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MARKET OUTLOOK and ECONOMIC UPDATE

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# Economic Conclusions

- The current recession is now the longest and deepest in the post-WWII period.
- Recent economic indicators such as manufacturing indices, housing starts and unemployment claims indicate we may have hit bottom.
- Cash for Clunkers and inventory re-stocking should lead to positive RGDP growth in Q3.
- Growth in Asia is picking up again, especially in China.
- However, secular forces (such as consumer deleveraging, taxes and re-regulation) are likely to make the shape and pace of this economic recovery sub par from a historical perspective.

## Workers Comp Market - 2008 Year In Review

- Changing regulatory issues and reforms are continuing to impact W/C markets and bringing volatility to pricing, loss costs, severity, and profitability.
- New income dropped 62% in 2008 for AM Best W/C Composite.
- Earnings impacted by both dislocations in the financial markets as well as sharply reduced premium volume.
- Net premiums written dropped to lowest level since 2000 and down 30% from high in 2004
- Calendar year Combined Ratios, after hitting a low of 98.5 in 2006, have risen to 103.6 and 104.4 in 2007 and 2008 respectively.
- Net premiums written fell for third consecutive year in 2008, declining 12%, far faster than 2% decrease in overall P/C industry.

## Workers Comp Market – Looking Ahead 2009-2010

- Rising levels of unemployment and shrinking payrolls will lead to lower levels of premiums.
- Market will remain soft as companies struggle to maintain market share and capital remains adequate
- Continued low levels of interest rates and investment income makes focus on underwriting even more important
- Rising medical costs above the rate of inflation will continue to be a challenge.
- Uncertain impact of national medical reform
- Many companies looking outside W/C for growth opportunities (i.e. Employment Practices Liability Insurance)
- On a positive note, reserves appear adequate and frequency will continue to decline as payrolls shrink.