

Primary Casualty—U.S.

Market Update Spring 2010



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Market Overview

Carrier earnings in the fourth quarter—and for the 2009 fiscal year—were very strong across the board. Many carriers produced record quarterly results in the fourth quarter boosted by historically low combined ratios and low catastrophic activity.

A sampling of the results from the major carriers is highlighted below:

Carrier	Fourth Quarter—2009		Year End—2009	
	Net Income	Combined Ratio	Net Income	Combined Ratio
ACE	\$953M	89.6%	\$2.5B	88.3%
ARCH	\$285M	88.8%	\$851M	88.1%
Hartford	\$508M	92.6%	(\$887M)	85.1%
Travelers	\$1.3B	94.0%	\$3.6B	83.4%
Zurich	\$1.1B	N/A	\$3.2B	96.8%

Contributing to the strong earnings was a string of reserve releases. All of these carriers released reserves from prior years due to more favorable loss development trends accounting for as much as 10 to 20 percent of earnings in the fourth quarter. Travelers' combined ratio was lifted 9.4 points by bringing down their reserves.

A notable exception to the strong carrier performance is Chartis. The insurance operations of Chartis lost \$1.8 billion in the fourth quarter due to the need to strengthen their reserves by \$2.3 billion. Their combined ratio was 132.5 percent for the quarter, which included 28.2 points of reserve strengthening, and 99.2 percent for the entire year.

As an industry, returns on equity were healthy and high by historical standards. Carriers were able to increase their overall capital levels, repurchase stock, pay dividends, or a combination of each.

The strong profitability was impressive given the investment environment. Investment returns were modest due to the low yields and because many carriers took a more conservative stance with their investment portfolio given the uncertain economic and credit conditions.

What does this mean for insurance buyers? The favorable pricing environment will continue and may accelerate. Despite falling prices, carriers have been able to produce very healthy financial results compared to historical standards. In addition, industry surplus (supply) continues to increase, and the surplus is chasing a finite number of buyers (demand). Most of these buyers have reduced exposures (revenue, payroll, etc.) due to the impact of the economy, resulting in lower premiums.

The business environment is increasingly forcing buyers to market their business to attain the best deal. Carriers have consistently generated solid retention rates over the past several years, but they may be asked to concede more today to retain the business given the dynamics of the marketplace. These conditions set up a very favorable environment for buyers.

In addition, it is difficult for companies to switch carriers because overall collateral levels tend to be incrementally higher when you move from one carrier to another. In the current credit environment, buyers are seeking to minimize collateral, and this proves to be a formidable impediment to switching carriers. This places more carrier emphasis on retaining its existing business and has caused carriers to drop prices, sometimes significantly.

Our view is for a continuing soft marketplace characterized by declining prices, strong carrier competition, and choice as well as improving terms and conditions.