Equity Research
North America

Industry

Insurance - Property-Casualty

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Industry Overview

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World Trade Center Special Issue

- **37 insurers have estimated $13.6 billion of total losses**
  Industry loss estimates now range as high as $40 billion (Munich Re). Most of the difference has been ceded to the reinsurance market, and has not been reported yet by individual insurers.
- **Reinsurance recoverables are a huge problem**
  We believe large swaths of the reinsurance market are likely insolvent. Uncollectible reinsurance is going to be a problem. Companies should be considering their gross, not net losses.
- **Lloyd's of London is in jeopardy**
  Already financially troubled, we believe the World Trade Center losses will sink some Lloyd's syndicates, drain Lloyd's Central Fund of cash, and exhaust Lloyd's insurance coverage.
- **We are maintaining our industry loss estimate**
  However, the revisions to its components suggest the high end of our $25-30 billion range is now more likely than the low end.
- **Congress is considering a bailout**
  This is a very bad idea for the financial health of the insurance industry, as we discuss in this report. Past examples of propping up weak financial institutions are not inspiring of confidence.

World Trade Center Special Issue

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Note from Research Management: All of us in Equity Research are struggling to come to terms with the horror of the terrorist attacks in the US. But there is some solace in returning to the challenges of our business and in trying to make sense of the changed world. It is not an easy thing to do, in human or professional terms. Nonetheless, our analysts are responding to client inquiries as best they can, under the circumstances, and on the basis of very preliminary information. We are distributing their provisional views in order to communicate with as many of our clients as we can, and to contribute to their understanding once equity markets resume trading. At this moment, however, the investment implications are, of course, subordinate to the human dimensions of this tragedy. We thank all our clients for their concerns and prayers.

Introduction

The World Trade Center attack is unquestionably the most significant event in the history of the insurance industry. Loss estimates are rising, with current estimates in some cases at the $40 billion level. The aggregate total will depend on the extent of governmental assistance to the insurance industry (which we ironically believe would ultimately be deleterious to the industry's financial health, for reasons discussed in this report).

In lieu of our regular weekly newsletter, *Insurance and Risk Briefing*, we are publishing this industry report, focusing on a number of issues that we believe will affect insurance stocks in the days and weeks ahead.

- Please see our separate report, "Earnings and Valuations – A Starting Point," being issued today, for a separate discussion of stock valuations and estimates.
- Although we have discussed non-US insurance stocks in this report, please refer to the work of Espen Nordhus, Rob Procter and Greg Thompson, our European and Canadian team, for more detailed research of the event and impact on their companies.
- For more information on the impact on the life sector, please see Nigel Dally's research.

People First

Among the missing we have been terribly saddened to see many fellow analysts, including Vita Marino and others of Sandler O'Neil, and our friends from Keefe, Bruyette & Woods: Research Director David Berry and analysts Jeffrey Bittner, Dean Eberling, David Graifman, Mary Lou Hague, Scott Johnson, Don Kauth, Russell Keene, Lindsay Morehouse, Marni Pont O'Doherty, Joe Roberto, Paul Sloan, Derek Statkevicus, Kevin Szocik, Tom Theurkauf, Greg Trost, and David Winton.

Some of the companies we followed also have suffered terrible losses. Our heartfelt condolences go especially to Marsh & McLennan and Aon for their hundreds of missing employees. Also missing is distinguished former New York Insurance Commissioner Neil Levin. There are others we have not yet learned the fate of, but whom we are praying for.

We were ecstatic, however, to learn of clients such as Michelle Meyer of Fiduciary Trust and all of the folks at Oppenheimer Management, Morgan Stanley Asset Management, and Salomon Asset Management (including, of course, our own former partner Greg Lapin), who are safe.

Remembering Northridge

In thinking about the World Trade Center attack losses, its a good idea to reflect briefly on the Northridge earthquake, which took place in January 1994, as a comparison.

- Early estimates of insured losses from Northridge were in something like the $2 billion range; the industry's losses subsequently quadrupled to more than $10 billion.
- Insurers initially put out quick, low estimates based on mathematical calculations of theoretical exposures that subsequently went through what seemed like an endless number of revisions after actual claims were received.
- Allstate's initial estimate for Northridge was, as we recall, in the low hundreds of millions and subsequently developed to nearly $2 billion. Allstate strengthened its Northridge earthquake reserves as recently as the second quarter of 2001. This pattern is not atypical.
- The stocks reacted sharply and negatively to Northridge immediately after the event. They continued to decline for months thereafter as losses were revised.
- Northridge was a straightforward, simple, and small event compared to the World Trade Center attack.

Reinsurance Recoverables – The Lake Wobegon Problem

The Problem: How can this be the largest workers compensation loss in history (by multiples), the most expensive aviation disaster in history (by multiples), one of the largest property losses in history, the most expensive business interruption in history (by multiples), the largest life insurance catastrophic loss in history (by multiples), and one of the largest potential liability claims in history – yet every one of the 36 major companies that have reported, representing the vast majority of market exposures, says it is going to come out of it financially A-OK, with little more than a bad quarter or year to report?

The answer: they can't – all the companies can't be above average. The sum of the losses has to add up to the total. Some of the numbers you are seeing reported by companies are likely significantly understated, mostly because they are *net of reinsurance recoverables* that in many cases will never be collected.

What do we mean by this? The implied amount ceded to reinsurers is large enough to bankrupt many reinsurers. Most of the gap between the total loss estimate that is developing by consensus ($30 billion or even higher) and the net losses reported by insurers ($13.6 billion) by implication has been ceded to reinsurers. A $25 billion loss to the reinsurance market (including losses separately reported by reinsurers), especially if weighted toward the Lloyd's market, as suggested by the property and aviation nature of this loss, would be fatal to more than a trivial segment of the reinsurance market. *And bankrupt reinsurers can't pay*.

Companies do not have to report their total gross estimates of a loss – the sum of the risks they have insured on which they will pay claims. Rather, they are allowed to offset anticipated recoveries from reinsurers against their loss payments, reporting the expected net liability. In reality, there is no *right of offset* against reinsurance. The insurer is primarily liable to its customer, and must pay even if its reinsurer does not pay.

In this situation, some companies have reinsured with blue chip reinsurers such as Berkshire Hathaway (General Re/Berkshire Re), Munich Re (and its US operation American Re), General Electric's Employers Re and Swiss Re. These companies will collect every penny they are owed. Many have reinsured with other relatively secure reinsurers (including those with well-capitalized parents that presumably will back their obligations), such as XL Capital, St. Paul Re, Hartford Re, CNA Re and ACE. These obligations we also consider secure, absent an "end of the world" scenario.

Still others have reinsured in the smaller or more leveraged broker markets, or other Lloyd's markets. The Lloyd's market in turn has partially reinsured internally, creating a possible "spiral" of risks in which reinsurers have reinsured each other, simply passing the hot potato around.

Inevitably, some of the reinsurers in this chain will be overleveraged. How do we know this?

- Eight small US insurers were bankrupted by Hurricane Andrew. The entire Australian reinsurance market was rendered insolvent by a series of catastrophes in the late 1990s. Whenever a very large loss occurs, somebody somewhere is nearly always overleveraged.
- For its part, this will be *by far* the largest reinsured loss in history and therefore almost by definition will not be an exception to the general rule of insurance overleverage.
- This is what in insurance is referred to as a "clash" event – in which multiple losses in different lines of coverage arise from the same underlying cause. Clash events are riskier for the reinsurance market as they give rise to claims from a variety of different customers under different types of policies, in a scenario outside of reinsurers' normal assessments of aggregate exposures.
- Clash events concentrate exposures (often in unpredictable, unusual, novel and thus, unanticipated, ways) in an industry where the predominant risk management strategy is actuarial diversification. When actuarial diversification fails – as it has in the WTC loss – capital takes the hit. While the industry remains overcapitalized, ironically, the excess capital primarily resides on the balance sheets of personal lines companies and the strongest reinsurers that are not overleveraged from a risk standpoint. Many other insurers would be undercapitalized if their reserves were marked to market.
- The reinsurance market has not recovered from its weak financial condition of the late 1990s. Pricing began to turn up only in 2000 and many insurers were counting on 2001 as the down payment on a return to normalcy. A huge hole has just been gouged out of companies' balance sheets. Some companies that would not have otherwise been toppled by a large catastrophe probably just can't afford this one given its timing.
- Tropical Storm Allison, asbestos, loss cost inflation, a string of reserve deficiencies and lower investment income already are pressuring insurer's balance sheets and earnings. This event simply may be the *coup de grace* for some companies.
- Reinsurance is a credit business – some reinsurers may now have balance sheets that look like those of

Japanese banks. We believe that customers will flee to the most secure carriers, further weakening the remaining companies by disrupting their premium cash flow.

We had already been hearing of requests for backup and replacement covers for smaller reinsurers, indicating the flight to quality was in full flow, before this event. We had commented with our European colleagues earlier this summer that investors should shift money in favor of the largest, strongest reinsurance stocks in favor of that trend. Now, we believe this loss is a recipe for disaster for overleveraged reinsurers. *We would call it close to a 100% probability that some reinsurers will fail and be unable to pay claims as a result of this event.*

Desperate reinsurers may try to 1) use coverage provisions such as the war exclusion to avoid their fate – although AIG's Hank Greenberg told us there would be dire consequences for anyone who tried this; 2) slow pay – we expect this; record-keeping problems by brokers will be a great excuse to drag out the cash flows; 3) cut loose subsidiary reinsurers they own that issued covers and let them fail – a one-time-only solution; you can't sponsor another reinsurer if you've let one sink, but the truly desperate may not care; 4) delay, delay, delay through arbitrations and other disputes over coverage language.

We strongly suspect at least one spiral will come to light at Lloyds and the untangling of reinsurance spirals is always a lengthy and messy affair. Meantime, the primary companies who issued the underlying policies must pay claims promptly; they have no choice.

Two key statistics to watch over the next few quarters: Cash flows and the buildup of gross reinsurance recoverables on the balance sheets of insurers. The presence of large recoverables should be cause for concerns about collectibility unless the insurer is one known to be fanatical about only doing business with secure reinsurers. AIG is an example of such a fanatical company.

What All This Means: The capacity of the reinsurance market worldwide to take risk, currently around $120 billion annually of premium, will shrink significantly – perhaps by one-third or even more. The shrinkage is a function not just of the losses – but of several other factors: 1) the perceived flight to quality and lack of faith in the credit-worthiness of lower-tier reinsurers; 2) underwriters' fear and greater recognition of higher risk factors will result in a lower willingness to assume and retain risk and greater allocations of capital to many types of risk; 3) fear of credit losses will cause buyers to shrink capacity allocated to some reinsurers and reduce their "approved lists"; 4) despite some commentary to the contrary, we believe the capital markets will not be willing to restore the industry's capital with the exception of the largest and strongest players because of demand shifts . The result is likely to be a winner-take-all scenario in which the largest reinsurers grab significant market share at much higher rates.

Exhibit 1

Top 25 Reinsurers

Rank	Company	Net Premiums
1	Munich Re	$14,974.80
2	Swiss Re	$13,790.40
3	Berkshire Hathaway	$13,540.00
4	Employers Re	$8,342.00
5	Hannover Re	$4,895.60
6	Gerling Global	$4,053.40
7	Lloyd's of London	$4,014.40
8	Generali	$3,951.90
9	Allianz Re	$3,726.50
10	Zurich Re	$3,065.80
11	SCOR Re	$2,754.20
12	London Re	$1,888.30
13	Transatlantic Holdings (AIG)	$1,658.60
14	AXA Re	$1,424.70
15	Reinsurance Group of America	$1,404.10
16	Lincoln Re	$1,383.50
17	PartnerRe Ltd.	$1,380.40
18	St. Paul Re	$1,251.50
19	Everest Re	$1,218.90
20	XL Capital	$1,022.20
21	QBE Insurance Group	$1,000.10
22	Toa Re	$952.40
23	CNA Re	$951.20
24	Korean Re	$901.80
25	Trenwick Group	$834.00
		$94,380.60

Source: Business Insurance, Standard & Poor's

Reinsurance and insurance pricing will rise significantly. This is not simply a function of reduced capacity: 1) the World Trade Center disaster has made underwriters aware of new types of risk and larger potential losses; 2) the standard deviation of loss appears wider than was previously being priced into insurance coverages, and that will now be reflected in pricing; 3) the amount of risk capital required to support insurance risks is greater than formerly understood; 4) the industry's liquidity needs also are greater than previously understood, a significant factor in an investing environment that only provides 3% returns on cash.

We aren't sure yet exactly where the cutoff is for the "largest reinsurers." There is no question that Berkshire

Hathaway, Swiss Re and Munich Re fall into this category. We believe that Employers Re, owned by General Electric, should also qualify. In the next tier are well capitalized broker markets, although buyers of reinsurance may demand security from the parent company (if a subsidiary) or letters of credit as collateral (increasing the reinsurers' capital costs) since some of these companies do business through subsidiaries around the world that could – theoretically – be disavowed, and reinsurance buyers are going to become ultra-cautious about this issue.

In general, we believe there may be nervousness in the market about placing certain types of new or renewal business in loss-affected lines (e.g., property facultative or risk excess, aviation) with companies that have been making strategic shifts or nonrenewing unprofitable types of reinsurance.

There are probably some other reinsurers that will wind up on the secure list: we don't mean this to be an exclusive list. But as a starting point, we know the "Big Three" – Munich, Swiss and Berkshire/General Re – are where buyers are going to head first, with Employers Re as the next stop. These companies will gain significant market share in a rising price environment.

A simple example: We estimate that Berkshire Hathaway and General Re combined will write around $12 billion in nonlife reinsurance premiums in 2001 and $2 billion in life/health reinsurance. We also estimate Berkshire's probable largest loss from this event at around $1.5 billion or roughly 11% of premiums. Looked at very simply therefore, a price increase of 11% on unchanged volume would recoup Berkshire's entire loss from the World Trade Center.

We expect Berkshire's volume to increase significantly – probably more than 25%. We expect rates to rise considerably more than 11%. Without trying to be overly precise, therefore, it's clear that the largest reinsurers should fare better as the flight to quality steers customers back to reinsurers who can, without question, pay claims.

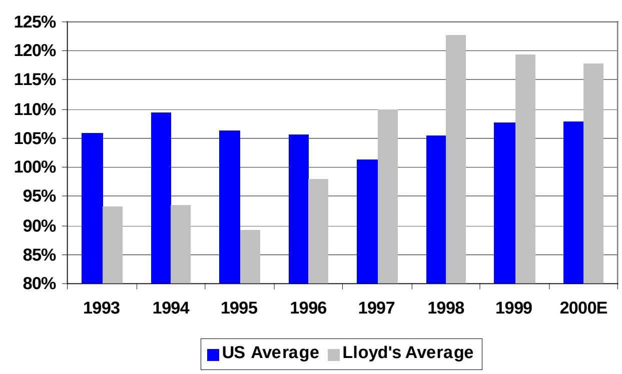
Lloyd's of London – Which Syndicates Will Survive?

Lloyd's of London, already in a precarious position, has been seriously jeopardized by the attack on the World Trade Center. Market losses have spiraled upward in recent years, and market participants were hoping that 2001 would turn the corner after a $1.04 billion loss in 2000, a $2.24 billion loss in 1999, and a $1.4 billion loss in 1998. Lloyd's is staggering from several large losses in recent years, including the Petrobras oil rig sinking (March 2001, $500 million of which Lloyd's paid approximately $200 million) and the September 1998 Swissair crash (previously the largest aviation loss in history at more than $1 billion, now dwarfed by the WTC aviation exposures which could total more than $4 billion). The WTC loss will certainly bring down several Lloyd's syndicates. The questions are:

- How many major Lloyd's syndicates may fail?
- To what degree will the Central Fund have to be tapped to cover claims?
- If the Central Fund is exhausted, as it most probably will be, will corporate capital sponsors, who now make up 80% of the market's capacity, support a levy on the market?
- Will corporate capital providers be willing to recapitalize insolvent syndicates? This decision will bear greatly on their willingness to support a levy.

Exhibit 2

Comparison of Avg. Lloyd's and US Combined Ratios



Source: CityPlace Research

Lloyd's syndicates were already in trouble going into this event. The average Lloyd's syndicate's underwriting performance since 1997 has been significantly worse than the US insurance industry, as shown in Exhibit 2. And results in 1998 included a £390 million reserve release that improved the market's result by approximately 22%.

At the end of 2000, reinsurance failures and uncollectible balances in the market were estimated at $295.6 million, primarily as a result of the collapse of the Australian reinsurance market, which had provided much of the world's retrocessional capacity in the late 1990s. To shore up the market, early in 2001 Lloyd's introduced a program to raise the market's standards and drive out underperforming syndicates. It was estimated that the bottom quartile of syndicates were dragging results so that eliminating that would have enabled the market to improve its results by more than 15 combined ratio points. Unfortunately, these actions may have been too late.

The recent liquidation of Independent Insurance Co. Ltd. is expected to add to the market's losses and place some Lloyd's marine syndicates in jeopardy. Directly as a result of the failure of Independent, the Cotesworth & Co. Ltd. managing agency suspended underwriting in its two syndicates 535 and 1688 recently following the liquidation in March 2001 of its corporate capital sponsor, HIH Insurance Ltd. of Australia. Cotesworth, which was founded in 1855, is one of the oldest Lloyd's agencies and had managed capacity of approximately $289 million writing energy, marine hull, liability, professional liability, medical malpractice, bankers bond and other lines. Cotesworth was sunk by a combination of losses from the Petrobras oil rig and uncollectible reinsurance from bankrupt Independent Insurance Co. Ltd. Marlborough Syndicate 62, part of the CGNU Group, also has been identified by Chatset, a Lloyd's market analyst, as in danger of failure due to its exposure to Independent. PXRE Group and Duncanson & Holt have ceased underwriting, while Markel, Chartwell Managing Agency (operated by Trenwick) and Crowe Underwriting reduced their Lloyd's underwriting capacities.

Current estimates suggest that approximately £150 ($167 US) of losses in the market are likely to go unpaid. Now comes the World Trade Center loss, to which many Lloyd's syndicates are exposed through aviation, workers' compensation, property reinsurance, whole account reinsurance, excess and umbrella casualty, life, disability, event covers, and other coverages. Lloyd's has a habit of reinsuring internally, creating reinsurance "spirals" among its members, and we'd bet a lot of money that at least one spiral comes to light as a result of the WTC loss.

It now appears inevitable that Lloyd's security will be tapped to cover uncollectible claims, and quite possible that Lloyd's security may be exhausted by those claims given the magnitude of the WTC loss.

Lloyd's Security: Lloyd's is a mutual market, with a market claims-paying rating that rests on backing by a chain of security to support syndicates that cannot pay claims. The structure of Lloyd's security is as follows:

Cash: At year-end 2000, the Central Fund had £323 million of cash. Theoretically, 46% of this available cash would be taken up already if Lloyd's Central Fund had to cover £150 million of potentially unpaid losses estimated to be already in the market (excluding any incremental losses from Cotesworth or others, and before considering the WTC losses). However, the Central Fund has a £100 million deductible before Lloyd's insurance kicks in. Therefore, we assume the first £100 million of the potential £150 million exposure would be paid by the Central Fund with the next £50 million and anything above that paid by insurance, up to the limit of the insurance.

Insurance: Lloyd's has insurance coverage, led by Swiss Re, covers $500 million (£350 million) in excess of the £100 million deductible in any one year, up to a limit of £500 million over the 5-year period of the contract, which ends December 31, 2003. The liability for this coverage is shared as shown in Exhibit 3. A glance at Exhibit 3 illustrates why we are so skeptical about many of the loss estimates reported by so many companies. Keep in mind that the Lloyd's Central Fund insurance is only one insurance policy issued by these companies among the many coverages they have exposed to the World Trade Center. We are doubtful whether a provision for responding to a loss from the Central Fund is included in any company's loss estimate at this point.

Exhibit 3

Central Insurance Fund

Insurer	Exposure	Share
Swiss Re	$163	32.50%
St. Paul	$100	20.00%
Employers Re	$100	20.00%
Hannover Re	$75	15.00%
XL Capital	$50	10.00%
Chubb	$13	2.50%
	$501	100.00%

Source: Lloyd's of London, $ millions

Contingent funds: After exhausting its insurance, Lloyd's reverts to a combination of cash and callable contingent capital, with cash totaling an estimated £235 million and callable capital of £316 million, either of which can drop down to replenish the £100 million deductible once it is exhausted.

Who's Who at Lloyd's: Exhibit 4 lists the largest syndicate managers at Lloyd's, along with a handful of other syndicate managers of interest to US investors. This exhibit shows the rank of the total syndicates managed by each agency for 1998; please note that ranks vary from year to year. In particular the Swissair crash in 1998 caused heavy losses to aviation syndicates, influencing their results.

Exhibits 7 - 59, at the end of this report, show the business mix of key syndicate managers of interest to US investors and their growth and profitability history, which may be helpful in gauging exposure to the World Trade Center disaster. Keep in mind that Lloyd's syndicates typically buy large amounts of reinsurance and often reinsure amongst themselves. It will be very difficult to assess the solvency of Lloyd's syndicates until more information is available.

Exhibit 4

Who's Who at Lloyd's

Group	Managing Agent	Capacity 2000, Pounds	Mkt Share	1997 P/(L) on Capacity	Rank (w/in 52 Synd.)	% of Corp. Capital
Limit	Limit Underwriting Limited	812,151,410	8.1%	1.1%	21	69.3%
Ace, RGB	Ace/RGB	609,989,048	6.1%	-27.5%	50	97.8%
Amlin	Amlin/Anderstein	537,953,201	5.3%	-1.6%	17	72.2%
XL Capital	Brockbank/Denham	524,517,743	5.2%	1.1% / -13.4%	19 / 43	69.8%
St. Paul's	St. Paul Syndicate Management	437,270,200	4.3%	N/A	N/A	78.3%
Cox	Cox Syndicate Management Ltd	433,284,188	4.3%	0.1%	26	82.6%
Wellington	Wellington Underwriting Agencies Ltd	430,003,123	4.3%	N/A	N/A	64.2%
SVB	SVB Syndicates ltd	393,496,598	3.9%	8.7%	3	74.8%
Hiscox	Hiscox Syndicates Ltd	360,353,325	3.6%	2.2%	15	67.2%
Markel	Octavian Syndicate Management Ltd	339,520,863	3.4%	-7.1%	36	93.3%
Kiln	RJ Kiln	311,466,954	3.1%	N/A	N/A	65.1%
CGU	Marlborough	285,774,057	2.8%	-0.4%	27	92.6%
Alleghany	Alleghany	275,000,000	2.7%	-2.6%	30	100.0%
Fairfax	Kingsmead/Newline	258,536,138	2.6%	-0.8%	28	79.9%
Berkshire Hathaway	D P Mann Limited	257,427,950	2.6%	N/A	N/A	60.1%
BRIT	Wren	257,314,845	2.6%	-3.9%	N/A	67.3%
Chaucer	Chaucer	254,147,743	2.5%	N/A	N/A	67.2%
Crowe	Crowe	235,980,482	2.3%	-20.1%	48	94.4%
Chartwell	Chartwell	232,902,199	2.3%	-15.2	44	99.6%
PXRE	Pxre Managing Agency Ltd	175,100,000	1.7%	-3.3%	31	100.0%
Liberty	Liberty	125,000,000	1.2%	1.0%	22	100.0%
QBE	QBE	94,225,062	0.9%	2.0%	16	100.0%
Munich Re	Apollo	85,000,000	0.8%	-2.4%	29	100.0%
Safeco	R F Bailey (Underwriting Agencies) Ltd	72,235,917	0.7%	N/A	N/A	51.9%
Gerling at Lloyd's	Gerling at Lloyd's	70,000,000	0.7%	10.1%	39	100.0%
CNA	CNA Underwriting Agencies Ltd	35,000,000	0.3%	-19.1%	47	100.0%
Total Market Capacity		**10,065,015,161**	78.5%			

Source: AM Best, Morgan Stanley Research

Losses Reported to Date

Exhibit 5 contains loss estimates updated for company announcements through 5 pm Sunday, September 16. We have made several assumptions in estimating numbers. First, we have estimated Berkshire Hathaway's loss as a percentage of the industry total based on its disclosure of typical ranges. Second, we have had to estimate tax rates for certain companies, which we expect to refine as we get more information.

- Unless we could confirm otherwise, for the Bermuda companies, we have generally assumed no tax when we believed their exposure is primarily from Bermuda-based catastrophe reinsurance. In some cases we were unable to confirm this but in others, we simply could not dial the phone fast enough on Friday to call everyone given the pace at which information is developing. We expect to refine most of our estimates for tax impacts this week.
- For ACE Limited, we are aware of certain onshore loss exposures, including its $200 million excess casualty exposure to the Silverstein risk (owner of WTC), its life reinsurance exposure, and its aviation exposure, that would give rise to tax benefits, and therefore have assumed a 20% tax rate.
- For XL Capital, we've likewise assumed a 20% tax rate, given its ownership of the former NAC Re, with its US casualty treaty book and clash reinsurance book, and its presence in the Lloyd's and aviation markets.
- PartnerRe Limited confirmed a 10-15% tax rate.
- For the Continental and UK insurers, we have assumed a 35% tax rate, which may be incorrect in some cases as tax rates in Europe are sometimes higher. A 5% increase in our estimate due to tax gross-up from this source would add $244 million to our total gross loss estimate, not a significant difference. In reality, we believe that many of these loss provisions were pre-tax. However, that is ambiguous, and it is more conservative to tax effect the number because that

results in a smaller difference between reported losses and the aggregate industry estimate.

Exhibit 5

Loss Estimates Reported to Date

		Loss Estimate		Percent of Total	
Company	**Euros**	**Low**	**High**	**Low**	**High**
Berkshire Hathaway		$900	$1,500	7.5%	11.1%
Lloyd's		$1,500	$1,500	12.5%	11.1%
Munich Re*	$1,000	$1,308	$1,385	10.9%	10.2%
Swiss Re**	$800	$1,186	$1,186	9.9%	8.7%
Allianz*		$969	$969	8.1%	7.1%
XL Capital		$750	$875	6.3%	6.4%
GE (Employers Re)		$600	$600	5.0%	4.4%
Hannover Re*		$554	$554	4.6%	4.1%
ACE Limited		$500	$500	4.2%	3.7%
AIG		$500	$500	4.2%	3.7%
MetLife		$385	$462	3.2%	3.4%
AXA		$126	$401	1.0%	3.0%
PartnerRe		$350	$400	2.9%	2.9%
Zurich Financial*		$400	$400	3.3%	2.9%
CNA (1)		$200	$350	1.7%	2.6%
SCOR		$231	$308	1.9%	2.3%
Royal & Sun Alliance*		$221	$221	1.8%	1.6%
Chubb (2)		$100	$200	0.8%	1.5%
White Mountains		$175	$175	1.5%	1.3%
Fairfax Fincl		$100	$125	0.8%	0.9%
Everest Re		$115	$115	1.0%	0.9%
Gerling Global*		$98	$98	0.8%	0.7%
Manulife*		$98	$98	0.8%	0.7%
Odyssey Re		$80	$80	0.7%	0.6%
CGNU*		$79	$79	0.7%	0.6%
Trenwick		$50	$75	0.4%	0.6%
IPC Holdings		$75	$75	0.6%	0.6%
Markel		$75	$75	0.6%	0.6%
Lincoln National (3)		$50	$50	0.4%	0.4%
Wellington*		$44	$44	0.4%	0.3%
RenaissanceRe		$36	$36	0.3%	0.3%
PXRE		$30	$35	0.3%	0.3%
HCC		$34	$34	0.3%	0.2%
WR Berkley		$25	$25	0.2%	0.2%
Unumprovident		$20	$20	0.2%	0.1%
Zenith		$7	$15	0.1%	0.1%
Ohio Casualty		$5	$7	0.0%	0.1%
Total		$11,976	$13,572	100.0%	100.0%

** Taxed at 35%   ** Taxed at 23%*

(1) Excludes liability, life and business interruption

(2) Excludes workers' compensation, A&H and business interruption

(3) Excludes individual and group life

Source: Company data, Morgan Stanley Research

We have several other observations about this table.

- As noted above, some companies have disclosed only part of their exposures. The parts not disclosed are more difficult to estimate and may have losses higher than the losses that have been disclosed.
- Early loss estimates are now out of date; significant new information has now been learned in the last few days.
- A handful of facts about some of the non-US insurers:
  1) Our European analysts have solvency concerns about Axa. Axa has high US primary life exposure.
  2) Allianz owns Fireman's Fund, a major US commercial lines writer.

3) CGNU is probably grateful it sold its US nonlife business to White Mountains last year.
4) Hannover Re is the world's fifth largest reinsurer and the largest aviation reinsurer. Hannover also owns Clarendon, a large US program writer with significant credit exposures to reinsurance. Irrespective of its losses we anticipate that Clarendon will struggle as reinsurers limit capacity and decline to support program business in favor of core clients.
5) Manulife writes life reinsurance and we believe has exposure through excess carve-out workers' compensation reinsurance.
6) Munich Re owns American Re, the third largest US reinsurer, a company whose exposures often resemble in nature those of Berkshire Hathaway's General Re.
7) 24% of Royal SunAlliance's business is US-based; its maximum loss is supposedly capped at $40 million.
8) Swiss Re owns a major North American reinsurer and is the world's largest life reinsurer.
9) Wellington manages the seventh largest syndicate capacity at Lloyd's, specializing in property and excess reinsurance.
10) Zurich Financial owns Zurich Insurance, one of the largest commercial property writers in the US and a major workers' compensation insurer, as well as the newly dubbed "Converium," a major broker market reinsurer. Our European analysts are concerned about Zurich due to its weak balance sheet.

- We continue to be *highly* skeptical about many of these estimates. Some of them are so low, given what we know about the businesses and exposures involved, they are simply not credible.
- Most estimates are net of reinsurance recoverables, and in some cases the recoverables may never be collected, as discussed previously.
- Many estimates were prepared and announced in haste. The European estimates were the first announced, in some cases within 24 hours, even though these reinsurers have among the most complex exposures of any companies imaginable. We question whether all relevant factors were adequately considered in these estimates. We have heard of insurers who were not aware they were on certain programs when they compiled their estimates and of European companies that did not discuss their estimates with their US operations before announcing a number. Certainly life

exposures could not have adequately been considered by companies that announced losses within 24 hours.

- Through no fault of the insurers, damaged properties were not inspected before releasing estimates (and still have not been). This will likely result in revisions.
- Reinsurers writing primarily excess-of-loss covers, which have limits to the amount the reinsurer will pay out, know their exposure to any one customer. Reinsurers writing uncapped proportional reinsurance have unlimited exposures to huge events. Proportional insurance is more popular in Europe and the broker markets, where it may be written with or without caps limiting exposures.
- Financial guarantee-type exposures such as exposure to Lloyd's Central Fund probably are not included in these estimates.
- Business interruption losses are notoriously difficult to estimate. The length of this business interruption, for downtown businesses especially, is not even known yet.
- While rates have risen over the past 18-24 months, many insurance policies still include broad coverage terms leftover from the soft market years. The flood losses in Houston are an excellent example of how unanticipated losses arise from such covered perils that were judged to be "remote" in a soft market and thrown into policies for free.

We have at least some information about specific claims, reinsurance programs and loss estimation practices that supports our view that many, if not most, of the loss estimates published so far should not be used for any serious purpose (such as estimating earnings, book values or valuations, much less for buying or selling stocks). Until companies are able to develop more realistic numbers, we assume the market will penalize the stocks of companies with estimates that are not credible.

Updated Total Industry Loss Estimate

On Sunday, September 16, Munich Re released a total loss estimate of $40 billion. That's not unreasonable considering potential business interruption exposures. We have updated our own estimate of the industry's total loss. After talking with a number of companies we are becoming more comfortable with our original estimate range of $25-30 billion, but continue to stress that it's just an estimate, there are lots of moving parts, and there will undoubtedly be changes. It's really too early to tell what the losses from this event will be. We are presenting an estimate simply because we've got to start somewhere.

What's included in our estimate: all losses originating in the nonlife industry, including workers' compensation losses even if subsequently reinsured to life companies (we don't have any way of knowing who the reinsurer may be). What's not included: life, annuity and disability exposures. Our life analyst, Nigel Dally, is estimating these.

We have made several revisions to the original assumptions underlying our total estimate. These revisions, taken together, push our total estimate from the lower end to the higher end of our $25-30 billion range:

- We had assumed a casualty number of 10,000, relying on early press reports of the number of missing persons. Fortunately the actual number has turned out to be more like 5,000, lowering our workers' compensation loss estimate significantly from $6 billion to $3 billion. By way of comparison, insurers paid out approximately $500 million in the 1993 World Trade Center bombing.
- We had originally assessed property damage outside the WTC at around $3 billion. We are now concerned this number is too low and are raising it to $5 billion. The value of 7 World Financial Center and other insured WFC properties is around $1 billion. We understand that Brookfield, owner of the World Financial Center and Liberty Plaza, has assured investors of the structural soundness of these buildings. However, we continue to believe, based on discussion with a number of insurers, that property and structural damage has occurred throughout lower Manhattan due to shock waves and debris that will result in a very costly cleanup and repair effort.
- We've raised our business interruption estimate to $8 billion. It could go *much, much* higher. Business interruption covers cost of moving to alternative locations, backup systems, lost profits (not revenues). *It would not cover the impact of an economic slowdown, however*. If we revise this number again, we may have to raise our overall estimate.
- We've added a new type of exposure – event cancellation & miscellaneous. Insurers cover concerts, athletic events and similar events against cancellations out of the control of the insured, and we expect that losses from this source will be high. We also suspect some other arcane coverages are going to come to light.

- We've reduced our casualty estimate slightly to $5 billion. If federal relief to the insurance industry is significant, we could reduce this number further. Liability is still the biggest wild card other than business interruption.

Exhibit 6

Updated Total Loss Estimate
A Scenario of Exposures $, MM

A Scenario of Exposures	$, MM
Property - towers One & Two	$3,300
Property - other	$5,000
Business interruption	$8,000
Workers compensation	$3,000
Event cancellation & misc.	$1,000
Aviation hull	$1,000
Liability - airlines	$3,000
Liability - other	$5,000
	$29,300

Source: Morgan Stanley Estimates

The Downside of "Double Leverage"

The reinsurance departments of primary insurance companies such as Hartford, St. Paul and CNA have long touted their "double leverage" advantage and 15% returns on undisclosed internally allocated equity numbers. By not capitalizing their reinsurance operations separately as a subsidiary, these companies are able to leverage their full capital bases to write reinsurance, using their main insurance subsidiary's claims-paying rating and attracting business to a larger capital base through greater financial security. From a business standpoint, this strategy is more flexible and enables these companies to compete more effectively with major reinsurers without committing large amounts of capital to dedicated subsidiaries. From our perspective, the negative has been that analysts have no way to independently assess the operating results or reserves of these operations, which has always caused us to view them more skeptically.

There is a downside to this double leverage, as the WTC loss now makes clear. The reinsurance losses from the risks written on the main insurance operation's balance sheet are going to sink a hole of some size, to be determined, in the balance sheets of the main insurers. Even assuming that none of these companies would cut loose an insolvent reinsurance subsidiary, which we believe is a fair assumption, the impact of the losses on the insurance balance sheet is not an academic issue – because from a rating perspective, a company's capital is not arrived at simply by adding up the sum of its subsidiaries' capital.

As a practical reality, an undercapitalized subsidiary is often granted the parent company's rating by tolerant rating agencies, whereas the main insurance subsidiary is held to a more critical standard. Thus, gouging a hole in the main insurance subsidiary's balance sheet has more serious consequences – for example, capital available for share repurchase may be affected more from these losses than had a stand-alone subsidiary taken the loss.

Insurance Demand – Replacement Value

Rising demand for property insurance – in fact for all types of insurance – is likely to be one of the consequences of the World Trade Center disaster. For example, the replacement cost of the two Towers is estimated at $5 billion, but they were insured for only $3.3 billion. We understand that the owner has claimed the disaster was two separate events, apparently in an attempt to tap two coverage limits and collect the full replacement cost. We don't think this will be successful. We do think property owners will take note of the perils of under-insurance.

In general, we believe the attack will increase risk aversion and therefore, unlike a normal market when prices rise, we do not expect as dramatic an increase in self-insurance and rising deductibles as would otherwise have occurred. Rather, we believe that buyers will rediscover the value of insurance, and be less reluctant to pay for what is, in fact, a very valuable product. This could be helpful to insurers who badly need to charge more economic pricing at a time when the outlook for the economy is not good. We can't quantify this, but we don't think rate increases next year will be nearly as hard to come by as they might have been.

This is not the way anyone would have chosen to prolong the hardening market, but our best guess is, that is what will happen.

Will the Alternative Market Replace Insurance?

One possible scenario in a hardening market is always that companies will choose to self-insure more and buy alternative forms of risk transfer, including finite structures. While we believe there will be some increased demands for these programs simply because of lack of capacity, we do not believe the alternative markets will be an adequate or even preferred substitute for insurance and reinsurance in the face of price increases for traditional risk transfer products.

The price hardening that is taking place now is not simply a function of lack of capacity and insurer resolve. The value of risk transfer has been clearly demonstrated by the attack on the World Trade Center. Demand for traditional risk transfer inevitably will rise. Alternative products are not a substitute for traditional risk transfer in that they do not transfer significant risk. Therefore, while we believe demand for both types of products will rise, we do not expect to see a vast expansion of self-insurance as a substitution for insurance.

A second consideration is the capacity of the alternative risk transfer market. Buyers were already finding a shrinking supply of captive management partners before the WTC disaster. A survey by the Captive Insurance Companies Association recently found that 75% of all captive fronting services are provided by just seven insurers: ACE Limited, AIG/Lexington, St. Paul's Discover Re, Liberty Mutual, Kemper, Old Republic and Zurich. Companies such as Mutual Risk Management also provide "rent-a-captives" for insureds that don't want to capitalize a permanent traditional captive.

How Insurers Could Achieve Stability

We believe there is a simple way insurers could make their loss estimates and financial statements much more credible and quickly stabilize their stock prices, as opposed to the volatility we are going to see over the next few weeks and months as individual company loss estimates are revised.

An insurer that voluntarily disclosed its gross, as well as net, losses from the disaster would go a long way toward helping investors understand its real exposures. Similarly, we consider a list of major reinsurance recoverables (receivables) from the event, and in total, to be a material and needed disclosure considering that collectibility of reinsurance recoverables is now in doubt.

We know that most insurers will not even consider disclosing such things, but any company that did would be a hero to its shareholders and would find the stability of its stock price reestablished straightaway. The fact that insurers will not disclose their gross losses should be considered indicative of how high those losses are. We note that Berkshire Hathaway is the one company that buys essentially no reinsurance and therefore, when it is able to release a loss estimate, gross losses can be considered equal to net and the company is exposed to essentially no credit risk.

Finally, instead of spending time on questionable ideas like discounting insurers' already understated claim reserves, we would prefer the SEC Chief Accountant's staff or FASB to instead address the inadequacy of insurance disclosures. Items like these would be high on our "wish list."

Rebuilding the WTC/Reoccupying the WFC – Maybe Not

We continue to wonder whether the World Financial Center in particular may be untenable as a commercial location for major financial companies in the future for structural, safety and psychological reasons. One possible scenario is that the west side of downtown will change dramatically, rather than resuming its former role as a vibrant financial center – as companies move elsewhere rather than force their employees to inhabit offices overlooking the site of the 1993 and 2001 terrorist attacks in the fairly isolated, exposed location that is now the WFC. We have already spoken with a few companies that are probably not going to return to the area, to avoid this unnecessary stress on their employees. We have also spoken with employees who don't want to go back. It's early, and people are emotionally in shock; still, we believe this will be an issue.

The debate over rebuilding on the site of WTC will be exhaustive; the only certainty is that nothing comparable in scale to the former Trade Center will ever be built on that site again. We believe the west side will find a purpose, just as important and meaningful as before – but it may not be as a money center.

Should There Be A Bailout?

This week Congressmen Mike Oxley of the Financial Institutions Committee and Bill Thomas of Ways and Means began crafting a proposal sponsored by industry trade groups to address the securities, bank and insurance implications of the disaster. We understand that provisions are extremely vague at this point, but the intent is to avert bankruptcy of major insurers in general as a result of claims from the attack. We have heard possible means to compensate insurers ranging from liquidity support by the Federal Reserve (which we support), federal excise tax relief (which would essentially only help primary companies that reinsure offshore, not reinsurers) to low cost long-term loans.

Before rushing headlong to bail out insolvent insurers, we would like to play devil's advocate and raise a few points.

There is a history of unsuccessful outcomes to ponder when Congress has interfered, with the best of intentions, to prop up insolvent financial institutions that got themselves in trouble through poor risk management. The savings and loan crisis comes to mind.

The problem with not allowing insolvent financial institutions to fail is the law of unintended consequences. As leveraged businesses that depend on sound risk management practices to operate successfully with other people's money, there is nothing more important in managing financial institutions that maintaining the correct alignment of incentives for management behavior.

Anytime managements are allowed to make bad risk management decisions and escape the consequences, a precedent is set and lessons are learned. In the case of insurance, two unfortunate consequences result: 1) customers learn not to discriminate – that is, pay for – the value of good risk management and strong ratings, driving down margins so that returns support only the lowest common denominator; 2) some managements learn there are no bad consequences for bad behavior, and take more risk, threatening the system and ultimately increasing costs to everyone.

The insurance business already suffers greatly from the fact that buyers do not discriminate adequately between companies with good and bad claims-paying ratings, and good and bad balance sheets. Now, a time has finally arrived in which the sheep and goats of the industry will be separated. It would be unfortunate if the sheep acquiesced with or even encouraged an effort by Congress to dress up the goats to look like sheep.

We have no doubt that some insurance companies will fail as a result of the WTC attack. These may be companies that were already weak financially and have overleveraged their reinsurance recoverables, have done business with lower-quality reinsurers who can't pay, or that have simply accumulated intolerably high loss exposures from the event. We don't believe major companies are at risk, however. Therefore, we hope that in considering any bailout proposal, Congress will enact it only if truly needed by the industry, with a threshold approach that triggers assistance only if the industry as a whole (not simply weak individual companies) is faltering.

Now that the cycle has finally turned upward, the last thing the insurance industry needs is to have the capital of its weakest, least successful players restored through fiat of Congress so that they can rejoin the poker game with a fresh pile of chips.

A hypothetical question for Dean O'Hare, Doug Leatherdale, Sandy Weill, Jack Byrne, Larry Tisch – even if Congressional relief would help you – do you *really* want Congress to bail out your weakest competitor?

A Roundup of the News and Miscellaneous Items

China/WTO – The Best of All Outcomes for AIG: We said not to worry, and in fact it turned out to be the best of all outcomes for AIG. WTO negotiators have agreed to honor AIG's 100%-ownership rights to operate and expand in China, clearing the way for the country's membership. Negotiators had postponed a meeting on Thursday in Geneva because of the World Trade Center tragedy, but reconvened Friday. European negotiators had insisted that European insurers be granted the same sole ownership rights as AIG enjoys. In the meeting that concluded at 1 a.m. Friday Geneva time, however, that dispute was resolved, leaving intact the 50% ownership limit on European insurers entering the Chinese market as well as AIG's asymmetrical full-ownership rights. After China becomes a WTO member – expected to take effect early next year – European insurers can use the WTO dispute-resolution process to challenge the 50% limit.

We had always assumed the US would not yield on AIG's terms, but did consider it possible that China would extend those terms to European companies. However, not only does this agreement preserve AIG's freedom to operate without having to take on domestic partners, it preserves the uniqueness of AIG's deal relative to future foreign competition in China, at least for now. In effect, this ratifies AIG's head start and extends it for however long it takes European insurers to prevail, if ever, in their efforts to gain parity. We should note that AIG would have supported a 100% ownership provision for the European companies and won't be troubled if that's what the dispute resolution process ultimately brings. It is unclear how successful these companies could be without a local partner – and going it alone, owning 100% of nothing is worth nothing, so AIG doesn't really lose anything either way.

As a WTO member, China becomes an even more desirable market, with domestic-driven growth potential enhanced by the further opening of international trade. We estimate AIG's premium volume in China – life and nonlife combined – will total about $360 million for 2001, still only about 1.5% of AIG's total premium revenue, but growing

20% per year. The company has filed applications to open in eight more Chinese cities. It is currently operating in four cities – Shanghai, Guongzhou, Shenzhen and Foshan – where it has been training agents brought in from those other cities to be ready to open for business as soon as licenses are granted. We will be considering how this latest development might change our thinking about the timing and extent of AIG’s growth prospects in China. However, it should be noted that our assumptions essentially were already in line with what has occurred.

SEC Share Repurchase Amnesty: The SEC announced an amnesty on share repurchases that would otherwise be prohibited. Companies can buy back without following limits on how many shares they can buy, restrictions forbidding buybacks at the beginning or end of a trading day, or restrictions based on pooling accounting rules, allowing companies to begin buying back stock on Monday for a five-day window. This is the first time the SEC has used its emergency authority to temporarily change its rules.

AIG Announces 40-Million Share Repurchase Program: AIG, which had just completed its acquisition of American General Corporation in what is likely to be one of the last large pooling transactions, announced a 40-million share repurchase program valued at up to $3 billion a last week’s close, as permitted under the SEC’s amnesty program. This repurchase is in addition to a 10 million share authorization already in place. AIG is down 25% year-to-date. The company has announced one of the smaller loss estimates from the WTC disaster; we think its $500 million provision is one of the more credible estimates considering AIG’s very low net retentions after reinsurance, its fanaticism about reinsurance security, and its preferred status as a reinsurance buyer, which ensures it is first in line to get paid. It’s hard to predict how the stock will open Monday but we tend to think it will emerge as a safe haven fairly quickly.

Gordon Gekko Would Be So Proud: In an audacious and unbelievable move that we can only call the ultimate in insider trading, Osama bin Laden, apparently taking a cue from Gordon Gekko in “Wall Street,” the movie, seems to have decided to finance his alleged Attack on America by picking the pockets of world investors through shorting insurance stocks and trading futures. Cagily choosing stocks of international reinsurers and operating through the Japanese market rather than the US (perhaps thinking to avoid scrutiny by the SEC), bin Laden reportedly may have shorted Axa, Swiss Re and Munich Re in the last few days before the attack. We hope its not too late for these trades to be DK’d. Undoubtedly, any suspicion that bin Laden may have profited financially from his alleged terrorism is only going to add to the outrage already being expressed over this event.

Congress Addresses Potential Airline Bankruptcies: On Thursday Congressional leaders began drafting legislation to limit liability claims from non-passengers and class actions against airlines related to the World Trade Center attacks in order to protect American and United Airlines against potential bankruptcy, which is widely expected as a result of judgments for such claims unless legislative action is taken. Senator John McCain, senior Republican on the Commerce, Science, and Transportation Committee, commented that the airlines wanted overly broad protection (of course) and would not get it (of course) but Congress appears, appropriately, committed to not allowing an “act of war” to destroy the domestic aviation industry even though victims need to be compensated.

The chairman of a House aviation subcommittee, Rep. John Mica (R., Fla.), said some of the aid being discussed would go to insurance companies that indemnify the airlines. We believe this would be a serious mistake, as discussed above in “Should There Be a Bailout?” We hope that Congress allows the law of supply and demand to restore the industry to health, without killing off the recovery through a bailout. Rep. Mica apparently does not understand that most aviation risks are reinsured overseas, and therefore theoretically the main beneficiaries of any such relief would be Lloyd’s of London and European reinsurers.

In its eagerness to show it is “doing something” for constituents, Congress would also do well to remember that, unlike airlines, insurers are fundamentally in the risk-taking business. However unprecedented the size of the loss, insurers deal with “hundred year storms” all the time, and assessing the risk of this very type of event is part of their day-to-day activity. Rushing in to rescue insurers before the industry has even settled on a total loss estimate is simply premature.

Another Footnote in History: GE Misses General Electric will miss quarterly earnings consensus expectations for the first time in many years as a result of its $400 million loss from the World Trade Center disaster. GE will come up about four cents short of Wall Street’s $0.37 consensus.

From Our “Amazing Stories” File: We were surprised to learn that Aon’s Ken LeStrange faxed a letter to insurers the day after the attack asking them to renew all treaties of Aon clients at expiring pricing in consideration of the firm's destroyed paperwork and 200 missing employees. Requesting a thirty-day extension at a negotiable price and assistance in reconstructing files would be reasonable, but asking insurers to stop raising rates after years of losing money we find surprising.

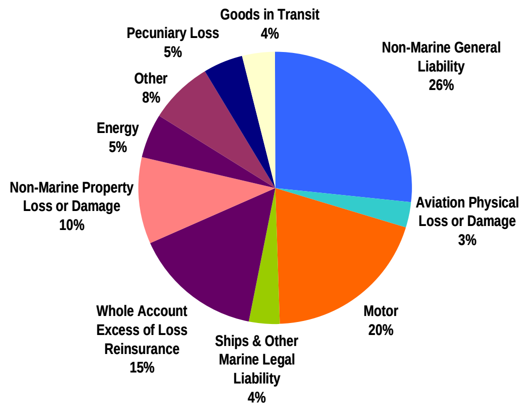
Warren Buffett's a Buyer: Berkshire Hathaway CEO Warren Buffett told 60 Minutes on Sunday night he has an offer outstanding for an acquisition, which he expected to be accepted, and doesn't plan to renegotiate in light of the World Trade Center attack. He also questioned whether a bailout of the airlines is necessary and said at certain prices he might be a buyer of stocks when the market opens on Monday, but would not be a seller.

Quote of the Week: "Since stocks are valued at levels that are rich by historical standards – an indication of investors' collective belief that nothing can go wrong – some panic may actually be prudent." David Schiff, September 14, 2001.

Prices and rating of companies mentioned in this report as of September 10, 2001. ACE Limited (ACE, $33, Outperform), AIG (AIG, $74, Strong Buy), Berkshire Hathaway (BRK, $68,000, Outperform), Hartford Financial (HIG, $62, Neutral), XL Capital (XL, $82, Strong Buy), CAN Financial (CNA, $28, not rated), Chubb (CB, $66, Outperform), Markel Corp. (MKL, $189, not rated), Philadelphia Cons. (PHLY, $30, Neutral), St. Paul Cos. (SPC, $41, Neutral), W.R. Berkley (BER, $39, Strong Buy), Allstate (ALL, $34, Neutral), Mercury General (MCY, $38, Neutral), Progressive (PGR, $124, Neutral), SAFECO (SAFC, $30, Strong Buy), Everest Re (RE, $62, Outperform), IPC Holdings (IPCR, $24, Outperform), Max Re Capital (MXRE, $14, Strong Buy), Odyssey Re Holdings (ORH, $16, not rated), Partner Re (PRE, $74, Outperform), Renaissance Re (RNR, $74, Outperform), Transatlantic Hldgs (TRH, $72, not rated), Trenwick (TWK, $14, not rated), Aon Corp. (AOC, $37, Outperform), Arthur J. Gallagher (AJG, $26, Outperform), Marsh & McLennan (MMC, $87, Neutral), Willis Group Hldgs (WSH, $18, Neutral), Ambac Inc. (ABK, $$57, Neutral), MBIA (MBI, $53, Neutral) CNA Financial Corp (CNA, Not Rated, $27.69), General Electric (GE, Strong Buy, $39.35), HCC Insurance Holdings (HCC, Not Rated, $24.50), Ohio Casualty (OCAS, Note Rated, $12.79), Lincoln National (LNC, Neutral, $48.05), MetLife (MET, Neutral, $28.50), PXRE (PXT, Not Rated, $17.45), UNUMProvident (UNM, Outperform, $27.07), White Mountains (WTM, Not Rated, $360.00), Zenith National (ZNT, Not Rated, $29.09).

Exhibit 7

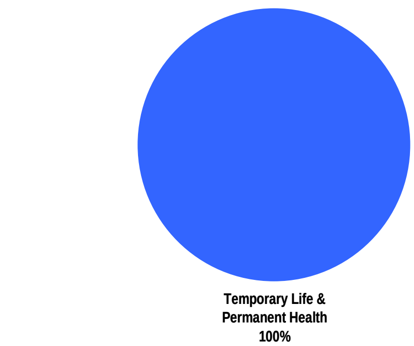
Limit Underwriting Limited
2000 Lines of Business Mix



Source: AM Best, Morgan Stanley Research

Exhibit 9

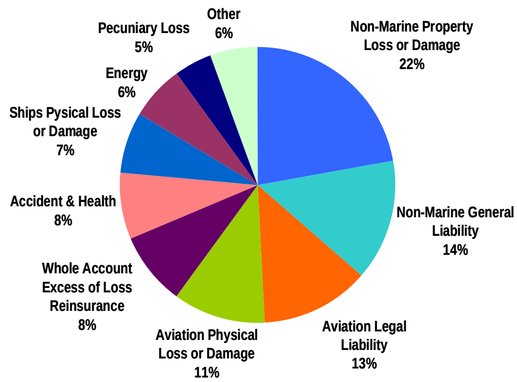
Ace (RGB) Agencies Ltd
2000 Lines of Business Mix



Source: AM Best, Morgan Stanley Research

Exhibit 8

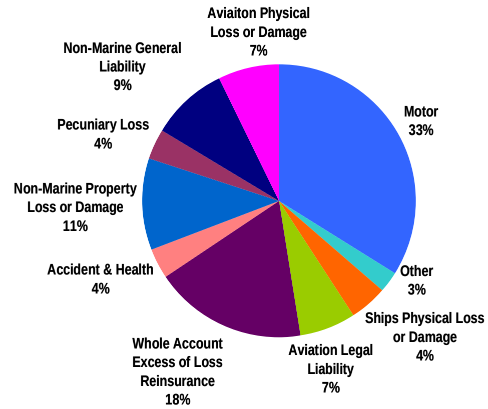
Ace Underwriting Agencies Ltd
2000 Lines of Business Mix



Source: AM Best, Morgan Stanley Research

Exhibit 10

Amlin Underwriting Limited
2000 Lines of Business Mix

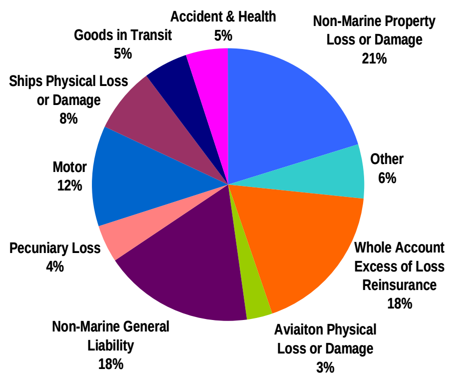


Source: AM Best, Morgan Stanley Research

Please see the important disclosures at the end of this report.

Exhibit 11

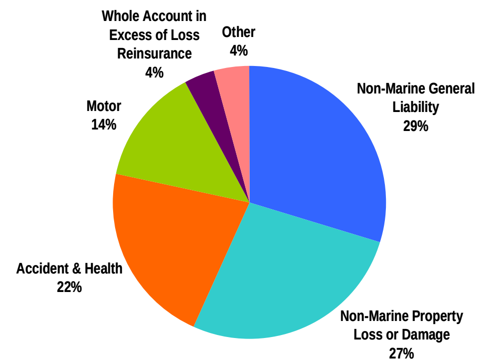
Angerstein Underwriting Limited
2000 Lines of Business Mix



Source: AM Best, Morgan Stanley Research

Exhibit 13

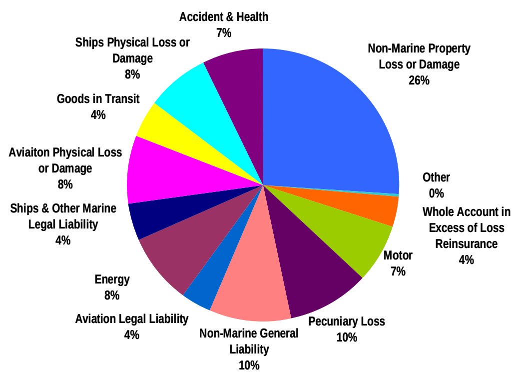
Denham Syndicate Management Ltd
2000 Lines of Business Mix



Source: AM Best, Morgan Stanley Research

Exhibit 12

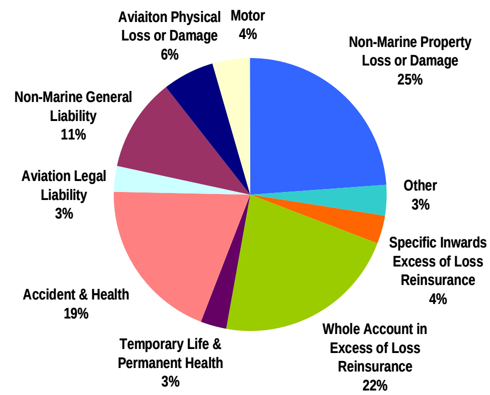
Brockbank Syndicate Management Ltd
2000 Lines of Business Mix



Source: AM Best, Morgan Stanley Research

Exhibit 14

St. Paul Syndicate Management Ltd
2000 Lines of Business Mix

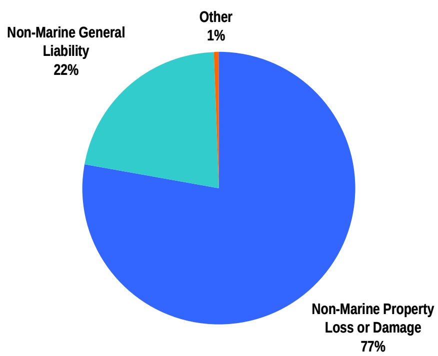


Source: AM Best, Morgan Stanley Research

Please see the important disclosures at the end of this report.

Exhibit 15

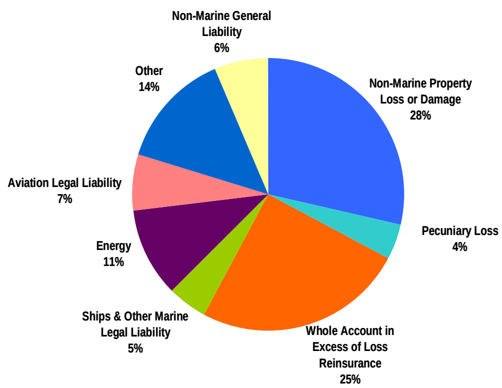
Cox Syndicate Management Ltd
2000 Lines of Business Mix



Source: AM Best, Morgan Stanley Research

Exhibit 16

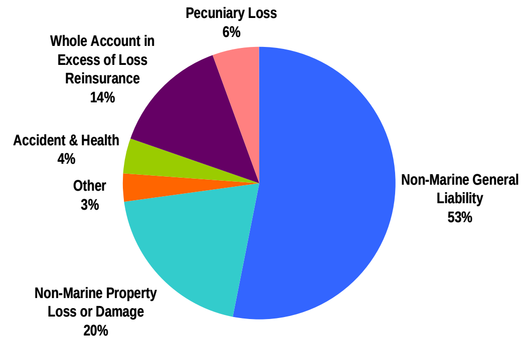
Wellington Underwriting Agencies Ltd
2000 Lines of Business Mix



Source: AM Best, Morgan Stanley Research

Exhibit 17

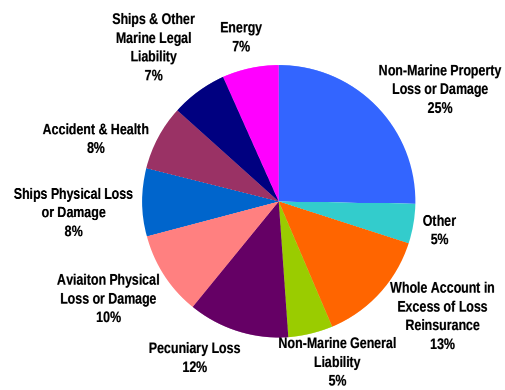
SVB Syndicates Ltd
2000 Lines of Business Mix



Source: AM Best, Morgan Stanley Research

Exhibit 18

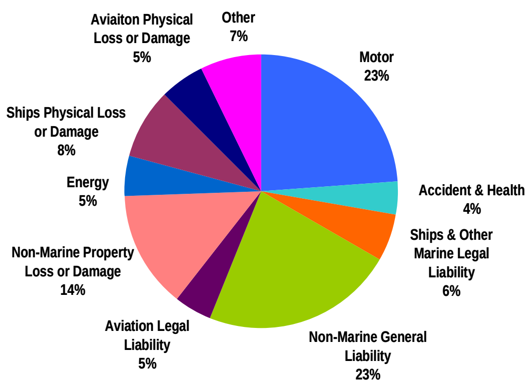
Hiscox Syndicates Ltd
2000 Lines of Business Mix



Source: AM Best, Morgan Stanley Research

Exhibit 19

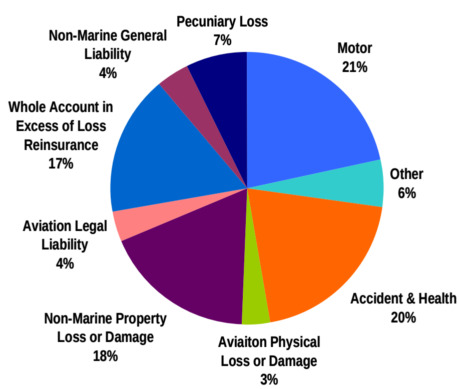
Markel Syndicate Mgmt Ltd
2000 Lines of Business Mix



Source: AM Best, Morgan Stanley Research

Exhibit 20

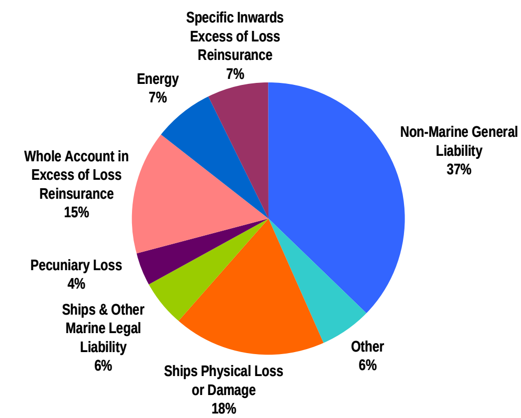
RJ Kiln & Company Ltd
2000 Lines of Business Mix



Source: AM Best, Morgan Stanley Research

Exhibit 21

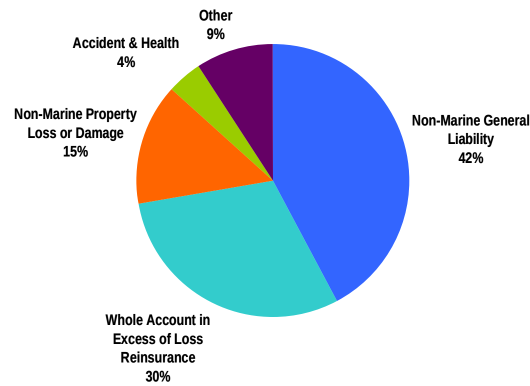
Marlborough Underwriting Agency Ltd
2000 Lines of Business Mix



Source: AM Best, Morgan Stanley Research

Exhibit 22

Alleghany Underwriting Ltd
2000 Lines of Business Mix

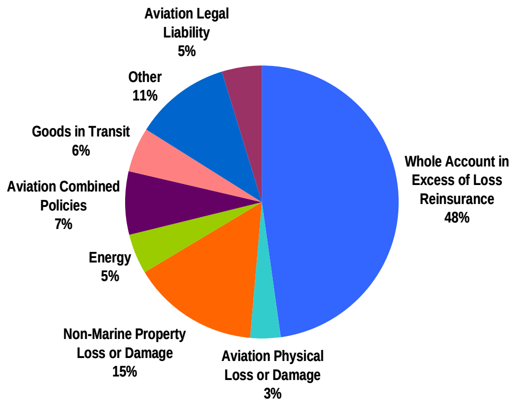


Source: AM Best, Morgan Stanley Research

Please see the important disclosures at the end of this report.

Exhibit 23

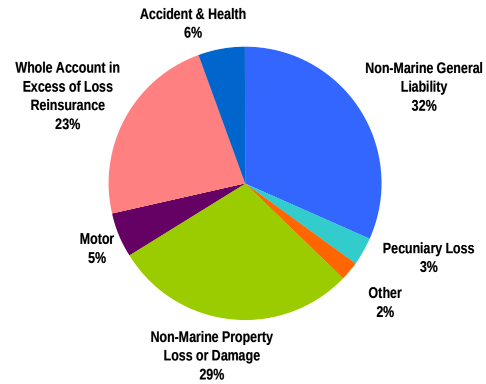
Kingsmead Underwriting Agency Ltd
2000 Lines of Business Mix



Source: AM Best, Morgan Stanley Research

Exhibit 25

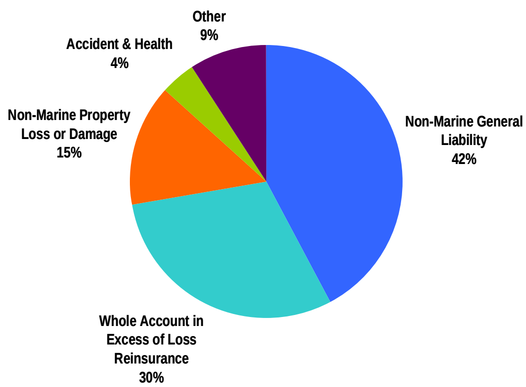
D P Mann Ltd
2000 Lines of Business Mix



Source: AM Best, Morgan Stanley Research

Exhibit 24

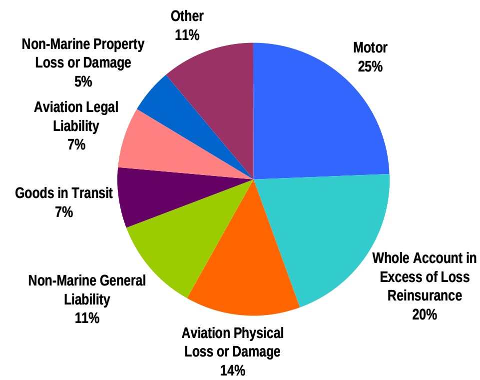
Newline Underwriting Management Ltd
2000 Lines of Business Mix



Source: AM Best, Morgan Stanley Research

Exhibit 26

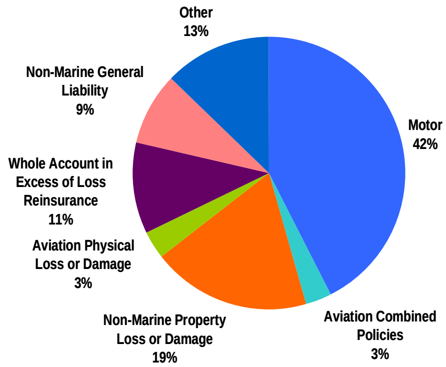
Wren Syndicates Management Ltd
2000 Lines of Business Mix



Source: AM Best, Morgan Stanley Research

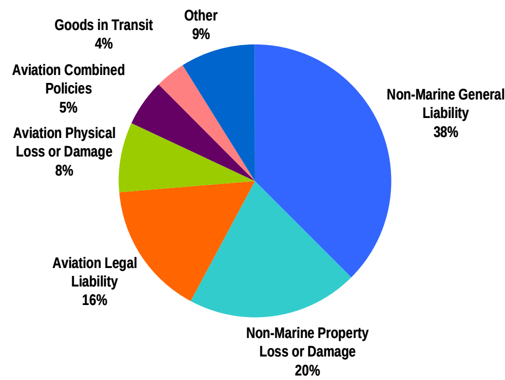
Please see the important disclosures at the end of this report.

Exhibit 27
Chaucer Syndicates Ltd
2000 Lines of Business Mix



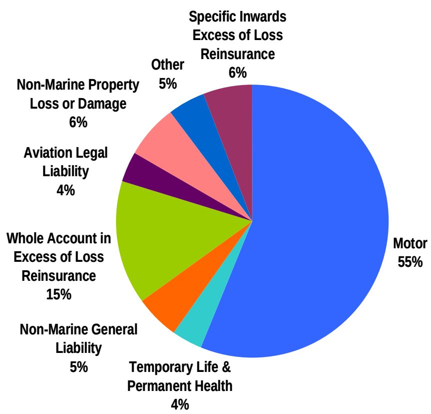
Source: AM Best, Morgan Stanley Research

Exhibit 29
Chartwell Managing Agents Ltd
2000 Lines of Business Mix



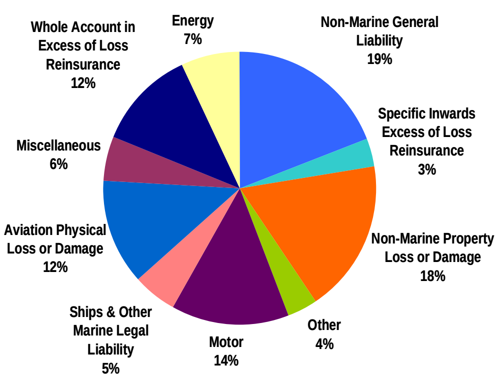
Source: AM Best, Morgan Stanley Research

Exhibit 28
Crowe Dedicated Limited
2000 Lines of Business Mix



Source: AM Best, Morgan Stanley Research

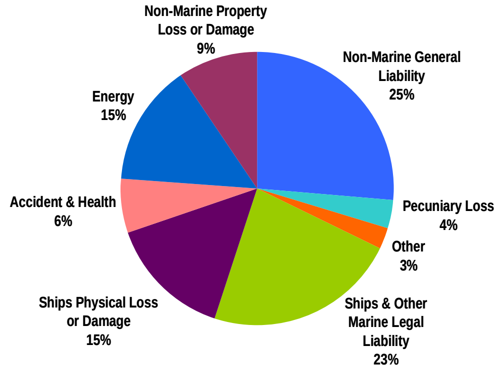
Exhibit 30
Liberty Syndicate Management
1998 Lines of Business Mix



Source: AM Best, Morgan Stanley Research

Exhibit 31

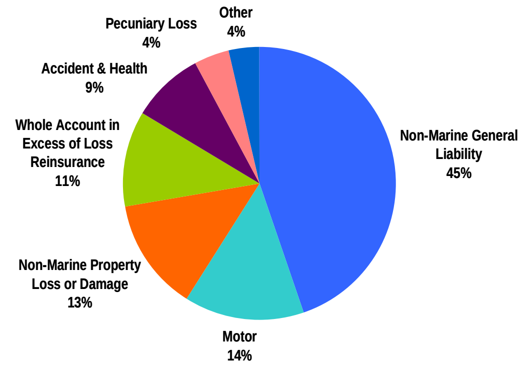
QBE Underwriting Agency Ltd
2000 Lines of Business Mix



Source: AM Best, Morgan Stanley Research

Exhibit 33

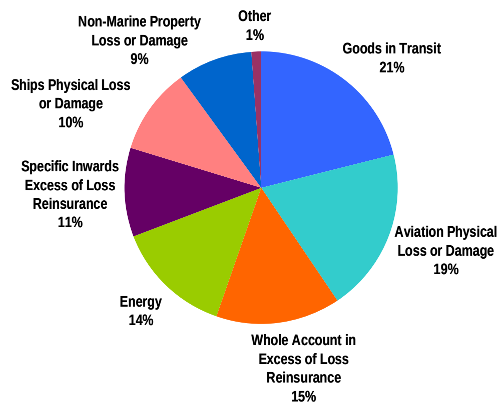
R F Bailey (Underwriting Agencies) Ltd
2000 Lines of Business Mix



Source: AM Best, Morgan Stanley Research

Exhibit 32

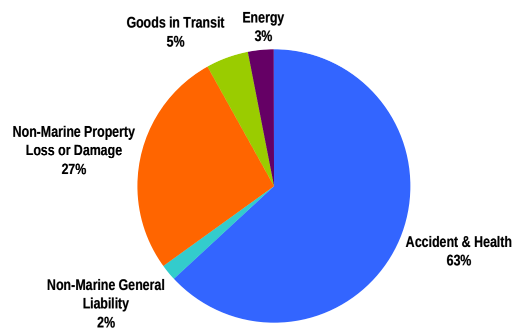
Apollo Underwriting Ltd
2000 Lines of Business Mix



Source: AM Best, Morgan Stanley Research

Exhibit 34

Gerling at Lloyd's Ltd
2000 Lines of Business Mix

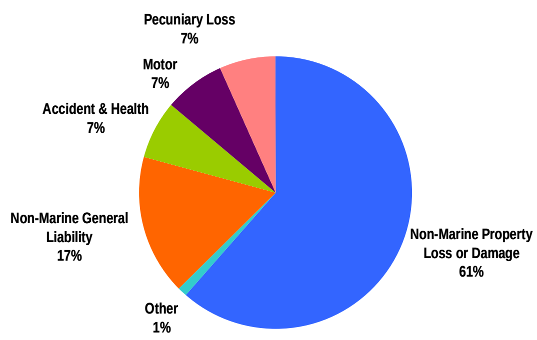


Source: AM Best, Morgan Stanley Research

Exhibit 35

CNA

2000 Lines of Business Mix

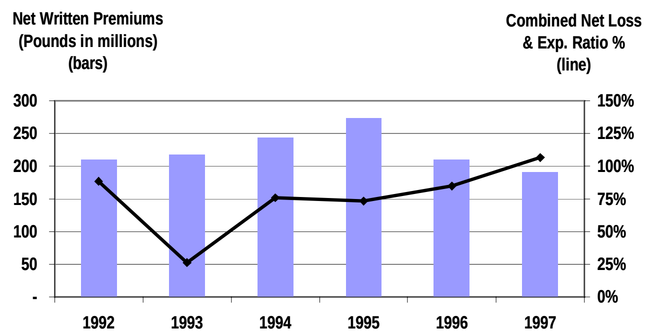


Source: AM Best, Morgan Stanley Research

Exhibit 36

Limit Underwriting Limited

Performance, 1992-1997

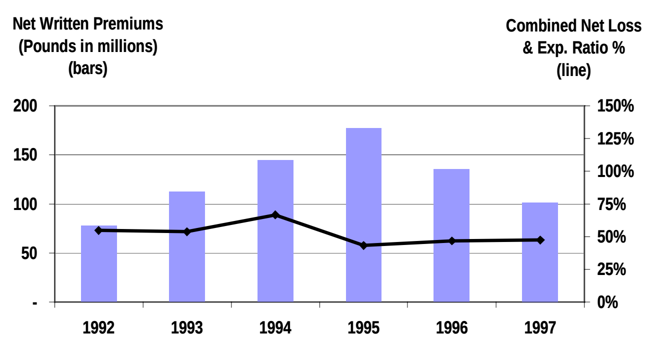


Source: AM Best, Morgan Stanley Research

Exhibit 37

Ace Underwriting Agencies Ltd

Performance, 1992-1997

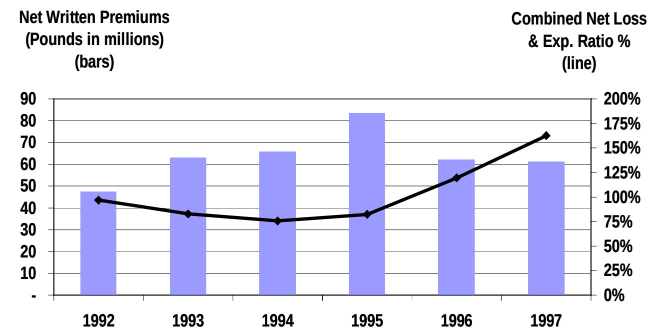


Source: AM Best, Morgan Stanley Research

Exhibit 38

Ace (RGB) Agencies Ltd

Performance, 1992-1997

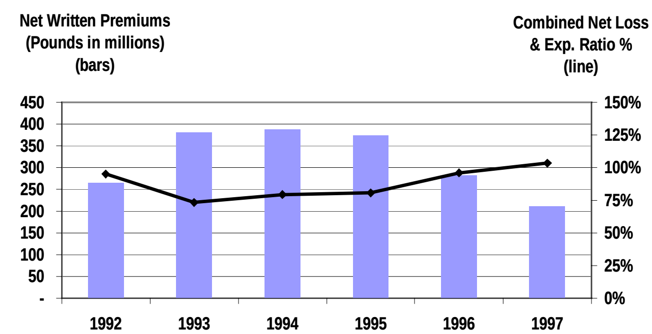


Source: AM Best, Morgan Stanley Research

Exhibit 39

Amlin Underwriting Limited

Performance, 1992-1997

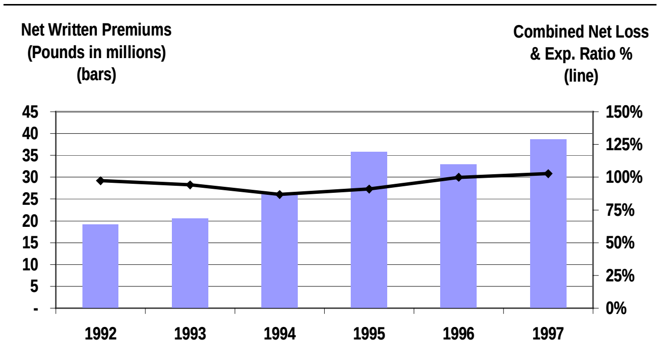


Source: AM Best, Morgan Stanley Research

Exhibit 40

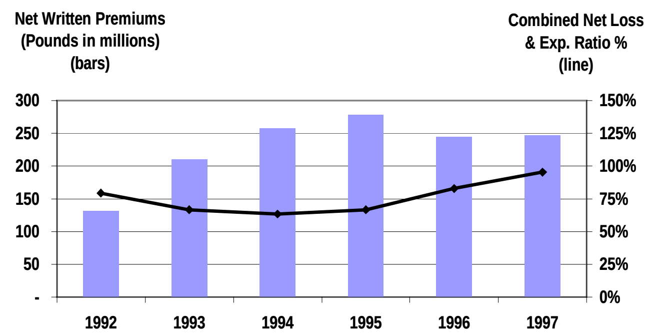
Angerstein Underwriting Limited

Performance, 1992-1997



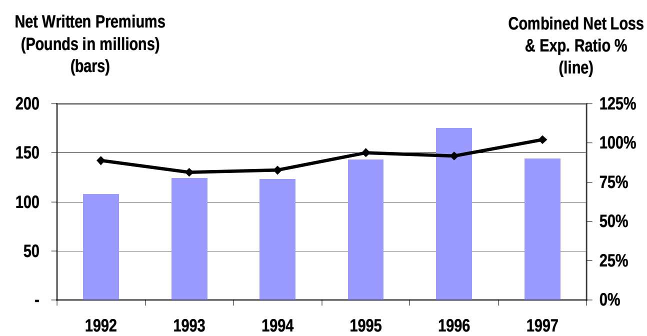
Source: AM Best, Morgan Stanley Research

Exhibit 41
Brockbank Syndicate Management Ltd
Performance, 1992-1997



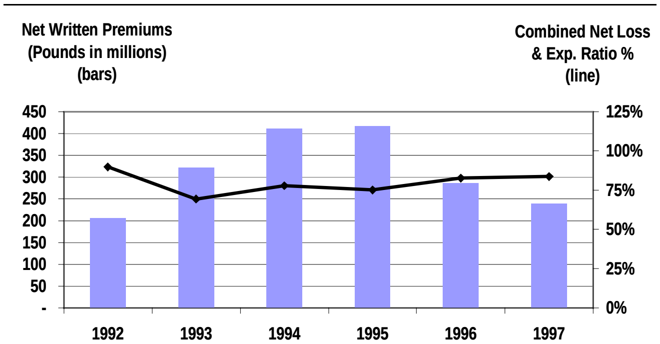
Source: AM Best, Morgan Stanley Research

Exhibit 42
Cox Syndicate Management Ltd
Performance, 1992-1997



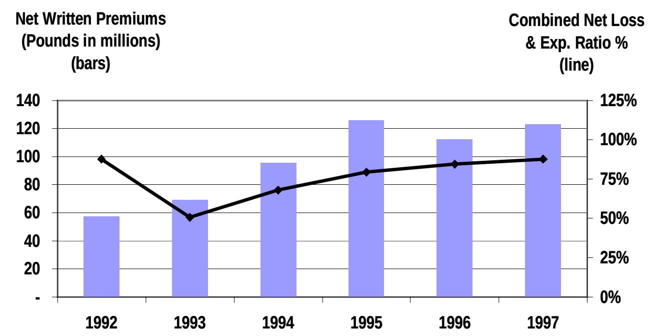
Source: AM Best, Morgan Stanley Research

Exhibit 43
Wellington Underwriting Agencies Ltd
Performance, 1992-1997



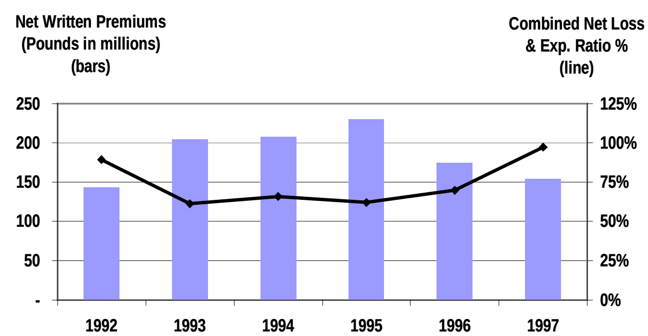
Source: AM Best, Morgan Stanley Research

Exhibit 44
SVB Syndicates Ltd
Performance, 1992-1997



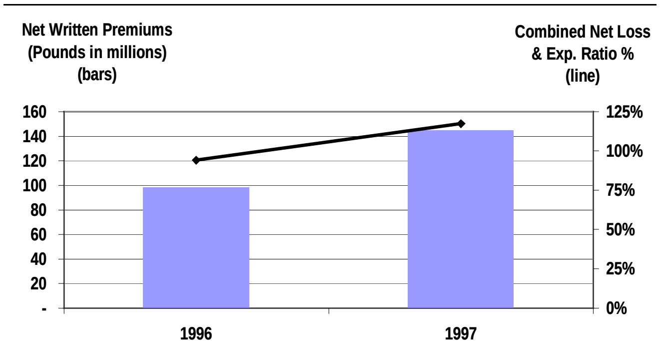
Source: AM Best, Morgan Stanley Research

Exhibit 45
Hiscox Syndicates Ltd
Performance, 1992-1997



Source: AM Best, Morgan Stanley Research

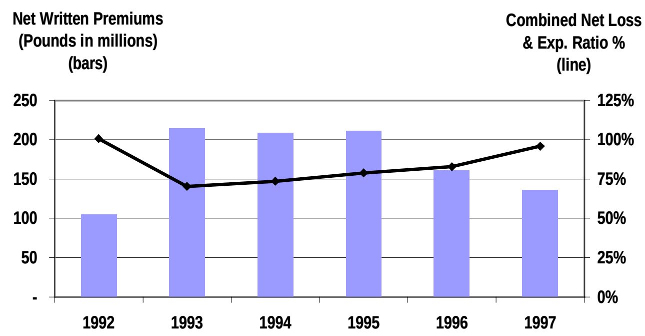
Exhibit 46
Markel Syndicate Mgmt Ltd
Performance, 1996-1997



Source: AM Best, Morgan Stanley Research

Exhibit 47

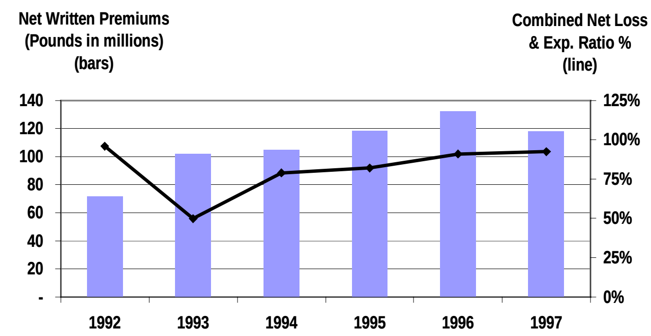
RJ Kiln & Company Ltd
Performance, 1992-1997



Source: AM Best, Morgan Stanley Research

Exhibit 50

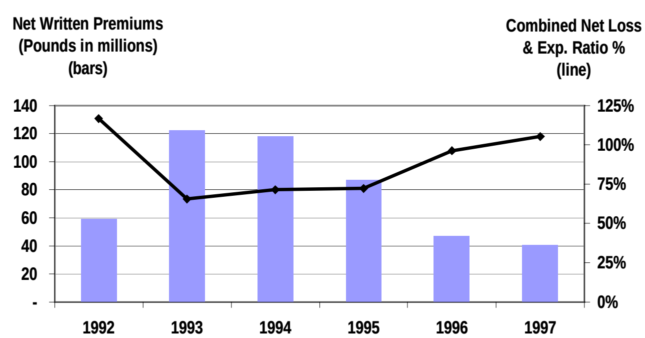
D P Mann Ltd
Performance, 1992-1997



Source: AM Best, Morgan Stanley Research

Exhibit 48

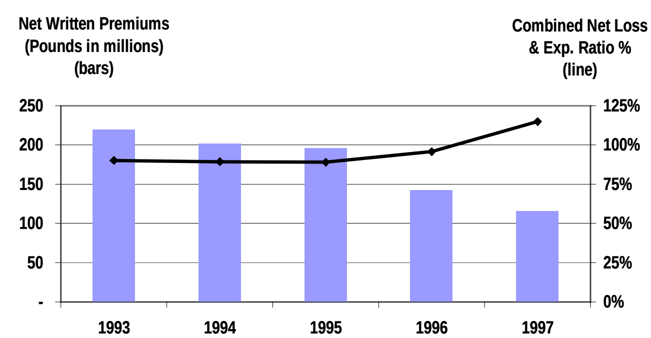
Marlborough Underwriting Agency Ltd
Performance, 1992-1997



Source: AM Best, Morgan Stanley Research

Exhibit 51

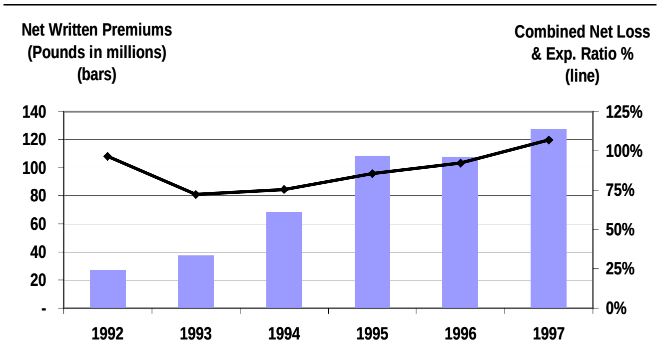
Wren Syndicates Management Ltd
Performance, 1993-1997



Source: AM Best, Morgan Stanley Research

Exhibit 49

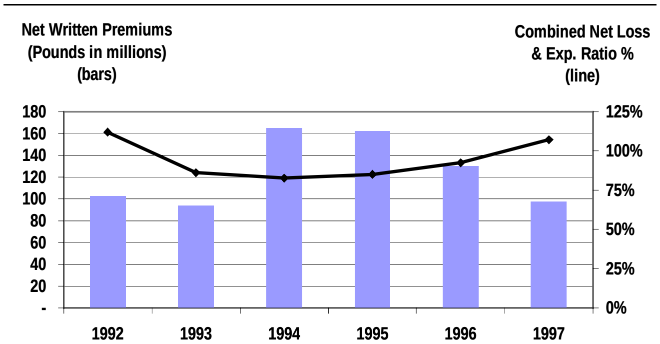
Alleghany Underwriting Ltd
Performance, 1992-1997



Source: AM Best, Morgan Stanley Research

Exhibit 52

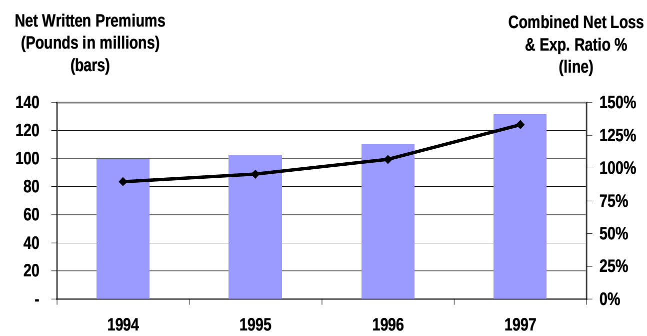
Chaucer Syndicates Ltd
Performance, 1992-1997



Source: AM Best, Morgan Stanley Research

Exhibit 53

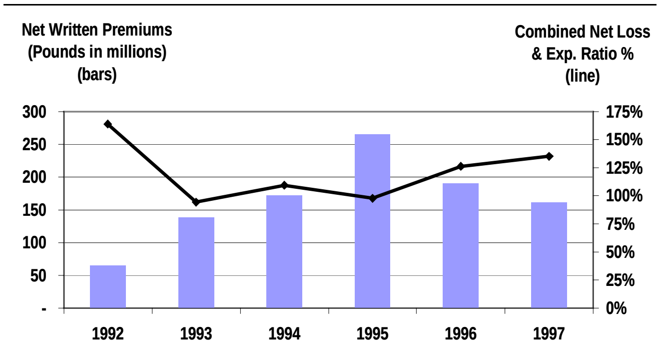
Crowe Dedicated Limited
Performance, 1994-1997



Source: AM Best, Morgan Stanley Research

Exhibit 54

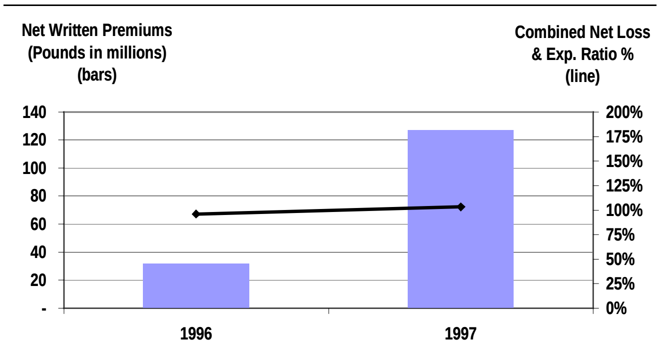
Chartwell Managing Agents Ltd
Performance, 1992-1997



Source: AM Best, Morgan Stanley Research

Exhibit 55

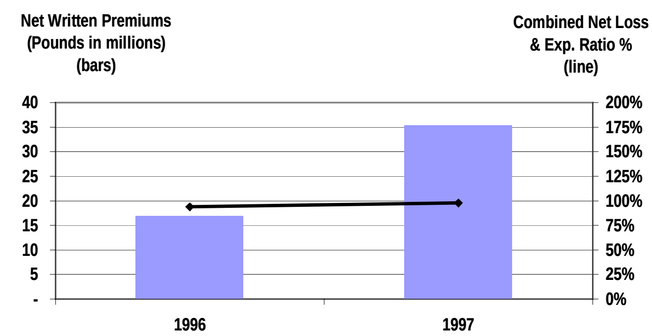
Liberty Syndicate Management
Performance, 1996-1997



Source: AM Best, Morgan Stanley Research

Exhibit 56

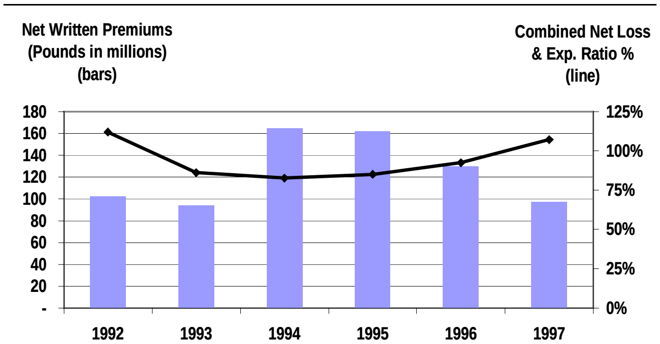
QBE Underwriting Agency Ltd
Performance, 1996-1997



Source: AM Best, Morgan Stanley Research

Exhibit 57

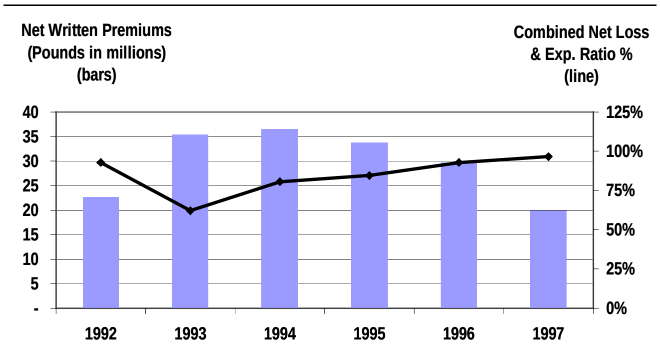
Apollo Underwriting Ltd
Performance, 1992-1997



Source: AM Best, Morgan Stanley Research

Exhibit 58

R F Bailey (Underwriting Agencies) Ltd
Performance, 1992-1997

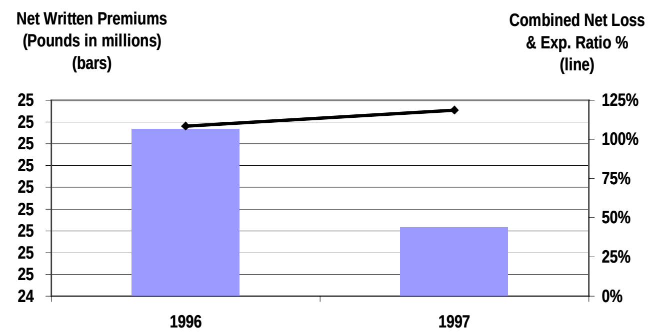


Source: AM Best, Morgan Stanley Research

Please see the important disclosures at the end of this report.

Exhibit 59

Gerling at Lloyd's Ltd
Performance, 1996-1997



Source: AM Best, Morgan Stanley Research

V = More volatile. We estimate that this stock has more than a 25% chance of a price move (up or down) of more than 25% in a month, based on a quantitative assessment of historical data, or in the analyst's view, it is likely to become materially more volatile over the next 1-12 months compared with the past three years. Stocks with less than one year of trading history are automatically rated as more volatile (unless otherwise noted). We note that securities that we do not currently consider "volatile" can still perform in that manner.

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