CUG.COMments

A Newsletter from Chicago Underwiting Group, Inc.
Underwriters of D & O and Professional Liability Insurance

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In this issue … a look at the current U.S. Property & Casualty Insurance Industry, plus, our D&O risk preferences, updated for the new year.

TODAY'S U.S. P&C INSURANCE INDUSTRY: WATERSHED OR PHONY WAR?

As 2009 begins, the overall condition of the U.S. Property & Casualty insurance industry is coming under more scrutiny than usual. The underlying data are not positive and this has given rise to speculation about the effect on premiums. This issue of CUG.COMments looks at those broad data and some current interpretations.

Losses

Although the past year did not feature a hurricane whose name entered the public lexicon in the way that Katrina did, there were nevertheless six named Atlantic storms, of which Hurricane Ike was probably the most significant. These storms, along with other events around the world, caused enough aggregated damage that Swiss Re declared it to be the second costliest year ever for catastrophe losses.

Financial claims arising from the credit crisis have been and will continue to be a significant drain on parts of the D&O and professional liability market, and the ramifications from the recent Madoff scandal will almost certainly exacerbate insured losses in this sector.

Investments

Historically used as a buffer against poor underwriting results, insurance company investments have done little to compensate the industry for its deteriorating claims picture. The bleak equities markets — the S&P 500 index closed at around 903 on December 31, 2008; twelve months earlier on January 3, it had ended the day at around 1,447— are casting a pall over the entire economy, devastating the portfolios of individuals as well as businesses. Though experiencing nothing like the same decline as equities, the value of insurers' bond holdings has also been depressed, including high-grade and municipal issues, an area traditionally favored by insurance companies.

Overall Operating Performance

A recent report by A.M. Best compares some of the key metrics for the first nine months of 2008 with the same period in 2007:

- Net written premiums were down by 0.6%.
- The combined loss and expense ratio jumped from 94.1% to 105.1%.
- Net income after taxes dropped by 85%, down to $7.3 billion.
- Policyholders' surplus declined by $36.8 billion for the twelve months ending September 2008, a reduction of around 7%.

Comments

Whether the market is "soft" or "hard," insurance professionals like to talk about when it will change. The combination of reduced income, shrinking surplus, significant losses and weak investments has prompted speculation that the downward drift in pricing is due to be reversed. Advisen Ltd., the provider of insurance information and analytics, has forecast an end to the soft market by the fourth quarter of 2009 or early 2010, and believes that the ensuing "hard" market will last longer than in recent cycles. Securities analysts at banking and financial services provider Sandler O'Neill see a hard market by the middle of 2009 as insurers face serious capital shortfalls and so will need to raise prices to help recapitalize.

Of course, there is not just one market but many. Property underwriters will respond differently to an insured's premises in coastal Florida than to those in Ohio; a D&O insurance buyer whose business is involved with financial services is already seeing a hardening market.

However, if insurers in the general marketplace continue to value market share over increasing premium, it would not be the first time in the insurance marketplace that apparent warning signals have been ignored. Pricing is also affected by demand as well as supply, and there is reason to think that less insurance will be bought in the coming year. Business failures, corporate mergers and a limit on insurance budgets will serve to reduce the aggregate commercial demand for coverage, forcing continued competition among carriers anxious to protect their books of business. Faced with a choice between renewing as expiring or losing the account because of a proposed price increase, macro-economic statistics can mean little to a harried underwriter. It is when a determination to get the desired premium outweighs the fear of a lost renewal that the "market" will begin to change.□

CURRENT D&O UNDERWRITING PREFERENCES

COVERAGE	✓ YES [⊙ Target Class]	Pass
PRIMARY **Public Company D&O** ***Capacity:*** ***Up to $15,000,000***	✓ Small to mid-size market caps ⊙ ✓ Technology ⊙ ✓ Life Sciences ⊙ ✓ IPOs ⊙ ✓ Fortune 1000 companies ✓ Energy ✓ Insurance companies ✓ All other classes, except those in "Pass" column	× Fortune 200 Companies × Financial Institutions × Financial Services × Tobacco × Gaming × Healthcare × Utilities × SPACs * × Hedge Funds × Private Equity Investment Groups
EXCESS **Public Company D&O** ***Capacity:*** ***Up to $15,000,000***	✓ Small to mid-size market caps ⊙ ✓ Technology ⊙ ✓ Life Sciences ⊙ ✓ Insurance companies ⊙ ✓ IPOs ⊙ ✓ Fortune 1000 companies ⊙ ✓ Energy ⊙ ✓ Reverse Mergers ✓ Fortune 200 companies ✓ Healthcare ✓ Utilities ✓ Financial Services ✓ Gaming ✓ Community & Regional Financial Institutions ✓ All other classes, except those in "Pass" column	× Tobacco × SPACs * × Hedge Funds × Private Equity Investment Groups × Large, Global Financial Institutions

Side A Only 1. **ExcessFirst** lead layer of a Side A / DIC program 2. Excess Side A 3. IDL ***Capacity:*** ***Up to $25,000,000***	✓ All Classes, except those in "Pass" column	✗ SPACs * ✗ Hedge Funds ✗ Private Equity Investment Groups

* Special Purpose Acquisition Companies, also known as "blank check" companies

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