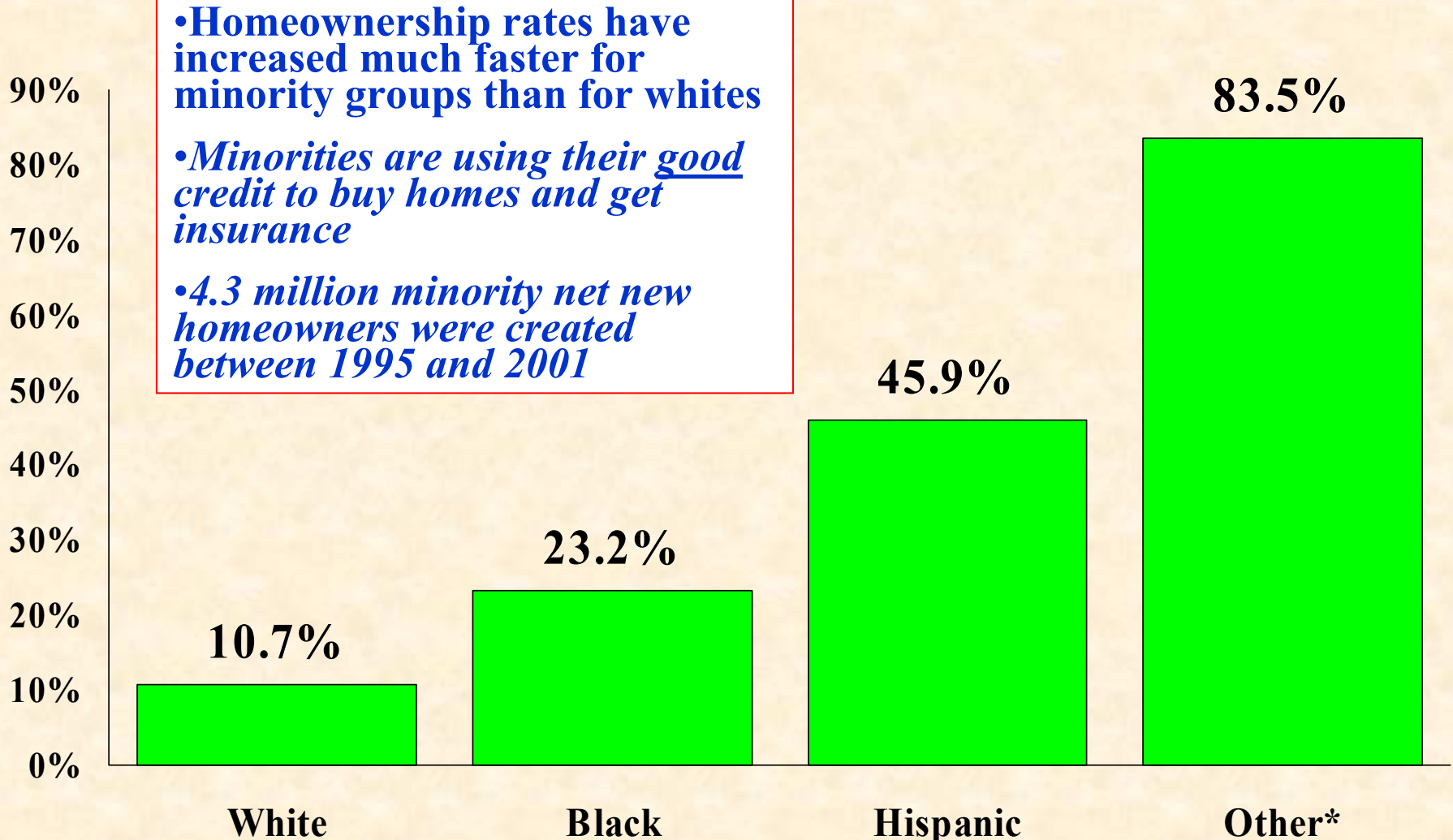


# Homeownership Rates Among Minorities is Rising, 1994 to 2002



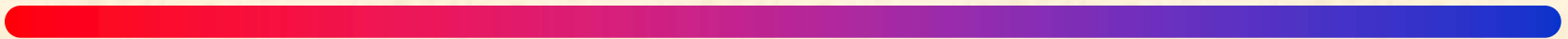


# Percent Change in Homeownership, 1995-2001



\*Includes American Indian, Eskimo, Aleut, Asian and Pacific Islander.  
Source: U.S. Census Bureau

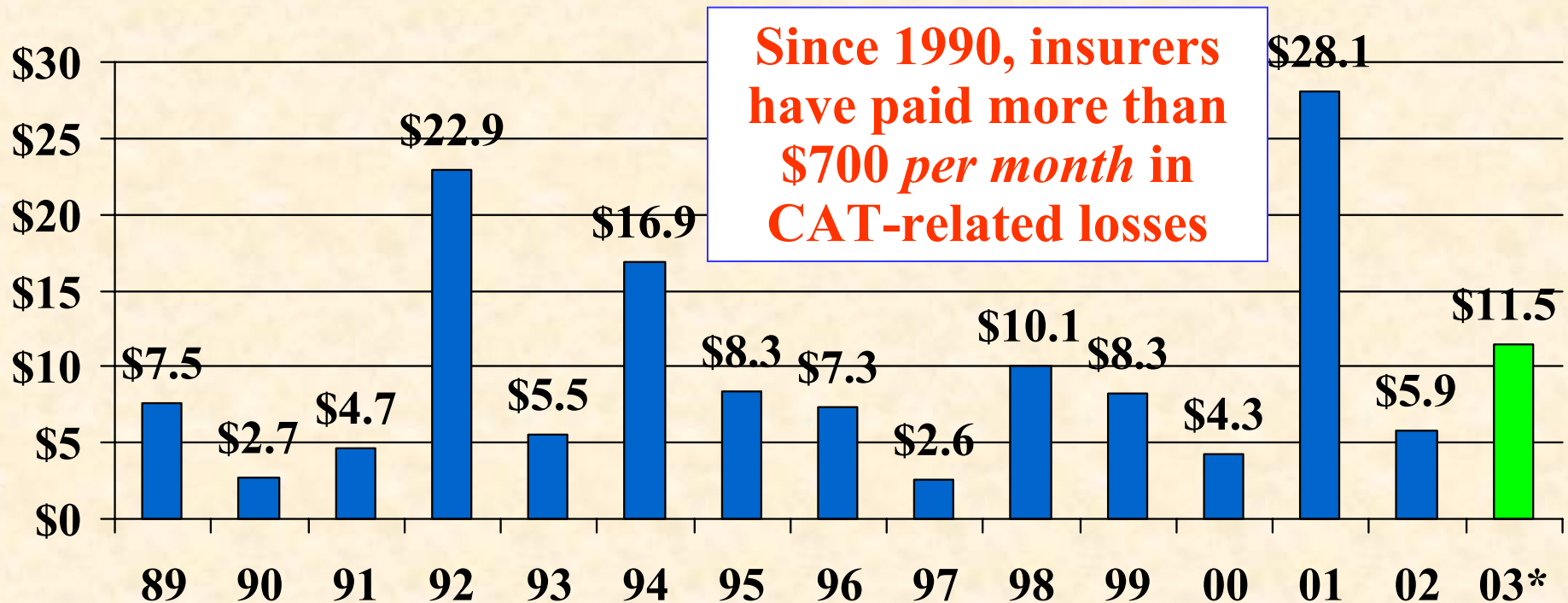
# *CATASTROPHIC PROPERTY LOSS*





# U.S. Insured Catastrophe Losses

**\$ Billions**



\*Through October 2003, including \$2B Ill estimate for California wildfires.

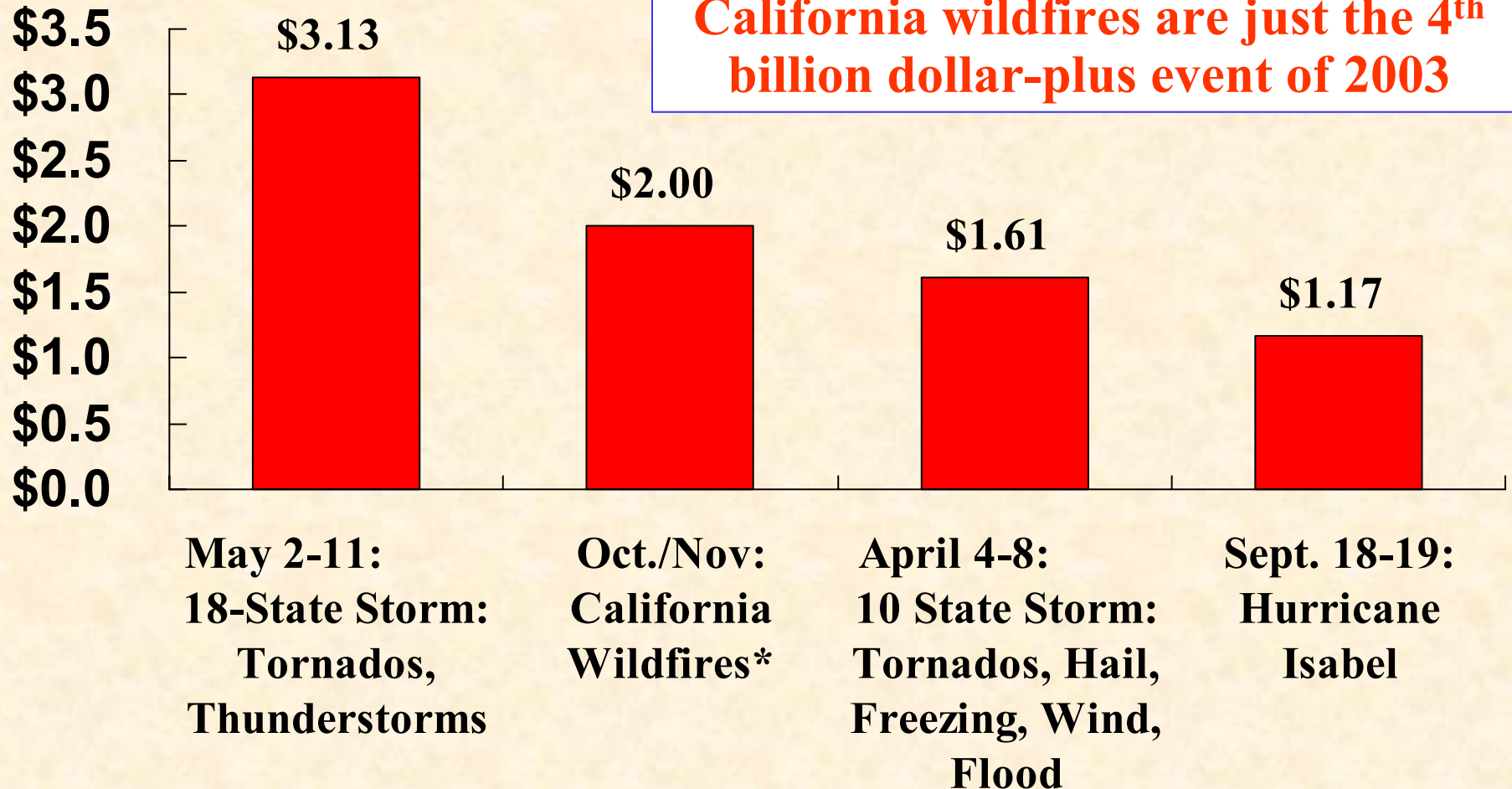
**Note:** 2001 figure includes \$20.3B for 9/11 losses reported through 12/31/01. Includes only business and personal property claims, business interruption and auto claims.

**Source:** Property Claims Service/ISO; Insurance Information Institute





# *Billion Dollar Disasters of 2003 by Insured Losses (\$ Billions)*



\*Insurance Information Institute estimate as of November 4, 2003.

Sources: Insurance Services Office



# *California Wildfires*



A home is destroyed by a wildfire in the resort community of Lake Arrowhead, California, October 29, 2003



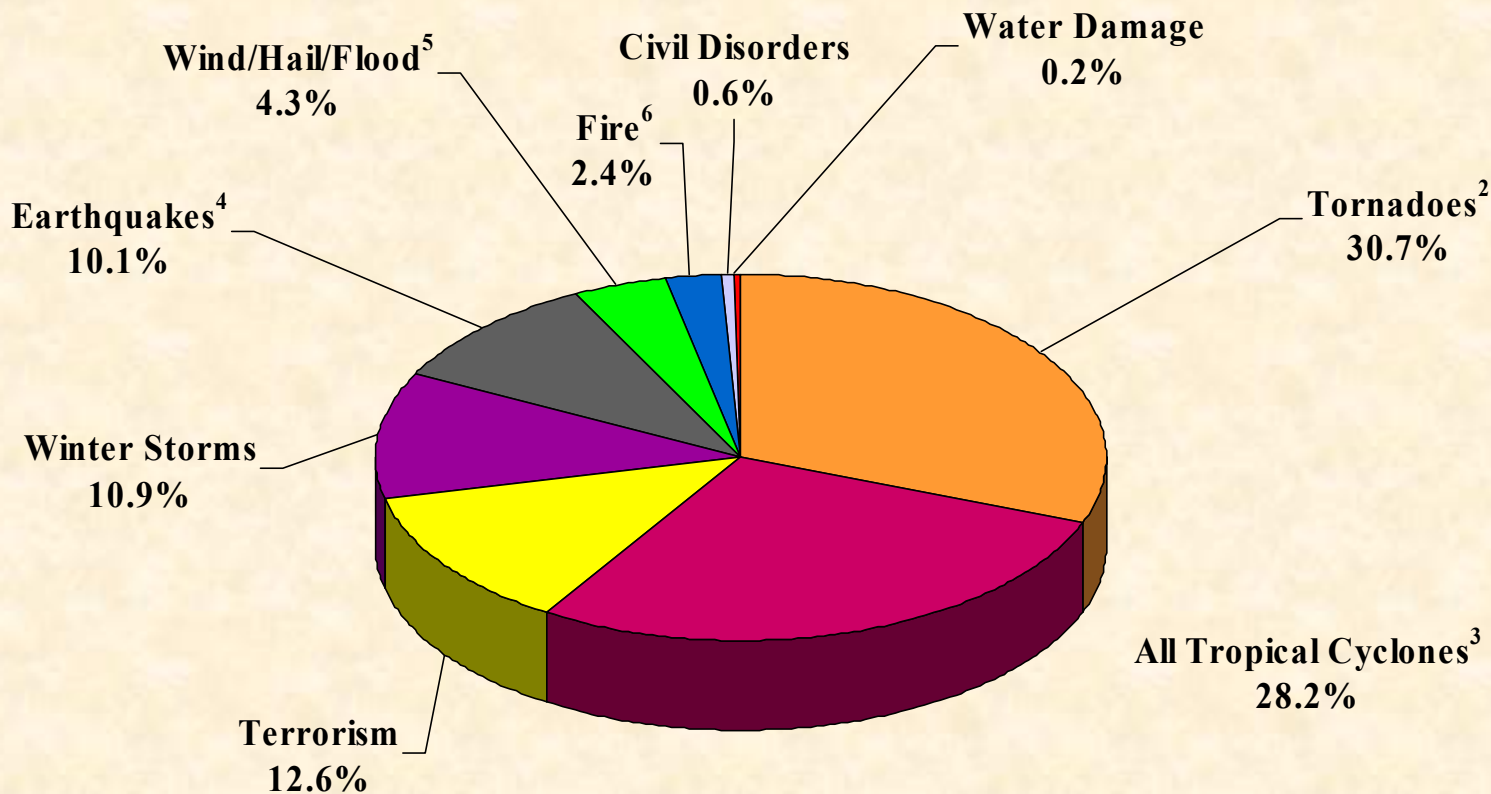
# *California Wildfires*



Homes destroyed by a wildfire near Lake Arrowhead in San Bernardino, California, Monday, Nov. 3, 2003



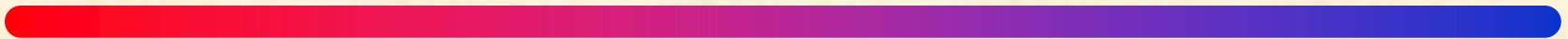
# *Inflation-Adjusted U.S. Catastrophe Losses By Cause of Loss, 1982-2001<sup>1</sup>*



<sup>1</sup> Catastrophes are all events causing direct insured losses to property of \$25 million or more in 1997 dollars. Adjusted for inflation by ISO. <sup>2</sup> Excludes snow. <sup>3</sup> Includes hurricanes and tropical storms. <sup>4</sup> Includes other geologic events such as volcanic eruptions and other earth movement. <sup>5</sup> Does not include flood damage covered by the federally administered National Flood Insurance Program. <sup>6</sup> Includes wildland fires.

*DISASTER DECLARATIONS &  
DISASTER AID:*

*PUBLIC POLICY OR POLITICS?*



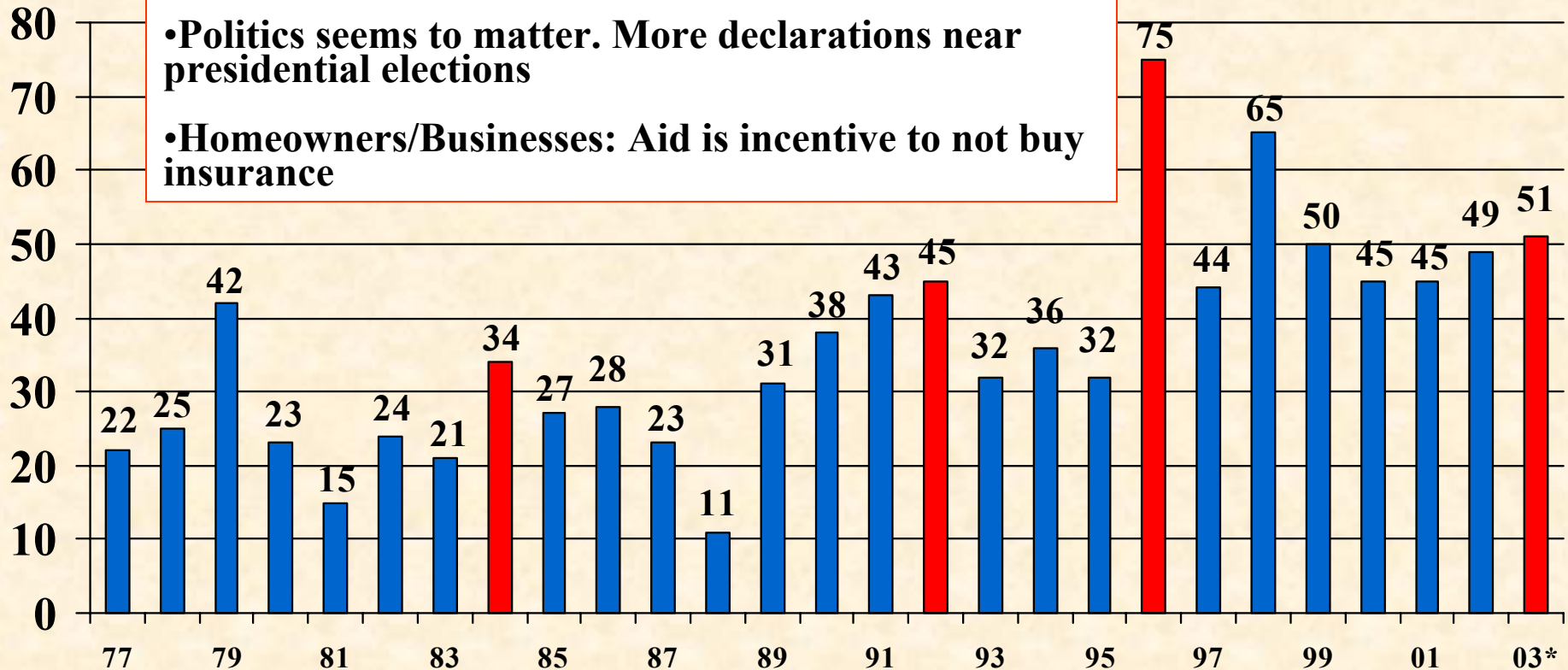




# Major Disaster Declarations By Number (1976-2003)

- A total of 1,005 major disasters have been declared by the federal government since 1977.
- The average annual figure in 2002/3 is double the 25 annual average of the 1980s.
- Politics seems to matter. More declarations near presidential elections
- Homeowners/Businesses: Aid is incentive to not buy insurance

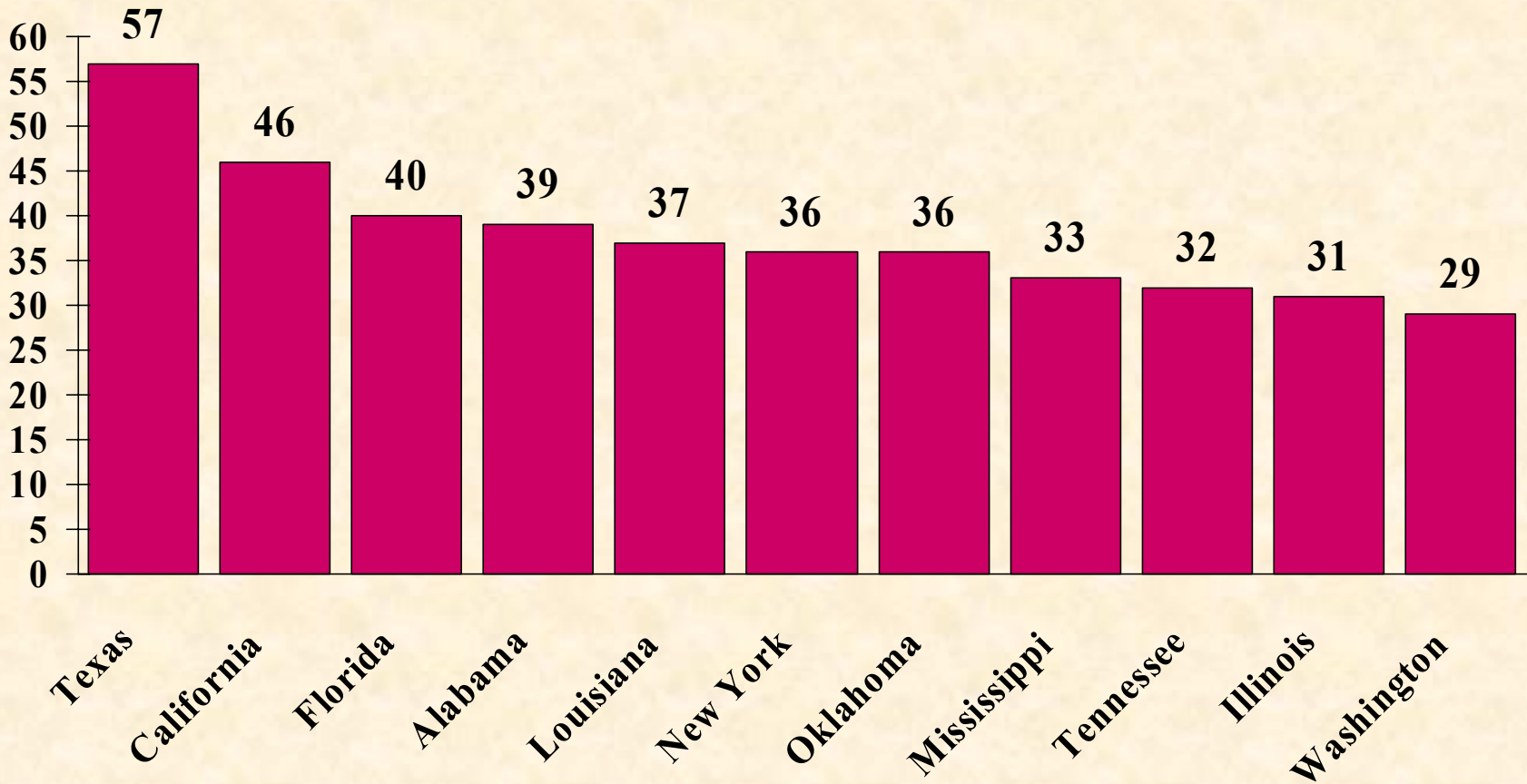
Declarations





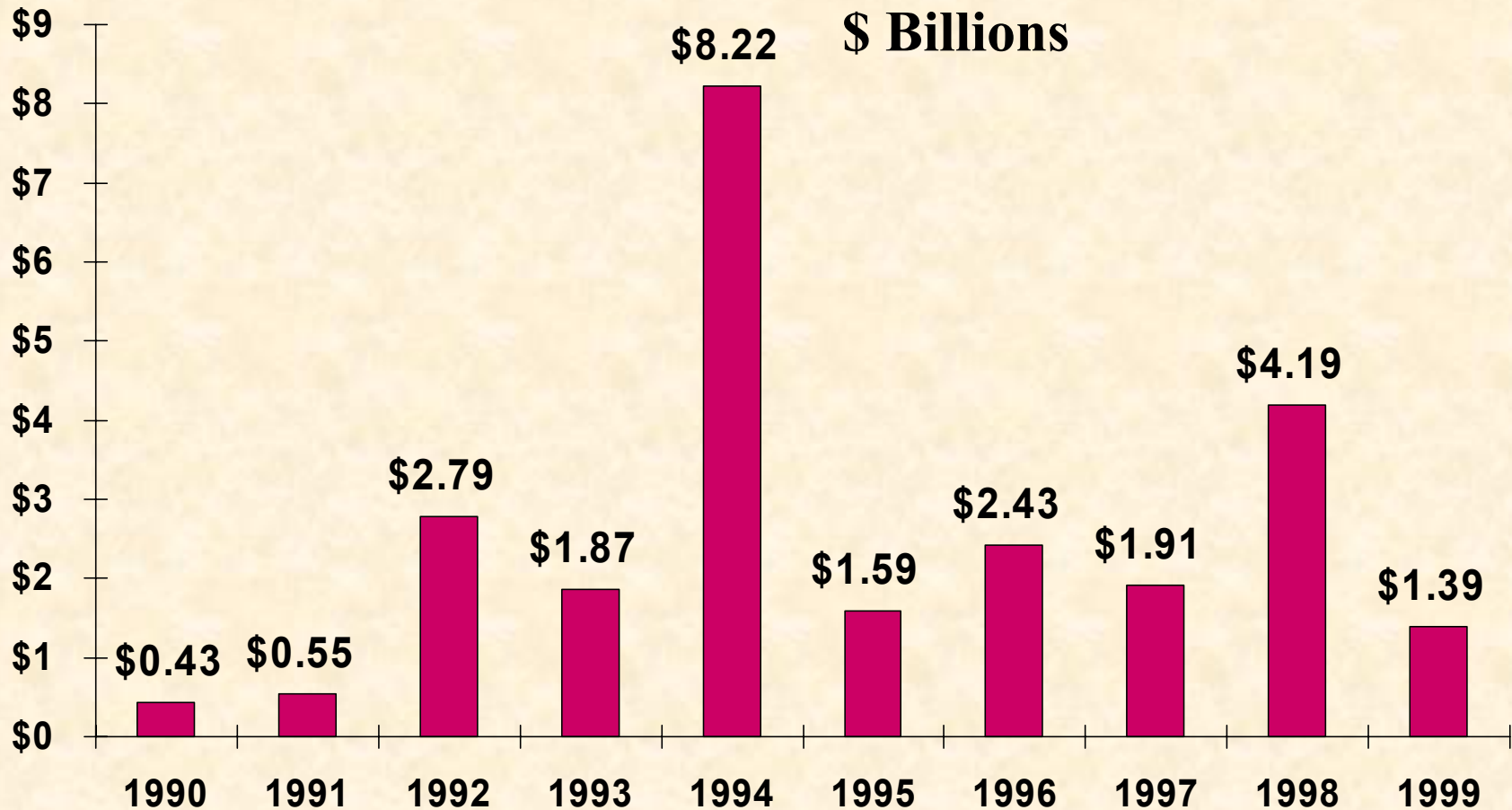
# *Top 10 Major Disaster Declaration Totals By State (1972- 2003 to-date)*

Total Number





# FEMA Disaster Expenditures\* (1990-1999)



\*Funding represents total FEMA expenditures obligated from the President's Disaster Relief Fund for declared disasters, emergencies and fire suppression grants as of February 29, 2000. Expenditures include costs for FEMA's disaster assistance programs, hazard mitigation, mission assignments, contractual services and administrative expenses. Figures are stated in current dollars and do not include funding provided separately by other participating federal agencies.

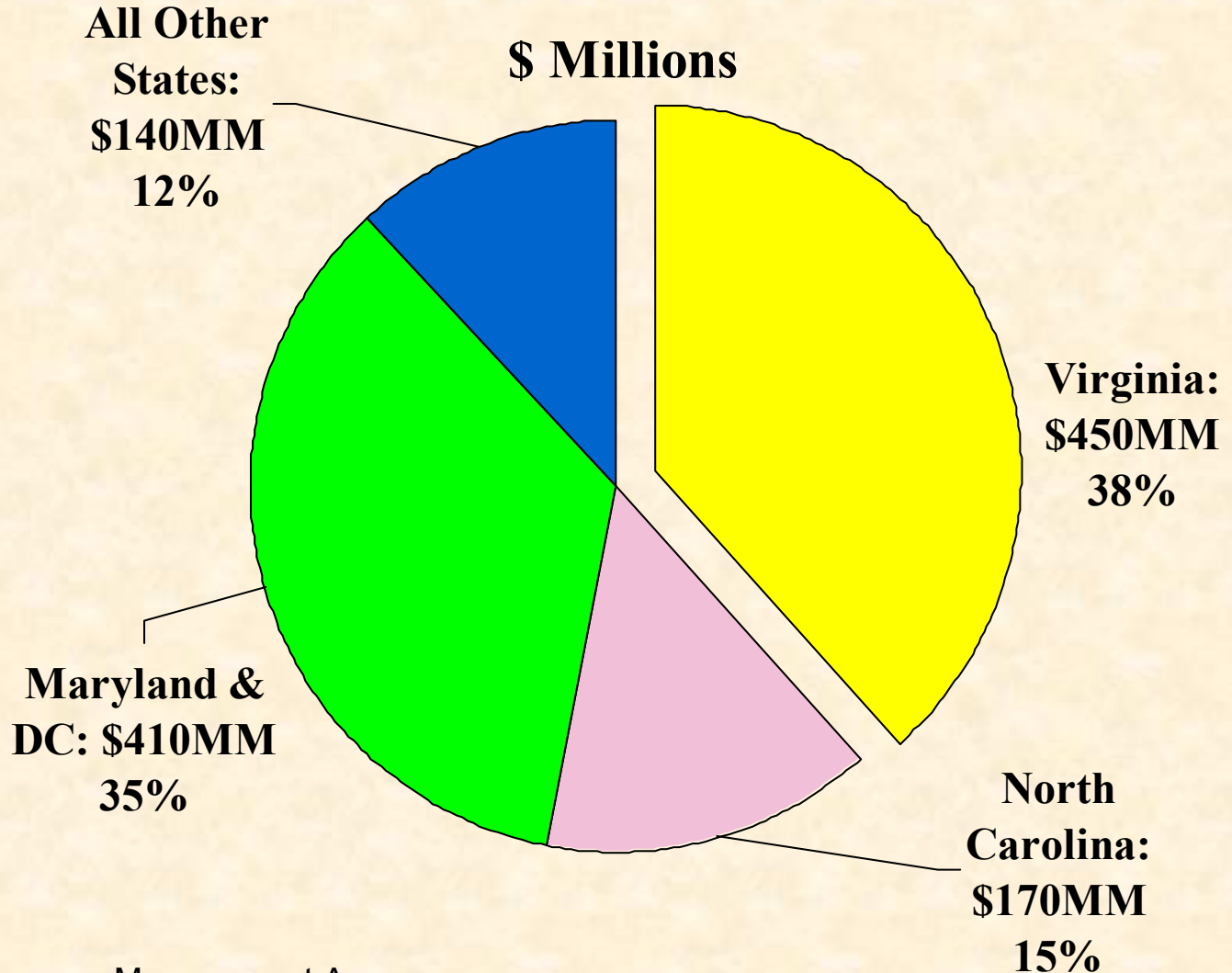
Source: FEMA



# Insured Loss Distribution for States Affected by Hurricane Isabel

## ISABEL:

- Likely economic cost \$4 - \$5 billion
- Disaster aid \$215+ million
- Private insurers paid \$1.2billion

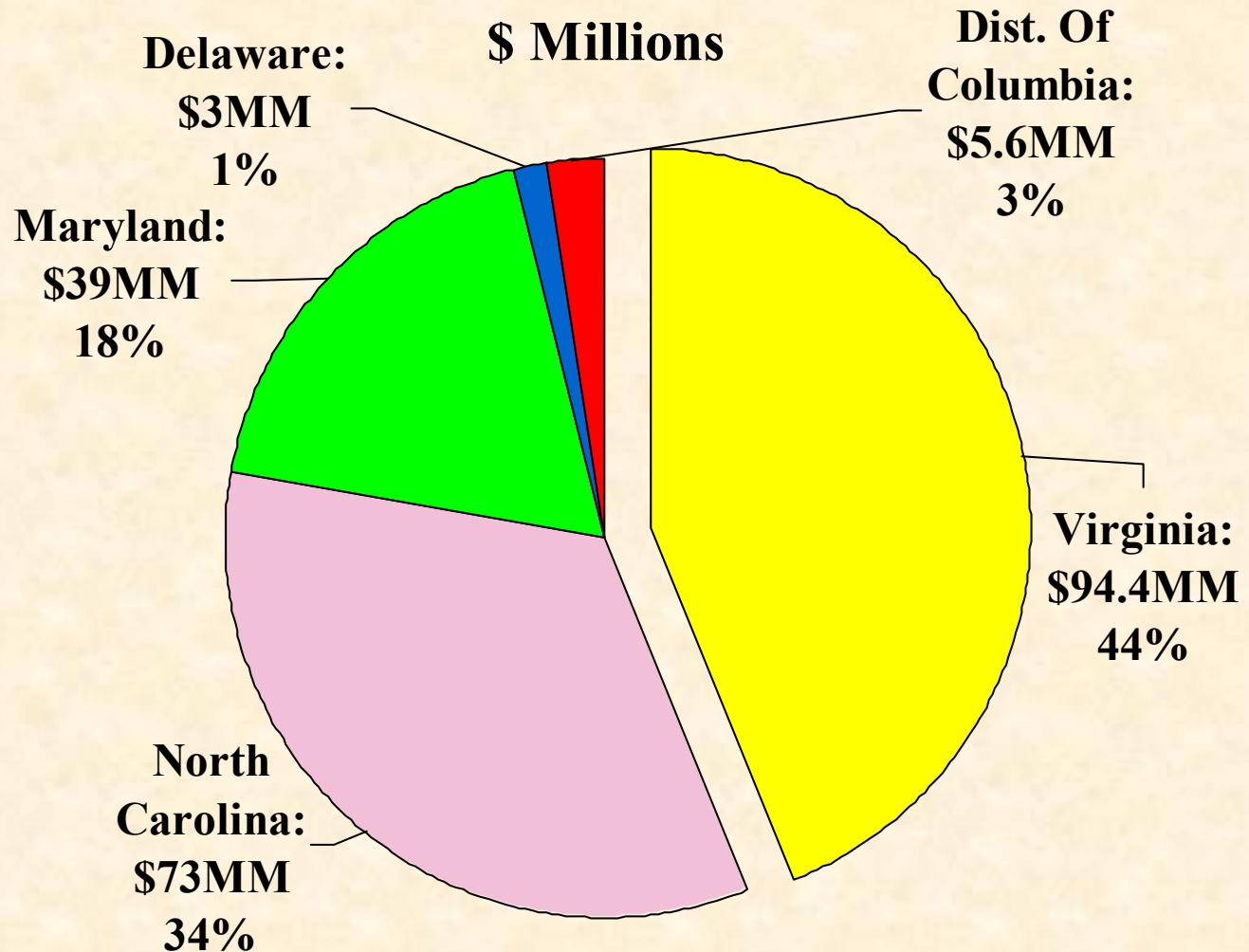




# Disaster Assistance to States Affected by Hurricane Isabel

## ISABEL:

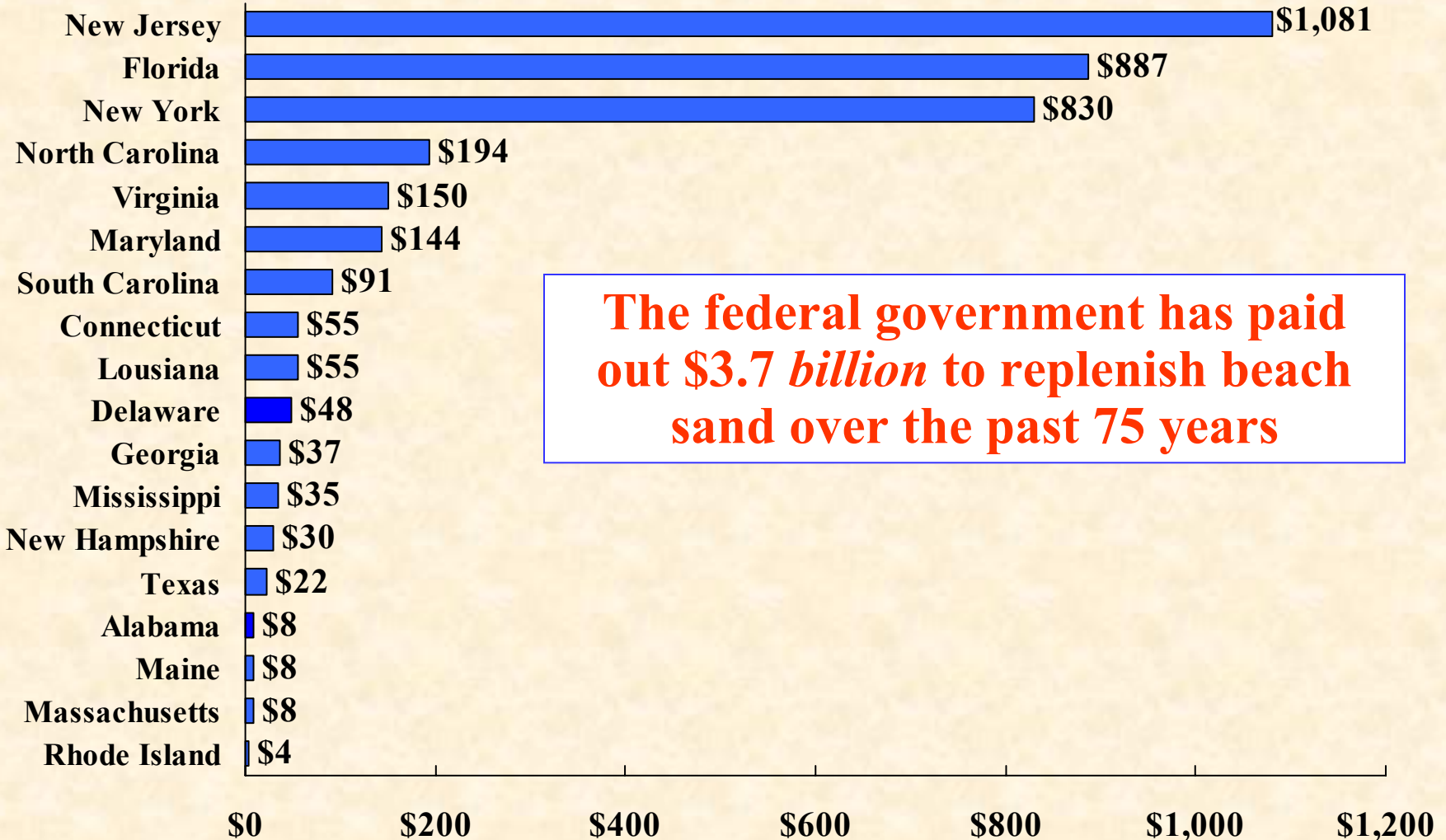
- Likely economic cost \$4 - \$5 billion
- Disaster aid \$215+ million
- Private insurers paid \$1.2 billion







# *Life's a Beach: Federal Beach Replenishment Expenditures Over the Past 75 Years, by State (2002 Dollars)*

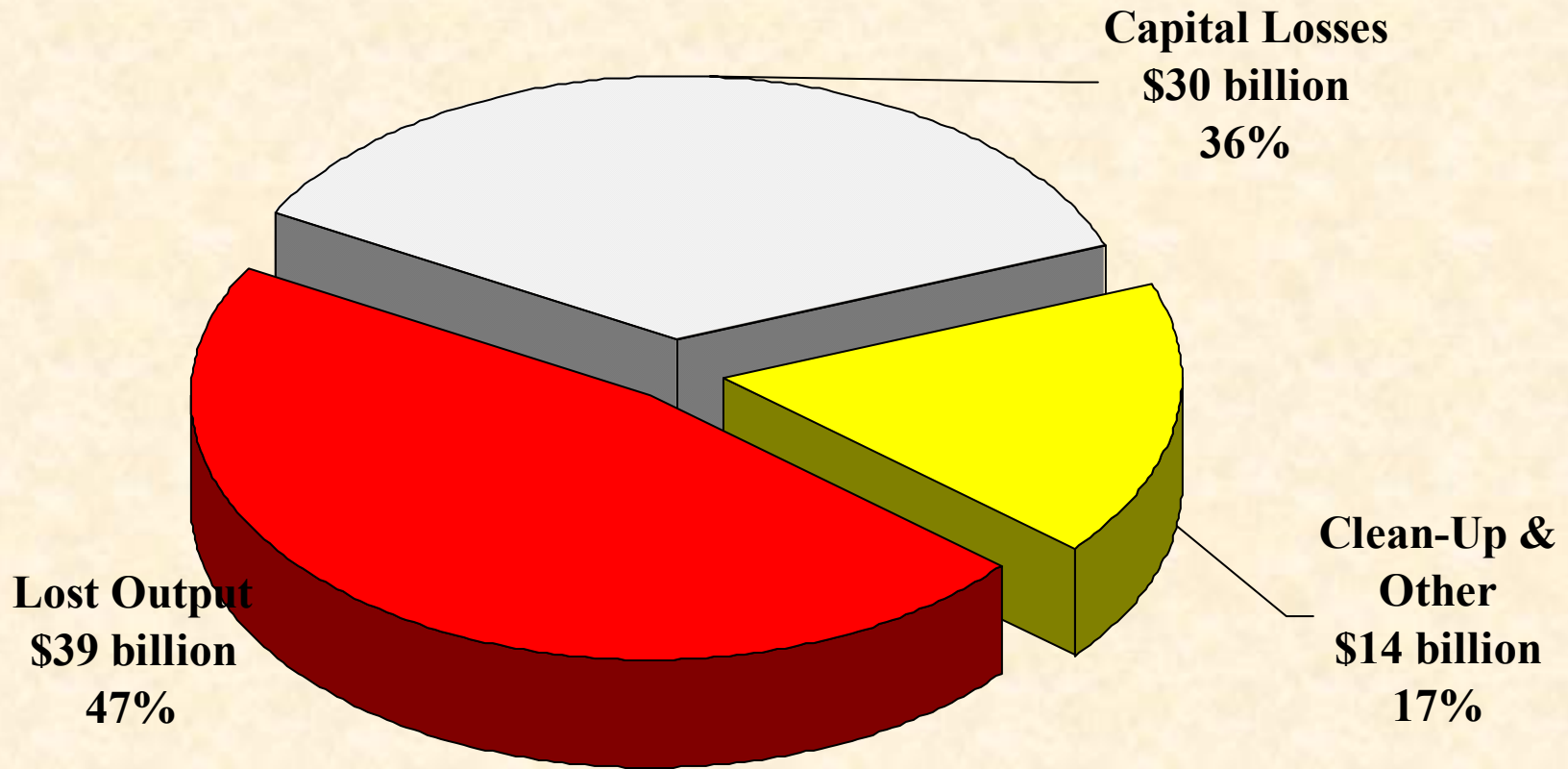


Source: Insurance Information Institute, calculated from A.M. Best combined ratio data.

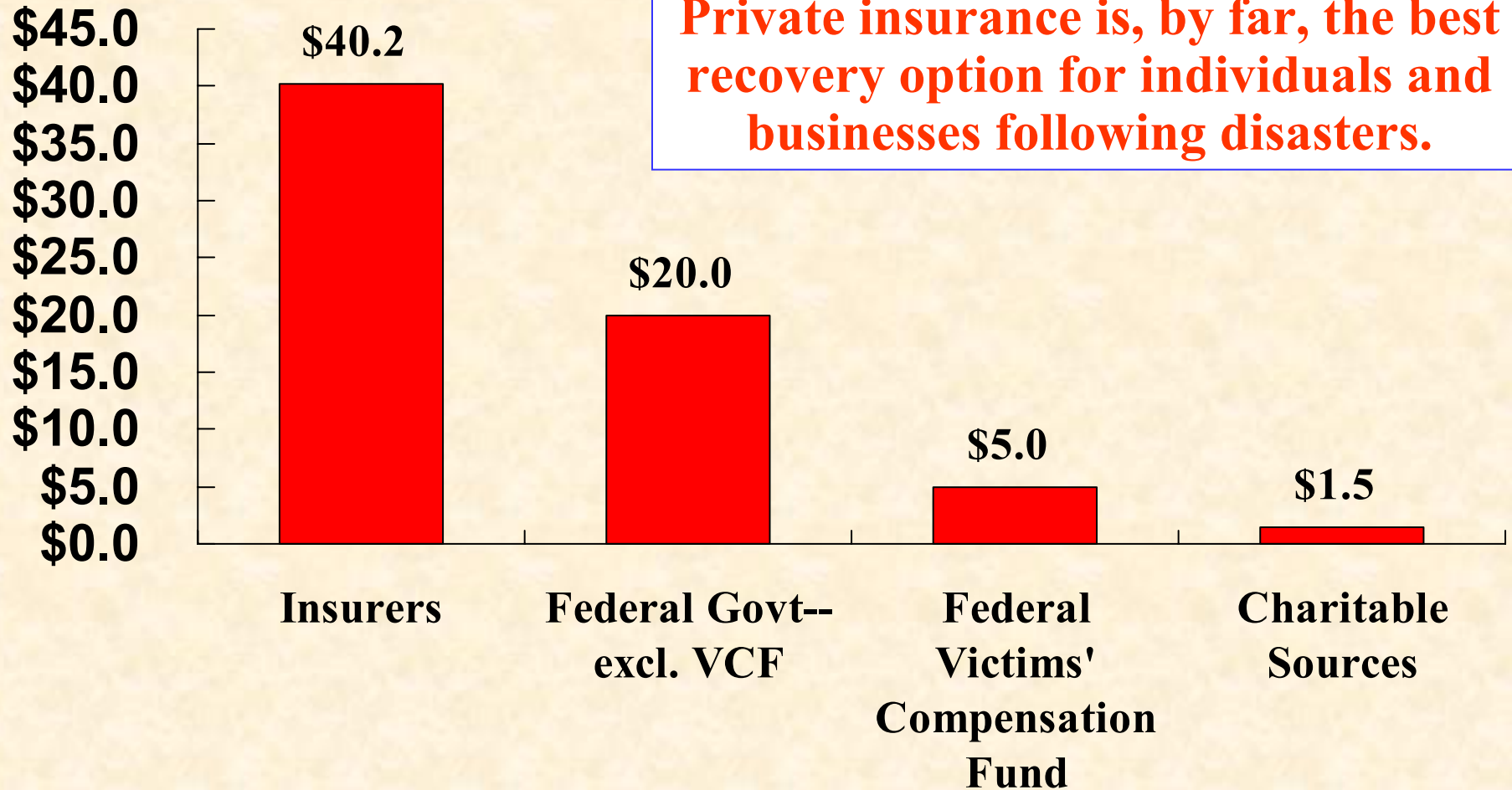


# *September 11: Economic Losses Sustained by New York City*

**Total Economic Losses to NYC = \$83 Billion**



# *No Doubt It: We (Re) Built This City* Post-9/11 Relief, by Source (*\$ Billions*)



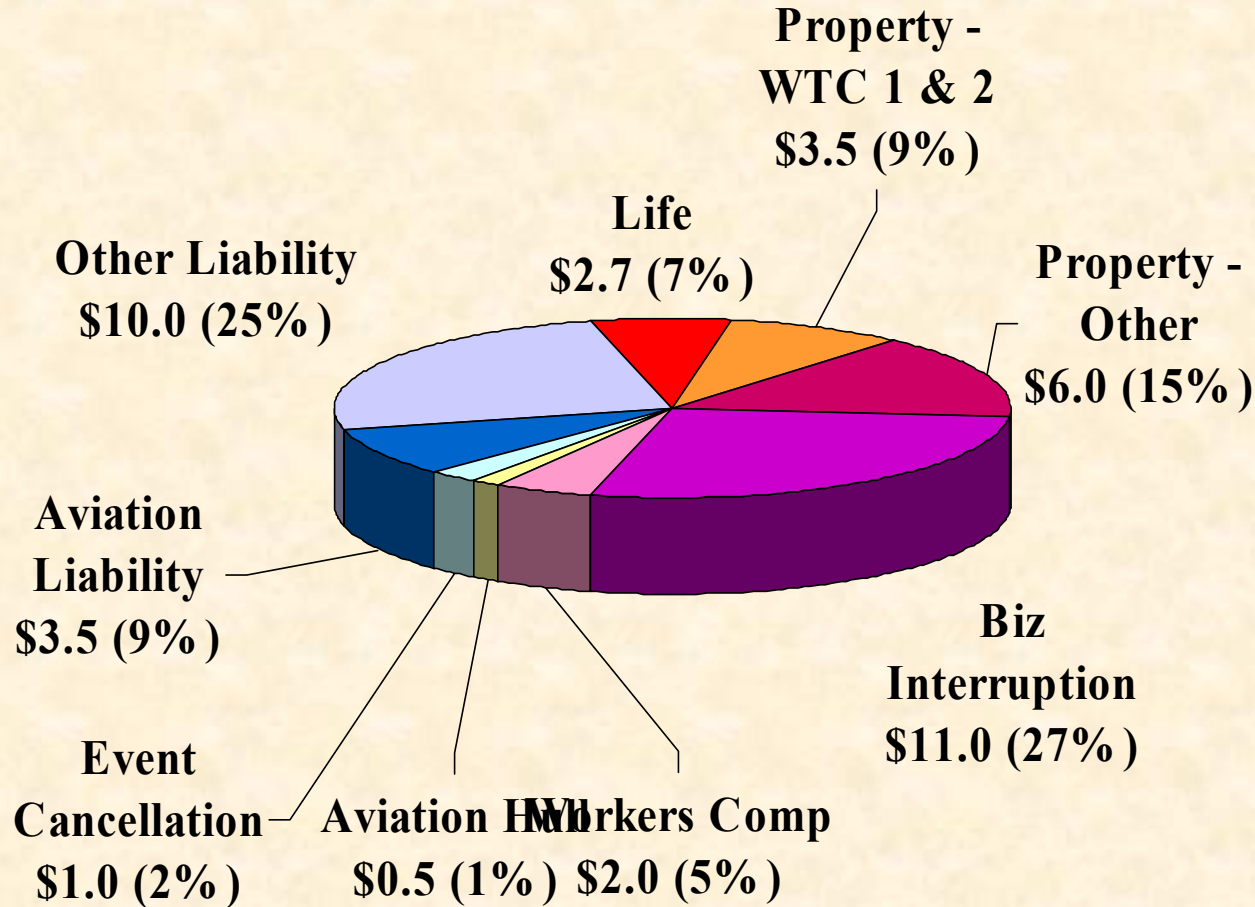
# ***TERRORISM***





# Sept. 11 Industry Loss Estimates

(\$ Billions)



## Consensus Insured Losses Estimate: \$40.2B





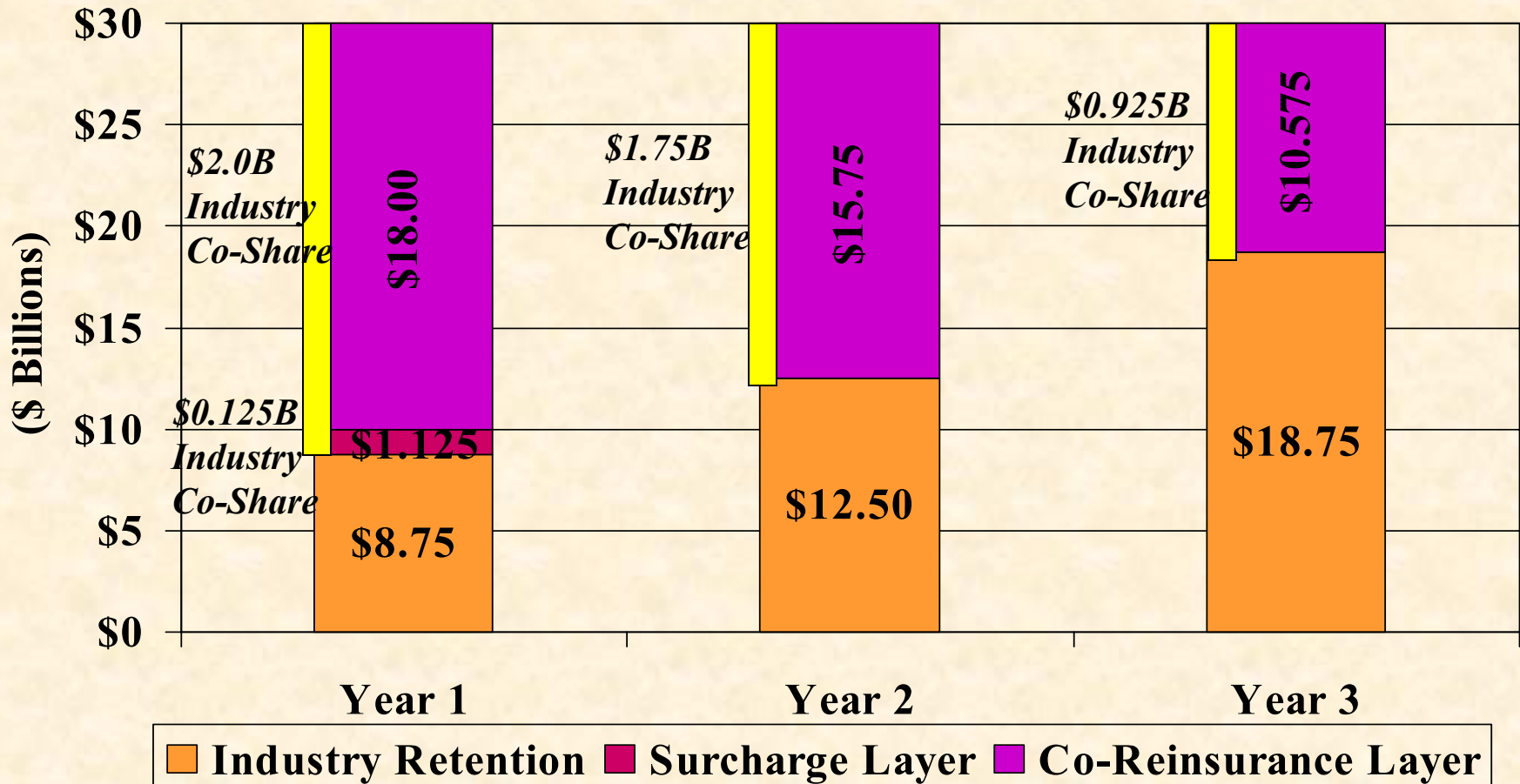
# Industry Losses Under Proposed Federal Backstop Using 9/11 Scenario

(as interpreted on date of enactment, Nov. 26, 2002)

**Total Ind. Loss:** \$10.875B

\$14.25B

\$19.675B



**Assumes \$30B Commercial Prop & WC Loss, \$125B "At Risk" Commercial DPE**



# *Insurance Information Institute On-Line*

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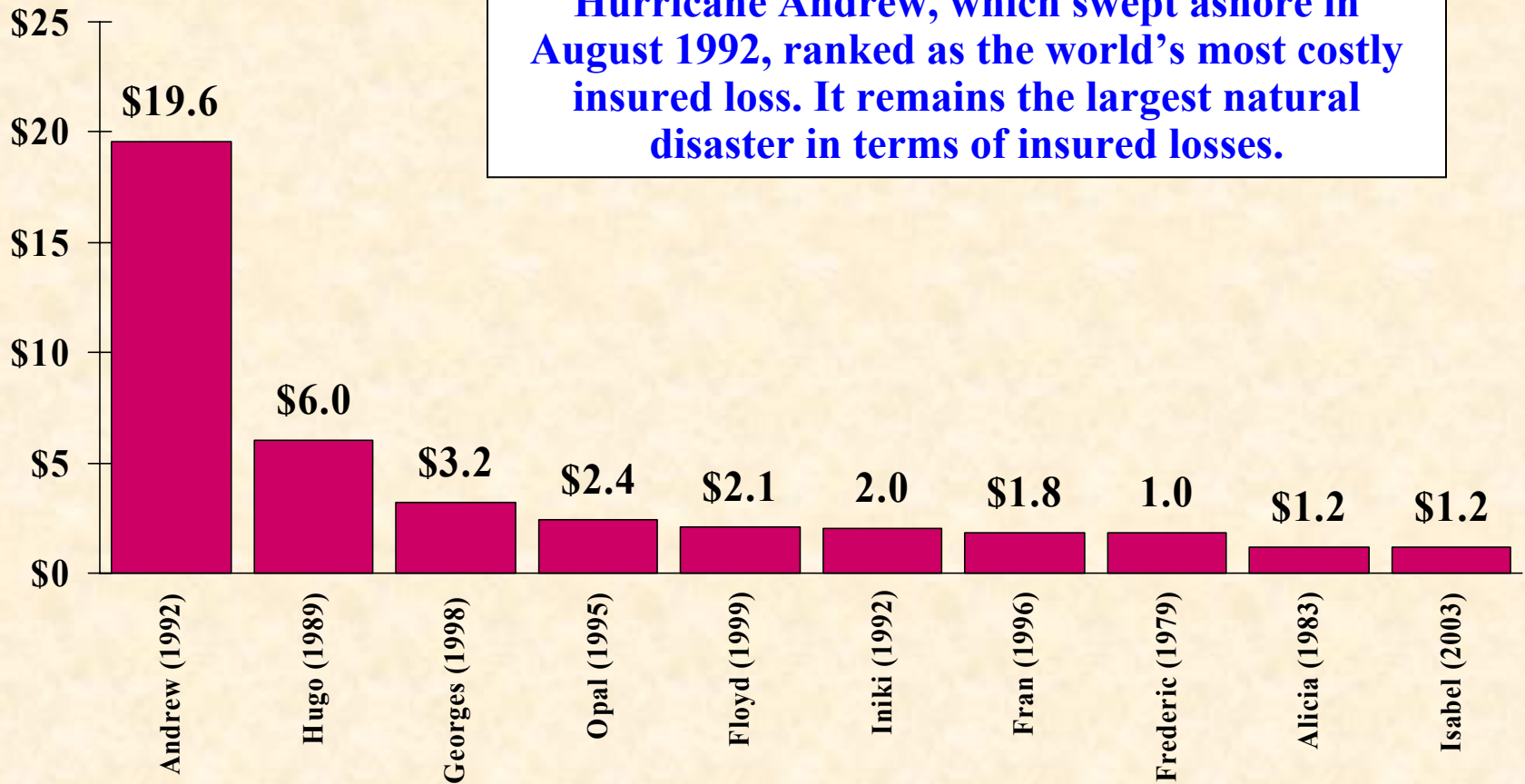
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give me your business card with e-mail address*



# The Ten Most Costly Hurricanes in the U.S. (\$ Billions)\*

\$ Billions

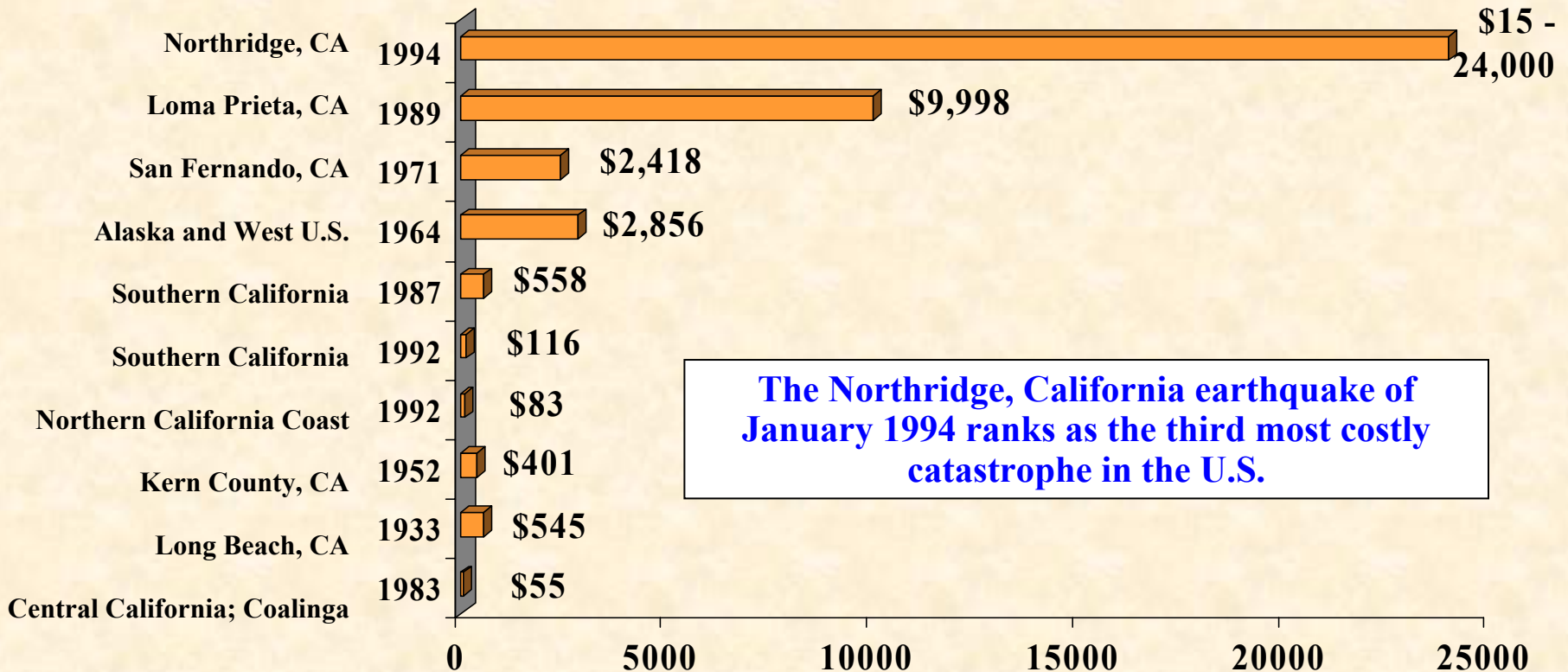


Until the World Trade Center/Pentagon attacks, Hurricane Andrew, which swept ashore in August 1992, ranked as the world's most costly insured loss. It remains the largest natural disaster in terms of insured losses.

\*Insured losses  
Source: ISO, III, AIA



# *The Ten Most Costly U.S. Earthquakes (\$ Millions\*)*



\*In 2001 dollars



# *Worst Catastrophic Wildland Fires in the US (\$ Millions)*

<b>Date</b>	<b>Location</b>	<b>In 2002 Dollars</b>
Sep. 22-30, 1970	Oakland-Berkeley Hills, California	\$114.0
Jul. 26-27, 1977	Santa Barbara, Montecito, California	59.0
Oct. 23-25, 1978	Los Angeles and Ventura Counties, California	40.2
Sep. 12-18, 1979	Hollywood Hills, California	12.1
Nov. 16-17, 1980	Bradbury, Pacific Palisades, Malibu, Sunland, Carbon Canyon and Lake Elsinore, California	33.7
Nov. 24-30, 1980	Los Angeles, San Bernardino, Orange, Riverside, and San Diego Counties, California	90.5
Oct. 9-10, 1982	Los Angeles, Ventura, and Orange Counties, California	29.3
May 17-20, 1985	Florida	55.3
Jun. 27-Jul. 2, 1990	Santa Barbara County, California	366.3
Oct. 20-21, 1991	Oakland and Alameda Counties, California	2,225.8
Oct. 27-28, 1993	Orange County, California	432.2
Nov. 2-3, 1993	Los Angeles County, California	462.7
May 10-16, 2000	Cerro Grande, New Mexico	146.9
June 23-28, 2002	Rodeo-Chediski Complex, Arizona	120.0
Oct 21-Nov 5, 2003	Los Angeles, San Bernardino, San Diego and Ventura Counties, California	2,000*
	<b>Total</b>	<b>\$6,067.9</b>

\*I.I.I. estimated insured losses as of Nov. 10, 2003

Source: Property Claim Services, Insurance Services Office, Inc. (ISO)