EMERSON, REID'S
INSURANCE OBSERVER

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A Change of Heart

We generally like to start each newsletter with a little item about us. You know the sort of thing we're talking about—a reference to our reputation as the world's greatest DBL general agency or something along those lines. Well frankly, that type of shameless promotion gets embarrassing after a while, so we're going to skip it for this issue.

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What's Up Doc?

What gives with the insurance business and the stock market? Insurance stocks chalked up sizable gains the day after the earthquake in San Francisco, as investors speculated that this tragic event—coming so soon after Hurricane Hugo—would finally shock underwriters into raising rates. But let's examine this a little closer. AIG's stock, for example, was up more than two points the day after the quake. Since AIG has 163 million shares outstanding, that means investors felt it was worth about $350 million more post-quake than pre-quake.

Of course that's Wall Street for you. We can readily understand why investors (and insurance brokers) would be glad to see our industry pull out of the vicious underwriting cycle it has been in. But that brings up a very important question. Have we really been in a vicious underwriting cycle? Let's take a look at the earnings of some of the larger insurers and you be the judge. AIG's earnings per share increased 28% in 1988 and an estimated 22% this year. CNA, GEICO, General Re, Hartford Steam Boiler, Progressive, Safeco and others have also shown nice gains. Although Chubb won't be recording much of an increase this year, they should still net over $350 million. Considering that they only made $10 million in 1985, that's quite a turnaround. And Value Line's Property-Casualty Composite showed $1.5 billion in profits this year versus a $97 million loss in 1985. Even Lloyd's of London's after-tax return on investment for 1986—the most recent year for which results are available—was 6.5%. While that's rather paltry, it still beats the returns registered by many savings and loans.

Perhaps the proper question is: If things are so bad why do they look so good? Sure, we know that the industry is probably underreserving, but what's new about that? Let's also not forget that the stock and bond markets have rallied mightily in the Roaring Eighties, fattening the insurance company coffers in the process. Those who pay attention to such things will remember that many insurance company bond portfolios were so far underwater in the early eighties that their net worth and surplus would have been wiped out had they been forced to mark their bonds to market.

Things have been getting tougher for the brokers, though, if one uses the publicly held ones as a benchmark. Earnings at Marsh & McLennan have been flat for three years, and Alexander & Alexander's earnings per share peaked way back in 1980. Unfortunately, it has been our experience that insurance rates don't rise just because brokers' profits are being squeezed. [We wish they would though.—Ed]

We believe the bitter truth is that insurance—for the most part—is a commodity, and like most commodity businesses, it is prone to harsh cycles. Since the demand for insurance doesn't vary that much from year-to-year, it is the supply side of the equation that is relevant. Underwriters are still caught in a vortex of excessive capital and too much capacity. Until that capital is whittled down it seems unlikely that rates will rise significantly, or that insurance companies overall will enjoy high returns on equity. We don't enjoy being bearers of bad news, but we just don't think the recent disasters portend an increase in rates. Far from it.

We don't know when or why rates will finally turn up, but we do have one heartfelt conviction. It will take a lot longer than everyone thinks it will.

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Goodbye New Jersey, Hello Iowa

For the year ended 1986 New Jersey led all states with the highest average automobile insurance premium—$603.55—followed by Alaska, California and Massachusetts.

For those looking for a bargain, we suggest moving to Iowa. The average premium there is only $243.95.

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"The Gunner" Stumbles

Poor Gunner. Since we last chatted with him he's run into some problems. It seems that the new business he wrote last year didn't turn out quite the way he expected. "How'd I know that our loss ratio would be 157?%," he sobbed, downing his second martini.

"But Gunner, didn't you review the loss history?"

"You know Duke, I meant to. I really did. But we were writing so much premium so quickly, I guess I just got a little carried away. Anyway, I've always said that underwriting is an art, not a science. And the money we saved on actuaries just about covered the cost of my Mercedes with the car phone."

"Interesting way of looking at things Gunner. By the way, how many times do we have to tell you to stop calling us Duke."

The Gunner was chain smoking Camels as he finished his story. ". . . so we've been losing business like crazy. And since we let our secretary and claims staff go things have really been piling up. Everybody's mad at me." He took a deep breath and gave me his best salesman's smile. "You know, our company's for sale, if you're interested. In many ways it's a gem, Duke. But even if you don't want it, I'm sure some Japanese insurance company will pay a big price for us. . ."

Sayonara, honorable Gunner.

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The Big Boys

The insurance brokerage industry is increasingly dominated by giants, as a recent Business Insurance Top 20 ranking attests. Marsh & Mc's $2.3 billion in revenues is greater than that of all the firms ranked between 20 and 100 combined. There are those who remember a time—it wasn't all that long ago—when even the largest firms weren't all that big.

Of course size is no guarantee of success, nor is it necessarily a cause for failure. We are pleased to count as friends a number of hardy folks who've made their way through the alphabet houses and lived to tell about it.

One thing is certain. To a client, an insurance brokerage is only as good as the person handling his account.

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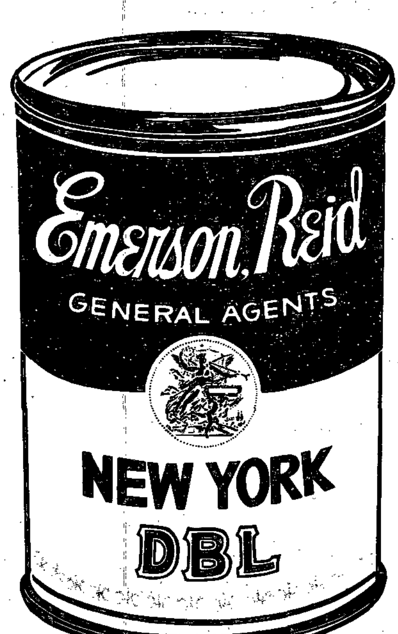

The Emerson, Reid Soup Can

"What's the meaning of this?" We've been asked that repeatedly since the soup can began appearing in our ads and mailings. "What's it all about? Is it a reference to the convenience of dealing with Emerson, Reid? Was it really painted by Andy Warhol? Is it a pun? Is it a comment on the duality of human nature? (Not too many people asked that last question.) Does DBL really come in cans?"

An art critic friend of ours wrote: "The juxtaposition of the pop imagery with the commercial iconography of the Emerson, Reid name creates a dynamic harmony rich in textural subtones." Although we don't know what he's talking about, it sure sounds impressive.

By the way, we'd be curious to find out what you think of the Emerson, Reid Soup Can, so write us a letter or give David Schiff a call.

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Any Comments?

We welcome your comments or letters. Also, if you have something interesting to write about—the sort of thing that one doesn't see in the mainstream insurance press—try it out on us.

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Some Worthwhile Reading

The self-improvement market is a huge one, which is probably why bookstores are loaded with volumes that purport to teach the reader how to effortlessly climb the corporate ladder. Whether it's *In Search of Excellence, The Ten Minute Manager* or *All I Really Need To Know I Learned In Kindergarten*, the reader is led to believe that the secrets of success are simple and can be learned in a short time—say, over the weekend. Sure.

Being the skeptical sort, it's our belief that experience—and mistakes in particular—are an excellent teacher. That's why we enjoyed *How To Lose $100,000,000 And Other Valuable Advice* by Royal Little.

Little, who is best known as the "father of conglomerates" and as the founder of Textron, Narragansett Capital, Amtel, Indian Head and American Television & Communications, died recently, just seven years shy of his hundredth birthday. Although easily one of the most innovative and successful businessmen of his generation, he chose to focus on the many mistakes he made over his long career. That's one of the great charms about this well-written book, because quite frankly, we're sick and tired of reading ghostwritten books by self-important, big shot blowhard

CEO's who recount how they made millions selling razors, chocolate chip cookies or just about anything else.

Unfortunately, Little's book, which was published in 1979, seems to be out of print. However, if any of our clients are unable to locate a copy we just may be able to help you out.

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Take My January Renewals; Please

We're not kidding about this. Due to the recent benefit increase, there's going to be a lot of DBL activity at year end, so it makes more sense than ever to get an early start on the process and give Emerson, Reid a call right away. As we have pointed out in the past, no one insurance company can come through for you all the time, so you can't afford to limit yourself to a handful of carriers. That's why you need us. We give brokers access to more than fifteen DBL markets.

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DBL Rate Stabilization Program

We think this is an interesting approach to take for larger insureds (over $25,000 in premium) who have had reasonable claims experience. Give us a call and we'll tell you more about our ideas.

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Take Advantage Of Payroll Rates For Under 50 Lives

As many of you are undoubtedly aware, most insurance companies discontinued payroll rates for small DBL accounts. While this is no big deal in the grand scheme of the universe, it has posed a slight hardship for companies with part time, seasonal or low paid help, such as restaurants, resorts, camps, etc. We are pleased to report that we have a market than can give us payroll rates for less than 50 lives. Call us.

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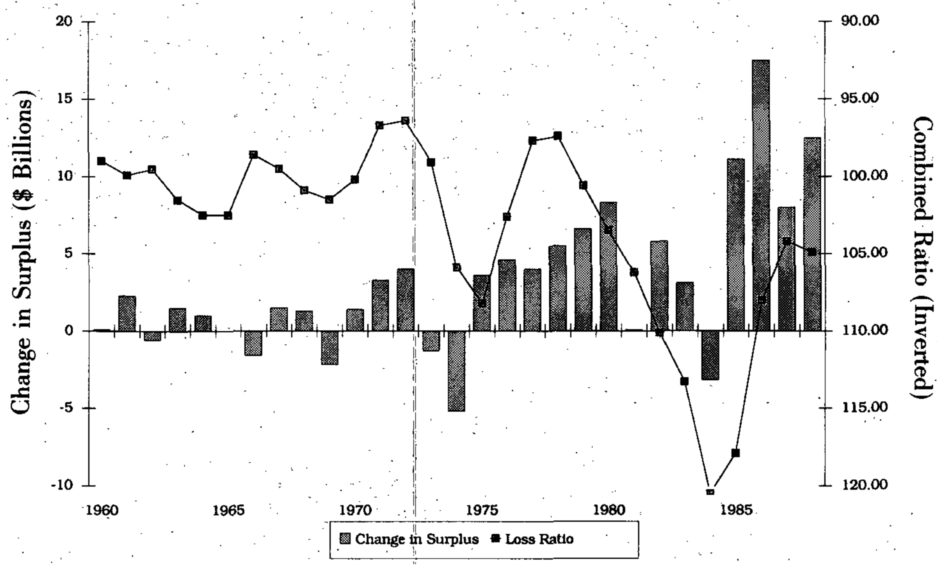
Change In Surplus and Combined Ratios

Here's an interesting graph. On the left is the insurance industry's annual dollar change in surplus. On the right is an inverted scale of the industry's combined loss ratio. Note that surplus doesn't usually begin to decline until the combined ratio heads somewhere south of 110%. It's only when surplus declines—in other words, capital is impaired—that underwriters usually come to their senses and start to get around to raising premiums.

Goldman Sachs projects that the combined ratio will be 109% this year, 110.5% next year and 114% in 1991. At that point, surplus will decline and rates should start to turn back up.



Source: Best's Aggregates

New Jersey TDB—Get your clients out of the State Fund

Unlike New York, where most of the DBL is written with private insurance carriers, most of the TDB (Temporary Disability Benefits Law) in New Jersey is written through the State Fund. This need not be the case. Emerson, Reid has a number of very competitive markets that are actively seeking TDB.

In case you need a refresher in TDB, here it is: The New Jersey Temporary Disability Benefits Law requires employers in New Jersey to provide Short Term Disability benefits to their eligible employees who are unable to work because of an off-the-job injury or sickness.

The benefit in the state of New Jersey is $66\frac{2}{3}\%$ of the average weekly wage to a maximum of $261 per week. TDB is rated on an annual wage base, with the employer paying a rate as a percentage of the first $13,900 of annual earnings.

Benefits begin on the eighth day of disability for both accident and sickness and there is a 26 week duration. If an employee is disabled for three consecutive weeks following the waiting period benefits are retroactive to the first day of disability.

Got it?

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Travel Accident

We do so much DBL business that our clients sometimes forget we can do a great job with Travel Accident. That's too bad—for us and for them. So from now on, think of Emerson, Reid for all your Travel Accident accounts. Give Mark Wintjen a call and he'll take care of you.

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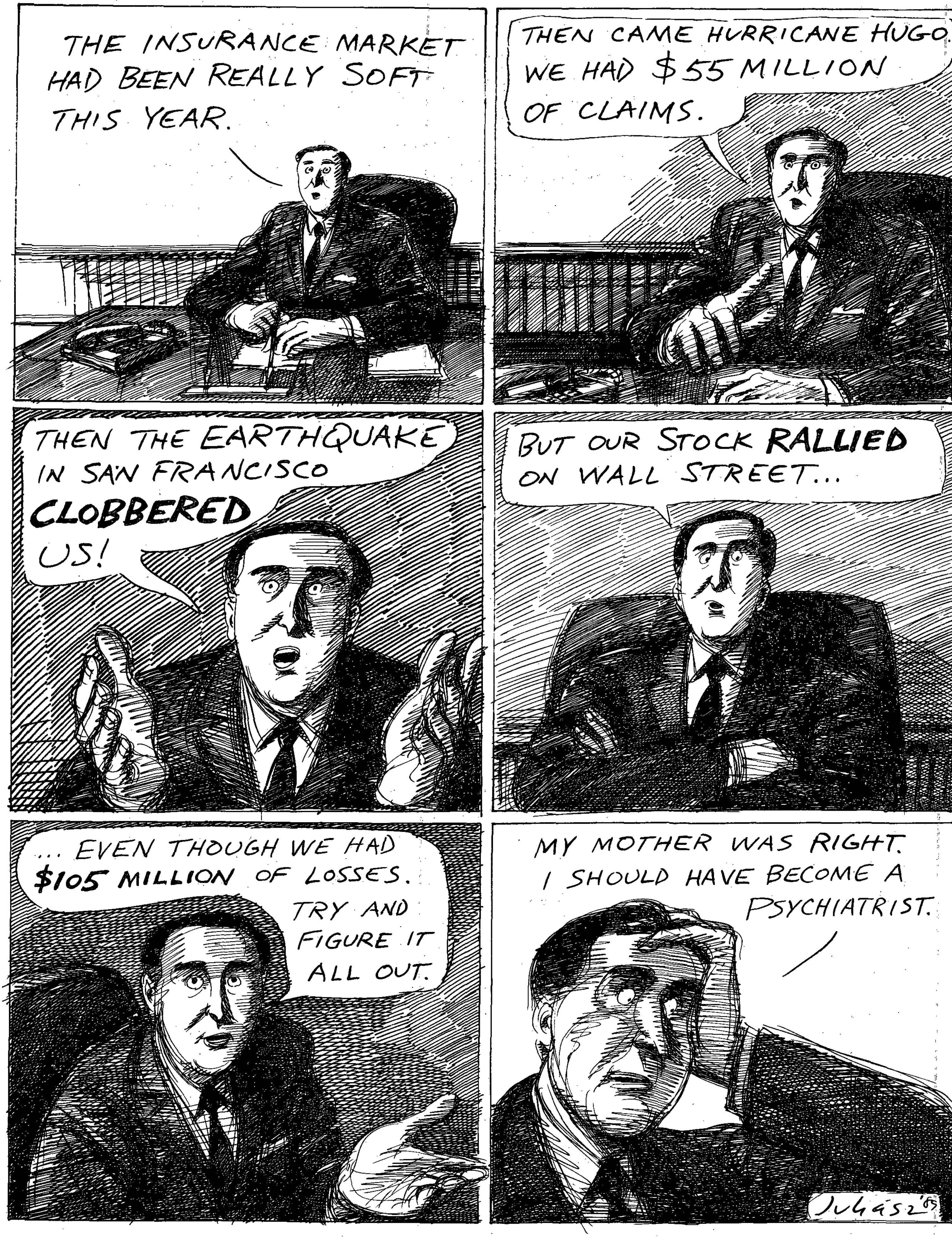
THE INSURANCE MARKET HAD BEEN REALLY SOFT THIS YEAR.
THEN CAME HURRICANE HUGO. WE HAD $55 MILLION OF CLAIMS.
THEN THE EARTHQUAKE IN SAN FRANCISCO CLOBBERED US!
BUT OUR STOCK RALLIED ON WALL STREET...
... EVEN THOUGH WE HAD $105 MILLION OF LOSSES.
TRY AND FIGURE IT ALL OUT.
MY MOTHER WAS RIGHT. I SHOULD HAVE BECOME A PSYCHIATRIST.
JUHASZ '89