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Date: August 3, 2018

**TO: MEMBERS, BOARD OF DIRECTORS**

<b>I. AGENDA ITEM # AND TITLE:</b>	Open Agenda Item 5 – Financial Update: 2 <sup>nd</sup> Quarter 2018
<b>II. NAME AND PROGRAM:</b>	Peter Guastamachio, Chief Financial Officer
<b>III. ACTIVITY:</b>	<input checked="" type="checkbox"/> Informational <input type="checkbox"/> Request for Direction <input type="checkbox"/> Action Proposed <input type="checkbox"/> Exploratory
<b>IV. JUSTIFICATION:</b>	<input checked="" type="checkbox"/> Standard/Required Item <input type="checkbox"/> Board Request – New Item <input type="checkbox"/> New Topic from Staff

**V. EXECUTIVE SUMMARY:**

- Net premiums earned of \$694 million were 0.2% more than the prior year.
- Combined ratio of 132.5% was slightly higher than the same period last year which resulted in underwriting loss of \$224 million.
- Net income of \$72 million was \$94 million less than the same period in the prior year.
- Policyholders’ surplus grew by \$38 million since December 31, 2017.

**VI. ANALYSIS /BACKGROUND:**

- Statutory financial results are filed with the California Department of Insurance and the National Association of Insurance Commissioners on a quarterly basis.
- Highlights are also shared with the Board on a quarterly basis.

**STATE COMPENSATION INSURANCE FUND**  
**Report on Statutory Financial Results**  
**Six Months Ended June 30, 2018**

The following summarizes our statutory financial results for the six months ended June 30, 2018. Our results reflect a slight increase in premiums earned and increase in policyholders' surplus.

- Underwriting results
  - Due to the nature of our business, our underwriting results are significantly impacted by the dynamics that affect California business including economic conditions, market pricing as well as the effects of the insurance profitability cycle.
  - Though the market continues to be competitive, net premiums earned of \$694 million were 0.2% higher than the prior year mainly due to increase in audited premiums.
  - Our loss and loss adjustment expenses (LAE) ratio of 99.3% were 1 point lower than prior year.
  - Underwriting expense ratio of 33.2% was 2 points higher than the same period last year.
  - Combined ratio of 132.5% was slightly higher than the same period last year mainly due to the increase in our underwriting expenses.
- Investment and other non-underwriting results
  - Net investment income of \$310 million was \$8 million lower than the same period in prior year.
  - Realized capital gains of \$15 million were \$79 million lower than the same period in prior year. The liquidation of holdings from the termination of an equity portfolio manager in the first quarter of 2017 generated large capital gains which was a one-time event.
  - Other expenses, mostly representing charge-offs of uncollectible premiums, were \$7 million higher than the same period in the prior year.
- Net income and policyholders' surplus
  - Net income of \$72 million was \$94 million lower than the same period in the prior year mainly due to lower realized capital gains.
  - Policyholders' surplus grew by \$38 million since December 31, 2017.

**STATE COMPENSATION INSURANCE FUND**  
**Report on Statutory Financial Results**  
**Six Months Ended June 30, 2018**

Financial Results (\$ millions)	2017 Actual	2018 Actual	Actual vs. Prior Year \$ Diff	Actual vs. Prior Year % Diff
Net premiums earned (NPE)	692	694	1	0.2%
Losses	512	499	(13)	-2.5%
Loss adjustment expenses	184	189	5	2.8%
Underwriting (UW) expenses	219	229	10	4.7%
Underwriting results	(223)	(224)	(1)	-0.5%
Net investment income	318	310	(8)	-2.5%
Realized capital gain (loss)	94	15	(79)	-84.1%
Other income (expense)	(21)	(28)	(7)	-30.6%
Income before dividends to policyholders	167	73	(94)	-56.6%
Dividends to policyholders (credits)	0	0	(0)	-79.2%
Net income (loss)	167	72	(94)	-56.5%
<b>Standard Industry Ratios</b>				
Loss ratio	74.0%	72.0%		-2.0%
LAE ratio	26.6%	27.3%		0.7%
Loss and LAE ratio	100.6%	99.3%		-1.3%
UW expense ratio	31.5%	33.2%		1.7%
Combined ratio	132.1%	132.5%		0.4%

Numbers or ratios may not foot due to rounding.

Dash (-) represents a null value.

Zero (0) represents a calculated zero or number which rounds to zero

Green represents better than prior year.

Red represents worse than prior year.