

2020 FINANCIAL SUMMARY

RESULTS OF OPERATIONS

State Fund's results of operations for years ended December 31, 2020 and 2019 and its corresponding financial ratios are shown below:

(In millions)	2020	2019
Net premiums earned	\$ 1,016	\$ 1,190
Losses incurred	711	464
Loss adjustment expenses (LAE) incurred	223	201
Underwriting and administrative expenses	509	472
Premium deficiency	<u>15</u>	<u>-</u>
Net underwriting gain (loss)	(442)	53
Net investment and realized gain	662	726
Other loss	<u>(48)</u>	<u>(80)</u>
Income before dividends	172	699
Dividends to policyholders	<u>(100)</u>	<u>(160)</u>
Net income	<u><u>\$ 72</u></u>	<u><u>\$ 539</u></u>
Loss ratio	70.0%	39.0%
LAE ratio	22.0%	16.9%
Underwriting expense ratio	<u>49.2%</u>	<u>39.6%</u>
Combined ratio	<u><u>141.2%</u></u>	<u><u>95.5%</u></u>

State Fund's premium declined in 2020 due to the reduction of estimated audit premium bills of \$45 million as a result of projected reduced payroll brought by the COVID-19 impact and decrease in rate filed of 10%. State Fund had a \$442 million underwriting loss in 2020 compared to a \$53 million underwriting gain in prior year. The 2020 underwriting loss was due to decline in premium, higher Loss and LAE incurred of \$269 million due to less reserves release compared to prior year to recognize the uncertainties introduced by COVID-19 claims, \$15 million in premium deficiency reserve, and \$37 million increase in underwriting expenses, of which \$44 million was from COVID-19 safety funds net of the \$7 million decrease in premium taxes.

Net investment income and realized gain on sale of equity decreased by \$64 million primarily due to lower interest rates and increase in amortization expenses of \$25 million. Net income before dividends of \$172 million was \$527 million lower than prior year mainly due to the significant reserve release mentioned above. The board of directors declared regular dividends of \$114 million and large account safety dividend of \$4 million but this was partially offset by an \$18 million release of 2019 policyholders' dividends reserves in excess of estimated payments. Therefore, total declared dividends were \$100 million, which resulted in net income after dividends of \$72 million.

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FINANCIAL POSITION

State Fund's financial positions at December 31 are as follows:

(In millions)

Admitted Assets	2020	2019
Bonds, at amortized cost	\$ 18,977	\$ 19,094
Common stocks	941	1,037
Real estate	288	276
Cash and short-term investments	55	145
Total cash and invested assets	<u>20,261</u>	<u>20,552</u>
Other assets	369	423
Total admitted assets	<u>\$ 20,630</u>	<u>\$ 20,975</u>

Liabilities and Policyholders' Surplus

Loss and LAE reserves net of reinsurance	\$ 11,424	\$ 11,880
Other liabilities	<u>2,840</u>	<u>2,583</u>
Total liabilities	14,264	14,463
Policyholders' surplus	<u>6,366</u>	<u>6,512</u>
Total liabilities and policyholders' surplus	<u>\$ 20,630</u>	<u>\$ 20,975</u>

State Fund maintained a balanced investment portfolio that was focused on both credit quality and investment yield (88% of the \$18.9 billion bond portfolio was rated NAIC 1, the NAIC's highest quality credit class). The weighted average credit quality of the overall bond portfolio was Aa3/AA- by Moody's and Standard & Poor's, respectively. Book yield at December 31, 2020 was 2.92%, decreased from 3.22% at December 31, 2019.

Management believes that its reserves are adequate, and State Fund's appointed Actuary, Guy Avagliano of Milliman, Inc., consulting actuaries, opined to the adequacy of State Fund's carried reserves as of December 31, 2020 and 2019.

State Fund operates in conformity with the California law imposed for risk-based capital (RBC). As of December 31, 2020 and 2019, policyholders' surplus exceeded the minimum RBC requirements. In addition, it passed all the Insurance Regulatory Information System (IRIS) tests at year-end 2020 and 2019.

Policyholders' surplus went down by \$145 million to \$6.4 billion since December 31, 2019. This was mainly due to \$181 million reclassification of surplus to recognize State Fund's share of Pension and Other Post Employment Benefit (OPEB) as liabilities in compliance with Statements of Statutory Accounting Principles (SSAP) No. 5R – "Liabilities, Contingencies and Impairments of Assets". The additional differences were attributed to a decrease of \$17 million in unrealized capital gains, a \$19 million decrease in non-admitted assets, offset by net income of \$72 million.

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CASH FLOW

State Fund's statements of cash flow are summarized below:

(In millions)	2020	2019
Premiums collected net of reinsurance	\$ 1,001	\$ 1,163
Net investment income	669	685
Miscellaneous income	9	23
Benefits and loss related payments	(1,113)	(1,060)
Other underwriting expenses	(814)	(806)
Dividend paid to policyholders	(141)	-
Net cash provided by (used in) operations	<u>(389)</u>	<u>5</u>
Proceeds from investments sold, matured, or repaid	5,491	4,186
Cost of investments acquired:	<u>(5,288)</u>	<u>(4,149)</u>
Net cash provided by investments	<u>203</u>	<u>37</u>
Net cash provided by financing and miscellaneous sources	<u>96</u>	<u>21</u>
Net change in cash, cash equivalents, and short-term investments	(90)	63
Cash, cash equivalents, and short-term investments, beginning of year	<u>145</u>	<u>82</u>
Cash, cash equivalents, and short-term investments, end of year	<u><u>\$ 55</u></u>	<u><u>\$ 145</u></u>

Primary sources of cash included cash flow from premiums, investment income, and the sale or maturity of invested assets. Primary uses of cash included the purchase of long-term investments and the payments of benefits, loss related expenses, and other underwriting expenses.

Cash flow provided by insurance operations decreased from prior year mainly due to less premium resulting from the negative impact of COVID-19, moratorium on policy cancellations, and \$141 million dividend payments.

Cash flow provided by investments increased from prior year mainly due to proceeds from sale of investments exceeding reinvestment.